SENATE TAXATION
EXHIBIT NO. 7
DATE 3-3-05
BILL NO. SB 463

# FISCAL NOTE

**Bill #:** SB0463 **Title:** Eliminate local option vehicle tax and revise local option fee

**Primary Sponsor:** Story, B **Status:** As Introduced

2/22/05 2/21/05

Sponsor signature Date David Ewer, Budget Director Date

## Fiscal Summary

| | FY 2006 Difference | FY 2007 Difference |
|---|---|---|
| **Expenditures:** | | |
| General Fund | ($13,995) | ($20,000) |
| **Revenue:** | | |
| General Fund | $0 | ($102,541) |
| **Net Impact on General Fund Balance:** | $13,995 | ($82,541) |

- ☒ Significant Local Gov. Impact
- ☐ Included in the Executive Budget
- ☐ Dedicated Revenue Form Attached
- ☒ Technical Concerns
- ☒ Significant Long-Term Impacts
- ☐ Needs to be included in HB 2

## Fiscal Analysis

ASSUMPTIONS:

1. Effective January 1, 2006 (calendar 2006), SB 463 replaces the local option vehicle license tax based on the value of a vehicle, with a new local option vehicle flat fee based on three (3) categories of vehicle ages.
2. The proposal also provides that revenue received in calendar year 2006 cannot increase more than 10% over the amount received in calendar 2005.
3. Additionally, the bill allows contractors to use the local option flat fee paid to local governments to be credited against the amount of contractor's gross receipt tax they owe. This fiscal note does not provide an estimate of the impact that this provision would have on the state general fund, but it is likely that allowing the local option flat fee to be used as an offset to the contractor's gross receipts tax would reduce general fund slightly in each year that this bill is in effect.
4. The current law local option vehicle tax is deductible for individual income tax purposes. Section 3 of the bill provides that the proposed local option flat fee also may be taken as a *state* itemized deduction for individual income tax purposes. (However, per technical note #1, the new tax would not be deductible on federal income taxes.) Because of the delayed effective date, deduction of the local option fee would not occur until a taxpayer files a tax year 2006 income tax return. The first year the state general fund will see an impact is FY 2007.



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5. This bill would require a vehicle owner to pay 5 times the local option flat fee or $30 (5 x $6 = $30) when permanently registering their vehicle. This has no impact on the state general fund.
6. The Department of Justice (DOJ) motor vehicle database shows that local option vehicle taxes totaled $29,382,008 in calendar year 2003.
7. The table below shows the distribution of light motor vehicles that paid the local option vehicle tax by age, and the total revenue collected from each group. By using the distribution of light motor vehicles by vehicle age and this bill's proposed *maximum* flat fees, it is estimated that in calendar year 2003 the local option flat fee would have generated $36,961,862 in taxes for local government, if the *maximum* flat fee allowed by the proposed bill had been levied. (Note that not all counties impose a local option tax.)

**Calendar 2003 Distribution of Local Option Vehicle Tax Collected By Age of Light Motor Vehicle**
**Estimated Proposed Law Revenue of Local Option Flat Fee Based on CY2003 Distribution of Light Motor Vehicles**

| Age of Light Motor Vehicle | Count of Light Motor Vehicles | CL Revenue From Local Option Tax | Proposed Law Fee | Est. Revenue From Local Opt. Flat Fee | Difference in Revenue |
|---|---|---|---|---|---|
| 4 years old or less | 195,678 | $ 18,762,153 | $ 125 | $ 24,459,750 | $ 5,697,597 |
| between 5 and 10 years old | 224,660 | $ 8,208,262 | $ 46 | $ 10,334,360 | $ 2,126,098 |
| 11 or more years old | 361,292 | $ 2,411,593 | $ 6 | $ 2,167,752 | $ (243,841) |
| Total | 781,630 | $ 29,382,008 | | $ 36,961,862 | $ 7,579,854 |

8. However, section 11 sub (5) of the bill limits the amount of revenue that can be generated from the new flat fees in tax year 2006 to just 10% more than the amount levied in tax year 2005.
9. Under the 10% limitation, instead of generating $36,961,862 the local option flat fee would be limited to $32,320,209 ($29,382,008 x 110%).
10. If counties assessed the maximum $6 fee on vehicles 11 years or older, it would not generate the same amount of revenue as the current ad-valorum local option tax. Counties could increase the fee for vehicles 10 years old or newer to make up the difference, but it is unknown if counties would, or how counties would determine those fees. For purposes of this fiscal note, it is assumed that counties would only increase the amount of revenue generated from each grouping of vehicles by 110%.
11. For purposes of this analysis, all Montana counties would levy a flat fee lower than the maximum allowed under the bill on motor vehicles that are new to 10 years old. For vehicles that are 11 years old or older counties would levy the maximum flat fee of $6 and still generate $243,841 ((361,292 x $6.00) - $2,411,593)) less in revenue than generated under current law.
12. Per the aforementioned assumptions and shown in the table below, the total amount of revenue generated by the new fees in calendar year 2003 is $31,835,209, or an overall increase of $2,453,200.

**Calendar Year 2003 Distribution of Local Option Vehicle Tax Collected By Age of Light Motor Vehicle**
**Estimated Proposed Law Revenue of Local Option Flat Fee**
**Based on Limiting Increase in New Revenue to 10% above Current Renevue**

| Age of Light Motor Vehicle | Count of Light Motor Vehicles | CL Revenue From Local Option Tax | Maximum Allowed Under FL | Estimated Ave Eff Flat Fee | Difference in Revenue |
|---|---|---|---|---|---|
| 4 year old or less | 195,678 | $ 18,762,153 | $ 20,638,368 | $ 105.47 | $ 1,876,215 |
| between 5 and 10 years old | 224,660 | $ 8,208,262 | $ 9,029,088 | $ 40.19 | $ 820,826 |
| 11 or more year old | 361,292 | $ 2,411,593 | $ 2,167,752 | $ 6.00 | $ (243,841) |
| Total | 781,630 | $ 29,382,008 | $ 31,835,209 | | $ 2,453,200 |

13. Under current law and proposed law (15-30-121(1)(h) MCA) local option motor vehicle fees can be deducted from income when computing net income for state income tax purposes.
14. Tax year 2003 Montana income tax return data indicates that the average effective income tax rate for filers of a Montana income tax return is 3.85%. If this bill were in effect during calendar 2003, it would have reduced Montana income tax liabilities by the amount of the excess of the proposed tax over the current law tax, multiplied by the average effective income tax rate, or by $94,448 ($2,453,201 x 3.85%). The table below shows the estimated reductions in income tax liability due to increased collections of local option motor vehicle revenue.
15. Anticipated light vehicle growth, as shown in the table ranges from 3.65% for calendar 2004, to 2.36% for calendar 2007.

**Estimated Reduction in Montana Income Tax Liability Due to Proposed Changes to Local Option Motor Vehicle Taxes**

| Calendar Year | Growth Rate[1] | Difference PL - CL | | Effective Tax Rate | | Reduction in Income Tax Liability |
|---|---|---|---|---|---|---|
| 2003 | - | $2,453,200 | x | 3.85% | = | $94,448 |
| 2004 | 3.65% | $2,542,742 | x | 3.85% | = | $97,896 |
| 2005 | 2.25% | $2,599,954 | x | 3.85% | = | $100,098 |
| 2006 | 2.44% | $2,663,393 | x | 3.85% | = | $102,541 |
| 2007 | 2.36% | $2,726,249 | x | 3.85% | = | $104,961 |

[1] OBPP's Fiscal Years 2006 - 2007 Revenue Estimates

16. FY 2007 revenue reductions are based on calendar year 2006 reductions (shown in the table).
17. Based on the assumptions listed above, it is estimated that in FY 2007 the state general fund would experience a reduction in total revenue of $102,541.

Administrative Impacts

**Department of Justice**

18. Operating expenses would decrease $20,000 due to the elimination of the need to purchase the vehicle valuation tapes to update the motor vehicle database annually.
19. Operating expenses will increase $6,005 in FY 2006 for programming analysis, design, implementation, and computer processing time (52 hours programming and 5 days computer time) to replace the existing county option tax table to reflect the new three bands of county taxes, and allow each county to charge different amounts or nothing, depending on local public hearings and elections.

FISCAL IMPACT:

| | FY 2006 Difference | FY 2007 Difference |
|---|---|---|
| Expenditures: | | |
| Operating Expenses | ($13,995) | ($20,000) |
| Funding of Expenditures: | | |
| General Fund (01) | ($13,995) | ($20,000) |

| | | |
|---|---|---|
| Revenues: | | |
| General Fund (01) | $0 | ($102,541) |
| Net Impact to Fund Balance (Revenue minus Funding of Expenditures): | | |
| General Fund (01) | $13,995 | ($82,541) |

EFFECT ON COUNTY OR OTHER LOCAL REVENUES OR EXPENDITURES:
Since the effective date of this bill, January 1, 2005, is in the middle of FY 2006, local governments would see a partial year impact in FY 2006, and a full year impact in FY 2007. For purposes of this fiscal note, it is assumed that local option taxes are receive evenly throughout the year, with 50% being received each half of the fiscal year.

Using the aforementioned assumptions, it is estimated that local governments would see their local option motor vehicle revenues increase by $1,331,697 ($2,663,393 x 50%) in FY 2006 and $2,694,821 (($2,663,393 x 50%) + ($2,726,249 x 50%)) in FY 2007. Under this bill, 50% of the increase in revenue will accrue to county governments, and 50% would accrue to cities and towns.

LONG-RANGE IMPACTS:
Revenue to the state general fund will decrease by about $105,000 in FY 2008, and will continue to grow as the number of registered light motor vehicles increases.

TECHNICAL NOTES:
1. Because the existing local option vehicle tax is an ad valorem tax, it is deductible under federal law and state law. Since the new local option flat fee is based on age, it is no longer deductible for federal income tax purposes, whereas it would be a deduction for state purposes.
2. Section 11 sub (5), which specifies a 10% limit on revenue received from tax year 2005 to tax year 2006, will makes this bill difficult for local government to administer. The 10% cap on the increase in local option flat fee revenue assumes that counties can manage the growth of revenue by lowering the amount of each flat fee. It would be difficult for counties to project revenue, and cap revenue at the 10% set limit based on fee amounts because the absolute number of vehicles registering in a given year, and the age of vehicles in a county can vary significantly each year. For instance, if counties set their flat fees on an anticipated number of vehicles with a mix of ages, then their citizens buy more new(er) vehicles than they projected (or population growth exceeds expectations), revenue from local option flat fee could exceed the 10% increase cap.
3. Additionally, there are no provisions in the bill specifying how a county would resolve a revenue increase above the proposal's 10% cap if a county under projected their revenue amounts and applied higher fees.
4. The 10% revenue limitation provided for by section 11 sub (5) is only for tax year 2006. There is no limitation specified for succeeding years.
5. Section 11, provides for a new fee based on the age of a vehicle, but does not provide for how age would be determined. Language, like that under 61-3-561(3), MCA, should be included in section 11. 61-3-561(3), MCA, reads as follows: *For the purposes of this section, "vehicle age" means the age of the vehicle determined by subtracting the manufacturer's model year of the vehicle from the calendar year for which the registration fee is due.*