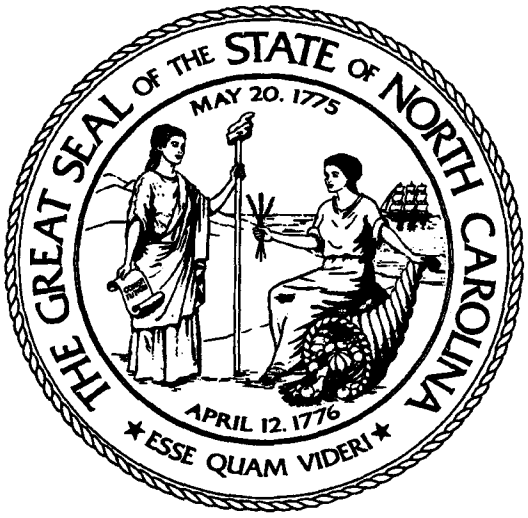
LEGISLATIVE

RESEARCH COMMISSION

REVENUE LAWS



REPORT TO THE
1995 GENERAL ASSEMBLY
OF NORTH CAROLINA

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STATE OF NORTH CAROLINA

LEGISLATIVE RESEARCH COMMISSION

STATE LEGISLATIVE BUILDING

RALEIGH 27611

January 11, 1995

TO THE MEMBERS OF THE 1995 GENERAL ASSEMBLY:

The Legislative Research Commission submits to you for your consideration its report on revenue laws. The report was prepared by the Legislative Research Commission's Committee on Revenue Laws pursuant to G.S. 120-30.17(1).

Respectfully submitted,

Daniel T. Blue, Jr.
Speaker of the House

Marc Basnight
President Prop Tempore

Cochairs
Legislative Research Commission

1993 - 1994

LEGISLATIVE RESEARCH COMMISSION

MEMBERSHIP

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Senator Frank W. Ballance, Jr.	Rep. Marie W. Colton
Senator R. L. Martin	Rep. W. Pete Cunningham
Senator J. K. Sherron, Jr.	Rep. Bertha M. Holt
Senator Lura S. Tally	Rep. Vernon G. James

PREFACE

The Legislative Research Commission, established 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 of Representatives and the President Pro Tempore of the Senate and has five additional members 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 investigations into governmental agencies and institutions and matters of public policy as will aid the General Assembly in performing its duties in the most efficient and effective manner." (G.S. 120-30.17(1)).

The Legislative Research Commission has undertaken studies of numerous subjects, to be carried out during the period between the adjournment of the 1993 Regular Session of the 1993 General Assembly and the convening of the 1995 General Assembly. These studies were grouped into broad categories and each member of the Commission was given responsibility for one category of study. The Cochairs of the Legislative Research Commission, under the authority of G.S. 120-30.10(b) and (c), appointed committees consisting of members of the General Assembly and the public to conduct the studies. Cochairs, one from each house of the General Assembly, were designated for each committee.

The study of the revenue laws would have been authorized by Sections 2.1(9) and 2.1(88) of House Bill 1319 (2nd Edition), which passed both the House of Representatives and the Senate in 1993 but was not ratified because of a procedural problem. The Legislative Research Commission authorized the study of the revenue laws in 1993 pursuant to its authority under G.S. 120-30.17(1) and grouped the study in its Budget and Revenue area under the direction of Senator R.L. Martin. House Bill 1319 was later amended and ratified in 1994. However, the language in House Bill 1319 (2nd Edition) referring to the Legislative Research Commission studies was deleted because the Legislative Research Commission had already acted on these matters.

Sections 2.1(9) and 2.1(88) of House Bill 1319 (2nd Edition) stated that the Commission may consider House Joint Resolution 123 and Senate Joint Resolution 1167 in determining the nature, scope, and aspects of the study. House Joint Resolution 123, introduced by Representative Mary L. Jarrell in the 1993 Session, gives the Legislative Research Commission's study of the revenue laws a very broad scope,

stating that the "Commission may review the State's revenue laws to determine which laws need clarification, technical amendment, repeal, or other change to make the laws concise, intelligible, easy to administer, and equitable." Senate Joint Resolution 1167, introduced by Senator Frank W. Ballance, Jr. in the 1993 Session, provides for the study of the current system for allocation of the clear proceeds of fines and forfeitures. The relevant portions of House Bill 1319 (2nd Edition), House Joint Resolution 123, and Senate Joint Resolution 1167 are included in Appendix A. The Revenue Laws Study Committee is chaired by Senator Dennis J. Winner and Representative Mary L. Jarrell. The full membership of the Committee and the staff assigned to the Committee are listed in Appendix B of this report.

COMMITTEE PROCEEDINGS

The Legislative Research Commission's Revenue Laws Study Committee met twice before the 1994 Session. The Committee recommended five bills in the interim report to the 1994 Session of the 1993 General Assembly. All five of these recommendations were enacted in 1994, although some were modified before enactment. Appendix D lists the recommendations and the action taken on them during the 1994 Session.

The Committee held four meetings after the 1994 Session, including a two-day meeting in November. The Committee was inundated with requests from legislators, taxpayers, the Department of Revenue, and interest groups to study numerous issues of tax policy and tax administration. Although the Committee met often and for some length, it was unable to take up all of the issues suggested to it, including the issue of fines and forfeitures.

The Committee investigated and adopted many proposals to give tax relief. These recommendations are reflected in Legislative Proposals 1, 4, 5, 8, 9, and 12. Legislative Proposal 1 gives inheritance tax relief to every class of beneficiary. Legislative Proposal 12 lowers the minimum highway use tax from $40 to $20. The Committee has recommended this proposal to each General Assembly since the highway use tax was enacted in 1989.

Legislative Proposal 4 gives additional franchise tax relief to holding companies by amending the definition of holding company to provide that a minor one-year fluctuation in income does not disqualify a company as a holding company. The Committee used this opportunity to not only broaden the definition of holding company but also adjust the $75,000 maximum tax imposed on holding companies whose taxable base is determined by their capital stock, surplus, and undivided profits.

Legislative Proposal 5 gives broad income tax relief to corporations. It lowers the corporate income tax rate and establishes a graduated income tax rate for corporations ranging from 5% to 7%. Legislative Proposals 8 and 9 provide sales and use tax relief to certain businesses. Legislative Proposal 8 exempts from sales and use tax property manufactured or purchased for resale by a wholesale merchant or a retailer and then withdrawn from inventory and donated to a nonprofit organization to be used for

charitable purposes. Legislative Proposal 9 exempts from sales and use tax free samples of prescription drugs distributed by the manufacturer.

The Committee, as well as interested parties, spent a considerable amount of time studying whether or not to give property tax relief to businesses by limiting local governments' ability to tax construction in progress. The Committee decided not to take any action on this issue.

The Committee investigated many proposals recommended by the Department of Revenue and others to improve tax administration. The most significant recommendation in this area is Legislative Proposal 13, which changes the point of taxation for gasoline and diesel fuel to the terminal rack. The purpose of this proposal is to remove opportunities to evade taxes and to establish a system that can be more easily administered. North Carolina is particularly vulnerable to motor fuel tax evasion because its motor fuel tax rate is 22¢ a gallon compared to 16¢ a gallon in South Carolina and 7.5¢ a gallon in Georgia. The proposal is expected to generate an additional $28 million a year in revenues without increasing the motor fuel tax rates. The Committee's staff solicited input in developing this proposal from the North Carolina Service Station Association, the North Carolina Association of Convenience Stores, the North Carolina Petroleum Marketers' Association, the American Petroleum Institute, the Department of Revenue, and other states. This recommendation is the second step in the Committee's efforts to prevent motor fuel tax evasion. Last year the General Assembly adopted the Committee's recommendation on "destination state" legislation.

Legislative Proposals 1, 3, 7, and 11 also reflect the Committee's recommendations on how to improve tax administration. They include recommendations on the inheritance tax laws, the sale of loose cigarettes, the repeal of the special use tax on construction equipment brought into this State, transporter plates for special mobile equipment, and salvage title transfers. Finally, the Committee addressed numerous technical changes that need to be made to the revenue laws. Legislative Proposal 14 contains the Committee's recommendations for technical changes.

The Committee adopted three proposals in response to recent court decisions. Legislative Proposal 2 strengthens the State's Controlled Substance Excise Tax against constitutional attack. Legislative Proposal 6 achieves uniform tax treatment for all federal, State, and local bonds in accordance with the constitutional doctrine of intergovernmental immunity. Legislative Proposal 10 reflects the Committee's

recommendation on how to repeal the intangibles tax in light of the pending appeal of a North Carolina Supreme Court decision that the taxable percentage deduction of the intangibles tax law does not violate the interstate commerce clause of the federal constitution.

The Committee expresses its appreciation for the assistance of Ms. Janice Faulkner, Secretary of Revenue, Mr. Jack L. Harper, Assistant Secretary of Tax Administration, and the staff of the Department of Revenue. The Committee's task is made easier by the informed comments and suggestions of these individuals.

COMMITTEE RECOMMENDATIONS AND LEGISLATIVE PROPOSALS

The Revenue Laws Study Committee recommends the following legislation to the 1995 General Assembly. The Committee's legislative proposals consist of * bills and a resolution. Each proposal is followed by an explanation; each proposal that has a fiscal impact is followed by a fiscal note indicating the anticipated revenue gain or loss resulting from the proposal.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

S D

Proposal 1 (95-LJX-5B(1.2))
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Inheritance/Gift Tax Changes. (Public)

Sponsors: Senators Kerr, Cochrane, and Hoyle.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO INCREASE THE CLASS A INHERITANCE TAX CREDIT, TO REDUCE THE INHERITANCE AND GIFT TAX RATES FOR CLASS B AND C BENEFICIARIES, TO CONFORM NORTH CAROLINA INHERITANCE AND GIFT TAX PROVISIONS TO FEDERAL ESTATE AND GIFT TAX PROVISIONS REGARDING QUALIFIED TERMINABLE INTEREST PROPERTY, AND TO MAKE OTHER INHERITANCE TAX CHANGES.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-4 reads as rewritten:

"**§ 105-4. Rate of tax -- Class A.**

(a) Rate. -- ~~Where the person or persons entitled to any beneficial interest in such property shall be the lineal issue, or lineal ancestor, or stepchild of the person who died possessed of such property aforesaid, or child adopted by the decedent in conformity with the laws of this State or of any of the United States, or of any foreign kingdom or nation, or a son-in-law or a daughter-in-law whose spouse is not entitled to any beneficial interest in such property of the person who died possessed of such property aforesaid, at the following rates of tax (for each one hundred dollars ($100.00) or fraction thereof) of the value of such interest:~~ A Class A beneficiary of a decedent is the decedent's lineal issue, lineal ancestor, adopted child, stepchild, or son-in-law or daughter-in-law whose spouse is not entitled to an interest in the decedent's property. The rate of

tax on property transferred to a Class A beneficiary is the percentage set in the following table for each one hundred dollars ($100.00), or fraction thereof, of value of the property:

Value of Property Transferred	Rate
First $10,000	1 ~~percent~~ %
Over $10,000 and to $25,000	2 ~~percent~~ %
Over $25,000 and to $50,000	3 ~~percent~~ %
Over $50,000 and to $100,000	4 ~~percent~~ %
Over $100,000 and to $200,000	5 ~~percent~~ %
Over $200,000 and to $500,000	6 ~~percent~~ %
Over $ 500,000 and to $1,000,000	7 ~~percent~~ %
Over $1,000,000 and to $1,500,000	8 ~~percent~~ %
Over $1,500,000 and to $2,000,000	9 ~~percent~~ %
Over $2,000,000 and to $2,500,000	10 ~~percent~~ %
Over $2,500,000 and to $3,000,000	11 ~~percent~~ %
Over $3,000,000	12 ~~percent~~ %.

(b) Credit. -- An inheritance tax credit ~~in the amount specified in the following table~~ of thirty-three thousand one hundred fifty dollars ($33,150) is allowed against the tax imposed by this Article on the transfer of property to a Class A beneficiary. This

~~For Decedents Dying on or After~~	~~Amount of Credit~~
~~August 1, 1985~~	~~$ 2,350~~
~~July 1, 1986~~	~~8,150~~
~~January 1, 1987~~	~~14,150~~
~~January 1, 1988~~	~~20,150~~
~~January 1, 1989~~	~~26,150~~

~~This~~ credit is allowed to Class A beneficiaries in the following order:

(1) Children who are less than 18 years old, and children who are at least 18 years old and who are single, are unable to support themselves because of mental or physical incapacity, and either are members of the decedent's household or, because of their mental or physical incapacity, live in an institution.

(2) Other Class A Beneficiaries. ~~-- The~~

The status of a beneficiary is determined as of the date of the decedent's death. When two or more beneficiaries are equally entitled to the credit, the credit shall be allocated among those beneficiaries on a pro rata basis according to their tax liability. The credit allowed by this section may not exceed the amount of tax imposed by this Article."

Sec. 2. G.S. 105-5 reads as rewritten:

"§ 105-5. Rate of tax -- Class B.

~~Where the person or persons entitled to any beneficial interest in such property shall be the brother or sister or descendant of the brother or sister, or shall be the uncle or aunt by blood of the person who died possessed as aforesaid, at the following rates of tax (for each one hundred dollars ($100.00) or fraction thereof) of the value of such interest:~~ A Class B beneficiary of a decedent is the decedent's brother, sister, descendant of a brother or sister, or uncle or aunt by blood. The rate of tax on property transferred to a Class B beneficiary is the percentage set in the following table for each one hundred dollars ($100.00), or fraction thereof, of value of the property:

Value of Property Transferred	Rate
First $5,000	~~4 percent~~ 3%
Over $5,000 and to $10,000	~~5 percent~~ 4%
Over $10,000 and to $25,000	6 ~~percent~~ %
Over $25,000 and to $50,000	7 ~~percent~~ %
Over $50,000 and to $100,000	8 ~~percent~~ %
Over $100,000 and to $250,000	10 ~~percent~~ %
Over $250,000 and to $500,000	11 ~~percent~~ %
Over $500,000 and to $1,000,000	12 ~~percent~~ %
Over $1,000,000 and to $1,500,000	13 ~~percent~~ %
Over $1,500,000 and to $2,000,000	14 ~~percent~~ %
Over $2,000,000 and to $3,000,000	15 ~~percent~~ %
Over $3,000,000	16 ~~percent~~ %."

Sec. 3. G.S. 105-6 reads as rewritten:

"§ 105-6. Rate of tax -- Class C.

~~Where the person or persons entitled to any beneficial interest in such property shall be in any other degree of relationship or collateral consanguinity than is hereinbefore stated, or shall be a stranger in blood to the person who died possessed as aforesaid, or shall be a body politic or corporate, at the following rates of tax (for each one hundred dollars ($100.00) or fraction thereof) of the value of such interest:~~ A Class C beneficiary of a decedent is a person who is not a Class A or Class B beneficiary. The rate of tax on property transferred to a Class C beneficiary is the percentage set in the following table for each one hundred dollars ($100.00), or fraction thereof, of value of the property:

Value of Property Transferred	Rate
First $5,000	4%
~~First~~ Over $5,000 and to $10,000	~~8 percent~~ 6%
Over $10,000 and to $25,000	~~9 percent~~ 8%

Over $25,000 and to $50,000	10 ~~percent~~ %
Over $50,000 and to $100,000	11 ~~percent~~ %
Over $ 100,000 and to $250,000	12 ~~percent~~ %
Over $ 250,000 and to $500,000	13 ~~percent~~ %
Over $ 500,000 and to $1,000,000	14 ~~percent~~ %
Over $1,000,000 and to $1,500,000	15 ~~percent~~ %
Over $1,500,000 and to $2,500,000	16 ~~percent~~ %
Over $2,500,000	17 ~~percent~~ %."

Sec. 4. G.S. 105-188(f) reads as rewritten:

"(f) The rates of ~~tax, which~~ tax on net gifts are based on the relationship between the donor and the ~~donee, shall be~~ donee and are as follows:

(1) ~~Where the~~ For a donee who is the lineal issue, lineal ancestor, adopted child, or stepchild of the ~~donor (for each one hundred dollars ($100.00) or fraction thereof):~~ donor, the rate is the percentage set in the following table for each one hundred dollars ($100.00), or fraction thereof, of value of the gift:

Value of Gift	Rate
First $10,000 ~~above exemption~~	1 ~~percent~~ %
Over $10,000 and to $25,000	2 ~~percent~~ %
Over $25,000 and to $50,000	3 ~~percent~~ %
Over $50,000 and to $100,000	4 ~~percent~~ %
Over $100,000 and to $200,000	5 ~~percent~~ %
Over $200,000 and to $500,000	6 ~~percent~~ %
Over $500,000 and to $1,000,000	7 ~~percent~~ %
Over $1,000,000 and to $1,500,000	8 ~~percent~~ %
Over $1,500,000 and to $2,000,000	9 ~~percent~~ %
Over $2,000,000 and to $2,500,000	10 ~~percent~~ %
Over $2,500,000 and to $3,000,000	11 ~~percent~~ %
Over $3,000,000	12 ~~percent~~ %.

(2) ~~Where the~~ For a donee who is the donor's brother or sister, ~~or~~ a descendant of the donor's brother or sister, or ~~is~~ the donor's uncle or aunt by ~~blood of the donor (for each one hundred dollars ($100.00) or fraction thereof):~~ blood, the rate of tax is the percentage set in the following table for each one hundred dollars ($100.00), or fraction thereof, of value of the gift:

Value of Gift	Rate
First $5,000	~~4 percent~~ 3%
Over $5,000 and to $10,000	~~5 percent~~ 4%
Over $10,000 and to $25,000	6 ~~percent~~ %

Over $25,000 and to $50,000	7 ~~percent~~ %
Over $50,000 and to $100,000	8 ~~percent~~ %
Over $100,000 and to $250,000	10 ~~percent~~ %
Over $250,000 and to $500,000	11 ~~percent~~ %
Over $500,000 and to $1,000,000	12 ~~percent~~ %
Over $1,000,000 and to $1,500,000	13 ~~percent~~ %
Over $1,500,000 and to $2,000,000	14 ~~percent~~ %
Over $2,000,000 and to $3,000,000	15 ~~percent~~ %
Over $3,000,000	16 ~~percent~~ %.

(3) ~~Where the donee is in any other degree of relationship than is hereinbefore stated, or shall be a stranger in blood to the donor, or shall be a body politic or corporate (for each one hundred dollars ($100.00) or fraction thereof):~~ For a donee who is not described in subdivisions (1) or (2) of this subsection, the rate of tax is the percentage set in the following table for each one hundred dollars ($100.00), or fraction thereof, of value of the gift:

Value of Gift	Rate
First $ 5,000	4%
Over $5,000 and to ~~First~~ $10,000	~~8 percent~~ 6%
Over $10,000 and to $25,000	~~9 percent~~ 8%
Over $25,000 and to $50,000	10 ~~percent~~ %
Over $50,000 and to $100,000	11 ~~percent~~ %
Over $100,000 and to $250,000	12 ~~percent~~ %
Over $250,000 and to $500,000	13 ~~percent~~ %
Over $500,000 and to $1,000,000	14 ~~percent~~ %
Over $1,000,000 and to $1,500,000	15 ~~percent~~ %
Over $1,500,000 and to $2,500,000	16 ~~percent~~ %
Over $2,500,000	17 ~~percent~~ %."

Sec. 5. G.S. 105-3 is amended by adding a new subdivision to read:

"(11) Property transferred to another when the transfer of the property is exempt from federal estate and gift taxes under § 2056(b)(7) of the Code because it is considered qualified terminable interest property."

Sec. 6. G.S. 105-188 is amended by adding a new subsection to read:

"(j) The tax does not apply to property transferred to another when the transfer of the property is exempt from federal estate and gift taxes under § 2523(f) of the Code because it is considered qualified terminable interest property."

Sec. 7. G.S. 105-2(a) reads as rewritten:

"(a) A tax shall be and is hereby imposed upon the transfer of any property, real or personal, or of any interest therein or income therefrom, in trust or otherwise, to persons or corporations, in the following cases:

(1) When the transfer is from a person who dies seized of the property while a resident of the State and it is made:

a. By will or by intestacy;

b. Pursuant to a final judgment entered in a proceeding to caveat a will; or

c. Pursuant to a settlement agreement, to which the personal representative is a party, that, in the determination of the Secretary of Revenue in his sole discretion based on evidence presented by the personal representative, reflects the good faith, arm's-length compromise of an actual dispute between beneficiaries, heirs, or personal representatives and does not have the primary purpose of avoiding inheritance tax.

(2) When the transfer is by will or intestate laws of this or any other state of real property or goods, wares, and merchandise within this State, or of any property, real, personal, or mixed, tangible or intangible, over which the State of North Carolina has a taxing jurisdiction, including State and municipal bonds, and the decedent was a resident of the State at the time of death; when the transfer is of real property or tangible personal property within the State, or intangible personal property that has acquired a situs in this State, and the decedent was a nonresident of the State at the time of death.

(3) When the transfer of property made by a resident, or nonresident, is of real property within this State, or of goods, wares and merchandise within this State, or of any other property, real, personal, or mixed, tangible or intangible, over which the State of North Carolina has taxing jurisdiction, including State and municipal bonds, by deed, grant, bargain, sale, or gift made in contemplation of the death of the grantor, vendor, or donor, or intended to take effect in possession

or enjoyment at or after such death, including a transfer under which the transferor has retained for his life or any period not ending before his death (i) the possession or enjoyment of, or the income from, the property or (ii) the right to designate the persons who shall possess or enjoy the property or the income therefrom. The aggregate value exceeding ten thousand dollars ($10,000) of transfers to any one donee within a tax year by deed, grant, bargain, sale, gift, or combination thereof, made within three years prior to the death of the grantor, vendor, or donor, without an adequate valuable consideration, shall be presumed, subject to rebuttal, to have been made in contemplation of death within the meaning of this section; the first ten thousand dollars ($10,000) in value shall be deemed not made in contemplation of death.

(4) When any person or corporation comes into possession or enjoyment, by a transfer from a resident, or from a nonresident decedent when such nonresident decedent's property consists of real property within this State or tangible personal property within the State, or intangible personal property that has acquired a situs in this State, of an estate in expectancy of any kind or character which is contingent or defeasible, transferred by any instrument taking effect after March 24, 1939.

(5) a. For purposes of this Article, the term "general power of appointment" means a power which is exercisable in favor of the decedent, his estate, his creditors, or the creditors of his estate; except that:

1. A power to consume, invade or appropriate property for the benefit of the decedent which is limited by an ascertainable standard relating to the health, education, support or maintenance of the decedent shall not be deemed a general power of appointment.

2. A power of appointment which is exercisable by the decedent only in conjunction with another person:

I. If the power is not exercisable by the decedent except in conjunction with the creator of the power, such power shall not be deemed a general power of appointment.

II. If the power is not exercisable by the decedent except in conjunction with a person having a substantial interest in the property, subject to the power, which is adverse to exercise of the power in favor of the decedent, such power shall not be deemed a general power of appointment. For the purposes of this clause a person who, after the death of the decedent, may be possessed of a power of appointment (with respect to the property subject to the decedent's power) which he may exercise in his own favor shall be deemed as having an interest in the property and such interest shall be deemed adverse to such exercise of the decedent's power.

III. If (after the application of clauses I and II) the power is a general power of appointment and is exercisable in favor of such other person, such power shall be deemed a general power of appointment only in respect of a fractional part of the property subject to such power, such part to be determined by dividing the value of such property by the number of such persons (including the decedent) in favor of whom such power is exercisable.

IV. For purposes of clauses II and III, a power shall be deemed to be exercisable in favor of a person if it is exercisable in favor of such person, his estate, his creditors, or the creditors of his estate.

b. Whenever any person shall have a general power of appointment with respect to any interest in property, such person shall, for the purposes of this Article, be deemed the owner of such interest and accordingly:

1. If in connection with any transfer of property taxable under this Article the transferor shall give to any person a general power of appointment with respect to any interest in such property, the transferor shall be deemed to have given such interest in such property to such person.
2. If any person holding a general power of appointment with respect to any interest in property shall exercise such power in favor of any other person or persons, either by will or by an appointment made in contemplation of the death of such person, or by an appointment intended to take effect in possession or enjoyment at or after such death, he shall be deemed to have made a transfer of such interest to such person or persons.
3. If any person holding a general power of appointment with respect to any interest in property shall relinquish such power by any action taken in contemplation of death or intended to take effect at or after his death, or shall die without fully exercising such power, he shall be deemed, to the extent of such relinquishment or nonexercise, to have made a transfer of such interest to the person or persons who shall benefit thereby.

(6) Neither the exercise nor the relinquishment of a special power of appointment (which shall mean any power other than a general power) with respect to an interest in property shall be deemed to constitute a transfer of such interest within the meaning of this Article. If in connection with any transfer taxable under this Article the transferor shall give to any person a special power of

appointment with respect to any interest in property, he shall be deemed, for the purpose of computing the tax applicable thereto, to have given such interest in equal shares to those persons, not more than two, among the possible appointees and takers in default of appointment whom the transferor's executor or administrator may designate as transferees in the inheritance tax return, except that:

a. If a gift tax return is filed with respect to such transfer, the persons designated therein shall also be designated in the inheritance tax return, and

b. The tax shall be computed according to the relationship of the donee of the power to the persons designated if the possible appointees and takers in default of appointment include any persons more closely related to the donee of the power than to the donor, and if such computation would produce a higher tax.

(7), (7a) Repealed by Session Laws, 1985, c. 656, s. 1.

(8) Where the proceeds of life insurance policies are payable as provided in G.S. 105-13.

(9) Whenever any person or corporation comes into possession or enjoyment of any real or personal property, including bonds of the United States and bonds of a state or subdivision or agency thereof, at or after the death of an individual and by reason of said individual's having entered into a contract or other arrangement with the United States, a state or any person or corporation to pay, transfer or deliver said real or personal property, including bonds of the United States and bonds of a state, to the person or corporation receiving the same, whether said person or corporation is named in the contract or other arrangement or not: Provided, that no tax shall be due or collected on that portion of the real or personal property received under the conditions outlined herein which the person or corporation receiving the same purchased or otherwise acquired by funds or property of the person or corporation receiving the same, or had acquired by a completed inter vivos gift.

Nothing in subdivision (9) shall apply to the proceeds of life insurance policies.

(10) Upon the death of a decedent who had a qualifying income interest for life in qualified terminable interest property whose previous transfer was exempt from inheritance or gift taxes under G.S. 105-3(11) or G.S. 105-188(j), the qualified terminable interest property that was previously exempt is considered to pass from the decedent to the person who is entitled to the property upon the termination of the decedent's qualifying income interest for life. This subdivision does not apply to an interest in qualified terminable interest property that the decedent transferred to another and was not part of the decedent's qualifying income interest for life.

However, nothing in this Article shall be construed as imposing a tax upon any transfer of intangibles not having a commercial or business situs in this State, by a person, or by reason of the death of a person, who was not a resident of this State at the time of his death, and, if held or transferred in trust, such intangibles shall not be deemed to have a commercial or business situs in this State merely because the trustee is a resident or, if a corporation, is doing business in this State, unless the same be employed in or held or used in connection with some business carried on in whole or in part in this State."

Sec. 8. G.S. 105-9(8) reads as rewritten:

"(8) Costs of ~~administration, including~~ administration not claimed as a deduction on the federal income tax return filed under the Code by the fiduciary for the decedent's estate. Costs of administration include reasonable attorneys' fees."

Sec. 9. G.S. 105-29 reads as rewritten:

"**§ 105-29. Uniform valuation.**

~~(a) If the value of any estate taxed under this schedule shall have been assessed and fixed by the federal government for the purpose of determining the federal taxes due thereon prior to the time the report from the executor or administrator is made to the Secretary of Revenue under the provisions of this Article, the amount or value of such estate so fixed, assessed, and determined by the federal government shall be stated in such report. If the assessment of the estate by the federal government shall be made after the filing of the report by the executor or administrator~~

with the Secretary of Revenue, as provided in this Article, the said executor or administrator shall, within 30 days after receipt of notice of the final determination by the federal government of the value or amount of said estate as assessed and determined for the purpose of fixing federal taxes thereon, make report of the amount so fixed and assessed by the federal government, under oath or affirmation, to the Secretary of Revenue. If the amount of said estate as assessed and fixed by the federal government shall be in excess of that theretofore fixed or assessed under this schedule for the purpose of determining the amount of taxes due the State from said estate, then the Secretary of Revenue shall reassess said estate and fix the value thereof at the amount fixed, assessed, and determined by the federal government, unless the said executor or administrator shall, within 30 days after notice to him from the Secretary of Revenue, show cause why the valuation and assessment of said estate as theretofore made should not be changed or increased. If the valuation placed upon said estate by the federal government shall be less than that theretofore fixed or assessed under this Article, the executor or administrator may, within 30 days after filing his return of the amount so fixed or assessed by the federal government, file with the Secretary of Revenue a petition to have the value of said estate reassessed and the same reduced to the amount as fixed or assessed by the federal government. In either event the Secretary of Revenue shall proceed to determine, from such evidence as may be brought to his attention or which he shall otherwise acquire, the correct value of the said estate, and if the valuation is changed, he shall reassess the taxes due by said estate under this Article and notify the executor or administrator of such fact. In the event the valuation of said estate shall be decreased and if there shall have been an overpayment of the tax in the amount of three dollars ($3.00) or more, the Secretary of Revenue shall, within 60 days after the final determination of the value of said estate and the assessment of the correct amount of tax against the same, refund the amount of such excess tax theretofore paid. In the event that the amount of such overpayment is less than three dollars ($3.00) the overpayment shall be refunded upon receipt by the Secretary of Revenue of a written demand for such refund from the taxpayer. No overpayment shall be refunded, irrespective of whether upon discovery or receipt of written demand if such discovery is not made or such demand is not received within three years from the date set by the statute for the filing of the return, or within six months after the date of

~~the final determination of the federal estate tax liability, or within six months from the date of the payment of the tax alleged to be an overpayment, whichever is the later.~~

~~(b) If the executor or administrator shall fail to file with the Secretary of Revenue the return under oath or affirmation, stating the amount or value at which the estate was assessed by the federal government as provided for in this section, the Secretary of Revenue shall assess and collect from the executor or administrator a penalty equal to twenty-five percent (25%) of the amount of any additional tax which may be found to be due by such estate upon reassessment and reappraisal thereof, which penalty shall under no condition be less than twenty-five dollars ($25.00) or more than five hundred dollars ($500.00) and which cannot be remitted by the Secretary of Revenue except for good cause shown. The Secretary of Revenue is authorized and directed to confer quarterly with the Department of Internal Revenue of the United States government to ascertain the value of estates in North Carolina which have been assessed for taxation by the federal government, and he shall cooperate with the said Department of Internal Revenue, furnishing to said Department such information concerning estates in North Carolina as said Department may request.~~

When filing an inheritance tax return, the personal representative of an estate must report as the value of the estate the value that is reported on an estate tax return filed for the estate under the Code. If the federal government does not correct or otherwise determine the value of an estate reported on an estate tax return, the Secretary may determine the value based on evidence of any kind that becomes available to the Secretary from any source.

If the federal government corrects or otherwise determines the value of an estate reported on an estate tax return, the personal representative must, within two years after being notified of the correction or final determination by the federal government, file an inheritance tax return with the Secretary reflecting the corrected or determined value. The Secretary must adopt the value as corrected or determined by the federal government for federal estate tax purposes. The Secretary shall assess and collect any additional tax due on the transfer of property in the estate as provided in Article 9 of this Chapter and shall refund any overpayment of tax as provided in Article 9 of this Chapter. A personal representative who fails to report a federal correction or determination is subject to the penalties in G.S.

105-236 and forfeits the right of the estate to any refund due by reason of the determination."

Sec. 10. G.S. 105-241.1(e) reads as rewritten:

"(e) Statute of Limitations. -- The Secretary may propose an assessment of tax due from a taxpayer at any time if (i) the taxpayer did not file a proper application for a license or did not file a return, (ii) the taxpayer filed a false or fraudulent application or return, or (iii) the taxpayer attempted in any manner to fraudulently evade or defeat the tax. If a taxpayer files a return reflecting a federal determination as provided in G.S. 105-29, 105-130.20, 105-159, 105-160.8, 105-163.6A, or 105-197.1, the Secretary must propose an assessment of any tax due within one year after the return is filed or within three years of when the original return was filed or due to be filed, whichever is later. If there is a federal determination and the taxpayer does not file the required return, the Secretary must propose an assessment of any tax due within three years after the date the Secretary received the final report of the federal determination. If a taxpayer forfeits a tax credit pursuant to G.S. 105-163.014, the Secretary must assess any tax or additional tax due as a result of the forfeiture within three years after the date of the forfeiture. In all other cases, the Secretary must propose an assessment of any tax due from a taxpayer within three years after the date the taxpayer filed an application for a license or a return or the date the application or return was required by law to be filed, whichever is later. If the Secretary proposes an assessment of tax within the time provided in this section, the final assessment of the tax is timely.

A taxpayer may make a written waiver of any of the limitations of time set out in this subsection, for either a definite or an indefinite time. If the Secretary accepts the taxpayer's waiver, the Secretary may propose an assessment at any time within the time extended by the waiver."

Sec. 11. Sections 1 through 7 of this act and this section are effective upon ratification and apply to the estates of decedents dying on or after January 1, 1995, and to gifts made on or after January 1, 1995. Sections 8 through 10 of this act become effective July 1, 1995. Section 8 applies to the estates of decedents dying on or after that date. Sections 9 and 10 apply to assessments of taxes for which the statute of limitations had not expired on or before July 1, 1995.

Explanation of Proposal 1

This proposal reduces inheritance and gift taxes in a number of ways and makes two slight adjustments in the inheritance tax laws. The reductions are effective upon ratification and apply to the estates of decedents dying on or after January 1, 1995, and to gifts made on or after January 1, 1995. The adjustments become effective July 1, 1995.

The reductions occur from four changes. First, the proposal increases the Class A inheritance tax credit from $26,150 to $33,150. This increase in the credit increases the amount of property exempted by it from at least $500,000 to at least $600,000 and thereby reduces the amount of property subject to inheritance tax. Second, the proposal reduces inheritance and gift taxes for Class B beneficiaries by reducing the tax rates on the first $10,000 in value of each taxable gift or amount of property inherited. It reduces the current 4% Class B bracket to 3% and reduces the 5% Class B bracket to 4%.

Third, the proposal reduces inheritance and gift taxes for Class C beneficiaries by reducing the tax rates on the first $25,000 in value of each taxable gift or amount of property inherited. It replaces the current Class C 8% bracket with two brackets, a 4% bracket and a 6% bracket, and it reduces the current 9% Class C bracket to an 8% bracket. Fourth, the proposal exempts from State inheritance and gift taxes property that is exempt from federal estate and gift taxes because it is considered qualified terminable interest property (QTIP). Section 1 of the proposal increases the Class A credit, Sections 2 through 4 reduce the Class B and C inheritance and gift tax rates, and Sections 5 through 7 make the QTIP changes.

The two adjustments prevent the same item of expense from being deducted on an income tax return and an inheritance tax return filed for an estate and make the time limits for assessing any inheritance tax due after a federal determination of the value of an estate the same as the time limits that apply to assessments of other state taxes following a federal determination. Section 8 prevents the double deduction and Sections 9 and 10 make the changes to the time limits.

Background

North Carolina inheritance and gift tax rates are based on the relationship of the person transferring the property to the person receiving the property. This is in contrast to federal law, which has a single rate schedule for gifts and estates. As under federal law, however, all transfers to a spouse are exempt from State inheritance or gift taxes.

State law classifies beneficiaries into three classes, Class A, Class B, and Class C, and sets different rates for each class. A Class A beneficiary is a lineal ancestor, a lineal descendant, an adopted child, a step-child, or a son-in-law or daughter-in-law whose spouse is not entitled to any of the decedent's property; a Class B beneficiary is a sibling, a descendant of a sibling, or an aunt or uncle by blood; and a Class C beneficiary is anyone who is not a Class A or Class B beneficiary. Class A beneficiaries have the lowest rates, Class B beneficiaries have higher rates, and Class C beneficiaries have the highest rates. Thus, North Carolina's rate structure favors transfers to children and parents by giving these transfers the lowest rates and prefers transfers to other close family members over transfers to more distant relatives or to persons who are not related by giving these transfers the in-between rate.

Increase in Class A Inheritance Tax Credit

In addition to enjoying the lowest inheritance tax rate, Class A beneficiaries also receive an inheritance tax credit. The credit is currently $26,150, which exempts $500,000 of property if all the property is given to one child, for example, and exempts more than $500,000 of property if the property is divided among two or more children or other Class A beneficiaries. Any unused portion of the credit cannot be applied to transfers to Class B or Class C beneficiaries.

Several members of the Revenue Laws Study Committee advocated increasing the Class A credit so that the amount exempted by it would be the same as the amount that is exempted from federal estate and gift taxes by application of the federal unified credit. The federal unified credit is $192,800, which exempts $600,000 of property from federal estate or gift taxes. The federal credit is unified in that it applies to both federal estate and gift taxes. Any part of the credit that is not used on gift taxes is applied to estate taxes.

The State Class A inheritance tax credit is not a unified credit. It does not apply to State gift taxes. State law provides a separate $100,000 lifetime exemption for gifts made to Class A beneficiaries. Under current law, therefore, the combination of the

State gift tax lifetime exemption for Class A beneficiaries and the Class A inheritance tax credit exempts the same amount of property as the federal unified credit.

The Committee members decided that, because any unused portion of the State gift tax lifetime exemption cannot be added to the State inheritance tax credit, the State inheritance tax credit needs to be increased to the level of the federal unified credit. The Committee consequently adopted Section 1 of this proposal. That section increases the Class A inheritance tax credit to $33,150, which exempts an additional $100,000 from inheritance tax. If the proposal is enacted and a person fully uses both the State $100,000 gift tax lifetime exemption and the State Class A inheritance tax credit, the person can exempt more property from gift and inheritance taxes under State law than under federal law.

Reduction in Class B Inheritance and Gift Tax Rates

An individual who had moved to North Carolina in 1989 came to the Committee and asked that State inheritance taxes be repealed or that Class C beneficiaries be given some tax relief. He pointed out that he does not have any living blood relatives, who would be Class A or Class B beneficiaries. In response to this, the Committee tentatively adopted a proposal to reduce the Class C rates on the first $10,000 of property to the Class B rates.

Upon further reflection, the Committee decided that the Class B rates needed to be changed as well to avoid several pitfalls of its initial proposal. Changing the Class C rates as originally contemplated would depart from the underlying inheritance tax premise that rates should increase with distance from familial relationships and would produce Class C brackets with precipitous rather than gradual increases.

The Committee therefore adopted changes in the Class B rates. It recommended lowering the 4% Class B bracket to 3% and lowering the 5% Class B bracket to 4%. The current 4% bracket applies to the first $5,000 in value, and the 5% bracket applies to the next $5,000 in value. The result is that the tax rate on the first $10,000 in value is reduced for all property inherited by or given to Class B beneficiaries. Sections 2 and 4 of the bill make these changes.

Reduction in Class C Inheritance and Gift Tax Rates

In response to the taxpayer request described above under the discussion of the reductions in the Class B tax rates, the Committee decided to recommend lowering the Class C inheritance and gift tax rates. The proposal changes the current 8% Class C

bracket, which applies to the first $10,000 in property, to two brackets and sets the rate on the first $5,000 of value at 4% and the rate on the next $5,000 of value at 5%. It also lowers the Class C rate on the next $15,000 in value from 9% to 8%. Sections 3 and 4 of the proposal make these changes.

Qualified Terminable Interest Property (QTIP) Changes

At the request of the Estate Planning and Fiduciary Law Section of the North Carolina Bar Association, the Committee reviewed Senate Bill 566 of the 1993 Session to determine whether to recommend it to the 1995 General Assembly. That bill was sponsored by Senator Dennis Winner, passed the Senate, and was considered but not given a favorable report by the House Finance Committee. Since the time the bill was considered in the House Finance Committee, the Department of Revenue prepared a fiscal estimate of the loss of inheritance tax revenue that would result from the bill. The estimate of the Department is less than the estimate used by the House Finance Committee when considering the bill.

The Committee found the QTIP issue to be complex. After debating the issue, however, the Committee concluded that North Carolina law should conform to federal law on this topic for two reasons. First, conformity would provide consistent treatment at the federal and State level. Second, this type of property is more like an outright transfer to a spouse than it is to any other kind of transfer and, consequently, no inheritance tax should be due until the spouse subsequently dies and passes the property on to its ultimate beneficiaries. The Committee's conclusions were not unanimous, however. Concerns were expressed at the effect of the proposed change, which is to reduce inheritance taxes on the wealthiest estates.

The proposed QTIP changes require North Carolina to exempt from State inheritance and gift taxes property that is exempt from federal estate and gift taxes because it is considered qualified terminable interest property. Put simply, QTIP property is property placed in a trust in which a person's spouse has an income interest for life and the person's children or other designated beneficiaries have a remainder interest.

Under federal law, a transfer of property that qualifies as QTIP property is not taxable when the transfer is made. Instead, it is taxed when the spouse who had the lifetime income interest in the property dies. At that time, the value of the QTIP property is included in the spouse's gross estate.

Under North Carolina law, when property is transferred by means of a QTIP trust, two transfers are considered to have been made. One transfer is the transfer to the spouse of a life estate in the trust income. The transfer of the life estate to the spouse is not taxed because all property that passes to a spouse is exempt from State inheritance and gift taxes. The value of the spouse's life estate is the present value of the stream of income based on the life expectancy of the spouse.

The other transfer is a transfer of the remainder interest in the trust property to the transferor's children or other designated beneficiaries. The transfer of the remainder interest is subject to inheritance or gift tax. The value of the remainder interest is its present value as of the date of death or date of the gift.

Under this proposal, the remainder interest in QTIP property would no longer be taxable under North Carolina law when the QTIP trust is established. Instead, it would be taxable when the spouse with the life estate in the income died and would be taxed on the basis of the value at the spouse's death. In some cases, taxes would be collected at a later time than under current law, but in many cases less tax would be collected than under current law. Further reductions in tax would occur if the value of the trust property declined over time. No tax would be collected at a later date if the spouse moved out of the State before death and the trust consisted of securities rather than real property located in the State. By the same token, some tax would be collected that is not now collected if a spouse with a QTIP trust moves into the State.

The following examples illustrate some of the differences in taxes under the current law and the proposed law:

Example 1: Husband dies having a $1,500,000 estate, QTIP trust is established for 75-year-old widow, remainder to children

Current Law

NC Taxes at Husband's Death:	$ 46,925	(tax on remainder interest to children)
NC Taxes at Widow's Death:	3,600	(State pick-up tax through federal State death tax credit)
	50,525	

Proposed Law

NC Taxes at Husband's Death:	7,000	(assumes $600,000 given to someone outside QTIP to reduce federal taxes)
NC Taxes at Widow's Death:	28,000	
	35,000	

Tax Loss in Example 1 = 15,525 (31%)

Example 2: Husband dies having an $8,000,000 estate, QTIP trust is established for 65-year-old widow, remainder to children

Current Law

NC Taxes at Husband's Death:	$ 320,874	(tax on remainder interest to child)
NC Taxes at Widow's Death:	612,400	(State pick-up tax through federal State death tax credit)
	933,274	

Proposed Law

NC Taxes at Husband's Death:	7,000	(assumes $600,000 given to someone outside QTIP to reduce federal taxes)
NC Taxes at Widow's Death:	753,000	
	640,000	

Tax Loss in Example 2 = 173,274 (19%)

A QTIP trust need not be established before a gift is made or the decedent dies. If the transfer is a gift, the trust can be established any time before the gift tax return is filed. If the transfer is a devise upon death, the trust can be established any time before the estate tax return is due if the will gives the personal representative the option of establishing a QTIP trust. The decision of whether or not to establish a QTIP trust is made after considering tax consequences and other factors.

The purpose of the QTIP exemption under federal law is to avoid taxing the life estate interest of the spouse. Generally, under federal law, a life estate interest of a spouse that is not created in a QTIP trust is not entitled to the marital deduction and is

therefore subject to tax. By contrast, under North Carolina law, a life estate interest of a spouse is entitled to the marital deduction and is not subject to tax.

Prevention of Double Deduction

Current law allows the costs of administering an estate to be deducted when determining the amount of inheritance tax payable on property in the estate. Costs of administration include attorney fees, accountant fees, and executor fees. The law, however, does not limit the inheritance tax deduction to costs that are not deducted on a fiduciary income tax return filed for the estate. If the same cost is deducted on both returns, the taxpayer receives an unintended double deduction for the same item.

A double deduction for the same item of cost is most likely to result when, because of the small size of an estate, no federal estate tax return is filed but a federal fiduciary income tax return is filed. In this instance, all costs will be deducted on the federal fiduciary income tax return.

North Carolina's income tax uses federal taxable income as the starting point in computing North Carolina taxable income. A result of this is that deductions taken on the federal return are automatically passed through on the North Carolina return. Thus, any item that is deducted on the federal fiduciary income tax return is also deducted on the State fiduciary income tax return. To prevent a double deduction, Section 8 of the proposal prohibits the deduction of an item on an inheritance tax return if the item was deducted on the federal fiduciary income tax return.

Time Limits After A Federal Determination

Sections 9 and 10 of the proposal make the same changes for inheritance tax that were made for gift tax, income tax, and withholding tax by Chapter 582 of the 1993 Session Laws. Consequently, they revise the procedures for assessments of inheritance tax following a federal determination of federal estate tax to match those that apply to gift tax, income tax, and withholding tax. The revision makes the following substantive changes:

(1) It extends from 30 days to two years the period of time in which a taxpayer must file an amended inheritance tax return following a federal determination.

(2) It gives the State an additional one-year or three-year period to make an assessment of inheritance tax following a federal determination.

(3) It reduces the penalty for failure to file an amended return following a federal determination from 25% of the amount of any additional tax due, with a minimum of $25 and a maximum of $500, to 5% of the amount of tax due, with an additional 5% for each month the tax is overdue.

(4) It denies a refund that would otherwise be due if an amended return is not filed after a federal determination.

A federal determination is a report by the Internal Revenue Service (IRS) that a taxpayer has not filed a return or has filed an incorrect return and, therefore, either owes more taxes or is entitled to a refund. If a taxpayer did not file a return or understated the amount due on a return, the determination states the amount of tax the IRS finds is due and serves as the federal notice of assessment. The IRS eventually sends the appropriate state a copy of the federal determination. A delay between when a taxpayer receives a federal determination and when a state receives a copy of the determination occurs when the taxpayer is in the process of resolving with the IRS questions raised by the determination.

Under the State income, gift, and withholding tax laws, a taxpayer who receives a federal determination of federal income, gift, or withholding tax must, within two years, file the appropriate amended State return with the Department of Revenue reflecting the determination. Under these taxes, if a taxpayer files an amended return in response to a federal determination, the Department of Revenue has one year from the date it receives the return to make an assessment of State income, gift, or withholding taxes. If a taxpayer does not file an amended return in response to a federal determination, the Department of Revenue has three years from the date it receives a copy of the determination from the IRS to make an assessment.

The general limitations period for an assessment of any State tax is three years after a return was filed or due to be filed. The one-year and three-year periods following a federal determination are in addition to the regular three-year period, which is set out in G.S. 105-241.1. An additional time period is necessary when a federal determination is made to allow the State adequate time to respond to the federal determination. The State may not receive an amended return following a federal determination or a notice of a federal determination from the IRS until near the end of or after the end of the general three-year period.

Unlike the income, gift, and withholding tax laws, the inheritance tax laws do not give the State any additional time to make an assessment following a federal determination. Therefore, for an assessment of inheritance tax, the State must make an

assessment within the general three-year time period for making assessments. When the State does not receive notice of a federal determination of estate taxes until near the end of or after the end of this three-year period, the State is foreclosed from making an assessment.

Section 9 also makes technical changes to G.S. 105-29, the principal statute affected. It rewrites the statute to make it clearer and it deletes provisions, such as those on overpayments, that are also contained in other portions of the tax laws. G.S. 105-266, for example, sets out the general provisions on overpayments.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: PROPOSAL #1
SHORT TITLE: INHERITANCE/GIFT TAX RELIEF
SPONSOR(S):

FISCAL IMPACT: Expenditures: Increase ( ) Decrease ( )
Revenues: Increase ( ) Decrease (X)

FUND AFFECTED: General Fund (X) Highway Fund ( ) Local Govt. ( )
Other Funds ( )

BILL SUMMARY: (1) Increases inheritance tax credit for Class A beneficiaries (lineal ancestors, lineal descendants) from $26,150 (equivalent to exemption of first $500,000) to $33,150 (exemption of first $600,000)

(2) Reduces the inheritance tax rate for Class B & C beneficiaries on first few rate brackets as follows:

	Class B		Class C	
Taxable Value	Current Rate	Proposed Rate	Current Rate	Proposed Rate
First $5,000	4%	3%	8%	4%
5,000-10,000	5	4	9	6
10,000-25,000	6	6	10	8

(3) Exempts from inheritance and gift taxes property that is exempt from federal estate and gift taxes because it is considered qualified terminable interest property (QTIP).

(4) Prevents the same item of expense from being deducted on both the inheritance tax return and the income tax return filed for an estate.

(5) Makes the time limits for assessing any inheritance tax due after a federal determination of estate value the same as the time limits that apply to assessments of other State taxes following a federal determination.

EFFECTIVE DATE: Items #1 - 3: Deaths occurring on or after January 1, 1995 and gifts made on or after that date. Items #4 & 5: July 1, 1995.

FISCAL IMPACT

	$Million FY96	FY97	FY98	FY99	FY00
REVENUES:					
GENERAL FUND	-$4.2	-$6.1	-$6.5	-$7.1	-$7.7

ASSUMPTIONS AND METHODOLOGY: Items #4 and #5 have an insignificant impact, based on discussion with the Department of Revenue. The estimates for the remaining portions of the proposal are based on an analysis by the Department of Revenue of a manual sample of inheritance tax returns filed in 1993. The numbers were adjusted to future years by Fiscal Research based on 8% annual growth (actual experience in recent years).

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: Dave Crotts
APPROVED BY:
DATE: December 1, 1994
[FRD#001]

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

Proposal 2 (95-LCX-014(1.1))
(THIS IS A DRAFT AND NOT READY FOR INTRODUCTION)

Short Title: Revise Drug Tax. (Public)

Sponsors: Representatives Arnold, Gamble, Luebke, Ramsey, and Tallent.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO REVISE THE CONTROLLED SUBSTANCE EXCISE TAX.

The General Assembly of North Carolina enacts:

Section 1. Article 2D of Chapter 105 of the General Statutes reads as rewritten:

"ARTICLE 2D.

Schedule B-D. Controlled Substance Tax.

"§ 105-113.105. Purpose.

The purpose of this Article is to levy an excise tax ~~on persons who possess controlled substances and counterfeit controlled substances in violation of North Carolina law and to provide that a person who possesses such substances in violation of this Article is guilty of a felony.~~ to generate revenue for State and local law enforcement agencies and for the General Fund. Nothing in this Article may in any manner provide immunity from criminal prosecution for a person who possesses an illegal substance.

"§ 105-113.106. Definitions.

The following definitions apply in this Article:

(1) Controlled Substance. -- Defined in G.S. 90-87.

~~(2) Counterfeit Controlled Substance. -- Defined in G.S. 90-87.~~

(3) Dealer. -- A person who ~~in violation of G.S. 90-95 possesses, delivers, sells, or manufactures~~

actually or constructively possesses more than 42.5 grams of marijuana, ~~or~~ seven or more grams of any other controlled substance ~~or counterfeit controlled substance~~ that is sold by weight, or 10 or more dosage units of any other controlled substance ~~or counterfeit controlled substance~~ that is not sold by weight.

~~(4) Deliver. -- Defined in G.S. 90-87.~~

(4a) Reserved.

(4b) Reserved.

(4c) Low-street-value drug. -- Any of the following controlled substances:

a. An anabolic steroid as defined in G.S. 90-91(k).

b. A depressant described in G.S. 90-89(d), 90-90(d), 90-91(b), or 90-92(a).

c. A hallucinogenic substance described in G.S. 90-89(c) or G.S. 90-90(e).

d. A stimulant described in G.S. 90-89(e), 90-90(c), 90-91(j), 90-92(d), or 90-93(a)3.

e. A controlled substance described in G.S. 90-91(c), (d), or (e), 90-92(c), (e), or (f), or 90-93(a)1.

~~(5) Manufacture. -- Defined in G.S. 90-87.~~

(6) Marijuana. -- ~~Defined in G.S. 90-87.~~ All parts of the plant of the genus Cannabis, whether growing or not; the seeds of this plant; the resin extracted from any part of this plant; and every compound, salt, derivative, mixture, or preparation of this plant, its seeds, or its resin.

(7) Person. -- Defined in G.S. 105-228.90.

(8) Secretary. -- ~~The Secretary of the Department of Revenue.~~ Defined in G.S. 105-228.90.

"§ 105-113.107. Excise tax on controlled substances.

An excise tax is levied on controlled substances ~~and counterfeit controlled substances possessed~~ possessed, either actually or constructively, by dealers at the following rates:

(1) At the rate of forty cents (40¢) for each gram, or fraction thereof, of harvested marijuana stems and stalks that have been separated from and are not mixed with any other parts of the marijuana plant.

(1a) At the rate of three dollars and fifty cents ($3.50) for each gram, or fraction thereof, of ~~marijuana or counterfeit marijuana.~~ marijuana,

other than separated stems and stalks taxed under subdivision (1) of this section.

(2) At the rate of two hundred dollars ($200.00) for each gram, or fraction thereof, of any other controlled substance ~~or counterfeit controlled substance~~ that is sold by weight.

(2a) At the rate of fifty dollars ($50.00) for each 10 dosage units, or fraction thereof, of any low-street-value drug that is not sold by weight.

(3) At the rate of four hundred dollars ($400.00) for each 10 dosage units, or fraction thereof, of any other controlled substance ~~or counterfeit controlled substance~~ that is not sold by weight.

A quantity of marijuana or other controlled substance is measured by the weight of the substance whether pure or impure or dilute, or by dosage units when the substance is not sold by weight, in the dealer's possession. A quantity of a controlled substance is dilute if it consists of a detectable quantity of pure controlled substance and any excipients or fillers.

"**§ 105-113.107A. Exemptions.**

(a) Authorized Possession. -- The tax levied in this Article does not apply to a controlled substance in the possession of a dealer who is authorized by law to possess the substance. This exemption applies only during the time the dealer's possession of the substance is authorized by law.

(b) Certain Marijuana Parts. -- The tax levied in this Article does not apply to the following marijuana:

(1) Harvested mature marijuana stalks when separated from and not mixed with any other parts of the marijuana plant.

(2) Fiber or any other product of marijuana stalks described in subdivision (1) of this subsection, except resin extracted from the stalks.

(3) Marijuana seeds that have been sterilized and are incapable of germination.

(4) Roots of the marijuana plant.

"**§ 105-113.108. Reports; revenue stamps.**

The Secretary shall issue stamps to affix to controlled substances ~~and counterfeit controlled substances~~ to indicate payment of the tax required by this Article. Dealers shall report the taxes payable under this Article at the time and on the form prescribed by the Secretary. Dealers are not required to give their name, address, social security number, or other identifying information on the form. Upon payment of the tax,

the Secretary shall issue stamps in an amount equal to the amount of the tax paid. Taxes may be paid and stamps may be issued either by mail or in person.

"**§ 105-113.109. When tax payable.**

The tax imposed by this Article is payable by any dealer who actually or constructively possesses a controlled substance ~~or counterfeit controlled substance~~ in this State upon which the tax has not been paid, as evidenced by a stamp. The tax is payable within 48 hours after the dealer acquires actual or constructive possession of a non-tax-paid controlled ~~substance or counterfeit controlled substance,~~ substance, exclusive of Saturdays, Sundays, and legal holidays of this State, in which case the tax is payable on the next working day. Upon payment of the tax, the dealer shall permanently affix the appropriate stamps to the controlled substance. Once the tax due on a controlled substance ~~or counterfeit controlled substance~~ has been paid, no additional tax is due under this Article even though the controlled substance ~~or counterfeit controlled substance~~ may be handled by other dealers.

~~"§ 105-113.110. Violations of Article a felony.~~

~~(a) A dealer who possesses marijuana or any other controlled substance or counterfeit controlled substance upon which the tax due under this Article has not been paid, as evidenced by a stamp, is guilty of a Class I felony.~~

~~(b) Notwithstanding any other provision of law, no prosecution for a violation of this Article shall be barred before the expiration of six years after the date of the violation.~~

"**§ 105-113.110A. Interest and penalty.**

The tax due under this Article shall bear interest at the rate established pursuant to G.S. 105-241.1(i) from the date due until paid. In addition, a dealer who neglects, fails, or refuses to pay the tax due under this Article is liable for a penalty equal to ~~one hundred percent (100%)~~ fifty percent (50%) of the tax."

"**§ 105-113.111. Assessments.**

~~(a)~~ Notwithstanding any other provision of law, an assessment against a dealer who possesses a controlled substance to which a stamp has not been affixed as required by this Article shall be made as provided in this section. The Secretary shall assess a tax, applicable penalties, and interest based on personal knowledge or information available to the Secretary. The Secretary shall notify the dealer in writing of the amount of the tax, penalty, and interest due, and demand its immediate payment. The notice and demand shall be either mailed to the dealer at the dealer's last known address or served on the dealer in person. If

the dealer does not pay the tax, penalty, and interest immediately upon receipt of the notice and demand, the Secretary shall collect the tax, penalty, and interest pursuant to the procedure set forth in G.S. 105-241.1(g) for jeopardy assessments or the procedure set forth in G.S. 105-242, including causing execution to be issued immediately against the personal property of the ~~dealer~~ dealer, unless the dealer files with the Secretary a bond in the amount of the asserted liability for the tax, penalty, and interest. The Secretary shall use all means available to collect the tax, penalty, and interest from any property in which the dealer has a legal, equitable, or beneficial interest. The dealer may seek review of the assessment as provided in Article 9 of this Chapter.

~~(b) Reserved.~~

"§ 105-113.112. Confidentiality of information.

Notwithstanding any other provision of law, information obtained pursuant to this Article is confidential and may not be disclosed or, unless independently obtained, used in a criminal prosecution other than a prosecution for a violation of this Article. Stamps issued pursuant to this Article may not be used in a criminal prosecution other than a prosecution for a violation of this Article. A person who discloses information obtained pursuant to this Article is guilty of a Class 1 misdemeanor. This section does not prohibit the Secretary from publishing statistics that do not disclose the identity of dealers or the contents of particular returns or reports.

"§ 105-113.113. Use of tax proceeds.

The Secretary shall credit the proceeds of the tax levied by this Article to a special nonreverting account, to be called the State Controlled Substances Tax Account, until the tax proceeds are unencumbered. Tax proceeds are unencumbered when the taxpayer no longer has a current right to challenge the assessment of the tax.

The Secretary shall, on a quarterly or more frequent basis, remit the unencumbered tax proceeds as follows: seventy-five percent (75%) of the amount collected by assessment shall be remitted to the State or local law enforcement agency that conducted the investigation of a dealer that led to the assessment; and the remainder of the unencumbered tax proceeds shall be credited to the General Fund. If more than one State or local law enforcement agency conducted the investigation, the Secretary shall determine the equitable pro rata share for each agency based on the contribution each agency made to the investigation."

Sec. 2. G.S. 114-18.1 and G.S. 114-19(b) are repealed.

Sec. 3. Prosecutions for offenses committed before the effective date of this act are not abated or affected by this act, and the statutes that would be applicable but for this act remain applicable to those prosecutions.

This act does not affect the rights or liabilities of the State, a taxpayer, or another person arising under a statute amended or repealed by this act before its amendment or repeal; nor does it affect the right to any refund or credit of a tax that would otherwise have been available under the amended or repealed statute before its amendment or repeal.

Sec. 4. This act becomes effective October 1, 1995, and applies to substances acquired on or after that date.

Explanation of Proposal 2

Proposal 2 revises the excise stamp tax on controlled substances to bring it in line with a recent ruling of the United States Supreme Court. The bill would become effective October 1, 1995.

On June 6, 1994, the United States Supreme Court ruled that Montana's tax on illegal drugs was unconstitutional. In Montana v. Kurth Ranch, 114 S.Ct. 1937 (1994), the court held that the tax was in fact a punishment, not a true tax, and thus violated the Fifth Amendment's double jeopardy clause which protects against multiple punishments for the same offense. The court acknowledged that a tax is not necessarily a punishment if it is at a high rate and is designed to deter unlawful conduct; the court also acknowledged that an unlawful activity may be taxed. The court found that Montana's tax crossed the line from a tax to a punishment because, in addition to being on an illegal activity, at a high rate, and designed to deter undesirable behavior, the tax was conditioned on the commission of a crime and was exacted only after the taxpayer was arrested and the taxed drugs were no longer in the taxpayer's possession. The court based its decision on its finding that under Montana law, a taxpayer has no obligation to file a return or pay tax unless and until the taxpayer is arrested for illegal possession of the drugs. Four Justices dissented from the court's decision.

North Carolina levies an excise stamp tax on the possession of illegal drugs. The tax is at the rates of $3.50 for each gram of marijuana, $200 for each gram of any other drug sold by weight, and $400 for each 10 dosage units of any drug not sold by weight. Seventy-five percent (75%) of the tax proceeds received due to an assessment of the tax are distributed to the law enforcement agency that conducted the investigation leading to the assessment; the remaining tax proceeds are credited to the General Fund. A chart showing the amount of tax proceeds distributed to law enforcement each year is Appendix E of this report.

The Attorney General's Office reviewed the opinion in Montana v. Kurth Ranch and concluded that North Carolina's drug tax law is not unconstitutional because it differs from the Montana law in one key respect: our law applies whether or not a person is arrested for a drug violation. Our law requires a person who acquires more than a minimum amount of illegal drugs to pay the tax within 48 hours and place stamps on the drugs to show that the tax has been paid. In other respects our law is similar to Montana's: it is at similar rates, it is designed to deter undesirable behavior, and it applies only to drugs possessed in violation of the criminal law.

The Attorney General's Office and the Controlled Substance Tax Division of the Department of Revenue recommended that the Revenue Laws Study Committee consider several changes to North Carolina's drug tax law to clarify that the tax is not a punishment but is a true tax designed to raise revenue. The Study Committee adopted as Proposal 2 the following recommended changes to the current law:

--Clarify that the purpose of the tax is to raise revenue for law enforcement and for the General Fund (not to provide a second punishment).

--Revise the tax rates so that they do not, in general, exceed the market value of the various illegal drugs. A lower tax rate will apply to low-street-value drugs, which include steroids, depressants, stimulants, and hallucinogenic substances. A lower tax rate will also apply to stems and stalks of marijuana that have been separated from other parts of the plant. Separated stems and stalks are usually the debris left over from harvesting marijuana and are of much less value in this form. The failure of Montana's drug tax to provide lower tax rates for lower value drugs was a key factor in the court decision finding the tax unconstitutional.

--Provide that the tax applies to any actual or constructive possession of drugs, with an exemption for a person who is authorized by law to possess the drugs. Currently, the tax applies to anyone who possesses drugs in violation of criminal drug statutes.

--Repeal the special law that makes failure to pay the drug tax a felony. Other tax laws are covered by the general tax penalty provisions of G.S. 105-236, which criminalize only intentional conduct. The drug tax would be covered by the same penalty provisions as other tax laws if the special felony provision is repealed.

--Reduce the civil penalty for failure to pay the tax from 100% of the tax due to 50% of the tax due, so it will be the same as the penalty for failure to pay the tobacco tax. The current 100% drug tax penalty has been imposed but, as a practical matter, is virtually never collectible.

--Repeal provisions that require State and local law enforcement agencies to report drug arrests to the State Bureau of Investigation which, in turn, must report them to the Department of Revenue. These law enforcement agencies plan to continue to cooperate with the Department of Revenue on a voluntary basis.

--Repeal the tax on counterfeit controlled substances, which do not have the same value as true controlled substances.

--Clarify that the proceeds of the tax may be distributed more frequently than quarterly.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: 95-LCX-014(1.1); Proposal 2
SHORT TITLE: Revise Drug Tax
SPONSOR(S): Revenue Laws Study Committee

FISCAL IMPACT: Expenditures: Increase ( ) Decrease ( )
Revenues: Increase ( ) Decrease ( )
No Impact ( )
No Estimate Available (X)

FUND AFFECTED: General Fund (X) Highway Fund ( ) Local Govt. (X)
Other Funds ( )

BILL SUMMARY:
The proposed act makes technical and clarifying changes to the Controlled Substance tax. It clarifies that the purpose of the tax is to raise revenue for local law enforcement and for the State's General Fund, revises the tax rates, and defines to whom the tax applies. It repeals the special law that makes failure to pay the tax a felony and reduces the civil penalty for failure to pay the tax from 100% to 50% of the tax due. The provision that requires State and local law enforcement agencies to report drug arrests to the SBI is repealed. The tax on counterfeit controlled substances, which do not have the same value as true controlled substances, is repealed.

EFFECTIVE DATE: October 1, 1995

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED:
Department of Revenue Controlled Substance Tax Division

FISCAL IMPACT

	FY 95-96	FY 96-97	FY 97-98	FY 98-99	FY 99-00
REVENUES:					
GENERAL FUND	No Estimate Available				
LOCAL					

ASSUMPTIONS AND METHODOLOGY:
The Department of Revenue reports that less than 5% of assessments and collections of the tax could be affected by the changes in this proposal. If this legislation has a fiscal impact, it will be a (loss) and is expected to be small. The loss could result from no tax on counterfeit controlled substances, the reduction in rates, or the reduction in penalties.

SOURCES OF DATA:
Department of Revenue

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: H. Warren Plonk
APPROVED BY: Tom L. Covington
DATE: November 30, 1994
[FRD#001]

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

Proposal 3 (95-RB-07)
THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION

Short Title: No Sales of Loose Cigarettes. (Public)

Sponsors: Representative Braswell; Arnold, Gamble, Luebke, Ramsey, and Tallent.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO PROHIBIT THE SALE OF LOOSE, UNPACKED CIGARETTES.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-113.17 reads as rewritten:

"§ 105-113.17. Identification of ~~dispensers.~~ dispensers; sale of loose cigarettes prohibited.

(a) Dispensers. -- Each vending machine that dispenses cigarettes must be marked to identify its owner in the manner required by the Secretary.

(b) Prohibition. -- It is unlawful to sell loose, unpacked cigarettes."

Sec. 2. This act becomes effective July 1, 1995, and applies to offenses occurring on or after that date.

Explanation of Proposal 3

Proposal 3 clarifies that the sale of loose, unpacked cigarettes is prohibited by State law by expressly prohibiting these sales. The proposal does not prohibit the sale of a single cigarette, but it does require the single cigarette to be packaged. A violation of this law would be a Class 1 misdemeanor punishable by fine, by imprisonment for a term not exceeding two years, or by both, in the discretion of the court. The Department of Revenue recommended this clarification.

Under current law, the definition of package is "[t]he individual packet, can, box, or other container used to contain and to convey tobacco products to the consumer." It is the Department's interpretation that the package must be conveyed to the consumer with the tobacco products in it. However, a few retailers have removed cigarettes from their package and placed them in bowls, jars, or other containers for sale. Not only does this practice pose a health and safety concern, it also makes it difficult to determine whether or not the tax has been properly paid on these cigarettes.

Section 5723 of the Internal Revenue Code requires all tobacco products to be "put up in such packages as the Secretary shall by regulation prescribe." The official position of the Bureau of Alcohol, Tobacco, and Firearms is that the sale of loose cigarettes from bowls, jars, or other containers is not permitted under federal law.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

Proposal 4 (95-RBX-10)
THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION

Short Title: Franchise Tax on Holding Companies. (Public)

Sponsors: Representative Luebke; Arnold, Gamble, Ramsey, and Tallent.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO AMEND THE DEFINITION OF HOLDING COMPANY FOR FRANCHISE TAX PURPOSES TO PROVIDE THAT A MINOR ONE-YEAR FLUCTUATION IN INCOME DOES NOT DISQUALIFY A COMPANY AS A HOLDING COMPANY AND TO ANNUALLY ADJUST THE MAXIMUM FRANCHISE TAX ON HOLDING COMPANIES BY AN AMOUNT EQUAL TO THE PERCENTAGE INCREASE OR DECREASE IN STATE PERSONAL INCOME DURING THE MOST RECENT 12-MONTH PERIOD.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-120.2 reads as rewritten:

"**§ 105-120.2. Franchise or privilege tax on holding companies.**

(a) Every corporation, domestic and foreign, incorporated or, by an act, domesticated under the laws of this State or doing business in this State which, at the close of its taxable year is a holding company as defined in subsection (c) of this section, shall, pursuant to the provisions of G.S. 105-122:

(1) Make a report and statement, and

(2) Determine the total amount of its issued and outstanding capital stock, surplus and undivided profits, and

(3) Apportion such outstanding capital stock, surplus and undivided profits to this State.

(b) (1) Every corporation taxed under this section shall annually pay to the Secretary of Revenue, at the time the report and statement are due, a franchise or privilege tax, which is hereby levied, at the rate of one dollar and fifty cents ($1.50) per one thousand dollars ($1,000) of the amount determined under subsection (a) of this section. ~~section, but in no case shall the~~ The tax ~~be more than seventy-five thousand dollars ($75,000)~~ may not exceed the maximum tax amount determined under subsection (g) of this section nor be less than thirty-five dollars ($35.00).

(2) Notwithstanding the provisions of subdivision (1) of this subsection, if the tax produced pursuant to application of this ~~paragraph (2)~~ subdivision exceeds the tax produced pursuant to application of subdivision (1), then the tax shall be levied at the rate of one dollar and fifty cents ($1.50) per one thousand dollars ($1,000) on the greater of the amounts of

a. Fifty-five percent (55%) of the appraised value as determined for ad valorem taxation of all the real and tangible personal property in this State of each such corporation plus the total appraised value of intangible property returned for taxation of intangible personal property as computed under G.S. 105-122(d); or

b. The total actual investment in tangible property in this State of such corporation as computed under G.S. 105-122(d).

(c) For purposes of this section, a 'holding company' is ~~any~~ a corporation ~~which~~ that meets at least one of the following conditions:

(1) ~~receives~~ Received during its taxable year more than eighty percent (80%) of its gross income from corporations in which it owns directly or indirectly more than fifty percent (50%) of the outstanding voting stock.

(2) Received an average of more than eighty percent (80%) of its gross income during its taxable year and the two preceding taxable years from corporations in which it owns directly or indirectly more than fifty percent (50%) of the outstanding voting stock.

(3) Received more than eighty percent (80%) of its gross income during two of the preceding three taxable years from corporations in which it owns directly or indirectly more than fifty percent (50%) of the outstanding voting stock.

(d) Repealed by Session Laws 1985, c. 656, s. 39.

(e) Counties, cities and towns shall not levy a franchise tax on corporations taxed under this section. The tax imposed under the provisions of G.S. 105-122 shall not apply to businesses taxed under the provisions of this section.

(f) In determining the total tax payable by any holding company under this section, there shall be allowed as a credit on such tax the amount of the credit authorized under Division V of Article 4 of this Chapter.

(g) For the 1995 taxable year, the maximum tax amount is seventy-five thousand dollars ($75,000). For each subsequent taxable year, the maximum tax amount is the maximum tax amount for the preceding year, plus or minus the product of that amount and the percentage by which State personal income has increased or decreased during the most recent 12-month period for which State personal income data has been compiled by the Bureau of Economic Analysis of the United States Department of Commerce, rounded to the nearest hundred."

Sec. 2. This act is effective upon ratification and applies to taxable years beginning on or after January 1, 1995.

Explanation of Proposal 4

Proposal 4 addresses two different issues concerning the franchise tax on holding companies. First, it amends the definition of holding company to provide that a minor one-year fluctuation in income does not disqualify a company as a holding company. Second, the proposal provides that the $75,000 maximum franchise tax amount for holding companies whose tax base is determined by its capital stock, surplus, and undivided profits will be automatically adjusted annually by an amount equal to the percentage increase or decrease in State personal income during the most recent 12-month period.

Franchise Tax on Holding Companies

North Carolina imposes a series of franchise taxes upon corporations for the right or privilege to exist as a corporate entity and, in the case of foreign corporations, for the right or privilege to do business in a corporate capacity in North Carolina. The franchise tax is levied on the assets of a corporation. The tax rate is $1.50 per $1,000. The minimum franchise tax is $35. The taxable franchise tax base is the largest of the following tax bases:

(1) Capital stock, surplus, and undivided profits.

(2) 55% of appraised property tax value of all tangible property plus the value of all intangible property in North Carolina.

(3) Actual investment in tangible property in North Carolina.

In 1975, the General Assembly enacted a specific franchise tax on holding companies. Although the tax rate is the same as for corporations in general, the tax base may not be. The taxable franchise tax base for a holding company is the largest of the following tax bases:

(1) Capital stock, surplus, and undivided profits, with a maximum tax of $75,000. The maximum tax amount has not changed since its enactment in 1975.

(2) 55% of appraised property tax value of all tangible property plus the value of all intangible property in North Carolina.

(3) Actual investment in tangible property in North Carolina.

Although many holding companies pay more than $75,000 in franchise tax, those companies pay less than they would under the general franchise tax statute because under the general franchise tax statute, the company would have to pay the tax based upon its capital stock, surplus, and undivided profits with no limit on the tax amount.

Definition of Holding Company

For franchise tax purposes, a holding company is defined as "any corporation which receives during its taxable year more than eighty percent (80%) of its gross income from corporations in which it owns directly or indirectly more than fifty percent (50%) of the outstanding voting stock." In other words, it is a parent company that receives more than 80% of its gross income from its subsidiaries. Income from subsidiaries includes dividends, interest, royalties, and management fees. This proposal amends the definition so that a company may remain a holding company for franchise tax purposes, even though less than 80% of its income came from its subsidiaries in a given taxable year, if either one or both of the following conditions apply:

(1) The company received an average of more than 80% of its gross income during its taxable year and the two preceding taxable years from its subsidiaries.

(2) The company received more than 80% of its gross income during two of the preceding three taxable years from its subsidiaries.

The purpose of this proposal is to prevent minor one-year fluctuations in income from disqualifying a company as a holding company.

Maximum Franchise Tax on Holding Companies

When G.S. 105-120.2 was enacted, proponents of the law argued that corporations in a holding company ownership pattern were double taxed because the assets upon which the franchise tax base of the parent company is determined are the same assets upon which the franchise tax base of its subsidiary companies are based. To limit the impact of the perceived double taxation, the General Assembly modified the first of the three tax bases used to determine a company's franchise tax liability. A holding company's taxable franchise tax base is still the largest of the three tax bases, however, the maximum franchise tax payable under the first of the three bases, capital stock, surplus, and undivided profit, is limited to $75,000. This maximum tax amount has not increased since its enactment in 1975.

The counterpoint to this argument is that the franchise tax is levied on a corporation for the privilege of being a corporate entity. A corporation's franchise tax liability is measured by its net worth. Each corporate entity must base its net worth on the form it has chosen. If a corporate entity has chosen to be a holding company, then its net worth, by virtue of the form it has chosen, is based on the assets of its subsidiary corporations.

This proposal, much like the legislative compromise in 1975, balances both of these arguments by giving greater flexibility to holding companies in the definitional part of the statute, and by adjusting the maximum tax amount, effective for taxable years beginning on or after January 1, 1996, in an amount equal to the percentage increase or decrease in State personal income during the most recent 12-month period. The first change will decrease revenues slightly because it will allow a company to continue to be taxed as a holding company even if less than 80% of its income comes from its subsidiary companies in a given year. The second change will probably increase revenues slightly because the percentage change in personal income is almost always positive. Therefore, the tax ceiling should rise and any increase in the ceiling will increase revenues.

This proposal is effective upon ratification and applies to taxable years beginning on or after January 1, 1995.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: PROPOSAL #4
SHORT TITLE: FRANCHISE TAX ON HOLDING COMPANIES

FISCAL IMPACT: Revenues: Insignificant Impact
FUND AFFECTED: General Fund (X)

BILL SUMMARY: The State franchise tax on corporations is levied at the rate of $1.50 per $1,000 of taxable value. Taxable value is generally year-end net worth, but may be the value of the corporation's property in the State, if that value exceeds net worth. In 1975 the General Assembly enacted a law providing that the maximum tax for a holding company is $75,000, if the tax based on net worth; the tax may be greater if based on the holding company's property. A company is eligible for this holding company provision if during the taxable year it receives 80% or more of its gross income from corporations in which it has majority ownership.

The proposal amends the holding company provisions by:

(1) Preventing a holding company from being disqualified due to a minor one-year fluctuation in income.
(2) Indexing the $75,000 maximum tax in the future to the annual increase in state personal income (the income of N.C. residents). This increase would amount to approximately 6% per year.

EFFECTIVE DATE: Tax years beginning on or after January 1, 1995

METHODOLOGY: Discussions with the research staff of the Department of Revenue led to the conclusion that it is impossible to predict the number of companies affected by the "one-year fluctuation waiver". Indexing the maximum will produce a revenue gain of no more than $100,000 per year.

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: Dave Crotts
APPROVED BY:
DATE: January 4, 1995
[FRD#001]

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

Proposal 5 (95-LC-017B(1.1))
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Reduce Corporate Income Tax. (Public)

Sponsors: Representatives Luebke; Arnold, Gamble, Ramsey, and Tallent.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO REDUCE THE CORPORATE INCOME TAX.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-130.3 reads as rewritten:

"§ 105-130.3. Corporations.

A tax is imposed on the State net income of every C Corporation doing business in this ~~State at seven and seventy-five one-hundredths percent (7.75%) of the corporation's State net income.~~ State. An S Corporation is not subject to the tax levied in this section. The tax is a percentage of the taxpayer's State net income computed as follows:

State Net Income	Tax
Up to $10,000	5%
Over $10,000 up to $25,000	6%
Over $25,000	7%"

Sec. 2. G.S. 115C-546.1 reads as rewritten:

"§ 115C-546.1. Creation of Fund; administration.

(a) There is created the Public School Building Capital Fund. The Fund shall be used to assist county governments in meeting their public school building capital needs.

(b) Each calendar quarter, the Secretary of Revenue shall remit to the State Treasurer for credit to the Public School Building Capital Fund an amount equal to ~~two thirty-firsts (2/31)~~

one-fourteenth (1/14) of the net collections received during the previous quarter by the Department of Revenue under G.S. 105-130.3 minus two million five hundred thousand dollars ($2,500,000). All funds deposited in the Public School Building Capital Fund shall be invested as provided in G.S. 147-69.2 and G.S. 147-69.3.

(c) The Fund shall be administered by the Office of State Budget and Management."

Sec. 3. Section 2 of this act becomes effective October 1, 1995, and applies to remittances made on or after that date; the remainder of this act is effective for taxable years beginning on or after January 1, 1995.

Explanation of Proposal 5

Proposal 5 reduces the corporate income tax, effective beginning with the 1995 tax year. Under current law, corporations pay a flat tax of 7.75% of their State net income. Proposal 5 would create a graduated tax schedule. The rate of 5% would apply to a corporation's first $10,000 of state net income. Net income above $10,000 up to $25,000 would be taxed at 6% and net income above $25,000 would be taxed at 7%.

Until 1987, North Carolina's corporate income tax was 6% of a corporation's State net income. In 1987, as part of a tax package that included repeal of the property tax on inventories, the corporate income tax was increased to 7%. One-half of the additional 1% was dedicated to public school capital needs.

In 1991, the State faced a severe budget crisis, with an estimated shortfall of over $1 billion. As part of a legislative package that cut spending and raised revenues to make up the shortfall, the corporate income tax was increased to 7.75% and a surtax was enacted. The surtax was phased out over four years and expired January 1, 1995.

A recent study conducted by the North Carolina Business Council of Management and Development, a group of CEO's of the State's 21 largest corporations, compared the business tax burden in 12 Southeastern states. The study measured both state and local taxes as they affect different types of large businesses. The study found that North Carolina's business tax burden, taken as a whole, was below the average in the region. When viewed separately, however, North Carolina's state business taxes are significantly above average and local business taxes are well below average. North Carolina's property tax rates are quite low when compared to those in other states because North Carolina funds more local services, such as public education, with State taxes.

Although this recent study confirmed that North Carolina is a relatively low-tax state for large business, many businesses may perceive North Carolina as a high-tax state because they tend to focus more on state taxes and may be less aware of property taxes. The Revenue Laws Study Committee decided that the 1991 corporate tax increase should be repealed, returning the corporate tax rate to its pre-1991 level of 7%. In addition, the Study Committee determined that additional tax relief was appropriate for corporations with lower levels of State net income, many of which are small businesses. The Study Committee recommended that graduated rates of 5% and

6% should apply to businesses with State net income below $10,000 and $25,000, respectively. Finally, the Study Committee recommended that the amount of corporate income tax proceeds earmarked for public school capital needs should not be reduced. Proposal 5 would implement these recommendations, effective beginning with the 1995 tax year.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: PROPOSAL #5
SHORT TITLE: REDUCE CORPORATE INCOME TAX
SPONSOR(S):

FISCAL IMPACT: **Expenditures:** Increase ( ) Decrease ( )
Revenues: Increase ( ) Decrease (X)
No Impact ( )
No Estimate Available ( )

FUND AFFECTED: General Fund (X) Highway Fund ( ) Local Govt. ( )
Other Funds ( )

BILL SUMMARY: Restructures state corporate income tax rate schedule by replacing the flat 7 3/4% rate on net taxable income with the following schedule:

Net Taxable Income	Rate
First $10,000	5%
$10,000-25,000	6%
$25,000 & Over	7%

EFFECTIVE DATE: Tax years beginning on or after January 1, 1995

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED: The tax is collected by the Department of Revenue.

FISCAL IMPACT
$Million

	FY96	FY97	FY98	FY99	FY00
REVENUES:					
GENERAL FUND:					
Recurring	-$86.0	-$91.1	-$96.6	-$102.4	-$108.6
One-Time	- 41.0				

ASSUMPTIONS AND METHODOLOGY: The estimate for 1995-96 is based on an analysis of 1990 tax year returns by Department of Revenue, updated by Fiscal Research Division for projected 1995 tax year liabilities (43% increase over 1990). For future years a 6% growth rate was used (projected growth in state personal income).

TECHNICAL NOTES: The one-time impact for the 1995-96 fiscal year is due to the fact that during the 12-month period there will a full loss for the 1995 tax year as well as reduced quarterly estimated tax payments in April and June of 1996 for he 1996 tax year.

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: Dave Crotts
DATE: January 4, 1995
[FRD#001]

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

S D

Proposal 6 (95-LCX-008(1.1))
(THIS IS A DRAFT AND NOT READY FOR INTRODUCTION)

Short Title: Make Bond Taxation Uniform. (Public)

Sponsors: Senators Kerr, Cochrane, and Hoyle.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO PROVIDE UNIFORM TAX TREATMENT OF NORTH CAROLINA OBLIGATIONS AND FEDERAL OBLIGATIONS.

The General Assembly of North Carolina enacts:

Section 1. Article 1 of Chapter 53A of the General Statutes is repealed.

Sec. 2. G.S. 63A-9(1) reads as rewritten:

"(1) Bonds and notes ~~and their transfer, including any profit made on their sale,~~ are exempt from all State, county, and municipal taxation or assessment, direct or indirect, general or special, whether imposed for the purpose of general revenue or otherwise, excluding inheritance and gift ~~taxes.~~ taxes, income taxes on the gain from the transfer of bonds and notes, and franchise taxes. The interest on bonds and notes is not subject to taxation as ~~income, and the bonds and notes are not subject to taxation when constituting a part of the surplus of any bank, trust company, or other corporation.~~ income."

Sec. 3. G.S. 105-134.6 reads as rewritten:

"**§ 105-134.6. Adjustments to taxable income.**

(a) S Corporations. -- The pro rata share of each shareholder in the income attributable to the State of an S Corporation shall be adjusted as provided in G.S. 105-130.5. The pro rata share of each resident shareholder in the income not attributable to the

State of an S Corporation shall be subject to the adjustments provided in subsections (b), (c), and (d) of this section.

(b) Deductions. -- The following deductions from taxable income shall be made in calculating North Carolina taxable income, to the extent each item is included in taxable income:

(1) Interest upon the obligations of ~~(i) the United States or its possessions, (ii) this State or a political subdivision of this State, or (iii) a nonprofit educational institution organized or chartered under the laws of this State.~~ any of the following:

a. The United States or its possessions.

b. This State, a political subdivision of this State, or a commission, an authority, or another agency of this State or of a political subdivision of this State.

c. A nonprofit educational institution organized or chartered under the laws of this State.

(2) ~~Interest upon obligations and gain~~ Gain from the disposition of obligations issued before July 1, 1995, to the extent the ~~interest or~~ gain is exempt from tax under the laws of this State.

(3) Benefits received under Title II of the Social Security Act and amounts received from retirement annuities or pensions paid under the provisions of the Railroad Retirement Act of 1937.

(4) Repealed by Session Laws 1989 (Reg. Sess., 1990), c. 1002, s. 2.

(5) Refunds of state, local, and foreign income taxes included in the taxpayer's gross income.

(6) a. An amount, not to exceed four thousand dollars ($4,000), equal to the sum of the amount calculated in subparagraph b. plus the amount calculated in subparagraph c.

b. The amount calculated in this subparagraph is the amount received during the taxable year from one or more state, local, or federal government retirement plans.

c. The amount calculated in this subparagraph is the amount received during the taxable year from one or more retirement plans other than state, local, or federal government retirement plans, not to exceed a total of two thousand dollars ($2,000) in any taxable year.

d. In the case of a married couple filing a joint return where both spouses received retirement benefits during the taxable year, the maximum dollar amounts provided in this subdivision for various types of retirement benefits apply separately to each spouse's benefits.

(7) Recodified as G.S. 105-134.6(d)(1).

(8) Recodified as G.S. 105-134.6(d)(2).

(9) Income that is (i) earned or received by an enrolled member of a federally recognized Indian tribe and (ii) derived from activities on a federally recognized Indian reservation while the member resides on the reservation. Income from intangibles having a situs on the reservation and retirement income associated with activities on the reservation are considered income derived from activities on the reservation.

(10) The amount by which the basis of property under this Article exceeds the basis of the property under the Code, in the year the taxpayer disposes of the property.

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

(1) Interest upon the obligations of ~~states, other than this State, and their political subdivisions.~~ states other than this state, political subdivisions of those states, and agencies of those states and their political subdivisions.

(2) Any amount allowed as a deduction from gross income under the Code that is taxed under the Code by a separate tax other than the tax imposed in section 1 of the Code.

(3) Any amount deducted from gross income under section 164 of the Code as state, local, or foreign income tax to the extent that the taxpayer's total itemized deductions deducted under the Code for the taxable year exceed the standard deduction allowable to the taxpayer under the Code reduced by the amount by which the taxpayer's allowable standard deduction has been increased under section 63(c)(4) of the Code.

(4) The amount by which the taxpayer's standard deduction has been increased for inflation under

section 63(c)(4) of the Code and the amount by which the taxpayer's personal exemptions have been increased for inflation under section 151(d)(4)(A) of the Code. For the purpose of this subdivision, if the taxpayer's personal exemptions have been reduced by the applicable percentage under section 151(d)(3) of the Code, the amount by which the personal exemptions have been increased for inflation is also reduced by the applicable percentage.

(5) The fair market value, up to a maximum of one hundred thousand dollars ($100,000), of the donated property interest for which the taxpayer claims a credit for the taxable year under G.S. 105-151.12 and the market price of the gleaned crop for which the taxpayer claims a credit for the taxable year under G.S. 105-151.14.

(6) The amount by which the basis of property under the Code exceeds the basis of the property under this Article, in the year the taxpayer disposes of the property.

(d) Other Adjustments. -- The following adjustments to taxable income shall be made in calculating North Carolina taxable income:

(1) The amount of inheritance tax attributable to an item of income in respect of a decedent required to be included in gross income under the Code, adjusted as provided in G.S. 105-134.5, 105-134.6, and 105-134.7, may be deducted in the year the item of income is included. The amount of inheritance tax attributable to an item of income in respect of a decedent is (i) the amount by which the inheritance tax paid under Article 1 of this Chapter on property transferred to a beneficiary by a decedent exceeds the amount of inheritance tax that would have been payable by the beneficiary if the item of income in respect of a decedent had not been included in the property transferred to the beneficiary by the decedent, (ii) multiplied by a fraction, the numerator of which is the amount required to be included in gross income for the taxable year under the Code, adjusted as provided in G.S. 105-134.5, 105-134.6, and 105-134.7, and the denominator of which is the total amount of

income in respect of a decedent transferred to the beneficiary by the decedent. For an estate or trust, the deduction allowed by this subdivision shall be computed by excluding from the gross income of the estate or trust the portion, if any, of the items of income in respect of a decedent that are properly paid, credited, or to be distributed to the beneficiaries during the taxable year.

The Secretary ~~of Revenue~~ may provide to a beneficiary of an item of income in respect of a decedent any information contained on an inheritance tax return that the beneficiary needs to compute the deduction allowed by this subdivision.

(2) The taxpayer may deduct the amount by which the taxpayer's deductions allowed under the Code were reduced, and the amount of the taxpayer's deductions that were not allowed, because the taxpayer elected a federal tax credit in lieu of a deduction. This deduction is allowed only to the extent that a similar credit is not allowed by this Division for the amount."

Sec. 4. G.S. 115C-513(b) reads as rewritten:

"(b) Issuance of Bonds. -- The board of education of a merged school administrative unit may issue notes, bonds, or refunding bonds at one time or from time to time to pay the capital costs of school facilities as described in G.S. 159-48. The bonds shall be issued and maintained in accordance with the provisions of Articles 1, 4, 5A, 7, 9, 10, and 11 of Chapter 159 of the General Statutes, except as modified by this section.

The board of education of a merged school administrative unit shall call for a referendum authorizing the issuance of notes, bonds, and refunding bonds and the levy of a tax to pay amounts relating to these notes, bonds, or refunding bonds. The referendum may be called only with the consent of the boards of commissioners of both counties in which the merged school administrative unit is located. The referendum shall be held in the merged school administrative unit and only those qualified voters who reside in the unit may vote. The board of commissioners of each county shall have the referendum conducted by the board of elections of its county.

After issuance of the approved bonds, the merged school administrative unit shall make timely payments of principal and

interest on the bonds after receipt of notification of its debt service obligation pursuant to G.S. 159-35. The provisions of G.S. 159-36 govern a failure by the merged school administrative unit to levy taxes or otherwise provide for payment of the debt.

Bonds, notes, and refunding bonds issued under this section ~~and their transfer (including any profit made on the sale thereof)~~ shall be exempt from all State, county, and municipal taxation and assessment, direct or indirect, general or special, whether imposed for the purpose of general revenue or otherwise, excluding inheritance and gift ~~taxes.~~ taxes, income taxes on the gain from the transfer of bonds, notes, and refunding bonds, and franchise taxes. The interest on bonds, notes, and refunding bonds is not subject to taxation as ~~to~~ income. ~~The bonds, notes, and refunding bonds are not subject to taxation when they constitute a part of the surplus of a bank, trust company, or other corporation.~~

Article 9 of the North Carolina Uniform Commercial Code, Chapter 25 of the General Statutes, does not apply to any security interest created in connection with the issuance of bonds under this section."

Sec. 5. G.S. 115E-21 reads as rewritten:

"**§ 115E-21. Tax exemption.**

The exercise of the powers granted by this Chapter will be in all respects for the benefit of the people of the State and will promote their health and welfare, and no tax or assessment shall be levied upon any project undertaken by the agency prior to the retirement or provision for the retirement of all bonds or notes issued and obligations incurred by the agency in connection with such project.

Any bonds or notes issued by the agency under the provisions of this ~~Chapter, their transfer and the income therefrom (including any profit made on the sale thereof)~~ Chapter shall at all times be free from taxation by the State or any local unit or political subdivision or other instrumentality of the State, excepting inheritance or gift ~~taxes.~~ taxes, income taxes on the gain from the transfer of the bonds and notes, and franchise taxes. The interest on the bonds and notes is not subject to taxation as income."

Sec. 6. G.S. 116-183 reads as rewritten:

"**§ 116-183. Acceptance of grants; exemption from taxation.**

The Board is hereby authorized, subject to the approval of the Director of the Budget, to accept grants of money or materials or property of any kind for any project from a federal agency, private agency, corporation or individual, upon such terms and

conditions as such federal agency, private agency, corporation or individual may impose. The bonds issued under ~~the provisions of~~ this Article ~~and the income therefrom shall at all times be free from taxation within the State.~~ are exempt from all State, county, and municipal taxation or assessment, direct or indirect, general or special, whether imposed for the purpose of general revenue or otherwise, excluding inheritance and gift taxes, income taxes on the gain from the transfer of the bonds and notes, and franchise taxes. The interest on the bonds and notes is not subject to taxation as income."

Sec. 7. G.S. 116-196 reads as rewritten:

"**§ 116-196. Exemption from taxation; bonds eligible for investment or deposit.**

Any bonds issued under this ~~Article, including any of such bonds constituting a part of the surplus of any bank, trust company or other corporation, and the transfer of and the income from any such bonds (including any profit made on the sale thereof and all principal, interest and redemption premiums, if any)~~ Article shall at all times be exempt from all taxes or assessment, direct or indirect, general or special, whether imposed for the purpose of general revenue or otherwise, which are levied or assessed by the State or by any county, political subdivision, agency or other instrumentality of the ~~State.~~ State, excluding inheritance and gift taxes, income taxes on the gain from the transfer of the bonds, and franchise taxes. The interest on the bonds is not subject to taxation as income. Bonds issued by the Board under the provisions of this Article are hereby made securities in which all public officers and public bodies of the State and its political subdivisions, all insurance companies, trust companies, banking associations, investment companies, executors, administrators, trustees and other fiduciaries may properly and legally invest funds, including capital in their control or belonging to them. Such bonds are hereby made securities which may properly and legally be deposited with and received by any State or municipal officer or any agency or political subdivision of the State for any purpose for which the deposit of bonds or obligations of the State is now or may hereafter be authorized by law."

Sec. 8. G.S. 116-198.39 reads as rewritten:

"**§ 116-198.39. Bonds are exempt from taxation.**

Any bonds issued under this ~~Article, including any of such bonds constituting a part of the surplus of any bank, trust company, or other corporation, and the transfer of and the income from any such bonds (including any profit made on the sale~~

~~thereof and all principal, interest, and redemption premiums, if any)~~ Article shall at all times be exempt from all taxes or assessment, direct or indirect, general or special, whether imposed for the purpose of general revenue or otherwise, which are levied or assessed by the State or by any county, political subdivision, agency, or other instrumentality of the ~~State.~~ State, excluding inheritance and gift taxes, income taxes on the gain from the transfer of the bonds, and franchise taxes. The interest on the bonds is not subject to taxation as income. Bonds issued by the Board under the provisions of this Article are hereby made securities in which all public officers and public bodies of the State and its political subdivisions, all insurance companies, trust companies, banking associations, investment companies, executors, administrators, trustees, and other fiduciaries may properly and legally invest funds, including capital in their control or belonging to them. Such bonds are hereby made securities which may properly and legally be deposited with and received by any State or municipal officer or any agency or political subdivision of the State for any purpose for which the deposit of bonds or obligations of the State is now or may hereafter be authorized by law."

Sec. 9. G.S. 116-209.13 reads as rewritten:

"**§ 116-209.13. Tax exemption.**

The exercise of the powers granted by this Article in all respects will be for the benefit of the people of the State, for their well-being and prosperity and for the improvement of their social and economic conditions, and the Authority shall not be required to pay any taxes on any property owned by the Authority under the provisions of this Article or upon the income therefrom, and the bonds issued under the provisions of this ~~Article, their transfer and the income therefrom (including any profit made on the sale thereof),~~ Article shall at all times be free from taxation by the State or any local unit or political subdivision or other instrumentality of the State, excepting inheritance or gift ~~taxes.~~ taxes, income taxes on the gain from the transfer of the bonds, and franchise taxes. The interest on the bonds is not subject to taxation as income."

Sec. 10. G.S. 122A-19 reads as rewritten:

"**§ 122A-19. Tax exemption.**

The exercise of the powers granted by this Chapter will be in all respects for the benefit of the people of the State, for their well-being and prosperity and for the improvement of their social and economic conditions, and the Agency shall not be required to pay any tax or assessment on any property owned by

the Agency under the provisions of this Chapter or upon the income therefrom.

Any obligations issued by the Agency under the provisions of this ~~Chapter, their transfer and the income therefrom (including any profit made on the sale thereof),~~ Chapter shall at all times be free from taxation by the State or any local unit or political subdivision or other instrumentality of the State, excepting inheritance or gift ~~taxes.~~ taxes, income taxes on the gain from the transfer of the obligations, and franchise taxes. The interest on the obligations is not subject to taxation as income."

Sec. 11. G.S. 122D-14 reads as rewritten:

"**§ 122D-14. Exemption from taxes.**

The exercise of the powers granted by this Chapter will be in all respects for the benefit of the people of the State, for their well-being and prosperity and for the improvement of their social and economic conditions, and the Authority shall not be required to pay any tax or assessment on any property owned by the Authority under the provisions of this Chapter or upon the income therefrom.

Any obligations issued by the Authority under the provisions of this ~~Chapter, their transfer and the income therefrom (including any profit made on the sale thereof),~~ Chapter shall at all times be free from taxation by the State or any local unit or political subdivision or other instrumentality of the State, excepting inheritance or gift ~~taxes.~~ taxes, income taxes on the gain from the transfer of the obligations, and franchise taxes. The interest on the obligations is not subject to taxation as income."

Sec. 12. G.S. 131A-21 reads as rewritten:

"**§ 131A-21. Tax exemption.**

The exercise of the powers granted by this Chapter will be in all respects for the benefit of the people of the State and will promote their health and welfare, and no tax or assessment shall be levied upon any health care facilities undertaken by the Commission prior to the retirement or provision for the retirement of all bonds or notes issued and obligations incurred by the Commission in connection with such health care facilities.

Any bonds or notes issued by the Commission under the provisions of this ~~Chapter, their transfer and the income therefrom (including any profit made on the sale thereof)~~ Chapter shall at all times be free from taxation by the State or any local unit or political subdivision or other instrumentality of the State, excepting inheritance or gift ~~taxes.~~ taxes, income

taxes on the gain from the transfer of the bonds and notes, and franchise taxes. The interest on the bonds and notes is not subject to taxation as income."

Sec. 13. G.S. 131E-28(c) reads as rewritten:

"(c) Bonds, notes, debentures, or other evidences of indebtedness of a hospital authority issued under the Local Government Revenue Bond Act, Chapter 159 of the General Statutes, Article 5, or issued pursuant to the bond and revenue anticipation provisions of Chapter 159 of the General Statutes, Article 9, or issued pursuant to G.S. 131E-26(b) or contracted pursuant to G.S. 131E-32 ~~and the transfer of and income from such instruments, including profits on sales,~~ shall at all times be free from taxation by the State or any of its subdivisions, except for inheritance or gift ~~taxes.~~ taxes, income taxes on the gain from the transfer of the instruments, and franchise taxes. The interest on the instruments is not subject to taxation as income."

Sec. 14. G.S. 142-12 reads as rewritten:

"**§142-12. State bonds exempt from taxation.**

~~The original bonds or certificates of debt of the State, which have been issued since the first day of January, 1853, or which may hereafter be issued under the authority of any act whatever, as likewise the bonds and certificates substituted for such original bonds and certificates, shall be, they and the interest accruing thereon, exempt from taxation.~~ Bonds and other evidences of indebtedness issued by the State are exempt from taxation by the State or any of its subdivisions, except for inheritance or gift taxes, income taxes on the gain from the transfer of the instruments, and franchise taxes. The interest on the instruments is not subject to taxation as income."

Sec. 15. G.S. 142-29.6(f) reads as rewritten:

"(f) All refunding ~~obligations, coupons (if any) and any evidences of additional interest appertaining thereto, and their transfer (including any profit made on the sale thereof),~~ obligations shall be exempt from all State, county and municipal taxation or assessment, direct or indirect, general or special, whether imposed for the purpose of general revenue or otherwise, ~~including~~ except for inheritance and gift taxes, income taxes on the gain from the transfer of the obligations, and franchise taxes. The interest on the refunding obligations is not subject to taxation as income. ~~and the interest on the refunding obligations shall not be subject to taxation as to income, nor shall the refunding obligations or coupons (if any) or evidences of additional indebtedness be subject to taxation when~~

~~constituting a part of the surplus of any bank, trust company or other corporation.~~"

Sec. 16. G.S. 143B-456(g) reads as rewritten:

"(g) Any obligations issued by the Authority under the provisions of this ~~Part, their transfer and the income therefrom (including any profit made on the sale thereof),~~ Part shall at all times be free from taxation by the State or any local unit or political subdivision or other instrumentality of the State, excepting inheritance or gift ~~taxes.~~ taxes, income taxes on the gain from the transfer of the obligations, and franchise taxes. The interest on the obligations is not subject to taxation as income."

Sec. 17. G.S. 157-26 reads as rewritten:

"**§ 157-26. Tax exemptions.**

An authority is a local government agency and is exempt from taxation to the same extent as a unit of local government. Property owned by an authority is exempt from taxation in accordance with Article V, § 2 of the North Carolina Constitution. Bonds and other obligations issued by an authority or its corporate agent authorized by this Article to exercise its powers ~~The authority shall be exempt from the payment of any taxes or fees to the State or any subdivision thereof, or to any officer or employee of the State or any subdivision thereof. The property of an authority used for public purposes shall be exempt from all local and municipal taxes and for the purposes of such tax exemption, it is hereby declared as a matter of legislative determination that an authority is and shall be deemed to be a municipal corporation. Bonds, notes, debentures and other evidences of indebtedness of an authority (including any corporate agent thereof authorized by this Article to exercise the powers of the authority) heretofore or hereafter issued~~ are declared to be issued for a public purpose and to be public ~~instrumentalities and, together with the interest thereon, shall be exempt from taxes.~~ instrumentalities. These obligations are exempt from all State, county, and municipal taxation or assessment, direct or indirect, general or special, whether imposed for the purpose of general revenue or otherwise, excluding inheritance and gift taxes, income taxes on the gain from the transfer of the obligations, and franchise taxes. The interest on the obligations is not subject to taxation as income."

Sec. 18. G.S. 159B-26 reads as rewritten:

"**§ 159B-26. Tax exemption.**

~~Bonds, their transfer and the income therefrom (including any profit made on the sale thereof),~~ Bonds shall at all times be free from taxation by the State or any political subdivision or any ~~agency of either thereof,~~ of their agencies, excepting inheritance or gift ~~taxes.~~ taxes, income taxes on the gain from the transfer of the bonds, and franchise taxes. The interest on the bonds is not subject to taxation as income."

Sec. 19. G.S. 159I-23 reads as rewritten:

"**§ 159I-23. Tax exemption.**

All of the bonds and notes authorized by this ~~Chapter and the coupons, if any, appertaining thereto, and their transfer (including any profit made on the sale thereof),~~ Chapter shall be exempt from all State, county, and municipal taxation or assessment, direct or indirect, general or special, whether imposed for the purpose of general revenue or otherwise, excluding inheritance and gift ~~taxes.~~ taxes, income taxes on the gain from the transfer of the bonds and notes, and franchise taxes. The interest on the bonds and notes shall not be subject to taxation as ~~to income, nor shall the bonds, notes, and coupons, if any, be subject to taxation when constituting a part of the surplus of any bank, trust company, or other corporation.~~ income."

Sec. 20. G.S. 160A-516(b) reads as rewritten:

"(b) Neither the commissioners of a commission nor any person executing the bonds shall be liable personally on the bonds by reason of the issuance ~~thereof.~~ of the bonds. The bonds and other obligations of the commission (and ~~such~~ the bonds and obligations shall so state on their face) shall not be a debt of the municipality, the county, or the State and neither the municipality, the county, nor the State shall be liable ~~thereon,~~ on the bonds, nor in any event shall ~~such~~ the bonds or obligations be payable out of any funds or properties other than those of ~~said~~ the commission acquired for the purpose of this Article. The bonds shall not constitute an indebtedness of the municipality within the meaning of any constitutional or statutory debt limitation or restriction. Bonds of a commission are declared to be issued for an essential public and governmental purpose and to be public ~~instrumentalities and, together with interest thereon and income therefrom, shall be exempt from all taxes.~~ instrumentalities. The bonds are exempt from all State, county, and municipal taxation or assessment, direct or indirect, general or special, whether imposed for the purpose of general revenue or otherwise, excluding inheritance and gift taxes, income taxes on the gain from the transfer of the

bonds and notes, and franchise taxes. The interest on the bonds is not subject to taxation as income. Bonds may be issued by a commission under this Article notwithstanding any debt or other limitation prescribed in any statute. This Article without reference to other statutes of the State shall constitute full and complete authority for the authorization and issuance of bonds by the commission ~~hereunder~~ under this Article and ~~such~~ this authorization and issuance shall not be subject to any conditions, ~~restrictions~~ restrictions, or limitations imposed by any other statute whether general, ~~special~~ special, or local, except as provided in subsection (d) of this section."

Sec. 21. This act becomes effective July 1, 1995, and applies to obligations issued on or after that date.

Explanation of Proposal 6

Proposal 6 changes the State tax treatment of capital gains on a select group of State and local bonds. It would apply to bonds issued on or after July 1, 1995.

The interest earned on federal bonds is exempt from State income tax, as is the interest earned on North Carolina State and local bonds. If the holder of a bond transfers it, there may be a capital gain. Gain from the transfer of federal bonds is subject to State income tax. Gain from the transfer of most North Carolina State and local bonds is also subject to State income tax. There are some State and local bonds, however, for which the bond law provides a State income tax exemption for gain from their transfer.

The Attorney General's Office has notified the Department of Revenue, the State Treasurer, and the Revenue Laws Study Committee that allowing a tax exemption for gain from some North Carolina bonds but not for gain from federal bonds may violate the constitutional doctrine of intergovernmental tax immunity. In order to avoid constitutional problems, the State must treat federal and North Carolina bonds alike.

To achieve uniform tax treatment for bonds, the General Assembly could either repeal the special capital gain exemption that applies to a limited number of bonds, or grant a tax exemption for capital gains from all federal bonds and all North Carolina State and local bonds. The former option will cause a revenue increase that is expected to be small for three reasons: (1) there are relatively few bonds affected, (2) North Carolina bonds are not generally traded for capital gains, and (3) some bondholders are probably not aware of the tax exemption and are not currently claiming it. Exempting the capital gain from all bonds will cause a General Fund revenue loss that is expected to be of greater magnitude because it would involve a much larger group of State and local bonds as well as all federal bonds. The amount of the potential loss to the General Fund is unknown due to a lack of data.

The Revenue Laws Study Committee considered these options and recommended Proposal 6, which would repeal the special capital gain exemption that applies to a select group of North Carolina State and local bonds and make technical changes. The bill also clarifies that bonds are not exempt from franchise tax or inheritance and gift tax; some bond statutes are ambiguous on this point, but the statutes have not been interpreted as granting a special exemption from these taxes. The bill would apply to

bonds issued on or after July 1, 1995; it would not affect outstanding bonds. The bill is not expected to affect the marketability of future bonds.

Sections 2, 4 - 13, and 15 - 20 of Proposal 6 repeal the capital gains tax exemption for the following bonds:

--Bonds of the Global TransPark Authority, a State agency

--Bonds of the Nash-Edgecombe merged school administrative unit

--Revenue bonds of the Higher Education Facilities Finance Agency, a State agency

--Revenue bonds of The University of North Carolina system

--Revenue bonds of the State Education Assistance Authority, a State agency

--Bonds of the N.C. Housing Finance Agency, a State agency

--Bonds of the N.C. Agricultural Finance Authority, a State agency

--Bonds of the N.C. Medical Care Commission, a State agency

--Revenue bonds of public hospital authorities created by local governments

--Refunding bonds issued by the State

--Bonds of the N.C. State Ports Authority, a State agency

--Bonds of local government housing authorities

--Bonds issued by municipalities or joint municipal power agencies to finance electrical power projects

--Special obligation bonds issued for solid waste capital projects by local governments or by the N.C. Solid Waste Management Capital Projects Agency, a State agency

--Bonds issued by local government housing agencies

Section 3 of the bill revises the individual income tax law to reflect that interest on federal and North Carolina bonds is tax-exempt but gain on these bonds is taxable, except for certain North Carolina bonds issued before July 1, 1995.

Section 1 of the bill repeals a 1955 law authorizing the creation of business development corporations and allowing them to issue bonds. This law has never been used and is now obsolete. Section 14 of the bill clarifies that gain from the transfer of State bonds is not exempt from State income tax. Section 21 of the bill provides that it applies to bonds issued on or after July 1, 1995.

NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: Proposal 6
SHORT TITLE: Make Bond Taxation Uniform
SPONSOR(S): Revenue Laws Study Commission

FISCAL IMPACT: **Expenditures:** Increase ( ) Decrease ( )
Revenues: Increase (X) Decrease ( )
No Impact ( )
No Estimate Available (X)

FUND AFFECTED: General Fund (x) Highway Fund ( ) Local Govt. ( )
Other Funds ( )

BILL SUMMARY:
The proposed act repeals the capital gains exemption for a select group of North Carolina and local bonds and makes technical changes to the statutes. The 1955 law authorizing the creation of business development corporations and allowing them to issue bonds is repealed. The act clarifies that gains from the transfer of State bonds is not exempt from State income tax

The following bonds are affected:
1. Bonds of the Global TransPark Authority
2. Bonds of the Nash-Edgecombe merged school administrative unit
3. Revenue bonds of the Higher Education Facilities Finance Agency
4. Revenue bonds of the University of North Carolina system
5. Revenue bonds of the State Education Assistance Authority
6. Bonds of the North Carolina Housing Finance Agency
7. Bonds of the North Carolina Agriculture Finance Authority
8. Bonds of the North Carolina Medical Care Commission
9. Revenue bonds of the public hospital authorities created by local governments
10. Refunding bonds issued by the State
11. Bonds of the North Carolina Ports Authority
12. Bonds of local government housing authority
13. Bonds issued by municipalities or joint municipal power agencies
14. Special obligation bonds issued for solid waste capital projects by local governments or by the North Carolina Solid Waste Management Capital Projects Agency
15. Bonds Issued by local Government housing agencies

EFFECTIVE DATE: Applies to obligations issued on or after July 1, 1995

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED:
Department of Revenue Personal Income Tax Division

ESTIMATE
FISCAL IMPACT

	FY 95-96	FY 96-97	FY 97-98	FY 98-99	FY 99-00
REVENUES:					
GENERAL FUND	No Estimate Available				

ASSUMPTIONS AND METHODOLOGY:
The revenue bonds and other indebtedness of State authorities and institutions as of June 30, 1994 was $9.7 billion.

In an attempt to estimate the fiscal impact of the proposed legislation an analyst at CDA Bulls Eye in Maryland was consulted. The company attempted to determine a variable by which an estimate could be made from the amount of capital gains tax collected annually in the State. (CDA Bulls Eye tracks bond ownership.) After the initial conversation the representative has not been forthcoming with the information. However, the prevailing investment philosophy is to purchase these products and hold them until maturity.

SOURCES OF DATA:
Department of State Treasurer
CDA Bulls Eye, Maryland

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: H. Warren Plonk
APPROVED BY: Tom C. Covington
DATE: November 16, 1994
[FRD#001]

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

Proposal 7 (95-LC-021(1.1))
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Repeal Obsolete Use Tax. (Public)

Sponsors: Representatives Tallent, Arnold, Gamble, Luebke, and Ramsey.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO REPEAL THE SPECIAL USE TAX ON CONSTRUCTION EQUIPMENT BROUGHT INTO THE STATE.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-164.6(g) is repealed.

Sec. 2. This act does not affect the rights or liabilities of the State, a taxpayer, or another person arising under a statute repealed by this act before its repeal; nor does it affect the right to any refund or credit of a tax that would otherwise have been available under the repealed statute before its repeal.

Sec. 3. This act becomes effective July 1, 1995.

Explanation of Proposal 7

Proposal 7 repeals a special use tax that is obsolete and generates almost no revenue. The bill would become effective July 1, 1995.

In 1957, the General Assembly levied a special use tax on machinery, tools, and other equipment brought into North Carolina for use in construction. The tax is computed by multiplying the sales price of each item of equipment by the percentage of the equipment's useful life it is expected to be used in North Carolina, applying the 4% tax, and subtracting a credit for the proportional amount of sales taxes paid on each item in another state. Until 1989, there was no credit for taxes paid to another state; accordingly, the tax operated as a protectionist measure to give North Carolina construction companies a competitive advantage over companies from other states.

In 1989, the Revenue Laws Study Committee determined that without a credit for taxes paid in another state, the special use tax violated the federal constitution's interstate commerce clause. In addition, the committee found that retaliatory laws in neighboring states created a burden on North Carolina companies seeking to do construction business in those states. In accordance with the committee's recommendation, the 1989 General Assembly enacted the use tax credit for sales taxes paid to other states.

Since enactment of the credit in 1989, this special use tax has generated little revenue. It is extremely complex for taxpayers to comply with and for the Department of Revenue to administer. Each piece of equipment must be listed separately, along with its original purchase price, the amount of sales tax paid when it was purchased, the state to which the tax was paid, the equipment's estimated useful life, and the period of time the equipment is expected to be in North Carolina. After the tax is calculated, most of it is offset by the credit for taxes paid on other states. Accordingly, the tax no longer either generates revenue or provides protection to North Carolina companies. As the tax is now obsolete, the Revenue Laws Study Committee determined that repeal is appropriate.

Of our neighboring states, Virginia and South Carolina have similar use taxes but North Carolina companies do not have to pay these taxes because they receive credit for the sales taxes they have paid in North Carolina on the equipment. Repeal of North Carolina's use tax will not affect North Carolina companies doing business in

South Carolina and Virginia; they will continue to receive credit for North Carolina sales taxes paid.

NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: Proposal 7
SHORT TITLE: Construction Use Tax
SPONSOR(S): Revenue Laws Study Commission

FISCAL IMPACT: **Expenditures:** Increase ( ) Decrease ( )
Revenues: Increase ( ) Decrease (X)
No Impact ( )
No Estimate Available ( )

FUND AFFECTED: **General Fund (X) Highway Fund ( ) Local Fund ( )**
Other Fund ( )

BILL SUMMARY:
The proposed act repeals G.S. 105-164.6(g), the special use tax on construction equipment brought into the State of North Carolina.

EFFECTIVE DATE: July 1, 1995

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED:
Department of Revenue Sales and Use Tax Division

FISCAL IMPACT

	FY 95-96	FY 96-97	FY 97-98	FY 98-99	FY 99-00
REVENUES					
General Fund	($10,000 to $20,000) Loss				

ASSUMPTIONS AND METHODOLOGY:
The Department of Revenue Sales and Use Tax Division reports the loss is small due to the credit allowed for sales taxes paid to other states. The credit was enacted in 1989, as a recommendation by the Revenue Laws Study Commission.

SOURCES OF DATA:
Department of Revenue Sales and Use Tax Division

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: H. Warren Plonk
APPROVED BY: Tom C. Covington
DATE: November 7, 1994
[FRD#002]

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

S D

Proposal 8 (95-RB-01)
THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION

Short Title: No Sales Tax on Donated Items. (Public)

Sponsors: Senator Cochrane; Hoyle and Kerr.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO EXEMPT FROM SALES AND USE TAX TANGIBLE PERSONAL PROPERTY THAT IS MANUFACTURED OR PURCHASED FOR RESALE BY A WHOLESALE MERCHANT OR A RETAILER AND THEN DONATED TO A NONPROFIT ORGANIZATION TO BE USED FOR A CHARITABLE PURPOSE.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-164.13 is amended by adding a new subdivision to read:

"(42) Tangible personal property that is purchased by a retailer for resale or is manufactured or purchased by a wholesale merchant for resale and then withdrawn from inventory and donated by the retailer or wholesale merchant to a nonprofit organization to be used for a charitable purpose."

Sec. 2. G.S. 105-164.13 (13a) and (31b) are repealed.

Sec. 3. This act is effective upon ratification.

Explanation of Proposal 8

Proposal 8 creates a new sales and use tax exemption for tangible personal property that is donated to a nonprofit organization by a retailer or a wholesale merchant. Under current law, medicine and certain food donated to a nonprofit organization to be used for a charitable purpose are exempt from sales and use tax. This proposal repeals these two exemptions since they become redundant in light of the new, and broader, exemption created by this proposal.

Under current law, a wholesale merchant or retailer who donates products to a nonprofit organization instead of selling them is liable for the sales and use tax. A wholesale merchant or retailer does not pay sales or use taxes when purchasing the products or the ingredients used to manufacture the products because the products are to be resold. Sales and use taxes do not apply to property purchased for resale or ingredients purchased to manufacture products for resale. If the wholesale merchant or retailer chooses not to sell the goods, the wholesale merchant or retailer becomes liable for use tax on the goods because the resale exemption no longer applies. This is true no matter what the company chooses to do with the products. Section 1 of this proposal eliminates this liability for use tax by providing a specific exemption for tangible personal property purchased or manufactured by a wholesale merchant or retailer for resale and then withdrawn from inventory and donated to a nonprofit organization to be used for a charitable purpose.

The General Assembly enacted a law exempting food that is acquired at wholesale and then donated to a nonprofit organization in 1992. That year, it also enacted a law exempting from sales and use tax prescription and nonprescription drugs donated to a nonprofit organization. Section 2 of this proposal repeals these two exemptions because they are part of the more inclusive exemptions created by this proposal.

This proposal becomes effective upon ratification.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: Proposal 8
SHORT TITLE: Donated Property Use Tax
SPONSOR(S): Revenue Laws Study Committee

FISCAL IMPACT: Expenditures: Increase ( ) Decrease ( )
Revenues: Increase ( ) Decrease (X)
No Impact ( )
No Estimate Available ( )

FUND AFFECTED: General Fund (X) Highway Fund ( ) Local Govt. (X)
Other Funds ( )

BILL SUMMARY:
The proposed act creates a new sales and use tax exemption for tangible personal property that is donated to a nonprofit organization by a retailer or a wholesale merchant. Under current law, medicine and certain food donated to a nonprofit organization to be used for a charitable purpose are exempt from sales and use tax. This act broadens the exemption to include anything taken from inventory and donated to a nonprofit organization.

EFFECTIVE DATE: Upon ratification

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED:
Department of Revenue Sales and Use Tax Division

FISCAL IMPACT

	FY 95-96	FY 96-97	FY 97-98	FY 98-99	FY 99-00
REVENUES:					
GENERAL FUND	($600,000) loss annually				

ASSUMPTIONS AND METHODOLOGY:
Estimate prepared by the Department of Revenue

SOURCES OF DATA:
Department of Revenue Sales and Use Tax Division

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: H. Warren Plonk
APPROVED BY: Tom L. Covington
DATE: September 15, 1994
[FRD#001]

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H **D**

Proposal 9 (95-RB-03)
THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION

Short Title: Tax Free Samples of Prescription Drugs. (Public)

Sponsors: Representative Gamble; Arnold, Luebke, Ramsey, and Tallent.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO EXEMPT FROM SALES AND USE TAX FREE SAMPLES OF PRESCRIPTION DRUGS DISTRIBUTED BY THE MANUFACTURER.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-164.13 is amended by adding a new subdivision to read:

"(13b) Prescription drugs distributed free of charge by the manufacturer."

Sec. 2. This act is effective upon ratification.

Explanation of Proposal 9

Proposal 9 creates a new sales and use tax exemption for prescription drugs that are distributed free of charge by the manufacturer. The sale of drugs bought with a prescription has been exempt from sales tax since 1937.

Under current law, a pharmaceutical manufacturer is liable for use tax on free samples of prescription drugs distributed to physicians, dentists, and veterinarians. The use tax, first enacted in 1939, is the complement of the State's sales tax and is imposed on the storage, use, or consumption in this State of tangible personal property. A pharmaceutical manufacturer is not liable for sales or use taxes when it purchases the ingredients used to manufacture drugs because the products are to be resold. Sales and use taxes do not apply to property purchased for resale or ingredients purchased to manufacture products for resale. However, when the manufacturer chooses to give the drug samples away rather than sell them, the manufacturer becomes liable for the use tax on the drugs.

The free distribution of prescription drugs by physicians is not subject to tax because the taxable use of the samples occurred prior to their distribution by the physician when the manufacturer provided the drugs to its salespersons. Hospitals and other purchasers of drugs without a prescription will still be subject to the sales and use tax. Nonprofit hospitals are entitled to a refund of any sales and use taxes paid under G.S. 105-164.14(b). The proposal becomes effective upon ratification.

This proposal does not attempt to regulate the practice of prescription drug sample distribution. However, the Revenue Laws Study Committee spent considerable time discussing the potential abuses associated with drug sample distribution. The Committee learned that Congress adopted the Prescription Drug Marketing Act of 1987 and the Prescription Drug Amendments of 1992. The Act prohibits the sale, purchase, or trade, or the offer to sell, purchase, or trade of a drug sample. The prohibition applies to physicians as well as to distributors.

The Act establishes a strict system of controls over the distribution of prescription drug samples. Only a manufacturer or an authorized distributor of record may distribute prescription drug samples. The distributor may only distribute drug samples in accordance with specific requirements, which include:

* A written request from a licensed practitioner on a form containing certain information including the signature of the practitioner making the request. The act defines "licensed practitioner" as a person licensed by State law to prescribe drugs.
* A written receipt by the recipient upon delivery of a drug sample by mail or common carrier. The Federal Drug Administration has tentatively concluded that this requirement should extend to all drug sample deliveries.
* A complete and accurate inventory, conducted annually, of all drug samples in the possession of representatives of a manufacturer or distributor.
* A legal responsibility to investigate and report any alleged abuses to the appropriate government authority, such as falsified drug sample requests, receipts, or records.
* Civil penalties of up to $1 million for violations of the Act.

North Carolina law also limits the distribution of prescription drug samples to practitioners who request the samples in writing. A written request is required for each distribution and must contain the name and address of the supplier and the requester and the name and quantity of the specific drug requested. The manufacturer must keep a record of the distribution for at least two years.

The Act does not impose restrictions on the distribution of prescription samples by licensed practitioners to their patients. The day-to-day operations of licensed practitioners, including the provision of prescription drugs to patients, are regulated primarily by the states. Our State's laws do not specifically address the provision of sample prescription drugs to patients. The Board of Medical Examiners can revoke the license of a practitioner if a licensee exhibits unprofessional conduct, fails to conform to the ethics of the medical profession, or commits any act contrary to honesty, justice, or good morals.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: Proposal 9
SHORT TITLE: Prescription Drug Sample Use Tax
SPONSOR(S): Revenue Laws Study Committee

FISCAL IMPACT: Expenditures: Increase ( ) Decrease ( )
Revenues: Increase ( ) Decrease (X)

FUND AFFECTED: General Fund (X) Highway Fund ( ) Local Govt. (X)

BILL SUMMARY:
The proposed act creates a new sales and use tax exemption for prescription drugs that are distributed free of charge within the State by the manufacturer or by a physician, dentist, or veterinarian.

EFFECTIVE DATE: Upon Ratification

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED:
Department of Revenue Sales and Use Tax Division

ESTIMATE
FISCAL IMPACT

	FY 95-96	FY 96-97	FY 97-98	FY 98-99	FY 99-00
REVENUES:					
GENERAL FUND	Loss at least ($400,000) annually				

ASSUMPTIONS AND METHODOLOGY:
The Department of Revenue Sales and Use Tax Division reports that, between 1987 and 1992, audits were conducted on seven separate drug manufacturers producing in the State. The audits revealed an amount equal to $273,955 in assessed sales and use taxes paid on both prescription and non-prescription samples. Assuming the producers are similar in practice the average sales tax liability per taxpayer was $39,000 a year.

Currently, the State hosts 10 facilities producing pharmaceutical products. If $39,000 portrays the average sales and use tax liability of a single producer in the state industry, then on average the total sales and use tax liability from the distribution of free prescription and non-prescription drugs from in State producers should not exceed $400,000 in a tax year.

The estimate is based on available data for North Carolina producers and does not take into account the fiscal impact associated with producers located outside the State who send drug "samples" to physicians practicing in the State.

SOURCES OF DATA:
Department of Revenue Sales and Use Tax Division

FISCAL RESEARCH DIVISION 733-4910
PREPARED BY: H. Warren Plonk
APPROVED BY: Tom L. Covington
DATE: November 10, 1994

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H/S D

Proposal 10 (95-LCX-040(1.1))
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Repeal Intangibles Tax. (Public)

Sponsors: Representatives Arnold and Ramsey (Co-Sponsors); Gamble, Luebke, and Tallent.
Senator Hoyle; and Kerr.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO REPEAL THE INTANGIBLES TAX EFFECTIVE WITH THE 1994 TAX YEAR, TO DISTRIBUTE REVENUE TO COUNTIES AND CITIES FOR PUBLIC SCHOOLS AND INFRASTRUCTURE, AND TO REPEAL EXISTING INCOME TAX PREFERENCES FOR NORTH CAROLINA DIVIDENDS.

The General Assembly of North Carolina enacts:

Section 1. (a) Effective January 1, 1995, G.S. 105-213.1 is recodified as G.S. 105-275.2 and G.S. 105-213 is repealed.

(b) Effective January 1, 1994, the remainder of Article 7 of Chapter 105 of the General Statutes is repealed. Any taxes collected pursuant to Article 7 of Chapter 105 of the General Statutes on or after the date the Article is repealed shall remain in the General Fund and any refunds made on or after the date the Article is repealed of taxes collected pursuant to that Article shall be charged to the General Fund. The Secretary shall retain from collections under Division II of Article 4 of Chapter 105 of the General Statutes the cost for the 1994-95 fiscal year of collecting, administering, and refunding the taxes levied in Article 7 of Chapter 105 of the General Statutes.

Sec. 2. G.S. 105-275 is amended by adding the following new subdivisions:

"(31a) Accounts receivable.
(31b) Bonds, notes, and other evidences of debt.
(31c) Shares of stock, including shares and units of ownership of mutual funds, investment trusts, and investment funds.
(31d) The beneficial or equitable interest in a trust, trust fund, or trust account, including custodial accounts, held by a foreign fiduciary."

Sec. 3. G.S. 105-213.1, as recodified as G.S. 105-275.2 by Section 1 of this act, reads as rewritten:

"**§ 105-275.2. Reimbursement to counties and municipalities for ~~partial~~ repeal of State tax on intangible personal property.**

(a) Reimbursement for Repeal of Tax on Money on Deposit, Money on Hand, and Funds on Deposit with Insurance Companies. -- On or before August 30 of each year, the Secretary of Revenue shall allocate for distribution to each county and the municipalities in the county the amount allocated to the county under this subsection in 1990.

~~Amounts allocated to a county under this subsection shall in turn be divided and distributed between the county and the municipalities located in the county in accordance with the method of allocating intangible tax revenue between a county and the municipalities located in the county provided in G.S. 105-213.~~

(a1) Reimbursement for Partial Repeal of Tax on Accounts Receivable. -- On or before August 30 of each year, the Secretary of Revenue shall distribute to counties and municipalities an amount equal to forty percent (40%) of the tax collected on accounts receivable under former Article 7 of this Chapter (repealed) during the 1989-90 fiscal year. ~~The Secretary of Revenue shall first allocate the amount to be distributed in this subsection to the counties in the same manner as the amount allocated in G.S. 105-213. The amount allocated to each county shall in turn be divided and distributed between the county and the municipalities located in the county in accordance with the method of allocating intangible tax revenue between a county and the municipalities located in the county provided in G.S. 105-213.~~ The Secretary shall allocate this amount among the counties in proportion to the amount allocated to each county under former G.S. 105-213 (repealed) in August 1994.

(a2) Distribution Between County and its Municipalities. -- The amounts allocated to each county under subsections (a) and (a1) of this section shall be divided and distributed to the county and the municipalities in the county in proportion to the total

amount of ad valorem taxes levied by each during the fiscal year preceding the distribution. In dividing these amounts between each county and its municipalities, the Secretary of Revenue shall treat taxes levied by a merged school administrative unit described in G.S. 115C-513 in a part of the unit located in a county as taxes levied by the county in which that part is located. Funds distributed under this subsection shall be drawn from collections received under Division II of Article 4 of this Chapter.

For the purpose of computing the distribution to any county and the municipalities located in the county for any year with respect to which the property valuation of a public service company is the subject of an appeal and the Department of Revenue is restrained by law from certifying the valuation to the county and the municipalities in the county, the Department shall use the last property valuation of the public service company that has been certified.

The chair of each board of county commissioners and the mayor of each municipality shall report to the Secretary of Revenue information requested by the Secretary to enable the Secretary to allocate the amount distributed by this subsection. If a county or municipality fails to make a requested report within the time allowed, the Secretary may disregard the county or municipality in allocating the amount distributed by this section.

(b) Restrictions on Use. -- ~~Amounts distributed to a county or a municipality under this section are subject to the same restrictions as amounts distributed under G.S. 105-213.~~ The amount distributed to each county and municipality pursuant to subsection (a2) of this section shall be used by the county or municipality in proportion to property tax levies made by it for the various funds and activities of the county or municipality, unless the county or municipality has pledged the amount to be distributed to it under this section in payment of a loan agreement with the North Carolina Solid Waste Management Capital Projects Financing Agency. A county or municipality that has pledged amounts distributed under this section in payment of a loan agreement with the Agency may apply the amount the loan agreement requires.

~~(c) Municipality Defined. -- As used in this section, the term 'municipality' has the same meaning as in G.S. 105-213.~~

~~(d) Source. -- Funds distributed under this section shall be drawn from collections received under Division II of Article 4 of this Chapter.~~

(e) Reimbursement to Counties for Repeal of Tax on Accounts Receivable, Bonds, Stocks, and Foreign Trust Interests. -- There is annually appropriated from the General Fund to the Public School Building Capital Fund created in G.S. 115C-546.1 the county distribution amount determined under this subsection. For the 1995-96 fiscal year, the county distribution amount is one hundred three percent (103%) of the amount distributed to counties in August 1994 under former G.S. 105-213 (repealed). Each fiscal year thereafter, the county distribution amount is one hundred three percent (103%) of the amount appropriated under this subsection the preceding fiscal year. The appropriation shall be distributed by August 30 of each year. The appropriation shall be included in the Current Operations Appropriations Act.

(f) Reimbursement to Municipalities for Repeal of Tax on Accounts Receivable, Bonds, Stocks, and Foreign Trust Interests. -- There is annually appropriated from the General Fund to municipalities the municipality distribution amount determined under this subsection. For the 1995-96 fiscal year, the municipality distribution amount is one hundred three percent (103%) of the amount distributed to municipalities in August 1994 under former G.S. 105-213 (repealed). Each fiscal year thereafter, the municipality distribution amount is one hundred three percent (103%) of the amount appropriated under this subsection the preceding fiscal year. The appropriation shall be included in the Current Operations Appropriations Act.

The appropriation shall be distributed among the municipalities of the State each year on a per capita basis. In making the per capita distributions under this subsection, the Secretary shall use the most recent annual population estimates certified by the State Planning Officer. The appropriation shall be distributed by August 30 of each year.

A municipality may use the funds distributed to it under this subsection only for capital outlay for public facilities and infrastructure or to retire any indebtedness incurred by the municipality for this purpose."

Sec. 4. G.S. 105-501 reads as rewritten:

"**§ 105-501. Distribution of additional taxes.**

The Secretary shall, on a quarterly basis, allocate the net proceeds of the additional one-half percent (1/2%) sales and use taxes levied under this Article to the taxing counties on a per capita basis according to the most recent annual population estimates certified to the Secretary by the State Budget Officer. The Secretary shall then adjust the amount allocated to each

county as provided in G.S. 105-486(b). The amount allocated to each taxing county shall then be divided among the county and the municipalities located in the county in accordance with the method by which the one percent (1%) sales and use taxes levied in that county pursuant to Article 39 of this Chapter or Chapter 1096 of the 1967 Session Laws are distributed.

If any taxes levied under this Article by a county have not been collected in that county for a full quarter because of the levy or repeal of the taxes, the Secretary shall distribute a pro rata share to that county for that quarter based on the number of months the taxes were collected in that county during the quarter.

In determining the net proceeds of the tax to be distributed, the Secretary shall deduct from the collections to be allocated an amount equal to one-fourth of the costs during the preceding fiscal year of:

(1) The Department of Revenue in performing the duties imposed by Article 15 of this Chapter.

(2) The Property Tax Commission.

(3) The Institute of Government in operating a training program in property tax appraisal and assessment.

(4) The personnel and operations provided by the Department of State Treasurer for the Local Government Commission."

Sec. 5. G.S. 105-288(d) reads as rewritten:

"(d) Expenses. -- The members of the Property Tax Commission shall receive travel and subsistence expenses in accordance with G.S. 138-5 and a salary of two hundred dollars ($200.00) a day when hearing cases. The Secretary of Revenue shall supply all the clerical and other services required by the Commission. All expenses of the Commission and the Department of Revenue in performing the duties enumerated in this Article shall be paid ~~from funds appropriated out of revenue derived from the tax on intangible personal property as provided by G.S. 105-213.~~ as provided in G.S. 105-501."

Sec. 6. G.S. 105-276 reads as rewritten:

"**§ 105-276. Taxation of intangible personal property.**

Intangible personal property that is not excluded from taxation under G.S. ~~105-275(31) or classified under Schedule H, G.S. 105-198 through G.S. 105-217,~~ 105-275 is subject to this Subchapter. ~~The classification of such property for taxation under Schedule H shall not exclude the property from the system property valuation of public service companies under Article 23~~

~~provided proper adjustments are made to prevent duplicate taxation.~~ "

Sec. 7. G.S. 105-282.1(a)(2) reads as rewritten:

"(2) Owners of the special classes of property excluded from taxation under G.S. 105-275(5), (15), (16), (26), (31), (31a), (31b), (31c), (31d), (32a), (33), (34), or (40), or exempted under G.S. 105-278.2 are not required to file applications for the exclusion or exemption of that property."

Sec. 8. G.S. 105-305 reads as rewritten:

"**§ 105-305. Place for listing intangible personal property.**

(a) Listing Instructions. -- This section ~~shall apply~~ applies to all taxable intangible personal property that has a tax situs in this ~~State, that~~ State and is not required by this Subchapter to be appraised originally by the Department of ~~Revenue, and that is not subject to taxation under the provisions of Schedule H, G.S. 105-198 through 105-217.~~ Revenue. The place in this State at which ~~such~~ this property is taxable shall be determined ~~according to the rules prescribed in subsections (b) through (e), below.~~ as provided in this section. The person whose duty it is to list property shall list it in the county in which the place of taxation is located, indicating on the abstract the information required by G.S. 105-309(d). If the place of taxation lies within a city or town that requires separate listing under G.S. 105-326(a), the person whose duty it is to list shall also list the property for taxation in the city or town.

(b) General Rule. -- Except as otherwise provided in subsections (c) through ~~(e), below,~~ (e) of this section, intangible personal property shall be taxable at the residence of the owner. For the purposes of this section:

(1) The residence of a person who has two or more places in this State at which ~~he~~ the person occasionally dwells shall be the place ~~at which he~~ the person dwelt for the longest period of time during the calendar year immediately preceding the date as of which property is to be listed for taxation.

(2) The residence of a domestic or foreign taxpayer other than an individual person shall be the place at which its principal North Carolina office is located.

(c) Intangible personal property representing an interest or interests in real property that is situated in this State shall

be taxable in the place in which the represented real property is located.

(d) The intangible personal property of a decedent whose estate is in the process of administration or has not been distributed shall be taxable in the place at which it would be taxable if the decedent were still alive and still residing in the place at which ~~he~~ the decedent resided at the time of ~~his~~ death.

(e) Intangible personal property within the jurisdiction of the State held by a resident or nonresident trustee, guardian, or other fiduciary having legal title to the property shall be taxable in accordance with the following rules:

(1) If ~~any~~ a beneficiary is a resident of the State, an amount representing ~~his~~ the beneficiary's portion of the property shall be taxable in the place at which it would be taxable if ~~he~~ the beneficiary were the owner of ~~his~~ that portion.

(2) If ~~any~~ a beneficiary is a nonresident of the State, an amount representing ~~his~~ the beneficiary's portion of the property shall be taxable in the place at which it would be taxable if the fiduciary were the beneficial owner of the property."

Sec. 9. G.S. 108A-93 reads as rewritten:

"**§ 108A-93. Withholding of State moneys from counties failing to pay public assistance costs.**

The Director of the Budget ~~is authorized to~~ may withhold from any county that does not pay its full share of public assistance costs to the State and has not ~~arranged for payment pursuant to G.S. 108-54.1 or~~ obtained a loan for repayment under G.S. 108A-89, any State moneys appropriated from the General Fund for public assistance and related administrative costs, or ~~to~~ may direct the Secretary of Revenue and State ~~Treasurer~~ Controller to withhold any tax owed to a county under ~~Article 7 of Chapter 105 of the General Statutes,~~ G.S. 105-113.82, ~~Article 39 of Chapter 105 of the General Statutes~~ Subchapter VIII of Chapter 105 of the General Statutes, or Chapter 1096 of the Session Laws of 1967. The Director of the Budget shall notify the ~~chairman~~ chair of the board of county commissioners of the proposed action prior to the withholding of funds."

Sec. 10. G.S. 142-12.1(c) reads as rewritten:

"(c) The interest on any ~~such~~ of these bonds or obligations shall maintain its existing exemption from State income taxation, or other taxation, if any, ~~including, but not limited to, the tax on intangible personal property now imposed by the State,~~

notwithstanding that ~~such~~ the interest may be or become subject to federal income taxation as a result of legislative action by the federal government."

Sec. 11. G.S. 105-151.19 is repealed.

Sec. 12. G.S. 105-130.7 reads as rewritten:

"§ 105-130.7. Deductible portion of dividends.

Dividends from stock issued by ~~any~~ a corporation ~~shall be deducted to the extent herein provided.~~ are deductible to the extent provided in this section.

~~(1) As soon as may be practicable after September 30 of each year, the Secretary of Revenue shall determine from the corporate income tax return filed during the year ending September 30 by each corporation required to file a return during that period the proportion of the entire net income or loss of the corporation allocable to this State under the provisions of G.S. 105-130.4, except as provided herein. If a corporation has a net income in North Carolina and a net loss from all sources wherever located, or if a corporation has a net loss in North Carolina and a net income from all sources wherever located, the Secretary shall require the use of the allocation fraction determined under the provisions of G.S. 105-130.4. A corporation which is a stockholder in any such corporation shall be allowed to deduct the same proportion of the dividends received by it from such corporation during its income year ending on or after September 30. No deduction shall be allowed for any part of any dividend received from any corporation that was required to file an income tax return during the year ending September 30 but failed to file the return. In the case of dividends received from a corporation that was not required to file a return during the year ending September 30, the proportion of dividends deductible by the stockholder shall be determined by the Secretary from the best information available.~~

~~(2) Dividends received by a corporation from stock in any insurance company of this State taxed under the provisions of G.S. 105-228.5 shall be deductible by such corporation, and a proportionate part of any dividends received from stock in any foreign insurance corporation shall be deductible, such~~

~~part to be determined on the basis of the ratio of premiums reported for taxation in this State to total premiums collected both in and out of this State.~~

(3) A corporation shall be allowed to deduct such proportionate part of dividends received by it from a regulated investment company or a real estate investment trust, as defined in G.S. 105-130.12, as represents and corresponds to income received by such regulated investment company or real estate investment trust which would not be taxed by this State if received directly by the corporation.

(3a) Dividends received on shares of capital stock owned in a stock-owned savings and loan association taxed under Article 8D of this Chapter shall be deductible.

(4) Notwithstanding ~~the provisions of subdivisions (1) through (3a)~~ any other provision of this section, a corporation ~~which, at the close of its taxable year, has its commercial domicile within North Carolina shall be allowed to~~ may deduct all dividends received from corporations in which it owns more than fifty percent (50%) of the outstanding voting stock.

(5) Notwithstanding any other provisions of this Division, a corporation ~~which~~ that is a shareholder in a holding company ~~shall be allowed as a deduction~~ may deduct an amount equal to those dividends received by it from ~~such~~ the holding company, multiplied by a fraction, the numerator of which ~~shall be~~ is the dividends received by ~~such~~ the holding company ~~attributable to North Carolina,~~ that are deductible by it under subdivisions (3) and (3a) of this section and the denominator of which ~~shall be~~ is the gross dividends received by ~~such~~ the holding company. ~~company; provided, however, that no deduction shall be allowed where the fraction is smaller than one-third (1/3). For purposes of this section, 'dividends attributable to North Carolina' shall be the amount of dividend income received by the holding company on stock owned in other corporations equal to the total of the proportion of each of such corporation's dividends as shall be determined deductible by the~~

~~Secretary under subdivisions (1) through (3a) of this section; provided that a~~ A holding company ~~which~~ that owns more than fifty percent (50%) of the outstanding voting stock of one or more holding companies as defined in this subdivision ~~shall be permitted~~ is allowed a deduction for all dividends received from ~~such~~ those holding companies and all other corporations in which it owns more than fifty percent (50%) of the outstanding voting stock. ~~stock except that no deduction shall be allowed if less than one-third (1/3) of the dividends received by the holding company are attributable to North Carolina. A shareholder of such a holding company shall determine the deductible portion of its dividends received from such holding company as hereinabove provided except that the amounts received from a subsidiary holding company as 'dividends attributable to North Carolina' shall be determined as though the subsidiary corporation of the subsidiary holding company had paid the dividends directly to the parent holding company. For the purposes of this section and unless the context clearly requires a different meaning,~~ As used in this section, the term 'holding company' ~~shall mean any~~ means a corporation subject to the tax imposed by G.S. 105-130.3 whose ordinary gross income consists of fifty percent (50%) or more of dividend income received from corporations in which it owns more than fifty percent (50%) of the outstanding voting ~~stock, and 'subsidiary' shall mean any corporation, more than fifty percent (50%) of whose outstanding voting stock is owned by another corporation. For the purposes of this subsection,~~ stock. As used in this subdivision, the term 'dividend' includes, in addition to corporate dividends, distributions received from a partnership by a corporation owning more than a fifty percent (50%) interest in the partnership.

(6) In no case shall the total amount of dividends that are allowed as a deduction to a corporation as a result of the application of subdivisions ~~(1) through~~ (3) and (3a) of this section be in excess of fifteen thousand dollars ($15,000) for the taxable year."

Sec. 13. Notwithstanding the provisions of G.S. 105-163.15 and G.S. 105-163.41, no addition to tax shall be made under those sections for a taxable year beginning on or after January 1, 1995, and before January 1, 1996, with respect to any underpayment to the extent the underpayment was created or increased by Section 11 or 12 of this act.

Sec. 14. Section 1(a) of this act becomes effective January 1, 1995. Section 1(b) of this act is effective retroactively for taxable years beginning on or after January 1, 1994. Section 3 of this act becomes effective January 1, 1995. Sections 4, 5, and 9 of this act become effective July 1, 1995, and apply to distributions made on or after that date. Sections 11, 12, and 13 of this act are effective for taxable years beginning on or after January 1, 1995. The remainder of this act is effective retroactively for taxable years beginning on or after January 1, 1994.

This act does not affect the rights or liabilities of the State, a taxpayer, or another person arising under a statute amended or repealed by this act before its amendment or repeal; nor does it affect the right to any refund or credit of a tax that would otherwise have been available under the amended or repealed statute before its amendment or repeal.

Explanation of Proposal 10

This proposal would repeal the intangibles tax, provide for annual appropriations to local governments to make up for their resulting revenue loss, and repeal existing income tax preferences for North Carolina dividends. The intangibles tax repeal would become effective retroactively to the 1994 tax year, the local government distributions would begin in August 1995, and the income tax changes would become effective in the 1995 tax year.

North Carolina levies an intangibles tax of 25¢ per $100 market value of stock and shares in mutual funds. The tax on stock is one part of the intangibles tax; the other parts are the taxes on bonds and accounts receivable. The stock tax statute exempts a proportion of corporate stock equal to the percentage of the corporation's business that is conducted in North Carolina. Thus, stock of a corporation that does 100% of its business in North Carolina is 100% exempt from the intangibles tax. This exemption is known as the "taxable percentage" deduction.

The North Carolina Court of Appeals ruled in June 1993 that the taxable percentage deduction violates the interstate commerce clause of the federal constitution. In Fulton Corp. v. Justus, 110 N.C.App. 493, 430 S.E.2d 494 (1993), the court invalidated the taxable percentage deduction beginning with the 1994 tax year (tax due April 15, 1995). This ruling was overturned by the North Carolina Supreme Court on December 9, 1994. The Supreme Court ruled that the taxable percentage deduction is not unconstitutional.

The plaintiffs will ask the United States Supreme Court to review the decision of the North Carolina Supreme Court. If the United States Supreme Court agrees to hear the case, it could agree that the taxable percentage deduction is constitutional, rule that the taxable percentage deduction is unconstitutional, or declare the entire tax on stock invalid. Many months could pass before the United States Supreme Court issued a ruling.

The elimination of the taxable percentage deduction ordered by the court of appeals would have subjected all stock in North Carolina companies to tax, resulting in a gain to the General Fund of approximately $55 to $75 million annually. If the United States Supreme Court invalidates the entire stock tax, the General Fund would be reduced by about $90 million annually and refunds would have to be paid to taxpayers who filed under protest in 1994 and 1995.

The Revenue Laws Study Committee determined that the intangibles tax should be repealed for several reasons. First, many consider it an unfair tax because, unlike tangible property, intangible property does not require local government services and thus should not be subject to tax. Second, many also believe the tax has a negative effect on economic development, causing corporate executives, retirees, and wealthy individuals to leave the State or to decide against moving into the State. Third, if the United States Supreme Court overturns the North Carolina Supreme Court's decision and agrees with the court of appeals that the taxable percentage deduction is invalid, the result would be a tax increase for many taxpayers, particularly individuals who own small, in-State businesses.

The Revenue Laws Study Committee determined that there should be some reimbursement to local governments for the revenue loss resulting from repeal of the tax, but that State taxes should not be increased to pay for the reimbursement. The Study Committee found that a "hold harmless" distribution from the General Fund to local governments would not be equitable because it would have the effect of transferring money from poorer counties to more prosperous counties. The Study Committee chose to redistribute the county money on a per average daily membership basis (ADM) and require counties to use it only for public school capital outlay purposes. Similarly, the bill would distribute the city money on a per capita basis and require cities to use it only for capital outlay for public facilities and infrastructure.

A section by section analysis of Proposal 10 follows:

Section	Explanation
1	Repeals the tax on intangible personal property effective retroactively to the 1994 tax year, so that no returns will be due in April 1995 or thereafter. The distribution of intangibles tax revenue made to local governments in August 1994 for the 1994-95 fiscal year will be the last; this distribution will be replaced by an annual appropriation to counties and cities beginning in August 1995, as outlined in Section 3. The existing reimbursement for previously repealed parts of the tax is not repealed but is recodified as G.S. 105-275.2. These reimbursements will continue to be made in August of each year.
2	Continues the exemption from local ad valorem tax for those items of intangible property subject to the intangibles tax repealed by the bill: accounts receivable, bonds and notes, stocks and mutual funds, and

Section	Explanation
	beneficial interests in foreign trusts. These items will now be subject to neither intangibles tax nor local property tax.
3	Makes technical changes to the existing reimbursement for local governments and provides two new reimbursements for the repeal of the remainder of the tax. Beginning in August 1995, there will be an annual appropriation to the Public School Building Capital Fund. Money in this fund is allocated quarterly to counties on a per average daily membership basis and may be used only for public school capital outlay projects. Beginning in August 1995, there will also be an annual appropriation distributed among cities on a per capita basis. Cities may use these funds only for capital outlay for public facilities and infrastructure. The amounts appropriated to counties and cities in 1995 will be 103% of the amounts of intangibles tax revenue distributed to counties and cities, respectively, in 1994. Each year thereafter, the appropriations will grow by 3%.
4	Provides that the costs of the Property Tax Commission, the Department of Revenue in performing property tax duties, the Institute of Government in providing property tax training, and the Local Government Commission, will be deducted from local sales tax revenues that are distributed to local governments. These costs currently are deducted from intangibles tax distributions. The 93-94 fiscal year expenses were deducted from intangibles taxes in August 1994. The deduction for 94-95 fiscal year expenses will be made quarterly from local sales tax distributions beginning in July 1995.
5	Makes a conforming change to reflect the change in Section 4.
6 - 10	Make conforming changes to reflect that the intangibles tax has been repealed.
11	Repeals G.S. 105-151.19, the individual income tax credit for North Carolina dividends, effective beginning with the 1995 tax year. This statute allows an individual to take a credit equal to 6% of the individual's dividends received from corporations that do at least 50% of their business in this State. The maximum credit is $300.00 per year. This tax preference for North Carolina dividends is similar to the intangibles tax deduction that was struck down by the North Carolina Court of Appeals because it violates the interstate commerce clause of the federal constitution.

Section	Explanation
12	Repeals the corporate income tax deduction for North Carolina dividends, effective beginning with the 1995 tax year. A corporation is allowed to deduct a percentage of the dividends its receives from corporations in proportion to the percentage of business those corporations do in North Carolina. This tax preference for North Carolina dividends is similar to the intangibles tax deduction that was struck down by the North Carolina Court of Appeals because it violates the interstate commerce clause of the federal constitution.
13	Provides that there will be no penalty for underpayment of estimated income tax for the 1995 tax year to the extent the underpayment was caused by the repeal of preferences for North Carolina dividends for the 1995 tax year.
14	Provides the effective dates of the act.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: PROPOSAL #10
SHORT TITLE: REPEAL INTANGIBLES TAX

FISCAL IMPACT: **Expenditures:** Increase ( ) Decrease (X)
Revenues: Increase (X) Decrease (X)
No Impact ( )
No Estimate Available ( )

FUND AFFECTED: General Fund (X) Highway Fund ( ) Local Govt. (X)
Other Funds ( )

BILL SUMMARY: (1) Repeals intangibles tax and provides for annual appropriations to local government units to replace revenue loss. The reimbursement to county government units would be based on public school enrollment and the reimbursement to cities would be allocated on a population basis. The reimbursement would grow at the rate of 3% per year.

(2) Repeals personal income tax credit for dividends received by taxpayers that are associated with the North Carolina operations of companies located in the state and the corporate income tax exclusion for the same type of dividends.

EFFECTIVE DATE: The intangibles tax repeal becomes effective retroactive to the 1994 tax year (December 31, 1994 valuation of assets). This tax is due April 15 of each year. The elimination of the N.C. dividend exclusion is effective beginning with the 1995 tax year.

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED: Both taxes are collected by the Department of Revenue.

FISCAL IMPACT: See Attachment.
FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: DAVE CROTTS
DATE: JANUARY 4, 1995
[FRD#001]

FISCAL IMPACT OF PROPOSAL # 10

	FY 95	FY 96	($ MIL.) FY 97	FY 98	FY 99
STATE GENERAL FUND:					
Intangibles Tax Repeal*	-125.1	-128.4	-131.3	-134.2	-137.3
Eliminate Dividend Credit/Exclusion	-	+16.9	+17.8	+18.9	+20.9
Net State Impact	-125.1	-111.5	-113.5	-115.3	-116.4
LOCAL GOVERNMENT:					
Intangibles Tax Repeal	-	+3.9**	-2.9	-9.7	-15.3
Collection Cost Elimination	-	+1.8	+1.9	+2.0	+2.1
Net Local Cost	-	+5.7	-1.0	-7.7	-13.1

* Loss is offset by use of 3% growth in reimbursing local units in lieu of actual collection growth under current law.

** Loss for this year is due to local units receiving 3% growth in reimbursement, being versus a small decline under current law. The decline is due to a projected drop in intangibles tax collections for 1995-96 (falling stock prices).

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

Proposal 11 (95-LJX-2)
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Transporter Plate/Salvage Changes. (Public)

Sponsors: Representatives Arnold, Gamble, Luebke, Ramsey, and Tallent.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO ALLOW SPECIAL MOBILE EQUIPMENT DEALERS TO USE TRANSPORTER PLATES ON THE EQUIPMENT IN CERTAIN CIRCUMSTANCES AND TO PROVIDE A HIGHWAY USE TAX EXEMPTION AND A REDUCED TITLE FEE FOR THE TRANSFER OF A WRECKED MOTOR VEHICLE FROM AN INSURANCE COMPANY TO THE PERSON WHO OWNED THE VEHICLE WHEN IT WAS WRECKED.

The General Assembly of North Carolina enacts:

Section 1. G.S. 20-79.2(a) reads as rewritten:

"(a) Who Can Get a Plate. -- A person engaged in a business requiring the limited operation of a motor vehicle for any of the following purposes may obtain a transporter plate authorizing the movement of the vehicle for the specific purpose:

(1) To facilitate the manufacture, construction, rebuilding, or delivery of new or used truck cabs or bodies between manufacturer, dealer, seller, or purchaser.

(2) To repossess a motor vehicle.

(3) To pick up a motor vehicle that is to be repaired or otherwise prepared for sale by a dealer, to road-test the vehicle, if it is repaired, within a 10-mile radius of the place where it is repaired, and to deliver the vehicle to the dealer.

(4) To move a motor vehicle that is owned by a public utility, as defined in G.S. 62-3(23)a, and is a replaced vehicle offered for sale.

(5) To take a motor vehicle either to or from a motor vehicle auction where the vehicle will be or was offered for sale.

(6) To road-test a repaired truck whose GVWR is at least 15,000 pounds when the test is performed within a 10-mile radius of the place where the truck was repaired and the truck is owned by a person who has a fleet of at least five trucks whose GVWRs are at least 15,000 pounds and who maintains the place where the truck was repaired.

(7) To move a mobile office, a mobile classroom, or a mobile or manufactured home.

(8) To drive a motor vehicle that is at least 25 years old to and from a parade or another public event and to drive the motor vehicle in that event. A person who owns a motor vehicle that is at least 25 years old is considered to be in the business of collecting those vehicles.

(9) To drive a motor vehicle that is part of the inventory of a dealer to and from a motor vehicle trade show or exhibition or to, during, and from a parade in which the motor vehicle is used.

(10) To drive special mobile equipment in any of the following circumstances:

a. From the manufacturer of the equipment to a facility of a dealer.

b. From one facility of a dealer to another facility of a dealer.

c. From a dealer to the person who buys the equipment from the dealer."

Sec. 2. G.S. 105-187.6(a) reads as rewritten:

"(a) Full Exemptions. -- The tax imposed by this Article does not apply when a certificate of title is issued as the result of a transfer of a motor vehicle:

(1) To the insurer of the motor vehicle under G.S. 20-109.1 because the vehicle is a salvage vehicle.

(1a) By an insurer to a person who was required by G.S. 20-109.1 to transfer the vehicle to the insurer because the vehicle was a salvage vehicle.

(2) To either a manufacturer, as defined in G.S. 20-286, or a motor vehicle retailer for the purpose of resale.
(3) To the same owner to reflect a change or correction in the owner's name.
(4) By will or intestacy.
(5) By a gift between a husband and wife, a parent and child, or a stepparent and a stepchild.
(6) By a distribution of marital property as a result of a divorce.
(7) To a handicapped person from the Department of Human Resources after the vehicle has been equipped by the Department for use by the handicapped.
(8) To a local board of education for use in the driver education program of a public school when the motor vehicle is transferred:
a. By a retailer and is to be transferred back to the retailer within 300 days after the transfer to the local board.
b. By a local board of education."

Sec. 3. G.S. 20-85 reads as rewritten:

"§ 20-85. Schedule of fees.

(a) The following fees are imposed concerning a certificate of title, a registration card, or a registration plate for a motor vehicle. These fees are payable to the Division and are in addition to the tax imposed by Article 5A of Chapter 105 of the General Statutes.

(1)	Each application for certificate of title	$35.00
(2)	Each application for duplicate or corrected certificate of title	10.00
(3)	Each application of repossessor for certificate of title	10.00
(4)	Each transfer of registration	10.00
(5)	Each set of replacement registration plates	10.00
(6)	Each application for duplicate registration card	10.00
(7)	Each application for recording supplementary lien	10.00
(8)	Each application for removing a lien from a certificate of title	10.00
(9)	Each application for certificate of title for a motor vehicle transferred to a manufacturer,	

as defined in G.S. 20-286, or a motor vehicle retailer for the purpose of resale..... ~~10.00.~~ 10.00

(10) Each application by an insurer for a salvage certificate of title..... 10.00

(11) Each application for reissuance of a certificate of title for a salvage vehicle made by the person who owned the vehicle when its title was transferred to its insurer... 10.00.

(b) Thirty-one dollars and fifty cents ($31.50) of each title fee collected under subdivision (a)(1) of this section and all of the fees collected under ~~the other~~ subdivisions ~~in subsection (a)~~ (a)(2) through (a)(9) of this section shall be credited to the North Carolina Highway Trust ~~Fund; the~~ Fund. The remaining three dollars and fifty cents ($3.50) of the title fee collected under subdivision (a)(1) and the fees collected under subdivisions (a)(10) and (a)(11) shall be credited to the Highway Fund. Fifteen dollars ($15.00) of each title fee credited to the Trust Fund under subdivision (a)(1) shall be added to the amount allocated for secondary roads under G.S. 136-176 and used in accordance with G.S. 136-44.5."

Sec. 4. G.S. 20-109.1(e) reads as rewritten:

"(e) ~~The Commissioner shall charge a fee of ten dollars ($10.00) for issuing a title or forms as required by this section.~~ G.S. 20-85 sets the fee for issuing a salvage certificate of title and for reissuing a certificate of title for a rebuilt salvage vehicle."

Sec. 5. Sections 2, 3, and 4 of this act become effective July 1, 1995. The remaining sections of this act are effective upon ratification.

Explanation of Proposal 11

This proposal makes two changes to the motor vehicle laws. First, it allows a dealer of special mobile equipment to use transporter plates on the equipment in three circumstances. Second, it provides a highway use tax exemption and a reduced title fee for the transfer of a salvage vehicle when the transfer is from an insurance company to the person who owned the vehicle when it became a salvage vehicle. The transporter plate change is effective upon ratification and the salvage vehicle changes become effective July 1, 1995. Section 1 of the proposal makes the transporter plate change and Sections 2 through 4 make the salvage vehicle changes.

Transporter Plate Change

Section 1 of the proposal allows a dealer of special mobile equipment to use a transporter plate on the equipment in the following three circumstances: to drive the equipment from its manufacturer to the dealer's place of business, to drive the equipment from one facility of the dealer to another, and to drive the equipment from the dealer's facility to the buyer of the equipment. Under current law, a special mobile equipment dealer must use a dealer plate in these circumstances. Under the proposal, the special mobile equipment dealer could use either a dealer plate or a transporter plate in these circumstances.

A transporter plate is a type of commercial license plate. It bears the letters TP followed by numbers and letters and is printed in the same color as other commerical plates. A transporter plate is issued on a calendar-year basis, can only be used for a purpose that is listed in the statutes, and can be transferred from one vehicle to another during the year as long as the vehicle to which it is transferred is driven for one of the authorized business purposes. It differs from a dealer plate in its restrictions on use. A vehicle bearing a dealer plate can be driven for any purpose as long as the driver is an officer or an employee of the dealer.

Special mobile equipment is a class of vehicles; the class consists of vehicles that have permanently attached special equipment whose purpose is to perform off-road work. Truck cranes and well-drilling rigs are two types of special mobile equipment. Special mobile equipment is driven on the roads only to get to off-road jobs. It is

subject to sales tax rather than highway use tax and pays a flat annual registration fee of $20 rather than a fee based on weight.

A person who sells special mobile equipment is a dealer in vehicles and must have a dealer's license. As a dealer, that person is eligible for dealer license plates. The number of dealer license plates a dealer can obtain is based on the number of vehicles the dealer sold the previous year. For example, a dealer who sold fewer than 12 vehicles the previous year is entitled to one dealer plate, a dealer who sold at least 12 but less than 25 is entitled to four, a dealer who sold at least 25 but less than 37 is entitled to five, and a dealer who sold at least 37 but less than 49 is entitled to six. These restrictions were enacted by the 1993 General Assembly on the recommendation of the Revenue Laws Study Committee.

A dealer in special mobile equipment may sell fewer than 12 pieces of special mobile equipment in a year and may therefore be eligible for only one dealer plate. Mr. Marion Hodges of J.W. Burress, Inc., which sells special mobile equipment, told the Committee that one dealer plate is not enough to conduct business. He explained that his company may need a dealer plate to drive a piece of special mobile equipment from the manufacturer to one of the company's places of business in this State and may simultaneously need a dealer plate to drive a different piece of special mobile equipment to a person who bought the equipment from the company. He asked the Committee to consider allowing special mobile equipment dealers to use transporter plates rather than dealer plates.

The Committee considered the request and decided that allowing special mobile equipment dealers to use transporter plates in the limited circumstances described in the proposal is a reasonable accommodation to the unintended impact of the 1993 dealer plate revisions on special mobile equipment dealers. The revisions were intended to curb abuses in the use of dealer plates and were not intended to hamper dealers of any type in conducting business.

Salvage Vehicle Changes

Sections 2 through 4 of the proposal exempt certain transfers of salvage vehicles from the highway use tax and reduce the title fee for these transfers from $35 to $10. The vehicle transfers affected are those made by an insurance company to the person who owned the vehicle when it became a salvage vehicle and, consequently, had to be transferred to the insurance company.

Under current law, the title to a vehicle must be transferred to the company that insures it when the company pays a claim on the vehicle that exceeds 75% of the fair market value of the vehicle, as determined by the National Automobile Dealers' Association Pricing Guide Book or another pricing guide approved by the Commissioner of Motor Vehicles. A vehicle on which a 75% claim has been paid is considered a salvage vehicle.

The owners of some salvage vehicles want to keep the vehicles and repair them. An owner of a salvage vehicle, however, must transfer the title to the vehicle to the vehicle's insurer. The insurer can then transfer the title to the vehicle back to the owner, but when it does so, the transfer is subject to highway use tax and a $35 title fee. The highway use tax is 3% of the retail value of the vehicle, subject to a minimum tax of $40 and, for automobiles, a maximum tax of $1,500. In contrast, the transfer of a salvage vehicle to its insurer is exempt from the highway use tax and is subject to a title fee of only $10.

The committee received a complaint from a taxpayer who had to transfer a salvage vehicle to its insurer, against his wishes, and then had to pay highway use tax and the $35 fee to get the vehicle back. The committee reviewed the law on this topic in response to this complaint and learned from the Director of Vehicle Registration of the Division of Motor Vehicles of the Department of Transportation that the requirement to pay highway use tax on the transfer of a salvage vehicle from an insurer to the original owner of the vehicle is among the top three complaints the Division receives about the highway use tax.

After reviewing the topic, the committee decided to adopt this proposal. The committee concluded that a transfer of a salvage vehicle from its insurer to the person who owned it when it became a salvage vehicle should be treated the same as the transfer of the vehicle from the owner to the insurance company. Thus, the transfer should be exempt from the highway use tax and should be subject to a $10 title fee instead of the regular $35 title fee.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: Proposal 11
SHORT TITLE: Transporter Plate/Salvage Changes
SPONSOR(S):

FISCAL IMPACT: **Expenditures:** Increase ( ) Decrease ( )
Revenues: Increase ( ) Decrease (X)
No Impact ( )
No Estimate Available ( )

FUND AFFECTED: **General Fund ( ) Highway Fund (X) Local Govt. ( )**
Other Funds (X) Highway Trust Fund

BILL SUMMARY: This proposal makes two changes to the motor vehicle laws. It allows a dealer of special mobile equipment to use transporter plates on the equipment in three circumstances, and it provides a highway use tax exemption and a reduced title fee from $35 to $10 for the transfer of a salvage vehicle when the transfer is from an insurance company to the person who owned the vehicle when it became a salvage vehicle.

EFFECTIVE DATE: The transporter plate change is effective upon ratification and the salvage vehicle changes become effective July 1, 1995.

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED: Department of Transportation, Division of Motor Vehicles

FISCAL IMPACT

	FY95	FY96	FY97	FY98	FY99
REVENUES:					
GENERAL FUND	Insignificant impact (maximum loss of $100,000 annually)				
HIGHWAY FUND					
HIGHWAY TRUST FUND					
LOCAL					
EXPENDITURES					
POSITIONS:					

ASSUMPTIONS AND METHODOLOGY: The estimate given in this note is a preliminary figure that has not yet been finalized. Allowing special mobile equipment dealers to use transporter plates will increase revenues in the Highway Fund to a small degree, but this revenue increase will be offset by the reduction in the title fee for salvage vehicles.

The Highway Trust Fund will lose $40 in minimum highway use taxes and $21.50 in title fees for each salvage title transaction. It is assumed at this time that the number of transactions that would be affected by the changes in this bill would be very small. Therefore, an

insignificant revenue loss to the Highway Trust Fund is estimated at this time.

SOURCES OF DATA: Department of Transportation, Division of Motor Vehicles

TECHNICAL CONSIDERATIONS:

FISCAL RESEARCH DIVISION 733-4910
PREPARED BY: Ruth Sappie
APPROVED BY:
DATE: December 9, 1994

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

Proposal 12 (95-LJ-6)
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Lower Minimum Highway Use Tax. (Public)

Sponsors: Representatives Ramsey, Arnold, Gamble, Luebke, and Tallent.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO LOWER THE MINIMUM HIGHWAY USE TAX.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-187.3 reads as rewritten:

"§ 105-187.3. Rate of tax.

(a) Amount. -- The rate of the use tax imposed by this Article is three percent (3%) of the retail value of a motor vehicle for which a certificate of title is issued. The tax is payable as provided in G.S. 105-187.4. The tax may not be less than ~~forty dollars ($40.00)~~ twenty dollars ($20.00) for each motor vehicle for which a certificate of title is issued, unless the issuance of a title for the vehicle is exempt from tax under G.S. 105-187.6(a). The tax may not be more than one thousand dollars ($1,000) for each certificate of title issued for a Class A or Class B motor vehicle that is a commercial motor vehicle, as defined in G.S. 20-4.01. The tax may not be more than one thousand five hundred dollars ($1,500) for each certificate of title issued for any other motor vehicle.

(b) Retail Value. -- The retail value of a motor vehicle for which a certificate of title is issued because of a sale of the motor vehicle by a retailer is the sales price of the motor vehicle, including all accessories attached to the vehicle when it is delivered to the purchaser, less the amount of any

allowance given by the retailer for a motor vehicle taken in trade as a partial payment for the purchased motor vehicle. The retail value of a motor vehicle for which a certificate of title is issued because of a sale of the motor vehicle by a seller who is not a retailer is the market value of the vehicle, less the amount of any allowance given by the seller for a motor vehicle taken in trade as a partial payment for the purchased motor vehicle. The retail value of a motor vehicle for which a certificate of title is issued because of a reason other than the sale of the motor vehicle is the market value of the vehicle. The market value of a vehicle is presumed to be the value of the vehicle set in a schedule of values adopted by the Commissioner.

(c) Schedules. -- In adopting a schedule of values for motor vehicles, the Commissioner shall adopt a schedule whose values do not exceed the wholesale values of motor vehicles as published in a recognized automotive reference manual."

Sec. 2. G.S. 105-187.7 reads as rewritten:

"**§ 105-187.7. Credit for tax paid in another state.**

A person who, within 90 days before applying for a certificate of title for a motor vehicle on which the tax imposed by this Article is due, has paid a sales tax, an excise tax, or a tax substantially equivalent to the tax imposed by this Article on the vehicle to a taxing jurisdiction outside this State is entitled to a credit against the tax due under this Article for the amount of tax paid to the other jurisdiction. The credit may not reduce the person's liability under this Article below the minimum ~~forty-dollar ($40.00) tax.~~ tax set in G.S. 105-187.3."

Sec. 3. G.S. 105-187.8 reads as rewritten:

"**§ 105-187.8. Refund for return of purchased motor vehicle.**

When a purchaser of a motor vehicle returns the motor vehicle to the seller of the motor vehicle within 90 days after the purchase and receives a vehicle replacement for the returned vehicle or a refund of the price paid the seller, whether from the seller or the manufacturer of the vehicle, the purchaser may obtain a refund of the privilege tax paid on the certificate of title issued for the returned motor vehicle, less the minimum tax ~~of forty dollars ($40.00).~~ set in G.S. 105-187.3.

To obtain a refund, the purchaser must apply to the Division for a refund within 30 days after receiving the replacement vehicle or refund of the purchase price. The application must be made on a form prescribed by the Commission and must be supported by documentation from the seller of the returned vehicle."

Sec. 4. This act becomes effective July 1, 1995.

Explanation of Proposal 12

With this proposal, the Revenue Laws Study Committee renews its recommendation that the minimum highway use tax be lowered from $40.00 to $20.00. The proposal becomes effective July 1, 1995. The Committee has made this same recommendation to each session of the General Assembly since the enactment of the highway use tax in 1989.

In 1989 the General Assembly created the Highway Trust Fund and imposed the highway use tax to provide revenue for that Fund. The highway use tax replaces the former sales tax on motor vehicles. The highway use tax is 3% of the retail value of a motor vehicle, subject to both a minimum and a maximum tax. The minimum tax is $40.00. The maximum tax is $1,500 for automobiles and other vehicles that weigh no more than 26,000 pounds and is $1,000 for vehicles that weigh more than 26,000 pounds.

The highway use tax is payable when a certificate of title is issued for a motor vehicle. The tax is in addition to the $35.00 fee that is charged for the issuance of a title and the $10.00 or $20.00 fee that is charged for the transfer or issuance of a license plate. Thus, the minimum combined tax and fees payable when a certificate of title is transferred as the result of the sale of a motor vehicle is $85.00 if the new owner transfers a license plate to the vehicle and is $95.00 if the new owner obtains a new license plate for the vehicle. These figures are the result of adding the $40.00 tax, the $35.00 title fee, and either the $10.00 or $20.00 fee for a license plate.

When the highway use tax was first enacted, the Committee received numerous complaints about the high minimum amount that must be paid to transfer a certificate of title. The Committee continues to receive complaints about this aspect of the highway use tax. The Division of Motor Vehicles of the Department of Transportation continues to receive complaints about this aspect of the highway use tax as well. According to the Director of Vehicle Registration of that Division, the high minimum tax on utility trailers and other low-value vehicles is the number one complaint from the public about the highway use tax.

In response to these complaints, the Committee has discussed the highway use tax several times. Each time, the Committee has concluded that the minimum tax of $40.00 is not fair, particularly when coupled with the $35.00 title fee, because the tax

is very regressive and does not distinguish between motor vehicles valued at less than $1,300. The transfer of a boat trailer, for example, that has a value of $150 triggers the payment of at least $85.00 in taxes and fees while the transfer of a car valued at $1,300 triggers payment of the very same amount of taxes and fees.

The Committee makes this recommendation with the knowledge that less revenue will accrue to the Highway Trust Fund if the recommendation is enacted. The Committee believes, however, that it is more important to make the tax equitable than to maximize tax revenue by continuing to collect an unfair tax.

Because of the inherent inequities of the minimum tax, the Committee debated eliminating the minimum altogether, thereby making the tax based entirely on value until the maximum tax is reached. The Committee chose to recommend lowering the minimum tax rather than eliminating it out of consideration for the strong desires expressed during past legislative debates on this proposal to not reduce Highway Trust Fund revenue for any reason. The Committee's recommendation is therefore a compromise.

Section 1 of the proposal reduces the minimum highway use tax to $20.00. Sections 2 and 3 are conforming changes and change references to the amount of the minimum tax.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: Proposal 12
SHORT TITLE: Lower Minimum Highway Use Tax
SPONSOR(S):

FISCAL IMPACT: **Expenditures:** Increase ( ) Decrease ( )
Revenues: Increase ( ) Decrease (X)
No Impact ( )
No Estimate Available ( )

FUND AFFECTED: **General Fund ( ) Highway Fund ( ) Local Govt. ( )**
Other Funds (X) Highway Trust Fund

BILL SUMMARY: This proposal reduces the minimum highway use tax from $40 to $20.

EFFECTIVE DATE: July 1, 1995

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED: Division of Motor Vehicles, Department of Transportation

FISCAL IMPACT

	FY94	FY95	FY96	FY97	FY98
REVENUES					
GENERAL FUND					
HIGHWAY FUND					
HIGHWAY TRUST FUND		$6-7 million annually			
LOCAL					
EXPENDITURES					
POSITIONS:					

ASSUMPTIONS AND METHODOLOGY: The Division of Motor Vehicles has recently completed a manual survey of title transactions at the Raleigh window for the month of November. This data has not yet been analyzed. Data from a survey done four years ago is used in this note to produce the preliminary estimate of an annual revenue loss to the Highway Trust Fund of $6-7 million.

SOURCES OF DATA: Division of Motor Vehicles, Department of Transportation

TECHNICAL CONSIDERATIONS:

FISCAL RESEARCH DIVISION 733-4910
PREPARED BY: Ruth Sappie
APPROVED BY:
DATE: December 9, 1994

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

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Proposal 13 (95-LJX-4(1.5))
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Collect Fuel Tax At Rack. (Public)

Sponsors: Senators Kerr and Hoyle.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO ADDRESS MOTOR FUEL TAX EVASION BY CHANGING THE POINT OF TAXATION OF GASOLINE AND DIESEL FUEL.

The General Assembly of North Carolina enacts:

PART I. MOTOR FUEL LAW CHANGES

Section 1. The heading to Subchapter V of Chapter 105 of the General Statutes reads as rewritten:

"SUBCHAPTER V. ~~GASOLINE TAX.~~ MOTOR FUEL TAXES."

Sec. 2. Articles 36 and 36A of Chapter 105 of the General Statutes are repealed.

Sec. 3. Subchapter V of Chapter 105 of the General Statutes is amended by adding a new Article to read:

"Article 36C.

"Per Gallon Excise Taxes.

"Part 1. General Provisions.

"§ 105-449.60. Definitions.

The following definitions apply in this Article:

(1) Blended fuel. -- A mixture composed of gasoline or diesel fuel and another liquid, other than a de minimus amount of a product such as carburetor detergent or oxidation inhibitor, that can be used as a fuel in a highway vehicle.

(2) Blender. -- A person who produces blended fuel outside the bulk transfer and terminal system.

(3) Bulk end user. -- A person that maintains storage facilities for motor fuel and uses part or all of the stored fuel to operate a highway vehicle.

(4) Bulk plant. -- A motor fuel storage and distribution facility that is not a terminal and from which motor fuel may be removed at a rack.

(5) Bulk transfer. -- Either of the following:

a. A transfer of motor fuel by pipeline or marine vessel.

b. A transfer, by railroad tank car or transport truck, of fuel grade ethanol to a terminal or a refinery.

(6) Bulk transfer and terminal system. -- The motor fuel distribution system consisting of refineries, pipelines, marine vessels, and terminals.

(7) Code. -- Defined in G.S. 105-228.90.

(8) Destination state. -- The state, territory, or foreign country to which motor fuel is directed for delivery into a storage facility, a receptacle, a container, or a type of transportation equipment for the purpose of resale or use.

(9) Diesel fuel. -- Any liquid, other than gasoline, that is suitable for use as a fuel in a diesel-powered highway vehicle. The term does not include jet fuel sold to a buyer who is registered to purchase jet fuel under § 4101 of the Code.

(10) Distributor. -- A person who acquires motor fuel from a supplier or from another distributor for subsequent sale or use.

(11) Dyed diesel fuel. -- Diesel fuel that meets the dying and marking requirements of § 4082 of the Code.

(12) Export. -- To obtain motor fuel in this State for sale or other distribution in another state. In applying this definition, motor fuel delivered out-of-state by or for the seller constitutes an export by the seller and motor fuel delivered out-of-state by or for the purchaser constitutes an export by the purchaser.

(13) Fuel alcohol. -- Methanol or fuel grade ethanol.

(14) Fuel alcohol provider. -- A person that produces fuel alcohol or imports fuel alcohol by transport truck or railroad tank car.

(15) Gasohol. -- A blended fuel composed of gasoline and fuel grade ethanol.

(16) Gasoline. -- Any of the following:

a. All products that are commonly or commercially known or sold as gasoline and are suitable for use as a fuel in a highway vehicle, other than products that have an American Society for Testing Materials octane number of less than 75 as determined by the motor method.

b. A petroleum product component of gasoline, such as naptha, reformate, or toluene.

c. Gasohol.

d. Fuel grade ethanol.

The term does not include aviation gasoline sold for use in an aircraft motor. 'Aviation gasoline' is gasoline that is designed for use in an aircraft motor and is not adapted for use in an ordinary highway vehicle.

(17) Highway. -- Defined in G.S. 20-4.01(13).

(18) Highway vehicle. -- A self-propelled vehicle that is designed for use on a highway.

(19) Import. -- To bring motor fuel into this State by any means of conveyance other than in the fuel supply tank of a highway vehicle. In applying this definition, motor fuel delivered into this State from out-of-state by or for the seller constitutes an import by the seller, and motor fuel delivered into this State from out-of-state by or for the purchaser constitutes an import by the purchaser.

(20) Motor fuel. -- Gasoline, diesel fuel, and blended fuel.

(21) Motor fuel rate. -- The rate of tax set in G.S. 105-449.80.

(22) Motor fuel transporter. -- A person who transports motor fuel by transport truck or railroad tank car.

(23) Permissive supplier. -- An out-of-state supplier that elects, but is not required, to have a supplier's license under this Article.

(24) Person. -- Defined in G.S. 105-228.90.

(25) Position holder. -- The person who holds the inventory position in motor fuel in a terminal, as reflected on the records of the terminal operator. A person holds the inventory position in motor fuel when that person has a contract with the terminal

operator for the use of storage facilities and terminaling services for fuel at the terminal. The term includes a terminal operator who owns fuel in the terminal.

(26) Rack. -- A mechanism for delivering motor fuel from a refinery, a terminal, or a bulk plant into a railroad tank car, a transport truck, or another means of nonbulk transfer.

(27) Removal. -- A physical transfer other than by evaporation, loss, or destruction.

(28) Reseller. -- A person that maintains storage facilities for motor fuel and that sells the fuel at retail or dispenses the fuel at a retail location.

(29) Secretary. -- Defined in G.S. 105-228.90.

(30) Supplier. -- Any of the following:

a. A position holder or a person that receives motor fuel pursuant to a two-party exchange.

b. A fuel alcohol provider.

(31) Tank wagon. -- A truck that is not a transport truck.

(32) Terminal. -- A motor fuel storage and distribution facility that is approved under the Code, is supplied by pipeline or marine vessel, and from which motor fuel may be removed at a rack.

(33) Terminal operator. -- A person who owns, operates, or otherwise controls a terminal.

(34) Transport truck. -- A semitrailer combination rig designed or used to transport loads of motor fuel over a highway.

(35) Two-party exchange. -- A transaction in which a licensed supplier transfers ownership of motor fuel at a terminal to another licensed supplier, as reflected on the records of the terminal operator.

"**§ 105-449.61. No local tax; administration.**

(a) No Local Tax. -- A county or city may not impose a tax on the sale, distribution, or use of motor fuel.

(b) Administration. -- Article 9 of this Chapter applies to this Article.

"Part 2. Licensing.

"**§ 105-449.65. List of persons who must have a license.**

(a) License. -- A person may not engage in business in this State as any of the following unless the person has a license

issued by the Secretary authorizing the person to engage in that business:

(1) A refiner.
(2) A supplier.
(3) A terminal operator.
(4) An importer.
(5) A blender.
(6) A motor fuel transporter.
(7) A bulk end user of undyed diesel fuel.
(8) A reseller of undyed diesel fuel.

(b) Types of Importers. -- An applicant for a license as an importer must indicate the type of importer license sought. A person may not be licensed as more than one type of importer. The types of importers are as follows:

(1) Bonded Importer. -- A bonded importer is a person, other than a supplier, that imports, by transport truck or another means of nonbulk transfer, motor fuel removed from a terminal located in another state in any of the following circumstances:

a. The state from which the fuel is imported does not require the seller of the fuel to collect motor fuel tax on the removal either at that state's rate or the rate of the destination state.

b. The seller of the fuel is not a licensed supplier that has elected to collect motor fuel tax on motor fuel that is removed by the supplier in another state and has this state as its destination state.

c. The seller of the fuel is not licensed under this Part as a permissive supplier.

(2) Occasional Importer. -- An occasional importer is a person that imports motor fuel by an means outside the bulk transfer and terminal system.

(3) Tank Wagon Importer. -- A tank wagon importer is a person that imports, by nonbulk transfer only in tank wagons, motor fuel that is removed from a bulk plant located in another state.

(c) Multiple Activity. -- A person who is engaged in more than one activity for which a license is required must have a separate license for each activity, unless this subsection provides otherwise. A person who is licensed as a supplier is not required to obtain a separate license for any other activity for which a license is required and is considered to have a license

as a distributor. A person who is licensed as a blender is not required to obtain a separate license as a motor fuel transporter.

"**§ 105-449.66. List of persons who may obtain a license.**

A person who is engaged in business as any of the following may obtain a license issued by the Secretary for that business:

(1) A distributor.

(2) A permissive supplier.

"**§ 105-449.67. How to apply for a license.**

(a) General. -- To obtain a license, an applicant must file an application with the Secretary on a form provided by the Secretary. An application must include the applicant's name, address, federal employer identification number, and any other information required by the Secretary.

(b) Most Licenses. -- An applicant for a license as a refiner, a supplier, a terminal operator, an importer, a blender, a bulk end user of undyed diesel fuel, a reseller of undyed diesel fuel, or a distributor must meet the following requirements:

(1) If the applicant is a corporation, the applicant must either be incorporated in this State or be authorized to transact business in this State.

(2) If the applicant is a limited liability company, the applicant must either be organized in this State or be authorized to transact business in this State.

(3) If the applicant is a limited partnership, the applicant must either be formed in this State or be authorized to transact business in this State.

(4) If the applicant is an individual or a general partnership, the applicant must designate an agent for service of process and give the agent's name and address.

(c) Federal Certificate.-- An applicant for a license as a refiner, a supplier, a terminal operator, a blender, or a permissive supplier must have a federal Certificate of Registry that is issued under § 4101 of the Code and authorizes the applicant to enter into federal tax-free transactions in taxable motor fuel in the bulk transfer and terminal system. An applicant that is required to have a federal Certificate of Registry must include the registration number of the certificate on the application for a license under this section.

An applicant for a license as an importer or a distributor that has a federal Certificate of Registry issued under § 4101 of the

Code must include the registration number of the certificate on the application for a license under this section.

(d) Import and Export Activity. -- An applicant for a license as an importer must list on the application each state from which the applicant intends to import motor fuel. An applicant for a license as a distributor must list on the application each state to which the applicant intends to export motor fuel received by nonbulk transfer in this State and, if required by a state listed, must be licensed or registered for motor fuel tax purposes in that state.

"**§ 105-449.68. Supplier election to collect tax on out-of-state removals.**

(a) Election. -- An applicant for a license as a supplier may elect on the application to collect the excise tax due this State on motor fuel that is removed by the supplier at a terminal located in another state and has this State as its destination state. The Secretary must provide for this election on the application form. A supplier that does not make the election on the application for a supplier's license may make the election later by completing an election form provided by the Secretary.

(b) Effect. -- A supplier that makes the election allowed by this section agrees to all of the following with respect to motor fuel that is removed by the supplier at a terminal located in another state and has this State as its destination state:

(1) To collect the excise tax due this State on the fuel.

(2) To report and pay the tax due on the fuel in the same manner as if the removal had occurred at a terminal located in this State.

(3) To keep records of the removal of the fuel and submit to audits concerning the fuel as if the removal had occurred at a terminal located in this State.

"**§ 105-449.69. Permissive supplier election to collect tax on out-of-state removals.**

An out-of-state supplier that is not required to have a license under this Part may elect to have a license and thereby become a permissive supplier. By obtaining a license as a permissive supplier, the permissive supplier agrees to be subject to the same requirements as a supplier and to all of the following with respect to motor fuel that is removed by the permissive supplier at a terminal located in another state and has this State as its destination state:

(1) To collect the excise tax due this State on the fuel.
(2) To report and pay the tax due on the fuel in the same manner as if the removal had occurred at a terminal located in this State.
(3) To keep records of the removal of the fuel and submit to audits concerning the fuel as if the removal had occurred at a terminal located in this State.

"**§ 105-449.70. Bond or letter of credit required as a condition of obtaining and keeping certain licenses.**

(a) Initial Bond. -- An applicant for a license as a refiner, a terminal operator, a supplier, an importer, a permissive supplier, or a distributor must file with the Secretary a bond or an irrevocable letter of credit. The amount of the bond or irrevocable letter of credit is determined as follows:

(1) For an applicant for a license as any of the following, the amount is two million dollars ($2,000,000):
a. A refiner.
b. A terminal operator.
c. A supplier that is a position holder or a person that receives motor fuel pursuant to a two-party exchange.
d. A bonded importer.
E. A permissive supplier.

(2) For an applicant for a license as any of the following, the amount is two times the applicant's average expected monthly tax liability under this Article, as determined by the Secretary. The amount may not be less than two thousand dollars ($2,000) and may not be more than two hundred fifty thousand dollars ($250,000):
a. A supplier that is a fuel alcohol provider but is not a position holder or a person that receives motor fuel pursuant to a two-party exchange.
b. An occasional importer.
c. A tank wagon importer.
d. A distributor,

A bond filed under this section must be conditioned upon compliance with the requirements of this Article, be payable to the State, and be in the form required by the Secretary. An applicant for a license as a distributor and as a bonded importer

must file only the bond required of a bonded importer. An applicant for a license as a distributor and either an occasional importer or a tank wagon importer may file one bond that covers the combined liabilities of the applicant under both activities.

(b) Adjustment To Bond. -- When notified to do so by the Secretary, a person that has filed a bond or an irrevocable letter of credit and that holds a license listed in subdivision (a)(2) of this section must file an additional bond or irrevocable letter of credit in the amount requested by the Secretary. The person must file the additional bond or irrevocable letter of credit within 30 days after receiving the notice from the Secretary, The amount of the initial bond or irrevocable letter of credit and any additional bond or irrevocable letter of credit filed by the license holder, however, may not exceed the limits set in subdivision (a)(2) of this section.

"§ 105-449.71. Reasons why the Secretary can deny an application for a license.

The Secretary may refuse to issue a license to an individual applicant who has done any of the following and may refuse to issue a license to an applicant that is a business entity if any principal in the business has done any of the following:

(1) Had a license or registration issued under this Article or former Articles 36 or 36A of this Chapter cancelled by the Secretary.

(2) Had a federal certificate of registry issued under § 4101 of the Code, or a similar federal authorization, revoked.

(3) Been convicted of fraud or misrepresentation.

(4) Been convicted of any other offense that indicates that the applicant may not comply with this Article if issued a license.

"§ 105-449.72. Issuance of license.

Upon approval of an application, the Secretary must issue a license to the applicant as well as a duplicate copy of the license for each place of business of the applicant. A supplier's license must indicate the category of the supplier. A license holder must display a license issued under this Part in a conspicuous place at each place of business of the license holder. A license is not transferable and remains in effect until surrendered or cancelled.

"§ 105-449.73. Supplier must notify the Secretary of discontinuance of business.

A supplier that stops engaging in business in this State as a supplier must give the Secretary written notice of the change. The notice must give the date the change takes effect and, if the supplier has transferred the business to another by sale or otherwise, the date of the transfer and the name and address of the person to whom the business is transferred. All taxes for which the supplier is liable under this Article but are not yet due become due on the date of the change. A supplier that stops engaging in business as a supplier must surrender its supplier's license to the Secretary.

If a supplier does not give a notice required by this section, the person to whom the supplier has transferred the business is liable for the amount of tax the supplier owed the State on the date the business was transferred. The liability of the person to whom the business is transferred is limited to the value of the property acquired from the supplier.

"**§ 105-449.74. Reasons why the Secretary can cancel a license.**

The Secretary may cancel a license issued under this Article upon the written request of the license holder. The Secretary may summarily cancel the license of a supplier when the Secretary finds that the supplier is incurring liability for the tax imposed under this Article after failing to pay a tax when due under this Article. In addition, the Secretary may cancel the license of a supplier or any other license holder who commits one or more of the acts listed in G.S. 105-449.108 after holding a hearing on whether the license should be cancelled.

The Secretary must send a supplier whose license is summarily cancelled a notice of the cancellation and must give the supplier an opportunity to have a hearing on the cancellation within 10 days after the cancellation. The Secretary must give a licensee whose license may be cancelled after a hearing at least 10 days' written notice of the date, time, and place of the hearing. A notice of a summary license cancellation and a notice of hearing must be sent by registered mail to the last known address of the license holder.

When the Secretary cancels the license of a supplier and the supplier has paid all taxes and penalties due under this Article, the Secretary must take one of the following actions on the concerning a bond or an irrevocable letter of credit filed by the supplier:

(1) Return an irrevocable letter of credit to the supplier.

(2) Return a bond to the supplier or notify the person liable on the bond and the supplier that the person is released from liability on the bond.

"**§ 105-449.75. Records and lists of license applicants and license holders.**

(a) Records. -- The Secretary must keep a record of the following:

(1) Applicants for a license under this Article.

(2) Persons to whom a license has been issued under this Article.

(3) Persons who hold a current license issued under this Article, by license category.

(b) List. -- The Secretary must give a list of licensed distributors to each licensed supplier who asks for a copy of the list. The list must state the name and business address of each distributor on the list. The Secretary must send a monthly update of the appropriate list to each supplier who requested a copy of the list.

"Part 3. Tax and Liability.

"**§ 105-449.80. Tax rate.**

(a) Rate. -- The motor fuel excise tax rate is a flat rate of seventeen and one-half cents (17 1/2¢) a gallon plus a variable wholesale component. The variable wholesale component is either three and one-half cents (3 1/2¢) a gallon or seven percent (7%) of the average wholesale price of motor fuel for the applicable base period, whichever is greater.

The two base periods are six-month periods; one ends on September 30 and one ends on March 31. The Secretary must set the tax rate twice a year based on the wholesale price for each base period. A tax rate set by the Secretary using information for the base period that ends on September 30 applies to the six-month period that begins the following January 1. A tax rate set by the Secretary using information for the base period that ends on March 31 applies to the six-month period that begins the following July 1.

(b) Wholesale Price. -- The Secretary must determine the average wholesale price of motor fuel for each base period. To do this, the Secretary must use information on refiner and gas plant operator sales prices of finished motor gasoline and No. 2 diesel fuel for resale, published by the United States Department of Energy in the 'Monthly Energy Review,' or equivalent data.

The Secretary must compute the average sales price of finished motor gasoline for the base period, compute the average sales price for No. 2 diesel fuel for the base period, and then compute

a weighted average of the results of the first two computations based on the proportion of tax collected on each under this Article for the base period. The Secretary must then convert the weighted average price to a cents-per-gallon rate and round the rate to the nearest one-tenth of a cent (1/10¢). If the converted cents-per-gallon rate is exactly between two tenths of a cent, the Secretary must round the rate up to the higher of the two.

(c) Notification. -- The Secretary must notify affected taxpayers of the tax rate to be in effect for each six-month period beginning January 1 and July 1.

"**§ 105-449.81. Excise tax on motor fuel.**

An excise tax at the motor fuel rate is imposed on motor fuel that is:

(1) Removed from a refinery or a terminal and, upon removal, is subject to the federal excise tax imposed by § 4081 of the Code.

(2) Imported by bulk transfer to a refinery or a terminal and, upon importation, is subject to the federal excise tax imposed by § 4081 of the Code.

(3) Imported by a nonbulk transfer for consumption, use, or warehousing in this State and would have been subject to the federal excise tax imposed by § 4081 of the Code if it had been removed at a terminal or bulk plant rack in this State instead of imported.

(4) Is blended fuel and is removed from a bulk plant.

"**§ 105-449.82. Liability for tax on removals from a refinery or terminal.**

(a) Refinery Removal. -- The excise tax imposed by G.S. 105-449.81(1) on motor fuel removed from a refinery in this State is payable by the refiner.

(b) Terminal Bulk Removal. -- The excise tax imposed by G.S. 105-449.81(1) on motor fuel removed by bulk transfer from a terminal in this State is payable by the position holder for the fuel. If the position holder is not the terminal operator, the terminal operator is jointly and severally liable for the tax.

(c) Terminal Rack Removal. -- The excise tax imposed by G.S. 105-449.81(1) on motor fuel removed at a terminal rack in this State is payable by the position holder for the fuel, if the position holder owns the fuel when it crosses the rack. If the position holder for motor fuel removed at a terminal rack does not own the fuel when it crosses the rack, the excise tax on the fuel is payable by the supplier to whom the position holder

transferred the fuel pursuant to a two-party exchange. The position holder or other supplier that owns the fuel when it crosses the rack and the distributor that receives the fuel are liable for the tax, as described in this Part.

If a position holder or other supplier that is liable for the tax under this subsection is not the terminal operator and does not have a license required by this Article, the terminal operator is jointly and severally liable for any amount for which the position holder or other supplier is liable. If the motor fuel removed is not dyed diesel fuel but the shipping document issued for the fuel states that the fuel is dyed diesel fuel, the terminal operator is jointly and severally liable for the tax due on the fuel.

"**§ 105-449.83. Liability for tax on imports.**

(a) By Bulk Transfer. -- The excise tax imposed by G.S. 105-449.81(2) on motor fuel imported by bulk transfer to a refinery is payable by the refiner. The excise tax imposed by that subdivision on motor fuel imported by bulk transfer to a terminal is payable by the person importing the fuel and by the terminal operator, both of which are jointly and severally liable for payment of the tax due on the fuel.

(b) From Out-of-State Terminal. -- The excise tax imposed by G.S. 105-449.81(3) on motor fuel that is removed from a terminal rack located in another state and has this State as its destination state is payable as follows:

(1) By the supplier of the fuel, if the supplier is required to be licensed as a supplier in this State and either of the following applies:

a. The supplier has elected to collect the excise tax due this State on these out-of-state removals.

b. The fuel is removed for the supplier's own account for use in this State.

(2) By the supplier of the fuel, if the supplier is licensed as a permissive supplier.

(3) By the importer of the fuel, if no other subdivision of this subsection applies.

(c) From Out-of-State Bulk Plant. -- The excise tax imposed by G.S. 105-449.81(3) on motor fuel that is removed from a bulk plant located in another state is payable by the supplier who imports the fuel.

"**§ 105-449.84. Liability for tax on blended fuel produced in this State.**

The excise tax imposed by G.S. 105-449.81(4) on blended fuel removed from a bulk plant in this State is payable by the blender. The number of gallons of blended fuel on which the tax is payable is the difference between the number of gallons of blended fuel removed and the number of gallons of previously taxed motor fuel used to make the blended fuel that is removed.

"**§ 105-449.85. Tax on and liability for certain blends made at a terminal.**

(a) In-Line-Blends. -- A tax at the motor fuel rate is imposed on a liquid that is combined with gasoline or undyed diesel fuel as the fuel is delivered at a terminal rack into the motor fuel storage compartment of a motor fuel tank truck. The supplier of the gasoline or undyed diesel fuel used in the blended fuel is liable for the tax.

(b) Kerosene Splash-Blends. -- A tax at the motor fuel rate is imposed on kerosene that is delivered at a terminal into a motor fuel storage compartment of a motor fuel tank truck when undyed diesel fuel is also delivered at that terminal into the same storage compartment and the buyer of the kerosene notified the supplier before or at the time of delivery that the kerosene would be used to make a splash-blend. The supplier of the kerosene is liable for the tax.

"**§ 105-449.86. Tax on and liability for dyed diesel fuel used to operate certain highway vehicles.**

(a) Tax. -- An excise tax at the motor fuel rate is imposed on dyed diesel fuel acquired to operate any of the following:

(1) Either a local bus or an intercity bus that is allowed by § 4082(b)(3) of the Code to use dyed diesel fuel.

(2) A highway vehicle that is owned by or leased to an educational organization that is not a public school and is allowed by § 4082(b)(1) or (b)(3) of the Code to use dyed diesel fuel.

(b) Liability. -- The person who acquires fuel that is taxable under this section is liable for the tax.

"**§ 105-449.87. Tax on alternative fuel and liability for the tax.**

A tax at the equivalent of the motor fuel rate is imposed on fuel that is used to operate a highway vehicle and is not a motor fuel. The Secretary must determine the equivalent rate. In the case of a liquid fuel or a fuel that is a gas, the tax is payable by the person who provides the fuel.

"**§ 105-449.88. Backup tax and liability for the tax.**

(a) Tax. -- An excise tax at the motor fuel rate is imposed on the following:

(1) Dyed diesel fuel that is used to operate a highway vehicle for a use that is not a nontaxable use under § 4082(b) of the Code.

(2) Motor fuel that is used to operate a highway vehicle and for which a refund of part or all of the motor fuel tax has been allowed.

(b) Liability. -- The operator of a highway vehicle that uses motor fuel that is taxable under this section is liable for the tax. If the highway vehicle that uses the fuel is owned by or leased to a motor carrier, the motor carrier is jointly and severally liable for the tax. If the end seller of motor fuel taxable under this section knew or had reason to know that the motor fuel would be used for a purpose that is taxable under this section, the end seller is jointly and severally liable for the tax.

(c) Imputed Knowledge. -- An end seller of dyed diesel fuel is considered to have known or had reason to know that the fuel would be used for a purpose that is taxable under this section unless the end seller delivered the fuel into a storage facility that meets any of the following requirements:

(1) It contains fuel used only in heating, drying crops, or a manufacturing process and is installed in a manner that makes use of the fuel for any other purpose improbable.

(2) It is marked as follows with the phrase 'Dyed Diesel,' 'For Nonhighway Use,' or a similar phrase that clearly indicates the fuel is not to be used to operate a highway vehicle:

a. The storage tank of the storage facility is marked if the storage tank is visible.

b. The fillcap or spill containment box of the storage facility is marked.

c. The dispensing device that serves the storage facility is marked.

"**§ 105-449.89. Exemptions from the excise tax.**

The excise tax on motor fuel does not apply to the following:

(1) Motor fuel removed by a nonbulk transfer for export, if the person to whom the fuel is sold is licensed as a distributor and the supplier who would otherwise be required to pay the tax collects tax on the motor fuel at the rate of the fuel's

destination state that is printed on the shipping document for the fuel.

(2) Motor fuel sold to the federal government.

(3) Motor fuel sold to the State for its use.

(4) Motor fuel sold to a local board of education for use in the public school system.

"Part 4. Payment and Reporting.

"**§ 105-449.90. When tax return and payment are due.**

(a) Filing Periods. -- The excise tax imposed by this Article is payable when a return is due. A return is due monthly or within three days of incurring liability for the tax, as specified in this section. A return must be in the form required by the Secretary.

A monthly return is due within 20 days after the end of each month. A monthly return covers tax liabilities that accrue in the calendar month preceding the date the return is due.

A three-day return is due within three days of incurring liability for the tax. A three-day return covers tax liabilities that accrued no later than three days before the return is due.

(b) Monthly Filers. -- The following license holders must file a monthly return:

(1) A refiner.

(2) A supplier.

(3) A blender.

(4) A bonded importer.

(5) A tank wagon importer.

(6) A person who is liable under G.S. 105-449.86 for the tax on dyed diesel fuel used to operate certain highway vehicles.

(c) Three-day Filers. -- An occasional importer must file a three-day return.

"**§ 105-449.91. Return and discounts of supplier.**

(a) Return. -- A return of a supplier must list all of the following information:

(1) The number of gallons of motor fuel received during the month by the supplier by bulk transfer, by type of fuel and by terminal.

(2) The number of gallons of motor fuel imported during the month by the supplier by nonbulk transfer.

(3) The number of gallons of motor fuel removed at a terminal rack during the month from the account of the supplier, by type of fuel and by receiving distributor.

(4) The number of gallons of motor fuel removed during the month for export and, for each removal, the destination state of the fuel.

(5) The number of gallons of motor fuel sold during the month by the supplier to either of the following:

a. A governmental unit whose use of fuel is exempt from the tax.

b. A distributor that resold the motor fuel to a governmental unit whose use of fuel is exempt from the tax, as reported by the distributor.

(6) The amount of discounts allowed under G.S. 105-449.93 on motor fuel sold during the month to licensed distributors.

(b) Uncollectible Taxes. -- A supplier may take a credit for uncollectible taxes when filing a return. Uncollectible taxes are taxes owed to the supplier by a licensed distributor that has not paid the overdue taxes to either the supplier or the Secretary after receiving a demand for payment from the Secretary under G.S. 105-449.94. If a licensed distributor pays tax owed to a supplier after the supplier claims a credit for the amount of the tax on a return, the supplier must promptly remit the distributor's payment to the Department.

(c) Administrative Discount. -- A supplier that is liable for the excise tax imposed by this Article and who files a timely return may deduct from the amount remitted with the return a discount of one-tenth (1/10) of one percent (1%), not to exceed eight thousand dollars ($8,000) a month. The discount covers expenses incurred in collecting taxes on motor fuel from distributors and in maintaining the records and preparing the returns required by this Article.

(d) Percentage Discount. -- A supplier that sells motor fuel directly to the bulk end user, the reseller, or user of the fuel can take the same percentage discount on the fuel that a licensed distributor can take when making deferred payments of tax to the supplier.

(e) Payment Applied To Tax. -- A supplier that receives a payment of excise tax from a distributor may not apply the payment to debts for motor fuel purchased from the supplier.

"**§ 105-449.92. Returns and discounts of importers.**

(a) Bonded or Occasional. -- A monthly return of a bonded importer and a three-day return of an occasional importer must contain the following information:

(1) The number of gallons of motor fuel imported during the period covered by the return and the state from which the fuel was imported.

(2) The import authorization number of each import included in the return.

(b) Tank Wagon. -- A return of an occasional importer must list the number of gallons of motor fuel imported during the month and the bulk plant from which the fuel was imported.

(c) Discounts. -- An importer may not deduct an administrative discount from the amount remitted with a return. An importer can take the same percentage discount on motor fuel imported by the importer that a licensed distributor can take when making deferred payments of tax to a supplier.

"**§ 105-449.93. Payments by licensed distributors to suppliers.**

(a) Deferred Payment. -- A licensed distributor may defer payment of the excise tax due on motor fuel received from a supplier until the date the supplier must pay the tax to the State if the distributor complies with any requirements of the supplier to pay the tax due the supplier by electronic funds transfer and the distributor has not lost the privilege of making deferred payments. A licensed distributor loses the privilege of making deferred payments when the distributor does any of the following and the Secretary determines that collection of excise tax revenue will be jeopardized if the distributor has the privilege of making deferred payments to a supplier:

(1) Fails to make a timely payment to a supplier or to the Department.

(2) Falsely reports the amount of exempt sales made by the distributor to a governmental unit.

(3) Submits a false application for a refund of motor fuel taxes.

(b) Discount. -- A licensed distributor that pays the excise tax due a supplier by the date the supplier must pay the tax to the State may deduct from the amount due a discount of X percent (X%) of the amount of tax payable. The discount covers the expense of furnishing a bond and losses due to shrinkage or evaporation.

(c) Deduction For Exempt Sales. -- A distributor may deduct from the amount of tax otherwise payable to a supplier the amount calculated on motor fuel the distributor received from a supplier and resold to a governmental unit whose purchases of motor fuel are exempt from the tax under G.S. 105-449.89 if the distributor complied with requirements of the supplier concerning notification of the distributor's intent to resell the fuel in an

exempt sale. When making this deduction, the distributor must report to the supplier the number of gallons sold in exempt sales, by type of sale, and the purchasers of the fuel in the exempt sales.

"§ 105-449.94. Notification to Department of distributors that do not pay supplier on time and effect of notification.

(a) Notification. -- A supplier of motor fuel at a terminal must notify the Department within 10 days after a return is due of any distributors who did not pay the tax due the supplier when the supplier filed the return. The notification must be transmitted to the Department in the form required by the Department.

(b) Department Action. -- When the Department receives a notice under subsection (a), it must contact the distributor who failed to pay and inform the distributor that the Secretary will consider terminating the distributor's privilege of making deferred excise tax payments to suppliers if the distributor does not pay the tax due within 24 hours. If the distributor does not pay the supplier or the Department within the required time, the Department must consider terminating the distributor's deferred payment privilege. After consideration, if the Secretary determines that collection of excise tax revenue will be jeopardized if the distributor continues to have the privilege of making deferred payments, the Secretary must terminate the privilege, The Secretary must notify all suppliers of the termination of a distributor's privilege to make deferred payments.

(c) Effect of Termination. -- A supplier who sells motor fuel to a distributor after receiving notice that the distributor's deferred payment privileges have been terminated is jointly and severally liable with the distributor for any tax due on motor fuel the supplier sells to the distributor. A supplier may not take a deduction for uncollectible taxes for any tax for which the supplier is made jointly and severally liable under this subsection.

(d) Restoration of Privilege. -- A distributor whose privilege of making deferred payments of tax to suppliers has been terminated may apply to the Department to reinstate the privilege. The Department may remove the distributor from the list of those whose privileges have been terminated if the Department finds that the reinstatement will not jeopardize collection of any motor fuel tax revenue.

"§ 105-449.95. Report by terminal operator.

A terminal operator must make a monthly report to the Secretary of motor fuel received or removed from the terminal during the month. The report is due by the 25th day of the month following the month covered by the report and must contain the following information and any other information required by the Secretary:

(1) The number of gallons of motor fuel received in inventory at the terminal during the month and each position holder for the fuel.

(2) The number of gallons removed from the terminal during the month and, for each removal, the position holder for the fuel and the destination state of the fuel.

"**§ 105-447.97. Reports by those who transport motor fuel.**

A person who transports, by pipeline, marine vessel, railroad tank car, or transport truck, motor fuel that is being imported into this State or exported from this State must make a monthly report to the Secretary of motor fuel received or delivered for import or export by the transporter during the month. The report is due by the 25th day of the month following the month covered by the report and must contain the following information and any other information required by the Secretary:

(1) The name and address of each person from whom the transporter received motor fuel outside the State for delivery in the State, the amount of motor fuel received, the date the motor fuel was received, and the person to whom the fuel was delivered.

(2) The name and address of each person to whom the transporter delivered motor fuel from a location inside the State to a location outside the State, the amount of motor fuel delivered, and the date the motor fuel was delivered.

"**§ 105-449.98. Report of exports from a bulk plant.**

A distributor who exports motor fuel from a bulk plant located in this State must make a monthly report to the Secretary of the exports. The report is due by the 25th day of the month following the month covered by the report. The report must contain the following information and any other information required by the Secretary:

(1) The number of gallons of motor fuel exported during the month.

(2) The destination state of the motor fuel exported during the month.

"Part 5. Refunds.

"**§ 105-449.100. Refunds upon application for tax paid on exempt fuel, lost fuel, and fuel unsalable for highway use.**

(a) Licensed Distributor. -- A licensed distributor may obtain a refund for tax paid by the distributor on the following motor fuel:

(1) Fuel sold by the distributor to a governmental unit whose use of fuel is exempt from the motor fuel excise tax.

(2) Fuel exported by the distributor, including fuel whose shipping document shows this State as the destination state but was diverted to another state in accordance with the diversion procedures established by the Secretary.

(b) Lost Fuel. -- A person that is licensed as a supplier, an importer, or a distributor and that loses taxpaid motor fuel due to damage to a conveyance transporting the motor fuel, fire, a natural disaster, an act of war, or an accident may obtain a refund for the tax paid on the fuel.

(c) Accidental Mixes. -- A person who accidentally combines dyed diesel fuel with taxpaid motor fuel or accidentally combines gasoline with undyed diesel fuel may obtain a refund for the amount of tax paid on the fuel.

(d) Refund Amount. -- The amount of a refund allowed under this section is the amount of tax paid. Interest is payable at the rate set in G.S. 105-241(i) on a refund after 90 days.

"**§ 105-449.101. Quarterly refunds for certain local governmental entities, nonprofit organizations, and taxicabs.**

(a) Government and Nonprofits. -- A local governmental entity or a nonprofit organization listed below that purchases and uses motor fuel may receive a quarterly refund, for the tax paid during the preceding quarter, at a rate equal to the amount of the flat cents-per-gallon rate plus the variable cents-per-gallon rate in effect during the quarter for which the refund is claimed, less one cent (1¢) per gallon. Any of the following entities may receive a refund under this section:

(1) A county or a municipal corporation.

(2) A private, nonprofit organization that transports passengers under contract with or at the express designation of a unit of local government.

(3) A volunteer fire department.

(4) A volunteer rescue squad.

(5) A sheltered workshop recognized by the Department of Human Resources.

An application for a refund allowed under this section must be made in accordance with this Part and must be signed by the chief executive officer of the entity. The chief executive officer of a nonprofit organization is the president of the organization or another officer of the organization designated in the charter or by-laws of the organization.

(b) Taxi. -- A person who purchases and uses motor fuel in a taxicab, as defined in G.S. 20-87(1), while the taxicab is engaged in transporting passengers for hire, or in a bus operated as part of a city transit system that is exempt from regulation by the North Carolina Utilities Commission under G.S. 62-260(a)(8), may receive a quarterly refund, for the tax paid during the preceding quarter, at a rate equal to the flat cents-per-gallon rate plus the variable cents-per-gallon rate in effect during the quarter for which the refund is claimed, less one cent (1¢) per gallon. An application for a refund must be made in accordance with this Part.

§ 105-449.102. Annual refunds for off-highway use and use by certain vehicles with power attachments.

(a) Off-highway. -- A person who purchases and uses motor fuel for a purpose other than to operate a licensed highway vehicle may receive an annual refund for the tax the person paid on fuel used during the preceding calendar year at a rate equal to the amount of the flat cents-per-gallon rate in effect during the year for which the refund is claimed plus the average of the two variable cents-per-gallon rates in effect during that year, less one cent (1¢) per gallon. An application for a refund allowed under this section must be made in accordance with this Part.

(b) Certain Vehicles. -- A person who purchases and uses motor fuel in one of the vehicles listed below may receive an annual refund for the amount of fuel consumed by any of the following vehicles:

(1) A concrete mixing vehicle.
(2) A solid waste compacting vehicle.
(3) A bulk feed vehicle that delivers feed to poultry or livestock and uses a power take-off to unload the feed.
(4) A vehicle that delivers lime or fertilizer in bulk to farms and uses a power take-off to unload the lime or fertilizer.

The refund rate shall be computed by subtracting one cent (1¢) from the combined amount of the flat cents-per-gallon rate in effect during the year for which the refund is claimed and the average of the two variable cents-per-gallon rates in effect

during that year, and multiplying the difference by thirty-three and one-third percent (33 1/3%). An application for a refund allowed under this section shall be made in accordance with this Part. This refund is allowed for the amount of fuel consumed by the vehicle in its mixing, compacting, or unloading operations, as distinguished from propelling the vehicle, which amount is considered to be one-third of the amount of fuel consumed by the vehicle.

§ 105-449.103. When an application for a refund is due.

(a) Annual Refunds. -- An application for an annual refund of tax permitted by this Article is due by April 15th following the end of the calendar year for which the refund is claimed. The application must state whether or not the applicant has filed a North Carolina income tax return for the preceding taxable year, and must state that the applicant has paid for the fuel for which a refund is claimed or that payment for the fuel has been secured to the seller's satisfaction.

(b) Quarterly Refunds. -- An application for a quarterly refund of tax permitted by this Article is due by the last day of the month following the end of the calendar quarter for which the refund is claimed. The application must state that the applicant has paid for the fuel for which a refund is claimed or that payment for the fuel has been secured to the seller's satisfaction.

§ 105-449.104. Reduction or denial of late annual or quarterly refund application.

An application filed with the Secretary within six months of the date the application is due must be accepted but is subject to a penalty of twenty-five percent (25%) of the amount of the refund otherwise due if the application is filed within 30 days after the date the application is due, and is subject to a penalty of fifty percent (50%) of the amount of the refund otherwise due if the application is filed more than 30 days but within six months after the date the application is due. The Secretary may not accept an application filed more than six months after the date the application is due.

"§ 105-449.105. Review of refund application.

Upon determining that an application for refund is correct, the Secretary must issue the applicant a warrant upon the State Treasurer for the amount of the refund. If the Secretary determines that an application for refund is incorrect, the Secretary must send a written notice of the determination to the applicant, stating a time and place for a hearing. If, upon holding the hearing, the Secretary finds the applicant has

collected or sought to collect a refund to which the applicant is not entitled, the Secretary must reject the application and the applicant must pay back the tax, if any, refunded on the basis of the rejected application. The applicant may seek review of the Secretary's decision under G.S. 105-241.2, 105-241.3, and 105-241.4.

Part 6. Enforcement and Administration.

"§ 105-449.106. Shipping document required to transport motor fuel by railroad tank car or transport truck.

(a) Issuance. -- A person may not transport motor fuel by railroad tank car or transport truck unless the person has a shipping document for its transportation that complies with this section. A terminal operator and the operator of a bulk plant must give a shipping document to the person who operates a railroad tank car or a transport truck into which motor fuel is loaded at the terminal rack or bulk plant rack.

(b) Content. -- A shipping document issued by a terminal operator or the operator of a bulk plant must be machine-printed and must contain the following information and any other information required by the Secretary:

(1) Identification, including address, of the terminal or bulk plant from which the motor fuel was received.

(2) The date the motor fuel was loaded.

(3) The gross volume of motor fuel loaded.

(4) The destination state of the motor fuel, as represented by the purchaser of the motor fuel or the purchaser's agent.

(5) If the document is issued by a terminal operator, the following information:

a. The net volume temperature-corrected to 60° Fahrenheit of the motor fuel loaded.

b. A tax responsibility statement indicating the name of the supplier that is responsible for the tax due on the motor fuel and the name of the state for whose tax the supplier is responsible.

(c) Reliance. -- A terminal operator or bulk plant operator may rely on the representation made by the purchaser of motor fuel or the purchaser's agent concerning the destination state of the motor fuel. A purchaser is liable for any tax due as a result of the purchaser's diversion of fuel from the represented destination state.

(d) Duties of Transporter. -- A person to whom a shipping document was issued must do all of the following:

(1) Carry the shipping document in the conveyance for which it was issued when transporting the motor fuel described in it.

(2) Show the shipping document to a law enforcement officer upon request when transporting the motor fuel described in it.

(3) Deliver motor fuel described in the shipping document to the destination state printed on it unless the person does all of the following:

a. Notifies the Secretary before transporting the motor fuel into a state other than the printed destination state that the person has received instructions since the shipping document was issued to deliver the motor fuel to a different destination state.

b. Receives from the Secretary a confirmation number authorizing the diversion.

c. Writes on the shipping document the change in destination state and the confirmation number for the diversion.

(4) Give a copy of the shipping document to the distributor or other person to whom the motor fuel is delivered.

(e) Duties of Person Receiving Shipment. -- A person to whom motor fuel is delivered by railroad tank car or transport truck may not accept delivery of the motor fuel if the destination state shown on the shipping document for the motor fuel is a state other than North Carolina. To determine if the shipping document shows North Carolina as the destination state, the person to whom the fuel is delivered must examine the shipping document and must keep a copy of the shipping document. The person must keep a copy at the place of business where the motor fuel was delivered for 90 days from the date of delivery and must keep it at that place or another place for at least three years from the date of delivery.

(f) Sanctions. -- The following acts are grounds for a civil penalty payable to the Department of Transportation, Division of Motor Vehicles, or the Department of Revenue:

(1) Transporting motor fuel in a railroad tank car or transport truck without a shipping document or with a false or an incomplete shipping document.

(2) Delivering motor fuel to a destination state other than that shown on the shipping document.

The penalty imposed under this subsection is payable by the person in whose name the conveyance is registered, if the conveyance is a transport truck, and is payable by the person responsible for the movement of motor fuel in the conveyance, if the conveyance is a railroad tank car. The amount of the penalty depends on the amount of fuel improperly transported or diverted and whether the person against whom the penalty is assessed has previously been assessed a penalty under this subsection. For a first assessment under this subsection, the penalty is the amount of motor fuel tax payable on the improperly transported or diverted motor fuel. For a second or subsequent assessment under this subsection, the penalty is the greater of one thousand dollars ($1,000) or five times the amount of motor fuel tax payable on the improperly transported or diverted motor fuel. A penalty imposed under this subsection is in addition to any motor fuel tax assessed.

"§ 105-449.107. Penalties for highway use of dyed diesel or other nontaxpaid fuel.

It is unlawful to use dyed diesel fuel for a highway use unless that use is permitted under section 4082 of the Code. A person who operates on a highway a highway vehicle whose supply tank contains dyed diesel fuel whose use is unlawful under this section or contains other fuel on which the tax imposed by this Article has not been paid is guilty of a Class 1 misdemeanor and is liable for a civil penalty.

The penalty is payable to the Department of Transportation, Division of Motor Vehicles, or the Department of Revenue and is payable by the person in whose name the highway vehicle is registered. The amount of the penalty depends on the amount of fuel in the supply tank of the highway vehicle. The penalty is the greater of one thousand dollars ($1,000) or five times the amount of motor fuel tax payable on the fuel in the supply tank. A penalty imposed under this section is in addition to any motor fuel tax assessed.

"§ 105-449.108. Acts that are misdemeanors.

(a) Class 1. -- A person who commits any of the following acts is guilty of a Class 1 misdemeanor:

(1) Fails to obtain a license required by this Article.

(2) Willfully fails to make a report required by this Article.

(3) Willfully fails to pay a tax when due under this Article.

(4) Makes a false statement in an application, a report, or a statement required under this Article.
(5) Makes a false statement in an application for a refund.
(6) Fails to keep records as required under this Article.
(7) Refuses to allow the Secretary or a representative of the Secretary to examine the person's books and records concerning motor fuel.
(8) Fails to disclose the correct amount of motor fuel sold or used in this State.
(9) Fails to file a replacement bond or an additional bond as required under this Article.
(10) Fails to show or give a shipping document as required under this Article.

(b) Class 2. -- A person who commits any of the following acts is guilty of a Class 2 misdemeanor:
(1) Knowingly dispenses non-tax-paid motor fuel into the supply tank of a highway vehicle.
(2) Knowingly allows non-tax-paid fuel to be dispensed into the supply tank of a highway vehicle.

"**§ 105-447.109. Records and examination of records and other items.**

(a) What Must Be Kept. -- A person who is required to submit a report or file a return under Part 4 of this Article must must keep a record of all shipping documents or other documents used to determine the information provided in the report or return. The records must be kept for three years from the due date of the report or return to which the records apply.

(b) Inspection. -- The Secretary or a person designated by the Secretary may do any of the followng to determine tax liability under this Article:
(1) Examine any record a person is required to keep under subsection (a) of this section.
(2) Examine a tank or other equipment used to make, store, or transport motor fuel, diesel dyes.
(3) Take a sample of a product from a vehicle, a tank, or another container in a quantity sufficient to determine the composition of the product.

"**§ 105-449.110. Miscellaneous requirements.**

(a) Metered Pumps. -- All motor fuel dispensed at retail must be dispensed from metered pumps that indicate the total amount of fuel measured through the pumps. Each pump must be marked to indicate the type of motor fuel dispensed

(b) Truck Equipment. -- A highway vehicle that transports diesel in a tank that is separate from the fuel supply tank of the vehicle may not have a connection from the transporting tank to the motor or to the supply tank of the vehicle.

"Part 7.

"Use of Revenue.

"**§ 105-449.115 Distribution of tax revenue among various funds and accounts.**

The Secretary shall allocate the amount of revenue collected under this Article from an excise tax of one-half cent (1/2¢) a gallon to the following funds and accounts in the fraction indicated:

Fund or Account	Amount
Commercial Leaking Petroleum Underground Storage Tank Cleanup Fund.....	Nineteen thirty-seconds (19/32)
Noncommercial Leaking Petroleum Underground Storage Tank Cleanup Fund.....	Three thirty-seconds (3/32)
Water and Air Quality Account.....	Five sixteenths (5/16).

The Secretary shall allocate seventy-five percent (75%) of the remaining excise tax revenue collected under this Article to the Highway Fund and shall allocate twenty-five percent (25%) to the Highway Trust Fund.

The Secretary shall charge a proportionate share of a refund allowed under this Article to each fund or account to which revenue collected under this Article is credited. The Secretary shall credit revenue or charge refunds to the appropriate funds or accounts on a monthly basis.

"**§ 105-449.116. Distribution of part of Highway Fund allocation to Wildlife Resources Fund.**

The Secretary shall credit to the Wildlife Resources Fund one-sixth of one percent (1/6 of 1%) of the amount that is allocated to the Highway Fund under G.S. 105-449.115 and is from the excise tax on gasoline or blended fuel that contains gasoline. Revenue credited to the Wildlife Resources Fund under this section may be used only for the boating and water safety activities described in G.S. 75A-3(c). The Secretary must credit revenue to the Wildlife Resources Fund on an annual basis.

"**§ 105-449.117. Civil penalties.**

The Secretary must credit civil penalties collected under this Article to the Highway Fund as nontax revenue."

PART II.

TRANSITIONAL PROVISIONS

Sec. 4. December, 1995, Fuel Tax Liabilities. -- A distributor of gasoline or a supplier of diesel fuel that incurred liability in December of 1995 under Article 36 or 36A of Chapter 105 of the General Statutes for the per gallon excise taxes on gasoline and diesel fuel imposed by those Articles shall report the liability and pay the taxes in January of 1996 as if those Articles had not been repealed.

Sec. 5. Floor Stocks Tax.-- Every distributor of motor fuel, both at wholesale and retail, and every supplier or reseller of special fuel must inventory all motor fuel that is on hand or in the person's possession as of 12:01 a.m. on January 1, 1996, and is not in the bulk transfer and terminal system and must report the results of the inventory to the Secretary of Revenue. The report must be made on a form provided by the Secretary. The report is due by January 15, 1996.

A tax at the rate set in G.S. 105-449.80, as enacted by this act, is imposed on all fuel that is included in the reportable inventory of a distributor, a supplier, or a reseller. The tax does not apply, however, to fuel on which the per gallon excise taxes imposed by former Articles 36 and 36A of Chapter 105 of the General Statutes have been paid nor to fuel for which liability for those taxes attached before the repeal of those Articles.

A distributor, a supplier, or a reseller may pay the tax due on fuel in inventory at at any time before February 28, 1997, but at least one-twelfth (1/12) of the amount due must be paid by the last day of each month starting with February of 1996. Payments made after February 28, 1997, are late and are subject to penalties and interest under Article 9 of Chapter 105 of the General Statutes.

Sec. 6. Notwithstanding G.S. 105-449.80, the weighted average of gasoline and diesel fuel used to determine the variable component of the per gallon excise tax to be in effect for the six-month period beginning July 1, 1996, shall be computed based on the tax collected on each during the base period under former Articles 36 and 36A of Chapter 105 of the General Statutes and under Article 36C of that Chapter, as enacted by this act.

Sec. 7. This act does not affect the rights or liabilities of the State, a taxpayer, or another person arising under a statute amended or repealed by this act before its amendment or repeal; nor does it affect the right to any refund

or credit of a tax that would otherwise have been available under the amended or repealed statute before its amendment or repeal.

PART III.

CONFORMING CHANGES

Sec. 8. G.S. 119-15 reads as rewritten:

"§ 119-15. ~~'Gasoline' defined.~~ Definitions that apply to Article.

The following definitions apply in this Article:

(1) Gasoline. -- Defined in G.S. 105-449.60.

(2) Kerosene. -- Petroleum oil that is free from water, glue, and suspended matter and that meets the specifications and standards adopted by the Gasoline and Oil Inspection Board.

(3) Motor fuel. -- Defined in G.S. 105-449.60.

(4) Person. -- Defined in G.S. 105-229.90.

~~The term "gasoline" wherever used in this Article shall be construed to mean refined petroleum naphtha which by its composition is suitable for use as a carburant in internal combustion engines.~~"

Sec. 9. G.S. 119-16 is repealed

Sec. 10. G.S. 119-16.1 is repealed.

Sec. 11. G.S. 119-6.2 reads as rewritten:

"§ 119-16.2. Application for license.

A person may not engage in business as a kerosene distributor unless the person has either a license issued under ~~G.S. 105-433~~ Article 36C or a kerosene license issued under this section. To obtain a license under this section, an applicant must file an application with the Secretary of Revenue on a form provided by the Secretary and file with the Secretary a bond in the amount required by the Secretary, not to exceed twenty thousand dollars ($20,000). An applicant must give the Secretary the same information the applicant would be required to give under ~~G.S. 105-433~~ Article 36C if the applicant were applying for a license under that section. A bond filed under this section must be conditioned on compliance with this Article, be payable to the State, and be in the form required by the Secretary. A license issued under this section remains in effect until surrendered or canceled, must be displayed in the same manner as a license issued under ~~G.S. 105-433,~~ Article 36C, and is subject to the same restrictions as a license issued under that section. A person who fails to comply with this section is guilty of a Class 1 misdemeanor."

Sec. 12. G.S. 119-18(a) reads as rewritten:

"(a) Tax. -- An inspection tax of one fourth of one cent (1/4 of 1¢) per gallon is levied upon all kerosene and motor fuel. The

inspection tax on motor fuel is due and payable to the Secretary of Revenue at the same time that the per gallon excise tax on motor fuel is due and payable under ~~Articles 36 and 36A~~ Article 36C of Chapter 105 of the General Statutes. The inspection tax on kerosene is payable monthly to the Secretary by a distributor required to be licensed under G.S. 119-16.2. A monthly report by a distributor required to be licensed under G.S. 119-16.2 is due by the 20th of each month and applies to kerosene received by the distributor during the preceding month."

Sec. 13. G.S. 119-19 reads as rewritten:

"**§ 119-19. Failure to report or pay tax; cancellation of license.**

If any person shall at any time file a false report of the data or information required by law, or shall fail or refuse or neglect to file any report required by law, or to pay the full amount of the tax as required by law, the Secretary of Revenue may forthwith cancel the license of such person issued under ~~G.S. 105-433 or~~ Article 36C or G.S 119-16.2, and notify such person in writing of such cancellation by registered mail to the last known address of such person appearing in the files of the Secretary of Revenue. In the event that the license of any person shall be canceled by the Secretary of Revenue as hereinbefore provided in this section, and in the event such person shall have paid to the State of North Carolina all the taxes due and payable by him under this Article, together with any and all penalties accruing under any of the provisions of this Article, then the Secretary of Revenue shall cancel and surrender the bond theretofore filed by said person under ~~G.S. 105-433 or~~ Article 36C or G.S. 119-16.2."

Sec. 14. G.S. 119-22 is repealed.

Sec. 15. This act becomes effective January 1, 1996.

Explanation of Proposal 13

Proposal 13 changes the point of taxation for gasoline and diesel fuel to the terminal rack. The purpose of the proposal is to remove opportunities to evade taxes and to establish a system of motor fuel tax collection that can be more easily administered. North Carolina is particularly vulnerable to motor fuel tax evasion because its motor fuel tax rate is 22¢ a gallon compared to 16¢ a gallon in South Carolina and 7.5¢ a gallon in Georgia. The proposal is expected to generate an additional $24 million a year in revenues without increasing the motor fuel tax rates. The Committee's staff solicited input in developing this proposal from the North Carolina Service Station Association, the North Carolina Association of Convenience Stores, the North Carolina Petroleum Marketers' Association, the American Petroleum Institute, the Department of Revenue, and other states. Below is a side-by-side comparison of the proposed legislation and the current law.

Proposed Legislation	Current Law
A. Taxing Point	
Terminal Rack for Gasoline and Diesel	Gasoline - first sale Diesel - last sale before highway use
B. Who collects the tax?	
1. In-State Removals Supplier	Distributor
2. Out-of-State Removals Importer: Bonded Importer Occasional Importer Tank Wagon Import Permissive Supplier Electing Licensed Supplier	Distributor
C. When is it paid?	
20th of 2nd month except for occasional importer, who pays in 3 days	Gasoline is 20th of 2nd month Diesel is 25th of 2nd month

D.	**When does distributor pay supplier?**	
	Same day that supplier pays the State	Not applicable
E.	**What discounts are allowed?**	
	To be determined during session The proposal has a blank	Tax allowance on gasoline only 2% on first 150,000 1½% on nest 100,000 1% on excess over 250,000
F.	**What are the bonding requirements?**	
	Refiner, supplier, terminal operator, bonded importer -- $2,000,000	Gasoline Distributor - Two times monthly liability with with minimum of $2,000 and maximum of $125,000
	Distributor, occasional importer, tank wagon importer - Two times monthly liability with minimum of $2,000 and maximum of $250,000	Diesel Supplier - Two times monthly liability with minimum of $500 and a maximum of $125,000
G.	**Exemptions**	
	Exports, sales to federal government, sales to state, sales to local boards of education, sales to counties and municipalities	Same except for counties and municipalities; they now get a refund
H.	**Refunds**	
	Exempt sales, exports, diversions, lost fuel, accidental mixes, a few nonprofit organizations, taxis, off-highway use	Same except for lost fuel and accidental mixes; lost fuel not allowed on diesel
I.	**Enforcement**	
	Destination state shipping document Import verification number	Destination state the same

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: Proposal #13
SHORT TITLE: Collect Fuel Tax at Rack
SPONSOR(S): Senators Kerr, Cochrane and Hoyle

FISCAL IMPACT: **Expenditures:** Increase ( ) Decrease ( )
Revenues: Increase (X) Decrease ( )
No Impact ( )
No Estimate Available ( )

FUND AFFECTED: **General Fund ( ) Highway Fund (X) Local Govt. ( )**
Other Funds (X) Highway Trust Fund

BILL SUMMARY: Proposal 13 changes the point of taxation for gasoline and diesel fuel to the terminal rack. Current law places motor fuel tax liability at the point of the first sale of gasoline in the state and at the first sale for highway use of diesel fuel.

EFFECTIVE DATE: January 1, 1996

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED: Department of Revenue, Motor Fuels Tax Division

FISCAL IMPACT

	FY95	FY96	FY97	FY98	FY99
REVENUES: (in $millions)					
GENERAL FUND					
HIGHWAY FUND		$7.5	$18.0	$18.4	$18.7
HIGHWAY TRUST FUND		$2.5	$ 6.0	$ 6.1	$ 6.2
LOCAL					

EXPENDITURES None

POSITIONS: None

ASSUMPTIONS AND METHODOLOGY: It is assumed that state gasoline tax collections would increase by 2% and state diesel fuel tax collections would increase by 5% upon implementation of this proposed legislation. These assumptions were based on actual collection experience of the Federal government and six other states who have already moved their point of motor fuel tax collection to the terminal rack.

SOURCES OF DATA: Internal Revenue Service; North Carolina Department of Revenue, Motor Fuels Tax Division

TECHNICAL CONSIDERATIONS:
FISCAL RESEARCH DIVISION 733-4910
PREPARED BY: Ruth Sappie
APPROVED BY:
DATE: January 6, 1995

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

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Proposal 14 (95-LCX-001(1.1))
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Revenue Laws Technical Changes. (Public)

Sponsors: Senator Cochrane; Hoyle, Kerr.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO MAKE TECHNICAL AND CLARIFYING CHANGES TO THE REVENUE LAWS AND RELATED STATUTES.

The General Assembly of North Carolina enacts:

Section 1. Effective July 1, 1995, G.S. 105-113.82(a) reads as rewritten:

"(a) Amount, Method. -- The Secretary shall distribute annually the following percentages of the net amount of excise taxes collected on the sale of malt beverages and wine during the preceding 12-month period ending March 31, less the amount of the net proceeds credited to the Department of Agriculture under ~~G.S 105-113.81A,~~ G.S. 105-113.81A, to the counties and cities in which the retail sale of these beverages is authorized:

(1) Of the tax on malt beverages levied under G.S. 105-113.80(a), twenty-three and three-fourths percent (23 3/4%);

(2) Of the tax on unfortified wine levied under G.S. 105-113.80(b), sixty-two percent (62%); and

(3) Of the tax on fortified wine levied under G.S. 105-113.80(b), twenty-two percent (22%).

If malt beverages, unfortified wine, or fortified wine may be licensed to be sold at retail in both a county and a city located in the county, both the county and city shall receive a portion of the amount distributed, that portion to be determined on the

basis of population. If one of these beverages may be licensed to be sold at retail in a city located in a county in which the sale of the beverage is otherwise prohibited, only the city shall receive a portion of the amount distributed, that portion to be determined on the basis of population. The amounts distributed under subdivisions (1), (2), and (3) shall be computed separately."

Sec. 2. G.S. 105-130.25(b) reads as rewritten:

"(b) Cogenerating Power Plant Defined. -- For purposes of this section, a cogenerating power plant is a power plant that ~~that~~ sequentially produces electrical or mechanical power and useful thermal energy from the same primary energy source. The credit allowed by this section does not apply to construction of a cogenerating power plant whose combustion equipment uses residual oil, middle distillate oil, gasoline, or liquid propane gas (LPG) as a primary fuel."

Sec. 3. G.S. 105-130.2(5c) reads as rewritten:

"(5c) State net income. -- ~~Federal~~ The taxpayer's federal taxable income as determined under the Code, adjusted as provided in G.S. 105-130.5 and, in the case of a corporation that has income from business activity that is taxable both within and without this State, allocated and apportioned to this State as provided in G.S. 105-130.4."

Sec. 4. G.S. 105-134.5 reads as rewritten:

"**§ 105-134.5. North Carolina taxable income defined.**

(a) Residents. -- For residents of this State, the term 'North Carolina taxable income' means the taxpayer's taxable income as ~~calculated~~ determined under the Code, adjusted as provided in G.S. 105-134.6 and G.S. 105-134.7.

(b) Nonresidents. -- For nonresident individuals, the term 'North Carolina taxable income' means the taxpayer's taxable income as ~~calculated~~ determined under the Code, adjusted as provided in G.S. 105-134.6 and G.S. 105-134.7, multiplied by a fraction the denominator of which is the taxpayer's gross income as ~~calculated~~ determined under the Code, adjusted as provided in G.S. 105-134.6 and G.S. 105-134.7, and the numerator of which is the amount of that gross income, as adjusted, that is derived from North Carolina sources and is attributable to the ownership of any interest in real or tangible personal property in this State or is derived from a business, trade, profession, or occupation carried on in this State.

(c) Part-year Residents. -- If an individual was a resident of this State for only part of the taxable year, having moved into

or removed from the State during the year, the term 'North Carolina taxable income' has the same meaning as in subsection (b) except that the numerator shall include gross income, adjusted as provided in G.S. 105-134.6 and G.S. 105-134.7, derived from all sources during the period the individual was a resident.

(d) S Corporations and Partnerships. -- In order to calculate the numerator of the fraction provided in subsection (b), the amount of a shareholder's pro rata share of S Corporation income that is includable in the numerator shall be the shareholder's pro rata share of the S Corporation's income attributable to the State, as defined in G.S. 105-131(b)(4). In order to calculate the numerator of the fraction provided in subsection (b) for a member of a partnership or other unincorporated business with one or more nonresident members that operates in one or more other states, the amount of the member's distributive share of income of the business that is includable in the numerator shall be determined by multiplying the total net income of the business by the ratio ascertained under the provisions of G.S. 105-130.4. As used in this subsection, total net income means the entire gross income of the business less all expenses, taxes, interest, and other deductions allowable under the Code which were incurred in the operation of the business."

Sec. 5. Effective for taxable years beginning on or after January 1, 1995, G.S. 105-134.6(c) is amended by adding a new subdivision to read:

"(7) The amount of federal estate tax that is attributable to an item of income in respect of a decedent and is deducted from gross income under section 691(c) of the Code."

Sec. 6. G.S. 105-164.4(c) reads as rewritten:

"(c) Any person who engages in any business for which a privilege tax is imposed by this Article shall apply for and obtain from the Secretary upon payment of fifteen dollars ($15.00) a license to engage in and conduct the business upon the condition that the person shall pay the tax accruing to the State under this Article; the person shall thereby be duly licensed and registered to engage in the business.

A license issued under this subsection shall be a continuing license until it becomes void or is revoked for failure to comply with the provisions of this Article. A license issued under this ~~section~~ subsection to a person, other than a person who makes only wholesale sales or only exempt sales, becomes void if, for a

period of eighteen months, the license holder files no return or files returns showing no sales.

A retailer who sells tangible personal property at a flea market shall conspicuously display the retailer's sales tax license when making sales at the flea market."

Sec. 7. G.S. 105-164.6(f) reads as rewritten:

"(f) Every retailer engaged in business in this State selling or delivering tangible personal property for storage, use, or consumption in this State shall apply for and obtain from the Secretary upon payment of fifteen dollars ($15.00) a license to engage in and conduct the business upon the condition that the person shall pay the tax accruing to the State under this Article; the person shall thereby be duly licensed and registered to engage in the business. ~~Except as hereinafter provided, a~~ A license issued under this subsection shall be a continuing license until it becomes void or is revoked for failure to comply with the provisions of this Article. A license issued under this subsection to a person, other than a person who makes only wholesale sales or only exempt sales, becomes void if, for a period of eighteen months, the license holder files no return or files returns showing no sales.

~~A license issued under this section becomes void if the license holder ceases to be engaged in a business for which a tax is imposed by this Article and remains continuously out of business for a period of five years. The burden of proving that a license is still valid is on the license holder.~~"

Sec. 8. G.S. 105-164.14 reads as rewritten:

"**§ 105-164.14. Certain refunds authorized.**

(a) Interstate Carriers. -- An interstate carrier is allowed a refund, in accordance with this section, of part of the sales and uses taxes paid by it on lubricants, repair parts, and accessories purchased in this State for a motor vehicle, railroad car, locomotive, or airplane the carrier operates. ~~Any person~~ An 'interstate carrier' is a person who is engaged in transporting persons or property in interstate commerce for ~~compensation who~~ compensation, is subject to regulation by, and to the jurisdiction of, the Interstate Commerce Commission or the United States Department of ~~Transportation and who~~ Transportation, and is required by either ~~such~~ federal agency to keep records according to ~~its standard classification of accounting~~ generally accepted accounting principles (GAAP) or, in the case of a small certificated air carrier, ~~is required by the U.S. Department of Transportation~~ to make reports of financial and operating ~~statistics, may secure a refund from the Secretary of Revenue~~

~~with respect to sales or use tax paid by such person on purchases or acquisitions of lubricants, repair parts and accessories in this State for motor vehicles, railroad cars, locomotives, and airplanes operated by such person, upon the conditions described below.~~ statistics. The Secretary ~~of Revenue~~ shall prescribe the periods of time, whether monthly, quarterly, ~~semiannually~~ semiannually, or otherwise, with respect to which refunds may be claimed, and shall prescribe the time within which, following ~~such~~ these periods, an application for refund may be made.

An applicant for refund shall furnish ~~such~~ the following information ~~as the Secretary may require,~~ and any proof of the information required by the Secretary:

(1) A list identifying the lubricants, repair parts, and accessories purchased by the applicant inside or outside this State during the refund period.

(2) The purchase price of the items listed in subdivision (1) of this subsection.

(3) The sales and use taxes paid in this State on the listed items.

(4) The number of miles the applicant's motor vehicles, railroad cars, locomotives, and airplanes were operated both inside and outside this State during the refund period.

(5) Any other information required by the Secretary.

~~including detailed information as to lubricants, repair parts and accessories wherever purchased, whether within or without the State, acquired during the period with respect to which a refund is sought, and the purchase price thereof, detailed information as to sales and use tax paid in this State thereon, and detailed information as to the number of miles such motor vehicles, railroad cars, locomotives, and airplanes were operated both within this State, and without this State, during such period, together with satisfactory proof thereof. The~~

For each applicant, the Secretary shall ~~thereupon~~ compute the amount to be refunded as follows. First, the Secretary shall determine the ratio of the number of miles the applicant operated its motor vehicles, railroad cars, locomotives, and airplanes in this State during the refund period to the number of miles it operated them both inside and outside this State during the refund period. Second, the Secretary shall determine the applicant's proportional liability for the refund period by multiplying this mileage ratio by the purchase price of the items identified in subdivision (1) of this subsection and then multiplying the resulting product by the tax rate that would have

applied to the items if they had all been purchased in this State. Third, the Secretary shall refund to each applicant the excess of the amount of sales and use taxes the applicant paid in this State during the refund period on these items over the applicant's proportional liability for the refund period. ~~tax which would be due with respect to all lubricants, repair parts and accessories acquired during the refund period as though all such purchases were made in this State, but only on such proportion of the total purchase prices thereof as the total number of miles of operation of such applicants' motor vehicles, railroad cars, locomotives, and airplanes within this State bears to the total number of miles of operation of such applicants' motor vehicles, railroad cars, locomotives and airplanes within and without this State, and such amount of sales and use tax as the applicant has paid in this State during said refund period in excess of the amounts so computed shall be refunded to the applicant.~~

(b) Nonprofit Corporations. -- The Secretary ~~of Revenue~~ shall make refunds semiannually to hospitals not operated for profit (including hospitals and medical accommodations operated by an authority created under the Hospital Authorities Law, Article 2 of Chapter 131E of the General Statutes), educational institutions not operated for profit, ~~churches, orphanages~~ and churches, orphanages, and other charitable or religious institutions and organizations not operated for profit of sales and use taxes paid under this Article, except under G.S. ~~105-164.4(4a) and G.S. 105-164.4(4c),~~ 105-164.4(a)(4a) and G.S. 105-164.4(a)(4c), by ~~such~~ these institutions and organizations on direct purchases of tangible personal property for use in carrying on the work of ~~such~~ the institutions or organizations. Sales and use tax liability indirectly incurred by ~~such~~ one of these institutions ~~and~~ or organizations on building materials, supplies, ~~fixtures~~ fixtures, and equipment ~~which shall~~ that become a part of or annexed to any building or structure that is owned or leased by the institution or organization and is being erected, ~~altered~~ altered, or repaired for ~~such~~ use by the institution or organization ~~institutions and organizations~~ for carrying on ~~their~~ its nonprofit activities ~~shall be construed as~~ is considered a sales or use tax liability incurred on direct purchases by ~~such institutions and organizations, and such the institutions and organizations may obtain refunds of such these taxes indirectly paid.~~ the institution or organization. The Secretary ~~of Revenue~~ shall also make refunds semiannually to all other hospitals not excluded by this subsection ~~(not specifically~~

~~excluded herein)~~ of sales and use tax paid by them on medicines and drugs purchased for use in carrying out ~~the work of such hospitals.~~ their work. This subsection does not apply to organizations, corporations, and institutions that are owned and controlled by the United States, the State, or a unit of local government, except hospital facilities created under Article 2 of Chapter 131E of the General Statutes and nonprofit hospitals owned and controlled by a unit of local government that elect to receive semiannual refunds under this subsection instead of annual refunds under subsection (c). ~~In order to receive the refunds herein provided for, such institutions and organizations shall file a written request for refund covering the first six months of the calendar year on or before the fifteenth day of October next following the close of said period, and shall file a written request for refund covering the second six months of the calendar year on or before the fifteenth day of April next following the close of that period. Such requests for refund shall be substantiated by such proof as the Secretary of Revenue may require, and no refund shall be made on applications not filed within the time allowed by this section and in such manner as the Secretary may require.~~ A request for a refund must be in writing and must include any information and documentation required by the Secretary. A request for a refund for the first six months of a calendar year is due the following October 15; a request for a refund for the second six months of a calendar year is due the following April 15.

(c) Certain Governmental Entities. -- A governmental entity listed in this subsection is allowed an annual refund ~~Upon receipt of timely applications for refund, the Secretary of Revenue shall make refunds annually to all governmental entities, as hereinafter defined,~~ of sales and use tax paid by it under this Article, except under G.S. ~~105-164.4(4a) and G.S. 105-164.4(4c), by said governmental entities~~ 105-164.4(a)(4a) and G.S. 105-164.4(a)(4c), on direct purchases of tangible personal property. Sales and use tax liability indirectly incurred by ~~such governmental entities~~ a governmental entity on building materials, supplies, ~~fixtures~~ fixtures, and equipment ~~which shall~~ that become a part of or annexed to any building or structure that is owned or leased by the governmental entity and is being erected, ~~altered~~ altered, or repaired ~~which is owned or leased by such governmental entities shall be construed as~~ for use by the governmental entity is considered a sales or use tax liability incurred on direct purchases by the governmental entity for the purpose of this subsection. ~~such governmental entities, and such~~

~~entities may obtain refunds of such taxes indirectly paid. The refund provisions contained in this subsection shall not apply to any governmental entities not specifically named herein. In order to receive the refund~~ A request for a refund must be in writing and must include any information and documentation required by the Secretary. A request for a refund is due within six months after the end of the governmental entity's fiscal year. ~~herein provided for, governmental entities shall file a written request for said refund within six months of the close of the fiscal year of the governmental entities seeking said refund, and such request for refund shall be substantiated by such records, receipts and information as the Secretary may require. No refunds shall be made on applications not filed within the time allowed by this section and in such manner as the Secretary may otherwise require. The term "governmental entities," for the purposes of this subsection, shall mean~~

This subsection applies only to the following governmental entities:

(1) A county.
(2) A city as defined in G.S. 160A-1.
(3) A metropolitan sewerage district or a metropolitan water district in this State.
(4) A water and sewer authority created under Chapter 162A of the General Statutes.
(5) A lake authority created by a board of county commissioners pursuant to an act of the General Assembly.
(6) A sanitary district.
(7) A regional solid waste management authority created pursuant to G.S. 153A-421.
(8) An area mental health, developmental disabilities, and substance abuse authority, other than a single-county area authority, established pursuant to Article 4 of Chapter 122C of the General Statutes.
(9) A district health department.
(10) A regional council of governments created pursuant to G.S. 160A-470.
(11) A regional planning and economic development commission or a regional economic development commission created pursuant to Chapter 158 of the General Statutes.
(12) A regional planning commission created pursuant to G.S. 153A-391.

(13) A regional sports authority created pursuant to G.S. 160A-479.
(14) A public transportation authority created pursuant to Article 25 of Chapter 160A of the General Statutes.
(15) A regional public transportation authority created pursuant to Article 26 of Chapter 160A of the General Statutes.
(16) A local airport authority that was created pursuant to a local act of the General Assembly and has at least one of the following characteristics:
a. It has all of the rights of a municipality.
b. A local act of the General Assembly declares it to be a municipality.
c. A local act of the General Assembly specifically authorizes it to receive a refund under this section.
(17) A joint agency created by interlocal agreement pursuant to G.S. 160A-462 to operate a public broadcasting television station.
(18) The North Carolina Low-Level Radioactive Waste Management Authority created pursuant to Chapter 104G of the General Statutes.
(19) The North Carolina Hazardous Waste Management Commission created pursuant to Chapter 130B of the General Statutes.
(20) A constituent institution of The University of North Carolina, but only with respect to sales and use tax paid by it for tangible personal property acquired by it through the expenditure of contract and grant funds.

~~all counties, incorporated cities and towns, water and sewer authorities created and existing under the provisions of Chapter 162A of the General Statutes, lake authorities created by a board of county commissioners pursuant to an act of the General Assembly, sanitary districts, regional councils of governments created pursuant to G.S. 160A-470, area mental health, developmental disabilities, and substance abuse authorities (other than single-county area authorities) established pursuant to Article 4 of Chapter 122C of the General Statutes, district health departments, regional planning and economic development commissions created pursuant to G.S. 158-14, regional sports authorities created pursuant to G.S. 160A-479, regional economic development commissions created pursuant to G.S. 158-8, regional~~

~~planning commissions created pursuant to G.S. 153A-391, regional solid waste management authorities created pursuant to G.S. 153A-421, public transportation authorities created pursuant to Article 25 of Chapter 160A of the General Statutes, regional public transportation authorities created pursuant to Article 26 of Chapter 160A of the General Statutes, metropolitan sewerage districts and metropolitan water districts in this State, the North Carolina Low-Level Radioactive Waste Management Authority created pursuant to Chapter 104G of the General Statutes, the North Carolina Hazardous Waste Management Commission created pursuant to Chapter 130B of the General Statutes, a joint agency created by interlocal agreement pursuant to G.S. 160A-462 to operate a public broadcasting television station, and the Rockingham County Airport Authority. Notwithstanding the foregoing provisions of this subsection, the constituent institutions of The University of North Carolina may obtain in the manner prescribed by this subsection a refund of sales and use tax paid by them on or after January 1, 1992, for tangible personal property acquired by them through the expenditure of contract and grant funds.~~

(d) Penalties for Late Applications. -- Refunds made pursuant to applications filed after the dates specified in subsections (b) and (c) above ~~shall be~~ are subject to the following penalties for late filing: applications filed within 30 days after ~~said dates,~~ the due date, twenty-five percent (25%); applications filed after 30 days but within six months after ~~said dates,~~ the due date, fifty percent (50%). ~~However, refunds which are~~ Refunds applied for ~~after~~ more than six ~~months following said dates shall be~~ months after the due date are barred.

(e) State Agencies. -- The State is allowed quarterly refunds of local sales and use taxes paid by a State agency on direct purchases of tangible personal property and local sales and use taxes paid indirectly by the State agency on building materials, supplies, fixtures, and equipment that become a part of or annexed to a building or structure that is owned or leased by the State agency and is being erected, altered, or repaired ~~and is owned or leased~~ for use by the State agency. This subsection does not apply to purchases for which a State agency is allowed a refund under subsection (c) of this section.

A person who pays local sales and use taxes on building materials or other tangible personal property for a State building project shall give the State agency for whose project the property was purchased a signed statement containing all of the following information:

(1) The date the property was purchased.
(2) The type of property purchased.
(3) The project for which the property was used.
(4) If the property was purchased in this State, the county in which it was purchased.
(5) If the property was not purchased in this State, the county in which the property was used.
(6) The amount of sales and use taxes paid.

If the property was purchased in this State, the person shall attach a copy of the sales receipt to the statement. A State agency to whom a statement is submitted shall verify the accuracy of the statement.

Within 15 days after the end of each calendar quarter, every State agency shall file with the Secretary a written application for a refund of taxes to which this subsection applies paid by the agency during the quarter. The application shall contain all information required by the Secretary. The Secretary shall credit the local sales and use tax refunds directly to the General Fund."

Sec. 9. Effective for taxable years beginning on or after January 1, 1995, G.S. 105-228.90(b)(1) reads as rewritten:

"(1) Code. -- The Internal Revenue Code as enacted as of January 1, ~~1994,~~ 1995, including any provisions enacted as of that date which become effective either before or after that date."

Sec. 10. G.S. 105-241.2(a) reads as rewritten:

"(a) Petition for Administrative Review. -- Without having to pay the tax or additional tax assessed by the Secretary under this Chapter, any taxpayer may obtain from the Tax Review Board an administrative review with respect to the taxpayer's liability for the tax or additional tax assessed by the Secretary. Such a review may be obtained only if the taxpayer has obtained a hearing before the Secretary and the Secretary has rendered a final decision with respect to the taxpayer's liability. If a taxpayer has made a timely written demand for refund of an alleged overpayment and the Secretary has issued a decision denying part or all of the claimed refund, the taxpayer may obtain from the Tax Review Board an administrative review of the Secretary's decision. To obtain administrative review the taxpayer must take the following actions:

(1) Within 30 days after the Secretary's final decision is issued, file with the Tax Review Board, with a copy to the Secretary, notice of intent to file a petition for review.

(2) Within 60 days after ~~the Secretary's final decision is issued,~~ filing a notice of intent under subdivision (1) of this subsection, file with the Tax Review Board, with a copy to the Secretary, a petition requesting administrative review and stating in concise terms the grounds upon which review is sought."

Sec. 11. G.S. 105-259(b) is amended by adding the following new subdivisions to read:

"(11a) To provide a copy of a return to the taxpayer who filed the return.

(11b) In the case of a return filed by a corporation, a partnership, a trust, or an estate, to provide a copy of the return or information on the return to a person who has a material interest in the return if, under the circumstances, section 6103(e)(1) of the Code would require disclosure to that person of any corresponding federal return or information.

(11c) In the case of a return of an individual who is legally incompetent or deceased, to provide a copy of the return to the legal representative of the estate of the incompetent individual or decedent."

Sec. 12. G.S. 105-434(a) reads as rewritten:

"(a) Tax. -- An excise tax is levied on motor fuel sold, distributed, or used by a distributor within this State at a flat rate of seventeen and one-half cents (17 1/2¢) per gallon, plus a variable rate of either three and one-half cents (3 1/2¢) per gallon or seven percent (7%) of the average wholesale price of motor fuel for the applicable base period, whichever is greater. The Secretary of Revenue shall semiannually determine the average wholesale price of motor fuel using information on refiner and gas plant operator sales prices of finished motor gasoline and No. 2 diesel fuel for resale, published by the United States Department of Energy in the 'Monthly Energy Review,' or equivalent data. The Secretary shall determine the average wholesale price of motor fuel by computing the average sales price of finished motor gasoline for the base period, computing the average sales price for No. 2 diesel fuel for the base period, and then computing a weighted average of the results of the first two computations based on the proportion of tax collected under this Article on motor fuel and Article 36A on fuel for the base period. The Secretary shall notify affected

taxpayers of the tax rate to be in effect for each six-month period beginning January 1 and July 1.

To facilitate administration of the motor fuel tax, the Secretary shall convert the wholesale percentage component to a cents-per-gallon rate. The rate for the six-month period beginning January 1 shall be computed from data published for the six-month base period ending on the preceding September 30, and the rate for the six-month period beginning July 1 shall be computed from data published for the six-month base period ending on the preceding March 31. The cents-per-gallon rate computed by the Secretary shall be rounded to the nearest one-tenth of a cent (1/10¢). If the cents-per-gallon rate computed by the Secretary is exactly between ~~two tenths~~ two-tenths of a cent, the rate shall be rounded up to the higher of the two."

Sec. 13. G.S. 105-449.20 reads as rewritten:

"**§ 105-449.20. When Secretary may estimate tax liability of supplier or user-seller.**

Whenever a supplier or a user-seller fails to file a report under G.S. 105-449.19 or G.S. 105-449.21 or files a false report under one of those statutes, the Secretary shall determine, from any information obtainable, the number of gallons of fuel with respect to which the supplier or user-seller owes tax under this Article. When a user-seller sells or uses more fuel than the user-seller reports to the Secretary as having been purchased from a supplier, the user-seller is presumed to have acquired the unreported fuel tax-free to operate a motor vehicle. When a user-seller sells or uses more fuel to operate a motor vehicle than the user-seller reports to the Secretary as having been purchased from a supplier to operate a motor vehicle, the user-seller is presumed to have acquired tax-free to operate a motor vehicle all fuel not reported as having been acquired to operate a motor vehicle."

Sec. 14. G.S. 153A-158 reads as rewritten:

"**§ 153A-158. Power to acquire ~~property in other counties.~~ property.**

A county may acquire, by gift, grant, devise, bequest, exchange, purchase, lease, or any other lawful method, the fee or any lesser interest in real or personal property for use by the county or any department, board, commission, or agency of the county. In exercising the power of eminent domain a county shall use the procedures of Chapter 40A."

Sec. 15. (a) Chapter 885 of the 1989 Session Laws, as amended by Chapters 120, 533, 832, 848, 865, and 1001 of the 1991 Session Laws, as codified as G.S. 153A-157, and as further

amended by Chapters 611, 612, 614, 622, 623, 642, and 655 of the 1993 Session Laws, is recodified as G.S. 153A-158.1(a).

(b) G.S. 153A-158.1, as amended by subsection (a) of this section, reads as rewritten:

"~~§ 153A-158.1. School property in certain counties; construction and other improvements; transfers.~~ Acquisition and improvement of school property in certain counties.

(a) ~~Power to acquire property in certain counties.~~ Acquisition By County. -- A county may ~~acquire, by gift, grant, devise, bequest, exchange, purchase, lease, or any other~~ acquire, by any lawful method, ~~the fee or any other lesser~~ any interest in real or personal property for use by ~~the county or any department, board, commission, or agency of the county or~~ a school administrative unit within the county. In exercising the power of eminent domain a county shall use the procedures of Chapter 40A. ~~The~~ The county shall use its authority under this ~~section~~ subsection to acquire ~~the fee or any lesser interest in real or personal~~ property for use by a school administrative unit within the county only upon the request of the board of education of that school administrative unit and after a public hearing.

~~This section applies to Ashe, Avery, Bladen, Brunswick, Cabarrus, Carteret, Chowan, Columbus, Duplin, Forsyth, Franklin, Harnett, Haywood, Iredell, Johnston, Lee, Macon, Nash, Orange, Pasquotank, Pender, Richmond, Rowan, Sampson, and Stanly Counties.~~

(b) Construction or Improvement By County. -- A county may construct, equip, expand, improve, renovate, or otherwise make available property for use by a school administrative unit within the county. ~~This subsection applies only to Ashe, Avery, Brunswick, Chowan, Forsyth, Harnett, Haywood, Lee, Macon, Nash, Orange, Pasquotank, Richmond, and Sampson Counties and to local boards of education for school administrative units in or for Ashe, Avery, Brunswick, Chowan, Forsyth, Harnett, Haywood, Lee, Macon, Nash, Orange, and Pasquotank Counties.~~

(c) Lease or Sale by Board of Education. -- Notwithstanding the provisions of G.S. 115C-518 and G.S. 160A-274, a local board of education ~~may~~ may, in connection with additions, improvements, renovations, or repairs to all or part of any of its property, lease or sell ~~any of its~~ the property to the board of commissioners of the county in which the property is located for any price negotiated between the two boards. ~~This subsection applies only to Ashe, Avery, Brunswick, Cabarrus, Carteret, Chowan, Duplin, Forsyth, Harnett, Haywood, Iredell, Lee, Macon, Nash, Orange, Pasquotank, Rowan, Sampson, and Stanley Counties~~

~~and to local boards of education for school administrative units in or for these counties. This subsection applies only to sales and leases of property in connection with additions, improvements, renovations, or repairs to the property or to some part of the property.~~

(d) Board of Education May Contract for Construction. -- Notwithstanding the provisions of G.S. 115C-40 and G.S. 115C-521, ~~local boards of education are authorized to~~ a local board of education may enter into contracts for the erection or repair of school buildings upon sites owned in fee simple by one or more counties in which the local school administrative ~~units are~~ unit is located. ~~This subsection applies only to Ashe, Avery, Brunswick, Chowan, Forsyth, Harnett, Lee, Nash, Orange, Pasquotank, and Sampson Counties and to local boards of education for school administrative units in or for those counties.~~

(e) Scope. -- This section applies to Ashe, Avery, Bladen, Brunswick, Cabarrus, Carteret, Chowan, Columbus, Duplin, Forsyth, Franklin, Harnett, Haywood, Iredell, Johnston, Lee, Macon, Nash, Orange, Pasquotank, Pender, Richmond, Rowan, Sampson, Stanly, and Watauga Counties."

Sec. 16. As amended by this act, G.S. 153A-158.1 now incorporates and codifies, in addition to Chapter 885 of the 1989 Session Laws as amended, the following: Chapter 487 of the 1989 Session Laws, Sections 2 and 3 of Chapter 848 of the 1991 Session Laws, Sections 2 and 3 of Chapter 1001 of the 1991 Session Laws, Sections 2 and 3 of Chapter 611 of the 1993 Session Laws, Sections 2, 3, and 4 of Chapter 612 of the 1993 Session Laws, Sections 3, 4, and 5 of Chapter 614 of the 1993 Session Laws, Sections 2, 3, and 4 of Chapters 622 and 623 of the 1993 Session Laws, Section 3(c), Section 3(e), and the first sentence of Section 3(b) of Chapter 642 of the 1993 Session Laws, and Sections 2, 3, and 4 of Chapter 655 of the 1993 Session Laws.

Sec. 17. Section 4 of Chapter 681 of the 1993 Session Laws reads as rewritten:

"Sec. 4. This act is effective for taxable years beginning on or after January 1, ~~1994.~~ 1994, and ending on or before February 28, 1996."

Sec. 18. Effective January 1, 1995, Section 14 of Chapter 745 of the 1993 Session Laws is repealed.

Sec. 19. Section 1 of Chapter 922 of the 1989 Session Laws reads as rewritten:

"Section 1. Part IV of Chapter 908 of the 1983 Session Laws, as amended by Chapter 821 of the 1989 Session Laws, is further

amended by adding at the end of Section 7 a new subsection to read:

'(d) Refunds. -- The local administrative authority shall refund to a nonprofit or governmental entity the prepared food and beverage tax paid by the entity on eligible purchases of prepared foods and beverages. A nonprofit or governmental entity's purchase of prepared food and beverages is eligible for a refund under this subsection if the entity is entitled to a refund under G.S. ~~105-164.14~~ 105-164.14(b) or (c) of the sales and use tax paid on the purchase. The time limitations, application requirements, penalties, and restrictions provided in G.S. 105-164.14(b) and (d) ~~shall~~ apply to refunds to nonprofit entities; the time limitations, application requirements, penalties, and restrictions provided in G.S. 105-164.14(c) and (d) ~~shall~~ apply to refunds to governmental entities. When an entity applies for a refund of the prepared food and beverages tax paid by it on purchases, it shall attach to its application a copy of the application submitted to the Department of Revenue under G.S. 105-164.14 for a refund of the sales and use tax on the same purchases. An applicant for a refund under this subsection shall provide any information required by the local administrative authority to substantiate the claim.'"

Sec. 20. Subsection 4(e) of Chapter 449 of the 1985 Session Laws, as amended by Chapter 826 of the 1985 Session Laws and Chapter 177 of the 1991 Session Laws, reads as rewritten:

"(e) Refunds. -- The county shall refund to a nonprofit or governmental entity the prepared food and beverage tax paid by the entity on eligible purchases of prepared food and beverages. A nonprofit or governmental entity's purchase of prepared food and beverages is eligible for a refund under this subsection if the entity is entitled to a refund under G.S. ~~105-164.14~~ 105-164.14(b) or (c) of the sales and use tax paid on the purchase. The time limitations, application requirements, penalties, and restrictions provided in G.S. 105-164.14(b) and (d) ~~shall~~ apply to refunds to nonprofit entities; the time, limitations, application requirements, penalties, and restrictions provided in G.S. 105-164.14(c) and (d) ~~shall~~ apply to refunds to governmental entities. When an entity applies for a refund of the prepared food and beverages tax paid by it on purchases, it shall attach to its application a copy of the application submitted to the Department of Revenue under G.S. 105-164.14 for a refund of the sales and use tax on the same purchases. An applicant for a refund under this subsection shall provide any information required by the county to substantiate the claim."

Sec. 21. Section 6 of Chapter 413 of the 1993 Session Laws reads as rewritten:

"Sec. 6. Refunds. -- The county shall refund to a nonprofit or governmental entity the prepared food and beverage tax paid by the entity on eligible purchases of prepared food and beverages. A nonprofit or governmental entity's purchase of prepared food and beverages is eligible for a refund under this section if the entity is entitled to a refund under G.S. ~~105-164.14~~ 105-164.14(b) or (c) of ~~local~~ the sales and use tax paid on the purchase. The time limitations, application requirements, penalties, and restrictions provided in G.S. 105-164.14(b) and (d) ~~shall~~ apply to refunds to nonprofit entities; the time, limitations, application requirements, penalties, and restrictions provided in G.S. ~~105-164.14(c), (d), and (e)~~ 105-164.14(c) and (d) ~~shall~~ apply to refunds to governmental entities. When an entity applies for a refund of the prepared food and beverages tax paid by it on purchases, it shall attach to its application a copy of the application submitted to the Department of Revenue under G.S. 105-164.14 for a refund of the sales and use tax on the same purchases. An applicant for a refund under this section shall provide any information required by the county to substantiate the claim."

Sec. 22. Subsection 1(f) of Chapter 449 of the 1993 Session Laws reads as rewritten:

"(f) Refunds. -- The town shall refund to a nonprofit or governmental entity the prepared food and beverage tax paid by the entity on eligible purchases of prepared food and beverages. A nonprofit or governmental entity's purchase of prepared food and beverages is eligible for a refund under this subsection if the entity is entitled to a refund under G.S. ~~105-164.14~~ 105-164.14(b) or (c) of ~~local~~ the sales and use tax paid on the purchase. The time limitations, application requirements, penalties, and restrictions provided in G.S. 105-164.14(b) and (d) ~~shall~~ apply to refunds to nonprofit entities; the time, limitations, application requirements, penalties, and restrictions provided in G.S. ~~105-164.14(c), (d), and (e)~~ 105-164.14(c) and (d) ~~shall~~ apply to refunds to governmental entities. When an entity applies for a refund of the prepared food and beverage tax paid by it on purchases, it shall attach to its application a copy of the application submitted to the Department of Revenue under G.S. 105-164.14 for a refund of the sales and use tax on the same purchases. An applicant for a refund under this subsection shall provide any information required by the town to substantiate the claim."

Sec. 23. Chapters 781 and 782 of the 1971 Session Laws are repealed.

Sec. 24. Except as otherwise provided in this act, this act is effective upon ratification.

Explanation of Proposal 14

This proposal makes numerous technical and clarifying changes to the revenue laws and related statutes. The following table provides a section-by-section analysis of the proposed changes.

Section	Explanation
1	Adds a missing period in the phrase "G.S".
2	Deletes a duplicate word.
3 - 4	Clarifies that a taxpayer's federal taxable income, used as a starting point for North Carolina corporate and individual income tax, is to be determined in accordance with the Internal Revenue Code.
5	Requires a taxpayer to add to State taxable income the amount of any federal estate tax paid on an item of income in respect of a decedent that is included in federal taxable income. Under current law, taxpayers are allowed an income tax deduction for both State inheritance tax paid on an item of income in respect of a decedent and federal estate tax paid on the same item of income in respect of a decedent. Allowing a State deduction for a federal tax is contrary to the tax structure of the State and is the result of an oversight. This proposal corrects this oversight by repealing the deduction for federal estate tax but retaining the deduction for State inheritance tax paid on an item of income in respect of a decedent. Income in respect of a decedent is income to which a person was entitled when the person died. An example of an item of income in respect of a decedent is the gain from an installment sale made by the decedent before death. This income is subject to inheritance tax upon the death of the decedent as part of the decedent's property. An income tax deduction is allowed for the inheritance tax paid on an item of income in respect of a decedent to prevent double taxation.
6	Changes the word "section" to "subsection."
7	Makes a conforming change to the use tax statutes. In 1993, upon recommendation of the Revenue Laws Study Committee, the General Assembly enacted legislation providing that a retailer's sales tax license

Section	Explanation
	becomes void if, for a period of 18 months, the retailer does not file any returns showing taxable sales. This section makes the same change to the corresponding retail use tax license.
8	Corrects two incorrect cross-references and reorganizes and modernizes the current law allowing certain entities refunds of sales and use taxes.
9	Rewrites the definition of the Internal Revenue Code used in State tax statutes to change the reference date from January 1, 1994, to January 1, 1995. Updating the Internal Revenue Code reference makes recent amendments to the Code applicable to the State to the extent that State tax law previously tracked federal law. This update has the greatest effect on State corporate and individual income taxes because these taxes are based on federal taxable income and are therefore closely tied to federal law. The franchise tax, gift tax, highway use tax, inheritance tax, insurance company premiums tax, and intangibles tax also determine some exemptions based on the provisions of the Code. This year, because the federal government has not enacted any changes to the Code that affect our statutes, the update has no substantive effect and is merely a technical change.
10	Restores the correct time period for filing a petition for administrative review with the tax review board. This time period was inadvertently shortened in a rewrite of the statute enacted in 1993.
11	Adds three new exceptions to the prohibition against disclosing confidential tax information. The State's Tax Secrecy Act, G.S. 105-259, prohibits the disclosure of a taxpayer's tax information except in specified circumstances. The act fails to provide that the Department of Revenue may share a copy of a tax return with the taxpayer who filed it. This section corrects this problem in three ways: it allows the Department to provide a copy of a tax return (1) to the taxpayer who filed it, (2) to the legal representative of the estate of the taxpayer if the taxpayer is incompetent or deceased, or (3), in the case of a return filed by a partnership, a corporation, an estate, or a trust, to a "person having a material interest" as determined under the Code. A person having a material interest would be, for example, a partner in the partnership that filed the return, a corporate agent designated by the corporation's board of directors or CEO, a corporate shareholder with more than 1% of the outstanding stock, a shareholder in a Subchapter S corporation, the executor of an estate, or the trustee of a trust.

Section	Explanation
12	Adds a missing hyphen.
13	Restores a missing portion of a cross-reference.
14 - 16	Consolidates, codifies, and conforms various local acts that authorize certain counties to acquire and improve public school property on behalf of their local school boards. These existing local acts authorize the named counties to finance school construction projects through lease-purchase. This section eliminates the confusion of having numerous similar local acts scattered throughout the Session Laws and provides that clarifying language that was included only in some of the more recent local acts will apply equally to all affected counties.
17	Chapter 681 of the 1993 Session Laws revised the State Ports Tax Credit. Because that tax credit expires for tax years ending after 2/28/96, the revisions to the credit need to expire at the same time.
18	Repeals a Session Law that duplicates another Session Law; both laws revised G.S. 105-241.1(e).
19 - 22	Clarifies that refunds of local meals taxes must be made only to certain nonprofit and government entities to the same extent as State sales tax refunds. The following local governments are currently authorized to levy a meals tax: Charlotte/Mecklenburg County, Dare County, Wake County, Cumberland County, and the Town of Hillsborough.
23	Repeals two 1971 acts that gave Nash County and Edgecombe County a special 1¢ local option sales tax as an alternative to the 1¢ local option sales tax enacted for all counties. These local acts provided that each county could levy or repeal the tax only if the other took the same action. These alternate local options were never exercised and are no longer viable because of subsequent changes in the State and local sales tax laws.
24	Provides that the act is effective upon ratification.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

S **D**

Proposal 15 (95-RBX-08)
THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION

Short Title: Correct Income Tax Penalty. (Public)

Sponsors: Senator Kerr.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO CLARIFY CALCULATION OF THE THRESHOLD USED TO DETERMINE WHEN A HIGHER INCOME TAX PENALTY APPLIES FOR NEGLIGENT FAILURE TO PAY THE AMOUNT OF TAX DUE.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-236(5) reads as rewritten:

"(5) Negligence. -- For negligent failure to comply with any of the provisions of this ~~Subchapter, or rules and regulations issued pursuant thereto,~~ Subchapter or rules issued under it, without intent to defraud, there shall be assessed, as a penalty, an additional tax of ten percent (10%) of the deficiency due to ~~such negligence; provided, that in~~ the negligence.

In the case of income tax, if ~~gross income is understated by as much as twenty-five percent (25%), or deductions, exclusive of personal exemptions, are overstated by as much as twenty-five percent (25%) of gross income, or if there is a combination of understatement of gross income and overstatement of deductions, exclusive of personal exemptions, equaling twenty-five percent (25%) of gross income, there shall be assessed, as a penalty, an additional tax equal to twenty-five percent (25%) of the total deficiency;~~

~~provided further, that in~~ a taxpayer understates gross income, overstates deductions from gross income, other than personal exemptions, makes erroneous adjustments to federal taxable income, or does any combination of these, and the combined errors equal or exceed twenty-five percent (25%) of gross income, the penalty assessed shall be twenty-five percent (25%) of the deficiency. For purposes of this subdivision, 'gross income' means gross income as defined in section 61 of the Code and 'deductions' means deductions allowed in arriving at federal taxable income.

In the case of sales and use taxes, if ~~it is established that the~~ a taxpayer understates total tax liability ~~is understated~~ by twenty-five percent (25%) or more as a result of ~~any~~ one or more of the following, the penalty assessed shall be twenty-five percent (25%) of the total deficiency:

a. Omission or understatement of gross sales, gross ~~receipts~~ receipts, or gross ~~purchases;~~ purchases.

b. Overstatement of exemptions or ~~deductions;~~ deductions.

c. Incorrect application of a lesser rate of tax. ~~tax; or~~

~~d. Any combination of the foregoing; there shall be assessed as a penalty an additional tax equal to twenty-five percent (25%) of the total deficiency. If a penalty is assessed under subdivision (6) of this section, no additional penalty for negligence shall be assessed with respect to the same deficiency.~~"

Sec. 2. This act is effective upon ratification and applies to taxable years beginning on or after January 1, 1995.

Explanation of Proposal 15

Proposal 15, recommended by the Department of Revenue, will allow the Secretary of Revenue to assess a negligence penalty for reporting improper adjustments to federal taxable income to the same extent that the Secretary can assess a penalty for understating gross income or overstating deductions. The negligent adjustments could be in the form of an understatement of additions made to federal taxable income or an overstatement of deductions made to federal taxable income. The proposal would become effective beginning with the 1995 taxable year.

Under the general administrative provisions of the Revenue Act, a penalty equal to 10% of a deficiency caused by negligently failing to comply with any of the tax provisions is imposed. In the case of income tax, the penalty amount is 25% of the amount of the deficiency if gross income is negligently understated by more than 25%, or if deductions, exclusive of personal exemptions, are negligently overstated by more than 25%.

Under current law, individual and corporate income taxes are based on federal taxable income. Federal taxable income is adjusted in accordance with State tax law to determine a taxpayer's North Carolina taxable income. As the 25% penalty provisions now read, the penalty is assessed against deficiencies caused by understating gross income or by overstating deductions, both of which are determined on the federal return. The penalty provisions do not address deficiencies caused by improper adjustments to federal taxable income: adjustments that are made at the State level to determine North Carolina taxable income. Under this proposal, the Secretary could assess the negligence penalty for deficiencies in income tax payments negligently caused by erroneous adjustments made to federal taxable income.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: PROPOSAL 15
SHORT TITLE: INCOME TAX TECHNICAL CHANGES

FISCAL IMPACT: **Revenues:** Insignificant Impact (X)

FUND AFFECTED: General Fund (X)

BILL SUMMARY: Makes the following technical change to the state personal income tax:

The State income tax calculation starts with federal taxable income and requires certain additions and deductions from this base figure. The proposal would allow the Secretary of Revenue to assess an income tax negligence penalty for reporting improper adjustments to federal taxable income (favorable to the taxpayer) to the same extent the Secretary can assess a penalty for understating gross income or overstating deductions.

EFFECTIVE DATE: Tax years beginning on or after January 1, 1995.

ASSUMPTIONS AND METHODOLOGY: Conclusion based on discussions with Department of Revenue

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: Dave Crotts
APPROVED BY:
DATE: December 1, 1994
[FRD#001]

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H **D**

Proposal 16
HOUSE JOINT RESOLUTION 95-LC-031(1.1)
(THIS IS A DRAFT AND NOT READY FOR INTRODUCTION)

Sponsors: Representatives Gamble; Arnold, Luebke, Ramsey, and Tallent.

Referred to:

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

Whereas, the Legislative Research Commission has been authorized by the 1977, 1979, 1981, 1983, 1985, 1987, 1989, 1991, and 1993 General Assemblies to conduct a study of the revenue laws of North Carolina; and

Whereas, since 1977 the committee appointed by the Legislative Research Commission to study the revenue laws has recommended many changes in the revenue laws in the committee's attempt to improve these laws; and

Whereas, the Revenue Laws Study Committee has proved to be an excellent forum for both taxpayers and tax administrators to present their complaints about existing law and make suggestions to improve the law;

Now, therefore, be it resolved by the House of Representatives, the Senate concurring:

Section 1. The Legislative Research Commission is authorized to study the revenue laws of North Carolina and the administration of these laws. The Commission may review the State's revenue laws to determine which laws need clarification, technical amendment, repeal, or other change to make the laws concise, intelligible, easy to administer, and equitable. When the recommendations of the Commission, if enacted, would result

in an increase or decrease in State tax revenues, the report of the Commission shall include an estimate of the amount of the increase or decrease.

Sec. 2. The Commission may call upon the Department of Revenue to cooperate with it in its study of the revenue laws. The Secretary of Revenue shall ensure that the Department's staff cooperates fully with the Commission.

Sec. 3. The Commission shall make a final report of its recommendations for improvement of the revenue laws to the 1997 General Assembly and may make an interim report to the 1996 Session of the 1995 General Assembly.

Sec. 4. This resolution is effective upon ratification.

Explanation of Proposal 16

This joint resolution simply authorizes the Legislative Research Commission to continue to study the revenue laws of this State. The resolution gives the study of the revenue laws a broad scope and permits the Commission to make an interim report to the 1996 Session of the 1995 General Assembly and a final report to the 1996 General Assembly on the results of its study of the revenue laws.

APPENDIX A

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1993

H 2

House Bill 1319
Committee Substitute Favorable 7/24/93

Short Title: The Studies Act of 1993. (Public)

Sponsors:

Referred to:

June 1, 1993

A BILL TO BE ENTITLED

AN ACT TO AUTHORIZE STUDIES BY THE LEGISLATIVE RESEARCH COMMISSION, TO CREATE AND CONTINUE VARIOUS COMMITTEES AND COMMISSIONS, AND TO DIRECT VARIOUS STATE AGENCIES TO STUDY SPECIFIED ISSUES.

The General Assembly of North Carolina enacts:

PART I.-----TITLE

Section 1. This act shall be known as "The Studies Act of 1993".

PART II.-----LEGISLATIVE RESEARCH COMMISSION

Sec. 2.1. The Legislative Research Commission may study the topics listed below. Listed with each topic is the 1993 bill or resolution that originally proposed the issue or 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) Education Support Services (H.B. 11 - Fussell, S.B. 13 - Martin of Guilford),

(2) Water Issues-Surface Water and Groundwater -- study continued (H.J.R. 52 - Fussell, S.J.R. 67 - Tally),

(3) Alternative Approaches to Deal with Discrimination in Employment -- study continued (H.B. 54 - Kennedy),

(4) Solid Waste Management -- study continued (H.J.R. 69 - R. Thompson, S.J.R. 56 - Odom),
(5) Emergency Management Issues -- study continued (H.B. 88 - Hightower, S.B. 75 - Parnell),
(6) State Real Property Transfers -- study continued and expanded, (H.B. 92 - Bowman, S.B. 756 - Sherron).
(7) Ways to Promote Energy Conservation and the Use of Renewable Sources of Energy in North Carolina -- study continued (H.J.R. 104 and H.J.R. 150 - Bowman, S.B. 337 - Plexico),
(8) Mountain Area Study (H.B. 117 - Crawford, S.B. 85 - Hyde),
(9) Revenue Laws -- study continued (H.J.R. 123 - Jarrell),
(10) Criminal Case Disposition (H.B. 127 - Michaux, S.B. 250 - Soles),
(11) State Parks and Recreation Areas (H.B. 149 - DeVane),
(12) Information Technology (H.B. 172 - Bowman, S.B. 741 - Sherron),
(13) Fire and Occupational Safety Issues -- study continued (H.J.R. 191 - Fitch, S.J.R. 107 - Plyler),
(14) State Personnel (H.B. 196 - Fitch, S.B. 119 - Johnson),
(15) Child Care Issues (H.B. 213 - Rogers, S.B. 89 - Walker),
(16) Need to Establish a College of Chiropractic in North Carolina (H.B. 224 - Black, S.B. 223 - Conder),
(17) Immunity from Liability Resulting from Negligent Acts (H.B. 242 - Nye and Jeffus),
(18) Fiscal Trends and Reform (H.B. 267 - Diamont, S.B. 194 - Perdue),
(19) Child Support (H.B. 272 - Diamont, S.B. 314 - Martin of Guilford),
(20) Public Health Programs Organization (H.B. 289 - Blue, S.B. 298 - Martin of Guilford),
(21) Reducing the Legal Limit of Blood Alcohol from 0.10 to 0.02 for 18 to 20 Year Olds While Driving a Motor Vehicle (H.B. 366 - Easterling),
(22) Model Employment Termination Act (H.B. 384 - Beall),
(23) Recycling and Composting Poultry Mortalities (H.B. 421 - James),
(24) Unfunded Mandates to Counties and Cities (H.B. 433 - Joye),
(25) Ways to Improve Guardianship Services (H.B. 451 - Gottovi),
(26) Law Regulating Mortgage Bankers and Mortgage Brokers (H.B. 464 - Smith and Brubaker),
(27) Development of a Lead Hazard Management Program in the State (H.B. 623 - Moore),
(28) Family Law Reform (H.J.R. 705 - R. Thompson),
(29) Health and Fitness Club Issues (H.J.R. 714 - G. Thompson),
(30) Bid Laws and Reciprocity (H.B. 716 - Daughtry),
(31) Voter Registration (H.B. 778 - Michaux),
(32) Rental Vehicle Insurance (H.B. 798 - Stamey),
(33) Emergency Cardiac Care (H.J.R. 805 - Green),

(34) Need for a Property Owners' Association Act (H.B. 919 - R. Thompson),
(35) Tobacco Warehouse (H.B. 889 - Bowen),
(36) All-Terrain Vehicles Licensing and Regulation (H.B. 1006 - Smith),
(37) Public Assistance Direct Deposit (H.B. 1022 - Spears),
(38) Residential Property Disclosure Act (H.B. 1032 - Hensley),
(39) Professional Firefighters Early Retirement Incentives (H.B. 1033 - Hensley,
(40) Restitution Policy as a Part of Criminal Justice System (H.B. 1035 - Michaux),
(41) Farmland Preservation Enabling Act, including Dairy Farmer Economic Issues (H.J.R. 1060 - Colton),
(42) Alcoholic Beverage Control Laws (H.B. 1093 - Hensley),
(43) Literacy (H.B. 1131 - Gottovi),
(44) Business Tax Credits for Purchases of Recycled Products (H.B. 1132 - Gottovi),
(45) Divorce Education Program for Couples with Children (H.B. 1148 - Alexander),
(46) Recreational Hook-and-Line Fishing License in Coastal Fishing Waters and Use of Commercial Nets (H.B. 1156 - Bowman),
(47) Insurance Coverage for Biologically Based Brain Diseases (H.B. 1161 - Alexander),
(48) Bingo (H.B. 1190 - Flaherty),
(49) Liabilities of Registers of Deeds under the Torrens Land Registration System (H.J.R. 1194 - Redwine),
(50) Public Transportation and Railroads (H.J.R. 1225 - Luebke),
(51) Effect of the Use of Commercial Nets on Fish and Shellfish Stocks and their Estuarine Habitats (H.J.R. 1282 - Richardson),
(52) Disaster Relief Volunteer Protection (H.B. 1283 - Redwine, S.B. 1192 - Doyle),
(53) Representation of Extraterritorially Zoned Areas (H.J.R. 1284 - Ellis),
(54) Consumer Protection Issues (H.J.R. 1303 - Spears; H.B. 1453 Easterling),
(55) Application of Chiropractic Care for the Cost-Effective Delivery of Health Care (H.J.R. 1309 - Stamey, S.J.R. 1156 - Odom),
(56) Issues Relating to Pilot Programs (H.J.R. 1319 - Ramsey),
(57) Cemetery Commission and the Regulation of Cemeteries in the State (H.B. 1320 - Hill),
(58) Advisability of Protecting Purchasers of Used Motor Vehicles and of Extending Warranties to the Sale or Lease of Used Motor Vehicles (H.J.R. 1324 - Beall),
(59) Temporary Employment in the State (H.B. 1351 - Holt),

(60) Tort Reform (H.J.R. 1378 - Gamble),
(61) East Carolina University School of Medicine's Potential Scope and Focus for the Next Decade (H.J.R. 1389 - Gamble),
(62) Alternate Election Systems (H.J.R. 1397 - Luebke),
(63) Health Care Insurance Coverage for Chemical Dependency (H.J.R. 1411 - Alexander),
(64) Medicaid (H.J.R. 1412 - Alexander),
(65) Exactions (H.B. 1413 - Richardson, S.B. 1181 - Conder),
(66) Historic Preservation Crafts Training in North Carolina (H.J.R. 1426 - Colton),
(67) Juvenile Code (H.J.R. 1429 - Hensley),
(68) Recovery Care Centers and Their Role in Developing a System of Affordable, Quality Health Care (H.J.R. 1434 - Richardson, S.J.R. 1172 - Parnell),
(69) Disposition of Public Historic Structures (H.J.R. 1447 - Colton),
(70) Equitable Distribution (H.J.R. 1452 - Easterling),
(71) Consumer Protection Issues (H.B. 1453 - Easterling),
(72) Long-Term Care Issues (H.J.R. 1456 - Gardner),
(73) Constitutional Review (S.B. 21 - Lee),
(74 Barrier to Meeting Human Services Needs Because of Confidentiality Requirements Set Out in State and Federal Laws and Regulations (S.J.R. 22 - Martin of Guilford),
(75) Comprehensive Transportation Funding (S.B. 165 and S.B. 166 - Martin of Guilford),
(76) UNC Board of Governors Appointment Process (S.J.R. 390 - Martin of Guilford),
(77) Legislative Compliance Review (S.B. 395 - Perdue),
(78) Physical Fitness Among Youth (S.B. 443 - Warren),
(79) Fletcher-Jeralds Omnibus Health Reform Act of 1993 (S.B. 554 - Daniel),
(80) Workers' Compensation (S.B. 587 - Simpson),
(81) Law Officer Conduct Review System (S.B. 683 - Richardson of Mecklenburg),
(82) Partnership for Quality Growth (S.B. 736 and S.B. 737 - Sherron),
(83) Certificates of Participation (S.B. 739 - Sherron),
(84) Development of Markets for Animal Residues (S.B. 956 - Albertson),
(85) Family Law Reform (S.J.R. 993 - Perdue),
(86) Legal Research (S.B. 1092 - Martin of Guilford),
(87) Medical Malpractice Compensation (S.J.R. 1159 - Ballance),
(88) Forfeitures and Fines Clear Proceeds Allocation (S.J.R. 1167 - Ballance),
(89) State Purchasing (S.B. 1178 - Sherron),
(90) Alternative Schools (S.B. 1200 - Gunter),

(91) Minority Males (S.B. 1236 - Martin of Guilford),
(92) Medicaid Eligibility Requirements (S.B. 1251 - Marshall),
(93) Economic Impact of Rules (S.B. 1261 - Sherron),
(94) African-American Cultural Center (S.B. 1262 - Jordan),
(95) Early Retirement Penalty Reduction for Members of the Teachers' and State Employees' Retirement System (S.B. 1264 - Harris),
(96) Fire Fighter Benefits (S.B. 1266 - Sherron),
(97) Alternative Revenue Sources for State Government (S.B. 1268 - Kaplan),
(98) Regional Government and Economic Development Zones (S.B. 1269 - Kaplan),
(99) North American Free Trade Agreement Impact on North Carolina (S.B. 1271 - Kaplan),
(100) Health Care Reform (S.B. 1293 - Daniel), and
(101) Wastewater Discharge Requirements at Public Schools (S.B. 1295 - Daniel).

Sec. 2.2. Committee Membership. For each Legislative Research Commission Committee created during the 1993-94 biennium, the cochairs of the Commission shall appoint the Committee membership.

Sec. 2.3. Reporting Dates. For each of the topics the Legislative Research Commission decides to study under this act or pursuant to G.S. 120-30.17(1), the Commission may report its findings, together with any recommended legislation, to the 1994 Regular Session of the 1993 General Assembly or the 1995 General Assembly, or both.

Sec. 2.4. Bills and Resolution References. The listing of the original bill or resolution in this Part is for reference purposes only and shall not be deemed to have incorporated by reference any of the substantive provisions contained in the original bill or resolution.

Sec. 2.5. Funding. From the funds available to the General Assembly, the Legislative Services Commission may allocate additional monies to fund the work of the Legislative Research Commission.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1993

H 1

HOUSE JOINT RESOLUTION 123

Sponsors: Representatives Jarrell, Gamble, Justus, Luebke, and Tallent.

Referred to: Rules, Calendar, and Operations of the House.

February 10, 1993

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

Whereas, the Legislative Research Commission has been authorized by the 1977, 1979, 1981, 1983, 1985, 1987, 1989, and 1991 General Assemblies to conduct a study of the revenue laws of North Carolina; and

Whereas, since 1977 the committee appointed by the Legislative Research Commission to study the revenue laws has recommended many changes in the revenue laws in the committee's attempt to improve these laws; and

Whereas, the Revenue Laws Study Committee has proved to be an excellent forum for both taxpayers and tax administrators to present their complaints about existing law and make suggestions to improve the law;

Now, therefore, be it resolved by the House of Representatives, the Senate concurring:

Section 1. The Legislative Research Commission is authorized to study the revenue laws of North Carolina and the administration of these laws. The Commission may review the State's revenue laws to determine which laws need clarification, technical amendment, repeal, or other change to make the laws concise, intelligible, easy to administer, and equitable. When the recommendations of the Commission, if enacted, would result in an increase or decrease in State tax revenues, the report of the Commission shall include an estimate of the amount of the increase or decrease.

Sec. 2. The Commission may call upon the Department of Revenue to cooperate with it in its study of the revenue laws. The Secretary of Revenue shall ensure that the Department's staff cooperates fully with the Commission.

Sec. 3. The Commission shall make a final report of its recommendations for improvement of the revenue laws to the 1995 General Assembly and may make an interim report to the 1994 Session of the 1993 General Assembly.

Sec. 4. This resolution is effective upon ratification.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1993

S 1

SENATE JOINT RESOLUTION 1167

Sponsors: Senator Ballance.

Referred to: Rules and Operation of the Senate.

May 17, 1993

A JOINT RESOLUTION AUTHORIZING THE LEGISLATIVE RESEARCH COMMISSION TO STUDY THE CURRENT SYSTEM FOR ALLOCATION OF THE CLEAR PROCEEDS OF FINES AND FORFEITURES.

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

Section 1. The Legislative Research Commission may study the current system for allocation of the clear proceeds of fines and forfeitures. In the course of its study, the Commission shall:

(1) Consider Article IX of Section 7 of the Constitution, which provides that the clear proceeds of all penalties and forfeitures and of all fines collected for any breach of the penal laws of the State shall go to the counties and be used exclusively for establishing and maintaining a uniform system of free public schools.

(2) Examine current statutory law and current practices and policies throughout the State to determine whether they are consistent with Article IX of Section 7 of the Constitution;

(3) Consider the impact of federal law, practices, and procedures on the ability of North Carolina to carry out the intent of Article IX, Section 7, of the Constitution.

The Commission may make an interim report to the 1993 General Assembly, 1994 Regular Session and a final report to the 1995 General Assembly.

Sec. 2. This resolution is effective upon ratification.

APPENDIX B

REVENUE LAWS STUDY COMMITTEE

1993 - 1994

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Sen. Betsy Cochrane
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APPENDIX C

1994 Tax Law Changes

Prepared by Cynthia Avrette, Sabra J. Faires, and Martha H. Harris

Chapter 10, 1994 Extra Session (Senate Bill 151, Sen. Daniel)
AN ACT TO REDUCE THE UNEMPLOYMENT INSURANCE TAX RATE.

During the 1994 Extra Session on crime, the General Assembly enacted this act, which reduces unemployment insurance taxes for employers. A related act, enacted during the subsequent 1994 Regular Session, increases unemployment benefits for workers. Because the unemployment insurance tax rate had been increased and benefits had been reduced in 1983, the reduction of the tax rate during the 1994 Extra Session was viewed as only the first part of a two-part package to restore both employees and employers to their pre-1983 status regarding both the tax and benefits. Together, the two acts provide relief to both workers and employers.

Tax Rate Reduction for Employers

This act reduces the standard beginning contribution rate for unemployment insurance tax from 2.25% to 1.8% of the employer's wages paid during a calendar year for employment occurring after December 31, 1993. Effective January 1, 1994, it also reduces the tax rates that apply to rated employers with a credit balance in their unemployment insurance tax account in two ways, by reducing the rates in the rate schedule applicable to these employers and by providing an additional reduction in years in which there is a specified minimum balance in the Unemployment Insurance Fund. In 1993, the General Assembly enacted legislation that reduced the unemployment tax contribution rate by 30% for rated employers with a credit balance in their unemployment insurance tax account for any calendar year in which the balance in the Unemployment Insurance Fund equals or exceeds $800,000,000 as of the preceding August 1. This act increases that reduction, providing these employers with a 50% reduction in their contribution rate for the 1994 calendar year and for any calendar year in which the balance in the Unemployment Insurance Fund equals or exceeds $800,000,000 as of the preceding August 1.

The act's changes in the rate schedule along with the conditional change of the rate reduction from 30% to 50% will combine to give rated employers with positive credit balances an average tax reduction of 38% (the actual reduction for an individual employer depends on the employer's experience rating). A rated employer is an employer who has had a chargeable account for more than 13 consecutive months immediately preceding the date for calculating the employer's tax rate. The act's change in the standard beginning tax rate will provide a 20% tax reduction for employers who are not yet rated. The Employment Security Commission projected that the act will reduce employer tax payments by more than $67 million in 1994 and more than $73 million in 1995. Most North Carolina employers will benefit from the act; only those rated employers who have taken out more in unemployment benefits than they have put in will not experience a rate reduction. The Employment Security Commission estimates that the remaining 95% of employers will save an average of $22.00 in taxes per worker employed.

Unemployment tax contributions are paid by employers on a quarterly basis and deposited into the State Unemployment Insurance Fund. After deducting any refunds payable from the Fund pursuant to G.S. 96-10(f), the money is deposited with the secretary of the treasury of the United States to the credit of this State's account in the Unemployment Trust Fund. Funds in the State's account earn interest that is also

credited to the account. As money in the State's account is needed to pay benefits, it is transferred to the State and credited to the benefits account of the State's Unemployment Insurance Fund to be used to pay benefits to people who lose their job through no fault of their own.

North Carolina's account in the federal trust fund is one of the most solvent accounts of any state in the country. In 1994, the State's account in the trust fund had a balance of $1.49 billion, the fifth largest account in the nation, despite the 1993 legislation providing a 30% cut in the rate for rated employers with a credit balance. North Carolina's account has continued to grow since the 1993 tax cut because it earns interest at a high rate, because new unemployment taxes were collected on the many new jobs created in North Carolina during the past year, and because claims for unemployment benefits to be paid from the account have been consistently low. Even after the 1994 tax cut, the account is expected to grow or remain static each year.

This act is the third unemployment tax reduction in three years. As noted above, in 1993 the General Assembly reduced the tax rate for rated employers by 30%. In 1992, the General Assembly was able to suspend an additional unemployment tax collected from employers and credited to the Employment Security Commission Reserve Fund. This Reserve Fund bolsters the State Unemployment Insurance Fund. Before enactment of the 1994 legislation, North Carolina's average unemployment tax rate, 0.5%, was already the 45th lowest in the nation. The 1.8% starting rate for new employers is now the second lowest rate in the nation. The three unemployment tax reductions enacted by the General Assembly in three years have provided substantial tax relief to North Carolina employers.

Benefit Increase for Workers

During the 1994 Regular Session, the General Assembly enacted a related bill to increase unemployment benefits. House Bill 1889, AN ACT TO RESTORE UNEMPLOYMENT BENEFITS TO THEIR PRE-1983 LEVEL, TO MAKE PARTICIPATION IN REEMPLOYMENT SERVICES A CONDITION OF RECEIVING CERTAIN BENEFITS, AND TO MAKE TECHNICAL CHANGES IN THE EMPLOYMENT SECURITY LAWS, was enacted as Chapter 680 of the 1993 Session Laws (1994 Regular Session). Chapter 680 restores the pre-1983 formulas for computing unemployment benefits, implements a federal requirement concerning worker profiling and participation in reemployment services, and deletes obsolete provisions from the unemployment law. The benefit changes became effective for benefits paid to claimants whose benefit year begins on or after August 1, 1994. The other changes became effective upon ratification.

The effect of the benefit changes is to increase unemployment benefits. The specific formula changes are:

(1) Use of an individual's high quarter wages in determining the weekly benefit for an individual who is totally or partially unemployed. Prior law used an average of the two highest quarter wages. The law had changed from high quarter wages to an average of the two highest quarter wages effective October 1, 1983. Chapter 680 therefore reinstates the pre-1983 law on this issue. Section 1 makes the change for total unemployment and Section 2 makes the change for partial unemployment.

(2) Use of a multiplier of 8 2/3 in determining an individual's total benefit amount. Prior law used a multiplier of 8. The law had changed from 8 2/3 to 8 effective October 1, 1983. Chapter 680 therefore reinstates the pre-1983 law on this issue. Section 3 makes this change.

The Employment Security Commission has estimated that these benefit changes will increase benefit costs payable from North Carolina's account in the federal Unemployment Trust Fund by approximately $30 million a year. These increased costs

are expected to be offset by employer tax payments and interest earnings credited to the account.

Chapter 680 also implements the mandates of the federal Unemployment Compensation Amendments of 1993, Pub. L. 103-152. That law requires states to establish a worker profiling system that identifies claimants for unemployment benefits who need reemployment services to become employed and to impose participation in the needed reemployment services as a condition of receiving unemployment benefits. Sections 4 through 6 make these changes. Examples of reemployment services are assessments of skills, job search workshops, and providing information on jobs. Finally, Chapter 680 deletes obsolete provisions and language from the unemployment laws.

Chapter 582 (House Bill 80, Rep. Gamble)

AN ACT TO REDUCE THE TIME ALLOWED THE DEPARTMENT OF REVENUE TO MAKE ASSESSMENTS OF TAXES FOLLOWING A FEDERAL DETERMINATION, TO REINSTATE AN INADVERTENTLY DELETED PROVISION RELATING TO ASSESSMENTS FOR EMPLOYER WITHHOLDING BASED ON FEDERAL DETERMINATIONS, AND TO CLARIFY THE ASSESSMENT STATUTES.

This act makes three substantive changes and several technical changes to the statutes concerning the assessment of certain State taxes by the North Carolina Department of Revenue after the federal Internal Revenue Service (IRS) has corrected or otherwise determined a taxpayer's liability for a federal tax that affects the amount of State tax owed. The changes become effective January 1, 1995, and apply to assessments of taxes for which the time period for making assessments has not yet expired. The act is expected to have no significant effect on State revenues.

The substantive changes affect the statute of limitations that applies to assessments of State income, gift, or withholding taxes following a federal determination. The changes reduce the period of time the Department of Revenue has to assess an underpayment of State income or gift taxes following a federal determination of federal income or gift taxes, give the Department of Revenue a longer time to make an assessment of State withholding taxes following a federal determination of withheld federal employment taxes, and give taxpayers a longer time to file an amended State gift tax return following a federal determination of federal gift tax liability.

The technical changes consolidate into G.S. 105-241.1(e) the various limitation periods on making assessments following a federal determination and make technical changes in the wording of G.S. 105-241.1(b), (i), and (j). The various limitation periods are moved to G.S. 105-241.1 from G.S. 105-230.20 (corporate income tax), G.S. 105-259 (individual income tax), G.S. 105-160.8 (estate and trust income tax), and G.S. 105-197.1 (gift tax) to avoid duplication in the statutes and to establish a uniform period for these taxes.

A federal determination is a report by the Internal Revenue Service (IRS) that a taxpayer has not filed a return or has filed an incorrect return and, consequently, either owes more taxes or is entitled to a refund. If a taxpayer did not file a return or understated the amount due on a return, the determination states the amount of tax the IRS finds is due and serves as the federal notice of assessment. The IRS eventually sends the appropriate state a copy of a federal determination. A delay between when a taxpayer receives a federal determination and when a state receives a copy of the determination occurs when the taxpayer is in the process of resolving with the IRS questions raised by the determination.

Under the State income tax laws, a taxpayer who receives a federal determination of federal income tax must, within two years, file an amended State income tax return

with the Department of Revenue reflecting the determination. Under the State gift tax laws, a taxpayer who receives a federal determination of federal gift tax must, within 30 days, file an amended gift tax return reflecting the determination. This act extends from 30 days to two years the period of time in which a taxpayer must file an amended gift tax return following a federal determination. In making this change, the act establishes a uniform period for both income and gift taxes.

Until January 1, 1995, if a taxpayer files an amended State income or gift tax return in response to a federal determination, the Department of Revenue has three years from the time it receives the return to make an assessment of State income or gift tax. If a taxpayer does not file an amended return in response to a federal determination, the Department of Revenue has five years from the date it receives a copy of the determination from the IRS to make an assessment of State income or gift tax. This act shortens the additional three-year period to one year and shortens the additional five-year period to three years. Thus, under the act, the Department of Revenue has an additional one-year period to make an assessment of State income or gift tax when a taxpayer files an amended return within two years of receiving a federal determination, and the Department has an additional three-year period to make an assessment after receiving notice from the IRS of a federal determination when a taxpayer does not file the required amended return.

The general limitations period for an assessment of any State tax is three years after a return was filed or due to be filed. The one-year and three-year periods following a federal determination are in addition to the regular three-year period, which is set in G.S. 105-241.1. An additional time period is necessary when a federal determination is made to allow the State adequate time to respond to the federal determination. The State may not receive an amended return following a federal determination or a notice of a federal determination from the IRS until near the end of or after the end of the general three-year period.

Unlike the income tax laws, the withholding tax laws do not give the State any additional time to make an assessment following a federal determination. Therefore, for an assessment of withholding taxes, the State must make an assessment within the general three-year time period for making assessments. When the State does not receive notice of a federal determination of employment taxes until near the end of or after the end of this three-year period, the State is foreclosed from making an assessment.

This act gives the State the same additional one-year or three-year period to make an assessment of withholding taxes following a federal determination of federal employment taxes that it gives for assessments of income or gift taxes following a federal determination. In making this change, the act restores part of the 1990 law on assessments for withholding taxes. Until 1990, the withholding tax laws gave the same additional time periods for making an assessment after a federal determination that the income tax and gift tax laws provide. In 1990, the withholding tax statutes were extensively rewritten to speed up payments of withheld taxes. As part of the changes, G.S. 105-163.17 was rewritten and the cross-reference to the additional time periods was inadvertently deleted. The act reinstates additional time periods following a federal determination but shortens the allowed additional time periods to either one year or three years as described for income and gift taxes.

Sections 1, 2, 3, and 6 of the act rewrite the individual income tax statute, the corporate income tax statute, the estate and trust income tax statute, and the gift tax statute, respectively, concerning federal determinations to delete the portions that are consolidated into rewritten G.S. 105-241.1(e) in Section 5 of the bill. Section 4 of the bill adds a statute that gives additional time periods for making an assessment of withholding taxes following a federal determination. Section 5 rewrites part of the

assessment statute, G.S. 105-241.1, to consolidate the various time periods that apply to assessments and to make the statute easier to understand.

The act does not affect assessments of State inheritance tax following a federal determination of federal estate tax, nor does it affect when interest begins to accrue on an overpayment of State income, gift, or withholding tax. The act deletes language from several statutes that directs the Department of Revenue to refund overpayments of tax within 30 days because the language is unnecessary and confusing. The 30-day limit does not determine when interest begins to accrue on overpayments and has no practical effect. G.S. 105-266(a) requires the Department of Revenue to refund overpayments of any tax as soon as possible, and G.S. 105-266(b) states when interest begins to accrue on overpayments.

The act stems from a recommendation of the Revenue Laws Study Committee. The recommendation of the study committee covered only the additional periods for an assessment of State withholding taxes after a federal determination and the technical changes.

Chapter 584 (Senate Bill 1045, Sen. Allran)

AN ACT TO BROADEN EXISTING INCOME TAX CREDITS FOR THE PRODUCTION AND INSTALLATION OF SOLAR AND PHOTOVOLTAIC EQUIPMENT BY INCREASING THE AMOUNTS OF THE CREDITS AND EXTENDING THE SOLAR EQUIPMENT CREDITS TO INCLUDE EQUIPMENT THAT GENERATES ELECTRICITY.

This act broadens two existing corporate and individual income tax credits concerning the installation of solar energy equipment and one existing corporate income tax credit concerning the production of photovoltaic equipment. Photovoltaic equipment is equipment that uses solar energy to produce electricity. The act is effective for taxable years beginning on or after January 1, 1994, and is expected to result in an annual decrease in General Fund revenues of between $127,500 and $178,500. The changes made by the act to each credit are described below.

Credits for Installing Residential Solar Energy Equipment

- Increases the costs for which a credit can be claimed from 25% to 40%.
- Increases the maximum credit per system from $1,000 to $1,500.
- Expands the credit to include photovoltaic equipment.
- Increases from 3 years to 5 years the number of years a credit can be carried forward.

Corporate Credit For Constructing Photovoltaic Equipment Facility

- Increases the costs for which a credit can be claimed from 20% to 25%.

Credits for Solar Equipment Used To Produce Heat in Certain Processes

- Increases the costs for which a credit can be claimed from 20% to 35%.
- Increases the maximum credit for an installation from $8,000 to $25,000.
- Expands the credit to include the production of electricity.

The corporate income tax credit for installing residential solar equipment is available to corporations that construct or install solar energy equipment in residential buildings used or sold by the corporation for commercial or business purposes. The credit is available to the corporation that owns or controls the use of the building when the equipment is installed or, in the case of a building constructed to be sold, to the owner who first occupies or leases the building for use. The credit taken may not exceed the amount of income taxes imposed on the person taking the credit and a credit is not

allowed to the extent any of the cost of the equipment was provided by federal, State, or local grants. A similar individual income tax credit is allowed.

The photovoltaic corporate income tax credit is allowed to a corporation that constructs a facility in North Carolina for the production of photovoltaic equipment. The credit may not exceed the amount of income tax imposed on the corporation and it is not allowed to the extent that any of the costs were provided by governmental grants. Any excess credit may be carried forward for five years. There is no parallel individual income tax credit.

The credit for installing solar equipment to produce heat is allowed to a corporation or an individual for constructing or installing solar equipment to produce heat in the manufacturing or service processes of a business located in North Carolina. The credit may not exceed the amount of tax imposed on the corporation or individual and the credit is not allowed to the extent that any of the costs were provided by governmental grants.

Chapter 600 (House Bill 1663, Rep. Black)

AN ACT TO EXEMPT ALL ANNUITIES AND FUNDING AGREEMENTS FROM PREMIUM TAXATION; TO CLARIFY THE AUTHORIZATION FOR THE ISSUANCE OF AND ESTABLISH STANDARDS FOR FUNDING AGREEMENTS; AND TO MAKE CONFORMING CHANGES IN LAWS ON PRIORITY OF DISTRIBUTION OF ASSETS OF INSOLVENT INSURERS AND ON SECURITIES.

This act changes the insurance laws by authorizing certain insurers to issue funding agreements in this State, subject to regulation by the Department of Insurance, and by changing the priority of certain claims against the assets of an insolvent insurance company. The act changes the tax laws by exempting all annuities and the new funding agreements from the gross premiums tax levied on insurance companies and by making technical changes to the statute that imposes the gross premiums tax to make the statute easier to understand. These tax changes become effective January 1, 1995; the rest of the act became effective July 1, 1994.

A funding agreement is, in effect, a kind of annuity. It is an agreement between an insurer and another person for the person to provide funds to the insurer and for the insurer to pay the funds, in one or more payments, to a designated person at a future date based on contingencies other than death or disease. For example, a party responsible for cleanup of a hazardous waste site could use a funding agreement for the cleanup. The party could deposit funds with an insurer pursuant to a funding agreement that would establish a periodic payment schedule and the time period for the cleanup.

The act changes the priority in insurer insolvency proceedings of the portion of a benefit claim that exceeds $300,000. Under prior law, the portion above this amount had no priority and was in the same status as claims of general creditors. The act gives the portion of a benefit claim that exceeds $300,000 the same priority as the portion that does not exceed this amount and clarifies that claims under funding agreements are to be given the same priority as other claims for benefits.

As part of the goal of the act to remove obstacles to the issuance of funding agreements in this State, the act repeals the gross premiums tax on annuities. Prior law imposed a gross premiums tax of 1.9% on annuities. The tax was payable at the "back end" rather than the "front end," which means that the tax was paid when the annuity payments began rather than when money was deposited with the insurance company to fund the annuity. When payments on an annuity began, the tax was calculated as 1.9% of the present value of the stream of income to be received under the annuity. The insurer deducted the amount of the tax from the initial payments to be made under the

annuity. North Carolina was one of about 13 states that imposed a premiums tax on annuities. Of these, about five either required or allowed the tax to be computed and paid at the "back end" rather than the "front end."

The exemption of annuities from the gross premiums tax has two fiscal effects. First, it decreases premiums tax revenue each fiscal year by approximately $1 million. Second, because it reduces the amount of premiums tax payable, it reduces by approximately $72,500 the amount collected each fiscal year from the insurance regulatory charge. That charge, which is imposed by G.S. 58-6-25, is set annually and, for the 1994 taxable year, is 7.25% of gross premiums tax liability.

The technical changes to the gross premiums tax statute, G.S. 105-228.5, break the statute into subsections, delete incorrect cross-references, clarify that the gross premiums tax is in lieu of only income and franchise taxes, and delete obsolete provisions. The act makes no substantive change to G.S. 105-228.5 other than to repeal the tax on annuities.

Chapter 661 (Senate Bill 1377, Sen. Winner of Buncombe)

AN ACT TO CONFORM THE THRESHOLD FOR DETERMINING IF A PENALTY APPLIES TO AN UNDERPAYMENT OF WITHHELD STATE INCOME TAXES TO THAT USED UNDER THE INTERNAL REVENUE CODE FOR DETERMINING IF A PENALTY APPLIES TO AN UNDERPAYMENT OF WITHHELD FEDERAL INCOME TAXES, AND TO CLARIFY THE TYPE OF INFORMATION A TAXPAYER MUST PROVIDE TO THE SECRETARY OF REVENUE.

This act makes one substantive change to the State law concerning payment to the Department of Revenue of withheld State income taxes plus two technical changes to this law and a clarifying change concerning the kinds of information the Secretary of Revenue can ask a person who is required to file any tax return or report to provide. Section 1 of the act makes the State withholding tax changes and Section 2 makes the clarifying change concerning tax information. The State withholding tax changes become effective January 1, 1995, and apply to payments of withheld State income taxes made on or after that date. The clarifying change concerning tax information became effective upon ratification. This act was recommended by the Revenue Laws Study Committee. The withholding tax change is expected to cause a minimal increase in General Fund revenues because it accelerates slightly the payment schedule for underpayments of withholding tax and lowers slightly the threshold for imposing penalties for underpayments of withholding tax.

The substantive change to the State withholding tax laws ties the State penalty provisions concerning payments by employers of withheld State individual income taxes to the federal penalty provisions that apply to payments to the Internal Revenue Service of federal employment taxes attributable to the same wages. The immediate effect of this change is twofold. First, it changes the amount of a shortfall in the remittance of withheld State income taxes that triggers the imposition of interest and penalties from the current State amount to the current federal amount. Second, it changes the time by which a shortfall must be remitted in order to avoid the imposition of penalties and interest. The continuing effect of the change is to adjust the State provisions for determining when an employer is subject to interest and penalties on a shortfall in withheld State income taxes automatically in accordance with changes in the corresponding federal provisions.

Under prior State law, an employer who did not remit the full amount of State income taxes withheld from wages by the date they were due was not liable for interest or penalties on the shortfall if the amount of the shortfall was less than 5% of the amount due and the employer included the amount of the shortfall in the next

withholding tax return the employer filed. A return is due quarterly by the last day of the month following the end of the quarter.

Under current federal law, an employer who does not remit the full amount of federal employment taxes attributable to wages by the date they are due is not liable for interest or penalties on the shortfall if the amount of the shortfall does not exceed the greater of 2% of the amount due or $100 and the employer remits the shortfall by the shortfall make-up date. The shortfall make-up date for an employer who remits monthly is the due date of the quarterly return. The shortfall make-up date for an employer who remits on a semi-weekly basis is the first Wednesday or Friday that falls on or after the 15th day of the month following the month in which the remittance was required to be made. Federal employment taxes attributable to wages are withheld federal income taxes, withheld employee old age, survivor, and disability insurance taxes and hospital taxes, the employer's corresponding old age, survivor, and disability insurance taxes and hospital taxes, and certain amounts withheld under the backup withholding requirements.

Thus, the immediate effects of the act are to delete the 5% shortfall threshold and substitute a threshold that is the greater of 2% or $100, and to require employers who remit on a semi-weekly basis to remit a shortfall by approximately the 15th day of the month following the month in which it occurred instead of at the time the employer files the next quarterly return. The result is that the shortfall threshold for determining whether a penalty applies and the due date of a shortfall will be the same for federal and State law; to avoid interest or a penalty on a shortfall of withheld State income taxes, an employer must remit more of the total amount payable by the due date and remit any shortfall within a shorter amount of time than was required under prior State law.

In addition to the substantive change, the act makes two technical changes to the State withholding tax laws. First, it changes the phrase "federal income taxes withheld from the same wages" to "federal employment taxes attributable to the same wages" because this latter phrase is more accurate. As noted above, federal income tax withheld from wages is only one of the kinds of taxes that are included under federal law in applying the test for determining when interest and penalties apply.

Second, it changes the phrase "within three banking days" to "semi-weekly" for the same reason; the former phrase is no longer accurate. Effective January 1, 1993, the Internal Revenue Service changed the designation of employers who are required to remit more frequently than on a monthly basis from a "within three-banking-day" employer to a "semi-weekly" employer to reflect changes in the payment schedule for employers. The Internal Revenue Service abandoned the eighth-monthly periods in favor of semi-weekly periods. Under the former law, an employer who accumulated $3,000 or more in employment taxes in any eighth-monthly period had to remit the taxes within three banking days after the end of that eighth-monthly period. Under the revised regulations, employers who paid at least $50,000 of employment taxes in the previous 12-month period ending June 30 must remit whatever amount of employment taxes they accumulate in a semi-weekly period. One semi-weekly period consists of Wednesday, Thursday, and Friday; employment taxes attributable to wages paid in this period are due on or before the following Wednesday. The other semi-weekly period consists of Saturday, Sunday, Monday, and Tuesday; employment taxes attributable to wages paid in this period are due on or before the following Friday.

The State withholding tax changes made by this act keep the penalty provisions concerning payments of withheld State income taxes consistent with the intent of the 1990 act of the General Assembly that revised the laws concerning payment of these taxes. Chapter 945 of the 1989 Session Laws (1990 Regular Session) revised the withholding tax provisions to require payment of the taxes on a faster basis. It did so by putting payment of the taxes by larger employers on the same schedule that applied

under federal law. As part of the changes, that act set the penalty provisions to mirror the federal ones. The federal law changed in 1993, however, and a corresponding change was not made to State law.

Section 2 of the act makes a clarifying change concerning information provided by taxpayers. It updates the law that requires various entities to complete tax returns and answer questions submitted to them by the Secretary by incorporating the definitions of "person," "Secretary," and "taxpayer" that now apply to this law and by referring specifically to reports as well as returns. It also clarifies the type of information the Secretary can require a taxpayer to provide by enumerating the permissible kinds of information.

The changes concerning tax information were included in the act because, in reviewing the State withholding tax changes, the Revenue Laws Study Committee became concerned about the scope of information the Secretary could request. The State withholding tax law required a person who must file a withholding tax return to provide any information requested by the Secretary. The Committee wanted to ensure that all information requested is related to a determination of tax liability. The requirement that a person provide any information requested by the Secretary appears throughout Chapter 105 of the General Statutes. To provide a uniform policy on tax information, the Committee therefore decided to amend the appropriate statute in Article 9 of Chapter 105 rather than make a change that applies only to information about withholding taxes. Article 9 of Chapter 105 contains the administrative provisions that apply to all taxes administered by the Secretary under that Chapter.

Chapter 662 (Senate Bill 1619, Sen. Winner of Buncombe)

AN ACT TO UPDATE THE REFERENCE TO THE INTERNAL REVENUE CODE USED IN DETERMINING CERTAIN TAXABLE INCOME AND TAX EXEMPTIONS AND TO RESOLVE AN UNINTENDED CONFLICT BETWEEN THE STATUTE OF LIMITATIONS FOR CERTAIN TAX REFUNDS AND THE LAW ALLOWING DEDUCTIONS FOR CARRYBACKS, BAD DEBTS, AND WORTHLESS SECURITIES.

This act rewrites the definition of the Internal Revenue Code used in State tax statutes to change the reference date from January 1, 1993, to January 1, 1994, and revises the tax refund statute of limitations to eliminate an unintended conflict between that statute and the law allowing deductions for carrybacks, worthless debts, and worthless securities.

The act updates the Internal Revenue Code reference, thus making recent amendments to the Code applicable to the State to the extent that State tax law previously tracked federal law. This update has the greatest effect on State corporate and individual income taxes because these taxes are based on federal taxable income and are therefore closely tied to federal law. The franchise tax, gift tax, highway use tax, inheritance tax, insurance company premiums tax, and intangibles tax also determine some exemptions based on the provisions of the Code. The federal Omnibus Budget Reconciliation Act of 1993 enacted a number of different changes that affect individual and corporate income tax. The following are among the most important of the federal changes that affect the State:

1. Changes in the moving expense deduction.
2. Valuation of securities dealers' inventory at fair market value; securities not in inventory are considered to have been sold at fair market value.
3. Reduction of the amount of qualifying business meals and entertainment expenses that may be deducted, from 80% to 50%.
4. Repeal of the deduction for certain club dues.

5. Expansion of the rules for amortization of certain intangible business assets, including goodwill.
6. Elimination of passive loss restrictions for certain real estate professionals.
7. Retroactive extension of the health insurance deduction for self-employed individuals.
8. Increase in the recovery period for depreciation of non-residential property, from 31.5 years to 39 years.
9. Deduction for wages of the CEO and four highest paid officers of a public corporation limited to $1 million each.
10. Repeal of the deduction for lobbying expenses.

The act also eliminates an inconsistency in the tax law. Since 1989, the State individual income tax law has conformed to the federal law that allows a taxpayer to carry net operating losses and certain capital losses back to the three previous tax years and then forward for fifteen years. Under the new law, the first tax year to which a loss could be carried back is 1989, which means that carrybacks were allowed beginning with losses incurred in 1992. To deduct the loss carryback for the 1989 tax year, the taxpayer must file an amended return for that year. The taxpayer would first learn of the loss in preparing the tax return for the 1992 tax year, which was due April 15, 1993, for calendar year taxpayers. Under federal law, the taxpayer has three years from the due date of the 1992 return to claim the loss carryback on an amended return for 1989. Under prior North Carolina law, however, the normal statute of limitations applied: the loss had to be claimed within three years after the due date of the 1989 return. Thus, in most cases, the taxpayer would have had to file the amended return within days or weeks of learning the deduction was available.

This discrepancy in the law occurred because, at the time the law was changed to allow loss carryback deductions, no conforming change was made to the statute of limitations to allow time to file for the deductions. The act makes this conforming change so that the usual three-year period for claiming refunds will run, in the case of loss carryback deductions, from the due date of the return for the year the loss occurs rather than the year to which the deduction is carried back.

Another change made by the act conforms the State individual income tax law to the federal law that allows a seven-year period for claiming a refund due to a deduction for a worthless debt or a worthless security. This longer period is considered equitable because of the complexity under federal law of determining when a debt or security became worthless and, consequently, which year is the appropriate year for taking the deduction. A security becomes worthless for federal tax purposes not when it loses value but when the taxpayer has no reasonable expectation that it will become valuable at some future time. A debt becomes worthless for federal tax purposes when there are identifiable events that have caused the taxpayer to reasonably abandon hope of ever recovering any payment. In many cases, a taxpayer may take the deduction for the wrong year and learn much later that the deduction should have been taken for a different year. Without the longer statute of limitations, the taxpayer could not then file an amended return to take the deduction and claim a refund for the appropriate year.

The conforming changes made by the act to the statute of limitations are retroactive to the 1989 tax year, the year in which the changes were first needed. Interest on refunds due to loss carrybacks will run, however, only from 45 days after the filing date of the return for the year in which the loss occurred rather than from the year to which the loss is carried back. For example, if the taxpayer is a calendar year taxpayer, interest on a refund for a loss that occurred in 1992 and is carried back to 1989 will run only from May 30, 1993, which is 45 days after the April 15 due date of the 1992 return.

The Department of Revenue estimates that the revenue gain from conforming the Internal Revenue Code reference to the latest federal changes will be approximately $5 million in the 1994-95 fiscal year. The estimated loss from the net operating loss carryback change is a one-time loss of $3.4 million in the 1994-95 fiscal year. Therefore, the net impact of this act is a gain to the General Fund of $1.6 million for the 1994-95 fiscal year and a gain of at least $5 million for each fiscal year thereafter.

Chapter 674 (Senate Bill 716, Sen. Kerr)

AN ACT TO MODIFY THE CORPORATE INCOME TAX CREDIT FOR CONSTRUCTION OF A COGENERATING POWER PLANT BY (1) PROVIDING THAT A PARTNERSHIP MAY QUALIFY FOR THE CREDIT, (2) CLARIFYING THAT A PARTNERSHIP MAY PASS AN INCOME TAX CREDIT THROUGH TO ITS PARTNERS, (3) EXPANDING THE CREDIT TO INCLUDE NATURAL GAS COGENERATING POWER PLANTS, (4) PROVIDING AN ALTERNATIVE METHOD TO CALCULATE THE CREDIT, (5) LIMITING THE AMOUNT OF CREDIT THAT MAY BE ALLOWED EACH YEAR EFFECTIVE BEGINNING IN 1994, AND (6) RESTRICTING THE CREDIT TO NATURAL GAS COGENERATING POWER PLANTS EFFECTIVE BEGINNING IN 1998.

This act modifies the corporate income tax credit for construction of a cogenerating power plant and codifies the principles that apply to all income tax credits of partnerships. The modifications to the cogenerating power plant tax credit that broaden the credit are effective for taxable years beginning on or after January 1, 1993, and the modifications that limit the credit become effective for taxable years beginning on or after either January 1, 1994 or January 1, 1998, as explained below. The codification of the principles that apply to all income tax credits of partnerships is effective for taxable years beginning on or after January 1, 1993. The changes to the cogenerating power plant tax credit are expected to decrease General Fund tax revenue annually by an amount that ranges from $275,000 in fiscal year 1994-95 to $800,000 in fiscal year 1997-98; codification of the principles that apply to income tax credits of partnerships has no fiscal impact.

The cogenerating power plant tax credit, set out in G.S. 105-130.25, is a corporate income tax credit that has no parallel individual income tax credit. Until this act, the credit applied to 10% of the costs of purchasing and installing in a power plant equipment that sequentially produced electrical or mechanical power and useful thermal energy from a shared power source that used a fuel other than residual oil, middle distillate oil, gasoline, natural gas, or liquid propane gas. The credit was allowed only for costs paid during the taxable year, could not exceed the amount of tax owed for the taxable year, and could not be carried forward or backward if the allowable credit exceeded the amount of tax owed.

The act both broadens and limits this tax credit and sets out the current administrative practice concerning the availability of the credit to a corporate partner in a partnership. Section 1 of the act broadens the credit in two ways. First, it extends the credit to cogenerating equipment fueled by natural gas. Second, it gives a corporation the option of cumulating costs paid for cogenerating equipment in years before a plant becomes operational and claiming a credit for the cumulated costs in the year the plant becomes operational. Prior to this act, natural gas was not an allowable fuel source and the cost of cogenerating equipment could be claimed as a credit only in the year the cost was paid.

If a corporation chooses the optional method of calculating costs and claims a credit for cumulated costs in the year the plant becomes operational, the credit cannot exceed one-fourth of the amount of corporate income tax the corporation owes for the taxable

year reduced by any other credits allowed the corporation. Other credits allowed the corporation for the taxable year include carry-forwards of the cogenerating credit. If the credit claimed exceeds this one-fourth limitation, the excess can be carried forward for the next 10 taxable years. To carry forward an amount that exceeds the one-fourth limitation, however, a corporation must submit an application for the credit for each year the corporation seeks to claim the carry-forward.

Sections 2 and 4 of the act limit the credit in three ways. Section 2 sets an annual ceiling on the credit and creates a one-year delay in taking the credit. Section 4 eventually allows a credit only for cogenerating equipment fueled by natural gas.

Beginning in taxable year 1994, the act sets a ceiling of $5 million on the amount of cogenerating power plant credits that can be taken in a taxable year by all corporations combined. The amount of any cogenerating credits to be carried forward from a previous year is included in determining whether the total amount claimed for a year exceeds the ceiling. Current law does not set a ceiling on the total amount of credits that can be claimed. The amounts claimed for the taxable years for which the credit has been in effect have ranged from zero to $2.9 million, and the total amount claimed for all taxable years for which the credit has been in effect is approximately $6.1 million. The ceiling was enacted to prevent a large loss in any one year due to the new option of cumulating costs.

Under the revised credit, if the amount claimed by all corporations exceeds the $5 million ceiling, the credit claimed by each corporation is reduced proportionally until the total reduced amount does not exceed the ceiling. A corporation whose credit is reduced to meet the ceiling may carry the amount of the reduction forward for the next 10 taxable years. To carry the amount forward, however, the corporation must submit an application for the credit for each year the corporation seeks to claim the carry-forward. An annual application is necessary to enable the Department of Revenue to determine for each year whether the amounts claimed exceed the $5 million ceiling.

The act further limits the credit by delaying by one year the tax period for which the credit can be taken. Until taxable year 1994, a corporation that claims a credit for a taxable year takes the credit for the year the credit is claimed. Thus, a corporation that claims a credit for the 1993 taxable year can subtract the amount of the credit from the amount of tax due for the 1993 taxable year. Starting with the 1994 taxable year, a corporation must apply for the credit in one year and then take the credit in the following year. This delay is a result of the $5 million ceiling. The delay allows the State to determine in advance of a taxable year whether the credits claimed for that year will exceed the ceiling and to notify corporations of any reduction in the credits claimed in the event the amount claimed by all corporations exceeds the ceiling.

The final limitation the act imposes on the credit is to require the cogenerating equipment to be fueled by natural gas beginning in taxable year 1998. Thus, the act first allows natural gas as a fuel source beginning in taxable year 1993 and then excludes all fuel sources other than natural gas beginning in taxable year 1998.

The act also changes the language of the credit to include a partnership as well as a corporation. This is a clarifying change rather than a substantive change, however, because corporate partners of a partnership could already take the credit under the prior law because they were corporations. Corporate partners of partnerships were allowed to take corporate income tax credits in proportion to the corporate partner's distributive share of the partnership income.

Because the application of the cogenerating credit to a corporate partner was not clear, the act codifies the principles that apply to the eligibility of a partnership for any corporate or individual income tax credit. Section 3 of the act sets out these principles. Under these principles, a partner in a partnership is eligible for a credit if the partnership qualifies for the credit and the partner could take the credit if the partner

stood in the position of the partnership. Thus, an individual partner in a partnership could not take the cogenerating credit because the credit is not available to individuals.

Partnerships qualify for corporate income tax credits on behalf of their corporate partners. Whether a partnership qualifies for an individual income tax credit depends on the wording of the credit. For example, a partnership qualifies for an individual income tax credit that is allowed to a person, but not one that is allowed to an individual or a taxpayer.

The amount of a credit that can be taken by a partner is determined by the partner's distributive share of the partnership in accordance with sections 702 and 704 of the Internal Revenue Code. Under those sections, a partner's distributive share is determined by the partnership agreement. If the partnership agreement does not provide for the distributive shares, however, a partner's share is determined in accordance with the partner's interest in the partnership.

Any limit on the amount of a credit that can be taken or any other restrictions on a credit apply separately to each partner of a partnership that is eligible for a credit. Thus, if a credit cannot exceed 25% of a person's tax liability, the limit is calculated separately for each partner. This principle results from the nature of a partnership as a pass-through entity. In a partnership, the partners and not the partnership itself is liable for any income tax due on income earned by the partnership.

Chapter 679 (Senate Bill 906, Sen. Daniel)

AN ACT TO MAKE VARIOUS SUBSTANTIVE AMENDMENTS TO THE WORKERS' COMPENSATION ACT AND TO MAKE RELATED CHANGES.

This act amends the Workers' Compensation Act to make it fairer to employees as well as to employers and to make it simpler and easier to enforce. Among the changes made by the act are two that affect tax information. The act requires employers to include information relating to their workers' compensation coverage on the annual informational return they must file with the Department of Revenue concerning the taxes deducted and withheld from their employees' wages. The employers must name their workers' compensation insurance carriers and the number and expiration dates of their policies. If self-insured, the employers will report the name of their self-insurance group, if applicable, the names of the third parties that administer their self-insurance programs, and the employer code numbers used by the Department of Insurance for these self-insureds. The act also amends the confidentiality provisions of the revenue laws to allow the Department of Revenue to release to the Industrial Commission the information it collected on the annual informational returns concerning employers' workers' compensation coverage. The act provides that these changes became effective on the date it was ratified, July 5, 1994. Employers will be required to provide the information beginning with their next annual informational return, which is due in early 1995.

Chapter 681 (House Bill 1944, Rep. Redwine)

AN ACT TO EXPAND THE STATE PORTS TAX CREDIT.

This act changes the State ports income tax credit by expanding it to include any charges assessed on cargo exported by a taxpayer as well as any charges paid on the cargo exported by a taxpayer. The change, recommended by the Economic Development Board of the Department of Commerce, is effective for taxable years beginning on or after January 1, 1994. It is estimated that this act will reduce General Fund revenues by approximately $50,000 annually.

Many exporters sell their products "F.O.B. plant" (free on board plant), which means that the buyer rather than the seller (exporter) pays the cost of shipping the product, including the port costs for which the State ports income tax credit is

available. Under prior law, a taxpayer could claim the ports credit only for charges paid by the taxpayer. Therefore, a taxpayer who exported a product that is shipped "F.O.B. plant" could not take the credit for that export because the taxpayer did not pay for the shipping costs.

This act eliminates the requirement that a person who claims the ports credit must have paid the shipping cost. It allows a taxpayer to claim a credit for all of the port costs assessed on cargo exported by the taxpayer, regardless of who paid the costs.

The 1992 General Assembly enacted the State ports income tax credit to encourage exporters to use the two State-owned port terminals at Wilmington and Morehead City. When the credit was enacted, 70% of North Carolina exporters and importers used ports in other states to move their cargo, even though the North Carolina ports had the capacity to accommodate the additional vessels and cargo. The amount of credit allowed is equal to the amount of charges paid to the North Carolina Ports Authority in the taxable year that exceeds the average amount of charges paid to the Authority for the past three years. The credit is limited to 50% of the tax imposed on the taxpayer for the current year. Any excess credit may be carried forward and applied to the taxpayer's income tax liability for the next five years. The cumulative credit may not exceed one million dollars per taxpayer. The credit will expire in 1996.

Chapter 697 (House Bill 1775, Rep. Luebke)

AN ACT TO RESOLVE A CONFLICT IN THE DEALER LICENSE PLATE LAW CONCERNING THE USE OF DEALER LICENSE PLATES ON VEHICLES USED BY A DEALER IN A BUSINESS THAT IS SEPARATE FROM THE BUSINESS OF SELLING MOTOR VEHICLES, AND TO PROVIDE THAT A REGISTRATION CARD ISSUED FOR A DEALER PLATE IS NOT REQUIRED TO BE SPECIFIC FOR THAT DEALER PLATE.

This act makes two changes in the dealer plate laws. First, it establishes a uniform policy on the display of dealer license plates on motor vehicles that are used in a business that is separate from a dealer's business of selling motor vehicles. It does this by repealing the one exception to the general prohibition on this type of use. Second, it allows a registration card for dealer plates to be a generic card that applies to all dealer plates issued to the same dealer rather than a card that is specific to a particular dealer plate.

The first of these two changes was proposed by the Revenue Laws Study Committee. It becomes effective July 1, 1996. The second change was added by the House Transportation Committee. It became effective upon ratification, July 6, 1994.

With one exception, the dealer license plate laws prohibit a dealer from putting a dealer license plate on a motor vehicle that is used by the dealer in a business that is separate from the business of selling motor vehicles. The one exception is for a motor vehicle dealer who also sells, trades, or services farm tractors or other farm-related equipment. The law allows these dealers to put a dealer license plate on a motor vehicle that is used to haul the farm tractors or other farm-related equipment.

This one exception to the general prohibition is the result of two conflicting provisions concerning dealer license plates that were enacted in the 1993 Session. Section 169.4 of Chapter 321 of the 1993 Session Laws, the Current Operations Appropriations Act, amended the dealer license plate laws by inserting the exception to the general prohibition. Chapter 321 was ratified on July 9, 1993; the exception was effective July 1, 1993. On July 12, 1993, the General Assembly enacted Chapter 440 of the 1993 Session Laws. Chapter 440 rewrote the dealer license plate laws to restrict the number of plates that can be issued to a dealer and to set out clearly the existing restrictions on the use of dealer plates. That act, which was recommended by the Revenue Laws Study Committee, became effective October 1, 1993.

Chapter 440 made no exceptions to the general prohibition against the display of a dealer license plate on a motor vehicle that is used in a business that is separate from a dealer's business of selling motor vehicles. The exception created by Chapter 321 remained, however, even though the exception was contrary to the intent of Chapter 440.

The result is that the current law allows a dealer who sells tractors or other farm-related equipment to put a dealer plate on a vehicle used in a business that is separate from the business of selling motor vehicles and prohibits all other dealers from a similar use of dealer plates. A dealer's business of selling motor vehicles includes only the sale of motor vehicles that must have a license plate to be driven on a highway. Consequently, if a dealer both sells and services motor vehicles, the dealer cannot put a dealer plate on a motor vehicle the dealer loans to a car owner whose vehicle is being repaired by the dealer. That dealer also cannot put a dealer license plate on a motor vehicle the dealer uses to pick up parts for the vehicles the dealer services.

Dealers have been and are now generally restricted from using dealer license plates on motor vehicles that are used in a separate business of the dealer because this use is contrary to the purpose of dealer license plates and is difficult to reconcile with the requirement that a motor vehicle displaying a dealer license plate be part of the inventory of the dealer. The purpose of a dealer license plate is to allow a customer of the dealer to test-drive a motor vehicle offered for sale by the dealer and to allow the dealer to pick up a motor vehicle from its point of purchase by the dealer and to have the vehicle prepared for sale. Furthermore, a motor vehicle used regularly by the dealer for property-hauling purposes or any other purpose is not in fact part of the dealer's inventory.

The Revenue Laws Study Committee is concerned about the improper use of dealer plates because of the effect of the improper use on State and local revenues. A motor vehicle that is improperly driven with a dealer license plate escapes local property taxes, escapes State motor vehicle title and registration fees, and receives an unfair advantage on automobile insurance. It escapes property taxes because it is supposedly part of the inventory of the dealer and is, therefore, exempted from property tax by the exemption of inventory. It escapes motor vehicle title and registration fees because the title to the vehicle has not been transferred to the person who uses the vehicle. It enjoys an unfair advantage on insurance because it is insured through the dealer's blanket liability insurance policy rather than through a policy that is specific to the vehicle.

The second change made by the act implements a recommendation of the automobile dealers. The dealers explained that the requirement of having the proper registration card in a vehicle that displays a dealer plate becomes a logistical problem when the plates are switched in a short period of time from one vehicle to another. To solve the problem, they suggested that a dealer receive the same number of registration cards as dealer plates, but that each registration card be interchangeable and apply to any of the plates. Section 2 of the act changes the law to accommodate this request. The Division of Motor Vehicles of the Department of Transportation plans to implement the change by printing on a registration card issued for a dealer plate the series of dealer plates to which the card applies.

Chapter 726 (Senate Bill 1473, Sen. Kerr)

AN ACT TO ADDRESS MOTOR FUEL TAX EVASION.

This act addresses two areas of motor fuel tax evasion: cross-border movements of fuel and the use of non-tax-paid fuel in a motor vehicle for highway use. The parts of the act addressing cross-border movements of fuel were recommended by the Revenue Laws Study Committee. The act becomes effective January 1, 1995; the resulting

reduction in fuel tax evasion is expected to increase collections by an unknown amount, possibly several million dollars.

Cross-border Movement of Fuel

A cross-border movement of fuel is a movement of fuel across state borders. To avoid fuel taxes in a state with a high fuel tax rate, a person can buy fuel in one state, pay that state's tax on the fuel, bring the fuel to a state with a higher fuel tax, and then sell the fuel in that higher fuel tax state without paying the higher rate of tax. North Carolina is particularly vulnerable to tax evasion by cross-border movements of fuel because its motor fuel tax rate is 22¢ a gallon compared to 16¢ a gallon in South Carolina and 7.5¢ a gallon in Georgia. The act combats this problem through improved documentation and reporting requirements for interstate movements of fuel.

The most important change the act makes concerning cross-border movements of fuel is the "destination state" requirement. Under this requirement, a shipping paper issued by a terminal operator for fuel to be delivered by transport truck or railroad tank car must state the destination state of the fuel, the driver of the truck or the rail carrier must deliver the fuel in accordance with the listed destination state, and the buyer of the fuel is prohibited from accepting delivery if the destination state on the shipping document is not correct. Section 4 of the act contains these requirements along with sanctions for failure to comply with the requirements. For the first violation, there is a civil penalty equal to the amount of fuel tax payable on the improperly transported or diverted fuel. For a second or subsequent violation, there is a civil penalty equal to the greater of $1,000 or five times the the amount of fuel tax payable on the improperly transported or diverted fuel.

Two of our neighboring states, Virginia and Georgia, have already enacted destination state legislation. The Uniformity Committee of the Motor Fuel Tax Section of the Federation of Tax Administrators is strongly encouraging all states to enact similar legislation.

In addition to the destination state requirement, the act modifies the kind of information that must be reported to the Secretary by those who receive or deliver fuel by pipeline, marine vessel, railroad tank truck, or transport truck. Section 6 of the act requires these transporters of motor fuel to report all fuel imported into or exported from the State.

Prior law required these transporters to report all fuel imported into the State and all fuel transported from one place in the State to another place in the State. It did not require the transporters to report fuel exported from the State and it did not limit reports of tank truck movements to movements of fuel by trucks that carry at least 4,200 gallons. The prior law was not enforced, however. Section 6 therefore changes the reporting requirements by deleting both the requirement that intrastate movements be reported and the requirement that trucks designed to carry fewer than 4,200 gallons file reports and by expanding the law to include reports of exports. The section also changes the date a report is due from the 10th of each month to the 25th. This later date corresponds better to the tax reports of motor fuel, which are due either on the 20th or the 25th of each month.

The other sections of the act that concern cross-border movements of fuel make conforming changes needed to implement the destination state requirement or the modified reporting requirements. Section 1 adds definitions of "bulk plant," "destination state," "rack," "terminal," "terminal operator," and "transport truck," and clarifies the definitions of "import" and "export." All of the added or modified definitions, except that of "transport truck," reflect definitions used by the Internal Revenue Service or recommended for use by the Uniformity Committee of the Motor Fuel Tax Section of the Federation of Tax Administrators. The definition of "transport truck" is used to distinguish the large transport trucks that typically carry between

8,000 and 9,000 gallons of motor fuel from the small "tank wagons" used to carry less than 4,200 gallons.

Section 2 requires terminal operators who are not already licensed as distributors of gasoline or suppliers of diesel fuel to register with the Secretary of Revenue. There are only a few of these in the State. The registration requirement is needed to enable the Department of Revenue to enforce the requirement that terminal operators print the destination state on shipping documents and make reports to the Secretary.

Section 3 modifies the requirements that apply to persons whose only connection with motor fuel in this State is to buy it for export to another state. Under prior law, these persons could buy the fuel tax-free because it is exported to another state, and they did not have to show that they were licensed for motor fuel tax purposes with the state to which the fuel is exported. The act requires these buyers of motor fuel to establish that they are registered with another state for the payment of fuel taxes to that state before they can buy tax-free fuel in this State.

Section 5 makes a conforming change to the list of Class 1 misdemeanor gasoline tax violations to include failure to give or show a shipping document when required by Section 4 of the act. Section 5 also provides that the violations apply to a "person" rather than a "distributor," so that terminal operators as well as licensed distributors will be covered.

Sections 7 and 8 make conforming changes to the diesel fuel tax laws. Section 7 makes the destination state requirement applicable to shipments of diesel fuel; it deletes the provisions of a statute that duplicate G.S. 105-228.90 and substitutes the destination state requirement for diesel fuel. Section 8 conforms the list of Class 1 diesel fuel tax violations to the list of gasoline tax violations by adding to the list failure to give or show a shipping document when required.

Non-Tax-Paid Fuel Used on the Highways

Diesel fuel is subject to federal and State per gallon excise taxes if it is used to operate a motor vehicle on a highway. Beginning in 1994, the federal government began requiring non-tax-paid diesel fuel, which is supposed to be used only for non-highway uses, to be dyed. Diesel fuel on which the tax has been paid is therefore "clear" diesel because it is not dyed. Under the federal law, it is unlawful to use dyed diesel fuel for a highway use, and a person who operates on a highway a motor vehicle whose supply tank contains dyed diesel fuel is liable for a civil penalty equal to $10 a gallon or $1,000, whichever is greater.

Section 10 of this act makes it a State violation as well as a federal violation to use dyed diesel fuel for a highway use. A person who operates on a highway a motor vehicle whose supply tank contains dyed diesel fuel is guilty of a Class 1 misdemeanor and is liable for a civil penalty. The penalty is the greater of $1,000 or five times the amount of motor fuel tax payable on the fuel in the supply tank. This penalty is in addition to any motor fuel tax assessed.

Chapter 739 (Senate Bill 605, Sen. Seymour)

AN ACT TO EXEMPT WORKS OF ART FOR STATE BUILDINGS FROM STATE AND LOCAL SALES TAXES.

As its title indicates, this act exempts certain works of art from State and local sales and use taxes. The works of art affected are those purchased for State buildings under the State's "Art Works in State Buildings Program," which is set out in Article 47A of Chapter 143 of the General Statutes. The exemption becomes effective September 1, 1994.

The Art Works in State Buildings Program requires that one-half of one percent of the amount appropriated to construct a State building be used to buy works of art for the building. A State building is a building that is to be used by a State agency and is

to be constructed or renovated by means of a State appropriation of $1 million or more. A work of art can be sounds, such as the North Carolina sound tape in the Department of Revenue, a mural, such as the one on the side of the Department of Public Instruction's Education Building, or more traditional art forms such as sculptures or paintings. The only restriction on works of art is that they cannot be reproductions of original art by mechanical means.

This exemption is the second sales and use tax exemption specifically for works of art. G.S. 105-164.13(29) exempts works of art purchased by the North Carolina Museum of Art in whole or in part with money received through gifts or other donations.

The exemption delays the timing but not the amount of revenue received by the State. It does not affect the amount of local sales and use tax paid by the State because the State receives a refund under G.S. 105-164.14(e) of any local sales and use taxes paid. Thus, the act allows the State to retain revenue it would otherwise receive in the form of a refund. The act does not affect the net amount of State revenue because the reduction in the State's cost for the required artwork in State buildings offsets the reduction in State sales and use tax revenue.

The exemption applies to the 2% local sales and use taxes as well as the 4% State sales and use taxes. The exemption from local sales and use taxes results from G.S. 105-467. That statute limits local sales and use taxes to items that are taxed by the State at the general State 4% sales tax rate.

Chapter 745 (House Bill 1725, Rep. Jarrell)

AN ACT TO MAKE TECHNICAL AND CLARIFYING CHANGES TO THE REVENUE LAWS AND RELATED STATUTES, TO IMPROVE THE ADMINISTRATION OF THE SOFT DRINK EXCISE TAX, AND TO EXTEND THE SUNSET OF A TAX CREDIT, TO AMEND THE LAW REGARDING APPLICATION FOR CERTIFICATION AS A CLINICAL SOCIAL WORKER, TO RESTORE THE SOFT DRINK TAX EXEMPTION FOR NATURAL JUICE WITH NO ADDITIVES OTHER THAN VITAMINS, MINERALS, OR SUGAR, AND TO MAKE THE EFFECTIVE DATE OF CHANGES MADE DURING THE 1993 SESSION TO THE CONSUMER CREDIT SALE LAWS RETROACTIVE.

This act makes a number of technical and clarifying changes to various revenue laws and makes four substantive changes in these laws. The act also makes two substantive changes unrelated to revenue laws. The original bill, which consisted only of technical and clarifying changes to various revenue laws and related statutes, was recommended by the Revenue Laws Study Committee.

The first substantive change modifies liability for and payment of the soft drink excise tax. This change allows a person who is not otherwise liable for the tax to assume liability for the tax, effective October 1, 1994. It does this at the request of soft drink taxpayers who would rather be responsible for paying the tax than have to trace the method of shipment of soft drink products they receive in order to determine their liability. This change is expected to be revenue-neutral.

The soft drink excise tax is payable by the person who is the first to bring the product into the State. Who the first person is depends on how the product is brought into the State. If it is brought in by common carrier, the person who receives it is the person to bring it in. If it is brought in on a truck owned or operated by the out-of-state seller of the product, the out-of-state seller is the person to bring it in.

Taxpayers of the soft drink excise who receive products from a person who both transports some products by the person's own trucks and ships others by common carrier often find it difficult to sort out the products for which they are liable and those for which they are not. Sections 32 and 33 create a soft drink certificate of liability

that allows a taxpayer to assume liability for all soft drink products the taxpayer acquires, regardless of their mode of shipment. The act does not change the rate of tax or the total amount of tax payable.

The second substantive change extends the sunset on the corporate and individual income tax credits for constructing a fuel ethanol distillery. Under prior law, the credits were set to expire January 1, 1996. The bill extends the expiration date until January 1, 1998. A credit has never been claimed under these sections. The credit is allowed for 20% of the cost of constructing a distillery to make ethanol, at least 80% of which will be used for fuel for motor vehicles or airplanes, as a de-icer, or in a process that removes pollutants from coal or other sources of fuel. Section 34 extends the corporate credit and Section 35 extends the individual credit.

Sections 36 through 38 make the third substantive change. They prohibit a county from charging a disposal fee for the disposal of a white good while the white goods disposal tax is in effect. A white goods disposal tax is levied on the sale of a white good. The tax is $5.00 if the white good does not contain chlorofluorocarbons and it is $10 if the white good does contain chlorofluorocarbons. Although under prior law a county could not charge an additional fee to dispose of a white good, it could charge whatever fee it levied for the disposal of other types of municipal solid waste. Many taxpayers complained about the disposal fee, which was in addition to the white goods disposal tax. This change became effective August 1, 1994.

The fourth substantive change exempts from the soft drink excise tax juice whose only added ingredients are sugar, vitamins, minerals, or extracts of the juice. These juices were exempt from the excise tax prior to 1991. In 1991, the General Assembly replaced the exemption for soft drinks that contained at least 35% natural fruit juice with an exemption for soft drinks that are 100% natural fruit juice. The definition of "natural" now specifies that a product is not "natural" if it has sugar as an added ingredient.

Under the prior law, bottled juice that would be natural if it did not contain sugar was taxed at the rate of one cent (1¢) per bottle. Juice concentrate that would be natural if it did not contain sugar was taxed at the rate of $1.00 per gallon, or four-fifths of a cent (4/5¢) an ounce. Under the act, both forms of juice are exempt from the tax beginning October 1, 1994. The revenue loss from this exemption is expected to be $1 million in fiscal year 1994-95 and $1.3 to $1.5 million for each fiscal year thereafter. Section 38.2 contains this exemption.

The last two substantive changes are unrelated to the revenue laws. The first of these two changes, made by Section 38.1, extends the deadline that allows a person with experience in clinical social work to apply for certification as a clinical social worker without meeting the educational requirements. Prior to this act, a person with at least one year experience in social work could apply for certification without meeting the educational requirements of the Social Worker Certification Act if the person applied for certification prior to January 1, 1993. This act extends the deadline to include people who applied for certification between December 1, 1993, and January 15, 1994.

The second of these two changes, made by Section 38.3, amends a law enacted by the General Assembly last session. Prior to October 1, 1993, the law required that payments made by a buyer be applied to the purchases bought on credit in proportion to the amount owing on each purchase. Last year, the General Assembly changed the law to reflect the more common accounting practice of applying payments first to finance charges and then to principal in the order that each obligation is assumed. That act, however, did not address how merchants were to apply payments on accounts to which items had been charged prior to October 1, 1993. The implementation problem created by this oversight meant merchants had to bifurcate each account and divide each payment made so as to apply payments proportionally on items charged

before October 1, 1993, and to apply payments on a "first in-first out" basis to charges made after October 1, 1993. This section solves the implementation problem by allowing merchants to treat payments received on or after October 1, 1988, on a "first in-first out" basis if the seller determined, and disclosed to the buyer, that this accounting method would be used at the time the items were charged.

The technical changes are described below by section:

Section	Explanation
1	Repeals a Session Law that duplicates another Session Law, Section 18 of Chapter 485 of the 1993 Session Laws.
2	Adds a missing catchline to a subdivision.
3	Conforms statute to existing administrative practice that soft drink base products are taxed on a per container basis. If a container contains less than the unit measure (a gallon for liquid products and an ounce for dry products), the tax is reduced proportionally.
4	Reenacts a provision that may not have been rollcalled when originally enacted and corrects a grammatical error.
5	Clarifies that the deduction described in this subdivision is based on two forms of the same federal adjustment. This change was requested by the Department of Revenue.
6	Removes an unnecessary cross-reference and a reference to a repealed statute and substitutes a reference to the Code.
7	Provides an individual income tax deduction to prevent double taxation in cases in which the basis of property for State tax purposes exceeds the basis of property under the Code. For example, individual taxpayers who claim certain federal income tax credits may be required to make a reduction in the basis of their property; if there is no corresponding State tax credit, the basis for State tax purposes will be higher.
8	Clarifies that the reduction in basis required when a taxpayer takes a tax credit for a qualified business investment applies only if the taxpayer was not required to make a corresponding adjustment under the State corporate income tax.
9	Deletes a reference to a repealed subsection and clarifies that certain references to "the Secretary" mean the Secretary of State.
10	Adds a missing catchline.
11	Makes a language change that was in the 1993 Session Laws but did not go into effect due to a redlining error.
12	Deletes a word that was inadvertently retained due to a redlining error and modernizes and clarifies language.
13	Makes conforming changes to reflect the fact that the gasoline and oil inspection fee has been renamed the gasoline and oil inspection tax.
14	Removes a redundant sentence, adds a catchline, and modernizes and clarifies language.
15	Corrects an incorrect word.
16	Corrects an incorrect term.
17	Removes an obsolete reference to pensions for Confederate soldiers and widows and deletes redundant provisions.
18	Removes language that gives the incorrect impression that there are restrictions on whom a taxpayer is permitted to consult with and clarifies that an interview will not be suspended if the taxpayer is already accompanied by a representative.
19	Makes a conforming change to reflect the fact that the gasoline and oil inspection fee has been renamed the gasoline and oil inspection tax.

20 - 25 Changes the word "propel" to "operate" to clarify that fuel used to operate a motor vehicle on the highways is equally taxable whether the vehicle is moving or idling.

26 Makes a conforming change to reflect the fact that the gasoline and oil inspection fee has been renamed the gasoline and oil inspection tax and changes the word "propel" to "operate" to clarify that fuel used to operate a motor vehicle on the highways is equally taxable whether the vehicle is moving or idling.

27 Repeals a redundant statute. The substance of this statute is contained in Article 9 of Chapter 105 of the General Statutes, which governs the administration of taxes collected by the Department of Revenue.

28 In 1993, the fees for nonresident malt beverage permits and nonresident wine vendor permits were raised from $25.00 to $50.00. The 1993 legislation failed to make a conforming increase from $25.00 to $50.00 in the fee for a combined nonresident malt beverage and nonresident wine vendor permit. This section makes the conforming increase in the combined permit fee.

29 Makes a conforming change to reflect the fact that the gasoline and oil inspection fee has been renamed the gasoline and oil inspection tax. Also clarifies and modernizes the language of the statute.

30 Deletes a reference to a repealed subsection.

31 Changes a cross-reference to reflect that the powers of a regional economic development commission, formerly listed in a single statute, are now listed in several statutes in Article 2 of Chapter 158 of the General Statutes.

32-38.3 Discussed above.

39: Clarifies that real and personal property belonging to the Woodmen of the World is exempt from property tax under the exemption for fraternal or civic orders and organizations operated for nonprofit benevolent, patriotic, historical, charitable, or civic purposes. This organization is a kind of fraternal order.

40 Provides that the act is effective upon ratification except as otherwise provided: Section 11 becomes effective July 1, 1995, Sections 32 and 33 (soft drink tax liability) become effective October 1, 1994, Section 36 (no white goods fee) became effective August 1, 1994, Section 38 (white goods fee when tax repealed) becomes effective July 1, 1998, and Section 38.2 (soft drink exemption for certain juice with sugar) becomes effective October 1, 1994.

Chapter 772 (Senate Bill 733, Sen. Sherron)

AN ACT TO ESTABLISH A PARKS AND RECREATION TRUST FUND.

This act is part of a continuing effort to secure additional funds for State and local park needs. It takes a first step towards this goal by establishing the Parks and Recreation Trust Fund as a special revenue fund and by annually appropriating revenue in this Fund to the Department of Environment, Health, and Natural Resources to be used for the State Parks system (75%), matching grants to local units for local parks (20%), and the Coastal and Estuarine Water Beach Access Program (5%). As a special revenue fund, revenue in the new Trust Fund will not revert to the General Fund at the end of a fiscal year and interest and other investment income earned by the Fund will be credited to it. The act is only the first step towards the goal of securing additional funds for State and local park needs because it does not provide a source of revenue for the new Trust Fund. The act is effective upon ratification.

Although the act does not provide a source of revenue for the new Trust Fund, it declares that it is the intent of the General Assembly to dedicate an amount equal to 75% of the State's share of the deed stamp tax imposed by G.S. 105-228.30 to the new

Trust Fund and to dedicate an additional 10% of the State's share of this tax to the Recreation and Natural Heritage Trust Fund, which the act renames as the Natural Heritage Trust Fund. To implement this intent, the General Assembly must pass another act making the changes to the use of the deed stamp tax.

The deed stamp tax is an excise tax on instruments transferring real property. It is collected by the register of deeds of the county in which the property is located and is collected when the deed transferring the property is recorded. The tax rate is $1.00 for each $500.00 (0.2%) of the value of the property conveyed. Each county must remit one-half of the net proceeds of the tax to the Department of Revenue. The requirement that each county send one-half of the tax to the State was enacted in 1991 when the State doubled the tax rate from 50¢ for each $500.00 of value to $1.00 for each $500.00 of value and kept the increase.

The Department of Revenue credits 15% of the State's share of the tax to the Natural Heritage Trust Fund and credits the remaining 85% to the General Fund. The State receives approximately $14 million from this tax each year. If the intent language in this act is implemented, the State's share of the tax would be allocated among the new Parks and Recreation Trust Fund (75%), the Natural Heritage Trust Fund (10%), and the General Fund (15%).

APPENDIX D

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September 16, 1994

MEMORANDUM

TO: Revenue Laws Study Committee

FROM: Myra M. Torain and Cindy Avrette

SUBJECT: Bills Recommended to the 1994 Regular Session of the 1993 General Assembly by the Revenue Laws Study Committee

The following is a summary of the disposition of bills that were recommended by the Revenue Laws Study Committee to the 1994 Regular Session of the 1993 General Assembly. All of the committee's recommendations became law.

Legislative Proposal 1: Enacted.
Senate Bill 1619, **AN ACT TO UPDATE THE REFERENCE TO THE INTERNAL REVENUE CODE USED IN DETERMINING CERTAIN TAXABLE INCOME AND TAX EXEMPTIONS AND TO RESOLVE AN UNINTENDED CONFLICT BETWEEN THE STATUTE OF LIMITATIONS FOR CERTAIN TAX REFUNDS AND THE LAW ALLOWING DEDUCTIONS FOR CARRYBACKS, BAD DEBTS, AND WORTHLESS SECURITIES,** was introduced by Senator Winner of Buncombe and was ratified as Chapter 662 of the 1993 Session Laws.

Legislative Proposal 2: Enacted.
Senate Bill 1377, **AN ACT TO CONFORM THE THRESHOLD FOR DETERMINING IF A PENALTY APPLIES TO AN UNDERPAYMENT OF WITHHELD STATE INCOME TAXES TO THAT USED UNDER THE INTERNAL REVENUE CODE FOR DETERMINING IF A PENALTY APPLIES TO AN UNDERPAYMENT OF WITHHELD FEDERAL INCOME TAXES, AND TO CLARIFY THE TYPE OF INFORMATION A TAXPAYER MUST PROVIDE TO THE SECRETARY OF REVENUE,** was introduced by Senator Winner of Buncombe and was ratified as Chapter 661 of the 1993 Session Laws.

Legislative Proposal 3: Enacted.
House Bill 1775, **AN ACT TO RESOLVE A CONFLICT IN THE DEALER LICENSE PLATE LAW CONCERNING THE USE OF DEALER LICENSE PLATES ON VEHICLES USED BY A DEALER IN A BUSINESS THAT IS**

SEPARATE FROM THE BUSINESS OF SELLING MOTOR VEHICLES, AND TO PROVIDE THAT A REGISTRATION CARD ISSUED FOR A DEALER PLATE IS NOT REQUIRED TO BE SPECIFIC FOR THAT DEALER PLATE, was introduced by Representative Luebke and after some modification was ratified as Chapter 697 of the 1993 Session Laws. The House added a section to the bill providing that a registration card issued for a dealer plate does not have to be specific for that dealer plate. The Senate delayed the effective date of part of the bill so that a dealer who sells, trades, or services farm tractors may use a dealer plate on a vehicle owned by the dealer and used to haul farm tractors or any other farm-related equipment sold, traded, or serviced by the dealer until July 1, 1996.

Legislative Proposal 4: Enacted.
House Bill 1725, **AN ACT TO MAKE TECHNICAL AND CLARIFYING CHANGES TO THE REVENUE LAWS AND RELATED STATUTES, TO IMPROVE THE ADMINISTRATION OF THE SOFT DRINK EXCISE TAX, AND TO EXTEND THE SUNSET OF A TAX CREDIT, TO AMEND THE LAW REGARDING APPLICATION FOR CERTIFICATION AS A CLINICAL SOCIAL WORKER, TO RESTORE THE SOFT DRINK TAX EXEMPTION FOR NATURAL JUICE WITH NO ADDITIVES OTHER THAN VITAMINS, MINERALS, OR SUGAR, AND TO MAKE THE EFFECTIVE DATE OF CHANGES MADE DURING THE 1993 SESSION TO THE CONSUMER CREDIT SALE LAWS RETROACTIVE,** was introduced by Representative Jarrell and after several modifications was ratified as Chapter 745 of the 1993 Session Laws. The original bill consisted only of technical and clarifying changes. The bill enacted makes four substantive changes to the revenue laws and two substantive changes unrelated to revenue laws.

Legislative Proposal 5: Enacted.
Senate Bill 1473, **AN ACT TO ADDRESS MOTOR FUEL TAX EVASION,** was introduced by Senator Kerr and after several modifications was ratified as Chapter 726 of the 1993 Session Laws. The bill was amended by the Senate to make it a State violation as well as a federal violation to use dyed diesel fuel for a highway use.

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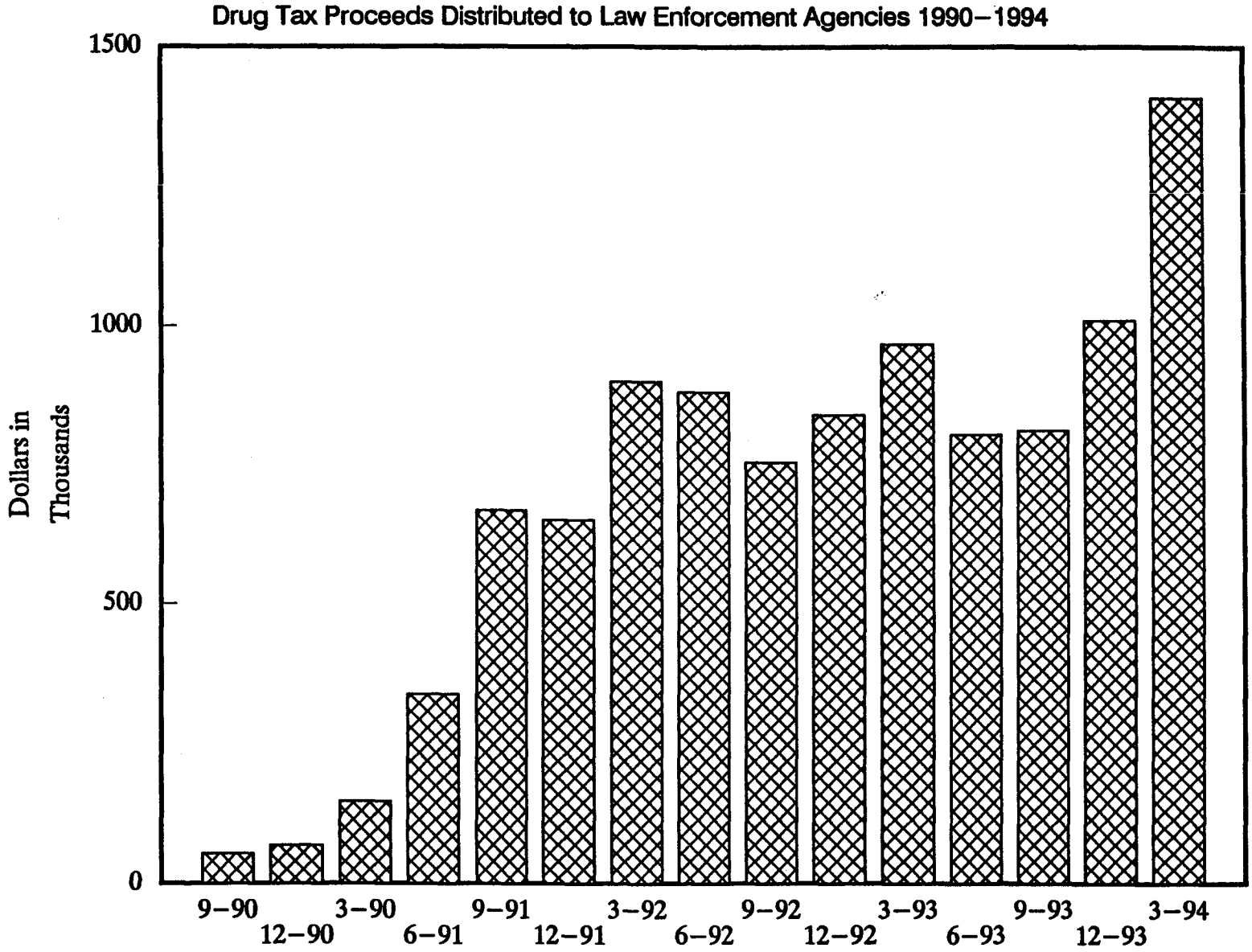
APPENDIX E


Drug Tax Proceeds Distributed to Law Enforcement Agencies 1990–1994
Dollars in Thousands
1500
1000
500
0
9–90
12–90
3–90
6–91
9–91
12–91
3–92
6–92
9–92
12–92
3–93
6–93
9–93
12–93
3–94