This policy brief presents an analysis of several potential reforms of the personal property tax system in Georgia. Taxable personal property consists of property that is moveable and can be seen, weighed, measured, felt, touched or is otherwise perceptible to the senses. Included as personal property are inventories, livestock, machinery and equipment. Personal property is a large share of the property tax base in Georgia. But there are concerns regarding the inconsistency of personal property assessment across counties, the inconsistent treatment of the same types of property within the same county, the rate of depreciation for machinery and equipment used in industries where technology is rapidly advancing, implementing changes in personal property tax that result from court decisions, the assessment of items such as older boats, older farm equipment, and the assessment of idle equipment. The analysis in this brief is based on a report on personal property taxation prepared by the author.

POTENTIAL REFORMS

Eliminate the Tax on Personal Property

The personal property tax has been a decreasing share of local taxable assessed value in many states. In Georgia, personal property decreased from 36.6 percent of locally assessed value in 1956 to 13.7 percent in 1996. A total of nine states did not tax personal property in 1991.

Eliminating the tax on personal property would have a substantial impact on property tax revenues. While the personal property tax represents about 13.7 percent of total general property taxable value, it is a substantial portion of the total assessed value of all property in some counties. For example, the assessed value of personal property is over 20 percent of total net assessed property value for 30 counties. Personal property as a proportion of total net assessed property value ranges from 1.4 percent in Burke County to 45.3 percent in Twiggs County. Since counties apply the same millage rate to both real and personal property, total property tax revenues derived from personal property approximately equals the share of personal property in the tax base for each county. Careful consideration should be given to methods of replacing this revenue if the personal property tax was eliminated.

Exempt Selected Personal Property

The personal property exemptions offered by the states vary widely. A total of 33 states fully exempt and three states partially exempt business inventories while nine states fully exempt agricultural personal property, 35 fully exempt household personal property, and 32 fully exempt motor vehicles. Relative to other states, Georgia exempts few of the major types of personal property. Thus, consideration could be given to expanding...
the list of personal property tax exemptions. Interviews with county tax officials identified older property, especially farm implements and attachments, boats, heavy construction and manufacturing equipment used in nontransferable production processes as being particularly hard to assess. Many states exempt these types of property.

Current Georgia law has two personal property exemptions based on value: (1) an exemption for domestic animals and tools of trade valued at less than $300 (established in 1978) and (2) an exemption for personal property accounts worth less that $500 in total (established in 1986). Increasing the minimum value of the exemptions for tools and total value of personal property will decrease the administrative and compliance cost of the personal property tax system.

Small accounts generate a very small portion of tax revenue in Georgia counties. Personal property tax accounts with a market value of $15,000 or less generate less than one percent of total personal property tax revenues for Gwinnett County, 2.8 percent for Bibb County and 1.4 percent for Laurens County. In contrast, large accounts generate a substantial portion of personal property tax revenues. Accounts valued at greater than $500,000 generate 85 percent, 74 percent, and 86 percent of personal property tax revenues for Gwinnett, Bibb, and Laurens counties, respectively. Raising the exemptions to $500,000, $10,000 or even $15,000 would have a small impact on tax revenues and would decrease administrative costs of a reported $125 per account.

Modify the depreciation schedule

Georgia law allows assessors to use the original cost of the property, depreciation or obsolescence and increased value due to inflation as factors in determining value of personal property. The current depreciation schedules recommended by the Georgia Department of Revenue divide depreciable personal property into four groups: (1) property with a useful life of 1 - 7 years, (2) property with a useful life of 8 - 12 years, (3) property with a useful life of 13 or more years and (4) computer equipment. The basis for depreciation is the original cost of the property. Property is depreciated by a fixed percentage each year and all property is taxed based on some minimum residual value regardless of its purported useful life. The depreciation schedule includes an index factor which adjusts the value of property due to inflation.

An option is to replace the current depreciation schedule with the federal income tax depreciation schedule. Advantages of this option are: firms already use the federal depreciation schedules when calculating their federal income tax; it would reduce compliance costs since firms would have to calculate depreciation of assets based on one set of schedules as opposed to using both the federal and state schedules; using the federal depreciation schedules could improve the auditing process and decrease auditing costs. One disadvantage is that the state will have to pass new legislation to adopt the new schedule. In addition, the state will be subject to whatever changes the federal government makes or fails to make in the depreciation schedule.

There are two main factors, beyond simplification of the depreciation process, to contemplate when considering a change to the federal depreciation schedule: the uniformity provision of the Georgia Constitution and the implications for revenue. There are three major differences between the federal depreciation schedules and the Georgia recommended schedule: (1) the federal schedules depreciate most assets at a faster rate than the Georgia schedule; (2) the Georgia depreciation schedule includes an index factor which allows the value of an asset to appreciate due to inflation while the federal depreciation schedules do not; (3) when the class life of an asset is passed, the asset is no longer has value and therefore incurs not tax liability under the federal depreciation schedules while the Georgia schedule continues to tax a portion of the original value of the assets as long as the asset is in use.

The uniformity provision of the Georgia Constitution requires that real and tangible personal property be taxed alike. Both types of property are assessed at fair market value. One complication is that the federal depreciation schedules consist of two methods of depreciation — General Depreciation System (GDS) and Alternative Depreciation System (ADS) — with various schedules for different types of property. Different depreciation schedules provide widely divergent values for fair market value of personal property. Since the federal depreciation schedules return lower values, in many cases, than the current Georgia depreciation schedule, use of the federal schedules may increase the divergence between the fair market value of real and personal property and provide fertile ground for legal cases. If the federal depreciation schedule is adopted, careful attention should be given to potential legal implications.

Use of the federal schedules would greatly reduce taxable value for most assets and therefore tax revenues from the personal property tax. The difference in assessed value and tax revenue is substantial. For the sample of large firms, there is an average decrease in personal property tax revenues of 36 percent, 63 percent and 83 percent.
respectively, for Gwinnett, Bibb, and Laurens counties. For the small-firm sample the average decrease is also substantial (43 percent, 58 percent, and 69 percent, respectively).

An alternative to adopting the federal depreciation schedules is to adopt the class lives used under the federal system but continue to use the current Georgia depreciation schedule for each property group. This approach would reduce compliance costs because assets would have the same class life under both the federal and state personal property tax system. Another advantage to this approach is that special tools and devices use in manufacturing have a shorter class life under the federal system than the current Georgia depreciation system which would address some of the complaints of business groups. A disadvantage is that the shortened class life for some manufacturing assets will have a negative impact on personal property tax revenues.

Administrative Issues

One of the largest differences among counties in administration of the personal property tax concerns auditing practices. Some counties regularly audit their personal property tax accounts while others basically do no auditing, but simply accept the numbers and values of property that businesses record on their property reports. Thus, to the extent that businesses do not file personal property tax returns or submit incorrect returns, variation in the level of auditing may lead to differences in the assessed value of personal property among counties.

Businesses often feel that they are treated unfairly by tax officials while tax officials feel as if businesses purposefully misreport assets to decrease tax liability. Self-reporting makes the personal property tax hard to administer. The ultimate purpose of audits is to increase compliance in the personal property tax system. In Georgia, the penalty for incorrectly reporting personal property tax is among the lowest in the Southeast. When a county audits a personal property tax account they audit the return for the current tax year and three prior years. If the account is found to be in default, the firm must pay back taxes and 10 percent of total taxes due (simple interest). North Carolina audits the current tax year and five prior years and charges a 10 percent per year cumulative penalty on taxes due for a maximum penalty of 60 percent if property has not been reported for 6 years. Tennessee charges a 10 percent penalty on taxes due, plus interest from the date the taxes were due. If a Georgia firm misreports tax liability for five years before it is audited, unpaid taxes in the first two years are uncollected since these years are not included in the audit. The low penalty for misreporting combined with the low audit rates in many counties may encourage firms to misreport personal property to lower their tax liability. Requiring counties to perform audits, collecting data on the number and returns to audits in each county and increasing the penalty for misreporting property value would increase uniformity of the treatment of personal property across counties.

CONCLUSION

A few changes in Georgia’s current personal property tax law could ease administration and compliance costs and improve uniformity of assessment between counties. The options considered in this analysis are:

- Eliminate the personal property tax. This option would have a substantial effect on revenues, decreasing revenues by approximately 13.7 percent on average and up to 45 percent.

- Expand the list of exemptions. This may increase the number of business start ups since it lowers the cost of doing business in the state, but it may have a substantial impact on revenues.

- Increase the minimum value of the exemption on domestic animals and tools of trade ($300 currently) and total value ($500 currently) to remove small accounts from the property tax system. This option would reduce administrative costs and have a very small impact on revenues (less than a three percent reduction for even a large increase).

- Change the exemption to a deduction. This would increase the equity of the system but may cause owners of property to subdivide accounts if the deduction is large.

- Replace the current depreciation schedule with the federal depreciation schedules to reduce compliance costs and potentially increase returns to auditing. Disadvantages are the General Assembly will have pass legislation each time there is a change in the federal schedule, and it would cause a substantial reduction (36 to 83 percent) in tax revenues. In addition, the choice of two federal depreciation schedules affects the uniformity of treatment of personal property.

- Require counties to conduct audits. This option would increase the uniformity of treatment of personal
property among counties. Some counties may not have the administrative capacity to conduct audits.

- Increase the penalty for misreporting personal property to improve the uniformity of treatment among firms within the personal property tax system. This may not be popular with business groups.

- Develop and implement a procedural manual for county property tax officials to provide standards which should increase uniformity of treatment between counties. The manual should include supplements that address recent court decisions concerning the treatment of property. (This manual is currently under review.)

- Develop a way of measuring uniformity for personal property, similar to sales ratio studies for real property, to provide a method for evaluating county performance.

ACKNOWLEDGMENTS

Special thanks to the following tax officials who provided much of the information and data used in this study: Larry Griggers of the Georgia Department of Revenue, Calvin Hicks and Len Harper of Bibb County; Jeffrey Underwood of Dodge County; Kay Koon of Fulton County; Sharlene Brantley, Jeanie Logue and Chuck Nazerian of Laurens County; and especially Steve Pruitt of Gwinnett County who provided insight for many of the ideas developed in the study.

For a free copy of the study from which this Policy Brief is drawn, or any of the other publications listed, call the Fiscal Research Program at 404/651-4342, or fax us at 404/651-2737.

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