NC Chamber Foundation

North Carolina's Business Tax Climate Report

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INTRODUCTION





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Overview

- North Carolina has one of the most competitive business tax climates in the country
- On multiple measures, NC's total taxes and business taxes are lower than the US average and lower than benchmark states
- While NC has a competitive tax environment, the franchise sticks out as one area where NC diverges from other states
- Several other tax and administrative leading practices would help increase NC's competitiveness further

Agenda

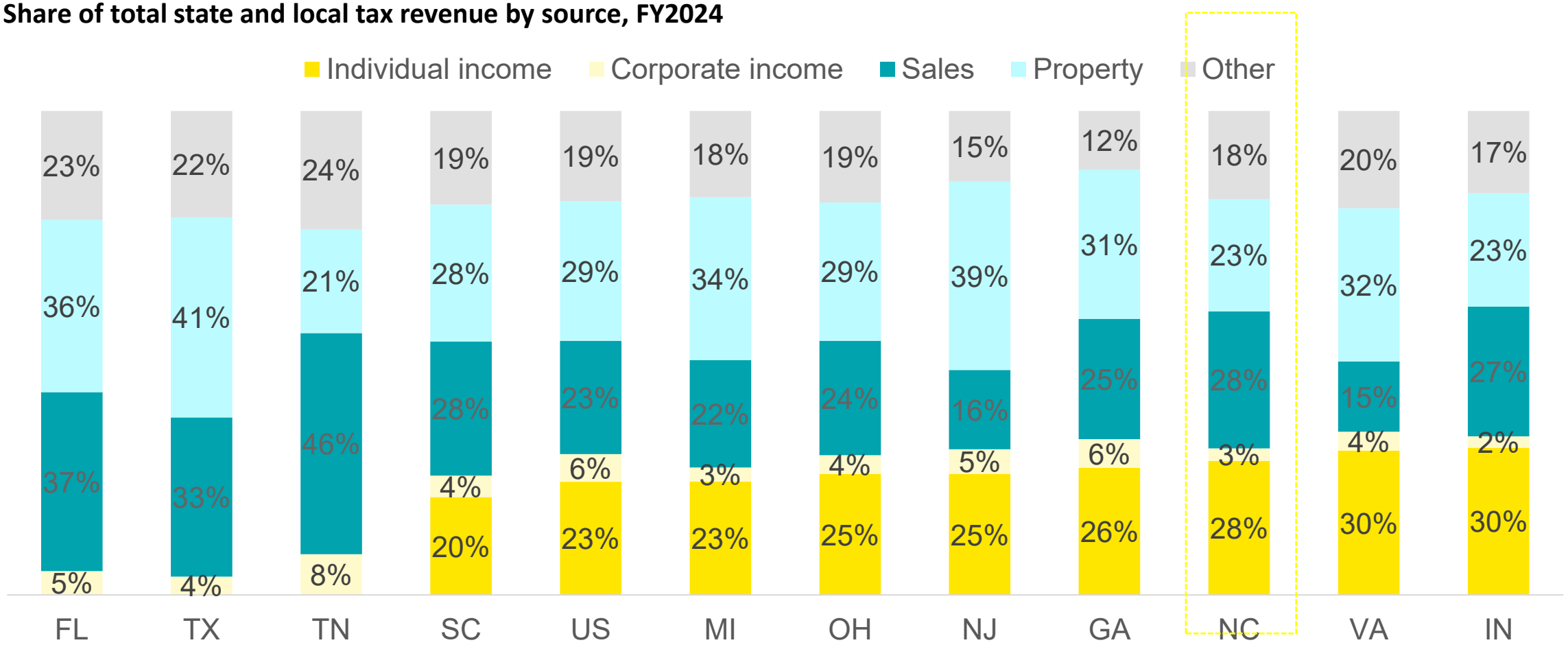
1. Overview of NC's tax structure and revenue collections
2. NC's business tax mix and business tax burden
3. Representative firm analysis
4. Tax structure and administrative changes to improve NC's competitiveness

NC’s total state and local revenue mix

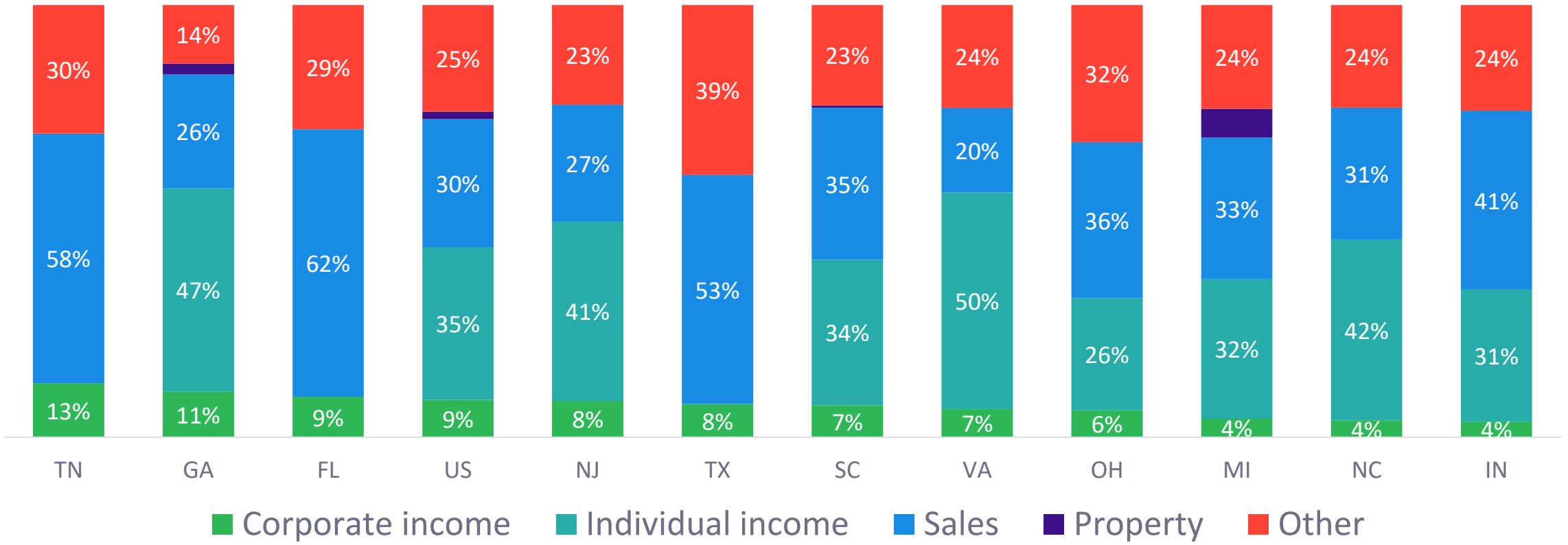
State and local tax revenue in North Carolina, FY24 ($billions)					
Tax type	**FY24**	**% of total FY24**	**FY14**	**10-yr growth**	**Annual growth rate**
Individual income	$16.7	28%	$10.4	60%	4.8%
Sales and use	$17.0	28%	$8.2	109%	7.6%
Property	$14.0	23%	$9.5	48%	4.0%
Corporate income	$1.6	3%	$1.4	15%	1.4%
Franchise tax	$0.7	1%	$0.5	35%	3.0%
Other	$10.2	17%	$8.2	33%	2.9%
Total	**$60.2**	**100%**	**$38.1**	**58%**	**4.7%**

At the state and local level, NC depends more on individual income tax and less on corporate tax than most of the benchmark states

Share of total state and local tax revenue by source, FY2024

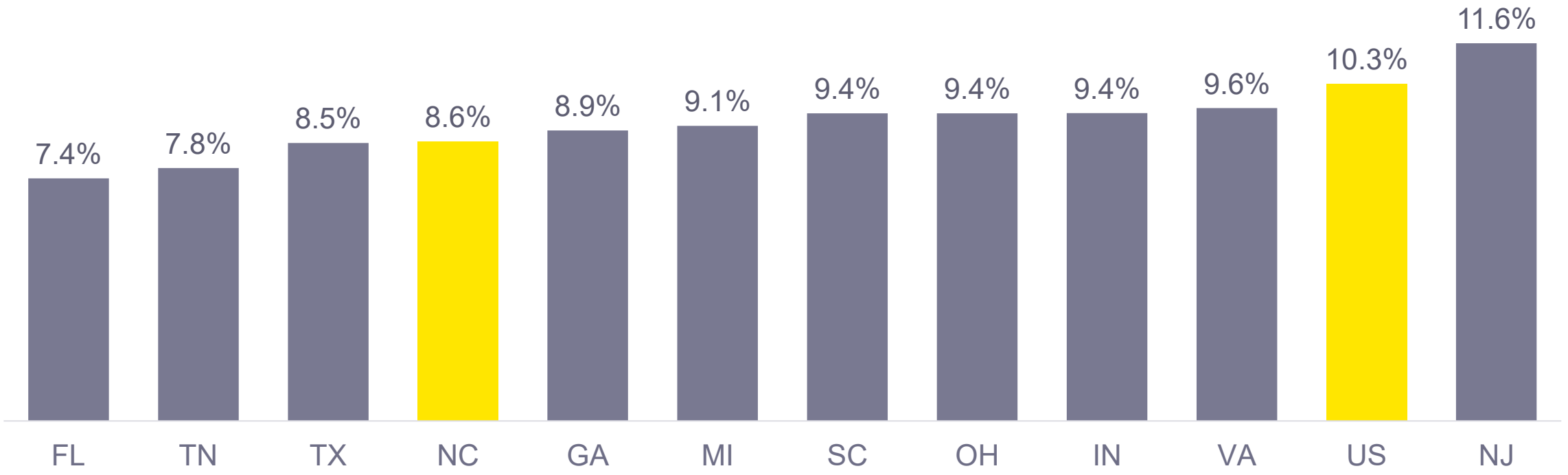


NC's state-level tax mix reflects more reliance on individual income and less on corporate income than US average



NC's overall tax collections are fourth-lowest among benchmark states and significantly less than US average

Total state and local taxes as a share of personal income, FY24



Business taxes: North Carolina relies on business taxes materially less than the US average or benchmark states

Estimated business shares of tax collections in North Carolina, US and peer state average, by tax type, FY24			
Tax type	**North Carolina**	**Benchmark states**	**United States**
Corporate income	100.0%	100.0%	100.0%
Property	49.4%	46.1%	54.1%
Sales	41.0%	39.9%	41.8%
Individual income*	12.2%	13.1%	15.8%
Other	54.3%	55.6%	59.1%
Total	**38.9%**	**40.8%**	**45.8%**

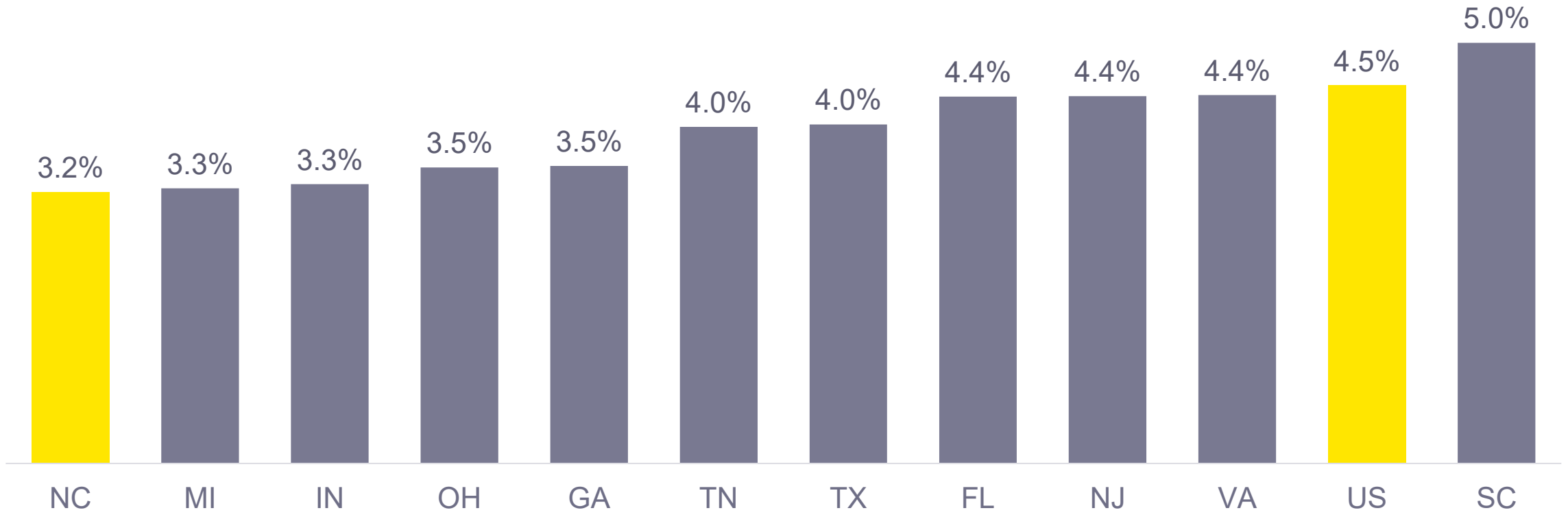
*Business share for this category is pass-through income taxes and pass-through entity tax.

Source: Ernst & Young LLP estimates based on data from the U.S. Census Bureau Annual Survey of State and Local Government Finances.

Note: Other taxes include corporate license (franchise),death and gift, documentary and stock transfer and severance taxes.

Business taxes: NC has the lowest amount of business tax collected per dollar of gross state product (economic activity)

Total effective business tax rates, TEBTR FY24



Source: Ernst & Young LLP estimates based on data from the U.S. Census Bureau Annual Survey of State and Local Government Finances and state annual consolidated fiscal reports. See the EY and Council on State Taxation, "Total state and local business taxes: state-by-state estimates for FY24," December 2025.

Business taxes: NC's business tax collections per dollar of GSP are lower than benchmark for most taxes

State and local business taxes as a share of state GSP, by type of tax, FY24							
	Individual income	Corporate income	Franchise /net worth	Sales	Property	Other	Total
South Carolina	0.22%	0.45%	0.06%	1.03%	2.21%	0.95%	4.93%
New Jersey	0.59%	0.62%	0.00%	0.86%	1.16%	1.14%	4.37%
Florida	0.00%	0.40%	0.00%	1.26%	1.66%	1.05%	4.37%
Virginia	0.25%	0.40%	0.00%	0.60%	1.98%	1.11%	4.35%
Texas	0.00%	0.28%	0.00%	1.27%	1.76%	0.99%	4.30%
Tennessee	0.00%	0.62%	0.30%	1.35%	0.92%	0.77%	3.96%
Georgia	0.23%	0.47%	0.01%	0.86%	1.39%	0.59%	3.54%
Ohio	0.18%	0.34%	0.00%	0.83%	1.23%	0.95%	3.53%
Indiana	0.44%	0.21%	0.00%	0.75%	1.33%	0.60%	3.32%
Michigan	0.22%	0.27%	0.00%	0.74%	1.28%	0.78%	3.28%
North Carolina	0.28%	0.21%	0.10%	0.96%	0.95%	0.72%	3.23%
Benchmark avg.	0.16%	0.37%	0.03%	1.04%	1.49%	0.92%	4.00%
United States	0.37%	0.56%	0.02%	0.97%	1.54%	1.07%	4.53%

Source: Ernst & Young LLP estimates based on data from the U.S. Census Bureau Annual Survey of State and Local Government Finances and state annual consolidated fiscal reports. See the EY and Council On State Taxation, "Total state and local business taxes: state-by-state estimates for FY24," December 2025. Note: amounts may not sum due to rounding.

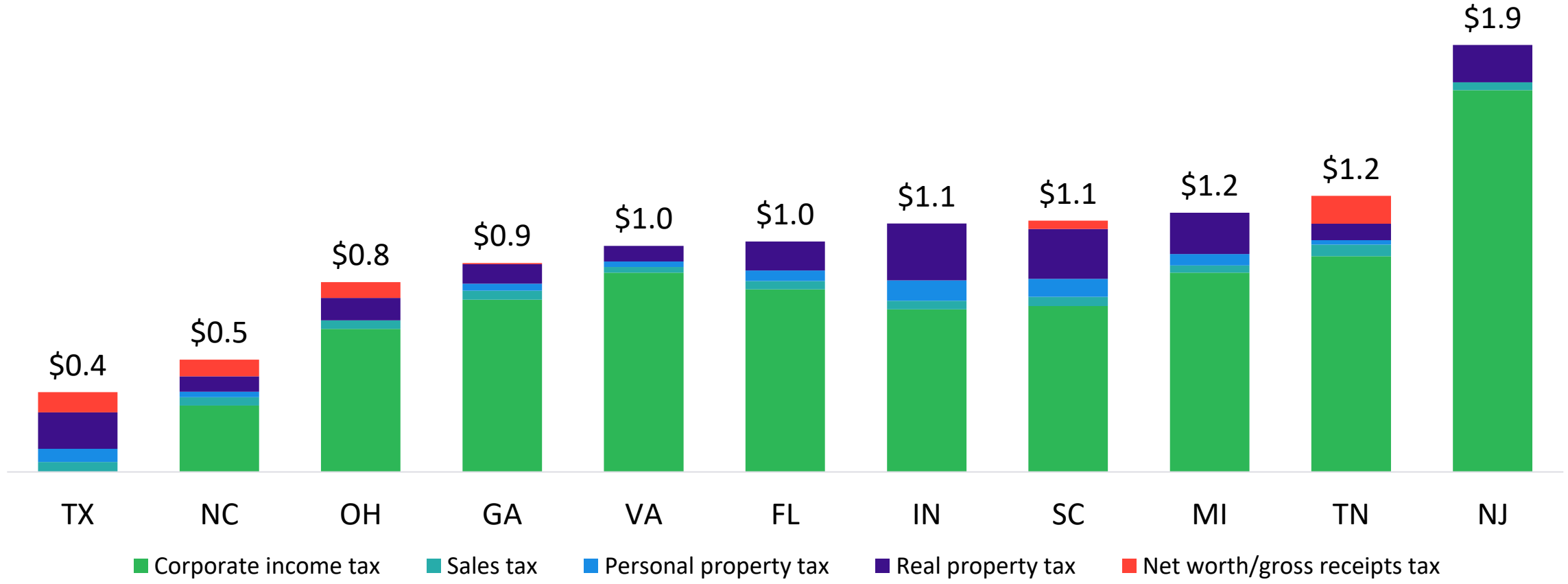
Representative firms: Three firms are developed to illustrate differential impacts of NC's business tax structure

Financial profiles for representative firms ($000s)			
	High-margin mature firm	Start-up innovator	High-volume, low-margin mature firm
Net worth, total	$50,000	$50,000	$50,000
Capital stock	5,535	10,075	1,126
Additional paid-in capital	32,340	107,723	14,568
Total assets	112,726	144,024	90,007
Depreciable assets	9,986	17,261	19,458
Business receipts	27,309	37,312	60,064
Other deductions	3,606	9,495	3,710
Cost of goods sold	15,251	23,970	47,609
Net income	14,853	(13,016)	2,968
Return on equity	30%	-26%	6%
Profit margin	54%	-35%	5%

Source: Ernst and Young LLP based on IRS Statistics of Income, U.S. Economic Census and U.S. Bureau of Economic Analysis data. High-margin firm is based on positive net income pharmaceutical corporate taxpayers, the start up innovator is based on no net income pharmaceutical companies, and the low-margin mature firm is based on the food wholesale industry.

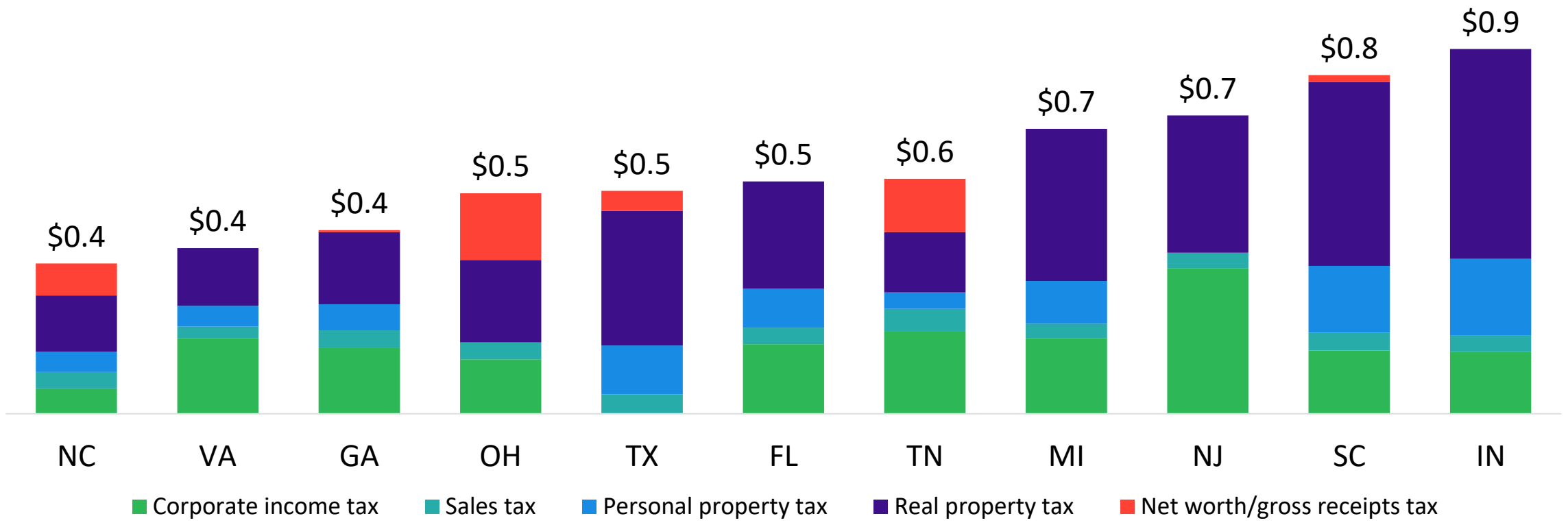
Representative firms:
North Carolina is second-most competitive for high-margin firm

Annual taxes for mature high-margin firm with $50 million net worth ($000s)



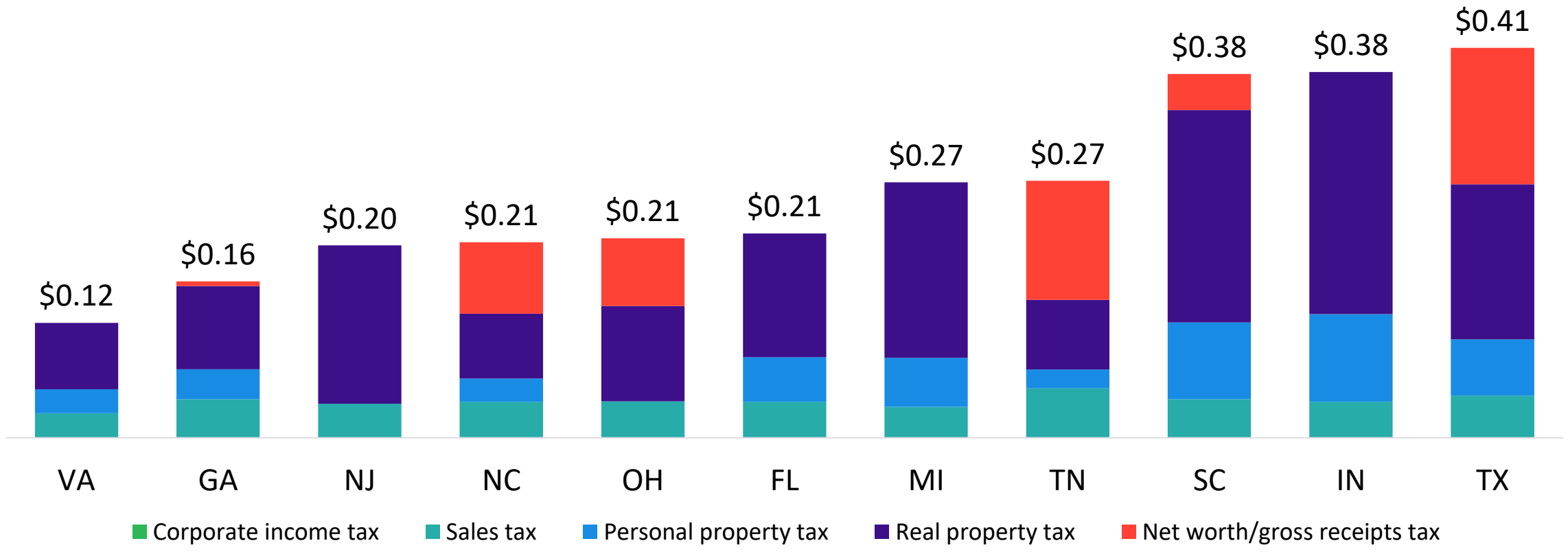
Representative firms:
North Carolina is most competitive for high-volume firm

Annual tax for mature, high volume, low margin firm with $50 million net worth ($000s)



Representative firms:
North Carolina is fourth-most competitive for start-up innovator

Annual tax for loss-making firm with $50 million net worth ($000s)



Franchise tax

- The franchise tax is levied on net worth, making it a tax on capital invested rather than income. As a key factor of productivity, taxing capital investment runs contrary to promoting economic growth.
- North Carolina's franchise tax burden equals 0.10% of GSP, compared to a benchmark-state average of 0.03% and a national average of 0.02%. Among benchmark states, only Georgia, South Carolina, and Tennessee retain some form of net worth or capital stock tax.
- The tax disproportionately impacts start-ups, growth-stage companies, and other well-capitalized firms with low or negative earnings, because liability is based on capital rather than profitability.
- For a representative start-up innovator firm, the franchise tax is the primary reason North Carolina ranks only fourth-best among peers despite otherwise favorable tax policies.
- The franchise tax generates only 1.8% of North Carolina state tax revenue, making it a relatively small revenue source.
- Nationally, the trend has been away from taxing net worth and capital stock: 11 states have repealed franchise taxes over the past 25 years, with additional states continuing phase-outs.

Sales tax

- North Carolina provides a sales tax exemption for manufacturers' purchases of equipment and production inputs, as do nearly all states
- North Carolina's exemption generally requires that exempted machinery and production inputs are directly used in production to qualify for exemption
- States applying "integrated plant theory" provide a broader exemption for machinery, equipment, supplies, and utilities that are part of an integrated manufacturing process from the receipt of raw materials through packaging and preparation for shipment

Evaluating State Tax Administration

COST Scorecard: *The Best and Worst of State Tax Administration*

- Evaluates independence and fairness of state tax tribunals and appeals
- Evaluates statutory framework of procedural elements of tax reporting:
  - Even-handed statutes of limitation and interest rates
  - Adequate tax return due dates and extension requests
  - Reporting and filing of federal (IRS) changes
- Assesses transparency in tax guidance and rulings by states
- Highlights other burdensome, inequitable, or ineffective administrative practices or procedures

North Carolina earned a “C” in our latest Scorecard

Improving NC's Tax Administration

State Tax Appeals

- Remove 'pay-to-play' at all levels of appeal
- Require state tax expertise of OAH judges: complex issues demand technical fluency and consistent precedent
- Extend the 45-day protest period to 90 days, matching the ABA Model State Administrative Tribunal Act

Improving State Tax Return Compliance

Easing State Tax Return Compliance

- Extend the corporate tax return due date to one month past the federal due date, thus allowing a more accurate state return with fewer amended filings
- Allow an automatic seven-month extension based solely on the taxpayer's federal extension. No need for a separate State filing.
- The State fisc is not affected since payment of tax is still required by the original due date of the tax return

Improve Reporting and Compliance with Federal Tax Changes

Simplifying the Reporting of IRS Changes to the State

- Corporate taxpayers often file thousands of state returns based using the federal return as a starting point
- When a taxpayer experiences a federal change, all state returns that are affected must be corrected and amended
- North Carolina does not have a clear and consistent definition of "final determination" that triggers the State reporting requirement
- Many states have adopted the Multistate Tax Commission's *"Consensus Model for Reporting Federal Changes including Partnerships"* developed in conjunction with the MTC, COST, AICPA, and the ABA Tax Section
- NC should do the same

Fairness for Nonresident Employees

Reduce Tax Compliance Burdens on Nonresident Employees

- Adopt a 30-day safe harbor before nonresident income tax and withholding requirements attach for employees traveling and working in the State
- Employees and employers continue paying and withholding in the resident state during that period
- Minimizes selective enforcement and will bring thousands of traveling employees into compliance immediately
- COST has drafted model state legislation constructing a 30-day safe harbor before nonresident employees and their employers face North Carolina tax obligations, based on federal legislation
- Uniformity among states with a personal income tax is critical

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