# LEGISLATIVE RESEARCH COMMISSION

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# REVENUE LAWS


## REPORT TO THE 1981 GENERAL ASSEMBLY OF NORTH CAROLINA 1982 SESSION

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# REVENUE LAWS


## REPORT TO THE 1981 GENERAL ASSEMBLY OF NORTH CAROLINA 1982 SESSION

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STATE OF NORTH CAROLINA

LEGISLATIVE RESEARCH COMMISSION

STATE LEGISLATIVE BUILDING

RALEIGH 27611

May 20, 1982

TO THE MEMBERS OF THE 1981 GENERAL ASSEMBLY (1982 REGULAR SESSION):

The report of the Legislative Research Commission's Committee on Revenue Laws made pursuant to Resolution 61 of the 1981 Session is attached.

The Legislative Research Commission adopts, approves and recommends to the 1982 Regular Session of the General Assembly the following recommendations: Legislative Proposals 4, 10, 14, 17, 32 and 33 of its Committee on Revenue Laws contained in this report.

The Legislative Research Commission transmits, for informational purposes only, the following recommendations: Legislative Proposals 1 through 3, 5 through 9, 11 through 13, 15, 16, 18 through 31 and 34 contained in this report.

Respectfully submitted,

Liston B. Ramsey

W. Craig Lawing

Cochairmen

1981-83

LEGISLATIVE RESEARCH COMMISSION MEMBERSHIP

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PREFACE

The Legislative Research Commission, authorized by Article 6B of Chapter 120 of the General Statutes, is a general purpose study group. The Commission is cochaired by the Speaker of the House and the President Pro Tempore of the Senate and has ten additional members, five appointed from each house of the General Assembly. Among the Commission's duties is that of making or causing to be made, upon the direction of the General Assembly, "such studies of and investigation into governmental agencies and institutions and matters of public policy as will aid the General Assembly in performing its duties in the most effective manner" (G.S. 120-30.17(1)).

At the direction of the 1981 General Assembly, the Legislative Research Commission has undertaken studies of numerous subjects. These studies were grouped into broad categories, and each member of the Commission was given responsibility for one category of study. The Cochairmen of the Legislative Research Commission, under the authority of General Statutes 120-30.10(b) and (c), appointed committees consisting of members of the General Assembly and the public to conduct the studies. Cochairmen, one from each house of the General Assembly, were designated for each committee.

The study of the revenue laws of North Carolina was authorized by Resolution 61 of the 1981 Session Laws. The resolution authorizes the Commission to continue the study of North Carolina's revenue laws begun in 1977.

The Legislative Research Commission grouped this study in its recreation and revenue area under the direction of Senator Robert W. Wynne. The Cochairmen of the study committee established by the Research Commission are Senator Marshall A. Rauch and Representative Daniel T. Lilley. The full membership of the committee is listed in Appendix A of this report. Resolution 61 authorizing the study and House Joint Resolution 15, which the committee was authorized to consider in determining the scope of the study, are attached as Appendix B.

## COMMITTEE PROCEEDINGS

The Legislative Research Commission's Revenue Laws Study Committee met five times. At its organizational meeting the Committee made a list of topics to be considered and decided to examine changes made in federal law by the Economic Recovery Tax Act of 1981 to determine whether conforming changes in state law were needed or desired. The Committee further decided that topics requiring considerable study should be deferred until after the June legislative session.

As in the past, the study committee proved to be an excellent forum for taxpayers and tax administrators to propose changes in the revenue laws. Numerous taxpayers appeared before the Committee to speak on topics ranging from repeal of the intangibles tax to energy tax credits. The division directors of the Department of Revenue addressed the Committee and recommended changes in the laws in their respective areas. Revenue Department personnel also appeared before the Committee to answer specific questions raised by the Committee.

A list of persons appearing before the Committee is contained in Appendix C. For those persons outside the Revenue Department who spoke to the Committee, the list indicates the group represented by the speaker, if any, or the subject of the presentation if the speaker did not represent a group. The Committee expresses its appreciation for the assistance of Mr. Mark Lynch, Secretary of Revenue, Mr. Jim Senter, Deputy Secretary of Revenue, and the staff of the Revenue Department.

Following are the recommendations of the Committee. Each recommendation is followed by an explanation of the recommendation and a report on its fiscal effect.

## RECOMMENDATIONS

The Legislative Research Commission's Study Committee on Revenue Laws recommends the following legislation:

### Legislative Proposal 1

A BILL TO BE ENTITLED AN ACT TO CONFORM THE STATE REPLACEMENT PERIOD FOR NON-RECOGNITION OF GAIN ON THE SALE OF A PRINCIPAL RESIDENCE TO THE FEDERAL PERIOD.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-144.2 is amended by deleting the phrase "18 months" each time it appears and inserting in lieu thereof the phrase "2 years".

Sec. 2. G.S. 105-144.2(c)(4) is amended by deleting the phrase "18-month" and inserting in lieu thereof the phrase "2-year".

Sec. 3. G.S. 105-144.2(c)(5) is repealed.

Sec. 4. This act is effective upon ratification and applies to old residences sold or exchanged (i) after July 20, 1981, or (ii) on or before July 20, 1981, if the rollover period under G. S. 105-144.2 determined without regard to this act expires on or after July 20, 1981.

### Explanation of Proposal 1

G. S. 105-144.2 allows a taxpayer to defer recognition of gain from the sale of a principal residence if the taxpayer either purchases a new residence within 18 months of the sale of the former residence or constructs a new residence within 2 years of the sale of the former residence, and reinvests the amount of gain realized from the sale of the former residence in the purchase or construction

of the new residence. If the taxpayer does not reinvest the full amount of the gain realized from the sale of the former residence, minus the cost of work performed on the residence in connection with its sale, in the purchase or construction of a new residence, the taxpayer must report the amount that is not reinvested as income.

This statute was enacted in 1957 in response to similar federal legislation. The economic Recovery Tax Act of 1981 amended the federal law by extending the replacement period for the purchase of a new residence from 18 months to 24 months. This bill conforms state law to the amended federal law; it extends the replacement period for the purchase of a new residence from 18 months to 24 months. Because the law no longer distinguishes between the periods allowed for the purchase and the construction of a new residence, Section 3 of the bill repeals that section of the statute which allowed a longer replacement period for construction. The bill applies to residences sold after January 19, 1980.

Fiscal Report for Proposal

Number 1

Fiscal Research Division

January 14, 1982

Explanation of Proposal:

The previous federal personal income tax rule regarding the tax-free sale of a principal residence is that the homeowner had 18 months to purchase and 24 months to construct a new residence whose cost exceeds the adjusted sales price of the old residence. The current state law tracks the old federal law.

In July the Congress, as part of the 1981 Economy Recovery Tax Act, increased the period from 18 months to 24 months. Proposal 1 would amend the state law accordingly and would apply to sales made after January 19, 1980.

Fiscal Effect:

Would have little, if any, effect on General Fund tax revenue because almost all homeowners find ways to meet the 18-month requirement.

Legislative Proposal 2

A BILL TO BE ENTITLED AN ACT TO CONFORM THE STATE LIMIT ON THE EXCLUDABLE AMOUNT OF GAIN FROM THE SALE OF A RESIDENCE TO THE FEDERAL LIMIT.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-141(b) (26) b.1. is amended by substituting the phrase "one hundred twenty-five thousand dollars ($125,000)" for the phrase "one hundred thousand dollars ($100,000)", and by substituting the phrase "sixty-two thousand five hundred dollars ($62,500)" for the phrase "fifty thousand dollars ($50,000)".

Sec. 2. This act is effective upon ratification and applies to residences sold or exchanged after July 20, 1981.

Explanation of Proposal 2

G.S. 105-141 (b)(26) allows taxpayers aged 55 or over to exclude from income up to $100,000 of gain realized from the sale of the taxpayer's principal residence. This provision is elective and is available to the taxpayer for only one sale. A married couple who owns a home jointly is considered one taxpayer in applying the $100,000 limit; thus, a husband and wife who sell their home may each exclude up to $50,000 gain.

G.S. 105-141(b)(26) was enacted in 1979 in response to similar federal legislation. The Economic Recovery Tax Act of 1981 amended the federal law by increasing the excludable amount from $100,000 to $125,000. This bill changes state law to conform to the federal change. It increases the amount of gain a taxpayer aged 55 or over may exclude upon the sale of his principal residence from $100,000 to $125,000. The increased exclusion would apply to residences sold after July 20, 1981.

Fiscal Report for Proposal

Number 2

Fiscal Research Division
January 14, 1982

Explanation of Proposal:

In 1978 the U.S. Congress enacted legislation that allowed homeowners aged 55 and over a "once-in-a-lifetime" $100,000 personal income tax exclusion for the capital gains from the sale of a principal residence. In 1979 the General Assembly enacted an identical exclusion.

In July the Congress, as part of the 1981 Economic Recovery Tax Act, increased the exclusion to $125,000. Proposal 2 would amend the North Carolina law in a similar fashion, retroactive to sales made after July 20, 1981. (federal effective date)

Fiscal Effect:

Would reduce General Fund tax revenue by an insignificant amount because:

(1) Very few elderly homeowners would have a home with a capital gain of $100,000-$125,000.

(2) Few homes are being sold at the present time.

Legislative Proposal 3

A BILL TO BE ENTITLED AN ACT TO CONFORM THE STATE FOREIGN INCOME EXCLUSION TO THE FEDERAL EXCLUSION AND TO ELIMINATE THE EXCESS FOREIGN LIVING COSTS DEDUCTION.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-141(b)(22) is amended by deleting the words "in certain camps" and inserting the words "living abroad" in lieu thereof.

Sec. 2. G.S. 105-147(1)f. is repealed.

Sec. 3. G.S. 105-147(1)g. is relettered as (1)f.

Sec. 4. This act is effective for taxable years beginning on and after January 1, 1982.

Explanation of Proposal 3

G.S. 105-141(b)(22) allows North Carolina residents who work in foreign countries and who live in camps in hardship areas while working abroad for someone other than the United States government to exclude the amount of income earned abroad from gross income to the extent it is excludable for federal income tax purposes. Section 911 of the Internal Revenue Code formerly provided that an individual who worked abroad and lived in a camp in a hardship area could exclude up to $20,000 of the income he earned abroad. "Camp" was defined as substandard lodging provided by the employer for the convenience of the employee that was near the work site and that accommodated ten or more employees. "Hardship area," as formerly defined in section 913(h)(2) of the Internal Revenue Code, meant a foreign area designated by the Secretary of State as a hardship

post where extraordinarily difficult living conditions existed.

G.S. 105-147(1)f. allows North Carolina residents who work abroad to deduct as a business expense certain expenses of living abroad to the extent they are deductible for federal income tax purposes. Former section 913 of the Internal Revenue Code allowed individuals who worked and lived in a foreign country for an entire year or for 17 out of 18 consecutive months to deduct the cost-of-living differential, housing expenses, education expenses and travel expenses.

The Economic Recovery Tax Act of 1981 rewrote section 911 of the Internal Revenue Code and repealed section 913. Amended section 911 allows an individual who works abroad for someone other than the United States government to exclude the amount of income earned abroad from gross income up to the amount set forth in the following table:

| Taxable year | Maximum amount |
|---|---|
| 1982 | $75,000 |
| 1983 | $80,000 |
| 1984 | $85,000 |
| 1985 | $90,000 |
| 1986 and thereafter | $95,000 |

Amended section 911 also allows individuals who live and work abroad to exclude an amount equal to their "housing cost amount." This exclusion applies to employees of the United States government as well as non-governmental employees.

This bill amends state law to conform to the changes in federal law made by the Economic Recovery Tax Act concerning foreign living

exclusions and deductions. Section 1 of the bill conforms state law to amended section 911 of the Internal Revenue Code. Section 2 of the bill conforms state law on foreign living deductions to federal law by repealing the section. Without the amendments made by this bill, G.S. 105-141(b)(22) and G.S. 105-147(1)f. will refer to obsolete exclusions and will be of no effect.

Fiscal Report for Proposal

Number 3

Fiscal Research Division
January 14, 1982

Explanation of Proposal:

Currently, North Carolina personal income tax law with regard to the excess foreign living expense deduction is identical to federal law. These laws also included an income tax exclusion for persons living in hardship area camps.

Beginning with the 1982 income year this present federal system of deductions and exclusions will be consolidated into a new exclusion of $75,000 increasing to $95,000 by 1986. Proposal 3 would adopt the new system for North Carolina.

Fiscal Effect:

Negligible, due to small number of individuals affected and existence of present deductions and exclusions.

Related Information:

The purpose of the special tax treatment for persons living in foreign countries is to allow for taxes paid to those countries. In some cases, taxes can be much higher than those in the U. S.

Legislative Proposal 4

A BILL TO BE ENTITLED AN ACT MAKING TECHNICAL CORRECTIONS TO THE REVENUE LAWS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-241.3(a) is amended by deleting the phrase "Article 33 of Chapter 143" each time it appears and inserting the phrase "Article 4 of Chapter 150A" in lieu thereof.

Sec. 2. G.S. 105-241.1(h) and G.S. 105-266.1(b) are each amended by deleting the phrase "The provisions of Article 33A of Chapter 143 of the General Statutes shall" and inserting in lieu thereof the phrase "G.S. 150A-29 does".

Sec. 3. G.S. 105-449.43 is rewritten to read:

"§105-449.43. Taxes and fees to be paid to Highway Fund.--All taxes and fees collected under this Article shall be paid to the State Highway Fund."

Sec. 4. G.S. 105-147(7) is amended by deleting the reference "G.S. 105-130.7(6)" and inserting the reference "G.S. 105-130.7(5)" in lieu thereof.

Sec. 5. G.S. 105-122 is amended by deleting subsection (h).

Sec. 6. This act is effective upon ratification.

Explanation of Proposal 4

Each section of the bill makes a technical correction to the revenue laws as explained below:

Section 1. G.S. 105-241.3(a), concerning appeals of Tax Review Board decisions to Superior Court, refers to Article 33 of Chapter 143. This Article was repealed effective February 1, 1976, by the Administrative Procedure Act. The correct reference to the appropriate article of the Administrative Procedure Act is Article 4 of Chapter 150A. Both Article 4 of Chapter 150A and former Article 33 of Chapter 143 deal with judicial review of administrative decisions.

Sec. 2. This section corrects two references to an Article that was repealed effective February 1, 1976. Repealed Article 33A of Chapter 143 established the rules of evidence applicable to administrative hearings. The correct reference to the appropriate part of the Administrative Procedure Act is G.S. 150A-29.

Sec. 3. This section corrects the reference to the Highway Fund in G.S. 105-449.43 and provides that fees as well as taxes collected under Article 36B of Chapter 105 be paid to the Highway Fund. G.S. 105-449.43 incorrectly refers to the Highway Fund as the State Highway and Public Works Fund. In addition to levying a highway use tax, Article 36B of Chapter 105 imposes registration fees and will impose permit fees if "An Act to Charge Motor Carriers a Fee for Obtaining a Temporary Permit" is enacted.

Sec. 4. This section corrects an incorrect reference in G.S. 105-147(7) to the definition to a holding company. "Holding company" is defined in G.S. 105-130.7(5), not G.S. 105-130.7(6). G.S. 105-147(7) concerns deductions for stock dividends.

Sec. 5. This section deletes G.S. 105-122(h). G.S. 105-122(h) contains transitional franchise tax provisions for 1968, the year in which the due date of the franchise tax was changed from July 31 to the fifteenth day of the third month following the close of the corporation's income year.

Fiscal Report for Proposal

Number 4

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

Makes technical corrections to Revenue Laws.

Fiscal Effect:

None.

Legislative Proposal 5

A BILL TO BE ENTITLED AN ACT TO EXEMPT FEDERAL CIVIL SERVICE SURVIVOR ANNUITIES FROM INHERITANCE TAX.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-3 is amended by adding a new subdivision to read:

"(8) The value of an annuity receivable by any beneficiary, other than the executor, under a federal employee retirement program to which the employee made contributions during his working years."

Sec. 2. This act shall become effective July 1, 1982, and shall apply to the estates of decedents dying on or after that date.

Explanation of Proposal 5

This bill exempts federal civil service survivor annuities from inheritance tax. Survivor annuities of state or local employees who are members of one of the state or local retirement plans are exempt from inheritance tax. Also, G.S. 105-3 currently exempts military survivor annuities from inheritance tax. The bill, therefore, extends the current exemption for state employee survivor annuities and military survivor annuities to federal civil service survivor annuities. Federal civil service survivor annuities are now taxed according to the amount of contributions made by the employee to the federal retirement system, plus accrued interest, or in accordance with a formula used by the Internal Revenue Service.

Fiscal Report for Proposal

Number 5

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

Allows a full state inheritance tax exclusion for the value of a federal civil service survivor's annuity, effective for deaths occurring on or after July 1, 1982.

Fiscal Effect:

A Revenue Department sample last year of 500 inheritance tax returns found only 15 returns that had a survivor annuity. Due to the 1979 legislation increasing the general inheritance tax exemption to $100,000, only 1 of these 15 returns would be taxable. Thus, the effect on General Fund Tax revenue would be negligible.

Related Information:

(1) Under state retirement law state and local employees' survivor annuities are exempt. In 1977 the General Assembly exempted the first $70,000 of military annuities. The 1979 General Assembly exempted the full value of military survivor annuities. Under present law Federal civil service survivor annuities and qualified private sector annuities are treated identically--the share of the annuity tied to the employee's contribution (and associated investment income) is taxable while the share associated with the employer's contribution is exempt.

(2) As far as we can determine, 8 states allow a full exclusion

of civil service survivor annuities. Approximately 3/4 of the states use the current North Carolina and Federal treatment.

(3) Federal civil service employees are not required to contribute to Social Security, nor do they draw Social Security benefits upon retirement or disability.

Legislative Proposal 6

A BILL TO BE ENTITLED AN ACT TO INCREASE THE REGISTRATION FEE CHARGED MOTOR CARRIERS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-449.48 is rewritten to read:

"§105-449.48. Registration fee.--Upon application to the Secretary and payment of a fee of five dollars ($5.00), a motor carrier may obtain a vehicle registration card and identification marker."

Sec. 2. This act shall become effective January 1, 1983.

Explanation of Proposal 6

G.S. 105-449.48 imposes a $1 registration fee on motor carriers. This act increases that fee from $1 to $5 to more accurately cover the cost to the Department of Revenue of issuing registration cards and identification markers. This registration fee has not been increased since it was first imposed in 1955.

Fiscal Report for Proposal

Number 6

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

Motor fuel tax law imposes a $1 registration fee on interstate motor carriers. Proposal 6 would increase this fee to $5, effective January 1, 1983.

Fiscal Effect:

For 1982-83, we project that 457,000 registrations will occur. The $4 increase in the fee will increase Highway Fund tax revenue by $1.8 million.

Related Information:

(1) The fee is designed to cover the Revenue Department's cost of issuing registration cards and identification markers put on trucks to indicate registration.

(2) The fee was first imposed in 1955. To adjust for inflation would lead to a fee of $4.

Legislative Proposal 7

A BILL TO BE ENTITLED AN ACT TO CHARGE MOTOR CARRIERS A FEE FOR OBTAINING A TEMPORARY PERMIT.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-449.49 is rewritten to read:

"§105-449.49. Temporary permits.--Upon application to the Secretary and payment of a fee of twenty-five dollars ($25.00), a motor carrier may obtain a temporary permit authorizing the carrier to operate a vehicle in the State without a registration card and identification marker for not more than 20 days. A motor carrier to whom a temporary permit has been issued may elect not to report its operation of the vehicle during the twenty-day period, as otherwise required by G.S. 105-449.45. A motor carrier who files a report for a quarter in which the carrier paid a temporary permit fee may claim a credit for the amount of the fee. A motor carrier whose operations are exclusively intrastate may obtain a refund of the fee by filing a report for the quarter in which the fee was paid."

Sec. 2. G.S. 105-449.45 is amended by deleting the word "Every" and inserting in lieu thereof the phrase "Except as provided in G.S. 105-449.49, every".

Sec. 3. This act shall become effective January 1, 1983.

Explanation of Proposal 7

This act imposes a fee for a temporary permit that allows a motor carrier to operate a vehicle in North Carolina without

obtaining a registration card and identification marker. The act does not require carriers to report the operation of the vehicle during the 20 day period covered by the permit. The act, however, allows those carriers who file reports with the Department of Revenue setting forth the amount of highway use tax owed by the carrier to obtain a credit against the highway use tax for the amount of the temporary permit. Carriers who operate exclusively within the State, and therefore owe no highway use tax, may obtain a refund of the permit fee.

Currently, motor carriers are not charged a fee for temporary permits. Many carriers obtain temporary permits and then do not file a report with the Department stating the amount of highway use tax owed by the carrier. By charging carriers for the temporary permit and allowing a credit or refund of the permit fee, carriers will be encouraged to file reports of their operations in North Carolina, as required by law.

Fiscal Report for Proposal

Number 7

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

Under present motor fuel tax law motor carriers may receive from the Department of Revenue a free temporary permit that allows the carrier to operate a vehicle in the state without obtaining a registration card and identification marker. For the 20 days the permit is in effect carriers are not required to report on the operation of the vehicle. One problem with the current system is that many carriers obtain temporary permits but do not file a highway use tax report with the Revenue Department.

Proposal 7 would establish a $25 permit fee and by allowing a credit or refund for this fee, carriers will be encouraged to file the required road use reports.

Fiscal Effect:

None, as carriers would receive credit or refund for fee.

Legislative Proposal 8

A BILL TO BE ENTITLED AN ACT TO ALLOW A MOTOR FUEL TAX REFUND TO THOSE WHO TRANSPORT TAXPAID MOTOR FUEL TO ANOTHER STATE FOR SALE OR USE IN THAT STATE.

The General Assembly of North Carolina enacts:

Section 1. Article 36 of Chapter 105 is amended by adding a new section to read:

"§105-446.6. Refund on taxpaid motor fuel transported to another state.--Upon application to the Secretary, any person, association or corporation who purchases motor fuel upon which the tax imposed by this Article has been paid, and who transports the fuel to another state for sale or use in that state may be reimbursed at the rate of eleven cents (11¢) per gallon for the amount of tax paid. As used in this section, to "transport" means to carry motor fuel in a cargo tank, tank car, barge or barrel and does not include carrying fuel in a tank connected with or attached to the engine of a motor vehicle."

Sec. 2. This act shall become effective July 1, 1982, and shall apply to purchases of motor fuel made on or after that date.

Explanation of Proposal 8

This bill allows a refund of 11¢ per gallon of the motor fuel tax paid on fuel that is purchased in North Carolina and transported to another state for sale or use in that state. A similar refund is allowed for special fuels exported to another state. The bill,

therefore, corrects the inequity that exists between those who export motor fuel and those who export special fuel; the latter may obtain a refund and the former may not. The bill also eliminates the problem of double taxation of the exported fuel. Now, if fuel is purchased in North Carolina, then transported to South Carolina and resold there, both North and South Carolina impose a tax on the fuel.

The refund provided by this bill is one cent less than the tax on motor fuel because one cent of the per gallon tax is used to pay for road bonds.

Fiscal Report for Proposal

Number 8

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

Under existing motor fuel tax law fuel purchasers who buy special fuel in North Carolina and transport the fuel to another state for sale or use in the other state receive a tax refund for the fuel that goes to the other state. Such a refund is not allowed to motor fuel purchasers who have a similar practice. Double taxation occurs on these purchases in the case of South Carolina because that state levies a use tax.

Proposal 8 would allow these motor fuels purchasers an 11¢ tax refund, effective July 1, 1982.

Fiscal Effect:

Negligible effect on Highway Fund revenue.

Related Information:

1¢ of the 12¢ tax would not be refunded because of debt service dedication requirements.

Legislative Proposal 9

A BILL TO BE ENTITLED AN ACT TO RETAIN PART OF THE SPECIAL FUEL TAX REFUND ALLOWED TO THOSE WHO EXPORT TAXPAID SPECIAL FUEL FOR PAYMENT OF NORTH CAROLINA HIGHWAY BONDS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-449.31 is rewritten to read:

"§105-449.31. Refund on taxpaid fuel transported to another state.--Upon application to the Secretary, any person, association or corporation who purchases special fuel upon which the tax imposed by this Article has been paid, and who transports the fuel to another state for sale or use in that state may be reimbursed at the rate of eleven cents (11¢) per gallon for the amount of tax paid. As used in this section, to "transport" means to carry special fuel in a cargo tank, tank car, barge or barrel and does not include carrying fuel in a tank connected with or attached to the engine of a motor vehicle."

Sec. 2. This act shall become effective July 1, 1982, and shall apply to purchases of special fuel made on or after that date.

Explanation of Proposal 9

G.S. 105-449.31 allows a special fuel tax refund to those who transport fuel on which the special fuel tax has been paid to another state for sale or use in that state. Unlike all other refunds, this refund is a full refund; the total amount of tax paid on the exported fuel is refunded. This bill allows a refund

of one cent less than the tax on the fuel instead of a full refund. One cent of the per gallon tax is not generally refunded because it is used to pay for road bonds.

Fiscal Report for Proposal

Number 9

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

Under existing motor fuel tax law there is a full 12¢ per gallon special fuel tax refund to purchasers who transport the fuel to another state and pay the use tax to the other state.

Proposal 9 would reduce the refund from 12¢ to 11¢, effective July 1, 1982.

Fiscal Effect:

Negligible effect on Highway Fund revenue.

Related Information:

Due to debt service dedication requirements other motor fuel and special fuel tax refunds are 11¢ instead of 12¢.

Legislative Proposal 10

A BILL TO BE ENTITLED AN ACT TO REPEAL CERTAIN REPORTING REQUIREMENTS OF DISTRIBUTORS AND VENDORS OF COIN-OPERATED MACHINES.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-250.1 and G.S. 105-113.18(4) are repealed.

Sec. 2. This act is effective upon ratification.

Explanation of Proposal 10

G.S. 105-250.1 requires persons who lease or sell juke boxes or vending machines and who are required to pay a license tax under G.S. 105-65 or 105-65.1 to file semiannual reports with the Department of Revenue giving, among other information, the location of each machine leased or sold and the serial number of the machine. Because of the enactment of the general sundries license tax in 1979, which imposes one license tax for operating a variety of vending machines, and the repeal of the per dispenser license tax, which imposed a tax on each vending machine operated by a person who was not a distributor of vending machines, this section is no longer needed. Before the repeal of the per dispenser tax, the Department used the information supplied in the semiannual report to locate persons who had purchased vending machines and had not paid the per dispenser tax for the machine. Because only one license is now required to operate a variety of vending machines, it is not cost-effective to check to see that everyone who has purchased a vending machine has paid the sundries license tax.

Fiscal Report for Proposal

Number 10

Fiscal Research Division
January 14, 1982

Explanation of Proposal:

Prior to 1979 there were a number of separate privilege license taxes on "sundry" items. These separate taxes were consolidated into a sundries tax by the 1979 General Assembly. However, a semi-annual reporting requirement that is no longer administratively cost-effective was left in the law. Proposal 9 would eliminate this reporting requirement.

Fiscal effect:

None

Legislative Proposal 11

A BILL TO BE ENTITLED AN ACT TO UPDATE THE INTERNAL REVENUE CODE REFERENCE USED BY CORPORATIONS AS A BASE FOR DETERMINING STATE NET INCOME.

The General Assembly of North Carolina enacts:

Section 1. The first paragraph of G.S. 105-130.3 is amended by deleting the phrase "in effect on January 1, 1981", and inserting in lieu thereof the phrase "in effect on January 1, 1982".

Sec. 2. This act is effective for taxable years beginning on or after January 1, 1982.

Explanation of Proposal 11

G.S. 105-130.3 requires corporations to pay an annual income tax equal to 6% of their net income, with a few adjustments. "Net income" is defined as federal taxable income as computed under the Internal Revenue Code in effect on a certain date. The statute now provides that net income equals taxable income as defined in the Internal Revenue Code in effect on January 1, 1981. The Revenue Code has been amended significantly since January 1, 1981, and the reference needs to be updated to keep the state corporate income tax tied closely to current federal law. Similar legislation was passed by the 1977, 1979 and 1981 General Assemblies.

Fiscal Report for Proposal

Number 11

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

North Carolina's corporate income tax base is almost identical to the Federal tax base and legislation was enacted during the 1977, 1979, and 1981 sessions to update the state reference to the Internal Revenue Code.

Proposal 10 conforms state law to the changes under the Economic Recovery Tax Act of 1981. The proposal would be effective for the 1982 income year.

Fiscal Effect:

Negligible effect on General Fund tax revenue.

Legislative Proposal 12

A BILL TO BE ENTITLED AN ACT TO ALLOW CORPORATIONS TO DEDUCT THE REDUCTION IN BASIS OF CERTAIN REHABILITATED BUILDINGS IN DETERMINING STATE NET INCOME.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-130.5(b) is amended by adding a new subdivision to read:

"(14) The amount by which the basis of a qualified rehabilitated building was reduced because of an investment tax credit allowed on the corporation's federal income tax return for rehabilitation expenditures made during the income year."

Sec. 2. This act is effective for taxable years beginning on or after January 1, 1982.

Explanation of Proposal 12

G.S. 105-130.3 requires corporations to pay an annual income tax equal to 6% of their federal taxable income, with a few adjustments. Under federal income tax law, and consequently state corporate income tax law, the basis of a qualified rehabilitated building must be reduced by the amount of a federal investment tax credit received for rehabilitation expenses. This bill permits corporations to deduct this reduction in basis from their federal taxable income for state income tax purposes, thereby allowing corporations to recover their investment in the building. Without this legislation, corporations could not recover their investment in a rehabilitated building because the building would be depreciated in accordance with its reduced basis.

Fiscal Report for Proposal

Number 12

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

Under present Federal and state corporate income tax law, the cost basis of a qualified rehabilitated building must be reduced by the amount of federal investment tax credit for rehabilitation expenses.

Proposal 12 would require all corporations paying the state income tax to deduct this reduction in basis from their state tax base, thereby allowing corporations to recover their investment in the building. The proposal would be effective for the 1982 income year.

Fiscal Effect:

Negligible effect on General Fund tax revenue.

Related Information:

Without Proposal 12, Corporations could not recover their investment because the building would be depreciated on the reduced cost basis.

Legislative Proposal 13

A BILL TO BE ENTITLED AN ACT TO EXEMPT CERTAIN LUMP SUM DISTRIBUTIONS FROM INHERITANCE TAX.

The General Assembly of North Carolina enacts:

Section 1. The first sentence of G.S. 105-3(5) is amended by deleting the phrase "(other than a lump sum distribution described in section 402(e)(4) of the United States Internal Revenue Code, determined without regard to the next to the last sentence of section 402(e)(4)(A) of such Code)".

Sec. 2. This act shall become effective July 1, 1982, and shall apply to estates of decedents dying on and after that date.

Explanation of Proposal 13

This bill exempts lump sum distributions received by a beneficiary of a trust established by an employer for the benefit of his employees or a retirement annuity contract purchased by an employer for the benefit of his employees from inheritance tax. Currently, annuities and other payments from these plans, except lump sum distributions, that are taxable as income to the beneficiary are exempt from inheritance tax. Now, a lump sum distribution may be taxed under the inheritance tax and also taxed as income to the beneficiary.

Fiscal Report for Proposal

Number 13

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

Under current inheritance tax law annuities and other payments from trusts established by an employer for the benefit of employees are excluded from the inheritance tax if the annunities and payments are subject to the income tax. However, lump-sum distributions under these plans are taxed under both the income and inheritance tax.

Proposal 13 would extend the exclusion to lump-sum distributions. The proposal would become effective for deaths occurring on or after July 1, 1982.

Fiscal Effect:

Negligible effect on General Fund tax revenue.

Legislative Proposal 14

A BILL TO BE ENTITLED AN ACT TO REMOVE THE REPORTING REQUIREMENTS FOR ESTATES LESS THAN $75,000 IN VALUE.

The General Assembly of North Carolina enacts:

Section 1. The second sentence of G.S. 105-22 is amended by deleting the phrase "twenty thousand dollars ($20,000)" and inserting the phrase "seventy-five thousand dollars ($75,000)" in lieu thereof.

Sec. 2. The second paragraph of G.S. 105-23 is amended by deleting the phrase "twenty thousand dollars ($20,000)" and inserting in lieu thereof the phrase "seventy-five thousand dollars ($75,000)".

Sec. 3. The second sentence of G.S. 28A-21-2(a) is amended by inserting the words "fair market" between the words "total" and "value"; and is further amended by deleting the phrase "twenty thousand dollars ($20,000)" and inserting in lieu thereof the phrase "seventy-five thousand dollars ($75,000)".

Sec. 4. This act shall become effective July 1, 1982, and shall apply to estates of decedents dying on and after that date.

Explanation of Proposal 14

This bill raises from $20,000 to $75,000 the minimum value of estates with Class A beneficiaries only for which reports and returns must be filed with the Department of Revenue under G.S.105-22 and 105-23, and for which a certification that no tax is due must be made to the clerk of court under 28A-21-2(a). The present law unnecessarily burdens clerks of court and personal representatives by requiring them to file reports and returns for estates on which no inheritance tax is due.

G.S. 105-22 requires clerks of court to obtain information from the personal representative of an estate about the decedent's property and the decedent's heirs or the beneficiaries under the will and to report this information to the Department of Revenue. Estates of less than $20,000 in value whose beneficiaries all belong to Class A are excluded from the reporting requirement. Similarly, G.S. 105-23 requires the personal representative to submit to the Department a statement containing information about the decedent's heirs or the beneficiaries under the will, an inventory of the decedent's property, and a list of gifts made by the decedent within three years of death as well as an inheritance tax return. This provision also excludes estates of less than $20,000 in value whose beneficiaries all belong to Class A from the filing requirements. G.S. 28A-21-2(a), which requires the personal representative to file a final account with the clerk of court, provides that the representative must certify that no tax return had to be filed for an estate of not more than $20,000 in value whose beneficiaries all belong to Class A.

G.S. 105-4(a) gives Class A beneficiaries a credit of $3,150 against the inheritance tax, which exempts at least $100,000 of property from the tax. Thus, an estate whose beneficiaries all belong to Class A must exceed at least $100,000 in value for the beneficiaries to owe inheritance tax. Class A beneficiaries include parents, children and spouses.

The amendment to G.S. 28A-21-2(a) also makes clear that the value of an estate is its fair market value.

Fiscal Report for Proposal

Number 14

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

The 1979 General Assembly increased the $20,000 surviving spouse exemption under the inheritance tax to a $3,150 "family credit" equivalent to the tax on the first $100,000 of taxable share to Class A beneficiaries. However, current law still requires reports and returns from estates valued at $20,000 or more.

Proposal 14 would increase the reporting threshold to $75,000 effective for deaths occurring on or after July 1, 1982.

Fiscal Effect:

None

Related Information:

(1) The threshold will be brought up to $75,000 instead of $100,000 for enforcement purposes in order to ensure that the Revenue Department receives information on some estates which, upon determination, may be found to be liable for some tax though the taxpayer claims no liability.

(2) Present law unnecessarily burdens clerks of court and personal representatives to file reports when no tax is due.

## Legislative Proposal 15

A BILL TO BE ENTITLED AN ACT TO PROVIDE THAT AMOUNTS RECEIVED FROM CERTAIN EMPLOYEE TRUSTS BE REPORTED AS INCOME ONLY IN THE YEAR IN WHICH RECEIVED.

The General Assembly of North Carolina enacts:

Section 1. The first sentence of G.S. 105-142(d) is amended by deleting the phrase "or made available" the first two times it appears in the sentence; and is further amended by deleting the phrase ",in the year in which distributed or made available" following the phrase "Internal Revenue Code of 1954 as amended".

Sec. 2. The second sentence of G.S. 105-142(d) is amended by deleting the words "or made available to" and inserting the word "by" in lieu therof; and is further amended by deleting the words "or made available" each subsequent time they appear in the sentence.

Sec. 3. The third paragraph of G.S. 105-142(d) is amended by deleting the words "or made available".

Sec. 4. This act is effective for taxable years beginning on and after January 1, 1982.

Explanation of Proposal 15

G.S. 105-142(d) provides that individuals should report as income amounts received from certain trusts established by an employer for the benefit of his employees in the year in which the amount is actually received or the year in which the amount is

made available to the individual, whichever is earlier. North Carolina follows federal law on when income from these trusts must be reported to make it easier for North Carolina taxpayers. Federal law has been amended to delete the "made available" rule; amounts received from an employee trust should be reported in the year of receipt regardless when the amount was made available to the individual. This bill changes state law to conform to federal law and deletes the "made available" rule.

Fiscal Report for Proposal

Number 15

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

Current state income tax law and former federal law provides that individuals report as income amounts received from certain trusts established by an employer for the benefit of employees in the year in which the amount is actually received, or the year in which the amount is made available to the employee, whichever is earlier. Federal law has been amended to require that the amounts received shall be reported in the year received, regardless of when the amount was made available.

Proposal 15 amends the state law to conform to the federal change, effective for the 1982 income year.

Fiscal Effect:

Negligible effect on General Fund tax revenue.

Legislative Proposal 16

A BILL TO BE ENTITLED AN ACT TO CONFORM STATE INDIVIDUAL INCOME TAX LAW ON DEPRECIATION ALLOWANCES TO FEDERAL LAW.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-147(12) is rewritten to read:

"(12) An allowance for depreciation and obsolescence of property, including an allowance for the cost of property treated as an expense under §179 of the Internal Revenue Code, and an allowance for depletion of mines, oil and gas wells, other natural deposits, and timber to the extent allowable for federal income tax purposes under the Internal Revenue Code of 1954 as amended. When the basis of property differs for State and federal purposes, the difference shall be taken into account in determining the depreciation, obsolescence or depletion allowable under this subdivision."

Sec. 2. G.S. 105-148(2) is rewritten to read:

"(2) Amounts paid for new buildings, permanent improvements or betterments made to increase the value of any property, except expenses allowed as deductions under G.S. 105-147(12)."

Sec. 3. This act is effective for taxable years beginning on and after January 1, 1982.

Explanation of Proposal 16

G.S. 105-147(12) allows taxpayers to deduct depreciation of business property to the extent allowed for federal income tax purposes. Federal law has been amended to replace the additional first year depreciation allowance with an election to treat the

cost of qualifying property as a business expense rather than a capital expenditure, thereby allowing a deduction for the full cost of the property in the year of purchase instead of a deduction over several years for depreciation of the property. This bill ensures that property costs treated as an expense under the federal election provision will be allowed as a deduction under state law.

Federal law limits the amount that may be treated as an expense as follows:

| Taxable Year | Maximum Amount |
|---|---|
| 1982 | 5,000 |
| 1983 | 5,000 |
| 1984 | 7,500 |
| 1985 | 7,500 |
| 1986 and after | 10,000 |

Fiscal Report for Proposal

Number 16

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

Current state income tax law allows taxpayers to deduct depreciation on business property to the extent allowed for federal income tax purposes. Federal law was amended in 1981 to replace the additional first-year depreciation with an election to treat the cost of qualifying property as a business expense rather than a capital expenditure, thereby allowing a full write-off in one year instead of a depreciation expense over a number of years.

Proposal 16 would conform the state law to Federal changes, effective for the 1982 income year.

Fiscal Effect:

Negligible.

Related Information:

The new federal law limits the amount that can be treated as an expense to $5,000 for 1982 and 1983, $7,500 for 1984 and 1985, and $10,000 for all years beginning with 1986.

Legislative Proposal 17

A BILL TO BE ENTITLED AN ACT TO ADOPT CIVIL AND CRIMINAL SANCTIONS FOR FURNISHING FALSE TAX WITHHOLDING INFORMATION.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-163.5 is amended by adding two new subsections to read:

"(f) In addition to any criminal penalty provided by law, if an individual furnishes his employer with an exemption certificate that contains information which has no reasonable basis and that results in a lesser amount of tax being withheld under this Article than would have been withheld if the individual had furnished reasonable information, the individual is subject to a penalty of one hundred dollars ($100.00) for furnishing the exemption certificate.

(g) An individual required to furnish information to his employer under this section who willfully supplies false or fraudulent information, or who willfully fails to supply information that would increase the amount of tax withheld under this Article shall, upon conviction thereof, be fined not more than one thousand dollars ($1,000) or imprisoned not more than six months, or both."

Sec. 2. This act is effective upon ratification and applies to offenses committed on and after that date.

Explanation of Proposal 17:

G.S. 105-163.5 requires employees to furnish exemption certificates to their employers to enable the employer to determine the amount of tax to withhold from the employee's salary. North Carolina law currently imposes no penalties for furnishing false information on an exemption certificate. Consequently, many taxpayers claim an

unreasonably large number of exemptions so no tax will be withheld from their wages. This bill imposes a civil penalty of $100.00 and a criminal penalty of up to $1,000 or imprisonment for up to six months or both for furnishing false information.

Fiscal Report for Proposal

Number 17

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

Current income tax law imposes no penalties on wage and salary employees who falsify information on a withholding exemption certificate. Proposal 17 imposes a civil penalty of $100 and a criminal penalty of up to $1,000 or imprisonment of up to six months for such a violation.

Fiscal Effect:

Penalties could act as a deterrent and sharply reduce falsification. Also, the Revenue Department is currently attempting to identify flagrant violators.

Related Information:

Many taxpayers are claiming more exemptions than allowed on the annual return and in some cases the degree of falsification is large.

Legislative Proposal 18

A BILL TO BE ENTITLED AN ACT TO RAISE THE MINIMUM TAX THRESHOLD FOR FILING AN INTANGIBLES TAX RETURN.

The General Assembly of North Carolina enacts:

Section 1. The first sentence of G. S. 105-214 is amended by deleting the phrase "fifteen dollars ($15.00)" and inserting in lieu thereof the phrase "twenty dollars ($20.00)".

Sec. 2. This act is effective for taxable years beginning on and after January 1, 1982.

Explanation of Proposal 18

Under G. S. 105-214, a person who owes less than $15 intangibles tax on intangible assets other than money on deposit is not required to file a return. This bill raises the minimum tax threshold to $20. which means that a person who owns less than $8,000 worth of stocks, bonds and similar items would not have to file a return. Increasing the filing threshold to $20 would eliminate 11,000 returns and would reduce intangible tax collections by .5%. The threshold was increased from $5 to $15 by the 1979 General Assembly, Second Session.

Fiscal Report for Proposal

Number 18

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

The 1980 General Assembly raised the intangible tax filing threshold on non-deposit returns from $5 to $15 ($6,000 of stocks, bonds, etc.) Proposal 18 increases the threshold from $15 to $20 ($8,000 of tax base) effective January 1, 1982.

Fiscal Effect:

Would reduce intangibles tax revenue by $200,000 (.5% of total tax) and eliminate 11,000 returns (6.8% of total returns) for 1982-83.

Legislative Proposal 19

A BILL TO BE ENTITLED AN ACT TO RAISE THE TAXABLE THRESHOLD FOR MONEY ON DEPOSIT UNDER THE INTANGIBLE PERSONAL PROPERTY TAX.

The General Assembly of North Carolina enacts:

Section 1. The second paragraph of G.S. 105-199 is amended by deleting the phrase "one thousand dollars ($1,000)" and inserting in lieu thereof the phrase "one thousand five hundred dollars ($1,500)".

Sec. 2. This act is effective for taxable years beginning on and after January 1, 1982.

Explanation of Proposal 19

Money on deposit is taxed at the rate of 10¢ per $100 under the intangible personal property tax. Accounts with an average quarterly balance less than $1,000, however, are exempt from this tax. This bill increases the minimum taxable balance from $1,000 to $1,500. The minimum taxable balance was raised from $300 to $1,000 in 1979.

Fiscal Report for Proposal

Number 19

Fiscal Research Division
April 15, 1982

Explanation of Proposal:

The 1979 General Assembly increased the intangibles tax threshold on money on deposit from $300 to $1,000. This proposal would increase the threshold to $1,500 effective January 1, 1982.

Fiscal Effect:

Would reduce intangibles tax revenue by $600,000 for 1982-83.

Related Information:

The tax rate on money on deposits is 10¢ per $100 of the average balance for February 15, April 15, August 15, and November 15.

Legislative Proposal 20

A BILL TO BE ENTITLED AN ACT TO CLARIFY WHEN A CORPORATION MAY APPORTION PART OF ITS NET INCOME OR NET LOSS TO ANOTHER STATE.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-130.4(b) is amended by rewriting the second sentence of the subsection and by adding a sentence at the end of the subsection to read:

"For purposes of allocation and apportionment, a corporation is taxable in another state if (i) the corporation's business activity in that state subjects it to a net income tax or a tax measured by net income, or (ii) that state has jurisdiction based on the corporation's business activity in that state to subject the corporation to a tax measured by net income regardless whether that state exercises its jurisdiction. For purposes of this section, 'business activity' includes any activity by a corporation that would establish a taxable nexus pursuant to 15 United States Code §381."

Sec. 2. This act is effective upon ratification.

Explanation of Proposal 20

This bill adds a definition of business activity to G.S. 105-130.4(b) to clarify when a corporation may allocate

part of its income to another state, and, thus, pay North Carolina corporate income tax on only part of its income. The bill provides that a corporation may not allocate income to another state unless the corporation's business activity in that state is sufficient to establish a taxable nexus as defined in §381 of Title 15 of the United States Code. Section 381 provides that a state may not impose an income tax on a corporation if the corporation's only business activity in the state is soliciting orders for items that will be shipped to the customer from a point outside the state, unless the corporation is incorporated in that state. For example, a manufacturer located in North Carolina may not allocate part of its income to another state if its only business activity in that state is to solicit sales of the manufactured product.

Fiscal Report for Proposal

Number 20

Fiscal Research Division

May 12, 1982

Explanation of Proposal:

Clarifies corporate income tax law regarding cases when a corporation may allocate part of its income to another state for tax purposes. Generally, a corporation would not be allowed to make such an allocation if the only business activity in that other state is soliciting sales.

Fiscal Effect:

Insignificant.

Legislative Proposal 21

A BILL TO BE ENTITLED AN ACT TO INCREASE THE MINIMUM FRANCHISE TAX IMPOSED UPON CORPORATIONS.

The General Assembly of North Carolina enacts:

Section 1. The following statutes are amended by deleting the phrase "ten dollars ($10.00)" and inserting in lieu thereof the phrase "twenty-five dollars ($25.00)" each time it appears:

(1) G.S. 105-120.2(b)(1)

(2) G.S. 105-120.2(d)

(3) G.S. 105-122(d)

(4) G.S. 105-123(a)

Sec. 2. This act shall become effective January 1, 1983.

Explanation of Proposal 21

This bill increases the minimum corporate franchise tax from $10.00 per year to $25.00 per year. The minimum franchise tax has not been increased since at least 1923.

The franchise tax is a privilege tax on businesses. Although some franchise taxes, such as the taxes on express companies and telephone companies apply to individuals and partnerships as well as corporations, the taxes imposed by G.S. 105-120.2, 105.122

and 105-123 apply only to corporations. G.S. 105-120.2 applies to corporations that meet the definition of a holding company, 105-122 applies to all corporations that are not expressly excluded from the section, and 105-123 applies to new corporations.

Fiscal Report for Proposal

Number 21

Fiscal Research Division

May 12, 1982

Explanation of Proposal:

Increases minimum corporate franchise tax from $10.00 to $25.00, effective January 1, 1983.

Fiscal Effect:

Would increase General Fund tax revenue by $350,000-$400,000 for 1983-84.

Related Information:

(1) Minimum tax last increased from $5.00 to $10.00 in 1920. To adjust for inflation would bring the amount to $58.00.

(2) Approximately 20% of corporate taxpayers pay minimum tax.

Legislative Proposal 22

A BILL TO BE ENTITLED AN ACT TO CONFORM STATE LAW ON LEGISLATORS' INCOME TAX DEDUCTIONS FOR BUSINESS EXPENSES TO FEDERAL LAW.

The General Assembly of North Carolina enacts:

Section 1. G. S. 105-147(1) is amended by rewriting that part of the subsection preceding the colon to read:

"All the ordinary and necessary expenses paid during the income year in carrying on any trade or business to the extent allowed under the provisions of the Internal Revenue Code of 1954 as amended, except as otherwise provided, including".

Sec. 2. G.S. 105-147(1)c. is amended by deleting the phrase "to the extent allowable for federal income tax purposes under the provisions of section 175 of the Internal Revenue Code of 1954 as amended".

Sec. 3. G.S. 105-147(1)e. is amended by deleting the phrase "to the extent allowable under section 182 of the Internal Revenue Code of 1954 as amended".

Sec. 4. G.S. 105-147(1)g. is amended by adding a new sentence at the end to read:

"These expenses may be deducted regardless whether they are deductible for federal income tax purposes."

Sec. 5. G.S. 105-147(2) is amended by inserting between the words "individual," and "all" the phrase "to the

extent allowed under the provisions of the Internal Revenue Code of 1954 as amended".

Sec. 6. This act is effective for taxable years beginning on and after January 1, 1981.

Explanation of Proposal 22

This bill amends G.S. 105-147(1) and (2) to allow individuals to take the same business deductions on their state income tax return as on their federal income tax return. In particular, it allows state legislators the same living expense deduction as § 162 of the Internal Revenue Code.

The Economic Recovery Tax Act of 1981 amended § 162 of the Internal Revenue Code to allow legislators to deduct as living expenses an amount equal to the higher of the per diem rate for federal or state employees multiplied by the number of legislative days. The amendment defines legislative day as any day the legislature is in session, including days during the session when the legislature is in recess for four or fewer consecutive days, as well as any day the legislator's presence is formally recorded at a legislative committee meeting. The deduction allowed by this bill for state legislators is elective and, for taxable years beginning on or after January 1, 1981, is not available to legislators who live 50 or fewer miles from the capitol building.

Although the federal amendment is effective for taxable years beginning on or after January 1, 1976, this bill is effective only for taxable years beginning on or after January 1, 1981.

Fiscal Report for Proposal

Number 22

Fiscal Research Division

May 12, 1982

Explanation of Proposal:

The Economic Recovery Tax Act of 1981 amended the federal individual income tax law regarding state legislators' income and deductions reporting. The new law allows legislators to deduct as living expenses an amount equal to the higher of the per diem rate for federal or state employees (federal rate is $50.00) multiplied by the number of legislative days (would include days during the session when legislature is in recess for four or less consecutive days) as well as legislative committee meetings actually attended by the legislator. The deduction is not allowed for legislators living 50 or less miles from the Legislative Building.

The proposal is effective for income years beginning on or after January 1, 1981 and thus allows for the filing of amended returns for 1981.

Fiscal Effect:

Insignificant reduction in General Fund tax revenue.

Legislative Proposal 23

A BILL TO BE ENTITLED AN ACT TO PROVIDE AN INCOME TAX CREDIT FOR HEAT-PUMP WATER HEATERS.

The General Assembly of North Carolina enacts:

Section 1. Division I of Article 4 of Chapter 105 is amended by adding a new section to read:

"§105-130.34. Credit against corporate income tax for heat-pump water heater.--(a) Any corporation that constructs or installs a heat-pump water heater in a building located in North Carolina shall be allowed a credit against the taxes imposed by this Division equal to twenty-five percent (25%) of the installation and equipment costs of the heat-pump water heater. This credit may not exceed seven hundred fifty dollars ($750) per building or per family dwelling unit of a multi-dwelling building. To obtain the credit allowed by this section, the taxpayer must be liable for payment of the heat-pump water heater and must pay for the heat-pump water heater in the year for which the credit is claimed. This credit may not exceed the amount of tax imposed by this Division for the taxable year reduced by the sum of all credits allowable under this Division, except tax payments made by or on behalf of the taxpayer.

(b) As used in the section, 'heat-pump water heater' means an electric powered compression heating system that

uses air, gas, water or earth as a source of heat to assist in the production of hot water by a hot water heater."

Sec. 2. Division II of Article 4 of Chapter 105 is amended by adding a new section to read:

"§105-151.12. Credit against personal income tax for heat-pump water heater.--(a) Any person who constructs or installs a heat-pump water heater in a building located in North Carolina shall be allowed a credit against the taxes imposed by this Division equal to twenty-five percent (25%) of the installation and equipment costs of the heat-pump water heater. This credit may not exceed seven hundred fifty dollars ($750) per building or per family dwelling unit of a multi-dwelling building. To obtain the credit allowed by this section, the taxpayer must be liable for payment of the heat-pump water heater and must pay for the heat-pump water heater in the year for which the credit is claimed. This credit may not exceed the amount of tax imposed by this Division for the taxable year reduced by the sum of all credits allowable under this Division, except tax payments made by or on behalf of the taxpayer.

(b) As used in this section, 'heat-pump water heater' means an electric powered compression heating system that uses air, gas, water or earth as a source of heat to assist in the production of hot water by a hot water heater."

Sec. 3. This act is effective for taxable years beginning on and after January 1, 1982.

Explanation of Proposal 23

This bill provides both a corporate and an individual income tax credit for part of the purchase price and installation costsof a heat-pump water heater. The bill allows a corporation or individual to deduct 25% of the cost of the heat-pump water heater, up to a maximum of $750 per building or per family dwelling unit of a multi-dwelling building.

A heat-pump water heater attaches to an electric water heater and helps heat the water in the electric water heater by removing heat from the surrounding air and transferring it to the water. Thus, the heat-pump water heater, like a solar hot water heater, reduces the amount of electricity needed to heat water.

California, Hawaii and Oregon currently allow income tax credits for part of the purchase price and installation costs of a heat-pump water heater, and Florida exempts these heaters from sales tax and property tax.

Fiscal Report for Proposal

Number 23

Fiscal Research Division

May 12, 1982

Explanation of Proposal:

Allows a state corporate and individual income tax credit of 25% ($750 maximum per building) for the installation and equipment costs of a heat-pump water heater. The credit is limited to tax liability and there is no carry-forward provision. The proposal is effective beginning with the 1982 income year.

Fiscal Effect:

Would reduce General Fund tax revenue a maximum of $200,000 for 1982-83. There is no reliable data to develop an accurate estimate and if fuel prices stabilize the loss could be considerably less.

Related Information:

(1) Since 1977 there have been similar credits for active and passive solar equipment.

(2) The technology for the heat-pump water heaters was not in existence until 1979.

Legislative Proposal 24

A BILL TO BE ENTITLED AN ACT TO REPEAL THE PRIVILEGE LICENSE TAX ON COAL AND COKE DEALERS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-44 is repealed.

Sec. 2. This act shall become effective July 1, 1983.

Explanation of Proposal 24

This bill repeals the privilege license tax on coal and coke dealers. G.S. 105-44 imposes various privilege license taxes on persons engaged in the business of selling or delivering coal or coke. Wholesale dealers, who sell or deliver coal or coke in carload lots or greater quantities, must pay a license tax of $75.00; retail dealers must pay a tax of from $10.00 to $75.00 for each city or town in which they do business; peddlers, who sell coal in quantities of 100 pounds or less, must pay a $5.00 tax; and operators of vehicles coming into North Carolina from another state to deliver coal or coke must pay a tax of from $10.00 to $75.00 for each city or town in which deliveries are made.

Fiscal Report for Proposal

Number 24

Fiscal Research Division

May 7, 1982

Explanation of Proposal:

Repeals state privilege license tax on coal and coke dealers, effective July 1, 1983.

Fiscal Effect:

Would reduce General Fund tax revenue by $4,000 for 1983-84 and eliminate 215 licenses. Current average revenue per license is $19.

Related Information:

(1) Tax enacted in 1899.

(2) Number of dealers has declined substantially over last 20 years. In 1959-60 collections were $20,000.

(3) Repeal of tax will "free-up" Revenue Department staff time for the collection of higher-yield taxes.

(4) Repeal recommended by 1966 Tax Study Committee and 1982 Revenue Laws Study Committee.

(5) The 1979 and 1981 General Assembly repealed some low-yield privilege taxes and consolidated others.

Legislative Proposal 25

A BILL TO BE ENTITLED AN ACT TO REPEAL THE PRIVILEGE LICENSE TAX ON MERCHANTS WHO BUY OR SELL COMMODITIES ON COMMISSION.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-68 is repealed.

Sec. 2. This act shall become effective July 1, 1983.

Explanation of Proposal 25

This bill repeals the privilege license tax on cotton merchants and certain commodity buyers and sellers. G.S. 105-68 imposes a license tax of from $50.00 to $300 on cotton merchants, who are persons engaged in the business of selling more than 5,000 bales of cotton per year. The rate varies depending on the population of the city or town. Cotton merchants must pay this tax for each city or town in which they do business.

G.S. 105-68 also imposes a $50.00 license tax on persons engaged in the business of buying or selling commodities, such as cotton and grain, on commission. Commodity buyers and sellers who have a wire or ticker service must pay an additional tax of from $100 to $600 for each city or town in which they do business.

Fiscal Report for Proposal

Number 25

Fiscal Research Division

May 7, 1982

Explanation of Proposal:

Repeals state privilege license tax on cotton-brokers, effective July 1, 1983.

Fiscal Effect:

Would reduce General Fund tax revenue by $2,500 for 1983-84 and eliminate 30-35 licenses.

Related Information:

(1) Tax enacted in 1837.

(2) Collections have declined substantially from $5,800 in 1959-60.

(3) Repeal of tax will "free-up" Revenue Department staff time for the collection of higher-yield taxes.

(4) The Department of Agriculture has sufficient list of brokers for regulatory/information purposes.

(5) Repeal of tax recommended by 1966 Tax Study Committee and 1982 Revenue Laws Study Committee.

(6) The 1979 and 1981 General Assembly repealed some low-yield taxes and consolidated others,

Legislative Proposal 26

A BILL TO BE ENTITLED AN ACT TO REPEAL THE PRIVILEGE LICENSE TAX ON THOSE WHO ISSUE AND REDEEM TRADING STAMPS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-92 is repealed.

Sec. 2. This act shall become effective July 1, 1983.

Explanation of Proposal 26

This bill repeals the privilege license tax on persons who issue and redeem trading stamps. G.S. 105-92 imposes a $200.00 license tax on persons engaged in the business of issuing or selling trading stamps and subsequently redeeming these stamps. The tax does not apply to a merchant who gives trading stamps to a customer upon the purchase of goods sold by the merchant; it applies to the issuer and redeemer of the stamps, such as the S & H Green Stamp Company.

Fiscal Report for Proposal

Number 26

Fiscal Research Division

May 7, 1982

Explanation of Proposal:

Repeals state privilege license on trading-stamp redemption companies, effective July 1, 1983.

Fiscal Effect:

Would reduce General Fund tax revenue by $1,000 for 1983-84 and eliminate 5-10 licenses.

Related Information:

(1) Tax first enacted in 1903.

(2) Collections from this tax have declined substantially over last 20 years and it is possible that there will be no operators in a few years.

(3) Repeal of the tax will "free-up" Revenue Department staff time for the collection of higher-yield taxes.

(4) Repeal recommended by 1966 Tax Study Committee and 1982 Revenue Laws Study Committee.

(5) The 1979 and 1981 General Assembly repealed some privilege taxes and consolidated others.

Legislative Proposal 27

A BILL TO BE ENTITLED AN ACT TO REPEAL THE PRIVILEGE LICENSE TAX ON MANUFACTURERS AND SELLERS OF MONUMENTS AND GRAVESTONES.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-96 is repealed.

Sec. 2. This act shall become effective July 1, 1983.

Explanation of Proposal 27

This bill repeals the privilege license tax on persons engaged in the business of manufacturing, selling or erecting monuments or gravestones. G.S. 105-96 requires monument and gravestone manufacturers, sellers or erectors to pay a tax of from $15.00 to $75.00, depending on the population of the town or city, for each town or city in which they do business. The statute also imposes an additional tax of $10.00 for each salesman.

Fiscal Report for Proposal

Number 27

Fiscal Research Division

May 7, 1982

Explanation of Proposal:

Repeals state privilege license tax on marble yards, effective July 1, 1983.

Fiscal Effect:

Would reduce General Fund tax revenue by $10,500 for 1983-84 and eliminate 430 licenses. Current average revenue per license is $25.

Related Information:

(1) Tax enacted in 1927.

(2) Tax collections have grown at slow rate over last 30 years with 1959-60 collections at $6,400.

(3) Repeal of tax will "free-up" Revenue Department staff time for the collection of higher-yield taxes.

(4) Repeal recommended by 1966 Tax Study Committee and 1982 Revenue Laws Study Committee.

(5) The 1979 and 1981 General Assembly repealed some low-yeild privilege taxes and consolidated others.

Legislative Proposal 28

A BILL TO BE ENTITLED AN ACT TO REPEAL THE PRIVILEGE LICENSE TAX ON JUNK DEALERS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-102 is repealed.

Sec. 2. This act shall become effective July 1, 1983.

Explanation of Proposal 28

This bill repeals the privilege license tax on junk dealers. G.S. 105-102 imposes a license tax of from $25.00 to $125 on persons engaged in the business of buying or selling junk, such as scrap metal, glass, paper, cloth and cord, for each city or town in which they do business. The rate varies depending on the population of the city or town.

Fiscal Report for Proposal

Number 28

Fiscal Research Division

May 7, 1982

Explanation of Proposal:

Repeals state privilege license tax on junk dealers, effective July 1, 1983.

Fiscal Effect:

Would reduce General Fund tax revenue by $14,000 for 1983-84 and eliminate 302 licenses. Current average revenue per license is $44.

Related Information:

(1) Tax enacted in 1925.

(2) Collections from this tax have not changed over last 20 years.

(3) Solid Waste Division of Department of Human Resources has adequate list of junk dealers for regulatory/information purposes.

(4) Repeal of tax will "free-up" Revenue Department staff time for the collection of higher-yield taxes.

(5) Repeal recommended by 1966 Tax Study Committee and 1982 Revenue Laws Study Committee.

(6) The 1979 and 1981 General Assembly repealed some privilege taxes and consolidated others.

Legislative Proposal 29

A BILL TO BE ENTITLED AN ACT TO REPEAL THE PRIVILEGE LICENSE TAX ON SCRAP PROCESSORS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-102.2 is repealed.

Sec. 2. This act shall become effective July 1, 1983.

Explanation of Proposal 29

This bill repeals the privilege license tax on scrap processors. G.S. 105-102.2 imposes a license tax offrom $25.00 to $125 on persons engaged in the business of buying scrap iron and metals and processing these metals for reuse by steel mills, foundries, smelters and refineries. The rate varies depending on the population of the town or city. Scrap processors must pay the tax for each city or town in which they do business.

Fiscal Report for Proposal

Number 29

Fiscal Research Division

May 7, 1982

Explanation of Proposal:

Repeals state privilege license tax on scrap processors, effective July 1, 1983.

Fiscal Effect:

Would reduce General Fund tax revenue by $5,400 for 1983-84 and eliminate 51 licenses. Current average revenue per tax is $87.

Related Information:

(1) Tax enacted in 1965.

(2) Tax collections have not grown substantially since 1965-66 when collections were $3,650.

(3) The Solid Waste Division of the Department of Human Resources has an adequate list of processors for regulatory/information purposes.

(4) Repeal of tax will "free-up" Revenue Department staff time for the collection of higher-yield taxes.

(5) Repeal recommended by 1966 Tax Study Committee and 1982 Revenue Laws Study Committee.

(6) The 1979 and 1981 General Assembly repealed some low-yield privilege taxes and consolidated others.

Legislative Proposal 30

A BILL TO BE ENTITLED AN ACT TO CLARIFY WHAT CONSTITUTES AN ARTICLE FOR PREFERENTIAL SALES TAX TREATMENT AS EQUIPMENT USED IN THE PRODUCTION OF POULTRY PRODUCTS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-164.4(1)p. is rewritten to read:

"p. Sales to farmers of bulk feed handling equipment used to raise, feed or produce livestock or poultry products, including cages used in the production of these products. The sale of the total number of poultry cages to be served by the same automatic feeder, automatic waterer or automatic egg collector constitutes the sale of a single article that is separate and distinct from a feeder, waterer or egg collector."

Sec. 2. This act shall become effective July 1, 1982.

Explanation of Proposal 30

This bill clarifies the partial sales tax exemption for poultry cages under G.S. 105-164.4(1)p. G. S. 105-164.4(1)p. provides that all cages used in the production of livestock and poultry products shall be taxed at the rate of one percent instead of the general sales tax rate of three percent and sets the maximum tax for these items at $80.00. This $80.00 maximum applies to each article.

A problem has arisen in applying the "per article" standard to poultry cages. Numerous cages are commonly grouped together and served by the same automatic waterer, feeder or egg collector. The question arises whether the $80.00 maximum applies to each cage in the group or to the group as a whole. This bill makes clear that the $80.00 maximum applies to groups of cages that are to be served by the same automatic system, rather than each cage in the group.

The $80.00 maximum applies to the total number of cages that are to be served by the same system. Thus, if a poultry producer purchases less than the total number of cages to be served by an automatic feeder, waterer or egg collector, the $80.00 maximum applies to each cage purchased.

Fiscal Report for Proposal

Number 30

Fiscal Research Division

May 13, 1982

Explanation of Proposal:

Since the 1950's certain classes of agricultural items have either been exempt from the sales and use tax or subject to a 1% tax, with an $80.00 limit of tax per article. The 1979 General Assembly amended the law of items to include poultry cages. However, the law is unclear as to the definition of "article" and the technical characteristics and separate delivery system for the various components of poultry houses has led the Department of Revenue to conclude that each cage in a row of cages served by one feeding, watering and egg collecting system is a separate article. Thus, the $80.00 limit applies to each cage instead of the whole row of cages.

The proposal would clarify the law by stating that all cages connected by the same feeding, watering, and egg collecting devices would be considered a single article. The proposal would become effective July 1, 1982.

Fiscal Effect:

Would reduce General Fund tax revenue by $30,000 for 1982-83.

Legislative Proposal 31

A BILL TO BE ENTITLED AN ACT TO EQUALIZE THE RATE OF INTEREST ON TAX REFUNDS AND TAX ASSESSMENTS, AND TO SET THE RATE OF INTEREST ON TAX REFUNDS AND TAX ASSESSMENTS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-163.16(c) is amended by deleting the phrase "of six percent (6%) per annum" in the fourth sentence of the subsection and substituting the phrase "established in G.S. 105-141.1(i) for assessments" in lieu thereof.

Sec. 2. G.S. 105-266 is amended by deleting the phrase "of six percent (6%) per annum" in the first sentence of the section and substituting the phrase "established in G.S. 105-141.1(i) for assessments" in lieu thereof.

Sec. 3. G.S. 105-163.9(a) is amended by deleting the phrase "of six percent (6%) per annum" in that subsection and substituting the phrase "established in G.S. 105-241.1(i) for assessments" in lieu thereof.

Sec. 4. G.S. 105-241.1(i) is amended by rewriting the first paragraph of the subsection to read:

"All assessments of taxes or additional taxes, exclusive of penalties assessed thereon, shall bear interest from the time the taxes or additional taxes were due until paid. The rate of interest is twelve percent (12%) per annum, computed

at one percent (1%) per month or fraction thereof, or the rate established by the Secretary of Revenue as follows: the Secretary may, not later than December 1 of any year, declare the adjusted rate that will be in effect on January 1 of the succeeding calendar year under the provisions of the Internal Revenue Code to be the rate that will be in effect during the succeeding calendar year, or the Secretary may set the rate to be in effect during the succeeding calendar year at nine (9%) per annum, computed at three-fourths percent (3/4%) per month or fraction thereof."

Section 5. This act shall become effective July 1, 1982 and shall apply to refunds and assessments made on and after that date.

Explanation of Proposal 31

This bill affects the interest rate on tax refunds and assessments in two ways. First, it conforms the interest rate paid by the State on refunds of overpayments of tax to the rate paid by taxpayers on underpayments of tax. Currently, the rate on refunds is six percent, and the rate on underpayments is nine percent.

Secondly, the bill changes the method by which the interest rate on tax refunds and assessments is determined. The bill

provides that the rate will be twelve percent per year unless the Secretary of Revenue sets it at a different rate. The Secretary may set the rate at nine percent per year or may choose to follow the federal rate. If the Secretary decides to set the rate at nine percent or at the federal rate, he must do so no later than December 1. Otherwise, the rate for the following calendar year will be twelve percent. Currently the rate is nine percent per year unless the Secretary decides to follow the federal rate.

Fiscal Report for Proposal

Number 31

Fiscal Research Division

May 13, 1982

Explanation of Proposal:

Presently, the interest rate charged on late payments of state taxes is either the federal rate or 9% (at the discretion of the Secretary of Revenue). The rate for tax refunds is a flat 6%. The proposal would change the mechanism for establishing the state rate for both tax refunds and late payments. Under the mechanism the Secretary of Revenue, by December 1, would establish the rate for the upcoming year. The Secretary could first decide whether to use a 12% rate or not; in the absence of choosing 12%, the Secretary may choose either the federal rate or 9%. The proposal would be effective for refunds and assessments made on and after July 1, 1982.

Fiscal Effect:

For 1982-83 the Revenue Department estimates a net increase in General Fund tax revenue of $1.3 million, based on $1.5 million more interest on late payments to the State and $.2 million more interest on refunds to taxpayers.

Related Information:

(1) The current formula allows the Secretary of the Treasury to establish a rate once a year to become effective February 1

for the next 12 month period. The federal formula has a number of deficiencies:

(a) it is based on the average rate for one month in the past (September 15) and not a long-run average of recent rates.

(b) it uses the "prime" rate as a measure of market rates.

(c) it allows Treasury Secretary no options in situations where formula rate is vastly different from current rates.

The federal rate for 1982 is 20%. There is a proposal before Congress to modify some of the problems with the current federal formula. However, it is doubtful that the federal change will take place before late 1982.

(2) The estimated revenue effect occurs for the July 1 - December 31, 1982 period based on the assumption that the Secretary of Revenue will use the 12% option on late payments (currently 9%) and 12% on refunds currently 6%). It is impossible to predict the effect on revenue for the remainder of 1982-83 and future years.

Legislative Proposal 32

A BILL TO BE ENTITLED AN ACT TO SUPPLEMENT THE GOVERNING INSTRUMENTS OF CERTAIN NONEXEMPT CHARITABLE TRUSTS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 36A-54 is amended by redesignating subsections (b) and (c) as subsections (c) and (d) respectively, and by inserting a new subsection (b) to read:

"(b) Notwithstanding any provisions in the laws of this State or in the governing instrument to the contrary, unless otherwise decreed by a court of competent jurisdiction except as provided in subsection (c), the governing instrument of each trust that is a nonexempt charitable trust described in section 4947(a)(1) of the Code shall be deemed to contain the following provisions:

(1) The trust shall be operated exclusively for charitable, educational, religious and scientific purposes within the meaning of section 501(c)(3) and section 170(c)(2) of the Code.

(2) Upon any dissolution, winding up, or liquidation of the trust, its assets shall be distributed for one or more exempt purposes within the meaning of section 501(c)(3) of the Code, or shall be distributed to the Federal government, or a state or local government for a public purpose."

Sec. 2. The first sentence of G.S. 36A-54(a) is amended by deleting the phrase "subsection (b)" and inserting in lieu thereof the phrase "subsection (c)".

Sec. 3. G.S. 36A-54(b) is amended by deleting the phrase "subsection (a)" each time it appears and inserting in lieu thereof the phrase "subsections (a) or (b)".

Sec. 4. This act is effective upon ratification.

Explanation of Proposal 32

This bill amends G.S. 36A-54 to incorporate certain requirements of federal income tax law into the governing instruments of trusts created prior to 1970 that are organized and operated exclusively for tax exempt, charitable purposes. The amendment will facilitate the receipt of favorable Internal Revenue Service tax rulings concerning the exempt status of these trusts.

Prior to the effective date of the Tax Reform Act of 1969, charitable organizations, including trusts, that, in their own view, met the requirements of the federal income tax laws with regard to tax exemption, filed their federal income tax returns accordingly as organizations that were exempt from tax. It was not required that they obtain from the Internal Revenue Service a ruling or determination letter to the effect that they were in fact exempt.

The Tax Reform Act of 1969 and the Regulations issued under its provisions made two important changes in this respect. First, a newly created organization that desires to be treated as tax exempt must apply to the IRS and obtain a determination letter to the effect that it is exempt. Secondly, two particular requirements for exemption must not only be complied with in fact, but they must also be expressly stated in the organization's governing instrument. The requirements are:

(1) That the purposes of the organization are limited to one or more exempt purposes, and the organization is not empowered to engage in activities that in themselves are not in furtherance of one or more exempt purposes, otherwise than as an insubstantial part of its activities. Treas. Reg. §1.501(c)(3)-1(b); and

(2) That upon dissolution and liquidation of the organization any remaining assets will be distributed exclusively for one or more exempt purposes. Treas. Reg. §1.501(c)(3)-1(b)(4).

Charitable trusts that have not had a determination made by the IRS on their exempt status are referred to as nonexempt charitable trusts, and a question arises whether income paid out by them for charitable and exempt purposes is fully deductible by them for income tax purposes or is deductible only within the

percentage limitations that apply to individuals and corporations with respect to charitable contributions, with the result that part of their income would be subject to income tax.

This bill incorporates the required provisions into the governing instruments of these nonexempt charitable trusts. The trust can then obtain a favorable determination letter from the IRS and will not have to amend its governing instrument by bringing a State court civil action, which is prohibitively expensive in many cases.

Fiscal Report for Proposal

Number 32

Fiscal Research Division

May 12, 1982

Explanation of Proposal:

Amends state law regarding trusts in order that the organization can obtain a determination from the IRS that it meets federal requirements for income tax exemption. The effect of the change will be to allow a few taxpayers in North Carolina to take advantage of favorable federal income tax treatment. The proposal would become effective upon ratification.

Fiscal Effect:

No effect on North Carolina income tax liability.

Legislative Proposal 33

A BILL TO BE ENTITLED AN ACT TO PROVIDE FOR ADMINISTRATION OF CHARITABLE REMAINDER TRUSTS.

The General Assembly of North Carolina enacts:

Section 1. Chapter 36A of the General Statutes is amended by adding a new Article to read:

"ARTICLE 4A

Charitable Remainder Trusts Administration Act

§36A-55. Short Title.--This Article shall be known as the Charitable Remainder Trusts Administration Act.

§36A-56. General rule.--Notwithstanding any provisions in the laws of this State or in the governing instruments to the contrary, any charitable remainder annuity trust and any charitable remainder unitrust that cannot qualify for a deduction for federal tax purposes under §2055 or §2522 of the Code in the absence of this Article shall be administered in accordance with this Article.

§36A-57. Definitions.--The following definitions apply to this Article unless the context clearly requires otherwise. (1) 'Charitable remainder trust' means a trust that provides for a specified distribution at least annually for either life or a term of years to one or more beneficiaries, at least one of which is not a charity, (hereinafter referred to as "beneficiaries") with an

irrevocable remainder interest to be held for the benefit of, or paid over to, charity. For purposes of this Article, only a charitable remainder annuity trust or a charitable remainder unitrust is considered a charitable remainder trust.

(2) 'Charitable remainder annuity turst' means a charitable remainder trust:

a. from which a sum certain (which is not less than five percent (5%) of the initial net fair market value of all property placed in trust) is to be paid at least annually to one or more persons (at least one of which is not an organization described in §170(c) of the Code and, in the case of individuals, only to an individual who was living at the time of the creation of the trust) for a term of years (not in excess of twenty years) or for the life or lives of such individual or individuals;

b. from which no amount other than the payments described in a. above may be paid to or for the use of anyone other than an organization that is or was described in §170(c) of the Code; and

c. following the termination of the payments described in a. above, the remainder interest in

the trust is to be transferred to, or for the use of, an organization that is or was described in §170(c) of the Code or is to be retained by the trust for such a use.

(3) 'Charitable remainder unitrust' means a charitable remainder trust:

a. from which a fixed percentage (which is not less than five percent (5%)) of the net fair market value of its assets, valued annually, is to be paid at least annually to one or more persons (at least one of which is not an organization described in §170(c) of the Code and, in the case of individuals, only to an individual who was living at the time of the creation of the trust) for a term of years (not in excess of twenty years) or for the life or lives of such individual or individuals;

b. from which no amount other than the payments described in a. above may be paid to or for the use of anyone other than an organization that is or was an organization described in §170(c) of the Code; and

c. following the termination of the payments described in a. above, the remainder interest in the trust is to be transferred to, or for the use of, an organization that is or was described in §170(c)

of the Code, or is to be retained by the trust for such a use.

Notwithstanding the provisions of a. and b. above, the trust instrument may provide that the trustee shall pay to the income beneficiary for any year (i) the amount of the trust income if that amount is less than the amount required to be distributed under a. above, and (ii) any amount of the trust income that exceeds the amount required to be distributed under a. above to the extent that (by reason of a.) the aggregate of the amounts paid in prior years is less than the aggregate of the required amounts.

(4) 'Code' means the Internal Revenue Code of 1954 as amended.

§36A-58. Administrative provisions applicable to both charitable remainder annuity trusts and charitable remainder unitrusts. --(a) Creation of remainder interest in charity.--Upon the termination of the noncharitable interest, the trustee shall distribute all of the then principal and income of the trust, other than any amount due the noncharitable beneficiary or beneficiaries, to the designated charity or charities, or shall hold the property in trust for the designated charity or charities in accordance with the terms of the trust document.

(b) Selection of alternate charitable beneficiary if remaindermen do not qualify under §170(c) at time of distribution.--If the designated charity is not an organization described in §170(c) of the Code when any principal or income of the trust is to be distributed to it, the trustee shall distribute the principal or income to one or more organizations then described in §170(c) of the Code selected in accordance with the terms of the trust instrument. If the trust instrument does not provide for a method of selecting alternate charitable beneficiaries that are then qualified under §170(c) of the Code, the trustee shall, in his sole discretion, select alternate trust beneficiaries that are qualified under §170(c) of the Code.

(c) Prohibitions governing trustees.--Except for payment of the annuity amount or the unitrust amount to the beneficiaries, the trustee is prohibited from engaging in any act of self-dealing as defined in §4941(d) of the Code, retaining any excess business holdings as defined in §4943(c) of the Code that would subject the trust to tax under §4943 of the Code, making any investments that would subject the trust to tax under §4944 of the Code, and making any taxable expenditures as defined in §4945(d) of the Code. The trustee shall make distributions at

such time and in such manner as not to subject the trust to tax under §4942 of the Code.

(d) Distribution to charity during term of noncharitable interest and distributions in kind.--If the governing instrument of the trust provides for distribution to charity during the term of the noncharitable interests, the trustee may pay to the designated charity the amounts specified in the governing instrument that exceed the annuity amount or the unitrust amount payable to any of the beneficiaries for the taxable year of the trust in which the income is earned. If the governing instrument of the trust provides for distribution to charity in kind, the adjusted basis for federal income tax purposes of any trust property the trustee distributes in kind to charity during the term of the noncharitable interests must be fairly representative of the adjusted basis for such purposes of all trust property available for distribution on the date of distribution.

(e) Investment restrictions on trustee.--Nothing in the trust instrument shall be construed to restrict the trustee from investing the trust assets in a manner that could result in the annual realization of a reasonable amount of income or gain from the sale or disposition of trust assets.

(f) Distribution from trust used to administer an estate to charitable remainder trust.--If the governing instrument of a revocable inter vivos trust provides that the revocable inter vivos trust will be used partially to administer the estate of the grantor or for some other purpose, and then the assets will be distributed to a charitable remainder trust, upon the death of the grantor, or the occurrence of any event that causes the trust to become irrevocable, the trust shall become irrevocable and the trustee of this trust shall perform any remaining duties or obligations provided for in the trust instrument and then transfer the property specified in the governing instrument to the trustee of the charitable remainder trust to be held, administered and distributed in the manner and according to the terms and conditions provided by the charitable remainder trust.

§36A-59. Administrative provisions applicable to charitable remainder annuity trusts only.--(a) Creation of annuity amount for period of years or life.--The trustee shall pay the annuity amount designated in the trust instrument to the beneficiaries named in the instrument during their lives (or if the governing instrument so provides, for a period of 20 years or less) in each taxable year of the trust. The annuity amount shall be paid annually or in

more frequent equal or unequal installments if the governing instrument so provides. The annuity amount shall be paid from income, and, to the extent that income is not sufficient, from principal. Any income of the trust for a taxable year in excess of the annuity amount shall be added to principal.

The total amount payable at least annually to a person or persons named in the trust document, at least one of which is not an organization described in §170(c) of the Code, may not be less than five percent (5%) of the initial net fair market value of the property placed in trust as finally determined for federal tax purposes, except as provided in subsection (g).

(b) Computation of annuity amount in short and final taxable years.--For a short taxable year and for the taxable year in which the noncharitable beneficiary's interest terminates by death or otherwise, the trustee shall prorate the annuity amount on a daily basis.

(c) Prohibition of additional contributions.--No additional contributions shall be made to the trust after the initial contribution.

(d) Deferral of annuity amount during period of administration or settlement.--When property passes to the trust at the death of the grantor, the obligation to pay the annuity amount commences with the date of

death of the grantor, but payment of the annuity amount may be deferred from the date of the grantor's death to the end of the taxable year in which complete funding of the trust occurs. Payment of the annuity amount so deferred, plus interest computed at six percent (6%) a year, compounded annually, shall be made within a reasonable time after the close of the taxable year in which complete funding occurs.

(e) Dollar amount annuity may be stated as fraction or percentage.--If the governing instrument of the trust states the amount of the annuity as a fraction or a percentage, the trustee shall pay to the beneficiaries in each taxable year of the trust during their lives an annuity amount equal to a percentage (that percentage being stipulated in the governing instrument of the trust and, in any event, being five percent (5%) or greater) of the initial net fair market value of the assets constituting the trust. In determining this amount, assets shall be valued at their values as finally determined for federal tax purposes. If the fiduciary incorrectly determines the initial net fair market value of the assets constituting the trust, then, within a reasonable period after a final determination, the trustee shall pay to the beneficiaries in the case of an undervaluation or shall receive from the beneficiaries in the case of an overvaluation an amount equal to the difference between the annuity amount properly payable and the annuity amount actually paid.

(f) Annuity amount may be allocated among class of noncharitable beneficiaries in discretion of trustee. --If the governing instrument of the trust provides that the annuity trust amount may be allocated among a class of noncharitable beneficiaries in the discretion of the trustee, then the trustee shall pay the annuity amount, which is defined in the governing instrument of the trust, in each taxable year of the trust to the member or members of the class of noncharitable beneficiaries in such amount and proportions as the trustee in its absolute discretion shall from time to time determine until the last of the noncharitable beneficiaries dies. The trustee may pay the entire annuity amount to one member of this class or may apportion it among the various members in such manner as the trustee shall from time to time deem advisable as long as the allocation does not cause any person to be treated as the owner of any part of the trust under the rules of §§671 through 678 of the Code. If the class provided for in the governing instrument is open, then the distribution shall be for a period of years not to exceed twenty, notwithstanding a provision to the contrary in the trust instrument. If the class provided for in the governing instrument is closed at the creation of the trust, and all members of the class are ascertainable, the distribution may be for the lives of the members

of the class or for a period not exceeding twenty years. The trustee shall pay the entire annuity amount for each taxable year annually and may not delay payment of the annuity amount.

(g) Reduction of annuity amount if part of corpus is paid to charity at expiration of term of years or on death of recipient.--If the governing instrument of the trust provides for the reduction of the annuity amount if part of the corpus is paid to charity at the expiration of a term of years or upon the death of a recipient, then during the term of years or during the joint lives of the noncharitable beneficiaries, the trustee shall, in each taxable year of the trust, pay a total annuity amount of at least five percent (5%) of the initial net fair market value of the assets placed in trust. Upon the expiration of the term of years or the death of a beneficiary, the trustee shall distribute an amount or percentage of the trust assets, as provided in the governing instrument of the trust, to the charity named in the governing instrument, and thereafter, the trustee shall pay, annually or in more frequent installments, to the survivors for their lives, an annuity amount that in each taxable year of the trust, bears the same ratio to five percent (5%) of the initial net fair market value of the trust assets as the fair market value of the trust assets valued as of the date of distribu-

tion, less the amount or percentage of trust assets distributed to the charity, bears to the fair market value of the trust assets as of the date of distribution.

(h) Termination of annuity amount on payment date preceding termination of noncharitable interest.--If the governing instrument of the trust provides that payment of the annuity amount may terminate with the regular payment preceding the termination of all noncharitable interests, then the trustee shall pay to the noncharitable beneficiary during the term of the noncharitable interest the annuity amount, defined in the trust document, in each taxable year of the trust. The obligation of the trustee to pay the annuity amount shall terminate with the payment preceding the death of the noncharitable beneficiary or other event that terminates the noncharitable interest.

(i) Retention of testamentary power to revoke noncharitable interest.--The grantor may have the power, exercisable only by his will, to revoke and terminate the interest of the noncharitable beneficiary under the trust. If the governing instrument of the trust provides that the grantor of the trust shall retain the power,

exercisable only by will, to revoke or terminate the interest of any recipient other than an organization described in §170(c) of the Code, then the trustee shall pay to the grantor during his life the annuity amount, as defined in the governing instrument of the trust, and, upon the death of the grantor, if the noncharitable beneficiary survives the grantor the trustee shall pay to the noncharitable beneficiary during his life the annuity amount equal to the amount paid to the grantor. Upon the first to occur of (i) the death of the survivor of the grantor and noncharitable beneficiary or (ii) the death of the grantor if he effectively exercised his testamentary power to revoke and terminate the interest of the noncharitable beneficiary, the trustee shall distribute all of the then principal and income of the trust, other than any amount due the grantor or noncharitable beneficiary, to the charity named in the trust document or, if the governing instrument so provides, the trustee shall continue to hold the principal and income in trust for the charity or for the charitable purposes specified in the trust. No other retained power to terminate an interest in the trust shall be effective.

§36A-59.1. Administrative provisions applicable to charitable remainder unitrusts only.--(a) Creation of unitrust

amount for a period of years or life.--The trustee shall pay to the beneficiaries named in the trust instrument in each taxable year of the trust during their lives, or, if the governing instrument so provides, for a period not exceeding 20 years, a unitrust amount equal to a fixed percentage, as stated in the governing instrument of the trust, of the net fair market value of the trust assets valued annually on the date or by the method designated in the governing instrument of the trust or, if no date or method is specified, on the date or by the method selected by the trustee in his discretion, so long as the same valuation date or dates or valuation methods are used each year. The unitrust amount shall be paid annually or in more frequent equal or unequal installments if the governing instrument so provides. The unitrust amount shall be paid from income, and, to the extent that income is not sufficient, from principal. Any income of the trust for a taxable year in excess of the unitrust amount shall be added to principal.

The fixed percentage to be paid at least annually to all beneficiaries cannot be less than five percent (5%).

(b) Unitrust amount expressed as the lesser of income or a fixed percentage.--If the governing instrument of the trust provides that the trustee shall pay, instead of a regular unitrust amount (the fixed percentage of the net

fair market value of the trust assets, determined annually), the amount of trust income for the taxable year to the extent that this amount is not greater than the amount required to be distributed as a regular unitrust amount for that taxable year and/or the amount of the trust income for the taxable year that exceeds the regular unitrust amount for that taxable year to the extent that the aggregate of the amounts paid in prior years is less than the aggregate of the regular unitrust amount for those prior years, then the trustee shall pay to the beneficiaries in each taxable year of the trust during their lives, or for a period not exceeding twenty years if the trust agreement so provides, an amount equal to the lesser of (i) the trust income for the taxable year, as defined in §643(b) of the Code and the regulations thereunder, and (ii) the percentage, as stated in the governing instrument, of the net fair market value of the trust assets valued as of the taxable year decreased as appropriate if the taxable year is a short taxable year or is the taxable year in which the noncharitable interest terminates by death or otherwise, and increased as appropriate if additional contributions are made in the taxable year.

If the governing instrument of the trust so provides and if the trust income for any taxable year exceeds the amount determined under (ii) above, the payment to

beneficiaries shall also include the excess income to the extent that the aggregate of the amounts paid to beneficiaries in prior years is less than the percentage of the aggregate net fair market value of the trust assets, which percentage is defined in the governing instrument of the trust, for these years. Payments to beneficiaries shall be made annually or in more frequent equal or unequal installments if the governing instrument so provides. Any income of the trust in excess of payments shall be added to principal.

(c) Adjustment for incorrect valuation.--If the fiduciary incorrectly determines the net fair market value of the trust assets for any taxable year, the trustee shall, within a reasonable period after the final determination of the correct value, pay to the beneficiaries in the case of an undervaluation or receive from the beneficiaries in the case of an overvaluation an amount equal to the difference between the unitrust amount payable and the unitrust amount actually paid.

(d) Computation of unitrust amount in short and final taxable years.--For a short taxable year and for the taxable year in which the noncharitable beneficiary's interest terminates by death or otherwise, the trustee shall prorate the unitrust amount on a daily basis. If

a trust provides for a valuation date other than the first day of the taxable year, and the valuation date does not occur in a taxable year of the trust because the taxable year is either a short taxable year or is the taxable year in which the noncharitable interests terminate, the trust assets shall be valued as of the last day of the short taxable year or the day on which the noncharitable interests terminate, as appropriate.

(e) Additional contributions.-If the governing instrument does not prohibit additional contributions and additional contributions are made to the trust after the initial contribution in the trust, the unitrust amount for the taxable year in which the additional contributions are made shall be a fixed percentage, as stated in the governing instrument of the trust, of the sum of (i) the net fair market value of trust assets, excluding the additional contributions and any income from or appreciation of these contributions and (ii) that proportion of the value of the additional contributions excluded under (i) which the number of days in the period beginning with the date of contribution and ending with the earlier of the last day of the taxable year or the day the noncharitable beneficiary's interest terminated bears to the number of days in the period beginning on the first day of the taxable year and ending with the earlier of

of the last day in the taxable year or the day the noncharitable beneficiary's interest terminated. If no valuation date occurs after the contributions are made, the assets so added shall be valued as of the time of contribution.

(f) Deferral of unitrust amount during period of administration or settlement.--When property passes to the trust at the death of the grantor, the obligation to pay the unitrust amount commences with the date of the grantor's death, but payment of the unitrust amount may be deferred from the date of the grantor's death to the end of the taxable year of the trust in which complete funding of the trust occurs. Within a reasonable time after the occurrence of this event, the trustee shall pay the amount determined under the method described in Treasury Regulation §1.664-1(a)(5)(ii) less the sum of any amounts previously distributed, including interest paid on the amounts distributed computed at six percent (6%) a year, compounded annually, from the date of distribution to the occurrence of this event.

(g) Unitrust amount may be allocated among class of noncharitable beneficiaries in discretion of trustee.--If the governing instrument of the trust provides that the unitrust amount may be allocated to a class of non-

charitable beneficiaries in the discretion of the trustee, then the trustee shall pay, in each taxable year of the trust, the unitrust amount to the member or members of the class of noncharitable beneficiaries in such amounts and proportions as the trustee in its absolute discretion shall from time to time determine until the last of the noncharitable beneficiaries dies. The trustee may pay the unitrust amount to any one member of the class or may apportion it among the various members in such manner as the trustee shall from time to time deem advisable as long as the allocation does not cause any person to be treated as the owner of any part of the trust under the rules of §§671 through 678 of the Code. If the class provided for in the governing instrument is open, the distribution shall be for a period not exceeding twenty years, notwithstanding a provision to the contrary in the trust instrument. If the class provided for in the governing instrument is closed at the creation of the trust, and all members of the class are ascertainable, the distribution may be for the lives of the members of the class or for a period not exceeding twenty years. The trustee shall pay the entire unitrust amount for each taxable year annually and may not delay payment of the unitrust amount.

(h) Reduction of unitrust amount if part of corpus is paid to charity at expiration of term of years or on

death of a recipient.--If the governing instrument of the trust provides for the reduction of the unitrust amount if part of the corpus is paid to charity at the expiration of a term of years or upon the death of a recipient, then during the term of years or during the joint lives of the noncharitable beneficiaries the trustee shall, in each taxable year of the trust, pay the total unitrust amount equal to a percentage of the net fair market value of the trust assets valued annually, which shall not be less than five percent (5%). Upon expiration of the term of years or the death of a recipient, the trustee shall distribute an amount or percentage of the trust assets, as provided in the governing instrument of the trust, to the charity named in the governing instrument, and thereafter the trustee shall pay to the survivors for their lives a unitrust amount in each taxable year of the trust equal to at least five percent (the actual percentage being defined in the trust instrument) of the net fair market value of the remaining trust assets valued annually.

(i) Termination of unitrust amount on payment date preceding termination of noncharitable interests.--If the governing instrument of the trust provides that payment of the unitrust amount may terminate with the regular payment preceding the termination of all noncharitable

interests, then the trustee shall pay the unitrust amount to the noncharitable beneficiary in each taxable year of the trust during the term of the noncharitable interest. The obligation of the trustee to pay the unitrust amount terminates with the payment preceding the termination of the noncharitable interest by death or otherwise. The five percent (5%) requirement provided in subsection (a) shall be met until the termination of all payments of the unitrust amount.

(j) Retention of testamentary power to revoke noncharitable interest.--If the governing instrument of the trust provides that the grantor of the trust shall retain the power, exercisable only by will, to revoke or terminate the interest of any recipient other than an organization described in §170(c) of the Code, then the trustee shall pay the unitrust amount to the grantor during his life and, upon the death of the grantor, shall pay the unitrust amount to the noncharitable beneficiary during his life provided the noncharitable beneficiary survives the grantor. Upon the first to occur of (i) the death of the survivor of the grantor and the noncharitable beneficiary and(ii) the death of the grantor if he effectively exercised his testamentary power to revoke and terminate the interest of the noncharitable beneficiary, the trustee shall distribute all of the then principal and income of the trust, other than any amount

due the noncharitable beneficiaries, to the charity named in the trust document or, if the governing instrument so provides, the trustee shall continue to hold the principal and income in trust for the charity or for the charitable purposes specified in the trust. No other retained power to terminate an interest in the trust shall be effective.

§36A-59.2. Interpretation.--This Article shall be construed to effectuate its general purpose to cause all charitable remainder annuity trusts and all charitable remainder unitrusts to be administered in accordance with the provisions of §2055 and §2522 of the Code and the regulations thereunder."

Sec. 2. This act is effective upon ratification and applies to all charitable remainder annuity trusts and all charitable remainder unitrusts that would not qualify for the deduction pursuant to §2055 or §2522 of the Code in the absence of this Article that are in existence on that date or are established after that date. For trusts in existence on that date, this act relates back to the date of creation of the trust.

Explanation of Proposal 33

This bill ensures that certain charitable remainder interests in property held in trust are exempt from federal estate and gift

tax by requiring these trusts to be administered in accordance with the provisions of the Internal Revenue Code and the Treasury Regulations. Section 2055 of the Code provides that the value of a charitable remainder interest in property may not be deducted from the value of the estate before determining federal estate tax unless the interest is held in either a charitable remainder annuity trust or a charitable remainder unitrust. Similarly, Section 2522 of the Code provides that a gift of a charitable remainder interest in property will be taxable unless the interest is held in either a charitable remainder annuity trust or a charitable remainder unitrust.

These trusts are defined in §664 of the Code. Briefly, a charitable remainder annuity trust is a trust that pays a stated amount, equal to at least five percent of the initial net fair market value of the trust assets, to a noncharitable beneficiary over a period of years and then distributes the remainder of the property to a charity; and a charitable remainder unitrust is a trust that pays a fixed percentage, but no less than five percent, of the annual market value of the trust assets to a noncharitable beneficiary for a period of years and then distributes the remainder of the property to a charity.

Although §664 defines 'charitable remainder annuity trust' and 'charitable remainder unitrust,' it does not contain all the requirements these trusts must meet to exempt the charitable

remainder interests from federal estate and gift tax. The regulations promulgated under various Code sections impose numerous additional requirements. This bill imposes those same requirements on these trusts, thereby enabling them to qualify for the estate and gift tax exemption.

Until January 1, 1982, federal law allowed these trusts to bring a civil action to conform the governing instruments to the requirements of federal law. This action is no longer available, however.

Fiscal Report for Proposal

Number 33

Fiscal Research Division

May 12, 1982

Explanation of Proposal:

In 1969 the Congress enacted tax legislation that attempted to tighten up the charitable giving sections of the estate and gift tax law to prevent any possible abuses. The 1969 Act set out some complex requirements that must be met to allow for a deduction under the federal estate tax law for the establishment of a charitable remainder annuity trust or a charitable remainder unitrust. The 1969 Act as well as the numerous IRS regulations and revenue rulings since that time are somewhat difficult to understand and thus are deterring some giving due to the inability to predict whether the dedution would be allowed.

The proposed bill would amend the charitable trusts section of Chapter 36A of the North Carolina statutes by establishing a set of state provisions that would govern the establishment of such trusts in accordance with the IRS regulations and rulings handed down since 1969.

Fiscal Effect:

The legislation would affect only a handful of North Carolina situations. The North Carolina inheritance tax law does not

use the federal scheme for the classification of such gifts. The effect on North Carolina inheritance tax revenues and tax administration will be very minor, if there is any effect at all.

Legislative Proposal 34

A BILL TO BE ENTITLED AN ACT TO EXEMPT ALL TWO-AXLE CARRIERS FROM THE HIGHWAY USE TAX AND TO CLARIFY WHICH CARRIERS ARE SUBJECT TO THE HIGHWAY USE TAX.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-449.37 is rewritten to read:

"§105-449.37. Definitions; tax liability.--(a) The following definitions apply to this Article unless the context clearly requires otherwise:

(1) 'Motor carrier' means every person, firm or corporation who operates or causes to be operated on any highway in this State a passenger vehicle with seating capacity for more than twenty passengers, a road tractor, a tractor truck, or a truck having more than two axles. The term does not include the United States, the State or its political subdivisions, operators of special mobile equipment as defined in G.S. 20-4.01(44), or non-profit religious, educational, charitable or benevolent organizations.

(2) 'Operations' means operations of all vehicles described in subdivision (1), whether loaded or empty and whether or not operated for compensation.

(3) 'Secretary' means the Secretary of Revenue.

(b) A motor carrier who operates on one or more days of a quarter is liable for the tax imposed by this Article for that quarter and is entitled to the credits allowed for that quarter."

Sec. 2. This act shall become effective January 1, 1983.

Explanation of Proposal 34

This bill will be introduced only if the South Carolina legislature enacts legislation before the close of the June session to exempt all two-axle vehicles from South Carolina's highway use tax. The bill exempts all two-axle vehicles from North Carolina's highway use tax imposed by Article 36B of Chapter 105. G.S. 105-449.37 currently exempts only two-axle vehicles that are not operated for compensation.

Because two-axle private vehicles are exempt from North Carolina's highway use tax, these vehicles do not report their highway mileage to the Department of Revenue and, thus, cannot obtain a refund of the per gallon tax if they purchase more fuel in North Carolina than they use in driving on North Carolina roads. South Carolina, however, now imposes a highway use tax on two-axle diesel vehicles. Thus, two-axle diesel vehicles not operated for compensation may pay both a per gallon tax to North Carolina and a highway use tax to South Carolina on the same fuel.

If South Carolina enacts legislation to exempt all two-axle vehicles, two-axle vehicles operated for compensation that purchase fuel in South Carolina, but use some of the fuel driving on North Carolina highways will pay a per gallon tax to South Carolina and a highway use tax to North Carolina on the same fuel. This bill eliminates the double taxation problem that will be created if South Carolina exempts all two-axle vehicles from its use tax. A double taxation problem exists now for two-axle diesel vehicles operated for compensation that purchase fuel in North Carolina but use the fuel to drive on South Carolina roads. This problem can be corrected only by appropriate legislation in South Carolina or by requiring all two-axle diesel vehicles to pay the North Carolina highway use tax.

A bill to exempt all two-axle vehicles from South Carolina's highway use tax has been introduced in the South Carolina legislature and has passed the Senate.

The bill also clarifies that governmental units, non-profit organizations and operators of special mobile equipment, such as vehicles with permanently attached cranes, operated on the highway only for the purpose of getting from one job to another are not subject to the highway use tax.

Fiscal Report for Proposal

Number 34

Fiscal Research Division

May 13, 1982

Explanation of Proposal:

Many operators of two-axle private trucks purchase fuel in North Carolina for use on a trip that may take them out of North Carolina. As in most states, these trucks are exempt from North Carolina's highway use tax and thus do not report highway mileage to the Department of Revenue or receive a tax refund for the motor fuel tax purchased for use in another state. In South Carolina a use tax would be charged on the fuel purchased in North Carolina but used in South Carolina. No credit is allowed in South Carolina for the taxes paid to North Carolina for fuel used in South Carolina. Thus, the operator of a private two-axle vehicle pays taxes to both states for two reasons:

(a) The operator is exempt from the North Carolina use tax (and thus cannot file a report to obtain a per gallonage tax refund), but is not exempt from South Carolina's use tax; and

(b) South Carolina does not allow a use tax credit for fuel purchased in North Carolina.

South Carolina, like North Carolina, is one of the few states that does not exempt all two-axle trucks from its highway use tax. There is a bill in the South Carolina legislature that has passed one house. If that legislation is enacted the double taxation issue

would be resolved in respect to South Carolina because the South Carolina law would be in conformity with the practice of most states.

This proposal will be introduced only if the South Carolina law is ratified. Like the proposed South Carolina law, this bill exempts all two-axle vehicles from the highway use tax. Currently, North Carolina exempts only trucks not operated for compensation.

Fiscal Effect:

Negligible effect on Highway Fund tax revenue.

Appendix A

Legislative Research Commission

Committee on Revenue Laws

1981-1983

Rep. Daniel T. Lilley
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Kinston, North Carolina 28501
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Sen. Marshall A. Rauch
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Sen. T. Cass Ballenger
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Rep. Bertha "B" Holt
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Sen. James M. Clarke
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Rep. Robert A. (Bob) Jones
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Rep. John M. Jordan
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Mr. Michael C. Warren
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Rep. Charles M. Beall ( Replaced Jones)
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LRC Member responsible for Study: Senator Robert W. Wynne

Staff: Sabra J. Faires, Legislative Services Office, Bill Drafting Div.
Jim Blackburn, Legislative Services Office, General Research Div.
Dave Crotts, Legislative Services Office, Fiscal Research Div.
Ada B. Edwards, Committee Clerk

# GENERAL ASSEMBLY OF NORTH CAROLINA
# SESSION 1981
# RATIFIED BILL

RESOLUTION 61

HOUSE JOINT RESOLUTION 1292

A JOINT RESOLUTION AUTHORIZING STUDIES BY THE LEGISLATIVE RESEARCH COMMISSION.

Be it resolved by the House of Representatives, the Senate concurring:

Section 1. The Legislative Research Commission may study the topics listed below. Listed with each topic is the 1981 bill or resolution that originally proposed the study and the name of the sponsor. The Commission may consider the original bill or resolution in determining the nature, scope and aspects of the study. The topics are:

(1) Continuation of study of revenue laws (H.J.R. 15 -- Lilley).

(2) Continuation of study on problems of aging (H.J.R. 48 -- Messer/S.J.R. 37 -- Gray).

(3) Day care (H.J.R. 223 -- Brennan).

(4) Civil rights compliance of non-State institutions receiving State funds (H.J.R. 344 -- Spaulding).

(5) Social services and public assistance (H.B. 393 -- P. Hunt).

(6) The need for new health occupational licensing boards (H.B. 477 -- Lancaster/S.B. 285 -- Jenkins).

(7) Matters related to public education, including:

a. The feasibility of making the 12th grade optional in the public schools (H.J.R. 890 -- Tally).

b. Continue study of public school food service (H.J.R. 948 -- Brennan).

c. The teacher tenure law (S.J.R. 621 -- Royall).

d. Providing teachers with duty-free periods (S.J.R. 697 -- Speed).

e. Continuation of study regarding purchase of buses in lieu of contract transportation, and other school bus transportation matters (no 1981 resolution).

(8) Campaign financing and reporting (H.J.R. 975 -- D. Clark).

(9) State's interests in railroad companies and railroad operations (H.B. 1069 -- J. Hunt).

(10) Matters related to insurance, including:

a. Insurance regulation (H.B. 1071 as amended -- Seymour), including the feasibility of establishing within the Department of Insurance a risk and rate equity board.

b. How the State should cover risks of liability for personal injury and property damage (H.J.R. 1198 -- Seymour).

c. Credit insurance (H.J.R. 1328 -- Barnes).

(11) Matters related to public property, including:

a. Development of a policy on State office building construction (H.J.R. 1090 -- Nye).

b. The potential uses and benefits of arbitration to resolve disputes under State construction and procurement contracts (H.J.R. 1292 -- Adams).

c. The bonding requirements on small contractors bidding on governmental projects (H.J.R. 1301 -- Nye).

d. Continue study of the design, construction and inspection of public facilities (S.J.R. 143 -- Clarke).

e. Whether the leasing of State land should be by competitive bidding (S.J.R. 178 -- Swain).

(12) Allocation formula for State funding of public library systems (H.J.R. 1166 -- Burnley).

(13) Economic, social and legal problems and needs of women (H.R. 1238 -- Adams).

(14) Beverage container regulation (H.J.R. 1298 -- Diamont).

(15) Scientific and technical training equipment needs in institutions of higher education (H.J.R. 1314 -- Fulcher).

(16) Role of the State with respect to migrant farmworkers (H.J.R. 1315 -- Fulcher).

(17) Existing State and local programs for the inspection of milk and milk products (H.J.R. 1353 -- James).

(18) Laws authorizing towing, removing or storage of motor vehicles (H.J.R. 1360 -- Lancaster).

(19) Annexation laws (S.J.R. 4 -- Lawing).

(20) Laws concerning obscenity (House Committee Substitute for S.B. 295).

(21) The feasibility of consolidating the State computer systems (S.J.R. 349 -- Alford/H.J.R. 524 -- Plyler).

(22) Laws pertaining to the taxation of alcoholic beverages and the designation of revenues for alcoholism

education, rehabilitation and research (S.J.R. 497 -- Gray).

(23) Regional offices operated by State agencies (S.J.R. 519 -- Noble).

(24) Continue study of laws of evidence (S.J.R. 698 -- Barnes).

(25) Continue study of ownership of land in North Carolina by aliens and alien corporations (S.J.R. 714 -- White).

(26) Rules and regulations pertaining to the Coastal Area Management Act (S.J.R. 724 -- Daniels).

(27) Transfer of Forestry and Soil and Water from Department of Natural Resources and Community Development to Department of Agriculture (H.B. 1237 -- Taylor).

(28) Continue sports arena study (H.J.R. 1334 -- Barbee).

(29) State investment and maximum earning productivity of all public funds (H.J.R. 1375 -- Beard).

Sec. 2. For each of the topics the Legislative Research Commission decides to study, the Commission may report its findings, together with any recommended legislation, to the 1982 Session of the General Assembly or to the 1983 General Assembly, or the Commission may make an interim report to the 1982 Session and a final report to the 1983 General Assembly.

Sec. 3. The Legislative Research Commission or any study committee thereof, in the discharge of its study of insurance regulation under Section 1(10)a. of this act, may secure information and data under the provisions of G.S. 120-19. The powers contained in the provisions of G.S. 120-19.1 through

G.S. 120-19.4 shall apply to the proceedings of the Commission or any study committee thereof in the discharge of said study. The Commission or any study committee thereof, while in the discharge of said study, is authorized to hold executive sessions in accordance with G.S. 143-318.11(b) as though it were a committee of the General Assembly.

Sec. 4. This resolution is effective upon ratification.

In the General Assembly read three times and ratified, this the 10th day of July, 1981.

JAMES C. GREEN

James C. Green

President of the Senate

LISTON B. RAMSEY

Liston B. Ramsey

Speaker of the House of Representatives

# GENERAL ASSEMBLY OF NORTH CAROLINA
## SESSION 1981

H

I

HOUSE JOINT RESOLUTION 15

Sponsors: Representative Lilley; and Bertha Holt.

Referred to: Finance.

January 16, 1981

A JOINT RESOLUTION DIRECTING THE LEGISLATIVE RESEARCH COMMISSION TO CONTINUE TO STUDY THE REVENUE LAWS OF THE STATE OF NORTH CAROLINA.

Whereas, the Legislative Research Commission was directed by the 1977 General Assembly in ratified Resolution 85 to conduct a study of the revenue laws of North Carolina; and was directed by the 1979 General Assembly in ratified Resolution 83 to continue that study; and

Whereas, pursuant to Resolution 83 a Committee on Revenue Laws was appointed and held 11 meetings before reporting its recommendations to the Legislative Research Commission and the 1980 and 1981 General Assemblies; and

Whereas, the Committee on Revenue Laws reviewed many areas of the revenue laws and prepared 35 legislative proposals to modernize, improve, and delete obsolete sections from the revenue laws; and

Whereas, the scope of the subject matter assigned to the Committee on Revenue Laws was so broad that not all areas could

be addressed within the time and budget limits placed on the Committee; and

Whereas, in the course of its deliberations the Committee on Revenue Laws discovered several matters which warranted further investigation; and

Whereas, changes in federal tax laws often make review of related State laws advisable; and

Whereas, the Committee on Revenue Laws has proved to be an excellent forum to which both taxpayers and State officials can turn with problems and complaints about the revenue laws; Now, therefore, be it resolved by the House of Representatives, the Senate concurring:

Section 1. The Legislative Research Commission shall continue to study the revenue laws and their administration in North Carolina.

Sec. 2. The commission shall continue to review the revenue laws of the State of North Carolina to determine which laws need clarification, technical amendment, repeal, or other change to make the revenue laws as concise, intelligible, administratively responsive, and efficient as is reasonably practicable. Where the recommendations of the Commission, if enacted, would result in an increase or decrease in State tax revenues, the final report of the Commission shall include an estimate of the amount of such increase or decrease.

Sec. 3. The Commission may call upon the Department of Revenue to cooperate with it in its study, and the Secretary of Revenue shall insure that its employees and staff provide full

and timely assistance to the Commission in the performance of its duties.

Sec. 4. The Commission shall produce a final report with its recommendations for improvement of the revenue laws to the 1983 General Assembly and may produce an interim report to the 1981 General Assembly, Second Session 1982.

Sec. 5. This resolution is effective upon ratification.

Appendix C

## Persons Appearing Before the Committee

| Name | Group Represented or Subject of Presentation |
|---|---|
| Mark Baldwin<br>Southern Conservation Systems of Raleigh<br>Raleigh, North Carolina 27604 | Energy Tax Credit for Heat-Pump Water Heater |
| R. E. Beck<br>Director<br>Gasoline Tax Division<br>Department of Revenue | |
| B. W. Brown<br>Director<br>Individual Income Tax Division<br>Department of Revenue | |
| Paul Creech<br>Kirby, Wallace, Creech, Sarda & Zaytoun<br>P. O. Box 2477<br>Raleigh, North Carolina 27602 | Sales Tax on Poultry Cages |
| George Davis<br>Assistant Director<br>Individual Income Tax Division<br>Department of Revenue | |
| Linwood Davis<br>P. O. Drawer 84<br>Winston-Salem, North Carolina 27102 | Nonexempt Charitable Trusts |
| David Dowdy<br>Rite Aid Corporation<br>P. O. Box 5484<br>High Point, North Carolina 27262 | Privilege License Taxes |

| | |
|---|---|
| Claude Farrell | American Association of Retired People and the National Retired Teachers Association |
| Joseph F. Kelley<br>Fayetteville<br>North Carolina | North Carolina Senior Citizens Association |
| Richard Levis<br>Whispering Pines<br>North Carolina | Committee for Repeal of the Intangibles Tax |
| Mark Lynch<br>Secretary<br>Department of Revenue | |
| Gary McGrath<br>3000 Falstaff Road<br>Raleigh, North Carolina 27610 | Wake County Alcoholism Treatment Center |
| W. B. Matthews<br>Director<br>Corporate Income and Franchise Tax Div.<br>Department of Revenue | |
| George Robinson<br>Director<br>Inheritance and Gift Tax Division<br>Department of Revenue | |
| Larry Rogers<br>Director<br>License and Excise Tax Division<br>Department of Revenue | |
| Samuel Siegel<br>Charlotte, North Carolina | Inheritance and Gift Tax |

Tom Sinks
Tuggle, Duggins, Meschan, Thornton & Elrod, P.A.
P. O. Drawer X
Greensboro, North Carolina 27402-0190

Charitable Remainder Trust Administration

John Wallace
Kirby, Wallace, Creech, Sarda & Zaytoun
P. O. Box 2477
Raleigh, North Carolina 27602

James B. Hunt, Jr.
Governor

State of North Carolina
Department of Revenue
P. O. Box 25000
Raleigh, N. C. 27640

Mark G. Lynch
Secretary

James P. Senter
Deputy Secretary

December 16, 1981

MEMORANDUM

TO: David F. Crotts
Fiscal Analyst
Legislative Services Office

FROM: Mark G. Lynch
Secretary of Revenue

RE: Economic Recovery Tax Act of 1981

In compliance with your request of December 1, 1981, we are attaching hereto the effect of the Economic Recovery Tax Act of 1981 as it relates to our income tax laws, corporate and individual.

In compiling our response we used as our guide the article "Reagan Tax Plan Ready for Economic Test" appearing in the August 8, 1981 Congressional Quarterly publication, a copy of which is also attached. Due to our Revenue Laws containing separate divisions for individual and corporate income tax purposes, we have prepared a response as to the effect of the Economic Recovery Tax Act to each schedule rather than combining the two schedules.

Because of the difference in our inheritance and gift tax laws with the federal estate and gift tax laws, the changes incorporated in the Economic Recovery Tax Act will not be automatically reflected in either of these schedules.

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Encs.

ECONOMIC RECOVERY TAX ACT OF 1981

AND

EFFECT ON STATE INDIVIDUAL INCOME TAX LAWS

Depreciation. Our law allows a deduction for depreciation based on the allowance for federal purposes. The Economic Recovery Tax Act of 1981 provides new federal depreciation rules for property placed in service after 1980 called "accelerated cost recovery system" (ACRS).

Basically under ACRS all depreciable property is put into one of four categories having useful lives of 3, 5, 10, or 15 years.

We will follow these depreciation rules for State income tax purposes; however, we will be unable to follow the federal law which allows individuals an election to expense certain depreciable business assets placed in service after 1981. Unless the Legislature changes State law, this election will not be available for State income tax purposes because of G.S. 105-148(2) which denies the deduction of any amount paid out for new buildings or for permanent improvements or betterments, made to increase the value of any property or estate.

Individual Retirement Account Contributions. For tax years beginning after 1981 we will follow the new federal law with respect to the amounts allowed for contributions to IRAs, self-employed retirement plans, and simplified employee pension plans. The deduction for contributions to IRAs will be allowed to the extent of the smallest of the following amounts: (1) $2,000, (2) 100 percent of the individual's includible compensation, or (3) amount contributed. Contributions to spousal IRAs will be allowed as a deduction to the extent of the lesser of the following: (1) $2,250, (2) 100 percent of the individual's includible compensation; except that the individual may not contribute more than $2,000 to either the taxpayer's IRA account or the spouse's account. Contributions to self-employed retirement plans and simplified employee pension plans will be allowed as deductions for the lesser of 15 percent of the individual's net earnings from self-employment or $15,000. Individuals who are active participants in a qualified employer plan or government plan will be permitted to establish IRAs and deduct contributions. Voluntary contributions by an employee to a qualified employer retirement plan may qualify as deductions under certain conditions.

Exclusion on Sale of Residence up to $100,000 for Individuals Over Age 55. The 1979 General Assembly enacted legislation adopting the federal exclusion up to $100,000 on the sales of principal residences by individuals over age 55. For federal income tax purposes, the exclusion has been increased to $125,000. Unless the Legislature changes State law, we will be unable to follow this increase since our law specifically limits the exclusion to $100,000.

Replacement Period for Principal Residence. A gain on the sale of a principal residence may be postponed if a new residence is purchased within 18 months or within 2 years if a new one is constructed by the taxpayer. These periods were the same for federal and State income tax purposes. Federal law has been changed so that the period for reinvesting is 2 years whether the new residence is purchased or constructed. Our law specifically provides for the 18 month and 2 year periods, and we will be unable to follow the change in federal law unless the law is changed by the Legislature.

All-Savers Certificates. A change in federal law allows individuals to exclude up to $1,000 ($2,000 on a joint return) of interest received on special savings certificates issued after September 30, 1981, and before January 1, 1983. These certificates are referred to as "all-savers" certificates and are available in denominations of $500 and is a one-year certificate that has an interest yield that is equal to 70 percent of the average investment yield for the most recent auction of United States treasury bills with maturities of 52 weeks. Unless the law is changed, there will be no provision in our law to exempt the interest on these "all-savers" certificates; however, if the certificates evidence savings in banks, credit unions, or savings and loan associations located in North Carolina, the interest will be subject to the $200 interest exclusion of G.S. 105-141(b)(28).

Public Utility Dividends. A new provision of federal law allows an individual to exclude up to $750 per year ($1,500 on a joint return) from income of a dividend on a public utility's stock which he elects under the utility's reinvestment plan to receive in common stock rather than in cash or other property. There is no provision in our law in this respect; therefore, we will be unable to follow this provision of federal law unless there is a law change.

Foreign Income Exclusion and Excess Foreign Living Costs. Our law was like federal law in respect to the exclusion of income earned abroad by individuals living in certain camps set up by employers in remote areas and in respect to the deduction of excess living costs by individuals living abroad. Federal law has been changed effective for years after 1981 so that the excess foreign living expense deduction has been eliminated and the foreign income exclusion has been extended to individuals living abroad even though they are not living in the certain camps. Legislative action to change the law will be necessary if we follow the federal law and allow the exclusion to individuals living abroad although they do not live in the certain camps.

Retirement Plan Distributions. Under both our law and federal law, employees have been taxed on amounts from qualified retirement plans when the amounts are distributed or made available to the employee. The "made available" rule has been deleted from federal law for tax years beginning on and after January 1, 1982. Legislative action to change State law will be necessary if we continue to follow the federal law in this respect.

State Legislators' Expenses. Federal law has been changed retroactive for taxable years beginning on or after January 1, 1976, so that instead of claiming his actual away from home expenses a legislator may elect to treat his residence within the legislative district he represents as his tax home and be deemed to have expended for living expenses an amount equal to the greater of the daily per diem allowed federal employees (currently $50), or the State daily per diem, but not over 110 percent of the federal per diem for each day the legislature is in session including up to four consecutive days when the legislature is not in session. He may also count a day the legislature wasn't in session if his presence was recorded at a legislative committee meeting. For taxable years beginning after 1980, legislators whose place of residence is 50 miles or less from the State capital may not elect to have the new rules apply to them. We will follow the federal procedure under current State law. (After further study the Dept. decided that legislation was needed for state law to follow federal on this issue.)

Indexing. Federal law has been changed to increase the individual income tax brackets, the zero bracket amount, and the personal exemption to reflect annual increases in the Consumer Price Index beginning with the 1985 tax year. State law has no provision for indexing and any provision in this respect for State individual income tax purposes will require the enactment of the provision by the Legislature.

Marriage Deductions. Under the new federal law two-earner married couples filing joint returns, beginning in 1982, are allowed to deduct 5% of up to $30,000 (a maximum deduction of $1,500) of the lesser of their two incomes. The deduction will increase to 10% (a maximum of $3,000) in 1983 and after. State law does not allow the filing of joint returns and this provision is not applicable for State individual income tax purposes.

Child Care Tax Credit. For federal income tax purposes, the child care tax credit is increased from 20 percent to 30 percent of the employment related expenses for individuals earning $10,000 or less beginning in 1982. The credit will be reduced one percentage point for each $2,000 in additional income up to $28,000. Those earning over $28,000 will be eligible for a 20 percent credit. The amount of expenses eligible for the credit are increased from $2,000 to $2,400 for one dependent and from $4,000 to $4,800 for two or more dependents. For State income tax purposes, the allowable credit is 7 percent of the qualified expenses for in the household services up to $4,000 and for outside of the household services up to $2,000 for one dependent and up to $4,000 expenses for two or more dependents and has an overall maximum on expenses of $4,000. For State income tax purposes, there is no reduction in the credit percentage because of the amount of the individual's income. Unless State law is changed, we will continue to allow the tax credit under the provisions of current law.

Charitable Contributions for Non-Itemizers. For federal tax purposes, beginning with the 1982 tax year, individual income taxpayers who do not itemize their personal deductions, will be permitted to deduct a portion of their charitable contributions even though they claim the standard deduction. This special deduction for non-itemizers will

terminate after 1986. State law does not allow a deduction for charitable contributions unless the taxpayer itemizes his personal deductions, and a law change would be required if we were to follow federal law in this respect.

Dividend and Interest Exclusion. The federal interest and dividend exclusion of $200 ($400 on a joint return) has been changed to a $100 ($200 on a joint return) exclusion for dividend income only. State law allows an interest exclusion up to $200 of interest received from savings deposits in banks, credit unions, and savings and loan associations located in North Carolina and allows a nonbusiness deduction for a percentage of dividends received from corporations which pay taxes to North Carolina on their net earnings. Law changes will be necessary if the federal dividend exclusion is allowed for State income tax purposes.

Adoption Expenses. For federal tax purposes, beginning with the 1981 tax year, individual income taxpayers are allowed to deduct up to $1,500 for expenses of adopting a "child with special needs." State law contains no provision for an individual income tax deduction for adoption expenses and cannot be allowed unless State law is changed.

Fringe Benefit Regulations. Federal law has been amended so that no regulations or rulings altering the tax treatment of fringe benefits may be issued in final form on or before December 31, 1983, or with an effective date before January 1, 1984. We are currently following most federal fringe benefit provisions that are now in effect.

Estimated Income Tax. For federal tax purposes, beginning with the 1982 tax year, the $100 estimated tax liability threshold for filing individual declarations of estimated tax will be raised, in stages to $500 in 1985 and thereafter. Under State law this threshold is set at $40. Any change for State individual income tax purposes in this respect will require action by the Legislature.

Net Interest Exclusion. For tax years beginning after 1984, a new federal interest exclusion for net interest (interest income after reduction for interest deductions other than business and home mortgage interest deductions) is allowed but cannot exceed 15 percent of the lesser of:

(1) $3,000 ($6,000 on a joint return), or
(2) the taxpayer's net interest for the year.

State law has no provision in this respect; and if the exclusion is allowed for State income tax purposes, a law change will be necessary.

ECONOMIC RECOVERY TAX ACT OF 1981

Effect on State Corporation Income Tax Laws

The following Federal changes will automatically apply for State tax purposes:

Business Tax Cuts

Accelerated Depreciation

The Accelerated Cost Recovery System (ACRS) has been adopted for North Carolina corporate income tax purposes with the same effective date as for Federal purposes.

Small Business Depreciation

The deduction permitted for Federal tax purposes for the cost of new or used machinery and equipment will be permitted for State purposes in the amounts and for the years established by the Economic Recovery Tax Act of 1981.

Leasing

The liberalized leasing provision will apply for State tax purposes to the extent that depreciation allowances are involved.

Rehabilitation of Old Buildings

Allowance of more rapid depreciation will be the only effect for State tax purpose for buildings constructed on the site of a demolished historic structure.

Effective January 1, 1982

Small Business Accounting

The last in, first out (LIFO) method of accounting applicable to specified small businesses will be followed for State purposes with the same effective date as for Federal purpose.

Trucking Licenses

The deduction for loss in value of operating rights (licenses) over a 60-month period is permitted for the same periods as allowed for Federal purposes.

Gifts to Employees - New Limit $400

The allowable deduction for an employee award given for length of service, productivity or safety achievments is increased to $400.

The following changes would require legislative action before becoming effective:

Research and Development

The increased deduction for corporate contributions of new equipment to a college or university to be used for research cannot be allowed until G. S. 105-130.3 is updated.

Foreign Research

An update of G. S. 105-130.3 will be necessary to follow this provision.

Rehabilitation of Old Buildings

The Federal provision requires a reduction in the depreciable base for the amount of investment tax credit allowable. For North Carolina purposes the basis reduction cannot be followed. Legislation would have to be enacted to either allow the credit as a tax reduction or as an additional expense before the depreciable base would be the same for Federal and State purposes.

The Federal effective date is January 1, 1982.

The following changes will have no effect on State taxes as enacted:

1. Changes relating to Federal investment tax credit:

   Used property increased basis
   Credit carryover extended
   Leasing
   Rehabilitation of old buildings
   Research and development

2. Accumulated earnings

3. Shareholder size

4. Corporate rate reductions