



NORTH CAROLINA GENERAL ASSEMBLY

Session 2017

Fiscal Analysis Memorandum

CONFIDENTIAL

Requestor: House Finance Committee
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RE: PCS to S153n1

SUMMARY TABLE

FISCAL IMPACT OF PCS S153, V.1 (\$ in millions)

	<u>FY 2018-19</u>	<u>FY 2019-20</u>	<u>FY 2020-21</u>	<u>FY 2021-22</u>	<u>FY 2022-23</u>
State Impact					
General Fund Revenue	(44.3)	(47.4)	(50.7)	(54.1)	(57.6)
Less Expenditures	-	12.7	13.4	14.1	14.8
General Fund Impact	(44.3)	(60.1)	(64.1)	(68.2)	(72.4)
NET STATE IMPACT	(\$44.3)	(\$60.1)	(\$64.1)	(\$68.2)	(\$72.4)
Local Impact					
Local Revenue	(8.5)	(10.2)	(10.5)	(10.3)	(10.6)
Less Local Expenditures	-	-	-	-	-
NET LOCAL IMPACT	(\$8.5)	(\$10.2)	(\$10.5)	(\$10.3)	(\$10.6)

FISCAL IMPACT SUMMARY

Military Retirement Income Tax Deduction

Allows a deduction for military retirement and survivorship benefits. Benefits paid to retirees who had earned five years of creditable service in the Military Retirement System as of August 12, 1989 and their survivor beneficiaries are already deductible and may not be deducted twice. This memo assumes this provision is effective for taxable years beginning on or after January 1, 2018.

Disabled Veteran Property Tax Exclusion

Increases the Disabled Veteran Property Tax Exclusion from \$45,000 to \$100,000 of the

homestead appraised value and reimburses local governments for the revenue lost from valuations above \$45,000. This memo assumes this provision is effective for taxable years beginning on or after July 1, 2019.

Emergency Personnel Surviving Spouse Exclusion

Creates a homestead property tax exemption for the surviving spouse of an emergency personnel officer who was killed in the line of duty. This memo assumes this provision is effective for taxable years beginning on or after July 1, 2019.

Linens Sales and Use Tax

Authorizes the Secretary of Revenue to reduce certain tax assessments related to sales or use tax collections on linen rentals by 100%. This provision is not applicable to assessments related to incorrect application of the law for a period beginning on or after and assumed date of July 1, 2018.

Cranes Sales and Use Tax

Under North Carolina tax law, sales of tangible personal property are subject to Sales or Use taxes unless the tangible personal property is specifically exempted from tax in statute. The proposed legislation would create a statutory sales and use tax exemption for cranes, which would reduce both State and local sales tax revenue.

FISCAL ANALYSIS

Military Retirement Income Tax Deduction

Under the “Bailey Settlement,” military retirement income that is based on military service that includes at least five years of creditable service earned prior to August 1989 is exempt from North Carolina income tax. Senate Bill 153 exempts military retirement income that does not qualify for exemption under the “Bailey Settlement.”

To determine the amount of military retirement income that is not eligible for exemption, Fiscal Research obtained 2016 data on the total amount of military retirement benefits paid to North Carolina residents who first earned service after 1984 from DOD. This analysis assumes that all military retirement benefits based on service earned after 1984 are subject to taxation under current law. Projections of benefit payments were based on the growth predicted in the FY 2014 Valuation of the Military Retirement System.

The share of pension income that is subject to State income tax will increase each year because new retirees are less likely to meet the criteria required for exemption under the “Bailey Settlement.” To determine this share, Fiscal Research used data provided by DOD about retirees’ average years of service and year of retirement to approximate first year of employment for current retirees. This was used to approximate the share of benefit payments that would be eligible for the Bailey exemption each year, assuming no breaks in service during the first five years of employment. The share of benefits that would not be eligible for the Bailey exemption was multiplied by the total amount of benefits to determine the amount of income eligible for the tax deduction. The fiscal impact was calculated by multiplying this amount by an estimated effective tax rate of 3.5 percent. Because the military retirement system does not automatically

withhold state tax income, the impact for FY 2018-19 is assumed to equal the full-year impact of tax year 2018, -\$24.8 million.

Disabled Veteran Property Tax Exclusion

The third edition increases the exclusion amount from the first \$45,000 of home value to the first \$100,000. To determine the fiscal impact, the American Community Survey (ACS) was used to determine the percentage of NC homes valued at less than \$100,000. Homes valued at less than \$100,000 would receive an exclusion based on the value of the home because the total value is less than the exclusion amount of \$100,000. Homes valued higher would receive an exclusion of the first \$100,000.

Based on the ACS data, the average value of homes less than \$100,000 was calculated and used to determine the total value for all qualifying homes under \$100,000. The ACS data was also used to calculate the value of qualifying homes over \$100,000 that would receive the full exclusion. The values for home below and above \$100,000 are added together to get the total value of excluded property. The amount currently excluded is subtracted to determine the additional value excluded under the bill. Finally, the statewide weighted average tax rate of 94.3 cents per \$100 value is used to determine the amount of property tax loss, which is equal to the hold harmless amount. Moody's Analytics projections for existing home prices are used to determine the increase in cost for future years.

Emergency Personnel Surviving Spouse Exclusion

Based on data from the Department of State Treasurer, a total of 371 emergency personnel have been eligible for death benefit payments since 1971. The death benefit payment is made to the dependents of emergency personnel killed in the discharge of their official duties.

Assuming a total of 371 eligible beneficiaries and a median home value for NC of \$154,900, the cost of the bill in lost property tax revenue to counties and municipalities would be approximately \$700,000. It is not known how many of the 371 personnel have unmarried surviving spouses or if there are eligible surviving spouses of personnel killed prior to 1971. Therefore, it is not possible to estimate the cost more precisely; however, given the length of time covered by the data, the cost is estimated to be less than \$700,000.

Linens Sales and Use Tax

In S.L. 2017-204, Sec. 2.8A, the General Assembly authorized the Department of Revenue (DOR) to reduce by up to 90% a sales and use tax assessment against a taxpayer who failed to collect or remit sales and use tax on rental linens under certain circumstances. Based on data provided by DOR at that time regarding audits and assessments related to collection of sales or use taxes on linen rentals, the revenue loss from the tax law change was estimated to be 500,000. Allowing DOR to reduce the assessment by the full 100% would cost an additional \$56,000.

Cranes Sales and Use Tax

Creating a sales and use tax exemption for the sale of cranes would reduce sales and use tax revenue for both the State and local governments.



The North Carolina Department of Revenue does not collect data on the amount of sales tax revenue generated by specific categories of items sold in the State, so no definitive data exists on the fiscal impact of exempting cranes from taxation. The estimate presented here is based on data found in the US Census Bureau's 2012 Economic Census for North Carolina. The Economic Census reports that sales in North Carolina by retailers of "overhead traveling crane, hoist, and monorail system[s]" totaled approximately \$411 million when inflated to 2019 dollars. This equates to a State revenue loss of \$19.5 million based on the State's 4.75% sales and use tax rate, plus a loss for local governments of approximately \$8.5 million. Because this category in the Economic Census includes items besides cranes, these estimates may be higher than the actual fiscal impact. However, it should be noted that some of the items also included in this Economic Census category, such as monorail production, are not prevalent in the State's economy, which reduces the uncertainty of this estimate.

TECHNICAL CONSIDERATIONS

N/A.

DATA SOURCES

U.S. Census Bureau; NC Dept. of Revenue; Moody's Analytics; NC Dept. of State Treasurer

United States Department of Defense

- Data provided by the Office of the Actuary
- Data from the Office of the Secretary of Defense and the Joint Staff
- FY 2014 Valuation of the Military Retirement System
- FY 2001 – FY 2015 Military Retirement System Statistical Reports
- Defense Manpower Data Center December 2016 Report of Military and Civilian Personnel by Service/Agency by State/Country

FISCAL ANALYSIS MEMORANDUM – PURPOSE AND LIMITATIONS

This document is a fiscal analysis of a bill, draft bill, amendment, committee substitute, or conference committee report that is confidential under Chapter 120 of the General Statutes. The estimates in this analysis are based on the data, assumptions, and methodology described in the Fiscal Analysis section of this document. This document only addresses sections of the bill that have projected direct fiscal impacts on State or local governments and does not address sections that have no projected fiscal impacts. This document is not an official fiscal note. If a formal fiscal note is requested, please email your request to the Fiscal Research Division at FiscalNoteRequests@ncleg.net or call (919) 733-4910.

