DEPARTMENT OF TAXATION
2004 Fiscal Impact Statement

1. **Patron** Robert D. Orrock, Sr.

2. **Bill Number** HB 515
House of Origin:
_____ **Introduced**
_____ **Substitute**
_____ **Engrossed**

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

3. **Committee** Senate Finance

4. **Title** Sales and Use Tax; Nonprofit Entities

5. **Summary/Purpose:**

This bill would make several technical amendments to the new sales and use tax exemption process for nonprofit entities that is scheduled to go into effect on July 1, 2004. This bill would clarify that: (a) churches may continue to use self-issued exemption certificates; (b) the exemption from collecting sales tax on fund-raising sales currently enjoyed by certain organizations is grandfathered; and (c) the Department of Taxation may refuse to grant exemption certificates to applicants that that fail to disclose their total taxable purchases for the preceding year.

The effective date of this bill is not specified.

6. **No Fiscal Impact** (See Line 8.)

7. **Budget amendment necessary:** No.

8. **Fiscal implications:**

As this bill is technical in nature and only clarifies the intent of the legislation that created the new sales and use tax exemption process for nonprofit entities, this bill would have minimal fiscal implications.

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

Department of Taxation

10. **Technical amendment necessary:** No.

11. **Other comments:**

<u>New Process</u>

Legislation enacted in the 2003 Virginia General Assembly (Chapters 757 and 758) significantly alters the process by which nonprofit organizations obtain Virginia retail sales and use tax exemptions. This legislation eliminates the need for nonprofit organizations to seek new sales tax exemptions through the legislature. Effective July 1, 2004, all Internal Revenue Code (IRC) § 501(c)(3) and charitable § 501(c)(4) organizations can qualify for a sales tax exemption provided the criteria established by this legislation are met. The Department of Taxation will administer this process.

The legislation provides that any nonprofit organization that held a valid exemption certificate issued by the Department, or any nonprofit church that held a valid self issued certificate on June 30, 2003 will remain exempt from the collection or payment of such taxes. These grandfathered exemptions will expire and organizations will need to apply for a new exemption under the new process based on the following filing schedule:

Exemption Group	Deadline
Civic and community service (first half) (58.1-609.8)	July 1, 2004
Civic and community service (second half) (58.1-609.8)	July 1, 2005
Cultural and Miscellaneous (58.1-609.9, 58.1-609.10)	July 1, 2006
Educational (58.1-609.4)	July 1, 2007
Medical-Related (58.1-609.7)	July 1, 2008

Exemption Criteria

The new legislation provides that in order to qualify for an exemption under the new process, a nonprofit entity must meet all of the applicable criteria:

- The entity is exempt from federal income taxation under IRC § 501(c)(3) or, if organized for a charitable purpose, exemption under IRC § 501 (c) (4). Alternatively, the entity has annual gross receipts of less than $5,000 and is organized for at least one of the purposes set forth in IRC § 501(c)(3) or (4).

- The entity is in compliance with all applicable state solicitation laws, and where applicable, provides appropriate verification of such compliance.

- The entity's annual general administrative costs, including salaries and fundraising, relative to its annual gross revenue, under generally accepted accounting principles, is not greater than 40 percent.

- If the entity's gross annual revenue was $250,000 or greater in the previous year, the entity must provide a financial audit performed by an independent certified public accountant.

- If the entity filed an IRS Form 990 or 990 EZ, it must provide a copy of such form to the Department. If the entity did not file an IRS Form 990 or 990 EZ, the entity must provide a list of the Board of Directors or other responsible agents of the entity, composed of at least two individuals and the location where the financial records of the entity are available for public inspection.

Annual Report

The Department is required to file an annual report starting December 1, 2004 with the legislature setting forth the annual fiscal impact of the sales and use tax exemptions for nonprofit entities. In order to prepare this report, the Department is required to ask each applicant to submit an estimate of total taxable purchases for the next year and, where possible, for the total taxable purchases made in the preceding year.

Proposal

This bill clarifies that churches may continue to use their self-issued exemption certificate instead of applying for a new exemption under the new process. Churches using the self-issued exemption certificate will be entitled to the sales tax exemption accorded under current law.

This bill would also clarify that the exemption from collecting sales tax on fund-raising sales currently enjoyed by certain organizations is grandfathered. This exemption would also be available to any other organization that is within the same class of organization of any entity that was exempt from collecting sales and use tax on June 30, 2003. Additionally, this bill would grant an exemption from collecting sales tax on fund-raising sales to any entity that is organized exclusively to promote physical education, athletic programs and contests for youths that is exempt from paying sales taxes on its purchases.

Additionally, this bill would clarify that the Department is authorized to refuse to grant exemption certificates to applicants that that fail to disclose their total taxable purchases for the preceding year.

Other Legislation

Senate Bill 585 is identical to this bill.

House Bill 311 would modify the criteria for a nonprofit entity to qualify for a sales tax exemption certificate to require that the entity's administrative costs may not exceed 40 percent of its gross expenditures, rather than gross revenues. Also the bill would clarify that administrative costs include travel and office expenses and do not include programmatic costs.

cc : Secretary of Finance

Date: 2/24/2004 JEM