**GENERAL ASSEMBLY OF NORTH CAROLINA**

**Session 2005**

Legislative Fiscal Note

**BILL NUMBER**: House Bill 1004 (Fifth Edition)

**SHORT TITLE**: Extend JDIG and Bill Lee Act.

**SPONSOR(S)**: Representative Gibson

**FISCAL IMPACT ($Mill.)**

| | Yes (x) | No ( ) | No Estimate Available ( ) | | |
|---|---|---|---|---|---|
| | **FY 2005-06** | **FY 2006-07** | **FY 2007-08** | **FY 2008-09** | **FY 2009-10** |
| **REVENUES:** | | | | | |
| **State General Fund** | | | | | |
| **Lee Act Sunset** | | **-1.80** | **-6.70** | **-4.80** | **-4.80** |
| **Devel. Zone Sunset** | **-** | **-.23** | **-.52** | **-.67** | **-.84** |
| **Bill Lee Tier Adj.** | | **Insign.** | **Insign.** | **Insign.** | **Insign.** |
| **Total Bill Lee Act** | | **-2.03** | **-7.22** | **-5.47** | **-5.64** |
| **EXPENDITURES:** | | | | | |
| **State General Fund** | | | | | |
| **JDIG Sunset** | **-** | **-4.50** | **-9.00** | **-9.00** | **-6.00** |
| **POSITIONS (cumulative):** | | | | | |

**PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED:** Department of Revenue and Department of Commerce. The enactment of the bill is not expected to affect the budget requirements of either department.

**EFFECTIVE DATE:** When the bill becomes law.

**BILL SUMMARY**: **Bill Lee Act Sunset Extension.** The Lee Act is the package of state tax incentives that was first adopted in 1996 and has been modified on numerous occasions. The incentives are primarily in the form of tax credits for machinery and equipment, job creation, worker training, central administrative office, and research/development. The credits apply to activities undertaken by specifically named industrial classifications. For many of the credits, the counties of the State are divided into five economic distress tiers based on the unemployment rate, population growth, and per capita income. The lower the tier of a county, the more favorable the incentive.

The bill moves the sunset for most Lee Act credits from January 1, 2006 to January 1, 2008.

**Job Development Investment Grant Sunset Extension.** The 2002 General Assembly established a program whereby companies selected by an Economic Investment Committee of state officials will be provided a grant equal to a certain percentage of the company's income tax withholding payments.

The bill extends the sunset for the JDIG grants from January 1, 2006 to January 1, 2008.

**Development Zone Sunset Extension.** The 1998 General Assembly modified the Lee Act by authorizing development zones (DZ's). Development zones are areas of higher poverty within urban centers, as identified by the Department of Commerce. For a company locating in a DZ, the credits for machinery/equipment investment, jobs created, and worker training are the same as for Tier 1 counties (most distressed counties) regardless of the tier of the county of location. This enhances the value of the Lee Act credits affected.

The bill extends the sunset for certain projects located in development zones from January 1, 2006 to January 1, 2010. To be eligible for the extension: (1) the taxpayer must enter into a letter of commitment with Department of Commerce by January 1, 2006 describing the project; (2) the Department of Commerce must certify that over a three-year period the taxpayer is expected to place in service at least $10 million of real property and machinery and equipment in a DZ and create at least 300 jobs; and (3) the taxpayer must place in service at least $4 million of property and create at least 20 new jobs at the location.

**Bill Lee Act Tiers Adjustment.** Under the Lee Act, the counties are divided into five "enterprise tiers" based on a ranking of the counties on three factors: per capita income, population growth, and the unemployment rates. The rankings on the individual measures are combined to come up with an overall rank for each county.

The bill makes the following changes to the tier designation: (1) any of the 10 counties with the highest unemployment rates for the preceding 12 months is automatically put in Tier 1 (most distressed counties), regardless of the designation using the existing ranking system; (2) a county with a population of under 12,000 is designated as Tier 1 regardless of the poverty level in the county (now such a county must have a poverty rate of more than 16%).

**Health Insurance Eligibility Requirement.** Under current law a company must provide a specified amount of health insurance for all employees to be eligible for a JDIG grant. The bill removes certain high-income employees from the health insurance coverage requirement.

**Economic Development Oversight Committee**. Creates a legislative oversight committee on economic development. The committee would consist of six members appointed by the Speaker of the House and the same number by the President Pro Tempore of the Senate. The committee must complete a comprehensive analysis of the Bill Lee Act and the JDIG program and report its findings prior to the convening of the 2006 legislative session. In addition, the bill states the intent of the General Assembly for the 2006 session to replace the Bill Lee Act and to revamp JDIG based on the recommendations of the study committee.

**ASSUMPTIONS AND METHODOLOGY**: **Bill Lee Act Sunset Extension.** When the original Lee Act was adopted in 1996, a comprehensive model was used to estimate the impact of each of the credits over time. The model started with the announced investment and job creation levels and made adjustments to the raw data for eligibility considerations and other factors. Next the potential annual impact was adjusted down to assumed utilization levels based on the limitation of most credits to 50% of annual tax liability.

A review of the annual report data on Bill Lee Act utilization indicates that the amount of credits taken during the first 5 years of the Lee Act is roughly in line with the expectations used in the original 1996 fiscal note. The data support the observation of the Department of Revenue that much of the credit capacity in not used in early years due to the 50% limit. This means that much of the credits for job creation and machinery/equipment investment in 2006 and 2007, the sunset extension years, will be taken in years following the first year of eligibility.

Another timing consideration is that the jobs credit must be taken over four years, beginning in the year following the year the job is created. The machinery and equipment credit is taken over seven years, beginning in the year following the year the job is created. Thus, the impact of the two year extension for these credits will occur over many years. The estimates for these credits use the experience for the 1996-2003 period in terms of tax credits generated versus credits used. The projections used in this part of the fiscal note are cautious due to the lack of specific company-by-company data on the amount of credits taken by year under the 50% limitation.

The worker training tax credit is taken in the year in which the training is done. Thus, there will be a 2006-07 impact from this credit. The assumed credit usage level corresponds to the actual experience for the 1996-2003 period. The estimated 2006-07 amount is grown by 5% to get to the 2007-08 amount. This growth rate is tied to the estimate of state personal income growth used for state budget purposes.

**Job Development Investment Grant Sunset Extension.** The grants are limited to $15 million per calendar year. Thus, the maximum impact of the one-year sunset extension would be $15 million. However, an analysis of the cash flow of the grants awarded during the 2003 and 2004 calendar years indicates that for many projects there is a substantial lag time between the approval of a grant agreement with the Economic Investment Committee and the grant payout. In addition, there have been no JDIG grant agreements so far during the 2005 calendar year. Based on this information, the fiscal memo assumes that while 100% of the annual grant agreement limit will be used in 2006 and 2007, the payout of the $15 million of grants each year will take place over 4 years according to the following schedule: 30% for Year 1, 30% for Year 2, 30% for Year 3, and the remaining 10% in Year 4.

**Development Zone Sunset Extension.** Discussions with the Department of Commerce and a review of news articles indicated that there are two major projects that could be affected by this change. For these projects, the amount of machinery and equipment investment, jobs created, and workers trained were simulated, based on the news articles and discussions with Commerce. The primary impact of the development zone designation is the $4,000 increase in the credit for jobs created. This credit is taken over 4 years, beginning with the year following the job creation. Other impacts include an additional $500 of worker training tax credit per job, with the credit taken in the year of the training. Finally, the change would affect the threshold for the machinery and equipment credit. This credit is over 7 years, beginning in the year following the investment.

**Bill Lee Act Tiers Adjustment.** The practical effect of this provision is to allow companies locating in a handful of counties to receive enhanced credits for investing in machinery and equipment, creating jobs, and providing worker training. Based on a review of the county unemployment rate data for the most recent 12 months, five counties would move into Tier 1 from other tiers. A review of "announcements" data (investment, jobs) provided by the Department of Commerce for a couple of recent years indicates that the share of new activity from the four counties is only .8% of the statewide amount of new jobs and investment. Thus, the impact of this change, based on prior years' experience, is minimal.

The same conclusion would apply to the small county eligibility change as only two counties would be affected and their new economic activity levels are relatively small.

**Health Insurance Eligibility Requirement.** A discussion with the Department of Commerce indicated that this issue has affected very few applicants for JDIG grants and that the vague language under the current law could mean that affected companies would have still received the grants.

**Economic Development Oversight Committee.** There is no funding provided under the bill. Presumably the financing would come from the normal appropriations to the General Assembly in the same fashion as other independent study commissions.

**SOURCES OF DATA:**

**TECHNICAL CONSIDERATIONS**: None

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