

Computation of Net Income

To compute State net income or net loss, a corporation uses its Federal taxable income as defined in the Internal Revenue Code in effect for the tax year for which the return is to be filed as a beginning point and adds thereto or deducts therefrom the items listed below:

Additions to Federal Taxable Income

The following additions to federal taxable income must be made in determining State net income:

- (1) Taxes based on or measured by net income by whatever name called and excess profits taxes.
- (2) Interest paid in connection with income exempt from State income tax.
- (3) Contributions deducted on the federal return.
- (4) Interest income earned on bonds and other obligations of other states or their political subdivisions, less allowable amortization on any bond acquired on or after January 1, 1963.
- (5) The amount by which gains have been offset by the capital loss carry-over allowed under the Internal Revenue Code. (All gains recognized on the disposition of assets must be included in determining State net income or loss in the year of disposition.)
- (6) Net operating loss deducted on the Federal return.
- (7) Payments to or charges by a parent, subsidiary, or affiliated corporation in excess of fair compensation in all intercompany transactions.
- (8) The amount of tax credits allowed against North Carolina income tax. **In lieu of the addback of tax credits to federal taxable income, taxpayers must reduce the amount of credit available by the current income tax rate.**
- (9) The amount of percentage depletion in excess of cost depletion applicable to mines, oil and gas wells, and other natural deposits.
- (10) The amount allowed under the Code for depreciation for a utility plant acquired by a natural gas local distribution company.
- (11) The amount of royalty payments required to be added by G.S. 105-130.7A, to the extent deducted in calculating federal taxable income.
- (12) The amount of gross income from international shipping activities excluded from federal taxable income as a result of the corporation electing to be subject to the tonnage tax under subchapter R of Chapter 1 of the Internal Revenue Code.
- (13) The amount of gross income from domestic production activities deducted on the federal return pursuant to section 199 of the Internal Revenue Code.
- (14) The amount of dividends paid deduction allowed under the Internal Revenue Code to a captive REIT, as defined by G.S. 105-130.12.
- (15) The amount of donation to a nonprofit organization for which a credit is claimed.
- (16) The amount of income deferred under section 108(i)(1) of the code from the discharge of indebtedness in connection with a reacquisition of an applicable debt instrument.
- (17) The amount allowed as a deduction under section 163(e)(5)(F) of the code for an original issue discount on an applicable high yield discount obligation.
- (18) The amount required to be added under G.S. 105-130.5B when the State decouples from federal accelerated depreciation and expensing.

Deductions from Federal Taxable Income

The following deductions from federal taxable income must be made in determining State net income:

- (1) Interest income from obligations of the United States or its possessions net of direct or indirect expense related to the income.
- (2) Interest, net of related expenses, received from North Carolina obligations included in federal taxable income.
- (3) Payments received from an affiliated corporation not deductible by the corporation under North Carolina law.
- (4) The amount of dividends received from sources outside the United States as determined under Section 862 of the Internal Revenue Code, to the extent included in federal taxable income.
- (5) Any amount included in federal taxable income under Section 78 or Section 951 of the Code.
- (6) State net losses incurred by the corporation. **(A State net loss must be deducted on Schedule B, Line 22.)**
- (7) Contributions to the extent provided under G.S. 105-130.9.
- (8) Amortization in lieu of depreciation allowed for federal income tax purposes on the cost of qualified sewage, waste or air pollution facilities, recycling and resource recovering facilities, equipment mandated by OSHA, and equipment and facilities acquired for the purpose of reducing the volume of hazardous waste generated as provided in G.S. 105-130.10 and G.S. 105-130.10A.
- (9) Depreciation of emergency facilities acquired prior to January 1, 1955, if no amortization has been claimed on the

facilities for State income tax purposes.

- (10) The amount of losses realized on the sale or other disposition of assets not allowed under Section 1211(a) of the Internal Revenue Code. All losses recognized on the disposition of assets must be included in determining State net income or loss in the year of disposition.
- (11) The portion of undistributed capital gains of regulated investment companies included in federal taxable income and on which the federal tax paid by the regulated investment company is allowed as a credit or refund to the shareholder under Section 852 of the Internal Revenue Code.
- (12) The amount by which an ordinary and necessary business expense has been reduced on the federal income tax return because a tax credit was claimed in lieu of the deduction on that return if a similar State income tax credit is not allowed for the expense.
- (13) Reasonable expenses paid for reforestation and cultivation of commercially grown trees by a corporation owned entirely by natural persons actively engaged in the commercial growing of trees.
- (14) The amount of eligible income of an international banking facility to the extent included in determining federal taxable income.
- (15) The amount by which the tax basis of certain property is reduced as the result of compliance with federal investment tax credit provisions.
- (16) Marketing assessments paid on tobacco grown in N.C.
- (17) The amount of natural gas expansion surcharges collected by a natural gas local distribution company under G.S. 62-158.
- (18) Wireless enhanced 911 service charges collected under G.S. 62A-43 and remitted to the Wireless Fund under G.S. 62A-43.
- (19) Any interest, investment earnings, and gains of a trust established by two or more manufacturers that signed a settlement agreement with North Carolina to settle claims for damages attributable to a product of the manufacturers.
- (20) Amounts received from the Hurricane Floyd Reserve Fund in the Office of State Budget and Management.
- (21) The amount of royalty payment received from a related member who added the payments to income under G.S. 105-130.7A for the same taxable year.
- (22) The amount paid from the Disaster Relief Reserve Fund in the Office of State Budget and Management for hurricane relief or assistance. No deduction is allowed for payments for goods or services provided by the taxpayer.
- (23) The amount of a dividend received from a captive REIT, as defined by G.S. 105-130.12.
- (24) Five percent (5%) of the gross purchase price of a qualified sale of a manufactured home community.
- (25) The amount allowed as a deduction under G.S. 105-130.5B as a result of an add-back of special federal accelerated depreciation and section 179 expense.

Other Adjustments to Federal Taxable Income

The following other adjustments to federal taxable income must be made in determining State net income:

- (1) No deduction is allowed for annual amortization of bond premiums applicable to any bond acquired prior to January 1, 1963. The amount of premium paid on any such bond is deductible only in the year of sale or other disposition.
- (2) Federal taxable income must be increased or decreased to account for any difference in the amount of depreciation, amortization, or gains or losses applicable to property that has been depreciated or amortized by use of a different basis or rate for State income tax purposes than that used for federal purposes.
- (3) Federal taxable income must be increased or decreased to account for the recovery of previously deducted amounts that differ for State income tax purposes.
- (4) Interest on deposits with the FHLB of Atlanta
- (5) Deductions are generally not allowed for any direct or indirect expenses related to income not taxed.

To simplify the preparation and filing of its State income tax return, a corporation may attach a copy of its Federal income tax return and supporting schedules in lieu of completing the corresponding schedules in its State return.