

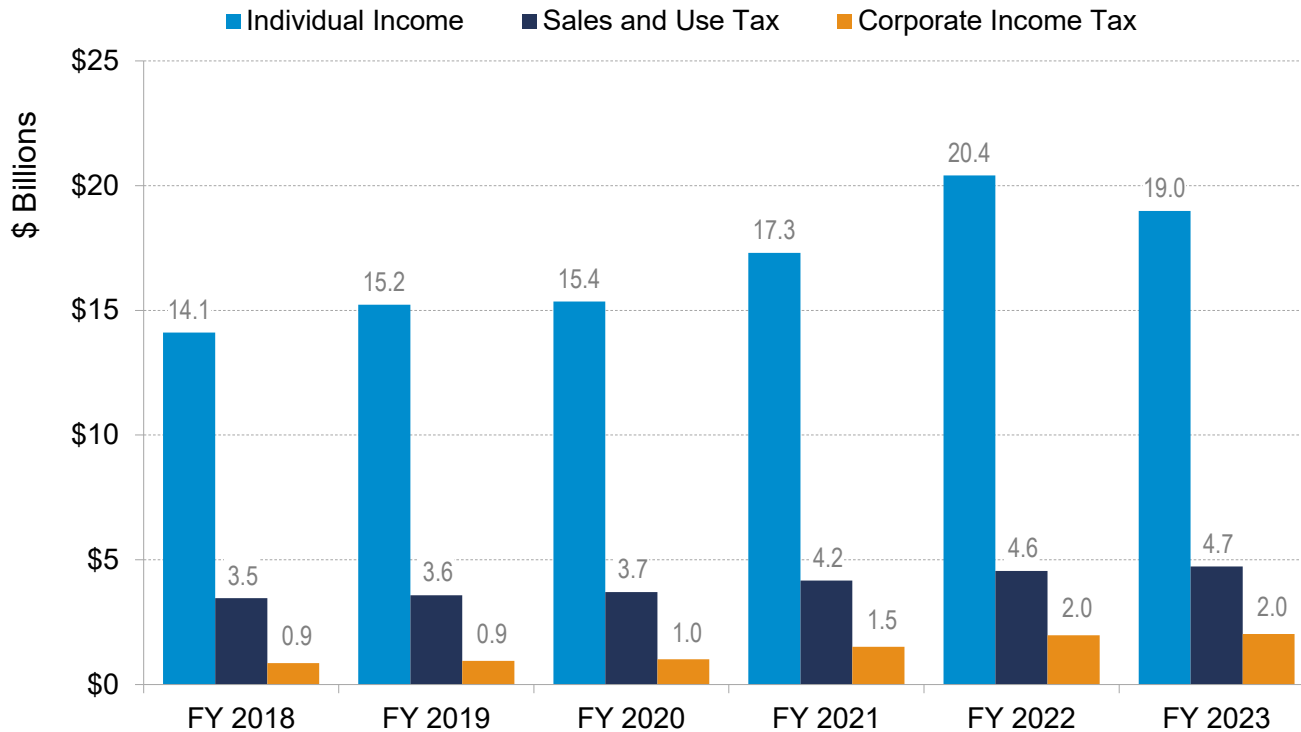
Overview of Virginia Taxes

August 14, 2024

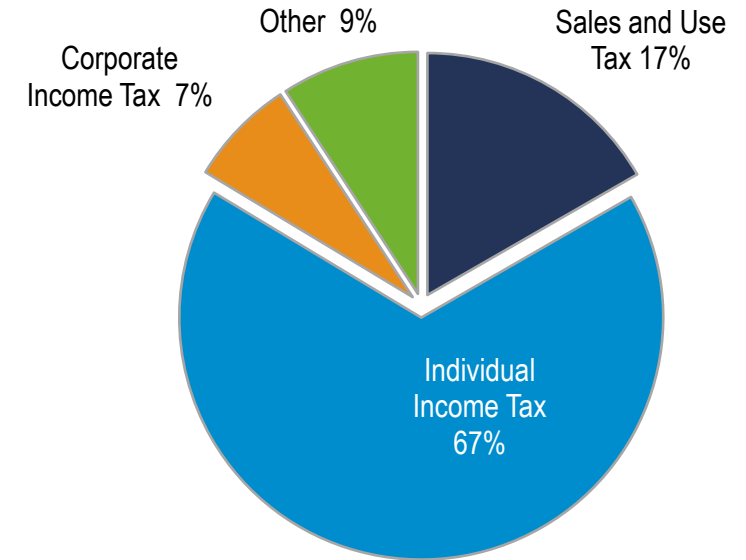
Types of Taxes

General Fund Revenues by Source (FY 2023)

Fiscal Year Department Net Revenue Collections Selected Tax Types



Collection of Revenues Administered by the Department



General Fund Revenue

- ▶ Individual Income Taxes
- ▶ Corporate Income Taxes
- ▶ Retail Sales and Use Tax (portion to localities and non-General Funds)
- ▶ Insurance Premiums License Tax (transferred to non-General Funds)
- ▶ Bank Franchise Tax (portion distributed to localities)
- ▶ Railroad Rolling Stock Tax
- ▶ Estate Tax (estates of persons who died before July 1, 2007)
- ▶ Recordation, Suits, and Probate Taxes (collected by clerks of the Circuit Courts)

Non-General Fund Revenue

- ▶ Communications Sales Tax (distributed to localities)
- ▶ Aircraft Sales and Use Tax
- ▶ Watercraft Sales and Use Tax (collected by Department of Wildlife Resources)
- ▶ Cigarette and Other Tobacco Products Taxes
- ▶ Commodity Taxes: Apple, Corn, Cotton, Egg, Forest Products, Peanut, Sheep, Small Grains, Soybeans, Tires, Litter, Soft Drinks

Examples of Taxes Administered by Other Agencies

- ▶ Public Utility License Tax (SCC)
- ▶ Beer and Beverage, Distilled Spirits, and License Taxes (ABC)
- ▶ Unemployment Compensation Tax (VEC)
- ▶ Premium Tax on Workers' Compensation Insurance (Workers' Compensation Commission)
- ▶ Motor Fuel, Motor Vehicle Sales, and Rental Taxes (DMV)
- ▶ Utility Consumer Taxes (SCC)

Examples of Taxes Administered by Localities

- ▶ Real Property Taxes
- ▶ Personal Property Taxes
- ▶ Machinery & Tools Tax
- ▶ Business, Professional, and Occupational License Tax (BPOL)
- ▶ Meals Tax
- ▶ Admissions Tax
- ▶ Transient Occupancy Tax

Individual Income Tax

Who Must File a Return

- ▶ You must file an income tax return in Virginia if:
 - ▶ You are a resident of Virginia, part-year resident, or a nonresident, and
 - ▶ You are required to file a federal income tax return, and
 - ▶ You have Virginia adjusted gross income equal to or greater than the amounts below:

Filing Status	Income Threshold
Single or married filing separately	\$11,950
Married filing jointly	\$23,900

- ▶ Businesses not organized as C corporations (such as partnership/LLCs/S corporations) pay tax on their profits at the owner level as part of the individual income tax.

Individual Income Tax Rates

- ▶ Virginia applies four different income tax rates based on the taxpayer's taxable income.

Virginia Taxable Income	Rate
\$0 to \$3,000	2%
\$3,001 to \$5,000	3% plus \$60
\$5,001 to \$17,000	5% plus \$120
\$17,001 and higher	5.75% plus \$720

- ▶ Most Virginia taxpayers pay the top marginal rate of 5.75%.
 - ▶ As a result, most Virginia taxpayers pay \$720 (the total amount of tax owed for the lower three tax brackets) + 5.75% on the amount of their income that exceeds \$17,000.

Conformity with Federal Law

- ▶ Since 2023, Virginia generally conforms to federal definitions of income included in the Internal Revenue Code (“IRC”) automatically on a rolling basis (“rolling conformity”) (HB 2193 & SB 1405).
 - ▶ Before 2023, Virginia conformed to the IRC as of a certain date (“fixed date conformity”).
 - ▶ Since switching to rolling conformity in 2023, there have been no major federal tax law changes impacting Virginia.
- ▶ Under current law, Virginia conforms to the IRC on a rolling basis, subject to the following exceptions:
 - ▶ Any amendment that would increase or decrease General Fund revenues by more than \$15 million.
 - ▶ All amendments if the cumulative impact of such amendments would increase or decrease General Fund revenues by more than \$75 million.

Deconformity Provisions

- ▶ Virginia deconforms from the following federal provisions:
 - ▶ Bonus depreciation allowed for certain assets under federal law.
 - ▶ The five-year carryback of certain NOL deductions generated in TY 2008 and 2009.
 - ▶ The federal treatment of applicable high yield discount obligations.
 - ▶ Tax exclusions related to cancellation of debt income.
 - ▶ The suspension of the federal overall limitation on itemized deductions.
 - ▶ The reduction in the medical expense deduction floor.
 - ▶ Certain business provisions of the federal CARES Act.
 - ▶ Certain COVID-related small business assistance programs before TY 2021.

Standard Deduction

- ▶ Under the TCJA, the federal standard deduction was increased to \$12,000 (\$24,000 for joint filers), indexed for inflation (set to expire in TY 2026).
- ▶ The 2019, 2022, and 2023 Virginia increases are also set to expire in TY 2026.

Filing Status	1972-1986	1987	1988	1989-2004	2005-2019	2020-2021	2022-2023	2024-2025	2026*
Single	The greater of 15% of AGI or \$1,300, not to exceed \$2,000	\$2,000	\$2,700	\$3,000	\$3,000	\$4,500	\$8,000	\$8,500	\$3,000
Married				\$5,000	\$6,000	\$9,000	\$16,000	\$17,000	\$6,000
Married Separate	The greater of 15% of AGI or \$650, not to exceed \$1,000	\$1,000	\$1,350	\$2,500	\$3,000	\$4,500	\$8,000	\$8,500	\$3,000

*Beginning with TY 2026, the standard deductions are set to return to the TY 2019 amounts of \$3,000/\$6,000.

Computation of Tax

Starting point is Federal Adjusted Gross Income (FAGI)	\$70,000
Add specified items to the extent that they are excluded from FAGI	+ \$100
Subtract specified items to the extent they are included in FAGI	- \$200
Specified deductions, such as the \$12,000 age deduction	- \$12,000
Either the standard deduction or itemized deductions; and	- \$17,000
Personal exemptions	<u>930+930+800+800 = - \$3,460</u>
Taxable Income	\$37,440
Apply tax rates	$[720 + (.0575 * (37,440 - 17,000))] =$ \$1,895
Apply any tax credits to reduce tax liability	<u>- \$1,000</u>
Virginia Tax Liability	\$895

- ▶ Federal law limited the federal deduction for state and local taxes (SALT) to \$10,000.
- ▶ Virginia's PTET was implemented as a SALT cap workaround.
 - ▶ It allows pass-through entities ("PTE") to make an annual election to pay an elective entity level income tax at a rate of 5.75%.
 - ▶ It also allows a corresponding refundable income tax credit to certain PTE owners for PTET paid by a PTE that makes the election.
- ▶ The PTET was intended to be revenue neutral but resulted in an initial revenue increase related to overpayments by taxpayers that carried forward into FY 2024.
- ▶ This appears gradually to be stabilizing as taxpayers claim PTET refunds and adjust their behavior going forward.

Corporate Income Tax

Taxation of Virginia and Multistate Corporations

- ▶ Virginia's corporate income tax is applied at a flat rate of 6%.
- ▶ Virginia taxes all of the taxable income of corporations doing business only in Virginia.
- ▶ In contrast, Virginia taxes only the percentage of taxable income apportioned to Virginia by multistate corporations (corporations doing business in multiple states).
 - ▶ Virginia's default method of apportionment consists of three factors: property, payroll, and sales (double-weighted).
 - ▶ In certain situations, Virginia permits or requires the use of special apportionment methods that differ from the default method of apportionment.

Virginia's Current Apportionment Structure

- ▶ Most corporations are required to use Virginia's default method of apportionment to determine the amount of income that is subject to Virginia income taxation.
- ▶ The default method of apportionment generally consists of three factors:
 - ▶ Property: Value of property in Virginia divided by the value of property everywhere.
 - ▶ Payroll: Compensation paid to employees in Virginia divided by compensation paid everywhere.
 - ▶ Sales: Sales (gross receipts) made in Virginia divided by sales everywhere. The sales factor is double weighted.

Special Apportionment Methods

- ▶ For certain taxpayers, Virginia permits or requires the use of special apportionment methods that differ from the default three factor apportionment method.
 - ▶ Virginia law includes special apportionment methods for certain industries, including: financial corporations, construction contractors, motor carriers, and railway companies.
 - ▶ In 2018, the General Assembly authorized certified company apportionment for companies operating in certain disadvantaged localities (administered by VEDP).
- ▶ Virginia also allows companies to request an alternative method of apportionment in situations where the statutory three-factor apportionment method is inapplicable or inequitable.

Single-Sales Factor

- ▶ Another alternative to Virginia's default three factor method of apportionment is the single-sales factor method of apportionment.
- ▶ Under single-sales factor apportionment, the share of a corporation's total profit that is taxed in Virginia is based solely on the share of the corporation's sales occurring in Virginia as compared to sales everywhere.
- ▶ The General Assembly has enacted single-sales factor methods for:
 - ▶ Manufacturers (elective - 2009)
 - ▶ Retailers (2012)
 - ▶ Enterprise data centers (2015) and
 - ▶ Debt buyers (in combination with market-based sourcing - 2018).

Virginia's Current Apportionment Structure – How Sales Are Assigned

- ▶ Sales of tangible personal property:
 - ▶ In Virginia if delivered to a location in Virginia.
 - ▶ Outside Virginia if delivered to a location outside of Virginia.
- ▶ Sales of services or intangible property:
 - ▶ Default rule is based upon whether the greater portion of income producing activity (measured by costs of performance) is in Virginia or not.
 - ▶ An alternative to Virginia's default cost of performance rule is market-based sourcing. It has been adopted for debt buyers (2018), property information and analytics firms (2022), and internet root infrastructure providers (2023).

General Rule: Corporate Filing Status Election

- ▶ Affiliated groups can file separate, combined, or consolidated returns.
- ▶ Virginia Tax has the statutory authority to grant or deny requests by corporations to change their Virginia tax filing status.
 - ▶ Because switching to/from the consolidated filing status affects the allocation and apportionment formulas and may affect how income arising from activity in Virginia is reflected, Virginia Tax generally will not grant permission to change to/from a consolidated filing status.
 - ▶ In contrast, separate and Virginia combined returns do not affect the allocation and apportionment formulas for each corporation; therefore, permission to change from separate to Virginia combined returns or from Virginia combined to separate returns is generally granted.

Exception: Switching Corporate Filing Election

- ▶ An affiliated group may elect to change to or from the consolidated filing status if:
 - ▶ It has filed on the same basis for at least the last 12 years and,
 - ▶ It agrees to pay the greater of the tax under the old filing method and the new filing method for the taxable year in which the new election is effective and for the immediately succeeding taxable year.
- ▶ Before changes made by the General Assembly in 2022 and 2023, this exception was more limited, requiring that:
 - ▶ The affiliated group had filed on the same basis for at least the last 20 years and,
 - ▶ For the year preceding the year for which the new election would be applicable, there would have been no decrease in tax computed under the new filing method as compared to old filing method.

Retail Sales and Use Tax

Overview

- ▶ Tax on the sale, lease, or rental of tangible personal property (TPP) or the use or consumption of tangible personal property in Virginia.
 - ▶ Consumers are responsible for paying sales tax at the time of purchase.
 - ▶ Dealers are responsible for charging and collecting the tax at the time of purchase and for remitting the tax timely.
- ▶ Although all sales taxes collected are remitted directly to Virginia Tax, a portion is distributed to the localities where the sales were made.
- ▶ Remote sellers and marketplace facilitators are required to collect the tax if annual sales made or facilitated to Virginia customers exceed \$100,000 or 200 transactions.
- ▶ Use tax also applies to TPP purchased outside of Virginia, but used, consumed or stored in Virginia that would have been subject to the tax had it been purchased in Virginia.

Rate Increases

- 1968: State rate increased from 2% to 3%
- 1987: State rate increased to 3.5%
- 2004: State rate increased to 4%
- 2013: State rate increased to 4.3%

Rate Reductions

- 2000: State tax on food reduced by 2% over 4 years (contingent on certain revenue targets)
- 2005: Food tax provisions accelerated to reduce state rate from 3% to 1.5% (2.5% state & local)
- 2019: State tax on personal hygiene products reduced to 1.5% (2.5% state & local)
- 2022: Eliminated the state tax on food/personal hygiene products (local 1% still applies)

Regional & Local Tax Rates

- 2013: Additional 0.7% tax in Hampton Roads and Northern Virginia (transportation funding)
- 2018: Additional 1% tax in Historic Triangle (regional tourism marketing)
- 2020: Additional 0.7% tax in Central Virginia (transportation funding)
- 2020-21: Certain localities authorized to impose an additional 1% tax for school construction

Hampton Roads & Historic Triangle (6-7%)*	Northern Virginia Region (6%)	Central Virginia Region (6%)	Additional 1% School Construction (6.3%)	Statewide Rate (5.3%)
Chesapeake Franklin Hampton Isle of Wight Newport News Norfolk Poquoson Portsmouth Suffolk Virginia Beach	Alexandria Arlington Fairfax City Falls Church Loudoun Manassas Manassas Park Prince William	Charles City Co. Chesterfield Goochland Hanover Henrico New Kent Powhatan	Charlotte Danville Gloucester Halifax Henry Northampton Patrick Pittsylvania	All other localities
Williamsburg* James City* York*				

*Williamsburg, James City Co., and York Co. subject to additional 1% Historic Triangle tax rate

- ▶ Retail sales tax is imposed on the sale, lease or rental of tangible personal property and limited services, as well as services in connection with the sale of tangible personal property.
- ▶ Transactions involving pure services, with no tangible deliverables, are generally not taxable.
- ▶ Services provided in connection with tangible personal property are taxable, unless there is a statutory exemption for such services.
- ▶ In addition, the following services are taxable:
 - ▶ Services in connection with fabrication of tangible personal property;
 - ▶ Services in connection with serving meals; and
 - ▶ Rooms, lodgings, or accommodations furnished to transients for less than 90 days.

Nontaxable Services

- ▶ Personal, professional, or insurance transactions which involve sales as inconsequential elements for which no separate charge is made.
- ▶ Separately stated services performed by repairmen.
- ▶ Separately stated labor or service charges for the repair, installation, application or remodeling of tangible personal property.
- ▶ Separately stated transportation charges.
- ▶ Separately stated charges for alterations to apparel, clothing and garments.
- ▶ Charges for gift wrapping services performed by a nonprofit organization.

- ▶ Goods available in digital or electronic formats are generally not taxable.
- ▶ Computer Software and Software Related Services:
 - ▶ Canned or off-the-shelf software is taxable if delivered in tangible format (e.g., on a CD).
 - ▶ However, if it is delivered via email or a key is supplied that facilitates a download, the software is not taxable.
 - ▶ Amounts separately charged for labor or services rendered in connection with modification of pre-written software programs are nontaxable.
 - ▶ Custom Software is not taxable regardless of the method of delivery; to be considered “Custom”, software must be developed from scratch.
- ▶ Software as a Service (SaaS) such as cloud computing, is considered a service and is not taxable.

Resources

- ▶ Virginia Tax Code: [Title 58.1 of the *Code of Virginia*](#)
- ▶ Annual Reports: <https://www.tax.virginia.gov/annual-reports>
- ▶ Legislative Summaries: <https://www.tax.virginia.gov/legislative-summary-reports>
- ▶ Virginia Tax homepage: <https://www.tax.virginia.gov>
- ▶ Laws, Rules, and Decisions: <https://www.tax.virginia.gov/laws-rules-decisions>
- ▶ Guidance Documents: <https://www.tax.virginia.gov/guidance-documents>
- ▶ Resident Individual Income Tax Return: [Form 760](#)
- ▶ [Virginia Tax Calculator](#)

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