NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: SB 1115 (Finance Committee Substitute Adopted 5/20/99) William S. Lee Act/1999

SHORT TITLE: William S. Lee Act/1999

FISCAL IMPACT ($Mill.)

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

	FY 1999-00	**FY 2000-01**	**FY 2001-02**	**FY 2002-03**	**FY 2003-04**
REVENUES					
State General Fund	-1.6	-2.1	-7.3	-23.5	-32.4
Local Government	-.8	-.9	-.9	-1.0	-1.1

PRINCIPAL DEPARTMENTS AFFECTED: Commerce; Revenue; Natural and Economic Resources

EFFECTIVE DATE: See "Bill Summary"

BILL SUMMARY:

Bill Lee Act* Changes:

1. Extend sunset on Act from 2002 to 2007.
2. Extend Act credits to customer service centers in Tiers 1 and 2, effective 1/1/00.
3. Allow annual refund of 6% sales taxes paid on capitalized machinery and equipment sold to businesses eligible for Bill Lee Act credits and located in Tier 1 or 2, effective 1/1/00.
4. Give a more favorable tier designation to small counties, effective 1/1/00.
5. Close loopholes in definition of development zones, effective 7/1/99.
6. Allow a 25% credit for contributions to nonprofits for capital projects within development zones, effective 1/1/00.

7. Allow credits to be taken against insurance premiums tax (in addition to corporate income and franchise tax), effective 1/1/99.

8. Require businesses to provide a portion of health insurance costs and meet environmental, safety, and health standards in order to qualify for credits, effective 1/1/00.

9. Eliminate the $75 application fee for credits in Tiers 1 and 2 and increase the fee to $500 per credit in other tiers, with a cap of $1,500 per applicant, effective 30 days after the bill becomes law.

10. Require applicants for credits to provide additional information to enable Commerce to evaluate the effectiveness of the credits in providing employment to residents of development zones, effective 7/1/99.

11. Clarify definitions of industries covered by Bill Lee Act, effective immediately and clarify sales tax refunds for sales of fuel to interstate air carriers.

Air Carrier Incentives (New):

1. Add passenger air carrier training center to credit for central administrative office, effective 1/1/99.

2. Allow an interstate passenger air carrier a sales tax exemption for aircraft parts and accessories purchased for use at its hub in this State, effective 5/1/99.

3. Reduce sales tax from 6% to 1% with an $80 cap for flight crew training aircraft simulators purchased by an interstate passenger air carrier for use at its hub in this State, effective 5/1/99.

Other Changes:

1. Allow a credit for rehabilitating or constructing affordable housing, effective 1/1/00.

2. Require projects to obtain an environmental certification in order to qualify for funding from the Industrial Development Fund (Building Renovation Fund), effective 7/1/99.

3. Allow a five-year sales tax refund to certain nonprofit insurance companies for taxes paid on building materials, effective 1/1/00.

*****The package of state tax credits first adopted in 1996 to attract new companies to North Carolina. Examples include an investment tax for machinery and equipment, a jobs credit, a research and development credit, and a worker training credit.

ASSUMPTIONS AND METHODOLOGY:

<u>Bill Lee Act Changes</u>:

<u>Sunset Extension</u>

A recent analysis of the impact of the Bill Lee Act on income tax returns for 1997 tax year indicated that the fiscal note estimates used during the 1996 session were reasonably close to the actual usage of the credits. Thus, the cost of extending the credits was based on a reconstruction of the 1996 model. This model used actual historical data on announcements of capital investment and jobs, as compiled by the Department of Commerce. In addition, the 1996 model contained assumptions about the usage pattern of the credits during the phase-up period.

The primary adjustment on this year's analysis was to assume that capital investment would continue to grow at 6% per year. This rate is similar to the state personal income growth assumption contained in the General Fund Budget Planning Model. Other credits were grown at the same annual rate.

The result of this analysis is that the cost of the tax credits will continue to rise over time, instead of the current law projection of a plateauing and then decline of the cost as the economic activity is no longer eligible for the credit and credit carry forwards are used up.

<u>Development Zone Loophole Closing</u>

This estimate by the Community Assistance Division of the Department of Commerce used the Geographic Information System (GIS) to look at census tract data.

<u>Investment Tax Credit for Nonprofits</u>

There is no data from other states or any source to assist in estimating the actual usage of the 25% credit for contributions or investments in certain nonprofit organizations located in a development zone. To be conservative, it was assumed that the maximum allowable credit limit of $4 million would be used. This usage was phased in over a two-year period.

<u>Credit Application Fees</u>

The Finance Division of the Department of Commerce provided 1997 calendar year data on applications by type of credit. The tabulation indicates that there were 1,181 credits for 674 companies, with over 80% of the activity in the investment tax credit and jobs credit areas. The estimated $500,000 of additional receipts would be earmarked for the Department of Revenue (75%) and Department of Commerce (25%) to offset costs incurred in administering the Act.

<u>Enhanced Tier 1 and 2 Incentives</u>

The analysis of the cost of the extension of the Bill Lee Act to customer call centers is based on a simulation that assumes each year one new company will locate in each tier. The assumed investment for each facility is $2 million and the new jobs amount is 200.

The cost of the sales tax refund is based on a simulation by the Department of Commerce, based on Tier 1 and 2 investment announcement data. In general, the purchase of machinery and equipment is assumed to be equal to 70% of the announced cost of investments.

Air Carrier Incentives:

Preferential Sales Tax on Training Equipment

This analysis assumed the purchase of $10 million of flight simulation equipment per year. For analysis purposes, it was assumed that all of the new purchases would cap out at the $80 limit under the bill. Thus, the tax that would be paid on the purchases under current law is equal to the revenue loss for the proposal.

Sales Tax Exemptions for Repair Parts, Lubricants

This analysis was based on an assumption of $30 million per year of taxable purchases.

Other Changes:

Affordable Housing Tax Credit

The estimate of the cost of the credit for rehabilitating or constructing affordable housing was made by the Community Assistance Division of the Department of Commerce. The credit is equal to 25% of the federal credit. The key assumptions are that 75% of the federal eligible buildings are put into service in the year after federal allocation of federal tax to each state and that North Carolina taxpayers will represent 40% of federal investors in North Carolina. Over time, the latter ratio is assumed to rise to 60%.

Nonprofit Insurance Company Sales Tax Refund

The estimate for the refund of the sales tax on building materials was based on an assumption of a $100 million office building construction over a three-year period with 50% of the cost taking place in the 2001 calendar year and 25% in years 2000 and 2002. The next step was to use the usual assumption of 50% of the construction cost ($50 million) for materials (versus labor charges). Finally, the legislation provides that the refund is received the year after the tax is paid.

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