GENERAL ASSEMBLY OF NORTH CAROLINA

Session 2007

Legislative Fiscal Note

BILL NUMBER: Senate Bill 1878 (Second Edition)

SHORT TITLE: Property Tax Modifications.

SPONSOR(S): Senator Clodfelter

FISCAL IMPACT

	Yes (x)	No ( )	No Estimate Available ( )		
	FY 2008-09	**FY 2009-10**	**FY 2010-11**	**FY 2011-12**	**FY 2012-13**
REVENUES:					
General Fund	***No General Fund Impact***				
Local Governments	***$2.5 - $5 million annual gain from mobile home lien changes***				
Local Governments	***Significant revenue loss from low-income housing changes - See assumptions and methodology***				
EXPENDITURES:					
Local Governments	***Some local governments will experience increased costs associated with a more frequent revaluation process. The amount per county will differ and the total cost is not known.***				

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

EFFECTIVE DATE: Part I (Revaluation Schedule) is effective July 1, 2009; Part II (PUV Changes) is effective for taxable years beginning on or after July 1, 2008; Part III (Low-Income Housing) is effective for taxable years beginning on or after July 1, 2008.

BILL SUMMARY:
Senate Bill 1878 is a recommendation of the Revenue Laws Study Committee and would make the following changes to the property tax laws:

- Part I would eliminate horizontal adjustments and would require advancing the next scheduled reappraisal to January 1 of the third year following the year in which the board of county commissioners was notified that the sales assessment ratio for the county was less than .90.
- Part II would modify the present-use value ownership requirements to reflect modern estate planning and would allow property to remain in present-use value when deferred taxes are paid at the time of transfer and the new owner continues to farm the land and files an application for present-use value status.

- Part III classifies qualified North Carolina low-income housing developments as a special class of property and requires valuation of the property to be based on the actual (rent restricted) income.

ASSUMPTIONS AND METHODOLOGY:

Part I - Revaluation Changes

Part I will require some counties to advance their revaluation schedule in the event that their sales assessment ratio drops below 90%. The county would be required to advance the schedule to January 1 of the third year following the notification of the sales assessment ratio. Although the revaluation of property on an advanced schedule would not necessarily have any revenue implications assuming the county adopts a revenue-neutral tax rate, a more frequent revaluation would require additional expenditures to pay for the revalution. The amount of additional expenditures will depend on the number of counties required to advance their revaluation schedules.

Part II - PUV Changes

The General Assembly provides special tax treatment for farmland if the property is used for agricultural, horticultural or forestry purposes. If the farmland meets certain ownership and size requirements and is engaged in commercial production under a sound management plan, the land may be appraised and taxed at its present-use value (PUV), rather than market value. When the land becomes disqualified from PUV, the deferred taxes for the current year and the previous three years become due.

The bill makes several changes to simplify the PUV ownership requirements. Currently, PUV land must be individually owned. This requirement can be satisfied by the following categories: natural persons, business entities, tenancy in common and trusts. To satisfy the definition of business entity, the entity must be composed of natural persons, and the members must be actively engaged in the business or be related to a member who is actively engaged in the business.

The current ownership requirements do not allow for a business entity, such as an LLC, to qualify if one of the members of the business is a trust. For example, if an LLC applies for PUV, and one of the members of the LLC is a trust, the property would not satisfy the ownership requirements because all of the members are not "natural persons," even though the members of the trust may be children of the members of the LLC.

The bill simplifies the ownership requirements by eliminating the requirement that all members of the business entity be natural persons. The definition of "individually owned is changed to include "farms groups," directly or indirectly by individuals in the group. An indirect owner may be the beneficiary of a trust or a business entity. The definition of business entity specifically excludes publicly-traded corporations and clarifies that the business entity must have as its principal business one of the following: agriculture, horticulture, or forestry.

The proposed changes allow the tax assessor to consider the make-up of individual ownership without excluding beneficiaries of a trust who would otherwise be eligible. The changes are not expected to have any significant fiscal impact.

Payment of Deferred Taxes
The bill also allows land to remain in the PUV system if it is transferred to a new owner and the deferred taxes are paid at the time of the transfer. Current law requires the new owner to assume the deferred taxes. This section of the bill is also not expected to have any significant impact.

Part III - Low-Income Housing
This section of the bill designates low-income housing as a special class of property under the North Carolina Constitution and provides for the property tax to be based upon the income generated by the property rather than the market value. To determine the potential fiscal impact of this section, Fiscal Research reviewed an analysis by the Community Investment Corporation of the Carolinas (CICCAR) in which property tax revenues for a sample of low-income housing properties were calculated based upon the current market value approach and the proposed income approach. The analysis indicated that the average property tax per unit would be $500 less using the income approach.

According to CICCAR, there are approximately 42,000 low-income units in North Carolina. Assuming a $500 reduction per unit, the total property tax loss to local governments would be $21 million. This is considered to be a maximum loss estimate because the CICCAR analysis estimates current property tax revenue based on the replacement cost value of the properties, which tends to be higher than assessed values. Therefore, the impact is likely to be less than $21 million.

SOURCES OF DATA: NC Department of Revenue; NC Tax Collectors Association; Community Investment Corporation of the Carolinas

TECHNICAL CONSIDERATIONS: None

FISCAL RESEARCH DIVISION: (919) 733-4910

PREPARED BY: Rodney Bizzell

APPROVED BY: Lynn Muchmore, Director
Fiscal Research Division

DATE: June 11, 2008

Official Fiscal Research Division Publication

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