

**November 14, 2011**

**Notice of correction and update to the July 11 issue of *Income Tax Update: News and developments for tax practitioners***

The July 2011 issue of *Income Tax Update: News and developments for tax practitioners* currently found on the Office of State Tax Commissioner's web site has been changed to correct an error and to update it because of legislation enacted by the Special Session of the North Dakota Legislature.

**Correction of Error**

**As originally published:** On page 7 of the newsletter originally released to the public, the article entitled "New tax credit for financial institutions that contribute to a qualified endowment fund" contained the following incorrect sentence:

"If the credit exceeds the tax liability, the unused portion may be carried over and used on subsequent years' returns for up to three tax years."

**Change to newsletter:** The incorrect sentence has been replaced with the following sentence:

"If the entire credit cannot be used in the tax year in which the contribution is made, the unused portion is not refundable and may not be used to offset any tax due for any other tax year."

**Legislative Update**

**As originally published:** On page 10 of the newsletter originally released to the public, there is an article entitled "SB 2210 – Housing incentive fund tax credit," which describes the provisions of Senate Bill 2210 enacted during the Regular Session of the 2011 North Dakota Legislature. That article contained the following three sentences:

**Sentence 1**—"No more than 20 percent of the credit attributable to each separate contribution to the fund may be used to offset the tax liability in any tax year."

**Sentence 2**—"The provisions providing for the 20 percent limitation, contribution addback to income, and carryover period apply to the passthrough entity's owners."

**Sentence 3**—"The total amount of tax credits allowed to all taxpayers under the program is \$4 million."

**Update:** The North Dakota Legislature, in Special Session commencing on November 7, 2011, enacted legislation (Senate Bill 2371) containing a number of disaster relief and oil and gas impact measures. Included among them were amendments to the housing incentive fund tax credit provisions in Senate Bill 2210 enacted during the Regular Session. The amendments removed the 20 percent limitation on the credit and increased the total credits allowed from \$4 million to \$15 million.

**Changes to newsletter:** With respect to the three sentences identified under "As originally published" above, Sentence 1 has been deleted from the article. Sentence 2 has been replaced with the following revised sentence:

"The provisions providing for the contribution addback to income and the 10-year carryover period apply to the passthrough entity's owners."

Lastly, Sentence 3 has been revised to replace "\$4 million" with "\$15 million."

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# Income Tax Update

News and developments for tax practitioners

A publication of the Tax Administration Division

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## 2011 legislative rundown

This newsletter provides a summary of the legislation passed by the 2011 North Dakota Legislative Assembly that affects North Dakota's income and financial institution tax laws. If a bill also contains

changes affecting areas of the law not related to income and financial institution taxes, this summary only covers the tax portions of the bill.

For the text of the bills and other legislative information, go to the 62nd North Dakota Legislative Assembly's web site at

[www.legis.nd.gov/assembly/62-2011/](http://www.legis.nd.gov/assembly/62-2011/)

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## HB 1047 - Income and financial institution tax rate reductions

### Individual, estate, and trust income tax rates

Starting with the 2011 tax year, the income tax rates for individuals, estates, and trusts are reduced by approximately 17.9 percent. The income brackets, as indexed for inflation for the 2011 tax year, were not changed. Following are the new tax rates and corresponding taxable income brackets for individuals, estates, and trusts for the 2011 tax year:

### LAST NEWSLETTER MAILING

This edition of *Income Tax Update* is the last paper edition to be mailed—see page 11.

2011 North Dakota Taxable Income

Bracket	Rate	Single		Married, Joint*		Head of Household	
		Over	Not Over	Over	Not Over	Over	Not Over
1	1.51%	\$ 0	\$ 34,500	\$ 0	\$ 57,700	\$ 0	\$ 46,250
2	2.82%	34,500	83,600	57,700	139,350	46,250	119,400
3	3.13%	83,600	174,400	139,350	212,300	119,400	193,350
4	3.63%	174,400	379,150	212,300	379,150	193,350	379,150
5	3.99%	379,150	-	379,150	-	379,150	-

\* Also applies to Qualifying Widow(er)

2011 North Dakota Taxable Income

Bracket	Rate	Married, Separate		Estate or Trust	
		Over	Not Over	Over	Not Over
1	1.51%	\$ 0	\$ 28,850	\$ 0	\$ 2,300
2	2.82%	28,850	69,675	2,300	5,450
3	3.13%	69,675	106,150	5,450	8,300
4	3.63%	106,150	189,575	8,300	11,350
5	3.99%	189,575	-	11,350	-



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*Estimated income taxes*—Individuals, estates, and trusts currently making payments of estimated North Dakota income tax for the 2011 tax year may adjust their remaining installments based on the lower tax rates. Each taxpayer is responsible for determining whether or not it is advisable to adjust the amount of their estimated payments. The 2011 Form ND-1ES for individuals and the 2011 Form 38-ES for estates and trusts have been revised to reflect the lower tax rates and are available on the Office of State Tax Commissioner’s web site at [www.nd.gov/tax](http://www.nd.gov/tax).

*Income tax withholding by employers*— The 2011 North Dakota income tax withholding tables have been revised to incorporate the reduced individual income tax rates. While use of the revised tables is optional for the remainder of calendar year 2011, employers are encouraged to incorporate them into their payroll systems as soon as they are able to do so. Employers do not need to make any adjustments to the North Dakota income tax withholding returns already filed or to employees’ paychecks already issued. Similarly, they do not need to adjust the withholding from future wages to account for any reduced withholding amounts relating to the paychecks already issued. If an employer incorporates the new tables for the remainder of 2011, the effect on employees’ paychecks and their total withholding for the year will depend on each employee’s situation.

### Corporation income tax rates

Starting with the 2011 tax year, the income tax rates for corporations are reduced by approximately 19.5 percent. The income brackets were not changed. Following are the new tax rates and corresponding taxable income brackets for corporations for the 2011 tax year:

Bracket	Rate	2011 North Dakota Taxable Income	
		Over	Not Over
1	1.68%	\$ 0	\$ 25,000
2	4.23%	25,000	50,000
3	5.15%	50,000	-

*Note for water’s edge filers:* If a corporation elects to use the water’s edge method to apportion its income to North Dakota, the corporation must pay a tax of 3.5% of its North Dakota taxable income in addition to the tax computed using the regular 3-bracket tax rate schedule shown above.

*Estimated income taxes*—Corporations making payments of estimated North Dakota income tax for the 2011 tax year may adjust their remaining estimated payment installments based on the lower tax rates. Each corporation is responsible for determining whether or not it is advisable to adjust their remaining estimated payments for 2011. *(The corporation income tax rates are not contained in the 2011 Form 40-ES, and therefore no changes were made to this form.)*

### Financial institution tax rate

Starting with the 2011 tax year, the income tax rate for financial institution tax purposes is reduced to 6.5 percent. In addition, the distribution of the tax was changed as follows:

- Three-thirteenths (3/13ths) of the tax must be paid by April 15th of the year immediately following the tax year. This amount is deposited into the state general fund.
- Ten-thirteenths (10/13ths) of the tax must be paid by January 15 of the year immediately following the year in which the financial institution tax return is due. This amount is deposited into the financial institution tax distribution fund, from which distributions are made to the counties according to a statutory formula.

### Tax study

House Bill 1047 also contained a provision requiring Legislative Management to consider the study of North Dakota’s corporation income tax laws, with special focus on the apportionment factors and potential impact of federal legislation, during the 2011-12 biennium. This study was given priority by Legislative Management and assigned to the Interim Taxation Committee. The findings and recommendations of the study must be reported to the 63rd Legislative Assembly (2013 session).

*Each taxpayer is responsible for determining whether or not it is advisable to adjust the amount of their estimated payments.*

**Statutory change:** Amended N.D.C.C. §§ 57-35.3-03, 57-35.3-05, 57-35.3-07, 57-35.3-08, 57-38-30, and 57-38-30.3(1).

**Effective date:** The tax rate reductions apply to taxable years beginning after December 31, 2010. 

## HB 1057 – Angel fund investment income tax credit

The law governing the income tax credit for making an investment in a North Dakota certified angel fund is significantly revised as follows:

- The tax credit is allowed to a partnership, S corporation, or other passthrough entity that makes a qualifying investment. The credit computed at the passthrough entity level is passed through to the entity's owners based on their respective ownership interests in the entity.
- The carryover period for an unused tax credit is extended from four to seven tax years.
- The angel fund certification conditions are revised as follows: (1) An angel fund's purpose must be to invest in at least three primary sector businesses that are early- or mid-stage private, nonpublicly traded entities with strong growth potential. (2) An "early-stage" entity is defined as having annual revenues up to \$2 million, and a "mid-stage" entity is defined as having annual revenues from \$2 million to \$10 million. (3) An early- or mid-stage entity may not include one deriving more than 25 percent of its revenues from income-producing real estate.
- Additional limitations and requirements are added as follows:
  - o Within thirty days after an investment is made in an angel fund, the angel fund must complete an investment reporting form and file it with the Office of State Tax Commissioner. A copy of the completed form must be provided to the investor. On the form, the angel fund must provide (1) the investor's name, address, and social security number or federal employer identification number, (2) the investment amount, and (3) the investment date. Except for the name, address, and social security number or federal employer identification number of the investor, the Office of State Tax Commissioner may disclose this information to Legislative Management.
  - o Within thirty days after the end of a calendar year, an angel fund must prepare and file with the Office of State Tax Commissioner a report showing the name and principal place of business of each business in which the angel fund invests its funds. The Office of State Tax Commissioner may disclose this information to Legislative Management.
  - o An angel fund may not invest its funds in a business if either of the following applies: (1) Any one investor in the angel fund directly or indirectly owns 50 percent or more of the business. (2) An investor in the angel fund is a passthrough entity and any one of its owners owns 50 percent or more of the business.
  - o A taxpayer is allowed no more than \$150,000 in credits over the taxpayer's lifetime. Married individuals are considered one taxpayer for this purpose. This limit applies to the sum of the credits earned for investments directly made by the taxpayer in an angel fund and any credits the taxpayer receives as an owner of a passthrough entity that invests in an angel fund. This limitation does not apply to any credits a taxpayer acquires from another taxpayer by purchase, assignment, or transfer—*see the next bulleted item.*
- For the 2011 and 2012 tax years only, a taxpayer may elect to sell, assign, or transfer tax credits to another taxpayer, subject to the following conditions:
  - o The election is irrevocable.
  - o The credit is based on an investment made in an angel fund that is first certified by the North Dakota Commerce Department on or after August 1, 2011. (*An investment must be made on or after the date of certification to be eligible for the credit.*)
  - o The credit is based on an investment the taxpayer makes directly to the angel fund. Credits received by a taxpayer as an owner of a passthrough entity that invests in an angel fund are not eligible for transfer.
  - o If the taxpayer is a passthrough entity, the taxpayer must transfer 100 percent of the allowable credit for the tax year and may transfer the credit to only one other taxpayer.
  - o A taxpayer may not transfer more than \$100,000 of credits over the taxpayer's lifetime.

**For the 2011 and 2012 tax years only, a taxpayer may elect to sell, assign, or transfer [angel] tax credits to another taxpayer**

...

*. . . joint filers who itemize deductions . . . may also benefit from this new state income tax deduction . . .*

- o If the transfer consists of a sale of the credit, the transferor must assign the gross proceeds received to North Dakota on the transferor's North Dakota income tax return.
- o The transferor and transferee must file a joint statement with the Office of State Tax Commissioner within thirty days after the transfer showing (1) their names, addresses, and social security numbers or federal employer identification numbers, (2) the amount of the transferred credit, and (3) the tax years in which the credit may be claimed. If the credit is sold, the joint statement also must show the gross proceeds from the sale of the credit, and a copy of the purchase agreement must be submitted with the joint statement. They also must give written authorization to the Office of State Tax Commissioner to disclose tax information to either party for the purpose of verifying the correctness of the transferred credit.
- o The transferee has only those rights to claim and use the credit that applied to the transferor.
- o The transferee may not transfer the credit.
- o The Office of State Tax Commissioner has four years after the date of the credit transfer to audit both parties' tax returns to verify the correctness of the credit. Any tax due resulting from a correction to the credit amount will be assessed to the transferee.
- o If the amount of the credit calculated by the transferor is changed as a result of an amended return or an audit, the transferor must inform the transferee about the adjusted credit amount within 30 days of filing the amended return or final audit determination. Subject to the time periods prescribed by law, the transferee must file an amended return for each affected tax year to pay any additional tax due or to claim a refund resulting from the changed credit. The Office of State Tax Commissioner may audit the original and amended returns of the transferee at any time, even though other time periods for assessment or refund have expired.
- The Office of State Tax Commissioner is required to provide a report to Legislative Management showing (1) the number of in-state and out-of-state investors, (2) the amount invested, and (3) the amount of credits earned, claimed, and transferred.

**Statutory change:** Amended N.D.C.C. § 57-38-01.26.

**Effective date:** Applies to taxable years beginning after December 31, 2010. The new transfer provisions apply for the first two tax years beginning after December 31, 2010, and are ineffective thereafter. 

## **HB 1072 – (Potential) new deduction for married persons filing jointly**

**Background**—Under federal tax law prior to 2001, the basic standard deduction amount for married persons filing jointly was 167% of the basic standard deduction amount for single persons (other than surviving spouses or heads of household). The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), as amended in 2003 and 2004, increased the basic standard deduction amount for married persons filing jointly to 200% of the amount of the basic standard deduction for single persons. This increase was intended to mitigate the so-called “marriage penalty” contained in the basic standard deduction. The changes made by EGTRRA were set to expire at the end of 2010, which would have resulted in the basic standard deduction for joint filers reverting back to the 167% level in 2011. However, the 2010 Tax Relief Act suspended the sunset clause for two additional years, maintaining the basic standard deduction for joint filers at the 200% level through the 2012 tax year.

**State tax law change**—House Bill 1072 provides that, if the federal basic standard deduction for married persons filing jointly should ever decrease to less than 200% of the federal basic standard deduction for single filers in any tax year, joint filers will be allowed a deduction equal to the amount of the decrease. Except for joint filers who elect to claim itemized deductions on their federal return even though the standard deduction is higher, joint filers who itemize deductions may also benefit from this new state income tax deduction to the extent their itemized deductions are less than 200% of the amount of the standard deduction for single filers.

**Note:** Due to the 2010 Tax Relief Act, and assuming no Congressional action to the contrary, this new state income tax deduction will not apply to the 2011 and 2012 tax years.

**Statutory change:** Added a new subdivision to subsection 2 of N.D.C.C. § 57-38-30.3.

**Effective date:** Applies to taxable years beginning after December 31, 2010. 

## HB 1102 – Renaissance zone program: Elective credit in lieu of business income exclusion

Under the Renaissance Zone Program, one of the tax incentives is a five-year business income exclusion for purchasing, rehabilitating, leasing, or making leasehold improvements to real estate used in a business. Under pre-2011 law, an eligible taxpayer could elect to take a \$2,000 income tax credit in each of the five years in lieu of the business income exclusion, but only if the election was made on the zone project application submitted to the local zone authority. This election provision has been changed to provide that the election is to be made on the taxpayer's timely filed original income tax return. An eligible taxpayer is an individual who spends at least \$75,000 to purchase or expand a business, or to make leasehold improvements to real estate used in a business, that is located in the renaissance zone of a city with a population no greater than 2,500 people. The individual must own or lease the qualifying real estate, and the transaction must be approved as a zone project by the city.

**Statutory change:** Amended N.D.C.C. § 40-63-04(3).

**Effective date:** Applies to zone projects approved after December 31, 2010. 

## HB 1124 – Technical changes to income and financial institution tax laws

This bill made numerous technical changes to the income and financial institution tax laws. The notable changes include the following:

- Under the provisions governing the planned gift and endowment income tax credits, if the contribution on which the credit is based was deducted in computing federal taxable income, the contribution must be added back to federal taxable income in computing North Dakota taxable income. This addback provision was revised to clarify that it applies to any tax year in which any part of the contribution was deducted from federal taxable income.
- Individuals are allowed to exclude 30 percent of net long-term capital gains and qualified dividends that are taxable by North Dakota. The provision providing for these exclusions was revised to clarify that there are two separate exclusions: one exclusion equals 30 percent of the excess of a North Dakota net long-term capital gain over a North Dakota net short-term capital loss, and the other exclusion equals 30 percent of qualified dividends taxable by North Dakota.
- The provisions governing the water's edge method of apportioning a corporation's income to North Dakota were revised to repeal the requirement to file a domestic disclosure spreadsheet.

**Statutory change:** Added new subsection to N.D.C.C. § 57-38-01.8, and amended N.D.C.C.

§§ 57-35.3-05(3), 57-35.3-07, 57-38-01.21(1), 57-38-01.21(6), 57-38-01.28, 57-38-01.31(1), 57-38-29.3, 57-38-30.3(2), 57-38-30.3(3), 57-38-59.2, 57-38.4-01, and 57-38.4-02(1).

**Effective date:** Applies to taxable years beginning after December 31, 2010. 

## SB 2006 – Income tax credit study

This is the Office of State Tax Commissioner's appropriation bill. A provision was added to it requiring Legislative Management to consider the study of North Dakota's income tax credits during the 2011-12 interim. This study was given priority by Legislative Management and assigned to the Interim Taxation Committee. With the assistance of the Office of State Tax Commissioner, the study must include an inventory of all income tax credits, a review of the nature of each credit and its targeted class of recipients, an analysis of possible barriers to each credit's use, an analysis of gaps and overlaps in the credit programs, the relationship of the credits to federal tax policy, and a review of each credit's effectiveness. The findings and recommendations must be reported to the 63rd Legislative Assembly (2013 session). 

*This addback . . . applies to any tax year in which any part of the contribution was deducted from federal taxable income.*

## SB 2034 – Green diesel fuel

Various provisions in North Dakota law governing biodiesel fuel programs were changed to add the language “green diesel.” The purposes of the change is to place green diesel fuel on an equal footing with biodiesel fuel for purposes of the programs. Under North Dakota income tax law, this change affected four income tax credit provisions: the tax credit for a fuel wholesaler for blending biodiesel fuel, the tax credit for a fuel retailer for adding or adapting equipment to sell biodiesel fuel, the tax credit for a corporation that builds or retrofits a facility to produce biodiesel fuel, and the tax credit for investing in an agricultural commodity processing facility.

**Statutory change:** Amended N.D.C.C. §§ 57-38-01.22, 57-38-01.23, 57-38-30.3(7), 57-38-30.6, and 57-38.6-01(2).

**Effective date:** August 1, 2011. 

## SB 2057 – Automation income tax credit

*The provisions of this bill do not take effect until the 2013 tax year, and they only apply to the 2013, 2014, and 2015 tax years.*

In the North Dakota Commerce Department’s appropriations bill, provisions were added to create a new income tax credit for purchasing new or used machinery and equipment for the purpose of automating a manufacturing process. Eligibility is limited to a primary sector business, which is a business certified by the Commerce Department as one using knowledge or labor to add value to a product, process, or service that results in the creation of new wealth in North Dakota. The credit is equal to 20 percent of the cost of the machinery and equipment approved by the Commerce Department. The credit must be claimed in the tax year in which the purchase occurs, and the excess, if any, of the credit over the tax liability may be carried over and used on subsequent years’ returns for up to five tax years. The total credits allowed for all qualifying purchases by all taxpayers is limited to \$2 million per calendar year. *(The Commerce Department will account for this annual limit on a first-come, first-serve basis according to the date of purchase. While the annual limit is measured on a calendar-year basis, the taxpayer will claim an allowable credit in the taxpayer’s tax year in which the purchase occurs.)*

In the case of a North Dakota corporation income tax return filed on a consolidated basis using the combined reporting method, a credit earned by any corporation included in the return may be offset against the combined tax liabilities of all corporations included in the return. If the taxpayer is a partnership or other passthrough entity, the credit is computed at the entity level and passed through to the entity’s owners based on their respective ownership interests in the entity. The amount of the approved purchases may not be used as the basis for any other deduction or credit allowed under North Dakota income tax law. The Commerce Department must provide a statement to the Office of State Tax Commissioner identifying the taxpayer and listing the machinery and equipment items approved for the credit. A taxpayer claiming the credit must be able to provide a statement showing the purchase date and the cost of each item of machinery and equipment approved for the credit.

**Statutory change:** Added a new section to N.D.C.C. ch. 57-38, and amended N.D.C.C. § 57-38-30.3.

**Effective date:** Applies to the first three taxable years beginning after December 31, 2012, and is ineffective thereafter. 

## SB 2160 – Qualified endowment fund tax credit

### **New income tax credit for individuals who contribute to a qualified endowment fund**

A new income tax credit is allowed to an individual who makes a charitable contribution of cash or property to a qualified endowment fund in North Dakota. The credit is equal to 40 percent of the qualifying contributions made during the tax year, up to a maximum credit of \$10,000 (\$20,000, if married filing jointly). A “qualified endowment ” means a permanent, irrevocable fund established for a specific charitable, religious, or educational purpose by a qualified nonprofit organization. A “qualified nonprofit organization” is a tax-exempt charitable organization under federal income tax law that has an established business presence or location in North Dakota. To qualify for the credit,

*The credit is equal to 20 percent of the cost of the machinery and equipment approved by the Commerce Department.*

the aggregate amount of contributions made to a qualified endowment fund must be at least \$5,000. The following examples illustrate the application of the \$5,000 minimum contribution requirement.

**Example 1**—A taxpayer makes one or more cash contributions totaling \$4,000 to Qualified Endowment Fund A. Because the aggregate amount of the contributions is not at least \$5,000, the contributions do not qualify for the credit.

**Example 2**—A taxpayer makes one or more cash contributions totaling \$4,000 to Qualified Endowment Fund A and one or more contributions totaling \$1,000 to Qualified Endowment Fund B. The contributions do not qualify for the credit because the aggregate amount contributed to either fund is not at least \$5,000.

**Example 3**—A taxpayer makes one or more cash contributions totaling \$5,000 to Qualified Endowment Fund A and one or more cash contributions totaling \$1,000 to Qualified Endowment Fund B. Only the \$5,000 contributed to Qualified Endowment Fund A qualifies for the credit. The \$1,000 contributed to Qualified Endowment Fund B does not qualify for the credit because it is not at least \$5,000.

**Example 4**—A taxpayer makes a cash contribution of \$500 at the beginning of each month to Qualified Endowment Fund A, for a total contribution of \$6,000 for the tax year. Although each monthly contribution is less than \$5,000, the tax credit is allowed on the entire \$6,000 because the aggregate amount of the contributions made during the tax year is at least \$5,000.

If the credit exceeds the individual's income tax liability, the unused portion may be carried over and used on subsequent years' returns for up to three tax years. North Dakota taxable income must be increased by the amount of the contribution upon which the credit is computed to the extent the contribution reduced federal taxable income. If a contribution is recovered by the individual, the credit allowed for the contribution must be added to the tax due on the return filed for the tax year in which the recovery occurs. A charitable contribution that is the basis for this credit may not be used as the basis for any other tax credit allowed for income tax purposes.

*Note: The provisions of this new credit were placed in the same section of law governing the individual income tax credit allowed for making a planned gift to a qualified nonprofit organization or a qualified endowment fund. However, this new credit differs from the planned gift credit in two ways: First, an individual does not have to make the contribution using a planned gift method to qualify for this new credit. Second, only contributions to qualified endowment funds are eligible to be considered for this new credit.*

#### **New tax credit for financial institutions that contribute to a qualified endowment fund**

A new tax credit is allowed to a bank or other entity subject to North Dakota's financial institution tax for making a charitable contribution to a qualified endowment fund in North Dakota. (*See the new income tax credit for individuals above for the definition of a qualified endowment fund.*) The tax credit is equal to 40 percent of the contributions made in a tax year, up to a maximum tax credit of \$10,000. The credit is allowed only against the state general fund portion of the financial institution tax. (*Starting with the 2011 tax year, the state general fund portion of the financial institution tax is equal to three-thirteenths of the total financial institution tax.*) If the entire credit cannot be used in the tax year in which the contribution is made, the unused portion is not refundable and may not be used to offset any tax due for any other tax year. North Dakota taxable income must be increased by the amount of the contribution upon which the credit is computed to the extent the contribution reduced federal taxable income. If a contribution is recovered by a financial institution, the tax credit allowed for the contribution must be added to the tax due on the return filed for the tax year in which the recovery occurs. A charitable contribution that is the basis for this credit may not be used as the basis for any other tax credit allowed for financial institution tax purposes.

**Statutory change:** Added a new subsection 4 to N.D.C.C. ch. 57-35.3-05, and amended N.D.C.C. §§ 57-35.3-07 and 57-38-01.21.

**Effective date:** Applies to taxable years beginning after December 31, 2010. 

*A new credit is allowed to a bank . . . for making a charitable contribution to a qualified endowment fund . . .*

## **SB 2170 – Income tax exemptions for certain nonresident individuals and their employers**

*The provisions of this bill do not take effect until the 2013 tax year.*

Starting with the 2013 tax year, this bill creates two new exemptions for North Dakota individual income tax purposes. One of the new exemptions applies to eligible nonresident individuals who work in North Dakota. The other exemption applies to eligible employers of nonresident individuals who work in North Dakota. The language of the bill is taken from a proposed model statute called the Model Mobile Workforce Statute developed by the Multistate Tax Commission (MTC), an organization of which North Dakota is a member. Work on the model statute was initiated by the MTC to craft an alternative to federal legislation introduced in recent sessions of Congress that would preempt states from taxing the income of nonresident individuals working within their borders on an occasional basis. The purpose of the federal legislation is to ease the state tax burdens for employers and their employees engaged in activity in multiple states. The model statute has recently been presented to the MTC's member states for their consideration of whether or not to enact legislation to adopt the model statute's provisions. North Dakota's adoption of the model statute in Senate Bill 2170 represents North Dakota's proactive effort to provide some relief to nonresident individuals and their employers and show that federal intervention is not necessary.

***Starting with the 2013 tax year, this bill creates two new exemptions for North Dakota individual income tax purposes.***

### **New exemption from income tax for certain nonresident individuals working in North Dakota**

Generally, compensation received by an individual for services performed in North Dakota is taxable by North Dakota even though the individual is not a legal resident of North Dakota. There are exceptions for U.S. armed forces servicemembers, certain interstate commerce employees, and Minnesota and Montana residents covered under the reciprocity agreements between North Dakota and those two states. Senate Bill 2170 adds a new exception to this group. Starting with the 2013 tax year, compensation received by an individual for services performed in North Dakota is excluded from North Dakota source income and therefore not subject to North Dakota income tax if all of the following conditions apply:

- The individual is not a legal resident of North Dakota for the tax year.
- The individual has no other income from sources in North Dakota for the tax year in which the compensation is received.
- The individual is present in North Dakota to perform employment duties for less than twenty-one days during the tax year.
- The individual's state of legal residence either (1) does not impose an income tax or (2) provides a substantially similar exclusion.

“Compensation” means wages as defined for federal income tax withholding purposes. In counting the number of the days present in North Dakota, presence in North Dakota for any part of a day constitutes presence for that day unless the presence is solely for purposes of transit through North Dakota.

The following individuals are not eligible for this new exemption:

- Professional athlete
- Member of a professional athletic team
- Professional entertainer
- Person of prominence performing services on a per event basis
- Person performing construction services that improve real property
- Person who is a key employee as defined under I.R.C. § 416(i) for the immediately preceding tax year (without regard to ownership or the existence of a benefit plan), or an employee of a noncorporate employer who would be a key employee if the term “officer” were replaced with the term “employee” and who is one of the fifty highest paid employees

The provisions of this new exemption do not affect the reciprocity agreements between North Dakota and the states of Minnesota and Montana, nor do they affect North Dakota's jurisdiction to impose any tax on any taxpayer.

Except where the Office of State Tax Commissioner requires the filing of an informational return, a nonresident individual whose compensation is eligible for exemption from North Dakota income tax under this new exemption is not required to file a North Dakota income tax return for the tax year.

### **New exception to income tax withholding from wages paid to certain nonresident individuals working in North Dakota**

Senate Bill 2170 also creates a new exception to an employer's requirement to withhold North Dakota income tax from compensation paid to an employee working in North Dakota. Starting with the 2013 tax year, an employer is not required to withhold North Dakota income tax from compensation paid to an employee working in North Dakota if all of the following conditions apply:

- The individual is not a legal resident of North Dakota for the tax year.
- The individual is present in North Dakota to perform employment duties for less than twenty-one days during the tax year.
- The individual's state of legal residence either (1) does not impose an income tax or (2) provides a substantially similar exclusion.

"Compensation" means wages as defined for federal income tax withholding purposes. In counting the number of the days present in North Dakota, presence in North Dakota for any part of a day constitutes presence for that day unless the presence is solely for purposes of transit through North Dakota.

Take note that this exception to the income tax withholding requirement for employers applies even if the employee has other types of income from North Dakota sources. So it is possible that a nonresident individual's compensation for services performed in North Dakota would be taxable by North Dakota but no North Dakota income tax would be withheld from it.

The provisions of this new exception to the income tax withholding requirement for employers does not affect North Dakota's jurisdiction to impose any tax on any taxpayer.

**Statutory change:** Added a new section to N.D.C.C. ch. 57-38 and amended N.D.C.C. § 57-38-59(1).  
**Effective date:** Applies to taxable years beginning after December 31, 2012. 

### **SB 2208 - Clarification of statutory Native American exemption**

Federal law generally prohibits states from taxing the income of a Native American who is an enrolled member of a federally-recognized Indian tribe, lives on the Indian reservation where enrolled, and derives his or her income from sources on the Indian reservation where enrolled. In 2007 the North Dakota Legislative Assembly added a provision to North Dakota income tax law that expanded upon this federal preemption by allowing the exemption to apply if the Native American lives on or derives income from sources on any Indian reservation located in North Dakota, not just the reservation where enrolled. In Senate Bill 2208, the 2011 North Dakota Legislative Assembly revised the North Dakota statute to clarify that, if an Indian reservation overlaps the border between North Dakota and its neighboring state, the state statutory exemption applies even if a Native American lives on or derives income from sources on the portion of the reservation located in the neighboring state. (Note: The Standing Rock and Lake Traverse Indian Reservations straddle the border between North Dakota and South Dakota.)

**Statutory change:** Amended N.D.C.C. § 57-38-30.3(2)(o).  
**Effective date:** Applies to taxable years beginning after December 31, 2010. 

... a nonresident individual whose compensation is eligible for ... this new exemption is not required to file a North Dakota income tax return ...

## SB 2210 – Housing incentive fund tax credit

*The provisions of this bill apply only to the 2011 and 2012 tax years.*

A new tax credit is allowed for income and financial institution tax purposes for contributing monies to a new housing incentive fund to be administered by the North Dakota Housing Finance Agency (Agency). The purpose of the fund is to provide assistance to public and private projects that address unmet housing needs in the state. The credit is equal to the amount contributed to the fund. Within thirty days of receiving a contribution from a taxpayer, the Agency must provide to the taxpayer a statement containing the taxpayer's name, address, and federal identification number, the amount of the contribution, and the date of the contribution. The Agency must provide a copy of the document to the Office of State Tax Commissioner. If part of the credit allowed in a tax year cannot be used because it exceeds the tax liability, the unused credit may be carried over and used on subsequent tax years' returns for up to ten years. North Dakota taxable income must be increased by the amount of the contribution upon which the credit is computed to the extent the contribution reduced federal taxable income. A contribution that is the basis for this credit may not be used as the basis for any other deduction or tax credit allowed for income or financial institution tax purposes. For financial institution tax purposes, the credit may only be used to offset the state general fund portion of the tax. For income tax purposes, if the taxpayer making the contribution is a partnership or other passthrough entity, the credit is passed through to the passthrough entity's owners in proportion to their respective ownership interests. The provisions providing for the contribution addback to income and the 10-year carryover period apply to the passthrough entity's owners. *(Starting with the 2011 tax year, the state general fund portion of the financial institution tax is equal to three-thirteenths of the total financial institution tax.)* The total amount of tax credits allowed to all taxpayers under the program is \$15 million.

**A new tax credit is allowed for . . . contributing monies to a new housing incentive fund to be administered by the North Dakota Housing Finance Agency . . .**

**Statutory change:** *Added a new subsection to N.D.C.C. § 57-35.3-05 and amended N.D.C.C. § 57-35.3-07, and added a new section to N.D.C.C. ch. 57-38.*

**Effective date:** *Applies to the first two taxable years beginning after December 31, 2010, and is ineffective thereafter.* 

## SB 2218 – Renaissance fund organization investment tax credit

Under the North Dakota Renaissance Zone Program, a city with an approved renaissance zone may set up a special fund called a renaissance fund organization (RFO). The purpose of an RFO is to raise funds to be used to provide financing to zone projects or to projects outside the zone but within the city. An RFO may not use more than 50 percent of its funds outside the zone. As an incentive to invest funds in the RFO, a tax credit equal to 50 percent of the investment is allowed. The provisions governing this tax credit were revised as follows:

- For new financing initiated after December 31, 2011, an RFO may no longer provide financing to projects outside of the zone, but must limit its financing activity to projects within a zone.
- The ceiling on the total tax credits allowed for investments in RFOs for all tax years was increased by \$1 million to \$8.5 million.
- For new financing initiated after December 31, 2011, an RFO may not provide financing to any project if an RFO's officers or employees individually or collectively own 50 percent or more of the project. This applies whether the ownership interest is held directly or is held indirectly through a partnership or other passthrough entity.

**Statutory change:** *Added a new subsection to N.D.C.C. § 40-63-07, and amended subsections 2 and 5 of N.D.C.C. § 40-63-07.*

**Effective date:** *The changes relating to the financing provided by an RFO applies to new financing initiated after December 31, 2011. The increase in the ceiling on total tax credit allowed takes effect August 1, 2011.* 

## Who to contact for assistance

To assist you in your tax preparation work, the following phone numbers and e-mail addresses are provided for your convenience. If calling from outside North Dakota, use area code 701.

Toll-free (in North Dakota) .....	1-877-328-7088
General (from Bismarck-Mandan area, or from outside North Dakota) .....	328-7088
E-mail .....	taxinfo@nd.gov
Tax form requests.....	328-1243
<i>Copy of previously filed return</i>	
<i>Blank tax forms and instructions</i>	
Taxpayer services.....	328-1242
<i>Correction notices and requests for information (except for C corporations)</i>	
<i>Income tax refund inquiries</i>	
Individual Income Tax Section .....	328-1247
E-mail .....	individualtax@nd.gov
<i>Individual, estate, or trust income tax questions</i>	
<i>Partnership and S corporation income tax questions (including withholding)</i>	
<i>Renaissance zone certificate of good standing requests</i>	
Income tax withholding (for employers) .....	328-1248
E-mail .....	withhold@nd.gov
Corporation Income Tax Section .....	328-1249
E-mail .....	corptax@nd.gov
<i>All corporation income tax matters (except for S corporations)</i>	
<i>Financial institution tax questions</i>	

Individuals needing help due to speech or hearing impairment may call Relay North Dakota at 1-800-366-6888, and then ask for one of the above numbers. 

## Discontinuance of paper newsletter mailings

This July 2011 edition of Income Tax Update is the last one that will be mailed in paper form. This publication is available on the Office of State Tax Commissioner's web site. An e-mail notification system is available for anyone interested in receiving notification of when a new issue of this publication is placed on the web site. To be added to the e-mail notification list, go to the web site at [www.nd.gov/tax](http://www.nd.gov/tax) and click on "Newsletters Subscription" located on the blue bar near the top of the home page. 



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