COMMONWEALTH of VIRGINIA

Department of Taxation

October 1, 2025

TO: The Honorable L. Louise Lucas
Chairwoman, Senate Finance and Appropriations Committee

The Honorable Luke E. Torian
Chairman, House Appropriations Committee

The Honorable Vivian E. Watts
Chairwoman, House Finance Committee

FROM: James J. Alex
State Tax Commissioner

During the 2025 Session, the General Assembly enacted House Bill 1743 (2025 Acts of Assembly, Chapter 192), which required the Department of Taxation ("the Department") to convene a workgroup to review the local license tax ("BPOL") deduction in Virginia for receipts attributable to out-of-state business. The report of the study is enclosed.

If you have any questions or comments regarding the study or the enclosed report, please do not hesitate to contact me.

C: The Honorable Stephen E. Cummings, Secretary of Finance

Workgroup To Review Business, Professional, and Occupational Licensing Deduction for Receipts Attributable to the Out-of-State Business

Department of Taxation

October 1, 2025

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Executive Summary

2025 House Bill 1743 (*2025 Acts of Assembly*, Chapter 192) requires the Department of Taxation ("the Department") to convene a workgroup to review the local Business, Professional, and Occupational License tax ("BPOL") deduction in Virginia for receipts attributable to out-of-state business, including a review of:

- Current policy and methodology of the deduction set forth in Subsection B 2 of *Virginia Code* § 58.1-3732;
- Any constitutional or case law concerns regarding the existing laws governing such deduction;
- Any potential impact on local government revenue as a result of determining such deduction based upon receipts subject to a net income tax or gross receipts tax in another state or foreign jurisdiction and alternatives to phase in any such potential impact;
- The potential administrative complexities or benefits for taxpayers and the support structure necessary to verify across local jurisdictions the applicable deduction and to enforce compliance; and
- Any impact to such deduction from other existing provisions of law.

The workgroup was required to consist of individuals with experience in local license tax compliance and enforcement, including representatives of:

- The Virginia Municipal League,
- The Virginia Association of Counties,
- The Commissioners of the Revenue Association of Virginia,
- The Virginia Society of Certified Public Accountants,
- The Council on State Taxation,
- The Virginia Chamber of Commerce, and
- Any other key business tax representatives as determined by the Department.

The legislation requires the Department to submit a report of the findings and recommendations, if any, of the workgroup to the Joint Subcommittee on Tax Policy and to the Chairs of the Senate Finance and Appropriations and House Appropriations Committees by October 1, 2025.

Virginia Code § 58.1-3732 (B)(2) provides that any receipts attributable to business conducted in another state or foreign country in which the taxpayer (or its shareholders, partners, or members in lieu of the taxpayer) is liable for an income or other tax based upon income are deductible from gross receipts or gross purchases for license tax purposes. The Department is authorized by *Virginia Code* § 58.1-3703.1 to issue determinations on taxpayer appeals of BPOL assessments. The Department's rulings on the scope of the deduction have clarified that the deduction is available for taxes paid to other states that are based on income regardless of whether such taxes are called an

"income tax" but the out-of-state taxes being deducted must be assessed on net income to be deductible.

The Department convened a meeting with workgroup members on June 3, 2025. The workgroup discussed all of the legislatively mandated topics related to the out-of-state BPOL deduction. While the participants engaged in frank and productive discussion, no consensus was reached to an extent that would permit the Department to make any recommendations in this report except that consistency, clarity, and fairness are all vital to the administration of BPOL and should be central to any action taken to change the deduction administratively or legislatively. On a broader level, all participants in the work group seem to support clarity in the statute and consistency in its interpretation, fairness for multi-jurisdictional businesses, and solutions that would ease the administrative burden related to both the enforcement and compliance sides of the deduction.

Background

Local License Taxes in Virginia

BPOL is a tax for the privilege of engaging in business at a definite place of business within a Virginia locality. BPOL tax is currently imposed in all 39 cities, 48 of the 95 counties, and many of the towns in the Commonwealth. The measure or basis of BPOL tax generally is the gross receipts of the business. However, current law allows localities to assess BPOL tax on either gross receipts or the Virginia taxable income of a business.

Under current law, any locality may charge a license fee in an amount not to exceed $50 for any locality with a population of 25,000 or greater or $30 for any locality with a population smaller than 25,000. However, a locality may not assess a license tax on gross receipts upon which it charges a license fee. Additionally, the locality may not impose a license tax on a business with gross receipts less than $100,000 in any locality with a population greater than 50,000 and less than $50,000 in any locality with a population of 25,000 but no more than 50,000.

Situs Rules

Situs generally refers to the locality in which a person subject to local license taxation for any business, profession, trade, occupation or calling has a definite place of business. If the person has a definite place of business in any other locality, then the other locality may impose a license tax on him, provided such other locality is otherwise authorized to impose a local license tax upon his business.

When BPOL tax is measured by gross receipts, the gross receipts included in the taxable measure are only those gross receipts attributed to the exercise of a privilege subject to licensure at a definite place of business within Virginia. Where activities are conducted outside of a definite place of business, such as during a visit to a customer location, gross receipts are attributed to the definite place of business from which such activities are initiated, directed, or controlled. The situs of gross receipts for different classifications of

business are attributed to one or more definite places of business or offices according to detailed rules set forth in Title 23 of the Virginia Administrative Code (VAC) § 10-500-160 through 23 VAC § 10-500-200.

Apportionment

If the taxpayer has more than one definite place of business and it is not possible or practical to determine at which definite place of business gross receipts should be taxed under the situs rules above, gross receipts must be divided between the definite places of businesses by payroll. Some activity must occur or be controlled from a definite place of business for gross receipts to be taxed by the locality of the definite place of business. If an entity's definite place of business is in a locality that does not tax gross receipts, a different locality may not tax these gross receipts simply because the first locality does not have a license tax.

Deduction for Out-of-State Taxes

Current law provides a deduction from a taxpayer's gross receipts or gross purchases for any receipts attributable to business conducted in another state or foreign country in which the taxpayer is liable for an income or other tax based upon income.

The deduction is generally available for impacted taxpayers that use the situs rules above. Unlike the situs rules, the deduction operates only one way. For example, if an employee in a Virginia definite place of business does some activity that assists in a sale outside Virginia to a state where such sale would be subject to an income tax, the business may receive a deduction from receipts that have been assigned to Virginia for taxation under the situs rules. However, if an out-of-state employee assists in or makes a sale to Virginia, there is no corresponding addition to receipts for such sales. Therefore, the situs rules generally ensure that BPOL is internally consistent under the U.S. Constitution, whereas the deduction is an additional safeguard that prevents potential double taxation that may result from the interaction between BPOL and another state's income tax that may affect certain taxpayers due to differing situs and sourcing rules. Depending on the taxpayer's specific facts, this may or may not be required by the external consistency test under the U.S. Constitution.

However, if apportionment has been used to divide the gross receipts of the business among its definite places of businesses, then the use of apportionment to assign gross receipts to a definite place of business is presumed to have compromised the ability of the taxpayer to determine the situs of the assigned gross receipts for any other purpose, such as the deduction provided by *Virginia Code* § 58.1-3732(B)(2). 23 VAC § 10-500-210 provides more information and examples regarding the use of apportionment and its interaction with this deduction.

This deduction was enacted in 1996 following a 1995 report by the Joint Subcommittee Studying the Business, Professional, and Occupational License Tax. Most of the recommendations resulted from a consensus between representatives of the business

community and localities. See House Document No. 59 (1995) attached hereto as Appendix F. However, consensus was not achieved regarding *Virginia Code* § 58.1-3732(B)(2). Instead, alternatives were presented to the joint subcommittee, which voted to adopt the language present in current law. Regarding this deduction, annotated comments to the proposed legislation—which are contained in the 1995 report—provide that:

> At its January 9, 1995 meeting, the Joint Subcommittee also adopted a deduction that effectively exempts all receipts that are subject to income tax in other states. This is contrary to the concept of a privilege tax, which generally looks to the place where the privilege was exercised rather than the destination of the goods. Localities are extremely concerned about such a provision, especially larger localities who contend it could cause significant revenue losses. The business community would prefer to exempt all gross receipts which have any connection with activity in other states. The provision, however, only exempts receipts when the activity in the other state has resulted in an actual income tax liability to the other state or foreign country. The apportionment of receipts attributable to activities within Virginia will not be affected. Nor does the provision allow for a deduction for a business which has its only office in Virginia and its contacts with other states is not sufficient to allow any other state to impose an income tax.

The Department is authorized by *Virginia Code* § 58.1-3703.1 to issue determinations on taxpayer appeals of BPOL assessments. Accordingly, the Department considered the scope of the deduction for out-of-state taxes in Public Document (P.D.) 18-170, (10/10/2018) and P.D. 22-117 (7/21/2022). In P.D. 18-170, the Department evaluated deductions relating to gross receipts attributable to Arizona, California, the District of Columbia, Florida, Georgia, New York, Texas, Utah, and West Virginia. Relying on P.D. 97-490 (12/19/1997) and 23 VAC § 10-500-80 (A)(2), the Department clarified that a business would be eligible for the deduction for gross receipts for states in which the business was liable for a tax based upon income, regardless of whether the tax is called an income tax. P.D. 97-490 clarifies that a taxpayer must be required by the laws of another state or foreign country to file an income tax return or other return for a tax based upon income in order to be eligible to claim a deduction. Title 23 VAC § 10-500-80 (A)(2) requires a taxpayer to file an income or income-like tax return in a state or foreign country even if there is no actual tax liability in a given year, in order to claim the deduction in that state or foreign country. Accordingly, the Department allowed a deduction for gross receipts attributable to California, Georgia, New York, and the District of Columbia because the Department determined they were privilege or franchise taxes that operated as "income like" taxes computed based on income. Conversely, the Department disallowed deductions for gross receipts attributable to Texas because Texas statutorily provides that its franchise tax is not subject to the limitations of P.L. 86-272 and the Texas case law had established that the tax is not an income tax or a tax that is measured by net income. Deduction for Florida's tax was also disallowed as applied to an S corporation because such corporations are not generally subject to income tax in Florida, either at the corporate or individual shareholder level.

In P.D. 22-117, the Department considered whether deductions for taxes paid in Ohio, Texas, and Washington were correctly disallowed due to those states not having an income tax filing requirement. Ohio's Commercial Activity Tax, Texas' Margin Tax, and Washington's Business and Occupation Tax are all gross receipt-based taxes levied in lieu of a corporate income tax. Focusing on whether the taxes at issue were imposed on net income and whether the taxes were subject to P.L. 86-272, the Department determined that deductions for these taxes were correctly disallowed. The Department determined that allowing the deduction for any taxes not imposed on or measured by net income would have the effect of broadening the deduction beyond the clear statutory language.

Definition of "Income Tax" In Other Areas of Law

While Virginia statutes do not explicitly define the term "income tax" for purposes of BPOL Out-of-State Taxes Deduction, the term is defined in other areas of law. For example, for the purposes of the federal Buck Act, which protects state and local income taxes on activity occurring within a federal area, 4 U.S.C. § 110 states the following:

> The term 'income tax' means any tax levied on, with respect to, or measured by, net income, gross income, or gross receipts.

Because this federal statutory definition explicitly includes gross receipts taxes, the Virginia Attorney General's Office concluded in 2012 that BPOL is an "income tax" for the purposes of the federal Buck Act. See Va. Att'y Gen. Op. 11-029 (2/24/2012). This Virginia Attorney General's Office Opinion was relied on by the Department in P.D. 22-164.

Another instance where the term "income tax" is defined is in the context of Virginia's credit for income taxes paid to other states (and foreign countries on retirement income) under its individual income tax. In this case, *Virginia Code* § 58.1-332.2 defines income tax as follows:

A. For purposes of the credits in §§ 58.1-332 and 58.1-332.1, the term "income tax" is a term of art that refers to a specific type of tax levied on earned and unearned income and shall not include any other type of tax merely because it may be measured by or referenced to gross or net income. An income tax includes, but is not limited to, a tax imposed on all income of an individual if a resident, or all income of an individual from the jurisdiction's sources if a nonresident; however, an income tax so imposed may incorporate other provisions that grant exemptions, exclusions, deductions, subtractions, credits, or other preferences for specific types of income, expenses, individuals, or other criteria.

B. An income tax shall not include:

> 1. A tax conditioned upon the exercise of any franchise, privilege, or business within the jurisdiction even though the tax is measured or based upon gross or net income derived therefrom, but such measure does not

> include income that the person exercising such franchise, privilege, or business may receive from other sources within the jurisdiction.
> 2. License and occupation taxes, which are payable in respect to the privilege of engaging in or carrying on a particular business or vocation, even though the amount of tax payable by an individual may be measured by the amount of business which he transacts or his earnings therefrom, but such measure does not include income that the person engaging in or carrying on a particular business or vocation may receive from other sources within the jurisdiction.

Unlike the Buck Act's broad definition, this narrow definition would exclude BPOL and similar gross receipts taxes from being considered an "income tax."

One final instance where the term "income" in the context of a "tax on income" had to be defined is in the context of the Sixteenth Amendment to the U.S. Constitution. In that case, the United States Supreme Court defined "income" as follows:

> For the present purpose we require only a clear definition of the term "income," as used in common speech, in order to determine its meaning in the Amendment; and, having formed also a correct judgment as to the nature of a stock dividend, we shall find it easy to decide the matter at issue.
>
> After examining dictionaries in common use (Bouv. L.D.; Standard Dict.; Webster's Internat. Dict.; Century Dict.), we find little to add to the succinct definition adopted in two cases arising under the Corporation Tax Act of 1909 (*Stratton's Independence* v. *Howbert,* 231 U.S. 399, 415; *Doyle* v. *Mitchell Bros. Co.,* 247 U.S. 179, 185) -- "Income may be defined as the gain derived from capital, from labor, or from both combined," provided it be understood to include profit gained through a sale conversion of capital assets, to which it was applied in the *Doyle Case* (pp. 183, 185).

Eisner v. Macomber, 252 U.S. 189, 206-207 (1920).

Again, this definition would appear to exclude BPOL and similar gross receipts taxes from being considered a "tax on income."

While none of these definitions are binding for the purposes of defining the term "income or other tax based upon income" under *Virginia Code* § 58.1-3732(B)(2), they are illustrative that there is no one, unified definition used for all tax purposes.

Constitutional Concerns

The U.S. Supreme Court, in *Complete Auto Transit, Inc. v. Brady* (1977), articulated a four-prong test for determining whether a state tax on interstate commerce passes Constitutional muster under the Commerce and Due Process Clauses:

- Substantial nexus,
- Fair apportionment,
- Non-discrimination against interstate commerce, and
- Fair relation between the tax and the services provided by the state.

If a constitutional question is raised regarding a deduction or credit for taxes paid to another state, it is most likely to be raised on the "fair apportionment" prong. Fair apportionment requires that the state may not exact from interstate commerce more than the state's fair share of a single integrated enterprise carried on both within and without the state. The Court's jurisprudence since *Complete Auto* has relied upon a test of internal and external consistency to determine whether a state's tax is fairly apportioned.

Internal consistency requires that a tax be structured so that if every state were to impose an identical tax, no multiple taxation would result. As explained by the U.S. Supreme Court:

> Internal consistency is preserved when the imposition of a tax identical to the one in question by every other State would add no burden to interstate commerce that intrastate commerce would not also bear. This test asks nothing about the economic reality reflected by the tax, but simply looks to the structure of the tax at issue to see whether its identical application by every State in the Union would place interstate commerce at a disadvantage as compared with intrastate commerce. A failure of internal consistency shows as a matter of law that a State is attempting to take more than its fair share of taxes from the interstate transaction, since allowing such a tax in one State would place interstate commerce at the mercy of those remaining States that might impose an identical tax.

Oklahoma Tax Comm'n v. Jefferson Lines, Inc., 514 US 175, 185, 115 S. Ct. 1331 (1995).

External consistency requires that a state tax only that portion of revenues from interstate activity that reasonably reflects the in-state component of the activity being taxed. According to the U.S. Supreme Court:

> The second and more difficult requirement [of fair apportionment] is what might be called external consistency -- the factor or factors used in the apportionment formula must actually reflect a reasonable sense of how income is generated… we will strike down the application of an apportionment formula if the taxpayer can prove "by 'clear and cogent evidence' that the income attributed to the State is in fact 'out of all appropriate proportions to the business transacted in that State….'"

Container Corp. of Am. v. Franchise Tax Bd., 463 US 159, 169-170, 103 S. Ct. 2933 (1983).

Consistent with the rules of statutory construction, the Department, as the executive agency charged with the administration of Virginia's tax statutes, presumes that all

statutes enacted by the General Assembly and incorporated into the *Code of Virginia* are constitutional.

Potential Impact to Local Governments of Expanding the Deduction

BPOL revenues represent a significant source of funding for the localities that impose the tax and expanding the deduction would most likely result in a reduction of those revenues. This reduction could have a significant impact as localities may not be equipped to replace the lost revenues since they are barred from imposing a tax on net income.

In addition, corporate apportionment methodologies amongst various states are not always consistent. Localities strive for consistency and predictability in their tax bases and expanding the deduction to include different and evolving types of taxes would not only lessen the tax base but would make year-over-year assumptions difficult for localities.

Alternatively, a broader deduction that offers greater predictability and a lower tax burden may encourage more businesses to establish business operations in Virginia.

Several other states that have adopted gross receipts taxes in lieu of income taxes include:

- Ohio
- Oregon
- Texas
- Nevada
- Washington
- Tennessee
- Delaware

The Potential Administrative Impact to Taxpayers

On the one hand, broadening the deduction could ease the administrative burden on taxpayers. Broadening the statutory language to include taxes on gross receipts or net income could potentially increase predictability and consistency for taxpayers as the amended deduction would presumptively apply to all similar taxes paid to other states. While the Department's rulings on this issue have consistently recommended that localities apply the same methodology for determining the eligible gross receipts, amending the statutory language to broaden the deduction would lessen the number of aggrieved taxpayers and reduce the number of appeals submitted to the Department.

On the other hand, broadening the deduction would also raise new issues that could increase the administrative burden on taxpayers, such as introducing gross receipts tax concepts into the analysis of whether a taxpayer is entitled to this deduction. While income tax concepts are relatively uniform among states, defining what constitutes a gross receipts tax may not be as uniform and well-defined.

Workgroup Meeting

The Department contacted the stakeholder groups identified in the legislation to notify them of the work group and to request that each stakeholder group appoint a representative to participate in the work group. The legislation required the work group consist of individuals with experience in local license tax compliance and enforcement, including representatives of:

- The Virginia Municipal League ("VML"),
- The Virginia Association of Counties ("VACO"),
- The Commissioners of the Revenue Association of Virginia ("CORVA"),
- The Virginia Society of Certified Public Accountants ("VSCPA"),
- The Council on State Taxation ("COST"),
- The Virginia Chamber of Commerce ("the Chamber"), and
- Any other key business tax representatives as determined by the Department.

The appointed representatives of each stakeholder were as follows:

- Joe Flores on behalf of the Virginia Municipal League
- Katie Boyle, Jay Doshi, and Young Tarry on behalf of the Virginia Association of Counties
- Patrick Reynolds on behalf of the Council on State Taxation
- Duane Dobson on behalf of Ryan
- On behalf of the Commissioners of the Revenue Association:
    a. Blythe Scott – City of Norfolk
    b. Kim Klingler – Arlington County
    c. Karen Bever – City of Hampton
- Ethan Betterton, Tim Winks, and Michele Borens on behalf of the Virginia Chamber of Commerce
- Emily Walker, Elil Arasu, and Kris Thomas on behalf of the Virginia Society of CPAs
- Duane Dobson (Ryan, LLC) and Elizabeth Rafferty (Hunton Andrews Kurth, LLP) on behalf of the business community.

The Department convened a meeting with workgroup members on June 3, 2025. Delegate Vivian E. Watts and all appointed representatives attended the meeting. Prior to the meeting, the Department gave all work group participants an agenda with an outline of topics to be discussed. See Appendix B.

At the beginning of the meeting, representatives of the Department provided an overview of the legislation and the work group mandate. Following the overview, each work group participant was given the opportunity to state their position and express any concerns and goals that they had for the work group. During this time, CORA offered a presentation summarizing its position and highlighting some relevant statistics. The presentation is attached as Appendix C. The remaining discussion of the workgroup was guided by the topics mandated by the 2025 legislation. Workgroup participants were encouraged to

discuss each topic freely and fully before moving on to the next subject. The topics addressed were:

- Constitutional, federal, and case law concerns
- Impact to local governments of expanding the deduction
- Potential administrative issues for taxpayers
- Other provisions of law that may impact the deduction
- Any other concerns or comments regarding the potential for expansion of the deduction including proposals on the ideal methodology
- There was no substantive discussion offered by the participants on the issue of the support system necessary to verify across local jurisdictions the applicable deduction and to enforce compliance.

a. Constitutional, federal, and case law concerns

VACO argued that the absence of cases litigating the constitutionality of the deduction in its current form despite the existence of legally sophisticated and well-funded businesses in Virginia is *prima facie* evidence of the validity of the deduction. The Chamber responded to this idea by noting that Fairfax County has not challenged these BPOL deductions taken by businesses in its jurisdiction and have therefore avoided any constitutional challenge.

COST argued in favor of equitable and non-discriminatory treatment of multi-jurisdictional businesses and a need for clarity to avoid confusion. COST also argued that the current statute and rulings may not be consistent or clear because the general definition of "income tax" includes both gross and net income taxes and that runs contrary to the Department's rulings. COST also noted that constitutional concerns may arise were a deduction to be allowed for one state purely over the vernacular of the tax itself. COST offered the Texas Margin Tax as an example of this since it is technically a franchise tax.

The Chamber fielded a discussion of the constitutional issues underlying the statute and rulings. The Chamber noted during the meeting that it may be instructive that the *Wynne* case provided that a gross receipts tax and an income tax are the same for purposes of double-taxation. Accordingly, treating them differently may facilitate legal challenges. The Chamber also noted that the constitutional limitations on localities imposing the tax under a "fair apportionment" scrutiny requires a deduction for taxes imposed on the same receipts. Therefore, the Chamber argued that the Department's interpretation is inconsistent. The Chamber also highlighted the potential for an "external consistency" issue with the current deduction since Virginia is taxing receipts that cannot be attributed to another state that are still potentially being taxed in another state due to differing statutory schemes in Virginia versus other states.

b. Impact to local governments of expanding the deduction

Delegate Watts noted the need to handle any statutory change to the deduction in a clear and professional manner to avoid burdening localities that are trying to collect the tax fairly. There seemed to be consensus on this issue from the municipalities as well.

CORVA, during its presentation, juxtaposed the small number of taxpayers that are currently impacted by the deduction against the potentially very large fiscal impact that broadening the deduction would have to localities. CORVA also noted in its presentation and comments that verification and enforcement of a deduction which depends on the interpretation of another state's tax laws would increase the administrative burden on localities. VML and VACO aligned themselves with CORVA's presentation and comments.

VACO also noted that broadening the deduction would require localities, some of which lack resources necessary, to look beyond the well-defined scope of state income taxes to different and smaller taxing schemes. VACO argued that this would create a substantial administrative burden on smaller localities.

c. Potential administrative issues for taxpayers

Delegate Watts pointed to the need for clarity on the deduction to ease the administrative burden on both sides of the issue. VACO expressed a desire for fairness and administrative ease for taxpayers, partially to avoid taxpayers having to produce, and localities having to review, hundreds of pages of documents in order to substantiate the deduction. In response to Mr. Duane Dobson from Ryan suggesting that a uniform or standardized form, especially a shorter one, would ease the burden on taxpayers, VACO proposed that it would not significantly ease the burden since the requirement to substantiate the deduction would still exist.

CORVA noted in its comments that the different taxes in different states receiving different BPOL deduction treatment creates a very difficult compliance situation for corporations and a time-consuming and burdensome process for localities. CORVA noted that audits on this issue can sometimes take as long as seven years.

The VSCPA noted that it supports a change in the deduction because similarly situated taxpayers will have different tax bases in different states, which raises fairness questions and increases the administrative burden on those taxpayers. The VSCPA also noted that, from a technical perspective, BPOL is already burdensome on taxpayers since returns are due March 1, which is before most businesses "close their books" for the fiscal year and therefore returns are not being filed by CPAs but rather by unsophisticated taxpayers. This type of misalignment between the return due dates and when the reporting information would be available to correctly categorize income and taxes paid to another state make it inherently difficult for taxpayers to comply.

d. Other provisions of law that may impact the deduction

Delegate Watts noted that any impact of the current deduction would be exacerbated in the future as more states consider levying taxes in lieu of income taxes and therefore Virginia should act now. Additionally, she suggested that Virginia may position itself ahead of the curve by taking this opportunity to modernize our Code as it relates to BPOL.

e. Any other concerns or comments regarding the potential for expansion of the deduction including proposals on the ideal methodology

VACO expressed support, generally, for the Department's administrative rulings interpreting the statutory language and noted that no change is required.

Meeting wrap-up and post-meeting

At the conclusion of the meeting, the Department requested written comments from all workgroup members. All comments received from the work group are attached. See Appendix D. Subsequently, the draft report was circulated to the workgroup and workgroup members were given the opportunity to provide another set of written comments before the final report was published.

Written Comments Received After the Meeting

The Department received submissions of written comments from the Chamber, CORVA, COST, Eversheds Sutherland, VACO, and VML.

Virginia Chamber of Commerce

In its written comments, the Chamber urged the Department to change its interpretation of the law to allow for deduction of gross receipts-based taxes to avoid double taxation of interstate receipts, to reflect the plain language of the statute, be consistent with the Department's own regulations, and avoid a potentially unconstitutional distortion of Virginia businesses' income. The Chamber also argued that allowing the deduction for gross-receipts based taxes would better reflect the purpose of the deduction without being overly formalistic since gross-receipts and net-receipts taxes are effectively similar. The Chamber also noted that the risk of double taxation is especially high for businesses headquartered in Virginia as those businesses are more likely to engage in sales and service-performance activities through a large number of employees in Virginia. To bolster its constitutional argument, the Chamber notes that over-representing a business' Virginia income would violate the external consistency test under the Commerce Clause.

Commissioners of the Revenue Association

In its written comments, CORVA echoed many of the concerns it communicated during the meeting and within its presentation. CORVA asserted that broadening the deduction

would strain local budgets during an already difficult time and would benefit only a few large, multistate or multinational corporations that already enjoy sufficient tax advantages. CORVA noted also that broadening the deduction could result in the non-taxation of certain taxable receipts since BPOL uses situs-based sourcing to allocate gross receipts to the locality where business activity occurs. CORVA asserted that imposing income tax concepts on this income could allow receipts that are properly situsted to a Virginia locality to be deducted simply because they appear on an income tax return in another jurisdiction regardless of whether those receipts were actually taxed in that jurisdiction. CORVA also noted the risk of increasing the administrative burden on taxpayers that may result from introducing gross-receipts tax concepts into an income tax reporting scheme, especially where the gross-receipts tax concepts may lack clearly defined definitions. CORVA also raised the issue of a potential increase in administrative burden for localities since taxpayers could claim deductions that exceed their gross receipts and localities would have to shoulder the burden of more frequent and in-depth audits to verify the deduction. CORVA concluded its written comments by advocating against expansion of the deduction and instead offering support for refreshing the Department's 2000 BPOL Guidelines to promote uniformity of interpretation.

Council on State Taxation

COST provided written comments to advocate for legislation to clarify that "income or other tax based on income" includes not just "net income tax" but also "gross income tax." COST asserted that this position is consistent with: 1) earlier guidance from the Department of Taxation; 2) recent guidance regarding BPOL and federal law; and 3) U.S. Constitutional limitations. COST noted that the Department issued arguably inconsistent guidance in P.D. 22-164 (12/20/2022) when it determined that BPOL is an income tax for purposes of the Buck Act, which protects state and local income taxes on activity occurring within a federal area. COST asserted that the ruling fostered inconsistency by supporting the idea that BPOL, which itself is a gross-receipts tax, is an income tax but other states' gross-receipts taxes are not income taxes. COST also argued that by denying a deduction for gross receipts attributable to jurisdictions that impose a gross receipts tax or modified gross receipts tax and not an income tax, BPOL is effectively taxing activity in those jurisdictions outside of Virginia. BPOL should instead provide for a deduction attributable to receipts situsted first to a Virginia jurisdiction that are also subject to an out-of-state gross income or net income tax.

Eversheds Sutherland

Michele Borens of Eversheds Sutherland provided written comments that explored arguments related to the constitutional infirmities of the current deduction and the concerns raised by localities about the expansion of the deduction. Eversheds Sutherland advocated for the workgroup to support amending the deduction to include state taxes that are based on gross receipts, imposed in lieu of income taxes. Eversheds Sutherland

argues that BPOL "violates the external consistency test because, in the absence of an Out-of-State Deduction applicable to other states' gross receipts taxes, BPOL Tax reaches beyond the portion of value that is fairly attributable to economic activity within Virginia." Eversheds Sutherland cites *Short Brothers (USA), Inc. v. Arlington County,* 244 Va. 520 (1992), to demonstrate that the Virginia Supreme Court's analysis of external consistency considered not whether there was a violation based on whether a taxpayer was subject to another state's income tax, but instead whether it was subject to any other state tax based on its gross receipts. Eversheds Sutherland also cited *City of Winchester v. American Woodmark Corp*., 252 Va. 98 (1996) in support of this proposition. Regarding the burden on localities, Eversheds Sutherland argues that a locality's fiscal concerns should not be material to the consideration of the scope of the deduction and localities have sufficient experience and expertise to appropriately administer and audit an expanded out-of-state deduction.

Virginia Association of Counties

In its written comments, VACO argues against expansion of the deduction based on the adverse fiscal impact to localities and the increased administrative complexity such a change would create for them. VACO notes that localities strive for consistency and predictability in their tax bases and expanding the deduction would introduce an element of unpredictability due to varying corporate apportionment methodologies. VACO also noted that, as reflected in the 1995 *Report of the Joint Subcommittee Studying the Business, Professional, and Occupational License Tax*, localities were not in support of importing income tax concepts into a gross-receipts tax framework and while income taxes are recognizable in other states, incorporating other tax types would require localities to become 50-state experts (and potentially international experts) in order to verify the deduction. VACO also cautioned against the risk of unintended consequences from the expansion such as arguments from taxpayers that deduction should be allowed for local gross-receipts taxes levied in addition to state ones. Finally, VACO noted its concerns over the fairness of potentially allowing a deduction for gross receipts generated in another state that may fall below that state's filing threshold and would therefore allow that income to escape taxation altogether.

Virginia Municipal League

VML provided concise written comments to echo their alignment with CORVA and VACO against expansion of the deduction on the basis of the resulting fiscal impact, fairness, the increased administrative burden, and constitutionality of the current deduction.

Written Comments Received in Response to Draft Report

Commissioners of the Revenue Association

CORVA provided comments in response to the Department's Draft Report which highlighted that brick-and mortar and other small businesses pay more BPOL tax than large multinational corporations when measured as a percentage of their gross receipts. CORVA also noted that smaller companies with local footprints do not benefit from a deduction for operations in other states and countries.

Council on State Taxation

COST's comments, in addition to reiterating the major themes of its earlier comments, advocated for the Department to recommend legislative clarification that the deduction apply to "gross income tax." COST also expressed disagreement that such legislation would amount to an expansion of the deduction but would instead be a clarification consistent with the original intent and plain meaning of the statute, earlier guidance from the Department of Taxation, recent guidance regarding BPOL and federal law, and U.S. Constitution limitations.

Virginia Chamber of Commerce

The Chamber's extensive comments in response to the draft report urged the Department to recommend legislative or administrative action to revise the scope of the deduction in order to remedy the BPOL's constitutional infirmities. The Chamber also warned that the out-of-state deduction is externally inconsistent and therefore likely to be challenged in court, citing several examples of cases where courts have applied the Commerce Clause's fair apportionment restraint on state taxation to prevent overreaching by localities. The Chamber argues that a judicially crafted solution may differ from one designed by the legislature. For instance, a court may not merely expand the deduction to account for out-of-state gross receipts taxes, but instead incorporate other out-of-state tax types, as well. The Chamber also refuted both the localities' need for revenue and any possible increase in administrative difficulty as valid reasons for inaction in the face of the current law's constitutional infirmities.

Conclusion & Findings

The work group mandated by 2025 House Bill 1743 brought together different constituencies involved in the administration, collection, and remittance of local license taxes in Virginia. The work group had one official meeting. Taxpayers and their representatives urged the workgroup to expand the deduction and argued that the existing interpretation of the deduction is unconstitutional and potentially unfair while those responsible for administering and collecting the tax were in favor of maintaining the status quo. All parties in the workgroup made cogent and well-supported arguments for

their positions and the Department is grateful to all those who participated and provided input for this report.

The work group did not achieve consensus on whether the deduction should be amended. Specifically:

- The workgroup did not reach consensus on whether it is necessary to expand the deduction to address constitutional concerns, and
- The workgroup did not reach consensus on whether there would be other benefits to expanding the deduction.

Other areas of disagreement were:

- Whether expanding the deduction would reduce or increase the administrative burden on taxpayers, and
- Whether the impact on localities is a concern in expanding the deduction.

Because the workgroup did not agree on whether to amend the deduction, it did not address how any changes to the deduction would best be structured.

Even though the workgroup did not agree on whether the deduction should be amended, the following area of consensus was identified:

- Consistency, clarity, and fairness are all vital to the administration of BPOL and should be central to any action taken to change the deduction administratively or legislatively.

Given the potential impact to the stakeholders involved and the inability of the parties to reach a consensus, the Department recommends that any proposed changes or additional clarifications to the BPOL out-of-state deduction should be pursued through legislative action rather than by amending the Department's previously established administrative interpretation of the existing statute.

APPENDIX A

CHAPTER 192

An Act to convene a work group to review the local license tax deduction in Virginia for receipts attributable to out-of-state business; report.

[H 1743]

Approved March 21, 2025

Be it enacted by the General Assembly of Virginia:

1. *§ 1. That the Department of Taxation shall convene a work group to review the local license tax deduction in Virginia for receipts attributable to out-of-state business, including a review of (i) current policy and methodology of the deduction set forth in subdivision B 2 of § 58.1-3732 of the Code of Virginia; (ii) any constitutional or case law concerns regarding the existing laws governing such deduction; (iii) any potential impact on local government revenue as a result of determining such deduction based upon receipts subject to a net income tax or gross receipts tax in another state or foreign jurisdiction and alternatives to phase in any such potential impact; (iv) the potential administrative complexities or benefits for taxpayers and the support structure necessary to verify across local jurisdictions the applicable tax deduction and to enforce compliance; and (v) any impact to such deduction from other existing provisions of law. The work group shall consist of individuals with experience in local license tax compliance and enforcement, including representatives of the Virginia Municipal League, the Virginia Association of Counties, the Commissioners of the Revenue Association of Virginia, the Virginia Society of Certified Public Accountants, the Council on State Taxation, the Virginia Chamber of Commerce, and any other key business tax representatives as determined by the Department of Taxation. The Department of Taxation shall submit a report of the findings and recommendations, if any, of the work group to the Joint Subcommittee on Tax Policy and to the Chairs of the Senate Committee on Finance and Appropriations and the House Committees on Finance and Appropriations by October 1, 2025.*

APPENDIX B

License Tax Out-of-State Deduction Work Group

June 3, 2025 Meeting Agenda

2:00 PM Start Time

I. Greeting

II. Legislative Overview and Background Information – Department of Taxation
   a. 2025 House Bill 1743 – Bill History and Impact Statement

III. Participants discuss their viewpoints and concerns (please try to limit to 3 minutes per organization represented)
   a. Delegate Watts
   b. Joe Flores – Virginia Municipal League
   c. Katie Boyle – Virginia Association of Counties
      i. Jay Doshi
      ii. Young Tarry
   d. Patrick Reynolds – Council on State Taxation
      i. Duane Dobson - Ryan
   e. Commissioners of the Revenue Association
      i. Blythe Scott – City of Norfolk
      ii. Kim Klinger – Arlington County
      iii. Karen Bever – City of Hampton
   f. Ethan Betterton – VA Chamber of Commerce
      i. Tim Winks
      ii. Michele Borens
   g. Emily Walker – Virginia Society of CPAs
      i. Elil Arasu
      ii. Kris Thomas
   h. Elizabeth Rafferty – Hunton Andrews Kurth, LLP

IV. Group Discussion and Questions
   a. Suggested Topics:
      i. Constitutional, federal, case law concerns
      ii. Impact to local governments of expanding the deduction
      iii. Potential administrative issues for taxpayers
      iv. The support system necessary to verify across local jurisdictions the applicable deduction and to enforce compliance
      v. Other provisions of law that may impact the deduction
      vi. Any other concerns or comments regarding the potential for expansion of the deduction including proposals on the ideal methodology

V. Meeting Wrap-up

Work Group Participants

Name	Organization	Email Address
Jay Doshi	Virginia Association of Counties	jay.doshi@fairfaxcounty.gov
Patrick Reynolds	Council on State Taxation	preynolds@cost.org
Katie Boyle	Virginia Association of Counties	kboyle@vaco.org
Ethan Betterton	Virginia Chamber of Commerce	e.betterton@vachamber.com
Joe Flores	Virginia Municipal League	jflores@vml.org
Delegate Vivian Watts	House of Delegates	delvwatts@house.virginia.gov
Emily Walker	Virginia Society of CPAs	ewalker@vscpa.org
Young Tarry	Virginia Association of Counties	young.tarry@fairfaxcounty.gov
Tim Winks	Virginia Chamber of Commerce	
Michele Borens	Eversheds Sutherland	micheleborens@eversheds-sutherland.com
Duane Dobson	Ryan	Duane.dobson@ryan.com
Blythe Scott	City of Norfolk	Blythe.Scott@norfolk.gov
Kim Klingler	Arlington County	KKlingler@arlingtonva.us
Karen Bever	City of Hampton	Kbever@hampton.gov
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Kris Thomas	Virginia Society of CPAs	Kris.Thomas@ey.com
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Department of Taxation

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APPENDIX C: Reference Materials Presented During the Meeting

2025 Workgroup to Review the BPOL Out-of-State Deduction

June 3, 2025

Virginia Tax

Meeting Agenda

- Introduction and purpose of the workgroup
- Background of the deduction
  - Scope of the deduction
  - P.D. 18-170 and 22-117
- Additional information on the deduction relevant to the Workgroup
  - Constitutional, federal, and case law concerns
  - Preliminary analysis on the impact to local governments of expanding the scope of the deduction
  - Potential administrative issues for taxpayers
  - Other provisions of law that may impact the deduction
    - Taxes in other states that may impact the deduction
- Statements from each workgroup member (please try to limit your statement to 3 minutes)
- Discussion of legislatively mandated topics
- Conclusion and follow-up items

What brings us together

- Chapter 192 of the 2025 Acts of Assembly (House Bill 1743) requires the Department to convene a workgroup to review the local license tax deduction in Virginia for receipts attributable to out-of-state business, including a review of:
  - Current policy and methodology of the deduction set forth in § 58.1-3732 (B)(2);
  - Any constitutional or case law concerns regarding the existing laws governing such deduction;
  - Any potential impact on local government revenue as a result of determining such deduction based upon receipts subject to a net income tax or gross receipts tax in another state or foreign jurisdiction and alternatives to phase in any such potential impact;
  - The potential administrative complexities or benefits for taxpayers and the support structure necessary to verify across local jurisdictions the applicable deduction and to enforce compliance; and
  - Any impact to such deduction from other existing provisions of law.

Introduction

- The workgroup shall consist of individuals with experience in local license tax compliance and enforcement, including representatives of:
  - The Virginia Municipal League,
  - The Virginia Association of Counties,
  - The Commissioners of the Revenue Association of Virginia,
  - The Virginia Society of Certified Public Accountants,
  - The Council on State Taxation,
  - The Virginia Chamber of Commerce, and
  - Any other key business tax representatives as determined by the Department.
- The Department must submit a report of the findings/recommendations, if any, of the workgroup to the Joint Subcommittee on Tax Policy and to the Chairs of SFAC and HAC by October 1, 2025.

Virginia Tax

Background

- The deduction in *Virginia Code* § 58.1-3732(B)(2) was enacted in 1996 following a 1995 report by a joint subcommittee's study of BPOL administration.
- Most of the recommendations resulted from a consensus between representatives of the business community and localities. See House Document No. 59 (1995).
- However, consensus was not achieved regarding *Virginia Code* § 58.1-3732(B)(2).
- Instead, alternatives were presented to the joint subcommittee, which voted to adopt the present language.

Background

- On the topic of the proposed deduction the subcommittee report noted:

> *At its January 9, 1995 meeting, the Joint Subcommittee also adopted a deduction that effectively exempts all receipts that are subject to income tax in other states. This is contrary to the concept of a privilege tax, which generally looks to the place where the privilege was exercised rather than the destination of the goods. Localities are extremely concerned about such a provision, especially larger localities who contend it could cause significant revenue losses. The business community would prefer to exempt all gross receipts which have any connection with activity in other states. The provision, however, only exempts receipts when the activity in the other state has resulted in an actual income tax liability to the other state or foreign country. The apportionment of receipts attributable to activities within Virginia will not be affected. Nor does the provision allow for a deduction for a business which has its only office in Virginia and its contacts with other states is not sufficient to allow any other state to impose an income tax.*

Deduction for Receipts Attributable to Out-of-State Business

- *Virginia Code* § 58.1-3732 (B)(2) provides that any receipts attributable to business conducted in another state or foreign country in which the taxpayer (or its shareholders, partners or members in lieu of the taxpayer) is liable for an income or other tax based upon income are deductible from gross receipts or gross purchases for license tax purposes.
- The Department is authorized by *Virginia Code* § 58.1-3703.1 to issue determinations on taxpayer appeals of BPOL assessments.
- The Department's rulings on the scope of the deduction have clarified that the deduction is available for taxes paid to other states that are based on income regardless of whether such taxes are called an "income tax" but the out-of-state taxes being deducted must be assessed on *net income* to be deductible.

Current Policy and Methodology

Scope of the Deduction

- Taxpayers must first identify whether employees at a Virginia location participated in interstate transactions to ascertain if the taxpayer may be subject to income taxation in another state.
- To that end, the methodology for determining the amount of taxes paid that are properly deductible generally requires that:
  - Receipts be sitused to a definite place of business in Virginia, and
  - From those receipts assigned to a definite place of business within a Virginia locality, a business may deduct receipts to the extent that the taxpayer can identify receipts attributable to business conducted in another state in which it filed an income tax return and income tax was paid.

Public Document 18-170

- In P.D. 18-170, the Department evaluated deductions for taxes paid to AZ, CA, DC, FL, GA, NY, TX, UT, and WV. Relying on P.D. 97-490 and 23 VAC 10-500-80 (A)(2), the Department clarified that a business is eligible for the deduction for gross receipts for states in which the business was liable for a tax based upon income, regardless of whether the tax is called an income tax.
  - P.D. 97-490 clarifies that a taxpayer must be *required* by the laws of another state or foreign country to file an income tax return or other return or for a tax based upon income in order to be eligible to claim a deduction.
  - 23 VAC 10-500-80 (A)(2) requires a taxpayer to file an income or income-like tax return in a state or foreign country even if there is no actual tax liability in a given year, in order to claim the deduction in that state or foreign country.

Current Policy and Methodology

Public Document 22-117

- In P.D. 22-117, the Department considered whether deductions for taxes paid in Ohio, Texas, and Washington were correctly disallowed due to those states not having an income tax filing requirement. The Department determined that allowing the deduction for any taxes not imposed on or measured by net income would have the effect of broadening the deduction beyond the clear statutory language.
  - OH's Commercial Activity Tax (CAT), TX's Margin Tax, and WA's Business and Occupation Tax (B&O Tax) are gross receipt-based taxes levied in lieu of a corporate income tax. The Department determined that deductions for these taxes were correctly disallowed.
  - The Department's analysis focused both on whether the taxes at issue were imposed on net income and whether the taxes were subject to P.L. 86-272.

Constitutional Concerns

The Complete Auto Transit Framework

- The U.S. Supreme Court, in *Complete Auto Transit, Inc. v. Brady (1977),* articulated a four-prong test for determining whether a state tax on interstate commerce passes Constitutional muster under the Commerce and Due Process Clauses:
  - Substantial nexus,
  - Fair apportionment,
  - Non-discrimination against interstate commerce, and
  - Fair relation between the tax and the services provided by the state.
- If a Constitutional question is raised regarding a deduction or credit for taxes paid to another state, it is most likely to be raised on the “fair apportionment” prong.

Constitutional Concerns

Fair Apportionment

- Fair apportionment requires that the state may not exact from interstate commerce more than the state's fair share of a single integrated enterprise carried on both within and without the state.
- The Court's jurisprudence since *Complete Auto* has relied upon a test of internal and external consistency to determine whether a state's tax is fairly apportioned:
  - Internal consistency requires that a tax be structured so that if every state were to impose an identical tax, no multiple taxation would result.
  - External consistency requires that a state tax only that portion of revenues from interstate activity that reasonably reflects the in-state component of the activity being taxed.

Constitutional Concerns

Federal Law and Nexus

- Public Law 86-272 prohibits a state from imposing a net income tax where the only contacts with a state are a narrowly defined set of activities constituting solicitation of orders for sales of tangible personal property.
- The scope of P.L. 86-272 is limited to only those activities that constitute solicitation, are ancillary to solicitation, or are de minimis in nature.
- The Department's rulings concerning the BPOL out-of-state deduction reflect consideration of the impact of P.L. 86-272 with regard to the methodology for computing the out-of-state deduction when payroll apportionment is used to situs gross receipts.

Constitutional Concerns

Federal Law and Nexus

- P.L. 86-272 is relevant to the consideration of the BPOL out-of-state deduction when determining whether the activities related to an interstate transaction that are undertaken by employees in Virginia are sufficient to qualify for the deduction of gross receipts upon which taxes were paid to a particular state.
  - Since the possible activities that could create taxable nexus with another state far exceed activities protected under P.L. 86-272, a taxpayer engaging in those activities has exceeded P.L. 86-272's protections and may be taxed in the other state or jurisdiction.
  - Accordingly, minimal contacts with an interstate transaction by personnel based at a definite place of business in a Virginia locality would be sufficient to qualify the business for an out-of-state deduction.

Additional Information

The Potential Impact to Local Governments of Expanding the Deduction

- BPOL revenues represent a significant source of funding for the localities that impose it and expanding the deduction would most likely result in a reduction of those revenues.
  - Localities may not be equipped to replace the lost revenues since they are barred from imposing a tax on net income.
- Corporate apportionment methodologies amongst various states are not always consistent.
  - Localities strive for consistency and predictability in their tax bases and expanding the deduction to include different and evolving types of taxes would not only lessen the tax base but would make year-over-year assumptions difficult for localities.
- Alternatively, a broader deduction that offers greater predictability and a lower tax burden may encourage more businesses to establish business operations in Virginia.

Additional Information

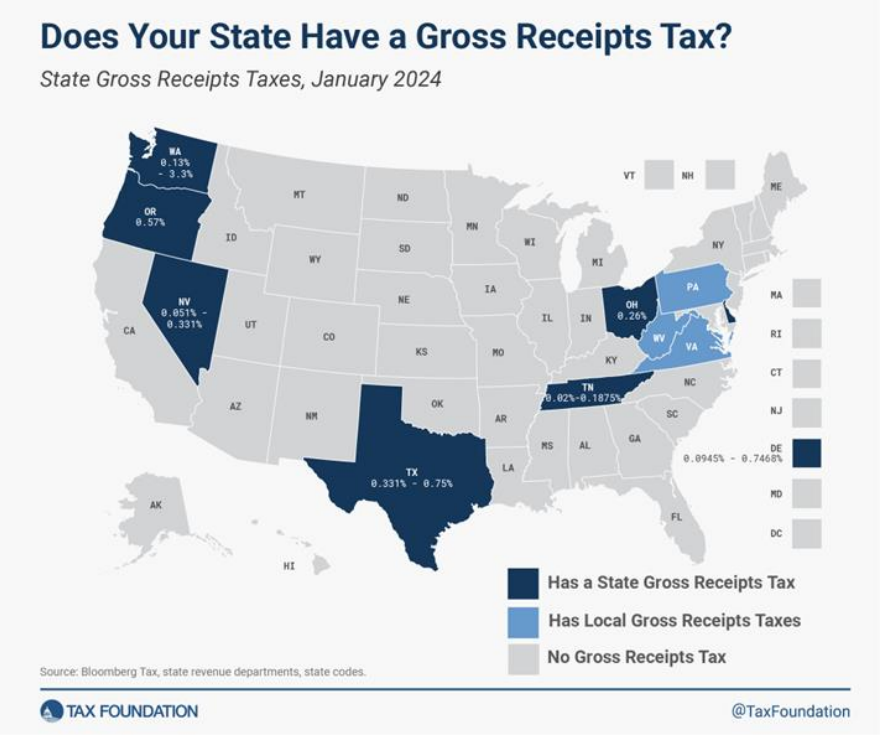
The Potential Administrative Impact to Taxpayers

- Broadening the deduction could ease the administrative burden on taxpayers.
  - Broadening the statutory language to include taxes on gross receipts or net income could potentially increase predictability and consistency for taxpayers as the amended deduction would presumptively apply to all similar taxes paid to other states.
  - While the Department's rulings on this issue have consistently recommended that localities apply the same methodology for determining the eligible gross receipts, amending the statutory language to broaden the deduction would lessen the number of aggrieved taxpayers and reduce the number of appeals submitted to the Department.
- It is unclear what support system is necessary to verify across local jurisdictions the applicable deduction and to enforce compliance. Localities are best situated to comment on this.

Additional Information

Other Provisions of Law That May Impact the Deduction

- Several other states have adopted gross receipts taxes in lieu of income taxes:
  - Ohio
  - Oregon
  - Texas
  - Nevada
  - Washington
  - Tennessee
  - Delaware



Other Provisions of Law That May Impact the Deduction

- Ohio's CAT is an annual privilege tax on businesses with annual taxable gross receipts greater than $3 million, measured by gross receipts from business activities in Ohio.
- Washington's B&O Tax is a gross receipts tax measured on the value of products, gross proceeds of sale, or gross income of the business. No deductions are permitted for business expenses or costs of production or labor.
- Oregon's Corporate Activity Tax is a privilege tax levied on commercial activity in Oregon which exceeds $1 million annually. A 35% deduction for certain business expenses is permitted.
- Texas's Franchise Tax is a privilege tax assessed on the revenue reported for federal income tax minus several statutory exclusions. The "no tax due" threshold is $2.47 million.

Other Provisions of Law That May Impact the Deduction

- Nevada's Commerce Tax is imposed on businesses exceeding $4 million in gross revenue.
- Tennessee imposes a Business Tax and, in very narrow instances, a Gross Receipts Tax. The tax is levied at the state and city level.
- Delaware's Gross Receipts Tax is levied on the total gross revenues of a business. There are no deductions for the cost of goods or property sold, material or labor costs, interest expense, discounts paid, delivery costs, state or federal taxes, or any other expenses allowed.

How BPOL Tax Works: Basic Considerations

1. Local Ordinance
    - Does the locality actually impose the BPOL tax?
2. Business
    - Is the person / entity in question conducting business activities?
3. Definite Place of Business
    - Does the person / entity have a definite place of business in the locality?
4. Classification
    - What type of business is it?
5. Situs
    - Given the type of business, what part of the taxpayer's gross receipts are properly "sitused" to the locality?

It is from this "pool" of taxable gross receipts that a deduction could potentially be taken for any receipts attributable to business activity conducted in another state.

Example:

Pleasantville County has adopted an ordinance imposing BPOL tax on the gross receipts of any business with more than $100,000 in gross receipts. As part of a County economic development initiative, Learn to Dink LLC, a newly formed pickleball coaching company, has established an office in an old blighted service station the County recently redeveloped and is leasing to new start ups. Coaches who work for LTD travel both inside and outside the County providing instructional services at customers' homes, public and private court complexes, schools, and rec centers. A few coaches even travel out of state to perform clinics. The County office serves as the administrative hub where all core business functions are managed, directed, and controlled, but no actual customer services are conducted at the office. LTD earned about $300,000 in revenue last year from performing its services and is now trying to figure out what its County BPOL tax liability is, if any.

HB 1743

WORKING IMPACT ANALYSIS

VERSION 2.0

JUNE | 3 | 2025

Contents

General Assembly Directs A Work Group To Study The BPOL Out-of-state Deduction

What is HB1743?

- HB1743 is a bill that was introduced in the General Assembly in 2025 that proposed to expand the scope of a deduction allowed under Virginia's BPOL (Business, Professional and Occupational License) tax for certain out-of-state receipts.
- It was subsequently amended to instead convene a Virginia Department of Taxation work group to examine the deduction. This group will review current policies, methods, laws, and potential impacts. They are required to submit their findings and any recommendations to the Joint Subcommittee on Tax Policy and the Chairs of the House and Senate Finance Committees by October 1, 2025.

What are the implications of this report?

- **Fiscal Impact:** Potential changes to local government revenue.
- **Business Fairness & Impact**: Effects on businesses with out-of-state activities.
- **Increased Complexity & Administrative Burden:** Challenges in verifying and enforcing the deduction.
- **Legal Considerations:** Current constitutionality and compliance with the Commerce Clause

We Need to Understand The Impact to Virginia Localities

Basic Scenario: Demonstrating How HB1743 Works

Example of Current vs. Future-State for the Business

IT Consulting company based in Arlington, VA, with customers in Arlington, VA and Seattle, WA

Total Gross Receipts $1,000,000

Current-State (Pre-HB1743)

Gross Receipts Sitused to Arlington VA	$600,000
Gross Receipts Sitused to Seattle, WA	$400,000
*Deductions:	None
Taxable in Arlington	$600,000

*WA receipts not eligible for deduction as it does not impose an income or income like tax; it does impose a gross receipts tax

Potential Future-State (Post HB-1743)

Gross Receipts Sitused to Arlington VA	$600,000
Gross Receipts Sitused to Seattle, WA	$400,000
***Deductions:**	**$420,000****
Taxable in Arlington	$180,000

*Washington State (WA receipts now deductible because it imposes a gross receipts tax)

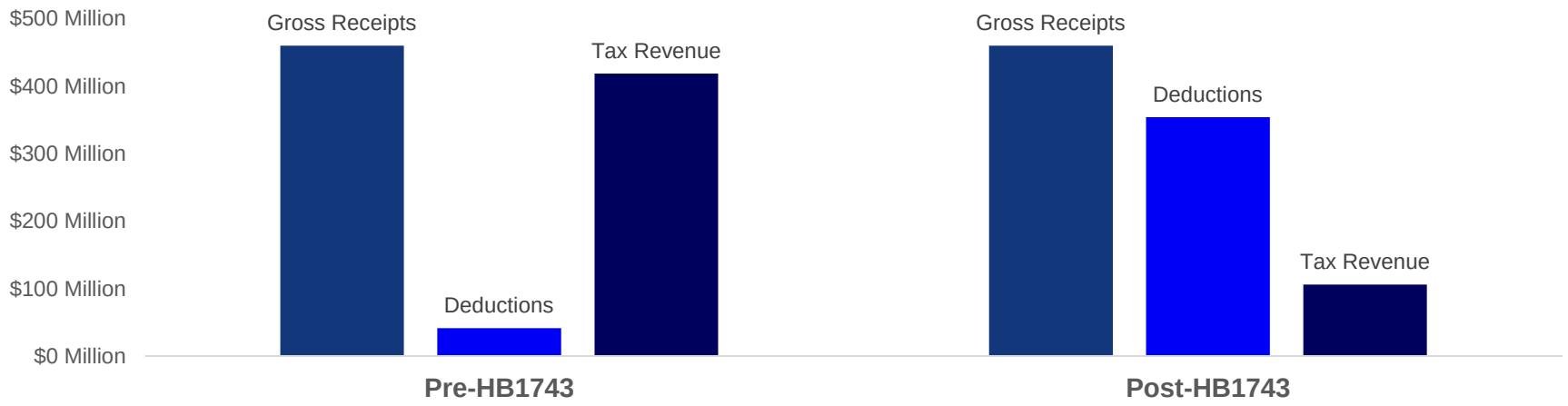
** Direct situs method used, assuming (i) workers in both offices work on all projects and (ii) 30% of receipts are from customers in VA and 70% from customers in WA

HB1743's proposed expansion to out-of-state deduction would result in Virginia losing tax revenue from in-state economic activity.

Practical Virginia Locality Scenario

		Current			HB1743		
Situs based on Payroll Apportionment	Payroll Apportionment	Deductible (based on filing state income tax return)	Taxable Gross Receipts based on Payroll Apportionment	Deduction Amount	Deductible (based on expansion to include gross receipts like tax)	Taxable Gross Receipts based on Payroll Apportionment	Deduction Amount
VA	23%	Y	$460,000,000		Y	$460,000,000	
PA	6%	Y		$27,600,000	Y		$27,600,000
MD	3%	Y		$13,800,000	Y		$13,800,000
WA	68%	N		$0	Y		$312,800,000
Total Deduction				$41,400,000			$354,200,000
BPOL Tax Basis				$418,600,000			$105,800,000
Tax Revenue				**$1,465,100**			**$370,300**

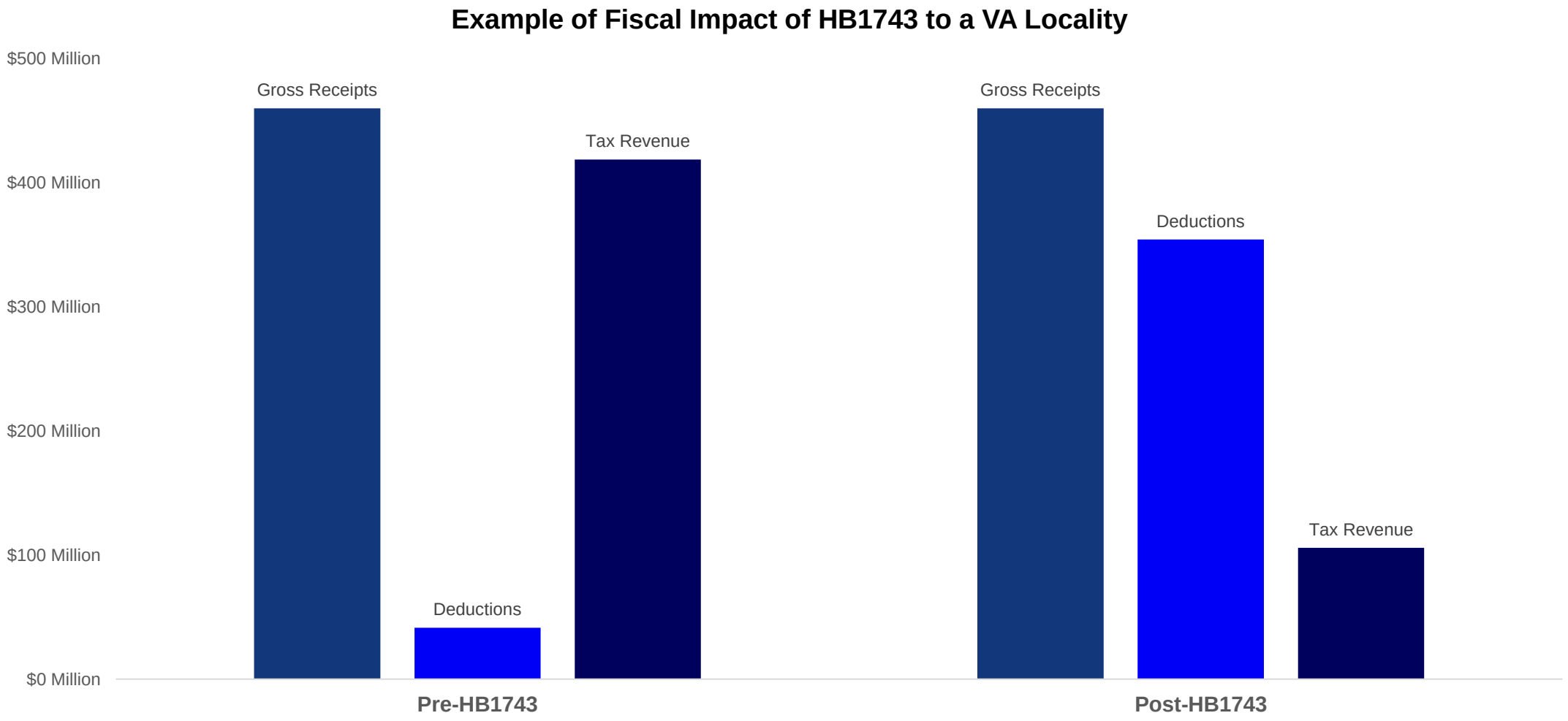
Example of Fiscal Impact of HB1743 to a VA Locality



Revenue Loss of 75%
($1,094,800)

COMMISSIONERS OF THE REVENUE ASSOCIATION OF VIRGINIA

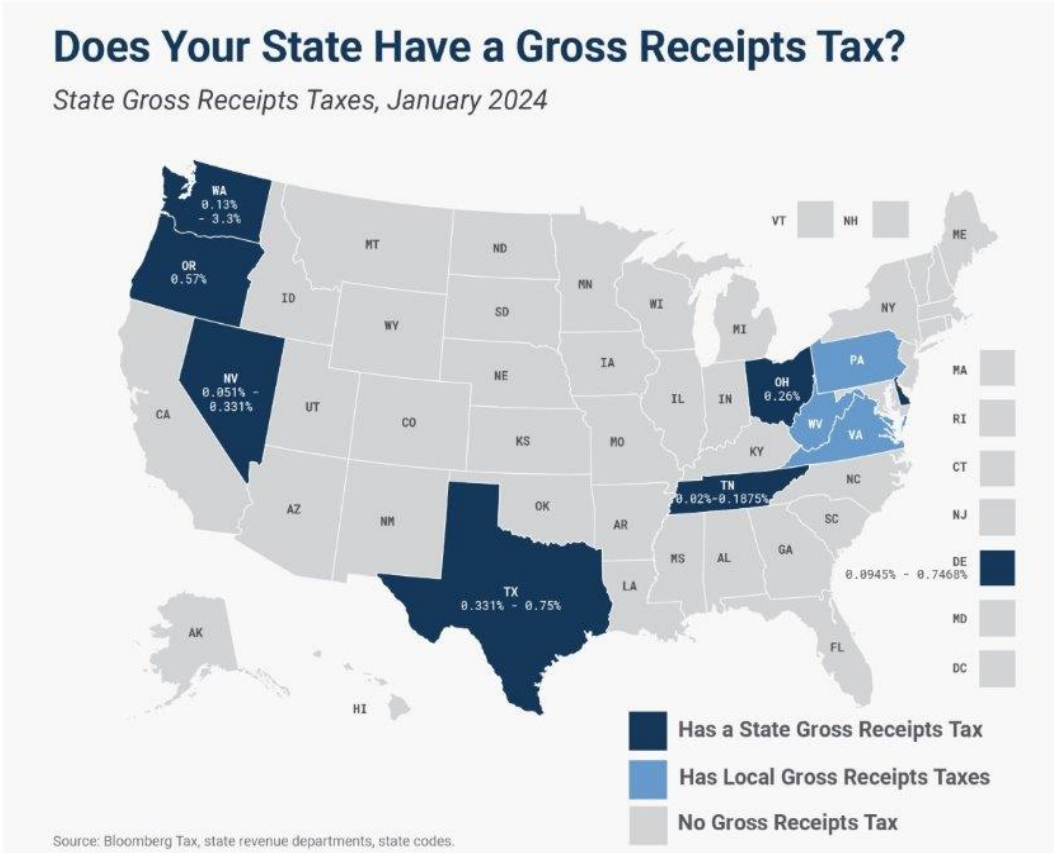
Practical Virginia Locality Scenario: Visual Representation



Potential Fiscal Impact - Statewide

Based on FY25 data for ***only 4*** Arlington-based companies that use payroll apportionment & assuming Arlington share of Virginia GDP applies to the State...

Arlington VA GDP	$41,000,000,000
VA State GDP	$597,000,000,000
Share of Arlington of VA GDP	7%
Partial Estimate of HB1743 Impact on Arlington, VA*	$4,200,000
Projected Calculation of HB1743 state-wide impact	**$60,000,000**



Revenues Across Virginia May Decrease Annually By More Than $60 Million

COMMISSIONERS OF THE REVENUE ASSOCIATION OF VIRGINIA

Fairness

"Virginia is committed to creating an environment where entrepreneurs and small businesses can thrive, grow and succeed."

-Gov. Glenn Youngkin

Large Nationwide Businesses

Already enjoy tax benefits and incentives designed to encourage business growth and <u>are more likely to benefit from HB 1743 due to having significant interstate operations</u>.

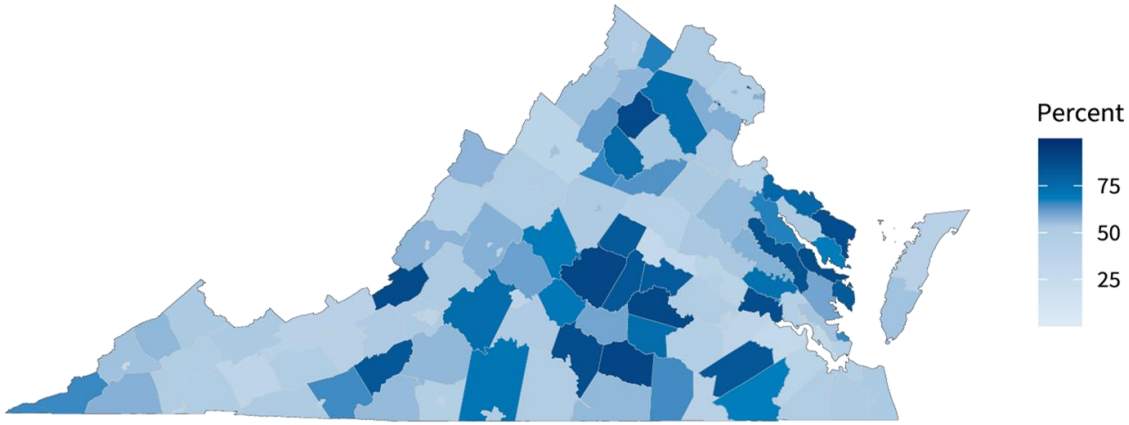
Including, but not limited to:

- Major Business Facility Job Credit
- Research and Development Tax Credit
- Virginia Economic Development Incentive Grant (VEDIG)
- Port of Virginia Economic and Infrastructure Development Grant

Small Businesses

818,450 small businesses in VA making up **99.5%** of VA businesses

1.6 million small business employees in VA making up **45.4%** of VA employees



Share of employees working at small businesses by county or independent city

Source of original data: Statistics of US Businesses (Census)

Large Businesses Already Enjoy Tax Benefits and HB 1743 Offers Minimal To No Benefit To Locally Owned & Operated Small Businesses

Increased Tax Complexity

State Mandate Creates Unfunded Local Burden

Additional Administrative Burden

The lack of uniformity in gross receipts tax thresholds across states leads to inequities particularly regarding eligibility for out-of-state deductions.

- For example, starting in 2025, Ohio's Commercial Activity Tax (CAT) will apply to businesses with taxable gross receipts exceeding $6 million (twice the previous threshold). This change further exempts smaller businesses from the requirement to file and pay the CAT. Thresholds for gross receipts tax vary by state may lead to different tax outcomes for similar taxpayers.

Gross receipts taxes and income taxes operate under fundamentally different principles, apply distinct standards for taxation. By amending the law to include a gross receipts tax which has a very broad base compared to a net income tax and is not subject to the limitations provided under P.L. 86-272, HB 1743 is compounding a problem.

- It introduces inequity as the tax policy will now be based on two completely different tax regimes with divergent underlying principles. The nexus requirements are completely different. The gross receipts tax does not start with the federal taxable income as state income taxes do in many states, including Virginia.

The former language in HB1743 referring to deduction eligibility for states which impose other taxes imposed "in lieu of an income tax" produces uncertainty. It could be interpreted to apply to taxes such as sales taxes or business property taxes if adopted.

Legal Considerations

- The BPOL tax as currently written is compliant with the Commerce Clause because it provides for fair apportionment among states on the basis of the share of work done in a state

- Opinions of the Virginia Supreme Court, Tax Commissioner and Attorney General have all found the current statute to be in compliance with the Commerce Clause


COMMONWEALTH OF VIRGINIA
VIRGINIA
SIC SEMPER TYRANNIS
COMMISSIONERS OF THE
REVENUE ASSOCIATION


VIRGINIA
VML
MUNICIPAL LEAGUE


VACo
Virginia Association of Counties

Thank you!

APPENDIX

HB 1743 – IMPACT ANALYSIS V2.0

- DEFINITIONS
- MITIGATION NEEDS

JUNE | 3 | 2025

Definitions

Situs: The jurisdiction to which, for purposes of taxation, property or income belongs and is taxable.

Deduction: An amount subtracted from gross receipts reducing the taxable basis.

BPOL Statute: Business, Professional, and Occupational License tax statute.

Gross Receipts: The total amount of money received by a business from its operations, before any deductions.

Income-like Tax: A tax based on a computation similar to federal income tax, where gross revenues are reduced by business-related expenses.

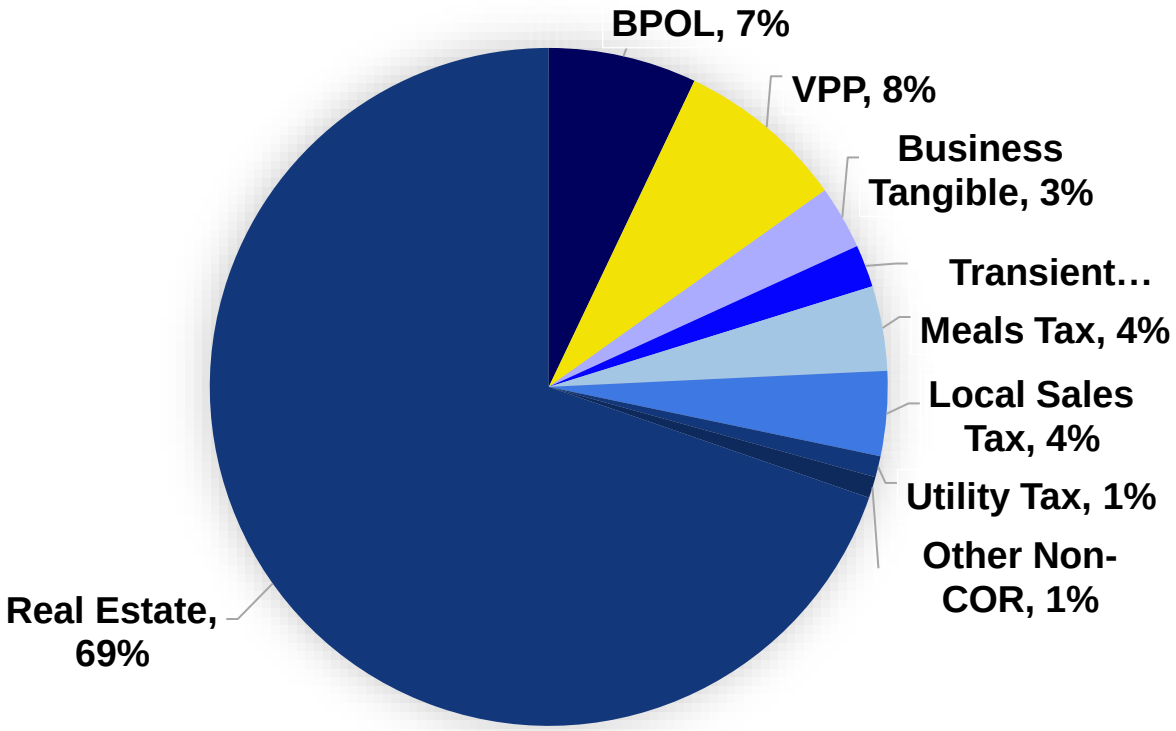
Payroll Apportionment: A method of allocating gross receipts based on the distribution of payroll across different states.

Mitigation Needs if HB1743 Passes

- **Revenue Replacement Mechanisms**
  - Funding to make up fiscal short fall.
- **Phase-in Periods**
  - Gradually implement the new deduction rules over several years. State that any new deduction rules are not retroactive.
- **Caps on Deductions**
  - Set a maximum dollar amount or percentage that a business can deduct.
- **Sunset Clauses**
  - Automatically end or review the deduction after a set period unless renewed by legislation.

This Fiscal Impact Will Be Felt By Localities

Composition of Arlington County Revenue



In Arlington, BPOL accounts for 7% of County Revenue, equivalent to ~$105M.

Services Could Be Decreased Or Even Cut

APPENDIX D: Comments Received Subsequent to the First Meeting

July 2, 2025

Dear Commissioner Alex:

The Virginia Chamber of Commerce (Virginia Chamber) is the largest business advocacy organization in the Commonwealth, with more than 30,000 members. The Chamber is a non-partisan, business advocacy organization that works in the legislative, regulatory, and political arenas to act as the catalyst for positive change in all areas of economic development and competitiveness for Virginia.

The Virginia Chamber is writing to address a concern regarding the Virginia Department of Taxation's ("Department") interpretation of the Business Professional and Occupational License Tax's ("BPOL Tax") deduction for out-of-state receipts ("Out-of-State Deduction"). The Department interprets the Out-of-State Deduction to not apply to states' gross receipts taxes. This interpretation adversely impacts Virginia taxpayers, particularly Virginia-headquartered taxpayers, by causing their receipts to be subject to both the BPOL Tax and other states' gross receipts taxes.

We respectfully request that the Department allow taxpayers to claim the Out-of-State Deduction for taxes that are based on gross receipts. This approach is consistent with the purpose and plain language of the Out-of-State Deduction statute and the Department's longstanding regulation that governs the administration of that statute.

Overview of the BPOL Tax and the Out-of-State Deduction

Pursuant to state law, Virginia localities may impose a BPOL Tax on a taxpayer's gross receipts within the jurisdiction[1]. In calculating the BPOL Tax, Virginia law allows for numerous exclusions and deductions from the tax base, including the Out-of-State Deduction for:

> Any receipts attributable to business conducted in another state or foreign country in which the taxpayer (or its shareholders, partners or members in lieu of the taxpayer) is liable for an income or other tax based upon income.[2]

The Department has construed the Out-of-State Deduction to be limited to traditional income taxes. It has issued a few rulings addressing whether specific other state taxes qualify for the Out-of-State Deduction. Namely, in 2018 and 2022, the Department concluded that the Ohio Commercial Activity

[1] Va. Code Ann. § 58.1-3703.1(A)(3)(a).
[2] Va. Code Ann. § 58.1-3732(B)(2)

Tax, Texas Margin Tax, and Washington Business and Occupation Tax do not qualify for the Out-of-State Deduction.[3]

However, the Department's longstanding regulation has acknowledged that the Out-of-State Deduction is not limited to solely traditional income taxes. The Department's regulation describes the statutory Out-of-State Deduction for "an income or other tax based on income" as applying to both income taxes and "income-like tax[es]."[4]

The Department's interpretation of the Out-of-State Deduction should be consistent with its purpose of eliminating the risk of double taxation

The Department should permit the Out-of-State Deduction for gross receipts-based taxes. This approach is consistent with the purpose for the deduction, which is to limit the double taxation of Virginia taxpayers' interstate receipts. The BPOL Tax's unique structure causes it to tax receipts that would normally be taxed outside of Virginia.[5] Specifically, under the BPOL Tax regime, a retailer with a Virginia sales office or a company that provides services from a Virginia office will be subject to the BPOL Tax on sales that are also taxed by other states. Unless the Out-of-State Deduction applies, taxpayers' interstate sales are subject to a high risk of double taxation.

The risk of double taxation particularly impacts Virginia-headquartered companies because they are likely to engage in sales and service-performance activities through large amounts of employees and property in Virginia. Importantly, the double taxation risk incentivizes companies to locate outside of Virginia. For companies headquartered outside of Virginia that do not have a Virginia location, the BPOL Tax would not apply. Such companies would therefore have an advantage because they would be subject to only one layer of state tax rather than two.

The Out-of-State Deduction is intended to eliminate this double taxation risk. However, under the Department's interpretation of the Out-of-State Deduction, the deduction is not available if the other state imposes a gross receipts-based tax, rather than a net income tax. An interpretation of the Out-of-State Deduction that allows a deduction for gross receipts-based taxes is consistent with the purpose of the deduction. Gross receipts-based taxes, especially when imposed by states that do not otherwise impose a corporate net income tax, like Ohio, Texas, and Washington, are effectively income taxes. The primary difference is merely that traditional income taxes are based on net income (i.e., net of expenses and other deductions), while a gross receipts-based tax is based on gross income. The gross receipts-based tax also serves the same purpose as a traditional income tax. Both types of taxes generate revenue

[3] Va. Public Document Ruling No. 22-117 (Jul. 21, 2022); Va. Public Document Ruling No. 18-170 (Oct. 10, 2018).
[4] Va. Admin. Code tit. 23, § 10-500-80(A)(2).
[5] See Va. Admin. Code tit. 23, § 10-500-80(B) (providing examples of sales of goods to non-Virginia customers that are, in the absence of the Out-of-State Deduction, subject to BPOL Tax)

for their states derived from the taxpayers' receipts-producing activities. Thus, the Out-of-State Deduction should apply to gross receipts-based taxes.

The Out-of-State Deduction should be allowed in a manner that is consistent with the plain language of the statute

The Department's explanation in its rulings as to why gross receipts taxes do not qualify for the Out-of-State Deduction is based on a misconception that the deduction applies to only net income taxes. For example, in a 2022 public document ruling, the Department denied the Outof-State Deduction for certain gross receipts taxes because the tax bases were not "equivalent to or measured by net income."[6]

In contrast with the Department's interpretation, the Virginia General Assembly did not specifically choose to limit the deduction to only net income taxes. Rather, the Virginia legislature has statutorily provided that the Out-of-State Deduction is allowed for an "income or other tax based upon income." A plain reading of this statute supports that the Out-of-State Deduction applies to both net and gross income-based taxes.

Had the legislature intended to limit the Out-of-State Deduction to only net income taxes, it could have done so but did not. In fact, elsewhere in Virginia tax law, the legislature has specifically taken that approach. For example, in calculating the Virginia Corporation Income Tax, Virginia statutes require the addition to federal taxable income of "...any net income taxes and other taxes, including franchise and excise taxes, which are based on, measured by, or computed with reference to net income …" [7] The Virginia legislature did not include this same limiting language for purposes of the Out-of-State Deduction.

Virginia Code Ann. § 58.1-3732(B)(2) does not restrict the Out-of-State Deduction to "net income taxes," but broadly allows for a deduction for "taxes based upon income." A reasonable interpretation of this broadly-worded language is that it provides a deduction for other types of taxes, including gross receipts-based taxes. Thus, a deduction for taxes imposed by states that do not impose an income tax, like Ohio, Texas, and Washington, should be permitted. Such taxes are the states' equivalent of an income tax and are based on taxpayers' income.

The Department's interpretation should be consistent with its longstanding regulation.

The Department's regulation set forth in Va. Admin. Code tit. 23, § 10-500-80(A)(2) provides that the Out-of-State Deduction is allowed for income taxes and "income-like tax[es]." In its regulation, the Department offers multiple examples of how to apply the Out-of-State Deduction. In the second

[6] Va. Public Document Ruling No. 22-117 (Jul. 21, 2022).
[7] Va. Code Ann. § 58.1-402.B.4 (emphasis added). See also Va. Admin. Code tit. 23, § 10-120-101.D.

example, with respect to a merchant selling goods to Ohio customers, the Department acknowledged that it considered a tax to be "an income or other tax based upon income," even if not a "net income" tax:

> Same facts as in Example 1[8] except that sales are delivered to a customer in Ohio. In Ohio, merchant pays either a tax based on income or based on net worth, whichever is greater. Merchant files the appropriate Ohio tax return. Gross receipts (or the cost of purchases if merchant is taxable on purchases) from sales delivered in Ohio are deductible from merchant's Virginia BPOL taxable gross receipts. Receipts attributed to business conducted in another state or foreign country in which the taxpayer is liable for an income or an income based tax are deductible from Virginia BPOL taxable gross receipts, if such receipts are also attributable to a definite place of business in Virginia.[9]

In this example, Virginia taxpayers were permitted to claim the Out-of-State Deduction against Ohio's now-repealed Corporate Franchise Tax, which the Department acknowledged was an "an income or other tax based upon income." The Ohio Corporate Franchise Tax was calculated on the greater of two bases: income and net worth. A tax based on net worth is plainly not a tax based on net income. Thus, the Department – via its own regulation – has not interpreted the Out-of-State Deduction as applying to only net income taxes. The Department's interpretation of the Out-of-State Deduction should be consistent with the regulation it has promulgated, which allowed a deduction for other taxes based upon income.

The BPOL Tax risks distorting taxpayers' Virginia gross receipts, in violation of the U.S. Constitution.

Finally, denying the Out-of-State Deduction for gross receipts-based taxes risks substantially overstating a taxpayer's receipts that are attributable to Virginia localities and does not reflect the taxpayer's business transacted in the locality. Thus, not allowing the deduction of receipts subject to gross receipts-based taxes can result in a BPOL Tax assessment that is not fairly apportioned in violation of the Commerce Clause of the U.S. Constitution.

To comply with the Commerce Clause, the Attorney General has opined that the Out-of-State Deduction "should be applied to business outside the Commonwealth so that the assessments are fairly apportioned between the activity in [the] jurisdiction and the activity outside the Commonwealth."[10] This mandate requires that the BPOL Tax "apply only to the 'portion of the revenues from the interstate

[8] Example 1 related to a merchant selling goods to a North Carolina resident and shipping the goods to him in that state. Va. Admin. Code tit. 23, § 10-500-80(B)(1).
[9] Va. Admin. Code tit. 23, § 10-500-80(B)(2).
[10] Att'y Gen. Opin. 02-114 (Dec. 12, 2002).

activity which reasonably reflects the in-state component of the activity being taxed'" (i.e., be externally consistent).[11]

By denying the Out-of-State Deduction for gross receipts-based taxes, the Department violates the Commerce Clause's external consistency test. The Department's position distorts taxpayers' Virginia receipts by over-representing the amount of a taxpayer's business that is transacted in Virginia localities. While taxpayers are subject to the BPOL Tax based on performing activities at a Virginia location, substantial non-Virginia activities (e.g., in Ohio, Texas, Washington, etc.) are also subject to the BPOL Tax because of the lack of a deduction for such interstate receipts. And as discussed above, restricting the Out-of-State Deduction to only net income taxes risk the double taxation of Virginia taxpayers' receipts. These outcomes violate the U.S. Constitution.

For the above reasons, the Virginia Chamber respectfully requests that the Department permits the Out-of-State Deduction for taxes that are based on gross receipts. If you have any questions about this request or would like to discuss it further, please reach out to me at (804) 418-2795 or by email at C.Whitelow@vachamber.com.

Thank you for your consideration of this request.

Respectfully,

Carter T. Whitelow
Vice President, Government Relations
Virginia Chamber of Commerce

CC: The Honorable Stephen E. Cummings, Secretary of Finance
Jason Powell, Deputy Secretary of Finance
The Honorable Juan Pablo Segura, Secretary of Commerce and Trade

[11] Id. (citing City of Winchester v. Am. Woodmark Corp., 252 Va. 98, 102 (1996)).

Commissioners of the Revenue Association of Virginia's (CORVA) Comments to the HB 1743 Study Group

On Tuesday, June 2, 2025, the Virginia Department of Taxation convened a workgroup to address HB 1743. Each workgroup member/organization was asked to provide commentary. VML, VACO, and CORVA provided a single partnered presentation to the Virginia Department of Taxation and the workgroup members.

While we are aligned in our views and recommendations with our partners, CORVA is providing our specific written comments in our order of concern and priority. Therefore, our written comments are as follows:

(1) FISCAL IMPACT

The proposed change to the out-of-state deduction will have a significant negative impact on locality revenues in a time of mounting fiscal uncertainty.

As a means to gauge the fiscal impact, Arlington County Commissioner of Revenue computed an initial assessment of this impact. Arlington reviewed recent audits of four companies with significant interstate operations. Assuming that the proposed expansion of the deduction to include those states that impose a gross receipts tax were enacted, an annual loss of $4.2 million of BPOL tax revenue would result *from just these four companies alone*. Extrapolating this estimate proportionally to the rest of the state from Arlington's share of statewide GDP would generate an estimated minimum of **$60 million** in revenue loss for localities across the state annually. The expected revenue loss would almost certainly be significantly larger than this, given the extremely limited nature of the sample examined (*i.e.* four companies). See Exhibit A for more details.

The legislation under consideration did not provide any mechanism for the Commonwealth to replace this lost revenue with state funds. If the General Assembly does enact this provision, it should provide such funding on an ongoing basis.

This proposed change comes at a particularly difficult moment for localities. Local budgets in Virginia are under pressure to eliminate the car tax, as well as recent federal initiatives that are also likely to reduce local revenues, including reduced employment due to federal worker firings, termination of numerous federal contracts and direct reductions in federal funding to localities. See Exhibit B for more details.

(2) FAIRNESS

If enacted, the benefits of an expanded out-of-state deduction would accrue disproportionately to the benefit of large, multistate or multinational corporations due to the very nature of the deduction. Smaller companies with local footprints do not benefit from a deduction for operations in other states and countries. Small businesses make up 99.5% of Virginia businesses, leaving just 0.5% of businesses in the Commonwealth to benefit most from this costly policy change.

Larger multinational corporations already enjoy significant tax breaks, subsidies, and other advantages.

In addition, while the out-of-state deduction is intended to prevent double taxation, its application in its current form can actually result in non-taxation of certain receipts.

This occurs because the BPOL tax already uses situs-based sourcing rules to allocate gross receipts to the locality where the business activity occurs, effectively preventing multiple jurisdictions from taxing the same revenue. However, the current deduction framework introduces income tax concepts, such as liability to file in another jurisdiction, into a gross receipts tax system that is fundamentally based on the location of business activity. This overlay creates a structural mismatch: receipts that are properly situsted to a Virginia locality may be deducted simply because they appear on an income tax return filed elsewhere, even if they were not actually taxed in that jurisdiction.

As a result, the deduction can override the situs rules and allow businesses to exclude receipts that were never subject to tax anywhere, undermining the fairness and integrity of the BPOL system.

This problem is multiplied if the deduction is expanded.

(3) INCREASED ADMINISTRATIVE BURDEN

Expanding the out-of-state deduction to cover other types of taxes would increase the administrative burden of assessing BPOL taxes for both localities and taxpayers.

a. Burden on Taxpayers

The current BPOL deduction framework is aligned with standardized principles used in income tax reporting. Introducing gross receipts taxes, which lack such uniform definitions and filing standards, would disrupt this consistency. Taxpayers may be required to compile and submit additional data—such as revenue by jurisdiction, customer location, and work performance details—to substantiate their deduction claims. This adds complexity and increases compliance costs for taxpayers.

b. Burden on Localities

Many taxpayers currently base their out-of-state deduction on apportionment data used for state income tax filings. However, gross receipts taxes often use different tax bases and sourcing rules. As a result, taxpayers could claim deductions that exceed their actual gross receipts, especially when combining data from multiple tax types. This discrepancy would increase the risk of over-deduction and require localities to conduct more frequent and detailed audits to verify claims.

Allowing deductions for non-income-based taxes would require local tax assessors to understand and evaluate new tax structures across all 50 states (including potentially their localities) and, for multinational taxpayers, foreign jurisdictions. This would place a significant burden on local governments and the Virginia Department of Taxation, which would need to allocate additional resources to research, training, and enforcement. The complexity and uncertainty also raises the likelihood of disputes and litigation. Most local audit programs are based on compliance of local taxes, not financial audits which are very detailed and time and resource consuming.

The proposed legislation does not clarify how to prioritize or interpret deductions when a state imposes both income and gross receipts taxes, but the taxpayer is only subject to one. It also opens the door to arguments for deductions based on local gross receipts taxes, sales taxes, or other non-income-based levies, depending on the wording of the legislation. Additionally, the term "liable to file," which has been clarified in prior rulings for income tax purposes, may not translate cleanly to gross receipts taxes, which have different nexus thresholds, rates, and filing requirements.

(4) CONSTITUTIONALITY

The legal arguments made by corporate special interest group members of the study group about the constitutionality of the existing BPOL tax structure to the Department of Taxation are without merit. The proposed expansion of the out-of-state deduction is not necessary to ensure compliance with the Commerce Clause. The Virginia Supreme Court, the Tax Commissioner and the Attorney General have each issued rulings confirming that the BPOL tax as currently enacted complies with the Commerce Clause.

A state tax violates the Commerce Clause if it (1) applies to an activity lacking a substantial nexus to the taxing state; (2) is not fairly apportioned; (3) discriminates against interstate commerce; or (4) is not fairly related to the services provided by the state. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977).

The BPOL tax applies to businesses that have a place of business in the state and so meets the substantial nexus test.

A tax is fairly apportioned if it is both internally and externally consistent. A tax is internally consistent if, assuming that every other jurisdiction applied the same statute, the taxpayer would not be subjected to a risk of double taxation. An assessment is externally consistent if the assessment applies only to the portion of revenues from interstate activity which reasonably reflects the in-state component of the activity being taxed.

The BPOL tax is internally consistent because if it were applied by every other state, there would be no risk of double taxation because each state would apportion to itself and tax only those gross receipts earned at a definite place of business within that state. The BPOL tax is also externally consistent because its situs rules ensure that the tax applies only to the portion of the revenues from interstate activity which reasonably reflects the in-state component of the activity being taxed. Revenues earned by businesses for work performed at an out-of-state location are situsued to that state for taxation in proportion to the amount of work performed there.

The BPOL tax does not discriminate against interstate commerce because gross receipts from domestic, interstate and international activities are treated exactly the same.

The BPOL tax is fairly related to the services provided by localities because it funds services (such as roads, police, firefighting, etc.) provided by the locality to residents, including businesses with a definite place of business in the county subject to the BPOL tax.

(5) SUMMARY & RECOMMENDATIONS

Due to the current economic climate, fiscal impact, unfairness, and increased administrative burden, CORVA recommends that the BPOL statute not be amended to expand the out-of-state deduction. CORVA is amenable to work with the Virginia Department of Taxation to revisit and refresh the 2000 BPOL Guidelines to promote uniformity of interpretation.

Exhibit A

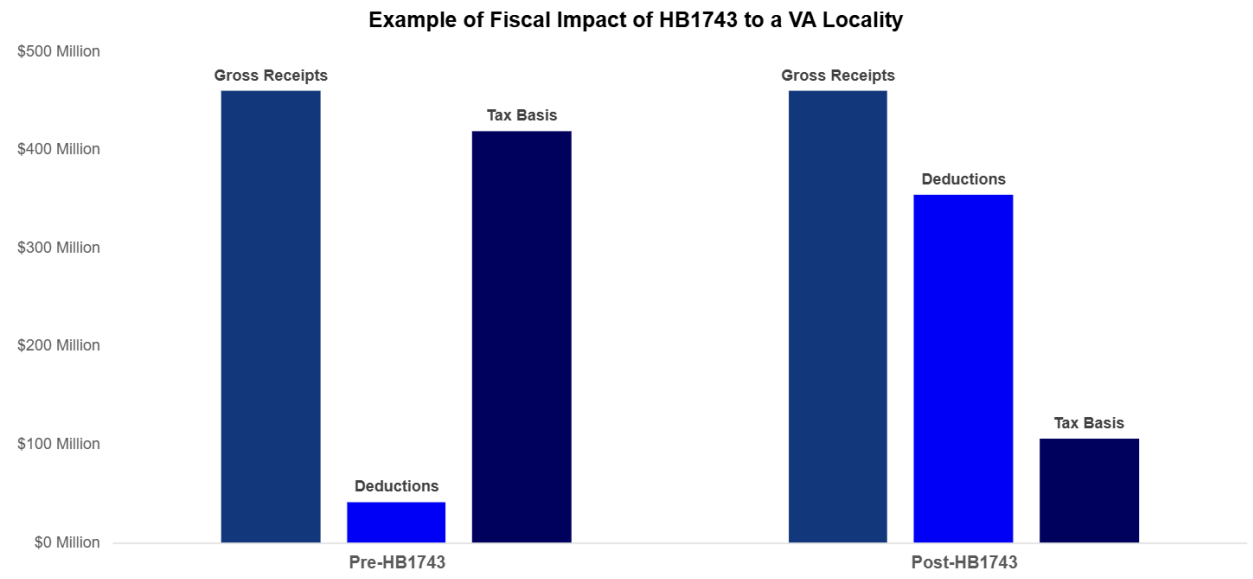
Sample Business: Potential Impact on Tax Basis

		Current			HB1743		
Situs based on Payroll Apportionment	Payroll Apportionment	Deductible (based on filing state income tax return)	Taxable Gross Receipts based on Payroll Apportionment	Deduction Amount	Deductible (based on expansion to include gross receipts like tax)	Taxable Gross Receipts based on Payroll Apportionment	Deduction Amount
VA	23%	Y	$460,000,000		Y	$460,000,000	
PA	6%	Y		$27,600,000	Y		$27,600,000
MD	3%	Y		$13,800,000	Y		$13,800,000
WA	68%	N		$0	Y		$312,800,000
Total Deduction				$41,400,000			$354,200,000
BPOL Tax Basis				$418,600,000			$105,800,000
Tax Revenue				**$1,465,100**			**$370,300**

Classification: Section 58 - Personal Services
Arlington County Tax Rate: 0.0035
Definite Places of Business: VA, PA, MD, WA
Total Gross Receipts: $2,000,000,000

Revenue Loss of 75% ($1,094,800)

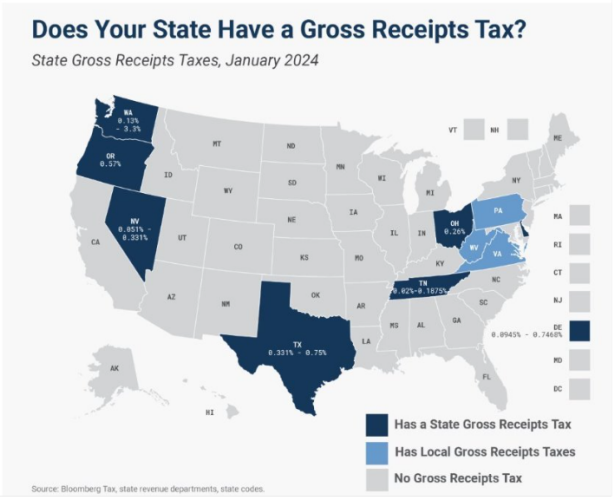
Sample Business: Potential Impact on Tax Basis



Potential Fiscal Impact - Statewide

Based on FY25 data for ***only 4**** Arlington-based companies that use payroll apportionment & assuming Arlington share of Virginia GDP applies to the State...

Arlington VA GDP	$41,000,000,000
VA State GDP	$597,000,000,000
Share of Arlington of VA GDP	7%
Partial Estimate of HB1743 Impact on Arlington, VA*	$4,200,000
Projected Calculation of HB1743 state-wide impact	**$60,000,000**

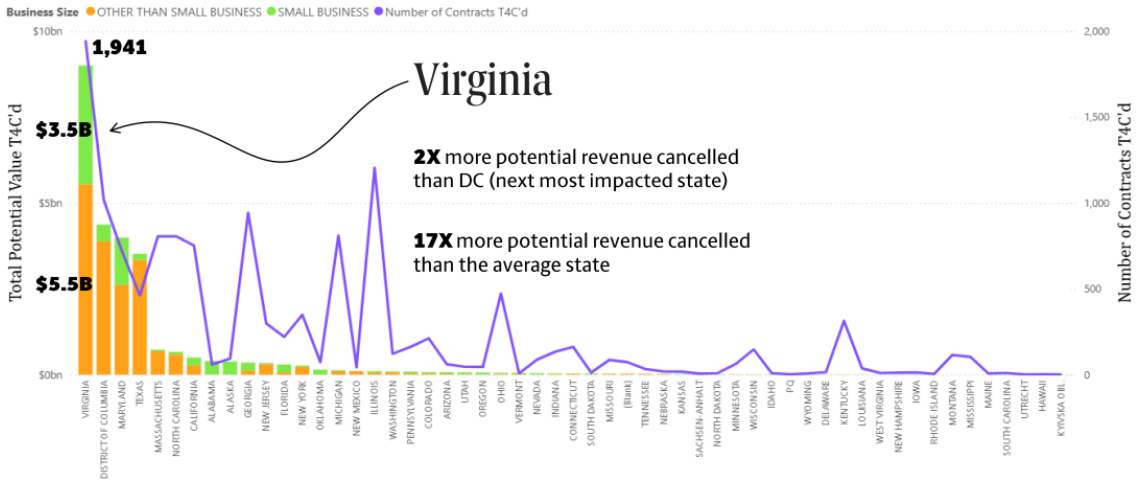


Revenues Across Virginia May Decrease Annually By More Than $60 Million

Exhibit B

ForsMarsh

Contract Awards* Terminated by State



Company Location (State)

*Contract awards include funded delivery/task orders on contract vehicles (BPAs and IDIQs) and standalone contracts. This is the most accurate account of potential revenue loss.

3

Patrick J. Reynolds
President & Executive Director
(202) 484-5218
preynolds@cost.org

July 8, 2025

VIA EMAIL TO:

Vivek Bakshi
Virginia Department of Taxation
Legislative Work Group to Study BPOL Out-of-State Deduction

Re: COST Comments to the Virginia BPOL Workgroup

Dear Members of the Virginia BPOL Workgroup:

On behalf of the Council On State Taxation (COST), I respectfully submit these comments related to Virginia's current business, professional, and occupational license tax (BPOL), which is a gross receipts tax imposed at the local level. Currently, the statute allows a deduction from gross receipts for "[a]ny receipts attributable to business conducted in another state or foreign country in which the taxpayer (or its shareholders, partners or members in lieu of the taxpayer) is liable for an income or other tax based upon income."[1] We respectfully urge the Workgroup to recommend legislation to clarify that "income or other tax based on income" includes not just "net income tax" but also "gross income tax." This position is consistent with: 1) earlier guidance from the Department of Taxation; 2) recent guidance regarding the BPOL and federal law; and 3) U.S. Constitution limitations.

About COST

COST is a nonprofit trade association based in Washington, DC. COST was formed in 1969 as an advisory committee to the Council of State Chambers of Commerce and today has an independent membership of approximately 500 major corporations engaged in interstate and international business, many of which do business in Virgina and are subject to the local BPOL taxes. COST's objective is to preserve and promote equitable and nondiscriminatory state and local taxation of multistate business entities.

Earlier Guidance That "Income Tax" Included "Gross Income Tax"

During the Workgroup discussion, it was clear that the Department of Taxation initially took the position that "income or other tax based on income" for purposes of the deduction was not limited to "net income tax" but also included "gross income

[1] Virginia Code § 58.1-3732(b)(2) (https://law.lis.virginia.gov/vacode/title58.1/chapter37/section58.1-3732/#:~:text=A.,the%20ordinary%20course%20of%20business.)

tax" or "gross receipts tax." This position intuitively makes sense as the BPOL tax itself is a gross receipts tax. Therefore, the BPOL deduction should include receipts attributable to business conducted in another state or foreign country in which the taxpayer is liable for a gross receipts tax (*i.e.*, gross income tax).

Recent guidance[2] from the Department of Taxation has created confusion by suggesting that taxpayers' BPOL deductions are restricted to receipts attributable to business conducted in another state or foreign country that imposes a "net income tax." We think this guidance is inconsistent with the statute and prior guidance from the Department.

Recent Guidance Finding the BPOL is an Income Tax Under Federal Law

Six months after issuing guidance that caused confusion, the Department issued seemingly inconsistent guidance,[3] that the BPOL, which is a gross receipts tax, is an "income tax" under the federal Buck Act,[4] which protects state and local income taxes on activity occurring within a federal area. Granted, the federal Buck Act specifically defines "income tax" as "any tax levied on, with respect to, or measured by, net income, gross income, or gross receipts." However, we believe it is inconsistent to hold that other states gross receipts taxes are not income taxes but the BPOL, which itself is a gross receipts tax, is an income tax.

Failure to Correct the Issue Raises Constitutional Concerns

The U.S. Constitution requires state and local taxes to be fairly apportioned and not based on extraterritorial activity.[5] By denying a deduction for gross receipts attributable to jurisdictions that impose a gross receipts tax or modified gross receipts tax and not an income tax, BPOL is effectively taxing activity in those jurisdictions outside of Virginia. The BPOL should instead provide for a deduction attributable to receipts sitused first to a Virginia jurisdiction that are also subject to an out-of-state gross income or net income tax. We suggest the legislative intent of the deduction is and always has been to avoid the incidence of double taxation.

Conclusion

COST respectfully urges the Workgroup to recommend legislation to clarify that the BPOL deduction for taxpayers extends to gross receipts attributable to business conducted in another state or foreign country for both net income taxes and gross income taxes. If you have any questions or would like to discuss further, please do not hesitate to contact me.

Sincerely,

Patrick J. Reynolds, President & Executive Director

CC: COST Board of Directors
Delegate Vivian E. Watts

[2] Tax Commissioner Ruling 22-117, July 21, 2022 (https://www.tax.virginia.gov/laws-rules-decisions/rulings-tax-commissioner/22-117)
[3] Tax Commissioner Ruling 22-164, December 20, 2022 (https://www.tax.virginia.gov/laws-rules-decisions/rulings-tax-commissioner/22-164)
[4] 4 U.S.C. §§ 105-110
[5] *Complete Auto Transit v. Brady*, 430 U.S. 274 (1977).

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Sent via email to vivek.bakshi@tax.virginia.gov

July 7, 2025

Commissioner James J. Alex
Virginia Department of Taxation
Legislative Work Group to Study BPOL Out-of-State Deduction

Dear Commissioner Alex:

We are submitting these comments in response to the recent discussion by the 2025 Work Group to Review the BPOL Out-of-State Deduction ("Workgroup"). We address two areas raised in the Work Group's discussion: (1) the constitutionality infirmities of the Virginia Business, Professional and Occupational License Tax ("BPOL Tax") deduction for out-of-state receipts subject to other states' income taxes ("Out-of-State Deduction"); and (2) concerns raised by localities about the expansion of the Out-of-State Deduction to out-of-state receipts subject to other states' taxes that are based on gross receipts, imposed in lieu of traditional income taxes.

We respectfully request that the Work Group support amending the Out-of-State Deduction to include state taxes that are based on gross receipts, imposed in lieu of a traditional income tax. This approach is consistent with the purpose of the Out-of-State Deduction statute and avoids Commerce Clause infirmities, namely external consistency.

I. Business, Professional, and Occupational License Tax

Under Virginia law, localities may impose a BPOL Tax on a taxpayer's gross receipts "attributed to the exercise of a privilege subject to licensure at a definite place of business within this jurisdiction."[1] Virginia sets out a variety of provisions to determine where to attribute gross receipts on the basis of the underlying activity:

- Activities conducted outside of a definite place of business: Attributed to the definite place of business from which the activities are "initiated, directed, or controlled";[2]
- Contractors: Attributed to the definite place of business at which the services are performed. If not performed at a definite place of business, then – in general – to the definite place of business where the services are "directed or controlled";[3]

[1] *See generally*, Va. Code Ann. § 58.1-3703.1(A)(3)(a).

[2] Va. Code Ann. § 58.1-3703.1(A)(3)(a).

[3] Va. Code Ann. § 58.1-3703.1(A)(3)(a)(1)

- Retailers or Wholesalers: Attributed to the definite place of business at which the "sales solicitation activities occur." But if they do not occur at a definite place of business, then they are attributed to "the definite place of business from which sales solicitation activities are directed or controlled";[4]

- Tangible Personal Property Rentals: Attributed to the definite place of business from which the tangible personal property is rented. But if the tangible personal property is not rented from a definite place of business, the gross receipts are attributed to the definite place of business from where the rental is managed;[5]

- Services: Attributed to the definite place of business at which the services are performed. But if the services are not performed at any definite place of business, the gross receipts are attributed to the definite place of business from where the services are directed or controlled.[6]

The BPOL Tax's unique structure causes it to tax receipts that would normally be taxed outside of Virginia.[7] For example, while a retailer's sales are subject to the BPOL Tax at the location of the sales' solicitation, other states' gross receipts and income taxes typically tax receipts at the location of delivery.[8] For sales of services, while the BPOL Tax sources receipts to the location of the service's performance (i.e., the location of the taxpayer's employees and property), many gross receipts and income-based taxes source these receipts to the location of the taxpayer's customer.[9] Thus, a retailer with a Virginia sales office or a company that provides services from a Virginia office will be subject to the BPOL Tax on these sales that are also being taxed by other states.

To avoid the inevitable multiple taxation caused by the BPOL Tax's unusual structure, Virginia law allows for numerous exclusions and deductions from the tax base including the Out-of-State Deduction. The Out-of-State Deduction provides a deduction for:

> Any receipts attributable to business conducted in another state or foreign country in which the taxpayer (or its

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4 Va. Code Ann. § 58.1-3703.1(A)(3)(a)(2). However, some localities instead impose the license tax on wholesalers or distribution houses that is "measured by purchases." In that case, the situs is "the definite place of business at which or from which deliveries of the purchased goods, wares and merchandise are made to customers." *Id.*

5 Va. Code Ann. § 58.1-3703.1(A)(3)(a)(3).

6 Va. Code Ann. § 58.1-3703.1(A)(3)(a)(4).

7 *See* Va. Admin. Code tit. 23, § 10-500-80(B) (providing examples of sales of goods to non-Virginia customers that are, in the absence of the Out-of-State Deduction, subject to BPOL Tax).

8 Va. Code Ann. § 58.1-3703.1(A)(3)(a)(2).

9 Va. Code Ann. § 58.1-3703.1(A)(3)(a)(4).

> shareholders, partners or members in lieu of the taxpayer) is liable for **an income or other tax based upon income**.[10]

The Virginia Department of Taxation ("Department"), in a regulation, describes the Out-of-State Deduction as relating to an "income-based" or "income-like" tax.[11] However, the Department has construed the Out-of-State Deduction to be limited to traditional income taxes.

II. Constitutional Limits on State Taxes, including the BPOL Tax

The United States Constitution imposes various limitations on states' ability to enact taxes. In particular, the Commerce Clause of the United States Constitution states that "Congress shall have the power … To regulate commerce … among the several states[.]"[12]

For a tax to comply with the dormant Commerce Clause, it must satisfy the four-part test described in *Complete Auto Transit*. Under that test, a tax must: (1) be applied to an activity with a substantial nexus with the taxing state, (2) be fairly apportioned, (3) not discriminate against interstate commerce, and (4) be fairly related to the services provided by the state.[13]

To satisfy the "fairly apportioned" prong of the test, a state tax must be both internally and externally consistent.[14] Under the internal consistency test, "a tax must be structured so that if every State were to impose an identical tax, no multiple taxation would result."[15]

The external consistency test instead "asks whether the State has taxed only that portion of the revenues from the interstate activity which reasonably reflects the in-state component of the activity being taxed."[16] Ultimately, the external consistency test "looks to the economic justification for the State's claim upon the value taxed, to discover whether the tax reaches beyond the portion of value that is fairly attributable to economic activity within the taxing State."[17] The court examines "the in-state business activity which triggers the taxable event and the practical or economic effect of the tax on that interstate activity."[18] The Virginia Supreme Court has observed:

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10 Va. Code Ann. § 58.1-3732(B)(2) (emphasis added).

11 23 Va. Admin. Code § 10-500-80.

12 U.S. Const. art. I, § 8, cl. 3.

13 *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977).

14 *Goldberg v. Sweet*, 488 U.S. 252, 261 (1989). *See also* Va. Att'y Gen. Op. No. 02-114 (Dec. 12, 2002) ("In considering the application of the BPOL tax to businesses outside the Commonwealth, assessments should be fairly apportioned, which initially requires that the assessment be both internally and externally consistent.").

15 *Goldberg v. Sweet*, 488 U.S. 252, 261 (1989).

16 *Id.* at 262.

17 *Okla. Tax Comm'n v. Jefferson Lines*, 514 U.S. 175, 185 (1995).

18 *Goldberg*, 488 U.S. at 262.

> A State may not "tax value earned outside [of] its borders," Container Corp. of Am. v. Franchise Tax Bd., 463 U.S. 159, 164, 103 S.Ct. 2933, 77 L.Ed.2d 545 (1983), and is limited to taxing "only its fair share of an interstate transaction." Goldberg v. Sweet, 488 U.S. 252, 261, 109 S.Ct. 582, 102 L.Ed.2d 607 (1989).[19]

In *Goldberg v. Sweet*,[20] the Supreme Court of the United States analyzed whether an Illinois tax on interstate telecommunications violated the Commerce Clause, including external consistency. In particular, the gross charge for interstate telecommunications was subject to the tax only if the telecommunications: (1) originated or terminated in Illinois; and (2) were charged to an Illinois service address, regardless of where the telephone call is billed or paid. The tax allowed a credit to taxpayers who proved that they had paid a tax in another state on the same telephone call that triggered the Illinois tax. The Court recognized that "some interstate telephone calls could be subject to multiple taxation" in the event that "the service address and billing location of a taxpayer are in different States."[21] However, the Court declined to find that this multiple taxation risk was sufficient to invalidate the tax because:

> To the extent that other States' telecommunications taxes pose a risk of multiple taxation, the credit provision contained in the Tax Act operates to avoid actual multiple taxation.[22]

As explained below, the BPOL Tax violates the external consistency test because, in the absence of an Out-of-State Deduction applicable to other states' gross receipts taxes, the BPOL Tax reaches beyond the portion of value that is fairly attributable to economic activity within Virginia.

III. Virginia Courts Have Recognized the Constitutional Infirmities Associated with the BPOL Tax

The BPOL Tax has been challenged in two relevant Virginia Supreme Court cases: (1) *Short Brothers (USA), Inc. v. Arlington County*;[23] and (2) *City of Winchester v. American Woodmark Corp.*[24]

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19 *Corporate Exec. Bd. Co. v. Va. Dep't of Tax'n*, 297 Va. 57, 71 (2019).

20 *Goldberg v. Sweet*, 488 U.S. 252 (1989).

21 488 U.S. at 264.

22 *Id.*

23 *Short Bros. (USA), Inc. v. Arlington Cnty.*, 244 Va. 520 (1992).

24 *City of Winchester v. American Woodmark Corp.*, 252 Va. 98 (1996). *See also In re Vecco Construction Industries, Inc.*, 33 B.R. 343 (1983) (Bankruptcy Court holding that the BPOL Tax violated the Commerce Clause because, as "the debtor has paid taxes to Maryland and the District of Columbia based upon revenues generated by the work performed there, the imposition of a local tax upon total gross

First, in 1992, in *Short Brothers (USA), Inc. v. Arlington County*, the Supreme Court of Virginia held the Arlington County BPOL Tax did not violate the fair apportionment prong of the *Complete Auto* test when the taxpayer could not prove it was subject to tax in any other jurisdiction. In that case, the taxpayer at issue was engaged in the business of demonstrating, selling, leasing, and providing support services for commuter aircraft designed and manufactured by an affiliate. The taxpayer's corporate headquarters was located in Arlington County, but the company conducted its activities throughout the country. The taxpayer argued in part that the BPOL Tax was unconstitutional because it was "not fairly apportioned."[25] The court observed that the *Complete Auto* test's fair apportionment prong "addresses a principal concern inherent in taxation of interstate activity – the risk of multiple taxation."[26] However, in this case, the taxpayer did not demonstrate that it had nexus with any other states. Because:

> [T]he tax is based on revenues attributed solely to the taxing jurisdiction and the taxpayer is not subject to taxation based upon those revenues elsewhere, there is no risk of double or multiple taxation and no need, or basis, for apportioning the tax.[27]

Thus, the taxpayer could not show that the BPOL Tax violated the Commerce Clause because there was no "evidence that any other taxing jurisdiction could subject [the taxpayer] to **any type of tax based on its gross receipts**. … Simply put, the evidence does not show that [the taxpayer] is under an actual or potential risk of multiple taxation based on the gross receipts at issue here."[28] The court thus considered not whether there was an external consistency violation based on whether the taxpayer was subject to another state's income tax, but instead whether it was subject to any other state tax based on its gross receipts.

Second, in 1996, in *City of Winchester v. American Woodmark Corporation*, the Supreme Court of Virginia affirmed a circuit court decision and held that "under the specific facts of [the] case, the City [of Winchester] failed to apportion the BPOL Tax assessments as required by the Commerce Clause."[29] In particular, the court held that the tax violated external consistency.[30]

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receipts, wherever earned, has the practical effect of burdening the debtor with cumulative taxation on its Maryland and District of Columbia earnings").

25 *Short Bros. (USA), Inc. v. Arlington Cnty.*, 244 Va. 520, 525 (1992).

26 *Id.*

27 *Id.*

28 *Id.* at 526 (emphasis added).

29 *City of Winchester v. American Woodmark Corp.*, 252 Va. 98, 104 (1996).

30 The circuit court had previously held that the assessments satisfied the internal consistency test because "if every taxing jurisdiction applied the tax as set out in the City's ordinance the taxpayer would be allowed to deduct amounts paid to other taxing jurisdictions and therefore would not be subject to multiple taxation." The internal consistency holding was not challenged on appeal.

The taxpayer maintained a corporate headquarters in the City of Winchester, Virginia and operated a number of manufacturing, storage, and distribution facilities throughout the United States, although none of those facilities were located in Winchester.[31] The taxpayer contested BPOL Tax assessments on the basis that they were not fairly apportioned under the Commerce Clause.[32] The circuit court concluded in 1995 that the tax violated the external consistency test because it was "wholly unapportioned and completely ignore[d] the out of state components of [the taxpayer's] business."[33]

On appeal, the Virginia Supreme Court considered whether the application of the BPOL Tax to the taxpayer violated external consistency.[34] Winchester argued that the record showed that the taxpayer is a "highly centralized, unitary business and its corporate headquarters contributes value to its business."[35] Winchester further argued that all of the taxpayer's "gross receipts are in some way attributable to the headquarters office and presumably could all be used as the basis for the assessment."[36]

The court noted that in this circumstance, where a city based its assessments on 100% of a taxpayer's revenues, the taxpayer was not required to produce evidence of a specific level of value attributable to its Winchester operation to succeed on its claim that the assessments were not externally consistent.[37] Instead, the taxpayer presented uncontested evidence that it operated 24 facilities in 13 different states and that common sense compelled "the conclusion that these operations added value to the taxpayer's business product and were revenue producing activities."[38] Thus, the court concluded, "[b]y definition, assessments based on 100% of [the taxpayer's] revenues included revenues realized from value produced in locations other than in [Winchester]."[39] Therefore, the court held that the taxpayer met its burden that the assessments attributed to operations conducted in Winchester were out of all appropriate proportions to and had no rational relationship to the business transacted in Winchester.[40] The court noted that in comparison with *Short Brothers*, the "only difference" between the cases was that the taxpayer here's "stipulated facts showed a 'legitimate basis

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31 *City of Winchester v. Am. Woodmark Corp.*, 252 Va. 98, 100 (1996).
32 *Id.*
33 *Am. Woodmark Corp. v. City of Winchester*, No. 94-101, 1995 WL 1055862 (Va. Cir. Ct. May 12, 1995).
34 *Id.* at 102.
35 *Id.* at 103.
36 *Id.*
37 *Id.*
38 *Id.*
39 *Id.*
40 *Id.*

on which to allocate [American Woodmark's] gross receipts to another taxing jurisdiction.'"[41]

IV. The Virginia General Assembly Intended for the Out-of-State Deduction to Address the BPOL Tax's Constitutional Infirmities

Prior to the 1996 enactment of the BPOL Tax uniform ordinance statute, Virginia only allowed a credit on the payment of other local license taxes. As part of the bill enacting the BPOL Tax uniform ordinance statute, the Virginia General Assembly also amended Va. Code Ann. § 58.1-3732 to allow a deduction for "receipts attributable to business conducted in another state … in which the taxpayer is liable for an income or other tax based upon income." This deduction relates to one of the act's purposes: preventing the "double taxation of receipts."[42]

Similarly, responding to the recent *Short Brothers* and *American Woodmark* decisions, the Virginia Attorney General issued an opinion that associated the Out-of-State Deduction with the Commerce Clause's limitations on state taxation and such cases.[43] Also, during the pendency of *American Woodmark*, the City of Winchester had offered to address the taxpayer's Commerce Clause arguments by "credit[ing] against their tax on nationwide receipts any taxes paid for the same 'type' of license in other jurisdictions."[44]

The General Assembly's goal was for the Out-of-State Deduction to eliminate double taxation. It is thus reasonable for the General Assembly to have intended to provide a deduction for all out-of-state receipts subject to other states' taxes, especially those taxes of the same "type" as the BPOL Tax (i.e., a gross receipts tax). In support, the legislature was presumed to be aware[45] of a 1975 Virginia Supreme Court case that broadly interpreted the term "income tax" – *City of Portsmouth v. Fred C. Gardner Co.*[46] In *City of Portsmouth v. Fred C. Gardner Co.*, the Supreme Court of Virginia addressed the definition of "income tax" for purposes of the Buck Act.[47] The Buck Act states that a person is not "relieved from liability for any income tax levied by any State … by reason of his residing within a Federal

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41 *Id.* at 104.

42 Summary, H.B. 293 BPOL Tax Uniform Ordinance (Va. 1996), *available at* LIS: Virginia's Legislative Information System.

43 *See* Va. Att'y Gen. Op. (Dec. 1, 1997).

44 *American Woodmark Corp. v. City of Winchester*, No. 94-101, 1995 WL 1055862, at *12 (Va. Cir. Ct., City of Winchester May 12, 1995).

45 *See Jones v. Phillips*, 299 Va. 285, 301 (2020) ("The legislative-acquiescence doctrine presumes that unless a newly enacted statute suggests otherwise, the legislature intends the statute to be interpreted consistent with prior binding precedent addressing the point being codified.").

46 Notably, this case was cited by *In re Vecco Construction Industries, Inc.*, a Virginia Bankruptcy Court case that held that Fairfax County's BPOL Tax violated the Commerce Clause. *In re Vecco Construction Indus., Inc.*, 33 B.R. 343 (E.D. Va. Bankr. Ct. 1983)

47 *City of Portsmouth v. Fred C. Gardner Co.*, 215 Va. 491 (1975).

area or receiving income from transactions occurring or services performed in such area."[48] The Buck Act defines "income tax" as "any tax levied on, with respect to, or measured by, net income, gross income, or gross receipts."[49] The Virginia Supreme Court stated:

> The Buck Act "income tax," broadly defined as it is, refers to the broad generic class of taxes based upon income. It does not require that the tax be denominated an income tax or that it conform to the federal income tax. If the tax in question is based upon income and is measured by that income in money or money's worth, as a net income tax, gross income tax, or gross receipts tax, it is an income tax. Humble Oil & Refining Co. v. Calvert,478 S.W.2d 926, 930 (Tex.1972).[50]

Such a reading would satisfy the General Assembly's goal for the Out-of-State Deduction. Applying the Out-of-State Deduction to states' gross receipts taxes imposed in lieu of corporate income taxation will remedy the BPOL Tax's external consistency infirmities.[51]

V. A Statutory Change is Required to Avoid a Violation of the Commerce Clause

If not remedied, the BPOL Tax taxes the same receipts that are taxed in other states. Such double taxation runs afoul of the external consistency test described under *Complete Auto Transit* in the same way that the City of Winchester failed it in *American Woodmark*. The Out-of-State Deduction is designed to avoid such double taxation issues by providing a deduction for certain taxes paid in other states. But it does not avoid double taxation by the states that impose gross receipts taxes in lieu of income taxes (e.g., Ohio, Texas, Washington).

The Virginia Attorney General has agreed that the Out-of-State Deduction – to comply with the Commerce Clause's external consistency requirement – "should be applied to businesses outside the Commonwealth so that the assessments are fairly apportioned between the activity in your jurisdiction and the activity outside the Commonwealth."[52]

The importance of a statutory change is to avoid the double taxation of out-of-state receipts, regardless of whether the other state's legislature has chosen to impose a gross receipts tax or a traditional income tax. The importance of this change and the constitutional violation if the change is not made is illustrated by the following fact patterns.

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48 4 U.S.C. § 106(a).

49 4 U.S.C. § 110(c).

50 *City of Portsmouth v. Fred C. Gardner Co.*, 215 Va. 491, 494 (1975) (emphasis added).

51 *See also* Va. Att'y Gen. Op. No. 11-029 (Feb. 24, 2012) (stating that the Virginia Beach BPOL Tax is an "income tax" for purposes of the Buck Act).

52 Va. Att'y Gen. Op. No. 02-114 (Dec. 12, 2002).

For example, consider Company A, which is headquartered in Virginia and has manufacturing and sales offices in Ohio. Company A pays the BPOL Tax and the Ohio Commercial Activity Tax but, under the Department's view, is unable to take the Out-of-State Deduction because the Ohio Commercial Activity Tax is based on gross receipts, rather than net income. In contrast, consider Company B, which is the exact same type of company as Company A but instead has manufacturing and sales offices in Georgia. Company B would be both a BPOL Tax and Georgia corporate income tax taxpayer but may claim the Out-of-State Deduction on its gross receipts generating its Georgia corporate income tax liability.

Under this example, Company A has a higher BPOL Tax burden because it pays an Ohio tax – rather than Georgia tax – on its gross receipts, despite having the same economic activity in Virginia. Company A could contend that the application of the BPOL Tax to them without the corresponding Out-of-State Deduction violates the external consistency test. There is no economic justification for Virginia to tax more of Company A's income simply because it has manufacturing and sales offices in a state that levies a gross receipts-based tax instead of traditional corporate income tax. By taxing Company A more than Company B, the practical or economic effect of the tax is to tax more activity than Virginia is entitled to under the Commerce Clause. The proper solution is to equally apply the Out-of-State Deduction to Company A and Company B so they are not treated differently.

The withholding of the Out-of-State Deduction from Company A, solely because the Ohio Commercial Activity Tax is one based on gross receipts, would result in Company A having the BPOL Tax being assessed on 100% of its revenues, even though a portion of that revenue is from value produced in a location other than in Virginia. Based on the Virginia Supreme Court's decision in *American Woodmark*, such an assessment would violate the external consistency test. Thus, the Out-of-State Deduction should be applied to both traditional net income taxes and gross receipts taxes, something that is contemplated by the statute when it states that the deduction is available for "other tax[es] based upon income[.]"

VI. The Localities' Concerns Are Not Valid and Can be Addressed

The request to expand the Out-of-State Deduction to apply to gross receipts taxes imposed in lieu of corporate income taxes does not run afoul of the localities' two primary concerns: (1) revenue loss; and (2) compliance.

First, revenue loss should not impact whether the legislature expressly expands the scope of the Out-of-State Deduction. Applying the deduction to certain gross receipts taxes is necessary to comply with the strictures of the U.S. Constitution. As such, remedying the BPOL Tax's external consistency issue is mandatory and any estimated revenue impact is not relevant.

Second, localities should not have significant issues with applying the Out-of-State Deduction against additional taxes. The Out-of-State Deduction has existed for nearly three decades. Localities have had plenty of experience applying – and auditing – the deduction. For example, localities have been able to successfully administer the Out-of-State Deduction

when applying it to an Ohio tax "based on net worth."[53] Further, the localities have indicated that they can comply with the expanded Out-of-State Deduction, as they have been able to attribute a revenue loss to it.

Sincerely,

Michele Borens

Michele Borens
EVERSHEDS SUTHERLAND (US) LLP

53 Va. Admin. Code tit. 23, § 10-500-80(B)(2).

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VIA ELECTRONIC MAIL

July 8, 2025

Mr. Vivek Bakshi
Senior Tax Law Analyst, Tax Legislation Division
Virginia Department of Taxation
1957 Westmoreland Street
Richmond, VA 23230

Dear Mr. Bakshi:

Thank you for the opportunity to submit public comments as part of the workgroup convened to discuss HB 1743. We appreciate your work and the efforts of your colleagues at the Department of Taxation to allow for further discussion of this complex issue. VACo had advocated during the 2025 General Assembly session for an opportunity to further explore this concept, and we are grateful to Delegate Watts and to all the participants in the workgroup for the conversation at our meeting in June. As we have further investigated the issue of expanding the deduction for out of state receipts from BPOL taxation, we offer the following comments, which are in alignment with our partners at the Virginia Municipal League and the Commissioners of the Revenue Association of Virginia.

Local revenue impact: As discussed at our June meeting, expanding this deduction to cover other types of taxes will have a local revenue impact. It was difficult to quantify this impact during the 2025 session, and it remains challenging to predict revenue losses, as a locality likely will not know that a local business is also operating in another state until the business claims the deduction. Arlington County staff developed a preliminary estimate based on analysis of four companies using payroll apportionment to pay taxes; this estimate indicated that the expanded deduction would result in an annual loss of $4.2 million to the County. Extrapolating this calculation to the rest of the state results in an estimated $60 million in lost revenue to localities annually – likely a conservative estimate, which understates the true impact.

The proposed expansion of the deduction introduces additional volatility into local government revenue predictions as well, as it would encompass new types of taxes, which may use different tax bases and sourcing rules. The Department's introductory presentation to the workgroup summarized this concern well: "Corporate apportionment methodologies amongst various states are not always consistent. Localities strive for consistency and predictability in their tax bases and expanding the deduction to include different and evolving types of taxes would not only lessen the tax base but would make year-over-year assumptions difficult for localities."

As you know, county governments, as well as the state, are operating in an environment of substantial economic uncertainty. Given the challenges surrounding federal actions to reduce the federal workforce and their potential impacts on state and local revenues, as well as federal actions to shift costs to states and localities or eliminate federal support for programs, localities are ill-positioned to absorb additional revenue shocks.

Administrative complexity: As documented in the 1995 *Report of the Joint Subcommittee Studying the Business, Professional, and Occupational License Tax*, when the existing deduction was established, localities were not in favor of this policy change, and the report notes that the creation of this deduction imported income tax concepts into a gross receipts tax system that is fundamentally based on the location of business activity. However, income taxes are recognizable in other states, and the administration of the existing deduction is relatively well-established. Expanding the deduction to allow other types of taxes that are not based on income to qualify will require tax officials to be experts in the tax structures of all 50 states, and potentially of other countries as well, so that determinations can be made as to whether other types of taxes qualify for the deduction.

In addition, we are concerned that expanding the deduction to other types of taxes may have unintended consequences; although we understand that the intention is to expand the deduction to cover gross receipts taxes imposed at the state level in lieu of a state corporate income tax, the proposed expansion could open the door to arguments that deductions should also be allowed for local gross receipts taxes that are imposed in addition to a state corporate income tax, or state gross receipts taxes that may be imposed in addition to other state income taxes.

Fairness: The nuances of other states' tax systems raise questions of fairness, as states have varying rules for filing and payment of gross receipts taxes. For example, Ohio's Commercial Activity Tax threshold was recently increased to $6 million in taxable gross receipts, beginning in tax year 2025. If a deduction were allowed in Virginia for gross receipts attributable to business activity in Ohio, we question whether a firm could deduct gross receipts from a local BPOL tax that were never taxed in Ohio.

It should also be noted that small businesses that operate only within one jurisdiction in Virginia would receive no benefit from the expanded deduction. We also would point out that BPOL is a tax on the privilege of conducting business within a locality in Virginia; it funds services provided by the locality to residents, including services that benefit businesses within the locality. A firm with a definite place of business within a locality that imposes a BPOL tax should be expected to contribute to those services, even if it also derives revenues from business conducted in other states.

Constitutionality: We do not share the views presented to the workgroup regarding the constitutionality of the current structure of BPOL as it relates to interstate commerce. As the Commissioners of the Revenue outline in their comments, BPOL as currently constructed meets the four-prong test outlined in *Complete Auto Transit, Inc. v. Brady.*

In light of the expected impact on local revenues and other concerns articulated above, we encourage the state not to pursue further expansion of the BPOL deduction.

We appreciate your consideration of our perspective, and we thank you again for your work to convene the workgroup and facilitate the discussion.

Sincerely,

Dean A. Lynch, CAE
Executive Director

cc: Members, Virginia Association of Counties Board of Directors

BETTER COMMUNITIES THROUGH SOUND GOVERNMENT

Tuesday, July 8, 2025

Vivek Bakshi
Senior Tax Law Analyst/Tax Legislation Division
Virginia Department of Taxation
600 E. Main Street, Suite 1100
Richmond, VA 23219

Dear Mr. Bakshi,

The staff and members of the Virginia Municipal League (VML) want to thank the Department of Taxation for convening the first meeting of the work group in June that is reviewing BPOL and local license tax deductions for out-of-state businesses. The history of BPOL that was presented by staff from the department was especially helpful to provide context for proposed changes to the program.

It was also informative to hear from the parties interested in BPOL and the deduction for out-of-state receipts to understand the current issue and proposed policy changes. Even though we had preliminary conversations during the 2025 Session about this policy issue, a fuller discussion of BPOL, including its complexity and the estimated cost of any changes, is better suited to this interim review.

VML has worked closely with the Commissioners of the Revenue and the Virginia Association of Counties on this policy issue and has mutual concerns regarding proposed changes, specifically related to:

1) The fiscal impact;
2) Fairness;
3) Increased administrative burden; and
4) Constitutionality;

As it relates to the changes, VML understands and appreciates what Del. Watts and the business community are attempting to accomplish with BPOL and out-of-state deductions, especially in states that are being creative in their taxation of businesses. However, the additional administrative cost of implementing such modifications at the local level, and more importantly, the lack of clarity this creates for local BPOL revenues gives us grave concerns. That concern has only grown in recent months as the federal government reduces its workforce, pares back federal grants to state and local governments, and shifts costs previously borne by the federal government to states and localities. Further, both gubernatorial candidates have suggested eliminating or phasing out the car tax, putting at risk the second largest revenue source for local governments.

To date, the combined cost of these federal changes on state and local revenues remains unknown. In an environment where the economic and fiscal outlook at the state and local

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BETTER COMMUNITIES THROUGH SOUND GOVERNMENT

level is not clear, VML cannot support any changes to the current policy regarding out-of-state deductions under BPOL absent certainty about the potential negative impact on local revenues and a firm commitment of ongoing general fund resources to offset any local revenue losses.

Thank you for the opportunity to submit our comments and concerns on this important fiscal issue for local governments. We look forward to additional conversations about BPOL and the out-of-state deductions should it be deemed appropriate.

Respectfully submitted,

Joe Flores
Director of Fiscal Policy
Virginia Municipal League

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APPENDIX E: Official Comments to the Draft Report

VIRGINIA CHAMBER

THE VOICE of BUSINESS

September 12, 2025

Mr. James Alex
Commissioner, Virginia Department of Taxation
1957 Westmoreland Street
Richmond, VA 23230

Dear Commissioner Alex,

The Virginia Chamber of Commerce is writing in response to the draft report issued by the 2025 Workgroup to Review the BPOL Out-of-State Deduction ("Workgroup").

The draft report indicates that the Workgroup was unable to reach consensus on whether: (1) it is necessary to expand the out-of-state deduction to address constitutional concerns; or (2) there would be other benefits to expanding the out-of-state deduction. The Workgroup also noted other areas of disagreement, including whether expanding the deduction would reduce or increase the administrative burden on taxpayers and whether the impact of on localities is a concern in expanding the deduction.

We urge the Workgroup to revise its draft report to recommend that the out-of-state deduction must be legislatively or administratively revised to address its serious constitutional infirmities. Remedying the BPOL Tax's constitutional infirmities must override any concerns that the localities may lose revenue or that a legislative change will be difficult to administer. If the legislature fails (or the Department of Taxation does not change its policy) to fix the BPOL Tax's externally inconsistent out-of-state deduction itself, there is no doubt that the out-of-state deduction will definitely be challenged in court. Any remedy designed by the court may vary from one designed by the legislature directly.

I. Irrespective of Other Concerns, the BPOL Tax's Constitutional Infirmities Must Be Remedied

The draft report recognizes that the out-of-state deduction is subject to concerns about whether it is satisfies the "fair apportionment" prong of the U.S. Supreme Court's *Complete Auto Transit* test. Despite these concerns, the draft report does not make a recommendation to fix this problem. The Virginia Supreme Court has already addressed the BPOL Tax's constitutional issues and there is no doubt that they will reach a similar finding if the BPOL out-of-state deduction is not fixed.

In *City of Winchester v. American Woodmark Corp*[1] the Virginia Supreme Court held that Winchester's assessment on 100% of American Woodmark's revenues violated the external consistency test. American Woodmark presented uncontested evidence that it operated 24 facilities in 13 different states that contributed to the value of its business. Thus, "[b]y definition, assessments based on 100% of American Woodmark's revenues

[1] *City of Winchester v. Am. Woodmark Corp.*, 252 Va. 98 (1996).

included revenues realized from value produced in locations other than in the taxing jurisdiction."[2]

If a court were to decide that the out-of-state deduction violates external consistency, it may not merely expand the deduction to account for out-of-state gross receipts taxes, but instead incorporate other out-of-state tax types, as well. The Department of Taxation ("Department") has the opportunity to recommend a change to the out-of-state deduction that is reasonable for both taxpayers and localities.

While the localities' have raised concerns about potential lost revenue or administration difficulties, any such concerns are overriden by the need to remedy the BPOL Tax's constitutional infirmities. The Department has an obligation to ensure that the BPOL Tax complies with the U.S. Constitution. Expanding the deduction to incorporate out-of-state gross receipts taxes remedies the BPOL Tax's external consistency violation. Put another way, expanding the BPOL out-of-state deduction is simply including receipts that are already protected by the U.S. Constitution's Commerce Clause's bar on externally inconsistent state taxation. For example, under the current deduction, Company A may claim a deduction against an out-of-state gross receipts tax and then be assessed an additional $100 in BPOL tax. Upon a court concluding the assessment violated the U.S. Constitution, Company A would be entitled to a refund of $100 plus interest. If the legislature expands the deduction to comply with federal law in advance, Company A and the city will be in the same position economically, except without the city paying Company A interest and both parties incurring the costs of litigation.

Second, any claims about difficulty in administration if the tax code is modified are not a valid reason to not cure the BPOL tax's serious constitutional infirmities. These constitutional infirmities create uncertainty for businesses, increasing compliance costs and making Virginia a difficult place to do business. Issues with administrability could also be solved in different ways. For example, the Workgroup, after consulting with businesses and localities, could recommend a detailed expanded deduction that would guide the localities in administration. Additionally, the Department of Taxation could also issue guidelines to assist localities with administering the amended deduction. In short, there are ways to address administration of any changes to the BPOL Tax.

II. Other State Courts are Finding that Local Gross Receipts Taxes are Unconstitutional

The Workgroup should also reconsider the draft report's conclusions because, in recent years, other states' courts have consistently ruled against localities in finding that gross receipts taxes violated the U.S. Constitution.

For example, in *Upper Moreland Township v. 7 Eleven, Inc.*, the Commonwealth Court of Pennsylvania held that a locality's business privilege tax ("BPT") assessment

[2] *Id.* at 103.

violated the United States Constitution's Commerce Clause.[3] The Township was attempting to tax 100% of the revenue from the franchise stores within Pennsylvania, along with an apportioned amount of the charges paid by the franchise stores in other states.[4] The Commonwealth Court found that the services provided by 7-Eleven to Pennsylvania franchise stores are produced by activity beyond the state.[5] The court concluded that the assessment was not externally consistent because it was disproportionate; the Township "failed to fairly apportion the [charges] when those charges reflected both intrastate and interstate activities."[6]

More recently, in *City of Atlanta v. Block, Inc. of Delaware*,[7] the Georgia Court of Appeals held that the City of Atlanta could not tax all of Block's receipts earned in Georgia because locations and activities outside the state contributed to this revenue. The court stated that the statute's plain language does not limit the number of offices contributing to Georgia gross revenue to only offices located within the state. The City's position in trying to tax all of Block's Georgia receipts did not avoid unconstitutional double taxation.

These decisions are just two examples of many cases where courts have consistently found that a localities taxation of receipts attributed to other states is unconstitutional. See also, *City of Seattle v. KMS Fin. Servs., Inc.*, 12 Wn. App. 2d 491 (2020); *Avanade, Inc. v. City of Seattle*, 151 Wn. App. 290 (2009); *KMS Fin. Servs., Inc. v. City of Seattle*, 135 Wn. App. 489 (2006); *Northwood Constr. Co. v. Twp. of Upper Moreland*, 579 Pa. 463 (2004); *Phila. Eagles Football Club, Inc. v. City of Philadelphia*, 573 Pa. 189 (2003).

Thus, courts across the country have consistently applied the Commerce Clause's fair apportionment restraint on state taxation to prevent overreaching by localities. In *7-Eleven*, the Pennsylvania Commonwealth Court held that the local business privilege tax was externally inconsistent. In *Block*, the Georgia Court of Appeals interpreted a statute by reading it to avoid unconstitutional double taxation. Any judicial review of the BPOL Tax's out-of-state deduction would also face constitutional scrutiny.

III. Conclusion

The BPOL Tax's constitutional infirmities must take precedence over any other concerns. The urgency of amending the deduction (or the Department changing its policy) to remedy those constitutional infirmities is heightened given the cases in other states that have concluded that the application of local gross receipts taxes, like the BPOL tax, in certain contexts are unconstitutional. If the BPOL tax is litigated under similar circumstances, localities will be left scrambling for solutions after a decision. But the

[3] *Upper Moreland Twp. v. 7 Eleven, Inc.*, 160 A.3d 921, 924 (Pa. Commw. Ct. 2017).
[4] Id. at 925-26.
[5] *Id.* at 926.
[6] *Id.* at 927.
[7] *City of Atlanta v. Block, Inc. of Delaware*, 917 S..2d 403 (Ga. Ct. App. 2025).

Workgroup can and should recommend a revised deduction as a way to proactively deal with these constitutional issues.

Regards,

Keith Martin
Interim President and Chief Executive Officer
Virginia Chamber of Commerce

CC: The Honorable Stephen E. Cummings, Secretary of Finance
Jason Powell, Deputy Secretary of Finance
The Honorable Juan Pablo Segura, Secretary of Commerce and Trade
The Honorable John Littel, Chief of Staff

Commissioners of the Revenue Association of Virginia's (CORVA) Comments to the HB 1743 Study Group

September 15, 2025

On Tuesday, June 2, 2025, the Virginia Department of Taxation convened a workgroup to address HB 1743. Each workgroup member/organization was asked to provide commentary. VML, VACO, and CORVA provided a single partnered presentation to the Virginia Department of Taxation and the workgroup members.

On Monday, July 7, 2025, in alignment with our mission and our principles to educate and inform ourselves and our partners, CORVA provided formal written comments to the Virginia Department of Taxation.

On Friday, August 29, 2025, the Virginia Department of Taxation sent out draft report of the workgroup's findings and recommendations that the Department will be submitted to the Joint Subcommittee on Tax Policy and to the Chairs of the Senate Committee on Finance and Appropriations and the House Committees on Finance and Appropriations.

CORVA's representatives have reviewed the draft report and found that it to be a summary of the workgroup's discussion and follow-up comments. Upon review, a few points of clarification have been added to the (2) Fairness Section below in *italics.*

(1) FISCAL IMPACT

The proposed change to the out-of-state deduction will have a significant negative impact on locality revenues in a time of mounting fiscal uncertainty.

As a means to gauge the fiscal impact, Arlington County Commissioner of Revenue computed an initial assessment of this impact. Arlington reviewed recent audits of four companies with significant interstate operations. Assuming that the proposed expansion of the deduction to include those states that impose a gross receipts tax were enacted, an annual loss of $4.2 million of BPOL tax revenue would result *from just these four companies alone*. Extrapolating this estimate proportionally to the rest of the state from Arlington's share of statewide GDP would generate an estimated minimum of **$60 million** in revenue loss for localities across the state annually. The expected revenue loss would almost certainly be significantly larger than this, given the extremely limited nature of the sample examined (*i.e.* four companies). See Exhibit A for more details.

The legislation under consideration did not provide any mechanism for the Commonwealth to replace this lost revenue with state funds. If the General Assembly does enact this provision, it should provide such

funding on an ongoing basis.

This proposed change comes at a particularly difficult moment for localities. Local budgets in Virginia are under pressure to eliminate the car tax, as well as recent federal initiatives that are also likely to reduce local revenues, including reduced employment due to federal worker firings, termination of numerous federal contracts and direct reductions in federal funding to localities. See Exhibit B for more details.

(2) FAIRNESS

If enacted, the benefits of an expanded out-of-state deduction would accrue disproportionately to the benefit of large, multistate or multinational corporations due to the very nature of the deduction. *Brick-and-mortar and other small businesses already pay more BPOL tax than large multinational corporations when measured as a percentage of their gross receipts. Smaller companies with local footprints do not benefit from a deduction for operations in other states and countries.* Small businesses make up 99.5% of Virginia businesses, leaving just 0.5% of businesses in the Commonwealth to benefit most from this costly policy change.

Larger multinational corporations already enjoy significant tax breaks, subsidies, and other advantages.

In addition, while the out-of-state deduction is intended to prevent double taxation, its application in its current form can actually result in non-taxation of certain receipts.

This occurs because the BPOL tax already uses situs-based sourcing rules to allocate gross receipts to the locality where the business activity occurs, effectively preventing multiple jurisdictions from taxing the same revenue. However, the current deduction framework introduces income tax concepts, such as liability to file in another jurisdiction, into a gross receipts tax system that is fundamentally based on the location of business activity. This overlay creates a structural mismatch: receipts that are properly situsted to a Virginia locality may be deducted simply because they appear on an income tax return filed elsewhere, even if they were not actually taxed in that jurisdiction.

As a result, the deduction can override the situs rules and allow businesses to exclude receipts that were never subject to tax anywhere, undermining the fairness and integrity of the BPOL system.

This problem is multiplied if the deduction is expanded.

(3) INCREASED ADMINISTRATIVE BURDEN

Expanding the out-of-state deduction to cover other types of taxes would increase the administrative burden of assessing BPOL taxes for both localities and taxpayers.

a. Burden on Taxpayers

The current BPOL deduction framework is aligned with standardized principles used in income tax reporting. Introducing gross receipts taxes, which lack such uniform definitions and filing standards, would disrupt this consistency. Taxpayers may be required to compile and submit additional data—such as revenue by jurisdiction, customer location, and work performance details—to substantiate their deduction claims. This adds complexity and increases compliance costs for taxpayers.

b. Burden on Localities

Many taxpayers currently base their out-of-state deduction on apportionment data used for state income tax filings. However, gross receipts taxes often use different tax bases and sourcing rules. As a result, taxpayers could claim deductions that exceed their actual gross receipts, especially when combining data from multiple tax types. This discrepancy would increase the risk of over-deduction and require localities to conduct more frequent and detailed audits to verify claims.

Allowing deductions for non-income-based taxes would require local tax assessors to understand and evaluate new tax structures across all 50 states (including potentially their localities) and, for multinational taxpayers, foreign jurisdictions. This would place a significant burden on local governments and the Virginia Department of Taxation, which would need to allocate additional resources to research, training, and enforcement. The complexity and uncertainty also raises the likelihood of disputes and litigation. Most local audit programs are based on compliance of local taxes, not financial audits which are very detailed and time and resource consuming.

The proposed legislation does not clarify how to prioritize or interpret deductions when a state imposes both income and gross receipts taxes, but the taxpayer is only subject to one. It also opens the door to arguments for deductions based on local gross receipts taxes, sales taxes, or other non-income-based levies, depending on the wording of the legislation. Additionally, the term "liable to file," which has been clarified in prior rulings for income tax purposes, may not translate cleanly to gross receipts taxes, which have different nexus thresholds, rates, and filing requirements.

(4) CONSTITUTIONALITY

The legal arguments made by corporate special interest group members of the study group about the constitutionality of the existing BPOL tax structure to the Department of Taxation are without merit. The proposed expansion of the out-of-state deduction is not necessary to ensure compliance with the Commerce Clause. The Virginia Supreme Court, the Tax Commissioner and the Attorney General have each issued rulings confirming that the BPOL tax as currently enacted complies with the Commerce Clause.

A state tax violates the Commerce Clause if it (1) applies to an activity lacking a substantial nexus to the taxing state; (2) is not fairly apportioned; (3) discriminates against interstate commerce; or (4) is not fairly related to the services provided by the state. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977).

The BPOL tax applies to businesses that have a place of business in the state and so meets the substantial nexus test.

A tax is fairly apportioned if it is both internally and externally consistent. A tax is internally consistent if, assuming that every other jurisdiction applied the same statute, the taxpayer would not be subjected to a risk of double taxation. An assessment is externally consistent if the assessment applies only to the portion of revenues from interstate activity which reasonably reflects the in-state component of the activity being taxed.

The BPOL tax is internally consistent because if it were applied by every other state, there would be no risk of double taxation because each state would apportion to itself and tax only those gross receipts earned at a definite place of business within that state. The BPOL tax is also externally consistent because its situs rules ensure that the tax applies only to the portion of the revenues from interstate activity which reasonably

reflects the in-state component of the activity being taxed. Revenues earned by businesses for work performed at an out-of-state location are sitused to that state for taxation in proportion to the amount of work performed there.

The BPOL tax does not discriminate against interstate commerce because gross receipts from domestic, interstate and international activities are treated exactly the same.

The BPOL tax is fairly related to the services provided by localities because it funds services (such as roads, police, firefighting, etc.) provided by the locality to residents, including businesses with a definite place of business in the county subject to the BPOL tax.

(5) SUMMARY & RECOMMENDATIONS

Due to the current economic climate, fiscal impact, unfairness, and increased administrative burden, CORVA recommends that the BPOL statute not be amended to expand the out-of-state deduction. CORVA is amenable to working with the Virginia Department of Taxation to revisit and refresh the 2000 BPOL Guidelines to promote uniformity of interpretation.

Exhibit A

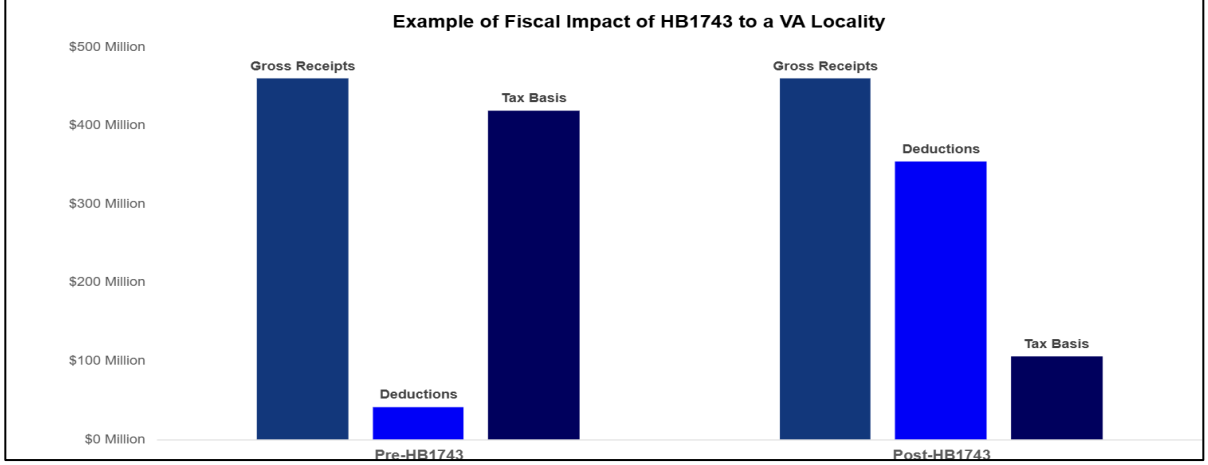
Sample Business: Potential Impact on Tax Basis

		Current			HB1743		
Situs based on Payroll Apportionment	Payroll Apportionment	Deductible (based on filing state income tax return)	Taxable Gross Receipts based on Payroll Apportionment	Deduction Amount	Deductible (based on expansion to include gross receipts like tax)	Taxable Gross Receipts based on Payroll Apportionment	Deduction Amount
VA	23%	Y	$460,000,000		Y	$460,000,000	
PA	6%	Y		$27,600,000	Y		$27,600,000
MD	3%	Y		$13,800,000	Y		$13,800,000
WA	68%	N		$0	Y		$312,800,000
Total Deduction				$41,400,000			$354,200,000
BPOL Tax Basis				$418,600,000			$105,800,000
Tax Revenue				**$1,465,100**			$370,300

Classification: Section 58 - Personal Services
Arlington County Tax Rate: 0.0035
Definite Places of Business: VA, PA, MD, WA
Total Gross Receipts: $2,000,000,000

Revenue Loss of 75% ($1,094,800)

Sample Business: Potential Impact on Tax Basis



Potential Fiscal Impact - Statewide

Based on FY25 data for ***only 4**** Arlington-based companies that use payroll apportionment & assuming Arlington share of Virginia GDP applies to the State...

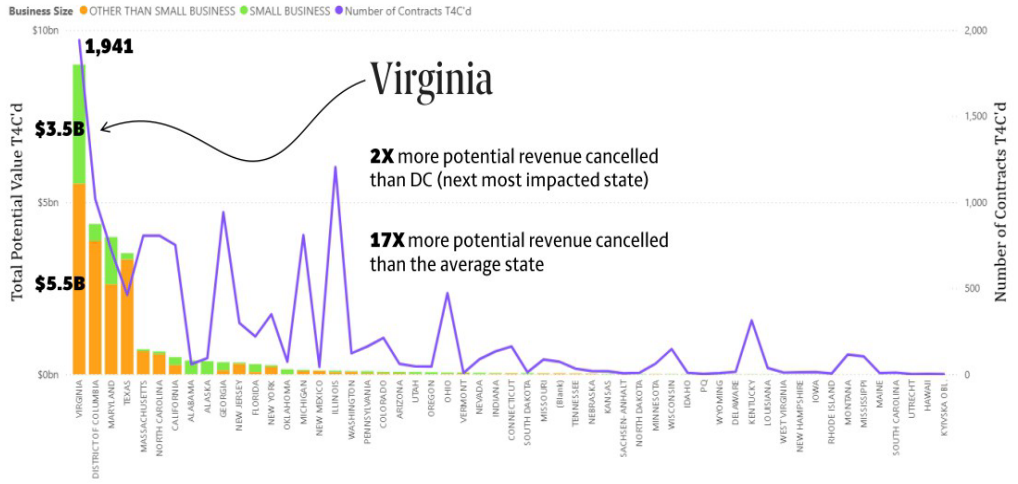
Arlington VA GDP	$41,000,000,000
VA State GDP	$597,000,000,000
Share of Arlington of VA GDP	7%
Partial Estimate of HB1743 Impact on Arlington, VA*	$4,200,000
Projected Calculation of HB1743 state-wide impact	**$60,000,000**

Revenues Across Virginia May Decrease Annually By More Than $60 Million

Exhibit B

ForsMarsh

Contract Awards* Terminated by State



Company Location (State)

*Contract awards include funded delivery/task orders on contract vehicles (BPAs and IDIQs) and standalone contracts. This is the most accurate account of potential revenue loss.

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Patrick J. Reynolds
President & Executive Director
(202) 484-5218
preynolds@cost.org

September 15, 2025

VIA EMAIL TO:

Vivek Bakshi
Virginia Department of Taxation
Legislative Work Group to Study BPOL Out-of-State Deduction

Re: COST Comments to the Virginia BPOL Workgroup

Dear Members of the Virginia BPOL Workgroup:

On behalf of the Council On State Taxation (COST), I want to express our disappointment and frustration that the draft report to the legislature makes no legislative recommendations, ostensibly because the work group did not achieve consensus. We believe avoiding recommendations shirks the responsibilities entrusted to the work group by the General Assembly. We instead encourage the work group to recommend, consistent with earlier guidance from the Department of Taxation, that the legislature clarify that "income or other tax based on income" as used in the statute[1] includes not just "net income tax" but also "gross income tax."

The tax policy and legal analyses supporting our suggested recommendation were thoroughly discussed during the meeting and were overwhelmingly uncontroverted.[2] The *only* purported policy position advanced for maintaining the recent inconsistent guidance[3] is local governments' desire for additional revenue.

We further disagree with the assertion in the report that the clarification we request is in any way an "expansion" of the deduction. It is simply a clarification consistent with: 1) the original intent and plain meaning of the statute; 2) earlier guidance from the Department of Taxation; 3) recent guidance regarding the BPOL and federal law; and 4) U.S. Constitution limitations. This clarification would achieve the consistency, clarity, and fairness the draft report recognizes is vital to the administration of the BPOL tax.

Sincerely,

Patrick J. Reynolds
President & Executive Director

CC: COST Board of Directors

[1] Virginia Code § 58.1-3732(b)(2) (https://law.lis.virginia.gov/vacode/title58.1/chapter37/section58.1-3732/#:~:text=A.,the%20ordinary%20course%20of%20business.)
[2] The argument by the Commissioners of the Revenue Association in its letter is clearly unsupportable. See Michele Borens (Eversheds Sutherland) letter included with the draft report.
[3] Tax Commissioner Ruling 22-117, July 21, 2022 (https://www.tax.virginia.gov/laws-rules-decisions/rulings-tax-commissioner/22-117)

APPENDIX F: House Document 59 (1995)

REPORT OF THE
JOINT SUBCOMMITTEE STUDYING

THE BUSINESS, PROFESSIONAL, AND OCCUPATION LICENSE TAX

TO THE GOVERNOR AND
THE GENERAL ASSEMBLY OF VIRGINIA

HOUSE DOCUMENT NO. 59

COMMONWEALTH OF VIRGINIA
RICHMOND
1995

MEMBERSHIP OF THE SUBCOMMITTEE

Delegate David G. Brickley, **Chairman**
Senator E.M. Holland, **Vice Chairman**
Delegate Linda T. Puller
Delegate Harry R. Purkey
Delegate James M. Scott
Delegate Mitchell Van Yahres
Senator Robert L. Calhoun
Senator Charles J. Colgan
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Helena L. Dodson
John R. Broadway, Jr.
Mark Jinks
George C. Newstrom
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HOUSE OF DELEGATES, OFFICE OF THE CLERK
Barbara H. Hanback, Committee Operations

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REPORT OF THE JOINT SUBCOMMITTEE STUDYING THE BUSINESS, PROFESSIONAL, AND OCCUPATIONAL LICENSE TAX

To
The Governor
and the
General Assembly of Virginia

Richmond, Virginia
March 1995

I. EXECUTIVE SUMMARY

House Joint Resolution 526 (Appendix A), passed by the 1993 General Assembly, established a joint subcommittee to study the business, professional, and occupational license ("BPOL") tax imposed by local jurisdictions and to consider alternative means of taxation. House Joint Resolution 110 (Appendix B), passed by the 1994 General Assembly, continued the study for another year for the purpose of improving the administration of the tax.

In its deliberations during the first year, the subcommittee considered options for restructuring or replacing some or all of such taxes with alternative revenue-neutral business taxes which are fairer, easier to understand and apply, and more efficient to administer. During the second year, the joint subcommittee focused on making the administration of the tax more uniform. To achieve this goal, the subcommittee relied on an advisory committee, consisting of business and local jurisdiction representatives, and the Department of Taxation for assistance in preparing a model BPOL ordinance for use by all localities.

The BPOL tax has been a controversial tax for many years. Some in the business community think the categories of occupations are inappropriate and the tax rates unfair. A majority of those objecting to the tax agree the tax should not be levied on the gross receipts of a business. However, local jurisdictions depend substantially on the BPOL tax revenues and, therefore, will not give them up without some alternative which will provide comparable funds in order to provide required services. An equitable distribution of the financial responsibilities for those local services is of paramount concern to the localities.

In 1993, the subcommittee considered amending the current BPOL tax statute as well as repealing the statute and replacing it with one allowing a different method of taxation. In order to decide, the subcommittee met twice to hear testimony from those representing the business community as well as local jurisdictions. In addition, an advisory committee consisting of business people and local jurisdiction officials was appointed by the chairman of the joint subcommittee. The advisory committee, which also met twice, was to develop alternatives for the joint subcommittee's consideration. Realizing that eliminating the tax was impossible without an alternative revenue producer, the subcommittee focused on the administration of the BPOL tax.

In 1994, the joint subcommittee met twice, with its third and final meeting in early January, 1995. The advisory committee met five times with representatives from the Department of Taxation to develop the model ordinance, which was introduced during the 1995 General Assembly Session as House Bill 2351 (see Appendix C for annotated legislation). A resolution was also introduced which continued the study for an additional year in order to examine once again the possibility of eliminating the BPOL tax entirely (Appendix D).

II. INTRODUCTION

The business, professional and occupational license ("BPOL") tax has been a controversial tax for many years. The fact that the tax is levied on the gross receipts, not profits, of certain businesses forms the most basic and the most widespread criticism against the tax. HJR 526, the resolution adopted by the 1993 General Assembly and establishing the joint subcommittee for this study, specifically recognizes this problem: "WHEREAS, a tax measured by gross receipts bears no necessary relationship to the profitability of the business which may pay the tax nor does such a tax give any consideration to the competitive situation a particular industry may face nor of the economic situation in general."

On the other hand, because local governments have come to rely on the revenues produced by the BPOL tax, its elimination without a replacement is unfeasible. Both the business community and local government agree, however, that a fair, equitable, and predictable tax structure which provides both a stable revenue stream and a fair taxing system is needed.

In 1993, the joint subcommittee consisted of 15 members as follows: Delegates David G. Brickley, Linda T. Puller, Harry R. Purkey, James M. Scott, and Mitchell Van Yahres; Senators E.M. Holland, Robert L. Calhoun, Charles J. Colgan, and Kevin G. Miller; and citizen members Connie Bawcum; Helena L. Dodson; Judith S. Fox; Mark Jinks; George C. Newstrom; and Carl W. Stenberg III. During 1994, Judith S. Fox resigned and was replaced by John R. Broadway, Jr.

In accordance with HJR 526, during its first year the joint subcommittee investigated several options for restructuring or replacing some or all of the BPOL taxes with alternative revenue-neutral business taxes which are fairer, easier to understand and apply, and more efficient to administer. In making its determinations the subcommittee considered the following factors:

(1) What is the purpose of the BPOL tax?
(2) How have the economic conditions changed since the current BPOL tax law was enacted?
(3) Will such changes be better addressed by amending the current law or by repealing it and replacing it with a different method of taxation?
(4) What method of taxation will be fair and equitable to business as well as provide a comparable revenue stream to local government?
(5) How can the administration of the tax be improved?

The subcommittee met twice and heard testimony from representatives of the business community as well as local jurisdictions. In addition, an advisory committee, appointed by the subcommittee chairman and comprised of business people and local jurisdiction representatives, met twice. The advisory committee focused on the administration of the tax in developing recommendations for the subcommittee. Its members included Mr. John L. Knapp, Ms. Betty Long, Mr. R. Michael Amyx, Ms. Ellen Davenport, Mr. James D. Campbell, the

Honorable Robert P. Vaughan, the Honorable Gerald H. Gwaltney, Mr. Ira F. Cohen, William L.S. Rowe, Esquire, Mr. Charles K. Trible, Ms. Sandra D. Bowen, Dr. Edward H. Bersoff, Mr. Michael W. Dawkins, and Mr. Jim DePasquale. Mr. Jaydeep Doshi also joined the advisory committee in 1994.

During 1994, the subcommittee focused on the administration of the tax, wanting to make its application more uniform throughout the Commonwealth. It met three times to consider and review the work of the advisory committee and the Department of Taxation (the "Department"), which had developed a model BPOL ordinance to be used by local governments levying the tax. Both the business community and local government thought that more uniformity would improve the system.

III. BACKGROUND

A. HISTORY

The license tax has existed for quite some time in Virginia. Practically unheard of in the colonial period, it was recognized as a source of revenue at the state level following the War of 1812, when the state government assumed Virginia's quota of the costs of that war. The license tax rates not only increased but were extended to more businesses. In addition, the tax was imposed at a flat rate for the "privilege" of establishing a business in a city or town which had to provide services to those businesses. By 1850, the policy of levying a license tax on practically all well-established businesses and professionals was adopted. In an attempt to provide a more equitable tax structure in the 20th century, the gross receipts basis of taxation was instituted because businesses had very different business volumes and the flat tax rate did not account for such differences. Today, the BPOL tax remains an important source of revenue to localities.

Although an important revenue source, the BPOL tax has been subject to criticism and study for many years, especially during the 1970s. BPOL tax rates were actually frozen at their December 31, 1974, level during the 1975 Session of the General Assembly at the recommendation of the Revenue Resources and Economic Commission, which was conducting a study that resulted in the publication of Fiscal Prospects and Alternatives: 1976. Included in the publication is a detailed analysis of the BPOL tax -- its advantages and disadvantages. The analysis points out the importance of the tax as a source of revenue and also discusses the inequities of the tax structure as it then existed. The tax was based on gross receipts, which had no relation to profitability. Further, different types of business had different levels of profitability relative to their receipts. For example, a grocery store would have a relatively low profit margin but a relatively high volume of gross receipts. However, other types of business have high profit margins with lower gross receipts. Finally, there were some extremely high tax rates for certain types of business in some localities.

The following year, in its 1977 Report to the Governor and General Assembly,[1] the commission focused on one alternative for restructuring the framework of the BPOL tax. The intent was to categorize activities that had displayed similar operating ratios over a recent time period and to set maximum tax rates per gross receipts for those classes reflecting the same relative differences in profitability. The report suggested that the state also could require that in addition to being within the state maximums, each locally set rate for each business category must be relative to the operating ratios for all categories. The report indicated that guidelines developed by the Department of Taxation would provide some assurance to the various categorized businesses that tax rates would reflect their general ability to pay and that no business would be subject to special treatment, because a rate change for one category would be accompanied by similar changes for other categories.

[1]Revenue Resources and Economic Commission, Report to the Governor and the General Assembly on Local Fiscal Issues, A Staff Report (December, 1977).

This 1977 report resulted in a proposal by the commission in its 1978 Report to the Governor and the General Assembly.[2] An excerpt from the 1978 report explains the proposal.

The proposal places ceilings on the local business, professional, occupational license tax as follows:

CATEGORY OF ENTERPRISE	Tax Rate Per $100 Gross Receipts
Contracting	.16
Retail Sales	.20
Finance, real estate, and professional services	.58
Repair, personal and business services, and all other business	.36

No such local license tax shall exceed $30 or the rate per $100.00 of the enterprise's gross receipts as stated above, whichever is greater. Massage parlors, fortune tellers, and carnivals, are allowed as exceptions and no ceilings are placed on these businesses.

NOTE:
The relationship between the ceiling rates reflects the relative differences in operating ratios between broad categories of similar activities, i.e., the gross profit ratios for similar business activities as reported by the Internal Revenue Service in Statistics of Income: Business Income Tax Returns, 1970.

The Department of Taxation will be responsible for drafting regulations enumerating the various types of businesses which fall within the four broad categories. Local governments will have the option of setting varied rates for sub-categories of businesses as long as the rates do not exceed the ceiling rate of the major category.

Any local government which presently has rates higher than the proposed ceilings is frozen at the same amount of dollars it collected in FY 1977-78 until such time as it is able to reduce its rates to the ceiling rates without a loss of revenue. When the locality has adjusted its rates at or below the ceiling, it may once more collect additional revenues as inflation and/or economic growth increases the tax base.

The administrative procedure for a locality that must roll back its BPOL rates is explained by the following example:

a) A locality is frozen at FY 1977-78 BPOL dollars (until such time as its tax rates are within the ceilings). For example, assume $100,000 is collected in FY 1977-78.
b) In FY 1978-79, assume $106,000 is collected.

[2]Revenue Resources and Economic Commission, Report to the Governor and the General Assembly, Senate Doc. No. 16 (1978).

c) The locality must lower the tax rates for the subsequent tax year on one or more of the categories which was above the ceiling rate. The rate (rates) must be lowered so that the total receipts in the next fiscal year can reasonably be expected to be the amount received in FY 1977-78 less the $6,000 in receipts which was over-collected.

The merchants' capital tax is repealed. This tax source yielded $2,806,321 for counties in tax year 1976 (Department of Taxation Annual Report 1976-77, Table 5.6). Some towns also levy this tax, but the total dollars collected is not available. It is perceived that counties now levying a merchants' capital tax would adopt a BPOL tax.

Any county license tax imposed shall not apply within the limits of any town located in such county. This is the present law (§ 58.1-266.1(7), *Code of Virginia*).[3]

Today's BPOL tax provisions, found in §§ 58.1-3700 through 58.1-3735, include many of the recommendations made by the Revenue Resources Commission in its 1978 report. The categories and maximum tax rates are identical to those recommended by the commission.

B. ADMINISTERING THE TAX

In Virginia, the governing body of any locality may levy and provide for the assessment and collection of local license taxes on businesses, trades, occupations, and professions. Whenever a local jurisdiction imposes a BPOL tax, the basis for the tax, whether it is gross receipts or otherwise, will be the same for all individuals engaged in the same business. Some occupations and businesses are exempt from the tax (e.g., some public service corporations, manufacturers who sell merchandise at wholesale at the place of manufacture, and affiliated corporations).[4]

For counties, the license tax imposed does not apply in any town in the county where the town has a similar tax, unless the town's governing body makes provision for the county tax to apply.

Under current law, the situs for BPOL tax purposes is any county, city, or town in which the individual maintains an office or place of business. If such taxable situs is in more than one local jurisdiction, the tax due in any one jurisdiction is based on only the amount of business attributable to that local jurisdiction. The general rule regarding situs under the proposed model ordinance looks to the gross receipts attributed to the exercise of a licensable privilege at a definite place of business within the local jurisdiction.

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[3] Id. at 3-5.
[4] Va. Code § 58.1-3703 B.

In general, the limits on the BPOL tax rates are as follows:

> [N]o local tax imposed ... shall be greater than thirty dollars or the rate set forth below for the class of enterprise listed, whichever is higher:
>
> 1. For contracting, and persons constructing for their own account for sale, sixteen cents per $100 of gross receipts;
> 2. For retail sales, twenty cents per $100 of gross receipts;
> 3. For financial, real estate and professional services, fifty-eight cents per $100 of gross receipts; and
> 4. For repair, personal and business services, and all other businesses and occupations not specifically listed or excepted in this section, thirty-six cents per $100 of gross receipts.[5]

These rates are the same as recommended by the Revenue Resources Commission in its 1978 report.

In the proposed model ordinance, a threshold of $100,000 of gross receipts had to be exceeded before any BPOL tax was due. An annual fee of fifty dollars, however, could be collected from everyone who acquired a business license.

In administering the BPOL tax, localities follow guidelines provided by the Department of Taxation, which define and explain the four categories of business named above. Because each local jurisdiction administers the tax, there are differences in rates as well as which businesses are subject to the tax; the model ordinance could eliminate some of the differences.

C. 1995 LEGISLATION

During the 1995 Session of the General Assembly, several bills addressing the BPOL tax were introduced. House Bill 1719 exempted independent start-up businesses from the BPOL tax for the first three years they were in business. House Bill 2463 repealed the tax effective January 1, 2001. Finally, House Bill 1974 and Senate Bill 895, the Governor's bills, called for a five-year phase-out of the tax so it would be eliminated by the year 2001 and contained hold harmless provisions for the phase-out period for the local jurisdictions which would stop levying the tax. In addition, the bills contained a model ordinance similar to the one adopted by the joint subcommittee.

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[5] Va. *Code* § 58.1-3706.

D. ACTIVITIES OF THE JOINT SUBCOMMITTEE

1. 1993 Activities

The purpose of the study was explained by staff during the joint subcommittee's June 1993 organizational meeting, which was also its first meeting. Staff also discussed the history of the tax, its problems and the issues on which the subcommittee needed to focus. This followed the election of Delegate David G. Brickley as chairman of the subcommittee and Senator Edward M. Holland as vice chairman.

During the second meeting, which was held in August 1993, representatives from the business community and local government voiced their concerns about the BPOL tax and offered suggestions for possible changes.

a. Business Concerns. The recurring theme from the business sector was how inequitable, regressive, and difficult to administer the BPOL tax is. A business subject to the tax in one locality may not be subject to it in a neighboring locality, or the rates for the same business might be different. This can create bookkeeping nightmares for businesses located in more than one locality, particularly smaller businesses.

Moreover, many businesses believe that the definition of gross receipts is much too broad. Some in the business community would like to see the definition refined to include only those receipts generated within the taxing local jurisdiction and only those receipts generated by the classified business.

Determining into which BPOL tax category businesses fall also can be confusing. The guidelines prepared by the Department of Taxation for use by the localities in making this determination have not been updated in several years. A great deal of flexibility is afforded the local jurisdictions, which makes it difficult for businesses to plan with any certainty.

b. Local Government Concerns. Local government representatives emphasized how important the BPOL tax revenues are to the localities that levy the tax. In most of those localities, the tax ranks fourth in producing revenues, exceeded only by real estate, personal property, and local sales taxes. Repealing the tax should not be considered without a replacement tax or an increase in the rates of some other existing tax to generate comparable revenues. Also, the elimination of the BPOL tax by the substitution of another tax raises the issue of who or what group should pay this alternative tax, as one taxpayer's BPOL reduction would become another taxpayer's tax increase.

Local government officials agreed that administration of the tax can be problematic and expensive. While open to the call for improvements to administering the tax, local officials generally did not want to relinquish control completely to the Department of Taxation.

c. Possible Solutions. Suggested solutions to the problems enumerated during the meeting included:

(1) Gradually repeal the BPOL tax over a 10-year period;
(2) Immediately repeal the tax and enact a local business net income tax;
(3) Revise classifications and rates to reflect the current economy;
(4) Transfer administration and audit of BPOL tax to the Virginia Department of Taxation;
(5) Enact short-term exemptions or reduced rates for new businesses;
(6) Designate threshold level of receipts before BPOL tax applies;
(7) Create model ordinance for use by localities;
(8) Create statewide mechanism for protest resolution; and
(9) Change appeal deadlines and procedures.

At the suggestion of one of the speakers, an advisory committee composed of individuals from the business and local government sectors was established to assist the joint subcommittee in developing mutually acceptable solutions for the BPOL tax problems.

The advisory committee for the BPOL tax study met in Richmond in October. The committee had a round table discussion and, while no consensus was reached, the following suggestions regarding possible changes in the BPOL tax and its administration were examined:

(1) Replace the BPOL tax system of four classifications having four different maximum rates with one classification having one rate.

(2) Create a uniform system of classifications to be used statewide along with a model ordinance.

(3) Create an appeals process with the Department of Taxation through which a business owner could object to the classification in which his business has been placed by the locality.

(4) Refine the definition of gross receipts so it is better understood and easier to apply.

(5) Request that the Department of Taxation update the guidelines used by the localities in classifying businesses. The last update was done in 1984.

(6) Grant the Department of Taxation the power to issue regulations and make rulings regarding classifications which would provide more guidance to localities and businesses.

The second meeting of the advisory committee was held in January just one week prior to the beginning of the 1994 General Assembly Session. The discussion centered on developing a model ordinance and uniform system of classification, and refining the definition of gross receipts.

After reviewing many of the major issues involved, the committee directed staff, with the Department of Taxation's assistance, to draft a model ordinance which was then circulated among the advisory committee for comment before going to the joint subcommittee as a recommendation.

Because of the tax's importance and complexity, Chairman Brickley, with the approval of the joint subcommittee, offered in the 1994 Session a resolution extending the study for one more year, a resolution asking the Department of Taxation to assist with the development of a model ordinance and uniform system of classification, and a bill requiring the Department of Taxation to update the guidelines used by the localities to classify businesses for BPOL tax purposes.

2. 1994 Activities

Beginning in May 1994, the advisory committee met and decided to divide the group into three subcommittees to focus on the following in attempting to develop the model ordinance:

1. Classification/Definitions
2. Audit and Appeals Procedures
3. Taxable Gross Receipts

The three subcommittees met in June and worked on the issues and recommendations related to each of these areas. The Department, particularly John Josephs, Lana Murray and Tim Winks, played an integral part in these meetings and in the entire process of developing the model BPOL ordinance.

The June meeting was followed by meetings in July and September, each one involving much discussion as well as compromise between the local government and business representatives who made up the advisory committee. By the first part of October a draft of the model BPOL ordinance was ready for presentation to the joint subcommittee.

a. October 27, 1994, Meeting. The joint subcommittee's first 1994 meeting focused on the model ordinance. A representative from the Department of Taxation reviewed the model ordinance, emphasizing the most controversial areas, which at that time included the definitions of "gross receipts," "definite place of business," and "professional services," and situs of gross receipts, penalty, interest on refunds, appeals, and audits.

Following the Department's presentation, representatives of the Virginia Association of Counties, the Virginia Municipal League, and the commissioners of the revenue conveyed the local government perspective on the ordinance. While willing to compromise, local government representatives continued to emphasize the importance of a solution that would be revenue-neutral. As previously stated, the revenues generated by the BPOL tax are the third or fourth largest category of local revenue, depending on the locality, exceeded only by real estate, personal property, and sales and use tax revenues. Therefore, the local governments rely on BPOL tax income and cannot afford to lose it.

The business community was represented by the Virginia Chamber of Commerce, the Virginia Manufacturer's Association, Bell Atlantic, and the Virginia Retail Merchants' Association. One business representative suggested repealing the BPOL tax and raising the local option sales and use tax by one percent; however, this suggestion was not supported by all of the business sector. Nevertheless, the BPOL tax is uniformly disliked by business and, in some cases, is harmful to economic development.

Both sides agreed that the model BPOL ordinance should help in administering the tax more uniformly. The chairman then directed the legislative and Department of Taxation staff members to meet with the advisory committee to discuss the remaining controversial areas and attempt to resolve them before the joint subcommittee met again in December.

The advisory committee met twice in November to work on the remaining differences. While many of the differences were resolved, some remained unresolved.

b. December 7, 1994, Meeting. When the joint subcommittee met in October, no one knew that by the next meeting on December 7 there would be a proposal from the Governor to phase out the tax. The Governor made the proposal on December 1 as part of a $2.1 billion tax cut plan and the subcommittee was anxious to hear more about it.

Danny M. Payne, Tax Commissioner, briefed the subcommittee on the basics of the BPOL tax phase-out. Beginning in 1996, localities would have to lower their BPOL tax rates and would continue to do so through the year 2000 until their tax rates were zero. By January 1, 2001, the BPOL tax would be eliminated. During that time, state appropriations would be made annually to localities which levy the tax to cover the reduction in BPOL tax revenues. Also, in order to provide uniformity during the phase-out period, the Governor supported the adoption of the model ordinance which the joint subcommittee had been developing.

In response to these proposals, some members of the subcommittee expressed concern over the appropriations to be made annually to the localities. Would the localities be held harmless and receive the funds in addition to others they expected to receive or would their other appropriations be reduced in order for this BPOL revenue substitute to be funded? What would happen in the year 2001? Would localities be on their own to deal with the lost revenues? The subcommittee was told that answers to these types of questions would be provided on December 19 when the Governor presented his budget amendments.

Other subcommittee members welcomed the proposal, seeing it as a plus for small business in particular and economic development in general. The business community agreed with this evaluation while local government was worried about what would happen after the five-year phase-out.

Tim Winks, Assistant Tax Commissioner for Tax Policy, reviewed the BPOL model ordinance, emphasizing the areas of disagreement between the business community and local government. These were:

- nonprofit organizations exemption
- professional services definition
- investment income deduction
- out-of-state businesses with no Virginia office
- apportionment and situs rules
- reasonable cause for waiving penalty
- impact of taxpayer fault on interest
- stay of collection during administrative appeal
- effective date

The joint subcommittee adopted the model ordinance, with the understanding that changes discussed in the meeting would be made and a final vote taken at the next meeting on January 9, 1995. Also, it was decided to defer until the January meeting a vote on a recommendation to support the Governor's proposal to phaseout the BPOL tax. The majority wanted more information with regard to the funding of the lost revenues during the phase-out and thereafter.

*c. **January 9, 1995, Meeting.*** At its final meeting under HJR 110, the joint subcommittee adopted legislation which included the uniform BPOL ordinance which was introduced during the 1995 General Assembly Session (Appendix C for annotated legislation). The subcommittee also proposed extending the study for one more year by resolution in order to examine the possibility of eliminating the tax and replacing the revenues. (See Appendix D.) This was suggested in place of the motion to support the Governor's proposal to eliminate the tax over a five-year period because a majority of the joint subcommittee members were still concerned about the loss of revenues to the localities during and at the end of the five-year period.

IV. ISSUES

(1) CAN THE BPOL TAX BE ELIMINATED?

(2) WHAT CHANGES CAN BE MADE THROUGH A MODEL ORDINANCE TO IMPROVE THE ADMINISTRATION OF THE BPOL TAX?

V. FINDINGS AND CONCLUSIONS

After determining that the BPOL tax could not be eliminated because an acceptable alternative revenue producer could not be created at this time, the subcommittee decided to focus on the administration of the tax. Both business and local jurisdiction representatives agreed that improvements in how the BPOL tax is administered could be made.

Because the BPOL tax is local option, it is the local jurisdiction which decides whether or not to levy the tax. Once that decision is reached, the local jurisdiction has some leeway on whom it levies the tax. This capability can cause confusion for businesses operating in more than one local jurisdiction. One jurisdiction might levy the tax on a certain business while another neighboring jurisdiction exempts that business. Or one jurisdiction might charge a lower rate than a neighboring jurisdiction does on the same business. Also, the definition of gross receipts is open to varying interpretations by each locality. These are only three of the most obvious problems with the way in which the tax is administered.

In order to alleviate some of these discrepancies the subcommittee recommends the following:

1. ***By legislation, provide a model BPOL ordinance to be used by local jurisdictions which levy the tax in order to bring uniformity to its administration (Appendix C).***

2. ***By joint resolution, extend the study (HJR 613) for one additional year in order to re-examine the possibility of eliminating the tax and replacing it with another source of revenue (Appendix D).***

The joint subcommittee extends its gratitude to everyone who contributed to a successful year of study. We look forward to continuing our work in 1995.

Respectfully submitted,

Delegate David G. Brickley, **Chairman**
Senator E.M. Holland, **Vice Chairman**
Delegate Linda T. Puller
Delegate Harry R. Purkey*
Delegate James M. Scott
Delegate Mitchell Van Yahres
Senator Robert L. Calhoun
Senator Charles J. Colgan
Senator Kevin G. Miller
Connie Bawcum*
Helena L. Dodson
John R. Broadway, Jr.
Mark Jinks
George C. Newstrom
Carl W. Stenberg III

**See Dissenting Remarks*

COMMONWEALTH OF VIRGINIA
HOUSE OF DELEGATES
RICHMOND

HARRY R. (BOB) PURKEY
2352 LEEWARD SHORE DRIVE
VIRGINIA BEACH, VIRGINIA 23451

EIGHTY-SECOND DISTRICT

COMMITTEE ASSIGNMENTS:
FINANCE
HEALTH, WELFARE AND INSTITUTIONS
LABOR AND COMMERCE

Dissenting Remarks

Page 14, First Paragraph:

I respectfully disagree with the first paragraph. I maintain the view that the BPOL tax **can** be eliminated. I believe that various economies of scale downsizing, economic development initiatives, privatization initiatives, agency consolidations, and many other cost savings endeavors can be implemented to offset the lost revenues.

Respectfully submitted,

Bob Purkey

Harry R. Purkey

City of Richmond
Office of the City Manager

900 East Broad Street, Richmond, Virginia 23219
804 • 780-7970

March 15, 1995

Joan Putney
Senior Attorney
Commonwealth of Virginia
Division of Legislative Services
910 Capitol Street, 2nd floor
Richmond, VA 23219

Dear Joan:

Thank you for sending me the draft report of the BPOL study committee. The Advisory Committee members, Legislative Services and the Department of Taxation are to be commended for their efforts on this important matter.

I believe that this study has helped address virtually all of the legitimate concerns of the business community. The model ordinance should assist taxpayers and tax administrators alike in achieving greater uniformity across the Commonwealth.

As a representative of local governments, I am generally very supportive of the overall results of this study. However, I feel that I must express dissent from the subcommittee's report as it relates to the proposed exemption of all businesses with gross receipts of $100,000 or less. The reasons for my dissent are as follows:

- I do not believe that this issue was seriously raised by the business community, or analyzed in any detail by the Advisory Committee. The Advisory Committee's suggested $10,000 threshold was increased tenfold in the very last subcommittee meeting with little analysis as to possible impact.

- There will be a very significant revenue loss to many smaller jurisdictions, especially towns. Very few localities had the opportunity to provide an analysis of fiscal impact.

- An exemption of $100,000, despite the proposed flat $50 license fee, will greatly reduce voluntary filings by the exempt businesses, diminishing the ability of localities to track economic activity in their jurisdictions.

I appreciate the opportunity to comment on this report and to work with all the subcommittee members on this study.

Sincerely,

Connie Bawcum
Deputy City Manager

cc: The Honorable David G. Brickley, Chairman
R. Michael Amyx, Virginia Municpal League

VI. APPENDICES

Appendix A: **House Joint Resolution No. 526 (1993)**

Appendix B: **House Joint Resolution No. 110 (1994)**

Appendix C: **House Bill 2351 (1995),** ***Annotated Legislation***
Prepared by Mr. John Josephs with the Department of Taxation

Appendix D: **House Joint Resolution No. 613 (1995)**

Appendix A

House Joint Resolution No. 526 (1993)

HOUSE JOINT RESOLUTION NO. 526

LD9384136

Establishing a joint subcommittee to study the business, professional, and occupational license tax imposed by localities and to consider alternative means of taxation.

Agreed to by the House of Delegates, February 18, 1993

Agreed to by the Senate, February 16, 1993

WHEREAS, the Commonwealth, within certain limits, has granted localities the authority to issue business, professional and occupational licenses and to charge a tax on the issuance thereof (the"BPOL" tax); and

WHEREAS, such taxes are imposed on the gross receipts generated by the businesses which may be subject to it; and

WHEREAS, a tax measured by gross receipts bears no necessary relationship to the profitability of the businesses which may pay the ta nor does such a tax give any consideration to the competitive situation a particular industry may face nor of the economic situation in general; and

WHEREAS, a business may be a high-volume, low-profit business and incur a large tax liability, while a low-volume, high-profit business will incur a small tax liability; and

WHEREAS, a progressive tax structure is considered one bearing some relationship to a taxpayer's ability to pay and not necessarily to its sales volume or revenue; and

WHEREAS, certain taxpayers in Virginia suffer a much larger local BPOL tax liability than state or federal income tax liability; and

WHEREAS, the BPOL tax may be placing the Commonwealth at a competitive disadvantage in terms of attracting new business to the state and, in fact, may constitute a disincentive for remaining in Virginia or locating here in the first instance; and

WHEREAS, the BPOL tax has become an increasingly important source of local tax revenues, and it would be unfair to reduce or eliminate this source of revenue without replacing it; and

WHEREAS, other forms of taxation may represent a fairer and more easily administered taxing system; and

WHEREAS, the interests of business and government coincide in the area of creating a fair, equitable, and predictable tax structure which provides government with a stable revenue stream and business with a fair taxing system without making the decision to do business in Virginia a competitive disadvantage; now, therefore, be it

RESOLVED by the House of Delegates, the Senate concurring, That a joint subcommittee be established to study the business, professional, and occupational license taxes by localities and to consider options for restructuring or replacing some or all of such taxes with alternative revenue neutral business tax or taxes that are fairer, easier to understand and apply, and more efficient to administer.

The joint subcommittee shall consist of 15 members who shall be appointed in the following manner: five members of the House of Delegates to be appointed by the Speaker of the House; four members of the Senate to be appointed by the Senate Committee on Privileges and Elections; three members of the business community, at least one of whom shall be from the high technology sector; one member of the academic community having knowledge and experience in the area of local government taxation; and a representative from the Virginia Municipal League and the Virginia Association of Counties. The Governor shall appoint all of the nonlegislative members.

The joint subcommittee shall complete its work in time to submits its findings and recommendations, if any, to the Governor and the 1994 Session of the General Assembly as provided in the procedures of the Division of Legislative Automated Systems for the processing of legislative documents.

The indirect costs of this study are estimated to be $9,680; the direct costs shall not exceed $10,800.

Implementation of this resolution is subject to subsequent approval and certification by the Joint Rules Committee. The Committee may withhold expenditures or delay the period for the conduct of the study.

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Appendix B
House Joint Resolution No. 110 (1994)

HOUSE JOINT RESOLUTION NO. 110

Continuing the Joint Subcommittee Studying the Business, Professional, and Occupational License (BPOL) Tax.

Agreed to by the House of Delegates, February 8, 1994

Agreed to by the Senate, February 28, 1994

WHEREAS, House Joint Resolution No. 526, adopted by the 1993 Session of the General Assembly, established a joint subcommittee to study the business, professional, and occupational license (BPOL) tax imposed by local governments; and

WHEREAS, the joint subcommittee was to consider options for restructuring or replacing such tax with an alternative revenue-neutral business tax or taxes that are fairer, easier to understand and apply, and more efficient to administer; and

WHEREAS, the joint subcommittee met twice to review data and to hear testimony from both the business community as well as local governments concerning the BPOL tax; and

WHEREAS, the joint subcommittee appointed an advisory committee consisting of representatives from local government and business to assist the joint subcommittee by developing recommendations concerning the BPOL tax; and

WHEREAS, the advisory committee met twice and discussed possible changes which would improve the administration of the BPOL tax but needs more time to finalize its recommendations; and

WHEREAS, the joint subcommittee realizes this is an important undertaking and any proposed changes must be thoroughly examined and understood prior to their adoption; now, therefore, be it

RESOLVED by the House of Delegates, the Senate concurring, That the joint subcommittee studying the business, professional, and occupational license tax be continued. The membership of the joint subcommittee shall continue as established by House Joint Resolution No. 526 of the 1993 Session of the General Assembly. Vacancies shall be filled by the Governor, the Speaker of the House of Delegates, and the Senate Committee on Privileges and Elections, as appropriate. The joint subcommittee shall continue to review the BPOL tax, particularly the administration of it.

The joint subcommittee shall submit its findings and recommendations to the Governor and the 1995 Session of the General Assembly in accordance with the procedures of the Division of Legislative Automated Systems for the processing of legislative documents.

The direct costs of this study shall not exceed $7,800.

Implementation of this resolution is subject to subsequent approval and certification by the Joint Rules Committee. The Committee may withhold expenditures or delay the period for the conduct of the study.

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Appendix C
House Bill 2351 (1995), *Annotated Legislation*
Prepared by Mr. John Josephs with the Department of Taxation

SENATE BILL NO. ..... **HOUSE BILL NO. .....**

A BILL to amend the Code of Virginia by adding §§ 58.1-3700.1 and 58.1-3703.1, and to amend and reenact §§ 58.1-3700, 58.1-3701, 58.1-3703, 58.1-3706, 58.1-3708, and 58.1-3732 of the Code of Virginia and to repeal §§ 58.1-3707 and 58.1-3725 of the Code of Virginia, relating to the local Business, Professional, and Occupational License tax.

Be it enacted by the General Assembly of Virginia:

1. That the Code of Virginia is amended by adding sections numbered §§ 58.1-3700.1 and 58.1-3703.1, and by amending and reenacting §§ 58.1-3700, 58.1-3701, 58.1-3703, 58.1-3706, 58.1-3708, and 58.1-3732 of the Code of Virginia as follows:

§ 58.1-3700. License requirement; requiring evidence of payment of business license, business personal property, meals and admissions taxes.

Whenever a license is required by ~~law~~ ordinance adopted pursuant to this chapter and whenever the ~~General Assembly~~ local governing body shall impose a license fee or levy a license tax on any business, employment or profession, it shall be unlawful to engage in such business, employment or profession without first obtaining the required license. The governing body of any county, city or town may require that no business license under this chapter shall be issued until the applicant has produced satisfactory evidence that all delinquent business license, personal property, meals, transient occupancy, severance and admissions taxes owed by the business to the county, city or town have been paid which have been properly assessed against the applicant by the county, city or town.

Any person who engages in a business without obtaining a required local license, or after being refused a license, shall not be relieved of the tax imposed by the ordinance.

COMMENT:

Amended to allow the imposition of a license fee and to clarify that the BPOL tax and fee are imposed by a local ordinance. A second paragraph is added to codify 1990 Att'y Gen. Ann. Rpt. 230 (tax owed when business conducted after license refused for zoning violation).

§ 58.1-3700.1. Definitions. For the purpose of this chapter and any local ordinances adopted pursuant to this chapter and unless otherwise required by the context:

"Affiliated group" means

(a) One or more chains of includible corporations connected through stock ownership with a common parent corporation which is an includible corporation if:

(i) Stock possessing at least eighty percent of the voting power of all classes of stock and at least eighty percent of each class of the nonvoting stock of each of the includible corporations, except the common parent corporation, is owned directly by one or more of the other includible corporations; and

(ii) The common parent corporation directly owns stock possessing at least eighty percent of the voting power of all classes of stock and at least eighty percent of each class of the nonvoting stock of at least one of the other includible corporations. As used in this subdivision, the term "stock" does not include nonvoting stock which is limited and preferred as to dividends. The term *"includible corporation"* means any corporation within the affiliated group irrespective of the state or country of its incorporation; and the term "receipts" includes gross receipts and gross income.

(b) Two or more corporations if five or fewer persons who are individuals, estates or trusts own stock possessing:

(i) At least eighty percent of the total combined voting power of all classes of stock entitled to vote or at least eighty percent of the total value of shares of all classes of the stock of each corporation, and

(ii) More than fifty percent of the total combined voting power of all classes of stock entitled to vote or more than fifty percent of the total value of shares of all classes of stock of each corporation, taking into account the stock ownership of each such person only to the extent such stock ownership is identical with respect to each such corporation.

When one or more of the includible corporations, including the common parent corporation is a nonstock corporation, the term "stock" as used in this subdivision shall refer to the nonstock corporation membership or membership voting rights, as is appropriate to the context.

COMMENT:

"Affiliated" is moved from § 58.1-3703 without substantive change.

"*Assessment*" means a determination as to the proper rate of tax, the measure to which the tax rate is applied, and ultimately the amount of tax, including additional or omitted tax, that is due. An assessment shall include a written assessment made pursuant to notice by the assessing official or a self-assessment made by a taxpayer upon the filing of a return or otherwise not pursuant to notice. Assessments shall be deemed made by an assessing official when a written notice of assessment is delivered to the taxpayer by the assessing official or an employee of the assessing official, or mailed to the taxpayer at his last known address. Self-assessments shall be deemed made when a return is filed, or if no return is required, when the tax is paid. A return filed or tax paid before the last day prescribed by ordinance for the filing or payment thereof shall be deemed to be filed or paid on the last day specified for the filing of a return or the payment of tax, as the case may be.

COMMENT:

"Assessment" is new, but based on the definition for state taxes in § 58.1-1820. Under this definition, when a taxpayer files a return showing a tax due, it is a "self-assessment" and the date of the assessment is the date filed or due, whichever is later. When the assessing official determines that a tax is due he must provide a written notice of assessment, whether it is based on an incomplete return (e.g., showing the gross receipts, but not computing the tax), discovery of errors on a return, or discovery of omitted tax (e.g., no return was filed). An assessment by the assessing official is deemed made when the written notice is hand delivered to the taxpayer or mailed to his last known address (the same standard as for state taxes).

"*Base year*" means the calendar year preceding the license year, except for contractors subject to the provisions of § 58.1-3715 or unless the local ordinance provides for a different period for measuring the gross receipts of a business, such as for beginning businesses or to allow an option to use the same fiscal year as for federal income tax purposes.

COMMENT:

The base year is the year used to calculate the gross receipts for most businesses subject to a tax measured by gross receipts. Typically the license, and license tax, for 1995 would be based on 1994 gross receipts; however, a new business usually would have to estimate its 1995 gross receipts. Also, certain contractors would have to base their 1995 license tax on 1995 gross receipts (if they exceed $25,000). Other types of business pay a flat amount without regard to gross receipts.

"*Business*" means a course of dealing which requires the time, attention and labor of the person so engaged for the purpose of earning a livelihood or profit. It implies a continuous and regular course of dealing, rather than an irregular or isolated transaction. A person may be engaged in more than one business. The following acts shall create a rebuttable presumption that a person is engaged in a business: (i) advertising or otherwise holding oneself out to the public as being engaged in a particular business; (ii) filing tax returns, schedules and documents that are required only of persons engaged in a trade or business.

COMMENT:

"Business" is new. The first two sentences are the common law definition quoted from City of Portsmouth v. Citizens Trust Co., 219 Va. 903, 252 S.E.2d 339 (1979). See also, 1987-1988 Att'y Gen. Ann. Rep. 513; and Va. Code § 58.1-5 (Dual Business). A person engaged in a "business" may be required to obtain a license. If the person is engaged in a second business another license may be required. It is not intended that secondary licenses be required for occasional transactions solely because they would be in a different classification from the primary licensed business if the transactions are merely ancillary to the primary business. See County of Chesterfield v. BBC Brown Boveri, 238 Va. 64 at 72 (1989). The assessing official will have to review the facts and circumstances of the primary business and its relationship to the transactions in question to determine if the transactions constitute a separate licensable business rather than occasional and irregular transactions or transactions that are ancillary to the primary business. The assessing official's determination would be subject to de novo review by the circuit court under § 58.1-3984. Persons who advertise their availability to engage in business activities, or who file a Schedule C with their federal tax return should have to overcome a presumption that they have accurately portrayed the nature of their activities to the public and I.R.S.

"*Definite place of business*" means an office or a location at which occurs a regular and continuous course of dealing for 30 consecutive days or more. A definite place of business for a person engaged in business may include a location leased or otherwise obtained from another person on a temporary or seasonal basis; and real property leased to another. A person's residence shall be deemed to be a definite place of business if there is no definite place of business maintained elsewhere and the person is not licensable as a peddler or itinerant merchant.

COMMENT:

"Definite place of business" is new. This definition, when combined with the license requirement in § 58.1-3703.1 (1) and the situs rules means that transient businesses can be taxed only by the locality where its definite place of business is located (office or residence). There are, however, statutory exceptions permitting the taxation of certain kinds of transient businesses such as itinerant merchants, peddlers, circuses and carnivals.

The broad definition would enable localities to require licenses and impose the $50 license fee (as set forth in § 58.1-3703) on business locations without regard to whether gross receipts are generated at the location. Having a definite place of business, however, will not result in a tax on gross receipts unless the situs rules in § 58.1-3703.1 A.3. attribute gross receipts to the definite place of business.

A small business with no office anywhere will be presumed to have a definite place of business at the person's residence. Defining a person's residence as a definite place of business conforms with § 58.1-3707(B) and 1985-1986 Att'y Gen. Ann. Rep. 288 and provides an exception to 1991 Att'y Gen. Ann. Rep. 252 and Commonwealth v. Manzer, 207 Va. 996 (1967), which held that a home office includes space set aside, equipped and regularly used to transact business. If uniform and predictable rules are to assign receipts somewhere for taxation (even if out of state), then the residence must be the last resort when there is no other definite place of business anywhere.

The 30 day rule seems to be a reasonable period, and is used by at least one locality. The person does not have to own the definite place of business, only use it for 30 days or more to engage in the licensable business. Thus, for example, a person who leases space from another and conducts a licensable business in such leased space for 30 days or more has a definite place of business at the leased space (note, however, that the 30 days does not apply to an itinerant merchant or peddler who must have a license for a single day's operation of a business).

In most localities an owner engaged in the business of renting space to others would be exempt from BPOL. See § 58.1-3703.B.7. However, in localities where a tax on such real estate rental businesses has existed since January 1, 1974, the real estate that is rented would be considered a definite place of business, and the gross rental income derived from the real estate would be taxable gross receipts.

"*Financial services*" means the buying, selling, handling, managing, investing, and providing advice regarding money, credit, securities, or other investments.

COMMENT:

The definition is derived from City of Richmond Code § 27-316 except that "commodities" was deleted (futures and options related to commodities are covered by "securities").

"*Gross receipts*" means the whole, entire, total receipts, without deduction.

COMMENT:

"Gross receipts" is new, and derived from Savage v. Commonwealth, 186 Va. 1012 (1947). Several exclusions from gross receipts are added to § 58.1-3732.

"*License year*" means the calendar year for which a license is issued for the privilege of engaging in business.

COMMENT:

"License year" and "base year" are defined. Generally the tax is paid early in one calendar year (license year) based on gross receipts for the preceding calendar year (base year).

"*Professional services*" means services performed by architects, attorneys-at-law, certified public accountants, dentists, engineers, land surveyors, surgeons, veterinarians, and practitioners of the healing arts (the arts and sciences dealing with the prevention, diagnosis, treatment and cure or alleviation of human physical or mental ailments, conditions, diseases, pain or infirmities) and such occupations, and no others, as the Department of Taxation may list in the BPOL Guidelines promulgated pursuant to § 58.1-3701. The Department shall identify and list each occupation or vocation in which a professed

knowledge of some department of science or learning, gained by a prolonged course of specialized instruction and study is used in its practical application to the affairs of others, either advising, guiding, or teaching them, and in serving their interests or welfare in the practice of an art or science founded on it. The word "profession" implies attainments in professional knowledge as distinguished from mere skill, and the application of knowledge to uses for others rather than for personal profit.

COMMENT:

"Professional services" is derived from the BPOL Guidelines promulgated by the Department on January 1, 1979, and last updated January 1, 1984. The advisory committee could not reach a consensus on this definition. The business community believed that the classification should be limited because it is subject to taxation at the highest rate. However, the term appears to have been given a broader meaning in the past. This definition implements a compromise in that, while the broader definition from the BPOL Guidelines is adopted, certainty will be achieved by limiting the professional classification to only those occupations listed by the department in the updated BPOL Guidelines. The Department will update the BPOL Guidelines by July 1, 1995, after consulting local officials and other interested parties and holding a hearing. The BPOL Guidelines currently exclude all consultants from the professional classification. In the update the department will consider if consultants who provide professional services should be classified as professionals.

"*Purchases*" means all goods, wares and merchandise received for sale at each definite place of business of every wholesale merchant. The term shall also include the cost of manufacture of all goods, wares and merchandise manufactured by any wholesale merchant and sold or offered for sale. A wholesale merchant may elect to report the gross receipts from the sale of manufactured goods, wares and merchandise if it cannot determine the cost of manufacture or chooses not to disclose the cost of manufacture.

COMMENT:

The definition of purchases is derived from §§ 58-304 and 58-317 relating to the state license tax on wholesale merchants before its repeal.

"*Real estate services*" means providing a service with respect to the purchase, sale, lease, rental, or appraisal of real property.

COMMENT:

The definition is new.

§ 58.1-3701. Department to promulgate guidelines.

The Department of Taxation shall promulgate guidelines ~~defining and explaining the categor... listed in subsection A of § 58.1-3706~~ for the use of local governments in administering the taxes imp... under authority of this chapter. In preparing such guidelines, the Department shall not be subject to provisions of the Administrative Process Act (§ 9-6.14:1 et seq.) of the Code of Virginia for guidel... promulgated on or before July 1, 2001, but shall cooperate with and seek the counsel of local officials interested groups and shall not promulgate such guidelines without first conducting a public hearing. S... guidelines shall be updated during the 1994 taxable year and available for distribution to local governm... on July 1, 1995. Thereafter, the guidelines shall be updated triennially. After July 1, 2001, guidelines shall be subject to the Administrative Process Act and accorded the weight of a regulation under § 58.1-205.

The Tax Commissioner shall have the authority to issue advisory written opinions in specific cases to interpret the provisions of this ~~section~~ chapter and the guidelines issued pursuant to this ~~subsection~~ section; provided, however, that the Tax Commissioner shall not be required to interpret any local ordinance. The guidelines and opinions issued pursuant to this section shall not be applicable as an interpretation of any other tax law.

COMMENT:

The language limiting the Department's authority to classification issues is deleted. Therefore, the guidelines and advisory opinions may involve any issues under this chapter. However, the Department will not be required to issue opinions involving the interpretation of a local ordinance. The BPOL Guidelines are not currently binding on localities, although they are accorded great weight by local officials and the courts. Effective July 1, 2001, the BPOL Guidelines must be promulgated in accordance with the Administrative Process Act and will be binding on all parties to the same extent as a regulation.

§ 58.1-3703. Counties, cities and towns may impose local license taxes and fees; limitation of authority.

A. The governing body of any county, city or town may charge a fee for issuing a license in an amount not to exceed fifty dollars and may levy and provide for the assessment and collection of county, city or town license taxes on businesses, trades, professions, occupations and callings and upon the persons, firms and corporations engaged therein within the county, city or town subject to the limitations provided in subsection B of this section. The ordinance imposing such license fees and levying such license taxes shall include the provisions of § 58.1-3703.1.

B. No county, city, or town shall impose a license fee or levy any license tax:

1. On any public service corporation except as provided in § 58.1-3731 or as permitted by other provisions of law;

2. For selling farm or domestic products or nursery products, ornamental or otherwise, or for the planting of nursery products, as an incident to the sale thereof, outside of the regular market houses and sheds of such county, city or town; provided, such products are grown or produced by the person offering such products for sale;

3. Upon the privilege or right of printing or publishing any newspaper, magazine, newsletter or other publication issued daily or regularly at average intervals not exceeding three months, provided the publication's subscription sales are exempt from state sales tax, or for the privilege or right of operating or conducting any radio or television broadcasting station or service;

4. On a manufacturer for the privilege of manufacturing and selling goods, wares and merchandise at wholesale at the place of manufacture;

5. On a person engaged in the business of severing minerals from the earth for the privilege of selling the severed mineral at wholesale at the place of severance, except as provided in §§ 58.1-3712 and 58.1-3713;

6. Upon a wholesaler for the privilege of selling goods, wares and merchandise to other persons for resale unless such wholesaler has a definite place of business or store in such county, city or town. This subdivision shall not be construed as prohibiting any county, city or town from imposing a local license tax on a peddler at wholesale pursuant to § 58.1-3718;

7. Upon any person, firm or corporation for engaging in the business of renting, as the owner of such property, real property other than hotels, motels, motor lodges, auto courts, tourist courts, travel trailer parks, lodging houses, rooming houses and boardinghouses; however, any county, city or town imposing such a license tax on January 1, 1974, shall not be precluded from the levy of such tax by the provisions of this subdivision;

8. Upon a wholesaler or retailer for the privilege of selling bicentennial medals on a nonprofit basis for the benefit of the Virginia Independence Bicentennial Commission or any local bicentennial commission;

9. On or measured by receipts for management, accounting, or administrative services provided on a group basis under a nonprofit cost-sharing agreement by a corporation which is an agricultural cooperative association under the provisions of Chapter 3, Article 2 (§ 13.1-312 et seq.), Title 13.1, or a member or subsidiary or affiliated association thereof, to other members of the same group. This exemption shall not exempt any such corporation from such license or other tax measured by receipts from outside the group;

10. On or measured by receipts or purchases by a corporation which is a member of an affiliated group of corporations from other members of the same affiliated group. This exclusion shall not exempt affiliated corporations from such license or other tax measured by receipts or purchases from outside the affiliated group. This exclusion also shall not preclude a locality from levying a wholesale merchant's license tax on an affiliated corporation on those sales by the affiliated corporation to a nonaffiliated person, company, or corporation, notwithstanding the fact that the wholesale merchant's license tax would be based upon purchases from an affiliated corporation. Such tax shall be based on the purchase price of the goods sold to the nonaffiliated person, company, or corporation. As used in this subdivision the term *"sales by the affiliated corporation to a nonaffiliated person, company or corporation"* shall mean sales by the affiliated corporation to a nonaffiliated person, company or corporation where goods sold by the affiliated corporation or its agent are manufactured or stored in the Commonwealth prior to their delivery to the nonaffiliated person, company or corporation.

~~For purposes of this exclusion, the term *"affiliated group" means*~~

~~(a) One or more chains of includible corporations connected through stock ownership with a common parent corporation which is an includible corporation if:~~

~~(i) Stock possessing at least eighty percent of the voting power of all classes of stock and at least eighty percent of each class of the nonvoting stock of each of the includible corporations, except the common parent corporation, is owned directly by one or more of the other includible corporations; and~~

~~(ii) The common parent corporation directly owns stock possessing at least eighty percent of the voting power of all classes of stock and at least eighty percent of each class of the nonvoting stock of at least one of the other includible corporations. As used in this subdivision, the term "stock" does not include nonvoting stock which is limited and preferred as to dividends. The term *"includible corporation"* means any corporation within the affiliated group irrespective of the state or country of its incorporation; and the term "receipts" includes gross receipts and gross income.~~

~~(b) Two or more corporations if five or fewer persons who are individuals, estates or trusts own stock possessing:~~

~~(i) At least eighty percent of the total combined voting power of all classes of stock entitled to vote or at least eighty percent of the total value of shares of all classes of the stock of each corporation, and~~

~~(ii) More than fifty percent of the total combined voting power of all classes of stock entitled to vote or more than fifty percent of the total value of shares of all classes of stock of each corporation, taking into account the stock ownership of each such person only to the extent such stock ownership is identical with respect to each such corporation.~~

~~When one or more of the includible corporations, including the common parent corporation is a nonstock corporation, the term "stock" as used in this subdivision shall refer to the nonstock corporation membership or membership voting rights, as is appropriate to the context;~~

11. On any insurance company subject to taxation under Chapter 25 (§ 58.1-2500 et seq.) of this title or on any agent of such company;

12. On any bank or trust company subject to taxation in Chapter 12 (§ 58.1-1200 et seq.) of this title;

13. Upon a taxicab driver, if the locality has imposed a license tax upon the taxicab company for which the taxicab driver operates;

14. On any blind person operating a vending stand or other business enterprise under the jurisdiction of the Department for the Visually Handicapped, or a nominee of the Department, as set forth in § 63.1-164;

15. **(Expires July 1, 1997)** On any hospital, college, university, or other institution of learning not organized or conducted for pecuniary profit which by reason of its purposes or activities is exempt from income tax under the laws of the United States unless such tax was enacted by the local governing body prior to January 15, 1991. The provisions of this subdivision shall expire on July 1, 1997;

16. ~~Upon any person who is authorized to celebrate the rites of marriage under §§ 20-23 and 20-25 and any person who is authorized to solemnize a marriage under § 20-26 provided such gross annual receipts total no more than $500;~~ ~~or~~

17. On an accredited religious practitioner in the practice of the religious tenets of any church or religious denomination. *"Accredited religious practitioner"* shall be defined as one who is engaged solely in praying for others upon accreditation by such church or religious denomination ; or

18. Nonprofit organizations.

(a) On or measured by receipts of a charitable nonprofit organization except to the extent the organization has receipts from any trade or business the conduct of which is not substantially related to the exercise or performance of its charitable, educational, or other purpose or function constituting the basis for its exemption. When determining whether a trade or business is substantially related to the exempt purpose of a nonprofit organization, the determination shall be based solely on the relationship of the business activities to the exempt purpose. The fact that profits derived from the trade or business may be used for an exempt purpose shall not be considered. For the purpose of this subdivision, the term "charitable nonprofit organization" shall mean an organization which is described in Internal Revenue Code § 501(c)(3) and to which contributions are deductible by the contributor under Internal Revenue Code § 170, except that educational institutions shall be limited to schools, colleges and other similar institutions of learning.

(b) On or measured by gifts, contributions, and membership dues of a non-profit organization. Activities conducted for consideration which are similar to activities conducted for consideration by for-profit businesses shall be presumed to be activities that are part of a licensable business. For the purpose of this subdivision, the term "nonprofit organization" shall mean an organization exempt from federal income tax under Internal Revenue Code § 501 other than charitable nonprofit organizations.

COMMENT:

The first paragraph is amended to retain licensing authority and allow localities to levy a flat license fee of $50 or less on all licensable businesses. The Joint Subcommittee adopted this concept at its January 9, 1995 meeting in conjunction with provisions in § 58.1-3706 which exempt businesses with gross receipts of $100,000 or less from the tax. The license fee would apply to all businesses, including larger businesses who would pay the fee, plus a tax on gross receipts. Although imposed as a fee, localities could provide a credit against the tax due by larger businesses.

The section also requires each locality imposing a BPOL tax to adopt the uniform ordinance provisions. The definition of "affiliated" is moved to the definitions section.

A new exemption is also added for nonprofit organizations. This exemption is a matter of great concern to localities because it may exempt significant business activities of some taxpayers. A distinction is drawn between traditional charities (churches, schools, etc.) to which tax deductible contributions can be made. Traditional charities will be subject to BPOL tax only if they engage in activities that would subject them to federal income tax on their unrelated business taxable income (UBIT) under the Internal Revenue Code. However, the UBIT rules are extremely complex and difficult to administer and the Internal Revenue Service enforcement of UBIT reporting by nonprofits has been criticized in the past. Therefore, local assessing officials will not be bound by the fact that the I.R.S. has failed to assess a tax on UBIT. Under this approach, when the current moratorium on taxing nonprofit hospitals and colleges expires in 1997 (together with the grandfather clause for existing taxes on such organizations) both types of organizations would be exempt except to the extent of UBIT.

Many other types of nonprofit organizations also exist, such as social clubs, business and trade organizations, and various types of employee benefit associations. Localities have generally required licenses when a nonprofit organization engages in a trade or business that competes with other licensable businesses. Under this approach, for example, a social club that occasionally organizes a trip for its members would not be engaged in a business, but a "club" that continuously advertises numerous trips to the general public is probably engaged in a business that competes with a licensable travel agency. As with any person, the determination of whether a particular nonprofit organization's activities constitute a licensable business is a factual issue for which the assessing official must make an investigation and initial determination.

§ 58.1-3703.1. Uniform ordinance provisions.

A. Every ordinance levying a license tax pursuant to this chapter shall include provisions substantially similar to the subdivisions of this subsection. As they apply to license taxes, the provisions required by this section shall override any limitations or requirements in Chapter 39 of Title 58.1 of the Code of Virginia to the extent that they are in conflict.

(1.) License requirement.

Every person shall apply for a license for each business or profession when engaging in a business in this jurisdiction if (i) the person has a definite place of business in this jurisdiction; or (ii) there is no definite place of business anywhere and the person resides in this jurisdiction; or (iii) there is no definite place of business in this jurisdiction but the person operates amusement machines or is classified as an itinerant merchant, a peddler, carnival, circus, contractor subject to § 58.1-3715, or a public service corporation. A separate license shall be required for each definite place of business and for each business. A person engaged in two or more businesses or professions carried on at the same place of business may elect to obtain one license for all such businesses and professions if all of the following criteria are satisfied: (i) each business or profession is licensable at the location and has satisfied any requirements imposed by state law or other provisions of the ordinances of this jurisdiction; (ii) all of the businesses or professions are subject to the same tax rate or, if subject to different tax rates, the licensee agrees to be taxed on all businesses and professions at the highest rate; and (iii) the taxpayer agrees to supply such information as the assessor may require concerning the nature of the several businesses and their gross receipts.

COMMENT:

Some localities use license tax information to keep track of the business conducted in the locality, the owner of each business, and other data. These localities may issue licenses without charge to small businesses as long as the information is supplied. The owner of two or more businesses taxed similarly may elect to obtain a single license for all business conducted at the same location, but the locality may require adequate information about the different businesses for recordkeeping purposes.

(2.) Due dates and penalties

a. Each person subject to a license tax shall apply for a license prior to beginning business, if he was not licensable in this jurisdiction on or before January 1 of the license year, or no later than March 1 of the license year if he has been issued a license for the preceding year. The application shall be on forms prescribed by the assessing official.

b. The tax shall be paid with the application in the case of any license not based on gross receipts. If the tax is measured by the gross receipts of the business the tax shall be paid on or before March 1 or later date, including installment payment dates, or 30 or more days after beginning business, at the locality's option.

c. The assessing official may grant an extension of time in which to file an application for license for reasonable cause. The extension may be conditioned upon the timely payment of a reasonable estimate of the appropriate tax, subject to adjustment to the correct tax at the end of the extension together with interest from the due date until the date paid and, if the estimate submitted with the extension is found to be unreasonable under the circumstances, a penalty of 10% of the portion paid after the due date.

d. A penalty of 10% of the tax may be imposed upon the failure to file an application or the failure to pay the tax by the appropriate due date. Only the late filing penalty shall be imposed by the assessing official if both the application and payment are late; however both penalties may be assessed if the assessing official determines that the taxpayer has a history of noncompliance. In the case of an assessment of additional tax made by the assessing official, if the application and, if applicable, the return were made in good faith and the understatement of the tax was not due to any fraud, reckless or intentional disregard of the law by the taxpayer, there shall be no late payment penalty assessed with the additional tax. If any assessment of tax by the assessing official is not paid within 30 days the Treasurer or other collecting official may impose a 10% late payment penalty. The penalties shall not be imposed, or if imposed shall be abated by the official who assessed them, if the failure to file or pay was not the fault of the taxpayer. In order to demonstrate lack of fault the taxpayer must show that he acted responsibly and that the failure was due to events beyond his control.

"Acted responsibly" means that: (i) the taxpayer exercised the level of reasonable care that a prudent person would exercise under the circumstances in determining the filing obligations for the business; and (ii) the taxpayer undertook significant steps to avoid or mitigate the failure, such as requesting appropriate extensions (where applicable), attempting to prevent a foreseeable impediment, acting to remove an impediment once it occurred, and promptly rectifying a failure once the impediment was removed or the failure discovered.

"Events beyond the taxpayer's control" include, but are not limited to, the unavailability of records due to fire or other casualty, or the unavoidable absence (e.g., due to death or serious illness) of the person with the sole responsibility for tax compliance; or the taxpayer's reasonable reliance in good faith upon erroneous written information from the assessing official, who was aware of the relevant facts relating to the taxpayer's business when he provided the erroneous information.

COMMENT:

A uniform March 1 due date is specified (see transitional provisions below for the effective date and proration by localities which must change their license year). Some businesses cannot ascertain their gross receipts until federal tax returns are prepared -- the assessing official can grant filing extensions, but may require payment of an estimated amount of tax. This is similar to how federal and Virginia income tax extensions are granted. Note that the locality has the option of specifying a later payment date or installment payment dates.

The Advisory Committee could not reach consensus on the issue of reasonable cause for waiving penalties. The business community believes that the existing language referring to lack of fault by the taxpayer means that penalties should be waived for "reasonable cause shown," a standard which is widely used but hard to define. Localities are concerned with the lack of uniformity an undefined standard would cause when administered by numerous officials. The standard in this draft requiring responsible action and events beyond the taxpayer's control is derived from U.S. Treas. Reg. § 301.6724-1 relating to reasonable cause for abating a penalty for failure to file information returns.

The business community also believes that a taxpayer who fails to file because he honestly believes that no tax is owed is entitled to penalty waiver. The holding of Commonwealth v. United Cigarette Machine Co., 120 Va. 835 (1917) lends support to this interpretation of lack of taxpayer fault. However, in United Cigarette the taxpayer had advice of counsel and the circuit court found in its favor. Not until the Virginia Supreme Court reversed was it clear that a tax was owed. Most taxpayers are unlikely to have such strong evidence supporting their "honest belief." The Internal Revenue Service has attempted to define the equivalent to an "honest belief" in its regulation § 1.6662-4 for accuracy related penalties, which requires a taxpayer to have substantial authority for a position taken in filing a return. Such a standard was omitted from this draft because of the complexity and uncertainty created when a taxpayer's motives and beliefs must be evaluated. Taxpayers desiring certainty may obtain an advance ruling from the assessing official under subdivision A.4. below. Further guidance is expected in the BPOL Guidelines.

If a return was filed and additional tax was found on audit, the local Commissioners generally do not assess any penalty. This practice is codified for returns filed in good faith with language derived from income tax penalty provisions except that "fraud, reckless or intentional disregard of the law" is substituted for "without any fault by the taxpayer." Mistakes happen, and a taxpayer who has filed a return in good faith should not be penalized for an innocent mistake, or required to prove that the mistake was an event beyond his control. Instead, the auditor will be required to determine that the under reporting of gross receipts was intentional.

e. Interest. Interest shall be charged on the late payment of the tax from the due date until the date paid without regard to fault or other reason for the late payment. Whenever an assessment of additional or omitted tax by the assessing official is found to be erroneous, all interest and penalty charged and collected on the amount of the assessment found to be erroneous shall be refunded together with interest on the refund from the date of payment or the due date, whichever is later. Interest shall be paid on the refund of any BPOL tax from the date of payment or due date, whichever is later, whether attributable to an amended return or other reason. Interest on any refund shall be paid at the same rate charged under § 58.1-3916.

No interest shall accrue on an adjustment of estimated tax liability to actual liability at the conclusion of a base year. No interest shall be paid on a refund or charged on a late payment, provided the refund or the late payment is made not more than thirty days from the date of the payment that created the refund or the due date of the tax, whichever is later.

COMMENT:

The business community and localities have differing views on when interest should apply: the localities consider interest to be related to fault, while the business community views interest as a charge for the use of funds without regard to fault. At one time state law required the payment of interest only if the taxpayer was not at fault (the United Cigarette case discussed above contains a reference to such a law). Fault is no longer relevant to interest on state taxes, but vestiges of fault can still be found in laws and ordinances relating to local taxes. See § 58.1-3916 which provides that no penalty or interest shall be assessed for late filing or late payment if the failure was not the fault of the taxpayer.

Per the Joint Subcommittee meeting of January 9, 1995, the section was amended to abandon fault with respect to interest on late payments and refunds and require that interest accrue in both instances. Additionally, a grace period is provided whereby interest would not be paid or charged if an error is discovered and corrected within 30 days, either on the part of the locality or the taxpayer. The refund interest rate is set at the same amount charged for late payments.

(3.) Situs of gross receipts.

(a) General Rule. Whenever the tax imposed by this ordinance is measured by gross receipts, the gross receipts included in the taxable measure shall be only those gross receipts attributed to the exercise of a licensable privilege at a definite place of business within this jurisdiction. In the case of activities conducted outside of a definite place of business, such as during a visit to a customer location, the gross receipts shall be attributed to the definite place of business from which such activities are initiated, directed, or controlled. The situs of gross receipts for different classifications of business shall be attributed to one or more definite places of business or offices as follows:

(i) the gross receipts of a contractor shall be attributed to the definite place of business at which his services are performed, or if his services are not performed at any definite place of business, then the definite place of business from which his services are directed or controlled, unless the contractor is subject to the provisions of § 58.1-3715;

(ii) the gross receipts of a retailer or wholesaler shall be attributed to the definite place of business at which sales solicitation activities occur, or if sales solicitation activities do not occur at any definite place of business, then the definite place of business from which sales solicitation activities are directed or controlled, provided, however, that a wholesaler subject to a license tax measured by purchases shall determine the situs of its purchases by the definite place of business at which or from which deliveries of the purchased goods, wares and merchandise are made to customers, and any wholesaler subject to license tax in two or more localities who is subject to multiple taxation because the localities use different measures may apply to the Department of Taxation for a determination as to the proper measure of purchases and gross receipts subject to license tax in each locality;

(iii) the gross receipts of a business renting tangible personal property shall be attributed to the definite place of business from which the tangible personal property is rented or, if the property is not rented from any definite place of business, then the definite place of business at which the rental of such property is managed;

(iv) the gross receipts from the performance of services shall be attributed to the definite place of business at which the services are performed or, if not performed at any definite place of business, then the definite place of business from which the services are directed or controlled.

(b) Apportionment. If the licensee has more than one definite place of business and it is impractical or impossible to determine to which definite place of business gross receipts should be

attributed under the general rule, the gross receipts of the business shall be apportioned between the definite places of businesses on the basis of payroll. Gross receipts shall not be apportioned to a definite place of business unless some activities under the applicable general rule occurred at, or were controlled from, such definite place of business. Gross receipts attributable to a definite place of business in another jurisdiction shall not be attributed to this jurisdiction solely because the other jurisdiction does not impose a tax on the gross receipts attributable to the definite place of business in such other jurisdiction.

(c) Agreements. The assessor may enter into agreements with any other political subdivision of Virginia concerning the manner in which gross receipts shall be apportioned among definite places of business. However, the sum of the gross receipts apportioned by the agreement shall not exceed the total gross receipts attributable to all of the definite places of business affected by the agreement. Upon being notified by a taxpayer that its method of attributing gross receipts is fundamentally inconsistent with the method of one or more political subdivisions in which the taxpayer is licensed to engage in business and that the difference has, or is likely to, result in taxes on more than 100% of its gross receipts from all locations in the affected jurisdictions, the assessor shall make a good faith effort to reach an apportionment agreement with the other political subdivisions involved. If an agreement cannot be reached, either the assessor or taxpayer may seek an advisory opinion from the Department of Taxation pursuant to § 58.1-3701, notice of which request shall be given to the other party. Notwithstanding the provisions of § 58.1-3993, when a taxpayer has demonstrated to a court that two or more political subdivisions of Virginia have assessed taxes on gross receipts that may create a double assessment within the meaning of § 58.1-3986, the court shall enter such orders pending resolution of the litigation as may be necessary to ensure that the taxpayer is not required to pay multiple assessments even though it is not then known which assessment is correct and which is erroneous.

COMMENT:

The situs and apportionment rules in this section, together with the amendments to § 58.1-3708 and the repeal of § 58.1-3707, create uniform rules for all businesses and professions. Gross receipts must be attributed to a definite place of business. The draft repeals language in § 58.1-3708 allowing a locality to tax gross receipts of an out of state business if it has no definite place of business anywhere in Virginia. It has also been the practice in a few localities to tax gross receipts that may properly be attributable to another locality if that locality did not impose a BPOL tax; this "throwback" practice is eliminated (except for contractors subject to § 58.1-3715).

Several localities objected to the limitation to a definite place of business, citing a revenue loss to the extent that out-of-state businesses with no definite place of business in Virginia are exempted. It is believed that the limitation is consistent with legislative intent and history, and reduces the risk of constitutional questions. Such a business may face multiple taxation if its sole office is in another state which has a gross receipts tax because there is no mechanism to ensure that receipts taxed elsewhere are not again taxed in Virginia. Such a business would be subject to different tax rules than a similar type of business with an office in Virginia, which raises constitutional issues, especially when the rules are internally inconsistent (i.e., that no more than 100% of gross receipts would be taxed if all jurisdictions imposed the same tax as the one in dispute).

Situs: With few exceptions, gross receipts are only taxable at a definite place of business that generated them. If a business has only one definite place of business then all of its gross receipts are properly attributable there. See Short Brothers, Inc. v. Arlington County, 244 Va. 520 (1992). However, application of BPOL tax to a large, decentralized business with numerous offices is difficult and often controversial. Several offices may participate or contribute to a particular sale, and the business may keep its records on a profit center basis rather than by political jurisdictions.

Rules are set out for sourcing gross receipts to the appropriate definite place of business. Several localities have expressed concern over these rules, particularly in the area of sales solicitation activity. This concept has been discussed (earlier drafts focused on customer contact) but not resolved. Under this proposal no gross receipts would be attributed to a warehouse even if it ships merchandise directly to customers. While many localities do not currently tax warehouses, those that do would lose revenue.

The Advisory Committee considered changing the measure for taxing wholesale merchants from purchases to gross receipts, since some are now taxed on gross receipts under the grandfather clause in § 58.1-3716 (i.e., the locality taxed wholesale merchants on gross receipts prior to 1964). This change, however, would have also changed where wholesalers were taxed. Purchases are taxed at the definite place of business where the goods are physically delivered to customers or placed on trucks for delivery to customers. See Richmond v. Petroleum Marketers, 221 Va. 372 (1980). The situs rules would have changed this to the location of the sales office. There was also concern that the change in measure would affect the taxation of distributing houses (warehouses owned by a chain of retail stores that distribute goods to the retail stores). Under former § 58-319 distributing houses were expressly subject to state license tax on purchases in the same manner as wholesale merchants. At its January 9, 1995, meeting the Joint Subcommittee decided to continue the existing treatment of wholesalers with the proviso that any allegation of double taxation by localities using different measures would be resolved by the Department of Taxation.

Apportionment: Where two or more locations participate in a sale, and the gross receipts cannot easily be sourced by the business records, then apportionment is required. The use of VEC payroll information seems to be the preferred method among localities and is mandated. Although the use of payroll information is relatively easy to administer, it must be emphasized that the purpose is to divide gross receipts among the definite places of business that participate in sales and service activities, not to impose a disguised payroll tax on all employees. Some localities have used apportionment to attribute gross receipts to a definite place of business which has no contact with customers, no participation in specific sales or service contracts, and to which no gross receipts would be attributable under the proposed situs rules. Examples of such locations might be a research facility, or general administrative facilities. Under the proposed apportionment rules no gross receipts could be attributed to such locations.

Comments from the business community expressed reservations about any formula for apportionment because it resembled an income tax. The business community also expressed reservations about taxing any item of gross receipts when all of the activity that was necessary to earn it did not occur in the taxing locality. Adopting such an approach would also look like an income tax, which considers all activity and expenses to "earn" income, than a gross receipts tax, which focuses on the activity that produced the sale. Both the Attorney General and Virginia Supreme Court have recently issued opinions on when apportionment of local taxes is required: Opinion to the Honorable Ross A. Mugler dated November 17, 1994, relating to BPOL tax, and Ryder Truck Rental, Inc. v. County of Chesterfield, (November 4, 1994) relating to personal property tax. The Ryder case is particularly relevant because the court noted that the fact that property was absent from Chesterfield for part of the year did not prove that the property had acquired tax situs elsewhere for property tax purposes. Thus, the fact that a taxpayer has activities in another state sufficient to subject it to property, income or other taxes is not sufficient to require apportionment under this draft unless the taxpayer has a definite place of business to which gross receipts would be properly attributable. But see § 58.1-3728 for a deduction allowed for receipts subject to an income tax in another state.

Agreements: Localities are encouraged to enter into agreements with other localities to ensure that the situs and apportionment rules are uniformly applied to a particular business in order to reduce the risk of multiple taxation. No mechanism is provided to resolve situations in which the localities cannot agree, but the Tax Department may be called upon to issue an advisory opinion.

Legislative History: The legislative history appears to demonstrate an intent to limit localities to taxing only gross receipts attributable to a definite place of business. For many years only cities and towns had the authority to impose a BPOL tax. Then in 1948 two counties were allowed to impose it, and additional counties were authorized in 1950 and 1952. In 1954 the General Assembly enacted a situs rule for professions (tied primarily to an office) and for a place of business that straddled a local boundary line (divided by area of the building in each locality). These rules survive in §§ 58.1-3707 and 58.1-3709. In 1956 another situs rule was added, initially applicable only to certain cities and adjacent counties, that focused on a definite place of business. This provision (§ 58-266.5, the predecessor to § 58.1-3708) used to allow localities to tax gross receipts attributable to picking up and delivering property, even though the work was done at a definite place of business in another locality. See Stork Diaper Serv. Inc. v. City of Richmond, 210 Va. 705 (1970). When BPOL tax authority was extended to all counties in 1964, wholesalers were taxable only if a definite place of business existed in the locality. See 1964 Acts of Assembly, Ch. 424. The 1974 General Assembly overturned Stork Diaper by amending § 58-266.5 to eliminate all authority for a locality to tax gross receipts solely on the basis of pickups and deliveries by a business located in another Virginia locality. 1974 Acts of Assembly Ch. 386. See also the comments following § 58.1-3707.

(4.) Limitations and extensions.

(a) Where before the expiration of the time prescribed for the assessment of any license tax imposed pursuant to this ordinance both the assessing official and the taxpayer have consented in writing to its assessment after such time, the tax may be assessed at any time prior to the expiration of the period agreed upon. The period so agreed upon may be extended by subsequent agreements in writing made before the expiration of the period previously agreed upon.

(b) Notwithstanding § 58.1-3903, the assessing official shall assess local license tax omitted because of fraud or failure to apply for a license for the current license year and the six preceding license years.

(c) The period for collecting any local license tax shall not expire prior to a date two years after the date of the assessment, two years after the final determination of an administrative appeal pursuant to § 58.1-3980, or two years after the final decision in a court application pursuant to § 58.1-3984 or similar law, whichever is later.

COMMENT:

The ability to extend the period for assessing tax by agreement is similar to that used by the Department of Taxation pursuant to the provisions of § 58.1-101. The extra time to review audit issues with the taxpayer may reduce instances in which an assessment must be protested. Because § 58.1-3940 limits the period for collecting local taxes to five years, the collection period must be similarly extended when the period to assess is extended. The collections period is also extended for the period of time an assessment is being appealed to the assessing officer and Tax Commissioner as provided in subdivision 5 below. The six year assessment period for fraud or failure to file is similar to the period for state taxes under § 58.1-104.

(5.) Appeals and rulings.

(a) Any person assessed with a license tax as a result of an audit may apply within ninety days from the date of such assessment to the assessor for a correction of the assessment. The application must be filed in good faith and sufficiently identify the taxpayer, audit period, remedy sought, each alleged error in the assessment, the grounds upon which the taxpayer relies, and any other facts relevant to the taxpayer's contention. The assessor may hold a conference with the taxpayer if requested by the taxpayer, or require submission of additional information and documents, further audit, or other evidence deemed necessary for a proper and equitable determination of the application. The assessment shall be deemed prima facie correct. The assessor will undertake a full review of the taxpayer's claims and issue a determination to the taxpayer setting forth its position. Every assessment pursuant to an audit shall be accompanied by a written explanation of the taxpayer's right to seek correction and the specific procedure to be followed in the jurisdiction (e.g., the name and address to which an application should be directed).

(b) Provided a timely and complete application is made, collection activity shall be suspended until a final determination is issued by the assessor, unless the assessor determines that collection would be jeopardized by delay or that the taxpayer has not responded to a request for relevant information after a reasonable time. Interest shall accrue in accordance with the provisions of subdivision 2e of this subsection, but no further penalty shall be imposed while collection action is suspended. The term "jeopardized by delay" includes a finding that the application is frivolous, or that a taxpayer desires (i) to depart quickly from the locality, (ii) to remove his property therefrom, (iii) to conceal himself or his property therein, or (iv) to do any other act tending to prejudice or to render wholly or partially ineffectual proceedings to collect the tax for the period in question.

(c) Any person assessed with a license tax as a result of an audit may apply within ninety days of the determination by the assessing official on an application pursuant to subparagraph (a) above to the Tax Commissioner for a correction of such assessment. The Tax Commissioner shall issue a determination to the taxpayer within ninety days of receipt of the taxpayer's application, unless the taxpayer and the assessing official are notified that a longer period will be required. The application shall be treated as an application pursuant to § 58.1-1821 and the Tax Commissioner may issue an order correcting such assessment pursuant to § 58.1-1822. Following such an order either the taxpayer or the assessing official may apply to the appropriate circuit court pursuant to § 58.1-3984. However, the burden shall be on the party making the application to show that the ruling of the Tax Commissioner is erroneous. Neither the Tax Commissioner nor the Department

of Taxation shall be made a party to an application to correct an assessment merely because the Tax Commissioner has ruled on it.

(d) On receipt of a notice of intent to file an appeal to the Tax Commissioner under subparagraph (c) above, the assessing official shall further suspend collection activity until a final determination is issued by the Tax Commissioner, unless the assessor determines that collection would be jeopardized by delay or that the taxpayer has not responded to a request for relevant information after a reasonable time. Interest shall accrue in accordance with the provisions of subdivision 2e of this subsection, but no further penalty shall be imposed while collection action is suspended. The term "jeopardized by delay" shall have the same meaning as set forth in subparagraph (b) above.

(e) Any taxpayer may request a written ruling regarding the application of the tax to a specific situation from the assessor. Any person requesting such a ruling must provide all the relevant facts for the situation and may present a rationale for the basis of an interpretation of the law most favorable to the taxpayer. Any misrepresentation or change in the applicable law or the factual situation as presented in the ruling request shall invalidate any such ruling issued. A written ruling may be revoked or amended prospectively if (i) there is a change in the law, a court decision, or guidelines issued by the Department of Taxation upon which the ruling was based, or (ii) the assessor notifies the taxpayer of a change in the policy or interpretation upon which the ruling was based. However, any person who acts on a written ruling which later becomes invalid shall be deemed to have acted in good faith during the period in which such ruling is in effect.

COMMENT:

Provides a defined, mandatory local appeals process that generally tracks the state administrative procedures. Per the decision of the Joint Subcommittee on January 9, 1995, it also provides taxpayers the option of a further appeal to the State Tax Commissioner before proceeding to court (a concept supported by the business community). Localities generally are opposed to staying collections while an appeal is pending as taxpayers have an obligation to pay taxes and should not be allowed to defer payment. An advance ruling process is provided for. While a government cannot be bound by an erroneous ruling, the uniform ordinance attempts to provide as much certainty as possible for taxpayers. A new assessing official would be bound by rulings of his predecessor until prospective notice of a policy change is given.

(6.) Recordkeeping and audits.

Every person who is assessable with a license tax shall keep sufficient records to enable the assessor to verify the correctness of the tax paid for the license years assessable and to enable the assessor to ascertain what is the correct amount of tax that was assessable for each of those years. All such records, books of accounts and other information shall be open to inspection and examination by the assessor in order to allow the assessor to establish whether a particular receipt is directly attributable to the taxable privilege exercised within this jurisdiction. The assessor shall provide the taxpayer with the option to conduct the audit in the taxpayer's local business office, if the records are maintained there. In the event the records are maintained outside this jurisdiction copies of the appropriate books and records shall be sent to the assessor's office upon demand.

COMMENT:

Localities need access to the relevant gross receipts information when auditing a business, but the information may be kept at a central or regional office elsewhere and the localities have no travel expenses budgeted. Businesses are concerned with the expense of providing information related to their worldwide operations just to resolve a local tax issue for a small part of its operations.

B. Transitional provisions.

1. A locality which changes its license year from a fiscal year to a calendar year and adopts March 1 as the due date for license applications shall not be required to prorate any license tax to reflect a license year of less than 12 months, whether the tax is a flat amount or measured by gross receipts, provided that no change is made in the taxable year for measuring gross receipts.

2. The provisions of this section relating to penalties, interest, and administrative and judicial review of an assessment shall be applicable to assessments made on and after January 1, 1997, even if for an earlier license year. The provisions relating to agreements extending the period for assessing tax shall be effective for agreements entered into on and after July 1, 1995. The provisions permitting an assessment of license tax for up to six preceding years in certain circumstances shall not be construed to permit the assessment of tax for a license year beginning before January 1, 1997.

3. Every locality shall adopt a March 1 due date for applications no later than the 2001 license year.

COMMENT:

While there was consensus that a uniform due date was desirable, and March 1 would be acceptable, there were reservations by some localities. In large, automated localities the programming lead time and expense would be considerable. In smaller offices the flow of work is a consideration; staff resources may not be able to handle BPOL licenses at the same time that property tax bills must be prepared. Therefore, a long period is provided for localities to plan for the programming and workload changes. It is desired that localities change to the March 1 date as soon as feasible; in fact a number of localities in the Tidewater area are already anticipating such a change. However, any locality that changes its due dates will not be required to prorate tax because of the change.

§ 58.1-3706. Limitation on rate of license taxes.

A. Except as specifically provided in this section, no local license tax imposed pursuant to the provisions of this chapter, except §§ 58.1-3712, 58.1-3712.1 and 58.1-3713, or any other provision of this title or any charter, shall be ~~greater than thirty dollars~~ imposed on any person whose gross receipts from a licensable business, profession or occupation are $100,000 or less annually. Any business with gross receipts of more than $100,000, shall be subject to the tax at ~~or~~ the rate set forth below for the class of enterprise listed, ~~whichever is higher~~:

1. For contracting, and persons constructing for their own account for sale, sixteen cents per $100 of gross receipts;

2. For retail sales, twenty cents per $100 of gross receipts;

3. For financial, real estate and professional services, fifty-eight cents per $100 of gross receipts; and

4. For repair, personal and business services, and all other businesses and occupations not specifically listed or excepted in this section, thirty-six cents per $100 of gross receipts.

The rate limitations prescribed in this section shall not be applicable to license taxes on (i) wholesalers, which shall be governed by § 58.1-3716; (ii) public service companies, which shall be governed by § 58.1-3731; (iii) carnivals, circuses and speedways, which shall be governed by § 58.1-3728; (iv) fortune-tellers, which shall be governed by § 58.1-3726; (v) massage parlors; (vi) itinerant merchants

or peddlers, which shall be governed by § 58.1-3717; (vii) permanent coliseums, arenas, or auditoriums having a maximum capacity in excess of 10,000 persons and open to the public, which shall be governed by § 58.1-3729; (viii) savings and loan associations and credit unions, which shall be governed by § 58.1-3730; (ix) photographers, which shall be governed by § 58.1-3727; and (x) direct sellers, which shall be governed by § 58.1-3719.1.

B. Any county, city or town which had, on January 1, 1978, a license tax rate, for any of the categories listed in subsection A, higher than the maximum prescribed in subsection A may maintain a higher rate in such category, but no higher than the rate applicable on January 1, 1978, subject to the following conditions:

1. A locality may not increase a rate on any category which is at or above the maximum prescribed for such category in subsection A.

2. If a locality increases the rate on a category which is below the maximum, it shall apply all revenue generated by such increase to reduce the rate on a category or categories which are above such maximum.

3. A locality shall lower rates on categories which are above the maximums prescribed in subsection A for any tax year after 1982 if it receives more revenue in tax year 1981, or any tax year thereafter, than the revenue base for such year. The revenue base for tax year 1981 shall be the amount of revenue received from all categories in tax year 1980, plus one-third of the amount, if any, by which such revenue received in tax year 1981 exceeds the revenue received for tax year 1980. The revenue base for each tax year after 1981 shall be the revenue base of the preceding tax year plus one-third of the increase in the revenues of the subsequent tax year over the revenue base of the preceding tax year. If in any tax year the amount of revenues received from all categories exceeds the revenue base for such year, the rates shall be adjusted as follows: The revenues of those categories with rates at or below the maximum shall be subtracted from the revenue base for such year. The resulting amount shall be allocated to the category or categories with rates above the maximum in a manner determined by the locality, and divided by the gross receipts of such category for the tax year. The resulting rate or rates shall be applicable to such category or categories for the second tax year following the year whose revenue was used to make the calculation.

C. Any person engaged in the short-term rental business as defined in § 58.1-3510 shall be classified in the category of retail sales for license tax rate purposes.

D. 1. Any person, firm, or corporation designated as the principal or prime contractor receiving identifiable federal appropriations for research and development services as defined in § 31.205-18 (a) of the Federal Acquisition Regulation in the areas of (i) computer and electronic systems, (ii) computer software, (iii) applied sciences, (iv) economic and social sciences, and (v) electronic and physical sciences shall be subject to a license tax rate not to exceed three cents per $100 of such federal funds received in payment of such contracts upon documentation provided by such person, firm or corporation to the local commissioner of revenue or finance officer confirming the applicability of this subsection.

2. Any gross receipts properly reported to a Virginia locality, classified for license tax purposes by that locality in accordance with subdivision 1 of this subsection, and on which a license tax is due and paid, or which gross receipts defined by subdivision 1 of this subsection are properly reported to but exempted by a Virginia locality from taxation, shall not be subject to local license taxation by any other locality in the Commonwealth.

3. Notwithstanding the provisions of subsection D 1 above, in any county operating under the county manager plan of government, the following shall govern the taxation of the licensees described in subsection D 1. Persons, firms, or corporations designated as the principal or prime contractors receiving identifiable federal appropriations for research and development services as defined in § 31.205-18 (a) of the Federal Acquisition Regulation in the areas of (i) computer and electronic systems, (ii) computer software, (iii) applied sciences, (iv) economic and social sciences, and (v) electronic and physical sciences may be separately classified by any such county and subject to tax at a license tax rate not to exceed the limits set forth in subsections A through C above as to such federal funds received in payment of such

contracts upon documentation provided by such persons, firms, or corporations to the local commissioner of revenue or finance officer confirming the applicability of this subsection.

COMMENT:

At its January 9, 1995 meeting, the Joint Subcommittee adopted a proposal to eliminate the tax for businesses with gross receipts of $100,000 or less annually. In conjunction with this exemption, the subcommittee approved a flat license fee of $50 or less on such businesses (see § 58.1-3703). The $100,000 threshold may have a 2-4% revenue impact on some larger localities, but result in over 75% of small businesses being exempt from the tax; however, the revenue impact on smaller localities, especially towns, could be much greater. The Joint Subcommittee further indicated its support to hold harmless localities which lose 4% or more of their total revenue due to the $100,000 provision.

~~§ 58.1-3707. Situs for local license taxation of practitioners of professions.~~

~~A. The situs for the local license taxation of every practitioner of a profession which the Commonwealth regulates by law shall be the county, city or town in which such a practitioner maintains his office in this Commonwealth. If any such person maintains offices in more than one county, city or town in this Commonwealth, the county, city or town in which each office is located may impose a local license tax on him, but if such local license tax is measured by volume, the volume on which the tax may be computed shall be the volume attributable to practice in each county, city or town in which such an office is maintained.~~

~~B. If any practitioner of a profession which the Commonwealth regulates by law does not maintain any office in this Commonwealth, but does maintain a place of abode in this Commonwealth, and does practice such profession in the Commonwealth, the situs for the local license taxation of such a practitioner shall be the county, city or town in which such person maintains his place of abode.~~

~~C. If any practitioner of a profession which the Commonwealth regulates by law does not maintain an office or a place of abode in this Commonwealth, the situs of local license tax shall be each county, city or town in which he practices his profession.~~

~~D. The word *"volume,"* as used in this section, means gross receipts or any other base for measuring a license tax which is related to the amount of business done.~~

COMMENT:

Repealed so that the same situs rules will apply to both professions and businesses, in particular the elimination of "throwback" of untaxed gross receipts to be taxed in another jurisdiction. In City of Richmond v. Pollok, 218 Va. 693 (1978) the court upheld Richmond's tax on gross receipts attributable to an attorney's branch office in Fluvanna because Fluvanna did not impose a BPOL tax. This case was decided on January 13, 1978, and the 1978 General Assembly added language to § 58-266.4 which overturned Pollok. See 1978 Acts of Assembly, ch. 433. This language was omitted as "unnecessary" when recodified into § 58.1-3707. Therefore, the general rules in § 58.1-3708 and the situs and apportionment rules of the uniform ordinance do not permit a locality to tax gross receipts properly attributable to a definite place of business in another locality (or another state).

§ 58.1-3708. Situs for local license taxation of businesses, professions, occupations, etc.

A. Except as otherwise provided by law and except as to public service corporations, the situs for the local license taxation for any licensable business, profession, trade, occupation or calling, shall be the county, city or town (hereinafter called "locality") in which the person so engaged has a definite place of business ~~or maintains his office~~. If any such person has a definite place of business ~~or maintains an office~~

in any other locality, then such other locality may impose a license tax on him, provided such other locality is otherwise authorized to impose a local license tax with respect thereto.

B. Where a local license tax imposed by any ~~such other~~ locality is measured by volume, the volume on which the tax may be computed shall be the volume attributable to all definite places of business of the business, profession, trade, occupation or calling in such ~~other~~ locality. All volume attributable to any definite places of business of the business, profession, trade, occupation or calling in any ~~such~~ other locality ~~which levies a local license tax thereon~~ shall be deductible from the base in computing any local license tax measured by volume imposed on him by the locality in which the first-mentioned definite place ~~or office~~ is located.

~~C. If any such person has no definite place of business or office within the Commonwealth, the situs for the local license taxation of such a person shall be each locality in which he engages in such business, trade, occupation or calling, with respect to what is done in each such locality.~~

D. The word *"volume,"* as used in this section, means gross receipts, sales, purchases, or other base for measuring a license tax which is related to the amount of business done.

E. This section shall not be construed as prohibiting any locality from requiring a separate license for each definite place of business ~~or each office~~ located in such locality.

~~F. Where a local license tax, or any portion thereof, is measured other than by volume, the tax, or such portion, shall first be computed for each locality as if the entire business were done within such locality and the amount so determined shall be multiplied by a fraction, the numerator of which is the volume of business done in such locality and the denominator of which is the volume of business done in this Commonwealth.~~

COMMENT:

The repeal of § 58.1-3707 makes professions subject to the same situs rules as other businesses. It will overturn City of Richmond v. Pollok, 218 Va. 693, 239 S.E.2d 915 (1978) which allowed the City of Richmond to levy the tax an attorney's total gross receipts (including those attributable to the attorney's branch office in Fluvanna County) since Fluvanna County had no tax based on gross receipts. Several localities were concerned about the revenue loss from eliminating this practice and the perceived equities of favoring a business located in a county without a BPOL tax that competes with similar businesses located in cities that have the tax. This draft recognizes that businesses are free to establish locations where they choose (subject to zoning restrictions), and taxes are a legitimate factor in the location decision.

Paragraphs A and B of § 58.1-3708 are amended to apply to both professions and other types of businesses. Paragraph C is repealed, and B amended to ensure that a locality taxes only receipts attributable to a definite place of business in that locality without regard to whether some other locality taxes the business. Paragraph F is repealed because license taxes will either be a flat amount or measured by gross receipts or purchases. References to an "office" are deleted because the definition of a "definite place of business" includes offices.

~~§ 58.1-3725. Collection agencies.~~

~~For purposes of the license tax authorized in § 58.1-3703, any person, firm or corporation whose business it is to collect claims, including notes, drafts and other negotiable instruments, on behalf of others, and to render an account of the same shall be deemed a collection agency. This section shall not apply, however, to a regularly licensed attorney-at-law.~~

~~No local license hereunder shall be issued to any person desiring to act as a collection agent or agency in the Commonwealth unless such person exhibits a current license or other evidence showing that~~

~~the applicant has been duly licensed to act as a collection agent or agency by the Virginia Collection Agency Board.~~

COMMENT:

Obsolete provision -- the Virginia Collection Agency Board was abolished many years ago. Collection agencies are taxed like any other business service (36¢ per $100 rate cap).

§ 58.1-3732. ~~Limitation on~~ Exclusions and deductions from "gross receipts."

A. Gross receipts for license tax purposes shall not include any amount not derived from the exercise of the licensed privilege to engage in a business or profession in the ordinary course of business.

The following items are excluded:

(i) amounts received and paid to the United States, the Commonwealth or any county, city or town for the Virginia retail sales or use tax, for any local sales tax or any local excise tax on cigarettes, for any federal or state excise taxes on motor fuels ~~, or~~ ;

(ii) any amount representing the liquidation of a debt or conversion of another asset to the extent that the amount is attributable to a transaction previously taxed (e.g., the factoring of accounts receivable created by sales which have been included in taxable receipts even though the creation of such debt and factoring are a regular part of its business);

(iii) any amount representing returns and allowances granted by the business to its customer;

(iv) receipts which are the proceeds of a loan transaction in which the licensee is the obligor;

(v) receipts representing the return of principal of a loan transaction in which the licensee is the creditor, or the return of principal or basis upon the sale of a capital asset;

(vi) rebates and discounts taken or received on account of purchases by the licensee. A rebate or other incentive offered to induce the recipient to purchase certain goods or services from a person other than the offeror, and which the recipient assigns to the licensee in consideration of the sale goods and services shall not be considered a rebate or discount to the licensee, but shall be included in the licensee's gross receipts together with any handling or other fees related to the incentive.

(vii) withdrawals from inventory for which no consideration is received and the occasional sale or exchange of assets other than inventory whether or not gain or loss is recognized for federal income tax purposes.

(viii) investment income not directly related to the privilege exercised by a licensable business not classified as rendering financial services. This exclusion shall apply to interest on bank accounts of the business, and to interest, dividends and other income derived from the investment of its own funds in securities and other types of investments unrelated to the licensed privilege. This exclusion shall not apply to interest, late fees and similar income attributable to an installment sale or other transaction that occurred in the regular course of business.

B. The following shall be deducted from gross receipts that would otherwise be taxable:

(i) any amount paid for computer hardware and software that are sold to a United States federal or state government entity provided that such property was purchased within two years of the sale to said entity by the original purchaser who shall have been contractually obligated at the time of purchase to resell such property to a state or federal government entity. This ~~exclusion~~ deduction shall not occur until the time of resale and shall apply to only the original cost of the property and not to its resale price, and the ~~exclusion~~ deduction shall not apply to any of the tangible personal property which was the subject of the original resale contract if it is not resold to a state or federal government entity in accordance with the original contract obligation.

(ii) any receipts attributable to activities conducted in another state or foreign country in which the taxpayer is liable for an income or other tax based upon income.

COMMENT:

This section is broken into two subsections to distinguish between items excluded because they are not receipts that should be taxable, and deductions from otherwise taxable receipts. While there was general consensus that the tax should be restricted to receipts arising from the exercise of the licensed privilege, there does not appear to be a consensus as to how to identify those receipts. Consideration was given to incorporating an "ordinary course of business" standard during Advisory Committee deliberations. However, local governments expressed concern that such a standard may give too much weight to how narrow a "business" someone advertises and how "ordinary" should be defined. Would a retailer who advertises only plain widgets be justified in classifying the sale of a blue widget as not being in the regular course of business? The Joint Subcommittee decided at its January 9, 1995 meeting to incorporate an "ordinary course of business" standard in the exclusion section so that it would not be necessary to provide an exhaustive list of exclusions. Further explanation and examples of this fact driven issue will be provided in the BPOL Guidelines.

There was general agreement that returns, allowances and returns of principal were not taxable gross receipts. While discounts on purchases would not be gross receipts, manufacturer's rebates and coupons offered to consumers and redeemed at a retailer would be gross receipts to the retailer.

Subsection (vii) addresses situations in which a withdrawal from inventory for personal use may create income tax consequences under the tax benefit rule (converting to personal use an item previously deducted for federal income tax purposes). For gross receipts tax purposes, a licensee cannot create taxable gross receipts by dealing with himself. An unresolved issue involves inventory swaps, such as an automobile dealer who exchanges cars with another dealer to supply a customer. While localities agreed that such swaps should not be taxable, language could not be agreed upon that would prevent potential abuse. It can be argued that such a swap is not a retail sale but an exchange at wholesale of property for resale. Because the transaction would merely be ancillary to a retail sale, such transactions would not constitute a separate licensable wholesale business. The occasional sale of assets would not be taxable--this is close to a "ordinary course of business" standard. A suggestion to incorporate federal non-recognition provisions (e.g., for like-kind exchanges) was not adopted because the occasional sale exclusion should cover most such instances.

It was generally agreed that funds received in a true fiduciary capacity, such as a trustee, are not taxable gross receipts. Examples of fiduciary capacity will be provided in the BPOL Guidelines. There was concern that language incorporating a fiduciary exclusion would become a loophole for businesses to structure transactions for tax avoidance purposes.

Subsection (viii) expands on the concept of income that is not related to the licensed privilege. Investment income is earned merely from the ownership of capital, not from the conduct of a business. However, it can be difficult to distinguish between some types of income, such as interest, that may arise from a transaction in the ordinary course of business or merely from the passive ownership of an investment. Localities were concerned that the allowance of such an exclusion may lead to a significant revenue loss.

New subsection B. incorporates a deduction for certain government contractors that is in existing law. A major unresolved issue relates to a government contractor's reimbursables, as well as subcontractors generally. A contractor and his subcontractors are separate, independent businesses and each is liable for BPOL tax on his own gross receipts. The controversy arises from the fact that the prime contractor is allowed no deduction for amounts paid to the subcontractor or to any other supplier. Some government contracts require the contractor to supply equipment at cost with no markup or profit. The reimbursement for such equipment is a taxable gross receipt even though no profit is possible on the transaction (although the whole contract may be profitable). Localities were concerned that any deduction for a contract expense would change the nature of the tax to an income tax and might cause a far greater revenue loss than anticipated. See § 58.1-3706 D. for an example of how complex a special deduction, exemption, or classification for government contractors can be.

At its January 9, 1995 meeting, the Joint Subcommittee also adopted a deduction that effectively exempts all receipts that are subject to income tax in other states. This is contrary to the concept of a privilege tax, which generally looks to the place where the privilege was exercised rather than the destination of the goods. Localities are extremely concerned about such a provision, especially larger localities who contend it could cause significant revenue losses. The business community would prefer to exempt all gross receipts which have any connection with activity in other states. The provision, however, only exempts receipts when the activity in the other state has resulted in an actual income tax liability to the other state or foreign country. The apportionment of receipts attributable to activities within Virginia will not be affected. Nor does the provision allow for a deduction for a business which has its only office in Virginia and its contacts with other states is not sufficient to allow any other state to impose an income tax.

2. That §§ 58.1-3707 and 58.1-3725 of the Code of Virginia are repealed.

3. That the transitional provisions of § 58.1-3703.1 B shall be effective as stated in such subsection.

4. That the remaining provisions of this act, including the repeal of §§ 58.1-3707 and 58.1-3725, shall be effective for license years beginning on and after January 1, 1997, but any provision, except the imposition of a license fee pursuant to § 58.1-3703, may, at the locality's election, be adopted and applied to an earlier license year.

COMMENT:

This act, together with the revised BPOL Guidelines to be issued July 1, 1995, make some substantial changes to the revenue in some localities, and to the administrative procedures in almost all localities currently imposing the tax. In addition to affecting tax revenue of certain localities, there may be some significant costs in other localities. Large localities with automated offices would incur significant programming costs. Small localities with small staffs may find that changes must be made during peak workloads for other tax types, such as assessing and billing property taxes. Localities have indicated concern that six months is not sufficient time for over 100 counties, cities, and towns to review the changes made by this act and the new BPOL Guidelines, draft, advertise and adopt new ordinances. Localities are particularly concerned with any impact on their FY96 budgets because they will generally be finalized early in 1995, in many cases before this legislation can be enacted. At that time the property tax rates are also fixed, which severely limits the ability of localities to deal with a significant revenue loss or a significant increase in administrative costs.

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Appendix D
House Joint Resolution No. 613 (1995)

1995 SESSION
ENGROSSED

LD9729136

HOUSE JOINT RESOLUTION NO. 613

House Amendments in { } -- February 4, 1995

Continuing the joint subcommittee studying the business, professional, and occupational license tax.

Patrons--Brickley, Albo, Almand, Croshaw, Diamonstein, Dillard, Harris, Parrish, Plum, Puller, Purkey, Scott and Van Landingham; Senators: Calhoun and Colgan

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Referred to Committee on Rules

WHEREAS, the business, professional, and occupational license (BPOL) tax has been studied for the past two years by a joint subcommittee established by House Joint Resolution No. 526 in 1993 and continued by House Joint Resolution No. 110 in 1994; and

WHEREAS, the joint subcommittee appointed an advisory committee consisting of representatives from the business community and local government; and

WHEREAS, the advisory committee worked closely with the Department of Taxation to develop a model BPOL ordinance to be used by local government throughout the Commonwealth; and

WHEREAS, the joint subcommittee adopted the model ordinance and proposed legislation for the 1995 General Assembly Session incorporating such ordinance; and

WHEREAS, the joint subcommittee agreed that eliminating the BPOL tax in the future should be studied further; now, therefore, be it

RESOLVED by the House of Delegates, the Senate concurring, That the Joint Subcommittee Studying the BPOL Tax be continued for a third year in order to examine existing local revenue resources, the economic impact eliminating the BPOL tax would have on localities, and if and how the tax could be eliminated over time while holding the local governments harmless.

The joint subcommittee shall { ~~complete its work in time to submit its~~ be continued for one year only and shall submit its final } findings and recommendations, if any, to the Governor and the 1996 Session of the General Assembly as provided in the procedures of the Division of Legislative Automated Systems for the processing of legislative documents.

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