



Special Council on Tax Reform and Fairness for Georgians

Objectives, Guiding Principles, Update
To N. Perimeter Chapter

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<http://fiscalresearch.gsu.edu/taxcouncil/index.htm>

www.gscpa.org

GA Tax System – Time Capsule

1931	Corporate Net Worth tax imposed, rate unchanged
1937	Income tax established with existing rates
1951	Sales tax established
1971	Motor fuel tax established
1981	Standard deduction unchanged
1931 to now	Cobbled additions, tax breaks
2010	Special Tax Council to study and recommend reform



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Reform and Fairness for Georgians

HB 1405

- Signed by Governor on June 1, 2010.
- Adds O.C.G.A. §§ 28-12-1, 2, 3, and 4.
- Creates 11-member “Special Council on Tax Reform and Fairness for Georgians” to study state’s revenue structure and recommend tax reform to new 12-member Joint Committee.
- Changes legislative procedure for recommendations of Council.



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HB 1405 Objectives

" You are being asked to do something no one to my knowledge has been able to do before.."

"...examine all 19 platforms and suggest reformation to our tax code...to make it more stable, balanced... fair, transparent, understandable, easy and inexpensive to comply.."

- Larry O'Neal
Chairman, House Ways and Means



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Revenue Sources

- Alcohol
- Tobacco
- Motor Fuel
- Corporate Income
- Insurance Premium
- Franchise Tax
- Personal Income
- Sales Tax



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HB 1405

Council Members

Special Council members include: Gov. Purdue, 4 leading GA university economists, chair of GA Chamber of Commerce, GA chair of National Federation of Independent Businesses, 2 appointees by the Lt. Gov., 2 appointees by Speaker of House.



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Joint Committee Members

Joint Committee members include: President Pro Tempore of Senate, Speaker Pro Tempore of House, Chairpersons of Way and Means and Senate Finance committees, Majority and Minority leaders of Senate and House, 2 appointees by House Speaker, and 2 appointees by Senate President



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HB 1405

- Special Council to issue report to Joint Committee on or before January 10, 2011.
- Joint Committee to introduce legislation incorporating recommendations of Special Council without significant change.
- House and Senate floor to vote legislation in up or down vote without amendment.
- Gov veto power in place.



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Guiding Principles



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Special Council's Guiding Principles Towards Responsible Tax Reform

- Growth Enhancing
- Efficient
- Stable
- Clear
- Fair and Equitable
- Properly Developed

Guiding principles are not mutually exclusive, but will require proper balancing.



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Guiding Principles Growth Enhancing

- Fosters economic growth, job creation, and rising standard of living.
- Encourages investment in human, physical and technological capital.
- Enhances GA's competitive position in business development and retention.



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Guiding Principles Efficient

- Reduces distortions in economic decision-making for households and businesses.
- Minimizes tax impact in allocation of capital and labor.
- Implies low marginal rates (*implies avoiding pyramiding*).
- However, may be used to discourage behaviors imposing cost on others.



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Guiding Principles Stable

- Stable to general economic activity, less volatile, and negatively buoyant.
- *Adequate to meet structural needs of state's services and obligations.*
- Implies infrequent changes in tax rates and severe changes to the delivery of services.
- *Would still expect falling revenues during great recession.*



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Guiding Principles

Clear

- Simple, understandable, and predictable.
- Increases voluntary compliance and lowers administrative costs, *including matters of controversy*.
- Does not disrupt tax planning and competitive effects of past actions.



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Guiding Principles

Fair and Equitable – Horizontal and Vertical

- Horizontal equity - taxes equals equally (or those in similar circumstances similarly).
- Vertical equity – varies the tax burden based on ability to pay.
- *Examples:*
 - *horizontal equity – avoids preferential treatment by groups.*
 - *vertical equity – avoids a pure per capital tax.*



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Guiding Principles Properly Developed

- Special Council will conduct its business openly.
- Will develop its recommendations based on analysis of issues and options.
- *Set agenda for lasting reform and possible further study.*



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Guiding Principles Concurrence

- Minimizes distortions in economic decision-making.
- Broad tax base and low rates.
- Few exemptions and special provisions.
- Promotes equity through transfers, subsidies, and credits rather than with progressive tax rates.
- Taxes consumption rather than income in order to encourage savings and investment.
- Keeps tax rates low so as to increase level of activity that is being taxed.



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Case Study: Michigan White Paper 2005 Legislation to tax services



STATE of GEORGIA



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Deliberations on Sales Tax on Services *

Positive Factors Relative to a Sales Tax on Services

Revenue Growth

- Significantly broadens tax base.
- Aligns tax system with service oriented economy.
- Modernizes tax system with consumer spending trends.

* Michigan Society of CPAs, Inc., Technical Observations on Legislation, June 2005



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Deliberations on Sales Tax on Services *

Positive Factors Relative to a Sales Tax on Services

Revenue Stability and Collections

- Consumption tax is less buoyant to profits and economic volatility.
- Accelerates collections with monthly reporting.

* Michigan Society of CPAs, Inc., Technical Observations on Legislation, June 2005



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Deliberations on Sales Tax on Services *

Positive Factors Relative to a Sales Tax on Services

Fairness

- Tax is transparent
- Services tax base is progressive with respect to discretionary or luxury spending.
- Taxing discretionary or luxury services follows ability to pay.

* Michigan Society of CPAs, Inc., Technical Observations on Legislation, June 2005



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Deliberations on Sales Tax on Services *

Positive Factors Relative to a Sales Tax on Services

Efficiency in Economic Process

- Reduces distortions in economic decision-making.
- Assumes there is substitution of choice (goods vs. service).
- Neutralizes economic inequalities:
 - DVD vs. tickets to a movie
 - Gym equipment vs. gym membership
 - Bug spay vs. pest control service
 - CD vs. iTunes download



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Deliberations on Sales Tax on Services *

Positive Factors Relative to a Sales Tax on Services

Administrative Ease

- Reduces (but does not eliminate) planning and manipulation.
- Lowers compliance costs relative to income tax, especially with few exemptions and single rate of tax.

Addresses Taxability of Technology

- Broadens tax base to capture digital delivery of software.
- Most effective where single rate of tax.



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Deliberations on Sales Tax on Services *

Negative Factors Relative to a Sales Tax on Services

Potential for Pyramiding

- Absent B-to-B exemption, purchased services taxed twice.
- Penalizes businesses that outsource services.
- Drafting business input exemption will take care.



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Deliberations on Sales Tax on Services *

Negative Factors Relative to a Sales Tax on Services

Incidence of Benefit

- Tax imposed on consumption within state (parallel use tax).
- Discourages location of businesses to state.
- Encourages consumers to procure service out of state (especially in border locations).
- Other manipulations (billing).



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Deliberations on Sales Tax on Services *

Negative Factors Relative to a Sales Tax on Services

Not Deductible for Federal Purposes

- Limited deductibility results in higher cost for individuals who could otherwise deduct income or property tax.

Administrative Burden

- New ground for many service providers and service consumers.
- Issues of structure, sourcing, consumption, registration, and exemption.
- General lack of precedent in other states for taxing services.



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Deliberations on Sales Tax on Services *

Characteristics of an Effective Sales Tax on Services

Structure:

Inclusive – applies to every service sourced to state unless specifically exempt.

- Creates presumption of tax with narrowly interpreted exemptions.
- Captures services not contemplated.
- May foster efforts to expand exemptions.



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Deliberations on Sales Tax on Services *

Characteristics of an Effective Sales Tax on Services

Structure:

Exclusive – imposes tax only on specifically enumerated service.

- Avoids controversy of presumption and services not contemplated.
- Limits need for exemptions.
- Most prevailing but may violate fairness and equity.



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Deliberations on Sales Tax on Services *

Characteristics of an Effective Sales Tax on Services

Sourcing

- Benefit sourcing (vs. performance) carefully defined.
- Price and place of benefit subject to manipulation.
- Must address multiple benefit locations.

Single Rate

- Single state rate critical for compliance and ease.
- Single rate required for membership in the Streamline Sales Tax Agreement (SSTA).



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Deliberations on Sales Tax on Services *

Characteristics of an Effective Sales Tax on Services

Limited Exemptions

- Overarching structure:
 - Exemptions on type of consumer vs. type of service/transaction.
 - Limit inequity and noncompetitive results.
 - Interpretation and enforcement of exemption process.
 - SSTA compliance.
 - Broadening base results in more permanent reform.



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Deliberations on Sales Tax on Services *

Characteristics of an Effective Sales Tax on Services

Input Exemption

- Addresses input exemption for purchased services
- Alternative B-to-B approach:
 - Purchased services consumed in rendering taxable service.
 - Consumed service necessary and integral to production of product or services to which business organized.
 - Blanket B to B.
 - VAT like
 - 199 like - Qualified production activity.



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Deliberations on Sales Tax on Services *

Characteristics of an Effective Sales Tax on Services

What did we learn from Michigan?



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The state of our State



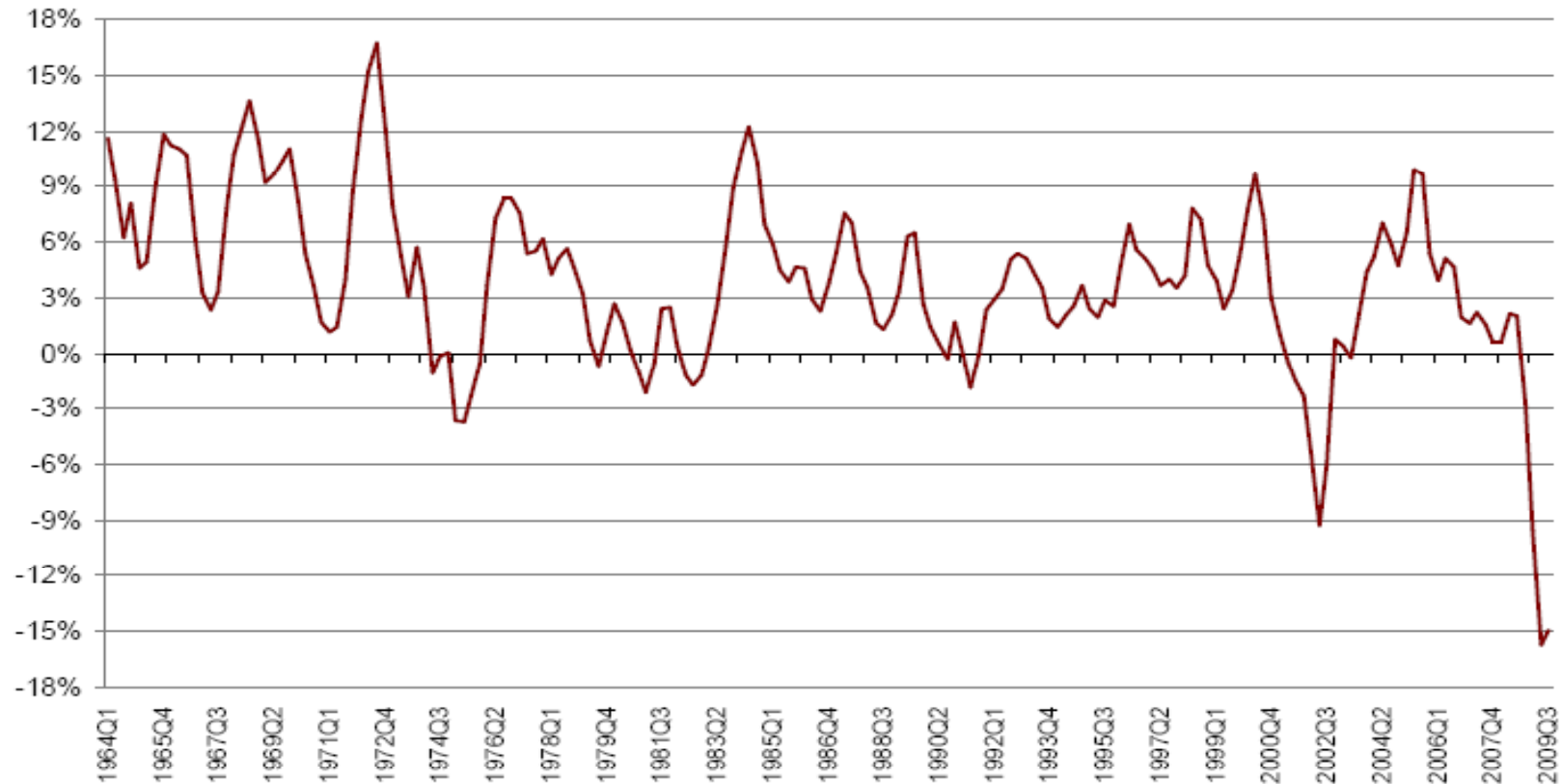
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Historic Revenue Declines Nationwide

Annual Change in Real State Taxes, 1964-2009



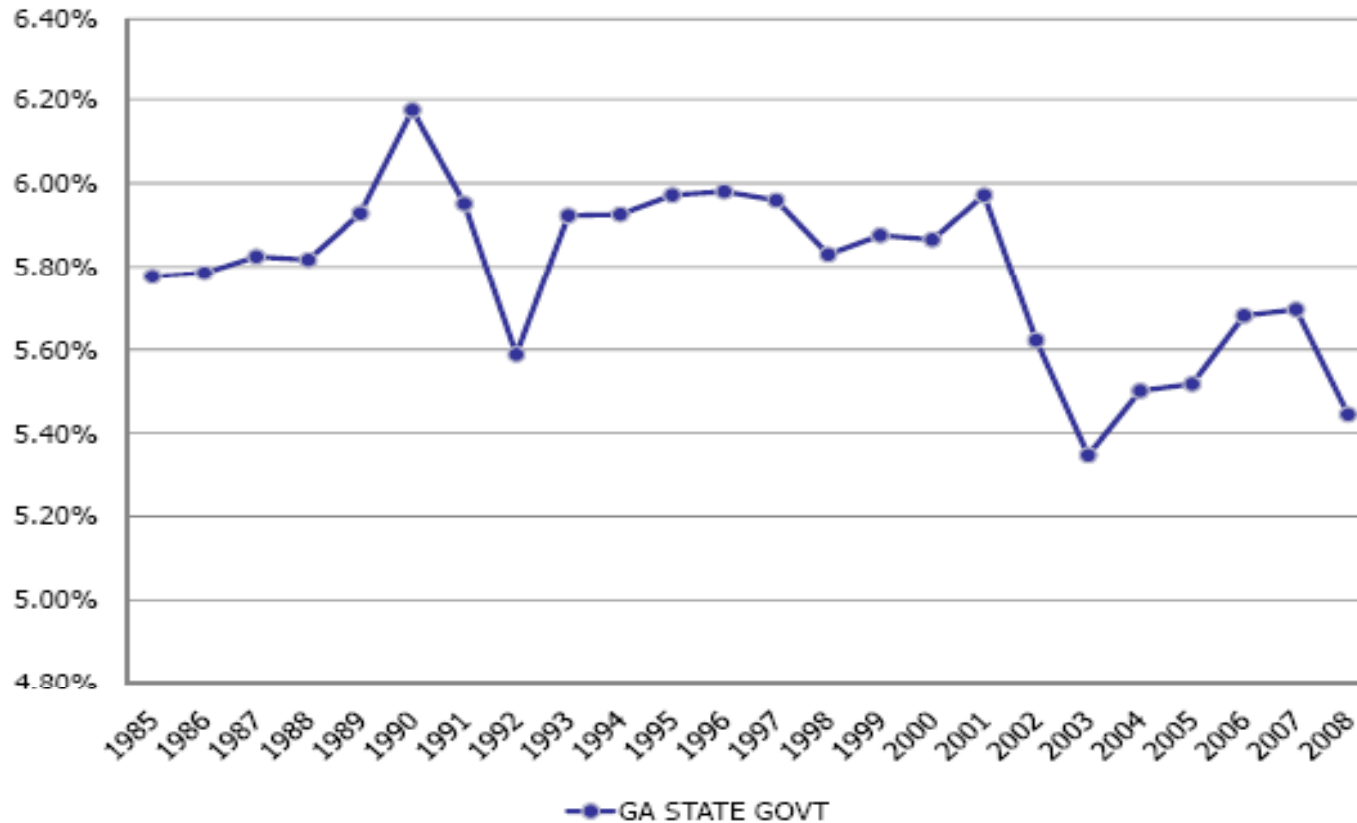
Sources: U. S. Census Bureau (Quarterly tax collections); Bureau of Economic Analysis (real GDP).
Notes: (1) Percentage changes averaged over 2 quarters; (2) No legislative adjustments; (3) Recession periods are shaded.



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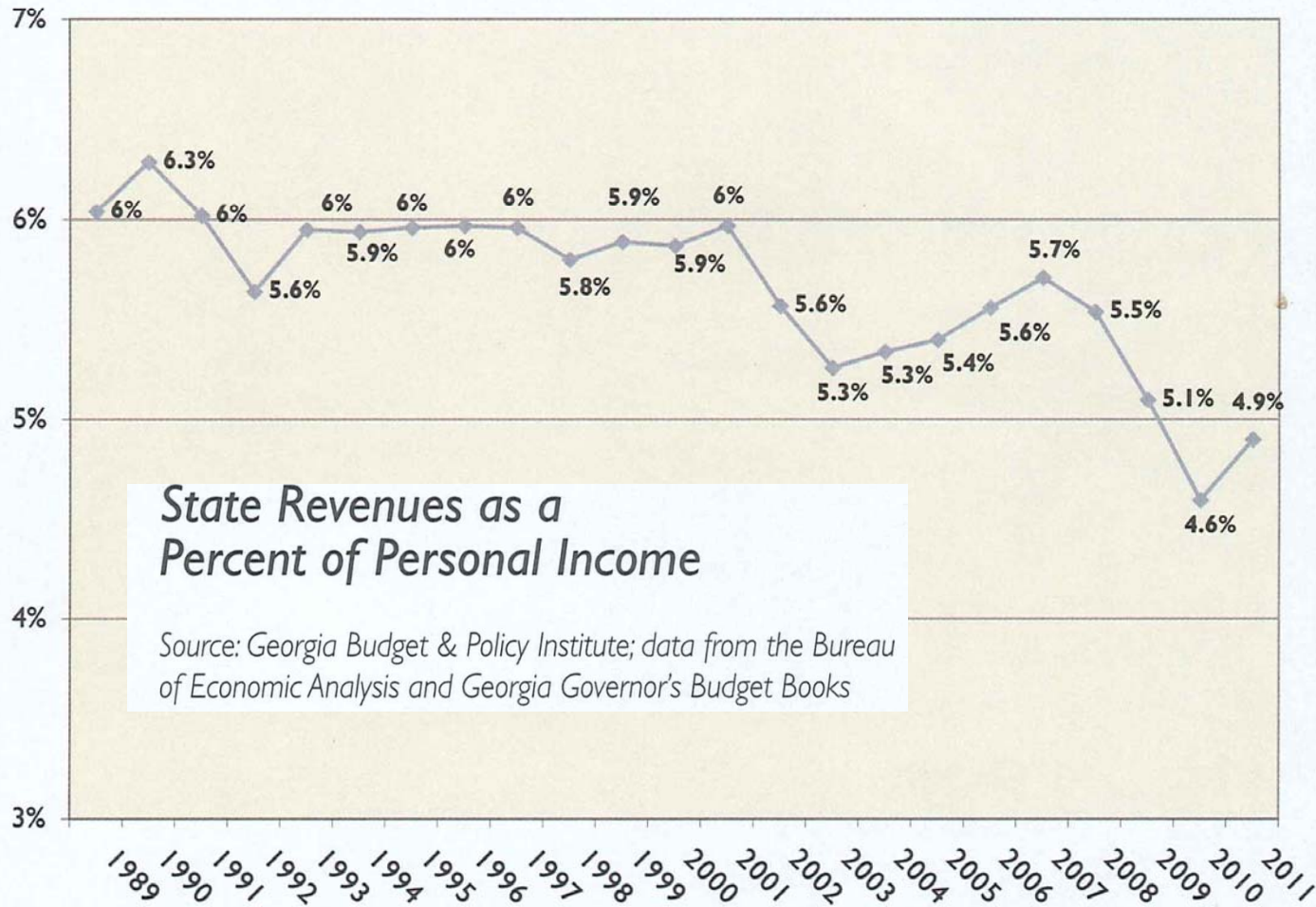
The State of our State

**Georgia State Tax Revenues as a % of Personal Income
(1985-2008)**



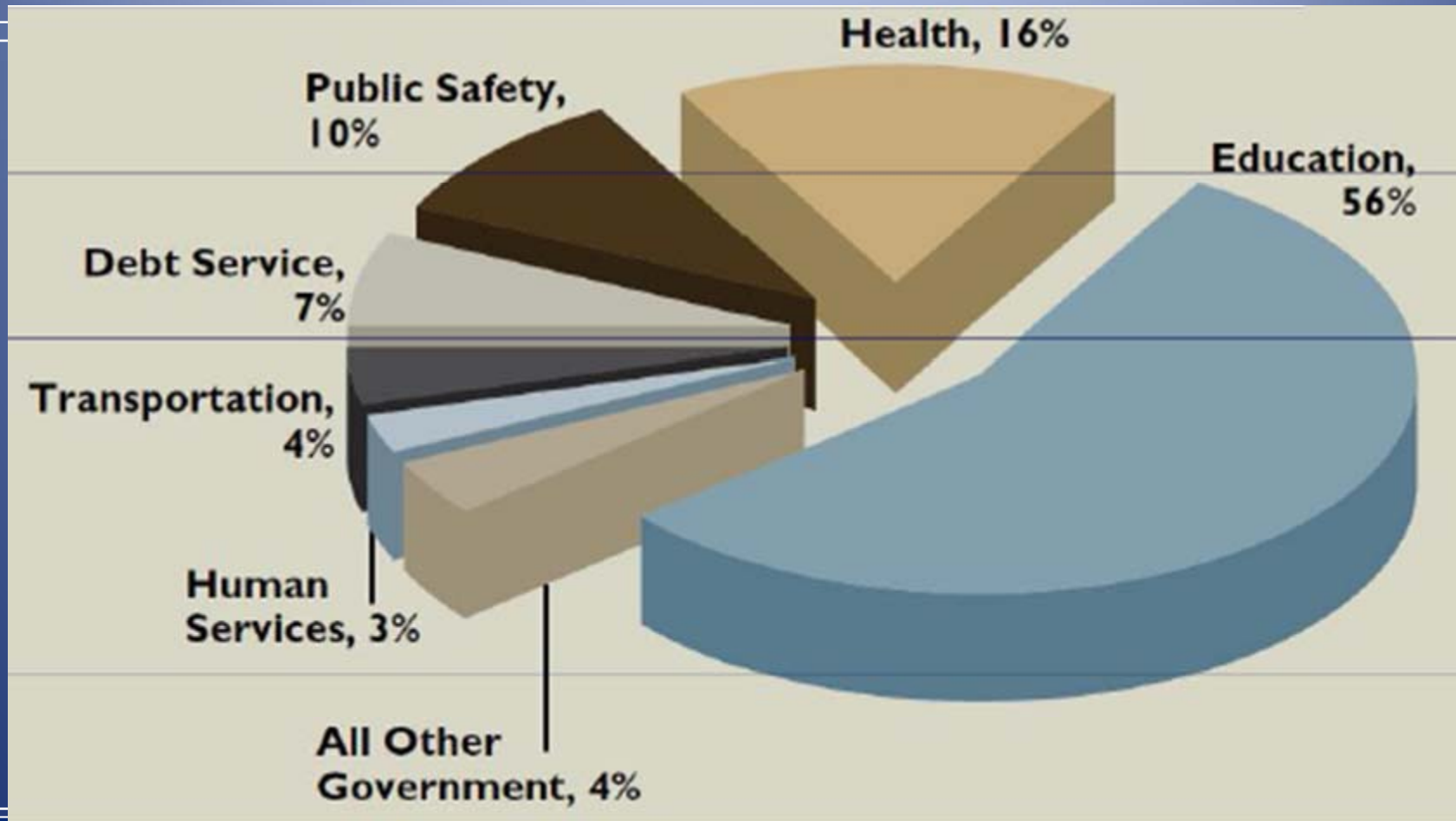
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The state of our State



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Where does it go?

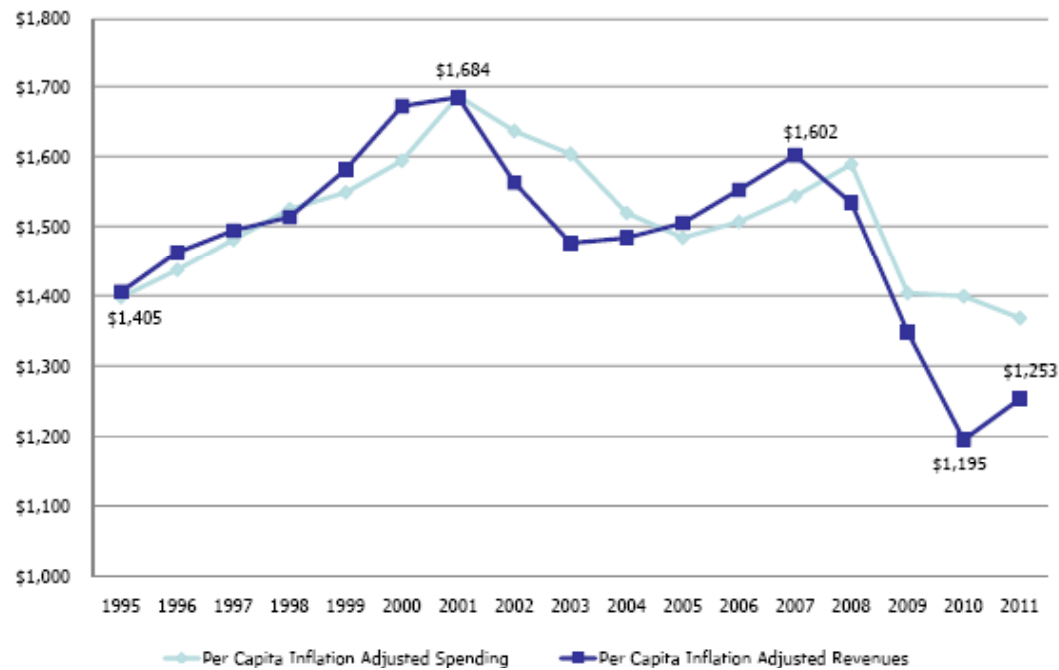


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The state of our State

Georgia's Per Capita Inflation Adjusted Appropriations and Revenues 1995-2011

(1995 Constant \$)



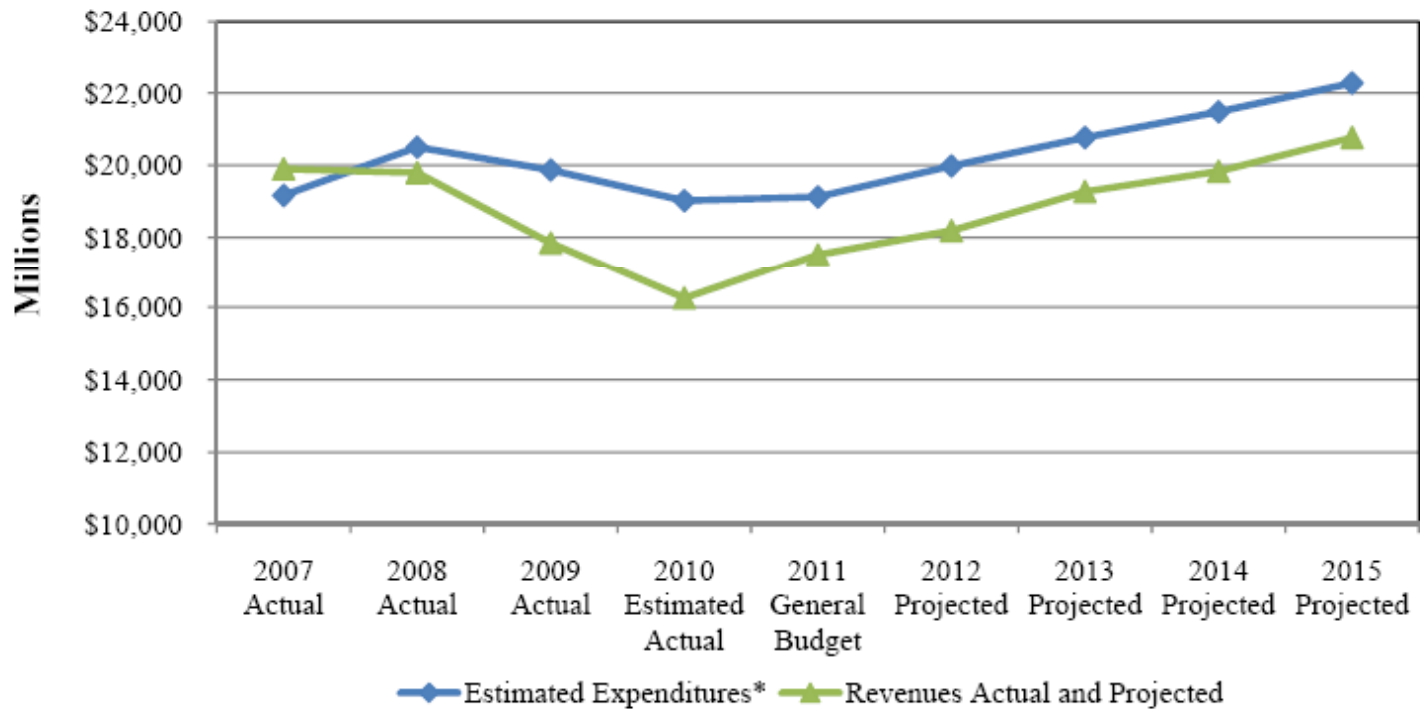
Data Sources: GA Department of Audits, Selected Summary of Financial Information; chart uses the Bureau of Economic Analysis GDP deflator to adjust for inflation



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FIGURE 1. EXPENDITURE AND REVENUE TRENDS FOR ALL STATE FUNDS (GDP INFLATIONARY INDEX)



*Projections use the FY 2011 general budget as the base year.



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Structural Deficit

State's revenue structure (taxes, fees, charges and other ongoing revenues) are insufficient to support ongoing operating expenditures.

General Assembly (O.C.C.A. §45-12-76)

- Required to adopt a balanced budget Must not appropriate funds exceeding:
 - Estimated CY estimated net treasury receipts + PY surplus



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Structural Deficit

Governor

- Sole authority to set the estimated treasury receipts for CY
- Required to implement balanced budget by YE by means of using:
 - reserves,
 - other one-time sources, or
 - withholding CY expenditures.
- Recent deficit have been funded by federal stimulus revenues, deferred benefits, and short-term federal Medicaid assistance programs.



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“Dealing with half a deck”

How State and Local Govts are Financed in Georgia (\$ millions)

	State and Local		State		Local	
	Total	%	Total	%	Total	%
Tax Revenues						
Property Tax	\$10,220	20%	\$82	0%	\$10,138	39%
Sales Tax	\$9,771	20%	\$5,797	25%	\$3,974	15%
Income Tax	\$8,845	18%	\$8,845	38%	\$0	0%
Corporate Income	\$943	2%	\$943	4%	\$0	0%
Selective Sales						
Motor Fuel	\$1,011	2%	\$1,011	4%	\$0	0%
Alcoholic Beverage	\$293	1%	\$166	1%	\$128	0%
Tobacco	\$233	0%	\$233	1%	\$0	0%
Public Utilities	\$280	1%	\$0	0%	\$280	1%
Other	\$1,063	2%	\$482	2%	\$581	2%
MV License	\$297	1%	\$297	1%	\$0	0%
Other Taxes	\$676	1%	\$214	1%	\$462	2%
Total Taxes	\$33,633	67%	\$18,070	77%	\$15,562	59%
Other Revenues						
User Fees/Charges	\$11,235	23%	\$3,263	14%	\$7,971	30%
Misc Revenue	\$4,986	10%	\$2,248	10%	\$2,738	10%
Total Own Source	\$49,853	100%	\$23,581	100%	\$26,272	100%

Data Source: US Census of Governments, 2008



Where do we stand?

State Versus Local Tax Revenues Per Capita (2007)

All Taxes - State Only		
Rank	State	\$ per capita
1	Alaska	\$5,415
2	Vermont	\$4,130
3	Hawaii	\$3,985
<i>Top Quintile Cutoff</i>		<i>\$3,200</i>
<i>50-State Mean</i>		<i>\$2,604</i>
<i>AAA Mean</i>		<i>\$2,482</i>
22	North Carolina	\$2,501
<i>Nat'l Median</i>		<i>\$2,447</i>
27	Virginia	\$2,425
38	Mississippi	\$2,189
40	Florida	\$2,133
<i>SE Mean</i>		<i>\$2,114</i>
<i>Last Quintile Cutoff</i>		<i>\$2,073</i>
42	South Carolina	\$1,973
43	Georgia	\$1,923
44	Alabama	\$1,917
46	Tennessee	\$1,852
48	Texas	\$1,691
49	New Hampshire	\$1,657
50	South Dakota	\$1,591

All Taxes - Local Only		
Rank	State	\$ per capita
1	New York	\$3,647
2	New Jersey	\$2,536
3	Connecticut	\$2,362
<i>Top Quintile Cutoff</i>		<i>\$1,946</i>
10	Florida	\$1,876
12	Virginia	\$1,781
22	Georgia	\$1,558
<i>Nat'l Median</i>		<i>\$1,504</i>
<i>50-State Mean</i>		<i>\$1,493</i>
<i>AAA Mean</i>		<i>\$1,367</i>
<i>SE Mean</i>		<i>\$1,301</i>
33	South Carolina	\$1,161
35	Tennessee	\$1,153
39	North Carolina	\$1,085
<i>Last Quintile Cutoff</i>		<i>\$993</i>
42	Alabama	\$992
48	Mississippi	\$800
49	Arkansas	\$630
50	Vermont	\$584



Data Source: US Census of Governments, 2007

Where do we stand?

Business Climate Measures

Tax Foundation (High Ranking Number is Less "Business Friendly")						
	Overall Rank	Corporate Income Tax Rank	Individual Income Tax Rank	Sales Tax Rank	Unemployment Insurance Index Rank	Property Tax Index Rank
Florida	5	15	1	32	3	22
Virginia	15	4	20	8	44	29
Alabama	19	23	17	25	16	17
Mississippi	21	13	18	35	4	23
Tennessee	22	11	8	49	32	46
South Carolina	26	9	28	18	43	26
Georgia	29	8	30	23	22	36
North Carolina	39	25	36	34	5	37



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Where do we stand?

Tax Structure: How and What You Tax

Georgia compares poorly with neighboring states, with lower rankings in business tax climate and taxation of items that few other states tax

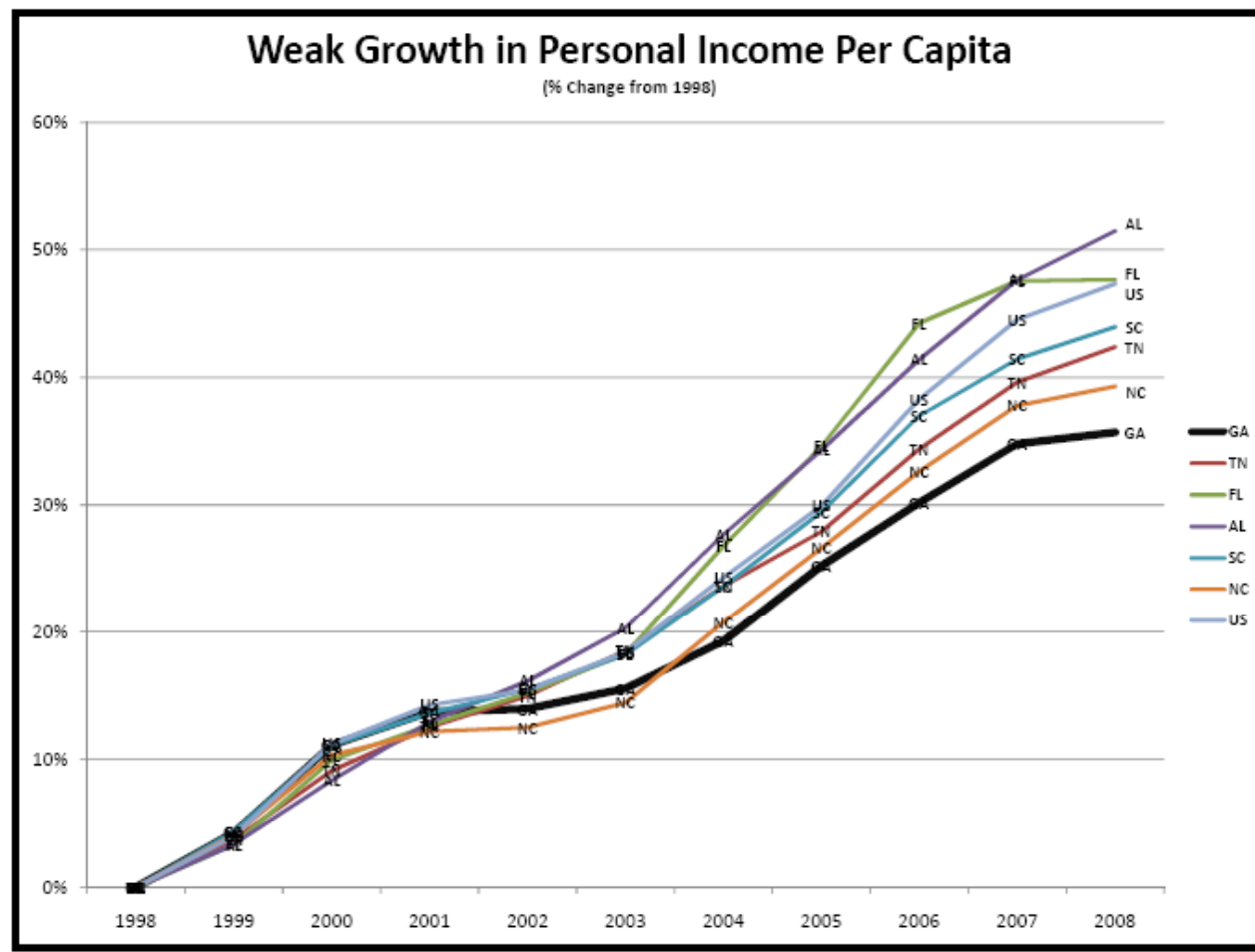
	<u>AL</u>	<u>FL</u>	<u>GA</u>	<u>NC</u>	<u>SC</u>	<u>TN</u>
2010 State Business Tax Climate Index	19	5	29	39	26	22
2010 Small Business Tax Index	7	6	21	37	12	13
Inventory Tax	Yes	No	Yes	No	No	No
Sales Tax on Energy Used in Manufacturing	Exempt	Exempt	Taxed at full rate	Taxed at reduced rate	Exempt	Exempt

Only 15 states levy an inventory tax and only 14 states fully tax energy used in manufacturing.



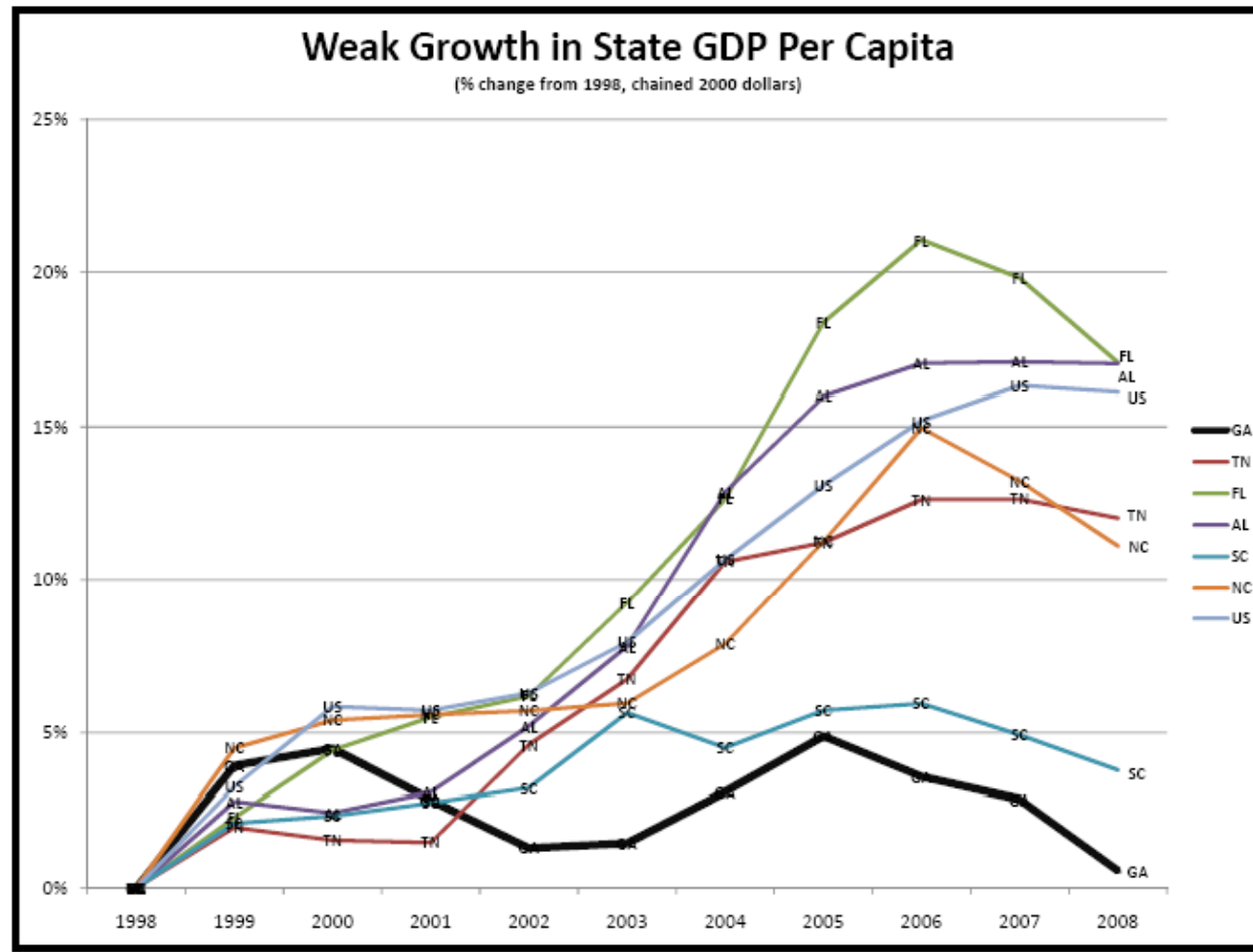
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The state of our State



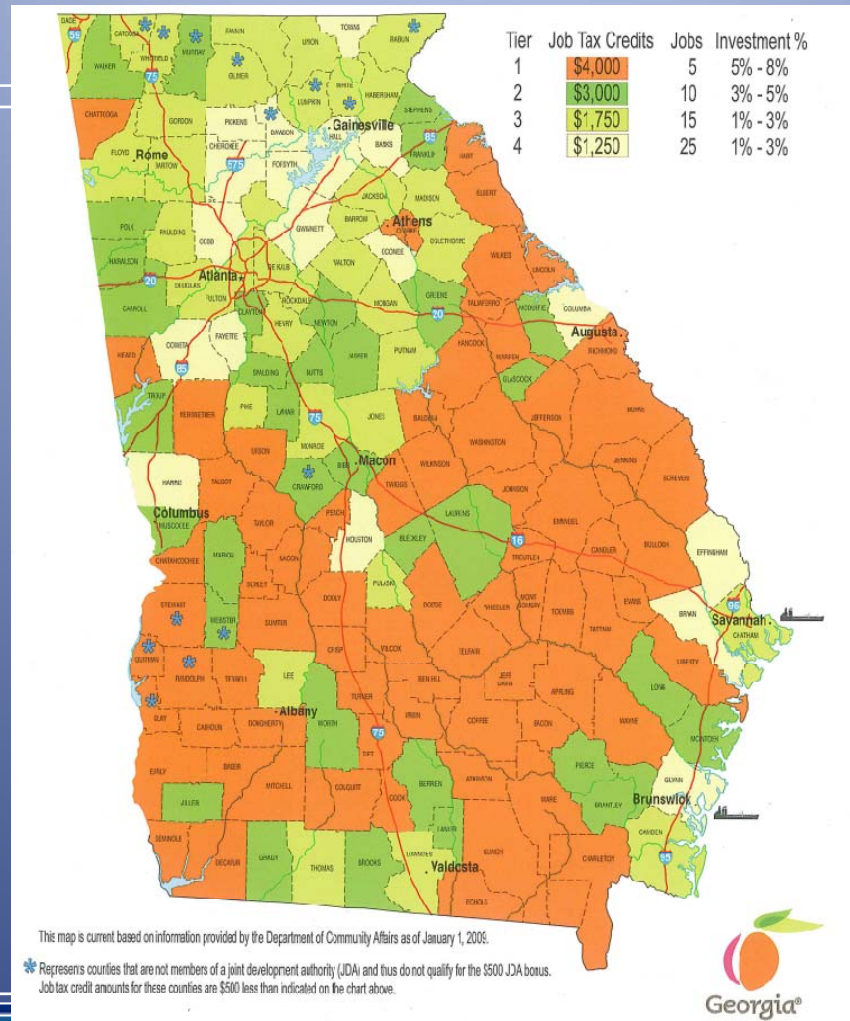
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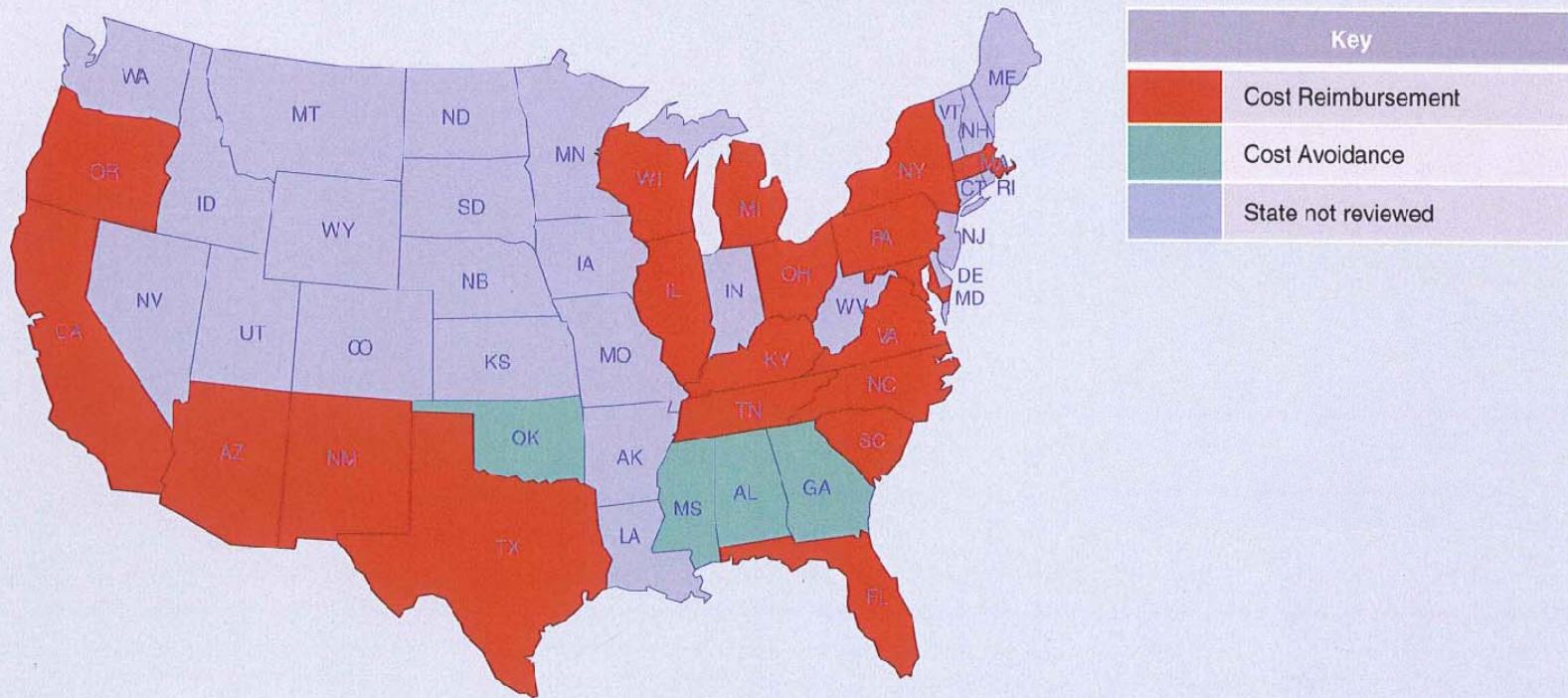
The state of our State – jobs credits



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State Training Assistance

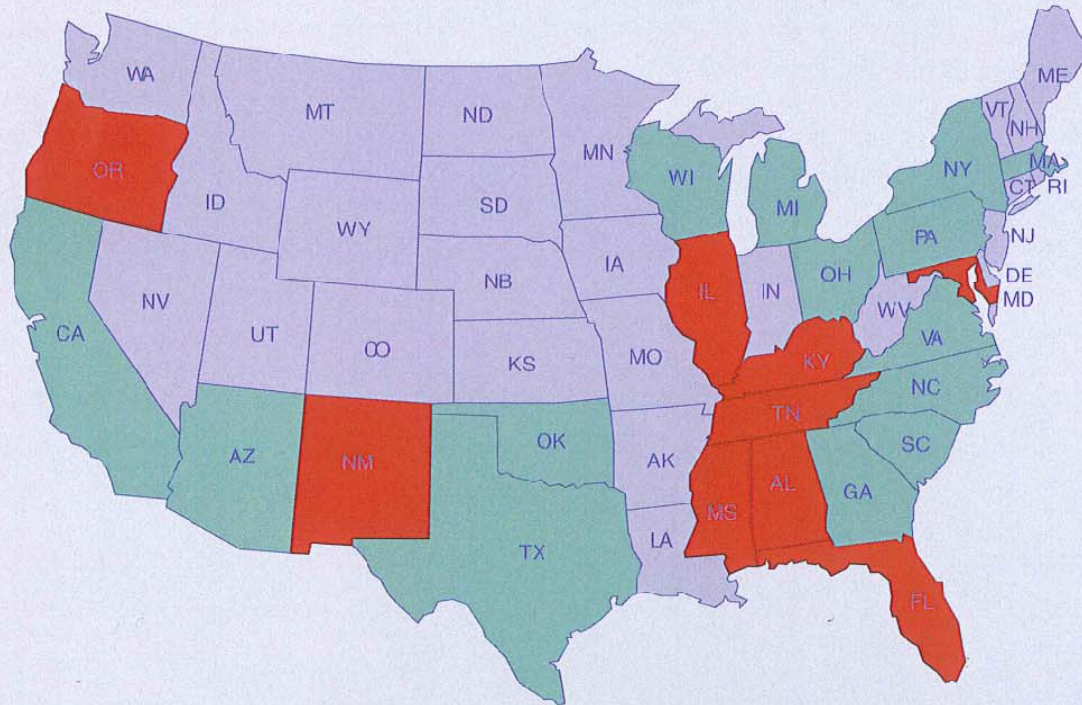
This map depicts states training programs offering cost avoidance* assistance and/or reimbursement employee training.



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State Sales Tax Exemptions – Construction Materials

The map depicts states that have an exemption for construction materials used in a qualifying new project.



Key	
	Exemption
	No Exemption
	State not reviewed

Sales tax exemptions on construction materials are generally not state-wide and are based on specific location or incentive program.

Notes:

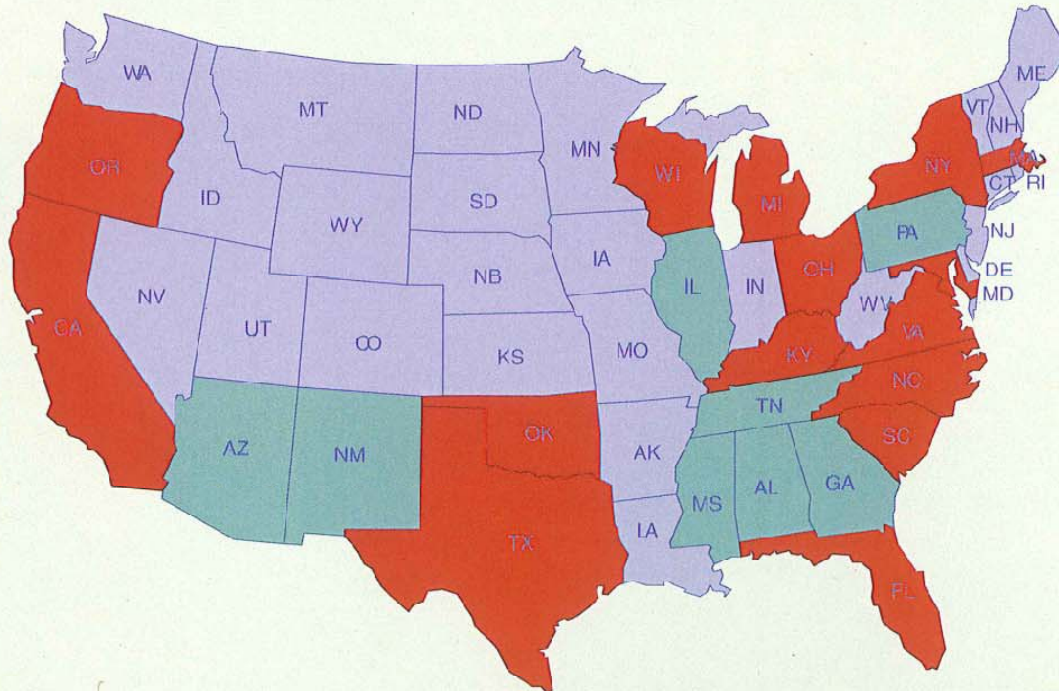
- AL - R&D facilities and projects in enterprise zones
- FL - Enterprise zone
- IL - Enterprise zones and wind energy projects
- MD - One Maryland Tax Credit
- MS - 50 - 100% of manufacturing projects and GAP areas
- NM - Construction Project Credit
- TN - HQ Facility Tax Credit
- OR - No Sales Tax



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Sales Tax Exemptions – Electricity Purchased by Manufacturers

The map depicts states that offer an exemption for electricity purchased for use in a manufacturing facility.



Key	
Red	Exemption
Green	No Exemption
Light Blue	State not reviewed

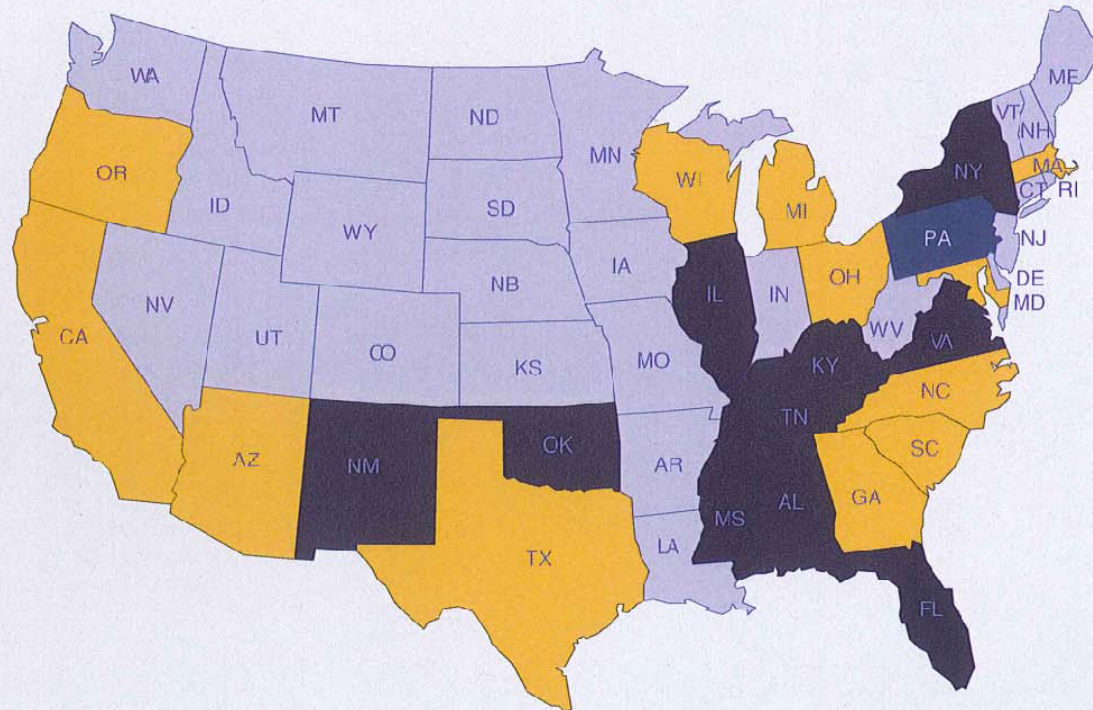
Georgia - Electricity used directly in manufacture of product is exempt if cost of electricity exceeds 50% of cost of all materials used in product, including electricity. From July 1, 2008, to December 31, 2010, partial exemption applies to certain fuels used in manufacturing or processing tangible personal property for resale.



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R&D Credits – Transferrable and Refundable

The map depicts states in which the R&D credit may be transferred (sold) to another party or refunded in excess of tax liability.



Key	
	Transferrable and refundable
	Not transferrable or refundable
	State not reviewed
	No Statewide R&D Credit

Georgia – Credits may be used against payroll withholdings for newly formed (less than 3-year old) companies.



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Sampling of Reform Ideas Received



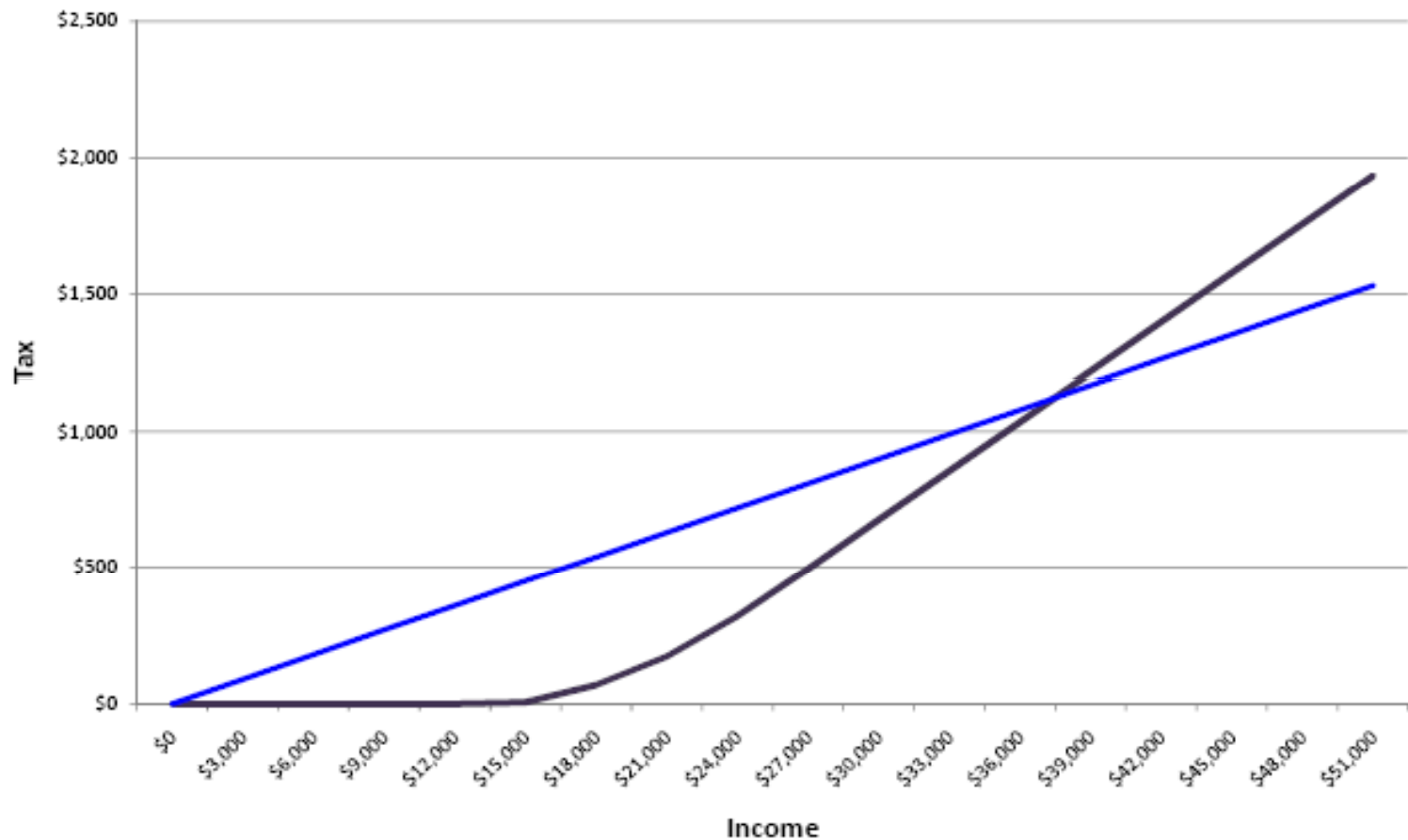
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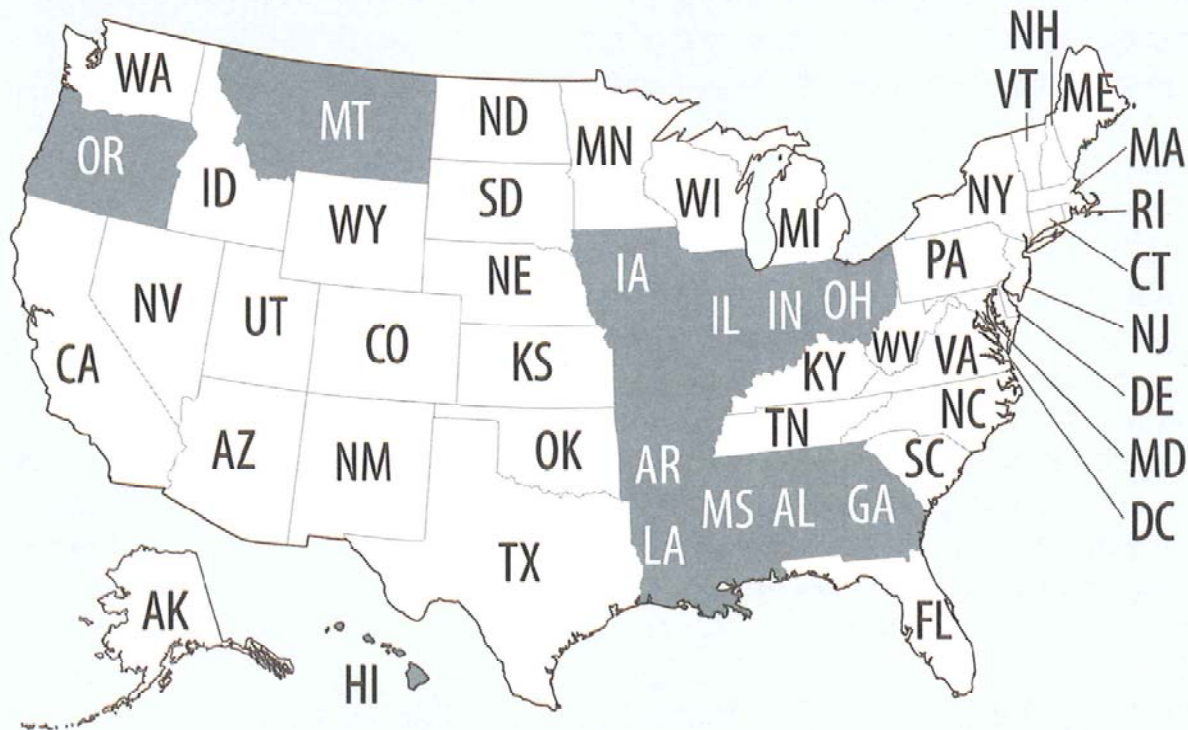
Sampling – Flatter Income Tax

**3% Flat Tax with No Exemptions vs. Current Income Tax
for a family of four**



Sampling – Address Poverty Levels

■ States imposing income tax on two parent families of four with incomes at or below the poverty line



Source: Center on Budget and Policy Priorities



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Sampling – Broaden Base, Compress Brackets

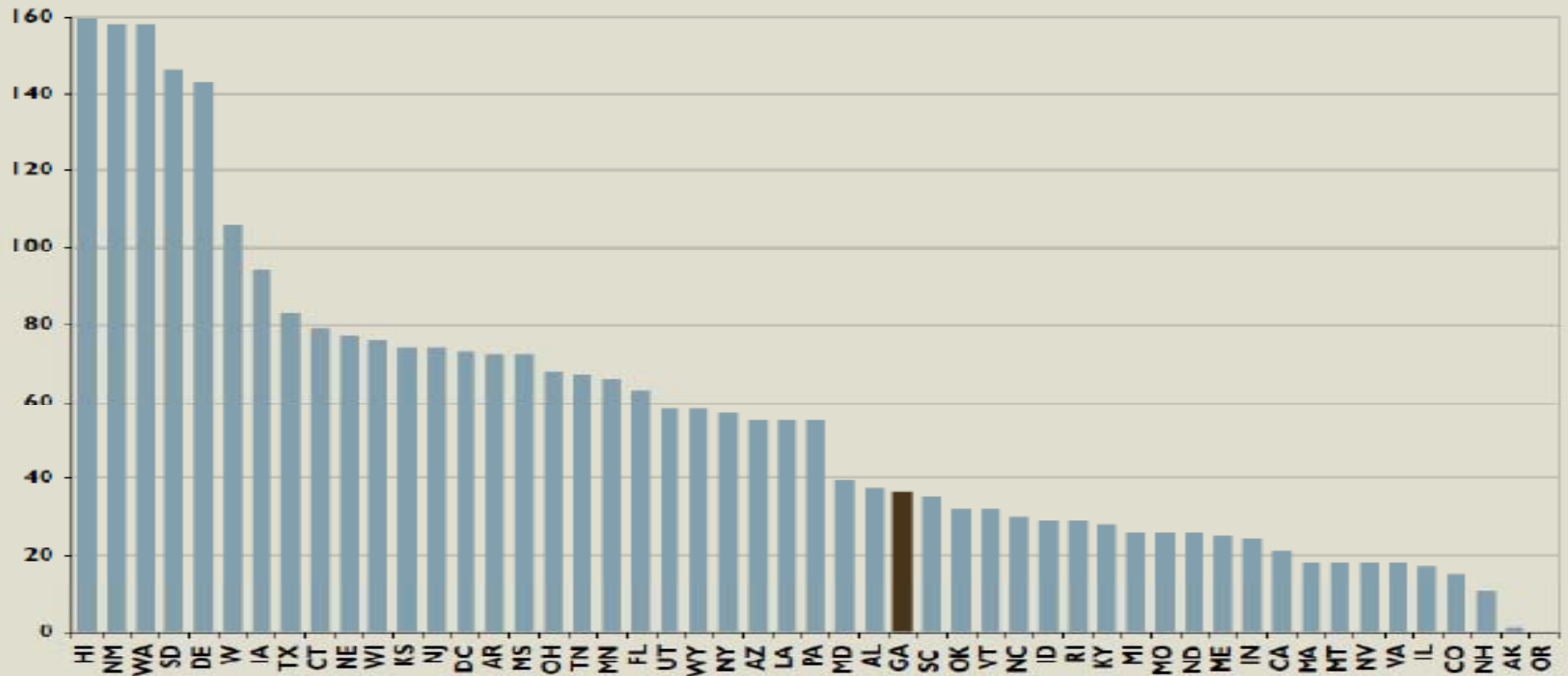
Rate	Single	Married Filing Jointly
1.0%	Less than \$800	Less than \$1,600
2.0%	\$800-\$4,000	\$1,600-\$8,000
4.0%	\$4,000-\$8,000	\$8,000-\$16,000
5.5%	\$8,000 and above	\$16,000 and above



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Sampling – Tax more services

The Number of Services Georgia Taxes is Below Average



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Sampling – which services?

SERVICES TAXED IN AT LEAST 15 STATES, BUT NOT IN GEORGIA

Labor charges on repairs to motor vehicles	Repair labor, general
Automotive washing and waxing	Labor on radio/TV repairs; other electronic equip.
Automotive road service and towing services	Labor charges – repairs, other tangible property
Auto service, except repairs, including painting & lube	Service contracts sold at the time of sale of tangible personal property
Parking lots and garages	Installation charges by persons selling property
Automotive rustproofing and undercoating	Installation charges – other than seller of goods
Software – Downloaded	Custom processing (on customer's property)
Books – Downloaded	Taxidermy
Music – Downloaded	Welding labor (fabrication & repair)
Movies/Digital Video – Downloaded	Janitorial services
Carpet and upholstery cleaning (in-home)	Pest control
Altering and repairing garments	Landscaping services (includes lawn care)
Health clubs, tanning parlors, reducing salons	Automotive storage
Shoe repair	Marina service/docking
Swimming pool cleaning and maintenance	Overnight RV park
Membership fees in private clubs	



Sampling – Model For Reform

Tax Reform Option	Estimated Revenue Impact (in millions)	Average Tax Change as a Percent of Income (by income group)						
		Lowest 20% Less than \$15,000	Second 20% \$15,000 to \$28,000	Third 20% \$28,000 to \$46,000	Fourth 20% \$46,000 to \$77,000	Next 15% \$77,000 to \$161,000	Next 4% \$161,000 to \$400,000	Top 1% \$400,000 or More
Reform Income Tax System <ul style="list-style-type: none"> • Modernize brackets and rates • Raise standard deduction and eliminate itemized deductions • Lower retirement exclusion • Enact refundable EITC 	\$85	-1.4%	-1.1%	-0.4%	0.0%	0.2%	0.4%	0.3%
Reform Sales Tax System <ul style="list-style-type: none"> • Reduce sales tax rate to 3.75% • Broaden the tax base to select personal services 	\$357	0.3%	0.2%	0.2%	0.1%	0.1%	0.1%	0.1%
Increase Cigarette Tax Rate by \$1, along with increases for other tobacco products	\$380	0.6%	0.4%	0.2%	0.2%	0.1%	0.0%	0.0%
Reform Corporate Taxes <ul style="list-style-type: none"> • Close corporate loopholes • Eliminate select tax breaks • Modernize corporate net worth tax^{HI} 	\$100	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Total Estimated Tax Change	\$922	- 0.53%	- 0.55%	0.02%	0.28%	0.40%	0.47%	0.35%

Source: Institute on Taxation and Economic Policy



Calendar Ahead

Full Council: Sept 29, Presentations Private/Public Sectors
Nov 3, Work Session
Dec 1, Work Session
Jan 10, Report Deadline

Fact Finding: Oct 6, Columbus
Oct 7, Albany
Oct 21, Blue Ridge
Oct 27, Dalton



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Questions?



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