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ANALYSIS AND RECOMMENDATIONS FOR THE PROPERTY TAX ON MOTOR VEHICLES IN GEORGIA

Nothing excites Americans like taxes and automobiles. Thus, it is hard to imagine a more potent tax proposal than one that lowers the tax on automobiles. Over the past several months, there has been renewed interest by citizens and legislators in Georgia in the idea of reducing the property tax levied on motor vehicles. In 1998, legislatures in four states (Virginia, South Carolina, California, and Missouri) proposed bills that 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.

Georgia Proposal to Eliminate the Motor Vehicle Property Tax

Recently, a proposal, HB 585, has been advanced by members of the Georgia General Assembly that eliminates the property tax on motor vehicles. The proposal phases out the property tax paid by all noncommercial motor vehicle owners over a three-year period. The motor vehicle exemption applies to all school, county, state, and municipal property taxes. The proposal provides that the state reimburse the local governments for lost revenue by transferring funds on a monthly basis to the respective local governments. Reimbursements are to be equal to the full amount

taxpayers would have paid in the absence of this legislation.

The legislation includes a provision to cover circumstances in which insufficient funds may exist in the state budget to cover the cost of the reimbursements to the local governments. Under this situation the legislation allows for funds to be diverted from other programs to cover the cost of reimbursements. Alternatively, the legislation allows for a reduction in the amount of the exemption level.

Issues Associated with the Motor Vehicle Property Tax

- Part of what is disliked about the motor vehicle property tax is that property taxes are taxes on a stock of wealth instead of a stream of income. Therefore, an asset may have a positive value, such as a house or car, but creates no income from which to pay the annual property tax.
- Another source of ire with the motor vehicle property tax is that it is due in its entirety on the vehicle owner's birthday. This can cause a cash flow problem for taxpayers who have more than one vehicle registered under their name. This administrative issue could be addressed by collecting the tax on the anniversary of the vehicle purchase.

TABLE A. REVENUE EFFECT OF MOTOR VEHICLE PROPERTY TAX EXEMPTION FOR 2004 (\$ IN MILLIONS)

Exemption Level	Revenue		Total Revenue Loss	Reimbursement as a
	Loss to State	Revenue Loss to Local Gov't		percent of Total Net State Revenue Collections
\$10,000	\$2.1	\$240	\$243	1.8%
\$15,000	\$2.4	\$270	\$273	2.0%
\$20,000	\$2.5	\$288	\$290	2.1%
100 percent of vehicle value	\$2.7	\$308	\$311	2.3%

TABLE B. DISTRIBUTIONAL EFFECT OF MODIFYING THE MOTOR VEHICLE PROPERTY TAX

Income Category	-----Amount of Motor Vehicle Value Exempted-----					
	-----\$10,000-----		-----\$20,000-----		----Complete Exemption----	
	Average Tax Savings	As a % of Total Income	Average Tax Savings	As a % of Total Income	Average Tax Savings	As a % of Total Income
Less than \$25,000	\$78	0.7%	\$90	0.8%	\$92	0.9%
\$25,000<=Income<\$50,000	\$115	0.3%	\$143	0.4%	\$149	0.4%
\$50,000<=Income<\$75,000	\$162	0.3%	\$214	0.4%	\$229	0.4%
\$75,000<=Income<\$100,000	\$186	0.2%	\$258	0.3%	\$278	0.3%
\$100,000<=Income<\$150,000	\$202	0.2%	\$296	0.2%	\$336	0.3%
\$150,000<=Income	\$228	0.1%	\$359	0.1%	\$486*	0.2%*

Source: Calculations are based on 2005 Consumer Expenditure Survey. * Because the values for income and vehicle value are top-coded in the dataset, this result understates the average tax savings and tax savings as a percent of total income for individuals in this income category.

- Exempting all motor vehicles from the property tax base creates some additional avenues for avoiding the tax. Recreational vehicles that also serve as primary and secondary homes would no longer be subject to tax but permanent structures serving in this same purpose would. Modifying the law to only exempt vehicles under a certain weight or those without sleeping facilities would easily address this issue.

Revenue Effect of Reducing the Motor Vehicle Property Tax

An estimate of the revenue loss associated with various exemption levels is shown in Table A. The revenue estimate assumes the exemption only applies to personal-use vehicles. Furthermore, the estimate provided below is tentative in that it is based on a state-wide average property tax of 28.47 mills that existed in 2004.¹ It is assumed that the state would fully reimburse the local governments for lost revenue.

The revenue effect consists of two pieces. The first is the direct loss in revenues to the state from a reduction in the state property tax base. The second revenue loss is the loss to the local governments. This is the value of the state reimbursement to the localities. The last column represents the size of the state reimbursements to localities relative to the size of net

state revenue collections. It is estimated that eliminating the tax on vehicle values of \$20,000 or less would completely exempt about 96 percent of the vehicle stock from the property tax. A \$10,000 cap would exempt about 88 percent of the vehicle stock.

Table B shows the distributional effect of eliminating the property tax on motor vehicles under three alternatives. The data in Table B reflects the total tax savings per family over all personal vehicles. The lowest income groups experience the greatest gain when expressed as a percent of income. On the other hand, the average tax savings increases with income, reflecting both the consumption of higher-end vehicles and of a larger number of vehicles as income increases.

Recommendations

- From an economic standpoint, the preferred choice is to eliminate the many exemptions to the property tax base and by doing so, expand the base and allow property tax rates to be reduced for all types of property and all owners. Limiting the exemption to personal-use motor vehicles only lowers the value of the remaining base and forces the state to seek other sources of revenue.

- If the decision is made to go forward with property tax relief, then this proposal should be considered in tandem with the existing Homeowner Tax Relief Credit (HTRC) program. That is, this proposal should be viewed as an extension of the original HTRC. Designed in the same manner, both programs provide relief from state, local, and school property taxes. As such, these programs will be competing for the same state resources to fund their reimbursement obligations to the local governments. Increasing the exemption of one program will reduce the likelihood of an increase in the exemption of the other.
- With that tradeoff in mind, lawmakers should focus on their desired goal of property tax relief. Offering property tax relief through an exemption in the motor vehicle tax base affects a larger population and is more progressive than tax relief provided through the HTRC.

This is because the ownership of motor vehicles is more wide-spread and less concentrated among higher-income individuals relative to property ownership. On the other hand, taxpayer relief may not be as important in the case of a depreciating asset, such as motor vehicles. If this is the case, then state resources should be targeted to increasing the exemption granted under the HTRC program.
- Based on a review of the experiences of other states, it seems clear that the state's annual obligation to the local governments should be predictable and limited. To this end, provisions in the legislation that cap the exemption amount, freeze the local government millage rates that are used to determine the amount of state reimbursement, or permanently set the reimbursement amount will create more manageable, less volatile and burdensome obligations for the state.
- To increase the progressive nature of this tax provision and limit the revenue effect to the state, exemptions could be granted only up to some specified amount. Approximately 96 percent of all vehicles registered in Georgia would be completely exempt from the motor vehicle property tax with a \$20,000 exemption cap. Allowing an exemption up to some level of value benefits all vehicle owners, but concentrates the benefits on relatively lower-income individuals. While the revenue loss may not be particularly large, allowing a complete exemption of all personal-use vehicles creates some very large gains for a select number of luxury vehicle consumers.
- In addition, a proposal that only eliminates the tax on personal-use vehicles creates a need to clearly define what is meant by personal-use, especially in the case of mixed-use vehicles, and have in place a procedure for preventing tax avoidance. This is probably best done by a sharing of information between the federal government and the state government. This will prevent taxpayers from claiming a vehicle as business property on the federal return and as personal-use vehicle at the state and local level. Furthermore, if the reimbursement process involves sending checks directly to the individuals, the state government would need to annually send a 1099 statement to the federal government for each check received by all vehicle owners in the state.
- Legislation in this area needs to clearly specify the conditions under which the state reimbursements cease or are curtailed. Several states have legislation stipulating that reimbursements are to cease or be restricted when there are insufficient funds to cover the state obligation. In order for this type of language to be effective, a list of state priorities including the reimbursements to localities for this lost revenue must also be available. Without an understanding of the relative position of this state obligation compared to others, it will be difficult to determine when the state has adequate revenues for this program or if other state funding obligations should be cut instead.
- Including explicit procedures in the legislation to cover situations in which state motor vehicle property tax reimbursements are in jeopardy is critical. Tying actions to a slower than anticipated growth in tax receipts or larger than anticipated revenue effect to the state budget provides some guidance. But even in this case, it is not clear whether the exemption level should be reduced, or if so, by how much. One alternative would be to limit this obligation to a fixed amount or fixed percentage of the state own-source revenues. It should also be made clear whether or not this limit applies solely to the reimbursements for the motor vehicle property tax revenues or is also meant to include state reimbursements associated with the Homeowner's Tax Relief Credit.
- While not included in the current version of the proposal, a previous version incorporated an alternative reimbursement system that was designed to eliminate any risk of reduced funding on the part of the local governments, a procedure similar to Virginia's original program. This was done by requiring the taxpayer to continue to pay in full their usual motor vehicle property tax liability. Therefore, the local taxing authorities would see no change in their level of incoming revenues or in the timing of these revenues. A significant problem with the Virginia motor vehicle tax reduction plan was that the local governments were completely dependent on the state for the eliminated revenues. If the state did not have the resources to fulfill this obligation or if the state's timing of payment to the local governments' was different or late, then the local governments' had no recourse. The revised Georgia proposal has the potential to create similar situations for the Georgia local governments.
- Although the direct taxpayer reimbursement design has many advantages, it also has several disadvantages.
 - Under the direct reimbursement design, taxpayers still paid the tax liability in a lump sum. This can create liquidity problems, especially for those individuals with more than one vehicle. To address this issue, the tax can be levied instead on the anniversary of the vehicle purchase.
 - Additionally, the taxpayer reimbursement design is administratively costly, as it is expensive to issue 6 million reimbursement checks annually.² Some costs may be avoided if the reimbursement is combined with the state income tax. If the reimbursement process is combined with the state income tax then the reimbursement must be

treated as a 100 percent refundable credit so that all individuals have an incentive to file a return even when no income tax liability is incurred.

- Furthermore, if the reimbursement check is issued directly to the taxpayer after the taxes are paid, the taxpayer may not link the check to the property tax liability but see it instead as simply an annual windfall. In addition, there will be much less pressure on the state to provide the same level of reimbursements each year since the local governments would have already received their payments.
- Finally, with regards to a capped exemption level, to maintain the same level of property tax relief from year to year, the exemption level should be indexed each year to reflect the annual increase in automobile prices. Without an indexed threshold the percent of a vehicle's value covered by the exemption will decline each year.

Notes

1. A formal revenue estimate of this proposal would incorporate the actual millage rates of the taxing districts.
2. This is the number of registered vehicles from the DOR 2005 property tax digest.

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