

# State-Collected Local Taxes: Basis of Distribution

PREPARED BY THE NORTH CAROLINA LEAGUE OF MUNICIPALITIES -- MARCH 2019

---

## Powell Bill Funds

**Distribution Schedule:** Powell Bill proceeds are distributed twice during the fiscal year, on or before October 1, and on or before January 1. The total amount of these funds distributed to municipalities in FY 18-19 was \$147,392,460.15. This distribution was based on a per mile rate of \$1,600.17 and a per capita rate of \$19.56. *[Background information on Powell Bill and electronic copies of the "State Street Aid Allocations to Municipalities Report" can be found at:*

*<https://connect.ncdot.gov/municipalities/State-Street-Aid/Pages/default.aspx>].*

**Distribution Formula:** Prior to 2015, the overall amount of Powell Bill distributions had been tied to the state's motor fuels tax, with cities receiving a specific portion of revenues derived from that tax. That changed in the 2015 state budget, Session Law 2015-241. Now, G.S. 136-41.1(a) states that Powell Bill revenues will be determined by an appropriation of funds by the General Assembly. There is no set formula that determines the total amount of Powell Bill funds available each year. Of the funds available each year, 25 percent is distributed to cities and towns based on local street miles, and 75 percent based on population. New language in the 2015 budget also specifies that cities must spend their Powell Bill funds "primarily for the resurfacing of streets" (G.S. 136-41.3).

**Background:** The change of Powell Bill funds to a direct appropriation from the State was just the latest change to the Powell Bill program. Previously, the transportation reform legislation passed in 2013 (S.L. 2013-183) changed the source of Powell Bill funds to a percentage of

motor fuel taxes in the State Highway Fund. Previously, out of the gasoline tax, 1 ¾ cents was distributed to cities and towns for street and sidewalk construction and maintenance purposes. In addition, 6.5 percent of Highway Trust Fund net revenues were allocated for Powell Bill. The General Assembly in 2013 chose to provide municipalities with 10.4 percent of motor fuels taxes from the State Highway Fund with the intent that that would be enough to hold all cities and towns harmless from what they were receiving previously.

To receive funds, a municipality must maintain public streets within its jurisdiction that are not part of the State highway system.

There are additional eligibility requirements that differ depending upon when a municipality was incorporated. A municipality incorporated before January 1, 1945 must have:

- conducted an election within the preceding four years, and
- either imposed an ad valorem tax or provided other funds for its operating expenses.

For a city or town incorporated after January 1, 1945, to share in Powell Bill funds, it must certify that [G.S. 136-41.2]:

- it has conducted its most recent required election,
- it has levied at least a five cent ad valorem tax for the current fiscal year,
- it has collected at least 50 percent of the total ad valorem tax levied for the preceding fiscal year, and
- it has formally adopted a budget ordinance showing revenue received from all sources and showing that funds have been appropriated for at least four of the following municipal services: water distribution; sewage collection or disposal; garbage and refuse

collection or disposal; fire protection; police protection; street maintenance, construction or right-of-way acquisition; street lighting; or zoning.

Each municipality receiving funds must file an annual certified street map and an annual expenditure report. [G.S. 136-41.1]. As of 2017, municipalities failing to file an expenditure report will be ineligible to continue to receive Powell Bill distributions. [G.S. 136-41.3(b1)].

Questions may be directed to [PowellBillHlep@ncdot.gov](mailto:PowellBillHlep@ncdot.gov) or (919) 707-2208.

### *Exemption from the State Road Tax on Motor Fuels*

In 2002, the General Assembly eliminated the extra steps and paperwork of applying for a refund of the State Road Tax on Motor Fuels by exempting from the excise tax fuel that is sold to a county or municipality for its use, effective January 1, 2003. If distributors attempt to charge tax on fuel for municipal use, please report this to the Motor Fuels Division at DOR.

## **Electricity Sales Tax**

**Distribution Schedule:** The municipal distributions of the sales tax on electricity gross receipts are on September 15, December 15, March 15, and June 15. The total amount distributed to municipalities during FY 2017-18 was \$318,132,130.18. *[Electronic copies of quarterly reports on the distribution of the sales tax on electricity gross receipts can be found at: [www.dor.state.nc.us/publications/reimbursement.html](http://www.dor.state.nc.us/publications/reimbursement.html)].*

**Distribution Formula:** Effective July 1, 2014, the general sales tax rate is applied to the sale of electricity. From the proceeds of that tax, 44 percent is allocated to be distributed to cities and towns. Each city receives a franchise tax share and an ad valorem share of these proceeds. The franchise tax share is equivalent to the electricity franchise tax distribution that each city received as its quarterly distribution in Fiscal Year 2013-14. If there is insufficient revenue to provide each municipality with the same distribution that it received in FY13-14, then every municipality's distribution will be reduced proportionally. If there is excess sales tax

revenue after distributing every municipality's franchise tax share, then each municipality will receive an ad valorem share. The excess sales tax revenue will be distributed based on each city's ad valorem taxes levied as a percentage of all cities' ad valorem taxes levied. [G.S. 105-164.44K].

**Background:** The distribution formula described above was passed as part of the tax reform legislation approved by the General Assembly in 2013 (S.L. 2013-316). It first went into effect for Fiscal Year 2014-15. Previously, the state levied a 3.22 percent franchise tax on the total gross receipts of all businesses within the State that furnish electricity. An amount equal to 3.09 percent of the total gross receipts of electricity service derived from the sale within any municipality was distributed to the municipality in which these gross sales are made. [G.S. 105-116, now repealed].

During the 1990 session, the General Assembly converted the utility franchise tax distribution from an automatic reserve for local governments to an annual appropriation by the legislature. In 1991, the Legislature froze all growth in the franchise tax.

During the 1993 session, the Legislature removed the utility franchise tax from the annual appropriation process and returned it to an automatic distribution with normal growth, effective in FY 1995-96. The state retains forever the amount of growth in the franchise tax from FY 1990-91 through FY 1994-95 (approximately \$30,000,000) and deduct it from the amount due local governments.

This retained growth, or holdback, is calculated separately for each municipality by subtracting each city's FY 1990-91 Utility Franchise Tax collections from those in FY 1994-95. In calculating quarterly distributions, this annual figure is divided by the state into four, equal quarterly holdback amounts and subtracted from actual collections before distribution to each city [G.S. 105-116(d) and G.S. 105-120(c)].

The lifting of the freeze meant that the distributions of these revenues was again based on actual utility franchise tax collections within each city's limits. It is important to remember

that there are significant local variations in revenues and significant differences from city to city in the amount of holdback from the state, due to variations in each city's prior franchise tax growth rate.

Any local utility rate increases or decreases approved during the year, local variations in the weather, annexations, and losses or gains of industrial or other facilities that are heavy users of electric service during the fiscal year could cause individual city receipts to differ from the statewide average growth rate.

Legislation passed during the 1997 session made adjustments to the holdback amounts for those cities and towns that received in FY 1995-96 less than 95 percent of the amount of utility franchise tax they got in FY 1990-91. It also provided for the proportionate cost to the Department of Revenue of administering the distribution to be subtracted from each city's distribution [G.S. 105-114(b), -116, -116.1, -120].

Legislation passed during the 2000 session amends G.S. 105-116.1 to provide an additional limited hold-harmless adjustment of utility franchise tax distributions to cities that in 1995-96 received less than 60 percent of the amount they received from such taxes in 1990-91. It applies to distributions on or after October 1, 2000.

## Piped Natural Gas Sales Tax

**Distribution Schedule:** Distributions of the municipal portion of the sales tax on piped natural gas are made on September 15, December 15, March 15, and June 15. The total amount distributed to municipalities during FY 2017-18 was \$19,891,817.85.

*[Electronic copies of quarterly reports on the distribution of the piped natural gas excise tax can be found at:*

[www.dor.state.nc.us/publications/reimbursement.html](http://www.dor.state.nc.us/publications/reimbursement.html)].

**Distribution Formula:** Effective July 1, 2014, the general sales tax rate is applied to the sale of piped natural gas. From the proceeds of that tax, 20 percent is allocated to be distributed to cities and towns. Each city receives an excise tax share and an ad valorem share of these proceeds. The excise tax share is equivalent to the distribution

of the excise tax on piped natural gas that each city received as its quarterly distribution in Fiscal Year 2013-14. If there is insufficient revenue to provide each municipality with the same distribution that it received in FY13-14, then every municipality's distribution will be reduced proportionally. If there is excess sales tax revenue after distributing every municipality's excise tax share, then each municipality will receive an ad valorem share. The excess sales tax revenue will be distributed based on each city's ad valorem taxes levied as a percentage of all cities' ad valorem taxes levied. [G.S. 105-164.44L].

**Background:** The distribution formula described above was passed as part of the tax reform legislation approved by the General Assembly in 2013 (S.L. 2013-316). It first went into effect for Fiscal Year 2014-15. Previously, in 1998, the General Assembly replaced the utility franchise tax and sales and use tax on piped natural gas with a new excise tax on piped natural gas. Rates were based on monthly therm (a unit of heat) volumes received by the end-user of the gas.

The law provided for the quarterly distribution of part of the tax proceeds to cities, with each city receiving one-half of the amount of the new tax attributable to customers within that city's municipal boundaries for the quarter. It required the Secretary of Revenue to determine each city's "benchmark amount" (amount of the utility franchise tax attributable to piped natural gas the city received for the corresponding quarter in FY 1998-99) and provided that the amount distributed to a city under the new tax may not exceed the city's benchmark amount until each city receives its benchmark amount. The tax provisions of the law were effective July 1, 1999 and applied to natural gas delivered on or after that date. [G.S. Chapter 105, Article 5E; G.S. 105-116, -116.1, -122, -164.3 (25), -164.4(a), -164.13, -164.20, -259(b); G.S. 160A-211].

## Telecommunications Sales Tax

**Distribution Schedule:** The municipal distributions of the sales tax on telecommunications gross receipts are on September 15, December 15, March 15, and June 15. The total amount distributed to municipalities during FY

2017-18 was \$45,510,007.64. *[Electronic copies of quarterly reports on the distribution of sales tax on telecommunications gross receipts can be found at:*

[www.dor.state.nc.us/publications/reimbursement.html](http://www.dor.state.nc.us/publications/reimbursement.html)]

**Distribution Formula:** Legislation passed during the 2001 session repealed the utility franchise tax on telephone companies and replaced it with a sales tax on telecommunications of 6 percent (now 8.0 percent) of gross receipts. Included in gross receipts are receipts from local, intrastate, interstate, toll, private, and mobile telecommunications services; charges for directory assistance, call forwarding, call waiting, and similar services; customer access line charges billed to subscribers for access to the intrastate or interstate inter-exchange network; and charges billed to a pay telephone provider who uses the telecommunications service to provide pay telephone service [G.S. 105-164.3, -164.4, -164.4B, -164.16, -164.20, -164.27A, -164.44F].

The amount of the tax the Secretary of Revenue must distribute quarterly to municipalities is currently 18.7 percent of the net proceeds of the tax, minus \$2,620,948. (This deduction is 1/4 of the annual amount by which the distribution to cities of the franchise tax on telephone companies was required to be reduced beginning in FY 1995-96 as a result of the "freeze deduction.")

Cities incorporated before January 1, 2001, receive a proportionate share of the amount to be distributed to all cities incorporated before that date. The quarterly share is based on the amount of telephone gross receipts franchise taxes attributed to the city under G.S. 105-116.1 for the same quarter that was the last quarter in which taxes were imposed on telephone companies under repealed G.S. 105-120 (franchise or privilege tax on telephone companies).

The share for a city incorporated on or after January 1, 2001 is its per capita share of the amount to be distributed to all cities incorporated on or after that date. That amount is the proportion of the total to be distributed that is the same as the proportion of the population of

cities incorporated on or after January 1, 2001 compared to the population of all cities.

**Background:** In 2005, the General Assembly set the State rate of tax on the gross receipts derived from providing telecommunications service at the combined general rate, which is defined in G.S. 105-164.3(4a) as "the State's general rate of tax . . . plus the sum of the rates of the local sales and use taxes."

As State and local tax rates change, the percentage of the net proceeds on which the municipal distribution is based also changes in order to keep the municipal share revenue neutral. The rate currently is 18.7.

## Local Video Programming Tax

**Distribution Schedule:** The municipal distributions of the local video programming revenues are on September 15, December 15, March 15, and June 15. The total amount distributed to municipalities during FY 2017-18 was \$75,380,558.58. *[Electronic copies of the annual reports on the distribution of video programming taxes can be found at:* [www.dor.state.nc.us/publications/reimbursement.html](http://www.dor.state.nc.us/publications/reimbursement.html)].

**Distribution Formula:** To replace the local cable franchise fee revenues that were lost when the State took over the franchising of video programming, G.S. 105-164.44I requires the NC Department of Revenue to distribute part of the state sales tax collected on video programming and telecommunications services to counties and cities on a quarterly basis. Local governments receive 23.6 percent of the sales tax collections from video programming service, an additional 7.7 percent of the existing telecommunications sales tax, and 37.1 percent of sales tax collections on satellite television service.

Each city's proportionate share of these new revenues is the base amount for that city compared to the base amount for all other cities and counties. The base amount of a city or county that imposed a cable franchise tax before July 1, 2006 is the amount of cable franchise tax and Public, Educational, and Governmental (PEG) channel subscriber fee revenue the unit certified in 2007 to DOR that it had imposed

during the first six months of the 2006-07 fiscal year. The base amount for a city or county that did not impose a cable franchise tax before July 1, 2006, is \$2 multiplied by the most recent annual population estimate for that unit.

For subsequent fiscal years, the Secretary must multiply the amount of a city's or county's share for the preceding year by the percentage change in its population for that fiscal year and add the result to the city or county's share for the preceding fiscal year to obtain the county's or city's adjusted amount. Each city or county's proportionate share for that year is its adjusted amount compared to the sum of the adjusted amounts for all counties and cities.

These funds may be used for general public purposes, with one exception. A city or county that imposed subscriber fees in fiscal year 2006-07 for the operation and support of PEG channels must use the video programming funds distributed to it for support of PEG channels in the same proportion as the subscriber fees were of total franchise and tax and subscriber revenue during the first six months of the 2006-07 fiscal year.

**Background:** During the 2006 session, the General Assembly designated the North Carolina Secretary of State as the exclusive franchising authority in the state for cable service provided over a cable system. The state franchise for cable service authorizes the holder of the franchise to construct and operate a cable system over public rights-of-way within the area to be served.

The Act eliminated county and city authority to award or renew a franchise for cable service as of January 1, 2007. It specified that the new provisions do not affect existing local franchise agreements except as follows:

1. Effective January 1, 2007, gross revenue used to calculate the payment of the franchise tax imposed by G.S. 153A-154 or G.S. 160A-214 no longer includes gross receipts from cable services that are subject to sales tax on video programming under G.S. 105-164.4, which applies the existing state general sales tax rate to gross receipts derived from video programming service to a subscriber in the state. (The Act defines video programming to include all

programming provided by, or generally considered comparable to programming provided by, a television broadcast station, regardless of the method of delivery.) Local cable franchise taxes/fees on those components of local franchise agreements' (LFA) definitions of "gross revenues" that are not subject to the state sales tax on video programming can continue to be collected.

2. A cable service provider under an existing agreement may terminate the agreement when one of a specific series of conditions is met.

**PEG Channel Supplemental Funding:** The Secretary of Revenue must include the applicable amount of supplemental PEG channel support in each quarterly distribution to a city or county. The amount of money distributed for PEG channels may not exceed \$4 million in a fiscal year. Each certified channel receives an equal share of the funding. A city or county must certify to the Secretary by July 15 of each year the number of qualifying PEG channels it operates, and it may not receive PEG channel support for more than three qualifying PEG channels. For FY 2018-19, the amount per channel was roughly \$27,027.04. Supplemental PEG channel funds can only be spent on PEG channels, and the total amount of PEG support received by a municipality must be allocated equally among its PEG channel operators.

## Alcoholic Beverage Tax

**Distribution Schedule:** The distribution of alcoholic beverage taxes is within 60 days of March 31. The amount distributed to municipalities in FY 2017-18 was \$38,859,776.74.

*[Electronic copies of the annual reports on the distribution of beer and wine taxes can be found at:*

[www.dor.state.nc.us/publications/reimbursement.html](http://www.dor.state.nc.us/publications/reimbursement.html)]

**Distribution Formula:** G.S. 105-113.82 provides for the distribution of 20.47 percent of state beer tax collections to local governmental units in which beer is legally sold. It further provides for the distribution of 49.44 percent of the state tax collections for taxes on unfortified wine and 18 percent of collections for taxes on

fortified wine to local governmental units in which wine is legally sold. Funds are distributed among local governments on a per capita basis. These distributions use incorporated municipal populations and the unincorporated population of counties to determine their respective per capita shares.

## Local Option Sales and Use Taxes

**Distribution Schedule:** All 100 counties levy the Article 39, 40, and 42 local option taxes, which are distributed monthly. The total municipal and county allocation for FY 2017-18 from the Department of Revenue for these taxes was \$2,965,271,613.26. G.S.105-501 allows new municipalities (incorporated with an effective date of on or after January 1, 2000) to participate in the sales tax distribution if they are not disqualified from receiving funds under G.S. 136-41.2 (Powell Bill) and a majority of their street mileage is open to the public. *[Electronic copies of the annual reports on the distribution of sales taxes can be found at: [www.dor.state.nc.us/publications/reimbursement.html](http://www.dor.state.nc.us/publications/reimbursement.html)]*

### **Article 39 One Percent Local Government Sales Tax (1971)**

Article 39 of Chapter 105 of the General Statutes provides that the county commissioners may, either upon their own action or upon the approval of the voters, levy a 1 percent local government sales tax along with the State sales and use tax at the general State rate. All 100 counties levy the tax.

The act further provides for the allocation of all the local sales taxes to the county of origin, but collected and administered by the Secretary of Revenue. In 2001, SB144, *Streamlined Sales/Use Tax Agreement*, changed the rule for determining the source of sale for a product. The distribution of this tax is now on a **point of delivery basis**, with most sales “delivered” within the county (in the store) in which the sales take place. However, for certain types of products, especially furniture, which are purchased in one county for delivery in another, there could be a shift in sales tax revenues away from a limited number of counties.

The division of the proceeds among a county and its municipalities is on one of two bases, depending upon the method chosen by the county commissioners when they levy the tax.

### **County Sales Tax Distribution Methods**

Every April, counties can change the method of distributing local option sales tax revenues within the county: from per capita to the proportion of ad valorem tax levies or the other way around. The method chosen by the county board of commissioners determines the division of money within a county area among county and municipal governments for the next year. Population or tax levy changes might make some counties take a close look at the distribution method they now use to see if it is still advantageous to them. A change made in April is effective for the distribution made in July.

**Population Distribution.** The county commissioners may choose to distribute the proceeds between the county and the municipalities on a population basis. After adding the total population of the county (incorporated and unincorporated) to the population of each municipality, the distribution of the tax to each unit is on a per capita basis. For distributions based on the proportional populations of the units, a large annexation by one city, effective by July 1, may distort the next year’s allocations. The population figure is the most recent estimate of population as certified to the Secretary of Revenue by the State Budget Officer.

**Ad Valorem Distribution.** The commissioners may choose to distribute the net proceeds of the tax collected in their county on an ad valorem basis. If they choose this method, the proceeds must be divided between the county and the municipalities in proportion to the total amount of ad valorem taxes levied by each. Therefore, a large tax increase by a unit in one year may distort the next year’s allocations. When a county increases tax rates each year and the cities in that county hold the line on tax increases or keep increases at a minimum, it is possible for municipalities in ad valorem distribution counties to find that not only are their sales tax revenues not increasing at the statewide average, but that they are lower than the previous year.

For the purposes of this type of distribution, the amount of the ad valorem taxes levied by the county or municipality includes any ad valorem taxes levied by the county or municipality on behalf of a taxing district or districts (such as fire or sanitary) and collected by the county or municipality. If the county employs this basis, a municipality or county must share the proceeds with any district or districts on behalf of which the county or municipality levied ad valorem taxes in the proportion that the district levy bears to the total levy of the county or municipality.

#### ***Article 40 Supplemental ½ Percent Local Government Sales Tax (1983)***

The 1983 General Assembly gave each county authority to levy an additional ½ percent local option sales tax [Article 40, G.S. Chapter 105]. All 100 counties levy the tax.

The procedures for levy and collections are the same as for the original local option sales tax. However, the distribution of net proceeds is on a per capita basis among the counties that have levied the tax, instead of on a point-of-delivery basis. Once allocated to a county, the distribution of the funds among the county and its municipalities is under the same formula selected for use by that county under the original sales tax.

#### ***Article 42 Additional ½ Percent Local Government Sales Tax (1986)***

The 1985 General Assembly (1986 Regular Session) authorized counties to levy a second ½ percent local option sales tax, with an effective date not earlier than September 1, 1986 [Article 42, G.S. Chapter 105]. The distribution of net proceeds originally was on a per capita basis. In 2007, the General Assembly passed legislation to change the distribution for the Article 42 local option sales tax from per capita to point of delivery distribution, effective October 1, 2009.

Funds are deducted from the proceeds of the second ½ percent local option sales tax before distribution to cities and counties to pay for the following State functions that support local governments:

- the DOR Local Government Division,
- the Property Tax Commission,

- the Institute of Government's Property Tax Training Programs, and
- Operations of the Local Government Commission.

#### ***City Hold Harmless (Article 44 Replacement)***

**Background:** The 2001 General Assembly gave each county authority to levy a third ½ percent local option sales tax [Article 44, G.S. Chapter 105]. Food was exempted from this new tax.

In 2007, the General Assembly passed legislation to have the State assume county Medicaid costs, eliminate the Article 44 local sales tax, and raise the State tax rate commensurately (G.S. 105-164.4, -269.14, -472, -501, 520, -521, -522, -523; G.S. 108A-54). Effective October 1, 2008, the state took over ¼ cent of the Article 44 local option sales tax and effective October 1, 2009, the state took over the remaining ¼ cent of that local tax. Because the assumption of Medicaid costs did not benefit municipalities, the 2007 legislation provided for municipalities to be completely reimbursed for the loss of Article 44 taxes through a "City Hold Harmless" payment.

**Distribution Schedule:** The City Hold Harmless is calculated and distributed monthly and is equal to 150 percent of the non-food sales and use tax revenue allocated to the municipality under Article 40 for the month, minus 25 percent of the amount of non-food sales and use tax revenue allocated under Article 39 for the month. The payment is calculated to compensate for both the loss of the Article 44 tax and the change in the distribution of the Article 42 from per capita to point of delivery distribution. The City Hold Harmless payment ensures that neither change reduces the amount of revenue that any municipality will receive.

Funds for the City Hold Harmless payments come from the counties' share of monthly sales tax revenues, but the Department of Revenue makes payments directly to municipalities. There is no expiration date on the City Hold Harmless payments.

***Article 44 Additional Sales Tax Revenue  
for Economic Development, Public  
Education, and Community Colleges  
(2015)***

The 2015 state budget, Session Law 2015-241, established a “distribution of additional sales tax revenue for economic development, public education, and community colleges” in Article 44 under G.S. 105-524. As of April 1, 2016, the distribution was scheduled to work as follows:

Annually, a total of \$84.8 million would be deducted proportionally from sales tax revenues derived from Articles 39, 40, and 42, in 12 equal installments over the fiscal year. This \$84.8 million would be distributed to counties based on percentages specified in G.S. 105-524(c). Each month, one-twelfth of that amount would be distributed to counties with 50 percent of the funds being distributed under Article 39, 25 percent under Article 40, and 25 percent under Article 42.

G.S. 105-524(c) specifies that a “county must use the revenue it receives under this section for economic development, public education, and community college purposes,” although it does not specifically reference cities. The \$84.8 million reallocated under this article is scheduled to increase annually by the same amount as total local sales tax collections increased, beginning in July 1, 2017. The amount reallocated in FY2017-18 will be roughly \$90.7 million.

***Accruing Monthly Sales Tax Distributions***

The distribution of local option sales tax proceeds changed from quarterly to monthly in 2003, which created an inconsistency in the way the September 15<sup>th</sup> distribution was being treated from an accounting perspective. The September 15 distribution is for taxes collected by the Department of Revenue on sales made in June. Because the sales were in June, the September distribution should be accrued to the fiscal year ending in June.

The inconsistency results because September falls beyond the 60-day period that most units have used for determining if revenues are available for accrual at year end in General Fund

statements. The continued use of a 60-day period would have resulted in units recording less than 12 months of sales tax revenue in the 2003-04 fiscal year. The use of a 60-day period would also have resulted in different revenue amounts between general fund and government-wide statements.

To solve this problem, the Local Government Commission (LGC) encourages the use of a 90-day period for determining if revenues are available. By extending the accrual period from 60 to 90 days, the September 15 distribution can be properly accrued to the prior fiscal year. This meets GASB 33 measurement focus requirements and results in prior period adjustments only if the amounts are material. 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.

[\[https://www.nctreasurer.com/slg/Memos/1015.pdf\]](https://www.nctreasurer.com/slg/Memos/1015.pdf)

*l*

***Two Percent Local Government Sales Tax  
on Food***

The 2003 session of the General Assembly passed legislation that provides for the administration of local sales taxes on food as if they were state taxes. (Food is taxed under the Article 39, 40, and 42 sales and use taxes, but not under the Article 44 tax.) This was done to prevent any distortions in local sales tax distributions as North Carolina met the requirement of the national sales tax streamlining project to have a uniform tax rate on food. The sales tax streamlining project is designed to help capture sales tax revenue currently lost with remote (Internet and mail order) sales.

One-half of the net proceeds of local sales taxes on food are allocated among counties on a per capita basis. The remaining net proceeds are distributed to each county based on the county’s proportion of the FY 1997-98 Article 39 distribution of the tax on food, the last year in which the separate distribution of the food tax to county areas was known.

In 2005, the General Assembly changed the statute to clarify that one-half of the per capita amount of the local sales taxes on food is



included in the distribution for the first one-half percent local tax [Article 40] and the other one-half is in the distribution for the second one-half percent local tax [Article 42]. This method of distribution was not altered when the Article 42 tax changed to a point of sale distribution.

### ***Local Government Public Transportation Sales Tax (1997)***

The 1997 General Assembly gave Mecklenburg County authority to levy an additional ½ percent local option sales and use tax, the proceeds of which are to be used only for financing, constructing, operating, and maintaining local public transportation systems [Article 43, G.S. Chapter 105]. The distribution of the funds among the county and its municipalities that operate public transportation systems is per capita.

### ***Refunds of Sales and Use Tax***

In 1991, the General Assembly authorized state agencies to get a refund of local government sales taxes, just as local governments have long enjoyed a refund of the state sales tax. In 2003, the General Assembly exempted state agencies from paying local sales taxes on direct purchases of tangible personal property and services [G.S. 105-164.14(e)]. The change from refund to exemption has administratively simplified the process and reduced agency and Department of Revenue costs.

During the 1998 session, the General Assembly added local school administrative units to the list of governmental entities that may request refunds of sales and use taxes. [G.S. 105-164.14(c)].

Currently, 28 separate types of entities are entitled to sales tax refunds, excluding those related to economic development incentives. Not only have refunds been getting larger over the past 10 years, but the change from quarterly to monthly distributions has also made them more noticeable, since they are not averaged out over three months as before. Refunds tend to bunch up in certain months, as there are monthly, quarterly, semi-annual, and annual filers. Therefore, the impact of refunds on a single month's distribution can be considerable. The variable impact of refunds, together with timing issues in the administration of the taxes (changing close-out dates, late submissions,

etc.), also makes month-to-month comparisons with past sales tax data difficult.

### **Municipal Access to Refund Information:**

Municipalities may request that DOR provide them with a list of each claimant that received a sales tax refund in the past 12 months of at least \$1,000 of tax paid to any of the counties in which the municipality is located. The list will include the name and address of each of these claimants and the amount of the refund received from each county covered by the request. A municipality may require any claimant on the list to provide a copy of the official request for the refund and any supporting documentation requested by the municipality to verify the request. The requests to DOR and claimants must be made by the mayor of the city or a city official designated in a resolution adopted by the city's governing board. Information given to a county or city official under this section is not a public record and may not be disclosed except as provided in G.S. 160A-208.1.

**Municipal Refunds:** Just a reminder that municipalities are eligible for a refund of the state sales and use taxes they pay on direct purchases of tangible personal property during the year. [G.S. 105-164.14(c)]. You must file a claim for refund within six months following the close of the fiscal year during which the tax was paid. While this is not a direct revenue source, it is an important way to cut the cost of city purchases during the year. Municipalities received over \$115 million in refunds during FY 2015-16.

### **Solid Waste Disposal Tax**

The \$2 per-ton solid waste disposal tax is charged on municipal solid waste and construction and demolition debris that is deposited in a landfill in the state or transferred at a transfer station for disposal outside the state. The amount of the tax distributed to municipalities in FY 2017-18 was \$3,700,184.10. The proceeds of the tax are distributed as follows: 50 percent to the Inactive Hazardous Sites Cleanup Fund to help pay for assessment and remediation of pre-1983 landfills (including abandoned, unlined city or county dumps), 18.75 percent to cities on a per capita basis for solid waste management programs and

services, 18.75 percent to counties on a per capita basis for solid waste management programs and services, and 12.5 percent to the State's general fund.

However, the legislation allows those who applied for landfill permits before August 1, 2006, and whose applications would be denied under the new standards of the act, to request reimbursement of their reasonable costs in exchange for executing a covenant not to sue the state. Proceeds of the tax will first be used to pay such costs, and reduced two of the first five quarterly distributions of the tax. It is not clear whether additional applications will be made that could reduce future distributions.

### **Local Occupancy Taxes**

More than 150 municipalities and counties now have local act authority to levy hotel, motel and other occupancy taxes. Each act is different and municipalities may levy an occupancy tax only under authority of a local act. Occupancy taxes are administered and collected by local governments, not DOR.

### **Prepared Food and Beverage Taxes**

Four counties, the Town of Hillsborough, and the City of Monroe (although it has not yet been approved by the voters) now have local act authority to levy a one percent sales tax on prepared food and beverages. Municipalities may levy this tax only under authority of a local act.

### **Eligibility for State-Collected Local Revenues**

No municipality incorporated with an effective date on or after January 1, 2000, is eligible for Powell Bill funds, local option sales tax proceeds, utility tax distributions, or beer and wine tax distributions unless it complies with the 5-cent property tax rate and four services requirements for Powell Bill funds. A municipality incorporated with an effective date on or after January 1, 2000, is ineligible for state-collected local revenues unless a majority of its street miles are open to the public.

### **Transitional Hold Harmless (expired August 2013)**

In exchange for the authority to levy a third ½ percent local option sales tax, the General Assembly repealed \$333.4 million in reimbursement payments to local governments, effective July 1, 2002. Included were reimbursements for the inventory tax, intangibles tax, sales tax on food stamp purchases, and homestead exemption. [SB 1115, Section 30A.1 - SL 2002-126]. The legislation included a hold harmless provision requiring the Secretary of Revenue to make an annual payment on or before August 15, beginning in 2003 [G.S. 105-521], to those local governments whose estimated revenue from the sales tax is less than 100 percent of the value of their repealed reimbursements. The minimum amount of hold harmless that was distributed was \$100. This payment continued despite the repeal of Article 44. The Transitional Hold Harmless payment was to expire in August 2012. However, following lobbying by the League and its members, it was extended by one year at 50 percent of its previous value. By statute, the last Transitional Hold Harmless payment was made in August 2013. No additional payments will be made without a change in State law. *[Electronic copies of the annual reports on the sales tax hold harmless distribution can be found at: [www.dor.state.nc.us/publications/reimbursement.html](http://www.dor.state.nc.us/publications/reimbursement.html)]*