Joint Meeting: Small Business Commission and Manufacturing Development Commission

June 14, 2013
Meeting Summary

Introduction

The Small Business Commission and the Manufacturing Development Commission, convened to evaluate a restructuring plan to eliminate the business, professional and occupational license (BPOL) tax, the machinery and tools (M&T) tax and the merchants' capital tax, held its second meeting on June 14 in Virginia Beach at the Meyera E. Oberndorf Central Library.

The Commissions proceeded to receive presentations relating to follow-up issues from the first meeting of the Commissions in April, the potential impact of the machinery and tools tax on a business's decision of where to locate operations, and the status of career and technical education in Virginia.

Mark Vucci
Division of Legislative Services

Mark Vucci, Senior Attorney with the Division of Legislative Services, discussed local governments' reliance on the machinery and tools, merchants' capital, and BPOL taxes for local tax revenues in Fiscal Year 2011.

Cities - The machinery and tools tax accounts for 39.98% of the City of Covington's tax revenues; 14.11% of the City of Hopewell's tax revenues; 9.19% of the City of Petersburg's tax revenues; and 6.99% of the City of Galax's tax revenues. Fourteen other cities depend upon the machinery and tools tax for at least 2% of their tax revenues.

With the regard to the merchants' capital tax, only the City of Radford imposes the tax, and it accounts for 1.98% of the City's tax revenues.

Many cities rely heavily on the BPOL tax for local tax revenues. Martinsville (12.47%), Norton (11.5%), Danville (10.49%), and Galax (10.38%) each rely on the BPOL tax for at least 10% of their tax revenues. Every city in the Commonwealth imposes the BPOL tax with the City of Poquoson relying least on the tax for local tax revenues. The BPOL tax accounts for 2.2% of the City of Poquoson's local tax revenues.

Counties - Counties relied on the machinery and tools tax for local tax revenues as follows: Alleghany (37.33% of local tax revenues), Giles (22.93%), Greensville (16.29%), Isle of Wight (16.1%), Campbell (14.83%), Rockingham (13.05%), Henry (12.2%), Sussex (11.91%), Wythe (10.52%), and Smyth (10%). Thirty-six additional counties relied on the machinery and tools tax for at least 2% of their tax revenues.

Forty-six counties imposed the merchants' capital tax in Fiscal year 2011 with Tazewell County relying most on the tax for local tax revenues (3.08% of Tazewell County's local tax revenues).

More than half (52) of Virginia's 95 counties imposed the BPOL tax. Arlington relied on the BPOL tax for 7.34% of its local tax revenues, Prince George (6.34%), King George (6.18%), Henrico (5.82%), and York (5.48%). Twenty-one additional counties relied on the BPOL tax for at least 2% of their local tax revenues.

Towns - The machinery and tools tax accounted for 42.46% of West Point's local tax revenues, 9.8% of Berryville's, 9.59% of Strasburg's, 9.07% of Pulaski's, and 6% of Bridgewater's. Five additional towns relied on the machinery and tools tax for at least 2% of their local tax revenues.

No towns imposed a merchants' capital tax.

Warrenton relied on the BPOL tax for 25.17% of its local tax revenues followed by Farmville (24.3%), Richlands (20.9%), Herndon (18.82%), Marion (17.57%), and Rocky Mount (16.74%). Thirty additional counties relied on the BPOL tax for at least 2% of their local tax revenues.

Mr. Vucci also compared and contrasted the taxation of services by the Commonwealth with that of other states. In 2007 the Federation of Tax Administrators (FTA) published a study that identified 168 services sectors and which sectors were subject to excise taxes in the 50 states and the District of Columbia. Of the 168 services sectors, 18 were subject to an excise tax in the Commonwealth. Only Alaska (1), Colorado (14), Illinois (17), New Hampshire (11), and Oregon (0) taxed less services sectors. Massachusetts, Montana, and Nevada, like Virginia, also taxed 18 services sectors. The taxation of services sectors in Virginia is well below the national average. It is also well below the average number of services sectors taxed in neighboring and Southeastern states. More than half the states (28), including the Commonwealth, imposed excise taxes on less than one-third of the 168 services sectors identified by FTA. States on average taxed only 1 out of the 9 professional services sectors identified by FTA. Professional services sectors identified by FTA were accounting and bookkeeping, architects, attorneys, dentists, engineers, land surveying, medical test laboratories, nursing services out-of-hospital, and physicians.

Lastly, Mr. Vucci reviewed recommendations made by the Manufacturing Development Commission in 2012 pursuant to House Joint Resolution No. 735 (2011), which directed the Commission to develop a plan for repatriating manufacturing jobs and evaluating possible tax incentives. Some of the Commission's recommendations overlap with the current study being undertaken by the Manufacturing Development and Small Business Commissions. The 2012 recommendations of the Manufacturing Development Commission pursuant to House Joint Resolution No. 735 that touch upon the current study include: (i) requesting JLARC to analyze why the manufacturing sector pays a disproportionately large share of the state's corporate income tax and other taxes and to identify measures to eliminate this disparity, (ii) requesting the Department of Taxation to study the consequences and costs of permitting manufacturers to offset their local machinery and tools tax payments against certain state taxes, (iii) legislation to provide that the assessed value of machinery and tools for property taxation be limited to the depreciated value of the machinery and tools consistent with Internal Revenue Service rules, (iv) legislation to exempt new investments from the machinery and tools tax, (v) legislation to exempt manufacturers from BPOL tax liability for retail sales made at a store located at the site of the products' manufacture, and (vi) legislation to exempt combined heat and power projects for high energy users from local taxation similar to the exemptions for persons producing electricity from natural gas.

Carter Barrett
STIHL, Inc.

Carter Barrett, Manager of Financial Accounting of STIHL, Inc., provided an overview of STIHL's operations nationally, internationally, and in Virginia Beach. STIHL's production in the United States since 1974 has been approximately 50 million units. More than half of its worldwide production is attributable to its plant in Virginia Beach. Its manufacturing site in Virginia Beach covers 2.2 million square feet on 151 acres and is the home for 1,900 employees. STIHL utilizes 120 robots all of which are subject to the machinery and tools tax. Even with automation STIHL has increased its employment. The robots used by STIHL require highly skilled employees for operation.

Mr. Barrett indicated that STIHL can exercise some control over its labor costs, material costs, indirect materials supplies, overhead costs, and investments. Costs that it cannot control are federal and state income taxes, sales and use taxes, business personal property taxes, real estate taxes, and foreign exchange rates. Mr. Barrett noted that the United States corporate income tax rate is one of the highest in the world and that STIHL pays one of the highest income taxes when compared to competitors. He stated that taxes have a significant impact on the costs of production and directly impact STIHL's ability to compete for investment and that taxes are a factor in a business' decision of where to locate operations.

Mr. Barrett told the members that automation has been key in keeping STIHL competitive worldwide as it has helped level the playing field with countries with low labor rates, ensured repetitive tasks have been completed to specifications, and improved ergonomics for employees. Local machinery and tools taxes increase the costs of automation. Robots with a long useful life are subject to the tax until such time as they become obsolete.

He concluded his presentation by observing that Virginia Beach has always had a relatively low machinery and tools tax, which has enhanced STIHL's return on investment on automation. In 2012, Virginia Beach eliminated its machinery and tools tax.

Michelle Chapleau
Virginia Beach Department of Economic Development

Michelle Chapleau, Business Development Manager of the Virginia Beach Department of Economic Development, spoke with regard to the Virginia Beach machinery and tools tax. Machinery and tools were assessed at 33.3% of fair market value for purposes of the tax and then a tax rate of $1 per $100 of assessed value was imposed by the City. Approximately 200 manufacturing business paid the tax generating approximately $1.46 million annually. STIHL paid more tax on machinery and tools than any other business, accounting for approximately 40% of the annual revenues generated from the tax in Virginia Beach. Relative to other taxes imposed and collected by the City, revenues from the machinery and tools tax were small. Virginia Beach's hotel tax generates about $23 million each year and its meals tax generates about $48 million each year. Beginning in Fiscal Year 2012, Virginia Beach eliminated its machinery and tools tax to attract new companies and create jobs and to remain competitive with other communities. Ms. Chapleau stated that revenues lost from the elimination of the machinery and tools tax have been replaced by increased tax revenues from business growth and job creation. She noted that manufacturers in Virginia Beach do not pay an inventory, business equipment, or machinery and tools tax.

Since Virginia Beach eliminated its machinery and tools tax, Green Flash Brewing Co., Architectural Graphics Inc., IMS: Gear, Osen-Hunter Defense Systems, STIHL Inc., and BMZ USA, Inc. all have announced plans to invest in capital and hire new employees in Virginia Beach. The capital investment to be made by these six companies totals $95.3 million with 317 new jobs anticipated to be created. Green Flash Brewing Co. announced that it will make $20 million in capital investments and will create 41 new jobs. Green Flash Brewing Co. is scheduled to begin operations in 2015 and will become the largest craft brewer in Virginia. Architectural Graphics, Inc. announced that it will make $17.3 million in capital investments and will create 125 new jobs. Virginia Beach competed with Georgia for the Architectural Graphics, Inc. economic development project.

Delegate Michael B. Watson, House of Delegates

93rd District

Delegate Watson updated the Commission members on career and technical education in the Commonwealth. Statewide over 50,000 students are coming out of high school with some type of industrial certification. Virginia has 10 Regional Education Centers that focus on career and technical education. Career and technical education courses are driven by industry needs, and, therefore, course subject matter changes on average every 3 to 5 years. Annually, 50 to 70 career and technical education courses are updated. Currently, beginning with 8th grade and at the end of the 9th, 10th, and 11th grades, students must participate in an exercise to identify a prospective academic or career path plan. Beginning with the 2013-2014 academic year and starting with 9th grade classes, students pursuing a Standard Diploma must have some kind of career credential in order to graduate.

First-time ninth graders pursuing a Standard Diploma must earn the following number of verified credits in: English (2), Mathematics (1), Laboratory Science (1), History and Social Sciences (1), and Student Selected Test (1). For the Student Selected Test verified credit, students may utilize additional tests for earning verified credit (SOL alternative) in computer science, technology, career and technical education, economics or other areas as prescribed by the Board of Education. In addition, students who complete a career and technical education program sequence and are conferred with a certification or an occupational competency credential from a recognized industry, or trade or professional association, or who acquire a professional license in a career and technical education field from the Commonwealth may substitute the certification, competency credential, or license for (a) the Student Selected verified credit and (b) either a Science or History and Social Sciences verified credit when the certification, license, or credential confers more than one verified credit.

Delegate Watson stated that steps must be taken to eradicate any stigma associated with career and technical education. Many graduating high school students are not prepared or trained to fill high paying jobs requiring highly skilled workers, which is a deterrent to drawing manufacturing and other businesses to the Commonwealth. One possibility for removing any stigma is to rename career and technical education competency assessments to Standards of Career and Technical Education assessments. The concept is to place SOLs and competency assessments on the same playing field.

Delegate Watson concluded by stating that further steps should be undertaken to educate parents and students on career and technical education career-related opportunities.