DEPARTMENT OF TAXATION
2007 Fiscal Impact Statement

1. Patron Kathy J. Byron

2. Bill Number HB 2803

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

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

3. Committee House Finance

4. Title Income Tax and Sales and Use Tax; Tax Preferences for Certain Telecommunications Service Providers

5. Summary/Purpose:

This bill would provide a nonrefundable individual and corporate income tax credit to taxpayers who purchase and install wireless and broadband equipment in order to provide communications services, including Internet access, to rural areas within the Commonwealth. The amount of the credit would be equal to thirty percent of such expenditures. Taxpayers would be allowed to carry over unused amounts of the credit for the next five tax years until the total amount of the credit has been taken.

The total amount of tax credits granted to all taxpayers could not exceed $1 million per tax year. Taxpayers would be required to apply for the credit by making an application to TAX. If the applications for the credit exceeded the $1 million amount, TAX would be required to apportion the money by dividing the $1 million by the total amount of tax credits applied for in order to determine the percentage that each taxpayer would receive.

In addition, this bill would provide a sales and use tax exemption for tangible personal property that was sold or leased to a telecommunications company for use or consumption by such a company directly in the rendition of its public service.

The tax credit portion of this bill would be effective for taxable years beginning on and after January 1, 2007. The sales and use tax exemption portion would be effective beginning July 1, 2007.

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

6a. Expenditure Impact:

Fiscal Year	*Dollars*	*Fund*
2006-07	$22,975	GF
2007-08	$26,200	GF
2008-09	$26,700	GF
2009-10	$27,200	GF
2010-11	$27,700	GF
2011-12	$28,200	GF
2012-13	$28,700	GF

6b. Revenue Impact:

Fiscal Year	*Dollars*	*Fund*
2006-07	$0	GF
2007-08	($26.3 million)	GF
	($3.7 million)	TTF
	($7.4 million)	Local
2008-09	($29.0 million)	GF
	($4.1 million)	TTF
	($8.2 million)	Local
2009-10	($29.0 million)	GF
	($4.1 million)	TTF
	($8.2 million)	Local
2010-11	($29.1 million)	GF
	($4.1 million)	TTF
	($8.2 million)	Local
2011-12	($29.1 million)	GF
	($4.1 million)	TTF
	($8.2 million)	Local
2012-13	($29.4 million)	GF
	($4.1 million)	TTF
	($8.3 million)	Local

7. Budget amendment necessary: Yes.
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264 and 265, Department of Taxation

8. Fiscal implications:

Administrative Costs

The Department would incur administrative costs of $22,975 for FY 2007, $26,200 for FY 2008, $26,700 for FY 2009, $27,200 for FY 2010, $27,700 for FY 2011, $28,200 for FY 2012, and $28,700 for FY 2013 in order to hire a part-time employee to administer and allocate the tax credit.

Revenue Impact

This bill would have a negative revenue impact on state and local revenues. The total revenue loss would be $37.4 million in FY 2008 and approximately $42 million per year thereafter. Of this amount, $1 million is attributed to the new credit for those who provide communications services, while the remaining $41 million per year is attributed to the restoration of the sales and use tax exemption for telecommunications companies.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Current Law

Until 2004, public service corporations had an exemption for the purchase of all tangible personal property <u>used directly</u> in the rendition of their pubic service. Direct usage refers to those activities that are an integral part of the rendition of a public utility service, including all steps of a utility's production, generation or initiation process as well as a utility's transmission or distribution process, but not including incidental public utility functions such as administration and management. This exemption was enjoyed by i) public service corporations subject to state franchise or license tax on gross receipts, ii) telecommunications companies and certain telephone companies, and iii) common carriers of property or passengers by motor vehicle or railway.

With the exception of common carriers by railway, the 2004 tax reform (House Bill 5018, Chapter 3, 2004 Acts of Special Session I) repealed all the exemptions for public service corporations. These included all public service corporations subject to the state franchise and license tax on gross receipts, telecommunications and certain telephone companies, and motor vehicle common carriers.

The law that repealed these exemptions also contained an enactment clause, which allows those entities that are now required to pay a sales and use tax to impose a separate line item surcharge on customers' bills in order to recoup the taxes paid as a result of the repeal of the exemption. This enactment clause does not apply to motor vehicle common carriers,

Proposal

<u>Income Tax Credit</u>

This bill would provide a nonrefundable individual and corporate income tax credit to taxpayers who purchase and install wireless and broadband equipment in order to provide communications services, including Internet access, to rural areas within the Commonwealth. This bill would define a "rural area" as any locality with an overall population density of less than or equal to 120 people per square mile.

The amount of the credit would be equal to thirty percent of such expenditures. Taxpayers would be allowed to carry over unused amounts of the credit for the next five tax years until the total amount of the credit has been taken. The amount of any credit that was attributable to a partnership, electing small business corporation (S corporation), or limited liability company would be required to be allocated to the individual partners, shareholders, or members, respectively, in proportion to their ownership or interest in such business entities.

The total amount of tax credits granted to all taxpayers could not exceed $1 million per tax year, however. Taxpayers would be required to apply for the credit by making an application to TAX. If the applications for the credit exceeded the $1 million amount, TAX would be required to apportion the money by dividing the $1 million by the total amount of tax credits applied for in order to determine the percentage that each taxpayer would receive. If a pass-through entity were involved, the partnership, S corporation, or limited liability company making the expenditures would be responsible for making the application to TAX, not the individual taxpayers.

Sales and Use Tax Exemption

This bill would provide a sales and use tax exemption for tangible personal property that was sold or leased to a telecommunications company for use or consumption by such a company directly in the rendition of its public service. It would not reinstate the exemption for the other public service corporations that lost the exemption in 2004, however.

If this sales tax exemption were reinstated, telecommunications companies would no longer have the authority to impose a separate line item surcharge on customers' bills in order to recoup the taxes paid as a result of the repeal of the exemption.

Similar Legislation

House Bill 2385 would create a separate classification for local property tax purposes for any tangible personal property owned and used by the providers of wireless broadband Internet service in providing such service.

cc : Secretary of Finance

Date: 1/23/2007 AMS
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