

NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: House Bill 1734 (Sixth Edition)

SHORT TITLE: NC Economic Stimulus and Job Creation Act

FISCAL IMPACT (\$MIL.)					
	Yes (X)	No ()	No Estimate Available ()		
	<u>FY 2002-03</u>	<u>FY 2003-04</u>	<u>FY 2004-05</u>	<u>FY 2005-06</u>	<u>FY 2006-07</u>
GENERAL FUND REVENUES:					
Bill Lee Act Changes:					
Machinery/Equip. Credit	-	3.64	7.27	10.91	14.54
Wage Test for Tiers 1 & 2	-	(0.08)	(0.16)	(0.24)	(0.32)
Worker Training Wage Test	-	(0.11)	(0.11)	(.11)	(.11)
Job Development Grants	"See Assumptions and Methodology"				
TOTAL	-	3.45	7.00	10.56	14.11
PRINCIPAL DEPARTMENTS AFFECTED: Department of Revenue, Department of Commerce, Office of State Budget and Management.					

BILL SUMMARY:

PART 1: BILL LEE ACT CHANGES

Issue Background: The Bill Lee Act is the package of state tax incentives that was first adopted in 1996 and has been modified in each subsequent year. The incentives are primarily in the form of tax credits for investment in machinery and equipment, job creation, worker training, 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, per capita income, and population growth. In general, the lower the tier of a county, the more favorable the incentive.

Restructure Machinery and Equipment Credits. Under current law, the targeted statewide investment tax credit is equal to 7% of eligible investment in machinery and equipment. The credit is taken over seven years and applies to the investment that exceeds a certain threshold. The threshold amount varies by tier as follows:

<u>Tier</u>	<u>Threshold</u>	<u>Credit</u>
1	0	7%
2	100,000	7%
3	200,000	7%
4	500,000	7%
5	1,000,000	7%

The threshold is used first to determine eligibility. In addition, the credit is based on the amount of the investment in machinery and equipment that exceeds the threshold amount. The bill restructures the credit rate and threshold by increasing the minimum investment threshold in Tiers 4 and 5 and lowers the credit percentage in Tiers 3 through 5. The new credit schedule would be as follows:

<u>Tier</u>	<u>Threshold</u>	<u>Credit</u>
1	0	7%
2	100,000	7%
3	200,000	6%
4	1,000,000	5%
5	2,000,000	4%

The change is effective for business activities that occur on or after January 1, 2003, but not for those activities occurring on or after that date that are subject to a letter of commitment signed before the date.

Overdue Tax Debts. Prohibits taxpayers from receiving Lee Act credits if the taxpayer has not resolved and overdue tax debt. The change is effective for tax years beginning on or after January 1, 2003.

Worker Training Credit Wage Test. In order to be eligible for Lee Act credits, taxpayers must meet certain wage tests. These tests are based on the average wage of the company's jobs, calculated based on all jobs at an establishment. The bill eliminates the wage test for the worker training credit. The change is effective for tax years beginning on or after January 1, 2003.

Eliminate Wage Test for Tiers 1 and 2. Under current law, taxpayers applying for the Lee Act credits must meet 100% of the wage standard in Tier 1 and exceed 110% of the wage standard in the remaining tiers. The bill eliminates the wage standard for Tiers 1 and 2. The change is effective for tax years beginning on or after January 1, 2003.

Wage Test Timing. Changes wage test from a calendar year calculation to taxpayer's fiscal year, effective for tax years beginning on or after January 1, 2003.

Development Zone Technical Change. Enhanced Lee Act credits are allowed for projects in development zones (high poverty areas). The bill indicates that a parcel of property partially located in a development zone is considered entirely within the zone if all of the following conditions are met: (1) at least 50% of the parcel is located within the zone; (2) the parcel was in

existence and under common ownership prior to the most recent population census; and (3) the parcel is a portion of land made up of one or more tracts or tax parcels of land that is surrounded by a continuous perimeter boundary. This change becomes effective for tax years beginning on or after January 1, 2003.

PART 2: JOB DEVELOPMENT INVESTMENT GRANT PROGRAM

Bill Summary: Establishes the Job Development Investment Grant Program to be administered by the Economic Investment Committee. Under the program, the Committee may enter into agreements with businesses to provide grants in the form of withholding tax payment rebates. Before entering into an agreement, the Committee must find that all the following conditions are met:

- (1) The project proposed by the business will create, during the term of the agreement, a net increase in employment in this State.
- (2) The project will benefit the people of the state by increasing employment opportunities and by strengthening the state's economy.
- (3) The project is consistent with economic development goals for the State and for the area where it will be located.
- (4) A grant is necessary for the completion of the project in North Carolina.
- (5) The total benefits of the project to the State outweigh its costs and render the grant appropriate for the project.

The number of agreements the Committee may enter into during a calendar year is limited to 15. In addition, there is a \$10 million limit on the total annual grants entered into during a single calendar year. The maximum amount of a grant attributable to any specific position in a year is \$6,500. Finally, the program expires on January 1, 2005.

A business may apply to the Committee for a grant for any project that creates the minimum number of eligible positions as set out in the table below. If the project will be located in more than one enterprise tier area, the location with the highest enterprise tier area designation determines the minimum number of eligible positions that must be created.

<u>Enterprise Tier Area</u>	<u>Number of Eligible Positions</u>
Tier One	10
Tier Two	10
Tier Three	10
Tier Four	20
Tier Five	20

A project that consists solely of retail facilities or a professional or semiprofessional sports team or club is not eligible for a grant. If a project consists of both retail facilities and non-retail facilities, only the portion of the project consisting of non-retail facilities is eligible for a grant, and only the withholdings from employees in eligible positions that are employed exclusively in the portion of the project that represents non-retail facilities may be used to determine the amount of the grant. If a warehouse facility is part of a retail facility and supplies only that retail facility, the warehouse facility is not eligible for a grant. Catalog distribution centers are not considered retail facilities for the purpose of this program.

The grants may not be used as venture capital funds, business incubator funds, business start-up funds, or to otherwise fund the initial capitalization of a business.

Just like the Bill Lee Act, a business must provide health insurance for all full-time employees of the project for which the grant is made. In addition, the average wage for all jobs at the location with respect to which the grant is sought must meet the Lee Act wage standard. Finally, the grants may not be provided to taxpayers who have an overdue tax debt or who have had an OSHA citation that has become a final order during preceding three years.

The Economic Investment Committee will consist of the following members:

- (1) The Secretary of Commerce.
- (2) The Secretary of Revenue.
- (3) The Director of the Office of State Budget and Management
- (4) One member appointed by General Assembly upon recommendation of Speaker of House.
- (5) One member appointed by General Assembly upon recommendation of President Pro Tempore of Senate.

The members of the Committee appointed by the General Assembly may not be members of the General Assembly and will serve a two-year term beginning upon appointment.

The Committee may act only upon a decision of three of its five members.

A business shall apply, under oath, to the Committee for a grant on a form prescribed by the Committee that includes at least all the following:

- (1) The name of the business, the proposed location of the project, and the type of activity in which the business will engage at the project site or sites.
- (2) The names and addresses of the principals or management of the business, the nature of the business, and the form of business organization under which it is operated.
- (3) The most recent audited financial statements of the business and any other financial information the Committee considers necessary.
- (4) The number of eligible positions proposed to be created during the base years and thereafter, and the salaries for these positions.
- (5) An estimate of the total withholdings.
- (6) Information concerning other states being considered for the project and the nature of any benefits the company would enjoy as a result of locating in those states.
- (7) Certification that the business will provide health insurance to all full-time employees of the project.
- (8) Information concerning any other state or local government incentives for which the business is applying or that it has an expectation of receiving.
- (9) Any other information necessary for the Committee to evaluate the application.

A business may apply, in one consolidated application in a form and manner determined by the Committee, for a grant on its own behalf as a business and for grants on behalf of the related members of the business who may qualify.

The Committee will consider a application by a business for grants on behalf of its related members only if the related members for whom the application is submitted have assigned to the business any claim of right the related members may have under this program to apply for grants individually during the term of the agreement and have agreed to cooperate with the business in providing to the Committee all the information required for the initial application and the agreement, and any other information the Committee may require. The applicant business is responsible for providing to the Committee all the information required.

If a business applies for a grant on behalf of its related members, the related members included in the application may be permitted to meet the qualifications for a grant collectively by participating in a project that meets the requirements of the program. The amount of a grant may be calculated as if the related members were all collectively one business entity. Any conditions for a grant, other than the number of eligible positions created, apply to each related member who is listed in the application as participating in the project. The grants awarded shall be paid to the applicant business. A grant received by a business may be apportioned to the related members in a manner determined by the business. In order for an agreement to be executed, each related member included in the application must sign the agreement and agree to abide by its terms.

When filing an application under this section the business must pay the Committee a fee of \$5,000. The fee is due at the time the application is filed. The executive branch members of the Committee shall determine the allocation of the fee imposed by this section among the agencies responsible for evaluating the application. The proceeds of the fee are receipts of the agency to which they are credited.

The bill establishes extensive reporting requirements for the Committee.

The Committee is required to conduct a study to determine the minimum funding level required to implement the program successfully and to report the results of this study no later than March 1 of each year.

The amount of the grant awarded in each case shall be a percentage of the withholdings of eligible positions. The percentage shall be no less than 10% and no more than 75% of the withholdings of the eligible positions for a period of years. The percentage used to determine the amount of the grant shall be based on criteria developed by the Committee after considering the following:

- (1) The number of eligible positions to be created.
- (2) The expected duration of those positions.
- (3) The type of contribution the business can make to the long-term growth of the State's economy.
- (4) The amount of other financial assistance the business will receive from the State for the project.
- (5) The total dollar investment the business is making in the project.

- (6) Whether the project uses existing infrastructure and resources in the community
- (7) Whether the project is located in a development zone
- (8) The number of eligible positions that would be filled by residents of a development zone.
- (9) The extent to which the project will mitigate unemployment in the state and the locality.

The term of the grant shall not exceed 12 years starting with the first year a grant is made.

The grant percentage may be based only on eligible positions created during the base years (first two years of program) unless the Committee makes an explicit determination that the grant shall also be based on additional eligible positions created during the remainder of the term of the grant.

The percentage established in the agreement shall be reduced by 25% for any eligible position that is located in an enterprise tier four or five area.

Each community economic development agreement shall include the following:

- (1) A detailed description of the proposed project that will result in job creation and the number of new employees to be hired in the base years and later years.
- (2) The term of the grant and the criteria used to determine the first year for which the grant may be claimed.
- (3) The number of eligible positions that are subjects of the grant and a description of those positions and the location of those positions.
- (4) The amount of the grant based on a percentage of withholdings.
- (5) A method for determining the number of new employees hired during a grant year.
- (6) A method for the business to report annually to the Committee the number of eligible positions for which the grant is to be made.
- (7) A requirement that the business report to the Committee annually the aggregate amount of withholdings during the grant year.
- (8) A provision permitting an audit of the payroll records of the business by the Committee from time to time as the Committee considers necessary.
- (9) A provision that permits the Committee to amend an agreement pursuant to certain guidelines.
- (10) A provision that requires the business to maintain operations at the project location or another location approved by the Committee for at least 150% of the term of the grant and a provision to permit the Committee to recapture all or part of the grant at its discretion if the business does not remain at the site for the required term.
- (11) A provision that requires the business to maintain employment levels in this State at the level of the year immediately preceding the base years.
- (12) A provision establishing the conditions under which the grant agreement may be terminated and grant funds recaptured by the Committee.

- (13) A provision stating that unless the agreement is amended or terminated the agreement is binding and constitutes a pledge and a continuing obligation of the state.
- (14) A provision setting out any allowed variation in terms of the agreement that will not subject the business the business to amendment or termination of the agreement.
- (15) A provision that prohibits the business from manipulating or attempting to manipulate employee withholdings with the purpose of increasing the amount of the grant and that requires the Committee to terminate the agreement and take action to recapture grant funds if the Committee finds that the business has manipulated or attempted to manipulate withholdings with the purpose of increasing the amount of the grant.
- (16) A provision requiring that the business engage in fair employment practices as required by State and federal law and that the business endeavor to use small contractors, minority contractors, physically handicapped contractors, and women contractors whenever practicable in the conduct of its business.
- (17) A provision requiring that the business gives priority consideration to hiring North Carolina residents.
- (18) A provision encouraging the business to use the N.C. State Ports.
- (19) A provision stating that the state is not obligated to make a grant payment until the state has received withholding payments from the business that exceed the grant payments.
- (20) A provision describing the manner in which the amount of the grant will be measured to ensure compliance with the grant caps.
- (21) A provision stating that any recapture of a grant and any amendment to an agreement reducing the amount of the grant or the term of the agreement must, at a minimum, be proportional to the failure to comply measured relative to the condition or criterion with respect to which the failure occurred.
- (22) A provision stating that any disputes over interpretation of the agreement shall be submitted to binding arbitration.
- (23) A provision stating that the amount of a grant associated with any specific eligible position may not exceed six thousand five hundred dollars (\$6,500) in any year.
- (24) A provision stating that the business agrees to submit to an audit at any time the Committee requires one.

Proposed agreements must be reviewed by and signed personally by the Attorney General.

No later than February 1 of each year, for the preceding grant year, every business that is awarded a grant shall submit to the Committee a copy of its State and federal tax returns showing business and nonbusiness income and a report showing withholdings as a condition of its continuation in the grant program. In addition, the business shall submit to the Committee an annual payroll report showing the eligible positions that are created during the base years and the new eligible positions created during each subsequent year of the grant. When making a submission under this section the business must pay the Committee a fee of \$1,500. The fee is due at the time the submission is made. The executive branch members of the Committee shall determine the allocation of the fee imposed by this section among the agencies responsible for

evaluating the submission. The proceeds of the fee are receipts of the agency to which they are credited.

The Committee may require any information that it considers necessary to effectuate the provisions of this program. The Committee may audit any business receiving a grant at any time.

If the business receiving a grant fails to meet or comply with any condition or requirement set forth in an agreement or with criteria developed by the Committee, the Committee shall amend the agreement to reduce the amount of the grant or the term of the agreement and may terminate the agreement. The reduction in the amount or the term must, at a minimum, be proportioned to the failure to comply measured relative to the condition or criterion with respect to which the failure occurred.

If a business fails to maintain employment at the levels stipulated in the agreement or otherwise fails to comply with any condition of the agreement in any year, the Committee must terminate the agreement.

If the Committee finds that the business has manipulated employ withholdings in order to increase the grant amount, the Committee shall immediately terminate the agreement and take action to recapture any grant funds disbursed in any year in which the violation occurred.

Disputes involving interpretation of the agreement must be submitted to binding arbitration.

A qualifying business may receive an annual disbursement of a grant only after the Committee has certified to the State Controller that the business has met the terms and conditions of the agreement. No amount shall be disbursed to a business as a grant under this program in any year until the Secretary of Revenue has certified to the Committee the amount of withholdings received in that year by the Department of Revenue from the business. A qualifying business that has met the terms of the agreement shall make an annual certification of this to the Committee. The Committee shall verify this information and certify to the State Controller that the terms of the agreement have been met. The Committee shall further certify to the State Controller the amount of a grant for which the business is eligible under the agreement and the amount of a grant for which the business would be eligible under the agreement without regard to the 25% grant reduction in Tiers 4 and 5. The State Controller shall remit a check to the business in the amount of the certified grant amount within 90 days of receiving the certification of the Committee.

At the time the State Controller remits a check to a business, the State Controller shall transfer to the Utility Account of the Industrial Development Fund an amount equal to the amount certified by the Committee as the difference between the amount of the grant and the amount of the grant for which the business would be eligible without regard to the 25% reduction for Tiers 4 and 5.

In developing criteria for the awarding of grants and for determining the percentage upon which the amount of a grant is based, the Economic Investment Committee shall consider criteria that address the following:

- (1) Economic impact of the project.
 - a. Impact on gross regional product and gross State product.
 - b. Costs and benefits of the project to the State, including the expected return on investment made in the project by the State.
 - c. Number of direct jobs that will be created by the project, the wages of those jobs, and the total payroll for the project.
 - d. Number of induced short-term, project-related jobs expected to be generated by the project as well as the number of long-term permanent jobs expected to be generated indirectly in the economy as a result of the project.
 - e. Dollar value of the investment, including the size of the investment in real versus personal property and expected depreciation rates.
 - f. Economic circumstances of the county and region, including the extent to which the project will serve to mitigate unemployment.
 - g. The expected time frame during which the project is expected to pay back in State tax revenues the amount of any grants to be paid out.
 - h. The economic demands the project is expected to place upon the community or communities in which it will locate.
 - i. The number of eligible positions that would be filled by residents of development zones.

- (2) Strategic importance of the project to the State, region, or locality.
 - a. The extent to which the project builds or enhances an industrial cluster.
 - b. The extent to which the project falls within a classification of business and industry that the Department of Commerce regards as a target for growth and expansion in the State.
 - c. The ability of the project to attract follow-on investment in the State by suppliers and vendors.
 - d. The extent to which the project serves to maintain and grow jobs in the State in a business undergoing an internal restructuring or rationalization process.
 - e. The extent to which the project can be expected to contribute significantly to and support the local community.

- (3) Quality of jobs.
 - a. The wage level and status of the jobs to be created.
 - b. The quality and value of benefits offered by the company.
 - c. The potential for employee advancement.
 - d. The extent of training programs offered by the company.
 - e. The sustainability of the jobs in the future.
 - f. The workplace safety record of the company.

- (4) Quality of the industry and the project.
 - a. The nature of the project and the projects' relationship to the larger business of the company.
 - b. The nature of the industrial classification of the project and the nature of the business of the company undertaking it.
 - c. The long-term prospects for growth at the project site or sites.

- d. The long-term prospects for growth of the company and the industry within the United States.
 - e. The financial stability of the company associated with the project.
- (5) Environmental impact of the project.
- a. The nature of the business to be conducted.
 - b. The ability of the project to satisfy State, federal, and local environmental law and regulations.
- (6) Geographical dispersion among regions of state and between rural and urban areas.

The bill also makes two changes to the Industrial Development Fund (IDF) and to the Utility Account, which is part of that Fund. The IDF provides assistance to local governments for improvements to infrastructure to enable the locality to attract new businesses. Usually, this assistance is provided to make general improvements, such as improvements to or development of industrial parks, and is not tied to luring a specific project.

The first change is to expand the purposes for which funds in both the Fund and the Account may be used to allow expenditures for telecommunications and high-speed broadband lines and equipment. In addition, the bill would expand the focus of the Utility Account to allow funds to be used to assist local governments in enterprise Tier 3 as well as Tiers 1 and 2 (current law).

The authority to authorize job development investment grants becomes effective January 1, 2003 and expires on January 1, 2005. The remainder of this part of the bill becomes effective when the bill becomes law.

PART 3: FILM INCENTIVES

Under current law, film production companies that engage in production activities in North Carolina may apply for a grant from the Department of Commerce. This grant cannot exceed fifteen percent (15%) of the amount the production company spends for goods and services in the state during a calendar year, or \$200,000 per production. The recently passed budget bill deposited \$500,000 in this account.

The bill tightens the requirements to receive the grant by limiting it to production companies that expend at least \$1,000,000 in the state. This part of the bill becomes effective when the bill becomes law.

PART 6. CAPITAL PLANNING COSTS FOR BIOPHARMACEUTICAL TRAINING CENTER AND CANCER REHABILITATION TREATMENT CENTER.

Section 6. The State Board of Community Colleges, the Board of Governors of The University of North Carolina, and the North Carolina Biotechnology Center are authorized to initiate planning and development of a new biopharmaceutical/bioprocess manufacturing training center to be centrally located and related training facilities to be located at various community colleges. The Board of Directors of the University of North Carolina Health Care System is authorized to

initiate planning and development of a new cancer rehabilitation and treatment center to be located at the University of North Carolina Hospitals at Chapel Hill.

ASSUMPTIONS AND METHODOLOGY:

Bill Lee Act Changes: The fiscal impact estimates for the proposals modifying the Bill Lee Act are based on a sampling of 1999 tax returns filed by businesses reporting or claiming Lee Act credits. The sampling was carried out by the Department of Commerce, based on a universe of 566 firms claiming credits, and was based on scientific methodology. The actual sample size represented 39% of the firms. Since some firms in the sample had facilities at two or more sites, there were a total of 260 locations included in the sample.

Job Development Investment Grant Program: This initiative represents a significant change from the structure of the Bill Lee Act incentives. Eligibility language in the bill leaves the determination to the Economic Investment Committee. This committee will have broad discretion to negotiate the terms of an agreement, including the amount of the grant and the number of years for which the grant is provided. This makes it impossible to determine the exact dollar cost of the grant program. However, the program is limited to 15 projects per year, to \$10 million in grants per year, and sunsets after two years. Thus, the maximum grant amount that may be awarded during the 13 years the program is in effect is \$240 million.

Film Industry Incentives: The first change, tightening the eligibility requirements, is not expected to carry a fiscal impact. Under current law, the Department of Commerce has a great deal of discretion in determining grant awards. It is unlikely Department officials would award a grant to a production company that does not meet the new criteria. Therefore, no fiscal impact is anticipated.

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DATE: October 3, 2002



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