

DEPARTMENT OF TAXATION

2010 Fiscal Impact Statement

1. **Patron** Harry R. Purkey

3. **Committee** House Appropriations

4. **Title** Income Tax: Conformity with Internal Revenue Code

2. **Bill Number** HB 614

House of Origin:

 Introduced

 X **Substitute**

 Engrossed

Second House:

 In Committee

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would advance Virginia's date of conformity to the Internal Revenue Code (IRC) from December 31, 2008 to December 31, 2009. Virginia would continue to disallow most bonus depreciation, and any five year carry-back of certain net operating losses (NOL) allowed for NOLs generated in taxable years 2001 or 2002.

This bill would also disallow the tax deductions related to applicable high yield discount obligations and the ratable deferral of cancellation of debt income allowed under the American Reinvestment and Recovery Act (ARRA) of 2009.

This bill contains an emergency clause and would be in force from its passage.

6. **Fiscal Impact Estimates are:** Final. (See Line 8.)

6b. **Revenue Impact:**

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Fund</i>
2009-10	\$0	GF
2010-11	(\$30 Million)	GF
2011-12	(\$30 Million)	GF
2012-13	(\$30 Million)	GF
2013-14	(\$30 Million)	GF
2014-15	(\$30 Million)	GF
2015-16	(\$30 Million)	GF

7. **Budget amendment necessary:** Yes.

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8. Fiscal implications:

Administrative Costs

TAX considers implementation of this bill as routine, and does not require additional funding.

Revenue Impact

The Introduced Executive Budget assumes the passage of this bill and deconformity from the deduction allowed for domestic productions activities. Therefore, there is no fiscal impact from federal tax laws passed during 2009, as well as the deconformity from additional federal provisions. However, as this bill conforms to the deduction for domestic production activities under § 199 of the IRC, unlike what was assumed in the Introduced Executive Budget, this bill will have a negative revenue impact of \$30 million per year.

The following amounts attributable to conformity with the ARRA are incorporated into the Introduced Executive Budget for this bill:

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Fund</i>
2009-10	(\$14.72 Million)	GF
2010-11	(\$6.37 Million)	GF
2011-12	\$2.07 Million	GF
2012-13	\$1.65 Million	GF
2013-14	\$0.06 Million	GF
2014-15	(\$1.44 Million)	GF
2015-16	(\$1.13 Million)	GF

This bill would avoid the impact of two provisions in the ARRA – the discount on applicable high yield discount obligations and the cancellation of debt provision. Deconforming from these provisions eliminates a loss of \$99.39 million in FY 2010 and \$38.47 million in FY 2011 in General Fund revenue.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Current Law

Virginia's conformity to the IRC is currently fixed to the IRC as it existed on December 31, 2008. Since that date, Congress has enacted one significant measure that would affect income taxation in Virginia:

- The American Recovery and Reinvestment Act of 2009, which provides a variety of monetary provisions for states and localities to help improve the economy and tax relief for individuals and families.

Unless the date of IRC conformity is advanced, none of the provisions of this Act will flow through to Virginia taxable income. Because federal adjusted gross income (individuals) and federal taxable income (corporations) are the starting point for Virginia tax returns, if this bill is not enacted, Virginia taxpayers would be required to make complex “Fixed-Date Conformity” adjustments to remove the changes made by this Act when they prepare their Virginia tax returns.

Federal Law

In 2009, the American Recovery and Reinvestment Act (ARRA) was enacted. This legislation provides a variety of monetary provisions for states and localities to help improve the economy and tax relief for individuals and families. Among the significant tax provisions was a temporary increase in the earned income tax credit for 2009 and 2010 and an extension of the temporary increase in the expensing of certain business assets.

ARRA also added IRC § 108(i). This section allows deferral of cancellation of debt income realized in connection with a reacquisition of business debt at a discount after December 31, 2008 and before January 1, 2011. Such income is then recognized ratably over the five-year tax period beginning in the fifth taxable year following a 2009 reacquisition and in the fourth taxable year following a 2010 reacquisition.

In addition, ARRA established a provision under IRC § 163(e)(5)(F) that suspends the application of the applicable high yield debt obligation (AHYDO) rules for certain debts issued after September 30, 2008 and before January 1, 2010. Under this provision corporate and certain partnership debt that would have otherwise created deferred or non-deductible interest will be provided immediate tax deductions under general interest deductibility principles.

Proposed Legislation

This bill would advance Virginia’s date of conformity to the Internal Revenue Code (IRC) from December 31, 2008 to December 31, 2009 and incorporate most changes contained in the ARRA. Virginia would continue to disallow most bonus depreciation, and any five year carry-back of certain net operating losses (NOL) allowed for NOLs generated in taxable years 2001 or 2002.

In addition, this bill would deconform from the following provisions:

- IRC § 108(i), relating to the ratable deferral of cancellation of debt income; and
- IRC § 163(e)(5)(f), relating to the tax deductions related to applicable high yield discount obligations.

This bill contains an emergency clause and would be in force from its passage.

Similar Bills

Senate Bill 545 is identical to this bill.

cc : Secretary of Finance

Date: 2/12/2010 TG
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