

# Fast Facts

## Exempting Business Property Taxes: HJR 101 and SJR 11

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### Background

HJR 101 asks state voters in November to consider a constitutional amendment allowing counties to exempt “newly entered” business personal property (Inventory, Machinery/Equipment (M&E), and Other Personal Property such as storage buildings and computers) from “property tax rolls.” If voters approve measure, the Legislature must pass a bill setting parameters of county authority. Upon this action, counties can pass an ordinance adopting an exemption authorized by the Legislature. The estimated FY 2010 property tax collections on business personal property are \$260 million. Of the \$260 million, M&E makes up \$128 million (49%), Inventory \$62 million (24%), and Other Personal Property \$70 million (27%). Of the \$260 million, an estimated 20 percent or \$54 million is collected from coal business personal property.<sup>1</sup>

As currently written, counties, if they adopt the exemption, would likely experience a decline in overall business personal property tax collections. This would be driven largely by a sharp reduction and eventual elimination of assessed inventory valuations. This is because over time almost all inventories would be considered “new” and would therefore be exempt. A gradual decline in M&E and Other Personal Property tax collections could occur as some businesses flock to a border county that exempt this property from taxation. In the long run, however, most M&E and Other Personal Property would become “new” and therefore exempt from taxation.

The central argument being made by proponents of this measure is to increase manufacturing investment and employment. These arguments, so far, are unsubstantiated by empirical evidence.

### POTENTIAL FISCAL IMPACT ON COUNTIES

Of the 43 Counties that have excess levies, 21 have excess levies at the maximum rate (Class 1:22.95¢/\$100) allowed by statute. If one or more of the 21 counties<sup>2</sup> experiences a drop in assessed valuation of property due to exempting business personal property, then services will have to be cut to make up for the revenue loss. If one or more of 22 counties<sup>3</sup> with excess levies below the maximum statutory rate experiences a decline in assessed valuation due to exempting business personal property, then the county board of education would have to increase its levy rate to make up the difference or chose to cut service or program costs. As a result, counties would either shift the tax burden to other taxpayers or would have to cut service or program costs.

### PONTENTIAL FISCAL IMPACT ON STATE

The School Aid Formula provides a program allowance to counties at a rate of 90 percent. For example, if a county’s projected regular levy tax collections are \$1 million and the total program allowance under the formula is \$10 million the state aid to the county would be \$9.1 million (\$10 million – 90% of \$1 million). If a county’s projected tax collections decrease as a result of exempting business personal property to \$800,000, then state aid cost for this county will increase by \$180,000 (\$10 million – 90% of \$800,000). Without Legislative action the state would incur costs. To avoid increases in the county allowance under the Public School Support Program (school aid formula), the Legislature would have to increase regular levy rates to make up for decreases in tax collections. Consequently, either action would cause a shift in taxes among taxpayers to make up the difference.

<sup>1</sup> “The West Virginia Coal Economy 2008,” Bureau of Business and Economic Research, West Virginia University and Center for Business and Economic Research, Marshall University, February 2010, pp. 29.

<sup>2</sup> Boone, Brooke, Cabell, Doddridge, Fayette, Hancock, Jackson, Jefferson, Lincoln, Logan, Marion, McDowell, Mercer, Mineral, Mingo, Putnam, Raleigh, Tyler, Wayne, Wetzel, and Wyoming.

<sup>3</sup> Berkley, Calhoun, Clay, Gilmer, Harrison, Kanawha, Lewis, Marshall, Mason, Monongalia, Monroe, Morgan, Nicholas, Ohio, Pleasants, Preston, Ritchie, Taylor, Upshur, Wirt, and Wood.

## OTHER CONSIDERATIONS

1. According to 2006 Ernest & Young study, West Virginia's total business property (real and personal) tax burden is slightly above the national average with 20 states ranking higher. In terms of "overall cost of doing business," West Virginia ranks 13 percent below the national average – according to the Milken Institute and WV Commerce Department.<sup>4</sup> There is no obvious relationship between state and local business taxes and recent state employment growth trends.
2. The inventory and machinery/equipment tax has not been proven to be a key deterrent to business location decisions and employment of wholesale trade or manufacturing in West Virginia. In fact, these industries tend to employ more people in "higher tax" counties than in "lower tax" counties.
3. Taxes only have a small effect on business location decisions and job growth, representing a very small cost of doing business (4-5 percent). Businesses are more concerned with the higher costs of labor, transportation, utility, and occupancy. Availability of inputs (coal, natural gas, limestone, ect), access to markets, quality public services, a highly trained workforce, and high quality of life are also big factors affecting business location decisions. The existing literature and our analysis supports the conclusion that business property taxes, in general, do not play a major role in business site locations.
4. The consensus among economists is that the average responsiveness (or tax elasticity) for a \$100 million business tax cut is \$20 million, resulting in an \$80 million reduction of revenue. If the proposed amendments did boost revenue, it would be state and city revenue, not county revenue.
5. Since 2007, the state has reduced major business tax revenues by an estimated \$165 million. Upon full impact, the major business tax cuts will cost the state an estimated \$240 million per year.

### Policy Options

- a. Amend Resolution from "newly entered on the property tax rolls" to "newly entered on any county's property tax rolls" or specify only manufacturing personal property is exempt. This will ensure the exemption is better targeted toward new capital and it will reduce the incentive to move property from one county to another or from transferring property from an old company to a new one.
- b. Amend Resolution by including a "home rule" provision giving local governments the option of levying a sales or income tax to replace any lost revenue.
- c. Pass a study resolution that examines the potential impacts of business personal property taxes on manufacturing employment.
- d. Modify Resolution to exempt industries not directly related to boosting manufacturing employment:

Option 1: Coal and natural gas industries

Option 2: Inventory

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· Joomi Kim, Andrew Phillips, and Robert Cline, "Property Taxes on Business Capital: A Large and Growing Share of State and Local Business Taxes," *State Tax Notes*, March 27, 2006. (NOTE: This is the same study that Deputy Director of Revenue Mark Muchow has used in his presentations to the Legislature.)

<sup>4</sup> <http://www.milkeninstitute.org/research/research.taf?cat=indexes&function=detail&ID=29&type=CDB>