

DEPARTMENT OF TAXATION

2012 Fiscal Impact Statement

1. **Patron** Harry R. Purkey

3. **Committee** House Finance

4. **Title** Machinery and Tools; Intangible Personal Property

2. **Bill Number** HB 512

House of Origin:

 X **Introduced**

 Substitute

 Engrossed

Second House:

 In Committee

 Substitute

 Enrolled

5. Summary/Purpose:

This bill would reclassify as intangible personal property and exempt from state and local taxation, i) machinery and equipment used by farm wineries; and ii) machinery and tools that have not been in service for more than three years. The new classification would apply only to machinery and tools purchased on or after July 1, 2012.

Under current law, idle machinery and tools are classified as intangible personal property and exempt from state and local taxation. Machinery and equipment used by farm wineries are excluded from the machinery and tools tax but are a separate classification for local tangible personal property tax purposes. Localities are authorized, by ordinance, to exempt or provide a different rate of tax for such classification.

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. As this bill would exempt certain machinery and tools from local taxation, this bill would have an unknown negative impact on local revenues. According to the Auditor of Public Account's Comparative Report of Local Government Revenues and Expenditures, local revenues from the machinery and tools tax totaled \$200.3 million in Fiscal Year 2008, \$214.0 million in Fiscal Year 2009, and \$221.2 million in Fiscal Year 2010.

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.

Intangible Personal Property

Under current law, intangible personal property is a separate class of property segregated for taxation by the Commonwealth. Localities are prohibited from taxing intangible personal property.

Certain personal property, while tangible in fact, has been designated as intangible and has been exempted from state and local taxation. For example, tangible personal property used in manufacturing, mining, water well drilling, radio or television broadcasting, dairy, dry cleaning or laundry businesses has been designated as exempt intangible personal property.

In the case of a manufacturing business, all personal property except machinery and tools, motor vehicles and delivery equipment used in the manufacturing business are considered to be intangible personal property. The 1950 opinion of the Tax Commissioner also established the Department's longstanding policy that idled machinery and tools are generally considered intangible personal property because they are not used in the manufacturing business. The opinion stated that in order to be considered "idle," machinery and tools must be in "prolonged and indefinite" disuse, not seasonal or occasional disuse, such that the machinery and tools are stored or storage of the machinery and tools would be proper if it were practicable to place the machinery and tools into storage. The opinion stated that, as a general rule, machinery and tools may be considered idle if they have been discontinued in use for as long a period as one year prior to the date they are returnable for taxation, provided there is no reasonable prospect that they will return to an active state within at least one year after such date.

House Bill 2181 and Senate Bill 1151 (2007)

House Bill 2181 and Senate Bill 1151 (*Acts of Assembly 2007*, Chapters 191 and 159) provided for the uniform statewide classification and taxation of idle machinery and tools on a prospective basis, effective January 1, 2007. The law codified the Department's administrative rulings holding that idle machinery and tools are to be classified as

intangible personal property not subject to local taxation. The law also codified the Department's administrative rulings that machinery and tools are to be considered idled if they (1) have been discontinued in use continuously for at least one continuous year prior to any tax day, (2) are not in use on the tax day and (3) no reasonable prospect exists that such machinery and tools will be returned to use during the tax year.

The law also provided an alternate rule for determining that machinery and tools are to be considered idle. The alternate rule requires that on and after January 1, 2007, the machinery and tools (1) be specifically identified in writing by the taxpayer to the commissioner of the revenue or other assessing official on or before April 1 of the current tax year as machinery and tools that will be withdrawn from service before tax day of the next tax year, (2) are not in use on the tax day, and (3) have no reasonable prospect of being returned to use during the next tax year.

Proposal

This bill would reclassify as intangible personal property and exempt from state and local taxation, i) machinery and equipment used by farm wineries; and ii) machinery and tools that have not been in service for more than three years. The new classification would apply only to machinery and tools purchased on or after July 1, 2012.

The effective date of this bill is not specified.

Similar Legislation

Senate Bill 549 is identical to this bill.

House Bill 298 would create a separate class of property for purposes of the Machinery and Tools Tax for machinery and tools used directly in cleaning motor vehicles by a motor vehicle cleaning business.

House Joint Resolution 4 would direct the Department of Taxation to conduct a study of the BPOL tax with the input of business, industry, and local government representatives in order to determine whether the current business classifications and tax rates reflect today's economy.

Senate Joint Resolution 86 would direct the Department of Taxation to study the impact of a state income tax credit for local machinery and tools taxes paid by manufacturers on the Commonwealth, local governments, and manufacturers, including any anticipated increase in investments in machinery and tools.

cc : Secretary of Finance

Date: 1/21/2012 AM
DLAS File Name: HB512F161