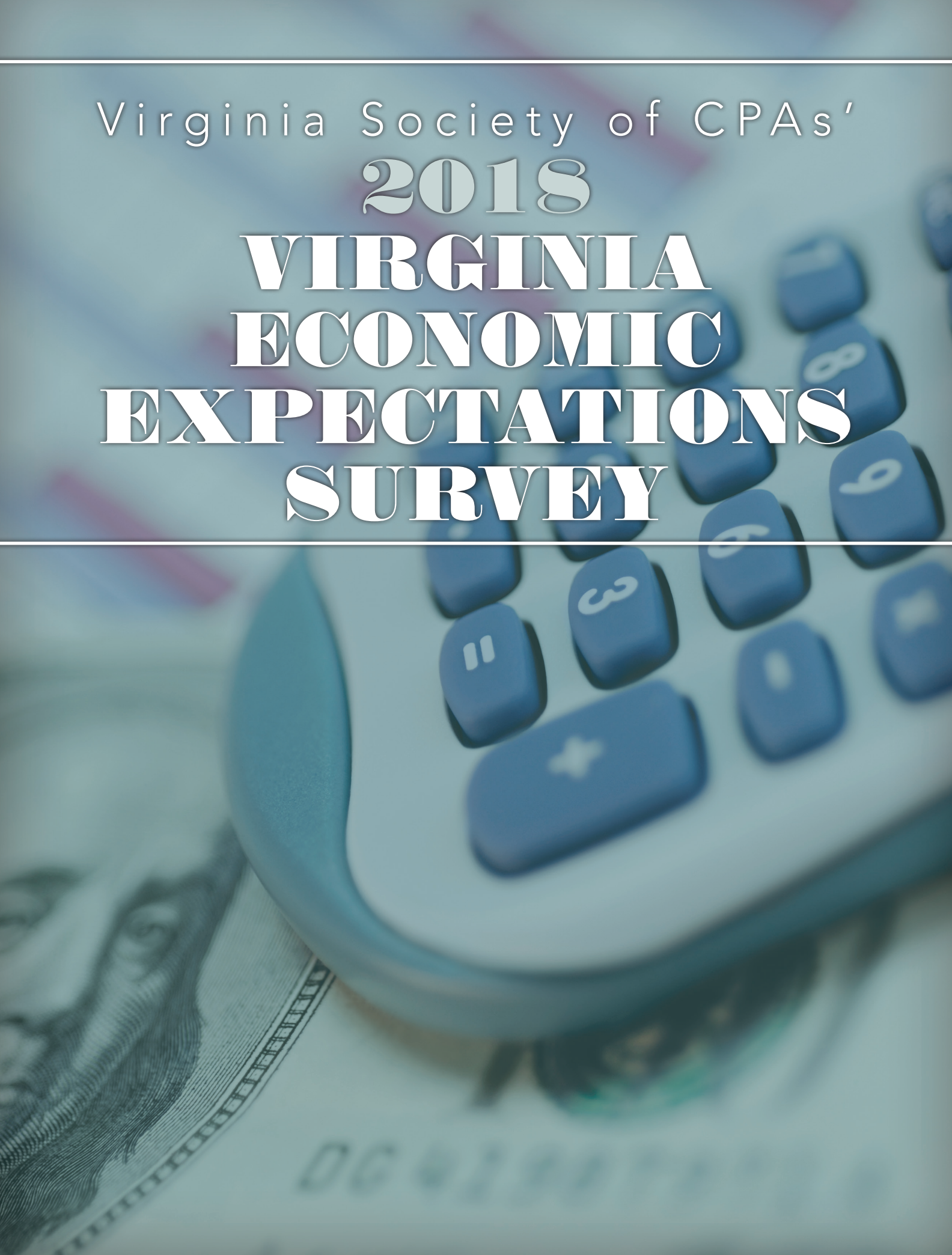


Virginia Society of CPAs'
2018

**VIRGINIA
ECONOMIC
EXPECTATIONS
SURVEY**



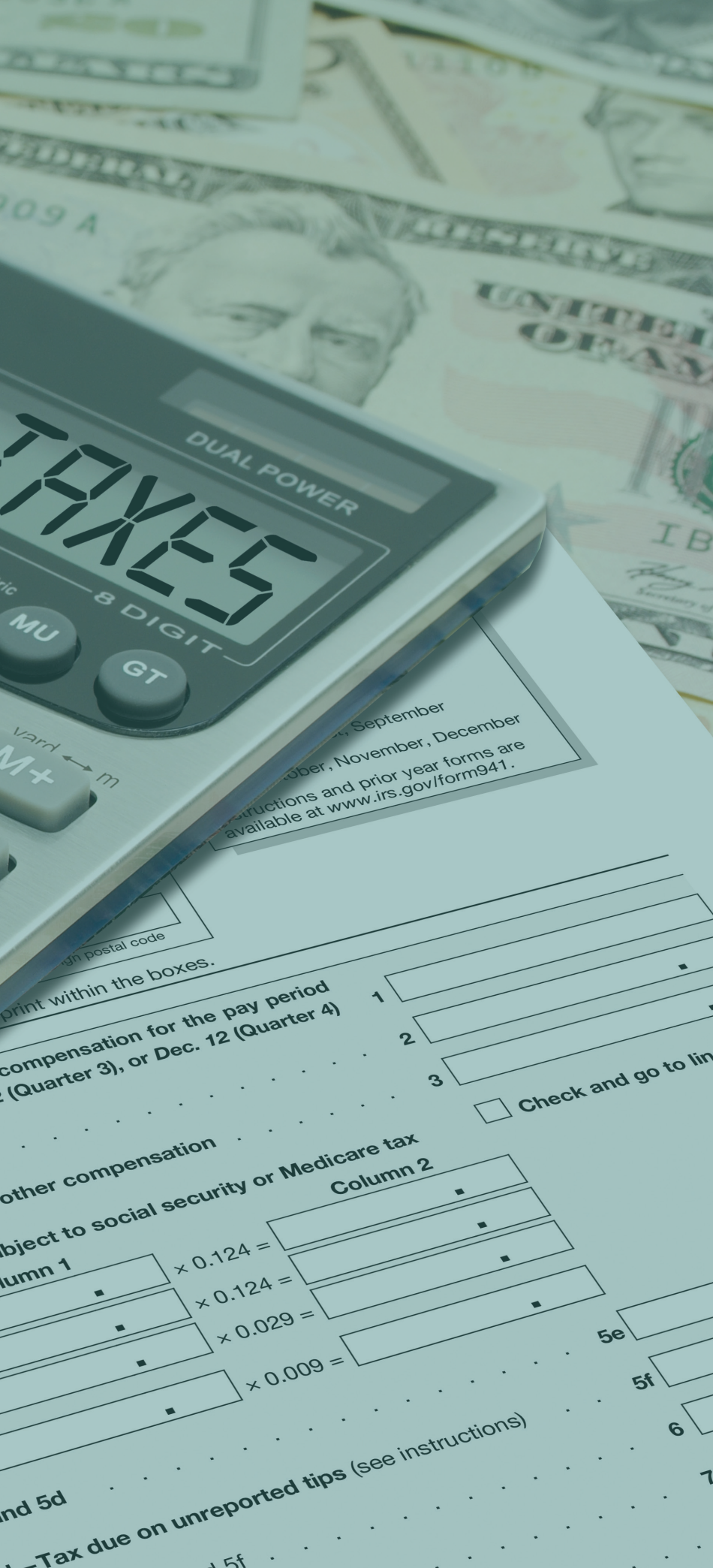
The background of the image is a collage of financial and administrative items. It includes several US dollar bills, including a \$100 bill and a \$50 bill, which are slightly out of focus. A silver and blue calculator is prominently placed in the lower right quadrant. In the bottom right corner, there is a portion of a tax form, likely a W-2, with various line items and numbers visible. The overall color palette is muted, with a light blue/green tint.

Moving forward

The business community looks to Washington and Richmond for answers

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■ SPECIAL REPORT:
**VIRGINIA SOCIETY OF CPAs’
2018 VIRGINIA
ECONOMIC
EXPECTATIONS
SURVEY**

by Veronica Garabelli

Taxes may not be the sexiest issue, but they have been a hot topic lately in Washington and Virginia.

“I can’t really think of the last time I’ve been in a client meeting over the past six months where they haven’t asked me what [I] think that Congress is going to do with tax reform,” says Stephen Kimberlin, a CPA who is senior tax manager at Dixon Hughes Goodman in Richmond. “It goes hand-in-hand. It’s not a Virginia specific issue, but it does affect state taxes greatly.”

A recent survey of Virginia certified public accountants shows that they see tax reform as a major issue that needs to be tackled at the national and state level.

The Virginia Society of Certified Public Accountants’ Economic Expectations survey also highlights other pressing issues, including health care, infrastructure and workforce readiness.

More than 250 accountants throughout the Old Dominion participated in the survey, which offers their viewpoints on the state’s business climate and the top economic issues they expect to impact Virginians in 2018.



Vinod Agarwal, director of the Economic Forecasting project at Old Dominion University, says Virginia's economy is lagging behind the national economy.

Sizing up the economy

When asked about their outlook on next year's economy, a majority of CPAs had positive views about the national economy, but they had conflicting views about Virginia's economy. More than 58 percent were optimistic about the Old Dominion's overall economic climate. Nonetheless, a majority of respondents picked the "economy" as the biggest issue in the upcoming 2018 election, in which all of Virginia's 11 congressional seats and the U.S. Senate seat held by Tim Kaine will be up for grabs.

Vinod Agarwal, an economics professor at Norfolk-based Old Dominion University and director of the Economic Forecasting Project at its Strome College of Business, has reservations about Virginia's economy.

Indecision in Washington is affecting Virginia's economic growth, he says, particularly in areas such as Hampton Roads that still are dependent on federal spending. The commonwealth created about 45,000 jobs from December 2016 to August 2017, Agarwal says, but most of those new positions are concentrated in Northern and Central Virginia. The

other areas in the commonwealth, he says, saw little job growth if not a decline.

"We're still seeing the effects of sequestration and the budget uncertainties in Washington, D.C.," Agarwal says. "When Congress continues to pass [continuing budget] resolutions, that does not really help businesses that depend on this money to plan their activities because they simply do not know what in the world is coming."

He says Virginia's economy is lagging the national economy. The gross domestic product of Virginia and the U.S. will see similar growth this year, but not next year, he predicts.

In 2017, the GDP is expected to increase 1.8 percent in the commonwealth and 1.9 percent nationally. Next year, however, Virginia should see only 1.7 percent GDP growth as opposed to 2.7 percent nationally.

The U.S. also is expected to have a slightly higher job growth rate than Virginia, Agarwal says. U.S. jobs are forecast to grow by 1.5 percent this year and 1.4 percent next year. Virginia should see jobs grow 1.3 percent each year in 2017 and 2018.

Taxing issues

The CPA survey says the commonwealth's tax climate is one of the top two issues that need to be addressed in the 2018 Virginia General Assembly session. (The other big issue is health-care costs.)

Nonetheless, a majority of survey respondents say Virginia's current corporate income tax rate of 6 percent should be maintained.

"I think 6 [percent] is a fair rate," says Gary Dittmer, CPA, a senior tax director at Spok Inc., a Springfield-based health-care communications firm. "Virginia has done well with that. We've attracted a lot of business here."

CPAs, however, say they aren't as pleased with the federal corporate income tax. More than 60 percent say a rate drop would stimulate the economy. President Donald Trump's recently unveiled tax plan seeks to lower the corporate rate from 35 to 20 percent. A plurality of CPAs surveyed were optimistic that tax reform will pass under Trump's administration.

Tax reform has been widely discussed in Virginia politics, too. Both of Virginia's major gubernatorial candidates have called for changes at the state and local level. Ed Gillespie, the Republican nominee, has proposed phasing out the machinery and tools tax; the merchants' capital tax; and the Business, Professional and Occupational License (BPOL) tax, which is based on a company's revenue instead of its profit.

Gillespie also wants to cut individual income tax rates by 10 percent across-the-board. He says this move will impact businesses because most Virginia company owners pay taxes as individuals, not corporations.

"Virginia's antiquated tax code was designed in a bygone era, and our income tax rates have never been lowered since they were established in 1972," his tax plan says.

His Democratic rival, Lt. Gov. Ralph Northam, has advocated exempting startups in rural or economically distressed areas from BPOL and merchants' capital taxes for the first two years of their operation.

Virginia's tax structure has been cited as one of the reasons for

the commonwealth's recent slide in national business rankings. Those lower rankings are the focus of a study underway by the Virginia Economic Development Partnership (VEDP), Virginia Chamber of Commerce and Virginia Tech's Pamplin College of Business.



Moret

"It's not so much that this one thing is a deal breaker or a major obstacle by itself, but ultimately the choices we make across a wide range of public policies will impact the overall

standing of the state," says Stephen Moret, the CEO of the VEDP, which markets the commonwealth to businesses thinking of expanding or locating in the state.

On Dec. 1, the chamber will present its updated business plan, Blueprint Virginia 2025, to the newly elected governor. The document will outline priorities for improving Virginia's business climate, including tax reform. It is based on a recent statewide survey of 6,000 people in the business community.

The Blueprint survey also identified tax reform as a priority for business. A majority of people participating in the chamber's Blueprint said Virginia should start moving forward now with a comprehensive tax reform plan to make Virginia more economically competitive. Thirty-nine percent of respondents to the chamber's survey identified reforming corporate income taxes as the move that would have the greatest impact on improving Virginia's business climate. Thirty-two percent of respondents pointed to personal income taxes, while 29 percent targeted local taxes such as BPOL and machinery and tools.

One issue that has come to the forefront through the rankings study is Virginia's tax burden for new, job-creating business investment projects. Virginia ranks poorly in this area, according to the Tax Foundation's Location Matters study. Its results are factored into national rankings, including CNBC's and Forbes' lists of best states for business.



Virginia's major gubernatorial candidates, Ralph Northam and Ed Gillespie, have advocated for tax reform in Virginia.

"Virginia has very few statutory, by-right incentives to encourage new job creation or investment; hence, our state/local tax burdens for new investment are worse than for existing firms that aren't expanding," Moret explains in an email.

Of course, tax issues vary by industry. According to the Location Matters study, property taxes pose the biggest tax burden for Virginia manufacturers. With a corporate headquarters, the burden is more evenly split among different taxes, including property, sales and income taxes.

The Virginia Manufacturers Association says local taxes are an issue for its members. The organization has been advocating the removal of the machinery and tools tax, which is imposed on manufacturers in every locality in the commonwealth except Virginia Beach.

"We have a member who's been paying the same tax on the same piece of equipment since World War II," says Brett Vasse, VMA's president and CEO.

The price of health care

According to the CPA survey, the biggest obstacle to business growth

continues to be the rising cost of health care. Survey respondents have cited health care as Virginia's most pressing issue for many years. Health-care costs also were identified as the largest area of concern for businesses in the Virginia Chamber's Blueprint survey.

Rising health-care costs are becoming more of a challenge for PBMAres but not a crisis. The company, an accounting and consulting firm with eight offices in Virginia and one in Baltimore, says it has seen a gradual uptick in its health-care costs over the past five years.

"We do our best not to pass costs on to employees when we don't have to," says Mary Aldrich, PBMAres' chief operating officer and partner.

The implementation of the Affordable Care Act (ACA) has been a major part of the health-care debate, but CPAs seem split on whether efforts by Congress to replace the ACA represent an improvement.

A plurality of survey respondents said they were unsure whether replacing or modifying the ACA would be better than current regulations (38 percent). Almost 32 percent said repealing or modifying the law would

be an improvement while 30 percent said it would be detrimental.

Inadequate infrastructure

Another detriment to business, according to the survey, is the commonwealth's infrastructure. Twenty-five percent of respondents picked infrastructure as the most pressing issue for Virginia, behind health-care costs.

The problem is acutely felt in traffic-jammed areas like Northern Virginia and

Hampton Roads. Andrew Martin, CPA, a vice president and principal at Corbin & Co. in Chesapeake, says a big problem in Hampton Roads is the number of water crossings involved in driving from one location to another in the region.

"We need to be able to effectively maintain the roadways and bridges/tunnels that we have as well as efficiently respond to needs for new ones," he says. "This will require a cohesive regional approach to the problem."

Finding the right talent

Roads and bridges aren't the only things that need to be maintained. The commonwealth also must have a competitive workforce. CPAs taking this year's survey say that the availability of an educated workforce and a pro-business climate are the top two factors that have the greatest impact in retaining or attracting businesses.

When asked about the commonwealth's supply of talent, a majority of respondents say there's an adequate labor pool to replenish Virginia's workforce.

Recruiting employees hasn't been an issue at PBMares, but the firm still makes workforce development a high priority.

"Talent is always in high demand to be a leading firm," says Aldrich. "What they're going to be teaching in college will be shifting, and as we gear our company towards the new technologies and align training our own staff and hiring new staff with those technologies, there will be a big race for the right talent — retaining it and attracting it."



Aldrich

Other industries, like manufacturing, are facing a talent shortage.

"We're very dependent on a much more diverse group of talent in order to compete globally," says VMA's Vassey. "We need everybody from research, Ph.D.s to folks that ... work in production."

Partisanship

No matter the issue, whether it is taxes, health care or workforce, finding a solution depends on what happens in Washington and Richmond.

But almost 82 percent of survey respondents say partisanship at the federal and state level is preventing government from addressing urgent business needs.

Take federal tax reform, for example. Martin, the CPA from Chesapeake, hopes that Congress finally takes some kind of action.

"Whatever the rules are, businesses are going to figure out a way to work around, or work with, the rules, for the best benefit," he says. **VB**



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YOUR
BUSINESS
FOR
TOMORROW?

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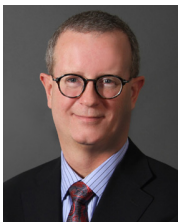
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Hampton Roads

We asked five financial professionals for their take on the state of their region. This is what they had to say.



Andrew Martin

Vice president/principal, CPA
Corbin & Co. PC
Chesapeake

How would you describe the economic climate in your part of the state?

I would generally describe the economic climate as positive and optimistic in Hampton Roads. I think that if regulation and uncertainty could be reduced, things could get even better.

What is your region doing well to retain/attract businesses?

Our region is making it a priority to attract businesses and thus their policy in other areas of governance reflects this and makes it attractive for businesses. One way that this is done is encouraging the community colleges to implement technical courses of training that satisfy the demands of local employers (e.g. welding programs to fit the demand of the ship repair industry in Hampton Roads).

What's the biggest impediment to doing business in the area?

I think the biggest impediment to doing business in Hampton Roads centers around transportation, which is made more difficult by the amount of water crossings required to conduct commerce. We need to be able to effectively maintain the roadways and bridges/tunnels that we have as well

as efficiently respond to needs for new ones. This will require a cohesive regional approach to the problem.

What major economic development project in your region are you most excited about?

I am most excited about the subsea fiber-optic cables that are coming on shore in Virginia Beach from Europe and South America along with the "mega-site" approved in Chesapeake. I think that these two developments will allow our region to further diversify its commercial interests and make us less reliant on Department of Defense spending.

What is the No. 1 item on your tax reform wish list?

That it happens! I think that it is imperative to get business tax reform in place in order to remove the uncertainty for business owners. I think this applies to both federal and state business tax reform in order to allow businesses to develop and implement long-term growth and expansion plans. Once business owners get a commitment from regulators as to what the rules are, they can make commitments to their employees and communities.

Shenandoah Valley

How would you describe the economic climate in your part of the state?

The local and regional economy is doing well. The Valley's economy is fairly diverse and, therefore, does not experience the extreme swings of other regions. The stability and growth of Harrisonburg's biggest sector, higher education, helps the retail, hospitality and construction sectors. Agriculture provides a strong solid base for us as well. There is not one dominant manufacturer or large employer, which gives us stability. Recent population growth from in-migration has helped residential and commercial growth the past few years.

What is your region doing well to retain/attract businesses?

Most of the communities have good economic development programs that emphasize retention and expansion of existing companies. Historically, the communities have not spent nearly the money that other areas have on economic development, specifically on recruitment. But, recent increased commitments to economic development and the regional partnership has changed that.

What's the biggest impediment to doing business in the area?

I don't think there is a major im-

pediment. If I was pushed for an answer, it would be "It depends," maybe a skilled workforce if you need a lot of workers in a short period of time. However, when there has been an identified need, those industries partner with Blue Ridge Community College and Massanutten Technical Center to offer classes and programs to train in the areas of need.

What major economic development project in your region are you most excited about?

In comparison to larger urban areas, we don't have one large economic development project. However, the Hotel Madison and Shenandoah Valley Conference Center has been a wonderful addition to our community and is scheduled to open in early 2018.

What is the No. 1 item on your tax reform wish list?

Simplicity. However, that has to start at the federal level first, and there is little effort or ability to see that take place. The tax implications brought about by the Affordable Care Act need to be made simpler for individuals and businesses. The employer mandate is so complicated and administratively burdensome that businesses have a hard time complying, even with the best intentions.



Michael Garber

Partner, CPA
PBMares LLP
Harrisonburg

Central Virginia



Stephen Kimberlin

Senior tax manager, CPA
Dixon Hughes Goodman LLP
Richmond

How would you describe the economic climate in your part of the state?

The economic climate is positive. When I started practicing in 2008, most of my clients were not reporting positive earnings. Today, while my clients have concerns, things have turned around and they are generally showing positive growth and earnings.

What is your region doing well to retain/attract businesses?

We have a very competitive tax environment. I met recently with a potential client that is considering the Richmond area and a location out of Virginia. One of their biggest concerns was state and local tax compliance requirements and tax rates. Our tax compliance requirements from the state level down to the county level are fairly simple. The particular county they are considering has a favorable local tax structure for their industry. Those factors are attractive to businesses and have put Central Virginia in a position to land new opportunities.

What's the biggest impediment to doing business in the area?

While our area is growing, I would say that the size of Richmond is a small impediment. Some compa-

nies are concerned that they will not have enough talent to support their businesses. However, I would challenge that sentiment by pointing out the numerous surveys noting that Richmond is attracting new residents and the growth of area colleges increases the pool of available talent.

What major economic development project in your region are you most excited about?

I have been interested in craft beers for a while, and it is exciting to see the local breweries experience success and have the ability to expand their operations. We have seen a couple of development projects that have brought/expanded brewery operations in Richmond and other projects that have expanded the reach of Richmond breweries to other markets within Virginia.

What is the No. 1 item on your tax reform wish list?

Certainty for what will happen and when it will happen. I spend most of my time in the tax planning area. It would be helpful for me to have some concrete ideas of what is going to happen. My clients could also plan and run their business more effectively if they knew what to plan for.

Northern Virginia

How would you describe the economic climate in your part of the state?

Based on my observations, the economic climate in Northern Virginia is good. The job market is competitive; we are trying to hire a few positions and candidates are receiving multiple offers; restaurants are crowded for lunch and dinner, and there is no relief from the traffic.

What is your region doing well to retain/attract businesses?

Economic development is an important activity of our local county/city governments and they are in competition with each other. Being close to Washington, D.C., is an advantage.

What's the biggest impediment to doing business in the area?

Traffic must be the major impediment, which is partially offset by the EZPass [electronic toll collection] system. We have frequent meetings in Tysons Corner (about 10 miles from Springfield) and before EZ Pass, a trip from Springfield to Tysons could take over one hour. Now with EZ Pass it's less than 30 minutes. Most of my colleagues agree with me and will pay any amount to avoid sitting in traffic.



What major economic development project in your region are you most excited about?

Infrastructure projects, like the extension of the Metro System to Dulles Airport; expanding the EZ Pass lanes to I-395 in Arlington; and improvements to I-66. Any project to alleviate traffic is going to add to the quality of life and attract businesses to come and remain here.

What is the No. 1 item on your federal tax reform wish list?

Lowering the corporate tax rate from 35 percent would make our corporations more competitive with the rest of the world.

Gary D. Dittmer

Senior tax director, CPA
Spok Inc., *Springfield*

Southwest Virginia



Tamara R. Greear

Partner
Thrower, Blanton & Associates PC
Norton

How would you describe the economic climate in your part of the state?

The current economic climate in Southwest Virginia is somewhat pessimistic. While there has been a marginal improvement in the region with some of the deregulations on the coal industry since the beginning of 2017, there is still very little progress towards a steady or growing economy.

What is your region doing well to retain/attract businesses?

The University of Virginia's College at Wise, along with the workforce development programs of the various community colleges in the region, are working diligently to provide education and training that will develop a workforce that can adapt to a changing economic environment. The biggest challenge is knowing what the appropriate skills will be in an area that must generate new forms of business and industry, but has yet to establish what businesses can be best developed for sustainable growth in the region.

What's the biggest impediment to doing business in the area?

There is not just one big impediment, but a combination of contributors. The natural terrain of the area provides challenges to affordable and efficient transportation/transit of goods and services and basic communication through a lack of high speed Internet and

cellular service. Such challenges make attracting and retaining new businesses difficult at best, and impossible to an extent. The other significant impediment is a lack of a diverse skilled labor force ready to meet the challenges of any business.

What major economic development project in your region are you most excited about?

There is not a specific economic development project in the region that excites me as our region is struggling to develop new opportunities in an extremely distressed economy that has for too long been dependent on one primary industry/product for survival without a forward-thinking vision that would sustain our region in times of downturn or distress.

I am, however, optimistic about the regional efforts that are emerging, such as groups like GO Virginia [an economic development initiative], just to mention one ... This is a positive move outside of what tends to be a "town by town" attitude to the realization that we are one community in this together.

What is the No. 1 item on your tax reform wish list?

I'd say start with reducing the tax brackets for individuals to no more than perhaps 4 brackets not exceeding 35 percent, and also reducing the corporate tax bracket to somewhere around 15-20 percent.

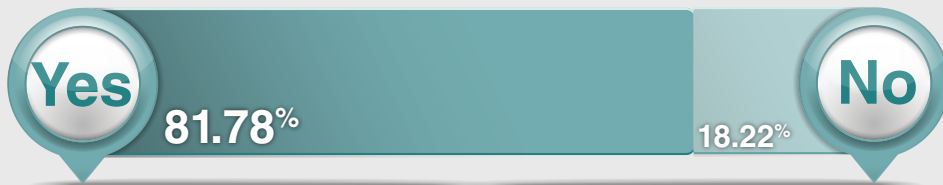
The results

Virginia Society of Certified Public Accountants' (VSPCA) Economic Expectations report highlights several key issues impacting Virginia businesses, ranging from the economy to taxes and workforce. The survey was sent to 7,584

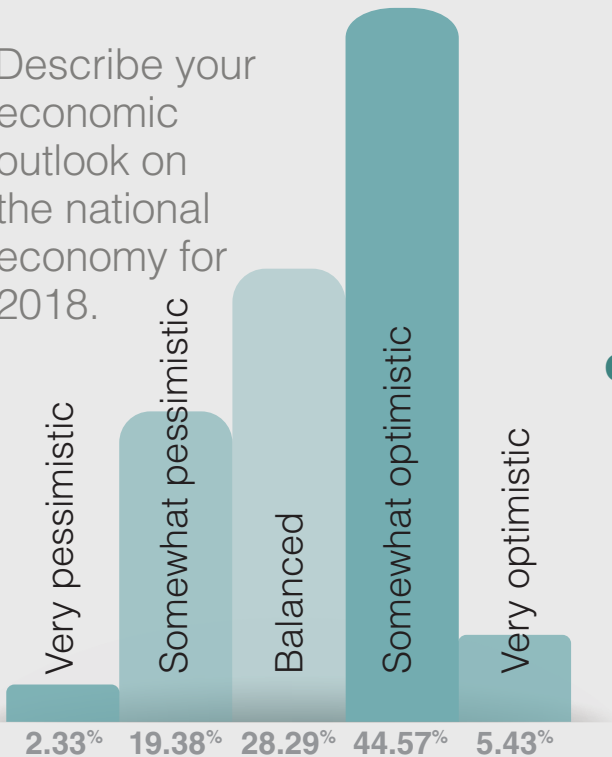
VSCPA members in August. The survey had 258 respondents, yielding a 3.4 percent response rate. More than 49 percent of the respondents work in public accounting. The rest work in business and industry and other sectors.

A majority of people taking the survey (55 percent) represented businesses with more than 50 employees; 37 percent represented companies with between two and 50 workers; and 8 percent had sole proprietorships.

Q1 Do you believe the U.S. economy is moving in a positive direction?



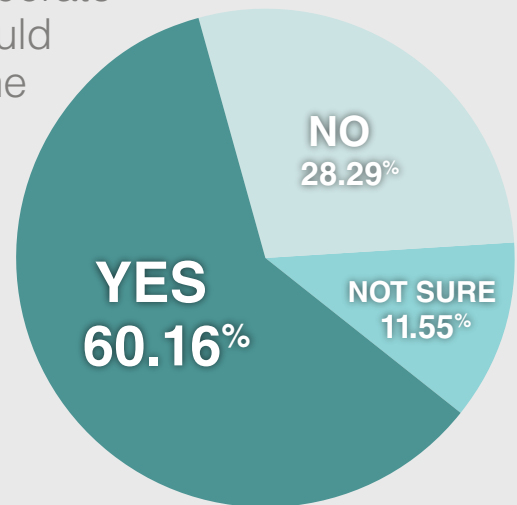
Q2 Describe your economic outlook on the national economy for 2018.



Q5 Republicans and Democrats have proposals to replace or modify the Affordable Care Act (Obamacare). Are these proposals an improvement over the current law?

Yes: 31.87% No: 30.28% Not sure: 37.85%

Q8 Do you think a drop in the federal corporate tax rate would stimulate the economy?



Q3 Is partisanship at the federal and state level preventing government from addressing urgent needs that have an impact on business?

Yes: 81.89% No: 7.09% Don't know: 11.02%

Q6 Do you expect that tax reform will pass under President Trump's administration?

Yes: 47.20% **No: 29.20%** **Not sure: 23.60%**

Q7 Do you think the new administration's initiatives are having a positive, negative or neutral effect on the economy and business?

Positive: 41.43% **Negative: 31.47%** **Neutral: 27.09%**

Q12 In 2018, do you think capital investments in Virginia will increase, decrease or stay the same?

Increase: 53.04%

Decrease: 4.45%

Stay the same: 42.51%

Q13 The Virginia corporate tax rate is 6 percent. Should Virginia maintain, decrease or increase the rate?

Maintain: 68.70%

Decrease: 26.42%

Increase: 4.88%

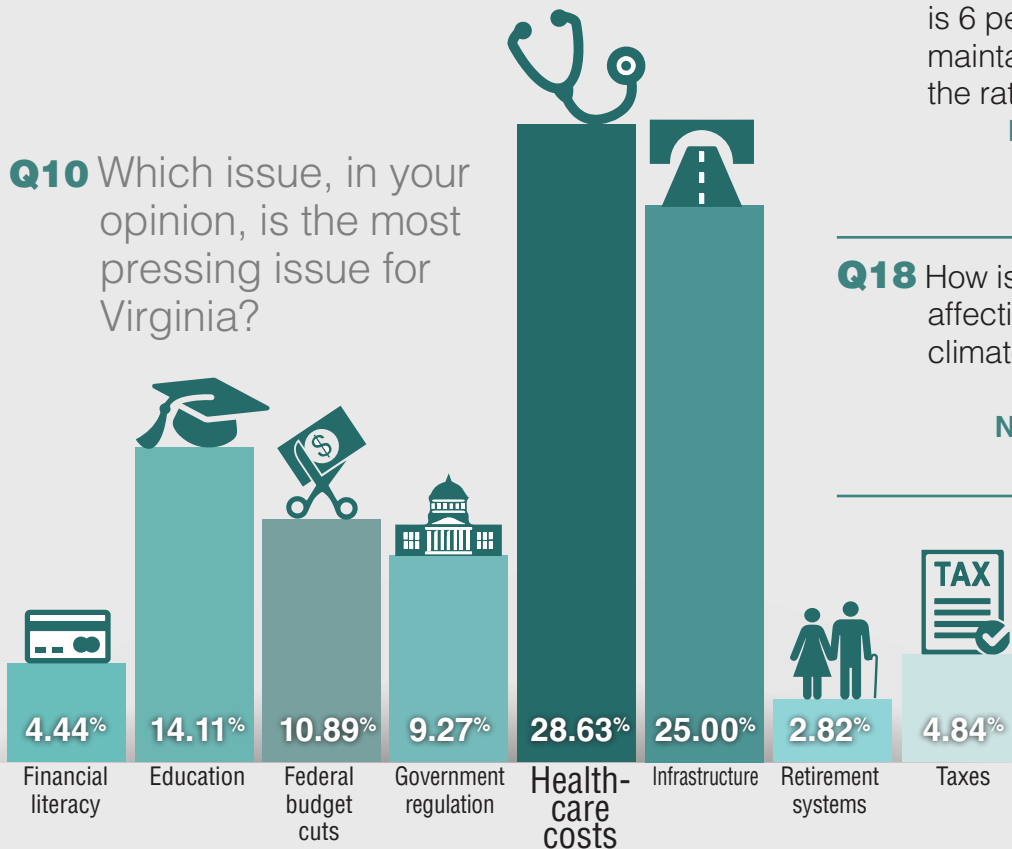
Q18 How is the regulatory environment affecting the overall economic climate?

Positively: 4.60%

Negatively: 53.56%

Neutral: 41.84%

Q10 Which issue, in your opinion, is the most pressing issue for Virginia?



Q11 How would you rate the overall business climate in Virginia as compared to that of neighboring states?

Excellent: 13.31%

Good: 69.35%

Fair: 16.13%

Poor: 1.21%

Q19 Which TOP TWO issues need to be addressed in the 2018 session of the General Assembly?

Health-care costs: 86.19%

Tax climate: 48.12%

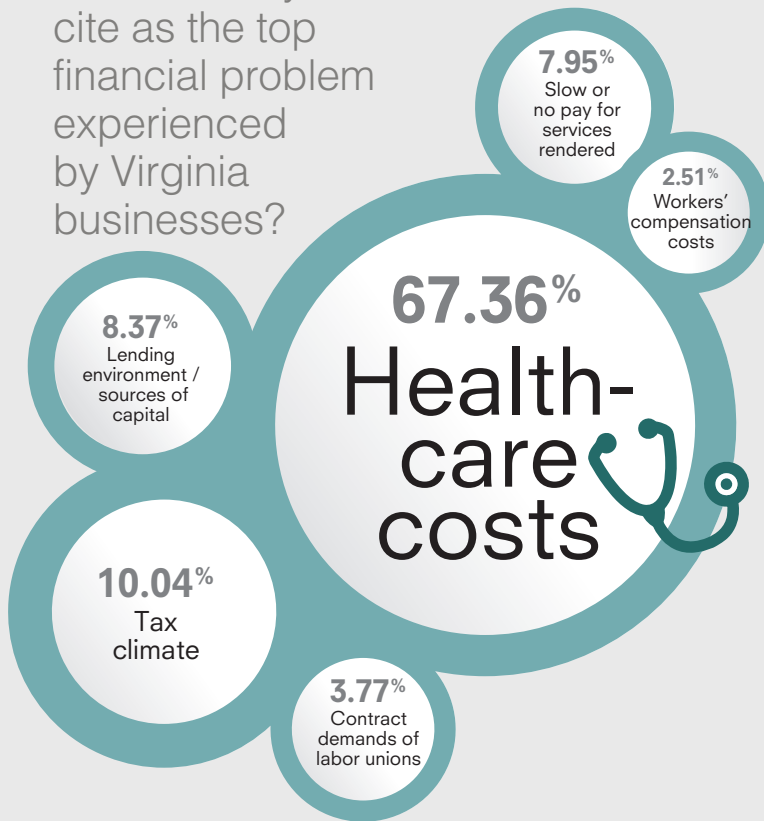
Lending environment / sources of capital: 19.67%

Slow or no pay for services rendered: 12.13%

Contract demands of labor unions: 11.72%

Workers' compensation costs: 6.69%

Q17 What would you cite as the top financial problem experienced by Virginia businesses?



Q28 Does your company, firm or organization anticipate increasing, maintaining or decreasing revenues in 2018 based on the past year's revenue?

Increasing: 64.19%

Maintaining: 26.64%

Decreasing: 9.17%

Q31 Has your region done enough to lessen its dependence on federal spending?

No: 79.87%

Yes: 20.13%

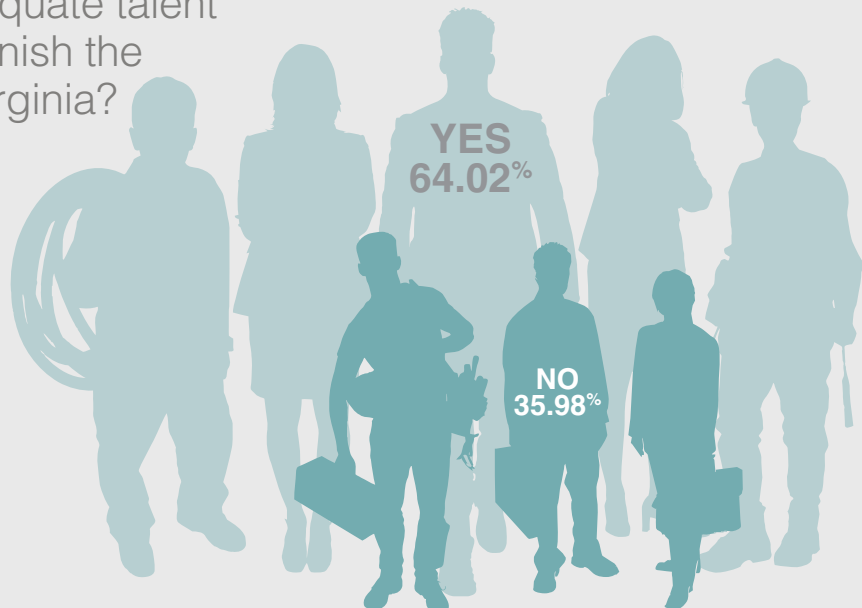
Q22 Do you believe Virginia small businesses currently have access to adequate credit to sustain and grow their businesses?


Yes: 43.51%

No: 25.10%

Don't know: 31.38%

Q23 Is there an adequate talent supply to replenish the workforce in Virginia?



A photograph of a man and a woman in conversation. The man, in the foreground, has grey hair and is wearing a blue denim shirt. He is looking down and to the left with a serious expression. The woman, in the background, has dark hair and is wearing a pink top. She is looking towards the man. The background is a warm, out-of-focus indoor setting.

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