

**DEPARTMENT OF TAXATION  
2002 Fiscal Impact Statement**

1. **Patron** Whipple

3. **Committee** Senate Finance

4. **Title** Retail Sales and Use Tax: Refunds on  
Certain Energy Efficient Property

5. **Summary/Purpose:**

2. **Bill Number** SB 377

**House of Origin:**

  X   **Introduced**

       **Substitute**

       **Engrossed**

**Second House:**

       **In Committee**

       **Substitute**

       **Enrolled**

This bill would create a sales and use tax refund program for sales taxes paid on the purchase of large appliances and heating and cooling systems that meet certain energy efficiency requirements.

The sales tax refund program would be effective for sales taxes paid on or after January 1, 2003, and before January 1, 2007 on purchases of the qualifying appliances and equipment. The refund application must be filed with the Department of Taxation within one year from the date the tax is paid. The refunds would be limited to a maximum of \$500 in tax per qualifying item and the total amount of refunds received by an organization or person in a calendar year would be limited to \$5,000.

The amount of the refunds attributable to the 1% local sales and use tax would be deducted from the monthly distributions of sales tax revenues made to localities.

This bill would establish two new grant programs to be administered by the Department of Mines, Minerals and Energy (DMME) related to alternative energy use. The bill would create grant programs for: 1) corporations that produce electricity from certain renewable energy resources and 2) corporations and individuals that install photovoltaic property, solar water heating property, or wind-powered electrical generators. The bill refers to the grant programs as the Renewable Electricity Production Grant Program and the Photovoltaic, Solar, and Wind Energy Utilization Grant Program, respectively.

**NOTE:** This fiscal impact statement only addresses the sales and use tax refund program and the grant programs contained in this bill. Comments on the grant programs are based on information provided by DMME. The fiscal impact information relates to the sales tax refund program that would be administered by the Department of Taxation.

**6. Fiscal Impact Estimates are:** Tentative. (See Line 8.)

**6a. Expenditure Impact:**

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Fund</i>
2001-02	\$0	GF
2002-03	\$553,100	GF
2003-04	\$167,000	GF

**6b. Revenue Impact:**

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Fund</i>
2002-03	(\$2.2 million)	GF
2002-03	(\$0.4 million)	TTF
2002-03	(\$0.7 million)	Local
2003-04	(\$5.3 million)	GF
2003-04	(\$0.9 million)	TTF
2003-04	(\$1.8 million)	Local

**7. Budget amendment necessary:** Yes.

Page 1, Revenue Estimates  
Item 283, Department of Taxation

**8. Fiscal implications:**

Administrative

There are costs associated with modifying the system to implement this legislation. TAX is currently in the process of replacing its automated systems as part of a partnership with AMS. As a result, TAX will be maintaining two systems – the current STARS system and the new IRMS system – for a period of time as a contingency. The contract with AMS generally provides for the costs of implementing routine legislation. However, changes attributable to major legislation are not within the scope of the contract.

Because the scope of this legislation is significant, systems changes will not be paid through the AMS contract. Systems costs to implement this proposal would total \$377,000. In addition, the department would need to hire two full-time positions, at a cost of \$68,600, to review and process the refund requests. The department would incur costs of \$10,000 for equipment, \$90,000 for postage, and \$7,500 to develop forms and informational materials. It is estimated that the Department of Taxation's administrative costs would total \$553,100 in fiscal year 2003.

For fiscal year 2004 and beyond, the department would incur continuing costs of \$167,000 annually for personnel, forms, and postage. These costs assume there is no enforcement or verification required other than an office review of the refund requests.

### Revenue

This bill would have a negative impact on General Fund, Transportation Trust Fund, and local revenues. It is estimated that this bill would have a negative impact on state and local revenues of \$3.3 million (state: \$2.6 million; local: \$0.7 million) for fiscal year 2003 and \$8.0 million (state: \$6.2 million; local: \$1.8 million) for fiscal year 2004. The revenue estimates assume that sales tax refunds would be issued in the same fiscal year that the tax is paid. Energy Star efficiency requirements are expected to become more stringent in the future. Changes in these requirements could affect these estimates.

### **9. Specific agency or political subdivisions affected:**

Department of Taxation  
Department of Mines, Minerals and Energy

### **10. Technical amendment necessary:** Yes, as provided by DMME.

DMME has proposed amendments to this bill that would make the grant management requirements of this bill consistent with those in HB 746.

The first two amendments would amend the definitions of solar energy property and solar water heating property to include property that provides hot water associated with a property. As written, the bill's current definitions exclude solar water heating systems serving outdoor pools and equipment.

The third and fourth amendments would eliminate the requirement that DMME promulgate regulations to administer this bill. DMME believes that the grant programs in this bill could be administered more efficiently and effectively without regulations. The main requirements of the programs are clearly established in the legislation. DMME would prefer to let the application and procedures for the programs serve as guidance documents in much the same manner as the Photovoltaic Manufacturing Incentive Grant Program is currently administered. Removal of the requirement to promulgate regulations would be consistent with the provisions of Code of Virginia §§ 59.1-284.21.F and 59.1-284.31.F that provide that actions of DMME related to the allocation and awarding of grants are to be exempt from the provisions of the Administrative Process Act.

The final amendment would provide that the grant programs in this bill take effect only if funds are appropriated to administer them.

Page 4, Line 164, After: hot water for use

Strike: in  
Insert: associated with

Page 4, Line 168, After: hot water for use

Strike: within  
Insert: associated with

Page 5, Line 243, After: Tax Commissioner

Strike: ,  
Insert: and

Page 5, Line 243, After: Motor Vehicles

Strike: , and the Director of the Department of Mines, Minerals, and Energy

Page 5, Line 252, **at the beginning of the line**

Insert: 5. That the provisions of Chapters 22.5 and 22.6 of Title 59.1 shall become effective if the general appropriation act for 2002-2004 biennium provides funding to the Department of Mines, Minerals and Energy for implementation of this act.

#### **11. Other comments:**

This bill would create a refund program for retail sales and use taxes paid on purchases of various energy efficient appliances and heating and air conditioning equipment. Refunds would be available to any person or organization that pays sales and use taxes on the purchase of qualifying items on or after January 1, 2003. The refunds allowed by this bill would be limited to \$500 in tax paid per item and \$5000 in total tax paid for qualifying items by an organization or person in any calendar year.

Appliances that would qualify for a sales and use tax refund include clothes washers, room air conditioners, dishwashers, and standard size refrigerators that meet or exceed the energy star efficiency requirements established by the United States Environmental Protection Agency and the United States Department of Energy.

In addition, fuel cells that (i) generate electricity and heat using an electrochemical process; (ii) have an electricity-only generation efficiency greater than thirty-five percent; and (iii) have a generating capacity of at least two kilowatts, would qualify for the sales and use tax refund. The following heating and air conditioning equipment would also qualify for refunds:

- (1) natural gas heat pumps that have a coefficient of performance of at least 1.25 for heating and at least 0.70 for cooling;
- (2) electric heat pump hot water heaters that yield an energy factor of at least 1.7;
- (3) electric heat pumps that have a heating system performance factor of at least 8.0 and a cooling seasonal energy efficiency ratio of at least 13.0;
- (4) central air conditioners that have a cooling seasonal energy efficiency ratio of at least 13.5; and
- (5) advanced natural gas water heaters that have an energy factor of at least 0.65.

#### Dealer's Discount

This bill would *not* adjust the amount of the refunds to account for the dealer's discount allowed under Code of Virginia § 58.1-622. Dealers are compensated by the Commonwealth for accounting for and remitting the sales and use tax. This compensation is taken in the form of a discount on the sales and use tax return. Thus, the amount of refunds claimed under this proposal would exceed the actual amount of sales and use taxes remitted to the department by the dealers that collected the sales tax at the time the appliances or equipment were sold.

#### Local Tax Distribution

The Department of Taxation devotes a significant amount of resources to improve the distribution to Virginia localities of the 1% local option sales and use tax. These funds are a substantial revenue source for many localities and are closely tied to revenue fluctuations. Refund claims that do not accurately identify in which localities the purchases were made may result in the deduction of refunds from the revenue distributions for localities that did not receive the original tax payments.

#### Contractors

The department assumes that this bill would entitle contractors to refunds of sales and use taxes paid on qualifying purchases of heating and air conditioning equipment. The qualifying heating and air conditioning equipment in this proposal typically becomes real property when installed. Code of Virginia § 58.1-610 provides that any person who contracts to furnish and install tangible personal property that becomes real property upon installation is considered the final consumer of the property purchased for installation under the contract. Real property contractors must pay the sales and use tax on their purchases and include the tax in the price of the contract. The contractor does not separately bill sales and use tax to the customer. When homeowners or others hire a contractor to repair, install, or replace a heat pump or central air conditioning unit, the contractor, not the owner or lessee of the real property, would be eligible for the refund of

sales and use tax paid on the equipment. By law, the contractor is legally liable for payment of the tax and would be entitled to the tax refund under this proposal.

### Interest

This bill does not specify that interest would be paid on the refunds.

### Regulations and Public Information Materials

This bill would require the department to promulgate regulations to carry out the provisions of this legislation. The department would also be required to consult with manufacturers, retailers, local government officials and other interested groups to develop voluntary labeling and public information materials to identify products that would be eligible for tax refunds.

### From the Department of Mines, Minerals and Energy:

Proponents of alternative energy use such as the MD-DC-VA Solar Energy Industries Association and the American Wind Energy Association support this bill. They cite the expansion of sales of energy efficient equipment and alternative fueled vehicles, and support for economic development through expansion of the state's alternative energy industries. Supporters also state this will provide for further diversification of sources of electricity production in Virginia. They also claim air quality benefits from this bill, as more alternative fuel vehicles are used and more energy efficient equipment is placed in service.

This bill will be seen as providing support for economic development in Virginia. There are two solar photovoltaic panel manufacturers located in James City and Northampton Counties. Solar installers are located throughout the state. A German wind power company is locating its U.S. headquarters in Cape Charles and wishes to develop wind projects on the Eastern Shore and elsewhere in Virginia. At least two landowners in Lee County are working to develop wind projects. Another landowner is developing a project for Highland County, and there is interest in developing wind resources on Tangier Island, in Tazewell County and in Grundy. A national wind system developer is located in Richmond and would be interested in projects in the state.

The Legislative Transition Task force on utility restructuring did not recommend this bill. While supporting the concept, the LTTF felt the fiscal impact from this would be too great. The LTTF did recommend HB 746, which includes the solar utilization grants proposed in this bill due to that bill's smaller fiscal impact.

There has been a similar federal incentive of 1.5 cents/kwh sold for the production of electricity from renewable energy sources (wind, closed-loop biomass and poultry waste). This credit ended on December 31, 2001, and has not yet been extended. There is some indication that Congress may extend this incentive as part of national energy legislation.

cc: Secretary of Finance

**Date:** 1/23/02/GRM

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