

DEPARTMENT OF TAXATION

2005 Fiscal Impact Statement

1. **Patron** Harry J. Parrish

3. **Committee** Senate Finance

4. **Title** Withholding from Nonresident Contractors

2. **Bill Number** HB 2065

House of Origin:

 Introduced

 Substitute

 Engrossed

Second House:

 X **In Committee**

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would establish a procedure for withholding Virginia sales and use tax and income tax from nonresident contractors. Under the bill, certain individuals and entities that do business with a nonresident contractor where the contract price equals or exceeds \$70,000 would be required to withhold payment of 3% of the amount of the contract. Thirty days after the end of the contract, the individual or entity would pay the withholding to the nonresident contractor if certain conditions are met. If the conditions were not met, the individual or entity would remit the amount withheld to the Department.

The bill would be effective for contracts executed on or after July 1, 2005.

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

6a. **Expenditure Impact:**

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Fund</i>
2004-05	\$0	GF
2005-06	\$356,380	GF
2006-07	\$0	GF
2007-08	\$0	GF
2008-09	\$0	GF
2009-10	\$0	GF
2010-11	\$0	GF

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

ITEM(S): Lines 284 and 286, Department of Taxation

8. Fiscal implications:

Revenue Impact

Because these provisions would enhance compliance among nonresident contractors, the bill would increase General Fund revenue for Fiscal Year 2006 and thereafter. Due to the lack of reliable data, however, the impact of this bill on General Fund revenue is unknown.

Administrative Impact

The Department would incur administrative costs of \$356,380 for Fiscal Year 2006 to implement this bill, including necessary systems changes.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Under this bill, individuals and business entities that do business with a nonresident real property contractor would be required to withhold 3% of the amount of the contract to cover Virginia sales and use tax and individual income tax generated by the activities of the nonresident contractor. The 3% withholding would be held until 30 days after the:

1. contract is completed;
2. a request has been made for a tax clearance certificate; and
3. a receipted copy of the request has been given to the person required to withhold the payment.

Within 30 days after receipt of a request for a tax clearance certificate, the Department would furnish to the nonresident contractor and to the person required to withhold the payment:

1. a certificate indicating that no tax is due from the nonresident contractor;
2. a certificate indicating that taxes are due, including the amount of sales and use tax due and income tax withheld, from the nonresident contractor including any interest and penalties; or
3. a notice of rejection for missing information or that the request is otherwise unverifiable.

The individual or business entity required to withhold payment would be able to pay the nonresident contractor if the Department (i) furnishes a certificate indicating no tax is due from the nonresident contractor; (ii) fails to provide to both the nonresident contractor and

the person required to withhold the payment a certificate within the time allowed; or (iii) fails to provide notice of rejection within the time allowed.

If the Department furnishes a certificate indicating that taxes are due from the nonresident contractor, the person required to withhold the payment would be required to remit the amount due as stated in the certificate up to 3% of the contract price to the Department. Any remaining balance of the amount withheld would be paid to the nonresident contractor.

If a notice of rejection is issued, and the nonresident contractor fails to reapply for a tax clearance certificate within 30 days of receipt of the notice, then the individual or business entity required to withhold the payment would remit the entire 3% of the contract price to the Department.

An individual or business entity that fails to withhold or to pay over the amounts withheld would be held personally liable for the payment of any sales and use tax or income tax withheld attributable to the contract up to 3% of the contract price.

The withholding requirement would not apply to an individual that is the owner of property who contracts for the improvement of residential real property that the individual occupies or intends to occupy. In addition, the requirement would be waived if the total value of the improvement under a real property contract is less than \$500,000 or if a subcontracted improvement of real property is less than \$500,000; and this waiver would also apply to subcontracts under such a contract.

The bill would be effective for contracts executed on or after July 1, 2005.

cc : Secretary of Finance

Date: 2/11/2005 AMS
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