DEPARTMENT OF TAXATION
2012 Fiscal Impact Statement

1. Patron William M. Stanley, Jr.

2. Bill Number SB 61

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

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

3. Committee Senate Finance

4. Title Corporate income tax; lower rate for certain businesses.

5. Summary/Purpose:

This bill would reduce the corporate income tax rate for certain businesses that open a satellite office or operation in a Virginia locality with a population of 200,000 or fewer. In order to qualify a corporation would have to (1) either be located outside Virginia or located in a Virginia locality with a population exceeding 200,000 people; (2) make a capital investment equal or greater than $250,000 in the new or satellite office; and (3) either hire five new employees or reduce commute times for at least five employees. The rate would be reduced from six percent to three percent for the first three taxable years the new office is in operation, but any tax reduction could not exceed the amount of the capital investment.

The bill would be effective for taxable years beginning on or after January 1, 2012.

6. Budget amendment necessary: Yes.
Page 1, Revenue Estimates

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

8. Fiscal implications:

<u>Administrative Costs</u>

The Department of Taxation considers implementation of this bill as “routine,” and does not require additional funding.

<u>Revenue Impact</u>

This bill would result in an unknown loss in General Fund revenues potentially beginning as early as Fiscal Year 2012 with a significant unknown revenue loss in Fiscal Year 2013 and thereafter. The impact for Fiscal Year 2012 would depend on the timing of the enactment by the General Assembly and whether businesses could adjust their estimated payments based on qualifying projects.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

<u>Current Law</u>

Virginia currently offers several tax credits to businesses that encourage investment and job creation at Virginia locations. The Major Business Facility Job Tax Credit is a credit for taxpayers in qualifying industries that create at least 50 new full-time jobs (25 jobs for economically distressed areas or enterprise zones). The amount of the credit is equal to $1,000 for each qualifying new job in excess of the 50/25 job threshold.

The International Trade Facility Tax Credit is a credit for either capital investment in or increased employment at a qualifying international trade facility. This credit is equal to $3,000 per new qualified full-time employee that results from increased qualified trade activities or two percent of the amount of capital investment made by the taxpayer to facilitate such qualified activities.

The Telework Expenses Tax Credit is a credit that encourages businesses to promote teleworking by allowing a credit equal to the amount of telework expenses incurred, up to $1,200 per employee, and the amount of expenses incurred for conducting a telework assessment, up to $20,000. The total amount of this credit cannot currently exceed $50,000 per employer.

The Green Jobs Tax Credit is a tax credit for each new “green job” that is created in Virginia by the taxpayer. The credit is equal to $500 for each new position with an annual salary of $50,000 or more. The tax credit is allowed in the first taxable year in which the job has been filled for at least one year, and in the four succeeding taxable years in which the job is continuously filled. The tax credit may be claimed for up to 350 green jobs per taxpayer.

<u>Proposal</u>

Under this bill, any corporation located outside Virginia that opens an office in a Virginia locality with a population of 200,000 or fewer individuals would be permitted to use a reduced corporate income tax rate for determining its Virginia income tax for the first three taxable years such new office is in operation.

In addition, any corporation located in a Virginia locality with a population in excess of 200,000 individuals that opens a satellite office or operation in a Virginia locality with a population of 200,000 or fewer individuals would be permitted to use a reduced corporate income tax rate for determining its Virginia income tax for the first three taxable years such satellite offices are in operation.

In order to be eligible for the lower tax rate, the corporation would have to make a capital investment for the new office or operation of at least $250,000. The corporation would also have to hire five or more full-time employees or reduce the commuting distance to less than 10 miles for at least five existing full-time employees.

For corporations meeting the requirements of this bill, the corporate income tax rate would be reduced from six percent to three percent. However, the tax reduction resulting from the lower tax rate could not exceed the capital investment made by the corporation in establishing the new or satellite office or operation.

Businesses that do not operate as corporations would not be eligible for the reduced tax rate proposed in this bill. The majority of businesses that conduct business in Virginia are organized as pass-through entities or sole proprietorships, rather than as corporations. For Taxable Year 2009, more than 179,000 pass-through entity returns were filed, as compared to fewer than 69,000 corporate income tax returns. Additionally, many businesses file individual returns as sole proprietorships. For example, according to IRS data, 578,234 individual income tax returns were filed in Virginia for Taxable Year 2007 by owners of sole proprietorships. This number includes a broad range of businesses, from people selling products part-time, to tradesmen (plumbers, electricians, carpenters, etc.) running a full-time business. Such businesses would not benefit from the reduced rate proposed by this bill.

Because this bill requires that the business be located outside Virginia or in another Virginia locality with a population exceeding 200,000 people, it would not apply to new corporations that start a new business in Virginia. Additionally, because the bill applies to satellite offices, it would not apply to corporations that move their headquarters to Virginia from another state, or corporations that relocate their headquarters from a Virginia locality with a population of more than 200,000 people.

Although not required by the bill, the Department of Taxation would likely need to work with Virginia localities to develop procedures for providing documentation to corporations that qualify for the reduce income tax rate.

The bill would be effective for taxable years beginning on or after January 1, 2012.

<u>Similar Legislation</u>

House Bill 149 is identical to this bill.

Senate Bill 178 would create a corporate income tax credit for any corporation that invests at least $250,000 to open a satellite office or operation in a Virginia locality that reduces the commute of at least 10 current employees to five miles or less.

cc : Secretary of Finance

Date: 1/28/2012 KLC
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