I. FRANCHISE TAX  
(Article 3)

A. General Information (G.S. 105-114)

1. Scope and Nature

North Carolina levies a series of franchise taxes upon corporations, both domestic and foreign, and upon certain persons, limited liability companies (“LLCs”), and partnerships. The taxes levied in this subchapter are for the privilege of engaging in business or doing the act named. Specific sections of the law under which the various corporations and businesses are taxed are as follows:

- G.S. § 105-114.1 Limited liability companies
- G.S. § 105-120.2 Holding companies
- G.S. § 105-122 General business corporations
- G.S. § 105-125 Exempt corporations

The taxes levied upon corporations organized under the laws of North Carolina (domestic corporations) are for the corporate rights and privileges granted by their charters, and the enjoyment of corporate powers, rights, privileges and immunities under the laws of North Carolina.

The taxes levied upon corporations not organized under the laws of North Carolina (foreign corporations) are for the privilege of doing business in this State and for the benefit and protection they receive from the government and laws of this State.

A corporation, other than a holding company taxed under G.S. § 105-120.2, that is subject to one of the franchise taxes other than the general business franchise tax, is subject to the general business franchise tax to the extent it exceeds the other franchise tax.

2. Corporation Defined

For franchise tax purposes, the term “corporation” includes not only corporations in the usual meaning of the term, but also associations, joint stock companies, trusts and other organizations formed or operating for pecuniary gain which have capital stock represented by shares and privileges not possessed by individuals or partnerships. The term includes limited liability companies that elect to be taxed as corporations for federal income tax purposes.

3. S Corporations

S corporations are liable for franchise tax levied under Article 3 of the Revenue Laws.

4. Period Covered
Taxes levied under this Article are for the fiscal year of the State in which they become due, except that the taxes levied are for the income year of the corporation in which such taxes become due.

5. **Inactive Corporations (17 NCAC 05B.0104)**

A corporation that is inactive and without assets is subject to an annual minimum franchise tax of two hundred dollars ($200). Failure to file this return and pay the minimum tax will result in the suspension of the Articles of Incorporation or Certificate of Authority. Any corporation that intends to dissolve or withdraw through suspension for nonpayment of franchise tax should indicate its intention in writing to the Department.

6. **Voluntary Dissolution or Withdrawal of Corporate Rights (G.S. § 105-127(d))**

Corporations are not subject to franchise tax after the end of the income year in which articles of dissolution or withdrawal are voluntarily filed with the Secretary of State unless they engage in business activities not reasonably incidental to winding up their affairs. Therefore, no franchise tax is required with the income tax return filed for the year in which the application is filed or with any subsequent income tax returns that may be required in connection with winding up the affairs of the corporation.

Example 1: A calendar year corporation voluntarily files articles of dissolution or withdrawal during the calendar year 2017. Although its final income tax return will be filed on a franchise and income tax return, the franchise tax portion of the return need not be completed since the franchise tax applicable to calendar year 2017 was calculated on the 2016 tax return.

Example 2: A corporation using an income year ending April 30 voluntarily files articles of dissolution or withdrawal on May 19, 2017. Although its final income tax return will be filed on a franchise and income tax return, the franchise tax portion of the return need not be completed since the franchise tax applicable to the income year beginning May 1, 2017, was calculated on the tax return for the income year ended April 30, 2017.

A corporation is not entitled to a partial refund of franchise tax paid if the corporation files articles of dissolution or withdrawal during the year.

7. **Payment of Franchise Taxes (G.S. § 105-122(a))**

Franchise tax is due on the statutory filing date of the return, without regard to extensions.

8. **Extension of Filing Date (17 NCAC 05B.0107)**

A corporation subject to the franchise tax may obtain an extension of time for filing its franchise tax return by filing Form CD-419 within the time required pursuant to G.S. § 105-263. Form CD-419 is available at: [http://www.dor.state.nc.us/downloads/corporate.html](http://www.dor.state.nc.us/downloads/corporate.html).
An extension of time for filing a franchise tax return does not extend the time for paying the tax due or the time when a penalty attaches for failure to pay the tax. For additional detailed information concerning the requirements for obtaining an extension of time for filing a corporate franchise and income tax return, see “Extension of Time for Filing Return” in Section II, Corporate Income Tax.

9. **Tax Credit for Limited Liability Companies Subject to Franchise Tax (G.S. § 105-122.1)**

LLCs that elect to be taxed as corporations for federal income tax purposes are allowed a tax credit against franchise tax equal to the difference between the annual report fee on corporations for filing paper annual reports under G.S. § 55-1-22(a)(23) and the annual report fee for limited liability companies under G.S. § 57D-1-22. The credit allowed may not exceed the franchise tax liability for the year reduced by the sum of all credits allowed, except payments of tax made by or on behalf of the taxpayer.

Example. An LLC that has elected to be taxed as a corporation computes its franchise tax due to be $500. Because the fee under for an LLC under G.S. § 57D-1-22 is $200, while the fee for a corporation filing a paper annual report under G.S. § 55-1-22(a)(23) is $25, a credit of $175 is allowed to the LLC against franchise tax.
B. Holding Companies (G.S. § 105-120.2)

1. Definition

A holding company is any corporation that receives more than eighty percent (80%) of its gross income during its taxable year from corporations in which it owns, directly or indirectly, more than fifty percent (50%) of the outstanding voting stock or voting capital interest. A corporation will also qualify for holding company status if it has no assets other than ownership interests in corporations in which it owns, directly or indirectly, more than 50% of the outstanding stock or voting capital interests.

If a holding company has an ownership interest in an LLC doing business in the State and the LLC is taxed as a corporation for federal income tax purposes, the holding company’s share of the income of the LLC is included in the denominator and, if the corporation owns more than fifty percent (50%) of the voting capital interest in the LLC, the holding company’s share of the income of the LLC is included in the numerator when computing the holding company test.

2. Basis for Taxation

The basis of the tax for a holding company is the same as for general business corporations. However, franchise tax payable by a qualified holding company on its net worth base is limited to one hundred and fifty thousand dollars ($150,000). Any corporation that qualifies as a holding company for franchise tax should fill in the circle next to Line 1 on Page 1 of the appropriate form, CD-405 or CD-401S. There is no limitation on the amount of franchise tax payable where the tax produced by the investment in tangible property or appraised value of property exceed the tax produced by the net worth base.
C. General Business Corporations (G.S. § 105-122)

1. Basis for the Tax

For years beginning on or after January 1, 2017, the basis of the tax is the net worth of the taxpayer. The basis is the same for both domestic and foreign corporations. Corporations doing business both within and without North Carolina are required to apportion their net worth to North Carolina in accordance with a specified statutory apportionment formula. Regardless of the actual amount of net worth, the amount determined for purposes of this tax cannot be less than fifty-five percent (55%) of appraised ad valorem tax value of all the real and tangible property in North Carolina or less than the actual investment in tangible property in North Carolina.

2. Franchise Tax Calculation

Franchise tax is calculated on the largest of the following amounts:

- The net worth tax base
- Fifty-five percent (55%) of appraised ad valorem tax value of all real and tangible property in N. C.
- Actual investment in tangible property in North Carolina

3. Corporations Required to File

Unless specifically exempt under G.S. § 105-125, all active and inactive domestic corporations, and all foreign corporations with a Certificate of Authority to do business, or which are in fact doing business in this State, are subject to the annual franchise tax levied under G.S. § 105-122.

If an LLC is taxed as a corporation for federal tax purposes and a corporate member’s only connection to North Carolina is its ownership interest in the LLC, the corporate member(s) is not required to file a North Carolina corporate income and franchise tax return. The corporate member(s) is not required to file in this circumstance because the LLC reports its North Carolina income at the entity level and the apportionment attributes of the LLC do not flow through to the corporate member(s) as is the case when the LLC is disregarded or is treated as a partnership.

If an LLC is taxed as a corporation for federal tax purposes and a corporate member has activities in this State in addition to its ownership interest in the LLC, the corporate member(s) is required to file a corporate income and franchise tax return.

4. Forms to be Used for Filing
The franchise tax is filed on Form CD-405 for C corporations and Form CD-401S for S corporations. These forms, along with other required corporate forms and instructions, are available from the Department’s web site at:


5. **Substitute Returns**

Any substitute form must be approved by the Department of Revenue prior to its use. The guidelines for producing substitute forms are available on the Department’s website. If a taxpayer uses computer-generated returns, the software company is responsible for requesting and receiving an assigned barcode. The Department publishes a list of software developers that have received approval on the Department’s web site. Photocopies of the return are not acceptable. Returns that cannot be processed by our imaging and scanning equipment may be returned to the taxpayer with instructions to refile on an acceptable form.

6. **Report and Payment Due**

Corporations must file returns annually on or before the fifteenth day of the fourth month following the end of the income year. The return is filed as a part of a joint franchise and income tax return. Payment of the entire amount of franchise tax is required by the statutory due date of the return.

7. **Tax Rate**

The franchise tax rate is one dollar and fifty cents ($1.50) per one thousand dollars ($1,000) and is applied as set forth in the law. The minimum franchise tax is two hundred dollars ($200).

8. **Franchise Tax Payable in Advance (G.S. § 105-114)**

Franchise tax is payable in advance for the privilege of doing business in North Carolina or for the privilege of existing as a corporation in North Carolina.

Example: A corporation incorporates, domesticates or commences business in North Carolina on October 15, 2016. The corporation has selected a calendar year end. The first tax return due on April 15, 2017 will be a short period return covering the income tax period from October 15, 2016 to December 31, 2016. Franchise tax due on this return covers the ensuing calendar year through December 31, 2017 for the privilege of doing business in North Carolina or for the privilege of existing as a corporation in North Carolina.
D. Net Worth Base (G.S. § 105-122(b)) – (Applicable to Tax Years Beginning On or After January 1, 2017 calculated on 2016 and after income tax returns)

1. Based on Year End Balance Sheet

Net worth is measured as of the end of the taxable year using generally accepted accounting principles (“GAAP”). If the corporation does not use GAAP in maintaining its books and records, then net worth is computed using the same accounting method used for federal income tax purposes, so as long as this method fairly represents the corporation’s net worth for franchise tax purposes.

2. Net Worth Defined

A corporation’s net worth is defined as the total assets of the corporation without regard to deductions for accumulated depreciation, depletion, or amortization minus total liabilities.

3. Adjustments to Net Worth

In determining net worth, the following adjustments are required:

(a) A deduction for accumulated depreciation, depletion, or amortization allowed for federal income tax purposes.

(b) A deduction for the cost of treasury stock.

(c) An addition for the amount of affiliated indebtedness owed to a parent, subsidiary, affiliate, or noncorporate entity if the corporation or affiliated group directly or indirectly owns 50% or more of the noncorporate entity, other than debt that is merely endorsed, guaranteed or otherwise supported by the corporation or affiliated group of corporations. The addition for affiliated indebtedness may be reduced based on the ratio of the borrowed capital over the total assets of the creditor corporation. Borrowed capital does not include indebtedness incurred by a bank from a deposit evidenced by a certificate of deposit, passbook, cashier’s check, certified check, or similar document or record.

(d) A creditor corporation that is subject to franchise tax may deduct the amount of indebtedness owed to it by a parent, subsidiary, or affiliated corporation to the extent such indebtedness has been added by the debtor corporation in computing its franchise tax liability.

4. Other Definitions

In determining the net worth base, the following definitions apply:

(a) Affiliate – A corporation is an affiliate of another corporation if it is controlled directly or indirectly by the same parent corporation or same or associated financial interests through
stock ownership, interlocking directors, or by any other means whatsoever, whether the control is direct or through one or more subsidiary, affiliate, or controlled corporation.

(b) **Affiliated Group** – The same meaning as defined in G.S. § 105-114.1.

(c) **Capital Interest** – The right under the entity’s governing law to receive a percentage of the entity’s assets, after payments to creditors, if the entity were dissolved.

(d) **Governing Law** – The law under which the noncorporate entity was organized.

(e) **Indebtedness** – All loans, credits, goods, supplies, or other capital of whatsoever nature furnished by a parent, a subsidiary, an affiliate, or a noncorporate entity in which the corporation or an affiliated group of corporations owns directly or indirectly more than 50% of the capital interests of the noncorporate entity. Indebtedness does not include amount endorsed, guaranteed, or otherwise supported by one of the related corporations.

(f) **Noncorporate entity** – a person that is neither a human being nor a corporation.

(g) **Parent** – A corporation that directly or indirectly controls another corporation by stock ownership, interlocking directors, or by any other means whatsoever exercised by the same or associated financial interests, whether such control is direct or through one or more subsidiary, affiliated, or controlled corporations.

(h) **Subsidiary** – A corporation that is directly or indirectly subject to control by another corporation by stock ownership, interlocking directors, or by any other means whatsoever exercised by the same or associated financial interest, whether the control is direct or through one or more subsidiary, affiliated, or controlled corporations.

(i) **Total assets** – The sum of all cash, investments, furniture, fixtures, equipment, receivables, intangibles, and any other items of value owned by a person or a business entity.
E. Multistate Corporations (G.S. § 105-122(c1))

1. Apportionment Formula

Every corporation permitted to apportion its net income for income tax purposes under the provisions of G.S. § 105-122(c1) must apportion its net worth for franchise tax purposes through use of the same fraction computed for apportionment of its apportionable income under G.S. § 105-130.4. A corporation that is subject to the general business franchise tax, but exempt from income tax, must apportion its net worth by using the apportionment factor it would have used had it been subject to the income tax. Adjustments in the method of apportionment authorized by the Secretary of Revenue for apportionment of net income do not apply automatically to apportionment of net worth. Unless the Secretary specifically authorizes a modified method of allocation for franchise tax purposes, the statutory formula must be used.

2. Alternate Apportionment Formula

If any corporation believes that the statutory apportionment formula allocates more of its net worth to North Carolina than is reasonably attributable to its business in this State, it may make a written request to the Secretary of Revenue for permission to use an alternative formula which it believes is a better method to apportion its net worth to North Carolina.

The written request must be made with the Secretary not later than ninety (90) days after the regular or extended due date of the tax return. Taxpayers should address all correspondence in connection with such petitions to the Secretary of the Revenue.

The Secretary must issue a written decision on a corporation’s request for an alternative apportionment method. The decision can apply to no more than three years. If the request is denied, the Secretary’s decision is final and is not subject to administrative or judicial review. A corporation authorized to use an alternative formula may apportion its net worth base using the alternative method or the statutory method.
F. Investment in Tangible Property in North Carolina Base (G.S. § 105-122(d))

1. Basis For the Investment Base

   This base includes the original purchase price plus additions and improvements and less reserve for depreciation permitted for income tax purposes of all tangible property, including real estate located in North Carolina at the end of the income year immediately preceding the due date of the return.

2. What is Includable in the Investment Base (17 NCAC 05B.1302)

   Include all tangible assets located in North Carolina at original purchase price less reserve for depreciation permitted for income tax purposes. In addition to the types of property listed in the schedule, include all other tangible property owned such as supplies and tools. Typical items of tangible property would include: inventory (valued at actual cost or by method consistent with the actual flow of goods), consigned inventories to be included by consignor, machinery and equipment, furniture and fixtures, containers, tools and supplies, land, buildings, leasehold improvements, and all other tangible assets.

3. Treatment of Construction in Progress (17 NCAC 05B.1303)

   Construction in progress is excluded from this base only if such property is not owned by the corporation filing the return.

4. Determination of Inclusion Based on Depreciation Deduction (17 NCAC 05B.1309)

   When two or more corporations are in doubt as to which should include property, including leased property, in the investment in tangible property base, such property shall be included by the corporation allowed depreciation under the Federal Code.

5. Holding Company

   There is no limitation on the franchise tax payable by a holding company on its investment in tangible property tax base.
G. **Appraised Valuation of Tangible Property Base (G.S. § 105-122(d), 17 N.C.A.C. 05B.1406)**

Tangible property values for this base are computed on fifty-five percent (55%) of the appraised value of all property listed for county ad valorem tax in North Carolina as of January 1 of the calendar year next preceding the due date of the return.

Note: Also included in the appraised value of property for county ad valorem tax is the appraised value of all vehicles for which the county tax assessor has issued a billing during the income year.

There is no limitation on the franchise tax payable by a holding company on its appraised valuation of property tax base.
H. Corporate Members of LLCs (G.S. § 105-114.1)

(This section does not apply to limited liability companies that are taxed as corporations, but does apply to noncorporate limited liability companies, i.e., limited liability companies that do not elect to be taxed as corporations under the Code.)

If a corporation or affiliated group of corporations owns, directly or constructively, more than fifty percent (50%) of the capital interests in an LLC, the corporation or group of corporations must include the same percentage of the LLC’s assets in its three franchise tax bases. In that case, the corporation’s investment in the LLC is not included in the calculation of the corporation’s capital stock, surplus and undivided profits base. The attribution to the three bases is equal to the same percentage of (1) the LLC’s capital stock, surplus and undivided profits, (2) fifty-five percent (55%) of the LLC’s appraised ad valorem tax value of property, and (3) the LLC’s actual investment in tangible property in this State.

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

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

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

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

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

If the owner of the capital interests in an LLC is an affiliated group of corporations, the percentage to be included by each member that is doing business in this State is determined by multiplying the capital interests in the LLC owned by the affiliated group by a fraction.
The numerator of the fraction is the capital interests of the LLC owned by the group member, and the denominator is the capital interests in the LLC owned by all group members that are doing business in this State.

Ownership of the capital interests in an LLC is determined under the constructive ownership rules for partnerships, estates, and trusts in IRC § 318(a)(2)(A) and (B), modified as follows:

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

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

Corporation A: \[100\% \times 50\% \div (50\% + 10\%) = 83.33\%\]
Corporation B: \[100\% \times 10\% \div (50\% + 10\%) = 16.67\%\]

A corporation that is required to include a percentage of the LLC’s assets in its franchise tax computation may exclude its investment in the LLC from its computation of the net worth base.

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

Any taxpayer who, because of fraud with intent to evade tax, underpays the tax under this Article (G.S. 105 Article 3) is guilty of a Class H felony in accordance with G.S. 105-236(7). For additional information on the filing requirements for members of LLCs, see Item 5, Subsection J “Corporations Conditionally or Partially Exempt.”
I. Change of Income Year (105-122(e))

1. Computation of Tax (17 NCAC 05B.1501)

A change in income year automatically establishes a new franchise year. A joint franchise and income tax return is required for the short income period. Credit is permitted on such return against the franchise tax to the extent that the new franchise year overlaps the old year.

Example: A corporation changes its income year from a calendar year to one ending July 31. A combined franchise and income return is required for the short period January 1, 2017 through July 31, 2017 (seven (7) months). Franchise tax paid on the 2016 return applicable to the calendar year 2017 was $240. Franchise tax on the short period would be applicable to the year August 1, 2017 through July 31, 2018, and would be computed as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total tax due per return</td>
<td>$268</td>
</tr>
<tr>
<td>Less credit for portion of prior year’s tax:</td>
<td></td>
</tr>
<tr>
<td>Total tax paid on 2006 return</td>
<td>$240</td>
</tr>
<tr>
<td>Less amount applicable to short period (7/12 of $240)</td>
<td>140</td>
</tr>
<tr>
<td>Amount applicable beyond short period</td>
<td>100</td>
</tr>
<tr>
<td>Net franchise tax due on short period return</td>
<td>$168</td>
</tr>
</tbody>
</table>

G.S. § 105-129.5(b) applies in computing the net franchise tax due for the short period. The statutorily computed tax is reduced by current installments and carryforwards of available tax credits, subject to the fifty percent (50%) limitation, before calculating the amount applicable to the short period and the amount applicable beyond the short period.

2. Computation of Tax When Merger is Involved (17 NCAC 05B.1502)

Often when two corporations merge, a question arises concerning which corporation is liable for the franchise tax. If the merger is effective at any time after the close of the submerged corporation’s year-end, then the submerged corporation is liable for the tax. If the merger is effective at any time prior to the close of the submerged corporation’s year-end, then the surviving corporation is liable for the tax.

Since franchise tax is paid prospectively, a special computation is sometimes required to prevent a duplication of tax when two or more corporations with different income years merge or otherwise transfer the entire assets from one corporation to the other. The following example illustrates the conditions under which this occurs.

Example: ABC Corporation, whose income year ends July 31, merged into XYZ Corporation, whose income year is the calendar year. The merger occurred on October 31, 2016. ABC filed a combination franchise and income tax return for the year ended July 31, 2016 and paid franchise tax of six hundred dollars ($600) applicable to the ensuing year ending July 31, 2017. XYZ filed a combination franchise and income tax return for the
calendar year 2016 and paid franchise tax of seven hundred dollars ($700) applicable to the ensuing calendar year 2017. The assets reflected in ABC’s tax base were also reflected in XYZ’s tax base since they had been transferred to XYZ in the merger, and therefore, were on its books as of the end of its income year, December 31, 2016. The year to which ABC’s payment applied overlapped the year to which XYZ’s payment applied by seven months (January 1, 2017 through July 31, 2017) and reflected a duplication of tax to that extent.

When the conditions illustrated in the above example exist, where, the acquiring corporation acquired the entire assets of the disposing corporation, the acquiring and disposing corporations had different income years, the date of merger or transfer was after the end of the disposing corporation’s income year next preceding such transfer but before the beginning of the surviving corporation’s income year next following such transfers, and the disposing corporation had paid franchise tax applicable to its income year in which the transfer occurred, the acquiring corporation may compute its franchise tax on its franchise and income tax return for the income year in which the transfer occurred as shown in the following example:

Franchise tax per surviving corporation’s return for income year in which transfer occurred

Less: Franchise tax paid by submerged corporation per return for income year immediately preceding transfer

Number of months between the ending dates on the above returns

Number of months in year x $600 =

Amount pertaining to overlapping months

Net franchise tax due
J. Corporations Conditionally or Partially Exempt (G.S. § 105-122, G.S. § 105-125)

1. Non-Profit Organizations

The following organizations and any other organization exempt from federal income tax under the Code are exempt from franchise tax if they are not organized for profit and if no profit inures to the benefit of any member, shareholder or other individual:

a. Fraternal societies, orders or associations. To qualify for income tax exemption, the organization must operate under the lodge system or for the exclusive benefit of members of a fraternity that is operating under the lodge system, and provide life, sick, accident or other benefits to the members or their dependents.

b. Corporations organized or trusts created for religious, charitable, scientific or educational purposes, including cemetery corporations and organizations for the prevention of cruelty to children and animals.

c. Business leagues, chambers of commerce, merchants associations and boards of trade.

d. Civic leagues or organizations operated exclusively for the promotion of civic welfare.

e. Clubs organized and operated exclusively for pleasure, recreation and other non-profit purposes.

f. Mutual hail, cyclone and fire insurance companies; mutual ditch, irrigation, canning and breeding associations; mutual or cooperative telephone companies; and like organizations of a purely local character which derive their entire income from assessments, dues or fees collected from members for the sole purpose of meeting expenses.

g. Farmer’s marketing associations operating as sales agents to market the products of members or other farmers, and to return to them the proceeds, less the necessary selling expenses, on the basis of the quantity of product furnished by them.

h. Pension, profit-sharing, stock bonus and annuity trusts established by employers for the purpose of distributing both the principal and income thereof exclusively to eligible employees or the beneficiaries of such employees. There must be no discrimination in favor of any particular employee. The interest of individual employees must be irrevocable and nonforfeitable to the extent of contributions by such employees. Exemption of a trust under the Federal income tax law is a prima facie basis for granting exemption from North Carolina franchise and income taxation.

i. Condominium associations, homeowner associations or cooperative housing corporations not organized for profit, the membership of which is limited to the owners or occupants of residential units in the condominium, housing development, or cooperative housing corporation.
2. Corporations Fully Exempt

These corporations qualify for the full franchise tax exemption:

- Insurance companies subject to the tax on gross premiums are exempt from the general business franchise tax.
- Telephone membership corporations organized under Chapter 117 of the General Statutes of North Carolina are exempt from the general business franchise tax. Electric membership corporations are, however, subject to franchise tax.

3. Regulated Investment Companies (RIC) and Real Estate Investment Trusts (REIT)

These organizations are required to pay franchise tax; however, in determining net worth they are allowed to deduct the aggregate market value of investments in the stock, bonds, debentures, or other securities or evidences of debt of other corporations, partnerships, individuals, municipalities, governmental agencies or governments. Captive REITs are not allowed this deduction. A captive REIT is a REIT whose shares or certificates of beneficial interest are not regularly traded on an established securities market and are owned or controlled, at any time during the last half of the tax year, by a person that is subject to tax under this Part and is not a trust or another entity that qualifies as a real estate investment trust under section 856 of the Code or a listed Australian property.

4. Real Estate Mortgage Investment Conduits (REMIC)

These organizations are exempt from franchise tax to the extent the REMIC is exempt from income tax under the Code.

5. Limited Liability Company (LLC)

The “North Carolina Limited Liability Company Act” (Chapter 57C of the North Carolina General Statutes) permits the organization and operation of limited liability companies (LLC). An LLC is a business entity that combines the S corporation characteristic of limited liability with the flow-through features of a partnership. Noncorporate limited liability companies are not subject to the franchise tax. A noncorporate limited liability company is an LLC that does not elect to be taxed as a corporation under the Code.