2000 Tax Law Changes

REFORM LOCAL TAX ON RENTAL CARS

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-2	**SB 1076**	**Senator Cooper**

AN ACT TO REPEAL THE PROPERTY TAX ON CERTAIN VEHICLES LEASED OR RENTED UNDER RETAIL SHORT-TERM LEASES OR RENTALS AND TO REPLACE THE TAX REVENUE WITH A LOCAL TAX ON GROSS RECEIPTS DERIVED FROM RETAIL SHORT-TERM LEASES OR RENTALS.

Overview: This act repeals the property tax on vehicles owned and offered for short-term rental by someone engaged in the business of renting vehicles to the public, and enacts in its place local option county and city gross receipts taxes on short-term vehicle rentals.

Fiscal Impact: There is no General Fund or Highway Fund impact. The property tax exemption will result in an annual loss to local governments of at least $5.6 million. Because the county and city gross receipts taxes are local option, it is not known how much revenue they would generate.

Effective Date: July 1, 2000.

Background & Analysis: This act excludes from property tax vehicles that are offered at retail for short-term lease or rental, if the vehicle is owned or leased by an entity engaged in the business of leasing vehicles short-term to the general public. A short-term lease or rental is a lease or rental for fewer than 365 continuous days. Under prior law, rental car businesses paid property taxes on their vehicle inventory.

The act replaces the property tax on short-term rental inventory with a local option gross receipts tax. Long-term rental inventory remains subject to property tax. In order to recover its revenue lost due to the property tax exclusion, each county and each city may levy a gross receipts tax of up to 1.5% on short-term vehicle rentals. A vehicle is defined as any of the following:

- A passenger-type vehicle (including vans and sports utility vehicles).
- A cargo-type vehicle other than (1) a truck over 26,000 pounds, (2) a truck used to transport commercial freight, or (3) a truck that requires the driver to have a commercial drivers license.
- A trailer or semitrailer under 6,000 pounds.

The tax would be collected and retained by the taxing city or taxing county and would apply to agreements under which the customer takes possession of the vehicle in the taxing city or county. The taxing city or county would administer the local gross receipts tax in the same manner as the sales tax and the alternate highway use tax on rental vehicles. The taxing city or county would have the same collection powers that the Secretary of Revenue has in collecting local sales taxes, and the same penalties and remedies would apply. The act provides that the tax will be passed on to the customer. The lease or rental agreement must specify the rate of the local gross receipts tax being charged.

The act requires the Fiscal Research Division to determine the total amount of revenue generated by local gross receipts taxes authorized by the act and compare that to the total amount of ad valorem taxes that would have been generated if the act had not excluded short-term rental vehicles. The Fiscal Research Division must report its findings to the 2003 session.

BONDS FOR HIGHER EDUCATION

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-3	**SB 912**	**Senator Rand**

AN ACT TO (1) TO AUTHORIZE THE ISSUANCE OF THREE BILLION ONE HUNDRED MILLION DOLLARS GENERAL OBLIGATION BONDS OF THE STATE, SUBJECT TO A VOTE OF THE QUALIFIED VOTERS OF THE STATE, TO PROVIDE FUNDS FOR CAPITAL IMPROVEMENTS FOR THE UNIVERSITY OF NORTH CAROLINA AND GRANTS TO COMMUNITY COLLEGES FOR CAPITAL IMPROVEMENTS AND (2) TO AUTHORIZE THE BOARD OF GOVERNORS OF THE UNIVERSITY OF NORTH CAROLINA TO ISSUE SPECIAL OBLIGATION BONDS FOR IMPROVEMENTS TO THE FACILITIES OF THE UNIVERSITY OF NORTH CAROLINA AND FOR THE UNIVERSITY OF NORTH CAROLINA HOSPITALS AT CHAPEL HILL AND OTHER FACILITIES OF THE UNIVERSITY OF NORTH CAROLINA HEALTH CARE SYSTEM.

Overview: This act known as the Michael K. Hooker Higher Education Facilities Finance Act, creates a new Chapter 116D of the General Statutes to establish the following mechanisms for debt financing of higher education facilities:

- It authorizes the State to issue general obligation bonds to finance $2.5 billion of capital facilities for the University of North Carolina and $600 million of capital facilities for community colleges. The bonds would be subject to approval by the voters in the November 2000 statewide general election.

- It authorizes the UNC Board of Governors to issue special obligation bonds to finance capital facilities for the University. The University's receipts other than tuition or appropriations from the General Fund would secure the bonds. S.L. 2000-168 sets forth the first projects that will be funded by special obligation bonds.

Fiscal Impact: The act limits the maximum amount of general obligation bonds that may be issued each year for the next six fiscal years. The debt service costs paid from the State General Fund will be $28.7 million for fiscal year 2001-2002, increasing to $194.9 million by fiscal year 2004-2005.

Effective Date: The act became effective May 25, 2000.

Background & Analysis: Eva Klein, consultant to the Board of Governors for the study of the equity and adequacy of capital facilities, prepared a report detailing the deterioration of the current facilities of The University of North Carolina. In response to this report, the General Assembly began considering a significant bond proposal in 1999. The Speaker and the President Pro Tempore appointed a conference committee towards the end of the 1999 Session to consider the differences between the houses on the bond bill. During the interim, a Joint Select Committee on Higher Education Facilities Needs met and toured various campuses within the University of North Carolina and the North Carolina Community College System. Shortly after the convening of the 2000 Session, the General Assembly enacted this act.

This act creates two different funding mechanisms to finance higher education facilities. First, it authorizes the State to issue $3.1 billion of general obligation bonds to finance capital facilities for the University of North Carolina and for community colleges. The voters in the November 2000 statewide general election must approve the bonds before they may be issued. The UNC projects that can be financed with the bond revenues are set out in this act. Second, it authorizes the UNC Board of Governors to issue special obligation bonds to finance capital facilities for the University. The bonds would not be subject to a referendum because they are not secured by the taxing power of the State. The University's receipts other than tuition or appropriations from the General Fund would secure the bonds. Although this act does not authorize any particular projects, S.L. 2000-168 gives legislative approval for at least one project financed with special obligation bond revenues. The act also imposes reporting requirements to allow the General Assembly to monitor all aspects of the proposed bonds.

General Obligation Bonds

Article 2 of the new Chapter 116D created by this act authorizes the State to issue university improvement general obligation bonds to acquire, construct, and improve University property and Article 4 of the new Chapter 116D authorizes the State to issue community college general obligation bonds to acquire, construct, and improve community college property. Both bonds must be approved by the voters of the State in a single ballot question in November 2000. If a majority of those voting on the question do not approve the bonds, neither the UNC bonds nor the Community College bonds can be issued.

The university improvement general obligation bonds would be used for construction, improvement, and acquisition of capital facilities for constituent and affiliated institutions of The University of North Carolina, including the Center for Public Television, the UNC Health Care System, the School of Science and Mathematics, and the North Carolina Arboretum. Similarly, the community college general obligation bonds would be used for grants to community colleges for construction, improvement, and acquisition of their capital facilities. The act specifically defines capital facilities as buildings, utilities, structures, and other facilities and property developments, including streets, landscaping, equipment, and furnishings in connection with a building project, and land acquisition. The facilities may include physical education facilities, housing, and administrative offices as well as educational buildings.

The bonds would be issuable by the Treasurer only to fund allocations established by the General Assembly; those allocations are set out in this act. The act limits the amount of bonds that may be issued each year over six years as follows:

Fiscal Year	University	Community Colleges
2000-2001	$201,600,000	$ 48,400,000
2001-2002	241,900,000	58,100,000
2002-2003	483,900,000	116,100,000
2003-2004	483,900,000	116,100,000
2004-2005	564,500,000	135,500,000
2005-2006	524,200,000	125,800,000

The full faith and credit and the taxing power of the State would secure the proposed general obligation bonds; a statement to this effect would appear on the face of the bonds. These general obligation bonds would be repaid from the General Fund. The maximum maturity on the bonds would be 25 years.

The allocations established in the act include a $25 million reserve for repair and renovations and cost overruns. If the cost of a project changed, the Board of Governors could reallocate funds from one project to another, but only between projects at the same institution. The act states the intent of the General Assembly that the repairs and renovations shall preserve the historical and architectural fabric of the buildings.

The act also sets out the amount allocated to sites at each community college for new construction and for repairs and renovations and requires that the allocations must be used in accordance with the State Board of Community Colleges' funding formulas for new construction needs and repair and renovation needs at each community college. A community college could reallocate to another site new construction funds that the consultant's report allocates to a specific site only if (1) the community college finds that the funds are not needed at the site for which the report allocates them and (2) the State Board approves the reallocation, except that funds allocated to a site away from the main campus county may not be reallocated back to the main campus county. Bond proceeds allocated for repair and renovations could be used only for repair and renovations, but bond proceeds allocated for new construction could be used either for new construction or for repair and renovations. The local board of trustees is directed to allocate repair and renovation funds in accordance with need, subject to approval by the State Board of Community Colleges.

Under general law, community colleges are required to match State capital funds on a dollar-for-dollar basis. The act provides three limited exceptions to this requirement for the bond proceeds. First, bond proceeds allocated for repair and renovations need not be matched. Second, community colleges that the consultant's report determined had a matching ability of less than 40%, based on ability to pay, need not match allocations for new construction. Third, community colleges which the consultant's report determined had a matching ability of 40% or more must match new construction allocations only at the matching ability percentage assigned to them in the report. If any community colleges could not meet their matching requirements by July 1, 2006, the funds that were not matched would be pooled and reallocated among those community colleges that had met their requirements, based on capital improvement needs determined by the State Board of Community Colleges.

Under current law, a community college project in the amount of $100,000 or more is subject to approval and supervision by the State Construction Office under G.S. 143-341. An exception created under this act limits the approval and supervision requirement for bond-funded projects to those that exceed $250,000.

UNC Special Obligation Bonds

Article 3 of the new Chapter 116D created by this act authorizes the UNC Board of Governors to issue a second type of self-liquidating bonds, known as special obligation bonds. Prior to the enactment of this act, the Board of Governors could issue revenue bonds. Revenue bonds are payable from rentals, charges, fees, and other revenues, such as gifts. This act broadens the authority of the Board by allowing it to issue special obligation bonds payable with any sources of income or receipts of the Board of Governors or a constituent or affiliated institution, but not including tuition payments or appropriations from the General Fund. Special obligation bond proceeds may be used for construction, improvement, and acquisition of any capital facilities located at UNC constituent and affiliated institutions. The maximum maturity on the bonds is 25 years.

Special obligation bonds are not general obligation bonds and thus are not required to be approved by the voters. The full faith and credit or the taxing power of the State does not secure them and a statement to this effect would appear on the face of the bonds. Property could not be pledged to secure the bonds. The Board of Governors' pledge of obligated resources would secure the bonds. Obligated resources, defined in G.S. 116D-22, would include rents, charges, or fees to be derived by the Board of Governors or a constituent institution from any activity, earnings on the investment of an endowment fund, and funds to be received from grants and contracts. Obligated resources would not include tuition payments or appropriations of general revenues. Obligated resources derived from one institution could not be used to finance a bond project located at a different institution.

To the extent the generation of obligated resources is within the control of the Board of Governors, the Board is authorized and required to increase the underlying fees or charges as necessary to generate sufficient revenues to pay the bonds. An individual institution can not increase a fee or charge without approval of the Board of Governors. The Board must set aside a sufficient amount of obligated resources on a regular basis into a sinking fund pledged to pay the principal and interest on the bonds. The act provides that the State pledges and contracts that it will not limit or alter the rights vested in the Board of Governors with respect to the bonds as long as any bonds are outstanding.

Special obligation bonds may be issued only for projects specifically authorized by the General Assembly, as is the current practice for revenue bonds (self-liquidating bonds). Although this act does not give specific legislative approval for special obligation bond projects, S.L. 2000-168 provides for at least one project financed through special obligation bond proceeds.

The amount of special obligation bonds that can be issued is limited by the extent to which the Board of Governors finds that sufficient obligated resources are "reasonably expected" to be available to pay the debt service. In submitting proposed special obligation bond projects to the General Assembly for approval, the Board of Governors must justify the need for each project and must itemize the cost of the project, the estimated operating costs upon completion, and the sources and amounts of obligated resources to be pledged for repayment of the bonds. The Board of Governors may submit a proposed project for approval by the General Assembly only if the project has been approved by the board of trustees of the institution at which the project would be located.

Reports and Oversight

The act imposes reporting requirements to allow the General Assembly to monitor all aspects of the proposed bonds. The State Treasurer is required to report annually, and upon each issuance of university improvement general obligation bonds and community college general obligation bonds, on debt service requirements for the bonds. The Community Colleges System Office is required to report quarterly to the Joint Legislative Education Oversight Committee on projects funded from community college general obligation bonds, including total project costs, the amount funded by bonds, expenditures to date, and progress to completion. And the Board of Governors is required to report annually to the Joint Legislative Commission on Governmental Operations on the following:

- The university improvement general obligation bonds, including total project costs, amount funded by bonds, expenditures to date, progress to completion, and estimated operating costs and their proposed source of payment.

- The special obligation bonds, including, for each institution, outstanding debt, specific projects, debt service requirements, actual repayments, compliance with all applicable financial requirements, and trends and revenue streams for obligated resources.

The act also creates a Higher Education Bond Oversight Committee, which will consist of ten members appointed as follows: three by the Speaker of the House of Representatives, three by the President Pro Tempore of the Senate, two by the UNC Board of Governors, and two by the State Board of Community Colleges. It has the authority to receive reports and information from the facilities officers at UNC and its institutions, from the State Treasurer and the State Construction Office, from the Community Colleges System facilities officers, and from representatives of individual community colleges. It is required to review this information and make recommendations regarding the issuance of the bonds and the construction of the projects.

The act provides that existing minority business participation goals apply to projects funded with the bond proceeds. It requires annual reports on this issue to the General Assembly from the State Construction Office and the Board of Governors with respect to university improvement bonds and from the Community Colleges System Office with respect to community college bonds.

The act requires the State Treasurer to provide contracting opportunities for historically underutilized businesses in providing professional services in connection with the issuance of the bonds. It directs the State Treasurer to strive to increase the amount of legal, financial, and other professional services acquired by it from historically underutilized businesses, and to report quarterly to the Office for Historically Underutilized Businesses in the Department of Administration

The act directs the Board of Governors to continue to study and monitor any inequities in funding for capital improvements and facilities needs which may still exist on North Carolina's public historically black colleges and universities and the University of North Carolina at Pembroke, beyond the funding of the projects provided for in the act. The Board must report annually to the Joint Legislative Commission on Governmental Operations on any remaining inequities found, including recommendations as to how those inequities should be addressed.

Repairs and Renovations

The act contains two uncodified sections addressing the issue of maintaining the Universities' capital facilities. In the act, the General Assembly finds that the facilities of the universities have been allowed to deteriorate due to inadequate maintenance. Through the act, the General Assembly commits to responsible stewardship of the facilities by requiring monitoring and reporting of the conditions of all facilities and their needs for repair and renovation. The act states the intent of the General Assembly to assure that adequate oversight, funding, and accountability is continually provided with respect to the maintenance of university facilities. The Board of Governors must report annually to Governmental Operations and Education Oversight on the condition of all university capital facilities, the status of ongoing repair and renovation projects, and needs for additional funding. In addition, the act requires the Board of Governors to study the current repairs and renovation funding formula and make recommendations regarding its adequacy, scope, and methodology.

EXCISE TAX ON TIMBER CONTRACTS

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-16	**HB 1545**	**Representative Pope**

AN ACT TO CLARIFY THAT THE EXCISE TAX ON CONVEYANCES APPLIES TO TIMBER DEEDS AND CONTRACTS FOR THE SALE OF STANDING TIMBER.

Overview: This act clarifies that the State excise tax on instruments conveying an interest in real property applies to timber deeds and contracts for the sale of standing timber. The Revenue Laws Study Committee recommended this legislation to end any confusion resulting from two court decisions regarding the treatment of timber deeds and contracts for the sale of standing timber.

Fiscal Impact: No impact.

Effective Date: The act became effective July 1, 2000, and applies to timber deeds and contracts for the sale of standing timber executed on or after that date.

Background & Analysis: Historically, timber interests have been treated as an interest in real property, and the State excise tax on conveyances has been applied to deeds conveying timber. With the adoption of the Uniform Commercial Code, the sale of standing timber was deemed to be a sale of goods. Two North Carolina court decisions have addressed timber rights since the adoption of the UCC. The cases have led to disagreement among legal scholars and registers of deeds as to whether contracts for the sale of standing timber and timber deeds constitute a sale of personal property or a sale of real property for purposes of the excise tax on conveyances.

The proponents of timber as real property claim that these court decisions refer to timber as goods under the UCC only when the timber is subject to a contract for sale. The proponents of timber as personal property claim that both contracts and deeds for the sale of timber are governed by the UCC and, therefore, do not convey an interest in real property. This act clarifies that the excise tax on instruments conveying an interest in real property applies to timber deeds and contracts for the sale of standing timber. For purposes of Article 8E, Excise Tax on Conveyances, the timber will be treated as if it were real property. The act remedies any confusion resulting from the court decisions regarding the treatment of timber deeds and contracts for the sale of standing timber.

The excise tax on conveyances applies to conveyances of an interest in real property. The tax is imposed at the rate of $1.00 on each $500.00 or fractional part of the consideration or value of the interest or property conveyed. It is payable to the register of deeds at the time the interest in the property is recorded. One-half of the money generated by the tax stays with the county and the remainder is remitted to the State and credited to the Parks and Recreation Trust Fund and the Natural Heritage Trust Fund.

North Carolina adopted the UCC as Chapter 25 of the General Statutes in 1965. G.S. 25-2-107(2), as amended in 1975, provides that "(a) contract for the sale … of timber to be cut is a contract for the sale of goods within this article…" Consequently, the excise tax should not be imposed on timber deeds or contracts for the sale of standing timber if they are sales of personal property. However, G.S. 25-2-107(3) recognizes that a contract for the sale of standing timber can be treated as a conveyance of real property: "The provisions of this section are subject to any third-party rights provided by the law relating to realty records, and the contract for sale may be executed and recorded as a document transferring an interest in land and shall then constitute notice to third parties of the buyer's rights under the contract for sale."

There have been two North Carolina cases that have ruled on timber rights since the adoption of the UCC. In *Mills v. New River Wood Corp.,* 77 N.C. App. 576, 333 S.E.2d 759 (1985), the Court ruled that contracts for the sale of "timber to be cut" were governed by G.S. 25-2-107(2). In *Mills,* the cause of action was based on a timber deed, which the Court described as evidencing the underlying contract of sale. In a more recent case, the North Carolina Supreme Court concluded that when North Carolina adopted the UCC, it began classifying timber as goods when timber was the subject of a contract for sale. *Fordham v. Eason,* 521 S.E. 2d 701 (1999).

Despite these recent court decisions that argue timber deeds are personal property, most registers of deeds have continued to impose an excise tax on transfers of interests in timber deeds and contracts. This act ends the confusion by expressly providing that the excise tax on instruments conveying an interest in real property applies to timber deeds and contracts for the sale of standing timber.

EXEMPT DISABLED VETERAN VEHICLES

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-18	**HB 133**	**Representative Rogers**

AN ACT TO EXEMPT FROM PROPERTY TAX MODIFIED MOTOR VEHICLES OWNED BY DISABLED VETERANS WHO ARE ELIGIBLE FOR FEDERAL SPECIAL EQUIPMENT ALLOWANCES.

Overview: This act exempts motor vehicles that are (1) owned by veterans with certain service-related disabilities and (2) altered with special equipment to accommodate the service-related disability from property tax.

Fiscal Impact: The act will not affect State revenues. It will reduce revenues of local governments by approximately $120,00 per year.

Effective Date: Effective for tax years beginning on or after July 1, 2000.

Background & Analysis: Under current law, a property tax exemption is granted to vehicles that the U.S. government gives to veterans on account of disabilities they suffered in World War II, the Korean Conflict, or the Vietnam Era. This act also gives a property tax exemption to vehicles owned by veterans with certain service-related disabilities when the vehicles have been altered to accommodate the disability. Vehicles owned by these veterans and so altered would be eligible for the property tax exemption. To qualify for the exemption, the person must meet the following requirements under federal law:

- Veteran – Be a person who served in active military, naval, or air service, and who was discharged or released under conditions other than dishonorable.

- Service-related disability – Be disabled from an injury incurred or disease contracted in or aggravated by active service. The disability must be loss of one or both hands or feet, permanent loss of use of one or both hands or feet, or permanent impairment of vision of both eyes.

- Adaptive equipment – Have a vehicle that has been adapted for the disability. Adaptive equipment includes, but is not limited to, power steering, power brakes, power window lifts, power seats, and special equipment necessary to assist the veteran into and out of the automobile or other conveyance. The term also includes (1) air-conditioning equipment when the equipment is necessary to the health and safety of the veteran and to the safety of others, regardless of whether the vehicle is to be operated by the veteran or for the veteran by another person, and (2) any modification of the size of the interior space of the vehicle if needed because of the physical condition of the veteran in order for the veteran to enter or operate the vehicle.

The United States Department of Veterans Affairs (VA) offers a one-time payment of up to $8,000 towards the purchase of an automobile to all eligible veterans. In addition, the VA will also pay for adaptive equipment and for the repair, replacement, or reinstallation of adaptive equipment. Veterans who are eligible for these federal benefits will also be entitled to the tax exemption provided by this act.

In order to receive the exemption, the veteran must first file an application with the county assessor. Once an approved exemption is on file, it remains in effect and the vehicle is omitted from the tax rolls. The application need not be renewed each year.

DRY CLEANING SOLVENT CLEANUP AMENDS.

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-19	**HB 1326**	**Representative Gibson**

AN ACT TO DESIGNATE THE STATE SALES TAX REVENUE FROM DRY-CLEANING AND LAUNDRY SERVICES TO THE DRY-CLEANING SOLVENT CLEANUP FUND; TO INCREASE THE STATE SALES TAX ON DRY-CLEANING SOLVENTS; TO AMEND THE DRY-CLEANING SOLVENT CLEANUP ACT OF 1997 TO REPEAL THE REQUIREMENT OF FINANCIAL RESPONSIBILITY FOR DRY-CLEANING FACILITES AND WHOLESALE DRY-CLEANING SOLVENT DISTRIBUTION FACILITIES; TO ALLOW THE ENVIRONMENTAL MANAGEMENT COMMISSION TO ENTER INTO CONTRACTS WITH PRIVATE CONTRACTORS FOR ASSESSMENT AND REMEDIATION ACTIVITES AT DRY-CLEANING SOLVENT DISTRIBUTION FACILITES; TO DIRECT THE SECRETARY OF ENVIRONMENT AND NATURAL RESOURCES TO STUDY THE USE OF DRY-CLEANING SOLVENTS IN NORTH CAROLINA, AND TO MAKE OTHER CHANGES IN THE DRY-CLEANING SOLVENT CLEANUP ACT OF 1997.

Overview: This act earmarks a percentage of the State sales and use taxes collected on dry-cleaning and laundry services to the Dry-Cleaning Solvent Cleanup Fund, increases the privilege and excise taxes on dry-cleaning solvents, and clarifies that the sales tax is treated as part of the sales price for services as well as tangible personal property.

Fiscal Impact: Beginning in fiscal year 2003-2004, approximately $9.1 million per year will be transferred from the General Fund to the Dry-Cleaning Solvent Cleanup Fund due to the earmarking of State sales and use taxes collected on dry-cleaning and laundry services. The increase in the privilege and excise taxes on dry-cleaning solvents will generate an additional $500,000 in revenue each year for the Dry-Cleaning Solvent Cleanup Fund. The provision that clarifies that the sales tax is treated as part of the sales price for services as well as tangible personal property has no effect on State revenues.

Effective Date: The earmarking of sales and use tax proceeds becomes effective April 1, 2003, and expires June 30, 2010. The increase in the privilege and excise taxes becomes effective October 1, 2001, and expires January 1, 2010. The clarifying provision became effective June 26, 2000.

Background & Analysis*:* The Dry-Cleaning Solvent Fund was created by the General Assembly in 1997. The Fund is to be used to reimburse persons who clean up sites polluted by dry-cleaning solvents that have contaminated the water or surface or subsurface soils of the State. The Department of Environment and Natural Resources administers the Fund. Under current law, the major source of revenue for the Fund is a dry-cleaning solvent tax on in-state retailers that sell solvent to dry-cleaning facilities, and on dry-cleaning facilities that purchase solvent outside the State. The solvent tax is a per gallon privilege tax equal to $5.85 per gallon of chorine-based solvents, and 80 cents per gallon of hydrocarbon-based solvents. The tax became effective October 1, 1997 and expires January 1, 2010. The Department of Revenue collects the tax in the same manner as a sales tax.

This act increases the revenues of the Fund in two significant ways. First, under this act, at the end of each quarter, the Department of Revenue will transfer fifteen percent (15%) of the net revenues collected from the sales and use tax on dry-cleaning and laundry services in the previous fiscal year. Under current law, the 4% State sales and use tax is imposed on the gross receipts of the following retailers:

- Persons engaged in the business of operating a dry-cleaning, pressing, or hat-blocking establishment, a laundry, or any similar business.

- Persons engaged in the business of renting clean linen or towels or wearing apparel, or any similar business.

- Persons engaged in the business of soliciting cleaning, pressing, hat blocking, laundering, or linen rental business for any of these businesses.

The following receipts are exempt from the State sales and use tax: receipts derived from services performed for resale by a retailer that pays the tax on the total gross receipts derived from the services; and receipts derived from coin, token, or card-operated washing machines, extractor, and dryers.

Second, this act increases the rate of the privilege tax imposed on the dry-cleaning solvent retailer and the rate of the excise tax imposed on dry-cleaning solvent purchased outside of the State for storage, use, or consumption within the State. The privilege tax and excise tax rate is raised from $5.85 per gallon to $10.00 per gallon for dry-cleaning solvent that is chlorine-based. The privilege tax and excise tax rate is raised from $.80 per gallon to $1.35 per gallon for dry-cleaning solvent that is hydrocarbon based.

HEALTH CARE FACILITY/CCRC TAX EXEMPT

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-20	**HB 1573**	**Representative Jarrell**

AN ACT TO CLARIFY THE PROPERTY TAX TREATMENT OF A HEALTH CARE FACILITY UNDERTAKEN BY THE MEDICAL CARE COMMISSION PURSUANT TO THE HEALTH CARE FACILITIES FINANCE ACT AND TO EXTEND THE SUNSET ON THE PROPERTY TAX EXEMPTION FOR CONTINUING CARE RETIREMENT CENTERS.

Overview: This act does two things. First, it provides that the current property tax exemption for continuing care retirement centers (CCRCs) will remain in effect for one more year, by extending the exemption's sunset from July 1, 2000, to July 1, 2001. Second, it clarifies the property tax exemption for health care facilities financed with bonds or notes issued by the Medical Care Commission in two ways:

- The amount of the exemption cannot exceed the lesser of the principal amount of the bonds or notes or the assessed value of the facility.

- Only the part of a health care facility financed by bonds or notes issued by the Medical Care Commission is exempt from property tax. When bonds or notes are used to finance an expansion or a renovation of an existing facility, only the new part of the facility or the renovated part of the facility may be exempt from property tax, not the entire facility.

Fiscal Impact: The act has no fiscal impact on State revenues. The extension of the sunset of the CCRC property tax exemption has no fiscal impact on local governments. The Medical Care Commission bond clarification will not affect facilities funded under existing bonds. Since Fiscal Research cannot anticipate the amount of bonds to be issued in the future to these facilities, no fiscal estimate is possible.

Effective Date: The extension of the sunset of the CCRC property tax exemption became effective July 1, 2000. The clarification of the property tax exemption for facilities financed with bonds issued by the Medical Care Commission act becomes effective October 1, 2000, and applies to bonds or notes issued on or after that date.

Background & Analysis: The Revenue Laws Study Committee recommended two property tax proposals that were combined into this one act:

Extension of the Property Tax Exemption for CCRCs

North Carolina has long exempted from property tax homes for the aged, sick, and infirm if the homes are used exclusively for a charitable purpose and the owner of the property is not organized for profit. (G.S. 105-278.6) In 1983 and 1984, the North Carolina courts ruled that two retirement homes that had sought to claim this property tax exemption did not qualify because the homes were not charitable. In response to the courts' rulings, the General Assembly enacted a property tax exemption in 1987 for certain homes for the "aged, sick, or infirm". To qualify for the exemption, a CCRC did not have to be operated as a charity, but it did have to be owned and operated by a nonprofit organization that was a religious or Masonic organization. (G.S. 105-275(32))

In 1998, Springmoor, Inc., a nonprofit corporation that manages and operates a self-contained residential community for the elderly, successfully challenged the constitutionality of the 1987 legislation. Springmoor alleged that its center met all the requirements of G.S. 105-275(32), except that it was not affiliated with a religious or Masonic organization as required by a subpart of the statute. The North Carolina Supreme Court agreed that the statute violated the First Amendment because it was an unconstitutional establishment of religion. Instead of severing the unconstitutional subpart from the statute, which would have given Springmoor exempt status, the Court ruled the entire statute unconstitutional. The Court explained that it was not the General Assembly's intent to provide a blanket exclusion for all nonprofit homes for the elderly.

After the *Springmoor* decision, the General Assembly enacted G.S. 105-278.6A. This statute temporarily revises the property tax exemption for retirement communities that was held unconstitutional in *Springmoor*. The exemption was scheduled to expire July 1, 2000. The Revenue Laws Study Committee appointed a subcommittee consisting of interested parties (including representatives of the CCRCs, the counties, and the tax assessors) to review the tax status of the CCRCs and to seek a compromise. During its six meetings, the subcommittee discussed numerous proposals and looked at other states' laws. Because the subcommittee did not reach a consensus, it recommended extension of the sunset on the property tax exemption for one year, until July 1, 2001, in order to give all interested parties more time to seek a compromise.

Medical Care Commission Bonds

This act clarifies the property tax exemption for health care facilities financed with bonds or notes issued by the Medical Care Commission in two ways:

- The amount of the exemption cannot exceed the lesser of the principal amount of the bonds or notes or the assessed value of the facility.

- Only the part of a health care facility financed by bonds or notes issued by the Medical Care Commission is exempt from property tax. When bonds or notes are used to finance an expansion or a renovation of an existing facility, only the new part of the facility or the renovated part of the facility may be exempt from property tax, not the entire facility.

In 1975, the General Assembly enacted the Health Care Facilities Finance Act to help and encourage the modernization and expansion of the State's health care facilities. Under the Act, the Medical Care Commission may issue bonds or notes to finance the cost of building or improving health care facilities for public or nonprofit agencies. The Medical Care Commission indicates that over the last 20 years, approximately $5 billion in bonds or notes have been issued. Approximately 90% of these bonds or notes have been issued to hospitals for expansion and renovation of hospital facilities and for purchasing hospital equipment.

The Act provides that a health care facility financed through bonds or notes issued by the Medical Care Commission is exempt from property tax until the bonds or notes are retired. At the time the Act was enacted, the Medical Care Commission actually owned most, if not all, of the facilities financed through bond revenues until the bonds or notes were retired. Ownership was given to a public or nonprofit agency after the bonds or notes were retired. Today, the Commission does not generally own the facilities being financed; ownership remains with the public and nonprofit health care facilities requesting the financing. Most of these facilities are exempt from property tax under G.S. 105-278.8. The exemption being amended by this act was included in the law in 1975 because the Medical Care Commission did not fall within the tax exemption for charitable hospital purposes.

LINCOLN COUNTY E&R BOARD

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-40	**HB 1656**	**Representative Kiser**

AN ACT TO AUTHORIZE THE APPOINTMENT OF A SPECIAL BOARD OF EQUALIZATION AND REVIEW FOR LINCOLN COUNTY.

Overview: This act revises Lincoln County's authority to appoint a special board of equalization and review. Most notably, it allows the board to continue meeting after it has adjourned for the purposes of hearing and deciding appeals related to discovered property, classified motor vehicles, audits of property classified at present-use value, and audits of property exempted from or excluded from taxation.

Fiscal Impact: None

Effective Date: June 30, 2000

Background & Analysis: Under general law (G.S. 105-322), all counties must have a board of equalization and review (E&R board) to review the county's property tax listings and appraisals and to hear taxpayers' appeals. The E&R board is composed of the board of county commissioners unless the board of county commissioners adopts a resolution appointing a special board. This act makes local modifications to G.S. 105-322 for Lincoln County, setting forth specific qualifications for the E&R board and expanding its powers and duties. Specifically, this act makes the following local modifications to G.S. 105-322:

- **Membership**: This act provides that if the Lincoln County board of commissioners chooses to form a special E&R board, they must appoint five members and three alternate members. To be eligible for appointment, the person must have knowledge of or experience in real estate, fee appraisals, banking, farming, or other business management. Members serve two-year terms, and no member may serve more than three consecutive terms. The Lincoln County board of county commissioners will fill vacancies. Under general law, the county board of commissioners can specify the membership, qualifications, and terms of office and the filling of vacancies on the board.

- **Appeals**: Under general law, when a county appoints a special E&R board, it may allow taxpayers to appeal to the board of county commissioners from decisions of the special board. This act deletes that authority for Lincoln County. Thus, if Lincoln County appoints a special E&R board, the special board's decisions are appealable directly to the Property Tax Commission (G.S. 105-290) and from there to the court of appeals (G.S. 105-345).

- **Quorum**: This act specifies that a majority of the members of the special board constitute a quorum for the purpose of transacting business. Decisions are made by a majority of the members present. An alternate member, when sitting as a member, has all of the powers and duties of a regular board member.

- **Clerk**: Under general law, only the assessor can serve as clerk to a special E&R board. This act provides that for Lincoln County either the assessor or a person designated by the assessor will serve as clerk. Under general law, the clerk's duties include being present at all meetings, maintaining accurate minutes of the actions of the boards, and providing the board with information on the listing and valuation of taxable property in the county. This act expands the clerk's duties for Lincoln County to include drafting all written decisions of the special board, and specifies that the chair will review all written decisions drafted by the clerk. Furthermore, the act stipulates that only the chair, or in the chair's absence, the vice chair, can execute the decisions of the special board.

- **Time of Meeting**: The act maintains the general law setting an April or early May starting date for meetings of the E&R board, but changes the deadline for the completion of duties. Under general law, in non-revaluation years, a special E&R board must complete its duties within four weeks, although this deadline may be extended to July 1 if necessary. In revaluation years, a special E&R board must complete its duties by December 1, except to hear taxpayers' appeals filed before its adjournment. The act provides that the Lincoln County E&R board must complete its duties by July 1, except that it may sit year round to hear taxpayer appeals related to discovered property, classified motor vehicles, audits of present-use value property, and audits of exempt or excluded property. Under general law (G.S. 105-325), the board of county commissioners may meet after its special E&R board has adjourned only for limited purposes such as to correct clerical errors, to add discovered property to the lists, and to address facts that should have been, but were not, known before the special board adjourned.

- **Powers and Duties**: The act also expands the duties and powers of the Lincoln County E&R board by adding the following powers and duties:

1. Duty to Appoint Motor Vehicle Review Subcommittee: The chair of the E&R board must appoint a subcommittee at the first meeting of the calendar year to meet as needed to hear and decide all appeals relating to the appraisal, situs, and taxability of classified motor vehicles. Because motor vehicles are taxed on a staggered, year-round schedule, the subcommittee must be available throughout the year to hear motor vehicle appeals.

2. Power to Designate Reappraisal Year Panels: In a reappraisal year, the chair of the E&R board may divide the board into separate panels of three members, which may include the alternate board members. A decision of the panel constitutes a decision of the E&R board.

MODIFY BILL LEE ACT

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-56	**HB 1560**	**Representative Allen**

AN ACT TO MAKE MODIFICATIONS TO THE WILLIAM S. LEE ACT AND TO RELATED ECONOMIC DEVELOPMENT LAWS.

Overview: This act modifies the William S. Lee Quality Jobs and Business Expansion Act and related economic development laws by enacting application fee changes, extending credit carryforwards, requiring wage standards for grants, prohibiting funding for defaulting grantees, expanding credits, and making technical corrections. The provisions of the act are listed below:

Provision	Effective Date	Fiscal Impact
Application Fee Exemptions		
Exempts taxpayers applying for certification for a tax credit in a	1/1/2001 for applications	Insignificant impact

development zone from the $500 per credit application fee. Clarifies that there is no application fee associated with the application filed with the Department of Revenue concerning the credit for contributions for a development zone project.	made on or after that date	
Extend Credit Carryforwards		
Provides an enhanced carryforward of 10 years for a taxpayer who certifies that it will purchase or lease, and place in service within two years, at least $50 million worth of real property, machinery and equipment, or central office or aircraft facility property. The general Bill Lee Act carryforward is five years.	1/1/00	No fiscal impact until fiscal year 2013-2014
Require Wage Standard for Grants		
Requires the following to meet the Bill Lee Act wage standard: • A business seeking a grant from the Industrial Recruitment Competitive Fund. • A local government seeking a loan or grant from the Industrial Development Fund.	7/1/00	N/A
Prohibit Funding for Defaulting Grantee		
Prohibits the Department of Commerce from making a loan or awarding a grant to a person who is currently in default on any loan made by the Department.	7/1/00	N/A
Aircraft Maintenance Facility Credit		
Allows an auxiliary subdivision of an interstate passenger air carrier engaged primarily in aircraft maintenance and repair services or aircraft rebuilding to qualify for the Bill Lee Act tax credits.	1/1/01	This change is expected to reduce General Fund revenues by $30,000 in fiscal year 2002-2003, $60,000 in fiscal year 2003-2004, and $90,000 in fiscal year 2004-2005
Employee Buyout Incentive		
Revises the test for what constitutes an acquisition of a business by an employee buyout. An existing business that is acquired through an employee buyout is able to qualify for the Bill Lee Act credits	5/1/99	Insignificant impact

to the same extent as a new business.		
Low-Income Housing Credit Changes		
Allows a 75% credit for low-income buildings located in a county that has been designated as having sustained severe or moderate damage from a hurricane or hurricane-related disaster.	1/1/01	Insignificant impact
Clarifies that a building that fails to meet the eligibility requirements for the State low-income housing credit during the five-year installments of the credit forfeits the remaining installments.	1/1/00	Insignificant impact
Modify Credit and Expiration Provisions		
Modifies the jobs tax credit to allow a taxpayer to claim a tax credit for creating a full-time job when it has 5 full-time employees regardless of how many weeks those employees work during the taxable year.	1/1/00	Insignificant impact
Corrects a provision in the tax credit for investing in machinery and equipment that penalizes a taxpayer for replacing recently acquired equipment with new equipment.	1/1/00	N/A
Clarifies that a taxpayer loses any remaining installments on tax credits claimed under the Bill Lee Act if the taxpayer ceases to engage in an eligible business.	1/1/00	N/A
Technical Correction		
Clarifies that an insurance company qualifies for a sales tax refund on certain purchases if it is operated for the exclusive purpose of providing insurance products to certain nonprofit organizations or to public institutions and their employees.	5/1/99	N/A

Background & Analysis:

History of the Bill Lee Act

The William S. Lee Quality Jobs and Business Expansion Act (hereinafter Bill Lee Act) was enacted in 1996, effective beginning with the 1996 tax year with a 2002 sunset. The Act is a package of State tax incentives and has been modified in each subsequent year. The incentives are primarily in the form of tax credits for investment in machinery and equipment, job creation, worker training, and research/development. For many of the credits the counties are divided into five economic distress tiers based on the unemployment rate, per capita income, and population growth of the county. In general, the lower the tier of a county, the more favorable the incentive.

The Act requires the Department of Commerce to report annually on the credits allowed by the Act. In 1997, the General Assembly added specific issues that the Department of Commerce was required to study and report back on in 1999. Before 1996, North Carolina had made little use of tax incentives to lure businesses to the State. Even without incentives, North Carolina was consistently one of the top states in attracting industry. The array of credits authorized by the Bill Lee Act was viewed as an experiment, to be evaluated in five years to determine whether the incentives were cost effective and actually affected behavior, or merely provided tax reductions to businesses that would have located or expanded in any case. In 1999, the General Assembly expanded existing tax incentives for businesses, added new tax incentives and tax reductions for specific businesses, and made related changes. The General Assembly also extended the 2002 sunset to 2006.

During the 2000 Session, the General Assembly further modified the Bill Lee Act and related economic development laws by enacting application fee changes, extending credit carryforwards, requiring wage standards for grants, prohibiting funding for defaulting grantees, expanding credits, and making technical corrections.

Application Fee Exemptions

To claim a credit under the Bill Lee Act, a taxpayer must provide with the tax return the certification of the Secretary of Commerce that the taxpayer meets all of the eligibility requirements with respect to each credit that the taxpayer claims. The taxpayer must file an application for certification with the Secretary. In 1999, the General Assembly eliminated the $75 application fee for credits claimed in tiers one and two counties. For tiers three, four, and five counties, the application fee was increased to $500 per credit claimed with a cap of $1,500 per applicant. This act extends the fee exemption to apply not only to credits claimed in tiers one and two, but also credits claimed in a development zone. A development zone is an area within the corporate limits of a city with a population over 5,000. The area, composed of one or more contiguous census tracts or census block groups, must have a population of 1,000 or more. Of that population, more than 10% must be below the poverty level or the area must be adjacent to a tract or group that has more than 20% of its population below the poverty level.

This act also clarifies that there is no fee for an application filed with the Department of Revenue concerning the credit for a development zone project. In 1999, the General Assembly created a new tax credit for taxpayers that contribute cash or property to certain nonprofit agencies to be used for an improvement project in a development zone. An improvement project is a project to construct or improve real property for community development purposes or to acquire real property and convert it for community development purposes. The credit allowed is 25% of the amount contributed by the taxpayer. The total amount of credits that may be allowed in a taxable year is capped at $4 million. Taxpayers are required to apply to the Secretary of Revenue for these credits. If the total amount of credit applied for in a year exceed $4 million, the Secretary will reduce each applicant's credit proportionally.

These changes become effective January 1, 2001, and apply to applications made on or after that date.

Extend Credit Carryforwards

The Bill Lee Act credits may not exceed 50% of the tax against which they are claimed. The limitation applies to the cumulative amount of credit claimed by the taxpayer, including carryforwards. As a general rule, any unused portion of a credit may be carried forward five years. The Bill Lee Act provides two exceptions that allow twenty-year carryforwards. This act creates a third exception that allows a ten-year carryforward, effective for taxable years beginning on or after January 1, 2000. The three exceptions are:

- Any unused portion of a credit with respect to a large investment may be carried forward for 20 years. A large investment is one where an eligible business purchases or leases, and places in service within a two-year period, $150 million worth of one or more of the following: real property, machinery and equipment, or central administrative office property.

- Any unused portion of a credit with respect to the technology commercialization credit may be carried forward for 20 years. The General Assembly created the technology investment credit in 1999 as an alternative to the 7% credit for investing in machinery and equipment. The credit applies only to investments in machinery and equipment used in production based on technology licensed from a research university. The investments must be located in a tier one, two, or three county and must equal at least $10 million during the taxable year and must total at least $100 million over a five-year period.

- This act allows any unused portion of a credit to be carried forward for 10 years if the Secretary of Commerce certifies that the taxpayer will purchase or lease, and place in service in connection with an eligible business within a two-year period, at least $50 million worth of one or more of the following: real property, machinery and equipment, or central office or aircraft property. If the taxpayer fails to make the level of investment certified within the two-year period, the taxpayer forfeits the enhanced carryforward period.

Require Wage Standards for Grants

To be eligible for the credits under the Bill Lee Act, the jobs for which a credit is claimed and the jobs at the location with respect to which a credit is claimed must meet the applicable wage standard. For a tier one county, the jobs must pay an average weekly wage that is equal to the average weekly wage for that county. For other tier counties, the average weekly wage must equal 110% of the average weekly wage for that county. Effective July 1, 2000, this act requires jobs at the following projects also to meet the Bill Lee Act wage standards:

  - A project for which a business seeks a grant from the Industrial Recruitment Competitive Fund. The purpose of this Fund is to provide financial assistance to those businesses or industries deemed by the Governor to be vital to a healthy and growing State economy and that are making significant efforts to establish or expand in the State.

  - A project for which a local government seeks a loan or grant from the Industrial Development Fund. The purpose of this Fund is to assist local government units of the most economically distressed counties in creating jobs in certain industries.

Prohibit Funding for Defaulting Grantees

Effective July 1, 2000, the act prohibits the Department of Commerce from making a loan or awarding a grant to any individual, organization, or governmental unit that is currently in default on any loan made by the Department of Commerce.

Aircraft Maintenance Facility Credit

The act expands the list of eligible businesses that qualify for a credit under the Bill Lee Act to include an auxiliary subdivision of an interstate passenger air carrier engaged primarily in aircraft maintenance and repair services or aircraft rebuilding. An interstate passenger air carrier is a person whose primary business is scheduled passenger air transportation. This change is effective for taxable years beginning on or after January 1, 2001. It allows the air carrier to qualify for the central administrative office credit as well as the credit for creating jobs, credit for investing in machinery and equipment, credit for research and development, and credit for worker training. It also allows the air carrier to qualify for the enhanced twenty-year carryforward for large investments.

Employee Buyout Incentive

The act revises the test for what constitutes an acquisition by an employee buyout. Prior to 1998, the acquisition of a business by an employee buyout did not qualify for Bill Lee Act credits. The credits were allowed only for new and expanding businesses. As a general rule, the acquisition of a business, or any other transaction by which an existing business reformulates itself as another business, does not create new eligibility in the succeeding business. In 1998, the General Assembly provided an exception from this general rule for a business that has closed, has filed a federally required notice that closure is imminent, or has been purchased in an employee buyout. In these cases, the business is able to qualify for the credits to the same extent as a new business.

Effective May 1, 1999, the act revises the test for what constitutes an acquisition of a business by an employee buyout. It provides that the term "acquired" means that as part of the initial purchase of a business by employees, the purchase included an agreement for the employees, through the employee stock option transaction or another similar mechanism, to obtain one of the following:

- Ownership of more than 50% of the business.
- Ownership of not less than 40% of the business within seven years if the business has tangible assets with a net book value in excess of $100 million and has a majority of its operations located in an enterprise tier one, two, or three area.

Low-Income Housing Credit Changes

The act expands the applicability of the low-income housing credit and clarifies that the credit is forfeited under certain circumstances. In 1999, the General Assembly enacted a new tax credit for rehabilitating or constructing low-income housing. The credit is equal to a percentage of the amount of the taxpayer's federal credit for low-income housing with respect to eligible North Carolina low-income housing. The credit is 75% for buildings located in tier one or two counties and 25% for buildings located in other tiers. This act provides that the 75% credit is also allowed for buildings located in a county that has been designated as having sustained severe or moderate damage from a hurricane or a hurricane-related disaster, according to the Federal Emergency Management Agency impact map, revised on September 25, 1999. These counties are Bertie, Beaufort, Bladen, Brunswick, Carteret, Columbus, Craven, Dare, Duplin, Edgecombe, Greene, Halifax, Hertford, Jones, Lenoir, Martin, Nash, New Hanover, Northampton, Onslow, Pasquotank, Pender, Pitt, Washington, Wayne, and Wilson Counties. This change is effective for taxable years beginning on or after January 1, 2001, applies to buildings to which federal credits are allocated on or after January 1, 2001, and expires January 1, 2005.

To qualify for the State credit, the test of what constitutes low-income housing for a building located in a tier three, four, or five county is harder to meet than under the federal law. The federal law requires that either (1) at least 20% of the residential units are rent-restricted and occupied by individuals whose income is 50% or less of area median gross income, or (2) at least 40% of the residential units are rent-restricted and occupied by individuals whose income is 60% or less of area gross income. The State law for a tier three or four county requires that at least 40% of its residential units are rent-restricted and occupied by individuals whose income is 50% or less of area median gross income. For a tier five county, the State law requires that at least 40% of its residential units are rent-restricted and are occupied by individuals whose income is 35% or less of area median gross income. If, in one of the five years in which an installment is claimed, the taxpayer no longer qualifies for the federal credit, the taxpayer is no longer eligible for the State credit. This act clarifies that if a building in a tier three, four, or five county no longer meets the more stringent State tax credit requirements, the remaining installments of the credit may not be taken, even though the building may continue to qualify for the federal credit. This clarification is effective for taxable years beginning on or after January 1, 2000.

Modify Credit and Expiration Provisions of the Bill Lee Act.

The act makes three changes to credits in the Bill Lee Act and to the credits' expiration, effective for taxable years beginning on or after January 1, 2000. These changes were recommended by the Revenue Laws Study Committee and do the following:

- Modify the jobs tax credit to allow a taxpayer to claim a tax credit for creating a full-time job when it has five full-time employees regardless of how many weeks those employees work during the taxable year.
- Correct a provision in the tax credit for investing in machinery and equipment that penalizes a taxpayer for replacing recently acquired equipment with new equipment.
- Clarify that a taxpayer loses any remaining installments on tax credits claimed under the Bill Lee Act if the taxpayer ceases to engage in an eligible business.

Jobs Tax Credit Change

The Department of Commerce asked the Revenue Laws Study Committee to make this change to eliminate a restriction that has the unintended consequence of preventing a taxpayer from taking a tax credit for jobs created under certain circumstances. Under prior law, a taxpayer that met the eligibility requirement of the Bill Lee Act, had five or more employees for at least 40 weeks of the taxable year, and hired an additional full-time employee to fill a full-time position located in this State could claim a tax credit for creating a new full-time position. The credit for any specific full-time position may be claimed only once and must be taken in installments over four years. This act amends the jobs tax credit by eliminating the 40-week requirement, since it does not serve any apparent purpose.

The 40-week requirement had the unintended effect of denying the job tax credit to certain taxpayers. For example, an employer was not eligible for this credit if it began operations with more than five employees 13 or more weeks into the taxable year. However, a taxpayer could get around this 40-week requirement by signing a letter of commitment with the Department of Commerce to create at least 20 new full-time jobs in a specific area within a two-year period. This taxpayer would be eligible for a credit in the taxable year after at least 20 employees were hired.

The elimination of the 40-week requirement will have a minimal fiscal impact, since most taxpayers have been able to get around the requirement by signing a letter of commitment. The taxpayers who will benefit from this change are those that did not qualify for a letter of commitment and who began operations with between five and twenty employees more than 12 weeks into the taxable year.

Correct Investment Tax Credit

The act corrects a "reverse loophole" in the Bill Lee Act credit for investing in machinery and equipment. Under prior law, if a taxpayer earned a credit for investing in machinery and then, within the seven-year period that installments of the credit are allowed, replaced the machinery with newly acquired machinery, the taxpayer suffered two consequences. The taxpayer lost the remaining installments earned on the original machinery and received no credit for investing in the replacement machinery except to the extent its value exceeded the value of the original machinery. The act corrects this reverse loophole by providing that the remaining installments of the credit for the original machinery may be taken if the value of newly acquired machinery in the same enterprise tier offsets at least 80% of the value of the original machinery taken out of service. As under prior law, a new credit is allowed to the extent the remaining value of the newly acquired machinery creates a net investment increase in excess of the applicable investment threshold, and there is no penalty if the taxpayer replaces the machinery after the end of the seven-year installment period.

Clarify Expiration of Credits

The act clarifies that if a taxpayer that claims a Bill Lee Act credit ceases to engage in the type of business required for qualification of the credit, then the taxpayer loses any remaining installments of the credit (but does not lose accrued carryforwards).

Technical Correction

In 1999, the General Assembly provided a sales tax refund to certain nonprofit insurance companies for State and local taxes they pay on building materials, supplies, fixtures, and equipment that become a part of their real property and on capitalized computer systems hardware and software. To qualify for these refunds, the insurance company must be operated for the exclusive purposes of providing insurance products to nonprofit charitable organizations and their employees. In addition, the Secretary of Commerce must certify that the insurance company will invest at least $20 million in this State. This act added the underlined language to clarify that to be eligible for this refund, an insurance company must be operated for the exclusive purpose of providing insurance products to organizations exempt from federal income tax and their employees <u>or to public institutions and their employees.</u> This change became effective May 1, 1999, and applies to taxes paid on or after that date.

CHARTER SCHOOL FUEL EXEMPTION

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-72	**HB 1302**	**Representative Bonner**

AN ACT TO EXEMPT FROM TAX MOTOR FUEL SOLD TO CHARTER SCHOOLS.

Overview: This act exempts charter schools from paying the motor fuels tax.

Fiscal Impact: This act is expected to reduce Highway Fund revenues by about $24,000 a year and to reduce Highway Trust Fund Revenues by about $8,000 a year.

Effective Date: October 1, 2000.

Background & Analysis: This act adds "motor fuel sold to a charter school for use for charter school purposes" to the list of exemptions from the motor fuel excise tax. Thus, charter schools will join the following list to which the motor fuel excise tax does not apply:

- Motor fuel removed in this State for transportation to another state if the supplier collects tax on the motor fuel at the rate of the motor fuel's destination state.
- Motor fuel sold to the federal government for its use.
- Motor fuel sold to the State for its use.
- Motor fuel sold to a local board of education for use in the public school system.
- Diesel that is kerosene and is sold to an airport.

The motor fuel excise tax rate has two components: a flat rate and a variable rate. The flat rate is 17.5¢ per gallon. The variable component may change every six months. It is added to the flat rate. The variable component is equal to the greater of 3.5¢ a gallon or 7% of the weighted average wholesale price of gasoline and No. 2 diesel fuel for the most recent six-month base period. The current motor fuel tax rate is 23.1¢ a gallon. Due to increases in the weighted wholesale price of these motor fuels, the tax increased during each of the last two six-month base periods from a low of 21¢ in late 1999.

One-half cent a gallon of the motor fuel tax revenue is dedicated to the two underground storage tank funds and the water and air quality account. Seventy-five percent (75%) of the remainder of the revenue generated by this tax is allocated to the Highway Fund and the remaining 25% is credited to the Highway Trust Fund.

A charter school is defined in this act as a nonprofit corporation that has a charter under Part 6A of Article 16 of Chapter 115C of the General Statutes to operate a charter school. G.S. 115C-238.29D limits the number of charter schools to 100 schools statewide. Any person, group of persons, or nonprofit corporation may apply to the State Board of Education to establish a charter school. However, according to this act, a charter school will qualify for the exemption only if it is operated by a nonprofit corporation. To be approved as a charter school, the applicant must meet the statutory requirements of Part 6A of Article 16 of Chapter 115C and the Board must find that the proposed school will meet one or more of the following objectives:

- Improve student learning.
- Increase learning opportunities for all students.
- Encourage the use of different and innovative teaching methods.
- Create new professional opportunities for teachers.
- Provide expanded educational choices for parents and students.

To enable the Department of Revenue to administer the tax exemption and to verify the eligibility of the applicant for the exemption, this act requires the State Board of Education to direct the Department of Public Instruction to notify the Department of Revenue when the State Board terminates, fails to renew, or grants a charter for a charter school.

Charter schools will be able to buy non-tax-paid fuel directly from suppliers. The Department of Revenue will keep a list of exempt charter schools. Fuel suppliers will be able to check that list and then issue an "exempt card" to the school. The fuel supplier can then sell non-tax-paid fuel to the school, either directly or through a contractor. The school would need to have a storage tank or container for the fuel. Additionally, if the school buys fuel on which the tax has been paid, such as from a retail station, it can obtain a refund from the Department of Revenue.

AMEND BILL LEE ACT TIER DESIGNATIONS

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-73	**SB 1318**	**Senator Dalton**

AN ACT TO PROVIDE THAT AN ENTERPRISE TIER TWO AREA MAY NOT BE REDESIGNATED AS A HIGHER-NUMBERED TIER AREA UNTIL IT HAS BEEN AN ENTERPRISE TIER TWO AREA FOR TWO CONSECUTIVE YEARS.

Overview: This act amends the Bill Lee Act by providing that an enterprise tier two area may not be redesignated as a higher numbered tier area until it has been an enterprise tier two area for at least two consecutive years. In 1997 (S.L. 1997-277), the General Assembly amended the Bill Lee Act to guarantee that a county that obtained a tier one status could not lose that status for two years. The act extends this guarantee to a county designated as a tier two area.

Fiscal Impact: The act is expected to reduce General Fund revenues by $111,000 in fiscal year 2001-2002, $233,000 in fiscal year 2002-2003, $344,500 in fiscal year 2003-2004, and $456,000 in fiscal year 2004-2005. The act has no impact on fiscal year 2000-2001 because the credits are taken in the year after the investment and job creation activity take place.

Effective Date: Retroactive to tier designations for the 2000 and later calendar years.

Background & Analysis: Under the Bill Lee Act, all counties are divided into five enterprise tiers, ranked by economic distress as measured by a formula that combines unemployment, per capita income, and population growth. Those counties in lower-numbered tiers receive more favorable incentives than those in higher tiers. For example, enterprise tier one and two counties are the counties considered most in need of economic development based on high unemployment, low per capita income, and low population growth.

In 1997, the General Assembly amended the Bill Lee Act to guarantee that a county that obtained a tier one status could not lose that status for two years regardless of what the annual rankings would otherwise require. This act extends this guarantee to a county designated as a tier two area, so that a tier two area may not be redesignated as a higher numbered tier area until it has been a tier two area for two consecutive years.

During the 1999 Session, the Bill Lee Act was amended to provide the following three incentives for development in enterprise tier one and two counties:

- Extended the Bill Lee Act credits to electronic mail order houses that create at least 250 jobs in tiers one and two.
- Extended the Bill Lee Act credits to customer service centers in tiers one and two.
- Allowed an annual refund of 6% sales taxes paid on capitalized machinery and equipment sold to businesses

eligible for Bill Lee Act credits and located in tiers one and two.

In 1999, the General Assembly also allowed certain counties to qualify for a lower enterprise tier designation, effective January 1, 2000. The rules for assigning enterprise tier designations were changed to provide that the tier number that would otherwise be assigned by the formula is reduced by one for counties that have a population of less than 50,000 and also have more than 18% of their residents below the federal poverty level. Under this change, Alleghany, Ashe, Beaufort, Cherokee, Perquimans, Scotland, Vance, and Yancey Counties moved from tier two to tier one. Bladen, Hoke, Jones, Madison, Pamlico, and Pasquotank Counties moved from tier three to tier two. The 1999 change also provided that a county that has a population of less than 25,000 cannot be designated higher than tier three. Finally, the 1999 change provided that a county is designated as tier one if it has a population of less than 10,000 and also has more than 16% of its residents below the federal poverty level. Under this change, Camden, Clay, and Jones qualified as tier one counties.

EXTEND CABARRUS E&R BOARD

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-92	**SB 1364**	**Senator Hartsell**

AN ACT TO AUTHORIZE THE CABARRUS BOARD OF EQUALIZATION AND REVIEW TO MEET AFTER ITS FORMAL ADJOURNMENT.

Overview: The act authorizes the Cabarrus County Board of Equalization and Review to meet after its regular adjournment, in order to hear appeals relating to discovered property, motor vehicles, and audits of property taxed at preferential rates.

Fiscal Impact: No fiscal impact.

Effective Date: July 7, 2000.

Background & Analysis: This act adds Cabarrus County to Section 2 of S.L. 1999-353, which originally applied only to Stokes County. The effect of adding Cabarrus County is to authorize the Cabarrus County Board of Equalization and Review to continue meeting after it has completed its regular duties for the year. Under general law, a special board of equalization and review has the duty to examine and review the tax lists for the current year and to hear any timely request of a taxpayer with respect to the listing or appraisal of property. Under general law, in non-revaluation years, a special E&R board must complete its duties within four weeks, although this deadline may be extended to July 1 if necessary. In revaluation years, a special E&R board must complete its duties by December 1, except to hear taxpayers' appeals filed before its adjournment. This act provides an exception for Cabarrus County, allowing its E&R board to continue to meet after completing its regular duties in order to carry out the following duties:

- To hear and decide appeals relating to discovered property.
- To hear and decide appeals relating to the appraisal, situs, and taxability of classified motor vehicles.
- To hear and decide appeals relating to audits of property classified at present-use value and relating to audits of property exempted or excluded from taxation.

2000 FEE BILL

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-109	**HB 1854**	**Representative Miller**

AN ACT TO SET THE PUBLIC UTILITY REGULATORY FEES AND THE INSURANCE REGULATORY CHARGE, TO INCREASE COURT COSTS, TO INCREASE JAIL FEES FOR PERSONS PAYING JAIL FEES PURSUANT TO PROBATIONARY SENTENCES, TO INCREASE THE FEE IMPOSED FOR EMERGENCY PLANNING, TO AUTHORIZE CERTAIN CHANGES IN PERMITS FOR OVERSIZE LOADS AND ESTABLISH PENALTIES FOR PERMIT VIOLATIONS, TO AUTHORIZE AGENCIES TO PROVIDE ACCESS TO SERVICES THROUGH ELECTRONIC AND DIGITAL TRANSACTIONS AND TO IMPOSE A FEE FOR THOSE TRANSACTIONS, AND TO REPEAL THE SUNSET OF THE WHITE GOODS TAX AND DIRECT THE DEPARTMENT OF ENVIRONMENT AND NATURAL RESOURCES TO STUDY ISSUES RELATED TO THE SCRAP TIRE DISPOSAL TAX AND THE WHITE GOODS DISPOSAL TAX.

Overview: This act makes four tax law changes and five fee law changes; only the tax law changes are summarized here. The tax law changes are:

- Set the tax rates for the public utility regulatory fee for the 2000-2001 tax year.
- Set the tax rate for the North Carolina Electric Membership Corporation regulatory fee for the 2000-2001 fiscal year.
- Set the tax rate for the insurance regulatory charge for the 2000 calendar year.
- Repeal the July 2001 sunset on the White Goods tax.

Fiscal Impact:

- Public Utility Regulatory Fee: This fee is expected to generate $9.06 million.
- NC Electric M'ship Corp: This fee is expected to generate $200,000.
- Insurance Regulatory Charge: This fee is expected to generate $25.65 million.
- White Goods Sunset Repeal: This tax generates approximately $4 million a year, which is distributed as follows:
    - The Solid Waste Management Fund receives 8% of the tax.
    - The White Goods Management Account receives 20%.
    - The counties receive the remaining 72%.

Effective Date:

- Public Utility Regulatory Fee: 2000-2001 tax year
- NC Electric M'ship Corp Fee: 2000-2001 tax year

- Insurance Regulatory Charge: 2000 calendar year

- White Goods Sunset Repeal: July 13, 2000

Background & Analysis:

Public Utility Regulatory Fee

The act sets the general rate for the public utility regulatory fee at 0.09% for the 2000-2001 fiscal year. This is the same rate that was in effect for both the 1997-1998 and 1998-1999 fiscal years, and is expected to generate $9.06 million. The utility regulatory fee is a tax that was first imposed in 1989. The proceeds of the fee are credited to the Utilities Commission and Public Staff Fund and used to defray the State's cost in regulating public utilities. The regulatory fee is imposed on all utilities that are subject to regulation by the North Carolina Utilities Commission. The fee is a percentage of the utility's North Carolina jurisdictional revenues. In general, jurisdictional revenue is revenue derived from providing utility service in North Carolina.

In addition to funding the State's cost in regulating public utilities, the money in the Utilities Commission and Public Staff Fund is currently used to finance the work of the Study Commission on the Future of Electric Service in North Carolina. The General Assembly established the Commission in 1997 to examine the cost, adequacy, availability, and pricing of electric rates and service in North Carolina to determine whether legislation is necessary to assure an adequate and reliable source of electricity and economical, fair, and equitable rates for all consumers of electricity in North Carolina.

North Carolina Electric Membership Corporation Fee

The act sets at $200,000 the annual public utility regulatory fee imposed on electric membership corporations whose principal purpose is to furnish or cause to be furnished bulk electric supplies at wholesale, as provided in G.S. 117-16, effective for the 2000-2001 fiscal year. The North Carolina Electric Membership Corporation is the only electric membership corporation that fits this description. The proceeds of the fee will be credited to the Utilities Commission and Public Staff Fund and used to defray the State's cost in regulating electric membership corporations.

The 1999 General Assembly enacted S.L. 1999-180, which authorized electric membership corporations to form subsidiary corporations that may provide energy services and products, telecommunications services and products, and water and wastewater collection and treatment. The subsidiaries must fully compensate the electric membership corporation for its use of the corporation's personnel, services, equipment, and property. The Utilities Commission is charged with regulating this aspect of the subsidiary's business and, to pay for this regulation, S.L. 1999-180 levied a flat-rate regulatory fee to be paid annually by the North Carolina Electric Membership Corporation. The General Assembly must establish the fee amount each year. The North Carolina Electric Membership Corporation is the only electric membership corporation whose principal purpose is to furnish or cause to be furnished bulk electric supplies at wholesale, as provided in G.S. 117-16. It is a "generation and supply cooperative" owned by its members. Its members are all but one of the existing North Carolina electric membership corporations, which are "distribution cooperatives." Thus, the fee imposed on the North Carolina Electric Membership Corporation will be passed on to its member electric membership corporations.

Insurance Regulatory Charge

The act sets the insurance regulatory charge at 7% for the 2000 calendar year, the same rate used in the 1999 calendar year. The charge is expected to generate $25.65 million for the 2000-2001 fiscal year. The insurance regulatory charge is a tax that was enacted in 1991 to defray the State's cost of regulating the insurance industry. The charge is a percentage of each insurance company's premiums tax liability. The insurance regulatory charge is imposed on insurance companies that pay the gross premiums tax and, beginning in 2000, on health maintenance organizations and medical service corporations. For health maintenance organizations and medical service corporations, the fee is levied on each company's hypothetical gross premiums tax liability determined at the 1.9% gross premiums tax rate applied to its premiums base. The hypothetical calculation is necessary because medical service corporations pay premiums tax at a rate of 0.5% rather than 1.9% and because health maintenance organizations do not pay premiums tax.

Prior to 2000, the insurance regulatory charge was imposed only on insurance companies that paid the gross premiums tax.

Medical service corporations were exempt, and health maintenance organizations did not pay the regulatory charge because they do not pay a gross premiums tax. Prior to 1995, these entities contributed to the Department of Insurance Fund through insurance audit and examination fees. However, in 1995, the General Assembly eliminated the insurance audit and examination fees for insurance companies, health maintenance organizations, medical corporations, and guaranty associations. The costs of the audits are now paid for by the insurance regulatory charge as part of the costs of regulating the insurance industry.

White Goods Sunset Repeal

This act repeals the sunset on the white goods tax. Under prior law, the white goods tax was scheduled to sunset July 1, 2001. The Department of Environment and Natural Resources reports annually to the Environmental Review Commission on the management of white goods. This act directs the Department to study the scrap tire disposal tax as well as the white goods disposal tax, and evaluate whether the amounts of these taxes should be altered or whether the distribution of the proceeds of the taxes should be reapportioned. The Department must make a report on this study to the Environmental Review Commission by October 1, 2000.

The white goods tax was imposed effective January 1, 1994. The purpose of the tax is to provide a source of revenue for the proper disposal of discarded white goods. A white good is a domestic or commercial large appliance, such as a refrigerator, a water heater, an air conditioner unit, or a dishwasher. The tax is a flat rate charged on every new white good purchased in this State or brought into this State for storage or use. The tax rate is $3.00 per white good. The tax generates approximately $4 million each year.

Proceeds from the white goods tax are distributed as follows: 8% to the Solid Waste Management Trust Fund, 20% to the White Goods Management Account, and 72% to counties. Counties may use the white goods tax proceeds distributed to them only for the management of discarded white goods, which may include capital improvements for infrastructure to manage discarded white goods, operating costs associated with managing discarded white goods, and cleanup of white goods at illegal disposal sites.

Counties are limited in the amount of surplus white goods tax proceeds they can accumulate. Counties receive their distributions of white goods tax proceeds on a quarterly basis. If at the end of a fiscal year, the county has a surplus of white goods tax proceeds that equals or exceeds 25% of the amount it was eligible to receive for the fiscal year, it may not receive additional distributions until its surplus falls below that level. The amount that would have been distributed to a county will instead be credited to the White Goods Management Account.

Counties must include in their annual financial information report to the Local Government Commission information about their management of white goods and their receipt and expenditure of white goods tax proceeds and related revenues. The annual financial information report must be certified by the county finance officer based on an independent audit by a certified public accountant.

TAX ENFORCEMENT

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-119	**HB 1551**	**Representative Miller**

AN ACT TO MODIFY THE AUTHORITY OF DEPARTMENT OF REVENUE LAW ENFORCEMENT AGENTS, TO ALLOW THE SECRETARY OF REVENUE TO ADMINISTER THE OATH OF OFFICE TO DEPARTMENT OF REVENUE LAW ENFORCEMENT AGENTS, TO PROVIDE A CIVIL PENALTY FOR FILING A FRIVOLOUS INCOME TAX RETURN, AND TO CHANGE THE PROCEDURES FOR LAW ENFORCEMENT REPORTING ON NON-TAX-PAID UNAUTHORIZED SUBSTANCES.

Overview: This act makes the following changes to the law to facilitate enforcement of the tax laws:

- It expands the offenses revenue law enforcement officers may enforce to include misdemeanor offenses as well as felony offenses. This part of the act became effective July 14, 2000.

- It authorizes the Secretary of Revenue to administer the oath of office to revenue law enforcement officers. This part of the act became effective July 14, 2000.

- It creates a civil penalty for filing a frivolous income tax return. A frivolous return is one that meets both of the following conditions: (1) it does not include information on which the substantial correctness of the return may be judged or contains information that indicates that the return is substantially incorrect. (2) It evidences an intention to delay, impede, or negate the revenue laws of this State or purports to adopt a position that is lacking in seriousness. The penalty for filing a frivolous return is up to $500. This part of the act becomes effective October 1, 2000, and applies to returns filed on or after that date.

- It streamlines the procedures State and local law enforcement agencies must use to report arrests made for the failure to pay tax on unauthorized substances by allowing them to give the information directly to the Department of Revenue. This part of the act becomes effective December 1, 2000, and applies to arrests or seizures occurring on or after that date.

Fiscal Impact: The creation of a civil penalty for filing a frivolous income tax return could produce $300,000 to $1 million in revenue each year for the General Fund.

Effective Date: See the Overview above.

Background & Analysis: The Revenue Laws Study Committee recommended this act to the General Assembly, at the recommendation of the Department of Revenue. The act makes several changes to the law to facilitate the enforcement of the tax laws.

Authority of Law Enforcement Agents

The act expanded the offenses revenue law enforcement officers may enforce to include the following misdemeanor offenses:

- Willful failure to collect, withhold, or pay over tax. G.S. 105-236(8).

- Willful failure to file a return, supply information, or pay tax. G.S. 105-236(9).

- Highway use of dyed diesel or other non-tax-paid fuel. G.S. 105-449.117.

- Miscellaneous fuel tax misdemeanors. G.S. 105-449.120.

- Sale of certain packages of cigarettes. G.S. 14-401.18.

Revenue law enforcement officers already have the authority to enforce felony tax violations under G.S. 105-236 and to enforce numerous other offenses under State law when they involve a State tax. The act rewrites G.S. 105-236.1(a) by listing the offenses a revenue law enforcement officer may enforce.

Secretary to Administer Oath of Office

The act authorizes the Secretary of Revenue to administer the oath of office to revenue law enforcement officers. The Secretary is not one of the individuals who have general authorization under G.S. 11-7.1 to administer oaths. The Secretary does, however, have authority under G.S. 105-261 to administer an oath to a person with respect to a tax return or report. The act puts the qualifications for becoming a revenue law enforcement officer, including the oath of office, in a separate subsection.

Civil Penalty for Filing a Frivolous Income Tax Return

The act creates a civil penalty for filing a frivolous income tax return. In order for a return to be frivolous, it must meet both of the following conditions:

- The return does not include information on which the substantial correctness of the return may be judged or it contains information that positively indicates the return is incorrect.

- The return evidences an intention to delay or impede the revenue laws of this State or purports to adopt a position that is lacking in seriousness.

The penalty for filing a frivolous return could be up to $500. As with other penalties assessed under Subchapter I of Chapter 105, this penalty would be assessed as an additional tax. This penalty is similar to a penalty imposed on the federal level under section 6702 of the Internal Revenue Code.

The Criminal Investigations Division of the Department of Revenue requested this change in the law. In its work, the Division has investigated cases in which a taxpayer will knowingly file an incorrect return in order to inflate deductions and thus increase the amount of the taxpayer's refund. For example, a taxpayer may claim extra dependents or exaggerate the amount of charitable contributions. The current penalties do not provide a proper remedy because they are based upon failure to pay the amount of tax due. In most of these cases, there is no amount of tax due because the taxpayer is already due a refund. The offense is that the taxpayer is claiming a greater refund than the taxpayer is entitled to receive.

Streamline the Procedures for Reporting on

Non-Tax-Paid Unauthorized Substances

The act relieves the SBI of the burden of reporting drug-related offenses to the Department of Revenue. Under current law, State and local law enforcement agencies have to report to the SBI within 48 hours the arrest of any individual in possession of certain threshold amounts of drugs that do not bear unauthorized substances tax stamps. The SBI must then notify the Department of Revenue on a daily basis of the reports it receives. The SBI does not need this information and requested that it be relieved of this responsibility. Effective December 1, 2000, State and law enforcement agencies will report these arrests directly to the Department of Revenue, as opposed to the SBI. The act makes the following conforming changes: It moves the reporting requirement from Chapter 114 to Article 2D of Chapter 105; it repeals the requirement that the SBI notify the Department on the reports it receives.

STREAMLINED SALES TAX SYSTEM

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-120	**HB 1624**	**Representative Miller**

AN ACT TO IMPLEMENT THE RECOMMENDATION OF THE NATIONAL GOVERNORS' ASSOCIATION FOR A STREAMLINED SALES TAX COLLECTION SYSTEM AND TO OTHERWISE IMPROVE COLLECTION.

Overview: This act is a recommendation of the Revenue Laws Study Committee. It seeks to improve the State's tax collections in several different ways:

- It simplifies and streamlines the sales and use tax collection system for remote and in-state retailers.
- It provides that a remote seller who does not agree to collect the State's use tax may not use the State's courts to collect debts owed to it by a purchaser of its product in this State.
- It allows the Department of Revenue to exchange information concerning a taxpayer's social security number with the Division of Motor Vehicles when it is necessary to identify a taxpayer.
- It provides the Department of Revenue with the resources to continue its collection of delinquent tax debts owed by nonresidents and foreign entities for the remainder of this biennium.
- It allows the Department of Revenue to retain necessary funds from revenues it collects from its nonresident delinquent tax debt contracts to obtain assistance in developing a performance-based contract for an automated collection system. The General Assembly asked the Department and the State Controller to study how to collect taxes more efficiently. The centralization and automation of the Department's delinquent tax debts are the primary recommendations of this study, conducted by PricewaterhouseCoopers.
- It provides that, effective January 1, 2001, the penalty for misusing an exemption certificate applies not only to a certificate of resale, but also to a direct pay certificate and a farmer's certificate.
- It repeals the requirement that a taxpayer report use tax on the income tax return.

Fiscal Impact: No fiscal estimate is possible because the legislation is only the first step in establishing a new remote sales and use tax collection system. However, once this remote sales and use tax collection system is completed, the fiscal impact could be significant. A recent study by the University of Tennessee estimates that by 2003 the incremental State and local revenue loss on e-commerce transactions will be $238 million for North Carolina. If the current revenue losses on catalog sales and e-commerce transactions are included, the total amount could be over $400 million.

It is estimated that the implementation of an automated case management tool would increase delinquent tax collections by $11 million to $30 million annually. Additionally, contracting with collection agencies for out-of-state debts and for long-term delinquent accounts would yield an initial $20 million in additional revenues and an increase in recurring revenues of up to $23 million per year.

Effective Date: The provision dealing with the sales tax exemption certificate (Section 7) becomes effective January 1, 2001. The provisions dealing with the repeal of the use tax reporting requirement (Sections 10 and 11) becomes effective for taxable years beginning on or after January 1, 2003. The remainder of the act became effective July 14, 2000.

Background & Analysis:

Streamlined Sales Tax Collection System

This act enables North Carolina to become one of four states to participate in the streamlined sales tax collection system pilot project. The National Governors' Association recommended the streamlined sales tax collection system. The recommendation addresses the difficulty states have collecting sales and use taxes on purchases from remote retailers. The recommendation provides a simplified collection process that would allow participating retailers to use a computer software program to be able to calculate the amount of tax due to the State on a purchase based upon the customer's ship-to address. The administration of the program would be the responsibility of a person certified by the State to collect its taxes, not the retailer.

To begin this method of collection, the State must certify a person to act as its tax collector. It is anticipated that the identity of the "certified sales tax collector" will vary depending upon the type of retailer involved. Certain large retailers may choose to act as their own collector.

To be certified as a sales tax collector, this act would require the Secretary of Revenue to find that the person meets all of the following conditions:

- Uses a sales tax collection software program certified by the Secretary. To be certified by the Secretary, the program must be able to determine the applicable tax rate based on a ship-to address, determine whether or not an item is exempt from tax, determine whether or not an exemption certificate is valid, calculate the tax due, and generate the reports and returns required by State law.

- Agrees to update its certified software program upon notification by the Secretary.

- Agrees to integrate the certified software program with the retailer's system for which the person collects the tax.

- Remits the tax due and files the necessary returns on behalf of the retailers for whom the person collects the tax.

- Enters into a contract with the Secretary and agrees to comply with the conditions of the contract.

- Files a bond or an irrevocable letter of credit with the Secretary in an amount set by the Secretary.

The State would assume the responsibility for the costs of the system by contracting with the collector to reimburse the collector for the costs of operating the system and for the costs of integrating the system with those of participating retailers. The amount a collector charges under a contract is considered a cost of collecting the tax and is payable from the amount collected. The payments to the collector will be made on a per transaction basis based on negotiated rates. The per-transaction fee could be in the form of a flat per transaction rate, a percentage rate, or a combination of the two types of rates.

Participation in the program by retailers is voluntary. To participate in the program, a retailer must agree to let the certified sales tax collector integrate the certified software with the retailer's system so that the tax due on a sale can be determined at the time of the sale. The information on the amount of tax due will be available to a customer before completion of a transaction. Once the customer approves the purchase, the retailer will send the transaction through the payment processing system and the amount paid to the retailer will be the full amount of the purchase plus tax. A participating retailer will be required to enter into a standing debit authorization agreement with the collector that will enable the collector to debit the retailer's account on an agreed upon schedule for the amount of tax owed all participating states according to transactions processed by the collector. The collector will be liable for remitting the appropriate tax to the participating states. In the absence of fraud, the participating retailer will not be subject to audits by the states on the transactions it processes using the collector's software program. A contract with a collector will not be a factor in considering whether a person has nexus with a state for payment of a tax.

The act also makes the following statutory changes to meet the uniformity features needed to successfully implement the streamlined sales tax collection system:

- It makes the exemption process easier to administer by eliminating the "good faith" requirement when accepting an exemption certificate number from a purchaser on a sale made over the Internet or by other remote means. (Section 6) It codifies a long-standing practice of the Department of Revenue to issue "direct pay certificates" to a person who is unsure how property the person purchases should be taxed at the time the property is purchased. (Section 1) And it provides that, effective January 1, 2001, the penalty for misusing an exemption certificate applies not only to a certificate of resale, but also to a direct pay certificate and a farmer's certificate. (Sections 7 and 18)

- It establishes a uniform sourcing rule that calculates the amount of tax due on a sale based on its "ship-to address". (Section 2) To accomplish this sourcing rule, the bill expands the current sales tax exemption for printed materials that are shipped out-of-state and not subsequently used by the purchaser to include all tangible personal property. (Section 5)

- It provides that the customer of a retailer who participates in the program may not elect to pay the tax directly to the Secretary rather than to the seller. (Section 4)

- It provides that local government sales and use tax rate changes may only be made twice a year and the local government must give the State at least 90 days notice of any tax rate change. (Sections 12 and 13)

Use of NC Courts by Out-of-State Retailers

Under current law, a loan made by a person who fails to pay or comply with the State privilege tax statute, G.S. 105-88, may not be collected through the State's courts. This act extends this exclusion to include debts owed to a retailer who is required by G.S. 105-164.8(b) to collect use tax for the State but refuses to do so if the retailer reported gross sales of at least $5,000,000 on its most recent federal income tax return. (Sections 3 and 9) The exclusion would also apply to any person to whom the debt is assigned. The exclusion would only apply to debts owed on tangible personal property purchased from the retailer. A retailer is required to collect use tax for the State under G.S. 105-164.8(b) if the retailer maintains retail offices in the State, has representatives in the State who solicit business, or purposefully and systematically exploits the market in this State by any media-assisted means such as direct mail advertising, distribution of catalogs, computer-assisted shopping, television, radio, etc.

DMV Disclose Social Security Number to DOR:

Under federal law, 42 U.S.C. 405(c)(2)(C), a state may use a person's social security number for the purpose of identification in the administration of its tax laws. The Department of Revenue has used social security numbers to identify taxpayers for many years. Up until recently, the Department was able to obtain a taxpayer's social security number from the Division of Motor Vehicles. The Department may have asked the Division for a taxpayer's social security number when the Department had more than one number on file for a taxpayer and needed to know which number was correct, or when it needed to locate a taxpayer. The exchange of information between the Division and the Department was not addressed by statute. In 1997, the General Assembly amended the drivers license law to require all applicants for a drivers license to provide their social security numbers. The legislation gave specific authority for the Division to disclose social security numbers to the Child Support Enforcement Program. The law did not address the disclosure of the numbers to the Department of Revenue. As a result, the practice between the Division and the Department has stopped.

This act rewrites the drivers license statute pertaining to social security numbers to allow the Division to disclose a social security number to the Department for the purpose of verifying taxpayer identification. (Section 14) It also provides that the Division of Motor Vehicles may not use an applicant's social security number as the identifying number for the license holder. (Section 15) This clarification resolves a conflict between two subsections in G.S. 20-7: subsection (b1) provides that an applicant's social security number may not be printed on the license, while subsection (n) says that the license holder's social security number may be the license holder's identifying number.

Contract for Collection of Delinquent Tax Debts

Last session, the General Assembly allowed the Department of Revenue to contract for the collection of delinquent tax debts owed by nonresidents and foreign entities. A delinquent tax debt is the amount of tax due as stated in a final notice of assessment issued to the taxpayer when the taxpayer no longer has the right to contest the debt. The legislation stated that "[T]he Secretary of Revenue shall contract during the 1999-2001 fiscal biennium for the collection of delinquent tax debts…" However, the legislation provided a funding mechanism for only the first year of the biennium. This act provides funding for the second year of the biennium. It allows the Secretary to retain the costs of the contracts from the amounts collected under the contracts. (Section 16)

The Department is currently involved in a pilot effort to contract for the collection of out-of-state accounts receivable in conjunction with the Office of the State Controller. On March 16, 2000, the Department sent 1,016 accounts with a value of $927,170.46 to the Office of the State Controller for referral to a collection agency. Within the first 30 days, the Department realized a 2.5% return.

Implement Recommendation of PricewaterhouseCoopers to

Centralize and Automate Debt Collection System

Last session, the General Assembly authorized the Department of Revenue and the Office of the State Controller to conduct a study of the Department's delinquent collection practices and present findings and recommendations to the Revenue Laws Study Committee. The Office of the State Controller's existing contract with PricewaterhouseCoopers (PwC) was modified and PwC conducted the study. PwC made the following recommendations to improve the Department's debt collection practices:

- Implement an automated case management tool with debt scoring and performance measures. The projected impact of this recommendation would be an increase of delinquent tax collections by $11 million to $30 million annually.

- Centralize the collection process for individual income taxes, installment agreements, low-dollar debts, and wage garnishments. The impact of this recommendation would be a more efficient use of the Department's resources.

- Contract with collection agencies for out-of-state debts. The impact of this recommendation would be an initial $20 million in additional revenues and $3 million in recurring revenues.

- Contract with collection agencies for long term delinquent accounts. The impact of this recommendation would be up to $20 million in additional revenues per year.

The Department would like to implement the recommendations of this study. To centralize its collection process, the Department would like to enter into a performance-based contract where the person who provides the automated system would be paid from the proceeds of the system based upon some variable that pertains to how well the system works. To enable the Secretary of Revenue to obtain assistance in developing a request for proposal for the performance-based contract, this act allows the Secretary to draw the amount needed from the revenue collected pursuant to the contracts for the collection of delinquent tax debts owed by nonresidents and foreign entities. (Section 17)

CONFORM WITH FEDERAL LAW

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-126	**HB 1559**	**Representative Luebke**

AN ACT TO UPDATE THE REFERENCE TO THE INTERNAL REVENUE CODE USED IN DEFINING AND DETERMINING CERTAIN STATE TAX PROVISIONS, TO CONFORM TO FEDERAL LAW REGARDING PENSION TAX WITHHOLDING AND DEADLINES FOR PAYMENTS OF CERTAIN ESTIMATED INCOME TAXES, TO CLARIFY THE SALES FACTOR FOR DETERMINATION OF STATE CORPORATE INCOME AND FRANCHISE TAX, AND TO ENABLE THE COLLECTION OF TAX DEBT OWED TO NORTH CAROLINA THROUGH THE FEDERAL TREASURY OFFSET PROGRAM.

Overview: This act was a recommendation of the Revenue Laws Study Committee and makes the following changes relating to tax law:

- **Update IRC Reference.** It rewrites the definition of the Internal Revenue Code used in State tax statutes to change the reference date from June 1, 1999, to January 1, 2000. This change became effective for taxable years beginning on or after January 1, 2000.

- **Conform Pension Tax Withholding.** It requires withholding of State income taxes on an eligible rollover distribution to the extent permitted under federal law. This change becomes effective January 1, 2001.

- **Conform Estimated Tax Deadline for farmers and fishers.** It returns the withholding law for farmers and fishers to conformity with federal law, correcting an inadvertent change made in 1985. This change became effective July 14, 2000.

- **Clarify Sales Factor.** It amends the definition of "sales" for purposes of the apportionment formula to clarify that the receipts of a multi-state corporation should include only the net gain realized from the sale or maturity of securities, not the rolled over capital or return of principal and not receipts otherwise exempt from tax. This change became effective July 14, 2000.

- **Participate in Treasury Offset Program.** It enables the Department of Revenue to collect delinquent tax debts owed to the State through the United States Department of the Treasury Offset Program by providing for the imposition of a collection assistance fee. This change became effective July 14, 2000.

Fiscal Impact: The Code Update is expected to reduce General Fund revenues by $2,030,000 in fiscal year 2000-2001, and $4,350,000 in fiscal year 2001-2002. The Code Update is expected to increase General Fund revenues by $650,000 in fiscal year 2002-2003, $850,000 in fiscal year 2003-2004, and $600,000 in fiscal year 2004-2005. Conforming the tax deadline and the pension tax withholding, and clarifying the sales factor for multi-state corporations have no fiscal impact. Participating in the Treasury Offset Program has a potential revenue gain, but no estimate is available.

Effective Date: *See Overview section.*

Background & Analysis:

Update Code Reference

Updating the Internal Revenue Code reference makes recent amendments to the Code applicable to the State to the extent that State tax law previously tracked federal law. Since the General Assembly updated the State's reference to the Internal Revenue Code to June 1, 1999, Congress enacted Public Law 106-170, the Tax Relief Extension Act of 1999. That Act extends several expired and expiring tax provisions, some of which affect federal taxable income. Since the computation of State taxable income begins with federal taxable income, any changes to federal taxable income affect State taxable income.

This act rewrites the definition of the Code to change the reference date from June 1, 1999, to January 1, 2000. The act further provides that the federal tax law changes that could increase an individual's or a corporation's State taxable income for the 1999 tax year will not become effective for the 1999 tax year but will instead apply only to taxable years beginning on or after January 1, 2000. This provision is necessary because Article 1, Section 16, of the North Carolina Constitution prohibits the legislature from passing a law that will retroactively increase the tax liability of any taxpayer. There are a few changes in Public Law 106-170 that could increase taxable income for the 1999 tax year. Because the act could not be ratified until after the 2000 Session of the 1999 General Assembly convened, these changes were given a delayed effective date.

The following is a summary of the provisions of the Tax Relief Extension Act of 1999 that may affect State taxable income. These changes apply to taxable years beginning on or after January 1, 2000.

- Delays the sunset of the exclusion from gross income of up to $5,250 annually for employer-provided educational assistance for undergraduate courses. The exclusion would have expired with respect to courses beginning on or after June 1, 2000. Public Law 106-170 extends the exclusion with respect to courses beginning before January 1, 2002.

- Clarifies that no charitable contribution deduction is allowed for a transfer to or for the benefit of a charitable organization if, in connection with the transfer, the organization directly or indirectly pays any premium on any personal benefit contract with respect to the transferor. A personal benefit contract is a life insurance, annuity, or endowment contract. The clarification of this provision does not infer that a charitable split-dollar insurance arrangement was allowed under prior law. It does not apply to a person that benefits exclusively under a bona fide charitable gift annuity within the meaning of the Code.

- Delays the sunset of the work opportunity tax credit and the welfare-to-work tax credit. These credits would have expired for wages paid or incurred to a qualified individual who began work for an employer before July 1, 1999. Public Law 106-170 extends these credits for wages paid to qualified individuals who began work for the employer on or after July 1, 1999, and before January 1, 2000. To the extent an employer claims the federal credit, the employer must reduce its federal deduction for wages by the amount of the credit. Since North Carolina does not have comparable credits, it allows a taxpayer who claims the federal credits to claim a deduction from federal taxable income for the amount by which the employer's deduction for wages was reduced.

- Delays the sunset of the expensing of environmental remediation expenditures. The Code authorizes taxpayers to treat certain environmental remediation expenditures that would otherwise be chargeable to capital account as deductible in the year paid or incurred. The end of that period of time during which qualifying expenditures can be expensed is extended from January 1, 2001 to January 1, 2002.

- Provides that an option to accelerate the receipt of a payment under a production flexibility contract between the Secretary of Agriculture and a farmer will not accelerate the recognition of income. A taxpayer generally is required to include an item in income no later than the time of its actual or constructive receipt. If a taxpayer has an unrestricted right to demand the payment of an amount, the taxpayer is in constructive receipt of that amount whether or not the taxpayer makes the demand and actually receives the payment. The production flexibility contract payments are to be included in gross income in the year they are actually received. These contracts generally cover crop years 1996 through 2002.

- Prohibits use of the installment method by accrual method taxpayers. Under prior law, the installment method of reporting income from dispositions of property could be used by a taxpayer regardless of whether the taxpayer used the cash method or accrual method of accounting. An accrual method taxpayer is generally required to recognize income when all the events have occurred that fix the right to the receipt of the income and the amount of the income can be determined with reasonable accuracy. The installment method of accounting allows a taxpayer to defer the recognition of income from the disposition of certain property until payment is received, regardless of whether the taxpayer uses the cash method or accrual method of accounting. Public Law 106-170 generally prohibits accrual method taxpayers from using the installment method of reporting income from dispositions of property. It retains the present law regarding the availability of the installment method for dispositions of property used or produced in the trade or business of farming and for dispositions of timeshares or residential lots if the taxpayer elects to pay interest under section 453(l) of the Code. It does not change the ability of a cash method taxpayer to use the installment method.

- Adds new categories of non-capital assets. Three categories have been added to the list of assets the gain or loss on which is treated as ordinary income, as opposed to a capital gain or loss. The new categories are: commodities derivatives held by commodities derivatives dealers, hedging transactions, and supplies of a type regularly consumed by the taxpayer in the ordinary course of the taxpayer's trade or business.

- Limits conversion of character of income from constructive ownership transactions. Public Law 106-170 limits the amount of long-term capital gains a taxpayer can recognize from derivative transactions with respect to certain pass-through entities to the amount of gain the taxpayer would have had if the taxpayer owned a direct interest in the pass-through entity during the term of the derivative contract.

- Delays sunset on transfers of excess pension benefits to retiree health benefits accounts. The period of time permitting qualified transfers of excess defined benefit pension plan assets to retiree health benefits accounts under section 401(h) of the Code has been extended to include transfers that take place before January 1, 2006. The period of time would have expired on December 31, 2000.

- Allows a basis reduction to assets of a corporation if stock in the corporation is distributed by a partnership to a corporate partner. This reduction applies if, after the distribution, the corporate partner controls the distributed corporation.

- Delays sunset of exceptions under subpart F of the Code for active financing income of controlled foreign corporations. A foreign corporation is a "controlled foreign corporation" (CFC) if more than 50% of its outstanding voting stock, or more than 50% of the value of all its outstanding stock, is owned by U.S.

shareholders. A "U.S. shareholder" is a U.S. citizen or resident, or a U.S. corporation, partnership, estate or trust, that owns 10% or more of the foreign corporation's total combined voting stock. In general, the foreign-source income of a foreign corporation is not taxable to its U.S. shareholders until it is distributed to them. Recognizing that income could be accumulated in a CFC, thus deferring U.S. tax on this income indefinitely, Congress enacted the subpart F provisions of the Code in 1962. These provisions require certain items of income to be treated as deemed paid to U.S. shareholders and, therefore, subject to U.S. taxation. The income subject to current inclusion under the subpart F rules includes foreign personal holding company income, insurance income, and foreign base company services income. Examples of foreign personal holding company income include dividends, rents, royalties, annuities, net gains from commodity transactions, net gains from foreign currency transactions, and payments in lieu of dividends. Insurance income subject to inclusion under the subpart F rules includes any income of a CFC attributable to the issuing or reinsuring of any insurance or annuity contract in connection with risks located in a country other than the CFC's country of organization. "Foreign base company services income" is income derived from services performed for a related person outside the country in which the CFC is organized. Temporary exceptions from foreign personal holding company income, foreign base company services income, and insurance income apply for subpart F purposes for certain income that is derived in the active conduct of a banking, financing, or similar business, or in the conduct of an insurance business. These exceptions were set to expire on December 31, 1999. Public Law 106-170 extends these exceptions for two years, until January 1, 2002.

Background for Code Update

Since the State corporate income tax was changed to a percentage of federal taxable income in 1967, the reference date to the Internal Revenue Code has been updated periodically. In discussing bills to update the Code reference, the question frequently arises as to why the statutes refer to the Code on a particular date instead of referring to the Code and any future amendments to it. The answer to the question lies in both a policy decision and a potential restraint.

First, the policy reason for specifying a particular date is that, in light of the many changes made in federal tax law from year to year, the State may not want to adopt automatically federal changes, particularly when these changes result in large revenue losses. By pinning references to the Code to a certain date, the State ensures that it can examine any federal changes before making the changes effective for the State.

Secondly, and more importantly, however, 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."

In 1997, the Revenue Laws Study Committee explored the possibility of legislation that would automatically adopt federal changes to the Code each year, with legislative review and approval required in the succeeding legislative session. It was hoped that this approach would avoid the practical difficulties that occur when Code changes go into effect many months before the General Assembly has a chance to pass legislation adopting the changes. The Attorney General's Office reviewed the relevant case law in this State and other states before concluding that this approach would be unlikely to withstand a constitutional challenge.

Conform Pension Tax Withholding

Under federal law, withholding is required on pensions, annuities, and certain deferred income, including IRAs, unless the taxpayer makes an election not to have the tax withheld. There is one exception to this rule: withholding is required on an eligible rollover distribution, and a taxpayer may not elect not to have the tax withheld.

In 1999, the General Assembly passed S.L. 1999-414, which tracks part of the federal law. Under S.L. 1999-414, a pension payer must withhold State income tax on a pension payment, other than an eligible rollover distribution, if the pension payer was withholding federal income tax on the payment. As under federal law, a recipient of a pension payment that is not an eligible rollover distribution may elect not to have tax withheld from the pension payment. Unlike federal law, S.L. 1999-414 did not require that tax be withheld from an eligible rollover distribution. Effective January 1, 2001, this act requires that North Carolina tax be withheld on eligible rollover distributions to the same extent as required under federal law. A taxpayer may not elect not to have the tax withheld. The effect of this change is to conform North Carolina law to federal law in this regard.

Conform Estimated Tax Deadline

The act corrects an inadvertent change made in 1985 by conforming the State's estimated tax deadline for farmers and fishers to the federal deadline. Federal law forgives the penalty for late payment of estimated taxes by farmers and fishers if the final return is filed, with taxes paid in full, by March 1 following the end of the taxable year. Prior State law erroneously based the forgiveness on March 1 payment of estimated tax.

Prior to 1985, the federal and State tax law requirements to pay estimated tax and the imposition of the underpayment penalty were contained in different statutes. In 1984, federal law was rewritten to consolidate several Code sections regarding the payment of estimated tax into one Code section. In 1985, North Carolina enacted similar legislation consolidating the State statutes into one statute. The bill was entitled "AN ACT TO CONFORM PAYMENTS OF NORTH CAROLINA ESTIMATED TAX PENALTIES FOR INDIVIDUALS TO FEDERAL ESTIMATED TAX PAYMENT PENALTIES." The exceptions were intended to remain the same and the Department of Revenue has administered those exceptions in that manner since the federal legislation was enacted.

Clarify Sales Factor

A multi-state corporation that has income from business activity which is taxable in more than one state must allocate and apportion a percentage of its income to North Carolina for purposes of the State's corporate income and franchise tax law. An excluded corporation apportions its income to the State by multiplying its income by the sales factor. An "excluded corporation" is a corporation engaged in business as a building or construction contractor, a securities dealer, a loan company, or a corporation that receives more than 50% of its ordinary gross income from investments or dealings in intangible property. The sales factor is a fraction, the numerator of which is the total sales of the corporation in this State during the income year and the denominator of which is the total sales of the corporation everywhere during the income year.

The definition of "sales" is the gross receipts of the corporation except for receipts from a casual sale of property and receipts otherwise allocated by statute, such as rents, royalties,

sales of real property, interest, and net dividends. This act clarifies the definition of "sales" by excluding from gross receipts the following:

- Receipts exempt from taxation.
- The portion of receipts realized from the sale or maturity of securities or other obligations that represents a return of principal.

To include these receipts in the gross amount would distort the sales factor. For example, it is not unusual for working capital to be turned over repeatedly by investing in short term securities. When the receipts include both principal and interest, the principal may be included in the denominator several times. When the denominator is inflated, the fraction is diluted and it can not accurately reflect the true net earnings of the corporation in North Carolina. The act clarifies that only the net gain from the sale or maturity of securities should be included in the sales factor, not the rolled over capital or return of principal and not receipts otherwise exempt from taxation.

Participate in Treasury Offset Program

The Department of Revenue may collect delinquent tax debts owed to the State through the U.S. Department of the Treasury Offset Program. To participate in this method of collection, the State must pay a fee of $9.65 per offset claim to the Program, send a certified letter to the delinquent taxpayer at a cost of $3.01, and incur other incidental expenses. The act enables the Department of Revenue to impose a $15.00 collection assistance fee on each tax debt collected through the Treasury Offset Program. The Department requested the collection fee because of the cost of participating in the Program.

The State already imposes a collection assistance fee on debts collected through the State debt setoff collection act. The amount of that fee cannot exceed $15.00. The collection assistance fee authorized by the act is added to the amount of the tax liability submitted to the U.S. Department of the Treasury for setoff. As under the State setoff debt collection act, the collection assistance fee has priority over the debt setoff. Therefore, if the federal setoff covers only part of the tax due, the collection assistance fee has priority over the tax due.

RENEWABLE ENERGY MFR. CREDIT

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-128	**HB 1473**	**Representative Hackney**

AN ACT TO MODIFY THE INCOME TAX CREDIT FOR MANUFACTURERS OF CERTAIN RENEWABLE ENERGY EQUIPMENT AND TO FURTHER ADJUST THE SHARE CERTAIN CITIES RECEIVE FROM THE STATE GROSS RECEIPTS TAX.

Overview: This act expands the current corporate tax credit for a corporation that constructs a facility for the production of photovoltaic equipment to include the construction of a facility for the production of other types of renewable energy equipment. The act provides that the credit must be taken in five equal installments and extends the carryforward from five to ten years. The act also adjusts the distribution of the State franchise tax on utility gross receipts that is shared with cities.

Fiscal Impact: The current corporate income tax credit for constructing photovoltaic manufacturing facilities has not been used since it was created in 1981. Thus, neither the number of companies nor the amount of the credit to be requested can be estimated. However, if only one company applies for the credit, there will be a General Fund revenue loss due to the absence of applicants for the current tax credit program.

There is no State budget impact from the redistribution of the franchise tax proceeds among the cities.

Effective Date: Section 1 of this act, relating to the tax credit, is effective for taxable years beginning on or after January 1, 2000, and is repealed for costs incurred during taxable years beginning on or after January 1, 2006. Section 2 of the act, relating to the redistribution of the franchise tax, is effective October 1, 2000, and applies to distributions made on or after that date.

Background & Analysis:

Tax Credit for Manufacturers of Renewable Energy Equipment

nder prior law, a corporation that constructed a facility for the production of photovoltaic equipment was allowed a credit equal to 25% of the installation and equipment costs of construction paid during the taxable year. The amount of the credit could not exceed the amount of tax owed; any unused credit would be carried forward for five years. Photovoltaic equipment means products designed, manufactured, and produced to convert sunlight directly into electricity. The credit was not allowed to the extent that federal, State, or local grants provide any of the costs of the equipment. To secure the credit, the taxpayer must own or control the facility at the time of construction.

This act allows a corporation that constructed a facility in North Carolina for the manufacture of renewable energy equipment to receive a corporate income tax credit equal to 25% of the installation and equipment costs of construction paid during the taxable year. Renewable energy equipment is defined in the act as biomass equipment, solar electric or thermal equipment, and wind energy equipment. This broad definition encompasses the definition of photovoltaic equipment. As with the prior credit, the new credit is not allowed to the extent that any of the cost of the equipment is provided by governmental grants. The credit allowed under this act differs from the former credit in the following ways:

- The entire credit can not be taken for the taxable year in which the costs are paid, but must be taken in five equal installments beginning with the taxable year in which the costs are paid.

- The cumulative amount of the credit, including carryforwards, may not exceed 50% of the amount of the tax imposed for the taxable year.

- Any unused portion of the credit may be carried forward for ten years instead of five years.

- A taxpayer that claims any other credit with respect to the construction of a facility to manufacture renewable energy equipment may not take this credit with respect to the same facility.

Adjustment to Franchise Tax Distribution Formula for Cities

This act also makes an adjustment to the franchise tax distribution formula for cities. The State distributes part of the State franchise tax imposed on utilities to the cities. Before July 1, 1999, the franchise taxes that were distributed were the taxes on electricity, piped natural gas, and telephone service. The rate for each utility was 3.22%. In S.L. 1998-22, the General Assembly combined the franchise gross receipts and the sales taxes on piped natural gas into a single per therm excise tax. That act preserved the distribution of the gross receipts tax to cities by providing that 50% of the new excise tax on piped gas service within a city would be distributed to that city.

As part of the resolution of the 1991 State budget crisis, the State eliminated the future growth to cities of this shared revenue. The total amount distributed was frozen but the relative share of each city changed based on the proportion of that city's receipts compared to the total of all cities' receipts. When the 1993 General Assembly restored growth, effective beginning with the 1995-96 fiscal year, it was decided that the State would hold back an amount equal to the growth of the distribution base from 1990-91 to 1994-95 as the contribution of each city to the State's budget problems. After growth was restored in 1995-96, it was discovered that some cities received less net distribution than in 1990-91, the last year prior to the "growth freeze". This happened to cities that experienced a temporary franchise tax base growth in the freeze years (1990-91 through 1994-95) and then a reduction of the base in 1995-96. To adjust for this loss of tax base growth, the 1997 General Assembly reduced the holdback amount, thereby increasing the amount of State franchise tax distributed to 40 cities. These 40 cities were the ones whose 1995-96 distributions were less than 95% of their 1990-91 distributions. The 1997 act increased the annual distribution to the affected cities by a total of $194,841. The annual distribution to the other 500 cities was reduced by the same amount, so that the State share of the franchise tax was not reduced. The 1997 adjustment, however, was not sufficient to hold the Town of Denton's loss to a level that did not go below its 1990-91 distribution. The reason the 1997 adjustment formula did not fully compensate Denton is because the manufacturing facility that was the basis of the holdback had not fully closed by 1995-96.

This act allows the adjustment formula for a city that, in the 1995-96 fiscal year, received from gross receipts taxes less than 60% of the amount it received in the 1990-91 fiscal year, to be based upon the 1999-2000 fiscal year distribution rather than the higher 1995-96 distribution. Based on actual tax base holdback, and distribution data from the Department of Revenue, it is estimated that in future years the Town of Denton will receive an additional $14,000 per year.

This exception to the adjustment formula would apply to distributions made on or after October 1, 2000.

2000 TECHNICAL CORRECTIONS

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-140	**SB 1335**	**Senator Hartsell**

AN ACT TO MAKE TECHNICAL CORRECTIONS AND CONFORMING CHANGES TO THE GENERAL STATUTES AS RECOMMENDED BY THE GENERAL STATUTES COMMISSION, TO MAKE OTHER TECHNICAL AND CONFORMING CHANGES, AND TO AMEND LAWS RELATING TO URBAN WATERFRONT DEVELOPMENT AND THE CLASSIFICATION OF

GAMMA HYDROXYBUTYRIC ACID (GHB) AS A CONTROLLED SUBSTANCE.

Overview: This act makes conforming and technical changes to various statutes and session laws. Most of these changes were recommended by the General Statutes Commission. The sections of the act explained in the table below are changes made to the revenue laws and related statutes. These changes were recommended by the Revenue Laws Study Committee, the Department of Revenue, and legislative staff. Additional technical and conforming changes were made in House Bill 1290, enacted as S.L. 2000-173.

Fiscal Impact: Insignificant impact.

Effective Date: July 21, 2000, unless otherwise provided *(see Background & Analysis section)*.

Background & Analysis: The following table provides a section-by-section analysis of the changes that affect the revenue laws and related statutes:

Section	Explanation
56	Reorganizes and clarifies new regulatory fee levied in 1999 on certain electric membership corporations.
61	Updates the statute catchline to reflect that the nature of the tax on amusements has changed from a license tax to a privilege tax.
62	Makes conforming change to reflect that natural gas tax is now levied and distributed under a different statute.
63	Corrects wording problems that resulted when two different 1999 acts amended the same statutes.
64	Modernizes outdated language in the corporate income tax statutes.
65	Makes a conforming change to recognize that certain State, local, and federal government retirement benefits are exempt from North Carolina income tax pursuant to settlement of the *Bailey*, *Emory*, and *Patton* cases.
66	Repeals a criminal penalty for willful failure to pay corporate estimated tax, because it duplicates a penalty already provided in G.S. 105-236(9), in the general administrative section of the Revenue Act.
67	Conforms the statute to reflect that only one statewide retail sales tax license is required, reorganizes and consolidates two similar statutes, deletes obsolete language regarding renewal fees, and repeals a criminal penalty that duplicates a penalty already provided in the general administrative section of the Revenue Act.
68	Corrects the form of a reference to the Internal Revenue Code.
69	Adds a definition of "Department" in Chapter 105 of the General Statutes, consistent with the way the term is used in that Chapter to mean "Department of Revenue."

70	Adds the missing word "the" to the statute.
71	Corrects indentation of statute.
72	Corrects a numerical cite in G.S. 105-275, as amended in S.L. 2000-2, and clarifies the definition for the term "vehicle".
73	Makes a conforming change regarding a mailed notice to reflect a 1999 change in the content of property tax lien lists published in the newspapers. This section becomes effective January 1, 2001, the same date the 1999 changes become effective
74	Corrects definitional cross-references to avoid problems when definitions are renumbered.
75	Makes further technical corrections to S.L. 2000-2, effective July 1, 2000.
85	Extends hold harmless period for piped gas distributions to municipalities to allow the Revenue Laws Study Committee more time to evaluate whether the new distribution method enacted in 1998 will yield distribution amounts that are similar enough to those provided under prior law.
88	Corrects effective date for 1999 change to G.S. 105-241.1, the scope of which was inadvertently limited.

FINANCE NEW WILDLIFE CENTERS

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-143	**SB 1477**	**Senator Kerr**

AN ACT TO PROVIDE FOR A NEW, SUSTAINABLY DESIGNED, STATE OFFICE BUILDING AND WILDLIFE EDUCATION CENTER WITH RELATED PARKING FACILITIES, TO BE USED BY THE WILDLIFE RESOURCES COMMISSION, PURSUANT TO AN INSTALLMENT FINANCING CONTRACT IN A PRINCIPAL AMOUNT NOT TO EXCEED THIRTEEN MILLION FIVE HUNDRED THOUSAND DOLLARS, AND TO PROVIDE FOR A NEW EASTERN WILDLIFE EDUCATION CENTER WITH RELATED PARKING FACILITIES, TO BE ADMINISTERED BY THE WILDLIFE RESOURCES COMMISSION, PURSUANT TO AN INSTALLMENT FINANCING CONTRACT IN A PRINCIPAL AMOUNT NOT TO EXCEED FOUR MILLION DOLLARS.

Overview: This act authorizes the State to construct and finance two projects: a new, sustainably designed, office building and Wildlife Education Center for the Wildlife Resources Commission, to be located in Raleigh, and a new Eastern Wildlife Education Center, to be located in Currituck County. The projects would be financed with one or two installment purchase contracts under which the State would borrow up to $13.5 million for the Raleigh project and up to $4 million for the Currituck County project. Repayment of the debt would be secured by a lien on the building, land, or both.

Fiscal Impact: The construction financing costs authorized by this act have no General Fund impact, but rather are borne entirely by the Wildlife Resources Commission (WRC). The WRC expects to fund the construction of the new administration and education center and the Eastern Wildlife Education Center internally, with currently unbudgeted funds. The anticipated yearly loan payment cost of the $13.5 million Raleigh administration and education facility at 5.1% interest for 25 years is $956,495. The annual loan payment for the $4 million Eastern Wildlife Education Center given the same loan term and interest rate is $283,406.

Effective Date: This act became effective August 2, 2000.

Background & Analysis: This act would authorize the construction of two projects: a new office building and Wildlife Education Center for the Wildlife Resources Commission in Raleigh and a new Eastern Wildlife Education Center in Currituck County. The Raleigh project would include the 63,000 square foot building, related furnishings and equipment, and parking facilities, and would be located on the Centennial Campus of North Carolina State University. The land would be leased from the Centennial Campus under a long-term lease. The Currituck project would include the 19,800 square foot building, related furnishings and equipment, and parking facilities, and would be located on land adjacent to the Currituck Beach Lighthouse and the historic Whalehead Club. This land is available at no cost from Currituck County.

These two projects would be financed with one or more installment purchase financing contracts. Under such a contract, the State would borrow up to $13.5 million for the Raleigh project and up to $4 million for the Eastern Wildlife Education Center. It is anticipated the amounts borrowed would be repaid with interest in installments over a period of 20 to 25 years. The debt would be tax-exempt. It is the intent of the General Assembly that the repayments would be made not from the General Fund but with funds available to the Wildlife Resources Commission from the Wildlife Resources Fund and the Wildlife Endowment Fund.

The debt would be secured by a security interest in the buildings, the land, or both. There would be no pledge of the State's taxing power or full faith and credit. Thus, voter approval is not necessary for the borrowing. If the Wildlife Resources Commission defaulted on its repayments, the buildings could be disposed of to generate funds to satisfy the debt. Under the act, the funds could be borrowed either from a single entity or by the sale of certificates of participation. A certificate of participation represents the holder's undivided interest in the right to receive the installment payments to be made by the State. If certificates of participation are issued, a nonprofit corporation will have to be created to facilitate the financing.

Before a financing contract could be entered into, it would have to be approved by the Council of State. The Council of State would, by resolution, set the maximum interest rate and the maximum number of years over which the debt would be repaid. In addition, the State Treasurer must approve the financing, finding that the amount to be borrowed is adequate and not excessive and will not require an excessive increase in any State revenues to provide for repayment.

It is intended that the Raleigh facility will be sustainably designed, i.e., the building and surrounding environs will be designed using features that are energy efficient, incorporate reusable and renewable resources, provide natural lighting, are nontoxic, require low maintenance, are congruent with the natural characteristics of the site, and cause minimum adverse impact to the environment.

REALLOCATE WATER BOND FUNDS

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-156	**SB 1381**	**Senator Kerr**

AN ACT TO REALLOCATE THE PROCEEDS OF THE CLEAN WATER BONDS.

Overview: This act reallocates $200 million in Clean Water Bonds proceeds from a program that makes loans to local governments, to related grant programs. The act also revises caps on some of the grants, places a moratorium on making grants from one-half of the reallocated proceeds, and requires the State Infrastructure Council to study the geographic distribution of loans and grants from Clean Water Bonds proceeds.

Fiscal Impact: Converting some of the loan funds to grant funds will reduce loan repayments credited to the General Fund in an amount estimated to range from about $1 million to $20 million a year between 2001 and 2005.

Effective Date: August 1, 2000.

Background: S.L. 1998-132 authorized the issuance of $800 million in Clean Water Bonds. The bonds were approved by the voters in November 1998. Of the $800 million, $300 million was designated for loans to local governments, administered by DENR, to be used for water supply systems, water conservation projects, water reuse projects, wastewater collection systems, and wastewater treatment works. Repayments of the loans are credited to the General Fund. The remaining $500 million of Clean Water Bond proceeds was allocated for various grant programs and to match federal wastewater or water assistance funds. S.L. 1998-132 provided that the $800 in Clean Water Bonds could be reallocated by the General Assembly between the various loan and grant programs designated in the act.

Analysis: This act withdraws $200 million of the $300 million loan funds and reallocates the funds for the following four grant programs that were established in the Clean Water Bonds act:

- $146 million for High Unit Cost Grants. High Unit Cost Grants are grants administered by DENR for wastewater and water system projects that would otherwise require estimated household water and sewer user fees greater than 1.5% of the median household income. These grants are administered under the Clean Water Revolving Loan and Grant Fund.

- $25.9 million for Unsewered Community Grants. Unsewered Community Grants are grants administered by the Rural Economic Development Center for units of local government serving small, rural communities not served by centralized sewer systems for wastewater collection and treatment.

- $28.1 million for Supplemental and Capacity Grants. Supplemental Grants are grants administered by the Rural Economic Development Center to help local governments match other grant or loan funds. Capacity Grants are grants administered by the Rural Economic Development Center to help local governments pay the cost of preparing grant and loan applications, capital improvement plans, and other efforts to support growth and development in rural areas. The act also makes a conforming change to the annual total limits on these Supplemental and Capacity Grants, raising the Supplemental Grant limit from $8 million to $12 million and raising the Capacity Grant limit from $2 million to $3 million.

The act places a moratorium on granting part of the $200 million in bond proceeds reallocated for grants. Only one-half of these funds may be granted before March 31, 2001; the remainder may be granted after that date. The first one-half of the $146 million reallocated for High Unit Costs Grants is available only to units whose applications were filed with DENR by July 1, 2000. The moratorium was imposed in response to concerns by some local governments that the Clean Water Bond proceeds were being awarded in a manner that favored some geographical areas over others. To address these concerns, the act directs the State Infrastructure Council, an advisory body established in the Clean Water Bond Act, to study the geographic distribution of loans and grants and report any disparities or inequities by December 1, 2000.

Finally, this act modifies the cap on grants made under the Clean Water Revolving Loan and Grant Fund. Under prior law, a unit of local government could not receive grants exceeding $3 million a year. This act reduces the cap to $3 million over three years, except that the cap is not reduced for water districts and sewer districts that include three or more local government units, or for counties in which less than 50% of the population is served by a government or nonprofit public water system. The reduction of the cap on grants will apply to grants made on or after the date the act became law, July 13, 2000, but will take into account grants made on or after July 1, 1999, in determining whether the three-year cap has been exceeded. The purpose of this change was to address concerns by some units of local government that too much of the available funds was going to larger grants to a small number of units.

BROWNFIELDS TAX INCENTIVE

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-158	**SB 1252**	**Senator Odom**

AN ACT TO CREATE A TAX INCENTIVE FOR THE REDEVELOPMENT OF BROWNFIELDS PROPERTIES, AS RECOMMENDED BY THE ENVIRONMENTAL REVIEW COMMISSION.

Overview: This act allows a partial exclusion from property taxes for qualifying improvements made on brownfields property. The partial exclusion is limited to five years and decreases from an exclusion of 90% in the first year to an exclusion of 10% in the fifth year. The Environmental Review Commission recommended this exclusion. Additionally, this act amends the statute governing brownfields agreements so that the Department will give particular consideration to the written comments of units of local government with taxing jurisdiction over property subject to the brownfields agreement.

Fiscal Impact: This act does not affect General Fund revenues. The fiscal impact of this act on local government revenues is not clear. However, Department of Environment and Natural Resources staff and numerous county tax assessors feel that the additional property tax revenue provided by improvements to brownfields sites would be far greater than the combined tax loss over the five-year partial exemption period.

Effective Date: The section of this act that established the property tax exclusion becomes effective for taxable years beginning on or after July 1, 2001. The remainder of the act became effective August 2, 2000.

Background & Analysis: This act provides that improvements made to real property that is subject to a brownfields agreement will be granted a partial property tax exclusion for the first five taxable years beginning after completion of qualifying improvements made after the later of July 1, 2000, or the date of the brownfields agreement. The property entitled to the exclusion must be appraised annually during the period that the owner is entitled to the exclusion.

The amount of the exclusion declines over the five-year period as follows:

Year	Percent of appraised value excluded
1	90%
2	75%
3	50%
4	30%
5	10%

Additionally, this act amends G.S. 130A-310.34(d) to require the Department of Environment and Natural Resources, when developing brownfields agreements, to give particular consideration to written comment from the local governments having taxing jurisdiction over the brownfields property.

In 1997, the General Assembly enacted The Brownfields Property Reuse Act of 1997. Brownfields property is defined in that act as abandoned, idled, or underused property at which expansion or redevelopment is hindered by actual environmental contamination or the possibility of environmental contamination and that is or may be subject to remediation. Under the 1997 act, the Department of Environment and Natural Resources may enter into a brownfields agreement with a prospective developer. These brownfields agreements allow a developer to clean up a contaminated property to a level that is less "clean" than would otherwise be required by law in exchange for subjecting the property to land-use restrictions. A developer who complies with the agreement will not be held liable for clean-up of areas of contaminants identified in the agreement, so long as the activities conducted on the property do not increase the risk of harm to public health or the environment.

NONHAZARDOUS DRY-CLEANING TECH. INCENTIVE

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-160	**HB 1583**	**Representative Gibson**

AN ACT TO PROVIDE AN INCENTIVE FOR INVESTING IN DRY-CLEANING EQUIPMENT THAT DOES NOT USE HAZARDOUS SUBSTANCES AND TO MODIFY THE AUTHORIZATION FOR INVESTING STATE FUNDS IN RURAL NORTH CAROLINA.

Overview: This act provides a tax credit for commercial dry-cleaners who invest in environmentally friendly dry-cleaning equipment. Additionally, this act modifies the way in which the State Treasurer may invest certain funds held by the State Treasurer. The Environmental Review Commission recommended the dry-cleaning portion of this act.

Fiscal Impact: The estimated General Fund loss of the tax credit enacted by this act is as follows:

Fiscal Year	**Fiscal Impact**
2001-2002	($584,100)
2002-2003	($423,000)
2003-2004	($507,600)
2004-2005	($625,200)

Effective Date: The tax credit enacted by this act is effective for taxable years beginning on or after July 1, 2001, and is repealed for taxable years beginning on or after January 1, 2006. The remainder of this act became effective August 2, 2000.

Background & Analysis: This act adds a new section to Article 3B of Chapter 105 of the General Statutes, which provides tax credits for investing in general business property, renewable energy property, and low-income housing. The new section provides a tax credit for commercial dry-cleaners who buy or lease "qualified dry-cleaning equipment." "Qualified dry-cleaning equipment" is defined as dry-cleaning equipment that does not use any of the following:

- A chlorine-based solvent.
- A hydrocarbon-based solvent.
- A solvent that contains a hazardous substance as defined in the federal Comprehensive Environmental Response, Compensation, and Liability Act.

- A solvent that contains a substance determined by the Environmental Protection Agency or the National Institute of Occupational Safety and Health to possess carcinogenic potential to humans.

- A substance that the Department of Environment and Natural Resources (DENR) determines to pose a threat to human health or the environment.

It is estimated that 99% of the State's dry-cleaners currently use chlorine-based or hydrocarbon-based solvent. Use of these solvents has led to soil and groundwater contamination.

The new credit, which is similar to the renewable energy credit that was enacted in 1999, (*See*: S.L. 1999-342) provides a credit for equipment placed in service in this State equal to 20% of the taxpayer's cost. Like the other credits in Article 3B, this credit may be taken against corporate or individual income tax or corporate franchise tax, at the taxpayer's choice. The total credits allowed under Article 3B may not exceed 50% of the taxpayer's tax liability in any given year. Any excess over this limit may be carried forward for up to five years**.** Article 3B requires the taxpayer to maintain and make available in case of audit any records necessary to determine and verify the amount of the credit to which the taxpayer is entitled. A taxpayer claiming the credit allowed under the new section must file with the tax return a certification by DENR that the equipment purchased or leased by the taxpayer is "qualified dry-cleaning equipment." No credit is allowed under this section for equipment for which the taxpayer claims another credit under Chapter 105 of the General Statutes.

Section 2 of this act modifies the ways in which the State Treasurer may invest certain State funds. G.S. 147-69.2 sets out the permitted investments for cash in trust funds and special funds held by the State for any purpose other than meeting State appropriations. Under prior law, G.S. 147-69.2 allowed the State Treasurer to invest up to $20 million in the obligations and securities of the North Carolina Enterprise Corporation. Section 2 expands this authorization to include the North Carolina Economic Opportunities Fund. Since $10 million is currently invested in the North Carolina Enterprise Corporation, the State Treasurer could, but is not required to, invest up to $10 million in the North Carolina Economic Opportunities Fund.

The North Carolina Economic Opportunities Fund is a Small Business Investment Corporation (SBIC). An SBIC is an investment company licensed by the federal Small Business Administration to invest in small businesses. Once licensed, the SBIC can leverage two dollars in federal investment funds for each dollar in non-federal funds invested. The purpose of the North Carolina Economic Opportunities Fund is to provide venture capital for smaller companies in rural North Carolina. Initial financings would typically range from $500,000 to $2 million with investments generally in the form of preferred stock, common stock, or subordinated debts with warrants.

Section 2 of this act also modifies G.S. 147-69.2 to allow the reinvestment in venture capital investments of any income from these venture capital investments without regard to the respective $20 million and $30 million caps. The result of the change is that the State Treasurer could invest substantially more than $50 million in capital projects depending on the economic success of past projects.

The State Treasurer has a fiduciary duty to seek the best possible investments in terms of return and safety. Existing law reflects the policy of the State that the State Treasurer's investment decisions should be professional decisions made in the best interest of the owner of the assets and not influenced by political or economic development considerations. The Treasurer is independent of fiscal control by the Governor and is authorized to contract with independent professionals and experts as necessary for proper administration of the investment programs. The Treasurer is required to establish annual yield targets for investments and to report annually to the General Assembly on the nature and character of all investments, the return on the investments, and the extent to which the annual yield targets have been reached. The Treasurer is also required to report quarterly on all investments to the Joint Legislative Commission on Governmental Operations and to the Co-Chairs of the House and Senate Appropriations Committee

UNC APPROPRIATED CAPITAL/

REVENUE BONDS

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-168	**HB 1853**	**Representative Miller**

AN ACT TO AUTHORIZE THE CONSTRUCTION AND THE FINANCING, WITHOUT APPROPRIATIONS FROM THE GENERAL FUND, OF CERTAIN CAPITAL IMPROVEMENTS PROJECTS OF THE CONSTITUENT INSTITUTIONS OF THE UNIVERSITY OF NORTH CAROLINA AND TO AMEND THE LAWS REGARDING CERTAIN REVENUE BONDS THAT MAY BE ISSUED BY THE BOARD OF GOVERNORS.

Overview*:* This act authorizes the construction of several projects by The University of North Carolina. The projects will be financed through revenue bonds and special obligation bonds, not appropriations from the General Fund.

Fiscal Impact: The projects authorized by this act will not be constructed with General Fund revenues. However, there are two projects that the institutions will request a General Fund appropriation for operating expenses. The General Fund expenditure for fiscal year 2001-2002 is expected to be $113,179.

Effective Date: The act became effective July 10, 2000.

Background & Analysis: There are two types of self-liquidating bonds that may be issued by the Board of Governors of the University of North Carolina: revenue bonds and special obligation bonds. These bonds are not payable from tax revenues. However, the General Assembly must authorize the projects for which special obligation bonds may be issued. Although the statute does not expressly require legislative authorization of revenue bond projects, the General Assembly has historically authorized the projects for many years. This act sets forth the self-liquidating projects the Board of Governors plans to finance with revenue or special obligation bonds this year.

Article 21 of Chapter 116 of the General Statutes authorizes the Board of Governors to issue revenue bonds for the types of projects enumerated in the article. The types of projects for which revenue bonds may be issued include educational buildings, dormitories, recreational facilities, dining facilities, student centers, health care buildings, parking decks, etc. The revenue bonds are payable from rentals, charges, fees, and other revenues such as gifts.

Article 3 of Chapter 116D of the General Statutes, enacted this session by S.L. 2000-3, authorizes the Board of Governors to issue special obligation bonds. Special obligation bonds are payable with any sources of income or receipts of the Board of Governors or a constituent or affiliated institution, but not including tuition payments or appropriations from the General Fund from State revenues. The bond proceeds could be used for construction, improvement, and acquisition of any capital facilities located at UNC constituent and affiliated institutions.

This act also rewrites the existing revenue bond law for clarification purposes. It rewrites the definition of "institution" to recognize that UNC Hospitals at Chapel Hill is now referred to and known as the UNC Health Care System and to include The University of North Carolina General Administration. It rewrites the definition of "project" in the revenue bond law to conform the authority of the Board of Governors to issue revenue bonds for academic facilities to the wording of the authority granted in the special obligation law this year with the passage of S.L. 2000-3.

REFUND OVERPAYMENT OF DEED STAMP TAX

Session Law #	*Bill #*	*Sponsor*

S.L. 2000-170	HB 1544	Representative Pope

AN ACT TO CLARIFY THAT A TAXPAYER IS ENTITLED TO A REFUND OF AN OVERPAYMENT OF THE STATE EXCISE TAX ON CONVEYANCES.

Overview: This act establishes a procedure through which a taxpayer may request a refund of an overpayment of the State excise tax on conveyances.

Fiscal Impact: No General Fund impact. The bill will affect other funds as follows:

- Parks & Rec. Trust Fund No Impact to Less than $2000 per Year
- Natural Heritage Trust Fund No Impact to Less than $1000 per Year
- Local Government Minimal Impact in Selected Counties

Effective Date: July 13, 2000, and applies retroactively to taxes paid on or after January 1, 2000.

Background & Analysis: The excise tax on conveyances, known as the deed stamp tax, is a State tax on instruments transferring an interest in real property. The register of deeds of the county in which the property is located collects the tax when the deed transferring the property is recorded. The person presenting the instrument for recording is responsible for indicating on the instrument the amount of tax due. The register of deeds must collect the tax due and mark on the instrument to indicate payment of the tax and the amount paid. The tax rate is $1.00 for each $500.00 (0.2%) of the value of the property conveyed. The county retains one-half of the net proceeds of the tax and remits the remaining one-half to the State. Seventy-five percent of the funds remitted to the State is dedicated to the Parks and Recreation Trust Fund created in G.S. 113-44.15 and 25% is dedicated to the Natural Heritage Trust Fund created in G.S. 113-77.7. None of the State's share of the excise tax on conveyances goes to the General Fund.

The prior law did not provide a mechanism for a taxpayer to receive a refund of an overpayment of the excise tax on conveyances. The tax is governed generally by the administrative provisions in Article 9 of Chapter 105 of the General Statutes. Under Article 9, a taxpayer must apply to the Secretary of Revenue for a refund of an overpayment of tax. However, the State excise tax is administered at the county level, as opposed to the State level. Therefore, the refund procedure in Article 9 did not work well for the excise tax on conveyances.

This act provides that a taxpayer that pays more tax than is due may request a refund of the overpayment by filing a written request for a refund with the board of commissioners of the county where the tax was paid. The request must be filed within six months after the date the tax was paid and must explain why the taxpayer believes a refund is due. There will probably be few situations in which a refund is requested, because the taxpayer is responsible for indicating the amount of tax due. However, there are instances when an instrument is recorded in the wrong county. In those cases, no tax would be due in the county where the instrument was recorded and the taxpayer should be entitled to a refund of the tax paid.

The act provides that the board of county commissioners must review a request for a refund within the time limitations of G.S. 105-266.1. The board must hold a hearing on the request within 90 days after receiving it. The board must make its decision on the request within 90 days after the hearing and it must send a copy of its decision to the Secretary of Revenue. If the board determines that a refund is due, it must refund the county's portion of the overpayment with interest to the taxpayer. If the board determines that a refund is not due, it must inform the taxpayer that the taxpayer may request the Secretary of Revenue to review the decision.

To obtain the Secretary's review of the board's decision, the taxpayer must request a hearing in writing. The request must be filed within 30 days after the taxpayer receives the board of county commissioners' decision denying the refund. Like the board, the Secretary must review the request for a refund within 90 days after the Secretary receives the request. The Secretary must send the board a copy of the Secretary's decision. The Secretary's decision is binding on the board of county commissioners. If the Secretary determines that a refund is due, the board must refund the county's portion of the overpayment with interest to the taxpayer.

A taxpayer that disagrees with the Secretary's decision may bring an action against the county and the State to recover the disputed amount. The action may be brought in the Superior Court of Wake County or in the superior court of the county where the tax was paid.

Before the taxpayer may receive a refund, the taxpayer must record a new instrument indicating the correct amount of tax due. If no tax is due because the instrument was recorded in the wrong county, the taxpayer must record an instrument stating that no tax was owed and the reason why. Once the correcting instrument has been recorded, the register of deeds must notify the county finance officer and the Secretary of Revenue so that the overpayment may be refunded to the taxpayer. Like other State taxes, the overpayment bears interest at the rate established in G.S. 105-241.1. The interest begins to accrue on the overpayment 30 days after the taxpayer requests a refund of the tax.

REVENUE LAWS CLARIFYING CHANGES

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-173	**HB 1290**	**Representative Luebke**

AN ACT TO IMPROVE THE ADMINISTRATION OF THE TAX LAWS BY MAKING CLARIFYING AND CONFORMING CHANGES TO THE REVENUE AND RELATED LAWS.

Overview: This act makes numerous clarifying and conforming changes to the revenue laws and related statutes as recommended by the Revenue Laws Study Committee. These changes were originally included in House Bill 1575. Additional conforming and technical changes to the revenue laws were made in Senate Bill 1335, enacted as S.L. 2000-140.

Fiscal Impact: Only section 2 of the act has a fiscal impact *(see Background & Analysis section).*

Effective Date: August 2, 2000, unless otherwise provided *(see Background & Analysis section).*

Background & Analysis: The following table provides a section-by-section analysis of the changes:

Section	**Explanation**
1	Reorganizes the sunsets for the William S. Lee Act and the General Business Credits Act, so that the sunset language will be codified within each Act. Also codifies the William S. Lee Study provisions with the sunset. Codifying the sunsets separates the two Acts' sunsets, which were in the same session law, and makes them easier for taxpayers to find. This section also clarifies the sunset of the Renewable Energy Tax Credits added to the General Business Credits Act in 1999.
2	Clarifies that the $100 local tax limitation enacted in S.L. 1999-438 for loan agencies and other related businesses does not repeal the pre-existing local authority to tax pawnbrokers up to $275 a year. This section becomes effective July 1, 2001. This section will allow local governments to regain revenue lost due to the 1999 legislation. Based on a 1996 survey of local governments, if all local governments changed their ordinance in response to the 1999 legislation, they would have experienced a loss of $47,999.

3	Clarifies that a county or city does not share in the distribution of beer and wine tax if the only place where beer and wine sales are authorized in the county or city is a sports club. Also repeals an obsolete subsection.
4	Eliminates the requirement that resident breweries, resident wineries, and nonresident vendors file an invoice with the Secretary and that two copies of the invoice be given to wholesalers and importers. The person will still be required to file a report that contains the information required by the Secretary.
5	Conforms the discount statutes for excise taxes on beer, wine, and liquor to those for tobacco products so that they are uniform. The language, that the discount is not allowed on taxpaid beverages given as free goods for advertising, is removed because similar language is not included in the tobacco product article. The Department of Revenue plans to administer the excise tax on tobacco products and the excise taxes on beer, wine, and liquor through the same computer program.
6	Allows the resident breweries, resident wineries, and nonresident vendors to keep information needed to file reports with the Department of Revenue in a format that is useful to them by not restricting them to invoices. These businesses will have to keep records of the information needed to file reports and returns for three years.
7	Repeals the special franchise taxes on telegraph companies and street bus companies. According to the Department of Revenue, there are no taxpayers paying tax under these provisions. With repeal of these special taxes, the general corporate franchise tax will apply to any company that might have otherwise fallen under the provisions of the special taxes.
8	Repeals a cross-reference to the special franchise tax on street bus companies, repealed by section 7 of the act, and reorganizes the language of the statute.
9	Changes the form of the definition of "manufactured home" in the sales tax law from a restatement of federal standards to a cross-reference to federal standards. This section also codifies an administrative application of the sales tax definition for ‘manufactured home" to include a modular home that is built on a permanent chassis and is transportable in one or more sections.
10	Clarifies that a retailer for purposes of the Highway Use Tax must be engaged in the business of selling or leasing motor vehicles, and clarifies and updates definition language in Chapter 20 of the General Statutes.
11	Allows the Department of Revenue to exchange information with the Division of Adult Probation and Parole of the Department of Correction. This change will assist in collecting

	the controlled substances tax.
12	Clarifies that motor carrier fuel tax assessments based on presumed mileage are used only if the Department of Revenue considers the presumption reasonable. The section also corrects incorrect terminology and changes sentence order.
13	Effective July 1, 2000, changes the method by which tax on fuel is charged at the destination state's rate when the fuel is simultaneously sold from one supplier, to another supplier, to a customer who picks the fuel up at the rack for export. S.L. 1998-146 attempted to address this situation by expanding the definition of two-party exchange to include buy-sell agreements as one type of two-party transaction for purposes of the definition of "supplier". That change created confusion and led to mismatches between terminal operator reports and supplier returns. This section changes back to the old, narrower definition of two-party exchange and then adds a specific provision allowing the destination state's tax rate to be paid when the fuel is transferred at the rack pursuant to a buy-sell agreement.
14	Restores to the definition of "user" a provision that was inadvertently deleted, and makes conforming changes to reflect defined term. This added provision, regarding vehicle weight threshold was formerly provided in G.S. 105-449.9 (repealed). Since users are subject to audit, the vehicle weight threshold will limit the audits to larger vehicles.
15	Conforms the motor fuel excise tax exemption statute to reflect that an unlicensed exporter or distributor is liable for the tax under G.S. 105-449.82(c). This change exempts fuel from the tax only when it is removed by a licensed distributor or licensed exporter.
16	Conforms the statute catchline by removing a reference to a repealed provision.
17	Incorporates a change concerning "locked pumps" made by the federal law in 1998. The federal change already applies in the State, and the bill simply codifies the change and clarifies that a distributor is still eligible for a refund of the excise taxes paid on kerosene if the pump meets the requirements of federal law. A "locked pump" is one that is kept locked by the retailer and must be unlocked by the retailer for each sale of kerosene. The distributor may currently apply for a refund if the dispensing device for the kerosene is not suitable for use in fueling a highway vehicle.
18	Restores a provision making fuel retailers and bulk-end users subject to audit by the Department of Revenue. S.L. 1999-438 repealed the requirement that retailers and bulk-end users obtain licenses. An unintended consequence of this repeal was elimination of the Department's audit authority over these users and sellers of motor fuel.

19	Moves the tax exemption language for "911" telephone service from G.S. 62A-5 to the corporate income tax statutes. This change makes Articles 1 and 2 of Chapter 62A consistent.
20	Effective date

CONDUIT AGENCY FINANCING

Session Law #	*Bill #*	*Sponsor*
S.L. 2000-179	**SB 1472**	**Senator Rand**

AN ACT TO PROVIDE REVENUE BOND FINANCING OF CERTAIN PRIVATE PROJECTS THAT PERFORM A PUBLIC PURPOSE AND TO REORGANIZE THE INDUSTRIAL FACILITIES AND POLLUTION CONTROL FINANCING AUTHORITY.

Overview: This act provides specific statutory authority for conduit financing of special purpose projects through County Industrial Facilities and Pollution Control Financing Authorities and the North Carolina Capital Facilities Finance Agency. In a conduit financing, a governmental entity issues its bonds to finance facilities for a private party, then receives payments from the private party to service the bonds. The "special purpose projects" that may be financed through conduit financing include:

- Water systems and facilities
- Sewage disposal systems or facilities
- Public transportation systems, facilities, or equipment
- Public parking facilities
- Public auditoriums and similar facilities
- Recreational facilities
- Solid waste facilities
-
- Facilities for persons with disabilities and for the disadvantaged, such as Goodwill stores and sheltered workshops, but not including retail establishments unless 75% of the inventory is used, donated goods and 75% of the employees will be disadvantaged or disabled persons
- Student housing facilities owned by entities other than educational institutions

Fiscal Impact: No fiscal impact.

Effective Date: The act became effective July 1, 2000.

Background & Analysis: This act provides specific statutory authority for conduit financing of special purpose projects. In a conduit financing, a governmental entity issues its bonds to finance facilities for a private party, then receives payments from the private party to service the bonds. If the federal tax law permits tax-exempt bond issues for the type of facility financed, the private party is able to borrow at tax-exempt rates.

Prior to the enactment of this act, conduit financing was available to a limited extent in North Carolina. County Industrial Facilities and Pollution Control Financing Authorities and the NC Industrial Facilities and Pollution Control Financing Authority can provide conduit agency financing for private industrial and pollution facilities. The NC Educational Facilities Finance Agency can provide conduit financing for educational facilities. Counties and cities may also provide conduit financing directly.

Federal law allows tax-exempt conduit financing for a variety of projects beyond the industrial, pollution control, and educational projects currently authorized in Chapters 159C, 159D, and 115E of the General Statutes. Recent financings have been proposed and entered into for new types of projects, such as recreational facilities to be leased to or operated by a YMCA. The Treasurer's Office had two concerns about the expansion of the type of projects being financed under the prior law. First, although the projects had a public purpose and satisfied federal requirements, the North Carolina statutes did not clearly authorize conduit financing for these types of projects. Second, to the extent the conduit financing was conducted directly by a local government, rather than a special purpose authority, the local government's credit rating was at risk if the private entity were to go into default.

This act addresses the Treasurer's concerns by providing specific statutory authority for conduit financing of special purpose projects. To accomplish this expansion, it makes the following changes regarding revenue bonds issued on behalf of private entities:

- Expands the NC Educational Facilities Finance Agency to become the NC Capital Facilities Finance Agency, and authorizes the agency to issue bonds on behalf of private entities for various projects that have a public purpose ("special purpose projects").

- Authorizes County Industrial Facilities and Pollution Control Financing Authorities to issue bonds on behalf of private entities for various projects that have a public purpose.

- Dissolves the NC Industrial Facilities and Pollution Control Financing Authority and transfers its powers and duties to the NC Capital Facilities Finance Agency.

"Special purpose projects" encompass a variety of private, public purpose projects. The types of projects that the act gives County Industrial Facilities and Pollution Control Financing Authorities and the NC Capital Facilities Finance Agency the power to finance are:

- Water systems and facilities

- Sewage disposal systems or facilities

- Public transportation systems, facilities, or equipment

- Public parking facilities

- Public auditoriums and similar facilities

- Recreational facilities

- Solid waste facilities

- Facilities for persons with disabilities and for the disadvantaged, such as Goodwill stores and sheltered workshops, but not including retail establishments unless 75% of the inventory is used, donated goods and 75% of the employees will be disadvantaged or disabled persons

Student housing facilities owned by entities other than educational institutions would also be authorized for the Capital Facilities Financing Agency. Under prior law, the NC Educational Facilities Financing Agency could provide conduit financing for student housing facilities owned or operated by an educational institution. The inclusion in this act of student housing that is not owned or operated by an educational facility addresses current proposals to finance private, nonprofit housing for students at various universities, including Appalachian State University, Fayetteville State University, and North Carolina Agricultural and Technical State University.

The act renames the NC Educational Facilities Finance Agency and it recodifies its statutes from Chapter 115E of the General Statutes to Article 2, of Chapter 159D of the General Statutes to reflect the broader financing authority given to it under this act. Besides educational facilities, the authority, renamed the NC Capital Facilities Finance Agency, may provide conduit financing for special purpose projects. One reason for the expansion of this authority is to allow it to provide conduit financing for multi-county projects, such as a proposed multi-county recreational facility to be operated by a YMCA near Winston-Salem. Industrial Facilities and Pollution Control Financing Authorities created by county governments have limited ability to finance multi-county projects.

The act also authorizes the NC Educational Facilities Finance Agency to take over the remaining responsibilities of the NC Industrial Facilities and Pollution Control Financing Authority, which is dissolved under this act. The Industrial Facilities and Pollution Control Financing Authority, created under Chapter 159D of the General Statutes, is a State entity that issued bonds in the late 1980s and early 1990s for purposes similar to those provided for County Industrial Facilities and Pollution Control Financing Authorities. The State authority is moribund at this time due to the loss of records regarding its creation and membership. However, administrative duties regarding its outstanding bonds continue to arise from time to time. Although additional bonds are not expected to be issued under Chapter 159D for industrial or pollution control projects, the act makes a few changes to conform the provisions to those governing County Industrial Facilities and Pollution Control Financing Authorities in Chapter 159C, and to delete obsolete provisions.

Under the act, a private entity (either nonprofit or for-profit) could obtain financing from a County Industrial Facilities and Pollution Control Financing Authority or from the North Carolina Capital Facilities Finance Agency in order to acquire, construct, and improve a special purpose project. The act authorizes both the initial financing of special purpose projects and the refinancing of pre-existing debt for special purpose projects. The financing would usually be tax-exempt under federal law and could include revenue bonds or other forms of debt, but would not include any financing that pledges the faith or credit of the State, a local government, or any political subdivision. The advantage to private entities of tax-exempt financing is that interest rates on tax-exempt financing are significantly lower than on taxable financing. The private entity must pay for the entire cost of the financing and of the facility being financed.

Besides providing tax-exempt financing for capital facilities for special purpose projects, conduit financing may cover land acquisition, landscaping, site preparation, furniture, and machinery and equipment, as well as engineering and architectural services and other administrative expenses related to construction or acquisition of a project. Financing from the Capital Facilities Finance Agency is not available for projects that discriminate based on race, creed, color, or national origin. The law governing County Industrial Facilities and Pollution Control Financing Authorities does not contain a similar restriction.

Conduit financing through the State would be administered by the Capital Facilities Finance Agency, which is located in the Department of State Treasurer. The Agency has seven members: the State Treasurer, the State Auditor, one member appointed upon the recommendation of the President Pro Tempore of the Senate, one member appointed upon the recommendation of the Speaker of the House of Representatives, and three members appointed by the Governor. The appointive members must be residents of North Carolina and cannot hold other public office. The Agency is audited annually and submits an annual report to the Governor and the General Assembly.

A private entity could qualify for financing only if the Agency found it to be financially responsible and capable of fulfilling its obligations. Before financing is approved, the Agency must find that the entity has provided adequately for the payment of principal and interest on the bonds and for the operation, repair, and maintenance of the facility to be financed. The act clarifies that the Agency, in making this finding, may consider whether the private entity on behalf of whom the bonds will be issued has arranged for delivery of a letter of credit or for any other credit enhancement to secure the obligations. Similar provisions are found in the current law governing County Industrial Facilities and Pollution Control Financing Authorities.

Public notice and a public hearing are required before the bonds may be approved. The governing body of the county, and of any municipality, in which the project will be located must be notified of the hearing.

The Agency may issue bonds only if the Local Government Commission approves them. The Local Government Commission sets the interest rates on the bonds and administers their sale. The bonds may be secured by a trust agreement with a corporate trustee, such as a bank. The Agency will require the private entity to pay fees, loan repayments, rents, or other charges sufficient to cover the payment of principal and interest on the bonds and the operation, repair, and maintenance of the facility to be financed, and the bonds will be secured by the pledge of these revenues.