LEGISLATIVE

RESEARCH COMMISSION

REVENUE LAWS

REPORT TO THE
1995 GENERAL ASSEMBLY
OF NORTH CAROLINA
1996 REGULAR SESSION

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STATE OF NORTH CAROLINA
LEGISLATIVE RESEARCH COMMISSION
STATE LEGISLATIVE BUILDING
RALEIGH 27601-1096

May 1, 1996

TO THE MEMBERS OF THE 1995 GENERAL ASSEMBLY (REGULAR SESSION 1996):

The Legislative Research Commission herewith submits to you for your consideration its interim 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,

Harold J. Brubaker
Speaker of the House

Marc Basnight
President Pro Tempore

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Legislative Research Commission

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1995 - 1996

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PREFACE

The Legislative Research Commission, established by Article 6B of Chapter 120 of the General Statutes, is a general purpose study group in the legislative branch of State government. 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, prompted by actions during the 1995 Session, has undertaken studies of numerous subjects. These studies were grouped into broad categories and each member of the Commission was given responsibility for one category of study. The 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 was authorized by Section 2.1(19) of Part II of Chapter 542 of the 1995 Session Laws. That Part states that the Commission may consider House Joint Resolution 246 in determining the nature, scope, and aspects of the study. House Joint Resolution 246, introduced by Representative John Gamble in the 1995 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." The relevant portions of Chapter 542 of the 1995 Session Laws and House Joint Resolution 246 are included in Appendix A.

The Legislative Research Commission authorized the study of the revenue laws 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. The Committee is chaired by Senator John H. Kerr, III and Representative Charles B. Neely, Jr. 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 six times before the 1996 Regular Session of the 1995 General Assembly, once in January, once in February, twice in March, and twice in April. The Committee focused on issues that needed to be resolved before the convening of the 1997 General Assembly and on broad issues of tax policy.

The Committee first reviewed the tax law changes enacted in 1995 and evaluated the fate of the 1994 Revenue Laws Study Committee's sixteen recommendations to the 1995 Session. Ten of these recommendations were enacted in whole or in part in 1995. Four are pending and eligible for consideration in the 1996 Regular Session; the remaining two are not eligible for consideration in 1996. Appendix C contains a summary of tax law changes enacted in 1995; Appendix D lists the 1994 Committee's recommendations and the action taken on them during the 1995 Session.

The Committee decided that it should consider all proposed tax changes in light of general principles of tax policy and as part of an examination of the existing State tax structure as a whole. To this end, the Committee invited the following four speakers to lecture on tax policy: Dr. Charles D. Liner of the Institute of Government, Dan Gerlach of the North Carolina Budget and Tax Center, John Hood of the John Locke Foundation, and Dr. Michael L. Walden of North Carolina State University. The text of their presentations on tax policy are Appendix E, F, G, and H, respectively.

The Committee determined that fairness is the first tax policy to be considered in evaluating a proposed change in the tax law. Taxes should be uniform, applying to a broad base at low rates. Special loopholes and exemptions create a sense of inequity and require higher tax rates to make up the revenue lost due to gaps in the tax base. Fairness can be evaluated by comparing the tax burden to the benefit received or to the ability to pay.

The Committee learned that stability of the State's revenues and their responsiveness to growth in income and population are also vital. Tax neutrality is a general principal that is often ignored: a tax structure serves to raise revenues; it should not interfere unnecessarily with taxpayers' economic decisions. Administrative efficiency -- the cost of collecting a tax relative to revenues produced -- is also important, as are simplicity and ease of compliance. If taxes are overly complex and

difficult to comply with, taxpayers must waste time and money on tax paperwork and may become alienated from government and its system for raising revenues.

Based on its consideration of these tax policies, the Committee studied many issues of tax reform and tax relief. It decided to combine a number of tax reform proposals into Legislative Proposal 1, a tax package recommended for enactment in 1996. This tax reform package would implement the policies of tax fairness and tax simplicity and reduce taxes on individuals by increasing the income tax personal exemption amounts to the same level as the federal personal exemptions, and increasing these amounts each year at the same rate as inflation. This proposal provides for automatic, annual tax reductions by preventing the gradual increase in income taxes that otherwise results as inflation increases the dollar amounts, but not the real value, of individuals' incomes. Legislative Proposal 1 would also further tax fairness, tax simplicity, and tax efficiency by eliminating two of the State's most inefficient taxes: the inheritance tax and State privilege license taxes. The inheritance tax is unnecessarily complex, while the State privilege license taxes are very inequitable and uneven in their application to various types of businesses. The bill would also exempt from State inheritance and gift tax property that is exempt from federal estate and gift taxes because it is considered qualified terminable interest property.

The Committee recognized a strong policy in favor of administering taxes so that taxpayers cannot easily avoid paying the taxes they owe. When some taxpayers do not pay their taxes, the difference must be made up by raising taxes on those who comply with the law. Legislative Proposal 1 includes a provision authorizing the Department of Revenue to enter into agreements with out-of-state merchants for voluntary collection of use taxes on sales to customers in this State. Legislative Proposal 12 appropriates funds for 15 additional interstate auditors. As a general rule, each interstate auditor generates $2 million in assessments each year, 75% of which is ultimately collected. Thus, the 15 new auditors should generate $22.5 million in new, additional revenues each year. Finally, Legislative Proposal 1 contains the Committee's recommendations for addressing a series of tax provisions that, in light of a recent decision of the United States Supreme Court, may be in violation of the interstate commerce clause of the federal constitution. The Committee considered it very important, as a matter of policy, that the State's tax structure be cleansed of any provisions that may be unconstitutional.

The Committee considered many other tax policy issues that it did not include in its recommendations for enactment in 1996. Among these issues were reduction of the

corporate income tax and reduction of the State sales tax on food. The Committee considered the cost of reducing the State sales tax on food, which is $84.5 million for each cent, as well as the idea of allowing a refundable income tax credit for low and middle income taxpayers. The history of the State sales tax on food is Appendix I of this report. While tax relief measures such as these are popular, the Committee decided that it was important to consider balancing the resulting revenue losses with measures that would increase revenues. Accordingly, the Committee studied the existing tax structure to determine whether there were loopholes or special tax preferences in the law that were not supported by broad tax policies. The Committee considered but took no action regarding the tax on telecommunications, which falls on local and in-state long distance telephone calls but not on interstate telephone calls. The Committee also examined a number of preferential tax rates and provisions in the existing law. A summary of these tax preferences prepared by the Fiscal Research Division is Appendix J of this report.

As in the past, the Committee proved to be an excellent forum for taxpayers and tax administrators to propose changes in the revenue laws. A number of taxpayers wrote to or appeared before the Committee to discuss tax problems they felt need to be resolved. As a result of input from taxpayers and tax administrators, the Committee recommends the following proposals: Legislative Proposal 3, which simplifies and eases income tax penalties; Legislative Proposal 6, which provides an improved mechanism for lienholders to repossess manufactured homes while helping property tax assessors monitor taxation of the homes; Legislative Proposal 11, which allows corporations to carry their net economic loss deductions forward to the same extent as under federal law; and Legislative Proposal 14, which facilitates better monitoring of counties' use of fees collected for 911 emergency response systems.

The Committee studied numerous proposals for technical and administrative changes to the revenue laws raised by the Department of Revenue and by legislative staff. Legislative Proposal 7 clarifies the tax treatment of free items given away by merchants, an area of law that was confused for taxpayers and tax administrators as the result of an ambiguous opinion issued recently by the North Carolina Court of Appeals. Legislative Proposal 8, which transfers from the Department of Insurance to the Department of Revenue the responsibility for collecting most gross premiums taxes, reflects the policy in favor of having the State's tax collection experts, rather than other agencies, collect general revenues for the State's General Fund.

The Department of Revenue suggested that the Committee consider amending the franchise tax base to remove the amount of any debt of the taxpayer that is endorsed or guaranteed by a related corporation, because this provision is difficult to enforce and is not needed. The Committee adopted this suggestion as Legislative Proposal 10.

Legislative Proposal 4 contains the Committee's annual recommendation that references in State tax statutes to the Internal Revenue Code be updated to include federal amendments made during the past year. Legislative Proposal 13 contains the Committee's suggestions for technical, clarifying, and conforming changes to the laws.

The Committee recognized that individuals deployed in connection with the United Nations peacekeeping efforts in Bosnia and Herzegovina might miss deadlines for listing property and paying property taxes while they are away from home. To prevent this hardship, the Committee recommends Legislative Proposal 2 to allow a grace period after the end of an individual's deployment for listing property and paying property taxes.

The Committee studied the organization of the Property Tax Commission, which constitutes the State Board of Equalization and Review. The cases before the Commission are becoming increasingly complex and time-consuming. To ensure that the Commission is able to maintain qualified commissioners, the Committee recommends Legislative Proposal 5 to increase the salary of the Chair of the Commission from $200 a day to $625 a day and to increase the salary of the remaining four members of the Commission from $200 a day to $500 a day. The proposal encourages case preparation by allowing each member one additional day of pay for every three days of hearings. The proposal also provides for regional hearings conducted by a single commissioner when the appraised value of the property is less than $500,000.

Finally, Legislative Proposal 9 reflects the Committee's continuing interest in improving the enforcement of the per gallon motor fuel taxes. That proposal is the final step in this effort, which began with the Committee's 1994 recommendation to improve tracking of cross-border shipments and fuel and was continued with the Committee's 1995 recommendation to establish a uniform system for the collection of the per gallon motor fuel excise taxes on gasoline and clear diesel, thereby eliminating opportunities for tax evasion and making the system easier to administer. Legislative Proposal 9 fine tunes the new tax system and makes technical changes.

The Committee expresses its appreciation for the assistance of Ms. Janice H. 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 1996 Regular Session of the 1995 General Assembly. The Committee's legislative proposals consist of fourteen bills. Each proposal is followed by an explanation and, if it has a fiscal impact, a fiscal note indicating any anticipated revenue gain or loss resulting from the proposal.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H/S **D**

LEGISLATIVE PROPOSAL 1
95-LCX-304G(2.3)
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: 1996 Tax Reform Act. (Public)

Sponsors: Reps. Neely, Blue, Cansler, Capps, Church, Robinson, Shaw, and Shubert.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO PROVIDE TAX REFORM AND TAX RELIEF FOR THE CITIZENS OF NORTH CAROLINA.

The General Assembly of North Carolina enacts:

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I. REFORM UNCONSTITUTIONAL TAX PROVISIONS
II. VOLUNTARY USE TAX COLLECTION
III. PROVIDE AUTOMATIC ANNUAL INCOME TAX REDUCTIONS
IV. REPEAL STATE PRIVILEGE LICENSE TAXES
V. SIMPLIFY AND REDUCE INHERITANCE TAXES; REPEAL GIFT TAXES
VI. EFFECTIVE DATES

PART I. REFORM UNCONSTITUTIONAL TAX PROVISIONS

Section 1. G.S. 105-130.38, 105-151.15, and 105-151.19 are repealed.

Sec. 2. 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~~ may 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) of this section, a corporation which, at the close of its taxable year, has its commercial domicile within North Carolina shall be allowed to 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 is a shareholder in a holding company shall be allowed as a deduction an amount equal to those dividends received by it from such holding company, multiplied by a fraction, the numerator of which shall be the dividends received by such holding company attributable to North Carolina, and the denominator of which shall be the gross dividends received by such holding 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 holding company which 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 a deduction for all dividends received from such holding companies and all other corporations in which it owns more than fifty percent (50%) of the outstanding voting 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, "holding company" shall mean any 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, 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 (3a)~~ under subdivision (3) of this section ~~be in excess of~~ exceed fifteen thousand dollars ($15,000) for the taxable year."

Sec. 3. G.S. 105-130.5(b)(3) reads as rewritten:

"(3) The deductible portion of dividends from stock ~~issued by any corporation~~ as provided under G.S. 105-130.7."

Sec. 4. G.S. 105-130.4(f) reads as rewritten:

"(f) Interest and net dividends are allocable to this State if the corporation's commercial domicile is in this ~~State subject to the following limitations:~~ State. For

~~(1) Net dividends received by a corporation from another corporation in which the recipient corporation owns fifty (50%) or more per centum of the paying corporation's voting stock, shall be allocated to this State if the paying corporation is subject to income tax in this State. In such~~

~~case, the net amount of such dividends received by the recipient corporation from the paying corporation is allocable to this State by use of the same percentage figure used in determining the portion of the paying corporation's dividends deductible under the provisions of G.S. 105-130.7.~~

~~(2) For~~ purposes of this section, the ~~net amount of dividends shall mean~~ term 'net dividends' means gross dividend income received less related expenses and less that portion of ~~such~~ the dividends deductible under ~~the provisions of~~ G.S. 105-130.7."

Sec. 5. G.S. 105-163.012(b) reads as rewritten:

"(b) The total amount of all tax credits allowed to taxpayers under G.S. 105-163.011 for investments made in a calendar year may not exceed ~~twelve million dollars ($12,000,000).~~ six million dollars ($6,000,000). The Secretary of Revenue shall calculate the total amount of tax credits claimed from the applications filed pursuant to G.S. 105-163.011(c). If the total amount of tax credits claimed for investments made in a calendar year exceeds ~~twelve million dollars ($12,000,000),~~ six million dollars ($6,000,000) the Secretary shall allow a portion of the credits claimed ~~on the following basis:~~ by allocating a total of six million dollars ($6,000,000) in tax credits in proportion to the size of the credit claimed by each taxpayer.

~~(1) A total of six million dollars ($6,000,000) in tax credits for investments in North Carolina Enterprise Corporations shall be allocated among all taxpayers claiming the credits in proportion to the size of the credit claimed by each taxpayer.~~

~~(2) A total of six million dollars ($6,000,000) in tax credits for investments in qualified business ventures and qualified grantee businesses shall be allocated among all taxpayers claiming the credits in proportion to the size of the credit claimed by each taxpayer.~~

~~(3) If the total amount of the credits claimed by taxpayers for the investments described in either subdivision (1) or (2) is less than six million dollars ($6,000,000), the Secretary shall allow additional credits for the investments described in the other subdivision until the total amount of all tax credits allowed equals twelve million dollars ($12,000,000).~~"

Sec. 6. G.S. 105-130.7(4) reads as rewritten:

"(4) ~~Notwithstanding the provisions of subdivisions (1) through (3a) of this section, a corporation which, at the close of its taxable year, has its commercial domicile within North Carolina shall be allowed to~~ A corporation may deduct all ~~dividends~~ dividends, less related expenses, received from corporations in which it owns more than fifty percent (50%) of the outstanding voting stock. The amount of direct or indirect expenses related to dividends deductible under this subdivision is presumed to be fifteen percent (15%) of the amount of the dividends. A taxpayer who claims a smaller amount of related expenses must maintain and make available for inspection by the Secretary all records necessary to determine and verify the amount claimed."

Sec. 7. Division V of Article 4 of Chapter 105 of the General Statutes, as amended by this act, reads as rewritten:

"DIVISION V. TAX CREDITS FOR QUALIFIED BUSINESS INVESTMENTS.

§ 105-163.010. (Repealed effective for investments made on or after January 1, 1999) Definitions.

The following definitions apply in this Division:

(1) Affiliate. -- An individual or business that controls, is controlled by, or is under common control with another individual or business.

(2) Business. -- A corporation, partnership, association, or sole proprietorship operated for profit.

(3) Control. -- A person controls an entity if the person owns, directly or indirectly, more than ten percent (10%) of the voting securities of that entity. As used in this subdivision, the term 'voting security' means a security that (i) confers upon the holder the right to vote for the election of members of the board of directors or similar governing body of the business or (ii) is convertible into, or entitles the holder to receive upon its exercise, a security that confers such a right to vote. A general partnership interest is a voting security.

(4) Equity security. -- Common stock, preferred stock, or an interest in a partnership, or subordinated debt that is convertible into, or entitles the

holder to receive upon its exercise, common stock, preferred stock, or an interest in a partnership.

(5) Financial institution. -- A business that is (i) a bank holding company, as defined in the Bank Holding Company Act of 1956, 12 U.S.C. §§ 1841 et seq., or its wholly-owned subsidiary, (ii) registered as a broker-dealer under the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a et seq., or its wholly-owned subsidiary, (iii) an investment company as defined in the Investment Company Act of 1940, 15 U.S.C. §§ 80a-1 et seq., whether or not it is required to register under that act, (iv) a small business investment company as defined in the Small Business Investment Act of 1958, 15 U.S.C. §§ 661 et seq., (v) a pension or profit-sharing fund or trust, or (vi) a bank, savings institution, trust company, financial services company, or insurance company; provided, however, that a business, other than a small business investment company, is not a financial institution if its net worth, when added to the net worth of all of its affiliates, is less than ten million dollars ($10,000,000); provided further, however, that a business is not a financial institution if it does not generally market its services to the public and it is controlled by a business that is not a financial institution.

(6) Repealed by Session Laws 1991, c. 637.

~~(6a) North Carolina Enterprise Corporation. -- A corporation established in accordance with Article 3 of Chapter 53A of the General Statutes or a limited partnership in which a North Carolina Enterprise Corporation is the only general partner.~~

(6b) Pass-through entity. -- An entity or business, including a limited partnership, a general partnership, a joint venture, a Subchapter S Corporation, or a limited liability company, all of which is treated as owned by individuals or other entities under the federal tax laws, in which the owners report their share of the income, losses, and credits from the entity or business on their income tax returns filed with this State. For the purpose of this Division, an owner of a pass-

through entity is an individual or entity who is treated as an owner under the federal tax laws.

(7) Qualified business venture. -- A ~~North Carolina~~ business that (i) engages primarily in manufacturing, processing, warehousing, wholesaling, research and development, or a service-related industry, and (ii) is registered with the Secretary of State under G.S. 105-163.013.

(8) Qualified grantee business. -- ~~A North Carolina~~ business that (i) has received during the preceding three years a grant or other funding from the North Carolina Technological Development Authority, the North Carolina Technological Development Authority, Inc., North Carolina First Flight, Inc., the North Carolina Biotechnology Center, the Microelectronics Center of North Carolina, the Kenan Institute for Engineering, Technology and Science, or the Federal Small Business Innovation Research Program, and (ii) is registered with the Secretary of State under G.S. 105-163.013.

(9) Repealed by Session Laws 1993, c. 443, s. 1.

(9a) Real estate-related business. -- A business that is involved in or related to the brokerage, selling, purchasing, leasing, operating, or managing of hotels, motels, nursing homes or other lodging facilities, golf courses, sports or social clubs, restaurants, storage facilities, or commercial or residential lots or buildings is a real estate-related business, except that a real estate-related business does not include (i) a business that purchases or leases real estate from others for the purpose of providing itself with facilities from which to conduct a business that is not itself a real estate-related business or (ii) a business that is not otherwise a real estate-related business but that leases, subleases, or otherwise provides to one or more other persons a number of square feet of space which in the aggregate does not exceed fifty percent (50%) of the number of square feet of space occupied by the business for its other activities.

(9b) Selling or leasing at retail. -- A business is selling or leasing at retail if the business either (i) sells or leases any product or service of any

nature from a store or other location open to the public generally or (ii) sells or leases products or services of any nature by means other than to or through one or more other businesses.

(9c) Service-related industry. -- A business is engaged in a service-related industry, whether or not it also sells a product, if it provides services to customers or clients and does not as a substantial part of its business engage in a business described in G.S. 105-163.013(b)(4). A business is engaged as a substantial part of its business in an activity described in G.S. 105-163.013(b)(4) if (i) its gross revenues derived from all activities described in that subdivision exceed twenty-five percent (25%) of its gross revenues in any fiscal year or (ii) it is established as one of its primary purposes to engage in any activities described in that subdivision, whether or not its purposes were stated in its articles of incorporation or similar organization documents.

(10) Security. -- A security as defined in Section 2(1) of the Securities Act of 1933, 15 U.S.C. § 77b(1).

(11) Subordinated debt. -- Indebtedness that (i) by its terms matures five or more years after its issuance, (ii) is not secured, and (iii) is subordinated to all other indebtedness of the issuer issued or to be issued to a financial institution other than a financial institution described in subdivisions (5)(ii) through (5)(v) of this section. Any portion of indebtedness that matures earlier than five years after its issuance is not subordinated debt.

§ 105-163.011. (Repealed effective for investments made on or after January 1, 1999) Tax credits allowed.

(a) No Credit for Brokered Investments. -- No credit is allowed under this section for a purchase of equity securities or subordinated debt if a broker's fee or commission or other similar remuneration is paid or given directly or indirectly for soliciting the purchase.

~~Corporations. -- Subject to the limitations contained in G.S. 105-163.012, a corporation that purchases the equity securities of a North Carolina Enterprise Corporation directly from the Enterprise Corporation is allowed as a credit for the taxable year an amount equal to twenty-five percent (25%) of the amount~~

~~invested. The aggregate amount of credit allowed a corporation for one or more investments in a single taxable year under this Division, whether directly or indirectly as owner of a pass-through entity, may not exceed seven hundred fifty thousand dollars ($750,000). The credit is allowed against one or more of the following taxes:~~

~~(1) The income tax imposed by Division I of this Article.~~

~~(2) The franchise tax imposed by G.S. 105-116, 105-120.2, and 105-122.~~

~~(3) The gross premiums tax imposed by G.S. 105-228.5 and G.S. 105-228.8.~~

~~The credit may not be taken for the year in which the investment is made but shall be taken for the taxable year beginning during the calendar year in which the application for the credit becomes effective as provided in subsection (c) of this section. This subsection does not apply to a corporation that is also a pass-through entity.~~

(b) Individuals. -- Subject to the limitations contained in G.S. 105-163.012, an individual who purchases the equity securities or subordinated debt of ~~(i) a qualified business venture, (ii) a qualified grantee business, or (iii) a North Carolina Enterprise Corporation~~ a qualified business venture or a qualified grantee business directly from that ~~entity~~ business is allowed as a credit against the tax imposed by Division II of this Article for the taxable year an amount equal to twenty-five percent (25%) of the amount invested. The aggregate amount of credit allowed an individual for one or more investments in a single taxable year under this Division, whether directly or indirectly as owner of a pass-through entity, may not exceed fifty thousand dollars ($50,000). The credit may not be taken for the year in which the investment is made but shall be taken for the taxable year beginning during the calendar year in which the application for the credit becomes effective as provided in subsection (c) of this section.

(b1) Pass-Through Entities. -- This subsection does not apply to a pass-through entity that has committed capital under management in excess of five million dollars ($5,000,000) or to a pass-through entity that is a qualified grantee business, a qualified business venture, or a North Carolina Enterprise Corporation. Subject to the limitations provided in G.S. 105-163.012, a pass-through entity that purchases the equity securities or subordinated debt of a qualified grantee ~~business,~~ business or a qualified business ~~venture, or a North Carolina~~

~~Enterprise Corporation~~ venture directly from the business ~~or Corporation~~ is eligible for a tax credit equal to twenty-five percent (25%) of the amount invested. The aggregate amount of credit allowed a pass-through entity for one or more investments in a single taxable year under this Division, whether directly or indirectly as owner of another pass-through entity, may not exceed seven hundred fifty thousand dollars ($750,000). The pass-through entity is not eligible for the credit for the year in which the investment by the pass-through entity is made but shall be eligible for the credit for the taxable year beginning during the calendar year in which the application for the credit becomes effective as provided in subsection (c) of this section.

Each individual who is an owner of a pass-through entity is allowed as a credit against the tax imposed by Division II of this Article for the taxable year an amount equal to the owner's allocated share of the credits for which the pass-through entity is eligible under this subsection. The aggregate amount of credit allowed an individual for one or more investments in a single taxable year under this Division, whether directly or indirectly as owner of a pass-through entity, may not exceed fifty thousand dollars ($50,000).

~~Each corporation that is an owner of a pass-through entity is allowed as a credit for the taxable year an amount equal to the corporation's allocated share of the tax credits for which the pass-through entity is eligible under this subsection as a result of the pass-through entity's investment in equity securities of a North Carolina Enterprise Corporation. The credit is allowed against one or more of the following taxes:~~

~~(1) The income tax imposed by Division I of this Article.~~

~~(2) The franchise tax imposed by G.S. 105-116, 105-120.2, and 105-122.~~

~~(3) The gross premiums tax imposed by G.S. 105-228.5 and G.S. 105-228.8.~~

~~The aggregate amount of credit allowed a corporation for one or more investments in a single taxable year under this Division, whether directly or indirectly as owner of a pass-through entity, may not exceed seven hundred fifty thousand dollars ($750,000).~~

If an owner's share of the pass-through entity's credit is limited due to the maximum allowable credit under this section for a taxable ~~year or if a corporate owner is not eligible for the credit because the investment was not made in a North Carolina Enterprise Corporation,~~ year, the pass-through entity

and its owners may not reallocate the unused credit among the other owners.

(c) Application. -- To be eligible for the tax credit provided in this section, the taxpayer must file an application for the credit with the Secretary on or before April 15 of the year following the calendar year in which the investment was made. The Secretary may grant extensions of this deadline, as the Secretary finds appropriate, upon the request of the taxpayer, except that the application may not be filed after September 15 of the year following the calendar year in which the investment was made. An application is effective for the year in which it is timely filed. The application shall be on a form prescribed by the Secretary and shall include any supporting documentation that the Secretary may require. If an investment for which a credit is applied for was paid for other than in money, the taxpayer shall include with the application a certified appraisal of the value of the property used to pay for the investment. The application for a credit for an investment made by a pass-through entity must be filed by the pass-through entity.

(d) Penalties. -- The penalties provided in G.S. 105-236 apply in this Division.

§ 105-163.012. (Repealed effective for investments made on or after January 1, 1999) Limit; carry-over; ceiling; reduction in basis.

(a) The credit allowed a taxpayer under G.S. 105-163.011 may not exceed the amount of income tax imposed by Division ~~I or~~ II of this ~~Article, the amount of franchise tax imposed by Article 3 of this Chapter, or the amount of gross premiums tax imposed by Article 8B of this Chapter, as appropriate,~~ Article for the taxable year reduced by the sum of all other credits allowable except tax payments made by or on behalf of the taxpayer. The amount of unused credit allowed under G.S. 105-163.011 may be carried forward for the next five succeeding years. The fifty thousand dollar ($50,000) ~~and seven hundred fifty thousand dollar ($750,000) limitations~~ limitation on the amount of credit allowed a taxpayer under G.S. 105-163.011 ~~do~~ does not apply to unused amounts carried forward under this subsection.

(b) The total amount of all tax credits allowed to taxpayers under G.S. 105-163.011 for investments made in a calendar year may not exceed six million dollars ($6,000,000). The Secretary of Revenue shall calculate the total amount of tax credits claimed from the applications filed pursuant to G.S. 105-163.011(c). If the total amount of tax credits claimed for investments made in a calendar year exceeds six million dollars ($6,000,000) the

Secretary shall allow a portion of the credits claimed by allocating a total of six million dollars ($6,000,000) in tax credits in proportion to the size of the credit claimed by each taxpayer.

(c) If a credit claimed under G.S. 105-163.011 is reduced as provided in this section, the Secretary shall notify the taxpayer of the amount of the reduction of the credit on or before December 31 of the year following the calendar year in which the investment was made. The Secretary's allocations based on applications filed pursuant to G.S. 105-163.011(c) are final and shall not be adjusted to account for credits applied for but not claimed.

(d) ~~Unless the taxpayer is required to add the amount of allowable credit to federal taxable income under G.S. 105-130.5(a)(10), the~~ The taxpayer's basis in the equity securities or subordinated debt acquired as a result of an investment in a ~~North Carolina Enterprise Corporation,~~ qualified business ~~venture,~~ venture or qualified grantee business shall be reduced for the purposes of this Article by the amount of allowable credit. 'Allowable credit' means the amount of credit allowed under G.S. 105-163.011 reduced as provided in subsection (c) of this section.

§ 105-163.013. (Repealed effective for investments made on or after January 1, 1999) Registration.

(a) Repealed by Session Laws 1993, c. 443, s. 4.

(b) Qualified Business Ventures. -- In order to qualify as a qualified business venture under this Division, a business must be registered with the Securities Division of the Department of the Secretary of State. To register, the business must file with the Secretary of State an application and any supporting documents the Secretary of State may require from time to time to determine that the business meets the requirements for registration as a qualified business venture. A business meets the requirements for registration as a qualified business venture if all of the following are true as of the date the business files the required application:

~~(1) Its headquarters and principal business operations are in North Carolina or it has, as a condition to approval of the registration, agreed to establish its headquarters and principal business operations in North Carolina within three months after the date the first investment eligible for a credit under this Division is made.~~

(1b) Either (i) it was organized after January 1 of the calendar year in which its application is filed or (ii) during its most recent fiscal year before filing the application, it had gross revenues, as determined in accordance with generally accepted accounting principles, of five million dollars ($5,000,000) or less on a consolidated basis.

~~(2) It has, as a condition to approval of the registration, agreed to retain its headquarters and principal business operations in North Carolina for at least three years after the date the last investment eligible for credit under this Division is made.~~

(3) It is organized to engage primarily in manufacturing, processing, warehousing, wholesaling, research and development, or a service-related industry.

(4) It does not engage as a substantial part of its business in any of the following:

a. Providing a professional service as defined in Chapter 55B of the General Statutes.

b. Construction or contracting.

c. Selling or leasing at retail.

d. The purchase, sale, or development, or purchasing, selling, or holding for investment of commercial paper, notes, other indebtedness, financial instruments, securities, or real property, or otherwise make investments.

e. Providing personal grooming or cosmetics services.

f. Offering any form of entertainment, amusement, recreation, or athletic or fitness activity for which an admission or a membership is charged.

(5) It was not formed for the primary purpose of acquiring all or part of the stock or assets of one or more existing businesses.

(6) It is not a real estate-related business.

The effective date of registration for a qualified business venture whose application is accepted for registration is the filing date of its application. No credit is allowed under this Division for an investment made before the effective date of the registration or after the registration is revoked.

To remain qualified as a qualified business venture, the business must renew its registration annually as prescribed by rule by filing a financial statement for the most recent fiscal year showing gross revenues, as determined in accordance with generally accepted accounting principles, of five million dollars ($5,000,000) or less on a consolidated basis and an application for renewal in which the business certifies the facts required in the original ~~application and that it has not moved its headquarters or principal business operations out of North Carolina.~~ application.

Failure of a qualified business venture to renew its registration by the applicable deadline shall result in revocation of its registration effective as of the next day after the renewal deadline, but shall not result in forfeiture of tax credits previously allowed to taxpayers who invested in the business except as provided in G.S. 105-163.014. The Secretary of State shall send the qualified business venture notice of revocation within 60 days after the renewal deadline. A qualified business venture may apply to have its registration reinstated by the Secretary of State by filing an application for reinstatement, accompanied by the reinstatement application fee and a late filing penalty of one thousand dollars ($1,000), within 30 days after receipt of the revocation notice from the Secretary of State. A business that seeks approval of a new application for registration after its registration has been revoked must also pay a penalty of one thousand dollars ($1,000). A registration that has been reinstated is treated as if it had not been revoked.

If the gross revenues of a qualified business venture exceed five million dollars ($5,000,000) in a fiscal year, the business must notify the Secretary of State in writing of this fact by filing a financial statement showing the revenues of the business for that year.

(c) Qualified Grantee Businesses. -- In order to qualify as a qualified grantee business under this Division, a business must be registered with the Securities Division of the Department of the Secretary of State. To register, the business must file with the Secretary of State an application and any supporting documents the Secretary of State may require from time to time to determine that the business meets the requirements for registration as a qualified grantee business. A business meets the requirements for registration as a qualified grantee business if ~~all of the following are true as of the date the business files the required application:~~

~~(1) Its headquarters and principal business operations are in North Carolina or it has, as a condition to approval of the registration, agreed to establish its headquarters and principal business operations in North Carolina within three months after the date the first investment eligible for a credit under this Division is made.~~

~~(2) It has, as a condition to approval of the registration, agreed to retain its headquarters and principal business operations in North Carolina for at least three years after the date the last investment eligible for a credit under this Division is made.~~

~~(3) It~~ it has received during the preceding three years a grant or other funding from the North Carolina Technological Development Authority, the North Carolina Technological Development Authority, Inc., North Carolina First Flight, Inc., the North Carolina Biotechnology Center, the Microelectronics Center of North Carolina, the Kenan Institute for Engineering, Technology and Science, or the Federal Small Business Innovation Research Program.

The effective date of registration for a qualified grantee business whose application is accepted for registration is the filing date of its application. No credit is allowed under this Division for an investment made before the effective date of the registration or after the registration is revoked.

To remain qualified as a qualified grantee business, the business must renew its registration annually as prescribed by rule by filing an application for renewal in which the business certifies the facts listed in this subsection.

(d) Application Forms; Rules; Fees. -- Applications for registration, renewal of registration, and reinstatement of registration under this section shall be in the form required by the Secretary of State. The Secretary of State may, by rule, require applicants to furnish supporting information in addition to the information required by subsections (b) and (c) of this section. The Secretary of State may adopt rules in accordance with Chapter 150B of the General Statutes that are needed to carry out the Secretary's responsibilities under this Division. The Secretary of State shall prepare blank forms for the applications and shall distribute them throughout the State and furnish them on request. Each application shall be signed by the owners of the business or, in the case of a corporation, by its

president, vice-president, treasurer, or secretary. There shall be annexed to the application the affirmation of the person making the application in the following form: 'Under penalties prescribed by law, I certify and affirm that to the best of my knowledge and belief this application is true and complete.' A person who submits a false application is guilty of a Class 1 misdemeanor.

The fee for filing an application for registration under this section is one hundred dollars ($100.00). The fee for filing an application for renewal of registration under this section is fifty dollars ($50.00). The fee for filing an application for reinstatement of registration under this section is fifty dollars ($50.00).

An application for renewal of registration under this section shall indicate whether the applicant is a minority business, as defined in G.S. 143-128, and shall include a report of the number of jobs the business created during the preceding year that are attributable to investments that qualify under this section for a tax credit and the average wages paid by each job. An application that does not contain this information is incomplete and the applicant's registration may not be renewed until the information is provided.

(e) Revocation of Registration. -- If the Securities Division of the Department of the Secretary of State finds that any of the information contained in an application of a business registered under this section is false, it shall revoke the registration of the business. The Secretary of State shall not revoke the registration of a business solely because it ceases business operations for an indefinite period of time, as long as the business renews its registration each year as required under G.S. 105-163.013.

(f) Transfer of Registration. -- A registration as a qualified business venture or qualified grantee business may not be sold or otherwise transferred, except that if a qualified business venture or qualified grantee business enters into a merger, consolidation, or other similar transaction with another business and the surviving corporation would otherwise meet the criteria for being a qualified business venture or qualified grantee business, the surviving company retains the registration without further application to the Secretary of State. In such a case, the qualified business venture or qualified grantee business shall provide the Secretary of State with written notice of the merger, consolidation, or similar transaction and the name,

address, and jurisdiction of incorporation of the surviving company.

(g) Report by Secretary of State. -- The Secretary of State shall report to the Legislative Research Commission by October 1 of each odd-numbered year and by February 1 of each even-numbered year all of the businesses that have registered with the Secretary of State as qualified business ventures and qualified grantee businesses. The report shall include the name and address of each business, a detailed description of the types of business in which it engages, whether the business is a minority business as defined in G.S. 143-128, the number of jobs created by the business during the period covered by the report, and the average wages paid by these jobs.

§ 105-163.014. (Repealed effective for investments made on or after January 1, 1999) Forfeiture of credit.

(a) Participation in Business. -- A taxpayer who has received a credit under this Division for an investment in a qualified business venture or qualified grantee business forfeits the credit if, within three years after the investment was made, the taxpayer participates in the operation of the qualified business venture or qualified grantee business. For the purpose of this section, a taxpayer participates in the operation of a qualified business venture or a qualified grantee business if the taxpayer, the taxpayer's spouse, parent, sibling, or child, or an employee of any of these individuals or of a business controlled by any of these individuals, provides services of any nature to the qualified business venture or qualified grantee business for compensation, whether as an employee, a contractor, or otherwise. However, a person who provides services to a qualified business venture or a qualified grantee business, whether as an officer, a member of the board of directors, or otherwise does not participate in its operation if the person receives as compensation only reasonable reimbursement of expenses incurred in providing the services, participation in a stock option or stock bonus plan, or both.

(b) False Application. -- A taxpayer who has received a credit under this Division for an investment in a qualified business venture or a qualified grantee business forfeits the credit if the registration of the qualified business venture or qualified grantee business is revoked because information in the registration application was false at the time the application was filed with the Secretary of State.

~~(c) Location Out-of-State. -- A taxpayer who has received a credit under this Division for an investment in a qualified~~

~~business venture or a qualified grantee business does not forfeit the credit if the business fails to renew its registration, except that a taxpayer forfeits the credit if the qualified business venture (i) moves its headquarters or its principal business operations outside this State within three years after the date of the taxpayer's investment or (ii) in the case of a business that promised to move its headquarters and principal business operations to this State as a condition to approval of its registration, fails to comply with this condition.~~

(d) Transfer or Redemption of Investment. -- A taxpayer who has received a credit under this Division for an investment in a ~~North Carolina Enterprise Corporation, a~~ qualified business ~~venture,~~ venture or a qualified grantee business forfeits the credit in the following cases:

(1) Within one year after the investment was made, the taxpayer transfers any of the securities received in the investment that qualified for the tax credit to another person or entity, other than in a transfer resulting from one of the following:

a. The death of the taxpayer.

b. A final distribution in liquidation to the owners of a taxpayer that is a corporation or other entity.

c. A merger, consolidation, or similar transaction requiring approval by the shareholders of the ~~North Carolina Enterprise Corporation,~~ qualified business ~~venture,~~ venture or qualified grantee business under applicable State law, to the extent the taxpayer does not receive cash or tangible property in the merger, consolidation, or other similar transaction.

(2) Within five years after the investment was made, the ~~North Carolina Enterprise Corporation,~~ qualified business ~~venture,~~ venture or qualified grantee business in which the investment was made makes a redemption with respect to the securities received in the investment.

In the event the taxpayer transfers fewer than all the securities in a manner that would result in a forfeiture, the amount of the credit that is forfeited is the product obtained by multiplying the aggregate credit attributable to the investment by a fraction whose numerator equals the number of securities transferred and whose denominator equals the number of securities

received on account of the investment to which the credit was attributable. In addition, if the redemption amount is less than the amount invested by the taxpayer in the securities to which the redemption is attributable, the amount of the credit that is forfeited is further reduced by multiplying it by a fraction whose numerator equals the redemption amount and whose denominator equals the aggregate amount invested by the taxpayer in the securities involved in the redemption. The term 'redemption amount' means all amounts paid that are treated as a distribution in part or full payment in exchange for securities under section 302(a) of the Code.

(e) Effect of Forfeiture. -- A taxpayer who forfeits a credit under this section is liable for all past taxes avoided as a result of the credit plus interest at the rate established under G.S. 105-241.1(i), computed from the date the taxes would have been due if the credit had not been allowed. The past taxes and interest are due 30 days after the date the credit is forfeited; a taxpayer who fails to pay the past taxes and interest by the due date is subject to the penalties provided in G.S. 105-236."

Sec. 8. G.S. 53A-46 is repealed.

PART II. VOLUNTARY USE TAX COLLECTION

Sec. 9. Article V of Chapter 105 of the General Statutes is amended by adding a new section to read:

"**§ 105-164.6A. Voluntary collection of use tax by sellers.**

(a) Voluntary Collection Agreements. -- The Secretary may enter into agreements with sellers pursuant to which the seller agrees to collect and remit on behalf of its customers State and local use taxes due on items of tangible personal property the seller sells. For the purpose of this section, a seller is a person engaged in the business of selling tangible personal property for use in this State who does not have sufficient nexus with this State to be required to collect use tax on the sales.

(b) Mandatory Provisions. -- The agreements shall contain the following provisions:

(1) The customer may elect to pay the use tax directly to the Secretary in accordance with law rather than to the seller.

(2) A customer's payment of a use tax to the seller relieves the customer of liability for the use tax.

(3) The seller shall remit all use taxes it collects from customers on or before the due date specified in the agreement, which may not be later than 31

days after the end of a quarter or other collection period.

(4) If a seller fails to remit use taxes collected on behalf of its customers by the due date specified in the agreement, the seller is subject to the interest and penalties provided in Article 9 of this Chapter with respect to the taxes to the same extent as if it were a retailer required to collect use taxes under this Article.

(c) Optional Provisions. -- The agreements may contain the following provisions:

(1) The seller will collect the use tax only on items that are subject to the general rate of tax.

(2) The seller will collect local use taxes only to the extent they are at the same rate in every unit of local government in the State.

(3) The seller will remit the tax and file reports in the form prescribed by the Secretary.

(4) Other provisions establishing the types of transactions on which the seller will collect tax and prescribing administrative procedures and requirements."

PART III. PROVIDE AUTOMATIC ANNUAL INCOME TAX REDUCTIONS

Sec. 10. G.S. 105-134.6(c)(4a) is repealed.

Sec. 11. The Department of Revenue shall draw from collections under Division II of Article 4 of Chapter 105 of the General Statutes for the 1996-97 fiscal year the amount needed to pay for the cost of printing and mailing new withholding tables required by this act, up to a maximum of one hundred sixteen thousand six hundred dollars ($116,600) for the 1996-97 fiscal year.

PART IV. REPEAL STATE PRIVILEGE LICENSE TAXES

Sec. 12. The following sections of Article 2 of Chapter 105 of the General Statutes are repealed:

G.S. 105-36	Amusements -- Manufacturing, selling, leasing, or distributing moving picture films.
G.S. 105-36.1	Amusements -- Outdoor theatres.
G.S. 105-37	Amusements -- Moving pictures -- Admission.
G.S. 105-41	Attorneys-at-law and other professionals.
G.S. 105-42	Private detectives and investigators.
G.S. 105-45	Collecting agencies.
G.S. 105-46	Undertakers and retail dealers in coffins.
G.S. 105-50	Pawnbrokers.

G.S. 105-51.1	Alarm systems.
G.S. 105-53	Peddlers, itinerant merchants, and specialty market operators.
G.S. 105-54	Contractors and construction companies.
G.S. 105-55	Installing elevators and automatic sprinkler systems.
G.S. 105-58	Fortune tellers, palmists, etc.
G.S. 105-60	Day-care facilities
G.S. 105-61	Hotels, motels, tourist courts and tourist homes.
G.S. 105-62	Restaurants.
G.S. 105-65	Music machines.
G.S. 105-65.1	Merchandising dispensers and weighing machines.
G.S. 105-66.1.	Electronic video games.
G.S. 105-70	Packinghouses.
G.S. 105-72.	Persons, firms, or corporations selling certain oils.
G.S. 105-74	Pressing clubs, dry cleaning plants, and hat blockers.
G.S. 105-75.1.	Municipal license tax on barbershops and beauty salons.
G.S. 105-77	Tobacco warehouses.
G.S. 105-80	Firearms dealers and dealers in other weapons.
G.S. 105-85	Laundries.
G.S. 105-86	Outdoor advertising.
G.S. 105-89.	Automobiles, wholesale supply dealers and service stations.
G.S. 105-89.1	Motorcycle dealers.
G.S. 105-90	Emigrant and employment agents.
G.S. 105-91	Plumbers, heating contractors, and electricians.
G.S. 105-97	Manufacturers of ice cream.
G.S. 105-98	Branch or chain stores.
G.S. 105-99	Wholesale distributors of motor fuels.
G.S. 105-102.1	Certain cooperative associations.
G.S. 105-102.5	General business license.

Sec. 13. G.S. 105-33(b) reads as rewritten:

"(b) If the business made taxable or the privilege to be exercised under this Article is carried on at two or more separate places, a separate State license for each place is required. ~~For the purpose of this Article, a specialty market is not considered a specialty market vendor's place of business.~~"

Sec. 14. G.S. 105-33(d) reads as rewritten:

"(d) ~~The State license issued under G.S. 105-41, 105-42, 105-45, 105-53, 105-54, 105-55, 105-58, and 105-91 shall be and constitute a personal privilege to conduct the profession or business named in the State license, shall not be transferable to any other person, firm or corporation and shall be construed to limit the person, firm or corporation named in the license to conducting the profession or business and exercising the privilege named in the State license to the county and/or city and location specified in the State license, unless otherwise provided in this Article or schedule. Other~~ A license issued for a tax year for the conduct of a business at a specified location shall upon a sale or transfer of the business be deemed a sufficient license for the succeeding purchaser for the conduct of the business specified at such location for the balance of the tax year: Provided, that if the holder of a license under this schedule moves the business for which a license has been paid to another location, a new license may be issued to the licensee at a new location for the balance of the license year, upon surrender of the original license for cancellation and the payment of a fee of five dollars ($5.00) for each license certificate reissued."

Sec. 15. G.S. 105-38(g) is repealed.

Sec. 16. G.S. 105-109.1 reads as rewritten:

"**§ 105-109.1. Interest.**

The taxes on gross receipts levied in G.S. ~~105-37.1(a),~~ 105-37.1(a) and G.S. 105-38(f), ~~and 105-65.1(b)(2),~~ the tax on installment paper dealers levied in G.S. 105-83(b), and the tax on publishers of newsprint publications levied in G.S. 105-102.6, shall bear interest at the rate established under G.S. 105-241.1(i) from the time the taxes were due until the taxes are paid."

Sec. 17. G.S. 153A-152 reads as rewritten:

"**§ 153A-152. Privilege license taxes.**

A county may levy privilege license taxes on trades, occupations, professions, businesses, and franchises to the extent authorized by ~~Schedule B of the Revenue Act (Chapter 105, Subchapter I, Article 2)~~ Article 2 of Chapter 105 of the General Statutes and any other acts of the General Assembly. A county may levy privilege license taxes to the extent formerly authorized by the following sections of Article 2 of Chapter 105 of the General Statutes before they were repealed:

G.S. 105-50	Pawnbrokers.
G.S. 105-53	Peddlers, itinerant merchants, and specialty market operators.

G.S. 105-55	Installing elevators and automatic sprinkler systems.
G.S. 105-58	Fortune tellers, palmists, etc.
G.S. 105-65	Music machines.
G.S. 105-66.1	Electronic video games.
G.S. 105-80	Firearms dealers and dealers in other weapons.
G.S. 105-89	Automobiles, wholesale supply dealers and service stations.
G.S. 105-89.1	Motorcycle dealers.
G.S. 105-90	Emigrant and employment agents.
G.S. 105-102.5	General business license."

Sec. 18. G.S. 160A-211 reads as rewritten:

"**§ 160A-211. Privilege license taxes.**

(a) Authority. -- Except as otherwise provided by law, a city shall have power to levy privilege license taxes on all trades, occupations, professions, businesses, and franchises carried on within the city. A city may levy privilege license taxes on the businesses that were formerly taxed by the State under the following sections of Article 2 of Chapter 105 of the General Statutes only to the extent the sections authorized cities to tax the businesses before the sections were repealed:

G.S. 105-36	Amusements -- Manufacturing, selling, leasing, or distributing moving picture films.
G.S. 105-36.1	Amusements -- Outdoor theatres.
G.S. 105-37	Amusements -- Moving pictures -- Admission.
G.S. 105-41	Attorneys-at-law and other professionals.
G.S. 105-42	Private detectives and investigators.
G.S. 105-45	Collecting agencies.
G.S. 105-46	Undertakers and retail dealers in coffins.
G.S. 105-50	Pawnbrokers.
G.S. 105-51.1	Alarm systems.
G.S. 105-53	Peddlers, itinerant merchants, and specialty market operators.
G.S. 105-54	Contractors and construction companies.
G.S. 105-55	Installing elevators and automatic sprinkler systems.
G.S. 105-61	Hotels, motels, tourist courts and tourist homes.
G.S. 105-62	Restaurants.
G.S. 105-65	Music machines.
G.S. 105-65.1	Merchandising dispensers and weighing machines.
G.S. 105-66.1.	Electronic video games.

G.S. 105-72.	Persons, firms, or corporations selling certain oils.
G.S. 105-74	Pressing clubs, dry cleaning plants, and hat blockers.
G.S. 105-77	Tobacco warehouses.
G.S. 105-80	Firearms dealers and dealers in other weapons.
G.S. 105-85	Laundries.
G.S. 105-86	Outdoor advertising.
G.S. 105-89.	Automobiles, wholesale supply dealers and service stations.
G.S. 105-89.1	Motorcycle dealers.
G.S. 105-90	Emigrant and employment agents.
G.S. 105-91	Plumbers, heating contractors, and electricians.
G.S. 105-97	Manufacturers of ice cream.
G.S. 105-98	Branch or chain stores.
G.S. 105-99	Wholesale distributors of motor fuels.
G.S. 105-102.1	Certain cooperative associations.
G.S. 105-102.5	General business license.

(b) Barbershop and Salon Restriction. -- A privilege license tax levied by a city on a barbershop or a beauty salon may not exceed two dollars and fifty cents ($2.50) for each barber, manicurist, cosmetologist, beautician, or other operator employed in the barbershop or beauty salon."

Sec. 19. Chapter 66 of the General Statutes is amended by adding a new Article to read:

"ARTICLE 31.

"Peddlers, Itinerant Merchants, and Specialty Markets.

"**§ 66-230. Definitions.**

The following definitions apply in this Article:

(1) Itinerant merchant. -- A person, other than a merchant with an established retail store in the county, who transports an inventory of goods to a building, vacant lot, or other location in a county and who, at that location, displays the goods for sale and sells the goods at retail or offers the goods for sale at retail.

(2) Peddler. -- A person who travels from place to place with an inventory of goods, who sells the goods at retail or offers the goods for sale at retail, and who delivers the identical goods.

(3) Person. -- An individual, a firm, an association, a partnership, a limited liability company, a

corporation, a unit of government, or another group acting as a unit.

(4) Specialty market. -- A location, other than a permanent retail store, where space is rented to others for the purpose of selling goods at retail or offering goods for sale at retail.

(5) Specialty market operator. -- A person, other than the State or a unit of local government, who rents space, at a location other than a permanent retail store, to others for the purpose of selling goods at retail or offering goods for sale at retail.

(6) Specialty market vendor. -- A person, other than a merchant with an established retail store in the county, who transports an inventory of goods to a specialty market and, at that location, displays the goods for sale and sells the goods at retail or offers the goods for sale at retail.

"**§ 66-231. Itinerant merchant and peddler must have permission of property owner.**

An itinerant merchant or a peddler who travels from place to place by vehicle must obtain a written statement signed by the owner or lessee of any property upon which the itinerant merchant or peddler offers goods for sale giving the owner's or lessee's permission to offer goods for sale upon the property of the owner or lessee. This statement must clearly state the name of the owner or lessee, the location of the premises for which the permission is granted, and the dates during which the permission is valid. The statement must be conspicuously and prominently displayed, so as to be visible for inspection by patrons of the itinerant merchant or peddler, at the places or locations at which the goods are to be sold or offered for sale.

"**§ 66-232. Display and possession of retail sales tax license.**

(a) When Required. -- An itinerant merchant must keep the merchant's retail sales tax license conspicuously and prominently displayed, so as to be visible for inspection by patrons of the itinerant merchant at the places or locations at which the goods are to be sold or offered for sale. A peddler must carry the peddler's retail sales tax license when the peddler offers goods for sale and must produce the license upon the request of any customer, State or local revenue agent, or law enforcement agent. A specialty market vendor must keep the retail sales tax license conspicuously and prominently displayed, so as to be visible for inspection by patrons of the specialty market vendor at the places or locations at which the goods are to be sold or offered

for sale. A specialty market operator must have its retail sales tax license, if any, available for inspection during all times that the specialty market is open and must produce it upon the request of any customer, State or local revenue agent, or law enforcement agent.

(b) Compliance. -- The requirement that a retail sales tax license be displayed is satisfied if the vendor displays either of the following:

(1) A copy of the license.

(2) Evidence that the license has been applied for and the applicable license fee has been paid within 30 days before the date the license was required to be displayed.

"**§ 66-233. Display of identification upon request.**

Upon the request of any customer, State or local revenue agent, or law enforcement agent, a peddler, an itinerant merchant, a specialty market operator, or a specialty market vendor must provide its name and permanent address. If the peddler, itinerant merchant, specialty market operator, or specialty market vendor is not a corporation, he or she must, upon the request of any customer, State or local revenue agent, or law enforcement agent, provide a valid drivers license, a special identification card issued under G.S. 20-37.7, military identification, or a passport bearing a physical description of the person named reasonably describing the peddler, itinerant merchant, specialty market operator, or specialty market vendor. If the peddler, itinerant merchant, specialty market operator, or specialty market vendor is a corporation, it must, upon the request of any customer, State or local revenue agent, or law enforcement agent, give the name and registered agent of the corporation and the address of the registered office of the corporation, as filed with the Secretary of State.

"**§ 66-234. Records of source of new merchandise.**

(a) Record Required. -- Each peddler, itinerant merchant, and specialty market vendor must keep a written record of the source of new merchandise the merchant offers for sale. The record must be a receipt or an invoice from the person who sold the merchandise to the merchant. The invoice or receipt must specifically identify the product being sold by product name and quantity purchased and must contain the complete business name of the seller and a description of the type of business. If the seller was an individual, the receipt or invoice must contain the seller's drivers license number, its state of issuance and expiration date, and the seller's date of birth. The merchant

must verify this information by comparing the seller's drivers license to the invoice or receipt and signing the invoice or receipt. A special identification card issued by the Division of Motor Vehicles may be used in place of the seller's drivers license for the purposes of providing and verifying information required under this section. If the seller was a corporation, the receipt or invoice must contain the corporation's federal tax identification number, the state of incorporation, the name and address of the corporation's registered agent in this State, if any, and the corporation's principal office address.

(b) Keeping the Record. -- Each peddler, itinerant merchant, and specialty market vendor must keep the record required by subsection (a) of this section with the new merchandise being offered for sale. Once the new merchandise is sold, the merchant must keep the record for a period of three years after the date of the sale.

(c) Displaying Record or Affidavit. -- Upon the request of a law enforcement agent, a peddler, an itinerant merchant, or a specialty market vendor must produce either of the following:

(1) The record required by subsection (a) of this section of the source of new merchandise the merchant offers for sale.

(2) An affidavit under oath or affirmation identifying the source of new merchandise the merchant offers for sale, including the name and address of the seller, the license number of any auctioneer seller, and the date and place of purchase of the merchandise.

A merchant's failure to produce the requested record or an affidavit within a reasonable time of request by a law enforcement agent is prima facie evidence of possession of stolen property. Pending the production of the requested record or affidavit, the agent may take the merchandise into custody as evidence at the time the request is made. Merchandise impounded under this subsection must be disposed of in accordance with G.S. 15-11.1.

(d) Posted Notice. -- A specialty market operator must conspicuously post in plain view of all specialty market vendors a sign informing all vendors that failure to produce, upon the request of a law enforcement agent, either the records or affidavit required under this section is prima facie evidence of possession of stolen property.

"**§ 66-235. Specialty market registration list.**

A specialty market operator must maintain a daily registration list of all specialty market vendors selling or offering goods for sale at the specialty market. The registration list must clearly and legibly show each specialty market vendor's name, permanent address, and retail sales and use tax registration number. The specialty market operator must require each specialty market vendor to exhibit a valid retail sales tax license for visual inspection by the specialty market operator at the time of registration, and must require each specialty market vendor to keep the retail sales tax license conspicuously and prominently displayed, so as to be visible for inspection by patrons of the specialty market vendor at the places or locations at which the goods are offered for sale. Each daily registration list maintained pursuant to this section must be retained by the specialty market operator for no less than two years and must at any time be made available upon request to any law enforcement officer."

"**§ 66-236. Exemptions from Article.**

This Article does not apply to the following:

(1) A peddler or an itinerant merchant who meets any of the following descriptions:
   a. Sells farm or nursery products produced by the merchant.
   b. Sells crafts or goods made by the merchant or the merchant's own household personal property.
   c. Is a nonprofit charitable, educational, religious, scientific, or civic organization;
   d. Sells printed material, wood for fuel, ice, seafood, meat, poultry, livestock, eggs, dairy products, bread, cakes, or pies.
   e. Is an authorized automobile dealer licensed pursuant to Chapter 20 of the General Statutes.

(2) A peddler who maintains a fixed permanent location from which at least ninety percent (90%) of the peddler's sales are made but who sells some goods in the county of the fixed location by peddling.

(3) An itinerant merchant who meets any of the following descriptions:
   a. Locates at a farmer's market.
   b. Is part of the State Fair or an agriculture fair that is licensed by the Commissioner of Agriculture pursuant to G.S. 106-520.3.

c. Sells goods at an auction conducted by an auctioneer licensed pursuant to Chapter 85B of the General Statutes.

(4) A peddler who complies with the requirements of G.S. 25A-38 through G.S. 25A-42, or who complies with the requirements of G.S. 14-401.13.

"**§ 66-237. Misdemeanor violations.**

(a) Class 1 Misdemeanors. -- A person who does any of the following commits a Class 1 misdemeanor:

(1) Fails to keep a record of new merchandise offered for sale as required by G.S. 66-234.

(2) Fails to produce a record or an affidavit pursuant to G.S. 66-234.

(3) Falsifies a record of new merchandise required by G.S. 66-234.

(b) Class 3 Misdemeanors. -- A person who does any of the following commits a Class 3 misdemeanor:

(1) Knowingly gives false information when registering pursuant to G.S. 66-235.

(2) If the person is an itinerant merchant or a specialty market vendor, fails to display the retail sales tax license as required by G.S. 66-232.

(3) If the person is a peddler or specialty market operator, fails to produce the retail sales tax license as required by G.S. 66-232.

(4) Fails to obtain the permission of the property owner as required by G.S. 66-231.

(5) Fails to provide name, address, or identification upon request as required by G.S. 66-233 or provides false information in response to the request.

(6) If the person is a specialty market operator, fails to maintain the daily registration list as required by G.S. 66-235.

(c) Defense. -- Whenever satisfactory evidence is presented in any court of the fact that a retail sales tax license was not displayed or produced as required by G.S. 66-232 or that permission to use property was not displayed as required by G.S. 66-231, the person charged may not be found guilty of that violation if the person produces in court a valid retail sales tax license or valid permission, respectively, that had been issued prior to the time the person was charged.

"**§ 66-238. Local regulation not affected.**

This Article does not affect the authority of a county or city to impose additional requirements on peddlers, itinerant merchants, specialty market vendors, or specialty market operators by an ordinance adopted under G.S. 153A-125 or G.S. 160A-178."

PART V. SIMPLIFY AND REDUCE INHERITANCE TAXES; REPEAL GIFT TAXES

Sec. 20. Article 1 of Chapter 105 of the General Statutes is amended by adding a new section to read:

"**§ 105-6.1. Phase-out of inheritance tax.**

When this Article imposes an inheritance tax on property transferred by a decedent but no state death tax credit is allowed under section 2011 of the Code against federal estate tax due on the transfer of the decedent's estate, the amount of inheritance tax is reduced by the appropriate percentage in the phase-out table set out below. When this Article imposes an inheritance tax on property transferred by a decedent and a state death tax credit is allowed under section 2011 of the Code against federal estate tax due on the transfer of the decedent's estate, the amount of inheritance tax that exceeds the maximum credit for state death taxes is reduced by the appropriate percentage in the following phase-out table:

Calendar Year Of Decedent's Death	Percentage Reduction
1997	20%
1998	40%
1999	60%
2000	80%
2001 and after	100%."

Sec. 21. 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. 22. 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. 23. 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. 24. 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. 25. Article 1 of Chapter 105 of the General Statutes is amended by adding a new section to read:

"**§ 105-23.1. Making installment payments of tax due when federal estate tax is payable in installments.**

A personal representative who elects under section 6166 of the Code to make installment payments of federal estate tax may elect to make installment payments of the tax imposed by this Article. An election under this section extends the time for payment of the tax due in accordance with the extension elected under section 6166 of the Code. Payments of tax are due under this section at the same time and in the same proportion to the total amount of tax due as payments of federal tax under section 6166

of the Code. Acceleration of payments under section 6166 of the Code accelerates the payments due under this section."

Sec. 26. Effective January 1, 1999, Article 6 of Chapter 105 of the General Statutes is repealed.

Sec. 27. Effective January 1, 2001, Article 1 of Chapter 105 of the General Statutes is repealed.

Sec. 28. Effective January 1, 2001, Chapter 105 of the General Statutes is amended by adding a new Article to read:

"ARTICLE 1A.

"Estate Taxes.

"**§ 105-32.1. Definitions.**

The following definitions apply in this Article:

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

(2) Personal representative. -- The person appointed by the clerk of superior court under Chapter 28A of the General Statutes to administer the estate of a decedent or, if no one is appointed under that Chapter, the person required to file a federal estate tax return for the estate of the decedent.

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

"**§ 105-32.2. Estate tax imposed in amount equal to federal state death tax credit.**

(a) Tax. -- An estate tax is imposed on the transfer of the estate of a decedent when a federal estate tax is imposed on the transfer of the estate under section 2001 of the Code and any of the following apply:

(1) The decedent was a resident of this State at death.

(2) The decedent was not a resident of this State at death and owned any of the following:

a. Real property or tangible personal property that is located in this State.

b. Intangible personal property that has a tax situs in this State.

(b) Amount. -- The amount of the estate tax imposed by this section is the maximum credit for state death taxes allowed under Section 2011 of the Code. If property in the estate is located in a state other than North Carolina, the amount of tax payable is the North Carolina percentage of the credit.

If the decedent was a resident of this State at death, the North Carolina percentage is the net value of real property in the estate that is located in North Carolina plus the net value of all personal property in the estate that does not have a tax situs in another state, divided by the net value of all the property in the estate. If the decedent was not a resident of

this State at death, the North Carolina percentage is the net value of real property in the estate that is located in North Carolina plus the net value of any personal property in the estate that has a tax situs in North Carolina, divided by the net value of all property in the estate, unless the decedent's state of residence uses a different formula to determine the North Carolina percentage. In that circumstance, the North Carolina percentage is the amount determined by the formula used by the decedent's state of residence.

The net value of property that is located in or has a tax situs in this State is its gross value reduced by any debt secured by that property. The net value of all the property in the estate is its gross value reduced by any debts of the estate.

"**§ 105-32.3. Liability for estate tax.**

(a) Primary. -- The tax imposed by this Article is payable from the assets of the estate. A person who receives property from an estate is liable for the amount of estate tax attributable to that property.

(b) Personal Representative. -- The personal representative of an estate is liable for an estate tax that is not paid within two years after it was due. This liability is limited to the value of the assets of the estate that were under the control of the personal representative. The amount for which the personal representative is liable may be recovered from the personal representative or from the surety on any bond filed by the personal representative under Article 8 of Chapter 28A of the General Statutes.

(c) Clerk of Court. -- A clerk of court who allows a personal representative to make a final settlement of an estate without presenting one of the following is liable on the clerk's bond for any estate tax due:

(1) An affirmation by the personal representative certifying that no tax is due on the estate because this Article does not require an estate tax return to be filed for that estate.

(2) A certificate issued by the Secretary stating that the tax liability of the estate has been satisfied.

"**§ 105-32.4. Payment of estate tax.**

(a) Due Date. -- The estate tax imposed by this Article is due when an estate tax return is due. An estate tax return is due on the date a federal estate tax return is due.

(b) Filing Return. -- An estate tax return must be filed under this Article if a federal estate tax return is required. The

return must be filed by the personal representative of the estate on a form provided by the Secretary.

(c) Extension. -- An extension of time to file a federal estate tax return is an automatic extension of the time to file an estate tax return under this Article. The Secretary may, in accordance with G.S. 105-263, extend the time for paying the estate tax imposed by this Article or for filing an estate tax return.

(d) Interest and Penalties. -- The penalties in G.S. 105-236 apply to the failure to file an estate tax return or to pay an estate tax when due. Interest at the rate set in G.S. 105-241.1 accrues on estate taxes paid after the date they are due.

(e) Obtaining Amount Due. -- The personal representative of an estate may sell assets in the estate to obtain money to pay the tax imposed by this Article.

"**§ 105-32.5. Making installment payments of tax due when federal estate tax is payable in installments.**

A personal representative who elects under section 6166 of the Code to make installment payments of federal estate tax may elect to make installment payments of the tax imposed by this Article. An election under this section extends the time for payment of the tax due in accordance with the extension elected under section 6166 of the Code. Payments of tax are due under this section at the same time and in the same proportion to the total amount of tax due as payments of federal estate tax under section 6166 of the Code. Acceleration of payments under section 6166 of the Code accelerates the payments due under this section.

"**§ 105-32.6. Estate tax is a lien on property in the estate.**

The tax imposed by this Article on an estate is a lien on the real property in the estate and on the proceeds of the sale of the real property in the estate. The lien is extinguished when one of the following occurs:

(1) The personal representative certifies to the clerk of court that no tax is due on the estate because this Article does not require an estate tax return to be filed for that estate.

(2) The Secretary issues a certificate stating that the tax liability of the estate has been satisfied.

(3) For specific real property, when the Secretary issues a tax waiver for that property.

(4) Ten years have elapsed since the date of the decedent's death.

"**§ 105-32.7. Federal determination that changes the maximum state death tax credit allowed.**

If the federal government corrects or otherwise determines the amount of the maximum state death tax credit allowed an estate under section 6166 of the Code, the personal representative must, within two years after being notified of the correction or final determination by the federal government, file an estate tax return with the Secretary reflecting the correct amount of tax payable under this Article. The Secretary must assess and collect any additional tax due on the estate as provided in Article 9 of this Chapter and must 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.

"**§ 105-32.8. Generation skipping transfer tax.**

(a) Tax. -- A tax is imposed on a generation skipping transfer that is subject to the tax imposed by Chapter 13 of Subtitle B of the Code in the following circumstances:

(1) When the original transferor is a resident of this State at the date of the original transfer. In this circumstance, the tax is the amount of the credit for State generation-skipping transfer taxes allowed under section 2604 of the Code that exceeds the amount of taxes paid on the transfer to all states other than this State.

(2) When the original transferor is not a resident of this State at the date of the original transfer and the transfer includes real or personal property with a situs in this State. In this circumstance, the tax is the amount of the credit for State generation-skipping transfer taxes allowed under section 2604 of the Code, reduced by an amount that bears the same ratio to the federal credit as the value of the transferred property taxable by all states other than this State bears to the gross value of the generation-skipping transfer.

(b) Payment. -- The tax imposed by this section is due when a return is due. A return is due the same date as the federal return for payment of the federal generation-skipping transfer tax. The tax is payable by the person who is liable for the federal generation-skipping transfer tax."

PART VI. EFFECTIVE DATES

Sec. 29. Notwithstanding G.S. 105-163.15 and G.S. 105-163.41, no addition to tax may be made under either of those statutes for a taxable year beginning on or after January 1, 1996, and before January 1, 1997, with respect to an underpayment of individual or corporation income tax to the extent the underpayment was created or increased by this act.

Sec. 30. 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. 31. This act becomes effective as follows:

(1) Unconstitutional Tax Preferences -- Sections 1 through 4 of Part I of this act are effective for taxable years beginning on or after January 1, 1996.

(2) $6 Million Cap on Qualified Investments. -- Section 5 of Part I of this act is effective for investments made on or after January 1, 1996.

(3) Subsidiary Dividend Deduction. -- Section 6 of this act is effective for taxable years beginning on or after January 1, 1997.

(4) Modify Qualified Business Investment Credits. -- Sections 7 through 8 of Part I of this act become effective for investments made on or after January 1, 1997.

(5) Voluntary Use Tax Collection. -- Part II of this act is effective upon ratification.

(6) Automatic Annual Income Tax Reductions. -- Part III of this act is effective for taxable years beginning on or after January 1, 1997.

(7) Repeal Privilege License Taxes. -- Part IV of this act becomes effective July 1, 1997.

(8) Inheritance and Gift Tax Changes. -- Sections 20 through 23 of Part V become effective January 1, 1997, and apply to the estates of decedents dying on or after that date. Sections 24 and 25 of Part V become effective July 1, 1996, and apply to the estates of decedents dying on or after that date. Section 26 of Part V becomes effective January 1, 1999, and applies to gifts made on or after that date. Sections 27 and 28 of Part V become

effective January 1, 2001, and apply to the estates of decedents dying on or after that date.

(9) Remainder. -- The remainder of this act is effective upon ratification.

Explanation - 1996 Tax Reform Act

INTRODUCTION

Legislative Proposal 1 would provide tax reform and tax relief for the citizens of North Carolina. The proposal is divided into six parts. Part I would revise certain North Carolina tax preferences that appear to violate the interstate commerce clause of the United States Constitution. Part II would enhance compliance and enforcement of existing tax laws by authorizing the Secretary of Revenue to enter into agreements for voluntary collection of use taxes by direct marketers over which the State has no jurisdiction. Part III would provide automatic annual income tax reductions for individuals by increasing the amount of the personal exemption and indexing it to rise automatically at the same rate as inflation. Part IV would repeal most State privilege license taxes on businesses and professions and Part V would simplify and reduce inheritance taxes. Part VI of Legislative Proposal 1 sets out the effective date for these tax law changes. Each Part of the proposal is explained below.

PART I. REFORM UNCONSTITUTIONAL TAX PROVISIONS

Part I of Legislative Proposal 1 would repeal several tax preferences for North Carolina stock: the corporate income tax deductions for North Carolina dividends, the individual income tax credit for North Carolina dividends, the tax credits for investments in North Carolina Enterprise Corporations, and the corporate tax credits for qualified business investments. It would also repeal a tax preference for distributors of North Carolina wine. In addition, it would restrict the remaining tax credits for qualified business investments to direct investments by individuals or small partnerships in qualified businesses, remove the requirement that qualified businesses be headquartered and operating in North Carolina, and cap the credits at $6 million a year. Finally, Part I would expand the subsidiary dividend deduction to non-domiciled corporations and require that related expenses be subtracted from dividends in calculating the deduction. The changes to the qualified business investment credits would become effective for investments made on or after January 1, 1997. The changes to the subsidiary dividend deduction would become effective beginning with the 1997 tax year. The $6 million cap on credits for qualified business investments and the repeal of the other North Carolina tax preferences would become effective beginning with the 1996 tax year.

Repeal and reform of these North Carolina tax preferences is recommended because of their similarity to a provision of the intangibles tax that was recently declared unconstitutional by the United States Supreme Court. The constitutional issues are complex. As explained in the attachment to this summary, the tax preferences addressed by this bill probably have the same constitutional problem as the intangibles tax provision struck down by the Supreme Court.

-----**Fiscal Impact of Reforming Unconstitutional Tax Preferences**

Repeal of the corporate income tax deductions for North Carolina dividends is expected to increase General Fund revenues by $2 million a year. If the deductions are not repealed and are challenged successfully in court, North Carolina could be liable for $20 - $40 million in refunds plus interest. The fiscal issues surrounding the subsidiary dividend deduction are discussed below. The fiscal impact of expanding or restricting this provision is more significant because it is not subject to the $15,000 cap per taxpayer that applies to the North Carolina dividend deductions. Repeal of the individual income tax credit for North Carolina dividends is expected to increase General Fund revenues by $11 million a year. If the credit is not repealed and is challenged successfully in court, North Carolina could be liable for $213 million in refunds plus another $14 million in interest. Repeal of the income tax credits for distributing North Carolina wine is expected to increase General Fund revenue by less than $20,000. If the credits are not repealed, North Carolina could be liable for an amount equal to 20¢ times the number of liters of wine on which each taxpayer paid excise tax for a three-year period. If the damages were limited to excise taxes paid to North Carolina, they could be up to $15 - 20 million plus interest. If the damages cover excise taxes paid to other states, the amount would be much greater. Reform of the qualified business investment credits would probably not affect General Fund revenues, although lowering the cap from $12 million to $6 million a year prevents a potential future revenue reduction of $2 - $6 million. It is not known how much the potential damages would be if the credits were not reformed and were challenged successfully in court.

-----**Description of Tax Preferences Affected**

The corporate income tax deductions for North Carolina dividends found in G.S. 105-130.7 include several separate provisions. Repeal of these dividend deductions is expected to have only a small impact on taxpayers because the deductions are all subject to a $15,000 cap. Subdivision (1) of G.S. 105-130.7 allows a deduction for corporate dividends to the extent the issuing corporation's income is derived from business done in North Carolina. Subdivision (2) of G.S. 105-130.7 allows a deduction for an out-of-state insurance company's dividends to the extent it does business in North Carolina and allows a deduction for 100% of a North Carolina insurance company's dividends. Subdivision (3a) of G.S. 105-130.7 allows a deduction for 100% of a North Carolina savings institution's dividends. Subdivision (5) of G.S. 105-130.7 allows the above North Carolina dividend deductions to be passed through a holding company from corporations in which it owns stock to its corporate stockholders, if at least one-third of the dividends received by the holding company are from North Carolina sources.

Subdivision (4) of G.S. 105-130.7 is a deduction not for dividends received from North Carolina corporations but for dividends received by North Carolina parent corporations from their subsidiaries. Part I of Legislative Proposal 1 extends this deduction to out-of-state parent corporations and modifies the deduction to require related expenses to be subtracted from the dividends before they are deducted. The subsidiary dividend deduction is discussed at more length below.

The individual income tax credit for North Carolina dividends is found in G.S. 105-151.19. It allows a credit of 6% of the amount of dividends a taxpayer receives from a corporation that does 50% or more of its business in North Carolina. The credit is capped at $300 per taxpayer and $600 per married couple filing a joint return.

The individual and corporate income tax credits for distributing North Carolina wine are found in G.S. 105-130.38 and 105-151.15. They allow a credit equal to 20¢ times the number of liters of North Carolina wine on which a distributor paid North Carolina excise tax. The credit applies to wineries, wine wholesalers, and wine importers. North Carolina wine is wine that is at least 60% North Carolina-grown fruits and berries and is part of the first 950 liters of wine produced per ton of North Carolina-grown fruits or berries.

The qualified business investment tax credits, in G.S. 105-163.010 through G.S. 105-163.014, allow individuals and corporations credit against income taxes, gross premiums taxes, or franchise taxes for 25% of their investments in qualified North Carolina businesses registered with the Secretary of State or in North Carolina

Enterprise Corporations. To qualify, the North Carolina business must have its headquarters and most of its operations in North Carolina. A North Carolina Enterprise Corporation must invest in businesses with headquarters and most operations in North Carolina. The tax credits are subject to a cap of $50,000 for individuals and $750,000 for corporations.

-----Revise Subsidiary Dividend Deduction

G.S. 105-130.7(4) allows a corporation domiciled in North Carolina that holds more than 50% of the outstanding voting stock of another corporation (a subsidiary) to deduct dividends it receives from the subsidiary. The restriction of this deduction to North Carolina corporations creates interstate commerce clause problems in light of the Fulton decision. In an informal discussion with staff of the Revenue Laws Study Committee, representatives of the Revenue Section of the Attorney General's Office confirmed the opinion of committee staff that this provision would not survive a constitutional challenge. It is true that most subsidiary dividends of non-domiciled corporations are not included in North Carolina taxable income anyway -- as non-business income, they are allocated to the state of domicile under uniform rules for allocating multi-state corporations' income among the states in which they do business. For subsidiary dividends that are business income, however, no allocation or deduction is allowed to non-domiciled companies. Furthermore, the law that allows domiciled companies a deduction and non-domiciled companies an allocation discriminates because the allocation is less generous than the deduction. Related expenses must be netted out from the amount allocated but related expenses are apparently not required to be netted from the amount deducted.

The Committee was placed in a difficult position when it learned that the existing subsidiary dividend deduction discriminates against out-of-state companies. Because of the recent United States Supreme Court decision in the Fulton case, the State is on notice that the federal constitution does not allow this type of discrimination. In addition to the likelihood of the State having to make refunds if the law were challenged, a federal court could hold the personnel of the Department of Revenue personally liable under 42 U.S.C. § 1983 for knowingly enforcing an unconstitutional law. Moreover, the State could be forced to pay attorneys fees.

In order to provide constitutionally acceptable equal treatment of North Carolina companies and out-of-state companies, the General Assembly could merely repeal the subsidiary dividend deduction, but this repeal would cause a significant tax increase for North Carolina parent corporations. The obvious choice is to extend the subsidiary

dividend deduction to non-domiciled companies. As part of this recommendation, the Revenue Laws Study Committee was forced to equalize the expense treatment for North Carolina companies and other companies as well. Representatives of the Revenue Section of the Attorney General's Office have given committee staff an informal, oral indication that unless all companies are either required to net related expenses or allowed to deduct gross dividends without netting related expenses, the law will likely violate the interstate commerce clause of the federal constitution.

Having to make this choice created a dilemma for the Study Committee. Allowing deduction of only net dividends would be consistent with general tax policy and would cause a gain to the General Fund, but would cause a tax increase for North Carolina parent companies even if the negative effect on taxpayers were offset somewhat by simplifying the rules for determining the amount of related expenses that must be netted from dividends. Allowing deduction of gross dividends would cause a loss to the General Fund by decreasing taxes on out-of-state companies and would be inconsistent with general tax policy that dictates that expenses incurred in generating non-taxable income should not be deductible from taxable income.

It is a general rule of tax policy that expenses related to untaxed income should not be deductible from taxed income. This policy is reflected in section 265 of the Code and in G.S. 105-130.5(c)(3). The deduction for subsidiary dividends operates to exempt the dividends from tax; they appear to be untaxed income for the purpose of this policy. Allowing a net dividend deduction would be consistent with the policy expressed in G.S. 105-130.5(c)(3). For example, if a corporation earns $10 million in gross income and has expenses of $4 million in generating this income, and half the gross income is deductible subsidiary dividends, then assuming the expenses are proportionally related to each category of income, a net dividend deduction yields taxable income of $3 million ($10 minus $4 expenses minus $3 net dividends) while a gross dividend deduction yields taxable income of $1 million ($10 minus $4 expenses minus $5 gross dividends).

Section 6 of Part I of Legislative Proposal 1 reflects the Committee recommendation that the subsidiary dividend deduction should be extended to out-of-state corporations and that related expenses should be netted from dividends before the dividends are deducted. The negative impact of this provision on in-state companies may be lessened somewhat by a proposed 15% cap on the amount of related expenses that must be netted. If a parent corporation can show that its actual related expenses are less than 15% of dividends, then it can net the lesser amount.

PART II. VOLUNTARY USE TAX COLLECTION

Part II of Legislative Proposal 1 would enhance compliance and enforcement of existing tax laws by authorizing the Secretary of Revenue to enter into agreements under which direct marketers over which the State has no jurisdiction would agree to collect use taxes on sales to North Carolina customers.

Many North Carolina residents order products from direct marketers in other states. Because the sales occurs in another state, North Carolina sales tax does not apply. The resident is, however, liable for paying a use tax on the property ordered. Most residents do not pay this use tax and it would be extremely inefficient for the State to try to pursue every individual for the use tax due on their mail order purchases. In order for the State to be able to require a direct marketer to collect use tax, the marketer must have some minimal contact (nexus) with the State. If the direct marketer has a store in North Carolina or other ties sufficient to give the State jurisdiction over it, the marketer can be required to collect the tax on sales to North Carolina residents. If the direct marketer does business with North Carolina residents only through telephone, mail, and freight transactions, it does not have "nexus" with this state and is not required to collect the tax. The United States Supreme Court has held that states' efforts to require these out-of-state marketers to collect sales or use tax on sales to residents violate the interstate commerce clause of the United States Constitution.

As a result of these constitutional restrictions, out-of-state direct marketers have a competitive advantage over in-state merchants, and states lose significant amounts of revenue. A few direct marketers collect and remit use taxes voluntarily as a convenience to their customers. The Direct Marketers Association, the Federation of Tax Administrators, and the Multi-state Tax Commission are currently negotiating a possible agreement under which more direct marketers would voluntarily collect use tax on behalf of customers in states in which the marketers do not have nexus. Under this agreement, tax collection would be simplified by using the same form and payment deadlines in every state. In addition, the direct marketers would collect at only one rate per state; non-uniform county and city rates would be disregarded. If these parties are able to design a system that would be acceptable to all involved, North Carolina would need authority to enter into such an agreement. Part II of Legislative Proposal 1 would provide that authority and set out some of the parameters for the agreement. If the ongoing negotiations result in a viable multi-state program for collection of use taxes by direct marketers and North Carolina enters into agreements pursuant to the

program, the Department of Revenue could potentially collect millions of dollars in use taxes that are owed under current law but are not being paid.

PART III. PROVIDE AUTOMATIC ANNUAL INCOME TAX REDUCTIONS

Part III of Legislative Proposal 1 would increase the State income tax personal exemptions to the amount of the federal personal exemptions, and provide that the exemption amounts would increase automatically each year at the same rate as the federal exemptions, based on the rate of inflation. This Part would become effective beginning with the 1997 tax year. Increasing the personal exemption amounts reduces State income taxes for all individuals who pay income tax.

The State's personal exemption amounts were increased in 1995 in two stages, from $2,000 to $2,250 for the 1995 tax year and then to $2,500 for the 1996 tax year. The federal personal exemption amounts increase automatically each year to keep pace with inflation. The federal amount for the 1996 tax year is $2,550 and is expected to increase about $50 each year thereafter. Increasing the State's personal exemption amounts to the federal amounts, and allowing them to grow at the same pace in future years has three benefits. First, it reduces State personal income taxes for all North Carolina citizens who pay income tax. Families with children receive a larger tax reduction because a personal exemption deduction is allowed for the taxpayer, the spouse, and each dependent. Second, it allows the State tax structure to respond automatically to inflation. If the personal exemption amounts are not indexed to inflation, taxpayer's taxes increase automatically each year because the value of their income dollars is inflated, even if, in real terms, they make the same amount of income or less income each year. Third, it greatly simplifies tax filing. North Carolina's individual income tax uses federal taxable income as the starting point for calculating North Carolina taxable income. As long as North Carolina's personal exemptions are not indexed to the federal amounts, every taxpayer must perform an extra calculation to adjust for the gap by adding back to federal taxable income the difference between the lower North Carolina personal exemption amount and the higher federal personal exemption amount.

PART IV. REPEAL STATE PRIVILEGE LICENSE TAXES

This Part makes the following changes concerning privilege license taxes:

(1) It repeals all State privilege license taxes imposed under Article 2 of Chapter 105 of the General Statutes except for the taxes imposed by G.S. 105-37.1 (amusements); 105-38 (circuses and similar shows); 105-83

(installment paper dealers); 105-88 (loan agencies or brokers); 105-102.3 (banks); and 105-102.6 (newsprint publications).

(2) It preserves the status quo on privilege license taxation for cities and counties. The current limitations and authorizations in Article 2 that apply to cities and counties would continue to apply.

(3) It preserves the itinerant merchant license and regulatory provisions but moves them to Chapter 66, Commerce and Business.

The recommendations in this Part are the product of the committee's subcommittee on privilege license taxes. That subcommittee found that the privilege license tax structure in Article 2 of Chapter 105 of the General Statutes is outmoded, inefficient, and not designed on proper principles of taxation such as tax fairness, ability to pay, responsiveness to growth, or administrative cost. The subcommittee found no rationale for a tax on the privilege to work that applies only to a limited portion of businesses or the work force and that has a different and inconsistent tax rate for each different class of business. Because the tax is not indexed to any economic parameter, the cost to administer the tax has become increasingly high over time compared to the amount of tax collected. As a result, the tax has become more of a nuisance tax than a properly designed source of revenue for the State.

The subcommittee therefore recommended the changes in this Part and made recommended that the subcommittee on privilege license taxes continue to work on a proposal for consideration after the 1996 Regular Session that will:

(1) Repeal the State privilege license taxes in Article 2 that are not repealed in the 1996 Regular Session and restructure other taxes where necessary in light of the repeal.

(2) Repeal the local privilege license tax restrictions and authorizations in Article 2 and replace them with a uniform system of local privilege license taxes based on sound principles of taxation.

PART V. SIMPLIFY AND REDUCE INHERITANCE TAXES; REPEAL GIFT TAXES

This Part changes the inheritance and gift tax laws as follows:

(1) Phases out the current inheritance tax over 5 years, beginning with calendar year 1997, by reducing all inheritance taxes payable during that period by 20% each year.

(2) Retains the federal "pick-up" tax, which is the federal state death tax credit, as the state estate tax.

(3) Repeals the gift tax effective January 1, 1999.

(4) Conforms the inheritance and gift taxation of property placed in a qualified terminable interest trust to the federal estate and gift tax treatment of the property, effective January 1, 1997..

(5) Allows installment payments of State inheritance or estate tax in the same circumstances in which installment payments of federal estate tax are allowed. This provision applies to closely-held businesses.

(6) Provides that expenses deducted on a fiduciary income tax return cannot also be deducted on the inheritance or estate tax return.

-----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.

------Conform to Federal QTIP

This proposal exempts from State inheritance and gift tax property that is exempt from federal estate and gift taxes because it is considered qualified terminable interest property. The previous Revenue Laws Study Committee recommended the same proposal for two reasons. First, the committee found that conforming to federal law on this topic would provide consistent treatment at the federal and State level. Second,

the committee found that 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.

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 other 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 * of this Part prohibits the deduction of an item on an inheritance tax return if the item was deducted on the federal fiduciary income tax return.

PART VI. EFFECTIVE DATES

Part VI provides the effective dates of each provision of Legislative Proposal 1.

ATTACHMENT

CONSTITUTIONAL ANALYSIS OF TAX PREFERENCES

On February 21, 1996, the United States Supreme Court ruled in Fulton Corp. v. Faulkner that North Carolina's intangibles tax on stock is unconstitutional because it discriminates against interstate commerce in violation of the commerce clause of the United States Constitution. The Court noted that the commerce clause prohibits economic protectionism -- that is, laws "designed to benefit in-state economic interests by burdening out-of-state competitors." The commerce clause, Article I, Section 8, Paragraph 3, of the United States Constitution, states simply, "The congress shall have power... To regulate commerce with foreign nations, and among the several states." This brief provision has given rise to a long stream of litigation, and the courts have expounded upon it in a multitude of cases. Among the most well-founded of case law principles is that one state cannot discriminate in favor of local commerce against out-of-state commerce.

The intangibles tax on stock, which was repealed in 1995, exempted from tax that proportion of corporate stock that corresponds to the amount of business the corporation conducted in North Carolina. The Court held in Fulton that this exemption clearly discriminated against interstate commerce because the tax would fall on corporate stock only to the degree the corporation participates in commerce outside North Carolina.

The tax preferences addressed in this bill all have a similar discriminatory effect. The corporate income tax deduction for North Carolina dividends causes the income tax to fall on dividends to the degree the issuing corporation participates in commerce outside North Carolina, subject to a $15,000 cap on the deduction per taxpayer. If the corporation is a savings and loan or an insurance company, its dividends are not taxed at all if it is domiciled in North Carolina. The corporate income tax deduction for subsidiary dividends is allowed only to corporations domiciled in North Carolina. Comparable corporations domiciled in other states must pay more North Carolina taxes either because their dividends are business income allocable to and fully taxable in North Carolina or because their dividends are nonbusiness income allocable out of state by a formula that is less generous than the deduction allowed to corporations domiciled in North Carolina.

The individual income tax credit for North Carolina dividends causes the income tax to fall only on dividends of corporations that do less than half of their business in North Carolina, subject to a per taxpayer cap. The tax credits for distributing North

Carolina wine effectively exempt North Carolina wine from the excise tax levied under G.S. 105-113.80, a tax scheme that has been declared unconstitutional by the United States Supreme Court in Bacchus Imports, Ltd. v. Dias, 468 U.S. 263, 82 L.Ed.2d 200, 104 S.Ct. 3049 (1984). In addition, the tax credits are limited to those taxpayers that pay the North Carolina excise tax on wine; by definition, this group is limited to those who distribute wine in North Carolina. Thus the amount of the tax reduction is dependent upon the amount of wine distribution business the taxpayer conducts in this state.

The qualified business investment tax credits reduce a taxpayer's income, franchise, or gross premiums tax by an amount equal to 25% of the cost of purchasing stock in certain businesses with most of their operations in North Carolina (subject to various caps), while no tax reduction is allowed for purchasing similar stock in corporations most of whose operations are outside of North Carolina. This measure is designed to make investment in these North Carolina companies more attractive than investments in other companies.

The Fulton Court's second step in analyzing the constitutionality of the intangibles tax on stock was to determine whether the discrimination could be justified as compensating for a similar burden that falls solely on intrastate commerce. Three tests must be met to uphold a discriminatory tax as a valid compensating tax: (1) there must be an identifiable burden on intrastate commerce for which the discriminatory tax compensates; (2) the discriminatory tax must be roughly equal to the identified intrastate tax; and (3) the two taxes must fall on events that are sufficiently similar that they serve as mutually exclusive proxies. After a lengthy analysis, the Court held that the stock tax failed all three of these tests. With respect to the first test, the Court noted that it was not sufficient to say that a tax compensates for the fact that the corporate income tax does not fall on income from business done outside the State because North Carolina has no sovereign interest in taxing income from business outside the State.

The Court also noted that the only discriminatory taxes that have been found to satisfy the third test are use taxes that compensate for sales taxes, which cannot be imposed on sales that occur out-of-state. These compensating use taxes allow a credit for any sales taxes that are paid to another state. That is an important element, because the compensating tax tests can be satisfied only by tax schemes designed to enable in-state and out-of-state businesses to compete on an equal, tax-neutral basis.

Based on the analysis in the Fulton opinion, it does not appear that any of the tax preferences addressed in this bill would satisfy the three tests. The income tax

preferences for dividends could be said to compensate for the fact that the corporation's income was already subject to North Carolina income tax, but North Carolina does not have a valid interest in taxing income from business outside of North Carolina and, because there is no credit for income taxes paid to other states, the tax scheme does not create a tax-neutral playing field. In the case of the tax credits for distributing North Carolina wine and the qualified business investment credits, there is no evident intrastate burden for which the tax compensates. The wine distribution tax scheme clearly creates a competitive advantage for North Carolina wine over wine produced in other states and the qualified business investment tax scheme is obviously designed to make investment in certain companies operating in North Carolina more attractive than investment in other companies.

Fiscal Report
Fiscal Research Division
April 24, 1996

Proposal #1: 1996 Tax Reform Act

Fiscal Effect:

SECTION 1

(1) Repeal credit for distributing North Carolina wine.
The Tax Research Division of the Department of Revenue estimates the annual impact of this credit to be $20,000. From a review of income tax returns from 1992, 1993, and 1994, the Department found the total income tax credit deducted ranged from $12,000 to $19,000 each year.

(2) Repeal individual income tax credit for North Carolina dividends.
The Department of Revenue estimates this credit is equal to $11 million. This fiscal report assumes that dividend earnings will grow 5% a year. It is also assumed that the credit's repeal on January 1, 1996 will create a first year revenue windfall of nearly five million dollars due to two quarterly estimated payments paid by high income individuals from January to June, 1977. In effect, individuals are paying the tax for 18 months because the tax year and fiscal year are not concurrent.

SECTIONS 2-4

Repeal corporate income tax deduction for N.C. dividends.
The Department of Revenue estimates that the tax benefit to corporations from this deduction equals $2 million. This fiscal report assumes that the tax benefit would grow 2% a year if not repealed. With a January 1, 1996 effective date, corporate taxpayers will pay tax on their dividends for 18 months due to two quarterly payments in 1997. This will generate a small $900,000 windfall in FY 1996-97.

SECTION 5

Cap Qualified Business Tax Credit at $6 million.
In 1996, the qualified business investment tax credits equal $3,523,894. Only once since 1989 have the credits equaled $6 million. The cap reduces the state's potential liability from the credits, but the General Fund does not gain additional revenue from this change.

SECTION 6

Modify the subsidiary dividend deduction.
The best cost estimate available for this proposal was prepared for a similar bill by the Department of Revenue in 1992. The Department estimated the state would gain $16.9 million in revenue each year if all corporations were required to attribute expenses to deductible dividends. If the provision is effective January 1997, then the FY 1996-97 gain would be less than half the annual amount, $7.6 million, since corporations have to make only two estimated payments in that fiscal year. When the cost estimate was prepared it did not consider a 15% cap on the amount of expenses that must be netted. Fiscal Research will work with the Department of Revenue to revise this estimate before the Short Session.

SECTIONS 7 & 8

Modify Qualified Business Tax Credit
No fiscal Impact.

SECTION 9

Enact Voluntary Use Tax Collection Agreement.
A 1994 Advisory Commission on Intergovernmental Relations report estimated that North Carolina could earn $47.4 million and local governments could earn $23.7 million from collecting use taxes on mail order sales. No revenue gain is included in this fiscal report due to the uncertainty of when and if mail order companies will collect and remit the tax.

SECTIONS 10 & 11

Index personal exemptions.
To remove the personal exemption income cap, to raise the state personal exemption to the federal level and to index the personal exemption beginning in Tax Year 1997 will cost $23.3 million in FY 1996-97 and roughly $18 million more each year thereafter. Fiscal Research used 1993 tax data (latest year available) to estimate the cost to the General Fund. 1994 data should be available in time to revise this estimate for the Short Session. It will cost the Department of Revenue approximately $120,000 each year to print and mail new withholding tables to employers.

SECTIONS 12-19

Repeal privilege license taxes.
It is estimated that the state will collect approximately $35 million in revenue from privilege license taxes in Fiscal Year 1995-96. Repealing all privilege license taxes except those on amusements, circuses, installment paper dealers, loan agencies or brokers, banks, and newsprint publications will cost the General Fund $14.5 million each year. The taxes are repealed effective July 1, 1997, thus the revenue loss will not occur until FY 1997-98. This bill will not affect privilege license taxes authorized for local governments.

SECTIONS 20-28

Simplify/reduce inheritance tax.
Based on 1993 inheritance tax returns, the five year phase out of the inheritance tax, the repeal of the state gift tax, and the exemption of Qualified Terminable Interest Property from taxation will reduce General Fund revenue by $5.78 million in FY 1996-97. When the bill is fully implemented in FY 2000-01, the General Fund will lose $58.14 million in revenue.

TAX REFORM ACT OF 1996
FISCAL IMPACT OF PROPOSED CHANGES
($million)

	96-97	97-98	98-99	99-00	00-01
Repeal Credit for Distributing NC Wine	.02	.02	.02	.02	.02
Repeal Ind. Tax Credit for NC Dividends	15.95	11.55	12.13	12.73	13.37
Repeal Corp. Deduction for NC Dividends	2.9	2.04	2.08	2.12	2.16
Cap Qualified Business Credit at $6 million	-	-	-	-	-
Modify Subsidiary Dividend Deduction	7.6	16.9	16.9	16.9	16.9
Enact Voluntary Use Tax Collection	NA	NA	NA	NA	NA
Index Personal Exemption in 1997	(23.3)	(55.9)	(74.1)	(92.8)	(111.7)
Cost of forms due to change in Exemption	(.12)	(.12)	(.12)	(.12)	(.12)
Simplify/Reduce Inheritance Tax	(5.78)	(19.31)	(33.4)	(48.58)	(58.14)
Repeal Most Privilege License Taxes	-	(14.5)	(14.5)	(14.5)	(14.5)
TOTAL FISCAL IMPACT	(2.73)	(59.32)	(90.99)	(124.23)	(152.01)

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

S **D**

LEGISLATIVE PROPOSAL 2
95-LC-285(1.1)
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Bosnia Troops Tax Extension. (Public)

Sponsors: Senators Kerr, Cochrane, Cooper, Soles.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO PROVIDE A GRACE PERIOD FOR MILITARY PERSONNEL TO LIST AND PAY PROPERTY TAXES AFTER DEPLOYMENT IN CONNECTION WITH OPERATION JOINT ENDEAVOR.

The General Assembly of North Carolina enacts:

Section 1. Notwithstanding G.S. 105-360 and 105-330.4, an individual liable for property taxes for the 1995-96 tax year or a subsequent tax year who, on or after December 4, 1995, was a member of the armed forces or the armed forces reserves and was deployed outside the State in connection with performing "Operation Joint Endeavor services," is allowed 90 days after the end of the individual's deployment to pay the property taxes at par. For these individuals, the taxes do not become delinquent until after the end of the 90-day period provided in this act, and an individual who pays the property taxes before the end of the 90-day period is not liable for interest on the taxes for the applicable tax year. If the individual does not pay the taxes before the end of the 90-day period, interest shall accrue on the taxes according to the schedule provided in G.S. 105-360 or G.S. 105-330.4, as appropriate, as if no grace period had been allowed under this act. If the individual owns property jointly or by the entirety with his or her spouse, the extension provided in this section applies to both spouses.

Sec. 2. Notwithstanding G.S. 105-307, an individual required to list property for taxation for the 1996-97 tax year or a subsequent tax year who, on or after December 4, 1995, was a member of the armed forces or the armed forces reserves and was deployed outside the State as a result of performing "Operation Joint Endeavor services," is allowed 90 days after the end of the individual's deployment to list the property. For these individuals, the listing period for the applicable tax year is extended until the end of the 90-day period provided in this act, and an individual who lists the property before the end of the 90-day period is not subject to civil or criminal penalties for failure to list the property for that tax year. If the individual owns property jointly or by the entirety with his or her spouse, the extension provided in this section applies to both spouses.

Sec. 3. As used in this act, the term "Operation Joint Endeavor services" has the meaning provided in federal Pub. L. No. 104-117 (1996).

Sec. 4. This act is effective retroactively as of December 4, 1995. If any penalty or interest forgiven by this act has been paid before the date this act is ratified, the taxing unit shall refund the penalty or interest.

Explanation - Bosnia Troops Tax Extension

Legislative Proposal 2 would give military personnel deployed in the peacekeeping effort in Bosnia and Herzegovina, known as Operation Joint Endeavor, 90 days after the end of their deployment to pay their 1995-96 or later property taxes without interest and to list property for the 1996-97 tax year or a later tax year. The proposal applies to those serving in or in support of the armed forces and armed forces reserves, including the national guard. Deployment of military personnel pursuant to Operation Joint Endeavor began December 4, 1995.

Property taxes for the 1995-96 fiscal year would otherwise become delinquent if not paid by January 6, 1996, and interest would accrue at the rate of 2% for the first month and 3/4% each month thereafter. The regular listing period for property taxes for the 1996-97 year ended on January 31, 1996. Failure to list is punishable as a misdemeanor and also subjects the owner of the property to a tax penalty equal to 10% of the tax due on the property. Automobiles are taxed on a staggered, year-round schedule, so the listing date and the date the taxes become delinquent may fall at any time during the year.

Legislative Proposal 2 would become effective retroactively as of December 4, 1995. Any interest and penalties assessed before it is enacted would be refunded.

G.S. 105-249.2 and G.S. 105-158 already provide income tax extensions for military personnel serving in a combat zone and income tax forgiveness for personnel who are killed while serving in a combat zone, to the same extent as federal law (sections 7508 and 692 of the Internal Revenue Code). Our Department of Revenue will automatically follow the federal law. Congress has enacted Public Law 104-117 providing that these sections of the Code apply to personnel deployed in connection with Operation Joint Endeavor.

NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: Proposal 2
SHORT TITLE: Bosnia Troops Tax Amnesty
SPONSOR(S): Revenue Laws Study Committee

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

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

BILL SUMMARY: The proposal allows members of the armed forces or reserves who are deployed overseas as part of peace keeping operations in Bosnia to delay payment of their 1995-96 property taxes and listing of property for their 1996-97 property taxes until 90 days after their deployment has been completed.

EFFECTIVE DATE: Retroactive to December 4, 1995.

FISCAL IMPACT

	95-96	96-97	97-98	98-99	99-00
REVENUES:					
Local Governments	Loss cannot be estimated				

ASSUMPTIONS AND METHODOLOGY: The Department of Defense can not provide figures on the number of armed forces personnel based in North Carolina who will be deployed as part of operations in Bosnia. The amount of property subject to taxation in North Carolina that is owned by personnel who might be deployed is also unknown. Thus, the tax loss can not be estimated.

The effect on local governments is not expected to be significant, however. A similar provision was enacted in 1991 for personnel serving in the Gulf War. This loss did not cause a noticeable decrease in property tax revenues for the counties near military bases in North Carolina. Because real property and vehicles are listed for assessment through automated processes, the amount of property that will fail to be listed should be small. In addition, many armed forces personnel based in North Carolina do not own homes or register their vehicles in the State.

TECHNICAL NOTES: This proposal affects only the payment of local property taxes. Existing law provides an extension for the filing of State taxes for armed forces personnel who are provided extensions regarding the filing of Federal taxes.

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: Karl Knapp
APPROVED BY:
DATE: March 27, 1996

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

LEGISLATIVE PROPOSAL 3
95-LJ-33(1.2)
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Revise Failure To Pay Penalty. (Public)

Sponsors: Representatives Cansler, Blue, Capps, Church, Neely, Robinson, Shaw, and Shubert.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO PROHIBIT THE IMPOSITION OF A FAILURE TO PAY PENALTY WHEN ADDITIONAL TAX DUE IS PAID AT THE TIME AN AMENDED RETURN IS FILED OR WITHIN 30 DAYS AFTER THE ADDITIONAL TAX WAS ASSESSED.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-236(4) reads as rewritten:

"(4) Failure to Pay Tax When Due. -- In the case of failure to pay any tax when due, without intent to evade the tax, there shall be an additional tax, as a penalty, of ten percent (10%) of the tax; provided, that such penalty shall in no event be less than five dollars ($5.00). This penalty does not apply in any of the following circumstances:

a. When the amount of tax shown as due on an amended return is paid when the return is filed.

b. When a tax due but not shown on a return is assessed by the Secretary and is paid within 30 days after the date of the proposed notice of assessment of the tax."

Sec. 2. This act becomes effective January 1, 1997, and applies to taxes due on or after that date.

Explanation of Revise Failure to Pay Penalty

This proposal prohibits the imposition of a tax penalty for failure to pay in two circumstances. The first circumstance is when an additional tax is due with an amended return. The second circumstance is when a tax assessed by the Secretary of Revenue is paid within 30 days after it was assessed. The changes become effective for taxes due on or after January 1, 1997.

The failure to pay penalty is 10% of the amount due, with a minimum penalty of $5.00. The Secretary of Revenue has the authority under G.S. 105-237 to waive the penalty. The decision of whether or not to waive a penalty is made on a case by case basis.

Currently, G.S. 105-236(4) requires the failure to pay penalty to be assessed whenever a tax is not paid when it was due. The due date for additional tax owed on an amended return is considered to be the date the original return was due. Consequently, any time a taxpayer files an amended return and pays additional tax with the return, the taxpayer is assessed the failure to pay penalty. Similarly, the due date for a tax assessed by the Secretary is considered to be the date the tax should have been paid without resort to an assessment. Consequently, any time a taxpayer is assessed for unpaid taxes, the taxpayer is also assessed the failure to pay penalty.

The Revenue Laws Study Committee received numerous letters on this topic. The Committee compared the circumstances in which a federal failure to pay penalty is assessed with the circumstances in which a State failure to pay penalty is assessed. The Committee found that the federal failure to pay penalty is not assessed when additional tax shown on an amended return is paid when the return is filed nor when a tax assessed by the Internal Revenue Service is paid within 10 days after the date on the notice of assessment and demand for payment. The penalty is not assessed under either federal or State law if a return is filed after an extension has been granted and the amount of tax paid when the extension was granted is at least 90% of the amount shown on the return.

The Committee concluded that applying a failure to pay penalty to additional tax that is shown due on an amended return and is paid with the return discourages the filing of an amended return and does not allow for reporting errors on tax reporting statements such as 1099s issued by banks and brokerage houses and W-2s issued by employers that result in the need for an amended return. The Committee further

concluded that allowing a grace period after a tax is assessed before applying a failure to pay penalty would encourage prompt payment of the assessed taxes. Finally, the Committee concluded that applying a State failure to pay penalty in the circumstances described when no federal penalty applies is unnecessarily confusing and makes the State law on this topic harsher than the federal.

The Committee therefore recommends eliminating the application of a failure to pay penalty in the circumstances described. The changes make the State law on this topic the same as the federal, except for the penalty amount and except that the proposal allows 30 days to pay a tax after an assessment and the federal law allows only 10.

Fiscal Report
Fiscal Research Division
April 24, 1996

Proposal #3: Revise Failure to Pay Penalty

Summary:

See previous explanation.

Effective Date:

Effective January 1, 1997 and applies to taxes due on or after that date.

Fiscal Effect:

The Department of Revenue estimates the revenue impact of this bill to be minimal. The bill returns the Department to the policy it followed until 1994. Since 1994, many of the penalties have been waived when taxpayers sent in a written request for a waiver. The exact number of penalties paid in 1995 is not available from the computer database.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

LEGISLATIVE PROPOSAL 4
95-LCX-303(1.1)
(THIS IS A DRAFT AND NOT READY FOR INTRODUCTION)

Short Title: Update Code Reference. (Public)

Sponsors: Representatives Shubert, Blue, Cansler, Capps, Church, Neely, Robinson, and Shaw.

Referred to:

A BILL TO BE ENTITLED

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

The General Assembly of North Carolina enacts:

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

"(1a) Code. -- The Internal Revenue Code as enacted as of ~~January 1, 1995,~~ March 20, 1996, including any provisions enacted as of that date which become effective either before or after that date."

Sec. 2. This act is effective upon ratification.

Explanation - Update Code Reference

Legislative Proposal 4 would rewrite the definition of the Internal Revenue Code used in State tax statutes to change the reference date from January 1, 1995, to March 20, 1996. 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 a significant 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. It also has a significant effect on motor fuel taxes because the definitions of gasoline and diesel are tied to federal law and the time these fuels become taxable is tied to federal law. The franchise tax, gift tax, highway use tax, inheritance tax, and insurance company premiums tax determine some exemptions based on the provisions of the Code.

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

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

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

Each year, in deciding whether the Internal Revenue Code reference should be updated, the Revenue Laws Study Committee considers the changes that have been made to the Code in the past year. The Revenue Laws Study Committee was informed by the Department of Revenue that, during 1995, Congress made only three changes affecting income tax and no changes affecting the other State taxes that make reference to the Code. A memorandum from the Department of Revenue states:

> The only legislation enacted by Congress since January 1, 1995, that affected the Internal Revenue Code was Public Law 104-7 (H.R. 831). The Self-Employed Health Insurance Act reinstated and made permanent the deduction for health insurance premiums paid by self-employed individuals. This includes premiums paid on behalf of the self-employed individual, a spouse, and dependents. The deduction is twenty-five percent of the qualifying premiums for tax years beginning after December 31, 1993, and increases to thirty percent for tax years beginning after December 31, 1994.
>
> The act also made C corporations and certain partnerships ineligible to defer gain on an involuntary conversion under Code section 1033 when replacement property is purchased from a related person effective for acquisitions after February 5, 1995. Code section 1071, which allowed a taxpayer to treat the sale of a broadcast property as an involuntary conversion if the sale is certified by the FCC as necessary to effectuate an FCC ownership and control policy, was repealed effective for sales or exchanges after January 16, 1995.

In addition, the Committee was informed of federal legislation enacted on March 20, 1996, to increase the amount of exempt military pay for certain commissioned officers serving in the peacekeeping efforts in the former Republic of Yugoslavia and to exclude exempt military pay from withholding requirements. Although our income tax law automatically adopts most income tax benefits extended to active duty military personnel by Congress, these changes were made as an amendment to the Internal Revenue Code and can, therefore, by adopted only by setting our Code reference date at March 20, 1996.

Other legislation is pending in Congress that proposed major tax changes to become effective for the 1995 tax year. The legislation is tied up in the federal budget stalemate; if enacted, it is unlikely that, at such a late date, significant changes would be made retroactive to the 1995 tax year. In any case, Legislative Proposal 4 would not automatically adopt those federal changes; it adopts only the federal changes that have already been enacted as of March 20, 1996.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: Proposal 4
SHORT TITLE: Update Code Reference
SPONSOR(S): 1996 Revenue Laws Study Committee

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

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

BILL SUMMARY: Section 1 rewrites the definition of the Internal Revenue Code used in State tax statutes to change the reference date from January 1, 1995, to March 20, 1996. An update to the Internal Revenue code is brought to the legislature annually as both a policy decision and a response to a legal restraint. The policy reason for specifying a particular date is that, in light of continuous changes made to the federal tax law, the State may not want to automatically adopt federal changes, particularly when they result in large revenue losses. The legal restraint involves Article V, Section 2(1) of the North Carolina State Constitution which states in pertinent part that the "power of taxation … shall never be surrendered, suspended, or contracted away". A 1977, memorandum from the State Attorney General's Office to the Tax Research Division of the Department of Revenue concluded that a "statute which adopts by reference future amendments to the Internal Revenue Code would… be invalidated as an unconstitutional delegation of legislative power".

Legislation enacted by Congress since January 1, 1995, that affects the Internal Revenue Code is as follows:

Public Law 104-7, the Self-Employed Health Insurance Act reinstated and made permanent the deduction for health insurance premiums paid by self-employed individuals. This includes premiums paid on behalf of the self-employed individual, a spouse, and dependents. The deduction is twenty-five percent of the qualified premiums for tax years beginning after December 31, 1993, and increases to thirty percent for tax years beginning after December 31, 1994.

The act also made C corporations and certain partnerships ineligible to defer gain on a involuntary conversion under the Code section 1033 when replacement property is purchased from a related person effective for acquisitions after February 5, 1995.

Code section 1071, which allowed a taxpayer to treat the sale of a broadcast property as an involuntary conversion if the sale is certified by the FCC as necessary to effectuate an FCC ownership and control policy, was repealed effective for sales or exchanges after January 16, 1995.

Public Law 104-117, gives members of the Armed Forces serving in combat zones the same tax benefits as those serving peace keeping missions in the former Republic of Yugoslavia. The law identifies Bosnia, Herzegovina, Croatia, and Macedonia as qualified hazardous duty areas to be treated as combat zones.

Sections 112 and 3401 of the Code were amended to increase the amount of exempt military pay for certain commissioned officers to an amount equal to the highest rate of basic pay of any enlisted member plus any special pay and by excluding the exempt pay from withholding requirements.

EFFECTIVE DATE: Upon Ratification

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED:
Department of Revenue, Corporate Income Tax Division
Department of Revenue, Individual Income Tax Division

FISCAL IMPACT

	FY 96-97	FY 97-98	FY 98-99	FY 99-00	FY 00-01
REVENUES:					
GENERAL FUND	Insignificant revenue (loss)				

ASSUMPTIONS AND METHODOLOGY:
Unsuccessful attempts have been made to determine the number of service personnel from North Carolina that are serving in combat zones; without knowledge of this number it is impossible to create assumptions.

The loss, due to the deductions for health insurance premiums paid by self-employed individuals, is a continuation of 1994 policy.

SOURCES OF DATA: Department of Revenue

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: H. Warren Plonk
APPROVED BY:
DATE: April 22, 1996
[FRD#001]

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H **D**

LEGISLATIVE PROPOSAL 5
96-RLRB-9(4.23)
THIS IS A DRAFT 26-APR-96 10:48:59

Short Title: Increase Pay of Property Tax Comm. (Public)

Sponsors: Representatives Capps, Blue, Cansler, Church, Neely, Robinson, Shaw, and Shubert.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO INCREASE THE COMPENSATION OF THE MEMBERS OF THE PROPERTY TAX COMMISSION AND TO PROVIDE FOR REGIONAL HEARINGS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-288(a) reads as rewritten:

"(a) Creation and Membership. -- The Property Tax Commission is created. It consists of five members, three of whom are appointed by the Governor and two of whom are appointed by the General Assembly. Of the two appointments by the General Assembly, one shall be made upon the recommendation of the Speaker of the House of Representatives and the other shall be made upon the recommendation of the President Pro Tempore of the Senate. The terms of the members appointed by the Governor and of the member appointed upon the recommendation of the President Pro Tempore of the Senate are for four years. Of the members appointed for four-year terms, two expire on June 30 of each odd-numbered year. The term of the member appointed upon the recommendation of the Speaker of the House of Representatives is for two years and it expires on June 30 of each odd-numbered year. The General Assembly shall make its appointments in accordance with G.S. 120-121 and shall fill a vacancy in accordance with G.S. 120-122. A vacancy occurs on the Commission

when a member resigns, is removed, or dies. The person appointed to fill a vacancy shall serve for the balance of the unexpired term. The Governor may remove any member for misfeasance, malfeasance, or nonfeasance.

The Commission shall have a chair and a vice-chair. The Governor shall designate one of the Commission members as the chair, to serve at the pleasure of the Governor. The members of the Commission shall elect a vice-chair from among its membership. The vice-chair serves until the member's regularly appointed term expires.

The standards of judicial conduct applicable to administrative law judges apply to members of the Property Tax Commission."

Sec. 2. 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~~ G.S. 138-5. The chair of the Commission shall receive a salary of six hundred twenty-five dollars ($625.00) a day when hearing cases and when addressing administrative matters of the Commission, plus an additional six hundred twenty-five dollars ($625.00) for each three days of hearings. The chair of the Commission may use up to two days a month to attend to administrative matters of the Commission. The other members of the Commission shall receive a salary of ~~two hundred dollars ($200.00)~~ five hundred dollars ($500.00) a day when hearing ~~cases.~~ cases, plus an additional five hundred dollars ($500.00) for each three days of hearings. 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 as provided in G.S. 105-501."

Sec. 3. G.S. 105-290(b) reads as rewritten:

"(b) Appeals from Appraisal and Listing Decisions. -- The Property Tax Commission shall hear and decide appeals from decisions concerning the listing, appraisal, or assessment of property made by county boards of equalization and review and boards of county commissioners. Any property owner of the county may except to an order of the county board of equalization and review or the board of county commissioners concerning the listing, appraisal, or assessment of property and appeal the order to the Property Tax Commission.

(1) In these cases, taxpayers and persons having ownership interests in the property subject to taxation may file separate appeals or joint appeals at the election of one or more of the taxpayers.

It is the intent of this provision that all owners of a single item of personal property or tract or parcel of real property be allowed to join in one appeal and also that any taxpayer be allowed to include in one appeal all objections timely presented regardless of the fact that the listing or valuation of more than one item of personal property or tract or parcel of real property is the subject of the appeal.

(2) When an appeal is filed, the Property Tax Commission shall provide a hearing ~~before representatives of the Commission or the full Commission~~ as specified in this subdivision.

a. ~~Hearing by Commission Representatives.~~ Values Less Than $500,000. -- In cases in which the county's assessed value of the property is less than five hundred thousand dollars ($500,000), the ~~The~~ chair of the Commission ~~may~~ shall authorize one ~~or more members~~ member of the Commission ~~or employees of the Department of Revenue~~ to hear ~~an appeal, to make examinations and investigations, to have made from stenographic notes a full and complete record of the evidence offered at the hearing, and to make recommended findings of fact and conclusions of law.~~ the appeal. Prior to the hearing, the taxpayer who has filed the appeal may request that the appeal be heard by the full Commission. If the Commission agrees with the taxpayer's request, then the appeal will be heard by the full Commission. An order entered by or any other action taken by a single commissioner under this sub-subdivision is the same as an order entered by or an action taken by the full Commission and the order or action is binding on the full Commission. ~~Should the Commission elect to follow this procedure, it shall fix the time and place at which its representatives will hear the appeal and, at least 10 days before the hearing, give written notice of the hearing to the appellant and to the clerk of the board of commissioners of the county from which the appeal is taken. At the~~

~~hearing the Commission's representatives shall hear all evidence and affidavits offered by the appellant and appellee county and may exercise the authority granted by subsection (d), below, to obtain information pertinent to decision of the appeal. The representatives conducting the hearing shall submit to the Commission and to the appellant and appellee their recommended findings of fact and conclusions of law. Upon the request of any party, the representatives conducting the hearing shall also submit to the Commission and to the appellant and appellee a full record of the proceeding. The cost of providing the full record of the proceeding shall be borne by the party requesting it, unless the Commission determines for good cause that the cost should be borne by the Commission. The Commission shall review the record, the recommended findings of fact and conclusions of law, and any written arguments that may be submitted to the Commission by the appellant or appellee within 15 days following the date on which the findings and conclusions were submitted to the parties and shall take one of the following actions:~~

~~1. Accept the recommended findings of fact and conclusions of law and issue an appropriate order as provided in subdivision (b)(3), below.~~

~~2. Make new findings of fact or conclusions of law based upon the materials submitted by the Commission's representatives and issue an appropriate order as provided in subdivision (b)(3), below.~~

~~3. Rehear the appeal under the procedure provided in subdivision (b)(2)b, below, with respect to any portion of the record or recommended findings of fact or conclusions of law.~~

b. ~~Hearing by Full Commission.~~ Values of $500,000 or More. -- ~~Should the Commission elect not to employ the procedure provided in subdivision (b)(2)a, above, it~~ In cases in which the

county's assessed value of the property is five hundred thousand dollars ($500,000) or more, the full Commission must hear the appeal unless the county, the taxpayer, and the chair of the Commission all agree that one member of the Commission shall hear the appeal.

c. Procedures. -- The chair of the Commission shall fix a time and place at which the ~~commission~~ Commission shall hear the appeal and, at least 10 days before the hearing, give written notice of the hearing to the appellant and to the clerk of the board of commissioners of the county from which the appeal is taken. At the hearing the Commission shall hear all evidence and affidavits offered by the appellant and appellee county and may exercise the authority granted by subsection (d), below, to obtain information pertinent to decision of the appeal. The Commission shall make findings of fact and conclusions of law and issue an appropriate order as provided in subdivision (b)(3), below.

(3) On the basis of the findings of fact and conclusions of law made after any hearing provided for by this subsection (b), the Property Tax Commission shall enter an order ~~(incorporating the findings and conclusions)~~ reducing, increasing, or confirming the valuation or valuations appealed or listing or removing from the tax lists the property whose listing has been appealed. The order must incorporate the findings of fact and the conclusions of law. A certified copy of the order shall be delivered to the appellant and to the clerk of the board of commissioners of the county from which the appeal was taken, and the abstracts and tax records of the county shall be corrected to reflect the Commission's order."

Sec. 4. Under the authority of G.S. 105-290(b)(2), the Property Tax Commission is strongly encouraged to authorize single member panels of the Commission to travel to the three major geographic regions of the State to hear appeals. The Commission will report to the Legislative Research Commission's Study Committee on Revenue Laws, if it is authorized, or to another study committee authorized to study tax matters if the

Revenue Laws Study Committee is not authorized, on whether the small panel hearings conducted throughout the State have made the appeals process more accessible to the public. The Commission must report its findings on or before October 1, 1997. The report should include the number of cases filed with the Commission, the number of cases resolved without a hearing before the Commission, the number of cases resolved by a hearing before the Commission, the number of cases heard by a single commissioner, the number of hearing days conducted by a single commissioner and the location of those hearings, the citizen response to the regional location of the hearings, the expenditures of the Commission for the 1996-97 fiscal year, and any other information requested by the tax study committee.

Sec. 5. There is appropriated from the General Fund to the Department of Revenue the sum of one hundred twenty-one thousand six hundred eighty dollars ($121,680) for the 1996-97 fiscal year to fund the increase in the per diem pay for the commissioners of the North Carolina Property Tax Commission.

Sec. 6. This act becomes effective July 1, 1996.

Explanation - Increase Pay of Property Tax Commission

Legislative Proposal 5 increases the salary of the five members of the Property Tax Commission and provides for regional Commission hearings. The Committee believes the changes proposed in the bill are necessary to maintain a high level of competence on the Commission and to improve its efficiency and accessibility. The bill would become effective July 1, 1996.

The Property Tax Commission is a quasi-judicial commission that constitutes the State Board of Equalization and Review for the valuation and taxation of property in the State. It hears appeals from the County Boards of Equalization and Review concerning the listing, appraisal, and assessment of property. Appeals of its decisions lie directly with the North Carolina Court of Appeals. The Commission is composed of five members appointed by the Governor and the General Assembly. The Commission meets an average of 40 days a year to hear appeals.

The Revenue Laws Study Committee heard testimony from the Chair of the Commission, Dan Murray, concerning the increasingly complex workload of the Commission. The Chairs of the Committee created a Subcommittee to study the organization of the Property Tax Commission. The Subcommittee, chaired by Representative Capps, met three times. The Subcommittee talked at some length with four of the five members of the current Commission, as well as representatives of the Department of Revenue, Bill Campbell with the Institute of Government, and local tax officials.

The Subcommittee discussed the need for a full-time Commission as well as the idea of incorporating the Commission's duties into the duties of the Administrative Office of the Courts. The Subcommittee believed that these ideas would have a difficult time in the short session. Therefore, the Committee, based upon a Subcommittee proposal, recommends the following changes to the Property Tax Commission and the property tax appeal process:

1. Increase the pay of the Chair of the Commission from $200 a day to $625 a day.
2. Increase the pay of the remaining Commission members from $200 a day to $500 a day.

3. Give all members one day for every three days of hearings for case preparation. The members would be compensated for that day at the rate of pay stated above.
4. Give the Chair of the Commission up to two days a month to attend to administrative matters of the Commission.
5. Direct appeals of values of less than a set amount ($500,000) to be heard by a single commissioner. The case could be heard by the full Commission upon the motion of a party and the concurrence of the Commission. Appeals of values above that amount would be heard by the full Commission, unless all the parties agree otherwise. A decision after a hearing is final and may be appealed to the Court of Appeals.

The proposal also provides that the standards of judicial conduct applicable to administrative law judges apply to members of the Commission. Under current law, the Governor may remove a member for misfeasance, malfeasance, or nonfeasance. Under 26 NCAC 3.0101, Canons 1, 2, and 3 of the Code of Judicial Conduct apply in contested cases in the Office of Administrative Hearings. Canon 1 provides that a judge should uphold the integrity and independence of the judiciary; Canon 2 provides that a judge should avoid impropriety and the appearance of impropriety in all of the judge's activities; and Canon 3 provides that a judge should perform the duties of the office impartially and diligently.

Section 5 of the bill is an appropriation provision that will provide the necessary funds to implement the proposal. It provides that $121,680 will be appropriated from the General Fund to the Department of Revenue for the 1996-97 fiscal year to carry out the provisions of this bill.

Section 6 provides that the bill will become effective July 1, 1996.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: Proposal 5
SHORT TITLE: Increase Pay of Property Tax Commission
SPONSOR(S): 1996 Revenue Laws Study Committee

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

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

BILL SUMMARY The proposed act provides for an increase in the per diem pay for Commissioners of the North Carolina Property Tax Commission. There are five part-time Commissioners one of whom serves as the Chair. The current per diem is $200.00 per hearing day for each Commissioner.

Under this proposal, the Chair's per diem is increased to $625.00 per hearing day. In addition, the Chair is to receive two days per month at $625.00 a day for administrative matters and one day at $625.00 for every three days of hearings for case preparation. The per diem of the four part-time Commissioners is increased to $500.00 per hearing day plus $500.00 a day for every three days of hearings for case preparation.

Appeals of value less than $500,000 may be heard by a single Commissioner. Such cases could be heard by the full Commission upon the motion of a party and the concurrence of the Commission or upon the Commission's own decision. Appeals of value greater than $500,000 would be heard by three Commissioners, unless all parties agreed otherwise. A decision after a hearing is final and may be appealed to the Court of Appeals.

EFFECTIVE DATE: July 1, 1996

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED:
Ad Valorem Tax Division of the Department of Revenue

	$ ESTIMATE FISCAL IMPACT	
	FY 96-97	FY 97-98
APPROPRIATION:		
GENERAL FUND	$ 121,680	$121,680

ASSUMPTIONS AND METHODOLOGY: The estimate assumes a maximum of 42 hearing days in each fiscal year of the 1996-98 Biennium.

Equations:

Four Part-time Commissioners
$300.00 * 42 * 4 = $50,400
$500.00 * (42/3) * 4 = 28,000
Total $78,400

Per diem per Commissioner $19,600

One Chair Person
$465.00 * 42 * 1 = $19,530
$625.00 * (12*2) * 1 = 15,000
$635.00 * (42/3) * 1 = 8,750
Total $43,280

Per diem Chair $43,280

$78,400 + $43,280 = $121,680 increase per year of the Biennium

SOURCES OF DATA:
Department of Revenue, Property Tax Division
Fiscal Research Division

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: H. Warren Plonk
APPROVED BY:
DATE: April 15, 1996
[FRD#001]

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H **D**

LEGISLATIVE PROPOSAL 6
95-LCX-300(2.21)
(THIS IS A DRAFT AND NOT READY FOR INTRODUCTION)

Short Title: Manufactured Home Property Tax. (Public)

Sponsors: Representatives Shaw, Blue, Cansler, Capps, Church, Neely, Robinson, Shaw, and Shubert.

Referred to:

A BILL TO BE ENTITLED

AN TO ACT TO PROVIDE A PROCEDURE FOR LIENHOLDERS ON MANUFACTURED HOMES TO REGISTER FOR NOTIFICATION OF DELINQUENT PROPERTY TAXES ON THE HOMES AND, ONCE REGISTERED, TO BE ABLE TO REPOSSESS A HOME BY PAYING NO MORE THAN TWO YEARS' PROPERTY TAXES.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-316.4 reads as rewritten:

"§ 105-316.4. ~~Issuance of permits under repossession.~~ Special rules for lienholders repossessing mobile homes.

(a) Requirements for Obtaining Permit. -- A person who intends to take possession of a mobile home as the holder of a lien on the home shall notify the tax collector of the location to which the home is to be taken. The tax collector shall then give the lienholder a statement of taxes due only on the mobile home. If the lienholder has not filed a timely continuing request for notice of delinquent taxes as set out in subsection (b) of this section, the lienholder must pay all unpaid taxes on the mobile home before obtaining a permit and repossessing the home. If the lienholder has filed a timely continuing request for notice of delinquent taxes as set out in subsection (b) of this section, the lienholder may obtain a permit by paying the applicable amount provided in subsection (c) by the deadline provided in

subsection (d). The tax collector shall issue a permit to a lienholder who complies with the requirements of this section.

(b) Continuing Request for Notice of Delinquent Taxes. -- A lienholder may, at any time at least three months before repossessing a mobile home, file with the tax collector a continuing request to be notified of taxes on the mobile home that become delinquent. The request must be in writing and must include all of the following information:

(1) The name and mailing address of the lienholder.

(2) The name and mailing address of the owner of the mobile home.

(3) The address where the mobile home is located.

(4) The serial number, year, make, model, and dimensions of the mobile home.

After a lienholder has filed a request, the tax collector may notify the lienholder of taxes on the mobile home that are or become delinquent. In addition, when the lienholder requests a permit, the tax collector shall give the lienholder a statement of taxes due on the mobile home as provided in subsection (a).

(c) Amount of Taxes Payable by Lienholder. -- To obtain a permit, a lienholder who has filed a timely request under subsection (b) of this section must pay the current year's property taxes on the mobile home. In addition, if there were any delinquent taxes on the mobile home at the time the request was filed or if the tax collector has notified the lienholder of any delinquent taxes on the mobile home within six months after they became delinquent, the lienholder must pay the delinquent taxes for the year preceding the current tax year.

(d) When Taxes Payable. -- A resident lienholder who has filed a timely request under subsection (b) of this section must pay the taxes due under subsection (c) within seven days after the permit is issued. A nonresident lienholder who has filed a timely request under subsection (b) of this section must pay the taxes due under subsection (c) before the permit is issued. A lienholder who has not filed a timely request under subsection (b) of this section must pay all taxes due on the mobile home as provided in subsection (a) before the permit is issued.

(e) Effect of Payment of Taxes. -- After a lienholder has paid the amount of taxes required by this section, the mobile home is no longer subject to levy or attachment of any lien for any other taxes then owed by the owner of the mobile home, whether or not previously determined.

~~Notwithstanding the provisions of G.S. 105-316.2(a) and 105-316.3(a), above, any person who intends to take possession of~~

~~a mobile home, whether by judicial or nonjudicial authority, as a holder of a lien on said mobile home shall apply for, and be issued, the permit herein provided without paying all taxes due to be paid by the owner of the mobile home being repossessed, upon notifying the tax collector of the location in North Carolina to which the mobile home is to be taken. At the time of notification the tax collector shall render to the holder of the lien a statement of taxes due against only the mobile home. Within seven days of the issuance of the permit the applicant shall pay to the tax collector the taxes due as set forth in the statement.~~

~~Notwithstanding the foregoing, any applicant who is a nonresident of North Carolina must pay the taxes due as set forth above at the time of notification to the tax collector and application for the permit.~~

~~Upon issuance of the permit and the payment of any taxes as prescribed herein, the mobile home shall no longer be subject to levy or attachment of any lien for any other taxes then owed by the owner thereof, whether or not previously determined.~~"

Sec. 2. G.S. 105-355 reads as rewritten:

"**§ 105-355. Creation of tax lien; date as of which lien attaches.**

(a) Lien on Real Property. -- Regardless of the time at which liability for a tax for a given fiscal year may arise or the exact amount thereof be determined, the lien for taxes levied on a parcel of real property shall attach to the parcel taxed on the date as of which property is to be listed under G.S. 105-285, and the lien for taxes levied on personal property shall attach to all real property of the taxpayer in the taxing unit on the same date. All penalties, interest, and costs allowed by law shall be added to the amount of the lien and shall be regarded as attaching at the same time as the lien for the principal amount of the taxes. For purposes of this ~~subsection (a):~~ subsection:

(1) Taxes levied on real property listed in the name of a life tenant under G.S. 105-302(c)(8) shall be a lien on the fee as well as the life estate.

(2) Taxes levied on improvements on or separate rights in real property owned by one other than the owner of the land, whether or not listed separately from the land under G.S. 105-302(c)(11), shall be a lien on both the improvements or rights and on the land.

(b) Lien on Personal Property. -- Taxes levied on real and personal property (including penalties, interest, and costs allowed by law) shall be a lien on personal property from and

after levy or attachment and garnishment of the personal property levied upon or attached.

(c) Mobile Homes. -- The lien of taxes on a mobile home on which a security interest exists of record shall be enforceable against the holder of the security interest only for taxes that the holder of the security interest would be required to pay in order to repossess the mobile home under G.S. 105-316.4. If the holder of a security interest of record on a mobile home has paid all taxes required under G.S. 105-316.4 in order to repossess the mobile home, the mobile home is no longer subject to levy or attachment of any lien for any other taxes owed at the time of payment by the owner of the mobile home."

Sec. 3. G.S. 105-366(b)(6) reads as rewritten:

"(6) Personal property of the taxpayer that has been repossessed by one having a security interest therein so long as the property remains in the hands of the person who has repossessed it or the person to whom it has been transferred other than by bona fide sale for value. However, a levy on a mobile home in the hands of a repossessor, or a person to whom the repossessor transferred it other than by bona fide sale for value, may be made only for taxes that the repossessor was required to pay in order to repossess the mobile home under G.S. 105-316.4."

Sec. 4. This act becomes effective July 1, 1996.

Explanation - Manufactured Home Property Tax

Legislative Proposal 6 would provide an improved procedure for lienholders of manufactured homes to repossess the homes by paying property taxes that may be due on the homes. The proposal would become effective July 1, 1996.

Under current law, a manufactured home cannot be moved unless the person moving the home obtains a tax permit from the tax collector by paying all property taxes owed by the owner of the manufactured home, or by proving that no taxes are due or that moving the home will not jeopardize payment of the taxes. These requirements protect the taxing unit, because the manufactured home is the unit's security for payment of property taxes owed by the home's owner. Taxes owed by a property owner become a lien against the owner's real property as of the listing date. Under current law, a lienholder may repossess a manufactured home to a location in North Carolina by paying, within seven days after moving the home, the taxes due on the home only.

Legislative Proposal 6 would create a procedure that would help taxing units better collect taxes on manufactured homes and also reduce the amount of taxes that lienholders must pay in order to repossess a home. Under this procedure, a lienholder may file with the tax collector a continuing request for notice of delinquent taxes. This request must be filed at least three months before the lienholder seeks to repossess the home. The request will contain information that will help the taxing unit monitor taxation of the manufactured home: the name and address of the home's owner, the address where the home is located, and the serial number, year, make, model, and dimensions of the home. The tax collector who receives such a request may notify the lienholder of taxes that are or have become delinquent on the home. When the lienholder applies for a permit to repossess the home, the tax collector must provide a statement of all taxes due on the home. The lienholder may repossess the home by paying the current year's taxes. In addition, the lienholder must pay the previous year's delinquent taxes if either of the following is true: (i) there were already delinquent taxes on the home at the time the lienholder filed the request for notice or (ii) within six months after any taxes subsequently became delinquent on the mobile home, the tax collector notified the lienholder of the delinquent taxes. If the lienholder is a resident of North Carolina, the taxes do not have to be paid until seven days after

the home is repossessed. For nonresident lienholders, the taxes must be paid before the home is repossessed. If a lienholder has not chosen to file a continuing request for notice of delinquent taxes with respect to a manufactured home, the lienholder must pay all taxes due on the home before repossessing it.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: Proposal 6
SHORT TITLE: Manufactured Home Property Tax
SPONSOR(S): 1996 Revenue Laws Study Commission

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

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

BILL SUMMARY:
The proposed act allows lien-holders to register with the property tax administrator of a local unit of government for notification of delinquent taxes on manufactured homes located in a county.

Before a lien-holder can repossess a mobile home, a permit must be secured from the local property tax administrator. Under current law, a permit is obtained by the lien-holder from the property tax administrator once all delinquent property taxes are paid.

Under the proposed act:

(1) If a "Continuing Request for Notice of Delinquent Taxes" was **not** filed with the county tax administrator at least three months before the property is to be repossessed, then the lien-holder must pay all delinquent taxes owed on the property before a permit to repossess will be granted.

(2) If a lien-holder does file a "Continuing Request for Notice of Delinquent Taxes", three months before the property is to be repossessed, then the lien-holder must pay the current year's property tax to obtain a permit to repossess. In addition, the previous year's delinquent taxes must be paid if there were any delinquent taxes owed at the time the lien-holder filed for notice or if the tax collector notified the lien-holder within six months after any taxes became delinquent.

EFFECTIVE DATE: July 1, 1996

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED:
Units of local government that levy a property tax

$ ESTIMATE
FISCAL IMPACT

	FY 96-97	FY 97-98	FY 98-99	FY 99-00	FY 00-01
REVENUES					
LOCAL		Indeterminate			

ASSUMPTIONS AND METHODOLOGY: Local units of government do not know the amount of delinquent taxes owed on mobile homes in a county. Often the administrator discovers such property exists when the lien-holder files for a permit to repossess the home.

SOURCES OF DATA:
Department of Revenue, Property Tax Division

TECHNICAL CONSIDERATIONS:

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: H. Warren Plonk
DATE: April 23, 1996

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

LEGISLATIVE PROPOSAL 7
95-LCX-284(1.1)
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Clarify Free Item Sales Tax. (Public)

Sponsors: Representatives Shubert, Blue, Cansler, Capps, Church, Neely, Robinson, and Shaw.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO CLARIFY THE SALES TAX TREATMENT OF ITEMS GIVEN AWAY BY MERCHANTS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-164.3(15) reads as rewritten:

"(15) 'Sale' or 'selling' ~~shall mean any~~ means the transfer of title or ~~possession, or both, exchange, barter, lease, license to use or consume, or rental~~ possession of tangible personal property, conditional or otherwise, in any manner or by any means whatsoever, ~~however effected and by whatever name called,~~ for a consideration paid or to be ~~paid, and~~ paid.

The term includes the fabrication of tangible personal property for consumers by persons engaged in business who furnish either directly or indirectly the materials used in the fabrication ~~work, and~~ work. The term also includes the ~~furnishing, preparing, or serving~~ furnishing or preparing for a consideration of any tangible personal property consumed on the premises of the person ~~furnishing, preparing, or serving such~~

~~tangible personal~~ furnishing or preparing the property or consumed at the place at which ~~such~~ the property is ~~prepared, served or sold.~~ furnished or prepared. ~~A transaction whereby~~ The term also includes a transaction in which the possession of the property is transferred but the seller retains title or security for the payment of the ~~price shall be deemed a sale.~~ consideration.

If a retailer engaged in the business of selling prepared food and drink for immediate or on-premises consumption also gives prepared food or drink to its patrons or employees free of charge, for the purposes of this Article the property given away is considered sold along with the property sold. In all other cases, property given away or used by any retailer or wholesale merchant is not considered sold, whether or not the retailer or wholesale merchant recovers its cost of the property from sales of other property."

Sec. 2. This act becomes effective July 1, 1996.

Explanation - Clarify Free Item Use Tax

Legislative Proposal 7 would clarify the sales tax treatment of items given away by merchants. The general rule in this State and in virtually all states is that a wholesale merchant or retailer who gives away products free of charge instead of selling them is liable for the sales and use tax. The use tax, first enacted in 1939, is the complement of the sales tax and applies to the storage, use, or consumption in this State of tangible personal property. A merchant is liable for the use tax on property it uses in its business, whether furniture, equipment, decor, or promotional giveaways. Items sold by a merchant, however, are not subject to use tax because sales tax will apply when the items are sold at retail.

A wholesale merchant or retailer might not pay sales or use taxes when purchasing 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, however, 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 merchant chooses to do with the products.

There are some gray areas in determining whether a product is sold or is given away. For example, if a merchant has a "buy one, get one free" sale, both items are considered sold for the price of the first one. Although the second item appears to be given away, in fact both items are being sold at a discounted price. Another example is paper napkins, catsup, and other items that accompany and are consumed along with meals. These items are considered sold as part of the meal.

Until 1993, the following items were considered used, not sold, and thus subject to use tax: meals provided free to the merchant's employees, food given away to the merchant's patrons, and matches given away to patrons, other than matches given along with the sale of cigarettes. A group of restaurants appealed the assessment of this tax, claiming that in their case these items should be considered sold. The restaurants were

selling meals to patrons and, at the same time, providing some of the food to employees and some to patrons as "bar food" such as chips. In addition, free books of matches were provided to patrons for use in the restaurant.

The North Carolina Court of Appeals agreed with the restaurants that these items should be considered sold along with the food the restaurant sold as part of its business. In its opinion, however, the court gave an overly broad rationale: that the cost of these items was recovered by the sale of other items. This rationale is overly broad because the cost of all of a merchant's purchases are covered by the price of sold items; a merchant's profits from its sales generate the funds to purchase furniture, equipment, decorations, etc. Thus, taken literally, the court ruling could be interpreted to eliminate the use tax altogether for merchants.

Legislative Proposal 7 clarifies that property given away or otherwise used by a merchant is not exempt from use tax, except in the case of restaurants and caterers that provide free meals to employees or free bar food to patrons. As under former law, free books of matches would not be subject to use tax if they are given away along with the sale of cigarettes. Matches given away where cigarettes are not sold would remain subject to use tax. The proposal would become effective July 1, 1996.

NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: Proposal 7
SHORT TITLE: Free Food Use Tax
SPONSOR(S): 1996 Revenue Laws Study Committee

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

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

BILL SUMMARY: The proposed act clarifies that property given away or used by the merchant is not exempt from use tax, except in the case of restaurants and caterers that provide free meals to employees or free bar food to patrons.

EFFECTIVE DATE: July 1, 1996

PRINCIPAL DEPARTMENT(S)/PROGRAM(S) AFFECTED:
Sale and Use tax Division, Department of Revenue
Sales tax collections for city and county governments

Estimate
FISCAL IMPACT

	FY 96-97	FY 97-98	FY 98-99	FY 99-00	FY 00-01
REVENUES:					
GENERAL FUND	Insignificant Gain				

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

FISCAL RESEARCH DIVISION
733-4910
PREPARED BY: H. Warren Plonk
DATE: April 15, 1996

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

LEGISLATIVE PROPOSAL 8
95-LCX-290(1.5)
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Premiums Tax Collection. (Public)

Sponsors: Representatives Cansler, Blue, Capps, Church, Neely, Robinson, Shaw, and Shubert.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO TRANSFER RESPONSIBILITY FOR COLLECTING THE REMAINDER OF THE GROSS PREMIUMS TAX FROM THE DEPARTMENT OF INSURANCE TO THE DEPARTMENT OF REVENUE AND TO CLARIFY RELATED STATUTES.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-228.9 reads as rewritten:

"§ 105-228.9. ~~Commissioner of Insurance to administer portions of Article.~~ Cross-reference to other taxes relating to insurance.

~~Notwithstanding any other provision of this Article, the taxes levied in this Article on self-insurers and the additional tax levied in this Article at the rate of one and thirty-three hundredths percent (1.33%) on contracts of insurance applicable to fire and lightning coverage shall be administered solely by the Commissioner of Insurance, who~~ The following taxes relating to insurance are collected by the Commissioner of Insurance:

(1) Surplus lines tax, G.S. 58-21-85.

(2) Tax on risk retention groups not chartered in this State, G.S. 58-22-20(3).

(3) Tax on person procuring insurance directly with an unlicensed insurer, G.S. 58-28-5(b).

The Commissioner of Insurance has the same authority and responsibility in administering those ~~portions of this Article~~

taxes as the Secretary of Revenue has in administering ~~the other portions of~~ this Article."

Sec. 2. G.S. 105-228.5 reads as rewritten:

"**§ 105-228.5. Taxes measured by gross premiums.**

(a) Tax Levied. -- A tax is levied in this section on insurers, Article 65 corporations, and self-insurers. An insurer or Article 65 corporation that is subject to the tax levied by this section is not subject to franchise or income taxes imposed by Articles 3 and 4, respectively, of this Chapter.

(b) Tax Base. --

(1) Insurers. -- The tax imposed by this section on an insurer shall be measured by gross premiums from business done in this State during the preceding calendar year.

(2) Additional Local Fire and Lightning Rate. -- The additional tax imposed by subdivision (d)(4) of this section shall be measured by gross premiums from business done in fire districts in this State during the preceding calendar year. For the purpose of this section, the term 'fire district' has the meaning provided in G.S. 58-84-5.

(3) Article 65 Corporations. -- The tax imposed by this section on an Article 65 corporation shall be measured by gross collections from membership dues, exclusive of receipts from cost plus plans, received by the corporation during the preceding calendar year.

(4) Self-insurers. -- The tax imposed by this section on a self-insurer shall be measured by the gross premiums that would be charged against the same or most similar industry or business, taken from the manual insurance rate then in force in this State, applied to the self-insurer's payroll for the previous calendar year as determined under Article 2 of Chapter 97 of the General Statutes modified by the self-insurer's approved experience modifier.

(b1) Calculation of Tax Base. -- In determining the amount of gross premiums from business in this State, all gross premiums received in this State, credited to policies written or procured in this State, or derived from business written in this State shall be deemed to be for contracts covering persons, property, or risks resident or located in this State unless one of the following applies:

(1) The premiums are properly reported and properly allocated as being received from business done in some other nation, territory, state, or states.

(2) The premiums are from policies written in federal areas for persons in military service who pay premiums by assignment of service pay.

Gross premiums from business done in this State in the case of life insurance contracts, including supplemental contracts providing for disability benefits, accidental death benefits, or other special benefits that are not annuities, means all premiums collected in the calendar year, other than for contracts of reinsurance, for policies the premiums on which are paid by or credited to persons, firms, or corporations resident in this State, or in the case of group policies, for contracts of insurance covering persons resident within this State. The only deductions allowed shall be for premiums refunded on policies rescinded for fraud or other breach of contract and premiums that were paid in advance on life insurance contracts and subsequently refunded to the insured, premium payer, beneficiary or estate. Gross premiums shall be deemed to have been collected for the amounts as provided in the policy contracts for the time in force during the year, whether satisfied by cash payment, notes, loans, automatic premium loans, applied dividend, or by any other means except waiver of premiums by companies under a contract for waiver of premium in case of disability.

Gross premiums from business done in this State for all other contracts of insurance, including contracts of insurance required to be carried by the Workers' Compensation Act, means all premiums written during the calendar year, or the equivalent thereof in the case of self-insurers under the Workers' Compensation Act, for contracts covering property or risks in this State, other than for contracts of reinsurance, whether the premiums are designated as premiums, deposits, premium deposits, policy fees, membership fees, <u>installment payment charges,</u> or assessments. Gross premiums shall be deemed to have been written for the amounts as provided in the policy contracts, new and renewal, becoming effective during the year irrespective of the time or method of making payment or settlement for the premiums, and with no deduction for dividends whether returned in cash or allowed in payment or reduction of premiums or for additional insurance, and without any other deduction except for return of premiums, deposits, fees, or assessments for adjustment of policy rates or for cancellation or surrender of policies.

(c) Exclusions. -- Every insurer, in computing the premium tax, shall exclude all of the following from the gross amount of premiums:

(1) All premiums received on or after July 1, 1973, from policies or contracts issued in connection with the funding of a pension, annuity, or profit-sharing plan qualified or exempt under section 401, 403, 404, 408, 457 or 501 of the Code as defined in G.S. 105-228.90.

(2) Premiums or considerations received from annuities, as defined in G.S. 58-7-15.

(3) Funds or considerations received in connection with funding agreements, as defined in G.S. 58-7-16.

The gross amount of the excluded premiums, funds, and considerations shall be exempt from the tax imposed by this section.

(d) Tax ~~Rates.~~ Rates; Disposition. --

(1) Workers Compensation. -- The tax rate to be applied to gross premiums, or the equivalent thereof in the case of self-insurers, collected on contracts applicable to liabilities under the Workers' Compensation Act shall be two and five-tenths percent (2.5%). The net proceeds shall be credited to the General Fund.

(2) Other Insurance Contracts. -- The tax rate to be applied to gross premiums collected on all other insurance contracts issued by insurers shall be one and nine-tenths percent (1.9%). The net proceeds shall be credited to the General Fund.

(3) Additional Statewide Fire and Lightning Rate. -- An additional tax shall be applied to amounts collected on contracts of insurance applicable to fire and lightning coverage, except in the case of marine and automobile policies, at the rate of one and thirty-three hundredths percent ~~(1.33%); twenty-five~~ (1.33%). Twenty-five percent (25%) of the net proceeds of this additional tax shall be deposited in the ~~Rural~~ Volunteer Fire Department Fund established in ~~Articles 84 through 88~~ Article 87 of Chapter 58 of the General Statutes. The remaining net proceeds shall be credited to the General Fund.

(4) Additional Local Fire and Lightning Rate. -- An additional tax shall be applied to amounts

collected on contracts of insurance applicable to fire and lightning coverage within fire districts at the rate of one-half of one percent (1/2 of 1%). The net proceeds shall be credited to the Department of Insurance for disbursement pursuant to G.S. 58-84-25.

(5) Article 65 Corporations. -- The tax rate to be applied to gross premiums and/or gross collections from membership dues, exclusive of receipts from cost plus plans, received by Article 65 corporations shall be one-half of one percent (1/2 of 1%). The net proceeds shall be credited to the General Fund.

(e) Report and Payment. -- Each insurer, Article 65 corporation, and self-insurer doing business in this State shall, within the first 15 days of March, file with the Secretary of Revenue a full and accurate report of the total gross premiums as defined in this section, the payroll and other information required by the Secretary in the case of a self-insurer, or the total gross collections from membership dues exclusive of receipts from cost plus plans collected in this State during the preceding calendar year. The report shall be verified by the oath of the official or other representative responsible for transmitting it; the taxes imposed by this section shall be remitted to the Secretary with the report.

In the case of an insurer liable for the additional local fire and lightning tax, the report shall include the information required under G.S. 58-84-1.

(f) Installment Payments Required. -- Insurers, Article 65 corporations, and self-insurers that are subject to the tax imposed by this section and have a premium tax ~~liability~~ liability, not including the additional local fire and lightning tax, of ten thousand dollars ($10,000) or more for business done in North Carolina during the immediately preceding year shall remit three equal quarterly installments with each installment equal to at least thirty-three and one-third percent (33 1/3%) of the premium tax liability incurred in the immediately preceding taxable year. The quarterly installment payments shall be made on or before April 15, June 15, and October 15 of each taxable year. The company shall remit the balance by the following March 15 in the same manner provided in this section for annual returns.

The Secretary of Revenue may permit an insurance company to pay less than the required estimated payment when the insurer reasonably believes that the total estimated payments made for

the current year will exceed the total anticipated tax liability for the year.

An underpayment of an installment payment required by this subsection shall bear ~~interest, as a penalty,~~ interest at the rate established under G.S. 105-241.1(i). Any overpayment shall bear interest as provided in G.S. 105-266(b) and, together with the interest, shall be credited to the company and applied against the taxes imposed upon the company under this Article.

(g) Exemptions. -- This section does not apply to farmers' mutual assessment fire insurance companies or to fraternal orders or societies that do not operate for a profit and do not issue policies on any person except members."

Sec. 3. G.S. 58-6-25(a) reads as rewritten:

"(a) Charge Levied. -- There is levied on each insurance company an annual charge for the purposes stated in subsection (d) of this section. As used in this section, the term "insurance company" means a company that pays the gross premiums tax levied in G.S. 105-228.5 and G.S. 105-228.8, except that the term does not include a hospital, medical, or dental service corporation regulated under Articles 65 and 66 of this Chapter. The term "insurance company" does not include a company regulated under Article 67 of this Chapter. The charge levied in this section is in addition to all other fees and taxes. The charge shall be at a percentage rate of the company's premium tax liability for the taxable year. In determining an insurance company's premium tax liability for a taxable year, additional taxes imposed by G.S. 105-228.8 and the additional local fire and lightning tax imposed by G.S. 105-228.5(d)(4) shall be disregarded."

Sec. 4. G.S. 58-84-1 reads as rewritten:

"**§ 58-84-1.** ~~**Insurance companies to report premiums collected.**~~ **Fire and lightning insurance report.**

~~Every insurance company, corporation, or association doing business in any town or city in North Carolina that has, or may hereafter have, a regularly organized fire department under the control of the mayor and city council or other governing body of said town or city, and which has in serviceable condition for fire duty apparatus and equipment amounting in value to one thousand dollars ($1,000) or more, and which enforces the fire laws to the satisfaction of the Insurance Commissioner, shall return to the Insurance Commissioner of the State of North Carolina~~ Every insurance company doing business in a fire district in this State shall report to the Secretary of Revenue by March 15 of each year a just and true account of all premiums collected and received from all fire and lightning insurance

business done within the limits of ~~such towns and cities during the year ending December 31, or such portion thereof as it may have transacted such business in such towns and cities. Such companies, corporations, or associations shall make said returns within 60 days from and after the thirty-first day of December of each year.~~ each fire district during the preceding calendar year and shall pay the tax levied in G.S. 105-228.5(d)(4). The Secretary of Revenue shall provide the Commissioner the reports filed pursuant to this section and shall credit the net proceeds of the tax to the Department of Insurance for disbursement pursuant to G.S. 58-84-25."

Sec. 5. G.S. 58-84-5 reads as rewritten:

"**§ 58-84-5. Definitions.**

~~As used in Articles 84 through 88 of this Chapter, the words "city," "cities," "town" or "towns" shall also include and mean sanitary districts, school districts, rural fire districts and any other political subdivisions of the State having an organized fire department.~~

~~Whenever the clerk of any city or town is required to perform any act pursuant to Articles 84 through 88 of this Chapter, clerk shall mean the person so designated by the governing body or committee where there is no clerk.~~

The following definitions apply in Articles 84 through 88 of this Chapter:

(1) City. -- A fire district.

(2) Clerk. -- The clerk of a fire district or, if there is no clerk, the person so designated by the governing body of the fire district.

(3) Fire district. -- Any political subdivision of the State that meets all of the following conditions:

a. It has an organized fire department under the control of its governing body.

b. Its fire department has apparatus and equipment that is in serviceable condition for fire duty and is valued at one thousand dollars ($1,000) or more.

c. It enforces the fire laws to the satisfaction of the Commissioner.

(4) Town. -- A fire district."

Sec. 6. G.S. 58-84-10, 58-84-15, and 58-84-20 are repealed.

Sec. 7. G.S. 58-84-25 reads as rewritten:

"**§ 58-84-25. Disbursement of funds by Insurance Commissioner.**

The Insurance Commissioner shall deduct the sum of three percent (3%) from the ~~money so collected from the insurance companies, corporations, or association, as aforesaid,~~ tax proceeds credited to the Department pursuant to G.S. 105-228.5(d)(4) and pay the same over to the treasurer of the State Firemen's Association for general purposes. The Insurance Commissioner shall deduct the sum of two percent (2%) from the ~~money so collected from the insurance companies, corporations, or associations, as aforesaid,~~ tax proceeds and retain the same in the budget of the Department of Insurance for the purpose of administering the disbursement of funds by the board of trustees in accordance with the provisions of G.S. 58-84-35. The Insurance Commissioner shall, pursuant to G.S. 58-84-50, credit the amount forfeited by nonmember fire districts to the North Carolina State Firemen's Association. The ~~remainder of the money so collected from the insurance companies, corporations, or associations, as aforesaid, doing business in the towns and cities in the State having or that may hereafter have organized fire departments as provided in this Article, said~~ Insurance Commissioner shall pay the remaining tax proceeds to the treasurer of each ~~town or city to be held by him~~ fire district in proportion to the amount of business done in the fire district. These funds shall be held by the treasurer as a separate and distinct ~~fund, and he~~ fund. The fire district shall immediately pay the ~~same~~ funds to the treasurer of the local board of trustees upon ~~his~~ the treasurer's election and qualification, for the use of the board of trustees of the firemen's local relief fund in each ~~town or city,~~ fire district, which board shall be composed of five members, residents of ~~said city or town~~ the fire district as hereinafter provided for, to be used by it for the purposes ~~as named~~ provided in G.S. 58-84-35."

Sec. 8. G.S. 58-22-15(a) reads as rewritten:

"(a) A risk retention group seeking to be chartered in this State must be chartered and licensed as a liability insurance company under Article 7 of this Chapter and, except as provided elsewhere in this Article, must comply with all of the laws and rules applicable to such insurers chartered and licensed in this State and with G.S. 58-22-20 to the extent such requirements are not a limitation on laws, administrative rules, or requirements of this State. As a chartered and licensed liability insurance company, the group is subject to the taxes imposed in Article 8B of Chapter 105 of the General Statutes."

Sec. 9. G.S. 58-22-20(3) reads as rewritten:

"(3) Taxation.

a. All premiums paid for coverages within this State to risk retention groups shall be subject to taxation at the same rate and subject to the same payment procedures and to the same interest, fines, and penalties for nonpayment as those applicable to surplus lines insurance under Article 21 of this Chapter. Premiums paid by purchasing groups are, however, taxed as provided in G.S. 58-22-35(b).

b. To the extent licensed agents or brokers are utilized pursuant to G.S. 58-22-60, they shall report and pay the taxes for the premiums for risks that they have placed with or on behalf of a risk retention group not chartered in this State. Such agent or broker shall keep a complete and separate record of all policies procured from each such risk retention group, which record shall be open to examination by the Commissioner, as provided in G.S. 58-2-185. These records shall, for each policy and each kind of insurance provided thereunder, include the following:

1. The limit of liability;
2. The time period covered;
3. The effective date;
4. The name of the risk retention group that issued the policy;
5. The gross premium charged; and
6. The amount of return premiums, if any.

c. To the extent that insurance agents or brokers are not utilized or fail to pay the tax, each risk retention group shall pay the tax for risks insured within the State. Each risk retention group shall report to the Commissioner all premiums paid to it for risks insured within the State. "

Sec. 10. G.S. 58-22-35(b) reads as rewritten:

"(b) Taxes on premiums paid for coverage of risks resident or located in this State by a purchasing group or any members of the purchasing group shall be:

(1) Imposed at the same rate and subject to the same interest, fines, and penalties as those applicable to premium taxes on similar coverage from a similar

insurance source by other ~~insureds; and~~ insureds. For example, coverage provided by a surplus lines licensee is taxed under Article 21 of this Chapter, coverage provided by an insurance company is taxed under Article 8B of Chapter 105 of the General Statutes, and coverage provided by an unlicensed insurer is taxed under G.S. 58-28-5(b).

(2) Paid first by such insurance source, and if not by such source then by the agent or broker for the purchasing group, and if not by such agent or broker then by the purchasing group, and if not by such group then by each of its members."

Sec. 11. G.S. 58-6-20 reads as rewritten:

"**§ 58-6-20. Policyholders to furnish information.**

~~To enable the Commissioner the better to enforce the payment of the taxes imposed by Articles 1 through 64 of this Chapter and by G.S. 105-228.5 every~~ Every corporation, firm, or individual doing business in the State shall, upon ~~demand~~ request of the Commissioner, furnish ~~to him, upon blanks to be provided by him, a statement of the amount of all insurance held by them, giving the name of the company, number, and amount of policies and the premiums paid on each, and such other information as the Commissioner calls for, or shall file an affidavit with the Commissioner that all their insurance is placed in companies licensed to do business in this State.~~ the Commissioner any information the Commissioner considers necessary to enable the Commissioner to enforce the payment of a tax levied in this Chapter."

Sec. 12. G.S. 58-45-80 reads as rewritten

"**§ 58-45-80. Premium taxes to be paid through ~~Association to Commissioner.~~ Association.**

All premium taxes due on insurance written under this Article shall be remitted by each insurer to the Association; and the Association, as collecting agent for its member companies, shall forward all such taxes to the ~~Commissioner~~ Secretary of Revenue as provided in Article 8B of Chapter 105 of the General Statutes."

Sec. 13. G.S. 58-46-45 reads as rewritten:

"**§ 58-46-45. Premium taxes to be paid through ~~Association to Commissioner.~~ Association.**

All premium taxes due on insurance written under this Article shall be remitted by each insurer to the Association; and the Association, as collecting agent for its member companies, shall forward all such taxes to the ~~Commissioner~~ Secretary of Revenue

as provided in Article 8B of Chapter 105 of the General Statutes."

Sec. 14. G.S. 58-47-30(d) reads as rewritten:

"(d) The fund ~~shall be subject to the premium tax law as stated in North Carolina G.S. 105-228.5.~~ is an insurer for the purposes of Article 8B of Chapter 105 of the General Statutes and assessments paid to the fund are subject to the tax levied in that Article."

Sec. 15. This act becomes effective January 1, 1997, but it is effective only if the sum of one hundred thirty-four thousand twenty-one dollars ($134,021) for the 1996-97 fiscal year is appropriated to the Department of Revenue for two processing positions and one auditing position needed to carry out the tax collection responsibilities transferred to the Department of Revenue pursuant to this act. This act does not obligate the General Assembly to appropriate funds.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H **D**

LEGISLATIVE PROPOSAL 8 - PART TWO
95-LC-290A(1.5)
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Premiums Tax Collection Funds. (Public)

Sponsors: Representatives Shubert, Blue, Cansler, Capps, Church, Neely, Robinson, and Shaw.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO APPROPRIATE FUNDS TO THE DEPARTMENT OF REVENUE FOR PERSONNEL TO CARRY OUT THE RESPONSIBILITY FOR COLLECTING THE GROSS PREMIUMS TAX, WHICH WAS TRANSFERRED FROM THE DEPARTMENT OF INSURANCE TO THE DEPARTMENT OF REVENUE.

The General Assembly of North Carolina enacts:

Section 1. There is appropriated from the General Fund to the Department of Revenue the sum of one hundred thirty-four thousand twenty-one dollars ($134,021) for the 1996-97 fiscal year for two processing positions and one auditing position to carry out the gross premiums tax collection responsibilities transferred from the Department of Insurance to the Department of Revenue pursuant to Chapter 360 of the 1995 Session Laws and the additional collection responsibilities proposed to be transferred by the 1995 General Assembly, 1996 Regular Session.

Sec. 2. This act becomes effective July 1, 1996.

Explanation - Premiums Tax Collection

In 1995, the General Assembly transferred from the Department of Insurance to the Department of Revenue the responsibility for collecting most of the gross premiums taxes on insurance companies. Legislative Proposal 8 would transfer the responsibility for collecting the remaining gross premiums taxes effective January 1, 1997.

Under G.S. 105-228.5, instead of paying corporate income and franchise taxes, insurance companies pay taxes based on gross premiums collected on business done in this State. In addition, employers that carry their own workers' compensation risk, known as self-insurers, and employers that pool their workers' compensation liabilities pay the gross premiums tax on premiums they pay or on the premiums that would be charged to cover the risk. The workers compensation premiums tax rate is 2.5% of gross premiums and the general premiums tax rate is 1.9% of gross premiums. The tax rate on receipts of nonprofit companies providing hospital, medical, and dental coverage is 0.5%. Insurers that provide fire and lightning coverage pay an additional tax at the rate of 1.33% of gross premiums for fire and lightning coverage provided on property other than vehicles and boats.

Chapter 360 of the 1995 Session Laws, which gave the Department of Revenue responsibility for collecting most of the gross premiums tax, provided that collection of the 2.5% tax on workers' compensation self-insurers and the additional 1.33% tax on fire and lightning coverage would remain with the Department of Insurance. In addition, collection of certain special taxes remained with the Department of Insurance: a special local tax on fire and lightning insurance provided within municipalities and fire districts and taxes on surplus lines insurance, some risk retention groups, and unlicensed insurers. The Revenue Laws Study Committee determined that the Department of Revenue should collect the fire and lightning taxes and the self-insurers tax because these taxes are also gross premiums taxes the collection of which is similar to the collection of the general gross premiums tax. As explained below, the Study Committee determined that the Department of Insurance should continue to collect tax on surplus lines insurance, unlicensed insurers, and risk retention groups chartered in other states.

There are two extra taxes on fire and lightning coverage. The first is an extra tax of 1.33% which is distributed 75% to the State and 25% to the Volunteer Fire

Department Fund in the Department of Insurance. Although the responsibility for collecting this tax remained with the Department of Insurance under the 1995 legislation, the Department of Revenue is already collecting it pursuant to an agreement with the Department of Insurance. The second fire and lightning tax is at the rate of 0.5% on coverage provided within municipalities and fire districts; the proceeds of this tax are distributed to the municipalities and fire districts for fire fighters' local relief funds. This tax is paid annually by approximately 600 taxpayers and brings in about $2.5 million a year. Unlike the first fire and lightning tax, the base of this tax includes coverage on vehicles and boats. It is not part of the gross premiums tax base used to calculate the insurance regulatory charge.

The tax on employers who carry their own workers' compensation risk (self-insurers) is measured by the gross premiums that would be charged against the same or similar business applied to the employer's payroll modified by the employer's approved experience modifier. This tax brings in about $17 million a year and is part of the gross premiums tax base used to calculate the insurance regulatory charge. Two Department of Insurance employees administer collection of the tax based on payroll information supplied by employers.

Surplus lines insurance is a market of last resort for commercial property and liability risks. The tax is collected not from insurance companies but from the brokers who place the coverage. The tax is based on information sent in by these brokers, who are called surplus lines licensees, and must be reconciled based on the surplus lines market and other technical factors. The tax is levied on a quarterly basis and is not similar in administration, calculation, or collection to the gross premiums tax. For these reasons, the Study Committee determined that the Department of Insurance should continue to collect it.

For risk retention groups chartered in other states, there is a quarterly tax similar to the surplus lines tax; collection of this tax should be retained in Insurance for the same reasons as the surplus lines tax. There are only about 35 risk retention groups charted in other states; their total tax represents less than $250,000 a year. Existing law requires any State-chartered risk retention group to be licensed as an insurance company; it would, therefore, be covered by the general gross premiums tax collected by the Department of Revenue. In addition, insurers of purchasing groups already pay the gross premiums tax to the Department of Revenue like any other insurance company. If a purchasing group purchases coverage from a surplus lines insurer, however, the surplus lines tax applies to the premiums.

Unlicensed insurers are a special category of insurers, allowed to provide coverage only if the insured makes an affidavit that the insured could not obtain insurance from licensed insurers after diligent search. A detailed report and this affidavit must be filed by the person who procures the insurance within 30 days after the insurance is procured and the tax is due at that time. This tax is closely tied to regulation of the insurers and its collection is not similar to the gross premiums tax. For these reasons, the Study Committee determined that the Department of Insurance should remain responsible for its collection.

Fiscal Report
Fiscal Research Division
April 16, 1996

Proposal #8: Premiums Tax Collection

Explanation:

Refer to the attached document for details of the legislation.

Effective Date:

July 1, 1996 for appropriation to Department of Revenue to support costs to implement the act; January 1, 1997 actual transfer of collection responsibilities.

Fiscal Effect:

The legislation proposes to designate the Department of Revenue the collection agent for the Firemen's Relief Fund and the Self-Insured Workers' Compensation Premiums tax. Proceeds to the relief fund are paid annually by 600 taxpayers and produces about $2.5 million. Tax on employers who provide their own workers' compensation (self-insured) coverage yields $17 million a year. The Department of Insurance has two employees assigned to collection of the self-insured tax, as well as, staff who conduct field audits for this tax. To maintain the same efficiency in managing collection of proceeds from the additional premiums tax, the Department of Revenue estimates two positions are required to meet processing responsibilities, and an auditor to continue the local program review.

Resources to meet the additional cost of the positions would come from the General Fund. The estimate includes an allowance for a 2% increase in salaries annually, and assumes that the Department of Revenue will have responsibilities only for collecting the ½ of 1% premiums tax for the relief fund, but not distribution of proceeds to volunteer fire departments.

	FY 96-97	FY 97-98	FY 98-99	FY 99-00	FY 00-01
EXPENDITURES:					
Recurring	116,011	117,655	119,331	121,041	122,784
Non-recurring	18,010				
POSITIONS:	3	3	3	3	3

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

S D

LEGISLATIVE PROPOSAL 9
95-LJX-24(1.5)
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Tax At Rack Fine Tuning. (Public)

Sponsors: Senators Kerr, Cochrane, Cooper, and Soles.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO CLARIFY THE REQUIREMENTS CONCERNING IMPORTS AND EXPORTS OF MOTOR FUEL UNDER THE "TAX AT THE RACK" LAWS AND TO MAKE OTHER ADJUSTMENTS TO THOSE LAWS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-449.60 is amended by adding the following subdivision in the appropriate alphabetical order and renumbering the succeeding subdivisions accordingly:

"(20) In-State-only supplier. -- Either of the following:

a. A supplier that is required to have a license and elects not 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.

b. A supplier that does business only in this State."

Sec. 2. G.S. 105-449.60, as amended by Section 1 of this act, is amended by adding the following subdivision in the appropriate alphabetical order and renumbering the succeeding subdivisions accordingly:

"(35) Tax. -- An inspection or other excise tax on motor fuel and any other fee or charge imposed on motor fuel on a per-gallon basis."

Sec. 3. G.S. 105-449.65 reads as rewritten:

"**§ 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) An exporter, if the Secretary imposes this requirement by rule.~~
~~(6)~~ (5) A blender.
~~(7)~~ (6) A motor fuel transporter.
~~(8)~~ (7) A bulk-end user of undyed diesel fuel.
~~(9)~~ (8) A retailer of undyed diesel fuel.

(b) 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 an occasional importer or a tank wagon importer is not required to obtain a separate license as a distributor. A person who is licensed as a distributor is not required to obtain a separate license as an importer if the distributor acquires fuel for import only from an elective supplier or a permissive supplier. A person who is licensed as a distributor or a blender is not required to obtain a separate license as a motor fuel transporter if the distributor or blender does not transport motor fuel for others for hire."

Sec. 4. G.S. 105-449.66(a)(2) reads as rewritten:

"(2) Occasional importer. -- An occasional importer is ~~a person who~~ any of the following that imports motor fuel by any means outside the terminal transfer ~~system.~~ system:

a. A distributor that imports motor fuel on an average basis of no more than once a month during a calendar year.
b. A bulk-end user that is not a distributor.
c. A distributor that imports motor fuel for use in a race car."

Sec. 5. G.S. 105-449.67 reads as rewritten:

"**§ 105-449.67. List of persons who may obtain a license.**

(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.

(3) An exporter.

(b) Effect on Exports. -- An exporter license or a distributor license authorizes the license holder to pay the destination state tax on motor fuel purchased for export instead of paying this State's tax on the fuel. An unlicensed exporter or unlicensed distributor must pay this State's tax on motor fuel purchased for export.

(c) Multiple Activity. -- A person who is licensed as a distributor is considered to have a license as an exporter."

Sec. 6. G.S. 105-449.69 reads as rewritten:

"**§ 105-449.69. 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 retailer 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 terminal transfer 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~~ importer, an exporter, 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 or as a distributor must list on the application each state from which the applicant intends to import motor fuel and, if required by a state listed, must be licensed or registered for motor fuel tax purposes in that state. If a state listed requires the applicant to be licensed or registered, the applicant must give the applicant's license or registration number in that state.

A license holder that intends to import motor fuel from a state not listed on the license holder's application for an importer's license or a distributor's license must give the Secretary written notice of the change before importing motor fuel from that state. The notice must include the information that is required on the license application.

(e) Export Activity. -- An applicant for a license as an exporter must designate an agent located in North Carolina for service of process and must give the agent's name and address. An applicant for a license as an exporter or as a distributor must list on the application each state to which the applicant intends to export motor fuel received in this State by means of a transfer that is outside the terminal transfer system and, if required by a state listed, must be licensed or registered for motor fuel tax purposes in that state. If a state listed requires the applicant to be licensed or registered, the applicant must give the applicant's license or registration number in that state.

A license holder that intends to export motor fuel to a state not listed on the license holder's application for an exporter's license or a distributor's license must give the Secretary written notice of the change before exporting motor fuel to that state. The notice must include the information that is required on the license application."

Sec. 7. G.S. 105-449.70(a) reads as rewritten:

"(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 makes the election allowed by this section is an elective supplier. A supplier that does not make the election allowed by this section is an in-State-only supplier."

Sec. 8. G.S. 105-449.70(b) is amended by adding a new subdivision to read:

"(4) To report removals of fuel received by a person who is not licensed in the state where the removal occurred."

Sec. 9. G.S. 105-449.71(b) is amended by adding a new subdivision to read:

"(4) To report removals of fuel received by a person who is not licensed in the state where the removal occurred."

Sec. 10. G.S. 105-449.72 reads as rewritten:

"**§ 105-449.72. 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, an exporter, a blender, a permissive supplier, or a distributor must file with the Secretary a bond or an irrevocable letter of credit. A bond 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. 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~~ neither a position holder ~~or~~ nor a person that receives motor fuel pursuant to a two-party exchange.

b. An occasional importer.

c. A tank wagon importer.

d. A distributor.

e. An exporter.

(3) For an applicant for a license as a blender, a bond is required only if the applicant's average expected annual tax liability under this Article, as determined by the Secretary, is at least two thousand dollars ($2,000). When a bond is required, the bond amount is the same as under subdivision (2) of this subsection.

(b) Multiple Activity. -- ~~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~~ two or more of the licenses listed in subdivision (a)(2) or (a)(3) of this section may file one bond that covers the combined liabilities of the applicant under ~~both activities.~~ all the activities. A bond for these combined activities may not exceed the maximum amount set in subdivision (a)(2) of this subsection.

~~(b)~~ (c) 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."

Sec. 11. G.S. 105-449.73 reads as rewritten:

"**§ 105-449.73. Reasons why the Secretary can deny an application for a license.**

The Secretary may refuse to issue a license to an individual applicant that 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 Article 36 or 36A of this Chapter cancelled by the Secretary for cause.

(2) Had a motor fuel license or registration issued by another state cancelled for cause.

~~(2)~~ (3) Had a federal Certificate of Registry issued under § 4101 of the Code, or a similar federal authorization, revoked.

~~(3)~~ (4) Been convicted of fraud or misrepresentation.

~~(4)~~ (5) Been convicted of any other offense that indicates that the applicant may not comply with this Article if issued a license."

Sec. 12. G.S. 105-449.77 reads as rewritten:

"**§ 105-449.77. 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 that hold a current license issued under this Article, by license category.

(b) ~~Distributor List.~~ Supplier Lists. -- The Secretary must give a list of licensed ~~distributors~~ suppliers, licensed terminal operators, licensed importers, licensed distributors, and licensed exporters to each licensed ~~supplier that asks for a copy of the list.~~ supplier. The list must state the ~~name~~ name, account number, and business address of each ~~distributor~~ license holder on the list. The Secretary must send a monthly update of the list to each ~~supplier that requested a copy of the list.~~ licensed supplier.

~~(c) Supplier List. -- The Secretary must give a list of licensed suppliers to each distributor that asks for a copy of the list. The list must state the name and business address of each supplier on the list and must indicate whether the supplier is an elective supplier or a permissive supplier. The Secretary must send an annual update of the list to each distributor that requested a copy of the list.~~

The Secretary must give a list of licensed suppliers to each licensed distributor, licensed exporter, and licensed importer.

The Secretary must also give a list of licensed suppliers to each unlicensed distributor or unlicensed exporter that asks for a copy of the list. The list must state the name, account number, and business address of each supplier on the list and must indicate whether the supplier is an elective supplier, a permissive supplier, or an in-State-only supplier. The Secretary must send an annual update of the list to each licensed distributor, licensed exporter, and licensed importer, and to each unlicensed distributor or unlicensed exporter that requested a copy of the list.

(c) Transporter Lists. -- The Secretary must give a list of licensed motor fuel transporters to each licensed supplier, licensed terminal operator, licensed importer, licensed blender, licensed distributor, and licensed exporter. The list must state the name, account number, and business address of each motor fuel transporter on the list. The Secretary must send a monthly update of the list to each license holder to whom the Secretary must give the list.

The Secretary must give a list of licensed suppliers, licensed terminal operators, licensed importers, licensed blenders, licensed distributors, and licensed exporters to each licensed motor fuel transporter. The list must state the name, account number, and business address of each license holder on the list. The Secretary must send a monthly update of the list to each licensed motor fuel transporter."

Sec. 13. G.S. 105-449.81 reads as rewritten:

"**§ 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 a system 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 means of transfer outside the terminal transfer system for sale, use, or storage 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) Fuel grade ethanol that meets any of the following descriptions:

a. Is removed from a terminal or another storage and distribution facility, unless the removed fuel is received by a supplier for subsequent sale.

b. Is imported to this State outside the terminal transfer system by a means other than a marine vessel, a transport truck, or a railroad tank car.

~~(4)~~ (5) Blended fuel made in this State or imported to this State.

(6) Transferred within the terminal transfer system and, upon transfer, is subject to the federal excise tax imposed by § 4081 of the Code."

Sec. 14. G.S. 105-449.82(c) reads as rewritten:

"(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 person that first receives the fuel upon its removal from the terminal. If the motor fuel is removed by an unlicensed distributor, the supplier of the fuel is jointly and severally liable for the tax due on the fuel. If the motor fuel is sold by a person who is not licensed as a supplier, as required by this Article, the terminal operator, the person selling the fuel, and the person removing the fuel are jointly and severally liable for the tax due on the fuel. 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, the supplier, and the person removing the fuel are jointly and severally liable for the tax due on the fuel."

Sec. 15. Part 3 of Article 36C of Chapter 105 of the General Statutes is amended by adding a new section to read:

"**§ 105-449.83A. Liability for tax on fuel grade ethanol.**

The excise tax imposed by G.S. 105-449.81(4) on fuel grade ethanol removed from a storage facility is payable by the fuel alcohol provider. The excise tax imposed by that subdivision on fuel grade ethanol imported to this State is payable by the importer."

Sec. 16. G.S. 105-449.84 reads as rewritten:

"**§ 105-449.84. Liability for tax on blended fuel.**

(a) On Blender. -- The excise tax imposed by G.S. ~~105-449.81(4)~~ 105-449.81(5) on blended fuel made 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 made and the number of gallons of previously taxed motor fuel used to make the blended fuel.

(b) On Importer. -- The excise tax imposed by G.S. ~~105-449.81(4)~~ 105-449.81(5) on blended fuel imported to this State is payable by the importer.

(c) Blends Made at Terminal. -- The following blended fuel is considered to have been made by the supplier of gasoline or undyed diesel fuel used in the blend:

(1) An in-line-blend made by combining a liquid with gasoline or undyed diesel fuel as the fuel is delivered at a terminal rack into the motor fuel storage compartment of a transport truck or a tank wagon.

(2) A kerosene splash-blend made when kerosene is delivered at a terminal into a motor fuel storage compartment of a transport truck or a tank wagon and undyed diesel fuel is also delivered at that terminal into the same storage compartment, if 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."

Sec. 17. Part 3 of Article 36C of Chapter 105 of the General Statutes is amended by adding a new section to read:

"**§ 105-449.84A. Liability for tax on behind-the-rack transfers.**

The excise tax imposed by G.S. 105-449.81(6) on motor fuel transferred within the terminal transfer system is payable by the supplier of the fuel, the person receiving the fuel, and the terminal operator of the terminal at which the fuel was transferred, all of whom are jointly and severally liable for the tax."

Sec. 18. G.S. 105-449.85(b) reads as rewritten:

"(b) Liability. -- The terminal operator whose motor fuel is unaccounted for is liable for the tax imposed by this ~~section.~~ section and is liable for a penalty equal to the amount of tax payable. Motor fuel received by a terminal operator and not shown on ~~a report~~ an informational return filed by the terminal operator with the Secretary as having been removed from the terminal is presumed to be unaccounted for. A terminal operator may establish that motor fuel received at a terminal but not shown on ~~a report~~ an informational return as having been removed from the terminal was lost or part of a transmix and is therefore not unaccounted for."

Sec. 19. G.S. 105-449.87(a)(4) is repealed.

Sec. 20. G.S. 105-449.88 reads as rewritten:

"**§ 105-449.88. Exemptions from the excise tax.**

The excise tax on motor fuel does not apply to the following:

(1) Motor fuel removed, by transport truck or another means of transfer outside the terminal transfer system, from a terminal for export, if the supplier of the motor fuel collects tax on it at the rate of the motor fuel's destination ~~state that is printed on the shipping document for the motor fuel.~~ state. If the removed fuel is to be used for a purpose that is exempt from tax in the destination state and, when removing the fuel, the licensed distributor or licensed exporter uses an access card or code specified by the supplier to notify the supplier that the fuel will be resold in an exempt sale, no tax is due on the removal.

(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."

Sec. 21. Effective July 1, 1997, G.S. 105-449.88, as amended by Section 20 of this act, reads as rewritten:

"**§ 105-449.88. Exemptions from the excise tax.**

The excise tax on motor fuel does not apply to the following:

(1) Motor fuel removed, by transport truck or another means of transfer outside the terminal transfer system, from a terminal for export, if the supplier of the motor fuel collects tax on it at the rate of the motor fuel's destination state. ~~If the removed fuel is to be used for a purpose that is exempt from tax in the destination state and, when removing the fuel, the licensed distributor or licensed exporter uses an access card or code specified by the supplier to notify the supplier that the fuel will be resold in an exempt sale, no tax is due on the removal.~~

(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."

Sec. 22. Part 3 of Article 36C of Chapter 105 of the General Statutes is amended by adding a new section to read:

"**§ 105-449.89. Removals by out-of-state bulk-end user.**

An out-of-state bulk-end user may remove motor fuel from a terminal in this State for use in the state in which the bulk-end user is located as follows:

(1) Upon payment to the supplier of tax on the motor fuel at the motor fuel rate.

(2) Upon payment to the supplier of destination state tax on the motor fuel if the bulk-end user acquires the fuel from a supplier who, with respect to the destination state of the fuel, is either a permissive supplier or an elective supplier and therefore collects the destination state tax on the fuel."

Sec. 23. G.S. 105-449.90 reads as rewritten:

"**§ 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 annually, quarterly, or monthly, as specified in this section. A return must be filed with the Secretary and be in the form required by the Secretary.

An annual return is due within 45 days after the end of each calendar year. An annual return covers tax liabilities that accrue in the calendar year preceding the date the return is due.

A quarterly return is due by the last day of the month that follows the end of a calendar quarter. A quarterly return covers tax liabilities that accrue in the calendar quarter preceding the date the return is due.

A monthly return of a person other than an occasional importer is due within 22 days after the end of each month. A monthly return of an occasional importer is due by the 1st of each month. A monthly return covers tax liabilities that accrue in the calendar month preceding the date the return is due.

(b) Annual Filers. -- A terminal operator must file an annual return for the compensating tax imposed by G.S. 105-449.85.

(c) Quarterly Filers. -- A licensed importer that removes fuel at a terminal rack of a permissive or an elective supplier and a licensed distributor must file a quarterly return under G.S. 105-449.94 to reconcile exempt sales.

(d) Monthly Filers on 22nd. -- The following persons must file a monthly return by the 22nd of each month:

(1) A refiner.

(2) A supplier.

(3) A bonded importer.

(4) A blender.

(5) A tank wagon importer.

(6) A person that ~~is liable~~ incurred a liability under G.S. 105-449.86 during the preceding month for the tax on dyed diesel fuel used to operate certain highway vehicles.

(7) A person that ~~is liable~~ incurred a liability under G.S. 105-449.87 during the preceding month for the backup tax on motor fuel.

(e) Monthly Filers on 1st. -- An occasional importer must file a monthly return by the 1st of each month. An occasional importer is not required to file a return, however, if all the motor fuel imported by the importer in a reporting period was removed at a terminal located in another state and the supplier of the fuel is an elective supplier or a permissive supplier."

Sec. 24. Part 4 of Article 36C of Chapter 105 of the General Statutes is amended by adding the following section to read:

"**§ 105-449.90A. Payment by supplier of destination state tax collected on exported motor fuel.**

Tax collected by a supplier on exported motor fuel is payable by the supplier to the destination state if the supplier is licensed in that state for payment of motor fuel excise taxes. Tax collected by a supplier on exported motor fuel is payable to the Secretary for remittance to the destination state if the supplier is not licensed in that state for payment of motor fuel excise taxes. Payments of destination state tax are due to the destination state or the Secretary, as appropriate, on the date set by the law of the destination state. Payments of destination state tax to the Secretary must be accompanied by a form provided by the Secretary that contains the information required by the Secretary."

Sec. 25. G.S. 105-449.91 reads as rewritten:

"**§ 105-449.91. Remittance of tax ~~by distributor.~~ to supplier.**

(a) Distributor. -- A distributor ~~that is liable for the~~ must remit tax ~~imposed~~ due on motor fuel removed at a terminal rack ~~must remit the tax~~ to the supplier of the fuel. A licensed distributor has the right to defer the remittance of tax to the supplier, as trustee, until the date the trustee must pay the tax to ~~the State. Payment of tax by~~ this State or to another state. The time when an unlicensed distributor must remit tax to a supplier is governed by the terms of the contract between the ~~unlicensed distributor and the supplier. G.S. 105-449.76 governs the cancellation of a distributor's license.~~ supplier and the unlicensed distributor.

(b) Exporter. -- An exporter must remit tax due on motor fuel removed at a terminal rack to the supplier of the fuel. A licensed exporter that is also licensed in the destination state has the right to defer the remittance of tax to the supplier until the date set by the law of the destination state of the fuel. The time when an unlicensed exporter, or a licensed exporter that is not also licensed in the destination state, must remit tax to a supplier is governed by the terms of the contract between the supplier and the exporter.

(c) Importer. -- A licensed importer must remit tax due on motor fuel removed at a terminal rack of a permissive or an elective supplier to the supplier of the fuel. A licensed importer that removes fuel from a terminal rack of a permissive or an elective supplier has the right to defer the remittance of tax to the supplier until the date the supplier must pay the tax to this State.

(d) General. -- The method by which a distributor, an exporter, or a licensed importer must remit tax to a supplier is governed by the terms of the contract between the supplier and the distributor, exporter, or licensed importer and the supplier. G.S. 105-449.76 governs the cancellation of a the license of a distributor, an exporter, and an importer."

Sec. 26. G.S. 105-449.92 reads as rewritten:

"**§ 105-449.92. Notice to suppliers of cancellation or reissuance of ~~a distributor's license;~~ certain licenses; effect of notice.**

(a) Notice to Suppliers. -- If the Secretary cancels a distributor's ~~license,~~ license, an exporter's license, or an importer's license. the Secretary must notify all suppliers of the cancellation. If the Secretary issues a license to a ~~distributor~~ distributor, an exporter, or an importer whose license was cancelled, the Secretary must notify all suppliers of the issuance.

(b) Effect of Notice. -- A supplier that sells motor fuel to a distributor or an exporter after receiving notice from the Secretary that the Secretary has cancelled the distributor's or exporter's license is jointly and severally liable with the distributor or exporter for any tax due on motor fuel the supplier sells to the distributor or exporter after receiving the notice. This joint and several liability does not apply to excise tax due on motor fuel sold to a previously unlicensed distributor or unlicensed exporter after the supplier receives notice from the Secretary that the Secretary has issued another license to the ~~distributor.~~ distributor or exporter."

Sec. 27. G.S. 105-449.93 reads as rewritten:

"§ 105-449.93. Exempt sale deduction and percentage discount for licensed ~~distributors.~~ distributors and some licensed importers.

(a) Deduction. -- A ~~licensed distributor~~ license holder listed below may deduct from the amount of tax otherwise payable to a supplier the amount calculated on motor fuel the ~~distributor~~ license holder received from the supplier and resold to a governmental unit whose purchases of motor fuel are exempt from the tax under G.S. 105-449.88 if, when removing the fuel, the ~~distributor~~ license holder used an access card or code specified by the supplier to notify the supplier of the ~~distributor's~~ license holder's intent to resell the fuel in an exempt ~~sale.~~ sale:

(1) A licensed distributor.

(2) A licensed importer that removed the motor fuel from a terminal rack of a permissive or an elective supplier.

(b) Percentage 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 one percent (1%) of the amount of tax payable. A licensed importer that removes motor fuel from a terminal rack of a permissive or an elective supplier and that pays the tax due the supplier by the date the supplier must pay the tax to the State may deduct from the amount due a discount of the same amount allowed a licensed distributor. The discount covers the expense of furnishing a bond and losses due to shrinkage or evaporation. A supplier may not directly or indirectly deny this discount to a licensed distributor or licensed importer that pays the ~~excise~~ tax due the supplier by the date the supplier must pay the tax to the State."

Sec. 28. G.S. 105-449.94 reads as rewritten:

"§ 105-449.94. Quarterly reconciling return for exempt sales by licensed ~~distributor.~~ distributor and some licensed importers.

(a) Return. -- A licensed distributor or a licensed importer that deducts exempt sales under G.S. 105-449.93(a) when paying tax to a supplier must file a quarterly reconciling return for the exempt sales. The return must list the following information:

(1) The number of gallons for which a deduction was taken during the quarter, by supplier.

(2) The number of gallons sold in exempt sales during the quarter, by type of sale, and the purchasers of the fuel in the exempt sales.

(b) Payment. -- If the number of gallons for which a licensed distributor or licensed importer takes a deduction during a

quarter exceeds the number of exempt gallons sold, the licensed distributor or licensed importer must pay tax on the difference at the motor fuel rate. The licensed distributor or licensed importer is not allowed a percentage discount when paying tax under this subsection.

(c) Refund. -- If the number of gallons for which a licensed distributor or licensed importer takes a deduction during a quarter is less than the number of exempt gallons sold, the Secretary must refund the ~~licensed distributor for the~~ amount of tax paid on the difference. The Secretary must reduce the amount of the refund by the amount of the percentage discount ~~the distributor~~ received on the fuel.

~~(d) Exception. -- If the number of gallons for which a licensed distributor takes a deduction during a quarter equals the number of exempt gallons sold, the licensed distributor is not required to file a return under this section for that quarter. The Secretary may waive the requirement of filing a return under this section in other specified circumstances.~~"

Sec. 29. G.S. 105-449.95 reads as rewritten:

"**§ 105-449.95. Quarterly hold harmless for licensed ~~distributors.~~ distributors and some licensed importers.**

(a) Calculation. -- At the end of each calendar quarter, the Secretary must review the amount of discounts each licensed distributor licensed importer received under G.S. 105-449.93(b). The Secretary must determine if the amount of discounts the distributor or importer received under that subsection in each month of the quarter is less than the amount the distributor or importer would have received if the distributor or importer had been allowed a discount on taxable gasoline purchased by the distributor or importer from a supplier during each month of the quarter under the following schedule:

Amount of Gasoline Purchased Each Month	Percentage Discount
First 150,000 gallons	2%
Next 100,000 gallons	1 1/2%
Amount over 250,000 gallons	1%.

(b) Refund. -- If the amount the licensed distributor or licensed importer received under G.S. 105-449.93(b) for a month in the quarter is less than the amount the distributor or importer would have received on the distributor's or importer's taxable gasoline purchases under the monthly schedule in subsection (a) of this section, the Secretary must send the distributor or importer a refund check for the difference. In determining the amount of discounts a distributor or importer received under G.S. 105-449.93(b) for gasoline purchased in a

month, a distributor or importer is considered to have received the amount of any discounts the distributor or importer could have received under that subsection but did not receive because the distributor or importer failed to pay the tax due to the supplier by the date the supplier had to pay the tax to the State."

Sec. 30. G.S. 105-449.96 reads as rewritten:

"**§ 105-449.96. Information required on return filed by supplier.**

A return of a supplier must list all of the following information and any other information required by the Secretary:

(1) The number of gallons of tax-paid motor fuel received by the supplier during the ~~month by the supplier by a system transfer, by~~ month, sorted by type of fuel, ~~and by terminal.~~ seller, point of origin, destination state, and carrier.

~~(2) The number of gallons of motor fuel imported during the month by the supplier by a means of transfer outside the terminal transfer system.~~

~~(3)~~ (2) The number of gallons of motor fuel removed at a terminal rack during the month from the account of the supplier, sorted by type of fuel, ~~by~~ receiving distributor, ~~and by terminal.~~ exporter, or importer, terminal code, and carrier.

~~(4)~~ (3) The number of gallons of motor fuel removed during the month for export, sorted by ~~distributor and by terminal, and, for each removal, the destination state of the fuel.~~ type of fuel, receiving distributor or exporter, terminal code, destination state, and carrier.

~~(5)~~ (4) The number of gallons of motor fuel removed during the ~~month, by distributor and by terminal, at~~ month at a terminal located in another state for destination to this State, as indicated on the shipping document for the ~~fuel.~~ fuel, sorted by type of fuel, receiving distributor, exporter, or importer, terminal code, and carrier.

~~(6)~~ (5) The number of gallons of motor fuel the supplier sold during the ~~month, by distributor and by terminal,~~ month to ~~either~~ any of the ~~following:~~ following, sorted by type of fuel,

exempt entity, receiving distributor, terminal code, and carrier:

a. A governmental unit whose use of fuel is exempt from the tax.

b. A licensed distributor that resold the motor fuel to a governmental unit whose use of fuel is exempt from the tax, as ~~reported~~ indicated by the distributor.

c. A licensed exporter that resold the motor fuel to a person whose use of fuel is exempt from tax in the destination state, as indicated by the exporter.

~~(7)~~ (6) The amount of discounts allowed under G.S. 105-449.93(b) on motor fuel sold during the month to licensed ~~distributors, sorted by distributor.~~ distributors or licensed importers."

Sec. 31. G.S. 105-449.97 reads as rewritten:

"**§ 105-449.97. Deductions and discounts allowed a supplier when filing a return.**

(a) Taxes Not Remitted. -- When a supplier files a return, the supplier may deduct from the amount of tax payable with the return the amount of tax ~~a licensed distributor~~ any of the following license holders owes the supplier but failed to remit to the ~~supplier.~~ supplier:

(1) A licensed distributor.

(2) A licensed importer that removed the motor fuel on which the tax is due from a terminal of an elective or a permissive supplier.

(3) A licensed exporter, if the destination state of the exported motor fuel allows a supplier in that state to deduct from the amount of tax payable with a return the amount of tax an exporter licensed in that state owes the supplier but fails to pay.

A supplier is not liable for tax a ~~licensed distributor~~ license holder listed in this subsection owes the supplier but fails to pay. If a ~~licensed distributor~~ listed license holder pays tax owed to a supplier after the supplier deducts the amount on a return, the supplier must promptly remit the ~~distributor's~~ payment to the Secretary. When a supplier deducts an amount not paid to the supplier by a licensed distributor or licensed exporter on exported motor fuel, the Secretary must notify the appropriate destination state of the failure and cooperate with that state in recovering from the exporter the amount deducted.

(b) Administrative Discount. -- A supplier that files a timely return may deduct from the amount of tax payable with the return an administrative discount of one-tenth of one percent (0.1%) of the amount of tax payable to this State as the trustee, not to exceed eight thousand dollars ($8,000) a month. The discount covers expenses incurred in collecting taxes on motor ~~fuel from distributors.~~ fuel.

(c) Percentage Discount. -- A supplier that sells motor fuel directly to an unlicensed distributor or unlicensed exporter or to the bulk-end user, the retailer, or user of the fuel ~~can~~ may take the same percentage discount on the fuel that a licensed distributor ~~can~~ may take under G.S. 105-449.93(b) when making deferred payments of tax to the supplier."

Sec. 32. Effective July 1, 1997, G.S. 105-449.97(a), as amended by Section 31 of this act, reads as rewritten:

"(a) Taxes Not Remitted. -- When a supplier files a return, the supplier may deduct from the amount of tax payable with the return the amount of tax any of the following license holders owes the supplier but failed to remit to the supplier:

(1) A licensed distributor.

(2) A licensed importer that removed the motor fuel on which the tax is due from a terminal of an elective or a permissive supplier.

~~(3) A licensed exporter, if the destination state of the exported motor fuel allows a supplier in that state to deduct from the amount of tax payable with a return the amount of tax an exporter licensed in that state owes the supplier but fails to pay.~~

A supplier is not liable for tax a license holder listed in this subsection owes the supplier but fails to pay. If a listed license holder pays tax owed to a supplier after the supplier deducts the amount on a return, the supplier must promptly remit the payment to the Secretary. ~~When a supplier deducts an amount not paid to the supplier by a licensed distributor or licensed exporter on exported motor fuel, the Secretary must notify the appropriate destination state of the failure and cooperate with that state in recovering from the exporter the amount deducted.~~"

Sec. 33. G.S. 105-449.98 reads as rewritten:

"**§ 105-449.98. Duties of supplier concerning payments by ~~distributors.~~ distributors, exporters, and importers.**

(a) As Fiduciary. -- A supplier has a fiduciary duty to remit to the Secretary the amount of tax paid to the supplier by a licensed ~~distributor.~~ distributor, licensed exporter, or licensed importer. A supplier is liable for taxes paid to the

supplier by a licensed ~~distributor.~~ distributor, licensed exporter, or licensed importer.

(b) Notification to ~~Distributor.~~ Distributor or Exporter. -- A supplier must notify a licensed distributor or licensed exporter that received motor fuel from the supplier during a reporting period of the number of taxable gallons received. The supplier must give this notice after the end of each reporting period and before the licensed distributor or licensed exporter must remit to the supplier the amount of tax due on the fuel.

(c) Notification to Department. -- A supplier of motor fuel at a terminal must notify the Department within 10 business days after a return is due of any licensed distributors or licensed exporters that 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.

(d) Payment Application. -- A supplier that receives a payment of ~~excise~~ tax from a distributor or a licensed exporter may not apply the payment to debts for motor fuel purchased from the supplier."

Sec. 34. G.S. 105-449.100 reads as rewritten:

"§ 105-449.100. ~~Report by terminal operator.~~ Terminal operator to file informational return showing changes in amount of motor fuel at the terminal.

A terminal operator must ~~make~~ file a monthly ~~report to~~ informational return with the Secretary ~~of~~ that shows the amount of motor fuel received or removed from the terminal during the month. The ~~report~~ return is due by the 25th day of the month following the month covered by the ~~report and~~ return. The return 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 of motor fuel removed from inventory at the terminal during the month and, for each removal, the position holder for the fuel and the destination state of the fuel.

(3) The number of gallons of motor fuel gained or lost at the terminal during the month."

Sec. 35. G.S. 105-449.101 reads as rewritten:

"§ 105-449.101. ~~Reports by those that transport motor fuel.~~ Motor fuel transporter to file informational return showing deliveries of imported or exported motor fuel.

(a) Requirement. -- A person that 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~~ file a monthly ~~report to~~ informational return with the Secretary ~~of~~ that shows motor fuel received or delivered for import or export by the transporter during the month. This requirement does not apply to a distributor that is not required to be licensed as a motor fuel transporter.

(b) Content. -- The ~~report~~ return required by this section is due by the 25th day of the month following the month covered by the ~~report and~~ return. The return 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 destination state of the fuel.

(2) The name and address of each person from whom the transporter received motor fuel in the State for delivery outside the State, the amount of motor fuel delivered, the date the motor fuel was delivered, and the destination state of the fuel."

Sec. 36. G.S. 105-449.102 reads as rewritten:

"**§ 105-449.102. ~~Report of~~ Distributor to file return showing exports from a bulk plant.**

(a) Return. -- A distributor that exports motor fuel from a bulk plant located in this State must ~~make~~ file a monthly ~~report to~~ return with the Secretary ~~of~~ that shows the exports. The ~~report~~ return is due by the 25th day of the month following the month covered by the ~~report. The report~~ return. The return serves as a claim for refund by the distributor for tax paid to this State on the exported motor fuel.

(b) Content. -- The return 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.

(3) A certification that the distributor has paid to the destination state of the motor fuel exported during the month, or will pay on a timely basis, the amount of tax due that state on the fuel."

Sec. 37. Part 4 of Article 36C of Chapter 105 of the General Statutes is amended by adding a new section to read:

"§ 105-449.104. Use of name and account number on return.

When a transaction with a person licensed under this Article is required to be reported on a return, the return must state the license holder's name and the account number used by the Department to identify the license holder. The name of a license holder and the license holder's account number is stated on the lists compiled under G.S. 105-449.77."

Sec. 38. G.S. 105-449.105 reads as rewritten:

"**§ 105-449.105. Refunds upon application for tax paid on exempt fuel, lost fuel, ~~used in boats~~ fuel unsalable for highway use, and undyed diesel fuel used in boats.**

(a) Exempt Fuel. -- A distributor may obtain a refund of tax paid by the distributor on motor fuel sold to a governmental unit whose use of motor fuel is exempt from the motor fuel excise tax. A governmental unit whose use of motor fuel is exempt from the motor fuel excise tax may obtain a refund of tax paid by it on motor fuel. A person may obtain a refund of tax paid by the person on exported fuel, 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 supplier, an importer, or a distributor that loses tax-paid 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 that accidentally combines any of the following may obtain a refund for the amount of tax paid on the fuel:

(1) Dyed diesel fuel with tax-paid motor fuel.

(2) Gasoline with diesel fuel.

(3) Undyed diesel fuel with dyed kerosene.

(d) Marina. -- A marina may obtain a refund of tax paid by the marina on undyed diesel fuel purchased for use in a boat or another marine vessel. The refund applies only to undyed diesel fuel delivered at the time of purchase into a storage facility that is marked "For Boat Use Only" or another phrase that clearly indicates the fuel is not to be used to operate a highway vehicle.

(e) Refund Amount. -- The amount of a refund allowed under this section is the amount of tax ~~paid.~~ paid, less the amount of any discount allowed on the fuel under G.S. 105-449.93."

Sec. 39. G.S. 105-449.115(e) reads as rewritten:

"(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. A person who accepts delivery of motor fuel in violation of this subsection is jointly and severally liable for any tax due on the fuel."

Sec. 40. G.S. 105-449.115(f) reads as rewritten:

"(f) ~~Sanctions.~~ Sanctions Against Transporter. -- 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.~~ one thousand five hundred dollars ($1,500). 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.~~ seven thousand five hundred dollars ($7,500). A penalty imposed under this subsection is in addition to any motor fuel tax assessed."

Sec. 41. Part 6 of Article 36C of Chapter 105 of the General Statutes is amended by adding a new section to read:

"§ 105-449.118A. Civil penalty for refusing to allow the taking of a motor fuel sample.

A person who refuses to allow the taking of a motor fuel sample is subject to a civil penalty of one thousand dollars ($1,000). The penalty is payable to the Department of Transportation, Division of Motor Vehicles, or the Department of Revenue. If the refusal is for a sample to be taken from a vehicle, the penalty is payable by the person in whose name the vehicle is registered. If the refusal is for a sample to be taken from any other storage tank or container, the penalty is payable by the owner of the container."

Sec. 42. G.S. 105-449.120(a) reads as rewritten:

"(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~~ file a ~~report~~ return required by this Article.

(3) Willfully fails to pay a tax when due under this Article. Failure to comply with a requirement of a supplier to remit tax payable to the supplier by electronic funds transfer is considered a failure to make a timely payment.

(3a) Willfully fails to pay to a destination state tax collected on behalf of that state when due.

(4) Makes a false statement in an application, a ~~report,~~ return, 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.

(11) Willfully refuses to allow a licensed distributor, a licensed exporter, or a licensed importer to defer payment of tax to the supplier, as required by G.S. 105-449.91."

(12) Willfully refuses to allow a licensed distributor or a licensed importer to take the discount allowed by G.S. 105-449.93 when remitting tax to the supplier."

Sec. 43. G.S. 105-449.121(a) reads as rewritten:

"(a) What Must Be Kept. -- A person who is ~~required to submit a report or file a return under Part 4 of this Article~~ subject to audit under subsection (b) of this section must keep a record of all shipping documents or other documents used to determine ~~the information provided in the report or return.~~ information the person provides in a return or to determine the person's motor fuel transactions. The records must be kept for three years from the due date of the ~~report or~~ return to which the records ~~apply.~~ apply or, if the records apply to a transaction not required to be reported in a return, for three years from the date of the transaction."

Sec. 44. G.S. 105-449.130 reads as rewritten:

"**§ 105-449.130. Definitions.**

The following definitions apply in this Article:

(1) Alternative fuel. -- A combustible gas or liquid that can be used to generate power to operate a highway vehicle and that is not subject to tax under Article 36C of this Chapter.

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

~~(2)~~ (3) Highway. -- Defined in G.S. 20-4.01(13).

~~(3)~~ (4) Highway vehicle. -- Defined in G.S. 105-449.60.

~~(4)~~ (5) Motor fuel. -- Defined in G.S. 105-449.60.

~~(5)~~ (6) Motor fuel rate. -- Defined in G.S. 105-449.60.

(7) Provider of alternative fuel. -- A person who does one or more of the following:

a. Acquires alternative fuel for sale or delivery to a bulk-end user or a retailer.

b. Maintains storage facilities for alternative fuel, part or all of which the the person uses or sells to someone other than a bulk-end user or a retailer to operate a highway vehicle.

c. Sells alternative fuel and uses part of the fuel acquired for sale to operate a highway vehicle by means of a fuel supply line from

the cargo tank of the vehicle to the engine of the vehicle.

d. Imports alternative fuel to this State, by a means other than the usual tank or receptacle connected with the engine of a highway vehicle, for use by that person to operate a highway vehicle.

(8) Retailer. -- A person who maintains storage facilities for alternative fuel and who sells the fuel at retail or dispenses the fuel at a retail location to operate a highway vehicle."

Sec. 45. G.S. 105-449.131 reads as rewritten:

"**§ 105-449.131. List of persons who must have 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 provider of alternative fuel.

(2) A bulk-end ~~user of alternative fuel that uses part or all of the fuel in a highway vehicle.~~ user.

(3) A ~~retailer of alternative fuel that sells part or all of the fuel for use in a highway vehicle.~~ retailer."

Sec. 46. G.S. 105-449.134 reads as rewritten:

"**§ 105-449.134. Denial or cancellation of license.**

The Secretary may deny an application for a license or cancel a license under this Article for the same reasons that the Secretary ~~can~~ may deny an application for a license or cancel a license under Article 36C of this Chapter. The procedure in Article 36C for cancelling a license applies to the cancellation of a license under this Article."

Sec. 47. G.S. 105-449.136 reads as rewritten:

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

A tax at the motor fuel rate is imposed on liquid alternative fuel used to operate a highway vehicle by means of a vehicle supply tank that stores fuel only for the purpose of supplying fuel to operate the vehicle. A tax at the equivalent of the motor fuel rate is imposed on all other alternative fuel used to operate a highway vehicle. The Secretary must determine the equivalent rate. The exemptions from the tax on motor fuel in G.S. 105-449.88(2), (3), and (4) apply to the tax imposed by this section. The refunds for motor fuel tax allowed by Part 5 of Article 36C of this Chapter apply to the tax imposed by this ~~section.~~ section, except that the refund allowed by G.S. 105-449.107(b) for certain vehicles that use power takeoffs does not

apply to a vehicle whose use of alternative fuel is taxed on the basis of miles driven. The proceeds of the tax imposed by this section must be allocated in accordance with G.S. 105-449.125."

Sec. 48. G.S. 105-449.138 reads as rewritten:

"**§ 105-449.138. Requirements for bulk-end users and retailers.**

(a) ~~Reports.~~ Informational Return. -- A bulk-end user ~~of alternative fuel that uses part or all of the fuel in a highway vehicle~~ and a retailer ~~of alternative fuel that sells part or all of the fuel for use in a highway vehicle~~ must file a quarterly ~~report~~ informational return with the Secretary. A quarterly ~~report~~ return covers a calendar quarter and is due by the last day of the month that follows the quarter covered by the ~~report.~~ return.

The ~~report~~ return must give the following information and any other information required by the Secretary:

(1) The amount of alternative fuel received during the quarter.

(2) The amount of alternative fuel sold or used during the quarter.

(b) Storage. -- A storage facility used by a bulk-end user ~~of alternative fuel~~ or a retailer ~~of alternative fuel~~ must be marked in a manner similar to that required for diesel fuel by G.S. 105-449.87(c) if the alternative fuel stored in the facility is to be used for a purpose other than to operate a highway vehicle."

Sec. 49. G.S. 105-449.139 is amended by adding the following subsection to read:

"(c) Lists. -- The Secretary must give a list of licensed alternative fuel providers to each licensed bulk-end user and licensed retailer. The Secretary must also give a list of licensed bulk-end users and licensed retailers to each licensed alternative fuel provider. A list must state the name, account number, and business address of each license holder on the list. The Secretary must send an annual update of a list to each license holder, as appropriate."

Sec. 50. G.S. 105-449.57 reads as rewritten:

"**§ 105-449.57. Cooperative agreements between ~~states.~~ jurisdictions.**

The Secretary may enter into cooperative agreements with other ~~states~~ jurisdictions for exchange of information in administering the tax imposed by this Article. No agreement, arrangement, declaration, or amendment to an agreement is effective until stated in writing and approved by the Secretary.

An agreement may provide for determining the base state for motor carriers, records requirements, audit procedures, exchange

of information, persons eligible for tax licensing, defining qualified motor vehicles, determining if bonding is required, specifying reporting requirements and periods, including defining uniform penalty and interest rates for late reporting, determining methods for collecting and forwarding of gasoline or other motor fuel taxes and penalties to another jurisdiction, and such other provisions as will facilitate the administration of the agreement.

In accordance with G.S. 105-259, the Secretary may, as required by the terms of an agreement, forward to officials of another ~~state~~ jurisdiction any information in the Department's possession relative to the use of gasoline or other motor fuels by any motor carrier. The Secretary may disclose to officials of another ~~state~~ jurisdiction the location of offices, motor vehicles, and other real and personal property of motor carriers.

An agreement may provide for each ~~state~~ jurisdiction to audit the records of motor carriers based in the ~~state~~ jurisdiction to determine if the gasoline or other motor fuel taxes due each ~~state~~ jurisdiction are properly reported and paid. Each ~~state~~ jurisdiction shall forward the findings of the audits performed on motor carriers based in the ~~state~~ jurisdiction to each ~~state~~ jurisdiction in which the carrier has taxable use of gasoline or other motor fuels. For motor carriers not based in this State who have taxable use of gasoline or other motor fuels in this State, the Secretary may utilize the audit findings received from another ~~state~~ jurisdiction as the basis upon which to propose assessments of gasoline or other motor fuel taxes against the carrier as though the audit had been conducted by the Secretary. Penalties and interest shall be assessed at the rates provided in the agreement.

No agreement entered into pursuant to this section may preclude the Department from auditing the records of any motor carrier covered by this Chapter.

The provisions of Article 9 of this Chapter apply to any assessment or order made under this section.

The Secretary may not enter into any agreement that would increase or decrease taxes and fees imposed under Subchapter V of Chapter 105 of the General Statutes, and any provision to the contrary is void."

Sec. 51. G.S. 105-236(10) is amended by adding a new subpart to read:

"c. For failure to file an informational return required by Article 36C or 36D of this Chapter by the date the return is due, there shall be

assessed as a tax a penalty of fifty dollars ($50.00)."

Sec. 52. G.S. 105-253(b) reads as rewritten:

"(b) Each responsible corporate officer is personally and individually liable for all of the following:

(1) All sales and use taxes collected by a corporation upon taxable transactions of the corporation.

(2) All sales and use taxes due upon taxable transactions of the corporation but upon which the corporation failed to collect the tax, but only if the responsible officer knew, or in the exercise of reasonable care should have known, that the tax was not being collected.

(3) All taxes due from the corporation pursuant to the provisions of Article ~~36 and Article 36A~~ 36C and 36D of Subchapter V of this ~~Chapter.~~ Chapter and all taxes payable under those Articles by the corporation to a supplier for remittance to this State or another state.

The liability of the responsible corporate officer is satisfied upon timely remittance of the tax ~~to the Secretary~~ by the corporation. If the tax remains unpaid by the corporation after it is due and payable, the Secretary may assess the tax against, and collect the tax from, any responsible corporate officer in accordance with the procedures in this Article for assessing and collecting tax from a taxpayer. As used in this section, the term 'responsible corporate officer' includes the president and the treasurer of the corporation and any other officers assigned the duty of filing tax returns and remitting taxes ~~to the Secretary~~ on behalf of the corporation. Any penalties that may be imposed under G.S. 105-236 and that apply to a deficiency shall apply to any assessment made under this section. The provisions of this Article apply to an assessment made under this section to the extent they are not inconsistent with this section.

The period of limitations for assessing a responsible corporate officer for unpaid taxes under this section shall expire one year after the expiration of the period of limitations for assessment against the corporation."

Sec. 53. G.S. 119-15 reads as rewritten:

"**§ 119-15. Definitions that apply to Article.**

The following definitions apply in this Article:

(1) Alternative fuel. -- Defined in G.S. 105-449.130.

(2) Gasoline. -- Defined in G.S. 105-449.60.

(3) 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.

(4) Kerosene distributor. -- A person who acquires kerosene from any of the following for subsequent sale:

a. A supplier licensed under Part 2 of Article 36C of Chapter 105 of the General Statutes.

b. A kerosene supplier.

c. Another kerosene distributor.

(5) Kerosene supplier. -- A person who is not required to be licensed as a supplier under Part 2 of Article 36C of Chapter 105 of the General Statutes and who maintains storage facilities for kerosene to be used to fuel an airplane.

~~(4)~~ (6) Motor fuel. -- Defined in G.S. 105-449.60.

~~(5)~~ (7) Person. -- Defined in G.S. 105-229.90."

Sec. 54. G.S. 119-16.2 reads as rewritten:

"**§ 119-16.2. Application for license.**

(a) When Required. -- A person may not engage in business as a kerosene ~~distributor~~ supplier unless the person ~~is licensed as a supplier or a distributor under Part 2 of Article 36C of Chapter 105 of the General Statutes or~~ has a kerosene supplier license issued under this section. A kerosene distributor is required to have a kerosene distributor license only if the distributor imports kerosene. Other kerosene distributors may elect to have a kerosene distributor license. A licensed kerosene distributor that buys kerosene from a supplier licensed under Part 2 of Article 36C of Chapter 105 of the General Statutes has the right to defer payment of the inspection tax until the supplier is required to remit the tax to this State or another State. A licensed kerosene distributor that pays the tax due a supplier licensed under that Part by the date the supplier must pay the tax to the State may deduct from the amount due a discount in the amount set in G.S. 105-449.93.

(b) Application. -- 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 Part 2 of Article 36C of Chapter 105 of the General

Statutes if the applicant were applying for a license under that Part.

(c) General. -- 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 Part 2 of Article 36C of Chapter 105 of the General Statutes, and is subject to the same restrictions as a license issued under that Part. A person who fails to comply with this section is guilty of a Class 1 misdemeanor."

Sec. 55. 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, motor fuel, and alternative fuel.~~ of the following fuel, regardless of whether the fuel is exempt from the per-gallon excise tax imposed by Article 36C or 36D of Chapter 105 of the General Statutes:

(1) Motor fuel that is not dyed diesel fuel.
(2) Dyed diesel fuel used to operate a highway vehicle.
(3) Alternative fuel used to operate a highway vehicle
(4) Kerosene.

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 Article 36C of Chapter 105 of the General Statutes. The inspection tax on alternative fuel is due and payable to the Secretary of Revenue at the same time that the excise tax on alternative fuel is due and payable under Article 36D 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.~~ supplier that is licensed under Part 2 of Article 36C of Chapter 105 of the General Statutes and by a kerosene supplier. A monthly report ~~by a distributor required to be licensed under G.S. 119-16.2~~ is due by the ~~20th~~ 22nd of each month and applies to kerosene sold during the preceding month by a supplier licensed under that Part and to kerosene received during the preceding month by ~~the distributor during the preceding month.~~ a kerosene supplier."

Sec. 56. The following sections in Article 3 of Chapter 119 of the General Statutes are repealed:

G.S. 119-40	Manufacturers to notify Commissioner of shipments.
G.S. 119-41	Persons engaged in transporting are subject to inspection laws.

G.S. 119-44	Registration of exclusive industrial users of napthas and coal tar solvents.

Sec. 57. Sections 21 and 32 of this act become effective July 1, 1997. The remaining sections of this act become effective July 1, 1996.

TAX AT RACK FINE TUNING

I. IMPORTER AND EXPORTER CHANGES

1.1 Clarifies the licensing requirements for importing and exporting motor fuel.

An exporter license is optional, but any licensed exporter gets deferred payment and the ability to pay at the rate of the destination state.

A separate importer license is not required if the person is licensed as a distributor and buys only from an elective or a permissive supplier.

1.2 Clarifies that a licensed importer that buys fuel from an out-of-state elective or permissive supplier gets deferred payment and the discount.

1.3 Allows exports to be sold without collecting the destination state tax if the use in the destination state is exempt.

1.4 Clarifies that destination state taxes collected by North Carolina suppliers are payable either to the destination state or the Secretary of Revenue by the due date set under the destination state law.

1.5 Authorizes an out-of-state bulk end user to export fuel in specified circumstances.

II. BLENDER AND ETHANOL CHANGES

2.1 Clarifies that the tax on fuel grade ethanol parallels the tax on other gasoline and is payable by the highest person in the distribution chain. In most cases, that person is a fuel alcohol provider - a supplier by definition.

2.2 Requires a blender to post a bond if the blender's average expected annual tax liability is at least $2,000.

III. ALTERNATIVE FUEL CHANGES

3.1 Clarifies the definition of alternative fuel provider by including use by the provider and eliminating those who provide alternative fuel for a non-highway use, such as home heating.

3.2 Makes a clarifying change to the alternative fuel refunds for vehicles that use power take offs.

TAX AT RACK FINE TUNING (Continued)

3.3 Requires the Secretary to provide lists of licensed alternative fuel providers, licensed bulk-end users and licensed retailers.

IV. INSPECTION TAX CHANGES

4.1 Makes the timing of payment of the inspection tax parallel that for motor fuel.

4.2 Eliminates need for kerosene distributor license in most circumstances.

V. PENALTY CHANGES

5.1 Imposes liability on a person who accepts delivery of fuel when the shipping document for the fuel shows a different destination state for the fuel. The person is jointly and severally liable for any tax due on the fuel.

5.2 Adds as Class 1 misdemeanors and, by operation of -449.76, as grounds for revoking a license the willful failure by a supplier to pay destination state tax, the failure by a supplier to allow the "float", and the failure by a supplier to allow the "discount".

5.3 Adds a civil penalty for refusal to allow a sample of motor fuel to be taken.

5.4 Adds a penalty payable by a terminal operator when the operator has unaccounted for losses of motor fuel at the terminal; the penalty equals the amount of tax due on the unaccounted for fuel.

5.5 Changes the penalty for failure to comply with the destination state shipping document requirement from a variable rate based on the amount of fuel shipped to a flat rate that is equivalent to the amount now due on a full load.

5.6 Adds a $50 penalty for failure to file a motor fuel informational return.

5.7 Clarifies when officers of motor fuel corporations can be held liable for unpaid motor fuel taxes.

VI. OTHER MOTOR FUEL CHANGES

6.1 Authorizes the Secretary to deny a motor fuel license to a person whose motor fuel license issued by another state was revoked.

6.2 Adds a definition of in-state-only supplier and tax for clarification. Suppliers are one of three types - elective, permissive, or in-state only. The tax definition makes it clear that the term includes all charges imposed on a per gallon basis. This has significance for destination state taxes in states that impose environmental fees on motor fuel that are disguised excise taxes.

6.3 Clarifies that refunds of the total motor fuel tax are net of any discount already allowed.

6.4 Imposes a tax on unauthorized behind-the-rack transfers in the same circumstances in which a federal tax is imposed.

VII. REPORTING CHANGES

7.1 Requires the Secretary to give appropriate lists of license holders to other license holders to enable them to report transactions using the correct name and account number.

7.2 Conforms the information required on a supplier's return to that requested on the forms.

7.3 Requires all returns to state names and account numbers.

7.4 Clarifies that everyone who can be audited must keep appropriate records.

7.5 Requires distributors to file quarterly reconciling returns of exempt sales even if the amount reported to a supplier and the amount actually sold are the same, so that Revenue will know who purchased exempt fuel.

FISCAL REPORT
FISCAL RESEARCH DIVISION
April 12, 1996

Proposal # 9: Tax at the Rack Fine Tuning

Background:
The 1995 General Assembly passed Senate bill 943, introduced by Senator Kerr, to "address motor fuel tax evasion and to improve the administration of the motor fuel taxes by changing the point of taxation of gasoline and diesel fuel". The bill moved the point of taxation up the distribution chain to the "rack" at the motor fuel terminal. This method of taxation greatly reduces the number of taxpayers and parallels the federal system.

Summary:
This proposed bill fine tunes the 1995 tax at rack legislation.

Effective Date:
July 1, 1996

Fiscal Effect:
No fiscal impact to the Highway Fund or Highway Trust Fund.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

LEGISLATIVE PROPOSAL 10
95-LJ-27(1.2)
(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)

Short Title: Limit Franchise Add-Back For Debt. (Public)

Sponsors: Representatives Shaw, Blue, Cansler, Capps, Church, Neely, Robinson, and Shubert.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO DELETE THE REQUIREMENT THAT A COMPANY ADD BACK TO ITS NET WORTH FRANCHISE TAX BASE THE AMOUNT OF ITS LOANS THAT ARE PAYABLE TO AN UNRELATED COMPANY BUT ARE ENDORSED OR GUARANTEED BY A RELATED COMPANY, AS RECOMMENDED BY THE DEPARTMENT OF REVENUE.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-122(b) reads as rewritten:

"(b) Every such corporation taxed under this section shall determine the total amount of its issued and outstanding capital stock, surplus and undivided profits; no reservation or allocation from surplus or undivided profits shall be allowed other than for definite and accrued legal liabilities, except as herein provided; taxes accrued, dividends declared and reserves for depreciation of tangible assets as permitted for income tax purposes shall be treated as deductible liabilities. There shall also be treated as a deductible liability reserves for the entire cost of any air-cleaning device or sewage or waste treatment plant, including waste lagoons, and pollution abatement equipment purchased or constructed and installed which reduces the amount of air or water pollution resulting from the emission of air contaminants or the discharge of sewage and industrial wastes or

other polluting materials or substances into the outdoor atmosphere or streams, lakes, or rivers, upon condition that the corporation claiming such deductible liability shall furnish to the Secretary a certificate from the Department of Environment, Health, and Natural Resources or from a local air pollution control program for air-cleaning devices located in an area where the Environmental Management Commission has certified a local air pollution control program pursuant to G.S. 143-215.112 certifying that the Environmental Management Commission or local air pollution control program has found as a fact that the air-cleaning device, waste treatment plant or pollution abatement equipment purchased or constructed and installed as above described has actually been constructed and installed and that such plant or equipment complies with the requirements of the Environmental Management Commission or local air pollution control program with respect to such devices, plants or equipment, that such device, plant or equipment is being effectively operated in accordance with the terms and conditions set forth in the permit, certificate of approval, or other document of approval issued by the Environmental Management Commission or local air pollution control program and that the primary purpose thereof is to reduce air or water pollution resulting from the emission of air contaminants or the discharge of sewage and waste and not merely incidental to other purposes and functions. The cost of purchasing and installing equipment or constructing facilities for the purpose of recycling or resource recovering of or from solid waste or for the purpose of reducing the volume of hazardous waste generated shall be treated as deductible for the purposes of this section upon condition that the corporation claiming such deductible liability shall furnish to the Secretary a certificate from the Department of Environment, Health, and Natural Resources certifying that the Department of Environment, Health, and Natural Resources has found as a fact that the equipment or facility has actually been purchased, installed or constructed, that it is in conformance with all rules and regulations of the Department of Environment, Health, and Natural Resources, and the recycling or resource recovering is the primary purpose of the facility or equipment. The cost of constructing facilities of any private or public utility built for the purpose of providing sewer service to residential and outlying areas shall be treated as deductible for the purposes of this section; the deductible liability allowed by this section shall apply only with respect to such pollution abatement plants or equipment constructed or installed on or

after January 1, 1955. Treasury stock shall not be considered in computing the capital stock, surplus and undivided profits as the basis for franchise tax, but shall be excluded proportionately from said capital stock, surplus and undivided profits as the case may be upon the basis and to the extent of the cost thereof. In the case of an international banking facility, the capital base shall be reduced by the excess of the amount as of the end of the taxable year of all assets of an international banking facility which are employed outside the United States over liabilities of the international banking facility owed to foreign persons. For purposes of such reduction, foreign persons shall have the same meaning as defined in G.S. 105-130.5(b)(13)d.

Every corporation doing business in this State which is a parent, subsidiary, or affiliate of another corporation shall add to its capital stock, surplus and undivided profits all indebtedness owed to ~~or endorsed or guaranteed by~~ a parent, subsidiary or affiliated corporation as a part of its capital used in its business and as a part of the base for franchise tax under this section. The term "indebtedness" as used in this paragraph ~~shall include~~ includes all loans, credits, goods, ~~supplies~~ supplies, or other capital of whatsoever nature furnished by a parent, subsidiary, or affiliated ~~corporation.~~ corporation, other than indebtedness endorsed, guaranteed, or otherwise supported by one of these corporations. The terms "parent," "subsidiary," and "affiliate" as used in this paragraph shall have the meaning specified in G.S. 105-130.6. If any part of the capital of the creditor corporation is capital borrowed from a source other than a parent, subsidiary or affiliate, the debtor corporation, which is required under this paragraph to include in its tax base the amount of debt by reason of being a parent, subsidiary, or affiliate of the said creditor corporation, may deduct from the debt thus included a proportionate part determined on the basis of the ratio of such borrowed capital as above specified of the creditor corporation to the total assets of the said creditor corporation. Further, in case the creditor corporation as above specified is also taxable under the provisions of this section, such creditor corporation shall be allowed to deduct from the total of its capital, surplus and undivided profits the amount of any debt owed to it by a parent, subsidiary or affiliated corporation to the extent that such debt has been included in the tax base of said parent, subsidiary or affiliated debtor corporation reporting for taxation under the provisions of this section."

Sec. 2. This act is effective for taxable years beginning on or after October 1, 1996.

Explanation: Limit Franchise Add-Back For Debt

Under current law, a corporation that is a parent, a subsidiary, or an affiliate of another corporation is required to add back to its net worth franchise tax base the amount of any debt it has that is payable to its parent, affiliate, or subsidiary or is endorsed or guaranteed by its parent, affiliate, or subsidiary. Debt that is not payable to a parent, affiliate, or subsidiary and is not guaranteed by one of these corporations is not required to be added back to the base. This proposal deletes the requirement that debt endorsed or guaranteed by a related company be added back and retains the requirement that debt payable to a related company be added back. The change is effective for taxable years beginning on or after October 1, 1996. The change is made at the recommendation of the Department of Revenue and is expected to have a negligible fiscal impact.

The Department recommended this change because of the difficulty of enforcing it and the lack of need for the requirement. The existence of endorsed or guaranteed debt is often not readily ascertainable from the financial statements of a corporation. When a corporation endorses or guarantees a debt, it makes no accounting entry, such as the creation of a liability, to acknowledge the endorsement or guarantee. If the amount of debt endorsed or guaranteed is significant, the existence of the debt will be reflected in a footnote of the financial statements.

The franchise tax is a tax on corporations for the right or privilege to exist as a corporate entity and, in the case of foreign corporations, the right or privilege to do business in a corporate capacity in North Carolina. The tax is levied on the assets of a corporation. The tax rate is $1.50 per $1,000 with a minimum of $35.

The franchise tax base on which the tax is computed is the largest of the following:

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

(2) 55% of appraised property tax value of all taxable personal property

(3) The corporation's actual investment in tangible property in North Carolina.

The add-back requirement is imposed to prevent related companies from understating their net worth through means of transactions with each other. A corporation can make capital available to another corporation in several ways. For

example, it can buy the corporation's stock or loan the corporation money. The stock purchase would be reflected in the net worth of the company but the debt would be a deduction in computing net worth. To establish the economic reality between the companies, the loan is required to be added back so that it is in effect treated the same as the stock purchase.

Under current law, endorsed or guaranteed debt is required to be added back also even though the corporation making the endorsement or guarantee did not decrease its capital to increase that of the corporation receiving the loan. Endorsed or guaranteed debt is more like third-party debt than a loan from one company to another.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

LEGISLATIVE PROPOSAL 11
95-LC-301(2.1)
(THIS IS A DRAFT AND NOT READY FOR INTRODUCTION)

Short Title: Extend Corporate Loss Carryforward. (Public)

Sponsors: Representatives Neely, Blue, Cansler, Capps, Church, Robinson, Shaw, and Shubert.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO EXTEND THE CORPORATE INCOME TAX CARRYFORWARD FOR NET ECONOMIC LOSSES FROM FIVE YEARS TO FIFTEEN YEARS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-130.8 reads as rewritten:

"**§ 105-130.8. Net economic loss.**

Net economic losses sustained by a corporation in any or all of the ~~five~~ fifteen preceding income years shall be allowed as a deduction to ~~such~~ the corporation subject to the following limitations:

(1) The purpose in allowing the deduction of a net economic loss of a prior year ~~or years~~ is ~~that of granting~~ to grant some measure of relief to the corporation ~~which~~ that has incurred economic misfortune or ~~which~~ is otherwise materially affected by strict adherence to the annual accounting rule in the determination of net income. The deduction ~~herein specified~~ allowed in this section does not authorize the carrying forward of any particular items or category of loss except to the extent that ~~such loss or losses shall result~~ the loss results in the impairment of the net

economic situation of the corporation so as to result in a net economic loss as ~~hereinafter defined.~~ defined in this section.

(2) The net economic loss for any year ~~shall mean~~ means the amount by which allowable deductions for the year other than prior year losses ~~shall~~ exceed income from all sources in the year including any income not taxable under this Division.

(3) Any net economic loss of ~~a prior year or~~ prior years brought forward and claimed as a deduction in any income year may be deducted from net income of the year only to the extent that ~~such~~ the carry-over loss from the prior ~~year or~~ years ~~shall exceed~~ exceeds any income not taxable under this Division received in the same year in which the deduction is claimed, except that in the case of a corporation required to allocate and apportion to North Carolina its net income, ~~as defined in this Division,~~ only ~~such~~ that proportionate part of the net economic loss of a prior year shall be deductible from total income allocable to this State as would be determined by the use of the allocation and apportionment provisions of G.S. 105-130.4 for the year of ~~such~~ the loss.

(4) A net economic loss carried forward from any year shall first be applied to, or offset by, any income taxable or nontaxable of the next succeeding year before any portion of ~~such~~ the loss may be carried forward to a succeeding year.

(5) For purposes of this section, any income item deductible in determining State net income under the provisions of G.S. 105-130.5 and any nonbusiness income not allocable to this State under the provisions of G.S. 105-130.4 shall be considered as income not taxable under this Division.

(6) No loss shall either directly or indirectly be carried forward more than ~~five~~ fifteen years.

(7) A corporation claiming a deduction for a loss for the current year or carried forward from a prior year shall maintain and make available for inspection by the Secretary all records necessary to determine and verify the amount of the deduction. The burden of proving eligibility for

the deduction and the amount of the deduction shall rest upon the corporation, and no deduction shall be allowed to a corporation that fails to maintain adequate records or to make them available for inspection."

Sec. 2. G.S. 105-130.5(b)(4) reads as rewritten:

"(4) Losses in the nature of net economic losses sustained by the corporation in any or all of the ~~five~~ fifteen preceding years pursuant to the provisions of G.S. 105-130.8. ~~Provided, a~~ A corporation required to allocate and apportion its net income under the provisions of G.S. 105-130.4 shall deduct its allocable net economic loss only from total income allocable to this State pursuant to the provisions of G.S. 105-130.8."

Sec. 3. This act is effective for taxable years beginning on or after January 1, 1996, and applies to losses incurred for taxable years beginning on or after January 1, 1990.

Explanation - Extend Corporate Loss Carryforward

Legislative Proposal 11 would extend the corporate income tax carryforward for net economic loss deductions from five years to fifteen years. Fifteen years is the carryforward period for the similar net operating loss deduction under the Internal Revenue Code. Because it may be difficult for an auditor to substantiate a loss carryforward based on deductions that are ten to fifteen years old, the proposal clarifies that the corporation has the burden of maintaining records that verify the amount of the loss deduction claimed. The proposal would become effective for taxable years beginning on or after January 1, 1996, and would apply to losses incurred for taxable years beginning on or after January 1, 1990.

A net economic loss is the amount by which a corporation's deductions for a taxable year exceed its income from all sources, including income not taxable by the State. Income not taxable includes income items that are deductible in determining State net income as well as a multi-state corporation's nonbusiness income that is allocable to another state. G.S. 105-130.8 allows a corporation to carry a net economic loss forward and deduct it in the next five succeeding taxable years, but only to the extent the carried forward loss exceeds the amount of any income not taxable for each succeeding year. If the corporation is a multi-state corporation, it may deduct from income allocable to this State only that percentage of the carried forward loss that corresponds to the percentage of the corporation's income allocated and apportioned to this State.

The State's net economic loss provision is apparently based on a similar provision that was in the 1939 Internal Revenue Code. The State originally allowed a two-year carryforward; the carryforward period was extended to five years in 1957.

Even if the carryforward period is extended to match the fifteen-year period provided in the Internal Revenue Code, the State calculation will differ from the federal calculation in a number of respects. The Internal Revenue Code of 1954 changed the federal net economic loss deduction to a net operating loss calculation based primarily on revenues and expenditures affecting taxable income. Some limitations and restrictions have evolved in the ensuing years relating to continuity of corporate ownership, corporate equity, successor corporations, and other situations. Of course, under federal law, it is not necessary to address the state income tax issues regarding

multi-state corporations whose income is allocable to more than one state. Finally, under federal law, a corporation may elect to carry the federal net operating loss deduction back for three earlier years as well as forward for fifteen years.

Fiscal Report
Fiscal Research Division
April 12, 1996

Proposal # 11: Extend Corporate Loss Carryforward

Summary:
This act extends the corporate income tax carry forward for net economic losses from 5 years to 15 years.

Effective Date:
Effective for taxable years beginning on or after January 1, 1996, and applies to losses incurred on or after that date.

Fiscal Effect:
The Department of Revenue's Tax Research Division estimates this change in the corporate income tax will produce a $5 to $10 million loss in the General Fund. The estimate cannot be more precise due to the volatility of corporate taxable income and due to the Department's lack of information on "expired" losses.

Using 1990 corporate returns, the Department found 8,764 of the 39,165 non-taxable returns were non-taxable due to net economic loss (NEL) carry-overs. Corporations used the NEL carry-over to offset $424.2 million in taxable income, but had $1.2 billion left for the following years. The other 30,401 non-taxable corporations used current operating losses to offset taxable income. These corporations had $7.4 billion unexpended NEL carry-overs for use in future years.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H D

LEGISLATIVE PROPOSAL 12
96-RLRB-11
THIS IS A DRAFT 26-APR-96 10:20:43

Short Title: Expand Interstate Audit Division. (Public)

Sponsors: Representatives Neely, Blue, Cansler, Capps, Church, Robinson, Shaw, and Shubert.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO ENHANCE COMPLIANCE AND ENFORCEMENT OF EXISTING TAX LAWS BY APPROPRIATING FUNDS TO EXPAND THE NUMBER OF AUDITORS AND SUPPORT PERSONNEL IN THE INTERSTATE AUDIT DIVISION OF THE DEPARTMENT OF REVENUE.

The General Assembly of North Carolina enacts:

Section 1. There is appropriated from the General Fund to the Department of Revenue the sum of one million eighty-five thousand six hundred ten dollars ($1,085,610) for the 1996-97 fiscal year for 15 additional auditors in the Interstate Audit Division, five support personnel, and other costs resulting from the additional tax enforcement personnel.

Sec. 2. This act is effective upon ratification.

Explanation - Expand Interstate Audit Division

Legislative Proposal 12 would enhance enforcement and compliance of existing tax laws by increasing the number of auditors in the Interstate Audit Division of the Department of Revenue. The bill appropriates $1,085,610 for the fiscal year 1996-97 to the Department of Revenue to be used to hire 15 additional auditors in the Interstate Audit Division and to hire five new support personnel. Of this amount, $913,035 is recurring expenditures and $172,575 is nonrecurring expenditures for computer equipment and office furnishings.

After an initial training period of approximately one year, the Department estimates that these auditors will generate a minimum of $20 million annually in new, additional revenues. The Interstate Audit Division averages annual assessments of $2 million per auditor. Of this amount, the Department collects close to 75%, so the projected $30 million in assessments by the 15 auditors should yield $22.5 million in new, additional revenues per year. In the short term, for the 1996-97 fiscal year, the Division believes the 15 new auditors would assess a total of $15 million in new tax revenues for the State, resulting in collections of approximately $11.25 million. Also, as additional audits are performed, future revenues will increase due to improved compliance.

Fiscal Research Division
April 23, 1996

Proposal #12: Additional Audit Staff

Explanation:

New personnel is requested to increase revenue collections and enhance efficiency in the Interstate Audit Division and in divisions with collateral workloads that will experience an increase.

Effective Date:

July 1, 1996.

Fiscal Effect:

First year estimate supports recurring costs of salaries, benefits, and supplies; and non-recurring costs for computer equipment and office furnishings.

The annual estimates of continued expense include a 2% increase in salaries, only.

Interstate Audit Division

- Auditing Personnel (15 Positions)

  Since 1990 the in Department of Revenue has lost 31 field audit positions, resulting in a reduction in personnel from 181 to 150. The majority of the positions (128) are located in the State's fourteen (14) field offices. The remaining twenty-two (22) auditors are assigned to the Interstate Audit Division with twelve (12) auditors located in Raleigh and ten (10) in satellite offices operating in eight (8) states. The focus of auditors in this division is on industrial, global and service Fortune 500 companies. Assessments in the Interstate Division average $2 million annually per auditor with average expenses per auditor of $64,000. During the first year of service (FY 96-97), the new audit staff will be phased-in with 5 positions effective October 1, 1996, 5 positions effective November 1, 1996, and the remaining 5 positions effective December 1, 1996. This will allow the department time to advertise and recruit the 15 positions. It is anticipated that the 15 new auditors will gross $10,000,000 in assessments in the first year. An estimated 75% of all audit assessments are collected, which provides a yield in collections of $7,500,000. The expectation is that 15 new Interstate Auditors will produce approximately $30 million annually in additional assessments, thus the 15 new audit positions should contribute approximately $22.5 million in new tax revenue annually in subsequent years.

- Support Personnel (2 positions)

  The Tax Technician positions will support new and existing auditing staff to allow concentration more on conducting audits, and less time on research, refund claims and other administrative responsibilities.

- Department Wide (3 positions)
  The additional assessments will create collateral workload within other divisions. Two (2) clerical positions will assist the Accounting Division manage an expanded workload, and an Administrative Officer with the Corporate Tax Division will allow improved responses to Corporate tax inquiries; and protests, etc.

	FY 96-97	FY 97-98	FY 98-99	FY 99-00	FY 00-01
REVENUES					
GENERAL FUND:	**7,500,000**	**22,500,000**	**22,500,000**	**22,500,000**	**22,500,000**
HIGHWAY FUND					
HIGHWAY TRUST FUND					
LOCAL					
EXPENDITURES					
Recurring	**913,035**	**1,140,619**	**1,157,132**	**1,173,970**	**1,191,151**
Non-Recurring	**172,575**				
POSITIONS:	**20**	**20**	**20**	**20**	**20**

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

S D

LEGISLATIVE PROPOSAL 13
95-LCX-282(1.1)
(THIS IS A DRAFT AND NOT READY FOR INTRODUCTION)

Short Title: Revenue Laws Technical Changes. (Public)

Sponsors: Senators Cochrane, Cooper, Kerr, and Soles.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO MAKE TECHNICAL AND CONFORMING CHANGES TO THE REVENUE LAWS AND RELATED STATUTES.

The General Assembly of North Carolina enacts:

Section 1. G.S. 105-53(i2) reads as rewritten:

"(i2) Affidavit in Lieu of Records. -- The merchant may satisfy the record requirement of subsection (i1) of this section by producing, in lieu of a receipt or invoice, an affidavit under oath or affirmation identifying the source of the merchandise for which a record is requested, including the name and address of the seller, the license number of any auctioneer seller, and the date and place of purchase of the merchandise."

Sec. 2. G.S. 105-113.45(c) reads as rewritten:

"(c) Liquid Base Products. -- An excise tax at the rate of seventy-five cents (75¢) a gallon is levied on each individual container of a liquid base product. The tax applies regardless whether the liquid base product is diverted to and used for a purpose other than making a soft drink."

Sec. 3. G.S. 105-117 and G.S. 105-118 are repealed.

Sec. 4. G.S. 105-164.13(2a) reads as rewritten:

"(2a) Any of the following when purchased for use ~~in the commercial production of animals or plants, as~~

~~appropriate:~~ on animals or plants, as appropriate, held or produced for commercial purposes:

a. Remedies, vaccines, medications, litter materials, and feeds for animals.

b. Rodenticides, insecticides, herbicides, fungicides, and pesticides.

c. Defoliants for use on cotton or other crops.

d. Plant growth inhibitors, regulators, or stimulators, including systemic and contact or other sucker control agents for tobacco and other crops."

Sec. 5. G.S. 105-164.13(29a) is repealed.

Sec. 6. G.S. 105-164.14(c)(2a) reads as rewritten:

"(2a) A consolidated city-county ~~created pursuant to Article 2 or Article 5 of Chapter 160B of the General Statutes.~~ as defined in G.S. 160B-2."

Sec. 7. G.S. 105-191 and G.S. 105-196 are repealed.

Sec. 8. G.S. 105-197 reads as rewritten:

"**§ 105-197. When return required; due date of tax and return.**

Anyone who, during the calendar year, gives to a donee a gift of a future interest or one or more gifts whose total value exceeds the amount of the annual exclusion set in G.S. 105-188(d) must file a gift tax return, under oath or affirmation, with the Secretary ~~of Revenue~~ on a form prescribed by the Secretary. ~~A return~~ The tax is due on ~~or before~~ April 15th following the end of the calendar year. A return must be filed on or before the due date of the tax. A taxpayer may ask the Secretary of Revenue for an extension of time for filing a return under G.S. 105-263."

Sec. 9. G.S. 105-229 is repealed.

Sec. 10. G.S. 105-236 reads as rewritten:

"**§ 105-236. Penalties.**

Except as otherwise provided ~~in this Subchapter,~~ by law, and subject to the provisions of G.S. 105-237, the following penalties shall be applicable:

(1) Penalty for Bad Checks. -- When the bank upon which any uncertified check tendered to the Department of Revenue in payment of any obligation due to the Department returns the check because of insufficient funds or the nonexistence of an account of the drawer, an additional tax equal to ten percent (10%) of the check shall be imposed, subject to a minimum of one dollar ($1.00) and a maximum of one thousand dollars ($1,000). This penalty does not apply if the Secretary ~~of Revenue~~

finds that, when the check was presented for payment, the drawer of the check had sufficient funds in an account at a financial institution in this State to pay the check and, by ~~inadvertance,~~ inadvertence, the drawer of the check failed to draw the check on the account that had sufficient funds. The additional tax imposed may not be waived or diminished by the ~~Secretary of Revenue. This subsection applies to all taxes levied or assessed by the State.~~ Secretary.

(1a) Penalty for Bad Electronic Funds Transfer. -- When an electronic funds transfer cannot be completed due to insufficient funds or the nonexistence of an account of the transferor, the Secretary shall assess a penalty equal to ten percent (10%) of the amount of the transfer, subject to a minimum of one dollar ($1.00) and a maximum of one thousand dollars ($1,000). ~~This subdivision applies to all taxes levied or assessed by the State.~~ This penalty may be waived by the Secretary in accordance with G.S. 105-237.

(1b) Making Payment in Wrong Form. -- For making a payment of tax in a form other than the form required by the Secretary pursuant to G.S. 105-241(a), the Secretary shall assess a penalty equal to five percent (5%) of the amount of the tax, subject to a minimum of one dollar ($1.00) and a maximum of one thousand dollars ($1,000). This penalty may be waived by the Secretary in accordance with G.S. 105-237.

(2) Failure to Obtain a License. -- For failure to obtain a license before engaging in a business, trade or profession for which a license is required, there shall be assessed an additional tax equal to five percent (5%) of the amount prescribed for ~~such~~ the license per month or fraction thereof until paid, which additional tax shall not exceed twenty-five percent (25%) of the amount so prescribed, but in any event shall not be less than five dollars ($5.00).

(3) Failure to File Return. -- In case of failure to file any return ~~required under this Subchapter~~ on the date prescribed therefor (determined with regard to any extension of time for filing), unless

it is shown that ~~such~~ the failure is due to reasonable cause, there shall be added to the amount required to be shown as tax on ~~such~~ the return, as a penalty, five percent (5%) of the amount of ~~such~~ the tax if the failure is for not more than one month, with an additional five percent (5%) for each additional month, or fraction thereof, during which ~~such~~ the failure continues, not exceeding twenty-five percent (25%) in the aggregate, or five dollars ($5.00), whichever is the greater.

(4) Failure to Pay Tax When Due. -- In the case of failure to pay any tax when due, without intent to evade the tax, there shall be an additional tax, as a penalty, of ten percent (10%) of the tax; provided, that such penalty shall in no event be less than five dollars ($5.00).

(5) Negligence. --

a. Most cases. -- For negligent failure to comply with any of the provisions ~~of this Subchapter,~~ to which this Article applies, or rules ~~and regulations~~ issued pursuant thereto, 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.

b. Large income tax deficiency. -- 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.

c. Large sales tax deficiency. -- 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 reasons, the penalty assessed shall be twenty-five percent (25%) of the total deficiency:

~~a.~~ 1. Omission or understatement of gross sales, gross ~~receipts~~ receipts, or gross ~~purchases;~~ purchases.

~~b.~~ 2. Overstatement of exemptions or ~~deductions;~~ deductions.

~~c.~~ 3. 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.~~

d. No double penalty. -- 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.

(5a) Misuse of Certificate of Resale. -- For misuse of a certificate of resale by a purchaser, the Secretary shall assess an additional tax, as a penalty, of two hundred fifty dollars ($250.00).

(5b) Road Tax Understatement. -- If a motor carrier understates its liability for the road tax imposed by Article 36B of this Chapter by twenty-five percent (25%) or more, the Secretary shall assess the motor carrier a penalty in an amount equal to two times the amount of the deficiency.

(6) Fraud. -- If there is a deficiency or delinquency in payment of any ~~tax levied by this Subchapter, due to~~ tax because of fraud with intent to evade the tax, there shall be assessed, as a penalty, an additional tax equal to fifty percent (50%) of the total deficiency.

(7) Attempt to Evade or Defeat Tax. -- Any person who willfully attempts, or any person who aids or abets any person to attempt in any manner to evade or defeat ~~any tax imposed by this Subchapter of the General Statutes, or the payment thereof,~~ a tax or its payment, shall, in addition to other penalties provided by law, be guilty of a Class I felony which may include a fine up to twenty-five thousand dollars ($25,000).

(8) Willful Failure to Collect, Withhold, or Pay Over Tax. -- Any person required ~~under this Subchapter~~ to collect, withhold, account for, and pay over any tax ~~imposed by this Subchapter~~ who willfully fails to collect or truthfully account for and pay over ~~such~~ the tax shall, in addition to other penalties provided by law, be guilty of a Class 1 misdemeanor. Notwithstanding any other provision of law, no prosecution for a violation brought under this subdivision shall be barred before the expiration of three years after the date of the violation.

(9) Willful Failure to File Return, Supply Information, or Pay Tax. -- Any person required ~~under this Subchapter~~ to pay any tax, to make a return, to keep any records, or to supply any information, who willfully fails to pay ~~such~~ the tax, make ~~such~~ the return, keep ~~such~~ the records, or supply ~~such~~ the information, at the time or times required by law, or ~~regulations~~ rules issued pursuant thereto, shall, in addition to other penalties provided by law, be guilty of a Class 1 misdemeanor. Notwithstanding any other provision of law, no prosecution for a violation brought under this subdivision shall be barred before the expiration of three years after the date of the violation.

(9a) Aid or Assistance. -- Any person, pursuant to or in connection with the revenue laws, who willfully

aids, assists in, procures, counsels, or advises the preparation, presentation, or filing of a return, affidavit, claim, or any other document that ~~he~~ the person knows is fraudulent or false as to any material matter, whether or not the falsity or fraud is with the knowledge or consent of the person authorized or required to present or file the return, affidavit, claim, or other document, shall be guilty of a Class I felony which may include a fine up to ten thousand dollars ($10,000).

(10) Failure to File Informational Returns. --

a. For failure to file a partnership or a fiduciary informational return when ~~such returns are~~ the return is due to be filed, there shall be assessed as a tax against the delinquent five dollars ($5.00) per month or fraction thereof of ~~such~~ the delinquency, ~~such tax,~~ this penalty, however, in the aggregate not to exceed ~~the sum of~~ twenty-five dollars ($25.00). When assessed against a fiduciary, the ~~tax herein provided~~ penalty shall be paid by the fiduciary and shall not be passed on to the trust or estate. No tax may be assessed against the delinquent when it is a partnership as defined under Section 6231(a)(1)(B) of the Code and no penalty could be assessed as provided by Rev. Proc. 84-35, except that for the purpose of Section 3.01 of that procedure 'the Department of Revenue' is substituted for 'the Internal Revenue Service'.

b. For failure to file timely statements of payments to another person ~~or persons~~ with respect to wages, dividends, ~~rents~~ rents, or interest paid to ~~such other person or persons,~~ that person, there shall be assessed as a tax a penalty of one dollar ($1.00) for each statement not filed on time, the aggregate of ~~such~~ the penalties for each tax year not to exceed one hundred dollars ($100.00), and in addition thereto, if the Secretary ~~shall request~~ requests the ~~payor~~ payer to file ~~such~~ the statements and ~~shall set~~ sets a date ~~on or~~

~~before such statements shall~~ by which the statements must be filed, and the ~~payor shall fail to file such~~ payer fails to file the statements within ~~such~~ this time, the amounts claimed on ~~payor's~~ payer's income tax return as deductions for salaries and wages, or rents or interest shall be disallowed to the extent that the ~~payor~~ payer failed to comply with the Secretary's request with respect to ~~such~~ the statements.

(11) Any violation of Subchapter I, V, or VIII of this Chapter or of Article 3 of Chapter 119 of the General Statutes is considered an act committed in part at the office of the Secretary in Raleigh. The certificate of the Secretary that a tax has not been paid, a return has not been filed, or information has not been supplied, as required by law, is prima facie evidence that the tax has not been paid, the return has not been filed, or the information has not been supplied.

(12) Repealed by Session Laws 1991, c. 45, s. 27."

Sec. 11. G.S. 105-241.1(e) reads as rewritten:

"(e) Statute of Limitations. -- ~~The~~ There is no statute of limitations and 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. If a taxpayer elects under section 1033(a)(2)(A) of the Code not to recognize gain from involuntary conversion of property into

money, the Secretary must assess any tax due as a result of the conversion or election within the applicable period provided under section 1033(a)(2)(C) or section 1033(a)(2)(D) of the Code. If a taxpayer sells at a gain the taxpayer's principal residence, the Secretary must assess any tax due as a result of the sale within the period provided under section 1034(j) of the Code.

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. 12. G.S. 105-275(21) reads as rewritten:

"(21) The first thirty-eight thousand dollars ($38,000) in assessed value of housing together with the necessary land therefor, owned and used as a residence by a disabled veteran who receives benefits under ~~Title 38, section 801, United States Code Annotated.~~ 38 U.S.C. § 2101. This exclusion shall be the total amount of the exclusion applicable to such property."

Sec. 13. Effective July 1, 1996, G.S. 105-275.1(b) reads as rewritten:

"(b) Subsequent Distributions. -- As soon as practicable after January 1, 1990, the Secretary shall pay to each county and city the amount it received under subsection (a) in 1989 plus an amount equal to the county or city average rate multiplied by the value of the items described in subdivisions (ii) and (iii) of subsection (a) that were required to be listed and assessed as of January 1, 1987, and were listed on or before September 1, 1987, in the county or city, plus or minus the percentage of this product that equals 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. As soon as practicable after January 1, 1990, the Secretary shall also pay to each county and city an amount equal

to the average rate for each special district for which the county or city collected taxes in 1987, but whose tax rates were not included in the county or city's rates, multiplied by the value of the items described in subdivisions (ii) and (iii) of subsection (a) that were required to be listed and assessed as of January 1, 1987, and were listed on or before September 1, 1987, in the district, plus or minus the percentage of this product that equals 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. As soon as practicable after January 1, 1991, except as provided in subsection (f), the Secretary shall pay to each county and city the amount it received under this section the preceding year plus an amount equal to the county or city average rate multiplied by the value of the items described in subdivision (v) of subsection (a) contained in the list submitted by the county or city, plus or minus the percentage of this product that equals 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. As soon as practical after January 1, 1992, except as provided in subsection (f), the Secretary shall distribute to each county and city the amount it received under this section the preceding year. On or before April 30, 1993, except as provided in subsection (f), the Secretary shall distribute to each county and city ninety-nine and eighty-one one-hundredths percent (99.81%) of the amount it received under this section the preceding year. Thereafter, until August 1995, except as provided in subsection (f), on or before April 30 of each year, the Secretary shall distribute to each county and city the amount it received under this section the preceding year. On or before August 30, 1995, the Secretary shall determine for each county and city the amount it received in April 1995 under this section. ~~Beginning in August 1995 and each~~ Each year thereafter, except as provided in subsection (f), the Secretary shall distribute to each county and city ~~sixty percent (60%)~~ fifty percent (50%) of this amount on or before ~~August~~ September 30 and the remaining ~~forty percent (40%)~~ fifty percent (50%) on or before the following April 30.

Of the funds received by each county and city pursuant to this subsection in 1990, the portion that was received because the county or city was collecting taxes for a special district (either because the district's tax rate was included in the city

or county's rate or because the Secretary paid the county or city the product of the district's average rate and the value of the inventories and other items in the district) shall be distributed among the districts in the county or city as soon as practicable after the city or county receives the funds. The county or city shall distribute to each special district in the county or city the amount it distributed to the district in 1989 plus an amount equal to the average rate for the district multiplied by the value of the items, other than inventory, described in subdivisions (ii) and (iii) of subsection (a) that were required to be listed and assessed as of January 1, 1987, and were listed on or before September 1, 1987, in the district, plus or minus the percentage of this product that equals 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.

Each year thereafter, until August 1995, as soon as practicable after receiving funds under this subsection, every county and city shall distribute among the special districts for which the county or city collects tax an amount equal to the amount it distributed among such districts the previous year. Each year thereafter, ~~beginning in August 1995,~~ as soon as practical after receiving funds under this subsection in ~~August,~~ September, every county and city shall distribute among the special districts for which the county or city collects tax an amount equal to ~~sixty percent (60%)~~ fifty percent (50%) of the amount it distributed among such districts in April 1995, and as soon as practicable after receiving funds under this subsection in April, every county and city shall distribute among the special districts for which the county or city collects tax an amount equal to ~~forty percent (40%)~~ fifty percent (50%) of the amount it distributed among such districts in April 1995.

The Local Government Commission may adopt rules for the resolution of disputes and correction of errors in the distribution among special districts provided in this subsection. In addition, the Local Government Commission may adopt rules for the reallocation of funds when a special district is dissolved, merged, or consolidated, or when a special district ceases to levy tax, either temporarily or permanently."

Sec. 14. Effective July 1, 1996, G.S. 105-277A reads as rewritten:

"**§ 105-277A. Reimbursement for exclusion of retailers' and wholesalers' inventories.**

(a) Submission of Claims. -- On or before January 15, 1989, the governing body of each county and city shall furnish to the Secretary a list of all the inventories owned by retailers and wholesalers that were required to be listed and assessed as of January 1, 1987, and were listed on or before September 1, 1987, in the county or city under this Subchapter. The list shall contain the value of the inventories as well as the property tax rates in effect in the county or city for the eight years from 1980 through 1987. The list shall also contain the property tax rates in effect for those years in each special district for which the county or city collected taxes in 1987 but whose tax rates were not included in the rates listed for the county or city, and the value of the inventories owned by retailers and wholesalers that were required to be listed and assessed as of January 1, 1987, and were listed on or before September 1, 1987, in that district. The list shall be accompanied by an affidavit attesting to the accuracy of the list and shall be on a form prescribed by the Secretary.

The Secretary shall calculate an average rate for each county and city, and for each special district whose tax rates were not included in the tax rates of a county or city, as the arithmetic mean of the property tax rates in effect in the county, city, or district for the eight years from 1980 through 1987. If a county, city, or district did not have tax rates in effect for the entire eight-year period, the average rate shall be the arithmetic mean of the property rates in effect for the years during the eight-year period that it did have rates in effect.

(b) First Per Capita Distribution. -- As soon as practicable after January 1 of 1989, the Secretary shall distribute to each taxing unit the unit's per capita share of the sum of fifteen million seven hundred forty-five thousand dollars ($15,745,000). Thereafter, as soon as practicable after January 1 of 1990 and 1991, the Secretary shall distribute to each taxing unit the unit's per capita share of an amount equal to the sum distributed to all taxing units the previous year under this subsection plus or minus the product of the sum distributed the previous year 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.

On or before April 30 of 1992, 1993, 1994, and 1995, the Secretary shall distribute to each taxing unit the unit's per capita share of the sum that this subsection provided was to be distributed to all taxing units in 1991. Beginning August 1995

and each year thereafter, the Secretary shall determine for each taxing unit the unit's per capita share of the sum that this subsection provided was to be distributed to all taxing units in 1991. Each year, the Secretary shall distribute to each taxing unit ~~sixty percent (60%)~~ fifty percent (50%) of this share on or before ~~August~~ September 30 and the remaining ~~forty percent (40%)~~ fifty percent (50%) of this share on or before the following April 30.

To make the per capita distributions required by this subsection, the Secretary shall first allocate the sum to be distributed among the counties on a per capita basis. The Secretary shall then compute a per capita distributable amount for each county by dividing the amount allocated to a county by the total population of the county, plus the population of any incorporated towns and cities located in the county. Each taxing unit in a county, including the county itself, shall receive the product of the population of the taxing unit and the per capita distributable amount for that county.

A city or county that receives funds under this subsection and that collects taxes for another taxing unit shall distribute part of the taxes received by it to the taxing unit for which it collects tax. The distribution shall be made on the basis of the proportionate amount of ad valorem taxes levied, for the most recent fiscal year beginning July 1, by the city or county and by all the taxing units for which the city or county collects tax. This distribution shall be made as soon as practicable after a city or county receives funds from the State under this section.

(c) Second Per Capita Distribution. -- On or before March 20, 1989, the Secretary shall allocate to each county the county's per capita share of the sum of thirty-nine million dollars ($39,000,000).

Each year thereafter through April 1995, on or before April 30, the Secretary of Revenue shall allocate to each county the amount it received the previous year under this subsection. On or before August 30, 1995, the Secretary shall determine for each county the amount it received in April 1995 under this subsection. ~~Beginning in August 1995 and each~~ Each year thereafter, the Secretary shall distribute ~~sixty percent (60%)~~ fifty percent (50%) of this amount to each county on or before ~~August~~ September 30 and the remaining ~~forty percent (40%)~~ fifty percent (50%) to each county on or before the following April 30.

Amounts allocated to a county under this subsection shall in turn be divided and distributed between the county and the cities located in the county in proportion to the total amount of ad

valorem taxes levied by each during the fiscal year preceding the distribution. For the purposes of this section, the amount of the ad valorem taxes levied by a county or city shall include any ad valorem taxes collected by the county or city in behalf of a special district. For the purpose of computing the distribution 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 appropriate counties and cities, the Department shall use the latest property valuation of that public service company that has been certified.

The governing body of each county and city shall report to the Secretary of Revenue such information as he may request in order to make the distribution under this subsection. If a county or city fails to make a requested report within the time prescribed, the Secretary may disregard that county or city and the other taxing units in the county or city in making the distribution.

(c1) Claims-based Distribution. -- On or before March 20, 1989, the Secretary shall distribute to each county and city an amount equal to the amount by which the county or city's inventory loss, as defined in subsection (d) of this section, exceeds the amount of the reimbursement received by the county or city under subsection (c) of this section.

Except as provided in subsection (g) of this section, each year thereafter through April 1995, on or before April 30, the Secretary shall distribute to each county and city the amount it received the previous year under this subsection. On or before August 30, 1995, the Secretary shall determine for each county and city the amount it received in April 1995 under this subsection. ~~Beginning in August 1995 and each~~ Each year thereafter, the Secretary shall distribute ~~sixty percent (60%)~~ fifty percent (50%) of this amount to each county and city on or before ~~August~~ September 30 and the remaining ~~forty percent (40%)~~ fifty percent (50%) of this amount to each county and city on or before the following April 30.

(c2) Supplemental Distribution. -- On or before March 20, 1989, the Secretary shall determine, with respect to each county and city, whether the sum of (i) the amount the county or city received under subsection (c), plus (ii) the amount the county or city received under subsection (c1), plus (iii) three and four-tenths percent (3.4%) of the total distribution received by the county or city under G.S. 105-472, 105-486, 105-501, and Chapter 1096 of the 1967 Session Laws between January 1, 1988, and December 31, 1988, is less than ninety percent (90%) of the

amount of taxes the county or city actually levied on inventories owned by retailers and wholesalers for the 1987-88 tax year. If that sum is less than ninety percent (90%) of the amount of taxes the county or city actually levied on those inventories for the 1987-88 tax year, the Secretary shall distribute to that county or city a supplemental amount equal to the amount by which ninety percent (90%) of the taxes it actually levied on inventories owned by retailers and wholesalers for the 1987-88 tax year exceeds the total of subdivisions (i), (ii), and (iii).

Except as provided in subsection (g) of this section, each year thereafter through April 1995, on or before April 30, the Secretary shall distribute to each county and city the amount it received the previous year under this subsection. On or before August 30, 1995, the Secretary shall determine for each county and city the amount it received in April 1995 under this subsection. ~~Beginning in August 1995 and each~~ Each year thereafter, the Secretary shall distribute ~~sixty percent (60%)~~ fifty percent (50%) of this amount to each county and city on or before ~~August~~ September 30 and the remaining ~~forty percent (40%)~~ fifty percent (50%) of this amount to each county and city on or before the following April 30.

(c3) Distribution to Special Districts. -- Of the funds received by each county and city pursuant to subsections (c), (c1), and (c2) of this section, the portion that was received because the county or city was collecting taxes for a special district shall be distributed among the districts in the county or city in proportion to the amount of each special district's inventory levy, as defined in subsection (d) of this section, as soon as practicable after the city or county receives funds under this subsection. The Local Government Commission may adopt rules for the resolution of disputes and correction of errors in the distribution among special districts provided in this paragraph. In addition, the Local Government Commission may adopt rules for the reallocation of funds when a special district is dissolved, merged, or consolidated, or when a special district ceases to levy tax, either temporarily or permanently. ~~The Local Government Commission shall report to the 1990 General Assembly any errors it discovers in the information furnished by local governments to the Secretary as required in subsection (a) of this section.~~

(d) Definitions. -- The following definitions apply in this section:

(1) 'City' has the same meaning as in G.S. 153A-1(1).

(2) 'City's inventory loss' means the city's average rate multiplied by eighty percent (80%) of the value of the inventories reported to the Secretary under subsection (a) of this section by the city, plus the average rate for each special district for which the city collected taxes in 1987, but whose tax rates were not included in the city's rates, multiplied by eighty percent (80%) of the value of the inventories reported to the Secretary under subsection (a) of this section in behalf of the district, plus or minus the percentage of this amount that equals the lesser of five percent (5%) or 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, minus three and four-tenths percent (3.4%) of the total distribution received by the city under G.S. 105-472, 105-486, 105-501, and Chapter 1096 of the 1967 Session Laws between January 1, 1988, and December 31, 1988.

(3) 'County's inventory loss' means the county's average rate multiplied by eighty percent (80%) of the value of the inventories reported to the Secretary under subsection (a) of this section by the county, plus the average rate for each special district for which the county collected taxes in 1987, but whose tax rates were not included in the county's rates, multiplied by eighty percent (80%) of the value of the inventories reported to the Secretary under subsection (a) of this section in behalf of the district, plus or minus the percentage of this amount that equals the lesser of five percent (5%) or 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, minus three and four-tenths percent (3.4%) of the total distribution received by the county under G.S. 105-472, 105-486, 105-501, and Chapter 1096 of the

1967 Session Laws between January 1, 1988, and December 31, 1988.

(4) 'Special district's inventory levy' means the special district's average rate multiplied by eighty percent (80%) of the value of the inventories reported to the Secretary under subsection (a) of this section in behalf of the district.

(5) 'Taxing unit' means a unit that levied a property tax or for which another unit collected a property tax for the fiscal year preceding the fiscal year a distribution is made under this section.

(e) Population Estimates. -- In making the per capita calculations under this section, the Secretary shall use the most recent annual population estimates certified by the State Planning Officer.

(f) Source of Funds. -- To pay for the distribution required by this section and the cost of making the distribution, the Secretary shall draw from collections received under Division I of Article 4 of this Chapter an amount equal to the amount distributed and the cost of making the distribution.

(g) Correction of Errors. -- If the Secretary discovers that the amount or value of any inventories listed by a county or city pursuant to subsection (a) of this section was overstated or understated, the Secretary shall adjust the amount to be distributed under subsections (c1) and (c2) as follows. For the distribution to be made in the year following discovery of the overstatement or understatement, the Secretary shall distribute to the county or city the amount it would have received under subsections (c1) and (c2) in 1989 if it had not overstated or understated the amount or value of any inventories, plus the total amount it failed to receive in 1989 and subsequent years due to understatement of the amount or value of the inventories, or minus the total amount it received in 1989 and subsequent years due to overstatement of the amount or value of the inventories. Thereafter, each year the Secretary shall distribute to the county or city the amount it would have received under subsections (c1) and (c2) in 1989 if it had not overstated or understated the amount or value of any inventories."

Sec. 15. G.S. 105-278.7(a)(1) reads as rewritten:

"(1) Wholly and exclusively used by its owner for nonprofit educational, scientific, literary, or

charitable purposes as defined in subsection ~~(e),~~ (f), below; or".

Sec. 16. G.S. 105-282.1(a)(3) reads as rewritten:

"(3) After an owner of property entitled to exemption under G.S. 105-278.3, 105-278.4, 105-278.5, 105-278.6, 105-278.7, or 105-278.8 or exclusion under G.S. 105-275(3), (7), (8), (12), (17) through (19), (21) or (39), G.S. ~~105-277.1~~ 105-277.1, or G.S. 105-278 has applied for exemption or exclusion and the exemption or exclusion has been approved, the owner is not required to file an application in subsequent years except in the following circumstances:

a. New or additional property is acquired or improvements are added or removed, necessitating a change in the valuation of the property; or

b. There is a change in the use of the property or the qualifications or eligibility of the taxpayer necessitating a review of the exemption or exclusion."

Sec. 17. 105-277.2(4)a. reads as rewritten:

"a. A natural person. For the purpose of this section, a natural person who is an income beneficiary of a trust that owns land may elect to treat the person's beneficial share of the land as owned by that person. If the person's beneficial interest is not an identifiable share of land but can be established as a proportional interest in the trust income, the person's beneficial share of land is a percentage of the land owned by the trust that corresponds to the beneficiary's proportional interest in the trust income. For the purpose of this section, a natural person who is a member of a business ~~entity~~ entity, other than a corporation, that owns land may elect to treat the person's share of the land as owned by that person. The person's share is a percentage of the land owned by the business entity that corresponds to the person's percentage of ownership in the entity."

Sec. 18. G.S. 105-333 reads as rewritten:

"**§ 105-333. Definitions.**

~~When used~~ The following definitions apply in this Article unless the context requires a different meaning:

(1) ~~"Airline company" means a public service~~ Airline company. -- A company engaged in the business of transporting passengers and property by aircraft for hire within, into, or from this State.

(2) ~~"Bus line company" means a public service~~ Bus line company. -- A company engaged in the business of transporting passengers and property by motor vehicle for hire over the public highways of this State (but not including a bus line company operating primarily upon the public streets within a single local taxing unit), whether the transportation ~~be~~ is within, into, or from this State.

(3) ~~"Distributable system property" means all~~ Distributable system property. -- All real property and tangible and intangible personal property owned or used by a railroad company other than nondistributable system property.

(4) ~~"Electric membership corporation" means a public service~~ Electric membership corporation. -- A company ~~which is~~ organized, reorganized, or domesticated under ~~the provisions of~~ Chapter 117 of the General Statutes and ~~which is~~ engaged in the business of supplying electricity for light, heat, or power to consumers in this State.

(5) ~~"Electric power company" means a public service~~ Electric power company. -- A company engaged in the business of supplying electricity for light, heat, or power to consumers in this State.

(6) Repealed by Session Laws 1973, c. 783, s. 5.

(7) ~~"Flight equipment" means aircraft~~ Flight equipment. -- Aircraft fully equipped for flying and used in any operation within this State.

(8) ~~"Gas company" means a public service~~ Gas company. -- A company engaged in the business of supplying artificial or natural gas to, from, within, or through this State through pipe or tubing for light, heat, or power to consumers in this State.

(9) ~~"Locally assigned rolling stock" means rolling~~ Locally assigned rolling stock. -- Rolling stock that is owned or leased by a motor freight carrier company, specifically assigned to a terminal or other premises, and ~~is~~ regularly used at the premises to which assigned.

(10) ~~"Motor freight carrier company" means a~~ Motor freight carrier company. -- A company engaged in the business of transporting property by motor vehicle for hire over the public highways of this State as provided in this subdivision:

a. As to interstate carrier companies domiciled in North Carolina, this term includes carriers who regularly transport property by tractor trailer to or from one or more terminals owned or leased by the carrier outside this State or two or more terminals inside this State. For purposes of appraisal and allocation only, the term also includes a North Carolina interstate carrier that does not have a terminal outside this State but whose operations outside the State are sufficient to require the payment of ad valorem taxes on a portion of the value of the rolling stock of the carrier to taxing units in one or more other states.

b. As to interstate carrier companies domiciled outside this State, this term includes carriers who regularly transport property by tractor trailer to or from one or more terminals owned or leased by the carrier inside this State.

c. As to intrastate carrier companies, this term includes only those carriers that are engaged in the transportation of property by tractor trailer to or from two or more terminals owned or leased by the carrier in this State.

(11) ~~"Nondistributable system property" means the~~ Nondistributable system property. -- The following properties owned by a railroad company: ~~Land~~ land other than right-of-way, depots, machine shops, warehouses, office buildings, other structures, and the contents of the structures listed in this subdivision.

(12) ~~"Nonsystem property" means the~~ Nonsystem property. -- The real and tangible personal property owned by a public service company but not used in its public service activities.

(13) ~~"Pipeline company" means a public service~~ Pipeline company. -- A company engaged in the business of transporting natural gas, petroleum products, or

other products through pipelines to, from, within, or through this State, or having control of pipelines for such a purpose.

(14) ~~"Public service company" means~~ Public service company. -- A railroad company, a pipeline company, a gas company, an electric power company, an electric membership corporation, a telephone company, a telegraph company, a bus line company, an airline company, and any other company performing a public service that is regulated by the Interstate Commerce Commission, the Federal Power Commission, the Federal Communications Commission, the Federal Aviation Agency, or the North Carolina Utilities Commission, except that the term does not include a water company, a radio common carrier company as defined in G.S. 62-119(3), a cable television company, or a radio or television broadcasting company. The term also includes a motor freight carrier company. For purposes of appraisal under this Article, the term also includes a pipeline company whether or not it performs a public service and whether or not it is regulated by one of the regulatory agencies named in this subdivision.

(15) ~~"Railroad company" means a public service~~ Railroad company. -- A company engaged in the business of operating a railroad to, from, within or through this State on rights-of-way owned or leased by the company. It also means a company operating a passenger service on the lines of any railroad located wholly or partly in this State.

(16) ~~"Rolling stock" means motor~~ Rolling stock. -- Motor vehicles, railroad locomotives, and railroad cars that are propelled by mechanical or electrical power and used upon the highways or, in the case of railroad vehicles, upon tracks.

(17) ~~"System property" means the~~ System property. -- The real property and tangible and intangible personal property used by a public service company in its public service activities. ~~It also means~~ The term also includes public service company property under construction on the day as of which property is assessed which when completed will be used by the owner in its public service activities.

(18) ~~"Telegraph company" means a public service~~ Telegraph company. -- A company engaged in the business of transmitting telegraph messages to, from, within, or through the State.

(19) ~~"Telephone company" means a public service~~ Telephone company. -- A company engaged in the business of transmitting telephone messages and conversations to, from, within, or through this State.

(20) Repealed by Session Laws 1973, c. 783, s. 5."

Sec. 19. G.S. 58-6-25(d) reads as rewritten:

"(d) Use of Proceeds. -- The Insurance Regulatory Fund is created in the State treasury, under the control of the Office of State Budget and Management. The proceeds of the charge levied in this section and all fees collected under Articles 69 through 71 of this Chapter and under Articles 9 and 9C of Chapter 143 of the General Statutes shall be credited to the Fund. The Fund shall be placed in an interest-bearing account and any interest or other income derived from the Fund shall be credited to the Fund. Moneys in the Fund may be spent only pursuant to appropriation by the General Assembly and in accordance with the line item budget enacted by the General Assembly. The Fund is subject to the provisions of the Executive Budget Act, except that no unexpended surplus of the Fund shall revert to the General Fund. All money credited to the Fund shall be used to reimburse the General Fund for the following:

(1) Money appropriated to the Department of Insurance to pay its expenses incurred in regulating the insurance industry and other industries in this State.

(2) Money ~~money~~ appropriated to State agencies to pay the expenses incurred in regulating the insurance industry, in certifying statewide data processors under Article 11A of Chapter 131E of the General Statutes, and in purchasing reports of patient data from statewide data processors certified under that Article."

Sec. 20. G.S. 113-44.15(b) reads as rewritten:

"(b) ~~Beginning July 1, 1995, funds~~ Funds in the Trust Fund are annually appropriated to the North Carolina Parks and Recreation Authority and, unless otherwise specified by the General Assembly or the terms or conditions of a gift or grant, shall be allocated and used as follows:

(1) Sixty-five percent (65%) for the State Parks System for capital projects, repairs and renovations of park facilities, and land acquisition.
(2) Thirty percent (30%) to provide matching funds to local governmental units on a dollar-for-dollar basis for local park and recreation purposes. These funds shall be allocated by the North Carolina Parks and Recreation Authority based on criteria patterned after the Open Project Selection Process established for the Land and Water Conservation Fund administered by the National Park Service of the United States Department of the Interior.
(3) Five percent (5%) for the Coastal and Estuarine Water Beach Access Program.

Of the funds appropriated to the North Carolina Parks and Recreation Authority from the Trust Fund each year, no more than three percent (3%) may be used by the Department for operating expenses associated with managing capital improvements projects, acquiring land, and administration of local grants programs."

Sec. 21. G.S. 132-1.1(b) reads as rewritten:

"(b) State and Local Tax Information. -- Tax information may not be disclosed except as provided in G.S. ~~105-259, 153A-148.1, and 160A-208.1.~~ 105-259. As used in this subsection, 'tax information' has the same meaning as in G.S. 105-259. Local tax records that contain information about a taxpayer's income or receipts may not be disclosed except as provided in G.S. 153A-148.1 and G.S. 160A-208.1."

Sec. 22. (a) The text of G.S. 160B-3 is designated as subsection (a) and G.S. 160B-4(c) is recodified as G.S. 160B-3(b).

(b) G.S. 160B-3, as amended by this section, reads as rewritten:

"**§ 160B-3. Authority; ~~purpose of district.~~ purpose; administration.**

(a) The governing board may define any number of urban service districts in order to finance, provide or maintain for the districts services, facilities and functions in addition to or to a greater extent than those financed, ~~provided~~ provided, or maintained for the entire consolidated city-county.

(b) The powers, duties, functions, rights, privileges, and immunities of an urban service district shall be exercised or administered by the governing board of the consolidated city-county. Any revenues, ~~distributions~~ distributions, or other

funds due an urban service district shall be paid to the governing board of the consolidated city-county."

Sec. 23. (a) Section 4 of Chapter 991 of the 1983 Session Laws reads as rewritten:

"Sec. 4. District Established; Tax Levy. If a majority of the qualified voters voting in an election called under Section 1 of this act vote in favor of creating the Duck Area Beautification District and authorizing the levy and collection of an ad valorem tax in the district, the Dare County Board of Commissioners shall, upon receipt of a certified copy of the election results, adopt a resolution creating the Duck Area Beautification District and shall file a copy of the resolution with the clerk of superior court of Dare County. Upon establishing the Duck Area Beautification District, the Dare County Board of Commissioners may annually levy <u>on behalf of the district</u> an ad valorem tax on all taxable property in the district in an amount the board considers necessary to provide for the installation of underground power lines, not to exceed ten cents (10c) for each one hundred dollars ($100.00) taxable valuation of property. The proceeds of this tax shall be used only to provide for the underground installation of power lines in the district."

(b) Section 4 of Chapter 363 of the 1989 Session Laws reads as rewritten:

"Sec. 4. District Established; Tax Levy. If a majority of the qualified voters voting on an election called under Section 1 of this act vote in favor of creating the Outer Banks Beautification District and authorizing the levy and collection of an ad valorem tax in the district, the Dare County Board of Commissioners shall, upon receipt of a certified copy of the election results, adopt a resolution creating the Outer Banks Beautification District and shall file a copy of the resolution with the clerk of superior court of Dare County. Upon establishing the Outer Banks Beautification District, the Dare County Board of Commissioners may annually levy <u>on behalf of the district</u> an ad valorem tax on all taxable property in the district in an amount the board considers necessary to provide for the installation of underground utility lines and facilities, not to exceed five cents (5¢) for each one hundred dollars ($100.00) taxable valuation of property. The proceeds of this tax shall be used only to provide for the underground installation of utility lines and facilities in the district."

(c) Sections 1 through 5 of Chapter 400 of the 1989 Session Laws are repealed.

(d) Section 4 of Chapter 703 of the 1989 Session Laws reads as rewritten:

"Sec. 4. District Established; Tax Levy. If a majority of the qualified voters voting in an election called under Section 1 of this act vote in favor of creating the Coinjock Canals Area Beautification District and authorizing the levy and collection of an ad valorem tax in the district, the Currituck County Board of Commissioners shall, upon receipt of a certified copy of the election results, adopt a resolution creating the Coinjock Canals Area Beautification District and shall file a copy of the resolution with the clerk of superior court of Currituck County. Upon establishing the Coinjock Canals Area Beautification District, the Currituck County Board of Commissioners may annually levy on behalf of the district an ad valorem tax on all taxable property in the district in an amount the board considers necessary to provide for the installation of underground utility lines, not to exceed ten cents (10¢) for each one hundred dollars ($100.00) taxable valuation of property. The proceeds of this tax shall be used only to provide for the underground installation of utility lines in the district."

(e) Section 4 of Chapter 685 of the 1991 Session Laws reads as rewritten:

"Sec. 4. District Established; Tax Levy. If a majority of the qualified voters voting in an election called under Section 1 of this act vote in favor of creating the Poplar Tent Beautification District and authorizing the levy and collection of an ad valorem tax in the district, the Cabarrus County Board of Commissioners shall, upon receipt of a certified copy of the election results, adopt a resolution creating the Poplar Tent Beautification District and shall file a copy of the resolution with the clerk of the superior court of Cabarrus County. Upon establishing the Poplar Tent Beautification District, the Cabarrus County Board of Commissioners may annually levy on behalf of the district an ad valorem tax on all taxable property in the district in an amount the board considers necessary to develop and implement the beautification plan and projects described in Section 1 of this act, that amount not to exceed five cents (5¢) for each one hundred dollars ($100.00) taxable valuation of property. The proceeds of this tax shall be used only to develop and implement the beautification plan and projects described in Section 1 of this act."

Sec. 24. Except as otherwise provided in this act, this act is effective upon ratification.

Explanation - Revenue Laws Technical Changes

Legislative Proposal 13 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 caption to this subsection. The other subsections of this statute all have captions.
2	Returns to the statute words that were inadvertently deleted in 1995.
3	Repeals two obsolete statutes, imposing franchise taxes on pullman, sleeping, chair, and dining cars, and on express companies. Railroads pay general franchise and income taxes. There are no longer any express companies; if there were, they would pay the general franchise and income taxes.
4	Returns the term "held" to the statute. In 1995, this sales tax exemption was revised to clarify that aquaculture is covered. The statute applies to animals or plants produced or held for commercial purposes; the 1995 rewrite accidentally removed "held".
5	Repeals a provision that grants a sales tax exemption for works of art purchased pursuant to the art in State buildings program of Article 47A of Chapter 143B of the General Statutes. Because that program has been repealed, the sales tax exemption is no longer needed.
6	Corrects an incorrect citation.
7,8	Repeals obsolete administrative provisions in the gift tax provisions. These provisions have been superseded by Article 9 of Chapter 105 of the General Statutes. Article 9 of Chapter 105 contains the administrative provisions that apply to all taxes administered by the Secretary under that Chapter.
9	Repeals the penalty of $10 a day for failure to file a privilege license tax return or franchise tax return, which is obsolete and redundant. The general penalties that apply to all taxes already apply to these taxes.

Section	Explanation
10	Allows the Secretary of Revenue to assess a negligence penalty for reporting improper adjustments to federal taxable income to the same extent as for understating gross income or overstating deductions. In cases of substantial income tax deficiencies, a 25% penalty is assessed if the deficiency was 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. This section provides that the same penalty applies whether the deficiency resulted from understating gross income, overstating deductions, or misstating adjustments. This section also repeals references to "this subchapter," which are obsolete. The term "tax" is now defined to include not only taxes under Subchapter I of Chapter 105 of the General Statutes but also taxes under Subchapters V and VIII and inspection taxes levied under Article 3 of Chapter 119 of the General Statutes. Finally, this section corrects spelling errors and modernizes the language of the statute.
11	Reinstates an extended period of time for making assessments for income tax due attributable to gains from involuntary conversions or from the sale of a principal residence parallel to federal law. The extension is necessary because the law allows the taxpayer a period of time to replace the converted property or the principal residence with similar property and thereby avoid recognition of the gain. If the taxpayer fails to replace the property, gain is recognized and the assessment may be made within three years after the Secretary is notified that the requirements for nonrecognition will not be met. Before 1989, North Carolina's individual income tax contained a similar provision; when the tax law was rewritten to "piggyback" the federal internal revenue code, that provision was inadvertently not picked up.
12	Corrects a citation. The federal statute to which this language refers has been renumbered.
13, 14	Effective July 1, 1996, revises the split inventory tax reimbursement date from an August/April date to a September/April date and changes the 60%/40% split to a 50%/50% split. 1995-96 will be the only year in which the 60/40 August/April split reimbursement occurred. Because these

Section	Explanation
	sections become effective July 1, 1996, changing the 1995 languages does not affect the validity of what is being done in 1995-96.
15	Corrects an incorrect cross-reference.
16	Exempts certain property owners from filing annual applications for property tax exemptions. According to the Institute of Government, by administrative practice, annual applications are not required for exempt property of veterans' organizations, masonic lodges and shrines, elks and similar fraternal organizations, or disabled veterans. In addition, the Institute of Government suggests that there is no reason to require annual applications for exemption of pollution control and recycling equipment because the exemption is automatic once the Department of Environment, Health, and Natural Resources determines that the equipment qualifies.
17	Corrects an inadvertent expansion of the use value law. Legislation enacted in 1995 codified existing interpretations of the use value law that allow a partner in a partnership or a member of a limited liability company to treat their share of land owned by the entity as if they owned it directly. The legislation inadvertently included corporate-owned land under the same rule.
18	Removes redundant language that renders certain definitions circular. This section also modernizes the form in which the definitions are set out.
19	Restores omitted reference. Until 1995, funds in the Insurance Regulatory Fund could be used only to reimburse the General Fund for the Department of Insurance's expenses in regulating the insurance industry and other industries in this State. The statute was expanded in 1995 to include expenses of other State agencies in regulating the insurance industry and in carrying out certain duties under the Medical Care Data Act. The 1995 rewrite inadvertently omitted reference to other industries, in addition to insurance, that the Department of Insurance regulates. For example, the Department regulates bail bondsmen and collection agencies.
20	Removes an unnecessary reference to an effective date.
21	Existing law provides that certain local tax records are not public records; this section clarifies the corresponding provision under the Public Records Act.
22	Relocates a provision in the consolidated city-county act to the appropriate statute. The provision applies to all urban service districts but is currently located in a statute that applies only to certain urban service districts. A

Section	Explanation

consolidated city-county is a county in which the largest municipality has been abolished and its powers, duties, rights, privileges, and immunities have been consolidated with those of the county. Other municipalities may also be abolished and consolidated with the county. A consolidated city-county may define urban service districts to finance services within the county at a higher level than in other areas of the county. These urban service districts may replace municipalities that have been abolished or may be created to serve areas that have population density, property valuation, and needs that justify a higher level of services than is provided in the county generally.

23 Amends existing local acts establishing beautification districts to clarify that the districts are special districts established under Article VII of the North Carolina Constitution and not special tax areas governed by Section 2(4) of Article V of the North Carolina Constitution. The constitution permits local acts establishing special tax districts but not local acts establishing special tax areas. The following local acts authorize beautification districts:

(1) Dare County, Duck District: SL83-991, SL93-610, and SL95-303.

(2) Dare County, Outer Banks District: SL89-363.

(3) Currituck County, Currituck Outer Banks District: SL89-400 and SL95-446. The former citation appears to be obsolete.

(4) Currituck County, Coinjock Canals District: SL89-703.

(5) Cabarrus County, Poplar Tent: SL91-685.

24 Effective date.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

S **D**

LEGISLATIVE PROPOSAL 14
96-RLRB-10
THIS IS A DRAFT 26-APR-96 10:36:48

Short Title: Accounting for 911 Surcharges. (Public)

Sponsors: Senators Kerr, Cochrane, Cooper, and Soles.

Referred to:

A BILL TO BE ENTITLED

AN ACT TO REQUIRE LOCAL GOVERNMENTS TO ACCOUNT FOR 911 SURCHARGES IN THEIR ANNUAL FINANCIAL STATEMENTS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 62A-7 reads as rewritten:

"**§ 62A-7. Emergency Telephone System Fund.**

The fiscal officer to whom 911 charges are remitted under G.S. 62A-6 shall deposit the charges in a ~~separate, restricted fund.~~ special revenue fund pursuant to G.S. 159-26(b)(2). The Fund shall be known as the Emergency Telephone System Fund. The fiscal officer may invest money in the Fund in the same manner that other money of the local government may be invested. The fiscal officer shall deposit any income earned from such an investment in the Emergency Telephone System Fund."

Sec. 2. This act becomes effective July 1, 1996.

Explanation - Accounting for 911 Surcharges

Eighty-three counties in North Carolina impose a telephone surcharge on their residents to pay for a 911 Emergency Telephone Service. The General Assembly authorized local governments to establish telephone surcharges in 1989 as a way to pay for emergency telephone systems. Although the statute requires a local government to maintain the surcharge revenues in a separate account, it does not require the Fund revenue, expenditures, and ending balance to be shown in the annual financial statement. To better enable public examination of this revenue, Legislative Proposal 14 specifies that the revenues should be placed in a special revenue fund. By definition, budget activity in this type of fund is included in a local government's financial statement.

Upon adoption of a local ordinance, a local government may impose a monthly 911 service charge on each telephone subscriber. The 911 charges are collected by the phone company and remitted to the local government within ten days after the last day of the month, less 1% that is retained by the phone company to compensate it for its administrative expenses associated with collecting and remitting the charges. The local government deposits these charges into an Emergency Telephone System Fund. The money in the Fund may be invested, but all earnings remain in the Fund. The money in the Fund may be used only to pay for the lease, purchase, or maintenance of emergency telephone equipment and the rates associated with the service supplier's 911 service.

The 911 surcharges brought counties $19.3 million in fiscal year 1994-95. Based on financial statements for the fiscal year ending June 30, 1995, 50 counties reported positive fund balances with an average fund balance being $237,893. Sixteen cities also impose a surcharge on telephone subscribers to pay for a 911 service. These charges raised $1,737,738 in revenue for fiscal year 1994-95.

Based on a 1994 survey by the North Carolina chapter of the National Emergency Number Association, 99 counties in the State have a 911 system. The lone county without a system, Greene County, plans to have a system in place by 1997. Approximately half of the counties have an enhanced 911 system that directs calls to the appropriate public safety agencies based on geographic location of the caller and provides automatic number identification and automatic location of the caller.

APPENDIX A

GENERAL ASSEMBLY OF NORTH CAROLINA
1995 SESSION
RATIFIED BILL

CHAPTER 542
HOUSE BILL 898

AN ACT TO AUTHORIZE STUDIES BY THE LEGISLATIVE RESEARCH COMMISSION, TO CREATE AND CONTINUE VARIOUS COMMISSIONS, TO DIRECT STATE AGENCIES AND LEGISLATIVE OVERSIGHT COMMITTEES AND COMMISSIONS TO STUDY SPECIFIED ISSUES, TO MAKE VARIOUS STATUTORY CHANGES, AND TO MAKE TECHNICAL CORRECTIONS TO CHAPTER 507 OF THE 1995 SESSION LAWS.

The General Assembly of North Carolina enacts:

PART I.-----TITLE

Section 1. This act shall be known as "The Studies Act of 1995".

PART II.-----LEGISLATIVE RESEARCH COMMISSION

Sec. 2.1. The Legislative Research Commission may study the topics listed below. When applicable, the 1995 bill or resolution that originally proposed the issue or study and the name of the sponsor is listed. The Commission may consider the original bill or resolution in determining the nature, scope, and aspects of the study. The topics are:

(1) Atlantic States Marine Fisheries Compact withdrawal (H.B. 948 - Preston)
(2) Bad check fees (S.B. 876 - Ballance)
(3) Chiropractic care (S.J.R. 228 - Odom, Soles)
(4) Consolidation of regulatory agencies of financial institutions (H.B. 839 - Tallent)
(5) Consumer protection issues:
    a. Consumer protection (S.B. 59 - Jordan; H.B. 196 - Thompson)
    b. Rental property rights (S.B. 861 - Perdue)
(6) Domiciliary care and nursing homes (H.B. 685, H.B. 745 - Clary)
(7) Education issues:
    a. Education improvement (State grants and loans for community college tuition and fees, H.B. 42 - Warner)
    b. School building disposition (S.B. 60 - Jordan, Edwards; H.B. 78 - Wainwright)
    c. School funding (S.B. 1088 - Winner, Plexico)
    d. Ability grouping and tracking of students (S.B. 1004 - Martin, W.; H.B. 1051 - Cunningham)
    e. Teacher tenure, performance evaluation, and incentives (H.B. 210 - Arnold)

f. Choice in education (Shubert, Linney, Miller, K., Wood), including tuition tax credits (H.B. 954 - Wood)

(8) Election laws reform (S.B. 982 - Plexico; H.B. 922 - Cansler; H.B. 858 - Miner)

(9) Emergency medical services (S.J.R. 1045 - Speed)

(10) Energy conservation (S.J.R. 461 - Edwards; H.J.R. 275 - Brawley)

(11) Grandparent visitation rights (S.B. 841 - Forrester, Kerr, and Carpenter; H.J.R. 872 - Mitchell)

(12) Illegitimacy, its prevention, and related child support and welfare benefits issues (Basnight)

(13) Insurance and insurance-related issues:

a. Coastal insurance availability and affordability (S.J.R. 881 - Soles, Parnell)

b. Long-term care insurance (S.B. 102 - Parnell; H.B. 98 - Edwards)

c. Statewide flexible benefits program and third-party administrator contracts (Executive Order 66)

(14) Juvenile and family law (S.J.R. 381 - Cooper, Allran, Winner; H.J.R. 251 - Hensley, Rogers, Russell; H.J.R. 274 - Hackney)

(15) Lien laws (S.B. 434 - Hartsell, Soles, and Cooper)

(16) Mold Lien Act (H.B. 617 - McMahan)

(17) Occupational and professional regulation:

a. Fire Alarm Installers (Capps)

b. Forester licensing (Weatherly)

c. Qualified environmental professionals (H.B. 880 - Wood)

d. Psychology Practice Act (H.B. 452 - Lemmond)

(18) Property issues.

a. Property rights (H.B. 597 - Nichols)

b. Extraterritorial jurisdiction representation (H.J.R. 73 - Ellis)

c. Annexation laws (H.B. 660 - Pulley; H.B. 539 - Sherrill)

d. Condemnation by government entities, including the condemnation process, fair market value for property, payment of condemnees' attorneys' fees and court costs, and related matters (Allred)

(19) Revenue and tax issues:

a. Revenue laws (H.B. 246 - Gamble)

b. Interstate Tax Agreements (S.J.R. 122 - Webster)

c. Tax expenditures (H.J.R. 95 - Gamble, Luebke)

d. Nonprofit continuing care facilities property tax exemption (S.B. 980 - Plexico and Sherron)

e. Diesel Fuel Payment method (S.B. 797 - Hoyle; H. B. 975 - Barbee)

f. Taxation of business inventory donated to nonprofit organization (McMahan)

(20) State Personnel Issues, including needed revisions to the State Personnel Act (Morgan)

(21) State purchasing and Correction Enterprises (S.B. 420 - Kerr, Sherron; H.B. 302 - Warner)

(22) Water issues:

a. Water issues (S.B. 95 - Albertson; H.B. 46 - Ives)

b. Drinking water tests (H.B. 930 - Allred)

c. Water conservation measures to reduce consumption (Sherron)

Sec. 2.2. Executive Budget Act Revision (Morgan, Holmes, Gray). The Legislative Research Commission may study the Executive Budget Act and the budget process. The study may consider this State's and other states' laws and policies on the budget process and any other matters it considers necessary in order to recommend a complete revision of the Executive Budget Act and its policies. A study of these revisions shall specifically address the constitutional requirement of separation of powers as it relates to proposing, enacting, and executing a State budget and as it relates to the gubernatorial veto.

Sec. 2.3. Criminal Laws and Procedures; Sentencing (Neely, Odom, and Ballance). The Legislative Research Commission may study criminal laws and procedures, including criminal offenses, criminal penalties, criminal process and procedure, sentencing, and related matters.

Sec. 2.4. Downtown Revitalization (Brawley and Sherron). The Legislative Research Commission may study ways to encourage the development and use of downtown area structures. The use of these structures may include both commercial and residential uses in the same structure. To encourage the development of downtown area structures, the Legislative Research Commission study should evaluate the usefulness and cost-effectiveness of providing the following State and local incentives:

(1) Income tax credits.
(2) Reduced property tax liability through the use of exemptions, deferrals, or lower values.
(3) Zoning law modifications.
(4) Building code modifications.

Sec. 2.5. State and Federal Retirees (Rand, Perdue, Warren, Edwards, Grady, Morgan, Gray). The Legislative Research Commission may study North Carolina's tax treatment of the retirement benefits of State and federal government retirees residing in North Carolina, the potential need to make changes in the revenue laws of North Carolina relative to such benefits, and recommendations by which any alleged unconstitutional or inequitable tax treatment of retirement benefits might be redressed.

Sec. 2.6. Cape Fear River Basin (Shaw). The Legislative Research Commission may study the uses of the Cape Fear River Basin, including increased economic development, the use of hydroelectric power, recreational uses, and improving water quality for citizens of southeastern North Carolina.

Sec. 2.7. Workers' Compensation (S.J.R. 996 - Kerr). The Legislative Research Commission may study the effect of the assigned risk pool on small employers, the funding mechanisms of the Industrial Commission, workers' compensation premium tax, or any other matter raised by the Chairman or Advisory Panel of the Industrial Commission; provided, however, the Legislative Research Commission shall not study any matter contained in the original or any subsequent version of Senate Bill 906, the legislation that led to the Workers' Compensation Reform Act of 1994. The Commission may also study the issue of funding of workers' compensation for volunteer fire department and rescue squad members.

Sec. 2.8. Committee Membership. For each Legislative Research Commission committee created during the 1995-96 biennium, the cochairs of the Legislative Research Commission shall appoint the committee membership.

Sec. 2.9. 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 1996 Regular Session of the 1995 General Assembly, if approved by the cochairs, or the 1997 General Assembly, or both.

Sec. 2.10. 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. 2.11. 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.

PART III.------SENATE AND HOUSE STUDIES

Sec. 3.1. The President Pro Tempore of the Senate may direct a Senate standing committee or select committee to study the following issues:

(a) Campaign reform (S.B. 982 - Plexico).

(b) Travel and Tourism Division of Department of Commerce merger with the Division of Parks and Recreation of the Department of Environment, Health, and Natural Resources (S.J.R. 1050 - Sherron).

Sec. 3.2. The Speaker of the House of Representatives may direct a House standing committee, permanent standing subcommittee, or select committee to study the following:

(a) Issues involved in tort reform which were introduced in the 1995 Regular Session of the General Assembly but not enacted (Daughtry).

(b) The facilitation of greater cooperation between the public and nonprofit sectors and the fostering of growth of the nonprofit sector, including, but not limited to, a review of government funding of nonprofits through State agencies, allowing local governments to take measures to encourage philanthropy within their communities and the feasibility of privatization of services and programs through nonprofit organizations (McMahan).

Sec. 3.3. A standing committee, permanent subcommittee, or select committee may report pursuant to this Part to the 1996 Regular Session of the 1995 General Assembly with any recommended legislation.

PART IV.-----BLUE RIBBON STUDY COMMISSION ON AGRICULTURAL WASTE (S.B. 695 - Albertson; H.B. 524 - H. Hunter).

Sec. 4.1. The Blue Ribbon Study Commission on Agriculture Waste is created in the General Assembly. The Commission shall study the following issues:

(1) The effect of agriculture waste on groundwater, drinking water, and air quality and any other environmental impacts of agriculture waste.

(2) Methods of disposing of and managing agriculture waste currently in use in this State.

(3) Methods of disposing of and managing agriculture waste that have fewer adverse impacts than those methods currently in use in this State, including positive commercial and noncommercial uses of agriculture waste.

(4) The economic impact of agriculture waste in areas in this State where there is a high concentration of agriculture waste, including, but not limited to, the impact on property values of land adjacent to agriculture sites and on water treatment costs.

(5) Implementation of the recommendations contained in the Swine Odor Task Force reports by the Swine Farm Odor Abatement Study authorized by Section 45 of Chapter 561 of the 1993 Session Laws and any recommendations that result from the federally funded study of the potential for groundwater contamination from

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1995

H 1

HOUSE JOINT RESOLUTION 246

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

Referred to: Rules, Calendar and Operations of the House.

February 22, 1995

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 Regular Session of the 1995 General Assembly.

Sec. 4. This resolution is effective upon ratification.

APPENDIX B

REVENUE LAWS STUDY COMMITTEE
MEMBERSHIP
1995 - 1996

LRC Member: Sen. R.L. Martin
126 Nelson Street
PO Box 387
Bethel, NC 27812
(919) 825-4361

President Pro Tempore Appointments

Sen. John H. Kerr, III, Cochair
PO Box 1616
Goldsboro, NC 27533
(919) 734-1841

Sen. Betsy L. Cochrane
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APPENDIX C

1995 Tax Law Changes

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Chapter 4 (Senate Bill 13, Sen. Kerr)

AN ACT TO FURTHER REDUCE EMPLOYERS' UNEMPLOYMENT INSURANCE TAXES.

This act reduces unemployment insurance taxes, effective January 1, 1995, in the following ways:

(1) It lowers the taxable wage base for the tax by changing the formula used to compute the base. It reduces from 60% to 50% the percentage of annual average wages used to calculate the taxable wage base. This change reduces the 1995 wage base from 13,500 to 12,300. This tax reduction benefits all employers and will save existing employers as well as new businesses an estimated $36 to $40 million a year.

(2) It reduces the tax rates that apply to rated employers with a positive unemployment insurance account balance. This reduction is estimated to save employers about $15 million a year.

(3) It sets a zero tax rate for employers with credit ratios of 5.0 or over. Under current law, the lowest rate is 0.01%. This change is estimated to save employers about $130,000 a year.

Taken together, the changes cut unemployment insurance taxes by about 23% and save employers more than $51 million a year. Unemployment tax contributions are paid by employers on a quarterly basis and deposited into the State Unemployment Insurance Trust 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. Federal law prohibits transfer of or payment of refunds from money in the Trust Fund.

The General Assembly has reduced unemployment insurance taxes several times in recent years. In 1994, the General Assembly reduced the taxes by an average of 38% for rated employers with a positive credit balance and by 20% for employers who are not yet rated. 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.

In 1993, the General Assembly enacted legislation that reduced the unemployment tax 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 Trust Fund equals or exceeds $800,000,000 as of the preceding August 1. This percentage reduction in the tax rate was increased to 50% in the 1994 legislation as part of the tax rate reduction for employers who have a credit balance in their unemployment insurance tax account. In 1992, the General Assembly suspended an additional unemployment tax collected from employers and credited to the Employment Security Commission Reserve Fund, which bolsters the State Unemployment Insurance Trust Fund. Despite these cuts, the North Carolina Trust Fund in Washington, from which unemployment benefits are paid, is close to $1.5 billion.

Before enactment of the 1994 legislation, North Carolina's average unemployment tax rate, 0.5%, was already the 45th lowest in the nation. Since the enactment of the 1995 act, North Carolina's average unemployment tax rate is the lowest in the nation. The 1.8% starting rate for new employers is now the second lowest rate in the nation. The North Carolina average weekly benefit amount paid to claimants for unemployment benefits is the highest in the southeast at $171.41. North Carolina also pays the highest maximum weekly benefit amount in the southeast at $289.00.

Chapter 7 (House Bill 80, Rep. Tallent)

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

This act repeals the special use tax that was levied in 1957 on vehicles, machinery, tools, and other equipment brought into North Carolina for use in construction. The repeal became effective July 1, 1995. This act was recommended by the Revenue Laws Study Committee. The Department of Revenue suggested this issue as a study topic for the committee because the tax generated little revenue, was difficult for taxpayers to understand and comply with, was difficult to administer, and no longer served its original purpose of protecting North Carolina contractors from out-of-state competition. The repeal is expected to result in a General Fund revenue loss of no more than $20,000 a year.

The special use tax applied to contractors who do work in more than one state, purchase equipment in a state other than North Carolina for use in the other state, and then bring the equipment to this State for use in construction. The regular sales and use tax would not apply to this equipment because the equipment was not purchased in this State and was not purchased for use in this State. The special use tax rate for an item other than a motor vehicle was the regular use tax rate of 4% State and 2% local. The special use tax rate on a motor vehicle was the same as the highway use tax rate, which is 3% subject to the applicable maximums.

To compute the special use tax due on an item of equipment, a contractor had to multiply the sales price of the equipment by the percentage of the equipment's useful life that was expected to be spent in North Carolina. The contractor then had to apply the applicable special use tax rate and subtract as a credit the proportional amount of sales and use tax paid on the equipment in another state. When filing a return, the contractor had to list each piece of equipment separately, along with the equipment's original purchase price, the amount of sales and use tax paid when the equipment 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.

Until 1989, the special use tax did not allow a credit for taxes paid in 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 probably 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 special use tax credit for regular sales and use taxes paid to other states and to local governments in other states.

Of our neighboring states, Virginia, South Carolina, and Tennessee have similar special use taxes on construction equipment brought into the state. Georgia does not have a similar tax. The border states that have a similar special use tax allow a credit for regular sales and use taxes paid in another state. Repeal of North Carolina's special use tax will therefore not affect North Carolina companies doing business in the border

states; the companies will continue to receive credit for North Carolina sales and use taxes paid.

Chapter 17 (Senate Bill 104, Sen. Cochrane)

AN ACT TO MAKE TECHNICAL AND CLARIFYING CHANGES TO THE REVENUE LAWS AND RELATED STATUTES.

This act makes a number of unrelated technical and clarifying changes to various revenue statutes. The changes are described below by section:

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 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.

11.1 Gives a person who files an amended return after receiving a federal determination the same amount of time to ask for a refund that the Department of Revenue has to assess additional taxes. A federal determination is a change or correction made by the IRS to a federal tax that affects the person's liability for State income, gift, or withholding taxes. Last session, the General Assembly (in Chapter 582) revised and consolidated the provisions concerning assessments of tax following a federal determination and did not make a corresponding change to the statute of limitations for refunds.

11.2 Makes a conforming change to correspond to the change made by Section 11.1. The section deletes language in the statute that describes the procedure for claiming a refund that conflicts with the statute of limitations set in G.S. 105-266(c).

12 Adds a missing hyphen.

13 Restores a missing portion of a cross-reference.

13.1 Makes it clear that a motor carrier that operates in interstate, as opposed to intrastate, commerce must file a road tax report for each quarter whether or not the carrier drove in North Carolina during the quarter for which the report is due. The Department now requires these carriers to file quarterly reports but the statute can be construed as requiring them to file a report only if they drove in North Carolina during that quarter. When a motor carrier registers with the Department, the carrier must state on the application whether the carrier is an intrastate or an interstate carrier.

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 1¾¢ local option sales tax as an alternative to the 1¾¢ 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 sections of the act are effective upon ratification unless otherwise specified. Section 1 became effective July 1, 1995; Sections 5 and 9 became effective for taxable years beginning on or after January 1, 1995; and Section 11.1 and Section 18 became effective January 1, 1995. All other sections became effective March 23, 1995, the date of ratification.

Recommended by the Revenue Laws Study Committee.

Chapter 21 (Senate Bill 220, Sen. Martin of Pitt)

AN ACT TO PROVIDE COUNTIES WITH INFORMATION TO ENABLE THEM TO VERIFY CLAIMS FOR REFUNDS OF THEIR LOCAL SALES AND USE TAX.

This act gives counties access to information regarding local sales tax refunds paid to nonprofit corporations and governmental entities, beginning July 1, 1995. Under prior law, counties did not have access to this information because the local sales tax is collected by the State and the tax secrecy statute prevents the Department of Revenue from disclosing information about individual taxpayers. Without information about local sales tax refunds, counties were not able to audit claims for refunds against them. The counties had to rely on the Department of Revenue to audit the claims, but the Department does not have enough resources to provide the level of audit some counties wished to provide for themselves.

Under G.S. 105-164.14, nonprofit corporations and certain governmental entities may seek a refund of State and local sales taxes they pay on their purchases. To do so, these entities must file a written request for refund with the Department of Revenue and name the counties where the purchases were made. The Secretary of Revenue deducts the claimed refunds of local sales taxes from tax revenue distributed to the counties. Errors in identifying the correct county in refund claims occur because the local sales tax applies to the county in which the retailer is located, not the county in which the purchaser is located. Some counties believe that entities located in one county who pay sales tax to another county are claiming the refund against the county in which they are located, rather than against the county in which they made the purchase.

To obtain information concerning local sale tax refunds under this act, a county must request the information in writing from the Secretary of Revenue. The Secretary has 30 days to provide the chair of the board of county commissioners with a list of each nonprofit corporation or governmental entity that received a refund of at least $1,000 of that county's local taxes within the last 12 months. The county can then use this list to identify entities whose refund claims the county may wish to audit. Upon the

written request of the county, this act requires an entity that has received a refund to provide the county with a copy of the request for refund, along with supporting documentation requested by the county to verify the request. If an entity determines that a refund it has received has been charged to the wrong county, it must file an amended return for the refund. The amended return will enable the Department to make the appropriate adjustments in the subsequent quarterly distribution of local sales tax revenue.

This act specifies that the information disclosed to the county is not a public record and may not be disclosed except in accordance with G.S. 153A-148.1, which governs the disclosure of local tax records. Section 2 of the act amends the tax secrecy statute to allow the Department to furnish the county with the required tax refund information.

During the first year the act is in effect, the Department of Revenue will have 90 rather than 30 days to provide a county the requested information. This extra time is allowed because the Department will have to compile the information manually. After the first year, it is anticipated that the new Integrated Tax Administration System will enable the Department to compile the information electronically.

Chapter 41 (Senate Bill 8, Sen. Kerr)

AN ACT TO REPEAL THE INTANGIBLES TAX AND TO REIMBURSE LOCAL GOVERNMENTS FOR THEIR RESULTING REVENUE LOSS.

This act repeals the intangibles tax on stock, bonds, mutual funds, and accounts receivable effective for the 1995 tax year (taxes due April 15, 1996). The repeal will result in a tax reduction of $124 million a year for individuals and corporations. This act dedicates $93 million in recurring General Fund revenue for distribution to local governments annually to reimburse them for their revenue loss due to the repeal of the tax. A total of $95 million of State funds will be distributed to local governments for the intangibles tax because $2 million that was formerly deducted from the tax to pay for the Local Government Commission and similar local cost items will instead be deducted from local sales taxes distributed to local governments.

The intangibles tax was a State-levied property tax of 25¢ per $100 of value of stocks, bonds, notes, mutual funds, certain accounts receivable, and interests in foreign trusts. Accounts with investment brokers and securities dealers were exempt from the tax on accounts receivable. Until 1985, the tax applied also to cash on hand, money on deposit, and accounts with investment brokers and securities dealers. These portions of the tax were repealed in 1985; at that time, the General Assembly dedicated recurring General Fund revenues for distribution to local governments to reimburse them for their revenue loss due to the repeal. The amount of the reimbursement was indexed to grow automatically at the same rate as State personal income.

Before 1937, the intangibles tax was levied by local governments. It was converted in 1937 to a State-levied tax with 50% of the revenue to be shared with local governments. The local share was increased to 75% in 1941 and to 100% in 1957. In 1991, in order to balance the State budget, the Governor cut local governments' share of the tax and their reimbursement for the parts of the tax repealed in 1985. Later that year, the General Assembly restored this cut but froze the distribution and reimbursement amounts, so that the State would share in the tax revenue as it grew above the frozen amount. In 1993, the General Assembly enacted legislation that would have frozen the State's share of the tax and restored future growth to local governments beginning in 1995. That legislation never went into effect, however, because the tax was repealed by this act.

By 1995, the State's share was approximately $31 million and the local share was approximately $93 million. By dedicating State revenue to reimburse local governments for their share in future years, this act requires the State to absorb the entire $124 million loss from the General Fund. Because the reimbursement to local

governments is frozen and will not grow, local governments must absorb the loss of expected revenue growth that would have been restored to them in 1995 had the tax not been repealed.

The reimbursements enacted in 1985 and the new reimbursement provided in this act are allocated among the counties in proportion to the amount of tax collected in each county in the last year the tax that is being reimbursed was in effect. The amounts allocated are then divided among the county and its municipalities in proportion to the total amount of ad valorem taxes levied by each during the fiscal year preceding the distribution. The distributions will be made each August, beginning in 1995.

The repeal of the intangibles tax by this act was precipitated by litigation challenging the constitutionality of the tax on stocks and stock mutual funds. The stock tax statute exempted 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 did 100% of its business in North Carolina was 100% exempt from the intangibles tax. This exemption was known as the "taxable percentage" deduction. In 1993, in Fulton Corp. v. Justus, the North Carolina Court of Appeals ruled that the taxable percentage deduction violates the interstate commerce clause of the federal constitution. The court invalidated the deduction effective for the 1994 tax year but, before the decision could go into effect, it was overturned by the North Carolina Supreme Court in December 1994. The North Carolina Supreme Court agreed with the State's argument that the stock tax and the taxable percentage deduction are both constitutional. The case is now on appeal in the United States Supreme Court. The plaintiffs are arguing that the entire stock tax is unconstitutional and should be invalidated by the court. If the 1995 General Assembly had not repealed the tax, taxpayers, the State, and local governments would have remained uncertain as to whether the court's decision would prohibit collection of the stock tax for the 1995 tax year, authorize collection of the tax but prohibit allowance of the taxable percentage deduction for the 1995 tax year, or leave the entire stock tax structure in place.

Chapter 42 (House Bill 2, Rep. Daughtry)

AN ACT TO REDUCE INCOME TAXES FOR THE LOWER AND MIDDLE-INCOME PEOPLE OF NORTH CAROLINA BY INCREASING THE PERSONAL EXEMPTION DEDUCTION BY FIVE HUNDRED DOLLARS AND BY ALLOWING A TAX CREDIT OF SIXTY DOLLARS PER DEPENDENT CHILD.

This act, as amended by Chapter 370 of the 1995 Session Laws, provides income tax relief only to low and middle income taxpayers. The act will reduce the number of taxpayers by between 260,000 and 280,000 people. The tax relief provided by the act will result in a General Fund revenue loss of $235 million in fiscal year 1995-96 and $244.1 million in fiscal year 1996-97. The act makes the following changes in State individual income taxes:

(1) Increases each personal exemption the taxpayer may claim by $250 for the 1995 taxable year if the taxpayer has an adjusted gross income less than the applicable amount listed below:

Married filing jointly	$100,000
Head of Household	80,000
Single	60,000
Married filing separately	50,000

(2) Increases each personal exemption the taxpayers may claim by an additional $250 for the 1996 taxable year if the taxpayer has an adjusted gross income of less than the applicable amount stated above.

(3) Allows a tax credit of $60 per dependent child for taxpayers with adjusted gross incomes of less than the applicable amount stated above.

Increase in personal exemptions

Prior to this act, the State personal exemption amount of $2,000 had not been changed since 1989, when North Carolina began using federal taxable income as the starting point in calculating North Carolina taxable income. The State personal exemption is not indexed for inflation, as is the federal personal exemption. Therefore, to calculate North Carolina taxable income, a taxpayer must add back to federal taxable income the difference between the lower North Carolina personal exemption amount and the higher federal personal exemption amount.

The effect of this act is to require a lower amount to be added back each year for taxpayers whose adjusted gross income is less than the stated amounts. For the 1995 taxable year, the amount to be added back is $250 less than under the current law. For example, the federal personal exemption amount for the 1995 taxable year is $2,500. Under this act, the State personal exemption amount will be $2,250, rather than $2,000, for taxpayers whose adjusted gross income is less than the stated amounts. For taxpayers whose adjusted gross income is equal to or more than the stated amounts, the State personal exemption amount will remain at $2,000. For the 1996 taxable year and subsequent taxable years, the amount to be added back is $500 less than under the current law for taxpayers whose adjusted gross income is less than the stated amounts.

Credit for dependent children

The $60 tax credit for dependent children also applies only to taxpayers whose adjusted gross incomes are less than the stated amounts. The credit is in addition to the federal and state tax credits or exclusions for child care expenses. The new credit is allowed for each dependent child for whom the eligible taxpayer could take a federal personal exemption under section 151(c)(1)(B) of the Internal Revenue Code. That Code section allows an exemption for each dependent child who either is less than 19 years old at the end of the taxable year or is a student and is less than 24 years old at the end of the taxable year. A child is a son, stepson, daughter, or stepdaughter. A dependent child is a child over half of whose support was provided by the taxpayer.

Chapter 46 (Senate Bill 120, Sen. Kerr)

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

This act provides that capital gains from the transfer of all State, local, and federal bonds will be subject to uniform State income tax treatment; it does this by repealing special State tax exemptions for capital gains from transfers of certain State and local bonds. The act becomes effective July 1, 1995, and applies to bonds issued on or after that date. It does not affect the tax treatment of capital gains on bonds issued before July 1, 1995.

This act was recommended by the Revenue Laws Study Committee to address an inconsistency in the State income tax treatment of capital gains from various bonds. 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 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 federal 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 had the choice of

either repealing the special capital gains exemption for a limited number of bonds or granting a tax exemption for capital gains from all federal bonds and all North Carolina State and local bonds. The Revenue Laws Study Recommended the former option. Repealing the special exemption is expected to cause only a small revenue increase, 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. The other option, exempting the capital gain from all bonds, would have caused a General Fund revenue loss that was 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 was unknown due to a lack of data.

In addition to repealing the special capital gains exemption for a select group of State and local bonds, this act makes other two changes. First, it 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. Second, in Section 1, it 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.

This act is not expected to affect the marketability of State or local bonds, whether outstanding or issued in the future. The tax changes in the act do not apply to any bonds issued before July 1, 1995. Future issues of State and local bonds in the following categories will be subject to the same capital gains tax treatment as other 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

Chapter 50 (House Bill 122, Rep. Arnold)

AN ACT TO EXPAND THE ALLOWABLE USES OF TRANSPORTER PLATES, TO ALLOW OWNERS OF SALVAGE VEHICLES TO RETAIN TITLE TO THE VEHICLES, AND TO EXEMPT OUT-OF-STATE UTILITY VEHICLES THAT ARE USED IN CERTAIN EMERGENCY OPERATIONS FROM THE VEHICLE REGISTRATION AND ROAD TAX REQUIREMENTS.

This act makes several unrelated changes to the laws concerning motor vehicles. The changes expanding the allowable uses of transporter plates only for special mobile equipment and providing a highway use tax exemption and a reduced title fee for the

transfer of a salvage vehicle when the transfer was from an insurance company to the person who owned the vehicle when it became a salvage vehicle were recommended by the Revenue Laws Study Committee. The changes made by this act will reduce the Highway Trust Fund by approximately $171,600 a year and the Highway Fund by approximately $32,400 a year.

Transporter plate changes

The act allows transporter plates to be used on vehicles in two new circumstances. The first circumstance is to drive special mobile equipment from the manufacturer of the equipment to the facility of the special mobile equipment dealer, from one facility of the dealer to another, or from the dealer to the buyer of the equipment. The second circumstance is to move a motor vehicle that is owned by a business and is a replaced vehicle offered for sale; under current law only a utility may obtain a transporter plate to move a replaced motor vehicle. The changes are effective upon ratification.

A transporter plate is a type of commercial license plate. 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. The fee for a transporter plate is $10.

Under the law prior to the enactment of this act, a special mobile equipment dealer had to use a dealer plate to drive special mobile equipment on the highway. The number of dealer plates available to a dealer is based on the dealer's sales volume. A dealer in special mobile equipment might sell fewer than 12 pieces of special mobile equipment in a year, and based on that sales volume, may be entitled to only one dealer plate. This part of the act alleviates this problem by allowing the special mobile equipment dealer to use either transporter plates or dealer plates for the three limited transport purposes.

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.

Salvage vehicle changes

The act eliminates the double title transfer now required when a vehicle is wrecked to the extent it is a salvage vehicle and the owner wants to keep the vehicle. Under the prior law, the owner had to transfer the vehicle to the insurer and the insurer had to then transfer the vehicle back to the owner. A salvage vehicle is one on which a claim has been paid 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. In place of the double transfer, the act requires the owner of the salvage vehicle to sign a form acknowledging the status of the vehicle as a salvage vehicle. This change became effective July 1, 1995.

For those salvage vehicles retained by their owners, eliminating the double title transfer means that the insurer will not have to pay the $10.00 fee that applies to transfers of salvage vehicles to an insurer and that the owner will not have to pay the highway use tax and $35 title fee that applies to transfers of titles in general. The

insurer and the owner will not have to pay these fees because there will be no title transfer that triggers their payment.

Utility vehicles

The act exempts utility vehicles that are licensed in another state and are used in this State in an emergency to restore utility service from two different registration requirements. The two requirements from which the vehicles are exempt are (i) the requirement to register with the Division of Motor Vehicles and pay an apportioned license fee and (ii) the requirement to register with the Department of Revenue and pay a road tax based on the number of miles driven in the State. These changes were recommended to the 1994 General Assembly by the Joint Legislative Utility Review Committee. They passed the House of Representatives during the 1994 biennium as part of a larger bill, but the larger bill did not pass the Senate. These changes become effective October 1, 1995.

Chapter 89 (Senate Bill 245, Sen. Hartsell)

AN ACT TO AUTHORIZE THE OPENING OF EMPTY LOCK BOXES OF DECEDENTS OUTSIDE THE PRESENCE OF THE CLERK OF SUPERIOR COURT, AS RECOMMENDED BY THE GENERAL STATUTES COMMISSION.

This act, which was recommended by the General Statutes Commission, establishes a procedure to allow a decedent's safe deposit box to be opened outside the presence of the Clerk of Superior Court if the box is empty. Under current law, financial institutions managing safety deposit lock boxes may not open a box after the death of the box holder unless someone from the clerk of court's office is present. When the box is opened, the clerk makes an inventory of its contents and furnishes a copy to the Secretary of Revenue for inheritance tax purposes. This requirement serves no purpose in cases in which the box is empty.

Under this act, if the personal representative of an estate believes the box may be empty, the representative may request the clerk of court to authorize the box to be opened outside the presence of an employee of the clerk of court. With this permission, the box may be opened in the presence of a representative of the financial institution, who must certify that the box is empty. No notice is sent to the Department of Revenue. If the box is not empty, the box must be closed immediately and reopened only in the presence of the clerk. This act becomes effective October 1, 1995, and applies to the estates of decedents dying on or after that date.

Chapter 109 (House Bill 213, Rep. Bowie)

AN ACT CONCERNING THE COLLECTION OF DELINQUENT TRUCK PENALTIES AND ASSESSED TAXES AND THE CONSOLIDATION OF THE VARIOUS PROVISIONS CONCERNING OVERWEIGHT VEHICLES.

This act clarifies the law concerning the authority of a law enforcement officer of the Division of Motor Vehicles (DMV) to detain a truck until any delinquent penalties or taxes previously assessed against the truck's owner for motor carrier vehicle violations or motor carrier taxes have been paid. It also consolidates the various provisions concerning the weighing of trucks and eliminates inconsistencies in these provisions. The act becomes effective October 1, 1995. It is one of the recommendations of the Joint Legislative Transportation Oversight Committee to the 1995 General Assembly.

G.S. 20-96 authorizes the detention of a truck "with an overload as described in this section or which is equipped with improper registration plates, or the owner of which is liable for any overload penalties or assessments applicable to the vehicle and due and

unpaid for more than 30 days." This language can be construed to mean that a vehicle can be detained only when it has an overload, has improper registration plates, or has an overdue overweight penalty assessed against that particular truck. However, in practice, a DMV law enforcement officer can detain a truck when the officer finds that the truck's owner has previously been assessed a penalty for a motor carrier vehicle violation and payment of the penalty is overdue. Penalties are due upon assessment and become delinquent 30 days after the date of assessment. Motor carrier vehicle violations include registration, equipment, and overweight violations. A DMV officer can also detain a truck when the officer finds that the trucks' owner is delinquent in paying motor carrier road taxes due under Article 36B of Chapter 105 of the General Statutes. This act rewrites G.S. 20-96 to make it clear that the authority applies to all motor carrier vehicle violations and to delinquent motor carrier taxes.

The act also consolidates the statutory provisions on the weighing of trucks and eliminates inconsistencies in those provisions. Currently, G.S. 20-96 has several inconsistencies. First, it states that overweights are subject only to axle-group penalties, and not single-axle or tandem-axle weight limit penalties. Second, it states that overweights on light-traffic roads are subject only to single-axle or tandem-axle penalties, and not axle-group penalties. Both of those statements conflict with G.S. 20-118. Third, it refers to a tax that was repealed years ago.

Chapter 329 (Senate Bill 496, Sen. Blackmon)

AN ACT TO ALLOW LOCAL GOVERNMENTS TO FORGO COLLECTION OF AD VALOREM TAX BILLS WHEN THE ORIGINAL PRINCIPAL AMOUNT DUE IS UNDER FIVE DOLLARS.

This act gives the governing body of a taxing unit that collects its own taxes the authority to adopt a resolution directing the tax collector not to collect property taxes when the amount of tax due is less than the amount set in the resolution. The amount set may not exceed $5.00 and should be the amount it would cost the taxing unit to send a tax bill. All of the taxes and fees due on a tax receipt or on a motor vehicle property tax notice, including those taxes and fees of other units for which it collects taxes, are included in determining whether the amount due is less than the threshold set by the taxing unit.

Under current law, the governing body of a taxing unit may permit its tax collector to treat small underpayments of taxes as fully paid and to not refund small overpayments of taxes unless the taxpayer requests a refund. The statute defines "small" as $1.00 or less. This act expands that concept, by allowing taxing units to eliminate billing and collection of minimal taxes up to $5.00. As with small underpayments and small overpayments, the tax collector must keep a record of the taxes by taxpayer and amount and must report the amount of taxes to the governing body as part of the settlement for the year.

The act is effective July 1, 1995, which is the beginning of the 1995-96 tax year. To authorize the tax collector not to collect minimal taxes for a tax year, the governing body must adopt a resolution to that effect by June 15 preceding the first day of the tax year (July 1). The resolution remains in effect for subsequent tax years until amended or repealed by another resolution of the taxing unit. Because this act was ratified June 26, 1995, it gives taxing units an extension until June 30, 1995, to adopt a resolution for the 1995-96 tax year.

The General Assembly had earlier ratified as Chapter 24 of the 1995 Session Laws an act that allowed counties not to bill for motor vehicle property taxes when the amount due on the tax bill is less than the cost of preparing and sending the bill. That act was repealed by this act because this act will cover motor vehicle property taxes as well as all other property taxes. If a county adopted a resolution under Chapter 24 before its repeal, the resolution will be effective under this act.

Chapter 340 (House Bill 123, Rep. Arnold)

AN ACT TO REVISE THE CONTROLLED SUBSTANCE EXCISE TAX.

This act revises the State excise stamp tax on controlled substances to bring it in line with a 1994 decision of the United States Supreme Court. The act becomes effective October 1, 1995, and is expected to have a minimal negative impact on excise stamp tax collections.

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 that 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.

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: the North Carolina law applies whether or not a person is arrested for a drug violation. North Carolina 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 the North Carolina 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 act makes the following changes to North Carolina's drug tax law to remove any aspects of the tax that could indicate that the tax is a punishment rather than a true tax designed to raise revenue; these changes were recommended by the Revenue Laws Study Committee on the advice of the Attorney General's Office and the Controlled Substance Tax Division of the Department of Revenue.

(1) It clarifies that the purpose of the tax is to raise revenue for law enforcement and for the General Fund rather than to provide a second punishment.

(2) It revises the tax rates so that they do not, in general, exceed the market value of the various illegal drugs. The act imposes a lower tax rate on low-street-value drugs, which include steroids, depressants, stimulants, and hallucinogenic substances. It also imposes a lower tax rate on 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.

(3) It provides 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.

(4) It repeals 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. Under the act, the drug tax is subject to the same penalty provisions as other tax laws.

(5) It reduces the civil penalty for failure to pay the drug 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 100% drug tax penalty has been imposed but, as a practical matter, is virtually never collectible.

(6) It repeals the tax on counterfeit controlled substances, which do not have the same value as true controlled substances.

(7) It clarifies that the proceeds of the tax may be distributed more frequently than quarterly.

Chapter 349 (House Bill 768, Rep. Sexton)

AN ACT TO PROVIDE THAT THE HIGHWAY USE TAX TRADE-IN ALLOWANCE APPLIES WHEN TWO CARS ARE EXCHANGED FOR ONE ANOTHER.

This act specifies in the statutes that an exchange of motor vehicles between two parties is a sale under the highway use tax. An exchange between two parties has always been considered a sale under the highway use tax, so the act does not change the law on this subject. The act became effective July 1, 1995. Because the act does not change the law, the act has no fiscal impact.

The definition of "sale" in G.S. 105-164.3(15) that applies to the highway use tax specifically includes an exchange of property. The Division of Motor Vehicles, which administers the tax, has followed this definition and treated exchanges as sales.

If a transaction is a sale under the highway use tax, the amount on which the highway use tax is computed is reduced by the amount of any trade-in allowance. The amount on which highway use tax is computed is the market value of the vehicle. If a seller of a vehicle is not a car dealer, the market value of the vehicle is presumed to be the wholesale book value of the vehicle. The amount allowed as a trade-in allowance, however, is not based on market value. The amount allowed as a trade-in allowance is the amount determined by the seller to be the value of the vehicle.

The effect, therefore, of treating a two-party exchange of vehicles as two sales is to allow a trade-in allowance to be applied to each sale, thereby reducing the amount on which highway use tax is computed. If each seller gives a trade-in allowance equal to the market value (wholesale book value) of the vehicle owned by the seller at the time of the exchange, no highway use tax will be due because the market value of the vehicle less the trade-in allowance will be zero.

The highway use tax was enacted in 1989 to provide revenue for the Highway Trust Fund. It 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 tax that applies until July 1, 1996, and to a maximum tax. The minimum tax, which is repealed effective July 1, 1996, 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.

Chapter 350 (House Bill 1058, Rep. McComas)

AN ACT TO MAKE CONFORMING CHANGES TO THE TAX LAW IN LIGHT OF FEDERAL LAW PREEMPTING STATE REGULATION OF MOST MOTOR FREIGHT CARRIERS.

This act amends the property tax laws and the corporate income tax laws to preserve the existing property tax and income tax treatment of for-hire motor carriers of property. Because of changes in federal law, these motor carriers did not fit the statutory definitions that applied prior to the effective date of this act. This act became effective June 29, 1995. The act is not expected to have a fiscal impact.

A federal act passed in the fall of 1994 prohibits federal or state regulation of rates, routes, and service of trucking companies, other than those that carry household goods. Until this prohibition, the North Carolina Utilities Commission regulated intrastate trucking companies and the Interstate Commerce Commission (ICC) regulated interstate trucking companies. The North Carolina Utilities Commission can no longer regulate these intrastate trucking companies, and the ICC's regulation of interstate trucking companies has been greatly reduced.

The state property tax and income tax definitions of trucking companies that were in effect when the 1994 federal act became effective referred to trucking companies as being regulated by the Utilities Commission or the ICC. Because of the change in the scope of regulation, these definitions no longer applied. The act therefore modifies the definitions to ensure that the change in regulation does not inadvertently cause a change in the way the trucking companies pay property and income taxes.

Under the State property tax laws, the "rolling stock" (vehicles) of all intrastate trucking companies that have two or more terminals in the State and of all interstate trucking companies that do business in the State is valued by the Department of Revenue rather than by the county assessor of the counties in which the company's terminals are located. The value of the vehicles is then allocated among the counties in which the terminals are located in proportion to the percentage (tonnage) of freight handled at each terminal during the preceding year. This method of taxation avoids the problem of multiple counties trying to tax the same property.

If the trucking company does business outside the State, the Department of Revenue must determine the share of the company's property that is taxable in this State and will therefore be allocated among the counties. This determination is made on the basis of mileage in this State. Similarly, under the corporate income tax, the income of a trucking company that does business in more than one state is allocated among those states based on the number of vehicle miles traveled in each State.

Chapter 360 (House Bill 994, House Appropriations Committee)

AN ACT TO IMPLEMENT THE RECOMMENDATIONS OF THE COMMITTEE ON APPROPRIATIONS BY CHANGING VARIOUS REVENUE STATUTES.

This act contains a variety of changes that concern either insurance taxes and fees or the payment of administrative costs under the Setoff Debt Collection Act. The changes were recommended by the House and Senate Appropriations Committees as part of the biennial State budget and were revised by the House and Senate Finance Committees.

Section 1 of this act transfers the responsibility of collecting part of the premiums tax imposed on insurance companies from the Department of Insurance to the Department of Revenue, effective January 1, 1996. This responsibility will cost the Department about $100,000 a year, with additional one-time costs of about $200,000 in the 1995-96 fiscal year. These amounts were appropriated to the Department of Revenue in the expansion budget, Chapter 570 of the 1995 Session Laws.

Under G.S. 105-228.5, insurance companies pay taxes based on their gross premiums instead of paying corporate income and franchise taxes. In addition,

employers that carry their own workers' compensation risk, known as self-insurers, and employers that pool their workers' compensation liabilities pay the gross premiums tax on premiums they pay or on the premiums that would be charged to cover the risk. The workers compensation premiums tax rate is 2.5% of gross premiums and the general premiums tax rate is 1.9% of gross premiums. The tax rate on receipts of nonprofit companies providing hospital, medical, and dental coverage is 0.5%. Insurers that provide fire and lightning coverage pay an additional tax at the rate of 1.33% of gross premiums for fire and lightning coverage provided on property other than vehicles and boats.

Section 1 of this act provides that collection of the 2.5% tax on workers' compensation self-insurers and the additional 1.33% tax on fire and lightning coverage remains with the Department of Insurance. Collection of the 2.5% tax on other workers' compensation premiums and of the rest of the premiums tax is transferred to the Department of Revenue. This section also reorganizes and modernizes the language of the gross premiums tax statutes, clarifies that interest on installment overpayments of gross premiums tax is calculated the same way as interest on installment overpayments of corporate income tax, and deletes from Article 2 of Chapter 97 of the General Statutes, the Workers' Compensation Act, redundant and inaccurate provisions about the collection of the tax on workers' compensation insurance.

Section 2 of this act eliminates the insurance audit and examination fees for insurance companies, HMOs, medical corporations, and guaranty associations, effective July 1, 1995. Under current law, when the Insurance Department audits an insurer or a rate organization, it charges the cost of the audit to the company as a fee. The act repeals these fees. Consequently, the costs of the audits will be paid for by the insurance regulatory charge as part of the costs of regulating the insurance industry. The Fiscal Research Division estimated that the amount of fee revenue that will be replaced by regulatory charge revenue is $4.5 million a year.

Section 3 of this act expands the purposes for which the insurance regulatory charge is to be used, effective July 1, 1995, to include costs incurred by other departments as well as by the Department of Insurance in regulating the insurance industry. The insurance regulatory charge, which is a percentage of gross premiums tax liability, was imposed on insurance companies in 1991 in order to make the Department of Insurance receipt-supported and thereby eliminate General Fund support of that department. Its use was limited to paying the cost to the Department of Insurance of regulating the insurance industry and other industries as well as the State's costs incidental to the Department of Insurance's costs. Section 3 removes the limitation that costs payable from the charge must be incurred by the Department of Insurance; this change is designed to include in the costs that are paid from the charge the costs of the Attorney General's Office in providing counsel on insurance matters. To reflect the broader application of the insurance regulatory charge, Section 3 also changes the name of the fund to which the charge is credited from the Department of Insurance Fund to the Insurance Regulatory Fund and specifies that this fund is to be administered by the Office of State Budget and Management.

Section 4 of this act changes the administrative reimbursement under the Setoff Debt Collection Act by excluding child support collections from payment of the administrative costs, effective January 1, 1996. The Setoff Debt Collection Act is the law under which the Department of Revenue retains an income tax refund of an individual who owes money to a claimant agency and sends the refund to the claimant agency to be applied to the debt. The Department pays for this program by deducting its administrative costs from amounts collected on behalf of all claimant agencies. The Department of Human Resources and county agencies are claimant agencies that use the debt setoff program to collect child support arrearages pursuant to the federal Child Support Enforcement Program. This section provides that the Department of Revenue

will no longer deduct its administrative costs from amounts collected for child support arrearages, but it will continue to receive the same amount of reimbursement as under the current law by spreading among other claimant agencies the portion of the Department's administrative costs now deducted from child support collections. Thus, a greater percentage of other debts collected will be deducted for administrative costs. The Fiscal Research Division has estimated that approximately $300,000 a year in child support setoff administrative costs will be shifted from child support collections to other setoff collections, resulting in an increase in the percentage deducted from those other collections from the current 7% to about 14% of the amount collected.

Section 5 of this act repeals a provision in the 1995 continuation budget that made certain budget reductions contingent on enactment of this act. Because this act has been enacted, the contingency language in the budget is not needed.

Chapter 370 (House Bill 142, Rep. C. Wilson)

AN ACT TO MAKE TECHNICAL CHANGES RELATING TO THE REPEAL OF THE INTANGIBLES TAX AND TO OTHER TAX LAWS.

Sections 1 through 3 of this act make clarifying and technical changes to acts enacted during the 1995 session. Sections 4 through 6 make clarifying changes and technical corrections to laws enacted in previous sessions.

Sections 1 and 2 make changes to Senate Bill 8, Intangibles Repeal/Hold Harmless, enacted as Chapter 41 of the 1995 Session Laws. Section 1 inserts a cross-reference to the Department's costs of administering the intangibles tax reimbursement. The effect of the cross-reference is to maintain the Department's current authorization to deduct from local government revenues its costs of administering the intangibles tax distributions. Section 2 makes technical wording changes so that the various intangibles tax reimbursement allocations will read the same. These sections became effective July 1, 1995; the Fiscal Research Division reported that they have no fiscal impact.

Section 3 of this act makes a clarifying change to the personal exemption increase enacted by House Bill 2, Income Tax Cut/Child Care Credit as Chapter 42 of the 1995 Session Laws. The additional language added by the increased exemption was slightly ambiguous and might have been misconstrued to require an inflation adjustment only if the taxpayer's adjusted gross income was below the thresholds set in the act. The inflation adjustment -- an addition to taxable income -- is required of all taxpayers, however. This section becomes effective for the current tax year and has no fiscal impact.

Section 4 of this act clarifies the amount of a deduction a corporation may take as a charitable contribution for donating land for conservation purposes when it also takes a credit for the donation under G.S. 105-130.34. That statute allows a credit of 25% of the value of the land, up to a maximum credit of $25,000. This section clarifies that a deduction is allowed for the excess value of the land over the value used in computing the credit, rather than the excess value over the amount of the credit itself. For example, if the value of the land is $120,000, the credit is 25% of that value, $30,000, capped at $25,000. Because the credit is based on the first $100,000 of land value, a deduction is allowed only for the remaining $20,000 of value. Before clarification by this section, the current provision could have been construed to allow a deduction in this circumstance for $95,000, which is the excess value of the land over the amount of the credit allowed. This section becomes effective for the current tax year and could result in a minor increase in General Fund tax revenue.

Sections 6 and 7 of this act correct errors in the jobs tax credit statutes that reverse the proper order of the county rankings based on population. The correct order is highest to lowest instead of lowest to highest. These sections are effective upon ratification and have no fiscal impact.

Chapter 390 (Senate Bill 943, Sen. Kerr), as amended by Sections 32.1 and 32.2 of Chapter 523

AN ACT TO ADDRESS MOTOR FUEL TAX EVASION AND TO IMPROVE THE ADMINISTRATION OF THE MOTOR FUEL TAXES BY CHANGING THE POINT OF TAXATION OF GASOLINE AND DIESEL FUEL, TO REPEAL THE MINIMUM HIGHWAY USE TAX, AND TO STRENGTHEN THE ENFORCEMENT OF THE ROAD TAX PAID BY MOTOR CARRIERS.

This act makes several significant changes to the motor fuel tax laws and to the highway use tax laws. The changes become effective at various times as explained. The changes are expected to generate net annual additional Highway Trust Fund revenue of $10 million when all the changes have become effective.

First, the act establishes a uniform system for the collection of the per gallon motor fuel excise taxes on gasoline and clear diesel. Under the system, fuel is taxed when it is removed at a "rack" at a motor fuel terminal. Under current law, gasoline is taxed on its first sale after the rack and clear diesel is taxed when it is sold to a person who is going to either resell it at a service station to operate highway vehicles or store it for subsequent use in highway vehicles the person owns. Parts I, II, and III of the act make this change, effective January 1, 1996.

Second, the act repeals the $40 minimum highway use tax that is payable when the title to a vehicle is transferred, effective July 1, 1996. Part IV of the act makes this change.

Third, it establishes a minimum mileage presumption for motor carriers that drive in the State but do not report mileage to the State and imposes increased penalties for motor carriers that understate mileage to the State by more than 25%. Part V of the act makes these changes, effective October 1, 1995.

Uniform System For Motor Fuel Tax Collection

Part I of the act repeals the current laws on the collection of motor fuel excise taxes and replaces them with new laws on this subject. The new laws move the point of collection for the per gallon motor fuel excise taxes to the terminal, thereby eliminating opportunities for tax evasion and making the system easier to administer. North Carolina is particularly vulnerable to motor fuel tax evasion because its motor fuel tax rate is 21.95¢ a gallon compared to 16¢ a gallon in South Carolina and 7.5¢ a gallon in Georgia.

The new system will eliminate opportunities for tax evasion by reducing the availability of non-tax-paid fuel purchased in this State and by having a large part of the tax on imported fuel collected by out-of-state suppliers. The proposed system will be easier to administer because it will parallel the federal system as well as South Carolina's and the number of taxpayers will be greatly reduced.

Part II of the act provides for transitional provisions to facilitate the change to the new system. Part III of the act makes conforming changes to various statutes that refer to motor fuel laws. The following outline summarizes the distinctions between the act and the current law:

Subject	Chapter 390	Current Law
Taxing Point	Removal from terminal	Gasoline - first sale Diesel - last sale before highway use
Taxpayer	Distributor; supplier is trustee and will collect tax from distributor	Distributor, who pays directly to state

	and remit to state	
Tax Due Date	22nd of each month; licensed distributor can pay supplier the same date that supplier must pay the state	Gasoline- 20th Diesel- 25th
'Tare' Allowance	Licensed distributor gets 1% on taxable gasoline and diesel plus quarterly hold-harmless	Licensed gasoline distributor gets: 2% on first 150,000 1½% on next 100,000 1% on excess over 250,000 and tare applies to exempt gov't sales; Diesel distributor does not get tare
Supplier Allowance	1/10 of 1%, with $8,000 monthly maximum	None; supplier does not collect from distributors and remit to the state
Tax on Imports	Reported and paid by distributor	Paid mainly by elective or permissive supplier; paid in part by one of three types of importers: bonded, occasional, and tank wagon. Import verification number required.
Bond Amounts	$2,000,000 for refiner, supplier, terminal operator, and bonded importer. Two times monthly liability with minimum of $2,000 and maximum of $250,000 for distributor, occasional importer, tank wagon importer, blender.	Gasoline: two times monthly liability with minimum of $2,000 and maximum of $125,000 Diesel: Two times; monthly liability with minimum of $500 and maximum of $125,000
Exemptions	Same as current law	Exports, sales to federal government, sales to state, sales to local boards of education
Refunds	Motor fuel delivery vehicle, accidental mixes, lost diesel fuel, and clear diesel bought	Exempt gov't sales, exports, cities and counties, a few

	by marinas; otherwise the same	nonprofits, taxis, cement mixers, garbage compactors, and a few other vehicles that have power equipment, and off-highway uses
Enforcement	Same shipping document plus import verification number	Destination state shipping document

Repeal of Minimum Highway Use Tax

Part IV of the act repeals the minimum $40 highway use tax, effective July 1, 1996. Section 30 of that Part repeals the tax. Sections 31, 32, and 33 are conforming changes to references to the minimum tax. Section 34 adjusts revenue between the Highway Fund and the Highway Trust Fund to ensure that the Highway Trust Fund does not lose revenue.

The highway use tax was enacted in 1989 as part of the Highway Trust Fund legislation 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.

The $40.00 minimum tax is 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.

Since the enactment of the tax, the Revenue Laws Study Committee and the Division of Motor Vehicles of the Department of Transportation have received numerous complaints about the high minimum amount that must be paid to transfer a certificate of title. 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. Part IV of this act responds to these complaints by repealing the minimum tax.

Motor Carrier Enforcement Changes

Part V of the act makes changes to the road tax that are designed to increase compliance with that tax. It establishes a minimum mileage presumption for motor carriers that drive in the State, as evidenced by records of the Division of Motor Vehicles, but either do not report mileage to the State or underreport mileage. The presumption is 10 trips of 450 miles each for each of the carrier's vehicles.

The act also imposes an increased penalty on motor carriers that understate their mileage to the State by more than 25%. Under current law, the penalty for negligently understating the amount of tax owed is 10% of the deficiency. This act increases the

penalty for motor carriers that understate their mileage by more than 25% to an amount equal to two times the amount of the deficiency. This Part becomes effective October 1, 1995.

The purpose of the road tax is to tax motor carriers who drive in the State using fuel purchased in another State. The road tax on motor carriers is set at the same rate as the per gallon excise tax and a credit is given for any State per gallon excise taxes paid. The number of miles a motor carrier drives in North Carolina in a reporting period and the total amount of fuel consumed by the motor carrier in that reporting period determine the motor carrier's road tax liability.

Chapter 404 (Senate Bill 293, Sen. Rand)

AN ACT TO PERMIT THE IMPORTATION AND BOTTLING OF SPIRITUOUS LIQUOR WITHIN FOREIGN TRADE ZONES LOCATED AT THE WILMINGTON AND MOREHEAD CITY PORTS.

This act creates a new type of commercial ABC permit known as a liquor importer/bottler permit. The application fee for this permit is $250.00. The fee is collected by the ABC Commission and remitted to the State Treasurer for the General Fund. The permit is valid for one year, from May 1 to April 30. G.S. 18B-903 provides that the renewal fee is 25% of the original application fee: $62.50. The holder of a liquor importer/bottler permit would also need to obtain a State license. The annual tax for this license is $250.00. The act became effective upon ratification, July 11, 1995, and will generate a small amount of revenue for the General Fund.

A liquor importer/bottler permit will allow the holder of the permit to import liquor in closed containers into the foreign trade zone at either of the State Ports via ships that dock at the Ports. The imported liquor can be bottled, packaged, or labeled or it can be stored and shipped to State or local ABC warehouses and, where permitted by other jurisdictions, to public and private agencies in those jurisdictions. The liquor can also be transported from the State Ports for purposes related to bottling, packaging, labeling, sale, or storage.

Prior to the enactment of this new permit, State law did not provide a way for liquor to be imported into North Carolina. For imported liquor to be sold in this State, it had to be imported into another State and then be sold to this State. This act will allow a person to purchase liquor in bulk, import it into the State, bottle it, and send it to a warehouse. The permit is similar to the bottler permit the State currently provides for malt beverages, unfortified wine, and fortified wine and to the distillery permit, which allows the holder to import ingredients used in the distillation of spirituous liquor.

Chapter 410 (House Bill 504, Rep. G. Robinson)

AN ACT TO SUBTRACT ANY TRADE-IN ALLOWANCE IN CALCULATING THE ALTERNATIVE HIGHWAY USE TAX ON LEASED VEHICLES.

This act excludes a trade-in allowance from the amount on which the alternate highway use tax on leased vehicles is calculated. The change becomes effective October 1, 1995. The change is expected to reduce Highway Trust Fund revenue by $1 million to $1.5 million a year.

Until October 1, 1995, the highway use tax on leased vehicles will apply to the gross receipts from the lease or rental of the vehicle with no deduction for the value of a trade-in allowance. If, for example, a person leases a vehicle for $250 a month and at the same time trades in a vehicle worth $5,000, highway use tax is due on the monthly payment and on the trade-in allowance of $5,000.

This is in contrast to the way highway use tax is calculated on the sale of a motor vehicle. The sales price of a motor vehicle is reduced by 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. If, for example, a person buys a car worth $20,000 and at the same time trades in a vehicle worth $5,000, highway use tax is due on $15,000.

The difference in treatment between sales and leases stems from differences in the highway use tax and the sales tax. As part of the 1989 Highway Trust Fund legislation, motor vehicles were exempted from sales tax and made subject to highway use tax. When vehicles were subject to sales tax, the sales price was not reduced by the amount of a trade-in allowance. The new highway use tax specifically allows a reduction in sales price for the value of a trade-in but does not allow a reduction in the lease price. The highway use tax legislation provides that highway use tax due on the lease of a motor vehicle is to be administered as if it were a sales tax on the motor vehicle. Consequently, the general sales tax rule that the lease price is not reduced by a trade-in allowance applies to the collection of highway use tax on leased 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 until July 1, 1996. Beginning July 1, 1996, the minimum tax is repealed. 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. When a lessor of vehicles buys a vehicle to be leased, the lessor has the option of either paying highway use tax when the lessor obtains a certificate of title for the vehicle or paying a tax on the gross receipts of the vehicle. If the lessor elects to pay on the gross receipts, the lessor must pay the alternate tax to the Department of Revenue. The alternate tax is 3% on the gross receipts from long term leases and rentals and 8% on the gross receipts from short term leases and rentals. The 8% tax goes to the General Fund and the 3% tax goes to the Highway Trust Fund.

Chapter 443 (Senate Bill 229, Sen. Odom)

AN ACT TO REMOVE IMPEDIMENTS AND DISINCENTIVES TO DONATING CONSERVATION LAND OR PRESERVATION STRUCTURES OR SITES.

This act removes disincentives for donations of conservation or preservation land or property in three ways:

(1) It recognizes and ratifies conservation and preservation agreements with the federal government.
(2) It amends the Marketable Title Act to prevent conservation and preservation agreements from expiring if not rerecorded.
(3) It eliminates the requirement that back property taxes be paid when use value property is donated for conservation or preservation purposes.

Section 1 of this act adds the federal government as a recognized holder of a conservation or preservation agreement under Article 4 of Chapter 121 of the General Statutes, the Conservation and Historic Preservation Agreements Act. That Article permits an owner of real property to include restrictions on property interests transferred to a governmental entity or nonprofit corporation to retain land and water in their natural, scenic, or open condition or in agricultural, horticultural, farming, or forest use. The Article also authorizes restrictions on transferred historical structures to preserve their historically significant architecture, archaeology, or historical associations. This section became effective upon ratification, July 18, 1995, and Section 2 extends it retroactively to June 1, 1979, thereby ratifying conservation and preservation agreements entered into with the federal government since that date.

Section 3 of this act adds an additional exception to the Marketable Title Act for conservation and preservation agreements entered into pursuant to the Conservation and Historic Preservation Agreements Act. The purpose of the Marketable Title Act is to simplify chains of title to real property by extinguishing certain claims against property if the claims are more than 30 years old, unless the claimed interest is rerecorded

within the 30-year period. Because of concerns that the renewal dates for conservation and preservation agreements could be overlooked by the government or nonprofit corporation that holds the property interest, and because these agreements serve a public purpose, this act provides that they will not be allowed to expire or be terminated as a matter of law by the Marketable Title Act.

Section 4 of this act eliminates the rollback of deferred taxes on transferred use value property if the property is donated to a governmental unit or is donated to a nonprofit organization for use as a protected natural area or for nonprofit historic preservation purposes. Property tax law provides that all property is to be taxed at its market value. A special use value law makes an exception for agricultural land, horticultural land, and forestland: it can be taxed at its value in its current use. The taxes that would otherwise have been due are deferred and become a lien on the land, however. If the property is transferred or otherwise becomes ineligible for use value taxation, three years of these deferred taxes become due and payable to the local government taxing units. This section provides an exception for land the owner donates to governmental units or donates to nonprofits for conservation or preservation. This section, which became effective January 1, 1995, will cause a revenue loss to local governments. The amount of the loss cannot be determined because one cannot predict how much property will be donated each year.

Chapter 451 (House Bill 360, Rep. Black)

AN ACT TO EXEMPT RAILROADS FROM PAYMENT OF SALES TAX ON DIESEL FUEL USED BY LOCOMOTIVES AND RAILROAD CARS.

This act exempts railroad companies from paying the 6% State and local sales tax on diesel fuel used to operate railroad locomotives and railroad cars. Railroad companies do not pay motor fuel tax on diesel fuel used to operate railroad locomotives and railroad cars because the fuel is not used to operate a vehicle on the highways. The motor fuel tax on diesel fuel is 21.95¢ per gallon. This act, introduced on behalf of the Department of Transportation, exempts railroad companies from paying either sales tax or motor fuel tax on diesel fuel. The act is effective September 1, 1995, and is expected to reduce General Fund tax revenues by about $1.5 million a year.

There are many exemptions from the sales and use tax in the current law. An existing exemption, similar to the railroad diesel exemption added by this act, is the sale of fuel used by ocean-going vessels engaged in interstate commerce.

Chapter 454 (Senate Bill 237, Sen. Speed)

AN ACT TO CLARIFY THE USE VALUE TAX LAW, TO UPDATE THE LAW TO CONFORM TO MODERN FAMILY PROPERTY TRANSACTIONS, AND TO EXPAND THE CATEGORY OF PERSONS WHO MAY QUALIFY FOR USE VALUE PROPERTY TRANSFERS.

This act makes several changes to the special property tax classification for farm property taxed at its use value rather than its market value. It clarifies the kinds of individual owners who can qualify for this classification, allows farmland owned by a partnership, a trust, or a limited liability company to qualify for use value tax treatment to the same extent as a corporation, allows farmland owned by certain trusts to qualify for use value tax treatment, and expands the definition of "relative" used to determine qualification for use value tax treatment. The changes became effective January 1, 1995, and apply to tax years beginning with the 1995-96 tax year. The changes are not expected to have a significant impact on local property tax revenues, but will reduce revenue to a slight extent.

Property tax law provides that unless property is exempted or classified for special tax treatment, it is to be taxed at its market value. Agricultural land, horticultural land, and forestland are classified and are taxed at their value in their present use as

agricultural land, horticultural land, or forestland. The difference between the taxes due on the present use value treatment and the taxes that would have been payable in the absence of this special treatment, together with any interest, penalties, or costs, are a lien on the property. The difference in taxes is carried forward in the records of the taxing unit as deferred taxes. The deferred taxes for the preceding three years become payable whenever the property is sold or whenever the property loses its eligibility for the benefit of the special use value law.

To qualify for use value taxation, the property must meet minimum size requirements, must be in actual production, must be owned by an individual or by a corporation whose principal business is cultivating the land and whose shareholders are all either actively engaged in this business or are relatives of someone who is actively engaged in this business. Agricultural land and horticultural land must also produce gross income that meets minimum thresholds.

Before the enactment of this act, the term "individually owned" had been interpreted administratively to include an individual who is a beneficiary of a trust, a partner in a partnership, or a member of a limited liability company. Under this interpretation, these individuals could qualify their share of the land as if they owned it directly. The act codifies this interpretation of the law by modifying the definition of "individually owned" to specifically include these individuals and to clarify how an undivided interest is identified.

The act expands the special use value law to allow partnerships and limited liability companies to qualify their property for use value if they meet the conditions set for corporations. These conditions are that the principal business of the entity is cultivating the land, that the partners or members are all actively engaged in this business or are relatives of someone who is actively engaged in this business, and that the entity or a partner or member of the entity owned the land for the previous four years.

The act further expands the special use value law to allow three types of trusts to qualify. The first type is a trust that is created by an individual and whose beneficiaries are all either the creator of the trust or a relative of the creator. The second type is an extension of the first type; it is a trust that is created by an individual and whose beneficiary is a trust whose beneficiaries are all either the creator of the initial trust or a relative of the creator. The third type is a testamentary trust created by an individual who owned land that was taxed at its use value, transferred the land to the trust upon death, had no relatives at the time of death, and designated that all trust income be used exclusively for nonprofit purposes. For any of these trusts to qualify, the trust or the creator of the trust had to own the land for the previous four years.

Finally, the act expands the definition of "relative" to include nieces and nephews and their descendants, aunts and uncles, parents-in-law, stepchildren and their descendants, and the spouse of any of these relatives. The definition of "relative" in the current law does not include these relatives.

Chapter 456 (House Bill 718, Rep. Gray)

AN ACT TO ESTABLISH A NORTH CAROLINA PARKS AND RECREATION AUTHORITY AND TO EARMARK FUNDS FOR THE PARKS AND RECREATION TRUST FUND AND THE NATURAL HERITAGE TRUST FUND.

This act reallocates the State's share of the deed stamp tax to the Parks and Recreation Trust Fund and the Natural Heritage Trust Fund, modifies the purposes for which the Parks and Recreation Trust Fund may be used, and creates the North Carolina Parks and Recreation Authority to administer the Parks and Recreation Trust Fund. These changes become effective July 1, 1996.

Under current law, 15% of the State's share of the deed stamp tax ($3.1 million) each year is dedicated to the Natural Heritage Trust Fund created in G.S. 113-77.7 and the remaining 85% ($18 million) goes to the General Fund. Chapter 772 of the 1993 Session Laws declared that it was the intent of the General Assembly to dedicate 75% of the State's share of the deed stamp tax each year to the Parks and Recreation Trust Fund and an additional 10% to the Natural Heritage Trust Fund. Section 3 of this act fulfills that intent by dedicating 75% of the State's share ($15.9 million) to the Parks and Recreation Trust Fund and 25% ($5.3 million) to the Natural Heritage Trust Fund. These funds will be transferred on a quarterly basis each year beginning July 1, 1996. None of the State's share of the deed stamp tax will go to the General Fund after that date.

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¢ to $1.00 for each $500.00 of value.

Section 2 of this act modifies the use of revenue in the Parks and Recreation Trust Fund. It decreases the amount of the Fund that is to be used for the State Parks system from 75% to 65% and increases the amount that is to be used for local matching grants for local parks and recreation from 20% to 30%. In addition, it allows the use of up to 3% of the Fund each year for operating expenses associated with managing capital improvements, acquiring land, and administering local grants.

The remainder of this act creates the North Carolina Parks and Recreation Authority within the Department of Environment, Health, and Natural Resources. The Authority will administer the Parks and Recreation Trust Fund and report annually to the General Assembly on allocations from that Trust Fund. The Authority will also advise the Secretary of Environment, Health, and Natural Resources. The existing Parks and Recreation Council, an advisory council within the Department of Environment, Health, and Natural Resources, is repealed. The Authority will have nine members; the Governor, the Speaker of the House of Representatives, and the President Pro Tempore of the Senate will each select three. Members will serve staggered two-year terms.

Chapter 458 (Senate Bill 606, Sen. Sherron)

AN ACT TO PROVIDE FOR THE CREATION OF FACILITY AUTHORITIES AND TO ESTABLISH THE CENTENNIAL AUTHORITY.

This act provides the statutory framework for the General Assembly to create a "facility authority" and, in conjunction with that framework, establishes a Centennial Authority in Wake County. The purpose of a facility authority is to study, design, plan, construct, own, promote, finance, and operate a regional facility. A regional facility is a facility designed to attract major regional, national, and international sports and recreational events. The act became effective upon ratification.

A facility authority will have either eight or 13 members, depending on the territorial jurisdiction of the authority. The initial eight members are appointed by the General Assembly. The territorial jurisdiction of an authority is the county in which the regional facility is to be located. If the jurisdiction of an authority is a county where the main campus of a constituent institution of The University of North Carolina is located, then the authority will have 13 members. Of the additional five members, two are appointed by the board of county commissioners, two are appointed by the city council of the city with the largest population in the county, and the remaining member is appointed jointly by the mayors of all the cities in the county. A member may be

removed by the appointing authority for cause and a vacancy occurring in the membership will be filled by the remaining members.

An authority has the power to issue bonds, approved by the Local Government Commission. The bonds may be secured by the revenues of the regional facility, by security interests in real or personal property, including a leasehold interest, acquired or improved with the proceeds of the bonds, and, with the approval of the county levying the tax, by the receipts of a room occupancy and prepared food and beverage tax levied by the county. A pledge of a county's room occupancy and prepared food and beverage tax does not restrict the county's right to repeal the tax. The faith and credit of the State or a political subdivision of the State may be pledged as security for bonds.

An authority has the power to contract with any public entity. Also, The University of North Carolina or any constituent institution of The University of North Carolina may enter into a contract with an authority if the function is one The University of North Carolina could undertake separately. If a regional facility is used to host an athletic event sponsored by a constituent institution of The University of North Carolina whose principal campus is located in the territorial jurisdiction of the authority, then at least 50% of the seats for the event must be made available to students at that institution and to members of the general public. The act also amends the ABC laws to allow the sale of beer and unfortified wine at a regional facility unless the events being hosted are high school or college functions.

After setting forth the statutory framework for facility authorities, the act specifically creates one in Wake County, to be known as the Centennial Authority. The act authorizes the Director of the Budget to allocate any funds which have been appropriated to the Centennial Authority, but not yet expended or obligated, to the Centennial Authority. The act also amends the Wake County room occupancy and prepared food and beverage tax law to require some distribution of revenue to the Centennial Authority.

Under the new distribution of tax proceeds, Wake County and the City of Raleigh must jointly transfer $11 million to the Centennial Authority by June 30, 1996, and an additional $11 million by June 30, 1997. This money may be used by the Authority only to fund all or part of the acquisition, construction, financing, and debt servicing of a regional facility to be located in the general vicinity of the Carter-Finley stadium. The act also directs Wake County and the City of Raleigh to transfer 7% of the total undesignated proceeds distributed to them to the Centennial Authority by July 1 of each year, beginning July 1, 1995. This money may be used only for enhancement of operating revenues of a regional facility and for planning, design, renovations, maintenance, and repairs to a regional facility. "Undesignated proceeds" are all tax proceeds distributed to Wake County and to Raleigh other than annual distributions to Raleigh of $680,000 of room tax proceeds and $680,000 of meals tax proceeds.

Chapter 459 (Senate Bill 1055, Sen. Kerr)

AN ACT TO MODIFY THE EXCISE TAX ON NEWSPRINT.

This act amends the excise tax on newsprint that was enacted in 1991. The purpose of the tax is to encourage the use of recycled newsprint by imposing a privilege license tax on those who produce publications printed on newsprint and do not use a minimum amount of recycled paper. The tax became effective October 1, 1991, and is payable quarterly. The tax rate is $15.00 for each ton of newsprint that is consumed during a reporting period and has an average recycled content percentage that is less than the required minimum recycled content percentage. The proceeds of the tax are earmarked for the Solid Waste Management Trust Fund created under G.S. 130A-309.12.

Under the law, a publisher must pay the tax unless the recycled content percentage of the newsprint consumed by the publisher equals or exceeds stated percentages.

Under the original legislation, the percentage of required recycled content of the newsprint consumed gradually increased from 12% in 1991 to 40% in 1997. This act eases the burden on publishers to meet these purchasing percentage goals in two ways:

(1) It extends the period of time a publisher has to reach the goal of using newsprint with at least 40% recycled content. Under this act, the percentage increase from 25%, which is the current percentage rate, to 40% would be extended by 3 years to the year 2000.

(2) It creates a credit, that can be used towards the recycled content percentage goals, for publishers who develop and operate or contract for the operation of a newspaper recycling program. A publisher would receive one-half ton credit toward its total recycled content tonnage for each ton of recycling tonnage.

The act also makes a few less substantive changes:

(1) It eliminates the need for filing a quarterly return and substitutes the use of an annual return. To conform with this change, the act directs the Secretary of Revenue to credit the tax proceeds to the Solid Waste Management Trust Fund on or before April 15 of each year.

(2) It changes the term "producer" to "publisher".

(3) It changes the basis for determining the recycled content percentage to gross tonnage of newsprint consumed, instead of net tonnage. The act also clarifies how this calculation is made.

The tax does not apply in a few circumstances. It does not apply to newsprint that is acquired by a publisher and then recycled by the publisher. It also does not apply if the publisher of a publication could not meet the required minimum recycled content standards for one or more of several reasons. The reasons are an inability to obtain newsprint made from recycled paper at a price or quality comparable to other newsprint, in an amount needed for a publication, or in a reasonable amount of time. A publisher who claims an exemption for one of these reasons must document the publisher's effort to obtain newsprint that contained the required minimum percentage of recycled paper.

Chapter 461 (House Bill 1060, Rep. McComas)

AN ACT AMENDING THE GENERAL STATUTES RELATING TO THE CONSOLIDATION OF CITIES AND COUNTIES AND CONSOLIDATED CITY-COUNTY TAXATION AND FINANCE.

This act modifies the law relating to consolidated city-counties, effective July 19, 1995. Article 20 of Chapter 153A of the General Statutes provides a procedure for a city and a county to form a consolidation study commission to adopt a plan of consolidation and to hold a referendum on the consolidation. The consolidation of a city and a county must be enacted by the General Assembly, however, before it can become effective.

Chapter 160B of the General Statutes, the Consolidated City-County Act of 1973, governs consolidated city-counties. A consolidated city-county is a county in which the largest municipality has been abolished and its powers, duties, rights, privileges, and immunities have been consolidated with those of the county. Other municipalities may also be abolished and consolidated with the county. A consolidated city-county may define urban service districts to finance services within the county at a higher level than in other areas of the county. These urban service districts may replace municipalities that have been abolished or may be created to serve areas that have population density, property valuation, and needs that justify a higher level of services than is provided in the county generally. The consolidated city-county may levy property taxes, motor vehicle taxes, and privilege license taxes within an urban service district to finance additional services within the district.

Sections 1 and 2 of this act amend Chapter 160B of the General Statutes to clarify the powers and governance of a consolidated city-county. A consolidated city-county has the same powers, duties, rights, etc., as a county throughout its jurisdiction and as a city within its urban service districts. To the extent a city can exercise powers, duties, rights, etc., outside its boundaries, a consolidated city-county can exercise those powers, duties, rights, etc., outside the boundaries of its urban service districts. The powers, duties, rights, etc., of an urban service district are exercised by the governing body of the consolidated city-county and debts owed an urban service district are payable to the governing body of the consolidated city-county.

This act makes other miscellaneous changes relating to consolidated city-counties. Section 1 provides a procedure for a consolidated city-county to study dissolution and prepare a plan of dissolution. Section 2 provides that, before the effective date of a consolidation, an interim governing board of a proposed consolidated city-county may define an urban service district, which will take effect on the effective date of the consolidation. Sections 2 and 3 provide that a plan for consolidation may include proposed urban service districts and, if the planned consolidation goes into effect, no additional notice is required of the proposed district. Sections 6 - 18 make conforming and technical changes to various statutes relating to taxation, water sewer districts, solid waste, and local government fiscal control to clarify the status of a consolidated city-county.

Sections 4 and 5 make changes that apply only to New Hanover County. In order to comply with the State constitutional requirement in Section 4(1) of Article V that only general, not local, laws may be enacted relating to local government debt, these provisions are made applicable only to a class that includes counties with a population over 120,000 and a land area less than 200 square miles. New Hanover County is the only county in this class. Sections 4 and 5 provide that a consolidation cannot become effective unless the voters of the county have approved the assumption of the city's debt. These sections provide a procedure for the referendum, requirements for assumption of debt and notification, and limitations on actions to contest consolidations.

Chapter 463 (Senate Bill 180, Senator Shaw)

AN ACT TO MODIFY THE PAYMENT AND REPORTING REQUIREMENTS AND THE COLLECTION PROCEDURES FOR UNEMPLOYMENT CONTRIBUTIONS AND TO PROVIDE FOR A REDUCTION IN THESE CONTRIBUTIONS IN CERTAIN CIRCUMSTANCES.

This act makes the following changes in the payment and collection of unemployment contributions:

(1) It increases the minimum payment threshold from $1 to $5. A person is not required to make unemployment contributions if the amount owed is less than the minimum payment threshold. This change becomes effective September 30, 1995.

(2) It increases the unemployment contribution refund threshold from $1 to $5. If a person overpays unemployment contributions by less than the refund threshold, the Employment Security Commission will refund the overpayment only if the person who made the overpayment asks for a refund in writing. This change becomes effective September 30, 1995.

(3) It gives the Employment Security Commission the authority to allow certain small employers to file an annual report rather than quarterly reports and to file the annual report by telephone. The small employers that can be allowed to do this are those that have filed reports with the Commission for at least

the past three years and have not been liable for quarterly contributions for the past year.

For those allowed to make annual reports, the report is due by January 31 of each year. The authority to make an annual report is revoked if the employer becomes liable for contributions or if certain information on the employer's last report changes. To ensure that the Commission has timely employee and wage information, employers filing annual reports must report changes in employment status and wages to the Commission within 14 days and must respond to inquiries from the Commission within 14 days. This change becomes effective September 30, 1995.

(4) It establishes another automatic reduction in unemployment contributions for employers with positive ratings in one circumstance. That circumstance is when the Unemployment Insurance Fund has a balance of at least $800,000,000 and the Unemployment Insurance Fund ratio is at least 5%. The Unemployment Insurance Fund ratio is determined by dividing the amount in the Fund by the State taxable wage base. The current ratio is 4.6% and is not expected to reach or exceed 5% in the next five years. If the fund ratio does reach 5%, the taxes of employers with positive ratings will be reduced by 60% rather than 50%. This change becomes effective for quarters beginning on or after March 31, 1996.

(5) It requires a representative of the Employment Security Commission to attempt to contact a person who owes less than $50 in delinquent unemployment contributions before the Commission obtains a judgment lien for the delinquent amount. This change becomes effective upon ratification.

(6) It eliminates the imposition of a $5 late filing penalty for employers who file a return within 30 days after the due date and owe no tax with the return. This change becomes effective upon ratification.

(7) It removes the current 24-month restriction on waiving penalties. This restriction prohibited the Commission from waiving penalties against the same employer more than once in a 24-month period. Under the act, there is no limit on the number of times a penalty can be waived against the same employer in any time period. This change also becomes effective upon ratification.

Chapter 465 (Senate Bill 407, Sen. Perdue)

AN ACT TO EXEMPT TRAILERS FROM THE PAYMENT OF THE GLOBAL TRANSPARK TEMPORARY ZONE VEHICLE REGISTRATION TAX.

This act exempts trailers from the annual $5 vehicle registration tax imposed in the counties in the Global Transpark Development Zone. The counties in the Transpark Zone are Carteret, Craven, Duplin, Edgecombe, Greene, Jones, Lenoir, Nash, Onslow, Pamlico, Pitt, Wayne, and Wilson counties. The exemption becomes effective October 1, 1995. The exemption will reduce annual revenue for the Transpark Zone by approximately $330,000.

The $5 tax is in addition to the regular vehicle registration fee. When the additional $5 tax was imposed on July 1, 1994, it applied to all trucks, all trailers except mobile homes, and all passenger vehicles registered in a county in the Transpark Zone. When this act becomes effective, the tax will no longer apply to trailers. The regular annual registration fee for a trailer is 10.00.

The vehicle registration tax levied by the Zone is a temporary tax that will expire 5 years after the effective date of the first tax levy, which was July 1, 1994. The Division of Motor Vehicles collects and administers the tax at the same time and in the same manner that it administers the annual vehicle registration fees.

The Commissioner of Motor Vehicles credits the proceeds of the $5.00 temporary Zone vehicle registration tax to a special account. The interest on the special account is credited quarterly to the Highway Fund to reimburse the Division for the cost of collecting and administering the tax. The Zone must place 15% of the tax proceeds distributed to it in a general funds account and the remaining 85% in an interest-bearing trust account. The Zone may not disburse the principal of the trust account except pursuant to a contract that provides that the Zone will recover or be repaid the amount disbursed within a reasonable period of time, not to exceed 20 years. Each county that is a member of the Zone is the beneficial owner of a share of the principal of the trust account in proportion to the amount of tax proceeds collected in that county.

The enactment of this act makes the vehicle base for the Triangle Transit Authority different from the vehicle base for the Global Transpark. The $5 vehicle registration tax imposed by the Triangle Transit Authority applies to trailers.

Chapter 468 (Senate Bill 121, Sen. Kerr)

AN ACT TO REVISE THE PROCEDURES FOR ASSESSMENTS OF INHERITANCE TAX FOLLOWING A FEDERAL DETERMINATION.

This act makes 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. The act became effective August 1, 1995. The original bill, recommended by the Revenue Laws Study Committee, would also have reduced inheritance and gift taxes in a number of ways.

The act makes 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: it revises 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 in order to allow the State adequate time to respond to the federal determination. The State might 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, prior to the enactment of this act, did not give the State any additional time to make an assessment following a federal determination. Therefore, for an assessment of inheritance tax, the State had to make an assessment within the general three-year time period for making assessments. When the State did 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 was foreclosed from making an assessment.

Chapter 472 (House Bill 759, Rep. Gray)

AN ACT TO PROVIDE THAT A HOME FOR THE AGED, SICK, OR INFIRM WHOSE PROPERTY IS EXEMPT FROM PROPERTY TAX IS ALLOWED A REFUND OF STATE AND LOCAL SALES AND USE TAXES.

This act allows certain nonprofit homes for the aged, sick, or infirm to obtain semiannual refunds of State and local sales and use taxes paid by the homes. The act became effective upon ratification and applies retroactively to purchases made on or after January 1, 1995. The refunds will reduce General Fund revenue by approximately $1.5 million a year and they will reduce local government revenues by approximately $.7 million a year.

The homes covered by the act are those whose property is exempt from property taxes under G.S. 105-275(32). That provision exempts the property of church-related and Masonic continuing care retirement homes from property tax. The homes that qualify are nonprofit self-contained communities that meet the following qualifications:

(1) Are designed for elderly residents.
(2) Operate a skilled nursing facility, an intermediate care facility, or a home for the aged.
(3) Include residential dwelling units, recreational facilities, and service facilities.
(4) Have a charter that provides that in the event of dissolution, the assets of the home will revert or be conveyed to a nonprofit entity.
(5) Are managed by a church or other religious body or a Masonic group.
(6) Have an active program to generate funds through one or more sources, such as gifts, grants, trusts, bequests, an endowment, or an annual giving program, to assist the home in serving persons who might not be able to reside at the home without financial assistance or subsidy.

In exempting these homes from sales and use taxes, the act resolves lingering issues from a 1984 property tax case. Before 1984, the Department of Revenue allowed sales and use tax refunds to these homes as nonprofit charitable or religious institutions. In 1984, the Court of Appeals upheld a decision of the Property Tax Commission denying a property tax exemption to Lutheran Home Ministries on the basis that it was not a charitable institution. The General Assembly responded to the court's ruling by granting these homes a property tax exemption in 1987 under G.S. 105-275(32).

The Department of Revenue applied the court's reasoning to sales and use taxes and denied sales and use tax refunds to some of these homes beginning in 1984. Because the 1987 legislation did not change the sales and use tax laws, the Department continued to deny refunds to some of these homes based upon the 1984 Court of Appeals decision. This act clarifies that homes that are exempt from property tax as charitable institutions are also entitled to a refund of sales and use taxes. The General Assembly ratified this act on July 25, 1995. Subsequently, on August 1, 1995, the Court of Appeals issued a decision finding that these homes are entitled to a refund of sales and use taxes. The case before the court concerned whether or not Southminster, Inc. and Davidson Retirement Community, Inc. were charitable organizations and as such were entitled to a semiannual refund of sales and use taxes. The court found that the two institutions were charitable organizations, based partially on the fact that they are considered charitable organizations for property tax purposes under G.S. 105-275(32).

Chapter 474 (House Bill 223, Rep. Gray)

AN ACT TO REDUCE THE EXCISE TAX ON SOFT DRINKS.

This act reduces the State excise tax on soft drinks by 25% effective July 1, 1996. It does not phase out the soft drink tax, as did the original version of House Bill 223.

The act reduces the excise tax on bottled soft drinks from 1¢ a bottle to 3/4¢ a bottle, reduces the excise tax on liquid base products from $1.00 a gallon to 75¢ a gallon, and reduces the excise tax on dry base products from 1¢ an ounce to 3/4¢ an ounce. It preserves the current 1/2 rate of tax on the first 15,000 gross of bottled soft drinks sold each year by a distributor. The act is expected to reduce soft drink tax revenue by $9.6 million in fiscal year 1996-97 and $10.1 million in 1997-98.

The soft drink excise tax was enacted in 1969. The purpose of the tax is to provide an additional source of revenue to the General Fund. In fiscal year 1993-94, the soft drink excise tax accounted for $36,538,688 of the General Fund tax collections. A soft drink is defined as a beverage that is not an alcoholic beverage. The following items are exempt from the tax:

(1) Natural liquid milk drink produced by a farmer or a dairy.
(2) A bottled soft drink that contains at least 35% natural milk.
(3) Natural juice.
(4) Juice that would be natural if it did not contain sugar.
(5) Natural water.
(6) A base product used to make a bottled soft drink subject to tax under this Article.
(7) Coffee or tea in any form.
(8) A bottled soft drink or base product sold outside the State.
(9) A bottled soft drink or base product sold to the federal government.
(10) A base product for home use that either contains milk or requires milk to be added to make a soft drink.

The soft drink excise tax is payable by the person who is the first to bring the product into the State. The soft drink excise tax has a bifurcated tax rate system. The purpose of the bifurcated tax system is to tax the sale or distribution of the soft drink itself when practical, but to tax the sale or distribution of the ingredients of the soft drink when the taxation of the product itself is not practical.

Chapter 477 (House Bill 55, Rep. Redwine)

AN ACT TO PROVIDE THAT SALES TAX PREFERENCES FOR AGRICULTURE APPLY TO AQUACULTURE.

This act clarifies the application of two sales and use tax agricultural preferences to farmers who raise fish or water plants and expands a current agricultural sales and use

tax exemption to include this type of farmer. The act became effective August 1, 1995. The act is projected to reduce annual State sales and use tax collections by less than $50,000 and to reduce annual local sales and use tax collections by less than $25,000. The act was recommended by the Joint Legislative Commission on Seafood and Aquaculture.

A sales and use tax preference is the exemption of an item from sales and use tax or the taxation of an item at less than the regular 6% combined State and local rate. The two sales and use tax preferences the act clarifies are the taxation of certain items at the rate of 1% with an $80 cap and the exemption of certain items used in agriculture.

Section 1 of the act makes it clear that machines and machine parts sold to a farmer for use in raising an aquatic species are taxable at the State rate of 1% with an $80 cap rather than at the full State and local 6% rate. An aquatic species is any species of finfish, mollusk, crustacean, or other aquatic invertebrate, amphibian, reptile, or aquatic plant. The Department of Revenue has construed "farm crops" in this category to include aquatic species. The act therefore clarifies the application of this reduced rate to fish farmers rather than include them in the reduced rate for the first time.

Section 2 of the act makes it clear that the agricultural exemptions in G.S. 105-164.13(2) apply to aquatic species farmers and that all the exemptions in this subdivision, other than the one for seeds, are limited to commercial production. It does this by changing references to "livestock and poultry" to "animals," by changing references to "agriculture" to the "commercial production of plants or animals," and by inserting a statement that the items must be for commercial use. The exemptions are for medicine, litter material, feed, pesticides and similar products, defoliants, and plant growth regulators.

The Department of Revenue has construed "livestock" in the exemptions in G.S. 105-164.13(2) to include fish and has for many years interpreted the exemptions for all items in this subdivision, other than seeds, to apply to commercial use only. The act therefore clarifies these exemptions and their application to aquaculture.

In addition to clarifying these two sales and use tax preferences, the act expands the agricultural exemption in G.S. 105-164.13(4c) for certain kinds of facilities and equipment to include fish facilities and equipment. Prior law exempted facilities for commercial use in housing, raising, or feeding swine, livestock, or poultry, equipment used in these facilities, and building materials used to construct these facilities. "Livestock" under this exemption had not been interpreted to include fish. Section 3 of the act expands this exemption to include fish by deleting references to "swine, livestock, and poultry" and referring instead to "animals." This exemption applies to both State and local sales and use taxes

Chapter 491 (Senate Bill 1049, Sen. Sherron)

AN ACT TO CLARIFY THE QUALIFIED BUSINESS TAX CREDIT TO ELIMINATE AN UNINTENDED LOOPHOLE THAT ALLOWS DOUBLE CREDITS FOR THE SAME INVESTMENT AND TO AUTHORIZE THE LEGISLATIVE RESEARCH COMMISSION TO STUDY THE QUALIFIED BUSINESS TAX CREDIT.

This act addresses a loophole in the Qualified Business Investment tax credit by prohibiting an investor from receiving two tax credits on the same investment. The act also authorizes the Legislative Research Commission to study the tax credit.

In 1987, the General Assembly enacted the Qualified Business Investment tax credit to allow tax credits to individuals and corporations that invest in qualified North Carolina businesses registered with the Secretary of State or in North Carolina Enterprise Corporations. The amount of the credit allowed is 25% of the amount invested, up to a maximum credit of $50,000 for individuals and $750,000 for corporations. If the allowable credit exceeds the taxpayer's tax liability, the excess may

be carried forward for five years. The total amount of tax credits that can be granted in any tax year is capped at $12 million. The investors apply for the credit through an application filed with the Department of Revenue by April 15; the Department then determines whether the $12 million cap has been exceeded and, if so, proportionally reduces the amount of each credit applied for.

In 1993, the General Assembly enacted legislation to allow a pass-through entity to qualify for the credit and pass it on to the entity's owners. A pass-through entity is an entity, such as a partnership, a limited liability company, or a Subchapter S corporation, that is treated as owned by individuals or other entities under federal tax law and whose income, losses, and credits are reported by the owners on their State income tax returns.

The law allowing pass-through entities to qualify for this credit became effective with the 1994 tax year. A problem arose because an investor could invest money in a pass-through entity that is itself a qualified business. The investor would receive a 25% tax credit for this investment and, if the pass-through entity then invests in another qualified business, the original investor would receive a second 25% tax credit, via the pass-through entity, based upon the original financial investment. Section 1 of this act, recommended by the Secretary of State, eliminates this problem by prohibiting a pass-through entity that is also a qualified business from passing the tax credit through to its owners. Therefore, the investor's initial investment in the pass-through entity will qualify for the 25% tax credit but the entity's subsequent investment in another qualified business will not qualify for an additional tax credit for the original investor.

Section 1 will have an unknown effect on General Fund revenues. This section became effective beginning with the 1995 tax year; in order to protect investments made in reliance on the current law, it does not apply to investments and commitments to invest made before August 1, 1995.

Section 2 of the act authorizes the Legislative Research Commission to study the Qualified Business Investment tax credit, in particular to consider how the law can be modified to better encourage venture capital investment in North Carolina. The Commission may make an interim report to the 1996 Session and must make a final report to the 1997 General Assembly.

Chapter 495 (House Bill 396, Rep. McComas)

AN ACT TO MODIFY THE STATE PORTS TAX CREDIT BY EXPANDING IT TO INCLUDE IMPORTS, BY EXTENDING THE SUNSET ON THE CREDIT, AND BY LIMITING THE CREDIT FOR BULK EXPORTS.

This act modifies the income tax credit allowed for amounts assessed by the State ports in three ways. The act was an agency bill requested by the State Ports Authority. The modifications, outlined below, became effective for taxable years beginning on or after January 1, 1995:

(1) It expands the credit to include imports; the current credit applies only to exports. The act allows a credit for break-bulk cargo and container cargo imported at either Wilmington or Morehead City and for bulk cargo imported at Morehead City. The act does not allow a credit for bulk cargo imported at Wilmington.

(2) It limits the credit for bulk exports to bulk exports at the Morehead City terminal. The current export credit applies to bulk exports at Wilmington as well as at Morehead City.

(3) It extends the sunset on the credit for two years. Under prior law, the credit would have expired for taxable years ending on or before February 28, 1996. Under this act, the credit will expire for taxable years ending on or before February 28, 1998.

The State ports income tax credit was enacted in 1992 and expanded in 1994. It was enacted to encourage exporters to use the two State-owned port terminals, which are at Wilmington and Morehead City. When enacted, the credit applied to amounts paid by a taxpayer on cargo exported at either port. The General Assembly expanded the credit in 1994 to include all amounts assessed on exported cargo, regardless of who paid the shipping costs.

The amount of credit allowed is equal to the amount of charges assessed on a taxpayer's cargo that exceeds the average amount assessed on the taxpayer's cargo during the three-year period that includes the current taxable year and the previous two taxable years. The credit may not exceed 50% of the amount of income tax owed by the taxpayer for the taxable 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 allowed to the same taxpayer may not exceed $1 million.

Chapter 510 (Senate Bill 693, Sen. Kerr)

AN ACT TO MAKE TECHNICAL AMENDMENTS TO IMPROVE THE ADMINISTRATION OF THE PROPERTY TAX ON MOTOR VEHICLES.

This act makes various technical changes to the statutes concerning the property tax on motor vehicles. The changes are effective for taxes imposed for taxable years beginning on or after July 1, 1995. The changes were suggested by a committee of assessors, collectors, and finance officers as amendments that would improve the administration of the tax. The act has no fiscal effect.

In 1991, the General Assembly created a new procedure for collecting property taxes on motor vehicles that are registered with the Division of Motor Vehicles. Under the system, the registration of a motor vehicle with the Division of Motor Vehicles is considered a listing of the vehicle for property tax purposes and the taxes payable on the vehicle are due four months after the registration is obtained or renewed. If the taxes are not paid within four months after they become due, the Division of Motor Vehicles will refuse to renew the vehicle's registration the following year unless the taxpayer obtains a receipt showing that the previous year's taxes have been paid.

The amendments to the motor vehicle property tax statutes are as follows:

Section	Explanation
1	The changes in subsection (a) of G.S. 105-330.2 eliminate the problem of the correct evaluation date when an owner with a registration that expires December 31 renews during the January grace period. Under the amendment, the value of the vehicle is determined as of January 1 preceding the date the current registration expires. The ownership, situs, and taxability of the vehicle are determined on the actual day the current registration is renewed. The change in subsection (b) deletes taxability and situs from the requirement that appeals must be taken within 30 days of the date of the notice. Because of incorrect information in DMV records, many situs appeals must be handled more than 30 days after the date of the notice. Under the amended statutes, appeals of situs and taxability will be handled under G.S. 105-381, which allows a taxpayer to contest the situs and taxability within 6 months of the date of payment or within 5 years after the tax first became due, whichever is later.
2	The change in subsection (a) of G.S. 105-330.4 establishes a new procedure for prorating taxes on vehicles registered under the annual system. Currently, when a vehicle is first registered under the annual system in a month other than December, no taxes are due on that vehicle

until after the registration is renewed. This amendment makes prorated taxes due on that vehicle four months after it is registered.

The change in subsection (b) postpones the accrual of interest when, for whatever reason, the tax notice is not prepared until some time after the tax due date for a vehicle. In such a case, the amendment provides that interest will begin to accrue on the first day of the second month following the date of the notice, rather than on the first day of the first month following the date the taxes were due.

3 A new subsection (a1) is created in G.S. 105-330.5 that establishes a formula for prorating taxes on vehicles registered under the annual system. For example, if a new registration is obtained in July, five months remain in the calendar year, so the taxes on that vehicle would be 5/12 of the full amount. These taxes would be due November 1, four months after the date the vehicle is registered.

The amendment to subsection (b) requires a county to remit municipal and special district taxes at least once a month rather than the current 30 days after collection. It also requires the county to furnish municipalities and special districts located in it information that will enable them to account for the tax payments remitted to them.

The amendment to subsection (d) changes the rule concerning the levy year in which a tax is to be included when the notice is prepared after the tax due date. For example, under the current law, if a tax is due June 1 but the notice is prepared in August, the tax must still be included in the previous fiscal year's levy. Under the amendment, the tax would be included in the levy for the current fiscal year.

4 The amendment to subsection (a) of G.S. 105-330.6 establishes a tax year for vehicles registered under the annual system that is based on a January 1 - December 31 calendar year. The addition of this tax year is needed to deal with prorated refunds and releases of prorated taxes due on annual system registrations.

The amendment to subsection (c) increases the time a taxpayer has to request a refund or release of taxes after surrendering the vehicle's plates from 60 days to 120 days.

Chapter 512 (House Bill 1001, Rep. Allred)

AN ACT TO PROVIDE THAT ANTIQUE AUTOMOBILES SHALL BE VALUED AT NO MORE THAN FIVE HUNDRED DOLLARS FOR PROPERTY TAX PURPOSES AND TO ELIMINATE DOUBLE TAXATION OF A MOTOR VEHICLE WHEN THE OWNER MOVES AWAY AND THEN RETURNS TO THE STATE WITHIN ONE YEAR.

This act combines two bills that were considered by the General Assembly this session. The original bill, House Bill 1001, reduces the amount of property tax collectors of antique vehicles must pay by limiting their value to no more than $500 for property tax purposes. The Senate amended the bill to include the contents of Senate Bill 170, which eliminates the highway use tax on a motor vehicle when the owner moves away and then returns to the State within one year. The first part of the act will result in an annual local government revenue loss of less than $700,000. The second part of the act will result in a maximum annual loss to the Highway Trust Fund of approximately $15,000.

Antique automobiles

Under this act, antique automobiles owned by collectors will be effectively exempt from property tax, effective for taxable years beginning on or after October 1, 1995. A vehicle qualifies for this exemption if it meets all of the following conditions:

1. It is registered with the Division of Motor Vehicles and has an historic vehicle special license plate. To be qualify for an historic vehicle special license plate, a vehicle must be 35 years old from the date of manufacture. The annual license plate fee for an historic vehicle special license plate is the regular license fee plus an additional $10.00.
2. It is maintained for use in exhibitions, club activities, parades, and other functions of public interest.
3. It is used only occasionally for other purposes.
4. It is owned by an individual.
5. It is used by the owner for a purpose other than the production of income and is not used in connection with a business.

Motor vehicles are designated as a special class of property under G.S. 105-330.1. Vehicles that are registered with the Division of Motor Vehicles are taxed annually as of the day on which the current registration is renewed or the day on which a new registration is applied for. Under Chapter 329, ratified by the General Assembly this session, a local government may adopt a resolution directing the tax collector not to collect property taxes when the amount due is less than $5.00. Few, if any, taxing units have a property tax rate that exceeds $1.00 per $100 of value. Therefore, since the value of the car can not exceed $500 under this act, any unit that adopts a resolution allowing the tax collector to forego collection of property tax bills that are less than $5.00 will effectively eliminate property taxes on antique automobiles owned by collectors.

Personal property that is used by the owner of the property for a purpose other than the production of income and that is not used in connection with a business has been exempt from property taxes since 1987. Personal property includes household furnishing, clothing, pets, and lawn equipment. The term also includes collectibles such as antiques, coins, and paintings. However, the term does not include motor vehicles.

Eliminate double vehicle tax

Effective October 1, 1995, a motor vehicle owner will be allowed a credit against the highway use tax for the amount of highway use tax paid on the same vehicle within the past year. This credit is available only to a person who applies for a certificate of title for a motor vehicle that is titled in another state. The effect of the act is to relieve a person from paying the highway use tax if, within a single year, a person paid the highway use tax in this State, moved to a different state and titled the motor vehicle in that state, and then moved back to North Carolina and titled the vehicle in this State.

The highway use tax is a titling tax that is collected whenever a certificate of title is issued. A resident of North Carolina is required to have a certificate of title for each vehicle the resident owns that is operated on the highways. The highway use tax is 3% of the value of the vehicle, subject to a maximum tax of $1,500 and a minimum tax of $40 until July 1, 1996. Beginning July 1, 1996, the minimum tax is repealed.

Under current law, there are two provisions for motor vehicles brought into North Carolina from another state. Under G.S. 105-187.6, the maximum highway use tax that maybe imposed on a vehicle that has been titled in another state for at least 90 days is $150.00. Under G.S. 105-187.7, a person is allowed a credit against the highway use tax for the amount of a substantially equivalent tax imposed and paid to another state within 90 days before applying for a certificate of title.

Chapter 533 (Senate Bill 710, Sen. Kincaid)

AN ACT TO INCREASE THE NORTH CAROLINA SELF-INSURANCE GUARANTY FUND AND TO ALLOW A CREDIT AGAINST THE GROSS PREMIUMS TAX FOR ASSESSMENTS PAID BY SELF-INSURERS TO THE GUARANTY FUND.

This act represents one part of a two-part plan to address the self-insured workers compensation market. At the present time, over 55% of the employees in the State have workers compensation coverage through either self-funded plans or pools. These plans or pools are currently unregulated by the Department of Insurance and several are skirting potential insolvency. This act seeks to put the Self-Insurance Guaranty Fund in a better position that it currently is to pay claims if insolvencies occur. The second part of the plan was embodied in Senate Bill 931, ratified as Chapter 471 of the 1995 Session Laws. Under that act, the Department of Insurance was given more regulatory oversight over the self-insured plans or pools. That part of the plan seeks to decrease the risk of insolvencies among this group of insurers.

Under this act, the Self-Insurance Guaranty Fund cap is raised from $1,000,000 to $5,000,000. The Fund is financed by assessments paid by self-insurers. These assessments represent .25% of the self-insurers premiums tax base. The assessment is credited toward the insurers premium tax liability. As such, any assessments paid by self-insurers are deducted from their tax payments and represent a loss to the General Fund. The act is expected to decrease General Fund revenues $1.8 million in fiscal years 1995-96 and 1996-97 and $400,000 in fiscal year 1997-98. It is assumed that the $5,000,000 cap will be reached within three years and that continued assessments beyond the third year will not be needed.

The assessments paid by self-insurers to the Self-Insurance Guaranty Fund differ from the assessments paid by private insurers in two respects:

(1) The assessment is paid to the State. The amount assessed is "diverted" from gross premium tax revenue. With private insurers, the assessment is paid to the private Guaranty Fund. The premium tax liability is not affected. However, the General Assembly allows a credit against an insurer's premium tax liability equal to the amount paid by the insurer to the Guaranty Fund.

(2) The amount paid as an assessment is determined by the State. Therefore, the amount of potential loss to the General Fund is more fixed.

Chapter 543 (Senate Bill 202, Sen. Albertson)

AN ACT TO ENCOURAGE THE COMPOSTING OF POULTRY CARCASSES AND PROVIDE AN INCOME TAX CREDIT FOR POULTRY COMPOSTING FACILITIES.

This act creates a temporary income tax credit for constructing a facility in this State for the composting of poultry carcasses resulting from commercial poultry operations. The credit is available only to individuals and shareholders in Subchapter S corporations; it is not available to C corporations. The amount of the credit allowed is 25% of the installation, equipment, and materials cost of building the facility, not to exceed $1,000. The credit does not apply to costs paid with funds provided to the taxpayer by a State or federal agency. The amount of the credit allowed cannot exceed the amount of tax imposed for the taxable year.

The credit is effective for taxable years beginning on or after January 1, 1995, and expires for taxable years beginning on or after January 1, 1998. The yearly General Fund revenue loss from the credit is not expected to exceed $350,000.

A poultry composting facility is a structure or an enclosure in which whole, unprocessed poultry carcasses are decomposed by a natural process into an organic, biologically safe by-product that can be used for plant food. Every person that is engaged in raising poultry for commercial purposes and has a flock of at least 200 fowl

is required by G.S. 106-549.70 to dispose of the poultry carcasses in a pit, an incinerator, or a poultry composting facility that has been approved by the Department of Agriculture.

The purpose of the credit is to encourage people who raise turkey, chickens, or other poultry to compost the dead poultry rather than burn it or put it in a pit. By composting the poultry carcasses, the by-product can be converted into a useful product.

In the poultry business, the grower of a bird is often not the owner of the bird. The burden of disposing of poultry mortalities is usually on the grower of the bird.

Recommended by the Agriculture and Forestry Awareness Study Commission.

APPENDIX D

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January 5, 1996

MEMORANDUM

TO: Revenue Laws Study Committee

FROM: Myra M. Torain, Legal Analyst

SUBJECT: Bills Recommended to the 1995 Session 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 1995 General Assembly. A majority of the committee's recommendations became law. Of the sixteen proposals, ten were enacted in whole or in part, or incorporated into other bills. Four are pending and eligible for consideration in the 1996 Regular Session. The two remaining recommendations are not eligible for consideration in the 1996 Regular Session.

Legislative Proposal 1: Enacted in part

Senate Bill 121, 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, was introduced by Senator Kerr and was ratified as Chapter 468 of the 1995 Session Laws, AN ACT TO REVISE THE PROCEDURES FOR ASSESSMENTS OF INHERITANCE TAX FOLLOWING A FEDERAL DETERMINATION. The original portion of the bill that would have reduced inheritance and gift taxes was deleted by a Senate committee substitute. The remaining portion

of the original bill, which makes the time limits for assessing inheritance tax due after a federal determination the same as the time limits applicable to assessments of other state taxes following a federal determination, was left intact and enacted.

Legislative Proposal 2: Enacted

House Bill 123, AN ACT TO REVISE THE CONTROLLED SUBSTANCE EXCISE TAX, was introduced by Representative Arnold and after some modification was ratified as Chapter 340 of the 1995 Session Laws.

Legislative Proposal 3: Not eligible

House Bill 138, AN ACT TO PROHIBIT THE SALE OF LOOSE, UNPACKED CIGARETTES, was introduced by Representative Braswell and reported to the House Committee on Business and Labor.

Legislative Proposal 4: Pending

House Bill 245, 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, was introduced by Representative Luebke and was referred to the House Committee on Finance.

Legislative Proposal 5: Pending

House Bill 244, AN ACT TO REDUCE THE CORPORATE INCOME TAX, was introduced by Representative Luebke and referred to the House Committee on Finance.

Legislative Proposal 6: Enacted

Senate Bill 120, AN ACT TO PROVIDE UNIFORM TAX TREATMENT OF NORTH CAROLINA OBLIGATIONS AND FEDERAL OBLIGATIONS, was introduced by Senator Kerr and enacted as Chapter 46 of the 1995 Session Laws.

Legislative Proposal 7: Enacted

House Bill 80, AN ACT TO REPEAL THE SPECIAL USE TAX ON CONSTRUCTION EQUIPMENT BROUGHT INTO THE STATE, was introduced by Representative Tallent and enacted as Chapter 7 of the 1995 Session Laws.

Legislative Proposal 8: Pending

Senate Bill 103, 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, was introduced by Senator Cochrane and was re-referred to the Senate Committee on Appropriations.

Legislative Proposal 9: Pending

House Bill 94, AN ACT TO EXEMPT FROM SALES AND USE TAX FREE SAMPLES OF PRESCRIPTION DRUGS DISTRIBUTED BY THE MANUFACTURER, was introduced by Representative Gamble and was referred to the House Committee on Finance.

Legislative Proposal 10: Enacted

Draft Bill, 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, was not introduced. Senate Bill 8, a similar bill, was introduced by Senator Kerr and enacted as Chapter 41 of the 1995 Session Laws, AN ACT TO REPEAL THE INTANGIBLES TAX AND TO REIMBURSE LOCAL GOVERNMENTS FOR THEIR RESULTING REVENUE LOSS.

Legislative Proposal 11: Enacted

House Bill 122, 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, was introduced by Representative Arnold. After some modification, it was enacted as Chapter 50 of the 1995 Session Laws, AN ACT TO EXPAND THE ALLOWABLE USES OF TRANSPORTER PLATES, TO ALLOW OWNERS OF SALVAGE VEHICLES TO RETAIN TITLE TO THE VEHICLES, AND TO EXEMPT OUT-OF-STATE UTILITY VEHICLES THAT

APPENDIX E

Summary of remarks to the Revenue Laws Study Committee, January 5, 1996
Charles D. Liner, Institute of Government

Revenue Policy: What is a "good" revenue source?

There are several widely-accepted criteria, or standards, by which revenue sources can be judged: (1) fairness in the distribution of burdens; (2) responsiveness of revenues to growth in income, population, and inflation; (3) stability; (4) economic neutrality; (5) low cost and ease of administration; and (6) suitability to the unit of government.

1. Fairness

Fairness is the paramount criterion. The purpose of a revenue system is to distribute the cost of government services among the people in a fair and equitable manner. North Carolina's constitution requires that "the power of taxation shall be exercised in a just and equitable manner..."

There are two widely-accepted principles of fairness. The first is the benefits-received principle, which requires that those who benefit more than others from government services should pay more. For example, highways and roads are financed through benefits-related taxes and fees, and charges are used to finance such services and water and sewer, higher education (tuition charges), and medical care in public health facilities. Municipal revenue sources such as municipal property taxes are also based on this principle, since municipal residents pay an extra property tax for the additional services provided by their municipal governments.

The second principle is the ability to pay principle--government services that provide benefits to the people of the state as a whole, or to a community as a whole, should be financed from general taxes whose burden in relation to taxpayers' ability to pay is fair and equitable.

The latter principle has two subordinate principles. The first is horizontal equity--people who have the same ability to pay should pay the same amount. The second is vertical equity--those who have a greater ability to pay should pay more than those who have a lesser ability to pay. Vertical equity is assessed according to the amount of taxes or charges relative to income. If higher income taxpayers pay proportionately more than lower income taxpayers, the burden is "progressive" with respect to ability to pay. If lower income taxpayers pay proportionately more of their income than others, the burden is "regressive" with respect to ability to pay.

Estimates of vertical equity of the major North Carolina taxes were shown for representative families at different income levels. The estimates show that the state income tax is progressive, while the retail sales tax, property tax, and gasoline tax (like other excise taxes) tend to be regressive, in varying degrees.

The total burden of the major state taxes on individuals appears to be moderately progressive, while the combined burden of local property and retail sales taxes appears to be moderately regressive. According to these estimates, the combination of the state and local taxes estimated for representative families suggests that the overall burden of major state and local taxes paid by individuals is slightly progressive.

2. Responsiveness

As incomes, population, and prices increase, demand for government services and the cost of providing services increase, so revenues should grow along with growth in the economy and population and with inflation. Of the major taxes, the personal income tax is relatively responsive to growth in personal income, while retail sales and corporate income taxes tend to grow somewhat less than does personal income. The property tax has tended to grow about in proportion to income growth. Excise taxes such as gasoline, cigarette, and soft drink taxes tend to be very unresponsive to growth in personal income.

3. Stability

Revenues should not fluctuate greatly with economic cycles or other factors. Local governments in particular must be able to count on stable revenues during the budget year.

4. Economic neutrality

Revenue sources should not interfere unnecessarily with economic decisions of individuals and business firms. However, some taxes, such as tobacco and alcoholic beverage taxes, might be intended to affect such decisions.

5. The cost and ease of administration

The costs of administering a revenue source should not be unduly costly or burdensome, either to government or to taxpayers.

6. Suitability to the unit of government

Some revenue sources might be suitable for the state but not for local governments (and vice versa), and some might be suitable for municipalities but not for counties (and vice versa).

Don Liner
For the Revenue Laws
Study Committee
January 5, 1996

Revenue Policy: What is a "good" revenue source?

1. The Paramount Criterion: Fairness

The purpose of a revenue system is to distribute the cost of government services among the people in a fair and equitable manner. North Carolina's constitution requires that "the power of taxation shall be exercised in a just and equitable manner..."

There are two widely-accepted principles of fairness:

The benefits-received principle. Those who benefit more than others from government services should pay more.

The ability-to-pay principle. Government services that provide general benefits to the people of the state as a whole or to a community as a whole should be financed from general taxes whose burden in relation to taxpayers' ability to pay is fair and equitable. Two subordinate principles are:

Horizontal equity. People who have the same ability to pay should pay the same amount.

Vertical equity. Those who have a greater ability to pay should pay more than those who have a lesser ability to pay. But how much more should higher-income taxpayers pay than lower-income taxpayers? Should they pay in *proportion* to their income? Or should higher-income taxpayers pay a higher percentage of their income--in which case the tax is "*progressive*" with respect to ability to pay. A tax that imposes a higher relative burden on lower-income taxpayers is "*regressive*" with respect to ability to pay.

2. Responsiveness--do revenues grow with income, population, and inflation?

As incomes, population, and prices increase, demand for government services and the cost of providing services increase, so revenues should grow along with growth in the economy and with inflation.

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Revenues should not fluctuate greatly because of economic cycles or other factors. Local governments in particular must be able to count on revenues during the budget year.

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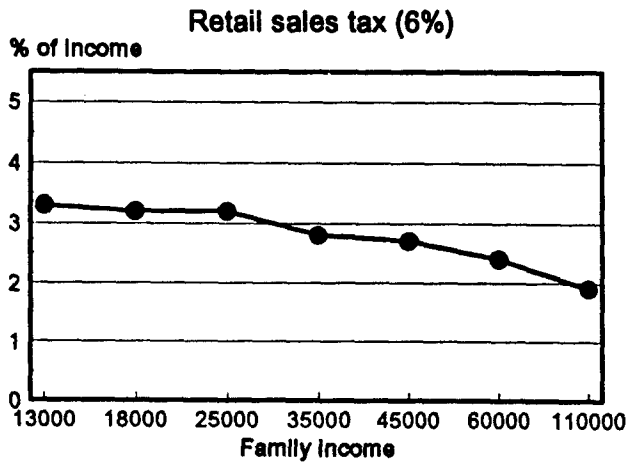
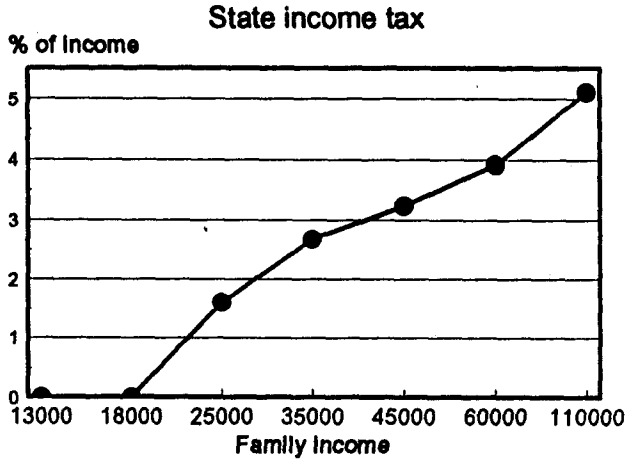
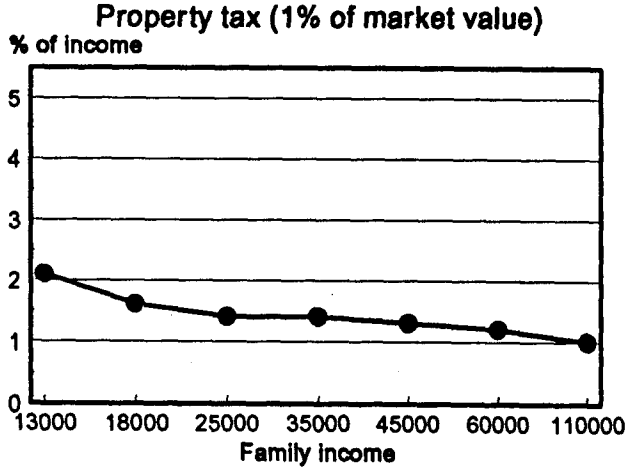
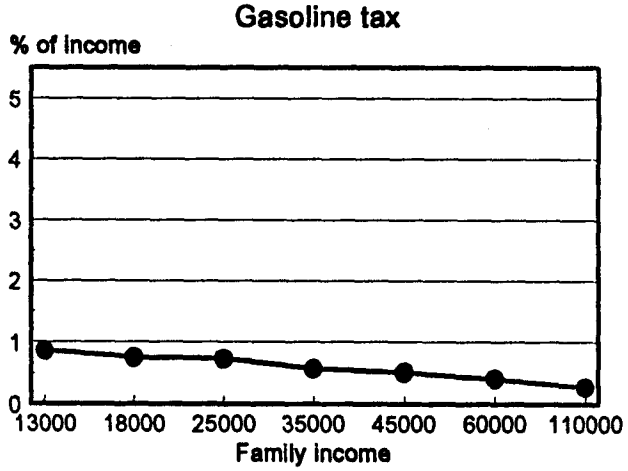
Some revenue sources might be suitable for the state but not for local governments (and vice versa), and some might be suitable for municipalities but not for counties (and vice versa).

North Carolina Taxes as a Percentage of Income for Representative Families



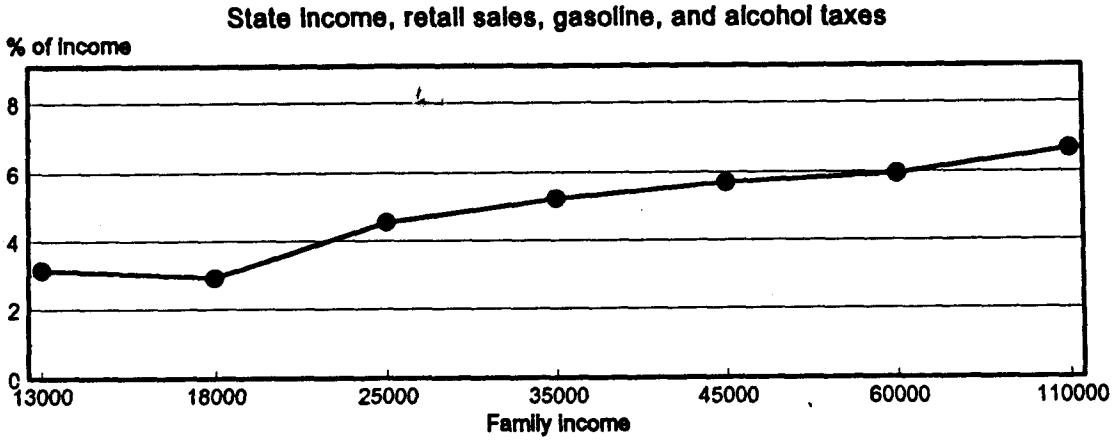


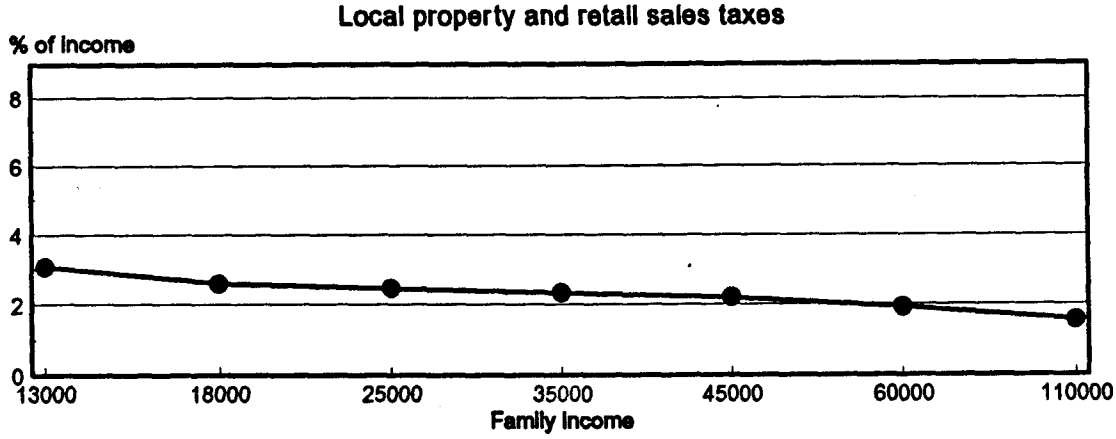


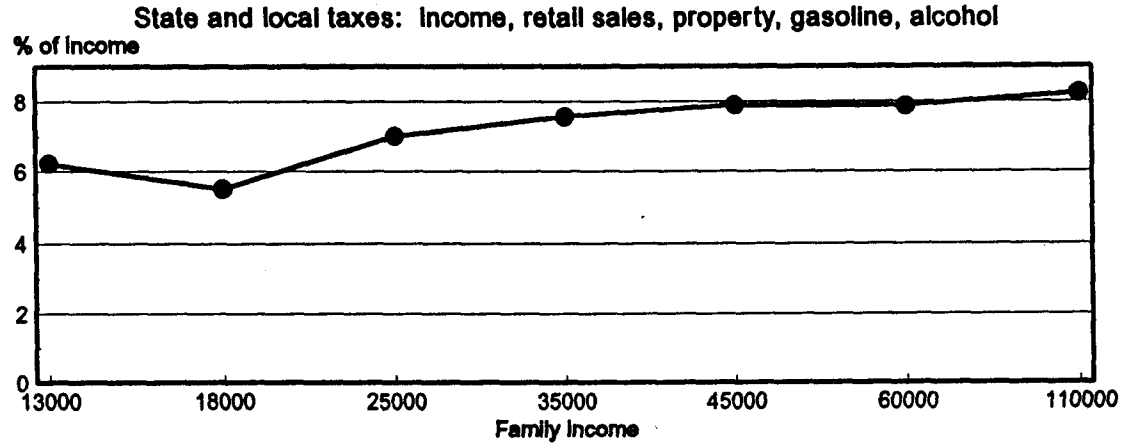


Notes: Estimates are based on the Consumer Expenditure Survey, 1993, Bureau of Labor Statistics, U.S. Department of Labor. Prepared by Don Liner, Institute of Government, December 1995.

State and Local Taxes as a Percentage of Family Income of Representative Families







Prepared by Don Liner, Institute of Government, December 1995.

APPENDIX F

WHAT ARE THE HALLMARKS OF A GOOD STATE AND LOCAL TAX SYSTEM?

Presentation to the Revenue Laws Study Commission

February 9, 1996

Dan Gerlach
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WHAT ARE THE HALLMARKS OF A GOOD TAX SYSTEM?

- **EQUITY**

  Do taxpayers with the same resources pay the same in taxes?

  Do taxpayers with greater resources pay more than those with less resources?

  Do taxpayers who benefit from services pay more than those who benefit less?

- **STABILITY**

  Are tax revenues sufficient enough to pay for adequate public services?

  Do public officials save money in good times to offset the need for tax increases during bad times?

  Do tax rates need constant tinkering, or do tax revenues respond to economic growth?

- **NEUTRALITY**

Are taxes broad-based, or are there an abundance of credits, exemptions, deductions?

Do the tax system overtly interfere with economic decision-making, except where there are market failures?

NORTH CAROLINA'S TAX SYSTEM

For Individuals:

- **State & Local Tax System is fairly flat to moderately regressive across all income levels - better than most states, due to low reliance on property taxes;**

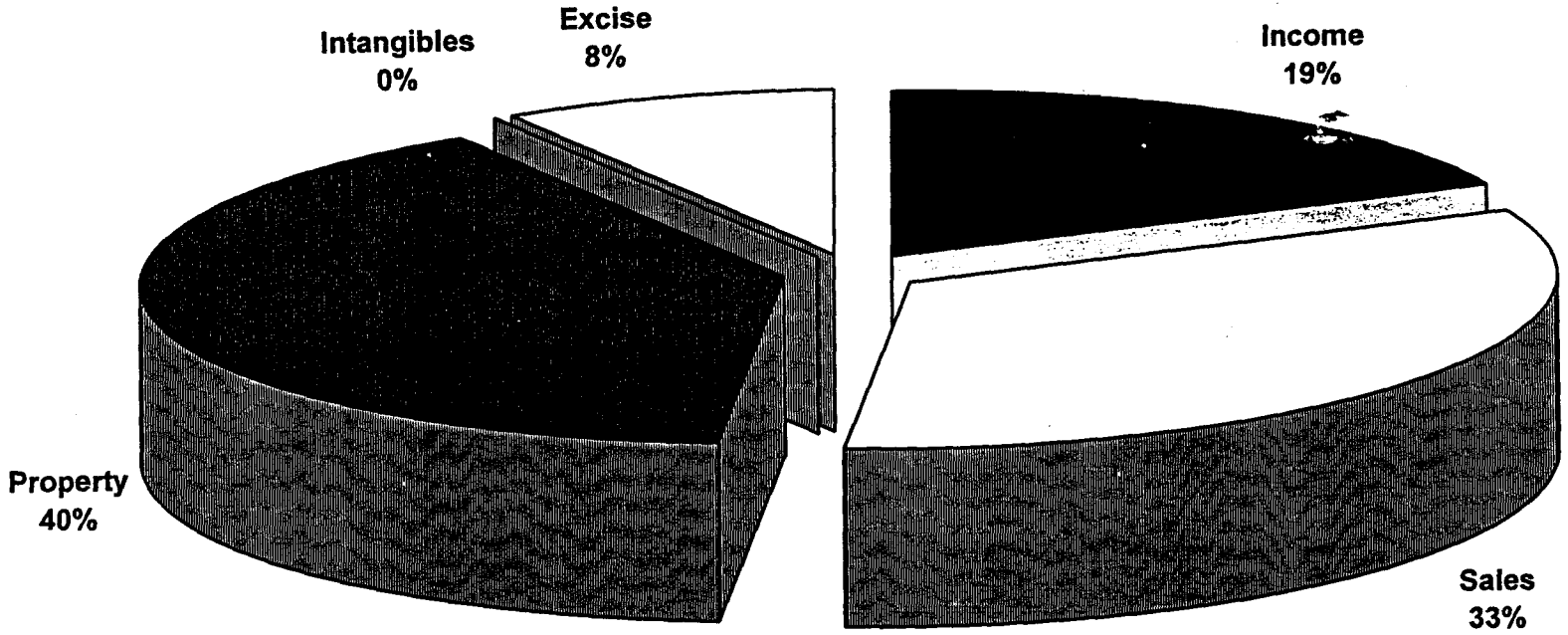
- **Child care credit and new child tax credit reduce burden on families, offset by inclusion of food in the tax base;**

For Businesses

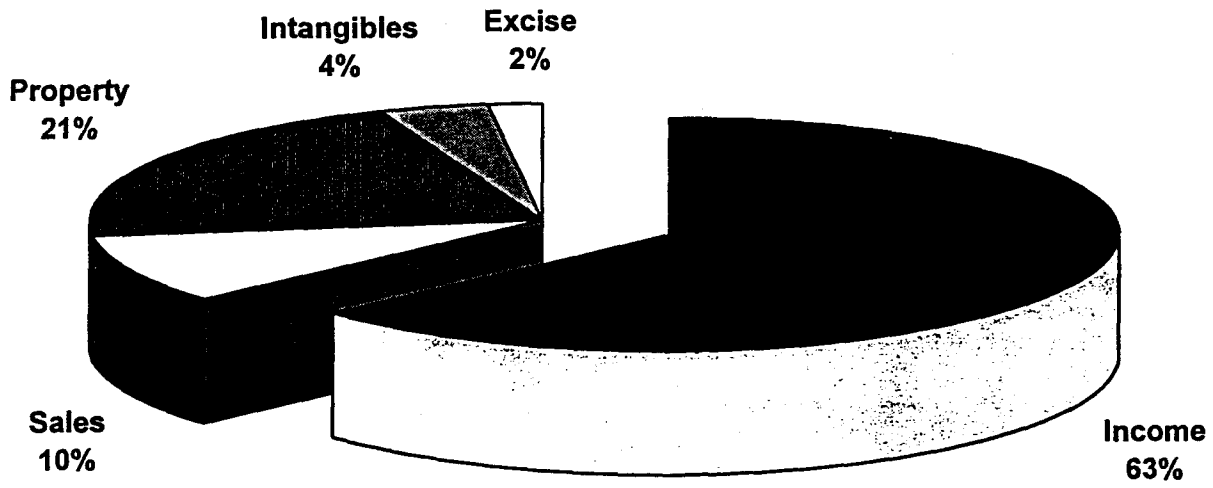
- **State has 4th lowest taxes among 22 competitor states and low unemployment insurance tax rate;**

- **Large multistate businesses benefit from double-weighting of sales in corporate income calculation and manufacturing businesses benefit from lower sales taxes for machinery, but corporate income tax rate is higher than other states in the region;**

Composition of Family Tax Burden - Family of Three with $20,000 Income
Total Tax Burden = 10.04% of Income



Composition of Family Tax Burden - Family of Four with $200,000 Income
Total Tax Burden = 9.48% of Income



INDIVIDUAL INCOME TAX

- **Largest source of revenue for the State;**

- **Equity: Taxpayers with more income have higher rates and more of their income subject to tax**

- **Stability: Generally less stable than other major taxes, very responsive to the economy**

- **Neutrality: Income tax often subsidizes home ownership, charitable giving, local taxation, dependent care, etc.**

SALES TAX

- **Largest source of revenue for most states;**

- **North Carolina's combined state and local rate is about average;**

- **Equity:** **Regressive, because of the inclusion of food and goods in the tax base;**

- **Stability:** **Moderately responsive to economic swings;**

- **Neutrality:** **Tax is only on certain kinds of consumption - most services are excluded;**

CORPORATE INCOME TAX

- Businesses do not pay taxes, people pay taxes - so there is a question about why corporate taxation should exist at all;

- Owners of company stock and consumers of company products pay;

- Businesses benefit from government - so it's appropriate for them to share in its cost;

- Equity: Incidence varies widely;

- Stability: Most volatile tax;

- Neutrality: Various credits, double-weighted sales and ability to export income to other states have different effects;

EXCISE TAXES

- **Generally small parts of state revenue systems (exception of gasoline tax);**

- **Equity:** **Most excise taxes are very regressive;**

- **Stability:** **Consumption of these goods is fairly stable, but revenues rise at far slower rate than the economy;**

- **Neutrality:** **Does inflate the cost of certain goods;**

NORTH CAROLINA'S TAX CHANGES IN 1995

Equity: **Income tax changes eliminated income tax entirely for 270,000 households;**

Intangibles tax relief primarily benefited those with sizable assets and incomes;

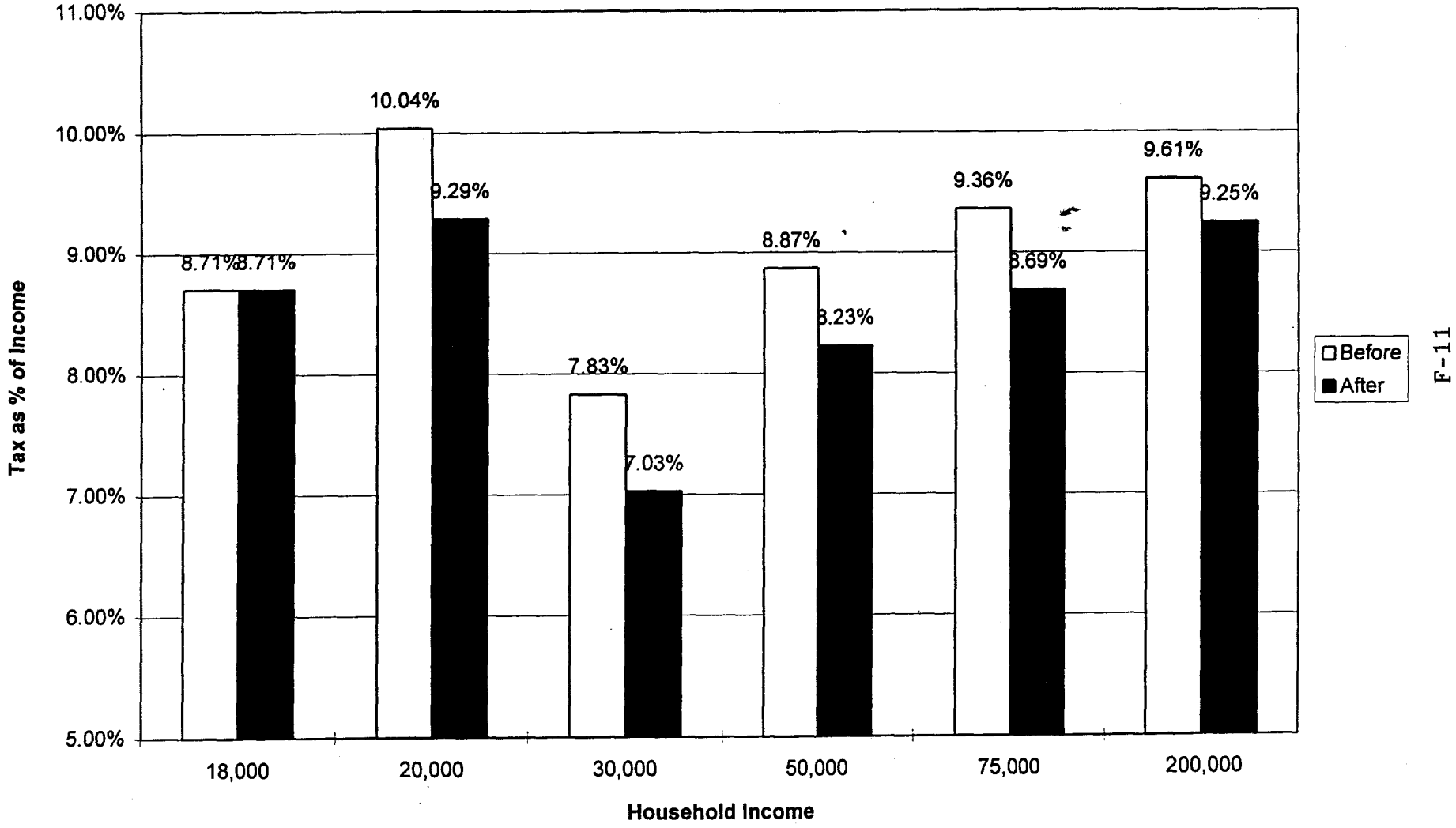
Some low-income families received no tax relief at all;

STABILITY: **State still has sizable rainy day fund & $193 million in unencumbered funds;**

State enacted tax relief that does not grow over time - will be easier to manage finances in next downturn;

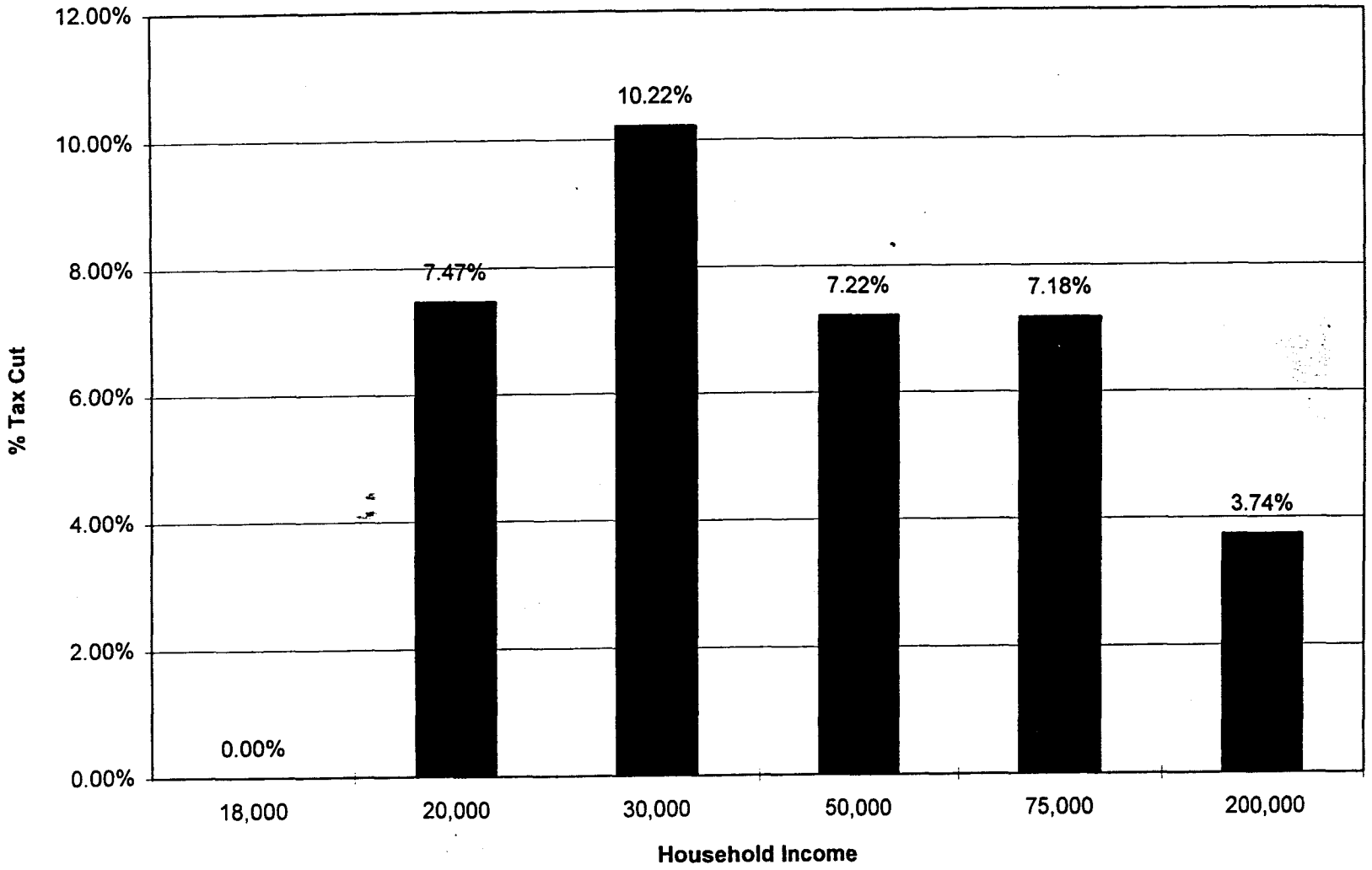
NEUTRALITY: **Intangibles tax was "sore thumb"**
Soft drink tax reduction made on this basis

North Carolina State and Local Tax Burdens for Various Incomes, Before and After Tax Cuts



NC Budget and Tax Center

1995 Tax Cuts as a Percent of Total Tax Burden for Various Income Classes



NC Budget and Tax Center

WHAT WERE OTHER STATES DOING?

1995 State and Local Tax Reductions as a percent of revenue	Number of States
1% or less	14
1% - 2%	4
2% - 3%	4
3% - 4%	3 (with North Carolina)
4%+	5 - of which 2 are permanent cuts, 2 are property tax cuts and 1 is a one-time refund
TOTAL	30

- North Carolina accounted for 10 percent of the total new cuts in state taxes and 23 percent of the total cuts in local taxes;

- Personal income taxes (14 states) and property taxes (7 states) were the most popular targets for changes;

WHAT IS NEXT FOR TAX POLICY?

- **Most states will hold the line on tax changes until the Federal agenda becomes more clear;**

- **If tax cuts happen:**

  -- **Unemployment Insurance Tax;**
  -- **State Earned Income Credit;**
  -- **Sales Tax on Food;**
  -- **Corporate Income Tax;**
  -- **Business Incentives;**

- **If tax increases happen:**

  -- **Sales tax (increase rate/broaden base);**
  -- **Excise tax (lottery, cigarette tax);**

STATE EARNED INCOME CREDIT

- **Equity:** Provides relief primarily for working families earning less than $27,000;

  650,000 NC families receive the credit in 1995;

- **Stability:** Federal government expects the EIC to grow at 4% a year;

  State has flexibility on level of relief by setting the credit as a percent of federal liability;

- **Neutrality:** Question over its effect on promoting work, as credit phases out as wages go up;

SALES TAX ON FOOD

- **Equity:** Low-income earners spend twice as much of their income on food as do high-income earners;

- **Stability:** Inclusion of food in the tax base does reduce the volatility of tax revenues, but tax on food is slow growing;

  Costs $338 million to replace state share;

- **Neutrality:** Usually prefer broad base, but many states exempt food currently

CORPORATE TAX CUT

- **EQUITY: Varies by company;**

  Tax reduction would be spread among investors, consumers (in and out-of-state) and Federal government revenues (loss in deduction for many companies);

- **STABILITY: Corporate income tax has declined in its important to state revenue - less volatile;**

- **NEUTRALITY: Shift in burden to residents v. hope for econ growth;**

INCENTIVES FOR BUSINESS

- **Stability:** Size of incentives can be capped - targeted relief for companies fulfilling certain goals;

- **Neutrality:** Similarly situated companies can pay different amount of taxes;

  Difficulty of defining areas of market failure where intervention may be needed;

SALES TAX INCREASES

- **Equity:** **(Rate Increase) - Sales tax is regressive, so this would increase taxes more for low-income people;**

  (Broad Base) - By taxing services, rate can remain lower and sales tax becomes less regressive;

- **Stability:** **The service sector of the economy is growing more quickly;**

- **Neutrality:** **Broadening the base helps neutrality - could have problems since tax would be new to certain businesses;**

EXCISE TAX INCREASES

- **Equity:** Both the lottery and cigarette taxes are very, very regressive;

- **Stability:** Cigarette revenues are stable, but lottery revenues in other states experience wide swings;

- **Neutrality:** Cigarette changes could have some impact on the industry; lottery changes could attract residents playing in other states;

WHAT WOULD THESE CHANGES YIELD?

TAX CUTS

STATE EARNED INCOME CREDIT	
10% of Federal Credit	($86 million)
SALES TAX ON FOOD	
Full Repeal	($510 million)
State Share	($340 million)
Penny on Tax	($85 million)
CORPORATE TAX CUT	
7.75 to 7%	($88 million)
BUSINESS INCENTIVES	
Governor's Package	($20-$30 million)?

TAX INCREASES	
SALES TAX	
Penny Increase	$650 million
Broadening Base	$280 million
LOTTERY	$250 million
CIGARETTE (Southeast Avg)	$65 million

APPENDIX G

John
LOCKE
FOUNDATION

Testimony by

John Hood, President

John Locke Foundation

before the

Revenue Laws Study Commission

North Carolina General Assembly

February 9, 1996

I would like to thank the members of this panel for the invitation to address you about the issue of tax reform, which I believe to be one of the most topics in state government today. North Carolina lawmakers, business executives, and citizens should all take the opportunity provided by the current national debate over the flat tax to become better informed about tax issues. With better information and understanding will come better tax policy. We cannot afford to rely on knee-jerk reactions, and certainly not on the poor reporting of the press about tax reform issues. As John Locke wrote three centuries ago, "to prejudge other men's notions before we have looked into them is not to show their darkness but to put out our own eyes."

Tax reform may be a hot issue, but it is hardly a new one. If you think about it, taxation is the most basic function of government. Indeed, the power to tax is itself the definition of a government. Other social institutions such as corporations, private schools, churches, and charities deliver many of the same services that government attempts to deliver. The difference is that

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governments can tax. They can force people to pay the bill for their activities. Other social institutions must rely on persuasion.

Historical Perspectives on Tax Policy

Because of taxation's fundamental role in defining government, some of history's greatest minds have struggled with the issue. Almost every idea about taxes that you think might be new has probably already been thought of by someone else centuries ago. For example, part of what supply-side economics is about is the argument that when marginal tax rates rise too high, the government actually loses tax revenue rather than gaining it. This idea didn't originate with Arthur Laffer or the Reagan Administration. A Taoist text from ancient China related the story of a king and policy advisor discussing budget woes:

"What should I do when my government does not have enough money to do all the important things," the perplexed king asked. The sage responded that the king should levy a flat 10 percent tax on production. When the king protested that 10 percent wouldn't be enough money, the sage replied that he should "decrease the tax, attract people to till the land, and invest in your country."

"This means *increase* the revenue by *decreasing* it," the ancient economist continued. "When all people have enough, the government has enough. When people do not have enough, how can the government have enough? Too much tax is self-robbery in that it does not nurture the strength of the people to pay the tax."

The notion that tax rates affected the growth rate of the economy is common sense, but I have heard many people, including high-ranking state officials and legislators, deny it. One observant Islamic scholar of the Abbasid period wrote that "A ruler who burdens his taxpayers until they cannot

cultivate the land is like one who cuts off his own flesh and eats it when he is hungry. He grows stronger in one part and weaker in another, and the pain and weakness he brings on himself is greater than the ache of hunger which he remedies."

Throughout history, rulers who were able to levy relatively fair, uniform, and well-administered taxes have prospered. Those who have imposed high rates (historically, anything over about 10 percent) and who have riddled their tax system with loopholes and special immunities have sparked revolt and the flight of productive citizens.

It's not simply the sheer weight of the tax burden but how it is applied that matters. Today, both the U.S. and North Carolina tax income with variable rates in a system misleadingly called "progressive" but might more accurately be called "punitive." The ostensible goal is to equate the tax burden with a citizen's ability to pay, but that is already accomplished by levying a percentage rather than a dollar amount per person. A percentage rate adjusts the tax burden according to a taxpayer's stake in the community. If your neighbor earns 50 times more than you do, he pays 50 times more in taxes.

Statesmen have long recognized the dangers inherent in a tax system designed more for redistribution of wealth than for financing necessary government. Benjamin Oliver, an early 19th century historian, noted that the U.S. Constitution imposed specific limits on what kinds of taxation could be imposed on citizens. "[Property rights] are not infringed by equal taxes for public purposes, imposed by adequate legitimate authority," he said. "A misapplication or misappropriation of funds in the public treasury, however, must be considered as a violation of this right . . as it would be unconstitutional, therefore, to lay an unequal tax, as well as an act of oppression upon those who were compelled to pay the larger proportion of it." John Stuart Mill wrote that graduated income taxes were "a mild form of robbery." James Madison zeroed in on the major problem that I still see today:

unless you charge the same rate to everyone, there is no objective basis for gauging the fairness of the tax system. "The moment you abandon the cardinal principle of exacting from all individuals the same proportion of their income or of their profits you are at a sea without a rudder or compass and there is no amount of injustice and folly you may not commit."

Three Principles of Good Taxation

There are many constitutional and economic issues involved in taxation at the state and local level, but today I'd like to zero in on three important principles. I'll list them now, and then explain them in detail.

The first principle is that a tax is really a bill for government services. The method by which we tax citizens should bear some logical relationship to the services being provided to them. I'll call this the functional principle of good taxation, though others refer to it, sometimes misleadingly, as equity.

The second principle is that the tax system should affect economic decisions to the least degree possible. In other words, decisions made on the basis of economic signals before taxation and decisions made after taxation shouldn't be dramatically different — or, at the very least, the difference should be intended rather than accidental. Let's call this the efficiency principle of good taxation.

The third principle is that the tax system should be as simple and as understandable as possible. Most citizens, after all, have better things to do than pay attention to government rules and regulations. The time they must spend complying with the tax code is time they can't spend making a living, rearing their children, or watching a good movie on cable — all arguably more important, and certainly more enjoyable, tasks than paying taxes. This is the simplicity principle of good taxation.

The Functional Principle

Sometimes we forget that the purpose of taxation is to pay for government services. In some cases, the customer and the beneficiary of the service is essentially the same person, and he or she is easily identified. For these services, the most direct way of billing them is simply to charge them a user fee. We have a number of user fees at the state and local level, for such services as processing applications, disposing of commercial waste in landfills, or using recreational and cultural amenities. In each case, it is easy and appropriate to charge users close to the full cost of the services they consume. Such an accurate price encourages them to consume services efficiently. For example, if a business generates a great deal of waste and must pay by the bag or the truckload to dispose of it, it has an incentive to find less expensive and wasteful ways of doing business. If you significantly subsidize the tipping fee, on the other hand, the business has less of an incentive to worry about waste generation — and, well, you get more waste.

In my opinion, we should employ user fees much more extensively to fund government services that directly benefit the user. Cultural amenities such as museums and arts groups should be funded solely or mostly by user fees. So should state parks and historic sites. These user fees should represent dedicated revenue, for use only where they are collected. This would prevent those who enjoy state parks, for example, from be charged to subsidize the bill for others who prefer the North Carolina Museum of Art.

Of course, there are many government services for which user fees are unsuited. Law enforcement, for example, is a core governmental function that involves protecting individual rights. One shouldn't have to pay a fee for a policeman to stop a criminal from attacking you. Citizens have certain rights, and they are entitled to the protection of those rights.

Similarly, true public goods cannot be paid for by user fees. The *Constitution of North Carolina* guarantees, for example, that citizens will have access to education. This guarantee was not offered simply to train future workers, which could be done through fees and loans contingents on future earnings. Rather, education was viewed as a core state function because democracy required it. Without citizens who can communicate, who know the political and cultural history of their society, and, especially in today's world, who understand basic principles of science, democratic government cannot succeed.

Well, to bring the discussion back to tax policy, what is an appropriate way for taxpayers to pay for services such as law enforcement and education? In the former case, the value of the promise of law enforcement, or fire protection for that matter, is partly predicated on how much real property you own. Think about it as if law enforcement were an insurance policy: the more you want to insure, the higher a premium you will be charged. Similarly, taxation of real property seems to me to be an appropriate way of paying for local provision of police and fire protection. Of course, such protection also extends to your body and those of your family, but at least property taxation bears some functional relationship to the services provided.

Property taxation makes less sense for funding education. One person who rents a condo and travels around in taxicabs but who has high annual income and participates significantly in the local economy would seem to benefit from the education of future voters and workers no less than another person of otherwise modest means who owns a home and a two cars. For education, levying a tax on one's stake in the overall economy — through income and sales taxes at a flat rate — makes more sense to me.

What I'm saying is that, before we can begin to discuss the economic impact or complexity of the tax code, we should examine whether the mix of

taxes we currently use to pay for state and local services makes any sense. I don't think it does.

The Efficiency Principle

Now, let's move on to something perhaps more basic. Does our current system minimize the economic distortions of taxes? I think most people who have looked at the system would agree it does not. For example, we tax goods sold at retail but not services sold at retail. This strange consumption tax is patently unfair in that it imposes a disproportionately large tax on lower-income people for whom goods purchases often outweigh the purchase of services. Broadening the base of the sales tax would make it more fair and allow us to reduce the tax rate substantially, thus boosting after-tax earnings and growth. Of course, if you extended the scope of the sales tax, you'd have to have an enforceable provision for keeping the correspondingly lower rate low, or else you've accomplished little more than a tax increase.

Now I'd like to discuss one of the most poorly reported and understood tax proposals of recent years, the flat tax. The most important thing about the flat tax is not necessarily that it is flat — though, as I argued earlier, I do think that single rate is the only fair way to tax income. The key point is that the tax code will no longer discriminate among different types of income and different consumption decisions.

Today, both the state and federal income tax systems discourage savings and investment and encourage current consumption. Some forms of income are taxed once, while others are taxed twice, three times, four times, or more. This causes our economy to grow more slowly than it otherwise would, and causes many other social problems, from spiraling health care costs to family insecurity.

Let me illustrate the current bias against investment with an example. Suppose I earn $1,000 from the Locke Foundation — which, if I am lucky, is not a hypothetical example. If there were no income tax, I would then have $1,000 either to invest in a stock mutual fund or to buy that big-screen TV I've always wanted. Further suppose that that mutual fund will earn me 10 percent next year. I must decide whether I prefer to spend $1,000 now for the TV or have $1,100 to spend next year, maybe for a TV with Dolby stereo.

Now suppose that North Carolina levies a 10 percent tax on income. I now have only $900 to spend on the TV or to invest. If I invest it, I will earn only $90 rather than $100 on my investment, so my return to investment has been reduced by the tax rate of 10 percent. But remember, I will also pay income tax on my mutual fund earnings. If I invested the $900 in the fund, the following year I would actually have only $981 to spend. That doesn't represent a 10 percent tax on what I would have earned without the tax. Instead, it is an effective rate of 11 percent, that's $1,100 without tax vs. $981 with the tax. On the other hand, the effective rate if I spent the money this year on the TV is only 10 percent, $1,000 vs. $900. Obviously, in the real world, the combined state and federal income tax is far higher than 10 percent, and the resulting difference between tax rates on consumption and investment is much greater.

Believe it or not, it's even worse than that. Keep in mind that I've invested in a *stock* mutual fund. That means I, in effect, own shares in corporations that must first pay income tax on their net earnings before I get my dividend. If I own 1 percent of a firm with $1,000 of net earnings to distribute and it must first pay a 10 percent income tax on those earnings, then I will receive 1 percent of $900, or $9, rather than 1 percent of $1,000, which is $10. Then my $9 dividend gets taxed when I receive it through the mutual fund. Since my original investment in the fund, and thus my expected earnings, was also taxed, I've now been hit three times. If I died that year and left my mutual fund to my child, it would be taxed as inheritance

income yet again. Obviously, this system is extremely punitive toward savers and investors, and encourages all of us, on the margin, to buy those big-screen TVs rather than plan for tomorrow. There is nothing wrong with big-screen TVs, of course, but we shouldn't create an artificial incentive for people to buy them through poor tax policy.

You could fix this problem in at least two ways: Steve Forbes' way and my way. Forbes would tax the initial investment in the mutual fund but then not tax the dividends you earn in subsequent years. I would rather let an investor deduct the initial investment and then pay on investment earnings he consumes in future years. I'll explain why my system is better if you wish, but the point is that rationalizing the tax code is crucial if we want to reduce the distorting effects of the income tax on our economy and our lives.

Let me mention one other issue of economic efficiency, and that is inflation. I understand that later this morning, you will discuss the indexation of North Carolina's personal exemptions, standard deductions, and tax brackets. This is absolutely critical. Otherwise, every year North Carolina families will get a tax increase as inflation erodes the value of their exemptions and deductions and pushes some of them into higher brackets. Indexation would have cost about $50 million this year, I believe.

The Simplicity Principle

Lastly, let me briefly discuss why one of your goals in tax reform should be simplicity. Basically, it is an issue of public trust. When the tax code is too complex for the ordinary citizen to understand, and contains all sorts of loopholes and deductions that only the politically connected or the fiscally savvy can use, the public gets the idea that they're getting the boot. They're probably right.

Right now, we collectively spend at least $300 billion a year complying with individual and corporate income taxes. That is a staggering amount of largely useless effort. Accountants and tax lawyers are wonderful people, but I think their talents could be better employed creating wealth for their fellow citizens rather than hiding it from the government. Furthermore, a simple tax system makes it clear to everyone how much government costs. This is a crucial first step to getting government costs under control.

Let me end my prepared remarks by saying that, from the perspective of the Locke Foundation, the most important goal for tax reform should be simply to lower the overall tax burden on North Carolina families and businesses. We currently impose the highest tax rates on individual income, corporate income, and sales in the Southeast. However we reform the code to make it more efficient, more comprehensible, and more directly related to the government services it funds, we should make sure that the overall tax burden follows a steady downward course. Let's avoid what novelist Leo Tolstoy wrote was the standard excuse of the bureaucrat for high taxes:

"I sit on a man's back, choking him and making him carry me, and yet assure myself and others that I am very sorry for him and wish to lighten his load by all possible means — except by getting off his back."

Suggested Readings:

• Robert E. Hall and Alvin Rabushka, *The Flat Tax*, Second Edition, Stanford, California: Hoover Institution Press, 1995.

• Charles Adams, *For Good and Evil: The Impact of Taxes on the Course of Civilization*, New York: Madison Books, 1993.

• Bob McTeer, Rep. Dick Armey, and Rep. Bill Archer, "Tax Reform: An Opportunity to Increase Our Saving" (debate on tax reform) *Economic Insights*, Federal Reserve Bank of Dallas, Vol. 1, No. 2, 1995.

APPENDIX H

COMMONSENSE ABOUT TAXES: A STATE AND LOCAL PERSPECTIVE

Dr. Michael L. Walden
Professor
North Carolina State University

Presentation Before the Revenue Laws Study Commission of
the North Carolina General Assembly, March 18, 1996

Thank you for inviting me to speak before this very important group on the important topic of taxes. In government, there are two broad functions: (1) deciding which activities, products, or services to produce or support publicly, and (2) deciding how to finance those items which government will produce or support. The second function is broadly called "taxes".

Citizens generally complain about taxes, and this is to be expected. Taxes are a cost, or price, and consumers complain about prices and costs because they represent a transfer of resources out of consumers' pockets into producers' pockets. Consumers will always think producers are getting "too much".

The same goes for government. A large number of consumers will always think taxes are too high for the government services they receive. Some of this is because it's often hard for citizens to identify exactly what they receive for their tax dollar. There is frequently a "disconnect" between tax payments and the receipt of government program benefits. More on this later.

A look at statistics, however, does show some support for a citizen concern about a growing tax burden. All taxes, federal, state, and local combined, today take about a third of total

income, and this is up from 25% in 1950 and a mere 12% in 1930. The Tax Foundation estimates that the average two-earner income family now pays about 40% of their income in taxes of all kinds. Here in North Carolina, state taxes as a percent of total state income (state gross income) have also drifted upward.

But at the same time that the complaints about taxes are becoming louder, the demands on state and local governments may be getting greater for two reasons. First is the trend toward budget balancing at the federal level which will likely result in pushing some programs and their responsibilities "down" to the state and local levels. Second is the growth and development which North Carolina is expected to experience in the coming years. As economic development occurs and population densities increase, there will be a greater demand for highways and other infrastructure, for state or local action to control pollution, noise, and for ways to address conflicting and competing land uses.

In this context, there could be no better time to re-think and re-evaluate state and local taxes in North Carolina. Of course, this can be done on several levels. You have had excellent presentations from Don Liner, Dan Gerlach, and Rick Carlisle on the more technical aspects and evaluation methods of state and local taxes. You have also had an excellent and more general, or philosophical, presentation by John Hood. My presentation will be more in the spirit of John Hood's. I will discuss preferred elements of state and local taxes from two perspectives: from the perspective of the average citizen (as I interpret "average"), and from the perspective of economic efficiency. Since there are at least two sides to every issue about taxes, I will present these elements in the form of "clashes".

CLASH ONE: SIMPLICITY VERSUS COMPLEXITY IN THE TAX CODE

Despite efforts at "tax simplification", our tax codes remain incredibly complex. Some of this is by accident, as it is often easier to add to existing rules rather than make wholesale changes. But some of the complexity is by design, as legislators use deductions, exemptions, credits, and other devices in the tax code to favor or encourage certain kinds of spending by consumers and businesses.

The issue is whether government should use the tax code to achieve ends other than raising revenue. For example, consider the home mortgage interest deduction. This deduction obviously benefits homeowners at the expense of renters. Taxes paid by renters must be higher to fund the tax revenues lost by the mortgage interest deduction. Should government be tilting the scales in favor of homeowners and away from renters? If so, why? Or, should government stay out of the decision about how consumers spend their shelter dollars?

My own preference is for simplicity in the tax code for several reasons. Any preference or "favor" in the tax code will immediately create suspicion among some taxpayers that others are receiving the benefits. This creates distrust about the tax code and for government.

I also think the government should generally refrain from attempting to direct consumer or business spending with the tax code. The government shouldn't be in the business of picking "good" and "bad" spending since this is so subjective. Individuals and businesses best know how to spend their money.

However, there's one exception to my rule. The exception exists when a "positive externality" occurs with the consumer or business spending. A "positive externality" happens when a major benefit occurs from the spending to society at large beyond the benefit received by

the consumer or business. Furthermore, the consumer or business doesn't recognize and take into account the broader benefits of their spending. Here it can make sense to use tax policy to encourage spending which has major positive externalities.

Two examples will illustrate this idea. First is charitable giving. Charitable giving has large positive externalities in the community at large. Tax deductions for charitable giving recognize these positive externalities and encourage this spending. Interestingly, there are calls from some quarters to expand this deduction into a credit at the same time that welfare programs are shifted from government to the non-profit sector.

The second example is homeownership. Homeownership may provide community benefits if it encourages community stability and pride. If such is the case, homeownership may deserve special tax treatment.

Caution is in order here. The idea of positive externalities can be overused and misused. Public decision makers will have to exercise caution in making positive externalities the exception to the idea of a simple tax code.

CLASH TWO: USER FEES VS. GENERAL FINANCE

A clash that will likely become increasingly important in the future is that between user fee finance versus general finance. User fees identify the direct beneficiaries of a government project or service and have the users pay the cost. Non-users aren't charged. General finance charges everyone for the government project or service whether they use it or not.

User fees often create complaints from users who argue they have been singled-out for taxation. The path of least "political resistance" is usually to finance projects and services by general taxation.

Despite the potential political fallout, my preference is for user fees whenever possible. User fees promote economic efficiency because users are forced to pay the cost of the resources they use. User fees are also "fair" because users pay and non-users don't.

Modern technology may make user fees more practical than in the past. Toll roads are a good example. The premise of toll roads is that users pay for the road. Yet toll roads always had the reputation of being costly to administer and implement. Travellers would have to come to a complete halt in order to deposit payments at a manned station.

Sensor technology eliminates these drawbacks of toll roads. Sensors can be embedded in roadway entry and exit points and be used to read license numbers or other identification of entering and exiting autos. In this way, travellers can be charged for their use of the highway. Charges can be levied for both construction and maintenance costs. The fee rate can also be varied over the time of day to address congestion problems.

One argument against the whole idea of user fees, such as toll roads, is that they hurt the poor. My opinion is that income redistribution issues should be handled outside of tax policy. In other words, public policies to help the poor should be handled separately from tax policies. If not, economic efficiency is hurt. For example, if the poor are exempt from paying for highways, then the poor won't recognize the resource allocation to highways and will overuse them.

CLASH THREE: EFFICIENCY VS. INCOME REDISTRIBUTION

There is a strong view held by some that the tax code should be used to redistribute income. Income redistribution can be seen in the current tax code in at least two ways. First is in progressive tax rates, which tax higher levels of income at higher rates. Second is in the phaseout or reduction of certain tax exemptions at higher levels of income.

The idea of taxing higher incomes at higher rates is based on the "ability to pay" concept. This concept says that richer taxpayers have a greater ability to pay taxes; therefore, they should be taxed at higher rates. It also implies that dollars have less intrinsic value to richer persons than to poorer persons. Therefore, to equalize the "pain" of taxes, richer persons must be taxed at higher rates.

However, these views are not universally accepted. For one, increasing the tax rate for richer taxpayers deters those taxpayers from earning, investing, and contributing to additional economic growth. Phasing out tax deductions and exemptions at certain levels of income creates distortions at those levels. Last, even if we accept that the additional value of a dollar falls with income, we don't know the speed of this fall, and so we can't set tax rates accordingly.

My preference is not to use the tax code for income redistribution purposes. Again, I recommend that income redistribution efforts be handled overtly in other ways. In this sense, I like a "flat tax" concept with a generous household (or standard of living) deduction which is indexed to inflation.

CLASH FOUR: BUSINESS TAXES VS. CONSUMER TAXES

A popular view is that businesses should be taxed, and taxed more, because they make big profits. Many people think that businesses are rolling in money that's just waiting to be taxed.

Besides the problem that the profit rate of the average business is not as high as people think, there's another problem with this line of thought. Although a business may pay a tax (i.e., they write the check for the tax), they frequently don't bear the incidence of the tax. They will pass on some part of the tax to consumers in the form of higher prices, to workers in the form of lower wages, or to stockholders in the form of lower rates of return.

My preference is to tax the net income of businesses that won't be taxed at another level, and to tax that net income once. So taxing the net income of sole proprietorships and partnerships is fine. Taxing corporate net income is another matter. Corporate net income which is paid to stockholders in the form of dividends will be taxed again by the individual income tax. This means corporate income can be taxed twice. Therefore, I would look closely at reducing or eliminating the corporate income tax in North Carolina.

CLASH FIVE: WHAT SHOULD BE TAXED, WEALTH, INCOME, OR CONSUMPTION?

In North Carolina, as in most states, the tax base varies between wealth, income, and consumption. The property tax taxes wealth, the income tax taxes income, and the sales tax taxes consumption. Is this system logical?

The principle that should be used in answering this question is this: government should tax that tax base which best corresponds to the resource which benefits from the government program or service financed by the tax. Take police and fire protection provided at the local government level. The tax base which is most directly related to the protection provided by these services is property wealth. The greater a citizen's property wealth, the greater the protection received from

locally provided police and fire services. Therefore, it makes sense to fund local police and fire protection with a property tax.

Most other government services will be most directly related to income. Education, which consumes a dominant share of state and local spending, is a good example. The rationale for funding education publicly is that everyone benefits from an educated labor force. Presumably, a more educated workforce will be more productive, and this will lead to lower consumer prices and higher investment rates of return. Therefore, citizens with higher income, who both spend and invest more, will benefit more from an educated workforce. Taxing their income would be the tax base most directly related to this benefit.

What about the sales tax? At one level, it doesn't matter if income is taxed or only spending is taxed, if the difference between the two, which is savings, will eventually be converted to spending. But taxing only spending has two problems, in my opinion. First, even assuming that savings will be spent and taxed, there is the problem of timing. The conversion of savings to spending may occur well in the future and therefore not be coordinated with the current government service. Second is the problem of regressivity. Without some deduction or rebate, sales taxes are regressive because lower income households spend a much higher percentage of their incomes than do higher income households.

Therefore, my preference is for a greater reliance on the income tax for funding most local and state government programs and services, with the exception of using the property tax for funding those services which are most directly related to property wealth. I would correspondingly reduce or eliminate the reliance on the sales tax.

CLASH SIX: DISCRETION VS. EARMARKING

Politicians generally prefer discretion in determining how tax revenues are spent. This is not a criticism; it is simply a reflection of human nature to have control over activities. There's also a practical element to such discretionary power. Having discretion over spending allows politicians to quickly adjust spending to meet new priorities and needs.

But there is a cost to this discretion, and it's increasingly reflected in the public's skepticism about government. With discretion comes an inability for the public to know what tax revenues are being spent on what government functions. With discretion comes an inability of the public to know what "bang" they're getting for their "buck". Also, with most government revenues lumped into one pot for distribution, it becomes easy for competing government functions to lobby for a greater share of the pot without consideration of what happens to the shares of other functions.

My preference is for greater earmarking and accountability of tax revenues. If a taxpayer knows that a certain tax is used to fund a certain government project or service, then the taxpayer can see a link between that tax and that government project or service. If the government project or service requires more funds, the taxpayer can see the need for the particular tax rate to be increased.

In essence, I would like us to move government funding to more of an "automatic pilot" system. For example, if residential growth of a certain amount requires an additional school building, fire station, and police, why couldn't we establish a system which automatically taxes the growth to provide the needed facilities? Something along the lines of "impact fees" would be an

example. In this way the developers and new residents would know what is expected of them and would be required to "pay their way" for the necessary new public infrastructure.

I respectively submit that these six clashes represent today's "cutting edge" issues in state and local public finance. Our tax system needs a top to bottom examination with the goals of increasing simplicity, efficiency, logic, and public acceptability and support.

APPENDIX I

HISTORY OF THE SALES TAX ON FOOD
16-APR-96

Effective Year	Action
1933	North Carolina adopted a 3% sales tax. It exempted essential food items, such as flour, corn meal, meat, lard, milk, molasses, salt, sugar, and coffee, from the tax.
1935	The exemption for essential food items was eliminated. Food was subject to the State sales tax.
1937	The exemption for essential food items was reinstated and expanded to include bread products.
1941	The legislature broadened the exemption for essential food items to "food purchased for home consumption".
1961	The exemption for food is eliminated. Food is subject to the State sales and use tax. In Governor Terry Sanford's special message to the 1961 General Assembly, he outlined the needs of the State, particularly in the field of education. To meet those needs, he recommended eliminating all exemptions from the sales tax, effective July 1, 1961. He also recommended that a state-wide vote be held to determine whether the tax should continue beyond July 1, 1963. The legislature did repeal several exemptions to the sales tax, including the exemption of food purchased for home consumption. The legislation did not include an earmarking of tax revenues for education, it did not sunset the tax in two years, and it did not subject the tax revision to a vote of the people.
1971	A one-cent local sales tax is authorized, for a combined State and local sales tax rate of 4%.
1983	A half-cent local sales tax is authorized, for a combined State and local sales tax rate of 4.5%.
1985	Food purchased with food stamps is exempted from the sales tax. A nonrefundable tax credit for individuals with low or moderate incomes is enacted. Although the credit was a general credit ranging in amount from $15 to $25, depending on the taxpayer's net taxable income, the 1989 Select Legislative Committee on Tax Fairness found that the timing of those tax credits and the record of legislative deliberations suggest that one objective of the credit was to provide some offset for the sales tax on food to low and moderate income persons not receiving Food Stamps.

HISTORY OF THE SALES TAX ON FOOD
Page 2

Effective Year	Action
1986	An additional half-cent local sales tax is authorized, for a combined State and local sales tax rate of 5%.
1989	The credit was repealed in the Tax Fairness Act of 1989 because the Act reduced taxes for a large number of low and moderate income taxpayers. The 1989 Select Legislative Committee on Tax Fairness recommended a proposal to the 1989 General Assembly that would have created a refundable income tax credit for individuals with low or moderate incomes. The stated intent of the credit was to provide some relief for these individuals from the sales tax on food. This proposal did not pass.
1991	The State sales tax rate is increased to 4%, for a combined State and local sales tax rate of 6%.

APPENDIX J

Tax Preferences
Revenue Laws Study Commission
March 18 & 19, 1996

CHANGE CATEGORY	CURRENT LAW	PROPOSAL	EFFECT 96-97	EFFECT 96-97
Sales & Use Tax				
Farm & mfg. machinery (parts and accessories)	Certain sales taxed at 1% with maximum tax of $80.00	1%, $280 limit	$2m	
		1%, $700 limit	$5m	
		1%, no limit	$20m	
		2%, $240 limit	$36m	
		2%, no limit	$70m	
		3%, no limit	$120m	
		4% & 2%, no limit	$170m	$104m
Interstate Telecom.	Exempt	6.5%, Intrastate rate	$48.6m	
Amusement admission				
Movie theaters	$200 & $100 Annual License	6%, sales tax rate	$5.3m	$2m
Pay for play	Exempt	6%, sales tax rate	$2.8m	$1m
Cable TV	Exempt	4% State & 2% local sales tax	$14.4m	$7.2m
Print media				
Newspapers & magazines	Door to door sales exempt	4% State & 2% local sales tax	$4.2m	$2.1m
Newspapers inserts	Advertising inserts are exempt	4% State & 2% local sales tax	$.8m	$.4m
Shoppers guides	Materials used to produce are exempt	4% State & 2% local sales tax	$1.0m	$.5m
Vending & coin laundries	Exempts 50% of vending sales price and 100% laundry gross receipts	4% State & 2% local sales tax	$2.2m	$1.1m

CHANGE CATEGORY	CURRENT LAW	PROPOSAL	EFFECT 96-97
Corporate Income			
Apportionment	Allocate nationwide income to N.C.: 50% sales 25% payroll 25% property	Allocate by pre-1988 formula: 33 1/3% sales 33 1/3% payroll 33 1/3% property	$60.0m
Throwback rule	No provision	Allocate certain sales to N.C.	?
Insurance Preferences			
Guaranty Fund	Annual payment taken over 5 years	Repeal	$ 31.7m
Personal Income Tax			
Base Changes:	Full exclusion for Social Security income	Conform to federal law: 85% of benefits on incomes greater than $34,000 ; ($44,000 married joint filings)	$85.3m
	Retirement income exclusion of $4,000 for public and $2,000 for private	Federal rule no exclusion	$60-80m
Excise Tax			
Tobacco	4% of excise tax	Disallow discount	$1.9m
Soft Drinks	4% of excise tax	Disallow discount	$2.6m
Beer & wine	4% of excise tax	Disallow discount	$3.4m

A. One Percent Sales and Use Tax Classification

Prior to 1961, North Carolina levied a sales tax on the gross receipts of both wholesale and retail merchants. The wholesale rate was 1/20 of 1% and the rate on items sold at retail was 3%; all items sold were limited to a maximum tax of $15.00. In 1955, the General Assembly enacted several measures to broaden the retail sales tax base. Two of the measures employed were: (1) repeal of the $15.00 maximum tax limit on all sales; and (2) the creation of a separate tax classification for motor vehicles, airplanes, and accompanying parts and accessories. The sales and use tax rate applied to this "new" classification was 1% with a maximum tax of $80.00.

In 1961, the General Assembly eliminated the wholesale tax and created another special classification to tax farm machinery, mill machinery, and their accompanying parts and accessories. Prior to 1961, mill and farm machinery were taxed at the wholesale rate. Parts and accessories were exempt from sales tax before 1957 when the General Assembly began taxing them at the wholesale rate. Under the new special classification, all machinery, parts, and accessories became subject to the 1% rate with an $80.00 cap. It is not clear why a rate of 1% with an $80.00 cap was chosen. The 1% classification may have been created to minimize the revenue impact from eliminating the wholesale tax. It could have been selected because the same rate had been imposed on motor vehicles and airplanes in 1955 when the $15.00 per article limitation was repealed.

Sales Subject to the 1% Sales or Use Tax Rate with no Cap

<u>Agricultural Group</u>

* Horses and Mules (Effective 1961)

  Prior to 1961, horses and mules were exempt from the sales tax due to their use in agricultural production. At the time, dealers were charged a "per head" tax of $3.00 as part of the privilege license tax. The tax was paid by a dealer for every horse or mule sold. In 1961, the exemption was repealed and horses and mules were subject to a 1% sales tax.

* Semen used in the artificial insemination of animals (Effective 1961) In 1949, the sale of semen was exempt.

* Fuel, other than electricity or piped natural gas, sold to farmers for farm purposes other than household. (Effective 1961). In 1949, the General Assembly exempted fuel used in agribusiness.

* Sales of containers, wrapping, packaging, and shipping materials to farmers that do not go with and become part of the sale of the product. (Effective 1982).

Commercial Group

* Fuel, other than electricity or piped natural gas, sold to manufacturers and dry cleaning plants for purposes other than residential. (Effective 1961).

* Lubricants used in lubricating production machinery. (Effective 1962).

* Sales to commercial printers of photoengravings, electrotypes, and lithographs used by the purchaser in printing tangible personal property for sale. (Effective 1962).

* Materials such as film, chemicals, proof paper, cameras, trays, and similar items used in the manufacturing or fabricating of pictures for sale. (Effective 1962).

* Containers, wrapping, packaging, and shipping materials consumed in the operations of freezer locker plants. (Effective 1961).

Sales Subject to the 1% Sales or Use Tax Rate with an $80.00 Cap per Article

Agriculture Group

* Farm machinery, parts, and accessories including bulk tobacco barns, and similar tangible property used for curing and drying farm products. (Effective 1961). In 1955, parts and accessories were exempt if used in the production of tobacco and machinery was taxed at a rate of 1/20 of 1%. In 1957, parts and accessories were taxed at the rate of 1/20 of 1%.

* Storage facilities and accessories sold to farmers for the storage of grains, feeds, or soybeans. (Effective 1979). In 1981, the General Assembly expanded the 1979 levy include storage equipment for all types of livestock.

* Sales to farmers of commercially manufactured portable swine equipment or facilities and accessories. (Effective 1979).

* Bulk feed handling equipment which has been constructed to be used in the production of livestock. (Effective 1979).

* The total number of poultry cages served by the same automatic feeder, water dispenser, or egg collector. (Effective July 1, 1982).

- Nurserymen and greenhouse operators are given the same consideration as farmers and purchases of machinery, parts, and accessories for use in planting, cultivating, and harvesting horticulture products are taxed at the 1% rate.

Commercial Group

Mill machinery is defined as machinery, parts, and accessories purchased by industrial processors which are used or consumed in different production phases of tangible personal property. (Effective 1961). In 1933, this group of machinery was taxed at 1/25 of 1% and in 1959, 1/20 of 1%.

Specific industries for which the classification of "mill machinery" applies:

- Furniture Factories
- Plants
- Electric Power Companies
- Mining and Quarrying
- Sawmills, Lumber Mills, Ready Mixed Concrete and Asphalt Plants, Brick Manufacturers, Cotton gins, etc.
- Dairies and Creameries

Specific types of equipment classified as "Mill Machinery":

- Motors, pulleys, motor bases, gears, belts
- Steam engines, gasoline engines, diesel engines, generators
- Boiler room machinery
- Conveyers, hoists, and hoist cables

* Purchases of machinery, parts, and accessories, by printers and publishers, used directly in the production of newspapers, magazines, and other printed matter for sale.

* Sales to dental laboratories of machinery, equipment, and accessories for use directly in dental fabricating of false teeth. (Effective 1962).

* Machinery, parts, and accessories used in the direct performance of laundering and dry cleaning services. (Effective 1961).

* Broadcasting equipment, including towers, parts, and accessories sold to commercial radio and television stations. (Effective 1961). In 1957, the General Assembly exempted this group.

* Central office equipment, switchboard equipment, private branch exchange equipment, and prewritten computer programs purchased by telephone and telegraph companies for use in providing telephone services to subscribers. (Effective 1963). In 1959, the latter was taxed at the wholesale rate of 1/20 of 1%. Computer programs were included in 1983.

* Sales to tire recappers of machinery, parts, and accessories for the exclusive use in the recapping process.

* Sales of machinery, parts, and accessories to machinist, foundrymen or pattern makers for the exclusive use in the fabrication of tangible personal property. (Effective 1977).

* Sales to freezer locker plants of machinery, parts, and accessories. (Effective 1961). In 1957, machinery, wrapping paper, and supplies were exempt.

Neighboring States Policies

Trends: The majority of States allow an exemption for machinery and equipment used in manufacturing

STATE	SALES TAX ON MACHINERY
Florida	Exempt
Georgia	Exempt
Kentucky	Exempt
South Carolina	Exempt
Tennessee	Exempt
Virginia	Exempt

States Taxing Machinery

STATE	RATE	STATE SALES TAX RATE
Alabama	1.5%	4%
California	6	6
Louisiana	4	4
Mississippi	1.5	4.2
Nebraska	5	5
New Mexico	5	5
South Dakota	4	4
Washington	6.5%	6.5%

B. Interstate Telecommunications

There is a 6 ½% sales tax on the gross receipts derived from providing long distance and private telecommunication services that originate and terminate within the State. A sales tax of 3% applies to the gross receipts from sales of local telecommunication services. In addition to a sales tax, companies providing local telecommunication services pay a franchise tax of 3.22% on their gross taxable receipts. Interstate telecommunication services that originate or terminate inside the State and are billed to a billing address in this State are not taxed; neither a sales tax nor a franchise tax is levied by the State on these transactions.

Other States Policies
(Rate) where available

Twenty state tax interstate telecommunications: Arkansas, Connecticut (6%), District of Columbia, Florida, Hawaii(4%), Illinois (5%), Kansas (4.9%), Massachusetts (5%), Minnesota (6.5%), New Hampshire (6%), New Jersey (6%), New Mexico (4.25%), Ohio (5%), Oklahoma (4.5%), Pennsylvania (6%), Rhode Island(7%), Tennessee (6%), Texas(6.25%), Washington (6.5%), and Wisconsin(5%).

C. Amusements/Entertainment and Gross Receipts Taxation

Businesses and other organizations that offer entertainment or amusement for which an admission fee is charged pay to the State a gross receipts tax of 3%. In addition to a gross receipts tax, most businesses and organizations are required to pay a licensing tax of $50.00 for each room, hall, tent, or place where admission charges are made. The license tax is an advance payment of the gross receipts tax. Some organizations because of their corporate income status are not required to pay a license tax except for the locations where they hold sporting events and charge an admission fee.

The general rule regarding cities' ability to levy a licensing tax is that they have the power to levy a tax on all trades, occupations, professions, businesses, and franchises carried on within the city except where this authority is limited by statute.

Counties, on the other hand, are prohibited from levying license taxes except where authorized to do so by statute. In most cases the amount of tax a local unit of government can levy on amusements is restricted to a percentage amount of the State tax.

The gross receipts tax applies to college and professional sporting events, circuses, theater, concerts, and all other amusements and entertainment for which admission is charged.

Exclusion and reduced tax rates from the 3% gross receipts tax

- Motion picture theaters do not pay a gross receipts tax. Instead, such businesses pay a license tax for each hall, room, or tent used to show motion pictures; the license tax is $100.00 per year for outdoor movie theaters and $200.00 a year for indoor theaters.

- Motion picture shows operating three days a week or less are taxed at one-half the amount otherwise charged.

- Civic organizations and private and public schools are not subject to the license tax and may exclude the first $1,000 in gross receipts from the tax if the entire proceeds are to be used by the organization or school and not to defray the expenses of conducting the amusement.

Exemptions from the 3% gross receipts tax

- Pay for play entertainment such as green fees, tennis court rentals, target shooting, and swimming is not subject to the 3% gross receipts tax. These types of businesses may pay a general business license tax. However, if there is an admission charge to view a sporting tournament, then the gross receipts from the ticket sales are subject to the 3% tax.

- Pay for view entertainment such as cable and satellite television services and other similar video services which are broadcast to subscribers in the State are not subject to a gross receipts tax.

- The admission charge to motion pictures shown by a qualified corporation that operates a center for the performing and visual arts is exempt if the showing of motion pictures is not the primary purpose of the center. (The admission to dances is included in this exemption.)

- Admission fees to high school and elementary school athletic events are exempt.

- The admission charge to entertainment events on the Cherokee Indian Reservation is exempt if a gross receipts levy is paid to the tribal council.

- Athletic contests and dances for which an admission charge is 50 cents or less are exempt from the tax.

- Teen centers, exempt from State income tax, whose primary purpose is to provide recreational activities and other amusement exclusively for teenagers are exempt from the gross receipts tax.

- The admission charge to all amusements exclusively produced by local talent for the benefit of religious, charitable, benevolent or educational purposes and where the talent receives no compensation is exempt from the tax.

Neighboring States Policies
Trends: There are no identifiable trends

STATE		POLICIES
Florida	(6%)	Admission charge if not exempt by statute; exempts most public and private school events; exempts NFL Championship games
Georgia	(4%)	Admission charge if not exempt by statute; exempts most public and private school events
Kentucky	(6%)	Admission charge; exempts charges to historic sites

South Carolina	(5%)	Admission to places of amusement if admission is charged
Tennessee	(5%)	Country club dues, (exempts country club assessments on capital improvements); membership and admission fees to public golf courses sports and recreational clubs; pay-for-play; theatrical and sporting events; expanded cable
Virginia		To Be Confirmed

D. Newspapers and Magazines Sold Door to Door

The sale of newspapers by newspaper street vendors and by newspaper carriers making door to door deliveries and sales of magazines by magazine vendors making door to door sales are exempt from the sales tax. Newspapers purchased from the publisher and sold by a vendor, whose primary business is the sale of newspapers, through newspaper boxes are not subject to the sales tax. Newspapers published in this State and delivered to subscribers outside the State are not subject to the sales tax. Newspapers sold in stores and subscription sales by the publisher are taxable at the State and local sales tax rate of 6%. The retail sale of magazines sold in stores is a taxable exchange; subscription sales are not.

Newspapers were exempted from the sales tax in 1957. In 1961, the General Assembly partially repealed the exemption. Sales of newspapers by newspapers street vendors and by "newsboys" making house to house deliveries remained exempt. In 1974, magazines sold door to door were added to the exemption.

The newspaper exemption established in 1957 and continued, as amended, to the present was enacted to avoid or eliminate the administrative problem of trying to collect small amounts of sales tax from hundreds of independent contractors, many of whom are[were] children. The magazine exemption was enacted to eliminate the problem of trying to collect a use tax from individual subscribers of magazines.

D. Free Circulation Publications

In 1983, the General Assembly exempted sales of advertising supplements and any other printed material that is distributed with a newspaper from the sales and use tax. The supplies used to produce free circulation publications such as shoppers' guides and sales by printers of free circulation publications to the publishers of these publications were exempt from sales and use taxation in 1985.

Neighboring States Policies
Trends: There are no identifiable trends
yes - tax
no - exempt

State	Newspapers	Magazines	Free Circulation
Florida	yes	yes	no
Georgia	yes	yes	yes
Kentucky	yes	yes	yes
South Carolina	no	yes	no*
Tennessee	no	subscription	no
Virginia	no	no	no
		To be Confirmed	

* Circulations printed on newsprint are exempt
Tennessee exempts direct mail advertisements from outside state
Virginia taxes subscription sales of publications

F. Sales Through Vending Machines & Coin Operated Laundries

The sale of tangible personal property, other than soft drinks and cigarettes, through vending machines is taxed at 50% of the sales price while similar products sold across the counter are taxed at 100% of the sales price. The sales tax on soft drinks and cigarettes is levied on 100% of the sales price whether sold through a vending machine or across the counter. The legislation that changed the definition of sales price on some products sold through vending machines was passed in 1989.

The gross receipts from coin operated laundry machines are not subject to the sales tax. Other services provided by laundries, dry cleaners, and businesses leasing clean linens, towels and apparel are taxed at the 6% rate.

Neighboring States Policies
Trends: No identifiable trends

STATE	POLICIES
Florida	Tax food and beverages sold through vending machines. Rate varies by taxing unit but greater than state rate of 6%.
Georgia	Taxes food sold through vending and receipts of coin operated laundries
Kentucky	Exempts sales through coin operated vending machines of 25 cents or less
South Carolina	No exemptions allowed
Tennessee	Exempts vending, coin operated laundry machines, & amusement devices; vending and amusement devices are subject to a privilege license tax
Virginia	TO Be Confirmed

IV. Corporate Income Tax Multi-State Apportionment

A. Multi-State Apportionment Formula

Apportionment is the means by which multi-state corporations allocate their nationwide income to each state in which they operate. An apportionment formula is a ratio of a corporation's business activity in a state to its total business activity in the U.S.. The formula adopted in the late 1930's by most states is a three factor formula comparing the property, payroll, and sales in each state to the national total.

In the 1930's when North Carolina adopted an apportionment formula all the factors were "weighted" equally; (33 1/3%) property, (33 1/3%) payroll, and (33 1/3%) sales. In 1988, North Carolina, following the practice of many other states, changed the weighting to favor home-state industries by adopting the "double-weighted sales factor".

This change, provides tax relief for corporations that are domiciled in the State because those corporations tend to have a greater concentration of property and payroll in North Carolina, but shipments all over the United States. The majority of states that have modified their formulas weight the sales factor by an amount greater than the weights on property and payroll.

Neighboring States Policies

Trends: The majority of states use a three factor apportionment formula of property, payroll, and sales. As recently as 1994, Arizona, California, Maine, Maryland, Michigan, New Hampshire, and Oregon adopted a double weighted sales factor. Minnesota weights property and payroll at 15% and sales at 70%.

	APPORTIONMENT FACTORS			
STATE	**SALES**	**PROPERTY**	**PAYROll**	**THROWBACK RULE**
Florida	50 %	25	25 %	no
Georgia	331/3	331/3	331/3	no
Kentucky	50	25	25	no
North Carolina	50	25	25	no
South Carolina	331/3	331/3	331/3	no
Tennessee	331/3	331/3	331/3	no
Virginia	331/3	331/3	331/3	no

IV B. The Throwback Rule

Under an apportionment formula the income from sales is generally assigned to a state based on the ultimate destination of the goods. There is an exception when computing the sales factor. Sales can be "thrown back" to the state from which the goods are shipped if the seller is not taxable in the state of the purchaser or the purchaser is the U.S. Government.

Sales to the U.S. Government are allowed to be thrown back because it is often difficult to determine the true destination of shipments. The taxability of a seller in the state of the purchaser is based on whether the seller has employees, property, or sufficient activity in the state. If the state of the purchaser cannot tax the seller, sales to that state will escape taxation unless they are thrown back to the seller's state.

Throwback
continued

Other States Policies

Trends: Twenty four states have adopted a throwback rule that applies to sales. Four states do not have a corporate income tax.

Alabama	Maine	Oregon
Alaska	Massachusetts	Texas
Arizona	Michigan	Utah
California	Missouri	Vermont
Colorado	Montana	
District of Columbia	Nebraska	
Idaho	New Hampshire	
Illinois	New Mexico	
Indiana	North Dakota	
Kansas	Oklahoma	

V. Gross Premiums Tax, Guaranty Fund Credit

Insurers in North Carolina must pay an annual tax on the gross premiums credited to policies written or processed in this state or derived from business written in this state. The tax rates for various types of insurance are as follows:

Workers' Compensation	2.5%
All Other Insurance	1.9%
Surcharge on Fire and Lightning	1.33%
Blue Cross & Blue Shield	.5%

The tax is paid in three quarterly payments with the balance due March 15. Insurers are exempt from the franchise and income tax.

In 1991, the General Assembly enacted a credit against the gross premium tax for assessments paid to the North Carolina Insurance Guaranty Association and the North Carolina Life and Health Insurance Guaranty Association. An insurer who pays an assessment to one of the Associations receives a tax credit equal to the assessment amount. The insurer may take 20% of the credit in each of the five tax years following the year in which the assessment was paid. For example, insurers in 1991 paid $20,299,250 in assessments. Beginning in 1992, the insurers claimed 20% of the assessments or $4,059,850 as a credit against their gross premium tax bill. On the insurers' 1996 tax returns, the fifth year of the 1991 credit will be taken. **The total cost of the Guaranty Fund tax credit in 1996 is $34,113,686.**

Assessments are made against insurers to pay for the covered claims and all other expenses of insolvent insurers. Assessments are made by the Guaranty Associations in proportion to the amount of premiums written by an insurer for each type of insurance. The assessment cannot exceed 2% of the net direct written premiums for the preceding calendar year. The Associations may exempt insurers from the assessments if they endanger the firms' financial health.

Neighboring States Policies

STATE	% Assessment	Credit # Years Allowable
Florida	Repealed	
Georgia	100%	5
Kentucky	100%	5 & 10
South Carolina	100%	5
Tennessee	100%	4 & 10
Virginia	100%	*

* Credits are allowed as a percentage of tax liability

VI. Individual Income Tax

A. Conform to Federal Law Regarding Social Security Income

In 1983, the National Commission on Social Security Reform ("Greenspan Commission")came out with a set of recommendations designed to ensure the solvency of the Social Security system into the early years of the next century. One of the recommendations was to tax the Social Security benefits of high-income recipients. The approach adopted by the Congress was to tax up to 50% of benefits for recipients whose base income exceeded $25,000 ($32,000 for married couples filing jointly). Base income was defined as the sum of adjusted gross income, tax-exempt interest, and one-half of Social Security benefits.

In 1993, the Congress changed the system to levy a tax on up to 85% of Social Security benefits for recipients whose base income exceeded $34,000 ($44,000 for married couple filing jointly).

In North Carolina, the 1987-88 Tax Fairness Study Commission adopted a recommendation to convert the state's free-standing personal income tax to one that tied into federal taxable income (income remaining after deductions and exemptions). This change would pick up the federal rules on income subject to taxation, including Social Security benefits. However, concerns raised by recipients during the 1989 legislative session led the chief sponsor to decide to maintain the full exemption. This would allow legislators to re-focus their attention on the overall reform package.

B. Exclusions for Private and Public Retirement Benefits

For decades the federal approach to the taxation of pensions and other retirement benefits has been to exempt the contributions (and associated investment earnings) of employers. When the retiree begins drawing benefits, the federal tax applies to any contributions that were sheltered on the front end.

Until 1989, North Carolina allowed a full exemption for the retirement benefits of state and local retirees. The exclusion for state benefits goes back to the early-1950's and was codified in the retirement system law.

In the late-1960's and early-1970's the state began allowing a small exemption for federal civil service and military retirees. In 1988 these exemptions were increased from $3,000 to $4,000.

In 1989 the U.S. Supreme Court ruled in the Davis case that it is unconstitutional for a state to allow more favorable tax treatment for its own employees (including retirees) than that allowed federal workers. The 1989 General Assembly addressed this issue by adopting a $4,000 exemption for all public sector retirees. In addition, a $2,000 exclusion was provided for private pensions.

VII. Excise Tax Discounts and Timely Payments

Distributors of tobacco, soft drink, beer, and wine products in the State are allowed a discount for the payment of the excise tax if the tax is paid when due.

Distributors of tobacco, beer, and wine products are allowed a 4% discount of the excise tax due the State. Distributors of soft drink products pay a reduced rate equal to ½ the excise tax on the first 15,000 gross of ready to drink product sold at wholesale; after this amount the discount is 4% of the excise tax on bottled soft drinks owed. The discount on the sale of powdered and liquid base product is limited to 4% of the tax due. Retailers of soft drink products that are required to remit the excise tax are allowed a 4% discount.

Neighboring States Policies
Trend: No identifiable trend

STATE	POLICY
Florida	1.9% distributors of wine 2.5% distributors of malt and beer 1% distributors of spirituous liquor
Georgia	No discounts
Kentucky	No discounts
South Carolina	2% distributors of wine, beer & liquor
Tennessee	3% of beer
Virginia	1% of tax due

State Apportionment of Corporate Income

January 1, 1996

ALABAMA *	3 Factor	MONTANA *	3 Factor
ALASKA *	3 Factor	NEBRASKA	Sales
ARIZONA *	Double wtd. sales	NEVADA	No State Income Tax
ARKANSAS *	Double wtd. sales	NEW HAMPSHIRE	Double wtd. sales
CALIFORNIA *	Double wtd. sales	NEW JERSEY (1)	3 Factor
COLORADO *	3 Factor/Sales & Property	NEW MEXICO *	3 Factor
CONNECTICUT	Double wtd. sales	NEW YORK	Double wtd sales
DELAWARE	3 Factor	NORTH CAROLINA	Double wtd. sales
FLORIDA *	Double wtd. sales	NORTH DAKOTA *	3 Factor
GEORGIA	Double wtd. sales	OHIO	Double wtd. sales
HAWAII *	3 Factor	OKLAHOMA	3 Factor
IDAHO *	Double wtd. sales	OREGON *	Double wtd. sales
ILLINOIS*	Double wtd. sales	PENNSYLVANIA *	Double wtd. sales
INDIANA	3 Factor	RHODE ISLAND	3 Factor
VA	Sales	SOUTH CAROLINA	Double wtd. sales
NSAS *	3 Factor/Sales & Property	SOUTH DAKOTA	No State Income Tax
KENTUCKY *	Double wtd. sales	TENNESSEE *	3 Factor
LOUISIANA	3 Factor	TEXAS	No State Income Tax
MAINE *	Double wtd. sales	UTAH *	3 Factor
MARYLAND	Double wtd. sales	VERMONT	3 Factor
MASSACHUSETTS*	Double wtd. sales	VIRGINIA	3 Factor
MICHIGAN	Double wtd. sales	WASHINGTON	No State Income Tax
MINNESOTA	70% Sales,15% Property, and 15% Payroll	WEST VIRGINIA	Double wtd. sales
		WISCONSIN *	Double wtd. sales
MISSISSIPPI	Accounting/3 Factor	WYOMING	No State Income Tax
MISSOURI *	3 Factor/sales	DIST. OF COLUMBIA *	3 Factor

Source: Compiled by FTA from various sources.
** State has adopted substantial portions of the UDITPA.*
(1) Will adopt a double weighted sales factor for tax years beginning after 7/1/96.

Table 18

State Income Tax Treatment of Social Security and Pension Income Exemptions, 1993

State	Social Security Tax Exempt	Amount of Exemptions				Age Minimums for Pension Exclusions	Income Qualifying Restrictions for Pension Exclusions
		Private	Military	Federal	State/ Municipal		
Alabama*	Yes	None/Full	Full	Full	Full	No	No
Alaska	No state income tax						
Arizona	Yes	None	$2,500	$2,500	$2,500	No	No
Arkansas*	Yes	$6,000	$6,000	$6,000	$6,000	No	No
California*	Yes	None	None	None	None	n.a.	n.a.
Colorado*	No	$20,000	$20,000	$20,000	$20,000	Yes	No
Connecticut	No	None	None	None	None	n.a.	n.a.
Delaware*	Yes	$2,000/ $3,000	$2,000/ $3,000	$2,000/ $3,000	$2,000/ $3,000	No	Yes
District of Columbia*	Yes	None	$3,000	$3,000	$3,000	Yes	No
Florida	No state income tax						
Georgia*	Yes	See state note					
Hawaii*	Yes	Full	Full	Full	Full	No	No
Idaho*	Yes	None	$13,536	$13,536	None	Yes	No
Illinois*	Yes	Full	Full	Full	Full	No	No
Indiana*	Yes	None	$2,000	$2,000	None	Yes	No
Iowa*	No	None	None	None	None	n.a.	n.a.
Kansas*	No	None	$120 TC	Full	Full	No	No
Kentucky	Yes	None	Full	Full	Full	No	No
Louisiana*	Yes	$6,000	Full	Full	Full	Yes	No
Maine*	Yes	None	None	None	None	n.a.	n.a.
Maryland*	Yes	See state note				Yes	Yes
Massachusetts*	Yes	None	None	Full	Full	No	No
Michigan*	Yes	$7,500	Full	Full	Full	No	No
Minnesota*	No	See state note					
Mississippi	Yes	$6,000	$6,000	$6,000	$6,000	No	No
Missouri*	No	None	$6,000	$6,000	$6,000	No	Yes
Montana*	No	$3,600	$3,600	$3,600	$3,600	No	Yes
Nebraska	No	None	None	None	None	n.a.	n.a.
Nevada	No state income tax						
New Hampshire	Only dividends and interest subject to state income tax						
New Jersey*	Yes	$7,500	$7,500	$7,500	$7,500	Yes	No
New Mexico*	No	See state note					
New York*	Yes	$20,000	Full	Full	Full	Yes	No
North Carolina*	Yes	$2,000	$4,000	$4,000	$4,000	No	No
North Dakota*	No	None	$5,000	$5,000	$5,000	Yes	No
Ohio*	Yes	None	None	None	None	n.a.	n.a.
Oklahoma	Yes	None	$5,500	$5,500	$5,500	No	No
Oregon*	Yes	See state note					

Table 18 (cont.)

State Income Tax Treatment of Social Security and Pension Income Exemptions, 1993

State	Social Security Tax Exempt	Amount of Exemptions				Age Minimums for Pension Exclusions	Income Qualifying Restrictions for Pension Exclusions
		Private	Military	Federal	State/ Municipal		
Pennsylvania	Yes	Full	Full	Full	Full	No	No
Rhode Island*	No	None	None	None	None	n.a.	n.a.
South Carolina*	Yes	$3,000/ $10,000	$3,000/ $10,000	$3,000/ $10,000	$3,000/ $10,000	No	No
South Dakota	No state income tax						
Tennessee	Income tax base excludes pensions and retirement income						
Texas	No state income tax						
Utah*	No	See state note					
Vermont*	No	None	None	None	None	n.a.	n.a.
Virginia*	Yes	See state note					
West Virginia*	No	None	$2,000	$2,000	$2,000	No	No
Wisconsin*	No	None	None/Full	None/Full	None/Full	No	No
Wyoming	No state income tax						

TC—tax credit
n.a.—not applicable

'ate Notes

..labama Only private pensions under a defined benefit plan are tax exempt.

Arkansas The total exemption from all retirement plans may not exceed $6,000 per pensioner. Persons age 65 and over who do not claim the $6,000 deduction qualify for a $20 tax credit.

California California also offers an elderly (age 65 or older) tax credit equal to 50% of the federal elderly tax credit, also available to taxpayers under age 65 and disabled.

Colorado Pensioners must be age 55 to claim an exemption. The $20,000 pension exclusion also includes Social Security benefits (i.e., a taxpayer whose Social Security benefits and pension income exceed $20,000 is taxed on the excess income).

Delaware Persons under age 60 receive a $2,000 pension exclusion; persons age 60 and over receive a $3,000 pension exclusion. The total exemption from all retirement plans cannot exceed the $2,000 or $3,000 exclusions. Single taxpayers or married taxpayers filing separately who are 60 or older with an earned income of less than $2,500 and a Delaware adjusted gross income (AGI) of $10,000 or less are eligible to receive an additional $2,000 exemption. Joint filers who are age 60 or over with an earned income of less than $5,000 and a Delaware AGI of $20,000 or less are eligible to receive an additional $4,000 exemption.

District of Columbia Pensioners must be age 62 to qualify for the $3,000 exemption. Taxpayers age 62 and over are eligible to receive a property tax credit.

Georgia Taxpayers must be age 62 or older or totally disabled to claim this retirement income exemption, which includes all unearned income, such as pension income, interest, and dividends, and the first $4,000 of earned income for a maximum exclusion of $10,000 per taxpayer. With married couples, each can exclude up to $10,000.

Hawaii Noncontributory private pension plans are tax exempt. With contributory private pension plans, earnings are taxed and employee contributions are tax exempt.

Idaho Pensioners must be age 65 and over or from 62-64 and disabled to qualify for the pension exclusion. Pension exemption amounts are $13,536 (single filers) and $20,304 (married couples); these amounts are adjusted annually according to the maximum benefit under Social Security and railroad pension amounts received. Allowable state/municipal pension exclusions include pensions from a city police retirement fund or from the state retirement fund for fire fighters.

Illinois Private pension income is fully exempt if income is under Internal Revenue Code sections 402(a), 402(c), 403(b), 406(a), 407, and certain other distributions.

Indiana Federal pensioners must be age 62 or older to claim the pension exemption. The amount federal retirees may exclude is offset by Social Security and railroad retirement benefits. Military pensioners must be age 60 or older to claim the exemption. Limited tax credits are available to persons over age 65.

State Notes *(cont.)*

Iowa All pension income is fully taxed, effective tax year 1991.

Kansas Military pensions are fully taxed, but military pensioners age 62 and over may claim a $120 credit against income tax liability. The April 1992 U.S. Supreme Court ruling in *Barker* v. *Kansas* resulted in the state exempting military pensions effective tax year 1992 and repealing the $120 tax credit for military pensions.

Louisiana Private pensioners must be age 65 or over to qualify. Pension exclusions will be reduced for federal income tax attributable to exempt income for pensioners receiving $15,000 or over in exempt income including pension income; interest income from U.S. government obligations and federal taxable Social Security benefits based on reported exempt income over $15,000.

Maine Retirement contributions under Maine's retirement system, which were previously taxed by Maine, are not taxed as retirement income for pensioners retiring in 1989, 1990, and 1991. Taxpayers qualifying for the federal elderly tax credit may claim 20% of the federal credit as a Maine tax credit.

Maryland All pensions are fully taxed except for persons age 65 or over and/or disabled. Pensioners who are age 65 or over and/or disabled must exclude the lesser amount of net taxable pension and retirement annuity included as income on the federal return, or $13,100 minus Social Security and federal railroad retirement benefits received. The exemption amount changes annually according to the maximum Social Security benefit received. Military pensioners are eligible for an additional pension exclusion of up to $2,500. To qualify, a pensioner must be age 55 or older and be an enlisted member of the military at retirement. The exclusion amount depends on federal adjusted gross income, which must be under $22,500 to qualify.

Massachusetts Most federal and state-municipal pensions are contributory and, therefore, are fully tax exempt, while military and most private pensions are noncontributory and, therefore, fully taxed. Massachusetts does not tax income of Massachusetts residents from contributory public pensions from other states that do not tax former pensions of Massachusetts state employees. In February 1990, the Massachusetts Commissioner of Revenue determined these states to be Alaska, Connecticut, Florida, Hawaii, Illinois, Nevada, New Hampshire, Pennsylvania, South Dakota, Tennessee, Texas, Washington, and Wyoming.

Michigan Private pensioners may exclude up to $7,500 (single filers), $10,000 (married filing jointly), and $10,000 (married filing separately for a combined total). To qualify for the exemptions, pension plans or private pensioners must define eligibility for retirement and set contribution and benefit amounts in advance.

Minnesota Although Minnesota does not specifically exclude pension income, persons age 65 or older who qualify may subtract from any income source $8,000 (single filers) or $10,000 (married filing jointly) or $5,000 (married filing separately) less nontaxable Social Security and retirement benefits, and one-half of federal adjusted gross income (AGI) over $12,000 (single filers) or $15,000 (married filing jointly) or $7,500 (married filing separately). Since nontaxable Social Security benefits are subtracted, those who benefit from this exclusion are usually not receiving Social Security benefits, such as federal retireees. As a result of how the formula works, to qualify for the subtractions, one must meet the following income requirements: (1) AGI must be less than $35,000 and railroad retirement benefits and nontaxable Social Security are less than $10,000 (married filing jointly); (2) AGI must be less than $17,500 and railroad retirement benefits and nontaxable Social Security are less than $5,000 (married filing separately); (3) AGI must be less than $32,000 and railroad retirement benefits and nontaxable Social Security are less than $10,000 (married, one spouse under 65, filing jointly); (4) AGI must be less than $28,000 and railroad retirement benefits and nontaxable Social Security are less than $8,000 (single filers).

Missouri The $6,000 exemption for state, federal, and military pensioners is available if the single pensioner earns less than $25,000 per year (Missouri AGI less federal taxable Social Security) or if the pensioner who is married and files separately earns less than $16,000 or $32,000 maximum filing combined (Missouri AGI less federal taxable Social Security). Tax credits with income restrictions are available for taxpayers age 65 or older.

Montana The exemption is reduced by $2 for every $1 that federal AGI exceeds $30,000. The exemption is entirely phased out when income equals $31,800 (assuming a retirement income of $3,600 or greater).

New Jersey Pensioners must be age 62 or older or disabled under Social Security to qualify for the exclusion. Exclusion amounts are $7,500 (single filers), $10,000 (married filing jointly), and $5,000 (married filing separately).

New Mexico Taxpayers age 65 or older might be eligible to exlude up to $8,000 from any source depending on their income level and marital status.

New York Private pensioners have to be at least 59 1/2 years old to qualify for the $20,000 exemption.

North Carolina The total pension exemption from all pension income sources may not exceed $4,000 per pensioner. A tax credit is available for pensioners who did not receive a tax refund for taxes paid on public pensions in 1988.

North Dakota For military pension exclusions, pensioners must be age 50 or older to qualify. Pensioners must file the long form to qualify for pension exclusions. All pension exclusions are reduced by Social Security benefits received. Only highway patrol, city police, and city fire fighters qualify to receive the $5,000 exemptions under state-municipal retirement pension plans.

Table 18 (cont.)

State Income Tax Treatment of Social Security and Pension Income Exemptions, 1993

tate Notes *(cont.)*

Ohio Limited tax credits are available to pensioners. Some of these tax credits are restricted to taxpayers age 65 or older.

Oregon Starting in 1991, taxpayers over age 58 whose household income is less than $45,000 (married filing jointly) or $22,500 (other filing statuses), are eligible for a retirement tax credit that can be as much as 9% of pension income depending on the level of total income and Social Security benefits. The minimum eligibility age will gradually increase each year until age 62 for tax year 1999. Oregon also offers an elderly tax credit equal to 40% of the federal elderly tax credit; however, taxpayers may apply for either this credit or the retirement income tax credit, but not both.

Rhode Island Taxpayers age 65 and over are eligible to receive a property tax credit.

South Carolina Beginning in tax year 1993, a taxpayer, under 65 years of age, receiving a qualified retirement income must irrevocably elect: (1) to claim no retirement deduction until the taxpayer turns 65 at which time the taxpayer would be entitled up to a $10,000 retirement deduction for life; or (2) to claim a deduction up to $3,000 each year for life. If age 65 years or older in 1993, retirement income would automatically qualify for the $10,000 deduction. Qualified retirement income includes those plans defined in *Internal Revenue Code* sections 401, 403, 408, 457, and all public retirement plans of the federal, state, and local governments.

Utah Pensioners under age 65 may exclude up to $4,800 on pension income and Social Security benefits (taxable on federal form). Pensioners age 65 or over may exclude up to $7,500 on all income sources. Since 1988, exclusions have been subject to $1 reduction for every $2 of AGI in excess of $25,000 (single filers), $32,000 (married filing jointly), and $16,000 (married filing separately).

Vermont Taxpayers age 65 or older are eligible for a nonrefundable elderly tax credit equal to 28% of the federal elderly tax credit.

Virginia Taxpayers age 62 to 64 receive a $6,472 exclusion from any income source while those age 65 or older receive a $12,944 exclusion from any income source. Both exclusions are, however, decreased by Social Security and railroad retirement benefits. Joint filers qualify for twice the exclusion amounts even if one spouse earns less than the exclusion amount of $6,000 or $12,000 minus Social Security and railroad retirement benefits. As of 1992, exclusions are indexed by FICA wage base percentage increases.

West Virginia Pensioners receive up to a $2,000 pension exclusion (except for private pensioners and some small municipalities that do not participate in the state retirement system). Some public safety officials get a full exemption (i.e., any state or local police or fire fighters' retirement system). Taxpayers age 65 or over and/or taxpayers of any age who are permanently disabled may exclude a total of up to $8,000 of income from any source. However, any of the pension exclusions count toward the $8,000 ceiling.

Wisconsin Only military, federal, and certain state or municipal pensioners who retired prior to 1/1/64, or were members of the retirement system prior to 1/1/64 and then retired at a later date, qualify for a tax exemption on their pension income. However, for state and local government retirees, only certain Milwaukee city, Milwaukee County, and the Wisconsin teachers' retirement systems qualify for exemptions, subject to the aforementioned conditions. In addition to the pension exemption, a $25 tax credit is offered to taxpayers age 65 and over.

Source: David Baer, *State Taxation of Social Security and Pensions* (Washington, DC: American Association of Retired Persons, 1993).