

ARTICLE 13

Revenues

by David M. Lawrence and Kara A. Millonzi

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COUNTIES AND CITIES MUST raise revenues to support the services they provide. Revenues increase a local government's net worth or financial resources. Revenues are usually cash receipts, but not all cash receipts are revenues. For example, when a county redeems an investment, one asset—the investment—is exchanged for another—cash. Except for interest earnings from the investment, the county's net worth does not increase, and no revenues accrue. Likewise, when a city issues bonds, its cash receipts increase by the amount of the bond proceeds, but the city also incurs a debt or a liability equal to the proceeds. The addition to cash receipts in this case is balanced by the liability, and neither the city's net worth nor its revenues are increased.

The major types of revenues available to North Carolina counties and cities are local taxes, state-shared taxes, user charges, other local fees and charges, and federal and state grants and aid. *Taxes* are compulsory charges that governments levy on persons or property. They need not bear any relation to the benefit from *public* services received by the taxpaying persons or property. The most important taxes for North Carolina local governments are the property tax, the local-option sales tax, and a variety of taxes levied by the state and shared with local governments. On a statewide average, property taxes constitute about 39 percent of total county revenues, and local-option sales taxes constitute about 15 percent.¹ In cities, by contrast, property taxes constitute about 18 percent of total city revenues, local-option sales taxes slightly less than 9 percent. The reason for cities' lower reliance on property and sales taxes, as a percentage of their total revenues, is widespread city operation of utilities, which account for 34 percent of total city revenues.²

User charges are levied on those who avail themselves of certain county or city services in proportion to the benefit they receive from the services. Water supply and distribution and sewage collection and treatment are the most important local government activities supported by user charges. Other user charges levied by the state's counties are for solid waste collection and disposal, health and mental health services, ambulance services, recreation and cultural activities, airports, and several other functions. Cities levy user charges for electric power and gas distribution, solid waste collection and disposal, off-street parking, mass transit, ambulance services, cemeteries, recreation and cultural activities, airports, and several other functions.

Besides taxes and user charges, counties and cities have other local revenue sources available to them. The more important of these are fees levied to cover the cost of regulatory activities, special assessments, profits from alcoholic beverage control (ABC) stores, and investment earnings.

Finally, North Carolina local governments, especially counties, receive intergovernmental grants and aid. One major change in public finance since the early 1980s has been the reduction in federal aid to local governments. In 1979 direct federal aid to local governments as a percentage of general revenues from local sources was more than 17 percent nationally; twelve years later such aid had dropped to less than 6 percent,³ where it roughly remains today.

Local Taxes

As creations of the legislature, counties and cities may impose only the local taxes specifically authorized by the General Assembly. The following local taxes are available to them under the general law: the property tax, the local-option sales and use tax (levied by counties but shared with cities), the privilege license tax, the animal tax, the rental car gross receipts tax, the motor vehicle license tax (cities only), and the local land transfer tax (counties only). A number of counties and cities levy or share in other local taxes as authorized by local acts of the legislature.

1. North Carolina Department of State Treasurer, Financial Information, County Population Group: Statewide, found on the Internet at www.nctreasurer.com/lgc/units/D_E.htm. The percentages given were those in effect for the 2006–7 fiscal year.

2. North Carolina Department of State Treasurer, Financial Information, Municipalities: All Statewide, found on the Internet at www.nctreasurer.com/lgc/units/D_AG.htm. The percentages given were those in effect for the 2006–7 fiscal year.

3. Bureau of the Census, *Government Finances, 1978–79* (Washington, D.C.: Government Printing Office, 1979), 64; and *Government Finances, 1991–92* (Washington, D.C.: Government Printing Office, 1993), 1.

The Property Tax

The property tax is levied against real and personal property and ultimately is an obligation of the property, not its owner. If the tax is not paid, the final enforcement procedure is to sell the property and pay the tax from the proceeds of the sale. Before resorting to foreclosure, however, tax collectors can proceed against the taxpayer more directly, such as by seizing personal property or attaching the taxpayer's bank account. For total county and city property tax levies in North Carolina in recent years, see Appendix 13-1. Part of the annual increase in property tax levies evident in that table is due to increases in the tax rate and part is due to growth in the tax base, that is, in the value of property.

Tax Base

The property tax base consists of real property (land, buildings, and other improvements to land); personal property (business equipment, automobiles, etc.); and the property of public service companies (electric power companies, telephone companies, railroads, airlines, and certain other companies). Not all property is subject to taxation. Government-owned property is exempt under Article V, sections 2(2) and (3) of the state constitution. In addition, the General Assembly may exempt property from taxation or classify property to exclude it from the tax base, give it a reduced valuation, or subject it to a reduced tax rate. It must do so, however, only on a statewide basis (G.S. 105-275 through -278.9). A local government itself may not exempt or classify or otherwise give a tax preference to property within its jurisdiction. For the assessed value of property subject to taxation in North Carolina's counties and cities, see Appendix 13-2. (The administration of the property tax is discussed in much greater detail in Article 14 of this book.)

Tax Rate Limitations and Voter Approval

Property taxes levied for certain purposes are subject to rate limitations and, in a very few cases, must be approved by the voters. These restrictions are pursuant to Article V, section 2(5) of the state constitution, which reads as follows:

The General Assembly shall not authorize any county, city or town, special district, or other unit of local government to levy taxes on property except for purposes authorized by general law uniformly applicable throughout the State, unless the tax is approved by a majority of the qualified voters of the unit who vote thereon.

This provision means that unless the General Assembly specifically authorizes the levy of property taxes for a particular purpose and does so on a statewide basis, property taxes may be levied for that purpose only with voter approval.

To implement Article V, section 2(5), the General Assembly has enacted G.S. 153A-149, for counties, and G.S. 160A-209, for cities. These two statutes place functions that counties and cities are authorized to undertake in three groups. The governments may levy property taxes for Group I functions without restriction on tax rate or amount. For cities, this group includes only debt service on general obligation debt, but for counties the group includes the most important state-mandated functions: schools and social services. Counties and cities may levy property taxes for Group II functions without a vote, to a maximum rate of \$1.50 per \$100.00 valuation of taxable property. They include almost all of the remaining functions of both county and city government. A local government may hold a referendum on the levy of property taxes for any Group II function. If such a referendum passes, the tax levied under it does not count against the \$1.50 limitation. A local government may also hold a referendum to raise the \$1.50 limitation. Group III functions include all authorized activities that the General Assembly has not specified as either Group I or Group II functions. The statute does not identify Group III functions. If the voters approve the levy of property taxes for a Group III function, any tax levied for that function does not count against the \$1.50 rate limitation. For a list of Group I, Group II, and the most important Group III functions, see Appendix 13-3.

Tax-Levy Formula

The formula for setting the property tax rate and enacting property taxes is relatively simple. One determines the amount of property tax revenue that must be *collected* to balance the budget, considering estimated expenditures and the amount of money that other revenue sources are likely to yield. (The full property tax levy—the total dollar value of the tax enacted—is never collected. Most North Carolina local governments collect 95 to 99 percent of the levy; the statewide average is almost 97 percent.) In calculating the amount of tax expected to be collected, the government may not use an estimated collection percentage that exceeds the current year's collection percentage [G.S. 159-13(b)(6)].

To illustrate the procedure for determining the tax levy and rate, let us say that a county must collect \$10,000,000 in property tax revenue to balance its budget and that its finance officer expects 96 percent of the property tax levy to be collected. Being a little conservative, the finance officer assumes that the collection percentage for the coming budget year will be 95 percent. She divides the \$10,000,000 of required property tax revenue by 0.95, which yields

a property tax levy of \$10,526,000. She then divides that levy by taxable valuation—say, \$1.5 billion—which yields \$.007017. This figure is multiplied by 100 to produce a tax rate of \$.7017 per \$100.00. (North Carolina tax rates increasingly use fractional cents.) To check her arithmetic, the finance officer multiplies the \$1.5 billion by 0.007017, which yields \$10,526,000, the levy. Ninety-five percent of the levy is \$10,000,000 in collected property taxes.

Collection of Property Taxes and Cash Flow

Property taxes are due on September 1, but taxpayers may delay payment until January 5 without incurring a penalty. In one county in a recent year, 5 percent of the tax levy was paid in August; 4 percent in September and October; 15 percent in November; 36 percent in December; 28 percent in January; and 6 percent in all other months of the year.⁴ Such a concentration of property tax collections in the middle of the fiscal year is typical of most North Carolina cities and counties. It means that cities and counties must rely on fund balances and other revenue sources to finance expenditures during the first part of the fiscal year.

Uniformity of Taxation and Service Districts

With one exception the state constitution requires that the county or city property tax rate be uniform throughout the government. The uniformity rule applies only to the levy of the tax, not to the use of its proceeds, which may be spent wherever needed. The exception arises from Article V, section 2(4), of the state constitution, which authorizes the General Assembly to permit counties and cities to define special service districts within their borders and to levy additional taxes in those areas to provide services or facilities that are not offered throughout the unit or that are offered at a lower level in the rest of the unit.

Pursuant to this constitutional provision, the General Assembly has enacted the County Service District Act of 1973, G.S. Chapter 153A, Article 16, Part 1, and the Municipal Service District Act of 1973, G.S. Chapter 160A, Article 23. These statutes authorize counties and cities, respectively, to define a part of the county or the city as a service district, to levy a property tax in the district additional to the countywide or citywide property tax, and to use the proceeds to provide services to the district. A service district is in no way a separate unit of government. It is simply a geographic designation, a defined part of the county or city in which the county or city government levies extra taxes and provides extra services. Counties may define a service district for any of the following functions:

1. beach erosion control and flood and hurricane protection works
2. fire protection
3. recreation
4. sewage collection and disposal
5. solid waste collection and disposal
6. water supply and distribution
7. ambulance and rescue services
8. watershed improvement, drainage, and water resources development
9. cemeteries

Despite the various purposes for which these districts may be established, almost all county service districts have been created for fire protection purposes.⁵

Cities may define a service district for any of the following functions:

1. beach erosion control and flood and hurricane protection works
2. downtown revitalization projects
3. urban area revitalization projects⁶
4. transit-oriented development projects
5. drainage projects
6. sewage collection and disposal systems
7. off-street parking facilities
8. watershed improvement, drainage, and water resources development projects

4. These data were supplied by the county finance director.

5. In Mecklenburg County the county may also establish a service district for law enforcement. In Camden County the county may establish a service district for a variety of services if the county adopts a unified government plan.

6. This purpose is only available to cities of 150,000 or more.

As with counties, cities have used service districts almost entirely for a single purpose: downtown revitalization. Such downtown districts have been used to finance services, such as additional police patrols or more frequent solid waste collection; for capital improvements, such as sidewalk or street improvements; and to finance downtown promotional programs, such as the Main Street program.⁷

A service district does not have its own governing body separate from the board of county commissioners or city council that established it. Occasionally, though, the governing board will create an advisory board within the district, especially for districts established for fire protection, or will contract for operation of the district with a nonprofit organization that represents district property owners, especially in downtown districts.

G.S. 153A-302 and 160A-537 establish the standards for creating a county or municipal service district. A district is defined by simple action of the governing board. No petition from district residents or property owners is required, although the board could establish a policy of defining districts only when they receive such a petition. A vote need not be held within the district in order to create it. In fact, there is no authority to hold a vote even if the governing board thinks one is desirable. The board has only to find that the district needs the proposed service or services “to a demonstrably greater extent” than the rest of the county or city. Usually a county or city sets the effective date for a new service district at the beginning of the first new fiscal year after the governing board adopts the resolution approving the district, though the board may postpone that date. Once the district becomes effective, the unit must “provide, maintain, or let contracts for” the service or services involved within a reasonable time, not to exceed one year.

All of the services or facilities that a county or city may provide in a service district are Group II functions (see Appendix 13-3) for purposes of the application of tax rate limitations. Because of this the property tax rate for taxes levied exclusively in such a district, when taken together with the general county or city tax rate attributable to Group II functions, may not exceed the rate limitation of \$1.50 per \$100 of valuation.

Payments in Lieu of Taxes

The state constitution exempts from taxation property owned by the federal government or by the state or a local government. Occasionally, however, the government that owns the property makes payments in lieu of taxes to the government that could have taxed the property had it been privately owned. Most of these payments are directed by statute. For example, the federal housing law requires each local housing authority to make payments in lieu of taxes to the city or cities in which its projects are located. A city or county receiving payments in lieu of taxes may use such payments for any public purpose.

The Local-Option Sales and Use Tax

The local-option sales and use tax is in fact two taxes. The sales tax is basically a tax on the retail sale or lease of tangible personal property and on the rental of motel and hotel rooms. The use tax is an excise tax on the right to use or consume property in North Carolina or elsewhere. The use tax produces about 10 percent of the total sales and use tax yield. For the total amounts of sales and use tax proceeds received by counties and cities in recent years, see Appendix 13-4.

The local sales and use taxes (local sales taxes) are levied by counties (not cities). During the 2007 and 2008 legislative sessions, the General Assembly made significant changes to local sales tax authorizations in exchange for incrementally assuming the county share of Medicaid expenses over a three-year period. (As of July 1, 2007, the county Medicaid share was 15 percent of the nonfederal share of Medicaid costs and Medicare Part D clawback payments.) The following describes the current local sales tax scheme and details changes in succeeding years resulting from the Medicaid funding reform legislation.⁸

From October 1, 2008, through September 30, 2009, all counties are authorized to levy up to 2.50 percent in local sales taxes. (In addition, Mecklenburg County has been authorized to levy a 0.50 percent tax to be used for mass transit only.) The 2.50 percent is comprised of five separate local sales taxes—all counties currently levy four of the five

7. In addition to the listed purposes, three cities—Greensboro, Hickory, and Wilmington—may create service districts for any municipal activity within historic districts; St. Pauls may create a district to finance lighting at an interstate highway interchange ramp.

8. For a complete description of the Medicaid funding reform legislation, see Kara A. Millonzi and William C. Rivenbark, “Phased Implementation of the 2007 and 2008 Medicaid Funding Reform Legislation in North Carolina,” *Local Finance Bulletin* No. 28 (Sept. 2008).

taxes, totaling 2.25 percent. Counties received authorization for the additional 0.25 percent local sales tax in 2007 and, pending voter approval, may levy either this tax or a local land transfer tax (discussed below).⁹ The five separate local sales and use taxes are allocated differently and carry different expenditure requirements, and for that reason they must be discussed separately. The five taxes, characterized by the articles in G.S. Chapter 105 under which they are levied, are the Article 39 one-cent tax, the Article 40 half-cent tax, the Article 42 half-cent tax, the Article 44 quarter-cent tax, and the Article 46 quarter-cent tax.

Each of the local sales taxes is collected by the state, along with the state's comparable tax. (Currently the state levies a 4.50 percent sales and use tax; thus the total sales tax in all North Carolina counties is at least 6.75. The combined sales tax rate increases to 7.0 percent in those counties where the voters approve and the commissioners choose to levy the Article 46 tax. The current sales tax rate in Mecklenburg County is 7.25 percent; it could increase to a maximum of 7.5 percent.) After collection costs (slightly less than one-half of one percent of collections) are subtracted, the net proceeds of the Article 39, 40, 42, and 44 taxes are allocated among the 100 counties. The net proceeds of the Article 39 and 44 taxes are returned to the county to which the goods were delivered (which is usually also the county in which they were purchased). The net proceeds of the Article 40 and Article 42 taxes are placed in a statewide pool and allocated among the counties on a per capita basis.¹⁰ Finally, the net proceeds of the Article 46 tax (if levied) are returned to the county in which the goods were delivered.

Once the proceeds are allocated among the counties, as set out in the preceding paragraph, the proceeds of the Article 39, 40, 42, and 44 taxes are divided among government units in the county by one of two distribution formulas; per capita or *ad valorem* (property) tax. The county commissioners select the distribution formula and may change it in April of each year, to take effect in the ensuing fiscal year. The per capita formula uses the annual population estimates of the State Department of Administration. The county's total population is added to the population of all cities in the county. This adjusted population figure is divided into the local sales tax revenue available to the county to determine the county's per capita local sales tax amount. The resultant figure is then multiplied by the population of the county and each city within it to determine each unit's share of the county's allocation. Under the *ad valorem* tax formula, the dollar amounts of *ad valorem* taxes levied by the county and each city in the county are added. The proportion that the levy of each of these units bears to the total levy of all units in the county is the proportion of the county local sales tax revenue that each unit receives. *Ad valorem* tax figures used in the formula are those of the fiscal year immediately preceding the year in which the distribution is made. The proceeds of the Article 46 tax (if levied) are retained by the county only—there is no requirement and, in fact, no authorization for a county to share the proceeds with other government units in the county.

Cities may spend local sales and use tax proceeds for any public purpose that they are authorized to undertake, and counties may do the same with the proceeds of the Article 39 one-cent tax, the Article 44 half-cent tax, and (if levied) the Article 46 quarter-cent tax. For counties, however, the proceeds of the other two half-cent taxes are partially earmarked until at least 2011; for the Article 40 tax, 30 percent is earmarked, and for the Article 42 tax, 60 percent is earmarked. The earmarked portions must be used for school capital outlay or for debt service on county borrowing for school projects.

Before October 1, 2008, counties were authorized to levy a half-cent Article 44 tax. The state reduced the authorization to a quarter-cent to defray the cost of the state assuming 50 percent of the county's share of Medicaid expenses. Counties, however, must hold any municipalities incorporated as of October 1, 2008, harmless for the loss of the municipalities' share of the repealed portion of the Article 44 tax. The hold harmless funds are calculated as 50 percent of the proceeds a municipality receives from the Article 40 tax. (This amount will be adjusted to account for revenue distributed from the repealed portion of the Article 44 tax during the second quarter of the fiscal year.) The proceeds will be distributed directly to an eligible municipality by the Department of Revenue from the county's Article 39 local sales tax proceeds.¹¹

9. As of August 2008, voters have approved the Article 46 quarter-cent tax in the following eight counties—Catawba, Martin, Pitt, Sampson, Surry, Cumberland, Haywood, and Alexander.

10. The actual per capita amounts due each county are in fact adjusted under a statutory formula set out in G.S. 105-486(b), which increases or reduces the actual per capita amounts for each county. This adjustment factor was added to the statute in 1987, when the tax itself was expanded to include intercounty sales.

11. Pursuant to the Medicaid funding reform legislation, the state guarantees that all counties experience an annual financial gain of at least \$500,000 as a result of the *Medicaid swap* (defined as the state's assuming the counties' Medicaid costs

Beginning October 1, 2009, to defray the costs to the state of assuming 100 percent of the county's share of Medicaid expenses, the authorization for the remaining quarter-cent Article 44 tax is repealed. Thus all counties will be authorized to levy up to 2.25 percent in local sales and use taxes. The state sales and use tax will be increased by a quarter-cent; the combined sales tax rate for all counties, except Mecklenburg, will be 6.75 percent or 7.0 percent, depending on whether a county has adopted the Article 46 quarter-cent tax. (The combined sales tax rate in Mecklenburg will be 7.0 percent or 7.25 percent.) Additionally, the proceeds of the Article 42 half-cent tax will be distributed to the county where the goods are delivered, instead of being allocated on a per capita basis.

The counties must hold any municipalities incorporated as of October 1, 2008, harmless for the loss of the entire half-cent Article 44 tax. The hold harmless funds are equivalent to the proceeds a municipality receives from the Article 40 tax. (In fiscal 2009–10, this amount will be adjusted to account for revenue distributed from the repealed portion of the Article 44 tax during the second quarter of the fiscal year.) The hold harmless calculation also must factor in any increase or decrease in municipal revenue due to the change in the Article 42 tax proceeds allocation method from per capita to point-of-origin. To calculate the revised hold harmless amount, subtract the amount determined by taking 25 percent of the amount of local sales tax revenue a municipality receives from the Article 39 tax from the amount determined by taking 50 percent of the amount of local sales tax revenue a municipality receives from the Article 40 tax. The difference, positive or negative, is added to the hold harmless amount to determine the revised hold harmless amount.

Counties also must hold their local school administrative units harmless for the loss of any Article 42 tax revenue earmarked for public school capital outlay or debt service on county borrowing for school projects due to the change in allocation method of the Article 42 proceeds from a per capita to a point-of-origin basis. Recall that until October 1, 2009, 60 percent of the amount a county receives from the Article 42 tax is specifically earmarked for these purposes. After that date, when the allocation method of the Article 42 proceeds changes, the legislation directs a county to use 60 percent of the following for public school capital outlay purposes or to retire any indebtedness incurred by the county for public school capital outlay purposes:

- The amount of revenue the county receives from the Article 42 tax, *plus*
- If the amount allocated to the county under G.S. 105-486 (Article 40 tax) is greater than the amount allocated to the county under G.S. 105-501(a) (Article 42 tax), the difference between the two amounts.¹²

It appears that the legislature intended that the phrase “amount allocated to the county” be interpreted to refer to the amount a county receives from both the Article 40 and Article 42 taxes—after the full amount of the proceeds due to the county from these taxes are distributed among the county and any eligible municipalities.¹³

in exchange for the state repealing a portion of the counties' local sales tax authority). From October 1, 2008, through September 30, 2009, the state must make a supplemental payment to the county for the absolute value of the difference if the amount of a county's Medicaid costs assumed by the state minus \$500,000 (county hold harmless threshold) is less than the county's repealed sales tax amount plus its municipal hold harmless amount. A county's repealed sales tax amount is calculated as 50 percent of the Article 40 tax proceeds distributed to a county. (This amount is reduced to account for revenue distributed from the repealed portion of the Article 44 tax during the second quarter of the fiscal year.) The municipal hold harmless amount is the amount of a county's Article 39 tax revenue distributed to eligible municipalities in the county to compensate those municipalities for their loss in Article 44 tax revenue. If the amount of a county's Medicaid costs assumed by the state minus \$500,000 is greater than or equal to the county's repealed sales tax amount plus its municipal hold harmless amount, the county will not receive a supplemental payment from the state.

The state supplemental payments are made semiannually. The secretary of revenue estimates the hold harmless amount and sends each county 90 percent of any estimated supplemental payment with the March local sales tax distribution. The secretary of revenue determines the actual amount owed, if any, at the end of the fiscal year and remits the balance to each county by August 15.

12. The earmark currently is set to sunset in 2011.

13. Pursuant to the Medicaid funding reform legislation, the state guarantees that all counties experience an annual financial gain of at least \$500,000 as a result of the *Medicaid swap* (defined as the state's assuming the counties' Medicaid costs in exchange for the state repealing a portion of the counties' local sales tax authority). After October 1, 2009, the state must make a supplemental payment to the county for the absolute value of the difference if the amount of a county's Medicaid costs assumed by the state minus \$500,000 (county hold harmless threshold) is less than the county's repealed sales tax amount plus its municipal hold harmless amount. A county's repealed sales tax amount is calculated as the amount distributed to the county

Local-Option Land Transfer Tax

As of July 1, 2007, counties are authorized to adopt either an additional 0.25 percent local sales and use tax (the Article 46 tax discussed above) or up to a 0.4 percent land transfer tax (in 0.1 percent intervals), the proceeds of which may be used for any public purpose. There is no requirement, and, in fact, no authorization for a county to share the proceeds of either of the new revenue sources with municipalities.

A county must hold an advisory referendum on either additional revenue source; it may hold a referendum on both at the same time. If the majority of those voting in the referendum vote for the levy of the local land transfer tax or Article 46 local sales and use tax, the board of county commissioners may adopt a resolution levying the tax after providing ten days' public notice. If both ballot measures are successful, however, a board of county commissioners only may implement one of the additional revenue options. The levy of the land transfer tax may become effective the first day of the second succeeding calendar month after the date the resolution is adopted, at the earliest.

The local land transfer tax applies to transfers of interests in real property located within the county. It is payable by the seller of the interest and applies to the consideration or value, whichever is greater, of the interest conveyed, including the value of any lien or encumbrance remaining on the property at the time of the conveyance. If the property is located in two or more counties, a transfer of an interest in the property is taxable only by the county in which the part with the greater value lies.

The authorizing legislation specifically exempts certain transferors, specifically governmental units or instrumentalities of governmental units. It also exempts certain conveyances of interests in real property to the same extent that they are exempted from the state land transfer excise tax (discussed below); transfers that are required by operation of law; leases for a term of years; transfers by or pursuant to the provisions of a will, by intestacy, or by gift; transfers where no consideration in property or money is due or paid by the transferee to the transferor; transfers that are accomplished by merger, conversion, or consolidation and transfers made by an instrument securing indebtedness. Additionally, unlike the state land transfer excise tax, the local land transfer does not apply to contracts for the sale of standing timber; although it is unclear whether it applies to timber deeds.¹⁴

The administrative provisions for the state land transfer excise tax, codified in G.S. 105-228.32-.37, also apply to the local land transfer tax. A county may repeal or reduce the rate of the local land transfer tax by resolution, but the repeal or reduction may not become effective until the end of the fiscal year in which the repeal or reduction resolution is adopted.

under Article 40. Added to this figure is the amount, positive or negative, determined by subtracting 25 percent of the Article 39 tax proceeds distributed to a county from 50 percent of the Article 40 tax proceeds distributed to a county. (In fiscal year 2009–10 only, this amount is reduced to account for revenue distributed from the repealed portion of the Article 44 tax during the second quarter of the fiscal year.) The municipal hold harmless amount is the amount of a county's Article 39 tax revenue distributed to eligible municipalities in the county to compensate those municipalities for their loss in Article 44 tax revenue. If the amount of a county's Medicaid costs assumed by the state minus \$500,000 is greater than or equal to the county's repealed sales tax amount plus its municipal hold harmless amount, the county will not receive a supplemental payment from the state.

The state supplemental payments are made semiannually. The secretary of revenue estimates the hold harmless amount and sends each county 90 percent of any estimated supplemental payment with the March local sales tax distribution. The secretary of revenue determines the actual amount owed, if any, at the end of the fiscal year and remits the balance to each county by August 15.

14. The authorizing legislation for the state land transfer excise tax explicitly states that the tax "applies to timber deeds and contracts for the sale of standing timber *to the same extent as if these deeds and contracts conveyed an interest in real property.*" G.S. 105-228.30(a) (emphasis added). The legislation authorizing the local land transfer tax does not include this provision. The language was added to the state land transfer excise tax statute in 2000 in response to a 1999 decision by the North Carolina Supreme Court holding that contracts for the sale of standing timber are transfers of personal property, not real property. *Fordham v. Eason*, 351 N.C. 151, 521 S.E.2d 701 (1999). Although the amendment to G.S. 105-228.30(a) suggests that both contracts for the sale of standing timber and timber deeds are conveyances of personal property, it is an open question in North Carolina whether timber deeds constitute conveyances of real property or personal property. See David M. Lawrence, *Local Government Property Transactions in North Carolina*, 2d ed. (2000), 161–70. If timber deeds do, in fact, convey real property, they are subject to the local land transfer tax despite the absence of an explicit provision addressing timber deeds in the authorizing legislation.

Other Local Taxes

The general law authorizes both counties and cities to levy a few other taxes: the privilege license tax, the rental car gross receipts tax, and the animal tax. In addition, cities (but not counties) are authorized to levy motor vehicle license taxes. Furthermore, many counties and cities may levy occupancy taxes pursuant to local acts of the General Assembly, and a few local governments may levy prepared-food taxes, deed transfer taxes, and motor vehicle taxes, also pursuant to local acts. Although none of these local taxes are significant in the overall revenue picture for North Carolina's local governments, they produce hundreds of thousands of dollars for many counties and cities and up to several million dollars for some of the state's largest local governments. Except for a portion of city motor vehicle license taxes, revenue from the taxes authorized by general law may be spent for any public purpose. Revenue from the taxes permitted by local act is usually earmarked for specific purposes.

The Privilege License Tax

The privilege license tax is imposed on the privilege of carrying on a business or engaging in certain occupations, trades, employment, or activities. City and county authority to levy this tax is quite different. Under G.S. 153A-152 a county may levy privilege license taxes *only* as specifically authorized by law. The authorizations appear primarily in Article 2, Schedule B, of G.S. Chapter 105. The state formerly levied a privilege license tax on a few categories of businesses under that article and frequently permitted some county taxation of the same businesses. Although the state has repealed its own privilege license tax, the Schedule B authorizations remain valid for counties.

Under G.S. 160A-211 a city may levy privilege license taxes *except* as specifically restricted or prohibited by law. As with the county authorizations, the city restrictions and the prohibitions appear primarily in Article 2, Schedule B, of G.S. Chapter 105 and were imposed when the state levied a tax on a business or an occupation. These restrictions remain on city taxes, even though the state has repealed its own privilege license tax. In devising local privilege license taxes for businesses and occupations, cities have much flexibility. The basic rate of taxation must be uniform for each class of taxpayer (that is, for each occupation and business), but may differ among classes. Some authorities recommend that privilege license taxes be based on gross receipts and be uniform on all businesses and occupations, and increasingly cities are adopting that measure for the tax.

For both cities and counties, the privilege license tax is paid once a year, and the license period usually runs for the fiscal year. An Institute of Government publication entitled *North Carolina City and County Privilege License Taxes* is a useful guide to this tax.¹⁵

The Rental Car Gross Receipts Tax

In 2001 the General Assembly removed rental cars from the property tax base and instead authorized cities and counties to levy a tax on the gross receipts of car rental companies operating inside the city or county (G.S. 160A-215.1 and G.S. 153A-156). The maximum rate of tax is 1.5 percent of gross receipts.

The Animal Tax

Counties and cities may levy taxes on the privilege of keeping dogs and other pets (G.S. 153A-153 and 160A-212). These taxes evolved from local dog taxes, and most counties and cities still tax only dogs, although an increasing number of cities tax cats as well. A local government is free to decide which pets to tax and to set the rate of the tax. Rates often are based on the type of animal and whether it has been spayed or neutered, with higher rates—as much as \$30 in some local governments—for animals that have not been fixed. It is no longer legally required (or lawfully authorized, for that matter) to use the proceeds of dog taxes to compensate people for damage done to their livestock by dogs running at large.

The Short-Term Heavy Equipment Rentals Tax

In 2008 the General Assembly removed heavy equipment that is rented or leased on a short-term basis from the property tax base and instead authorized counties and cities to levy a tax on the gross receipts of entities operating within a county or city whose principal business is the short-term lease or rental of heavy equipment at retail. G.S. 153A-156.1 and G.S. 160A-215.2 authorize counties and cities, respectively, to adopt a resolution imposing the gross receipts tax—counties are authorized to impose a tax of 1.2 percent of gross receipts if the place of business from which the heavy equipment is delivered is located in the county and cities may impose a tax of 0.8 percent of gross receipts if the place of business from which the heavy equipment is delivered is located in the city.

15. William A. Campbell, *North Carolina City and County Privilege License Taxes*, 5th ed. (Chapel Hill, N.C.: Institute of Government, The University of North Carolina at Chapel Hill, 2000).

Heavy equipment is defined as earthmoving, construction, or industrial equipment that is mobile, weighs at least 1,500 pounds, and is either:

1. a self-propelled vehicle that is not designed to be driven on a highway, or
2. industrial lift equipment, industrial handling equipment, industrial electrical generation equipment, or a similar piece of industrial equipment.

The definition includes attachments for heavy equipment, regardless of the weight of the attachments.

The Motor Vehicle License Tax

G.S. 20-97 authorizes cities to levy two motor vehicle license taxes on the privilege of keeping a motor vehicle within the city. The first tax carries no earmark, and for almost all cities the rate may not exceed \$5 per vehicle per year. The proceeds of the second tax, also subject to a maximum of \$5 per vehicle per year, may be used only to support public transportation systems. (A few counties also enjoy authority pursuant to local legislation to levy such a tax.)

Taxes Permitted by Local Act

Local governments in more than seventy counties are permitted by local act to levy occupancy taxes, which are taxes on the occupancy of hotel and motel rooms. Although most of these taxes are levied by county governments, a few are levied by cities, and cities frequently receive a share of the tax even if the county levies it. In most cases the local act authorizing the tax limits the use that the levying government may make of the proceeds, often to travel- or tourism-related programs. In some instances, though, the levying government may use the money for any public purpose. The authorizations are usually for a tax of up to 3 percent of gross receipts, although several permit a rate of up to 6 percent.

A much smaller number of counties are authorized to levy taxes on prepared food (or restaurant meals) and on the transfer of real estate, in both cases at the rate of 1 percent. (As discussed above, as of July 1, 2007, all counties are authorized to levy up to a 0.4 percent local land transfer tax, pending voter approval. Counties that currently levy the 1 percent real estate transfer tax pursuant to local legislation are authorized to also levy up to the additional 0.4 percent, again, pending voter approval.) In addition, another local act permits Greensboro to levy a tax on admissions to the Greensboro Coliseum (although it has not done so). No other local government may currently levy such a tax.

State-Shared Taxes

State taxes that are shared with counties are the beer and wine taxes, the real estate transfer tax, two disposal taxes, and, as of January 1, 2008, a portion of a 911 charge on voice communication services. State taxes that are shared with cities are the beer and wine taxes, electric franchise taxes, telecommunications taxes, video services taxes, satellite services taxes, the piped natural gas tax, motor fuel taxes, and, as of January 1, 2008, a portion of a 911 charge on voice communication services. Appendix 13-5 sets out the statewide amounts of the major state-shared taxes for several recent years. (The table groups together the electric franchise and piped natural gas taxes because that is how the Department of Revenue reports them.)

Video Programming Services Taxes

As of January 1, 2007, the local cable franchise system was replaced with a statewide video service franchising process and local governments no longer have the authority to assess and collect the cable franchise taxes. In lieu of the cable franchise tax revenue, all cities and counties currently receive shares of three state sales tax revenues—7.23 percent of the net proceeds of tax collections on telecommunications services, 22.61 percent of the net proceeds of taxes collected on video programming services, and 37 percent of the net proceeds of taxes collected on direct-to-home satellite services.

The first \$2 million of the local share of the proceeds from these three taxes are distributed to local governments to support local public, educational, or governmental access channels (PEG channels). Local governments will receive \$6,250 per quarter for each qualifying PEG channel, up to a maximum of three channels. (A qualifying PEG channel is one that meets specified programming requirements.¹⁶) If the aggregate distribution for qualifying PEG channels

16. G.S. 105-164.44J defines a qualifying public, educational, or governmental access channel (PEG channel) as one that operates for at least ninety days during a fiscal year and that meets the following programming requirements:

does not equal \$2 million, the remaining funds will be allocated to the PEG Channel Fund to be used to provide loans to local governments for the capital expenditures necessary to provide PEG channel programming. Conversely, if the aggregate distribution would exceed \$2 million, the amount to be distributed for each qualifying PEG channel will be proportionately reduced.¹⁷ A local government must equally allocate the supplemental PEG channel support funds for the operation and support of each of its qualifying PEG channels.

The remaining funds are distributed according to each local government's proportionate share. A city's or county's proportionate share for 2006–7 was calculated by dividing the local government's base amount for that year by the aggregate base amounts of all the cities and counties. The base amount was determined in one of two ways: (1) for cities or counties that did not impose a cable franchise tax before July 1, 2006, the base amount was \$2.00 times the most recent annual population estimate; or (2) for cities or counties that did impose a cable franchise tax before July 1, 2006, the base amount was the total amount of cable franchise tax and subscriber fee revenue the county or city certified to the secretary of state that it imposed during the first six months of the 2006–7 fiscal year. In each subsequent fiscal year, the proportionate share is adjusted for per capita growth.

These funds are partially earmarked. A city or county that imposed subscriber fees during the first six months of the 2006–7 fiscal year must use a portion of the funds distributed to it for the operation and support of PEG channels. The amount of funds that must be used for this purpose is the proportionate share of funds that were used for this purpose in fiscal year 2006–7, which was equal to two times the amount of subscriber fee revenue the county or municipality certified that it imposed during the first six months of fiscal year 2006–7. The remainder of the distribution may be used for any public purpose.

Beer and Wine Taxes

The state levies a number of taxes on alcoholic beverages. These include license taxes, excise taxes on liquor, and excise taxes on beer and wine.¹⁸ The state shares 23.75 percent of its excise tax on beer, 62 percent of its excise tax on unfortified wine, and 22 percent of its excise tax on fortified wine with cities and counties. A city or a county is eligible to share in beer or wine excise tax revenues if beer or wine may legally be sold within its boundaries. If only one beverage may be sold, the city or county shares only in the tax for that beverage. General law permits beer and wine to be sold statewide but allows any county to hold a referendum on prohibiting the sale of either beverage (or both) within the county. The statutes also allow a city in a dry county to vote to permit the sale of beer or wine within its boundaries.

Distribution of state beer and wine tax revenue that is shared with local governments is based on the population of eligible cities and counties. Counties are given credit only for their *nonmunicipal* population. Since 1983–84 such revenue has grown slowly but steadily to its present level. The money is distributed annually, around Thanksgiving. Counties and cities may spend state-shared beer and wine tax revenue for any authorized public purpose.

Solid Waste Tipping Tax

The state imposes a \$2-per-ton statewide excise tax on the following:

- The disposal of municipal solid waste and construction and demolition debris in any landfill permitted under the state's solid waste management program.
- The transfer of municipal solid waste and construction and demolition debris to a transfer station permitted under the state's solid waste management program for disposal outside the state.

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- It delivers at least eight hours of scheduled programming a day.
 - It delivers at least six hours and forty-five minutes of scheduled non-character-generated programming a day.
 - Its programming content does not repeat more than 15 percent of the programming content on any other PEG channel provided to the same county or municipality.

17. A county or city must certify to the secretary of revenue by July 15 of each year all of the qualifying PEG channels it provided during the previous fiscal year. If a county or municipality subsequently determines that it certified a PEG channel in error, it must submit a revised certification to the secretary of revenue and return all supplemental PEG channel support funds distributed to the unit as a result of the error. The secretary of revenue must add any returned funds in the prior fiscal year to the amount of supplemental PEG channel support funds available for distribution.

18. North Carolina Department of Revenue, Tax Research Division, *Statistics of Taxation 1980* (Raleigh, N.C.: North Carolina Department of Revenue, 1981), 172.

Municipal solid waste is defined as any solid waste resulting from the operation of residential, commercial, industrial, governmental, or institutional establishments that would normally be collected, processed, and disposed of through a public or private solid waste management service.

The state shares a portion of the excise tax revenue with counties and cities who provide, and are responsible for the payment of, solid waste management programs and services, or that are served by a regional solid waste management authority. G.S. 105-187.63 directs that 37.5 percent of the excise tax proceeds (after subtracting certain administrative expenses) are distributed to counties and cities on a per capita basis—with one-half distributed to counties and one-half distributed to cities. For purposes of calculating the per capita amount, the population of a county does not include the population of its incorporated areas. The revenue must be used to fund solid waste management programs and services.

Real Estate Transfer Taxes

The state imposes an excise stamp tax on the conveyance of any interest in real estate. The tax is levied on each recorded deed and is measured by the price paid for the property. The tax rate is \$1 for each \$500 of the sales price. (The local deed transfer taxes in effect in a few counties and the newly authorized general county local-option land transfer tax are in addition to this statewide tax.) The tax is collected by the county, which must remit one-half of the proceeds to the state; the county's portion may be used for any authorized public purpose.

Disposal Taxes

The state imposes special sales taxes on the sale of automobile tires and white goods and distributes the major portion of the proceeds of each tax to counties on a per capita basis. A county must use the tire tax to dispose of scrap tires and the white goods tax for management of discarded white goods.

911 Charge

Effective January 1, 2008, the General Assembly has established a new consolidated system for administering both wireline (landline) and wireless 911 systems. The authorizing legislation creates a 911 Board and authorizes it to develop a comprehensive state plan for communicating 911 call information across networks and among local public safety answering points (PSAPs)—defined as the local public safety agencies that receive incoming 911 calls and dispatch appropriate public safety agencies to respond to the calls.

Among other powers, the 911 Board is authorized to levy a monthly service charge of 70 cents on each active voice communications service connection, defined as each telephone number assigned to a residential or commercial subscriber by a voice communications service provider, without regard to the technology deployed, which is capable of accessing the 911 system. [The Board must reduce the rate if it produces revenue in excess of the amount needed to ensure full cost recovery for voice communication service providers and primary PSAPs (the first point of reception of a 911 call).] As of January 1, 2008, local governments are not authorized to levy any charges for 911 services.

The monthly service charge is collected by each voice communications service provider and remitted to the 911 Board on a monthly basis, less an administrative allowance equal to the greater of 1 percent of the amount of the service charge collections or \$50.00. Revenue from the monthly service charge will be credited to the 911 Fund, an interest-bearing special revenue fund within the state treasury that is administered by the 911 Board. The 911 Board also may retain up to 1 percent of the revenue to cover administrative expenses. The 911 Board determines the amount of the remaining proceeds that will be distributed to Commercial Radio Service (CMRS) providers and primary PSAPs. (A CMRS provider is an entity that is licensed by the Federal Communications Commission to provide commercial mobile radio service or that resells commercial mobile radio service in the state.) The board may adjust the amounts allocated to ensure full cost recovery for CMRS providers and, if there are excess funds, to provide for additional distributions to primary PSAPs.

The money distributed to primary PSAPs is allocated according to the following formula. Each PSAP receives a base amount that is the amount that it received during fiscal 2006–7 and deposited in the Emergency Telephone System Fund of its local governing entity. The 911 Board must designate a percentage of the remaining funds to be distributed to primary PSAPs on a per capita basis, based on the most recent population estimates certified by the State Budget Officer; the rest will be allocated to the PSAP Grant Account to be distributed to eligible PSAPs in rural and other high-cost areas. In order to be eligible for its share of the per capita distribution, a PSAP must provide enhanced 911 service. (Enhanced 911 service is the ability to direct a 911 call to an appropriate PSAP by selective routing based

on the geographical location from which the call originated and providing information defining the approximate geographic location and telephone number of a 911 caller.) If the board does not designate an amount to be allocated to the PSAP Grant Account, all remaining funds will be distributed on a per capita basis. The board may change its percentage designation once per fiscal year.

In order to receive a distribution from the 911 Fund, each PSAP, or the governing entity of a PSAP, must comply with specified reporting and financial auditing requirements. The proceeds received by each PSAP are specifically earmarked to pay for (1) the lease, purchase, or maintenance of emergency telephone equipment, including necessary computer hardware, software, and database provisioning, addressing, and the nonrecurring costs of establishing a 911 system; (2) certain allowable expenses incurred for in-State training of 911 personnel regarding the maintenance and operation of the 911 system and, on a limited basis, certain expenses incurred for out-of-State training; (3) expenses incurred for training specific to the receipt of 911 calls but only for intake and related call taking quality assurance and improvement; and (4) charges associated with the service supplier's 911 service and other service supplier recurring charges. The proceeds may not be used to pay for the lease or purchase of real estate, cosmetic remodeling of emergency dispatch centers, hiring or compensating telecommunicators, or the purchase of mobile communications vehicles, ambulances, fire engines, or other emergency vehicles. The 911 Board may require a PSAP to refund any monies improperly spent after notice and a hearing.

The Electric Franchise Tax

Under G.S. 105-116 the state levies a franchise tax on electric utilities, and pursuant to G.S. 105-116.1 it shares a portion of the tax proceeds with cities. The state taxes these companies at a rate of 3.22 percent of gross receipts, over and above the regular state sales tax, and shares with each city an amount equal to roughly 3 percent of such receipts on the sales of service within the city's boundaries. The money is distributed quarterly, and cities may spend the money for any public purpose.

The Telecommunications Tax

Under G.S. 105-164C the state levies a sales tax on the gross receipts of telecommunications services; the rate is the total of the state's sales tax rate plus the rates of local sales taxes levied in all 100 counties. G.S. 105-14.44F then requires that the Department of Revenue distribute a share of the proceeds from this tax with cities. Each quarter, the state is to distribute to cities 18.03 percent of the proceeds from that quarter, minus \$2.6 million. The telecommunications tax was enacted in 2001 and replaced a telephone franchise tax that was identical to the electric franchise tax described above; each city's share of the telecommunications tax is the same percentage of the new tax that the city received from the repealed telephone franchise tax during the last comparable quarter that the earlier tax was still in force. (Cities incorporated after January 1, 2001, receive a per capita share of the tax; distributions to such cities are subtracted from the total amount going to cities before the much larger distribution described just above is made.) Cities may spend telecommunications tax revenue for any public purpose.

The Piped Natural Gas Tax

G.S. 105-187.41 imposes a state excise tax on the distribution of piped natural gas, with rates that decrease with the amount of gas used by each consumer. The state distributes to each city served by a natural gas system one-half of the tax attributable to sales within that city, with the distributions made quarterly. Cities may spend these revenues for any public purpose.

The Motor Fuels Tax

North Carolina levies motor fuel taxes pursuant to a formula that increases taxes when the wholesale price of motor fuels increases.¹⁹ G.S. 136-41.1 appropriates from this revenue an amount equal to the proceeds of \$.0175 per gallon taxed, plus an additional 6.5 percent of the net proceeds of the North Carolina Highway Trust Fund, and distributes

19. The motor fuels excise tax is a flat rate of 17.5¢ per gallon or 7 percent of the average wholesale price of motor fuel for the base period, whichever is greater. As of fiscal year 2006–7, there is a cap on the variable wholesale component of the tax rate at 12.4¢ per gallon.

that amount among the state's cities. The legislation that first established this distribution is known as the Powell Bill (after its principal sponsor in the North Carolina Senate), and the moneys distributed to the cities are often called Powell Bill funds.

The available funds are distributed according to a two-part formula. Three-quarters of the local proceeds are distributed among cities on a per capita basis and one-quarter according to the number of miles of nonstate streets in each city. Street mileage information comes from annual reports by each city to the State Department of Transportation; annual population estimates come from the State Office of Budget and Management. The money is distributed annually, around October 1. Appendix 13-6 sets out the per capita and per mile amounts distributed to cities over several recent years.

Cities may use motor fuel tax revenue only for maintaining, repairing, and constructing streets or thoroughfares, including bridges, drainage, curbs and gutters, sidewalks, and other necessary appurtenances to streets, including sidewalks. Street maintenance includes street cleaning and snow removal. Permitted construction expenditures include all phases of construction: right-of-way acquisitions; legal and engineering expenses; salaries, wages, and fringe benefits; materials for construction; payments to contractors, and so forth. Cities may also use gasoline tax money for traffic control devices and signs, debt service on street bonds, and the city's share of special assessments for street improvements. They may not use it for street lighting, on- or off-street parking, traffic police, or thoroughfare planning.

User Charges

Revenues from user charges finance in whole or in part numerous local government functions. *User charges* means charges to those who voluntarily receive or use certain government services or facilities. In this context the phrase does not include fees that are incidental to a regulatory program or fees established by law for the performance of official acts, such as the recording of deeds or the serving of legal papers.

Many revenues from user charges are placed in the general fund and are available to support any general fund activity or program. Charges for recreation and cultural activities, ambulance services, and airports are budgeted in the general fund in most local governments. User charges for these and most general fund services typically cover only a portion of the cost of providing the service.

Some activities supported by user charges are set up and operated as public enterprises. A *public enterprise* is an activity of a commercial nature that could be provided by the private sector. Most public enterprises are self-supporting or predominantly so. The General Statutes authorize both counties and cities to operate public enterprises for water supply and distribution, sewage collection and treatment, solid waste collection and disposal, airports, public transportation, off-street parking, and stormwater systems (G.S. 153A-274 and 160A-311); cities are additionally authorized to operate enterprises for electric power generation and distribution, gas production and distribution, and cable television. A local government often sets up a separate accounting fund for each enterprise that it owns or operates,²⁰ and user-charge revenue generated by the enterprise is deposited in that fund and applied first to pay operating expenses, debt service, and capital outlay for the enterprise [G.S. 159-136(b)(4)]. If any user-charge revenue from the enterprise remains, it may be transferred from that enterprise fund and made available to support general government activities or another enterprise.²¹ The authorizing statutes for county public enterprises are contained in G.S. Chapter 153A, Article 15, while those for cities are found in G.S. Chapter 160A, Article 16.

Reasons for Charging Fees to Users

User charges are feasible for any service that directly benefits individual users, is divisible into service units, and can be collected at a reasonable cost. For example, a county landfill provides a direct benefit to each user (his or her garbage is disposed of), the service is divisible into units (each ton of waste disposed of), and the fee for landfill use can be collected at a reasonable cost (by weighing solid waste and charging and collecting so much per ton before it

20. Water and sewer systems operated as a consolidated enterprise may be accounted for in the same fund. G.S. 159-26(b)(4).

21. There are special restrictions on certain solid waste services and stormwater management systems that prohibit transfers from these enterprise funds to support other enterprises or general fund activities.

may be disposed of in the landfill). User charges also allocate limited services and resources efficiently. For example, free water, financed by general taxes, tends to be wasted. But when people are charged for water, they use it more economically.

Cities, and less so counties, often impose user charges for services that are heavily used by nonresidents—for example, airports, parking facilities, cultural facilities, coliseums, and convention centers. The government cannot tax nonresidents, but it can levy charges on them to recoup its cost for providing a service that directly and individually benefits them. Similarly, user charges can be imposed on owners of property that is exempt from property taxes, such as churches and other nonprofit organizations. Some local government officials favor making such owners bear a larger share of the cost of providing services, and this can be done by financing an activity from user charges rather than from property taxes.

On the other hand, other considerations sometimes argue against adoption or expansion of user charges. Compared with the property tax, user charges can be regressive in nature. Furthermore, user charges might cause poor persons and families to decide not to use certain public services. For example, imposing a high fee for use of public recreation facilities might reduce use of the facilities by poor children, and such children are often a primary target for public recreation services. These concerns often lead local government officials to retain some tax support for activities that could, in a technical sense, be fully supported by user charges.

Types of User Charges

Water and Sewer Services

In North Carolina the most important city services that are supported by user charges are water supply and distribution and sewage collection and treatment. The gross receipts generated by the charges for these services contribute 15 to 25 percent of most cities' annual revenue. These services are less pervasive with counties, but an increasing number of counties do provide some kind of water or sewer service to some of their citizens. (Many counties provide these services, especially water, through county water and sewer districts, which are legally separate entities but are governed by the board of county commissioners.) Almost all local governments meter water consumption and charge for water use on this basis. Sewer charges are usually set at some percentage—often at or close to 100 percent—of the water charges. Sewer services to large industries are increasingly metered, and the charge for service to them is based on how much sewage is treated and how difficult it is to treat. A city is permitted by statute to charge higher rates for water and sewer services provided outside its boundaries, and such higher outside rates are common; they range from 50 to 100 percent higher than in-town rates. County and city water and sewer system rates are not subject to regulation by the State Utilities Commission.

Nearly all city water and sewer systems in North Carolina are operated as public enterprises, and increasingly county systems are as well. A water and sewer system is self-supporting when its charges for service plus other recurring revenues—for example, interest earned on water and sewer investments—equal or exceed operating expenses, interest on outstanding water and sewer debt, and depreciation. In recent years many local governments have received grants from the state Clean Water Bond program and from the U.S. Environmental Protection Agency to construct water and sewer systems; to receive the grants, the governments have to agree to keep their water and sewer systems self-supporting.

Electric Power and Gas Services

Seventy-two cities in North Carolina operate electric power distribution systems, and eight have natural gas distribution systems. These cities buy power or gas wholesale from private utility companies, joint power agencies, or other *electric cities* (the term for cities that distribute electric power). They then distribute and sell it retail to households and businesses within their boundaries and sometimes in unincorporated areas outside their city limits.

Most of the state's electric cities participate in generating their own power through joint power agencies. North Carolina has two active joint power agencies. One is made up of nineteen electric cities in the central and western parts of the state. This agency owns a 75 percent interest in Unit Two of Duke Energy's Catawba nuclear power station. The second active joint power agency is in eastern North Carolina; it is composed of twenty-one electric cities once served by Carolina Power and Light Company and eleven cities once served by Virginia Electric Power Company. It owns between 12.44 and 18.33 percent of five generating facilities (plus a number of canceled plants).

Cities that have electric power and gas systems charge for these services on the basis of metered usage by customers. The cities set their utility rates at about those of private power and gas companies in their areas. Because they do and because the cities do not pay property taxes or federal and state income taxes, their utility systems are normally profitable, although the size of electric system profits has decreased in recent years. Most of these surpluses are spent

for capital improvements for the electric and gas systems, and the rest, if any, is sometimes transferred to the general fund to finance general government activities. As with water and sewer services, electric power and gas system rates are not subject to State Utilities Commission regulations.

Solid Waste Collection and Disposal

Counties and cities are both authorized to collect and dispose of solid wastes. In practice, cities commonly carry on collection programs, whereas counties more often provide disposal facilities. (The private sector also provides both collection services and disposal facilities.) Revenues from collection services include the basic service fee, charges for additional or special services, and proceeds from the sale of bags or the rental or the sale of commercial or industrial solid waste containers. A city may charge higher fees for collection outside its borders; but if the county wishes, it may regulate the city's extraterritorial fee schedule through its authority to franchise and regulate collection in unincorporated areas. Revenue generated by disposal facilities comes from fees per weight of load and from sales of recyclable materials. State law mandates a reduction in solid wastes entering the waste stream, and that has caused increasing numbers of cities to institute fee-supported collection services. The hope is that if a person's solid waste collection costs are sensitive to the amount of waste generated, people will recycle more, use products with less elaborate packaging, and otherwise reduce the amount of waste generated. In addition to the above fees, a county or city may levy an "availability fee" for the "availability of a disposal facility provided by" the local government; the proceeds of such a fee cannot exceed the actual cost of providing the facility.

Public Transportation

Cities may own and operate public transportation systems, although only a few cities now do so. A small but growing number of counties operate bus or van transit systems to serve unincorporated areas. The principal local revenue source for public transportation is fares. County and city fare schedules are not subject to State Utilities Commission regulation.

Off-Street Parking

Both counties and cities may provide off-street parking and charge for the privilege of parking in such a facility on either a short- or long-term basis, although this service is much more common with cities than with counties. The revenue from these charges usually supports all operating costs and sometimes all debt service costs for off-street parking.

Airports

A variety of fees, charges, and rents raise revenue for an airport operation: landing fees; rentals of hangar space, terminal space, and land; franchise fees for ground transportation services; sale of gasoline, aircraft materials, and the like; and parking receipts.

Cable Television

Cities (but not counties) are authorized to establish and operate cable television systems, and one—Morganton—started doing so in 1992. The fees charged to subscribers are the basic revenue source.

Stormwater

Recent federal law has required larger cities and some counties in North Carolina and elsewhere to increase their stormwater management programs significantly. A number of local governments have established programs that will be operated as enterprises, with the principal revenue being a monthly charge to property owners, added to the water and sewer bill.

Hospitals

A county- or city-operated hospital typically charges in the same manner as a privately operated hospital does for patient care.

Ambulance and Rescue Services

A county or city that provides or contracts for the provision of ambulance services may charge fees for them. These fees may include a flat amount per trip within the county or city; a mileage charge for trips to distant locations; and scheduled charges for medically related services such as providing oxygen.

Cemeteries

Cities (but not counties) may operate cemeteries. The revenue sources for cemetery operations are the sale of plots and perpetual care, and fees for opening and closing graves and for setting monuments and markers.

Recreation and Cultural Activities

Counties and cities may operate recreation programs, art galleries, museums, auditoriums, coliseums, convention centers, libraries, and the like. A variety of support sources are available in this category of service: admission charges, concessions, facility rentals, and parking receipts. For most recreation and cultural programs, user charges are not the principal means of support; rather, the programs are largely financed by tax proceeds. Auditoriums and coliseums can more readily be supported by user charges. G.S. 153A-264 entitles any resident of a county or city that operates or contributes to a public library to free use of the library; user charges may be assessed as a penalty for overdue materials or to provide ancillary services but not for access to the library or its core services.

Other Local Revenues

Other local revenues for local governments include statutory fees charged by public officers; facilities fees assessed as part of the cost of court operation; fees that are incidental to regulation; special assessments; profits from ABC stores; investment earnings; and revenues from many miscellaneous sources.

Statutory Fees of Public Officers

At one time the entire cost of operating the offices of the county sheriff and register of deeds was financed by the statutory fees charged by these officers for the performance of official duties. They collected the fees, hired their own help, paid their own expenses, and kept the remainder as their compensation. Although this financing system has been abolished throughout the state, the statutory fees remain. They are collected by the sheriff or register of deeds and deposited in the county's general fund.

Sheriff

The sheriff collects fees for executing a criminal warrant and for serving any civil process paper. A sheriff who is also the jailer collects a jail fee from persons held awaiting trial, if the person being held is convicted. When conducting sales of real estate or personal property, the sheriff receives a commission plus reimbursement of associated expenses [G.S. 7A-304(a)(1), -311, -313].

Register of Deeds

The register of deeds collects fees for virtually every official act performed, ranging from the fee for issuing marriage licenses to fees for certifying probate instruments. The largest revenue-producing fee is for recording deeds and other instruments that affect land titles. Fees for recording security interests under the Uniform Commercial Code and for issuing marriage licenses are also major sources of revenue. In many counties, the fees received by the register of deeds exceed the cost of operating the office (G.S. 161-10).

Each county must deposit an amount equal to 1.5 percent of register of deeds fees collected under G.S. 161-10 with the state treasurer. This money is earmarked for a supplemental pension payment for eligible retired registers of deeds. In addition, 10 percent of the register's fees retained by the county must be used for computer and imaging technology in the register's office. Other than these provisions, there is no legal restriction on the use of register of deeds' fees paid into the county's general fund.

Court Facilities and Related Fees

The state assesses fees against criminal defendants and civil litigants to offset in part the costs of operating the court system. As part of these charges, an arrest fee is paid to the government employing the officer making an arrest or serving criminal process. In addition, a facilities fee for each court case is paid to the local government unit (usually the county) that provides the courtroom in which judgment in the case is rendered [G.S. 7A-304(a)(2), -305(a)(1), -306(a)(1), and -307(a)(1)]. (The current amounts of these fees are set out in Appendix 13-7.)

The proceeds of the facilities fee may be used only for providing courtrooms and related judicial facilities, including jails and law libraries. In most counties the fees barely cover the cost of utilities, insurance, and maintenance of the building(s) occupied by the court system. (Financing of the court system is discussed further in Article 36 of this book.)

Fees Incidental to Regulation

Local governmental regulatory programs frequently have associated fees and charges. The person being regulated is required to meet some or all of the costs occasioned by the regulated action. Programs that often have such fees and charges are building inspection, land use regulation, health and sanitation regulation, and the like.

The authority to impose reasonable charges for regulatory activities is subsumed in the power to regulate.²² There is no general statutory limit to such charges, although occasionally the amount of a regulatory fee is set by statute. A rough limit to reasonableness for these fees is the amount necessary to meet the full cost of a regulatory program. Fees and charges for regulatory programs may be used for any public purpose that counties or cities are authorized to undertake, except that fees imposed for public health and sanitation regulation [see G.S. 130A-39(g)] must be expended for public health purposes.

Impact Fees

In rapidly growing areas of the state, officials are seeking new ways to finance the many new public facilities needed to accommodate development. Impact fees are one device serving that need. These fees require a developer to pay a substantial capital fee upon the issuance of a building permit, and the local government then uses the proceeds of the fees to construct new public infrastructure, such as streets, utilities, parks and open spaces, and other facilities. A county or city may impose impact fees for water and sewer infrastructure under existing general law. For other sorts of facilities, however, local legislation is necessary from the General Assembly. Several counties and cities have received such legislation, and others are watching those governments' experiences to decide whether they should seek comparable legislation.

Special Assessments

Special assessments are levied against property to pay for public improvements that benefit that property. Like user charges and unlike property taxes, special assessments are levied in some proportion to the benefit received by the assessed property. Unlike user charges, special assessments are levied against property rather than persons and are typically for public improvements rather than for services. Although special assessments are a relatively minor revenue source in the overall revenue picture of North Carolina's cities and counties, they are significant in reimbursing the units that use them for such projects as extensions of water distribution or sewage collection lines or construction of streets or sidewalks.

As of August 2008, there are two different statutory methods to levy special assessments in North Carolina, which are summarized below as Special Assessment Methods A and B. The authorities overlap in some respects but provide two distinct methods to levy the assessments.

Special Assessment Method A

Under G.S. 153A-185 and 153A-206, counties may levy special assessments to finance the following public improvements:

1. water systems
2. sewage collection and disposal systems (including septic tank systems)
3. beach erosion control and flood and hurricane protection works; watershed improvement, drainage, and water resources development projects
4. the local cost of improvements made by the Department of Transportation to subdivision and residential streets outside municipalities
5. street light maintenance

Although most special assessments are levied for capital projects, counties may also levy them on benefiting property for annual maintenance and operating costs for beach erosion control or flood or hurricane protection works (G.S. 153A-204.1) and street lights (G.S. 153A-206).

22. Homebuilders Ass'n of Charlotte v. City of Charlotte, 336 N.C. 37, 442 S.E.2d 45 (1994).

Under G.S. 160A-216 and 160A-238, cities may levy special assessments to finance the following public improvements:

1. streets
2. sidewalks
3. water systems
4. sewage collection and disposal systems (including septic tank systems)
5. storm sewer and drainage systems
6. beach erosion control and flood and hurricane protection works

The amount of each assessment must bear some relationship to the amount of benefit that accrues to the assessed property.

The most common basis of assessment is front footage: each property is assessed on a uniform rate per foot of property that abuts on the project. Other bases include the size of the area benefited and the value added to the property because of the improvement.

The governing board may levy the special assessments without a petition except for street and sidewalk improvements. For such improvements a county must first receive a petition requesting the assessments from 75 percent of the property owners to be assessed, and those who petition must own at least 75 percent of the frontage on the street. In a city the comparable percentages are a majority of the owners and a majority of the frontage.

The assessments may be paid (and often are) in up to ten annual installments along with interest on the amount outstanding in any year. Assessment revenue, including the interest portion, generally is not earmarked and may be used for any public purpose. Local improvements are often financed from special-assessment revolving funds; assessment revenues generated from finished projects are used to finance new improvements.

The special assessments may not be levied until the improvement being financed has been completed. Therefore the county or city must advance its own funds to construct the improvement.

Special Assessment Method B

Under G.S. 153A, Article 9A, and G.S. 160A, Article 10A, both counties and cities may levy special assessments to finance the following public improvements:

1. sanitary sewer systems
2. storm sewers and flood control facilities
3. water systems
4. public transportation facilities
5. school facilities
6. streets and sidewalks

The projects must be financed, at least in part, by revenue bonds issued by the unit, with the special assessments pledged as collateral for the borrowing. Additional financing sources may include general obligation bond proceeds or unrestricted general fund revenues.

Before imposing a special assessment, a local unit must receive a petition for the project to be financed by the assessment signed by at least a majority of the owners of real property to be assessed and who represent at least 66 percent of the assessed value of all real property to be assessed. The petition must include a statement of the project, an estimate of the cost of the project, and an estimate of the portion of the cost of the project to be assessed.

The special assessments may be imposed before the costs of the project are incurred by the unit, based on the governing board's cost estimates. The amount of the assessment must bear some relationship to the amount of benefit that accrues to the assessed property. The governing board may authorize the assessments to be paid, with interest, in up to thirty annual installments.

Profits from ABC Stores

Both counties and cities may establish and operate ABC stores. By the end of 2005, forty-eight counties had their own ABC systems, while there were three combined county–municipal systems and 102 city systems. Together, these local systems generated about \$57 million in annual profits. Net profits equal gross sales minus state taxes; the per-bottle add-on tax; the cost of goods; the contributions for ABC law enforcement, education, and rehabilitation programs for alcoholics; and operating expenses. About 80 percent of the net profits are distributed to the units that are authorized to share in the profits. The rest of the profits are kept by the ABC systems as working capital.

ABC profits are constitutionally subject to no limitations except public purpose. However, local acts of the General Assembly frequently earmark all or some portion of a system's profits.

Investment Earnings

G.S. 159-30 authorizes counties and cities to invest their idle cash. Funds for investment come from bond proceeds, capital and operating revenues, and fund balances. Local governments' most common investments are certificates of deposit in banks and savings and loan associations, obligations of the U.S. government (called "treasuries"), obligations that mature no later than eighteen months from the date of purchase of certain agencies set up under federal law (called "agencies"), and the North Carolina Capital Management Trust, a mutual fund for local government investment. The interest earned on investments must be credited proportionately to the funds from which the moneys that were invested came.

The importance of investment income fluctuates from year to year because of changes in short-term interest rates. North Carolina's local governments sometimes earn investment income that is the equivalent of five or more cents on the property tax rate, exclusive of income on invested bond proceeds. For total cash and investments, and investment earnings of North Carolina counties for recent years, see Appendix 13-8. The ups and downs in earnings reflect shifts in interest rates from one year to another.

Minor Sources

Local governments have numerous minor sources of local revenue. For example, many units receive payments from other local governments for joint or contractual programs. Some units receive funds from the management of their property, such as from leasing of county-owned building space or land, or sale of surplus equipment. Further, counties and cities receive refunds on the state sales taxes that they pay. Occasionally a local government receives a bond forfeiture from a prospective vendor or a contractor.

Additional Resources

Campbell, William A. *North Carolina City and County Privilege License Taxes*, 5th ed. Chapel Hill, N.C.: Institute of Government, University of North Carolina at Chapel Hill, 2000.

Lawrence, David M. *Local Government Finance in North Carolina*, 2d ed. Chapel Hill, N.C.: Institute of Government, University of North Carolina at Chapel Hill, 1990.

David M. Lawrence and **Kara A. Millonzi** are School of Government faculty members whose interests include the legal aspects of local government finance.

Appendixes

Appendix 13-1. Total County and Municipal Property Tax Levies, Selected Years

Fiscal Year	Total County Levies	Total Municipal Levies
1990—1991	\$1,660,134,729	\$ 687,891,579
1995—1996	2,392,106,387	883,712,276
2000—2001	3,377,402,521	1,318,265,598
2002—2003	3,911,185,715	1,500,740,927
2004—2005	4,326,784,544	1,663,373,556
2005—2006	4,669,143,970	1,751,740,005

Source: North Carolina Department of Revenue, Statistical Abstract of North Carolina Taxes 2006, Part IV, Local Government Taxes and Revenues, Table 60, Tax Levies of Local Governments by Type of Tax, accessed on the Internet at www.dor.state.nc.us/publications/abstract/index.html.

Appendix 13-2. Assessed Valuation of Property Subject to Taxation, Selected Years

Fiscal Year	Property, Unincorp. Areas	Property, Incorp. Areas	Total
1990—1991	\$125,412,804,970	\$122,826,033,966	\$248,238,838,936
1995—1996	170,707,500,540	178,422,329,157	349,129,829,697
2000—2001	233,017,556,599	284,349,922,593	517,367,479,192
2002—2003	262,553,139,693	327,208,092,118	589,761,231,811
2004—2005	295,394,343,744	374,081,212,905	669,475,556,649
2005—2006	315,654,933,221	402,959,798,899	718,614,732,120

Source: North Carolina Department of Revenue, Statistical Abstract of North Carolina Taxes 2006, Part IV, Local Government Taxes and Revenues, Table 69, Assessed Valuation of Property Locally Taxable by Location, accessed on the Internet at www.dor.state.nc.us/publications/abstract/index.html.

Appendix 13-3. Functions Included in Groups I, II, and III for Purposes of the Property Tax

The legislation establishing the three-group system for property taxes specifically lists each function in Groups I and II. Any function that a county or city is authorized to perform that is not listed in Group I or Group II is automatically in Group III. The Group III listing in this table, then, is not necessarily as complete as the Group I and Group II listings. Every effort has been made to include all functions, but omissions are possible. The fact that a particular authorized function is not listed at all does not mean that property taxes may in no circumstances be expended for that function. Rather, the function is a Group III function and was inadvertently omitted from the list.

Counties

Group I Functions

Courts	Jails
Debt service	Schools
Deficits	Social services (mandated programs)
Elections	Joint undertakings of the above

Group II Functions

General administration	Libraries
Air pollution control	Mapping
Airports	Medical examiner or coroner
Ambulance/emergency medical	Mental health
Animal protection and control	Open space
Armories	Parking
Arts programs and museums	Planning and regulation of development
Auditoriums, coliseums, and convention centers	Ports and harbors and cooperative programs with N.C. Ports Authority
Beach erosion and natural disasters	Public transportation
Cemeteries	Railway corridor preservation
Civil preparedness	Recreation
Debts and judgments	Register of deeds
Defense of officers and employees	Sewage collection and treatment
Economic development	Social services (nonmandated programs)
Fire protection	Solid waste collection and disposal
Forest protection	Stormwater and drainage
Health	Veterans' service officers
Historic preservation	Water supply and distribution
Hospitals	Water resources projects
Housing	Watershed improvement projects
Human relations programs	Joint undertakings of any of the above
Industrial development	
Law enforcement or sheriff's department	

Group III Functions

Community action	Redevelopment
Community development	Sedimentation control
Employment service offices	Streets
Game commissions	Joint undertakings of any of the above
Manpower programs	

Appendix 13-3. Functions Included in Groups I, II, and III for Purposes of the Property Tax (continued)

 Cities

Group I Functions

Debt service	Suppression of riots and civil disorders
Deficits	

Group II Functions

General administration	Industrial development
Air pollution control	Jails
Airports	Law enforcement
Ambulance and rescue squads	Libraries
Animal protection and control	Mosquito control
Arts programs and museums	Open space
Auditoriums, coliseums, and convention centers	Parking
Beach erosion and natural disasters	Planning and regulation of development
Cemeteries	Ports and harbors and cooperative programs with N.C. Ports Authority
Civil defense	Public transportation
Community development	Railroad corridor preservation
Debts and judgments	Recreation
Defense of officers and employees	Senior citizens programs
Drainage	Sewage collection and treatment
Economic development	Solid waste collection and disposal
Elections	Streets
Electric power	Traffic control and on-street parking
Fire protection	Urban redevelopment
Gas transmission and distribution	Water supply and distribution
Historic preservation	Water resources projects
Housing	Watershed improvement projects
Human relations programs	Joint undertakings of any of the above

Group III Functions

Armories	Employment service offices
Cable television	Manpower programs
Stormwater	Joint undertakings of any of the above
Community action programs	

Appendix 13-4. North Carolina Local-Option Sales and Use Tax Revenue, Selected Years

Fiscal Year	Counties (in millions)	Cities (in millions)
1985–1986	\$ 340.9	\$144.7
1990–1991	624.8	271.7
1995–1996	933.0	356.1
2000–2001	1,163.9	505.1
2002–2003	1,210.0	507.8
2004–2005	1,612.3	664.0
2005–2006	1,706.0	707.4

Sources: 1985–1986, from David M. Lawrence and Warren Jake Wicker, *Municipal Government in North Carolina*, 2d ed. (Institute of Government 1995), 221. Subsequent years from North Carolina Department of Revenue, Statistical Abstract of North Carolina Taxes 2006, Part IV, Local Government Taxes and Revenues, Table 60, Tax Levies of Local Governments by Type of Tax, accessed on the Internet at www.dor.state.nc.us/publications/abstract/index.html.

Appendix 13-5. Total Distributions, State-Shared Taxes, Selected Years

(Totals stated in millions)				
Fiscal Year	Beer/Wine	Utility Franchise	Telecommunications	Motor Fuels
1990–1991	\$ 21.0	\$ 121.5	—	\$ 81.3
1995–1996	22.5	136.7	—	104.9
2000–2001	26.0	194.0	—	133.2
2002–2003	27.4	150.0	\$ 55.2	130.2
2004–2005	29.8	156.4	56.2	135.3
2005–2006	30.2	163.1	53.9	136.9

Source: North Carolina Department of Revenue, Statistical Abstract of North Carolina Taxes 2006, Part IV, Local Government Taxes and Revenues, Table 62, Local Government Shares of State Administered Tax Levies by Types of Taxes, accessed on the Internet at www.dor.state.nc.us/publications/abstract/index.html.

Appendix 13-6. Powell Bill Distribution Amounts, Recent Years

Distribution Year	Per Capita Amount	Per-Mile Amount
2000	\$ 25.37	\$ 1,816.88
2003	21.38	1,557.47
2004	23.43	1,718.80
2005	23.20	1,709.23
2006	22.63	1,685.56

Sources: North Carolina Department of Transportation, Program Development Branch, Powell Bill, North Carolina State Street-Aid Allocations to Municipalities, Reports for 2000, 2003, 2004, and 2005, the latter two accessed on the Internet at www.ncdot.org/financial/fiscal/ExtAuditBranch/Powell_Bill/powellbill.html.

Appendix 13-7. Court-Related Fees Coming to Local Governments

Fee	Amount	Citation
Arrest fee, to county or city whose officer made arrest	\$ 5.00	7A-304(a)(1)
Criminal facilities fee, to unit providing court facility		
District court	12.00	7A-304(a)(2)
Superior court	30.00	7A-304(a)(2)
Pretrial release services fee, to county	15.00	7A-304(a)(5)
Crime laboratory fee, to local government operator	300.00	7A-304(a)(8)
Civil facilities fee, to unit providing court facility		
Magistrate	12.00	7A-305(a)(1)
District or superior court	16.00	7A-305(a)(1)
Special proceedings in superior court	10.00	7A-306(a)(1)
Estates facilities fee, to unit providing court facility	10.00	7A-307(a)(1)

Appendix 13-8. Total Cash and Investments and Investment Earnings for North Carolina Counties, Recent Years

Cash & Investments	2006	2005	2004	2003
Held in Debt				
Service Funds	\$97,810,901	\$115,412,533	\$59,445,158	\$46,135,089
Held in Construction				
Funds	983,923,839	997,979,944	600,725,805	988,041,215
Held in All Other Funds (except agency funds)	4,152,854,757	3,925,154,833	3,378,879,491	3,235,230,850
Investment Earnings				
On Bond Proceeds	\$33,807,549	\$24,409,174	\$11,361,892	\$14,289,560
On All Other Funds	176,107,624	97,893,380	41,975,648	66,118,791

Source: North Carolina Department of State Treasurer, Annual Financial Information Report Forms for 2003–2006, accessed on the Internet at www.treasurer.state.nc.us/DSTHome/StateAndLocalGov/AuditingAndReporting/AFIR.hAptm.

