

W E S T V I R G I N I A



DEPARTMENT OF REVENUE

Joint Select Committee on Tax Reform **Historical Review of Tax Reform Studies** DEPUTY REVENUE SECRETARY MARK B. MUCHOW

West Virginia State Capitol
May 4, 2015

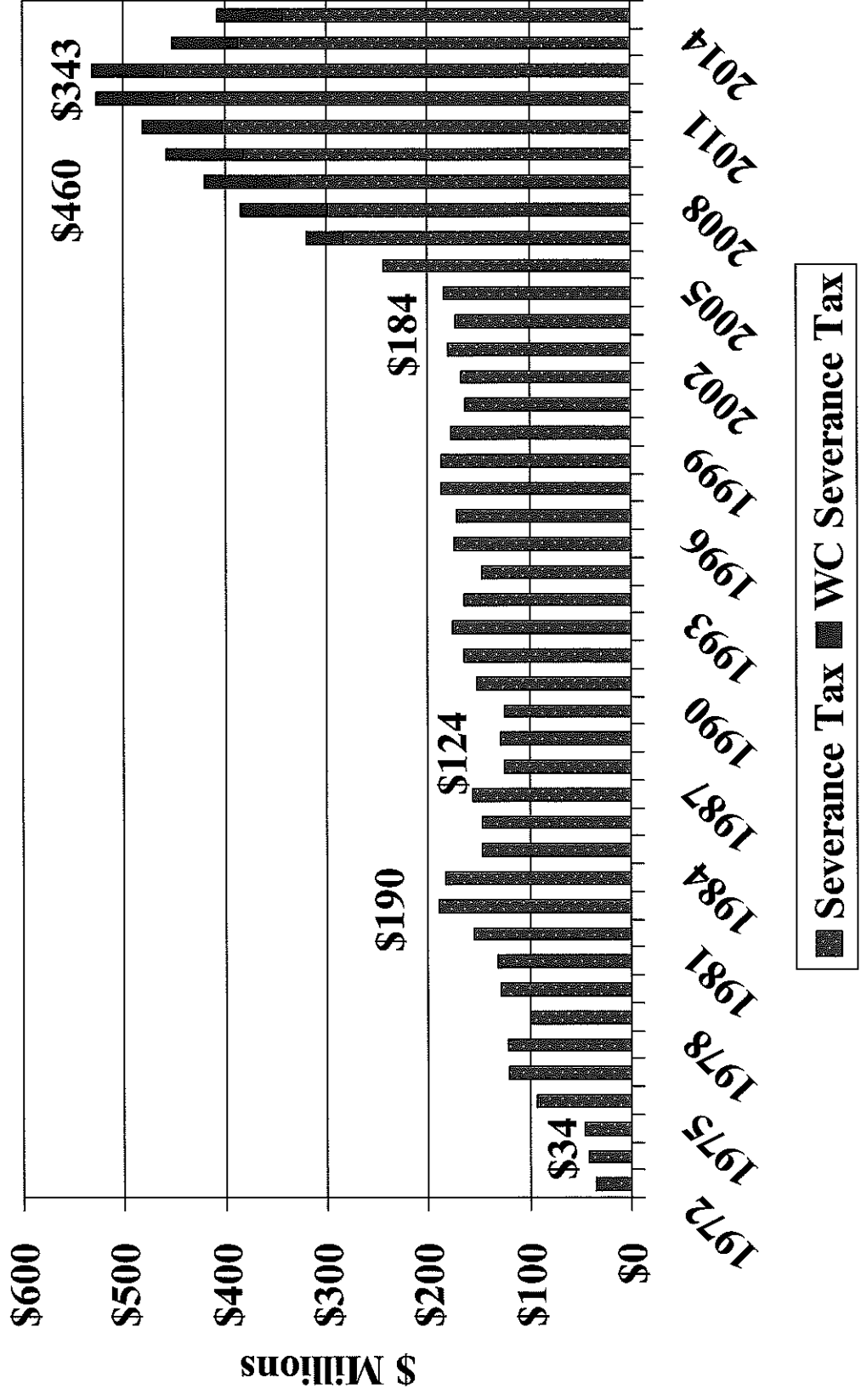
Secretary **Robert S. Kiss**

Governor **Earl Ray Tomblin**

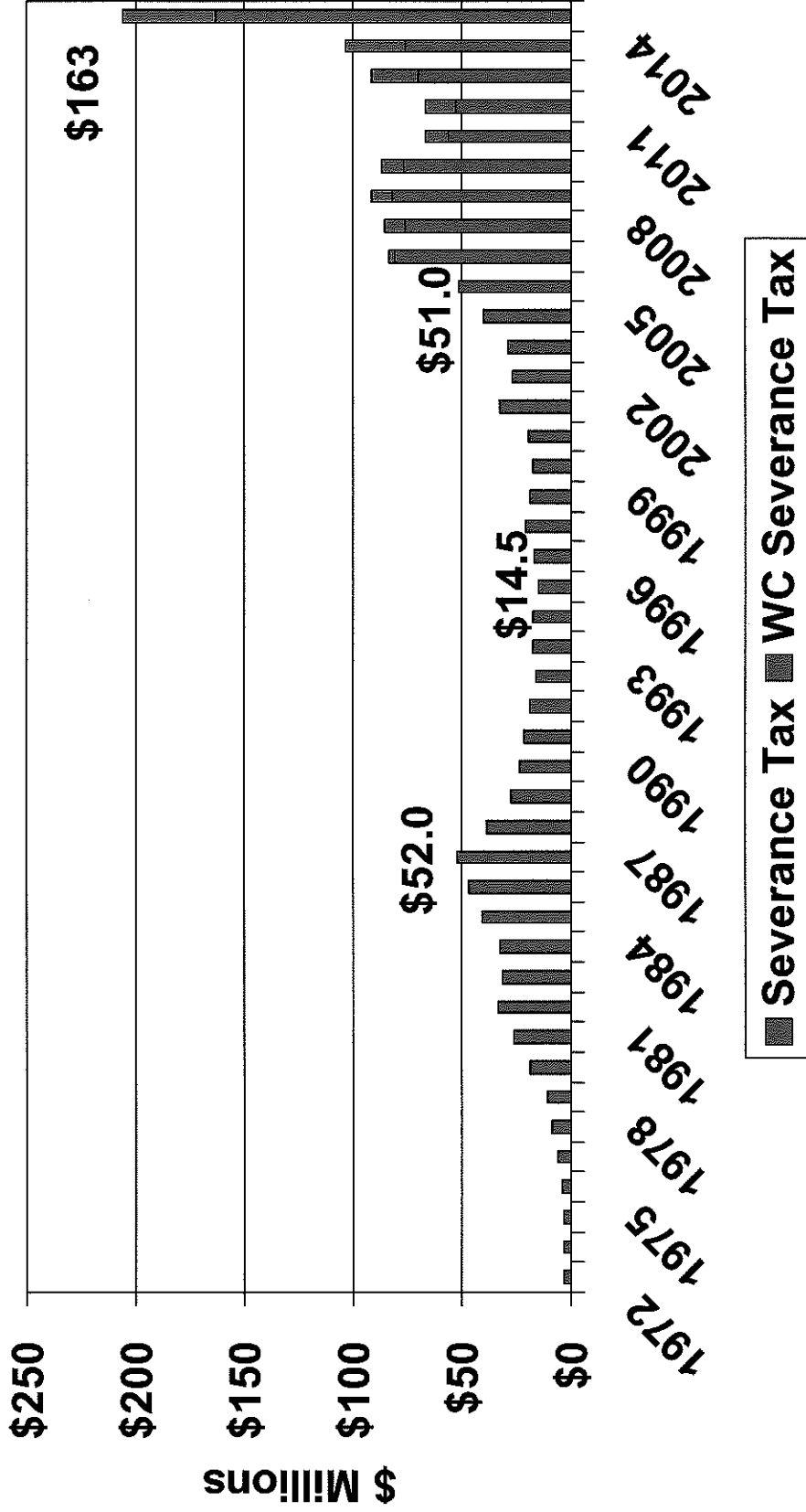
Historical Events Shape Tax System

- Prohibition: (WW goes Dry in 1914: New Tax System)
 - Move to State consumption taxes (B&O and gasoline)
- Great Depression of the 1930s
 - Property Tax Revolt (Move toward government centralization)
 - Move to more State consumption taxation (Sales Tax and more)
 - Roads transferred from counties to State
- Educating Baby Boomers in 1960s:
 - Higher sales tax rates
 - Introduction of personal income tax and corporate income tax
- 1970s Energy Boom Followed by Bust in 1980s
 - Significant growth in B&O taxes due to energy and inflation
 - Removal of sales tax on groceries and increase in tax rate
 - Shift from consumption tax (B&O) to income taxes
 - Reinstatement of grocery tax and higher sales tax rate
- 2000s Energy Boom Followed by Recent Downturn
 - Removal of sales tax on groceries
 - Repeal of a number of taxes and other tax relief
 - Record levels of severance tax collection

WV Coal Severance Tax Collections By Fiscal Year 1972-2014



WV Natural Gas Severance Tax Collections by Fiscal Year 1972-2014



Major Tax Changes in 1985-87

West Virginia Tax Study Commission: A Tax Study For West Virginia In The 1980's
Federal Tax Reform Act

- 1985: Repeal of Inheritance Tax (Estate Tax)
- 1987: Implementation of Business Tax Reform Act of 1985
 - Elimination of B&O Tax as a broad business tax in favor of income base
 - Corporation Net Income Tax base broadened with rate increase from 7% to 9.75%
 - Creation of secondary Business Franchise Tax at rate of 0.55%
 - Mining Industry subject to Severance Tax with rates converging to 4%
 - Electric Power Generation Industry & Public Utilities continue with B&O Tax
 - Informational Tax Returns to be filed for two years reflecting TY1984 & TY1985
 - Elimination of Carrier Income Tax; Telecommunications Tax replacement
- 1987: Personal Income Tax Reform Act
 - State response to 1986 Federal Tax Reform Act
 - Broaden the base & lower tax rates
 - Give back windfall to Taxpayers

Executive & Legislative Disagree on Tax Reform

- Tax Study Commission Created by West Virginia Legislature in 1982
 - Paul Volcker appointed Chairman of Federal Reserve Board-High Interest Rate Medicine
 - 1980-82 Severe National Recession-Transition to Lower Inflation
 - West Virginia enters Recession later in 1982-83
- 1984: Election of Governor Moore – Party Switch
 - Governor has Own Agenda
 - Economic Development Incentives to stimulate economy – Super Tax Credit – Saturn Plant
 - Research & Development, Capital Company, Residential Housing Development, Enterprise Zones
 - Tax Study Commission: “No more need for economic development tax credits after tax reform”
 - A number of tax reform recommendations adopted [Reorganization of Tax Department; Repeal of Inheritance Tax, Freeport Amendment]
- 1984-1988: Economy Weak and Energy Prices Falling
- Governor Wishes to Delay Implementation of Tax Reform; Legislature Disagrees
 - Tax Department measures significant gap & growing gap in revenues under Tax Reform Plan
 - Personal Income Tax: Give back windfall to Taxpayers
 - 1985 Business Tax Reform Act tweaked before implementation (e.g., Telecommunications Tax)
 - General Revenues fall by more than 7.5% between FY1987 and FY1988 (\$115 million)

Major Tax Changes in 1988-93

Numerous Tax Changes to Close Gap, Provide Funding for Roads & Legacy Costs

- 1988: Sales tax rate increased from 5% to 6% & \$50 million state loan for bills
 - Unpaid tax refunds carried over to future fiscal year rise significantly
- March 1, 1989: Fiscal Responsibility Act (Governor Caperton) : \$400 million
 - Increased Gasoline Excise Tax rate from 10.5 cents per gallon to 15.5 cents
 - 6% Sales Tax rate made permanent
 - Sales Tax base broadened to include groceries, purchases by contractors, and some business inputs
 - Business Franchise Tax Rate increased from 0.55% to 0.75% & severance tax offset credit ends
 - Severance Tax rates increase from 4% to 5%
 - New B&O Tax on gas storage facilities
 - B&O Tax on electric power restructured from a gross receipts tax to a kilowatt-hour tax
- 1990: B&O Tax rate increase, Sales Tax change-Gov't Contracts, Super Credit Change
- 1991: HCP Medicaid Tax [January 1992-May 31, 1993]
- 1993: Health Care Provider Taxes replace Medicaid Tax
 - Gasoline Tax Rate increased to 20.5 cents;
 - Additional Super Credit Changes

Period of Relative Tax Stability: 1994-2004

- Period of Significant Expansion of Lottery Programs and revenues
- 1995: Kilowatt-hour tax converted to tax on taxable capacity
- 1996: Low-Income Exclusion added to Personal Income Tax
- 1997: Business Franchise Tax rate reduced to 0.7%
- 1997-1999: Governor Underwood's Commission on Fair Taxation
 - Final report issued in September 2009
 - No action taken prior to 2000 General Election
- 2001: 10-year phase-out of certain health care provider taxes begins
- 2001-02: Analysis and Recommendations for West Virginia Tax Incentives
- 2001-03: Medical Malpractice Reform & Tax Credits
- 2002: OTP tax created with 7% rate & Tax Credit Reform Legislation
- 2002: Estate Tax scheduled for repeal when federal death tax credit expires in 2005
- 2003: Cigarette Tax rate increased from 17 cents per pack to 55 cents per pack

Major Tax Changes Since 2005

Some Increases But More Decreases:

Energy Price Boom & Excess Lottery Revenues

- 2005: December 1, 2005: Workers' Compensation Severance Tax
- 2006: January 1, 2006 - Grocery Tax Phase-Out Begins (\$170 million)
- 2007: Business Franchise Tax rate reduced to 0.55% & Corporate Tax rate to 8.75%
- 2007-2009: Combined reporting enacted in 2007 and refined in 2008 to take effect in 2009
 - Phase-out of Business Franchise Tax between 2009 & 2015
 - Phase-down of Corporation Net Income Tax rate from 8.75% to 6.5% from 2009-2013
 - Expanded tax credits for manufacturing, including inventory tax credit
- Other significant tax changes:
 - 2007: Low Income Tax Credits (Family Tax Credit & Doubling Homestead)
 - 2007: Expansion of prescription drug exemption
 - 2007: Expansion of Pass-through Sales Tax Exemption for Contractors
 - 2008: Repeal Corporate Charter Tax
 - 2010: Repeal State AMT – Personal Income Tax
 - 2011-12: Elimination of business registration renewal fees

Centralized Government Responsibility

Limits Reform Options

- Successful long-term tax reduction at the State level often depends on some shift of government responsibility down to the local level
- In West Virginia, government responsibilities continue to migrate from the local level to the State level
- K-12 Education is a local responsibility in most states with some aid from State government; In WV, it is a State responsibility with some local government support.

Conclusions

- States reduce taxes during periods of budget surplus and raise taxes during periods of revenue downturn
- Coal industry fortune (natural gas industry) has significant impact on direction of tax policy
- Tax reform is rarely revenue neutral
- Economic gains often associated with government stability
- Measured tax changes may be better than dramatic wholesale change
- The balance budget requirement restricts state policy changes
- The share of funding responsibility at the local level a key to degree of State tax reform

