DEPARTMENT OF TAXATION
2023 Fiscal Impact Statement

1. **Patron** Vivian E. Watts

2. **Bill Number** HB 2268
   House of Origin:
   X **Introduced**
   _____ **Substitute**
   _____ **Engrossed**

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

3. **Committee** House Finance

4. **Title** Individual Income Tax; Brackets, Deductions, and Exemptions

5. **Summary/Purpose:**

   This bill would make numerous changes to individual income tax brackets, deductions, and exemptions for individuals.

   For taxable years beginning on and after January 1, 2023 but before January 1, 2026, this bill would increase the standard deduction from $8,000 to $9,650 for single individuals and married taxpayers filing separately and from $16,000 to $19,300 for married persons filing jointly. This bill would also repeal language in the 2021 Appropriation Act that made a standard deduction increase contingent on meeting a revenue trigger.

   The bill would create a seven percent income tax bracket for individual taxpayers with income in excess of $600,000.

   The bill would adjust the amount of the standard deduction; personal and other individual exemption deductions; filing threshold; and income tax brackets to the annual change in 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, 2023.

6. **Budget amendment necessary:** Yes.
   Item(s): Page 1, Revenue Estimates

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

Fiscal Year	*Dollars*	*Fund*
2023-24	$139.4 million	GF
2024-25	$21.5 million	GF
2025-26	($41.8 million)	GF
2026-27	($107.4 million)	GF
2027-28	($175.9 million)	GF
2028-29	($246.8 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 result in an estimated positive General Fund revenue impact of $139.4 million in Fiscal Year 2024 and $21.5 million in Fiscal Year 2025. The bill would result in an estimated negative General Fund revenue impact of $41.8 million in Fiscal Year 2026, $107.4 million in Fiscal Year 2027, $175.9 million in Fiscal Year 2028, and $246.8 million in Fiscal Year 2029.

The table below shows the estimated positive revenue impact of the new seven percent income tax bracket, the estimated negative revenue impact of the standard deduction and indexing provisions, and the estimated net revenue impact of this bill (amounts shown in millions):

Fiscal Year	New 7% Rate	Standard Deduction and Indexing	Net Revenue Impact*
2024	$676.2	($536.8)	$139.4
2025	$477.8	($456.4)	$21.5
2026	$510.0	($551.7)	($41.8)
2027	$544.7	($652.1)	($107.4)
2028	$581.7	($757.6)	($175.9)
2029	$621.5	($868.3)	($246.8)

**Amounts may be different due to rounding.*

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

Department of Taxation

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

11. Other comments:

Virginia's Individual Income Tax

Under current law, the Virginia individual income tax is imposed at the following 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 only 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.

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 2022, the amount of the federal standard deduction, after indexing, is as follows:

- $25,900 for married taxpayers filing jointly;
- $19,400 for heads of household; and
- $12,950 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 the amounts in the law prior to passage of the Tax Cuts and Jobs Act. Additional federal 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 2022 Session, the General Assembly enacted legislation that increased the amounts of Virginia's standard deduction for Taxable Year 2022 through Taxable Year 2025. The increase for Taxable Year 2022 is contingent on annual revenue growth of at least five percent for the six-month period of July 2022 through December 2022. The increase for Taxable Year 2023 is contingent on annual revenue growth of at least five percent for the twelve-month period of July 2022 through June 2023. If the five percent growth rate is not met for either taxable year, the standard deduction for that taxable year will be $7,500 for single individuals and $15,000 for married persons.

The increased standard deduction amounts are $8,000 for single individuals and $16,000 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 in the table 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
2019-2021	$4,500	$9,000
2022-2025*	$8,000	$16,000

* *The increased standard deduction for Taxable Years 2022 and 2023 are contingent on the specific revenue growth amounts detailed above. If the revenue growth rate is not met for either taxable year, the standard deduction for that taxable year will be $7,500 for single individuals and $15,000 for married persons.*

For taxable years beginning on or after January 1, 2026, the Virginia standard deduction is scheduled to revert to its pre-2019 form ($3,000 for single filers and to $6,000 for married couples filing jointly). In addition, the amounts of the Virginia standard deduction 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 in the table 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.

Taxpayers are allowed an additional $1,000 exemption deduction for each child residing for the entire taxable year in a home under permanent foster care placement, provided that the taxpayer can also claim the child as a personal exemption under the IRC.

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.

Virginia Age Deduction

Virginia currently provides an age deduction in an amount equal to $12,000 for taxpayers who have attained age 65. During the 2004 Session, the General Assembly modified the age deduction for taxpayers born after January 1, 1939 by requiring a reduction based on income. Such individuals are required to reduce their $12,000 age deduction by $1 for every $1 of adjusted federal adjusted gross income ("FAGI") above $50,000. Married individuals are required to reduce their $12,000 age deduction by $1 for every $1 of their total combined adjusted FAGI above $75,000. For married taxpayers filing separately, the $12,000 age deduction is required to be reduced by $1 for every $1 the total combined adjusted FAGI of both spouses exceeds $75,000. "Adjusted federal adjusted gross income" is defined as federal adjusted gross income modified for any fixed date conformity adjustments and reduced by any taxable Social Security and Tier 1 Railroad Benefits.

Virginia Individual Income Tax Filing Thresholds

In 2007, legislation was enacted that modified the individual income tax filing thresholds. The threshold for single individuals was increased from $7,000 to $11,250 for 2008 and 2009, $11,650 for 2010 and 2011, and $11,950 for 2012 and beyond. The threshold for married couples was increased from $14,000 to $22,500 for 2008 and 2009, $23,300 for 2010 and 2011, and $23,900 for 2012 and beyond.

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

This bill would make numerous changes to individual income tax brackets, deductions, and exemptions for individuals.

"Indexing ratio" would be defined as the percentage, if any, by which the Chained Consumer Price Index for All Urban Consumers (C-CPI-U) as published by the U.S. Department of Labor, or any successor index, for the most recent calendar year exceeds the C-CPI-U published at the close of the 12-month period ending on December 31, 2022. If the percentage is less than zero, the indexing ratio would be zero.

Increase Standard Deduction

For taxable years beginning on and after January 1, 2023 but before January 1, 2026, this bill would increase the standard deduction from $8,000 to $9,650 for single individuals and married taxpayers filing separately, and from $16,000 to $19,300 for married persons filing jointly. This bill would also repeal language in the 2021 Appropriation Act that made a standard deduction increase contingent on meeting a revenue trigger.

Index Standard Deduction

This bill would index the Virginia standard deduction for Taxable Year 2023 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, 2022.

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, 2022.

Create a New Individual Income Tax Bracket

For taxable years beginning on and after January 1, 2023, this bill would create a seven percent income tax bracket for individual taxpayers with income in excess of $600,000.

Index Individual Income Tax Brackets

This bill would index the Virginia individual income tax brackets for Taxable Year 2023 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, 2012.

Index Individual Exemption Deductions and Filing Threshold

The bill would adjust the amount of the personal and other individual exemption deductions and the filing threshold for Taxable Year 2023 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, 2022.

This bill would be effective for taxable years beginning on and after January 1, 2023.

Similar Legislation

House Bill 2319 would decrease the top individual income tax rate from 5.75 percent to 5.5 percent and increase the standard deduction from $8,000 to $9,000 for single individuals and married taxpayers filing separately, and from $16,000 to $18,000 for married persons filing jointly.

cc : Secretary of Finance

Date: 1/31/2023 JLOF
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