

## New Virginia Tax Law

### How will the new law affect your taxes?

By Kay F. Gotshall, CPA

The tax law passed by the Virginia Assembly on April 30, 2004 and signed by Governor Warner enacts significant changes to many Virginia taxes that could impact both your business and personal income tax. Affecting both is an increasing general sales tax, somewhat offset by a decreasing rate for food and vending machine sales. On the individual income tax side, there are changes to the filing thresholds, personal exemptions, standard deduction and the age based deduction. In addition, the new law implemented a new earned income tax credit for individuals. On the business side of things, new filing requirements have been introduced for partnerships and there are other tax changes that disallow the deduction of intangible expenses for certain related party transactions. Finally, the new law increases the Virginia document recording tax and cigarette tax as well as adding a new Virginia tax on tobacco products.

#### Sales Tax Changes

Getting ready to make a large purchase of tangible personal property (such as a new copier)? You may want to consider accelerating the purchase - taking delivery before September 1, 2004. The new Virginia state sales and use tax is increasing to 4.0% effective September 1, 2004. If you add that to the Virginia local rate of 1%, the total sales tax rate will be 5%. As a compromise to this increase, there is a decrease in the sales tax rate on food for human consumption from 3% to 2.5% from July 1, 2005 through June 30, 2006, with other decreases through June 30, 2007. Finally, the vending machine sales tax rate decreases from 4.5% to 4%.

Some purchases for bona fide real estate construction may qualify for a refund of 0.5%, but be sure to file your refund application on time. Finally, the exemption used by a public service corporation in the generation of electric power to purchase industrial materials, machinery, tools and packaging has been revoked.

#### Personal Income Tax Changes

The 2005 tax year will bring many changes to personal tax calculated on Form 760. First, the adjusted gross income (AGI) filing threshold for singles is increasing from \$5,000 to \$7,000 and for the married filing joint (MFJ) taxpayer it increases to \$14,000. For example if your Virginia AGI is less than \$7,000 and you are single, you do not have to file a return in 2005. Second, the standard deduction for MFJ taxpayers increases to \$6,000. Finally, beginning 2006, the personal exemption increases to \$900.

One of the more painful provisions of the law enacted is the phase out of the \$6,000 age deduction currently allowed by taxpayers

between age 62 and 64. Taxpayers who are 62 to 64 as of January 1, 2004, will continue to receive the \$6,000 deduction, but those under age 62 will not receive it at all. In addition, the \$12,000 deduction for taxpayers reaching age 65 after January 1, 2004 will be reduced dollar-for-dollar for every dollar the taxpayer's federal AGI exceeds \$50,000 (\$75,000 for married taxpayers). Federal AGI for this purpose excludes any social security and Tier I Railroad Retirement benefits.

Furthermore, under the personal income tax arena beginning in 2006, taxpayers claiming the federal earned income tax credit will be allowed up to 20% of the federal EIC as a credit for Virginia tax purposes, in lieu of the current low-income credit. As with the current low-income credit, this credit is non-refundable and cannot be carried forward.

#### Miscellaneous

Beginning in 2004, pass-through entities are required to file information returns with the Virginia Department of Taxation on a new Form 502. The due date of the return is the 15<sup>th</sup> day of the fourth month following the close of the tax year, or April 15<sup>th</sup> for a calendar year taxpayer, unless an extension is granted. Pass-through entities include partnerships and S corporations.

Effective September 1, 2004, the Virginia document recording tax for deeds of trust or mortgages relating to real or personal property has increased by 10 cents for every \$100 or portion thereof of the value of the obligation or contract.

The Virginia cigarette tax rate increased to 1 cent on each cigarette sold, stored or received after September 1, 2004 and to 1.5 cents per cigarette after June 30, 2005.

As you can see there were sweeping changes across an array of different tax areas. It is recommended that you contact your tax professional or visit the Virginia Department of Taxation's website at [www.tax.state.va.us](http://www.tax.state.va.us) in order to determine the impact these changes will have on your personal situation.

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