



Finance Committee FY 2012-13 Highlights

Fiscal Brief

October 2012

The North Carolina General Assembly House and Senate Finance Committees address changes to state tax law. This fiscal brief highlights the tax law changes enacted during the 2012 Session.

Actual and Projected General Fund Tax and Non-Tax Revenue Sources since FY 2009-10, (\$ In Millions)

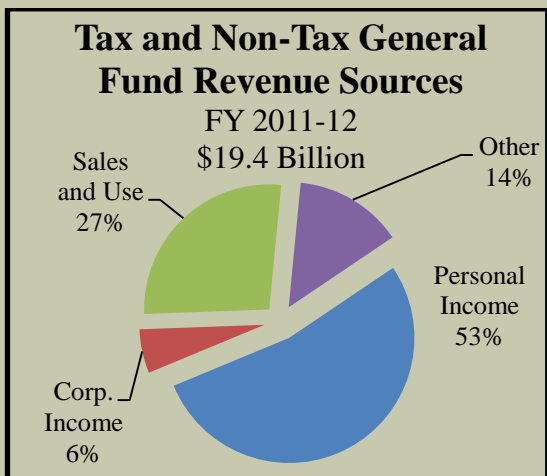
	<u>Actual FY 2009-10</u>	<u>Actual FY 2010-11</u>	<u>Actual FY 2011-12</u>	<u>Projected FY 2012-13</u>
Personal Income	9,048	9,735	10,272	10,520
Sales and Use	5,565	5,873	5,258	5,459
Corporate Income	1,198	1,014	1,133	1,075
Other¹	2,700	2,472	2,577	2,651
Total	\$18,511	\$19,094	\$19,239	\$19,705

¹"Other" includes other taxes and non-tax revenue sources

Revenue Outlook and Finance Overview

The revised consensus revenue estimate continues to maintain a cautious approach to the State's fiscal outlook, while slightly increasing forecasted collections. The North Carolina economy appears to be returning to the pre-recession employment and population growth levels seen in 2007.

Final collections exceeded the original FY 2011-12 forecasts by two percent. The increase stemmed from modest growth in employment and personal income.



S.L. 2012-142, Modify 2011 Appropriations Act (H.B. 950), as amended by S.L. 2012-145, Modifications/2012 Appropriations Act (S.B. 187), reduced FY 2012-13 expenditures by \$5.75 million. This \$5.75 million reduction in General Fund Availability allowed the General Assembly to enact S.B. a \$2.6 million reduction in personal income tax collections and a \$3.15 million reduction in sales and use tax collections for FY 2012-13. The \$5.75 million reduction in General Fund availability during the 2012-13 fiscal year can be attributed to three tax credits/economic development incentives: 1) the Work Opportunity Tax Credit Extension (included in S.L. 2012-36, H.B. 1025), 2) the Tax Deduction for Education Supplies (included in S.L. 2012-74, H.B. 1015), and 3) the Sales Tax Refund Application for Passenger Air Carriers (included in S.L. 2012-74, H.B. 1015).

This Fiscal Brief provides an overview of the three tax law changes alongside summaries of other legislation enacted by the 2012 House and Senate Finance Committees. The major decisions of the House and Senate Finance Committees were enacted through five pieces of legislation:

- S.L. 2012-36 (H.B. 1025) Extend Tax Provisions,



- S.L. 2012-43 (S.B. 824) Expedited Rule Making and Forced Combinations,
 - S.L. 2012-74 (H.B. 1015) Economic Development and Finance Changes,
 - S.L. 2012-79 (S.B. 826) Revenue Laws Technical, Clarifying, and Administrative Changes, and
 - S.L. 2012-194 (S.B. 847), GSC Technical Corrections and Other Changes.
- Adoption expenses (G.S. 105-151.32(c)).
- The legislation extended the following income tax credits through January 1, 2015:
 - Credits for rehabilitating historic mill structures (G.S. 105-129.39) and
 - Credits for rehabilitating historic mill property (G.S. 105-129.75).

These five bills extended several income and sales tax economic development incentives and created certainty in the tax code.

Extending Economic Development Incentives

Income Tax Provisions

S.L. 2012-36 (H.B. 1025), Extend Tax Provisions, extended the sunset on several economic development tax credits through January 1, 2014. North Carolina typically imposes a sunset on its tax credits and deductions, allowing these incentives to be reviewed for effectiveness. The 2012 General Assembly anticipates tax reform as a major task of the 2013 session. S.L. 2012-36 maintains the current state of the North Carolina tax code by extending several tax credits until comprehensive tax modernization is considered. The legislation provides preferential income tax treatment for several groups, business activities, and expenses:

- The tier 1 designation for seafood industrial parks was extended through July 1, 2013 (modifies Section 2 of S.L. 2009-505),
- The following corporate and personal income tax credits were extended through January 1, 2014:
 - Renewable fuel facilities (G.S. 105-129.16D(d)),
 - Biodiesel producers (G.S.105-129.16F(b)),
 - The work opportunity tax credit (G.S.105-129.16G(b)),
 - Companies qualifying for the Article 3J tax credits (G.S.105-129.16F(b)),
 - The recycling of oyster shells (G.S. 105-130.48(f) and G.S. 105-151.30(f))
 - Premiums paid for long-term care insurance (G.S. 105-151.28(d)),
 - The refundable earned income tax credit (G.S. 105-151.31(c)),
 - Investments in qualified business ventures (G.S. 105-163.015), and

S.L. 2012-36 (H.B. 1025) extended the NC Film Income Tax Credit through January 1, 2014. A later session law, S.L. 2012-194 (S.B. 847), added an additional tax year of eligibility for the credit. S.L. 2012-194 (S.B. 847), GSC Technical Corrections and Other Changes, Sec. 79.10 (a) and (b) extends eligibility for the personal and corporate income tax film credit through January 1, 2015. This change has no fiscal impact during the biennium, but does reduce General Fund availability by \$60.0 million in FY 2014-15.

Section 2 of S.L. 2012-74 (H.B. 1015), Economic Development and Finance Changes, creates an individual income tax deduction for educator expenses to ensure that North Carolina educators continue to receive the same tax benefit received since 2002, regardless of whether Congress extends the federal educator expense deduction. The deduction will reduce General Fund revenue by \$1.8 million for FY 2012-13. The legislation amends G.S. 105-134.6(d).

Section 5 of S.L. 2012-74 (H.B. 1015), Economic Development and Finance Changes, temporarily allows a 20-year carryforward period under Article 3J for a taxpayer who makes an investment of \$100 million in a tier one county. The change may decrease General Fund revenues by \$2.7 million over the 20-year lifetime of the credit, but the timing of the fiscal impact is unknown. The temporary change is effective for taxable years beginning on or after January 1, 2012, and expires for taxable years beginning on or after January 1, 2013.

Sales Tax Provisions

S.L. 2012-36 (H.B. 1025) modified four sales tax economic development incentives. The legislation extended the sales tax refunds for the following industries and/or qualified purchases found in G.S. 105-164.14A(a) and G.S. 105-164.14B(f) through January 1, 2014:

- Passenger air carriers,



- Machinery and equipment placed in a tier one county,
- Aviation fuel of motorsports team or sanctioning body,
- Analytical business services, and
- Certain industrial facilities.

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Section 3 of S.L. 2012-74 (H.B. 1015), Economic Development and Finance Changes, clarifies and extends the time to apply for a sales tax refund of aviation fuel for FY 2010-11 and FY 2011-12. The refund will reduce General Fund revenues by \$3.15 million for FY 2012-13 and it will reduce local government revenues by \$2.72 million. The provision became effective June 26, 2012.

Creating Certainty in the Tax Code

S.L. 2011-390 (H.B. 619) established new procedures for the Secretary of Revenue to follow when he believes that separate entity returns of affiliated corporations should be combined into one tax return. S.L. 2012-43 (S.B. 824) supplemented this legislation by creating an expedited rule-making process for the Department of Revenue regarding the determination of whether affiliated corporations are required to file combined tax returns. S.L. 2012-43 has been highlighted in State Tax Notes, a multi-state tax news source produced by the media group, Tax Analysts (65 State Tax Notes 149 (July 16, 2012): "Transparency in North Carolina: Portrait of a State in Flux.")

Fiscal Impact of Tax Law Changes

Table 1 of the Appendix summarizes the four year fiscal impact of the tax law changes made during the 2012 session of the North Carolina General Assembly. The information summarizes the expected General Fund impact of extending several economic development tax incentives alongside other income and sales tax changes.

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APPENDIX

Table 1. Four-Year Fiscal Impact of Tax Law Changes Occurring During the 2012 Session (\$ In Millions)

	<u>FY 2012-13</u>	<u>FY 2013-14</u>	<u>FY 2014-15</u>	<u>FY 2015-16</u>
Extending Economic Development				
Tax Incentives	-0.8	-135.8	-46.7	-14.3
<i>Other Income Tax Changes</i>				
Educator Expenses Deduction	-1.8	-1.8	-1.8	-1.8
Extend Film Credit			-60.0	
<i>Other Sales Tax Changes</i>				
Clarify Sales Tax Refund	-3.15			
Refund for Machinery Used at a Port Facility		-0.1		
TOTAL	-\$5.75	-\$137.7	-\$108.5	-\$16.1