ROUGH DRAFT:
Prepared by the Legislative Council staff for the Taxation Committee
November 2007

Sixty-first
Legislative Assembly
of North Dakota

Introduced by

A BILL for an Act to amend and reenact subsection 4 of section 10-33-124, subsection 5 of section 11-37-08, section 37-28-07, subsections 1 and 3 of section 40-63-04, section 40-63-06, subsection 4 of section 40-63-07, subsections 1 and 2 of section 57-38-01.7, subsections 1 and 4 of section 57-38-01.8, sections 57-38-01.14, 57-38-01.16, and 57-38-01.17, subsection 1 of section 57-38-01.20, subsections 2 and 4 of section 57-38-01.21, sections 57-38-01.22, 57-38-01.23, 57-38-01.24, 57-38-01.25, 57-38-01.26, subsection 6 of section 57-38-01.27, subsection 1 of section 57-38-01.29, subsection 1 of sections 57-38-01.30, and sections 57-38-30.3, 57-38-30.5, 57-38-31, 57-38.5-03 and 57-38.6-03 of the North Dakota Century Code, relating to elimination of the optional long-form income tax return; to repeal sections 57-38-01.2, 57-38-01.18, 57-38-02, 57-38-03, 57-38-06.1, 57-38-29, 57-38-29.2, 57-38-30.4, 57-38-67, 57-38-68, 57-38-69, 57-38-70, 57-38-71, 57-38-72, 57-38-73, and 57-38-74 of the North Dakota Century Code, relating to elimination of the optional long-form income tax return; and to provide an effective date.

BE IT ENACTED BY THE LEGISLATIVE ASSEMBLY OF NORTH DAKOTA:

SECTION 1. AMENDMENT. Subsection 4 of section 10-33-124 of the North Dakota Century Code is amended and reenacted as follows:

4. a. ~~An individual or a~~ <u>A</u> corporation that buys membership in, or pays dues or contributes to, a nonprofit development corporation is entitled to an income tax credit <u>against the tax liability under section 57-38-30</u> equal to twenty-five percent of the amount paid.

b. This credit may not be claimed by ~~an individual who elects to file an income tax return under section 57-38-30.3 or by~~ a corporation that is recognized as a subchapter S corporation under section 57-38-01.4.

c. No taxpayer is entitled to more than two thousand dollars in total income tax credits under this section.

d. The amount of the credit under this section in excess of the taxpayer's income tax liability may be carried forward for up to seven taxable years.

SECTION 2. AMENDMENT. Subsection 5 of section 11-37-08 of the North Dakota Century Code is amended and reenacted as follows:

5. Bonds issued by a commerce authority under this section are declared to be issued for an essential public government purpose, and together with interest and income on the bonds, are exempt from all individual and corporate taxes imposed under sections 57-35.3-03, ~~57-38-29,~~ 57-38-30, and 57-38-30.3.

SECTION 3. AMENDMENT. Section 37-28-07 of the North Dakota Century Code is amended and reenacted as follows:

37-28-07. Payments exempt from taxation and from execution - Assignments void - Debts to state and political subdivisions not deducted. Payments under this chapter are exempt from all state and local taxes, including taxes determined under section 57-38-29 or 57-38-30.3, and from levy, garnishment, attachment, and sale on execution. Any pledge, mortgage, sale, assignment, or transfer of any right, claim, or interest in any claim or payment under this chapter is void and payment to the veteran may not be denied because of any sums owed to the state or any political subdivisions, except as provided in section 37-26-05.

SECTION 4. AMENDMENT. Subsections 1 and 3 of section 40-63-04 of the North Dakota Century Code are amended and reenacted as follows:

1. An individual taxpayer who purchases or rehabilitates single-family residential property for the individual's primary place of residence as a zone project is exempt from up to ten thousand dollars of personal income tax liability as determined under section ~~57-38-29 or~~ 57-38-30.3 for five taxable years beginning with the date of occupancy or completion of rehabilitation.

3. If the cost of a new business purchase or expansion of an existing business, approved as a zone project, exceeds seventy-five thousand dollars, and the business is located in a city with a population of not more than two thousand five hundred, an individual taxpayer may, in lieu of the exemption provided in subsection 2, elect to take an income tax exemption of up to two thousand dollars

of personal income tax liability as determined under section ~~57-38-29 or~~ 57-38-30.3. The election must be made on the taxpayer's zone project application. The election is irrevocable and binding for the duration of the exemptions provided in subsection 2 or 3. If no election is made on the zone project application, the taxpayer is only eligible for the exemption provided in subsection 2.

SECTION 5. AMENDMENT. Section 40-63-06 of the North Dakota Century Code is amended and reenacted as follows:

40-63-06. Historic preservation and renovation tax credit. A credit against state tax liability as determined under sections 57-35.3-03, ~~57-38-29,~~ 57-38-30, and 57-38-30.3 is allowed for investments in the historic preservation or renovation of property within the renaissance zone. The amount of the credit is twenty-five percent of the amount invested, up to a maximum of two hundred fifty thousand dollars. The credit may be claimed in the year in which the preservation or renovation is completed. Any excess credit may be carried forward for a period of up to five taxable years.

SECTION 6. AMENDMENT. Subsection 4 of section 40-63-07 of the North Dakota Century Code is amended and reenacted as follows:

4. A credit against state tax liability as determined under section 57-35.3-03, ~~57-38-29,~~ 57-38-30, or 57-38-30.3 is allowed for investments in a renaissance fund organization. The amount of the credit is fifty percent of the amount invested in the renaissance fund organization during the taxable year. Any amount of credit which exceeds a taxpayer's tax liability for the taxable year may be carried forward for up to five taxable years after the taxable year in which the investment was made.

SECTION 7. AMENDMENT. Subsections 1 and 2 of section 57-38-01.7 of the North Dakota Century Code are amended and reenacted as follows:

1. At the election of the taxpayer, there must be allowed, subject to the applicable limitations provided in this subsection, as a credit against the income tax ~~imposed by this chapter~~ <u>liability under section 57-38-30</u> for the taxable year, an amount equal to fifty percent of the aggregate amount of charitable contributions made by the taxpayer during the year to nonprofit private institutions of higher education located within the state or to the North Dakota independent college fund.

~~a.~~ ~~In the case of a taxpayer other than a corporation, the amount allowable as a credit under this subsection for any taxable year may not exceed forty percent of the taxpayer's total income tax under this chapter for the year, or two hundred fifty dollars, whichever is less.~~

~~b.~~ ~~In the case of a corporation, the~~ The amount allowable as a credit under this subsection for any taxable year may not exceed twenty percent of the corporation's total income tax under this chapter for the year, or two thousand five hundred dollars, whichever is less.

2. At the election of the taxpayer, there must be allowed, subject to the applicable limitations provided in this subsection, as a credit against the income tax ~~imposed by this chapter~~ liability under section 57-38-30 for the taxable year, an amount equal to fifty percent of the aggregate amount of charitable contributions made by the taxpayer during the year directly to nonprofit private institutions of secondary education, located within the state.

~~a.~~ ~~In the case of a taxpayer other than a corporation, the amount allowable as a credit under this subsection for any taxable year may not exceed forty percent of the taxpayer's total income tax under this chapter for the year, or two hundred fifty dollars, whichever is less.~~

~~b.~~ ~~In the case of a corporation, the~~ The amount allowable as a credit under this subsection for any taxable year may not exceed twenty percent of the corporation's total income tax under this chapter for the year, or two thousand five hundred dollars, whichever is less.

SECTION 8. AMENDMENT. Subsections 1 and 4 of section 57-38-01.8 of the North Dakota Century Code are amended and reenacted as follows:

1. ~~Any~~ A taxpayer filing a North Dakota income tax return pursuant to the provisions of this chapter may claim a credit against the tax liability under section 57-38-30 for the cost of a geothermal, solar, or wind energy device installed before January 1, 2011, in a building or on property owned or leased by the taxpayer in North Dakota. The credit provided in this section for a device installed before January 1, 2001, must be in an amount equal to five percent per year for three years, and for a device installed after December 31, 2000, must be in an amount equal to three

percent per year for five years of the actual cost of acquisition and installation of the geothermal, solar, or wind energy device and must be subtracted from any income tax liability of the taxpayer as determined pursuant to the provisions of this chapter.

4. A partnership, subchapter S corporation, limited partnership, limited liability company, or any other passthrough entity that installs a geothermal, solar, or wind energy device in a building or on property owned or leased by the passthrough entity must be considered to be the taxpayer for purposes of this section, and the amount of the credit allowed with respect to the entity's investments must be determined at the passthrough entity level. The amount of the total credit determined at the entity level must be passed through to the corporate partners, shareholders, or members in proportion to their respective interests in the passthrough entity.

SECTION 9. AMENDMENT. Section 57-38-01.14 of the North Dakota Century Code is amended and reenacted as follows:

57-38-01.14. No gain recognized on property subject to eminent domain sale or transfer. If any private property, through the exercise of eminent domain, is involuntarily converted into property of either like or unlike kind, no gain, either ordinary or capital, may be recognized for corporate income tax purposes.

SECTION 10. AMENDMENT. Section 57-38-01.16 of the North Dakota Century Code is amended and reenacted as follows:

57-38-01.16. Income tax credit for employment of developmentally disabled or chronically mentally ill persons. ~~Any~~ A taxpayer filing an income tax return under this chapter~~, except a return on which liability is determined under section 57-38-30.3,~~ may claim a credit against the tax liability imposed under section 57-38-30 for a portion of the wages paid to a developmentally disabled or chronically mentally ill employee. The credit allowed under this section equals five percent of up to six thousand dollars in wages paid during the first twelve months of employment by the taxpayer for each developmentally disabled or chronically mentally ill employee of the taxpayer. Only wages actually paid during the taxpayer's taxable year may be considered for purposes of this section. An employee of a subcontractor is considered an employee of the contractor to the extent of any wages paid under the contract.

The total of credits allowed under this section may not exceed fifty percent of the taxpayer's liability under this chapter.

SECTION 11. AMENDMENT. Section 57-38-01.17 of the North Dakota Century Code is amended and reenacted as follows:

57-38-01.17. Credit for investments in development corporations. ~~An individual, estate, trust, or~~ A corporation is allowed, as a credit against a tax otherwise due under section ~~57-38-29 or~~ 57-38-30, the credit for buying membership in, or paying dues or contributions to, a certified nonprofit development corporation as provided in section 10-33-124.

SECTION 12. AMENDMENT. Subsection 1 of section 57-38-01.20 of the North Dakota Century Code is amended and reenacted as follows:

1. An individual is entitled to a credit against the tax imposed under section ~~57-38-29 or~~ 57-38-30.3 in the amount of qualified care expenses under this section paid by the individual for the care of a qualifying family member during the taxable year.

SECTION 13. AMENDMENT. Subsections 2 and 4 of section 57-38-01.21 of the North Dakota Century Code are amended and reenacted as follows:

57-38-01.21. Planned gifts and qualified endowments credit - Definitions.

2. An individual is allowed a tax credit against the tax imposed by section 57-38-29 or 57-38-30.3 in an amount equal to forty percent of the present value of the aggregate amount of the charitable gift portion of planned gifts made by the taxpayer during the year to a qualified nonprofit organization or qualified endowment. The maximum credit that may be claimed under this subsection for contributions made in a taxable year is ten thousand dollars, or twenty thousand dollars for married individuals filing a joint return. The credit allowed under this section may not exceed the taxpayer's income tax liability.

4. An estate or trust is allowed a tax credit in an amount equal to forty percent of a charitable gift to a qualified endowment. The maximum credit allowed under this subsection for contributions made in a taxable year is ten thousand dollars. The allowable credit must be apportioned to the estate or trust and to its beneficiaries on the basis of the income of the estate or trust allocable to each, and the beneficiaries may claim their share of the credit against the tax imposed by section 57-38-29, 57-38-30, or 57-38-30.3. A beneficiary may claim the credit only in the

beneficiary's taxable year in which the taxable year of the estate or trust ends. Subsections 6 and 7 apply to the estate or trust and its beneficiaries with respect to their respective shares of the apportioned credit.

SECTION 14. AMENDMENT. Section 57-38-01.22 of the North Dakota Century Code is amended and reenacted as follows:

57-38-01.22. Income tax credit for blending of biodiesel fuel. A fuel supplier licensed pursuant to section 57-43.2-05 who blends biodiesel fuel is entitled to a credit against tax liability determined under section 57-38-29, 57-38-30, or 57-38-30.3 in the amount of five cents per gallon [3.79 liters] of biodiesel fuel of at least five percent blend, otherwise known as B5. For purposes of this section, "biodiesel" means fuel meeting the specifications adopted by the American society for testing and materials. The credit under this section may not exceed the taxpayer's liability as determined under this chapter for the taxable year and each year's unused credit amount may be carried forward for up to five taxable years.

A partnership, subchapter S corporation, limited partnership, limited liability company, or any other passthrough entity entitled to the credit under this section must be considered to be the taxpayer for purposes of this section, and the amount of the credit allowed must be determined at the passthrough entity level. The amount of the total credit determined at the entity level must be passed through to the partners, shareholders, or members in proportion to their respective interests in the passthrough entity.

SECTION 15. AMENDMENT. Section 57-38-01.23 of the North Dakota Century Code is amended and reenacted as follows:

57-38-01.23. Income tax credit for biodiesel sales equipment costs. A seller of biodiesel fuel is entitled to a credit against tax liability determined under section 57-38-29, 57-38-30, or 57-38-30.3 in the amount of ten percent per year for five years of the biodiesel fuel seller's direct costs incurred after December 31, 2004, to adapt or add equipment to a facility, licensed under section 57-43.2-05, to enable the facility to sell diesel fuel containing at least two percent biodiesel fuel by volume. For purposes of this section, "biodiesel fuel" means fuel meeting the specifications adopted by the American society for testing and materials. The credit under this section may not exceed a taxpayer's liability as determined under this chapter for the taxable year and each year's unused credit amount may be carried forward for up to five taxable years. A biodiesel fuel seller is limited to fifty thousand dollars in the cumulative amount of credits under this section for all taxable years. A biodiesel fuel seller may not claim a credit under this section for any taxable year before the taxable year in which the facility begins selling biodiesel fuel containing at least two percent biodiesel fuel by volume, but eligible costs incurred before the taxable year sales begin may be claimed for purposes of the credit under this section for taxable years on or after the taxable year sales of biodiesel fuel begin.

A partnership, subchapter S corporation, limited partnership, limited liability company, or any other passthrough entity entitled to the credit under this section must be considered to be the taxpayer for purposes of this section, and the amount of the credit allowed must be determined at the passthrough entity level. The amount of the total credit determined at the entity level must be passed through to the partners, shareholders, or members in proportion to their respective interests in the passthrough entity.

SECTION 16. AMENDMENT. Section 57-38-01.24 of the North Dakota Century Code is amended and reenacted as follows:

57-38-01.24. Internship employment tax credit.

1. A taxpayer that is an employer within this state is entitled to a credit as determined under this section against state income tax liability under section 57-38-29, 57-38-30, or 57-38-30.3 for qualified compensation paid to an intern employed in this state by the taxpayer. To qualify for the credit under this section, the internship program must meet the following qualifications:
    a. The intern must be an enrolled student in an institution of higher education or vocational technical education program who is seeking a degree or a certification of completion in a major field of study closely related to the work experience performed for the taxpayer;
    b. The internship must be taken for academic credit or count toward the completion of a vocational technical education program;
    c. The intern must be supervised and evaluated by the taxpayer; and
    d. The internship position must be located in this state.
2. The amount of the credit to which a taxpayer is entitled is ten percent of the stipend or salary paid to a college intern employed by the taxpayer. A taxpayer may not receive more than three thousand dollars in total credits under this section for all taxable years combined.

a. The tax credit under this section applies to a stipend or salary for not more than five interns employed at the same time.

b. A partnership, subchapter S corporation, or limited liability company that for tax purposes is treated like a partnership that is entitled to the credit under this section must be considered to be the taxpayer for purposes of calculating the credit. The amount of the allowable credit must be determined at the passthrough entity level. The total credit determined at the entity level must be passed through to the partners, shareholders, or members in proportion to their respective interests in the passthrough entity.

SECTION 17. AMENDMENT. Section 57-38-01.25 of the North Dakota Century Code is amended and reenacted as follows:

57-38-01.25. Workforce recruitment credit for hard-to-fill employment positions. A taxpayer that is an employer in this state is entitled to a credit as determined under this section against state income tax liability under section 57-38-29, 57-38-30, or 57-38-30.3 for costs the taxpayer incurred during the tax year to recruit and hire employees for hard-to-fill employment positions within this state for which the annual salary for the position meets or exceeds the state average wage.

1. The amount of the credit to which a taxpayer is entitled is five percent of the salary paid for the first twelve consecutive months to the employee hired for the hard-to-fill employment position. To qualify for the credit under this section, the employee must be employed by the taxpayer in the hard-to-fill employment position for twelve consecutive months.

2. For purposes of this section:

   a. "Extraordinary recruitment methods" means using all of the following:

      (1) A person with the exclusive business purpose of recruiting employees and for which a fee is charged by that recruiter.

      (2) An advertisement in a professional trade journal, magazine, or other publication, the main emphasis of which is providing information to a particular trade or profession.

      (3) A web site, the sole purpose of which is to recruit employees and for which a fee is charged by the web site.

(4) Payment of a signing bonus, moving expenses, or nontypical fringe benefits.

b. "Hard-to-fill employment position" means a job that requires the employer to use extraordinary recruitment methods and for which the employer's recruitment efforts for the specific position have been unsuccessful for six consecutive calendar months.

c. "State average wage" means one hundred twenty-five percent of the state average wage published annually by job service North Dakota and which is in effect at the time the employee is hired.

3. The taxpayer may claim the credit in the first tax year beginning after the employee hired for the hard-to-fill position has completed the employee's first twelve consecutive months of employment in the hard-to-fill position with the taxpayer.

4. The credit under this section may not exceed a taxpayer's liability for the taxable year as determined under this chapter. Any amount of unused credit may be carried forward for up to four taxable years after the taxable year in which the credit could initially be claimed.

5. A partnership, subchapter S corporation, or limited liability company that for tax purposes is treated like a partnership that is entitled to the credit under this section must be considered to be the taxpayer for purposes of this section and the amount of the credit allowed must be determined at the passthrough entity level. The amount of the total credit determined at the passthrough entity level must be allowed to the members in proportion to their respective interests in the passthrough entity.

SECTION 18. AMENDMENT. Section 57-38-01.26 of the North Dakota Century Code is amended and reenacted as follows:

57-38-01.26. Angel fund investment tax credit. A taxpayer is entitled to a credit against state income tax liability under section 57-38-29, 57-38-30, or 57-38-30.3 for an investment made in an angel fund that is incorporated in this state. The angel fund must be in compliance with the securities laws of this state for the investment to qualify for the tax credit under this section. The amount of the credit to which a taxpayer is entitled is forty-five percent of the amount invested by the taxpayer in an angel fund during the taxable year. The aggregate annual credit for which a taxpayer may obtain a tax credit is not more than forty-five thousand dollars. To be eligible for the credit, the investment must be at risk in the angel fund for at least three years. Investments placed in escrow do not qualify for the credit. The credit must be claimed in the taxable year in which the investment in the angel fund was received by the angel fund. The credit allowed may not exceed the liability for tax under this chapter. If the amount of credit determined under this section exceeds the liability for tax under this chapter, the excess may be carried forward to each of the four succeeding taxable years. A taxpayer claiming a credit under this section may not claim any credit available to the taxpayer as a result of an investment made by the angel fund in a qualified business under chapter 57-38.5 or 57-38.6.

SECTION 19. AMENDMENT. Subsection 6 of section 57-38-01.27 of the North Dakota Century Code is amended and reenacted as follows:

6. "Foreign" when applied to a corporation means created or organized outside of North Dakota.

SECTION 20. AMENDMENT. Subsection 1 of section 57-38-01.29 of the North Dakota Century Code is amended and reenacted as follows:

1. In addition to any other credit or deduction allowed by law for a homeowner, an individual is entitled to a credit against the tax imposed under section 57-38-29 or 57-38-30.3 for taxable years 2007 and 2008 in the amount of ten percent of property taxes or mobile home taxes that became due during the income tax taxable year and are paid which were levied against the individual's homestead in this state. For purposes of this section, "property taxes" does not include any special assessments.

SECTION 21. AMENDMENT. Subsection 1 of section 57-38-01.30 of the North Dakota Century Code is amended and reenacted as follows:

1. In addition to any other credit or deduction allowed by law for a property owner, an individual or corporation is entitled to a credit against the tax imposed under section 57-38-29, 57-38-30, or 57-38-30.3 for taxable years 2007 and 2008 in the amount of ten percent of property taxes or mobile home taxes that became due during the income tax taxable year and are paid which were levied against

commercial property in this state. For purposes of this section, "property taxes" does not include any special assessments.

a. The amount of the credit under this section may not exceed one thousand dollars for any taxpayer.

b. The amount of the credit under this section may not exceed the taxpayer's tax liability under this chapter.

c. The amount of the credit under this section may not exceed one thousand dollars for married persons filing a joint return or five hundred dollars for a single individual or married individual filing separate returns.

SECTION 22. AMENDMENT. Section 57-38-30.3 of the North Dakota Century Code is amended and reenacted as follows:

57-38-30.3. Simplified method of computing tax.

1. A tax is hereby imposed for each taxable year upon income earned or received in that taxable year by every resident and nonresident individual, estate, and trust. A taxpayer computing the tax under this section is only eligible for those adjustments or credits that are specifically provided for in this section. Provided, that for purposes of this section, any person required to file a state income tax return under this chapter, but who has not computed a federal taxable income figure, shall compute a federal taxable income figure using a pro forma return in order to determine a federal taxable income figure to be used as a starting point in computing state income tax under this section. The tax for individuals is equal to North Dakota taxable income multiplied by the rates in the applicable rate schedule in subdivisions a through d corresponding to an individual's filing status used for federal income tax purposes. For an estate or trust, the schedule in subdivision e must be used for purposes of this subsection.

a. Single, other than head of household or surviving spouse.

If North Dakota taxable income is:	The tax is equal to:
Not over $27,050	2.10%
Over $27,050 but not over $65,550	$568.05 plus 3.92% of amount over $27,050
Over $65,550 but not over $136,750	$2,077.25 plus 4.34% of amount over $65,550

Over $136,750 but not over $297,350	$5,167.33 plus 5.04% of amount over $136,750
Over $297,350	$13,261.57 plus 5.54% of amount over $297,350

b. Married filing jointly and surviving spouse.

If North Dakota taxable income is:	The tax is equal to:
Not over $45,200	2.10%
Over $45,200 but not over $109,250	$949.20 plus 3.92% of amount over $45,200
Over $109,250 but not over $166,500	$3,459.96 plus 4.34% of amount over $109,250
Over $166,500 but not over $297,350	$5,944.61 plus 5.04% of amount over $166,500
Over $297,350	$12,539.45 plus 5.54% of amount over $297,350

c. Married filing separately.

If North Dakota taxable income is:	The tax is equal to:
Not over $22,600	2.10%
Over $22,600 but not over $54,625	$474.60 plus 3.92% of amount over $22,600
Over $54,625 but not over $83,250	$1,729.98 plus 4.34% of amount over $54,625
Over $83,250 but not over $148,675	$2,972.31 plus 5.04% of amount over $83,250
Over $148,675	$6,269.73 plus 5.54% of amount over $148,675

d. Head of household.

If North Dakota taxable income is:	The tax is equal to:
Not over $36,250	2.10%
Over $36,250 but not over $93,650	$761.25 plus 3.92% of amount over $36,250
Over $93,650 but not over $151,650	$3,011.33 plus 4.34% of amount over $93,650
Over $151,650 but not over $297,350	$5,528.53 plus 5.04% of amount over $151,650
Over $297,350	$12,871.81 plus 5.54% of amount over $297,350

e. Estates and trusts.

If North Dakota taxable income is:	The tax is equal to:
Not over $1,800	2.10%
Over $1,800 but not over $4,250	$37.80 plus 3.92% of amount over $1,800
Over $4,250 but not over $6,500	$133.84 plus 4.34% of amount over $4,250
Over $6,500 but not over $8,900	$231.49 plus 5.04% of amount over $6,500
Over $8,900	$352.45 plus 5.54% of amount over $8,900

f. For an individual who is not a resident of this state for the entire year, or for a nonresident estate or trust, the tax is equal to the tax otherwise computed under this subsection multiplied by a fraction in which:

(1) The numerator is the federal adjusted gross income allocable and apportionable to this state; and

(2) The denominator is the federal adjusted gross income from all sources reduced by the net income from the amounts specified in subdivisions a and b of subsection 2.

In the case of married individuals filing a joint return, if one spouse is a resident of this state for the entire year and the other spouse is a nonresident for part or all of the tax year, the tax on the joint return must be computed under this subdivision.

g. For taxable years beginning after December 31, 2001, the tax commissioner shall prescribe new rate schedules that apply in lieu of the schedules set forth in subdivisions a through e. The new schedules must be determined by increasing the minimum and maximum dollar amounts for each income bracket for which a tax is imposed by the cost-of-living adjustment for the taxable year as determined by the secretary of the United States treasury for purposes of section 1(f) of the United States Internal Revenue Code of 1954, as amended. For this purpose, the rate applicable to each income bracket may not be changed, and the manner of applying the cost-of-living adjustment must be the same as that used for adjusting the income brackets for federal income tax purposes.

2. For purposes of this section, "North Dakota taxable income" means the federal taxable income of an individual, estate, or trust as computed under the Internal Revenue Code of 1986, as amended, adjusted as follows:

a. Reduced by interest income from obligations of the United States and income exempt from state income tax under federal statute or United States or North Dakota constitutional provisions.

b. Reduced by the portion of a distribution from a qualified investment fund described in section 57-38-01 which is attributable to investments by the qualified investment fund in obligations of the United States, obligations of North Dakota or its political subdivisions, and any other obligation the interest from which is exempt from state income tax under federal statute or United States or North Dakota constitutional provisions.

c. Reduced by the amount equal to the earnings that are passed through to a taxpayer in connection with an allocation and apportionment to North Dakota under chapter 57-35.3.

d. Reduced by thirty percent of the excess of the taxpayer's net long-term capital gain for the taxable year over the net short-term capital loss for that year, as computed for purposes of the Internal Revenue Code of 1986, as amended. The adjustment provided by this subdivision is allowed only to the extent the net long-term capital gain is allocated to this state.

e. Increased by the amount of a lump sum distribution for which income averaging was elected under section 402 of the Internal Revenue Code of 1986 [26 U.S.C. 402], as amended. This adjustment does not apply if the taxpayer received the lump sum distribution while a nonresident of this state and the distribution is exempt from taxation by this state under federal law.

f. Increased by an amount equal to the losses that are passed through to a taxpayer in connection with an allocation and apportionment to North Dakota under chapter 57-35.3.

g. Reduced by the amount received by the taxpayer as payment for services performed when mobilized under title 10 United States Code federal service as a member of the national guard or reserve member of the armed forces of the United States. This subdivision does not apply to federal service while attending annual training, basic military training, or professional military education.

h. Reduced by income from a new and expanding business exempt from state income tax under section 40-57.1-04.

i. Reduced by interest and income from bonds issued under chapter 11-37.

j. Reduced by up to ten thousand dollars of qualified expenses that are related to a donation by a taxpayer or a taxpayer's dependent, while living, of one or more human organs to another human being for human organ transplantation. A taxpayer may claim the reduction in this subdivision only once for each instance of organ donation during the taxable year in which the human organ donation and the human organ transplantation occurs but if qualified expenses are incurred in more than one taxable year, the reduction for those expenses must be claimed in the year in which the expenses are incurred. For purposes of this subdivision:

(1) "Human organ transplantation" means the medical procedure by which transfer of a human organ is made from the body of one person to the body of another person.

(2) "Organ" means all or part of an individual's liver, pancreas, kidney, intestine, lung, or bone marrow.

(3) "Qualified expenses" means lost wages not compensated by sick pay and unreimbursed medical expenses as defined for federal income tax purposes, to the extent not deducted in computing federal taxable income, whether or not the taxpayer itemizes federal income tax deductions.

k. Increased by the amount of the contribution upon which the credit under section 57-38-01.21 is computed, but only to the extent that the contribution reduced federal taxable income.

l. Reduced by the amount of any payment received by a veteran or beneficiary of a veteran under section 37-28-03 or 37-28-04.

m. Reduced by the amount received by a taxpayer that was paid by an employer under paragraph 4 of subdivision a of subsection 2 of section 57-38-01.25 to hire the taxpayer for a hard-to-fill position under section 57-38-01.25, but only to the extent the amount received by the taxpayer is included in federal taxable income. The reduction applies only if the employer is entitled to the credit under section 57-38-01.25. The taxpayer must attach a statement from the employer in which the employer certifies that the employer is entitled to the credit under section 57-38-01.25 and which specifically identified the type of payment and the amount of the exemption under this section.

n. Reduced by the amount up to a maximum of five thousand dollars, or ten thousand dollars if a joint return is filed, for contributions made under a higher education savings plan administered by the Bank of North Dakota, pursuant to section 6-09-38.

o. Reduced by the amount of income of a taxpayer, who resides within the boundaries of any reservation in this state and who is an enrolled member of a federally recognized Indian tribe, from activities or sources within the boundaries of any reservation in this state.

3. Married individuals filing a joint federal income tax return shall file a joint state income tax return if the return is filed under this section. If separate federal income tax returns are filed, one spouse's state income tax return may be filed under this section and the other spouse's income tax return may be filed under the other provisions of this chapter.

4. a. A resident individual, estate, or trust is entitled to a credit against the tax imposed under this section for the amount of income tax paid by the taxpayer for the taxable year by another state or territory of the United States or the District of Columbia on income derived from sources in those jurisdictions that is also subject to tax under this section.

b. For an individual, estate, or trust that is a resident of this state for the entire taxable year, the credit allowed under this subsection may not exceed an amount equal to the tax imposed under this section multiplied by a ratio equal to federal adjusted gross income derived from sources in the other jurisdiction divided by federal adjusted gross income less the amounts under subdivisions a and b of subsection 2.

c. For an individual, estate, or trust that is a resident of this state for only part of the taxable year, the credit allowed under this subsection may not exceed the lesser of the following:

(1) The tax imposed under this chapter multiplied by a ratio equal to federal adjusted gross income derived from sources in the other jurisdiction received while a resident of this state divided by federal adjusted gross

income derived from North Dakota sources less the amounts under subdivisions a and b of subsection 2.

(2) The tax paid to the other jurisdiction multiplied by a ratio equal to federal adjusted gross income derived from sources in the other jurisdiction received while a resident of this state divided by federal adjusted gross income derived from sources in the other states.

d. The tax commissioner may require written proof of the tax paid to another state. The required proof must be provided in a form and manner as determined by the tax commissioner.

5. Individuals, estates, or trusts that file an amended federal income tax return changing their federal taxable income figure for a year for which an election to file state income tax returns has been made under this section shall file an amended state income tax return to reflect the changes on the federal income tax return.

6. The tax commissioner may prescribe procedures and guidelines to prevent requiring income that had been previously taxed under this chapter from becoming taxed again because of the provisions of this section and may prescribe procedures and guidelines to prevent any income from becoming exempt from taxation because of the provisions of this section if it would otherwise have been subject to taxation under the provisions of this chapter.

7. A taxpayer filing a return under this section is entitled to the following tax credits:

a. Family care tax credit under section 57-38-01.20.

b. Renaissance zone tax credits under sections 40-63-04, 40-63-06, and 40-63-07.

c. Agricultural business investment tax credit under section 57-38.6-03.

d. Seed capital investment tax credit under section 57-38.5-03.

e. Planned gift tax credit under section 57-38-01.21.

f. Biodiesel fuel tax credits under sections 57-38-01.22 and 57-38-01.23.

g. Internship employment tax credit under section 57-38-01.24.

h. Workforce recruitment credit under section 57-38-01.25.

i. Angel fund investment tax credit under section 57-38-01.26.

j. Microbusiness tax credit under section 57-38-01.27.

k. Marriage penalty credit under section 57-38-01.28.

l. Homestead income tax credit under section 57-38-01.29.

m. Commercial property income tax credit under section 57-38-01.30.

n. Research and experimental expenditures under section 57-38-30.5.

8. A taxpayer filing a return under this section is entitled to the exemption provided under section 40-63-04.

9. a. If an individual taxpayer engaged in a farming business elects to average farm income under section 1301 of the Internal Revenue Code [26 U.S.C. 1301], the taxpayer may elect to compute tax under this subsection. If an election to compute tax under this subsection is made, the tax imposed by subsection 1 for the taxable year must be equal to the sum of the following:

(1) The tax computed under subsection 1 on North Dakota taxable income reduced by elected farm income.

(2) The increase in tax imposed by subsection 1 which would result if North Dakota taxable income for each of the three prior taxable years were increased by an amount equal to one-third of the elected farm income. However, if other provisions of this chapter other than this section were used to compute the tax for any of the three prior years, the same provisions in effect for that prior tax year must be used to compute the increase in tax under this paragraph. For purposes of applying this paragraph to taxable years beginning before January 1, 2001, the increase in tax must be determined by recomputing the tax in the manner prescribed by the tax commissioner.

b. For purposes of this subsection, "elected farm income" means that portion of North Dakota taxable income for the taxable year which is elected farm income as defined in section 1301 of the Internal Revenue Code of 1986 [26 U.S.C. 1301], as amended, reduced by the portion of an exclusion claimed under subdivision d of subsection 2 that is attributable to a net long-term capital gain included in elected farm income.

c. The reduction in North Dakota taxable income under this subsection must be taken into account for purposes of making an election under this subsection for any subsequent taxable year.

d. The tax commissioner may prescribe rules, procedures, or guidelines necessary to administer this subsection.

10. The tax commissioner may prescribe tax tables, to be used in computing the tax according to subsection 1, if the amounts of the tax tables are based on the tax rates set forth in subsection 1. If prescribed by the tax commissioner, the tables must be followed by every individual, estate, or trust determining a tax under this section.

SECTION 23. AMENDMENT. Section 57-38-30.5 of the North Dakota Century Code is amended and reenacted as follows:

57-38-30.5. Income tax credit for research and experimental expenditures. A taxpayer is allowed a credit against the tax imposed under section 57-38-29, 57-38-30, or 57-38-30.3 for conducting qualified research in this state.

1. The amount of the credit for taxpayers that earned or claimed a credit under this section in taxable years beginning before January 1, 2007, is calculated as follows:

a. For the first taxable year beginning after December 31, 2006, the credit is equal to twenty-five percent of the first one hundred thousand dollars of the qualified research expenses for the taxable year in excess of the base period research expenses and equal to seven and one-half percent of all qualified research expenses for the taxable year more than one hundred thousand dollars in excess of the base period research expenses.

b. For the second taxable year beginning after December 31, 2006, the credit is equal to twenty-five percent of the first one hundred thousand dollars of the qualified research expenses for the taxable year in excess of the base period research expenses and equal to eleven percent of all qualified research expenses for the taxable year more than one hundred thousand dollars in excess of the base period research expenses.

c. For the third taxable year beginning after December 31, 2006, the credit is equal to twenty-five percent of the first one hundred thousand dollars of the qualified research expenses for the taxable year in excess of the base period research expenses and equal to fourteen and one-half percent of all qualified research expenses for the taxable year more than one hundred thousand dollars in excess of the base period research expenses.

d. For the fourth through the tenth taxable years beginning after December 31, 2006, the credit is equal to twenty-five percent of the first one hundred thousand dollars of the qualified research expenses for the taxable year in excess of the base period research expenses and equal to eighteen percent of all qualified research expenses for the taxable year more than one hundred thousand dollars in excess of the base period research expenses.

e. For the eleventh taxable year beginning after December 31, 2006, and for each subsequent taxable year in which the taxpayer conducts qualified research in this state, the credit is equal to twenty-five percent of the first one hundred thousand dollars of the qualified research expenses for the taxable year in excess of the base period research expenses and equal to eight percent of all qualified research expenses for the taxable year more than one hundred thousand dollars in excess of the base period research expenses.

f. The maximum annual credit a taxpayer may obtain under this section is two million dollars. Any credit amount earned in the taxable year in excess of two million dollars may not be carried back or forward as provided in subsection 7.

2. For taxpayers that have not earned or claimed a credit under this section in taxable years beginning before January 1, 2007, and which begin conducting qualified research in North Dakota in any of the first four taxable years beginning after December 31, 2006, the amount of the credit is equal to twenty-five percent of the first one hundred thousand dollars of the qualified research expenses for the taxable year in excess of the base period research expenses and equal to twenty percent of all qualified research expenses for the taxable year more than one hundred thousand dollars in excess of the base period research expenses.

a. This rate applies through the tenth taxable year beginning after December 31, 2006.

b. For the eleventh taxable year beginning after December 31, 2006, and for each subsequent taxable year in which the taxpayer conducts qualified research in this state, the credit is equal to twenty-five percent of the first one hundred thousand dollars of the qualified research expenses for the taxable year in excess of the base period research expenses and equal to eight percent of all qualified research expenses for the taxable year more than one hundred thousand dollars in excess of the base period research expenses.

3. For taxpayers that have not earned or claimed a credit under this section in taxable years beginning before January 1, 2007, and which begin conducting qualified research in North Dakota in any taxable year following the fourth taxable year beginning after December 31, 2006, the amount of the credit is equal to twenty-five percent of the first one hundred thousand dollars of the qualified research expenses for the taxable year in excess of the base period research expenses and equal to eight percent of all qualified research expenses for the taxable year more than one hundred thousand dollars in excess of the base period research expenses.

4. For purposes of this section:

a. "Base period research expenses" means base period research expenses as defined in section 41(c) of the Internal Revenue Code [26 U.S.C. 41(c)], except it does not include research conducted outside the state of North Dakota.

b. "Director" means the director of the department of commerce division of economic development and finance.

c. "Primary sector business" means a qualified business that through the employment of knowledge or labor adds value to a product, process, or service.

d. "Qualified research" means qualified research as defined in section 41(d) of the Internal Revenue Code [26 U.S.C. 41(d)], except it does not include research conducted outside the state of North Dakota.

e. "Qualified research and development company" means a taxpayer that is a primary sector business with annual gross revenues of less than seven hundred fifty thousand dollars and which has not conducted new research and development in North Dakota.

f. "Qualified research expenses" means qualified research expenses as defined in section 41(b) of the Internal Revenue Code [26 U.S.C. 41(b)], except it does not include expenses incurred for basic research conducted outside the state of North Dakota.

5. The credit allowed under this section for the taxable year may not exceed the liability for tax under this chapter.

6. In the case of a taxpayer that is a partner in a partnership or a member in a limited liability company, the credit allowed for the taxable year may not exceed an amount separately computed with respect to the taxpayer's interest in the trade, business, or entity equal to the amount of tax attributable to that portion of the taxpayer's taxable income which is allocable or apportionable to the taxpayer's interest in the trade, business, or entity.

7. Except as provided in subsection 1, if the amount of the credit determined under this section for any taxable year exceeds the limitation under subsection 5, the excess may be used as a research credit carryback to each of the three preceding taxable years and a research credit carryover to each of the fifteen succeeding taxable years. The entire amount of the excess unused credit for the taxable year must be carried first to the earliest of the taxable years to which the credit may be carried and then to each successive year to which the credit may be carried and the amount of the unused credit which may be added under this subsection may not exceed the taxpayer's liability for tax less the research credit for the taxable year.

8. A taxpayer that is certified as a qualified research and development company by the director may elect to sell, transfer, or assign all or part of the unused tax credit earned under this section. The director shall certify whether a taxpayer that has requested to become a qualified research and development company meets the requirements of subsection 4. The director shall establish the necessary forms and procedures for certifying qualifying research and development companies. The

director shall issue a certification letter to the taxpayer and the tax commissioner. A tax credit can be sold, transferred, or assigned subject to the following:

a. A taxpayer's total credit assignment under this section may not exceed one hundred thousand dollars over any combination of taxable years.

b. If the taxpayer elects to assign or transfer an excess credit under this subsection, the tax credit transferor and the tax credit purchaser jointly shall file with the tax commissioner a copy of the purchase agreement and a statement containing the names, addresses, and taxpayer identification numbers of the parties to the transfer, the amount of the credit being transferred, the gross proceeds received by the transferor, and the taxable year or years for which the credit may be claimed. The taxpayer and the purchaser also shall file a document allowing the tax commissioner to disclose tax information to either party for the purpose of verifying the correctness of the transferred tax credit. The purchase agreement, supporting statement, and waiver must be filed within thirty days after the date the purchase agreement is fully executed.

c. The purchaser of the tax credit shall claim the credit beginning with the taxable year in which the credit purchase agreement was fully executed by the parties. A purchaser of a tax credit under this section has only such rights to claim and use the credit under the terms that would have applied to the tax credit transferor, except the credit purchaser may not carry back the credit as otherwise provided in this section. This subsection does not limit the ability of the tax credit purchaser to reduce the tax liability of the purchaser, regardless of the actual tax liability of the tax credit transferor.

d. The original purchaser of the tax credit may not sell, assign, or otherwise transfer the credit purchased under this section.

e. If the amount of the credit available under this section is changed as a result of an amended return filed by the transferor, or as the result of an audit conducted by the internal revenue service or the tax commissioner, the transferor shall report to the purchaser the adjusted credit amount within thirty days of the amended return or within thirty days of the final determination made by the internal revenue service or the tax commissioner. The tax credit purchaser shall file amended returns reporting the additional tax due or claiming a refund as provided in section 57-38-38 or 57-38-40, and the tax commissioner may audit these returns and assess or issue refunds, even though other time periods prescribed in these sections may have expired for the purchaser.

f. Gross proceeds received by the tax credit transferor must be assigned to North Dakota. The amount assigned under this subsection cannot be reduced by the taxpayer's income apportioned to North Dakota or any North Dakota net operating loss of the taxpayer.

g. The tax commissioner has four years after the date of the credit assignment to audit the returns of the credit transferor and the purchaser to verify the correctness of the amount of the transferred credit and if necessary assess the credit purchaser if additional tax is found due. This subdivision does not limit or restrict any other time period prescribed in this chapter for the assessment of tax.

h. The tax commissioner may adopt rules to permit verification of the validity and timeliness of the transferred tax credit.

9. If a taxpayer acquires or disposes of the major portion of a trade or business or the major portion of a separate unit of a trade or business in a transaction with another taxpayer, the taxpayer's qualified research expenses and base period must be adjusted in the manner provided by section 41(f)(3) of the Internal Revenue Code [26 U.S.C. 41(f)(3)].

10. If a taxpayer entitled to the credit provided by this section is a member of a group of corporations filing a North Dakota consolidated tax return using the combined reporting method, the credit may be claimed against the aggregate North Dakota tax liability of all the corporations included in the North Dakota consolidated return. This section does not apply to tax credits received or purchased under subsection 8.

11. An individual, estate, or trust that purchases a credit under this section is entitled to claim the credit against state income tax liability under section 57-38-29 or 57-38-30.3.

12. A partnership, subchapter S corporation, limited partnership, limited liability company, or any other passthrough entity entitled to the credit under this section must be considered to be the taxpayer for purposes of calculating the credit. The amount of the allowable credit must be determined at the passthrough entity level. The total credit determined at the entity level must be passed through to the partners, shareholders, or members in proportion to their respective interests in the passthrough entity. An individual taxpayer may take the credit passed through under this subsection against the individual's state income tax liability under sections 57-38-29 and 57-38-30.

SECTION 24. AMENDMENT. Section 57-38.5-03 of the North Dakota Century Code is amended and reenacted as follows:

57-38.5-03. Seed capital investment tax credit. If a taxpayer makes a qualified investment in a qualified business, the taxpayer is entitled to a credit against state income tax liability under section ~~57-38-29 or~~ 57-38-30.3. The amount of the credit to which a taxpayer is entitled is forty-five percent of the amount invested by the taxpayer in qualified businesses during the taxable year, subject to the following:

1. The aggregate annual investment for which a taxpayer may obtain a tax credit under this section is not less than five thousand dollars and not more than two hundred fifty thousand dollars. This subsection may not be interpreted to limit additional investment by a taxpayer for which that taxpayer is not applying for a credit.

2. In any taxable year, a taxpayer may claim no more than one-third of the credit under this section which is attributable to investments in a single taxable year.

3. Any amount of credit under this section not allowed because of the limitations in this section may be carried forward for up to four taxable years after the taxable year in which the investment was made.

4. A partnership that invests in a qualified business must be considered to be the taxpayer for purposes of the investment limitations in this section and the amount

of the credit allowed with respect to a partnership's investment in a qualified business must be determined at the partnership level. The amount of the total credit determined at the partnership level must be allowed to the partners, limited to individuals, estates, and trusts, in proportion to their respective interests in the partnership.

5. The investment must be at risk in the business. An investment for which a credit is received under this section must remain in the business for at least three years.

6. The entire amount of an investment for which a credit is claimed under this section must be expended by the qualified business for plant, equipment, research and development, marketing and sales activity, or working capital for the qualified business.

7. A taxpayer who owns a controlling interest in the qualified business or whose full-time professional activity is the operation of the business is not entitled to a credit under this section. A member of the immediate family of a taxpayer disqualified by this subsection is not entitled to the credit under this section. For purposes of this subsection, "immediate family" means the taxpayer's spouse, parent, sibling, or child or the spouse of any such person.

8. The tax commissioner may disallow any credit otherwise allowed under this section if any representation by a business in the application for certification as a qualified business proves to be false or if the taxpayer or qualified business fails to satisfy any conditions under this section or any conditions consistent with this section otherwise determined by the tax commissioner. The amount of any credit disallowed by the tax commissioner that reduced the taxpayer's income tax liability for any or all applicable tax years, plus penalty and interest as provided under section 57-38-45, must be paid by the taxpayer.

SECTION 25. AMENDMENT. Section 57-38.6-03 of the North Dakota Century Code is amended and reenacted as follows:

57-38.6-03. Agricultural business investment tax credit. If a taxpayer makes a qualified investment in a qualified business, the taxpayer is entitled to a credit against state income tax liability as determined under section ~~57-38-29 or~~ 57-38-30.3. The amount of the credit to which a taxpayer is entitled is thirty percent of the amount invested by the taxpayer in qualified businesses during the taxable year, subject to the following:

1. The aggregate annual investment for which a taxpayer may obtain a tax credit under this section is not more than twenty thousand dollars. This subsection may not be interpreted to limit additional investment by a taxpayer for which that taxpayer is not applying for a credit.
2. In any taxable year, a taxpayer may claim no more than fifty percent of the credit under this section which is attributable to qualified investments in a single taxable year. The amount of the credit allowed under this section for any taxable year may not exceed fifty percent of the taxpayer's tax liability as otherwise determined under chapter 57-38.
3. Any amount of credit under this section not allowed because of the limitations in this section may be carried forward for up to fifteen taxable years after the taxable year in which the investment was made.
4. A partnership that invests in a qualified business must be considered to be the taxpayer for purposes of the investment limitations in this section and the amount of the credit allowed with respect to a partnership's investment in a qualified business must be determined at the partnership level. The amount of the total credit determined at the partnership level must be allowed to the partners, limited to individuals, estates, and trusts, in proportion to their respective interests in the partnership.
5. The investment must be at risk in the business. A qualified investment must be in the form of a purchase of ownership interests or the right to receive payment of dividends from the business. An investment for which a credit is received under this section must remain in the business for at least three years.
6. The entire amount of an investment for which a credit is claimed under this section must be expended by the qualified business for plant, equipment, research and development, marketing and sales activity, or working capital for the qualified business.
7. The tax commissioner may disallow any credit otherwise allowed under this section if any representation by a business in the application for certification as a qualified

business proves to be false or if the taxpayer or qualified business fails to satisfy any conditions under this section or any conditions consistent with this section otherwise determined by the tax commissioner. The amount of any credit disallowed by the tax commissioner that reduced the taxpayer's income tax liability for any or all applicable tax years, plus penalty and interest provided under section 57-38-45, must be paid by the taxpayer.

SECTION 26. REPEAL. Sections 57-38-01.2, 57-38-01.18, 57-38-02, 57-38-03, 57-38-06.1, 57-38-29, 57-38-29.2, and 57-38-30.4, 57-38-67, 57-38-68, 57-38-69, 57-38-70, 57-38-71, 57-38-72, 57-38-73, and 57-38-74 of the North Dakota Century Code are repealed.

SECTION 27. EFFECTIVE DATE. This Act is effective for taxable years beginning after December 31, 2008.