DEPARTMENT OF TAXATION
2004 Fiscal Impact Statement

1. **Patron** Walter A. Stosch
2. **Bill Number** SB 537
   House of Origin:
   _____ **Introduced**
   _____ **Substitute**
   _____ **Engrossed**

   Second House:
   X **In Committee**
   _____ **Substitute**
   _____ **Enrolled**
3. **Committee** House Finance
4. **Title** Income Tax Credit For Exported Cigarettes

5. **Summary/Purpose:**

This bill would allow an income tax credit to cigarette manufacturers if they export at least 50% of the volume of cigarettes exported in 2003. The credit would vary from 20¢ per 1,000 cigarettes exported if at least 50% of 2003 exports, to 40¢ per 1,000 cigarettes exported if at least 120% of 2003 exports. The credit would be capped at $6 million per taxpayer per year and could not exceed 50% of the tax liability. The total amount of credits allowed to all taxpayers would not be allowed to cannot exceed $6 million.

The credit would be effective for taxable years beginning on or after January 1, 2004.

6. **Fiscal Impact Estimates are:** Not available. (See Line 8.)
   6a. Expenditure Impact:

Fiscal Year	***Dollars***	***Positions***	***Fund***
2003-04	$0	0	GF
2004-05	$46,000	1	GF
2005-06	$35,000	1	GF
2006-07	$35,000	1	GF
2007-08	$35,000	1	GF
2008-09	$35,000	1	GF
2009-10	$35,000	1	GF

7. **Budget amendment necessary:** Yes.
   Item(s): 284 and 286, Department of Taxation

8. **Fiscal implications:**

Administrative

The Department would incur administrative costs to implement this bill of $46,000 in FY 2005, and $35,000 annually thereafter for one full-time position to administer the proposed registration, reservation, tracking, allocation and reallocation procedures.

The bill would require the Department to develop complex and unique procedures for allocating and reallocating credits and tracking carryovers of allocated credits as well as eligibility for reallocation of credits. Although the development of these policies and procedures would be exempt from the Administrative Process Act, the Department would still solicit comment and need some time to resolve any issues raised by commentators.

Revenue

The revenue impact of this bill is unknown. However, it is anticipated that the $6 million cap amount would be reached each year as tobacco manufactured products are one of Virginia's largest exports.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

This bill would grant a credit of up to 40 cents per 1,000 cigarettes exported each taxable year if the volume exported is at least 50% of the cigarettes exported in 2003. The credit would be calculated on the total volume exported, not just the portion that exceeds 50% of the base year exports. The Virginia credit would be granted only cigarettes manufactured in Virginia and exported. The credit would be computed as follows:

If, compared to 2003 exports the current year exports are	But not in Excess of	Credit per 1,000 Cigarettes Exported
50%	60%	$0.20
60%	80%	$0.25
80%	100%	$0.30
100%	120%	$0.35
120%	- - - -	$0.40

The credit may not exceed 50% of the taxpayer's income tax liability or $6 million, whichever is less. However, any credit not used may be carried forward until utilized. The Department would be required to promulgate guidelines, which would be exempt from the Administrative Process Act, to address issues such as adjusting the credit when exported cigarettes are later returned to the manufacturer.

The bill would impose a statewide cap of $6 million for the total credits granted to all manufacturers. Based on the credits granted under a similar law in North Carolina, it is likely that taxpayers manufacturing and exporting cigarettes from Virginia will be eligible for more than the $6 million statewide cap on the credit. Therefore, the manufacturers must apply for the credits in advance, and the Department must establish policies and procedures to allocate the credits among eligible cigarette manufacturers in an orderly and equitable manner. The initial allocation would have to be based upon estimated future exports and tax liability, as well as other criteria to be established. Among the issues to be addressed in the Department's credit allocation policies and procedures would be:

- If the actual tax liability is lower than estimated the manufacturer may not be able to use all of the credit allocated and earned. Such unused credits may carried forward indefinitely until used.
- If the actual export volume is significantly below estimates, the credit that the manufacturer actually earns could be much lower than the credit allocated in advance. The bill would require the Department to reallocate such allocated but unearned credits to other manufacturers.
- Two types of allocations would be required:
  i. First, the full $6 million must be allocated among the applicants based on criteria established in the Department's credit allocation policies and procedures.
  ii. Second, some credits may be reallocated when the manufacturer that was originally allocated a credit fails to earn the full amount based on actual exports and tax liability. Eligibility for reallocated credits could arise from an initial allocation of fewer credits than requested, and actual exports and tax liability being greater than estimated at the time of the request for the initial allocation. Such reallocations would probably require the manufacturer receiving them to file an amended return.
- Two types of carryovers must be tracked by the Department:
  i. Carryovers of eligibility by manufacturers who applied for credits but were not allocated the full amount of credits for which they were eligible. The allocation policies and procedures must provide for the treatment of such carryover eligibility when reallocating credits as well as when allocating credits in subsequent years.
  ii. Carryovers of credits that were allocated to a manufacturer and earned by that manufacturer based on export volume, but could not be fully used because of the limitation to 50% of the manufacturer's Virginia tax liability. Such credits may be carried over by the manufacturer indefinitely until used. However, a manufacturer having such carryovers available may not be able to use additional credits allocated and earned in subsequent years. The Department's credit allocation policies and procedures would have to take the existence of such carryovers into consideration.

cc : Secretary of Finance
Date: 2/24/2004 JPJ