

# GENERAL ASSEMBLY OF NORTH CAROLINA

Session 2007

## Legislative Fiscal Note

**BILL NUMBER:** Senate Bill 1952 (Second Edition)

**SHORT TITLE:** Small Business Tax Protection Act

**SPONSOR(S):** Senator Hoyle

FISCAL IMPACT					
	Yes (X)	No ( )	No Estimate Available ( )		
	(\$ In Millions)				
	<u>FY 2008-09</u>	<u>FY 2009-10</u>	<u>FY 2010-11</u>	<u>FY 2011-12</u>	<u>FY 2012-13</u>
REVENUES:					
General Fund	(\$5.9)	(\$2.3)	(\$2.4)	(\$2.4)	(\$2.5)
Local Governments	(\$3.5)	(\$1.0)	(\$1.0)	(\$1.0)	(\$1.1)
EXPENDITURES					
Department of Revenue	No Fiscal Impact				
PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED: North Carolina Department of Revenue; North Carolina Local Governments					
EFFECTIVE DATE: Section 1 becomes effective when it becomes law and apply retroactively to sales and use tax assessments made on or after May 1, 2005; Sections 2 and 3 become effective January 1, 2009; Section 4 becomes effective when law.					

### BILL SUMMARY:

Senate Bill 1952 provides small businesses (defined as businesses with gross receipts below \$1.8 million) with certain protections related to their sales and use tax obligations, including an opportunity to consult with the Department of Revenue regarding the application of sales and use tax laws, the reduction of an assessment for good faith compliance, and a waiver of penalties and interest for reasonable reliance on erroneous verbal advice.

If a business meets certain requirements, the Department must waive penalties and reduce any assessment for sales and use taxes. The requirements are as follows:

- The business remitted all the sales and use taxes it collected during the relevant period.

- The business was not instructed in a prior audit to collect sales and use taxes in the circumstance that is the basis of the assessment.
- The business attempted to comply with the law by seeking and following advice from the Department regarding its sales and use tax obligations.
- The business made a good faith effort to comply with the sales and use tax laws and the assessment is based on the incorrect application of one of the following complex areas:
  1. The rate of tax that applies to food.
  2. The distinction between a retailer and a performance contractor.
  3. The distinction between a service that is exempt from tax and a service that is provided in conjunction with the delivery of tangible personal property and is part of the sales price of the tangible personal property.
  4. The determination of whether a person is a manufacturer.

The amount of the reduction is a percentage of the assessment and varies depending on the average monthly gross receipts of the business.

Section 2 requires the Department to document the verbal advice provided to taxpayers and provide in writing if requested. If the Department furnishes erroneous written advice in response, and the taxpayer reasonably relies on the advice, the taxpayer is not liable for any penalty or additional assessment attributable to the erroneous advice. Section 3 of this bill would waive penalties and any additional assessment resulting from erroneous verbal advice furnished by the Department as long as neither was the result of the taxpayer's failure to provide adequate or accurate information.

Section 4 of the bill rewrites the offer and compromise statute so that it more accurately reflects current practice, is adjusted for inflation, and eliminates the requirement that the Department obtain approval from the Attorney General unless the matter is in litigation. Section 4 also adds a new condition under which the Department may settle a tax liability for less than that asserted to be due. The new provision is consistent with the sales and use tax protections afforded small retailers under other sections of this bill.

#### **ASSUMPTIONS AND METHODOLOGY:**

Fiscal Research estimates that SB 1952 represents \$9.4 million in state and local sales and use tax expenditures for the 2008-09 fiscal year and \$3.5 million in subsequent years.

According to the Department of Revenue, small business audits from July 1, 2005 to date represent a total of \$19.8 million in sales and use tax assessments, penalties, and interest. Contingent on each company's gross receipts, between 98 percent and 90 percent of assessments and other fees are eligible for forgiveness under SB 1952. If 95 percent of the \$19.8 million is eligible for forgiveness, companies could be refunded a maximum of \$18.8 million in assessments, penalties, and interests.

Based on the percent of non-profits that apply for the sales and use tax refund, Fiscal Research estimates that roughly 50 percent of the businesses will apply for a refund under SB 1952. Therefore, this legislation represents \$9.4 million (50 percent of \$18.8 million) in forgiven sales and use tax assessments, penalties, and interest for the 2008-09 fiscal year. For future years, Fiscal

Research estimates that roughly one-sixth of the existing sales and use tax assessments and the associated fees will be applicable to the criteria set forth in the bill and thus remain uncollected.

## **Section 2**

Section two of the bill addresses the administrative responsibilities of the Department and will not have a fiscal impact on the Department's expenditures. The Department's current policy requires employees to document requests from and responses to taxpayers. The Department established a Notes Policy in August of 2000. The Notes Policy requires employees to document taxpayers' requests and responses through notes in the ITAS system in certain cases. The policy states there may be additional situations not covered in the document that require notes. The policy also directs employees to always err on the side of making the note if they question whether the matter should be documented or not.

**SOURCES OF DATA:** North Carolina Department of Revenue

**TECHNICAL CONSIDERATIONS:** None

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