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SENATE BILL NO. 1443

Offered January 9, 2019

Prefiled January 8, 2019

A BILL to amend and reenact §§ 58.1-301, 58.1-320, 58.1-322.03, 58.1-400, and 58.1-402 of the Code of Virginia, relating to Virginia income tax; emergency.

Patron—Stuart

Referred to Committee on Finance

Be it enacted by the General Assembly of Virginia:

1. That §§ 58.1-301, 58.1-320, 58.1-322.03, 58.1-400, and 58.1-402 of the Code of Virginia are amended and reenacted as follows:

§ 58.1-301. Conformity to Internal Revenue Code.

A. Any term used in this chapter shall have the same meaning as when used in a comparable context in the laws of the United States relating to federal income taxes, unless a different meaning is clearly required.

B. Any reference in this chapter to the laws of the United States relating to federal income taxes shall mean the provisions of the Internal Revenue Code of 1954, and amendments thereto, and other provisions of the laws of the United States relating to federal income taxes, as they existed on February 9 December 31, 2018, except for:

1. The special depreciation allowance for certain property provided for under §§ 168(k), 168(l), 168(m), 1400L, and 1400N of the Internal Revenue Code;

2. The carry-back of certain net operating losses for five years under § 172(b)(1)(H) of the Internal Revenue Code;

3. The original issue discount on applicable high yield discount obligations under § 163(e)(5)(F) of the Internal Revenue Code;

4. The deferral of certain income under § 108(i) of the Internal Revenue Code. For Virginia income tax purposes, income from the discharge of indebtedness in connection with the reacquisition of an "applicable debt instrument" (as defined under § 108(i) of the Internal Revenue Code) reacquired in the taxable year shall be fully included in the taxpayer's Virginia taxable income for the taxable year, unless the taxpayer elects to include such income in the taxpayer's Virginia taxable income ratably over a three-taxable-year period beginning with taxable year 2009 for transactions completed in taxable year 2009, or over a three-taxable-year period beginning with taxable year 2010 for transactions completed in taxable year 2010 on or before April 21, 2010. For purposes of such election, all other provisions of § 108(i) of the Internal Revenue Code shall apply mutatis mutandis. No other deferral shall be allowed for income from the discharge of indebtedness in connection with the reacquisition of an "applicable debt instrument.";

5. The amount of the deduction allowed for domestic production activities pursuant to § 199 of the Internal Revenue Code for taxable years beginning on or after January 1, 2010. For Virginia income tax purposes, two-thirds of the amount deducted pursuant to § 199 of the Internal Revenue Code for federal income tax purposes during the taxable year may be deducted for Virginia income tax purposes for taxable years beginning on and after January 1, 2010. For taxable years beginning on and after January 1, 2013, the entire amount of the deduction allowed for domestic production activities pursuant to § 199 of the Internal Revenue Code may be deducted for Virginia income tax purposes;

6. The provisions of the Tax Cuts and Jobs Act (the Act) enacted December 22, 2017, as Public Law 115-97, provided, however, that this exception shall not apply to the following:

a. Treatment of certain individuals performing services in the Sinai Peninsula of Egypt pursuant to § 11026 of the Act;

b. Relief for 2016 disaster areas pursuant to § 11028 of the Act;

c. Any other provision of the Act that affects the computation of federal adjusted gross income of individuals or federal taxable income of corporations for taxable years beginning after December 31, 2016, and before January 1, 2018, other than the temporary reduction in the medical expense deduction floor pursuant to § 11027 of the Act; and

7. The provisions of the Bipartisan Budget Act of 2018 enacted February 9, 2018, as Public Law 115-123, that affect any taxable year other than a taxable year beginning after December 31, 2016, and before January 1, 2018.

The Department of Taxation is hereby authorized to develop procedures or guidelines for implementation of the provisions of this section, which procedures or guidelines shall be exempt from

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the provisions of the Administrative Process Act (§ 2.2-4000 et seq.).

§ 58.1-320. Imposition of tax.

A tax is hereby annually imposed on the Virginia taxable income for each taxable year of every individual as follows:

~~Two~~ For taxable years beginning before January 1, 2020, two percent on income not ~~exceeding~~ in excess of \$3,000;

For taxable years beginning on and after January 1, 2020, two percent on income not in excess of \$3,000 adjusted each year by the percentage, if any, by which the Chained Consumer Price Index for All Urban Consumers (C-CPI-U), as published by the U.S. Department of Labor or any successor index, for the most recent calendar year differs from the C-CPI-U published at the close of the 12-month period ending on December 31, 2019;

~~Three~~ For taxable years beginning before January 1, 2020, three percent on income in excess of \$3,000, but not in excess of \$5,000;

For taxable years beginning on and after January 1, 2020, three percent on income in excess of \$3,000, but not in excess of \$5,000, adjusted each year by the percentage, if any, by which the Chained Consumer Price Index for All Urban Consumers (C-CPI-U), as published by the U.S. Department of Labor or any successor index, for the most recent calendar year differs from the C-CPI-U published at the close of the 12-month period ending on December 31, 2019;

Five percent on income in excess of \$5,000, but not in excess of \$12,000 for taxable years beginning before January 1, 1987;

Five percent on income in excess of \$5,000 but not in excess of \$14,000 for taxable years beginning January 1, 1987, through December 31, 1987;

Five percent on income in excess of \$5,000 but not in excess of \$15,000 for taxable years beginning January 1, 1988, through December 31, 1988;

Five percent on income in excess of \$5,000 but not in excess of \$16,000 for taxable years beginning January 1, 1989, through December 31, 1989;

~~Five~~ For taxable years beginning before January 1, 2020, five percent on income in excess of \$5,000 but not in excess of \$17,000 for taxable years beginning January 1, 1990;

For taxable years beginning on and after January 1, 2020, five percent on income in excess of \$5,000, but not in excess of \$17,000, adjusted each year by the percentage, if any, by which the Chained Consumer Price Index for All Urban Consumers (C-CPI-U), as published by the U.S. Department of Labor or any successor index, for the most recent calendar year differs from the C-CPI-U published at the close of the 12-month period ending on December 31, 2019;

Five and three-quarters percent on income in excess of \$12,000 for taxable years beginning before January 1, 1987;

Five and three-quarters percent on income in excess of \$14,000 for taxable years beginning January 1, 1987, through December 31, 1987;

Five and three-quarters percent on income in excess of \$15,000 for taxable years beginning January 1, 1988, through December 31, 1988;

Five and three-quarters percent on income in excess of \$16,000 for taxable years beginning January 1, 1989, through December 31, 1989; and

Five and three-quarters For taxable years beginning before January 1, 2020, five and three-quarters percent on income in excess of \$17,000 for taxable years beginning on and after January 1, 1990; and

For taxable years beginning on and after January 1, 2020, five and three-quarters percent on income in excess of \$17,000, adjusted each year by the percentage, if any, by which the Chained Consumer Price Index for All Urban Consumers (C-CPI-U), as published by the U.S. Department of Labor or any successor index, for the most recent calendar year differs from the C-CPI-U published at the close of the 12-month period ending on December 31, 2019.

§ 58.1-322.03. Virginia taxable income; deductions.

In computing Virginia taxable income pursuant to § 58.1-322, there shall be deducted from Virginia adjusted gross income as defined in § 58.1-321:

1. a. The amount allowable for itemized deductions for federal income tax purposes where the taxpayer has elected for the taxable year to itemize deductions on his federal return, but reduced by the amount of income taxes imposed by the Commonwealth or any other taxing jurisdiction and deducted on such federal return and increased by an amount that, when added to the amount deducted under § 170 of the Internal Revenue Code for mileage, results in a mileage deduction at the state level for such purposes at a rate of 18 cents per mile; or

b. ~~Three thousand dollars~~ Provided that the taxpayer has not itemized deductions for the taxable year on his federal income tax return, (i) for taxable years beginning before January 1, 2018, and on and after January 1, 2026, \$3,000 for single individuals and \$6,000 for married persons (one-half of such amounts in the case of a married individual filing a separate return); ~~provided that the taxpayer has not itemized deductions for the taxable year on his federal income tax return;~~ (ii) for taxable years

beginning on and after January 1, 2018, but before January 1, 2019, \$6,000 for single individuals and \$12,000 for married persons (one-half of such amounts in the case of a married individual filing a separate return); and (iii) for taxable years beginning on and after January 1, 2019, but before January 1, 2026, an amount equal to the deductions set forth in clause (ii), adjusted each year by the percentage, if any, by which the Chained Consumer Price Index for All Urban Consumers (C-CPI-U), as published by the U.S. Department of Labor or any successor index, for the most recent calendar year differs from the C-CPI-U published at the close of the 12-month period ending on December 31, 2018. In no case shall the amount of the adjusted deduction be less than the amounts set forth in clause (ii).

For purposes of this section, any person who may be claimed as a dependent on another taxpayer's return for the taxable year may compute the deduction only with respect to earned income.

2. a. A deduction in the amount of \$930 for each personal exemption allowable to the taxpayer for federal income tax purposes. For taxable years beginning on and after January 1, 2020, such amount shall be adjusted each year by the percentage, if any, by which the Chained Consumer Price Index for All Urban Consumers (C-CPI-U), as published by the U.S. Department of Labor or any successor index, for the most recent calendar year differs from the C-CPI-U published at the close of the 12-month period ending on December 31, 2019.

b. Each blind or aged taxpayer as defined under § 63(f) of the Internal Revenue Code shall be entitled to an additional personal exemption in the amount of \$800. For taxable years beginning on and after January 1, 2020, such amount shall be adjusted each year by the percentage, if any, by which the Chained Consumer Price Index for All Urban Consumers (C-CPI-U), as published by the U.S. Department of Labor or any successor index, for the most recent calendar year differs from the C-CPI-U published at the close of the 12-month period ending on December 31, 2019.

The additional deduction for blind or aged taxpayers allowed under this subdivision shall be allowable regardless of whether the taxpayer itemizes deductions for the taxable year for federal income tax purposes.

3. A deduction equal to the amount of employment-related expenses upon which the federal credit is based under § 21 of the Internal Revenue Code for expenses for household and dependent care services necessary for gainful employment.

4. An additional \$1,000 deduction for each child residing for the entire taxable year in a home under permanent foster care placement as defined in § 63.2-908, provided that the taxpayer can also claim the child as a personal exemption under § 151 of the Internal Revenue Code.

5. a. A deduction in the amount of \$12,000 for individuals born on or before January 1, 1939.

b. A deduction in the amount of \$12,000 for individuals born after January 1, 1939, who have attained the age of 65. This deduction shall be reduced by \$1 for every \$1 that the taxpayer's adjusted federal adjusted gross income exceeds \$50,000 for single taxpayers or \$75,000 for married taxpayers. For married taxpayers filing separately, the deduction shall be reduced by \$1 for every \$1 that the total combined adjusted federal adjusted gross income of both spouses exceeds \$75,000.

For the purposes of this subdivision, "adjusted federal adjusted gross income" means federal adjusted gross income minus any benefits received under Title II of the Social Security Act and other benefits subject to federal income taxation solely pursuant to § 86 of the Internal Revenue Code, as amended.

6. The amount an individual pays as a fee for an initial screening to become a possible bone marrow donor, if (i) the individual is not reimbursed for such fee or (ii) the individual has not claimed a deduction for the payment of such fee on his federal income tax return.

7. a. A deduction shall be allowed to the purchaser or contributor for the amount paid or contributed during the taxable year for a prepaid tuition contract or college savings trust account entered into with the Virginia College Savings Plan, pursuant to Chapter 7 (§ 23.1-700 et seq.) of Title 23.1. Except as provided in subdivision b, the amount deducted on any individual income tax return in any taxable year shall be limited to \$4,000 per prepaid tuition contract or college savings trust account. No deduction shall be allowed pursuant to this subdivision 7 if such payments or contributions are deducted on the purchaser's or contributor's federal income tax return. If the purchase price or annual contribution to a college savings trust account exceeds \$4,000, the remainder may be carried forward and subtracted in future taxable years until the purchase price or college savings trust contribution has been fully deducted; however, except as provided in subdivision b, in no event shall the amount deducted in any taxable year exceed \$4,000 per contract or college savings trust account. Notwithstanding the statute of limitations on assessments contained in § 58.1-312, any deduction taken hereunder shall be subject to recapture in the taxable year or years in which distributions or refunds are made for any reason other than (i) to pay qualified higher education expenses, as defined in § 529 of the Internal Revenue Code or (ii) the beneficiary's death, disability, or receipt of a scholarship. For the purposes of this subdivision, "purchaser" or "contributor" means the person shown as such on the records of the Virginia College Savings Plan as of December 31 of the taxable year. In the case of a transfer of ownership of a prepaid tuition contract or college savings trust account, the transferee shall succeed to the transferor's tax

182 attributes associated with a prepaid tuition contract or college savings trust account, including, but not
183 limited to, carryover and recapture of deductions.

184 b. A purchaser of a prepaid tuition contract or contributor to a college savings trust account who has
185 attained age 70 shall not be subject to the limitation that the amount of the deduction not exceed \$4,000
186 per prepaid tuition contract or college savings trust account in any taxable year. Such taxpayer shall be
187 allowed a deduction for the full amount paid for the contract or contributed to a college savings trust
188 account, less any amounts previously deducted.

189 8. The total amount an individual actually contributed in funds to the Virginia Public School
190 Construction Grants Program and Fund, established in Chapter 11.1 (§ 22.1-175.1 et seq.) of Title 22.1,
191 provided that the individual has not claimed a deduction for such amount on his federal income tax
192 return.

193 9. An amount equal to 20 percent of the tuition costs incurred by an individual employed as a
194 primary or secondary school teacher licensed pursuant to Chapter 15 (§ 22.1-289.1 et seq.) of Title 22.1
195 to attend continuing teacher education courses that are required as a condition of employment; however,
196 the deduction provided by this subdivision shall be available only if (i) the individual is not reimbursed
197 for such tuition costs and (ii) the individual has not claimed a deduction for the payment of such tuition
198 costs on his federal income tax return.

199 10. The amount an individual pays annually in premiums for long-term health care insurance,
200 provided that the individual has not claimed a deduction for federal income tax purposes, or, for taxable
201 years beginning before January 1, 2014, a credit under § 58.1-339.11. For taxable years beginning on
202 and after January 1, 2014, no such deduction for long-term health care insurance premiums paid by the
203 individual during the taxable year shall be allowed if the individual has claimed a federal income tax
204 deduction for such taxable year for long-term health care insurance premiums paid by him.

205 11. Contract payments to a producer of quota tobacco or a tobacco quota holder, or their spouses, as
206 provided under the American Jobs Creation Act of 2004 (P.L. 108-357), but only to the extent that such
207 payments have not been subtracted pursuant to subsection D of § 58.1-402, as follows:

208 a. If the payment is received in installment payments, then the recognized gain may be subtracted in
209 the taxable year immediately following the year in which the installment payment is received.

210 b. If the payment is received in a single payment, then 10 percent of the recognized gain may be
211 subtracted in the taxable year immediately following the year in which the single payment is received.
212 The taxpayer may then deduct an equal amount in each of the nine succeeding taxable years.

213 12. An amount equal to 20 percent of the sum paid by an individual pursuant to Chapter 6
214 (§ 58.1-600 et seq.), not to exceed \$500 in each taxable year, in purchasing for his own use the
215 following items of tangible personal property: (i) any clothes washers, room air conditioners,
216 dishwashers, and standard size refrigerators that meet or exceed the applicable energy star efficiency
217 requirements developed by the U.S. Environmental Protection Agency and the U.S. Department of
218 Energy; (ii) any fuel cell that (a) generates electricity using an electrochemical process, (b) has an
219 electricity-only generation efficiency greater than 35 percent, and (c) has a generating capacity of at least
220 two kilowatts; (iii) any gas heat pump that has a coefficient of performance of at least 1.25 for heating
221 and at least 0.70 for cooling; (iv) any electric heat pump hot water heater that yields an energy factor of
222 at least 1.7; (v) any electric heat pump that has a heating system performance factor of at least 8.0 and
223 a cooling seasonal energy efficiency ratio of at least 13.0; (vi) any central air conditioner that has a
224 cooling seasonal energy efficiency ratio of at least 13.5; (vii) any advanced gas or oil water heater that
225 has an energy factor of at least 0.65; (viii) any advanced oil-fired boiler with a minimum annual
226 fuel-utilization rating of 85; (ix) any advanced oil-fired furnace with a minimum annual fuel-utilization
227 rating of 85; and (x) programmable thermostats.

228 13. The lesser of \$5,000 or the amount actually paid by a living donor of an organ or other living
229 tissue for unreimbursed out-of-pocket expenses directly related to the donation that arose within 12
230 months of such donation, provided that the donor has not taken a medical deduction in accordance with
231 the provisions of § 213 of the Internal Revenue Code for such expenses. The deduction may be taken in
232 the taxable year in which the donation is made or the taxable year in which the 12-month period
233 expires.

234 14. For taxable years beginning on and after January 1, 2013, the amount an individual age 66 or
235 older with earned income of at least \$20,000 for the year and federal adjusted gross income not in
236 excess of \$30,000 for the year pays annually in premiums for (i) a prepaid funeral insurance policy
237 covering the individual or (ii) medical or dental insurance for any person for whom individual tax filers
238 may claim a deduction for such premiums under federal income tax laws. As used in this subdivision,
239 "earned income" means the same as that term is defined in § 32(c) of the Internal Revenue Code. The
240 deduction shall not be allowed for any portion of such premiums paid for which the individual has (a)
241 been reimbursed, (b) claimed a deduction for federal income tax purposes, (c) claimed a deduction or
242 subtraction under another provision of this section, or (d) claimed a federal income tax credit or any
243 income tax credit pursuant to this chapter.

§ 58.1-400. Imposition of tax.

A tax at the rate of six percent is hereby annually imposed on the Virginia taxable income for each taxable year of every corporation organized under the laws of the Commonwealth and every foreign corporation having income from Virginia sources. *The rate of the tax shall be as follows:*

1. *For taxable years beginning before January 1, 2018, six percent;*
2. *For taxable years beginning on and after January 1, 2018, but before January 1, 2019, five and one-half percent; and*
3. *For taxable years beginning on and after January 1, 2019, five percent.*

§ 58.1-402. Virginia taxable income.

A. For purposes of this article, Virginia taxable income for a taxable year means the federal taxable income and any other income taxable to the corporation under federal law for such year of a corporation adjusted as provided in subsections B, C, D, and E.

For a regulated investment company and a real estate investment trust, such term means the "investment company taxable income" and "real estate investment trust taxable income," respectively, to which shall be added in each case any amount of capital gains and any other income taxable to the corporation under federal law which shall be further adjusted as provided in subsections B, C, D, and E.

B. There shall be added to the extent excluded from federal taxable income:

1. Interest, less related expenses to the extent not deducted in determining federal taxable income, on obligations of any state other than Virginia, or of a political subdivision of any such other state unless created by compact or agreement to which the Commonwealth is a party;

2. Interest or dividends, less related expenses to the extent not deducted in determining federal taxable income, on obligations or securities of any authority, commission or instrumentality of the United States, which the laws of the United States exempt from federal income tax but not from state income taxes;

3. [Repealed.]

4. The amount of any net income taxes and other taxes, including franchise and excise taxes, which are based on, measured by, or computed with reference to net income, imposed by the Commonwealth or any other taxing jurisdiction, to the extent deducted in determining federal taxable income;

5. Unrelated business taxable income as defined by § 512 of the Internal Revenue Code;

6. [Repealed.]

7. The amount required to be included in income for the purpose of computing the partial tax on an accumulation distribution pursuant to § 667 of the Internal Revenue Code;

8. a. For taxable years beginning on and after January 1, 2004, the amount of any intangible expenses and costs directly or indirectly paid, accrued, or incurred to, or in connection directly or indirectly with one or more direct or indirect transactions with one or more related members to the extent such expenses and costs were deductible or deducted in computing federal taxable income for Virginia purposes. This addition shall not be required for any portion of the intangible expenses and costs if one of the following applies:

(1) The corresponding item of income received by the related member is subject to a tax based on or measured by net income or capital imposed by Virginia, another state, or a foreign government that has entered into a comprehensive tax treaty with the United States government;

(2) The related member derives at least one-third of its gross revenues from the licensing of intangible property to parties who are not related members, and the transaction giving rise to the expenses and costs between the corporation and the related member was made at rates and terms comparable to the rates and terms of agreements that the related member has entered into with parties who are not related members for the licensing of intangible property; or

(3) The corporation can establish to the satisfaction of the Tax Commissioner that the intangible expenses and costs meet both of the following: (i) the related member during the same taxable year directly or indirectly paid, accrued or incurred such portion to a person who is not a related member, and (ii) the transaction giving rise to the intangible expenses and costs between the corporation and the related member did not have as a principal purpose the avoidance of any portion of the tax due under this chapter.

b. A corporation required to add to its federal taxable income intangible expenses and costs pursuant to subdivision a may petition the Tax Commissioner, after filing the related income tax return for the taxable year and remitting to the Tax Commissioner all taxes, penalties, and interest due under this article for such taxable year including tax upon any amount of intangible expenses and costs required to be added to federal taxable income pursuant to subdivision a, to consider evidence relating to the transaction or transactions between the corporation and a related member or members that resulted in the corporation's taxable income being increased, as required under subdivision a, for such intangible expenses and costs.

If the corporation can demonstrate to the Tax Commissioner's sole satisfaction, by clear and

convincing evidence, that the transaction or transactions between the corporation and a related member or members resulting in such increase in taxable income pursuant to subdivision a had a valid business purpose other than the avoidance or reduction of the tax due under this chapter, the Tax Commissioner shall permit the corporation to file an amended return. For purposes of such amended return, the requirements of subdivision a shall not apply to any transaction for which the Tax Commissioner is satisfied (and has identified) that the transaction had a valid business purpose other than the avoidance or reduction of the tax due under this chapter. Such amended return shall be filed by the corporation within one year of the written permission granted by the Tax Commissioner and any refund of the tax imposed under this article shall include interest at a rate equal to the rate of interest established under § 58.1-15 and such interest shall accrue as provided under § 58.1-1833. However, upon the filing of such amended return, any related member of the corporation that subtracted from taxable income amounts received pursuant to subdivision C 21 shall be subject to the tax imposed under this article on that portion of such amounts for which the corporation has filed an amended return pursuant to this subdivision. In addition, for such transactions identified by the Tax Commissioner herein by which he has been satisfied by clear and convincing evidence, the Tax Commissioner may permit the corporation in filing income tax returns for subsequent taxable years to deduct the related intangible expenses and costs without making the adjustment under subdivision a.

The Tax Commissioner may charge a fee for all direct and indirect costs relating to the review of any petition pursuant to this subdivision, to include costs necessary to secure outside experts in evaluating the petition. The Tax Commissioner may condition the review of any petition pursuant to this subdivision upon payment of such fee.

No suit for the purpose of contesting any action of the Tax Commissioner under this subdivision shall be maintained in any court of this Commonwealth.

c. Nothing in subdivision B 8 shall be construed to limit or negate the Department's authority under § 58.1-446;

9. a. For taxable years beginning on and after January 1, 2004, the amount of any interest expenses and costs directly or indirectly paid, accrued, or incurred to, or in connection directly or indirectly with one or more direct or indirect transactions with one or more related members to the extent such expenses and costs were deductible or deducted in computing federal taxable income for Virginia purposes. This addition shall not be required for any portion of the interest expenses and costs, if:

(1) The related member has substantial business operations relating to interest-generating activities, in which the related member pays expenses for at least five full-time employees who maintain, manage, defend or are otherwise responsible for operations or administration relating to the interest-generating activities; and

(2) The interest expenses and costs are not directly or indirectly for, related to or in connection with the direct or indirect acquisition, maintenance, management, sale, exchange, or disposition of intangible property; and

(3) The transaction giving rise to the expenses and costs between the corporation and the related member has a valid business purpose other than the avoidance or reduction of taxation and payments between the parties are made at arm's length rates and terms; and

(4) One of the following applies:

(i) The corresponding item of income received by the related member is subject to a tax based on or measured by net income or capital imposed by Virginia, another state, or a foreign government that has entered into a comprehensive tax treaty with the United States government;

(ii) Payments arise pursuant to a pre-existing contract entered into when the parties were not related members provided the payments continue to be made at arm's length rates and terms;

(iii) The related member engages in transactions with parties other than related members that generate revenue in excess of \$2 million annually; or

(iv) The transaction giving rise to the interest payments between the corporation and a related member was done at arm's length rates and terms and meets any of the following: (a) the related member uses funds that are borrowed from a party other than a related member or that are paid, incurred or passed-through to a person who is not a related member; (b) the debt is part of a regular and systematic funds management or portfolio investment activity conducted by the related member, whereby the funds of two or more related members are aggregated for the purpose of achieving economies of scale, the internal financing of the active business operations of members, or the benefit of centralized management of funds; (c) financing the expansion of the business operations; or (d) restructuring the debt of related members, or the pass-through of acquisition-related indebtedness to related members.

b. A corporation required to add to its federal taxable income interest expenses and costs pursuant to subdivision a may petition the Tax Commissioner, after filing the related income tax return for the taxable year and remitting to the Tax Commissioner all taxes, penalties, and interest due under this article for such taxable year including tax upon any amount of interest expenses and costs required to be added to federal taxable income pursuant to subdivision a, to consider evidence relating to the

transaction or transactions between the corporation and a related member or members that resulted in the corporation's taxable income being increased, as required under subdivision a, for such interest expenses and costs.

If the corporation can demonstrate to the Tax Commissioner's sole satisfaction, by clear and convincing evidence, that the transaction or transactions between the corporation and a related member or members resulting in such increase in taxable income pursuant to subdivision a had a valid business purpose other than the avoidance or reduction of the tax due under this chapter and that the related payments between the parties were made at arm's length rates and terms, the Tax Commissioner shall permit the corporation to file an amended return. For purposes of such amended return, the requirements of subdivision a shall not apply to any transaction for which the Tax Commissioner is satisfied (and has identified) that the transaction had a valid business purpose other than the avoidance or reduction of the tax due under this chapter and that the related payments between the parties were made at arm's length rates and terms. Such amended return shall be filed by the corporation within one year of the written permission granted by the Tax Commissioner and any refund of the tax imposed under this article shall include interest at a rate equal to the rate of interest established under § 58.1-15 and such interest shall accrue as provided under § 58.1-1833. However, upon the filing of such amended return, any related member of the corporation that subtracted from taxable income amounts received pursuant to subdivision C 21 shall be subject to the tax imposed under this article on that portion of such amounts for which the corporation has filed an amended return pursuant to this subdivision. In addition, for such transactions identified by the Tax Commissioner herein by which he has been satisfied by clear and convincing evidence, the Tax Commissioner may permit the corporation in filing income tax returns for subsequent taxable years to deduct the related interest expenses and costs without making the adjustment under subdivision a.

The Tax Commissioner may charge a fee for all direct and indirect costs relating to the review of any petition pursuant to this subdivision, to include costs necessary to secure outside experts in evaluating the petition. The Tax Commissioner may condition the review of any petition pursuant to this subdivision upon payment of such fee.

No suit for the purpose of contesting any action of the Tax Commissioner under this subdivision shall be maintained in any court of this Commonwealth.

c. Nothing in subdivision B 9 shall be construed to limit or negate the Department's authority under § 58.1-446.

d. For purposes of subdivision B 9:

"Arm's-length rates and terms" means that (i) two or more related members enter into a written agreement for the transaction, (ii) such agreement is of a duration and contains payment terms substantially similar to those that the related member would be able to obtain from an unrelated entity, (iii) the interest is at or below the applicable federal rate compounded annually for debt instruments under § 1274(d) of the Internal Revenue Code that was in effect at the time of the agreement, and (iv) the borrower or payor adheres to the payment terms of the agreement governing the transaction or any amendments thereto.

"Valid business purpose" means one or more business purposes that alone or in combination constitute the motivation for some business activity or transaction, which activity or transaction improves, apart from tax effects, the economic position of the taxpayer, as further defined by regulation.

10. a. For taxable years beginning on and after January 1, 2009, the amount of dividends deductible under §§ 561 and 857 of the Internal Revenue Code by a Captive Real Estate Investment Trust (REIT). For purposes of this subdivision, a REIT is a Captive REIT if:

(1) It is not regularly traded on an established securities market;

(2) More than 50 percent of the voting power or value of beneficial interests or shares of which, at any time during the last half of the taxable year, is owned or controlled, directly or indirectly, by a single entity that is (i) a corporation or an association taxable as a corporation under the Internal Revenue Code; and (ii) not exempt from federal income tax pursuant to § 501(a) of the Internal Revenue Code; and

(3) More than 25 percent of its income consists of rents from real property as defined in § 856(d) of the Internal Revenue Code.

b. For purposes of applying the ownership test of subdivision 10 a (2), the following entities shall not be considered a corporation or an association taxable as a corporation:

(1) Any REIT that is not treated as a Captive REIT;

(2) Any REIT subsidiary under § 856 of the Internal Revenue Code other than a qualified REIT subsidiary of a Captive REIT;

(3) Any Listed Australian Property Trust, or an entity organized as a trust, provided that a Listed Australian Property Trust owns or controls, directly or indirectly, 75 percent or more of the voting or value of the beneficial interests or shares of such trust; and

428 (4) Any Qualified Foreign Entity.

429 c. For purposes of subdivision B 10, the constructive ownership rules prescribed under § 318(a) of
430 the Internal Revenue Code, as modified by § 856(d)(5) of the Internal Revenue Code, shall apply in
431 determining the ownership of stock, assets, or net profits of any person.

432 d. For purposes of subdivision B 10:

433 "Listed Australian Property Trust" means an Australian unit trust registered as a Management
434 Investment Scheme, pursuant to the Australian Corporations Act, in which the principal class of units is
435 listed on a recognized stock exchange in Australia and is regularly traded on an established securities
436 market.

437 "Qualified Foreign Entity" means a corporation, trust, association or partnership organized outside the
438 laws of the United States and that satisfies all of the following criteria:

439 (1) At least 75 percent of the entity's total asset value at the close of its taxable year is represented
440 by real estate assets, as defined in § 856(c)(5)(B) of the Internal Revenue Code, thereby including shares
441 or certificates of beneficial interest in any REIT, cash and cash equivalents, and U.S. Government
442 securities;

443 (2) The entity is not subject to a tax on amounts distributed to its beneficial owners, or is exempt
444 from entity level tax;

445 (3) The entity distributes, on an annual basis, at least 85 percent of its taxable income, as computed
446 in the jurisdiction in which it is organized, to the holders of its shares or certificates of beneficial
447 interest;

448 (4) The shares or certificates of beneficial interest of such entity are regularly traded on an
449 established securities market or, if not so traded, not more than 10 percent of the voting power or value
450 in such entity is held directly, indirectly, or constructively by a single entity or individual; and

451 (5) The entity is organized in a country that has a tax treaty with the United States.

452 e. For taxable years beginning on or after January 1, 2016, for purposes of subdivision B 10, any
453 voting power or value of the beneficial interests or shares in a REIT that is held in a segregated asset
454 account of a life insurance corporation as described in § 817 of the Internal Revenue Code shall not be
455 taken into consideration when determining if such REIT is a Captive REIT.

456 11. For taxable years beginning on or after January 1, 2016, to the extent that tax credit is allowed
457 for the same donation pursuant to § 58.1-439.12:12, any amount claimed as a federal income tax
458 deduction for such donation under § 170 of the Internal Revenue Code, as amended or renumbered.

459 C. There shall be subtracted to the extent included in and not otherwise subtracted from federal
460 taxable income:

461 1. Income derived from obligations, or on the sale or exchange of obligations, of the United States
462 and on obligations or securities of any authority, commission or instrumentality of the United States to
463 the extent exempt from state income taxes under the laws of the United States including, but not limited
464 to, stocks, bonds, treasury bills, and treasury notes, but not including interest on refunds of federal taxes,
465 interest on equipment purchase contracts, or interest on other normal business transactions.

466 2. Income derived from obligations, or on the sale or exchange of obligations of this Commonwealth
467 or of any political subdivision or instrumentality of this Commonwealth.

468 3. Dividends upon stock in any domestic international sales corporation, as defined by § 992 of the
469 Internal Revenue Code, 50 percent or more of the income of which was assessable for the preceding
470 year, or the last year in which such corporation has income, under the provisions of the income tax laws
471 of the Commonwealth.

472 4. The amount of any refund or credit for overpayment of income taxes imposed by this
473 Commonwealth or any other taxing jurisdiction.

474 5. Any amount included therein by the operation of the provisions of § 78 of the Internal Revenue
475 Code (foreign dividend gross-up).

476 6. The amount of wages or salaries eligible for the federal Targeted Jobs Credit which was not
477 deducted for federal purposes on account of the provisions of § 280C(a) of the Internal Revenue Code.

478 7. Any amount included therein by the operation of § 951 of the Internal Revenue Code (subpart F
479 income) or § 951A of the Internal Revenue Code (Global Intangible Low-Taxed Income).

480 8. Any amount included therein which is foreign source income as defined in § 58.1-302.

481 9. [Repealed.]

482 10. The amount of any dividends received from corporations in which the taxpaying corporation
483 owns 50 percent or more of the voting stock.

484 11. [Repealed.]

485 12, 13. [Expired.]

486 14. For taxable years beginning on or after January 1, 1995, the amount for "qualified research
487 expenses" or "basic research expenses" eligible for deduction for federal purposes, but which were not
488 deducted, on account of the provisions of § 280C(c) of the Internal Revenue Code.

489 15. For taxable years beginning on or after January 1, 2000, the total amount actually contributed in

funds to the Virginia Public School Construction Grants Program and Fund established in Chapter 11.1 (§ 22.1-175.1 et seq.) of Title 22.1.

16. For taxable years beginning on or after January 1, 2000, but before January 1, 2015, the gain derived from the sale or exchange of real property or the sale or exchange of an easement to real property which results in the real property or the easement thereto being devoted to open-space use, as that term is defined in § 58.1-3230, for a period of time not less than 30 years. To the extent a subtraction is taken in accordance with this subdivision, no tax credit under this chapter for donating land for its preservation shall be allowed for three years following the year in which the subtraction is taken.

17. For taxable years beginning on and after January 1, 2001, any amount included therein with respect to § 58.1-440.1.

18. For taxable years beginning on and after January 1, 1999, income received as a result of (i) the "Master Settlement Agreement," as defined in § 3.2-3100; and (ii) the National Tobacco Grower Settlement Trust dated July 19, 1999, by (a) tobacco farming businesses; (b) any business holding a tobacco marketing quota, or tobacco farm acreage allotment, under the Agricultural Adjustment Act of 1938; or (c) any business having the right to grow tobacco pursuant to such a quota allotment.

19, 20. [Repealed.]

21. For taxable years beginning on and after January 1, 2004, any amount of intangible expenses and costs or interest expenses and costs added to the federal taxable income of a corporation pursuant to subdivision B 8 or B 9 shall be subtracted from the federal taxable income of the related member that received such amount if such related member is subject to Virginia income tax on the same amount.

22. For taxable years beginning on and after January 1, 2009, any gain recognized from the sale of launch services to space flight participants, as defined in 49 U.S.C. § 70102, or launch services intended to provide individuals the training or experience of a launch, without performing an actual launch. To qualify for a deduction under this subdivision, launch services must be performed in Virginia or originate from an airport or spaceport in Virginia.

23. For taxable years beginning on and after January 1, 2009, any gain recognized as a result of resupply services contracts for delivering payload, as defined in 49 U.S.C. § 70102, entered into with the Commercial Orbital Transportation Services division of the National Aeronautics and Space Administration or other space flight entity, as defined in § 8.01-227.8, and launched from an airport or spaceport in Virginia.

24. For taxable years beginning on or after January 1, 2011, any income taxed as a long-term capital gain for federal income tax purposes, or any income taxed as investment services partnership interest income (otherwise known as investment partnership carried interest income) for federal income tax purposes. To qualify for a subtraction under this subdivision, such income must be attributable to an investment in a "qualified business," as defined in § 58.1-339.4, or in any other technology business approved by the Secretary of Technology, provided the business has its principal office or facility in the Commonwealth and less than \$3 million in annual revenues in the fiscal year prior to the investment. To qualify for a subtraction under this subdivision, the investment must be made between the dates of April 1, 2010, and June 30, 2020. No taxpayer who has claimed a tax credit for an investment in a "qualified business" under § 58.1-339.4 shall be eligible for the subtraction under this subdivision for an investment in the same business.

25. a. Income, including investment services partnership interest income (otherwise known as investment partnership carried interest income), attributable to an investment in a Virginia venture capital account. To qualify for a subtraction under this subdivision, the investment shall be made on or after January 1, 2018, but before December 31, 2023. No subtraction shall be allowed under this subdivision for an investment in a company that is owned or operated by an affiliate of the taxpayer. No subtraction shall be allowed under this subdivision for a taxpayer who has claimed a subtraction under subdivision C 24 for the same investment.

b. As used in this subdivision 25:

"Qualified portfolio company" means a company that (i) has its principal place of business in the Commonwealth; (ii) has a primary purpose of production, sale, research, or development of a product or service other than the management or investment of capital; and (iii) provides equity in the company to the Virginia venture capital account in exchange for a capital investment. "Qualified portfolio company" does not include a company that is an individual or sole proprietorship.

"Virginia venture capital account" means an investment fund that has been certified by the Department as a Virginia venture capital account. In order to be certified as a Virginia venture capital account, the operator of the investment fund shall register the investment fund with the Department prior to December 31, 2023, (i) indicating that it intends to invest at least 50 percent of the capital committed to its fund in qualified portfolio companies and (ii) providing documentation that it employs at least one investor who has at least four years of professional experience in venture capital investment or

substantially equivalent experience. "Substantially equivalent experience" includes, but is not limited to, an undergraduate degree from an accredited college or university in economics, finance, or a similar field of study. The Department may require an investment fund to provide documentation of the investor's training, education, or experience as deemed necessary by the Department to determine substantial equivalency. If the Department determines that the investment fund employs at least one investor with the experience set forth herein, the Department shall certify the investment fund as a Virginia venture capital account at such time as the investment fund actually invests at least 50 percent of the capital committed to its fund in qualified portfolio companies.

26. a. Income attributable to an investment in a Virginia real estate investment trust. To qualify for a subtraction under this subdivision, the investment shall be made on or after January 1, 2019, but before December 31, 2024. No subtraction shall be allowed for an investment in a trust that is managed by an affiliate of the taxpayer. No subtraction shall be allowed under this subdivision for a taxpayer who has claimed a subtraction under subdivision C 24 or 25 for the same investment.

b. As used in this subdivision 26:

"Distressed" means satisfying the criteria applicable to a locality described in subdivision E 2 of § 2.2-115.

"Double distressed" means satisfying the criteria applicable to a locality described in subdivision E 3 of § 2.2-115.

"Virginia real estate investment trust" means a real estate investment trust, as defined in 26 U.S.C. § 856, that has been certified by the Department as a Virginia real estate investment trust. In order to be certified as a Virginia real estate investment trust, the trustee shall register the trust with the Department prior to December 31, 2024, indicating that it intends to invest at least 90 percent of trust funds in Virginia and at least 40 percent of trust funds in real estate in localities that are distressed or double distressed. If the Department determines that the trust satisfies the preceding criteria, the Department shall certify the trust as a Virginia real estate investment trust at such time as the trust actually invests at least 90 percent of trust funds in Virginia and at least 40 percent of trust funds in real estate in localities that are distressed or double distressed.

27. *Any amount of business interest disallowed as a deduction pursuant to § 163(j) of the Internal Revenue Code. For purposes of this subdivision, "business interest" means the same as that term is defined under § 163(j) of the Internal Revenue Code.*

D. For taxable years beginning on and after January 1, 2006, there shall be subtracted from federal taxable income contract payments to a producer of quota tobacco or a tobacco quota holder as provided under the American Jobs Creation Act of 2004 (P.L. 108-357) as follows:

1. If the payment is received in installment payments, then the recognized gain, including any gain recognized in taxable year 2005, may be subtracted in the taxable year immediately following the year in which the installment payment is received.

2. If the payment is received in a single payment, then 10 percent of the recognized gain may be subtracted in the taxable year immediately following the year in which the single payment is received. The taxpayer may then deduct an equal amount in each of the nine succeeding taxable years.

E. Adjustments to federal taxable income shall be made to reflect the transitional modifications provided in § 58.1-315.

F. Notwithstanding any other provision of law, the income from any disposition of real property which is held by the taxpayer for sale to customers in the ordinary course of the taxpayer's trade or business, as defined in § 453(l)(1)(B) of the Internal Revenue Code, of property made on or after January 1, 2009, may, at the election of the taxpayer, be recognized under the installment method described under § 453 of the Internal Revenue Code, provided that (i) the election relating to the dealer disposition of the property has been made on or before the due date prescribed by law (including extensions) for filing the taxpayer's return of the tax imposed under this chapter for the taxable year in which the disposition occurs, and (ii) the dealer disposition is in accordance with restrictions or conditions established by the Department, which shall be set forth in guidelines developed by the Department. Along with such restrictions or conditions, the guidelines shall also address the recapture of such income under certain circumstances. The development of the guidelines shall be exempt from the Administrative Process Act (§ 2.2-4000 et seq.).

2. That an emergency exists and this act is in force from its passage.

3. That the provisions of this act amending § 58.1-301 of the Code of Virginia shall be effective only for taxable years beginning on and after January 1, 2018.

4. That any additional revenues generated by the federal Tax Cuts and Jobs Act, P.L. 115-97 (2018), in fiscal year 2019-2020, beyond those revenues necessary to offset the reduction in revenues resulting from the provisions of this act, shall be transferred to a special nonreverting fund hereby established and to be known as the Tax Policy Fund. The Governor shall submit, with his budget proposal submitted for the 2020-2022 biennium pursuant to § 2.2-1508 of the Code of Virginia, a plan to provide tax reform to Virginia taxpayers with revenues in the Tax Policy

613 Fund.