DEPARTMENT OF TAXATION
2002 Fiscal Impact Statement

1. Patron Mims

2. Bill Number SB 530

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

3. Committee Senate Finance

4. Title Income Tax: Accrual and Payment of Interest on Refunds

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

5. Summary/Purpose:

It is the department's understanding that the patron intends to offer an amendment in the nature of a substitute for this bill. This impact statement addresses the substitute bill.

This bill would reduce the time before interest begins to accrue on individual income tax overpayments depending on the filing channel chosen by the taxpayer. Interest would accrue after intervals of 30 or 60 days from the date a return was filed according to the following conditions:

- 30 days if filed electronically (iFile, Telefile, or ELF - the joint Federal-State Electronic Filing program), or
- 60 days if filed by paper.

The effective date of this bill is for returns filed for taxable years beginning on and after January 1, 2003.

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

7. Budget amendment necessary: No.

8. Fiscal implications:

Revenue Impact

No measurable revenue impact is expected. With an effective date applicable to returns filed for taxable years beginning on and after January 1, 2003, the department will have two more filing seasons to perfect newly installed imaging technology, exploit process improvements, and encourage electronic filing channels. Taxpayers will also have two more filings using the redesigned income tax form. By then, the combined effect of these changes should position the department to meet the provisions of this bill with no overall loss in interest revenue.

Administrative Costs

Administrative costs will be limited to systems development and programming costs. These are estimated as one-time costs of $100,000 in FY 03.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: None.

11. Other comments:

This bill would revise the rate at which interest accrues on income tax overpayments after an individual income tax return has been filed with the Department of Taxation. Current law provides that interest accrues on tax overpayments from the later of 60 days after the return's due date (May 1) or its filing date.

This bill would reduce the time before interest begins to accrue on individual income tax overpayments depending on the filing channel chosen by the taxpayer. Interest would accrue after intervals of 30 or 60 days from the date a return was filed according to the following conditions:

- 30 days if filed electronically (iFile, Telefile, or ELF - the joint Federal-State Electronic Filing program), or
- 60 days if filed by paper

Example #1: Taxpayer files income tax return on March 15.

		As Proposed	**Current Law**
	Filing Date	Accrual Begins	Accrual Begins
Electronic	March 15	April 15	July 1
Paper	March 15	May 15	July 1

Example #2: Taxpayer files income tax return on May 1.

		As Proposed	**Current Law**
	Filing Date	Accrual Begins	Accrual Begins
Electronic	May 1	June 1	July 1
Paper	May 1	July 1	July 1

This would provide more generous interest accruals and at the same time encourage taxpayers to use electronic filing channels. Electronic filing methods are less error prone and less costly to administer. Returns with errors require manual review to investigate and correct, thereby adding to the time and expense required to process returns and issue refunds.

On average, electronically filed returns experience an error rate of five percent. Paper returns, on the other hand, experience error rates of about twenty percent. Paper returns are much more expensive to process, not only because of higher error rates, but also because of the added time and effort required to open, screen, batch, sort, scan, and perform data capture.

For these reasons, the department has gone to great lengths to build and perfect electronic filing/payment channels and strongly encourages their use. In the 2001 income tax filing season, 3.2 million current-year returns were filed, 82 percent by paper and 18 percent by electronic channels. However, the use of electronic channels is expected to grow by 15 to 20 percent annually. This bill might encourage further growth in electronic channels.

Comparison to Other Tax Authorities

A survey of other states that impose an individual income tax, the District of Columbia ("D.C."), and the Internal Revenue Service ("IRS") reveals a variety of rules for accruing and paying refund interest. For example, 20 states' period for beginning to accrue refund interest is longer than 60 days (75 days to six months); four states are the same as Virginia; and 11 states, D.C., and the IRS have a period less than 60 days (30 to 45 days). The IRS uses a 45-day period. Seven states do not have any delay period for the accrual of refund interest except for those taxpayers who file before the due date of a return.

Period of Days for Beginning to Accrue Refund Interest

	> 60 Days	60 Days	< 60Days	None
Taxing Authorities	20 states	4 states & Virginia	11 states, D.C. & the IRS	7 states

In addition, 37 states, D.C., and the IRS are similar to Virginia in that the beginning of their period for accruing refund interest is from the later of the due date of the return or the date the return is filed. Two states start their period from the date a return is due, and the three states have periods that begin when the return is filed.

Start Date for Period of Days for Beginning to Accrue Refund Interest

	Due Date	Filing Date	Later of Filing or Due Date
Taxing Authorities	2 states	3 states	37 states, D.C., the IRS & Virginia

Further, ten states and the IRS are allowed the same refund interest cut off period as Virginia. Twelve states and D.C. have a cut off period shorter than 30 days while 20 states do not have a specified time in which to cut off the accrual of refund interest. The following tables illustrate how these taxing authorities accrue and pay interest on individual income tax refunds.

Refund Interest Accrual Cut Off Period

	30 Days	< 30 Days	None Specified
Taxing Authorities	10 states, the IRS & Virginia	12 states & D.C.	20 states

cc : Secretary of Finance

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