

DEPARTMENT OF TAXATION

2020 Fiscal Impact Statement

1. **Patron** Vivian E. Watts

3. **Committee** House Finance

4. **Title** Virginia Income Tax; Indexing; Chained
Consumer Price Index for All Urban
Consumers

2. **Bill Number** HB 735

House of Origin:

 X **Introduced**

 Substitute

 Engrossed

Second House:

 In Committee

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would index Virginia's individual income tax brackets, personal exemptions, and standard deduction amounts using the Chained Consumer Price Index for All Urban Consumers ("C-CPI-U").

This bill would be effective for taxable years beginning on and after January 1, 2020.

6. **Budget amendment necessary:** Yes.

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

7b. **Revenue Impact:**

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Fund</i>
2020-21	(\$21.2 million)	GF
2021-22	(\$67.1 million)	GF
2022-23	(\$116.0 million)	GF
2023-24	(\$166.6 million)	GF
2024-25	(\$219.7 million)	GF
2025-26	(\$238.3 million)	GF

8. **Fiscal implications:**

Administrative Costs

The Department of Taxation ("the Department") considers implementation of this bill as routine, and does not require additional funding.

Revenue Impact

This bill would have an estimated negative General Fund revenue impact of \$21.2 million in Fiscal Year 2021, \$67.1 million in Fiscal Year 2022, \$116.0 million in Fiscal Year 2023, \$166.6 million in Fiscal Year 2024, \$219.7 million in Fiscal Year 2025, and \$238.3 million in Fiscal Year 2026. This bill would reduce the individual income tax liability of taxpayers

by increasing Virginia’s tax brackets and by exempting more income from taxation by increasing the standard deduction and personal exemption amounts.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Virginia Individual Income Tax Rate Brackets

Under current law, the Virginia individual income tax is imposed on the following income brackets at these rates:

Virginia Taxable Income	Virginia Tax Rates
\$3,000 and less	2 percent
\$3,001 to \$5,000	3 percent
\$5,001 to \$17,000	5 percent
\$17,001 or more	5.75 percent

In 1971, when Virginia studied conforming to the federal income tax law, Virginia originally considered having on the first three tax brackets shown above. Therefore, the top marginal tax rate would have been 5 percent, applicable to Virginia taxable income of \$5,001 or more. However, by 1972, when the General Assembly voted to conform to federal income tax law, it enacted four tax brackets at the same tax rates as under current law.

The amount of Virginia taxable income subject to Virginia’s top marginal tax rate was last modified during the 1987 Session, in response to the 1986 federal tax reform.

Year	Taxable Income Subject to 5.75 percent Tax Rate
1972—1986	\$12,001 or more
1987	\$14,001 or more
1988	\$15,001 or more
1989	\$16,001 or more
1990—Present	\$17,001 or more

Since 1990, the General Assembly has not enacted any legislation affecting Virginia individual income tax rates or brackets and the brackets are not currently indexed for inflation. The federal individual income tax rate brackets are indexed for inflation.

Federal Standard Deduction

On December 22, 2017, the Tax Cuts and Jobs Act (Public Law 115-97) was signed into law. This federal tax reform legislation substantially changes the federal income taxation of individuals and businesses. These changes include substantially increasing the federal standard deduction beginning with Taxable Year 2018 as follows:

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

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.

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 Personal Exemption

Currently, a \$930 personal exemption may be claimed for each person filing a return (for married couples, each spouse is entitled to an exemption) and for each dependent. In 1971, when Virginia studied conforming to federal income tax law, Virginia's personal exemptions were originally intended to be the same as the federal personal exemptions. However, by 1972, when Virginia voted to conform to federal income tax law, Virginia's personal exemption amount was less than the federal amount because Virginia did not conform to the 1972 federal increase. Virginia's personal exemption amounts have changed over the years, as shown below:

Year(s)	Virginia Personal Exemption
1972	\$600
1973-1986	\$600
1987	\$700
1988-2005	\$800
2006-2007	\$900
2008-present	\$930

In addition to the \$930 personal exemption, an \$800 personal exemption for age or blindness may be claimed for each filer who is blind or who has attained the age of 65 before the close of the taxable year. Virginia's additional personal exemptions for age or blindness have changed over the years, as shown below:

Year(s)	Personal Exemption for Blindness/Age
1972	\$600
1973-1986	\$600 for blindness \$1,000 for age
1987	\$900
1988-present	\$800

Beginning in Taxable Year 1973, the General Assembly allowed an additional \$400 personal exemption for taxpayers who claimed the additional federal personal exemption for age. Therefore, for Taxable Years 1973 through 1986, the total Virginia additional personal exemption for age was \$1,000. There was no additional amount allowed for blindness. Thus, taxpayers who claimed the federal personal exemption for blindness were entitled to only a \$600 additional personal exemption on Virginia returns filed from 1973 through 1986.

For Taxable Years 2018 through 2025, the TCJA effectively eliminated the federal personal exemption by making the amount of the exemption equal to \$0. However, the TCJA did not remove the statutory language in the IRC granting personal exemptions. Therefore, federal law still contains a provision allowing personal exemptions, but the amount of such exemption is \$0. Because Virginia's personal exemption deduction is based on the number of personal exemptions allowable for federal income tax purposes and not on the amount of such exemptions, the TCJA has no effect on Virginia's personal exemption.

The amounts of the Virginia personal exemption are not currently indexed for inflation. Before it was temporarily suspended, the federal personal exemption was indexed for inflation.

Federal Indexing

Effective in 1985, 1986, and all taxable years after 1989, the federal individual income tax brackets, standard deduction, and personal exemptions were all indexed using CPI-U. CPI-U is a measure calculated by the Bureau of Labor Statistics that is used to track changes in the prices paid by urban consumers for common goods and services over time. This represents approximately 87 percent of the total population of the United States. The index produces monthly data on these changes. Typically, the Index for a given month is released approximately two or three weeks after the month ends.

The TCJA requires the use of chained CPI-U, instead of CPI-U, in indexing various federal tax provisions for inflation, including the standard deduction. Chained CPI-U, like CPI-U, is a measure of the average change over time in prices paid by urban consumers, but the chained CPI-U differs from the CPI-U in that it accounts for the ability of individuals to alter their consumption patterns in response to relative price changes. Chained CPI-U reflects people's ability to lessen the impact of inflation by buying fewer goods or services that have risen in price and buying more goods and services whose price have risen less, or not at all. Therefore, chained CPI-U is a slower-growing method of calculating cost-of-living adjustments.

The change to chained CPI-U for inflation indexing is effective for taxable years beginning after 2017 and will remain in effect after 2025, because it is not subject to the same sunset provision that applies to other individual income tax provisions of the TCJA.

Proposed Legislation

Index Virginia Individual Income Tax Brackets

This bill would index the Virginia individual income tax brackets for Taxable Year 2020 and after by the percentage, if any, by which the C-CPI-U for the most recent calendar year differs from the C-CPI-U published at the close of the 12-month period ending on December 31, 2019.

Index Virginia Standard Deduction

This bill would index the Virginia standard deduction for Taxable Year 2020 through Taxable Year 2025 by the percentage, if any, by which the C-CPI-U for the most recent calendar year differs from the C-CPI-U published at the close of the 12-month period ending on December 31, 2019. This bill would provide that in no case would the amounts of the standard deduction be less than the amounts provided for Taxable Year 2019.

For Taxable Year 2026 and thereafter, the standard deduction amounts would revert to the amounts provided for taxable years beginning before January 1, 2019. These amounts are \$3,000 for single taxpayers and married taxpayers filing separately and \$6,000 for married taxpayers filing jointly. However, such amounts would be required to be indexed by the percentage, if any by which the C-CPI-U for most recent calendar year differs from the C-CPI-U published at the close of the 12-month period ending on December 31, 2019. This bill would provide that in no case would the amounts of the standard deduction be less than the amounts provided for taxable years beginning before January 1, 2019.

Index Virginia Personal Exemptions

This bill would index the personal exemptions by the percentage, if any, by which the C-CPI-U for the most recent calendar year differs from the C-CPI-U published at the close of the 12-month period ending on December 31, 2019.

This bill would be effective for taxable years beginning on and after January 1, 2020.

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.

cc : Secretary of Finance

Date: 1/23/2020 JLOF
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