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HOUSE BILL NO. 1250

Offered January 11, 2006

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A BILL to amend and reenact §§ 58.1-320, 58.1-321, and 58.1-322 of the Code of Virginia, relating to income tax; indexing to inflation the income brackets for rates, filing thresholds, personal exemptions, and standard deduction.

 Patron—Hugo

Referred to Committee on Finance

Be it enacted by the General Assembly of Virginia:

1. That §§ 58.1-320, 58.1-321, and 58.1-322 of the Code of Virginia are amended and reenacted as follows:

§ 58.1-320. Imposition of tax.

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

Two percent on income not exceeding \$3,000;

Three percent on income in excess of \$3,000, but not in excess of \$5,000;

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 percent on income in excess of \$5,000 but not in excess of \$17,000 for taxable years beginning January 1, 1990;

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 percent on income in excess of \$17,000 for taxable years beginning on and after January 1, 1990.

B. For taxable years beginning on and after January 1, 2007, all amounts of income in this section shall be indexed annually by an amount equal to the percentage change in the Consumer Price Index for All Urban Consumers (CPI-U), for all items, from October 1 through September 30 for the year immediately preceding the affected taxable year.

§ 58.1-321. Exemptions and exclusions.

A. No tax levied pursuant to § 58.1-320 is imposed, nor any return required to be filed by:

1. A single individual where the Virginia adjusted gross income for such taxable year is less than \$5,000 for taxable years beginning on and after January 1, 1987, but before January 1, 2004.

A single individual where the Virginia adjusted gross income plus the modification specified in subdivision D 5 of § 58.1-322 for such taxable year is less than \$5,000 for taxable years beginning on and after January 1, 2004, but before January 1, 2005.

A single individual where the Virginia adjusted gross income plus the modification specified in subdivision D 5 of § 58.1-322 for such taxable year is less than \$7,000 for taxable years beginning on and after January 1, 2005.

2. An individual and spouse if their combined Virginia adjusted gross income for such taxable year is less than \$8,000 for taxable years beginning on and after January 1, 1987, (or one-half of such amount in the case of a married individual filing a separate return) but before January 1, 2004.

An individual and spouse if their combined Virginia adjusted gross income plus the modification specified in subdivision D 5 of § 58.1-322 is less than \$8,000 for taxable years beginning on and after January 1, 2004, (or one-half of such amount in the case of a married individual filing a separate return)

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59 but before January 1, 2005; and less than \$14,000 for taxable years beginning on and after January 1,
60 2005 (or one-half of such amount in the case of a married individual filing a separate return).

61 For the purposes of this section "Virginia adjusted gross income" means federal adjusted gross
62 income for the taxable years with the modifications specified in § 58.1-322 B, § 58.1-322 C and the
63 additional deductions allowed under § 58.1-322 D 2 b and D 5 for taxable years beginning before
64 January 1, 2004. For taxable years beginning on and after January 1, 2004, Virginia adjusted gross
65 income means federal adjusted gross income with the modifications specified in subsections B and C of
66 § 58.1-322.

67 *For taxable years beginning on and after January 1, 2007, the income amounts in this section shall*
68 *be indexed annually by an amount equal to the percentage change in the Consumer Price Index for All*
69 *Urban Consumers (CPI-U), for all items, from October 1 through September 30 for the year*
70 *immediately preceding the affected taxable year.*

71 B. Persons in the armed forces of the United States stationed on military or naval reservations within
72 Virginia who are not domiciled in Virginia shall not be held liable to income taxation for compensation
73 received from military or naval service.

74 § 58.1-322. Virginia taxable income of residents.

75 A. The Virginia taxable income of a resident individual means his federal adjusted gross income for
76 the taxable year, which excludes combat pay for certain members of the Armed Forces of the United
77 States as provided in § 112 of the Internal Revenue Code, as amended, and with the modifications
78 specified in this section.

79 B. To the extent excluded from federal adjusted gross income, there shall be added:

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

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

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

88 4. The amount of a lump sum distribution from a qualified retirement plan, less the minimum
89 distribution allowance and any amount excludable for federal income tax purposes that is excluded from
90 federal adjusted gross income solely by virtue of an individual's election to use the averaging provisions
91 under § 402 of the Internal Revenue Code; and

92 5. through 8. [Repealed.]

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

95 C. To the extent included in federal adjusted gross income, there shall be subtracted:

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

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

103 3. [Repealed.]

104 4. Benefits received under Title II of the Social Security Act and other benefits subject to federal
105 income taxation solely pursuant to § 86 of the Internal Revenue Code.

106 4a. Through December 31, 2000, the same amount used in computing the federal credit allowed
107 under § 22 of the Internal Revenue Code by a retiree under age 65 who qualified for such retirement on
108 the basis of permanent and total disability and who is a qualified individual as defined in § 22 (b) (2) of
109 the Internal Revenue Code; however, any person who claims a deduction under subdivision 5 of
110 subsection D of this section may not also claim a subtraction under this subdivision.

111 4b. For taxable years beginning on or after January 1, 2001, up to \$20,000 of disability income, as
112 defined in § 22 (c) (2) (B) (iii) of the Internal Revenue Code; however, any person who claims a
113 deduction under subdivision 5 of subsection D of this section may not also claim a subtraction under
114 this subdivision.

115 5. The amount of any refund or credit for overpayment of income taxes imposed by the
116 Commonwealth or any other taxing jurisdiction.

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

119 7, 8. [Repealed.]

120 9. [Expired.]

10. Any amount included therein less than \$600 from a prize awarded by the State Lottery Department.

11. The wages or salaries received by any person for active and inactive service in the National Guard of the Commonwealth of Virginia, not to exceed the amount of income derived from 39 calendar days of such service or \$3,000, whichever amount is less; however, only those persons in the ranks of O3 and below shall be entitled to the deductions specified herein.

12. Amounts received by an individual, not to exceed \$1,000 in any taxable year, as a reward for information provided to a law-enforcement official or agency, or to a nonprofit corporation created exclusively to assist such law-enforcement official or agency, in the apprehension and conviction of perpetrators of crimes. This provision shall not apply to the following: an individual who is an employee of, or under contract with, a law-enforcement agency, a victim or the perpetrator of the crime for which the reward was paid, or any person who is compensated for the investigation of crimes or accidents.

13. [Repealed.]

14. [Expired.]

15, 16. [Repealed.]

17. For taxable years beginning on and after January 1, 1995, the amount of "qualified research expenses" or "basic research expenses" eligible for deduction for federal purposes, but which were not deducted, on account of the provisions of § 280C (c) of the Internal Revenue Code and which shall be available to partners, shareholders of S corporations, and members of limited liability companies to the extent and in the same manner as other deductions may pass through to such partners, shareholders, and members.

18. For taxable years beginning on or after January 1, 1995, all military pay and allowances, not otherwise subtracted under this subsection, earned for any month during any part of which such member performed military service in any part of the former Yugoslavia, including the air space above such location or any waters subject to related naval operations, in support of Operation JOINT ENDEAVOR as part of the NATO Peace Keeping Force. Such subtraction shall be available until the taxpayer completes such service.

19. For taxable years beginning on and after January 1, 1996, any income received during the taxable year derived from a qualified pension, profit-sharing, or stock bonus plan as described by § 401 of the Internal Revenue Code, an individual retirement account or annuity established under § 408 of the Internal Revenue Code, a deferred compensation plan as defined by § 457 of the Internal Revenue Code, or any federal government retirement program, the contributions to which were deductible from the taxpayer's federal adjusted gross income, but only to the extent the contributions to such plan or program were subject to taxation under the income tax in another state.

20. For taxable years beginning on and after January 1, 1997, any income attributable to a distribution of benefits or a refund from a prepaid tuition contract or savings trust account with the Virginia College Savings Plan, created pursuant to Chapter 4.9 (§ 23-38.75 et seq.) of Title 23. The subtraction for any income attributable to a refund shall be limited to income attributable to a refund in the event of a beneficiary's death, disability, or receipt of a scholarship.

21. For taxable years beginning on or after January 1, 1998, all military pay and allowances, to the extent included in federal adjusted gross income and not otherwise subtracted, deducted or exempted under this section, earned by military personnel while serving by order of the President of the United States with the consent of Congress in a combat zone or qualified hazardous duty area which is treated as a combat zone for federal tax purposes pursuant to § 112 of the Internal Revenue Code.

22. For taxable years beginning on or after January 1, 2000, 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.

23. Effective for all taxable years beginning on or after January 1, 2000, \$15,000 of military basic pay for military service personnel on extended active duty for periods in excess of 90 days; however, the subtraction amount shall be reduced dollar-for-dollar by the amount which the taxpayer's military basic pay exceeds \$15,000 and shall be reduced to zero if such military basic pay amount is equal to or exceeds \$30,000.

24. Effective for all taxable years beginning on and after January 1, 2000, the first \$15,000 of salary for each federal and state employee whose total annual salary from all employment for the taxable year is \$15,000 or less.

25. Unemployment benefits taxable pursuant to § 85 of the Internal Revenue Code.

26. For taxable years beginning on and after January 1, 2001, any amount received as military retirement income by an individual awarded the Congressional Medal of Honor.

182 27. Effective for all taxable years beginning on and after January 1, 1999, income received as a
183 result of (i) the "Master Settlement Agreement," as defined in § 3.1-1106; (ii) the National Tobacco
184 Grower Settlement Trust dated July 19, 1999; and (iii) the Tobacco Loss Assistance Program, pursuant
185 to 7 C.F.R. Part 1464 (Subpart C, §§ 1464.201 through 1464.205), by (a) tobacco farmers; (b) any
186 person holding a tobacco marketing quota, or tobacco farm acreage allotment, under the Agricultural
187 Adjustment Act of 1938; or (c) any person having the right to grow tobacco pursuant to such a quota or
188 allotment, but only to the extent that such income has not been subtracted pursuant to subdivision C 18
189 of § 58.1-402.

190 28. For taxable years beginning on and after January 1, 2000, items of income attributable to,
191 derived from or in any way related to (i) assets stolen from, hidden from or otherwise lost by an
192 individual who was a victim or target of Nazi persecution or (ii) damages, reparations, or other
193 consideration received by a victim or target of Nazi persecution to compensate such individual for
194 performing labor against his will under the threat of death, during World War II and its prelude and
195 direct aftermath. This subtraction shall not apply to assets acquired with such items of income or with
196 the proceeds from the sale of assets stolen from, hidden from or otherwise lost to, during World War II
197 and its prelude and direct aftermath, a victim or target of Nazi persecution. The provisions of this
198 subdivision shall only apply to an individual who was the first recipient of such items of income and
199 who was a victim or target of Nazi persecution, or a spouse, widow, widower, or child or stepchild of
200 such victim.

201 "Victim or target of Nazi persecution" means any individual persecuted or targeted for persecution by
202 the Nazi regime who had assets stolen from, hidden from or otherwise lost as a result of any act or
203 omission in any way relating to (i) the Holocaust; (ii) World War II and its prelude and direct
204 aftermath; (iii) transactions with or actions of the Nazi regime; (iv) treatment of refugees fleeing Nazi
205 persecution; or (v) the holding of such assets by entities or persons in the Swiss Confederation during
206 World War II and its prelude and aftermath. A victim or target of Nazi persecution shall also include
207 any individual forced into labor against his will, under the threat of death, during World War II and its
208 prelude and direct aftermath. As used in this subdivision, "Nazi regime" means the country of Nazi
209 Germany, areas occupied by Nazi Germany, those European countries allied with Nazi Germany, or any
210 other neutral European country or area in Europe under the influence or threat of Nazi invasion.

211 29. For taxable years beginning on and after January 1, 2002, any gain recognized as a result of the
212 Peanut Quota Buyout Program of the Farm Security and Rural Investment Act of 2002 pursuant to 7
213 C.F.R. Part 1412 (Subpart H, §§ 1412.801 through 1412.811) as follows:

214 a. If the payment is received in installment payments pursuant to 7 C.F.R. § 1412.807(a) (2), then the
215 entire gain recognized may be subtracted.

216 b. If the payment is received in a single payment pursuant to 7 C.F.R. § 1412.807(a) (3), then 20
217 percent of the recognized gain may be subtracted. The taxpayer may then deduct an equal amount in
218 each of the four succeeding taxable years.

219 30. Effective for all taxable years beginning on and after January 1, 2002, but before January 1,
220 2005, the indemnification payments received by contract poultry growers and table egg producers from
221 the U.S. Department of Agriculture as a result of the depopulation of poultry flocks because of low
222 pathogenic avian influenza in 2002. In no event shall indemnification payments made to owners of
223 poultry who contract with poultry growers qualify for this subtraction.

224 31. Effective for all taxable years beginning on or after January 1, 2001, the military death gratuity
225 payment made after September 11, 2001, to the survivor of deceased military personnel killed in the line
226 of duty, pursuant to Chapter 75 of Title 10 of the United States Code; however, the subtraction amount
227 shall be reduced dollar-for-dollar by the amount that the survivor may exclude from his federal gross
228 income in accordance with § 134 of the Internal Revenue Code.

229 D. In computing Virginia taxable income there shall be deducted from Virginia adjusted gross
230 income as defined in § 58.1-321:

231 1. a. The amount allowable for itemized deductions for federal income tax purposes where the
232 taxpayer has elected for the taxable year to itemize deductions on his federal return, but reduced by the
233 amount of income taxes imposed by the Commonwealth or any other taxing jurisdiction and deducted
234 on such federal return and increased by an amount which, when added to the amount deducted under
235 § 170 of the Internal Revenue Code for mileage, results in a mileage deduction at the state level for
236 such purposes at a rate of 18 cents per mile; or

237 b. Three thousand dollars for single individuals for taxable years beginning on and after January 1,
238 1989; \$5,000 for married persons (one-half of such amounts in the case of a married individual filing a
239 separate return) for taxable years beginning on and after January 1, 1989, but before January 1, 2005;
240 and \$6,000 for married persons (one-half of such amounts in the case of a married individual filing a
241 separate return) for taxable years beginning on and after January 1, 2005; provided that the taxpayer has
242 not itemized deductions for the taxable year on his federal income tax return. For purposes of this
243 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.

For taxable years beginning on and after January 1, 2007, the \$3,000 and \$6,000 deduction amounts in this subdivision shall be indexed annually by an amount equal to the percentage change in the Consumer Price Index for All Urban Consumers (CPI-U), for all items, from October 1 through September 30 for the year immediately preceding the affected taxable year.

2. a. A deduction in the amount of \$800 for taxable years beginning on and after January 1, 1988, but before January 1, 2005, and \$900 for taxable years beginning on and after January 1, 2005, for each personal exemption allowable to the taxpayer for federal income tax purposes.

b. For taxable years beginning on and after January 1, 1987, 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.

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.

For taxable years beginning on and after January 1, 2007, the \$800 and \$900 deduction amounts in this subdivision shall be indexed annually by an amount equal to the percentage change in the Consumer Price Index for All Urban Consumers (CPI-U), for all items, from October 1 through September 30 for the year immediately preceding the affected taxable year.

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 the taxpayer can also claim the child as a personal exemption under § 151 of the Internal Revenue Code.

5. a. Effective for all taxable years beginning on or after January 1, 1996, but before January 1, 2004, a deduction in the amount of \$12,000 for taxpayers age 65 or older, or \$6,000 for taxpayers age 62 through 64.

b. For taxable years beginning on and after January 1, 2004, a deduction in the amount of \$12,000 for individuals born on or before January 1, 1939.

c. For taxable years beginning January 1, 2004, but before January 1, 2005, a deduction in the amount of \$6,000 for individuals born on or between January 2, 1940, and January 1, 1942.

d. For taxable years beginning January 1, 2005, but before January 1, 2006, a deduction in the amount of \$6,000 for individuals born on or between January 2, 1941, and January 1, 1942.

e. For taxable years beginning on and after January 1, 2004, 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 will be reduced by \$1 for every \$1 the total combined adjusted federal adjusted gross income of both spouses exceeds \$75,000.

f. 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. For taxable years beginning on and after January 1, 1997, 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 savings trust account entered into with the Virginia College Savings Plan, pursuant to Chapter 4.9 (§ 23-38.75 et seq.) of Title 23. Except as provided in subdivision 7 c, the amount deducted on any individual income tax return in any taxable year shall be limited to \$2,000 per prepaid tuition contract or savings trust account. No deduction shall be allowed pursuant to this section 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 savings trust account exceeds \$2,000, the remainder may be carried forward and subtracted in future taxable years until the purchase price or savings trust contribution has been fully deducted; however, except as provided in subdivision 7 c, in no event shall the amount deducted in any taxable year exceed \$2,000 per contract or 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

305 receipt of a scholarship. For the purposes of this subdivision, the term "purchaser" or "contributor"
306 means the person shown as such on the records of the Virginia College Savings Plan as of December 31
307 of the taxable year. In the case of a transfer of ownership of a prepaid tuition contract or savings trust
308 account, the transferee shall succeed to the transferor's tax attributes associated with a prepaid tuition
309 contract or savings trust account, including, but not limited to, carryover and recapture of deductions.

310 b. The amount paid for a prepaid tuition contract during taxable years beginning on or after January
311 1, 1996, but before January 1, 1998, shall be deducted in taxable years beginning on or after January 1,
312 1998, and shall be subject to the limitations set out in subdivision 7 a.

313 c. A purchaser of a prepaid tuition contract or contributor to a savings trust account who has attained
314 age 70 shall not be subject to the limitation that the amount of the deduction not exceed \$2,000 per
315 prepaid tuition contract or savings trust account in any taxable year. Such taxpayer shall be allowed a
316 deduction for the full amount paid for the contract or contributed to a savings trust account, less any
317 amounts previously deducted. If a prepaid tuition contract was purchased by such taxpayer during
318 taxable years beginning on or after January 1, 1996, but before January 1, 1998, such taxpayer may take
319 the deduction for the full amount paid during such years, less any amounts previously deducted with
320 respect to such payments, in taxable year 1999 or by filing an amended return for taxable year 1998.

321 8. For taxable years beginning on and after January 1, 2000, the total amount an individual actually
322 contributed in funds to the Virginia Public School Construction Grants Program and Fund, established in
323 Chapter 11.1 (§ 22.1-175.1 et seq.) of Title 22.1, provided the individual has not claimed a deduction for
324 such amount on his federal income tax return.

325 9. For taxable years beginning on and after January 1, 1999, an amount equal to 20 percent of the
326 tuition costs incurred by an individual employed as a primary or secondary school teacher licensed
327 pursuant to Chapter 15 (§ 22.1-289.1 et seq.) of Title 22.1 to attend continuing teacher education courses
328 that are required as a condition of employment; however, the deduction provided by this subsection shall
329 be available only if (i) the individual is not reimbursed for such tuition costs and (ii) the individual has
330 not claimed a deduction for the payment of such tuition costs on his federal income tax return.

331 10. For taxable years beginning on and after January 1, 2000, the amount an individual pays
332 annually in premiums for long-term health care insurance, provided the individual has not claimed a
333 deduction for federal income tax purposes.

334 E. There shall be added to or subtracted from federal adjusted gross income, as the case may be, the
335 individual's share, as beneficiary of an estate or trust, of the Virginia fiduciary adjustment determined
336 under § 58.1-361.

337 F. There shall be added or subtracted, as the case may be, the amounts provided in § 58.1-315 as
338 transitional modifications.