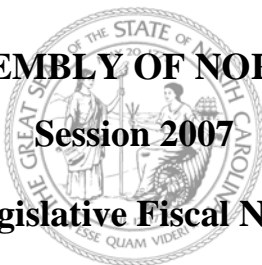


GENERAL ASSEMBLY OF NORTH CAROLINA



Session 2007

Legislative Fiscal Note

BILL NUMBER: Senate Bill 875 (First Edition)

SHORT TITLE: Research and Development Credits Enhancement

SPONSOR(S): Senator Cowell

FISCAL IMPACT					
	Yes ()	No ()	No Estimate Available ()		
	<u>FY 2007-08</u>	<u>FY 2008-09</u>	<u>FY 2009-10</u>	<u>FY 2010-11</u>	<u>FY 2011-12</u>
REVENUES (\$ millions)	(\$0.4)	(\$0.8)	(\$1.2)	(\$1.2)	(\$1.2)
EXPENDITURES					
POSITIONS (cumulative):					
PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED: Department of Revenue					
EFFECTIVE DATE: January 1, 2007					

BILL SUMMARY:

The bill amends GS 105-129.55 by increasing the research and development tax credit percentage allowed for eligible research expenses. The changes are effective beginning with the 2007 tax year.

The specific changes are as follows:

- (1) Small business. – If the taxpayer was a small business as of the last day of the taxable year, the applicable percentage is increased from 3 percent to 3.25 percent.
- (2) Low-tier research. – For expenses with respect to research performed in a development tier one area, the applicable percentage is increased from 3 percent to 3.25 percent.

(3) Other research. – For expenses not covered under subdivision (1) or (2) of this subsection, the percentages provided in the table below apply to the taxpayer's qualified North Carolina research expenses during the taxable year at the following levels:

Expenses

Up to \$50 million is increased from 1 percent to 1.25 percent.

From \$50 million to \$200 million is increased from 2 percent to 2.25 percent.

Over \$200 million is increased from 3 percent to 3.25 percent.

(4) North Carolina University Research Expenses. – A taxpayer that has North Carolina university research expenses for the taxable year is allowed the applicable percentage is increased from 15 percent to 20 percent.

ASSUMPTIONS AND METHODOLOGY:

In 2006, there were 55 companies who generated R&D tax credits under Article 3F. Based on information provided by the Department of Revenue, the calculated effective percent of expenses allowed for credits would increase by an overall effective rate of 18 percent with this bill. This effective increase was calculated by comparing estimates of the number of credits that would have been taken if the rates were in effect during 2006 with the actual credits generated.

It was assumed, consistent with other fiscal estimates of R&D tax credits, that the amount of credits actually taken will be 32 percent of the credits generated in any given tax year. Additionally, it was assumed that new tax credits generated each year would equal the credits generated in 2006 multiplied by the effective increase of 18 percent created with by the bill. Thus, there will be a pyramid effect as credits generated and taken increase while using the 15 year carry forward allowance. Based on those assumptions in 2007, the increased amount of expenses eligible for credit will reduce revenues by \$385,000, by tax year 2012 the amount of loss will have risen to \$1.2 million.

The Article 3F R&D credits are just now beginning to be utilized. There appears to have been scant usage of the university credits in 2006. Because there may be longer start up times with university R&D projects, it is possible that university related credits will increase significantly over the next several years. This could mean the impact of this bill may be underestimated given the 25 percent increase in university R&D expense credits.

SOURCES OF DATA: Department of Revenue

TECHNICAL CONSIDERATIONS: None

FISCAL RESEARCH DIVISION: (919) 733-4910

PREPARED BY: Barry Boardman

APPROVED BY: Lynn Muchmore, Director
Fiscal Research Division

DATE: April 24, 2007



Signed Copy Located in the NCGA Principal Clerk's Offices