REPORT OF THE
AUDITOR OF PUBLIC ACCOUNTS

A Study to Determine the Extent that Owners Receive Tax Relief for Unqualified Vehicles under the Personal Property Tax Relief Act of 1998

TO THE GOVERNOR AND
THE GENERAL ASSEMBLY OF VIRGINIA

SENATE DOCUMENT NO. 14

COMMONWEALTH OF VIRGINIA
RICHMOND
2001

Commonwealth of Virginia

Walter J. Kucharski, Auditor

Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218

December 1, 2000

The Honorable James S. Gilmore, III
Governor of Virginia
State Capitol
Richmond, Virginia

Members of the Virginia General Assembly
General Assembly Building
Richmond, Virginia

We have completed our study of the Personal Property Tax Relief Act of 1998 (the Act) as directed by Senate Joint Resolution 127 of the 2000 General Assembly and are pleased to submit our report entitled "A Study to Determine the Extent that Owners Receive Tax Relief for Unqualified Vehicles under the Personal Property Tax Relief Act of 1998."

Scope

In conducting this review, we researched the roles and responsibilities of state agencies, local governments, leasing companies and others involved in administering the Act. We reviewed the processes that local governments use to determine if vehicles qualify for tax relief under the Act. We obtained information regarding these processes through use of a survey sent to local Commissioners of the Revenue and through interviews with state and local officials.

Results

We have determined that the current process does not provide enough information for local Commissioners of the Revenue to enforce the provisions of the Act. Also, the process does not adequately inform the public of how they should comply with the laws of the Act.

We have recommended several measures to help Commissioners enforce the provisions of the Act and to educate the public about the law. We provide these recommendations within this report.

We discussed this report with agency directors from the Departments of Motor Vehicles and Taxation and the President of the Local Commissioners of the Revenue Association, and include their response to this study in Appendix C of this report.

AUDITOR OF PUBLIC ACCOUNTS

Preface

Senate Joint Resolution 127 required the Auditor of Public Accounts to review the extent to which owners receive tax relief under the Personal Property Tax Relief Act of 1998 for unqualified vehicles. The 1998 General Assembly enacted the Personal Property Tax Relief Act (the Act), which provides tax relief on personal property taxes paid on the first $20,000 of value for qualifying vehicles. The Act includes provisions for the phase out of the tax on qualified vehicles over 5 years. The Act also defines qualifying vehicles and requires that the vehicles' use be for non-business use.

A study group representing the Auditor of Public Accounts included the following assigned staff:

Walter J. Kucharski, Auditor of Public Accounts
Glenn M. Loehr, Audit Director
Kristin Anliker, Auditor

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Executive Summary

Senate Joint Resolution 127 required our office to review the extent to which owners received tax relief under the Personal Property Tax Relief Act of 1998 for unqualified vehicles. The 1998 General Assembly enacted the Personal Property Tax Relief Act (the Act), which provides tax relief on personal property taxes paid on the first $20,000 of value for qualifying vehicles. The Act includes provisions for the phase out of the tax on qualified vehicles over 5 years. The Act also defines qualifying vehicles and requires that the vehicles' use be for non-business use.

FINDING

We have determined that local Commissioners of the Revenue cannot enforce the provisions of the Act for determining if a vehicle's business use exceeds the levels set by statute. The current process does not provide Commissioners of the Revenue information on vehicles used for business purposes that do not qualify for tax relief under the Act.

Also, the current process does not adequately inform the public of how they should report their vehicle use to comply with the laws of the Act.

RECOMMENDATION

If the General Assembly wishes to have the Commissioners of Revenue enforce the provisions of the Personal Property Tax Relief Act of 1998 concerning unqualified vehicles used for business purposes, the General Assembly will need to have the following done.

1. The Department of Taxation must provide the Commissioner more information about who is claiming a deduction or expense and information about the vehicles.

2. The Commissioner must provide taxpayers information about the provisions of the Personal Property Tax Relief Act of 1998 concerning unqualified vehicles used for business purposes both when the taxpayer initially registers the vehicle and during the billing cycle. Commissioners and Treasurers must require taxpayers to certify the vehicle use at registration and billing.

3. The Department of Motor Vehicles must require vehicle dealers and leasing companies to certify use of vehicle at registration and provide this information to Commissioners.

4. The General Assembly may wish to provide some incentive to the Commissioners for enforcing this provision and defraying the cost of the information.

Purpose of Study

Senate Joint Resolution 127 (2000) requested the Auditor of Public Accounts to review the extent to which owners received tax relief under the Personal Property Tax Relief Act of 1998 for unqualified vehicles.

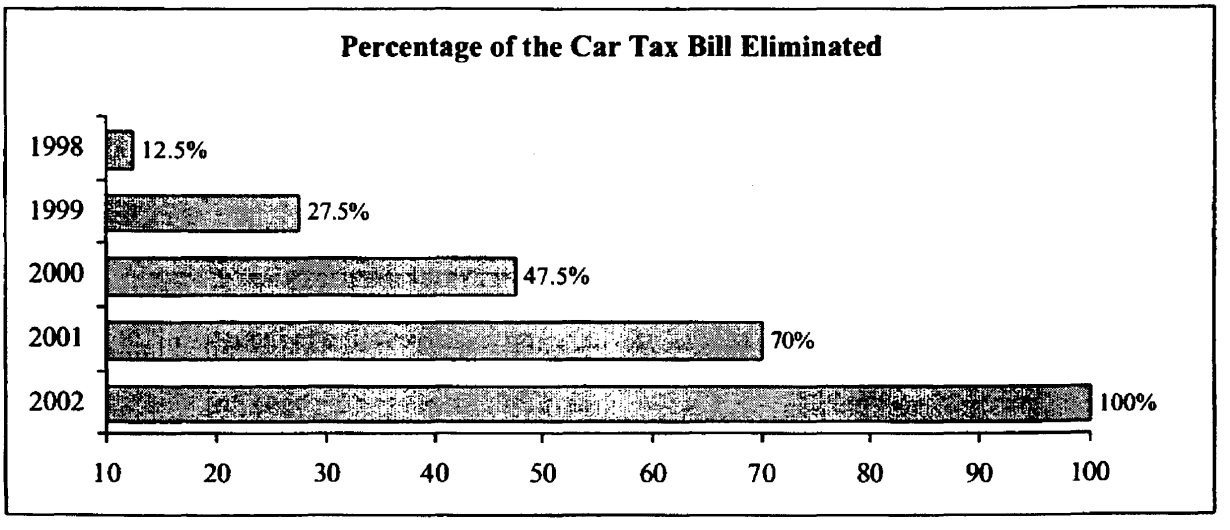
Background Information

The 1998 General Assembly enacted the Personal Property Tax Relief Act (the Act), which provides tax relief on personal property taxes paid on the first $20,000 of value for qualifying vehicles. The Act includes provisions for the phase out of the tax on qualified vehicles over 5 years. The Act also defines qualifying vehicles and requires that the vehicle use be for non-business use.

Qualifying vehicles are privately owned or leased cars, panel and pick-up trucks (less than 7,501 pounds) and motorcycles.

Non-business means that the preponderance of a vehicle's use is for other than business purposes. The Act further defines "preponderance of use for other than business purposes" shall be deemed not to be satisfied if: (i) the motor vehicle is expensed on the taxpayer's federal income tax return pursuant to Internal Revenue Code § 179; (ii) more than fifty percent of the basis for depreciation of the motor vehicle is depreciated for federal income tax purposes; or (iii) the allowable expense of total annual mileage in excess of fifty percent is deductible for federal income tax purposes or reimbursed pursuant to an arrangement between an employer and employee.

The chart below provides the percentage of taxes eliminated over a five-year period, for vehicles valued at more than $1,000 and less than $20,000.



For tax year 1998, taxpayers paid 100 percent of their tax bill and subsequently received a check from the Commonwealth of Virginia for the 12.5 percent tax reduction. Beginning in tax year 1999, localities reduced tax billings based on the percentage rates outlined in the chart above. Localities then receive payments from the state for the full amount of the reduced tax collections by submitting a reimbursement request to the Department of Accounts (Accounts). For the fiscal year ended June 30, 2000, the Commonwealth paid $338,790,000 to localities for tax relief granted to citizens.

Methodology

In conducting this review, we researched the roles and responsibilities of state agencies, local governments, leasing companies, and other parties involved in administering the Act. We reviewed the processes that local governments use to determine if vehicles qualify for tax relief under the Act. We obtained information regarding these processes through use of a survey sent to local Commissioners of the Revenue and through interviews with state and local officials.

Primary Study Issues

We have identified two primary study issues in determining whether owners using vehicles for business use have inappropriately received tax relief under the Act. These study issues involve the processes used by localities to determine a vehicle's use as either primarily for personal or business. The study issues follow.

- How do localities identify vehicles reported as personal use but used primarily for business purposes, at the time of purchase or lease?

- How do localities identify changes in a vehicle's use from year to year?

Purchase or Lease of a Vehicle

Commercial Vehicles

Under the Act, the vehicle dealer or leasing company does the initial determination of whether a vehicle will be subject to tax relief. Vehicle dealers and leasing companies know to report that all vehicles purchased in a company name, receiving a commercial license, or being over the weight limit do not qualify for tax relief. The Department of Motor Vehicles (DMV) receives the information, and the vehicle dealer data goes into the registration system, and the lease information goes into a separate leased vehicle database. After processing, DMV provides the information to the local Commissioner of Revenue (Commissioner).

Personal Vehicles

When an individual purchases or leases a vehicle, the vehicle dealer or leasing company could as part of this purchase inquire about the vehicle's use. This inquiry is especially important during the leasing process if a company leases a vehicle, but puts the vehicle in an individual's name. Based on the information obtained during the purchase or lease, this data goes from the vehicle dealer or leasing company to DMV and then to the local Commissioner.

Unless, the vehicle registration has a company name or identification or exceeds the weight limit, DMV does not have a mechanism to challenge the correctness of the information. Most Commissioners rely on the information from DMV to bill for either the city or county decal and prorated personal property taxes.

During this initial registration for a county or city decal, some Commissioners do have printed materials that ask the owner to indicate the use of the vehicle. These forms do not always explain what constitutes primarily personal use or business use, so the individual may not understand the reporting requirement. A few localities do have signed declaration of vehicle use, however, most localities do not have procedures requiring any declaration of vehicle use. Again, unless the Commissioners or their staff has some reason to challenge the taxpayer, they rely on the information provided.

DMV has noted the responsibilities that vehicle dealers and leasing companies play in this process may be unclear. To clarify and inform these groups, DMV has developed a pamphlet and training session explaining their responsibilities.

Issues with the Registration Process

The current registration process does not inform taxpayers of the restriction related to qualifying a vehicle for tax relief under the Act. The assumption in the process is that an individual is either purchasing or leasing a vehicle for personal use, unless the individual informs someone to contrary. In those circumstances where a Commissioner does attempt to obtain information about the use of the vehicle, many of the forms we saw did not explain the reason for asking the question about "personal use or business use." In some circumstance, the form appears to ask the question, who will drive the vehicle rather than how the owner will use the vehicle.

Currently, DMV does not have the information to improve this process. In order to assist Commissioner in obtaining information, DMV could alter the registration form and require vehicle dealers and leasing companies to provide information. Otherwise, DMV can only continue its educational process to keep vehicle dealers and leasing companies informed of their duty under the Act. Additionally, if the Commissioners do not take a more active role of informing individuals of the restriction related to business use, then the opportunity to gather this data does not exist.

Qualifying a vehicle for tax relief under the Act relies on the taxpayer voluntarily providing information about the business use of a vehicle. The current process assumes the taxpayer understands that all personal vehicles may not qualify for tax relief and will honestly inform the vehicle dealer, leasing company, DMV or the Commissioner of the vehicle's intended use. Based on our survey and discussions with others, we do not believe that the average person understands that business use of a vehicle would disqualify it for tax relief under the Act.

Additionally, there are only financial disincentives for any one in the registration process to aggressively seek this information. Obviously, vehicle dealers or leasing companies could potentially lose sales, and taxpayer ignorance works to their advantage. Commissioners reduce the cost to locality and improve collection rates with personal use vehicles rather than having to internally bill and collect on business use vehicles. And neither the Commissioners nor DMV receive funding to collect additional information and educate the public about the business use of vehicles.

Identifying changes in a vehicle's use

When an individual purchases or leases a vehicle, it may not be their intent to use the vehicle for business. However, they may change jobs or circumstances and begin using their vehicle for work.

If these individuals use their vehicles in their business endeavors, they may receive a mileage reimbursement or claim a tax deduction for the use of the vehicle on their income tax returns. The Act does not give tax relief if the taxpayer does any of the following (i) the motor vehicle is expensed on the taxpayer's federal income tax return pursuant to Internal Revenue Code § 179; (ii) more than fifty percent of the basis for depreciation of the motor vehicle is depreciated for federal income tax purposes; or (iii) the allowable expense of total annual mileage in excess of fifty percent is deductible for federal income tax purposes or reimbursed pursuant to an arrangement between an employer and employee.

If the amount of the deduction exceeds the percentages noted above, the individual should not receive tax relief. With some individuals the amount of usage and the amount of the deduction claimed varies from year to year.

We examined methods available to Commissioners within the current reporting structure to determine if they had the information to evaluate the level of business use. We also examined whether taxpayers received information that would allow them to voluntarily report changes in the personal versus business use of vehicles.

Taxpayers claiming vehicle expenses for business purposes, enter this information on their federal tax return on Schedule C. The Department of Taxation no longer requires taxpayers to file this schedule with their state returns. If the Department of Taxation did continue to require taxpayers to file this schedule, the schedule lacks sufficient information for the Commissioners to identify a specific vehicle since they do not contain a vehicle identification number or license plate number and, in many instances, do not contain even a description of the vehicle.

The Department of Taxation could obtain information from this schedule from the Internal Revenue Service information when a taxpayer files their return electronically. However, the quality of this information would be the same as on the physical Schedule C.

Additionally, we did not find any Commissioners or Treasurers that provide taxpayers with any information concerning the business use of vehicles and the potential loss of tax relief during the personal property tax billing process. Commissioners who used the federal tax schedule when the Department of Taxation provided them, stated that this was an extremely labor-intensive process and required significant verification before they could begin questioning a taxpayer about the business use of a vehicle.

Findings and Recommendations

The current process does not inform the taxpayers of the restrictions on tax relief when they use their vehicles for business use. As originally enacted, the business use provisions of the Act relied on voluntary compliance by the taxpayer. However, without knowledge of the business use restriction, taxpayers are unaware of the provision and, therefore, do not know to comply.

We found no evidence of any on-going effort to inform taxpayers of the business use restrictions in the Act, except when originally registering a vehicle with a Commissioner in a few localities. For the most part, the current initial purchasing or leasing process of personal vehicles does not attempt to obtain information about potential business use or inform the purchaser or leaser of the business use restriction.

The personal property tax billing process also does not provide taxpayers with information concerning the restriction on tax relief. We found no localities that provided taxpayers with any information on the business use restric tions after the initial registration of the vehicle.

The current lack of information on business use makes enforcement of this provision almost impossible. Commissioners and their staff must rely almost solely on observation or limited local information of an individual's business activities.

ESTIMATING IMPACT OF NON-COMPLIANCE

We could not find any actual information on the number of vehicles, amount of deductions, or other tax information that would provide either an actual or statistical projection of the non-compliance with the Personal Property Tax Relief Act of 1998 for unqualified vehicles.

In order to provide the General Assembly with some basis to evaluate the potential impact of this issue, we attempted to estimate the number of vehicles and the amount of improper tax relief the Commonwealth incurs. For this computation, we limited our analysis to only Schedule C filers. We believe that there are potentially individuals who file partnership returns and farming business returns (Schedule F) that also may claim a tax deduction that would disqualify them from receiving the personal property tax relief.

We obtained through the Internal Revenue Service the number of returns filed in Virginia with Schedule C for the tax year 1998. We discussed these provisions of the personal property tax act with local, state and federal tax officials and obtained a joint consensus that between 10 to 20 percent of the individuals filing the Schedule C returns would have vehicle expenses that meet the personal property tax act provisions. In appendix B, we have computed the potential payment for vehicles that do not qualify for the personal property tax relief at approximately $7.4 million.

POTENTIAL COMPLIANCE MEASURES

To ensure compliance with the business use restrictions of the personal property tax act will require a twofold approach. The first item is the need to inform the public of the restriction and how they should comply with the law. The second item is providing Commissioners with information that will allow them to enforce the restriction.

The information campaign on the restriction needs to start with the purchase of the vehicle and follow through to the annual personal property tax billing. DMV and the Commissioners need to develop an information campaign that informs vehicle dealers and leasing companies of their importance in this process of identifying business use of vehicles or at least the need to inform buyers or lessees of the restriction. The next phase for Commissioners is providing clearer information about the restriction to vehicle owner at the time they receive their decal. And finally, annual tax billings or other notifications should inform the taxpayers of the restriction and give them the opportunity to indicate the use of their vehicle.

The enforcement phase of compliance will require that Commissioners have better information to allow them to begin the enforcement process. To provide Commissioners with this information, we are recommending that Taxation begin collecting vehicle registration and information for anyone claiming a deduction for automotive expenses on Schedule C. Taxation plans to collect electronically the information from the Internal Revenue Service and vehicle registration and license tag information would supplement this information they already plan to gather. Taxation estimates that to develop a new form and collect the information will cost $275,000 annually.

While Taxation's estimate did not include funding for compliance enforcement, when individuals do not provide the information, we believe that the Commissioners have the responsibility to request information when a filer does not provide information. This information provides the Commissioners with at least the basic information to enforce the provisions of the business use restriction.

COMPLIANCE COSTING AND FUNDING

While we were able to obtain an estimate for the cost of new data collection forms at Taxation, we could not obtain any information on modifying existing Commissioner's tax forms either for the initial registration or annual billing. Several Commissioners indicated that determining the cost of the change would depend on the amount of information provided about the business use restrictions. All Commissioners indicated that they do not have the funding to make the change and provide for an enforcement effort. The Commissioners also stated that they would incur additional costs to review the forms and meet with the taxpayers to resolve vehicles in question.

RECOMMENDATION

If the General Assembly wishes to have the Commissioners of Revenue enforce the provisions of the Personal Property Tax Relief Act of 1998 concerning unqualified vehicles used for business purposes, the General Assembly will need to have the following done.

1. **The Department of Taxation must provide the Commissioner more information about who is claiming a deduction or expense and information about the vehicles.**

2. **The Commissioners and Treasurers must provide taxpayers information about the provisions of the Personal Property Tax Relief Act of 1998 concerning unqualified vehicles used for business purposes both when the taxpayer initially registers the vehicle and during the billing cycle. Commissioners and Treasurers must require taxpayers to certify the vehicle use at registration and billing.**

3. **The Department of Motor Vehicles must require vehicle dealers and leasing companies to certify use of vehicle at registration and provide this information to Commissioners.**

4. **The General Assembly may wish to provide some incentive to the Commissioners for enforcing this provision and defraying the cost of the information.**

APPENDIX A: Senate Joint Resolution No. 127

Directing the Auditor of Public Accounts to examine the extent to which tax relief granted under the Personal Property Tax Relief Act of 1998 is accruing to or being received by businesses ineligible for such tax relief under the provisions of the Act.

Agreed to by the Senate, February 15, 2000
Agreed to by the House of Delegates, March 8, 2000

WHEREAS, the Personal Property Tax Relief Act of 1998 (§ 58.1-3523 et seq. of the Code of Virginia) was passed during the 1998 Session of the General Assembly; and

WHEREAS, the Act grants personal property tax relief to private citizens of Virginia owning or leasing certain enumerated motor vehicles and using such vehicles for nonbusiness purposes; and

WHEREAS, the amount of such personal property tax relief appears as a credit or a reduction of the tax due on the personal property tax bills of Virginia's citizens; and

WHEREAS, the full amount of such personal property tax relief is being funded by the Commonwealth of Virginia through reimbursement payments to local governments to reimburse such governments for any decreases in revenue attributable to the Act; and

WHEREAS, the personal property tax relief for tax year 2000, as provided in the Act, is, in general, 47.5 percent of the personal property tax assessed on such motor vehicles; and

WHEREAS, there is credible evidence that personal property tax relief under the Act, which is funded or paid for by the Commonwealth, is being granted to or received by businesses; and

WHEREAS, such businesses are ineligible to receive tax relief under the provisions of the Act; and

WHEREAS, the cost of personal property tax relief to the Commonwealth will increase if such businesses continue to receive personal property tax relief at the expense of the Commonwealth; and

WHEREAS, the Auditor of Public Accounts is required by § 2.1-155 to incorporate into his audit procedures and processes a review process to ensure that the Commonwealth's payments for qualifying vehicles, as defined in § 58.1-3523, are consistent with the provisions of §§ 58.1-3525 and 58.1-3526; and

WHEREAS, it is in the best interests of the Commonwealth to ensure that its appropriations and expenses are limited to that required by law and no more; now, therefore, be it

RESOLVED by the Senate, the House of Delegates concurring, That the Auditor of Public Accounts be directed to examine the extent to which tax relief granted under the Personal Property Tax Relief Act of 1998 is accruing to or being received by businesses ineligible for such tax relief under the provisions of the Act. The Commissioner shall recommend a course of action to ensure that the Commonwealth's payments for qualifying vehicles, as defined in § 58.1-3523, are consistent with the provisions of the Act.

The Department of Motor Vehicles, the Department of Taxation, and localities shall provide technical assistance to the Auditor of Public Accounts in the conduct of this study. All agencies of the Commonwealth shall provide assistance to the Auditor of Public Accounts, upon request.

The Auditor of Public Accounts shall complete his work in time to submit his findings and recommendations by December 1, 2000, to the Governor and the 2001 Session of the General Assembly as provided in the procedures of the Division of Legislative Automated Systems for the processing of legislative documents.

APPENDIX B: Estimated Tax Payments on Business Use Vehicles; Cost Estimate for Additional State Tax Form

The current process does not provide information to determine the exact amount of tax relief paid for business use vehicles. However, we used the following information to estimate an amount the Commonwealth may have paid for these vehicles. All data relates to the 1998 tax year.

- Average assessed value for vehicles in Virginia $7,250
  (**Source**: Department of Motor Vehicles)
- Median personal property tax rate for all localities $2.60 per $100 assessed
  (**Source**: Weldon Coopers Center for Public Service, UVA)
- Federal Schedule C's filed by Virginia taxpayers 395,066 filings
  (**Source**: IRS, Statistics on Income website)

Taxpayers file Schedule C to report business income and expense, including expenses for use of business vehicles.

Estimated loss to Commonwealth for payments on business use vehicles

We assumed one vehicle per each Schedule C filed and multiplied this amount by the average assessed value per vehicle to obtain the total assessment of vehicles reported on Schedule C.

395,066	(vehicles per Schedule C)
X $7,250	(avg. assessed value per vehicle)
$2.8 billion	(total assessment of vehicles reported on Schedule C)

Applying the median tax rate of $2.60 to this total assessed value provides the total amount of tax relief possibly received for these business use vehicles.

$2.8 billion	(total assessment of vehicles reported on Schedule C)
X $2.60	(median tax rate per $100 assessment)
$74.4 million	(total amount of business use vehicles receiving tax relief)

In discussions with federal, state, and local officials, a reasonable assumption would be that 1 in 10 Schedule C filers do not qualify for tax relief under the Act. Using this assumption, the amount of tax paid on business use vehicles totals approximately $7.4 million. These calculations, however, do not include vehicles reported on Schedule F (Farm Businesses) and Partnership filings, which may also include business use vehicles. Also, as mentioned above, we have assumed only one vehicle reported on each Schedule C.

Estimated cost to obtain additional information from tax filers

Identifying vehicles claimed as expense deductions on federal tax returns would provide a mechanism for verifying vehicle use. Identifying these vehicles would require capturing additional information from taxpayers such as vehicle identification numbers. The State Department of Taxation has provided a cost estimate that includes developing and distributing an additional state tax form that captures the additional information. Taxation estimates the total cost at $275,000 annually. This cost, however, does not include a compliance program that ensures taxpayers file the required form. Also, localities would incur additional costs to review the forms and meet with taxpayers to resolve vehicles in question.

APPENDIX C: Agency Responses

State agencies and local government officials involved in our study have had the opportunity to review and comment on an exposure draft of the report. This appendix contains responses from the Departments of Motor Vehicles and Taxation, and the President of the Commissioners of the Revenue Association. Technical corrections have resulted from the written comments made to us in this version of the report. As a result, some response comments and page numbers do not correspond to this revision of the report.

The tables below present certain issues included in the agency responses that we believe require further clarification.

Department of Taxation Concerns/Comments	APA Response
1. The auditor's recommendation to develop an additional tax form would require Taxation to identify all Schedule C filers within the Commonwealth. Taxpayers are no longer required to file Federal Schedule C with their Virginia Individual Income Tax Returns. The IRS restricts the use forms or returns by state tax agencies to state tax administration purposes only. The Virginia vehicle tax is a local tax.	Although Taxation will not require filing of Schedule C's with individual returns, Taxation can still request that Schedule C filers provide the additional information on the proposed State return. Tax does receive IRS information that will allow Commissioners to determine who files a Schedule C. The audit recommendation provides for an additional state tax form that gathers vehicle information to assist Commissioners in determining vehicle use. As noted above, Taxation can require all Schedule C filers to submit the new state form. Commissioner will receive only information from the additional state form. We do not plan to use Federal Schedule C although Taxation plans to provide this information electronically to Commissioners for other purposes.
2. Taxpayers could certify vehicle use as a function of filing the local annual personal property tax return or Virginia Form 762 at the local level.	While the Form 762 would provide information that we are recommending in the recommendation related to the billing and registration process, it still does not provide information for enforcement.
3. Localities or DMV could cross check information obtained from vehicle owners regarding the use of vehicles, to insurance coverage records maintained by the owner's insurer.	There is no existing requirement to report insurance information to either DMV or the Commissioners. Implementing this proposal would require legislation and other extensive administrative changes.

Department of Motor Vehicles Concerns/Comments	APA Responses
1. The APA appears to assume that 100 percent of business vehicle owners are inappropriately reimbursed for their business vehicles. The $7.4 million estimate of the cost of improper reimbursement for business vehicles may be too high.	The auditor's calculation in appendix B assumed only 10 percent of the Schedule C filers would have a vehicle that would meet the business use disqualification. The estimate also assumes only one vehicle claimed for each Schedule C and the value is the statewide average assessment. In addition, our calculations do not include vehicles reported on Schedule F (Farm Businesses) and Partnership filings that may also include business use vehicles.
2. APA states that DMV should alter its registration form and require vehicle dealers and leasing companies to provide information on vehicle use. This is not included in their findings and recommendations.	Recommendation number 3 was added to the final report and states that "The Department of Motor Vehicles must require vehicle dealers and leasing companies to certify use of vehicles at registration and provide this information to Commissioners."
3. DMV would be reluctant to alter our current vehicle registration form to capture any information from vehicle owners, dealers, and leasing companies regarding vehicle use. DMV sites the lack of statutory requirements that would require citizens to provide DMV with data on vehicle use.	We are aware that current statutes do not require DMV to capture information on vehicle use. However, capturing this information would assist Commissioners in determining vehicle use, as DMV already provides the Commissioners with registration information. Our recommendations include General Assembly consideration of new statutes that require DMV to obtain additional vehicle information for use by Commissioners when determining vehicle use.
4. DMV began including new information about the Personal Property Tax Relief Program on its Vehicle Registration Application Renewal Form in October 2000.	DMV has included new information about the Personal Property Tax Relief Program on the renewal form, however, this information does not provide an explanation of what constitutes personal use versus business use vehicles. Without specific information, taxpayers generally do not know what constitutes business use.
5. If DMV started to maintain qualification data on our records, we would be usurping the duties and responsibilities set forth for the Commissioners of the Revenue.	DMV would only provide Commissioners with additional information to assist the Commissioner in determining a vehicle's use. The Commissioners, not DMV, would continue to determine the vehicle use.

COMMONWEALTH of VIRGINIA

Department of Taxation

December 11, 2000

Mr. Glenn Loehr
Audit Director
Office of the Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218

Dear Mr. Loehr:

In connection with your request that the Department of Taxation provide comments regarding the pending study to be issued by your office addressing the Personal Property Tax Relief Act of 1998, as directed by Senate Joint Resolution 127 of the 2000 General Assembly, I offer the following.

As stated in Mr. John Huston's memorandum to you dated December 6, 2000, the Department of Taxation does not believe that it should have a role in the administration of the car tax program. This conclusion has been reaffirmed in light of suggestions that the Department made to you in connection with Mr. Huston's memorandum dated December 6 that have been incorporated within the final report. Namely, the final report includes additional actions (Recommendation 2) that Commissioners and Treasurers must take to obtain certifications of vehicle use during initial registration and each billing cycle.

In addition, this report includes a new suggested recommendation, Number 3, that necessitates certain actions on the part of the Department of Motor Vehicles (DMV) requiring vehicle dealers and leasing companies to certify use of vehicles at registration. While Mr. Huston went further in his memorandum to suggest that certifications might also be obtained annually/biennially through DMV's vehicle registration renewal process, at this point, given your changes to Recommendation 2, DMV's role seems relevant and appropriate.

Through the expanded Recommendation 2 and Recommendation 3 in this report, it appears the needed actions to ensure greater compliance with the business/personal use aspects of the Personal Property Tax Relief Act of 1998, if adopted by the General Assembly, will be in place.

While your report continues to imply that the Department of Taxation can some how use information it receives from the Internal Revenue Service (IRS) to identify taxpayers who claim automobile expenses on Schedule C but fail to report properly to the Local Commissioners and Treasurers, a recent letter received from the IRS in connection with your review seems to indicate otherwise. I have attached a copy of the IRS letter for your reference. In addition, as you are probably aware, the Department of Taxation no longer requires taxpayers to provide a copy of Schedule C with the Virginia Individual Income Tax Return. As a result, I request, as Mr. Huston did in his December 6 memorandum, that you reconsider the role of the Department of Taxation and the attendant Recommendation Number 1, in this report.

I thank you for the opportunity to provide this response, and please let me know if there are further questions.

Sincerely,

Danny M. Payne
Tax Commissioner

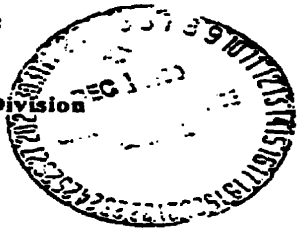
Attachment

c: John H. Huston
Director of Internal Audit

David E. Jordan
Disclosure Officer

Internal Revenue Service

Disclosure Office
Communications & Liaison Division



Department of the Tr[redacted]

P. O. Box 10107
Richmond, VA 23240

Mr. David E. Jordan
Disclosure Officer
Department of Taxation
P. O. Box 1880
Richmond, VA 23218-1880

Person to Contact:
Edwin R. Ward, Jr.
Badge No: 54-CC572
Phone Number:
(804) 916-8385
Refer Reply To:
54-2001-00155
Date:
November 28, 2000

Dear Mr. Jordan:

This letter is in response to your request dated November 20m, 2000, for assistance in obtaining approval for the release of summary statistics using the return information provided to your agency under the provisions of Section 6103(d) of the Internal Revenue Code.

The issue of the use of IRS computer media by state tax agencies to provide statistical summary data to other governmental agencies was the subject of discussion at our recent meeting in Dallas, TX, during the week of November 13, 2000.

The use of IRS returns or return information by state tax agencies under Section 6103(d) is restricted to state tax administration purposes only. Since the vehicle tax in Virginia is not a state tax, the Department of Taxation is precluded by law from using the IRS data to generate the requested statistical summary for the Virginia Auditor for Public Accounts.

I spoke to the state auditor today and informed him of our determination. I understand that he has found some useful information on the IRS Statistics of Income Division website. He may be able to use this information, in conjunction with information from the Department of Motor Vehicles, to estimate the impact of the revenue loss due to the business use by individuals exempted from the vehicle tax.

Mr. David E. Jordan

If you have any questions concerning this matter please call me at the number shown above.

Sincerely yours,

Edwin R. Ward, Jr.
Disclosure Officer

cc: Mary Beth Hawn, Governmental Liaison

COMMONWEALTH of VIRGINIA
Department of Taxation
Office of the Commissioner
Internal Audit Department

DATE: December 6, 2000

TO: Glenn Loehr, Audit Director, Office of the Auditor of Public Accounts

FROM: John Huston/Mike Dorris/David Morrison/Glenn Thacker

SUBJECT: APA Draft Report in Response to Senate Joint Resolution 127 (2000)
MESSAGE:

Glenn –

We appreciate the opportunity to review the above-mentioned report. As we discussed on the telephone, TAX does not believe that it should have a role in the administration of the car tax program. For this reason, including the alternatives outlined below which APA may not have fully considered while developing this report, TAX respectfully requests you eliminate the first recommendation from the report.

Instead, as we discussed, other alternatives should be considered including:

- Having taxpayers indicate/certify as a function of filing the locality annual personal property tax return or on Virginia Form 762, which TAX produces, whether vehicles owned/leased are used for personal or business purposes. As your report indicates, this will require changes on the part of some localities, such as, including a box to check on the personal property tax form, definitions of what is personal versus business use, and language (legal reference) that would indicate to the taxpayer the repercussions of providing false statements.

- Having the Department of Motor Vehicles (DMV) include a box for vehicle owners to check on the annual/biennial vehicle registration form. In addition to indicating the vehicle status (business/personal), material should also be included as part of the vehicle registration packet that defines what constitutes personal versus business uses. Also, as in the case where localities would obtain such information as described above, language (legal reference) should be included that would indicate to the taxpayer the repercussions of providing false statements

on the vehicle registration statement, similar to what I believe is currently done regarding required vehicle insurance. DMV could forward this information to the localities.

- Having localities or DMV cross check information obtained from vehicle owners regarding the use of the vehicle (business/personal) to insurance coverage records maintained by the owner's insurer. I have found insurers that I have dealt with to be very diligent when classifying a vehicle for insurance purposes because of the risk involved.

All things considered, because of the existing role localities and DMV have in the car tax program, the alternatives above seem more relevant, practical and economical to explore than that suggested in the first recommendation in the above-mentioned report.

If you have questions, please contact me at (804) 786-3453.

Thank you.

c: Danny M. Payne
Tax Commissioner

COMMONWEALTH of VIRGINIA
Department of Motor Vehicles
2300 West Broad Street

Richard D. Holcomb
Commissioner

Post Office Box 27412
Richmond, VA 23269-0001
(804) 367-0538

December 11, 2000

MEMORANDUM

TO: Glenn Loehr
Auditor

FROM: Jack Christian
Controller

SUBJECT: Draft Report on PPTRA (SJR 127)

As you requested, the Department of Motor Vehicles and the Department of Taxation have reviewed the draft report on the qualification of business vehicles for personal property tax relief that you plan to provide in response to Senate Joint Resolution 127 from the 2000 General Assembly session.

Enclosed are the responses from both agencies on this draft. Please feel free to contact me at 367-6943 if you have any questions on these responses.

JCC/kec

c: The Honorable Danny Payne
Department of Taxation

Enclosures

FAX: (804) 367-6631 TDD: 1-800-272-9268 E-MAIL: commish@dmv.state.va.us WEB SITE: www.dmv.state.va.us

RESPONSE OF
THE DEPARTMENT OF MOTOR VEHICLES
EXECUTIVE SUMMARY
Auditor of Public Accounts' Personal Property Tax Relief Study

Purpose of Study: SJR 127 (2000) requested the APA to review the extent to which non-qualifying vehicle owners received relief pursuant to the PPTRA.

Study Methodology: The APA used a survey instrument for local governments and interviews with state agencies to gain an understanding of the existing process.

Study Issues: The APA identified two "study issues:"

- How do localities identify vehicles reported as personal use but used primarily for business use, at the time of initial lease or purchase; and
- How do localities identify changes in vehicles' use (between personal and business) from year to year.

Pertinent APA Findings: Using some rather broad and unsupported assumptions, the APA estimates that the cost of providing relief to owners of non-qualifying business vehicles is $7.4 MM annually. The APA appears to assume that 100% of business vehicle owners are inappropriately reimbursed for their business vehicles.

The APA found "no evidence of any on-going effort to inform taxpayers of the business use restrictions in the Act, except when originally registering a vehicle with a Commissioner in a few localities."

"For the most part, the current initial purchasing or leasing process of personal vehicles does not attempt to obtain information about potential business use or inform the purchaser or leaser (*sic*) of the business use restriction."

"The personal property tax billing process also does not provide taxpayers with information concerning the restriction on tax relief."

"The current lack of information on business use makes enforcement of this provision almost impossible. Commissioners and their staff must rely almost solely on observation or limited local information of an individual's business activities."

Proposed Solutions to Findings: The APA offers the following solutions to the issues they identified:

APA proposes a two-fold solution: (a) inform the public about the business use provision and how individuals should comply with the law; and (b) provide Commissioners (local officials) with information that will allow them to enforce the restriction.

DMV and Commissioners need to develop an information campaign that informs vehicle dealers and leasing companies of the need to inform buyers or lessees of the business restriction provisions. Commissioners should provide clearer guidance at the time of decal sale as well as at the time of annual billings or other notifications.

APA recommends that TAX begin collecting vehicle registration and information for anyone claiming a deduction for automotive expenses on Schedule C. The APA recommendation would place enforcement powers for obtaining this information with the Commissioners (local officers).

APA recommends that DMV "alter the registration form and require vehicle dealers and leasing companies to provide information." (See Page 3 of the APA report – this is not included in their findings and recommendations section).

Cost Computation

Using some rather broad and unsupported assumptions, the APA estimates that the cost of providing relief to owners of non-qualifying business vehicles is $7.4 MM annually. The APA appears to assume that 100% of business vehicle owners are inappropriately reimbursed for their business vehicles. The $7.4 MM estimate of the cost of improper reimbursement for business vehicles may be too high.

Organization of the Report

Although the report has a "Findings and Recommendations" section, the report has finding in other places in the report. Suggest that the report consolidate all findings and recommendations in one section.

Overriding Issues

Under the PPTRA, the local Commissioners are responsible for assessing tax on all vehicles, and for making the final determination of whether vehicles qualify under the plan. The APA suggestions would spread the responsibility for information gathering from the local-elected officials to DMV and TAX. Specifically, DMV would be required to change its registration process to capture and more fully explain business vs. personal use, and TAX would be required to create a new form, administer it, and remit the information received to local-elected officials.

Given that local-elected officials are responsible for qualifying vehicles, and could more fully discharge these duties by changes to the annual return that all vehicle owners file with their locality, it appears that with the DMV and TAX suggestions, the APA is creating two new bureaucracies that may be unnecessary. TAX is gaining a significant new responsibility for a form and sending paper information (in and of itself inefficient and not in keeping with the Governor's e-business emphasis, since localities would have to have the manpower to key in information from these forms in order for it to be of any use to them). One could argue that this is a significant departure from TAX's core business function, the administration and collection of general fund revenue sources. One could also argue that this is a significant new burden on taxpayers, who would likely not welcome yet another tax form to fill out annually.

Since DMV has a significant number of two-year registrations, the registration process is also not the most accurate method of capturing this information. Also, information to DMV, like all other tax information reported in this state, is on a self-reporting basis, and is likely not subject to any more (or less) honesty than reporting is currently.

Recommendation to create an informational campaign:

- DMV already has several initiatives either in place or in progress that address this recommendation:
    - DMV began including new information about the Personal Property Tax Relief Program on its Vehicle Registration Renewal Application Form in October, 2000:

"Your vehicle may qualify for tax relief, up to the first $20,000 of value under Governor Jim Gilmore's historic Personal Property Tax Relief Act, enacted by the General Assembly. Qualifying vehicles include passenger vehicles, motorcycles, and pickup and panel trucks with a gross weight of less than 7,501 pounds ***used for personal use*** (emphasis added). Tax relief is 100% for vehicles valued $1,000 or less. For vehicles valued over $1,000, tax relief is 70% in 2001 and 100% in 2002 on the first $20,000 in assessed value. Contact your local Commissioner of the Revenue to determine if your vehicle qualifies."

- The information includes a brief recap about the tax relief program and advises the vehicle's owner to contact their local Commissioner of the Revenue to determine if their vehicle qualifies.

The language makes it clear that the way a vehicle is used factors into a qualifying decision related to tax relief. It also instructs the vehicle owner to contact their local Commissioner of the Revenue if they have questions regarding the qualification of their vehicle.

- Since 1998, DMV has carried a "No Car Tax " banner on our website (dmv.state.va.us). Anyone visiting DMV's site can click on this banner and be taken to information regarding the tax relief program, how it is administered, and the vehicle use criteria that determine whether a vehicle qualifies:

  "In general, a qualifying vehicle (Va. Code Section 58.1-3523 and 3525) is determined by the Commissioner of the Revenue (COR) of the county, city, or town where the vehicle is garaged. In order to qualify for the tax relief, the motor vehicle must be owned or leased by a natural person and be used for nonbusiness purposes." (*Source, DMV Web Page*).

- DMV believes that any additional educational efforts should be implemented by the Commissioners of the Revenue Association and/or individual Commissioners of the Revenue since that PPTRA statute clearly gives them the ultimate authority in making qualification decisions.

Recommendation to alter the DMV vehicle registration form

- DMV would be reluctant to alter our current vehicle registration form to capture any information from vehicle owners, dealers, and leasing companies regarding vehicle use for the following reasons:

  - Leasing companies by statute are already required to provide DMV information on which leased vehicles potentially qualify for tax relief because they are used predominantly for personal use. This data is made available to the Commissioners of the Revenue on a monthly basis to assist them in their qualifying decisions.

  - The PPTRA statute does not require dealers to submit any information related to vehicle use for purposes of qualification for personal property tax relief.

  - All data collected as part of a vehicle titling and registration process (either done at DMV or at an on-line dealer location) is self reported by the vehicle owner. If the application was modified to collect a self-report of vehicle use, there is no way to verify that the information is accurate.

  - Under PPTRA, there is no statutory requirement for a citizen to report any information to any governmental entity in order to comply with the Act. There are no statutes which require citizens to provide DMV with data on vehicle use or to notify DMV if vehicle use changes during the registration period.

  - Vehicle registrations can cover a two-year period. Thus, if DMV did collect and store vehicle use data collected at the time of registration, it might not be accurate for both of the tax years covered by the registration period.

  - If DMV started to maintain qualification data on our records, we would be usurping the duties and responsibilities set forth for the Commissioners of the Revenue under Va. Code §58.1-3526.

  - If DMV were to add qualification data on our records provided to us by the Commissioners of the Revenue, the data would be one year old before it was ever posted to our vehicle records. Currently, localities submit data on individual vehicles qualifying for tax relief by March of each year and that data is for the preceding tax year.

COMMISSIONERS OF THE REVENUE ASSOCIATION

"Elected To Serve"
P.O. Box 389
Franklin, VA 23851

December 7, 2000

Mr. Glenn Loehr
Commonwealth of Virginia
Auditor of Public Accounts
P. O. Box 1295
Richmond, Virginia 23218

DEC 11 '00 AM10:18

Dear Mr. Loehr:

In response to the draft copy of the study dealing with the Personal Property Tax Relief Act of 1998, I find it to be an honest and fair attempt to report your findings. I trust the Commissioners of the Revenue statewide were helpful in responding to the survey regarding the processes that our offices use to capture information for PPTRA.

My concern is the added cost that could be associated with obtaining the necessary information requested in the report for the Commissioners of the Revenue. I feel that for PPTRA to be uniform statewide, every taxpayer would have to be contacted by phone, mail or in person to ensure equity. It would also require most localities to change their personal property forms and bills to capture the necessary information required.

The Commissioners of the Revenue will do whatever it takes to get this accomplished not only for our localities to receive their fair share but to ensure that vehicles are taxed in a uniform manner in accordance to the Personal Property Tax Relief Act. However, it will cost funds that I am sure most localities would not be able to incur.

If I can be of further assistance, please let me know.

Very truly yours,

Brenda B. Rickman

Brenda B. Rickman
President