

**JUST WHEN YOU THOUGHT IT  
WAS SAFE . . .**

**Implementing Personal Property Tax  
Relief (Again)**

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**May 3, 2005**

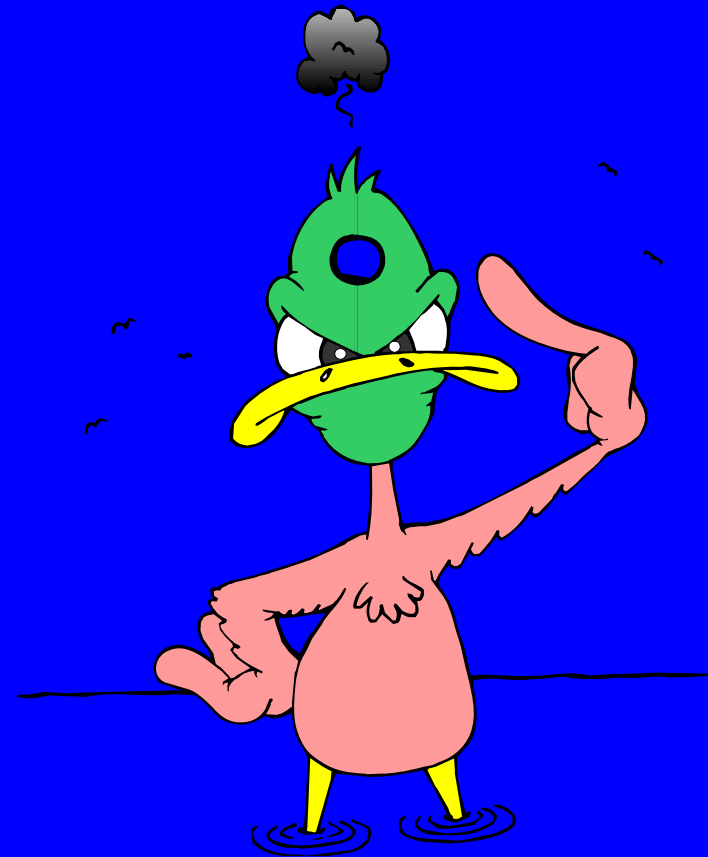
# THE ORIGINAL PROMISE



- Car tax will cost \$600 million when fully phased in
- Revenue growth will more than pay for the tax relief
- “Triggers” will protect the fiscal integrity of the Commonwealth by freezing relief if revenue growth slows or stops

# REALITY

- Program grows rapidly and continuously, defying accurate modeling
- Total cost \$1.6 billion or more if 100% ever reached
- Perspective: larger than *all* higher ed GF spending combined



# PROGRAM DRIVERS

- Population growth
- Per capita car ownership growth
- Inflation in prevailing new car prices substantially exceeding general inflation
- Unprecedented manufacturer incentives = subsidized cost of capital, shorter hold times = even more rapid growth in fleet value
- “Wealth effect” of program itself

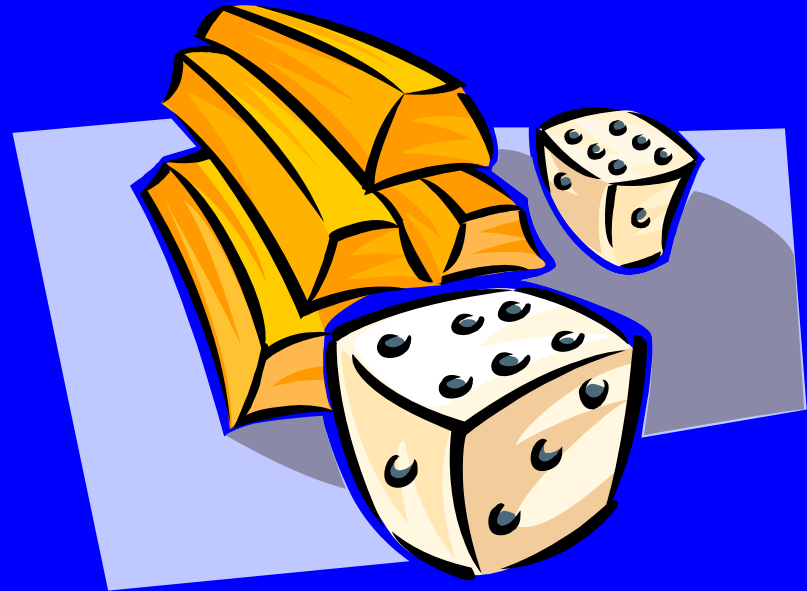
# 1998 IMPLEMENTATION: REMARKABLY SMOOTH



- Standardization of valuation methods
- Electronic interface with payments by EFT on daily basis
- Substantial improvement of DMV vehicle file and local vehicle files
- Reimbursement mimics real-time cash flow

# SUBSEQUENT HISTORY: BITTER WRANGLING

- Administrative costs buried and passed to localities
- Revenues manipulated to “pull” trigger, leading to budget impasse of 2001
- Near chaos, given legislative debate over changing reimbursement rate in midyear



# 2004: REALITY SETS IN

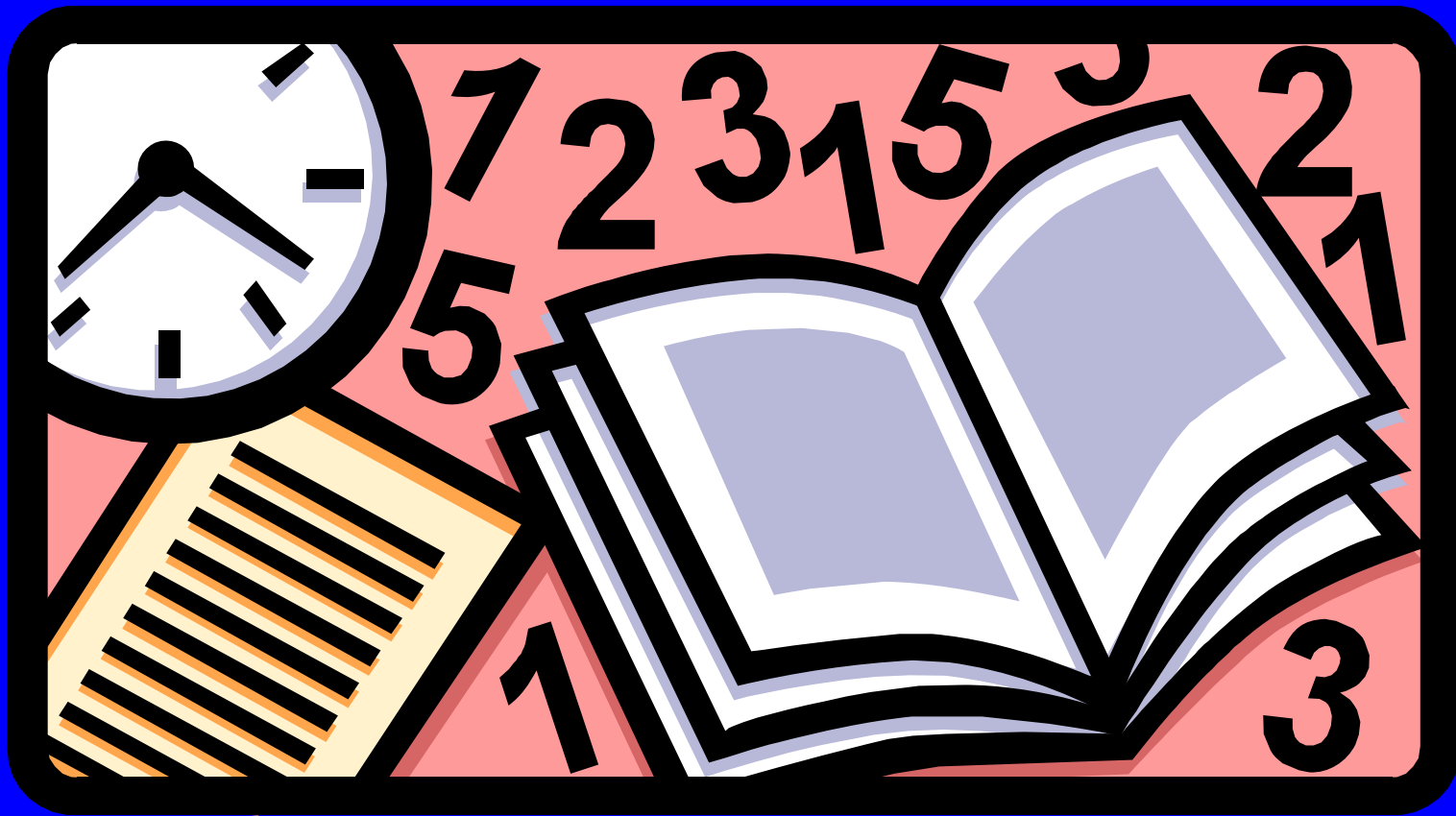
- Historic, crippling impasse over revenue enhancements
- “Psychological barrier” among many in House majority: revenue increase of no more than \$1 billion, BUT . . .
- Expenditure needs and bonding rating crisis require more than a billion . . . much more

# LEGISLATIVE SOLUTION!

- SB 5005 amended to “skin the cat” another way by . . .
- *Spending less over time on car tax!*
- Equates to an additional half penny to penny on the sales tax within a few years – or virtually overnight if compared to taking reimbursement to 100%



# THE ORIGINAL 2004 LEGISLATION



# HOW IT WORKS: GENERAL PRINCIPLES

- For TY2005, car tax relief remains at 70%.
- State spending for car tax relief is capped at \$950 million annually beginning in state FY2007.
- \$950 million equates to the estimated car tax expenditure for calendar year 2006 at 70% – thus no one “loses” anything at first.
- Result: combined with compromise revenue increases, gap between revenues and expenditures is substantially narrowed in “out years”

# HOW IT WORKS: THE GORY DETAILS

- From FY07 on, locality's payment will be a fixed sum that represents the locality's *pro rata* share of the total state reimbursement for TY05
- Total state "pie" will remain \$950 million
- Neat trick: payments move to *fiscal year* basis, not calendar year. Result . . . .  
Permanent movement of some \$250 million into a subsequent state fiscal year

# MULTI-TIERED TAX RATE REQUIRED

- Locality begins by setting its *general PPT rate* which applies to
  - nonqualifying vehicles, and
  - the portion of the value of each qualifying vehicle in excess of \$20,000.
- Locality then sets one *or more reduced rates*, applied to the first \$20,000 value of all qualified vehicles, the cumulative effect of which will be to “use up” the state tax relief payment.

# STEP ONE: DETERMINE YOUR STATE RELIEF PAYMENT

- Divide TY05 reimbursement received by locality by the total TY05 statewide reimbursement.
- Multiply the resulting percentage times \$950 million to yield a fixed-dollar amount of reimbursement that the locality will receive in FY (not CY!) 2007 and beyond.

## STEP TWO: SET A GENERAL PPT RATE

- Locality sets general PPT rate at own discretion
- Effective limitations on and disincentives to raising rates, contained in the original 1998 PPTRA legislation, are eliminated

# STEP THREE: SET ONE+ REDUCED RATES TO "USE" STATE RELIEF

- Value of qualifying fleet (first \$20,000 of value) multiplied by the general PPT rate = hypothetical amount of PPT revenue locality would have generated *but for* tax relief.
- From that figure, subtract the (fixed) amount of state reimbursement the locality receives.
- The balance is the "taxpayers' portion" – that is, the tax that must be recovered from owners of qualifying vehicles

# RECOVERING THE TAXPAYER PORTION

- Locality can structure rates any way it wishes to use up the state relief, so long as used for vehicles \$20,000 and under
- Simplest way is to take state relief, divide by total value of fleet of qualifying vehicles, and express result as a rate
- Localities may wish to set tiered rates for values between \$0 and \$20,000 – for instance, to continue exemption for vehicles valued at \$1000 and under, which have been exempt from *all* taxation since 1999

# GIVING CREDIT WHERE CREDIT IS DUE

- As passed, SB 5005 required localities to change tax bills to show how much the tax *rate* was lowered on the first \$20,000 of value in that locality, due to the state's tax relief payment.
- Substantial reprogramming costs for many localities

# EXAMPLE: CALCULATING THE STATE RELIEF

2005 Locality Reimbursement      \$3,809,992

divided by

2005 Statewide  
reimbursement      \$859,822,033

equals

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Locality's percentage      0.44%

# DETERMINE TOTAL STATE RELIEF FOR LOCALITY

Statewide reimbursement \$950,000,000

multiplied by

Locality's percentage

0.44%

\_\_\_\_\_ equals \_\_\_\_\_

Locality's *fixed* annual

\$4,180,000

reimbursement

# SET GENERAL TAX RATE AND COMPUTE HYPOTHETICAL REVENUE

Value of qualifying fleet under \$20,001		\$123,000,000
	multiplied by	
General Tax Rate		\$4.40
<hr/>		
Qualifying fleet's hypothetical revenue	equals	\$5,412,000

# DETERMINE TAXPAYER PORTION

Qualifying fleet's revenue	\$5,412,000
minus	
State reimbursement	\$4,180,000
_____ equals _____	
Taxpayers' portion	\$1,232,000

# SINGLE REDUCED RATE (TY2006)

Taxpayers' portion \$1,232,000

divided by

Value of Qualifying Fleet

under \$20,001 \$123,000,000

equals

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Reduced Tax Rate \$1.00

# SINGLE REDUCED RATE (Second Year - TY2007)

Value of qualifying fleet

under \$20,001                      \$141,450,000

multiplied by

General PPT rate                      \$4.40

   equals

Qualifying fleet's revenue

\$6,223,800

# SINGLE REDUCED RATE (TY2007), *continued*

Qualifying fleet's revenue	\$6,223,800
minus	
State reimbursement	\$4,180,000
equals	
<hr/> 2007 Taxpayers' portion	\$2,043,800

# SINGLE REDUCED RATE (TY2007), *continued*

Taxpayers' portion \$2,043,800

divided by

Value of Qualifying Fleet  
under \$20,001

\$141,450,000

equals

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Reduced Tax Rate

\$1.44

# WHAT HAPPENED?!

- Value of fleet increased by **15%** from CY05 to CY06, BUT . . .
- . . . the reduced PPT rate for qualifying vehicles jumped by **44%**!
- AND every taxpayer with a vehicle valued at \$1000 or less started paying taxes again – for the first time since 1997!

# MULTITIERED RATE

- Vehicles valued \$1000 and under have been completely exempt from PPT since *1999*
- As much as a quarter of all vehicles essentially removed from the collection program
- Only way to keep these vehicles out will be to adopt a multitiered rate structure that sets a zero or negligible rate for lowest-value vehicles

# MULTITIERED RATE: AN EXAMPLE

- Locality has 10,000 vehicles valued at \$1000 and under
- Three-tiered rate structure adopted:
  - 50 cents for first \$1000 of value
  - \$1.16 for \$1001 to \$20,000
  - \$3.70 for value in excess of \$20,000
- Vehicles valued at/under \$1000 would have bill of \$20 or less, which can be written off pursuant to general law

# ADVANTAGES OF MULTITIERED RATE

- Collection costs for small balances typically exceed amount collected
- Former imperative to collect – state’s “holding hostage” of state reimbursement – no longer applies
- To the extent vehicle valuation correlates with ability to pay, provides greater relief at lowest levels
- Public reaction to bringing tens of thousands of vehicles back into payment status

# REALITIES OF THE NEW PROGRAM

- The faster you add population, the faster you must raise your reduced rate
- The more affluent your locality becomes, the faster you must raise your reduced rate
- Virtually every locality's reduced rate must rise over time.
- Thousands of vehicle owners who were taken off the PPT rolls will return unless you adopt a multitiered rate structure

# CASH FLOW & ACCOUNTING PROBLEMS

- Transition to fiscal year basis will cause substantial cash flow disruption for localities with a spring billing cycle – no payments until July 2006 under SB 5005 and Appropriation Act as passed
- Possible accounting issues – state relief revenue for May and June billings will not be received until next fiscal year

# RISING "REDUCED" RATES: ACTUAL PROJECTIONS FROM A RAPID GROWTH LOCALITY

- TY05: Reduced rate = \$1.11 (ie, 70% of current rate of \$3.70 per \$100)
- TY06: Reduced rate = \$1.35
- TY07: Reduced rate = \$1.59
- TY08: Reduced rate = \$1.80
- TY09: Reduced rate = \$1.98
- Bottom line: **78%** increase in reduced rate over 4 fiscal years

# EFFECTIVE REIMBURSEMENT RATE: SAME LOCALITY

- FY05: 70%
- FY06: 64%
- FY07: 57%
- FY08: 51%
- FY09: 46%
- Decline in reimbursement rate over first four years is c. 6% per year

# SIMILAR PROJECTION FOR MODEST GROWTH LOCALITY

- Assume tax base growth of 1.6% to 2.8% per year (contrast 10% in rapid growth locality)
- Vehicle count growth: 2.4% per year (as opposed to 5% to 10% in rapid growth jurisdictions)
- Growth of local reduced rate will be significantly slower than rapid growth locality – but still will be in the range of 5 to 10 cents a year, just to maintain tax effort at constant level.

# VALUE OF THE FLEET SHOWS WIDE LOCAL VARIATIONS

	Vehicle value	
	<u>&lt;\$1000</u>	<u>&gt;\$20,000</u>
– Chesterfield	13%	6.1%
– Frederick	28%	4.7%
– Newport News	19%	3.4%
– Suffolk	24%	5.5%

# THE MORNING AFTER: CRITICAL CONCERNS



# CRITICAL ISSUES COMING INTO 2005

- Cash flow for spring billers
- Financial reporting and budgeting issues regarding revenue recognition
- Transition issues (delinquents collected, supplementals, exonerations)
- Programming costs
- Phase-out of DMV reconciliations, PPTRA Compliance Audit Program
- Bill formats

# *CRITICAL ISSUE #1*

## CASH CRUNCH FOR SPRING BILLERS

- About 37 counties, cities & towns
- Delay of as much as several months in receiving PPTRA funds from state
- ***NOT*** a one-time issue; recurs annually
- \$229 million to fix; no money in budget
- Secretary of Finance has authority to reimburse interest

# *CRITICAL ISSUE #2*

## TRANSITION PROBLEMS

- Availability of TY2005 reimbursement dollars for delinquent TY 2005 payments
- What to do when the money is gone?

# *CRITICAL ISSUE #3*

## ALLOCATION OF "PIE"

- SB 5005 required APA to certify TY2005 reimbursements by March 1, 2006
- Effective cutoff early February
- Some bills wouldn't even be issued by the time of the cutoff – harshest impact on December 5 billers (majority of jurisdictions)
- Possibility of "gaming" the system

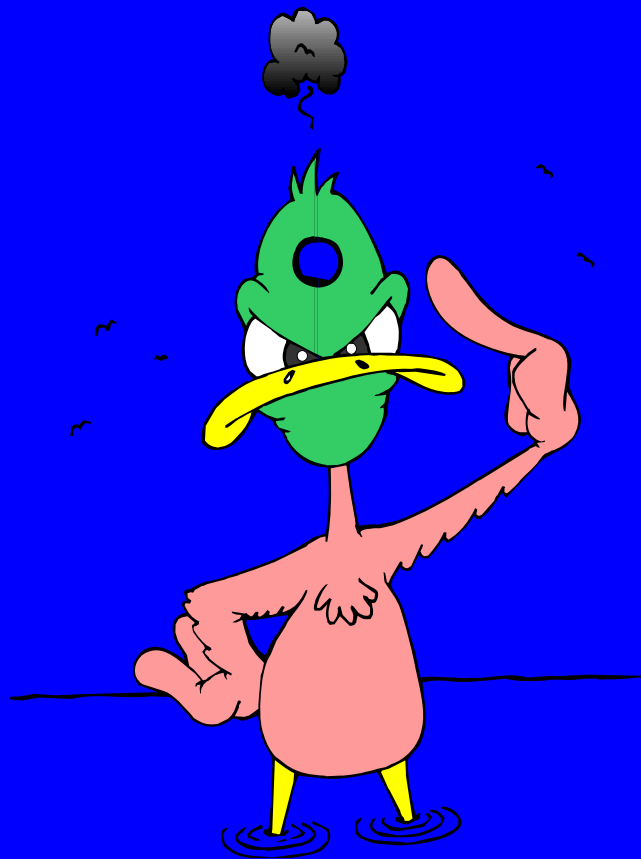
# *CRITICAL ISSUE #4*

## PROGRAMMING COSTS

- SB 5005 required tax bill to show difference in rate made possible by state PPT relief
- Substantial reprogramming required
- State appropriated \$5 million in 1998 to help with programming and related costs
- No \$ for this purpose in 2004 budget

# *SB 5005 AS PASSED*

## BOTTOM LINE



- Serious cash flow problems for some
- Accounting issues for all
- Programming \$ for all
- Rate increase *every* year
- Rampant citizen confusion

*2005 SESSION CHANGES*  
THE "NEW" PPTRA IS  
REWRITTEN YET AGAIN



# PPTRA WORKING GROUP

- SB 5005 required Secretary of Finance to work with local governments to *“develop a schedule of payment dates”*
- Portfolio is expanded at local governments’ insistence to consider budget language and/or legislative changes to address problems
- Meetings during fall 2004

# PRODUCTS OF EFFORTS

- Budget language amendments that essentially rewrite SB 5005's most troublesome aspects (*Item 503, 2005 Appropriations Act*)
- Reimbursement schedule that addresses cash crunch for spring billers and problems of towns (*Secretary of Finance, January 1, 2005*)

# KEY FEATURES OF BUDGET AMENDMENTS

- Base year for computing “slice of pie” changed to 2004
- Alternative to “reduced rate” method provided – “specific relief”
- Transition provisions + supplemental \$
- Balance billing authorized
- Special provisions for towns
- “Intent” language for spring billers

# BASE YEAR CHANGE

- Base will be tax year *2004* collections, measured through December 31, *2005*
- Change ensures that localities are finished the billing cycle *and* have at least 12 (and as many as 20) months to collect
- “Slice of pie” fixed by APA on March 1, 2005

# ALTERNATE METHOD AUTHORIZED

- Locality may elect to show specific relief, by vehicle, on bill *instead of* adopting “reduced rate”
- Programming changes will be minimal – existing programs designed to use percentage relief
- No need to adopt (annually increasing) “reduced rate” each year
- Public understanding likely to be enhanced because relief will be shown in same manner as present bills

# TRANSITION PROVISIONS

- Intent to pay TY2005 reimbursements on and after January 1, 2006 made clear
- Definitive end date provided: earlier of September 1, 2006 *or* when state \$ runs out
- \$24 million additional funding provided to cover delinquents (*but will it be enough?*)
- Treasurer may “balance bill” entire amount of bill if reimbursement unavailable
- Special provisions for City of Winchester

# PAYMENT SCHEDULE: OVERVIEW

- Eliminates potential balance sheet deficit, and softens cash crunch, for spring billers by making payments within availability period
- APA confirms that payment within availability period should be booked for fiscal year just ended
- Provides 4 distinct reimbursement schedules
- On average, localities will do slightly better than historical experience
- Lump sum payment to towns

# SPRING BILLERS

- Will receive, on July 31, the same % as collected in 2005 through June 30
- Second payment on August 15 (40% of balance) (*also within availability period*)
- Third payment (60% of balance) on November 15
- Acceleration of balance payments intended to help offset investment earnings lost on delayed first payment

# OTHER LOCALITIES

- Divided into categories to simplify administration
  - ✓ Localities receiving  $>$  \$20 million/year
  - ✓ Localities receiving  $<$  \$20 million
  - ✓ Towns (other than spring billing towns)
  - ✓ Spring billing towns

# LOCALITIES > \$20 MILLION

- Four cities and counties in this category;  
October 15 due date
- August 15: 50%
- November 15: 45%
- February 15: 3%
- May 15: 2%

# LOCALITIES < \$20 MILLION

- 93 cities and counties in this category; December 5 due date is typical
- August 15: 5%
- November 15: 75%
- February 15: 15%
- May 15: 5%

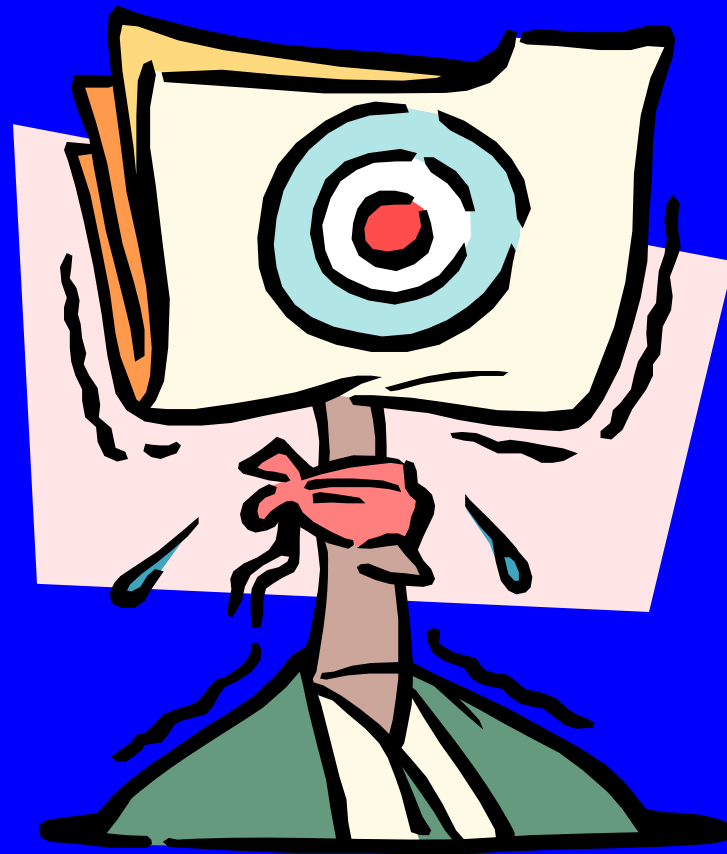
# TOWNS

- All but 7 towns (which are “true spring billers”) will be paid out in a lump sum on August 15
- Total of all town reimbursements statewide is only \$8 million
- Note that most towns that have a due date between January 1 and June 30 are not spring billers; they are billing in arrears for calendar year just completed

# TOWNS THAT ARE “TRUE SPRING BILLERS”

- 7 towns that have a due date between January 1 and June 30 for the *current* year
- All use cash basis of accounting and thus payment during availability period won't help
- Secretary of Finance granted authority to pay them out in spring

# POLICY CHOICES FOR LOCALITIES



# METHOD OF REFLECTING RELIEF

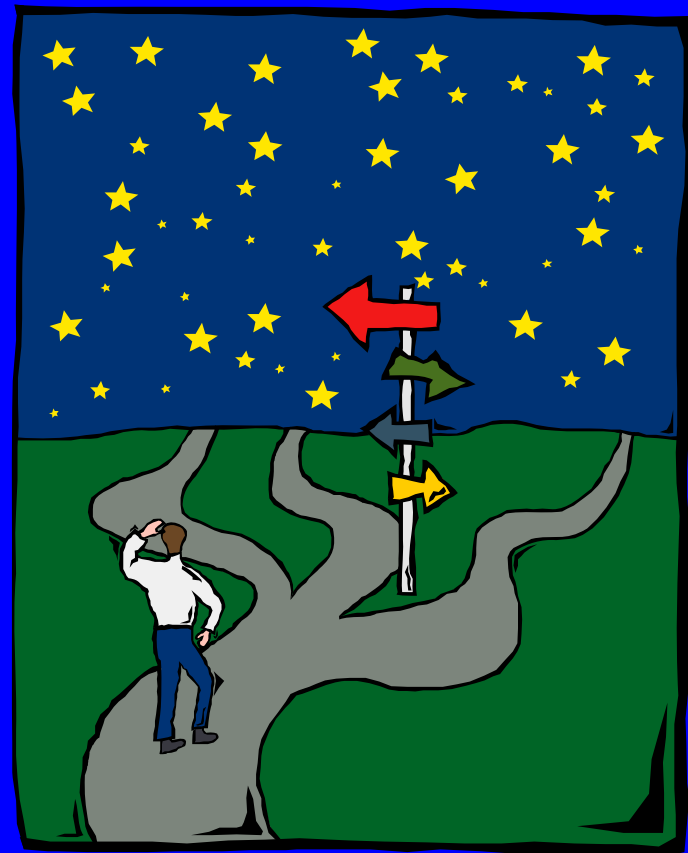


- “Reduced rate” method
- *or*
- “Specific relief” method

# ALLOCATING RELIEF

- Single rate
  - *or*
  - Multiple rates
- 

- \$20,000 ceiling
- *or*
- Lower ceiling



# LOW-VALUE VEHICLES

- Specific exemption (i.e., 100% relief)

*or*

- Rely on treasurer's writeoff authority

*or*

- Bill them anyhow

