NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: HB 1734 (Proposed Committee Substitute H1734-PCS4281-LY-50)

SHORT TITLE: NC Economic Stimulus and Job Creation Act

SPONSOR(S):

FISCAL IMPACT ($MIL.)

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

	FY 2002-03	**FY 2003-04**	**FY 2004-05**	**FY 2005-06**	**FY 2006-07**
REVENUES:					
Bill Lee Act Changes: State General Fund					
Machinery/Equip. Credit	-	3.64	7.27	10.91	14.54
Wage Test for Tiers 1 & 2	-	-.08	-.16	-.24	-.32
Worker Training Wage Test	-	-.11	-.11	-.11	-.11
		3.45	**7.00**	**10.56**	**14.11**

Job Creation Grant Program "See Assumptions and Methodology"

EXPENDITURES: The enactment of the bill is not expected to affect budget requirements of any of the affected agencies.

PRINCIPAL DEPARTMENTS AFFECTED: Department of Revenue, Department of Commerce, Office of State Budget and Management

ISSUE BACKGROUND: The Bill Lee Act is the package of state tax incentives that was first adopted in 1996 and has been modified in each subsequent year. The incentives are primarily in the form of tax credits for investment in machinery and equipment, job creation, worker training, and research/development. The credits apply to activities undertaken by specifically named industrial classifications. For many of the credits, the counties of the State are divided into five economic distress tiers based on the unemployment rate, per capita income, and population growth. In general, the lower the tier of a county, the more favorable the incentive.

BILL SUMMARY:

Restructure Machinery and Equipment Credits. Under current law, the targeted statewide investment tax credit is equal to 7% of eligible investment in machinery and equipment. The credit is taken over seven years and applies to the investment that exceeds a certain threshold. The threshold amount varies by tier as follows:

Tier	Threshold	Credit
1	0	7%
2	100,000	7%
3	200,000	7%
4	500,000	7%
5	1,000,000	7%

The threshold is used first to determine eligibility. In addition, the credit is based on the amount of the investment in machinery and equipment that exceeds the threshold amount. The bill restructures the credit rate and threshold by increasing the minimum investment threshold in Tiers 4 and 5 and lowers the credit percentage in Tiers 3 through 5. The new credit schedule would be as follows:

Tier	Threshold	Credit
1	0	7%
2	100,000	7%
3	200,000	6%
4	1,000,000	5%
5	2,000,000	4%

The change is effective for business activities that occur on or after January 1, 2003, but not for those activities occurring on or after that date that are subject to a letter of commitment signed before the date.

Worker Training Credit Wage Test. In order to be eligible for Lee Act credits, taxpayers must meet certain wage tests. These tests are based on the average wage of the company's jobs, calculated based on all jobs at an establishment. The bill eliminates the wage test for the worker training credit. The change is effective for tax years beginning on or after January 1, 2003.

Eliminate Wage Test for Tiers 1 and 2. Under current law, taxpayers applying for the Lee Act credits must meet 100% of the wage standard in Tier 1 and exceed 110% of the wage standard in the remaining tiers. The bill eliminates the wage standard for Tiers 1 and 2. The change is effective for tax years beginning on or after January 1, 2003.

Development Zone Technical Change. Enhanced Lee Act credits are allowed for projects in development zones (high poverty areas). The bill indicates that a parcel of property partially located in a development zone is considered entirely within the zone if all of the following conditions are met: (1) at least 50% of the parcel is located within the zone; (2) the parcel was in existence and under common ownership prior to the most recent population census; and (3) the parcel is a portion of land made up of one or more tracts or tax parcels of land that is surrounded by a continuous perimeter boundary. This change becomes effective July 1, 2002.

Job Development Investment Grant Program. Establishes the Job Development Investment Grant Program to be administered by the Economic Investment Committee. Under the program, the Committee may enter into agreements with businesses to provide grants in the form of withholding tax payment givebacks. Before entering into an agreement, the Committee must find that all the following conditions are met:

(1) The project proposed by the business will create, during the term of the agreement, a net increase in employment in this State.
(2) The project will benefit the people of the state by increasing employment opportunities and by strengthening the state's economy.
(3) The project is consistent with economic development goals for the State and for the area where it will be located.
(4) A grand is necessary for the completion of the project in North Carolina.
(5) The total benefits of the project to the State outweigh its costs and render the grant appropriate for the project.

The number of agreements the Committee may enter into during a state fiscal year is limited to 25.

A business may apply to the Committee for a grant for any project that creates the minimum number of eligible positions as set out in the table below. If the project will be located in more than one enterprise tier area, the location with the highest enterprise tier area designation determines the minimum number of eligible positions that must be created.

Enterprise Tier Area	Number of Eligible Positions
Tier One	10
Tier Two	10
Tier Three	10
Tier Four	20
Tier Five	20

A project that consists solely of retail facilities or a professional or semiprofessional sports team or club is not eligible for a grant. If a project consists of both retail facilities and non-retail facilities, only the portion of the project consisting of non-retail facilities is eligible for a grant, and only the withholdings from employees in eligible positions that are employed exclusively in the portion of the project that represents non-retail facilities may be used to determine the amount of the grant. If a warehouse facility is part of a retail facility and supplies only that retail facility, the warehouse facility is not eligible for a grant. Catalog distribution centers are not considered retail facilities.

Just like the Bill Lee Act, a business must provide health insurance for all of the full-time employees of the project for which the grant is made. In addition, the average wage for all jobs at the location with respect to which the grant is sought must meet the Lee Act wage standard and the business and related members must not have any outstanding final state tax assessments against it.

The Economic Investment Committee will consist of the following members:

(1) The Secretary of Commerce.
(2) The Secretary of Revenue.
(3) The Director of the Office of State Budget and Management.
(4) The President of the Community College System.
(5) The Commissioner of Labor.

The Committee may act only upon the unanimous consent of the members. A business shall apply, under oath, to the Committee for a grant on a form prescribed by the Committee that includes at least all the following:

(1) The name of the business, the proposed location of the project, and the type of activity in which the business will engage at the project site or sites.
(2) The names and addresses of the principals or management of the business, the nature of the business, and the form of business organization under which it is operated.
(3) The most recent audited financial statements of the business and any other financial information the Committee considers necessary.
(4) The number of eligible positions proposed to be created during the base years and thereafter, and the salaries for these positions.
(5) An estimate of the total withholdings.
(6) Information concerning other states being considered for the project and the nature of any benefits the company would enjoy as a result of locating in those states.
(7) Certification that the business will provide health insurance to all full-time employees of the project.
(8) Information concerning any other state or local government incentives for which the business is applying or that it has an expectation of receiving.
(9) Certification that the project will not be undertaken in North Carolina unless the applicant is awarded a grant.
(10) Any other information necessary for the Committee to evaluate the application.

A business may apply, in one consolidated application in a form and manner determined by the Committee, for a grant on its own behalf as a business and for grants on behalf of the related members of the business who may qualify.

The Committee will consider a application by a business for grants on behalf of its related members only if the related members for whom the application is submitted have assigned to the business any claim of right the related members may have under this program to apply for grants individually during the term of the agreement and have agreed to cooperate with the business in providing to the Committee all the information required for the initial application and the agreement, and any other information the Committee may require. The applicant business is responsible for providing to the Committee all the information required.

If a business applies for a grant on behalf of its related members, the related members included in the application may be permitted to meet the qualifications for a grant collectively by participating in a project that meets the requirements of the program. The amount of a grant may be calculated as if the related members were all collectively one business entity. Any conditions for a grant, other than the number of eligible positions created, apply to each related member who is listed in the application as participating in the project. The grants awarded shall be paid to the applicant business. A grant received by a business may be apportioned to the related members in a manner determined by the business. In order for an agreement to be executed, each related member included in the application must sign the agreement and agree to abide by its terms.

When filing an application under this section the business must pay the Committee a fee of $5,000. The fee is due at the time the application is filed. The Committee shall determine the allocation of the fee imposed by this section among the agencies responsible for evaluating the application. The proceeds of the fee are receipts of the agency to which they are credited.

The bill establishes extensive reporting requirements for the Committee.

The Committee is required to conduct a study to determine the minimum funding level required to implement the program successfully and to report the results of this study no later than March 1 of each year.

The amount of the grant awarded in each case shall be a percentage of the withholdings of eligible positions. The percentage shall be no less than 10% and no more than 75% of the withholdings of the eligible positions for a period of years. The percentage used to determine the amount of the grant shall be based on criteria developed by the Committee after considering the following:

(1) The number of eligible positions to be created.
(2) The expected duration of those positions.
(3) The type of contribution the business can make to the long-term growth of the State's economy.
(4) The amount of other financial assistance the business will receive from the State for the project.
(5) The total dollar investment the business is making in the project.
(6) Whether the project uses existing infrastructure and resources in the community
(7) Whether the project is located in a development zone
(8) The number of eligible positions that would be filled by residents of a development zone.

The term of the grant shall not exceed 12 years starting with the first year a grant is made.

The grant percentage may be based only on eligible positions created during the base years (first two years of program) unless the Committee makes an explicit determination that the grant shall also be based on additional eligible positions created during the remainder of the term of the grant.

The percentage established in the agreement shall be reduced by 25% for any eligible position that is located in an enterprise tier four or five area.

A business that is receiving any other grant by operation of State law may not receive grant monies under this program if the total state grants exceed (75%) of the withholdings of the business, unless the Committee makes an explicit finding that the additional grant is necessary to secure the project.

Each community economic development agreement shall include the following:

(1) A detailed description of the proposed project that will result in job creation and the number of new employees to be hired in the base years and later years.

(2) The term of the grant and the criteria used to determine the first year for which the grant may be claimed.

(3) The number of eligible positions that are subjects of the grant and a description of those positions and the location of those positions.

(4) The amount of the grant based on a percentage of withholdings.

(5) A method for determining the number of new employees hired during a grant year.

(6) A method for the business to report annually to the Committee the number of eligible positions for which the grant is to be made.

(7) A requirement that the business report to the Committee annually the aggregate amount of withholdings during the grant year.

(8) A provision permitting an audit of the payroll records of the business by the Committee from time to time as the Committee considers necessary.

(9) A provision that permits the Committee to amend an agreement pursuant to certain guidelines.

(10) A provision that requires the business to maintain operations at the project location or another location approved by the Committee for at least 150% of the term of the grant and a provision to permit the Committee to recapture all or part of the grant at its discretion if the business does not remain at the site for the required term.

(11) A provision that requires the business to maintain employment levels in this State at the level of the year immediately preceding the base years.

(12) A provision establishing the conditions under which the grant agreement may be terminated and grant funds recaptured by the Committee.

(13) A provision stating that unless the agreement is amended or terminated the agreement is binding and constitutes a pledge and a continuing appropriation of the amount of the grant.

(14) A provision setting out any allowed variation in terms of the agreement that will not subject the business the business to amendment or termination of the agreement.

(15) A provision that prohibits the business from manipulating or attempting to manipulate employee withholdings with the purpose of increasing the amount of the grant and that requires the Committee to terminate the agreement and take action to recapture grant funds if the Committee finds that the business has manipulated or attempted to manipulate withholdings with the purpose of increasing the amount of the grant.

(16) A provision requiring that the business engage in fair employment practices as required by State and federal law and that the business endeavor to use small contractors, minority contractors, physically handicapped contractors, and women contractors whenever practicable in the conduct of its business.

(17) A provision requiring that the business give priority consideration to hiring North Carolina residents.

A community economic development agreement may contain the following:

(1) A provision setting out allowed variation in the terms of the agreement that will not subject the business to amendment or termination of the agreement

(2) A provision that allows the Committee to consider entering into an additional agreement with the business within five years after the execution of the agreement regardless of whether the program is still in effect at that time if all of the following conditions are met:

a. The business's decision to locate in North Carolina is contingent upon the ability to have a later project considered for a grant.

b. The later project is described in detail in the agreement. This description must include the nature of the additional project, the anticipated investment and new jobs associated with the later project, the anticipated location of the later project, the anticipated wage of the new jobs, and the relationship of the later project to the business's current project.

c. The later project will create at least 75 new jobs in counties currently designated as enterprise tier one, two, or three areas, or 150 new jobs in counties currently designated as enterprise tier four and five areas.

If the current program is still in effect at the time the business applies for a grant for the later project, the business must apply for a grant as it exists at that time. If the current grant program is no longer in effect at the time the business applies for a grant for the later project, the business must apply for a grant according to the provisions of the grant program as it existed immediately before it was repealed or otherwise became ineffective.

No later than February 1 of each year, for the preceding grant year, every business that is awarded a grant shall submit to the Committee a copy of its State and federal tax returns showing business and nonbusiness income and a report showing withholdings as a condition of its continuation in the grant program. In addition, the business shall submit to the Committee an annual payroll report showing the eligible positions that are created during the base years and the new eligible positions created during each subsequent year of the grant. When making a submission under this section the business must pay the Committee a fee of $1,500. The fee is due at the time the submission is made. The Committee shall determine the allocation of the fee imposed by this section among the agencies responsible for evaluating the submission. The proceeds of the fee are receipts of the agency to which they are credited.

The Committee may require any information that it considers necessary to effectuate the provisions of this program. The Committee may audit any business receiving a grant at any time.

If the business receiving a grant fails to meet or comply with any condition or requirement set forth in an agreement or with criteria developed by the Committee, the Committee may amend the agreement to reduce the amount of the grant or the term of the agreement. The reduction of the grant is applicable to the grant year immediately following the grant year in which the Committee amends the agreement.

If a business fails to maintain employment at the levels stipulated in the agreement or otherwise fails to comply with any condition of the agreement for any two consecutive years, the Committee may terminate the agreement.

A qualifying business may receive an annual disbursement of a grant only after the Committee has certified to the State Controller that the business has met the terms and conditions of the agreement. No amount shall be disbursed to a business as a grant under this program in any year until the Secretary of Revenue has certified to the Committee the amount of withholdings received in that year by the Department of Revenue from the business. A qualifying business that has met the terms of the agreement shall make an annual certification of this to the Committee. The Committee shall verify this information and certify to the State Controller that the terms of the agreement have been met. The Committee shall further certify to the State Controller the amount of a grant for which the business is eligible under the agreement and the amount of a grant for which the business would be eligible under the agreement without regard to the 25% grant reduction in Tiers 4 and 5. The State Controller shall remit a check to the business in the amount of the certified grant amount within 90 days of receiving the certification of the Committee.

At the time the State Controller remits a check to a business, the State Controller shall transfer to the Utility Account of the Industrial Development Fund an amount equal to the amount certified by the Committee as the difference between the amount of the grant and the amount of the grant for which the business would be eligible without regard to the 25% reduction for Tiers 4 and 5.

In developing criteria for the awarding of grants and for determining the percentage upon which the amount of a grant is based, the Economic Investment Committee shall consider criteria that address the following:

(1) Economic impact of the project.
   a. Impact on gross regional product and gross State product.
   b. Costs and benefits of the project to the State, including the expected return on investment made in the project by the State.
   c. Number of direct jobs that will be created by the project, the wages of those jobs, and the total payroll for the project.
   d. Number of induced short-term, project-related jobs expected to be generated by the project as well as the number of long-term permanent jobs expected to be generated indirectly in the economy as a result of the project.

e. Dollar value of the investment, including the size of the investment in real versus personal property and expected depreciation rates.
f. Economic circumstances of the county and region, including the extent to which the project will serve to mitigate unemployment.
g. The expected time frame during which the project is expected to pay back in State tax revenues the amount of any grants to be paid out.
h. The economic demands the project is expected to place upon the community or communities in which it will locate.
i. The number of eligible positions that would be filled by residents of development zones.

(2) Strategic importance of the project to the State, region, or locality.
a. The extent to which the project builds or enhances an industrial cluster.
b. The extent to which the project falls within a classification of business and industry that the Department of Commerce regards as a target for growth and expansion in the State.
c. The ability of the project to attract follow-on investment in the State by suppliers and vendors.
d. The extent to which the project serves to maintain and grow jobs in the State in a business undergoing an internal restructuring or rationalization process.
e. The extent to which the project can be expected to contribute significantly to and support the local community.

(3) Quality of jobs.
a. The wage level and status of the jobs to be created.
b. The quality and value of benefits offered by the company.
c. The potential for employee advancement.
d. The extent of training programs offered by the company.
e. The sustainability of the jobs in the future.
f. The workplace safety record of the company.

(4) Quality of the industry and the project.
a. The nature of the project and the projects' relationship to the larger business of the company.
b. The nature of the industrial classification of the project and the nature of the business of the company undertaking it.
c. The long-term prospects for growth at the project site or sites.
d. The long-term prospects for growth of the company and the industry within the United States.
e. The financial stability of the company associated with the project.

(5) Environmental impact of the project.
a. The nature of the business to be conducted.
b. The ability of the project to satisfy State, federal, and local environmental law and regulations.

The bill also makes two changes to the Industrial Development Fund (IDF) and to the Utility Account, which is part of that Fund. The IDF provides assistance to local governments for improvements to infrastructure to enable the locality to attract new businesses. Usually, this assistance is provided to make general improvements, such as improvements to or development of industrial parks, and is not tied to luring a specific project.

The first change is to expand the purposes for which funds in both the Fund and the Account may be used to allow expenditures for telecommunications and high-speed broadband lines and equipment. In addition, the bill would expand the focus of the Utility Account to allow funds to be used to assist local governments in enterprise Tier 3 as well as Tiers 1 and 2 (current law).

The provisions dealing with the job development investment grant are effective when the bill becomes law.

ASSUMPTIONS AND METHODOLOGY:

Bill Lee Act Changes. The fiscal impact estimates for the proposals modifying the Bill Lee Act are based on a sampling of 1999 tax returns filed by businesses reporting or claiming Lee Act credits. The sampling was carried out by the Department of Commerce, based on a universe of 566 firms claiming credits, and was based on scientific methodology. The actual sample size represented 39% of the firms. Since some firms in the sample had facilities at two or more sites, there were a total of 260 locations included in the sample.

Job Development Investment Grant. This initiative represents a significant change from the structure of the Bill Lee Act incentives. Eligibility language in the bill leaves the determination to the Economic Investment Committee. This committee will have broad discretion to negotiate the terms of an agreement, including the amount of the grant and the number of years for which the grant is provided. This makes it impossible to determine the dollar cost of the grant program, even with the limitation of 25 projects during any state fiscal year.

In lieu of an actual projection, the Department of Commerce developed a simulation of the impacts under a specific set of assumptions. The first step in the model was a discussion with industrial recruitment personnel within Commerce. This discussion suggested approximately 140 prospects per year. Of this amount it was assumed that about 70 would be new projects of interest under the program. The next step was to assume 30 would qualify for a grant, with 22 of the projects resulting in an actual agreement. Of this total, 10 units would be located in Tiers 4 and 5 and the remaining 12 projects would be allocated equally to Tiers 1 through 3. For the new jobs in Tiers 4 and 5, an average salary of $40,000 was used. The salary amount for Tiers 1 through 3 was $30,000. The model assumed that withholding taxes would amount to 6% of total salary. Each project was based on 200 employees. Annual salary growth of 4% was used by Fiscal Research in lieu of the 3% rate in the Commerce simulation. The term of the grant was assumed to be 10 years. Finally, the analysis used the maximum 75% grant in the calculation.

Job Development Investment Grant ($Million)				
State Fiscal Year	**Withholding Tax Collected**	**Amount Retained By General Fund**	**Amount Retained By Taxpayer**	**Rural Infrastructure Allocation**
03-04	9.48	2.37	6.17	.94
04-05	19.53	4.89	12.73	1.91
05-06	30.22	7.55	19.75	2.92
06-07	31.42	7.85	20.50	3.04
07-08	32.68	8.17	21.35	3.16
08-09	34.00	8.49	22.23	3.28
09-10	35.34	8.83	23.10	3.41
10-11	36.79	9.19	24.01	3.59
11-12	38.27	9.55	25.03	3.69
12-13	39.81	9.94	26.03	3.84
13-14	27.36	6.83	17.92	2.61
14-15	14.10	3.53	9.24	1.33

SOURCES OF DATA:

TECHNICAL CONSIDERATIONS:

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