DEPARTMENT OF TAXATION
2001 Fiscal Impact Statement

1. Patron Whipple

2. Bill Number SB 792

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

3. Committee Senate Finance

4. Title Clean and Efficient Energy Tax Incentives

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

5. Summary/Purpose:

This bill would create two income tax credits, a sales and use tax exemption, and a reduction in the motor vehicle sales and use tax rate for various clean and efficient energy initiatives.

- The first income tax credit is for corporations who produce and sell electricity generated from wind or biomass.
- The second income tax credit is for individuals or corporations who purchase and use solar equipment to generate electricity or for water heating.
- The sales tax exemption exempts large appliances and heating and cooling systems that meet certain energy efficiency requirements.
- The motor vehicle sales and use tax rate reduction is for motor vehicles that use clean special fuels.

This income tax credits would be effective on taxable years beginning on and after January 1, 2001. An effective date is not specified for the other provisions of this bill.

6. Fiscal Impact Estimates are: Tentative. (See Line 8.)

7. Budget amendment necessary: Yes.
Item(s): Page 1, Revenue Estimate

8. Fiscal implications:

The total General Fund revenue impact of this bill is unknown. The revenue impact for certain incentives under this bill can be determined however. The two income tax credits under this bill would decrease General Fund revenues by $0.3 million in FY 2002 and FY 2003. The potential decrease in General Fund revenues due to the retail sales and use tax exemption under this bill is **unknown** because of the changing energy star requirements which may make them more stringent. However, the decrease could be as high as $6.0 million in FY 2002 and $6.8 million in FY 2003.

Based on average sales prices and the number of clean special fuel vehicles titled during the previous sales and use tax reduction from 1996 through 1999, the Department of Motor Vehicles (DMV) estimates revenue losses attributable to the motor vehicle sales and use tax provisions of this bill of approximately $38,500 per year. Data on future sales trends is both unreliable and subject to change due to technological advances in automotive fuels or other unforeseen incentives that could arise in the future. This potential market volatility puts the Commonwealth Transportation Fund at risk of substantially higher revenue losses over time.

While this bill does have costs associated with systems development, these cannot be ascertained at this time. The cost for implementing a **single** piece of legislation cannot be calculated precisely due to economies of scale. The actual cost to implement **all** legislation enacted during a given session will more than likely be less than the sum of the costs attributed to individual bills. Further, the ability to accurately predict costs is complicated because TAX is replacing its current database system. As a result, legislative changes may need to be made to both the current and the future system, depending on the effective date. Therefore, TAX is not providing specific systems costs for this bill, but will calculate the total for all tax bills once they have been acted upon favorably in both houses and prior to the conference committee report. Other administrative costs to implement this bill would be minimal.

9. Specific agency or political subdivisions affected:

Department of Taxation
Department of Motor Vehicles
Department of Mines, Minerals and Energy

10. Technical amendment necessary: Yes.

The DMV has requested that the following amendments (See Line 11.):

Page 3, Line 151, After: §
Strike: 58.1-2101
Insert: 46.2-749.3

Page 3, Line 159, After: §
Strike: 58.1-2101
Insert: 46.2-749.3

Page 4, Line 195, After: §
Strike: 58.1-2101
Insert: 46.2-749.3

Page 4, Line 212, at the end of the line

Insert: 4. That the provisions amending §§ 58.1-2402 and 58.1-2423.2 shall be effective January 1, 2002 to December 31, 2005.

11. Other comments:

This bill would create two income tax credits, a sales and use tax exemption, and a reduction in the motor vehicle sales and use tax rate for various clean and efficient energy initiatives.

Income Tax Credit for Producing Electricity from Renewable Sources

This bill would create an income tax credit for corporations equal to 0.85 cents for each kilowatt of electricity produced from qualified energy resources at a qualified Virginia facility and sold by the corporation to a non-related party. This credit would be effective for taxable years beginning on and after January 1, 2001, but before January 1, 2010.

“Qualified energy resources” are defined as wind, closed-loop biomass, and poultry waste. Closed-loop biomass means any organic material from a plant which is planted exclusively for purposes of being used to produce electricity. A “qualified Virginia facility” is a facility located in the Commonwealth that uses qualified energy resources to produce electricity.

This credit may not exceed the corporation’s tax liability in any given taxable year. Any unused credits may be carried forward for up to the earlier of five years or when the full amount of the credit is used. The corporation claiming this credit may not use the production of electricity under this legislation as the basis for claiming any other credit or grant provided for under Virginia law.

Photovoltaic and Solar Energy Tax Credit

This bill would create an income tax credit for the costs of placing photovoltaic property and solar water heating property into service during the taxable year. The credit would be equal to 15% of the total installed cost of such property, but may not exceed $2,000 for each system of photovoltaic property or $1,000 for each system of solar water heating property. This credit would be effective for taxable years beginning on and after January 1, 2001.

"Photovoltaic property" means solar energy property that uses a solar photovoltaic process to generate electricity and that meets certain requirements specified by the Department of Mines, Minerals and Energy (DMME). "Solar water heating property" means solar energy property that, when installed in connection with a structure, uses solar energy for the purpose of providing hot water for use within the structure and meets certain requirements as specified by DMME. "Solar energy property" means equipment that uses solar energy to generate electricity; to heat or cool a structure or provide hot water for use in a structure; or to provide solar process heat. Solar energy property does not include a swimming pool, hot tub, or any other storage medium that has a function other than storage.

This credit is available to individuals and corporations. This credit may not exceed the individual or the corporation's tax liability in any taxable year. Any unused credits may be carried forward for up to the earlier of five years or when the full amount of the credit is used. The individual or corporation claiming this credit may not use the production of electricity under this legislation as the basis for claiming any other credit or grant provided for under Virginia law.

In order to claim this credit, the individual or corporation would apply to DMME. DMME would then determine the proper amount of eligible costs and issue a certificate verifying such to the individual or corporation.

Retail Sales and Use Tax Exemption

This bill would provide a retail sales and use tax exemption for various energy efficient appliances. Specifically, clothes washers, room air conditioners, and standard size refrigerators that meet or exceed the energy star efficiency requirement established by the United States Environmental Protection Agency and the United States Department of Energy would be exempt from sales tax. In addition, a sales and use tax exemption would be created for fuel cells that (i) generate electricity and heat using an electrochemical process; (ii) have an electricity-only generation efficiency greater than thirty-five percent; and (iii) have a generating capacity of at least two kilowatts. Other appliances that would be exempt are:

(1) natural gas heat pumps that have a coefficient of performance of at least 1.25 for heating and at least 0.70 for cooling;
(2) electric heat pump hot water heaters that yield an energy factor of at least 1.7;
(3) electric heat pumps that have a heating system performance factor of at least 7.5 and a cooling seasonal energy efficiency ratio of at least 13.5;
(4) central air conditioners that have a cooling seasonal energy efficiency ratio of at least 13.5; and
(5) advanced natural gas water heaters that have an energy factor of at least 0.65.

Motor Vehicle Sales and Use Tax Rate Reduction

This bill would reduce the motor vehicle sales and use tax from three percent to one and a half percent for all vehicles that are manufactured, converted, or retrofitted to use clean special fuels as a source of propulsion.

"Clean special fuels" are defined as all products or energy sources used to propel a highway vehicle which, when compared to conventional gasoline or reformulated gasoline, will result in lower emissions of oxides of nitrogen, volatile organic compounds, carbon monoxide or particulates or any combination thereof, and includes compressed natural gas, liquified natural gas, liquified petroleum gas, hydrogen, hythane (a combination of compressed natural gas and hydrogen) and electricity. A hybrid gasoline/electric powered motor vehicle is deemed to use clean special fuels under this bill.

For motor vehicles converted or retrofitted to use clean special fuels, the owner would be entitled to a refund of one-half of the motor vehicle sales and use tax paid at the time of titling.

Department of Motor Vehicles Amendments

DMV has suggested that this bill be amended. Except for the hybrid vehicle provisions, the reduction proposed by this bill was in statute from January 1, 1996 through December 31, 1999. Although this bill essentially puts back in place this same motor vehicle sales and use tax reduction, DMV believes this proposal sets an undesirable precedent because it does not place a sunset on the reduction like the previous legislation.

Despite the relatively minimal fiscal impacts, DMV believes the sales of these vehicles should be monitored to ensure no major revenue impacts develop in the future. In order to assist in this monitoring process, DMV suggests that the motor vehicle sales and use tax reduction proposed by this bill have a limited effective period of up to four years, which is the same as the initial reduction put into effect from January 1, 1996 through December 31, 1999.

Also, the clean special fuels definition referred to in § 58.1-2101 expired as of January 1, 2001. DMV recommends changing all references to § 58.1-2101 to § 46.2-749.3 instead.

cc: Secretary of Finance

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