

TO: ALL NORTH CAROLINA PUBLIC SCHOOL SYSTEM ADVOCATES

**RE: A STUDY OF NORTH CAROLINA DEPARTMENT OF REVENUE (NCDOR)
SALES TAX AND REFUND POLICIES IMPACTING FRANKLIN COUNTY
SCHOOLS AND LOCAL GOVERNMENT**

Attached, please find a copy of the Study undertaken by Bob Radcliffe of the Ben Franklin Society in support of its commitment to the Public School System of Franklin County, North Carolina.

The impetus for this Study evolved from the Society's involvement as a Business Partner with the Franklin County Early College High School (ECHS) that was facilitated by the recently formed Franklin County Educational Foundation.

In response to the dire need to provide each ECHS student with access to a portable Chromebook Computer, the Society committed to secure private industry funds for the purchase of 120 additional Computers and 4 companion Teaching Carts.

In the course of preparing a Grant Proposal to NOVOZYMES for this purpose, Bob discovered that NCDOR was only ONE of FIVE STATES that imposes Sales Tax on such purchases. In particular, nearly \$2000 of Sales Tax was required to requisition FOUR Teaching Carts with 30 computers each.

Bob Radcliffe felt this was an incredible cost and initiated research to unveil why this was so. His efforts over several months confirmed the fact that the general public and nearly all responsible parties involved were totally unaware of this fact.

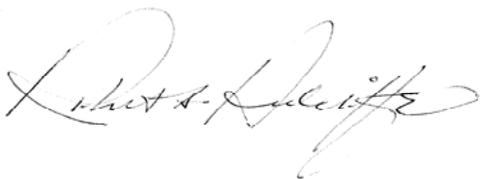
Bob concluded that a thorough, accurate study of the underlying issues was needed, and the attached Study Document fulfills that need.

Three RECOMMENDATIONS are included within the report.

It is hoped that Policy changes will be made to remedy the inequities of present NC Sales Tax Policy.

Please direct any questions, comments or corrections to Bob Radcliffe by emailing bob@lynchcreek.com

Feel free to redistribute this Letter and attached Study Document to others as you see fit.



COVER LETTER
Monday, July 24, 2017

FRANKLIN COUNTY, North Carolina
NCDOR Sales Tax Reform Study
Final Version - Monday, July 24, 2017

What is this document?

A Sales Tax process description of how Franklin County and the Franklin County Public School System – separate NC Department of Revenue (NCDOR) Account ID’s (Entities) – who may secure available Refunds of State and Local Sales Tax. Presently the State Sales Tax Rate is 4.75% and the Local (County) Sales Tax Rate is 2.00%

Why is this document needed?

A broad public misunderstanding exists about the State and Local Sales Tax obligations of FRANKLIN COUNTY and the FC SCHOOL SYSTEM. Presently, both are ARE NOT Tax Exempt. No one seems to understand that the FC SCHOOL SYSTEM pays Sales Tax on purchases like classroom books and computers. Refunds of such Taxes from NCDOR are possible, but differ between the two Tax Entities. This document will explain these differences, how each Entity may secure Refunds for its Purchases, and provide recommended Process Improvement Options.

How might this document impact Public Policy?

It is hoped that by understanding the complexity and cost of securing State and Local Sales Tax Refunds, the argument for eliminating the Sales Tax altogether for Local Educational Agencies (LEA’s) statewide will be strengthened. When asked the question “Why Does NC Impose a Sales Tax, then Offer a Refund?” the best answer quite simply is “Eliminate the Sales Tax for Local Government and LEA’s Altogether”.

How are Refunds presently handled by NCDOR?

Refunds for Governmental Entities may only be filed once per Fiscal Year (normally July 1st thru June 30th) within 6 months of the Fiscal Year end date. Refund payments by NCDOR are normally made within 6 months. Refunds must be sought within 3 years; otherwise, they are forfeited to NCDOR.

FRANKLIN COUNTY

Not Tax Exempt

Both State and Local Sales Tax Refunds are Available

FC SCHOOL SYSTEM

Not Tax Exempt

Only County Sales Tax Refunds are Available (Effective July 1, 2005)

Definition of “Not Tax Exempt” Entity

Both State and Local Sales Taxes on purchases must be collected and submitted to the NC Department of Revenue (NCDOR).

Definition of “Refunds are Available”

Subsequent to payment, State and Local Sales Tax Refunds may be requested annually from the NCDOR using Form E-585. Refunds to all Entities are not automatic and subject to periodic audit by NCDOR.

CURRENT PROCESS OBSERVATIONS

- 1) FRANKLIN COUNTY and the FC SCHOOL SYSTEM are separate NCDOR Entities.
- 2) Both Entities have separate Finance Departments. All Purchasing and Refund processing is presently handled separately.
- 3) Both are “NOT TAX EXEMPT” and therefore must pay State and Local Sales Tax on all purchases
- 4) FRANKLIN COUNTY may however file for BOTH State and County Sales Tax Refunds Annually, effectively negating any Sales Tax Revenue for NC.
- 5) FC SCHOOL SYSTEM may ONLY file for Local Sales Tax Refund Annually, and thereby pays a 4.75% Sales Tax on all school purchases.

CURRENT PROCESS CONCLUSIONS

- A) FRANKLIN COUNTY pays State and Local Sales Tax on all purchases, receives payment from NCDOR for ALL such County Sales Tax paid, but must file annually for the Refund of ALL State Sales Tax paid.
- B) FC SCHOOL SYSTEM pays State and Local Sales Tax on all purchases, but may ONLY recover the Local Sales Tax portion by filing for a Refund annually. All State Sales Tax payments (4.75%) are retained by NCDOR.
- C) It is estimated that in 2016, the FC SCHOOL SYSTEM was refunded \$75,500 Local Sales Tax. If the FC School System had received a State Sales Tax Refund as well, an additional \$178,125 would have been realized.
- D) There are presently significant administrative costs both for Franklin County and NCDOR to refund taxes. There are sizeable statewide cash flow impacts as well to prepay Sales Tax and then wait up to 1.5 yrs for a Refund. Additionally, the required periodic NCDOR auditing of 370+ Entities statewide cannot be ignored.
- E) Ideally, both FRANKLIN COUNTY and the FC SCHOOL SYSTEM should be granted a Sales Tax Exemption by NCDOR thereby eliminating the unnecessarily burdensome administrative costs now incurred by the taxpayers of North Carolina.
- F) If FRANKLIN COUNTY made all purchases for the FC SCHOOL SYSTEM, it could then recover the State Sales Tax portion presently paid by the FC SCHOOL SYSTEM, and by arrangement, transfer that Refund amount to the FC SCHOOL SYSTEM, thereby circumventing present law.

PROCESS IMPROVEMENT RECOMMENDATIONS

OPTION-1

FRANKLIN COUNTY and the FC SCHOOL SYSTEM should act to circumvent all Sales Tax liability by consolidating its Purchasing operations. The 4.75% State Sales Tax on FC SCHOOL SYSTEM purchases could then be REFUNDED to FRANKLIN COUNTY and the savings credited back to the FC SCHOOL SYSTEM. There are however, associated accounting implementation, coordination and auditing costs required to achieve an expected savings of \$175,000+ per year.

OPTION-2

NCDOR could grant a Sales Tax Exemption for all 100 COUNTY GOVERNMENTS, thereby eliminating all present State and Local administrative overhead with NO LOSS OF REVENUE.

OPTION-3

NCDOR could grant a Sales Tax Exemption for all LEA's (over 270 Public and Charter Schools), thereby eliminating all present State and Local administrative and auditing costs. NCDOR would then join company with 45 other States that DO NOT TAX public school purchases, leaving only Arizona, California, South Carolina and Washington that tax public school purchases.

<p>There appears to be no reason for NCDOR to continue taxing Local Government and Educational Agencies. If these Entities collaborate, No REVENUES are actually generated, but significant COSTS are incurred. (SEE Appendix A: NCSBA Brief)</p>
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ACKNOWLEDGEMENTS

Bob Radcliffe, Ben Franklin Society President initiated the creation and authored this document as an outgrowth of its organizational support for Public Education in Franklin County as Business Partner to the FC Early College High School (ECHS).

Angela Harris, Franklin County Manager, facilitated the investigation of this matter.

Chuck Murray, Franklin County Finance Director collaborated with Bob Radcliffe and provided essential details.

Douglas Hale, FC School System Chief of Finance assisted Chuck Murray.

CERTIFICATION

The information provided herein is complete and accurate. This document is authorized for public distribution.

**BEN FRANKLIN SOCIETY
NCDOR SALES TAX & REFUND POLICY STUDY**

APPENDIX-A

**NORTH CAROLINA SCHOOL BOARDS ASSOCIATION (NCSBA)
SALES TAX REFUND/EXEMPTION ISSUE BRIEF**



Sales Tax Refund/Exemption Issue Brief

Background

From 1998 until 2005, local boards of education were able to provide additional educational opportunities with savings from State and local sales and use tax refunds. A 2005 budget provision revoked LEA sales and use tax refund authority and attempted to supplant the estimated \$33.3 million in lost revenues by authorizing a quarterly transfer of revenue to the State Public School Fund.¹ The provision ultimately amounted to a shell game in which public schools were still short changed \$33.3 million.

During the 2006 legislative session, the General Assembly reinstated local school boards' authority to apply for the local sales tax refund, but declined to do likewise with regards to the State sales tax refund.² Today school districts remain one of the few public entities that cannot apply for a State sales tax refund at a cost the General Assembly's Fiscal Research Division has estimated to exceed \$40 million a year.³

NCSBA Position

Many other entities, including cities, counties, public universities, charter schools, private schools, and other non-profits, can apply for a State sales tax refund or exemption; no entity in recent history, other than public schools, has lost this ability. Even after a comprehensive tax reform, local boards are still excluded and are rightly troubled at being excluded from the group of entities eligible for a State sales tax refund.

One of the most problematic aspects of school districts' inability to apply for a State sales tax refund is that no alternative revenue options are available to supplant the lost funds. County governments are already appropriating almost \$2.7 billion per year for public school operating costs and bearing the primary burden for an estimated \$8.2 billion in school facility needs.⁴

Inability to apply for a State sales tax refund is costly for districts that are building or renovating schools. A 2009 report from the General Assembly's Joint Education Oversight Committee found that without authority to apply for a State sales tax refund many school districts are resorting to a burdensome, wasteful, and highly inefficient exercise of transferring title to their buildings to the county during the construction phase so that the county can apply for the sales

¹ S.L. 2005-276, sec. 7.51(a).

² S.L. 2006-66 sec. 7.20(a).

³ Given the fiscal climate of many school districts today, this number may be lower.

⁴ NC DPI. Five-Year Public School Facility Needs Assessment. 2010-11. Accessed at

<http://www.schoolclearinghouse.org/otherinf/FacilityNeedsSurvey/FacilityNeedsSummary2011Final.pdf>

tax refund on the school district's behalf⁵. The Committee found that "there are reports of significant costs related to these property transfers, and that the ability to engage in such transfers varies depending on the relationship between the school board and county commissioners." Districts that cannot transfer their capital costs, meanwhile, have delayed necessary renovations longer than they otherwise would because of the added costs. Some school boards are also entering into similar agreements with their county commissions whereby school supplies and equipment are purchased by the county commissions and transferred to the school board so the refunds on sales taxes paid can be realized. This practice raises its own set of concerns, including whether the applicable equipment warranties can be validly transferred from the county commission (the original purchaser) to the school board. Reinstating school district sales tax refunds/exemptions would eliminate these costly and wasteful transactions.

In addition to shorting public schools \$33.3 million on net, the attempt to supplant the funds lost through the lost sales tax refunds has essentially amounted to a transfer of wealth among school districts. Those districts that spend great sums on capital purchases or incur large sales tax liability subsidize those districts that can successfully transfer property to their county commissions to receive a refund or have relatively low sales tax exposure. The end result has been a net loss to public schools statewide, with negative repercussions on classroom operations and the delivery of quality educational services across the state.

NCSBA takes no position on the underlying policy of whether sales tax refunds/exemptions should be retained or abolished. NCSBA does request that public schools be treated equally as other entities. If North Carolina's tax code is going to continue to allow numerous entities, including other governmental entities, to not pay sales tax, then local boards of education should either be granted a sales tax exemption or have their sales tax refund reinstated.

⁵Joint Legislative Education Oversight Committee Report 2009.
<http://www.ncleg.net/documentsites/committees/JLEOC/Report%20to%20the%20General%20Assembly%20Session/Archives/2009%20Ed%20Oversight%20Report.pdf>