
Coates' Canons Blog: A New Tax Benefit for New Homes

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North Carolina auto dealers don't pay property taxes on the thousands of new and used cars sitting in their lots awaiting buyers. Walmart doesn't pay property taxes on the massive amount of stuff for sale at its nearly 100 big-box stores sprinkled across the state. Should North Carolina's home builders get the same tax benefit for their growing inventories of unsold new homes?

The home builders' lobby has long thought so, but until this legislative session the General Assembly had declined to include newly constructed homes on the lengthy list of properties that receives beneficial tax treatment. Goods and raw materials in the hands of manufacturers, wholesalers and retailers are exempt from local property taxes under the inventory exclusions in N.C.G.S. 105-275(32a), (33) and (34). However, these exclusions provide no benefit to home builders because homes are considered improvements to real property rather than goods.

As the economic crisis continued to pound the real estate market earlier this year, the pressure on the General Assembly to provide some relief for the home building industry grew. The volume of home sales across North Carolina dropped 28% in the first half of 2009 as compared to the first half of 2008, while the average time on market for new homes doubled from six months in 2007 to twelve months in 2009. The General Assembly responded with S.L. 2009-308, a bill that gives home builders some but not all of what they sought.

Newly constructed homes are still not considered exempt inventory. But beginning in 2010 new home builders will be able to *defer* up to three years of property taxes on their unsold new homes. Only the taxes related to the home itself will be deferred; the land on which the home sits will be taxed as usual. The law contains a sunset provision that terminates the tax benefit for the 2013 tax year. Click here for a recent Property Tax Bulletin describing this bill and the seven other deferred property tax programs in more detail.

How much damage will this new exclusion cause to local government finances? Not much, according to an analysis by the General Assembly's Fiscal Research Division. The Legislative Fiscal Note accompanying the bill concludes that local governments statewide will temporarily lose between \$30 and \$35 million in 2010 and between \$7 and \$12 million in 2011. Counties and municipalities should then experience "minimal or positive impact" in subsequent years as the program sunsets and the deferred taxes are paid.

Several factors contribute to this relatively slight anticipated effect on local finances. The most obvious one, of course, is the sunset provision, which will terminate the exclusion after only three years. Another factor is the expected turnaround in the housing market that will (hopefully) reduce home builders' inventory each year; if the bill were effective for the 2009 tax year, the Fiscal Research Division estimated that it would have cost local governments about 50% more than it will in 2010. Finally, local revenues are helped by the fact that interest accrues on deferred taxes as if they had been payable without the deferral. When a new home sells, either the builder or the buyer will be required to pay not only the deferred taxes but also interest on those deferred taxes at roughly 10% per year.

The real concern for local governments is that this bill could turn out to be the nose of the camel peeking into the tent. If the economy doesn't improve as much as we hope it will, home builders soon may be back in front of the General Assembly asking that it welcome in the entire camel by completely excluding unsold new homes from property taxes. That would carry a much bigger and permanent price tag for local government than does S.L. 2009-308, of course. Stay tuned.



Links

- www.ncga.state.nc.us/EnactedLegislation/Statutes/HTML/BySection/Chapter_105/GS_105-275.html
- www.census.gov/const/newressales.pdf
- www.ncga.state.nc.us/Sessions/2009/Bills/House/PDF/H852v5.pdf
- www.sog.unc.edu/pubs/electronicversions/pdfs/ptb149.pdf
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