Civitas Institute
Legislative Recap
2007 General Assembly

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Fee Increases and Tax Changes

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One of the main sticking points during this year's contentious and drawn out budget process was the debate over whether the "temporary" sales and income tax rates should be allowed to expire. In the end, the top income rate was allowed to return to 7.75 percent, while the remaining ¼ cent "temporary" sales tax rate was made permanent.

While the sunset of the "temporary" income tax rate on December 31, 2007, will put $40.8 million into the hands of North Carolina taxpayers for FY2007-08, making the "temporary" sales tax rate permanent equates to a tax increase of $258 million. Add to this roughly $64 million in fee increases, and it is easy to see that the cost of living for North Carolinians will go up significantly.

New Fees in the FY2007-08 Budget

Even though mandatory fees are not directly paid by all citizens, the higher costs they impose on businesses are typically passed along to consumers – which is why many economists refer to such fees as "hidden taxes." Most of these fees will impose higher costs on basic services. For example, the "certificate of need" and Health Care Facility Construction Project fee increases will make it more expensive to build new hospitals, nursing homes and adult care facilities – thus driving up healthcare costs for the elderly, retirees, and other vulnerable populations. Still worse, is an insurance regulatory fee that will drive up insurance costs by $24 million – thus making it more difficult for hardworking families to purchase private insurance.

The total price tag for these newly approved fee increases comes to roughly $64 million for FY2007-08. The new fees include:

- An increase in a wide variety of judicial fees. Estimated cost: $35.6 million. (More details on these fee increases can be found in the JPS legislative recap.)
- A new insurance regulatory fee of 5.5 percent of total tax liability on all insurance companies. The money from this fee will be used to finance the creation of an Insurance Regulatory Fund. Based on taxes paid by insurance companies in FY2005-06, this fee effectively amounts to a $24 million tax increase on insurance customers in North Carolina.
- An increase in permit and renewal fees imposed on landfills, as mandated in S1492. Estimated cost: $1.1 million.
- An increase of 20 percent in the water quality fee assessed on water treatment facilities. Estimated cost: $997,945.
- Fees will more than double on "certificate of need" applications. Such applications are used to request permission from the state to construct an institutional health service facility. Estimated cost: $852,687.
- Significant increases in the Health Care Facility Construction Project Fee. Estimated cost: $789,720. This mandatory fee is used to pay HHS expenses related to the review and approval of project plans and construction.
- An increase of 25 percent for the Secretary of State Corporate Annual Report Fee. Estimated cost: $563,016. This is a fee imposed when corporations file their annual reports. An increase in this fee further increases the cost of doing business in North Carolina.
- An increase in the Sediment and Erosion Control Plan Fee from $50 to $65 per acre of "disturbed land." Estimated cost: $472,500.
- An increase in mining permit fees. Estimated cost: $286,088.

PROPOSED TAX CHANGES

Local Option Taxes

With the inclusion of the "Medicaid swap" in the approved budget, counties are now authorized to levy a vote of their citizens on two potential local option taxes. Voters will decide on an increase of ¼ cent in the local sales tax, or a tripling of the land transfer tax from 0.2 percent to 0.6 percent.

Several counties had already requested authority for a vote to increase any of a variety of local taxes, including the sales tax and the land transfer tax. With the passage of the budget, many of these bills will now become moot. All told, nearly 50 bills were submitted in the House and Senate requesting local authority to raise taxes (subject to voter approval).

- The most common request was for a local sales tax increase. Eighteen counties were represented in a total of 22 bills.
- Nine counties and one city submitted a total of 12 bills requesting authority to increase the occupancy tax.
- Eight counties were represented in a total of 10 bills requesting authority to impose a land transfer tax.
- Two bills in the House and two in the Senate were introduced that would have authorized all counties to hold a vote on either a land transfer tax of 1 percent or an increase in the local sales tax. Another bill, HB 153, offered up a menu of local tax increases that counties could choose from: including the sales tax, land transfer tax, occupancy tax, income tax, impact tax and meals tax.

TAX BILL THAT PASSED

Solid Waste Landfill Bill (S1492)

Status: Presented to Governor Easley to sign on August 3, 2007.
Sponsor: Daniel Clodfelter (D-Mecklenburg) Charles W. Albertson (D-Duplin)
Cost: Expected to generate $25 million in tax revenues in fiscal year 2008-09, as well as new annual revenues from permit fees of $1.1 million.

Drastically increases the state's regulatory power over new landfill construction, including: permitting, compliance, and siting standards. Existing landfills will also have to pay additional taxes and fees ($2 per ton), which will be redirected to municipal recycling programs and cleanup of abandoned landfills around the state. Counties or concerns wishing to construct new landfills will face byzantine regulations and high barriers to entry, including environmental impact studies.

Any individual, business or group that produces waste will have to pay new costs associated with SB 1492. Direct costs will come via the $2 per ton tax on dumping, as well as new permit fees. Indirect costs will come from compliance, as well as transportation costs associated with increased exporting of waste to other states where regulations are less burdensome. Counties – such as those in eastern North Carolina – that might have benefited from new waste management industries will be far less likely to, as industries will probably build fewer landfills in the state.

OTHER TAX BILLS THAT DID NOT PASS

Modernize Corporate Income Tax Filing (HB 462)

Status: Referred to Committee on Finance; this bill is still alive for the 2008 short session
Sponsor: Paul Luebke (D-Durham)
Cost: No fiscal note, this bill would impose additional tax burdens on corporate subsidiaries operating in North Carolina

This bill applies to multi-state corporations and attempts to ensure that profits attributable to North Carolina are taxed at the full amount. Under current North Carolina law, corporations can establish "passive investment corporations" (PICs) in states that do not tax royalties, interest or other forms of intangible income. These PICs can then charge a royalty to the other subsidiaries of the multi-state corporation for use of a trademark or patent. The royalty is a deductible expense for the corporation paying it, reducing the taxable profit a corporation has in other states in which it does business. Under the "combined reporting" proposed in this bill, the parent company and most of its subsidiaries would be treated as one corporation for state income tax purposes. Nationwide profits would be "combined" into one lump sum and then North Carolina's state tax collected as a share of that total would be based on a formula derived from the corporation's level of activity in the state. See also SB 244

Repeal Estate and Gift Taxes, Expand Sales Tax to Include Services (HB 1564)

Status: Referred to the Committee on Rules, Calendar, and Operations of the House
Sponsors: Becky Carney (D-Mecklenburg); Jeff Barnhart (R-Cabarrus)
Cost: No fiscal note, bill calls for "revenue neutrality"

This bill would have offset the lost revenue from repealing the gift and estate taxes by expanding the sales tax to include services.

Sales Tax Exemption for Baked Goods (HB 2001/SB 281)
Status: Referred to the Finance Committee
Sponsors: Rep. Trudi Walend (R-Henderson); Sen. Bob Atwater (D-Chatham)
Cost: No fiscal note

Non-prepared food items, primarily groceries, are exempt from the state portion of the sales tax (soda and candy, however, are taxed by the state). Such food items are only taxed at the local option sales tax rate. This bill would have exempted baked goods "sold without eating utensils provided by the seller" from the state sales tax. Such items would primarily consist of bakery products such as muffins, rolls and donuts.

Repeal Estate and Gift Taxes (SB 104)
Status: Referred to the Finance Committee
Sponsor: Edwin Goodall (R-Mecklenburg)
Cost: No fiscal note.

This bill would have repealed the estate tax on decedents dying on or after July 1, 2007; and on gifts on or after January 1, 2008.

Reduce Tax/Cut Government Spending (SB 1012)
Status: Referred to the Finance Committee
Sponsor: Robert Pittinger (R-Mecklenburg)
Cost: No fiscal note, overall impact most likely positive.

This legislation would have reduced the corporate tax rate from 6.9 percent to 5.9 percent this year and down to 4.9 percent in 2008. The bill also would have reduced the personal income tax by 1/2 percentage point for each tax bracket. In addition, the bill would have reduced spending on nongovernmental organizations and eliminated some vacant positions in state departments. Finally, the bill instructs the Department of Health and Human Services to reduce Medicaid fraud by 5 percent.

Adjust Individual Income Tax Brackets (SB 778)
Status: Referred to the Finance Committee
Sponsor: Edward Goodall (R-Mecklenburg)
Cost: No fiscal note, overall impact most likely positive.

Would have reduced the number of tax brackets from four to three while adjusting upward the income threshold for each bracket, with the result that many taxpayers would pay a lower rate. The highest rate would become 7.75 percent on married taxpayers filing jointly, earning $144,000 and up. (With the expiration of the "temporary" income tax rate, the highest rate will become 7.75 percent, effective Jan. 1, 2008.)

Earned Income Tax Credit (EITC) (SB 955)
Status: Referred to the Finance Committee
Sponsor: Daniel Clodfelter (D-Mecklenburg)
Cost: $134 million

Would have set a state-level, refundable EITC at 10 percent of the federal credit. The final budget included the creation of a refundable state EITC valued at 3.5 percent of the federal credit.

Repeal Incentives – Lower Corporate Tax Rate (SB 1112)
Status: Referred to the Finance Committee
Sponsor: Robert Pittinger (R-Mecklenburg)
Cost: No fiscal note, overall impact likely positive

This legislation would have eliminated a total of 22 corporate tax breaks and used the savings to cut the corporate income tax rate to 2 percent. Also aimed to increase from 5/69 to 1/4 the proportion of corporate tax funds credited to the Public School Building Capital Fund.

Senior Homestead Tax Relief (HB 1917)
Status: Referred to Finance Committee
Sponsors: Annie Mobley (D-Hertford); Earl Jones (D-Guilford); Alice Bordsen (D-Alamance); Jean Farmer-Butterfield (D-Wilson)
Cost: No fiscal note

This bill would have frozen the appraisal value on permanent residencies owned by North Carolina seniors above the age of 70 who have occupied the residence for five years or more. The bill stipulated that property would be subject to reappraisal if there is a physical change or improvement in the land.

Property Tax and PUV Changes and Studies (HB 1499)
Status: Presented to Governor Easley on August 2, 2007
Sponsors: Grier Martin (D-Wake); Hugh Holliman (D-Davidson); Ray Warren (D-Alexander); R. Van Braxton (D-Greene)
Cost: No fiscal note

HB 1499 would have increased the property tax homestead exemption for seniors to become the greater of 50 percent of the appraised value or $25,000 (up from $20,000). Would also modify the present-use-value requirements for agricultural land use as an aquatic species farm. Bill would have authorized a study to "address the inability of landowners to pay escalating property taxes while maintaining nondevelopmental uses."

Three-Fifths Vote to Levy Taxes (HB 146)
Status: Referred to the Committee on Rules, Calendar, and Operations of the House
Sponsor: John Blust (R-Guilford)
Cost: No fiscal note, likely a positive impact for taxpayers

Currently, only a simple majority is required to approve a tax increase.

Tax Fairness in Education (HB 421)
Status: Referred to the Committee on Education
Sponsors: Paul Stam (R-Wake); Daniel McComas (R-New Hanover)
Cost: No fiscal note

This bill would have provided a tax credit to parents of dependent children who are "educated lawfully in grades K-12 other than in a public school." The tax credit amounts to $1,250 per semester (a semester is defined as six months) and applies to married couples with North Carolina taxable income of less than $100,000.

Taxpayers' Protection Act (HB 1543/SB 14)
Status: Referred to Committee on Rules, Calendar, and Operations in House; Committee on Ways and Means in Senate
Sponsors: Nelson Dollar (R-Wake); Wil Neuman (R-Gaston); Mitch Gillespie (R-McDowell); Dale Folwell (R-Forsyth); in Senate: Fred Smith (R-Johnston)
Cost: No fiscal note, impact likely positive for taxpayers

This legislation would have established a cap on the growth of state spending to be equal to the rate of inflation plus population growth in North Carolina for the prior calendar year. Revenues collected in excess of the spending limit would be treated as follows:

- Transferred to the Emergency Reserve Fund. This fund should equal 3 percent of the current year's spending limit.
- Any other remaining revenue would be transferred to the Budget Stabilization Fund. The goal is for this fund to amount to 18 percent of the previous year's spending limit.
- Above and beyond these transfers, any remaining revenue would be refunded to taxpayers in the form of tax rebates or temporary rate reductions.

Any increase in the fiscal year spending limit would be subject to the approval of 3/5 of the General Assembly.

Taxpayer Bill of Rights (HB 1773)
Status: Referred to Committee on Rules, Calendar and Operations of the House
Sponsors: John Blust (R-Guilford); Bryan Holloway (R-Stokes)
Cost: No fiscal note, impact likely positive for taxpayers.

This bill is very similar to the Taxpayers' Protection Act (TPA), with a few notable exceptions:

- Spending growth would be limited to a three-year rolling average of the rate of inflation plus population growth for North Carolina.
- Revenues in excess of the spending limit would go to an Emergency Reserve Trust Fund, with the maximum value of the fund set at 5 percent of General Fund Appropriations from the previous fiscal year. No excess revenues would go to the Budget Stabilization Fund.
- Any remaining reserves would be refunded to taxpayers in a manner similar to the TPA.
- Any increase in the fiscal year spending limit would be subject to 2/3 approval by the General Assembly.