

**Tax Policy**  
**Virginia Association of Counties**

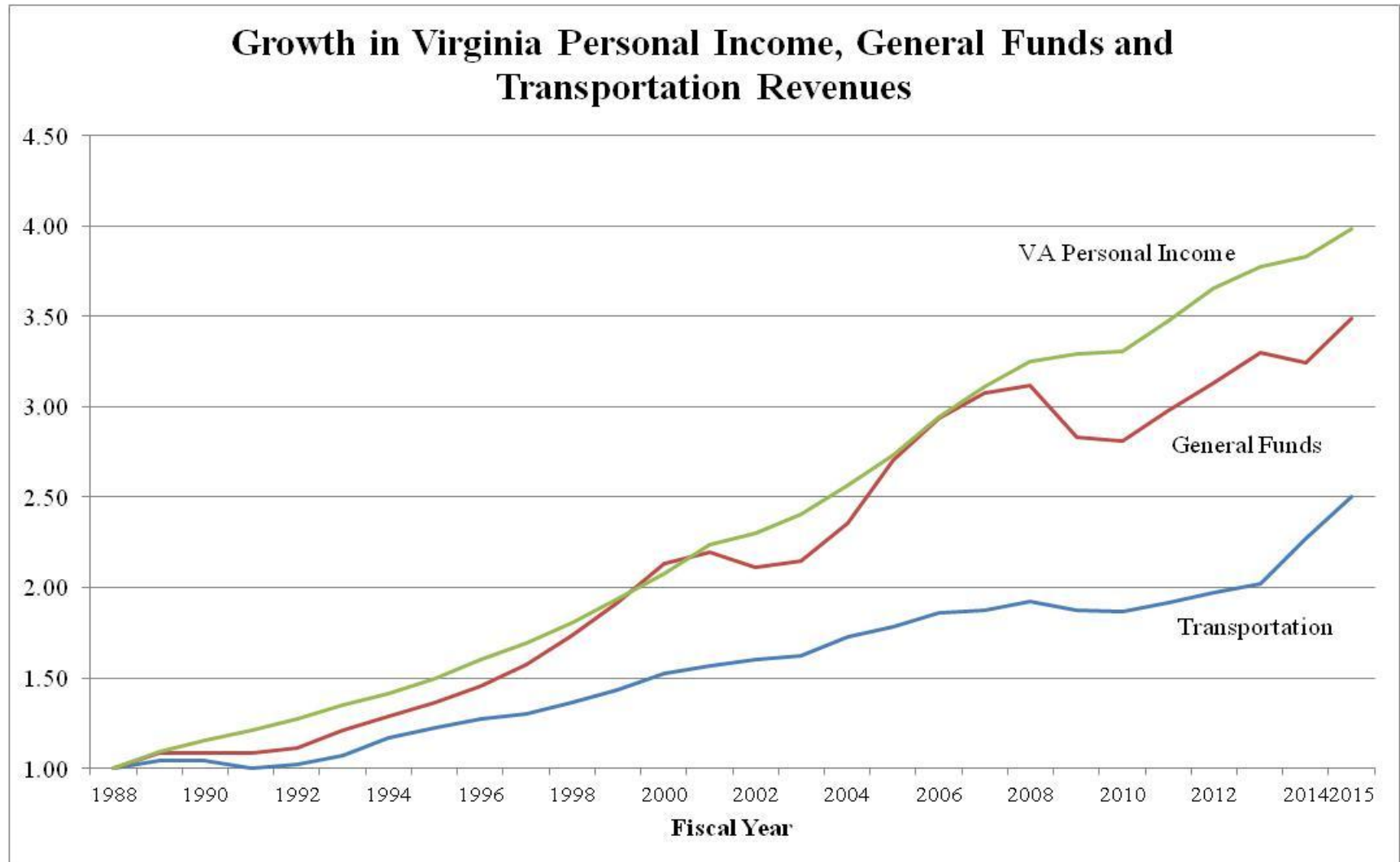
Fiscal Analytics, Ltd

August 14, 2015

# Will Tax Policy Be on the Agenda?

- Tax policy reductions occur most often when Virginia's revenues are growing.
- Governor recently indicated he is going to have Secretary of Finance Ric Brown look at the state tax code to see:
  - 1) "Is it as pro-business as it should be?"
  - 2) "Is there a way we can cut some of these rates?"
- Revenues are needed to fully fund state obligations -- particularly an adequate K-12 Standards of Quality.
  - Localities spend over \$3.6 bil. per year beyond state requirements for K-12. Over \$750 million per year in state funding needed to a) bring teacher salaries up to the national average and b) restore prevailing K-12 support costs.
  - Increase state aid also needed for local police departments (HB 599), jail per diems, sheriffs, constitutional officers, local health and human services, LODA, etc.
- Local tax bases need strengthening and diversification if state refuses to meet its funding commitments.
  - Does replacing BPOL/merchants capital with an alternative revenue source meet this objective?

# State Tax Revenue Is Lagging Overall Economic Growth



# Over Last 20 Years, Tax Changes Have Reduced Biennial State Revenues by \$3.1 Bil.

	<u>Enacted/Amended</u>	<u>Biennial (\$ Mil.)</u>
Age Subtraction (net of 2004 means testing)	1994 and 2004	(\$581)
Car Tax Reimbursement	1997, 2003	(\$1,900)
Subtraction for UI/Military/Gov't Empl	1999	(\$74)
Historic Rehab Tax Credit	1999	(\$152)
Coalfield Employment Tax Credits	2000	(\$68)
Low Income Tax Relief	2000, 2004, and 2007	(\$412)
Land Preservation Tax Credit	2003	(\$200)
Impose 2.5% Sales Tax on Food	2004	(\$1,094)
Estate Tax Repeal	2009	(\$280)
Other Tax Changes since 1999	1999-2014	(\$182)
<b>State Tax Reductions since 1994</b>		<b>(\$4,942)</b>
Sales Tax Presence in Virginia Amazon	2012	\$41
Sales tax on satellite TV equipment	2014	\$19
Add 1/2 percent sales tax on non-food items	2004	\$986
Recordation Tax Increase (net of 3 cents to transp.)	2004/2007	\$210
Tobacco Tax Increase	2004	\$285
Close 2 Corp. Tax Loopholes/Eliminate ST Exem for Pub. Svc. Co.	2004	\$286
<b>State Tax Increases since 1994</b>		<b>\$1,827</b>
<b>Net State Tax Change Since 1994</b>		<b>(\$3,115)</b>

Source: Senate Finance Committee Retreat, Revenue Outlook, Nov. 20, 2014

# Virginia Is a Wealthy, Low Tax State, With Higher Reliance on Locality Taxes

	<u>2012 JLARC Ranking</u>	<u>2015 JLARC Ranking</u>
Per capita personal income	8	10
State and local <i>revenue</i> as a percentage of personal income	49	49
State and local <i>taxes</i> as a percentage of personal income	43	45
Per capita state taxes	34	36
Per capita local taxes	13	15
Individual income taxes as a percentage of state and local tax revenue	7	6
State motor fuel tax rate rank	37	46

Source: *Virginia Compared to Other States, JLARC, 2012, 2015 Editions*

# Virginia Ranks Well Below the National Average in Spending Despite Its Wealth

	<u>2012 State Rank</u>	<u>2015 State Rank</u>
Per Capita Personal Income	8	10
Per Capita State Expenditures	32	27
State Per Pupil Funding	35	41
State and Local Per Pupil Funding	17	26
Average Salary of Public School Teachers	28	35
Per Capita State and Local Road Expenditures	38	28
Per Capita Medicaid Expenditures	47	48
Average Annual In-State Tuition and Fees at Public 4-Year Institutions	12	11

*Source: Virginia Compared to Other States, JLARC, 2012, 2015 Editions*

# Options for Strengthening/Diversifying the State/Local Tax Base

- Make the state income tax more progressive? A tax rate of 6.0% above \$50,000 and 6.25% above \$100,000 in taxable income would raise about \$700 mil. per year.
- Limit/means test individual income tax itemized deductions (e.g., mortgage interest) or special tax preferences (e.g., land preservation), or corporate tax benefits (e.g., single sales factor)?
- Increase the sales tax rate? Each additional statewide 1% raises \$1 bil.
- Apply sales taxes to selected personal and repair services?
- Increase “sin” taxes. Tobacco tax: \$6 mil per penny. Double the beer and beverage tax for \$43 mil.
- Expand the differential commercial/industrial property tax rate currently used in Northern Virginia (and available in Hampton Roads)?
- Allow counties same taxing authority *by ordinance* as cities for meals and transient occupancy taxes.
- Adopt additional regional taxing strategies?

# Difficult to Replace BPOL and M&T Taxes With an Alternative Revenue Source

- Total offsetting revenue needed would be about \$709 million for BPOL and \$216 million for M&T. 36 cities and 90 counties levy a BPOL tax.
- 60 percent of businesses pay under \$100 per year in BPOL. 3 percent of businesses pay nearly two-thirds of BPOL levies.
- There is a wide range of reliance on BPOL and M&T for locally-generated revenue. For BPOL, up to 10.7 percent in 36 cities and 6.2 percent in 90 counties and 18 percent in large towns. For M&T, up to 32 percent in cities, 27 percent in counties, and 36 percent in towns.
- Replacing BPOL with a higher local option sales tax would shift tax from businesses to consumers and would raise the sales tax rate to higher than Maryland and D.C.
- It would also be difficult to replace BPOL with an income tax surcharge, unless each locality is authorized to set their own income tax surcharge rate.



# *Detailed State/Local Tax Data Section*

# Main Elements of 2004 Tax Reform

Increased revenues a net \$800 million per year.

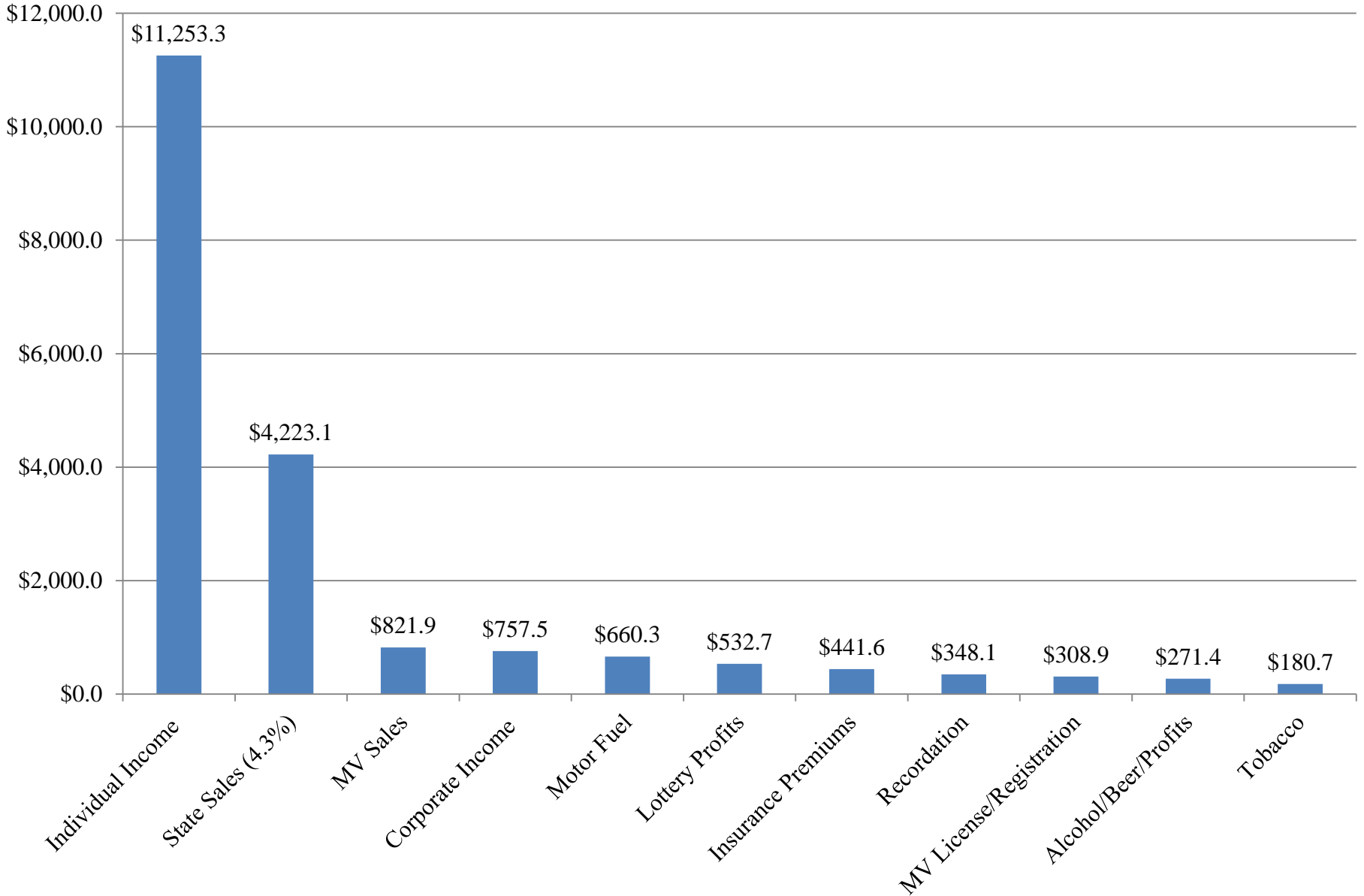
Major increases:

- Increased sales tax by 0.5 cents.
- Means-tested age 65 and over deduction and eliminated 62-64 deduction.
- Tobacco tax increase from 2.5 cents to 30 cents per pack
- Increased recordation tax from 15 cents to 25 cents per \$100 of value.
- Closed corporate loopholes.

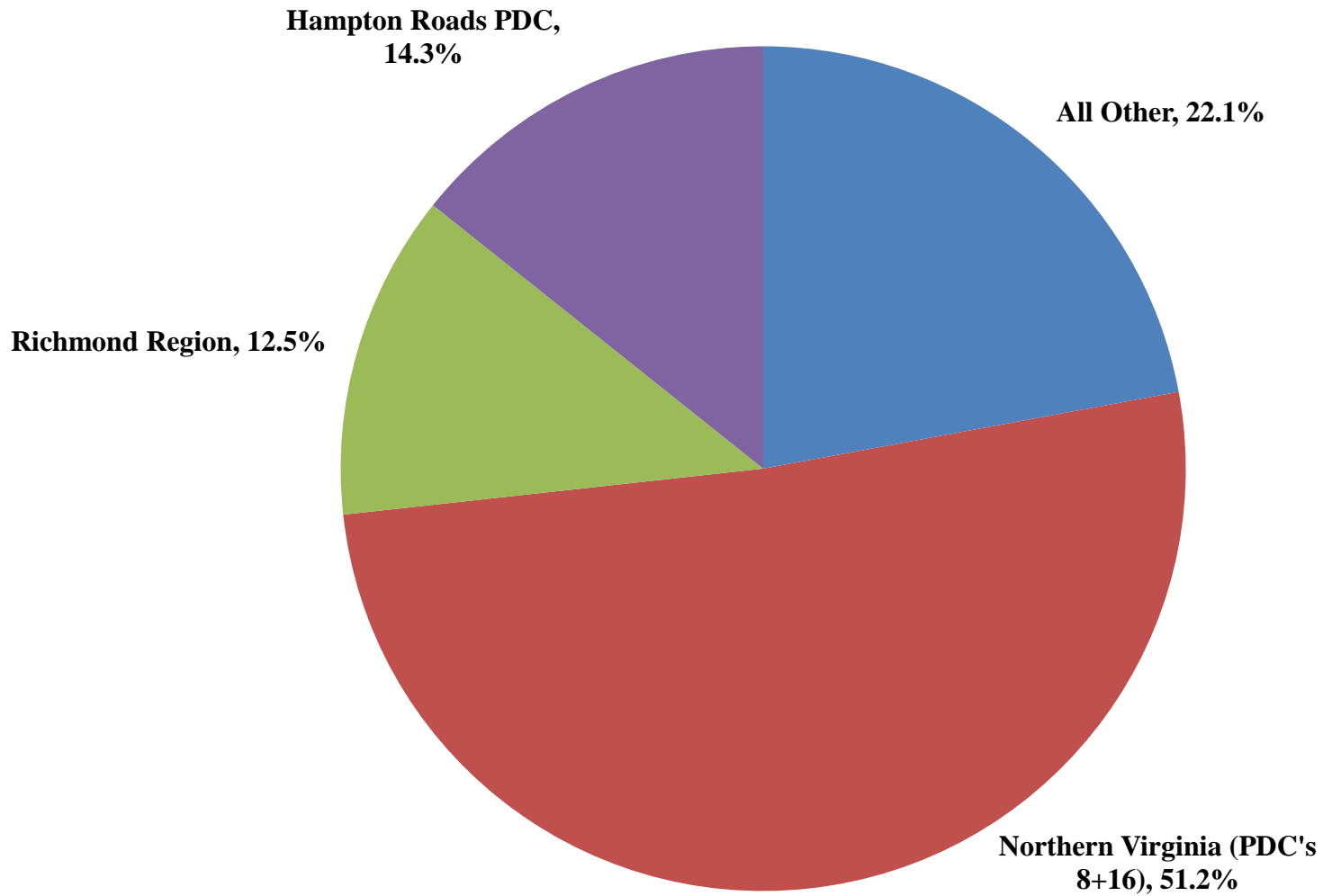
Major decreases:

- Increased income tax personal exemption and standard deduction.
- Allowed low income filers an earned income credit.
- Reduced food for home consumption sales tax rate from 4 percent to 2.5 cents (preserved food tax on local option and school-age population education funding).

# FY 2014 Major State Tax Revenues (\$ Mil.)



# Percent of 2012 State Income Tax



# Where Are the High Income Taxpayers Located?

## Tax Year 2012 Income Tax Returns

<b>PDC</b>	<b><u>%Returns over \$50,000 AGI</u></b>	<b><u>%Returns over \$100,000 AGI</u></b>
1 Lenowisco	13.1%	6.1%
2 Cumberland Plateau	16.1%	8.1%
3 Mount Rogers	12.5%	6.4%
4 New River Valley	18.2%	10.2%
5 Roanoke Valley-Alleghany	19.2%	11.1%
6 Central Shenandoah	16.9%	8.9%
7 Northern Shenandoah Valley	22.1%	13.0%
8 <b>Northern Virginia</b>	<b>40.1%</b>	<b>30.2%</b>
9 Rappahannock-Rapidan	29.3%	19.3%
10 Thomas Jefferson	25.5%	16.7%
11 Region 2000	18.2%	10.2%
12 West Piedmont	12.3%	6.2%
13 Southside	11.5%	5.7%
14 Commonwealth RC	12.7%	6.2%
15 Richmond Regional	26.0%	17.1%
16 George Washington RC	32.6%	22.3%
17 Northern Neck	17.3%	10.1%
18 Middle Peninsula	21.0%	11.6%
19 Crater	14.8%	7.8%
22 Accomack-Northhampton	12.1%	6.8%
23 Hampton Roads	21.4%	13.2%
Statewide	26.6%	18.0%

# Distributing the Virginia Sales Tax Is Complicated

	<u>FY 2016</u>
General Fund - Unrestricted	2.075
K-12 Education for SOQ by <i>School-Age Population</i>	1.125
K-12 Education for SOQ by <i>LCI</i>	<u>0.250</u>
<b><i>Subtotal GF</i></b>	<b>3.450</b>
Transportation TTF (highway construction, transit, ports, airports)	0.500
Transportation HMOF (highway maintenance)	0.225
Transportation Mass Transit	0.075
Transportation Intercity Rail	<u>0.050</u>
<b><i>Subtotal Transportation</i></b>	<b>0.850</b>
Local Sales Tax	1.000
Regional Sales Tax (NoVa, Hampton Roads)	<u>0.700</u>
<b><i>Subtotal Local</i></b>	<b>1.700</b>
Grand Total (Rest-of-State)	5.300
Grand Total (NoVa, Hampton Roads)	6.000

# Potential for an Expansion of the Sales Tax to Services

Many economic sectors are not potential or realistic candidates for a retail sales tax.

Some are producers or providers of goods that are already subject to the sales tax later in the economic stream, such as Forestry, Mining, Agriculture, Wholesale Trade, and Manufacturing

Other economic sectors are excluded from consideration because they involve intermediate services dealing with goods that are not provided to “end users” - Warehouse, Transportation, Management, and Information Technology services.

Utility Sector and Telecommunication products are already taxed at the state and local level -- to impose an additional state sales tax probably would not be politically feasible.

Finance, Insurance, and Real Estate are taxed with other types of taxes and the type of transaction does not readily lend itself to a “sales” tax (check cashing, insurance or stock purchases). TJI proposes a 5 percent sales tax on all real estate rental income – residential and nonresidential (\$462 mil.).

Health care, social services, and private education services are generally not politically viable industries for a sales tax.

Are professional (accountants, attorneys, engineers, architects) and skilled services (carpenters, plumbers, electricians) realistic candidates for a sales tax?

**Personal services and repair labor are the most likely candidate for an expansion of the sales tax base. Total potential new revenue: \$200-300 million/yr.**

# Highest Income Tax Rates by State

		<b>Highest Combined S/L Income Tax (%)</b>	<b>Highest State Tax (%)</b>	<b>Highest Local Tax (%)</b>	<b>Income Threshold for Highest Rate</b>
1	California	14.80	13.30	1.50	\$1,000,000
2	New York	12.70	8.82	3.88	\$1,062,650
3	Hawaii	11.00	11.00		\$200,000
4	Oregon	10.59	9.90	0.69	\$125,000
5	Iowa	9.98	8.98	1.00	\$69,255
6	New Jersey	9.97	8.97	1.00	\$500,000
7	Minnesota	9.85	9.85		\$154,950
8	Maryland	8.95	5.75	3.20	\$250,000
9	Vermont	8.95	8.95		\$411,500
10	Washington DC	8.95	8.95		\$350,000
11	Kentucky	8.50	6.00	2.50	\$75,000
12	Ohio	8.08	5.33	2.75	\$208,500
13	Maine	7.95	7.95		\$20,899
14	Delaware	7.85	6.60	1.25	\$60,000
15	Wisconsin	7.65	7.65		\$244,270
16	Idaho	7.40	7.40		\$10,717
17	Alabama	7.00	5.00	2.00	\$3,000
18	Arkansas	7.00	7.00		\$34,599
19	Missouri	7.00	6.00	1.00	\$9,000
20	Pennsylvania	7.00	3.07	3.93	\$0
21	South Carolina	7.00	7.00		\$14,400
22	Montana	6.90	6.90		\$17,000
23	Nebraska	6.84	6.84		\$29,460
24	Michigan	6.75	4.25	2.50	% of Federal
25	Connecticut	6.70	6.70		\$250,000
26	West Virginia	6.50	6.50		\$50,000



## Highest Income Tax Rates by State (Cont'd)

		Highest Combined S/L Income Tax (%)	Highest State Tax (%)	Highest Local Tax (%)	Income Threshold for Highest Rate
27	Indiana	6.43	3.30	3.13	% of Federal
28	Georgia	6.00	6.00		\$7,000
29	Louisiana	6.00	6.00		\$50,000
30	Rhode Island	5.99	5.99		\$137,650
31	Colorado	5.78	4.63	1.15	\$0
32	North Carolina	5.75	5.75		\$0
33	<b>Virginia</b>	<b>5.75</b>	<b>5.75</b>		<b>\$17,500</b>
34	Oklahoma	5.25	5.25		\$8,700
35	Massachusetts	5.15	5.15		\$0
36	Mississippi	5.00	5.00		\$10,000
37	Utah	5.00	5.00		\$0
38	New Mexico	4.90	4.90		\$16,000
39	Kansas	4.60	4.60		\$15,000
40	Arizona	4.54	4.54		\$150,000
41	Illinois	3.75	3.75		% of Federal
42	North Dakota	3.22	3.22		\$405,100
43	New Hampshire		Interest and Dividends Only		
44	Tennessee		Interest and Dividends Only		
45	Alaska		No Income Tax		
46	Florida		No Income Tax		
47	Nevada		No Income Tax		
48	South Dakota		No Income Tax		
49	Texas		No Income Tax		
50	Washington		No Income Tax		
51	Wyoming		No Income Tax		

# State and Local Sales Tax Rates

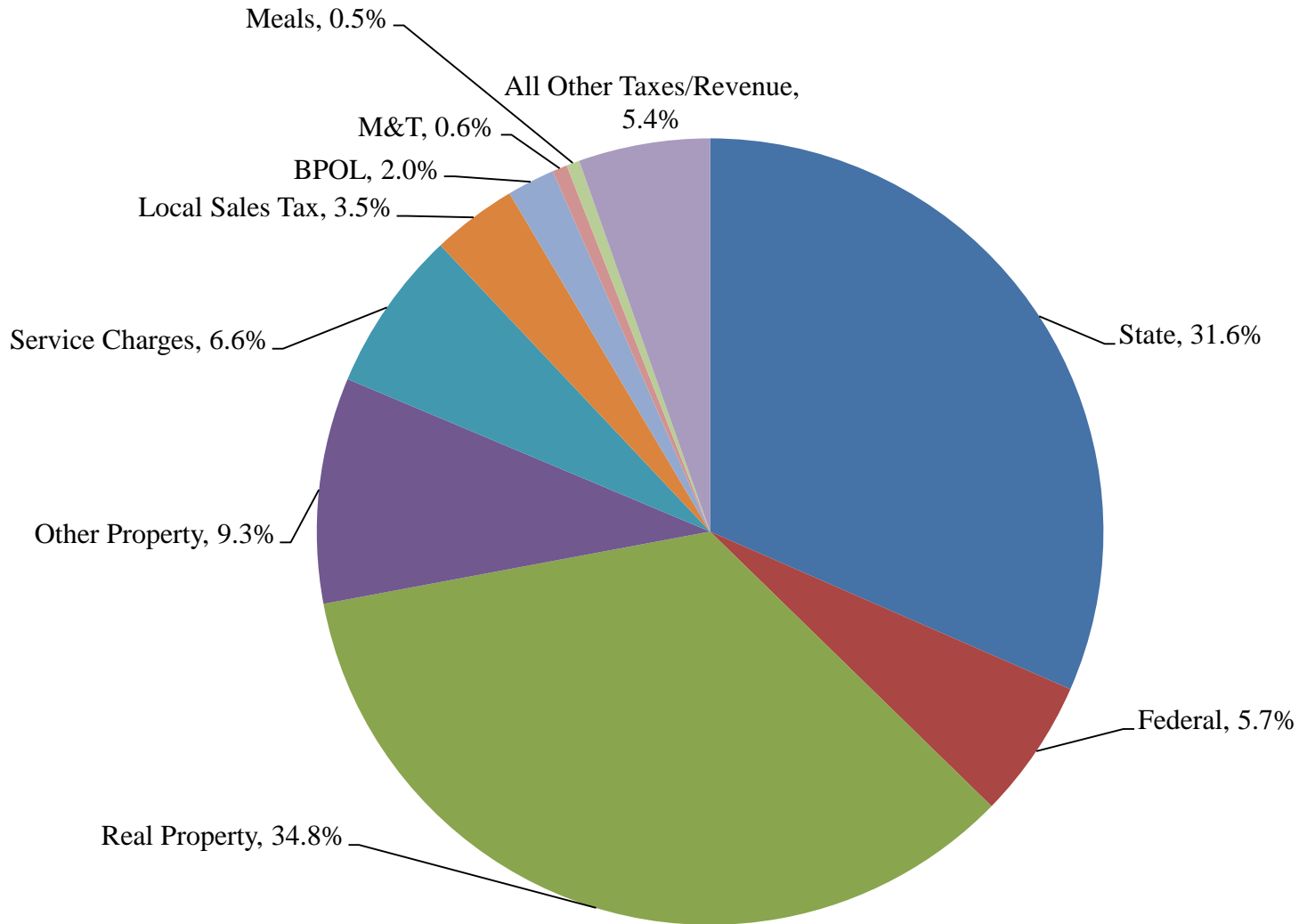
	<u>State</u>	<u>Lowest Local</u>	<u>Highest Local</u>	<u>Highest Combined</u>
Arkansas	6.50	0.00	5.50	12.00
Louisiana	4.00	0.00	7.00	11.00
Oklahoma	4.50	0.00	6.50	11.00
Arizona	5.60	0.25	5.11	10.71
Alabama	4.00	0.00	6.00	10.00
California	7.50	0.00	2.50	10.00
Colorado	2.90	0.00	7.10	10.00
Illinois	6.25	0.00	3.50	9.75
Tennessee	7.00	2.27	2.75	9.75
Kansas	6.15	0.00	3.50	9.65
Washington	6.50	7.00	3.10	9.60
Missouri	4.23	4.73	5.25	9.48
Idaho	6.00	0.00	3.00	9.00
South Carolina	6.00	0.00	3.00	9.00
New York	4.00	3.00	4.88	8.88
New Mexico	5.13	0.66	3.50	8.63
Utah	5.95	0.00	2.40	8.35
Texas	6.25	0.00	2.00	8.25
Nevada	6.85	0.00	1.25	8.10
Georgia	4.00	5.00	4.00	8.00
North Dakota	5.00	0.00	3.00	8.00
Ohio	5.75	6.50	2.25	8.00
Pennsylvania	6.00	0.00	2.00	8.00
Nebraska	5.50	0.00	2.50	8.00
Minnesota	6.88	0.00	1.00	7.88
Florida	6.00	0.00	1.50	7.50

## State and Local Sales Tax Rates (Cont'd)

	<u>State</u>	<u>Lowest Local</u>	<u>Highest Local</u>	<u>Highest Combined</u>
North Carolina	4.75	2.00	2.75	7.50
Mississippi	7.00	0.00	0.25	7.25
Indiana	7.00	0.00	0.00	7.00
Iowa	6.00	0.00	1.00	7.00
New Jersey	7.00	0.00	0.00	7.00
Rhode Island	7.00	0.00	0.00	7.00
Vermont	6.00	0.00	1.00	7.00
West Virginia	6.00	0.00	0.50	6.50
Connecticut	6.35	0.00	0.00	6.35
Massachusetts	6.25	0.00	0.00	6.25
Kentucky	6.00	0.00	0.00	6.00
Maryland	6.00	0.00	0.00	6.00
Michigan	6.00	0.00	0.00	6.00
<b>Virginia</b>	<b>4.30</b>	<b>1.00</b>	<b>1.70</b>	<b>6.00</b>
South Dakota	4.00	0.00	2.00	6.00
Wyoming	4.00	0.00	2.00	6.00
Washington D.C.	5.75			5.75
Wisconsin	5.00	0.00	0.60	5.60
Maine	5.50	0.00	0.00	5.50
Hawaii	4.00	0.00	0.50	4.50
Alaska	No Sales Tax			
Delaware	No Sales Tax			
Montana	No Sales Tax			
New Hampshire	No Sales Tax			
Oregon	No Sales Tax			

Source: <http://www.tax-rates.org/taxtables/sales-tax-by-state>

# FY 2014 Sources of Revenue for VA Counties - \$19.5B



Note: "All Other Taxes/Revenue" includes, licenses/permits, fines/fees, rental/sales, and other taxes incl. transient occupancy, MV license, recordation, bank stock, tobacco, admission, severance, franchise license, other

Source: Auditor of Public Accounts Comparative Report of Revenues and Expenditures

# Median Real Property Tax Rates By State

	<u>Median Property Tax (%)</u>		<u>Median Property Tax (%)</u>
1 New Jersey	1.89%	27 Indiana	0.85%
2 New Hampshire	1.86%	28 Nevada	0.84%
3 Texas	1.81%	29 Georgia	0.83%
4 Nebraska	1.76%	30 Montana	0.83%
5 Wisconsin	1.76%	31 North Carolina	0.78%
6 Illinois	1.73%	32 California	0.74%
7 Connecticut	1.63%	33 Oklahoma	0.74%
8 Michigan	1.62%	<b>34 Virginia</b>	<b>0.74%</b>
9 Vermont	1.59%	35 Arizona	0.72%
10 North Dakota	1.42%	36 Kentucky	0.72%
11 Ohio	1.36%	37 Idaho	0.69%
12 Pennsylvania	1.35%	38 Tennessee	0.68%
13 Rhode Island	1.35%	39 Colorado	0.60%
14 Iowa	1.29%	40 Utah	0.60%
15 Kansas	1.29%	41 Wyoming	0.58%
16 South Dakota	1.28%	42 New Mexico	0.55%
17 New York	1.23%	43 Arkansas	0.52%
18 Maine	1.09%	44 Mississippi	0.52%
19 Minnesota	1.05%	45 South Carolina	0.50%
20 Alaska	1.04%	46 West Virginia	0.49%
21 Massachusetts	1.04%	47 Washington DC	0.46%
22 Florida	0.97%	48 Delaware	0.43%
23 Washington	0.92%	49 Alabama	0.33%
24 Missouri	0.91%	50 Hawaii	0.26%
25 Maryland	0.87%	51 Louisiana	0.18%
26 Oregon	0.87%		