LOCAL GOVERNMENT RESPONSE TO SHEFFRIN PROPOSAL

HCR 11 TASK FORCE

The purpose of this correspondence is to provide commentary and clarity in regards to an evolving proposal that is being reviewed by the HCR 11 Task Force from the perspective of local government taxing bodies.

In response to Professor Sheffrin's proposal to the HCR 11 Task Force the following issues should be taken into consideration, at the request of the Louisiana School Boards Association, the Police Jury Association of Louisiana, the Louisiana Municipal Association, the Louisiana Tax Assessors, the Louisiana Sheriff's Association, and the Louisiana District Attorney's Association.

1. Any proposal to alter the property subject to ad valorem taxation or to alter the assessment rate of or create and set an assessment rate applicable to a new class of property should be by Constitutional amendment and should include an automatic millage adjustment.
2. The increase in one source or type of tax revenue as an off-set to a reduction of another source or type of tax revenue, when considering "local government" in the aggregate is not a valid concept.
3. The issues pertaining to the classification of property as "inventory" or otherwise, have nothing to do with the authority of a School Board, a Parish government, a Municipal government, a Sheriff, a District Attorney, or any other unit of government.

Further Explanation/Rationale

1. Any proposal to alter the property subject to ad valorem taxation or to alter the assessment rate of or create and set an assessment rate applicable to a class of property should be by Constitutional amendment and should include an automatic millage adjustment.

Adjusting the taxability of property or creating a new class of property or assessment rate are issues that must be addressed with a Constitutional amendment. The taxability of property and the assessment rate are set forth in Part II or Article VII of the Louisiana Constitution. Therefore, to make the proposed changes would require a Constitutional amendment. The last time the State imposed a significant change in the taxability of property was the adoption of the Homestead Exemption, through a Constitutional amendment. In that amendment was included the following language:

> *the total amount of ad valorem taxes collected by any taxing authority in the year in which Sections 18 and 20 of this Article are implemented shall not be increased or decreased, because of their provisions, above or below ad valorem taxes collected by that taxing authority in the year preceding implementation. To accomplish this result, it shall be mandatory for each affected taxing authority, in the year in which Sections 18 and 20 of this Article are implemented, to adjust millages upwards or downwards without regard to millage limitations contained in this constitution, and the maximum authorized millages shall be increased or decreased, without further voter approval, in proportion to the amount of the adjustment upward or downward.*

This language ensured that the benefit provided to the targeted taxpayers did not dramatically impact the local taxing bodies that were dependent on ad valorem tax revenue to meet their respective public obligations. Providing for the same in the proposed Constitutional amendment to create a class of "inventory property" and an assessment rate of 10% thereof would be a necessary component of any such proposal.

2. The increase in one source or type of tax revenue as an off-set to a reduction of another source or type of tax revenue, when considering "local government" in the aggregate is not a valid concept.

"Local government" is not a single homogeneous entity. There are critical differences in authority, function and obligation between the multiple "local government" entities that are often lumped together. There are "local government" entities that are not even represented by the organizations submitting this response, such as special districts (recreation, solid waste, fire, etc.) Even among the common districts, it should be noted that while the homestead exemption impacts the ad valorem taxes levied by parishes, school boards and even sheriffs, it has zero impact on municipal ad valorem taxes. The common misconception is the attempt to substitute an increase in sales taxes for a decrease ad valorem taxes. It should be noted that every parish and municipality levies ad valorem taxes but not every parish or municipality levies sales taxes.

It should be noted that many special districts, such as BREC (Baton Rouge Recreation Commission) levies ad valorem taxes as, essentially, its sole source of revenue, but does not levy a sales tax. A Parish like Cameron, which has no sales tax, would be in the same position as BREC, potentially losing ad valorem taxes without the increase in sales taxes.

Also, the payors of sales taxes and ad valorem taxes are, in many cases, disparate.

A Parish like St. James Parish has a relatively low population and no significant commercial center (no shopping mall) but has significant industry. That industry is a significant payer of property taxes, but the commercial driver of sales taxes, consumer commerce, is often shifted to more suburban parishes like EBR or Jefferson. Therefore, the concept of thinking of "local government" in the aggregate and proposing tax off-sets, also in the aggregate, ignore the reality that such a tax swap would actually create winners and losers among communities.

School Boards stand in a somewhat unique position as well, as a change in the ad valorem tax base will impact the relative wealth calculation of the Minimum Foundation Program (MFP). The MFP looks at the aggregate value of property subject to ad valorem taxation as a major component in determining a particular school district's allotment of MFP dollars.

Simply put, wealthier parishes get less MFP (state dollars for public education) and poorer parishes get more MFP. This calculation uses valuations that are generally two years old. Thus any significant change that would reduce a wealthy parish's aggregate value of taxable property would result in a reduction of local ad valorem revenues, but that change would lag two or more years back in the district's MFP allocation. T

Therefore, any proposal must avoid: the aggregation of "local government" into a single category and the aggregation of "local government tax revenues" in to a single lump sum total.

3. The issues pertaining to the classification of property as “inventory” or otherwise have nothing to do with the authority of a School Board, a Parish government, a Municipal government, a Sheriff, a District Attorney, or any other unit of government.

It is a common misconception that one of the factors attributing to the increase in the State’s obligation under the “inventory tax credit” is a lack of diligence on the part of one or more of the entities commonly referred to as “local government”. None of those entities plays any role in the classification of taxable property for assessment of ad valorem taxes.

By and large, taxpayers/property owners declare the nature of their property. In the case of “inventory” the business taxpayer declares what amount of the business’s movable property is “inventory”. The classification of a portion of that movable property as “inventory” does not impact the valuation of the assessment (the Assessor’s job) or the ad valorem tax payable from all movable property reported by the business taxpayer/property owner.

That classification impacts, only, the State of Louisiana, as a taxer of business income. The State generally simply accepts the classification of movable property by the business taxpayer/property owner as “inventory” and then executes the business income tax credit in accordance with such classification.

Presumably, the State could audit or question or require more evidentiary basis for the classification. Therefore, the comment in the report that “Local governments would have an incentive not to classify property as inventory…” evidences a fundamental misunderstanding of the ad valorem tax assessment process. “Local governments” do not make that classification determination.

Certainly, if the core proposal of creating a class of business movable property “inventory” was assessed at a lower rate than other movable property the classification issue would move down the chain, as it were. But it would not fall to the “local governments” as taxing bodies, but rather would fall to the Assessor and, in the event of a dispute, to the Louisiana Tax Commission, the entity that resolves disputes as to the proper valuation of assessment of property.

These examples also highlight why any proposal to substitute one source of tax revenue for another can be fraught with unintended negative consequences for individual jurisdictions and units of local government.

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