Commission on the Revision of Virginia's State Tax Code and the Streamlined Sales Tax Project Agreement (SJR 347, 2003)
http://dls.state.va.us/sjr347TaxCode.htm

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The third meeting of the Commission on the Revision of Virginia's State Tax Code and the Streamlined Sales Tax Project Agreement met in Richmond and adopted the same format it had in August with the full commission meeting briefly, followed by the subcommittee meetings, and finally, the full commission reconvening after lunch. The full commission received presentations from education and local government representatives in its morning meeting and a report from Delegate Preston Bryant, chairman of the telecommunications tax study (HJR 651, 2003), as well as subcommittee reports during its afternoon meeting.

Morning Meeting of Full Commission

Representatives from two education organizations, the Virginia Education Association and the Virginia Education Coalition, and one local government organization, Virginia First Cities Coalition, were the first to address the full commission.

Ms. Jean Bankos, President of the Virginia Education Association, asked the commission in their deliberations to consider the shortcomings of the current tax structure to support a high quality elementary and secondary education system that serves all Virginia students. The two main issues on which she asked them to focus are (i) the burden on Virginia's local governments to fund schools and the impact it has on local property taxes, and (ii) the inadequate level of state funding for Standards of Quality. (For a copy of Ms. Bankos' complete presentation, see the Commission's website.)

Next on the commission's agenda was Ms. Connie Bawcum representing Virginia First Cities Coalition (VFC). VFC is comprised of fifteen cities throughout the Commonwealth that have been losing population and tend to be home to lower income individuals, thereby placing a greater fiscal burden on the cities that already receive less state support in general than rural and suburban areas. Its recommendations are to:

1. Modernize the tax system to reflect current economic drivers and to more equitably share the tax and service burden;
2. Establish tax rates to produce enough revenue to meet the Commonwealth's obligations to core services and invest in its furture; and
3. Expand the Commonwealth's funding for at-risk students.

The third and final speaker during the morning session of the commission was Mr. Stuart Roberson representing the Virginia Education Coalition ("Coalition"). The Coalition suggested that the commission:

1. Develop real, long-term funding sources for education;
2. Use Coalition support to achieve its goals; and

3. Heighten interest throughout the Commonwealth in education needs. According to the Coalition, the most pressing needs are in special education, technology, school construction and teacher salaries. Mr. Roberson ended his presentation by offering his and the Coalition's support to the Commission in addressing these needs.

The Commission then adjourned for the morning and the subcommittee meetings began.

Subcommittee Meetings

The BPOL Tax Subcommittee, chaired by Delegate Thelma Drake, and the Transportation Subcommittee, chaired by Delegate Leo Wardrup, were the first two subcommittees to meet. Following them in the second hour were the Personal Income and Retail Sales and Use Tax Subcommittee, chaired by Delegate Allen Louderback, and the Miscellaneous State and Local Taxes Subcommittee, chaired by Senator Emmett Hanger. During the last hour of subcommittee meetings, the Personal Income and Retail Sales and Use Tax Subcommittee continued to meet for an additional hour and the State and Local Government Services and Responsibilites Subcommittee, chaired by Senator John Chichester met.

BPOL Tax Subcommittee

The BPOL Tax Subcommittee heard presentations by representatives from local government and the business community. Both sides had been asked to focus their remarks on two questions. First, if the BPOL tax is repealed, what other revenue-generating sources can be made available to localities in order for them to replace lost BPOL revenues and on whom should such new sources be imposed (only on business or more broad-based)? Second, if the BPOL tax is not repealed, how can the law be amended to improve the tax?

The Virginia Chamber of Commerce ("Chamber") representative, Mr. Steve Haner, was first to address the subcommittee. While the Chamber favors repealing the tax, it recognizes the difficulty with finding an alternative revenue source so localities would remain whole. Therefore, it suggested changes that include reviewing all BPOL tax rate caps in light of current economic data; exempting each service category from the BPOL tax if the sales tax is extended to that service category; totally exempt the first $100,000 (possibly less in towns) earned by a business from the BPOL tax; and maintain the laws against taxing sales and services delivered to other states. (For a copy of Mr. Haner's complete presentation, see the Commission's website.)

The next speaker, also representing the business community, was Mr. George Peyton with the Retail Merchants Association of Greater Richmond ("Association"). Retailers have pushed for the elimination of the BPOL tax for some time, citing the unfairness of the rate at which they are taxed and their generally low profit margin. As a replacement revenue source, the Association suggested that Virginia take a more active role in the Streamlined Sales Tax Project and adopt the necessary legislation to participate in the collection of sales and use tax by remote sellers. In the event the BPOL tax is not repealed, the Association suggested (i) reviewing all the BPOL tax rates and eliminating all exemptions for businesses that do not pay another tax similar to the BPOL tax, and (ii) using the revenues created by eliminating the exemptions to reduce the rates paid by each business category. (For a copy of Mr. Peyton's complete presentation, see the Commission's website.)

The final set of speakers to address the BPOL Tax subcommittee and represent local government were Mr. Charles Crowson, Jr., with the Commissioners of the Revenue Association, Ms. Ellen Davenport with the Virginia Association of Counties, and Mr. Mike Edwards with the Virginia Municipal League. They began by presenting a brief history of the BPOL tax followed by a summary of BPOL tax reforms that have been enacted since 1975. In 1978, legislation passed that created the current four major categories and rate limits for the tax, as recommended by the Revenue Resources and Economic Commission. Then beginning in 1993, work began to make the BPOL tax more uniform throughout the state. A uniform ordinance was adopted by the General Assembly in 1996, with an effective date of January 1, 1997. The ordinance established a mandatory appeals process, changed the penalty and interest rules, established a March 1 due date for license applications, clarified that certain moneys received by a business should be excluded from taxable gross receipts, created a deduction for receipts from business conducted in another state or foreign country on which taxes are paid on such receipts in the other state or foreign country, and established thresholds and maximum fees for BPOL tax liability. Finally, local government revenue data was made available to the BPOL tax subcommittee in an effort to illustrate the varied role BPOL tax plays as a revenue source in each locality.

At the conclusion of the meeting, the local government representatives were asked by Delegate Drake to answer more thoroughly the two questions during the subcommittee's next meeting in November.

Personal Income and Retail Sales and Use Tax Subcommittee

Delegate Louderback, chairman of the Personal Income and Retail Sales and Use Tax Subcommittee, began the meeting by reviewing his proposal for changes to the individual income tax and the retail sales and use tax. The remainder of the meeting was a public hearing during which twenty-five speakers shared their thoughts and concerns about the proposal. Most of the speakers represented organizations, some of which were the Virginia Organizing Project, the Virginia Association of Petroleum Marketers and Convenience Stores, the Virginia AFL/CIO, the National Federation of Independent Businesses, the MidAtlantic Association of Cleaners, National Association of Social Workers, the Virginia Golf Summit, the Coalition of Virginia Nonprofits, the Virginia Agribusiness Council, the Fairfax County Taxpayers' Alliance, and the Virginia Coalition for the Homeless. (For a complete list of the speakers and organizations, see the Commission's website.)

The majority of the speakers expressed concerns about the proposal and how it would affect, in a negative way, their organizations. Some speakers praised Delegate Louderback's effort to improve the current system by creating a more equitable and simplified way of levying the individual income and sales and use taxes. Delegate Louderback concluded the two-hour meeting by thanking all those who participated and encouraging ongoing discussions about the proposal in an effort to create a plan that all Virginians can support.

Transportation Subcommittee

Delegate Wardrup, Chairman of the Transportation Subcommittee, began the second meeting of his subcommittee, by briefly summarizing the first meeting during which Barbara Reese, Chief Financial Officer of VDOT, gave an in-depth presentation on the sources of funding for transportation and how such funds are spent. As a follow-up to that meeting, the following two documents were distributed to those in attendance: (i) a one-page short synopsis entitled "State Sources of Revenue for Transportation," and (ii) a chart comparing motor fuel excise tax rates for all states.

According to the chairman, the purpose of the second meeting was to look at the transportation needs of the Commonwealth, and to explore ways of meeting those needs other than through raising taxes. Accordingly, the Honorable Whitt Clement, Secretary of Transportation, had been invited to speak on this topic.

Secretary Clement said that certain recent factors have reduced the available transportation funds including (i) "deficit reduction" payments to projects in the Six Year Program as a result of realistic revenue projections; (ii) more costly winter storms in 2003; and (iii) the financial impact of Hurricane Isabel.

Regarding the relative expense of maintenance versus construction Secretary Clement said that $407 million in construction funds had to be transferred for maintenace costs. Projecting recent trends, VDOT expects planned maintenance spending to exceed construction spending by Fiscal Year 2005.

The Secretary set forth the Commonwealth Transportation Board's policy goals addressing limited resources as follows: (i) maintain what we have, (ii) finish what we have started, (iii) seek multimodal solutions, (iv) use realistic revenue and cost estimates, (v) restore and rebuild bridges, and (vi) relieve congestion in urban areas. He also emphasized some of VDOT's initiatives to address limited resources including a uniform cost estimating system, 24 month cash flow projections, and mandatory financial plans for major projects.

Federal funding is in a precarious position, with the current funding authorization set to expire on October 1, 2003, and uncertainties surrounding the amount that the Commonwealth might receive assuming there is a reauthorization. Delegate Wardrup expressed his concern at Virginia's reliance on federal funds because (i) for every $1.00 Virginians send to the federal government in taxes only about 90.5 cents return, and (ii) of the increasing trend of the federal government attaching conditions and dictating how the money is to be spent.

The Governor's general priorities regarding federal funding include: (i) national security, (ii) no mandates, (iii) mutimodal funding, (iv) rail and transit funding, and (v) adequate and fair funding. Some of the Governor's specific priorities for federal funding include: (i) I-81, (ii) Dulles Rail, (iii) Coalfields Expressway, (iv) High Speed Rail, (v) VRE, (vi) Third Crossing, (vii) Route 460, and (viii) Transit Capital.

Regarding tolls, in general they have been eliminated or are capped in Virginia. According to the Secretary, the Commonwealth is pursuing a federal pilot program for tolls on I-81, and value pricing in Northern Virginia and Hampton Roads where the amount of tolls can rise and fall depending on demand.

Moreover, 37 proposals have been submitted to VDOT under the Public-Private Partnership Act (PPTA) with six comprehensive agreements, two in negotiation, two to be reviewed by the Advisory Panel, and two in the competition period. The Secretary emphasized that PPTA projects are desirable only when they encourage competition of ideas and prices, and ensure risk and/or cost sharing.

Other Miscellaneous State and Local Taxes Subcommittee

Senator Hanger, chairman of the subcommittee, first recapped the substance of the first subcommittee meeting. He emphasized that the subcommittee had agreed to recommend to the full Commission (i) to eliminate the accelerated sales tax collections by vendors, (ii) eliminate the estate tax, and (iii) move forward with the Streamlined Sales Tax Project.

Senator Hanger said that the first item of new business was to examine the car tax issue. His goal would be to move to 100% elimination on the personal property tax on all vehicles for personal use, with no cap on the value of such vehicles. He acknowledged that to accomplish this goal, some feasible means would have to be developed to account for the additional revenue loss to localities in excess of $400 million.

Senator Hanger stated that allocations to localities under the current car tax reimbursement formula are not based on rational public policy, and have many disparities because they are based on whatever tax rate the locality happened to have had in place on such vehicles as of July 1, 1997, or August 1, 1997, whichever is greater.

In this regard, staff presented charts,as requested by the chairman, which showed (i) the amount of reimbursement to each locality for vehicles valued at $5,000, $10,000, and $20,000; and (ii) the per capita reimbursement amount for each locality. The first group of charts (divided among cities, counties, and towns) showed, for example, that the reimbursement amount of a vehicle valued at $10,000 ranged (i) for towns from a low of $1.50 in Haysi to a high of $330 for West Point; (ii) for cities from a low of $142 in Galax to a high of $500 in Emporia; and (iii) for counties from a low of $20 in Bath to a high of $490 in Dinwiddie.

The other chart depicted the similar information but showed the amount of reimbursement on a per person basis for each city and county. This chart showed a range (i) for cities from a low of $30.19 per person in Harrisonburg to a high of $195.72 per person in Falls Church; and (ii) for counties from a low of $8.09 per person in Bath to a high of $213.68 per person in Loudoun.

Senator Colgan recounted a proposal that he had introduced in a prior General Assembly Session that would have: (i) called for a referendum to amend the Constitution of Virginia to eliminate personal property taxes on all motor vehicles and boats; and (ii) increase the sales and use tax by one and one-half percent. His proposal also replaced the current car tax relief statutes with a funding formula that would pay (i) all counties 15% of their total local tax revenue indexed to the annual percentage growth in sales and use tax revenues; (ii) all cities 11% of their total local tax revenue indexed to the annual percentage growth in sales and use tax revenues; and (iii) all towns 5% of their total local tax revenue indexed to the annual percentage growth in sales and use tax.

Next, Senator Hanger discussed the cigarette tax and staff presented one potential proposal for a statewide uniform cigarette tax as requested by Senator Hanger. This proposal would impose a 30 cents per pack state cigarette tax, and eliminate any local cigarette taxes. Such a tax would generate net additional revenue in excess of $100 million per year. Mike Edwards of the Virginia Municipal League commented that his organization would be concerned at the loss of local taxing authority, and the fairness of how the additional revenue might be distributed. Mary Ann Bergeron of the Virginia Association of Community Services Boards said that she approves of an increase in the cigarette tax with the revenue being returned to localities for health purposes.

Senator Hanger commented that he believes that in considering such a tax that thought should be given to a more regional concept of allocating revenues instead of strictly by point of sale. He also said it is not his intent to propose anything in this regard that would be punitive against the tobacco industry.

Senator Hanger and Senator Colgan then requested staff to develop alternative allocation formulas for distributing possible increased revenues from an increase in the cigarette tax.

Senator Hanger concluded the meeting by briefly introducing an issue concerning real estate taxes that he said will be addressed more fully, along with other issues, at the next meeting of the subcommittee. In particular, he said he would like to explore if there are any ways in which the State could have an increased role in taking some pressure off the local real estate taxes which have seen relatively dramatic increases as a result of increasing valuation of real estate in certain areas.

State and Local Government Services and Responsibilities Subcommittee

The State and Local Government Services and Responsibilities Subcommittee meeting began with a presentation from representatives of the Virginia Municipal League (VML) and the Virginia Association of Counties (VACo) regarding local government expenditures and sources of local revenue that are used to fund such expenditures. A representative of the Joint Legislative Audit and Review Commission (JLARC) then discussed several key service functions that are funded, managed, or delivered by the Commonwealth in concert with local governments.

VML and VACo reviewed city, county, and town expenditures for Fiscal Year 2002. For cities, education made up 49% of total expenditures, public safety made up 17% of total expenditures, and health and welfare made up 12% of total expenditures. For counties, education made up 59% of total expenditures, public safety made up 13% of total expenditures, and health and welfare made up 11% of total expenditures. For towns, public works made up 35% of total expenditures, public safety made up 31% of total expenditures, and general government made up 14% of total expenditures. In general, because counties pay for public education expenses of town residents, town expenditures for public education average about 5% of total town expenditures. VML and VACo also stated that 63% of all services provided by cities and 72% of all services provided by counties are state-mandated. The subcommittee asked VML and VACo to supply information on urban, suburban, and rural spending on education.

VML and VACo indicated that local spending exceeds the Commonwealth's Standards-of-Quality requirements by over $ 2.7 billion per year and Commonwealth spending exceeds the Standards-of-Quality requirements by over $ 492 million per year. In regard to the funding of operating and capital expenditures for education, local governments account for 56% of all such funding, the Commonwealth accounts for 31%, the state sales tax accounts for 7%, and the federal government accounts for 6%.

For Fiscal Year 2002, of all local-generated revenue (i)real estate taxes made up 46%, (ii) personal property taxes made up 10%, and (iii) user fees made up 10% (local-generated revenue did not include reimbursement payments from the Commonwealth for personal property tax relief). VML and VACo were asked by the subcommittee to update this information to include personal property tax reimbursement payments from the Commonwealth. In addition, the subcommittee asked VML and VACo to provide information on all sources of revenue received by local governments, whether or not generated at the local level.

Real estate taxes account for 49.1% of all local-generated revenues in counties, 39.1% in cities, and 21.3% in towns. Total real estate tax revenues in Fiscal Year 2002 were $ 4.5 billion while total local education spending for the fiscal year equaled $ 6 billion.

Some of the major services for which the Commonwealth and its localities have shared responsibilities include local and regional jails, law enforcement, public education, comprehensives service for youth and families, health, community services boards, social services, transportation, and courts. For all these service areas, the Commonwealth has set minimum standards that must be met, and in many cases, funding to local governments has been conditioned upon achievement of the minimum standard.

JLARC compared the services provided by local governments with the minimum standards required by the Commonwealth. Most local governments exceed the staffing standards required for local and regional jails. They also exceed the training and staffing minimum standards in place for law enforcement. Local governments exceed the Standards-of-Quality and Standards-of-Learning for public education and 55% of public schools meet adequate yearly progress (AYP). Local governments spend more than is required as a match for comprehensive services for youths and families. For health services, although primarily operated by the Commonwealth, localities have developed local health programs and supplement salaries and staffing for the provision of health services. Most local governments provide more than the core services in contracts approved by the Commonwealth for community services. In regard to social services, all local governments exceed standards for administration and programs. Generally speaking, local governments do not exceed transportation minimum standards although some local governments have spent local funds on new roads and cities exceed street maintenance standards. For court services, local governments exceed some standards for office space, staffing, and salary supplements.

JLARC also reported on the overall degree of flexibility local governments have in performing these selected services under the mandate or statute requiring the provision of the service. JLARC indicated that local governments have moderate flexibility for the performance of services relating to local and regional jails, high flexibility for law enforcement, low to moderate flexibility for public education services, moderate flexibility for comprehensive services to youths and families, low to moderate flexibility for services relating to health, moderate flexibility in regard to community services boards, low to moderate flexibility in performing social services, low to moderate flexibility for transportation, and low flexibility for courts services.

Afternoon Meeting of the Full Commission

Delegate Bryant's Report

The full Commission reconvened after lunch and first heard an update from Delegate Preston Bryant regarding the work of the Telecommunications Tax Study (HJR 651, 2003), which he serves as chairman. Delegate Bryant explained that while there still exists a number of unresolved issues, the industry and local government negotiating group is making strides in finalizing changes in the way communications and video are taxed that will make the system fairer and simpler while maintaining revenue neutrality.

According to the Progress and Freedom Foundation's Committee on State Taxation, Virginia ranked first in the nation in 2001 having the highest overall tax rate on telecommunications. Delegate Bryant explained how the telecommunications tax burden is inequitable because only three industry sectors collect such taxes (local exchange providers, wireless,and cable) while four industry sectors do not (long distance providers, paging, satellite TV and phone cards).

In its deliberations during the last year and a half, HJR 651 joint subcommittee has been working with the industry and local government toward achieving the following six goals:

1. Consolidate taxes into fewer line items on the billing statement;
2. Make taxes uniform statewide;
3. Reduce tax rate on consumers;
4. Make taxes "competitively neutral" among industry sectors;
5. Preserve state and local government revenues now and into the future; and
6. Remit tax collections to a single point of administration.

The taxes that would be repealed under the new system, which would go into effect July 1, 2005, are the local consumer utility tax, local gross receipts tax (only portion billed to consumer where applicable), current E-911 rate structure, the Virginia relay fee, and the cable franchise fee.

The simplified telecommunications tax plan would impose a statewide sales and use tax of 4.5% on communications and video services, and a 911 fee/tax not to exceed $0.75 on wireline and wireless. Tax revenues collected would be remitted to a single point of administration (either the state or a third party administrator). Localities would be kept whole based on (i) tax rates adopted no later than July 1, 2003, and (ii) revenues from such rates collected beginning July 1, 2003, and ending June 30, 2004, as determined by the Auditor of Public Accounts (APA). The sales and use tax imposed on communications and video services will be in lieu of the retail sales and use tax; however, the rate of such tax will not exceed the retail sales and use tax rate. Finally, the distribution of revenues back to the localities under this plan will be determined by the local governments and approved by the General Assembly.

The industry and local government representatives will continue to meet to work on the outstanding issues in order for a final plan to be submitted to the HJR 651 Joint Subcommittee for its approval. It is anticipated that legislation will be introduced during the 2004 General Assembly Session that will meet the goals through a simplified telecommunications tax plan.

Subcommittee Reports

Each subcommittee chairperson briefed the full commission on the discussions that occurred within their subcommittees. Senator Chichester began by talking about public education and how it is both a state and local government responsibility. The state funds approximately two-thirds of the Standards of Quality costs with the local governments relying on the real estate tax to provide the funds for their portion of the costs. Education and the court system are constitutionally based and therefore, certain requirements fall on state and local governments. Senator Chichester's subcommittee will continue to examine the distribution of responsibilities and services between state and local governments.

Delegate Drake reported that the retail merchants suggested that if the BPOL tax were repealed, replacement revenues could be raised if the General Assembly adopts legislation that contains the Streamlined Sales Tax Agreement provisions, thereby requiring remote sellers to collect the sales tax and remit it to the state. It was also suggested that if the BPOL tax were repealed, the merchant's capital tax should also be repealed. If these taxes were repealed, local governments would seek additional revenues from the state to make up the loss.

Next, Delegate Louderback informed the commission that 27 speakers participated in the public hearing addressing his personal income tax and sales and use tax proposal. Many of the speakers talked about the sales tax being imposed on services and how it would be a burden to them. Delegate Louderback reminded everyone not to lose sight of what is fair in the overall plan and that reform must be done in an orderly process.

Delegate Wardrup told the commission what a thorough presentation the Secretary of Transportation made to the Transportation Subcommittee. It is anticipated that highway maintenance will exceed the construction allowance for the first time by 2005. Federal funidng is not as generous as it once was for highways. That factor affects the state's ability to pay dramatically. There is ongoing discussion regarding the placement of tolls on certain interstate highways but it must be approved by the federal government first.

Finally, Senator Hanger reported on the various state and local taxes that his subcommittee discussed. He indicated there was support for (i) eliminating the accelerated sales tax payment in June that currently is in the state budget, (ii) repealing the estate tax, and (iii) developing a process to more actively participate in the Streamlined Sales Tax Project and Agreement. The subcommittee also talked about developing a plan for completely repealing the personal property tax on personal cars (car tax). Concern was expressed about the disparities in the current law regarding the distribution formula for the car tax.

Replacing the state and local cigarette tax with a statewide 30 cents per pack state cigarette tax and redistributing a portion of the revenues back to all localities was another topic of discussion. On what basis the revenues would be redistributed and the impact on the tobacco industry were not determined. The last tax that Senator Hanger's subcommittee discussed was the real estate tax and how real estate tax bills have grown steadily over the last several years largely due to increased assessments. It was suggested that the state might take on more responsibility and ease the burden on local governments.

Next meeting

The full commission orginally set October 16 as the next meeting date but due to the upcoming elections decided to cancel that meeting so all the members could concentrate on the various races around the state. It was suggested that any subcommittee chair who wanted to call a meeting for that date could do so. Therefore, the next meeting of the full commission will be November 6 in Richmond followed by another meeting on November 25.