Fiscal Research Program

AN ANALYSIS OF THE ECONOMIC CONSEQUENSES OF MODIFYING THE PROPERTY TAX ON MOTOR VEHICLES IN GEORGIA : ALTERNATIVE PROPOSALS AND REVENUE EFFECTS

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EXECUTIVE SUMMARY

Introduction

Over the past year, there has been increased interest in Georgia and elsewhere in the idea of sharply reducing the property tax levied on motor vehicles. In 1998, legislatures in three states, Virginia, South Carolina, and California proposed bills which would, over time, eliminate or reduce the property tax on motor vehicles in those states.

In 1996, Georgian counties and municipalities collected $474 million from property taxes levied on motor vehicles. Of the total motor vehicle property tax revenues in 1996, 28 percent went to county governments, 57 percent to school districts, 14 percent to cities and special districts, and 1 percent to the state.

Proposal Descriptions and Estimates

At this time three states, Virginia, South Carolina, and California, have proposed to reduce or eliminate the property tax on motor vehicles, each state taking a slightly different approach to the issue. Virginia has adopted legislation, and after the research for this paper was conducted, Governor Pete Wilson of California signed legislation that would reduce the motor vehicle property tax rate by 25 percent initially, and by 67 percent when fully implemented. Although the South Carolina proposal had strong support in both houses of the legislature, it was delayed prior to final passage; no vote was taken before the close of the 1998 session. The California proposals considered are a proposal by Governor Wilson and a proposal introduced into the California State Assembly. For each of these four proposals, the revenue, distributional, and administrative implications for Georgia of adopting each proposal are considered. (More detail can be found in the full report from which this Policy Brief is drawn.)

Virginia Proposal

The Virginia approach eliminates the property tax on the first $20,000 of market value of a personal-use motor vehicle, which includes all personal passenger cars, motorcycles, and pickup or panel trucks. The tax reduction is phased-in over a 5-year period. The state government is to reimburse local governments for the loss of revenue, but based on the 1997 millage rate.

If adopted in Georgia the proposal would, when fully phased-in, completely eliminate the tax on over 80 percent of the vehicles currently subject to tax. This percentage would decrease over time as more new vehicles exceed the $20,000 ceiling. On average, each vehicle owner would receive a refund in 1999 of $12 per vehicle, and $79 per vehicle when the legislation is fully phased-in. This amount is dependent on each jurisdiction's actual millage rate and will vary widely across localities in Georgia.

South Carolina Proposal

The South Carolina proposal is designed to completely eliminate the property tax on all motor vehicles, personal and commercial. This proposal caps local government receipts from the property tax at their 1998 level. The proposal creates a property tax relief fund which is created by using annual state contributions of 30 percent of the increase in state revenue and is designed to reimburse localities for the loss in revenues stemming from the elimination of the property tax. If adopted in Georgia, this proposal would, when fully implemented, eliminate the tax on over 5 million personal and business use vehicles and result in an average tax savings of approximately $100 per vehicle.

California Proposals

Instead of a motor vehicles property tax, California levies an in-lieu tax, also called a privilege tax, referred to as the Vehicle License Fee. Californians pay an amount equal to 2 percent of the value of the motor vehicle. The tax rate is levied at the state level and is applied to all vehicles. Two bills reduce or eliminate this tax on motor vehicles are considered, one developed in the California Assembly and one proposed by Governor Wilson. Similar to the other state bills, each of the California proposals include for some kind of reimbursements to the local governments.

Assembly Bill 1776. This proposal phases-out the Vehicle License Fee in a manner very similar to the Virginia plan. The plan, as drafted, would apply only to noncommercial vehicles. Under this bill, the market value of all noncommercial vehicles is reduced in $5,000 increments until 2003, at which point the tax is completely eliminated. If adopted in Georgia, in 1999 the average tax savings per vehicle would be $28, which would increase to $81 when fully phased-in.

Governor Wilson's Plan. Governor Wilson has proposed a gradual reduction of this tax by cutting the state-wide tax rate from 2 percent to 1 percent in 1999 and to 0.5 percent in 2002. This tax reduction would apply to both personal and business use motor vehicles. His proposal also calls for an annual reimbursement to the localities for the loss in revenue. If adopted in Georgia, the average tax savings in 1999 per vehicle would be $59, which would increase to $96 when fully phased-in.

Table 1 shows the estimated magnitude of the cut in taxes for each of the four proposals if adopted in Georgia. Those plans that include commercial vehicles result in substantially greater loss in revenue. Placing a high cap on the value subject to the reduction (i.e., the Virginia proposal), results in almost the same revenue loss as a proposal with no cap at all (i.e. AB 1776).

Table 2 shows the manner in which the tax cut would be distributed across income classes for the Virginia and Governor Wilson plans. The distributional analysis reveals a progressive tax cut, which is not surprising given that motor vehicle ownership is highly correlated to income. The distribution of the tax cut is essentially the same for each of the proposals other than Governor Wilson's. Under the Wilson plan the tax savings for each income class is less than that experienced under the other plans, but the tax saving is still progressive.

Administrative Issues

The administrative issues associated with these proposals will vary depending on the proposal adopted. Many of the issues discussed below are based on the experience of implementing the Virginia proposal.

One issue which all proposals must face has to do with the determination of eligibility for the proposals that limit the tax break to personal use vehicles. One option is to make the vehicle ineligible if a vehicle owner takes a Federal tax deduction for business use of the vehicle. Verifying this status could be done by requiring a copy of the Federal tax return or by random audits.

This issue becomes particularly problematic in the case of leased vehicles. The proposals require that the leasing companies notify the Department of Revenue as to which vehicles are used for personal use. This information is not currently collected and would place a great burden on the leasing company.

In Georgia not all the taxing jurisdictions have the same fiscal year for their budget process. This creates some difficulty in terms of reporting and reimbursements. These proposals require input from both the county treasurer and from the county tax commissioner, which in Virginia required establishing new lines of communication and cooperation.

The sheer number of taxing jurisdictions (well over 1,000) will cause a paperwork and tracking ordeal. The Virginia legislation includes some funds to bring electronic information transfer to the local taxing jurisdiction. This will aid the state in determining the appropriate level of reimbursement and also in their audit procedures. Furthermore, there currently exist several districts in Georgia that appraise property at values other than 40 percent, so adjustment will have to be made for that. Lastly, there is no unique district identifier used by all state and local departments in Georgia, which creates a confusing system of data collection and information exchange.

All of these issues are solvable but the state and local governments will likely require additional resources in the form of additional staff and computers to audit, track, collect and transfer the needed information to the state level.

Conclusions and Policy Recommendations

The following are conclusions and recommendations based on the analysis of the several proposals to eliminate or reduce the property tax on motor vehicles.

- All these proposals offer well constructed models for other states to follow. While in each case there exist some problems with implementation, these can be overcome with advanced preparation and greater information.

- The stated objective of this tax cut has always been a bit vague. The major criticism of this tax, as opposed to other taxes, is that it is due as a lump sum payment. This can create a true financial burden for some households. This burden will be much greater, though, in states that base the tax on the full market value of the vehicle, such as California and Virginia.

- By requiring the state to reimburse the localities for the revenue loss associated with this exemption, the tax is simply shifted from the local level to the state level. In doing this, the tax becomes hidden from the taxpayers. The "exempted" motor vehicle value is not truly exempted but merely paid by the state taxpayers. But since state tax payments are due on a periodic basis or through payroll deduction, the obligation (i.e. the tax on motor vehicles shifted to the state taxpayers) is paid over time.

- A reduction in the tax will likely not result in an increase in motor vehicle consumption.

- Reducing or eliminating the tax will in the short run reduce the tax bill of state residents in a visible and straightforward manner by reducing or eliminating their annual property tax bill for motor vehicles. On the other hand, the long run consequences of a reduction or elimination may be quite different.

- These proposals are unlikely to reduce local government spending. The elimination of the motor vehicle tax base means that increased expenditures will have to be financed from a smaller property tax base, or from other revenue sources. The same would be true if the state does not fully reimburse local government for the reduction in revenue. To the extent there is a shift from property taxes to a sales tax or fees, the result would be a reduction in Federal income tax deductions for individuals who itemize their taxes, thus increasing the tax burden of individuals who itemize deduction on their tax return.

- The long run consequences depend on the growth of state revenues. While these proposals decrease taxes at the local level, they increase spending at the state level due to their reimbursement requirements. In times of budget surpluses or high growth this new obligation may not seem burdensome. (By way of comparison, the recent state income tax cut was $205 million.) Problems in fulfilling the obligation may arise, though, in times of decreased state tax revenues. During the initial phase-in period these proposals contain special provisions to limit the claims of the state reimbursements on the state budget in case of a decline in state revenues. With these provisions in place the state will only allow an exemption level which can be afforded by the current level of revenues.

- Once the proposal is fully phased-in it becomes less clear what happens to the state reimbursements in the event of a decline in state revenues. In the Virginia and South Carolina proposals some provisions are included to deal with this contingency, but none which would completely guarantee full reimbursement in the event of a decline in state revenues after the exemption has been fully phased-in.

- In addition to limiting the tax base of all localities, the modification to the property tax base will affect some localities more than others. If state reimbursements are tied to historical revenue collections, there is no accommodation made for future growth. In the Virginia proposal state reimbursements are based on the locality's millage rate in the initial year. While millage rates do rise and fall from year to year, over time these rates tend to follow an upward trend. Therefore, over the long run localities will likely face a decreasing reimbursement in real terms.

- Lastly, incursion of the state into the taxing domain of the localities is likely to meet with opposition from local public officials. Although localities are granted the privilege of taxation from the state, many local officials will see this effort to reduce the public’s tax burden as an effort to erode the localities’s power.

In conclusion, the merits of this tax are best judged when the proposal is considered in its true light. The real advantage of these motor vehicle proposals come from making the motor vehicle tax payable over time and redistributed over all state taxpayers. A true tax cut may occur only if neither state nor local governments increase their taxes due to this "exemption". The disadvantage of these proposals comes in the form of increased risk to the local governments that future reimbursements will be curtailed. In addition, because these reimbursements are tied to historical collections or previous millage rates, they erode the tax base under the control of the local governments.

AN ANALYSIS OF THE ECONOMIC CONSEQUENCES OF MODIFYING THE PROPERTY TAX ON MOTOR VEHICLES IN GEORGIA: ALTERNATIVE PROPOSALS AND REVENUE EFFECTS

I. Introduction

Nothing excites Americans like tax breaks and automobiles. Thus, it is hard to imagine a more potent tax proposal than one which lowers the tax on automobiles. Over the past year, there has been increased interest by legislators in the state of Georgia and elsewhere in the idea of sharply reducing the property tax levied on motor vehicles. In 1998, legislatures in four states (Virginia, South Carolina, California, and Missouri) proposed bills which would, over time, eliminate or reduce the property tax on motor vehicles in those states. With vehicle ownership so widespread, this is an appealing idea from which most citizens can benefit.

In 1997, 28 states included motor vehicles in the property tax base or imposed some other sort of property-like tax on their motor vehicles. The bulk of this revenue went to fund sub-state level government budgets. Traditionally, school districts have relied almost exclusively on revenues from property taxes. In addition, counties, cities and special districts such as fire and transit also receive significant funds from property taxes.

In 1996, Georgian counties and municipalities collected $7.0 billion from property taxes levied on tangible real and personal property. Of this, $474 million came from property taxes levied on motor vehicles. This compares to total county and municipality sales tax receipts of $1.4 billion and excise tax receipts of $516. Of the total motor vehicle property tax revenues in 1996, 28 percent went to county governments, 57 percent to school districts, 14 percent to cities and special districts, and 1 percent to the state.

Each county, municipality, school district and special district applies their own millage rate to the taxed property. In 1996, county millage rates ranged from a low of 11.00 mills to a high of 48.35 mills. By state law all tangible real and personal property including motor vehicles is assessed at 40 percent of its market value. The assessed value is multiplied by the applicable millage rate to determine the tax due.

From a policy standpoint, the rationale for including or excluding motor vehicles in the tax base is unclear. Some may argue that vehicle ownership is a necessity and as such should not be taxed. Traditionally, items deemed to be necessary for employment are not included in the Federal income tax base and are usually excluded from state sales tax bases. Under current law, Georgia only applies the property tax to 40 percent of the vehicle's market value and allows the remaining 60 percent to go untaxed. Thus, it could be argued that the untaxed 60 percent represents the exemption for the "necessary" portion of the vehicle value.

Furthermore, it could also be argued that eliminating the tax encourages motor vehicle consumption at a time when traffic problems in Georgia abound. Although, since motor vehicles are taxed at only 40 percent of their market value, changes to the tax structure will likely have little direct effect on automobile consumption. It is more likely that individuals will experience a slight increase in their disposable income and consumption of all items will increase.

From a political standpoint this is a very popular proposal. It is easy for the general public to understand. And with 4.8 million motor vehicles in Georgia in 1997 this issue applies to almost all citizens. In an era of rising automobile prices, proposals which decrease the cost of vehicle ownership should find strong public support.

The objective of this paper is to provide an analysis of the economic consequences of eliminating the property tax on motor vehicles and to explore the manner in which this may be accomplished. The paper outlines the major elements of several proposals, and provides estimates of the fiscal and distributional consequences associated with each proposal. In addition, the report discusses the hurdles discovered in implementing such a proposal. In conclusion, the paper offers several policy recommendations designed to aid policymakers in their decisions regarding this issue.

II. Description of Proposals

At this time there are four states, Virginia, South Carolina, California, and Missouri which have proposed to reduce or eliminate the property tax on motor vehicles. Each takes a slightly different approach to the issue. Only the Virginia proposal has been signed into law.[1] Although the South Carolina proposal had strong support in both houses of the legislature, it was delayed prior to final passage; no vote was taken before the close of the 1998 session. Governor Pete Wilson of California has proposed (using the existing state budget surplus) to fund a reduction in the California property tax on motor vehicles. In addition, other bills have been introduced into the California state Assembly which would also severely curtail the tax. Table 1 provides a summary of the four proposals.[2]

[1] After the initial research for this paper was conducted Governor Pete Wilson of California signed legislation that would reduce the motor vehicle tax rate by 25 percent initially, and by 67 percent when fully implemented.
[2] Due to lack of support, the Missouri proposal is not reviewed here.

Table 1. Summary of State Proposals to Modify the Tax on Motor Vehicles

Bill Specifications	*Virginia*	*South Carolina*	*Ca. - AB 1776*	*Ca. – Wilson Proposal*
Mechanism for tax cut	State pays 12.5% of tax on first $20,000 of vehicle value in 1998, 27.5% in 1999, 47.5% in 2000, 70% in 2001, and 100% in 2002	Creates a property tax relief fund with an initial state investment of $25 million. State annually contributes 30% of all new revenues into the fund until fund reaches level equal to 1998 property tax collections.	Levies tax on vehicle value in excess of $5,000 in 1999; on $10,000 in 2000; on $15,000 in 2001; on $20,000 in 2002; and eliminates tax completely in 2003.	Reduces the state imposed Vehicle License Fee from its current rate of 2% to 1% in 1999; to 0.5% in 2000.
Level of final reduction	Eliminates the tax from the first $20,000 of vehicle value.	Eliminates all tax on *all personal property* – not limited to motor vehicles.	Eliminates all in-lieu taxes on motor vehicles.	Lowers the state levied tax rate by 75%.
Reimbursements to local gov't.	Full reimbursements based on 1997 millage rates.	Provides for annual reimbursements based on amounts in relief fund.	Allows for reimbursements to be made based on loss of revenue due to the exemption.	Reimburses local governments for loss of revenues associated with this exemption.
Criteria for exemption	Personal use vehicles.	Business and personal use.	Applies only to personal use vehicles.	Applies to both business and personal use vehicles.
Budget safeguards	Limit reimbursements to 8.5% of annual state budget.	Reimbursements are limited to new revenues.	N/A	N/A

Virginia Proposal

The Virginia approach, first outlined by then Virginia gubernatorial candidate Jim Gilmore, gradually eliminates the property tax on the first $20,000 of value of a motor vehicle. In Virginia, property is assessed at 100 percent of fair market value. The bill also immediately eliminates 100 percent of the tax on vehicles with value of $1,000 or less. A motor vehicle for purposes of this legislation includes all personal passenger cars, motorcycles, and pickup or panel trucks. Commercial cars, fleet vehicles, and business-use autos are not eligible for the exemption. The proposal applies equally to owned and leased motor vehicles and to both new and used vehicles.

For vehicles with an assessed value in excess of $1,000 the tax reduction is phased-in over a 5-year period according to the following schedule:

Table 2. Phase-In Schedule for Virginia

Year	**Percent**
1	12.5%
2	27.5%
3	47.5%
4	70.0%
5	100.0%

In an effort to protect the fiscal freedom of the localities, the proposal requires that the state reimburse the taxing jurisdictions for the loss in revenue stemming from the reduction in the property tax base. In year one, vehicle owners are reimbursed directly by the state for 12.5 percent of the full exemption amount, which is defined as the value of the motor vehicle up to $20,000 multiplied by the taxing jurisdiction's 1997 motor vehicle millage rate. Vehicle owners pay their full property tax bill to the local taxing jurisdiction and receive a reimbursement directly from the state. This gives the localities a period of time to implement the appropriate accounting and record keeping practices required for handling the exemptions. In years 2-5, vehicle owners pay a property tax bill to the taxing locality equal to the tax on the first $20,000 of value of the vehicle times the phase-in percentage, plus the full tax on the value of the vehicle in excess of $20,000. The taxing jurisdictions are then reimbursed by the state for the lost revenue. However, reimbursements are always based on the 1997 millage rates. This means that increases in local millage rates would not be matched by the state. For example, if a locality increased its millage rate, it would only apply to the vehicle value in excess of the exemption amount. The state would continue to reimburse the locality based on the original millage rate for the vehicle values below $20,000. To the extent that localities continue to view their tax base as the entire vehicle value, this may be viewed as a revenue loss since they are not compensated by the state for the new revenues on vehicle values below $20,000. On the other hand, local governments would not lose any revenue provided they do not raise millage rates from their 1997 levels. Given the volatility of millage rates among the hundreds of taxing jurisdictions within the state, tying the reimbursement rate to one millage rate dramatically reduces the administrative costs associated with the proposal. It also prevents a locality from increasing their state subsidy by increasing their millage rate.

The proposal also contains a budget shortfall provision which states that if state revenues fail to increase by at least 5 percent, the tax reduction and associated reimbursements from the state to the taxing jurisdictions will remain at their current level and not increase as scheduled. For example, if in fiscal year 2000 it is determined that actual state revenues collections will not increase by 5 percent in the next fiscal year, then for the calendar year 2001 the taxpayers would receive a 27.5 percent reduction and the state would reimburse the taxing jurisdictions 27.5 percent of the exempted revenue as opposed to increasing the tax reduction to the scheduled 47.5

percent. The schedule may be delayed annually until there are sufficient general fund revenues to cover the additional state obligations created by the reimbursements. Furthermore, no more than 8.5 percent of general fund revenues may be used as reimbursements in any fiscal year. If it is forecasted that more than 8.5 percent of general fund revenues are required, then the reimbursements would be adjusted so as not to exceed 8.5 percent of general fund revenues.

South Carolina Proposal

The South Carolina proposal was designed to completely eliminate the property tax on all motor vehicles, both personal and commercial. As drafted, the proposal would actually eliminate the tax on all personal property defined as "all other personal property." [3] This would include motor vehicles, boats, airplanes, and business personal property. For purposes of this paper the analysis and discussion are limited to the elimination of the tax on motor vehicles.

Under this proposal, local government receipts from the property tax are capped at their 1998 level. The proposal creates a property tax relief fund, the purpose of which is to reimburse localities for the loss in revenues stemming from the elimination of the property tax. Each year the South Carolina Board of Economic Advisors places in the fund 30 percent of all new state revenues plus the total of all amounts previously credited to the fund. [4] Once the fund reaches an amount equal to the 1998 property tax receipts, all personal property classified as "other personal property" is wholly exempt from the property tax.

The bill specifies that the Commissioner of the Department of Revenue calculate and design a local government reimbursement formula to redistribute the funds in the Property Tax Relief Fund. Such a formula would probably be based on historical collections but could vary since in the early years the amount of funds to be redistributed are not linked to actual collections by the localities. Once the plan is fully implemented, reimbursements should match historical

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[3] "Other personal property" includes motor vehicles, boats, airplanes, and business personal property.
[4] New revenues are defined as general fund revenues in excess of the previous year's revenues.

collections by the localities. The legislation also requires that during the phase-in period local governments adjust their millage rates such that the sum of current property tax receipts and state reimbursements do not exceed their 1998 property tax receipts. Furthermore, the statute specifically prohibits the taxing entities from adjusting their millage rate to exceed the 1998 rate in an effort to collect additional revenues from a shrinking tax base.

California Proposals

Currently, instead of a property tax California levies an in-lieu tax, also called a privilege tax on automobiles. Referred to as the Vehicle License Fee, Californians pay an amount equal to 2 percent of the value of the motor vehicle. The tax rate is levied at the state level and is applied to all vehicles regardless of their locality of residence. The revenues are redistributed to the localities per a redistribution formula.

There are several bills in the California Assembly and proposed by the Governor to reduce or eliminate this tax on motor vehicles. Similar to the other state bills, each of the California proposals include some kind of reimbursements to the local governments.

<u>Assembly Bill 1776</u>

This proposal phases-out the Vehicle License Fee in a manner similar to the Virginia plan. This legislation, as currently drafted, would apply only to noncommercial vehicles but would apply to the full value, not the first $20,000 as in Virginia. Under this bill, the market value of all noncommercial vehicles is reduced by $5,000 in 1999, by $10,000 in 2000, and so forth until 2003 at which point the tax is completely eliminated.

Table 3. Assembly Bill 1776 Phase-In Schedule

1999	$5,000 of value is excluded
2000	$10,000 of value is excluded
2001	$15,000 of value is excluded
2002	$20,000 of value is excluded
2003	ALL TAX IS ELIMINATED

The bill stipulates that the lost revenue stemming from the implementation of this legislation be returned to the affected localities. At this point the legislation does not contain any provisions concerning the size of the reimbursements or any formula for the reimbursements. It has been suggested that the state redirect a portion of the state sales tax revenues to the localities as a source of the reimbursement funds.

Governor Wilson's Plan

In addition to Assembly Bill 1776, Governor Wilson has proposed a gradual reduction, but not elimination, of this tax. The details of this plan are contained in Senate Bill 1998. In this proposal, the state-wide tax rate would be reduced from 2 percent to 1 percent in 1999 and to 0.5 percent in 2002. This tax reduction would apply to both personal and business use motor vehicles. His proposal also calls for an annual reimbursement to the localities for the loss in revenue; the details of this reimbursement plan are not available at this time. For purposes of the revenue estimate it is assumed that the reimbursements are equal to the loss in local tax revenues.

Other Proposals

There are several other proposals which have received less attention in their respective state legislatures. These include proposals in South Carolina, Missouri, and California.

Under an alternative South Carolina proposal, the motor vehicle receipts to local governments are fixed at their 1997 values. A tax cut of $25 per vehicle is provided in the first year and a cut of $75 per vehicle is provided in year two, after which the tax cut increases an additional $50 per vehicle every year thereafter. This proposal applies only to personal-use vehicles.

The Missouri legislation proposed to reduce the assessment of motor vehicles based on their age. Under this bill, motor vehicle assessments are reduced 10 percent from a maximum of

33 1/3 percent for each year the vehicle is over 5 years of age. Vehicles over 10 years of age are completely exempt from taxation.[5]

An alternative California proposal creates a new state income tax deduction for motor vehicle property taxes paid to local governments. Under this approach, vehicle owners would pay their local property taxes to the localities as usual and receive an income tax deduction (or depending on the legislation perhaps a credit) at the state level equal to the amount of taxes paid. This approach has several advantages. First, this eliminates the need for a reimbursement procedure since the local governments are not denied any revenues. Second, it reduces the risk to the local governments of losing their state reimbursements at some time in the future. It also allows lawmakers to target the tax cut based on income. On the other hand, the benefits of the tax reduction may not reach the nonfiling population, many of whom are low-income.

III. Status of Motor Vehicle Taxes in Other States

Although this issue is gaining some interest among administrators, only twelve states currently include motor vehicles in the personal property tax base. These states along with their assessment practices and range of millage rates are shown in Table 4. In these states the local governments such as counties, cities, schools, and special districts, apply a millage rate to the assessed value of the motor vehicle. The assessed value is legislated to be some percentage of the market value of the vehicle. The market value is usually based on the purchase price, the National Automobile Dealers Association "blue book" value, or the Manufacturers' Suggested Retail Price. In addition to the twelve states shown in Table 4, there are sixteen states which levy "privilege" taxes or in-lieu taxes instead of property taxes. In these states, the tax rate is uniform across the state. The state collects the revenues and redistributes the receipts to the

[5] This proposal does not apply to antique motor vehicles.

Table 4. Summary of Motor Vehicle Taxes in Other States

State	**Assessment Rate**	**Effective Millage Rates***
Alabama	Locally determined mill rates applied to 15% of market value	0.3 to 1.5 percent
Arkansas	Locally determined mill rates applied to 20% of market value	State average of 0.64 percent
Connecticut	Locally determined mill rates applied to 70% of market value	0.75 to 5.25 percent
Georgia	Locally determined mill rates applied to 40% of market value	0.36 to 2.48 percent
Kentucky	Mill rates determined as the sum of mill levies from all taxing jurisdictions are applied to 100% of the market value	State rate is 0.45%; local rate average is 0.85%
Mississippi	Local mill rates applied to 24% of market value	State average is 2.64 percent
Missouri	Local mill rates applied to 33.3% of market value	State average is 1.9 percent
North Carolina	Local mill rates applied to 100% of market value as determined by local assessor	Weighted average 1.2 percent
South Carolina	Locally determined mill rates applied to 11% of market value	2 to 3.75 percent
Virginia	Locally determined mill rates applied to 100% of market value	3.58 percent nominal statewide average
West Virginia	Locally levied property tax applied to motor vehicles	0.8 to 1.9 percent

Source: *State Tax Notes*, February 16, 1998; State and Local Value-Based Taxes on Motor Vehicles by Scott Mackey and Mandy Rafool.

*Due to the variation in assessment practices across states, the millage rates were converted into effective millage rates to allow for comparisons across states. The effective millage rate is computed as the ratio of the tax levied to the market value of the vehicle.

localities according to a redistribution formula. These states include: California, Colorado, Kansas, Maine, Massachusetts, Michigan, Minnesota, Montana, Nebraska, Nevada, Oklahoma, Utah, Washington, and Wyoming.

In the case of Georgia, counties, schools, cities, and special districts, all include motor vehicles in their tax base. These jurisdictions apply the previous year's millage rates to the current year's tax base for motor vehicles to arrive at the current year's tax levy. For example, 1996 motor vehicle tax receipts are based on the application of 1995 personal property tax millage rates to the 1996 assessed value of the stock of motor vehicles. The tax base is the aggregate value of the motor vehicle stock multiplied by 40 percent.[6] Motor vehicles in Georgia constitute a separate class of property for property tax purposes. Motor vehicles are defined as a vehicle which is designed primarily for use upon public roads. Nearly all privately owned motor vehicles, commercial and personal, are subject to the motor vehicles property tax under current law. The specific exemptions are for motor vehicle used for driver education or for transporting handicapped or disabled students to and from educational institutions. Other vehicles may be exempt because all property of, for example, certain nonprofit organizations are exempt. In addition to the property tax assessed on motor vehicles, motor vehicle owners are required to pay a license fee each time the motor vehicle is registered. Elimination of this fee is not part to the proposals discussed in this paper.

IV. Revenue and Distributional Effects of Modifying the Personal Property Tax on Motor Vehicles

The revenue effect for each of the four principal proposals discussed above was estimated as if the proposal applied to motor vehicles in Georgia. In each case, it was assumed that the proposal would be effective for calendar years beginning after 1998. The estimates discussed below are based on 1996 data for motor vehicle property tax assessments (obtained from the

Georgia Department of Revenue) and 1996 motor vehicle property tax receipts (obtained from the Georgia Department of Community Affairs).

The data were arranged to form a 1996 baseline of motor vehicle property tax receipts for all counties in Georgia. This baseline was projected out to 2003 assuming there was no change in the property tax on motor vehicles. This baseline was then compared to an estimated baseline of receipts assuming that one of the four proposals discussed above was in effect. In deriving the estimates it is assumed that the current law mandating assessment of motor vehicles at 40 percent of their market value remains in effect.

Virginia Proposal

Under the Virginia proposal, the first $20,000 of the vehicle's market value is eliminated from tax.[7] The proposal applies only to personal use vehicles. It was assumed that this proposal would become effective on January 1, 1999.

Table 5. Revenue Effect – Virginia Proposal (Calendar Years/units in millions)

1999	**2000**	**2001**	**2002**	**2003**	**Total 99-03**
-$36	-$74	-$127	-$185	-$261	-$682
*Annual amounts may not sum to the total due to the effects of rounding					

The revenue estimate shown in Table 5 represents the loss of state budget revenues. The revenue effect stems from two sources. Currently, the state levies ¼ of a mill on the assessed value of all vehicles subject to the property tax. This revenue is collected by the counties on behalf of the state; in 1996 this amount was equal to $3.6 million. Elimination of the property tax on motor vehicles would curtail this state revenue source. The second and largest source of revenue loss is due to the reimbursements remitted to the taxing localities. Due to the gradual phasing-in of the reimbursement schedule, the combined revenue loss in the first year is only $36

[6] There are a few districts which levy the property tax on some other percentage of the market value.

million and constitutes 11 percent of current law revenues from personal use vehicles. As the reimbursement percentage increases in subsequent years, the revenue loss to the state also increases. In year 2003, the state is scheduled to reimburse the taxing localities 100 percent of the value up to $20,000 for all personal use motor vehicles. The revenue loss of $261 million represents 64 percent of current law revenues from personal use vehicles.

Using 1997 data from the Department of Revenue it was determined that when fully implemented the proposal would completely eliminate the tax on over 80 percent of the vehicles now currently subject to tax. This percentage will decrease over time as more new vehicles exceed the $20,000 ceiling.[8] Assuming a millage rate of 29.5 mills (approximately the state average), a vehicle owner would receive a refund in 1999 of at most $30. The maximum tax savings an owner could receive (assuming a millage rate of 29.5 mills) in 2000 is $65, in 2001 is $112, in 2002 is $166, and in 2003 is $237. It was estimated that the statewide average refund per owner would be approximately $12 in 1999, $24 in 2000, $40 in 2001, and $79 in 2003.

Using 1995 data from the Federal Reserve Board's Survey of Consumer Finances, it was possible to estimate the distributional effects by households of the proposed legislation (Table 6). The tax reduction that a household receives is dependent on the jurisdiction's actual millage rate, which varies widely across localities. Owners who face higher millage rates will receive higher refunds, while owners facing lower millage rates will receive lower refunds. To simplify, an average millage rate of 29.5 mills was assumed.[9] The tax savings by Adjust Gross Income (AGI) occurring in 2003 is shown in column 2 of Table 6. In 2003 the tax is fully phased-in and 100 percent of the first $20,000 of a vehicle's value is exempt from tax. Although not surprising the dollar benefit of the tax cut increases with income; when expressed as percentage of AGI the

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[7] Since motor vehicles in Virginia are assessed at 100 percent of market value, the original proposal did not distinguish between assessed and market value.

[8] Because the exemption ceiling is not indexed for inflation, the rise in vehicle prices over time will cause more and more vehicles to have a value in excess of the exemption ceiling.

benefit decreases as income increases. Thus, the tax cut serves to reduce the original regressive nature of the tax on motor vehicles.

Table 6. Distributional Effects of Virginia Proposal by AGI for 2003

Adjusted Gross Income	**Tax Savings Per Household**	**Tax Savings As a Percentage Of Mean AGI**
$0 - $10,000	$52	1.86
$10,000 - $20,000	$105	0.60
$20,000 - $30,000	$132	0.47
$30,000 - $40,000	$187	0.47
$40,000 - $50,000	$216	0.42
$50,000 - $75,000	$236	0.34
$75,000 - $100,000	$280	0.28
$100,000 and above	$368	0.14

South Carolina Proposal

The South Carolina proposal gradually eliminates the property tax on all motor vehicles. The legislation establishes a Property Tax Relief fund to which the state annually contributes an amount equal to 30 percent of new general fund revenues plus the total of all previous contributions to the fund. Based on the estimation for Georgia such a fund would be fully funded in approximately 3½ years. After this time all motor vehicles would be completely exempt from tax. When the tax on all motor vehicles is completely eliminated in 2002, the estimated total revenue effect is a $547 million per year tax cut. On average, there will be a tax savings of $100 per vehicle in 2002 and each year thereafter.

[9] This is the average county millage rate in effect in 1996.

A distributional analysis for the tax cut for personal use motor vehicles, ignoring any possible distributional effects of the reimbursement plan, would be essentially the same as for the California Assembly Bill 1776, which is presented in Table 9.

Table 7. Revenue Effect – South Carolina Proposal (Calendar Years/units in millions)

1999	2000	2001	2002	2003	Total 99-03
-$189	-$363	-$525	-$547	-$547	-$2,169
*Annual amounts may not sum to the total due to the effects of rounding					

California Proposals

Assembly Bill 1776 reduces the assessed value of personal use motor vehicles by $5,000 each successive year until 2002 at which point the tax is completely eliminated. The estimated revenue effect for Georgia of this proposal is shown in line 1 of Table 8. The first year revenue loss represents 25 percent of current law revenues from personal use motor vehicles. This percentage increases to 65 percent in 2003.

Because the California plan is phased-in at a faster rate that the Virginia plan, its revenue loss and consequently its tax savings to vehicle owners are greater each year prior to 2003, at which time each plan is fully phased-in. The only difference between the Virginia proposal and Assembly Bill 1776 is that households with motor vehicles of greater than $20,000 in value will gain some additional benefit under the California proposal. This is a relatively small amount, about $3 million, but it would benefit higher income households.

The distributional effects of Assembly Bill 1776 are similar, as one would expect, to those of the Virginia plan. In 1999 the average tax savings per vehicle is $28. This increases to $43 in 2000 and $54 in 2001. The fully phased-in distributional effects by income group are shown in Table 9. As expected, the distributional analysis reveals a progressive tax cut.

Table 8. Revenue Effect – California Proposals (Calendar Years/units in millions)

	1999	2000	2001	2002	2003	Total 99-03
AB 1776	-$86	-$136	-$172	-$196	-$264	-$854
Governor Wilson	-$297	-$457	-$469	-$485	-$502	-$2,209
*Annual amounts may not sum to the total due to the effects of rounding						

The proposal introduced by Governor Wilson would lower the state imposed tax rate by 75 percent over 2 years on all motor vehicles. For Georgia this proposal would result in an estimated revenue loss of $297 million in the first year, which represents 54 percent of current law revenues if implemented in Georgia. Over the five year period this proposal would result in a loss of $2.2 billion or 74 percent of current law revenues. On average, the tax savings in 1999 per vehicle is $59. This increases to $91 in 2001.

The distributional effects of the Wilson plan are straightforward. For each income class the tax savings under the Wilson plan is less than that experienced under AB1776, but both are equally progressive in nature. The effects for 2003 of lowering the state imposed tax rate by 75 percent is shown in Table 9.

Table 9. Distributional Effects of California Proposals by AGI for 2003

	AB 1776	**AB 1776**	**Wilson Plan**	**Wilson Plan**
Adjusted Gross Income	Tax Savings by Household	Tax Savings as a Percent of Mean AGI	Tax Savings by Household	Tax Savings as a Percent Of Mean AGI
$0 - $10,000	$52	1.86	$39	1.38
$10,000 - $20,000	$105	0.60	$79	0.45
$20,000 - $30,000	$132	0.47	$99	0.35
$30,000 - $40,000	$187	0.47	$141	0.35
$40,000 - $50,000	$218	0.43	$164	0.32
$50,000 - $75,000	$238	0.34	$178	0.26
$75,000 - $100,000	$280	0.28	$210	0.21
$100,000 and above	$370	0.15	$277	0.11

V. Administrative Issues

The administrative issues associated with these proposals will vary depending on the proposal adopted. Many of the issues discussed below are based on the experience of implementing the Virginia proposal.

One issue which all proposals must face has to do with the determination of eligibility when the tax break is limited to personal use vehicles. Several of the proposals rely on the definition used for the federal tax deduction concerning business-use vehicles. Simply put, if a vehicle owner takes a Federal tax deduction for business use of the vehicle, then the vehicle is not eligible for the state tax break on property taxes. This would require the Department of Revenue's Motor Vehicle office to verify this status. This could be done by requiring a copy of the Federal tax return or by random audits. Both options have drawbacks but without a means to verify eligibility many inappropriate vehicles may receive the tax break.

The issue of eligibility becomes particularly problematic in the case of leased vehicles. The property tax bill for many of these vehicles is paid by the leasing company, which may be located in another state.   Thus, these property tax proposals require that leasing companies notify the Department of Revenue as to which vehicles are used for personal use. This information is not currently collected and would place an additional burden on the leasing company.

The Virginia experience has brought to light two other issues. The first is that not all the taxing jurisdictions have the same fiscal year for their budget process. This is the case in Georgia as well. This creates some difficulty in terms of reporting and reimbursements. The second is that these proposals require input from both the county treasurer and from the county commissioner, each of whom are elected officials in Virginia, sometimes of different political parties. It has been the experience in Virginia that there are often no existing lines of communication between these officials. Thus, this legislation forces communication and cooperation between new groups within the government.

In addition to these issues, the sheer number of taxing jurisdictions (well over 1,000) will cause a paperwork and tracking ordeal. The Virginia legislation includes some funds to bring electronic information transfer to the local taxing jurisdiction. This will aid the state in determining the appropriate level of reimbursement and also in their audit procedures. Furthermore, there currently exist several districts in Georgia which appraise property at values other than 40 percent. For example, personal property in Summerville in Chattooga County is assessed at 100 percent and some property in Decatur in DeKalb County is assessed at 50 percent. Since the reimbursements are based on the millage rate, these millage rates must be adjusted to reflect an assessment practice of 40 percent. Lastly, there is no unique district identifier used by all state and local departments. In many cases counties use one set of district codes while the state uses another. This creates a confusing system of data collection and information exchange.

All of these issues are solvable, but the state and local governments will most likely require additional resources in the form of additional staff and computers to audit, track, collect, and transfer the needed information to the state level.

VI. Conclusion and Policy Recommendations

The analysis above outlines several proposals to eliminate or reduce the property tax on motor vehicles and the revenue consequences associated with each. The Virginia and South Carolina proposals offer well constructed models for other states to follow. The conditions for exemption contained in the proposals are straightforward and easy to understand. While in each case there exist some problems with implementation, these can be overcome with advanced preparation and additional resources and information.

The stated objective of this tax cut has always been a bit vague. The major criticism of this tax, as opposed to other taxes, is that it is due as a lump sum payment. This can create a true financial burden for some households. This burden will be much greater, though, in states that base the tax on the full market value of the vehicle, such as California and Virginia.

Owning to its design, this tax cut has some interesting effects. By requiring the state to reimburse the localities for the revenue loss associated with this exemption, the tax is simply shifted from the local level to the state level. In doing this, the tax becomes hidden from the taxpayers. The "exempted" motor vehicle value is not truly exempted but merely paid by the state and, thus, indirectly by state taxpayers. But since state tax payments are due on a periodic basis or through payroll deduction, the obligation (i.e. the tax on motor vehicles shifted to the state taxpayers) becomes less onerous but also less obvious.

The results of such a tax modification will vary over time and across districts. A reduction in the tax on motor vehicles will likely not result in an increase in motor vehicle consumption, an affect lawmakers would be careful to avoid in light of the air quality issues and traffic problems currently facing metropolitan Atlanta and potentially facing other areas of the state. The most probable short run result would be an increase in general consumption since most individuals are not likely to take the tax into account when purchasing a motor vehicle.

Reducing or eliminating the tax will, in the short run, reduce the local property tax bill of state residents in a visible and straightforward manner by eliminating their annual property tax bill for motor vehicles. On the other hand, the long run consequences of a reduction or elimination may be quite different.

This type of proposal will in all likelihood have little effect on the overall level of local taxes paid by the general population in the long run. Since these proposals are not linked to any mandate or even request to reduce local government spending, local government budgets are not likely to shrink. In fact, reductions in Federal transfers to states and localities are putting increased pressure on local government budgets. Curtailing the localities's ability to tax motor vehicles will force these entities to seek new sources of revenue or to increase the use of existing ones if the local governments need additional revenue because of, for example, increased costs or if motor vehicle reimbursements fall short. Under the Virginia plan, the localities could simply increase the millage rate applied to the remaining taxable property, including housing. The South Carolina proposal eliminates this alternative by completely eliminating the personal property tax base and freezing the levy on other property.[10] In this case one might expect to see an increased reliance on sales taxes, excise fees, and user charges at the county and local level. Shifting from a property tax to a sales tax and fees has the disadvantage of reducing Federal income tax deductions for individuals who itemize their taxes.[11]

The long run consequences also depend on the growth of state revenues. While these proposals decrease taxes at the local level, they increase spending at the state level due to their reimbursement requirements. In times of budget surpluses or high growth this new obligation may not seem burdensome. (By way of comparison, the recent cut in state personal income taxes was $205 million.) Problems in fulfilling the obligation may arise, though, in times of decreased state tax revenues. During the initial phase-in period these proposals contain special provisions to account for a decline in state revenues. These provisions are designed to limit the claims of the state reimbursements on the state budget. With these provisions in place the state will only

[10] The proposal affects all personal property in the category of "all other personal property" but does not include housing.

allow an exemption level which can be afforded by the current level of revenues. Once the proposal is fully phased-in it becomes less clear what happens to the state reimbursements in the event of a decline in state revenues. In the Virginia and South Carolina proposals discussed in this paper some provisions are included to deal with this contingency, but these cannot completely guarantee full reimbursement in the event of a decline in state revenues after the exemption has been fully phased-in. In fact, legislators might end up in the position of increasing state taxes in an effort to meet their property tax reimbursement obligations. This would result in a shifting of the tax burden from vehicle owners to an unknown group of state taxpayers.

In addition to limiting the tax base of all localities, the modification to the property tax base will affect some localities more than others. If state reimbursements are tied to historical revenue collections, such as the South Carolina proposal, there is no accommodation made for future growth. Thus, small and currently less developed counties will be at a disadvantage relative to counties which are closer to their population capacity. Under the Virginia proposal state reimbursements are based on the locality's millage rate in the initial year. While millage rates do rise and fall from year to year, over time these rates tend to follow an upward trend. Therefore, over the long run localities will likely face a decreasing reimbursement in real terms.

Lastly, incursion of the state into the taxing domain of the localities is likely to meet with opposition from local public officials. Although localities are granted the privilege of taxation from the state, many local officials will see this effort to reduce the public's tax burden as an effort to erode the localities's power. This will increase tension on intergovernmental relations at a time when the state and localities need to come together to face common issues. This would

[11] Property taxes, including property taxes on motor vehicles, are tax deductible on the state and federal level for filers who itemize their tax deductions. This serves to reduce the tax burden of these taxes on individuals who itemize their returns.

be a costly waste if in the long run the modifications to the motor vehicle tax do not reduce the tax burden of the individual.

In conclusion, the merits of this tax are best judged when the proposal is considered in its true light. The real advantage of these motor vehicle proposals come from making the motor vehicle tax payable over time and redistributed over all state taxpayers. A true tax cut may occur only if neither state nor local governments increase their taxes due to this "exemption". The disadvantage of these proposals comes in the form of increased risk to the local governments. While the proposals contain language to provide for ongoing reimbursements, nothing can guarantee that at some point in the future these payments will not be curtailed for the sake of other government programs or a state tax cut. In addition, because these reimbursements are tied to historical collections or previous millage rates, they erode the tax base under the control of the local governments. Although the localities can use other forms of taxation, such as fees or sales taxes, these require the approval of the local voters. In this day and age winning voter approval for additional taxes is no small hurdle.

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