

Stuck In a Rut

Senate's Version of HB2313 Still Lacks Offsetting Relief Measures

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While the Senate's version of Governor McDonnell's transportation bill looks very different from the bill passed by the House – and it is – the two versions have one major problem in common: they rely on regressive tax increases that will have low-income Virginians paying a greater share of their income towards funding transportation.

As the conference committee works to craft the best compromise possible for Virginia's roads, lawmakers should make sure it's the best it can be for Virginia's families, too. To do that, conferees should include targeted relief mechanisms – like a refundable earned income credit or a new targeted rebate program – to effectively offset the disproportionate impacts of regressive gas or sales tax increases on Virginia's low- and middle-income families.

Background on the Senate's Version of HB2313

The transportation bill that passed the Senate contains a few similar elements to the governor's original proposal and the House version. It also includes some significant departures from those approaches and contains a lot of moving pieces contingent on action (or inaction) by federal and local policymakers.

But, the net result of the Senate bill is that lower-income households will be disproportionately impacted.

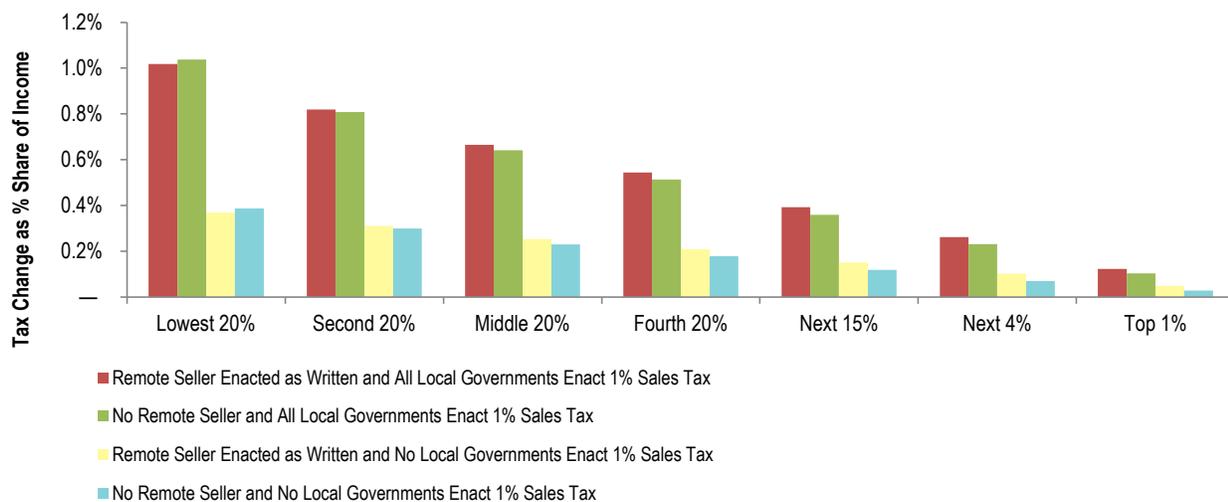
- **Sales Tax Diversion:** The Senate version retains the governor's general fund diversion plan, but at a lower rate. Instead of siphoning off .75 cents of the sales tax to transportation

(McDonnell's proposal), the Senate plan bleeds off .55 cents of the sales tax.

- **Remote Seller Legislation:** Like the House version, the Senate version also assumes passage of federal remote seller legislation allowing Virginia to require sellers to collect and remit sales taxes from online purchases and diverts a share of that new money away from education, public safety and other general fund expenses to transportation.
- **Registration Fee Increase:** The Senate version keeps the same \$15 increase in the vehicle registration fee as the governor's proposal and the House version.

Bad Directions: Tax Increases Higher for Low-Income Virginians

Senate Bill's New Taxes as a Share of Income, by Income Group



Source: Institute on Taxation and Economic Policy, February 2013

- **Gas Tax:** The Senate bill treats the gas tax very differently than either the House or the governor’s versions. Instead of eliminating this revenue source altogether, the Senate instead boosts the rate to 22.5 cents per gallon from 17.5 cents, and then indexes it to inflation of construction materials using the producer price index. The Senate also adds a one percent wholesale fuel tax, which would increase to two percent if Congress fails to enact remote seller legislation.
- **Local Sales Tax Authority:** The Senate version also gives local governments the option of enacting up to a one percent sales tax increase for transportation purposes. Neither the governor’s proposal nor the House version contain this provision.

The Net Result

Depending on how localities respond to the new local sales tax authority and whether Congress enacts remote seller legislation, the exact impact of HB2313 could vary. But in every possible scenario, the transportation plan would fall heaviest on Virginia’s lowest-income households and families.

The Senate transportation plan would fall heaviest on Virginia’s lowest-income households.

As more localities take advantage of the sales tax option, the disproportionate hit grows. Depending on how many utilize this enhanced funding stream, the poorest 20 percent of households in Virginia could see the share of their income paid in state and local taxes increase between .4 percent and one percent. By contrast, the top one percent would see almost no increase at all (as a share of their income).

From the perspective of the median Virginia household, average annual state and local taxes under the Senate plan would likely increase between \$117 and \$341.

A Better Route

Instead of fixing the state’s transportation problems by making low-income Virginians pay a greater share of the cost in higher taxes, conferees can rebalance the scale by including targeted mechanisms that effectively offset whatever tax increases are included for Virginia’s low- and middle-income families.

Two options for reducing the negative effects of broad-based tax increases on moderate- and low-income Virginians include:

Refundable Earned Income Credit

Making Virginia’s Earned Income Credit (EIC) refundable would be one way to offset part of the disproportionate impact on lower-income Virginians of any new sales or excise tax increases. By making the earned income credit refundable, workers whose credit is greater than the income tax they pay would receive their remaining credit in the form of a refund, which would help offset a portion of the other taxes they pay. Numerous studies have found that the federal version of this credit is a strong incentive to

work, boosting workforce participation among single mothers and low-wage working mothers, reducing cash welfare assistance, and lifting families out of poverty by helping them make ends meet. Refundability is critical to bringing the state’s earned income credit to its full potential.

Tax Rebate

Another option for off-setting the impact of new transportation taxes is to provide a straight rebate to low-income households. Five states (Arizona, Hawaii, Idaho, New Mexico, and Oklahoma) have some form of rebate designed to offset sales and excise taxes. Most of the rebates are a flat dollar amount per family member and are only available below a certain income threshold. All of these rebates are refundable in order to help the lowest income, hardest-hit families. While the particular details of such a rebate program would need careful attention – for example, to avoid a “cliff effect,” a gas tax rebate should phase out near the income limit – such a program would provide a simple way to give the tax relief to low-income Virginians.

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