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State Taxation

The General Assembly made numerous tax changes in 2006, including broad-based tax reductions, major changes to economic development incentives, a restructuring of the taxes on video programming services, and a multitude of more narrowly targeted tax reductions and incentives. The 2006 session also saw new attempts to close business tax loopholes as well as a host of tax administration adjustments.

Tax Reductions

Phaseout of Temporary Sales Tax and Income Tax

After several years of delays, the General Assembly began the process of phasing out the temporary additional one-half percent state sales tax and the temporary additional one-half percent income tax on upper-income individuals. Section 24.12 of the Appropriations Act of 2006, S.L. 2006-66 (S 1741), reduces the state sales tax rate from 4.5 percent to 4.25 percent effective December 1, 2006, and then to 4 percent effective July 1, 2007. The rate was originally increased from 4 to 4.5 percent in 2001 with a sunset date of July 1, 2003, but the sunset date was extended for two years in 2003 and for two more years in 2005. The 2006 change begins the phased sunset before the General Assembly has another chance to extend it.

Section 24.2 of S.L. 2006-66 provides for an earlier sunset in the higher income tax rate on individuals with state taxable income above \$120,000 and married couples filing jointly with income above \$200,000. The tax rate on these taxpayers will fall from 8.25 to 8 percent for the 2007 tax year and will be further reduced for the 2008 tax year to 7.75 percent, the same rate that applies to individuals with state taxable income above \$60,000 and married couples filing jointly with income above \$100,000. The extra one-half percent income tax was enacted in 2001 with a 2004 sunset; the sunset was extended to 2006 in 2003 and to 2008 in 2005. Perhaps because 2006 was an election year, the General Assembly characterized its accelerated sunset of the higher tax on individuals in the highest income brackets as an early reduction in the “rate applicable to most small businesses.”

Motor Fuel Tax Cap

In a year that saw substantial increases in the price of oil and the price of gas at the pump, the General Assembly chose to place a temporary cap on the motor fuel excise tax rate. The motor fuel tax rate in G.S. 105-449.80 consists of two components: a flat rate of 17.5 cents per gallon plus a variable rate equal to the greater of 3.5 cents per gallon or 7 percent of the average wholesale price of motor fuel during a six-month base period. The variable rate for the period of January 1, 2006, through June 30, 2006, was 12.4 cents per gallon. Section 24.3 of S.L. 2006-66 provides that from July 1, 2006, through June 30, 2007, the variable component of the motor fuel tax rate may not exceed 12.4 cents. The General Assembly decided that the General Fund would bear the risk of any revenue reduction that may result from the cap on the motor fuel tax, which supports the Highway Fund and the Highway Trust Fund. Section 2.2(g) of S.L. 2006-66 reserves \$22.9 million in the General Fund to reimburse the Highway Fund and the Highway Trust Fund for any revenue lost due to the motor fuel tax rate cap.

Manufacturing Electricity Sales Tax Reduction

Section 24.19 of S.L. 2006-66 reduces the state sales tax from 2.83 percent to 2.6 percent on electricity sold for use in manufacturing, effective July 1, 2007. To qualify for the 2.6 percent rate, the electricity must be separately metered. Electricity that is not separately metered is taxed at 3 percent.

Targeted Exemptions

S.L. 2006-19 (H 1938) exempts commercial logging machinery and related items from the sales tax and the equivalent privilege tax, effective July 1, 2006. The exemption applies to the following items if sold to a commercial logger: commercial logging machinery, attachments and repair parts for the machinery, lubricants applied to the machinery, and fuel to operate the machinery. These items were previously taxed at 1 percent, with an \$80 maximum tax per article.¹ Commercial logging machinery is machinery used to harvest raw forest products for transport to first market. Examples of commercial logging machinery include log skidders, log carts, tree shears, feller bunchers, winches, chainsaws, tractors, axes, and mallets used to cut and transport timber to a wood products manufacturer.

S.L. 2006-216 (H 143) exempts the following activities from the 3 percent gross receipts privilege tax on amusements: all farm-related exhibitions, shows, attractions, and amusements offered on land used for bona fide farm purposes as defined in G.S. 153A-340. The exemption would apply to hayrides, animal exhibitions, farm pond fishing, cornfield mazes, and other similar attractions. G.S. 153A-340 defines bona fide farm purposes as the production of marketable agricultural products and activities related or incidental to production of these products. Examples of marketable agricultural products are crops, fruits, vegetables, ornamental and flowering plants, dairy, livestock, and poultry. The exemption was made retroactive to January 1, 1999, presumably to release the tax on a specific taxpayer.

Economic Development Tax Changes

The General Assembly was very active in the economic development arena in 2006. It enacted a major new system of tax credits for new and expanding businesses to replace the Bill Lee Act effective January 1, 2007. The General Assembly also enacted new or bigger incentives for a host of specific projects and industries: (1) private rehabilitation of certain historic facilities;

¹ The tax was originally a sales and use tax but was converted to an equivalent privilege tax effective January 1, 2006, in a technical adjustment designed to retain the tax without violating the requirements of the Streamlined Sales and Use Tax Agreement.

(2) expenditures by movie, television, and radio production companies; (3) financial services and securities companies that invest at least \$50 million; (4) motorsports racing teams and facilities; and (5) a \$250 million facility to be constructed for use by an Internet service provider or Web search portal. Finally, the General Assembly granted retroactive tax benefits for an economic development district in Johnston County and a thread mill in Gaston County. These economic development tax changes are discussed in detail in Chapter 8, “Economic and Community Development.”

Sales Tax

Video Programming Services

One of the most significant acts of the 2006 session was the Video Service Competition Act, S.L. 2006-151 (H 2047). Effective January 1, 2007, it provides for equal taxation of video programming services without regard to how the services are delivered and it replaces locally negotiated franchises of cable service provided over a cable system with a state-issued franchise.

Local governments had the authority under federal and state law to award franchises for cable television services and impose cable franchise taxes on cable providers of up to 5 percent of gross receipts. S.L. 2006-151 replaces the local cable television franchising system with a statewide video service franchising scheme and eliminates the authority of local governments to grant new, or renew existing, cable franchises and assess and collect cable franchise taxes. It replaces local revenues from the cable franchise taxes with a new distribution of shared state sales tax collections on telecommunications services, video programming services, and direct-to-home satellite services. The act also modifies the law governing public access (PEG) channels. The franchising, revenue distribution, and PEG changes are described in more detail in Chapter 15, “Local Government and Local Finance.”

North Carolina began taxing communication services when the technologies enabling the services were distinct technologies and the providers of the services were separate taxpayers. Over the past several years, the technology used to provide these services has converged so that the line between the services is no longer distinct. The tax system that had evolved imposed a 7 percent sales tax on telecommunication services and on direct-to-home satellite service. Municipalities received a share of the tax on telecommunications but not on satellite service. Cable television services were also subject to a 7 percent sales tax but with a credit for any local franchise taxes paid on the service. Digital audio radio service was subject to a 4.5 percent state sales tax and a 2.5 percent local sales tax.

S.L. 2006-151 equalizes the taxes on video programming services by applying the state 7 percent sales tax to all video programming services, repealing the local authority to impose a franchise tax on cable services, and repealing the sales tax credit allowed to cable companies for local franchise taxes paid. The act preserves the local government revenue stream by distributing part of the sales tax revenues from telecommunications and video programming services to the counties and cities.

Video programming is defined as programming provided by, or generally considered comparable to programming provided by, a television broadcast station, regardless of the method of delivery. The term includes cable services offered over private rights-of-way as well as those offered over public rights-of-way. The 7 percent state sales tax applies to gross receipts derived from providing video programming to a subscriber in this state effective January 1, 2007. Although the term “video programming” includes broadcast services, the provision of these services would not be taxed unless the provider sells the service to subscribers and thus realizes gross receipts from the provision of the services.

Railway Cars

Section 24.13 of S.L. 2006-66 provides utility companies with the same refund for a portion of sales and uses taxes paid on purchases of railway cars and accessories that is currently available to interstate carriers for the same purchases. The formula for calculating the refund is based on the number of miles that the taxpayer operated the railway cars in the state as compared to the total miles, both inside and outside the state. Section 24.13 also establishes a special sourcing rule for periodic payments by utilities for lease or rental of certain railway cars. The general rule for a railway car is that all periodic payments are sourced based on the location of receipt or delivery of the car if it is used in interstate commerce; if it is not used in interstate commerce, the second and subsequent payments are sourced based on the location of the car for the period covered by each payment. Section 24.13 provides that for utility company railway cars all payments will be sourced based on the location of delivery or receipt whether or not the car is used in interstate commerce.

Alcohol

G.S. 105-164.14 allows a variety of taxpayers sales and use tax refunds on certain purchases if qualifying requirements are met. Section 24A.1 of S.L. 2006-66 provides that purchases of alcoholic beverages may not qualify for a refund. An alcoholic beverage is one that contains at least 0.5 percent alcohol by volume, such as malt beverages, unfortified wine, fortified wine, spirituous liquor, and mixed beverages.

Administrative Changes

S.L. 2006-33 (H 1915) makes three administrative changes to the sales tax law: it incorporates several definitions from the Streamlined Sales Tax Agreement into North Carolina law, changes the tax payment requirements for semi-monthly sales taxpayers, and allows a credit for sales tax paid on tangible personal property that is added to a modular home and sold with the modular home.

Sections 1 through 8 of the act modify the definitions that apply to telecommunications services for sales and use tax purposes, effective January 1, 2007. The changes were made to adopt the definitions in the Streamlined Sales Tax Agreement (SSTA). The SSTA is part of an effort by states, with input from local governments and the private sector, to simplify and modernize sales and use tax collection and administration. The goal of the project is to enhance collection of sales and use taxes on interstate transactions. The project, which began in March 2000, is intended to achieve sufficient simplification and uniformity to encourage sellers to voluntarily collect tax on sales to participating states even if the seller does not have nexus there.

The definition changes are mainly technical and conforming. The change in the definition of *telecommunications service* will, however, result in Universal Service Fund surcharges and paging service charges becoming part of the sales price and therefore subject to tax.

S.L. 2006-33 makes a conforming change to the requirements for a certified automated system that a taxpayer may use to collect sales and use taxes for all states under the SSTA. A *certified automated system* is a software program certified by the Secretary of Revenue as being able to correctly determine the applicable state and local sales tax rate. The act deletes a condition that is not part of the SSTA.

S.L. 2006-33 also simplifies tax filing for retailers that are liable for at least \$10,000 a month of sales tax, electric utility tax, or piped natural gas excise tax. The act replaces the semimonthly payment schedule with a single monthly payment that includes a prepayment of the next month's liability. On the twentieth of each month, the taxpayer pays any amount remaining due for the preceding month and 65 percent of the amount estimated to be due for the current month. The new schedule will be simpler and eliminates the need for underpayment penalties because taxpayers will have more time to gather data before filing a return.

Tax Credits

In addition to the economic development tax credit changes discussed in Chapter 8, "Economic and Community Development," the 2006 General Assembly enacted some new tax credits and modified several existing tax credits. Section 24.4 of S.L. 2006-66 enacts a new tax credit for small businesses that provide employee health insurance, effective beginning with the 2007 tax year. The credit is allowed to a taxpayer that employs no more than twenty-five full-time employees and provides health insurance for all of its employees who work at least thirty hours a week. The taxpayer is considered to provide health insurance for an employee if the taxpayer pays at least half of the premiums for basic health care coverage for the employee or if the employee has existing coverage that provides benefits equivalent to basic health care coverage. The amount of the credit is the first \$250 of annual cost to the taxpayer of providing health insurance for each employee with an annual salary of no more than \$40,000. The credit is in addition to the income tax deduction a taxpayer may take for providing health insurance for employees. The credit may be taken against either income tax or franchise tax and is limited to 50 percent of the taxpayer's tax liability. Any unused portion of the credit may be carried forward for five years. The new credit is set to expire January 1, 2009.

The income tax credits in G.S. 105-151.12 and G.S. 105-130.34 are allowed to individual and corporate taxpayers that make a qualified donation of an interest in North Carolina real property that is useful for conservation purposes. In S.L. 2001-335, the General Assembly corrected and clarified the general law governing allocation of partnerships' tax credits, so that any dollar amount limitation on a credit applies to the total credit allowed to a partnership. The limited amount is then allocated among the partners on a proportional basis. Before this change, the limit applied separately to each partner. The 2001 act delayed this dollar amount limitation until 2005 for partnerships that are allowed a credit for real property donations. In 2004, the limitation was further delayed until 2006. Section 24.15 of S.L. 2006-66 postpones for one more year, until 2007, the imposition of the dollar amount limitation on partners taking this credit.

Section 9 of S.L. 2006-18 (H 1892) conforms the amount of the credit for child care and certain employment-related expenses to the amount allowed for the corresponding federal credit, effective beginning with the 2006 tax year. North Carolina allows an income tax credit to a taxpayer who is eligible for the federal credit for child-care and employment-related expenses. The amount of each credit is based on a percentage of the expenses, up to a maximum amount. For the state credit, the maximum amount of expenses was \$2,400 when there is one qualifying individual in the household and \$4,800 when there is more than one qualifying individual. Until 2003, these maximum amounts were the same as the federal maximum amounts. In 2003, the federal maximums increased to \$3,000 and \$6,000, respectively. Section 9 increases the state maximums to the federal amounts. It also clarifies that the amount of expenses used in calculating the credit may not include any expenses excluded from gross income.

S.L. 2006-66 expands tax credit incentives for certain renewable fuel businesses. Section 24.7 extends from January 1, 2008, to January 1, 2011, the sunset on the credits for constructing renewable fuel production facilities and constructing renewable fuel dispensing facilities. Section 24.7, as amended by Section 19.5 of S.L. 2006-259 (S 1523), also creates a more generous credit if the taxpayer invests at least \$400 million in three separate facilities over a five-year period. The details of the enhanced credit are apparently tailored to fit a specific project. A taxpayer may not claim both credits with respect to the same facility. Section 24.8 of S.L. 2006-66 enacts a new tax credit for providers of 100 percent (not blended) biodiesel that produce at least 100,000 gallons of biodiesel during the taxable year. The amount of the credit is equal to the per gallon motor fuel tax paid by the producer on the biodiesel, not to exceed \$500,000 a year. The credit may be claimed against income tax or franchise tax, is limited to 50 percent of the amount of tax liability against which it is claimed, and has a carryforward period of five years. The credit sunsets January 1, 2010.

The Division of Marine Fisheries of the Department of Environment and Natural Resources operates a voluntary oyster shell donation program. In addition, the division purchases oyster shells in very large quantities from shucking houses at a negotiated price of 50 cents per bushel.

Recycled oyster shells can be used for landscaping, to manufacture nutritional supplements, and to be placed in sanctuaries or estuaries for restoration of oyster populations. Beginning October 1, 2009, oyster shells may not be disposed of in landfills.

Section 24.18 of S.L. 2006-66 enacts a nonrefundable income tax credit of \$1 per bushel of oyster shells donated to the Division of Marine Fisheries. The credit may be carried forward for five years. The taxpayer may not claim a deduction for any oyster shells for which the credit is claimed. The credit is effective beginning with the 2006 tax year and is set to expire in 2011.

Corporate and Business Taxes

Royalty Income

In 2001 the General Assembly enacted G.S. 105-130.7A, which restates that a company's receipts from royalty payments for the use of trademarks in North Carolina are income from doing business in North Carolina and provides adjustments to assure full and fair accountability of this income in relationship to where it is actually earned. Effective beginning with the 2006 tax year, Section 24A.3 of S.L. 2006-66 expands G.S. 105-130.7A to include royalties for the use of patents and copyrights in North Carolina. In cases where the recipient of the North Carolina royalty income is unrelated to the payer, the recipient is required to pay tax on the income to North Carolina. In cases where the recipient and the payer are related, they have an option on how the income is reported to North Carolina. Either the payer can deduct the North Carolina royalty payments on its North Carolina return and the recipient can include them on its North Carolina return, or the payer can add them to its North Carolina income and the recipient can deduct them on its North Carolina return. Section 10 of S.L. 2006-196 (§ 1891) further amends G.S. 105-130.7A to clarify that the payer is not required to add royalties to its North Carolina income if the related recipient is a foreign corporation that paid an equivalent tax on the royalties to a country that has a tax treaty with the United States.

Franchise Tax

The franchise tax is levied on S Corporations and C Corporations for the privilege of doing business in North Carolina. The tax rate is \$1.50 per \$1,000 of value of the greatest of (1) apportioned net book value of the corporation, (2) 55 percent of appraised value of real and tangible personal property in the state, or (3) total actual investment in tangible property in the state. The General Assembly enacted S.L. 2001-327 to close a franchise tax loophole whereby a corporation, subject to North Carolina franchise tax, could set up a single-member limited liability company (LLC), transfer assets to the LLC in a tax-free transfer, and avoid paying taxes on the transferred assets because LLCs were not subject to the franchise tax. The 2001 law evolved into G.S. 105-114.1 as the General Assembly wrestled with further loopholes and problems with the law in 2002 and 2004.

Effective beginning with the 2007 tax year, Section 24A.2 of S.L. 2006-66 further amends G.S. 105-114.1 and the franchise tax law to close another loophole in the franchise tax. In general, G.S. 105-114.1 requires a corporation to pay franchise tax on the assets of an LLC that it controls. The income tax law provides that an LLC may be disregarded and treated as a division of its parent; an out-of-state parent company of a North Carolina LLC is thus considered to own property in North Carolina and therefore has nexus, subjecting it to income and franchise tax, including the attribution rules of G.S. 105-114.1. The loophole addressed by S.L. 2006-66 arises if an out-of-state parent of a North Carolina corporation converts the corporation to an LLC but has it elect to file income taxes as a C Corporation. The North Carolina LLC is not required to pay franchise taxes on its assets and, if it elects to file income taxes as a C Corporation, no nexus is created for the out-of-state parent, so the parent cannot be required to pay franchise tax under G.S. 105-114.1. S.L. 2006-66 closes this loophole by providing that an LLC that elects to file

income taxes as a C Corporation is also treated as a C Corporation for purposes of the franchise tax.

Section 9 of S.L. 2006-196 makes a conforming change to the definition of *holding company* for franchise tax purposes, in order to recognize that LLCs have voting capital interests rather than voting stock. The maximum franchise tax on holding companies, which may be corporations or LLCs, is \$75,000 a year.

Effective beginning with the 2007 tax year, Part I of S.L. 2006-95 (S 1283) clarifies the treatment of deferred tax assets in the computation of the franchise tax capital base. The act amends G.S. 105-122(b) to provide that deferred tax liabilities may be reduced, but not below zero, by their corresponding deferred tax assets. The act also reorganizes and modernizes the language of the statute.

S Corporations

S.L. 2006-17 (H 1898) provides that corporate income tax adjustments do not apply to S Corporations, effective beginning with the 2007 tax year. The act amends the S Corporation Income Tax Act and the Individual Income Tax Act to provide that an individual's pro rata share of income from an S Corporation is subject only to individual income tax adjustments, rather than to both individual and corporate income tax adjustments. The act also makes a conforming change to require shareholders to add to North Carolina taxable income the amount of the federal built-in gains tax that the shareholder was allowed to deduct for federal tax purposes to offset the amount of the federal built-in gains tax imposed on the S Corporation. Because North Carolina does not impose a built-in gains tax on the S Corporation, no offsetting deduction is needed for the shareholder.

Individual Income Tax

In addition to starting the phase-down of the additional one-half percent income tax on upper-income individuals, S.L. 2006-66 makes two changes to the individual income tax. Effective beginning with the 2006 tax year, Section 24.11 allows a married couple the option of filing jointly if the couple files a federal joint return and if one spouse is a nonresident with no income from North Carolina. Because North Carolina does not have jurisdiction over the nonresident spouse, the law can permit but not require a joint return. If each spouse is either a resident or has North Carolina income, a married couple that files a federal joint return is required to file a joint North Carolina return.

Section 24.12 of S.L. 2006-66, as amended by Section 27 of S.L. 2006-198, allows certain individuals to deduct amounts contributed to an account in the Parental Savings Trust Fund. To qualify for the income tax deduction, the individual must have adjusted gross income below \$60,000 (\$100,000 for married couples filing jointly). For the 2006 tax year, the amount of the deduction is capped at \$750 for single filers and \$1,500 for married couples filing jointly. Beginning in the 2007 tax year, the caps are \$2,000 and \$4,000, respectively. The deduction is repealed beginning in 2011. The Parental Savings Trust Fund is a qualified tuition program under Section 529 of the Internal Revenue Code. Distributions from qualified tuition programs are excludable from taxable income to the extent the distributions are used to pay for qualified higher education expenses. The Parental Savings Trust Fund deduction allowed by Section 24.12 must be added back to taxable income if the amount is withdrawn from the fund but not used to pay for qualified higher education expenses of the designated beneficiary, unless the withdrawal was made because of the death or permanent disability of the beneficiary.

Tax Administration

Internal Revenue Code Reference Update

North Carolina's tax law tracks many provisions of the federal Internal Revenue Code by reference to the code.² The General Assembly determines each year whether to update its reference to the Internal Revenue Code.³ Updating the Internal Revenue Code reference makes recent amendments to the code applicable to the state to the extent that state law tracks federal law. The General Assembly's decision on whether to conform to federal changes is based on the fiscal, practical, and policy implications of the federal changes and is normally enacted in the following year, rather than in the same year the federal changes are made. Under North Carolina law prior to the enactment of S.L. 2006-18, the reference date to the code was January 1, 2005. Section 1 of S.L. 2006-18 changes the reference date to January 1, 2006. Updating the reference date to January 1, 2006, incorporates the federal changes to the code enacted during 2005. As required by the North Carolina Constitution, the act delays until January 1, 2006, the incorporation of any federal changes that would increase North Carolina taxable income retroactively for an earlier tax year.

There were four major pieces of federal legislation that amended the Internal Revenue Code in 2005: the Energy Tax Incentive Act of 2005 (P.L. 109-58); the Safe, Accountable, Flexible, Efficient (SAFE) Transportation Equity Act of 2005 (P.L. 109-59); the Katrina Emergency Tax Relief Act of 2005 (P.L. 109-73); and the Gulf Opportunity Zone Act of 2005 (P.L. 109-135). The tax changes made by the SAFE Transportation Equity Act have little impact on North Carolina taxes. The remaining three federal acts, however, made numerous changes that will affect North Carolina taxes for individuals, businesses, and other entities; those changes are described in detail in *2006 Finance Law Changes*, written by the legislature's tax staff and available on the Web at www.ncleg.net/LegislativePublications/.

Motor Fuel Tax Administration

S.L. 2006-162 (H 1963) makes a number of changes to the laws governing administration of the motor fuel tax. Section 12(c) repeals provisions that formerly required that civil penalties collected for violations of the motor fuel tax laws and the motor carrier laws be credited to the Highway Fund. Instead, the proceeds of these penalties are credited to the Civil Penalty and Forfeiture Fund as required by *North Carolina School Boards Assn. v. Moore*, 359 N.C. 474, 614 S.E.2d. 504 (2005). In the *Moore* case, the North Carolina Supreme Court held that the penalties assessed under G.S. Chapter 105 are imposed as a monetary payment for a taxpayer's noncompliance with a mandate of the Revenue Act, that they are punitive in nature, and that they are therefore subject to Article IX, Section 7, of the North Carolina Constitution, which requires civil penalties to be remitted to the Civil Penalty and Forfeiture Fund for use by the schools.

Section 13 of S.L. 2006-162 extends the authority of the Department of Revenue to cross-match information relating to motor fuel, so that it may now monitor intrastate movement of fuel in addition to fuel moving in or out of North Carolina. Effective July 1, 2007, the section provides

² North Carolina first began referencing the Internal Revenue Code in 1967, the year it changed its taxation of corporate income to a percentage of federal taxable income.

³ The North Carolina Constitution imposes an obstacle to a statute that automatically adopts any changes in federal tax law. Article V, Section 2(1) of the constitution provides in pertinent part that the "power of taxation . . . shall never be surrendered, suspended, or contracted away." Relying on this provision, the North Carolina court decisions on delegation of legislative power to administrative agencies, and an analysis of the few federal cases on this issue, the Attorney General's Office concluded in a memorandum issued in 1977 to the director of the Tax Research Division of the Department of Revenue that a "statute which adopts by reference future amendments to the Internal Revenue Code would . . . be invalidated as an unconstitutional delegation of legislative power."

that anyone who transports fuel must be licensed as a transporter and that all transporters must file informational returns on all movements of motor fuel.

Effective January 1, 2007, Section 14 of the act repeals the authority of licensed distributors and importers to use exempt cards at the terminal rack to remove fuel without paying tax. Instead, they will be able to obtain a monthly refund on any sales of fuel to exempt entities (the federal government, the state, local boards of education, charter schools, community colleges, counties, municipalities, and airports). This change conforms North Carolina law to the laws of the surrounding states that do not allow untaxed gasoline or undyed fuel to leave their terminals without the imposition of the tax. Effective January 1, 2007, Section 15 provides a common due date of the twenty-second day of the month for all motor fuel tax and informational returns.

Additional Gross Premiums Taxes on Fire and Lightning Coverage

Under prior law, G.S. 105-228.5(d)(3) imposed an additional statewide tax of 1.33 percent on gross premiums on insurance contracts that provide fire and lightning coverage, other than marine and automobile policies. G.S. 105-228.5(d)(4) imposes an additional local fire and lightning tax at 0.5 percent, which applies only to coverage within fire districts but has no exception for marine or automobile policies. Effective January 1, 2006, S.L. 2006-196 temporarily revises the statewide fire and lightning tax so that the percentage of gross premiums subject to the tax varies according to the type of insurance policy, as follows: (1) fire loss—100 percent; (2) nonliability portion of commercial multiple peril—100 percent, liability portion—0 percent; (3) homeowner's—50 percent; (4) farm owner's—30 percent. These percentages are consistent with how the tax had been administered before 2006.

Effective January 1, 2008, S.L. 2006-196 repeals the statewide and local fire and lightning taxes and replaces them with a simpler and broader tax that applies to property coverage. The tax rate is 0.85 percent applied to 100 percent of premiums for property coverage and 10 percent of premiums for automobile physical damage. S.L. 2006-196 also changes the way the tax proceeds are distributed, effective January 1, 2008. The act directs the Revenue Laws Study Committee to study the rewrite of the fire and lightning tax and the distribution of its net proceeds.

Other Technical and Administrative Changes

S.L. 2006-18 reduces from two years to six months the period of time in which a taxpayer must report a federal change. Taxpayers are required to report federal changes because North Carolina estate, gift, and income taxes are, to varying degrees, based on amounts determined with respect to federal law. The six-month deadline provided by this act conforms to the Multistate Tax Commission's model uniform statute for reporting federal changes, which is intended to bring uniformity to this issue among the states.

S.L. 2006-18 conforms the state filing date to the federal filing date for income tax returns of nonresident aliens, effective beginning with the 2006 tax year. Federal income tax returns for nonresident aliens are due June 15 for calendar year taxpayers. Under prior law, the North Carolina income tax return for a calendar year taxpayer would be due March 15 (corporations) or April 15 (individuals). Because the North Carolina return is based on the federal return, these dates created a compliance burden for nonresident aliens. S.L. 2006-18 makes the filing date the same as the federal date.

S.L. 2006-162 makes numerous technical, clarifying, and administrative changes to the revenue laws and related statutes. These changes are described in detail in *2006 Finance Law Changes*, written by the legislature's tax staff and available on the Web at www.ncleg.net/LegislativePublications/.

Martha H. Harris