Fiscal Research Center

policybrief

October 2007, Number 171

REPLACING ALL PROPERTY TAXES: AN ANALYSIS OF REVENUE ISSUES

The GREAT Plan for Georgia calls for the elimination of all property taxes, with local government property tax revenue being replaced by state grants. In this Policy Brief we provide an estimate of the amount of revenue that would have to be replaced. We also discuss the role of local sales tax revenue in replacing property taxes. This Policy Brief is part of series of reports and policy briefs that examine the GREAT Plan.

Property Taxes

In this section we discuss the revenue that would have to be replaced if the state eliminated all property taxes and replaced them with state grants. In 2006, Georgia's local governments plus the state had combined property tax levies, including those on motor vehicles and utilities, of more than $9.6 billion (Table 1).[1] Combined with other revenue associated with property taxes, total loss to Georgia's local governments from elimination of property taxes is over $10.8 billion for 2006.

Table 1 presents property tax levies calculated using a database obtained from the Georgia Department of Revenue listing the net assessed values and millage rates for all school districts, counties, cities, and special districts in the state. We use inflated 2005 figures for four counties – Bibb, Madison, Telfair, and Twiggs – as they were not reported in the 2006 database.

Property tax levies do not reflect all revenue associated with property taxes. Data from the Georgia Department of Community Affairs (2005) (DCA) indicates these other property tax revenue sources may generate about 12 percent additional local revenue. These additional sources include FI FA and other penalty revenue, real estate transfer and recording revenue, intangible property tax revenues, interest earned on received unspent property tax revenue, and property tax collection fees. If these revenues are included, the estimated total loss from the elimination of property taxes, at 2006 levels, increases to $10.8 billion.

The GREAT Plan for Georgia would allow property taxes to be collected to pay off general obligation bonds. Ignoring the associated revenue and excluding the property taxes levied to pay off general obligation bonds, in 2006, it would have been necessary to raise $9.4 billion to replace all non-general obligation debt property taxes. To the extent the state and local governments generated additional revenue through fines, etc., additional revenue would have to be generated.

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TABLE 1. 2006 GEORGIA PROPERTY TAX LEVIES AND OTHER PROPERTY TAX RELATED REVENUES (IN MILLIONS)

	Operating	Debt	Total
Schools	$5,383	$167	$5,550
Counties	$2,726	$79	$2,805
Cities	$775	$57	$831
Special Districts	$393	$14	$406
State	$79		$79
Subtotal	*$9,355*	*$316*	*$9,671*
Plus 12%	$10,478	$353	$10,831

Four counties not reported in 2006, inflated 2005 data used.
Source: Author's compilation of Georgia Department of Revenue and Department of Community Affairs Data.

Eliminating property taxes will reduce some costs and generate additional income tax revenue. If property taxes are eliminated, then counties can eliminate its tax assessor and tax commissioner offices. In 2005, DCA data suggests these offices cost $193.6 million. However, the Department of Revenue would have to add additional staff to handle the increased number of vendors that would have to pay sales tax, and there would be some continuing administrative expense for those jurisdictions that would continue to employ a property tax to pay off existing bonded debt. With no property tax, the Homeowner Tax Relief Grants do not have to be provided. In 2006, this amounted to $412.3 million.

Property taxes are a deduction for income tax purposes, but sales taxes would not be. The elimination of property taxes will thus increase state income tax revenue. But the elimination of property taxes will also increase the deduction of federal income taxes for state income tax purposes. Based on IRS reported deductions of property taxes, we estimate that the removal of the property tax deduction will generate an additional $105.6 million in income tax revenue for the state.

The GREAT Plan calls for an income tax credit for low income households to offset the increased sales tax from removing the exemption of food for home consumption and of prescription drugs. The only details we have found regarding this credit suggest that families with an income less than twice the poverty rate will be eligible for the credit. We estimate that the removal of the food for home consumption exemption will result in an increase in sales tax payments of between about $85 million and $100 million for these households. The cost of the credit will depend on the phase out rate and if the credit is refundable, i.e., can be claimed even if the family has no income tax liability. Without more details we ignore the additional revenue necessary to finance this credit.

The reduction in the cost of tax administration, the elimination of Homeowner Tax Relief Grants, and the additional income tax revenue sum to $711 million. Thus, sales tax revenue would have to increase by about $8.6 billion to replace property taxes.

Using Local Sales Tax Revenue

The expansion of the sales tax base through the elimination of sales tax exemptions and the addition of services to the sales tax base called for by the GREAT Plan for Georgia will generate additional sales tax revenue for both the state government and for local governments. Of the increase in sales tax revenue from expanding the sales tax base, about 60 percent of the additional revenue will go to the state through its 4 percent sales tax, and about 40 percent will be collected through local sales taxes. (We estimate that the weighted average local sales tax rate is 2.7 percent.)

Discussions of the GREAT Plan for Georgia suggest that the total additional sales tax revenue from expanding the sales tax base can go to replacing the property tax. Thus, on a net basis, it would be necessary to raise state sales tax revenue by the difference in property taxes and the additional local sales tax revenue in order to keep local governments whole in the aggregate. Under this assumption, the necessary additional state sales tax revenue would be 60 percent of $8.6 billion, or about $5.2 billion. The

$3.4 billion in additional local option sales tax revenue would make up the difference.

An issue that arises in determining the size of the state grants is how the state will account for the additional sales tax revenue generated by local option sales taxes. If this revenue is to be counted toward the revenue required to replace property taxes, then the state would have to reduce the state grants awarded to each local governments by the additional sales tax revenue generated by that local government. And, the state would have to make that calculation for each of the some 900 local governments in Georgia. Because services are unlikely to be the same percentage of sales tax base in each county, it would not be feasible to simply multiply each county's sales tax by the same percentage to determine how much each county's sales tax base increased from the elimination of the exemptions and the addition of services.

There is a further complication, namely that there are jurisdictions in which the increase in sales tax revenue will exceed the property tax levied by the jurisdiction. Currently, there are at least 133 local governments that do not impose a property tax. MARTA, for example, imposes no property tax but currently accounts for about 7.5 percent of all local sales tax revenue. Buford, Jonesboro, and Stockbridge, for example, levy no property taxes, relying instead principally on local options sales taxes. Thus, unless the state is going to require such local governments to turn over the additional sales tax revenue to the state for redistribution, the state will have to generate more than 60 percent of the approximately $8.6 billion needed to replace the property tax. We have not attempted to estimate the revenue implications of this for The GREAT Plan.

The issue of relating local sales tax revenue and the state grants is one of many issues that need to be addressed in determining how local governments will be financed through state grants. Many of these other issues are raised in Sjoquist (2007).

References

Sjoquist, David L. (2007). "Issues Associated with Replacing the Property Tax with State Grants." FRC Policy Brief No.157 (July 2007).

Georgia Department of Community Affairs (2005). *2005 Report of Local Government Finances*. Atlanta.

Note

1. The Georgia Department of Revenue, Local Services Division, posts annual property tax base and levy information for all property taxing jurisdictions at http://www.etax.dor.ga.gov/ptd/cds/csheets/menu.shtml. The levy data in Table 1 for types of local government operating and debt service levies is calculated from the databases for 2005 and 2006. Additionally, the Georgia Department of Community Affairs conducts an Annual survey of Local Government Finances, developing data for relatively detailed revenue sources and objects of expenditure for Georgia's cities and counties.

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