

**GENERAL ASSEMBLY OF NORTH CAROLINA**

**Session 2013**

**Legislative Fiscal Note**

**BILL NUMBER:** House Bill 998 (Third Edition)

**SHORT TITLE:** Tax Simplification and Reduction Act.

**SPONSOR(S):** Representatives Lewis, Setzer, Moffitt, and Szoka

Please see the fiscal impact table on the following page.

<b>FISCAL IMPACT</b>					
(\$ in millions)					
<b>State General Fund Revenues:</b>	<b>FY 13-14</b>	<b>FY 14-15</b>	<b>FY 15-16</b>	<b>FY 16-17</b>	<b>FY 17-18</b>
<b>Income, Franchise, and Piped Natural Gas Tax</b>					
Create flat personal income tax with 5.9% rate. Eliminate personal exemption. Allow greater of standard deduction or mortgage interest and property taxes capped at \$25,000 plus all charitable contributions. Enhances child credit.	(392.5)	(983.0)	(1024.9)	(1068.4)	(1113.7)
Repeal \$50,000 business income deduction effective for 2013	375.7	395.5	421.4	442.0	452.0
Reduce corporate income tax rate from 6.9% to 6.5% in 2014, 6.35% in 2015, 6.2% in 2016, 5.6% in 2017, 5.4% in 2018	(32.7)	(85.7)	(115.7)	(189.6)	(282.4)
End transfer to Public School Capital Fund	85.8	84.7	84.0	81.1	79.2
Reduce franchise tax rate from \$1.50 to \$1.35 per \$1,000		(52.5)	(54.6)	(56.8)	(59.1)
Repeal gross receipts franchise tax on electricity		(157.0)	(159.0)	(160.6)	(162.2)
Repeal excise tax on piped natural gas		(31.5)	(32.0)	(32.5)	(32.9)
<b>TOTAL INCOME AND FRANCHISE TAX</b>	<b>\$ 36.3</b>	<b>\$ (829.5)</b>	<b>\$ (880.8)</b>	<b>\$ (984.7)</b>	<b>(1119.1)</b>
<b>Sales and Privilege License Taxes</b>					
Make electricity subject to combined general sales tax rate		417.1	427.7	440.5	453.8
Make piped natural gas subject to combined general sales tax rate		102.3	103.9	105.4	107.0
Distribution to municipalities for franchise tax and piped natural gas		(207.1)	(209.4)	(211.6)	(213.8)
Repeal gross receipts tax on live entertainment and movies and other amusements, imposing a sales tax	9.3	16.5	17.2	17.9	18.6
Repeal sales tax exemption for nutritional supplements sold by chiropractors	0.1	0.1	0.1	0.1	0.1
Repeal Energy Star sales tax holiday	1.6	1.6	1.7	1.8	1.8
Expand sales tax to include repair, maintenance, and installation of tangible personal property		173.3	185.3	198.4	210.5
Expand sales tax to include service contracts		29.2	31.2	33.2	35.2
<b>TOTAL SALES and PRIVILEGE LICENSE TAX</b>	<b>\$11.0</b>	<b>\$533.1</b>	<b>\$557.6</b>	<b>\$585.7</b>	<b>\$613.2</b>
<b>STATE IMPACT</b>	<b>\$ 47.3</b>	<b>\$ (296.4)</b>	<b>\$ (323.2)</b>	<b>\$ (399.1)</b>	<b>(505.9)</b>
<b>Local Revenues</b>					
Repeal franchise tax on electricity		(187.0)	(189.0)	(190.9)	(192.8)
Repeal excise tax on piped natural gas		(20.1)	(20.4)	(20.7)	(21.0)
Distribution to municipalities for electric and piped natural gas		207.1	209.4	211.6	213.8
Repeal privilege tax on live entertainment and movies and other amusements, imposing a sales tax	5.8	6.6	6.9	7.2	7.4
Repeal exemption for nutritional supplements sold by chiropractors	0.0	0.0	0.0	0.0	0.0
Repeal Energy Star tax holiday	0.6	0.6	0.7	0.7	0.7
Expand base to include repair, maintenance, and installation of tangible personal property		69.3	74.1	79.4	84.2
Expand base to include service contracts		11.7	12.5	13.3	14.1
<b>LOCAL IMPACT</b>	<b>\$6.4</b>	<b>\$88.2</b>	<b>\$94.2</b>	<b>\$100.6</b>	<b>\$106.4</b>

## **BILL SUMMARY:**

### **PERSONAL INCOME TAX**

Section Two makes the changes described below to the personal income tax. Unless otherwise indicated, the changes are effective for the 2014 tax year.

- Eliminates the \$50,000 business income deduction, effective for the 2013 tax year
- Creates a flat 5.9% tax rate
- Eliminates the personal exemption
- Allows the greater of:
  - Standard deduction amount of \$12,000 for married filing joint taxpayers
  - Deductions for mortgage interest and property taxes capped at \$25,000
- Eliminates deduction for severance wages
- Repeals tax credit for non-itemizer charitable contributions
- Increases child tax credit from:
  - \$100 to \$250 if adjusted gross income is equal to or less than \$100,000
  - 0 to \$125 if adjusted gross income is greater than \$100,000
- Removes the sunset on the Low-income Housing Tax Credits renamed the Workforce Housing Loan Construction Program. The current sunset is January 1, 2015.

### **CORPORATE TAX**

Section Three makes the changes described below to the corporate income and franchise taxes.

- Reduces the corporate income tax rate from 6.9% to 6.5% in 2014, to 6.35% in 2015, to 6.2% in 2016, to 5.6% in 2017, and to 5.4% in 2018
- Reduces franchise tax rate from \$1.50 to \$1.35 per \$1,000, effective for taxes paid in 2015
- Repeals earmarking of corporate income tax revenues for Public School Building Capital Fund

### **SALES AND USE TAX**

Section Four makes the changes described below to the sales tax. Unless otherwise indicated, the changes are effective July 1, 2014.

- Repeals gross receipts franchise tax on electricity.
- Makes electricity subject to the full State and local sales tax rate.
- Repeals excise tax on piped natural gas.
- Makes piped natural gas subject to the full State and local sales tax rate.
- Directs the Utilities Commission to make rate cut to reflect the repeal of the gross receipts tax on electricity and the excise tax on piped natural gas.
- Distribute portion of State sales tax on electricity to cities, based on the amount a city received under the repealed gross receipts franchise tax distribution of electricity to the

city. The Department of Revenue must re-calculate a city's franchise tax share every five years, beginning July 1, 2020.

- Distribute portion of State sales tax rate on piped natural gas to cities, based on the amount a city received under the repealed excise tax distribution of piped natural gas to the city. The Department of Revenue must re-calculate a city's excise tax share every five years, beginning July 1, 2020.
- Repeals gross receipts privilege tax on live entertainment and movies (effective July 1, 2013).
- Imposes sales tax on live entertainment and movies. Retains all exemptions that apply in current gross receipts privilege license tax statute (effective July 1, 2013).
- Repeals sales tax exemption for nutritional supplements sold by chiropractors (effective July 1, 2013).
- Repeals Energy Star sales tax holiday (effective July 1, 2013).
- Expands sales tax to include repair, maintenance, and installation of tangible personal property
- Expands sales tax to include service contracts
- Repeals sales tax exemption for installation charges
- Exempts from sales tax repair, maintenance, installation, and service contracts applicable to items exempt from sales tax (except for motor vehicles)
- Allows the Secretary of Revenue to compromise a taxpayer's tax liability if the item subject to tax is one added by this act, ie, entertainment, movies, service contracts, repair & maintenance (expires effective July 1, 2016).

## **ASSUMPTIONS AND METHODOLOGY:**

### *Personal Income, Corporate Income, and Franchise Taxes*

The estimated impact of the individual income tax changes is based on the North Carolina BearingPoint Individual Income Tax Model and on information obtained from the Department of Revenue.

The estimated impact of the corporate income, and franchise tax changes are based on queries of tax collection data obtained from the Department of Revenue, on the Tax Expenditure Report, and on Economic Incentive Reports.

Sufficient data was not available to determine the impact of the sunset removal for the low-income housing credits. The credits currently cost approximately \$40 million annually; however, the PCS to H998 would extend the program only in tier 1 and 2 counties. Therefore, the impact would be less than \$40 million and would impact the General Fund beginning in FY 15-16.

### *Sales and Use and Privilege License Taxes*

Fiscal Research utilized data from the North Carolina Department of Revenue's 2011 Tax Expenditure Report as well as the information provided in the 2010 Statistical Abstract to calculate the impact of repealing various tax exemptions. The estimated impact of the sales and use tax base expansion is based on industry sales data compiled from the 2007 Economic Census, as reported by the US Census Bureau.

**SOURCES OF DATA:** NC Department of Revenue, North American Industry Classification System, U.S. Census Bureau, North Carolina BearingPoint Individual Income Tax Model

**TECHNICAL CONSIDERATIONS:** None

**FISCAL RESEARCH DIVISION:** (919) 733-4910

**PREPARED BY:** Jonathan Tart

**APPROVED BY:**

Mark Trogdon, Director  
**Fiscal Research Division**

**DATE:** June 7, 2013



**Signed Copy Located in the NCGA Principal Clerk's Offices**