DEPARTMENT OF TAXATION
2018 Fiscal Impact Statement

1. Patron Terry G. Kilgore

2. Bill Number HB 665
House of Origin:
_____ **Introduced**
_____ **Substitute**
_____ **Engrossed**

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

3. Committee Passed House and Senate

4. Title Income Tax; Virginia Coal Tax Credits

5. Summary/Purpose:

This bill would reinstate the Coalfield Employment Enhancement Tax Credit for taxable years beginning on and after January 1, 2018, but before January 1, 2023. Under this bill, taxpayers would be permitted to claim the Coalfield Employment Enhancement Tax Credit for metallurgical coal mined by underground methods and surface methods. Before it expired on December 31, 2016, the credit was available for all coal mined by such methods and was not restricted to metallurgical coal. In addition, this bill would permit taxpayers to claim the Coalfield Employment Enhancement Tax Credit for any coal mined for the production of coalbed methane.

This effective date of this bill is not specified.

6. Budget amendment necessary: No.

6. Fiscal Impact Estimates are: Preliminary. (See Line 8.)
7b. Revenue Impact:

Fiscal Year	***Dollars***	***Fund***
2017-18	$0	GF
2018-19	$0	GF
2019-20	$0	GF
2020-21	$0	GF
2021-22	($6.5 million)	GF
2021-22	$1.0 million	NGF
2022-23	($5.8 million)	GF
2022-23	$900,000	NGF
2023-24	($5.2 million)	GF
2023-24	$800,000	NGF

8. Fiscal implications:

Administrative Costs

The Department of Taxation ("the Department") considers implementation of this bill as "routine," and does not require additional funding.

Revenue Impact

This bill would have a negative General Fund revenue impact of $6.5 million in Fiscal Year 2022; $5.8 million in Fiscal Year 2023; and $5.2 million in Fiscal Year 2024. Because the Coalfield Employment Enhancement Tax Credit may not be claimed until the third taxable year after the credit was earned, the revenue impact of reinstating the credit would not be realized until income tax returns are filed for Taxable Year 2021, which generally occurs during Fiscal Year 2022. This estimate assumes that 60 percent of credits claimed under prior law were related to the mining of metallurgical coal.

The Virginia Coalfield Economic Development Authority receives 15 percent of the face value of coal tax credits redeemed by taxpayers. Accordingly, the reinstatement of the Coalfield Employment Enhancement Tax Credit would increase funding to the Virginia Coalfield Economic Development Authority by $1 million in Fiscal Year 2022; $900,000 in Fiscal Year 2023; and $800,000 in Fiscal Year 2024.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Coalfield Employment Enhancement Tax Credit

Persons with an economic interest in coal mined in Virginia were permitted to claim the Coalfield Employment Enhancement Tax Credit against any tax imposed by Virginia. For coal mined underground, the credit amount varied according to the seam thickness of the coal that is being mined. The credit was equal to $2.00 per ton for a seam thickness of 36 inches or less and $1.00 per ton for a seam thickness greater than 36 inches. For coal mined by surface mining methods, the credit was equal to $0.40 per ton of coal sold. Coalbed methane gas producers may claim a credit equal to $0.01 per million BTUs of gas produced.

The credit could be claimed in the third taxable year following the taxable year in which the credit was earned and allowed. To the extent the credit exceeded a taxpayer's Virginia tax liability, the taxpayer was entitled to redeem the excess credits in an amount equal to 85 percent of the face value of such excess. The remaining 15 percent was required to be deposited in a regional economic development fund administered by the Coalfields Economic Development Authority.

The Coalfield Employment Enhancement Tax Credit expired for taxable years beginning on or after January 1, 2017.

Virginia Coal Employment and Production Incentive Tax Credit

The Virginia Coal Employment and Production Incentive Tax Credit is a credit allowed to electricity generators in Virginia against the corporation income tax and the tax that applies to electric suppliers, pipeline distribution companies, gas utilities, and gas suppliers. The amount of the credit is equal to $3 for each ton of coal purchased and consumed by an electricity generator, provided such coal was mined in Virginia. Electricity generators may carry over unused credits for up to ten taxable years.

To the extent an electricity generator purchased coal qualifying for the credit from a person with an economic interest in coal, the credit may be allocated between the electricity generator and such person with an economic interest in coal. Any person with an economic interest in coal that received an allocation of credits is permitted to redeem such credits only if they were earned in a taxable year ending before July 1, 2016. To the extent credit allocated to a person with an economic interest in coal exceeds such person's Virginia tax liability, such taxpayer is entitled to redeem the excess credits in an amount equal to 85 percent of the face value of such excess. The remaining 15 percent is to be deposited in a regional economic development fund administered by the Coalfields Economic Development Authority.

For credits earned in a taxable year ending on or after July 1, 2016, a person with an economic interest in coal may still receive an allocation of credits. However, the credits must be used to reduce the person's corporate tax liability or any other tax imposed by Virginia in the year during which the credits are received. Any excess may not be carried over to a future taxable year and may not be redeemed in the current taxable year.

<u>JLARC Report on the Coal-Related Tax Credits</u>

During 2011, the Joint Legislative Audit and Review Commission ("JLARC") reviewed the effectiveness of Virginia's tax preferences. According to JLARC's report, the coal credits did not appear to be effectively promoting coal production and employment in Virginia. JLARC found that Virginia coal production and employment have declined by over 50 percent since their historic highs in 1990. Both of the coal credits were enacted to slow the decline of Virginia coal employment and production, which were each predicted to decline by 28 percent between 1996 and 2005 without the credits. Despite the enactment of the Coalfield Employment Enhancement Tax Credit in 1995 and the Virginia Coal Employment and Production Incentive Tax Credit in 1999, between 1996 and 2005, Virginia's coal production declined by 27 percent and coal employment declined by 36 percent. JLARC concluded that although the coal credits can significantly reduce tax liability for mine operators, they do not appear to be sufficient to counteract the negative impact of other factors on Virginia coal production and employment, such as the high costs of production and transportation.

Despite their potential ineffectiveness, taxpayers claimed $22.6 million in coal-related tax credits during Fiscal Year 2017. In addition to the large fiscal impact, these credits tend to be volatile, which can cause potential unexpected revenue shortfalls. For example, in Fiscal Year 2013, electricity generators claimed $59 million worth of Virginia Coal Employment and Production Incentive Tax Credits after not claiming any of this credit for several years prior. This large revenue loss was due to built-up credit carryovers that were claimed in the same year by several generators that began generating profits, and as a result, finally had sufficient tax liability to absorb the credits.

<u>Sunset Dates for Income Tax Credits and Sales Tax Exemptions</u>

Section 3-5.14 of the 2016-2018 Appropriation Act provides that the General Assembly may not advance the sunset date for any existing income tax credit or sales tax exemption beyond June 30, 2022. Any new income tax credit or sales tax exemption enacted by the General Assembly prior to the 2021 Session must have a sunset date not later than June 30, 2022. This requirement does not apply to sales tax exemptions related to nonprofit entities or to

income tax credits or sales tax exemptions with sunset dates after June 30, 2022 that were enacted or advanced during the 2016 Session.

Proposed Legislation

This bill would reinstate the Coalfield Employment Enhancement Tax Credit for taxable years beginning on and after January 1, 2018, but before January 1, 2023. Under this bill, taxpayers would be permitted to claim the Coalfield Employment Enhancement Tax Credit for metallurgical coal mined by underground methods and surface methods. Before it expired on December 31, 2016, the credit was available for all coal mined by such methods and was not restricted to metallurgical coal. In addition, this bill would permit taxpayers to claim the Coalfield Employment Enhancement Tax Credit for any coal mined for the production of coalbed methane.

This bill would define "metallurgical coal" as bituminous coal used for the manufacture of iron and steel with calorific value of 14,000 BTUs or greater on a moisture and ash free basis. A "BTU," or British thermal unit, is the amount of heat required to raise the temperature of one pound of water by one degree Fahrenheit.

This bill would require the Department to develop and make publically available guidelines implementing the provisions of this bill. Such guidelines would not be subject to the provisions of the Administrative Process Act.

This effective date of this bill is not specified.

Similar Bills

Senate Bill 378 is identical to this bill.

cc: Secretary of Finance

Date: 3/2/2018 JJS
HB665FER161