NORTH CAROLINA GENERAL ASSEMBLY
LEGISLATIVE FISCAL NOTE

BILL NUMBER: House Bill 1602 (Second Edition)

SHORT TITLE: Delay $ Limit on Credit for Partnerships.

SPONSOR(S): Representative McComas

FISCAL IMPACT

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

	($million)				
	FY 2004-05	**FY 2005-06**	**FY 2006-07**	**FY 2007-08**	**FY 2008-09**
REVENUES					
General Fund		(3.7)*	(3.7)*		

PRINCIPAL DEPARTMENT(S) &
PROGRAM(S) AFFECTED: Department of Revenue; Department of Environment and Natural Resources

EFFECTIVE DATE: This act is effective when it becomes law.

* Revenue loss assuming 20 tax credits each year involving pass-through entities with donation size similar to projects approved from 2001 to 2004. Assumes credit taken on final return with no adjustment in quarterly estimated payments.

BILL SUMMARY: This act delays from 2005 to 2007 the imposition of the dollar amount limitation on pass-through entities for the tax credit on certain real property donations.

BACKGROUND: In 2001, the General Assembly approved HB 146 (S.L. 2001-335) to modify the pass-through distribution of partnership income tax credits to conform to federal law. Prior to 2001, when a tax credit was capped at a specific dollar amount, each owner in a pass-through entity was allowed to take that dollar amount of credit. Under federal law, the total credit amount was shared proportionally with the investors in the pass-through entity based on their share of ownership. HB 146 placed this total credit amount limitation on tax credits for worker training, conservation tillage equipment, poultry composting facility, investment in business property, renewable energy property, and administrative office property, and real property donations. For the tax credit on real property donations, the limitation was delayed until January 1, 2005. For income tax law, a pass-through entity is a limited partnership, a general partnership, a joint venture, a subchapter S corporation, or a limited liability company that is owned by individuals or other entities in which the income, losses, and credits "pass through" the entity to the owner in proportion to ownership share.

ASSUMPTIONS AND METHODOLOGY: Based on the tax credits taken by pass-through entities from 2000 to 2004, this bill will increase the General Fund revenue loss due to the conservation tax credit. Upon the request of the General Assembly's Fiscal Research Division, the Department of Environment and Natural Resources provided a list of all companies that have applied for the conservation credit in the last five years. The companies on the list were matched against incorporation records kept by the Secretary of State to determine how each company was incorporated. The list contained 82 companies that were either limited partnerships or limited liability companies that fit the qualification of pass-through entity.

The chart below shows the conservation donations for 2001 with the company names deleted. The Amount column has the value of the conservation easement, donation, or bargain sale for each property. Since the number of investors for each company is unknown, for this analysis it is assumed that each company has five investors. The number of investors is important because until December 31, 2004, each investor can take the total credit amount. Thus, for Company D, the $3.6 million donation is divided by five investors to give each investor a $720,000 donation. This donation is multiplied by 25% to get an $180,000 tax credit per investor. The total tax credit for Company D under current law is $900,000 or $180,000 credit times five investors. If this same donation were made after January 1, 2005 when the limitation of HB 146 (S.L. 2001-335) takes effect, the maximum credit amount that all five investors would have to share would be $250,000. This would save the General Fund $650,000 on the tax credit for Company D.

Entity	Amount	Donation per Investor (Assume 5 Investors)	25% per credit investor	Total Credit until Dec 31, 2004	Total Credit after Jan 1, 2005
Company A	$1,525,000	$305,000	$76,250	$381,250	$250,000
Company B	$1,939,000	$387,800	$96,950	$484,750	$250,000
Company C	$2,144,537	$428,907	$107,227	$536,134	$250,000
Company D	$3,600,000	$720,000	$180,000	$900,000	$250,000
Company E	$670,000	$134,000	$33,500	$167,500	$167,500
Company F	$330,000	$66,000	$16,500	$82,500	$82,500
Company G	$364,000	$72,800	$18,200	$91,000	$91,000
Company H	$425,000	$85,000	$21,250	$106,250	$106,250
Company I	$92,000	$18,400	$4,600	$23,000	$23,000
Company J	$3,900,000	$780,000	$195,000	$975,000	$250,000
				$3,747,384	$1,720,250

For the ten donations made by pass-through entities in 2001, the state had an estimated revenue loss of $3.7 million. Had the donations been made under the law that takes effect January 1, 2005, the revenue loss would have been $1.7 million for a savings to the state of $2 million. Extension of the dollar amount limitation will negate such savings to the General Fund for two years. Using the same assumption of five investors per company, the chart below shows the cost of the conservation credits for 81 donations from 2001 to 2004. On average, the difference between the tax credit awarded until December 31, 2004 and the credit awarded after January 1, 2005 is $189,309. For 20 donations a year, this would equal a General Fund revenue loss of approximately $3.7 million annually. Assuming no quarterly estimated payments, the 2005 tax year credits will be taken in the spring of 2006 and thus are accounted for in FY 2005-06. The 2006 tax year credits will be taken in FY 2006-07.

	Donations	Total Credit until Dec 31 2004	Total Credit after Jan 1 2005	Difference	Difference per Credit	
2001	10	$3,747,384	$1,720,250	$2,027,134	$202,713	
2002	18	$7,089,550	$3,210,200	$3,879,350	$215,519	
2003	28	$6,550,274	$3,479,274	$3,071,000	$109,679	
2004	25	$10,698,060	$4,827,500	$5,870,560	$234,822	
	81					
				$14,848,044	$183,309	per credit

SOURCES OF DATA: Department of Environment and Natural Resources – N.C. Conservation Tax Credit Program; Department of Secretary of State

TECHNICAL CONSIDERATIONS: None

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