

From the Triangle Business Journal:

<https://www.bizjournals.com/triangle/news/2019/07/12/threat-to-n-c-s-tax-climate.html>

Threat to N.C.'s tax climate

Jul 12, 2019, 6:45am EDT

Sound tax policy and administration is an essential component of North Carolina's competitive business climate. Only six years ago, North Carolina's tax climate was among the worst in the nation, clocking in at 44th. Understanding the detriment this would have on North Carolina's overall competitive standing, the state enacted bipartisan, common sense reforms that catapulted its ranking to 12th in the country. This substantial jump has created greater wealth and opportunity for all North Carolinians, while bolstering North Carolina's economic advantage.

Maintaining a competitive and predictable tax climate requires good tax laws, as well as fair administration and execution of those laws. Improper administration can undermine good policy and do just as much harm as bad policy. Unfortunately, some recent cases involving the North Carolina Department of Revenue (DOR) suggest a worrisome trend toward overreaching and inequitable enforcement.



KEN HAMMOND/ NC CHAMBER

Ray Starling is the general counsel at the North Carolina Chamber.

In a case decided last month by the United States Supreme Court, the DOR attempted to tax an out-of-state trust solely because a trust beneficiary – who had received no money from the trust – was temporarily resident in North Carolina. After the DOR lost in every North Carolina court, the Supreme Court unanimously rejected the department's position holding that it violated the Constitution.

Trying to tax someone with so little connection to the state, the Court said, amounts to “confiscation” and an offense to “traditional notions of fair play and substantial justice.”

The Court's decision is not surprising. What is surprising is that the DOR sought to tax the trust in the first place. The trust was established by a New York resident; its trustees were residents of New York and Connecticut; its funds were held by custodians in Massachusetts; its books, records and tax returns were prepared and maintained in New York; and it was governed by New York law. The North Carolina beneficiary received no money from the trust and had no right to demand any money from it.

Taxing an out-of-state trust based on the temporary residence of a beneficiary who did not receive a penny from it seems obviously wrong, but the DOR still sought to do it. It is doubly concerning that the DOR did not yield gracefully to what every reviewing court in North Carolina said.

In addition to this concerning case, the DOR is also auditing hundreds of North Carolina individuals and businesses who invested in renewable energy partnerships. For some 20 years, until 2016, the General Assembly encouraged investments in these partnerships by offering investors tax credits equal to a percentage of the cost of developing the projects. These credits were made available because, without them, the projects would not have been economically viable.

The tax credit program helped make North Carolina one of the country's top producers of renewable energy. Now that the credits have sunset and the state has received the full benefit of the investment that the credits encouraged, the DOR has done an about-face and is disallowing credits for the last three years of the program. This without any change in the law or investment structures, and after allowing similar investments for almost two decades. The DOR's actions also

threaten continuing tax credit programs, such as the credits for rehabilitating historic structures.

Predictability and certainty are the cornerstones of a flourishing business environment. By enforcing the tax law in a way that offends “traditional notions of fair play” and by changing the rules of the game on taxpayers after the game was over, the DOR is threatening North Carolina’s favorable tax climate. The DOR’s pivot on the renewable energy tax credits is beginning to generate scrutiny among the investment community, and with last month’s Supreme Court decision, increased negative attention seems unavoidable.

Vigilant tax enforcement is important for the rule of law, and everyone must pay their fair share of taxes. However, when an administrative agency gets out of bounds, the rule of law suffers, and in this instance, so might North Carolina’s competitive tax climate.

Ray Starling is general counsel of the NC Chamber and president of the NC Chamber Legal Institute. He can be reached rstarling@ncchamber.org.