

Retail Sales and Use Tax Exemptions

Joint Subcommittee on Tax Policy

October 31, 2024

Divided into 8 Broad Categories

- ▶ Governmental exemptions:
 - ▶ Prevents unconstitutional taxation of federal government.
 - ▶ Prevents state government from taxing itself.
- ▶ Commodities exemptions:
 - ▶ Avoids double taxation.
- ▶ Agricultural exemptions:
 - ▶ Avoids taxing inputs used to create goods that will be taxed - tax pyramiding.
- ▶ Commercial & Industrial exemptions:
 - ▶ Avoids taxing inputs used to create goods that will be taxed - tax pyramiding.

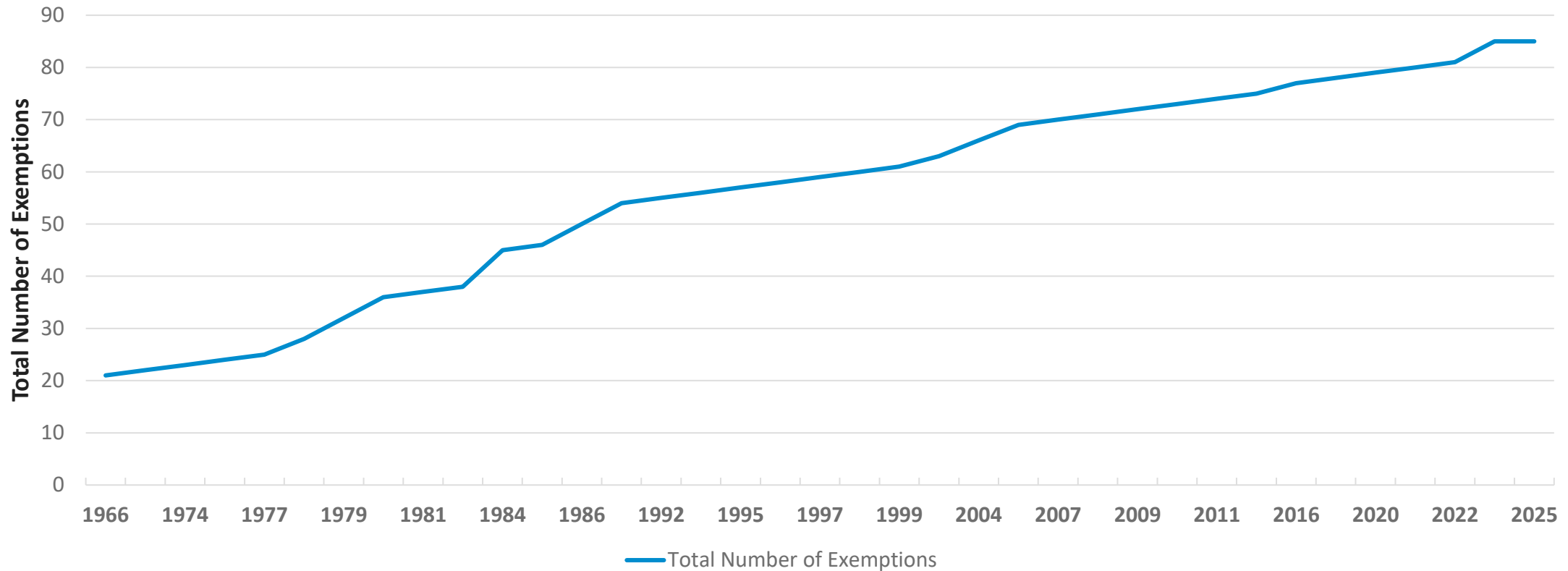
Divided into 8 Broad Categories

- ▶ Service exemptions:
 - ▶ Keeps the sales tax a tax on tangible personal property.
- ▶ Media-related exemptions:
 - ▶ Encourages the use of Virginia businesses.
- ▶ Medical-related exemptions:
 - ▶ Reduces cost of medical necessities.
- ▶ Nonprofit exemptions:
 - ▶ Reduces costs to those providing assistance to the community.

Number of Sales Tax Exemptions

- ▶ 21 of the current 82 exemptions were enacted in 1966.
- ▶ 11 exemptions (not including nonprofits) were enacted between 1966 and 1979.
- ▶ 22 were enacted in the 1980s.
- ▶ 8 were enacted in the 1990s.
- ▶ 10 were enacted in the 2000s.
- ▶ Since 2010, 13 exemptions have been enacted, and 3 have expired.
 - ▶ Multifuel heating stoves exemption sunset on July 1, 2012.
 - ▶ Catalog orders under \$100 sunset on July 1, 2013.
 - ▶ Donated educational materials sunset on July 1, 2022.

Number of Sales Tax Exemptions by Year: 1966-2025*



* Does not include the approximately 383 nonprofit entities separately listed and provided a sales tax exemption prior to July 1, 2004. Effective July 1, 2004, the exemptions were repealed and replaced with an administrative process allowing such nonprofits to receive a sales tax exemption.

Revenue Impact of Exemptions

- ▶ Most services are exempt from the Virginia Retail Sales and Use Tax.
- ▶ Cost of many exemptions is unknown because it is not reported to the Department.
 - ▶ Dealers report total exempt sales, without segregating exemptions by reason.
 - ▶ Purchasers are not required to report exempt purchases.
- ▶ Service exemption estimates are based on U.S. Economic Census Data.
 - ▶ This provides detail for more than 6,000 goods and services categories broken out by 18 industries.
 - ▶ About 380 service categories or subcategories were identified as potential areas of interest and selected by category-industry combination (i.e., NAPCS-NAICS code).

Personal Services: To Consumers & Businesses (B2C + B2B)

Total Revenue Estimates of Potential Taxable Categories (\$mil)¹
Effective July 1, 2025

Category	FY 2026 ²	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031
Admissions	102.9	117.0	122.0	127.2	132.6	138.2
Bowling	3.1	3.6	3.7	3.9	4.0	4.2
Carpet and Upholstery Cleaning	6.6	7.5	7.7	7.9	8.1	8.4
Delivery/Transportation Services	124.8	143.2	150.7	158.5	166.8	175.4
Funeral and Cemetery Services	21.2	23.9	24.8	25.7	26.6	27.5
Golf Courses and Country Clubs	37.0	42.1	43.9	45.8	47.7	49.7
Hairdressing, Nail Care, and Diet/Weight Reducing	64.3	73.1	76.2	79.4	82.7	86.2
Jewelry Repair	2.8	3.1	3.2	3.3	3.5	3.6
Dry Cleaning and Laundry	19.9	22.2	22.6	23.1	23.6	24.1
Marinas	2.1	2.4	2.5	2.6	2.8	2.9
Membership Fees/Dues	41.2	46.9	48.8	50.9	53.1	55.4
Motor Vehicle Repair (Including Detailing)	325.6	367.1	379.4	392.1	405.2	418.8
Parking Services	11.7	13.3	13.9	14.5	15.2	15.8
Pet Care Services	8.9	10.2	10.7	11.3	11.9	12.5
Selected Maintenance and Repair	103.9	117.5	121.8	126.3	131.0	135.9
Shoe Repair	0.3	0.3	0.4	0.4	0.4	0.4
Storage	27.8	31.3	32.4	33.5	34.7	35.9
Totals	904.1	1,024.8	1,064.8	1,106.5	1,149.8	1,194.9

¹ Revenue estimates are for all state funds, not just General Fund. The estimates are based on 2017 Economic Census data from the U.S. Census Bureau grown to the most recent year using various GDP category growth rates; The categories are projected to future fiscal years using growth rates consistent with the Official General Fund Revenue Forecast; Totals may vary slightly due to rounding.

² Adjusted for timing; Reflects 11 months of revenue.

Neighboring States

- ▶ Admissions, Dry Cleaning and Laundry Services, and labor related to Car Repair and Detailing are generally taxable across our neighboring states:
 - ▶ Taxable:
 - ▶ Kentucky, North Carolina, Tennessee, West Virginia, and the District of Columbia.
 - ▶ Exempt:
 - ▶ Virginia and Maryland.
- ▶ Transportation charges are widely exempt, whereas delivery charges are taxable in North Carolina and Tennessee.
- ▶ Hairdressing and Nailcare Services are widely exempt across our neighboring states.

Business Services: To Consumers & Businesses (B2C + B2B)

Total Revenue Estimates of Potential Taxable Categories (\$mil)¹
Effective July 1, 2025

Category	FY 2026 ²	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031
Advertising	672.6	752.1	770.9	790.1	809.9	830.1
Armored Car	3.9	4.4	4.5	4.7	4.8	5.0
Commercial Art and Graphic Design	27.2	30.9	32.3	33.8	35.3	36.9
Court Reporting	2.7	3.0	3.1	3.2	3.3	3.4
Credit Bureaus and Collections	66.2	75.8	79.5	83.5	87.6	92.0
Data Management	209.4	238.7	249.5	260.8	272.5	284.8
Employment and Staffing	609.6	696.2	728.9	763.1	798.9	836.3
Landscaping and Lawn Care	164.2	187.7	196.6	206.0	215.8	226.1
Maintenance and Janitorial	113.0	129.2	135.3	141.8	148.5	155.6
Painting and Wall Covering	39.9	45.6	47.8	50.0	52.4	54.9
Pest Exterminating and Inspection	31.3	35.7	37.4	39.2	41.1	43.1
Security and Investigation	99.4	113.6	119.0	124.6	130.6	136.8
Selected Consulting	773.6	866.8	890.2	914.3	939.1	964.5
Swimming Pool Maintenance	7.7	8.8	9.2	9.6	10.1	10.5
Taxi and Limousine	28.6	32.7	34.4	36.1	37.9	39.8
Telemarketing, Telephone Answering and Messaging Services	31.8	35.6	36.5	37.4	38.3	39.3
Travel Agents	82.5	93.7	97.6	101.6	105.8	110.2
Totals	2,963.4	3,350.4	3,472.7	3,599.8	3,732.0	3,869.3

¹ Revenue estimates are for all state funds, not just General Fund. The estimates are based on 2017 Economic Census data from the U.S. Census Bureau grown to the most recent year using various GDP category growth rates; The categories are projected to future fiscal years using growth rates consistent with the Official General Fund Revenue Forecast; Totals may vary slightly due to rounding.

² Adjusted for timing; Reflects 11 months of revenue.

Neighboring States

- ▶ Advertising, Staffing, Security, Landscaping, and Travel Agent Services are exempt in North Carolina and Tennessee.
 - ▶ These services are all taxable in West Virginia.
- ▶ Staffing, Security, and Landscaping are taxable in the District of Columbia while Travel Agent Services are exempt.
- ▶ West Virginia is the only neighboring state that taxes services rendered by travel agents.

Professional Services: To Consumers & Businesses (B2C + B2B)

Total Revenue Estimates of Potential Taxable Categories (\$mil)¹

Effective July 1, 2025

Category	FY 2026 ²	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031
Accounting	678.3	776.0	813.7	853.3	894.8	938.3
Architectural	82.8	94.7	99.2	104.0	109.0	114.3
Computer Services	2,004.5	2,274.1	2,364.9	2,459.3	2,557.5	2,659.7
Engineering	374.9	428.6	449.3	470.9	493.6	517.4
Health Care	3,264.3	3,736.7	3,921.0	4,114.5	4,317.4	4,530.4
Land Surveying	20.9	23.9	25.2	26.5	27.8	29.2
Legal	756.1	851.8	879.6	908.3	937.9	968.5
Veterinarians	90.0	103.3	108.6	114.1	120.0	126.1
Totals	7,271.8	8,289.1	8,661.5	9,050.9	9,458.1	9,883.9

¹ Revenue estimates are for all state funds, not just General Fund. The estimates are based on 2017 Economic Census data from the U.S. Census Bureau grown to the most recent year using various GDP category growth rates; The categories are projected to future fiscal years using growth rates consistent with the Official General Fund Revenue Forecast; Totals may vary slightly due to rounding.

² Adjusted for timing; Reflects 11 months of revenue.

Neighboring States

- ▶ Accounting, Engineering, Legal, and Healthcare Services are exempt in Virginia and all the neighboring states.
- ▶ Veterinarian Services are exempt in all our neighboring states, except for Kentucky. Small animal veterinarian services are taxable in Kentucky; however, large animal veterinarian services (such as those for horses) are exempt.
- ▶ Computer Services vary by state:
 - ▶ Taxable:
 - ▶ Kentucky, North Carolina, Tennessee, and the District of Columbia.
 - ▶ Exempt:
 - ▶ Maryland, Virginia, and West Virginia.

- ▶ Amounts separately charged for labor or services rendered in installing, applying, remodeling, or repairing property sold.
- ▶ Amounts separately charged for labor or services rendered in connection with the modification of prewritten computer programs.
- ▶ Custom computer programs.
- ▶ Amounts separately charged for 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 shop supply charge.
- ▶ Charges for accommodations furnished to transients for more than 90 continuous days by any place in which accommodations are regularly furnished to transients for consideration.

- ▶ Digital or electronic services are generally not taxable in Virginia.
 - ▶ Examples of digital services include:
 - ▶ Digital Downloads;
 - ▶ Streaming Services;
 - ▶ Website Hosting and Design;
 - ▶ Cloud-Based Services (including Software-as-a-Service and Data Storage Services).

- ▶ Digital Downloads include software, eBooks, music, and videos.
 - ▶ North Carolina, Tennessee, Kentucky, Maryland, and the District of Columbia all levy sales tax on digital downloads to some extent. Digital downloads are exempt in Virginia and West Virginia.

Estimated Fiscal Impact

Total Revenue Estimates of Potential Taxable Categories (\$mil)¹
Effective July 1, 2025

Category	FY 2026 ²	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031
Digital Downloads	73.8	90.0	99.4	109.4	120.2	130.9

¹ Revenue estimates are for all state funds, not just General Fund. The estimates are based primarily on Personal Consumption Expenditure (PCE) data from the U.S. Bureau of Economic Analysis (BEA) at the U.S. category level (i.e., software, eBooks, music, and videos). Virginia spending was estimated by applying Virginia's share of the population (~2.6%) to the U.S.-level estimates. Taxable spending was calculated by applying an estimated share representing e-commerce purchases of digital products – based on e-commerce sales by category from the Census Bureau with an adjustment to exclude tangible goods (based on secondary research).

² Adjusted for timing; Reflects 11 months of revenue.

- ▶ States that tax digital downloads typically do so by:
 - ▶ Broadening the existing retail sales tax definition of “tangible personal property” (TPP) to specifically include downloaded digital books, audio, and audiovisuals;
 - ▶ Alternatively, states may expand the definition of TPP to include property “in any other manner perceptible to the senses”;
 - ▶ Creating a new category of intangible property subject to Retail Sales and Use Tax that includes downloaded digital goods;
- ▶ Most states choose to create a new category of intangible property, as it is believed this method increases visibility and lessens the likelihood of ambiguity or taxpayer misunderstanding in its application.

- ▶ Streaming Services include any online provider of entertainment that delivers content over an internet connection to a subscriber's computer, TV, or mobile device (e.g. Netflix, Hulu, HBO, Disney, Spotify, and Apple TV+).
 - ▶ North Carolina, Tennessee, Maryland, West Virginia, Kentucky, and the District of Columbia levy tax on streaming services.
- ▶ Most states choose to tax streaming services under the Retail Sales and Use Tax.
 - ▶ Alternatively, it could be included under the Communication Sales and Use Tax, which has a narrower base, lower rate, and is collected by a much smaller group of dealers.

Retail Sales and Use Tax (RSUT)

Total Revenue Estimates of Potential Taxable Categories (\$mil)¹
Effective July 1, 2025

Category	FY 2026 ²	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031
Streaming Services	92.0	105.2	109.9	115.1	120.8	126.6

Communications Sales and Use Tax (CSUT)

Total Revenue Estimates of Potential Taxable Categories (\$mil)¹
Effective July 1, 2025

Category	FY 2026 ²	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031
Streaming Services	79.6	91.0	95.1	99.5	104.5	109.5

¹ Revenue estimates are for all state funds, not just General Fund. The estimates are based primarily on Personal Consumption Expenditure (PCE) data from the U.S. Bureau of Economic Analysis (BEA) at the U.S. category level (i.e., video and audio streaming services). Virginia spending was estimated by applying Virginia’s share of the population (~2.6%) to the U.S.-level estimates.

² Adjusted for timing; Reflects 11 months of revenue.

- ▶ Cloud-Based Services include Software-as-a-Service (SaaS) and data storage services, along with many others.
 - ▶ SaaS is a cloud computing model in which general or specialized software applications are hosted by a vendor or service provider and made available to customers over the internet.
 - ▶ Taxable in Tennessee, Maryland, West Virginia, Kentucky, and the District of Columbia;
 - ▶ Exempt in North Carolina and Virginia.
 - ▶ Data storage services is space in a data center on servers and equipment that can directly connect to the internet for online secure data backup.
 - ▶ Taxable in the District of Columbia;
 - ▶ Exempt in Virginia and other neighboring states.

- ▶ Definitional considerations are paramount when considering how to tax cloud-based services.
 - ▶ Options include taxing one or more broad categories of cloud-based services or any services that utilize the cloud to ensure a moderately broad reach.
 - ▶ Alternatively, Virginia could maximize the reach of the new tax by levying tax on all services that utilize the cloud and narrow the scope of the tax only through specific exemptions.
 - ▶ Some states that take a broad approach to taxing these services offer exemptions for data processing and informational services.

- ▶ Virginia uses origin-sourcing, but destination-sourcing is permitted in certain circumstances.
 - ▶ In the 2019 *Guidelines for Remote Sellers and Marketplace Facilitators*, Virginia expressly authorized marketplace facilitators accepting and processing orders to Virginia customers through a website or electronic application to use destination-based sourcing if unable to associate the order with a physical place of business in Virginia.
 - ▶ Sourcing the taxation of digital goods and services creates challenges because the seller may be out-of-state and the purchaser's location of use may be unknown or non-fixed.

- ▶ Sourcing approach taken by other states:
 - ▶ Maryland allows digital goods to be sourced to the origin if possible, or to the primary use address if known, or otherwise to the billing address of the purchaser.
 - ▶ Georgia allows digital goods to be sourced to the address where the goods are first used if no origin-sourcing or other destination-sourcing method is applicable.
 - ▶ North Carolina requires sourcing of digital goods to the seller's location, otherwise to the purchaser's location if received there, or alternatively to a known address of the purchaser.

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