



SC PRIVATE LETTER RULING #91-2

TO: ABC, Inc.

TAX ANALYST: Malane S. Pike

SUBJECT: Headquarters Credit/Property Tax Abatement  
(Income Tax and Property Tax)

REFERENCE: S.C. Code Ann. Section 12-7-1245 (Law. Coop. Supp. 1990)  
S.C. Code Ann. Section 12-37-220(B)(32) (Law Coop. Supp. 1990)

AUTHORITY: S.C. Code Ann. Section 12-3-170 (Law. Coop. 1976)  
SC Revenue Procedure #87-3

SCOPE: A Private Letter Ruling is a temporary document issued to a taxpayer, upon request, and it applies only to the specific facts or circumstances related in the request.

Private Letter Rulings have no precedential value and are not intended for general distribution.

FACTS:

"ABC," a wholly owned subsidiary of "XYZ," is located in South Carolina and provides services on a worldwide basis. ABC will build a regional headquarters at a location in South Carolina. ABC signed a 15-year lease on a 229,000 square-foot building to be constructed on a 22-acre site that will be named the XYZ Corporate Park. Under the terms of the lease, the direct lease cost for the first five years is expected to be:

Year 1	\$	
Year 2	\$	
Year 3-7.5	\$	(\$/year)
Year 7.5-15	\$	(\$/year)

The book expense (determined pursuant to Generally Accepted Accounting Principles) is expected to be \$ each year (\$ total lease expense divided by 15 years).

In addition to the lease costs, ABC has incurred approximately \$ in design and construction management costs. Approximately \$ of these costs have been performed by other subsidiaries of XYZ, with the balance performed by other firms. These costs represent 6% of the total cost of the new facility.

Approximately \$ of leased personal property is being or will be used in the new facility. The lease indicates that the lessee is ABC and XYZ. It provides that the place of installation is the ABC facility in South Carolina. The personal property is to be used by ABC and it is their responsibility to make all of these lease payments. Estimated moving and planning for the new facility will run between \$ and \$.

The new facility was occupied in the spring of 1990, and at least 150 jobs have been created. They expect to hire a total of over 500 employees in the next fiscal year; however the customary turnover in the business may result in a net increase which is less than 500. Not less than 40 of these jobs are filled by "staff employees" who occupy executive, administrative or professional positions for ABC and work in the new facility. Among these employees are engineers who are required to have a B.S. degree in engineering and at least an initial certification. The engineers make decisions for internal purposes involving moderate monetary amounts. They exercise judgment and initiative in the tasks assigned to them. Their work is diversified and requires skills of an advanced nature.

#### DISCUSSION:

The following questions and answers concern the income tax credit for corporate headquarters found in Section 12-7-1245 and the property tax abatement found in 12-37-220(B)(32). Section 12-7-1245 reads as follows:

A corporation establishing a corporate headquarters in this State, or adding to an existing corporate headquarters, is allowed a credit against any tax due pursuant to Section 12-7-230 or Section 12-19-70 of the 1976 Code in an amount equal to twenty percent of the (1) costs incurred in the design, preparation, and development of either establishing or expanding a corporate headquarters, and (2) direct construction or the direct lease costs during the first five years of operations for the corporate headquarters. This credit applies to all qualifying costs incurred to establish or expand a corporate headquarters which add at least seventy-five new jobs which are full-time in South Carolina with at least forty of the new jobs classified as staff employees, and the cost of the new construction or additions is fifty thousand dollars or more. This credit only applies to facilities established for the direct use of the headquarters staff employees. This credit is nonrefundable but an unused credit may be carried forward for ten taxable years for all qualifying corporate headquarters costs or fifteen years for all qualifying corporate headquarters costs in connection with which at least one hundred fifty new full-time jobs are created which (1) have an average cash compensation level more than one and one-half times the per capita income of the State at the time the jobs are filled, and (2) result in a total employee cash compensation per South Carolina employee of more than twice the per capita income of the State at the time the jobs are filled. In addition to the credits set forth above, qualifying headquarters meeting these per capita income criteria are further entitled to the credit in this section for personal property used for corporate headquarters related functions and services or research and development related functions and services.

For purposes of this section, the terms "corporate headquarters", "new jobs", and "full-time" are defined as provided in Section 12-37-220(B).

The amount of any credit allowed under this section must be reduced by the amount of any past-due debt owed to the State of South Carolina by the taxpayer.

Q1: Is the 20% income tax credit based on the actual lease payments or the actual book expense over the first five years?

A: Code Section 12-7-1245 states that a 20% income tax credit is available to corporations who establish a corporate headquarters in this state or add to an existing corporate headquarters. This credit is available for "direct lease costs" during the first five years of operations for the corporate headquarters. One of the primary rules of statutory construction is that words used in a statute should be taken in their ordinary and popular meaning, unless there is something in the statute which requires a different interpretation. *Hughes v. Edwards*, 265 S.C. 529, 220 S.E.2d 231 (1975); *Investors Premium Corp. v. South Carolina Tax Commission*, 260 S.C. 13, 193 S.E.2d 642 (1973). The term "direct lease costs" is not an accounting or tax term therefore, it should be given its ordinary meaning. As such, "direct lease cost" indicates the actual lease payments made by the corporation.

Q2: If personal property is leased for the facility, do these costs qualify for the income tax credit? If the parent's name (required by lessor) and ABC's name are listed on the lease, does this disqualify the lease payments for the credit?

A: Pursuant to Section 12-7-1245, personal property is entitled to the headquarters credit provided that the per capita income criteria are met and the personal property is used for corporate headquarters related functions or research and development related functions. The per capita income requirements state that 150 new full time jobs must be created which "(1) have an average cash compensation level more than one and one-half times the per capita income of the State at the time the jobs are filled, and (2) result in a total employee cash compensation per South Carolina employee of more than twice the per capita income of the State at the time the newly created jobs are filled". If these criteria are met, the actual lease cost of the personal property for the first five years qualifies for the credit provided that the personal property is used for headquarters related functions or research and development related functions and services.

This credit is not disallowed by virtue of the fact XYZ is listed as a lessee on the lease. The lease states that the lessees are ABC and XYZ. However, ABC is primarily liable on the lease and will make all lease payments. XYZ will only make payments if ABC is unable to make them. The equipment will be used by ABC at its headquarters in South Carolina.

Q3: Do design, construction, and planning management services performed by ABC or other subsidiaries of XYZ qualify for the income tax credit for corporate headquarters?

A: Section 12-7-1245 establishes a credit in the amount of twenty percent of the costs incurred in the design, preparation, and development of establishing a corporate

headquarters. The credit is for the costs of establishing a headquarters, not for the normal operating costs of the company. Management costs are a normal expenditure for ABC, irrespective of the establishment of a corporate headquarters. Although management personnel may be temporarily dedicated to the design, preparation, and development of the corporate headquarters, this does not represent additional cost to the corporation outside of what it would normally pay these individuals. Section 12-7-1245 provides a credit for the out of pocket cost of establishing a corporate headquarters in the State of South Carolina. Therefore, payments made for services performed by other corporations, including other subsidiaries of XYZ, qualify provided that such payments do not exceed the fair market value of the services. Payments for services provided by employees of ABC do not qualify.

Q4. Do the costs mentioned in Question 3 qualify if they were expensed instead of capitalized?

A: Code Section 12-7-1245 does not differentiate between capitalized or expensed costs. The costs indicated above may be expensed or capitalized for purposes of 12-7-1245.

It should be noted that this ruling expresses no opinion with respect to whether it is proper to expense any of these costs.

Q5: Do actual moving costs qualify for the income tax credit?

A: Pursuant to Section 12-7-1245, costs incurred in the design, preparation, and development of either establishing or expanding a corporate headquarters are eligible for the credit. The phrase "design, preparation, and development" relates to real property. In this regard, moving costs are not an expenditure to improve the real property for which a credit is allowed. Moving costs would also not qualify under the credit for personal property contained in Section 12-7-1245. The provision for personal property contemplates the purchase or lease of new personal property. This provision does not encompass the moving of furniture or other personal property to a new location.

Q6: How is the number of new jobs required by Section 12-7-1245 determined?

A: The Tax Commission will look to the number of full time, permanent jobs created at the time of the filing of Form PT-423, Certification of Eligibility New Jobs Credit and/or Five Year Property Tax Abatement for Corporate Headquarters, Corporate Office Facilities or Distribution Facilities. This form documents the 150 new jobs created, including the 40 staff positions. It requires the name, social security number, and the date hired for each full time employee hired pursuant to Section 12-37-220(B)(32). The company should identify the 40 staff employees in this list. Employees moved from an existing South Carolina location to work in the new or expanded facility do not count. Although employees may leave and be replaced, jobs must be full time, permanent positions. Jobs which are lost within the period of the credit may have the appearance of having been temporary positions. A decrease in

employment which was planned, expected or could reasonably be foreseen when the Form PT-423 is completed will reduce the number of new jobs created for the purposes of obtaining this credit. The company should be prepared to make employment records or other pertinent information available to the Tax Commission should any questions arise.

Q7: Are engineers, as determined in the facts, generally considered staff employees?

A: The term "staff employee" is defined in 12-37-220(B)(32) as follows:

... executive, administrative, or professional worker. At least eighty percent of an executive employee's business functions must involve the management of the enterprise and directing the work of at least two employees. An executive employee has the authority to hire and fire or has the authority to make recommendations related to hiring, firing, advancement, and promotion decisions, and an executive employee must customarily exercise discretionary powers. An administrative employee is an employee who is not involved in manual work and whose work is directly related to management policies or general business operations. An administrative employee must customarily exercise discretion and independent judgment. A professional employee is an employee whose primary duty is work requiring knowledge of an advanced type in a field of science or learning. This knowledge is characterized by a prolonged course of specialized study. The work must be original and creative in nature, and the work cannot be standardized over a specific period of time. The work must require consistent exercise of discretion.

Information provided by the company indicates that engineers are required to have a Bachelor of Science degree in engineering and at least an initial certification. They make decisions involving moderate monetary amounts. They are accountable for functions that exercise direct influence on project results. Engineers exercise judgment and initiative within certain guidelines. In addition, they are instrumental in determining the sequence of jobs where a choice of methods is available. Only questionable cases are referred to a supervisor. Thus, engineers meet the statutory requirements for a professional position in that they in that they are required to have knowledge of an advanced type and must exercise discretion in their job. Engineers qualifying for the headquarters credit must be placed in the headquarters complex.

Q8: Is the property tax exemption from county ad valorem taxes available to ABC since they lease the facility?

A: A five year property tax exemption is provided in Section 12-37-220(B)(32) and reads as follows:

All new corporate headquarters, corporate office facilities, distribution facilities, and all additions to existing corporate headquarters, corporate office facilities, or distribution facilities located in South Carolina, established or constructed, or placed in service, after June 27, 1988, are exempt from nonschool county ad valorem taxes

for a period of five years from the time of establishment, construction, or being placed in service if the cost of the new construction or additions is fifty thousand dollars or more and seventy-five or more new jobs which are full-time are created in South Carolina.

In general, owners of property are responsible for property taxes. Although the owner may contract with another party to pay the property taxes, for example by lease, the owner is liable for the property taxes. In applying this principle to the exemption in Section 12-37-220(B)(32), it has been the long standing administrative practice of the Tax Commission to strictly construe tax exemption statutes. "As a general rule, tax exemption statutes are strictly construed against the taxpayer." *Owner Industrial Products, Inc. v. Sharpe*, 274 S.C. 193, 262 S.E. 2d 33 (1980); *Hollingsworth on Wheels, Inc. v. Greenville County Treasurer et. al.*, 276 S.C. 314, 278 S.E. 2d 340 (1981). "This rule of strict construction simply means that constitutional and statutory language will not be strained or liberally construed in the taxpayer's favor." *York County Fair Association v. S. C. Tax Commission*, 249 S.C. 337, 154 S.E. 2d 361 (1967).

Thus, the exemption is only granted to the persons responsible for the property taxes even though they may have contractual arrangements to have another pay them. However, it should be noted that the lessor of the property may apply for the exemption based on the use of the property as a headquarters.

SOUTH CAROLINA TAX COMMISSION

s/S. Hunter Howard Jr.  
S. Hunter Howard, Jr., Chairman

s/A. Crawford Clarkson, Jr.  
A. Crawford Clarkson, Jr., Commissioner

s/T. R. McConnell  
T. R. McConnell, Commissioner

Columbia, South Carolina  
April 26 , 1991