COST
COUNCIL ON STATE TAXATION

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Delegate Joseph P. McNamara, Chair
House Finance Sub-Committee #1
The Virginia House of Delegates

Re: Support for House Bill 352, Decoupling from Federal Interest Limitation

Dear Chair McNamara and Members of the Sub-Committee:

On behalf of the Council On State Taxation (COST), I am writing in support of the provisions in H.B. 352 that would provide much needed relief to Virginia corporate taxpayers by partially decoupling from federal limitations on business interest expense effective January 1, 2022. While we support full decoupling, the 50% decoupling in H.B. 352 is a step in the right direction. The federal interest limitations were one of the base broadeners contained in the federal Tax Cuts and Jobs Act (TCJA) and were designed to partly offset a significant corporate tax rate decrease at the federal level. Decoupling from these limitations would reverse an inadvertent tax increase.

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 over 500 major corporations engaged in interstate and international business. COST's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities. Many COST members have operations in Virginia.

Interest Expense Limitation

Corporate tax "base broadeners," like the interest limitation provisions of I.R.C. § 163(j) under federal tax reform, funded in part the substantial reduction in federal corporate tax rates to make the U.S. more competitive internationally. As noted above, these rate reductions did not occur at the state level, and therefore maintaining Virginia's conformity to these provisions results in a substantial corporate income tax increase. This outcome is inadvertent and arbitrary and based solely on mechanical state conformity with the federal corporate tax base broadeners but not the federal corporate tax rate cuts.

Moreover, the I.R.C. § 163(j) provisions are not tailored to combat abusive or distortive intercompany lending. Rather, the provisions limit interest expenses across the board, for both intercompany and third-party borrowing, and thus impact all borrowing by Virginia taxpayers for both business operations and investment/expansion. Conformity to these provisions harms Virginia's competitiveness.

Conclusion

H.B. 352 partially decouples Virginia from the significant TCJA tax base expansion provision that unintentionally increased Virginia's business income tax base (with no corresponding tax rate decrease that occurred at the federal level). COST respectfully urges this Committee to favorably support this legislation. Please feel free to contact us with any questions regarding COST's position in this area.

Sincerely,

Patrick J. Reynolds

cc: COST Board of Directors
Douglas L. Lindholm, COST President & Executive Director