Advisory to the Media
January 12, 2004
Senator John H. Chichester

The Virginia Investment Act
Virginia - Ten Years and Beyond

Senator John Chichester released details today of tax reform legislation that he will sponsor to foster strategic investments in Virginia's future. The legislation, titled the Virginia Investment Act (VIA), is crafted to meet the following specific objectives:

- Honor prior promises for tax relief so future revenue growth is not obligated in advance, but can be used to address future needs;
- Put the transportation program back on the course envisioned in the 1986 special session;
- Regain structural balance in the budget to preserve the State's coveted Triple A bond rating;
- Make the tax code fairer;
- Begin to reduce pressure on local real estate taxes; and
- Invest strategically in priorities that have been neglected.

In presenting the legislation, Senator Chichester noted that the bottom line on proposed general tax actions, those related to **income, sales and car tax relief**, is essentially revenue neutral in FY 2006 (the first year that reflects 12 months of activity under the Act).

However, he quickly added that a bottom line of roughly $1.2 billion in additional general revenue offset by roughly $1.2 billion in additional tax relief does not mean that all taxpayers are affected the same. Some taxpayers will pay more, and some will pay less.

Tax Relief

A major premise of the Virginia Investment Act is that the obligation from prior promises must be shed in order to focus on the future. In explaining this objective, Senator Chichester said,

"If promises that have already been made are left unfunded, we are obligating future revenue before it is received, thereby crowding out funding choices that may need to be made down the road."

To avoid that consequence, VIA (1) provides **100% car tax relief in tax year 2005**, (2) **removes 2% of the sales tax on food in FY 2005**, and (3) **totally eliminates the estate tax by FY 2006**. Virtually all Virginians would benefit from one or more of these actions.

Localities would be reimbursed for 100% car tax relief through the dedication of 1½ cents of the current state sales tax, plus $230 million to produce $1.4 billion for car tax replacement in tax year 2005 -- roughly half a billion more than the current level of tax relief.

The dedicated revenue sharing for car tax replacement would be distributed to localities in the same proportion as car tax reimbursements are made in tax year 2004.

Another premise of the Virginia Investment Act is that certain inequities in the tax code can be remedied by having higher income filers pay slightly more and by eliminating tax loopholes.

In this regard, VIA will contain two new income tax brackets of 6.25% for taxable income between $100,000 - $150,000 and 6.50% for taxable income over $150,000.

Secondly, a means test will be applied to the tax preference that currently exists for those aged 62 and older. As Virginia income (not counting Social Security) rises above $64,000 for joint filers, the combined benefit of $24,000 for a couple 65 or older will be reduced dollar-for-dollar, and the phase-out is completed at income of

$88,000. For a single filer aged 65 or older, the current benefit will be phased down as income rises above $40,000, and the phase-out is completed at income of $52,000.

A similar means tested phase-out of the tax preference would occur for the $6,000 benefit that is available at age 62.

Effective January **2011**, the $12,000 benefit would be available to taxpayers when they reach normal federal (Social Security) retirement age rather than at age 65, and the $6,000 benefit would not be available for those who reach the age of 62 after January 1, 2011.

These measures will afford additional tax relief for Virginia families through the following:

- Increase personal exemption from $800 to $1,000;
- Increase standard deduction from $3,000 to $3,500 for single filers and from $5,000 to $7,000 for joint filers;
- Phase out low income tax credit as income rises marginally above the poverty level rather than eliminating all benefit at income $1 over the poverty level.

In addition, businesses will be provided relief from the requirement to accelerate the payment of sales tax collections.

Strategic Decisions

Another major goal of the Virginia Investment Act is to support strategic decisions that will affect Virginia's future. **Paramount among these is the preservation of Virginia's coveted Triple A bond rating.**

A necessary step in preserving the bond rating is to recapitalize the State's Rainy Day Fund. The VIA will require supplemental deposits of $60 million per year in the next biennium, and through budget language, will require that part of any revenue surplus be deposited into the Fund.

These actions, along with elimination of the planned withdrawal from the Fund in FY 2004, and the normal FY 2006 deposit will result in a balance of over half a billion by the end of the 2004-06 biennium.

A second step in regaining structural balance is to infuse the budget with $400 million per year to help offset the mismatch that occurs from projected revenue growth in the 5% range and 8-9% growth in the cost of Medicaid and SOQ re-benchmarking.

Beyond regaining structural balance in the budget**, other strategic decisions** supported by VIA include the adoption of well-thought-out and well-documented recommendations pertaining to public and higher education.

Specifically, the Virginia Investment Act starts to **reduce the pressure on local real estate taxes** by adopting selected JLARC and Board of Education recommendations that move part of the current SOQ cost from the local tax base to the state tax base.

Senator Chichester noted that the Board is on record with regard to the education standards – essentially, they are outdated because the SOQ doesn't reflect **existing** local practice that is required to offer a quality public education.

"By adopting Board recommendations to update the SOQ," Senator Chichester observed, "we simply are spreading an existing cost across a larger tax base than the local real estate tax base."

In addition to public education, the Virginia Investment Act supports recommendations of the Joint Subcommittee on Higher Education Funding Policies to begin picking up a larger share of higher education base operating costs, so that **rising tuition costs can be curbed**.

Senator Chichester noted,

"**A vibrant higher education system is crucial to growing jobs and the Virginia economy**. We must find a way to make the system affordable for all Virginians and to reduce the incentive for Virginia colleges to favor out-of-state students over Virginians.

Making strategic investments to position us for a better tomorrow always carries a price tag, even though we sometimes try to ignore that fact. **The VIA asks all Virginians to pay 1 percent more in sales tax on non-food purchases so that we can remove 2 percent of the sales tax on essential food purchases, and so we can make the strategic decisions necessary to protect our Triple A bond rating and invest in public and higher education**."

User Taxes and Fees

Transportation

Senator Chichester noted that the last component of the Virginia Investment Act, and perhaps the **most important to Virginia's continued economic vitality, is a major overhaul of user taxes and fees for transportation**.

The Virginia Investment Act re-aligns tax sources **to ensure that taxes dedicated to transportation are those that have a direct link with transportation needs**, and **brings taxes which have not been changed in years up-to-date,** producing a net increase of $725 million per year for transportation.

Senator Chichester said, "There is no escaping the fact that those of us who use the roadways will be asked to pay more to sustain that infrastructure . . . but where is there a clearer example of what a user charge was meant to do?"

Senator Chichester went on to observe that the General Assembly took a bold step in 1986 to provide ongoing road construction funds for Virginia.

"Unfortunately" he said, "inflation has undercut that effort, and all of the funds generated through 1986 actions soon will go to road maintenance rather than to road construction. Thus, another bold step is needed to **build on the momentum** that the General Assembly started in 1986. Transportation user fees must be updated to keep the construction program on track."

Under the VIA, the cost to own and operate a vehicle will increase by a little over 1 percent, or about $107 per year. Included in this amount is roughly $35 more per vehicle that the average taxpayer will pay in sales tax on fuel; however, it will enable him to get back twice as much in car tax relief.

Specifically, the VIA:

- Increases the fuel excise tax to 20.5 cents per gallon.
    - The price remains below that of most neighboring states.
- Updates the motor vehicle titling tax from 3.0% to the 5.5% level of general sales tax, but allows trade-in value to be deducted before applying the new tax rate.
- Applies the general sales tax to fuel purchases (before excise taxes are added) so the ½ cent sales tax on non-fuel purchases can be returned to the GF for car tax relief.
    - Exchanges the ½ cent sales tax on non-fuel purchases for other taxes that have a more direct link with transportation needs.
        (1) Existing automobile insurance premium tax;
        (2) Real estate deed recording tax (30 cent increase) with funds going to transportation in FY 2007)*;
    - The exchange of ½ cent general sales tax ($475 million) for automobile insurance premium tax ($119 million) produces a net difference of $356 million that can be returned to the GF to satisfy the car tax obligation.
- Increases the motor vehicle registration fee by $10.00, and dedicates the entire increase to transportation.

*For two years, the $60 million increase from real estate deed recording tax will be used to make supplemental deposits to Rainy Day Fund.

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Senator Chichester closed by saying that he cannot provide a precise scorecard on how many taxpayers will pay less and how many will pay more under the Virginia Investment Act. But, he offered several examples to give a sense of how the VIA will play out.

Under the VIA, a 3-person family with income **just above the poverty level** will pay an estimated **$376 less** in general taxes (**income, sales & car tax relief**) and about $107 more per vehicle operated.

A 3-person family with **$30,000 income** will pay **$258 less** in general taxes and $107 more per vehicle operated.

A 3-person family with **$90,000 income** will pay **$92 less** in general taxes and $107 more per vehicle operated.

A 4-person family with **$175,000 income** will pay **$278 more** in general taxes and $107 more per vehicle operated.

A 4-person family with **$250,000 income** will pay **$898 more** in general taxes and $107 more per vehicle operated.

A retired couple, **both over 65, with $60,000 income** will pay **$129 less** in general taxes and $107 more per vehicle operated.

A retired couple, **both over 65, with $100,000 income** will pay **$821 more** in general taxes and $107 more per vehicle operated.

- However, this retired couple still enjoys a tax preference of over $20,000 from exclusion of Social Security income and a double personal exemption.

- A younger couple with the same income would pay $4,718 in taxes, versus $3,425 for the couple over 65; therefore, the **value of remaining tax preference is $1,293**.

Tobacco Tax

In conjunction with the Virginia Investment Act, Senator Chichester also will sponsor legislation that increases the user tax on tobacco-related products. Senator Chichester noted that state revenue from the tobacco tax increase will support the VIA objective of regaining structural balance in the budget and preserving the State's Tripe A bond rating.

Specifically, the legislation will provide $224 million per year to apply toward the growth of Medicaid costs.

Senator Chichester, in observing that the cigarette tax is the lowest in the nation and that it has not changed in almost 40 years said,

"The cost of the State's Medicaid program continues to climb, and the logical nexus to help address cost increases is a user fee on products that are known to increase health care costs. States all around the nation have taken this step, and the frail elderly who reside in Virginia's nursing homes deserve no less in protecting the essential services they receive."

Under the proposed legislation, the state cigarette tax will be increased from 2.5 cents per pack to 35 cents per pack, and the combined State and local cigarette tax will be capped at 90 cents. Counties will be given the same authority as cities to impose the local tax, in five increments, starting in July 2005. Finally, a 10% excise tax will be placed on other tobacco products at the wholesale level.

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In closing, Senator Chichester noted that those who pay slightly more in taxes -- be it from general taxes or from user taxes and fees associated with transportation and tobacco -- will be the judge of whether the price is worth it to:

- Deliver on promises made, including getting rid of the annual bill on cars valued up to $20,000;
- Improve the road system;
- Improve the fairness of the tax code; and
- Invest strategically for the future.

Specific details of the Virginia Investment Act and the tobacco tax legislation are attached.