NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: Senate Bill 1214 (First Edition)

SHORT TITLE: Tax Credit for Certain Real Property Donations.

SPONSOR(S): Senator Clodfelter

FISCAL IMPACT

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

	FY 2004-05	FY 2005-06	FY 2006-07	FY 2007-08	FY 2008-09
REVENUES					
General Fund	See "Assumptions and Methodology"				

PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED: Department of Revenue; Department of Environment and Natural Resources

EFFECTIVE DATE: This act is effective for taxable years beginning on or after January 1, 2005.

BILL SUMMARY: This act recodifies the tax credit for certain real property donations and increases the credit for pass through entities from $250,000 to $500,000.

BACKGROUND: In 2001, the General Assembly approved HB 146 (S.L. 2001-335) to modify the pass-through distribution of partnership income tax credits to conform to federal law. Prior to 2001, when a tax credit was capped at a specific dollar amount, each owner in the partnership was allowed to take that dollar amount of credit. Under federal law, the total credit amount was shared proportionally with the partnership investors based on their share of ownership. HB 146 placed this total credit amount limitation on tax credits for worker training, conservation tillage equipment, poultry composting facility, investment in business property, renewable energy property, and administrative office property, and real property donations. For the tax credit on real property donations, the limitation was delayed until January 1, 2005.

ASSUMPTIONS AND METHODOLOGY: The statutes repealed in sections 2 and 3 of the bill are recodified in section 1 of the bill. The only language not found in the repealed sections is in proposed G.S. 105-163.021(b2) concerning pass-through entities. For income tax law, a pass-through entity is a limited partnership, a general partnership, a joint venture, a subchapter S corporation, or a limited liability company that is owned by individuals or other entities in which the income, losses, and credits "pass through" the entity to the owner in proportion to ownership share. The tax credit is limited to $250,000 for a pass-through entity owned by an individual and $500,000 for a pass-through entity owned by a corporation.

Based on the tax credits taken by pass-through entities from 2000 to 2004, this bill will increase the General Fund revenue loss due to the conservation tax credit. Upon the request of the General Assembly's Fiscal Research Division, the Department of Environment and Natural Resources provided a list of all companies that have applied for the conservation credit in the last five years. The companies on the list were matched against incorporation records kept by the Secretary of State to determine how each company was incorporated. The list contained 82 companies that were either limited partnerships or limited liability companies that fit the qualification of pass-through entity.

The chart below shows the conservation donations for 2001 with the company names deleted. The Amount column has the value of the conservation easement, donation, or bargain sale for each property. Since the number of investors for each company is unknown, for this analysis it is assumed that each company has five investors. The number of investors is important because until December 31, 2004, each investor can take the total credit amount. Thus, for Company D, the $3.6 million donation is divided by five investors to give each investor a $720,000 donation. This donation is multiplied by 25% to get an $180,000 tax credit per investor. The total tax credit for Company D under current law is $900,000 or $180,000 credit times five investors. If this same donation were made after January 1, 2005 when the limits of HB 146 (S.L. 2001-335) takes effect, the maximum credit amount that all five investors would have to share would be $250,000. Under the proposed bill, the maximum for pass-through entities is raised to $500,000, thus, the five investors of Company D would share $500,000.

Entity	Amount	Donation per Investor (Assume 5 Investors)	25% credit per investor	Total Credit until Dec 31, 2004	Total Credit after Jan 1, 2005	Total Credit with new bill
Company A	$1,525,000	$305,000	$76,250	$381,250	$250,000	$381,250
Company B	$1,939,000	$387,800	$96,950	$484,750	$250,000	$484,750
Company C	$2,144,537	$428,907	$107,227	$536,134	$250,000	$500,000
Company D	$3,600,000	$720,000	$180,000	$900,000	$250,000	$500,000
Company E	$670,000	$134,000	$33,500	$167,500	$167,500	$167,500
Company F	$330,000	$66,000	$16,500	$82,500	$82,500	$82,500
Company G	$364,000	$72,800	$18,200	$91,000	$91,000	$91,000
Company H	$425,000	$85,000	$21,250	$106,250	$106,250	$106,250
Company I	$92,000	$18,400	$4,600	$23,000	$23,000	$23,000
Company J	$3,900,000	$780,000	$195,000	$975,000	$250,000	$500,000
				$3,747,384	$1,720,250	$2,836,250

For the ten donations made by pass-through entities in 2001, the state had an estimated revenue loss of $3.7 million. Had the donations been made under the law that takes effect January 1, 2005, the revenue loss would have been $1.7 million for a savings to the state of $2 million. With the increased credit limits in this proposed bill, the 2001 donations would have received credits equal to $2.8 million. While the credits under the proposed bill are less than current law, they are greater than the law that takes effect in 2005. Using the same assumption of five investors per company, the chart below shows the cost of the conservation credits for 81 donations from 2001 to 2004. On average, the tax credit under the proposed bill is $86,105 more per donation than the credit under the law in effect January 1, 2005. For 20 donations a year, this would equal a revenue loss of approximately $1.7 million annually.

	Donations	Total Credit until Dec 31 2004	Total Credit after Jan 1 2005	Total Credit with new bill	Difference bill versus 1/1/05	Difference per Credit
2001	10	$3,747,384	$1,720,250	$2,836,250	($1,116,000)	($111,600)
2002	18	$7,089,550	$3,210,200	$4,931,635	($1,721,435)	($95,635)
2003	28	$6,550,274	$3,479,274	$4,724,024	($1,244,750)	($44,455)
2004	25	$10,698,060	$4,827,500	$7,719,810	($2,892,310)	($115,692)
	81				($6,974,495)	($86,105) per credit

SOURCES OF DATA: Department of Environment and Natural Resources – N.C. Conservation Tax Credit Program; Department of Secretary of State

TECHNICAL CONSIDERATIONS: None

FISCAL RESEARCH DIVISION: (919) 733-4910
PREPARED BY: Richard Bostic

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

Official
Fiscal Research Division
Publication

DATE: June 23, 2004

Signed Copy Located in the NCGA Principal Clerk's Offices