



SC PRIVATE LETTER RULING #91-3

TO: ABC

TAX ANALYST: Malane S. Pike

SUBJECT: Headquarters Credit for Personal Property
(Income Tax)

REFERENCE: S.C. Code Ann. Section 12-7-1245 (Law. Coop. Supp. 1990)
S.C. Code Ann. Section 12-7-1220 (Law. Coop. Supp. 1990)
S.C. Code Ann. Section 12-37-220 (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.

QUESTION:

Is ABC entitled to the Corporate Income Tax Credit under S. C. Code Ann. Section 12-7-1245 for their investment in personal property in connection with the corporation's expansion of its Corporate Headquarters Complex?

FACTS:

ABC, a South Carolina corporation, employs approximately 4000 individuals in 47 states and 7 countries. About 1700 of the corporation's employees are located at its existing corporate headquarters in South Carolina.

The corporation's mission is to develop and provide software for the insurance industry, and its principal product lines include software packages for property and casualty, life, health, and group insurance companies.

The corporation has acquired land on which it is constructing an addition (the "Expansion") to its Headquarters. The personal property purchased or to be purchased as part of the Expansion include furniture, fixtures, equipment, computer equipment (to be located in the Expansion building) and a mainframe computer and peripheral equipment (to be located in the data center portion of the existing headquarters complex). The expenditures relating to the Expansion were made primarily in 1990, but Expansion expenditures have also been made during 1989 and will be made during 1991. The current cost estimates for real and personal property purchased or to be purchased as part of the Expansion are as follows:

\$9.3 to \$9.5 Million	Real Property (not including the land which the Corporation already owned)
\$4.0 to \$5.0 Million	Furniture, Fixtures and Equipment
\$4.0 to \$5.0 Million	Computer Equipment (to be located inside the Expansion building)
\$6.4 to \$7.5 Million	Mainframe Computer and supporting peripheral equipment (to be located in the data center portion of the Headquarters Complex)
\$23.7 to \$27.0 Million	TOTAL

In connection with the Expansion, at least 150 new full-time jobs have been or will 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.

With respect to the expansion, the employees will perform duties concerning financial, investment, legal, audit, administrative, planning, business development and international, national and regional sales and marketing matters. Employees at the Expansion will also include management personnel who will manage employees at branch offices and elsewhere and direct sales representatives.

Employees at the Expansion will also include the following employees directly involved with new products:

1. Product/Project Manager
Product and project managers are senior level individuals responsible for identifying new product requirements in the marketplace and developing the product or project plan for a new product. They are also involved in identifying and staffing a project team and coordinating the research and product development activities necessary to take the project plan from conception to reality.
2. Systems Architect
Systems Architects are highly qualified technical resource individuals who solve complex system design and development problems. Their responsibilities also include the evaluation and analysis of current and future system trends. Systems architects also design and direct the overall new systems development specifications that, in turn, determine the systems design and programming specifications that are developed by product analysts or systems analysts.

3. Product/Insurance Analysts
Product and Insurance Analysts are individuals who provide assistance in complex situations requiring interaction between the business user and the technical programmers. These individuals develop the business requirements and the programming specifications that are the basis for new product development directions.
4. Systems/Programmer Analysts
Systems and Programmer Analysts are professionals who provide technical guidance and assistance in the product development process. They are responsible for formulating systems plans that provide technical data regarding the environment in which a particular development project is expected to perform. They also provide detailed specifications from which programs are written.
5. Programmers
Programmers are individuals who interpret the detailed instructions provided by systems architects, product analysts and systems analysts. Their primary tasks are to code, test and document the new programs and/or procedures that they are developing.

There may be a few corporation employees located in the Expansion with the same or similar job titles who instead provide functions or services such as custom programming for specific client needs, systems installations, or working in customer assistance centers. No credit is requested for the personal property used primarily by these employees.

ABC performs extensive experimental testing and development in connection with its offering of improved and new products. Each major functional component of a system is tested in order to prove that a system can perform functions needed by the industry.

Generally, all of the Expansion-related personal property will be located in the Expansion building. However, because of the special requirements and needs relating to modern mainframe computers and peripherals, the corporation has located, and intends in the future to locate, its mainframe computers in one special building which is a part of the existing Headquarters Complex and which was constructed solely for the purpose of housing these computers. Therefore, the corporation can provide these computers with the climate control, primary and backup power, security and other needs particular to such modern mainframe computers. The corporation will be purchasing the equivalent of at least one new mainframe computer (through the purchase of an additional mainframe computer or upgrades to existing mainframe computers) in order to provide the additional capacity required as a result of the Expansion.

Similarly, the corporation has located, and intends in the future to locate, all of its telephone switching computers and related equipment in a single location within the existing Headquarters Complex. In order to service the increased demands resulting from the Expansion, the corporation is increasing the processing and memory capacity of its Central Switching System. This cost is included in the estimated cost of Expansion furniture, fixtures and equipment.

DISCUSSION:

Section 12-7-1245 of the South Carolina Code provides a credit for qualifying corporate headquarters equal to 20% "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". Personal property "used for corporate headquarters related functions and services" or "research and development related functions and services" is also entitled to the headquarters credit provided that the per capita income requirements of this statute are met. Pursuant to the per capita income requirements, at least one hundred fifty 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.

This document will define "corporate headquarters related functions and services" and "research and development related functions and services". It will then determine if ABC's personal property fits within these definitions. ABC has stipulated that the per capita income requirements are met, therefore, that issue will not be addressed. Finally, the time period for obtaining the headquarters credit will be discussed.

Definition of "Corporate Headquarters Related Functions and Services"

Section 12-7-1245 defines the term "corporate headquarters related functions and services" by reference to Section 12-37-220(B)(32). This section provides a definition of "corporate headquarters" which outlines the activities which are considered to be headquarters related. This provision reads as follows:

"corporate headquarters" means the location where corporate staff members or employees are domiciled and employed, and where the majority of the company's financial, personnel, legal, planning, or other business functions are handled either on a regional or national basis and must be the sole such corporate headquarters within the region or nation.

Thus, employees physically located in the headquarters and performing these functions would qualify for the credit provided that the per capita income requirements are met.

Definition of "Research and Development Related Functions and Services"

Section 12-7-1245 does not provide a definition for "research and development related functions and services". For purposes of determining whether personal property qualifies for the credit, it is necessary to define this term. As seen with the definition of "headquarters related functions and services", Section 12-7-1245 refers directly to the property tax statute, Section 12-37-220.

Therefore, it is reasonable to construe these two statutes together. In addition, Section 12-7-1220, the jobs credit, provides a definition of "research and development". Both the headquarters credit and the jobs credit are designed to attract new business into South Carolina. Corporations availing themselves of the headquarters credit are often eligible for the jobs tax credit as well.

Therefore, it is reasonable to construe "research and development" as used in Section 12-7-1245 to be consistent with "research and development" as used in the jobs tax credit.

Section 12-37-220, a property tax exemption provision, contains a definition of a related term "facilities of enterprises engaged in research and development activities". This definition reads as follows:

For purposes of this section, facilities of enterprises engaged in a research and development activities are facilities devoted directly and exclusively to research and development in the experimental or laboratory sense for new products, new uses for existing products, or for improving existing products. To be eligible for the exemption allowed by this section, the facility must be a separate facility devoted exclusively to research and development as defined in this section. The exemption does not include facilities used in connection with efficiency surveys, management studies, consumer surveys, economic surveys, advertising, promotion, or research in connection with literary, historical, or similar projects.

Section 12-7-1220, an income tax credit provision for the creation of new jobs, contains a similar definition of the related term, "research and development facility". This definition reads as follows:

"Research and development facility" means an establishment engaged in laboratory, scientific, or experimental testing and development related to new products, new uses for existing products, or improving existing products, but a "research and development facility" does not include an establishment engaged in efficiency surveys, management studies, consumer surveys, economic surveys, advertising, promotion, or research in connection with literary, historical, or similar projects.

The definitions contained in 12-7-1220 and 12-37-220 are substantially similar. Given the legislative intent of these statutes and the direct reference from 12-7-1245 to 12-37-220, it is reasonable to construe "research and development" for use in 12-7-1245 to be consistent with these statutes.

Is ABC's Personal Property Being Used for Corporate Headquarters Related Functions and/or Research and Development Related Functions as Required by Section 12-7-1245?

Pursuant to the facts provided by ABC, a significant portion of the personnel to be located in the Expansion will perform services such as financial, investment, legal, audit, administrative, planning, business development, and international, national and regional sales and marketing management and support. The management staff located in the Expansion will be responsible for managing employees in the branch offices and elsewhere.

Based upon the definition given in Section 12-37-220(B)(32), the cost of purchasing personal property for use by ABC employees performing these functions qualifies for the credit.

With regard to research and development related activities, ABC develops new products and improves existing products in order to remain competitive in the insurance software business. Although the corporation does not have a research and development division as such, research and development functions and personnel are spread throughout the corporation on a product line basis.

Each product line has certain positions dedicated to the development of new software. Some of the job titles utilized to perform these functions are Product or Project Manager, Systems Architect, Product or Insurance Analyst, Systems or Programmer Analyst, and Programmer. Descriptions of these jobs are included in the facts submitted by ABC. Although these same job titles may be used in reference to personnel not performing research and development duties, the credit is only being requested for the personal property of those who are. ABC conducts extensive experimental testing to ensure that a system can perform functions needed by the industry.

Pursuant to the definitions in Sections 12-37-220 and 12-7-1220 and information provided by ABC, the corporation is performing research and development. Its personal property, used by employees performing these functions, therefore qualifies for the credit provided the per capita income requirements of Section 12-7-1245 are met. The personal property of those employees dedicated to marketing custom programming for specific client needs, systems installations, working in customer assistance centers or performing other functions does not qualify for the credit.

Necessary enhancements to the mainframe computer and the telephone system to serve the headquarters expansion is also personal property which qualifies for the credit in Section 12-7-1245. They are predominately used for corporate headquarters functions and research and development. The credit is allowed because the equipment is housed in the corporate headquarters complex.

Time Period for Obtaining the Credit

The corporation is entitled to the headquarters credit in the tax year in which the facility is placed in service. Qualifying headquarters expenses which have been incurred through the date on which the corporate return for that year is due, including extensions, are eligible for the credit. For the purposes of this credit, an expense is incurred if it is accrued under the accrual method of accounting for income tax purposes, without regard to subsection 461(h) of the Internal Revenue Code. Only the expenses which are part of the original headquarters expansion plan are eligible for the credit.

CONCLUSION:

ABC is entitled to the Corporate Income Tax Credit under S. C. Code Ann. Section 12-7-1245 for their investment in personal property devoted to headquarters related functions and services and research and development related functions and services, as defined in this document, for their corporate headquarters complex expansion. The personal property for employees not performing these functions is not eligible for the credit.

The corporation must claim the credit for the tax year in which the facility is placed in service. All expenses which otherwise qualify for the credit and which are incurred through the date on which the corporate return is due, including extensions, are eligible for the credit. For the purposes of this credit, an expense is incurred if it is accrued under the accrual method of accounting for income tax purposes, without regard to subsection 461(h) of the Internal Revenue Code.

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
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