

**NORTH CAROLINA GENERAL ASSEMBLY**

**LEGISLATIVE FISCAL NOTE**

**BILL NUMBER:** HB 14 (House Finance Committee Sub.)

**SHORT TITLE:** Update Custom Computer Software

**SPONSOR(S):** Rep. Lanier Cansler

**FISCAL IMPACT**

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

	<u><b>FY 1997-98</b></u>	<u><b>FY 1998-99</b></u>	<u><b>FY 1999-00</b></u>	<u><b>FY 2000-01</b></u>	<u><b>FY 2001-02</b></u>
<b>REVENUES</b>					
General Fund	\$512,000	\$738,000	\$799,000	\$865,000	\$935,000
Local Govts.	\$256,000	\$369,000	\$400,000	\$432,000	\$468,000

**PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED:** Department of Revenue; Local Governments

**EFFECTIVE DATE:** October 1, 1997

**BILL SUMMARY:** The act redefines custom computer software for sales tax purposes as software written according to the specifications of a specific customer. Custom software is not “prewritten software that can be installed and executed with no changes to the software’s source code other than changes made to configure hardware or software or to select personal preferences”.

**ASSUMPTIONS AND METHODOLOGY:** The Department of Revenue has no data on canned versus custom software, because it collects sales tax data by type of business and not by type of commodity. The Software Publishers Association reported retail software sales of \$10.6 billion in the US and Canada in 1996. If North Carolina’s share of the software sales equals its population share of the US and Canada (2.5%), then North Carolina retail software sales in 1996 were \$265 million. The Software Publishers Association reported software sales for 1995 and 1996 grew 8.2% each year. This inflation rate is used in this fiscal note for the next five years.

The Tax Research Division in the Department of Revenue believes the state is losing sales tax on 3% to 8% of retail software sales because of the ambiguous custom software language now in the statutes. In other words, by clarifying the definition of custom software in HB 14, the

Department of Revenue projects the annual revenue gain to the state and local governments will equal the sales tax on 3% to 8% of software sales. To simplify the estimation of the revenue gain, this fiscal note uses 5.5% or the midpoint of the Department of Revenue's estimate.

	(\$ Millions)						
	<u>FY 95-96</u>	<u>FY 96-97</u>	<u>FY 97-98</u>	<u>FY 98-99</u>	<u>FY 99-00</u>	<u>FY 00-01</u>	<u>FY 01-02</u>
	265.00	286.73	310.24	335.68	363.21	392.99	425.22
5.5% of sales			17.06	18.46	19.98	21.61	23.39
4% State tax			0.683	0.738	0.799	0.865	0.935
2% Local tax			0.341	0.369	0.400	0.432	0.468

FY 1997-98 tax revenues will be 75% of the total shown due to an October 1 effective date.

**FISCAL RESEARCH DIVISION 733-4910 DATE:** June 24, 1997  
**PREPARED BY:** Richard Bostic  
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