

NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: House Bill 1294 (Third Edition)

SHORT TITLE: Qualified Business Credit/Ports Credit

SPONSOR(S): Rep. Gordon Allen

FISCAL IMPACT					
	Yes (X)	No ()	No Estimate Available ()		
	(\$Million)				
	<u>FY 2003-04</u>	<u>FY 2004-05</u>	<u>FY 2005-06</u>	<u>FY 2006-07</u>	<u>FY 2007-08</u>
REVENUES					
General Fund					
QBV credit	-	-	(6.0)	(6.0)	(6.0)
Ports credit		(\$.65)	(\$.65)	(\$.65)	(\$.65)
EXPENDITURES					
POSITIONS:					
PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED: Department of Revenue; Department of the Secretary of State; North Carolina State Ports Authority					
EFFECTIVE DATE: Sections 1 through 6 (QBV credit) become effective for taxable years beginning on or after January 1, 2004. The remainder of the act is effective when it becomes law.					

BILL SUMMARY: The bill extends the qualified business tax credit program's sunset from 2004 to 2007, expands the definition of a qualified grantee business, and adds a new type of grantee business. The bill also extends the state ports tax credit from January 1, 2004, to January 1, 2009.

BACKGROUND:

- I. Enacted in August 1987 and scheduled to sunset in 2003, the **qualified business investment tax credit** is allowed to individuals and pass through entities. A maximum of \$6 million in credits is allowed each year. For individual taxpayers, the credit is for those who purchase the equity securities or subordinated debt of a qualified business venture or a qualified grantee business directly from that business.

The credit is equal to 25% of the amount invested and may not exceed \$50,000 per individual in a single taxable year. An individual investor may also claim the allocable share of credits obtained by "pass-through entities" of which the investor is an owner. Pass-through entities include limited partnerships, general partnerships, S corporations, and limited liability companies. To be eligible for the tax credit, an individual investor must file Form D-499, Application for Tax Credit for Qualified Business Investments, with the Department of Revenue on or before April 15 of the year following the calendar year in which the investment was made. Any unused credit may be carried forward for the next five years. The total amount of credits allowed to all taxpayers for investments made in a calendar year may not exceed \$6 million. The Secretary of Revenue calculates the total amount of tax credits claimed from applications filed with the Secretary of State. If the amount exceeds the cap, then the Secretary of Revenue allows a portion of the tax credits claimed by allocating the total of \$6 million in tax credits in proportion to the size of the credit claimed by each taxpayer.

- II. The **state ports tax credit** was enacted in 1992 to encourage exporters to use the two State-owned port terminals at Wilmington and Morehead City. This credit was extended in 1995, 1997, 2001, and 2002. The tax credit equals the amount of wharfage, handling, and throughput charges paid to the North Carolina State Ports Authority in the taxable year that exceeds the average amount of charges paid to the Authority for the current tax year and the two previous tax years. The credit is limited to 50% of the tax imposed on the taxpayer for the taxable year and has a five-year carryforward on excess credit. The maximum cumulative credit that one taxpayer may claim is \$2 million.

ASSUMPTIONS AND METHODOLOGY:

Qualified Business Investments Tax Credit

Section 1 of the bill extends the sunset of the Qualified Business tax credit from 2004 to 2007. Since the General Fund revenue forecast for future fiscal years assumes an end to the Qualified Business tax credit program, extension of the sunset means there will be a General Fund revenue loss from FY 2005-06 until FY 2007-08. The revenue loss from tax year 2004 is delayed because investments are made in 2004, applications for the tax credit on the 2004 investments are made in 2005, the Department of Revenue notifies taxpayers in November/December of 2005 of the amount of credit they will receive, then the taxpayers file their tax returns in spring 2006. This puts the revenue loss for 2004 into FY 2005-06.

The bill continues to cap the General Fund revenue loss from the tax credit at \$6 million. This fiscal analysis assumes the credit maximum will be reached in each of the next five years based on program history. The amount of credits applied for exceeded the \$6 million cap five out of six years between 1997 and 2002 (see the following chart).

Year Credit	Corporations/		
<u>Claimed</u>	<u>Individuals</u>	<u>Pass-Throughs</u>	<u>Total</u>
1997	2,322,317	3,677,683	6,000,000*
1998	4,235,771	1,108,870	5,344,641
1999	4,714,892	1,285,108	6,000,000*
2000	4,221,732	1,778,268	6,000,000*
2001	3,612,777	2,387,223	6,000,000*
2002	\$4,179,918	\$1,820,082	\$6,000,000*
	\$45,696,368	\$17,779,425	\$63,475,793
*In these years, total credits requested exceeded \$6 million. Actual requests were as follows:			
	1997	\$9,250,000	
	1999	6,450,000	
	2000	7,000,000	
	2001	19,000,000	
	2002	\$7,825,000	

In 2003, taxpayers have applied for \$5.6 million in credits for investments made in 2002, but the Department of Revenue will not have complete numbers on 2003 qualified business tax credits until extension returns are filed this fall.

Another reason this note assumes the credit maximums will be reached is the expansion in the number of investments taxpayers may receive a tax credit. Section 2 of the bill adds qualified licensee businesses to the list of entities that taxpayers may invest in to get a qualified business tax credit. Qualified licensee businesses have less than \$1 million in gross revenues and are under contract with a doctoral research university or a UNC system school to commercialize technology developed by the university or institution. Section 2 also expands the definition of qualified grantee business to include nonprofits organized to stimulate the wireless industry and the networking and related industry. This will make investors into MCNC-Research and Development Institute grantees eligible for the tax credit.

State Ports Tax Credit

Sections 7 and 8 extend the corporate and individual income tax credit for North Carolina State Ports Authority wharfage, handling and throughput charges from January 1, 2004, to January 1, 2009. Extension of the sunset is a loss because the General Fund revenue forecast for future fiscal years assumes an end to the credit. The projected revenue loss can be computed using North Carolina State Ports Authority annual reports to the General Assembly detailing the annual increase in cargo tons, cargo fees, and the amount of tax credit taken in the previous year.

The income tax credits reported in these annual statements since the program's inception are as follows:

1993	\$ 26,867
1994	\$512,003
1995	\$643,965
1996	\$854,645
1997	\$515,977
1998	\$814,986
1999	\$656,134
2000*	\$1,551,121
2001	\$365,474
2002	\$787,260

*Since the statute does not limit back certifications, four customers claimed \$1,116,565 in credits for shipping expenses from previous years.

The average tax credit for the eight years 1994 through 2002 is \$744,618 and the median tax credit for the same period is approximately \$650,000. This fiscal note will use the median, thus extending the State Ports Authority tax credit will cost the state General Fund \$650,000 each year beginning in tax year 2004 or FY 2004-05. The Ports Authority staff reports that no company has reached the \$2 million maximum cumulative credit and there are no companies close to the maximum amount of credits.

SOURCES OF DATA: Department of Revenue; Department of the Secretary of State; North Carolina State Ports Authority Annual Reports to the General Assembly

FISCAL RESEARCH DIVISION: (919) 733-4910

PREPARED BY: Richard Bostic

APPROVED BY: James D. Johnson, Director, Fiscal Research Division

DATE: June 25, 2003



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