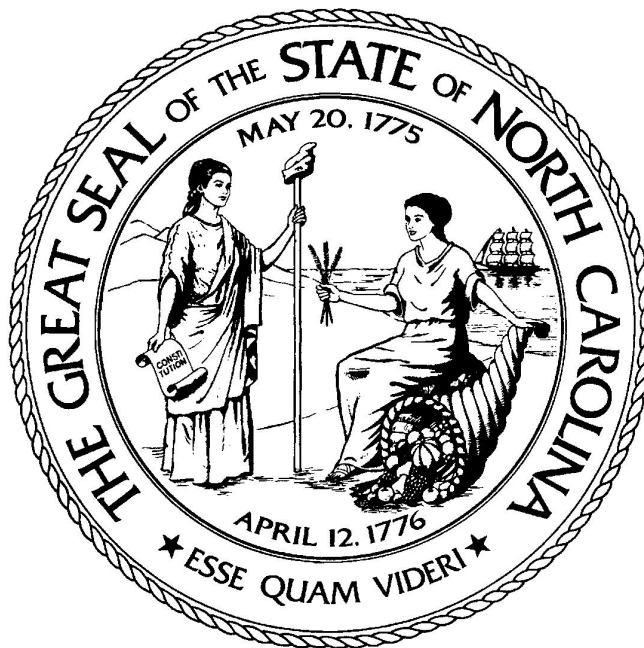


**2007-2008
REVENUE LAWS STUDY
COMMITTEE**



**REPORT TO THE 2009
GENERAL ASSEMBLY OF NORTH CAROLINA
2009 SESSION**

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TABLE OF CONTENTS

| | |
|---|----|
| <u>Letter of Transmittal</u> | i |
| <u>Revenue Laws Study Committee Membership</u> | ii |
| <u>Preface</u> | 1 |
| <u>Committee Proceedings</u> | 3 |
| <u>Committee Recommendations and Legislative Proposals</u> | 29 |
| 1. <u>AN ACT TO UPDATE THE REFERENCE TO THE INTERNAL REVENUE CODE USED IN DEFINING AND DETERMINING CERTAIN STATE TAX PROVISIONS</u> | 30 |
| 2. <u>AN ACT TO CHANGE THE CORPORATE INCOME TAX</u> | 46 |
| 3. <u>AN ACT TO URGE THE 111TH CONGRESS TO GRANT STATES THE ABILITY TO REQUIRE COLLECTION OF SALES AND USE TAX BY REMOTE RETAILERS AND TO UPDATE THE REFERENCE TO THE STREAMLINED SALES AND USE TAX AGREEMENT</u> | 51 |
| 4. <u>AN ACT TO ASSIST COUNTIES AND THE DEPARTMENT OF REVENUE IN OBTAINING ACCURATE REAL PROPERTY SALES INFORMATION NEEDED FOR PROPERTY TAX APPRAISALS BY REQUIRING A REPORT OF SALES INFORMATION WHEN REAL PROPERTY IS TRANSFERRED</u> | 57 |
| 5. <u>AN ACT TO MODERNIZE THE SALES AND USE TAX STATUTES BY TREATING MUSIC, MOVIES, COMPUTER SOFTWARE, AND BOOKS THAT ARE DELIVERED ELECTRONICALLY THE SAME AS THOSE THAT ARE PURCHASED IN A TANGIBLE MEDIUM AND BY REVISING THE "MAIL ORDER" SALES TAX PROVISIONS TO INCLUDE SPECIFIC REFERENCES TO INTERNET SALES</u> | 63 |
| 6. <u>AN ACT TO MAKE TECHNICAL, CLARIFYING, AND ADMINISTRATIVE CHANGES TO THE TAX AND RELATED LAWS</u> | 76 |

Appendices*

- A. [Authorizing Legislation, Article 12L of Chapter 120 of the General Statutes](#)
- B. [Meeting Agendas](#)
- C. [Disposition of Committee's Recommendations to the 2008 Session](#)
- D. [Remarks Concerning Sales Taxation of Digital Products from Brooks Raiford, President & CEO, North Carolina Technology Association](#)
- E. [List of Counties Impacted by 2008 Legislation Advancing Reappraisal Schedule](#)
- F. [List of Counties that Obtain Sales Information on Real Property Transfers](#)
- G. [Examples of Real Property Sales Information Forms](#)
- H. [North Carolina Hospital Association Report on Charity Care and Community Benefit Data](#)
- I. [North Carolina Department of Revenue Report on Revenue Generated from Captive REIT Provision](#)
- J. [Department of Revenue Report on Customer Service Initiatives dated January 27, 2009](#)

*All of the meeting handouts, including Power Point presentations, may be accessed online at the Revenue Laws Study Committee website: <http://www.ncleg.net/committees/>



REVENUE LAWS STUDY COMMITTEE
State Legislative Building
Raleigh, North Carolina 27603

Senator John H. Kerr, III, Cochair

Representative Paul Luebke, Cochair

February 10, 2009

TO THE MEMBERS OF THE 2009 GENERAL ASSEMBLY:

The Revenue Laws Study Committee submits to you for your consideration its report pursuant to G.S. 120-70.106.

Respectfully Submitted,

Rep. Paul Luebke, Co-Chair

Sen. John Kerr, Co-Chair

2007-2008

REVENUE LAWS STUDY COMMITTEE

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PREFACE

The Revenue Laws Study Committee is established in Article 12L of Chapter 120 of the General Statutes to serve as a permanent legislative commission to review issues relating to taxation and finance. Before it was created as a permanent legislative commission in 1997, the Revenue Laws Study Committee was a subcommittee of the Legislative Research Commission. It has studied the revenue laws every year since 1977. The Committee consists of sixteen members, eight appointed by the President Pro Tempore of the Senate and eight appointed by the Speaker of the House of Representatives. Committee members may be legislators or citizens. The co-chairs for 2007-2008 are Senator John Kerr and Representative Paul Luebke.

In its study of the revenue laws, G.S. 120-70.106 gives the Committee a very broad scope, stating that the Committee "may review the State's revenue laws to determine which laws need clarification, technical amendment, repeal, or other change to make the laws concise, intelligible, easy to administer, and equitable." A copy of Article 12L of Chapter 120 of the General Statutes is included in Appendix A. A committee notebook containing the Committee minutes and all information presented to the Committee is filed in the Legislative Library and may also be accessed online at the Committee's website: <http://www.ncleg.net/committees/>

In 2002, the General Assembly established a permanent subcommittee under the Revenue Laws Study Committee to study and examine the property tax system.¹ The subcommittee consists of eight members, four appointed by the Senate chair of the Revenue Laws Study Committee and four appointed by the House chair of the

¹ S.L. 2002-184, s. 8.

Committee. The subcommittee may recommend changes in the property tax system to the full Committee for its consideration in its final report to the General Assembly. Although the Property Tax Subcommittee did not meet during the 2008-2009 interim and has not met since 2004, staff met with representatives from the North Carolina Department of Revenue and groups of tax assessors and collectors throughout the State to discuss ways to improve the implementation of property tax changes that had been recommended by the Revenue Laws Study Committee and enacted during the 2007-2008 biennium.

COMMITTEE PROCEEDINGS

The Revenue Laws Study Committee met five times after the adjournment of the 2008 Regular Session of the 2007 General Assembly on July 18, 2008. Appendix B contains a copy of the Committee's agenda for each meeting. All of the materials distributed at the meetings may be viewed on the Committee's website: <http://www.ncleg.net/committees/>. The Committee received numerous requests from legislators, taxpayers, the Department of Revenue, and interest groups to study various issues of tax policy and tax administration. The Committee considered many issues but was unable to take up all of the issues suggested to it. The Committee considered all proposed tax changes in light of general principles of tax policy and as part of an examination of the existing tax structure as a whole.

REVIEW OF THE RECOMMENDATIONS MADE TO THE 2008 GENERAL ASSEMBLY

The 2008 General Assembly enacted 13 of the Revenue Laws Study Committee's 14 legislative proposals in whole or in part. Appendix C lists the Committee's recommendations and the action taken on them in 2008. A document entitled "**2008 Finance Law Changes**" summarizes all of the tax legislation enacted in 2008. It is available in the Legislative Library located in the Legislative Office Building. It may also be viewed on the Legislative Library's website: <http://www.ncleg.net/LegLibrary> under 'Studies and Reports,' 'Tax Law Changes (1996 – 2008)'.

IRC UPDATE

North Carolina's tax law tracks many provisions of the federal Internal Revenue Code by reference to the Code.² The General Assembly determines each year whether to update its reference to the Code.³ Updating the reference makes recent amendments to the Code applicable to the State to the extent that State law previously tracked federal law. The current reference to the Code is May 1, 2008. Since that date, Congress has enacted five pieces of legislation that made changes to the Code. This federal legislation includes the Heartland, Habitat, Harvest, and Horticulture Act of 2008, signed into law May 22, 2008 (P.L. 110-234); the Heroes Earnings Assistance and Relief Tax Act of 2008 signed into law June 17, 2008 (P.L. 110-245); the Housing Assistance Tax Act of 2008 signed into law July 30, 2008 (P.L. 110-289); the Emergency Economic Stabilization Act of 2008 signed into law October 3, 2008 (P.L. 110-343); and the Worker, Retiree, and Employer Recovery Act of 2008 (P.L. 110-458) signed into law December 23, 2008. In addition to the preceding acts, an action by the Treasury Department may affect State revenue. On September 30, 2008 the IRS issued Notice 2008-84. This notice provides a potential tax break to purchasers of banks with outstanding bad debt.

The Committee began its discussion of conformity with an overview of the five federal acts. Specific attention was given to the Housing Assistance Tax Act (HATA) and the Emergency Economic Stabilization Act (EESA) in light of the substantial fiscal

² North Carolina first began referencing the Internal Revenue Code in 1967, the year it changed its taxation of corporate income to a percentage of federal taxable income.

³ The North Carolina Constitution imposes an obstacle to a statute that automatically adopts any changes in federal tax law. Article V, Section 2(1) of the Constitution provides in pertinent part that the "power of taxation ... shall never be surrendered, suspended, or contracted away." Relying on this provision, the North Carolina court decisions on delegation of legislative power to administrative agencies, and an analysis of the few federal cases on this issue, the Attorney General's Office concluded in a memorandum issued in 1977 to the Director of the Tax Research Division of the Department of Revenue that a "statute which adopts by reference future amendments to the Internal Revenue Code would ... be invalidated as an unconstitutional delegation of legislative power."

impact conformity would have on State revenues. The HATA includes a provision that allows an additional standard deduction to be taken by non-itemizers for State and local real property taxes paid. The EESA provides compensation limits for executives of financial institutions participating in the Troubled Asset Relief Program, extends various deductions for both individuals and businesses, and provides disaster relief for victims of federally declared disasters occurring in 2008 and 2009.

The fiscal impact on the State's General Fund of fully conforming to all five acts would be a combined loss of approximately \$191 million for the 2009-10 and 2010-11 fiscal years. Of this loss to the General Fund, \$13 million is associated with the additional standard deduction for real property taxes provision. The additional standard deduction would reduce the State's General Fund by approximately \$3 million for the 2008-09 fiscal year and \$10 for the 2009-10 fiscal year.

In deciding whether to conform to the federal changes, the Committee balanced the benefits of conformity, which include improved compliance, tax simplicity, and ease of administration, against the General Assembly's responsibility to provide the necessary revenues to support the State's budget. In light of the cost of conformity, the unknowns associated with the budget outlook, and the possibility of further substantial federal legislative changes to the Code, the Committee recommended Legislative Proposal 1, *IRC Update*. The proposal updates the Code reference to January 1, 2009, and conforms to all of the federal changes, with the exception of the additional standard deduction for real property taxes provision in HATA and extended by the EESA. Under this proposal taxpayers would be required to add back the additional standard deduction for real property taxes to federal taxable income for the purposes of determining State net income.

CHANGE CORPORATE INCOME TAX

The Revenue Laws Study Committee recommended to the 2007 Session of the General Assembly that the State consider changing how a corporation determines its net income for corporate income tax purposes. Under current law, a corporation files as a separate entity, meaning it must determine its State net income as if a separate return had been filed for federal income tax purposes. Under the proposal recommended by the Committee to the 2007 General Assembly, a corporation that is part of an affiliated group engaged in a single trade or business would file a combined report.⁴ The General Assembly did not enact the legislation last biennium because many of the outstanding issues that needed to be addressed by the proposal were left unresolved. The Committee continued its study of business taxation this interim.

The Committee first began its study of the issue of business taxation with a directive from the General Assembly to review the authority of the Secretary of Revenue to require taxpayers to file consolidated returns and to consider whether the State should require corporations to file consolidated returns.⁵ The Committee considered the issue at five meetings prior to the convening of the 2007 Session of the General Assembly: September 5, 2006, November 16, 2006, December 12, 2006, January 16, 2007, and January 23, 2007. The Committee considered the issue at four meetings prior to the convening of the 2009 General Assembly: November 19, 2008, December 15, 2008, January 7, 2009, and January 28, 2009. Over the course of the past three years, the Committee heard from its staff, the Department of Revenue, and taxpayers. The Committee also sought the insight and knowledge of other states that have recently enacted legislation in this area, namely West Virginia and Texas.

⁴ Senate Bill 244 and House Bill 462.

⁵ S.L. 2006-196.

The Committee learned that North Carolina's corporate income tax has been declining as a percentage of tax revenues for decades. The reason for the decline is twofold: tax policy decisions enacted by the General Assembly and tax shifting strategies of corporate taxpayers. North Carolina begins its calculation of corporate income tax with federal taxable income. In addition to policy decisions made at the federal level that decrease federal taxable income⁶, such as accelerated depreciation, the General Assembly has amended the North Carolina tax laws to provide various corporate tax credits that reduce the amount of corporate tax payable to the State, such as the Article 3J tax credits. Business tax planning strategies also account for part of the decline in corporate tax revenues as a percentage of overall tax revenues. North Carolina's requirement that a corporation file as a separate entity enables many of these strategies.

Separate entity filing gives corporations with subsidiaries in multiple states the ability to devise ways to shift income from a high effective tax rate state to a low effective tax rate state, often through the use of passive investment companies and inter-company transactions. Over the past several years, the General Assembly has enacted changes to the State's corporate income tax laws to address the shifting of income between states by multistate corporations. Despite these efforts, the problem of income shifting between multistate corporations continues to be an issue.

The Department of Revenue has aggressively used the tools available to it to require a corporation to file a consolidated return when the Department believes the corporation's net income attributable to this State is not accurately reflected on its separate entity filing return. This action by the Department is referred to as "forced

⁶ The General Assembly chooses whether or not to conform to the federal tax law changes each year when it considers legislation updating the date of reference to the Internal Revenue Code.

combination." The Department has used forced combinations for a number of years and it has collected more than \$200 million in taxes from forced combinations.

Taxpayers, seeking clarity on the law, have filed lawsuits contesting the Department's authority to force combinations. G.S. 105-130.6 provides the authority the Department uses to force combinations. Taxpayers express concern that the statute is vague and there are no administrative rules or directives to provide guidance or certainty to taxpayers as to when a combined reporting is required, who is required to be included in the combined report, or how the combination is to be accomplished. Taxpayers believe the statute does not provide any meaningful taxpayer remedies because it says: "*The findings and conclusions of the Secretary shall be presumed to be correct and shall not be set aside unless shown to be plainly wrong.*"

The adoption of mandatory combined reporting would address both the issue of income shifting and the issue of the lack of clarity in the law concerning forced combinations. Several prior studies have recommended that North Carolina require combined reporting. The Governor's Commission to Modernize State Finances recommended moving from single entity reporting to combined reporting as long ago as 2001. In 2007, this Committee, the Income Tax Subcommittee of the State and Local Fiscal Modernization Study Commission, and Governor Easley⁷ all recommended this change. The Multistate Tax Commission adopted a model uniform statute for combined reporting in 2006. Twenty-two states⁸ require combined reporting; six of those states have adopted combined reporting since 2004.⁹

⁷ Governor Easley included the tax law change in his budget recommendation to the 2007 General Assembly, see HB 706, 707, and 708.

⁸ Alaska, Arizona, California, Colorado, Hawaii, Idaho, Illinois, Kentucky, Maine, Minnesota, Montana, Nebraska, New Hampshire, Massachusetts, Michigan, New York, North Dakota, Oregon, Texas, Utah, West Virginia, and Vermont.

⁹ Massachusetts, Michigan, New York, Texas, West Virginia, and Vermont.

The Committee acknowledges that its recommendation to the 2007 General Assembly did not resolve several key issues that would need to be addressed before the State could adopt combined reporting. Those issues include the following:

- The percentage reduction by which the corporate income tax rate could be reduced to render the proposal revenue-neutral. The Committee anticipates that broadening the corporate tax base, which combined reporting would do, would generate additional corporate income tax revenue. It continues to be the Committee's desire that any change to the corporate income tax structure be revenue-neutral.
- The relationship between combined reporting and the franchise tax statutes.
- A determination as to what corporations, if any, would be excluded from combined reporting.
- How the income of corporations with special apportionment formulas under the current law would be apportioned under combined reporting.
- Various transitional and administrative issues.

The Committee did not want to recommend a proposal to the 2009 General Assembly that did not address the unresolved issues from 2007. However, the Committee remains supportive of legislation that would further the following tax policy goals:

- Provide a more level playing field for all businesses, both those that operate only in North Carolina and those that operate in multiple states.
- Provide a comprehensive structure to nullify income shifting strategies.
- Modernize the tax laws to adapt to the growth of multi-state corporations.

- Reduce uncertainty about when a corporation needs to file a combined return, who the corporation includes in it, and how the combination is to be accomplished.
- Broaden the corporate income tax base and adjust the tax rate to make the changes revenue-neutral.

The Committee believes that, through its members, much work may be accomplished during the 2009 session on the issue of business taxation. Legislative Proposal #2, *Change Corporate Income Tax*, states the intent of the General Assembly to change the corporate income tax laws to accomplish the goals established by the Committee.

SALES AND USE TAX

Modernize Sales Tax Statutes/Digital Products

One of the primary objectives of the Revenue Laws Study Committee is to regularly review the tax laws to determine whether they need updating and whether they meet principles of simplicity, fairness, and ease of administration. In 2007, the Streamlined Sales and Use Tax Project (SSUTP) examined the issue of digital products and, after lengthy consideration, adopted definitions and issued rules to guide member states that choose to tax these items. In light of the Committee's mission and its ongoing participation in the SSUTP, the Committee undertook a study of taxing digital products.

Three findings emerged from its study of this issue. First, the Committee recognized that the sales and use tax statutes are outdated in relation to today's modern retail economy. The sales and use tax statutes were originally enacted in the 1930s and were drafted to apply to sales of tangible personal property because those items constituted the bulk of consumer purchases at that time. Technology and the

prevalence of the Internet have transformed society in a number of ways, including the way in which consumers make purchases. Over the last 10 years, more and more consumers shop online and download or stream media in digital format. When the sales tax statutes were enacted, intangible digital goods were not in existence and therefore not contemplated under the tax code. Because purchases of media in digital format are quickly becoming the norm, a number of State legislatures are revisiting their sales tax statutes and considering changes that would bring those statutes into the 21st Century.

Second, the Committee found that the sales and use statutes are inequitable to the extent that similar, if not identical, items are treated differently based upon the method of delivery or the point of purchase. This unequal treatment impacts consumers as well as retailers. For example, a consumer who purchases a CD in a "brick and mortar" retail establishment, such as Walmart, pays sales tax on that item. Likewise, a consumer who orders the CD from the Walmart website pays sales tax on that item. However, a consumer who downloads the exact same CD in MP3 format from the Walmart website does not pay any sales tax on the item. In these examples, the consumer purchases the same item, but the tax treatment differs. This differing tax treatment discriminates against consumers who either choose to purchase a tangible format or who do not have the technological capability to download or stream in digital format because they do not have a computer or high-speed Internet access. Moreover, the tax code should not drive consumer choice; it should be neutral as to industry, content, and delivery method. This unequal tax treatment also places brick and mortar retailers, or at least those without an Internet presence, at a competitive disadvantage with Internet retailers. A sound tax structure is one that is fair and neutral. Taxing digital goods in the same manner as their tangible counterparts would promote these

principles.

Third, the Committee recognized that the State will lose sales tax revenue that it is currently collecting as consumers continue to transition from purchases of tangible media to purchases of digital media. With these findings in mind, the Committee recommended Legislative Proposal #5, *Modernize Sales Tax Statutes/Digital Products*. The Proposal does three things:

- It applies the general rate of State and local sales tax to certain digital goods when the tangible equivalent of the good would be subject to sales tax.
- It eliminates the sales and use tax exemption on prewritten computer software delivered electronically or via load and leave.
- It revises the "mail order sale" provision by modernizing the terminology and by providing that a retailer is presumed to be soliciting business in this State when it enters into certain commission agreements with in-State residents and the contractual arrangement generates in excess of \$10,000 in sales to the retailer.

These three items relate to modernizing the sales tax statutes to more accurately reflect the current retail economy. The first two address items that are received in a digital format. The third item addresses the modern methods by which retailers sell their products. At its last meeting, the Committee discussed North Carolina's current "mail order" provisions and a recent New York trial court decision.

The current mail order provision, G.S. 105-164.8(b), sets out the circumstances under which a remote retailer is engaged in business in this State and, therefore, is required to collect sales tax. The circumstances listed in that statute include when a retailer has representatives in this State who solicit or transact business on behalf of the

retailer regardless of whether the sales subject to tax result from the solicitation. This specific statutory statement of when a retailer is engaged in business reflects the nexus principles established in the 1960 United States Supreme Court case of Scripto v. Carson. In that case, the Supreme Court held that sufficient nexus existed to subject an out-of-state company to tax collection by virtue of having 10 in-state independent contractors who solicited orders for products on behalf of that company.

New York recently amended its sales tax statutes to provide that a retailer is presumed to be soliciting business through an independent contractor or other representative in that State and, therefore, required to collect sales tax if all of the following conditions are met:

1. The retailer has entered into an agreement with a resident of that State.
2. Under the agreement, the resident receives a commission or other consideration in exchange for directly or indirectly referring potential customers, whether by a link on an Internet website or otherwise, to the retailer.
3. The cumulative gross receipts from sales by the retailer to purchasers in that State who are referred to the retailer by all residents with this type of agreement with the retailer is in excess of \$10,000 during the preceding four quarterly periods.

The presumption may be rebutted by proof that the resident with whom the retailer has an agreement did not engage in any solicitation in the State on behalf of the retailer that would satisfy the nexus requirement of the United States Constitution.

Amazon brought a lawsuit challenging the constitutionality of this provision arguing that it violates the Commerce Clause of the United States Constitution as well as both the Federal and State Constitutions' Due Process and Equal Protection Clauses.

On January 12, 2009, the New York Supreme Court¹⁰ dismissed the complaint for failure to state a cause of action. The court disagreed with Amazon's assertion that the commissioned agents were mere advertisers concluding out that the provision requires tax collection only when an out-of-state seller avails itself of the benefit of in-state contractors who are compensated for referrals and who generate actual business for the seller. Proposal #5 revises North Carolina's mail order provision by specifically adding language identical to the New York provision and by modernizing the terminology from "mail order" to "remote" to more accurately reflect the prevalence of Internet sales. The addition of the New York language continues to reflect the nexus principles established in the Scripto case.

After the presentation of the proposal, there was some Committee discussion with regard to the scope of the tax on digital goods under the proposal and the extent to which other states were already taxing these items. There was no discussion of the Amazon case. Brooks Raiford, President and CEO of the North Carolina Technology Association gave some remarks after the presentation of the proposal, which can be found in Appendix D. The Committee voted to include the proposal in its final report.

Streamlined Sales and Use Tax Project Update

The Revenue Laws Study Committee has spent a considerable amount of time over the past several years on the Streamlined Sales and Use Tax Project (SSUTP), which began in March 2000. The adoption of the Streamlined Sales and Use Tax Agreement (Agreement) in 2002 provided the framework for participating states to achieve the uniformity and simplification measures initially established by a coalition of states, local governments, and businesses. The goal of the SSUTP is to achieve sufficient

¹⁰ The New York Supreme Court is a trial-level court.

simplification and uniformity to encourage sellers without nexus in states to voluntarily collect use tax in those states that have adopted the uniform provisions of the Agreement. Based on decisions by the United States Supreme Court, states cannot require remote sellers that do not have a physical presence in the state to collect and remit its use tax.

Andy Sabol, the director of the Sales and Use Tax Division of the Department of Revenue, updated the Committee on the activities of the Streamlined Sales Tax Governing Board (Governing Board). North Carolina is one of twenty-two states represented on the Governing Board. The Governing Board established a central registration system in October 2005 that allows sellers to register for sales and use tax purposes in all member states. Over 1,000 sellers have registered since the system's inception.

Since October 2005, North Carolina has collected approximately \$36 million in use tax revenue from remote sellers. The State has received \$7.9 million during the 2008-2009 fiscal year to date. The amounts collected voluntarily are far less than the estimated amounts the State is not collecting in use tax revenue from sales by remote sellers. A University of Tennessee study, commissioned a few years ago, estimated a revenue loss to state and local governments of more than \$30 billion a year from uncollected use taxes on remote sales. The Governing Board has recently commissioned a study to provide an update on this estimate.

The United States Supreme Court has stated in its decisions that Congress has the authority to grant states the ability to require collection of sales and use tax by remote sellers. Sen. Mike Enzi (R-WY) and Rep. William Delahunt (D-MA) introduced a bipartisan bill in the 110th Congress to provide the necessary authorization to those states that had adopted the simplification and uniformity measures established in the

Agreement. Although Congress did not enact the legislation last biennium, the Governing Board believes that the 111th Congress may represent the best opportunity for action on the Streamlined-related legislation, known as the Sales Tax Fairness and Simplification Act (STFSA). The National Conference of State Legislatures has recommended that Congress include the provisions of the STFSA as part of the economic stimulus legislation it is working to develop. The provisions of the STFSA would provide tens of billions of dollars in funding to states and local governments at a minimal or no cost to the federal government.

Legislative Proposal #3, *Streamlined Sales and Use Tax Update*, does two things:

- It encourages the 111th Congress to enact the provisions of the STFSA.
- It updates the statutory reference to the Agreement by changing the date from June 23, 2007, to September 5, 2008. North Carolina does not need to amend its sales and use tax laws to conform to any of the changes made in the Agreement since June 23, 2007.

Taxation of Food

Section 28.16(h) of S.L. 2008-107 directed the Revenue Laws Study Committee to study the distinction between food for home consumption and prepared food under the sales and use tax laws and determine whether the distinction should be eliminated by applying a uniform, revenue-neutral rate to all food.

The Committee began its discussion by reviewing the legislative history of the sales tax on food for home consumption and prepared food:

- **1933:** Food for human consumption exempt from sales tax.¹¹
- **1961:** Food exemption repealed. Food for home consumption subject to

¹¹ Except from 1935-1937.

sales tax.

- **1998:** State sales tax rate on food for home consumption phased out. Food remains subject to a 2% local sales tax rate. Prepared food remains subject to the combined rate of State and local sales tax.
- **2000:** Definitions of "food" and "prepared food" modified to conform to the Streamlined Sales and Use Tax Agreement. Food for home consumption remains exempt from State sales tax and subject to local sales tax; prepared food remains subject to the combined State and local sales tax. However, some foods once defined as "food" and exempt from State tax become defined as "prepared food" and become subject to the combined State and local tax rate.
- **2007:** Bread, rolls, and buns sold at a bakery thrift store exempt from State sales tax; they remain subject to local sales tax.
- **2008:** Bakery items defined as a special class of prepared food. Bakery items exempt from State sales tax; remain subject to local sales tax.

The distinction between food for home consumption and prepared food often becomes complex. Prepared food is food that meets one or more of the following conditions: the retailer made the food item by mixing or combining two or more foods for sale as a single item or the retailer provides eating utensils to customers to use in consuming the food. Any food item prepared by a retailer and sold by the retailer to a consumer is a prepared food. A similar product produced by someone else, but sold by the same retailer, is food for home consumption. For example, slaw prepared by Harris Teeter and sold in its deli section is prepared food. Slaw produced by someone else and sold at Harris Teeter is food. Likewise, the same product may be defined differently

depending upon where it is purchased. For example, a donut purchased at the place where it is made is prepared food. The same donut purchased at a grocery store is food.

How food is defined determines its tax rate. In North Carolina, there is a local sales tax rate of 2% on food for home consumption while prepared food is subject to the general State sales tax rate of 4.25% as well as the applicable local rate, which ranges from 2.5% to 2.75%. The General Assembly directed the Committee to consider whether the distinction between food for home consumption and prepared food should be eliminated by taxing all food at a uniform, revenue-neutral rate. The Committee learned that the revenue-neutral rate that would need to apply to all food would be 5.1%. That would mean that the tax rate on prepared food would decrease from 6.75% to 5.1%; but the tax rate on food for home consumption would increase from 2% to 5.1%. The Committee did not move forward with a legislative proposal on this issue.

PROPERTY TAX

Advancement of Reappraisal Schedule

The Revenue Laws Study Committee recommended legislation to the 2008 Session of the 2007 General Assembly that would have advanced the octennial schedule for general appraisals of property tax to a quadrennial schedule. The purpose of this proposal was to reduce the discrepancy between the property tax value of property and its market value, since the law requires that property be appraised at its true or market value for property tax purposes. During the 2008 Session, several small, rural counties voiced concerns about their lack of manpower and the expense of conducting more frequent appraisals. As a result, the version of the Committee's proposal enacted during the 2008 Session requires an advanced reappraisal schedule only when a county has a population of 75,000 or greater and the county's sales assessment ratio shows that

the assessed value of the property differs from the sales price of the property by more than 15% (S.L. 2008-146). Currently, only ten counties are affected by the 2008 legislation, which are listed in the chart in Appendix E.

Legislative Proposal 4, *Real Property Sales Information*, is an attempt to assist the counties in satisfying the statutory requirement of appraising property at its true value without requiring more frequent appraisals. The proposal would require that certain information be reported to the county assessor each time property is transferred in the county. This information would be provided to the assessor on a form developed by the Department of Revenue, and the deed transferring the property would not be accepted by the county register of deeds until the tax assessor certifies that the form was filed. A list of counties that currently require this information to be provided and examples of their forms can be found in Appendix F and Appendix G, respectively.

The Committee recommended Proposal 4 after reviewing the current law on appraising real property and studying recommendations from tax assessors on how to assist them in conducting general reappraisals. These recommendations were elicited during field trips in which staff of the Committee and the Department's Property Tax Division met with tax assessors from large urban counties and small rural counties.¹² The assessors recognized the advantages of advancing the schedule; however, assessors from the smaller more rural counties pointed out that revaluations are expensive and that they do not have the manpower or revenue to conduct them. The three main recommendations made by the tax assessors were:

- Require statewide sales information forms.

¹² Staff met in Charlotte with tax assessors from Mecklenburg County and surrounding counties and in Edenton with assessors from Chowan County and surrounding counties.

- Provide funding for staff at the State level to assist smaller counties with revaluations.
- Update the schedules of values in the fourth year of a general reappraisal cycle in lieu of conducting a full reappraisal.

The Committee felt that a proposal requiring parties to a land transfer to file a sales information report with the county tax assessor would be the most helpful and cost-efficient way to assist the counties in achieving the statutory requirement of appraising property at its true value for tax purposes. The Committee was informed that approximately one-half of the counties are currently requesting confirmation letters regarding transfers of property while only five counties require information affidavits. A list of these counties is found in Appendix E, and examples of sales information disclosure forms used by some of these counties are in Appendix F. This proposal would require information reports in all counties before the deed transferring the property could be accepted for recording.

Tax Exemptions for Nonprofits

At its October 22, 2008, meeting, the Revenue Laws Study Committee heard two staff presentations regarding the tax treatment of nonprofits. The first presentation provided a general overview, and the second presentation focused specifically on hospital charity care, spotlighting ongoing measures at the federal level, both in Congress and within the Internal Revenue Service. These presentations were followed by remarks from a guest speaker, Stan Jenkins, a county tax assessor from Illinois, who discussed one of the nation's leading, ongoing cases involving the denial of a property tax exemption for a nonprofit hospital.

Nonprofit entities benefit from a number of both federal and state tax exemptions. One rationale for the exemptions is that nonprofits provide services and benefits that the government would otherwise have to provide with tax dollars. While nonprofits are subject to some federal taxes, such as FICA and telephone and gasoline excise taxes, they are not subject to income tax. At the State level, nonprofits are afforded the following tax benefits:

- Exemption from State income tax.
- Eligibility for a semiannual sales tax refund.
- Exemption from property tax.
- Deductibility for donors of charitable contributions.

Of the nonprofit entities, hospitals in particular have come under frequent scrutiny at the national, state, and local levels. Unfavorable newspaper articles have reported that many nonprofit hospital systems are more profitable than for-profit hospitals and cite examples of hospitals reinvesting most of the profits into rich executive pay and high-end capital improvements rather than focusing on the level of charity care being provided. In 2004, there were 40 class action lawsuits against nonprofit hospitals and legislation introduced in 12 states in an attempt to reign in their aggressive collection practices directed at uninsured patients. From 2005 to 2008, both the Government Accountability Office and the IRS conducted studies of the charity care issue resulting in consistent findings. Specifically, the IRS found:

- There is a wide variation in eligibility for charity care.
- There is a wide variation in publicizing opportunity for charity care.
- 45% of hospitals spent 3% or less on charity care.
- Nearly 25% spent 1% or less on charity care.

As a result of the study, the IRS modified the form on which nonprofits report their community activities as a means to justify their tax-exempt status. Areas of significant change included governance and compensation of officers, directors, trustees, key employees, and highest compensated employees as well as the method for determining public charity status. One of the goals of the new form is to standardize the definition and calculation of charity care and community benefits.

In addition to getting a national perspective, the Committee also looked at the relevant North Carolina statutes and found that for the different exemptions, there are different thresholds or standards that must be met in order to obtain the exemptions. Nonprofit hospitals, for example, may apply for a sales tax refund for purchases of tangible personal property¹³ used in carrying on the work of the nonprofit. The refund is essentially automatic. However, in order to obtain a property tax exemption, the statute requires that the property owned and operated by a nonprofit hospital be "actually and exclusively used for charitable hospital purposes." A charitable hospital purpose is defined as "a hospital purpose that has humane and philanthropic objectives; it is a hospital activity that benefits humanity or a significant rather than limited segment of the community without expectation of pecuniary profit or reward." Most states have similar language in their statutes, and nonprofits have increasingly come under fire for not meeting their statutory obligation of "actually and exclusively" or "wholly and exclusively" providing charity care, as those terms have been interpreted by the courts.

The Committee also heard examples of a growing trend among local governments to deny property tax exemptions for nonprofits, especially for hospitals, based on their failure to meet statutory thresholds of providing charity care. Mr.

¹³ Other than electricity, telecommunications service, and ancillary service.

Jenkins spoke to the Committee about one such example based on his experience as a county tax assessor involved in the Provena Covenant Medical Center case. His comments reflected themes similar to those found in the GAO and IRS studies as well as the newspaper articles regarding low levels of charity care and mistreatment of uninsured patients through overcharging and aggressive collection practices.

Also present at the meeting was Hugh Tilson of the North Carolina Hospital Association who informed the Committee that the Association was in the process of compiling information from its members related to the level of community benefit and charity care provided by its members using the revised IRS Guidelines. Mr. Tilson indicated that the Association planned to have this information available on its website by the end of the year. As a follow up, the Committee heard from Hugh Tilson at its final meeting who summarized the data collected to date, a copy of which is attached as Appendix H and for which more detail can be found on the Association's website: <http://www.ncha.org>.

Challenges to these exemptions are not new, but in recent years there has been a surge in the attention given to them. Factors contributing to this increased examination include the rapid and significant growth of nonprofits, the increase in their "commercial" activities, and the number and extent of states experiencing fiscal crisis. The Committee concluded its review of this issue by contemplating whether there is a clear rationale for the various tax exemptions for charitable nonprofits, whether the law is clear and consistent, and whether the current law fulfills its public purpose. The Committee, however, declined to move forward with any proposals on this issue.

PRIVILEGE LICENSE TAX

Local Privilege License Taxes

For the second time in four years, the Revenue Laws Study Committee considered the issue of reforming the privilege license tax system. The catalyst for revisiting this subject was the passage of House Bill 2558, *the Home Inspector Privilege License Act*. With the passage of this act, the General Assembly experienced for the first time since the repeal of most State-level privilege license taxes in 1996, a single industry seeking the imposition of a State privilege tax to shield it from local privilege license taxes. The home inspectors sought the change, in part, because of the way in which the local tax was being applied to businesses operating in multiple cities. Specifically, the home inspectors reported being double-taxed.

At its November 19, 2008, meeting, Christopher McLaughlin, Assistant Professor of Public Law and Government at the UNC School of Government, provided the Committee with an overview of the local privilege license tax system and an analysis of its deficiencies. Mr. McLaughlin characterized the system as archaic, inconsistent, and arbitrary. The system is archaic because it is based on references to repealed statutes, which are essentially "trapped in time" and cannot be changed. Specifically, the repealed statutes refer to monetary caps that have never been adjusted for inflation and to businesses that sell items like record players, tape cartridges, and bagatelle tables. The Committee heard that the law is often applied inconsistently because local business license officers have different, yet valid, interpretations of how to apply the repealed statutes. The system is arbitrary because there is no rationale for exempting some businesses altogether, subjecting some to caps, and subjecting others to an unlimited amount of tax. Given these characteristics, the administration of privilege license taxes frequently proves to be a source of confusion for local governments and taxpayers alike.

The Committee also heard testimony about instances of double taxation. If a city chooses to levy a privilege tax based on a business' total gross receipts while another city levies a tax only on the gross receipts derived from transacting business in that city, then a business that operates in both cities will pay tax twice on some portion of its gross receipts.

At its December 15, 2008, meeting, the Committee heard remarks from Karl Knapp with the North Carolina League of Municipalities and Jim Blackburn with the North Carolina Association of County Commissioners. Mr. Knapp informed the Committee that there was a meeting of business license officers in early December to discuss the issues raised about the privilege license system. He expressed the view of the group that while the system should be updated to eliminate references to repealed statutes and the various caps and exemptions, the system should not be repealed entirely because it is a significant source of income for cities. He also indicated that the group did not believe there were widespread instances of double taxation and that most cities allowed businesses to apportion their gross receipts. Mr. Blackburn was in general agreement with Mr. Knapp's statements and offered the assistance of the Association in helping to draft clarifying language, if the Committee so desired.

At its January 7, 2009, meeting, the Committee heard from Andy Ellen with the Retail Merchants Association and Mark Prak, a Raleigh attorney. Mr. Ellen emphasized the concerns illustrated in Mr. McLaughlin's November presentation. He gave the Committee two specific examples to illustrate the system's inequities. The first example was a grocery store subject to a gross receipts tax because the gross receipts method of taxation will disproportionately impact a business operating on a low gross margin. The second example was a pharmacy that collects copays from customers, which count toward gross receipts but are a pass-through cost that the pharmacy does not get to

keep in terms of profit. Mr. Prak echoed the concerns expressed by Mr. Ellen, stating that privilege license taxes are confusing and unequally applied. He also indicated that, in his law practice, he has been involved in cases where local governments were not apportioning gross receipts for purposes of applying the privilege license tax resulting in the double taxation of certain businesses.

Although the Committee was in general agreement that changes are needed to address the problems with the privilege license taxes, it did not reach a conclusion about specific changes. The Committee was presented with five broad options for modifying the system, but was unable to reach consensus on an approach that would balance the cities' concern about preserving this source of local revenue while addressing the business community's goal of modernization and uniformity.

Resale of Tickets on the Internet

The Revenue Laws Study Committee reviewed the legislation enacted by the 2008 General Assembly. In its review, it considered the sunset placed on S.L. 2008-158. This legislation, *Resale of Tickets via Internet*, allows admission tickets to be resold on the Internet at a price that exceeds the price printed on the ticket. Under prior law, this sale would be a criminal offense. Reselling tickets online is a new and growing business; the legislation recognized this reality and amended the law to remove the criminal offense and to provide safeguards for the venue and the customer.

The issue left unresolved by the legislation is the application of the State privilege license to the resell of the tickets. Under current law, the State imposes a privilege tax on a person engaged in the business of giving, offering, or managing a form of amusement or entertainment.¹⁴ The tax rate is 3% of the gross receipts derived

¹⁴ G.S. 105-37.1.

by the sale. Unlike the sales tax, the privilege tax is a tax on the person, not the transaction. The current law does not impose the privilege tax on a person engaged in the business of reselling tickets to an entertainment event and an entertainment event is not subject to sales tax.

Under the Senate version of the bill, the privilege tax would have been expanded to include a person engaged in the business of reselling tickets. The tax would have applied to the difference between the price of the ticket sold and the face price of the ticket. The House deleted this provision from the bill. The final bill, crafted by a conference committee, placed a sunset on the bill of June 30, 2009.¹⁵ The sunset necessitates the General Assembly revisiting the issue in 2009.

The Revenue Laws Study Committee did not recommend any legislation on this topic. It did recognize that the 2009 General Assembly has several choices:

- It could do nothing. In this event, the Act will sunset and the activity of reselling tickets will once again be illegal.
- It could extend the sunset.
- It could resolve the tax issue in one of three ways:
 - It could remove the sunset, thereby maintaining the status quo – no taxation on the resell of tickets.
 - It could impose the privilege license tax on a person engaged in the business of reselling tickets via Internet.
 - It could change the taxation of amusements by repealing the State privilege license tax on amusements and, in its place, imposing a State and local sales tax on the price of the tickets.

¹⁵ The final version of the bill contained a monthly reporting requirement. The Department of Revenue reported that only four reports have been filed. The reports, filed by different filers, showed less than 100 tickets resold and less than \$5,000 of net proceeds.

TECHNICAL, ADMINISTRATIVE, AND CLARIFYING CHANGES

The Revenue Laws Study Committee recommends Legislative Proposal 6, *Revenue Laws Technical, Administrative, and Clarifying Changes*. This proposal makes several technical and clarifying changes to the revenue laws and related statutes, including changes to the motor fuel tax and property tax laws. Many of the changes were recommendations of the Department of Revenue.

REPORTS TO REVENUE LAWS

At the last meeting, the Department of Revenue made two reports to the Committee. Section 31.18(d) of S.L. 2007-323 directed the Department to report the amount of corporate income tax revenue generated in the 2007 taxable year resulting from the new requirement that corporations are required to add back to taxable income dividends paid by captive real estate investment trusts (REITS). The Department reported that there were 12 entities who reported add-backs generating \$12,805,806 in revenue. A copy of this report is found in Appendix I.

The Small Business Protection Act (Section 28.16(i) of S.L. 2008-107) resulted from concerns raised by small businesses related to advice received by the Department, primarily concerning sales tax obligations. Part of this act required the Department to report to the Revenue Laws Study Committee prior to the convening of the 2009 Session on its customer service initiatives. Linda Millsaps, Chief Operating Officer of the Department of Revenue, presented this report to the Committee, which is attached as Appendix J.

COMMITTEE RECOMMENDATIONS AND LEGISLATIVE PROPOSALS

The Revenue Laws Study Committee makes the following six recommendations to the 2009 General Assembly. Each proposal is followed by an explanation and, if it has a fiscal impact, a fiscal note or memorandum, indicating any anticipated revenue gain or loss resulting from the proposal.

1. IRC Update
2. Change Corporate Income Tax
3. Streamlined Sales and Use Tax Update
4. Real Property Sales Information
5. Modernize Sales Tax Statutes/Digital Products
6. Revenue Laws Technical, Administrative, and Clarifying Changes

LEGISLATIVE PROPOSAL #1

IRC UPDATE

LEGISLATIVE PROPOSAL #1

A RECOMMENDATION OF THE REVENUE LAWS STUDY COMMITTEE
TO THE 2009 REGULAR SESSION OF THE 2009 GENERAL ASSEMBLY

AN ACT TO UPDATE THE REFERENCE TO THE INTERNAL REVENUE CODE USED IN DEFINING AND DETERMINING CERTAIN STATE TAX PROVISIONS.

SHORT TITLE: IRC Update.

SPONSORS:

BRIEF OVERVIEW: This proposal would update from May 1, 2008 to January 1, 2009, the reference to the Internal Revenue Code used in defining and determining certain State tax provisions. By doing so, North Carolina would conform to changes made by five federal acts, except the bill would not conform to the new additional standard deduction for real property taxes authorized by the Housing Assistance Tax Act. The five federal acts are as follows:

- 1) Heartland, Habitat, Harvest, and Horticulture Act of 2008.
 - 2) Heroes Earnings Assistance and Relief Tax Act of 2008.
 - 3) Housing Assistance Tax Act of 2008.
 - 4) Emergency Economic Stabilization Act of 2008.
 - 5) Worker, Retiree, and Employer Recovery Act of 2008.
-
-

FISCAL IMPACT: Based on the analysis of the Joint Committee on Taxation, the bill is expected to have an impact on the State's General Fund. The fiscal impact on the State's General Fund of conforming to all five acts except the new additional standard deduction for real property taxes would be a combined loss of approximately \$177.7 million for the 2009-10 and 2010-11 fiscal years. The methodology used begins with the Joint Tax Committee estimates of the nationwide federal impact by federal fiscal year (Federal fiscal years run from October through September). Fiscal Research adjusted these numbers back to an approximate calendar year tax impact. The next step was to

prorate the national numbers to the state impact. The Department of Revenue undertook this process using taxpayer data and North Carolina economic data.

After calculating the estimated State tax year impacts, the numbers were converted to state fiscal year by assuming that the traditional FRD method of putting 45% of a calendar year tax liability in the January-June period that finishes up one fiscal year and the allocating the remainder to the following fiscal year. There were not adjustments made to the JCT's estimates based on level of taxpayer compliance. Therefore, the fiscal estimates assume 100% taxpayer compliance with the tax law changes.

EFFECTIVE DATE: This act would become effective when it becomes law.

A copy of the proposed legislation, a bill analysis, and fiscal analysis begin on the next page.

**GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2009**

BILL DRAFT 2009-TDx-3 [v.5] (01/21)

**(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)
2/2/2009 8:59:23 AM**

Short Title: IRC Update.

(Public)

Sponsors: .

Referred to:

A BILL TO BE ENTITLED

AN ACT TO UPDATE THE REFERENCE TO THE INTERNAL REVENUE CODE
USED IN DEFINING AND DETERMINING CERTAIN STATE TAX PROVISIONS.

The General Assembly of North Carolina enacts:

SECTION 1. G.S. 105-228.90(b)(1b) reads as rewritten:

"(b) Definitions. – The following definitions apply in this Article:

...

(1b) Code. – The Internal Revenue Code as enacted as of ~~May 1,~~
2008, January 1, 2009 including any provisions enacted as of that date
which become effective either before or after that date."

SECTION 2. Notwithstanding Section 1 of this act, any amendments to the
Internal Revenue Code enacted after May 1, 2008, that increase North Carolina taxable
income for the 2008 taxable year become effective for taxable years beginning on or after
January 1, 2009.

SECTION 3. G.S. 105-134.6(c) reads as rewritten:

"(c) Additions. – The following additions to taxable income shall be made in
calculating North Carolina taxable income, to the extent each item is not included in
taxable income:

...

(11) The amount of the taxpayer's additional standard deduction for real
property taxes under section 63(c)(1)(C) of the Code."

SECTION 4. This act is effective when it becomes law.



Draft 2009-TDx-3: IRC Update

BILL ANALYSIS

| | | | |
|-----------------------|------------------------------|--------------------|-------------------|
| Committee: | Revenue Laws Study Committee | Date: | January 27, 2009 |
| Introduced by: | | Summary by: | Heather Fennell |
| Version: | | | Committee Counsel |

SUMMARY: *This proposal would update the reference to the Internal Revenue Code used in defining and determining certain State tax provisions from May 1, 2008 to January 1, 2009. By doing so, North Carolina would conform to the changes made by five federal acts, except the bill would not conform to the new additional standard deduction for real property taxes. This bill would become effective when it became law.*

CURRENT LAW: North Carolina's tax law tracks many provisions of the federal Internal Revenue Code by reference to the Code.¹ The General Assembly determines each year whether to update its reference to the Internal Revenue Code.² Updating the Internal Revenue Code reference makes recent amendments to the Code applicable to the State to the extent that State law tracks federal law. The General Assembly's decision whether to conform to federal changes is based on the fiscal, practical, and policy implications of the federal changes and is normally enacted in the following year, rather than in the same year the federal changes are made.

BILL ANALYSIS:

This bill would change the reference date to January 1, 2009, effective when the bill becomes law. Changing the reference date to January 1, 2009 would incorporate the changes made in the following acts:

- The Heartland, Habitat, Harvest, and Horticulture Act of 2008, signed into law May 22, 2008 (P.L. 110-234).
- The Heroes Earnings Assistance and Relief Tax Act of 2008 signed into law June 17, 2008 (P.L. 110-245);
- The Housing Assistance Tax Act of 2008 signed into law July 30, 2008 (P.L. 110-289);
- The Emergency Economic Stabilization Act of 2008 signed into law October 3, 2008 (P.L. 110-343);
- The Worker, Retiree, and Employer Recovery Act of 2008 (P.L. 110-458) signed into law December 23, 2008.

In addition to the preceding acts, an action by the Treasury Department may affect State revenue. On September 30, 2008 the IRS issued Notice 2008-84. This notice provides a potential tax break to purchasers of banks with outstanding bad debt.

¹ North Carolina first began referencing the Internal Revenue Code in 1967, the year it changed its taxation of corporate income to a percentage of federal taxable income.

² The North Carolina Constitution imposes an obstacle to a statute that automatically adopts any changes in federal tax law. Article V, Section 2(1) of the Constitution provides in pertinent part that the "power of taxation ... shall never be surrendered, suspended, or contracted away." Relying on this provision, the North Carolina court decisions on delegation of legislative power to administrative agencies, and an analysis of the few federal cases on this issue, the Attorney General's Office concluded in a memorandum issued in 1977 to the Director of the Tax Research Division of the Department of Revenue that a "statute which adopts by reference future amendments to the Internal Revenue Code would ... be invalidated as an unconstitutional delegation of legislative power."

Heartland, Habitat, Harvest, and Horticulture Act of 2008

Endangered species recovery expense. – The act creates a new deduction for endangered species recovery expenditures for expenses incurred after December 31, 2008. Farmers may currently claim a deduction for qualifying soil and water conservation expenditures and land erosion prevention expenditures. The deduction is limited to 25% of gross income derived from farming during the tax year but can be carried forward indefinitely. This act adds endangered species recovery expenditures to the category of expenditures that qualify for the deduction. The expenditures must be paid or incurred by a farmer after December 31, 2008 for the purpose of site-specific management actions recommended in recovery plans approved pursuant to the Endangered Species Act of 1973. Depreciable structures, appliances, or facilities do not qualify for the deduction.

Charitable Contributions of Real Property for Conservation Purposes. – The act extends the increased deduction for charitable contributions of real property for conservation purposes for tax years beginning before January 1, 2009. The deduction for capital gain appreciated real property is generally limited to 30% of the donor's adjusted gross income if the donor uses the fair market value of the donated property. If the donor's basis is used as the value of the property, and the property is donated to a "maximum deduction" organization, the deduction is limited to 50% of the donor's adjusted gross income.³ Deductions for donations to non-maximum donation organizations are limited to 20% of the donor's adjusted gross income. Contributions that exceed the deduction limit can be carried forward for five years. The Pension Protection Act of 2006 increased the deduction for donations of conservation easements. An individual may deduct the value of the easement, based on fair market value, up to 50% of adjusted gross income, with a 15-year carryforward for any excess. A "qualified farmer or rancher" may deduct the value of the gift up to 100% of adjusted gross income with a 15-year carryforward. A "qualified farmer or rancher" is an individual whose gross income from the trade or business of farming is greater than 50% of the taxpayer's gross income for the tax year. The land donated by a farmer or rancher also must "be available" for agricultural use, but it need not be used for that purpose. This act extends these provisions through December 31, 2009.

► ***BILL ANALYSIS:*** The bill conforms to the provisions of this act.

Heroes Earnings Assistance and Relief Tax Act of 2008

State or Local Bonuses for Combat Veterans. – The act excludes state or local bonuses for combat veterans from gross income for income tax purposes. Generally all income is included in gross income unless the income is explicitly excluded. "Qualified military benefits" are excluded from gross income. These benefits generally include allowances or in-kind benefits provided to family members and former members of the armed services, or their dependents by reason of the member's service, including housing, moving, and travel allowances. This act expands the definition of "qualified military benefits" to include bonus payments by a state or local government to a member or former member of the armed services, or to a dependent of a member. To qualify for the exclusion, the payment must have been made for the member's service in a combat zone.⁴

³ Maximum deduction organizations include public charities, private operating foundations, private non-operating foundations that distribute contributions within two and one-half months of the year's end, and private non-operating foundations that maintain a common fund.

⁴ A combat zone is defined as any area the president has by executive order designated an area in which the Armed Forces are or have engaged in combat.

Contributions of Military Death Gratuities to Roth IRAs and Coverdell ESAs. – The act allows military death gratuities to be contributed to a Roth IRA or Coverdell ESA regardless of contribution limits and income phase-out limits for Roth IRAs and Coverdell ESAs. Upon notification of the death of military personnel on active duty or on inactive duty training, a death gratuity is paid to or for the person's survivor. The death gratuity is a qualified military benefit and excluded from income. Roth IRAs are subject to annual contribution limits equal to the lesser of the statutory dollar amount or 100% of taxable income. For 2008, the annual limit on contributions is \$5,000 for individuals, with an additional catch up contribution of \$1,000 allowed for individuals over age 50. Sums may be rolled-over from eligible retirement plans to Roth IRAs, subject to income-phase out limitations. For 2008, rollovers are allowed for individuals whose gross adjusted income does not exceed \$100,000. A Coverdell Education Savings Account is a tax-exempt trust created for paying the education expenses of the trust's designated beneficiary. Annual contributions to Coverdell ESAs may not exceed \$2,000. This act allows the gratuity to be contributed to a Roth IRA or Coverdell ESA regardless of contribution limits and income phase-out limits for Roth IRAs and Coverdell ESAs.

► **BILL ANALYSIS:** The bill conforms to the provisions of this act.

Housing Assistance Tax Act of 2008

Real Property Tax Deduction for Non-itemizers. – The act creates a deduction for real property taxes paid by non-itemizers for any tax year beginning in 2008. Taxpayers can take either the basic standard deduction, or itemize deductions, but not both. Taxpayers who itemize deductions may deduct state and local taxes paid, including individual income taxes, real property taxes, and personal property taxes. This act allows taxpayers who take the standard deduction to claim an additional deduction for state and local real property taxes for any tax year beginning in 2008. The deduction is the lesser of (1) the amount allowable as a deduction for state and local taxes if the taxpayer claimed itemized deductions, or (2) \$500 for individuals, \$1000 for joint returns.

► **BILL ANALYSIS:** The bill does not conform to the provision of this act providing an additional standard deduction for state and local real property taxes.

Emergency Economic Stabilization Act of 2008

Executive Compensation Limits for Financial Institutions Participating in Troubled Asset Relief Program (TARP). – The act restricts certain financial institutions that sell troubled assets to the Treasury Department by means of a public action from deducting more than \$500,000 for executive compensation and prohibits the firms from contracting for new golden parachute payments. Firms that sell troubled assets directly to the government must exclude incentives for executive officers to take unnecessary risks; must recover bonuses to senior executives based on materially inaccurate information; and may not make any golden parachute⁵ payments to senior executives while the government holds an equity or debt position in the firm.

Previously, there were three limits in the IRC for executive compensation:

- (1) A publicly held corporation cannot deduct applicable employee remuneration that exceeds \$1 million per tax year.
- (2) A corporation cannot deduct excess golden parachute payments paid to a disqualified individual that were triggered by a change in ownership or control.
- (3) Excess payments are subject to a 20% excise tax paid by the recipient.

⁵ A parachute payment is any payment in the nature of compensation paid to a disqualified individual that either is contingent upon a change in ownership of the corporation and equals or exceeds 3 times the individual's base pay, or is made under an agreement that violates securities laws or regulation.

This act imposes new restrictions on executive compensation for financial institutions that sell troubled assets as part of TARP.

Limits when financial institutions sell troubled assets through a public auction. – If a firm sells troubled assets through a TARP managed public auction to the Treasury, and has assets in excess of \$300 million, the firm must adhere to the following limits on executive compensation.

- (1) \$500,000 limit on the deductibility of executive compensation, including incentive and commission pay.
- (2) No deduction for excess golden parachute payments; excess payments are also subject to a 20% excise tax paid by the recipient.
- (3) Prohibition from entering into a new employment contract that provides a golden parachute in the event of an involuntary termination, bankruptcy filing, insolvency, or receivership.

Limits when sales made directly to the Treasury: If a firm sells troubled assets directly to the Treasury, the firm must adhere to the following standards for compensation and benefits paid to senior executive officers for the duration of time the government holds the assets:⁶

- (1) Limits on compensation that exclude incentives for executives to take unnecessary and excessive risks that threaten the value of the firm.
- (2) Recovery of any bonus or incentive compensation paid to an executive based on statements of earnings, gains, or other criteria that are later proven to be materially inaccurate.
- (3) Prohibition on golden parachutes.

Extension of Income Exclusion for Discharged Indebtedness on Principal Residence. – The act extends the exclusion from income for discharged indebtedness on principal residences for discharges occurring before January 1, 2013. When a lender forecloses on property, sells the home for less than the borrower's outstanding mortgage and forgives all or part of the unpaid mortgage debt, the canceled debt is considered income under the Code. There is no income limitation but no more than \$2 million in mortgage debt is eligible for exclusion. The exclusion from income for discharged indebtedness related to a principal residence is for the three-year period beginning January 1, 2007 and ending December 31, 2009. This act extends the exclusions for discharged indebtedness related to a principal residence for the period beginning January 1, 2007 and ending on December 31, 2012.

Qualified Charitable Distribution from IRAs. – The act extends the favorable treatment of qualified charitable distributions from IRAs for two years, for distributions made in 2008 and 2009. Generally, to make a charitable donation from an IRA, a distribution must be taken and the applicable rules regarding taxable income apply. The distribution is included in taxable income to the extent the distributions are not attributable to a return of nondeductible contributions. The standard charitable deduction rules then apply to the donation. The Pension Protection Act of 2006 provided that individuals 70 ½ or older could distribute up to \$100,000 per taxable year from their IRAs to charitable institutions without recognizing the income. The distribution must be made directly to the charitable organization from the trustee. This distribution counts towards the required minimum distribution. This is extended by the act for distributions in 2008 and 2009.

Transportation Fringe Benefit for Bicycle Commuters. – The act allows a new transportation fringe benefit for bicycle commuters. In general, commuting expenses to and from a place of business are not deductible. Transportation fringe benefits can defray some of an employee's commuting expenses with either pre-tax dollars that reduce otherwise taxable compensation, or with direct, employer-subsidized amounts that are considered tax free. This act adds qualified bike commuting reimbursements to the

⁶ A senior executive officer is an individual who is one of the top five highly paid executives of a public company whose compensation is required to be disclosed pursuant to the Securities Exchange Act of 1934.

type of qualified transportation fringe benefits that an employer may provide to an employee who commutes to work using a bike.

Extension of certain deductions. –

Deduction for Qualified Tuition and Related Expenses. – The act extends the deduction for qualified tuition and related expenses for tax years beginning before January 1, 2010. The expenses eligible for the deduction include tuition and fees required for the enrollment or attendance of the taxpayer, the taxpayer's spouse, or dependent at an eligible institution of higher education. The maximum deduction is \$4,000 for taxpayers whose AGI does not exceed \$65,000 (\$130,000 for joint filers) and \$2,000 for taxpayers whose AGI does not exceed \$80,000 (\$160,000 for joint filers).

Above-the-Line Deduction for Certain Expenses of School Teachers. – The act extends the above-the-line deduction for eligible educators for tax years beginning in 2008 and 2009. The \$250 deduction is allowed for books, supplies, and computer equipment purchased by an eligible educator for use in the classroom.

Enhanced Deduction for Charitable Contributions of Computers. – The act extends the enhanced deduction for charitable contributions of computers for tax years beginning in 2008 and 2009. C corporations that make qualified contributions of computer technology and equipment may claim an enhanced deduction equal to the corporation's basis in the donated property plus one-half of the ordinary income that would have been realized if the property had been sold. The enhanced deduction may not exceed twice the corporation's basis in the property.

Enhanced Deduction for Charitable Contributions of Food Inventory. – The act extends the enhanced deduction for charitable contributions of food inventory for tax years beginning in 2008 and 2009. Taxpayers may take a deduction for donated food inventory equal to the lesser of (1) the donated item's basis plus one-half of the amount of gain that would be realized if the donated food item was sold at fair market value, or (2) two times the donated item's basis. The deduction is limited to 10% of the taxpayer's net income, however, the 10% limitation is suspended for contributions made by farmers or ranchers between October 3, 2008 and January 1, 2009.

Enhanced Deduction for Charitable Contributions of Book Donations. – The act extends the enhanced deduction for charitable contributions of book donations for tax years beginning in 2008 or 2009. Any corporation, other than an S corporation, can take an enhanced deduction for contributions of book inventory equal to the lesser of (1) the donated inventory item's basis plus one-half of the item's appreciation, or (2) two times the donated inventory item's basis.

Deduction for Environmental Remediation Costs. – The act extends the election to deduct environmental remediation costs to cover expenditures paid or incurred in 2008 and 2009. A taxpayer may elect to deduct certain environmental cleanup costs in the tax year paid or incurred, rather than capitalize them. The election only applies to costs that are incurred in connection with the abatement or control of hazardous substances at a "qualified containment site," also called a "brownfield site."

Deduction for Energy Efficient Commercial Buildings. – The act extends the deduction for energy-efficient commercial building property for five years and is available for qualified property placed into service after December 31, 2005 and before January 1, 2014. The deduction applies to "energy efficient commercial building property," which is defined as depreciable property that is installed as part of a building's (1) interior lighting systems, (2) heating, cooling,

ventilation, and hot water systems, or (3) envelope, and is part of a certified plan to reduce the total annual energy and power costs of these systems by at least 50%. The deduction is limited to the product of \$1.80 and the total square footage of the building, reduced by the aggregate amount deducted in any prior year.

Gain on Sales or Dispositions to Implement FERC or State Electric Restructuring Policy. –

The act extends the special gain recognition rule for qualifying electric transmission transactions that implement FERC or state electric restructuring policy for two years for qualified electric utilities to sales or dispositions prior to January 1, 2010. A qualified electric utility can elect to recognize qualified gain from a qualifying electric transmission transaction over an eight-year period to the extent the amount realized from the sale is used to purchase exempt utility property within an applicable period.

Treatment of RIC Dividends Paid to Foreign Persons. – The act extends the exemption from the 30% tax on regulated investment company (RIC)⁷ dividends that are designated as interest-related or short-term capital gains for two years to tax years beginning before January 1, 2010. Generally, US income paid to a nonresident alien or foreign corporation that is not connected with a US trade or business is subject to a flat 30% tax which is collected through withholding. Dividends that are designated as interest-related or short-term capital gains are exempt from the 30% tax.

15-Year MACRS Recovery period for Qualified Leasehold Improvements, Qualified Restaurant Improvements and Buildings, and Qualified Retail Improvement Property. –

The act extends the 15-year Modified Adjusted Cost Recovery System (MACRS) recovery period for qualified leasehold improvements and restaurant improvements and buildings for two years and applies to property placed in service before January 1, 2009. The act also creates 15-year a MACRS recovery period for qualified retail improvement property and applies to property placed in service after December 31, 2007 and before January 1, 2009. Before these provisions, the improvements would generally be considered a structural component of the building and would be depreciated over a 39 year period.

Tax Treatment of Certain Payments to Controlling Exempt Organizations. – The act extends the special rules that permit the exclusion of qualifying payments by a controlled entity to a tax-exempt organization from that tax exempt organization's unrelated business income (UBTI) for two years through December 31, 2009. Tax-exempt organizations are taxed on UBTI, including amounts paid by a controlled entity. Only the excess amount of certain qualifying payments of rent, royalties, annuities, or interest income is included. Qualifying payments must be made in connection with a contract that is in effect August 17, 2006. Payments that exceed the amount that would be paid in an arms-length transaction are included in the UBTI.

Basis adjustment to stock of S corporations making charitable contributions of property. – The act extends the provision providing that the amount of a shareholder's basis reduction in the stock of an S corporation by reason of a charitable contribution made by the corporation equals the shareholder's pro rata share of the adjusted basis of the contributed property for two years and applies to tax years beginning before January 1, 2009. This change preserves the intended benefit without causing the shareholder to recognize a gain or reduced loss that is attributable to the appreciation upon the subsequent sale of stock.

⁷ A RIC is commonly known as a mutual fund.

Seven-Year Depreciation Period for Motorsports Facilities. – The act extends the 7 year MACRS recovery period for motorsports entertainment complexes to property placed in service in 2008 and 2009. Historically, race tracks and facilities were treated by the IRS the same as theme and amusement parks. The American Jobs Creation Act of 2004 codified this treatment. A "motorsports entertainment complex" is a racing track facility that is permanently situated on land, hosts at least one racing event for cars of any type, trucks, or motorcycles during the 36-month period following the first day of the month in which it is put in service, and is open to the public for an admission fee.

Extend and Modify Treatment of Certain Qualified Film and Television Productions. – The act extends the expensing election related to film and television productions for one year for productions that begin before January 1, 2010, and allows the election to be made, in part, for productions with aggregate costs over the dollar production limit. A taxpayer may deduct the production costs of a qualifying film or television production. To qualify for the election, the aggregate production cost may not exceed \$15 million. This act modifies the provision so that the first \$15 million of otherwise qualifying film or television productions may be treated as an expense even if the aggregate cost of production exceeds \$15 million.

Certain Farming Equipment Business Machinery or Equipment Treated as Five-Year Property. –The act provides that certain machinery or equipment used in a farming business is treated as five-year property for purposes of claiming MACRS depreciation. The equipment does not include grain bins, cotton ginning assets, fences or land improvements. Property that is used in a farming business can be depreciated under the General Depreciation System (GDS) using the 150-percent declining-balance method. Farm machinery and equipment generally has a recovery period of 10 years and has a straight-line recovery method.

Disaster Relief. -

Relief for Midwestern Disaster Areas. – The act modifies and extends many of the tax benefits extended to the victims of Katrina, Wilma, and Rita hurricanes to the victims of storms that hit the Midwest in the summer of 2008. These include the extension of special expensing for qualified property, an enhanced low-income housing credit, and flexible tax-exempt bond financing rules.

Casualty Losses Attributable to Federally Declared Disasters. – The act increases the deduction for casualty losses attributable to federally declared disasters for tax years beginning after December 31, 2007. Personal casualty losses are deductible to the extent the losses exceed \$100 per casualty and the sum of the casualty losses exceed 10% of the taxpayer's AGI. For tax years beginning after December 31, 2007, the standard deduction is increased by the amount of any disaster loss amount for casualty losses attributable to a federally declared disaster occurring in 2008 and 2009. The losses are deductible without regard to whether the losses exceed 10% of a taxpayer's adjusted gross income. The deduction for any casualty attributable to a federally declared disaster occurring in 2009 is limited to the amount of the loss that exceeds \$500.

Expensing of Qualified Disaster Costs. – The act allows a taxpayer to elect to expense qualified disaster expenses after 2007, rather than capitalizing them. Qualified disaster expenses include any expenditure that is all of the following:

- (1) Paid or incurred in connection with a trade, business, or business-related property.
- (2) Otherwise chargeable to a capital account.
- (3) Made for any of the following:

- (a) The abatement or control of hazardous substances that were released on account of a federally declared disaster.
- (b) The removal of debris from, or the demolition of structures on, business-related property that is damaged as the result of a federally declared disaster.
- (c) The repair of business-related property damaged as a result of a federally declared disaster.

Net Operating Losses Attributable to Federally Declared Disasters. – The act creates a special five-year carryback period for net operating losses (NOLs) has been created for a qualified disaster loss. In general, NOLs may be carried back and deducted against taxable income in the two tax years before the NOL year, and then carried forward and applied against taxable income for up to 20 years after the NOL year.

Special Depreciation Allowance for Qualified Disaster Assistance Property. – The act allows an additional 50% depreciation allowance can be claimed for real and personal business property that is purchased to rehabilitate or replace similar property that is destroyed or condemned as a result of a residentially declared disaster for property placed in service after December 31, 2007, with respect to disasters declared after that date and occurring before January 1, 2010.

Increased Expensing for Qualified Disaster Assistance Property. – The act increases the maximum section 179 expense allowance and investment limitation amount for qualified section 179 disaster property placed in service after 2007. In general, a qualifying taxpayer may elect to treat the cost of certain property as an expense and deduct it in the year the property is placed in service instead of depreciating it over several years. This property is frequently referred to as section 179 property, after the relevant section in the Internal Revenue Code. To be eligible, the property must be tangible personal property which is actively used in the taxpayer's business for which a depreciation deduction would be allowed. The property must be used more than 50% for business and must be newly purchased property. Generally, taxpayers take expensing first and claim section 168(k) depreciation on any remaining basis. First year expensing is increased for disaster property:

- (1) The section 179 expense deduction (\$250,000 for 2008) is increased by the lesser of \$100,000 or the cost of the qualified section 170 disaster assistance property placed in service during the tax year.
- (2) The amount of the investment limitation (\$250,000 for 2008) is increased by the lesser of \$600,000 or the cost of qualified section 179 disaster assistance property placed in service during the tax year.

► ***BILL ANALYSIS:*** The bill conforms to the provisions of this act.

Worker, Retiree, and Employer Recovery Act of 2008

Required Minimum Distribution. – The act eliminates the required minimum distribution for calendar year 2009 for individual retirement plans and employer-provided qualified retirement plans that are defined contribution plans. Employer-provided qualified retirement plans and individual retirement accounts are subject to minimum distribution rules. Generally, required minimum distributions must begin by April 1 of the year following the calendar year in which the individual reaches 70 ½. The required minimum distribution for each year is determined by a formula that includes the account balance and the individual and individual's designated beneficiary's expected lifetime. Failure to make a required minimum distribution results in a 50% excise tax.

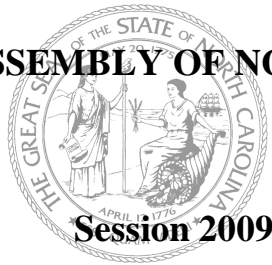
► **BILL ANALYSIS:** The bill conforms to the provisions of this act.

IRS Notice 2008-83

The IRS issued Notice 2008-83 on September 30, 2008. The notice suspends a rule that limits the use of built-in losses of banks following a change in ownership of the bank. Section 382 limits a corporation's ability to deduct its net operating losses against taxable income when the corporation undergoes an ownership change. An ownership change is defined as an increase in the percentage of a corporation's stock owned by one or more 5 percent shareholders by more than 50 percentage points within a 3-year period. After an ownership change, the deduction for the amount of losses attributable to the period before the ownership change is limited. The limit is generally equal to the value of the loss corporation at the time of the change multiplied by the applicable federal long-term tax-exempt interest rate. This notice provides that losses on loans or bad debts will not be limited by section 382 for banks that undergo an ownership change.

► **TECHNICAL CONSIDERATIONS:** The IRS notice is not a legislative change to the Code, rather it is a technical explanation meant to provide guidance on existing provisions of the Code as explained by the Treasury Department. Some practitioners believe this Notice goes beyond guidance on existing provisions and makes substantial changes to the Code. This bill does not address North Carolina's conformity to the provisions of the Notice.

GENERAL ASSEMBLY OF NORTH CAROLINA



FISCAL ANALYSIS MEMORANDUM

[This confidential fiscal memorandum is a fiscal analysis of a draft bill, amendment, committee substitute, or conference committee report that has not been formally introduced or adopted on the chamber floor or in committee. This is not an official fiscal note. If upon introduction of the bill you determine that a formal fiscal note is needed, please make a fiscal note request to the Fiscal Research Division, and one will be provided under the rules of the House and the Senate.]

DATE: January 27, 2009

TO: Revenue Laws Study Committee

FROM: Barry Boardman
Fiscal Research Division

RE: IRC Update

FISCAL IMPACT

| | Yes (X) | No () | No Estimate Available () | | |
|---|-------------------|-------------------|---------------------------|-------------------|-------------------|
| | <u>FY 2009-10</u> | <u>FY 2010-11</u> | <u>FY 2011-12</u> | <u>FY 2012-13</u> | <u>FY 2013-14</u> |
| REVENUES: | | | | | |
| Heartland, Habitat, Harvest, and Horticulture Act of 2008 | (0.5) | (1.0) | (0.8) | (0.5) | (0.5) |
| Heroes Earnings Assistance and Relief Tax Act of 2008 | (0.5) | (0.5) | (0.5) | (0.5) | (0.5) |
| Emergency Economic Stabilization Act of 2008 | | | | | |
| Extensions of Certain Deductions | (9.4) | (18.6) | (8.6) | 0.0 | 0.0 |
| MACRS recovery period and other business expensing | (8.5) | (18.2) | (13.6) | (8.3) | (7.4) |
| Disaster Relief | (7.2) | (16.7) | (15.4) | (5.8) | 3.4 |
| Other | (5.7) | (10.8) | (7.4) | (8.5) | (8.4) |
| EESA TOTAL | (30.9) | (64.3) | (45.0) | (22.7) | (12.5) |
| Workers, Retiree, and Employer Recovery Act 2008 | (36.0) | (44.0) | | | |
| TOTAL | (67.9) | (109.8) | (46.3) | (23.7) | (13.5) |

EXPENDITURES:

POSITIONS

(cumulative):

PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED: Department of Revenue

EFFECTIVE DATE: January 1, 2009

BILL SUMMARY: This proposal would update the reference to the Internal Revenue Code used in defining and determining certain State tax provisions from May 1, 2008 to January 1, 2009. By doing so, North Carolina would conform to the changes made by five federal acts, except the bill would not conform to the new additional standard deduction for real property taxes. This bill would become effective when it became law.

CURRENT LAW: North Carolina's tax law tracks many provisions of the federal Internal Revenue Code by reference to the Code.^{*} The General Assembly determines each year whether to update its reference to the Internal Revenue Code.[†] Updating the Internal Revenue Code reference makes recent amendments to the Code applicable to the State to the extent that State law tracks federal law. The General Assembly's decision whether to conform to federal changes is based on the fiscal, practical, and policy implications of the federal changes and is normally enacted in the following year, rather than in the same year the federal changes are made.

BILL ANALYSIS: *See the Bill Analysis of the preceding summary.*

ASSUMPTIONS AND METHODOLOGY: The methodology used begins with the Joint Tax Committee estimates of the nationwide federal impact by federal fiscal year (Federal fiscal years run from October through September). Fiscal Research adjusted these numbers back to an approximate calendar year tax impact. The next step was to prorate the national numbers to the state impact. The Department of Revenue undertook this process using taxpayer data and North Carolina economic data.

After calculating the estimated State tax year impacts, the numbers were converted to state fiscal year by assuming that the traditional FRD method of putting 45% of a calendar year tax liability in the January-June period that finishes up one fiscal year and the allocating the remainder to the following fiscal year. There were no adjustments made to the Joint Committee on Taxation's estimates based on the level of taxpayer compliance. Therefore, the fiscal estimates assume 100 percent taxpayer compliance with the tax law changes.

^{*} North Carolina first began referencing the Internal Revenue Code in 1967, the year it changed its taxation of corporate income to a percentage of federal taxable income.

[†] The North Carolina Constitution imposes an obstacle to a statute that automatically adopts any changes in federal tax law. Article V, Section 2(1) of the Constitution provides in pertinent part that the "power of taxation ... shall never be surrendered, suspended, or contracted away." Relying on this provision, the North Carolina court decisions on delegation of legislative power to administrative agencies, and an analysis of the few federal cases on this issue, the Attorney General's Office concluded in a memorandum issued in 1977 to the Director of the Tax Research Division of the Department of Revenue that a "statute which adopts by reference future amendments to the Internal Revenue Code would ... be invalidated as an unconstitutional delegation of legislative power."

SOURCES OF DATA: US Joint Committee on Taxation, NC Department of Revenue

TECHNICAL CONSIDERATIONS: None

LEGISLATIVE PROPOSAL #2

CHANGE CORPORATE INCOME TAX

LEGISLATIVE PROPOSAL #2

A RECOMMENDATION OF THE REVENUE LAWS STUDY COMMITTEE
TO THE 2009 REGULAR SESSION OF THE 2009 GENERAL ASSEMBLY

AN ACT TO CHANGE THE CORPORATE INCOME TAX

SHORT TITLE: Change Corporate Income Tax.

SPONSORS:

BRIEF OVERVIEW: This proposal states the intent of the General Assembly to enact changes to the corporate income tax laws that further the goals of equity, simplicity, modernization, and broad base/low rate. The proposal would also replace an antiquated term with the correct defined term.

FISCAL IMPACT:

EFFECTIVE DATE: The proposal would become effective when it becomes law.

A copy of the proposed legislation and a bill analysis begin on the next page.

**GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2009**

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BILL DRAFT 2009-RBxz-9A [v.3] (12/15)

**(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)
1/30/2009 5:34:20 PM**

Short Title: Change Corporate Income Tax.

(Public)

Sponsors: .

Referred to:

A BILL TO BE ENTITLED
AN ACT TO CHANGE THE CORPORATE INCOME TAX.

The General Assembly of North Carolina enacts:

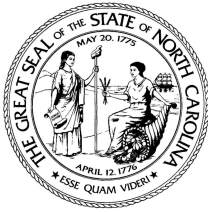
SECTION 1. The General Assembly intends to enact legislation to provide greater equity and certainty in the tax laws that affect businesses to achieve the following tax policy goals:

- (1) Provide a more level playing field for all businesses, both those that operate only in North Carolina and those that operate in multiple states.
- (2) Provide a comprehensive structure to nullify income shifting strategies.
- (3) Modernize the tax laws to adapt to the growth of multi-state corporations.
- (4) Reduce uncertainty about when a corporation needs to file a combined return, who the corporation includes in it, and how the combination is to be accomplished.
- (5) Broaden the corporate income tax base and adjust the tax rate to make the changes revenue-neutral.

SECTION 2. G.S. 105-130.4(h) reads as rewritten:

"(h) The income less related expenses from any other ~~nonbusiness~~ activities producing nonapportionable income or investments not otherwise specified in this section is allocable to this State if the business situs of the activities or investments are located in this State."

SECTION 3. This act is effective when it becomes law.



BILL DRAFT 2009-RBxz-9A: Change Corporate Income Tax

BILL ANALYSIS

| | | | |
|-----------------------|------------------------------|--------------------|------------------|
| Committee: | Revenue Laws Study Committee | Date: | January 28, 2009 |
| Introduced by: | | Summary by: | Cindy Avrette |
| Version: | Draft | | Committee Staff |

SUMMARY: *Draft 2009-RBxz-9A states the intent of the General Assembly to enact changes to the corporate income tax laws that further the goals of equity, simplicity, modernization, and broad base/low rate. The proposal would also replace an antiquated term with the correct defined term. The bill becomes effective when it becomes law.*

CURRENT LAW: To determine its State net taxable income, a corporation must begin with its federal taxable income. Multi-state corporations may file a consolidated federal return. However, under North Carolina law, a corporation may not file a consolidated return unless specifically required to do so by the Secretary of Revenue. North Carolina requires corporations to file as a separate entity, meaning it must determine its State net income as if a separate return had been filed for federal income tax purposes.

Separate entity filing gives corporations with subsidiaries in multiple states the ability to devise ways to shift income from a high effective tax rate state to a low effective tax rate state, often through the use of passive investment companies and inter-company transactions. Over the past several years, the General Assembly has enacted changes to the State's corporate income tax laws to address the shifting of income between states by multistate corporations. Despite the efforts, the problem of income shifting between multistate corporations continues to be an issue.

The Department of Revenue has aggressively used the tools available to it to require a corporation to file a consolidated return when the Department believes the corporation's net income attributable to this State is not accurately reflected on its separate entity filing return. This action by the Department is referred to as 'forced combination'. The Department has used forced combinations for a number of years and it has collected more than \$200 million in taxes from forced combinations.

Taxpayers, seeking clarity on the law, have filed lawsuits contesting the Department's authority to force combinations. G.S. 105-130.6 provides the authority the Department uses to force combinations. Taxpayers express concern that the statute is vague and there are no administrative rules or directives to provide guidance or certainty to taxpayers as to when a combined reporting is required, who is required to be included in the combined report, or how the combination is to be accomplished. Taxpayers believe the statute does not provide any meaningful taxpayer remedies because it says: "*The findings and conclusions of the Secretary shall be presumed to be correct and shall not be set aside unless shown to be plainly wrong.*"

BACKGROUND: The adoption of mandatory combined reporting would address both the issue of income shifting and the issue of the lack of clarity in the law concerning 'forced combinations'. The Revenue Laws Study Committee recommended mandatory combined reporting to the 2007 Session of the General Assembly.¹ Under the recommendation, a corporation that is part of an affiliated group engaged in a single trade or business would file a combined report as opposed to a single entity report. Combined reporting is a method of calculating the income of a group of related corporations for tax

¹ Senate Bill 244 and House Bill 462.

purposes. It looks beyond the legal structure of separate incorporations to determine whether two or more related corporations are engaged in a single unitary business.

The General Assembly did not enact the legislation last biennium because many of the outstanding issues that needed to be addressed by the recommendation were left unresolved. Those issues included the following:

- The percentage reduction by which the corporate income tax rate could be reduced to render the proposal revenue-neutral.
- The relationship between combined reporting and the franchise tax statutes.
- A determination as to what corporations, if any, would be excluded from combined reporting.
- How the income of corporations with special apportionment formulas under the current law would be apportioned under combined reporting.
- Various transitional and administrative issues.

Several prior studies have also recommended that North Carolina require combined reporting. The Governor's Commission to Modernize State Finances recommended moving from single entity reporting to combined reporting as long ago as 2001. In 2007, this Committee, the Income Tax Subcommittee of the State and Local Fiscal Modernization Study Commission, and Governor Easley all recommended this change. The Multistate Tax Commission adopted a model uniform statute for combined reporting in 2006. Twenty-two states² require combined reporting; six of those states have adopted combined reporting since 2004.³

BILL ANALYSIS: The Committee did not want to recommend a proposal to the 2009 General Assembly that did not address the unresolved issues from 2007. However, the Committee remains supportive of legislation that would further the following tax policy goals:

- Provide a more level playing field for all businesses, both those that operate only in North Carolina and those that operate in multiple states.
- Provide a comprehensive structure to nullify income shifting strategies.
- Modernize the tax laws to adapt to the growth of multi-state corporations.
- Reduce uncertainty about when a corporation needs to file a combined return, who the corporation includes in it, and how the combination is to be accomplished.
- Broaden the corporate income tax base and adjust the tax rate to make the changes revenue-neutral.

Section 1 of the proposal states the intent of the General Assembly to enact changes to the corporate income tax laws that further the goals of equity, simplicity, modernization, and broad base/low rate. Section 2 of the proposal would replace an antiquated term with the correct defined term.

The proposal would become effective when it becomes law.

² Alaska, Arizona, California, Colorado, Hawaii, Idaho, Illinois, Kentucky, Maine, Minnesota, Montana, Nebraska, New Hampshire, Massachusetts, Michigan, New York, North Dakota, Oregon, Texas, Utah, West Virginia, and Vermont.

³ Massachusetts, Michigan, New York, Texas, West Virginia, and Vermont.

LEGISLATIVE PROPOSAL #3

STREAMLINED SALES AND USE TAX UPDATE

LEGISLATIVE PROPOSAL #3

A RECOMMENDATION OF THE REVENUE LAWS STUDY COMMITTEE
TO THE 2009 REGULAR SESSION OF THE 2009 GENERAL ASSEMBLY

AN ACT TO URGE THE 111TH CONGRESS TO GRANT STATES THE ABILITY TO REQUIRE COLLECTION OF SALES AND USE TAX BY REMOTE RETAILERS AND TO UPDATE THE REFERENCE TO THE STREAMLINED SALES AND USE TAX AGREEMENT

SHORT TITLE: Streamlined Sales and Use Tax Update.

SPONSORS:

BRIEF OVERVIEW: The proposal would do two things:

- It would encourage the 111th Congress to enact the provisions of the Sales Tax Fairness and Simplification Act (STFSA), which would give states that have adopted the uniformity and simplification measures of the Streamlined Sales and Use Tax Agreement (Agreement) the ability to require collection of use tax by remote sellers.
 - It would update the statutory reference to the Agreement by changing the date from June 23, 2007, to September 5, 2008. North Carolina does not need to amend its sales and use tax laws to conform to any of the changes made in the Agreement since June 23, 2007.
-
-

FISCAL IMPACT: No impact.

EFFECTIVE DATE: This act would become effective when it becomes law.

A copy of the proposed legislation and a bill analysis begin on the next page.

**GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2009**

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BILL DRAFT 2009-RBz-5 [v.6] (01/07)

**(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)
1/26/2009 3:01:20 PM**

Short Title: Streamlined Sales and Use Tax Update. (Public)

Sponsors: .

Referred to:

A BILL TO BE ENTITLED
AN ACT TO URGE THE 111TH CONGRESS TO GRANT STATES THE ABILITY
TO REQUIRE COLLECTION OF SALES AND USE TAX BY REMOTE
RETAILERS AND TO UPDATE THE REFERENCE TO THE STREAMLINED
SALES AND USE TAX AGREEMENT.

The General Assembly of North Carolina enacts:

SECTION 1. The General Assembly strongly encourages Congress to grant states the ability to require collection of sales and use tax by remote retailers by enacting the provisions of the Sales Tax Fairness and Simplification Act, a bipartisan bill introduced in the 110th Congress as H.R. 3396 by Rep. William Delahunt (D-MA) and as S. 34 by Senator Mike Enze (R-WY), for the following reasons:

- (1) As Congress works to develop an economic stimulus package to provide much needed relief to businesses, individuals, and states, the Sales Tax Fairness and Simplification Act would provide tens of billions of dollars in funding to many states and local governments at minimal or no cost to the federal government.
- (2) The Sales Tax Fairness and Simplification Act would ensure a fairer and more equitable sales tax system by requiring all retailers, both Main Street brick-and-mortar retailers and remote retailers, to collect and remit state sales and use taxes.
- (3) Under previous United States Supreme Court decisions, the states' ability to collect sales and use taxes from remote retailers is restricted. However, the Court has stated in its decisions that Congress has the authority to grant states the ability to require collection of sales and use tax by remote retailers.
- (4) In an effort to address the collection issues identified by the United States Supreme Court, North Carolina is one of 22 states that have

1 enacted legislation to simplify their sales and use tax laws to conform
2 to the uniformity requirements of the Streamlined Sales and Use Tax
3 Agreement

- 4 (5) North Carolina has collected thirty-six million dollars (\$36,000,000) in
5 revenues since October 2005 through the voluntary remittance of sales
6 and use taxes by remote sellers under the Streamlined Sales and Use
7 Tax Agreement. This amount is far less than the estimated amount the
8 State is not collecting from sales by remote sellers.

9 **SECTION 2.** G.S. 105-164.3(45a) reads as rewritten:

10 "(45a) Streamlined Agreement. – The Streamlined Sales and Use Tax
11 Agreement as amended as of ~~June 23, 2007.~~September 5, 2008."

12 **SECTION 3.** This act is effective when it becomes law.
13



BILL DRAFT 2009-RBz-5: Streamlined Sales and Use Tax Update

BILL ANALYSIS

Committee: Revenue Laws Study Committee
Introduced by:
Version: Bill Draft

Date:
Summary by: Cindy Avrette
Committee Staff

SUMMARY: *This bill draft would do two things:*

- *It would encourage the 111th Congress to enact the provisions of the Sales Tax Fairness and Simplification Act, which would give states that have adopted the uniformity and simplification measures of the Streamlined Sales and Use Tax Agreement the ability to require collection of use tax by remote sellers.*
- *It would update the statutory reference to the Agreement by changing the date from June 23, 2007, to September 5, 2008. North Carolina does not need to amend any of its sales and use tax laws to conform to any of the changes made in the Agreement since June 23, 2007.*

The bill would become effective when it becomes law.

CURRENT LAW: The Streamlined Sales and Use Tax Project (Project) is entering its ninth year of efforts to provide simplification and uniformity to the administration of sales and use tax. The adoption of the Streamlined Sales and Use Tax Agreement (Agreement) in 2002 provided the framework for participating states to achieve the uniformity and simplification measures initially established by a coalition of states, local governments, and businesses. The goal of the Project is to achieve sufficient simplification and uniformity to encourage sellers without nexus in states to voluntarily collect use tax in those states that have adopted the uniform provisions of the Agreement. Based on decisions by the United States Supreme Court, states cannot require remote sellers that do not have a physical presence in the state to collect and remit its use tax.

North Carolina is one of twenty-two states represented on the Streamlined Sales Tax Governing Board. A state becomes a member of the Governing Board when its sales and use tax laws are found to conform to the uniformity and simplification measures in the Agreement. The Governing Board established a central registration system in October 2005 that allows sellers to register for sales and use tax purposes in all member states. Over 1,000 sellers have registered since the system's inception.

Since October 2005, North Carolina has collected approximately \$36 million in use tax revenue from remote sellers. The State has received \$7.9 million during the 2008-2009 fiscal year to date. The amounts collected voluntarily are far less than the estimated amounts the State is not collecting in use tax revenue from sales by remote sellers. A University of Tennessee study, commissioned a few years ago, estimated a revenue loss to state and local governments of more than \$30 billion a year from uncollected use taxes on remote sales. The Governing Board has recently commissioned a study to provide an update on this estimate.

The United States Supreme Court has stated in its decisions that Congress has the authority to grant states the ability to require collection of sales and use tax by remote sellers. Sen. Mike Enzi (R-WY) and Rep. William Delahunt (D-MA) introduced a bipartisan bill in the 110th Congress to provide the

necessary authorization to those states that had adopted the simplification and uniformity measures established in the Agreement. Although Congress did not enact the legislation last biennium, the Governing Board believes that the 111th Congress may represent the best opportunity for action on the Streamlined-related legislation, known as the Sales Tax Fairness and Simplification Act (STFSA). The National Conference of State Legislatures has recommended that Congress include the provisions of the STFSA as part of the economic stimulus legislation it is working to develop. The provisions of the STFSA would provide tens of billions of dollars in funding to states and local governments at a minimal or no cost to the federal government.

BILL ANALYSIS: The Revenue Laws Study Committee recognizes this year may be the best opportunity for action by Congress on the STFSA. Section 1 of the proposal would encourage Congress to consider and implement the provisions of the STFSA. The proposal provides both policy and fiscal reasons to support the enactment of the legislation. Not only would the legislation ensure a fairer and more equitable sales tax system for both Main Street brick-and-mortar retailers and remote retailers, but also

Section 2 of the proposal would update the State's statutory reference to the Agreement from June 23, 2007, to September 5, 2008. North Carolina does not need to amend its sales and use tax laws to conform to the changes made in the Agreement since June 23, 2007. A copy of the Agreement, as well as a document summarizing the changes made to the Agreement since June 23, 2007, may be found on the Streamlined Sales Tax Project's website: www.streamlinedsalestax.org.

LEGISLATIVE PROPOSAL #4

REAL PROPERTY SALES INFORMATION

LEGISLATIVE PROPOSAL #4

A RECOMMENDATION OF THE REVENUE LAWS STUDY COMMITTEE
TO THE 2009 REGULAR SESSION OF THE 2009 GENERAL ASSEMBLY

**AN ACT TO ASSIST COUNTIES AND THE DEPARTMENT OF REVENUE
IN OBTAINING ACCURATE REAL PROPERTY SALES INFORMATION
NEEDED FOR PROPERTY TAX APPRAISALS BY REQUIRING A REPORT
OF SALES INFORMATION WHEN REAL PROPERTY IS TRANSFERRED.**

SHORT TITLE: Real Property Sales Information.

SPONSORS:

BRIEF OVERVIEW: This proposal would assist the counties and Department of Revenue in obtaining the true value or market value of real property for property tax appraisal purposes by requiring that a sales information report be filed with the county whenever property changes hands.

FISCAL IMPACT:

EFFECTIVE DATE: This act would become effective January 1, 2010.

A copy of the proposed legislation and bill analysis begin on the next page.

**GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2009**

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BILL DRAFT 2009-LAz-5 [v.4] (1/6)

**(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)
1/7/2009 8:56:13 AM**

Short Title: Real Property Sales Information. (Public)

Sponsors: .

Referred to:

A BILL TO BE ENTITLED
AN ACT TO ASSIST COUNTIES AND THE DEPARTMENT OF REVENUE IN
OBTAINING ACCURATE REAL PROPERTY SALES INFORMATION NEEDED
FOR PROPERTY TAX APPRAISALS BY REQUIRING A REPORT OF SALES
INFORMATION WHEN REAL PROPERTY IS TRANSFERRED.

Whereas, the Constitution of North Carolina requires that property must be taxed by uniform rule and that every classification must be made by general law uniformly applicable in every county, city and town, and other unit of local government; and

Whereas, the North Carolina General Statutes require that all property, real and personal, must so far as practicable be appraised or valued at its true value which is interpreted as meaning market value; and

Whereas, taxes levied by all counties and municipalities must be levied uniformly on assessments determined by the true value of most property; and

Whereas, to help ensure that tax values of real property reflect fair market value when the counties value their property for property tax purposes, the North Carolina Department of Revenue must conduct annual studies of the ratio of the appraised value of real property to its true value and establish for each county the median ratio as determined by the study for each calendar year; and

Whereas, one of the most accurate and cost efficient methods of producing a fair revaluation of property based on the true value of the property is to require that sales information reports be filed with the county whenever property changes hands; Now, therefore,

The General Assembly of North Carolina enacts:

SECTION 1. Article 19 of Chapter 105 of the General Statutes is amended by adding a new section to read:

1 **"§ 105-317.2. Report on transfers of real property.**

2 To facilitate the accurate appraisal of real property for taxation, the information listed
3 in this section must be reported to the county tax assessor on a form developed by the
4 Department of Revenue. G.S. 161-32 prohibits recording a deed until the report is filed.
5 The following information is required:

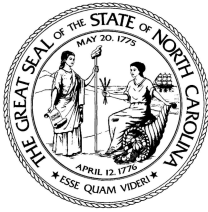
- 6 (1) The name of each grantor and grantee.
7 (2) A brief description of the property.
8 (3) The total sales price.
9 (4) Whether the transaction involves family members or affiliated
10 companies.
11 (5) A listing of any personal property conveyed with the transaction.
12 (6) Whether the transaction is the result of a forced sale."

13 **SECTION 2.** Article 2 of Chapter 161 of the General Statutes is amended by
14 adding a new section to read:

15 **"§ 161-32. Report on transfer of real property.**

16 The register of deeds may not accept for registration a deed transferring real property
17 unless the county tax assessor certifies that a sales information report required by G.S.
18 105-317.2 has been filed. Failure to comply with this section does not affect the validity
19 of a duly recorded deed."

20 **SECTION 3.** This act becomes effective January 1, 2010.
21
22
23



BILL DRAFT 2009-LAz-5: Real Property Sales Information

BILL ANALYSIS

| | | | |
|-----------------------|------------------------------|--------------------|-------------------|
| Committee: | Revenue Laws Study Committee | Date: | January 27, 2009 |
| Introduced by: | | Summary by: | Martha Walston |
| Version: | Draft | | Committee Counsel |

SUMMARY: *This proposal would assist the counties and Department of Revenue in obtaining the true value or market value of real property for property tax appraisal purposes by requiring that a sales information report be filed with the county whenever property changes hands.*

CURRENT LAW: Real property must be appraised for property tax purposes at least every eight years. The appraisal value must be its market or true value as of January 1 of the year of the general reappraisal.¹ Market or true value is the price at which property would change hands between a willing and financially able buyer and willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of all the uses to which property is adapted and for which it is capable of being used. To assist the counties in determining the true value, the Department of Revenue conducts yearly sales assessment ratio studies for each county. These studies compare the appraised value of parcels with the sales price. The closer the comparison is to 100%, the closer the property's appraised value is to the fair market value. Consequently, more frequent reappraisal schedules lessen the discrepancy between the appraised value of the property and the true value of the property.

Prior to the 2008 Session, the Revenue Laws Study Committee adopted a proposal to change the eight year appraisal cycle to a four year cycle. The version of this proposal ratified in S.L. 2008-146 requires advancement of the eight year schedule only for a county with a population of 75,000 or greater and when the sales assessment ratio for that county drops below .85 or becomes greater than 1.15.² For these counties, new values must be implemented by January 1 of the third year following notice by the Department of the sales assessment ratio study. All other counties retain the eight-year schedule.

BILL ANALYSIS: This bill would require that the following information be reported to and certified by the county tax assessor before a deed transferring property may be accepted by the county's register of deeds:

1. The name of each grantor and grantee.
2. A brief description of the property.
3. The total sales price.
4. Whether the transaction involves family members or affiliated companies.
5. A listing of any personal property conveyed with the transaction.
6. Whether the transaction is the result of a forced sale.

The above information would be reported on a form developed by the Department of Revenue.

¹ The following types of property are appraised at their use value: farmland, working waterfront property, and wildlife conservation property.

² Based upon the 2007 population estimates and 2008 sales ratios, only ten counties are affected by the 2008 legislation.

This proposed statewide sales information report is supported by comments made during meetings with tax assessors from large urban counties and smaller rural counties. Staff from the Revenue Laws Study Committee and the Property Tax Division within the Department of Revenue recently made field trips to the tax offices of Mecklenburg County and Chowan County. There they met with the tax assessors from those counties and surrounding counties to get the assessors' input on advancing the property tax appraisal schedule. The counties agreed that the advantage of advancing the schedule is that the appraised value of the property will be more equivalent to the fair market value of the property. However, the smaller more rural counties pointed out that revaluations are expensive and that they do not have the manpower or revenue to conduct them. The group discussed several recommendations to help them meet the statutory fair market appraisal standard. They concluded that one of the most helpful and cost efficient recommendations would be to require a statewide sales information report. They felt that the information on these reports could be used to generate a sales information list which would certainly help the counties obtain appraisal values that are closer to the true value of the property in the counties. Based upon information compiled by the Department of Revenue, 50 counties are already sending out letters requesting information to confirm a property transfer and six counties are requiring a transfer affidavit.³

EFFECTIVE DATE: This proposal would become effective January 1, 2010.

³ Five of the six counties that require an affidavit also assess a local land transfer tax. They are Camden, Chowan, Currituck, Dare, and Pasquotank.

LEGISLATIVE PROPOSAL #5

**MODERNIZE SALES TAX STATUTES/
DIGITAL PRODUCTS**

LEGISLATIVE PROPOSAL #5

A RECOMMENDATION OF THE REVENUE LAWS STUDY COMMITTEE
TO THE 2009 REGULAR SESSION OF THE 2009 GENERAL ASSEMBLY

**AN ACT TO MODERNIZE THE SALES AND USE TAX STATUTES BY
TREATING MUSIC, MOVIES, COMPUTER SOFTWARE, AND BOOKS
THAT ARE DELIVERED ELECTRONICALLY THE SAME AS THOSE THAT
ARE PURCHASED IN A TANGIBLE MEDIUM AND BY REVISING THE
"MAIL ORDER" SALES TAX PROVISION TO INCLUDE SPECIFIC
REFERENCES TO INTERNET SALES.**

SHORT TITLE: Modernize Sales Tax Statutes/Digital Products.

SPONSORS:

BRIEF OVERVIEW: This proposal would apply the State and local general rate of sales and use tax audio works, audiovisual works, books, and computer software that are delivered or accessed electronically to the extent those items would be taxable if sold in a tangible medium. It also revises the "mail order sales" provision by setting out specifically circumstances under which remote retailers are presumed to be soliciting business in this State for purposes of collecting sales tax.

FISCAL IMPACT: This proposal is estimated to generate in FY 2009-2010 a General Fund gain of \$8.4 million and a gain of \$3.7 million in local revenues.

EFFECTIVE DATE: The revisions to the mail order sale provisions become effective when the act becomes law. The remainder of the act becomes effective January 1, 2010, and applies to sales made on or after that date.

A copy of the proposed legislation, bill analysis, and fiscal analysis begin on the next page.

**GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2009**

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BILL DRAFT 2009-SVxz-5 [v.8] (01/23)

**(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)
1/29/2009 10:26:45 AM**

Short Title: Modernize Sales Tax Stat/Digital Products.

(Public)

Sponsors: .

Referred to:

A BILL TO BE ENTITLED
AN ACT TO MODERNIZE THE SALES AND USE TAX STATUTES BY TREATING
MUSIC, MOVIES, BOOKS, AND COMPUTER SOFTWARE THAT ARE
DELIVERED ELECTRONICALLY THE SAME AS THOSE THAT ARE
PURCHASED IN A TANGIBLE MEDIUM AND BY REVISING THE "MAIL
ORDER" SALES TAX PROVISIONS TO INCLUDE SPECIFIC REFERENCES TO
INTERNET SALES.

The General Assembly of North Carolina enacts:

SECTION 1. G.S. 105-164.3 reads as rewritten:

"§ 105-164.3. Definitions.

The following definitions apply in this Article:

...

(1b) Audio work. – A series of musical, spoken, or other sounds, including a
ringtone.

(1c) Audiovisual work. – A series of related images and any sounds
accompanying the images, that impart an impression of motion when
shown in succession.

~~(1b)~~(1d) Bundled transaction. – A retail sale of two or more distinct and
identifiable products, at least one of which is taxable and one of which
is exempt, for one nonitemized price. Products are not sold for one
nonitemized price if an invoice or another sales document made
available to the purchaser separately identifies the price of each product.
A bundled transaction does not include the retail sale of any of the
following:

a. A product and any packaging item that accompanies the product
and is exempt under G.S. 105-164.13(23).

b. A sale of two or more products whose combined price varies, or
is negotiable, depending on the products the purchaser selects.

- 1 c. A sale of a product accompanied by a transfer of another product
2 with no additional consideration.
3 d. A product and the delivery or installation of the product.
4 e. A product and any service necessary to complete the sale.

5 ~~(1d)~~(1e)Business. – Includes any activity engaged in by any person or caused
6 to be engaged in by him with the object of gain, profit, benefit or
7 advantage, either direct or indirect. The term "business" shall not be
8 construed in this Article to include occasional and isolated sales or
9 transactions by a person who does not hold himself out as engaged in
10 business.

11 ...
12 (7a) Digital code. – A code that gives a purchaser of the code a right to
13 receive electronic delivery an item by electronic delivery or electronic
14 access. A digital code may be obtained by an electronic means or by
15 tangible means. A digital code does not include a gift certificate or a gift
16 card.

17 ~~(7a)~~(7h)Direct mail. – Printed material delivered or distributed by the United
18 States Postal Service or other delivery service to a mass audience or to
19 addresses on a mailing list provided by the purchaser or at the direction
20 of the purchaser when the cost of the items is not billed directly to the
21 recipients. The term includes tangible personal property supplied
22 directly or indirectly by the purchaser to the direct mail seller for
23 inclusion in the package containing the printed material. The term does
24 not include multiple items of printed material delivered to a single
25 address.

26 ...
27 ~~(17a)~~ ~~Load and leave. – Delivery to the purchaser by use of a tangible storage~~
28 ~~media where the tangible storage media is not physically transferred to~~
29 ~~the purchaser.~~

30 ...
31 (35f) Ringtone. – A digitized sound file that is downloaded onto a device and
32 that may be used to alert the user of the device with respect to a
33 communication.

34 ..."

35 **SECTION 2.** G.S. 105-164.4(a) reads as rewritten:

36 "(a) A privilege tax is imposed on a retailer at the following percentage rates of the
37 retailer's net taxable sales or gross receipts, as appropriate. The general rate of tax is four
38 and one-half percent (4.5%).

39 ...
40 (6b) The general rate applies to the sales price of an item that is listed in this
41 subdivision, is delivered or accessed electronically, and would be
42 taxable under this Article if sold in a tangible medium. The retail sale of
43 a digital code that is used to obtain any of the items taxed by this
44 subdivision is considered a sale of that item. The tax applies regardless

1 of whether the purchaser of the item has a right to redistribute it, to use
2 it permanently, or to use it without making continued payments. The tax
3 does not apply to an item that is taxed under another subdivision of this
4 subsection or under G.S. 105-164.4C. A person who sells an item that is
5 taxable under this subdivision is considered a retailer under this Article.
6 The following items are subject to tax under this subdivision:

- 7 a. An audio work.
8 b. An audiovisual work.
9 c. A book.
10 d. Computer software."

11 **SECTION 3.(a)** G.S. 105-164.3(18) is recodified as G.S. 105-164.3(33g) and
12 reads as rewritten:

13 "~~(18)~~(33g) Mail-order-Remote sale. – A sale of tangible personal
14 property, ordered by mail, by telephone, computer link, via the Internet,
15 or other similar method, to a purchaser who is in this State at the time
16 the order is remitted, from a retailer who receives the order in another
17 state and transports the property or causes it to be transported to a
18 person in this State. It is presumed that a resident of this State who
19 remits an order was in this State at the time the order was remitted."

20 **SECTION 3.(b)** The catchline of G.S. 105-164.8 reads as rewritten:

21 "**§ 105-164.8. Retailer's obligation to collect tax; mail-order-remote sales subject to**
22 **tax."**

23 **SECTION 3.(c)** G.S. 105-164.8(b) reads as rewritten:

24 "(b) Mail-Order-Remote Sales. – A retailer who makes a mail-order-remote sale is
25 engaged in business in this State and is subject to the tax levied under this Article if at
26 least one of the following conditions is met:

- 27 (1) The retailer is a corporation engaged in business under the laws of this
28 State or a person domiciled in, a resident of, or a citizen of, this State.
29 (2) The retailer maintains retail establishments or offices in this State,
30 whether the mail-order-remote sales thus subject to taxation by this State
31 result from or are related in any other way to the activities of such
32 establishments or offices.
33 (3) The retailer ~~has representatives in this State who solicit business or~~
34 ~~transact business on behalf of the retailer,~~ solicits or transacts business
35 in this State by employees, independent contractors, agents, or other
36 representatives whether the mail-order-remote sales ~~thus~~ subject to
37 taxation by this State result from or are related in any other way to ~~such~~
38 the solicitation or transaction of business. A retailer is presumed to be
39 soliciting or transacting business by an independent contractor, agent, or
40 other representative if the retailer enters into an agreement with a
41 resident of this State under which the resident, for a commission or
42 other consideration, directly or indirectly refers potential customers,
43 whether by a link on an Internet website or otherwise, to the retailer, if
44 the cumulative gross receipts from sales by the retailer to purchasers in

1 this State who are referred to the retailer by all residents with this type
2 of agreement with the retailer is in excess of ten thousand dollars
3 (\$10,000.00) during the preceding four quarterly periods. This
4 presumption may be rebutted by proof that the resident with whom the
5 retailer has an agreement did not engage in any solicitation in the State
6 on behalf of the seller that would satisfy the nexus requirement of the
7 United States Constitution during the four quarterly periods in question.

8 (4) Repealed by Session Laws 1991, c. 45, s. 16.

9 (5) The retailer, by purposefully or systematically exploiting the market
10 provided by this State by any media-assisted, media-facilitated, or
11 media-solicited means, including direct mail advertising, distribution of
12 catalogs, computer-assisted shopping, television, radio or other
13 electronic media, telephone solicitation, magazine or newspaper
14 advertisements, or other media, creates nexus with this State.

15 (6) Through compact or reciprocity with another jurisdiction of the United
16 States, that jurisdiction uses its taxing power and its jurisdiction over the
17 retailer in support of this State's taxing power.

18 (7) The retailer consents, expressly or by implication, to the imposition of
19 the tax imposed by this Article. For purposes of this subdivision,
20 evidence that a retailer engaged in the activity described in subdivision
21 (5) shall be prima facie evidence that the retailer consents to the
22 imposition of the tax imposed by this Article.

23 (8) The retailer is a holder of a wine shipper permit issued by the ABC
24 Commission pursuant to G.S. 18B-1001.1."

25 **SECTION 4.** G.S. 105-164.13(43a) is repealed.

26 **SECTION 5.** G.S. 105-467(a) is amended by adding a new subdivision to

27 read:

28 "(8) The sales price of an audio work, audiovisual work, a book, and
29 computer software that is subject to the general rate of tax under
30 G.S. 105-164.4(a)(6b)."

31 **SECTION 6.** Section 4 of Chapter 1096 of the 1967 Session Laws, as
32 amended, reads as rewritten:

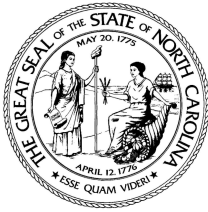
33 "Sec. 4. Scope of Sales Tax. The sales tax which may be imposed under this division
34 after the holding of a special election is limited to a tax at the rate of one per cent (1%)
35 of: (1) the sale price of those articles of tangible personal property now subject to the
36 general rate of sales tax imposed by the State under G. S. ~~105-164.4(a)(1) and (4b);~~
37 105-164.4(a)(1), (4b), and (6b); (2) the gross receipts derived from the lease or rental of
38 tangible personal property when the lease or rental of the property is subject to the
39 general rate of sales tax imposed by the State under G.S. 105-164.4(a)(2); (3) the gross
40 receipts derived from the rental of any room or lodging furnished by any hotel, motel,
41 inn, tourist camp or other similar public accommodations now subject to the general rate
42 of sales tax imposed by the State under G. S. 105-164.4(a)(3); (4) the gross receipts
43 derived from services rendered by laundries, dry cleaners, cleaning plants and similar
44 type businesses now subject to the general rate of sales tax imposed by the State under G.

1 S. 105-164.4(a)(4); (5) The sales price of food and other items that are not otherwise
2 exempt from tax pursuant to G.S. 105-164.13 but are exempt from the State sales and use
3 tax pursuant to G.S. 105-164.13B; and (6) The sales price of prepaid telephone calling
4 service taxed as tangible personal property under G.S. 105-164.4(a)(4d). The taxes
5 authorized by this division do not apply to sales that are taxable by the State under
6 G.S. 105-164.4 but are not specifically listed in this section.

7 "The exemptions and exclusions contained in G.S. 105-164.13 and the sales and use
8 tax holiday contained in G.S. 105-164.13C apply with equal force and like manner to the
9 local sales tax authorized to be imposed and levied under this division. The county shall
10 have no authority, with respect to the local sales and use tax imposed under this division,
11 to change, alter, add, or delete any exemptions or exclusions contained under
12 G.S. 105-164.13.

13 "The local sales tax authorized to be imposed and levied under the provisions of this
14 division shall be applicable to such retail sales, leases, rentals, rendering of services,
15 furnishing of lodging or accommodations and other taxable transactions which are made,
16 furnished or rendered by retailers whose place of business is located within the taxing
17 county. The tax imposed shall apply to the furnishing of rooms, lodging or other
18 accommodations within the county which are rented to transients. The sourcing principles
19 in G.S. 105-164.4B apply in determining whether the local sales tax applies to a
20 transaction. Provided, however, no tax shall be imposed where the tangible personal
21 property sold is delivered by the retailer or his agent to the purchaser at a point outside
22 this State."

23 **SECTION 7.** Section 3 of this act is effective when it becomes law. The
24 remainder of this act becomes effective January 1, 2010, and applies to sales made on or
25 after that date.
26



DRAFT 2009-SVxz-5: Modernize Sales Tax Statutes/Digital Products

BILL ANALYSIS

| | | | |
|-----------------------|-------------------------------|--------------------|-------------------|
| Committee: | Revenue Laws Study Committee | Date: | January 27, 2009 |
| Introduced by: | | Summary by: | Trina Griffin |
| Version: | Draft Proposal 2009-SVxz-5 | | Committee Counsel |

SUMMARY: *This legislative proposal would apply the State and local general rate of sales and use tax to audio works (music and ringtones), audiovisual works (movies), books, and computer software that are delivered or accessed electronically to the extent those items would be taxable if sold in a tangible medium. The draft also revises the mail order sale statute to specifically set out certain circumstances that constitute soliciting business in this State for purposes of requiring a remote retailer to collect sales tax.*

CURRENT LAW: Under current law, the general rate of State and local sales and use tax applies to the sale, lease, or rental of tangible personal property and some services. Tangible personal property is defined as "personal property that may be seen, weighed, measured, felt, or touched, or is in any other manner perceptible to the senses." Digital goods, such as downloaded music and movies, are not tangible personal property, and, therefore, are not taxed. Prewritten computer software is specifically included within the definition of tangible personal property, but it is exempt from sales tax when it is delivered electronically or by load and leave.¹

G.S. 105-164.8 sets out the circumstances under which a "remote" retailer is required to collect sales tax on mail order sales. Generally speaking, a remote retailer is one that does not maintain a "brick and mortar" establishment in this State. This statute reflects principles enunciated in a series of cases that set out circumstances under which a retailer has sufficient nexus with a state to require it to collect sales tax. Several of these cases involved businesses that used independent contractors or other commissioned agents to solicit orders in a state in which the business was not physically located. One of the leading cases in this area is *Scripto v. Carson*, in which the United States Supreme Court held that a state could require tax collection by a remote retailer that had contracts with 10 in-state residents deemed independent contractors who solicited orders for products on its behalf. This principle has been codified in G.S. 105-164.8, which states, in part, that a retailer who makes a mail order sale must collect the sales tax if:

"The retailer has representatives in this State who solicit business or transact business on behalf of the retailer, whether the mail order sales thus subject to taxation by this State result from or are related in any other way to such solicitation or transaction of business."

BILL ANALYSIS: This proposal does the following three things:

- It applies the general rate of State and local sales tax to certain digital goods when the tangible equivalent of the good would be subject to sales tax.
- It eliminates the sales and use tax exemption on prewritten computer software delivered electronically or via load and leave.

¹ The term "load and leave" is defined as "delivery to the purchaser by use of a tangible storage media where the tangible storage media is not physically transferred to the purchaser."

- It revises the "mail order sale" provision by modernizing the terminology and by providing that a retailer is presumed to be soliciting business in this State when it enters into certain commission agreements with in-State residents and the contractual arrangement generates in excess of \$10,000 in sales to the retailer.

The proposal imposes the general rate of sales and use tax on audio works, audiovisual works, books, and computer software that is delivered or accessed electronically and that would be taxable if purchased in a tangible format. The tax applies regardless of whether the purchaser has a right to redistribute it, to use it permanently, or to use it without making continued payments. The tax does not apply to a product that is taxed under another sales tax provision or the telecommunications statute. The purchase of a digital code used to obtain one of these items is considered a sale of that item.

The proposal also revises the mail order sales provision in two ways. First, it changes the term "mail order sale" to "remote sale," which covers all transactions that are not "face-to-face" but reflects more modern terminology and the prevalence of Internet sales. Second, it provides that a retailer is presumed to solicit or transact business in this State and is, therefore, required to collect sales tax if all of the following conditions are met:

4. The retailer has entered into an agreement with a resident of this State.
5. Under the agreement, the resident receives a commission or other consideration in exchange for directly or indirectly referring potential customers, whether by a link on an Internet website or otherwise, to the retailer.
6. The cumulative gross receipts from sales by the retailer to purchasers in this State who are referred to the retailer by all residents with this type of agreement with the retailer is in excess of \$10,000 during the preceding four quarterly periods.

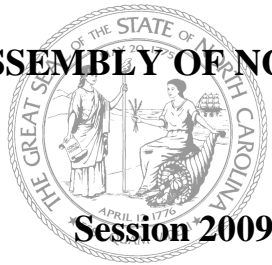
This presumption may be rebutted by proof that the resident with whom the retailer has an agreement did not engage in any solicitation in the State on behalf of the retailer that would satisfy the nexus requirement of the United States Constitution.

In a recent New York Supreme Court² case, Amazon challenged an identical provision in the New York sales tax statutes alleging that it violates the Commerce Clause of the United States Constitution as well as both the Federal and State Constitutions' Due Process and Equal Protection Clauses. The court dismissed the complaint for failure to state a cause of action. The court disagreed with Amazon's assertion that the commissioned agents were mere advertisers concluding that the provision requires tax collection only when an out-of-state seller avails itself of the benefit of in-state contractors who are compensated for referrals and who generate actual business for the seller. Moreover, the court stated that "Amazon should not be permitted to escape tax collection indirectly, through use of an incentivized New York sales force to generate revenue, when it would not be able to achieve tax avoidance directly through the use of New York employees engaged in the very same activities."

EFFECTIVE DATE: Section 3, which revises the mail order provisions, becomes effective when the act becomes law. The remainder of the act becomes effective January 1, 2010, and applies to sales made on or after that date.

² The New York Supreme Court is a trial-level court.

GENERAL ASSEMBLY OF NORTH CAROLINA



FISCAL ANALYSIS MEMORANDUM

[This confidential fiscal memorandum is a fiscal analysis of a draft bill, amendment, committee substitute, or conference committee report that has not been formally introduced or adopted on the chamber floor or in committee. This is not an official fiscal note. If upon introduction of the bill you determine that a formal fiscal note is needed, please make a fiscal note request to the Fiscal Research Division, and one will be provided under the rules of the House and the Senate.]

DATE: January 27, 2009

TO: 2009 Revenue Laws Study Committee

FROM: Sandra Johnson
Fiscal Research Division

RE: Modernize Sales Tax Statutes/Digital Products

FISCAL IMPACT (\$ In Millions)

| | Yes (X) | No () | No Estimate Available () | | |
|--|-------------------|-------------------|---------------------------|-------------------|-------------------|
| | <u>FY 2009-10</u> | <u>FY 2010-11</u> | <u>FY 2011-12</u> | <u>FY 2012-13</u> | <u>FY 2013-14</u> |

REVENUES:

| | | | | | |
|--------------|--------|-----|------|------|------|
| General Fund | \$ 3.7 | 9.2 | 10.2 | 11.3 | 12.7 |
| Local Impact | \$1.7 | 4.1 | 4.5 | 5.1 | 5.7 |

EXPENDITURES:

POSITIONS

(cumulative):

PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED: North Carolina
Department of Revenue

EFFECTIVE DATE: January 1, 2010

BILL SUMMARY: The proposed legislation does the following three things:

- Applies the general rate of State and local sales tax to certain digital goods when the tangible equivalent of the good would be subject to sales tax.

- Eliminates the sales and use tax exemption on prewritten computer software delivered electronically or via load and leave.
- Revises the "mail order sale" provision by modernizing the terminology and by providing that a retailer is presumed to be soliciting business in this State when it enters into certain commission agreements with in-State residents and the contractual arrangement generates in excess of \$10,000 in sales to the retailer.

The proposal imposes the general rate of sales and use tax on audio works, audiovisual works, books, and computer software that is delivered or accessed electronically and that would be taxable if purchased in a tangible format. The tax applies regardless of whether the purchaser has a right to redistribute it, to use it permanently, or to use it without making continued payments. The tax does not apply to a product that is taxed under another sales tax provision or the telecommunications statute. The purchase of a digital code used to obtain one of these items is considered a sale of that item.

ASSUMPTIONS AND METHODOLOGY: Fiscal Research estimates that North Carolina's digital download sales during the 2009-10 fiscal year will generate roughly \$3.7 million in State tax revenue. The outline below reviews the data sources and methodology used to estimate digital download sales tax revenue for each of the six products: 1) music, 2) video games, 3) movies and other filmed entertainment, 4) books, 5) computer software via digital download and 6) computer software provided through load and leave services.

It is important to note that the \$3.7 million is estimated tax revenue given a, January 1st, mid-fiscal year effective date. The \$3.7 million figure is solely based on the projected sales by vendors with a North Carolina nexus. In determining nexus versus non-nexus sales, the California Board of Equalization estimates that 65% of E-commerce sales are from vendors with nexus, a brick and mortar affiliation, in the state. The remaining 35% of E-commerce sales, according to the Board, are by out-of-state vendors and require individual purchasers to remit a use tax. Use taxes, the tax revenue from sales by vendors outside of the state, if remitted, would increase General Fund availability by an additional \$3.7 million for a total of \$5.4 million in FY 2009-10. Use taxes from online purchases are reported at a minimal rate.

To estimate North Carolina's digital download sales, Fiscal Research made state level inferences from national retail trends. North Carolina's retail sales represented roughly 3% of the nation's retail sales during the most recent Economic Census in 2002.

Music

If enacted for a full fiscal year, North Carolina's digital music sales would generate roughly \$1.6 million in tax revenue in 2009-2010. Assuming that the State represents 2.9% of all U.S. retail sales and a 16% annual growth rate, this figure would represent \$2.9 million by 2013.

The International Federation of the Phonographic Industry (IFPI), Digital Music Report 2009 estimates that international music sales via online and mobile channels rose from zero to \$3.7 billion within six years, making music more digitally advanced than any entertainment sector except games. Digital music now accounts for roughly 20 percent of all music sales and the 2009 IFPI report cites the U.S. as the world's biggest digital music market. America's online and mobile music sales account for \$1.9 billion or 50% of international revenues.

The U.S. Census, in addition to a state level economic census every five years, tracks the nation's annual retail sales including E-commerce and mail order sales. Mail-order and E-commerce music sales

increased by 16% between 2005 and 2006. The fiscal estimate assumes a 16% percent annual growth rate in digital music sales based on the 2005-2006 trend.

Video Games

North Carolina's digital gaming industry is expected to generate roughly \$2.7 million in sales tax revenue per fiscal year, a figure that is expected to grow by 6.3% annually representing \$3.5 million dollars in 2013. This fiscal estimate is based on information provided by the 2008 IFPI Music Industry report and PricewaterhouseCoopers' *Global Entertainment and Media Outlook: 2008-2012* report.

According to PricewaterhouseCoopers, the U.S. video game industry is being driven by the next generation of platforms, online and wireless games. The video and online gaming industry represented \$8.6 billion in 2007 and will increase at an average annual rate of 6.3 percent to \$11.7 billion in 2012. While PricewaterhouseCoopers projects \$11.7 billion in overall video game sales, the IFPI Digital Music Report 2008, estimates that digital downloads represents \$4 billion, 35 percent, of the video game industry.

Movies and Other Filmed Entertainment

Data on digitally downloaded filmed entertainment also comes from the PricewaterhouseCoopers' *Global Entertainment and Media Outlook: 2008-2012* report. The report states that, "Download-to-own movies streamed over the Internet will increase rapidly from a small base, rising at a compound annual growth rate of 51.4 percent equaling \$900 million in 2012, in the U.S." In North Carolina, digitally downloaded movies will generate approximately \$0.21 million in sales tax revenue per fiscal year.

Books

North Carolina's digital book sales are expected to generate \$0.4 million tax revenue per fiscal year. Digital browsing and electronic books, according to PricewaterhouseCoopers, will revitalize the consumer book market, with consumer print books increasing from \$21.7 billion in 2007 to \$22.5 billion in 2012. PricewaterhouseCoopers also projects that the consumer and educational book market will grow by 0.8% annually. IFPI estimates that, \$434 million, or roughly 2% of all book sales are in the form of digital media.

Computer Software

According the U.S. Census E-stats program, Americans purchased roughly \$2 billion in computer software through online vendors in 2006 an increase from \$1.5 billion in 2004. Between 2004 and 2006, online computer software purchases increased at rate of 12% annually. Using historical online commerce growth rates and assuming that 80 percent of online computer software purchases are digitally downloaded, North Carolina can expect to collect roughly \$2.5 million in tax revenue from digital computer software sales.

Computer Software provided through Load and Leave

The digital download legislation would also repeal the sales and use tax exemption for computer software included in G.S. 164.13 (43a). The statute currently exempts software delivered electronically or by load and leave from the sales and use tax. A repeal of G.S. 164.13 (43a) would generate roughly \$1.3 million in tax revenue per fiscal year.

SOURCES OF DATA:

California Board of Equalization. "Revenue Estimate: Electronic Commerce and Mail Order Sales. 2007." Available at: <http://www.boe.ca.gov/legdiv/pdf/e-commerce-07.pdf>

Condon, Stephanie. "States May Tax i-Tunes, Other Digital Downloads." CNET.com. Published August 12, 2008. Available at: http://news.cnet.com/8301-13578_3-10013327-38.html. Last accessed January 2009.

International Federation of the Phonographic Industry (IFPI). *Digital Music Report 2008*. Available at: <http://www.ifpi.org/content/library/DMR2008.pdf>.

International Federation of the Phonographic Industry (IFPI). *Digital Music Report 2009*. January 2009. Available at: <http://www.ifpi.org/content/library/DMR2009.pdf>.

PricewaterhouseCoopers. *Global Entertainment and Media Outlook: 2008-2012*, Available at: <http://www.pwc.com/extweb/pwcpublications.nsf/docid/5AC172F2C9DED8F5852570210044EEA7?opendocument&vendor=none>.

U.S. Census. E-Stats Program. Table 6. "U.S. Electronic Shopping and Mail-Order Houses (NAICS 4541) - Total and E-commerce Sales by Merchandise Line: 2006 and 2005." Available at: <http://www.census.gov/eos/www/2006/2006tables.html>. Last accessed January 2009.

TECHNICAL CONSIDERATIONS: None

LEGISLATIVE PROPOSAL #6

**REVENUE LAWS TECHNICAL, CLARIFYING, AND
ADMINISTRATIVE CHANGES**

LEGISLATIVE PROPOSAL #6

A RECOMMENDATION OF THE REVENUE LAWS STUDY COMMITTEE
TO THE 2009 REGULAR SESSION OF THE 2009 GENERAL ASSEMBLY

AN ACT TO MAKE TECHNICAL, CLARIFYING, AND ADMINISTRATIVE CHANGES TO THE TAX AND RELATED LAWS.

SHORT TITLE: Revenue Laws Technical, Clarifying, and Administrative Law Changes.

SPONSORS:

BRIEF OVERVIEW: This legislative proposal makes several technical, clarifying, and administrative changes to the revenue laws and related statutes.

FISCAL IMPACT:

EFFECTIVE DATE: Except as otherwise specifically provided, the act is effective when it becomes law.

A copy of the proposed legislation and a bill analysis begin on the next page.

**GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2009**

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BILL DRAFT 2009-SVz-4 [v.10] (12/31)

**(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)
1/30/2009 10:51:44 AM**

Short Title: Rev Laws Technical & Admin Changes.

(Public)

Sponsors: .

Referred to:

A BILL TO BE ENTITLED
AN ACT TO MAKE TECHNICAL, CLARIFYING, AND ADMINISTRATIVE
CHANGES TO THE TAX AND RELATED LAWS.

The General Assembly of North Carolina enacts:

SECTION 1. G.S. 105-41(a) reads as rewritten:

"(a) Every individual in this State who practices a profession or engages in a business and is included in the list below must obtain from the Secretary a statewide license for the privilege of practicing the profession or engaging in the business. A license required by this section is not transferable to another person. The tax for each license is fifty dollars (\$50.00).

...

(12) A home inspector or an associate home inspector licensed under Article 9F of Chapter 143 of the General Statutes."

SECTION 2. G.S. 105-130.4(h) reads as rewritten:

"(h) The income less related expenses from any other ~~nonbusiness~~ activities producing nonapportionable income or investments not otherwise specified in this section is allocable to this State if the business situs of the activities or investments are located in this State."

SECTION 3. G.S. 105-130.18 reads as rewritten:

"§ 105-130.18. Failure to file returns; supplementary returns.

If the Secretary determines that a corporation has failed to file a return or to include in a return filed, either intentionally or through error, items of taxable income, the Secretary may require from the corporation a return or supplementary return, under affirmation, of all the items of income that the corporation received during the year for which the return is made, whether or not taxable under this Part. If from a supplementary return or otherwise the Secretary finds that any items of income, taxable under this Part, have been omitted from the original return, that any items returned as taxable are not taxable, or that any item of taxable income is overstated or understated,

1 the Secretary may require that the item be disclosed under affirmation of the
2 corporation, and be added to or deducted from the original return. The filing of a
3 supplementary return and the correction of the original return does not relieve the
4 corporation from any of the penalties under G.S. 105-236. The Secretary may proceed
5 under the provisions of G.S. ~~105-241.1, 105-241.9,~~ whether or not the Secretary
6 requires a return or a supplementary return under this section."

7 **SECTION 4.** Section 4(b) of S.L. 2008-134 reads as rewritten:

8 "SECTION 4.(b) This section is effective for taxable years beginning on or
9 after January 1, ~~2009-2008.~~"

10 **SECTION 5.(a)** G.S. 105-228.5B reads as rewritten:

11 "**§ 105-228.5B. (Effective until June 30, 2010) Proceeds credited to High Risk Pool.**

12 ~~Within 75 days after the end of each fiscal year, By November 1 of each year, the~~
13 State Treasurer must transfer from the General Fund to the North Carolina Health
14 Insurance Risk Pool Fund established in G.S. 58-50-225 an amount equal to the growth
15 in net revenue from the tax applied to gross premiums under G.S. 105-228.5(d)(2). The
16 growth in revenue from this tax is the difference between the amount of revenue
17 collected during the preceding fiscal year on premiums taxed under that subdivision less
18 \$475,545,413, which is the amount of revenue collected during fiscal year 2006-2007
19 on premiums taxed under that subdivision. The Treasurer must draw the amount
20 required under this section from revenue collected on premiums taxed under that
21 subdivision."

22 **SECTION 5.(b)** G.S. 105-228.5B, as amended by S.L. 2008-118, reads as
23 rewritten:

24 "**§ 105-228.5B. (Effective June 30, 2010) Distribution of part of tax proceeds to**
25 **High Risk Pool.**

26 ~~Within 75 days after the end of each fiscal year, By November 1 of each year, the~~
27 State Treasurer must transfer from the General Fund to the North Carolina Health
28 Insurance Risk Pool Fund established in G.S. 58-50-225 an amount equal to thirty
29 percent (30%) of the growth in revenue from the tax applied to gross premiums under
30 G.S. 105-228.5(d)(2). The growth in revenue from this tax is the difference between the
31 amount of revenue collected during the preceding fiscal year on premiums taxed under
32 that subdivision less \$475,545,413, which is the amount of revenue collected during
33 fiscal year 2006-2007 on premiums taxed under that subdivision. The Treasurer must
34 draw the amount required under this section from revenue collected on premiums taxed
35 under that subdivision."

36 **SECTION 5.(c)** Subsections (a) and (c) of this section are effective when
37 they become law. Subsection (b) of this section becomes effective June 30, 2010.

38 **SALES TAX CHANGES**

39 **SECTION 6.(a)** G.S. 105-164.14(j)(2)n. reads as rewritten:

40 "n. Solar electricity generating materials manufacturing. Solar
41 ~~energy~~ electricity generating materials manufacturing means the
42 development and production of one or more of the following:
43

1. Photovoltaic materials or modules used in producing electricity.
2. Polymers or polymer films primarily intended for incorporation into photovoltaic materials or modules used in producing electricity."

SECTION 6.(b) This section is effective July 1, 2008, and applies to purchases made on or after that date.

SECTION 7. G.S. 105-187.51C(c) reads as rewritten:

"(c) Forfeiture. – If the required level of investment to qualify as an eligible datacenter is not timely made, then the rate provided under this section is forfeited. If the required level of investment is timely made but any eligible machinery and equipment is not located and used at an eligible datacenter, then the rate provided for that machinery and equipment under this subdivision is forfeited. A taxpayer that forfeits a rate under this subdivision is liable for all past sales and use taxes avoided as a result of the forfeiture, computed at the combined general rate from the date the taxes would otherwise have been due, plus interest at the rate established under G.S. ~~405-241.1(i)~~-105-241.21. If the forfeiture is triggered due to the lack of a timely investment required by this section, then interest is computed from the date the sales or use tax would otherwise have been due. For all other forfeitures, interest is computed at the combined general rate from the time as of which the machinery or equipment was put to a disqualifying use. A credit is allowed against the sales or use tax owed as a result of the forfeiture provisions of this subsection for privilege taxes paid pursuant to this section. For purposes of applying this credit, the fact that payment of the privilege tax occurred in a period outside the statute of limitations provided under G.S. ~~405-266~~ 105-241.6 shall not be considered. Interest shall not be computed against the amount of taxes offset by this credit. The past taxes and interest are due 30 days after the date of forfeiture. A taxpayer that fails to pay the past taxes and interest by the due date is subject to the provisions of G.S. 105-236."

PROPERTY TAX CHANGES

SECTION 8.(a) G.S. 105-273(6) reads as rewritten:

"(6) Corporation. – An organization having capital stock represented by shares or an incorporated, nonprofit organization."

SECTION 8.(b) G.S. 105-277.1B(i) reads as rewritten:

"(i) Disqualifying Events. – Each of the following constitutes a disqualifying event:

- (1) The owner transfers the residence. Transfer of the residence is not a disqualifying event if (i) the owner transfers the residence to a co-owner of the residence or, as part of a divorce proceeding, to his or her spouse and (ii) that individual occupies or continues to occupy the property as his or her permanent residence.
- (2) The owner dies. Death of the owner is not a disqualifying event if (i) the owner's share passes to a co-owner of the residence or to his or her

1 spouse ~~residence~~ and (ii) that individual occupies or continues to
2 occupy the property as his or her permanent residence.

3 (3) The owner ceases to use the property as a permanent residence."

4 **SECTION 9.(a)** G.S. 105-282.1(a)(1) reads as rewritten:

5 "(1) No application required. – Owners of the following exempt or
6 excluded property do not need to file an application for the exemption
7 or exclusion to be entitled to receive it:

8 a. Property exempt from taxation under G.S. 105-278.1 or
9 G.S. 105-278.2.

10 b. Special classes of property excluded from taxation under
11 G.S. 105-275(15), (16), (26), (31), (32a), (33), (34), (37), (40),
12 ~~or (42).~~(42), or (44).

13 c. Property classified for taxation at a reduced valuation under
14 G.S. 105-277(g) or G.S. 105-277.9."

15 **SECTION 9.(b)** This section is effective for taxes imposed for taxable years
16 beginning on or after July 1, 2008.

17 **SECTION 10.** G.S. 105-275 reads as rewritten:

18 **"§ 105-275. Property classified and excluded from the tax base.**

19 The following classes of property are ~~hereby~~ designated special classes under
20 ~~authority of~~ Article V, Sec. 2(2), of the North Carolina Constitution and ~~shall not be~~
21 ~~listed, appraised, assessed, or taxed~~ are excluded from tax as provided in this section if
22 they satisfy the application requirements in G.S. 105-282.1.

23"

24 **SECTION 11.(a)** G.S. 105-277.1(d) reads as rewritten:

25 **"§ 105-277.1. (Effective for taxes imposed for taxable years beginning before July**
26 **1, 2009) Property tax homestead exclusion.**

27 ...

28 (d) Multiple Ownership. – A permanent residence owned and occupied by
29 husband and wife as tenants by the entirety is entitled to the full benefit of this exclusion
30 notwithstanding that only one of them meets the age or disability requirements of this
31 section. When a permanent residence is owned and occupied by two or more persons
32 other than husband and wife as tenants by the entirety and one or more of the owners
33 qualifies for this exclusion, each qualifying owner is entitled to the full amount of the
34 exclusion not to exceed his or her proportionate share of the valuation of the property.
35 No part of an exclusion available to one co-owner may be claimed by any other
36 co-owner and in no event may the total exclusion allowed for a permanent residence
37 exceed the exclusion amount provided in this section.

38 **SECTION 11.(b)** G.S. 105-277.1(d) and (e) read as rewritten:

39 **"§ 105-277.1. (Effective for taxes imposed for taxable years beginning on or after**
40 **July 1, 2009) Elderly or disabled property tax homestead exclusion.**

41 ...

42 (d) Ownership by ~~Spouses.~~ Tenants by the Entirety. – A permanent residence
43 owned and occupied by husband and wife as tenants by the entirety is entitled to the full

benefit of this exclusion notwithstanding that only one of them meets the age or disability requirements of this section.

(e) Other Multiple Owners. – This subsection applies to co-owners who are not husband and ~~wife~~ wife as tenants by the entirety. Each co-owner of a permanent residence must apply separately for the exclusion allowed under this section.

When one or more co-owners of a permanent residence qualify for the exclusion allowed under this section and none of the co-owners qualifies for the exclusion allowed under G.S. 105-277.1C, each co-owner is entitled to the full amount of the exclusion allowed under this section. The exclusion allowed to one co-owner may not exceed the co-owner's proportionate share of the valuation of the property, and the amount of the exclusion allowed to all the co-owners may not exceed the exclusion allowed under this section.

When one or more co-owners of a permanent residence qualify for the exclusion allowed under this section and one or more of the co-owners qualify for the exclusion allowed under G.S. 105-277.1C, each co-owner who qualifies for the exclusion under this section is entitled to the full amount of the exclusion. The exclusion allowed to one co-owner may not exceed the co-owner's proportionate share of the valuation of the property, and the amount of the exclusion allowed to all the co-owners may not exceed the greater of the exclusion allowed under this section and the exclusion allowed under G.S. 105-277.1C."

SECTION 12. G.S. 105-277.1B reads as rewritten:

"§ 105-277.1B. (Effective for taxes imposed for taxable years beginning on or after July 1, 2009) Property tax homestead circuit breaker.

(a) Classification. – A permanent residence owned and occupied by a qualifying owner is designated a special class of property under Article V, Section 2(2) of the North Carolina Constitution and is taxable in accordance with this section.

(b) Definitions. – The definitions provided in G.S. 105-277.1 apply to this section. 'Deferred taxes' means the principal amount of tax deferred under this section.

(c) Income Eligibility Limit. – The income eligibility limit provided in G.S. 105-277.1(a2) applies to this section.

(d) Qualifying Owner. – For the purpose of qualifying for the property tax homestead circuit breaker under this section, a qualifying owner is an owner who meets all of the following requirements as of January 1 preceding the taxable year for which the benefit is claimed:

- (1) The owner has an income for the preceding calendar year of not more than one hundred fifty percent (150%) of the income eligibility limit specified in subsection (c) of this section.
- (2) The owner has ~~owned and~~ occupied the property as a permanent residence for at least five ~~years~~ years and has owned the property as a permanent residence for at least five consecutive years.
- (3) The owner is at least 65 years of age or totally and permanently disabled.
- (4) The owner is a North Carolina resident.

(e) Multiple Owners. – A permanent residence owned and occupied by husband and wife as tenants by the entirety is entitled to the full benefit of the property tax homestead circuit breaker notwithstanding that only one of them meets the length of occupancy ~~occupation~~ requirement and the age or disability requirement of this section. When a permanent residence is owned and occupied by two or more persons other than husband and ~~wife~~, wife as tenants by the entirety, no property tax homestead circuit breaker is allowed unless all of the owners qualify and elect to defer taxes under this section.

(f) Tax Limitation. – A qualifying owner may defer the portion of tax imposed on his or her permanent residence if it exceeds the percentage of the qualifying owner's income set out in the table in this subsection. If a permanent residence is subject to tax by more than one taxing unit and the total tax liability exceeds the tax limit imposed by this section, then both the taxes due under this section and the taxes deferred under this section must be apportioned among the taxing units based upon the ratio each taxing unit's tax rate bears to the total tax rate of all units.

| Income Over | Income Up To | Percentage |
|--------------------------|----------------------------------|-------------------|
| -0- | Income Eligibility Limit | 4.0% |
| Income Eligibility Limit | 150% of Income Eligibility Limit | 5.0% |

(g) Temporary Absence. – An otherwise qualifying owner does not lose the benefit of this circuit breaker because of a temporary absence from his or her permanent residence for reasons of health, or because of an extended absence while confined to a rest home or nursing home, so long as the residence is unoccupied or occupied by the owner's spouse or other dependent.

(h) Deferred Taxes. – The difference between the taxes due under this section and the taxes that would have been payable in the absence of this section are a lien on the real property of the taxpayer as provided in G.S. 105-355(a). The difference in taxes for the three fiscal years preceding the ~~current~~ tax year in which a disqualifying event occurs shall be carried forward in the records of the taxing unit or units as deferred taxes. The deferred taxes are due and payable in accordance with G.S. 105-277.1F when the property loses its eligibility for deferral because of the occurrence of a disqualifying event as provided in subsection (i) of this section. On or before September 1 of each year, the collector shall ~~notify each residence owner to whom a tax deferral has previously been granted of the accumulated sum of deferred taxes and interest~~ send to the mailing address of a residence on which taxes have been deferred a notice stating the amount of deferred taxes and interest that are due and payable upon the occurrence of a disqualifying event.

(i) Disqualifying Events. – Each of the following constitutes a disqualifying event:

- (1) The owner transfers the residence. Transfer of the residence is not a disqualifying event if (i) the owner transfers the residence to a co-owner of the residence or, as part of a divorce proceeding, to his or her spouse and (ii) that individual occupies or continues to occupy the property as his or her permanent residence.

1 (2) The owner dies. Death of the owner is not a disqualifying event if (i)
2 the owner's share passes to a co-owner of the residence or to his or her
3 spouse ~~residence~~ and (ii) that individual occupies or continues to
4 occupy the property as his or her permanent residence.

5 (3) The owner ceases to use the property as a permanent residence.

6 (j) Gap in Deferral. – If an owner of a residence on which taxes have been
7 deferred under this section is not eligible for continued deferral for a tax year, the three
8 years for which the deferred taxes deferred from the prior tax years are carried forward
9 are not due and payable ~~but are carried forward~~ until a disqualifying event occurs. If the
10 owner of the residence qualifies for deferral after one or more years in which he or she
11 did not qualify for deferral, the years in which the owner did not qualify are disregarded
12 in determining the three years for which the deferred taxes are carried forward.

13 (k) **(Repealed effective for taxes imposed for taxable years beginning on or**
14 **after July 1, 2008)** Prepayment. – All or part of the deferred taxes and accrued interest
15 may be paid to the tax collector at any time. Any partial payment is applied first to
16 accrued interest. A residence owner to whom a tax deferral has previously been granted
17 may revoke the application for deferral at any time by notifying the assessor in writing.

18 (l) Creditor Limitations. – A mortgagee or trustee that elects to pay any tax
19 deferred by the owner of a residence subject to a mortgage or deed of trust does not
20 acquire a right to foreclose as a result of the election. Except for requirements dictated
21 by federal law or regulation, any provision in a mortgage, deed of trust, or other
22 agreement that prohibits the owner from deferring taxes on property under this section
23 is void.

24 (m) Construction. – This section does not affect the attachment of a lien for
25 personal property taxes against a tax-deferred residence.

26 (n) Application. – An application for property tax relief provided by this section
27 should be filed during the regular listing period, but may be filed and must be accepted
28 at any time up to and through June 1 preceding the tax year for which the relief is
29 claimed. Persons may apply for this property tax relief by entering the appropriate
30 information on a form made available by the assessor under G.S. 105-282.1"

31 **SECTION 13. G.S. 105-277.1C reads as rewritten:**

32 **"§ 105-277.1C. (Effective for taxes imposed for taxable years beginning on or after**
33 **July 1, 2009) Disabled veteran property tax homestead exclusion.**

34 (a) Exclusion. – A permanent residence owned and occupied by an owner who is
35 a North Carolina resident and who is an honorably discharged disabled veteran or the
36 unmarried surviving spouse of an honorably discharged disabled veteran is designated a
37 special class of property under Article V, Section 2(2) of the North Carolina
38 Constitution and is taxable in accordance with this section. The first forty-five thousand
39 dollars (\$45,000) of appraised value of the residence is excluded from taxation. An
40 owner who receives an exclusion under this section may not receive other property tax
41 relief.

42 (b) Definitions. – The following definitions apply in this section:

43 (1) Disabled veteran. – A veteran who, as of January 1 preceding the
44 taxable year for which the exclusion allowed by this section is

1 claimed, ~~receives~~ received benefits under 38 U.S.C. § 2101 or has a
2 veteran's disability certification.

3 (2) Owner. – Defined in G.S. 105-277.1.

4 (3) Permanent residence. – Defined in G.S. 105-277.1.

5 (4) Property tax relief. – Defined in G.S. 105-277.1.

6 (5) Veteran. – A veteran of any branch of the Armed Forces of the United
7 States.

8 (6) Veteran's disability certification. – A certification by the United States
9 Department of Veterans Affairs or another federal agency that a
10 veteran has a permanent total disability that is service-connected.

11 (c) Temporary Absence. – An owner does not lose the benefit of this exclusion
12 because of a temporary absence from his or her permanent residence for reasons of
13 health or because of an extended absence while confined to a rest home or nursing
14 home, so long as the residence is unoccupied or occupied by the owner's spouse or other
15 dependent.

16 (d) Ownership by ~~Spouses~~ Tenants by the Entirety. – A permanent residence
17 owned and occupied by husband and wife as tenants by the entirety is entitled to the full
18 benefit of this exclusion notwithstanding that only one of them meets the requirements
19 of this section.

20 (e) Other Multiple Owners. – This subsection applies to co-owners who are not
21 husband and ~~wife~~ wife as tenants by the entirety. Each co-owner of a permanent
22 residence must apply separately for the exclusion allowed under this section.

23 When one or more co-owners of a permanent residence qualify for the exclusion
24 allowed under this section and none of the co-owners qualifies for the exclusion allowed
25 under G.S. 105-277.1, each co-owner is entitled to the full amount of the exclusion
26 allowed under this section. The exclusion allowed to one co-owner may not exceed the
27 co-owner's proportionate share of the valuation of the property, and the amount of the
28 exclusion allowed to all the co-owners may not exceed the exclusion allowed under this
29 section.

30 When one or more co-owners of a permanent residence qualify for the exclusion
31 allowed under this section and one or more of the co-owners qualify for the exclusion
32 allowed under G.S. 105-277.1, each co-owner who qualifies for the exclusion allowed
33 under this section is entitled to the full amount of the exclusion. The exclusion allowed
34 to one co-owner may not exceed the co-owner's proportionate share of the valuation of
35 the property, and the amount of the exclusion allowed to all the co-owners may not
36 exceed the greater of the exclusion allowed under this section and the exclusion allowed
37 under G.S. 105-277.1.

38 (f) Application. – An application for the exclusion allowed under this section
39 should be filed during the regular listing period, but may be filed and must be accepted
40 at any time up to and through June 1 preceding the tax year for which the exclusion is
41 claimed. An applicant for an exclusion under this section must establish eligibility for
42 the exclusion by providing a copy of the veteran's disability certification or evidence of
43 benefits received under 38 U.S.C. § 2101."

44 **SECTION 14.** G.S. 105-282.1(a) reads as rewritten:

1 "(a) Application. – Every owner of property claiming exemption or exclusion
2 from property taxes under the provisions of this Subchapter has the burden of
3 establishing that the property is entitled to it. If the property for which the exemption or
4 exclusion is claimed is appraised by the Department of Revenue, the application shall be
5 filed with the Department. Otherwise, the application shall be filed with the assessor of
6 the county in which the property is situated. An application must contain a complete and
7 accurate statement of the facts that entitle the property to the exemption or exclusion
8 and must indicate the municipality, if any, in which the property is located. Each
9 application filed with the Department of Revenue or an assessor shall be submitted on a
10 form approved by the Department. Application forms shall be made available by the
11 assessor and the Department, as appropriate.

12 Except as provided below, an owner claiming an exemption or exclusion from
13 property taxes must file an application for the exemption or exclusion annually during
14 the listing period.

15 (1) No application required. – Owners of the following exempt or
16 excluded property do not need to file an application for the exemption
17 or exclusion to be entitled to receive it:

- 18 a. Property exempt from taxation under G.S. 105-278.1 or G.S.
19 105-278.2.
20 b. Special classes of property excluded from taxation under G.S.
21 105-275(15), (16), (26), (31), (32a), (33), (34), (37), (40), ~~or~~
22 ~~(42)-(42), or (44).~~
23 c. Property classified for taxation at a reduced valuation under
24 G.S. 105-277(g) or G.S. 105-277.9.

25 (2) **(Effective for taxes imposed for taxable years beginning before**
26 **July 1, 2009)** Single application required. – An owner of one or more
27 of the following properties eligible to be exempted or excluded from
28 taxation must file an application for exemption or exclusion to receive
29 it. Once the application has been approved, the owner does not need to
30 file an application in subsequent years unless new or additional
31 property is acquired or improvements are added or removed,
32 necessitating a change in the valuation of the property, or there is a
33 change in the use of the property or the qualifications or eligibility of
34 the taxpayer necessitating a review of the exemption or exclusion:

- 35 a. Property exempted from taxation under G.S. 105-278.3,
36 105-278.4, 105-278.5, 105- 278.6, 105-278.7, or 105-278.8.
37 b. Special classes of property excluded from taxation under G.S.
38 105-275(3), (7), (8), (12), (17), (18), (19), (20), (21), (31e),
39 (35), (36), (38), (39), ~~or (41)(41), or (45)~~ or under G.S.
40 131A-21.
41 c. Special classes of property classified for taxation at a reduced
42 valuation under G.S. 105-277(h), 105-277.1, 105-277.10,
43 105-277.13, 105-278.

d. Property owned by a nonprofit homeowners' association but where the value of the property is included in the appraisals of property owned by members of the association under G.S. 105-277.8.

(2) **(Effective for taxes imposed for taxable years beginning on or after July 1, 2009 and before July 1, 2010)** Single application required. – An owner of one or more of the following properties eligible for a property tax benefit must file an application for the benefit to receive it. Once the application has been approved, the owner does not need to file an application in subsequent years unless new or additional property is acquired or improvements are added or removed, necessitating a change in the valuation of the property, or there is a change in the use of the property or the qualifications or eligibility of the taxpayer necessitating a review of the benefit.

a. Property exempted from taxation under G.S. 105-278.3, 105-278.4, 105-278.5, 105-278.6, 105-278.7, or 105-278.8.

b. Special classes of property excluded from taxation under G.S. 105-275(3), (7), (8), (12), (17), (18), (19), (20), (21), (31e), (35), (36), (38), (39), ~~or (41)~~(41).or (45) or under G.S. 131A-21.

c. Special classes of property classified for taxation at a reduced valuation under G.S. 105-277(h), 105-277.1, 105-277.1C, 105-277.10, 105-277.13, 105-277.14, or 105-278.

d. Property owned by a nonprofit homeowners' association but where the value of the property is included in the appraisals of property owned by members of the association under G.S. 105-277.8.

e. Repealed by Session Laws 2008-35, s. 1.2, effective for taxes imposed for taxable years beginning on or after July 1, 2008.

(2) **(Effective for taxes imposed for taxable years beginning on or after July 1, 2010)** Single application required. – An owner of one or more of the following properties eligible for a property tax benefit must file an application for the benefit to receive it. Once the application has been approved, the owner does not need to file an application in subsequent years unless new or additional property is acquired or improvements are added or removed, necessitating a change in the valuation of the property, or there is a change in the use of the property or the qualifications or eligibility of the taxpayer necessitating a review of the benefit.

a. Property exempted from taxation under G.S. 105-278.3, 105-278.4, 105-278.5, 105-278.6, 105-278.7, or 105-278.8.

b. Special classes of property excluded from taxation under G.S. 105-275(3), (7), (8), (12), (17), (18), (19), (20), (21), (31e),

(35), (36), (38), (39), ~~or (41)~~(41), or (45) or under G.S. 131A-21.

- c. Special classes of property classified for taxation at a reduced valuation under G.S. 105-277(h), 105-277.1, 105-277.1C, 105-277.10, 105-277.13, ~~105-278, or 105-277.15.~~105-277.14, 105-277.15, or 105-278.
- d. Property owned by a nonprofit homeowners' association but where the value of the property is included in the appraisals of property owned by members of the association under G.S. 105-277.8.
- e. Repealed by Session Laws 2008-35, s. 1.2, effective for taxes imposed for taxable years beginning on or after July 1, 2008."

SECTION 15. G.S. 105-277.14(d) is repealed.

SECTION 16. G.S. 105-361(a) reads as rewritten:

(a) Duty to Furnish a Certificate. – On the request of any of the persons prescribed in subdivision (a)(1), below, and upon the condition prescribed by subdivision (a)(2), below, the tax collector shall furnish a written certificate stating the amount of any taxes and special assessments owed for the current year and for any prior years in his hands for collection (together with any penalties, interest, and costs accrued thereon) including the amount due under G.S. 105-277.4(e) if the property should lose its eligibility for the benefit of classification under G.S. 105-277.2 et seq. that are a lien on a parcel of real property in the taxing unit. years. The certificate shall include deferred taxes that are due and payable because of the occurrence of a disqualifying event.

- (1) Who May Make Request. – Any of the following persons shall be entitled to request the certificate:
 - a. An owner of the real property;
 - b. An occupant of the real property;
 - c. A person having a lien on the real property;
 - d. A person having a legal interest or estate in the real property;
 - e. A person or firm having a contract to purchase or lease the property or a person or firm having contracted to make a loan secured by the property;
 - f. The authorized agent or attorney of any person described in subdivisions (a)(1)a through e above."

OCCUPANCY TAX CHANGES

SECTION 17. Section 1 of S.L. 2008-33 reads as rewritten:

"**SECTION 1.** Chapter 1055 of the 1983 Session ~~Laws~~Laws, as amended by Section 21(e) of S.L. 2007-527, reads as rewritten:

'Section 1. ~~Levy of Tax.~~Occupancy Tax. –

1 (a) Authorization and scope. – The Cherokee County Board of Commissioners
2 may by resolution, after not less than 10 days' public notice and after a public hearing
3 held pursuant thereto, levy a room occupancy and tourism development tax.

4 (b) ~~Collection of the tax, and liability therefor, shall begin and continue only on~~
5 ~~and after the first day of a calendar month set by the Cherokee County Board of~~
6 ~~Commissioners in the resolution levying the tax, which in no case may be earlier than~~
7 ~~the first day of the second succeeding calendar month after the date of adoption of the~~
8 ~~resolution.~~

9 'Sec. 2. Occupancy Tax.

10 (a) ~~The county room occupancy and tourism development tax that may be levied~~
11 ~~under this act shall be a percentage tax of three percent (3%) of the gross receipts~~
12 ~~derived from the rental of any room, lodging, or similar accommodation furnished by~~
13 ~~any hotel, motel, inn, tourist camp, or other similar place within the county now that is~~
14 ~~subject to the three percent (3%) sales tax imposed by the State under~~
15 ~~G.S. 105-164.4(3). 105-164.4(a)(3). During the first year in which a tax levied under~~
16 ~~this act is in effect, the tax shall be three percent (3%) of the gross receipts derived from~~
17 ~~the rental of taxable accommodations in the county. Thereafter, the rate of tax shall~~
18 ~~continue to be three percent (3%) unless the Cherokee County Board of Commissioners,~~
19 ~~by resolution, adopts a rate of less than three percent (3%). A change in the occupancy~~
20 ~~tax rate adopted by the board of commissioners becomes effective the first day of the~~
21 ~~second succeeding calendar month following the date of adoption of the resolution. The~~
22 ~~Cherokee County Board of Commissioners may not change the occupancy tax rate more~~
23 ~~than once a year.~~

24 (b) ~~The occupancy tax is in addition to any State or local sales tax. This tax does~~
25 ~~not apply to accommodations furnished by nonprofit charitable, educational,~~
26 ~~benevolent, or religious organizations.~~

27 (b) Authorization of additional tax. – In addition to the tax authorized by
28 subsection (a) of this section, the Cherokee County Board of Commissioners may levy
29 an additional room occupancy tax of up to three percent (3%) of the gross receipts
30 derived from the rental of accommodations taxable under subsection (a) of this section.
31 The levy, collection, administration, and repeal of the tax authorized by this subsection
32 shall be in accordance with the provisions of this act. Cherokee County may not levy a
33 tax under this subsection unless it also levies the tax authorized under subsection (a) of
34 this section.

35 'Sec. 3. Administration of Tax. – A tax levied under this act shall be levied,
36 collected, administered, and repealed as provided in G.S. 153A-155. The penalties
37 provided in G.S. 153A-155 apply to a tax levied under this act.

38 (a) ~~Any tax levied under this act is due and payable to the county in monthly~~
39 ~~installments on or before the 20th day of the month following the month in which the~~
40 ~~tax accrues. Every person, firm, corporation, or association liable for the tax shall, on or~~
41 ~~before the 20th day of each month, prepare and render a return on a form prescribed by~~
42 ~~the county. The return shall state the total gross receipts derived in the preceding month~~
43 ~~from rentals upon which the tax is levied.~~

1 (b) Any person, firm, corporation, or association who fails or refuses to file the
2 return required by this act shall pay a penalty of ten dollars (\$10.00) for each day's
3 omission.

4 (c) In case of failure or refusal to file the return or pay the tax for a period of 30
5 days after the time required for filing the return or for paying the tax, there shall be an
6 additional tax, as a penalty, of five percent (5%) of the tax due in addition to the penalty
7 prescribed in subsection (b), with an additional tax of five percent (5%) for each
8 additional month or fraction thereof until the occupancy tax is paid.

9 (d) Any person who willfully attempts in any manner to evade the occupancy tax
10 imposed by this act or to make a return and who willfully fails to pay the tax or make
11 and file a return shall, in addition to all other penalties provided by law, be guilty of a
12 misdemeanor and shall be punishable by a fine not to exceed one thousand dollars
13 (\$1,000), imprisonment not to exceed six months, or both.

14 'Sec. 4. Collection of Tax. Every operator of a business subject to the tax levied
15 pursuant to this act shall collect the tax on and after the effective date of the levy of the
16 tax.

17 This tax shall be collected as part of the charge for the furnishing of any taxable
18 accommodations. The tax shall be stated and charged separately from the sales records,
19 and shall be paid by the purchaser to the operator of the business as trustee for and on
20 account of Cherokee County. The room occupancy tax levied under this act shall be
21 added to the sales price and shall be passed on to the purchaser instead of being borne
22 by the operator of the business. The county shall design, print, and furnish to all
23 appropriate businesses in the county the necessary forms for filing returns and
24 instructions to ensure the full collection of the tax.

25 'Sec. 5. ~~Disposition of Taxes Collected.~~ Distribution and use of tax revenue. –
26 Cherokee County shall ~~shall~~, on a quarterly basis, remit the net proceeds of ~~all revenues~~
27 ~~received from the room occupancy tax to the Cherokee County Tourism Development~~
28 Authority. ~~Authority appointed pursuant to this act. The Authority shall use at least~~
29 two-thirds of the funds remitted to it under this act to promote travel and tourism in
30 Cherokee County and shall use the remainder for tourism-related expenditures. "Net
31 proceeds" means gross proceeds less the cost to the county of administering and
32 collecting the tax. The Authority may expend these funds only to further the
33 development of travel, tourism, and conventions in the county through advertising and
34 promotion.

35 The following definitions apply in this section:

36 (1) Net proceeds. – Gross proceeds less the cost to the county of
37 administering and collecting the tax, as determined by the finance
38 officer, not to exceed three percent (3%) of the first five hundred
39 thousand dollars (\$500,000) of gross proceeds collected each year and
40 one percent (1%) of the remaining gross receipts collected each year.

41 (2) Promote travel and tourism. – To advertise or market an area or
42 activity, publish and distribute pamphlets and other materials, conduct
43 market research, or engage in similar promotional activities that attract

1 tourists or business travelers to the area. The term includes
2 administrative expenses incurred in engaging in the listed activities.

3 (3) Tourism-related expenditures. – Expenditures that, in the judgment of
4 the Tourism Development Authority, are designed to increase the use
5 of lodging facilities, meeting facilities, or convention facilities in a
6 county or to attract tourists or business travelers to the county. The
7 term includes tourism-related capital expenditures.

8 'Sec. 6. Appointment, Duties of Cherokee County Tourism Development Authority.–

9 (a) Appointment and membership. – When the Cherokee County Board of
10 Commissioners adopts a resolution levying a room occupancy tax, tax under this act, it
11 shall also adopt a resolution creating a County Tourism Development Authority
12 composed of the director of the Cherokee County Chamber of Commerce and the
13 following four members appointed by the Cherokee County Board of Commissioners:

- 14 (1) an owner of a hotel, motel, or other accommodations subject to the tax
15 levied by this act;
16 (2) a member of the board of county commissioners;
17 (3) a town commissioner or the mayor of the Town of Murphy; and
18 (4) a town alderman or the mayor of the Town of Andrews.

19 ~~The director of the Cherokee County Chamber of Commerce shall serve as an ex~~
20 ~~officio member of the Authority. The members appointed by the board of county~~
21 ~~commissioners shall serve three year terms, except the initial appointees. Of the initial~~
22 ~~appointees, the board of commissioners shall designate one to serve a one year term,~~
23 ~~two a two year term, and one a three year term. Vacancies created by an appointed~~
24 ~~member shall be filled by the board of commissioners. Members appointed to fill~~
25 ~~vacancies shall serve the remainder of the unexpired term for which they are appointed~~
26 ~~to fill. Authority, which shall be a public authority under the Local Government Budget~~
27 ~~and Fiscal Control Act. The resolution shall provide for the membership of the~~
28 ~~Authority, including the members' terms of office, and for the filling of vacancies on the~~
29 ~~Authority. At least one-third of the members must be individuals who are affiliated with~~
30 ~~businesses that collect the tax in the county, and at least one-half of the members must~~
31 ~~be individuals who are currently active in the promotion of travel and tourism in the~~
32 ~~county. The board of commissioners shall designate one member of the Authority as~~
33 ~~chair and shall determine the compensation, if any, to be paid to members of the~~
34 ~~Authority.~~

35 The Authority shall meet at the call of the chair and shall adopt rules of procedure to
36 govern its meetings. The Finance Officer for Cherokee County shall be the ex officio
37 finance officer of the Authority.

38 (b) Duties. – The Authority shall expend the net proceeds of the tax levied under
39 this act for the purposes provided in this act. The Authority shall promote travel,
40 tourism, and conventions in the county, sponsor tourist-related events and activities in
41 the county, and finance tourist-related capital projects in the county.~~The members of the~~
42 ~~Tourism Development Authority shall elect from its membership a chairman. The~~
43 ~~Authority shall meet at the call of the chairman and shall adopt rules of procedure to~~

1 ~~govern its meetings. The finance officer of Cherokee County shall serve ex officio as~~
2 ~~accountant for the Authority.~~

3 (c) Reports. – ~~The Tourism Development Authority shall report quarterly and at~~
4 ~~the close of the fiscal year to the board of county commissioners on its receipts and~~
5 ~~disbursements for the preceding quarter and for the year in such detail as the board may~~
6 ~~require.~~

7 ~~'Sec. 7. Repeal of Levy.~~

8 (a) ~~The board of county commissioners may by resolution repeal the levy of the~~
9 ~~room occupancy tax in Cherokee County, but no repeal of taxes levied under this act is~~
10 ~~effective until the end of the fiscal year in which the repeal resolution was adopted.~~

11 (b) ~~No liability for any tax levied under this act that attached prior to the date on~~
12 ~~which a levy is repealed is discharged as a result of the repeal, and no right to a refund~~
13 ~~of a tax that accrued prior to the effective date on which a levy is repealed may be~~
14 ~~denied as a result of the repeal.~~

15 ~~'Sec. 8. This act is effective upon ratification.'~~

16 **SECTION 18.** The catchline for Section 21(j) of S.L. 2007-527 reads as
17 rewritten:

18 "SECTION 21.(j) Subsection (a) of Section 4 of Chapter 929 of the 1985
19 Session Laws as amended by S.L. 1985-929 Laws, as amended by Chapter 319 of the
20 1987 Session Laws, reads as rewritten:"

21 **SECTION 19.** Section 1(b) of S.L. 2005-68 reads as rewritten:

22 "SECTION 1.(b) Administration. – Except as otherwise provided in this act,
23 a tax levied under this section shall be levied, administered, and collected as provided in
24 Part IV of Chapter 908 of the 1983 Session Laws, as amended by Chapters 821 and 922
25 of the 1989 Session Laws and S.L. 2001-402. Laws, S.L. 2001-402, and Section 21(cc)
26 of S.L. 2007-527. The penalties provided in Part IV of Chapter 908 of the 1983 Session
27 Laws, as amended by Chapters 821 and 922 of the 1989 Session Laws and S.L.
28 2001-402, apply to a tax levied under this section."
29

30 **MOTOR FUEL TAX CHANGES**

31 **SECTION 20.** G.S. 105-449.72 is amended by adding a new subsection to
32 read:

33 "(f) Exemption. – The requirement to obtain a bond or irrevocable letter of credit
34 does not apply to a distributor, importer, or motor fuel transporter that supplies motor
35 fuel when the market for motor fuel is disrupted and emergency supplies are needed, as
36 identified by an executive order of the Governor."

37 **SECTION 21.** G.S. 105-449.121(b)(2) reads as rewritten:

38 "(2) Audit a distributor, a retailer, a ~~bulk end-user,~~ bulk end-user, or a
39 motor fuel user that is not licensed under this Article."

40 **SECTION 22.** G.S. 105-449.136 reads as rewritten:

41 **"§ 105-449.136. Tax on alternative fuel.**

42 A tax at the motor fuel rate is imposed on liquid alternative fuel used to operate a
43 highway vehicle by means of a vehicle supply tank that stores fuel only for the purpose
44 of supplying fuel to operate the vehicle. A tax at the equivalent of the motor fuel rate is

1 imposed on all other alternative fuel used to operate a highway vehicle. The Secretary
2 must determine the equivalent rate. The exemptions from the tax on motor fuel in ~~G.S.~~
3 ~~105-449.88(2), (3), and (4)~~ G.S. 105-449.88 apply to the tax imposed by this section.
4 The refunds for motor fuel tax allowed by Part 5 of Article 36C of this Chapter apply to
5 the tax imposed by this section, except that the refund allowed by G.S. 105-449.107(b)
6 for certain vehicles that use power takeoffs does not apply to a vehicle whose use of
7 alternative fuel is taxed on the basis of miles driven. The proceeds of the tax imposed
8 by this section must be allocated in accordance with G.S. 105-449.125."

10 OTHER CHANGES

11 **SECTION 23.** Section 67(a) of S.L. 2008-134 reads as rewritten:

12 "**SECTION 67.(a)** ~~G.S. 58-5-25(a)(2)~~58-6-25(a)(2) is repealed."

13 **SECTION 24.(a)** G.S. 153A-156.1 reads as rewritten:

14 "**§ 153A-156.1. (For effective date, see note) Heavy equipment gross receipts tax in**
15 **lieu of property tax.**

16 (a) Definitions. – The following definitions apply in this section:

17 (1) Heavy equipment. – Earthmoving, construction, or industrial
18 equipment that is mobile, weighs at least 1,500 pounds, and meets any
19 of the descriptions listed in this subdivision. The term includes an
20 attachment for heavy equipment, regardless of the weight of the
21 attachment.

22 a. It is a self-propelled vehicle that is not designed to be driven on
23 a highway.

24 b. It is industrial lift equipment, industrial material handling
25 equipment, industrial electrical generation equipment, or a
26 similar piece of industrial equipment.

27 (2) Short-term lease or rental. – Defined in G.S. 105-187.1.

28 (b) Tax Authorized. – A county may, by ~~resolution~~ordinance, impose a tax at the
29 rate of one and two-tenths percent (1.2%) on the gross receipts from the short-term lease
30 or rental of heavy equipment by a person whose principal business is the short-term
31 lease or rental of heavy equipment at retail. The heavy equipment subject to this tax is
32 exempt from property tax under G.S. 105-275, and this tax provides an alternative to a
33 property tax on the equipment. A person is not considered to be in the short-term lease
34 or rental business if the majority of the person's lease and rental gross receipts are
35 derived from leases and rentals to a person who is a related person under
36 G.S. 105-163.010.

37 The tax authorized by this section applies to gross receipts that are subject to tax
38 under G.S. 105-164.4(a)(2). Gross receipts from the short-term lease or rental of heavy
39 equipment are subject to a tax imposed by a county under this section if the place of
40 business from which the heavy equipment is delivered is located in the county.

41 (c) Payment. – A person whose principal business is the short-term lease or
42 rental of heavy equipment is required to remit a tax imposed by this section to the
43 county finance officer. The tax is payable quarterly and is due by the last day of the
44 month following the end of the quarter. The tax is intended to be added to the amount

1 charged for the short-term lease or rental of heavy equipment and paid to the heavy
2 equipment business by the person to whom the heavy equipment is leased or rented.

3 (d) Enforcement. – The penalties and collection remedies that apply to the
4 payment of sales and use taxes under Article 5 of Chapter 105 of the General Statutes
5 apply to a tax imposed under this section. The county finance officer has the same
6 authority as the Secretary of Revenue in imposing these penalties and remedies.

7 (e) Effective Date. – A tax imposed under this section becomes effective on the
8 date set in the ~~resolution-ordinance~~ imposing the tax. The date must be the first day of a
9 calendar quarter and may not be sooner than the first day of the calendar quarter that
10 begins at least two months after the date the ~~resolution-ordinance~~ is adopted.

11 (f) Repeal. – A county may, by ~~resolution-ordinance~~, repeal a tax imposed under
12 this section. The repeal is effective on the date set in the ~~resolution-ordinance~~. The date
13 must be the first day of a calendar quarter and may not be sooner than the first day of
14 the calendar quarter that begins at least two months after the date the ~~resolution~~
15 ~~ordinance~~ is adopted."

16 **SECTION 24.(b)** G.S. 160A-215.2 reads as rewritten:

17 **"§ 160A-215.2. (For effective date, see note) Heavy equipment gross receipts tax in**
18 **lieu of property tax.**

19 (a) Definitions. – The following definitions apply in this section:

20 (1) Heavy equipment. – Defined in G.S. 153A-156.1.

21 (2) Short-term lease or rental. – Defined in G.S. 105-187.1.

22 (b) Tax Authorized. – A city may, by ~~resolution-ordinance~~, impose a tax at the
23 rate of eight tenths percent (0.8%) on the gross receipts from the short-term lease or
24 rental of heavy equipment by a person whose principal business is the short-term lease
25 or rental of heavy equipment at retail. The heavy equipment subject to this tax is exempt
26 from property tax under G.S. 105-275, and this tax provides an alternative to a property
27 tax on the equipment. A person is not considered to be in the short-term lease or rental
28 business if the majority of the person's lease and rental gross receipts are derived from
29 leases and rentals to a person who is a related person under G.S. 105-163.010.

30 The tax authorized by this section applies to gross receipts that are subject to tax
31 under G.S. 105-164.4(a)(2). Gross receipts from the short-term lease or rental of heavy
32 equipment are subject to a tax imposed by a city under this section if the place of
33 business from which the heavy equipment is delivered is located in the city.

34 (c) Payment. – A person whose principal business is the short-term lease or
35 rental of heavy equipment is required to remit a tax imposed by this section to the city
36 finance officer. The tax is payable quarterly and is due by the last day of the month
37 following the end of the quarter. The tax is intended to be added to the amount charged
38 for the short-term lease or rental of heavy equipment and paid to the heavy equipment
39 business by the person to whom the heavy equipment is leased or rented.

40 (d) Enforcement. – The penalties and collection remedies that apply to the
41 payment of sales and use taxes under Article 5 of Chapter 105 of the General Statutes
42 apply to a tax imposed under this section. The city finance officer has the same
43 authority as the Secretary of Revenue in imposing these penalties and remedies.

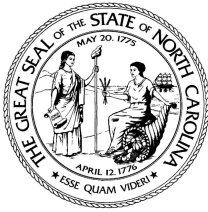
1 (e) Effective Date. – A tax imposed under this section becomes effective on the
2 date set in the ~~resolution-ordinance~~ imposing the tax. The date must be the first day of a
3 calendar quarter and may not be sooner than the first day of the calendar quarter that
4 begins at least two months after the date the ~~resolution-ordinance~~ is adopted.

5 (f) Repeal. – A city may, by ~~resolution, ordinance,~~ repeal a tax imposed under
6 this section. The repeal is effective on the date set in the ~~resolution, ordinance.~~ The date
7 must be the first day of a calendar quarter and may not be sooner than the first day of
8 the calendar quarter that begins at least two months after the date the ~~resolution~~
9 ordinance is adopted."

10 **SECTION 24.(c)** This section does not affect the rights or liabilities of a
11 county or city, a taxpayer, or another person arising under G.S. 160A-215.2 or G.S.
12 153A-156.1 before the effective date of this section; nor does it affect the right to any
13 refund or credit of a tax that accrued under G.S. 160A-215.2 or G.S. 153A-156.1 before
14 the effective date of this section. All existing ordinances or resolutions enacted under
15 G.S. 160A-215.2 or G.S. 153A-156.1 prior to the effective date of this section shall
16 continue in full force and effect until repealed, modified, or amended.

17
18
19 **EFFECTIVE DATE**

20 **SECTION 25.** Except as otherwise provided, this act is effective when it
21 becomes law.
22



BILL ANALYSIS

DRAFT BILL 2009-SVz-4: Revenue Laws Technical, Administrative, & Clarifying Changes

Committee: Revenue Laws Study Committee
Introduced by:
Version: Draft

Date: January 7, 2009
Summary by: Trina Griffin,
Cindy Avrette, &
Martha Walston
Committee Counsel

SUMMARY: *This legislative proposal makes several technical, clarifying, and administrative changes to the revenue laws and related statutes.*

BILL ANALYSIS: This draft proposal makes the following technical, clarifying, and administrative changes:

| Section | Explanation |
|--|--|
| <i>Corporate, Excise, and Insurance Taxes</i> | |
| 1 | Adds associate home inspectors to the State privilege license provision enacted last year for home inspectors so that associate home inspectors will be taxed similarly. S.L. 2008-206 imposed an annual State privilege license tax of \$50 on a home inspector licensed under the Home Inspector Act. The Home Inspector Act also licenses associate home inspectors, which are defined separately. However, they were not included in the law change. Without this change, associate home inspectors would be subject to local privilege license tax in each city that levies the tax. |
| 2 | Changes the term 'nonbusiness activities' to 'activities producing nonapportionable income', which is a defined term in the statute that sets out the manner in which corporations must allocate and apportion their income to North Carolina for income tax purposes. In 2002, the terms 'business income' and 'nonbusiness income' were replaced by apportionable and nonapportionable. This subsection was missed when those changes were made. |
| 3 | Changes an incorrect statutory reference. |
| 4 | Corrects an effective date relating to changes made to the statute designating who may sign an income tax return. These changes were originally part of the major rewrite of the tax appeals procedure in 2007 (SB 242). |
| 5(a) & (b) | Changes the date by which the State Treasurer must make a transfer from the General Fund to the North Carolina Health Insurance Risk Pool Fund. The current statute provides that <i>within 75 days after the end of each fiscal year</i> , the Treasurer must transfer to the Fund an amount equal to the growth in net revenue from the gross premiums tax on insurance companies. Insurance tax returns are due by March 15. Insurance companies are also required to prepay their tax in installments. The first installment of the fiscal year is due by October 15. Therefore, until those installments are remitted, little or no funds are available for transfer. This section changes the date from within 75 days after the end of the fiscal year, or September 14, to November 1, as recommended by the Department of Revenue. |

| | |
|---|---|
| | |
| <i>Sales and Use Tax Changes</i> | |
| 6 | Replaces the word 'energy' with the word 'electricity' for consistency. This term appears in the statute enacted last year authorizing a sales tax refund for materials used to build a facility that manufactures solar electricity generating materials. |
| 7 | Corrects two incorrect statutory references. |
| <i>Property Tax Changes</i> | |
| 8(a) & (b) | Reinserts the words 'shares' and 'residence', which were inadvertently deleted when changes were made in 2008 to the circuit breaker statute. |
| 9 | Makes a conforming change to the statute that sets out the application procedure for property tax exemption related to the exemption for drug samples enacted last year. |
| 10 | Clarifies that in order for property to be excluded from tax, it must first satisfy any statutory application requirements. |
| 11(a) & (b) | Clarifies treatment of property owned by husband and wife as tenants by the entirety as opposed to tenants in common when qualifying for the homestead exclusion. If owned in tenancy by the entirety, only one spouse has to meet the age or disability requirement. |
| 12 | <p>Makes the following clarifying and technical changes to the homestead circuit breaker:</p> <ul style="list-style-type: none"> • Defines deferred taxes. • Clarifies that the property owned by a qualifying owner must have been the owner's permanent residence for at least five consecutive years but that the owner's five-year occupancy does not have to be consecutive. • Clarifies that the occupancy requirement refers to "length" of occupancy. • Removes an unnecessary word. • Clarifies that only the deferred taxes for the last three years prior to the disqualifying event become due and payable. • Clarifies that notice of the sum of deferred taxes and interest that are due and payable must be sent annually to the mailing address of the residence subject to the circuit breaker benefit as opposed to mailing notice to each owner of the property. |
| 13 | <p>Makes the following clarifying changes to the disabled veteran homestead exclusion:</p> <ul style="list-style-type: none"> • Clarifies that the exclusion is available to a disabled veteran who "received" instead of "receives" federal benefits to adapt his or her housing, since these benefits are generally a one-time payment. • Clarifies that if the permanent residence is owned by spouses as tenants by the entirety, only one spouse has to meet the exclusion requirements. |
| 14 | <p>Makes the following conforming changes to the statute that sets out the application procedure for property tax exemptions:</p> <ul style="list-style-type: none"> • Adds drug samples to the list of exempt property not requiring an application. • Adds solar energy electric systems to the list of property excluded from taxation that must file a single application. • Adds working waterfront property to the list of property classified for taxation |

| | |
|--------------------------------------|--|
| | <p>at reduced valuation that must file a single application</p> <ul style="list-style-type: none"> • Makes a technical correction. |
| 15 | Repeals an unnecessary statute. |
| 16 | Clarifies that the amount of taxes that a tax collector must report on a tax certificate includes any deferred taxes. |
| <i>Occupancy Tax Changes</i> | |
| 17 | Adds a Session Law reference that was inadvertently omitted when the Cherokee County local occupancy tax act was amended last year. In 2007, a number of local occupancy tax local acts were amended to change the due date for remitting occupancy tax proceeds and filing returns from the 15 th to the 20 th of the month to conform to current sales tax statutes. The Cherokee County local occupancy tax act was one of the acts so amended. However, when the rest of the local act was amended in 2008, the 2007 change was not incorporated. To make this technical change, the entire local act must be set out under drafting convention. However, no substantive change is being made. |
| 18 | Corrects an incorrect Session Law reference. |
| 19 | Adds to S.L. 2005-68, a Session Law reference to the 2007 act referenced above that made changes to a number of local occupancy tax acts related to the due date of the tax and return. S.L. 2005-68 is the act that authorized the additional occupancy tax to finance the NASCAR Hall of Fame Museum. |
| <i>Motor Fuel Tax Changes</i> | |
| 20 | Provides an exception to the requirement that a distributor, importer, or motor fuel transporter must obtain a bond or irrevocable letter of credit when the person is supplying motor fuel into the State because the market for motor fuel has been disrupted and emergency supplies are needed, as identified by an executive order of the Governor. The bonding requirement became an issue during the recent motor fuel supply shortages in the western part of the State. |
| 21 | Corrects a misspelled word. |
| 22 | Conforms the tax exemptions for alternative fuel to the tax exemptions for motor fuel. |
| <i>Other Changes</i> | |
| 23 | Corrects an incorrect statutory reference. |
| 24(a) & (b) | Replaces the word 'resolution' with the word 'ordinance' in each of the statutes authorizing cities and counties to levy a gross receipts tax in lieu of a property tax on the short-term rental of heavy equipment. |

APPENDIX A

AUTHORIZING LEGISLATION ARTICLE 12L OF CHAPTER 120 OF THE GENERAL STATUTES

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<http://www.ncleg.net/committees/>

ARTICLE 12L

Revenue Laws Study Committee

§ 120-70.105. Creation and membership of the Revenue Laws Study Committee.

(a) Membership. -- The Revenue Laws Study Committee is established. The Committee consists of 16 members as follows:

- (1) Eight members appointed by the President Pro Tempore of the Senate; the persons appointed may be members of the Senate or public members.
- (2) Eight members appointed by the Speaker of the House of Representatives; the persons appointed may be members of the House of Representatives or public members.

(b) Terms. -- Terms on the Committee are for two years and begin on January 15 of each odd-numbered year, except the terms of the initial members, which begin on appointment. Legislative members may complete a term of service on the Committee even if they do not seek reelection or are not reelected to the General Assembly, but resignation or removal from service in the General Assembly constitutes resignation or removal from service on the Committee.

A member continues to serve until a successor is appointed. A vacancy shall be filled within 30 days by the officer who made the original appointment. (1997-483, s. 14.1; 1998-98, s. 39.)

§ 120-70.106. Purpose and powers of Committee.

(a) The Revenue Laws Study Committee may:

- (1) Study the revenue laws of North Carolina and the administration of those laws.
- (2) Review the State's revenue laws to determine which laws need clarification, technical amendment, repeal, or other change to make the laws concise, intelligible, easy to administer, and equitable.
- (3) Call upon the Department of Revenue to cooperate with it in the study of the revenue laws.
- (4) Report to the General Assembly at the beginning of each regular session concerning its determinations of needed changes in the State's revenue laws.

These powers, which are enumerated by way of illustration, shall be liberally construed to provide for the maximum review by the Committee of all revenue law matters in this State.

(b) The Committee may make interim reports to the General Assembly on matters for which it may report to a regular session of the General Assembly. A report to the General Assembly may contain any legislation needed to implement a recommendation of the Committee. When a recommendation of the Committee, if enacted, would result in an increase or decrease in State revenues, the report of the Committee must include an estimate of the amount of the increase or decrease. (1997-483, s. 14.1.)

§ 120-70.107. Organization of Committee.

(a) The President Pro Tempore of the Senate and the Speaker of the House of Representatives shall each designate a cochair of the Revenue Laws Study Committee. The Committee shall meet upon the joint call of the cochairs.

(b) A quorum of the Committee is nine members. No action may be taken except by a majority vote at a meeting at which a quorum is present. While in the discharge of its official duties, the Committee has the powers of a joint committee under G.S. 120-19 and G.S. 120-19.1 through G.S. 120-19.4.

(c) The Committee shall be funded by the Legislative Services Commission from appropriations made to the General Assembly for that purpose. Members of the Committee receive subsistence and travel expenses as provided in G.S. 120-3.1 and G.S. 138-5. The Committee may contract for consultants or hire employees in accordance with G.S. 120-32.02. Upon approval of the Legislative Services Commission, the Legislative Services Officer shall assign professional staff to assist the Committee in its work. Upon the direction of the Legislative Services Commission, the Supervisors of Clerks of the Senate and of the House of Representatives shall assign clerical staff to the Committee. The expenses for clerical employees shall be borne by the Committee. (1997-483, s. 14.1.)

APPENDIX B

MEETING AGENDAS

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REVENUE LAWS STUDY COMMITTEE AGENDA

Sen. John Kerr

Rep. Paul Luebke

*Wednesday, October 22, 2008
Room 544, Legislative Office Building
9:30 a.m.*

- I. Welcoming Remarks**
- Overview of 2008 Finance Law Changes and Fate of the Revenue**
- II. Laws Study Committee's Recommendations to the 2008 General Assembly**
 - Cindy Avrette, Research Division*
- Budget Outlook**
- III. – Barry Boardman, Fiscal Research Division**
- Overview of Issues Raised by Advancing the Reappraisal Schedule**
- IV. for Property Taxes (S.L. 2008-146 Property Tax Modifications)**
 - Martha Walston, Fiscal Research Division*
- Overview of Exemptions for Nonprofits**
- V. – Trina Griffin, Research Division**
 - Rodney Bizzell, Fiscal Research Division*
 - Lee Dixon, Fiscal Research Division*
- Discussion of the Illinois Provena Covenant Medical Center Case**
 - Stan Jenkins, Supervisor of Assessments*
- Champaign County, Illinois**
- Adjournment**
- VI.**

Next Meeting Date: Wednesday, November 19, 2008
All meetings in Room 544, LOB at 9:30 a.m.

REVENUE LAWS STUDY COMMITTEE AGENDA

Sen. John Kerr

Rep. Paul Luebke

*Wednesday, November 19, 2008
Room 544, Legislative Office Building
9:30 a.m.*

I. Approval of Minutes from October 22 Meeting

II. Update on Combined Reporting

- *Cindy Avrette, Research Division*
- *Mark Morton, General Counsel for Revenue Operations, West Virginia Tax Department*

III. Privilege License Taxes in North Carolina

- *Christopher McLaughlin, Assistant Professor of Public Law and Government, UNC School of Government*
- *Trina Griffin, Research Division*

IV. Sales Tax Treatment of Food vs. Prepared Food

- *Sandra Johnson, Fiscal Research Division*

V. Adjournment

**Next Meeting Date: Monday, December 15, 2008
All meetings in room 544, LOB, at 9:30 a.m.**

REVENUE LAWS STUDY COMMITTEE AGENDA

Sen. John Kerr

Rep. Paul Luebke

*Monday, December 15, 2008
Room 544, Legislative Office Building
9:30 a.m.*

- I. Approval of Minutes from November 19 Meeting**
- II. Alternative Methods of Business Taxation**
 - *Cindy Avrette, Research Division*
 - *Karey Barton, Principal, Ryan, Austin, Texas*
- III. Current Law on Combinations in North Carolina**
 - *Greg Radford, Department of Revenue*
 - *Bill Nelson, Attorney, Smith Anderson Blount Dorsett Mitchell & Jernigan, LLP*
- IV. Update on Privilege License Taxation Issue**
 - Update on Fiscal Estimates**
 - *Rodney Bizzell, Fiscal Research Division*
 - Response and Comments**
 - *League of Municipalities*
 - *Association of County Commissioners*
- V. Overview of Issues Raised by Advancing the Reappraisal Schedule for Property Taxes**
 - *Martha Walston, Fiscal Research Division*
- VI. Adjournment**

**Next Meeting Date: Wednesday, January 7, 2009
In Room 544 LOB, at 9:30 a.m.**

REVENUE LAWS STUDY COMMITTEE AGENDA

Sen. John Kerr

Rep. Paul Luebke

*Wednesday, January 7, 2009
Room 544, Legislative Office Building
9:30 a.m.*

- I. Approval of Minutes from December 15 Meeting**
- II. Review of Property Tax Recommendations**
 - Martha Walston, Fiscal Research Division*
- III. IRC Update**
 - Heather Fennell, Research Division*
 - Barry Boardman, Fiscal Research Division*
- IV. Taxation for the Digital Age**
 - Trina Griffin, Research Division*
- V. Resale of Tickets via the Internet & 2009 Sunset**
 - Cindy Avrette, Research Division*
- VI. Update on Streamlined Sales Tax Project**
 - Andy Sabol, Department of Revenue*
- VII. Comments on Changing the Corporate Tax Structure**
 - Andy Ellen, Retail Merchants Association*
 - Mark Prak, Brooks, Pierce, McLendon, Humphrey & Leonard*
 - John McAlister, NC Chamber*
 - Joseph Crosby, COST*

**Next Meeting Date: Wednesday, January 21, 2009
In Room 544 LOB, at 9:30 a.m.**

VIII. Revenue Laws Technical and Administrative Changes – Part I

– Trina Griffin, Research Division

IX. Adjournment

REVENUE LAWS STUDY COMMITTEE AGENDA

Sen. John Kerr

Rep. Paul Luebke

*Tuesday, January 27, 2009
Room 1228, Legislative Building
9:30 a.m.*

I. Approval of Minutes from January 7 Meeting

II. Department of Revenue

- Introduction of Secretary-Elect, Kenneth Lay
- Reports:
 - Revenue Generated from Captive REIT Provision, *William Spencer, Department of Revenue*
 - Small Business Protection Act, Quality Control Improvements, *Linda Millsaps, Department of Revenue*

III. North Carolina Hospital Association

- Report on Charity Care and Community Benefit Data, *Hugh Tilson*

IV. Budget Outlook Update

- Barry Boardman, Fiscal Research Division

V. Legislative Proposals For Consideration

- #1: IRC Update
Heather Fennell, Research Division
- #2: Modernize Corporate Income Tax Filings
Cindy Avrette, Research Division
- #3: Streamlined Sales and Use Tax Update
Cindy Avrette, Research Division
- #4: Real Property Sales Information
Martha Walston, Fiscal Research Division
- #5: Modernize Sales Tax Statutes/Digital Products
Trina Griffin, Research Division
 - *Comments from Brooks Raiford, President & CEO, NC Technology Association*

- #6: Revenue Laws Technical, Administrative, & Clarifying Changes -
 - Part I – *Trina Griffin, Research Division*
 - Part II (Property Tax Changes) – *Martha Walston, Fiscal Research Division*

APPENDIX C

DISPOSITION OF COMMITTEE'S RECOMMENDATIONS TO THE 2008 SESSION OF THE 2007 GENERAL ASSEMBLY

**ALL MATERIALS DISTRIBUTED AT MEETINGS MAY BE
VIEWED ON THE COMMITTEE'S WEBSITE:
<http://www.ncleg.net/committees/>**

| SHORT TITLE | SENATE SPONSORS | HOUSE SPONSORS | BILL # | FINAL STATUS* |
|---|-----------------|---|--------------------|--|
| Procedure for Tax Class Actions | Clodfelter | | SB 1715 | Enacted* SL 2008-107, Sec. 28.28(a) (Budget Bill) |
| IRC Update | Kerr | Luebke, Wainwright, Weiss, Gibson | HB 2416 SB 1939 | Enacted SL 2008-107, Sec. 28.1(a) (Budget Bill) |
| Corporate Tax Law Changes | | Gibson, Luebke, Wainwright, Weiss | HB 2508 | Enacted* SL 2008-107, Sec. 28.7(a) (Budget Bill) SL 2008-107, Sec. 28.8(a) (Budget Bill) |
| Estate and Gift Tax Law Changes | Hoyle | | SB 1756 | Enacted* SL 2008-107, Sec. 28.17(a) (Budget Bill) SL 2008-107, Sec. 28.18(a) (Budget Bill) SL 2008-107, Sec. 28.18(b) (Budget Bill) |
| Deferred Property Tax Program Changes | Clodfelter | Brubaker, Hill | SB 1876 HB 2483 | Enacted* SL 2008-35 |
| Property Tax Modifications | Clodfelter | Brubaker, Hill | SB 1878 HB 2476 | Enacted* SL 2008-146 |
| Exempt Disaster Assistance Debit Sales | Hartsell | | SB 1703 | Enacted SL 2008-107, Sec. 28.6(a) (Budget Bill) |
| Revenue Laws Technical, Clarifying & Administrative Changes | Hartsell | Luebke, Gibson, Wainwright, Weiss | SB 1704 HB 2352 | Enacted* SL 2008-134 |
| Tax on Short-Term Heavy Equipment Rentals | Brunstetter | Saunders | SB 1852 HB 2446 | Enacted* SL 2008-144 |
| Extend R & D Credit | Hoyle | Weiss, Luebke, Wainwright, Gibson | SB 1755 HB 2336 | Enacted* SL 2008-107, Sec. 28.2(a) (Budget Bill) |

* Bills were modified prior to enactment.

| SHORT TITLE | SENATE SPONSORS | HOUSE SPONSORS | BILL # | FINAL STATUS* |
|--|-----------------|---|--------------------|--|
| Extend State Ports Tax Credit | Boseman | McComas, Wainwright, Gibson | HB 2366 SB 1731 | Enacted SL 2008-107, Sec. 28.5(a) (Budget Bill) |
| Expand Small Business Health Benefits Credit | | Weiss, Luebke, Wainwright, Gibson | HB 2335 | Enacted* SL 2008-107, Sec. 28.9A(a) (Budget Bill) |
| Sunset Recycling Facility Credits | Hoyle | Wainwright, Gibson | SB 1747 HB 2472 | Not enacted |
| Supplemental PEG Support | Clodfelter | Luebke, Brubaker, Hill, McComas | SB 1716 HB 2342 | Enacted* SL 2008-148 |

* Bills were modified prior to enactment.

APPENDIX D

**REMARKS FROM BROOKS RAIFORD,
PRESIDENT & CEO
NORTH CAROLINA TECHNOLOGY ASSOCIATION**

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**North Carolina General Assembly
Revenue Laws Study Committee
January 27, 2009**

Remarks from:
**Brooks Raiford, President & CEO
North Carolina Technology Association**

Mr. Chairman, thank you for the opportunity to speak briefly today about the issue of digital taxation.

My name is Brooks Raiford, and I serve as the new president of the North Carolina Technology Association, known as NCTA, which has 400 member companies of all sizes, primarily from the technology sector. We just had our Annual Meeting a couple of weeks ago, and noted to our Members that our agenda for 2009 is driven by three things: jobs, jobs, and jobs. A significant number of people in North Carolina depend on the technology sector to support them and their families. Not only are there over 100,000 information technology workers in North Carolina, but many technology-oriented companies of course have non-IT workers as well who depend on the financial health of their employer.

So as you consider changes to the tax laws, we want to offer some comments. We don't come today with a blanket objection to taxes – our member firms pay income, payroll, and property taxes, among others. We do ask that as you explore revisions to the tax structure, that you remain mindful of several considerations:

- We're concerned about the impact on both the consumer and on commerce of new or increased taxes during an economic downturn, so would urge that new taxes not be imposed .
- We would emphasize the importance of the technology sector to the state's current and future economy, and would object to the technology sector being singled out for new taxation when there are dozens of examples of other cases of various sales tax exemptions.
- As you consider digital taxation, we would encourage you to note that purchasing digital products encourages "green" commerce – it avoids packaging, along with reducing the need for buildings and physical infrastructure to support the sale and distribution of hard copies of software, books, etc.

The General Assembly has been a great partner over the years in recognizing the impact of these companies and these workers. For example:

- This past Session, you encouraged the creation of jobs and growth of companies here by extending the R&D Tax Credit for five years, and raised the cap on the Qualified Business Ventures credit, which encourages investment in early-stage companies.
- In the 2007 Session, you encouraged software development in North Carolina by reducing the sales tax for equipment used in R&D for software development.
- Also in that Session, you encouraged research at our colleges and universities by increasing the tax credit percentage for R&D done in North Carolina, including at our colleges and universities.

So there is a history of tax policy that enhances the growth of the increasingly important technology sector in our state.

We understand the desire to streamline and make the imposition of sales taxes more fair, and appreciate the willingness of the Committee and staff to hear from those affected. Our request is that the technology sector not be singled out for changes, and that deliberate care is taken to avoid any unintended consequences of changing the definitions of what is taxed and how.

Mr. Chairman, you and the Committee staff have been generous in allowing our input to this point, and we'd ask that we continue to be included in discussions as legislation moves forward.

Thank you for giving me these few minutes to share our comments.

For more information, please contact:
Brooks Raiford, President & CEO
North Carolina Technology Association
4020 Westchase Boulevard, Suite 350
Raleigh, NC 27650
919-856-0393, ext. 224
braiford@nctechnology.org
www.nctechnology.org

APPENDIX E

LIST OF COUNTIES IMPACTED BY 2008 LEGISLATION ADVANCING REAPPRAISAL SCHEDULE

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APPENDIX F

LIST OF COUNTIES THAT OBTAIN SALES INFORMATION OF REAL PROPERTY TRANSFERS

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APPENDIX G

EXAMPLES OF REAL PROPERTY SALES INFORMATION FORMS

**CABARRUS COUNTY
DARE COUNTY
PERQUIMANS COUNTY**

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APPENDIX H

NORTH CAROLINA HOSPITAL ASSOCIATION REPORT ON CHARITY CARE AND COMMUNITY BENEFIT DATA

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Mr. Don Dalton, All NCHA
ANDI Participation Update

Requests Reports

Help Log Out

Community Benefit Report

Hospital or Group Name

All NCHA

Members

FY 2007

Total

Time Period

Statistic Type

Last Updated

1/27/2009 9:39

am

Number of Completed Surveys

106

Community Benefits

| | |
|--|---------------|
| A. Estimated Costs of Treating Charity Care Patients* | \$503,021,411 |
| B. Estimated Unreimbursed Costs of Treating Medicare Patients* | \$653,578,040 |
| C. This includes an adjustment in this period's Medicare revenues for extraordinary adjustments ² of: | \$ 54,731,976 |
| D. Without this Medicare adjustment, Medicare Losses would have been (B + C): | \$708,484,530 |
| E. Estimated Unreimbursed Costs of Treating Medicaid Patients* | \$324,342,641 |
| F. This includes an adjustment in this period's Medicaid revenues for extraordinary adjustments ² of: | \$ 69,822,891 |
| G. Without this Medicaid adjustment, Medicaid Losses would have been (E + F): | \$394,165,532 |
| H. Estimated Unreimbursed Costs of Treating Patients from Other Non-Negotiated Government Programs* | \$ 23,003,141 |
| I. This includes an adjustment in this period's Other Non-Negotiated Government Programs revenues for extraordinary adjustments ² of: | \$ 12,519,835 |
| J. Without this adjustment, Other Non-Negotiated Government Programs Losses would have been (H + I): | \$ 35,522,976 |
| K. Community Health Improvement Services & Community Benefit Operations | \$ 44,251,356 |
| L. Health Professions Education | \$258,608,026 |
| M. Subsidized Health Services ³ | \$280,629,382 |

ANDI Report

https://andi.ncha.org/reports/andi_report_list.lasso Page 2 of 4

1/29/09 8:38 AM

| | |
|--|------------------------|
| N. Research Costs | \$ 4,071,920 |
| O. Cash and In-kind Contributions to Community Groups | \$ 49,245,465 |
| P. Community Building Activities ⁴ | \$ 9,203,559 |
| <hr/> | |
| Q. Total Community Benefits¹ with Settlements and Extraordinary Adjustments (A + B + E + H + K + L + M + N + O + P) | \$2,148,889,482 |
| <hr/> | |
| R. Total Community Benefits¹ without Settlements and Extraordinary Adjustments (A + D + G + J + K + L + M + N + O + P) | \$2,286,138,69 |

8

Bad Debt Costs

| | |
|--|-----------------------|
| S. Estimated Costs of Treating Bad Debt Patients* | \$ 592,347,112 |
|--|-----------------------|

Notes:

(1) Grant monies received to support any community benefit activities. These amounts have not been netted from Total Community Benefits.

\$61,789,21

8

(2) Notes about prior period adjustments

(3) Notes about Subsidized Health Services

(4) Notes about Community Building Activities

(5) URL with additional information about this community benefits report

(6) Other Notes

«Back To Reports

If you see any statistic in any report that looks odd to you, please email andi@ncha.org us and let us know. All we need is the column and line description that looks suspicious. Thank you.

Report Error Key

divide by zero error The formula for this item includes division and when your value was being calculated, it was determined to have a denominator value of zero.

N/A There is an error in your hospital's response to this report item and no answer will be returned until corrected.

n/a error This number cannot be calculated. Possible reasons include

- It is (0/0)
- you have asked for a standard deviation based on one number (2 is minimum number of valid responses required in order to calculate a standard deviation.)
- A necessary threshold of variation has not been met.
- A facility "weight" statistics has been requested, but there is an error in the facility's answer (so it can't be used in the weighted average).

no supporting survey error This report item is dependent upon information in another survey which has not been released yet, or is for a pre-ANDI (prior to FiscalYear 2003) time period.

not answered error One or more of the questions needed to calculate this report item were not answered in this survey. Often this is because the question was accidentally left blank (signifying "Missing Value") rather than having a zero in it.

not completed error This survey has not been completed by this hospital.

not in survey error One or more of the questions needed to calculate this report item were not asked in this survey (so ANDI could not calculate a value). Try selecting a different survey.

out of range error Your value for this report item is considered either too high or too low and is suspected of being incorrect. If

the value is correct, please contact me so that I can adjust the range to accept this value.

too few resp error

The number of valid responses is less than the group's minimum number of facilities needed to calculate aggregate or rank statistics. In the first five years of ANDI we learned how many responses are needed to get a stable average (one that doesn't change much when another facility marks its survey complete). In general averages reach the first level of stability at 65%, but they really stop moving with each newly completed survey at 80% (this is the overall response rate statistic). We have restricted ANDI to not show averages where participation rates are below that first threshold (65%). In this way you can have more confidence that the averages you can see today are relatively stable averages. We recommend that you always add a column for the overall response rate when asking for any group statistic.

Export Options

HTML Table Export

The HTML Table option outputs the data from this page into a new Web page. Most ANDI users will be able to select the commands in the *Edit* menu to *Select All*, and then *Copy*, the data, then switch to Excel and *Paste* the data into a spreadsheet. For detailed export instructions, [please see the FAQ](#).

Delimited Export

The Semicolon-Delimited option outputs the data into a new Web page with semicolon-delimited values. Most ANDI users will be able to select the commands in the *Edit* menu to *Select All*, and then *Copy*, the data, then switch to Excel and *Paste* the data into a spreadsheet. For detailed export instructions, [please see the FAQ](#).

APPENDIX I

NORTH CAROLINA DEPARTMENT OF REVENUE REPORT ON REVENUE GENERATED FROM CAPTIVE REIT PROVISION

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<http://www.ncleg.net/committees/>

January 27, 2009

Report to

The Revenue Laws Study Committee

**Amount of Corporate Income Tax Revenue Generated by
the Requirement that Captive REITS Add
Dividends Paid to Taxable Income**

Tax Year 2007

As required by Section 31.18.(d) of Session Law 2007-323, this is to report that the amount of corporate income tax revenue generated in the 2007 taxable year by the addition of dividends paid by captive REITs to taxable income required by G.S. 105-130.5(a)(19) is \$ 12,805,806.

APPENDIX J

NORTH CAROLINA DEPARTMENT OF REVENUE REPORT ON CUSTOMER SERVICE INITIATIVES

**ALL MATERIALS DISTRIBUTED AT MEETINGS MAY BE
VIEWED ON THE COMMITTEE'S WEBSITE:**

<http://www.ncleg.net/committees/>



North Carolina Department of Revenue

Beverly Eaves Perdue
Governor

January 27, 2009

Kenneth R. Lay
Secretary

MEMORANDUM

TO: The Honorable Marc Basnight Senator John H. Kerr, III
 President Pro Tempore Revenue Laws Study Committee Chairman

 The Honorable Joe Hackney Representative Paul Luebke
 Speaker of the House Revenue Laws Study Committee Chairman

FROM: Kenneth R. Lay *Kenneth R. Lay*
 Secretary of Revenue

SUBJECT: Customer Service Initiatives

This report is prepared pursuant to Session Law 2008-107, Section 28.16(i) and addresses customer service initiatives undertaken by the Department of Revenue. The report covers five specific reporting requirements contained in the statute.

The Department has taken a comprehensive approach to customer service improvement. Delivering quality service to taxpayers and other constituents is a key strategic objective of the agency. The Department, in an effort to focus attention on this strategic objective, conducted service excellence training sessions in the fall of 2008. Over 1,400 agency personnel attended a total of 57 training sessions. This training emphasized the need to provide quality customer service in all instances, equipped employees with several tools and techniques for providing such service, and provided feedback on additional training and quality improvement issues to be considered in future efforts made by the agency regarding this important issue.

The agency also crafted a service excellence vision and nine guiding principles supporting this vision. This information became a focal point of the training efforts and other discussions about customer service improvement.

The remainder of this report provides specific information related to the five reporting requirements contained in Section 28.16(i):

P.O. Box 25000, Raleigh, North Carolina 27640
Phone (919) 733-7211

1. Efforts to ensure that inquiries on complicated tax matters are handled or reviewed by appropriate personnel within the Department.

Standard operating procedures for taxpayer inbound calls have been reviewed and enhanced. The procedures cover agency employees located at our Taxpayer Assistance and Call Center (TACC) and Taxpayer Assistance personnel located in Raleigh and in our service centers across the state. These procedures insure that employees with the requisite technical knowledge address complicated tax matters for various tax types.

The improved procedures also addressed several relevant points:

- (a) Additional and divisions on complex tax issues frequent training for personnel
- (b) Development of frequently asked questions with periodic updates
- (c) Enhancement and evaluations of the competency level of personnel responding to tax matters
- (d) Improved internal communication flow for complex tax matters
- (e) Consultation with Tax Administration

At each service center location across the state, Taxpayer Assistance managers serve as the primary contact for complicated tax matters. The managers address tax matters in consultation with administrative officers with this division based in Raleigh.

2. A review of the Department's efforts to provide accurate and timely information regarding changes in tax law resulting from legislative changes, court decisions, or revised interpretations.

The Department's efforts to provide accurate and timely information are noted in the following actions:

(1) The 2008 Tax Law Changes publication was placed on the DOR website on September 12, 2008. The publication documents the law changes enacted in 2008 and laws changes enacted in prior legislative sessions that affect 2008 tax returns. (applies to all tax schedules)

(2) The Corporate, Excise and Insurance Tax Division published a 2008 Supplement to the 2007/2008 Rules and Bulletins that modified the sections of the Rules and Bulletins that were affected by law changes enacted during the 2008 legislative session. The supplement was posted to the Department's website on September 26, 2008.

(3) Our Corporate, Excise and Insurance Tax Division developed a document titled "Important Notice Regarding Requirement for Licensed Home Inspectors to Obtain a State Privilege License" which was sent via e-mail to the North Carolina Home Inspector Licensure Board. The Board subsequently distributed the document to all of its licensed home inspectors. Form B-202A, Application for State Privilege License, was revised to include home inspectors in the list of occupations that requires a license.

Customer Service Initiatives
January 27, 2009
Page 3

(4) Created and added to the Department's website a Hot Topic titled "Internet Resale of Admission Tickets". Form TR-110, Internet Resale of Admission Tickets Report, was developed and added to the website.

(5) Refund of Unsaleable Other Tobacco Products - Form B-A-101R, was renamed and revised to reflect that the refund provision is no longer limited to cigars.

(6) Tax forms and instructions are revised each year to reflect law changes. The instructions include a section titled "Important Legislative Changes for 2008" that addresses law changes.

(7) The Department maintains on its website information about the tax credit allowed to a film production company in the form of frequently asked questions. That information was revised on August 22, 2008 to reflect legislative changes in 2008 and other policy changes.

(8) The Corporate, Excise and Insurance Tax Division published two Directives during 2008, both of which are available on the Department's website. Directive CD 08-1, dated January 23, 2008, addressed the allocation of premium income from group life insurance policies. Directive CD 08-2, dated September 15, 2008, revised the Department's guidelines for renewable energy tax credit

(9) The Personal Taxes Division revised the Individual Income, Gift, and Estate Tax Bulletins to reflect all law and administrative tax changes and posted the info to the website, including a special notice about the new earned income tax credit.

(10) All general information for Personal Taxes schedules on the website has been updated to reflect any law or administrative changes.

(11) The 2008 individual income tax return instructions include language on the front of the booklet highlighting the law changes.

(12) Personal Taxes posted a notice to the website on Jan. 6, 2009 regarding the administrative position on the addback treatment for bonus depreciation.

(13) Motor Fuels provides all licensed taxpayers with an annual notice of tax law changes. This is usually mailed to the taxpayer in the Fall. We also send these notices to the NC Petroleum Marketers Association and the NC Trucking Association to be included in their monthly newsletters. All correspondence is placed on the web for further reference.

3. A review of the Department's outreach efforts designed to assist taxpayers, particularly small business taxpayers, in complying with the State's tax laws.

Customer Service Initiatives

January 27, 2009

Page 4

The Department's outreach efforts to small businesses fall into two primary categories:

- Creating new communications and outreach channels to small business owners and entrepreneurs
- Improving the Department's existing outreach and education efforts

New Communication and Outreach Channels

The Department established a partnership with the Community College System in August 2008 in an effort to assist small businesses to better understand tax laws by providing free seminars at each of the 58 community college locations across our state. The seminars continue in 2009 and cover five key topics:

1. Tax implications for starting a business
2. Tax implications for growing a business
3. The basics of sales and use tax
4. The basics of withholding taxes
5. Dealing with the N.C. Department of Revenue.

In the first four months of the program, more than 250 small business owners and entrepreneurs attended tax seminars at the community colleges. Feedback from the attendees has been very positive, with most of the seminars rated as excellent or very good.

The N.C. Community College System Small Business Center Network also launched a website, www.sbcn.nc.gov, with a section dedicated to tax information provided by the Revenue Department. The site is a one-stop resource for small business owners and offers a variety of helpful information such as entrepreneurship training, guides and tools for starting a business, information on government contracts and business publications. Small business owners can sign up for confidential one-on-one counseling through the website.

The site also features a section from the Department of Revenue that focuses specifically on tax issues for small business owners. The key items are tax obligations, current announcements

from the Department, a tax checklist for starting a business, a guide for getting tax assistance and a list of helpful links for small businesses. The tax section is located at: www.sbcn.nc.gov/taxInfo/default.aspx

The Department has also begun issuing “plain-English” announcements about topics such as tax law changes, new electronic services, compliance issues and new reporting and filing requirements. Some of these announcements are more general and others are targeted at specific types of businesses. The announcements are similar to news releases and are designed for organizations to use in newsletters or on websites. They offer easy-to-understand explanations of complex tax issues and links to the Department’s website for additional information. They are specifically designed for small business owners who operate without the help of accountants, attorneys or tax preparers.

Customer Service Initiatives

January 27, 2009

Page 5

The announcements that apply to most businesses are sent to a network of organizations that include the North Carolina Chamber of Commerce, the North Carolina Retail Merchants Association (more than 25,000 members), local chambers of commerce across the state, business incubator organizations like the Upper Coastal Plains Council of Governments and the Rural Center. They have been sent by these organizations to members in e-mails, have appeared on websites, been published in newsletters and have gone out in broadcast faxes. The announcements have covered topics including:

1. The introduction of the new online file and pay system for businesses.
2. The introduction of the new online business registration system.
3. The introduction of the partnership with the Small Business Center Network.
4. The sales tax holiday.
5. A change in reporting for alcoholic beverage excise tax returns.
6. The phase-out of the excise tax on piped natural gas.

Many of these same announcements are also sent to tax preparer organizations like the N.C. Association of CPAs and the N.C. Society of Tax Professionals. These organizations also use the announcements frequently, which helps the Department reach businesses that employ professional tax preparation assistance.

Improving Existing Outreach Efforts

Department representatives have always been available to speak to groups of taxpayers about tax issues. This year the Department began offering public speaking training to its tax experts to improve the quality of its outreach efforts. This training covers the basics of public speaking, translating tax jargon into plain language and answering questions effectively in light of the Small Business Protection Act. It also includes a practical exercise in which the attendees make a presentation to their colleagues and receive feedback. Approximately 50 people have gone through the training and the feedback has been tremendous. Many of the attendees have reported back on how their presentations have improved and on the positive responses from their audiences.

The Department offers a comprehensive website as an information resource for taxpayers (including small business owners). Newcomers to the site often report that it is difficult to navigate and that they don't know which tax laws apply to them. In one of the first steps toward improving the site, the Department launched a Taxpayer Education section on the site. This new section helps taxpayers (including small business owners) navigate the site and find the information they need. It provides shortcuts to:

- Information about Tax Seminars and Presentations offered by the Department
- Current Tax Announcements
- Technical Bulletins, Directives and Notices
- Brochures and other Publications

Customer Service Initiatives

January 27, 2009

Page 6

This section was just launched recently. The Department will continue adding more content to make the section more robust and useful for small business owners.

Our Motor Fuels Division conducts annual motor carrier seminars throughout the State, usually during the month of August. In 2008, we conducted 2 seminars in Hickory, 1 in Charlotte, 1 in Asheboro, 1 in Greenville, 1 in Wilmington, and 1 in Cary. There was 56% attendance based on registration forms. Approximately 400 taxpayers attended the seminars. We have been conducting motor carrier seminars since 1999.

4 A review of the Department's efforts to ensure that taxpayers are informed of their rights to request written advice from the Department upon which they may reasonably rely.

The Department maintains a website section entitled "Verbal Advice" that addresses both verbal and written advice. It explains how a taxpayer can request written advice, as well as when and how the Department will document verbal advice given to a taxpayer.

This information is also included in the Department's 2008 Tax Law Change document. It was included in the sales and use tax law change information sent to all registered taxpayers.

Our tax seminars conducted at the Small Business Centers also include information on how to get help and information from the Department. Most of the instructors cover written advice regardless of the seminar topic. The seminar on Dealing with the Department covers the common interactions small business owners have with the Department. It includes specific information on how a taxpayer can request written advice.

5. A review of the Department's plan to record telephone calls at the Department's Taxpayer Assistance Center.

The Department has evaluated call recording software for the TACC. A Service Level Request for call recording will be submitted after a final price quote is provided by ITS.

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