DEPARTMENT OF TAXATION
2008 Fiscal Impact Statement

1. Patron Frank M. Ruff

2. Bill Number SB 459

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

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

3. Committee Senate Finance

4. Title Retail Sales and Use Tax; Nonprofit Exemption for § 501(c)(19) Organizations

5. Summary/Purpose:

This bill would permit nonprofit Veteran Service Organizations ("VSOs") that are exempt from federal income taxation under § 501(c)(19) of the Internal Revenue Code ("I.R.C."), to obtain an exemption from the Retail Sales and Use Tax on all purchases of tangible personal property by filing an application with TAX, meeting the applicable criteria, and being issued a certificate of exemption from TAX.

Under current law, only organizations exempt from federal income taxation under I.R.C. § 501(c)(3) or § 501(c)(4) are eligible for the Retail Sales and Use Tax exemption available to certain nonprofit entities on their purchases of tangible personal property.

The effective date of this bill is not specified.

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

7. Budget amendment necessary: No.

8. Fiscal implications:

Administrative Costs

TAX has not assigned any administrative costs to this proposal because the changes required by a single bill such as this can be implemented as part of the annual changes to our systems and forms. As stand-alone legislation, TAX considers implementation of this bill as "routine," and does not require additional funding.

TAX will provide specific administrative costs on any legislation that is not "routine." Additionally, TAX will review all state tax legislation likely to be enacted prior to the passage by each house. If the aggregate number of routine bills likely to pass either house is unusually large, it is possible that additional resources will be required. If so, TAX will identify the costs at that time.

Revenue Impact

To the extent that additional organizations qualify for a nonprofit exemption, this bill would result in a revenue loss of unknown magnitude. The U.S. Department of Veterans Affairs lists 47 organizations either chartered by the U.S. Congress or recognized by Veterans Affairs. TAX lists an additional 125 non-chartered organizations.

9. Specific agency or political subdivisions affected:
TAX

10. Technical amendment necessary: No.

11. Other comments:

Generally

Currently, nonprofit entities classified as § 501(c)(3) or § 501(c)(4) organizations by the I.R.C. may obtain an exemption from the Retail Sales and Use Tax on their purchases of tangible personal property, provided they: 1) file an appropriate application with TAX; 2) meet the applicable criteria; and 3) are issued a certificate of exemption from TAX. The exemption is only available to nonprofit entities that have been designated as § 501(c)(3) or § 501(c)(4) organizations.

This bill would expand the entities entitled to receive the nonprofit exemption to include all § 501(c)(19) organizations that followed the steps set forth above. Consequently, this bill would make the exemption available to most VSOs.

History of Virginia Exemption Process for Nonprofit Entities

Prior to July 1, 2004, the Code of Virginia separately listed and provided a sales tax exemption for over 180 categories of nonprofit entities. Entities not exempt by statutory classification were required to seek exemption through the Virginia General Assembly. Legislation enacted in the 2003 Virginia General Assembly, which became effective July 1, 2004, altered the process by eliminating the need for exempt organizations to renew their sales tax exemptions through the legislature. The legislature extended those organizations' exemptions for a specified term and required that, upon expiration, the organizations would have to adhere to a three-part process to include applying to TAX, meeting applicable criteria, and being issued a certificate of exemption from TAX. Organizations that were not previously granted an exemption were also required to follow the process set forth above in order to obtain an exemption. The result of this legislation was that organizations no longer needed to apply to the General Assembly to receive an exemption or to renew an exemption, provided that they met the applicable criteria and performed all the necessary procedures. If all requirements were met, TAX could grant each organization a sales tax exemption for an additional period to expire in no less than five and no more than seven years, at which time the organization would have to reapply for exemption status.

Since inception of the new process for nonprofit entities, certain organizations that once were eligible for an exemption are no longer eligible under the new process. Sunset provisions were made part of the exemption available under the old process. Organizations that do not meet the criteria set forth for nonprofit exemptions under the new process will have their exemptions expire, according to the expiration dates given under the old law.

Prior to the law change, the Virginia Army/Air National Guard Enlisted Association and the Virginia National Guard Association qualified for an exemption on their purchases of all tangible personal property as well as meals and lodging for members. This exemption expired on July 1, 2006, and neither organization qualifies for the exemption under the new process because neither meets the criteria set forth under the new process. These organizations are both classified as § 501(c)(19) organizations by the Internal Revenue Code, but they are the only two § 501(c)(19) organizations to which an exemption was given under the old process. The remaining § 501(c)(19) organizations were not granted an exemption under the old process, nor do they qualify for an exemption under the new process.

Current Requirements

The new exemption process requires that nonprofit organizations meet the following criteria to be eligible for exemption:

- The entity must be either an organization exempt under Internal Revenue Code ("IRC") §§ 501(c)(3) or 501(c)(4), or have annual gross receipts of less than $5,000 and be organized for a charitable purpose.
- The entity must have annual administrative costs that are 40% or less of annual gross receipts.
- The entity must be in compliance with state solicitation laws, if applicable.
- The entity must provide TAX with an estimate of its total taxable purchases
- The entity must provide TAX with a copy of its Form 990 or a list of its board of directors.
- The entity must provide TAX with a copy of a full financial audit performed by an independent certified public accountant, if its gross annual revenues for the previous year were $1 million or greater. A nonprofit organization with gross annual revenues between $750,000 and $1 million in the previous year is given the choice of providing either a full financial audit or a "financial review", both of which must be performed by an independent certified public accountant.

Classification of VSOs as § 501(c)(19) Organizations

There are over 150 different types of both federally chartered and non-chartered VSOs. Prior to the passage of Public Law 92-418, most veterans' organizations were classified as § 501(c)(4) social welfare organizations. Typically, these organizations now fall under § 501(c)(19) of the Internal Revenue Code.

While some VSOs meet the requirements of § 501(c)(3) or § 501(c)(4), most VSOs are characterized as § 501(c)(19) organizations. Under I.R.C. § 501(c)(19), a post or organization of past or present members of the Armed Forces of the United States or an auxiliary unit or society of, or a trust or foundation that meets the following requirements is exempt from federal income taxes: 1) organized in the United States or any of its possessions; 2) at least 75% of the members must be past or present members of the Armed Forces and substantially all of the remaining members must be cadets, spouses, widows, widowers, ancestors, or lineal descendants of past or present members of the Armed Forces of the United States or of cadets, and 3) no part of the net earnings may inure to the benefit of any private shareholder or individual. Under the provisions of this bill, organizations that meet these requirements would be eligible for exemption from the Retail Sales and Use Tax if they meet the other criteria to qualify for a nonprofit exemption.

Similar Legislation

House Bill 1284 and **Senate Bill 543** (identical) would exempt any non-profit school that is accredited by any entity approved by the Department of Education and any school licensed by the Department of Education as a school for students with disabilities from the requirement to submit an audit to TAX to obtain a sales and use tax exemption, if the school submits a federal 990 tax form.

Senate Bill 468 would exempt 4-H clubs from having to collect the Retail Sales and Use Tax on sales made by the club in fundraising.

cc : Secretary of Finance

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