



NC “DATACENTER”/“DATA CENTER” INCENTIVES:

A CASE STUDY IN NORTH CAROLINA (AND MULTI-JURISDICTIONAL) ECONOMIC DEVELOPMENT

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Brief Geek Intro: What are Datacenters? Why are They Important to *Business*?

Basic Definition:

- ❖ A technology facility housing computer systems, such as telecom/storage/retrieval systems
- ❖ [Note: very specific/varying definitions apply for NC tax and incentives purposes]

Basic Uses:

- ❖ Data protection; data recovery
- ❖ Computing power; processing speed; information access/retrieval
 - ✓ Streaming of multimedia data
 - ✓ “Cloud” computing (basically, remotely hosted, stored, and utilized software/data)

Basic Variations:

- ❖ Captive/affiliated (enterprise) datacenter vs. public service/access datacenter
- ❖ Industries served/type of data/retail vs. wholesale
- ❖ Four different industrial “tiers” (classes)
- ❖ Each datacenter industrial “tier” has varying:
 - ✓ Data retrieval/availability metrics
 - ✓ Redundancy of data distribution paths and capacity
 - ✓ Power and cooling characteristics

-Sources: Uptime Institute/TIA-942 Data Center Standards

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State Development Perspective: Why Do Many States Compete for Datacenters? (Part 1)

21st Century Economy:

- ❖ Many information systems companies are among the largest and the most profitable/stable
- ❖ These projects foster/require the latest in computing infrastructure
- ❖ Expansion into new economy; “wave of the future”; “cutting edge”
- ❖ Traditionally “green” projects

Most Datacenter Projects are Very Capital Intensive:

- ❖ Multiple hundreds of millions of dollars
- ❖ Equipment obsolescence means frequent equipment purchases
- ❖ Construction contractor-intensive and other area “multiplier” effects

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State Development Perspective: Why Do Many States Compete for Datacenters? (Part 2)

EXAMPLE: Department of Commerce Announcement for Apple Datacenter (6/3/09):

“A data center such as this will typically **contract locally** for services such as server maintenance and repair, building and HVAC maintenance, landscaping and security – **expenditures that could range from \$5 million to \$6 million annually in the region and create up to 250 jobs**. The North Carolina Department of Commerce projects that **a data center investment of \$1 billion would create more than 3,000 jobs in the regional economy**, including hundreds of jobs related to construction and others created as a result of economic growth.

‘We are very pleased the General Assembly has recognized the role capital-intensive industries play in the state’s economy and their relationship to small businesses in our communities. **Technology-driven projects like this may bring fewer overall jobs than traditional industry, but they have a tremendous economic impact through locally purchased goods and services,**’ Commerce Secretary Keith Crisco said.”

Datacenters Can’t Just Open Up “Just Any Old Place” - Few Sites are Chosen:

- ❖ **Most large datacenters are supra-regional if not national**
- ❖ **Need good power, data transfer, and water infrastructure (collateral public benefit)**
- ❖ **Virtually all citizens/businesses directly utilize/benefit from public access datacenters**
- ❖ **Education and services linkage**

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Datacenter Industry Perspective: What Has NC Got to Offer?

Generally:

- ❖ A good infrastructure base as a starting point – importantly, even in “less developed” areas
- ❖ An educated, technically proficient workforce
- ❖ Relatively reasonable land costs
- ❖ Relatively reasonable utilities costs
- ❖ Relatively stable weather and low incidence of natural disasters (esp. earthquake and tornado)

Also, “We’re not CA or NY” (???)***

“It is amazing to me that some high-tax, high-regulation states such as California and New York are trying to push business and entrepreneurs out of their states, while . . . so many pro-business . . . states are going to great lengths to make business formation easier, cheaper, and more competitive in this global economy.”

-Nolan Bushnell, Inc. magazine online (10/25/10)

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NC is not CA or NY [but. . .]

But many *other* states also have these favorable characteristics:

- ❖ Supra-regional/national datacenters don't come to NC just to "be in NC"
- ❖ Most *other* states are "not CA or NY" either

Heard on the Street: Pro and Con

- ❖ Pro: Site Selection magazine ranked NC the "*Top Business Climate*" for the 6th year in a row
- ❖ Con: Tax Foundation's annual "State Business Tax Climate Index" ranks NC as 41st (10th from worst) in the nation for 2011. [CA and NY are 49th and 50th]
- ❖ Universe of other tax and incentives reports are also mixed

High/highest tax rates in Southeast/well above average for the country:

- ❖ Corporate income tax (and administrative discretionary combined reporting)
- ❖ Sales tax (and tricky procurement rules)
- ❖ Personal income tax
- ❖ Franchise tax (often a *de facto* property tax)

Reputation for aggressive tax enforcement and technical and administrative tax "traps for the unwary"

-"Best and Worst of State Tax Administration" (COST ScoreCard)

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But This *is* a NC Success Story

A Few Examples:

- ❖ American Express (NY HQ)
- ❖ Apple (CA HQ)
- ❖ Facebook (CA HQ)
- ❖ Fidelity Investments (MA HQ)
- ❖ Google (CA HQ)
- ❖ IBM (NY HQ)
- ❖ National Climatic Data Center
- ❖ U.S. Social Security Administration
- ❖ Wipro Technologies
- ❖ Various telecom companies
- ❖ Several other projects in the works

Generally Available Tax Incentives? Income/Franchise/Property:

- ❖ Article 3J state income/franchise tax credits: jobs, investment, etc.
- ❖ State JDIG and/or ONE NC Fund grants
- ❖ Local property tax grants, etc.
 - ✓ Project location affects incentive amounts, but generally less so in NC than in neighboring states

But Many Other States have *at Least Somewhat* Comparable Incentives. . . .



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So How has NC Differentiated Itself from Other Non-CA, Non-NY States?

1) Excellent Recruiting – by DOC, Utility, and Construction Firms

2) A Variety of Targeted State and Local Tax Incentives (“Direct Marketing”):

❖ Income Tax Apportionment Incentive for Low-Development Tier, \$1BB Projects

- ✓ (Mandatory?) single sales factor apportionment for “qualified capital intensive corporation”
- ✓ Taking this incentive forfeits the *State* general incentives listed in first bullet point at top
- ✓ Employment, wage, and health insurance standards apply
- ✓ Value for datacenters dealing in intangibles?? Depends
 - Whether this incentive is advantageous to a taxpayer is *very* fact-dependent

❖ Three Main Possible Sales/Privilege Tax Incentives

- ✓ Full exemption for “eligible Internet data center” property/electricity
- ✓ *Virtually* full exemption (1%/\$80 per article cap) on “eligible datacenter” property, but not electricity
- ✓ Full exemption on software, however delivered, purchased by datacenter operator for use in datacenter

❖ But there are *many* traps for the unwary (different rules for different prior periods):

- ✓ Is the project a statutory “datacenter” (8/7/09 definition)?
- ✓ Is it an “*eligible* datacenter”?
- ✓ Is it an “eligible *Internet* data center”?
- ✓ Did the datacenter get advance Department of Commerce certification?

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Full vs. “Virtually Full” Exemptions (CURRENT Law) - Part 1

Full exemption for “eligible Internet data center” property/electricity

❖ Eligibility:

✓ Only “eligible Internet data centers” - ISPs and Web search portals

• **Watch those NAICS Codes! (7/1/10: “NAICS” changed from 2002 to 2007)**

• Prior to 7/1/10, NAICS 51811 (broadly, ISPS and Web Search Portals)

• After 7/1/10, NAICS 511210 and 519130 (software publishing, Internet activities)

✓ No Tier 3 (most developed) county projects

✓ Dept. of Commerce-certified investment of ≥\$250MM in real/personal property within five years

❖ Exemption scope - capital assets or electricity used/located at project for:

✓ Used in “datacenter user’s” “primary business” (pre-7/1/10, had to be used in performing ISP /Web search portal services)

✓ Computer engineering or computer science research

✓ Managing/powering any of the foregoing equipment

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Full vs. “Virtually Full” Exemptions (CURRENT Law) - Part 2

Virtually full exemption (1%/ \$80 per article cap) on “eligible datacenter” property

❖ Eligibility:

- ✓ Hosting or data processing services – not limited to ISPs/search portals
- ✓ Advance Department of Commerce-certified 5-year investment in real/personal property of:
 - ≥ \$150MM if in a Tier 1 (least developed) county
 - ≥ \$225MM in a Tier 2 or Tier 3 county (\$300MM prior to 7/1/10)
 - ≥ Effective 7/1/10, \$75MM for a taxpayer’s (or its affiliate’s) *second, linked* datacenter
- ✓ Concurrently maintainable power/cooling systems
- ✓ Redundant storage/processing capacity using multiple distribution paths
- ✓ Must meet traditional “Lee Act”-type wage and health insurance requirements apply

❖ “Exemption” scope - Electricity not covered (different for mfrs – electricity tax sunsets 7/10)

- ✓ Property used purely in the provision of datacenter services
- ✓ Equipment used to manage or power this property (**but not power itself**)
- ✓ Effective 7/1/10: Contractor/Subcontractor procurement option:
 - Requires contractor registration
 - Implications for contractor procurements for “fully” exempt projects unclear
- ✓ Exemption sunsets 7/1/15

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Concluding Remarks [Questions]

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