

MANUFACTURING

in Lehman's Terms

Incentives 101: New or Expanding Business Income Tax Exemption



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With summer set in, I hope everyone in the manufacturing community has had a chance to get out and enjoy the start to their summer. Last month's Lehman's Terms article kicked off North Dakota's tax incentive offerings with the property tax exemption for new and expanding businesses. This month I would like to continue down that road with another good incentive that manufacturing operations have at their disposal. We are seeing a lot of manufacturing operations looking at investing in North Dakota and this exemption is a perfect fit for those looking to do so.

The New or Expanding Income Tax Exemption allows a new or expanding primary sector or tourism business an exemption on their net taxable income pertaining to the new or expanding portion of their business for up to five years.

So, what constitutes a project? For a new operation, this is pretty clear-cut. It might involve new capital and workforce. For expansion of an existing operation, however, it may be less clear. Basically, there needs to be something added and the growth should be project based versus strictly low level steady organic growth. It may be capital required to produce more, or it could be additional workforce. Ultimately, the final decision as to whether or not it qualifies as an appropriate project comes down to the discretion of the board of equalization based on the business's submitted application.

A business is ineligible if:

1. If they have received an exemption under Tax Increment Financing (TIF).
2. There is an outstanding lien for delinquent property, income, sales or use taxes.
3. The exemption fosters unfair competition or endangers existing businesses.

The actual amount of the exemption for a new startup is straightforward in that it is an exemption on the business's net income. For an existing business expansion, however, it gets a little more difficult for the business to compute as there is a ratio determined which takes into account your base (pre-expansion level of property, payroll, and sales) compared to the respective post-expansion levels.

The easiest way to estimate your project's potential benefit would be to apply the following table to your incremental net taxable income to determine what your tax liability (potential exemption) would potentially be:

Incremental Net Taxable Income	Tax Liability
<\$25,000	0+1.41%
\$25,000-\$50,000	\$352+3.55%
>\$50,000	\$1,240 + \$4.31%

Although the above table won't give you the exact benefit on an expansion project, it should get you close. It should also be noted that there is a requirement to consider employment of North Dakota contractors and labor to the extent they are available and fully qualified for both the construction and operation phases. Failure to do so may result in revocation of the balance of the income tax exemption from the date of the breach of contract.

To apply for the income tax exemption:

1. Make sure you are a [primary sector certified](#) company through the North Dakota Department of Commerce. If you are unsure, you can contact me directly (contact information below).
2. [Apply](#) to the Corporate Income Tax Section, c/o the North Dakota State Tax Commissioner within one year preceding or following the start-up of the new/expanded operation.
3. Businesses must provide notice to competitors in the manner prescribed by the state board of equalization. This is typically done through a public notice ad.
4. State Board of Equalization hears any testimony at a public hearing and grants/denies the exemption. They will then notify the North Dakota Office of the State Tax Commissioner.

Please note that for a business that is a pass-through entity (LLC, partnership, or S corporation), the exemption is computed for the business, and then passed through to each owner. The deduction is then claimed on the owner's individual North Dakota return matching the deduction with where the income from the entity is reported and taxed.

That wraps up our brief overview of the income tax exemption. If you have an expansion projects on the horizon, please reach out to your local developer or myself, to ensure you are going through the proper steps as some of these programs need to be approved and in place prior to starting. For additional information regarding this or other incentives applicable to your manufacturing operation, please feel free to reach out and I will point you in the right direction. If you are considering an expansion or relocating to North Dakota, I would be happy to work with you to make that a reality!

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