MICROFILM DIVIDER

OMB/RECORDS MANAGEMENT DIVISION
SFN 2053 (2/85) 5M

ROLL NUMBER

DESCRIPTION

1471

2003 HOUSE FINANCE AND TAXATION

HB 1471

2003 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. **HB 1471**

House Finance and Taxation Committee

❑ Conference Committee

Hearing Date January 29, 2003

Tape Number	Side A	Side B	Meter #
1	X		21.5
Committee Clerk Signature	Janice Stein		

Minutes:

REP. WESLEY BELTER, CHAIRMAN Called the hearing to order.

REP. AL CARLSON, DIST. 41 Introduced the bill. He presented amendments to the bill. Because of miscommunication, the legislative council drafted the bill as a flat tax, it was not meant to be a flat tax, it was meant to bracket it, except with different rates. Summary of the testimony is with the amendments added. See attached summary. This bill deals with addressing corporate income tax. He felt the perception of North Dakota is that it is a high tax state. The main objective of this bill is to get us to a real rate.

JILL DENNING, GENERAL MANAGER OF BHG, INC. Testified in opposition of the bill. See attached written testimony.

REP. KLEIN How much would you have to raise the price of the paper, if we pass this bill?

JILL DENNING A couple of years ago, we raised the price of our news stand copies of fifty cents to seventy five cents, we were scared. Businesses cut back on their ads.

REP. HEADLAND Do you have any idea how long newspapers have been exempt in this state?

JILL DENNING I don't know.

ROGER BAILEY, EXECUTIVE DIRECTOR OF THE NORTH DAKOTA NEWSPAPER ASSOCIATION Testified in opposition of the bill. See written testimony.

REP. KELSH Do you know how many other states have newspaper exemptions?

ROGER BAILEY I don't know, there are some that have the tax, but they are in the minority.

REP. BELTER Is there some disagreement in your organization on this issue?

ROGER BAILEY I know that issue was explored by the forum editorily, and I believe they are with us on this opposition to the bill.

REP. KLEIN On your testimony you say a sales tax of $21,528, is that yearly?

ROGER BAILEY That is an annual figure.

REP. WEILER Referred to middle of testimony, to absorb the tax an increase will not be possible, will you explain why it wouldn't be possible, to add a nickle onto the price of the newspaper?

ROGER BAILEY It could be possible, but in many cases, such as the situation with vending machines, the overall average price of newspapers now is about fifty cents. Vending machines only work in increments of twenty five cents, if the sales tax is added onto an individual copy, we are either looking at going up a whole lot, so that the individual copy would be seventy five cents, the consumer would pick that up. In many cases, if we are only adding three or four cents of sales tax on to it, the newspaper is not going to invest in new machines to take care of that.

REP. WEILER If it is fifty cents in the vending machine and you get charged an extra three or four cents, but you bump it up to seventy five cents, you are kind of coming out pretty good on that, unfortunately, the consumer gets hurt, but overall the income for the newspaper, is substantially increased.

ROGER BAILEY After having gone through this experience personally, an increase in advertising and subscription, each time it happens, you see a decrease in single copy sales.

REP. WEILER What is the percentage of vending machine sales versus delivery to homes?

ROGER BAILEY I can speak from my own experience as publisher of a newspaper in Rolla, about half of our newspapers were sold through individual copy and half through subscription. That is probably average throughout North Dakota.

DAVE BUNDY, EDITOR OF THE BISMARCK TRIBUNE Testified in opposition of the bill. See written testimony.

REP. CLARK Has your paper ever published an editorial talking about how you integrate income tax?

DAVE BUNDY I would have to say, there is a strong likelyhood, that we have come out in favor of some kind of tax levy at one point or another. I don't have the facts in front of me right now.

REP. CLARK Don't you find your position a little schizophrenic then, talking about not wanting to pay taxes?

DAVE BUNDY Actually, I was pointing out on the first bullet item, we do not have a problem at all with paying our fair share of the tax, it is just how it applies to newspapers.

REP. WEILER You said your problem is singling out newspapers, if we put amendments on to add four or five others, would you be O.K. with adding newspapers?

DAVE BUNDY I think there are other bills that address reduction of a corporate income tax that are more palatable to us. I don't know what the four or five things are you might be thinking of, but if they were things that were able to contribute enough of a portion to reduce the corporate income tax, so that we weren't entirely responsible for it, I think that is something we would be much less opposed to.

JACK MCDONALD, NORTH DAKOTA NEWSPAPER ASSOCIATION Testified in opposition of the bill. See written testimony plus a copy of a Supreme Court ruling.

MARY LOFTSGARD, SUPERVISOR OF THE CORPORATE INCOME TAX SECTION OF THE STATE TAX DEPARTMENT. Appeared in a neutral position. Added comments to Rep. Carlson's testimony. Submitted a form 40 of the corporate income tax return. Referred to the income tax return relating to areas which could be deleted. She explained what water's edge filing was, and who used that type of filing. Companies who use the water's edge filing do not get the tax exemption. She also submitted a North Dakota Domestic Disclosure Spreadsheet form for committee members. See attached copy.

REP. BELTER Are all the rules the same in all states regarding the water's edge?

MARY LOFTSGARD No they are not.

REP. BELTER A deletion of the sales tax to newspapers would have a 1.4 million dollars fiscal note?

MARY LOFTSGARD Yes

REP. BELTER You mentioned in your earlier comments regarding the bank portion of it, do we need to amend this bill then?

MARY LOFTSGARD No, that is already in the bill.

REP. FROELICH If we break it out, instead of taxing both the newspapers and the ink, where would we be in income?

REP. BELTER Stated we have to get that information.

REP. GROSZ What would happen if someone was in the second year of the water's edge, then this bill passed, would they still be able to go through the five years, or would it be gone?

MARY LOFTSGARD It would be gone.

REP. KLEIN Asked for examples of the water's edge.

MARY LOFTSGARD She stated she couldn't divulge information as to what corporations were in the water's edge. She stated, these would tend to be large companies who extract national resources and process them. Generally, they are large multi national companies that operate world-wide.

REP. BELTER, TO MILES VOSBERG Asked if they have a break down in the newspaper situation of the sales tax of the sale of the paper, but there is also the sales tax on the ink and print of the paper?

MILES VOSBERG Stated they didn't have a break-down of those two items, the newspaper association testified that the tax on the newspaper would be about $750,000, so the remaining 4.1 million increase in tax revenue, would be on the sale of the newspaper.

REF. GROSZ I believe they were receiving one million dollars more by the elimination of the water's edge, so do we take one off of 4.1 million, should it be only 3.1 from the newspapers?

MILES VOSBERG There is a net loss of revenue of 4.1 million in the corporate income tax changes. About one million dollars is raised from the change in the water's edge, but there is still an overall net loss of corporate tax revenue of 4.1 million. The sales tax revenue between the tax on the sale of newspapers and the tax on the newspaper and ink, would be an increase in tax revenue of 4.1, to make it revenue neutral.

REP. KELSH The state of Minnesota was toying with eliminating the exemption on newspaper, did that ever come to pass?

MILES VOSBERG I am not sure, I could check on that.

REP. CARLSON Commented again, if you just took away the water's edge, and you took away the federal deductibility, the rate would be 7.6 percent. You have to use that as your benchmark. The only reason that rate went to 7.2 and down to 2.1, is because we took the revenue from taking the exemption off of newspapers, to lower the rate. If you want to further lower the rates, you do that by taking an exemption away, and that further lowers the corporate income tax. That would represent North Dakota's rate.

With no further testimony, the hearing was closed.

COMMITTEE ACTION 2-3-03, Tape #1, Side B, Meter #5.7

REP. BELTER Presented amendments to the committee, 30645.0103, which will take the newspapers out completely, but still makes the bill revenue neutral.

REP. GROSZ Made a motion to adopt the amendments as presented.

REP. DROVDAL Second the motion. Motion carried by voice vote, with one no vote.

REP. GROSZ Made a motion for a **DO PASS AS AMENDED**

REP. HEADLAND Second the motion. **MOTION CARRIED**

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Page 7
House Finance and Taxation Committee
Bill/Resolution Number HB 1471
Hearing Date January 1-29-03

COMMITTEE ACTION Cont'd. 2-3-03

8 yes 5 no 1 absent

REP. GROSZ Was given the floor assignment.

FISCAL NOTE
Requested by Legislative Council
03/27/2003

Amendment to: HB 1471

1A. **State fiscal effect:** *Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.*

	2001-2003 Biennium		2003-2005 Biennium		2005-2007 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues			($544,000)			
Expenditures						
Appropriations						

1B. **County, city, and school district fiscal effect:** *Identify the fiscal effect on the appropriate political subdivision.*

2001-2003 Biennium			2003-2005 Biennium			2005-2007 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

2. **Narrative:** *Identify the aspects of the measure which cause fiscal impact and include any comments relevant to your analysis.*

Engrossed HB 1471 with Senate amendments changes the corporation income tax structure by repealing the federal tax deduction, repealing net operating loss carryback provisions, and imposing five tax rates ranging from 2.6% to 7.0% of taxable income. The Senate amendments continue to allow the Water's Edge election at rates approximately equal to current law. Engrossed HB 1471 with Senate amendments is expected to reduce state general fund revenues by $544,000 in the 2003-05 biennium.

3. **State fiscal effect detail:** *For information shown under state fiscal effect in 1A, please:*
   A. **Revenues:** *Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.*

   B. **Expenditures:** *Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.*

   C. **Appropriations:** *Explain the appropriation amounts. Provide detail, when appropriate, of the effect on the biennial appropriation for each agency and fund affected and any amounts included in the executive budget. Indicate the relationship between the amounts shown for expenditures and appropriations.*

Name:	Kathryn L. Strombeck	**Agency:**	Tax Department
Phone Number:	328-3402	**Date Prepared:**	03/28/2003

FISCAL NOTE

Requested by Legislative Council
02/05/2003

Amendment to: HB 1471

1A. **State fiscal effect:** *Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.*

	2001-2003 Biennium		2003-2005 Biennium		2005-2007 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

1B. **County, city, and school district fiscal effect:** *Identify the fiscal effect on the appropriate political subdivision.*

2001-2003 Biennium			2003-2005 Biennium			2005-2007 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

2. **Narrative:** *Identify the aspects of the measure which cause fiscal impact and include any comments relevant to your analysis.*

Engrossed HB 1471 changes the corporation income tax structure by repealing the federal tax deduction, repealing the water's edge optional filing method, and imposing tax rates ranging from 2.2% to 7.5% of taxable income. Engrossed HB 1471 is expected to be approximately revenue neutral.

3. **State fiscal effect detail:** *For information shown under state fiscal effect in 1A, please:*
   A. **Revenues:** *Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.*

   B. **Expenditures:** *Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.*

   C. **Appropriations:** *Explain the appropriation amounts. Provide detail, when appropriate, of the effect on the biennial appropriation for each agency and fund affected and any amounts included in the executive budget. Indicate the relationship between the amounts shown for expenditures and appropriations.*

Name:	Kathryn L. Strombeck	**Agency:**	Tax Dept.
Phone Number:	328-3402	**Date Prepared:**	02/05/2003

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FISCAL NOTE
Requested by Legislative Council
01/21/2003

Bill/Resolution No.: HB 1471

1A. **State fiscal effect:** *Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.*

	2001-2003 Biennium		2003-2005 Biennium		2005-2007 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

1B. **County, city, and school district fiscal effect:** *Identify the fiscal effect on the appropriate political subdivision.*

2001-2003 Biennium			2003-2005 Biennium			2005-2007 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

2. **Narrative:** *Identify the aspects of the measure which cause fiscal impact and include any comments relevant to your analysis.*

HB 1471 changes the corporation income tax structure by repealing the federal tax deduction, repealing the water's edge optional filing method, and imposing a flat tax rate of 6.73%. This is expected to reduce revenues by an estimated $4.1 million per biennium. The bill also eliminates the sales tax exemption for newspapers and magazine subscriptions, which is expected to increase revenues by $4.1 million per biennium. Overall, with the exception of some possible timing differences, the provisions of HB 1471 are expected to be approximately revenue neutral.

3. **State fiscal effect detail:** *For information shown under state fiscal effect in 1A, please:*
   A. **Revenues:** *Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.*

   B. **Expenditures:** *Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.*

   C. **Appropriations:** *Explain the appropriation amounts. Provide detail, when appropriate, of the effect on the biennial appropriation for each agency and fund affected and any amounts included in the executive budget. Indicate the relationship between the amounts shown for expenditures and appropriations.*

Name:	Kathryn L. Strombeck	**Agency:**	Tax Dept.
Phone Number:	328-3402	**Date Prepared:**	01/28/2003

Date: 2-3-03
Roll Call Vote #: 1

2003 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. HB 1471

House FINANCE & TAXATION Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number 30645.0103

Action Taken Do Pass as amended

Motion Made By Rep. Grosz Seconded By Rep. Headland

Representatives	Yes	No	Representatives	Yes	No
BELTER, CHAIRMAN	✓				
DROVDAL, VICE-CHAIR	✓				
CLARK		✓			
FROELICH		✓			
GROSZ	✓				
HEADLAND	✓				
IVERSON		✓			
KELSH	A				
KLEIN		✓			
NICHOLAS	✓				
SCHMIDT		✓			
WEILER	✓				
WIKENHEISER	✓				
WINRICH	✓				

Total (Yes) 8 No 5

Absent 1

Floor Assignment Rep. Grosz

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

HB 1471: Finance and Taxation Committee (Rep. Belter, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (8 YEAS, 5 NAYS, 1 ABSENT AND NOT VOTING). HB 1471 was placed on the Sixth order on the calendar.

Page 1, line 2, after the first comma insert "and" and remove ", subsection 9 of section 57-39.2-01, and"

Page 1, line 3, remove "subsections 5 and 8 of section 57-40.2-01"

Page 1, line 4, after the second comma insert "and"

Page 1, line 5, remove ", and the sales and use tax application to newspapers and"

Page 1, line 6, remove "magazines" and remove ", subsection 16 of section 57-39.2-04, and subsection 6 of"

Page 1, line 7, remove "section 57-40.2-04"

Page 1, line 8, remove "and the sales tax exemption for newsprint and ink used in"

Page 1, line 9, remove "publication of a newspaper"

Page 6, replace lines 16 through 28 with:

"1. a. For the first three thousand dollars of taxable income, at the rate of ~~three~~ <u>two and two-tenths</u> percent.

b. On all taxable income above three thousand dollars and not in excess of eight thousand dollars, at the rate of ~~four and one-half~~ <u>three and two-tenths</u> percent.

c. On all taxable income above eight thousand dollars and not in excess of twenty thousand dollars, at the rate of ~~six~~ <u>four and three-tenths</u> percent.

d. On all taxable income above twenty thousand dollars, and not in excess of thirty thousand dollars, at the rate of ~~seven~~<u>five</u> and ~~one-half~~ <u>four-tenths</u> percent.

e. On all taxable income above thirty thousand dollars, and not in excess of fifty thousand dollars, at the rate of ~~nine~~ <u>six and five-tenths</u> percent.

f. On all taxable income above fifty thousand dollars, at the rate of ~~ten~~ <u>seven</u> and ~~one-half~~ <u>five-tenths</u> percent."

Page 7, remove lines 3 through 31

Page 8, remove lines 1 through 24

Page 8, line 25, remove ", subsection 16 of section 57-39.2-04, and"

Page 8, line 26, remove "subsection 6 of section 57-40.2-04" and replace "are" with "is"

IR

REPORT OF STANDING COMMITTEE (410)
February 4, 2003 9:47 a.m.

Module No: HR-21-1590
Carrier: Grosz
Insert LC: 30645.0103 Title: .0200

Page 8, line 27, replace "Sections 1 through 3 of this" with "This" and replace "and the repeal of" with "is"

Page 8, line 28, remove "chapter 57-38.4 are" and remove "Sections 4"

Page 8, remove lines 29 and 30

Renumber accordingly

2003 SENATE FINANCE AND TAXATION

HB 1471

2003 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB1471

Senate Finance and Taxation Committee

☐ Conference Committee

Hearing Date March 5, 2003

Tape Number	Side A	Side B	Meter #
1	X		3464-end
1		X	1-2600
Committee Clerk Signature			

Minutes:

Senator Urlacher opened the hearing HB1471. All committee members are present. This bill relates to financial institutions taxes, the corporate income tax deduction for federal income taxes paid, and corporate income tax rates.

Representative Al Carlson (mtr #3481) - Introduced the bill as it came from the House. Explained the intent of the bill. This bill does several things. Reviewed the sections of the bill and the effect it has on financial institutions, on state tax rates, and the repeal of the waters edge filing status. Would also consider grandfathering the users of the waters edge filing status. Talked about the total tax structure of the state and the competitiveness of the state tax rates. Does not believe the state should eliminate the corporate tax without eliminating the personal income tax. The bill sits before the committee with rates higher that he feels there should be.

Senator Nichols (mtr #4623) - Regarding the waters edge filing status, do you feel that we should do away with it over a period of time?

Representative Carlson (mtr #4666) - As the issue has been studied, when companies move their labor offshore and pay labor offshore and use that as a deduction, it is a complicated issue. Do feel that if a company elected that filing status for the five year period, they should be able to finish that period.

Senator Syverson (mtr #4807) - Could you describe the rational of using six different brackets.

Representative Carlson (mtr #4840) - Believes the brackets reflect what we have today, we just changed the rates within the brackets.

Ron Rauschenberger, Governor's Office (mtr #5038) - Like to concept of decoupling from federal taxes. Look forward to ongoing work on this bill to find a fair and equitable way to work this out.

Dale Anderson, President, GNDA (mtr #5189) - Testified in opposition to HB1471. Opposed due to business communities concerns with this bill. GNDA works on components for economic development, new business startups, business expansion within ND, and business expansion attraction from outside ND. The following amendments would be necessary for GNDA to support the bill. 1. Maintain waters edge filing status. 2. Improve corporate tax perception by lowering corporate tax rate by eliminating the federal income tax deduction for corps. 3. Accomplish 1 and 2 without a tax increase. 4. Publich the effective corporate income tax rate. GNDA offers its experience to work out a solution to HB1471. Written testimony is attached. Urges a do not pass as it is.

Tape 1, Side B

Senator Tollefson (mtr #1) - Dwelling on perception, is that over stressed or unfair?

Mr. Anderson (mtr #20) - Feels the real rate has to be marketed. The feedback received by GNDA is that site selectors look at certain cuts and we miss out because of our corporate income tax rates. The effective rate should be marketed.

Senator Nichols (mtr #113) - Regarding the waters edge provision, do you feel that should be continued or phased out?

Mr. Anderson (mtr #158) - Gave information on the federal issues with the waters edge filing status along with state issues. Feels that if waters edge is important at a federal level, the state should support as well. By eliminating waters edge we would be cutting off one element.

Senator Tollefson (mtr #263) - Clarifies that it would be a negative for North Dakota if eliminated.

Mr. Anderson (mtr #279) - Doesn't have the information right now. Would have to get that information.

Senator Tollefson (mtr #312) - To clarify, ND would be less attractive?

Mr. Anderson (mtr #333) - Not aware of any other state that has repealed waters edge.

Dennis Boyd, MDU Resources (mtr #380) - Testified in opposition to HB1471. Concerned about unequal consequences by repealing and changing rates. Would like to see the retention of the waters edge filing status. Feels the idea of fixing a perception is dubious. Had supported the Senate bill because it made a bold statement. Further testimony included the tax situation of MDU Resources and the taxes paid by the corporation. Agrees with the comments of Mr. Anderson.

Ron Ness, ND Petroleum Council (mtr #717) - Testified in opposition to HB1471 in its present form. We would like to see the effective rate become the actual rate. Agrees with the comments made by MDU Resources and GNDA. Feels the repeal of the waters edge filing status would be negative. Would like to see keeping the effect tax rate and retaining the waters edge filing status.

Rick Clayburgh, State Tax Commissioner (mtr #945) - Supports the concept of HB1471. Perception is an important issue. Has written several letters to business journals with an explanation of our tax rate structure. This bill as amended does create winners and losers. Regarding the waters edge status, doesn't feel that would be a big issue for the state. At this time the Federal government is concerned with waters edge and is reviewing that status. At this time we would be the only state not allowing waters edge. Continued testimony on his perception of the bill and the effect it would have. Feels it would be a disservice if the bill is defeated.

Senator Nichols (mtr #1318) - Regarding Mr. Clayburgh's comment about the federal review of the waters edge filing status. All states do not have this provision?

Mr. Clayburgh (mtr #1342) - Every state that participates in the unitary combined reporting, do recognize the waters edge status.

Senator Seymour (mtr #1456) - Have you looked at the cash flow comparing the current situation vs. if the bill is passed.

Mr. Clayburgh (mtr #1487) - Believes maintaining the status quo, we have wonderful things in this state that we continue to sell and work towards. We have a lot of tools in Commerce Department and Economic Development, a lot of programs in place working to reach out and bring businesses here. I feel strongly about this issue due to dealing with impediments that we don't have to have. It is a perception issue. Gave additional information on the ability of the Tax Department to project results. Can only use actual information on hand, can not use blue sky projections.

Senator Urlacher (mtr #1728) - Given no further testimony, closed the hearing on HB1471.

Senator Urlacher (mtr #1905) - Could establish a sub committee to work with the entities interested in the outcome or continue on as a full committee. Would like to appoint a sub committee to pull everyone together. Would like a consensus of involved parties.

Senator Tollefson (mtr #2067) - Supports the idea of a sub committee. Is there a way to correct the perception without eroding existing situation.

Senator Urlacher (mtr #2190) - We need to identify the depth of the concern out there.

Senator Wardner (mtr #2233) - Testifying on another bill. When he returned, question was the waters edge the main objection to the bill? Or were there other things in the bill they didn't like.

Senator Urlacher (mtr #2263) - Other things in the bill, shifting, offsetting of lost revenue, perception and waters edge was part of it. Mr. Anderson covered a broad area of concerns. Appointed sub committee members: Senator Nichols, Senator Tollefson, Senator Wardner with Senator Wardner as the Chairman.

Senator Tollefson (mtr #2403) - There was discussion on the objection to SB2374. The Commerce Department has not appeared at all. Feels they should address this issue.

Senator Urlacher (mtr #2455) - Agrees, the sub committee should call the Commerce Department for testimony.

Senator Wardner (mtr #2473) - Agrees with Senator Tollefson. Will schedule a subcommittee meeting.

Senator Urlacher - Adjourned the meeting.

2003 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB1471

Senate Finance and Taxation Committee

☐ Conference Committee

Hearing Date March 10, 2003

Tape Number	Side A	Side B	Meter #
1		X	176-4220
Committee Clerk Signature Mary Kay Wolny			

Minutes:

Sub committee Chairman Wardner called the meeting to order. Senator Wardner, Senator Tollefson and Senator Nichols are present. Are hearing input today to clarify some of the issues in the bill.

Ron Rauschenberger, Governor's Office (mtr #176) - Testified on the marketing aspects of the bill. The Governor feels it is important to remove the federal deduction from the corporate tax structure. The Department of Commerce, in working with Eide Bailly to do a study on taxes, received a memorandum that included the statement "the overall tax rates for each state varied from 0% for SD to 12% for Iowa, ND has the second highest rate at 10.5%". This is a company from ND, this information has since been corrected. Gives an idea of what kind of problems we run into. Want to get the tax rate down to the 6.9-7% level, has to happen fairly and equitably. Feels this is extremely important to the state.

Senator Wardner (mtr #489) - In your opinion, are there companies that take ND out of the mix when looking at locations before talking to us?

Mr. Rauschenberger (mtr #513) - Yes, I do. That happens in the site selector process.

Senator Wardner (mtr #568) - Rate listed in the bill is 7.5% for a top rate. Will that help?

Mr. Rauschenberger (mtr #587) - 7.5% would make a difference, but we feel it is important to get the tax rate lower than that.

Senator Tollefson (mtr #613) - If a greater effort was placed on the net corporate taxes, would that help?

Mr. Rauschenberger (mtr #658) - Have tried, there are 100's of companies that rate states. Usually end up looking at that 10.5%, part of that is the Water's Edge. Getting rid of the perception is hard.

Senator Tollefson (mtr #734) - If the bill passes and the perception is fixed, there has to be a tax shift.

Mr. Rauschenberger (mtr #771) - Working with Representative Carlson and the Tax Department and other entities to find a way to get fewer winners and losers.

Lee Peterson, Department of Commerce (mtr #835) - Testified regarding this bill. Written testimony is attached. Also referenced the booklet "ND Delivers Growth and Prosperity" (exhibit A). Testified as to the difficulty in explaining our corporate tax structure to site selectors. Dept of Commerce has three important areas they work on. The first and second deal with new business in ND and expanding existing businesses in ND, both are accustomed to the ND tax structure and it is not a problem explaining. The third area worked on is recruiting new industries to the state. This is the problem area, ND is often if not always misrepresented in the area of corporate income tax. Stated that ND does have a favorable tax climate, is just misrepresented. Written testimony is attached.

Senator Nichols (mtr #1460) - Regarding the site selectors, when seriously looking at locations, will they take the time and use accountants to get a true picture?

Mr. Peterson (mtr #1530) - In the initial overview of looking at states in the Midwest, we are often chucked. Easier to understand that South Dakota has no corporate income tax, than to try to understand what North Dakota's rate is. Again, dealing with perception not reality. North Dakota's tax climate is very favorable, we even have an edge over South Dakota in reality. We have a problem with perception. Would like a tax structure that can be easily explained.

Senator Wardner (mtr #1738) - Referenced information on state taxes and the federal deduction. ND is one of only four states that allow.

Senator Tollefson (mtr #1795) - Reference page two of written testimony, "effective rate" is actually around 6.83% assuming a 25% effective federal tax rate. Those are statements that are difficult to understand.

Mr. Peterson (mtr #1843) - This is an effort to try to explain our tax structure to companies that may come to our state. Is our effort to try to explain where a corporation could be in the taxing system in ND.

Senator Tollefson (mtr #1899) - In reference to the booklet, could the effective rate be listed?

Mr. Peterson (mtr #1934) - The effective rate is not the same for everyone, we can't give an actual rate.

Senator Wardner (mtr #1982) - Question regarding confidentiality. Is that a big issue?

Mr. Peterson (mtr #2022) - Correct, confidentiality is a big issue. If people know a company is looking for a site, every state will send an offer. May also have employee changes when an expansion occurs, they don't what their employees to start looking for work elsewhere. Many confidentiality issues. Companies will almost always do the initial look on their own. We will never have the opportunity to talk to them and will never know if they looked at ND. We need so desperately a rate that works.

Senator Wardner (mtr #2192) - What if the corporate tax rate is at 7.5%. Would that help?

Mr. Peterson (mtr #2210) - Yes, very much. Would be the biggest help in marketing ND that we ever had.

Senator Nichols (mtr #2348) - If we get rid of the federal tax exemption and reduce to whatever is agreeable, what happens with regard to Water's Edge?

Mr. Peterson (mtr #2386) - That is a tax question, not an economic development question. Water's Edge is a bigger issue. ND's tax needs to be quickly and easily explainable. Three out of five rating agencies list ND's corporate income tax as 10.5% and there are 100's of rating agencies.

Senator Wardner (mtr #2598) - Question about Water's Edge, is it in or out of this particular piece of legislation.

Rick Clayburgh, State Tax Commissioner (mtr #2656) - That is up to the committee. The two issues are separate. Gave detailed explanation of the elimination of the federal income tax deduction and the Water's Edge filing option.

Senator Tollefson (mtr #2813) - How many corporations use the Water's Edge option?

Mr. Clayburgh (mtr #2823) - Currently have 250 corporations using the Water's Edge filing method.

Dennis Boyd, MDU Resources Group (mtr #2896) - MDU is one of ND's oldest and largest companies. One of the largest corporate income tax payers in the state. Any effective rate above 6.5% is a tax increase to MDU. Concerned that MDU has projected no growth in customers through 2022. Due to territorial integrity act, MDU can not grow the electric business. REC's pay no tax and are the only electric company growing. We will not be substantial benefactors of new business due to growth because of a better tax climate. Gave examples of many businesses that were customers of MDU but are now customers of Capital Electric because of moving to the north part of town.

Senator Wardner (mtr #3469) - At 7.5% and losing the federal tax deduction, your tax?

Mr. Boyd (mtr #3485) - Means a substantial tax increase that will cost MDU approximately $140,000 to $150,000 annually.

Mr. Clayburgh (mtr #3544) - Addressed the committee on only rates. Structure is not out to get anyone to pay additional tax. Gave a detailed explanation of the corporate rate structure, states that are currently growing, and states that are in recession. Changing the perception would be tremendous for ND. Would be a positive move for ND.

Senator Nichols (mtr #3925) - Regarding the differences in businesses with a federal tax deduction that they may have. Only way to avoid negative hits from this bill is to accept a fiscal reduction?

Mr. Clayburgh (mtr #3998) - The rate to take it to 7.6 or 7.5 as the bill stands before you, anytime there is a tax change, will always create a winner and loser situation. Should try to keep this as revenue neutral as possible.

Senator Wardner (mtr #4220) - Recess subcommittee meeting on HB1471.

2003 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB1471

Senate Finance and Taxation Committee

☐ Conference Committee

Hearing Date March 11, 2003

Tape Number	Side A	Side B	Meter #
1		B	435-4390
Committee Clerk Signature			

Minutes:

Sub committee Chairman Wardner called the sub committee to order. Members present are Senator Wardner, Senator Tollefson and Senator Nichols.

Senator Wardner (mtr #445) - Will extend taking testimony from yesterday that dealt with perception.

Jim Melland, Grand Forks Region Economic Development Corporation (mtr #464) - Gave testimony dealing specifically with the perception of corporate income taxes on a national level. Talked about the nature of attracting business to ND and some of the issues prospective businesses look at. Medium sized corporations go through a group a consultants we refer to as site selectors, two of the largest site selectors in the nation, have personally visited with the people in those companies that deal with the kind of industries that ND targets. Here is the issue we face with the income tax problem in our state. These corporate site selectors use filters, when they are looking for a location, they do not contact the locations, they use filter, they go through data bases and look at census information, unemployment rates, population in different regions of the state, and they use guidelines they have received from the company they are working for. One of the filters is corporate taxes. Because of confidentiality issues, we never know if we are being looked at. We may be the best in all other areas but the10.5% corporate tax rate will knock us out. Large corporations do the same thing, they just do it in house. They use the same filtering system that site selecting consultant companies use. Also true that most economic growth comes from within the state. Urges finding and equitable way to not hurt one business sector more than another while decoupling the federal exemption.

Donnita Wald, State Tax Department (mtr #815) - Are neutral on the issue. Gave background on the Waters Edge filing method. Written testimony is attached. Testimony included a talking point on Waters Edge, the history of Waters Edge, and how it works for companies and gave examples.

Senator Tollefson (mtr #1322) - Question, is there action in Congress that will change the Waters Edge filing method?

Ms. Wald (mtr #1335) - The federal government is looking at how states utilize world wide combined reporting and the issues that have arisen. Not really looking at repealing, just looking at parts of it. There has been a steady increase in ND Waters Edge filers. Also referenced a list of issues to consider with this bill. See five bullet points on page three of the written testimony.

Senator Wardner (mtr #1621) - Clarified that there would be a large negative fiscal effect if the federal deduction is removed and the Waters Edge status is left in place.

Ms. Wald (mtr #1642) - That is correct. As the statistics show there will be a continuing increase in Waters Edge filers.

Senator Wardner (mtr #1717) - Clarified that states that do not have the Waters Edge option are struggling with their lack of revenue.

Ms. Wald (mtr #1728) - Talked about the issue of grandfathering in of the Waters Edge option. Referenced information on page three of the written testimony. Showed the number of tax payers that would be effected each year. Other option available, could do what Alaska does. Allow Waters Edge for oil companies only.

Senator Wardner (mtr #1845) - Allowed for oil companies only, no one else?

Ms. Wald (mtr #1850) - That is correct.

Senator Nichols (mtr #1964) - Regarding the steady increase of Waters Edge filers, are they new companies or existing companies shifting.

Ms. Wald (mtr #1994) - Looks like it is shifting. Top seven filers where here prior to the adoption to the Waters Edge option.

Senator Nichols (mtr #2030) - When working with those returns, do you feel confident that your getting good information?

Ms. Wald - Will defer to Mary Loftsgard to answer that question.

Mary Loftsgard, Supervisor of Corporate Income Tax Collection, State Tax Department (mtr #2097) - In response to Senator Nichols question, have greater information from Waters Edge filers than companies that file the World Wide Report. Gave more information regarding the amount of information Waters Edge filers need to provide.

Senator Tollefson (mtr #2251) -Regarding the international economy of today, would you anticipate more companies selecting Water Edge?

Ms. Loftsgard (mtr #2317) - In regards to question, yes, good likelihood that more companies will chose Waters Edge. Referred to examples attached to the written testimony. Went over the two different examples using the World Wide filing method and the Waters Edge filing method. Showing the taxes that would be paid in each situation. Also gave information on how ND actually gets taxes from these corporations.

Senator Wardner (mtr #3353) - Restated that if Waters Edge is elected it is for five years, if the taxes paid are more in that five years because of the Waters Edge option, the company has to stay with that option, can not jump out.

Ms. Loftsgard (mtr #3392) - That is correct, companies need to plan and look ahead.

Senator Wardner (mtr #3435) - Clarified that companies elect the option for five years and when that is up, will have to reassess for the next five years.

Dale Anderson, President GNDA (mtr #3555) - Gave additional comments on HB1471 in regards to the Waters Edge filing method. Handed out written testimony that included a section on Corporate Income Tax Policy: Water's Edge Election with six bullet points. Reviewed those bullet points. Written testimony is attached. Urges a do not pass until the Water's Edge issue has been resolved.

Senator Tollefson (mtr #4180) - Asked a question in regards to an international economy and the internet. Is the Internet going to be a part of this issue?

Mr. Anderson (mtr #4279) - Is a real possibility, want to ensure the best business climate for when changes do happen.

Senator Wardner (mtr #4320) - Given no further testimony or clarification of issues, recessed the sub committee on HB1471.

2003 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB1471

Senate Finance and Taxation Committee

❑ Conference Committee

Hearing Date March 17, 2003

Tape Number	Side A	Side B	Meter #
1		B	930-1360
Committee Clerk Signature			

Minutes:

Senator Urlacher opened the discussion on HB1471. All committee members are present. This bill relates to the corporate income tax deduction for federal income taxes paid and corporate income tax rates.

Senator Wardner (mtr #940) - The sponsor of the bill and the Tax Department were going to bring down one more proposal. The issue at this time is the Water's Edge election, which is $500,000 to the state. Many corporations in the state are interested in and are taking the Water's Edge election. Early on no one said much about the Water's Edge election, but the accountants are coming forward and saying be careful. Other issue is the giving up of the federal tax deduction for corporations to bring down the percent of the top rate. Most concerned with the top rate and bringing that down. But when you do that, some companies are going to pay more taxes. Would have to drop down to approximately 7.1%, and if do that, have a negative fiscal note and the state has to pick up the bill. Should be able to address the bill on Wednesday.

TP

Senator Tollefson (mtr #1241) - Just a statement, what is the value of perception. Is tough to pin down.

Senator Wardner (mtr #1315) - Agrees with Senator Tollefson, what are we willing to pay for perception?

Senator Urlacher (mtr #1335) - Closed the discussion on HB1471. Adjourned the meeting.

March 19, 2003 Tape 1, Side A

Senator Urlacher (mtr #4065) - Will address next week on Monday or Tuesday.

2003 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB1471

Senate Finance and Taxation Committee

☐ Conference Committee

Hearing Date March 24, 2003

Tape Number	Side A	Side B	Meter #
1	X		15-2715
Committee Clerk Signature			

Minutes:

Subcommittee Chairman Wardner called the meeting to order. Let the record show that members Senator Wardner, Senator Tollefson and Senator Nichols are present. This bill relates to the corporate income tax deduction for federal income taxes paid and corporate income tax rates. HB1471 the way it sits now is at 7.5% for a top bracket and Waters Edge option is out and the fiscal note is neutral. Another option is proposed. Asked for an explanation of the proposal from the Tax Department.

Donnita Wald, Legal Counsel, State Tax Department (mtr #106) - Distributed amendment .02TX dated 3-19-03 and explained the amendment. Deals with grandfathering the Waters Edge option. Pointed out the difference to engrossed HB1471. Reviewed all sections of the amendment. Reviewed sections 1 and 2 of the bill and the effective dates therein. Summarized all effective dates listed in the bill and the amendment.

Senator Tollefson (mtr #359) - With no more elections available for Waters Edge, any way to forecast the effect.

Kathy Strombeck, State Tax Department (mtr #384) - Based on Waters Edge elections in place, we do forecast that. We have a forecast on dollar amount of the grandfathering provision.

Senator Tollefson (mtr #419) - Question is really based on the time when there is no Waters Edge option.

Ms. Strombeck (mtr #466) - The corporations would still file using a World Wide Combined option. Is a change in method that 95% of our corporations do anyway. Some companies get little benefit from Waters Edge and some companies get a substantial benefit.

Senator Nichols (mtr #530) - With regard to Waters Edge, do not always know the effect, how many of the 210 filers get little benefit from that route.

Ms. Strombeck (mtr #564) - Is difficult to say. Of the 200 only half will pay substantial tax.

Senator Nichols (mtr #613) - Regarding the fiscal note, has it changed with these amendments.

Ms. Strombeck (mtr #621) - Yes it has. Gave the estimated fiscal effect of the amendments. Overall the set of amendments that Ms. Wald went over, for the 2003-2005 biennium, is estimated at $244,000.00 negative.

Senator Wardner (mtr #683) - Asked for additional input. We will not act on the bill today.

Representative Al Carlson (mtr #726) - Intent is to have ND establish our own corporate tax rate, attempting to get in the 7% range. Companies in the state felt that is a rate they could live with. Trying to find a methodology to eliminate winners and losers. Had recommended grandfathering the Waters Edge election. Other options with Waters Edge are available. Trying to find a common ground. Feels the fiscal note is very close to revenue neutral.

Senator Tollefson (mtr #1023) - Is the Waters Edge an attraction for corporations to come to ND?

Representative Carlson (mtr #1036) - Most filers using Waters Edge were already here.

Senator Tollefson (mtr #1103) - The idea of dropping the rate to 7% is perception. Is Waters Edge part of the perception?

Representative Carlson (mtr #1120) - If is wasn't at the beginning. Is not the biggest part of the pie for us. Tax committee's I served on, don't want to raise taxes, want to protect the revenue stream we had.

Rick Clayburgh, State Tax Commissioner (mtr #1245) - Responded to Representative Carlson's question and the term winners and losers. Has a goal to eliminate corporate income tax deduction and lower our rate to its effective rate, and try to minimize the impact on taxpayers. List of 20-25 corporate taxpayers that would be impacted over $5,000.00. One at top end would have a $100,000.00 tax impact. A goal has been achieved as far as eliminating that corporate income tax deduction. Eliminating the carryback option will decouple us from what will happen with the feds. Plan does a good job of achieving our interest in eliminating the perception we have of the 10.5% corporate income tax rate.

Dale Anderson, President, GNDA (mtr #1609) - Requested the opportunity to review the amendments that have been proposed and comment on them. Supportive of economic development in ND. But also need a positive strong tax climate. Waters Edge is part of that climate. Restated that existing businesses not be impacted as a result of this effort.

Senator Wardner (mtr #1793) - We won't act on this bill today. Will take more input.

Senator Nichols (mtr #1824) - Discussed earlier that most corporations that use Waters Edge were already here. Is it a factor in bringing new business to ND? And how does that weigh against a lowered rate.

Mr. Anderson (mtr #1889) - Feels the Waters Edge filing option is an important part of the tax policy for ND. Does not know who the Waters Edge filers are.

Ron Ness, ND Petroleum Council (mtr #2040) - Regarding Senator Nichols question, Russ Staiger of Bismarck Development uses the availability of Waters Edge all the time when recruiting. Feels it is a tool to keep companies here.

John Morrison, Fleck Mather Strutz Law Firm (mtr #2155) - Practices primarily natural resources law represent a number of energy companies. Commented on his industries perspective on Waters Edge in ND. Went over statutes of tax law which including World Wide Combination (WWC) and Waters Edge. As a result of a US Supreme court case, ND became aggressive in pursuing World Wide Combination. Gave history of ND's use of Waters Edge option. Every other state that uses WWC has a Waters Edge election. If Waters Edge is repealed, ND would become the only state in the union to aggressively tax foreign income. In speaking with Russ Staiger, feels very strongly that any such attempt would have a devastating impact on his ability to bring multinational companies into the state. Supports this bill as long as Waters Edge is not repealed.

Senator Tollefson (mtr #2639) - After five years it is repealed.

Mr. Morrison (mtr #2646) - Yes, companies will be prohibited from Waters Edge.

Senator Wardner (mtr #2672) - Given no further testimony or comments, adjourned the subcommittee on HB2715.

2003 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB1471

Senate Finance and Taxation Committee

☐ Conference Committee

Hearing Date March 25, 2003

Tape Number	Side A	Side B	Meter #
1		X	1-635

Committee Clerk Signature

Minutes:

Senator Urlacher opened the discussion on HB1471. All committee members are present.

Senator Wardner (mtr #10) - The subcommittee on HB1471 is done and have a just solution at this time. Amendment .0TX1 proposed and will have the Tax Department explain the amendments.

Donnita Wald, Legal Counsel, State Tax Department (mtr #55) - Present the amendment and explained the high point and the impact on the bill.

Senator Nichols (mtr #218) - What is the fiscal note with the latest amendment?

Ms. Wald (mtr #229) - Believes it to be about $545,000.00.

Senator Wardner (mtr #277) - Commented on the bill with the amendment. We have a 7% high rate for corporate income tax and the fiscal note is brought down to $545,000.00., eliminated the carry back provision on the net operating loss. The Waters Edge election is still in there. We take care of the companies in the state and hopefully making it attractive for other companies to at least take a look at us. It is going to cost the state $545,000.00. This is at cheap as it is going to get.

Senator Wardner moves to amend with amendment .0TX1. Second by Senator Syverson. Voice vote by 6 yea, 0 nay, 0 absent. Bill is amended.

Senator Wardner moves a Do Pass as Amended and rerefer to Appropriations. Second by Senator Tollefson. Roll call vote 6 yea, 0 nay, 0 absent. Carrier is Senator Wardner.

Amendment proposed 3.24.03

30645.02TX
Title.

Prepared by the Office of State Tax Commissioner
March 19, 2003

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1471

Page 1, line 2, replace "subsection" with "subsections" and after "1" insert "and 3", remove "and", and after "57-38-30" insert "and subsection 3 of section 57-38-40"

Page 1, line 4, after the comma insert "net operating losses,"

Page 6, after line 6, insert:

"**SECTION 3. AMENDMENT.** Subsection 3 of section 57-38-01.3 of the North Dakota Century Code is amended and reenacted as follows:

3. The sum calculated pursuant to subsection 1 must be reduced by the amount of any net operating loss that is attributable to North Dakota sources. If the net operating loss that is attributable to North Dakota sources exceeds the sum calculated pursuant to subsection 1, the excess may be ~~carried back or~~ carried forward for the same time period that an identical federal net operating loss may be ~~carried back or~~ carried forward. If a corporation uses an apportionment formula to determine the amount of income that is attributable to North Dakota, the corporation must use the same formula to determine the amount of net operating loss that is attributable to North Dakota. In addition, no deduction may be taken for a ~~carryback or~~ carryforward when determining the amount of net operating loss that is attributable to North Dakota sources."

Page 6, line 7, replace "3." with "4."

Page 6, line 14, replace "two-tenths" with "six-tenths"

Page 6, line 16, remove the overstrike over "~~four and~~" and replace "three and two-tenths" with "one-tenths"

Page 6, line 19, replace "four and three-tenths" with "five and six-tenths"

Page 6, line 21, replace "five" with "six"

Page 6, line 23, overstrike "and not in excess of fifty"

Page 6, line 24, overstrike "thousand dollars," and replace "six and five-tenths" with "seven"

Page 6, line 25, overstrike "f. On all taxable income above fifty thousand dollars, at the rate of" and remove "seven"

Page 6, line 26, overstrike "and", remove "five-tenths" and overstrike "percent"

Page 6, after line 30, insert:

"**SECTION 5. AMENDMENT.** Subsection 3 of section 57-38-40 of the North Dakota Century Code is amended and reenacted as follows:

3. A corporation may file a claim for credit or refund of an overpayment of tax resulting from the carryback of a net operating loss under subsection 3 of section 57-38-01.3, or resulting from a federal capital loss carryback, within three years after the prescribed due date for filing the return, including extensions for the tax

year in which the loss was incurred. The provisions of this subsection applicable to net operating losses are ~~effective~~ ineffective for loss years beginning after December 31, ~~1986~~ 2002."

Page 7, line 1, replace "**4.**" with "**6.**"

Page 7, line 3, replace "**5.**" with "**7.**" and replace "This" with "Section 1 of this"

Page 7, line 4, after the period insert "Sections 2 and 4 of this Act are effective for taxable years beginning after December 31, 2003. Section 3 of this Act is effective for net operating losses incurred in taxable years beginning after December 31, 2002. Section 6 of this Act is effective for taxable years beginning after December 31, 2002, except that, for water's edge elections made in taxable years beginning before January 1, 2003, the provisions of chapter 57-38.4 remain in effect but only for the remainder of the taxpayer's five year election period."

Renumber accordingly

30645.0TX1
Title.

Prepared by the Office of State Tax Commissioner
March 24, 2003

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1471

Page 1, line 1, after "to" insert "create and enact a new subsection to section 57-38.4-02 of the North Dakota Century Code, relating to the tax on the water's edge filing method; to"

Page 1, line 2, replace "subsection" with "subsections" and after "1" insert "and 3", remove "and", and after "57-38-30" insert "and subsection 3 of section 57-38-40"

Page 1, line 4, after the comma insert "net operating losses," and remove "to repeal chapter 57-38.4 of the North Dakota"

Page 1, line 5, remove "Century Code, relating to the corporate income tax water's edge filing election;"

Page 6, after line 6, insert:

"**SECTION 3. AMENDMENT.** Subsection 3 of section 57-38-01.3 of the North Dakota Century Code is amended and reenacted as follows:

3. The sum calculated pursuant to subsection 1 must be reduced by the amount of any net operating loss that is attributable to North Dakota sources. If the net operating loss that is attributable to North Dakota sources exceeds the sum calculated pursuant to subsection 1, the excess may be ~~carried back or~~ carried forward for the same time period that an identical federal net operating loss may be ~~carried back or~~ carried forward. If a corporation uses an apportionment formula to determine the amount of income that is attributable to North Dakota, the corporation must use the same formula to determine the amount of net operating loss that is at[illegible]utable to North Dakota. In addition, no deduction may be taken for a ~~carryback or~~ carryforward when determining the amount of net operating loss that is attributable to North Dakota sources."

Page 6, line 7, replace "**3.**" with "**4.**"

Page 6, line 14, replace "<u>two-tenths</u>" with "<u>six-tenths</u>"

Page 6, line 16, remove the overstrike over "~~four and~~" and replace "<u>three and two-tenths</u>" with "<u>one-tenths</u>"

Page 6, line 19, replace "<u>four and three-tenths</u>" with "<u>five and six-tenths</u>"

Page 6, line 21, replace "<u>five</u>" with "<u>six</u>"

Page 6, line 23, overstrike "and not in excess of fifty"

Page 6, line 24, overstrike "thousand dollars," and replace "<u>six and five-tenths</u>" with "<u>seven</u>"

Page 6, line 25, overstrike "f. On all taxable income above fifty thousand dollars, at the rate of" and remove "<u>seven</u>"

Page 6, line 26, overstrike "and", remove "<u>five-tenths</u>" and overstrike "percent."

Page 6, after line 30, insert:

"**SECTION 5. AMENDMENT.** Subsection 3 of section 57-38-40 of the North Dakota Century Code is amended and reenacted as follows:

3. A corporation may file a claim for credit or refund of an overpayment of tax resulting from the carryback of a net operating loss under subsection 3 of section 57-38-01.3, or resulting from a federal capital loss carryback, within three years after the prescribed due date for filing the return, including extensions, for the tax year in which the loss was incurred. The provisions of this subsection applicable to net operating losses are ~~effective~~ ineffective for loss years beginning after December 31, ~~1986~~ 2002.

SECTION 6. A new subsection to section 57-38.4-02 of the North Dakota Century Code is created and enacted as follows:

In addition to the tax imposed under subsection 1 of section 57-38-30, there is imposed an additional tax of three and one-half percent of taxable income which must be levied, collected and paid annually in the same manner as provided in chapter 57-38."

Page 7, remove lines 1 and 2

Page 7, line 3, replace "**5.**" with "**7.**" and replace "This Act is" with "Section 1 of this Act is"

Page 7, line 4, after the period insert "Sections 2, 4, and 6 of this Act are effective for taxable years beginning after December 31, 2003. Section 3 of this Act is effective for net operating losses incurred in taxable years beginning after December 31, 2002."

Renumber accordingly

30645.0201
Title.0300

Adopted by the Finance and Taxation Committee
March 25, 2003

JB 3-26-03 1 of 2

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1471

Page 1, line 1, after "to" insert "create and enact a new subsection to section 57-38.4-02 of the North Dakota Century Code, relating to the tax on the water's edge filing method; to"

Page 1, line 2, replace "subsection" with "subsections", after "1" insert "and 3", remove "and", and after "57-38-30" insert ", and subsection 3 of section 57-38-40"

Page 1, line 4, after the comma insert "net operating losses," and remove "to repeal chapter 57-38.4 of the North Dakota"

Page 1, line 5, remove "Century Code, relating to the corporate income tax water's edge filing election;"

Page 6, after line 6, insert:

"**SECTION 3. AMENDMENT.** Subsection 3 of section 57-38-01.3 of the North Dakota Century Code is amended and reenacted as follows:

3. The sum calculated pursuant to subsection 1 must be reduced by the amount of any net operating loss that is attributable to North Dakota sources. If the net operating loss that is attributable to North Dakota sources exceeds the sum calculated pursuant to subsection 1, the excess may be ~~carried back or~~ carried forward for the same time period that an identical federal net operating loss may be ~~carried back or~~ carried forward. If a corporation uses an apportionment formula to determine the amount of income that is attributable to North Dakota, the corporation must use the same formula to determine the amount of net operating loss that is attributable to North Dakota. In addition, no deduction may be taken for a ~~carryback or~~ carryforward when determining the amount of net operating loss that is attributable to North Dakota sources."

Page 6, line 14, replace "two-tenths" with "six-tenths"

Page 6, line 16, remove the overstrike over "~~four and~~" and replace "three and two-tenths" with "one-tenth"

Page 6, line 19, replace "four and three-tenths" with "five and six-tenths"

Page 6, line 21, replace "five" with "six"

Page 6, line 23, overstrike "and not in excess of fifty"

Page 6, line 24, overstrike "thousand dollars," and replace "six and five-tenths" with "seven"

Page 6, line 25, overstrike "f. On all taxable income above fifty thousand dollars, at the rate of" and remove "seven"

Page 6, line 26, overstrike "and", remove "five-tenths", and overstrike "percent."

2 of 2

Page 7, replace lines 1 and 2 with:

"**SECTION 5. AMENDMENT.** Subsection 3 of section 57-38-40 of the North Dakota Century Code is amended and reenacted as follows:

3. A corporation may file a claim for credit or refund of an overpayment of tax resulting from the carryback of a net operating loss under subsection 3 of section 57-38-01.3, or resulting from a federal capital loss carryback, within three years after the prescribed due date for filing the return, including extensions, for the tax year in which the loss was incurred. The provisions of this subsection applicable to net operating losses are ~~effective~~ ineffective for loss years beginning after December 31, ~~1986~~ 2002.

SECTION 6. A new subsection to section 57-38.4-02 of the North Dakota Century Code is created and enacted as follows:

In addition to the tax imposed under subsection 1 of section 57-38-30, there is imposed an additional tax of three and one-half percent of taxable income which must be levied, collected, and paid annually in the same manner as provided in chapter 57-38."

Page 7, line 3, replace "This Act is" with "Sections 1, 2, 4, and 6 of this Act are"

Page 7, line 4, replace "2002" with "2003. Sections 3 and 5 of this Act are effective for net operating losses incurred in taxable years beginning after December 31, 2002"

Renumber accordingly

Date: 3.25.03
Roll Call Vote #: 2

2003 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. HB1471

Senate Finance and Taxation Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number ______

Action Taken Do Pass as Amended & Rerefer to Approp.

Motion Made By Sen. Wardner Seconded By Sen. Tollefson

Senators	Yes	No	Senators	Yes	No
Senator Urlacher - Chairman	✓		Senator Nichols	✓	
Senator Wardner - Vice Chairman	✓		Senator Seymour	✓	
Senator Syverson	✓				
Senator Tollefson	✓				

Total (Yes) 6 No 0

Absent ______

Floor Assignment Sen. Wardner

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

HB 1471, as engrossed: Finance and Taxation Committee (Sen. Urlacher, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** and **BE REREFERRED** to the **Appropriations Committee** (6 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). Engrossed HB 1471 was placed on the Sixth order on the calendar.

Page 1, line 1, after "to" insert "create and enact a new subsection to section 57-38.4-02 of the North Dakota Century Code, relating to the tax on the water's edge filing method; to"

Page 1, line 2, replace "subsection" with "subsections", after "1" insert "and 3", remove "and", and after "57-38-30" insert ", and subsection 3 of section 57-38-40"

Page 1, line 4, after the comma insert "net operating losses," and remove "to repeal chapter 57-38.4 of the North Dakota"

Page 1, line 5, remove "Century Code, relating to the corporate income tax water's edge filing election;"

Page 6, after line 6, insert:

"**SECTION 3. AMENDMENT.** Subsection 3 of section 57-38-01.3 of the North Dakota Century Code is amended and reenacted as follows:

3. The sum calculated pursuant to subsection 1 must be reduced by the amount of any net operating loss that is attributable to North Dakota sources. If the net operating loss that is attributable to North Dakota sources exceeds the sum calculated pursuant to subsection 1, the excess may be ~~carried back or~~ carried forward for the same time period that an identical federal net operating loss may be ~~carried back or~~ carried forward. If a corporation uses an apportionment formula to determine the amount of income that is attributable to North Dakota, the corporation must use the same formula to determine the amount of net operating loss that is attributable to North Dakota. In addition, no deduction may be taken for a ~~carryback or~~ carryforward when determining the amount of net operating loss that is attributable to North Dakota sources."

Page 6, line 14, replace "two-tenths" with "six-tenths"

Page 6, line 16, remove the overstrike over "~~four and~~" and replace "three and two-tenths" with "one-tenth"

Page 6, line 19, replace "four and three-tenths" with "five and six-tenths"

Page 6, line 21, replace "five" with "six"

Page 6, line 23, overstrike "and not in excess of fifty"

Page 6, line 24, overstrike "thousand dollars," and replace "six and five-tenths" with "seven"

Page 6, line 25, overstrike "f. On all taxable income above fifty thousand dollars, at the rate of" and remove "seven"

Page 6, line 26, overstrike "and", remove "five-tenths", and overstrike "percent."

Page 7, replace lines 1 and 2 with:

"**SECTION 5. AMENDMENT.** Subsection 3 of section 57-38-40 of the North Dakota Century Code is amended and reenacted as follows:

3. A corporation may file a claim for credit or refund of an overpayment of tax resulting from the carryback of a net operating loss under subsection 3 of section 57-38-01.3, or resulting from a federal capital loss carryback, within three years after the prescribed due date for filing the return, including extensions, for the tax year in which the loss was incurred. The provisions of this subsection <u>applicable to net operating losses</u> are~~effective~~ <u>ineffective</u> for loss years beginning after December 31, ~~1986~~ <u>2002</u>.

SECTION 6. A new subsection to section 57-38.4-02 of the North Dakota Century Code is created and enacted as follows:

<u>In addition to the tax imposed under subsection 1 of section 57-38-30, there is imposed an additional tax of three and one-half percent of taxable income which must be levied, collected, and paid annually in the same manner as provided in chapter 57-38.</u>"

Page 7, line 3, replace "This Act is" with "Sections 1, 2, 4, and 6 of this Act are"

Page 7, line 4, replace "2002" with "2003. Sections 3 and 5 of this Act are effective for net operating losses incurred in taxable years beginning after December 31, 2002"

Renumber accordingly

2003 SENATE APPROPRIATIONS

HB 1471

2003 SENATE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1471 & Vote

Senate Appropriations Committee

❑ Conference Committee

Hearing Date 3-31-03

Tape Number	Side A	Side B	Meter #
1		X	1880-5090
Committee Clerk Signature Sandra Davison			

Minutes: CHAIRMAN HOLMBERG opened the hearing to HB 1471. A bill relating to financial institutions taxes, the corporate income tax deduction for federal income taxes paid, and corporate income tax rates; relating to the corporate income tax water's edge filing election; to provide an effective date.

(Meter 1880) RICK CLAYBURGH, ND Tax Commissioner testified in support of the bill. He explained the fiscal note and the bill. The bill eliminate the federal deduction we allow on our state tax form for corporations to deduct their federal tax payments. The bill allows the state to reduce the rate the state charges corporations from the high rate of 10 ½ % to 7%. If we were to eliminate the cooperate income tax deduction that is allowed in state law. The revenue neutral rate would be 7.6 %. The Senate Finance and Tax committee with a lot of work, from people from the tax department and the Governor's office where able to put together an agreement where it was further reduced the corporate income tax rate in ND from 7.6% down to 7%. The bill creates 5 brackets instead of 6 brackets. To help fund that one of the issues that was looked at was the elimination of net operating loss carry back provisions that appear in ND Century code. The net operating loss does allow a corporation to decide if they want to carry a loss backwards to a previous tax year, thereby, filing an amended return for a refund or carrying the loss forward. ND was a minority of states that allowed carry back and that is changed in the bill and eliminate the net operating loss carry back provisions in state tax law and carries that loss forward. The part of the bill that lowers the rate to 7% had a negative fiscal impact in this biennium of 2.3 million dollars approximately the net operating loss carry back provisions has a positive impact of 1.8 million dollars. The bill at one point did water's edge election eliminating but that now has been taken out. The bottom line is the fiscal impact is a negative $544,000. when you talk about corporate income taxes bring into our general fund about 92 million dollars projected in our biennium. That fiscal note is close to revenue neutral as possible. From the standpoint of tax policy, he supports the legislation, it does allow to address the perception that ND has, of one of the highest tax rates down to bring ND rate to one of the most attractive rates in the country. The range will be the top of 7% , this is a positive step for economic development for our state. (Meter 2220) SENATOR SCHOBINGER asked what is the current effective tax rate for each of the 6 brackets? RICK CLAYBURGH replied the current effective rate is 7.6% but he would have to get that information. SENATOR SCHOBINGER stated that there are two specific independent studies, one being the Frazier Institute and the other being the Small Survival Committee that each year ranks the state on their friendliness to business and both of those independent studies listed ND top rate currently at 6.8% or 6.825. When this report comes out next year, the rate will reach 7%, ND specifically in the Small Business Survival Committee index, is listed #35 out of 50 as friendliness to business. A listing of 7% will likely move ND downward even more. What is your comment on that? RICK CLAYBURGH address the question of the issue that is looked at in those studies are specifically looking at the effective rate, our effective rate of corporate income taxes is below that targeted 7.6%. It is a lower number because basically you are taking all of the rates, that all the tax payors fall into and coming up with an median rate. With the 75 high rate, we are going to be far below that 7% now in our average effective rate in ND. That would be a positive statement. The issue about the Small Business Survival Index not only looks at taxes rates but looks at other aspects as well, dealing with Worker's Compensations, other aspects as far as what businesses have to deal with the state, regulatory process, a number of issues not just tax issues. SENATOR SCHOBINGER stated that given what he seen this session, none of those other variables will change this session. They do list ND's top corporate tax rate, which is the rate they use is 6.825% and as he reads this, it will now be 7%. He had a question on Section 6 in the Senate amendment and what is that and what does it do? (Meter 2557) RICK CLAYBURGH answered that he wanted to clarify the 6.8% that was mentioned as the effective rate, that is the average effective rate of all rates combined targeted. That is not listing our top rate, that is an effective rate. If SENATOR SCHOBINGER could show him that study, he will clarify that study. The 7% rate being the top effective rate of all rates combined will drop our rate below the 7%. The rate will change January 1, 2004 and the current structure is in effect this tax year. In Section 6 of the bill, they were looking at a number of bills that have been addressed this session looking at water's edge election and without getting too complex looking at tax policy issue, ND is a worldwide combination state as far as how we look at corporations and what we bring into our three factor apportionment formula. We do allow tax payors to make an election if they want to file as a world wide combined reporting corporation, of bringing all of their corporate entities together or focus on the water's edge which technically is to the water's edge of the United States. In doing that, in taking that water's edge election, they do not allow those corporations to take the benefit also of the corporate income tax deduction. In this bill, by eliminating the corporate tax and lowering the rate, unless they did something to address water's edge, those water's edge filers would not only gain the water's edge filing but also would have the benefit of the lower rate. At one point had they not done anything, there would still be published a 10 ½ % rate for water's edge filers. The committee and the sponsors had looked at repeal the water's edge election and they felt that may cause some problems with economic development issues. So they have created the 7% top rate but for water's edge filers, people who elect to take water's edge, there is a surcharge added to rate of 3 ½ % basically taking them to the 10 ½ % if they were at the high rate or any subsequent rate below that . All of the business groups that came in with concern over the bill, their concerns deal with water's edge.

(Meter 2393) SENATOR SCHOBINGER stated in his opening statements he state that we are close to revenue neutral, how is it given we are scored these things statically rather than dynamically that we can reduce the corporate income tax rate and remain revenue neutral?

(Meter 2970) RICK CLAYBURGH stated when a fiscal note is put together in the tax department, the department does not put the analysis to a bill saying because of this legislation or but for this legislation, certain activity is going to occur. All the department can do is give a fiscal note based on the current information of what the tax types bring in. He believes there will be some positive impact because of this, exactly what it will be, he can't predict.

(Meter 3081) REPRESENTATIVE CARLSEN, District 41, sponsor of the bill testified on the bill. He felt it was important to look at the corporate income tax structure. There is an agreement that a reduction of the tax rates is positive for business growth in ND. He does not always agree with the methodology but does agree that the concept needs to be addressed and should be a long term goal of the state to make a direction towards reducing the tax rate. He talked about an analytic meeting in which the major points of discussion was what effects the tax rates have upon the states. Obviously there were a number of states that do not have income tax at all, personal nor corporate. On the other hand, they have other taxes that off set their revenue needs. There is no influx of people flocking to their states. The only time there was additional growth was when both areas of taxes were lowered it had a positive note. Last session they coupled the personal income tax and that did a couple of things, it established our own rates for ND and it maintained our revenue base. If you talk to people who filed out tax this year, their taxes went up because the federal government cut their personal income tax rate and when we decoupled, ours didn't go down, they stayed at the same rate we established last time. The revenue neutrality question is a good one. It is hard to maintain revenue neutrality and have a lower rate. The things need to look at are net operating loss, number of brackets that are in the bill, the question of perception is reality. If we publish a 10 ½ % rate, or if somebody averages our rate to 6.8%, do the businesses read that? If you talk to the Economic Development people, they say yes, they read that and it does have an effect. He feels this is a positive move and would like to see this move continue. He feels that need to protect the revenue stream, so either they need to raise the tax or take away exemptions. He attempted in an earlier bill to lower the rate but took away the exemption that retailers get for filing their sales tax with the state. The room was full of people who said that was not a good idea. He feels that if the state lowers the taxes, it should be both corporate and the individual income taxes.

(Meter 3645) SENATOR SCHOBINGER asked if the tax department knew what the current effective tax rates are? REPRESENTATIVE CARLSEN stated that 10 ½ % is the high and low is he doesn't know that rate. (Meter 3706) SENATOR SCHOBINGER stated there was complaints from the personal income that liabilities went up and his concern is about what will happen next year on this bill. REPRESENTATIVE CARLSEN stated anytime the brackets are changed, and it goes from $50,000 top bracket to $30,000 top tax bracket, there are going to be winners and losers.

(Meter 3840) RON ROSENBERGER, representing Governor's office and the Department of Commerce testified on HB 1471. He felt the tax department has worked extremely hard with the private businesses to come up with a good bill dealing with the net operating losses, it has been a cooperative and long process. This has been looked at for about 8-10 years. It is good for marketing the state of ND.

(Meter 3970) SENATOR SCHOBINGER asked is the reality of this bill is simply an attempt to change what we perceive to be a high corporate income tax? RON ROSENBERGER stated yes, the Commerce department as well as the tax department sees studies listing ND at 10 ½ % . They do not look into farther as sight selectors and do not take into consideration of the federal deduction which brings it down into the 7% or lower area.

(Meter 4097) SENATOR SCHOBINGER asked if there are specific numbers of industries or businesses that are paying the top corporate rate in ND that show us this will be a tax cut for them? (Meter 4150) RON ROSENBERGER doesn't have the information, the tax department may have some basic information on that. RICK CLAYBURGH stated the tax department has run many analysis on how this impacts the various tax payors. On this current proposal, the tax department has identified the top 8 winners and losers. Anytime there are changes in tax code, there is going to be somebody who pays differently that before. On this particular program at 7%, the tax department ran an analysis of the top 25 who will pay more liability and the 25 who will be paying less. Those would will be paying more liability, except for the top 4 or 5, all the rest will be less that $5,000 liability increase. The percentages are quite small. The list of names are confidentiality.

(Meter 4421) SENATOR ANDRIST made a motion of a DO PASS with SENATOR BOWMAN seconded.

Discussion

(4433) SENATOR SCHOBINGER stated his wish was not to pass this bill. For the majority of tax payers, it would be a tax increase. This bill is effectively increasing the corporate income tax in ND. This is not going to help change the problem in the state of losing people from this state.

(Meter 4582) SENATOR BOWMAN stated if it is going to raise the rate, why would there be a negative fiscal note? SENATOR SCHOBINGER stated it will raise the rate. It shows a negative $544,000 and that is why he asked for the working papers on it. That is why he asked for the effective rates of the top brackets.

(Meter 4800) SENATOR ROBINSON stated that perceptions becomes reality. He feels that they need to look at the packet of taxes. There isn't anyone who wants to come to a state that has quality infrastructure. Taxes are important but infrastructure and quality of life, are one number. We are low in worker's comp, low in unemployment compensation, and other factors that play into our ability and inability to sustain a strong economic growth in the state.

(Meter 4895) SENATOR MATHERN stated the questions raised by SENATOR SCHOBINGER are serious questions and questions of the fiscal note. Any input from legislative council on the fiscal note?

(Meter 4987) ALLEN KNUDSON stated that Legislative Council has not reviewed the fiscal note and do not do analysis on fiscal notes.

(Meter 5025) Roll was called on a DO PASS with a vote of 10 yeas, 3 nays, and 1 absent. The bill will be carried by the Finance and Tax committee, SENATOR WARDNER.

CHAIRMAN HOLMBERG closed the hearing to HB 1471.

Date: 3/31/03
Roll Call Vote #: 1

2003 SENATE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. 1471

Senate Appropriations Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number

Action Taken Do Pass

Motion Made By Andrist Seconded By Bowman

Senators	Yes	No	Senators	Yes	No
Senator Holmberg, Chairman	✓				
Senator Bowman, Vice Chair	✓				
Senator Grindberg, Vice Chair					
Senator Andrist	✓				
Senator Christmann	✓				
Senator Kilzer	✓				
Senator Krauter	✓				
Senator Kringstad	✓				
Senator Lindaas		✓			
Senator Mathern	✓				
Senator Robinson	✓				
Senator Schobinger		✓			
Senator Tallackson	✓				
Senator Thane		✓			

Total (Yes) 10 No 3

Absent 1

Floor Assignment Finance/Tax (Wardner)

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE (410)
March 31, 2003 11:31 a.m.

Module No: SR-57-6182
Carrier: Wardner
Insert LC: . Title: .

REPORT OF STANDING COMMITTEE

HB 1471, as engrossed and amended: Appropriations Committee (Sen. Holmberg, Chairman) recommends **DO PASS** (10 YEAS, 3 NAYS, 1 ABSENT AND NOT VOTING). Engrossed HB 1471, as amended, was placed on the Fourteenth order on the calendar.

2003 TESTIMONY

HB 1471

Rep Al Carlson
1-29.03

Summary of House Bill 1471

- Section 1 reinstates the federal tax deduction for financial institutions
- Section 2 repeals the federal tax deduction for corporations
- Section 3 imposes a reduced, flat rate (to be amended into brackets)
    - The proposed amendment from a "flat rate" to "brackets" are fiscally equal to the flat rate contained in the bill as filed (i.e. replacing the flat rate with the brackets ranging from 2.1% to 7.2% maintains the overall revenue-neutrality of the bill)
    - A top rate of 7.6% would be needed to be "revenue neutral" without the sales tax base broadening contained in HB 1471
- Sections 4 and 5 impose the sales and use tax on newspapers and magazine subscriptions
- Section 6 repeals the water's edge optional filing method and repeals the sales and use tax exemptions for newsprint and ink.
- The corporation income tax provisions are expected to reduce corporate income tax by an estimated $4.1 million per biennium
- The sales tax base broadening is expected to increase sales tax revenues by an estimated $4.1 million per biennium
- A small portion (8%) of the additional sales tax revenue from the base broadening will go to the state aid distribution fund
- Because corporations pay a year's tax liability over nearly three years, the general fund will receive the new sales tax revenues slightly sooner than it will "lose" the corporate revenues. This timing differential helps to offset the component of the sales tax base broadening "lost" to the state aid distribution fund

HB 1471
House Finance and Taxation Committee
Jan. 22, 2003

Chairman Belter and Members of the Committee,

I'm Jill Denning Gackle, general manager of BHG Inc., a group of 1 i newspapers in west central North Dakota. Although we don't own any of your newspapers, we have newspapers that are similar in size and content to your Cass County Reporter, Towner County Record-Herald and Herald-Press of Harvey and Fessenden. The newspapers we manage are from New Town, Parshall and Velva to Center, Turtle Lake and Washburn, each with 600 and 3,000 subscribers.

We employ more than 80 people, so by the looks of it, we must be doing well enough to send a little on to the state. Not so. Removing the tax exemption on newspapers would cost our 11 newspapers a total of between $30,000 and $35,000 each year. As if that isn't enough to worry about, we also are going to have a substantial hike in the unemployment tax this year and our property insurance is going up about $8,000. We have more subscribers dying than having babies and we work hard to keep every single business on our Main Streets.

Doing business in rural North Dakota gets harder every day. And now the sponsors of this bill want to tax newspapers in a specific bill that only names newspapers. It doesn't name all the other things that aren't taxed – like prescription drugs, farm chemicals, insurance premiums, Bibles, artificial teeth, eyeglasses, aircraft and tickets to church suppers.

It's simply not fair to try to lower the corporate income taxes for all businesses and then remove the sales tax exemption for just one type of business. The governor has stated that he wants to help rural North Dakota survive. By singling out the mainstays of rural North Dakota – the state's newspapers – it will make it more difficult for our communities to survive.

If this tax were removed, we would cut two to three employees from our business because we just can't pass any more on to our customers.

Don't single out newspapers. Don't tax us anymore than we're already taxed. Above all, please vote no on HB 1471.

Thank you for listening. I'll be happy to answer any questions you might have.

TESTIMONY BEFORE THE HOUSE FINANCE AND TAXATION COMMITTEE

HB 1471
January 29, 2003

Mr. Chairman and members of the committee:

I'm Roger Bailey, executive director of the North Dakota Newspaper Association, and I'm here to speak in opposition to House Bill 1471.

For almost 25 years, I was the publisher of the weekly newspaper at Rolla, and still have an interest in that newspaper and in North Central Printing at Rugby, a central printing plant owned by the newspapers in Harvey, Rugby, Cando, Bottineau and Rolla.

The implementation of HB 1471 could have dire consequences on the operations of the newspapers printed at North Central Printing. In addition, to the newspapers of its owners, North Central Printing also prints the Carrington and Minnewaukan newspapers.

In 2001 and 2002, North Central Printing purchased an average of $92,288 worth of newsprint and ink which would require a sales tax of $5537.28 if HB 1471 passes.

The seven newspapers printed at North Central Printing would also face a sales tax of approximately $21,528 if the tax is applied to the sale of newspaper subscriptions and single copies.

These are substantial increases in the cost of operations for all of North Dakota's newspapers. In some cases, the costs would need to be passed on to advertisers and readers. In some cases, notably with the sale of newspapers from vending machines, that won't be possible and the newspapers will have to absorb the taxes.

At a time when most of North Dakota's small towns are diminishing in population and the number of businesses declines as well, it will be difficult for the newspapers to increase their advertising rates to cover the proposed taxes. In essence, an increase in taxes will hasten the demise of many small North Dakota communities who rely on the newspaper as the primary form of community communication.

The North Dakota Newspaper Association represents 80 weekly and 10 daily newspapers in North Dakota. Among the 80 weekly newspapers are 25 with a circulation of 1,000 or fewer copies each week. The increase could be difficult for all of North Dakota's newspapers and particularly devastating to the smallest newspapers like those in Aneta, Carson, Center, Drayton, Edmore, Fordville, Gackle, Hatton, Larimore, McVille, Medora, Michigan, Northwood, Parshall, Turtle Lake, Underwood, Westhope, Edegely, Glen Ullin, Kulm, Litchville, McClusky, Velva and Walhalla.

HB 1471 presents a series of "fairness" questions.

Is it fair to single out newspapers as the only exemption in current law to be removed?

Is it constitutional to impose a tax that essentially would be a levy on the free flow of information in our society and is therefore contrary to the public interest?

Is it fair to require newspapers to pay a tax for the distribution of its product while other forms of communication such as radio, television and direct mail would not be subject to the tax?

Would adding a six percent tax on subscriptions discourage newspapers from maintaining and increasing circulation, thus hurting the overall economy? Fewer newspapers in circulation would hurt retail merchants who rely heavily on newspaper advertising to get their message out to potential customers.

If newspapers pay a tax on newsprint and ink, is it fair to tax the product a second time when a tax is also assessed on the sale of the individual copies of the printed newsprint?

Will taxing newspapers and their advertisers out-of-business help sustain North Dakota?

On behalf of the members of the North Dakota Newspaper Association, I ask that this committee vote "Do Not Pass" on HB 1471.

If you have any questions, I will make every effort to answer them.

Thank You.

Wednesday, January 29, 2003

House Finance and Taxation Committee

HB1471

Chairman Belter and Committee Members:

My name is Dave Bundy, and I'm editor of The Bismarck Tribune. I appear today in opposition to this bill.

We have concerns with HB1471 as it applies to newspapers as a business as well as an outlet for public information and a voice for the community. Our chief concerns are these:

- The bill, as written, singles out newspapers and magazines, effectively forcing us to foot the bill for an overall corporate income tax break. The Tribune is willing to shoulder its fair share of the tax burden but opposes newspapers as a group being targeted.
- Initial analysis shows the corporate income tax break the Tribune would receive will not offset the additional cost of the bill. Other papers' analyses show similar findings.
- Being forced to pay this new tax could affect the number of people newspapers are able to employ and papers' ability to serve the public.
- Levying this new tax puts newspapers at a relative competitive disadvantage with other media outlets — namely TV and radio — in terms of operating expense and, therefore, advertising rates, where newspapers might be forced to look to recoup some financial losses.
- Collection of sales tax on newspapers sold poses enormous complications due to the variety of ways the paper is distributed and circulation revenue collected. In some places, young paper carriers would be forced to collect and track sales tax. Vending machines could not be retooled to accommodate sales tax, so newspapers would eat the tax expense associated with papers sold in many, if not all, news rack and retail locations.
- Newspapers would have to pass added expenses on to the public or cut back their operations. Raising prices and advertising rates discourages customers and readership. Cutting back operations translates into a less informed community.
- Finally, a bill that specifically targets newspapers poses a threat to the operation of a free press and is at odds with the First Amendment. Any legislation that hinders the exchange of ideas and public information does a disservice to democracy as a whole.

January 29, 2003

HOUSE FINANCE & TAXATION COMMITTEE
HB 1471

CHAIRMAN BELTER AND COMMITTEE MEMBERS:

My name is Jack McDonald. I'm appearing here today on behalf of the North Dakota Newspaper Association. We oppose HB 1471 for several reasons and ask that you give it a do not pass.

First, the bill is simply not fair. It balances an across the board corporate income tax cut on the backs of just one industry in the state...an industry that will feel the brunt of this bill in two or three ways. This bill eliminates the lowest, 3% tax bracket for North Dakota corporations in favor of a flat rate of 6.73%.

As you've heard, more than 25% of North Dakota's weekly newspapers are small corporations now paying in this 3% bracket who will not only have to pay more sales tax, but will also have to pay more income tax. And, it will hit the other small businesses in North Dakota's small towns that these newspapers serve. Meanwhile, the state's biggest corporations in the state's biggest cities will pay less tax.

Secondly, the sales tax is particularly hard to administer for the newspaper industry because of news racks and cross border sales for newspapers in cities adjacent to Minnesota, particularly Grand Forks, Fargo and Wahpeton. Because of the news rack problems, our best estimate is that North Dakota newspapers would have to pay approximately $185,000 out of their own pockets since they won't be able to collect it from their customers.

Thirdly, there is a real question about how much money this would raise. While we haven't had time to do a thorough review, quick research indicates a tax on newspaper sales would bring in anywhere from $4 million to $5 million per year – or much more than the Tax Department's estimate. The sales tax on newsprint and ink would probably bring in an additional $750,000.

Finally, we don't believe the elimination of the sales tax exemption on the purchase of newsprint and ink is legal. The North Dakota Supreme Court, in a 1966 decision I've attached, indicated that newsprint and ink comes within the statutory definition of property used in processing and thus was exempt under state law from the use tax. That law is still in effect in North Dakota.

The newspaper industry is willing to share its tax load along with all other North Dakota businesses, but we respectfully feel that it is not fair to expect it to shoulder a tax reduction burden alone. Singling out newspapers in this way could well have First Amendment implications. We respectfully request a do not pass. If you have any questions, I will be happy to try to answer them. THANK YOU FOR YOUR TIME AND CONSIDERATION.

*903 147 N.W.2d 903

Supreme Court of North Dakota.

The BISMARCK TRIBUNE CO., a corporation, Forum Publishing Co., a corporation, Grand Forks Herald, Inc., a corporation, and the Minot Daily News, Inc., a corporation, Plaintiffs and Respondents,
v.
Lloyd OMDAHL, as the Tax Commissioner of the State of North Dakota, Defendantand Appellant.

No. 8223.
Oct. 20, 1966.

Declaratory judgment proceeding. The District Court, Burleigh County, Cliford Jansonius, J., held that purchase of newsprint in Canada and purchase of ink in states outside of North Dakota, which newsprint was used by publishers in publication of newspapers, were not subject to state use tax, and appeal was taken. The Supreme Court, Strutz, J., held that newsprint and ink came within statutory definition of 'property used in processing' which was tangible personal property that became component part of other tangible personal property intended to be sold at retail, and were exempt from payment of use tax under statute providing for imposition of use tax upon tangible personal property purchased for storage, use, or consumption.

Judgment affirmed.

West Headnotes

[1] Taxation 🔑1245
371 ----
371XVI Sales, Use, Service, and Gross Receipts Taxes
371XVI(B) Tax Liability and Exemptions
371XVI(B)1 Transactions Taxable in General
371k1244 Purpose of Use or Consumption as Affecting Taxability
371k1245 Manufacturing or Processing, Use or Consumption In; Incorporation in New Product.

(Formerly 238k15.1(10))
Tangible personal property used in business of manufacturing any article, which tangible personal property becomes integral or component part of the personal property manufactured, compounded, or produced, is exempt from state use tax. NDCC 57-02-07, 57-39-01, subd. 2, 57-40-01, 57-40-02.

[2] Taxation 🔑1245
371 ----
371XVI Sales, Use, Service, and Gross Receipts Taxes
371XVI(B) Tax Liability and Exemptions
371XVI(B)1 Transactions Taxable in General
371k1244 Purpose of Use or Consumption as Affecting Taxability
371k1245 Manufacturing or Processing, Use or Consumption In; Incorporation in New Product.

(Formerly 238k15.1(10))
Contention that newspaper was service which was based, to a degree, on theory that after it had been read it had no further value or use was not valid basis for determining nature of product resulting from publication of a newspaper for purposes of whether newsprint and ink purchased therefor were subject to state use tax. NDCC 57-02-07, 57-39-01,

subd. 2, 57-40-01, 57-40-02.

[3] Taxation ⚷1241.1
371 ----
371XVI Sales, Use, Service, and Gross Receipts Taxes
371XVI(B) Tax Liability and Exemptions
371XVI(B)1 Transactions Taxable in General
371k1241 Goods or Property Involved
371k1241.1 In General.

(Formerly 371k1241, 238k19(3))

[See headnote text below]

[3] Taxation ⚷1245
371 ----
371XVI Sales, Use, Service, and Gross Receipts Taxes
371XVI(B) Tax Liability and Exemptions
371XVI(B)1 Transactions Taxable in General
371k1244 Purpose of Use or Consumption as Affecting Taxability
371k1245 Manufacturing or Processing, Use or Consumption In; Incorporation in New Product.

Fact that no sales tax is paid on newspapers does not necessarily mean that use tax is imposed on items which are used in processing of newspapers, if such items are exempt from such tax by provisions of state use tax law. NDCC 57-02-07, 57-39-01, subd. 2, 57-40-01, 57-40-02.

[4] Taxation ⚷1245
371 ----
371XVI Sales, Use, Service, and Gross Receipts Taxes
371XVI(B) Tax Liability and Exemptions
371XVI(B)1 Transactions Taxable in General
371k1244 Purpose of Use or Consumption as Affecting Taxability
371k1245 Manufacturing or Processing, Use or Consumption In; Incorporation in New Product.

(Formerly 238k15.1(10))

Newsprint and ink purchased by publisher of newspaper came within statutory definition of "property used in processing" which was tangible personal property that became component part of other tangible personal property intended to be sold at retail, and were exempt from payment of use tax under statute providing for imposition of use tax upon tangible personal property purchased for storage, use, or consumption. NDCC 57-02-07, 57-39-01, subd. 2, 57-40-01, 57-40-02.

*904 Syllabus by the Court

1. The newsprint and ink purchased by a publisher of a newspaper come within the definition of 'property used in processing,' and are exempt from payment of use tax under statutes now in effect in this State.

2. For reasons set forth in the opinion, the judgment of the district court is affirmed.

Wattam, Vogel, Vogel, Bright & Peterson, Fargo, and Shaft, Benson, Shaft & McConn, Grand Forks, for plaintiffs and respondents.

Helgi Johanneson, Atty. Gen., and Joseph R. Maichel and Kenneth M. Jakes, Sp. Asst. Attys. Gen., Bismarck, for defendant and appellant.

STRUTZ, Judge (On reassignment).

The plaintiffs are four newspaper publishers doing business within the State of North Dakota. They seek a declaratory judgment, adjudging that the purchase of newsprint in Canada and the purchase of ink in States outside the State of North Dakota, which newsprint and ink are used by them in the publication of their newspapers, are not subject to the North Dakota use tax. The defendant, on the other hand, asks that the plaintiffs be denied the relief demanded, and prays that the court adjudge that sales of newspapers, printed by the plaintiffs, be declared to be sales of a service, and not sales of tangible personal property, and that for that reason such sales are exempt from the North Dakota retail sales tax. The defendant contends that sales of the newsprint and the ink to the plaintiffs for use in their business of publishing newspapers are sales to the plaintiffs of tangible personal property, purchased at retail for storage, use, and consumption in this State, and that such sales are subject to the North Dakota use tax.

The issues involved on this appeal, briefly stated, are whether the sale of a newspaper to a customer constitutes a retail sale of tangible personal property within the meaning of the North Dakota sales and use tax statutes, or whether it is a sale of a service. If the sale of a newspaper to a customer constitutes a retail sale of tangible personal property, even though such sale is exempt from sales tax, then the sale of newsprint and ink to the plaintiffs for the purpose of printing and publishing newspapers would not be subject to the North Dakota use tax. If, however, the sale of a newspaper to a customer constitutes *905 sale of a service, and the sale of newsprint and ink constitutes a retail sale, such sale would be subject to the North Dakota use tax.

The plaintiffs raise the further question of whether the imposition of a use tax on newsprint purchased by the plaintiffs in Canada--if the sale of such newspaper is held to be a service--would violate Article I, Section 10, clause 2 of the United States Constitution, which prohibits the States, without the consent of the Congress, from laying any imposts or duties on imports or exports, except what may be absolutely necessary for executing its inspection laws.

The following are North Dakota statutes pertinent to the issues in this case:

Section 57--40--02, North Dakota Century Code, as amended, provides:

'An excise tax is imposed on the storage, use, or consumption in this state of tangible personal property purchased at retail for storage, use, or consumption in this state, at the rate of two and one-quarter percent of the purchase price of such property. * * *' (Chap. 399, 1963 S.L.)

The term 'use' is defined by our statute as follows:

'2. 'Use' shall mean the exercise by any person of any right or power over tangible personal property incident to the ownership or possession of that property, except that it shall not include processing, or the sale of that property in the regular course of business. * * *' (Sec. 57--40--01(2), N.D.C.C.)

'Property' is defined by our use tax statute as follows:

'3. Property use in 'processing', as that term is used in subsection 2, shall mean any tangible personal property including containers which it is intended, by means of fabrication, compounding, manufacturing, producing or germination, shall become an integral or an ingredient or component part of other tangible personal property intended to be sold ultimately at retail; * * *' (Sec. 57--40--01(3), N.D.C.C., as amended by Sec. 2 of Chap. 364, 1961 S.L.)

Our statutes define who are included in the term 'manufacturers.' Section 57--02--07 provides:

'Every person who purchases, receives, or holds personal property of any description for the purpose of adding to the value thereof by any process of manufacturing, refining, rectifying, or by the combination of different materials, with a view of making gain or profit by so doing, shall be held to be a manufacturer, * * *'

A 'sale' is defined as follows:

'2. 'Sale' means any transfer of title or possession, exchange or barter, conditional or otherwise, in any manner or by any means whatsoever, for a consideration, and includes the furnishing of services relating to personal property, the furnishing or service of steam, gas, electricity, water, or communication, the furnishing of hotel, motel, or tourist court accommodations, the furnishing of tickets or admissions to any place of amusement, athletic event or place of entertainment including the playing of any machine for amusement or entertainment in response to the use of a coin, and sales of subscriptions to magazines and other periodicals regardless of whether or not such magazines or periodicals are to be delivered in the future and regardless of whether or not they are in existence at the time of the sale of any subscription; provided that the words 'magazines and other periodicals' as used herein shall not include newspapers nor shall they include magazines or periodicals that are furnished free by a nonprofit corporation or organization ot its members or because of payment by its members of membership fees or dues; * * *' (Sec. 57--39--01(2), *906. N.D.C.C ., as amended by Chap. 399, 1963 S.L.)

[1] Thus our law provides that tangible personal property used in the business of manufacturing any article, which tangible personal property becomes an integral or component part of the personal property manufactured, compounded, or produced, is exempt from use tax.

[2] The question to be determined, therefore, is whether a newspaper, when printed, is tangible personal property or whether, as urged by the appellant, it is merely a service. Webster's Third International Dictionary defines 'personal property' as 'property other than real property consisting in general of things temporary or movable including intangible property.' Thus 'tangible' personal property would be personal property that can be touched or handled. The argument of appellant that a newspaper is a service is based, to a degree, on the fact that after it has been read it has no further value or use. That hardly seems to be a valid basis for determining the nature of the product resulting from the publication of a newspaper. If the fact that such product cannot be used after it has been read should be the determining factor, hundreds of items, such as paper towels, paper napkins, paper cups, and similar articles would have to be classed as services rather than personal property.

The Supreme Court of California has specifically held that newspapers are personal property. Bigsby v. Johnson (Cal.), 99 P.2d 268. See also State v. Advertiser Co., Inc., 257 Ala. 423, 59 So.2d 576, in which the court holds that a newspaper, when printed or published, is tangible personal property. Newspapers can be stolen, and clearly are tangible personal property.

[3] It is true that the definition of a 'sale' in the sales tax law specifically exempts newspapers from that tax. The fact that no sales tax is paid on newspapers does not necessarily mean that a use tax is imposed on the items which are used in the processing of the newspapers, if such items are exempt from such tax by the provisions of the use tax law. Are the newsprint and the ink tangible personal property used in the manufacture or production of other tangible property intended to be sold at retail, under Section 57--40--01(3), North Dakota Century Code, as amended? We believe it cannot be denied that the newsprint and the ink purchased by the plaintiffs are combined by the process of printing and publishing into tangible personal property, the newspaper. The newsprint and the ink become ingredient or component parts of the newspaper, the product produced.

[4] We hold, therefore, that newsprint and ink are ingredients and component parts of the tangible personal property produced, and thus come within the definition of 'property used in processing,' and exempt from use tax under the law above set forth.

The judgment of the district court is in all things affirmed.

TEIGEN, C.J., and ERICKSTAD and KNUDSON, JJ., concur.

MURRAY, J., not being a member of the Court at the time of submission of this case, did not participate.

Mary Loftsgard
HB 1471

North Dakota Filer: ______________________

Address: ______________________

F.E.I.N. ______________________

Income Year Ended: ______________________

North Dakota Domestic Disclosure Spreadsheet

Affiliated Corporations

North Dakota
Schedule DDS-1

(a) No.	(b) Name and Address of Corporation	(c) FEIN	(d) Percentage of Ownership	(e) Corporation Owner (From (a))	(f) Type of Corporation[1]	(g) Country of Incorporation[2]	(h) Primary Business Location(s) (Country)[2]	(i) Primary Business Activity(s)[2]	(j) Date of Acquisition[2]	(k) Date of Disposition[2]
1.	Common Parent Corporation									

I declare under the penalties of North Dakota Century Code § 12.1-11-02, which provides for a Class A misdemeanor for making a false statement in a governmental matter, that this spreadsheet, including any accompanying schedules and statements, has been examined by me and to the best of my knowledge and belief is true, correct, and complete.

Date: ______________ Signature of Officer: ______________________ Title: ______________________

28842 Date: ______________ Signature of Preparer: ______________________ Address: ______________________

[1] Type of Corporation: A = Foreign B = 80/20 C = DISC/FSC
D = Possessions Corporation
E = Domestic Corporation (United States)

[2] Exception: Required only for members of the water's edge group.

North Dakota Filer: ____________________

Income Year Ended: ____________________

This Schedule is being completed for: ____________________
(Corporation Name of the Water's Edge Member)

North Dakota Domestic Disclosure Spreadsheet

Summary Schedule Of State Tax Computations

North Dakota
Schedule DDS-2

Schedules DDS-2, 2A, 2B and 2C must be completed for <u>each member</u> of the water's edge group, and for each state where the member has a presence, <u>regardless</u> of whether or not that state assesses a tax according to or measured by income.

(a) State	(b) Filer Name[3]	(c) Filing Method[4]	(d) Net Income Before State Adjustments	(e) Net Income After State Adjustments	(f) Nonbusiness Income/Loss Allocated out of the State[5]	(g) Business Income[6]	(h) Apportionment Percentage[7]	(i) Nonbusiness Income/Loss Allocated to the State[8]	(j) State Income Total[9]	(k) State Tax Liability	(l) Destination Sales[10]

[3] Enter the Filer Name from Schedule DDS-2A, Column (b)
[4] Enter the Filing Method from Schedule DDS-2A, Column (c)
[5] Enter amount from Schedule DDS-2C, Column (d)
[6] Column (e) minus Column (f)
[7] Enter percentage from Schedule DDS-2B, Column (f)
[8] Enter amount from Schedule DDS-2C, Column (e)
[9] [Column (g) times Column (h)] plus Column (i)
[10] Enter amount from Schedule DDS-2C, Column (g)

North Dakota Filer: ______________________

Income Year Ended: ______________________

This Schedule is being completed for: ______________
(Corporation Name of the Water's Edge Member)

North Dakota
Schedule DDS-2A

North Dakota Domestic Disclosure Spreadsheet

State Reporting Methods

This Schedule must be completed for each member of the water's edge group.
A combined report is a return in which apportionable income includes more than one corporation.
A consolidated state return is one which reports the state tax liability of more than one corporation liable to file in that state.

(a) State	(b) Filer Name	(c) Filing Method[11]	(d) Corporations Included in the Combined Return[12]	(e) If Filing A State Consolidated Return, Corporation Names of Nexus Companies (Taxpayers) Included in the State Consolidated Return[12]

[11] Enter "S" (Separate Company) or a "C" (Combined). Subdesignations, such as "C1", "C2", "C3", etc., are necessary if there are multiple combined filings in one state or different filings between states. (For example: A line of business combination may be "C1" or a combination consisting of nexus companies may be "C2".)

[12] Enter the corporation names from Schedule DDS-1, Column (b) or number from Schedule DDS-1, Column (a).

North Dakota
Schedule DDS-2B

North Dakota Filer: ____________________

Income Year Ended: ____________________

North Dakota Domestic Disclosure Spreadsheet

Apportionment Percentage

This Schedule is being completed for: ____________
(Corporation Name of the Water's Edge Member)

This Schedule must be completed for each member of the water's edge group.
This Schedule supports column (h) of the Summary Schedule of State Tax Computations (Schedule DDS-2)
The apportionment percentage must be for the water's edge member that this Schedule is being completed for.

(a)	(b)	(c)			(d)			(e)			(f)
		Property			Payroll			Sales			
State	Filer Name (From Schedule DDS-2A)	Numerator	Denominator	Percentage	Numerator	Denominator	Percentage	Numerator	Denominator	Percentage	Apportionment Percentage

North Dakota Filer: ______________________

Income Year Ended: ______________________

This Schedule is being completed for: ______________
(Corporation Name of the Water's Edge Member)

North Dakota
Schedule DDS-2C

North Dakota Domestic Disclosure Spreadsheet

Nonbusiness Income/Loss And Destination Sales

This Schedule must be completed for each member of the water's edge group which allocates income or has destination sales in any state.
This Schedule supports column (f), (i) and (l) of the Summary Schedule of State Tax Computations (Schedule DDS-2).

(a) State	(b) Filer Name (From Schedule DDS-2A)	(c) Type of Nonbusiness Income/Loss	(d) Amount of Non-business Income/Loss Allocated out of the State in Column (a)	(e) Amount of Nonbusiness Income/Loss Allocated to the State in Column (a)	(f) State(s) in which Income/Loss is Treated as Business Income/Loss	(g) Amount of Destination Sales	(h) Are Sales in Column (g) Immune from Taxation Under P.L. 86-272? Yes	No

North Dakota Domestic Disclosure Spreadsheet

Instructions

Who Must File: A corporation electing to use the water's edge method must file a domestic disclosure spreadsheet if the affiliated corporations as a group have property, payroll or sales in foreign countries exceeding ten million dollars and assets everywhere exceeding two hundred fifty million dollars.

Time For Filing: The domestic disclosure spreadsheet must be filed by a corporation with its North Dakota income tax return in the initial year of the water's edge election and every third year thereafter while the election remains in effect.

Extension Of Time For Filing: If the information required to be reported on the domestic disclosure spreadsheet is not available when the return is filed, a corporation may file the domestic disclosure spreadsheet within six months after the due date of the return, including extensions. If the aforementioned time deadlines cannot be met, a corporation must submit a written request for an additional extension of time to the Office of State Tax Commissioner within six months after the due date of the return, including extensions. The Office of State Tax Commissioner will notify the corporation if the request for additional time is granted; however, this additional extension of time may not exceed one hundred twenty days from six months after the due date of the return, including extensions.

Where To File Or Obtain Additional Forms And Instructions: The completed domestic disclosure spreadsheet, written requests for additional forms and instructions, and written requests for extensions of time should be addressed to the Office of State Tax Commissioner, State Capitol, 600 E. Boulevard Ave., Bismarck, ND 58505-0599.

Additional forms and instructions may also be obtained by calling 701-328-2046.

Failure To File: The water's edge election is not complete until the completed domestic disclosure spreadsheet is filed with the Office of State Tax Commissioner.

Additional Information Regarding The Water's Edge Method And The Domestic Disclosure Spreadsheet Is Contained In North Dakota Century Code ch. 57-38.4 and North Dakota Administrative Code ch. 81-03-05.2.

TR

North Dakota Office of State Tax Commissioner

2002 Corporation Income Tax

Rick Clayburgh
Tax Commissioner

Mary Loftsgard
HB 1471

Form 40
Form 40-UT
Form 40-ES

Forms and Instructions

Need help? Visit our Web site at:

www. ndtaxdepartment. com

Download income and business tax forms anytime - day or night!

Get answers to your tax questions through our Frequently Asked Questions.

E-mail your tax questions:

corptax@state.nd.us

Check it out today!

ndTax

As you prepare your North Dakota corporation income tax return, please consider the following:

- *Who Must File* Corporations engaged in business in North Dakota or having sources of income from North Dakota must file a North Dakota Corporation Income Tax Return, Form 40.

  A corporation which files a Federal Form 1120S as a small business corporation must file a North Dakota Small Business Corporation Income Tax Return, Form 60.

  Financial institutions *(See North Dakota Century Code ch. 57-35.3)* located or doing business within North Dakota must file a North Dakota Financial Institution Tax Return, Form 35.

Please remove label and attach it to your return

North Dakota Office of State Tax Commissioner
2002 Form 40-UT

Name as shown on return ______________________ Federal employer I.D. __-_______

derpayment of estimated North Dakota income tax by corporations

For the tax year beginning ____________ , ______ and ending ____________ _ ______ .

If a corporation's estimated income tax payment for any quarter (including overpayment credits from prior quarters) is less than 90% of the quarterly income tax liability or is less than the prior year's North Dakota income tax liability divided by four, it will be required to complete Form 40-UT and attach it to the North Dakota Corporation Income Tax Form 40 when filing.

1 Net income tax liability - From 2002, Form 40, ***(If $5,000 or less, do not complete form)*** ______

2 90% of line 1 ______

3 Prior year's net income tax liability - From 2001 Form 40, line 19 ***(If $5,000 or less, do not complete form)*** ______

	A	B	C	D
Enter in columns A through D the installment dates that correspond to the 15th day of the 4th, 6th and 9th months of the taxable year, and the first month of the following year				
4 Enter 25% of line 2 or line 3, whichever is less, in column A through D				
5 (a) 2001 overpayment credited to 2002 tax				
(b) Amount paid for each quarter				
(c) Overpayments. See line 7(b)	**Remaining lines for Column A must be completed before proceeding to Column B, C and D.**			
6 Add lines 5(a), 5(b), and 5(c)				
7 (a) Underpayment. *(line 4 less line 6)* If underpayment computed, see line 11 below.				
(b) Overpayment. *(line 6 less line 4)* Enter here and on line 5(c) above, in the following quarter				
8 Interest *(See Form 40-ES instruction)*				

9 Total interest *(Add line 8, columns A-D. Enter on 2002 Form 40, on line 21a)* ______

10 ☐ Check this box if the computed underpayment results from recurring seasonal income, as defined under IRC Section 6655(e) of 1986, as amended.

11 ☐ Check this box if the computed underpayment results from using the federal annualization method.

If either Box 10 or 11 is checked, interest on the underpayment(s) should not be computed or paid. Attach a copy of Federal Form 2220 *(including the worksheet in the instructions to Federal Form 2220)*.

North Dakota estimated income tax for corporations for the 2003 taxable year

General Instructions

Who must pay estimated tax

Estimated income tax must be paid if a corporation's net income tax liability can reasonably be expected to exceed five thousand dollars ($5,000) for the taxable year and the previous year's income tax liability exceeded five thousand dollars ($5,000).

"Net tax liability" is defined as North Dakota income tax due, as shown on the return, computed after the application of allowable credits and before the application of estimated income tax payments.

Where to file

Estimated income tax payments should be mailed to the Office of State Tax Commissioner, 600 East Boulevard Ave., Dept. 127, Bismarck, ND 58505-0599.

Which form to use

If payment for estimated income tax is to be made by check or money order, the Form 40-ES voucher must be used to ensure that proper credit for the payment is applied to the correct account.

If payment is to be made using the Automated Clearing House (ACH) credit procedures, do not use the Form 40-ES voucher.

Time for filing

The first estimated income tax payment is due no later than April 15 following the close of the calendar year.

Corporations reporting on a fiscal year basis must pay the first estimated tax installment no later than the 15th day of the fourth month following the close of their fiscal year.

No less than one fourth of the estimated income tax must be paid with the first installment, and with each of the three remaining installments on the 15th day of the sixth and ninth months of the taxable year, and the first month of the following year.

Extension of time to pay estimated tax cannot be granted.

How to pay

Do not commingle estimated income tax payments with any other payment to the North Dakota Office of State Tax Commissioner.

If payment for estimated income tax is to be made by check or money order, make it payable to North Dakota State Tax Commissioner.

Payment for estimated income tax may be made by electronic funds transfer. Information regarding electronic payments can be found on the department's Web site at www.ndtaxdepartment.com, under Corporate Income, Electronic Filing.

Amendments to estimated income tax

If it is found that the total estimated income tax is more or less than originally determined, amend the next installment.

Overpayment of estimated tax

An overpayment of estimated income tax from the prior taxable year may be credited to the current year's estimated payments. The amount of the 2002 overpayment will be applied to the first installment for 2003, unless the corporation elects another installment on Form 40, page 1, line 22a.

Application of estimated income tax payments

All payments submitted as 2002 estimated income tax and any overpayment credited from the 2001 taxable year must be reported on the 2002 North Dakota Corporation Income Tax Return Form 40.

Understatement of estimated income tax

Except for income computed using the federal annualization method or income qualifying as recurring seasonal income, interest charges will apply if the estimated income tax payment for any quarter *(including overpayment credits from prior quarters)* is less than 90% of the quarterly income tax liability or is less than the prior year's North Dakota income tax liability divided by four.

The Underpayment of Estimated North Dakota Income Tax by Corporations Form 40-UT must be attached to the North Dakota Corporation Income Tax Return, Form 40 when filing. The Form 40-UT is located within the Form 40 booklet.

Interest

The State Tax Commissioner will notify the taxpayer of any interest owed on any underpayment of estimated income tax. If desired, interest owed may be computed by the taxpayer on Form 40-UT and added to the 2002 corporation income tax liability on Form 40, Page 1. Interest is calculated at the rate of 12% per year from the installment due date to the earlier of the date the estimated tax is paid or the due date (without extension) of the return.

Exceptions

If the estimated tax paid on or before each due date is computed using the annualization method provided in the Internal Revenue Code of 1986, as amended, no interest is due. Also, no interest is due if the underpayment of any installment comes within the exception provided in the Internal Revenue Code of 1986, as amended, Section 6655(e) for income qualifying as recurring seasonal income.

Form **40-ES**

North Dakota Office of State Tax Commissioner

Estimated tax payment voucher — corporation

2003
1st Installment
Due 15th day of fourth month of 2003 taxable year.

☐ Calendar year: January 1 through December 31, 2003

☐ Fiscal year beginning ____________, 2003, and ending ____________, ______

FEIN ☐☐ - ☐☐☐☐☐☐☐

Name as shown on North Dakota corporation income tax return

Mailing address

Amount of Payment $ ☐,☐☐☐,☐☐☐

For Tax Department use only

City, state and zip code

- **Do not use this voucher if paying by means of an Automated Clearing House (ACH) credit.**
- Make check or money order payable to "North Dakota State Tax Commissioner"
- Mail to: Office of State Tax Commissioner, 600 E. Boulevard Ave., Dept. 127, Bismarck, ND 58505-0599

Form North Dakota Office of State Tax Commissioner

40 L01 Corporation income tax return 2002

Check One: ☐ Calendar Year January 1, 2002, through December 31, 2002

☐ Fiscal Year beginning ________, 2002 and ending ________

	Please Use Mailing Label (If none, type or print)	
Is an extension attached? Yes ☐ No ☐	Name	Federal employer identification no. ☐☐-☐☐☐☐☐☐☐
Date of incorporation __/__/____	Mailing address	Is this a farming or ranching corporation? Yes ☐ No ☐
Final return Yes ☐ No ☐	City, State, Zip Code / Phone number	Business code (from federal return) ☐☐☐☐☐☐

Computation of tax liability

Round off to dollars

1 Income from *(See instructions on page 3 before checking appropriate box)*:
a. ☐ Single Corporate Entity b. ☐ Combined Report Method b1. ☐ 100% North Dakota Consolidated Return b2. ☐ Apportioning Corp Consolidated Return c. ☐ Water's Edge Method d. ☐ Other — (LA) 1 ________

2 Total additions *(Enter amount from Schedule SA, line 7)* — (LB) 2 ________

3 Total subtractions *(Enter amount from Schedule SA, line 17)* — (LC) 3 ________

4 North Dakota apportionable income *(Subtract line 3 from the sum of lines 1 and 2 - See instr. on page 3)* — 4 ________

5 Apportionment Factor *(See instructions on page 3)* — (LE) 5 ________

6 Income apportioned to North Dakota *(line 4 multiplied by line 5)* — 6 ________

7 Income allocated to North Dakota ________ less related expenses ________ — (LF) 7 ________

8 North Dakota income *(Add lines 6 and 7)* — (LG) 8 ________

9 Federal tax deduction *(See instructions on page 4)* — (AJ) 9 ________

10 Exemption for new and expanding business *(See instructions on page 4)* — (CL) 10 ________

11 Renaissance zone income exemption *(See instructions on page 4)* — (RE) 11 ________

12 ND income after federal tax deduction and income exemptions *(Subtract lns. 9, 10 and 11 from ln. 8)*

If the amount on line 12 is a loss, to forego the carryback period, check the box in Question 10, page 2 — 12 ________

13 North Dakota loss carryforward *(Attach worksheet - See instructions on page 4)* — (LH) 13 ________

14 Balance *(Subtract line 13 from line 12)* — 14 ________

15 Recapture of federal alternative minimum tax *(See instructions on page 4)* — (AN) 15 ________

16 North Dakota taxable income *(Subtract line 15 from line 14)* — (LI) 16 ________

17 Income tax due *(See rates below) (Corp. filing a consol. return, enter amt. from Sch. CR, part I, ln. 17a)* — (LJ) 17 ________

Tax credits

18 Tax credits *(Enter amount from Schedule TC, line 11)* — (AZ) 18 ________

Balance due or overpayment

19 Net income tax liability *(Subtract line 18 from line 17)* — 19 ________

20 2002 Estimated income tax payments and payment with extension *(See instructions on page 4)* — (LN) 20 ________

21 **If line 19 is greater than line 20, enter difference as BALANCE DUE (Enter $0 if less than $5)** — (LR) 21 ________

a. Interest and penalty for Balance Due on line 21 *(See instructions on page 4)* — (LQ) 21a ________

b. Total **Payment Due** *(Add lines 21 and 21a - Pay to North Dakota State Tax Commissioner)* — 21b ________

If payment is to be made by Electronic Funds Transfer, check this box ☐ and enter date of payment ________.

22 **If line 20 is greater than line 19, enter difference as OVERPAYMENT** *(Enter $0 if less than $5)* — (LV) 22 ________

a. Amt. of line 22 to be credited to 2003 est. tax *(Min. $5) (Apply to quarter 1st 2nd 3rd 4th)* — (AI) 22a ________

b. Amount of line 22 to be **Refunded** *(Subtract line 22a from line 22 No refund under $5)* — 22b ________

I declare under the penalties of North Dakota Century Code § 12.1-11-02, which provides for a Class A misdemeanor for making a false statement in a governmental matter, that this return, including any accompanying schedules and statements, has been examined by me and to the best of my knowledge and belief is a true, correct, and complete return.

Date: ________ Signature of Officer: ________ Title: ________

Date: ________ Signature of Preparer: ________ Address: ________

Mail to: Office of State Tax Commissioner, 600 E. Boulevard Ave., Dept. 127, Bismarck, North Dakota 58505-0599

Tax Rate Table

If the amount on Line 16 is not over $3,000		3%	
$ 3,000 to $ 8,000	$ 90.00 plus	4.50% of excess over	$ 3,000
$ 8,000 to $20,000	$ 315.00 plus	6.00% of excess over	$ 8,000
$20,000 to $30,000	$1,035.00 plus	7.50% of excess over	$20,000
$30,000 to $50,000	$1,785.00 plus	9.00% of excess over	$30,000
Over $50,000	$3,585.00 plus	10.50% of excess over	$50,000

"Buy North Dakota Products"

PLEASE DO NOT WRITE IN THIS SPACE

North Dakota Office of State Tax Commissioner
2002 Form 40, page 2

Name as shown on return

Federal employer I.D. __ - _______

Schedule FACT: Apportionment factor for nonfinancial corporations not filing a consolidated state return

(If filing a consolidated N.D. return, use Schedule CR, part II. Do not use this schedule.)

Property Factor - Average value at original cost of real and tangible personal property used in the business *(Exclude value of construction in progress)*		1. Total	2. North Dakota	3. Factor
1 Inventories	1			*(Use 6-digit decimal only)*
2 Buildings and other fixed depreciable assets	2			
3 Depletable assets	3			*(Column 2 divided by Column 1 = Column 3)*
4 Land	4			
5 Other assets *(Detail)*	5			
6 Rented property *(Annual rental capitalized x 8)*	6			
7 Total Property *(Add lines 1 through 6)*	7		(BA)	(BB)
Payroll Factor:				
8 Wages, salaries, commissions and other compensation of employees which were included in the Federal Form 1120, or Federal Form 1120-A. *(If the amount reported in Column (2) does not agree with the total compensation reported for North Dakota unemployment insurance purposes, attach an explanation)*	8		(BC)	(BD)
Sales Factor:				
9 Gross receipts or sales, less returns and allowances *(Federal Form 1120 or Federal Form 1120-A, line 1c)*	9			
10 Sales delivered or shipped to North Dakota destinations			10	
11 Sales shipped from North Dakota to:				
(a) The United States Government			11a	
(b) Purchasers in a state or foreign country where the taxpayer was not subject to a net income tax or a tax measured by net income or, if subject, did not actually pay such tax			11b	
12 Total sales *(Add lines 9 through 11)*	12		(BE)	(BF)
13 Sum of factors *(Add lines 7, 8 and 12)*				13
14 Divide line 13 by the number of factors having an amount greater than zero in column 1, on lines 7, 8 and 12				14 (BG)

The following questions must be answered

			Yes	No
1	Has the IRS issued a Final Determination which affects any previously filed North Dakota return?	➤ 1		
2	If the answer to the above question is yes, have all such adjustments been reported to North Dakota?	➤ 2		
3	Has Form 1120S been filed for federal purposes? If yes, file North Dakota Form 60, not a North Dakota Form 40	➤ 3		
4	Is this return for a tax-exempt organization required to report unrelated business taxable income?	➤ 4		
5	Has this corporation filed as a cooperative, a Foreign Sales Corporation, or a Domestic International Sales Corporation for federal purposes?	➤ 5		
6	Does this corporation use the combined report method in any other states? If yes, attach a worksheet showing all states where the combined report method is used	➤ 6		
7	Does this corporation file its federal income tax return as a member of a consolidated group? If yes, please enter the Federal Employer I.D. No. under which the consolidated return is filed. (AM) __ - _______	➤ 7		
8	Does the numerator of the apportionment factor include the property, payroll or sales of more than one corporation required to file in this state? If yes, Schedule CR must be completed and attached to the return	➤ 8		
9	Is this a limited liability company?	➤ 9		
10	If this corporation has a loss on Form 40, line 12, and is electing to forego the carryback period, check the box. **Failure to check the box requires the loss to be carried back.**	➤10 ☐		
11	Is this a Renaissance Fund Organization for purposes of N.D.C.C. ch. 40-63, Renaissance Zones?	➤11		
12	Has this corporation changed names, been involved in a merger, reorganization or takeover during this tax year? If so provide former name and details of change.	(former name)		

Name as shown on return | Federal employer I.D. [ ][ ]-[ ][ ][ ][ ][ ][ ][ ]

chedule SA: Statutory adjustments

(See tax booklet for instructions)

Additions

1	Federal net operating loss deduction *(Federal Form 1120, line 29a or Federal Form 1120-A, line 25a)*	(CA)	1
2	Special deductions *(Federal Form 1120, line 29b or Federal Form 1120-A, line 25b)*	(CB)	2
3	All income taxes, franchise or privilege taxes measured by income, which were deducted to determine federal taxable income *(See instructions on page 4)*	(CC)	3
4	North Dakota depreciation adjustment *(See instructions on page 4)*	(CE)	4
5	Interest on state and local obligations *(Excluding North Dakota obligations)*	(CF)	5
6	Other additions *(Attach worksheet - See instructions on page 5)*	(CG)	6
7	Total additions (Add lines 1 through 6. Enter amount here and on page 1, line 2)		7

Subtractions

8	Tax refunds received in 2002 *(Attach worksheet - See instructions on page 5)*	(CH)	8
9	Interest on United States obligations	(CI)	9
10	North Dakota depreciation adjustment *(See instructions on page 5)*	(CJ)	10
11	Allocable income *(Attach worksheet - See instructions on page 5)*	(LS)	11
12	Related expenses *(Attach worksheet - See instructions on page 5)*	(LT)	12
13	Balance *(Subtract line 12 from line 11)*	(LD)	13
14	Interest on bonds issued by a regional railway authority in North Dakota	(CM)	14
15	North Dakota domestic dividend exclusion *(See instructions on page 5)*	(CN)	15
16	Other subtractions *(Attach worksheet - See instructions on page 5)*	(CO)	16
17	Total subtractions *(Add lines 8, 9, 10, 13, 14, 15, and 16. Enter amount here and on page 1, line 3)*		17

chedule FTD: Federal income tax deduction

omplete lines 1-8 of Form 40, page 1 before completing this schedule)
ee tax booklet for instructions)
(Corporations filing a consolidated North Dakota return, use Schedule CR, part III. Do not complete this schedule.)

(Use 6-digit decimal only)

1	Federal income tax liability *(See instructions on page 5)*	(EA)	1
1a	Federal alternative minimum tax liability *(See instructions on page 6)*	(EG)	1a
1b	Adjusted federal income tax liability *(Subtract line 1a from line 1)*		1b
2	Separate company(ies) federal income tax liability *(Attach worksheet - See instructions on page 6)*		2
3	Profit companies federal income tax liability *(Attach worksheet - See instructions on page 6)*		3
4	Ratio: (Divide line 2 by line 3. Not to exceed 1.000000)		4 _.______
5	Separate company(ies) share of federal income tax liability *(Multiply line 1b by line 4)*	(EB)	5
6	Federal taxable income *(Attach worksheet - See instructions on page 6)*		6
7	Income not taxable to North Dakota *(See instructions on page 6)*		7
8	Balance *(Subtract line 7 from line 6)*		8
9	Ratio: *(Divide line 8 by line 6. Not to exceed 1.000000)*		9 _.______
10	Federal tax on federal taxable income reportable to North Dakota: *(Multiply line 5 by line 9)*	(CK)	10

Corporations using the combined report method and claiming a federal foreign tax credit skip line 11 and use lines 12 - 16. Other corporations must use line 11.

11	ND apportionment factor *(Enter amount from page 1, line 5 and go to line 17 - See instr. on page 6)*		11 _.______
12	North Dakota income *(Enter amount from page 1, line 8)* *(If zero or less, skip lines 13 through 16)*		12
13	Total income *(See instructions on page 6)* *(If zero or less, skip lines 14 through 16)*		13
14	Income relating to Foreign Tax Credit *(See instructions on page 7)* *(If zero, skip lines 15 and 16)*		14
15	Income relating to federal income tax paid *(Subtract line 14 from line 13)* *(If zero or less, skip line 16)*		15
16	Federal income tax ratio *(Divide line 12 by line 15 and go to line 17. Not to exceed 1.000000)*	(EC)	16 _.______
17	Federal tax deduction *(Multiply line 10 by either line 11 or line 16. Enter amount here and on page 1, line 9)*	(ED)	17

Complete line 11 - or line 16 - but not both.

Name as shown on return ____________________ Federal employer I.D. __-_______

Schedule AMT-R: Recapture and carryforward of federal alternative minimum tax

(Use 6-digit decimal only)

(See tax booklet for instructions) (Corporations filing a consolidated North Dakota return, use Schedule CR, part IV. Do not complete this schedule.)

1	2002 Federal alternative minimum tax *(Enter amount from Form 40, Schedule FTD, line 1a)*	1 ______
2	Ratio from Form 40, Schedule FTD, line 4, if no ratio on line 4, enter 1.000000	2 ______
3	Multiply line 1 by line 2	3 ______
4	Ratio from Form 40, Schedule FTD, line 9	4 ______
5	Multiply line 3 by line 4	5 ______
6	Ratio from Form 40, Schedule FTD, line 11, or Form 40, Schedule FTD, line 16, whichever is applicable	6 ______
7	Multiply line 5 by line 6	7 ______
8	Carryforward of federal AMT disallowed *(Enter amount from 2001 Form 40, Schedule AMT-R, line 12)*	8 ______
9	Total federal AMT disallowed *(Add lines 7 and 8)*	9 ______

Corporations claiming a federal credit for prior year minimum tax on the 2002 federal return complete lines 10-12. Other corporations enter the amount from line 9 on line 12.

10	Enter the amount from the 2002 Form 40, page 1, line 14	10 ______
11	If line 10 is zero or less enter zero here and on the 2002 Form 40, page 1, line 15, otherwise, enter the smaller of line 9 or line 10 here and on the 2002 Form 40, page 1, line 15	11 ______
12	Available carryforward of federal AMT disallowed *(Subtract line 11 from line 9 if completing lines 10 and 11)*	(RA) 12 ______

Schedule TC: Tax credits

(See tax booklet for instructions - attach complete documentation)

1	Credit for contributions to nonprofit private colleges *(See instructions on page 7)*	(LK) 1 ______
2	Credit for contributions to nonprofit private high schools *(See instructions on page 7)*	(LL) 2 ______
3	Venture capital corporation credit *(See instructions on page 7)*	(LU) 3 ______
4	North Dakota Small Business Investment Company *(See instructions on page 7)*	(LW) 4 ______
5	Geothermal, solar or wind energy device tax credit *(Attach worksheet - See instructions on page 7)*	(LM) 5 ______
6	Credit for employment of the developmentally disabled or chronically mentally ill *(See instructions on page 8)*	(LX) 6 ______
7	Credit for research and experimental expenditures within North Dakota *(See instructions on page 8)*	(LY) 7 ______
8	Tax credit for new industry *(Attach worksheet - See instructions on page 8)*	(AK) 8 ______
9	Credit for payment to a certified nonprofit development corporation *(See instructions on page 8)*	(AG) 9 ______
10	Renaissance zone tax credit(s) *(Enter amount from Schedule RZ)*	(RC) 10 ______
11	Total tax credits *(Add lines 1 through 10. Enter amount here and on page 1, line 18)*	11 ______

Schedule FACT-1: Apportionment factor for financial organizations

(Financial Institutions as defined in North Dakota Century Code ch. 57-35.3 must not use Form 40, or this schedule.) (Financial Institutions must file North Dakota Form 35.)

	1. Total	2. North Dakota	3. Factor *(Column 2 divided by Column 1 = Column 3)*
Property Factor: *(Average value at original cost)*			
1 Tangible property held and owned for business use	1 ______	(AA) ______	(AB) ______
Business Factor:			*(Use 6-digit decimal only)*
2 Wages and salaries paid for services performed	2 ______	______	
3 Receipts from sales and other business sources as defined in N.D.C.C. § 57-38-13(6)	3 ______	______	
4 Total *(Add lines 2 and 3)*	4 ______	(AC) ______	(AD) ______
5 Sum of North Dakota property and business factors *(Add lines 1 and 4)*			5 ______
6 One-Half of line 5 *(Enter factor here and on page 1, line 5)*			(AE) 6 ______

North Dakota Office of State Tax Commissioner

2002 Form 40, page 5

Name as shown on return

Federal employer I.D.

See specific line instruction for lines 1, 5, 6, 8, and 9.

:hedule WW: Combined report method income schedule

1	Federal taxable income *(consolidated Federal Form 1120, line 30)*	(LA) 1	
2	Taxable income or loss included on line 1 from nonunitary corporations *(Attach worksheet)*	(WN) 2	
3	Balance *(Subtract line 2 from line 1)*		3
4	Taxable income or loss not included on line 1 from unitary corporations required to file a federal income tax return *(Attach worksheet)*		(WU) 4
5	Book income before income taxes of unitary foreign corporations *(Attach worksheet)*	5	
6	Optional: Book to tax reconciliation *(Attach worksheet)*	6	
7	Subtotal (Add lines 5 and 6)		(WF) 7
8	Income or loss from Interest Charge DISC *(Attach worksheet)*	8	
9	Income or loss from Foreign Sales Corporations *(Attach worksheet)*	9	
10	Subtotal *(Add lines 8 and 9)*		10
11	Income or loss from Internal Revenue Code of 1986, as amended, Section 936 Possession Corporations		11
12	Intercompany eliminations for members of the unitary group *(Attach worksheet)*		12
13	Total income *(Add lines 3, 4, 7, 10 and 11 then subtract line 12. Enter amount here and on Form 40, page 1, line 1, and check the appropriate box on Form 40, page 1, line 1)*		(WW) 13

Combined report method instructions

An apportioning corporation, see method of corporation taxation on page 2 of General Instructions, which is a member of a unitary group but has not elected the water's edge method is required to file its North Dakota income tax return using the combined report method.

A "unitary group" is a group of affiliated corporations engaged in a unitary business, irrespective of the country or counties in which the corporations conduct business activity.

An "affiliated corporation" means a parent corporation and any corporation of which more than fifty percent of the voting stock is owned directly or indirectly by the parent corporation or another member of the unitary group.

Two or more 100% North Dakota corporations affiliated as parent and subsidiary, and filing a consolidated federal tax return must file one consolidated North Dakota return using the "combined report method."

A corporation filing its North Dakota income tax return using the combined report method must include only the apportionment factors and statutory adjustments of the group.

Corporations completing Schedule CR must also complete Schedule WW to arrive at "total income."

Schedule WW specific line instructions

Line 1. Enter the amount from line 30 of the consolidated Federal Form 1120. If more than one consolidated federal return is filed, enter the total of lines 30 of the consolidated Federal Form 1120's. If a consolidated federal return is not filed, enter zero on lines 1 and 2 then proceed to line 4.

Line 5. Enter the amount of book income before income taxes of all unitary foreign corporations not eligible to be included in the consolidated federal income tax return or not required to file a federal income tax return.

Line 6. North Dakota Admin. Code 81-03-05.3 provides a choice either to adjust or not adjust the book income of all unitary foreign corporations to conform with the Internal Revenue Code of 1986, as amended. If a corporation chooses to make the book to tax adjustments, the adjustments must be made for all unitary foreign corporations and the total of such adjustments must be entered on line 6. If a corporation chooses not to make the book to tax adjustments, enter $0 on line 6.

Lines 8 and 9. Enter all exempt and nonexempt income before income taxes from the Federal Form 1120-IC-DISC or Federal Form 1120-FSC.

Additional Information Regarding The Combined Report Method Is Contained In N.D. Admin. Code ch. 81-03-05.3

North Dakota Office of State Tax Commissioner

2002 Form 40, page 6

Name(s) shown on return | Federal employer ID

Schedule WE: Water's edge method income schedule

1	Federal taxable income *(consolidated Federal Form 1120, line 30)*	(LA) 1	
2	Income or loss not included in line 1 from affiliated corporations required to file a federal income tax return	2	
3	Reversal of intercompany eliminations between water's edge corporations and non water's edge corporations *(Attach worksheet - See instructions below)*	3	
4	Intercompany eliminations for water's edge group corporations	4	
5	Total foreign dividends included in line 1	5	
6	Taxable income or loss included in line 1 or 2 from 80/20 corps.	6	
7	Balance (Add lines 1, 2 and 3 then subtract lines 4, 5 and 6)		7
8	Foreign dividends to be included in water's edge income *(Multiply line 5 by 30%) (See general definitions and enter amount on line 8)*		8
9	Total net book income of 80/20 corporations *(Attach worksheet)*	9	
10	Net book income of 80/20 corporations to be included in water's edge income *(Multiply line 9 by 30%)*		10
11	Total water's edge income *(Add lines 7, 8 and 10. Enter amount here and on page 1, line 1 and check the box entitled "Water's Edge Method.")*		(WE) 11

Worksheets containing totals of lines 3 and 9 are required

Water's edge method election instructions

A corporation required to file its North Dakota return using the worldwide unitary combined report method must do so unless it elects to apportion its income using the water's edge method.

A corporation elects and maintains the water's edge method election by checking the box entitled "Water's Edge Method" on page 1, line 1, and completing Schedule WE.

A corporation electing the water's edge method must comply with all of the following:

- The election must be made on the return as originally and timely filed;
- The corporation may not reduce taxable income for federal taxes deducted under N.D.C.C. 57-38-01.3(1)(c);
- The water's edge election is binding for five consecutive taxable years upon making the election; and
- The corporation must file with the Tax Commissioner a domestic disclosure spreadsheet if the first year the property, payroll, or sales in foreign countries exceed ten million dollars and total assets exceed two hundred fifty million dollars, and every third year thereafter provided the property, payroll, or sales in foreign countries exceed ten million dollars and total assets exceed two hundred fifty million dollars. The domestic disclosure spreadsheet must be filed by a corporation with its North Dakota income tax return. However, if the information is not available when the return is filed, a corporation may file the spreadsheet within six months after the due date of the return, including any extensions. The form for complying with the spreadsheet requirement must be obtained from the Office of State Tax Commissioner.

A corporation electing the water's edge method must include only the apportionment factors and statutory adjustments of the water's edge group.

Schedule WE general definitions

"Water's edge group" includes affiliated corporations incorporated in the U.S., excluding 80/20 corporations, affiliated corporations incorporated in a possession of the U.S., DISCs, FSCs, export trade corporations and foreign affiliated corporations which meet a defined minimum of U.S. activity.

"Affiliated corporation" means a parent corporation and any corporation of which more than fifty percent of the voting stock is owned directly or indirectly by the parent corporation or another member of the water's edge group.

"Reversal of intercompany eliminations between water's edge corporations and 80/20 corporations" means the reversal of eliminations made between water's edge corporations and 80/20 corporations that are included in the federal consolidated return. Dividends, interest, royalties, capital gains and losses, intercompany profit on sales, etc. between water's edge corporations and 80/20 corporations that have been eliminated in preparing the consolidated federal return must be reversed.

"Intercompany eliminations for water's edge group corporations" are eliminations of intercompany transactions between companies included in line 1 and companies included in line 2.

"80/20 corporation" is a corporation that is incorporated in the U.S., is eligible to be included in the federal consolidated return as defined in N.D.C.C. § 57-38.4-01(5) and has eighty percent of its average property and payroll assigned to locations in foreign countries.

"Foreign dividends" means any dividend received by a member of the water's edge group from any affiliated corporation incorporated outside the fifty states and District of Columbia, including amounts included in income computed under sections 951 through 954 of the Internal Revenue Code of 1986, as amended.

"Net book income of an 80/20 corporation" means net book income for financial statement purposes. However, a corporation's net book income cannot be offset by a net book loss from another 80/20 corporation.

"Rescission of a water's edge election". A corporation's water's edge election is rescinded if:

- It has had more than 50% of its voting stock acquired by a nonaffiliated corporation;
- It was formed as the result of a reorganization or spinoff and is no longer a member of the water's edge group; or
- It is completely liquidated. The water's edge election of any corporation receiving liquidated assets is not affected.

Additional Information Regarding The Water's Edge Method Is Contained In N.D.C.C. ch. 57-38.4 and N.D. Admin. Code ch. 81-03-05.2

North Dakota Office of State Tax Commissioner
2002 Form 40, page 7

Name as shown on return | Federal employer I.D.

Schedule CR, Part I: Computation of tax due for corporations filing a North Dakota consolidated return using the combined report method

	Corporation	Name of corporation	Federal Employer I.D.
Corporations having activity within North Dakota	A	➤ ______	➤ __-_______
	B	➤ ______	➤ __-_______
	C	➤ ______	➤ __-_______

Before starting part I of this schedule, complete lines 1-4 on Form 40, page 1

		Corporation A	Corporation B	Corporation C
4 North Dakota apportionable income *(Enter amount in Columns A, B & C from Form 40, page 1, line 4)*	4			
5 Apportionment factor *(Enter factor from part II, line 14)*	5			
6 Income apportioned to North Dakota *(line 4 multiplied by line 5)*	6			
7 Income allocated to North Dakota $ ______ less related expenses $ ______	7			
8 North Dakota income *(Add lines 6 and 7)*	8			
9 Federal tax deduction *(Enter amount from part III, line 17)*	9			
10 Exemption for new and expanding business *(Attach worksheet - See instructions on page 4)*	10			
11 Renaissance zone income exemption *(See instructions on page 4)*	11			
12 North Dakota income after federal tax deduction and income exemptions *(Subtract lines 9, 10 and 11 from line 8)*	12			

If the amounts on line 12 are losses, to forego the carryback period, check the box in Question 10, on Form 40, page 2

		Corporation A	Corporation B	Corporation C
13 North Dakota loss carryforward *(Attach worksheet - See instructions on page 4)*	13			
14 Balance *(Subtract line 13 from line 12)*	14			
15 Recapture of federal alternative minimum tax *(Enter amount from part IV, line 11)*	15			
16 North Dakota taxable income *(Subtract line 15 from line 14)*	16			
17 Income Tax Due *(See tax rate table on Form 40, page 1)*	17			

17a Total income tax due (Add amounts on line 17, Columns A, B & C, and enter the total amount here and on Form 40, page 1, line 17 and complete lines 18 through 22, on Form 40) **(GA) 17a** ______

Instructions for consolidated return using the combined report method

All corporations filing a consolidated North Dakota return, *(i.e. those corporations checking either box b1 or b2 on Form 40, page 1, line 1)* must complete the four parts of Schedule CR and attach the completed schedule to Form 40 when filed.

On the top of this page, space has been provided for three corporations (corporations A, B & C) having activity within North Dakota. If space is needed for additional corporations having activity within North Dakota, additional copies of Schedule CR can be obtained by photocopying all four parts of this original schedule or by requesting additional copies from the Office of State Tax Commissioner.

Complete Form 40, page 1, lines 1-4 before starting to complete Schedule CR, part I.

Schedule CR has been designed so the instructions for Form 40 in the booklet also apply to the line numbers on Schedule CR. For example, the instructions for Form 40, page 1, lines 4-17 also apply to Schedule CR, part I, lines 4-17.

After completing Schedule CR, part I, certain totals must be entered on Form 40. For each line 7, 9, 10, 11, 13 and 15, total the amounts for all corporations included on Schedule CR, part I. Enter the total from lines 7 onto line 7 of Form 40, page 1; enter the total from lines 9 onto line 9 of Form 40, page 1; enter the totals from lines 10 onto line 10 of Form 40, page 1; enter the total from lines 11 onto line 11 of Form 40, page 1; enter the total from lines 13 onto line 13 of Form 40, page 1; and enter the total from lines 15 onto line 15 of Form 40, page 1.

North Dakota Office of State Tax Commissioner
2002 Form 40, page 8

Name as shown on return | Federal employer I.D.

Schedule CR, Part II: Computation of factor for corporations filing a North Dakota consolidated return using the combined report method

(Property Factor:
Average value at original cost of real and tangible personal property used in the business. *(Exclude Value of construction in progress)*

(Use 6-digit decimal only)

Average Property:	Everywhere Average Property of All Corporations Being Combined	North Dakota Average Property — Corporation A	Corporation B	Corporation C
1 Inventories	1			
2 Buildings and other depreciable assets	2			
3 Depletable assets	3			
4 Land	4			
5 Other assets	5			
6 Rented property *(annual rental capitalized x 8)*	6			
7 Total average property *(Add lines 1 through 6)*	7			
7a Property factor *(Divide N.D. Total Average Property by Total Everywhere Average Property)*	7a			
7b Total property factor *(Add amounts on line 7a, columns A, B & C)*			(BB) 7b	

Payroll Factor:
Wages, salaries, commissions and other compensation of employees which were included in the Federal Form 1120 or Federal Form 1120-A.

	Everywhere Payroll All Corporations Being Combined	North Dakota Payroll — Corporation A	Corporation B	Corporation C
8 Payroll	8			
8a Payroll factor *(Divide N.D. Payroll by Everywhere Payroll)*	8a			
8b Total payroll factor *(Add amounts on line 8a, columns A, B & C)*			(BD) 8b	

Sales Factor:
Gross receipts or sales, less returns and allowances from Federal Form 1120 or Federal Form 1120-A, line 1 (c).

	Everywhere Sales All Corporations Being Combined	North Dakota Sales — Corporation A	Corporation B	Corporation C
9 Everywhere sales	9			
10 Sales delivered or shipped to North Dakota destinations		10		
11 Sales shipped from North Dakota to:				
(a) The United States Government		11a		
(b) Purchasers in a state or foreign country where the taxpayer was not subject to a net income tax or a tax measured by net income, or if subject, did not actually pay such tax		11b		
(c) Total North Dakota Sales *(Add lines 10, 11a and 11b)*		11c		
12 Sales Factor *(Divide Total N.D. Sales by Everywhere Sales)*		12		
12a Sales Factor *(Add amounts on line 12, columns A, B & C)*			(BF) 12a	
13 Sum of the factors *(Add lines 7a, 8a and 12)*		13		
14 **Apportionment Factor** *(Divide line 13 by the number of factors having an amount greater than zero in the everywhere column, on lines 7, 8 and 9) (Enter factor here and on part I, line 5, and part III, line 11, if applicable)*		14		
14a Total factor *(Add amounts on lines 7b, 8b and 12a. Divide the sum by three, and enter the total amount here and on Form 40, page 1, line 5)*			(BG) 14a	

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Name as shown on return | Federal employer I.D.

Schedule CR, Part III: Computation of federal income tax deduction for corporations filing a North Dakota consolidated return using the combined report method

(Use 6-digit decimal only)

Additional information regarding the filing of a consolidated North Dakota return using the combined report method is contained in North Dakota Century Code § 57-38-14(11) and North Dakota Administrative Code §§ 81-03-05.1-08, 81-03-05.2 and 81-03-05.3

1 Federal income tax liability *(See instructions on page 5)* (EA) 1 ______
1a Federal alternative minimum tax liability *(See instructions on page 6)* (EG) 1a ______
1b Adjusted federal income tax liability *(Subtract line 1a from line 1)* 1b ______
2 Separate company(ies) federal income tax liability *(Attach worksheet - See instructions on page 6)* 2 ______
3 Profit companies federal income tax liability *(Attach worksheet - See instructions on page 6)* 3 ______
4 Ratio: *(Divide line 2 by line 3. Not to exceed 1.000000)* 4 ______
5 Separate company(ies) share of federal income tax liability *(Multiply line 1b by line 4)* (EB) 5 ______
6 Federal taxable income *(See instructions on page 6)* 6 ______
7 Income not taxable to North Dakota *(See instructions on page 6)* 7 ______
8 Balance *(Subtract line 7 from line 6)* 8 ______
9 Ratio: *(Divide line 8 by line 6. Not to exceed 1.000000)* 9 ______
10 Federal tax on federal taxable income reportable to North Dakota *(Multiply line 5 by line 9)* *(Enter here and in Columns A, B & C)* (CK) 10 ______

Corporations using the combined report method and claiming a federal foreign tax credit, skip line 11 and use lines 12-16. Other corporations must use line 11.

Complete line 11 or line 16, but not both

			Corporation A	Corporation B	Corporation C
10	(carried from above)				
11	North Dakota apportionment factor *(Enter factor from part II, line 14)*	11			
12	North Dakota income *(Enter amount from part II, line 8)* *(If zero or less, skip lines 13 through 16)*	12			
13	Total income *(See instructions on page 6)* *(If zero or less, skip lines 14 through 16)*	13			
14	Income relating to foreign tax credit *(See instructions on page 7)* *(If zero, skip lines 15 and 16)*	14			
15	Income relating to federal income tax paid *(Subtract line 14 from line 13)* *(If zero or less, skip line 16)*	15			
16	Federal income tax ratio *(Divide line 12 by line 15 and go to line 17. (Not to exceed 1.000000)*	16			
16a	Total federal income tax ratio *(Add amounts on line 16, columns A, B & C)*	(EC) 16a			
17	**Federal income tax deduction** *(Multiply line 10 by either line 11 or line 16)*	17			
17a	Total federal income tax deduction *(Add amounts on line 17, columns A, B & C and enter the total amount here and on Form 40, page 1, line 9)*	(ED) 17a			

Instructions For Schedule CR, Part III

Schedule CR, part III has been designed so the instructions for Form 40, Schedule FTD under "Combined Report Method" in the booklet also apply to the line numbers on Schedule CR, part III

After completing Schedule CR, part III, the total from line 17a must be entered on Form 40, page 1, line 9.

North Dakota Office of State Tax Commissioner
2002 Form 40, page 10

Name as shown on return

Federal employer I.D.

Schedule CR, Part IV: Computation of recapture and carryforward of federal AMT disallowed for corporations filing a North Dakota consolidated return using the combined report method

(Use 6-digit decimal only)

			Corporation A	Corporation B	Corporation C
1 2002 Federal alternative minimum tax (AMT) *(Enter amount from Schedule CR, part III, line 1a)*	1				
2 Ratio from Schedule CR, part III, line 4, if no ratio on line 4, enter 1.000000	2				
3 Multiply line 1 by line 2	3				
4 Ratio from Schedule CR, part III, line 9	4				
5 Multiply line 3 by line 4	5				
6 N.D. apportionment factor *(Enter factor from Sch. CR, part III, line 11 or line 16)*		6			
7 Subtotal *(Multiply line 5 by line 6)*		7			
8 Carryforward of previously disallowed federal AMT *(Attach worksheet)*		8			
9 Total federal AMT disallowed *(Add lines 7 and 8)*		9			

Corporations claiming a federal consolidated credit for prior year minimum tax on the 2002 federal return, complete lines 10-12. Other corporations enter the amount from line 9 on line 12.

		Corporation A	Corporation B	Corporation C
10 Balance *(Enter amount from Schedule CR, part I, line 14)*	10			
11 **Subtotal** *(If the amount on line 10 is zero or less, enter zero here and on part I, line 15) (If the amount on line 10 is greater than zero, enter the smaller of line 9 or 10 here and on part I, line 15)*	11			
11a Total recapture of federal AMT disallowed *(Add amounts on line 11, column A, B & C and enter the total amount here and on Form 40, page 1, line 15)*			**11a**	
12 Available carryforward of federal AMT disallowed *(Subtract line 11 from line 9 if completing lines 10 and 11)*	12			
12a Total available carryforward of federal AMT disallowed *(Add amounts on line 12, columns A, B & C)*			**(RA) 12a**	

Instructions for Schedule CR, Part IV

Schedule CR, part IV has been designed so the instructions for Form 40, Schedule AMT-R in the booklet also apply to this part of Schedule CR.

After completing Schedule CR, part IV the total from line 11a must be entered on Form 40, page 1, line 15.

General Instructions

Who must file

Corporations engaged in business in North Dakota or having sources of income from North Dakota must file a 2002 North Dakota Corporation Income Tax Return, Form 40.

For example, a North Dakota Form 40 must be filed by:

- Corporations, including business trusts, associations, and joint-stock companies;
- Cooperative corporations which distribute their net income through patronage dividends;
- Insurance companies which conduct business activities not subject to the North Dakota gross premium tax;
- Tax exempt organizations which have unrelated business taxable income; and
- Organizations which anticipate receiving a tax exempt status notification from the Internal Revenue Service, but have not, by the end of the taxable year, actually received such notification.

A corporation which files a Federal Form 1120S as a small business corporation must file a North Dakota Small Business Corporation Income Tax Return, Form 60.

Financial institutions *(See N.D.C.C. ch. 57-35.3)* located or doing business within North Dakota must file a North Dakota Financial Institution Tax Return, Form 35.

Due date

A calendar year corporation filing Form 40 must file on or before April 15 following the close of the calendar year.

A corporation reporting on a fiscal year basis must file on or before the 15th day of the fourth month following the close of the fiscal year. Use the 2002 Form 40 for fiscal years that begin in 2002 and end in 2003.

A cooperative must file on or before the 15th day of the ninth month following the close of the calendar or fiscal year.

Tax-exempt organizations required to file an income tax return to report unrelated business taxable income must file a corporation income tax return on or before the 15th day of the [illegible] month after the tax year ends.

Short period return

A corporation required to file a federal short period return must file a North Dakota short period return for the same taxable period. The North Dakota return is due on or before the 15th day of the fourth month following the close of the short period. If the due date of the short period federal return falls on a date after the 15th day of the fourth month following the close of the short period, contact the Office of State Tax Commissioner for information regarding the due date for the North Dakota return.

A corporation which terminates as a Subchapter S Corporation during the year, or a corporation which changes its annual accounting period, must annualize its North Dakota taxable income and prorate its state tax liability in the same manner as the federal tax liability is prorated.

Extension of time for filing

An extension of time to file a federal return is automatically accepted by North Dakota as an extension of time to file the state return.

A copy of the federal extension, Form 7004, must be attached to the state return when it is filed. If a copy of the federal extension is not attached, the return must be processed as a delinquent return.

The extension of time to file the North Dakota return is the <u>same number of months</u> as the extension of time to file the federal return.

A state extension to file may be obtained, even if a federal extension has not been requested, providing a written request is made to the Office of State Tax Commissioner prior to the due date of the North Dakota return.

If a corporation has an extension of time to file its North Dakota return, but has not prepaid its entire state tax liability by the regular due date of the return, extension interest at the rate of 12% per annum applies. A corporation which desires to avoid extension interest may make a voluntary state payment by the regular due date of the state return. The payment must be accompanied by a copy of the federal extension Form 7004, and North Dakota Form 40-EXT, indicating the appropriate name, address, and Federal Identification Number of the taxpayer corporation. Alternatively, a letter containing the above information along with a copy of the approved state extension of time to file may be submitted with the prepayment of tax due.

Payment of tax

If tax due *(including interest and penalty)* is less than $5.00, payment need not be made. If tax is due, the total payment due must be paid at the time of, or before, the return is filed. Payment may be made with check or money order, made payable to the North Dakota State Tax Commissioner.

Payment may also be made by electronic funds transfer. Information regarding electronic payments can be found on the department's Web site at www.ndtaxdepartment.com, under Corporate Income, Electronic Filing.

Check the box on the line under Line 21b of Form 40, page 1, and fill in the date of the payment.

Attachments

A complete copy of the federal income tax return as filed with the Internal Revenue Service must be attached to Form 40.

Overpayments

Overpayments of income tax may be applied to the 2003 estimated tax *(minimum $5.00)*, or issued as a refund *(minimum $5.00)*.

A corporation may elect to have the overpayment credited to a 2003 estimated tax installment by circling the appropriate quarter on Form 40, page 1, line 22a.

Penalty and interest

The Office of State Tax Commissioner will notify the taxpayer of any penalty and interest owed on tax due and any interest accrued on a refund. If desired, penalty and interest may be computed on tax due and entered on the return by the taxpayer.

If the full amount of the tax is not paid by the due date, or extended due date, the current provisions for penalty and interest are:

- A penalty equal to 5% of the tax due or $5.00, whichever is greater; and
- Interest computed at the rate of 1% per month *(or a fraction of a month)* of the tax due except the month in which the tax became due.

If the return is not filed by the due date *(or extended due date)*, a penalty of 5% of the net tax liability or $5.00, whichever is greater, applies for the month in which the return is due, with an additional 5% for each additional month *(or a fraction of a month)* during which the delinquency continues, not to exceed 25% of the net tax liability.

If there is an overpayment on Form 40, page 1, interest at the rate of 1% per month accrues on the overpayment beginning forty-five days after the due date of the return *(without extension)* or after the date the return is filed, whichever date is later.

Incomplete return

All applicable lines on Form 40 must be completed. A return with incomplete lines or schedules, or with notations such as "see attached statement" or "available upon audit," is not properly filed and will be returned to the taxpayer.

Ratios and decimals

On all schedules where a ratio or decimal is called for, use 6 digits after the decimal point.

Where to file or obtain additional forms and instructions

Completed returns and written requests for information and forms should be mailed to the Office of State Tax Commissioner, 600 E. Boulevard Ave., Dept. 127, Bismarck, ND 58505-0599.

Obtain North Dakota tax forms, send messages, and find other information on the Office of State Tax Commissioner's Web site at www.ndtaxdepartment.com.

Forms and instructions may also be obtained by calling 701-328-2046.

For the speech or hearing impaired, call Relay North Dakota at 1-800-366-6888 and ask for 1-701-328-2046.

Information at the source

Any corporation doing business in North Dakota which is required to file a Federal Form W-2 or 1099 must also file one with this state. For more information on the requirements and alternatives for satisfying those requirements, contact the Office of State Tax Commissioner.

Quick refund

Quick refund of overpaid estimated income tax may be requested by a corporation if the overpayment exceeds five hundred dollars *($500)* and the claim for quick refund is filed after the close of the taxable year but before the 15th day of the fourth month thereafter. The form for the Quick Refund of Estimated Income Tax For Corporations *(Form 40 QR)* must be obtained from the Office of State Tax Commissioner.

Estimated tax payments

If a corporation's estimated state income tax liability exceeds five thousand dollars *($5,000)* and its previous year's state income tax liability exceeded five thousand dollars *($5,000)*, the corporation is required to make an estimated tax payment of at least one-fourth of the amount due on each of four prescribed dates.

Information regarding estimated tax payments is located at the back of this booklet.

Amended returns/federal audit changes

An Amended North Dakota Corporation Income Tax Return, Form 40X, must be filed if:

- An amended federal income tax return is filed;
- North Dakota income is changed as a result of a federal audit;
- A corporation's North Dakota income is changed as a result of a North Dakota net operating loss carryback;
- An error is discovered on a previously filed return;
- The corporation receives a refund of federal income tax which was deducted on a previously filed Form 40.

Information about amended returns can be found in N.D.C.C. §§ 57-38-38 and 57-38-40.

A current Form 40X and instructions can be obtained from the Office of State Tax Commissioner's web site at www.ndtaxdepartment.com

Federalization

The North Dakota income tax law is perpetually "federalized" for the Federal Taxable Income starting point of the North Dakota Return, for taxable years beginning after December 31, 1988.

Method of corporation taxation

The North Dakota corporation income tax applies only to that portion of a corporation's taxable income which is derived from or attributable to sources within this state.

A nonapportioning corporation, i.e. a corporation whose business activity is conducted solely within North Dakota, computes North Dakota taxable income by adjusting its federal taxable income by North Dakota statutory adjustments.

An apportioning corporation, i.e. a corporation whose business activity is conducted both within and without North Dakota, computes North Dakota taxable income by adjusting its federal taxable income by North Dakota statutory adjustments and apportioning this adjusted taxable income using Schedule FACT, FACT-1, or CR *(Part II)* of Form 40.

A corporation engaged in a unitary business with one or more corporations *(irrespective of the country or countries in which the corporations conduct business)* must file using the combined report method.

A unitary business is a group of corporations which carries on activities, the component parts of which transfer value among themselves through the unities of ownership, operation and use.

- "Unity of ownership" means the group is under the common control of a single corporation, which is also a member of the group. Control exists when the single corporation owns, directly or indirectly, more than fifty percent of the voting stock of another corporation;
- "Unity of operation" means the group receives benefits from functional integration or economies of scale;
- "Unity of use" means the group of corporations contributes to or receives benefits from centralized management and policy formation.

Whether a group of corporations is engaged in a unitary business depends on the facts and circumstances of each case. If unity of ownership exists, any of the following facts or circumstances creates a presumption that the unities of operation and use exist; therefore, the corporations are engaged in a unitary business if:

- All activities of the group are in the same general line or type of business;
- The activities of the group constitute different steps in a vertically structured enterprise; or
- The group is characterized by centralized management.

Water's edge election

A corporation required to file its North Dakota return using the worldwide unitary combined report method may elect to use the water's edge method. The water's edge election must be made on the return as originally filed and is binding for five consecutive years. If the election is made, a corporation may not reduce taxable income by a federal income tax deduction.

A domestic disclosure spreadsheet must be obtained from and filed with the Office of State Tax Commissioner the first year the property, payroll, or sales in foreign countries exceed ten million dollars and total assets exceed two hundred fifty million dollars, and every third year thereafter provided the property, payroll, or sales in foreign countries exceed ten million dollars and total assets exceed two hundred fifty million dollars.

Specific Instructions for Form 40, Page 1

Line 1
Income

Check the box for the reporting method used to complete the return and enter the income reportable under that method:

a. Single Corporate Entity

The single corporate entity method reports income or loss of only one incorporated business.

If the single corporate entity method is used for both North Dakota and federal purposes, enter the federal taxable income from:

- Federal Form 1120, line 30; or
- Federal Form 1120-A, line 26.

If the single corporate entity method is used for North Dakota purposes and the corporation is included in a consolidated Federal Form 1120, enter the corporation's federal taxable income before consolidating adjustments/eliminations from:

- A pro forma separate company federal income tax return, line 30; or
- The schedule showing gross income and deductions, which supports the consolidated federal taxable income.

Cooperatives and other business organizations using federal forms other than Federal Form 1120 must enter the federal taxable income from the appropriate form.

b. Combined Report Method

The combined report method is used if the corporation apportions its income from a unitary group of corporations.

The combined report method reports the income or loss of all unitary corporations in the unitary group (*See N.D. Admin. Code ch. 81-03-05.1*).

If the combined report method is used, enter the amount from the North Dakota Schedule WW, line 13 and attach the schedule to Form 40.

b1. 100% North Dakota Corporations Consolidated Return Using the Combined Report Method

Check the "100% North Dakota Consolidated Return" box if the corporation is required to file one consolidated North Dakota return using the combined report method.

Two or more corporations **are required** to file one North Dakota return using the combined report method if the corporations are affiliated as parent and subsidiary, are filing a consolidated federal tax return, and all corporations are operating solely within North Dakota.

If the box entitled "100% North Dakota Consolidated Return" is checked:

- Enter the amount from the North Dakota Schedule WW, line 13, and attach the schedule to Form 40; and
- Complete North Dakota Schedule CR, parts I through IV, and attach the schedule to Form 40.

b2. Apportioning Corporation Consolidated Return Using the Combined Report Method

Check the "Apportioning Corp Consolidated Return" box if the corporation is filing one consolidated North Dakota return using the combined report method.

Two or more corporations **may** file one North Dakota return using the consolidated return if the corporations are required to use the combined report method and more than one of the corporations has a filing requirement in North Dakota.

If box b2 entitled "Apportioning Corp Consolidated Return" is checked:

- Enter the amount from the North Dakota Schedule WW, line 13, and attach the schedule to Form 40; and
- Complete North Dakota Schedule CR, parts I through IV, and attach the schedule to Form 40.

c. Water's Edge Method

Check the "Water's Edge Method" box if the corporation is a member of a worldwide unitary group and elects to file a North Dakota return using the water's edge method (*See N.D. Admin. Code ch. 81-03-05.2*).

If the box entitled "Water's Edge Method" is checked, enter the amount from the North Dakota Schedule WE, line 11, and attach the schedule to Form 40.

If the corporation elects to use the water's edge method and is filing a consolidated North Dakota return, complete Schedule CR, parts I, II and IV, and attach the schedule to Form 40.

d. Other

Check the "Other" box if the corporation has received written permission from the Office of State Tax Commissioner to file a North Dakota return using a filing method other than those specified above.

Other filing methods are contained in N.D.C.C. § 57-38.1-18 (*for example, separate accounting or a method using an apportionment factor different from that computed on Schedules FACT, FACT-1 or CR*).

If the box entitled "Other" is checked, attach a copy of the letter granting permission to use, or requiring the use of, this filing method and a worksheet substantiating and explaining the computation of income. Enter the total income from this worksheet on Form 40, page 1, line 1

Line 4
North Dakota apportionable income

If completing Schedule CR, enter the amount from Form 40, page 1, line 4 on Schedule CR, part I, line 4 (*enter the same amount for each company*) and complete all parts of Schedule CR.

Line 5
Apportionment factor

If a corporation has business income (*See N.D.C.C. ch. 57-38.1*) from activity solely within this state, enter 1.000000 on this line. Corporations not filing a consolidated return, enter the apportionment factor from Schedule FACT, line 14 or Schedule FACT-1, line 6. Corporations completing Schedule CR, must enter the apportionment factor from Schedule CR, part II, line 14a.

Line 7
Income allocated to North Dakota

Enter nonbusiness income allocated to North Dakota less related expenses. Nonbusiness income is allocated to North Dakota if the income is attributable to North Dakota.

Expenses must be attributed to nonbusiness income in a manner which fairly distributes all of the corporation's expenses to its various types of income.

Corporations completing Schedule CR must enter the total nonbusiness income for all corporations having activity within North Dakota.

Line 9
Federal tax deduction

Corporations completing Schedule FTD, enter amount from Schedule FTD, line 17.

Corporations electing water's edge method, enter zero on this line.

Corporations completing Schedule CR, enter the amount from Schedule CR, part III, line 17a.

Line 10
Exemption for new and expanding business

If the corporation received a new and expanding business exemption from the State Board of Equalization, enter the amount of exempt income computed pursuant to N.D. Admin. Code § 81-03-01.1-06.

Corporations completing Schedule CR, enter the exempt income for each corporation having an exemption and activity within North Dakota.

Line 11
Renaissance zone income exemption

If the corporation is claiming exempt income as a result of the Renaissance Zone Act, enter total amount of exemption from the summary part of Schedule RZ. Contact the Office of State Tax Commissioner at 701-328-2040 to obtain Schedule RZ.

Line 12
ND income after federal tax deduction and income exemptions

If the amount on line 12 is a loss, the loss may be carried back and carried forward for the same number of years as a federal loss of like-kind.

Election to forego loss carryback

However, regardless of the corporation's treatment of a federal net operating loss, the corporation may elect to forego the allowable carryback period and carry forward the entire state loss. To elect to forego the carryback period for a North Dakota loss, check the box in Question 10 on page 2 of Form 40. A corporation must make this election on an original return that is timely filed for the year in which the loss was incurred.

If an election is not made, the loss must be carried back.

Additional information regarding loss carryback and loss carryforward provisions is contained in N.D.C.C. § 57-38-01.3(3) and N.D. Admin. Code § 81-03-05.1-07.

Line 13
North Dakota loss carryforward

The North Dakota loss carryforward allowed on the 2002 Form 40 is the amount of the accumulated loss less any previously deducted loss carryback or carryforward.

Attach a worksheet showing the accumulated loss, by year, less any previously deducted loss carryback or carryforward.

Corporations completing Schedule CR must enter the loss carryforward from all corporations having activity within North Dakota.

Line 15
Recapture of federal alternative minimum tax

Corporations completing Schedule AMT-R, enter amount from Schedule AMT-R, line 11.

Corporations completing Schedule CR, enter the amount from Schedule CR, part IV, line 11a.

Line 16
North Dakota taxable income

If the return reports a North Dakota loss on Form 40, page 1, line 12, or a North Dakota loss carryforward on Form 40, page 1, line 13, please complete lines 14-17.

Always complete line 16 by subtracting the amount on line 15 from the amount on line 14.

Line 20
Tax year 2002 estimated income tax payments

Enter the total 2002 estimated income tax payments. Also, enter any 2001 overpayment credited to the 2002 taxable year and any payment voluntarily made to the state with an extension of time for filing.

Line 21a
Interest and penalty for balance due

The Office of State Tax Commissioner will notify the taxpayer of any penalty and interest owed on tax due. If desired, penalty and interest may be computed by the taxpayer on tax due and entered on the return.

If the full amount of the tax is not paid by the due date, or extended due date, the current provisions for penalty and interest are:

- A penalty equal to 5% of the tax due or $5.00, whichever is greater; and
- Interest computed at the rate of 1% per month *(or a fraction of a month)*, of the tax due except the month in which the tax became due.

If the return is not filed by the due date *(or extended due date)*, a penalty of 5% of the net tax liability or $5.00, whichever is greater, applies for the month in which the return is due, with an additional 5% for each additional month *(or a fraction of a month)* during which the delinquency continues, not to exceed 25% of the net tax liability.

Line 22a
Amount to be credited to year 2003

A corporation may elect to have the overpayment credited to a 2003 estimated tax installment by circling the appropriate quarter on Form 40, page 1, line 22a to specify the particular installment to which the amount credited is to be applied.

Specific Instructions for Schedule SA

Additions

Line 3
All taxes measured by income deducted to arrive at federal taxable income

Enter all taxes measured by income, including income taxes, franchise or privilege taxes measured by income *(paid to any taxing authority including a foreign country)* to the extent such taxes were deducted to arrive at federal taxable income.

Line 4
North Dakota depreciation adjustment

North Dakota income tax statutes did not allow for the use of ACRS depreciation on assets placed in service between January 1, 1981 and the end of the 1982 tax year. These assets must be depreciated using methods allowed under the Internal Revenue Code provisions in effect as of December 31, 1980. Federal taxable income must be adjusted for the difference in these two methods. Enter the amount of ACRS depreciation deducted on the federal return for these assets for the current taxable year.

Include depreciation on all currently held assets which were placed in service between January 1, 1981 and the end of the 1982 tax year, **not** just such assets which are located within North Dakota.

In computing this adjustment, exclude safe harbor lease assets.

Line 6
Other additions

The safe harbor lease provisions in Section 168(f)(8) of the Internal Revenue Code of 1954, as amended, were not adopted in North Dakota in those instances where the minimum investment by the lessor is less than one hundred percent (100%). Enter amounts on line 6, as follows:

- Seller/Lessee: sale proceeds, rent expense, amortization expense, lease acquisition cost.
- Buyer/Lessor: Interest expense, depreciation expense, amortization expense, acquisition cost, loss on sale of property.

Additional information regarding this adjustment is contained in N.D.C.C. § 57-38-01(3)(a).

Subtractions

Line 8
Tax refunds received in year 2002

Enter all income, franchise or privilege tax refunds received in 2002, to the extent such taxes were previously included in North Dakota taxable income.

Federal income tax refunds received cannot be included on line 8. See General instructions, Amended returns/federal audit changes.

Line 10
North Dakota depreciation adjustment

Enter the amount of depreciation computed for the current taxable year on assets placed in service between January 1, 1981 and the end of the 1982 tax year, using methods allowable as of December 31, 1980. *(See instructions for line 4 for further explanation).*

Include depreciation on all currently held assets which were placed in service between January 1, 1981 and the end of the 1982 tax year, not just such assets which are located within North Dakota.

In computing this adjustment, exclude safe harbor lease assets.

Lines 11 and 12
Allocated income and related expenses

Enter on line 11 all nonbusiness income and enter related expenses on line 12. The method used to attribute expenses to nonbusiness income must fairly distribute all of the corporation's deductions to all of its various types of income.

If an entry is made on this line, all of the following must be attached to Form 40:

- A worksheet showing each type of income or loss item allocated and its amount;
- Documentation showing the state to which the item of income or loss was allocated *(a copy of the other state's tax return is preferred);* and
- A narrative explaining the reasons for allocating each item of income or loss.

Line 15
North Dakota domestic dividend exclusion

Dividends received by the corporation are not taxable in North Dakota if the dividends are received from a corporation which has paid North Dakota corporation income tax pursuant to N.D.C.C. ch. 57-38, or from a bank, trust company or building and loan association which has paid tax pursuant to N.D.C.C. ch. 57-35.3.

If the payor corporation's entire federal taxable income was subjected to North Dakota taxation, the full amount of the dividends may be subtracted on this line. If the payor corporation is an apportioning corporation, the deduction is computed by multiplying the dividends received by the payor corporation's North Dakota apportionment factor.

Line 16
Other subtractions

If the amount on Form 40, page 1, line 1 includes any gain, either ordinary or capital, from property subjected to eminent domain sale or transfer, such gain is not taxable and must be entered on this line.

Section 168(f)(8) of the Internal Revenue Code of 1954, as amended, was not adopted in North Dakota in those instances where the minimum investment by the lessor is less than one hundred percent (100%). Enter amounts as follows:

- Seller/Lessee: interest income and depreciation expense *(for assets placed in service between January 1, 1981 and the end of the 1982 taxable year, use methods allowed under the Internal Revenue Code as of December 30, 1980; for assets placed in service after the 1982 taxable year, use ACRS depreciation).*
- Buyer/Lessor: rental income.

Regulated investment companies, as defined by the Internal Revenue Code, will be allowed to subtract on this line certain dividends paid to shareholders. The dividends paid must be attributable to income that is taxable under N.D.C.C. ch. 57-38 when the regulated investment company earns the income.

Specific Instructions for Schedule FTD

Use the line instructions that apply to the filing method box that is checked on Form 40, page 1, line 1.

Corporations filing a consolidated North Dakota return must complete Schedule CR, Part III (*do not complete Schedule FTD*) and refer to the instructions below for the "Combined Report Method."

Single Corporate Entity (Box a - Form 40, page 1, line 1)

A corporation filing as a single corporate entity for **both** North Dakota and federal purposes must complete lines 1, 1a, 1b, 4, 5, 6, 7, 8, 9, 10, 11 and 17.

A corporation filing as a single corporate entity for North Dakota purposes **and** included in a consolidated Federal Form 1120 must complete lines 1-11 and 17.

Line 1
Federal income tax liability

Enter the federal income tax liability from the federal income tax return filed with the IRS as follows:

- If Federal Form 1120 was used, enter the amount from line 31;
- If Federal Form 1120-A was used, enter the amount from line 27.

Cooperatives or other business organizations using federal forms other than Federal Form 1120 must enter the federal tax liability from the appropriate form.

Line 1a
Federal alternative minimum tax liability

Enter the amount of Federal Alternative Minimum Tax (AMT) which has been included on line 1. Federal AMT is disallowed in computing the North Dakota Federal Income Tax Deduction because income which created federal AMT is not a part of North Dakota taxable income.

Disallowed federal AMT is carried forward and may be recaptured in future tax periods. For more information see Schedule AMT-R.

Line 2
Separate company(ies) federal income tax liability

Enter the federal income tax liability as computed on the corporation's pro forma separate company return. Attach a worksheet supporting this computation.

Line 3
Profit companies federal income tax liability

Enter the total pro forma separate company federal income tax liabilities for all corporations included in the consolidated federal return. The separate company tax liability of any corporation which does not result in a positive tax liability shall be zero. Attach a worksheet supporting this computation.

Line 4
Ratio

Enter 1.000000 if filing as a single corporate entity for both North Dakota and federal purposes.

Line 6
Federal taxable income

Enter the amount from Form 40, line 1.

Line 7
Income not taxed to North Dakota

Enter the income *(before apportionment)* included on line 6 not taxable to North Dakota, such as interest on U.S. obligations and income allocated outside North Dakota.

Line 11
North Dakota apportionment factor

Enter the apportionment factor from Form 40, line 5, and proceed to line 17.

Combined Report Method (Boxes b, b1, and b2 - Form 40, page 1, line 1)

The following line instructions apply to:

- Corporations filing a combined return and checking box b on Form 40, line 1 (using Schedule FTD);
- Corporations filing a consolidated return and checking either box b1 or b2 on Form 40, line 1 (using Schedule CR, part III).

If a corporation tax return includes income from more than one federal tax return, a separate pro forma Schedule FTD must be completed for each corporation that filed a federal tax return.

The amounts on lines 1, 1a, 1b, 5, 6, 10 and 11 from the separate pro forma Schedule FTD's must be aggregated and the totals entered on the appropriate lines on the corporation's Form 40.

Line 1
Federal income tax liability

Enter the federal income tax liability from the federal income tax return filed with the IRS as follows:

- If Federal Form 1120 was used, enter amount from line 31;
- If Federal Form 1120-A was used, enter the amount from line 27.

Cooperatives or other business organizations using federal forms other than Federal Form 1120 must enter the federal tax liability from the appropriate form.

Line 1a
Federal alternative minimum tax liability

Enter the amount of Federal Alternative Minimum Tax (AMT) which has been included on line 1. Federal AMT is disallowed in computing the North Dakota Federal Income Tax Deduction because income which created federal AMT is not a part of North Dakota taxable income.

Disallowed federal AMT is carried forward and may be recaptured in future tax periods. For more information see Schedule AMT-R.

Do not complete lines 2 and 3, and enter 1.000000 on line 4 if:

- ***A consolidated federal return is not filed; or***
- ***A consolidated federal return is filed in which all companies included in the consolidated federal return are included in the unitary group.***

Line 2
Separate company(ies) federal income tax liability

Enter the separate company pro forma federal income tax liability for all of the unitary corporations which are included in the consolidated federal return. The separate company tax liability of any corporation which does not result in a positive tax liability shall be zero. Attach a worksheet supporting this computation.

Line 3
Profit companies federal income tax liability

Enter the total pro forma separate company federal income tax liabilities for all corporations included in the consolidated federal return. The separate company tax liability of any corporation which does not result in a positive tax liability shall be zero. Attach a worksheet supporting this computation.

Line 6
Federal taxable income

Enter the total federal taxable income for all unitary corporations whose income is included in the Federal Form 1120. Attach a worksheet supporting this computation.

Line 7
Income not taxable to North Dakota

Enter the income *(before apportionment)* included on line 6 not taxable to North Dakota, such as interest on U.S. obligations and income allocated outside North Dakota.

Line 11
North Dakota apportionment factor

If a foreign tax credit is not claimed on the federal income tax return, enter the apportionment factor from Form 40, page 1, line 5, and proceed to line 17.

Corporations filing a consolidated state return enter the factors from Schedule CR, part II, line 14 on Schedule CR, part III, line 11.

If a foreign tax credit is claimed on the federal income tax return, skip line 11 and go to line 12.

Line 13
Total income

"Total income" is federal taxable income of those corporations which are included in the unitary group and are required to file a federal income tax return, plus or minus the adjustments *(before apportionment)* provided in N.D.C.C. § 57-38-01.3, except for the federal income tax deduction. Use the worksheet below to compute the total income to be entered on line 13, or Schedule CR, part ... ne 13.

1. Federal taxable income *(Schedule FTD, line 6)* ______
2. Total additions *(page 1, line 2)* ______
3. Total subtractions *(page 1 line 3)* ______
4. Subtotal *(Add lines 1 and 2, subtract line 3)* ______
5. Net intercompany adjustments in lines 2 & 3* ______
6. Total income *(Subtract line 5 from line 4. Enter here and on Schedule FTD, line 13, or Schedule CR, Part III, line 13)* ______

Line 14
Income relating to Foreign Tax Credit

Enter the total taxable income from sources outside the U.S., after loss recapture as computed on Federal Form(s) 1118, part II, Schedule B or Federal Form(s) 5735.

Water's Edge Method (Box c - Form 40, page 1, line 1)

A corporation electing the water's edge ... d cannot claim a federal income tax deduction. Do not complete Schedule FTD and enter zero on Form 40, page 1, line 9.

Other (Box d - Form 40 page 1, line 1)

A corporation which has checked the box entitled "Other" on Form 40, line 1, should contact the Office of State Tax Commissioner for specific instructions. Based on the instructions from the Office of State Tax Commissioner, attach a worksheet supporting the computations.

Specific Instructions for Schedule AMT-R

Corporations filing a consolidated state return and checking box b1 or b2 on Form 40, line 1, must complete Schedule CR, part IV *(do not complete Schedule AMT-R.)*

North Dakota Schedule AMT-R is used to compute the recapture and carryforward of Federal Alternative Minimum Tax (AMT) ... has been disallowed. Federal AMT may be recaptured only if:

- A federal credit for prior year minimum tax is claimed; and
- The recapture does not create or increase a North Dakota net operating loss.

The recapture of federal AMT disallowed in prior period(s) is used to reduce the current year's North Dakota income on Form 40, page 1 or part I of North Dakota Schedule CR *(for corporations filing a consolidated state return.)*

Any portion of the disallowed federal AMT remaining after 2002 may be carried forward and used to reduce North Dakota income in future years when a federal credit for prior year minimum tax is claimed.

For specific line instructions, see Schedule AMT-R, or Schedule CR, part IV *(for corporations filing a consolidated state return.)*

Specific Instructions for Schedule TC

Lines 1 and 2
Contributions to nonprofit private colleges and high schools

Tax credits are available for making contributions to qualifying nonprofit private institutions of secondary and higher education located in North Dakota *(including the North Dakota Independent College Fund).* Contributions do not qualify unless they are made directly to, or are specially designated for the exclusive use of, a qualifying institution. A contribution to an account, fund or entity benefiting both qualifying and nonqualifying institutions does not qualify for the credit. The credits are available if the contribution(s) are made by the due date of this return, including extensions.

The tax credit for contributions made to all eligible schools in each category of institution is equal to the lesser of:

- 50% of the contributions but not to exceed 20% of the total tax liability;
- $2,500.

Enter on line 1 the tax credit computed for contributions to nonprofit private institutions of higher education *(and the North Dakota Independent College Fund)* and enter on line 2 the tax credit computed for contributions to nonprofit private institutions of secondary education.

For each contribution, attach a copy of a receipt from the nonprofit private institution or a cancelled check *(front and back).*

Line 3
Venture Capital Corporation credit

A corporation may be entitled to a tax credit for investments made in a North Dakota venture capital corporation. The credit is limited to 25% of the amount invested or $250,000, whichever is less. If the amount of the credit exceeds the corporation's state tax liability for that taxable year, the credit may be carried forward for up to seven years.

The corporation income tax credit for investments made in a North Dakota venture capital corporation is NOT allowed for investments made after February 28, 1991 in a venture capital corporation organized before January 1, 1989, which invested in a business or an affiliate of a business that owned tax-exempt securities.

A copy of the Venture Capital Corporation Investment Reporting Form must be attached to Form 40 in the initial year the tax credit is claimed.

For additional information regarding this credit, contact the Office of State Tax Commissioner.

Line 4
North Dakota Small Business Investment Company credit

If the corporation made a qualifying investment in the North Dakota Small Business Investment Company, enter 25% of the amount invested. If the credit exceeds the amount of the current tax liability, the excess may be carried forward up to seven years.

Attach a copy of the North Dakota SBIC Investment Reporting Form.

For additional information regarding this credit, contact the Office of State Tax Commissioner.

Line 5
Geothermal, solar or wind energy device credit

If the corporation is claiming this credit for a device installed before January 1, 2001, on property owned by the taxpayer, the tax credit is allowed for three years and is computed at 5% of the actual cost of acquisition and installation of the device.

The credit for devices installed after December 31, 2000, is equal to three percent of the installation cost, each year for five years. The device must be installed in North Dakota on property owned or leased by the taxpayer. This tax credit is limited to devices installed before January 1, 2011.

For devices installed after December 31, 2000, by pass-through entities (partnerships, Subchapter S Corporations, and Limited Liability Companies) the tax credit must be passed through to partners, shareholders, or members in proportion to their respective interests in the pass-through entity.

Attach a worksheet substantiating date of purchase, actual cost of acquisition and installation, and computation of the tax credit.

Line 6
Credit for employing the developmentally disabled or chronically mentally ill

A corporation may claim a tax credit for a portion of North Dakota wages paid to a developmentally disabled or chronically mentally ill employee. The tax credit is 5% of up to $6,000 in wages paid to each such employee during the first twelve months of employment. The credit may not exceed 50% of the total tax liability. Only North Dakota wages actually paid during the taxable year may be considered for the tax credit. If this credit is claimed, attach an affidavit listing the amount of wages paid, the name and the social security number of each employee

Line 7
Research and experimental expenditures credit

A corporation which invests in research and experimental expenditures within North Dakota is entitled to a tax credit. The tax credit is determined by subtracting the base period research expenses *(as defined in Section 26 U.S.C. 41(c) of the Internal Revenue Code of 1986, as amended)* which are applicable to North Dakota from the qualified research expenses made in North Dakota, and applying the following rates to the resulting difference:

- 8% on the first $1,500,000;
- 4% on the excess over $1,500,000.

If the tax credit exceeds the current income tax liability, any unused tax credit may be carried back for three years and then carried forward for up to fifteen years.

Line 8
New industry credit

A corporation which has been incorporated in North Dakota for the first time after January 1, 1969, and which is not the result of a business reorganization or acquisition, or any out-of-state corporation that has received a certificate of authority to transact business in North Dakota for the first time after January 1, 1969, may be entitled to a tax credit. This tax credit is available only for new enterprises engaged in assembling, fabricating, manufacturing, mixing, or processing any agricultural, mineral, or manufactured products or any combination thereof. However, a corporation which is receiving any property tax or income tax exemption allowed by N.D.C.C. chs. 40-57 or 40-57.1 shall not be allowed this credit.

The tax credit is computed as a percentage the annual gross amount expended by the corporation for salaries and wages within North Dakota. The following percentages apply:

- 1% for each of the first three taxable yea a corporation qualifies for the tax credit.
- .5% for each of the fourth and fifth taxab years a corporation qualifies for the cred

Attach a worksheet substantiating date of incorporation or initial authority to transact business in this State, annual gross amoun of salaries and wages within this State and type of business activity.

Line 9
Credit for payment to a certified nonprofit development corporation

A tax credit is available to a corporation which invests in a certified nonprofit development corporation. The maximum tax credit allowed is 25% of the total investmen not to exceed $2,000. Any unused credit m be carried forward for up to seven years.

Line 10
Renaissance zone credits

If a corporation is claiming a tax credit as a result of the Renaissance Zone Act, enter total amount of credits from the summary pa of Schedule RZ. Contact the Office of State Tax Commissioner for Schedule RZ.

FEB. 14. 2003 4:10PM NO. 4200 P. 2

COST
Council On State Taxation

February 14, 2003

The Honorable John Hoeven
Governor of the State of North Dakota
State Capitol, Department 101
600 East Boulevard Avenue
Bismarck, ND 58505-0001

VIA FACSIMILE

Re: Opposition to Repeal of "Water's-Edge Election" in HB 1471/SB 2374

Dear Governor Hoeven:

The Council On State Taxation has recently reviewed House Bill 1471 and Senate Bill 2374, both of which would reduce the corporate income tax rate to encourage investment in North Dakota. We applaud your efforts to spur economic development in the state through both tax and non-tax initiatives. We are deeply troubled, however, by a provision in both pieces of legislation which would eliminate the water's-edge election for corporations that do business both within North Dakota and elsewhere and urge you to advocate that the existing water's-edge election be retained.

About COST

The Council On State Taxation (COST) is a nonprofit trade association based in Washington, DC. COST was formed in 1969 as an advisory committee to the Council of State Chambers of Commerce and today has an independent membership of 550 major corporations engaged in interstate and international business. COST's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities.

Many COST members conduct business in North Dakota—contributing to its commerce, employing its citizens, and paying a significant portion of the taxes collected from multistate corporations. As good corporate citizens, they are concerned that without a tax climate designed to encourage corporate growth, North Dakota's corporate taxpayers will be laboring unfairly under burdens not borne by corporations operating in other states.

Water's-Edge Election

HB 1471 and SB 2374 would eliminate the current water's-edge election available to multinational taxpayers and thus require these companies to include non-U.S. corporations that are part of the unitary group in the companies' tax returns. In other words, they would be required to calculate their worldwide income when filing a North Dakota corporate tax return.

122 C Street, N.W., Suite 330 • Washington, DC 20001-2109 • Tel: 202/484-5222 • Fax: 202/484-5229

The issue of worldwide combined reporting was thoroughly investigated in the early 1980s by President Ronald Reagan through the Worldwide Unitary Taxation Working Group. The Working Group included representatives of the federal government, the states (both the legislative and executive branches), and business.

In the Working Group's final report (July 31, 1984) to the President, Treasury Secretary Donald Regan noted that the Working Group agreed on three principles that should guide the state taxation of the income of multinational corporations. Principle one is that a water's-edge election be provided for both U.S. and foreign based companies. Secretary Regan recommended that federal legislation be enacted to that effect if the States failed to resolve the issue on their own.

At the time, twelve states (including North Dakota) did not allow a water's-edge election. All twelve changed their laws during the mid-to-late 1980s to provide for such an election. None of those states have since contemplated eliminating that election, and we urge North Dakota not to do so now.

Conclusion

The intent of both HB 1471 and SB 2374 is to encourage economic development in North Dakota. Unfortunately, elimination of North Dakota's water's-edge election creates tremendous administrative and compliance burdens and would thus have the exact opposite effect on many large corporations. Moreover, repeal of the water's-edge election may result in unnecessary federal intervention. In the words of Secretary Regan, "the use of the worldwide unitary method may interfere with the foreign commerce of the United States, so this becomes a matter of vital federal interest." We would most appreciate your support to amend HB 1471/SB 2374 so as to retain the existing water's-edge election.

Sincerely,

Joseph R. Crosby
Legislative Director

cc: The Honorable Rick Clayburgh, North Dakota Tax Commissioner
Representative Al Carlson, North Dakota House of Representatives
Dale Anderson, President, Greater North Dakota Association/State Chamber of Commerce
Board of Directors, Council On State Taxation

Greater North Dakota Association

STATEMENT BY DALE O. ANDERSON, PRESIDENT, GNDA, REGARDING ENGROSSED HB 1471, THE NORTH DAKOTA SENATE FINANCE AND TAXATION COMMITTEE, MARCH 5, 2003.

Chairman Urlacher and members of the Senate Finance and Taxation Committee. I am Dale O. Anderson, President, GNDA, North Dakota State Chamber of Commerce. Thank you for this opportunity to provide testimony in opposition to engrossed HB 1471.

We commend Representative Carlson for introducing HB 1471 to address the corporate income tax perception problem in marketing our state and to Governor Hoeven for placing a high priority on this issue in his address to the joint session of the 2003 North Dakota Legislature.

For nearly eighty years the Greater North Dakota Association is the voice for business and principal advocate for positive change for North Dakota. The organization's membership is an economic and geographic cross section of North Dakota's private sector, including statewide associations and local chambers of commerce, development organizations and convention and visitors associations and public sector organizations. GNDA is governed by a Board of Directors elected by our membership. The GNDA Board Chairman is Dr. Jay Leitch, Dean, College of Business Administration, NDSU, Fargo.

There are two components to GNDA's mission which are general business climate issues and economic development or new wealth creation. There are three strategies for economic development to occur which are: (1) entrepreneurship or new business startups within North Dakota, (2) business expansion from within North Dakota and (3) business attraction from outside North Dakota into North Dakota.

Two years ago, GNDA coordinated an effort to build a more successful economy in North Dakota – the New Economy Initiative. This Initiative has been successful to help mobilize North Dakotans create new ideas, new mindsets, new growth, and to leverage technology

opportunities to shape a more competitive state economy. In today's economy, information and ideas are the essential ingredients for generating wealth. Labor is needed, not so much for its muscle, but for its mind power.

GNDA is sympathetic to the problem that North Dakota is perceived as a high corporate income tax rate state. This problem can be fixed by reducing the corporate tax rate and thus, reducing corporate income tax collections or eliminating the federal corporate income tax deduction, which create winners and losers. We have not seen any solid evidence that removing this perception problem will result in an increase in primary sector jobs. We understand that some business sight selectors, in a first cut, see the 10.5 corporate income tax rate and eliminate a North Dakota sight without further consideration.

With regard to engrossed HB 1471, GNDA believes the following amendments would be necessary for GNDA to support the bill:

1. **Maintain the water's edge election passed into law in 1987, (See attached letter to Governor Hoeven from COST, February 14, 2003.)**

2. **Improve the corporate income perception problem by lowering the corporate income tax rate by eliminating the federal income tax deduction for corporations,**

3. **Accomplish items 1 and 2 without a tax increase, and**

4. **Publish the effective corporate income tax rate.**

Mr. Chairman, we, including business and developers, look forward to working with you and members of the Senate Finance and Taxation Committee, Representative Carlson Governor Hoeven, Tax Commissioner Clayburg, to come up with a workable solution to this issue that accomplishes items 1-3 above.

Thank you Chairman Urlacher and members of the Senate Finance and Taxation Committee for this opportunity to discuss the business community's position on engrossed HB 1471. We urge a do not pass recommendation on engrossed HB 1471. I welcome your questions.

1P

TESTIMONY
LEE PETERSON, COMMISSIONER OF THE DEPT OF COMMERCE
SENATE FINANCE & TAXATION COMMITTEE
MARCH 10, 2003 - 10:30 A.M.
HOUSE BILL 1471

Good morning, Chairman Urlacher, and members of the committee. I am Lee Peterson, Commissioner of the North Dakota Department of Commerce.

It is a pleasure to appear before you today and visit about our current corporate income tax rate and the difficulty of explaining it to site selectors and businesses looking at North Dakota as a place to expand.

In real and measurable economic development, we must work in 3 important areas:

1. Start-ups and entrepreneurs
   a. Bushel 42 in Crosby
2. Expand our existing industry
   a. Baker Boy in Dickinson
   b. Cloverdale in Minot and Mandan
   c. Imation in Wahpeton
3. Recruit new industry to North Dakota
   a. Infinity Windows by Marvin
   b. Direct Response in Beulah
   c. Northwest Alfalfa in Tioga
   d. Specialty Exports in Hatton

Recruiting new industry is where the problem lies with the perception of our Corporate Income Tax. North Dakota is often misrepresented with a stated corporate income tax rate of 10.5%, plus Water's Edge, etc. It is not very often that a footnote is included explaining the federal tax deduction and the fact that it drops the effective rate down to about 6.8%. Even if the footnote is included, it is so complicated that it becomes hard to explain. A prime example of our daily struggle with this issue is evidenced by our Department's own marketing materials. The only selling point we can use is the fact that our tax rates have not risen in 20 years. We can only talk about the specifics of the federal deduction and its impact when we have a captive audience and the opportunity to explain it face-to-face.

When we do have the chance to explain it, this is what we have to work with: North Dakota corporate income tax rates have remained unchanged since 1983. The state has a graduated scale of corporate income tax rates. Most corporations use the top rate, which is 10.5% for taxable income over $50,000. However, North Dakota is one of only five states to allow a corporation to deduct the entire amount of its federal income tax liability before calculating its state tax liability.

Thus, the "effective rate" is actually around 6.83%, assuming a 25 percent effective federal tax rate. In addition, new corporations that qualify as primary sector businesses may pay $0 in corporate income taxes for the first five years of their existence in North Dakota, if they apply for and are granted the exemption through the State Board of Equalization. Significant expansions beyond the initial location of a primary sector business may apply for additional five-year corporate income tax exemptions.

Site selectors are people that locate companies for a living. They spend every day finding the best location for the companies they work for. Most first-phase site eliminations include a matrix of factors, including state tax rates. When these site selectors see our misrepresented rate of 10.5%, which makes North Dakota one of the highest tax states in the country, they often are not interested or willing to work through the nearly impossible process of explaining the federal deduction to their clients. It is much easier to just recommend another state which shows a lower rate.

How many times this element has 'scared away' a prospect is impossible to determine. We have no idea how many companies and/or their site selectors visit our Web site or look at our marketing materials, and then choose not to follow-up with us based on their perception that our corporate income tax rate is too high. But, we do know that negative perception is out there, and we need to do all that we possibly can to change it. We also know that our nearby competitors (WY, MN, and SD) use our 10.5% corporate income tax rate against us. South Dakota gets a lot of mileage out of their "no taxes" slogan, claiming no corporate or personal state income tax. Of course, we all know that their state has to make up that lost money somewhere else, but it is a marketable tool that gives them a significant edge in this region.

Let me close by stressing that North Dakota does have a favorable tax climate; it is just that the structure is often misrepresented. What we need to do is simplify and be able to explain our corporate income tax rate. Instead of being a source of confusion and misconception, we need to be able to use it to our advantage and make it part of our tool kit for improving North Dakota's economy. What we are asking is to make our corporate income tax easily explainable so we can do a better job of marketing North Dakota as the best place to do business.

Thank you, Mr. Chairman. That concludes my testimony. I would be happy to answer any questions you may have.

Greater North Dakota Association

STATEMENT BY DALE O. ANDERSON, PRESIDENT, GNDA, REGARDING ENGROSSED HB 1471, THE NORTH DAKOTA SENATE FINANCE AND TAXATION SUB-COMMITTEE, MARCH 11, 2003.

Chairman Wardner and members of the Senate Finance and Taxation Sub-committee. I am Dale O. Anderson, President, GNDA, North Dakota State Chamber of Commerce. Thank you for this opportunity to provide testimony in opposition to Engrossed HB 1471.

For nearly eighty years the Greater North Dakota Association is the voice for business and principal advocate for positive change for North Dakota. The organization's membership is an economic and geographic cross section of North Dakota's private sector, including statewide associations and local chambers of commerce, development organizations and convention and visitors associations and public sector organizations. GNDA is governed by a Board of Directors elected by our membership. The GNDA Board Chairman is Dr. Jay Leitch, Dean, College of Business Administration, NDSU, Fargo.

There are two components to GNDA's mission which are general business climate issues and economic development or new wealth creation. There are three strategies for economic development to occur which are: (1) entrepreneurship or new business startups within North Dakota, (2) business expansion from within North Dakota and (3) business attraction from outside North Dakota into North Dakota.

Two years ago, GNDA coordinated an effort to build a more successful economy in North Dakota – the New Economy Initiative. This Initiative has been successful to help mobilize North Dakotans create new ideas, new mindsets, new growth, and to leverage technology opportunities to shape a more competitive state economy. In today's economy, information and ideas are the essential ingredients for generating wealth. Labor is needed, not so much for its muscle, but for its mind power.

On March 5, 2003 GNDA provided testimony in opposition to engrossed HB 1471. One item in that testimony dealt with water's-edge election that multi-national corporations operating in North Dakota can elect to utilize. The purpose of our testimony today is to focus more specifically on the water's-edge election and to strongly recommend that engrossed HB 1471 be amended to maintain the water's' edge election in current North Dakota corporate income tax policy. The following discussion is made available by Mr. Joseph Crosby, Council on State Taxation (COST) Washington, D.C. A copy of Mr. Crosby's letter to Governor Hoeven was attached to my testimony on March 5.

Corporate Income Tax Policy: Water's-Edge Election

- **The water's-edge election allows corporations engaged in business worldwide to apportion income to a state based on either its profits worldwide or its profits in the United States ("up to the water's edge"). Generally, once made, an election applies to future tax years absent agreement by the state to allow for a new election.**

- **Without a water's-edge election, the income of multinational corporations is subject to multiple taxation. According to Prof. Walter Hellerstein, the potential for multiple taxation results from "markedly different wage rates and property costs, varying rates of profitability, [and] dissimilar products and markets" between the U.S. and other countries.**

- **Companies that currently elect to file water's-edge presumably do so because doing otherwise would subject their income to multiple taxation. Those companies, who by definition engage in business worldwide, would have an incentive to locate facilities and personnel outside North Dakota if the water's-edge election is repealed.**

- **All sixteen states that require corporations to file a unitary combined tax return provide for a water's-edge election. By** eliminating this exemption, North Dakota would send a message that it is not interested in business investment from multinational corporations.

- The issue of worldwide combined reporting was thoroughly investigated in the early 1980s by President Ronald Reagan through the Worldwide Unitary Taxation Working Group. The Working Group included representatives of the federal government, the states (both the legislative and executive branches), and business. That group agreed that a water's-edge election be provided for both U.S. and foreign based companies.

- Repeal of the water's-edge election may result in unnecessary federal intervention in state taxation. In the words of Secretary Regan, "the use of the worldwide unitary method may interfere with the foreign commerce of the United States, so this becomes a matter of vital federal interest." In 1985, the U.S. Treasury introduced legislation that would prohibit worldwide unitary combined reporting but did not push the bill once the states began enacting water's edge elections. If that trend were reversed, foreign-based corporations and their national representatives would likely seek relief from Congress.

Thank you Chairman Wardner and members of the Senate Finance and Taxation Sub-committee for this opportunity to discuss the business community's position on engrossed HB 1471 with regard to the water's-edge election. We urge a do not pass recommendation on engrossed HB 1471. I welcome your questions.

BACKGROUND INFORMATION ON
NORTH DAKOTA'S WATER'S EDGE FILING METHOD
FOR CORPORATE INCOME TAX PURPOSES
(N.D.C.C. Chp. 57-38.4)

HISTORICAL INFORMATION:

- 1965 - North Dakota adopted the Uniform Division of Income Tax Purposes Act (UDITPA).
  - Under this Act, North Dakota adopted Worldwide Combined Reporting for unitary groups of corporations.
  - A unitary group of corporations' property, payroll, and sales within North Dakota are compared to its worldwide property, payroll, and sales to determine what portion of their income is taxable to North Dakota.
    - Unitary Business
      - Unity of Operation (contributions to or receipt of benefits from functional integration or economies of scale)
      - Unity of Ownership (common control by a single corporation)
      - Unity of Use (contributions to or receipt of benefits from centralized management and policy formation)
    - Example: Corporation A owns 100% of Corporations B and C. Corporation A mines copper in State X. Corporation A ships the copper to Corporation B in State Y, where B manufactures copper pipe. Corp B ships pipe to Corp. C's warehouse in State Z. Corp C ships the pipe to its retail hardware stores located throughout the United States.

- In response to a U.S. Supreme Court case, (Container Corp of America v. Franchise Tax Board, 463 U.S. 159 (1983)(worldwide combined reporting does not impose an undue burden on foreign commerce)), President Reagan established the Worldwide Unitary Taxation Working Group, which concluded that water's edge unitary apportionment should be applied to all corporations, foreign and domestic.[1]

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[1] The worldwide combined reporting method was again upheld as not burdening foreign commerce in 1994 by the U.S. Supreme Court in Barclays Bank v. Franchise Tax Board, 114 S.Ct. 2268 (1994). This case involved a foreign parent corporation with domestic subsidiaries.

- Under pressure from the Reagan administration's working group and from two bills introduced in Congress (S. 1974 and H.R. 3980) the States began to enact water's edge legislation.

North Dakota's Water's Edge Election (1987) (Effective for tax year 1989)

- Allows exclusion of most corporate income sourced outside the United States.

- Significant differences from Worldwide Combined Reporting (See attached)

    - 70% of Income from 80/20 Corporation's Excluded: An 80/20 corporation is an affiliated domestic corporation for which more than 80% or more of the corporation's property and payroll is assigned outside of the United States.
    - Income from Controlled Foreign Corporation (CFC) Excluded: A CFC is an affiliated corporation, incorporated outside the United States.
    - 70% of Dividends from CFC's are excluded.
    - Required to file a domestic disclosure spreadsheet.
    - Five year election
    - Not allowed a federal tax deduction – this was the "trade-off" for allowing companies to switch to a water's edge election

STATISTICAL INFORMATION

- Comparison to Other States

    - 5 States Require Worldwide Combined Reports for Unitary Groups of Corporations.
        - Alaska, California, Idaho, Montana, and North Dakota

    - 23 States Have Some Method of Domestic Combination, including the 5 States listed above.

    - 23 States Do Not Allow Combination (Separate entity filing)

    - 4 States do not have a corporate income tax

- Number of North Dakota Water's Edge Filers

1989 – 30	1996 – 142
1990 – 44	1997 – 175
1991 – 50	1998 – 199
1992 – 57	1999 – 210
1993 – 67	2000 – 215
1994 – 98	2001 – 233
1995 – 121	

ISSUES TO CONSIDER

- Perception Concerns: If the federal tax deduction is repealed and the water's edge election is not repealed , the current corporate tax brackets with the10.5% rate will have to be added to the water's edge provisions to maintain revenue neutrality.

- Continuing increase in the number of water's edge filers will further reduce corporate tax collections.

- According to tax analysts, our global economy is resulting in decreasing corporate tax revenues for those States that have domestic combination and separate entity filing. These states are unable to reach all the income that contributes to operations and profitability of the whole enterprise.

- Federal government is looking at certain concepts from worldwide combined reporting to minimize the impact from the use of foreign tax havens.

- If Current Water's Edge Filers Are Grandfathered Into The Repeal:

  - Of the 215 water's edge returns filed in tax year 2000, the elections have or will expire as follows
    - 2000 – 10
    - 2001 – 19
    - 2002 – 33
    - 2003 – 47
    - 2004 – 76
    - 2005 – 15
    - 2006 – 15

  - We are unable to determine how many corporations may have elected water's edge for the first time in 2001 or 2002

Prepared by the Office of State
Tax Commissioner for Senate Finance
and Taxation Subcommittee on
Engrossed House Bill 1471
March 11, 2003

WORLDWIDE - WATER'S EDGE COMPARISON
All Companies Are Profitable

WORLDWIDE COMBINATION

Total Federal Taxable Income	$40,000,000
Plus CFC Total Net Income	$37,000,000
Less: CFC dividends paid to Parent Corp	-$10,000,000
Total Worldwide Income	$67,000,000
Less: Federal Tax Deduction at 34%	-$13,600,000
Total Apportionable Income	$53,400,000
ND Apportionment Factor	0.037230
ND Taxable Income	$1,988,082
ND Income Tax	**$207,084**

		ND Factors
Property Factor		
ND Property	$5,000,000	0.037879
(3) Everywhere Property	$132,000,000	
ND Payroll	$250,000	0.050000
(3) Everywhere Payroll	$5,000,000	
ND Sales	$5,000,000	0.023810
(3) Everywhere Sales	$210,000,000	
Sum of Factors		0.111689
ND Apportionment Factor		0.037230

(3) Includes Parent Corp. & all Subsidiaries.

WATER'S EDGE ELECTION

Total Federal Taxable Income	$40,000,000
Less:	
Subsidiary C ("80/20")	-$5,000,000
CFC dividends paid to Parent Corp	-$10,000,000
Plus:	
30% of Subsidiary C Net Book Income	$900,000
30% of CFC dividends paid to Parent Corp	$3,000,000
	$28,900,000
ND Apportionment Factor	0.062500
ND Taxable Income	$1,806,250
ND Income Tax	**$187,991**

		ND Factors
Property Factor		
ND Property	$5,000,000	0.062500
(4) Everywhere Property	$80,000,000	
ND Payroll	$250,000	0.083333
(4) Everywhere Payroll	$3,000,000	
ND Sales	$5,000,000	0.041667
(4) Everywhere Sales	$120,000,000	
Sum of Factors		0.187500
ND Apportionment Factor		0.062500

(4) Includes Parent Corp & Subsidiaries A & B.

ASSUMPTIONS:

			Property Everywhere	Payroll Everywhere	Sales Everywhere
	Federal Income Tax Return				
	Parent Corporation	$25,000,000	$60,000,000	$2,000,000	$100,000,000
	Subsidiary A	$5,000,000	$10,000,000	$500,000	$10,000,000
	Subsidiary B	$5,000,000	$10,000,000	$500,000	$10,000,000
(1)	Subsidiary C	$5,000,000	$10,000,000	$500,000	$10,000,000
	Total Fed. Taxable Income	$40,000,000	$90,000,000	$3,500,000	$130,000,000

Note: Subsidiary C had net book income of $3,000,000

(2)	**CFCs (owned 100% by Parent Corporation) - Net Income**				
	Subsidiary D	$30,000,000	$40,000,000	$1,000,000	$70,000,000
	Subsidiary E	$7,000,000	$2,000,000	$500,000	$10,000,000
	Total Net Income	$37,000,000	$42,000,000	$1,500,000	$80,000,000

Subsidiary D pays $10,000,000 in dividends to Parent Corporation

	ND Property	ND Payroll	ND Sales
North Dakota Business of Subsidiary A	$5,000,000	$250,000	$5,000,000

(1) Subsidiary C is an "80/20" corporation. It is incorporated in the United States, but has 20% or less of its property and payroll assigned to locations in the United States. It is included in the consolidated federal income tax return.

(2) A CFC is a "controlled foreign corporation". It is incorporated outside of the United States and is not included in the consolidated federal income tax return.

WORLDWIDE - WATER'S EDGE COMPARISON
Some Foreign Operations Are Not Profitable

[redacted]

Total Federal Taxable Income	$40,000,000
Plus CFC Total Net Income	$23,000,000
Less: CFC dividends paid to Parent Corp	-$10,000,000
Total Worldwide Income	$53,000,000
Less: Federal Tax Deduction at 34%	-$13,600,000
Total Apportionable Income	$39,400,000
ND Apportionment Factor	0.037230
ND Taxable Income	$1,466,862
[redacted]	

			ND Factors
	Property Factor		
	ND Property	$5,000,000	0.037879
(3)	Everywhere Property	$132,000,000	
	ND Payroll	$250,000	0.050000
(3)	Everywhere Payroll	$5,000,000	
	ND Sales	$5,000,000	0.023810
(3)	Everywhere Sales	$210,000,000	
	Sum of Factors		0.111689
	ND Apportionment Factor		0.037230

(3) Includes Parent Corp. & all Subsidiaries.

[redacted]

Total Federal Taxable Income	$40,000,000
Less:	
Subsidiary C ("80/20")	-$5,000,000
CFC dividends paid to Parent Corp	-$10,000,000
Plus:	
30% of Subsidiary C Net Book Income	$900,000
30% of CFC dividends paid to Parent Corp	$3,000,000
	$28,900,000
ND Apportionment Factor	0.062500
ND Taxable Income	$1,806,250
[redacted]	

			ND Factors
	Property Factor		
	ND Property	$5,000,000	0.062500
(4)	Everywhere Property	$80,000,000	
	ND Payroll	$250,000	0.083333
(4)	Everywhere Payroll	$3,000,000	
	ND Sales	$5,000,000	0.041667
(4)	Everywhere Sales	$120,000,000	
	Sum of Factors		0.187500
	ND Apportionment Factor		0.062500

(4) Includes Parent Corp & Subsidiaries A & B.

ASSUMPTIONS:

	Federal Income Tax Return		Property Everywhere	Payroll Everywhere	Sales Everywhere
	Parent Corporation	$25,000,000	$60,000,000	$2,000,000	$100,000,000
	Subsidiary A	$5,000,000	$10,000,000	$500,000	$10,000,000
	Subsidiary B	$5,000,000	$10,000,000	$500,000	$10,000,000
(1)	Subsidiary C	$5,000,000	$10,000,000	$500,000	$10,000,000
	Total Fed. Taxable Income	$40,000,000	$90,000,000	$3,500,000	$130,000,000

Note: Subsidiary C had net book income of $3,000,000

(2)	CFCs (owned 100% by Parent Corporation) - Net Income				
	Subsidiary D	$30,000,000	$40,000,000	$1,000,000	$70,000,000
	Subsidiary E	-$7,000,000	$2,000,000	$500,000	$10,000,000
	Total Net Income	$23,000,000	$42,000,000	$1,500,000	$80,000,000

Subsidiary D pays $10,000,000 in dividends to Parent Corporation

	ND Property	ND Payroll	ND Sales
North Dakota Business of Subsidiary A	$5,000,000	$250,000	$5,000,000

(1) Subsidiary C is an "80/20" corporation. It is incorporated in the United States, but has 20% or less of its property and payroll assigned to locations in the United States. It is included in the consolidated federal income tax return.
(2) A CFC is a "controlled foreign corporation". It is incorporated outside of the United States and is not included in the consolidated federal income tax return.

created for sales to homes for the aged. In 1979 sales tax exemptions were created for sales to hospitals, sales of ostomy devices and supplies, and the exemption for devices to aid the handicapped was expanded. In 1981 sales of water and sales of used mobile homes were exempted from the sales tax. In 1983 sales tax exemptions were added for sales of air carrier transportation property subject to ad valorem taxation, rental of hotel or motel room or tourist court accommodations for periods of 30 or more consecutive days, and sales of aircraft subject to a special aircraft excise tax. In 1985 no new sales tax exemptions were created and the exemption was removed for sales of candy, chewing gum, carbonated beverages, powdered drink mixes, and soft drinks containing less than 70 percent fruit juice.

Testimony

The committee received testimony relating to sales tax exemptions on sales of goods for agricultural uses. A recently enacted Minnesota law reduced the Minnesota sales tax rate from six percent to two percent on sales of new farm machinery and removed the six percent sales tax on sales of farm machinery repair parts. The committee was urged to recommend that similar exemptions be enacted in North Dakota. The committee was urged to leave existing agricultural sales tax exemptions in place if no recommendation would be made to increase these exemptions.

The committee examined the rationale for each sales tax exemption and determined that the following exemptions are not likely to be removed: sales to federal, state, and local governments; sales to hospitals and nursing homes; sales of meals to shut-ins; sales to voluntary health associations; sales in interstate commerce; mobile home rentals; casual sales; sales for processing or resale; and sales to Indians. The revenue loss from these exemptions was not calculated. Fiscal estimates were obtained on revenue losses attributable to all other sales tax exemptions. Lost sales tax revenue for sales of exempt products was estimated to be from $99,405,500 to $112,484,100 annually. Lost sales tax revenue from sales of exempt services was estimated to be from $25,750,000 to $38,600,000 annually. Lost sales tax revenue from miscellaneous exemptions was estimated at $1,655,000 to $1,955,000 annually. Combining these fiscal estimates indicates a total annual sales tax revenue loss to the state of from $126,810,500 to $153,039,100. Because estimated annual sales tax revenues during the current biennium are approximately $150 to $160 million, and annual revenue loss estimates from the exemptions examined may exceed $150 million annually, it appears that the volume of sales exempt from the sales tax is approximately equal to the volume of sales subject to the sales tax.

The committee examined sales tax rates and exemptions in surrounding states and provinces. It appears that North Dakota allows more sales tax exemptions than do surrounding states and provinces but substantial similarity of major exemptions exists except in Montana, where no sales tax is imposed, and South Dakota, which has a very broad based sales tax. North Dakota and South Dakota general sales tax rates are four percent, Minnesota and Manitoba rates are six percent, and the rate in Saskatchewan is five percent.

The committee was requested to review a perceived inequity which arises in application of the sales tax exemption for educational, religious, or charitable activities and purchases by these exempt organizations. It appears that inequity exists when exempt organizations engage in regular competition with private enterprise and have the competitive advantage of a sales tax exemption. It appears that some exempt organizations engage in continuing fundraising sales campaigns, which compete with private business and go beyond the perceived intent of the exemption for educational, religious, or charitable activities.

Recommendation

The committee recommends Senate Bill No. 2077 to provide that the exemption otherwise available for educational, religious, or charitable activities does not apply to consistent retail sales that are in direct competition with retailers. The exemption would remain for casual sales, such as infrequent fundraising activities and similar functions. In addition, the sales tax exemption for purchases by hospitals and similar institutions is limited to purchases made for the use or benefit of a patient or occupant of the facility.

Committee members commented that proposals for further exemptions from sales taxes should be strictly scrutinized. Existing sales tax exemptions were found to be adequately justified.

UNITARY TAXATION

Background

Unitary taxation is formula apportionment of income of related corporations for corporate income tax purposes. The goal of formula apportionment is to determine how much corporate income is properly taxable within the state for corporations operating across state borders. Due to the complexity of interrelationships that may exist between related corporations, the difficulty of establishing the situs of taxable income of corporations and affiliates operating across state boundaries, the various methods used by states to apportion corporate income for income tax purposes, and the resulting dissatisfaction of states and corporate taxpayers, the corporate income tax imposed by state governments has been problematic since the earliest days of imposition of corporate income taxes by states.

In North Dakota the state corporate income tax was first imposed in 1919. From the beginning of imposition of corporate income taxes, the state has used apportionment to determine the proportion of corporate income attributable to North Dakota for tax purposes. Legal challenges to North Dakota's apportionment approach have occurred from the early 1920s to the present.

North Dakota's experience with challenges to its method of apportioning corporate income is not unique. All states imposing corporate income taxes had similar challenges. The states imposing corporate income taxes used similar but different methods of apportioning corporate income. The diversity of state income apportionment approaches made it likely that either more or less than 100 percent of corporate income was taxable by states and provided incentives f[illegible] -ious means of legal tax avoidance. This proved [illegible] in unacceptable situation to both states and corporate taxpayers. In an attempt to address the problem of diverse approaches, the National Conference of Commissioners on Uniform State Laws proposed the Uniform Division of Income Tax Act in 1957 and the Act was enacted in North Dakota in 1965. The Uniform Division of Income Tax Act is codified as North Dakota Century Code Chapter 57-38.1 and has been amended once since 1965. Under this Act affiliated corporations' property, payroll, and sales within North Dakota are compared to their property, payroll, and sales worldwide to determine what portion of their income is taxable in North Dakota. Although the Act does not specify worldwide unitary apportionment is to be used, that method has been employed in North Dakota since 1973 under an administrative interpretation by the Tax Commissioner.

As of 1984, 45 states imposed corporate income taxes and all of those states utilized formula apportionment to divide taxable income of a single corporation operating across state boundaries. Twenty-three of the corporate income tax states used the apportionment method for allocating income of multicompany corporations operating across state lines through subsidiaries. Eleven of these 23 states applied their apportionment formula to the combined [illegible]e and business activities of related United [illegible]s corporations forming a unitary business. The remaining 12 of these 23 states, including North Dakota, utilized worldwide unitary taxation, which included foreign activities that are part of a unitary business.

It was the worldwide unitary method of apportioning corporate income which drew the wrath of domestic and foreign-based multinational corporations and foreign governments. A significant corporate income tax case decided by the United States Supreme Court, Container Corporation of America v. Franchise Tax Board, 463 U.S. 159 (1983), held that the worldwide unitary combination method was constitutionally permissible. After this decision multinational corporations and foreign governments assailed the President with requests that the federal government support legislation to limit or prohibit state use of worldwide unitary taxation. The administration responded by establishing in July 1983 a Cabinet Counsel on Economic Affairs Working Group to identify federal and state interests in the worldwide unitary method of taxation. In September 1983 the President established the Worldwide Unitary Taxation Working Group, chaired by Treasury Secretary Donald T. Regan. The group was composed of federal and state government [illegible]sentatives and business leaders and the group [illegible]nable to agree fully on all areas of discussion. [illegible] final report of that group was issued in August 1984. The working group agreed on three principles:

1. Water's edge unitary combination apportionment should be applied to both United States and foreign-based companies.
2. Increased federal administrative assistance and cooperation with the states should be provided to promote full taxpayer disclosure and accountability.
3. Competitive balance should be established under state tax policies for United States multinationals, foreign multinationals, and purely domestic businesses.

Only these broad principles were agreed upon by the working group and remaining issues were left for resolution at the state level.

With pressure from the administration and from two bills introduced in Congress (S. 1974 and H.R. 3980), nine of the 12 states that had used worldwide unitary apportionment in 1984 have receded to water's edge unitary apportionment as of November 1986. The most recent and most notable of these nine states is California, which was a primary concern of foreign governments due to the level of corporate activity in that state. North Dakota is one of the three remaining states, with Alaska and Montana, which still use worldwide unitary apportionment for corporate income tax purposes.

During the 1985 legislative session, Senate Bill No. 2343 was considered by the North Dakota Legislative Assembly. This bill would have changed North Dakota law to provide for water's edge unitary taxation. The bill passed in the Senate and was substantially amended before failing to pass in the House of Representatives.

Although the majority of states that had used worldwide unitary apportionment in 1984 have now gone to water's edge unitary apportionment, several areas of difference exist among the laws of these states. Probably the most significant areas of difference and concern are definition of what constitutes a unitary group, treatment of dividends received from foreign corporations, and treatment of income from domestic corporations that have 80 percent or more of their property, payroll, and sales in foreign countries (called 80/20 corporations).

Testimony

The Tax Commissioner told the committee that, although North Dakota's use of worldwide apportionment is by administrative decision, he would not administratively revert to a water's edge approach. He said the matter is too significant for administrative resolution and should be decided by the Legislative Assembly. The committee considered bill drafts patterned after recent unitary legislation in Oregon, Colorado, and Idaho, as well as 1985 Senate Bill No. 2343, as amended by the House of Representatives. The consensus of business representatives was that the bill patterned after the Colorado approach was most favored, the bill patterned after the Idaho approach was also acceptable, but the bill drafts patterned after the Oregon approach and 1985 Senate Bill No. 2343 were unacceptable and would not meet minimum standards in pending federal legislation. The primary concerns of business representatives were with treatment of 80/20 corporations and foreign corporations. Business representatives recommended that 80/20 corporations and foreign source dividends should be taxed equally because these businesses compete on the same basis without regard to choice of the place of incorporation.

Under the worldwide unitary combination approach presently used in North Dakota, income of all companies with greater than 50 percent ownership by common corporate interests, 80/20 corporation income, and foreign dividend income are included in the unitary group. Under 1985 Senate Bill No. 2343 as introduced income of all domestic corporations with greater than 50 percent ownership by common corporate or noncorporate interests, 80/20 corporation income, and foreign dividend income are included in the unitary group. Under 1985 Senate Bill No. 2343 as amended by the House of Representatives income of all domestic corporations with greater than 50 percent common corporate or noncorporate ownership is included in the unitary group, 80/20 corporation income is excluded, and foreign dividend income is excluded if the foreign corporation is 80 percent or more owned by members of the unitary group.

Under the Colorado approach a line of business determination defines the unitary group, 80/20 corporation income is excluded, and foreign dividends are excluded if the foreign effective tax rate is 46 percent or greater. Under the Oregon approach, line of business corporations are included in the unitary group if they have been included in a federal consolidated return, 80/20 corporations are included in the group if they are 80 percent or more owned by interests within the group, and foreign dividends are 85 percent excluded. Under the Idaho approach, corporations eligible for inclusion in a federal consolidated return are included in the unitary group and income from 80/20 corporations and foreign dividends is 85 percent excluded.

Because a significant revenue loss to the state was anticipated from reverting from worldwide to water's edge unitary combination, the committee requested calculation of the fiscal impact of all bill draft approaches under consideration. Representatives of the Tax Commissioner estimated fiscal losses of $3.9 million to $6.2 million under the approach in 1985 Senate Bill No. 2343 as introduced; $14.9 million to $18.1 million under 1985 Senate Bill No. 2343 as amended by the House of Representatives; $12.6 million to $15.7 million under the Colorado approach; $9.4 million to $11 million under the Oregon approach; and $13.4 million to $14.9 million under the Idaho approach. All of these fiscal calculations were done under the assumption that the approach in question would be in place for the entire 1987-89 biennium and the estimates are based on comparison to current worldwide unitary taxation based on revenue projections for the 1985-87 biennium. Business representatives disputed the fiscal estimates as being too high in terms of revenue lost.

Recommendation

The committee recommends House Bill No. 1064, which is patterned after legislation recently enacted in Idaho. The most substantial difference between the bill recommended and the legislation enacted in Idaho is that the bill draft provides for mandatory unitary filing on a water's edge basis while the Idaho legislation provides the option for taxpayers to file on a worldwide combination basis.

The principal provisions of the bill are that corporations included in the water's edge unitary group are any corporations more than 50 percent of the voting stock of which are owned directly or indirectly by another corporate member of the water's edge combined group. Any corporation subject to the income tax must apportion its income under the bill. Included in apportionment is income from any of the following entities: any affiliated corporation eligible for inclusion in a federal consolidated return which has more than 20 percent of its payroll and property assigned to locations inside the 50 states and District of Columbia; domestic international sales corporations; foreign sales corporations; export trade corporations; foreign corporations disposing of a United States real property interest; tax haven corporations; and a foreign corporation with more than 20 percent of its payroll and property assignable to locations within the United States. Dividends received from foreign corporations and income from 80/20 corporations are subject to apportionment but 85 percent of income from both sources is excluded. The bill is effective for taxable years beginning after December 31, 1988, except that the bill may become effective earlier if federal legislation is enacted requiring corporations to file with the Internal Revenue Service a domestic disclosure spreadsheet providing full disclosure as to income reported to each state, the state tax liability, the method used for apportioning or allocating income to the states, and any other information as may be necessary to determine properly the amount of taxes due to each state and to identify the water's edge corporate group and providing that this information be made available to the states. Because of the contingent effective date clause and the fact that the bill may not become effective until taxable year 1989, this bill may have little or no fiscal effect during the 1987-89 biennium. If the first year for which the bill is effective is the 1989 taxable year, no tax liability would accrue for corporations filing under the bill until January 1, 1990, which is beyond the 1987-89 biennium. For this reason, only minimal fiscal effect may occur during the 1987-89 biennium which would be attributable to reduced estimated corporate income tax payments.

Among the significant considerations of the committee in recommending the bill is the equal treatment of 80/20 corporations and income received in foreign dividends. The decision of whether to incorporate in a foreign country or in the United States is often based on factors other than taxation. 80/20 corporations are in direct competition with foreign corporations, and the bill taxes such entities on an equal basis.

The bill appears to comply with minimum requirements contained in pending federal legislation.

The bill contains a statement of intent to the effect that any revenue loss to the state from the bill should be offset by appropriate adjustments to corporate income tax rates or deductions. The committee was unable to propose appropriate changes because of a lack of information on corporate income tax revenue for future bienniums under new federal tax law. Necessary information should be available during the '7 legislative session.

ENERGY TAXATION

Background

North Dakota imposes four separate direct taxes upon the mining or conversion of energy sources. Oil and gas are taxed under the oil and gas gross production tax enacted in 1953. Oil is also taxed by the oil extraction tax created by an initiated measure approved in 1980. The coal severance tax and the coal conversion facilities privilege tax, both enacted in 1975, are the two taxes imposed on the coal industry.

Present tax rates are five percent for the oil and gas gross production tax and 6.5 percent for the oil extraction tax. The coal severance tax rate is tied to increases in the wholesale price index and is presently at a rate of $1.04 per ton. For electrical generating plants the present coal conversion tax rate is one-half of one mill per kilowatt hour of electricity produced for the purpose of sale. For coal gasification plants constructed prior to July 1, 1985, the coal conversion tax is either 2.5 percent of gross receipts or 15 cents per 1,000 cubic feet of synthetic natural gas, whichever is greater. For coal gasification plants constructed after July 1, 1985, the rate of tax is either 2.5 percent of gross receipts or 10 cents per 1,000 feet of synthetic natural gas, whichever is greater. These ergy sources or conversion facilities are not subject sales taxes or property taxes.

The incidence of the energy boom of the 1970s and early 1980s heightened interest in severance taxes as a source of general fund revenue for the state. The creation of coal severance and conversion taxes in 1975 and the oil extraction tax in 1980 increased state reliance on revenue from taxation of energy sources. Dependence of the state general fund on revenue from these tax sources is evidenced by the fact that estimates for the 1985-87 biennium called for almost one-fourth of all state general fund revenue to come from oil and gas gross production taxes, oil extraction taxes, coal severance taxes, and coal conversion taxes.

The recent worldwide glut of oil has resulted in substantial decreases in the price of oil. Oil price decreases have been felt in North Dakota in terms of lost employment, lost exploration activity, lost state and political subdivision revenue, and difficulties of the state and political subdivisions to cope with the rapidly changing energy industry. Falling prices for sub-bituminous coal in neighboring states have increased competitive pressure on the North Dakota lignite industry, causing problems similar to those experienced because of the difficulties of the oil industry.

The chairman of the Legislative Council assigned the committee the duty of studying taxes on oil and as and lignite coal, including the correlation between e taxes on mineral resources and the development of those resources. In addition, the Legislative Council contracted with the University of North Dakota Bureau of Business and Economic Research to conduct an independent study of the effect of severance taxes on North Dakota industries, and to report its findings to the Taxation Committee.

Testimony

North Dakota Lignite Council representatives proposed reducing the coal severance tax rate from $1.04 to $.60 per ton, removing the escalator clause in the coal severance tax rate formula, and adjusting distribution of coal severance tax revenues. Several arguments were advanced in favor of the reduced coal severance tax rate. In 1986 North Dakota lignite production will be approximately 2 million tons below 1985 production levels, reversing a steady increase in production during the last decade. The principal reason given for this decline in production was that North Dakota lignite has become increasingly less competitive in the market as prices of higher grade coal from Montana and Wyoming have fallen. It was estimated that 500 jobs in the coal industry have been lost during the past year in North Dakota due to production declines and efforts of the industry to reduce costs. An additional 2,300 jobs indirectly related to coal production were also estimated to have been lost in North Dakota as a result of decreased coal production. Lignite industry representatives indicated that they are not relying solely on severance tax relief to aid the industry in its competitive struggle. Efforts are presently underway to reduce reclamation costs, reduce mining costs by increasing productivity, reduce federal coal royalties, reduce state severance taxes, and restrict or impede the flow of Canadian hydroelectricity into the North Dakota market. Concern was expressed for future production levels because of likely increases in competition from Montana and Wyoming coal and great increases in competition from Canadian hydroelectricity. It was stated that the North Dakota lignite industry has excess capacity and, if that excess capacity is to be used, the cost of North Dakota lignite must be reduced to compete in an increasingly competitive market.

Lignite industry representatives presented information on comparative tax rates per ton for coal mined in North Dakota, Wyoming, and Montana. These comparisons show that the rate of tax per ton of coal in North Dakota is less than that in Wyoming and Montana, both of which impose property taxes in addition to severance taxes. However, Wyoming and Montana coal is a higher grade of coal than lignite, and produces more energy per ton of coal. Thus, North Dakota's coal severance tax is higher than Montana's or Wyoming's, on the basis of energy produced per ton of coal.

The committee toured the coal production area of North Dakota and received substantial testimony from representatives of political subdivisions in the coal production area. Testimony from these individuals was generally to the effect that political subdivisions in the production area support the reduction in coal severance taxes to assist the lignite industry but oppose the reduction in impact funding which was proposed by the Lignite Council. Extensive testimony was received on tax levy and indebtedness levels of subdivisions in the coal production area in support of arguments that coal impact is still

Interim minutes are available upon request.

Alliance OF AUTOMOBILE MANUFACTURERS

February 20, 2003

The Honorable Tom Seymour
Senator
Senate Finance and Taxation Committee
1104 14th Avenue SW
Minot, ND 58701

Dear Senator Seymour:

The Alliance of Automobile Manufacturers welcomes the opportunity to comment on House Bill 1471 which would reduce the corporate income tax rate to encourage investment in the State of North Dakota. Our members oppose this legislation as currently written because it would eliminate the water's-edge election for corporations that conduct business both within North Dakota and outside the State. The elimination of the water's-edge election would create administrative and compliance burdens for good corporate citizens and may utimately discourage the corporate growth that the legislation intends to promote.

The Alliance of Automobile Manufacturers (Alliance) is a trade association of 10 car and light truck manufacturers who account for more than 90 percent of U.S. vehicle sales. Member companies, which include BMW Group, DaimlerChrysler, Ford Motor Company, General Motors, Mazda, Mitsubishi Motors, Nissan, Porsche, Toyota and Volkswagen, employ more than 620,000 Americans at 250 facilities in 35 states.

North Dakota's corporate taxpayers will be laboring unfairly under requirements that no longer exist in other states. As currently written, House Bill 1471 would require corporations doing business in North Dakota to calculate their worldwide income when filing corporate tax returns in the State. Requiring multinational taxpayers to include non-U.S. corporations that are part of the unitary group in the companies' tax returns creates a compliance burden on our membership. During the early 1980's, twelve states did not allow a water's-edge election. All twelve changed their laws shortly afterward to provide for such an election. With the exception of North Dakota, none of those states have since contemplated eliminating that election.

BMW Group • Daimler Chrysler • Ford Motor Company • General Motors
Mazda • Mitsubishi Motors • Nissan • Porsche • Toyota • Volkswagen

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The Alliance strongly urges that the existing water's-edge election be retained. As good corporate citizens, the Alliance is concerned that, without a tax climate designed to encourage corporate growth, North Dakota's corporate taxpayers will be laboring unfairly under burdens not borne by corporations operating in other states.

We would most appreciate your support to amend HB 1471 so as to retain the existing water's-edge election.

Sincerely,

Kris Kiser

Kris Kiser
Vice President of State Affairs

1P

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3-24-03

Alternative Proposal – HB 1471
Discussion Points

Goal of Legislation

- To remove the perception of high corporate income tax rates by repealing the federal tax deduction and lowering the rates as much as is feasible
- To offer a tool (lower corporate income tax rates) to economic developers
- To be as close to revenue-neutral to the state as possible, for this budget period and the next

Components of the Proposal

- Repeal the corporate federal tax deduction effective tax year 2004 (This impacts the second year of the 2003-05 biennium and beyond)
- Lower all rates and remove one bracket (from 6 brackets to 5), imposing a top rate of 7%, effective for tax year 2004
  - Retaining 5 brackets continues to allow lower rates for small businesses
  - A top rate of 7% compares favorably with other states
  - These rates represent an overall tax decrease of approx. $2.3 million per year
- Eliminate the net operating loss (NOL) carryback option effective tax year 2003 while continuing to allow the NOL carryforward provisions
  - NOL carrybacks result in refunds. Eliminating the option results in less refunds of tax and interest and time savings for audit staff
  - Taxpayers will continue to be allowed the full offset of their loss as they carry it forward and offset future income for up to 20 years
  - The immediate savings of refund dollars, estimated at $1.8 million per year, contributes to the closing the fiscal gap with the proposed 7% rate
  - 24 states do not allow NOL carrybacks; most do allow carryforwards
- Repeal the Water's Edge option effective for new elections in tax year 2003
  - Taxpayers currently within a 5-year election will be allowed to use the method until their election expires
  - If the method is not repealed, a 10.5% rate for water's edge filers will continue to be in the law resulting in a continuation of the perception problem of the state having high corporate income tax rates
  - When originally debated, the water's edge method was presented as an economic development tool. However, major users of the method are not new companies locating in the state because of the filing method
  - Potentially, there is greater economic development value to the lower 7% corporate rate than a water's edge filing method (developers and site selectors are usually unfamiliar with the term "Water's Edge Method")
  - Repeal of the method will safeguard the state from the potential abuse of corporate offshore tax havens
  - Other states, and the IRS, are considering similar action
  - When grandfathered in, the repeal contributes $300,000 to closing the fiscal gap and allowing a 7% top rate

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Alternative Proposal - HB 1471
Fiscal Analysis

	2003-05 Biennium	2005-07 Biennium
Effective Tax Year 2004		
Repeal Corp Federal Tax Deduction		
Reduce to five brackets (eliminate top bracket)		
Top Rate of 7.0% on $30,000 of taxable income		
Estimated Fiscal Impact	(2,344,000)	(4,688,000)
Effective Tax Year 2003		
Eliminate NOL carryback provisions		
(24 states do not allow NOL carrybacks)		
(Must be allowed on Tax Year 02- FY 03/04)		
Continue to allow carryforwards like Feds		
Estimated Fiscal Impact	1,800,000	3,600,000
Effective for New Elections Tax Year 2003		
Eliminate new Water's Edge elections		
Beginning with Tax Year 2003		
Allow all taxpayers to finish current election		
(Needed to avoid a published 10.5% rate)		
Estimated Fiscal Impact	300,000	800,000
Net Fiscal Impact	(244,000)	(288,000)

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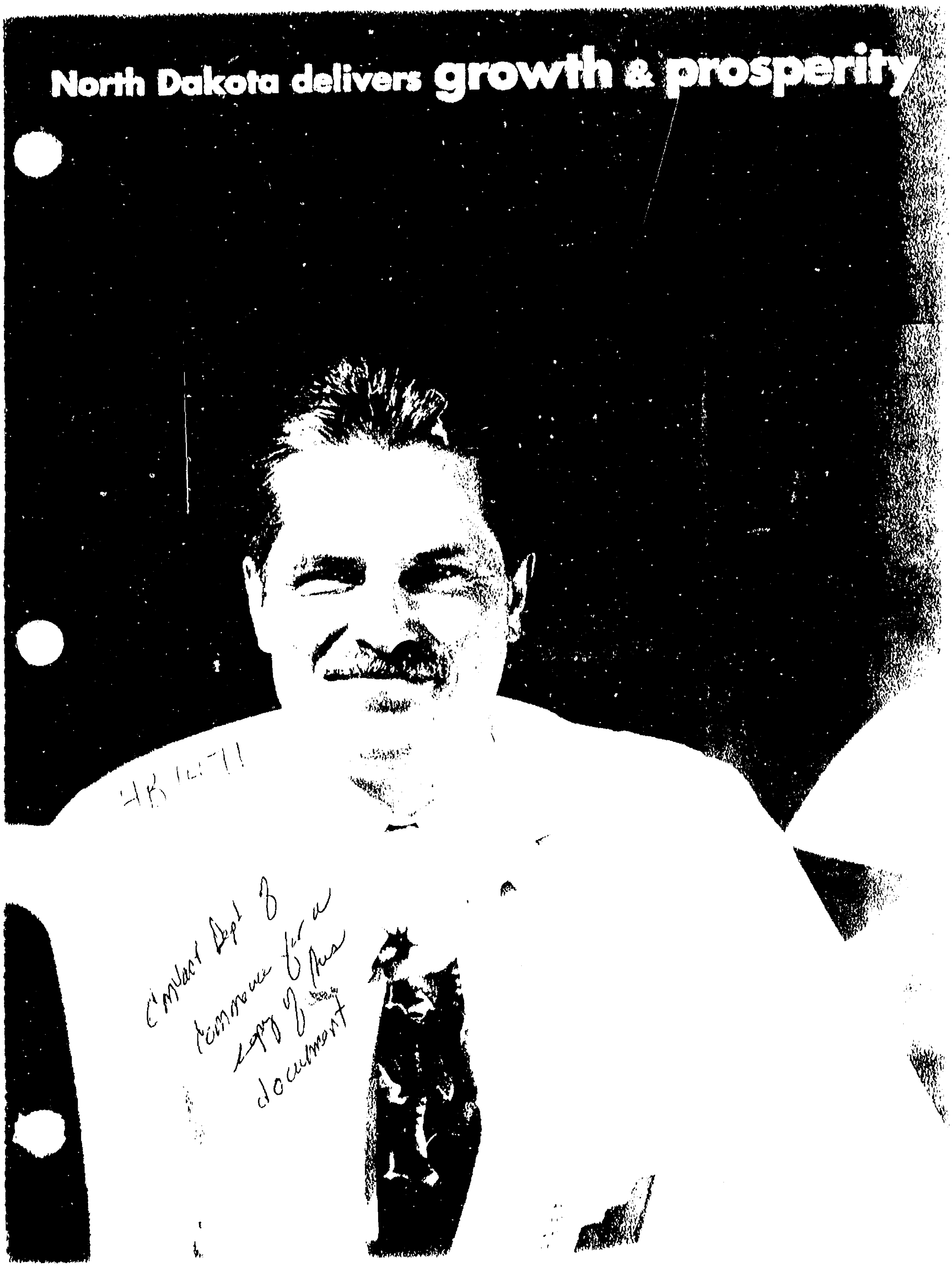

HB 1071

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