NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: H.B. 1509 Third Edition

SHORT TITLE: Revenue Administrative Changes

SPONSOR(S): Rep. Holliman

FISCAL IMPACT

Yes (X) **No ( )** **No Estimate Available ( )**

	FY 2002-03	FY 2003-04	FY 2004-05	FY 2005-06	FY 2006-07
REVENUES					
General Fund	Potential Revenue Change – See Assumptions and Methodology				
Local Government	**(Minimum $200,000 annually – see assumptions)**				

PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED: North Carolina Department of Revenue, Universities and affiliated institutions, and local governments..

EFFECTIVE DATE: Sections 2 and 3 (quarterly sales tax returns) become effective October 1, 2002, and applies to taxes levied on or after that date. The remainder of the act becomes effective when law.

BILL SUMMARY: This proposal includes several changes recommended by the North Carolina Department of Revenue. Section 1 clarifies that equipment used to dispense plant growth inhibitors is not exempt from sales tax. Section 2 changes the due date for quarterly sales tax returns from the 15th of the month to the last day of the month, following the end of the quarter. Section 3 changes the underpayment penalty calculation for semimonthly taxpayers to conform to the Streamlined Sales Tax Project. Section 4 clarifies the use of sales and use tax exemption certificates and is recommended by the Revenue Laws Study Committee. Section 5 expands the ownership requirements for a property tax exemption for an educational institution to include ownership by a nonprofit entity that holds the property in trust for the sole benefit of a constituent or affiliated institution of The University of North Carolina.

ASSUMPTIONS AND METHODOLOGY:

Section 1: This proposal is a result of a North Carolina Court of Appeals decision. In American Ripener Co. Inc. v. Muriel K. Offerman, Secretary of Revenue, the court considered the application of state sales taxes to a plant growth regulator or stimulator which controls the ripening of fruits and vegetables (ethylene), as well as the equipment used to deliver that chemical. Tax on replacement parts was also an issue. The court held that all of these items are exempt from sales and use tax under G.S. 105-164.13(2) and G.S. 105-164.13 (2a) which exempts "plant growth inhibitors, regulators, or stimulators for agriculture including systematic and contact or other sucker control agents for tobacco and other crops." The court also ruled that the generators and associate parts are also inhibitors and are therefore exempt from sales tax. The proposal effectively amends G.S. 105-164.13(2a) to make the equipment and parts associated with this gas treatment subject to sales and use taxes. (The Department had previously assumed all these items were taxable.) In making it's ruling, the court effectively reduced sales tax revenue. The bill would restore at least some of that revenue to the General Fund. As such, the bill in and of itself would create <u>a small revenue gain</u>. However, Fiscal Research is unable to create an exact estimate of the value of ethylene delivery parts and equipment. As a result, no estimate is possible on this portion of the proposal.

<u>Section 2:</u> Currently the Department of Revenue receives monthly withholding returns, monthly sales tax returns, and quarterly sales tax returns on the 15th of the month. On the 15th of March, April, September, and October income tax returns are due as well. Shifting the due date of quarterly sales and use tax returns from the 15th of the month to the end of the month will create a more even distribution of work in the Department. Because the payments are due in the month following the end of the quarter (October, February, April, and July), the shift will not move any revenue from one fiscal year to the next. Some loss of interest on the payments or "float" will occur. However, because of the relatively small sums of money involved, the Department <u>expects the loss to be minimal</u>.

<u>Section 3:</u> This section changes the calculation of penalty for underpayment by semimonthly sales tax payers. Under current law, the taxpayer must remit at least 95% of the amount due for each semimonthly payment period. This proposal allows the taxpayer to remit the lesser of this amount or the average semimonthly payment for the prior calendar year. This proposal will clearly result in some loss of penalty revenue. However, no data is available to determine the magnitude of the loss. The Department expects <u>the loss to be slight</u>.

<u>Section 4:</u> The Department of Revenue has historically issued exemption certificates to taxpayers in certain exempted industries to facilitate tax administration. However, there is no reference to exemption certificates in the statutes, except as it relates to penalties for misuse of such a certificate. This proposal would codify the practice of issuing exemption certificates. Since the proposal is only codifying the existing practice of the Department, <u>no fiscal impact is expected</u>.

<u>Section 5:</u> There are 16 constituent institutions of The University of North Carolina. There are also five (5) affiliated institutions – the University Hospitals, Arboretum (Asheville), School of Science and Math (Durham), NC School for the Arts, and WUNC public television station. Should any of these organizations choose to form a nonprofit entity to hold property in trust, that property would now become exempt. As such, the legislation puts these properties held in trust in the same category for local tax purposes as the constituent institutions themselves. To date, only six (6) of the constituent institutions have formed these organizations and acquired property. The institutions, the amount of acreage held, and the value of that property are as follows:

Institution	Acreage of Non-State Land	Exempt	Assoc. Tax Value
Appalachian State University	37.3	*Yes	24,314,800
Fayetteville State University	5.2	Yes	1,617,500
NC School of the Arts	4.3	Yes	6,110,000
NC A&T State University	2.0	Yes	4,610,400
UNC - Pembroke	13.0	Yes	8,315,000
Winston-Salem State University	3.3	Yes	374,500

University General Administration also reports that North Carolina Central University is also in the process of developing this type of non-profit structure.

According to data compiled by UNC General Administration, all but one of the properties listed above have been exempted from taxation by the impacted local government, either through a decision of the assessor or county commission. The property held for Appalachian State University, however, is in dispute. The property has been deemed taxable by the county and the city of Boone, but the university is appealing the ruling. In the case of Winston-Salem State University and North Carolina A&T University, the property is being exempted because it is held by the university's own foundation. It is not clear to the Department of Revenue or Fiscal Research under what statute the remaining properties are exempt.

If the local governments prevail in the Appalachian case, the bill will have the effect of removing the property from the local tax rolls. Using the current property tax rates, local officials estimate annual losses of approximately $200,000 for Watagua County and the Town of Boone, although the university system uses a lower estimate.

In future years the losses could grow substantially if the university system shifts more of its projects to this new structure. As a result, the $200,000 loss noted above is a minimum estimate.

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