REVISED

DEPARTMENT OF TAXATION
2001 Fiscal Impact Statement

1. Patron Parrish

2. Bill Number HB 1994

House of Origin:
X **Introduced**
_____ **Substitute**
_____ **Engrossed**

3. Committee House Finance

4. Title Income and Personal Property Taxes: Imposition and Administration

Second House:
_____ **In Committee**
_____ **Substitute**
_____ **Enrolled**

5. Summary/Purpose:

This bill would increase the corporate income tax rate and the individual income tax rates in each tax bracket by 1%. The additional income tax revenues would be distributed to localities based on the residence of each individual taxpayer (individual income tax) and each locality's share of total full-time employees (corporate income tax). This bill would also limit the tax rate localities could levy on personal property at $0.01 per $100 of assessed value.

This bill would be effective for taxable years beginning on or after January 1, 2002.

6. Fiscal Impact Estimates are:

6a. Expenditure Impact:

Fiscal Year	*Dollars*	*Positions*	*Fund*
2000-01	$0	0	GF
2001-02 *****	$196,950	0	GF
2002-03 *****	$217,000	6	GF

*** Does not include systems costs. (See line 8.)**

6b. Revenue Impact:

	State Revenues	
Fiscal Year	*General Fund*	*Special Fund*
2000-01	$0	$0
2001-02	$0	$441.1 million
2002-03	$0	$92.6 million
2003-04	$0	$28.9 million

	Local Revenues		
Fiscal Year	***Distribution from Special Fund***	***Tangible Personal Property Tax***	***Net***
2000-01	$0	$0	$0
2001-02	$368.8 million	<$670.9 million>	<$302.1 million>
2002-03	$1.67 billion	<$2.04 billion>	<$378.9 million>
2003-04	$1.79 billion	<$2.20 billion>	<$412.5 million>

7. **Budget amendment necessary:** Yes.
   Items: <u>Page 1, Revenue Estimates</u>
   <u>279 and 281, Department of Taxation</u>

8. **Fiscal implications:**

Administrative Costs

The department would be reimbursed for any direct costs associated with the administration of this bill from the additional income tax revenues.

While this bill does have costs associated with systems development, these cannot be ascertained at this time. The cost for implementing a **single** piece of legislation cannot be calculated precisely due to economies of scale. The actual cost to implement **all** legislation enacted during a given session will more than likely be less than the sum of the costs attributed to individual bills. Further, the ability to accurately predict costs is complicated because the department is replacing its current database system. As a result, legislative changes may need to be made to both the current and the future system, depending on the effective date. Therefore, the department is not providing specific systems costs for this bill, but will calculate the total for all tax bills once they have been acted upon favorably in both houses and prior to the conference committee report.

If the suggested amendments are adopted, the department's other administrative costs associated with this bill are estimated to be $196,950 in Fiscal Year 2002 for revised withholding and tax tables. Administrative costs would be $217,000 in Fiscal Year 2003 for additional equipment for the creation of 6 full time positions. Ongoing costs for Fiscal Year 2004 and thereafter would be $183,000. If the suggested amendments are not adopted, the department would incur additional processing costs of $400,000 annually beginning in Fiscal Year 2002.

Revenue Estimate

While this bill would not effect General Fund revenue, the additional income tax revenue generated as a result of this bill would be deposited into the General Fund and transferred monthly to a special fund called the Collections of Local Income Tax Revenues (the "Fund"). Revenues deposited into the Fund would be designated for distribution to localities to replace revenue lost from the reduction in tangible personal property tax rates. Because distributions would be made from the Fund at the end of each calendar quarter, a lag would occur between the time deposits are made to the Fund and distributions are made to localities. As a result, the Fund would experience net revenue increases of an estimated $441.1 million for Fiscal Year 2002, $92.6 million for Fiscal Year 2003, and $28.9 million for Fiscal Year 2004.

It is estimated that the reduction in the rate at which localities could impose the tangible personal property tax would reduce local revenues by an estimated $670.9 million in lost personal property tax revenues for Fiscal Year 2002, $2.04 billion for Fiscal Year 2003, and $2.2 billion for Fiscal Year 2004. Because of the lag time explained above, the net effect on local revenues would be an estimated decrease of $302.1 million for Fiscal Year 2002, $378.9 million for Fiscal Year 2003, and $412.5 million for Fiscal Year 2004. Also, because income tax revenues would not be distributed to localities in proportion to lost revenues, some localities will experience net revenue losses and some net revenue increases regardless of the net effect for all localities.

9. Specific agency or political subdivisions affected:

State Comptroller
Localities
Department of Taxation

10. Technical amendment necessary: Yes.

The department believes that the intent of the new *§ 58.1-320.1* E this bill would create is to ensure that localities would continue to be reimbursed under the Personal Property Tax Relief Act of 1998, but based on the personal property tax rate of one cent per $100 of assessed value this bill would establish. However, the Personal Property Tax Relief Act of 1998 reimburses localities based on the first $20,000 of the assessed value of qualifying vehicles using the rates in effect in the locality on August 1, 1997. If it is the intent of this bill to reimburse localities using the rate of one cent per $100 of assessed value; an amendment to the Personal Property Tax Relief Act of 1998 would be required. In order to make this amendment, an amendment in the nature of a substitute would be necessary.

In order for the department to administer the distributions to localities proposed in this bill (see discussion on line 11 below), the following amendments are suggested:

Page 1, Line 49, After: based on
Strike: on each taxpayer's residence
Insert: the relative share of the total individual income tax paid by taxpayers filing returns in each locality

Page 1, Line 50, After: § 58.1-320.1.
Strike: For purposes of this article, an individual shall be deemed to be a resident of any county or city in which the individual is domiciled at any time during the taxable year

or has maintained his place of abode for an aggregate of more than 183 days of the taxable year.

Page 2, Line 88, After: based on
Strike: each locality's share of total full-time employees, as determined by the Tax Commissioner.
Insert: where wages are earned. The amount of each locality's relative share of the total statewide wages earned according to the most recent Bureau of Labor Statistics ES202 data obtained from the Virginia Employment Commission annually shall be used to calculate this part of the formula.

11. Other comments:

This bill would effectively eliminate the tangible personal property tax by capping the rate that localities may impose at 1 cent per $100 of assessed value. In order to replace the lost local revenue, this bill would increase the corporate income tax rate by 1% (from 6% to 7%), and increase the rates for each of the individual income tax brackets by 1%. The following table shows how the individual income tax rates would change as a result this bill.

Individual Income Tax Rates

Income Brackets	Current Rates	Proposed Rates
Less than $3,000	2%	3%
$3,000 to $5,000	3%	4%
$5,000 to $17,000	5%	6%
More than $17,000	5.75%	6.75%

The added individual and corporate income tax revenue would be earmarked for distribution to localities. Distribution would take place in the first month after the end of each calendar quarter. Additional individual income tax revenue would be distributed to each locality to the extent generated by residents of that locality. Additional corporate income tax revenue would be distributed to localities according to their share of the state’s full-time workforce.

Proposed Amendments

Residency: The additional individual income tax revenue would be distributed based residency of individual taxpayers. For the purposes of this bill, an individual would be considered to be a resident of any county or city in which that individual is domiciled at any time during the taxable year or has maintained his place of abode for an aggregate of more than 183 days of the taxable year. It would be extremely difficult to verify the residency of an individual who moves from a locality to another during a taxable year or even after a taxable year but before the filing deadline. As such, the department has recommended amendments that would allow for the distribution of the additional individual income tax based on residency information provided on individual income taxpayers' returns for the taxable year being distributed. The department already captures this data.

Employment: The additional corporate income tax revenue would be distributed based on each locality's "share of total full-time employees." The Department of Taxation does not currently maintain employment data by locality. Such data is collected by the Virginia Employment Commission ("VEC") is based on wage reports submitted by employers. As such, the department has recommended an amendment that would allow for the distribution of the additional corporate income tax based on VEC wage reports. Employers that operate in more than one location are allowed to report all of their wages in the locality in which their operations are based. As a result, this data would include wages reported in one locality, but actually earned in another.

Other Legislation

House Bill 2017, House Bill 2446, Senate Bill 1165, and **Senate Bill 1218** would establish the Localities' Share of Individual Income Tax Revenue Fund. A portion of individual income tax revenues would be deposited into this fund for distribution to localities. The first deposit would be made by September 1, 2003, based on 2% of individual income tax collections for FY 2002. The percentage of individual income taxes deposited into this fund would increase 2% each year until it reaches 10% in 2007. Distributions to counties would be shared with towns located within the counties based on the towns' relative share of total population within the county.

House Bill 2036 and **House Bill 2867** would reduce the individual state income tax rates and authorize localities to impose a local income tax at rates equivalent to the reduction in the state income tax. These bills would also repeal the Personal Property Relief Act of 1998. In order for these bills to become effective, a Constitutional amendment would have to be ratified by voters exempting motor vehicles used for nonbusiness purposes from taxation.

House Bill 2249 would establish the Localities' Portion of State Tax Revenues Fund. 1% of individual income tax revenues would be deposited into this fund for distribution to localities. Distributions to localities would be based on each individual income taxpayer's residence. Distributions to localities would be made each September 1 of the year following the taxable year.

House Bill 2856 would make a number of changes to the individual income tax structure. The bill would also increase the corporate income tax rate and the individual income tax rates in each tax bracket by 1%. The additional income tax revenues would be distributed to localities based on the residence of each individual taxpayer (individual income tax) and each locality's share of total full-time employees (corporate income tax). The maximum tax rate localities could levy on any personal property would be reduced to $0.01 per $100 of assessed value.

Senate Bill 1083 would increase the retail sales and use tax and repeal the local tax on tangible personal property for certain motor vehicles and boats only if voters ratify a constitutional amendment exempting such motor vehicles and boats.

cc: Secretary of Finance

Date: 1/29/01/dtm
Document: S:\2001leg\WorkInProcess\OTPwork\House Bills\HB1994F161.doc