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THE REVENUE RESOURCES AND ECONOMIC COMMISSION

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and

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REVENUE RESOURCES AND ECONOMIC COMMISSION

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Richmond, Virginia

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Virginia Beach, Virginia

Lester E. Schlitz
Portsmouth, Virginia

Carrington Williams, Vice-Chairman
Fairfax, Virginia

Staff Members

From Department of Taxation:

Barry E. Lipman
Nancy D. Beistel
Robert T. Benton
John A. Garka

From Division of Legislative Services:
E. M. Miller, Jr.
Jill M. Pope

From Division of State Planning and Community Affairs:

Robert J. Griffis
Richard D. Brown
Sue A. Dawson
William P. Dickinson
Gail V. Tatum

Special Consultants on Taxation of Motor Vehicular Rolling Stock

Charles J. Gallagher
Virginia Commonwealth University

George E. Hoffer
Virginia Commonwealth University

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Introduction

The Revenue Resources and Economic Commission became a permanent legislative commission by act of the 1974 General Assembly. The commission was established to study the Commonwealth's tax structure and sources of revenue, to evaluate local revenue sources, and to recommend the proper division of sources of revenue between the state and local governments.

The major area of concern for the commission in 1974 has been real property tax reform. During its 1973 session, the General Assembly assigned the Governor's Office the responsibility for an in-depth study of this tax. The result was Reforming the Virginia Property Tax, a report made available to the General Assembly in 1974. This study examined the following seven topics:

(1) the assessment-sales ratio study,

(2) the roles of the state and local governments in property tax administration,

(3) property tax review and appeal procedures,

(4) property tax exemption and relief policies,

(5) assessment and taxation of public service corporation property,

(6) Virginia's constitutional debt limits for localities based on property assessments, and

(7) constitutional and statutory limitations on property tax reform.

The final recommendations emerging from this study have come under intensive review by the Revenue Resources and Economic Commission. In order to solicit citizen input, the commission sponsored in Richmond an educational seminar on property tax reform as well as public hearings in Richmond, Roanoke, Norfolk, and Alexandria. Utilizing public comment and staff research, the commission has formulated a set of property tax reform recommendations for consideration by the 1975 General Assembly. Chief

among these are measures to promote public understanding of the property tax and to improve the quality of appraisal and assessment functions. In addition, the commission recommends further study of review and appeal procedures as well as general property tax relief. Details of these recommendations are contained in Part I of this report.

The commission has also concerned itself with other fiscal issues such as:

(1) changes in the inheritance and gift taxes,

(2) exclusion of retirement income from the state personal income tax,

(3) elimination of the dividend exclusion from the state personal income tax,

(4) changes in the taxation of rolling stock of motor carriers, and

(5) tax relief for the disabled.

In October, a hearing was held in Richmond at which public comment was invited on these and other tax issues aside from the property tax. The commission's recommendations on these issues are contained in Part II of this report.

Recommendations

The Revenue Resources and Economic Commission recommends the following measures for legislative action by the 1975 General Assembly. (Proposed legislation is contained in the Appendix.)

Property Tax Reform

(1) All localities shall be required to assess at 100 percent of fair market value and to proportionately lower their nominal tax rates beginning January 1, 1976. Public service corporation property, currently assessed under the provisions of the Bemiss Bill (Section 58-512.1 of the Code of Virginia), will be assessed and taxed as a separate class of property until 1986.

(2) Each assessor shall enter the fair market value on the property record card and calculate the assessment from that figure.

(3) Each taxpayer shall have the right to examine the property record card for his or any other properties and to see the calculations upon which his own appraisal and assessment are based.

(4) Notification shall be given to taxpayers whenever an assessment is changed. The notice shall include the new appraised value of the property, the new assessment, and the local ratio upon which the assessment is based.

(5) A locality may require the submission of annual exemption applications, giving information on current property use and ownership, as a condition for retention of tax exempt status.

(6) Localities shall inventory all properties exempt or immune from inclusion in the taxable base (other than roads, streets, or highways) and report such properties on the land book with a general identifying description of the property, name and address of owner, fair market value appraisal, and the assessment and the tax as if the property were not exempt.

(7) The Department of Taxation shall be required by law to prepare assessment-sales ratio studies on an annual rather than biennial basis. Further, all localities shall classify the properties in their land books using classes developed by the Department of Taxation in cooperation with appropriate local officials.

(8) The Department of Taxation shall develop and administer a mandatory training program for state and local assessment personnel.

Other Tax Issues

(1) The rolling stock tax on intrastate common carriers of property shall be repealed. In its place, such vehicles will become subject to the local personal property tax along with other carriers of property. This change would redress the dual, discriminatory system presently used.

(2) A temporary ceiling shall be placed on all local license tax rates to preclude further increases in the inequity of local license taxation while study continues. This ceiling shall not allow tax rates to increase over the rates in effect on December 31, 1974 and shall last until December 31, 1976. This restriction will allow the Commission additional time to analyze the issues and to finalize its recommendations to the 1976 session of the General Assembly.

Part I: Property Tax Reform

The real property tax is the largest single source of revenue for localities in Virginia, accounting for approximately 45 percent of their locally raised revenue. Certain localities rely on the tax more heavily than others with its significance varying from 29 percent to 82 percent of locally raised revenues. In rural areas where commerce and industry are not a large segment of the tax base, the real property tax plays an especially important role. Because of this importance its retention seems assured. Therefore, our comments emphasize remedial efforts to make the present tax a more equitably administered one.

For the 1975 session of the General Assembly, the commission has attempted to pinpoint those recommendations in the Governor's Property Tax Reform Study which would promote taxpayer understanding, improve the quality of appraisal and assessment functions, improve assessment review and appeals procedures, and provide property tax relief.

Promote Taxpayer Understanding

The best method of assuring equitable property taxation is the promotion of widespread public understanding of property assessments. Unless the public is informed of the assessment ratio in use and the manner in which it is applied, an individual property owner will have difficulty relating the amount of his assessment to the value of his property. It is even more difficult for him to make the adjustments necessary to compare his assessment with those of other properties. This problem is often compounded by the fact that many assessors apply the ratio mentally and never formally decide on the full value of a piece of property. Thus, even if a property owner gains access to his property card, he is no nearer to the full appraisal put on his property.

If local assessments were made at 100 percent of appraised value, the taxpayer would be in a better position to identify an incorrect assessment and to insist upon equitable treatment. For this reason, the commission recommends that all localities be required by statute to assess at 100 percent of appraised value beginning January 1, 1976. Assurance of adherence to this requirement could be tested annually by the assessment-sales ratio study conducted by the Department of Taxation. Technically, it would not be necessary for the local ratio to register exactly 100 percent as measured by this study. This is especially true for those localities that do not assess on an annual basis since their ratio of assessments to sales' prices will decline over the assessment cycle until the next general reassessment.

The move to full value assessments will increase the property tax base of almost every locality in the state. To prevent this adjustment from becoming a tax burden on citizens of the Commonwealth, the commission also recommends that during 1976 each locality be required to lower its stated tax rate on real property in proportion to the increase in its assessment ratio. For example, a jurisdiction using a 1975 assessment ratio of 50 percent, as measured by the sales ratio study, would be required to halve its stated tax rate with the change to a 100 percent ratio in 1976. Thus, if the locality taxed at a rate of $2.00 per $100 of assessed valuation for 1975, it would initially adjust its rate to $1.00 per $100 of appriased value at the beginning of 1976. Afterwards, if the locality desired to raise taxes, it would be able to do so by expressing the increase in terms of the $1.00 rate applicable to 100 percent assessment.

In making this recommendation, the commission realizes that the lower nominal rates produced by 100 percent assessment would subsequently be applied to that portion of public service property now assessed under provisions of the Bemiss Act (Section 58-512.1 of the Code of Virginia). This Section provides for a gradually decreasing fraction of public service

corporation property to be assessed at 40 percent until 1986 when all public service property will be assessed at the prevailing local ratio. Thus, to avoid loss of local revenue from the application of a lower tax rate to that portion of public service property assessed at 40 percent or to prevent the loss of revenues to some localities with repeal of Section 58-512.1, the commission further recommends that public service corporation property assessed under the Bemiss Act be assessed and taxed as a different class of property until 1986. At that time the assessment ratio between public service and other types of property will be equalized at 100 percent. In the opinion of the Attorney General, this could be accomplished by legislation similar to that contained in a bill attached to the appendix of this report. (See Appendix Exhibits 1 and 12 for proposed legislation and Attorney General's opinion, pages 93 and 114.)

Example: To show how the mechanics of this recommendation would work, assume that a given locality in 1975 is assessing real estate at a 20 percent assessment ratio and levying a tax equal to $5.00 per $100 of assessed valuation. Under these conditions, the effective tax rate (the nominal tax rate times the local assessment ratio) for locally assessed properties is $1.00 per $100 of appraised value. For public service corporation property assessed at 40 percent, the effective tax rate is equal to $2.00 per $100 of full value as shown below.

1975 Tax Year

Local and Public Service Corporation Properties Assessed at 20 Percent of Full Value		Public Service Corporation Properties Assessed At 40 Percent of Full Value Under the Bemiss Act	
Nominal Tax Rate	Effective Tax Rate ($5.00 X 20%)	Nominal Tax Rate	Effective Tax Rate ($5.00 X 40%)
$5.00 per $100 of assessed valuation	$1.00 per $100 of full value	$5.00 per $100 of assessed valuation	$2.00 per $100 of full value

Under the Commission's recommendation, the locality in question would be required to move to 100 percent assessment as of January 1, 1976. To do this, it would raise its assessment ratio by a factor of five from 20 percent to 100 percent and reduce its nominal rate proportionately from $5.00 to $1.00. Initially, this would set the 1976 nominal tax rate at $1.00 per $100 of assessed valuation or exactly equal to the 1975 local effective rate as shown above. For public service corporation property assessed at 40 percent, however, a nominal rate of $1.00 would result in a 1976 effective rate of $.40 per $100 of full value or a reduction of $1.60 from the 1975 effective rate of $2.00 per $100 of full value. To prevent this reduction, these properties would be treated as a separate class for tax purposes with the tax rate frozen at the 1975 nominal rate. In terms of the example, this means that public service corporation property assessed at 40 percent would represent a separate class of property to be taxed at a rate of $5.00 per $100 of assessed value. This in turn would result in a 1976 effective tax rate for these properties equal to $2.00 per $100 of full value, the same as the effective rate for 1975.

1976 Tax Year

Local and Public Service Corporation Properties Assessed at 100 Percent of Full Value		Public Service Corporation Properties Assessed At 40 Percent of Full Value Under the Bemiss Act	
Nominal Tax Rate	Effective Tax Rate ($1.00 X 100%)	Nominal Tax Rate	Effective Tax Rate ($5.00 X 40%)
$1.00 per $100 of assessed valuation	$1.00 per $100 of full value	$5.00 per $100 of assessed valuation	$2.00 per $100 of full value

As shown above, therefore, the effective rate of property taxation remains unchanged after the shift to 100 percent assessment. The only difference in the two procedures is that the locality will use one nominal tax rate for 1975 while for 1976 it will use two nominal rates (one for properties assessed at 100 percent and one for public service properties assessed at 40 percent). Moreover, since public service corporation property assessed at 40 percent is to be taxed at the 1975 nominal rate, the difference between the effective rates on the two classes of property remains unchanged. This discrepency, however, will disappear with completion of the Bemiss Act adjustment in 1986. Until that time,

> the Commission feels that the nominal rate on that portion of public service corporation property currently assessed at 40 percent should be frozen at the 1975 rate. Only in those cases where the local effective rate on properties assessed at 100 percent exceeds the effective rate for public service corporation property assessed at 40 percent should the nominal rate for public service corporation property be altered. If this occurs, the latter rate should be raised only to the point where the effective rates for the two classes of property are equal.

Full disclosure of information to promote public understanding of the property tax also necessitates legislative passage of a requirement that local assessors enter the fair market appraisal on property record cards and calculate the assessment from that figure. Furthermore, any taxpayer should have the right by law to examine the property record card for his or any other properties he may wish to compare and to see the working papers or calculations upon which his own assessment is based. In conjunction with these measures, there should also be a requirement that notification be given to taxpayers whenever an assessment is changed. This provision was partially assured by enactment of Senate Bill No. 147 (Section 58-792.01 of the Code of Virginia) which required a mailed notice of any change in assessment. To strengthen this legislation, however, the commission feels the notice of assessment changes should also include the new appraised value of the property as well as the local ratio upon which the new assessment is based. In addition, it should be stipulated that the notification of assessment changes be mailed directly to property owners. (Proposed legislation incorporating these provisions is included in the Appendix of this report, pages 96, 97, 98, and 99.)

The amount of property taxes collected in a locality depends upon the size of its tax base and its effective tax rate. While the public may be aware of changes in tax rates, it is usually less aware of changes in the size of the property tax base.

Governments have traditionally exempted particular properties from taxation with the intent of encouraging certain uses of land, relieving the property tax burden for various classes of taxpayers, reducing the regressivity of the property tax, etc. As additional parcels are exempted (i.e., as the tax base is eroded), the burden on owners of taxable properties increases. The owners of these taxable properties pay in full for the relief given owners of tax-exempt properties.

Although Virginia has consistently maintained a conservative attitude toward real property exemptions, by 1973 the total value of exempt properties (including governmental holdings) for the state had reached an estimated $11 billion or 18 percent of total real property value. Revenue losses from these exempt properties were estimated to total more than $137 million in 1972.

In order to more fully monitor the effect of exemption practices and to systematize procedures for granting exemptions, the commission proposes legislation that would (a) require localities to inventory all properties exempt or immune from inclusion in the taxable base and (b) allow localities to require the submission of annual applications as a condition for retention of tax exempt status. (See proposed legislation, pages 100 and 101.)

Improve the Quality of Appraisal and Assessment Functions

Assessment-Sales Ratio Study

The commission has found that if assessments are poorly made in the first place, no amount of review and adjustment will correct them. A first step in insuring high quality technical work is the development of a measure of the accuracy of assessments. Since 1962, the Department of Taxation has prepared biennial assessment-sales ratio studies to show the actual, overall ratio of real property tax assessments to sales and the resultant overall effective tax rate in each locality.

With the 1973 assessment-sales ratio study now under way, the department has begun to perform the study annually rather than biennially. This step will help relieve inequities caused in the past by the time lags between studies. For instance, if a county had raised its assessment ratio in early 1974, the biennial approach would not recognize the change until the 1975 study was published in 1977. This lag would affect the assessment of public service corporation property and the distribution of state school aid funds. Therefore, the commission feels that annual rather than biennial assessment-sales ratio studies are needed and that they should be required by statute rather than be left to the discretion of the Department of Taxation. (Proposed legislation is included in Appendix Exhibit 7, pages 102 and 103.)

In 1971 and 1973 the department has made an effort to improve the statistical quality of the study by increasing sample sizes, giving more thorough instructions to field men, and screening unusual sales. A further and major improvement would be to develop the overall assessment ratio by weighting the median ratios in each class of property with the amount of assessed valuation in that class. This currently is not possible because most local land books are not classified, and there is no uniform system of classification generally accepted throughout the state. Therefore, the commission has instructed the Department of Taxation, in cooperation with local commissioners of the revenue and assessors, to develop a classification system of real property for inclusion on local land books. The number of classes developed will probably fall between the five currently used by the department (residential single family, residential multi-family, agricultural, commercial-industrial, and public service corporation) and the thirteen recommended in the Governor's Property Tax Reform Study (residential improved,

residential unimproved, apartment, agricultural improved, agricultural unimproved, commercial improved, commercial unimproved, industrial improved, industrial unimproved, horticultural, open space, forest, and public service corporations). Of course there would be no restrictions on any additional classifications a locality might wish to compile for its own purposes. (Proposed legislation is included in Appendix Exhibit 8, page 104.)

A third concern about the quality of assessment-sales ratio studies was brought up in the public hearings on the property tax held by the commission. Several people felt that the sales price of many properties was inflated by such items as the value of personal property and changes for credit reports, surveys, appraisals, inspections, title examinations, title insurance policies, title recordation, attorneys' services, processing services imposed by lending institutions, and other settlement services. These citizens believed that such amounts were often erroneously included in the figure used for recordation tax purposes. Since recordation tax receipts are the source of sales data for the ratio study, such a practice would obviously affect its accuracy. While the commission accepts the findings of the Governor's Property Tax Reform Study that there is no evidence of consistent overstatement of value, the commission is concerned about these charges and recommends more careful administration by filing attorneys and clerks of the court.

Assessment Cycle

Virginia law currently requires periodic reassessment of real property at a minimum of every four years in cities and every six years in counties. Provision is made for adjustments and additions resulting from division of parcels, zoning changes, and new construction between reassessment periods but not for changes in value demonstrated by sales.

The four and six year reassessment cycle is unrealistically long in view of present inflation levels and changing patterns of property values. Certain areas of Virginia are experiencing rapid economic growth which is reflected by increasing property values, while other areas are stagnant or declining with adverse effects on values. As a result, increasing disparity and inequity have developed in property valuation among and within taxing jurisdictions. This problem is compounded by the fact that public service corporation properties, mineral lands, and personal property are assessed on an annual basis in all jurisdictions. In addition, several jurisdictions, primarily the larger urban areas, have professional staffs and assess property on an annual or continuous basis.

In addressing this issue, the Governor's Property Tax Reform Study recommended that all jurisdictions be required to move to an annual assessment program following their next periodic reassessment. Recognizing that it would be difficult as well as costly for some localities to move rapidly to annual assessment, the study recommended that computer-assisted mass appraisal be investigated with consideration of substantial state financial assistance.

In reviewing this recommendation, the Revenue Resources and Economic Commission not only recognizes the inequities inherent in long reassessment cycles but also expresses concern about the substantial costs of rapid movement to annual assessment programs. In attempting to deal with these concerns, the commission recommends no legislative action at this time but urges that within the next six years all localities move to a reassessment cycle not exceeding three years and thereafter work toward annual reassessments.

Training of Assessment Personnel

Recognizing the importance of well trained assessment personnel and the strong link between trained assessment personnel and an equitable administration of the property tax, the Revenue Resources and Economic Commission recommends establishment of a mandatory training program for all assessment personnel in Virginia. The commission deferred action on proposals to establish a system of certification for appraisers and to establish a program of incentive pay to assessors exceeding basic requirements. In response to a request from the commission, the Department of Taxation has prepared the following course outline and cost estimates for this training program.

Course Outline

The wide differences in professional training and skill among Virginia's assessors and the differing requirements throughout the various localities of the Commonwealth appear to suggest implementation of a dual approach to the training program. The department recommends that there be a two level program of instruction, the first a basic program geared to fundamentals with the second aimed at the more experienced assessor. The first program would be for personnel who have had little or no formal training in the assessment field and would begin by stressing basic principles while evolving into an intermediate level program. The second program would emphasize certain specialized and more technical areas of the assessment profession. In addition, this second program could be designed to meet all of the requirements for full certification by the International Association of Assessing Officers (IAAO). By meeting the standards for full accreditation by the IAAO, this program could lead to the designation of Certified Assessment Evaluator (CAE), which indicates full professional qualification.

The Basic Program

The basic program would be aimed at meeting the needs of beginning appraisers and those persons who maintain assessments between general reassessments. The format would be a five day school (Monday - Friday) of instruction and discussion that would improve the basic knowledge of Virginia's assessors. The following is a partial list of the major topics to be covered:

(1) classification of real estate and buildings;

(2) development of square foot rates to value;

(3) constitutional, statutory, and case law provisions concerning assessments;

(4) special assessment plans (e.g., land use, etc.);

(5) basic elements of the three approaches to value (the income, market, and replacement cost approaches);

(6) proper methods of maintaining equity in assessments between general reassessments; and

(7) special regional assessment topics, etc.

The program would be conducted by the Department of Taxation with the instructors coming from department personnel, commissioners of the revenue, local assessing officers, and outside experts. To direct the training program a position of Supervisor of Instruction would be created in the Division of Real Estate Appraisal and Mapping. This person would be a competent appraiser whose primary responsibility would be to plan, organize, and conduct these courses and to represent the department in all educational activities in the property tax field. When not occupied in the training program, this person would be available to commissioners of the revenue and other local assessing officers to assist them with unusual assessment problems.

In order to make use of existing facilities, increase the convenience to the participants, and hold class size to manageable limits, the department recommends that this basic course be held in centrally located facilities provided by several community colleges and universities around the Commonwealth. It can reasonably be assumed that total attendance for this course would be about 150. An equal distribution among seven locations would result in a class size of approximately 20 to 25 participants at each location.

An examination of the schedules of the commissioners of the revenue, who are expected to make up a large percentage of the enrollment, indicates that September and October would be the preferred time for this program. The department recommends, therefore, that the first session begin in the second week in September and continue each week until completion. The program would extend over approximately two months.

The course would use standard texts and reference material, for example the IAAO's The Assessing and Appraisal Process. The IAAO has a large amount of instructional material that would be valuable for distribution to the assessors to help them in performing their jobs. Upon completion of the program, the participant would be issued a certificate indicating the participant's active role in the educational process.

The Commonwealth, through the Department of Taxation, would fully fund this program including outlays for travel, food, and lodging for employees of state and local governments in Virginia who attend. Others who wish to attend this program would be allowed to do so but would be required to pay a fee designed to cover their pro rata share of the cost of instruction, supplies, and facilities.

An estimate of the cost of this program for fiscal year 1975-76 is given below.

Supervisor of Instruction		
Salary	$15,000	
Expenses	5,000	
Expenses of Participants		$20,000
150 students at $28.00 per diem (5 days per student)	21,000	
		21,000
Outside Instruction		
Fees and expenses	3,000	
		3,000
Other Instruction Costs		
In-house personnel expenses	3,000	
Teaching aids, supplies and texts	5,000	
		8,000
	Total	$52,000

If funded, this program can begin in September, 1975.

The Advanced Program

The second part of this continuing education program would be for assessment personnel who have had a background in assessment courses and who have had some exposure to IAAO/VAAO (Virginia Association of Assessing Officers) course materials.

This advanced program could best be implemented by expanding and funding the Virginia Assessor's Institute, which is now sponsored by the VAAO and the Institute of Government of the University of Virginia. The present Virginia Assessor's Institute has an annual course program for increasing the professional capacity of advanced assessors. This program

would be expanded to meet all of the requirements for full certification by the IAAO. These standards along with accreditation by the IAAO could lead to the CAE degree, indicating full professional qualification. There are several IAAO certified instructors among the local assessing officers in Virginia who could teach the course.

The program's courses would follow an IAAO approved program and would deal with specialized topics. Traditionally, this program has taken place in the latter part of June, and there seems no reason to modify this time frame. The Supervisor of Instruction would be responsible for the development of the program in consultation with the appropriate authorities of the Institute of Government, VAAO, and IAAO.

As with the basic program, the advanced program would be fully funded by the Commonwealth through the Department of Taxation. Travel, food, and lodging expenses of participants who are employees of state and local governments in Virginia would be paid by the department. Others who desire to attend would be permitted to do so but would be required to pay a fee designed to cover their pro rata cost of instruction, materials, books, etc.

An estimate of the cost of this program for fiscal year 1975-76 is given below.

Cost of Instructors	$ 2,500
Expenses for Instructors	2,000
Expenses for Students	
150 students at $40.00 per diem (5 days per student)	30,000
Instructional Material and Supplies	4,000
Institute of Government	
(mailings, Newcomb Hall fee, and secretarial assistance)	4,500
	$43,000

Because of the preparation needed to implement the course, the first session would begin in June, 1976.

Cost of Programs

The total cost of both the basic program and the advanced program would be $95,000 in fiscal year 1975-76. The department estimates the cost of the program would increase by approximately seven percent per annum over the next few years, mainly due to inflation. Thus, the program would cost approximately $102,000 in fiscal year 1976-77 and $109,000 in fiscal year 1977-78 or a total of $211,000 in the 1976-78 biennium.

There is a possibility that the federal government would fund a part of the cost of this program under the Intergovernmental Personnel Act (IPA), which is currently administered by the State Division of Personnel.

The above proposal differs in some areas from the program prepared by the Jacobs Company for the Governor's Property Tax Reform Study. The higher cost of the Jacobs' program in the second and third year is mainly due to a more intensive training program and its higher estimate of enrollment. The lower cost of the Jacobs' program in the fourth and following years is due to the decrease in the level of training in its program. In contrast, the cost of the department's program would not decrease because it would be a continuing education program. The Department believes that a continuing education program is important, especially if there is a possibility of requiring certification within the next few years.

Appraisal of Public Service Corporation Property

The State Corporation Commission presently appraises public service corporation property on the basis of original cost less depreciation except for land which is appraised at current market value. This procedure was reviewed by consultants to the Governor's Property Tax Reform Study who found the methodology to be effective as it is applied in Virginia. In making this observation, however, the consultants felt that the system

might be strengthened by the use of additional appraisal techniques such as the unit valuation approach. In addition to depreciated cost, the unit value method incorporates income capitalization plus stock and debt value to arrive at appraisal value. Passage of Senate Bill 398 would allow the implementation of this method in Virginia.

The Revenue Resources and Economic Commission has examined the possibility of using alternative methodologies to appraise public service corporations. However, the commission finds that the unit valuation approach often involves subjective judgments in selecting income capitalization rates and in compensating for market fluctuations in the value of stock and debt. In addition, the commission questions the applicability of the unit value method to Virginia since it calculates full value for property tax purposes by appraising each company as a going concern. Such an appraisal would include the franchise value of the concern which is currently segregated for taxation by the state. If adopted, therefore, the unit value method could raise constitutional problems in that it subjects the franchise component of public service corporations to double taxation. For these reasons, the commission cannot concur in the consultants' recommendation. In its view, the cost-less-depreciation approach currently used by the State Corporation Commission produces stable and reliable results and should not be changed.

Improve Assessment Review and Appeal Procedures

The procedure for review and appeal of property tax assessments is as important as any facet of property tax administration. Currently in Virginia, an aggrieved taxpayer is afforded three avenues of appeal. He may first appeal to the local assessing body and then to the local equalization board. Finally, if still not satisfied, he may appeal his case to the circuit court.

The first step in the review process, a hearing before the local assessing body, is provided for by Section 58-792.01 of the Code of Virginia. This section requires assessing officers to send a notice to each taxpayer whose property is revalued, informing him of changes and of his right to appeal his assessment. In the past a large percentage of property owners never received the required notification because the addresses in the land book applicable to their properties were those of mortgage or finance companies which administered their mortgages and received their tax bills. However, the 1974 General Assembly required such companies to forward notification to the property owner.

Once the land book is prepared, property values can be changed only by an equalization board or a court. Equalization boards are usually appointed by the local circuit court at the request of the governing body. Unfortunately, members of these boards are frequently unfamiliar with appraisal technique and property values throughout the locality. Because of the inequitable assessment patterns often set by such boards, governing bodies have been reluctant to establish them.

Where equalization boards do not exist, the taxpayer must take his case directly to the circuit court. This course of action is expensive as well as time consuming, frequently requiring extensive expert testimony and legal documentation.

The commission feels a more effective review and appeal procedure would promote equitable treatment among property owners, better understanding and acceptance of assessments, and consistent administration throughout the state. Because of these considerations, the commission wishes to study further proposals to establish permanent local boards of assessment review and a state board of assessment appeal. The composition

of the boards, the responsibilities assigned to them, and their relationship to the courts and other state agencies must be defined before legislation can be introduced.

Measures for Property Tax Relief

At its public hearings, the commission heard two main areas of concern: rising tax burdens and unresponsive state and local government. Spokesmen for several groups expressed a desire that the General Assembly address the question of immediate property tax relief before considering long-term administrative reform. The fear was voiced that reform might be a back-door approach to higher taxes.

There are various programs for property tax relief which operate at the state or local levels. "Circuit breaker" plans are provided in a number of states to give property tax relief through state funding. These programs range from those that provide almost nominal relief to a limited number of senior citizen homeowners to those that cover households with incomes up to $15,000 without regard to age or whether the qualified household owns or rents. A typical "circuit breaker" plan for elderly homeowners was proposed and defeated at the 1974 session of the Virginia General Assembly. House Bill No. 807 required that the eligible homeowner be at least sixty-five, have income of no more than $5,000, and have a net worth of no more than $20,000, exclusive of his home. The maximum relief provided would have been $275. A companion proposal, House Bill No. 800, provided the same relief for elderly renters with the same stipulations on income and net worth. All relief would have been funded by the state government. The annual cost of the two bills would have been approximately $7.5 million.

In considering "circuit breaker" proposals, the method of extending relief (i.e. tax credits, direct payments, or both) is as important as the amount of relief offered. Because of the possible combinations, the commission wishes to review further the proposals in this area to determine program costs as well as the nature and number of beneficiaries.

An alternative to the circuit breaker approach is a switch to non-property taxes. Two measures currently under study by the commission are the Indiana and Iowa plans which limit the property tax through use of a local income tax. These programs are outlined below.

As an interim measure, the commission favors the requirement of public hearings during the local budgetary process to explain increases in assessments without proportionate decreases in the property tax rate. Such a measure is not intended to limit the right of local governments to increase tax collections but rather to assure taxpayer awareness of these increases.

Local Income Tax Alternatives

Although the income tax is a major source of revenue to localities in ten states, at the present time it is not available to local governments in Virginia. Eventhough the advantages or disadvantages of local income taxes have often been considered, the standard discussion has usually been on a general level while the features of existing local income taxes vary widely. In contrast to this approach, the commission is examining the specific plans that two states have enacted to combine a local income tax with the property tax. These are Indiana's "CAGIT" (County Adjusted Gross Income Tax) plan and Iowa's school foundation program plan.

The Indiana Plan

In July, 1973, Indiana implemented a program that attempts to provide

counties an alternate source of revenue to finance governmental services at the local level, while at the same time attempting to lower their reliance on the property tax. This CAGIT program allows counties on a local option basis to impose a local income tax on adjusted gross income at one of three resident rates: 0.5 percent, 0.75 percent, and 1 percent. Nonresidents who work in a locality that imposes the tax are subject to a 0.25 percent rate on their adjusted gross income derived from that locality. If both home and work counties impose the tax, then the taxpayer is subject only to the tax levied by his home locality. The base of the local option income tax is the same as the state base. This conformity allows both bases to be collected by the Indiana Department of Revenue. The Indiana individual income tax rate is a flat two percent of adjusted gross income.

The purpose of this local option income tax was not only to give counties an alternative source of revenue, but also to allow localities to grant a significant amount of property tax relief without decreasing local governmental services. Depending upon the tax rate adopted, the locality must apply a specific percentage of its income tax revenue to property tax relief while the remainder is placed in the locality's general fund. Because part of the revenue from the local option income tax is used for the general fund, actual revenues to the locality would tend to increase over time.

The CAGIT plan limits a CAGIT locality's total property tax revenues to the 1973 amount minus the property tax replacement credit, (i.e., the amount of CAGIT revenue required to be used for property tax relief). Thus, as revenue from the local income tax increases, property tax collections must decline. It should be noted that the effective rate of the property tax will decrease over time because total property tax collections will decline even as assessed values rise to reflect

increased market value. The localities that choose not to adopt CAGIT have their total tax rate frozen to the 1973 level. This would not, however, place a limit on total collections; although the tax rate is frozen, the assessments are not.

The schedule and percentage of CAGIT revenues that must be used for property tax relief are shown below.

Year and rate	Percent of CAGIT revenue used for property tax relief
First year	
0.5% rate	50
0.75% rate	66 2/3
1.0% rate	75
Second year	
1.5% rate	50
1.75% rate	31 1/3
1.0% rate	50
Third and all subsequent years	
1.5% rate	50
0.75% rate	33 1/3
1.0% rate	25

As of July 1, 1974, a total of 36 of Indiana's 92 counties had adopted the local income tax plan. Counties that wish to adopt the tax or to increase the existing rate of tax may do so only if the local county council so acts prior to April 1 of that year.

An additional feature of Indiana's new tax package is that revenue from

an increased state sales and use tax is being used to finance a Property Tax Relief Fund.[1/] This fund is used to reimburse all localities for a 20 percent credit allowed against local taxpayers' property tax liabilities. A taxpayer's tax liability is defined as the property tax payable in a given year plus the amount by which the tax due has been reduced because of the application of county adjusted gross income tax revenues or federal revenue sharing funds to the extent such funds were included in the determination of the total county tax levy for the tax year.

The Iowa Plan

The Iowa plan for decreasing the reliance on the property tax takes a slightly different approach, but the general concept is the same as for Indiana. A local option income tax is made available to school districts to increase the quality of the educational facilities and is an alternative to increasing property taxes.

The Iowa state school foundation program enacted in 1971 allows school districts to levy each year, for the school general fund, a foundation property tax of $.54 per one hundred dollars of assessed valuation on all taxable property in the district. Besides the foundation property tax levy, the district can levy an additional school district property tax. The districts are also entitled to receive state aid equal to the difference between the amount of foundation property tax collected in the district and the district cost or the state foundation base, whichever is less.

1/ Indiana increased their sales and use tax rate from 2 percent to 4 percent in May, 1973. At the same time, Indiana exempted food products for home consumption from the tax base.

If a school board wishes to spend more than is permitted under this law, the board in an effort to increase the level of education may hold a referendum on whether or not to finance the excess costs by a school district income surtax of a specified rate. If the higher budget and income surtax are not approved by the voters, the school board must reduce its proposed expenditures.

The surtax rate is determined by dividing the excess amount needed by the total amount of state individual income tax collected in the district. The quotient is the surtax rate to be imposed on the state individual income tax.

Future Plans

In the coming year the commission plans to look into these local income tax alternatives and to examine the merits and disadvantages of each. The examination will hopefully determine whether these types of proposals could be instituted in the Commonwealth.

Part II: Other Revenue Issues

Although the Revenue Resources and Economic Commission spent a great deal of time analyzing the property tax, the commission still considered a number of other important revenue issues. The following section contains the recommendations of the commission to the General Assembly on these other revenue issues. These recommendations are not listed in any order of priority, but are simply presented along with supplementary background material and analysis. The next section examines a number of alternative revenue sources that could be utilized to meet any unanticipated revenue demands. The final section presents the issues that the commission will study in the coming year.

Recommendations

Treatment of Retirement Income

The Present Law

Currently, retired persons and their surviving spouses receive individual income tax relief by having a certain portion of their retirement benefits excluded from taxation. Prior to 1974, the exclusions were as follows:

1. The first $2,000 of retirement benefits received by civil service retirees and the first $1,000 received by surviving spouses of civil service retirees (after cost recovery).

2. The first $2,000 of retirement benefits received by military retirees and the first $1,000 of benefits received by the surviving spouses of military retirees (with no cost recovery and an age sixty restriction on both exclusions).

3. That portion of the first $2,000 of retirement benefits, other than civil service and military retirement benefits, that exceeds social security benefits for persons age sixty-five or over (after cost recovery).

4. Total exclusion of Virginia Supplemental Retirement System (VSRS) benefits to retirees and surviving spouses (after cost recovery).

Legislation approved at the 1974 session of the General Assembly expanded these provisions somewhat but at the same time restricted relief to lower and middle income retirees (see Senate Bill No. 57, which is Chapter 682, 1974 Acts of Assembly). The current law provides the following retirement income exclusions:

1. A $3,000 exclusion for civil service retirees and $1,500 for their surviving spouses (after cost recovery).
2. A $2,000 exclusion for military retirees age sixty and over and a $1,500 exclusion for their surviving spouses (with no age restriction for surviving spouses and no cost recovery provision for either group).
3. A $2,000 exclusion for retirees from private industry and a $1,000 exclusion for their surviving spouses (after cost recovery).

All of these exclusions are to be reduced by the amount that adjusted gross income (AGI) exceeds $12,000. Benefits received by VSRS retirees and survivors remain totally excludable.

It is apparent that there is a lack of uniformity in the treatment accorded the various classes of annuitants by the current law. While military and private retirees receive the same maximum exclusions of $2,000, the maximum permissable exclusion for civil service retirees is $3,000, or 50 percent greater. The following example demonstrates how the notion of horizontal equity is violated by current law.[1/] Consider four single men over age sixty (but less than sixty-five) each with retirement income of $10,000, with itemized deductions of $2,000, and a personal exemption of $600. Based on the present rate schedule,

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[1/] Horizontal equity refers to that portion of the generally accepted "ability to pay" theory of taxation that calls for individuals with the same income to pay the same tax.

their state income tax liability would be as follows:

Retiree	Virginia Income Tax Liability
Federal civil service	$102
Military	140
Private industry	140
VSRS	None

Similarly, a lack of uniformity is apparent in the treatment of surviving spouses. The survivors of military and civil service retirees each receive maximum exclusions of $1,500, but surviving spouses of retirees from the private sector only receive a maximum of $1,000. A further disparity exists in that military retirees must have attained the age of sixty to be eligible for relief while no such restriction is placed on the other classes of annuitants.

The Retirement Income Credit Concept of Relief

In order to eliminate some of the existing inequities and to promote further conformity to the federal tax structure, the Revenue Resources and Economic Commission recommends that the present retirement income exclusion concept of tax relief be replaced by the retirement income tax credit concept adopted by the federal government. The federal retirement income credit dates back to 1954, when Congress enacted it as a part of major tax reform legislation. Prior to 1954, social security and railroad retirement benefits had been fully tax exempt; however, benefits received from other retirement programs had been fully taxable once cost recovery stages were exhausted.[1/]

1/ Joseph A. Pechman, Federal Tax Policy, (Washington: The Brookings Institution, September, 1966), pp. 85-86.

The objective of the credit was to provide comparable tax relief for those with social security and railroad retirement benefits and those with income from other retirement plans. To achieve this goal, Congress took two steps. First, it set the base of the credit at an amount equal to the maximum social security benefits payable in 1954 subject to reduction by actual social security or railroad retirement benefits paid to the individual. A further reduction for retirees under age seventy-five was to be made if earned income exceeded the amount that social security regulations had set as the limit for meeting the requirements of its test of retirement. The earned income restriction was not applicable after the individual reached age seventy-five, once again conforming to social security treatment. For individuals under the age of sixty-five, retirement income was defined as any pension or annuity income (other than military pension income) received from public retirement systems. For retirees age sixty-five and over, retirement income included any taxable pension or annuity and income from interest, dividends, and rents. If it did not exceed maximum social security benefits after the downward adjustments, retirement income became the base for the credit. As the second step, Congress decided that the actual tax relief provided by the credit would be at the marginal rate applicable to the first $2,000 of taxable income.

In 1954, the first bracket rate was 20 percent, maximum social security benefits were $1,200, and the earned income restriction was $900. Since 1954, the credit has been modified several times. Shortly after the credit was adopted, retirement income was redefined for individuals under age sixty-five to include military pensions. In 1956, the earned income restriction was increased from $900 to $1,200 and eliminated

after the individual reached age seventy-two instead of age seventy-five. These changes were the direct result of similar changes in social security regulations that were enacted in 1954 but after the tax reform legislation had already been passed by Congress. The base of the retirement income credit was increased in 1962 from $1,200 to $1,524, the maximum social security benefits payable at that time. In 1965, when federal tax rates were reduced, the credit was also reduced from 20 to 15 percent so that relief would be at the average of the marginal rates applicable to the first $2,000 of taxable income. Included in the same bill that reduced the credit were provisions to increase by 50 percent the maximum credit base for married taxpayers who file joint returns. This increase was intended to compensate for the 50 percent supplementary social security received by a husband on behalf of his wife.[1] In recent years maximum social security benefits have exceeded $1,524, and the earned income restriction for recipients of these benefits is now $2,400; however, Congress has made no other revisions to the federal retirement income credit to reflect these changes.

Tax Relief in Other States

When compared to the income tax relief granted to retirees in neighboring states, Virginia's current provisions are generally more generous. North Carolina and Kentucky both offer partial exclusions, and only West Virginia extends more relief than the Commonwealth. West Virginia taxpayers who are age sixty-five and over receive a

[1] Joseph A. Pechman, Federal Tax Policy, pp. 86-87.

$4,000 exclusion for retirement benefits from any source and a total exclusion for state pensions. Maryland also utilizes the retirement income exclusion concept of tax relief, but it bases the exclusion on the annual statewide average of social security and railroad retirement benefits paid to persons age sixty-five and over. The maximum exclusion is then reduced by actual social security or railroad retirement payments that the individual has received during the year. Thus, the Maryland exclusion is much the same as the base of the federal retirement income credit.

Several other states also provide income tax relief patterned after the federal retirement income credit. They include California, Indiana, and Oregon. It is worth noting that although these three states use the same base for the credit as used for federal tax purposes, they offer only a portion of the federal relief by basing their credit on their state individual income tax rates. California limits the tax credit to 1 percent of the credit base instead of the 15 percent granted by the federal government. A 1 percent credit is consistent with the California rate schedule, since the first $2,000 of California taxable income is subject to that rate. Indiana grants a state retirement income credit equal to two-fifteenths of the allowable federal credit. Two-fifteenths is equivalent to relief at a tax rate of 2 percent, which is the flat state individual income tax rate in Indiana.

Oregon applies a variation of the federal concept. A retirement income credit equal to 25 percent of the permissable federal credit may be claimed. This amount is also consistent with the notion that relief should be granted at the first bracket rate, since the first $500 of Oregon taxable income is subject to a 4 percent tax rate. In addition to the credit, retirees receive a variety of exclusions but

with a number of restrictions placed on eligibility for them. Payments received by retirees from the Oregon public retirement fund are totally excludable.

The Equity and Revenue Impact of the Credit Concept for Virginia

Using either the exclusion concept or the credit concept of tax relief may be viewed as a "tax expenditure," for that decision is no different from the decision to create a government program designed to provide financial assistance to retired taxpayers. While the government program would explicitly appear on the expenditure side, the tax expenditure does not appear anywhere and is therefore subject to far less scrutiny from policymakers and the general public. Furthermore, the tax expenditure does not grant relief to persons with too little income to file a tax return; the program could be specifically designed to aid that group. Finally, either type of relief reduces the revenues available for other functions in the same manner that budgetary outlays for the government program would.[1] Recently more and better data have become available indicating that relief granted by the current retirement income exclusions will cost the state from $9 to $12 million per year in individual income tax revenues, or $4 to $5 million more than the relief under the old law.[2] Any application of the federal retirement income credit to Virginia would reduce substantially the revenues

1/ Edward M. Fried, Alice M. Rivlin, Charles L. Schultze, and Nancy H. Teeters, Setting National Priorities: The 1974 Budget (Washington: The Brookings Institution, 1973), pp. 49-57.

2/ When the General Assembly passed Senate Bill No. 57, the Department of Taxation indicated that on the basis of limited information the modifications in the exclusions would not change individual income tax revenues. Since that time improved data have been acquired from the Social Security Administration, the Internal Revenue Service, the Civil Service Commission, and the Department of Defense. All revenue estimates in this section rely on these recently acquired statistics.

lost by the state. If Virginia were to adopt the full federal retirement income credit, the annual cost is estimated at approximately $4 million, or less than half the current cost.[1] If only a portion of the credit were adopted, the cost would be a proportional part of $4 million (i.e., 75 percent of the credit would cost $3 million, 50 percent of the credit would cost $2 million, and so on).

The credit concept would increase the equity of the tax relief granted to retirees. As mentioned earlier, the notion of horizontal equity is clearly violated by the current law in that retirees with equal retirement income must pay different amounts of tax. The concept of vertical equity also continues to be violated, although the current law did improve the previous treatment by imposing an income constraint on tax relief.[2] Without a concrete provision for actual social security or railroad retirement payments received by the individual as part of the eligibility requirements for relief, some retirees could be receiving larger amounts of nontaxable income than others. In addition, the current law does not prohibit individuals with more than one kind of pension from claiming more than one exclusion. The progressive nature of the individual income tax rate schedule compounds the vertical equity problem since a retiree whose total income places him in one of the higher marginal brackets receives more relief than one who is in a lower bracket. Finally, the current law is discriminatory against military retirees, since they are the only class of retirees upon whom an

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1/ Estimates of the cost of the retirement income credit for Virginia are based on an Internal Revenue Service sample of federal individual income tax returns filed by Virginians for the 1970 and 1972 tax years. Excessive sampling variability within AGI classes was noted in some instances.

2/ Vertical equity is the other half of the ability-to-pay theory of taxation and means that persons with higher incomes should pay a higher tax.

age constraint is placed.

Table 1 shows several alternative applications of the credit concept and their effects on the various classes of retirees. The table assumes retirement income of $5,000, which includes social security benefits up to $1,300, for each of the four retiree classes. Option 1 assumes that Virginia would permit retirees to claim the full federal retirement income credit against their state income tax liability. Options 2 through 5 assume that only a portion of the federal credit would be granted at the state level. For each of the options, the amount of the credit could not exceed the retiree's actual Virginia individual income tax liability. This constraint conforms to the federal limitation when the credit exceeds the tax liability.

Since federal civil service employees do not contribute to the social security system as part of their retirement plan, three assumptions are made about them in Table 1. The first is that civil service retirees receive no social security benefits. The second is that civil service retirees receive the minimum social security benefit payable because of limited employment outside the federal government. The final one is that federal civil service retirees receive the same social security payments as the other classes of retirees because of extensive outside employment. Given these three alternative sets of circumstances, Table 1 demonstrates how the federal credit concept would equalize relief. The greatest tax relief would go to those retirees who receive little or no social security benefits. The same tax relief would be granted to all retirees when social security payments are equivalent.

In any case, all retirees would receive up to $1,524 of nontaxable income, whether it is social security benefits or pension and annuity income. Since the base of the credit would be the same no matter what

TABLE 1--A COMPARISON OF THE EFFECTS OF VARIOUS APPLICATIONS OF THE FEDERAL RETIREMENT INCOME CREDIT TO CURRENT PROVISIONS FOR INCOME TAX RELIEF TO RETIREES[a]

Retiree	Tax Liability Without Exclusion or Credit	Current Law--Exclusion Concept[b]		Alternative Proportions of the Federal Retirement Income Credit Applied to Virginia[c]									
				Option 1		Option 2		Option 3		Option 4		Option 5	
		Income Tax Relief	Income Tax Liability	Relief	Liability	Relief	Liability	Relief	Liability	Relief	Liability	Relief	Liability
Federal Civil Service													
With no social security benefits	$42.00	$42.00	$ 0	$42.00[d]	$ 0	$42.00[d]	$ 0	$42.00[d]	$ 0	$42.00[d]	$ 0	$30.40	$11.60
With minimum social security benefits	19.50	19.50	0	19.50[d]	0	19.50[d]	0	19.50[d]	0	11.97	7.53	7.96	11.54
With same social security benefits as other sectors	16.00	16.00	0	16.00[d]	0	16.00[d]	0	16.00[d]	0	6.72	9.28	4.47	11.53
Military	16.00	16.00	0	16.00[d]	0	16.00[d]	0	16.00[d]	0	6.72	9.28	4.47	11.53
Private Industry	16.00	16.00	0	16.00[d]	0	16.00[d]	0	16.00[d]	0	6.72	9.28	4.47	11.53
VSRS	16.00	16.00	0	16.00[d]	0	16.00[d]	0	16.00[d]	0	6.72	9.28	4.47	11.53

a/ Assumes each retiree is single and age 65 or over. Each claims the minimum standard deduction of $1,300, the $600 personal exemption, and the $1,000 exemption for age. All retirees have total income of $5,000, which includes social security benefits of $1,300. As further alternatives, federal civil service retirees are assumed to receive either no social security benefits or the current minimum benefit of $1,125.

b/ Senate Bill No. 57, passed by the 1974 General Assembly.

c/

Option:	Assumes Virginia would adopt:	Equivalent to relief at a state income tax rate of:	Maximum credit available:
1	Full federal retirement income credit	15.0 %	$228.60
2	75% of Option 1	11.25%	171.45
3	50% of Option 1	7.5 %	114.30
4	20% of Option 1	3.0 %	45.72
5	13.3% of Option 1	2.0 %	30.40

d/ Actual computations yield a credit that is greater than state income tax liability. Federal provisions, however, require that the credit be limited to the amount of tax liability if it is smaller than the credit. It is assumed that Virginia would extend the same treatment.

portion of the federal credit were adopted, there would be a restoration of horizontal equity to tax relief. Enhancing vertical equity would be a reduction in the amount of the credit as social security and railroad retirement payments increase, elimination of the potential to claim more than one exclusion, and an inability to take advantage of the progressive rate schedule.

Adoption of any portion of the federal credit would eliminate the age discrimination in the current law. On the other hand, relief would increase as age advances because of the progressive decline and final disappearance of earned income restrictions and because of the federal definitions of retirement income for individuals under age sixty-five that limit relief to those with pension or annuity income from public retirement systems (i.e., federal, state, local, and military retirees).

While each of the options presented in Table 1 would either maintain or reduce for most retirees the amount of relief currently available, the relief granted by Options 1, 2, and 3 would be at rates equivalent to more than the maximum Virginia individual income tax rate of 5.75 percent. Only Option 5, which would provide relief at the 2 percent rate imposed between $0 and $3,000 of state taxable income, is consistent with the treatment at the federal level and in the three credit states.

Reform of the Federal Retirement Income Credit

The House Ways and Means Committee has recently considered various tax reform proposals. One of these measures would restructure the present federal retirement income credit and convert it to a tax credit for the elderly.[1] The proposed credit would be available to all

[1] Joint Committee on Internal Revenue Taxation, Tax Reform Bill of 1974, Tentative Decisions of the Ways and Means Committee Corresponding to Sections of Draft Bill, (Washington: U. S. Government Printing Office, November 18, 1974), p. 3.

taxpayers age sixty-five or over regardless of whether they receive retirement income (pensions, annuities, interest, dividends, rents) or earned income. Individuals under age sixty-five would also qualify for the credit if they received public retirement pensions.

The committee has tentatively decided the maximum base of the credit should be increased to $2,500 for single persons who are age sixty-five and over and for married couples who file joint returns but with only one spouse who is age sixty-five or over. Married couples who have both reached age sixty-five would receive a credit based on a maximum amount of $3,750. The present law provides single taxpayers a credit based on a maximum amount of $1,524; married taxpayers receive a credit based on a maximum amount of $2,286 when only one spouse receives retirement income or based on up to $3,048 when both receive retirement income.

The credit base is currently limited to the amount of retirement income if that amount is less than the maximum credit base after subtracting social security or railroad retirement payments and making the earned income adjustments. The restructured provisions would continue to require that the maximum credit base be reduced by actual social security or railroad retirement payments to the individual. However, the constraint on earned income that is imposed by the present law would be replaced with an income phaseout designed to limit relief to low and middle income elderly taxpayers. For single persons, the phaseout would reduce the credit base by $1 for every $2 of AGI in excess of $7,500. For married couples, the credit base would be reduced in the same manner when AGI exceeds $10,000.

If these provisions are enacted by Congress, it is obvious that benefits to some retirees would be increased, and relief would be

extended to some individuals who do not currently qualify for the retirement income credit. There are not sufficient data available to estimate how much the current average credit would increase or to determine the size of the enlarged sector that would qualify for the proposed credit. Therefore, it is difficult to estimate the revenue impact of the proposed provisions.

Conclusion

The commission recommends that the federal retirement income credit concept of tax relief be adopted in Virginia. Such a concept would bring more horizontal and vertical equity to the relief granted retirees. Moreover, under current federal provisions the cost of the relief could be reduced from its current level by percentages ranging from about 50 percent under Option 1 to about 95 percent under Option 5.

Rolling Stock Taxation

Background

The rolling stock of motor carriers of property in the Commonwealth is taxed ad valorem in one of two ways - through a state administered and collected rolling stock tax or through a locally administered and collected personal property tax.

Sections 58-618 to 58-626.1 of the Code of Virginia provide for a rolling stock tax of one dollar per hundred dollars of assessed value on intrastate common carriers in lieu of local personal property taxes. Proceeds from this State Corporation Commission (SCC) administered tax are prorated to the localities based on the mileage traveled over regular routes by each subject carrier.[1/] In 1973, there were sixteen

[1/] Data limitations prevent the inclusion of miles traveled over irregular routes.

motor carriers operating under intrastate common carrier freight certificates; these carriers paid $100,258 in rolling stock taxes.[1/] The owners of all other trucks, whether in for-hire or private use, are subject to personal property taxes, which are administered and collected in the locality of domicile.

The rolling stock tax recently has come under criticism from several sources. Some truckers assert that it constitutes differential treatment for one class of motor carriers, the intrastate common carrier. Fueling the charge of differential treatment is the procedure whereby most intrastate common carriers operate under more than one authority. For example, if a motor carrier operates under an intrastate common carrier certificate, then the entire fleet of that firm is exempt from local personal property taxes and subject to the rolling stock tax. This situation could exist even though only a very small portion of the carrier's total operation may be as an intrastate common carrier. These critics argue that if the fleets of the intrastate common firms were subject to the local personal property taxes, the tax bill of these firms would be higher; therefore, the intrastate common carriers enjoy a competitive advantage.

Criticism also comes from some commissioners of revenue. These commissioners feel that the rolling stock tax is preempting them from a source of revenue and that repeal of this tax in favor of local property taxes would increase local revenues. Finally, the SCC views the tax with disfavor. Since the tax yielded only about $100,000 in 1973, several parties within the SCC view it as a nuisance.

1/ "A Statement of Rolling Stock and Taxes for the Year 1973 for Motor Vehicle Carriers," State Corporation Commission, Commonwealth of Virginia, 1973.

Investigating these criticisms, the Revenue Resources and Economic Study Commission employed two consultants in 1973 to examine the relative merits of the rolling stock tax and the personal property tax as a means of taxing the rolling stock of motor carriers of property.[1] The study was commissioned to investigate the equity and efficiency of the present dual system.

The consultants found weaknesses in the present system. Significant differences were found to exist across the state in the assessment and collection of personal property taxes on motor carriers of property. While urban areas generally used fixed depreciation schedules in assessing rolling stock, rural areas used a variety of assessment methods. Some commissioners of revenue indicated that they used no specific schedule but rather negotiated assessments or relied on published data. Some of these data proved to be nonexistent. Consequently, assessment of rolling stock varies significantly throughout the Commonwealth.

Many local commissioners of revenue complained that staff size precluded their determining what rolling stock was actually domiciled in their locality and thus subject to personal property taxation. Several commissioners related that a number of vehicles were escaping local taxation entirely. They noted that when they approached carriers, they were told that the vehicles in question were domiciled elsewhere and paid taxes there. These commissioners felt that carriers were playing one locality against the other.

1/ C. J. Gallagher and G. E. Hoffer. "A Comparative Analysis of the Rolling Stock Tax and the Personal Property Tax: Virginia, 1972." Revenue Resources and Economic Study Commission, 1973.

All commissioners of revenue questioned said that they would welcome the opportunity to tax intrastate common carriers in the same manner that they currently assess all other private and for-hire carriers. Most commissioners recognized, however, that subjecting intrastate common carriers to local tangible personal property taxes would yield little additional revenues. The consultants estimated that the localities would collect up to an additional $300,000 annually if the rolling stock of intrastate common carriers of property were subject to local personal property taxation.

Recommendation

Because of the problems and inequities that have been found to exist in the procedures currently used to tax motor carriers, the commission recommends that the rolling stock tax as it applies to intrastate common carriers of property be repealed. In its place, the commission recommends that these vehicles become subject to the local personal property tax.

Using data supplied by the applicant on his registration card, the Division of Motor Vehicles (DMV) would notify each local commissioner of revenue of all vehicular rolling stock domiciled in his locality with the exception of any vehicle defined in the Code of Virginia as a pick-up truck not used for-hire. This would exempt all privately used trucks weighing less than 3-1/4 tons from the listing that the commissioner of revenue receives.

In addition to reporting the situs of each vehicle, DMV would report the purchase price of the vehicle when it was purchased new. DMV could obtain this figure either by requiring this data upon annual application for registration or by determining this price from the "Blue Book". Upon receiving this cost data, each commissioner would

then apply his locality's depreciation schedule and tangible personal property tax rate and bill the owner of the rolling stock. Each taxpayer would remit payment to this local commissioner. All funds collected would remain in the locality.

This method of assessment would be more efficient and more equitable than the current one. It would redress the dual, discriminatory system that the Commonwealth presently uses. All rolling stock, except smaller, privately used vehicles, would be taxed in a similar manner and would be subject to local taxation. Any firms or individuals who presently escape local *ad valorem* taxation by playing one locality against the other would be unable to continue this practice. Any vehicle with a current Virginia registration would pay local property taxes to some political subdivision of the Commonwealth.

With intrastate common carriers of property subject to local personal property taxation, it is estimated that localities would receive up to $300,000 in additional revenues annually. Whereas 279 localities receive distributions under the rolling stock tax, only 29 localities would receive property taxes from these carriers. They would be the 29 localities in which those carriers with intrastate common carrier certificates domicile rolling stock. Although elimination of the present rolling stock tax would deprive over 200 localities of some revenues, the amounts lost would be small, for in 1973 the total distribution to all localities was approximately $100,000. Almost 50 percent of the localities losing revenue would lose under $225 annually while no locality would lose over $2,100 annually.

To facilitate determining a situs for every Virginia registered vehicle, the commission further recommends that DMV be enjoined from issuing Virginia registrations unless the applicant specifies a

domicile for his vehicle. This requirement is currently made of all applicants with in-state addresses; no less should be expected of out-of-state applicants. (See the proposed legislation as Exhibit 10 in the Appendix.)

The current recommendation is similar to one introduced and rejected at the 1974 session of the General Assembly. That proposal provided for uniform assessment at the state level of all vehicular rolling stock in the Commonwealth with the exception of pick-up or panel trucks not used for-hire and trailers having a gross weight of less than 1,500 pounds and the taxation of all such rolling stock at the local level under the personal property tax. The committee amendment in the nature of a substitute that did pass at the 1974 session of the General Assembly required DMV to report the situs of any truck or trailer to the commissioner of the revenue in each locality before issuing the registration or certificate of title. Motor vehicles and rolling stock of intrastate common carriers and public service corporations, however, were exempted from this requirement (see Chapter 47, 1974 Acts of Assembly). The new commission recommendation would substantially expand the effects of that act.

Local License Taxes

Background

The 1974 session of the General Assembly directed the Revenue Resources and Economic Commission in Senate Joint Resolution No. 33 to study the license taxes that local governments are authorized to impose on the gross receipts of businesses, professions, and occupations and to examine the equity of these taxes. In addition, if any inequity were found, the resolution directed the commission to make either recommendations for alternate sources of revenue or modifications in the

present license tax structure.

The commission has found that local governments in Virginia impose a wide variety of license taxes. Although all local governments have the authority to impose license taxes, generally only the cities, incorporated towns, and suburban counties use them. The commission recognizes that there are problems with this tax at the local level. Many localities have license tax rates that are viewed as being highly discriminatory. Finally, some localities appear to use this tax as an attempt to regulate certain activities rather than to license them.

The commission has begun a thorough study of the issues in license taxation that has included receiving the comments of many citizens of the Commonwealth at a public hearing in Richmond on October 4, 1974. The commission realizes that this area is much more complex than previously believed and that the possible inequities could be potentially more serious than previously realized. Because of these unexpected complexities the commission is not yet prepared to make recommendations that would completely resolve these many issues.

Recommendation

In order to not increase the inequity of local license taxation the commission recommends that a temporary ceiling be placed on all local license tax rates. This ceiling would not allow tax rates to increase over the rates in effect on December 31, 1974 and would last only through December 31, 1976. The ceiling would of course allow the commission additional time to continue its study and finalize its recommendations. The commission places the highest priority on an intensive investigation of this tax and will present a comprehensive analysis and series of recommendations to the 1976 session of the

General Assembly. In addition the commission will study the issues involved in state license taxation, including the possibility of eliminating this form of taxation. (See the proposed legislation as Exhibit 11 in the Appendix.)

Alternative Revenue Sources

In addition to making the previous recommendations, the commission has studied a number of the Commonwealth's other fiscal issues. Although the commission has no more specific recommendations, the commission would like to present various alternative revenue sources that could be utilized to meet any unanticipated revenue demands. The revenue sources are not considered in any order of priority.

Inheritance and Gift Taxation

Present Structure and Revenues of the Virginia Inheritance Tax

The Virginia inheritance tax applies to the beneficiary shares of estates of residents and of nonresidents who come under its coverage. Estates consist of real and personal property. The tax levied depends on the share of the net estate (gross estate minus deductions and exemptions) received by the beneficiary and on the class of the beneficiary. There are three classes of beneficiaries.

Class A beneficiaries consist of the wife, husband, parents, grandparents, children, and all other lineally related persons. The first $5,000 of the inheritance received by each beneficiary is exempt from taxation and amounts above that are taxable as follows:

Over $5,000 to $50,000	1 percent
Over $50,000 to $100,000	2 percent
Over $100,000 to $500,000 .	3 percent
Over $500,000 to $1,000,000	4 percent
Over $1,000,000	5 percent

Class B beneficiaries are brothers, sisters, nephews, and nieces. They each receive a $2,000 exemption before the inheritance is subject to tax. Class C beneficiaries are grandnephews and grandnieces, firms, associations, corporations, other organizations, and those not elsewhere classified. In this class the first $1,000 of the inheritance is exempt. The inheritances of class B and C beneficiaries are taxable as follows:

	Class B	Class C
Over $1,000 to $2,000		5 percent
Over $2,000 to $25,000	percent	5 percent
Over $25,000 to $50,000 . .	percent	7 percent
Over $50,000 to $100,000 . .	percent	9 percent
Over $100,000 to $500,000 .	8 percent	12 percent
Over $500,000	10 percent	15 percent

Qualifying these rates is the state law allying the Virginia inheritance tax with the federal estate tax laws in order to take full advantage of the federal credit for state death taxes. Virginia statutes impose a tax equal to the federal estate tax credit if that credit is larger than the Virginia inheritance tax. In this manner the state can maximize its revenues, given the federal rate, because the Virginia tax assessment will never be less than the maximum federal credit for state death taxes. This process of imposing a floor on the tax liability is referred to as the "pick-up" statute.

In fiscal year 1973-74, the revenues from the inheritance tax were $18.6 million, which represented 1.6 percent of total general fund revenues. We must note that the revenues from this source are subject to continual fluctuation because of the dependence on large inheritances for much of the revenue.

Comparison of Death Taxes in Virginia and Other States

Structure—Tables 2 through 4 provide information on how the

Virginia inheritance tax compares with the death taxes in other states. The tables present the types of state death taxes, rates, and exemptions in effect as of July 1, 1973. We note in Table 2 that Virginia is among the large majority of states that have both an inheritance tax and a "pick-up" statute. The "pick-up" statute is widely used because with the present federal structure states can receive additional revenues while shifting the cost to the federal government.

Table 3 outlines the estate tax for each of the seventeen states using this alternative. Table 4 reveals that the exemptions that Virginia grants for a widow and children are lower than the exemptions granted by the majority of other states. A large majority of the other states also have more progressive rate structures and higher rates than Virginia. In order to clarify the position of the Virginia inheritance tax in relation to more progressive schemes, we compare it to the North Carolina tax using a class A beneficiary. The North Carolina tax exempts the first $10,000 of inheritance for each class A beneficiary; the rate structure is as follows:

First $10,000 above exemption	1 percent
Over $10,000 and to $25,000	2 percent
Over $25,000 and to $50,000	3 percent
Over $50,000 and to $100,000	4 percent
Over $100,000 and to $200,000	5 percent
Over $200,000 and to $500,000	6 percent
Over $500,000 and to $1,000,000	7 percent
Over $1,000,000 and to $1,500,000	8 percent
Over $1,500,000 and to $2,000,000	9 percent
Over $2,000,000 and to $2,500,000	10 percent
Over $2,500,000 and to $3,000,000	11 percent
Over $3,000,000	12 percent

Several differences between the Virginia and North Carolina inheritance taxes are obvious. First, in Virginia a tax is imposed on inheritances that North Carolina exempts from taxation. Second, the tax rates are more progressive over a larger number of inheritance

levels in North Carolina than in Virginia. Table 5 presents the actual tax and the effective tax rates on equivalent inheritances in Virginia and in North Carolina. The actual and effective rates are higher in North Carolina than in Virginia for all but the three smallest taxable inheritances.[1] The "pick-up" statute comes into use in Virginia for class A inheritances at approximately $770,000 (see Table 5). At inheritance levels above that amount the "pick-up" statute has the effect of raising the effective rates above those produced by the Virginia structure.

TABLE 2--TYPES OF STATE DEATH TAXES, JULY 1, 1973

Type of tax	State
"Pickup" tax only . . . . (6)	Alabama, Alaska, Arkansas, Florida, Georgia, New Mexico.
Estate tax only . . . . (2)	Mississippi, North Dakota.
Estate tax and "pickup" tax . . . . (7)	Arizona, New York,[1] Ohio, Oklahoma,[1] S. Carolina,[1] Utah, Vermont[1].
Inheritance tax only . . . . (2)	South Dakota, West Virginia.
Inheritance tax and "pickup" tax . . . . (31)	California,[1] Colorado,[1] Connecticut, Delaware,[1] District of Columbia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana,[1] Maine, Maryland, Massachusetts, Michigan, Minnesota,[1] Missouri, Montana, Nebraska, New Hampshire, New Jersey, North Carolina,[1] Pennsylvania, Tennessee,[1] Texas, Virginia,[1] Washington,[1] Wisconsin,[1] Wyoming.
Inheritance, estate and "pickup" taxes . . . . (2)	Oregon,[1] Rhode Island[1].
No tax . . . . (1)	Nevada.

[1] Also has gift tax (16 States).

Source: Commerce Clearing House, State Tax Reporter, as shown in Advisory Commission on Intergovernmental Relations, Federal-State-Local Finances: Significant Features of Fiscal Federalism, 1973-74 (Washington: Government Printing Office, 1974), p. 296.

1/ The greater progressiveness is also present in the rate structure for the North Carolina equivalent of Virginia classes B and C. However, there are no exemptions in these classes.

TABLE 3--STATE ESTATE TAX RATES AND EXEMPTIONS, JULY 1, 1973 1/

State	Rates	Maximum rate applies above	Exemption
Alabama	80 percent of 1926 Federal rates	$10,000,000	$100,000
Alaska	80 percent of 1926 Federal rates	10,000,000	100,000
Arizona[2]	4/5 of 1-16 percent	10,000,000	100,000
Arkansas	80 percent of 1926 Federal rates	10,000,000	100,000
Florida	80 percent of 1926 Federal rates	10,000,000	100,000
Georgia	80 percent of 1926 Federal rates	10,000,000	100,000
Mississippi	1-16 percent	10,000,000	60,000
New Mexico	80 percent of 1926 Federal rates	10,000,000	100,000
New York[2]	2-21 percent	10,100,000	[3]
North Dakota	2-23 percent	1,500,000	[4]
Ohio[2]	2-7 percent	500,000	5,000[5]
Oklahoma[2,6]	1-10 percent	10,000,000	15,000
Oregon[2]	2-10 percent	500,000	25,000
Rhode Island[2]	1 percent	[7]	10,000
South Carolina[2]	4-6 percent	100,000	[illegible]
Utah[2]	5-10 percent	[illegible]	[illegible][8]
Vermont[2]	The tax rate is 30% of the Federal estate tax liability due to Vermont gross estate.		

1/ Excludes states shown in Table 3 which, in addition to their inheritance taxes levy an estate tax to assure full absorption of the 80 percent federal credit.

2/ An additional estate tax is imposed to assure full absorption of the 80 percent federal credit.

3/ $20,000 of transfers to spouse and $5,000 to each lineal ascendant and descendant and to other specified relatives are exempt and deductible from first bracket.

4/ Exemption for spouse is $20,000 or 50 percent of adjusted gross estate, for minor child, $5,000, for lineal ancestor or decendants, $2,000.

5/ An additional $20,000 for spouse, $7,000 for minor child, and $3,000 for adult child.

6/ The maximum rate is increased from 10 percent to 15 percent and the exemption from $15,000 to $60,000 applicable July 1, 1974.

7/ Entire estate above exemption.

8/ Transfers, not to exceed $40,000, if made to the husband, wife and/or children of the decendent, are exempt from tax.

Source: Commerce Clearing House, State Tax Reporter, as shown in Advisory Commission on Intergovernmental Relations, Federal-State-Local Finances: Significant Features of Fiscal Federalism, 1973-74, (Washington: Government Printing Office, 1974), p. 296.

TABLE 4--STATE INHERITANCE TAX RATES AND EXEMPTIONS, FOR SELECTED CATEGORIES OF HEIRS, JULY 1, 1973

	Exemptions					Rates (percent)				In case of spouse	
State[1]	Widow	Minor child	Adult child	Brother or sister	Other than relative	Spouse or minor child	Adult child	Brother or sister	Other than relative	Size of first bracket	Level at which top rate applies
Alabama[2]	....	....	....	....	....	....	....	....	....	....	....
Alaska[3]	....	....	....	....	....	....	....	....	....	....	....
Arizona[3]	....	....	....	....	....	....	....	....	....	....	....
Arkansas[2]	....	....	....	....	....	....	....	....	....	....	....
California[3,4]	$ 5,000	$12,000	$ 5,000	$ 2,000	$ 300	3 – 14	3 – 14	6 – 20	10 – 24	$ 25,000	$ 400,000
Colorado	30,000	15,000	10,000	2,000	500[5]	2 – 8	2 – 8	3 – 10	10 – 19	50,000	500,000
Connecticut[3,6,7]	50,000	10,000[8]	10,000[8]	3,000	500	3 – 8[9]	2 – 8	4 – 10	8 – 14	150,000	1,000,000
Delaware[3]	20,000	3,000	3,000	1,000	None	1 – 4[9]	1 – 6	5 – 10	10 – 16	50,000	200,000
District of Columbia[3]	5,000	5,000	5,000	2,000	1,000	1 – 8	1 – 8	5 – 23	5 – 23	50,000	1,000,000
Florida[3]	....	....	....	....	....	....	....	....	....	....	....
Georgia[3]	....	....	....	....	....	....	....	....	....	....	....
Hawaii	20,000	5,000	5,000	500	500	2 – 6[9]	1.5 – 7.5	3.5 – 9	3.5 – 9	15,000	250,000
Idaho[4]	10,000	10,000	4,000	1,000	None	2 – 15	2 – 15	4 – 20	8 – 30	25,000	500,000
Illinois	20,000	20,000	20,000	10,000	100	2 – 14[10]	2 – 14	2 – 14	10 – 30	20,000	500,000
Indiana[3]	15,000	5,000	2,000	500	100	1 – 10	1 – 10	5 – 15	7 – 20	25,000	1,500,000
Iowa	40,000	15,000	15,000	None[11]	None[11]	1 – 8	1 – 8	5 – 10	10 – 15	5,000	150,000
Kansas	75,000	15,000	15,000	5,000	200[5]	0.5 – 2.5[9]	1 – 5	3 – 12.5	10 – 15	25,000	500,000
Kentucky	10,000	10,000	5,000	1,000	500	2 – 10	2 – 10	4 – 16	6 – 16	20,000	500,000
Louisiana[3,4]	5,000	5,000	5,000	1,000	500	2 – 3	2 – 3	5 – 7	5 – 10	25,000	25,000
Maine	15,000	10,000	10,000	500	500	2 – 6	2 – 6	8 – 12	12 – 18	50,000	250,000
Maryland[5]	150	150	150	150	150	1	1	7½	7½	[12]	[12]
Massachusetts[5,13]	30,000[14]	15,000	15,000	5,000	5,000	1.8 – 11.8	1.8 – 11.8	5.5 – 19.3	8 – 19.3	10,000	1,000,000
Michigan[3,15]	30,000[16]	5,000	5,000	5,000	None	2 – 8	2 – 8	2 – 8	10 – 15	50,000	750,000
Minnesota[3,17]	30,000	15,000	6,000	1,500	500	1.5 – 10	2 – 10	6 – 25	8 – 30	25,000	1,000,000
Mississippi[2]	....	....	....	....	....	....	....	....	....	....	....
Missouri	20,000[18]	5,000[19]	5,000[19]	500	100[5]	1 – 6	1 – 6	3 – 18	5 – 30	20,000	400,000
Montana[3]	20,000	5,000	2,000	500	None	2 – 8	2 – 8	4 – 16	8 – 32	25,000	100,000
Nebraska[3]	10,000	10,000	10,000	10,000	500	1	1	1	6 – 18	[12]	[12]
Nevada					No tax imposed						
New Hampshire	[20]	[20]	[20]	None[20]	None[20]	[20]	[20]	15	15	[20]	[20]
New Jersey	5,000	5,000	5,000	500[5]	500[5]	1 – 16	1 – 16	11 – 16	15 – 16	10,000	3,200,000
New Mexico[2]	....	....	....	....	....	....	....	....	....	....	....
New York[2]	....	....	....	....	....	....	....	....	....	....	....
North Carolina[21]	10,000[22]	5,000[22]	2,000	None	None	1 – 12	1 – 12	4 – 16	8 – 17	10,000	3,000,000
North Dakota[3]	....	....	....	....	....	....	....	....	....	....	....
Ohio[3]	....	....	....	....	....	....	....	....	....	....	....
Oklahoma[3]	....	....	....	....	....	....	....	....	....	....	....
Oregon[23,24]	None	None	None	1,000	500	2 – 10	2 – 10	2 – 15	4 – 20	25,000	500,000

See footnotes at the end of table.

TABLE 4 – STATE INHERITANCE TAX RATES AND EXEMPTIONS, FOR SELECTED CATEGORIES OF HEIRS, JULY 1, 1973 (Cont'd)

State[1]	Widow	Exemptions				Rates (percent)				In case of spouse	
		Minor child	Adult child	Brother or sister	Other than relative	Spouse or minor child	Adult child	Brother or sister	Other than relative	Size of first bracket	Level at which top rate applies
Pennsylvania	None[25]	None[25]	None[25]	None	None	6	6	15	15	[12]	[12]
Rhode Island[3,23]	$10,000	$10,000	$10,000	$ 5,000	$ 1,000	2 – 9	2 – 9	3 – 10	8 – 15	$ 25,000	$1,000,000
South Carolina[2]	....	....	....	....	....	....	....	....	....	....	....
South Dakota[3]*	15,000	10,000	10,000	500	100	1½ – 4	1½ – 4	4 – 12	6 – 20	15,000	100,000
Tennessee[3]	10,000[26]	10,000[26]	10,000[26]	1,000[26]	1,000[26]	1.4 – 9.5	1.4 – 9.5	6.5 – 20	6.5 – 20	25,000	500,000
Texas[3,4]	25,000	25,000	25,000	10,000	500	1 – 6	1 – 6	3 – 10	5 – 20	50,000	1,000,000
Utah[2]	....	....	....	....	....	....	....	....	....	....	....
Virginia[3]	5,000	5,000	5,000	2,000	1,000	1 – 5	1 – 5	2 – 10	5 – 15	50,000	1,000,000
Washington[3,4]	5,000[27]	5,000[27]	5,000[27]	1,000[6]	None	1 – 10	1 – 10	3 – 20	10 – 25	25,000	500,000
West Virginia[3]*	15,000	5,000	5,000	None	None	3 – 13	3 – 13	4 – 18	10 – 30	50,000	1,000,000
Wisconsin[3,28]	50,000	4,000	4,000	1,000	500	2½ – 12½	2½ – 12½	5 – 25	10 – 30	25,000	500,000
Wyoming	10,000	10,000	10,000	10,000	None	2	2	2	6	[12]	[12]

[1] All States, except those designated by asterisk (*), impose also an estate tax to assure full absorption of the 80 percent Federal credit.
[2] Imposes only estate tax.
[3] Exemptions are deductible from the first bracket.
[4] Community property passing to the surviving spouse is exempt, or only one-half is taxable.
[5] No exemption is allowed if beneficiary's share exceeds the amount shown in the exemption column, but no tax shall reduce the value of the amounts shown in the exemption column. In Maryland, it is the practice to allow a family allowance of $450 to a widow if there are infant children, and $225 if there are no infant children, although there is no provision for such deductions in the statute.
[6] The exemption shown is the total exemption for all beneficiaries falling into the particular class and is shared by them proportionately.
[7] An additional 30 percent surtax is imposed.
[8] Only one $10,000 exemption is allowed for beneficiaries in Class A, which includes minor and adult children.
[9] Rate shown is for spouse only. A minor child is taxed at the rates applying to an adult child.
[10] With respect to taxable transfers passing to a husband or wife of a decedent dying on or after July 5, 1969, if taxable transfer exceeds $5,000,000, the tax on the excess thereof is computed at 6%. Tax rates on the taxable amount up to and including $5,000,000 are the same rates as provided for in excess of the exemption.
[11] Estates of less than $1,000 after deduction of debts are not taxable.
[12] Entire share (in excess of allowable exemption).
[13] Applicable to property or interests passing or accruing upon the death of persons who die on or after July 18, 1969, a 14% surtax is imposed in addition to the inheritance tax.
[14] In addition, an exemption to the extent of the value of single family residential property and to the extent of $25,000 of the value, in the case of multiple family residential property, used by a husband and wife as a domicile, is allowed where the property was held by them as joint tenants or tenants by the entirety.
[15] There is no tax on the share of any beneficiary if the value of the share is less than $100.
[16] Plus an additional $5,000 for every minor child to whom no property is transferred.
[17] For a widow, an additional exemption is allowed equal to the difference between the maximum deduction for family maintenance ($5,000) and the amount of family maintenance actually allowed by the Probate Court. The total possible exemption therefore would be $35,000. If there is no surviving widow entitled to the exemption, the aggregate exemption is allowable to the children.
[18] In addition, an exemption is allowed for the clear market value of one-half of the decedent's estate, or one-third if decedent is survived by lineal descendents.
[19] Or the value of the homestead allowance, whichever is greater.
[20] No tax imposed on spouses, lineal ascendants and descendants, and eff. 3/23/72 persons who for 10 consecutive years prior to their 15th birthday were members of the decedent's household.
[21] Gift taxes paid on gifts included in the gross estate of the decedent are credited against the estate tax.
[22] A widow with a child or children under 21 and receiving all or substantially all of her husband's property, shall be allowed, at her option, an additional exemption of $5,000 for each such child. The children shall not be allowed the regular $5,000 exemption provided for such children.
[23] Imposes also an estate tax.
[24] Oregon imposes a basic tax, measured by the entire estate in excess of a single exemption ($15,000 prorated among all beneficiaries and deductible from the first bracket); and an additional tax, measured by the size of an individual's share for which each beneficiary has a specific exemption. All members of Class I (spouse, children, parents, grandparents, stepchildren or lineal descendants) are exempted from the additional tax.
[25] The $1,500 family exemption is specifically allowed as a deduction.
[26] Widows and children are included in Class A, with one $10,000 exemption for the entire class. Beneficiaries not in Class A are allowed one $1,000 exemption for the entire class.
[27] An additional $5,000 exemption is allowed to the class as a whole.
[28] These rates are subject to the limitation that the total tax may not exceed 20 percent of the clear market value of the property transferred to any distributee.

Source: ACIR staff compilation based on Commerce Clearing House, *State Tax Reporter.*

TABLE 5--A COMPARISON OF THE VIRGINIA AND NORTH CAROLINA INHERITANCE TAXES AT VARIOUS INHERITANCE LEVELS USING CLASS A SPOUSE

	Virginia			North Carolina		
Inheritance Before Exemption (1)	Taxable Inheritance (2)	Tax (3)	Effective Rate (%) (4)	Taxable Inheritance (5)	Tax (6)	Effective Rate (%) (7)
$ 10,000	$ 5,000	$ 50	0.50	$ 0	$ 0	0
20,000	15,000	150	0.75	10,000	100	0.50
25,000	20,000	200	0.80	15,000	200	0.80
50,000	45,000	450	0.90	40,000	850	1.70
100,000	95,000	1,450	1.45	90,000	2,750	2.75
200,000	195,000	4,450	2.22	190,000	7,650	3.82
500,000	495,000	13,450	2.69	490,000	25,550	5.11
1,000,000	995,000	36,560[a]	3.66	990,000	60,450	6.04
1,500,000	1,495,000	68,240	4.55	1,490,000	100,350	6.69
2,000,000	1,995,000	103,920	5.20	1,990,000	145,250	7.26
2,500,000	2,495,000	143,600	5.74	2,490,000	195,150	7.81
3,000,000	2,995,000	187,280	6.24	2,990,000	250,050	8.33
4,000,000	3,995,000	286,640	7.17	3,990,000	369,950	9.25

a/ The "pick-up" tax becomes effective at this level. Tax is based on the federal schedule for credit for state death taxes. For North Carolina the "pick-up" tax does not become effective for these sizes of inheritances.

Source: Tax Codes for the states of Virginia and North Carolina.

Receipts--The Bureau of the Census has compiled revenue data on the death and gift taxes of state governments.[1] Since death taxes account for the majority of such collections, the data give an idea of the relative effort of the states that levy death taxes. The 1972-73 per capita and per $1,000 of personal income receipts from these taxes are shown below for Virginia and neighboring states:

	Death and Gift Tax Receipts in Fiscal Year 1972-73	
State	Per Capita	Per $1,000 of Personal Income
U. S. average (excl. D.C.)	$ 6.84	$ 1.54
Kentucky	4.34	1.22
Maryland	2.90	.60
North Carolina	6.79	1.81
Tennessee	7.71	2.15
Virginia	3.47	.82
West Virginia	3.11	.87

These data indicate that Virginia's inheritance tax is relatively low when compared to either U. S. average and third lowest among the surrounding states on a per capita basis.

Economic Effects of the Inheritance Tax

There appears to be general agreement among economists that death taxes have fewer adverse effects on incentives than do income taxes.[2] Economists generally measure the effects of a tax by the distortions that it causes in the allocation of resources. Income taxes distort the allocation of resources because an income tax reduces the return from any given enterprise. When the rewards from a given effort are

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1/ U. S. Bureau of the Census, State Government Finances in 1973, GF 73, No. 3 (Washington: Government Printing Office, 1974), pp. 21 and 50.

2/ Richard A. Musgrave, The Theory of Public Finance, (New York: McGraw-Hill, Inc., 1959), p. 248.

reduced, less of that activity will be undertaken. Whatever distortions death taxes may cause, they will be minimal because death taxes are paid only after a lifetime of work and accumulation and are likely to be given much less weight in decisions to work, save, and invest. Minimizing distortions is certainly not the only criteria for a tax system; however, it does deserve consideration.

The Virginia Gift Tax

The Virginia gift tax operates on a framework similar to that of the Virginia inheritance tax. The Virginia gift tax applies to the beneficiary shares of all property within the jurisdiction of the Commonwealth—real, personal, and mixed that is passed by gift in any one calendar year. The tax levied depends upon the actual value of the net taxable gift (total actual value of gift - exemptions) received by each beneficiary. As in the inheritance tax there are three classes of beneficiaries, each with different rates of tax and exemptions. The exemptions, classes, and tax rates are identical to those of the inheritance tax. The tax is paid by the donor at the end of the calendar year. If an individual grants a number of gifts over the period of a calendar year to the same individual the gift tax is applied to the total value of the gifts to the beneficiary; thus, the tax is based on a cumulative actual value for each beneficiary but only over the single calendar year. In fiscal year 1973-74, the revenues from the gift tax were $1.1 million. This revenue source is subject to continual fluctuation. For example, gift tax revenues in fiscal year 1972-73 were $1.6 million.

Any thorough discussion of death taxes should consider the interrelationship of the gift and inheritance taxes. To maintain the existing relationship between these taxes, any change in the inheritance tax

would require a corresponding change in the gift tax. If the existing relationship of gift taxes vis-à-vis inheritance taxes were not maintained (e.g., only increasing the inheritance tax rates), taxpayers would be encouraged to distribute some part of their future estate before death because of the lower gift tax liability.

The Virginia gift tax is similar in concept to the federal gift tax. In both cases, the liability of the tax falls on the donor, and the tax is based on the value of the property transferred as a gift minus exemptions. The similarity ends at this point because there are a number of federal provisions that greatly increase the amount of exemptions and because the federal gift tax does not distinguish between the classes of beneficiaries.

In computing the federal gift tax base in any one year, the first $3,000 of gifts to each recipient is excluded; when a husband and wife each contribute half of the gift, the first $6,000 is excluded. In addition to this annual exclusion, a $30,000 total lifetime gift exclusion is granted to the donor that can be doubled for married couples. This lifetime exclusion may be used at any time at the discretion of the donor. The final exemption, one-half of the value of gifts made between a husband and wife, may be deducted from the amount subject to the gift tax. These adjustments to the total value of gifts yield net taxable gifts. After the taxable gift is determined for one year, the federal tax is cumulative in the sense that it applies each year to the aggregate sum of all taxable gifts made since enactment of the present tax.[1/] This is at direct odds with the Virginia gift

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[1/] The tax liability in any one year consists of the differences between 1) the tax on the aggregate sum of all taxable gifts made since 1932 and 2) the amount of tax on the aggregate gifts made up to the beginning of the current taxable year.

tax, which is not cumulative over time and which is levied separately on the value of the gift to each donee. These numerous adjustments help to lower the effects of the high nominal rates in the federal gift tax and the high tax imposed by the cumulative provisions.

An Analysis of 1973-74 Inheritance Tax Returns

To examine the inheritance tax structure and to see how the taxable base is actually composed, the Department of Taxation has undertaken a comprehensive study of the inheritance tax returns from fiscal year 1973-74. Table 6 shows the number of beneficiaries, taxable amount, and total tax collections by class and by tax rate level. The percentage distribution of these items is presented in Table 7. Although these tables do not include the "pick-up" returns, they do provide information on the source of the bulk of inheritance tax collections. As shown in these tables, the distribution of the number of returns was skewed toward the lowest size classes. For example, the returns in the exempt and first taxable level of each of the three classes comprised 84.7 percent of the total returns. The tax collections, however, were skewed in the opposite direction. The returns at the lowest rate level for each class comprised only 13.0 percent of total revenue exclusive of the "pick-up". These data confirm the hypothesis that most of the returns are in the lower size classes and produce an extremely small amount of revenue largely because of the high number of small inheritances and the relatively low exemptions.

An examination of the "pick-up" returns reinforced the finding that a relatively small number of returns produced the largest portion of revenues. Our preliminary findings on "pick-up" returns indicate that less than 100 returns brought in over $3.2 million in revenue. This dependence on larger inheritances points out the main reason for the

TABLE 6—INHERITANCE TAXES EXCLUSIVE OF THE "PICK-UP" FOR FISCAL YEAR 1973-74

Class A Beneficiaries

Number of Beneficiaries Taxable at Highest Rate Shown		Amount Taxable	Total Tax Collections
Exempt	1,698	$ 0	$ 0
1%	11,577	140,268,077	1,402,625
2%	1,521	99,111,144	1,982,250
3%	1,044	181,894,651	5,456,833
4%	59	36,442,560	1,457,703
5%	14	26,660,318	1,333,016
	15,913	$484,376,750	$11,632,427

Class B Beneficiaries

Number of Beneficiaries Taxable at Highest Rate Shown		Amount Taxable	Total Tax Collections
Exempt	908	$ 0	$ 0
2%	3,705	22,584,620	451,783
4%	474	15,605,721	624,212
6%	236	16,479,698	988,782
8%	109	19,608,650	1,568,692
10%	5	5,060,575	506,058
	5,437	$ 79,339,264	$ 4,139,527

Class C Beneficiaries

Number of Beneficiaries Taxable at Highest Rate Shown		Amount Taxable	Total Tax Collections
Exempt	1,043	$ 0	$ 0
5%	3,096	16,497,461	824,963
7%	309	10,774,633	754,222
9%	127	8,561,881	770,569
12%	61	11,521,596	1,382,597
15%	7	6,968,461	1,045,268
	4,643	$ 54,324,032	$ 4,777,619
Total	25,993	$618,040,046	$20,549,573

Note: It must be noted that because of the technique used to gather the inheritance tax returns, the results include data for a period slightly larger than the 1973-74 fiscal year.

Source: The data were compiled by the Department of Taxation.

TABLE 7--PERCENTAGE DISTRIBUTION OF INHERITANCE TAX DATA, EXCLUSIVE OF THE "PICK-UP", FOR RETURNS, TAXABLE AMOUNTS, AND TAX COLLECTIONS, FISCAL YEAR 1973-74

Class A Beneficiaries

Percentage of Beneficiaries Taxable at Highest Rates Shown		Percentage of Total Amount Taxable	Percentage of Total Tax Collections
Exempt	6.5%	0%	0%
1%	44.5	22.7	6.8
2%	5.9	16.0	9.6
3%	4.0	29.4	26.6
4%	0.2	5.9	7.1
5%	0.1	4.3	6.5
	61.2%	78.4%	56.6%

Class B Beneficiaries

Percentage of Beneficiaries Taxable at Highest Rates Shown		Percentage of Total Amount Taxable	Percentage of Total Tax Collections
Exempt	3.5%	0%	0%
2%	14.3	3.7	2.2
4%	1.8	2.5	3.0
6%	0.9	2.7	4.8
8%	0.4	3.2	7.6
10%	0.0	0.8	2.5
	20.9%	12.8%	20.1%

Class C Beneficiaries

Percentage of Beneficiaries Taxable at Highest Rates Shown		Percentage of Total Amount Taxable	Percentage of Total Tax Collections
Exempt	4.0%	0%	0%
5%	11.9	2.7	4.0
7%	1.2	1.7	3.7
9%	0.5	1.4	3.7
12%	0.2	1.9	6.7
15%	0.0	1.1	5.1
	17.9%	8.8%	23.2%
	100.0%	100.0%	

Source: The data were compiled by the Department of Taxation.

revenue from the inheritance tax fluctuating from one year to another.

Alternative Inheritance Tax Exemption Levels and Rates

Before discussing possible changes in the existing law, it must be noted that there has been a continuing discussion of possible changes in the federal estate and gift tax area for a number of years. To this date there has been no action nor has there been any indication that action might come in the immediate future. However, the potential for change in the federal law does not mean that possible modifications in the Virginia inheritance and gift taxes cannot be examined.

In the following analysis the Revenue Resources and Economic Commission presents four alternative inheritance schedules that would increase the progressivity of the inheritance tax. While the commission does not make any specific recommendations in this area it would like to point out that the adoption of any of these alternatives could be used to meet any unanticipated revenue demands.

Alternative 1 is presented in Table 8. The Revenue Resources and Economic Study Commission recommended this alternative to the 1974 session of the General Assembly. It became Senate Bill No. 60, which was carried over in the Senate. This bill would double the present exemption levels for each of the three classes of beneficiaries. Class A beneficiaries would have a $10,000 exemption, class B, $4,000, and class C, $2,000. This doubling of present exemptions would remove the tax liability of many small estates that contribute little to total revenues. Moreover, the changes in the exemptions would place Virginia more in line with the exemption policies of the other states. To make the tax more progressive would also require a more graduated rate schedule using a larger number of brackets in each class than the present

schedule. In the rate schedule for Alternative 1, the nominal rates for class A are greater for all beneficiary shares above $10,000. For class B beneficiaries the tax rates do not change from current levels, except for the higher exemption, on all beneficiary shares up to $500,000 but are higher above that amount. Class C beneficiaries are subject to the same tax rates as under present law, except for the higher exemption, on beneficiary shares up to $100,000. On shares of $100,000 to $200,000 the rate actually declines; on beneficiary shares above that amount the tax rate increases.

If Alternative 1 were adopted, the commission estimates that revenues from the inheritance tax would increase by approximately 18 percent over revenues from the current structure. On the basis of inheritance tax revenue in 1973-74, this would have meant an increase of approximately $3.3 million in that fiscal year. Almost all of this increase would be borne by class A beneficiaries. The revenue from class C beneficiaries would actually decline slightly because of the slight decrease in their rates.

To maintain the existing relationship between the inheritance tax and the gift tax, the gift tax rates and exemptions would also have to be changed to those in Table 8. In 1973-74 gift tax revenues were $1.1 million; therefore, the net effect of these changes would be to increase revenues by about $200,000 annually.

The final provision of Senate Bill No. 60 is an increase in the minimum gross estate necessary to file a return from the present $1,000 to $4,000. We must note that in the case of a class C beneficiary with a proposed exemption allowance of $2,000, there is a possibility that by requiring no returns on estates of less than $4,000,

TABLE 8.--PROPOSED CHANGES IN THE INHERITANCE TAX
ALTERNATIVE 1

Class A	Rate (%)	Class B	Rate (%)
First $10,000	Exempt	First $4,000	Exempt
Over $10,000 and to $25,000	1	Over $4,000 and to $25,000	2
Over $25,000 and to $50,000	2	Over $25,000 and to $50,000	4
Over $50,000 and to $100,000	3	Over $50,000 and to $100,000	6
Over $100,000 and to $200,000	4	Over $100,000 and to $200,000	8
Over $200,000 and to $500,000	5	Over $200,000 and to $500,000	10
Over $500,000 and to $1,000,000	6	Over $500,000 and to $1,000,000	12
Over $1,000,000 and to $2,000,000	7	Over $1,000,000 and to $2,000,000	14
Over $2,000,000	8	Over $2,000,000	16

Class C	Rate (%)
First $2,000	Exempt
Over $2,000 and to $25,000	5
Over $25,000 and to $50,000	7
Over $50,000 and to $100,000	9
Over $100,000 and to $200,000	11
Over $200,000 and to $500,000	13
Over $500,000 and to $1,000,000	15
Over $1,000,000 and to $2,000,000	17
Over $2,000,000	19

the class C beneficiary may be in the position of owing tax but not being required to pay it because his share of an estate may be over $2,000 but less than $4,000. One way to alleviate this problem would be to amend Senate Bill No. 60 to require a minimum gross estate of $2,000 to file a return. The revenue loss of this proposal would be practically zero while still relieving the Department of Taxation of administrative burden.

Alternative 2 is quite similar to the first alternative (see Table 9). The treatment of class A beneficiaries is almost identical. Tax rates on class B beneficiaries are slightly higher than those set forth in Alternative 1 on all inheritances above $25,000. This increase is generally an additional percentage point of tax. The greatest difference between Alternatives 1 and 2 is in class C. The rates are increased by approximately 4 percentage points at the $25,000 to $50,000 level, and this increase continues over the entire inheritance scale. The goal of this schedule is to double the exemptions for each class and to increase the tax proportionately for all classes and levels. In Alternative 1 the tax on class C beneficiaries did not increase in proportion to the other classes. Alternative 2 remedies this situation.

If Alternative 2 were adopted, the estimated rise in inheritance tax revenues would be approximately 27 percent. This would have meant an increase of approximately $5.0 million in fiscal year 1973-74. On a percentage basis this increase would be borne equally by class A and class C beneficiaries and to a lesser extent by class B beneficiaries.

Alternative 3 attempts to simplify the tax to a degree by offering wider rate brackets than Alternative 1 (see Table 10). On the whole, it decreases the rates of tax for class A beneficiaries as compared to

Alternative 1. It also decreases the rates of tax on class B beneficiaries relative to Alternative 1 although on a smaller scale. The rates of tax for class C increase. This option is in line with the actions of some states that are increasing the rates of tax on class C beneficiaries to a greater degree than on those beneficiaries who are lineal descendants.

Adoption of Alternative 3 would increase revenues from the inheritance tax by approximately 26 percent, or about $4.8 million in fiscal year 1973-74. All three classes would share in the increase in equal proportions.

Finally, Alternative 4 is an attempt to moderate the increase in tax for class A's relative to the others (see Table 11). Class A receives an exemption of $15,000 rather than $10,000 as in the other alternatives. The class B exemption increases to $5,000 from the $4,000 granted by the other alternatives while the class C exemption remains unchanged from the other alternatives at $2,000. Relative to Alternative 1, the tax rates decrease slightly for class A, remain almost the same for class B, and increase slightly for class C.

If adopted, Alternative 4 would increase inheritance tax revenues by approximately 12 percent. The increase in revenues would have been approximately $2.2 million in fiscal year 1973-74. The largest part of the increase would come from class A beneficiaries even though they receive a $15,000 exemption.

It should be noted again that to maintain the existing relationship between the inheritance tax and the gift tax, the gift tax rates and exemptions would also have to be changed. A modification of the gift tax rates and exemptions to those in Alternative 2 and 3 would yield approximately $250,000 annually while a change to Alternative 4 would yield approximately $100,000 annually.

TABLE 9.--PROPOSED CHANGES IN THE INHERITANCE TAX
ALTERNATIVE 2

Class A	Rate (%)
First $10,000	Exempt
Over $10,000 and to $25,000	1
Over $25,000 and to $50,000	2
Over $50,000 and to $100,000	3
Over $100,000 and to $250,000	4
Over $250,000 and to $500,000	5
Over $500,000 and to $1,000,000	6
Over $1,000,000 and to $2,000,000	7
Over $2,000,000	8

Class B	Rate (%)
First $4,000	Exempt
Over $4,000 and to $10,000	2
Over $10,000 and to $25,000	3
Over $25,000 and to $50,000	5
Over $50,000 and to $100,000	7
Over $100,000 and to $200,000	9
Over $200,000 and to $500,000	11
Over $500,000 and to $1,000,000	13
Over $1,000,000 and to $2,000,000	15
Over $2,000,000	17

Class C	Rate (%)
First $2,000	Exempt
Over $2,000 and to $5,000	5
Over $5,000 and to $10,000	7
Over $10,000 and to $25,000	9
Over $25,000 and to $50,000	11
Over $50,000 and to $100,000	13
Over $100,000 and to $200,000	15
Over $200,000 and to $500,000	17
Over $500,000 and to $1,000,000	19
Over $1,000,000 and to $2,000,000	21
Over $2,000,000	23

TABLE 10--PROPOSED CHANGES IN THE INHERITANCE TAX
ALTERNATIVE 3

Class A	Rate (%)
First $10,000	Exempt
Over $10,000 and to $50,000	2
Over $50,000 and to $100,000	3
Over $100,000 and to $500,000	4
Over $500,000 and to $1,000,000	6
Over $1,000,000	7

Class B	Rate (%)
First $4,000	Exempt
Over $4,000 and to $25,000	4
Over $25,000 and to $50,000	6
Over $50,000 and to $100,000	8
Over $100,000 and to $500,000	10
Over $500,000 and to $1,000,000	12
Over $1,000,000	14

Class C	Rate (%)
First $2,000	Exempt
Over $2,000 and to $25,000	7
Over $25,000 and to $50,000	10
Over $50,000 and to $100,000	13
Over $100,000 and to $500,000	15
Over $500,000 and to $1,000,000	17
Over $1,000,000	19

TABLE 11--PROPOSED CHANGES IN THE INHERITANCE TAX
ALTERNATIVE 4

Class A	Rate (%)	Class B	Rate (%)
First $15,000	Exempt	First $5,000	Exempt
Over $15,000 and to $50,000	2	Over $5,000 and to $25,000	3
Over $50,000 and to $100,000	3	Over $25,000 and to $100,000	6
Over $100,000 and to $500,000	4	Over $100,000 and to $500,000	9
Over $500,000 and to $1,000,000	5	Over $500,000 and to $1,000,000	11
Over $1,000,000 and to $2,000,000	6	Over $1,000,000 and to $2,000,000	13
Over $2,000,000	7	Over $2,000,000	15

Class C	Rate (%)
First $2,000	Exempt
Over $2,000 and to $25,000	6
Over $25,000 and to $100,000	9
Over $100,000 and to $500,000	12
Over $500,000 and to $1,000,000	15
Over $1,000,000 and to $2,000,000	18
Over $2,000,000	21

Inclusion of Life Insurance in the Base

At present, by administrative ruling, the proceeds from life insurance are taxable only if they go to the estate. If they go directly to a designated beneficiary, they are exempt.

There are factors that support a change in this area. To exclude a part of life insurance from taxation could be considered arbitrary. Other death taxes do not have this exclusion; for example, the base of the federal estate tax includes the proceeds from all life insurance. It should be pointed out, however, that there are substantial differences in the Virginia inheritance tax structure and the federal estate tax structure. Although federal law includes life insurance proceeds, it does permit many deductions and exemptions that Virginia law does not allow. The other factor that supports a change in this area is that the state is losing a large amount of revenue by not including all life insurance proceeds in the tax base. If life insurance had been included in the tax base for the year 1970, the base would have increased by an estimated $35.6 million.[1/] Given the assumption that it was subject to the overall effective rate of 3.3 percent for the inheritance tax in 1973-74, the additional revenue would have been approximately $1.1 million annually.

On the other hand, there is reason not to support a change in this area. Virginia's inheritance tax is based on the concept of taxable estate. If the decedent had life insurance that was not payable to

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1/ This estimate is based on federal estate tax returns filed during 1970. See Internal Revenue Service, Statistics of Income, 1969, Estate Tax Returns, (Washington: Government Printing Office, 1972), p. 11. The Virginia figure was estimated by taking the ratio of Virginia life insurance in force to U. S. life insurance in force in 1969.

his estate, then the life insurance proceeds would not necessarily constitute part of the decedent's estate.

Lifetime Exemption Under the Gift Tax

The present gift tax law allows a donor to take an unlimited number of annual exemptions with the amount and number each year dependent on the class and number of beneficiaries. The amounts of the exemption are identical to those allowed for the inheritance tax.

The commission has studied the feasibility of adopting a $30,000 lifetime limit on the amount of annual exemptions that a donor can claim before becoming liable for the gift tax. The primary advantage of such a lifetime maximum on annual exemptions is that it would limit tax free gifts and increase revenues by a small amount. In addition, the constraint would strengthen the inheritance tax by not allowing donors to dispose gradually of their estates before they became subject to the inheritance tax.

On the other hand, there are reasons not to change the present exemption treatment. The revenue loss caused by the present treatment is relatively small. The gift tax in recent years has produced only $1 to $1.5 million annually; moreover the adoption of a maximum lifetime exemption policy would increase the administrative duties of the Department of Taxation. The department would have to maintain additional records to keep track of the total exemptions that a donor had claimed in the past to determine if the donor could still claim any exemptions. Finally, if a fixed lifetime exemption were granted, the amount of relief given to a donor who distributed his gifts to a class C beneficiary would be substantially higher than for a donor who chose to distribute to a class A or class B beneficiary. The result of this provision would be radically different from the present inheritance tax law,

which taxes gifts to class A beneficiaries less than class B and similarly class B beneficiaries less than class C beneficiaries.

One alternative to mitigate the effects of this last problem would be to allow a different maximum exemption for each of the three different classes of beneficiaries. For example, the limit on lifetime exemptions could be set at a total of five annual exemptions regardless of class. Thus, if the present exemptions were doubled, the maximum lifetime exemption would be $50,000 for class A, $20,000 for class B, and $10,000 for class C. For a married couple these amounts could double. If a donor decided to apply the exemptions to more than one class of beneficiary, the situation could be handled by allowing the annual exemption to be granted until the fraction of all classes of exemptions used totaled 1. For example, if a donor wanted to distribute gifts to all three classes of beneficiaries and used 50 percent of the annual exemptions for class A, 25 percent for class B, and 25 percent for class C, the respective amounts of the lifetime exemption would be $25,000, $5,000, and $2,500.

Senate Bill No. 59, carried over to the 1975 session of the General Assembly in the Senate, embodies the lifetime exemption concept but not the specific one studied by the commission. A proposed amendment in the nature of a substitute drafted by the Department of Taxation reflects that specific lifetime constraint (see Exhibit 13 in the Appendix).

While the commission makes no specific recommendation in this area, a maximum lifetime exemption of $30,000 could be used to meet any unanticipated revenue demands. As already noted, its revenue yield would be small, perhaps approximately $100,000 per year.

Elimination of the Virginia Dividend Exclusion

At the present time the dividends paid by Virginia corporations are excluded from income taxation. There are, however, four types of corporations and associations that are not subject to the state corporation income tax, and the dividends paid by them are not deductible by the recipients:

1. Public service corporations
2. Insurance companies
3. Reciprocal or inter-insurance exchanges
4. Credit unions

National banks wherever located and state banks and trust companies in Virginia are not subject to the state corporation income tax, but the dividends paid by them are fully deductible by the recipients. For the most part, therefore, the question of exclusion is confined to dividends paid out of earnings and profits of corporations engaged in manufacturing, mining, merchandising, business service, and farming.

During preconformity (all taxable years beginning before January 1, 1972), Virginia law provided that if only part of the income were assessable - that portion derived from business within the state - then only the corresponding part of the dividends would be deductible. For example, if 40 percent of a corporation's income were taxable by Virginia, 40 percent of its dividends would be deductible on the Virginia individual income tax. The varying percentages of different corporations made this a complicated procedure. Conformity attempted to simplify this procedure. If less than 50 percent of the corporation's net income is taxable by Virginia, then no portion of the dividends paid by the corporation to Virginia residents is deductible. On the other hand, if 50 percent or more of the corporation's income is taxable in

Virginia, then all of the dividends paid by the corporation to Virginia residents are deductible.

There are arguments for continuing the present treatment. The exclusion of dividends may attract additional investment in Virginia corporations and thus encourage their development and growth. The present treatment of Virginia corporate dividends may also prevent double taxation. That is, if a tax is paid by a corporation on its profits and if a stockholder is taxed again when the profits are distributed to him in the form of dividends, the original income is taxed twice. It should be pointed out that the double taxation theory has been subject to much controversy. In effect, this theory implies that, if it were not for the tax at the corporate level, the stockholder would receive additional dividends equal to the amount of the tax paid in his behalf. If this implication were a fact, it could be argued that there is double taxation. It may be a fact in extremely rare cases but, as a general rule, would not be the case as this tax is viewed by most corporations as just another factor in the costs of production. If removed, it could be spread in at least three ways - in part as additional dividends, in part in lowered prices, and in part to higher wages or other costs. Thus, there is no general agreement as to who pays the tax, for the situation varies widely between corporations and within specific corporations may vary from year to year depending upon the economics of the situation at the time.1/

1/ Double taxation arguments apparently assume there is no shifting of the burden of the corporate income tax away from the owners of capital. There is considerable disagreement over how the corporate income tax is shifted. For a survey of the debate see William H. Oakland, "A Survey of the Recent Debate on the Short-Run Shifting of the Corporation Annual Income Tax," in Proceedings of the National Tax Association, 1969, pp. 525-547.

On the other hand, there are reasons to change the treatment of dividends paid by Virginia corporations. The exclusion represents a departure from the state's conformity to federal income tax law and appears to violate the notion of horizontal equity, which calls for individuals with the same income to pay the same tax. Moreover, the $100 dividend exclusion already granted under conformity probably mitigates any adverse effects of double taxation.

Another argument for elimination is that this form of tax relief is so limited that it provides little additional incentive to invest in Virginia corporations. This view has support from the Division of Industrial Development. The division thinks that eliminating the exclusion would have little effect on the ability of manufacturers to raise capital and generally would create no serious problems affecting Virginia's competitive position in attracting new industry.[1]

A final reason is that exclusion of Virginia corporate dividends costs the state $3 to $5 million annually.[2] This loss can be viewed as a tax expenditure. Its objectives and effects are similar to actual expenditures for a program in the budget. Both reduce revenues available for other purposes; however, the program would explicitly appear on the expenditure side while the tax expenditure does not appear anywhere. As a result, the executive branch, the legislature, and the public can subject this tax expenditure to less critical analysis than ______________ an explicit expenditure. Two other differences between the dividend

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[1] See as Exhibit 14 in the Appendix the letter from the Division of Industrial Development for these and other comments on the taxation of dividends.

[2] This estimate relies on data made available by the Internal Revenue Service in Statistics of Income - 1971, Individual Income Tax Returns (Washington: Government Printing Office, 1973).

exclusion and an explicit expenditure are that the exclusion is automatically more beneficial to high than to low income taxpayers because of the progressive rate schedule and that it provides no benefits to persons too poor to pay the income tax.

Elimination of the present Virginia dividend exclusion could be used to meet any unanticipated revenue demands, for such a step would yield the state $3 to $5 million annually. The commission recommendation to the 1974 session of the General Assembly to eliminate the Virginia dividend exclusion is embodied in Senate Bill No. 61, which the Senate Finance Committee carried over to the 1975 session of the General Assembly. Senate Bill No. 61 did reflect the desire of the commission to retain the exclusion from individual income taxation of the dividends paid by national banks and state banks and trust companies.

Effect of Federal Changes on Virginia's Tax Structure

Beginning in 1972, Virginia conformed its individual income tax structure in large part to the federal income tax structure. Basically, Virginia adopted the federal deductions, standard and itemized, but chose slightly lower personal and dependent exemptions. The original goals of conformity were to provide an equitable tax structure and to ease administrative problems for the taxpayer and the Commonwealth while minimizing the revenue impact of any changes. For the most part these goals have been achieved.

One drawback of conformity is the desire at the federal level in recent years to continually change the income tax structure and the resulting potential uncertainties that this imposes on the Virginia fiscal outlook. A current example of this problem is that in November, 1974, the House Ways and Means Committee voted to increase

the minimum standard deduction from the present $1,300, for either individuals or married couples, to $1,600 for single persons and $1,900 for married couples.[1/] Their proposed bill also included an increase in the maximum standard deduction from the present 15 percent of income up to $2,000 to 16 percent up to $2,300. The passage of this tax relief to lower and middle income persons would cause an estimated $12 to $15 million annual decline in state revenues. This decline would be only partially offset in Virginia by the additional revenue produced by the other components of the bill; for example, it calls for the gradual elimination of the oil depletion allowance, and at the federal level the revenues gained from this would almost equal the revenues lost through the tax relief provisions. In Virginia, though, the elimination of the oil depletion allowance would produce less than $1 million and cause a serious revenue shortfall. Other tax reform proposals similar to the bill approved by the Ways and Means Committee would have the same result for Virginia - tax relief causing a significant revenue decline offset only in part by the revenues generated through the closing of various tax loopholes.

The commission wishes to point out that the Commonwealth has two ways to deal with the effects of any changes at the federal level. The state could anticipate the federal reform and freeze the present provisions of the state income tax law (i.e. $1,300 minimum standard deduction and 15 percent up to $2,000 maximum standard deduction) for a specified period of time. The result could be deconformity but no

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1/ The 93rd Congress has not considered the bill. Possible action has been deferred to the 94th Congress.

immediate revenue loss and an opportunity to study means of returning to conformity. The other option would be to accept the federal reforms and the revenue drop and to decide on an alternative revenue source to make up the shortfall.

Issues for Further Study

The commission feels that a continuing review of the fiscal outlook at the state and local level, alternative sources of additional revenue, and new programs is essential. The commission will continue its work in these areas as it has in the past. In addition to the general framework, however, the commission would like to list a number of specific issues that will receive top priority in the coming year. These issues are as follows:

(1) State and local license taxation

(2) Comparison of the taxation of public service corporations to private corporations

(3) Taxation of trucks and railroads

(4) Taxation of capital not elsewhere taxed.

Respectfully submitted,

Leroy S. Bendheim, Chairman

Carrington Williams, Vice-Chairman

George S. Aldhizer, II

Sam T. Barfield *

George W. Jones

John L. Knapp

Joseph A. Leafe

J. Harry Michael, Jr.

Raymond Munch

Stanley A. Owens **

Owen B. Pickett ***

Lester E. Schlitz

* See Additional Comments of Mr. Barfield, page 78.
** See Dissenting Statement of Mr. Owens, beginning page 79.
*** See Partial Dissent of Mr. Pickett, page 91.

Additional Comments by Sam T. Barfield

While I approved and signed the report of the Revenue Resources and Economic Commission, I wish to make the following comments:

When the Commission approaches the question of local license taxes, it is urged that care be taken not to disturb a source of revenue, which is irreplaceable from the locality's standpoint.

I subscribe to the philosophy of limiting localities from applying discriminatory and inequitable taxes to certain classifications of business.

I would further urge the Commission not to be too hasty in removing State business license taxes, even though this might not be a large revenue producer. The application of State business licenses serves as a policing agency for the locality in their application of the local business license. I do not know of too much objection to the State business license and according to our local business population, they do not object to it.

FINAL STATEMENT OF STANLEY A. OWENS TO BE MADE A PART OF THE FINAL REPORT OF THE REVENUE RESOURCES AND ECONOMIC COMMISSION

I cannot conscientiously join in all aspects of the proposed report of the Revenue Resources and Economic Commission to be sent to the Governor and the General Assembly.

I do agree with Item (5) of the introduction regarding assessment and taxation of public service corporation property because it more nearly approaches fairness and equity for the reason that the Corporation Commission assesses primarily on the unit method and these units are fairly easily determined and over the years have developed more competence and expertise in arriving at fair and equitable values. Also, I think the gross receipts tax is grossly unfair because it is not based on ability to pay. This applies on the state level as well as the local level. This method of taxation should be completely abolished. A business may amass a million dollars in gross receipts but not have enough net profit to pay a tax based on gross receipts.

I agree basically with Items (1), (2), (3), (4), and (5) regarding inheritance and gift taxes, exclusion of retirement income from state personal income tax, elimination of the dividend exclusion from state personal income tax, changes in the taxation of rolling stock of motor carriers and tax relief for disabled.

I think we should determine what a basic cost of living is and apply it to everybody, which, in my opinion, would be equitable and fair to everybody, and those of sufficient industry and ingenuity to earn income over the predetermined floor of a decent cost of living should be permitted to do so. This basic cost of living, including that of dependents of the taxpayer, would then be deductible from income.

The assessment system, in my opinion, based on almost thirty-two years of observing the operation of it, is not based on equity and fairness and should be abolished.

To try to patch up the iniquitous assessment system would not accomplish such purpose but would simply perpetuate the inequities of it because human

error is inescapeable.

I am attaching herewith my updated statement previously filed with the Commission which I would like published as a separate statement under and over my name, knowing full well that further work needs to be done on many aspects of the ideas I promote and with the nagging feeling that if we do not go to the income and sales tax method of raising necessary revenue, tied to a local piggyback right and limitation, something equivalent to it will be forced on us by the courts.

I think the money expended in assessments and general reassessments is totally wasted for reasons I pointed out in my full statement attached hereto.

I talked with Senator Bendheim about filing this separate report and as I understand it, he thinks I am under obligation to make my own views known in my own way.

Therefore, an updated statement filed with the Commission is attached hereto as I wish it to appear in the report of the Revenue Resources and Economic Commission to be submitted to the Governor and the General Assembly. My report follows.

The premise of this statement is to equalize the tax burden and make

it fair and equitable. Each taxpayer can compare what he pays in real estate tax with what the result of this statement will mean in comparison thereto.

As all the members of this Commission are aware, the concept of local ad valorem property taxation has in recent years become the object of severe criticism from a growing variety of sources. The use of funds derived from local property taxation to help subsidize the costs of free public education and the non-uniform exemption and assessment policies of localities are just a couple of the issues hardest hit of recent criticism.

This criticism has resulted in nationwide litigation in the public education field and the Rodriguez case from Texas has gone all the way to the United States Supreme Court. In Rodriguez, the property tax was not invalidated on the basis that no applicable Federal Constitutional question was involved; however, it was acknowledged that the property tax probably could not adequately be made mathematically equal in its application to all groups of people. The Court further stated that any scheme of local taxation requires the establishment of arbitrary jurisdictional boundaries and that the need for reform is apparent in a taxation system which may well have relied too long

and too heavily on the local property tax. The Serrano case from California will test substantially the same issues and the decision in this case might well be different from the Rodriguez decision because California requires quality and equality of education just as Virginia does. However, Serrano has not yet reached a court of last resort.

Having served as Commonwealth's Attorney for Prince William County for sixteen years, I personally witnessed inequities and unfairness associated with local property taxation. During that sixteen years, our Board of Supervisors went through five or six general reassessments at a cost of thousands of dollars. For instance, Prince William County, during the years 1959, 1965, 1970, and an estimate for 1974 will have spent $962,947.66. The reassessment for 1974 will be obsolete even before it is completed. Moreover, these expenditures can be multiplied over and over statewide and some way should be found to eliminate this intolerable situation. I will not be around long enough to see complete and final reform that this Commission under Chapter 367 of the 1974 Acts of Assembly and the Senate Joint Resolution under which we are now working, come to full fruition.

There is no such thing as a true expert. I have represented the State Highway Department since 1938, and I observed early in the appraising of real property that there were no two "qualified"(?) experts, acting independently, who would arrive at anywhere near the same appraisal figure. As long as we have the assessment and reassessment system, local or state, it will be shot through with human error. It is just impossible to make it otherwise. This is the reason I am so "addicted" to the income and sales tax approach in raising revenue. Why has the federal government never resorted to the real estate assessment and levy system. The answer is obvious.

There was common agreement that inflation and developmental pressures immediately rendered every new general reassessment both disproportionate and unfair.

With these thoughts in mind, I have decided that the only way to develop a thoroughly proportionate, if not equitable source of revenue is through the income and sales tax and the elimination of taxation on real estate. I realize that the real estate property tax is the major source of revenue for local

governments and its elimination would call for a major restructuring of the State-local tax framework. In fiscal year 1973, total county, city and town levies on locally assessed real estate were $437 million and those on public service corporations property were $54 million, for a total of $491 million. In comparison, State individual income tax collections were $442 million, and State and local sales tax collections were $393 million for a total of $835 million.

From these figures, we can see that the property tax is a huge revenue producer and just like everything else in this period of inflation, it is growing rapidly. From fiscal year 1957 to fiscal year 1973 real estate property tax levies increased at an average annual rate of 10%. From fiscal year 1968 to fiscal year 1973, the average annual increase amounted to 12.5%. It is steadily becoming a larger percentage of personal income and a bigger burden on the taxpayer, especially those living on a fixed income. In recent public opinion polls on taxation, the property tax has consistently been shown to be the most disliked by the public.

This presents the dilemma of what to do with absentee landlord with large

real estate holdings in Virginia, which are not subject to the income or sales tax. This might call for radical amendments to our constitution and statutes dealing with assessments and taxation.

The Constitution might provide that as to land holdings owned directly or indirectly by a non-resident person, firm or corporation and which exceed fifty acres shall be assessed and taxed by the State in a manner to be provided by law. Each such owner would be given a credit against the State tax in the amount of the State income tax (especially possible capital gain taxes) it paid or its sales tax payments on its own purchases; this would insure payment for such owner in one form or another. The classification can be as high or as low as is desired and it could be made to apply only to unimproved property or property a majority of which is unimproved. The State Department of Taxation could make an analysis of land holdings that would give you a relatively good idea of how much money is involved.

As to changes in the Constitution, paragraph (a) of Section 10 of Article VII will have to be revised since it is tied to real estate; attention might be paid to have the bond limit fixed under Section 9 of Article X.

Article X will require numerous changes: Section 1 will have to be rewritten, as will Section 2; Section 3 should be repealed; Section 4 will have to be rewritten and made applicable to taxation of real estate by the state. There are doubtless other sections which will require corrections, but those listed appear to be the major ones.

While I realize that the approach I am suggesting does not get entirely away from the assessment problem, it does so to a major degree and will provide, as nearly as may be, for uniformity of assessments. Since the tax money will be going to the state without any local tax involved, the abuses which led to the state getting out of the real estate tax field in 1927 and the adoption of the 40% ratio, should not arise again.

If the property tax is to be replaced, we must find some alternate tax bases to replace the revenue now generated by the property tax. Those bases which distribute the tax burden most equitably according to the ability of the individual taxpayer to pay would seem to be the most readily acceptable to the majority of taxpayers.

As Dr. John L. Knapp has so aptly stated, "Elimination of the tax

would open a gaping hole in local government finance that would be difficult to fill by either expanding existing <u>local</u> revenue sources or cutting local expenditures. In rural localities where the tax makes up 60% or more of locally raised revenue, other revenue bases of sufficient size do not exist, and in urban areas, the required increases in local revenue sources would be very large".

Increasing the existing rates on income and sales taxes to replace the revenue presently derived from the property tax seems to be a feasible alternative to property taxation. Some limited type of pi ggy-back income tax authorized to localities might be indicated. This would give localities flexibility to supplement their local budgets for individual local purposes such as school frills if they see fit, or other purposes.

Economists have estimated that the tax revenue presently attributed to real property taxation can be replaced by increasing the sales tax to 7% and restructuring income tax rates to begin at 4.5% on the first dollar of taxable income and range to 8.5% on taxable income over $15,000. It has been estimated that a one percent increase in the sales tax rate coupled with a 90% increase in income tax collections via a local individual income tax would also replace

the revenue now generated by local property taxes.

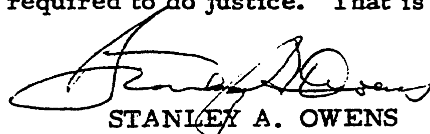
The elimination of local real property taxation will require both statutory amendments to Title 58 and constitutional amendments to Article VII and Article X of the Virginia Constitution. Chapter 15 of Title 58 entitled Real Estate Assessments and consisting of Sections 55-758 through 58-828 could be repealed. Chapter 19 dealing with local boards of equalization and Chapter 21 of Title 58 dealing with delinquent taxes on land and tax titles could also be repealed if the real estate tax is eliminated. However, these changes are only the ones that are readily apparent at first glance. Other changes throughout the body of the Code of Virginia would be necessary upon the elimination of the property tax and an increase in the rate of sales and income taxes.

The effects of such a change in the basic tax structure of the Commonwealth are patently far-reaching and I do not recommend that such changes be initiated without through in-depth study to determine the feasibility of such action. However, that is the charge this Revenue Resources and Economic Commission is now undertaking.

Evidence has shown that the property tax is in disfavor with the public and is based on an unscientific method of periodic assessment. Recent increases in property assessments and tax rates have made the property tax a barrier to home ownership for some citizens. It is estimated that the income tax which is based on self-reporting is about 98% honest. Also, the sales tax has proved able to reach the large majority of sales.

The duration of the search for suitable alternatives to the property tax will probably go on for a long time, probably beyond my lifetime, and prove to be very complex and controversial. However, I believe that the evidence presented to this Commission mandates that we continue our in-depth study of the feasibility of the elimination of the local property tax, a search for alternative bases of taxation and a study of the effects of the use of such bases on the taxpayers of the Commonwealth.

The local real estate tax field is so filled with inequities that medication cannot help it. Surgery is required to do justice. That is what this statement proposes.



STANLEY A. OWENS

Partial Dissent by Owen B. Pickett

I have reviewed the draft copy of the Report to the Governor and General Assembly by the Revenue Resources and Economic Commission and return herewith the signature page of the report which I have signed, although I do not concur with the recommendation in the report that public service corporation property be assessed and taxed as a separate class of property until 1986.

While we have undertaken a program to simplify and improve the assessment and collection of property taxes, this recommendation would have us start making exceptions at the very onset of a new program, which does not appear to me to be desirable, inasmuch as there are other alternatives for resolving this problem. The assessment and collection of taxes on public service corporation property already requires too much time of the State and local governments and it is my recommendation that public service corporation property be assessed and taxed by each locality the same as other property is assessed and taxed in that locality.

With the foregoing exception, I approve the draft copy of the Report of the Commission.

Appendix

EXHIBIT 1

3 A BILL to amend and reenact §§ 58-512.1 and 58-760 of the
4 Code of Virginia, relating to assessments and rates of
5 taxation.

6

7 Be it enacted by the General Assembly of Virginia:

8 1. That §§ 58-512.1 and 58-760 of the Code of Virginia are

9 amended and reenacted as follows:

10 § 58-512.1. Increase in assessed valuation.--_A._ Any

11 increase in the assessed valuation of any public service

12 corporation property in any taxing district shall be made by

13 application of the local assessment ratio prevailing in such

14 taxing district for other real estate as determined by the

15 most recently published findings of the Department of

16 Taxation; provided, however, that on January one, nineteen

17 hundred sixty-seven, one twentieth, and on each subsequent

18 January one for nineteen years an additional one twentieth,

19 of the assessed valuation on January one, nineteen hundred

20 sixty-six, (reduced by forty per centum of the value of the

21 amount, if any, by which total retirements since January

22 one, nineteen hundred sixty-six, exceed total additions

23 since that date), shall be assessed by application of the

24 local assessment ratio as provided above, and the remainder

25 shall continue assessed by application of the forty per

26 centum assessment ratio as heretofore administered.

27 Thereafter the whole shall be assessed by application of the

1 local assessment ratio as provided above provided however,
2 such property will be assessed at its fair market value at
3 the time of each assessment.
4 B. Notwithstanding any provision of subsection A., when the
5 assessment of property in any taxing district is made at one
6 hundred percent fair market value as provided in § 58-760,
7 the State Corporation Commission shall certify its
8 assessment to such taxing district for imposition of the
9 local tax rate. Beginning January one, nineteen hundred
10 seventy-six, all public service corporation property in the
11 process of equalization over a twenty-year period as
12 provided in subsection A., shall be defined as a separate
13 item of taxation and shall constitute a classification for
14 local taxation separate from other classifications of
15 property. Such property in the process of equalization
16 shall, for such period as provided for in subsection A.
17 continue to be assessed at forty percent of the fair market
18 value and taxed at the nominal rate applicable to public
19 service corporation property for the taxable year nineteen
20 hundred seventy-five; provided, however, that any county,
21 city or town may increase any such nominal rate, if the
22 effective rate for such separate class of public service corporation
23 property is lower than the effective tax rate applicable for other
24 classifications of property in that locality so that the effective
25 rate on the separate class of public service corporation property
26 is never less than the effective rate on all other classes of property.
27 C. On request of any local taxing district in connection
28 with any reassessment of property representatives of the
State Corporation Commission shall consult with

1 representatives of the district with regard to ascertainment
2 and equalization of values to help assure uniformity of
3 appraisals and assessments in accordance with the provisions
4 of this section.
5 § 58-760. What real estate to be taxed;assessment at
6 one hundred percent fair market value. --All real estate,
7 except such as is exempted by law, shall be subject to such
8 annual taxation as may be prescribed by law.
9 Beginning January one, nineteen hundred seventy-six,
10 all assessments of real estate shall be made at one hundred
11 percent fair market value. Any county or city, which prior
12 to January one, nineteen hundred seventy-six applied a fixed
13 multiple or percentage to fair market value in order to
14 derive the assessed value of property, shall lower the rate
15 of tax levy by such an amount that the aggregate real estate
16 tax payable would equal the amount of tax as would be payable
17 prior to assessment at one hundred percent fair market
18 value.
19 #

EXHIBIT 2

2 A BILL to amend the Code of Virginia by adding a section
3 numbered 58-817.1, relating to property record cards.

4

5 Be it enacted by the General Assembly of Virginia:

6 1. That the Code of Virginia is amended by adding a section

7 numbered 58-817.1 as follows:

8 § 58-817.1. Property record cards; required data.--Any

9 county or city assessor or other officer charged with the

10 assessment of real estate who maintains property record

11 cards shall include thereon the appraised value of the

12 property and improvements, if any, and the calculations used

13 in determining the assessed value of such property and

14 improvements.

15 #

EXHIBIT 3

3 A BILL to amend the Code of Virginia by adding a section
4 numbered 58-792.02, providing for public disclosure of
5 certain assessment records.

7 Be it enacted by the General Assembly of Virginia:

8 1. That the Code of Virginia is amended by adding a section

9 numbered 58-792.02 as follows:

10 § 58-792.02. Public disclosure of certain assessment

11 records.—A. Notwithstanding the provisions of § 58-46, all

12 property record cards, within the custody of a county or

13 city assessor or other officer charged with the assessment

14 of real estate, shall, during the normal office hours of

15 such official, be open for inspection by any person desiring

16 to review such cards.

17 B. Any person, whose real property has been assessed

18 for taxation, shall, upon request, be allowed to examine the

19 working papers used by any such assessing official in

20 arriving at the appraised and assessed value of such

21 person's land and improvements thereon, if any.

22 #

EXHIBIT 4

3 A BILL to amend and reenact § 58-792.01, as amended, of the
4 Code of Virginia, relating to notice of increase in
5 real estate assessments.

6

7 Be it enacted by the General Assembly of Virginia:

8 1. That § 58-792.01, as amended, of the Code of Virginia is

9 amended and reenacted as follows:

10 § 58-792.01. Notice of increase in

11 assessment.--Whenever in any county, city or town there is a

12 reassessment of real estate, or any change in the assessed

13 value of any real estate, notice shall be given by mail to

14 each landowner to whom tax bills are sent, as shown by the

15 land books of the county, city or town whose assessment has

16 been increased. Such notice shall be sent by postpaid mail

17 at least fifteen days prior to the date of a hearing to

18 protest such increase to the address of the landowner as

19 shown on such land books. The governing body of the county,

20 city or town shall require the officer of such county, city

21 or town charged with the assessment of real estate to send

22 such notices or it shall provide funds or services to the

23 persons making such reassessment so that such persons can

24 send such notices.

25 Every notice shall, among other matters, show the

26 magisterial or other district, if any, in which the real

1 estate is located, the-~~amount-and-the~~ new-~~assessed~~
2 appraised value of land-~~and~~ , the new-~~assessed~~ appraised
3 value of improvements , the new assessed value of each if
4 different from the appraised value, and the assessment ratio
5 employed by the locality . It shall further set out the
6 time and place at which persons may appear before the
officers making such reassessment or change and present
8 objections thereto.

9 Any-~~person~~ tenant , who receives a tax-~~bills-on-behalf~~
10 ~~of~~ bill addressed to the-~~owners~~ owner of the real property
11 such tenant is occupying , shall transmit such notice to
12 such owner if that address be known immediately on receipt
13 thereof. As used in this section, "tenant" shall mean a
14 person who is temporarily using or occupying the real
15 property of another.
16

EXHIBIT 5

3 A BILL to amend the Code of Virginia by adding a section
4 numbered 58-14.1, relating to annual applications for
5 exempt property.

6

7 Be it enacted by the General Assembly of Virginia:

8 1. That the Code of Virginia is amended by adding a section

9 numbered 58-14.1 as follows:

10 § 58-14.1. Annual application for exempt

11 property.--The governing body of any county, city or town by

12 local ordinance may require any organization or association

13 owning real property exempt under § 58-12 et. seq. to

14 annually file an application with the commissioner of the

15 revenue as a requirement for retention of the exempt status

16 of the property. Such application shall show the ownership

17 and usage of such property.

18 #

EXHIBIT 6

3 A BILL to amend the Code of Virginia by adding a section
4 numbered 58-14.1, relating to certain tax exempt
5 information.

6

7 Be it enacted by the General Assembly of Virginia:
8 1. That the Code of Virginia is amended by adding a section
9 numbered 58-14.1 as follows:
10 § 58-14.1. Tax exemption information.--The county,
11 city or town assessor or other officer charged with the
12 assessment of real estate shall regularly inventory and
13 assess all tax exempt real property and all such property
14 immune from real estate taxation within his county, city or
15 town, excluding streets, highways and other roadways. Such
16 official shall identify such property by a general site
17 description indicating the owner thereof and report such
18 information on the land book along with an appraisal of the
19 fair market value of such property, the total assessed
20 valuation for each type of exemption and a computation of
21 total tax which would be due if such property were not
22 exempt. A total of such assessed valuations and a
23 computation of the percentage such exempt and immune
24 property represents in relation to all property assessed
25 within the county, city or town shall be published annually
26 by such local assessing official.
27 #

EXHIBIT 7

3 A BILL to amend the Code of Virginia by adding a section
4 numbered 58-33.1, providing for the collection and
5 publication of certain real property tax data.

6

7 Be it enacted by the General Assembly of Virginia:

8 1. That the Code of Virginia is amended by adding a section

9 numbered 58-33.1 as follows:

10 § 58-33.1. Collection and publication of property tax

11 data.--A. The Commissioner annually shall make and issue

12 comprehensive assessment sales ratio studies of the average

13 level of assessment, the degree of assessment uniformity and

14 overall compliance with assessment requirements for each

15 major class of real property in each county, city and town

16 in the Commonwealth. In order to determine the degree of

17 assessment uniformity and compliance in the assessment of

18 major classes of property within each county, city and town,

19 the Commissioner shall compute measures of central tendency

20 and dispersion in accordance with appropriate standard

21 statistical analysis techniques.

22 B. The Commissioner shall construct and maintain his

23 system for the collection and analysis of real property tax

24 facts so as to enable him to make intra-jurisdictional

25 comparisons as well as intercounty, intercity and intertown

26 comparisons based on property tax and assessment sales ratio

27 data.

1 C. The Commissioner shall publish annually the findings
2 of the assessment sales ratio studies.
3 D. The county, city or town assessor or other officer
4 charged with the assessment of real estate shall post
5 annually in his office the assessment sales ratio studies as
6 published by the Commissioner.
7 #

EXHIBIT 8

A BILL directing the State Tax Commissioner to establish classifications for real property.

Be it enacted by the General Assembly of Virginia:

1. § 1. The State Tax Commissioner shall establish a classification system of real property appropriate for the inclusion on local land books. Such classification shall be placed on local land books or shall be organized in a manner appropriate for identification by the Commissioner in conducting the annual sales-ratio study for the year nineteen hundred seventy-six and each year following. The commissioner of the revenue of any county, city or town may divide these categories of classifications into lesser included classifications should he deem such classifications desirable.

#

EXHIBIT 9

2 A BILL to amend the Code of Virginia by adding a section
3 numbered 58-33.1, so as to provide a continuing
4 education program for assessing officers.

5

6 Be it enacted by the General Assembly of Virginia:

7 1. That the Code of Virginia is amended by adding a section

8 numbered 58-33.1 as follows:

9 § 58-33.1. Continuing education program for assessing

10 officers.--There shall be established within the Department

11 of Taxation a program of continuing education for county,

12 city or town officers responsible for the assessment of real

13 estate. Such program shall be composed of a basic course

14 embodying the fundamental instruction essential for the

15 equitable assessment of real estate and an advanced course

16 designed basically to meet the requirements for full

17 certification by the International Association of Assessing

18 Officers. Attendance in the program shall be mandatory for

19 all such assessing officials. Such officials shall be

20 reimbursed for the actual expenses incurred by their

21 attendance at such program.

22 #

EXHIBIT 10

2 A BILL to amend and reenact § 58-618 of the Code of
3 Virginia; and to amend the Code of Virginia by adding
4 in Chapter 12 of Title 58 an article numbered 11.1,
5 consisting of sections numbered 58-626.2 through
6 58-626.4; and to repeal § 46.1-32.1 of the Code of
7 Virginia, the amended, added and repealed sections
8 relating generally to the rolling stock of certain
9 motor vehicle carriers.

10

11 Be it enacted by the General Assembly of Virginia:
12 1. That § 58-618 of the Code of Virginia is amended and
13 reenacted, and that the Code of Virginia is amended by
14 adding in Chapter 12 of Title 58 an article numbered 11.1,
15 consisting of sections numbered 58-626.2 through 58-626.4,
16 as follows:
17 § 58-618. Reports of carriers.--Every certificated
18 motor vehicle carrier operating in this State, engaged in
19 the business of transporting people, shall report annually
20 on or before the first day of March to the Commission:
21 (1) All of its rolling stock, owned or operated as of
22 the beginning of the first day of January next preceding,
23 which shall include all busses, trucks, tractor trucks,
24 trailers and semi-trailers and all other equipment which it
25 is reasonably proper to class as rolling stock and which has
26 been, is now or shall be used directly or indirectly in the
27 transportation of persons ~~or property~~ on the public highways
28 of the State.
29 (2) The total vehicle miles traveled by the rolling

1 stock of such carriers in this State during the twelve
2 months ending December thirty-first next preceding.
3 (3) The total vehicle miles traveled by the rolling
4 stock of such carriers both within and without this State on
5 such operations as are related to this State, whether the
6 same be in the course of business conducted wholly
7 intrastate or whether in the course of business conducted
8 partly within and partly outside this State, during the
9 twelve months ending December thirty-first preceding.

10 Article 11.1.

11 Personal Property Taxation of

12 Motor Vehicle Carriers and Trailers.

13 § 58-626.2. Definitions.--The following words and
14 phrases when used in this article shall, for the purpose of
15 this article, have the meanings respectively ascribed to
16 them:
17 A. "Cost".--Price paid at the time of original purchase
18 from the manufacturer or dealer including any accessories or
19 options attached to the motor vehicle carrier or trailer,
20 but excluding any sum charged for titling by the State or
21 preparation by the dealer.
22 B. "Motor Vehicle Carrier".--Every motor vehicle
23 designed for the transportation of property except a pick-up
24 or panel truck not used or operated for hire.
25 C. "Pick-up or panel truck".--Shall be defined pursuant
26 to the provisions of § 46.1-1(20a).
27 D. "Pick-up or panel truck not used or operated for
28 hire".--A pick-up or panel truck used or operated by the

1 owner thereof for the transportation of property for which
2 no direct compensation will be received.
3 E. "Situs".--Domiciliary for purposes of taxation
4 pursuant to the provisions of § 58-834.
5 F. "Trailer".--Every vehicle without motive power
6 having a gross weight greater than two thousand pounds,
7 designed for carrying property wholly on its own structure
8 and for being drawn by a motor vehicle.
9 § 58-626.3. Duties of the Commissioner of the Division
10 of Motor Vehicles; assessment of motor vehicle carriers and
11 trailer.--The Commissioner of the Division of Motor Vehicles
12 shall, before issuance of any registration or certificate of
13 title for any motor vehicle carrier or trailer, except a
14 pick-up or panel truck not used or operated for hire, obtain
15 the cost of such motor vehicle carrier or trailer and its
16 situs. On or before January one of each year, the
17 Commissioner of the Division of Motor Vehicles shall forward
18 the cost of such motor vehicle carrier or trailer to
19 locality entered as the situs of such carrier or trailer.
20 Upon receiving such cost from the Commissioner of the
21 Division of Motor Vehicles, the commissioner of the revenue
22 of each locality shall determine the amount of tax due
23 thereon by applying the local depreciation schedule to such
24 cost and by using the appropriate tax rate of his respective
25 county, city or town. The commissioner of the revenue shall
26 then notify the owners of such carrier or trailer of the
27 amount of tax due thereon. Revenues received by the
28 commissoner of the revenue from the taxation of motor

1 vehicle carriers or trailers, pursuant to the provisions of
2 this section, shall be deposited in the treasury of his
3 respective county or city.
4 § 58-626.4. Procedure for judicial review.--Any person
5 aggrieved by the assessment under the provisions of this
6 article shall be entitled to review thereof in the manner
7 prescribed by law for local levies (§§ 58-1141 et.seq.).
8 2. That § 46.1-32.1 of the Code of Virginia is repealed.
9 3. That the provisions of this act shall be effective on
10 and after January one, nineteen hundred seventy-seven.
11 #

EXHIBIT 11

2 A BILL to amend and reenact § 58-266.1, as amended, of the
3 Code of Virginia, relating to local license taxes.

4

5 Be it enacted by the General Assembly of Virginia:

6 1. That § 58-266.1, as amended, of the Code of Virginia is

7 amended and reenacted as follows:

8 § 58-266.1. Cities, towns and counties may impose local

9 license taxes; limitation of authority.--_A._ The council of

10 any city or town, and the governing body of any county, may

11 levy and provide for the assessment and collection of city,

12 town or county license taxes on businesses, trades,

13 professions, occupations and callings and upon the persons,

14 firms and corporations engaged therein within the city, town

15 or county, whether any license tax be imposed thereon by the

16 State or not, subject to the following limitations:

17 (1) No city, town or county shall levy any license tax

18 in any case in which the levying of a local license tax is

19 prohibited by any general law of this State, or on any

20 public service corporation except as permitted by other

21 provisions of law, nor shall this section be construed as

22 repealing or affecting in any way any general law limiting

23 the amount or rate of any local license tax.

24 (2) No city, town or county shall impose upon or

25 collect from any person any tax, fine or other penalty for

26 selling farm or domestic products or nursery products,

1 ornamental or otherwise, or for the planting of nursery
2 products, as an incident to the sale thereof, within the
3 limits of any such town, county or city outside of the
4 regular market houses and sheds of such city, county or
5 town; provided, such products are grown or produced by such
6 person.

7 (3) No city, town or county shall require a license to
8 be obtained for the privilege or right of printing or
9 publishing any newspaper, or for the privilege or right of
10 operating or conducting any radio or television broadcasting
11 station or service, any municipal charter provisions to the
12 contrary notwithstanding.

13 (4) No city, town or county shall levy any license tax
14 on a manufacturer for the privilege of manufacturing and
15 selling goods, wares and merchandise at wholesale at the
16 place of manufacture, whether the same be measured by gross
17 receipts or otherwise, any city or town charter provisions
18 to the contrary notwithstanding; provided, that any city,
19 town or county which imposed such a tax prior to January
20 first, nineteen hundred sixty-four may continue it until
21 January first, nineteen hundred sixty-nine at the same or
22 reduced rates.

23 (5) Whenever any county imposes a county license tax on
24 merchants, the same shall be in lieu of a county property
25 tax on the capital of merchants, as defined by § 58-833.

(6) No city, town or county shall levy a tax upon a
27 wholesaler for the privilege of selling goods, wares and
28 merchandise to other persons for resale unless said

1 wholesaler has a definite place of business or store in said
2 city, town or county, but the foregoing shall not be
3 construed as prohibiting any city, town or county from
4 imposing a local license tax on a peddler at wholesale who
5 is subject to a State license tax under article 10 (Sec.
6 58-346 et seq.) of this chapter.
7 (6a) Notwithstanding any provision of law, general or
8 special, no city, town or county shall levy any license tax
9 upon any person, firm or corporation for engaging in the
10 business of renting, as the owner of such property, real
11 property other than hotels, motels, motor lodges, auto
12 courts, tourist courts, trailer parks, lodging houses,
13 rooming houses and boardinghouses; provided, however, that
14 any county, city or town having such a license tax on
15 January one, nineteen hundred seventy-four, shall not be
16 precluded from the levy of such tax by the provisions of
17 this subsection.
18 (7) Any county license tax imposed hereunder shall not
19 apply within the limits of any town located in such county,
20 where such town now, or hereafter, imposes a town license
21 tax on the same privilege; provided, however, that if the
22 governing body of any town within a county, which county has
23 a population of at least fourteen thousand six hundred fifty
24 but not in excess of fourteen thousand seven hundred, shall
25 provide that a county license tax shall apply within the
26 limits of such town, then such license tax may be imposed
27 within such town.
28 (8) Before issuing any license to do business as a tour

1 guide or tourist guide, the city council or the board of
2 supervisors may require that an applicant take and pass an
3 examination to determine the fitness of such person as to
4 his knowledge of the history of the city or the county and
5 of the historical and tourist attractions located therein.
6 (9) Gross receipts for license tax purposes shall not
7 include any amount paid to the State or any county, city or
8 town for the Virginia retail sales or use tax, for any local
9 sales tax or any local excise tax on cigarettes.
10 B. No local license tax, imposed pursuant to the
11 provisions of this section, shall be greater than such rate
12 as levied by such city, town or county on December
13 thirty-one, nineteen hundred seventy-four. Any city, town or
14 county, increasing such tax after December thirty-one,
15 nineteen hundred seventy-four, but prior to the effective
16 date of this subsection, to a rate greater than the levy
17 applicable on such date, shall roll back such taxes to the
18 December thirty-one, nineteen hundred seventy-four rate and
19 refund any amount in excess thereof.
20 The provisions of this subsection shall cease to be of
21 any force or effect on December thirty-one, nineteen hundred
22 seventy-six, unless extended by the General Assembly of
23 Virginia.
24 #

EXHIBIT 12

ANDREW P. MILLER
ATTORNEY GENERAL

M. HARRIS PARKER
CHIEF DEPUTY ATTORNEY GENERAL

RENO S. HARP, III
GERALD L. BALILES
ANTHONY F. TROY
WALTER A. McFARLANE
DEPUTY ATTORNEYS GENERAL

OFFICE OF THE ATTORNEY GENERAL
SUPREME COURT BUILDING
1101 EAST BROAD STREET
RICHMOND, VIRGINIA 23219
804-770-2071

WILLIAM P. BAGWELL, JR.
A. P. WOODROOF
WALTER H. RYLAND
JAMES E. KULP
HENRY M. MASSIE, JR.
FREDERICK S. FISHER
STUART H. DUNN
RICHARD K. C. SUTHERLAND
JOHN W. CREWS
D. PATRICK LACY, JR.
ROBERT E. SHEPHERD, JR.
GILBERT W. HAITH
BURNETT MILLER, III
DAVID T. WALKER
WALTER A. MARSTON, JR.
LINWOOD T. WELLS, JR.
KATHERINE L. GOOLSBY
WILBURN C. DIBLING, JR.
KAREN C. KINCANNON
CHARLES K. TRIBLE
GILMAN P. ROBERTS, JR.
J. THOMAS STEGER
JOHN J. BEALL, JR.
THOMAS F. HANCOCK, JR.
STACY F. GARRETT, III
JOSEPH D. FELTON, III
JAMES E. MOORE
JAMES E. RYAN, JR.
JOHN B. PURCELL, JR.
FRANCIS A. CHERRY, JR.
W. THOMAS HUDSON
JAMES W. HOPPER
PAUL L. GERGOUDIS
WALTER L. PENN, III
WILLIAM B. LISSNER
MICHAEL M. WEISE
M. STUART BATEMAN
ALAN KATZ
VALENTINE W. SOUTHALL, JR.
JIM LAI CHIN
MARY YANCEY SPENCER
ASSISTANT ATTORNEYS GENERAL

December 9, 1974

The Honorable Leroy S. Bendheim
Member, Senate of Virginia
Post Office Box 156
Alexandria, Virginia 22313

My dear Senator Bendheim:

This is in response to your recent request for my opinion on the constitutionality of separate tax classification of real estate owned by public service corporations. Specifically, you ask whether the General Assembly may provide for the assessment of public service corporation property under § 58-512.1 of the Code of Virginia (1950), as amended, through 1986, while requiring that all other real property be assessed at fair market value as of January 1, 1976. The proposed legislation would provide for a proportional decrease in the nominal tax rate for all real property assessed at fair market value, and a higher tax rate on that public service corporation property which is assessed at 40% through 1986 under § 58-512.1. The legislation would not change the existing relationship between the effective rates applicable to the property of public service corporations and the effective rates applicable to other real estate in the locality.

The United States Constitution does not prohibit state legislatures from making reasonable separate classifications of the property of public service corporations for purposes of taxation. Atlantic Coast Line R. Co. v. Doughton, 262 U.S. 413 (1923). Unless, on the facts, a

The Honorable Leroy S. Bendheim
Page 2
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particular classification is shown to be unreasonable, it is not prohibited by the United States Constitution. See also City of Richmond v. Comm., 188 Va. 600, 50 S.E.2d 654 (1948). In the present instance, I am unaware of any facts which would render the classification unreasonable.

Article X, Section 1, of the Constitution of Virginia provides in relevant part:

> "All taxes shall be levied and collected under general laws and shall be uniform upon the same class of subjects within the territorial limits of the authority levying the tax ...
>
> ***
>
> "The General Assembly may define and classify taxable subjects."

The General Assembly has classified public service corporation property separately for tax purposes. See §§ 58-512.1, 58-514.2.

Section 58-512.1 was designed "to equalize gradually, over a period of twenty years, the assessment of all public service corporation property with the respective ratios in force in localities where the properties are located." Southern Ry. v. Comm., 211 Va. 210, 218, 176 S.E.2d 578 (1970). This section does not violate the constitutional requirement of assessment at fair market value as this requirement has been interpreted by the Virginia Supreme Court. See my opinion to the Honorable Peter K. Babalas, dated March 30, 1973, and found in the Report of the Attorney General (1972-1973), p. 377. Section 58-512.1 does not violate the constitutional requirements of uniformity and equality. Southern Ry. v. Comm., supra. See City of Richmond v. Comm., supra, and my opinion to the Honorable J. Samuel Glasscock, dated June 14, 1974, and found in the Report of the Attorney General (1973-1974), p. 388.

The legislative proposal about which you inquire is intended to end the practice in Virginia localities of assessing real property at a fraction of fair market value and applying a higher tax rate. It is also intended to preserve the

gradual equalization of tax rates applicable to public service corporations with those which apply to real estate rates generally. Because the classification of which you inquire is constitutional in the context of assessments in relation to fair market value, and because it would not change the existing relationship between the effective rates applied to the property of public service corporations and other real estate in the locality, the proposal about which you inquire is constitutional.

With kindest regards, I remain

Sincerely yours,

Andrew P. Miller
Attorney General

5:40

EXHIBIT 13

AMENDMENT IN THE NATURE OF
A SUBSTITUTE FOR SENATE BILL NO. 59

A BILL

To amend and reenact § 58-219, as amended, of the Code of Virginia, relating to gift taxes.

Be it enacted by the General Assembly of Virginia:

1. That § 58-219, as amended, of the Code of Virginia be amended and reenacted as follows:

§ 58-219. Classification of beneficiaries; exemptions and rates of tax. (a) For the purposes of this chapter, the classification of beneficiaries, their exemptions and the rates of taxation shall be as follows:

Class A. The father, mother, grandfathers, grandmothers, husband, wife, children by blood or by legal adoption, stepchildren, grandchildren and all other lineal ancestors and lineal descendants of the donor shall constitute Class A.

Except as provided in paragraph (b) hereof, so much of such property as has the actual value of five thousand dollars and so passes to or for the use of any Class A beneficiary shall be exempt from taxation hereunder.

So much of such property as shall so pass to or for the use of a Class A beneficiary shall be subject to a tax of one per centum of the actual value of so much thereof as is in excess of five thousand dollars and is not in excess of fifty thousand dollars; to a tax of two per centum upon so much thereof as is in excess of fifty thousand dollars and is not in excess of one hundred thousand dollars; to a tax of three per centum upon so much thereof as is in excess of one hundred thousand dollars and is not in excess of five hundred thousand dollars; to a tax of four per centum upon so much thereof as is in excess of five hundred thousand dollars and is not in excess of one million dollars; and to a tax of five per centum upon all in excess of one million dollars.

Class B. The brothers, sisters, nephews and nieces of the whole or half blood of the donor shall constitute Class B.

Except as provided in paragraph (b) hereof, so

much of such property as has the actual value of two thousand dollars and so passes to or for the use of any Class B beneficiary shall be exempt from taxation hereunder.

So much of such property as shall so pass to or for the use of a Class B beneficiary shall be subject to a tax of two per centum of the actual value of so much thereof as is in excess of two thousand dollars and is not in excess of twenty-five thousand dollars; to a tax of four per centum upon so much thereof as is in excess of twenty-five thousand dollars and is not in excess of fifty thousand dollars; to a tax of six per centum upon so much thereof as is in excess of fifty thousand dollars and is not in excess of one hundred thousand dollars; to a tax of eight per centum upon so much thereof as is in excess of one hundred thousand dollars and is not in excess of five hundred thousand dollars; and to a tax of ten per centum upon all in excess of five hundred thousand dollars.

Class C. Grandnephews and grandnieces of the donor and all persons other than members of Classes A and B and all firms, institutions, associations and corporations shall constitute Class C.

Except as provided in paragraph (b) hereof, so

much of such property as has the actual value of one thousand dollars and so passes to or for the use of any Class C beneficiary shall be exempt from taxation hereunder.

So much of such property as shall so pass to or for the use of a Class C beneficiary shall be subject to a tax of five per centum of the actual value of so much thereof as is in excess of one thousand dollars and is not in excess of twenty-five thousand dollars; to a tax of seven per centum upon so much thereof as is in excess of twenty-five thousand dollars and is not in excess of fifty thousand dollars; to a tax of nine per centum upon so much thereof as is in excess of fifty thousand dollars and is not in excess of one hundred thousand dollars; to a tax of twelve per centum upon so much thereof as is in excess of one hundred thousand dollars and is not in excess of five hundred thousand dollars; and to a tax of fifteen per centum upon all in excess of five hundred thousand dollars.

(b) The exemptions provided herein shall not be applicable to any gift if the donor thereof has made gifts during his lifetime totaling thirty thousand dollars in value.

2. This Act shall be effective for all gifts made on and after January 1, 1976.

EXHIBIT 14

COMMONWEALTH OF VIRGINIA
GOVERNOR'S OFFICE
DIVISION OF INDUSTRIAL DEVELOPMENT
STATE OFFICE BUILDING
RICHMOND, VIRGINIA 23219
PHONE (804) 770-2660

J. FRANK ALSPAUGH
DIRECTOR

July 29, 1974

Date Received by Research Division
JUL 31 1974

Mr. Barry E. Lipman
Director of Research
Virginia Department of Taxation
State Office Building
Richmond, Virginia 23219

Dear Barry:

I am happy to reply to the questions you raised in your recent conversations with Ed Holm and Peggy Ware. I see no serious problem affecting our competitive position in attracting new industry if the General Assembly repeals the part of the tax law which permits dividends of certain Virginia corporations paid to Virginia individuals and corporations to be excluded from taxation.

First, there are very few manufacturing firms headquartered in Virginia which would have subsidiaries here paying dividends to the parent. Second, since the federal government excludes 85 percent of domestic intercorporation dividends from taxation and Virginia tax law conforms with the federal, we are talking about an extremely small portion of dividends that would be affected. State tax officials have assured us that additional taxes paid by corporations will be small if the change is made. Third, as I understand the proposal, the real effect of this change will fall on individuals.

With regard to future capital issues, I think the proposed change would have little effect on manufacturing operations in their process of raising new capital. I do believe, however, that it might impair capital issues of Virginia utilities and banks since a large number of Virginia citizens own shares in these corporations. I am sure that such companies follow the deliberations of the General Assembly closely and will bring their own individual cases to members of the General Assembly if they are strongly opposed to the change.

Since the Revenue Resources and Economic Study Commission will be studying dividend taxation, there are two related problems confronting our industrial development program which I would like to call to your attention. The first problem concerns the taxation of a Domestic International Sales Corporation, known as a DISC. The federal government devised the Domestic International Sales Corporation to encourage United States companies to

expand their production facilities and payrolls within the U. S., rather than overseas. From a federal income tax standpoint, a DISC effectively pays federal tax on 50 percent of its income. Under present Virginia law, a DISC effectively pays state tax on 100 percent of its income. Under Senate Bill 61 introduced at the last session of the General Assembly a DISC would effectively pay a state income tax on 150 percent of its income. None of these percentages take into consideration certain exclusions that are provided under state and federal tax laws.

It is my understanding that an amendment to Senate Bill 61 was presented to Counsel for the Finance Committee. The Amendment called for a DISC to be treated as it has in the past under Virginia law; that is, it would effectively pay 100 percent of the usual tax. In my opinion, this is the least that should be done. Since such an amendment was proposed, I think it would be the proper spirit for Virginia to give a DISC the same proportionate tax break that the federal government does and reduce this tax to an effective 50 percent, particularly in view of our aggresive and successful international program. Any revenue loss would be negligible if Virginia conformed to the federal treatment of DISCs.

I mentioned one other problem which puts Virginia at a serious competitive disadvantage. When we seek to attract corporate headquarters from the New York area, including New York, New Jersey, and Connecticut, we are faced with the fact that the large multi-national corporations pay very little attention to our invitations because we tax 100 percent of the dividends received from overseas sources. This is the same as the federal government's treatment. New York and Connecticut, while having a higher corporate income tax rate than Virginia, and in some instances a city income tax as well, and New Jersey give substantial dividend exclusions on dividends which come from foreign sources. This makes our efforts to attract such corporate headquarters fruitless. These companies would be prime corporate citizens for our State. However, we have had modest success in attracting some of the administrative support facilities of corporate headquarters. Perhaps the Revenue Resources and Economic Study Commission can study the feasibility of changing the law to make our State more attractive to corporate headquarters. Particular attention should be paid to the taxing procedures of North Carolina and Maryland, who represent our closest competition, when we are promoting such areas as northern Virginia, Richmond, and Norfolk for corporate headquarters locations.

I hope my comments will be helpful.

Sincerely,

J. Frank Alspaugh

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