

Review of General Fund Revenues and the Virginia Economy for Fiscal Year 2018

*A presentation to the Senate Finance,
House Appropriations and House Finance
Committees*

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Aubrey L. Layne, Jr., MBA, CPA
Secretary of Finance
Commonwealth of Virginia
www.finance.virginia.gov

Overview

Fiscal Year 2018 Year-in-Review

- Economic Performance
- Actual General Fund Collections
- Actual Commonwealth Transportation Fund Collections
- Financial Results Balance Sheet
- Revenue Stabilization Fund Balance

Looking Forward

- July 2018 General Fund Collections
- Fall Forecasting Process
- Tax Conformity for 2018
- Internet Sales Tax

Fiscal Year 2018 - U.S. Economy Performed Near Expectations, While Virginia's Economic Performance Was Slightly Below Projections

- As measured on a fiscal year basis (July through June), estimated real GDP increased 2.7 percent, slightly above the forecast, while nationally, personal income and wages and salaries were close to expectations.
- In Virginia, growth in employment, personal income, and wages and salaries were below the forecast based on available data.

Summary of Key U.S. and Virginia Economic Indicators Percent Change Over the Prior Fiscal Year

	FY17 <u>Actual</u>	FY18 <u>Forecast</u>	FY18 <u>Actual</u>
<u>U.S.</u>			
Real GDP	1.9	2.4	2.7
Consumer Spending	2.8	2.5	2.6
Employment	1.7	1.4	1.5
Personal Income	2.5	3.5	3.6
Wages & Salaries	2.7	4.1	4.2
<u>Virginia</u>			
Employment	1.0	1.3	0.9
Professional/Business	1.6	2.6	1.7
Construction/Mining	1.7	1.9	3.4
Education/Health	1.1	2.0	1.1
Government	0.5	0.4	0.0
Personal Income*	2.4	3.3	2.9
Wages & Salaries*	2.7	3.6	3.0

* FY17 Actual data is based on the first 3 quarters of the fiscal year. Fourth quarter data will be released in the fall and expectations are for continuing improvement based on withholding receipts.

Including Transfers, Fiscal Year 2018 General Fund Resources Grew 6.0 Percent and Finished \$555.5 Million (2.8 Percent) Above Forecast

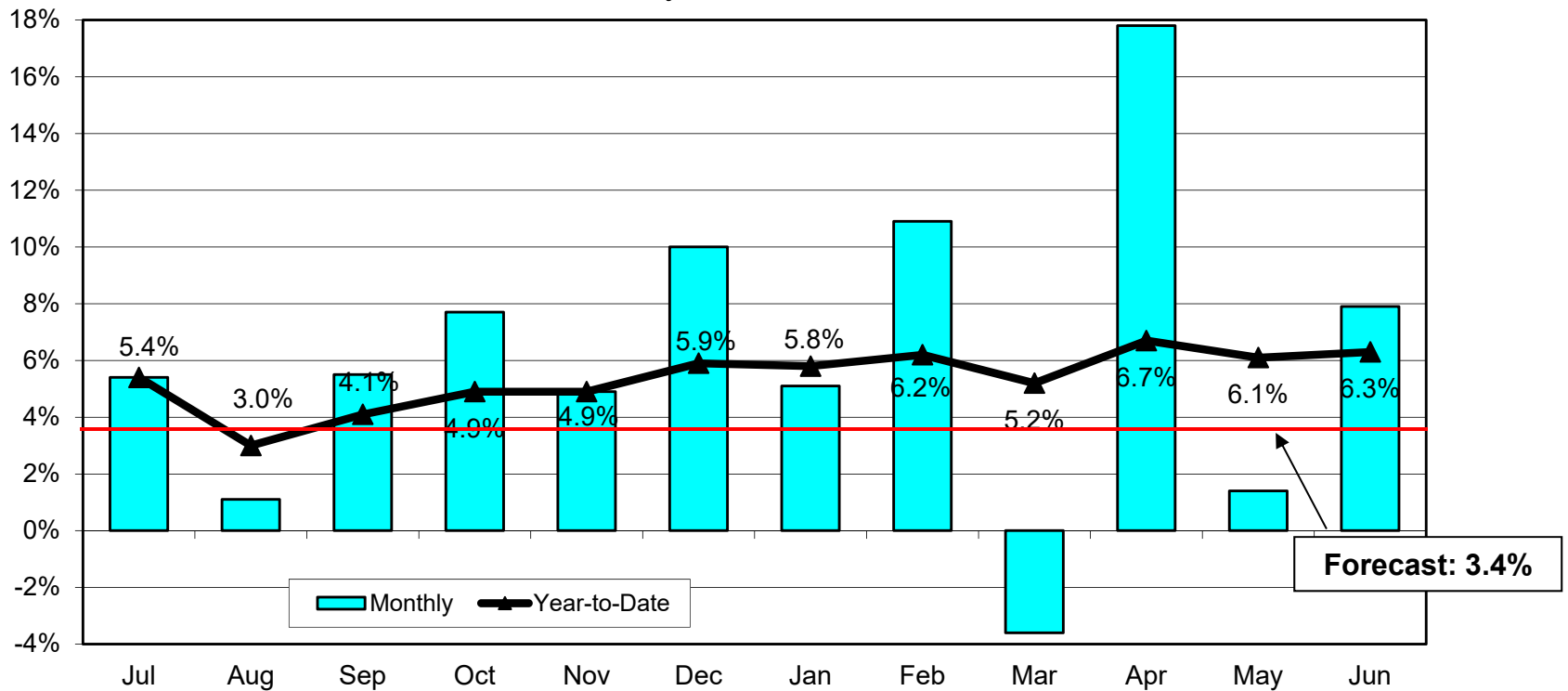
Summary of Fiscal Year 2018 Revenue Collections (millions of dollars)

Major Sources	As a % of Total General Fund				% Growth Over FY 17	
		Official	Actual	Change	Official	Actual
Withholding	61.5%	\$12,313.3	\$12,540.5	\$227.2	3.5 %	5.4 %
Nonwithholding	15.6	3,147.3	3,472.9	325.6	4.3	15.1
Refunds	(9.6)	(1,968.7)	(1,907.6)	61.1	5.8	2.5
Net Individual	67.5%	\$13,491.9	\$14,105.8	\$613.9	3.4 %	8.1 %
Sales	17.4%	\$3,458.2	\$3,461.8	\$3.6	3.0 %	3.1 %
Corporate	4.3	874.0	861.9	(12.1)	5.7	4.2
Wills (Recordation)	2.0	407.2	394.9	(12.3)	3.3	0.1
Insurance	1.8	362.1	337.9	(24.2)	6.2	(0.9)
All Other Revenue	3.7	734.8	718.5	(16.3)	1.6	(0.6)
Total Revenue	96.6%	\$19,328.2	\$19,880.8	\$552.6	3.4 %	6.3 %
A.B.C. Profits	0.6	\$104.1	\$109.5	\$5.4	(5.8) %	(0.9) %
Sales Tax (0.375%)	1.9	379.1	376.6	(2.5)	3.6	2.9
Transfers	0.9	142.1	142.2	0.1	(19.7)	(19.6)
Total Transfers	3.4%	\$625.3	\$628.3	\$3.0	(4.3) %	(3.8) %
TOTAL GENERAL FUND	100.0%	\$19,953.5	\$20,509.0	\$555.5	3.1 %	6.0 %

- The gain in net individual income tax and sales tax, about \$618 million, was somewhat offset by shortfalls in all other revenue sources.

Fiscal Year 2018 General Fund Revenue Grew at an Average Pace of 6.3 Percent

Growth in Total General Fund Revenue Collections FY18 Monthly and Year-to-Date

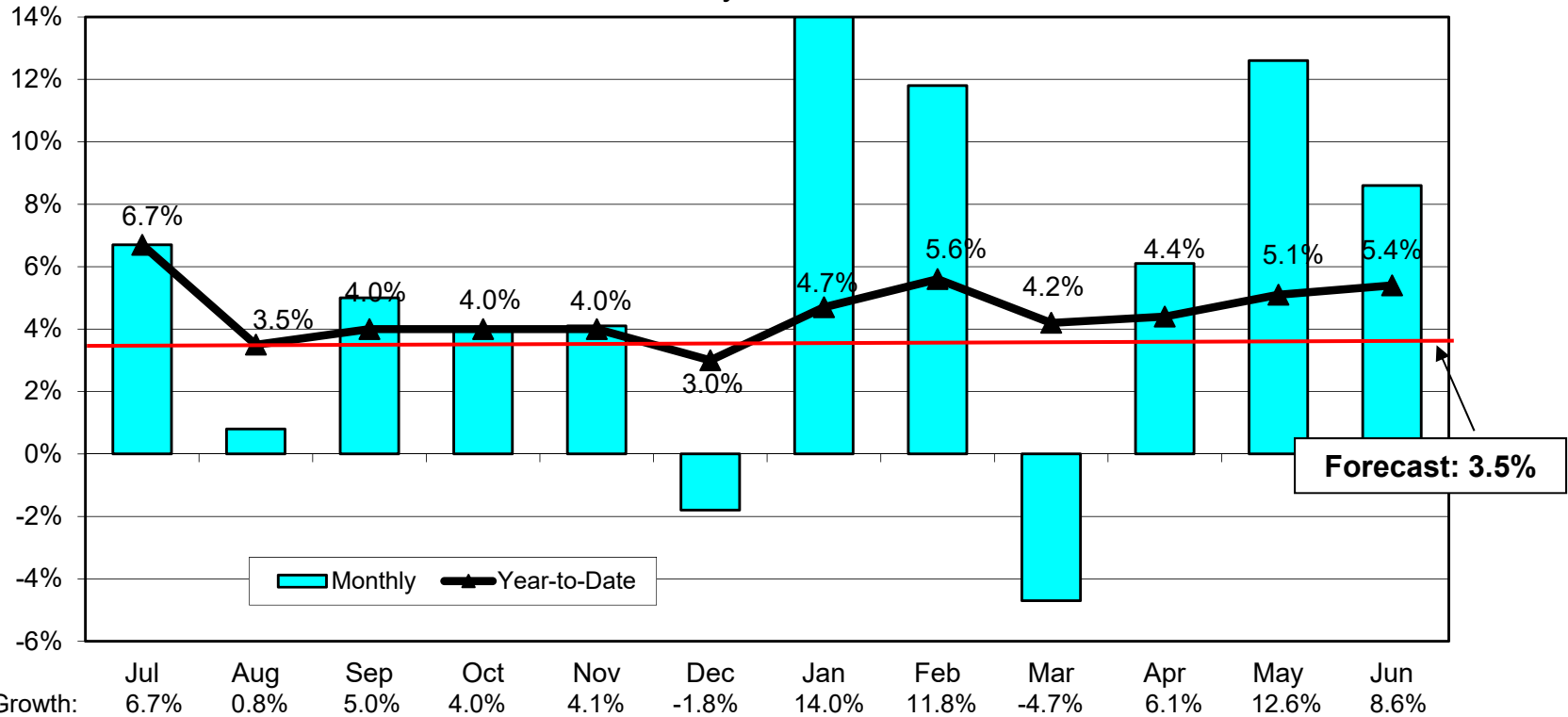


Monthly Growth: 5.4% 1.1% 5.5% 7.7% 4.9% 10.0% 5.1% 10.9% -3.5% 17.8% 1.4% 7.9%

- Total general fund revenue collections exceeded the forecast by \$552.6 million, excluding transfers in fiscal year 2018, a forecast variance of 2.9 percent.
- Total general fund revenues rose 6.3 percent, ahead of the annual forecast of 3.4 percent.

Payroll Withholding Tax Collections Exceeded the Annual Estimate by \$227.2 Million (1.8 percent) in Fiscal Year 2018

Growth in Withholding Tax Collections FY18 Monthly and Year-to-Date



- Collections of payroll withholding taxes, 63 percent of total general fund revenues, grew 5.4 percent, above the annual estimate of 3.5 percent. However, payments in June were inflated due to timing of year-end payments from some employers.
 - About \$120 million.
- Both employment and wage and salary gains are the drivers of this source.

Acceleration in Withholding Was Broad-based and Included Strong Growth in Large and Small Businesses

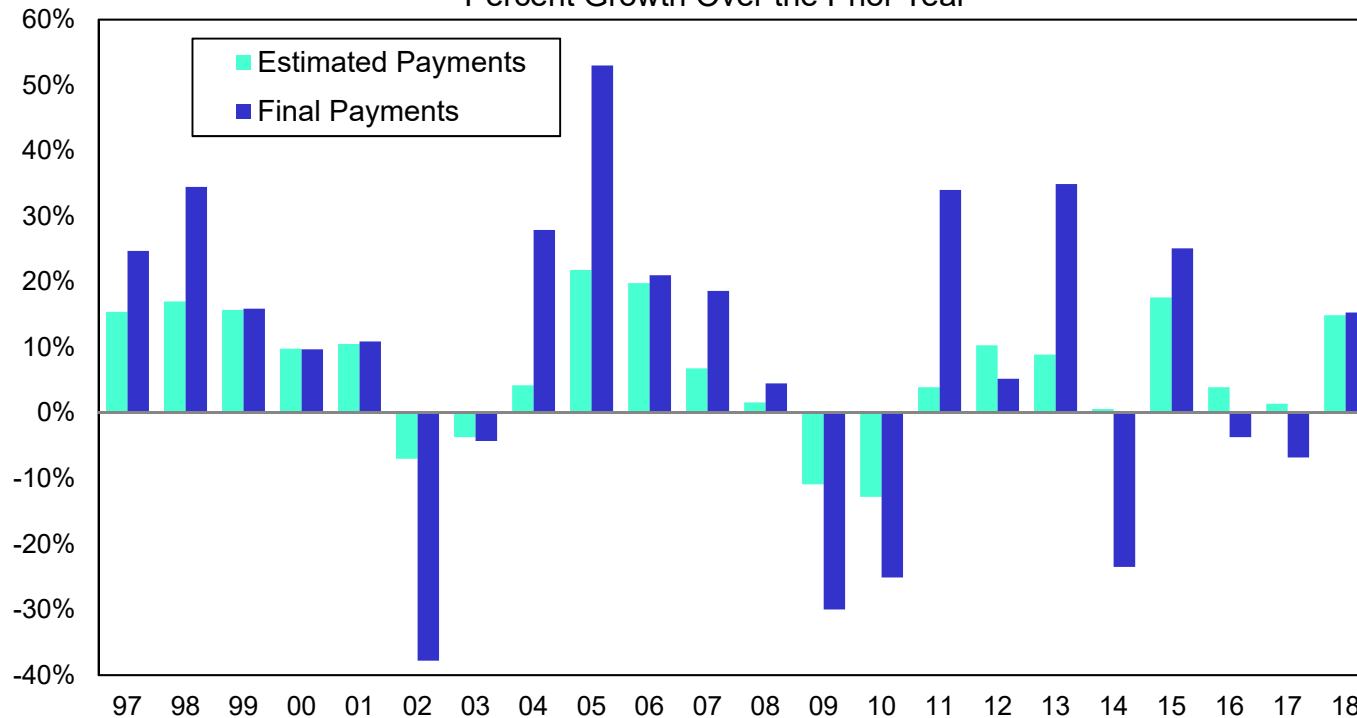
Withholding Tax Collections Fiscal Years 2016 - 2018 millions of dollars

Industry (% of Total \$ Amount)	# of Firms in FY16	Millions of Dollars		Percent Change		
		FY17	FY18	FY16	FY17	FY18
Public Sector (17%)	100	\$2,095.5	\$2,178.4	2.9%	3.0%	4.0%
Education and Health Services (8%)	300	\$965.9	\$1,011.8	6.1%	7.5%	4.8%
Federal Contractors (4%)	244	\$467.3	\$478.3	-1.9%	-2.0%	2.4%
Finance (3%)	170	\$379.7	\$412.9	6.7%	6.3%	8.7%
Professional and Business Services (3%)	719	\$390.9	\$403.1	5.9%	5.5%	3.1%
Investment (2%)	224	\$270.6	\$297.1	7.1%	9.7%	9.8%
Manufacturing (1%)	232	\$164.1	\$182.4	0.5%	-6.7%	11.2%
Transportation (1%)	59	\$137.1	\$144.2	2.5%	7.0%	5.2%
Housing (1%)	188	\$106.7	\$122.4	14.7%	2.4%	14.7%
Other (4%)	681	\$504.3	\$529.0	-9.4%	2.6%	4.9%
Total Large Payers (46%)	2,917	\$5,482.0	\$5,759.8	2.5%	3.7%	5.1%
Total Small Payers (54%)	221,588	\$6,413.4	\$6,780.7	2.3%	6.5%	5.7%
Total All	224,505	\$11,895.4	\$12,540.5	2.4%	5.2%	5.4%

Large Payers Include Payments in Excess of \$100,000

Individual Income Tax Nonwithholding Collections Were \$325.6 Million (10.3 Percent) Ahead of the Annual Estimate in Fiscal Year 2018

Growth in Estimated and Final Payments, FY97 - FY18
Percent Growth Over the Prior Year



- Collections of nonwithholding, 16 percent of total revenues and one of the most volatile revenue sources, were significantly ahead of expectations, due predominately to the timing of payments related to federal tax changes.
- Total nonwithholding collections grew 15.1 percent in fiscal year 2018 compared with the annual estimate of a 4.3 percent increase.
- The estimate included reducing forecasted collections by \$193 million for the nonwithholding collar. The nonwithholding collar is the 10 year average of nonwithholding payments as a percent of total revenues (16.15%), limited to 1 percent of general fund revenues.

Analysis of High-Net-Worth Individuals

- **In December and January:**

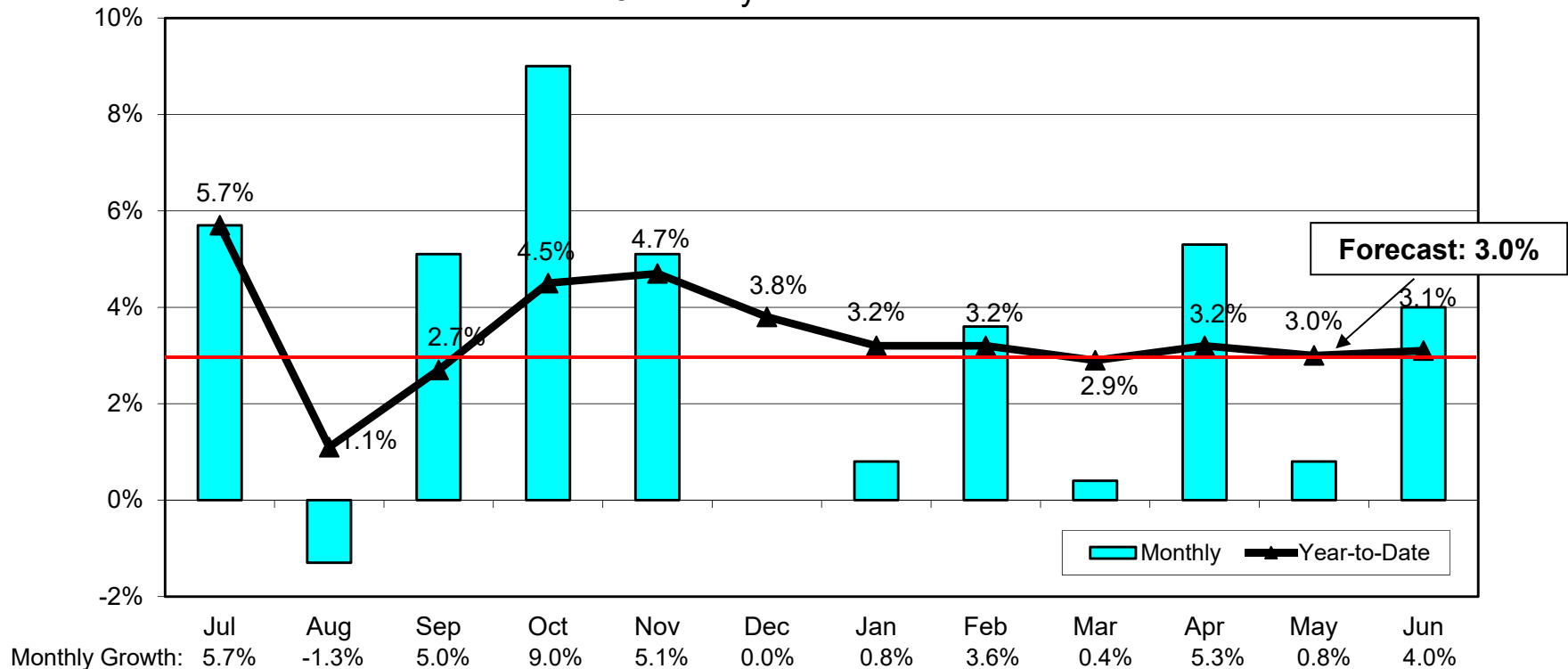
- 781 high-income taxpayers (more than \$1.7 million in taxable income) submitted \$297 million in payments
- This compares to the average of the last three years where 423 high-income taxpayers submitted \$162 million.
 - Previous peaks in payments were in FY07 and FY08 where an average of 478 high-income taxpayers submitted \$177 million.

- **From April 1 through July 31:**

- 54 have filed returns and requested \$2.9 million in refunds
- 59 have filed returns and applied \$2.4 million to tax year 2018
- 45 have filed returns and paid an additional \$2.0 million in taxes
- 203 have paid \$41.8 million via extension returns and have until November 1 to file returns
- The remaining 420 have had no additional activity and have a six-month automatic extension to file their returns by November 1, 2018.

Total Sales Tax Collections Slightly Exceeded the Annual Estimate Advancing 3.1 Percent – Above the Estimate by \$3.6 Million (0.1 Percent) in Fiscal Year 2018

Growth in Sales Tax Collections
FY18 Monthly and Year-to-Date



- On a year-to-date basis, collections increased 3.1 percent, ahead of the annual estimate of 3.0 percent growth.
- Sales tax collections posted the strongest growth in the last 3 years -- with growth below 2 percent in each of the last two fiscal years.

Other Revenue Sources Were Slightly Below Their Respective Forecasts in Fiscal Year 2018

Corporate Income Tax

- Corporate income tax collections fell short of its forecast by \$12.1 million (1.4 percent), advancing 4.2 percent.

Wills, Suits, Deeds, and Contracts (Recordation Tax)

- Wills, Suits, Deeds, and Contracts (primarily recordation tax collections) finished \$12.3 million behind the annual forecast (3.0 percent), advancing only 0.1 percent.

Insurance Premiums Tax

- Insurance premiums tax collections fell short of the annual estimate by \$24.2 million (6.7 percent), falling 0.9 percent.
 - Prior year Historic Rehab Tax Credits resulted in over \$20 million in refunds.

Commonwealth Transportation Fund (CTF) Revenues Finished Fiscal Year 2018 \$12.3 Million Below the Official Forecast

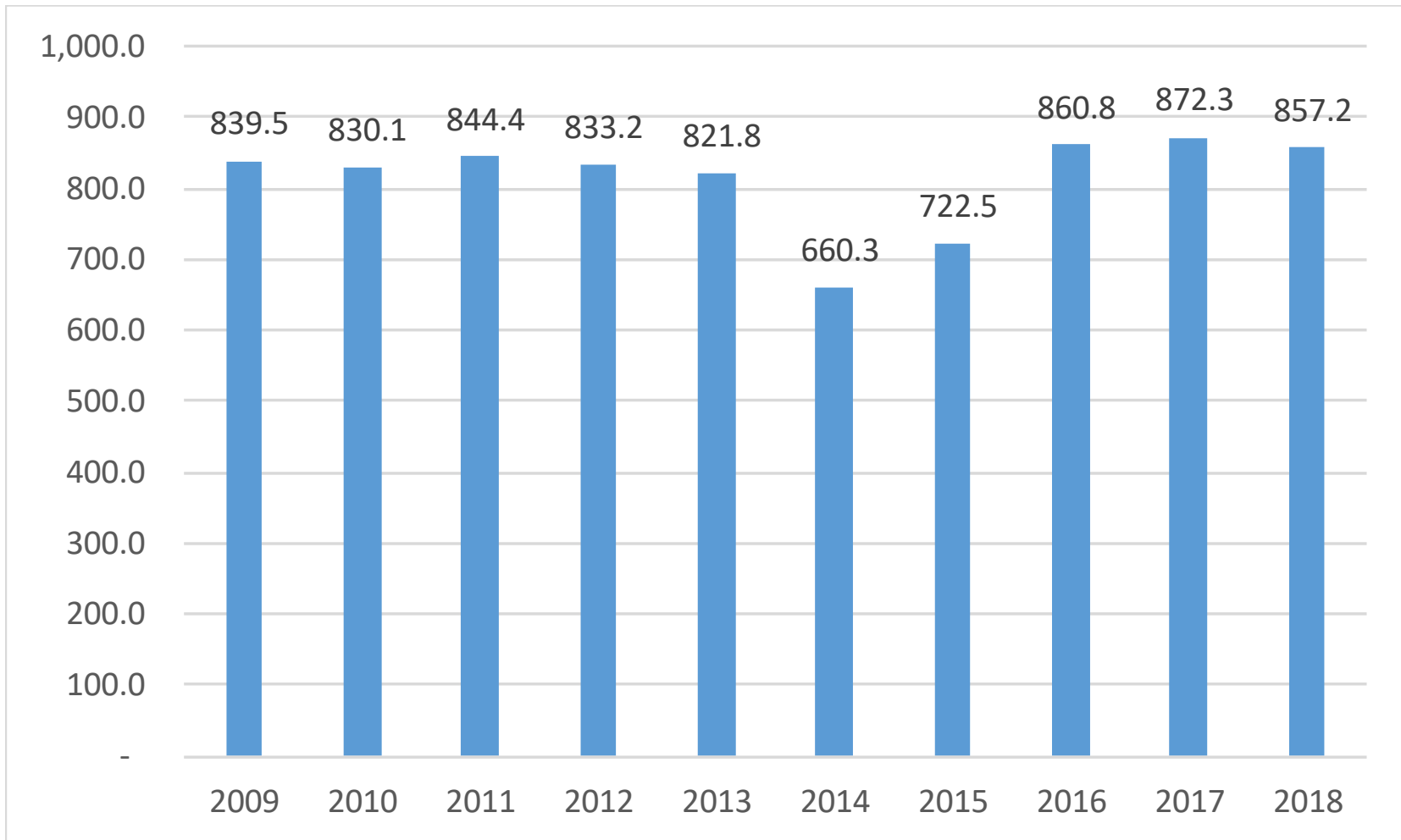
Actual Collections Compared to the Official Forecast for Fiscal Year 2018
(Millions of Dollars)

Revenue Sources	FY2017 Actual	FY2018 Actual	FY2018 Forecast	Percent Change 2017-2018		Forecast Variance	
				Actual	Forecast	Amount	Percent
Motor Fuels Tax	857.9	843.5	886.3	-1.7%	3.3%	(42.8)	-4.8%
Road Use Tax	12.3	11.7	10.5	(4.9)	(14.6)	1.2	11.4
Vehicle Sales Tax	957.7	943.6	922.4	(1.5)	(3.7)	21.2	2.3
Vehicle Licenses	260.2	258.8	259.2	(0.5)	(0.4)	(0.4)	(0.2)
State Sales Tax	1,020.4	1,043.8	1,047.0	2.3	2.6	(3.2)	(0.3)
Recordation Tax	48.1	47.8	48.3	(0.6)	0.4	(0.5)	(1.0)
Insurance Premiums Tax	163.1	168.0	168.0	3.0	3.0	0.0	0.0
Int'l Registration Plan	66.2	69.2	64.4	4.5	(2.7)	4.8	7.5
Interest Earnings	6.4	8.9	3.3	39.1	(48.4)	5.6	169.7
Rental Tax	39.5	40.2	40.9	1.8	3.5	(0.7)	(1.7)
Aviation Fuels Tax	2.0	2.0	1.9	0.0	(5.0)	0.1	5.3
Miscellaneous	18.4	19.6	17.2	6.5	(6.5)	2.4	14.0
TOTAL	\$3,452.2	\$3,457.1	\$3,469.4	0.1%	0.5%	(\$12.3)	-0.4%

- Total revenue growth was below target with a 0.4 percent forecast variance.
 - The forecast variance was due to slower than expected growth in motor fuels tax collections.

Total Virginia Motor Fuels Tax Collections

million of dollars



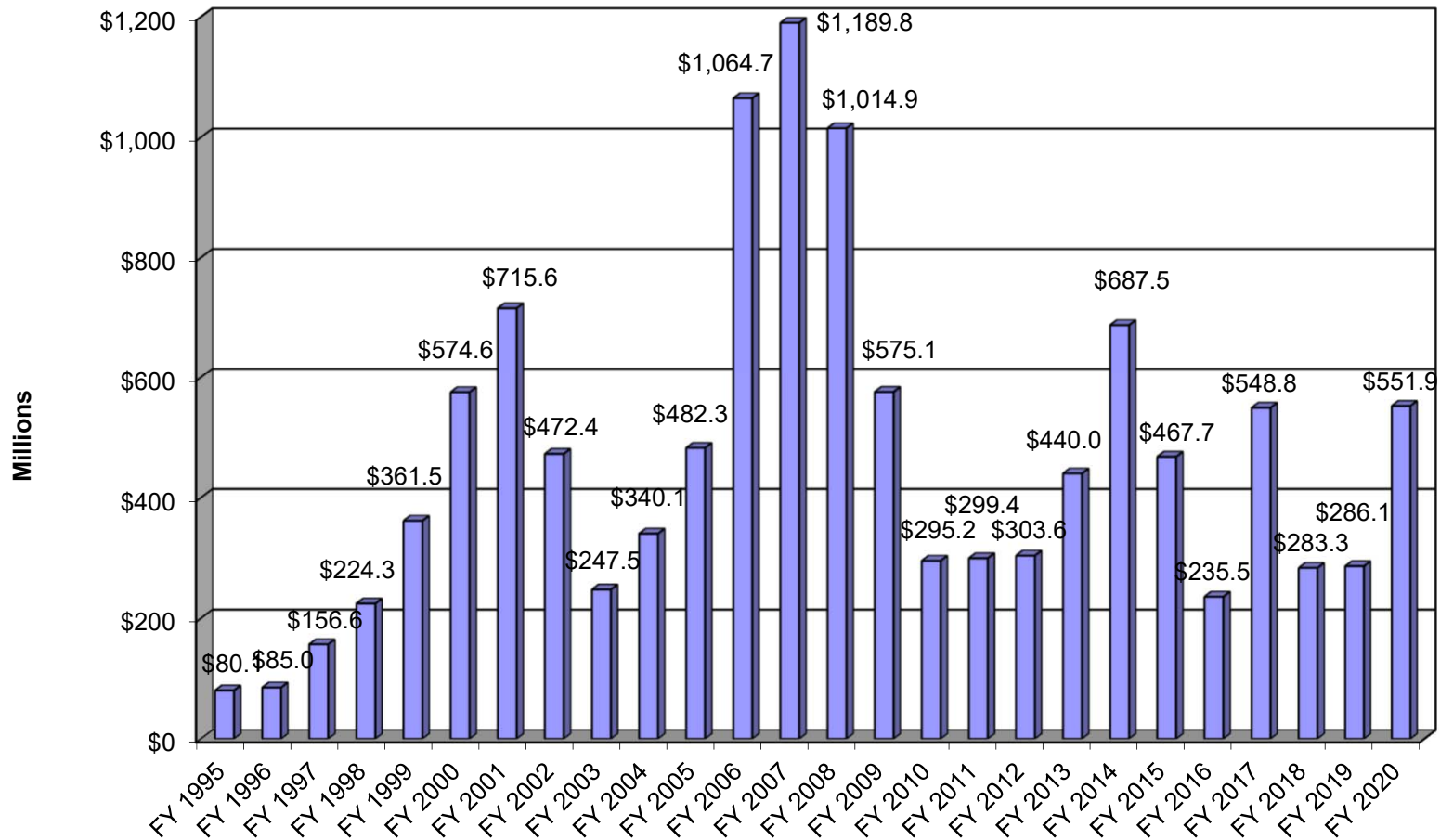
FY 2018 Revenue Surplus Is Allocated to the Revenue Stabilization, Water Quality A, and the Revenue Reserve

Preliminary Balance Sheet
General Fund - Cash Basis (Unaudited)
June 30, 2018
(Dollars in Thousands)

Assets		
Cash, Cash Equivalents, and Investments	\$ 1,890,814	
Cash and Travel Advances	483	
Other Assets	180	
Due From Other Funds	75	
Total Assets		<u>\$ 1,891,552</u>
Liabilities and Fund Equity		
Liabilities:		
Payments Awaiting Disbursement	92,931	
Deposits Pending Distribution	4,765	
Due To Other Funds	6,892	
Total Liabilities		\$ 104,588
Fund Equity:		
Restricted Fund Balance:		
Revenue Stabilization Fund as of June 30, 2018	283,275	
Revenue Stabilization Fund Deposit in FY 2020 from FY 2018 Surplus	262,941	
Lottery Proceeds Fund	7,675	
Water Supply Assistance Grant Fund	3,132	
Total Restricted Fund Balance		<u>557,023</u>
Committed and Assigned Fund Balance:		
Reappropriation of FY 2018 Unexpended Balances for Capital Outlay	7,274	
Virginia Health Care Fund	30,217	
Central Capital Planning Fund	2,773	
Communication Sales and Use Tax	34,002	
Commonwealth's Development Opportunity Fund	27,384	
Natural Disaster Sum Sufficient	17,070	
Amount Required for Mandatory Reappropriation	76,959	
Virginia Water Quality Improvement Fund	19,251	
Virginia Water Quality Improvement Fund - Part A	55,259	
Virginia Water Quality Improvement Fund - Part B	18,499	
Revenue Cash Reserve Fund	156,439	
Revenue Cash Reserve FY 2019 Deposit from FY 2018 Surplus	234,392	
Local Government Fiscal Distress	500	
Transportation Trust Fund	1,671	
Nonrecurring Expenditures	836	
Amount Required by Chapter 2	212,161	
Amount Required for Discretionary Reappropriations	163,980	
Nongeneral Fund Balances Reported in General Fund	171,274	
Total Committed and Assigned Fund Balance		<u>1,229,941</u>
Disposition of Revenue Surplus		\$552.6 million
Total Funds Restricted or Committed to Reserves as of June 30, 2018 =		\$937.0 million
Total Fund Equity		\$ 1,786,964
Total Liabilities and Fund Balance		<u>\$ 1,891,552</u>

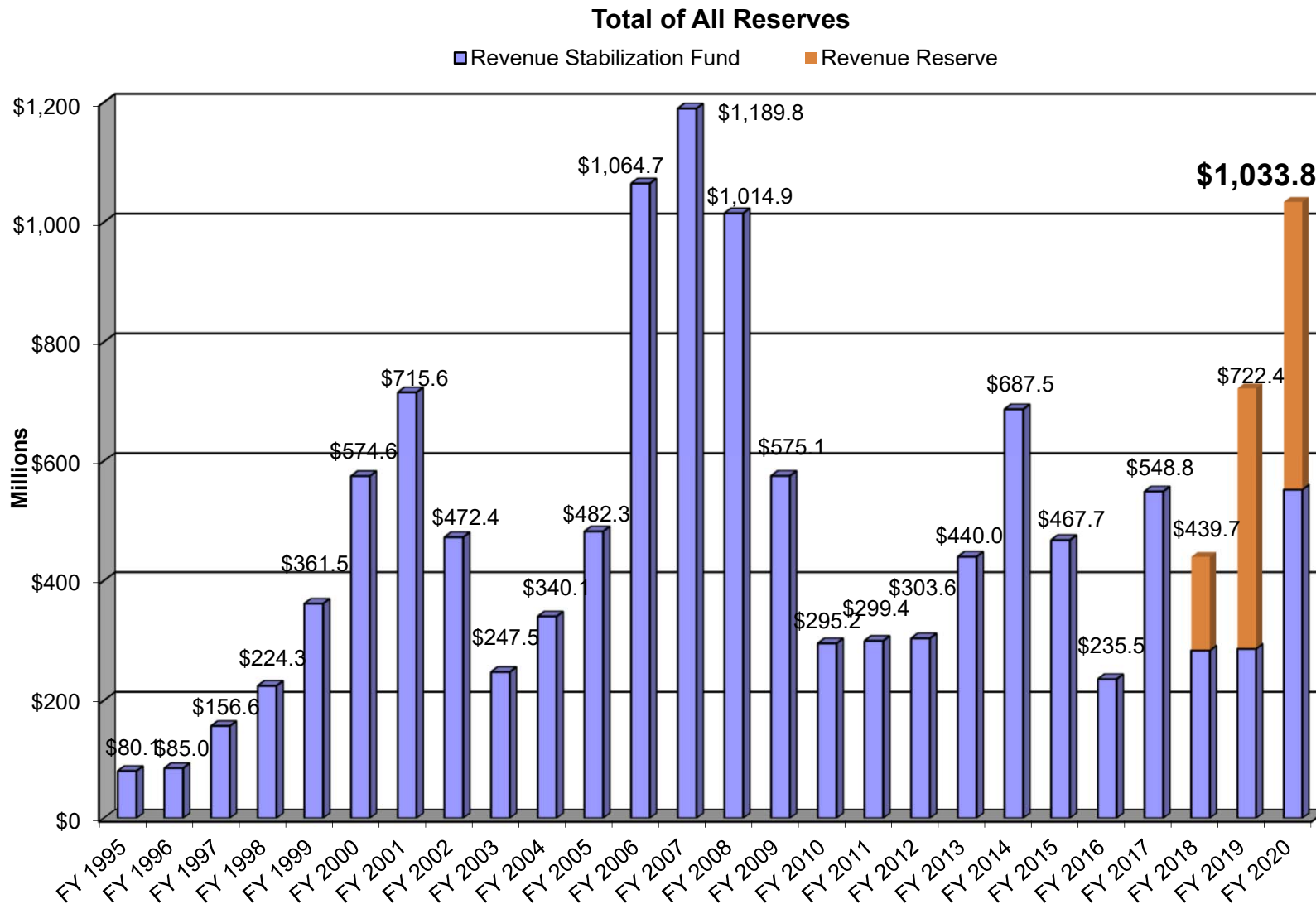
The Revenue Stabilization Fund Is Estimated To Be **\$551.9 million** as of June 30, 2020.

Revenue Stabilization Fund – June 30 Balances
 FY1995 - FY2018 Actual and FY2019 and FY2020 Forecast
 (millions of dollars)



- A mandatory deposit of \$262.9 million will be made to the Revenue Stabilization Fund in FY 2020 due to the FY 2018 surplus.
- No withdrawals are anticipated in FY 2019 or FY 2020.

By the Close of FY 2020, Total Reserves Are Estimated to Exceed **\$1.0 Billion**, the Third Largest Total Since 1995.



Official Fiscal Year 2019 Total General Fund Revenue and Transfers Forecast Calls for a 1.4 Percent Increase Compared to Actual Collections for Fiscal Year 2018

Summary of General Fund Revenue Collections FY2018 and FY2019
(millions of dollars)

<u>Revenue Source</u>	<u>Official Estimate FY2018</u>	<u>% Annual Growth Req By Estimate</u>	<u>Actual Collections FY2018</u>	<u>% Actual Growth</u>	<u>Amount Variance</u>	<u>Official Estimate FY2019</u>	<u>% Change From Actual</u>
Individual Income Tax:							
Withholding	\$ 12,313.3	3.5%	\$ 12,540.5	5.4%	\$ 227.2	\$ 12,870.2	2.6%
Nonwithholding	3,147.3	4.3	3,472.9	15.1	\$ 325.6	3,368.3	(3.0)
Refunds	(1,968.7)	5.8	(1,907.6)	2.5	61.1	(2,054.7)	7.7
Net Individual Income Tax	13,491.9	3.4	14,105.8	8.1	613.9	14,183.8	0.6
Sales and Use	3,458.2	3.0	3,461.8	3.1	3.6	3,547.3	2.5
Corporate Income	874.0	5.7	861.9	4.2	(12.1)	912.0	5.8
Insurance Premiums	362.1	6.2	337.9	(0.9)	(24.2)	376.6	11.5
Wills, Suits, Deeds, Contracts	407.2	3.3	394.9	0.1	(12.3)	407.2	3.1
Interest	67.8	21.9	61.4	10.4	(6.4)	66.2	7.8
Other Revenue	667.0	0.6	657.1	(0.9)	(9.9)	680.6	3.6
Total General Fund Revenue	19,328.2	3.4	19,880.8	6.3	552.6	20,173.7	1.5
Transfers	625.3	-4.3	628.3	(3.8)	3.0	621.0	(1.2)
Total General Fund Resources	\$ 19,953.5	3.1%	\$ 20,509.0	6.0%	\$ 555.5	\$ 20,794.7	1.4%

- FY2018 withholding growth was 4.4 percent when discounting for early July payments made on last day of June, 2018. Implies growth of 3.6% for FY2019 as compared to 2.6% listed on table.

Current *IHS Markit* Outlook for Fiscal Year 2019 Shows Improved Growth

- Supported by robust gains in employment and household wealth, real GDP is forecast to advance at a 3.0 percent rate.
 - 2018 Q2 increased by 4.1% driven by consumer spending, business investments, and purchases made ahead of a possible trade war (soybeans).
- Increases in federal deficit continue to be a concern. Federal FY19 deficit now projected to be \$1.1 trillion, up from FY18's \$666 billion – bringing the total national debt to over \$21 trillion.

Summary of Key U.S. and Virginia Economic Indicators Percent Change Over the Prior Fiscal Year

	FY18 <u>Actual</u>	FY19	
		<u>Official</u>	<u>July</u>
<u>U.S.</u>			
Real GDP	2.7	2.3	3.0
Consumer Spending	2.6	2.4	2.4
Employment	1.5	1.2	1.6
Personal Income	3.6	4.5	4.8
Wages & Salaries	4.2	4.9	4.9
<u>Virginia</u>			
Employment	1.3	1.0	tbd
Professional/Business	2.6	2.8	tbd
Construction/Mining	1.9	3.5	tbd
Personal Income*	3.3	4.3	tbd
Wages & Salaries*	3.6	4.4	tbd

* FY18 Actual data is based on the first 3 quarters of the fiscal year.

July's Revenue Collections Were Down 1.2 Percent

Summary of July FY19 Revenue Collections

Percent Growth over Prior Year

<u>Major Source</u>	As a % of Total <u>Revenues</u>	YTD <u>Actual</u>	Annual <u>Estimate</u>	<u>Variance</u>
Withholding	63.8 %	(5.5) %	2.6 %	(8.1) %
Nonwithholding	16.7	14.2	(3.0)	17.2
Refunds	(10.2)	2.9	7.7	(4.8)
Net Individual	70.3	(4.9)	0.6	(5.5)
Sales	17.6	7.5	2.5	5.0
Corporate	4.5	83.2	5.8	77.4
Wills (Recordation)	2.0	(10.5)	3.1	(13.6)
Insurance	1.9	na	11.4	na
All Other Revenue	3.7	18.8	3.9	14.9
Total	100.0 %	(1.2) %	1.5 %	(2.7) %

- July is not a significant month, representing only 6 percent of the FY19 forecast.
- The July decrease was largely due to timing of payroll withholding.
 - June included about \$120 million normally received in July.

Fall Forecasting Process Will Begin in September

- Trends in revenue collections over the next few months will be incorporated into the fall forecasting process.
 - **September:**
 - Individual, corporate, and insurance estimated payments are due
 - **October:**
 - Retailer's corporate estimated payments are due
 - Joint Advisory Board of Economists (JABE) reviews economic projections for current and next biennium.
 - **November:**
 - Corporate refunds from extension returns peak
 - Individual income tax extension returns due November 1
 - Governor's Advisory Council on Revenue Estimates (GACRE) reviews revenue forecast for fiscal year 2019, 2020, and the 2021 - 2022 biennium.
 - **December:**
 - General fund revenue forecast finalized
 - Governor Northam's amendments to the 2018 - 2020 budget are presented to the Joint Money Committee.

Tax Policy (Conformity): Certainty for 2018 Filing Season Is Critical

- Conformity means that Virginia generally adopts the federal definitions of income, such as any *above-the-line* modifications.
- Virginia does not currently conform to any Tax Cuts and Jobs Act (“TCJA”) provisions to the extent they are effective for Taxable Years 2018 and after.
- Virginia needs to advance the date of conformity to December 31, 2018 so that the 2019 filing season can begin.
- Once the date of conformity is advanced, other policy adjustments (*if any*) to Virginia law can be discussed to adjust for changes in federal law.
- Taxpayers, tax practitioners, and software vendors have historically assumed that Virginia will advance its date of conformity each year. Taxpayers will begin filing their 2018 income tax returns in January 2019.
- Failure to enact timely conformity legislation would negatively impact many constituents, including hundreds of thousands of individual taxpayers.
- In addition, if Virginia fails to advance the date of conformity:
 - Individuals would be required to complete additional forms to make up to 20 complex modifications on their Taxable Year 2018 returns.
 - Businesses would be required to make up to 30 additional modifications.

Tax Policy (Model): Certainty for 2018 Filing Season Is Critical

- Chainbridge model work is finished and the full report is available on the Finance web site – *www.finance.virginia.gov*.
 - Various assumptions have to be made regarding the choices taxpayers make in preparing their federal and Virginia returns and, to a certain extent, how their behavior may change in reaction to the TCJA. *These choices had to be made even before the enactment of TCJA.*
 - Very little federal guidance has been issued regarding the TCJA provisions. It is possible such guidance, when issued, could affect the assumptions made in developing these estimates and tax choices made by Virginia taxpayers.
 - State revenue estimates as a result of the TCJA are greater than the tax liability impact to Virginia taxpayers because of nonresident filers.
 - Many provisions related to TCJA are interrelated. Individual provisions will impact taxpayers on a case by case basis, depending on income level and other circumstances.

Total Federal Relief in Tax Year 2018

Almost \$4 Billion to Virginia

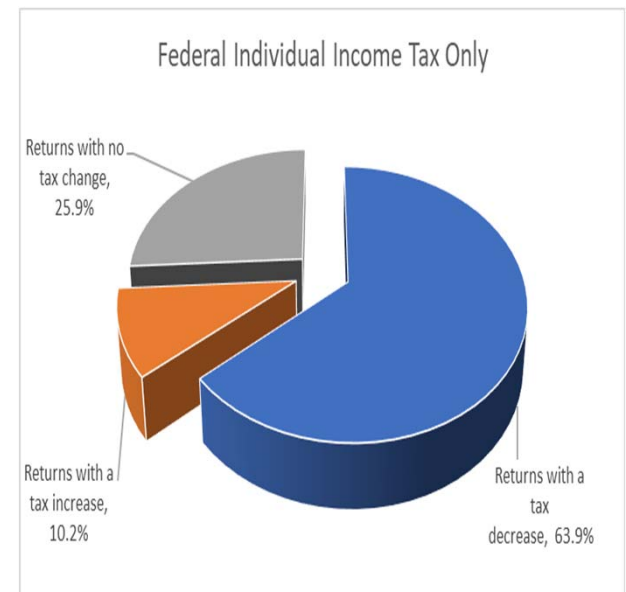
Estimated Federal Individual Income Tax Impact on the Provisions of the TCJA

Residents Only

Taxable Year 2018

Virginia Adjusted Gross Income	Tax Liability			Percent Change*
	Baseline (\$Millions)	New Law (\$Millions)	Tax Change (\$Millions)	
\$25,000 and below	240.0	211.1	(28.9)	-12.1%
25,000 - 50,000	1,510.5	1,259.1	(251.3)	-16.6%
50,000 - 75,000	2,559.0	2,131.0	(428.0)	-16.7%
75,000 - 100,000	3,073.6	2,551.8	(521.8)	-17.0%
100,000 - 125,000	3,246.0	2,675.1	(570.9)	-17.6%
125,000 - 150,000	3,064.8	2,655.8	(409.0)	-13.3%
150,000 - 175,000	2,731.3	2,500.8	(230.6)	-8.4%
175,000 - 200,000	2,347.5	2,219.8	(127.6)	-5.4%
200,000 - 250,000	3,763.6	3,620.5	(143.1)	-3.8%
250,000 - 500,000	7,691.1	7,180.7	(510.4)	-6.6%
500,000 - 1,000,000	4,326.3	3,952.9	(373.3)	-8.6%
\$1,000,000 and above	8,392.4	8,007.3	(385.1)	-4.6%
Totals	42,946.1	38,966.0	(3,980.1)	-9.3%

Source: Virginia Individual Income Tax Microsimulation Model
 * Percent Change = (Tax Change / Baseline) * 100



- About 90% of all Virginians will see no change or reduced federal tax liability.
- About 48.5% of the federal tax relief will flow to middle income taxpayers (\$50,000 - \$150,000).
- Approximately 7% of the federal tax relief will flow to taxpayers with income of \$50,000 or less.

Projected Tax Year 2018 Virginia Revenue Increase of \$333 million

Estimated Virginia Individual Income Tax Impact on the Provisions of the TCJA

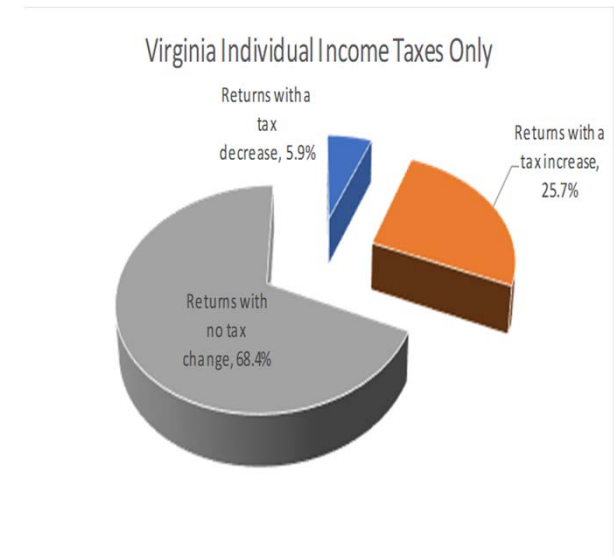
Residents Only

Taxable Year 2018

Virginia Adjusted Gross Income	Tax Liability			Percent Change*
	Baseline (\$Millions)	New Law (\$Millions)	Tax Change (\$Millions)	
\$25,000 and below	165.5	178.6	13.2	8.0%
25,000 - 50,000	866.9	899.9	33.0	3.8%
50,000 - 75,000	1,109.3	1,149.7	40.4	3.6%
75,000 - 100,000	1,188.9	1,228.9	40.0	3.4%
100,000 - 125,000	1,153.4	1,193.1	39.7	3.4%
125,000 - 150,000	1,001.8	1,030.3	28.4	2.8%
150,000 - 175,000	844.7	865.8	21.1	2.5%
175,000 - 200,000	697.2	713.1	15.9	2.3%
200,000 - 250,000	1,065.0	1,088.2	23.2	2.2%
250,000 - 500,000	1,897.9	1,927.8	29.8	1.6%
500,000 - 1,000,000	821.9	829.3	7.5	0.9%
\$1,000,000 and above	1,371.6	1,413.1	41.5	3.0%
Totals	12,184.0	12,517.7	333.7	2.7%

Source: Virginia Individual Income Tax Microsimulation Model
 * Percent Change = (Tax Change / Baseline) * 100

Approximately 13.8% of Virginia residents' tax liability resulting from TCJA will be paid by taxpayers with income of \$50,000 or less.



About 26% of Virginians will see increased state tax liability, with the highest percentage increases for taxpayers with less than \$50,000 in income.

Tax Year 2018 Net Federal and State Tax Relief Over \$3.6 Billion

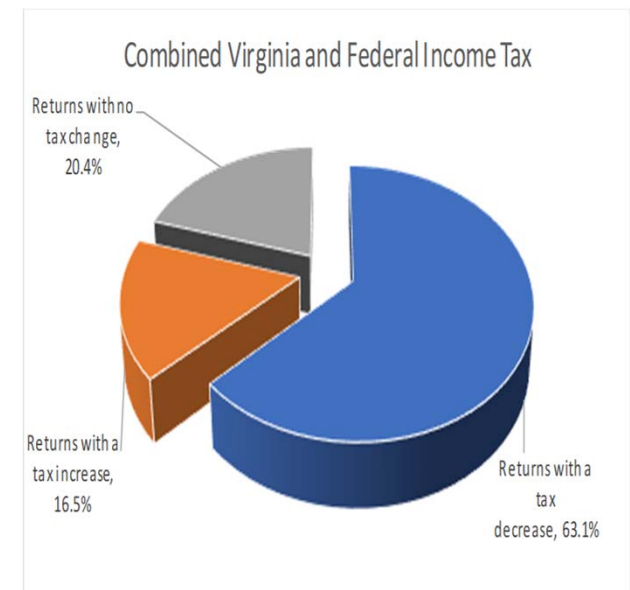
Estimated Combined Individual Income Tax Impact on the Provisions of the TCJA

Residents Only

Taxable Year 2018

Virginia Adjusted Gross Income	Tax Liability			Percent Change*
	Baseline (\$Millions)	New Law (\$Millions)	Tax Change (\$Millions)	
\$25,000 and below	405.5	389.7	(15.8)	-3.9%
25,000 - 50,000	2,377.4	2,159.1	(218.3)	-9.2%
50,000 - 75,000	3,668.3	3,280.7	(387.6)	-10.6%
75,000 - 100,000	4,262.5	3,780.7	(481.8)	-11.3%
100,000 - 125,000	4,399.4	3,868.2	(531.2)	-12.1%
125,000 - 150,000	4,066.7	3,686.1	(380.6)	-9.4%
150,000 - 175,000	3,576.0	3,366.5	(209.5)	-5.9%
175,000 - 200,000	3,044.7	2,932.9	(111.8)	-3.7%
200,000 - 250,000	4,828.7	4,708.8	(119.9)	-2.5%
250,000 - 500,000	9,589.0	9,108.4	(480.6)	-5.0%
500,000 - 1,000,000	5,148.1	4,782.3	(365.8)	-7.1%
\$1,000,000 and above	9,763.9	9,420.4	(343.6)	-3.5%
Totals	55,130.2	51,483.7	(3,646.5)	-6.6%

Source: Virginia Individual Income Tax Microsimulation Model
* Percent Change = (Tax Change / Baseline) * 100



- About 83% of all Virginians will see a net decrease or no change from Federal/Virginia tax liability.
- Only 7% of the tax relief will flow to income earners of less than \$50,000.

Fiscal Year Cash Flow of Almost \$600 Million per Year However, Significant Amount Is Not Permanent and Comes with Unknowns

Estimated Virginia Revenue Impact of the TCJA Fiscal Years 2019 to 2024 (Includes Residents and Nonresidents)

(\$Millions)

By Source	2019	2020	2021	2022	2023	2024
Individual Provisions	532.1	443.8	466.7	492.5	520.0	546.1
Business Provisions	29.4	114.6	181.5	300.3	417.2	398.2
International Provisions	32.6	52.7	5.5	5.8	6.0	6.3
Total, All Provisions	594.2	611.1	653.7	798.7	943.2	950.6

(\$Millions)

By Provisions	2019	2020	2021	2022	2023	2024
Temporary Provisions (Expiring after 2025)	517.3	433.6	455.7	480.4	506.8	532.5
Permanent Provisions	76.9	177.5	198.0	318.3	436.4	418.1
Total, All Provisions	594.2	611.1	653.7	798.7	943.2	950.6

- Most of the individual provisions are temporary and expire after 2025; the only substantial individual provision that is permanent is related to alternative inflation measures.
- Due to the likely timing of Virginia's conformity to the federal provisions, the full impact for Taxable Year 2018 is recognized in fiscal year 2019.
- Nonresidents account for approximately 11% of revenues.

Details of the Revenue Impacts from Individual Income Tax Provisions

Estimated Virginia Tax Impact of Individual Provisions of the TCJA

Residents and Nonresidents

Fiscal Year 2019 to 2024

	(\$Millions)						
	2019*	2020	2021	2022	2023	2024	Total
Simulation 1: Standard deduction modification	147.8	100.5	99.7	99.2	99.0	99.0	645.2
Simulation 2: Alternative inflation measure	14.2	9.4	9.8	9.8	10.3	10.8	64.4
Simulation 3: Loss limitation for noncorporate taxpayers	125.9	103.6	102.8	101.5	100.5	100.0	634.3
Simulation 4: Repeal and limitation of certain itemized deductions**	366.9	283.0	303.2	324.4	346.8	370.9	1,995.2
Simulation 5: Increase limit for cash charitable contributions	(0.9)	(0.7)	(0.7)	(0.8)	(0.8)	(0.9)	(4.9)
Simulation 6: Repeal of overall limitation on itemized deductions	(96.7)	(72.2)	(74.9)	(77.7)	(80.7)	(84.1)	(486.3)
Simulation 7: Changes to moving expense deduction and exclusion	6.2	4.3	4.4	4.6	4.8	4.9	29.1
Simulation 8: Medical expense deduction restoration for 2018	(45.6)	-	-	-	-	-	(45.6)
Simulation 9: Repeal deduction for alimony payments	0.8	1.1	1.6	2.2	2.9	3.7	12.2
Off-Model Estimate 1: Repeal itemized deduction for interest on mortgage debt & home equity debt	13.7	15.1	21.2	29.0	37.3	42.7	158.9
Off-Model Estimate 2: Repeal special rule permitting recharacterization of Roth conversions	-	-	-	0.6	1.0	1.0	2.5
Off-Model Estimate 3: Length of service awards for public safety volunteers	-	(0.3)	(0.4)	(0.4)	(0.4)	(0.8)	(2.2)
Off-Model Estimate 4: Allow 529 withdrawals up to \$10,000 for primary & secondary education	-	-	-	-	(0.6)	(1.1)	(1.7)
Total, All Provisions	532.1	443.8	466.7	492.5	520.0	546.1	3,001.3
* Due to the likely timing of Virginia's conformity to the federal provisions, the full revenue impact for Taxable Year 2018 is recognized in FY 2019							
** Limitation for state and local taxes and repeal of non-disaster casualty loss deduction; and deduction for certain miscellaneous expenses							

- About two-thirds of the revenues are from the repeal and limitation of certain itemized deductions.

Details on the Individual Income Tax Provisions

Comparison of Certain Itemized Deduction Changes to Repeal of Pease Limitation

Residents Only, Taxable Year 2018

Virginia Adjusted Gross Income	Repeal and Limitation of Certain Itemized Deductions (\$Millions)	Repeal of Pease Limitation (\$Millions)	Net (\$Millions)
\$25,000 and below	2.6	(0.0)	2.6
25,000 - 50,000	22.9	(0.0)	22.9
50,000 - 75,000	23.8	(0.0)	23.8
75,000 - 100,000	21.6	(0.0)	21.6
100,000 - 125,000	19.7	(0.0)	19.7
125,000 - 150,000	17.8	(0.0)	17.8
150,000 - 175,000	16.2	(0.0)	16.2
175,000 - 200,000	14.0	(0.0)	14.0
200,000 - 250,000	21.9	(0.1)	21.8
250,000 - 500,000	35.4	(7.4)	27.9
500,000 - 1,000,000	17.7	(16.2)	1.5
\$1,000,000 and above	25.6	(36.5)	(10.8)
Totals	239.2	(60.2)	179.0
Source: Virginia Individual Income Tax Microsimulation Model			
* Percent Change = (Tax Change / Simulation 5) * 100			

- Each provision cannot be considered without taking into account other related provisions. For example, those with income of \$250,000 or more will pay an additional \$78.7 million in Virginia taxes as a result of changes to the state and local tax and miscellaneous itemized deductions.
- However, that will be offset in \$60.2 million in tax savings from the federal repeal of the Pease limitation on itemized deductions, resulting in a net impact of \$18.5 million. Those in the highest income range will actually realize a net benefit of \$10.8 million from these two provisions.

Details on the Individual Income Tax Provisions

Impact on the Decision to Either Itemize or Take the Standard Deduction

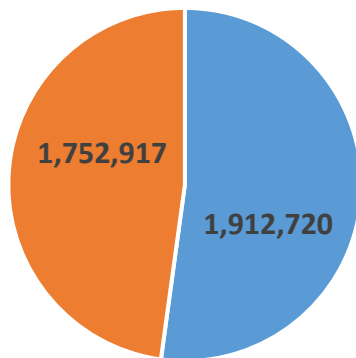
Residents Only, Taxable Year 2018

Virginia Adjusted Gross Income	Itemized Deduction Number of Returns		Standard Deduction Number of Returns		Number Switching from Itemized to Standard
	(Prior Law)	(New Law)	(Prior Law)	(New Law)	
\$25,000 and below	36,628	16,621	1,084,910	1,104,917	155,306
25,000 - 50,000	167,870	94,367	623,312	696,815	77,757
50,000 - 75,000	210,411	127,687	291,987	374,711	81,991
75,000 - 100,000	204,658	125,969	153,029	231,718	78,303
100,000 - 125,000	182,721	105,197	71,295	148,819	77,461
125,000 - 150,000	143,545	89,223	27,964	82,285	54,286
150,000 - 175,000	106,729	71,457	12,243	47,515	35,280
175,000 - 200,000	77,615	54,667	5,826	28,773	22,923
200,000 - 250,000	100,752	74,070	4,296	30,978	26,587
250,000 - 500,000	121,447	94,123	1,601	28,925	27,097
500,000 - 1,000,000	25,458	21,178	379	4,659	4,211
1,000,000 - and above	10,668	9,582	296	1,382	1,065
Totals	1,388,501	884,140	2,277,136	2,781,497	642,266

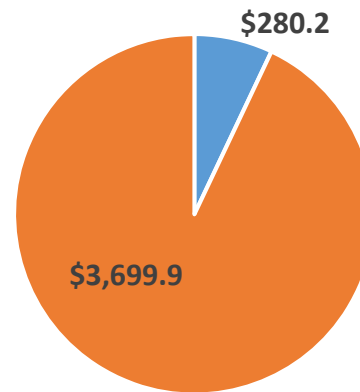
- An estimated 642,266 Virginians are projected to switch from itemizing to claiming the standard deduction.
- This is the combined result of (1) an increase in the federal standard deduction and (2) changes to itemized deductions, including the \$10,000 SALT deduction cap and repeal of certain deductions.
- 16.7% of households with income between \$50,000 and \$150,000 will be impacted by the repeal and limitation of itemized deductions on the Virginia return; these account for only 5.86% of all Virginia resident returns.

Tax Year 2018 Impact on Households with Income of Less than \$50,000

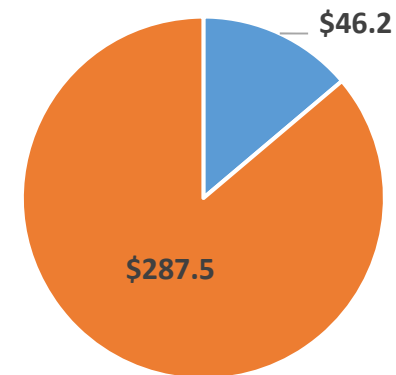
3,665,637 Virginia Returns
(Projected, Taxable Year 2018)



Federal Tax Savings for Virginians
(Taxable Year 2018, Dollars in millions)



Impact on Virginia Resident Returns
(Taxable Year 2018, Dollars in millions)



■ AGI < \$50,000 ■ AGI > \$50,000

- 52.2% of Virginia resident returns (3.67 million total projected for Taxable Year 2018) are filed by households with income of less than \$50,000.
- 93% of federal tax cuts benefit households with income over \$50,000; only 7% of federal tax cuts will flow to income earners of less than \$50,000.
- However, 13.8% of the Virginia revenues resulting from the TCJA will be paid by those with income of less than \$50,000.

Governor's Proposals to Provide Additional Investment in Main Street and Working Families, and Tax Relief to Income Earners of \$50,000 or Less

- **Invest in Main Street and working families**
 - Governor's priorities to be included in budget amendments:
 - Increase broadband access – one-time infrastructure spending
 - Invest in workforce development and education
 - Make health care more affordable
- **Return about one-half of the windfall to income earners of \$50,000 or less by making Virginia's *Earned Income Tax Credit for Low-income Taxpayers* (20% of the federal credit) refundable**
 - Current credit only applies to a positive tax liability
 - Approximate cost of \$250 million dollars and would allow 600,000 taxpayers to take full tax benefit for which they qualify
 - Proposal would apply to tax year 2018 requiring an emergency clause in the legislation proposed for the 2019 General Assembly.
 - The credit will mirror the federal individual provision.

Internet Sales (*Wayfair*)

Estimated Revenue Impact by Fund (millions of dollars)

State Sales and Use Tax (5.3% net of Dealer Discount)	5.280%	\$ 233.7
GF - Unrestricted ⁽¹⁾	2.015%	\$ 89.2
GF - Restricted 1% Education ⁽²⁾	0.990%	\$ 43.8
Education School Age 1/8%- (GF transfer from Restricted)	0.125%	\$ 5.5
Education SOQ- 1/4%(GF transfer from Unrestricted)	0.250%	\$ 11.1
Transportation ⁽³⁾	0.800%	\$ 35.4
HMOF (GF transfer)	0.100%	\$ 4.4
Local Option	1.000%	\$ 44.3
Regional Trans. Funds (0.7%) ⁽⁴⁾	0.367%	\$ 16.3
Hampton Roads (TPO)	0.127%	\$ 5.6
Northern Virginia (NVTA)	0.240%	\$ 10.6
Total Sales and Use Tax ⁽⁴⁾	5.647%	\$ 250.0

Notes:

- 1) Includes: 2.025% General Fund Unrestricted, -0.01% Dealer Discount.
- 2) Includes: 1% Education based on school age population, -0.01% Dealer Discount.
- 3) Includes 0.5% TTF, 0.175% HM OF, 0.050% IPROCF, and 0.075% Mass Transit Fund.
- 4) The assumed state, local and regional sales and use blended tax rate is 5.65%, after dealer discount.

“Interstate Sales-Tax Compliance Is Killing My Business”

The Supreme Court has spoken. Now Congress should step in to impose uniform nationwide rules.

American commerce has never stood still, and for more than 200 years the U.S. legal system has struggled to keep up with evolving sales trends. The Supreme Court’s ruling in *Gibbons v. Ogden* (1824) affirmed the federal government’s power to regulate steamboats crossing state lines. Now, the court’s June decision in *South Dakota v. Wayfair* has allowed states to tax sales of goods and services delivered to their residents, even when vendors aren’t based there.

In *Wayfair*’s wake, courts may soon be forced to rule on the regulation of transactions made via blockchain. If automated delivery vehicles are found to establish “nexus”—or physical presence—for their owners, sellers may be forced to remit taxes in states where they deliver goods. There currently are few limits on the sales rules states can impose, allowing legislatures to lay claim to all kinds of interstate commerce. These new layers of taxes and regulation could raise prices for vendors and consumers.

Congress must act to simplify the rules of commerce after the *Wayfair* decision. Though Justice Anthony Kennedy and Chief Justice John Roberts issued differing opinions on the case, both affirmed the federal government’s power to mandate open commerce. Alexander Hamilton wrote in *Federalist No. 11* that unrestrained commerce between the states would “advance the trade of each.” **Without a new law to limit state regulation of internet sales, interstate trade will soon be stifled.**

As a business owner, my main problem isn’t the money my company pays in state taxes. **Rather, it’s the compliance and paperwork we’re forced to undertake to make sure we don’t violate the law unintentionally. My employees and I must figure out what is taxable and what isn’t in all 50 states and countless localities. Is a bolt taxable?** In some states that depends on whether the bolt is used to repair office equipment, which is taxable, or to fix manufacturing equipment, which isn’t.

Taxes on services can be equally challenging. Texas taxes different kinds of services at different rates and requires vendors to fill out their own payment permits. For my supply-chain-management company, that means deciding which of three information-technology categories describes our services. To ensure accuracy, my employees and I have to determine whether each customer will use our products for wholesale purposes or whether they are the final user. Texas also allows its 254 counties and more than 1,000 municipalities to impose their own sales levies, which must be calculated individually.

Then come the audits. Our company has been audited as many as five times in a year each year. One audit from Illinois demanded rental-car and hotel receipts in an attempt to apply the nexus standard to services we delivered to a customer. So each time we do a custom installation or on-site maintenance, we need to check with our accountant to determine if we’re establishing nexus.

Congress should step in to untangle this convoluted mess of burdensome state rules. In its place, lawmakers should impose clear nationwide standards for interstate vendors. House Republicans will have an opportunity to do so in their coming plan for “Tax Reform 2.0,” announced last month by the Ways and Means Committee. The current outline doesn’t mention state sales taxes. But encouraging economic growth by simplifying taxes is the stated purpose of the reform and was the key to the success of the first iteration.

Previous attempts to establish fairness in state sales taxes, like Rep. Bob Goodlatte’s 2016 bill, have failed to gain steam. How about reframing sales-tax reform as a way to unleash economic activity and reduce prices for consumers?

The Council on State Taxation, an association of corporate taxpayers, issued a dense report in April that takes 66 pages to summarize the nation’s sales-tax regime. Among the best practices identified by the council are exemptions for small businesses, which are critical to boost startup activity, and centralized remittance to one state-revenue authority, which reduces accounting costs.

Making provisions like these into uniform rules for interstate vendors would help companies like mine expand our operations and reduce excessive record-keeping and pricey meetings with lawyers and accountants. If Congress chooses to enact sales-tax reform, interstate commerce will expand and everyone will win.

by Jay Steinmetz – *The Wall Street Journal*, Aug. 8, 2018

Known Funding Commitments / Risks

- **Major Employment and Investment (MEI) Project Approval Commission Obligations**
- **Virginia Retirement System (VRS) Investment Earnings**
- **Federal Actions**
 - Grants Funding
 - Budget
- **Agency Projects**
 - VITA – Northrop Grumman Settlement / Transition
 - DOA / DHRM – Human Resource System Replacement
 - Virginia State Police Communications – *Statewide Agencies Radio System* (STARS)
- **Transportation Funding**
- **Capital Allocation**
 - Priority
 - Deferred Maintenance

Appendix

- Fiscal Year 2018 General Fund Collections: Actual and Official Forecast
- Official General Fund Forecast for Fiscal Years 2019 and 2020
- Official Commonwealth Transportation Fund Forecast for Fiscal Years 2019 & 2020
- Growth in Total General Fund Revenues, Fiscal Years 1961 to 2020
- June 2018 Revenue Report
- July 2018 Revenue Report
- Chainbridge Summary Report

Note:

The General Fund Preliminary Annual Report, August, 2018 is available at the Department of Accounts web site (www.doa.virginia.gov).

This presentation is available at the Secretary of Finance web site (www.finance.virginia.gov).