Quarterly Revenue Report
Q4 FY 2017-2018 (April – June)

Prepared by:
Caitlin Saunders, Research Strategist
ABOUT THIS DOCUMENT

The League’s quarterly Revenue Reports provide a state-level update on tax revenues collected by the state that are returned to local governments throughout the year. These include a portion of local option sales and use taxes, utility sales taxes (on electricity, piped natural gas, telecommunications, and local video programming), beer and wine excise tax, and solid waste disposal tax. These taxes are distributed to municipalities throughout the year according to formulas outlined in state law. For more information on the different types of state-collected local taxes and distribution formulas, see the League’s “State-Collected Local Taxes: Basis of Distribution” memo.

WHAT’S NEW THIS QUARTER?

The following NC Department of Revenue (DOR) data was released since the League’s last Revenue Report in June:

<table>
<thead>
<tr>
<th>Distribution Data</th>
<th>From Sales Period</th>
<th>Distribution Received</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales &amp; Use Tax¹</td>
<td>April, May, &amp; June, 2018</td>
<td>July, August, &amp; Sept. 2018</td>
</tr>
<tr>
<td>Utility Sales Tax</td>
<td>April, May, &amp; June, 2018</td>
<td>September 2018</td>
</tr>
<tr>
<td>Solid Waste Tax</td>
<td>April, May, &amp; June, 2018</td>
<td>August 2018</td>
</tr>
</tbody>
</table>

Based on this data, the following table summarizes our analysis of statewide trends for the third quarter of local governments’ 2017-2018 fiscal year:

<table>
<thead>
<tr>
<th>Revenue Source</th>
<th>Quarter 4 Compared to Last Year</th>
<th>FY17-18 Compared to Last Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales &amp; Use Tax</td>
<td>+8.9%</td>
<td>+5.5%</td>
</tr>
<tr>
<td>Sales &amp; Use Tax Refunds</td>
<td>-49.1%</td>
<td>-11.1%</td>
</tr>
<tr>
<td>Natural Gas Sales Tax</td>
<td>+25.7%</td>
<td>+27.8%</td>
</tr>
<tr>
<td>Electricity Sales Tax</td>
<td>+2.5%</td>
<td>+1.5%</td>
</tr>
<tr>
<td>Telecommunication Services Sales Tax</td>
<td>-6.1%</td>
<td>-8.3%</td>
</tr>
<tr>
<td>Video Programming Sales Tax</td>
<td>-4.8%</td>
<td>-2.6%</td>
</tr>
<tr>
<td>Solid Waste Tax</td>
<td>-10.5%</td>
<td>+0.2%</td>
</tr>
</tbody>
</table>

¹ Distributions received are generally representative of sales three months prior, and were collected by DOR two months prior. Based on state accounting guidelines, the League assumes that revenues are accrued for 90 days. Please refer to memo #1015, “Recognition of Sales Tax and Other Revenues at Year-End,” issued by the LGC on March 31, 2004, for further details and guidance.
LOCAL GOVERNMENT SALES & USE TAXES

Of the taxes distributed to local governments by DOR, sales and use taxes make up the largest amount of revenue received. Local sales taxes are divided into different Articles, though not all are levied by every county. This report focuses only on Article 39 sales tax distributions. Article 39 tax is charged in every locale and distributed to counties based on where the Article 39 sale occurred. Because of this, Article 39 sales tax revenue trends perhaps best reflect the general trends in local government sales tax revenue.

Compared to last year, fourth quarter Article 39 sales and use tax revenue was 8.9 percent higher, and 5.5 percent higher for the entire fiscal year. This quarter’s increase was enhanced by a 49.1 percent decrease in quarter four sales tax refunds, compared to last year. During the entire fiscal year, there has been a 11.1 percent decrease in sales tax refunds issued, compared to last year.

May collections (April sales), June collections (May sales), and July collections (June sales) were all higher than the same months last year. Overall, 57 counties experienced a sales tax distribution increase equal to or greater than 6 percent, with 88 counties overall seeing growth. On the other hand, 12 counties experienced a decrease in sales tax revenue for the fourth quarter compared to last year. For the entire fiscal year, 93 counties experienced growth in their Article 39 sales tax distribution, compared to last year.

The two charts below show year-over-year comparisons of Article 39 sales tax distributions and sales tax refunds each month. The solid line represents the percent change from the same month in the previous fiscal year. The columns represent the totals each month.
Taxable sales in North Carolina fluctuate widely throughout the year but have been steadily increasing since 2010. At the end of Quarter 4, the 12-month moving average of taxable sales was $12.18 billion – 55 percent higher than its lowest point in February 2010 ($7.85 billion). However, the rate of increase has begun to slow.
Taxable sales have grown in all business type categories. The largest proportion of taxable sales occur in the General Merchandise, Unclassified, and Food business types. See Attachment A for more detail on what business types are included in these categories.

**Taxable Sales By Business Group**

<table>
<thead>
<tr>
<th>Business Type</th>
<th>12-Month Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>Apparel</td>
<td>12bn</td>
</tr>
<tr>
<td>Automotive</td>
<td>10bn</td>
</tr>
<tr>
<td>Furniture</td>
<td>8bn</td>
</tr>
<tr>
<td>Food</td>
<td>6bn</td>
</tr>
<tr>
<td>General Merchandise</td>
<td>4bn</td>
</tr>
<tr>
<td>Lumber &amp; Building Material</td>
<td>2bn</td>
</tr>
<tr>
<td>Unclassified</td>
<td>2bn</td>
</tr>
</tbody>
</table>

**UTILITY SALES TAXES**

Quarterly, the Department of Revenue distributes sales tax from four separate utilities – electricity, natural gas, telecommunication services, and video programming. During Fiscal Year 2017-18 the proportion of local government utility tax revenue from each source was the following:

**FY17-18 Utility Revenue % From Each Source**

- Electric Power: 69.32%
- Piped Natural Gas: 4.33%
- Telecommunication Services: 9.92%
- Video Programming: 16.43%
The most recent distribution of utility sales taxes occurred on September 17, 2018. The following graph shows the percent change from last year to this year for each quarter’s utility sales tax distributions.

**FY 17-18 Utility Tax Distributions (% Change From Same Quarter Last Year)**

Below is a more detailed summary of each distribution by utility type.

**Electricity**: Local governments received $69,137,410 in electricity sales tax revenue for the fourth quarter of Fiscal Year 2017-18. This is a 2.5 percent increase from the same quarter last year. For the entire fiscal year, revenue from electricity sales tax has increased by 1.5 percent compared to last year. Electricity tax revenue is dependent on the price of electricity and consumer demand. Prices are less volatile, as they are regulated by the NC Utility Commission. Consumption is highly dependent on weather. Both heating degree and cooling degree days were higher during the fourth quarter this year than last year. The number of cooling degree days this fourth quarter were 29 percent higher than the same quarter last year. This is likely the most significant factor driving the increase in electricity tax revenue this quarter. For more discussion on electricity sales tax trends, see the League’s recent "Factors Affecting Electricity Sales Tax Revenue" memo.

**Natural gas**: Local governments received $4,752,954 in natural gas sales tax revenue for the fourth quarter of Fiscal Year 2017-18. This is a 25.7 percent increase from the same quarter last year. For the entire fiscal year, revenue from natural gas sales tax has increased by 27.8 percent. Like electricity, natural gas tax revenue is largely dependent on weather-related consumption and prices. The fourth quarter’s 104 percent increase in heating degree days is likely the main factor driving this quarter’s large increase.

---

2 During the 2014-15 Fiscal Year, the electricity franchise tax was eliminated, and local governments began receiving a percentage of tax on electricity sales instead. Electricity tax revenues remained increased as a result of the change, but remain below their 2015-2016 Fiscal Year peak. 
3 [https://www7.ncdc.noaa.gov/CDO/DivisionalSelect.jsp#](https://www7.ncdc.noaa.gov/CDO/DivisionalSelect.jsp#) 
4 Like the electricity tax revenue, local governments now receive a percentage of tax revenue from the sale of natural gas, rather than the previous franchise tax.
**Telecommunication services:** Local governments received $11,397,681 in telecommunication sales tax revenue for the fourth quarter of Fiscal Year 2017-18. This is a 6.1 percent decrease from the same quarter in the previous year. For the entire fiscal year, revenue from telecommunication services sales tax has decreased by 8.3 percent. Taxes on telecommunication services continue to be negatively impacted by a growing reliance on cell phones in place of land line phone connections.

**Video programming:** Local governments received $18,576,843 in video programming sales tax revenue for the fourth quarter of Fiscal Year 2017-18. This is a 4.8 percent decrease from the same quarter in the previous year. For the entire fiscal year, revenue from video programming sales tax has decreased by 2.6 percent.

**SOLID WASTE DISPOSAL TAX**
Solid waste disposal tax revenue for the fourth quarter of Fiscal Year 2017-18 was 10.5 percent lower than the fourth quarter distribution in Fiscal Year 2016-17. For the entire fiscal year, solid waste disposal tax distributions were only 0.2 percent higher than the previous fiscal year. Until the fourth quarter this fiscal year, distributions had shown year-over-year increases for nine consecutive quarters. The cause of this quarter’s decline is unclear. In North Carolina, the health of the construction industry plays a large part. One indicator may be housing starts, which were down 12 percent this July compared to the same month last year.\(^5\)

---

\(^5\) [https://www.richmondfed.org/~media/richmondfedorg/research/regional_economy/reports/snapshot/pdf/snapshot_nc.pdf](https://www.richmondfed.org/~media/richmondfedorg/research/regional_economy/reports/snapshot/pdf/snapshot_nc.pdf)
ECONOMIC UPDATE

North Carolina’s economic outlook continues to be positive, though with some signs of slowing. Dr. Michael Walden’s August 2018 Index of North Carolina Leading Economic Indicators has continued on its two-year upward trend. The index increased by 0.1 percent from June to July, and is up 1.3 percent from the previous year. One contributing factor is another double-digit gain in building permits, along with a 6 percent drop in jobless claims. These two factors offset decreases in manufacturing hours and manufacturing earnings. Dr. John Connaughton’s September 2018 forecast predicts a 2.8 percent increase in Gross State Product (GSP) in 2019 over the 2018 level, slightly below the 2.9 percent growth forecast from 2017 and 2018. The state unemployment rate has declined even further, from 4.5 to 4.1 percent from January through July. The pace of job creation during the first six months of 2018 has not been seen in NC since the 1990’s, with manufacturing jobs, in particular, making a big gain. In addition, middle-paying jobs, which have seen little growth during most of the 21st century, have grown almost six times faster since 2017, compared to the annual average from 2009 to 2016. Wells Fargo reports a June gain of 13,200 jobs, bringing the annual total to 103,400.

However, the Carolinas Survey of Business Activity for August 2018 reported slowing growth for firms in the Carolinas, with a fall in both business conditions and sales. Firms also predict a slowing in employment growth in coming months and continue to experience a shortage of workers with needed skills. The gap between input prices and prices received continues to grow, despite firms reporting since May that they expect the gap to narrow in the coming months.

A National League of Cities (NLC) survey of 341 city finance officers, released in September, also identifies signs of slowed growth such as slowing housing markets and stagnant wages. Respondents reported that growth in service costs is outpacing the growth in tax revenue – a 1.25 percent growth in Fiscal Year 2017 revenues, compared to 2.16 percent growth in expenditures. However, the report acknowledges that fiscal conditions vary widely in cities across the country, with the Midwestern and smaller cities faring worse than others.

One area where the state is set to experience some revenue growth is the collection of taxes from online retail sales. The Supreme Court’s June 21st ruling on South Dakota v. Wayfair Inc. overturns a system created following the 1992 Quill Corporation v. North Dakota case, and finds that internet retailers can now be required to collect sales tax in states where they have no physical presence. Most of the top e-commerce retailers have a physical presence in North Carolina; therefore, the state already receives most of the possible sales tax from e-commerce. However, a June memo from the NC Department of Revenue states that as a result of South Dakota v. Wayfair Inc., existing statutes should allow DOR to require additional remote sellers to collect and remit. DOR estimates an annual state revenue increase of $75 million, with a corresponding local increase of $35 million, annually.

---

7 https://belkcollege.unc.edu/sites/belkcollege.unc.edu/files/media/0918%20Economic%20Forecast%20Presentation.pdf
8 https://cals.ncsu.edu/news/you-decide-how-is-north-carolinas-economy-at-mid-year/
11 https://www.nlc.org/resource/city-fiscal-conditions-2018
RESOURCES

- Local government revenue distribution data can be found on the N.C. Department of Revenue website.

- Information on economic indicators used in this report can be found in the following locations:
  - Federal Reserve Bank of Richmond
  - Wells Fargo
  - Dr. Michael Walden of N.C. State University
  - Dr. John Connaughton of UNC-Charlotte
ATTACHMENT A – Top Three Business Groups for Taxable Sales in NC

Unclassified Group - 4.75%
701 Beauty and barber shops and supply dealers
702 Bookstores, school supply stores
703 Newsstands
704 Coal, wood, fuel oil, and bottled gas dealers
705 Feed stores, millers, hatcheries
706 Florists and nurseries
707 Airplane dealers
708 Hotels, motels, cottage rentals, etc.
709 Office machine and supply dealers
710 Funeral homes
711 Others
712 Photographers, artists, photofinishers
713 Printers, publishers, blueprinters, engravers, etc.
714 Laundries, dry cleaners, etc.
715 Hospitals, physicians, veterinarians, etc.
716 Boat and marine supply dealers
717 Pet, hobby and craft shops
718 Chemical, janitorial supplies and paper products dealers
719 Machine shops; locksmiths, etc.

General Merchandise Group - 4.75%
501 Department stores
502 Drugstores; drug and medical supply houses
503 Dry goods stores; fabric and yarn shops
504 Farm implement and supply stores
505 Discount stores; general stores
506 Hardware stores
507 Jewelry stores; watch and clock repair shops
508 Leather and leather goods stores
509 Industrial machinery and supply dealers
510 Secondhand goods stores; flea markets
511 Sporting goods stores; toy shops
512 Variety stores; 5 & 10 specialty stores
513 Others
514 Paint, wallpaper, and glass stores
515 Pawn shops; army surplus stores, etc.
516 Road building equipment and supply dealers
517 Gift and novelty shops; coin dealers

Food Group - 4.75%
301 Bakeries
302 Candy and confectionery stores
303 Dairies and dairy bars
304 Grocery stores, meat markets, etc.
305 Vending machine operators; drink stands
306 Restaurants, cafeterias, grills, snack bars, etc.
307 Others
308 Taverns, nightclubs, etc.