GENERAL ASSEMBLY OF NORTH CAROLINA
1989 SESSION

CHAPTER 984
HOUSE BILL 2138

AN ACT TO PROVIDE TRANSITIONAL ADJUSTMENTS RELATING TO SUBCHAPTER S CORPORATIONS, TO CORRECT AN ERROR THAT INADVERTENTLY DISALLOWED DEDUCTIONS FOR SOME MORTGAGE INTEREST PAYMENTS, TO PROVIDE ADDITIONAL TAX RELIEF FOR TAXPAYERS WITH DEPENDENTS WHO ARE PERMANENTLY AND TOTALLY DISABLED, TO ALLOW A TAX CREDIT FOR STATE INCOME TAXES PAID ON GOVERNMENT RETIREMENT BENEFITS RECEIVED IN 1988, TO PROVIDE THAT AN EXTENSION OF TIME FOR FILING AN INCOME OR FRANCHISE TAX RETURN IS NOT AN EXTENSION OF TIME FOR PAYING THE TAX, AND TO REDUCE THE THRESHOLD FOR PAYMENTS OF ESTIMATED CORPORATE INCOME TAX.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-131.4 reads as rewritten:

"**§ 105-131.4. Carryforwards; carrybacks; loss limitation.**

(a) Carryforwards and carrybacks to and from an S Corporation shall be restricted in the manner provided in section 1371(b) of the Code.

(b) The aggregate amount of losses or deductions of an S Corporation taken into account by a shareholder pursuant to G.S. 105-131.1(b) may not exceed the combined adjusted bases, determined in accordance with G.S. 105-131.3, of the shareholder in the stock and indebtedness of the S Corporation.

(c) Any loss or deduction that is disallowed for a taxable period pursuant to subsection (b) of this section shall be treated as incurred by the corporation in the succeeding taxable period with respect to that shareholder.

(d) (1) Any loss or deduction that is disallowed pursuant to subsection (b) of this section for the corporation's last taxable period as an S Corporation shall be treated as incurred by the shareholder on the last day of any post-termination transition period.

(2) The aggregate amount of losses and deductions taken into account by a shareholder pursuant to subdivision (1) of this subsection may not exceed the adjusted basis of the shareholder in the stock of the corporation (determined in accordance with G.S. 105-131.3 at the close of the last day of any post-termination transition period and without regard to this subsection).

(e) Each shareholder's pro rata share of the reduction of an S Corporation's income because of the allowance of a carryforward loss to the S Corporation under this

subsection shall be taken into account by the shareholder as a transitional adjustment under G.S. 105-134.7. Notwithstanding the provisions of subsection (a) of this section, an S Corporation that sustained a net economic loss in a taxable year beginning before January 1, 1989, may carry the loss forward to a taxable year beginning on or after January 1, 1989, and before July 1, 1991, and may deduct the loss in that year to one-half of the extent it could have carried forward and deducted the loss pursuant to G.S. 105-130.5(b)(4) and G.S. 105-130.8 if the S Corporation Income Tax Act had not become effective until taxable years beginning on or after July 1, 1991. Any loss carryforward allowed as a deduction by this subsection may not exceed one-half of the S Corporation's net income, as defined in the Code subject to the adjustments provided in G.S. 105-130.5 other than the adjustment provided in G.S. 105-130.5(b)(4), and is subject to the limitations provided in G.S. 105-131.4(b) and (d). Notwithstanding the provisions of G.S. 105-131.3, the basis of a shareholder in the stock of an S Corporation shall be adjusted for the shareholder's pro rata share of the carryforward loss allowed as a deduction to the S Corporation under this subsection. Notwithstanding the provisions of G.S. 105-131.6(c)(2), the accumulated adjustments account maintained for each resident shareholder shall be adjusted for the shareholder's pro rata share of the carryforward loss allowed as a deduction to the S Corporation under this subsection."

Sec. 2. G.S. 105-151.19 reads as rewritten:

"**§ 105-151.19. Credit for North Carolina dividends.**

There is allowed as a credit against the tax imposed by this Division an amount equal to six percent (6%) of the amount of dividends received by the taxpayer during the taxable year from stock issued by a qualified corporation, up to a maximum credit of three hundred dollars ($300.00) per taxpayer for the taxable year. A corporation is a qualified corporation if fifty percent (50%) or more of the dividends from stock issued by the corporation would be deductible by a corporate shareholder for the taxable year under the provisions of G.S. 105-130.7(1), (2), (3), (3a), or (5) except that no credit shall be allowed for dividends ~~issued with respect to~~ deemed distributable from earnings for a taxable period during which the corporation is an S Corporation subject to the provisions of Division I-S of this Article.

This credit applies only with respect to dividends received while the taxpayer was a resident of this State. In the case of a married couple filing a joint return where both spouses received dividends during the taxable year, the three hundred dollar ($300.00) maximum applies separately to each spouse's dividends for a potential total credit of six hundred dollars ($600.00) for the couple. This credit may not exceed the amount of tax imposed by this Division for the taxable year reduced by the sum of all credits allowed under this Division, except payments of tax made by or on behalf of the taxpayer."

Sec. 3. Notwithstanding any other provision of law, with respect to dividends received by a taxpayer from an S Corporation and included in the taxpayer's North Carolina taxable income under Division II of Article 4 of Chapter 105 of the General Statutes for the taxpayer's 1989 taxable year, if (i) the dividends were distributed during the corporation's 1988 taxable year which began on or after January 2, 1988, and ended on or after January 1, 1989, or (ii) the dividends were distributed before October 1, 1989, then the three hundred dollar ($300.00) limitation in G.S. 105-151.19 shall not

apply and any credit otherwise allowable with respect to these dividends shall be allowed without regard to the three hundred dollar ($300.00) limitation. No additional credit is allowed under G.S. 105-151.19 for dividends distributed on or after October 1, 1989, from an S Corporation during its 1989 taxable year, to the extent the taxpayer's total credit under G.S. 105-151.19 for the taxable year exceeds three hundred dollars ($300.00).

Sec. 4. G.S. 105-134.6(b) reads as rewritten:

"(b) Deductions. The following deductions from taxable income shall be made in calculating North Carolina taxable income, to the extent each item is included in gross income:

(1) Interest upon the obligations of (i) the United States or its possessions, (ii) this State or a political subdivision of this State, or (iii) a nonprofit educational institution organized or chartered under the laws of this State.

(2) Interest upon obligations and gain from the disposition of obligations to the extent the interest or gain is exempt from tax under the laws of this State.

(3) Benefits received under Title II of the Social Security Act and amounts received from retirement annuities or pensions paid under the provisions of the Railroad Retirement Act of 1937.

(4) Any amount not to exceed one thousand five hundred dollars ($1,500) received by the taxpayer during the taxable year as compensation for the performance of duties as a member of the North Carolina organized militia, the national guard as defined in G.S. 127A-3.

(5) Refunds of State, local, and foreign income taxes included in the taxpayer's gross income.

(6) a. An amount, not to exceed four thousand dollars ($4,000), equal to the sum of the amount calculated in subparagraph b. plus the amount calculated in subparagraph c.

b. The amount calculated in this subparagraph is the amount received during the taxable year from one or more state, local, or federal government retirement plans.

c. The amount calculated in this subparagraph is the amount received during the taxable year from one or more retirement plans other than state, local, or federal government retirement plans, not to exceed a total of two thousand dollars ($2,000) in any taxable year.

d. In the case of a married couple filing a joint return where both spouses received retirement benefits during the taxable year, the maximum dollar amounts provided in this subdivision for various types of retirement benefits apply separately to each spouse's benefits.

(7) The amount of inheritance tax attributable to an item of income in respect of a decedent required to be included in gross income under the

Code, adjusted as provided in G.S. 105-134.5, 105-134.6, and 105-134.7. The amount of inheritance tax attributable to an item of income in respect of a decedent is (i) the amount by which the inheritance tax paid under Article 1 of this Chapter on property transferred to a beneficiary by a decedent exceeds the amount of inheritance tax that would have been payable by the beneficiary if the item of income in respect of a decedent had not been included in the property transferred to the beneficiary by the decedent, (ii) multiplied by a fraction, the numerator of which is the amount required to be included in gross income for the taxable year under the Code, adjusted as provided in G.S. 105-134.5, 105-134.6, and 105-134.7, and the denominator of which is the total amount of income in respect of a decedent transferred to the beneficiary by the decedent. For an estate or trust, the deduction allowed by this subdivision shall be computed by excluding from the gross income of the estate or trust the portion, if any, of the items of income in respect of a decedent that are properly paid, credited, or to be distributed to the beneficiaries during the taxable year.

(8) The amount by which the taxpayer's mortgage interest deduction under the Code was reduced pursuant to section 163(g) of the Code."

Sec. 5. G.S. 105-151.18 reads as rewritten:

"**§ 105-151.18. Credit for the disabled.**

(a) Disabled Taxpayer. A ~~person~~ taxpayer who (i) is retired on disability, (ii) at the time of retirement, was permanently and totally disabled, ~~disabled as defined in section 22 of the Code,~~ and (iii) claims a federal income tax credit under section 22 of the Code for the taxable year, is allowed as a credit against the tax imposed by this Division an amount equal to one-third of the amount of the federal income tax credit for which ~~he~~ the taxpayer is eligible under section 22 of the Code.

(b) Disabled Dependent. If a dependent or spouse for whom a taxpayer is allowed an exemption under the Code is permanently and totally disabled, the taxpayer is allowed a credit against the tax imposed by this Division. In order to claim the credit allowed by this subsection, the taxpayer must attach to the tax return on which the credit is claimed a statement from a physician or local health department certifying that the dependent or spouse for whom the credit is claimed is permanently and totally disabled, as defined in this section. The amount of the credit allowed shall be determined as follows: For a taxpayer whose North Carolina adjusted gross income does not exceed the appropriate income amount provided in the table below, based on the taxpayer's filing status, the credit allowed is the appropriate initial credit provided in the table below. For a taxpayer whose North Carolina adjusted gross income does exceed the appropriate income amount, the credit allowed is the appropriate initial credit reduced by four dollars ($4.00) for every one thousand dollars ($1,000) by which the taxpayer's North Carolina adjusted gross income exceeds the appropriate income amount.

Filing Status	**Initial Credit**	**Income Amount**

Head of Household	$64.00	$16,000
Surviving Spouse or Joint Return	$80.00	$20,000
Single	$48.00	$12,000
Married Filing Separately	$40.00	$10,000

(c) Definitions. The following definitions apply in this section:

(1) North Carolina Adjusted Gross Income. Adjusted gross income, as determined under the Code, adjusted as provided in G.S. 105-134.6 and G.S. 105-134.7.

(2) Permanently and Totally Disabled. Unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment that can be expected to result in death or that has lasted or can be expected to last for a continuous period of not less than 12 months. For the purpose of this section, a minor is permanently and totally disabled if the impact of the impairment on the minor's ability to function is equivalent in severity to that which would make an adult unable to engage in any substantial gainful activity.

(d) Limitations. A nonresident or part-year resident who claims the credit allowed by this section shall reduce the amount of the credit by multiplying it by the fraction calculated under G.S. 105-134.5(b) or (c), as appropriate. The credit allowed under this section may not exceed the amount of tax imposed by this Division for the taxable year reduced by the sum of all credits allowed under this Division, except payments of tax made by or on behalf of the taxpayer."

Sec. 6. Division II of Article 4 of Chapter 105 of the General Statutes is amended by adding after G.S. 105-151.19 a new section to read:

"**§ 105-151.20. Credit for tax paid on certain government retirement benefits.**

A taxpayer who received government retirement benefits during the 1988 tax year may claim a credit against the tax imposed by this Division equal to the amount by which the tax under this Division paid by the taxpayer for the 1988 tax year would have been reduced if none of the taxpayer's government retirement benefits had been included in the taxpayer's taxable income. If a taxpayer received a refund of any tax paid under this Division on government retirement benefits for the 1988 tax year, the amount of the refund reduces the amount of the credit allowed under this section.

As used in this section, the term 'government retirement benefits' means retirement benefits received from one or more state, local, or federal government retirement plans. As used in this section, the term '1988 tax year' means the taxpayer's taxable year beginning on a day in 1988.

The credit allowed under this section shall shall be taken in equal installments over the taxpayer's first three taxable years beginning on or after January 1, 1990. The credit allowed under this section may not exceed the amount of tax imposed by this Division reduced by the sum of all credits allowed against the tax, except payments of tax made by or on behalf of the taxpayer."

Sec. 7. G.S. 105-129 reads as rewritten:

"**§ 105-129. Extension of time for filing returns.**

~~(a)~~ The return required by this Article ~~or schedule~~ shall be due on or before the dates specified unless ~~written application for extension of time in which to file, containing reasons therefor, is made to~~ the Secretary of Revenue grants an extension on or before the due date of ~~such~~ the return. The Secretary of Revenue for good cause may extend the time for filing any return under this ~~Article or schedule, provided interest at the rate established pursuant to G.S. 105-241.1(i) is paid upon the total amount of tax due.~~ Article. A taxpayer requesting an extension of time for filing shall, on or before the date the return is due, submit an application for an extension of time for filing on a form prescribed by the Secretary and pay the full amount of the tax anticipated to be due."

Sec. 8. G.S. 105-130.17(d) reads as rewritten:

"(d) In case of sickness, absence, or other disability or whenever in his judgment good cause exists, the Secretary may allow further time for filing returns. A taxpayer requesting an extension of time for filing shall, on or before the date the return is due, submit an application for an extension of time for filing on a form prescribed by the Secretary and pay the full amount of the tax anticipated to be due."

Sec. 9. G.S. 105-130.19(a) reads as rewritten:

"(a) Except as provided in Article 4C of this Chapter, the full amount of the tax payable as shown on the face of the return shall be paid to the Secretary of Revenue at the office where the return is filed and within the time fixed by law for filing the return. An extension of time granted for filing the return under G.S. 105-130.17(d) is not an extension of time for payment of the full amount of the tax payable."

Sec. 10. G.S. 105-155 reads as rewritten:

"**§ 105-155. Time and place of filing returns.**

(a) Returns shall be in ~~such forms as the Secretary may from time to time prescribe,~~ the forms prescribed by the Secretary and shall be filed with the Secretary at ~~his~~ the Secretary's main office or at any branch office. The return of every taxpayer reporting on a calendar year basis shall be filed on or before the fifteenth day of April in each year, and the return of every taxpayer reporting on a fiscal year basis shall be filed on or before the fifteenth day of the fourth month following the close of the fiscal year. ~~In case of sickness, absence, or other disability or whenever in his judgment good cause exists, the~~

(b) The Secretary ~~may~~ may, for good cause, allow further time for filing returns. A taxpayer requesting an extension of time for filing shall, on or before the date the return is due, submit an application for an extension of time for filing on a form prescribed by the Secretary and pay the full amount of the tax anticipated to be due.

(c) There shall be annexed to the return the affirmation of the taxpayer making the return in the following form: 'Under penalties prescribed by law, I hereby affirm that to the best of my knowledge and belief this return, including any accompanying schedules and statements, is true and complete. (If prepared by a person other than the taxpayer, that the preparer's affirmation is based on all information of which the preparer has any knowledge.)' The Secretary shall prepare blank forms for the returns, distribute them throughout the State, and furnish them upon application; but failure to

receive or secure the form shall not relieve any taxpayer from the obligation of filing a return required by this Division."

Sec. 11. G.S. 105-157 reads as rewritten:

"**§ 105-157. Time and place of payment of tax.**

(a) Except as otherwise provided in this section and in Article 4A of this Chapter, the full amount of the tax payable as shown on the face of the return shall be paid to the Secretary at the office where the return is filed at the time fixed by law for filing the return. An extension of time granted for filing the return under G.S. 105-155 is not an extension of time for payment of the full amount of the tax payable. If the amount shown to be due is less than one dollar ($1.00), no payment need be made.

(b) The tax may be paid with uncertified check during such time and under such regulations as the Secretary may prescribe; but if a check so received is not paid by the bank on which it is drawn, the taxpayer by whom the check was tendered shall remain liable for the payment of the tax and for all legal penalties the same as if the check had not been tendered."

Sec. 12. G.S. 105-160.6 reads as rewritten:

"**§ 105-160.6. Time and place of filing returns.**

Returns required under the provisions of G.S. 105-160.5 shall be in such form as the Secretary may prescribe, and shall be filed with the Secretary at the Secretary's main office or at any branch office which the Secretary may establish. The return of every fiduciary reporting on a calendar-year basis shall be filed on or before the 15th day of April in each year, and the return of every fiduciary reporting on a fiscal year basis shall be filed on or before the 15th day of the fourth month following the close of the fiscal year. ~~In the case of sickness, absence, or other disability or whenever in his judgment good cause exists, the~~ The Secretary may for good cause allow further time for filing a return. A person requesting an extension of time for filing shall, on or before the date the return is due, submit an application for an extension of time for filing on a form prescribed by the Secretary and pay the full amount of the tax anticipated to be due."

Sec. 13. G.S. 105-160.7(a) reads as rewritten:

"(a) The full amount of the tax payable as shown on the face of the return shall be paid to the Secretary at the office where the return is filed at the time fixed by law for filing the return. However, if the amount shown to be due after all credits is less than one dollar ($1.00), no payment need be made. An extension of time granted for filing the return under G.S. 105-160.6 is not an extension of time for payment of the full amount of the tax payable."

Sec. 14. G.S. 105-263 reads as rewritten:

"**§ 105-263. Time for filing reports extended.**

The Secretary of ~~Revenue, when he deems the same necessary or advisable, may~~ Revenue may, in his discretion, extend to any person, firm, ~~or corporation or public utility~~ corporation, or public utility a further specified time within which to file any report required by law to be filed with the Secretary of ~~Revenue,~~ Revenue. ~~in which event the attaching or taking effect of any penalty for failure to file such report or to pay any tax or fee shall be extended or postponed accordingly.~~ An extension of time for filing a report granted under G.S. 105-129, 105-130.17, 105-155, or 105-160.6 is not an

extension of time for payment of the full amount of the tax payable or for the attachment of any penalty for failure to pay the tax. Any other extension of time for filing a report is also an extension of time for attachment of any penalty for failure to file a report or to pay any tax or fee. Interest, at the rate established pursuant to G.S. 105-241.1(i), from the time the report or return was originally required to be filed to the time of payment shall be added to and paid with any tax that might be due on returns so extended."

Sec. 15. G.S. 105-163.38 reads as rewritten:

"**§ 105-163.38. Definitions.**

~~As used in this Article,~~ The following definitions apply in this Article, unless the context requires otherwise:

(1) "Corporation" means a corporation that has a reasonably estimated tax liability of at least five thousand dollars ($5,000). The term "corporation" includes joint-stock companies or associations that meet these requirements. Code. The Internal Revenue Code as enacted as of January 1, 1990, including any provisions enacted as of that date which become effective either before or after that date.

(1a) Corporation. Defined in section 7701 of the Code.

(2) ~~"Estimated tax" means the~~ Estimated tax. The amount of income tax the corporation estimates as the amount imposed by Article 4 for the taxable year. ~~The appropriate percentage of estimated tax payable during the taxable year shall be determined by the following table:~~

~~For Taxable Years Beginning On and After:~~	~~Percentages~~
~~June 25, 1983, and before June 25, 1984~~	~~25%~~
~~June 25, 1984, and before June 25, 1985~~	~~50%~~
~~June 25, 1985, and before June 25, 1986~~	~~75%~~
~~June 25, 1986~~	~~100%~~

(3) ~~"Fiscal year" means an~~ Fiscal year. An accounting period of 12 months ending on the last day of any month other than December.

(4) ~~"Secretary" means the~~ Secretary. The Secretary of Revenue.

(5) ~~"Taxable year" means the~~ Taxable year. The calendar year or fiscal year used as a basis to determine net income under Article 4. If no fiscal year has been established, 'fiscal year' means the calendar year. In the case of a return made for a fractional part of the year under Article 4, or under rules prescribed by the Secretary, 'taxable year' means the period for which the return is made."

Sec. 16. G.S. 105-163.40 reads as rewritten:

"**§ 105-163.40. Time for submitting declaration; time and method for paying estimated tax.**

(a) Due Dates of Declarations. – Declarations of estimated tax are due at the same time as the corporation's first installment payment. Installment payments are due as follows:

(1) If, before the 1st day of the 4th month of the taxable year, the corporation's estimated tax equals or exceeds ~~five thousand dollars~~

~~($5,000),~~ five hundred dollars ($500.00), the corporation shall pay the estimated tax in four equal installments on or before the 15th day of the 4th, 6th, 9th and 12th months of the taxable year.

(2) If, after the last day of the 3rd month and before the 1st day of the 6th month of the taxable year, the corporation's estimated tax equals or exceeds ~~five thousand dollars ($5,000),~~ five hundred dollars ($500.00), the corporation shall pay the estimated tax in three equal installments on or before the 15th day of the 6th, 9th and 12th months of the taxable year.

(3) If, after the last day of the 5th month and before the 1st day of the 9th month of the taxable year, the corporation's estimated tax equals or exceeds ~~five thousand dollars ($5,000),~~ five hundred dollars ($500.00), the corporation shall pay the estimated tax in two equal installments on or before the 15th day of the 9th and 12th months.

(4) If, after the last day of the 8th month and before the 1st day of the 12th month of the taxable year, the corporation's estimated tax equals or exceeds ~~five thousand dollars ($5,000),~~ five hundred dollars ($500.00), the corporation shall pay the estimated tax on or before the 15th day of the 12th month of the taxable year.

(b) Payment of Estimated Tax When Declaration Amended. – When a corporation submits an amended declaration after making one or more installment payments on its estimated tax, the amount of each remaining installment shall be the amount that would have been payable if the estimate in the amended declaration was the original estimate, increased or decreased as appropriate by the amount computed by dividing:

(1) The absolute value of the difference between:
   a. The amount paid and
   b. The amount that would have been paid if the estimate in the amended declaration was the original estimate by

(2) The number of remaining installments.

(c) Short Taxable Year. – Payment of estimated tax for taxable years of less than 12 months shall be made in accordance with rules promulgated by the Secretary."

Sec. 17. The current operations budget that will likely be adopted by the 1990 Session of the General Assembly will contain $2.8 million of operating budget reductions for the Department of Revenue. This reduction would seriously undermine the actions of the 1989 General Assembly to modernize the State's tax enforcement efforts. In addition, the 1989-91 General Fund revenue estimates used during the budget process are based on projected revenues from the enactment of the modernization program. Thus, the proposed budget cuts will have a direct negative impact on 1990-91 revenue collections and will exacerbate the recognized 1991 Session General Fund shortfall.

It is the intent of the General Assembly that the proceeds of this act shall be used to maintain the integrity of the 1989 Session action modernizing the State's tax enforcement program.

Sec. 18. Section 1 of this act is effective retroactively for taxable years beginning on or after January 1, 1989, and shall expire for taxable years beginning on or after July 1, 1991. Sections 5 and 6 of this act are effective for taxable years beginning on or after January 1, 1990. Sections 7 through 14 of this act are effective upon ratification and apply to taxable years ending on or after the date of ratification. Sections 15 and 16 of this act are effective for taxable years beginning on or after August 1, 1990. The remainder of this act is effective retroactively for taxable years beginning on or after January 1, 1989.

In the General Assembly read three times and ratified this the 19th day of July, 1990.