

GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2003

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SENATE BILL 51
House Committee Substitute Favorable 7/10/03

Short Title: Amend Franchise Tax Loophole.

(Public)

Sponsors:

Referred to:

February 17, 2003

A BILL TO BE ENTITLED

AN ACT TO CLOSE A LOOPHOLE THAT ALLOWS CORPORATIONS TO CONTINUE AVOIDING FRANCHISE TAXES AND TO REMOVE PROVISIONS THAT COULD RESULT IN FRANCHISE TAXES ON UNRELATED LIMITED LIABILITY COMPANIES.

The General Assembly of North Carolina enacts:

SECTION 1. G.S. 105-114.1 reads as rewritten:

"§ 105-114.1. Limited liability companies.

(a) Definitions. – The definitions in G.S. 105-130.7A apply in this section. In addition, the following definitions apply in this section:

(1) Affiliated corporations. – Two or more corporations that are includible in the same affiliated group as defined in section 1504 of the Code.

(1b) Governing law. – A limited liability company's governing law is determined under G.S. 57C-6-05 or G.S. 57C-7-01, as applicable.

(2) Owned indirectly. – A person owns indirectly a percentage of the assets of a limited liability company if the limited liability company's governing law provides that ~~seventy percent (70%) or more the percentage~~ of its assets, after payments to creditors, must be distributed upon dissolution to the person as of the last day of the principal corporation's taxable year.

(3) ~~Principal corporation.~~ Qualified limited liability company. – A ~~corporation that is a member of a limited liability company that is not treated as a partnership for federal income tax purposes. or has a related member that is a member of a limited liability company.~~

(b) Controlled Companies. – ~~If Except as provided in subsection (e) of this section, if a corporation owns indirectly, or two or more affiliated corporations a related member of the corporation is a member of a limited liability company and the principal corporation and any related members of the principal corporation together own~~

1 ~~indirectly~~ indirectly, seventy percent (70%) or more of ~~the~~ a qualified limited liability
2 company's assets, then the following provisions apply:

3 (1) A percentage of the qualified limited liability company's income,
4 assets, liabilities, and equity is attributed to ~~that principal~~ each
5 corporation and must be included in the ~~principal~~ corporation's
6 computation of tax under this Article.

7 (2) ~~The principal~~ Each corporation's investment in the qualified limited
8 liability company is not included in the ~~principal~~ corporation's
9 computation of tax under this Article.

10 (3) The ~~attributable~~ percentage attributable under subdivision (1) of this
11 subsection is equal to the percentage of the qualified limited liability
12 company's assets owned indirectly by the ~~principal corporation~~ divided
13 by the percentage of the limited liability company's assets owned
14 indirectly by related members of the principal corporation that are
15 corporations ~~each corporation~~.

16 (b1) Attribution. – For the purpose of applying this section, the following rules
17 apply:

18 (1) Business trusts. – The direct or indirect ownership by a business trust
19 of any qualified limited liability company assets is attributed to the
20 owners of the beneficial interests in the business trust, according to
21 their interests in the trust, and the trust itself is disregarded as a
22 separate entity.

23 (2) Partnerships. – The direct or indirect ownership by a partnership of
24 any qualified limited liability company assets is attributed to the
25 partners according to their interests in the partnership, and the
26 partnership itself is disregarded as a separate entity.

27 (3) Related entities. – The direct or indirect ownership by a noncorporate
28 related entity of a corporation of any qualified limited liability
29 company assets is attributed to the corporation in proportion to the
30 actual aggregate percentage of stock ownership that establishes that the
31 entity is a related entity of the corporation, and the related entity itself
32 is disregarded as a separate entity.

33 (4) No double taxation. – If the same ownership interest is attributed to
34 more than one corporation under this subsection, with the result that
35 the same income, assets, liabilities, or equity must be included in more
36 than one corporation's computation of tax under this Article, those
37 corporations may proportionally reduce the amount included to the
38 extent necessary to avoid double taxation, as prescribed by the
39 Secretary.

40 (c) Other Companies. – In all other cases, none of the limited liability company's
41 income, assets, liabilities, or equity is attributed to a principal corporation under this
42 Article.

1 (d) Penalty. – A taxpayer who, because of fraud with intent to evade tax,
2 underpays the tax under this Article on assets attributable to it under this section is
3 guilty of a Class H felony in accordance with G.S. 105-236(7).

4 (e) Exception. – If a percentage of a qualified limited liability company's assets
5 would otherwise be considered indirectly owned by one or more corporations as a result
6 of attribution from a related entity pursuant to subdivision (b1)(3) of this section, the
7 assets are not considered indirectly owned by the corporation if the corporation can
8 demonstrate that no assets owned by the qualified limited liability company, and no
9 predecessor assets of any assets owned by the qualified limited liability company, have
10 ever been used by the corporation, used in connection with the corporation's business, or
11 owned by the corporation."

12 **SECTION 2.** G.S. 105-130.7A(b)(4) reads as rewritten:

13 "(4) Related entity. – Any of the following:

- 14 a. A stockholder who is an individual, or a member of the
15 stockholder's family enumerated in section 318 of the Code, if
16 the stockholder and the members of the stockholder's family
17 own in the aggregate at least eighty percent (80%) of the value
18 of the taxpayer's outstanding stock.
- 19 b. A stockholder, or a stockholder's partnership, limited liability
20 company, estate, trust, or corporation, if the stockholder and the
21 stockholder's partnerships, limited liability companies, estates,
22 trusts, and corporations own in the aggregate at least fifty
23 percent (50%) of the value of the taxpayer's outstanding
24 stock.~~are component members with respect to the taxpayer.~~
- 25 c. A corporation, or a party related to the corporation in a manner
26 that would require an attribution of stock from the corporation
27 to the party or from the party to the corporation under the
28 attribution rules of section 318 of the Code, if the taxpayer
29 owns at least eighty percent (80%) of the value of the
30 corporation's outstanding stock."

31 **SECTION 3.** This act becomes effective January 1, 2004, and applies to
32 taxes due on or after that date.