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Technical Report: Impact of Changing the Basis of the BPOL Tax From Gross Receipts to Income

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BACKGROUND

The Business, Professional, and Occupational License (BPOL) tax is imposed by local governments on businesses for the privilege of operating within the locality. In many areas of Virginia, the BPOL tax is a significant source of local revenue. In FY 2012, localities collected more than $680 million in BPOL taxes. For many years, certain business sectors have raised concerns about the BPOL tax, and since the 1970s the tax has been reevaluated and modified a number of times, partly in response to this opposition.

This JLARC study takes another look at the BPOL tax with a particular focus on one proposed change to the BPOL tax basis. The tax is currently assessed on gross receipts, and the study examines the implications of assessing the BPOL tax on net income instead.

KEY FINDINGS

An income-based tax would address many objections raised by businesses about the BPOL tax, in particular its perceived lack of fairness for businesses that generate low or no profits in a particular year. It would reduce the tax burden of businesses to varying degrees. Large businesses, retail businesses, and businesses with low or no profits would benefit the most.

Changing the BPOL tax basis from gross receipts to net income would create new problems, as it would cause a substantial drop in BPOL tax revenue. There appears to be broad agreement that any change to the BPOL tax should be revenue-neutral for localities. To maintain revenue, localities would have to increase BPOL tax rates to about five percent of income, a 40 percent tax increase on profitable businesses, on average. This would represent a significant shift in the local tax burden.

Changing the BPOL tax basis from gross receipts to net income would be challenging and expensive in terms of administration and compliance.

The maximum BPOL rates, which have not been updated since they were established in 1978, could be adjusted so that they better correspond to current levels of profitability across industry sectors. This change would improve the fairness of the tax without adding complexity and administrative burden. Going forward, the rates could be updated at regular intervals to reflect changes in profitability.