

J. Corporate Members of LLCs (G.S. 105-114.1)

Effective January 1, 2002, a corporation that is a member of a limited liability company (LLC) and is entitled to receive at least seventy percent (70%) of the LLC's assets upon dissolution is required to include a percentage of the LLC's income, assets, liabilities, and equity in the corporation's franchise tax calculation. In that case, the corporation's investment in the LLC is not included in the calculation of the corporation's capital stock, surplus and undivided profits base.

Effective January 1, 2003, if a corporation or affiliated group of corporations owns, directly or constructively, seventy percent (70%) or more of the capital interests in an LLC, the corporation or group of corporations must include the same percentage of the LLC's assets in its three franchise tax bases. The attribution to the three bases is equal to the same percentage of (1) the LLC's capital stock, surplus and undivided profits, (2) fifty-five (55%) of the LLC's appraised ad valorem tax value of property, and (3) the LLC's actual investment in tangible property in this State.

Exception – if the total book value of the LLC's assets never exceeds one hundred fifty thousand dollars (\$150,000) during its taxable year, no attribution is required.

Effective January 1, 2005, the ownership percentage that requires an attribution of the LLC's assets is reduced from seventy percent (70%) to fifty percent (50%).

When a partnership, trust, LLC, or other entity is placed between a corporation and an LLC, ownership of the capital interests in an LLC is determined under the constructive ownership rules for partnerships, estates, and trusts in IRC §318(a)(2)(A) and (B), modified as follows:

- The term “capital interest” is substituted for “stock” where that term appears in the referenced Code section.
- An LLC and any non-corporate entity other than a partnership, estate or trust is treated as a partnership.
- The operating rule of section 318(a)(5) applies without regard to section 318(a)(5)(C).

Example: A partnership owns one hundred percent (100%) of the capital interests of an LLC. Corporation A is a fifty percent (50%) owner of the partnership. Corporation A constructively owns fifty percent (50%) of the capital interest in the LLC.

The members of an affiliated group must determine the percentage of the LLC's assets to be included in each member's franchise tax bases. If all members of the group are doing business in North Carolina, then the percentage of the LLC's assets included by each member in its franchise tax bases is equal to the member's percentage ownership in the LLC. If some of the members of the group are not doing business in North Carolina, then the percentage of the LLC's assets owned by the group are allocated among the members that are doing business in North Carolina. The percentage attributed to each member doing business in North Carolina is determined by multiplying the percentage of the LLC owned by the entire group by a fraction. The numerator of the fraction is the percentage of the LLC owned by the member and the denominator is the total percentage of the LLC owned by all members doing business in North Carolina.

Example: An affiliated group of corporations own one hundred percent (100%) of the capital interests in an LLC. The group consists of three corporations. Corporation A is doing business in North Carolina and owns fifty percent (50%) of the LLC. Corporation B is doing business in North Carolina and owns ten percent (10%) of the LLC. Corporation C is not doing business in North Carolina and owns forty percent (40%) of the LLC. The percentage of the LLC's assets required to be included in Corporation A's and Corporation B's franchise tax bases is determined as follows:

$$\text{Corporation A: } 100\% \times 50\% \div (50\% + 10\%) = 83.33\%$$

$$\text{Corporation B: } 100\% \times 10\% \div (50\% + 10\%) = 16.67\%$$

A corporation that is required to include a percentage of the LLC's assets in its franchise tax bases may exclude its investment in the LLC from its computation of the capital stock base.

Shifting assets back and forth between a corporation and an LLC to avoid franchise tax is prohibited. Ownership of the capital interests in an LLC is determined as of the last day of the LLC's taxable year. The attribution of the LLC's assets and the exclusion of the corporation's investment in the LLC are made to the corporation's next following franchise tax return. However, if the corporation and LLC engage in a pattern of transferring assets between them so that each did not own the assets on the last day of its taxable year, the ownership of the capital interest in the LLC must be determined as of the last day of the corporation's taxable year.

Any taxpayer who, because of fraud with intent to evade tax, underpays the tax under this Article (G.S. 105 Article 3) is guilty of a Class H felony in accordance with G.S. 105-236(7). For additional information on the filing requirements for members of LLCs, see Item 5, Subsection M "Corporations Conditionally or Partially Exempt" in this section.