NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: HB 1753 (Second Edition)

SHORT TITLE: Bond and Incentive Act of 2002

FISCAL IMPACT ($MIL.)

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

	FY 2002-03	FY 2003-04	FY 2004-05	FY 2005-06	FY 2006-07
GENERAL FUND REVENUES:					
Corporate Rate Changes		(4.3)	(17.1)	(18.2)	(19.3)

PRINCIPAL DEPARTMENTS AFFECTED: Department of Revenue

PART I: FILM INDUSTRY 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 that the production company spends for goods and services in the state during a calendar year, or $200,000 per production. In addition, the production company must have expenditures of at least $1 million in the state. The recently passed budget bill deposited $500,000 in this account.

PART 3: CORPORATE INCOME TAX RATE CHANGE

Under current law all corporations pay tax at a rate of 6.9% of all taxable income. The bill lowers the tax rate on the net taxable income of up to $30,000 as follows:

Net Taxable Income*	Tax Rate
1-3,000	1%
3,001-6,000	2
6,001-9,000	3
9,001-12,000	4
12,001-15,000	5
15,001-30,000	6
30,001 & Over	6.9%

*Income remaining after deduction of expenses ("taxable profits").

The rate change is effective for tax years beginning on or after January 1, 2004.

ASSUMPTIONS AND METHODOLOGY:

Film Industry Incentives: The 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 met the new criteria. Therefore, no fiscal impact is anticipated.

Corporate Income Tax Rate Change: The latest available date on corporate income tax liability by size of taxpayer is for the 1994 tax year. In addition, we have data for the 1990 tax year. The 1990 and 1994 state data, combined with 1994-99 distribution data for federal corporate returns, provides evidence of how liabilities in the different size groupings grow over time. In addition, the data can be correlated with national measures of pre-tax corporate profits to gauge the factors affecting the growth in the number of taxable returns and changes in the average taxable income for each taxable income class.

Since there is no current annual liability distribution data available, a simulated distribution was developed. The starting point was a comparison of the Fiscal Research Division estimate of "collections based" annual liability (using monthly corporate income tax receipts matched to appropriate tax year) for 1990 and 1994 with the tabulated actual liability. This comparison provided a mechanism that could be used to simulate a 2004 tax year liability distribution by size based on an estimate of the 2004 tax year "collections-based" liability. The latter number was developed using a correlation between U.S. pretax profits and the North Carolina amount estimated by dividing "collections based liability" by the 6.9% tax rate. The U.S. pre-tax profits estimate is from the September 2002 forecast of *Economy.com*.

The FRD analysis, using 1990 and 1994 tax year data, agrees with the recent data furnished by the Department of Revenue for the 2000 tax year.

The analysis assumes that 25% of the 2004 calendar year changes will affect the 2003-04 fiscal year due to April and June estimated tax payments. Discussions with the Department of Revenue in the past have indicated that a substantial number of taxpayers do not reduce their estimated tax payments during the year in which tax relief is granted but choose to receive a refund the next Spring. Thus, the 25% factor is lower than the 45% adjustment if all affected taxpayers fully reduced their estimated tax payments.

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