

**DEPARTMENT OF TAXATION
2024 Fiscal Impact Statement**

1. **Patron** Richard H. Stuart
3. **Committee** Senate Finance and Appropriations
4. **Title** Taxation; Income, Retail Sales and Use Tax

2. **Bill Number** SB 632
House of Origin:
 Introduced
 Substitute
 Engrossed
- Second House:**
 In Committee
 Substitute
 Enrolled

5. Summary/Purpose:

This bill would decrease, beginning in Taxable Year 2025, the income tax imposed on individuals as follows:

<u>On Income between</u>	<u>Current Rate</u>	<u>Proposed Rate</u>
0 to \$3,000	2%	1.75%
\$3,000 to \$5,000	3%	2.65%
\$5,000 to \$17,000	5%	4.40%
\$17,000 or more	5.75%	5.10%

The bill would increase from 20 to 25 percent, beginning in Taxable Year 2025, the amount of Virginia Earned Income Tax Credit eligible taxpayers may claim on a nonrefundable basis. The bill would also increase the annual aggregate amount of Education Improvement Scholarships Tax Credits that are available from \$25 million to \$30 million beginning Fiscal Year 2025 and each fiscal year thereafter.

The bill would increase the rate of the Retail Sales and Use Tax from 4.3 percent to 5.2 percent and expand the application of sales tax to include digital personal property and certain taxable services in addition to tangible personal property. The bill would require that, of the portion of sales tax revenue generated by taxable services and digital personal property to be distributed to the Commonwealth Transportation Fund, one half of such revenue would be distributed to the Transportation Partnership Opportunity Fund, and the additional one half of such revenues be distributed to the Interstate 81 Corridor Improvement Fund until June 30, 2031, or until \$400 million has been deposited in the Interstate 81 Corridor Improvement Fund.

The income tax provisions would be effective for taxable years beginning on and after January 1, 2025. Certain sales tax and other provisions of the bill would have an effective date of January 1, 2025.

6. Budget amendment necessary: No.

7. No Fiscal Impact (See Line 8.)

8. Fiscal implications:

Administrative Costs

The Department of Taxation considers implementation of this bill as routine and does not require additional funding.

Revenue Impact

This bill would reduce revenues of the Commonwealth by \$256.5 million in FY 2025, \$202.3 million in FY 2026, \$181.3 million in FY 2027, \$184.5 million in FY 2028, \$223.3 million in FY 2029, and \$269.6 million in FY 2030. A detailed breakdown of the various components and their effect is included in the chart below (amounts in millions):

	FY 25	FY 26	FY 27	FY 28	FY 29	FY 30
Reduce Individual Rates - GF unrestricted	(\$1,118.9)	(\$2,339.8)	(\$2,430.1)	(\$2,552.2)	(\$2,683.3)	(\$2,822.0)
Increase EITC to 25% - GF unrestricted	\$0.0	(\$29.0)	(\$28.0)	(\$28.0)	(\$29.0)	(\$29.0)
Increase EISTC Cap - GF unrestricted	(\$5.0)	(\$5.0)	(\$5.0)	(\$5.0)	(\$5.0)	(\$5.0)
Increase RSUT Rate - GF unrestricted	\$520.1	\$1,299.3	\$1,369.7	\$1,447.3	\$1,498.0	\$1,546.0
Expand RSUT Base to Select Services	\$347.3	\$872.2	\$912.1	\$953.3	\$996.1	\$1,040.4
<i>GF Unrestricted (Excludes Transfers)</i>	\$151.4	\$380.2	\$397.6	\$415.6	\$434.2	\$453.6
<i>GF-Restricted (1% K-12 Education)</i>	\$51.9	\$130.4	\$136.4	\$142.6	\$149.0	\$155.6
<i>GF - Transfers</i>	\$19.0	\$47.6	\$49.8	\$52.0	\$54.4	\$56.8
<i>Local Option</i>	\$51.9	\$130.4	\$136.4	\$142.6	\$149.0	\$155.6
<i>Other - Regional</i>	\$26.3	\$66.1	\$69.1	\$72.2	\$75.5	\$78.8
<i>TPOF</i>	\$23.4	\$58.7	\$61.4	\$64.2	\$67.0	\$70.0
<i>ICIF</i>	\$23.4	\$58.7	\$61.4	\$64.2	\$67.0	\$70.0
Total Impact	(\$256.5)	(\$202.3)	(\$181.3)	(\$184.5)	(\$223.3)	(\$269.6)

No budget amendment is needed because the revenue impact of this bill is assumed in the Introduced Executive Budget.

9. Specific agency or political subdivisions affected:

Department of Taxation
Department of Treasury

10. Technical amendment necessary: Yes. The following amendments are necessary to ensure that all sales tax changes made by the bill become effective on January 1, 2025:

Page 16, Line 974, after 58.1-623
Delete: and

Page 16, Line 974, after 58.1-638
Insert: ,and 58.1-648.

11. Other comments:

Background

Individual Income Tax Rates

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.

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 the changes adopted during the 1987 Session adjusting the top bracket to the current income level for Taxable Year 1990 and thereafter, 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.

Virginia Low-Income Tax Credits

Virginia allows certain low-income individuals to claim either:

- The Tax Credit for Low-Income Individuals or
- The Virginia Earned Income Tax Credit ("Virginia EITC").

The Tax Credit for Low-Income Individuals is a nonrefundable individual income tax credit equal to \$300 each for the individual, the individual's spouse, and any person claimed as a dependent on such individual's or married person's income tax return for the taxable year.

The Virginia EITC generally equals 20 percent of the federal EITC. However, to the extent that a Virginia resident wishes to claim the Virginia EITC on a refundable basis, their credit is limited 15 percent of the federal EITC rather than 20 percent. Because the Virginia EITC is tied to the federal EITC, you must be eligible for the federal EITC to claim it. To qualify for the federal EITC for Taxable Year 2023, an individual's adjusted gross income and earned income must be less than:

- \$56,838 (\$63,398 for married filing jointly) if they have three or more qualifying children;
- \$52,918 (\$59,478 for married filing jointly) if they have two qualifying children;
- \$46,560 (\$53,120 for married filing jointly) if they have one qualifying child; or
- \$17,640 (\$24,210 for married filing jointly) if they do not have a qualifying child.

The maximum federal EITC for Taxable Year 2023 is:

- \$7,430 for an individual with three or more qualifying children;
- \$6,604 for an individual with two qualifying children;
- \$3,995 for an individual with one qualifying child; and
- \$600 for an individual with no qualifying children.

Education Improvement Scholarship Tax Credit

Taxpayers may claim a credit equal to 65 percent of value of monetary or marketable securities to a scholarship foundation on a list published by the Department of Education. However, the maximum amount of credits that may be awarded in any fiscal year is limited to \$25 million.

Retail Sales and Use Tax

Since the Retail Sales and Use Tax was first imposed in 1966, it has been limited to sales of tangible personal property and a few services in connection with the sale of tangible personal property. Specifically, current law provides an exemption from sales tax for the following services:

- Professional, insurance, or personal service transactions which involve sales as inconsequential elements for which no separate charges are made;
- Services rendered by repairmen for which a separate charge is made;
- Amounts separately charged for labor or services rendered in installing, applying, remodeling, or repairing property sold or rented;
- Transportation charges separately stated;
- Separately stated charges for alterations to apparel, clothing and garments;
- Charges for gift wrapping services performed by a nonprofit organization;
- Amounts separately charged for labor or services rendered in connection with the modification of prewritten programs;

- Custom programs; and
- An amount separately charged for labor rendered in connection with diagnostic work for automotive repair and emergency roadside service for motor vehicles, regardless of whether there is a sale of a repair or replacement part or a shop supply charge.

Proposed Legislation

Income Tax

Beginning with Taxable Year 2025, this bill would reduce individual income tax as follows:

<u>On Income between</u>	<u>Current Rate</u>	<u>Proposed Rate</u>
0 to \$3,000	2%	1.75%
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Retail Sales and Use Tax

This bill would increase the rate of the state Retail Sales and Use Tax from 4.3 percent to 5.2 percent. This bill would also expand the Retail Sales and Use Tax base to include (1) sales of digital personal property and (2) certain services that are not currently subject to the tax:

- Software application services
- Computer-related services
- Website hosting and design
- Data storage
- Streaming services

Business-to-business transactions involving these services would be exempt from taxation. The bill also expands the nonprofit exemption to include taxable services. Services performed by a person who does not receive more than \$2,500 per year in gross receipts for performance of such services would be exempt from the tax.

“Digital personal property” would be defined to mean digital products delivered electronically, including software, digital audio and audiovisual products, reading materials, and other data or applications, that the purchaser owns or has the ability to continually access, whether by downloading, streaming, or otherwise accessing the content, without

having to pay an additional subscription or usage fee to the seller after paying the initial purchase price.

“Streaming” would be defined to mean a method of transmitting or receiving video and audio data over a computer network as a steady, continuous flow, allowing playback to proceed while subsequent data is being received.

This bill would dedicate the revenue from the 0.9 percent state sales and use tax increase to the General Fund.

Under current law a certain percentage of the sales and use tax revenue is required to be deposited in the Commonwealth Transportation Fund. The portion of the state sales and use tax allocated to the Commonwealth Transportation Fund attributable to digital personal property and the services taxed under this bill would be deposited 50% into the Transportation Partnership Opportunity Fund and, until June 30, 2031, or until \$400 million has been deposited into the Interstate 81 Corridor Improvement Fund (“ICIF”), 50% into the ICIF.

The Department of Taxation would be authorized to develop guidelines implementing the Retail Sales and Use Tax provisions of this bill. The guidelines would be exempt from the provisions of the Administrative Process Act (§ 2.2-4000, *et seq.* of the *Code of Virginia*).

The income tax provisions would be effective for taxable years beginning on and after January 1, 2025. Certain sales tax and other provisions of the bill would have an effective date of January 1, 2025.

Similar Legislation

House Bill 1281 is identical to this bill.

House Bill 889 would expand the Retail Sales and Use Tax base to include specified services.

Senate Bill 703 would tax digital personal property and streaming services.

cc : Secretary of Finance

Date: 1/31/2024 JPJ
SB632F161