Utah Foundation Research Brief

Personal Property Taxes: Taxes on Business Equipment

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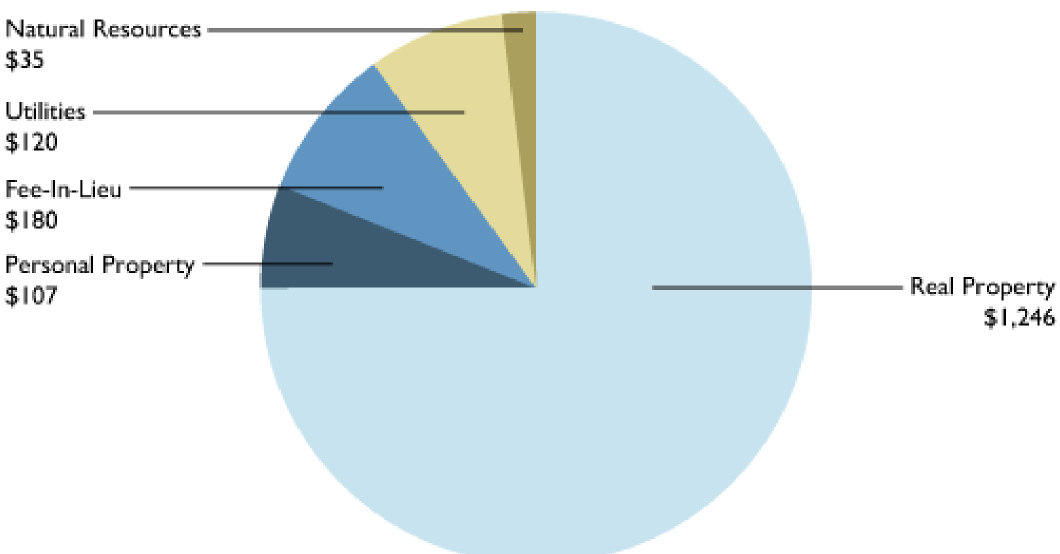
During the early part of this year's legislative session, there was a proposal to eliminate the personal property tax on businesses. While the bill was killed, the proposal has initiated dialogue on the efficacy and efficiency of the personal property tax on business equipment. This brief will explain the business personal property tax and some of the issues and trends surrounding the tax.

Introduction

The personal property tax is a component of the overall property tax structure in Utah. Personal property can generally be defined as any tangible property that is temporary or movable. According to the Salt Lake County Assessor, locally-assessed personal property is specific to business furniture and fixtures, business equipment, construction equipment, and manufactured homes. Other types of personal property, such as vehicles, boats, and trailers, are taxed by the state and are not included in this analysis. In 2003 personal property tax revenue (business personal property & mobile homes) contributed 6.3% of total property tax revenues. In contrast, real property is defined as any property that is permanently fixed, such as land and buildings. Real property taxes contribute 73.9% of the total property tax, making up the bulk of property tax revenue. Figure 1 shows the types of taxes charged for all Utah property in 2003.

Figure 1: Taxes Charged for all Utah Property (millions)



Source: Utah Tax Commission: Property Tax Division

The bulk of the Utah business property tax falls on machinery and equipment; however, there is an exemption for farming equipment. Also, while business' motor vehicles are also taxed, they are categorized separately into the fee-in-lieu tax classification because motor vehicles are assessed and administered differently than other personal property taxes on businesses. Figure 2 details the types of business personal property (other than motor vehicles) that are taxed.

Figure 2: Taxable Business Personal Property

Equipment	Useful Life
Software	3 years
Office Equipment	5 years
Computers	5 years
Trade Fixtures	10 years
Commercial/Industrial Machinery	12 years
Medical/Dental Equipment	12 years
Construction Equipment	15 years
Semiconductor Equipment	5 years
Oil & Gas Equipment	13 years
Longlife Equipment (Grain bins, tanks, etc.)	20 years
Aircraft Manufacturing Equipment	6 years
Computer Dependent Machinery (CNC machines, lathes, etc.)	8 years

Source: Utah Tax Commission: Property Tax Division

Concerns

Administration & Compliance

One of the chief concerns that opponents of the business personal property tax raise is that the tax is difficult for the government to administer and difficult for businesses to comply with. While the veracity of those claims is difficult to gauge, there is generally a consensus among administrators that the administration and compliance of business personal property taxes can be intensive. According to Gary Cornia and Gloria Wheeler in the book entitled, "Handbook on Taxation," administration of the personal property tax, like the real property tax requires active involvement by tax administrators[1]. Cornia and Wheeler state that there are seven steps in property tax administration: discovery, valuation, assessment of the tax, billing, collection, auditing, and an appeal process. These steps and the tasks for each step are outlined in Figure 3.

Figure 3: Steps in Property Tax Administration

Step	Tasks
Discovery	Identify legal owners Identify all taxable property Classify property in terms of use Develop reporting process
Valuation	Develop consistent process for determining appraised value Apply process to discovered property
Assessment	Assessed value multiplied by assessment rate to establish taxable value Assessed value listed to specific taxing jurisdictions Property owners informed of assessed true value
Bill & Collect Tax	Set tax rates Bill taxpayer Collect from taxpayer
Audit	Determine if all taxable property is identified Determine if correct value is being applied against property
Appeal	Inform process to "question" appraisal Formal process to "challenge" appraisal

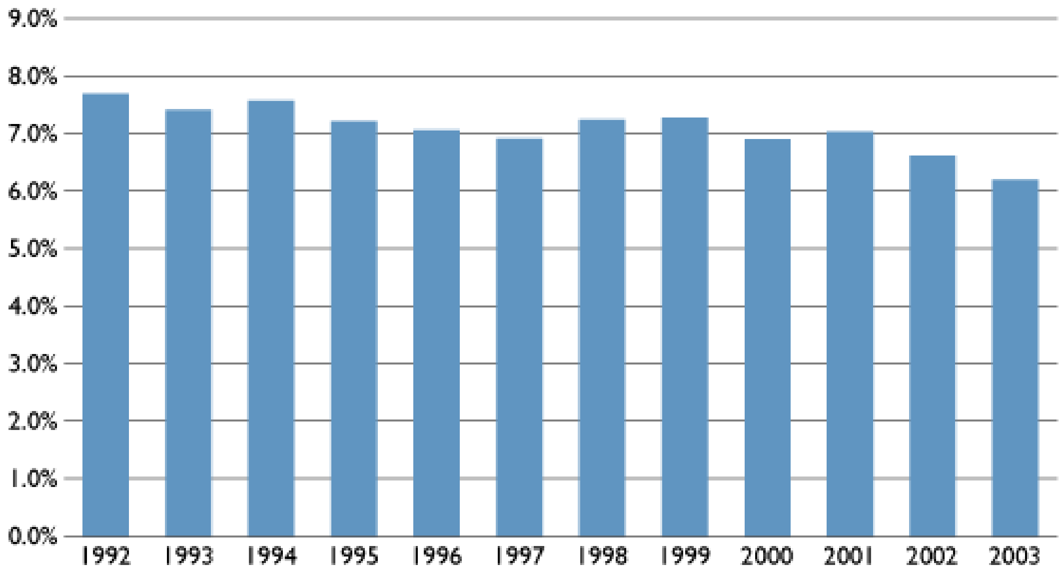
Source: Cornia, G.C. and Wheeler, G.E. (1999). The Personal Property Tax, *Handbook on Taxation* (W.B. Hildreth and J.A. Richardson, ed.)

Unlike real property taxes, personal property taxes also require an active role from the taxpayer. A business is required to inform the local county assessor that it has either began business or relocated to the county. The business must then fill out and a return a self-assessing form detailing all the personal property that it has, including information on the year of acquisition and cost of the equipment or machinery. The county assessor then calculates the tax based on valuation schedules developed by the Utah State Tax Commission. In subsequent years, businesses need only to report and assess newly acquired equipment and report sales of previously assessed property. Businesses have 30 days from the date the personal property tax notice is mailed to appeal assessments to the county board.

Decline of Personal Property Value

According to Cornia and Wheeler, "since the mid-1950s, the percentage of the total property tax assessed value coming from [personal property] has declined in virtually every state." While the decline has not been as precipitous in Utah as in other states, the assessed value of personal property as a percentage of assessed value of all property has fallen 2.2% from 1956 to 1991. In disaggregating the personal property tax values, we find that this decline continues in more significant fashion for business property tax values. From 1992 to 2003 the assessed business personal property value has fallen from 7.7% of total property values to 6.2%, a decline of 1.5% just in the last eleven years shown in Figure 4.

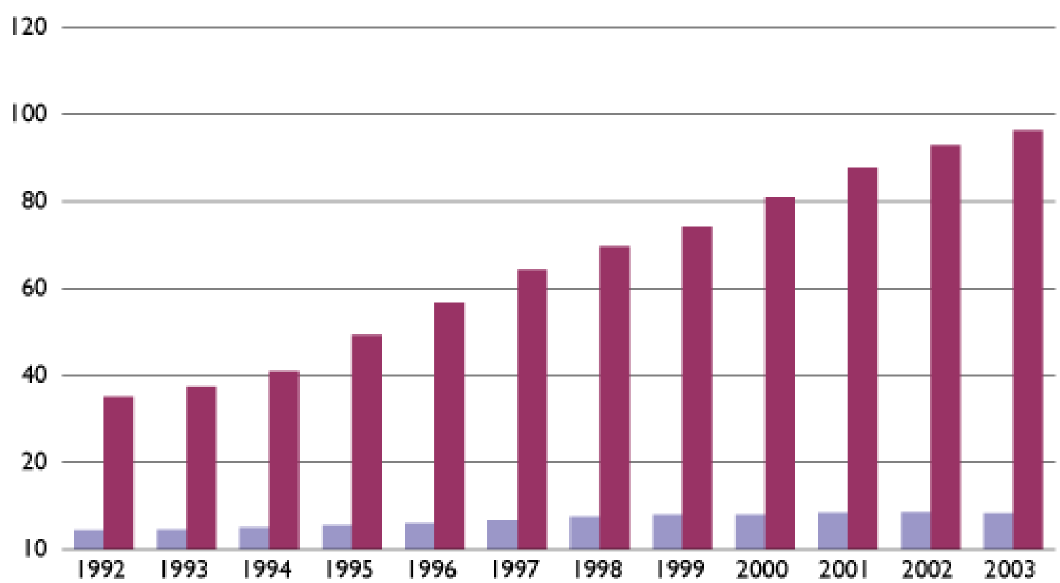
Figure 4: Business Personal Property Value as Percent of Total Property



Source: Utah State Tax Commission: Property Tax Division

The rapid increase of real property values is a major reason that the percentage of the total property tax assessed value coming from personal property has decreased significantly in the past decade. From 1992 to 2003 real property values grew 213%, while personal property values have only grown 53%. A comparison of personal property value and real property value is shown in Figure 5.

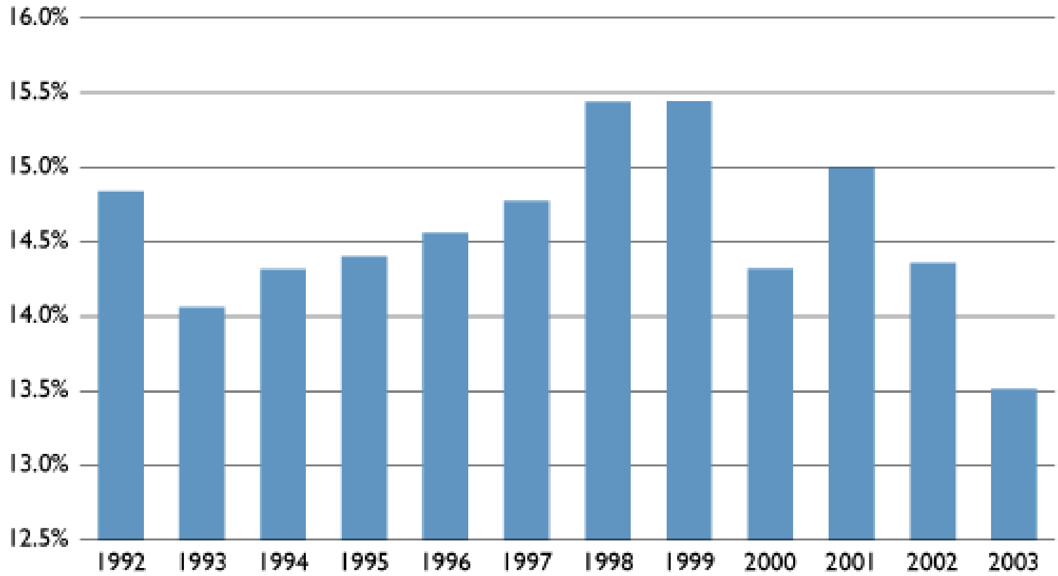
Figure 5: Taxable Value of Personal Property vs. Real Property ($Billions)



Source: Utah State Tax Commission: Property Tax Division

Another explanation for why personal property values are declining relative to total property values is that the tax base may be narrowing. However, from 1992 to 2003 there was no legislation to narrow the personal property tax base. Also a comparison of personal property value growth with personal income growth (an indicator for economic growth) does not provide any conclusive evidence that the tax base is eroding (Figure 6). Figure 6 shows that personal property value grows relative to personal income during economic expansion, but declines during economic contraction.

Figure 6: Business Personal Property Value as a Percent of Personal Income



Source: Utah State Tax Commission: Property Tax Division; Bureau of Economic Analysis; Calculations by Utah Foundation

Equity

Another concern that business personal property taxes raises is that of horizontal equity. Businesses with similar income levels may be paying significantly different amounts of personal property tax. If the assumption that manufacturing businesses utilize more personal property than service businesses, then a manufacturing business will end up paying more taxes than a service business that makes a similar profit. However, property taxes, in principle, are supposed to be a tax on wealth, and businesses that hold more assets may have more value than businesses with fewer assets, even if their profits are similar.

Comparison with Other States

Currently 39 other states and the District of Columbia continue to tax personal property (Figure 7). As of 1992, according to John Mikesell, sixteen states continue to tax business inventory and only eight states continue to tax intangible personal property (Figure 7)[2]. Utah taxes neither business inventory nor intangible property. Intangible personal property includes stocks, bonds, and franchises. Most states have eliminated taxes on intangible personal property because the tax is very difficult to administer. According to Cornia and Wheeler, most states have eliminated inventory taxes because they can cause competitive disadvantages for businesses that often ship goods to other states.

Figure 7: Taxability of General Personal Property Tax Bases (1992)

	Intangible Property	Business Inventory	Business Depreciable Fixed Assets
Alabama	Tax	Exempt	Tax
Alaska	Exempt	Tax	Tax
Arizona	Exempt	Exempt	Tax
Arkansas	Exempt	Tax	Tax
California	Exempt	Exempt	Tax
Colorado	Exempt	Exempt	Tax
Connecticut	Exempt	Exempt	Tax
District of Columbia	Exempt	Exempt	Tax
Florida	Exempt	Exempt	Tax
Georgia	Exempt	Tax	Tax
Idaho	Exempt	Exempt	Tax
Indiana	Exempt	Tax	Tax
Kansas	Exempt	Exempt	Tax
Kentucky	Tax	Tax	Tax
Louisiana	Tax	Tax	Tax
Maine	Exempt	Exempt	Tax
Maryland	Exempt	Tax	Tax
Massachusetts	Exempt	Tax	Tax
Michigan	Exempt	Exempt	Tax
Mississippi	Tax	Tax	Tax
Missouri	Exempt	Exempt	Tax
Montana	Exempt	Tax	Tax
Nebraska	Exempt	Exempt	Tax
Nevada	Exempt	Exempt	Tax
New Mexico	Exempt	Exempt	Tax
North Carolina	Exempt	Exempt	Tax
Ohio	Exempt	Tax	Tax
Oklahoma	Exempt	Tax	Tax
Oregon	Exempt	Exempt	Tax
Rhode Island	Exempt	Tax	Tax
South Carolina	Exempt	Exempt	Tax
Tennessee	Tax	Exempt	Tax
Texas	Exempt	Tax	Tax
Utah	Exempt	Exempt	Tax
Vermont	Exempt	Exempt	Tax
Virginia	Exempt	Exempt	Tax
Washington	Tax	Tax	Tax
West Virginia	Tax	Tax	Tax
Wisconsin	Exempt	Exempt	Tax
Wyoming	Tax	Exempt	Tax

Note: Delaware, Hawaii, Iowa, Illinois, Minnesota, North Dakota, New Hampshire, New Jersey, New York, Pennsylvania, and South Dakota have no personal property tax.

Source: Mikesell, J.L. (1992). Patterns of exclusion of personal property from American property tax systems, *Public Finance Quarterly*.

Conclusion

While the personal property tax on businesses only constitutes 6.3% of total property tax revenues, eliminating the tax would mean a loss of over $100 million in revenue for local governments and schools in Utah. However, if the personal property tax base continues to erode and real property values continue to rise, the personal property tax will play a smaller and smaller role in financing government and schools. These factors along with questions of administration, compliance, and equity must be considered when discussing the business personal property tax in Utah.

Endnotes

[1] Cornia, G.C. and Wheeler, G.E. (1999). The Personal Property Tax, Handbook on Taxation (W.B. Hildreth and J.A. Richardson, ed.).

[2] Mikesell, J.L. (1992). Patterns of exclusion of personal property from American property tax systems, Public Finance Quarterly.

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