DEPARTMENT OF TAXATION
2012 Fiscal Impact Statement

1. Patron Mark L. Cole

2. Bill Number HJ 52

House of Origin:
X Introduced
_____ Substitute
_____ Engrossed

Second House:
_____ In Committee
_____ Substitute
_____ Enrolled

3. Committee House Rules

4. Title Joint Subcommittee to Evaluate Tax Preferences; Report Established

5. Summary/Purpose:

This resolution would establish a thirteen-member joint subcommittee to study reforming Virginia's tax structure, including examining the feasibility of adopting a flat tax or fair tax. The joint subcommittee would consist of ten legislative members and three nonlegislative citizen members. Legislative members consist of six members of the House of Delegates, as appointed by the Speaker of the House of Delegates, and four members of the Senate, as appointed by the Senate Committee on Rules. The nonlegislative members would consist of two citizen members with experience in taxation and finance issues, as appointed by the Speaker of the House of Delegates, and one citizen member with experience in taxation and finance issues, as appointed by the Senate Committee on Rules.

The joint subcommittee would be required to review Virginia's entire state and local tax structure, examine ways to eliminate tax preferences and lower rates, eliminate or restructure unfair or unnecessarily burdensome taxes, and examine the feasibility of adopting a flat individual income tax. Administrative staff support for the joint subcommittee would be provided by the Office of the Clerk of the House of Delegates. Legal, research, policy analysis, and other services would be provided by the Division of Legislative Services. The Department of Taxation would be required to provide technical assistance.

The effective date of this resolution is not specified.

6. Budget amendment necessary: No.

7. No Fiscal Impact. (See Line 8.)

8. Fiscal implications:

<u>Administrative Costs</u>

The Department would not incur additional administrative costs in providing technical assistance to the joint subcommittee.

Revenue Impact

The existence of the joint subcommittee itself would not have a revenue impact. If actions of the joint subcommittee result in the repeal or modification of tax preferences or other changes in the tax structure, there would likely be a revenue impact.

9. Specific agency or political subdivisions affected:

Department of Taxation
Division of Legislative Services
Office of the Clerk of the House of Delegates

10. Technical amendment necessary: No.

11. Other comments:

JLARC Tax Preferences Study

The 2010 General Assembly passed Senate Joint Resolution 21, which required the Joint Legislative Audit and Review Commission (JLARC) to conduct a two-year examination of Virginia individual income tax, corporate income tax, and retail sales and use tax preferences. In its report, JLARC was required to do the following:

- Determine which individual income, corporate income, and sales and use tax preferences are being claimed or taken and to what extent;
- Provide an estimate of the fiscal impact of all such tax preferences claimed or taken;
- Examine the public policies for which the tax preferences were established and whether the desired public policies have been achieved;
- Report on whether other states routinely provide a sunset date for their tax preferences; and
- Establish a proposed mechanism or processes for the ongoing evaluation of the effectiveness of such tax preferences in bringing about the desired public policies for which the tax preferences were established.

JLARC was required to complete its meetings for the first year by November 30, 2010 and for the second year by November 30, 2011. A Commission Draft of the report was published November 14, 2011 and the final report will be submitted to the General Assembly during the 2012 session.

In its report, JLARC provided an overview of Virginia's tax preferences and the overall fiscal impact of these preferences. JLARC then divided existing preferences into various categories and determined the utilization of preferences within each category. The report identified several factors that hinder the effectiveness of certain tax preferences, including the limited use of sunset dates in tax preference bills and the lack of a formal process for evaluating the effectiveness of tax preferences.

The report concluded with the suggestion that the General Assembly establish a joint subcommittee to oversee an ongoing evaluation process. This subcommittee would direct the Department of Taxation to conduct routine evaluations and would assemble a technical advisory group to provide guidance and review findings. JLARC mentioned in its report that, if such a subcommittee were established, the Department would require additional staff, but the number of additional positions required would depend upon the scope of evaluations established by the joint subcommittee.

Sales and Use Tax Expenditure Study

The 1989 General Assembly passed legislation that required the Department to study all sales and use tax exemptions on a continuous five-year cycle, studying two categories of exemptions each year. The Department was required to publish the Sales and Use Tax Expenditure Study and present it to the Chairmen of the House Finance and Senate Finance Committees in December of each year. The goal of the Sales and Use Tax Expenditure Study was to provide a more complete picture of the revenue impact and policy issues surrounding each of the exemptions contained in the Retail Sales and Use Tax Act. The study included detailed information on the policy, fiscal, and economic impact of the exemptions as well as the apparent rationale for the exemptions and their legislative history. It was believed that the periodic review of sales and use tax exemptions was necessary in order to strengthen oversight and control over the process by which sales tax exemptions are granted. In order to complete the study, the Department needed to employ additional economists and analysts. The Department published its last study in December 1995. The 1996 General Assembly repealed the requirement that the Department conduct the study.

In 2005, the General Assembly reinstated a similar but limited study that requires the Department to determine the fiscal, economic, and policy impact of each miscellaneous and nonprofit sales and use tax exemption. Specifically, the Department must include the following in its report:

- An estimate of the foregone state and local revenues as a result of each exemption;
- Beneficiaries of each exemption;
- Direct or indirect local, state, or federal government assistance received by the persons or entities granted each exemption, to the extent such information is reasonably available;
- The extent to which a comparable person, entity, property, service, or industry is exempt from the retail sales and use tax in other states, particularly states contiguous to Virginia;
- Any external statutory, constitutional, or judicial mandates supporting an exemption;
- Other Virginia taxes to which the person, entity, property, service, or industry is subject;
- Similar taxpayers who are not entitled to a retail sales and use tax exemption; and
- Other criteria, facts, or circumstances that may be relevant to each exemption.

The Department must present its report to the chairmen of the House and Senate Finance Committees no later than December 1 of each year. Subgroups of the exemptions are reviewed in periodic cycles and reports are issued on a rotating basis. When such reports have been completed for each subgroup of the sales and use tax exemptions, the Tax Commissioner must repeat the process beginning with the subgroup of exemptions for which a report was made in 2007. No individual exemption is analyzed more frequently than once every five years.

Corporate Tax Preferences Report

In 2005, the General Assembly directed the Department to issue an annual report detailing the amount of income tax relief granted to corporations in the Commonwealth. This report must include the total dollar amount of income tax subtractions, deductions, exclusions, exemptions and credits claimed cumulatively by corporations. Beginning in 2010, this report also includes summary information regarding the types of taxpayers that claim corporate income tax relief, as well as information regarding the number of companies that have qualified for the major business facility job tax credit and the amount of such credits.

The Tax Commissioner is required to issue the corporate tax preferences report annually to the members of the House Appropriations Committee, the House Finance Committee, and the Senate Finance Committee. This report does not reflect all of the exemptions and exclusions available to corporations because not all of them are reported on the Virginia income tax return.

Fiscal Year Tax Credit Report

Beginning in 2011, the Department publishes an annual fiscal year tax credit report as part of its annual report. This report shows the number of individual and corporate taxpayers that claim each tax credit and the dollar amount of tax credits that are claimed each fiscal year.

Proposal

This resolution would establish a thirteen-member joint subcommittee to study reforming Virginia's tax structure, including examining the feasibility of adopting a flat tax or fair tax. The joint subcommittee would consist of ten legislative members and three nonlegislative citizen members. Legislative members consist of six members of the House of Delegates, as appointed by the Speaker of the House of Delegates, and four members of the Senate, as appointed by the Senate Committee on Rules. The nonlegislative members would consist of two citizen members with experience in taxation and finance issues, as appointed by the Speaker of the House of Delegates, and one citizen member with experience in taxation and finance issues, as appointed by the Senate Committee on Rules.

The joint subcommittee would be required to review Virginia's entire state and local tax structure, examine ways to eliminate tax preferences and lower rates, eliminate or restructure unfair or unnecessarily burdensome taxes, and examine the feasibility of adopting a flat individual income tax. Administrative staff support for the joint subcommittee would be provided by the Office of the Clerk of the House of Delegates. Legal, research, policy analysis, and other services would be provided by the Division of Legislative Services. The Department of Taxation would be required to provide technical assistance. All agencies of the Commonwealth would be required to provide assistance to the joint subcommittee upon request.

The joint subcommittee would be required to complete its meetings by November 30, 2012, and the chairman would submit tot eh Division of Legislative Automated Systems and executive summary of its findings and recommendations no later than the first day of the 2013 Regular Session of the General Assembly. The executive summary would be required to state whether the joint subcommittee intends to submit to the General Assembly and the Governor a report of its findings and recommendations for publication as a House or Senate document. The executive summary and report would be submitted according to the procedures of the Division of Legislative Automated Systems for the processing of legislative documents and reports and would be posted on the General Assembly's website.

No recommendation of the joint subcommittee would be adopted if a majority of the House members or a majority of the Senate members appointed to the joint subcommittee vote against the recommendation and vote for the recommendation to fail notwithstanding the majority vote of the joint subcommittee.

The joint subcommittee would be limited to six meetings for the 2012 interim. The direct costs of the study would not be permitted to exceed $33,600 without approval. Nonlegislative citizen members would only be reimbursed for travel originating and ending within the Commonwealth for the purpose of attending meetings. Approval for unbudgeted nonmember-related expenses would require the written authorization of the chairman of the joint subcommittee and the respective Clerk.

Implementation of this resolution would be subject to subsequent approval and certification by the Joint Rules Committee. The Committee would be permitted to approve or disapprove expenditures for this study, extend or delay the period for the conduct of the study, or authorize additional meetings during the 2012 interim.

The effective date of this resolution is not specified.

Similar Legislation

House Bill 146 would establish the Commission to Review the Effectiveness of Virginia's Tax Preferences and would require the Department to assist the proposed Commission in evaluating Virginia's tax preferences.

House Bill 246 would require the Tax Commissioner to undertake an annual study of tax credits that are scheduled to expire within the following two calendar years.

House Bill 777 would establish the Joint Subcommittee to Evaluate Tax Preferences and would require the Department to assist the proposed Joint Subcommittee in evaluating Virginia's tax preferences.

House Bill 1032 would prohibit any committee of the General Assembly from reporting any bill that proposes to establish, increase, or expand a state or local tax exemption, credit, deduction or any other reduction in tax liability, unless the bill contains an expiration date of not longer than five years from the effective date of the bill.

House Joint Resolution 4 would require the Department to study the Business, Professional, and Occupational License (BPOL) Tax.

House Joint Resolution 85 would require JLARC, with technical assistance from the Department, to study and determine the multiplier effects of various types of income tax credits, public-private partnerships, and other public private investment programs.

Senate Joint Resolution 85 would require JLARC, with technical assistance from the Department, to study and make recommendations regarding how to phase out the corporate income tax over a period of eight years, whether alternative taxes to the corporate income tax should also be phased out, and whether other areas of the Code should be amended or studies to avoid unintended consequences from a phase-out of the corporate income tax.

cc : Secretary of Finance

Date: 01/26/2012 KLC
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