

SUBJECT: Exempting from property taxation motor vehicles leased for personal use

COMMITTEE: Ways and Means — favorable, with amendment

VOTE: 7 ayes — Oliveira, McCall, Hartnett, Y. Davis, Heflin, Keffer, Ritter
0 nays
4 absent — Craddick, Bonnen, Hilbert, Ramsay

SENATE VOTE: On final passage, April 26 — voice vote (Shapleigh and Truan recorded nay)

WITNESSES: For — Phil Cates and Mark Johnston, National Vehicle Leasing Corp.; Jim Robinson, Texas Association of Appraisal Districts
Against — Dick Lavine, Center for Public Policy Priorities

BACKGROUND: Under the Texas Constitution, Art. 8 , sec. 1, most income-producing personal property is subject to ad valorem taxation. Under authority of sec. 1(d), the Legislature has exempted from taxation tangible personal property not held or used to produce income. However, the Constitution also gives local taxing units the option of overriding the exemption and levying ad valorem taxes on most exempt personal property, although relatively few do so. According to the standard practice of appraisal districts, the exemption applies to motor vehicles *owned* by a person and not used for income-producing purposes, but leased vehicles are not exempt.

In November 1999, voters approved SJR 21 by Carona, a proposed constitutional amendment authorizing the Legislature to exempt from property taxes vehicles leased for personal use and not used to produce income. The amendment also allows the Legislature to limit the ability of local taxing units to override the exemption. The 76th Legislature did not adopt enabling legislation that would take effect if the proposed amendment was approved.

DIGEST: SB 248, as amended, would entitle vehicle owners who leased vehicles not held to produce income and not used primarily to produce income to property-tax exemptions on such vehicles leased on or after January 1, 2002. A vehicle would be presumed to be used primarily for non-income-producing activities if at least 50 percent of the annual miles it was driven were for non-income-producing purposes.

The comptroller would have to develop exemption application requirements and procedures to determine whether a vehicle qualified for the exemption. The comptroller would have to adopt and issue forms to be distributed by owners (leasing companies) to their customers for obtaining their names, addresses, and driver's license or personal identification certificate numbers. The forms also would have to include an oath certifying that the vehicle was not held for production of income and was used primarily for non-income-producing activities. Forms would have to include notice of penalties for falsification under Penal Code, sec. 37.10. Owners would have to maintain forms and make them available to chief appraisers for inspection and copying at reasonable times. If an owner failed to maintain a completed form, the owner would have to render the vehicle for taxation and could not apply for an exemption for the vehicle.

The comptroller also would have to develop a property report form to be completed by lessors (leasing companies). The form would have to list each leased vehicle the lessor owned on January 1 of the tax year, including its year, make, model, vehicle identification number, the lessee's name, the address where the vehicle was kept, and whether it had been designated as not to be used for income production. Lessors would have to submit completed forms to chief appraisers.

The governing body of a city could adopt an ordinance before January 1, 2002, providing for the taxation of leased vehicles that otherwise would be exempt under the bill.

The bill would take effect January 1, 2002, and would expire December 31, 2003, unless continued by the Legislature.

SUPPORTERS
SAY:

SB 248, as amended, would implement the property-tax exemption for personal-use leased vehicles that Texas voters authorized in the 1999 constitutional amendment. Auto leasing has become an attractive option for many people and families. It would be even more popular in Texas if not for the punitive property tax that never was intended to be levied on those who lease vehicles for non-business purposes. Consumers deserve a tax break from what has become an anachronism in today's market.

The leased-vehicle tax is based on ownership by either the financing entity or the leasing company earning income from the vehicle. These entities pass the cost on to the consumer, which is unfair to people who do not use the vehicles primarily for business purposes. Texas is one of the few states that allows property taxes to be imposed on personal-use leased vehicles. This actually represents double taxation for the consumer, who also pays sales tax on the lease. This has led to Texas having one of the lowest leased-vehicle rates in the nation – about 17 percent of new-vehicle leases, compared to the national average of about 23 percent, according to the Legislative Budget Board (LBB). The auto leasing industry estimates that more than 60 percent of vehicles leased in Texas are for personal use. The LBB has put the figure at about 250,000 vehicles.

People who lease vehicles for business purposes receive a federal income-tax deduction that personal-use lessees do not. Also, almost all auto owners pay no personal property tax. It is unfair to penalize consumers because of how they finance a basic need. This policy hurts people with cash-flow problems who need transportation and want to lease but who cannot afford the taxes. On the other hand, it is only fair to allow primarily personal-use vehicles to be used for some income-producing activities, given that business lessees often use their vehicles for personal purposes.

Authorizing this exemption would end inconsistencies in tax administration across appraisal districts. The tax is figured differently in different counties. Some calculate it on the basis of the vehicle's original price, some on its depreciated value. This can lead to hybrid lease arrangements. Some leasing companies include taxes in lease payments; some do not collect the tax, so it is not included. Consequently, tax liability may accumulate over multiple tax years. Those customers often are surprised to receive tax bills from assessor-collectors.

In fiscal 1999, according to the comptroller, the 6.25 percent motor-vehicle sales tax generated more than \$2.2 billion. If SB 248 were enacted, increased leasing activity would leader to greater sales-tax revenue from more auto leasing. More car rental programs would become available in Texas offering safer, cheaper cars. Also, turnover of rental vehicles is shorter than for owned or financed vehicles (38 to 42 months as opposed to 53 months, respectively, according to the National Vehicle Leasing Association). Estimates of additional revenue vary widely because the exact number of personal-use leases is unknown. Also uncertain is the number of balloon payments that would be made on outstanding retail installment contracts (a variation on leasing), resulting in ownership transfer. LBB estimates about \$15.5 million in additional revenue for fiscal 2002-03. In 1999, the industry projected a \$213 million biennial gain. Regardless, long-term gains would more than offset the relatively small amount of local government revenue lost to the exemption.

Excluding deceptive trade practice language from the statute would make Texas more attractive to the car-leasing industry. Mere failure to provide customers with declaration forms should not be considered a deceptive trade practice, for example. Even though the Deceptive Trade Practices Act would not be mentioned in this section of the Tax Code, consumers still could sue under that act if they believed they had a cause of action. Companies already have economic incentive to treat customers well and might be inhibited from doing business in Texas if they faced more grounds for lawsuits.

Requiring inventory reporting is important to prevent fraud by companies that might falsely claim exemptions they did not give. Under this bill, they would have to report them to receive them.

The bill also would allow cities in counties such as Dallas that tax all vehicles as property to continue to do so. This local option override would be consistent with other ad valorem exemptions for personal property. Also, the bill would sunset on September 1, 2003, to allow the 78th Legislature to examine whether it should be continued.

OPPONENTS
SAY:

In granting the exemption proposed by SB 248, the state would create a special class of personal property exempt from taxes for the benefit of the car-leasing industry. Such decisions are better left to local taxing entities. In Dallas County, for example, all vehicles are taxed as personal property.

Consumers already can avoid these taxes by means of retail installment contracts developed for the Texas market. They feature a tax-exempt option to buy through a balloon payment. These contracts also remove some of the stigma of leasing by furnishing lessees copies of vehicle titles. These agreements are easier on appraisal districts, relieve taxes, and reduce fraud. Most Texans prefer to own their cars, so this exemption alone would not increase leasing significantly. But if fairness is the problem, state and local officials should take steps to raise public awareness of how the tax works.

Under the school finance system, the state would have to reimburse school districts for lost revenue, beginning with \$20.5 million in fiscal 2004, then almost \$17 million in fiscal 2005, even if the exemption expired. Cities and counties, however, would not be reimbursed for their losses, totaling almost \$31 million in fiscal 2003 and 2004, according to LBB. SB 248 should be postponed until the Legislature finds more money for public schools.

The bill would not curb fraud because it would contain no mechanism other than customers' declarations to verify personal use and no enforcement mechanism other than reports to the comptroller. Lessees at least should have to demonstrate to appraisers that they did not claim full business deductions for the vehicles on their federal income-tax returns. Under SB 248, they might be able to "double-dip" by deducting up to 49 percent of a vehicle's use for business purposes in addition to receiving a property-tax exemption.

OTHER
OPPONENTS
SAY:

SB 248 includes too few safeguards for consumers and businesses. It would not protect either party from tax liabilities incurred because of actions or omissions by the other party. The bill would not declare as a deceptive trade practice a company's failure to provide customers with forms declaring vehicles primarily for personal use. Such a provision would give customers a specific legal remedy.

Leasing companies should be entitled to refunds of excess taxes paid on vehicles that became exempt after approval of appraisal rolls. They also should be allowed to recover from customers any taxes paid on vehicles that lose their exemptions.

The bill is not specific enough about companies' reporting requirements to appraisers. Also, it would not specify whether an exemption could be prorated for the portion of a tax year during which a vehicle was leased.

Counties and school districts, not only cities, should have the option of overriding the exemption.

NOTES:

The House committee amendment to the Senate engrossed version would specify that a vehicle's non-income-producing use be established on the basis of annual miles driven and add the requirement for lessors to complete and file property report forms on their leased vehicles.

A similar bill, HB 1694 by Hamric, passed the House on May 8 by a nonrecord vote. It was considered in a public hearing by the Senate Finance Committee on May 11 and left pending. HB 1694 would authorize a property-tax exemption only for vehicles leased exclusively for personal use. It included no sunset provision or opt-out provision for cities. HB 1694 also includes different reporting, lessee declaration, and paperwork retention requirements, as well as indemnification clauses for tax liability caused by another party's acts or omissions.