

# DEPARTMENT OF TAXATION

## 2011 Fiscal Impact Statement

1. **Patron** Christopher K. Peace

3. **Committee** House Finance

4. **Title** Machinery and Tools Tax; Local Defense  
Manufacturing Zones

2. **Bill Number** HB 1822

**House of Origin:**

  X   **Introduced**

       **Substitute**

       **Engrossed**

**Second House:**

       **In Committee**

       **Substitute**

       **Enrolled**

### 5. **Summary/Purpose:**

This bill would create a separate class of property for purposes of the Machinery and Tools Tax for machinery and tools designed and used directly in manufacturing materials and equipment for national defense. Localities would be authorized to levy a tax on this separate class of property at a different rate from that levied on other machinery and tools, but which would not exceed the rate for the general class of machinery and tools.

Additionally, this bill would authorize local governing bodies to create, by ordinance, one or more defense production zones, inside which localities would be permitted to grant tax incentives and provide certain regulatory flexibility for a maximum period of twenty years. The bill would also authorize the adoption of a development taxation program for the defense production zone, regardless of whether the zone has been designated by the Governor as an enterprise zone, and would make the laws that apply to enterprise zones also applicable to defense production zones.

The effective date of this bill is not specified.

6. **Budget amendment necessary:** No.

7. **Fiscal Impact Estimates are:** Not available. (See Line 8.)

### 8. **Fiscal implications:**

This bill would have no impact on state revenues. This bill may initially result in a local revenue decrease for those localities that elect to enact defense production zone programs, to the extent that such programs grant tax incentives or reduce fees imposed by that locality. The bill would also decrease local revenues to the extent that localities exercise the option to levy the Machinery and Tools Tax at a lower rate than that levied on other machinery and tools.

### 9. **Specific agency or political subdivisions affected:**

All localities

**10. Technical amendment necessary: No.**

**11. Other comments:**

Machinery and Tools Tax

Generally, machinery and tools used in manufacturing, mining, water well drilling, processing or reprocessing, radio and television broadcasting, dairy, dry cleaning or a laundry business are segregated as a separate class of tangible personal property and are subject to local taxation only. The tax rate imposed on machinery and tools may not exceed that imposed on the general class of tangible personal property.

As established in a 1950 opinion of the Tax Commissioner, machinery and tools used in the manufacturing business are those machinery and tools (1) actually and directly used in manufacturing processes and (2) those machinery and tools used in the manufacturing business that are necessary in the particular manufacturing business and are used in connection with operation of machinery that is actually and directly used in manufacturing processes.

Machinery and Tools Tax Proposal

This bill would create a separate class of property for purposes of the Machinery and Tools Tax for machinery and tools, including repair and replacement parts, designed and used directly in manufacturing or processing materials, components, or equipment for national defense. Localities would, therefore, be authorized to levy a tax on this separate class of property at a different rate from that levied on other machinery and tools. The rate could not exceed that applicable to the general class of machinery and tools.

Virginia Enterprise Zone Program

The Virginia Enterprise Zone Program was created in 1982 to form a partnership between state and local governments to stimulate job creation, private investment, and revitalization of distressed Virginia localities. The act focused on state and local tax credits to assist areas designated as enterprise zones. Cities and counties that applied for, and were granted the designation, were able to receive tax credits for businesses situated in the zones.

In 2005, the General Assembly passed legislation (House Bill 2570, Chapter 884 and Senate Bill 983, Chapter 863, 2005 Acts) to phase out the existing system for enterprise zone tax credits and replaced it with t125

he Enterprise Zone Grant Program. The Enterprise Zone Act expired on July 1, 2005; however, all enterprise zones that were in effect as of July 1, 2005 would continue until the end of their 20 year designation period. Under the Enterprise Zone Grant Program, localities are able to apply for grants from the Department of Housing and Community Development and are allowed to offer a variety of tax incentives when applying for an enterprise zone designation.

Localities applying for enterprise zone designation are required to submit local incentives to stimulate real property improvements and the creation of new jobs. These incentives include, but are not limited to i) reduction in permit fees for businesses, ii) reduction in user fees, iii) reduction in BPOL license tax, iv) partial exemption of real property taxes for rehabilitative or refurbishing real property within the Enterprise Zone, and v) adoption of local enterprise development tax programs.

#### Local Enterprise Zone Development Taxation Program

A local enterprise zone development taxation program allows a specified percentage of real estate and machinery and tools tax revenue resulting from the incremental increase in the assessed value of real estate and machinery and tools located within an enterprise zone to be allocated to the Local Enterprise Zone Development Fund. This fund is used for grants aimed at attracting businesses to an enterprise zone or enhancing governmental services within an enterprise zone. Localities are currently authorized to adopt a local enterprise zone development taxation program for a locally designated technology zone, regardless of whether the technology zone has been designated as an enterprise zone.

#### Local Defense Production Zones Proposal

This bill would authorize local governing bodies to create, by ordinance, one or more defense production zones, inside which, localities would be permitted to grant tax incentives and provide certain regulatory flexibility. A “defense production business” would be defined as a business engaged in the design, development, or production of materials, components, or equipment required to meet the needs of national defense. Additionally, localities would be authorized to include under this definition any business that performs functions ancillary to or in support of the design, development, or production of such materials, components, or equipment.

The incentives permissible under this bill would include, but not be limited to reduction of permit fees, reduction of user fees, and reduction of any type of gross receipts tax. Localities would be authorized to provide such incentives for a maximum period of twenty years. Under the terms of this bill, local governing bodies would also be authorized to enter into agreements for the payment of economic development incentive grants to defense production businesses located in defense production zones, with payment of the grants conditioned upon the business making certain real property or capital investments, creating and maintaining new jobs, or performing or meeting other economic development objectives. The extent and duration of the incentive proposals would need to conform to the requirements of the Constitutions of Virginia and the United States.

In addition, localities would be authorized to offer regulatory flexibility in such zones, including, but not limited to special zoning for the district, permit process reform, exemption from ordinances, and any other incentive adopted by ordinance. Under the terms of the bill, localities could offer these regulatory incentives for a maximum period of twenty years.

The bill would also authorize the adoption of a local enterprise zone taxation program for the defense production zone, regardless of whether the defense production zone has

been designated by the Governor as an enterprise zone, and would make the laws that apply to enterprise zones also applicable to defense production zones. Under the terms of the bill, the establishment of a defense production zone would not preclude the area from also being designated as an enterprise zone or technology zone.

The effective date of this bill is not specified.

#### Similar Bills

**Senate Bill 999** is identical to this bill.

**House Bill 2215** and **Senate Bill 970** (identical) would authorize local governments to establish local defense production zones in which tax incentives and regulatory flexibility are provided for a maximum period of ten years. These bills would also authorize the locality to adopt a local enterprise zone development taxation program for the defense production zone.

**Senate Bill 969** would authorize local governments to establish local defense production zones in which tax incentives and regulatory flexibility are provided for a maximum period of ten years.

cc : Secretary of Finance

Date: 1/20/2011 KP  
DLAS File Name: HB1822F161.doc