DEPARTMENT OF TAXATION
2020 Fiscal Impact Statement

1. Patron Kathleen J. Murphy

2. Bill Number HB 844
House of Origin:
X **Introduced**
____ **Substitute**
____ **Engrossed**

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

3. Committee House Finance

4. Title Individual Income Tax; Claiming Itemized Deductions Regardless of Election on Federal Return

5. Summary/Purpose:

The bill would provide that a taxpayer may elect either to claim the Virginia standard deduction or to itemize deductions on his or her Virginia income tax return, regardless of whether the taxpayer elected for the taxable year to itemize deductions on his or her federal income tax return.

This bill is effective for taxable years beginning on and after January 1, 2020, but before January 1, 2026.

6. Budget amendment necessary: Yes.
Item(s): Page 1, Revenue Estimates
282 and 284, Department of Taxation

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

7a. Expenditure Impact:

Fiscal Year	***Dollars***	***Positions***	***Fund***
2020-21	$614,887	7	GF
2021-22	$705,312	7	GF
2022-23	$673,302	7	GF
2023-24	$681,801	7	GF
2024-25	$690,310	7	GF
2025-26	$592,230	7	GF

7b. Revenue Impact:

Fiscal Year	***Dollars***	***Fund***
2020-21	($381.4 million)	GF
2021-22	($266.4 million)	GF
2022-23	($282.4 million)	GF
2023-24	($295.4 million)	GF
2024-25	($310.4 million	GF
2025-26	($160.3 million)	GF

8. Fiscal implications:

Administrative Costs

This bill would result in administrative costs to the Department of Taxation ("the Department") of $614,887 in Fiscal Year 2021; $705,312 in Fiscal Year 2022; $673,302 in Fiscal Year 2023; $681,801 in Fiscal Year 2024; $690,310 in Fiscal Year 2025; and $592,230 in Fiscal Year 2026. Such funding would include costs for hiring two new full-time employees for customer service to respond to taxpayer calls arising from this bill and hiring five new full-time employees for compliance purposes.

Revenue Impact

This bill would result in a negative General Fund revenue impact of $381.4 million in Fiscal Year 2021; $266.4 million in Fiscal Year 2022; $282.4 million in Fiscal Year 2023; $295.4 million in Fiscal Year 2024; $310.4 million in Fiscal Year 2025; and $160.3 million in Fiscal Year 2026.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Federal Law

When completing their federal income tax return, taxpayers are generally allowed to elect to claim either the total amount of their itemized deductions or the flat amount of their standard deduction. Taxpayers will generally choose to deduct the greater of the two amounts.

Federal Standard Deduction

The standard deduction is a fixed dollar amount that reduces a taxpayer's taxable income and varies according to their filing status. The current amount of the federal standard deduction is $12,200 for single taxpayers; $18,350 for heads of household; and $24,400 for married taxpayers filing jointly.

The federal standard deduction amounts have increased significantly since 1988. The federal Tax Reform Act of 1986 increased the standard deduction amount for Taxable Year 1988 to $3,000 for individuals; $4,400 for heads of household; and $5,000 for married taxpayers filing jointly. The Act also required, beginning in Taxable Year 1989, the Internal Revenue Service to adjust the amount of such deduction annually for inflation based on the percentage change in the Consumer Price Index for Urban Consumers ("CPI-U") for the preceding calendar year. Because of these inflation adjustments, the federal standard deduction increased annually from Taxable Year 1988 through Taxable Year 2002. For Taxable Year 2002, the standard deduction amounts were $4,700 for individuals; $6,900 for heads of household; and $7,850 for married taxpayers filing jointly.

The federal Jobs and Growth Tax Relief Reconciliation Act of 2003 increased the standard deduction for married couples filing jointly to $9,500, which was equal to twice the standard deduction for single taxpayers. This was intended to eliminate the standard deduction marriage penalty. From 2003 until 2017, the federal standard deduction continued to increase annually due to inflation adjustments. For Taxable Year 2017, the standard deduction amounts were $6,350 for individuals; $9,350 for heads of household; and $12,700 for married taxpayers filing jointly.

On December 22, 2017, Congress enacted the TCJA, which substantially increased the federal standard deduction amounts beginning with Taxable Year 2018 as follows:

- From $6,350 to $12,000 for single taxpayers;
- From $9,350 to $18,000 for heads of household; and
- From $12,700 to $24,000 for married taxpayers filing jointly.

In addition, beginning with Taxable Year 2019, these amounts have been indexed for inflation based on chained CPI-U. Therefore, for Taxable Year 2020, the amount of the federal standard deduction, after indexing, is as follows:

- $24,800 for married taxpayers filing jointly;
- $18,650 for heads of household; and
- $12,400 for single taxpayers and married taxpayers filing separately.

Like most other individual provisions of the TCJA, the increase in the amount of the federal standard deduction is currently scheduled to sunset after December 31, 2025, and revert to its pre-2018 form. Future legislation would be required to make such increase effective beyond Taxable Year 2025.

Federal Itemized Deductions

In lieu of deducting the standard deduction amount, taxpayers may elect to claim up to approximately a dozen separate deductions, referred to as “itemized deductions,” on their federal return to the extent that they qualify for such deductions. The rationale for each itemized deduction is generally to take account of large or unusual personal expenditures that affect a taxpayer’s ability to pay. Certain itemized deductions are also provided as a way of encouraging certain desired behaviors and activities. The most common expenses that may be claimed as an itemized deduction include:

- Home mortgage interest;
- State and local income taxes or sales taxes (but not both);
- Real estate and personal property taxes;
- Gifts to charities;
- Casualty or theft losses;
- Unreimbursed medical expenses; and
- Unreimbursed employee business expenses.

The TCJA included a number of provisions that greatly limit or repeal certain federal itemized deductions, such as the $10,000 cap on the state and local tax deduction.

<u>Virginia Law</u>

When completing their Virginia income tax returns, taxpayers are bound by the election they made for federal purposes regarding whether to claim a standard deduction or to itemize their deductions. Therefore, if they claimed the standard deduction on their federal income tax return, they are not allowed to claim itemized deductions on their Virginia return. In contrast, if they claimed itemized deductions on their federal income tax return, they are not allowed to claim the standard deduction on their Virginia return.

Virginia's Standard Deduction

Under current law, taxpayers that do not itemize their deductions for federal purposes are permitted to claim a standard deduction on their Virginia income tax returns. During the 2019 Session, the General Assembly enacted legislation that increased the amounts of Virginia's standard deduction.

The standard deduction amounts are $4,500 for single individuals and $9,000 for married couples. Virginia's standard deduction amounts have changed over the years. The history of such changes from Taxable Year 1987 to the present is shown below:

Year	Virginia Standard Deduction for Single Taxpayers	Virginia Standard Deduction for Married Taxpayers
1987	$2,000	$2,000
1988	$2,700	$2,700
1989-2004	$3,000	$5,000
2005-2018	$3,000	$6,000
2019-present	$4,500	$9,000

Prior to 1987, the Virginia standard deduction was not a flat amount. Instead, for Taxable Year 1986 for example, the Virginia standard deduction was 15 percent of federal adjusted gross income with a $1,300 minimum and a $2,000 maximum. The Virginia standard deduction amounts are not currently indexed for inflation.

Virginia Itemized Deductions

Taxpayers that elect to itemize their deductions for federal purposes are permitted to claim such deductions on their Virginia income tax return as well. The amount of itemized deductions that may be claimed on such return is equal to the:

- Federally allowable amount of itemized deductions, *minus*

- Amount claimed as a federal deduction for income taxes paid to Virginia or any other state, locality, foreign country, or other taxing jurisdiction, *plus*

- Amount needed to increase the amount deducted federally for charitable contribution transportation to 18¢ per mile.

Other States

Of the 42 other states that impose an individual income tax, 21 states and the District of Columbia allow taxpayers to claim federal itemized deductions on their state returns. Eleven of these states (Colorado, Georgia, Maine, Maryland, Missouri, Nebraska, New Mexico, North Dakota, Oklahoma, South Carolina, and Vermont) and the District of Columbia only allow taxpayers to claim itemized deductions on their state return if they itemized for federal purposes. The remaining ten states (Arizona, Delaware, Hawaii, Idaho, Iowa, Kansas, Minnesota, Montana, New York, and Oregon) allow taxpayers to elect to itemize on their state return, regardless of whether they itemized for federal purposes.

The remaining 21 states that impose an individual income tax do not generally allow taxpayers to claim federal itemized deductions on their state return. Instead, such states have generally established their own rules for determining the state tax liability that may use state-specific credits or deductions that are substantially different from the federal itemized deduction structure.

Proposed Legislation

The bill would provide that a taxpayer may elect either to claim the Virginia standard deduction or to itemize deductions on his or her Virginia income tax return, regardless of whether the taxpayer elected for the taxable year to itemize deductions on his or her federal income tax return.

This bill is effective for taxable years beginning on and after January 1, 2020, but before January 1, 2026.

Similar Bills

House Bill 89 would increase the Virginia standard deduction from $4,500 to $4,581 for single taxpayers and married taxpayers filing separately, and from $9,000 to $9,162 for married taxpayers filing a joint return.

House Bill 1717 would increase the Virginia standard deduction from $4,500 to $6,000 for single taxpayers and married taxpayers filing separately, and from $9,000 to $12,000 for married taxpayers filing a joint return.

House Bill 735 would index Virginia's individual income tax brackets, personal exemptions, and standard deduction amounts using the Chained Consumer Price Index for All Urban Consumers.

cc : Secretary of Finance

Date: 1/23/2020 RWC
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