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digest the N.C. General Assembly's recent tax policy overhaul.

Aug. 26, 2013

Like many Charlotte-area small business owners, Doug Jones doesn't know how to digest the N.C. General Assembly's recent tax policy overhaul.

Even before he and his wife, Sophie, opened Pour Olive, a specialty oil and vinegar shop on East Boulevard, he believed the state's tax code needed revisions that would make the state more attractive to corporations.

But he worries one of the legislature's many policy changes — eliminating a \$50,000 tax deduction that small business owners can take on their personal income tax returns — could negatively impact some small businesses.

The deduction, approved by the legislature just two years ago, amounted to an annual savings of \$3,000 to \$4,000, according to the N.C. Association of Certified Public Accountants.

It was even greater in the case of some married couples who co-owned a business and could deduct up to \$100,000 on their personal income tax returns.

And though business at Pour Olive has been bustling, Jones says entrepreneurs like them know “everything counts, especially in the first few years.”

Jones' concerns are typical of many Charlotte-area small business owners who like the business-friendly philosophy of the changes but don't like losing the economic incentive of a deduction.

And while it probably won't drive any of them out of business, “it stinks” for a small business owner to lose several thousand dollars a year, says Deborah Millhouse,

owner of Charlotte-based recruitment agency CEO Inc., which has nearly 20

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State Sen. Bob Rucho cites cutting red tape and the legislature's reducing the state's progressive personal income tax to a flat 5.8 percent.

"We've been working diligently to help small businesses function more efficiently," Rucho says.

Experts say the tax policy is too complex to make blanket statements about whether the changes are, on the whole, good or bad for small business.

And because the new policies touch everything from deductions for mortgage interest to child tax credits, the changes touch all business owners differently.

For example, someone with a net business income of \$100,000 will pay more than \$2,400 more with the deduction eliminated.

But some small businesses with a higher net business income will benefit from the lower personal income tax rates, in spite of the lost deduction.

For example, a small business owner whose net business income was \$250,000, will save more than \$3,800 with the new rates.

"There are going to be winners and losers," said Jack Schmoll, a member of the North Carolina Association of CPAs, who has worked exclusively with state and local taxation for two decades.

Jonathan McGiverin, a career entrepreneur and self-employed consultant who recently moved to North Carolina from Pennsylvania, said he decided to build a home — and home office — in Pineville rather than Fort Mill, S.C., because of the \$50,000 deduction.

He calculated that the higher property taxes in North Carolina would be offset by the

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owners. It's not something to be taken lightly.

In Charlotte and other parts of the U.S., small businesses are an economic generator. In 2011 in Mecklenburg County, 26,706 employers, or 97 percent of all employers, had fewer than 100 workers.

### Small deduction, big debate

The deduction was hotly debated even when it was introduced by Republicans during the 2011 legislative session, underscoring how even a relatively small deduction for small businesses can become politically contentious.

The \$50,000 deduction was designed to stimulate “small businesses — the backbone of North Carolina’s struggling economy,” House Speaker Thom Tillis and Senate President Pro Tem Phil Berger said at the time.

But while the tax break — which UNC Chapel Hill estimated to be a loss of \$336 million a year — was designed to create jobs, it came the same year as 6,400 school employees lost their jobs to help balance the \$20 billion state budget.

And though the Senate initially capped income eligibility for the tax break, legislators later dropped it, making the deduction apply to roughly 460,000 business owners, including sole proprietors and active shareholders of S corporations, partnerships and limited liability companies. Corporations that issued stock and paid dividends were excluded.

Democrats and government advocates said the tax break was helping rich small business owners — such as equity partners at law firms.

“We got so chewed up and spit out about that,” says State Rep. Ruth Samuelson, a Charlotte Republican.

And now debate rages over taking it away. That's largely because it coincides with a

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South Carolina came in at No. 36, Virginia at No. 26 and Tennessee at No. 14.

But state Rep. Tricia Cotham, a Democrat, who owns the south Charlotte day care Kids Klub and voted against the tax overhaul, says it's simply shifting much of the tax burden away from large corporations and onto small businesses.

"While I understand the desire to make North Carolina more attractive to large multistate corporations, we cannot ignore the important role that small businesses play in our economy," Cotham said in an email.

'They have resilience'

State taxes and the loss of this \$50,000 deduction are far from the biggest problems entrepreneurs face, Millhouse of CEO Inc. says. However, every expense adds up. She says in all, taxes take "well over 50 percent" of her business income every year.

Couple that climate with the ongoing questions of how the federal health care law changes will impact the bottom line, and it would take a lot of determination to want to start a small business these days.

But, Millhouse adds, that's exactly what small business owners like herself are known for.

"You can be in a bad mood, but ... then you have to buck up and figure out how you're going to make up for it," Millhouse said. "And that's what makes small business owners amazing. They have resilience."

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