

DEPARTMENT OF TAXATION

2022 Fiscal Impact Statement

1. **Patron** Christopher T. Head

3. **Committee** House Finance

4. **Title** Individual and Corporate Income Tax; Small
Business Tax Credit

2. **Bill Number** HB 332

House of Origin:

X **Introduced**

 Substitute

 Engrossed

Second House:

 In Committee

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would provide an individual and corporate income tax credit for eligible small businesses. The portion of the credit for individual income tax payers would be equal to the amount of Virginia income tax owed by a taxpayer on up to \$250,000 of personal income during such taxable year. The portion of the credit for corporate income taxpayers would be equal to the amount of Virginia income tax owed by a taxpayer during such taxable year on up to \$250,000 of the amount that is not deductible when computing federal tax due to Virginia's partial deconformity from the federal treatment of deductions related to COVID-19 business assistance programs. The credit would be subject to an aggregate credit cap of \$75 million per taxable year.

This bill would be effective for taxable years beginning on and after January 1, 2022, but before January 1, 2023.

This is Executive Legislation.

6. **Budget amendment necessary:** Yes.

Item(s): Page 1, Revenue Estimates
274 and 276, Department of Taxation

7. **Fiscal Impact Estimates are:** Preliminary. (See Line 8.)

7a. **Expenditure Impact:**

| <i>Fiscal Year</i> | <i>Dollars</i> | <i>Positions</i> | <i>Fund</i> |
|---------------------------|-----------------------|-------------------------|--------------------|
| 2022-23 | \$238,060 | 0 | GF |
| 2023-24 | \$94,596 | 1 | GF |
| 2024-25 | \$93,896 | 1 | GF |
| 2025-26 | \$95,896 | 1 | GF |
| 2026-27 | \$97,896 | 1 | GF |
| 2027-28 | \$99,896 | 1 | GF |

8. **Fiscal implications:**

Administrative Costs

This bill would result in administrative costs to the Department of Taxation ("the Department") in the amount equal to \$238,060 in FY 2023, \$94,596 in FY 2024, \$93,896 in FY 2025, \$95,896 in FY 2026, \$97,896 in FY 2027, and \$99,896 in FY 2028. Such costs would primarily consist of

updating the Department's systems to implement the new tax credit that would be provided by this bill and the salary of one FTE to handle compliance related to such credit.

Revenue Impact

This bill would have an overall negative General Fund revenue impact of up to \$75 million. It is unknown to what extent taxpayers will qualify for and claim this credit. In addition, it is uncertain to what extent taxpayers will actually claim credits in Fiscal Year 2023 or Fiscal Year 2024. This depends on whether taxpayers are calendar year filers or fiscal year filers, whether they file by the applicable return due date or on extension, and whether and to what extent they claim credits on an amended return. However, this is a one-time credit that is subject to a credit cap. Therefore, the negative revenue impact will be limited to an overall maximum of \$75 million.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: Yes.

This bill would tie the corporate income tax portion of the credit to the amount not deductible solely on account of Virginia's partial deconformity from the federal treatment of deductions related to COVID-19 business assistance programs including Paycheck Protection Program loans. It is the Department's understanding that this bill was not intended to address this issue. Therefore, we recommend a technical amendment

Page 1, Lines 29-31, after \$250,000
Strike: the remainder of that sentence
Insert: corporate income

As currently drafted, this bill would allow businesses that file as individuals (i.e., sole proprietorships) and corporations to qualify for the credit that this bill would provide. Although pass-through entities are mentioned elsewhere in the bill, the language providing the credit appears to exclude them because pass-through entities are not subject to taxation and cannot owe taxes. For other incentive programs, there is more standard language used for situations in which all types of business entities may qualify. If the intent of the Patron is to include businesses that are pass-through entities, we recommend the following technical amendment:

Page 1, Line 23
Strike: All of subsection B
Insert: For taxable years beginning on and after January 1, 2022, but before January 1, 2023, an eligible small business may claim a nonrefundable credit against the tax levied pursuant to §§ 58.1-320 and 58.1-400, equal to the amount of Virginia income tax owed on up to \$250,000 of income during such taxable year.

This bill would limit the corporate portion of the credit to businesses that are at least 51 percent independently owned and controlled by one or more individuals who are US citizens or legal resident aliens. This limitation may be subject to constitutional challenges as discriminating against foreign commerce and/or violating the Supremacy Clause.

11. Other comments:

Sunset Dates for Income Tax Credits and Sales Tax Exemptions

Section 3-5.14 of the 2021 Appropriation Act provides that any new sales tax exemption or tax credit enacted by the General Assembly after the 2019 Session, but prior to the 2024 Session, must have a sunset date of not later than June 30, 2025.

Proposed Legislation

This bill would provide an individual and corporate income tax credit for eligible small businesses. The portion of the credit for individual income tax payers would be equal to the amount of Virginia income tax owed by a taxpayer on up to \$250,000 of personal income during such taxable year. The portion of the credit for corporate income taxpayers would be equal to the amount of Virginia income tax owed by a taxpayer during such taxable year on up to \$250,000 of the amount that is not deductible when computing federal tax due to Virginia's partial deconformity from certain COVID-19 business assistance programs.

"Eligible small business" would be defined as a pass-through entity authorized to do business in Virginia that employs fewer than 50 employees and that has no more than \$10 million in gross receipts for the taxable year, a self-employed individual, who is subject to the Virginia individual income tax, or Virginia corporations that are at least 51 percent independently owned and controlled by one or more individuals who are United States citizens or legal resident aliens, that has no more than \$10 million in gross receipts during such taxable year, and that, together with affiliates, employs 50 or fewer employees.

The credit would be subject to an aggregate credit cap of \$75 million per taxable year. If the applications for such credits exceed \$75 million for any taxable year, the Department would be required to allocate the credits on a pro rata basis

No taxpayer would be permitted to claim credits in excess of their tax liability for a taxable year. Any unused credits would be permitted to be carried over for the next five taxable years, or until the total amount of the credit has been used, whichever is sooner.

The Department would be required to develop guidelines, exempt from the Administrative Process Act, implementing the tax credit.

This bill would be effective for taxable years beginning on and after January 1, 2022, but before January 1, 2023.

Similar Legislation

Senate Bill 540 is identical to this bill.

cc : Secretary of Finance

Date: 2/3/2022 JLOF
HB332F161