

**DEPARTMENT OF TAXATION
2026 Fiscal Impact Statement**

1. **Patron** Emily M. Jordan

3. **Committee** Finance and Appropriations

4. **Title** Individual Income Tax; Tip Subtraction

2. **Bill Number** SB 694

House of Origin:

 X **Introduced**

 Substitute

 Engrossed

Second House:

 In Committee

 Substitute

 Enrolled

5. Summary/Purpose:

This bill would provide an individual income tax subtraction for tip income. The amount of the subtraction would be equal to 25 percent of the federal tip deduction for Taxable Year 2026, and 50 percent of the federal tip deduction for Taxable Years 2027 and 2028.

If enacted during the regular session of the 2026 General Assembly, this bill would become effective July 1, 2026.

6. Budget amendment necessary: No.

7. No Fiscal Impact: (See Line 8.)

8. Fiscal implications:

Administrative Costs

The Department of Taxation (“the Department”) considers this bill as routine and does not require additional funding.

This legislation does not require significant changes to the Department’s systems and is not impacted by the first phase of the Integrated Revenue Management System (“IRMS”) replacement project. No resource constraints or implementation considerations are anticipated.

Revenue Impact

This bill would have a negative General Fund revenue impact of \$18.3 million in Fiscal Year 2027, \$35.2 million in Fiscal Year 2028, \$26.3 million in Fiscal Year 2029, and \$6.1 million in Fiscal Year 2030. No budget amendment is needed because the revenue impact of this bill is assumed in the Introduced Executive Budget.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Virginia's Individual Income Tax Modifications

Federal Adjusted Gross Income

Virginia's Individual Income Tax substantially conforms to federal income tax law by using federal adjusted gross income ("FAGI") as the starting point for computing Virginia income taxes. Virginia law then provides various modifications to FAGI that must be taken into account that figure in determining Virginia taxable income.

Virginia Adjusted Gross Income

When completing a Virginia individual income tax return, a taxpayer starts with the amount of FAGI reported on his federal return. A taxpayer then calculates Virginia adjusted gross income by making two types of adjustments: (1) "additions" which increase the amount of income taxable by Virginia and (2) "subtractions" which reduce such amount. These adjustments are made only to the extent that they have not already been included or excluded from FAGI.

Virginia Taxable Income

The taxpayer calculates his Virginia taxable income by making another type of modification referred to as "deductions," which further reduce the amount of income taxable by Virginia. These modifications are made regardless of federal treatment unless specifically stated otherwise in the provision.

Please find below an illustration of how taxable income is computed for federal and Virginia income tax purposes and how they interrelate:

Federal Income Tax	Virginia Income Tax
+Wages and Other Income	=Federal Adjusted Gross Income ("FAGI")
+Federal Adjustments	+Virginia Additions (only if not included in FAGI)
-Federal Adjustments	-Virginia Subtractions (only if not excluded from FAGI)
=Federal Adjusted Gross Income ("FAGI")	=Virginia Adjusted Gross Income ("VAGI")
-Federal Standard Deduction or Itemized Deductions	-Virginia Standard Deduction or Federal Itemized Deductions (depends on federal election)
-QBI Deduction	-Deduction for Virginia Exemptions
	-Virginia Deductions (regardless of federal treatment)
=Federal Taxable Income	=Virginia Taxable Income

Because this bill would establish a new Virginia individual income tax subtraction, the amount allowed under this bill could be taken whether the taxpayer chooses to take the Virginia standard deduction or itemize their deductions.

Federal Tip Deduction

Under the 2025 H.R. 1, (*Public Law 119-21*) individuals who receive qualified tips may deduct such qualified tip income. The deduction is available for both itemizing and non-itemizing taxpayers in Taxable Years 2025 through 2028.

The maximum amount of the deduction is \$25,000. The deduction phases out for taxpayers with modified adjusted gross income over \$150,000 for single filers and \$300,000 for joint filers. This deduction is claimed after FAGI is calculated and is not part of itemized deductions. Because Virginia starts with FAGI, deductions taken after FAGI that are not itemized—such as this federal tip deduction—do not affect Virginia taxable income. Even if Virginia were to conform to H.R. 1, this deduction would still not flow through, which is why a Virginia-level tip deduction would be needed to provide a deduction specific to the Virginia return.

Proposed Legislation

This bill would provide an individual income tax subtraction for tip income. The amount of the subtraction would be equal to 25 percent of the federal tip deduction for Taxable Year 2026, and 50 percent of the federal tip deduction for Taxable Years 2027 and 2028.

If enacted during the regular session of the 2026 General Assembly, this bill would become effective July 1, 2026.

cc : Secretary of Finance

Date: 01/24/2026 JLOF
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