

The Way We Tax: Utah's State and Local Tax System

Prepared for:

Utah Legislature
“Bagels and Briefings”

February 12, 2013

Presentation Outline

- Tax Policy Overview
- Utah's Comparative State & Local Tax Burden
- Income Taxes
- Sales & Use Taxes
- Property Tax
- Fuel Taxes

Tax Policy: Why Does it Matter?

Tax Policy – Why Does it Matter?

- It's not only the amount of revenue that matters, but also how you get it
- Sound tax policy is concerned with how taxes:
 - Are designed and administered
 - Affect the taxpayer
 - Affect the economy
- Tax policy affects every citizen of Utah
- Tax policy provides revenue that funds state and local public services

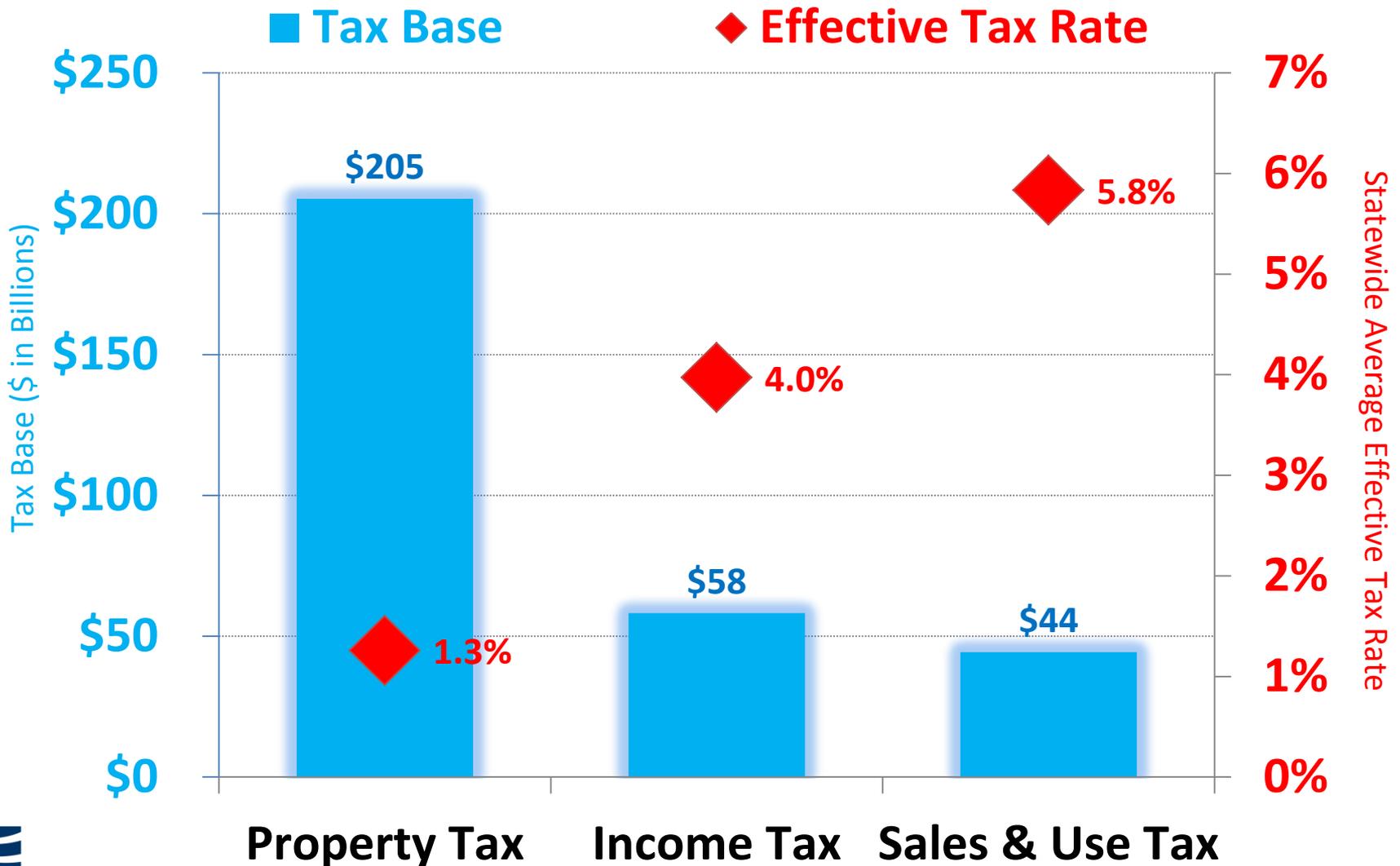
Elements of an Optimum Tax System

- **Reliable**
 - Sufficient
 - Stable
 - Certain
- **Equitable**
 - Vertical Equity
 - Horizontal Equity
- **Simple**
 - For taxpayers to pay
 - For tax collectors to collect
- **Responsive to interstate and international competition**
- **Economically neutral**
- **Accountable and transparent**

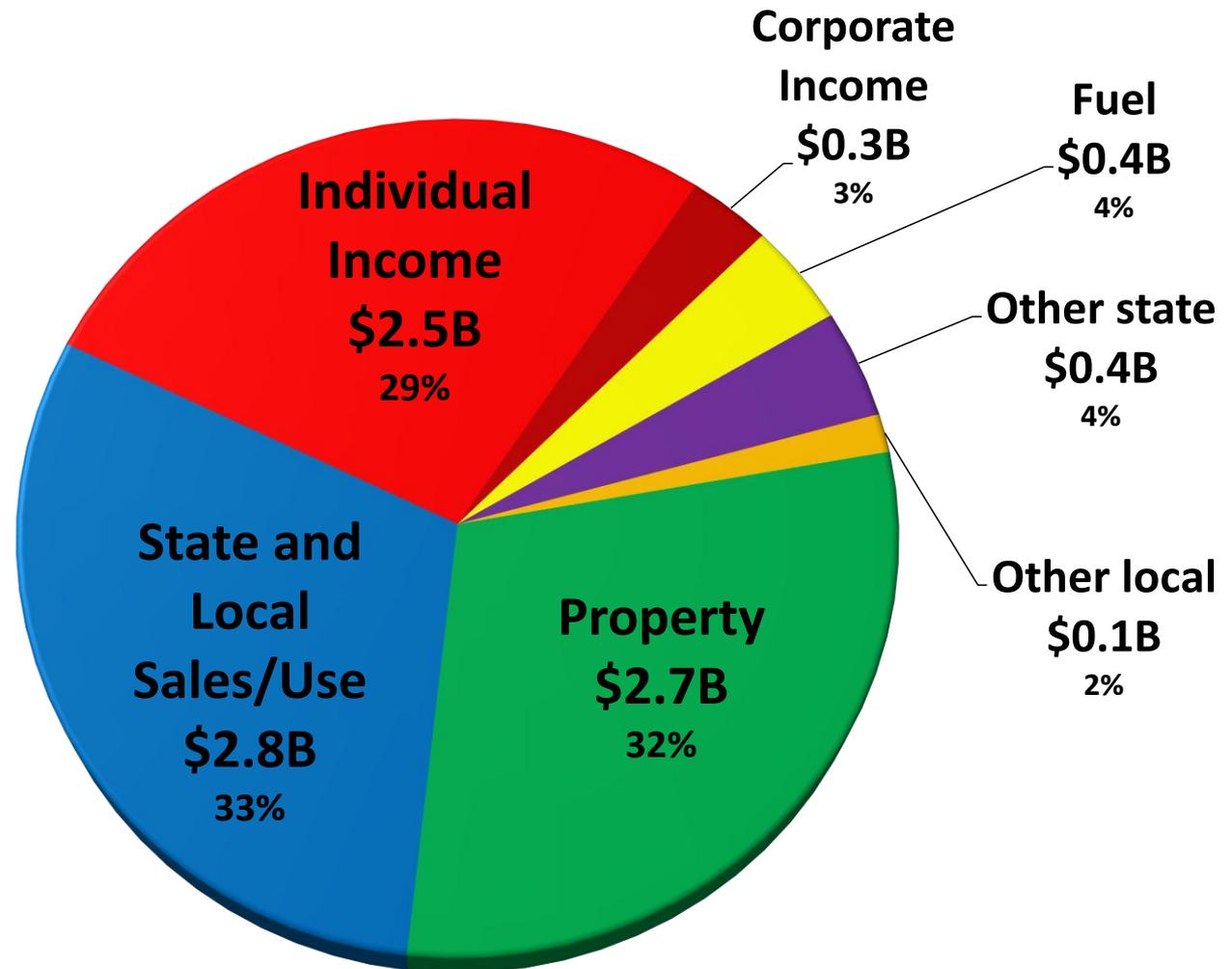
Taxation 101

$$\text{Base} * \text{Rate} = \text{Revenue}$$

Utah Tax Base & Effective Tax Rates

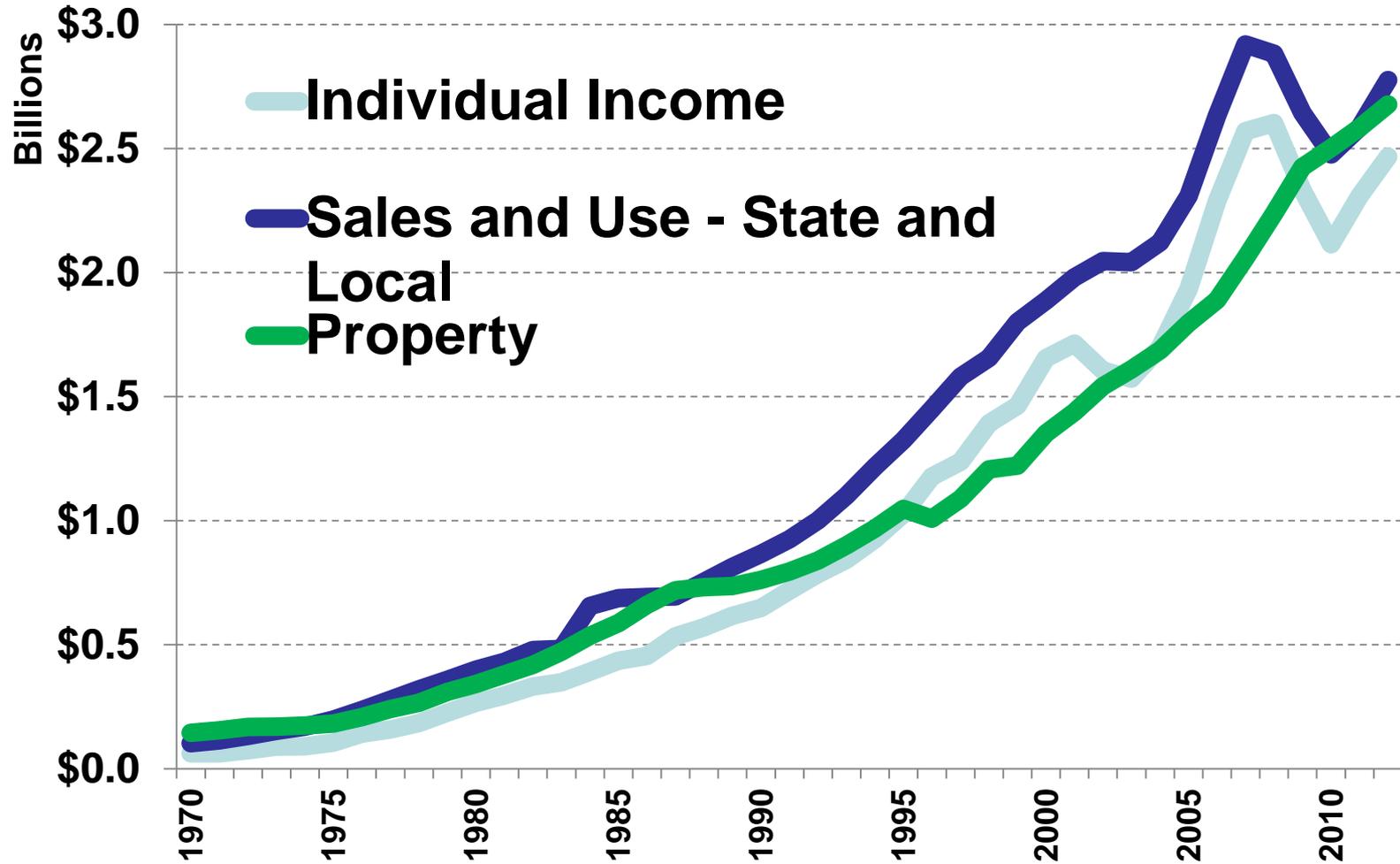


Utah's Three Major State and Local Taxes: Income, Property, and Sales & Use Tax Revenues FY 2012

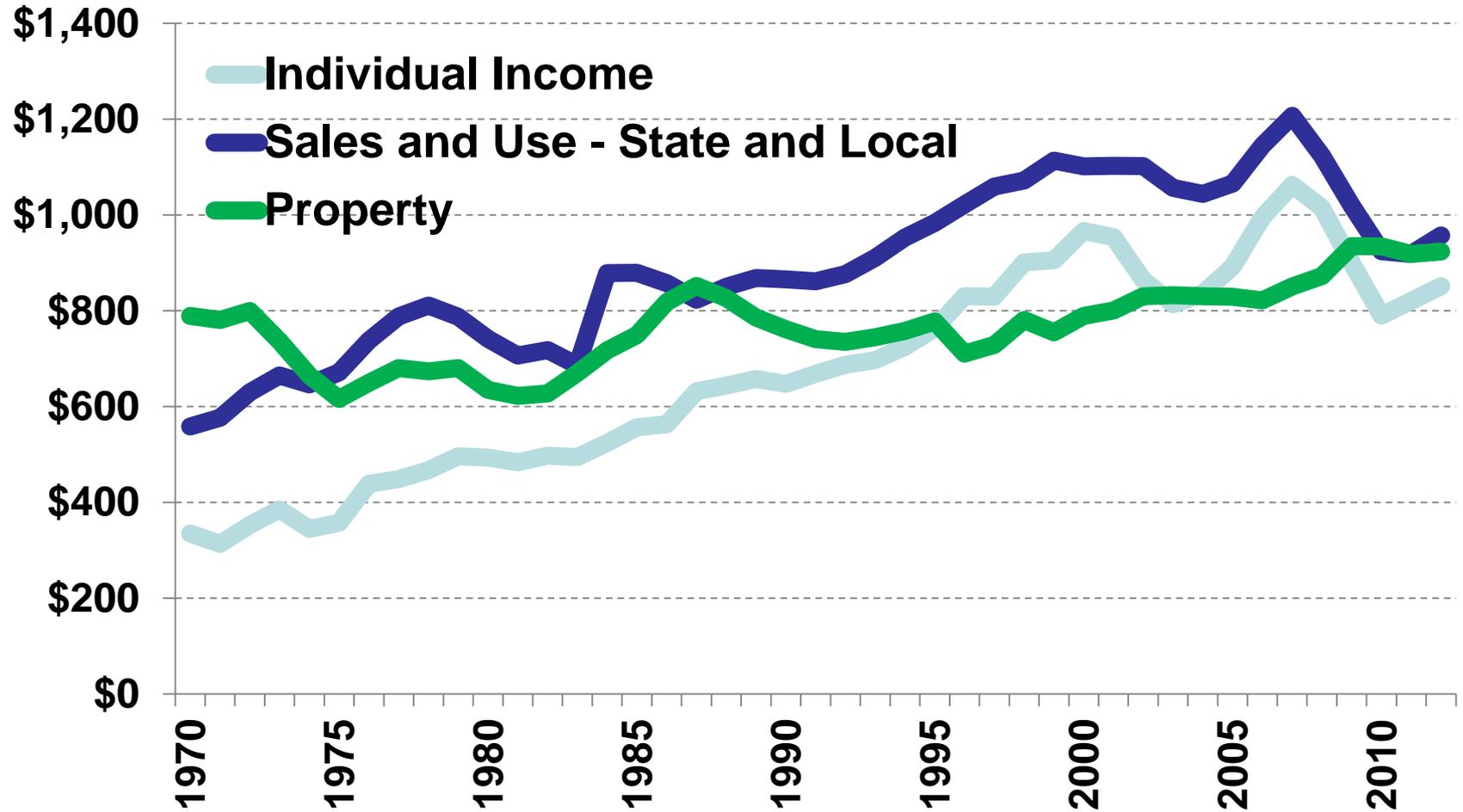


State and Local Sales & Use, Individual Income, and Property Tax Revenues

FY 1970 to FY 2012

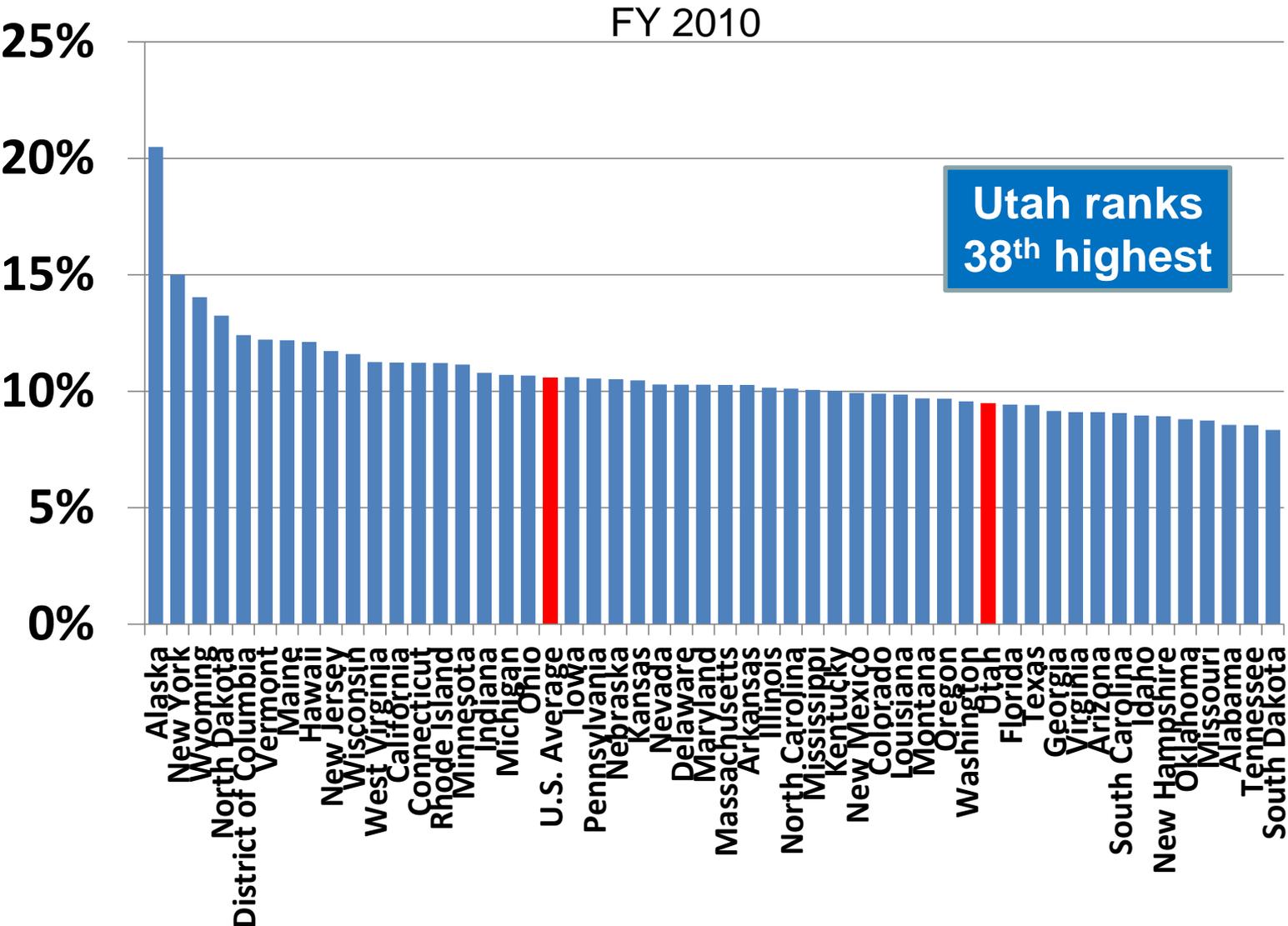


Real Per Capita State and Local Sales & Use, Individual Income, and Property Tax Revenues FY 1970 to FY 2012



Utah's State and Local Tax Burden: How Does It Compare?

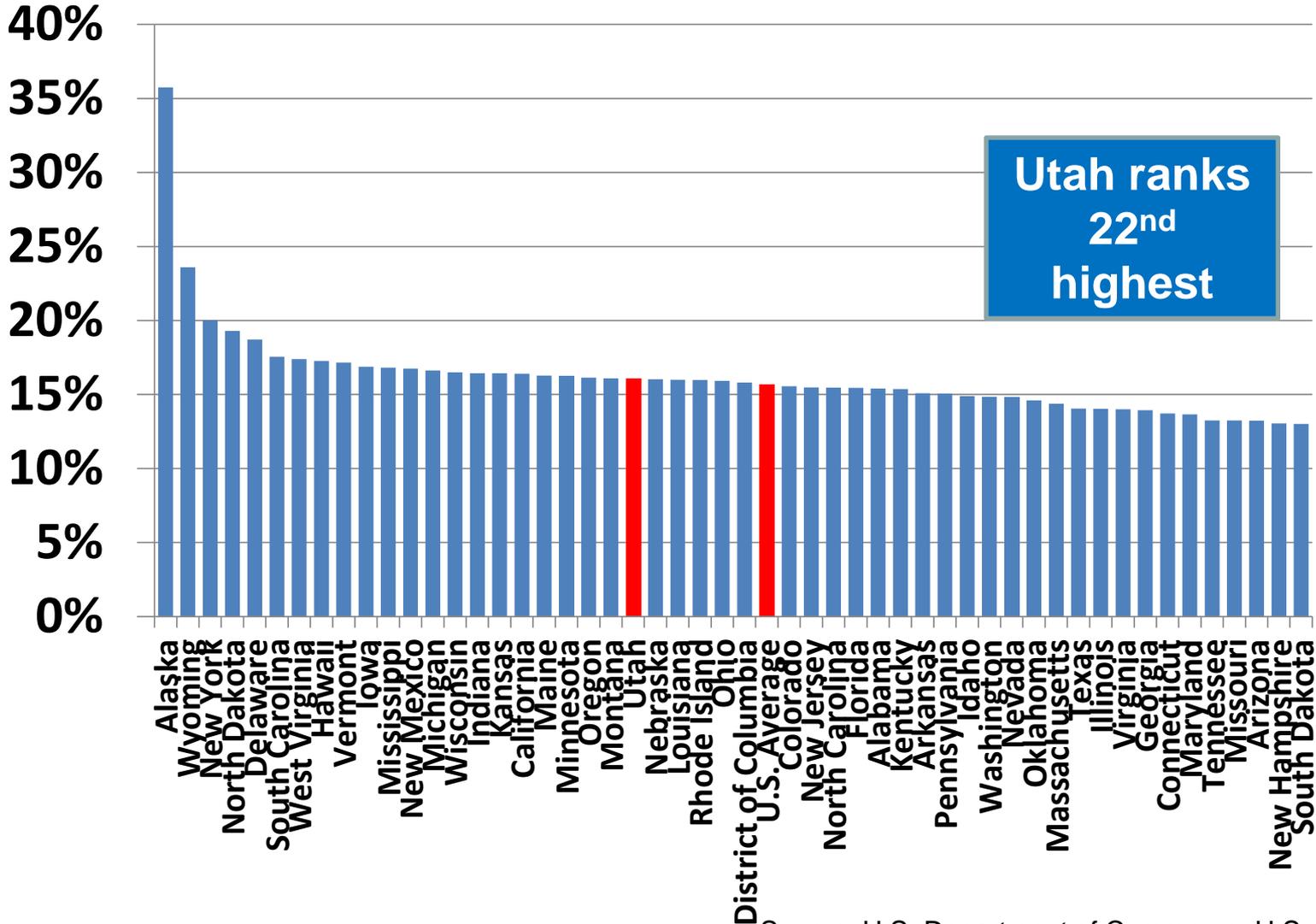
State and Local Taxes as a Percent of Personal Income



Source: U.S. Department of Commerce, U.S. Census Bureau

State and Local Total Own Source Revenue as a Percent of Personal Income

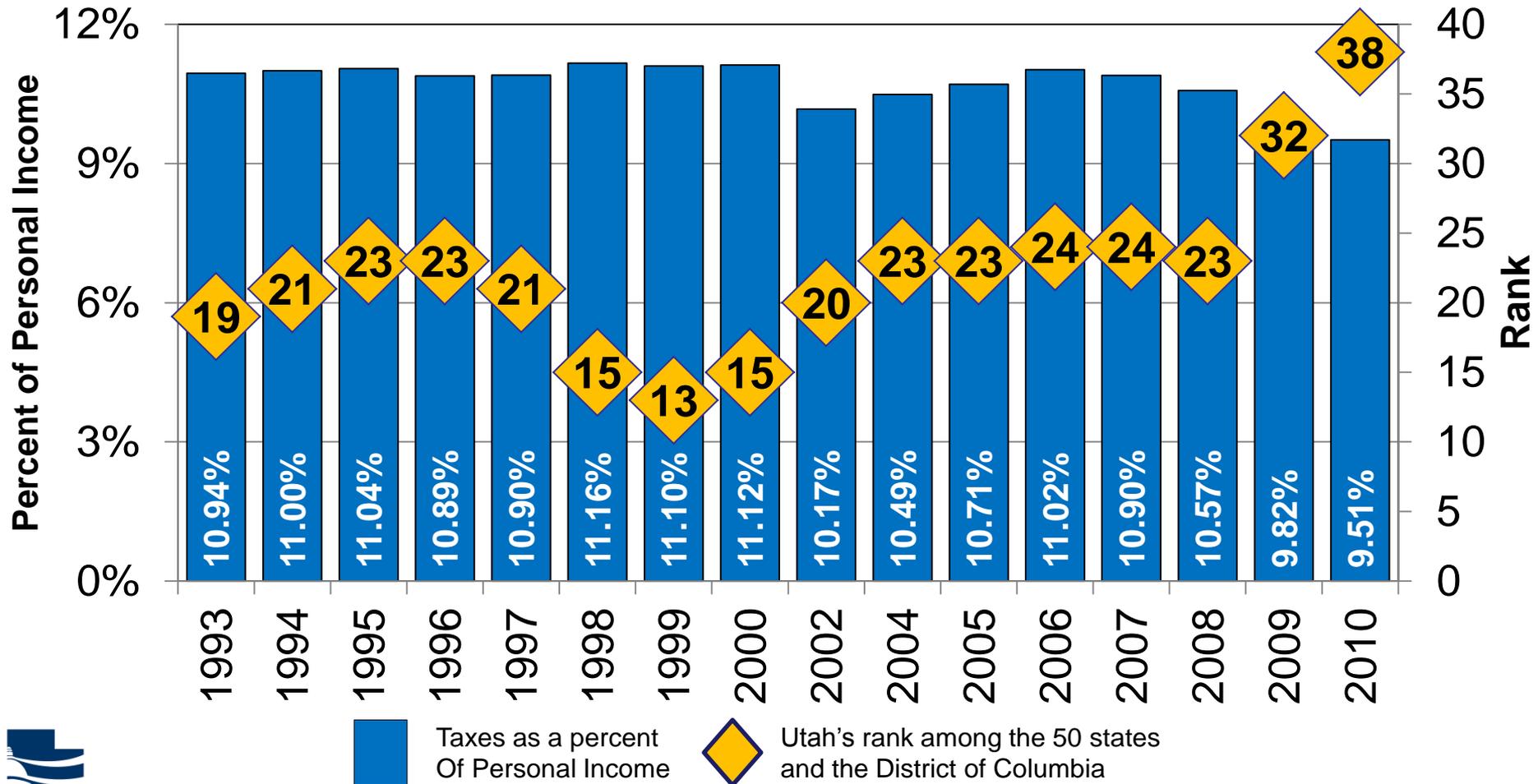
FY 2010



Source: U.S. Department of Commerce, U.S. Census Bureau

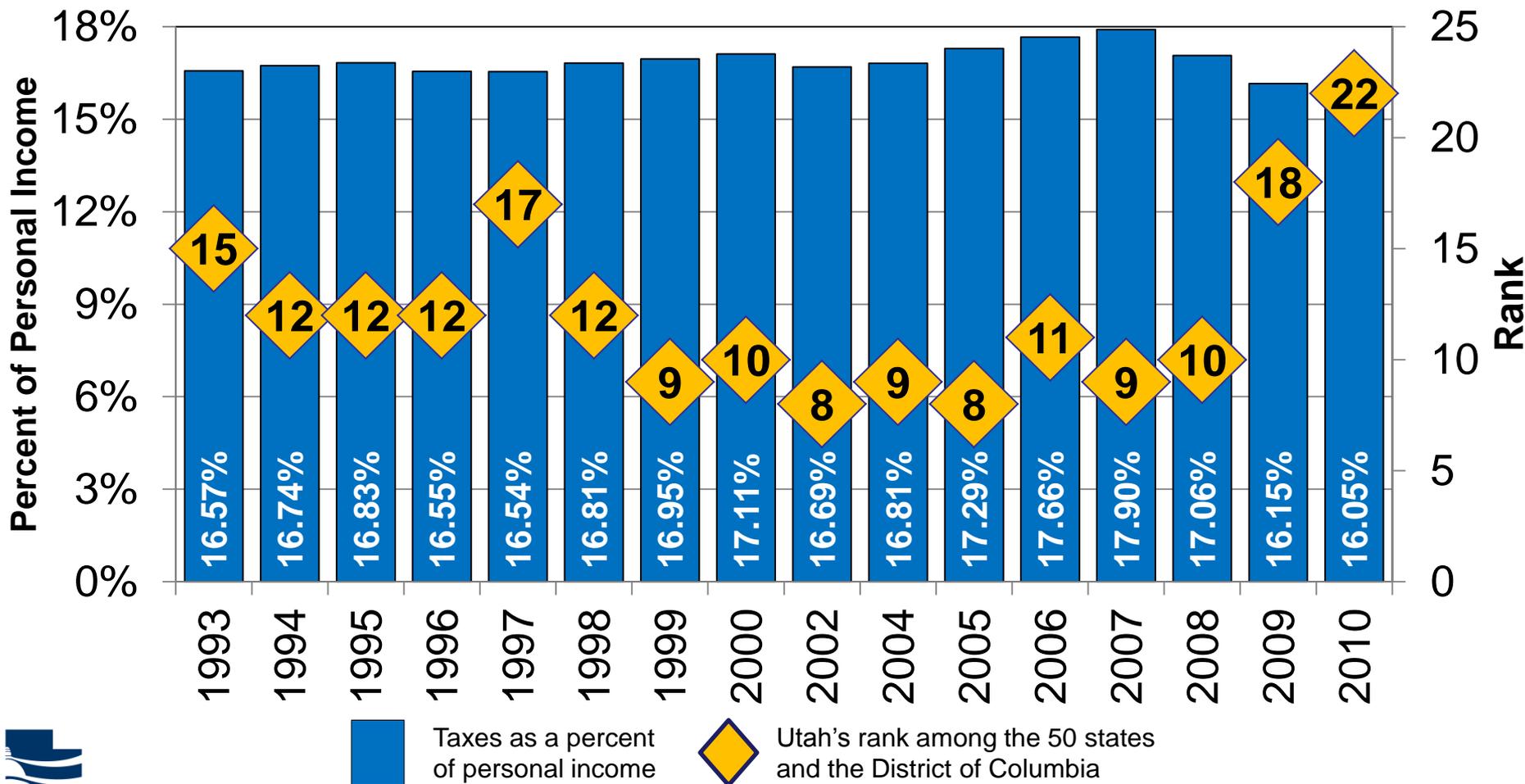
State and Local Taxes as a Percent of Personal Income

Utah: FY 1993 to FY 2010

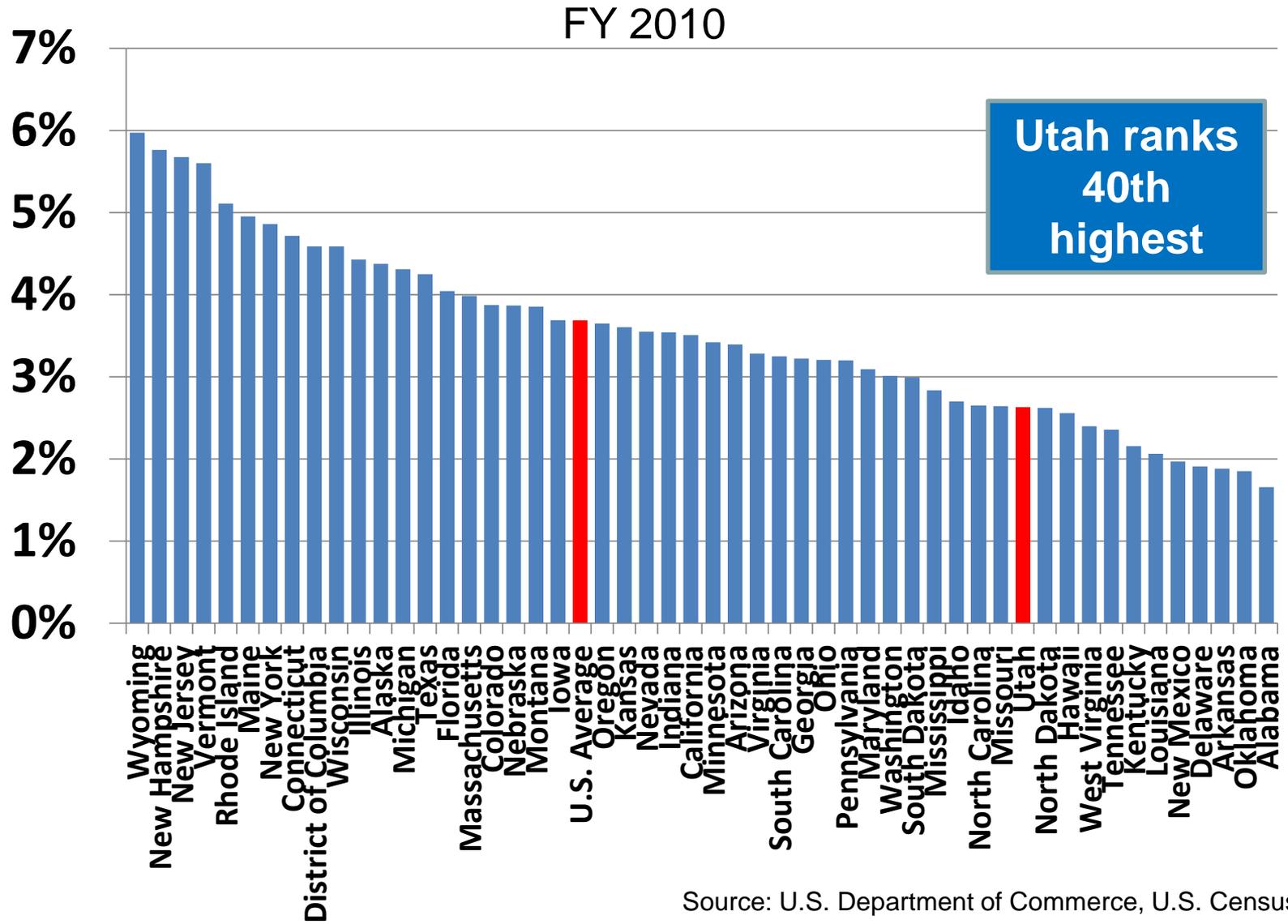


State and Local Total Own Source Revenue as a Percent of Personal Income

Utah: FY 1993 to FY 2010

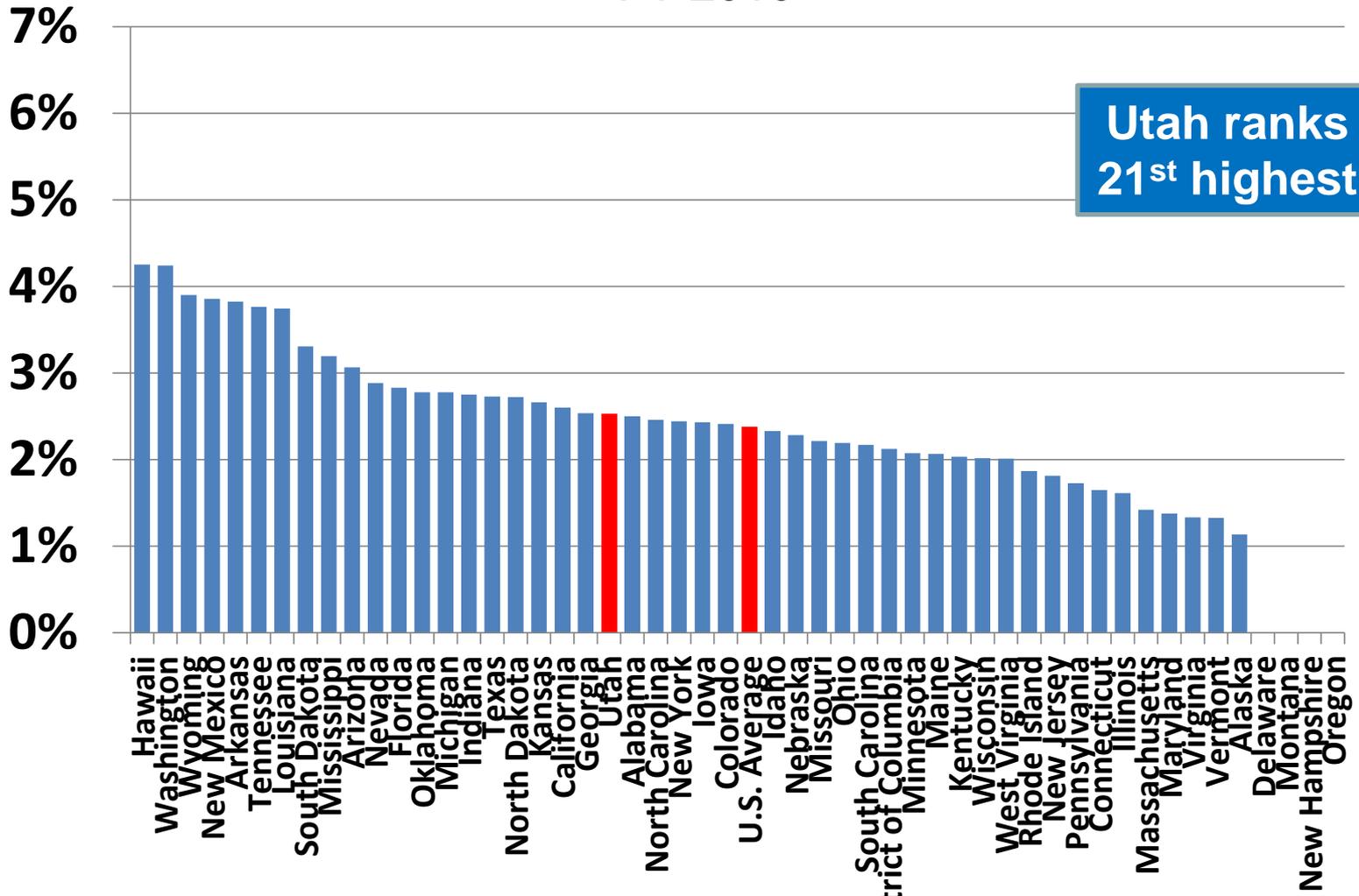


State and Local Property Taxes as a Percent of Personal Income



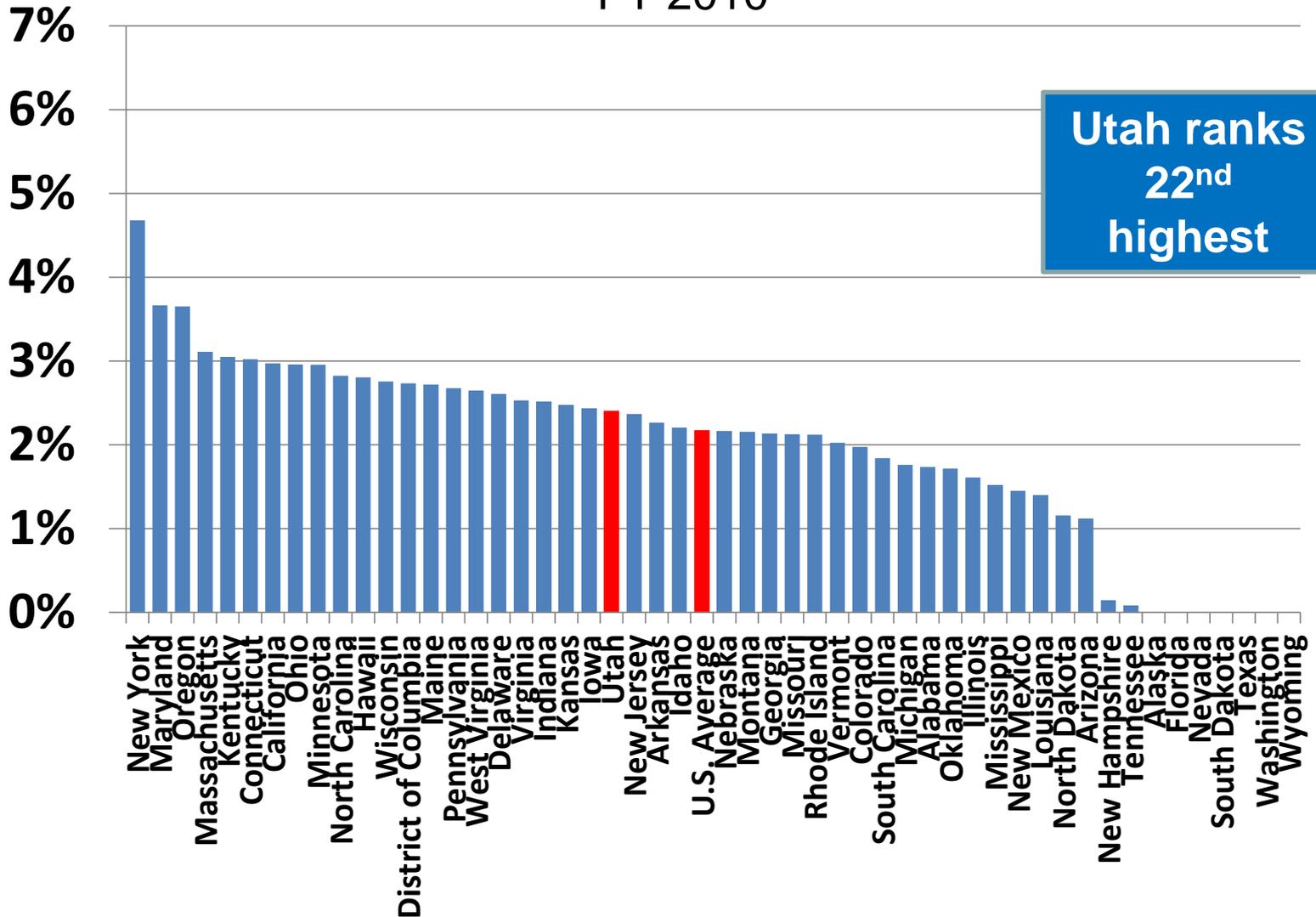
State and Local General Sales Taxes as a Percent of Personal Income

FY 2010



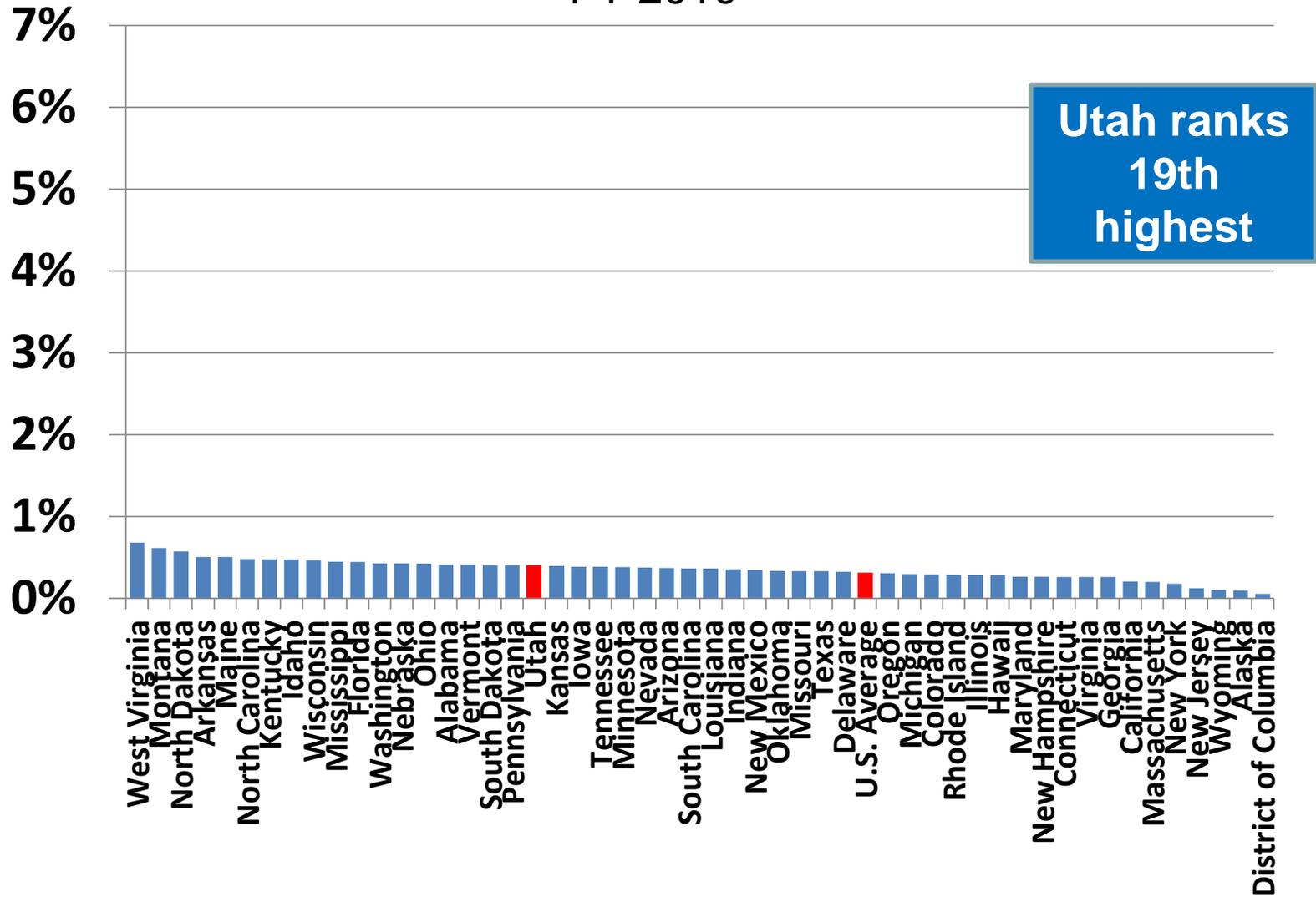
State and Local Income Taxes as a Percent of Personal Income

FY 2010



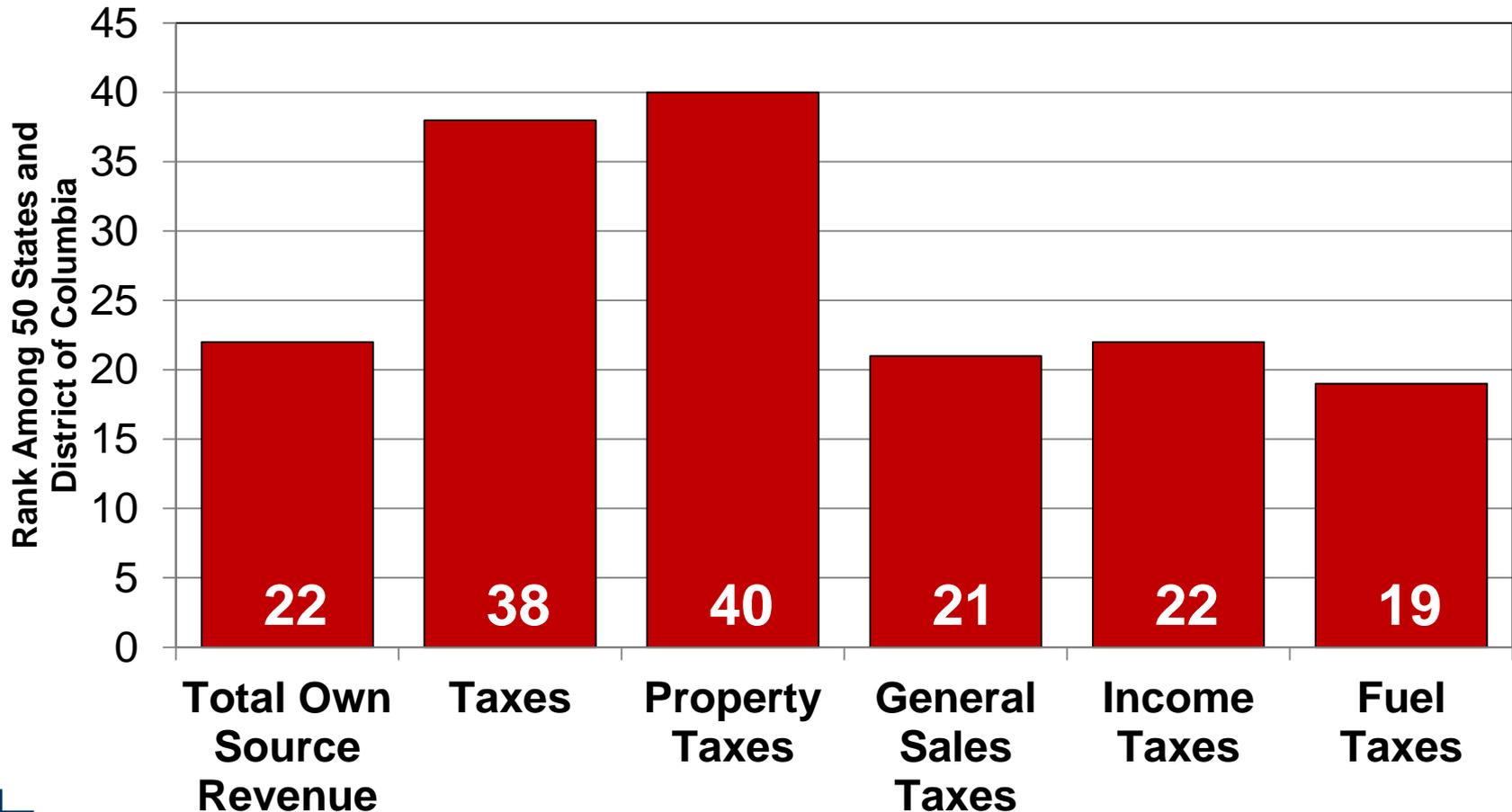
State and Local Fuel Taxes as a Percent of Personal Income

FY 2010



How Utah Compares

Utah Taxes and Own Source Revenue as a Percent of Personal Income: FY 2010



Income Taxes

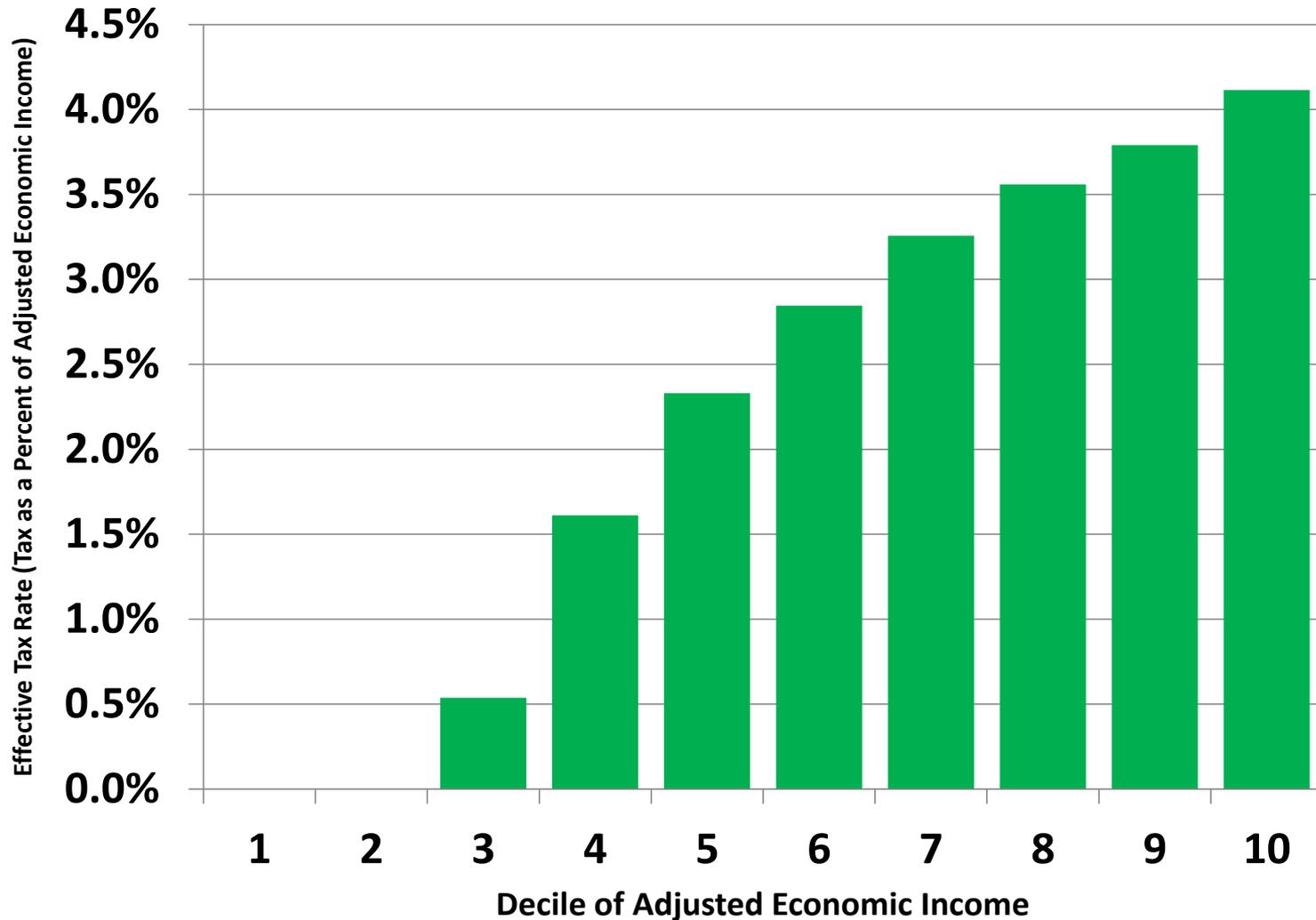
Utah's Single Rate Individual Income Tax

- New system took effect tax year 2008
- Single statutory tax rate of 5% applied to state taxable income
 - Start at federal adjusted gross income (AGI) with certain additions and subtractions
- Several tax credits that phase out as income increases
 - Taxpayer tax credit – phaseout 1.3%
 - Retirement tax credit – phaseout 2.5%

Effect of Recent Income Tax Changes

- Despite “flat tax” moniker, overall the new system is moderately progressive with respect to AGI
 - Basic Tax Formula
 - $(\text{Tax base} \times \text{tax rate[s]}) - \text{tax credit} = \text{tax liability}$
 - Old system – progressive through **tax base** and **tax rates**
 - New system – progressive through **tax credits**
- Briefing papers available summarizing major tax changes and impacts (visit le.utah.gov)
- Withholding changes altered the timing of income tax collections

Utah's Income Tax System Remains Progressive



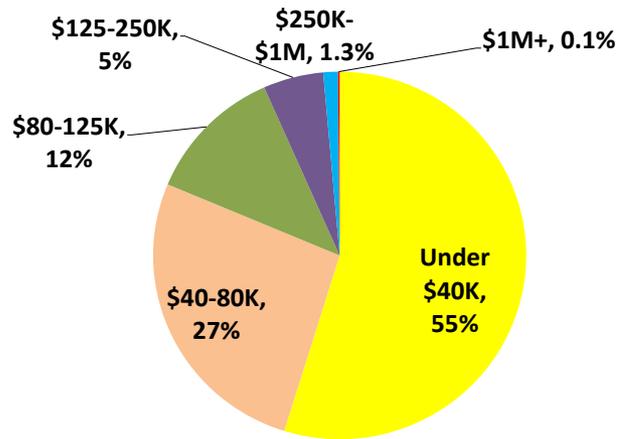
Distribution of Returns, AGI, and Utah Tax Tax Year 2010

	% of Returns	% of Exemptions	% of Income (AGI)	% of Utah Income Tax
less than \$40K	55%	43%	14%	8%
\$40-80K	27%	32%	29%	26%
\$80-125K	12%	16%	23%	25%
\$125-250K	5%	7%	16%	19%
\$250K-\$1M	1.3%	1.8%	10%	12%
\$1M+	<u>0.1%</u>	<u>0.2%</u>	<u>8%</u>	<u>9%</u>
	100%	100%	100%	100%

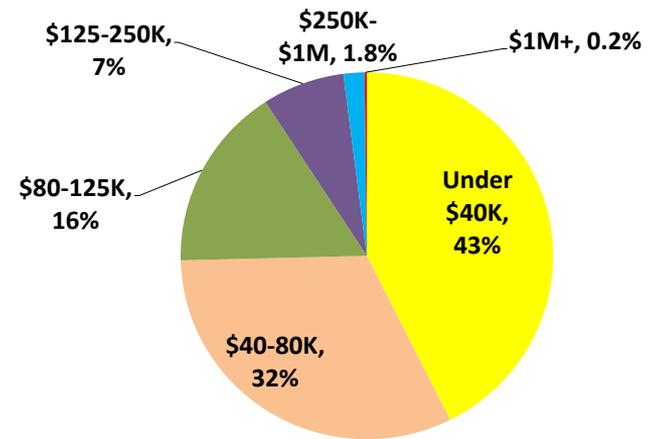
Individual Income Taxes by AGI Class

Tax Year 2010 Full Year Residents

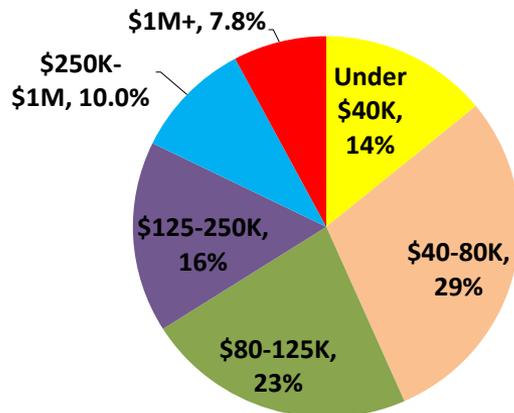
Returns



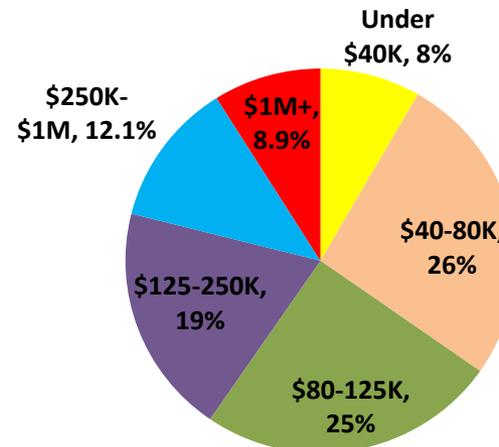
Exemptions



Income (AGI)



State Income Tax

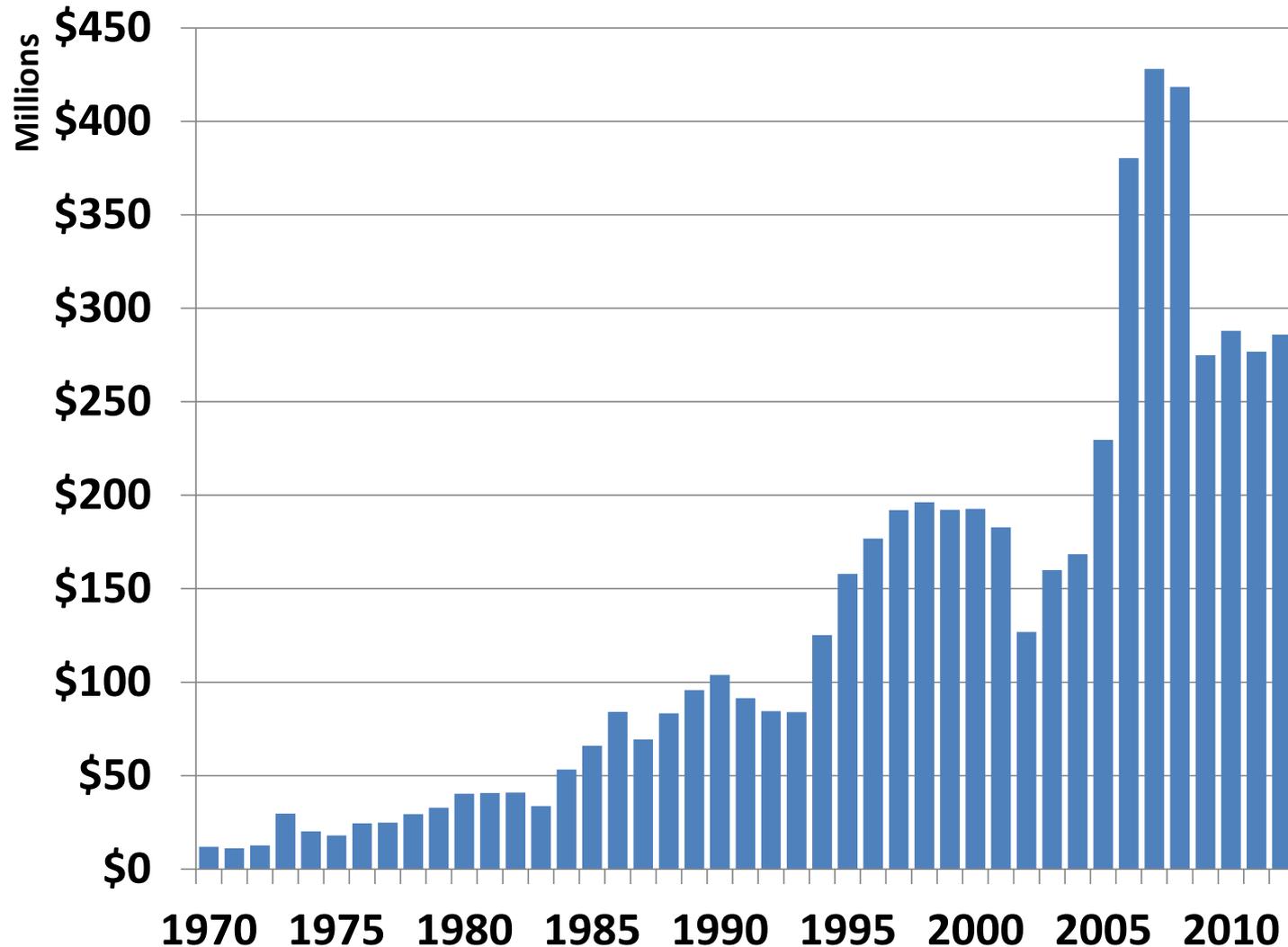


Why Does the Individual Income Tax Matter?

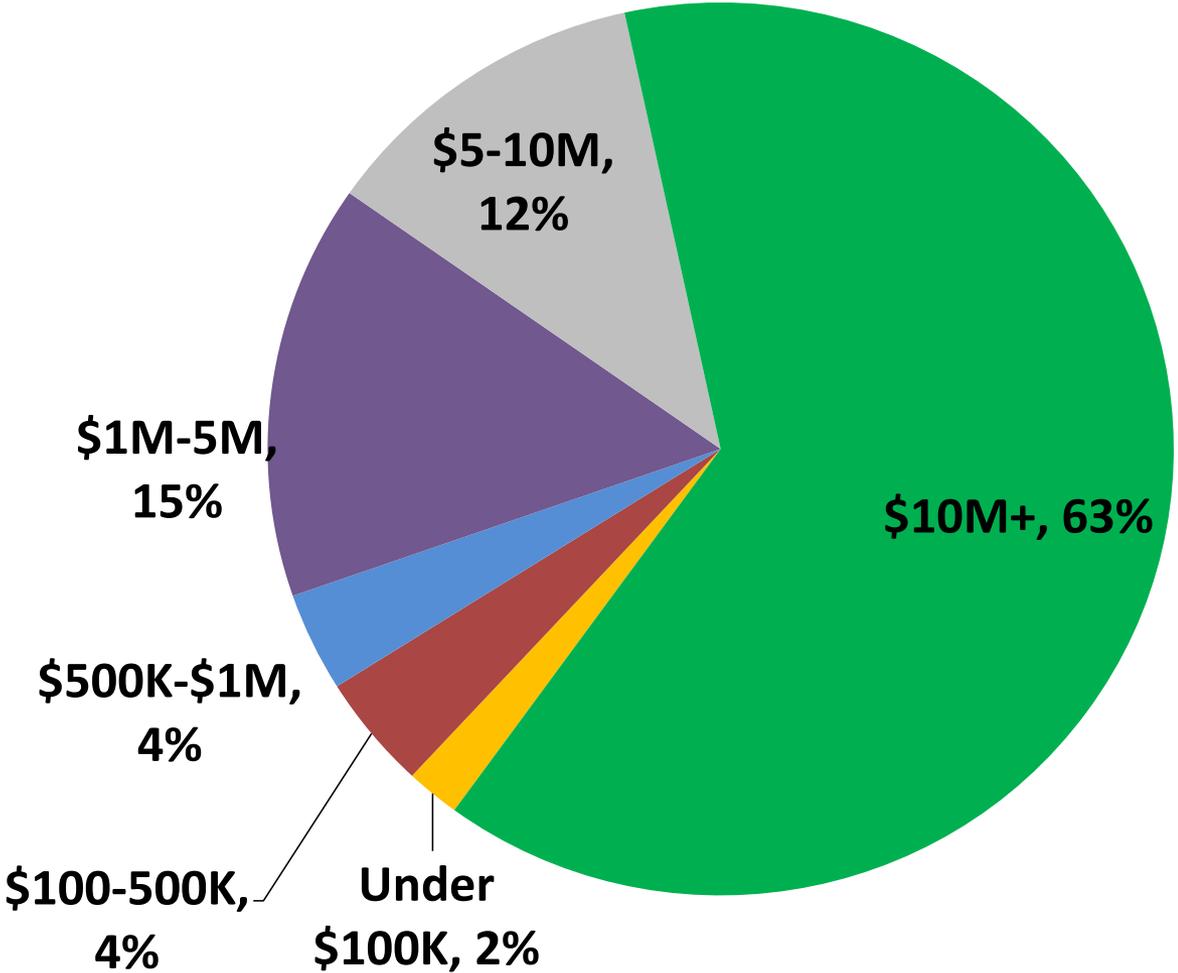
- Constitutionally earmarked revenue for public education and higher education
- Greatest ability to adjust for current ability to pay and offset regressivity of other taxes
- Most detailed information on taxpayers
- Visible
 - \$ withheld from paychecks
 - Annual tax return
- Tax on Income
 - Individuals
 - “Pass-through” business entities
 - Trusts and estates

Corporate Franchise & Income Tax Revenues

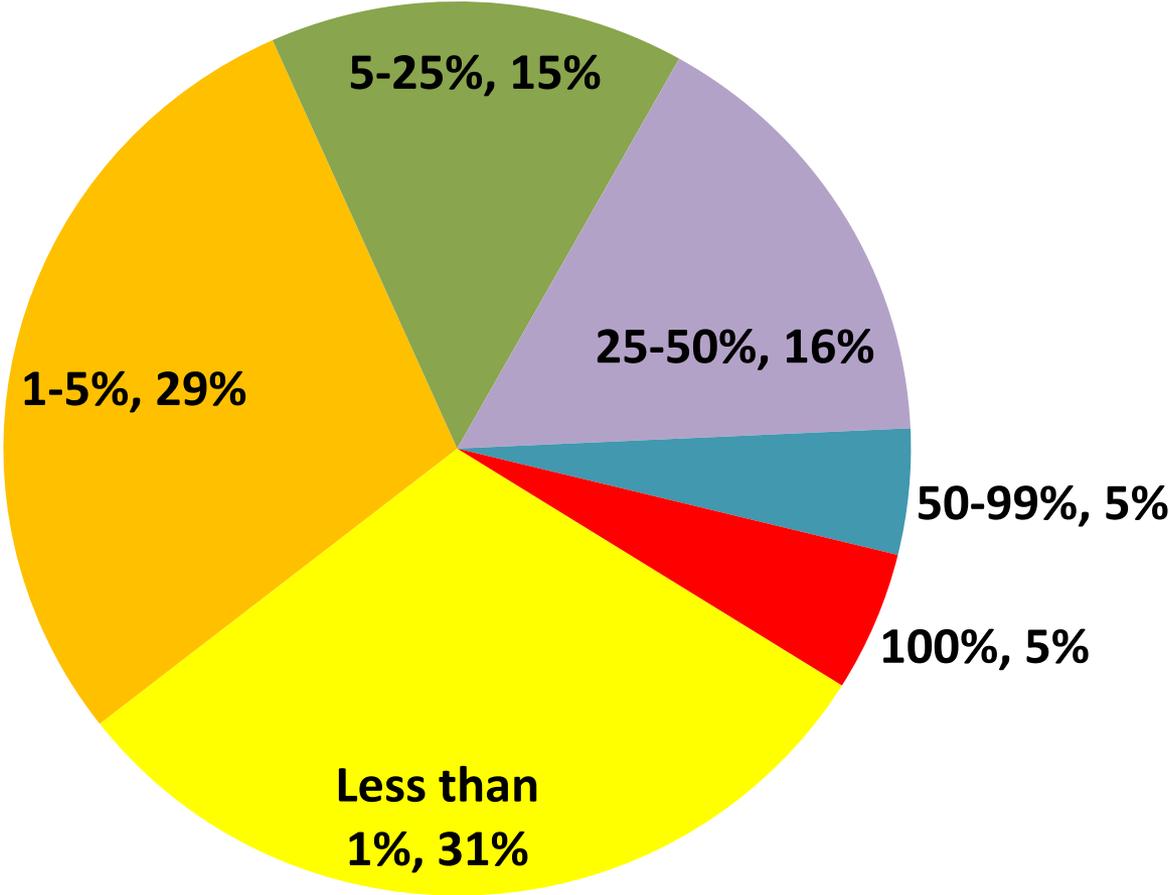
FY 1970 to FY 2012



Corporate Franchise & Income Tax Revenue by Utah Net Taxable Income, Tax Year 2010



Corporate Franchise & Income Tax Revenue by % of Business in Utah, Tax Year 2010



Why Does the Corporate Franchise & Income Tax Matter?

- Constitutionally earmarked revenue for public education and higher education
- Volatile revenues
- Tax on income
 - Generally C-corporations

Sales & Use Taxes

The Utah Sales and Use Tax Base: What Do We Tax?

Key transactions subject to tax include:

- Retail sales of tangible personal property
- Sales of certain telecommunication services, utility services, or passenger service (reduced rate may apply)
- Sales of food (reduced rate may apply)
- Certain admissions, such as movie tickets
- Certain services, such as cleaning and repair of tangible personal property
- Certain hotel or motel charges
- Products transferred electronically
- “Use tax”

The Utah Sales and Use Tax Base: What Don't We Tax?

- Some transactions are not specifically exempt from sales and use taxes but are not part of the tax base, such as professional services or personal care services
- Other transactions are specifically exempt from sales and use taxes
 - Currently 74 exemptions
 - Estimated FY 2011 state revenue effect: \$343 Million

The Utah Sales and Use Tax Base: What Don't We Tax?

Some examples of major sales and use tax exemptions include:

Exemption

FY 2011 State Impacts

Motor, special, aviation fuels	\$ 98 M
Manufacturing machinery & equipment	\$ 91 M
Prescription drugs	\$ 46 M
Resale property / component parts	\$ 19 M
Sale of natural gas, electricity, coal, etc. for industrial use	\$ 19 M
Food stamps & WIC	\$ 7 M
Certain religious / charitable sales & purchases	\$ 6 M
Farm machinery & equipment	\$ 6 M

State and Local Option Sales and Use Tax Rates

State tax rate +

Sum of local option tax rates where transaction occurs

Total tax rate imposed on a transaction

- The state tax rate depends on what is being taxed

For example:

General state tax rate (includes prepared food)	4.70%
Residential fuels tax rate	2.00%
Food and food ingredients tax rate	1.75%

Local Option Sales and Use Tax Rates

- Counties, cities, and towns are allowed to impose a variety of local option sales and use taxes
- Most local option sales and use taxes tax the same transactions taxed at the state level
- Some local option sales and use taxes may be used for general fund purposes

For example:

Local sales and use tax	1.00%
County option sales and use tax	0.25%

Local Option Sales and Use Tax Rates

- Other local option sales and use taxes may only be used for purposes specified in statute

For example:

Public transit tax (funds system for public transit)	up to 0.30%
County “ZAP” tax (“zoo, arts, and parks tax”)	0.10%

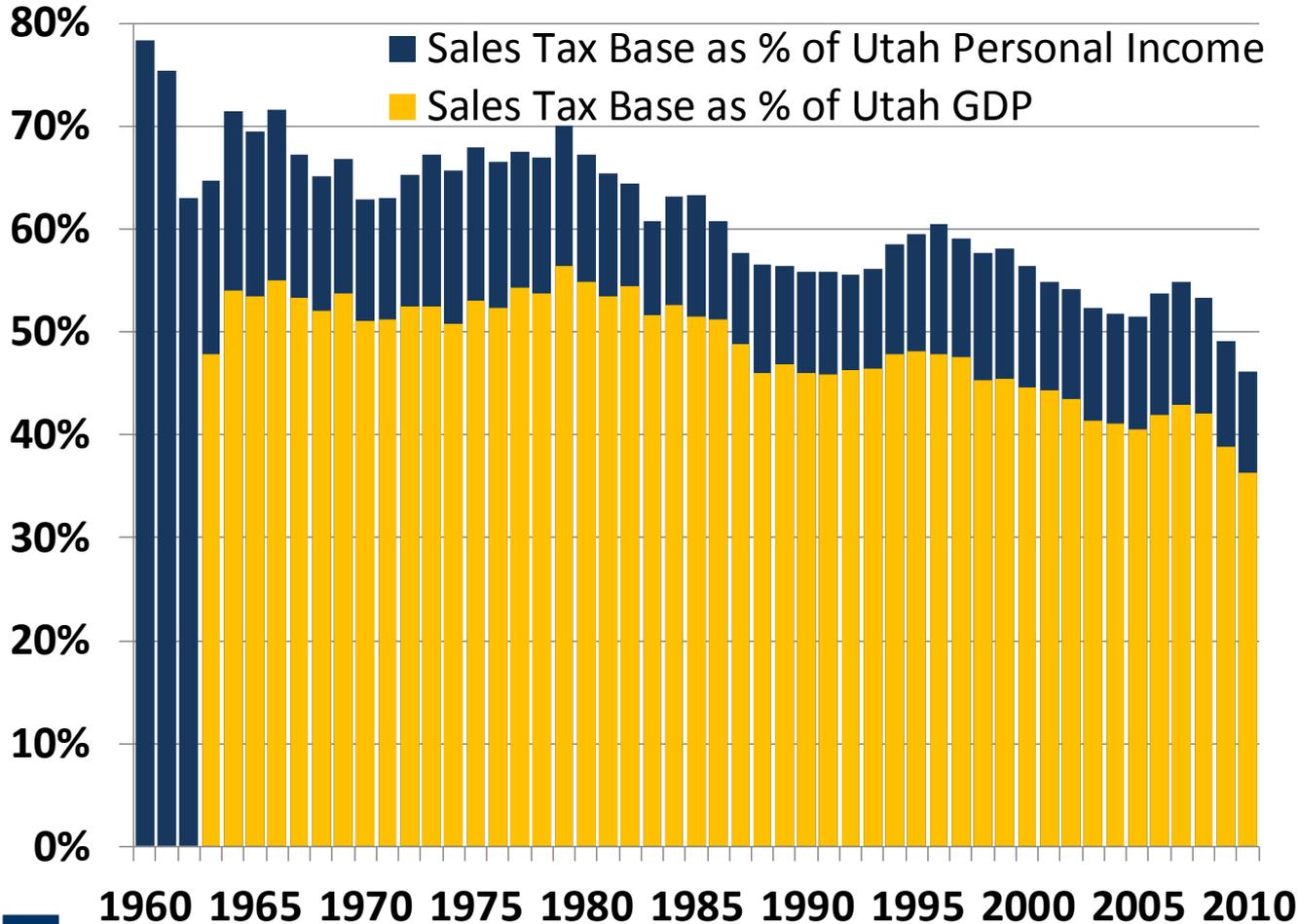
- Some local option sales and use taxes are imposed only on certain transactions, such as vehicle rentals, hotel or motel charges, or prepared food

For example:

County transient room tax on hotel / motel charges	up to 4.25%
County tax on food sold by restaurants (“TRCC tax”)	up to 1.00%

Sales & Use Tax Base

Gross Taxable Sales as a % of Personal Income



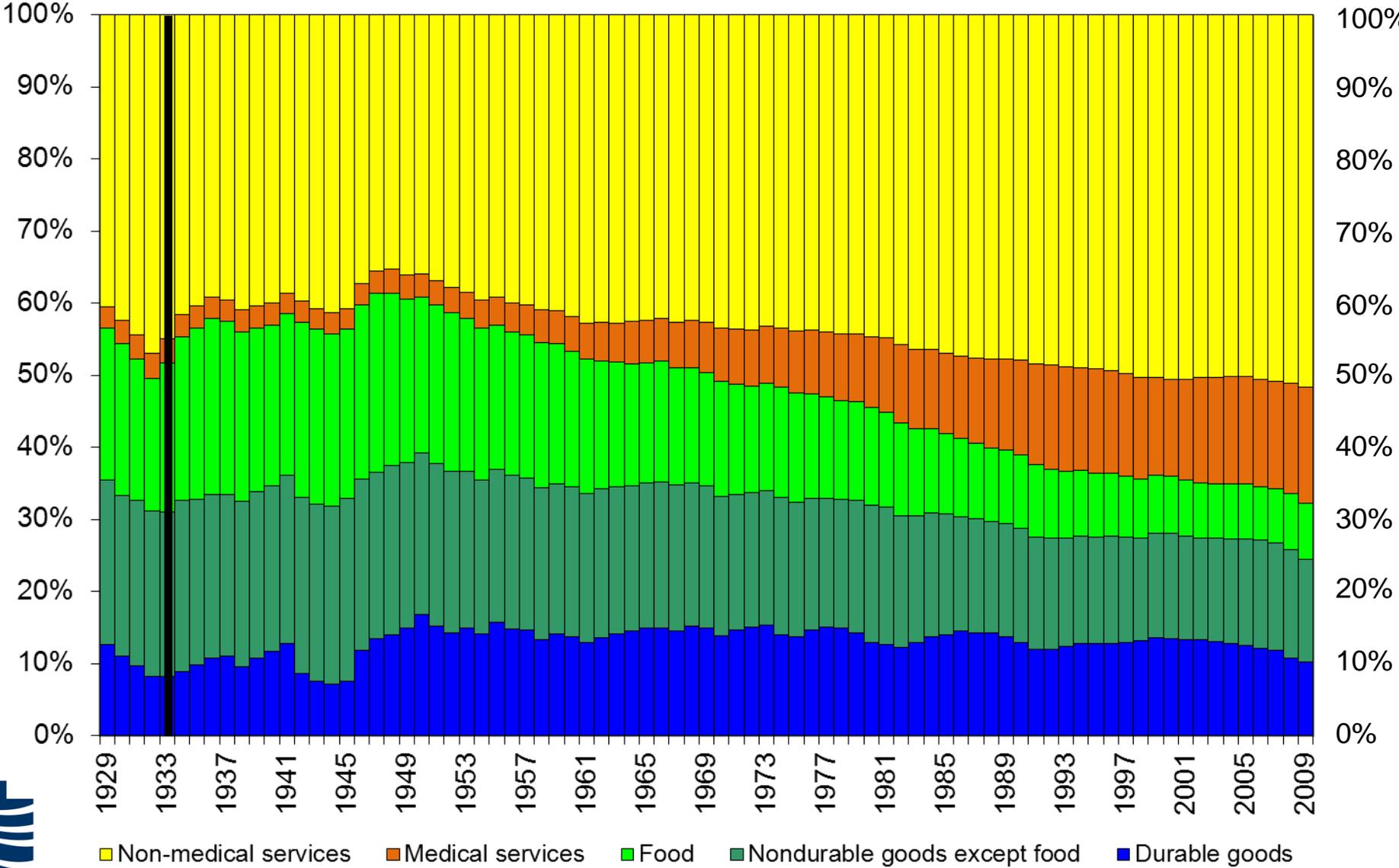
Over the long term, the sales and use tax base is gradually declining relative to the economy as a whole

The Sales & Use Tax Base:

Why is It Declining Over the Long Term?

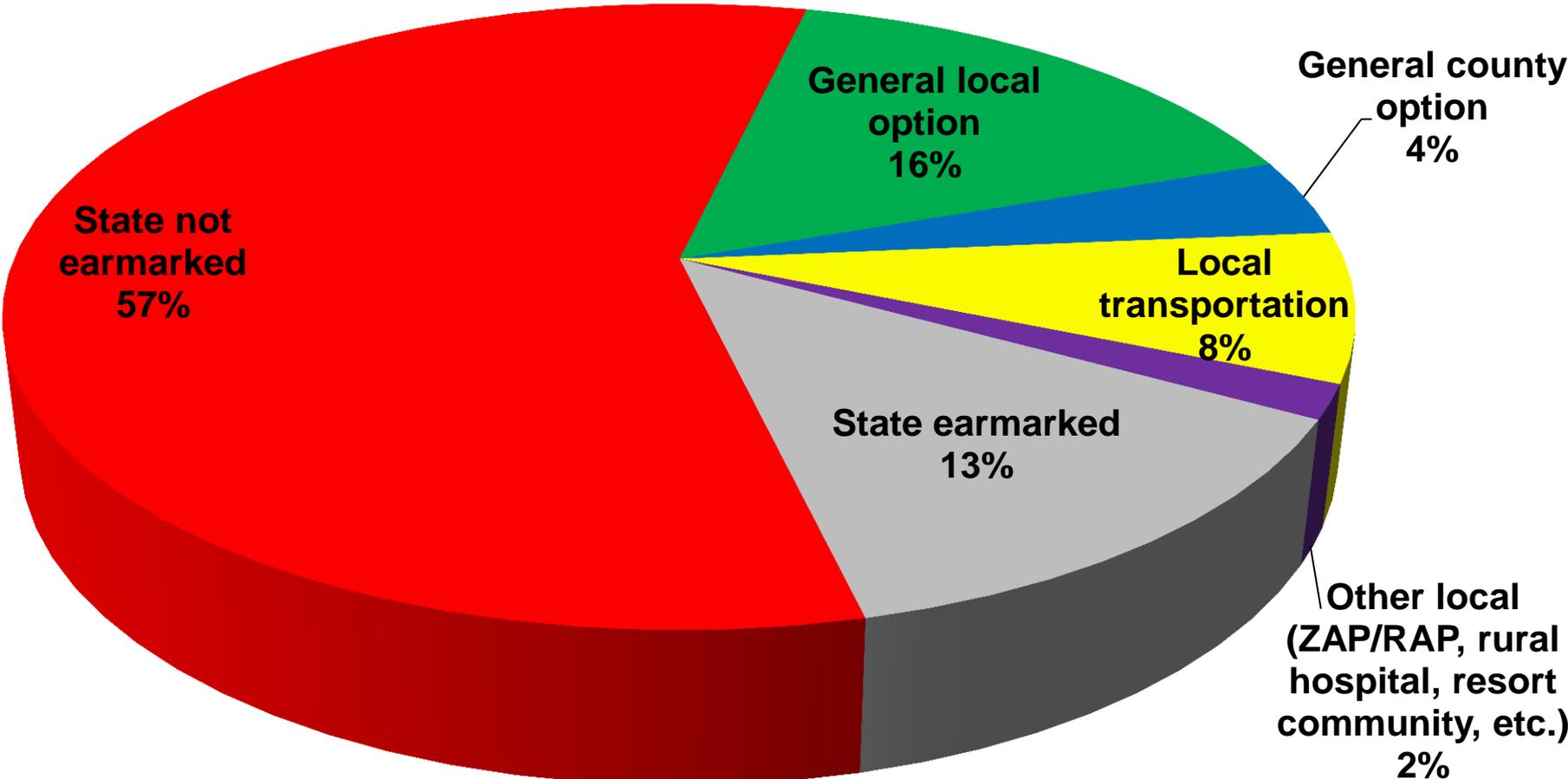
- Changing purchasing patterns
 - Movement to more of a service-based economy
 - Many services excluded from sales & use tax base
- Cross-border shopping
 - Internet, phone, and catalogue purchases
- Technological change
 - Digitization of goods (software, books, music)
- Legislated exemptions

US Personal Consumption Expenditures

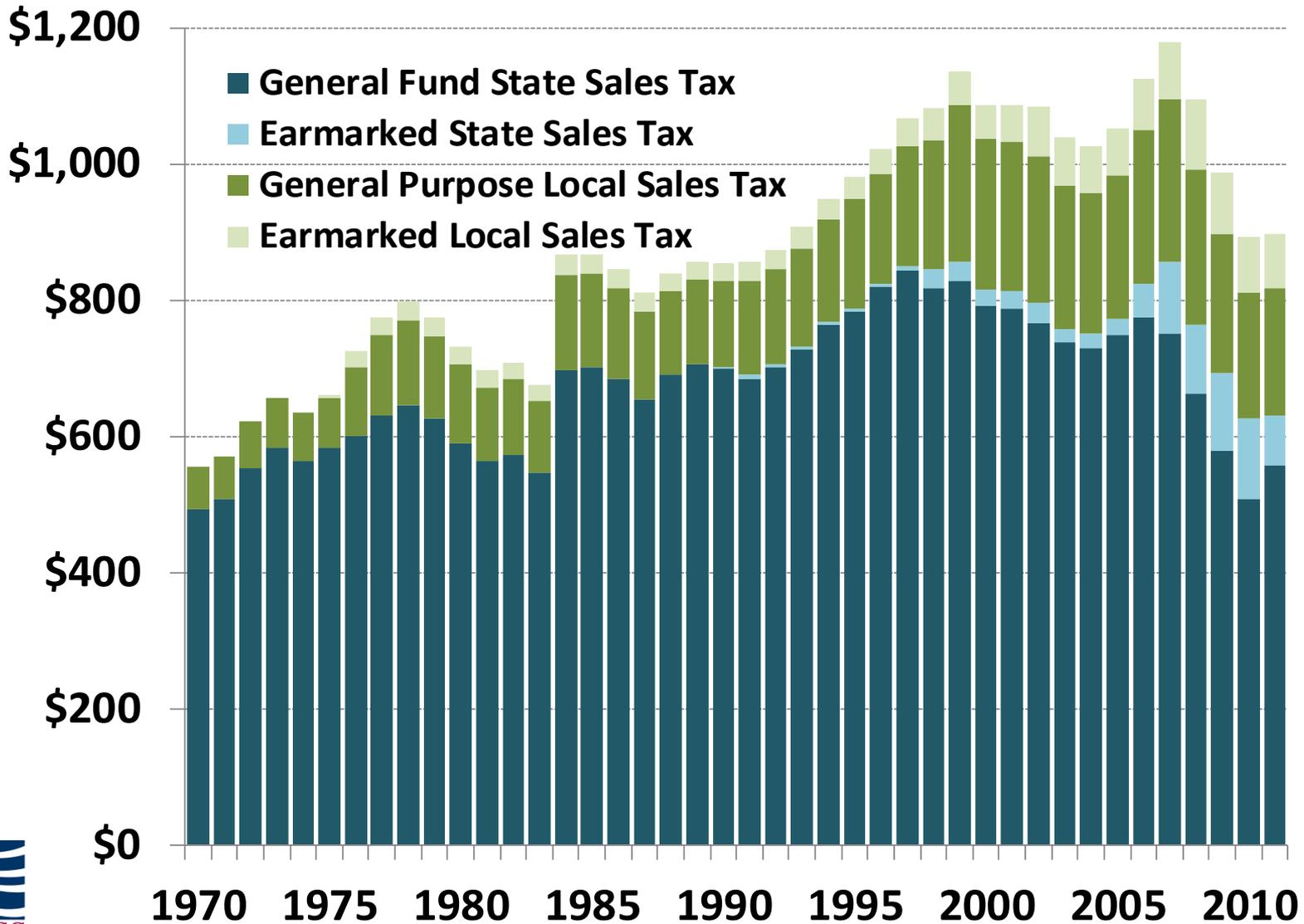


Source: US Dept of Commerce, Bureau of Economic Analysis

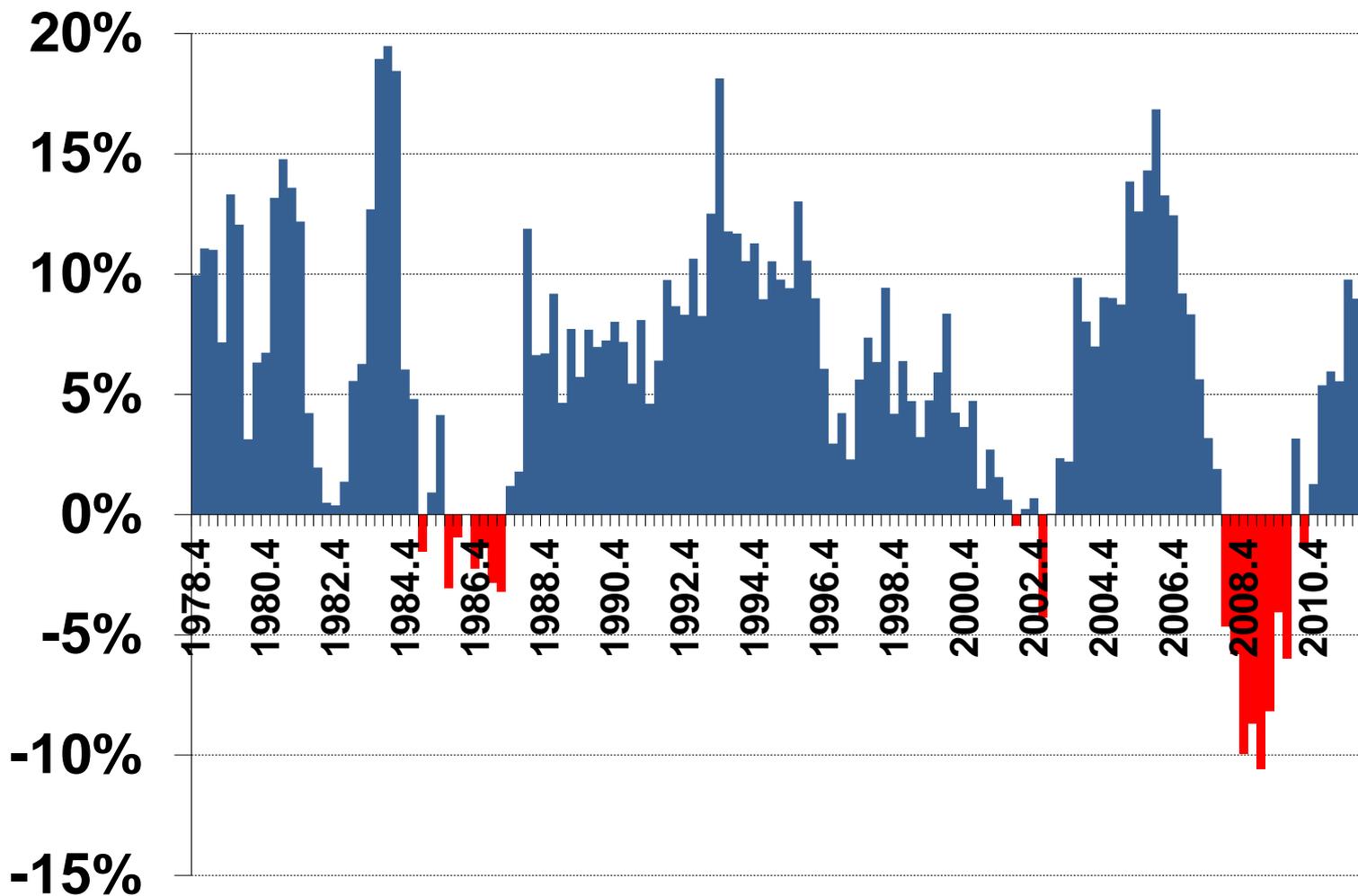
Sales and Use Tax Revenue - Where Does the Money Go? FY 2012



Real Per-Capita Sales and Use Tax Revenues Over Time



Year-Over Percent Change in Utah's Sales & Use Tax Base FY 1978Q4 to FY 2012Q2



Why Does the Sales and Use Tax Matter?

- Most significant source of revenue to state government and state higher education system
- Significant source of revenue to local governments, Utah Transit Authority, and other public transit districts
- Tax on consumption
- Politically ~~more popular~~ less unpopular than other taxes
- Impacts zoning decisions

Property Tax

The Property Tax: Embedded in the Utah Constitution

General Rule

- All tangible property shall be:
 - Assessed at a uniform and equal rate in proportion to its fair market value; and
 - Taxed at a uniform and equal rate

Exceptions to General Rule

Property Tax Exemptions

Exceptions to the General Rule

The Legislature may by statute:

- Provide for agricultural land to be assessed based on its value for agricultural purposes
- Determine the manner and extent of taxing livestock
- Determine the manner and extent of taxing or exempting intangible property
- Exempt tangible personal property required to be registered for use on a public highway, waterway, or land or in the air
- Provide for the remission or abatement of the taxes of the poor

Constitutionally Mandated Exemptions

- Government owned property
- Nonprofit entity-owned property used for religious, charitable, or educational purposes
- Burial places
- Farm equipment and machinery
- Water rights and facilities used to irrigate land owned by the owner of the water rights and facilities
- Nonprofit entity-owned water rights and facilities used to irrigate land, provide domestic water, or provide water to a public water supplier

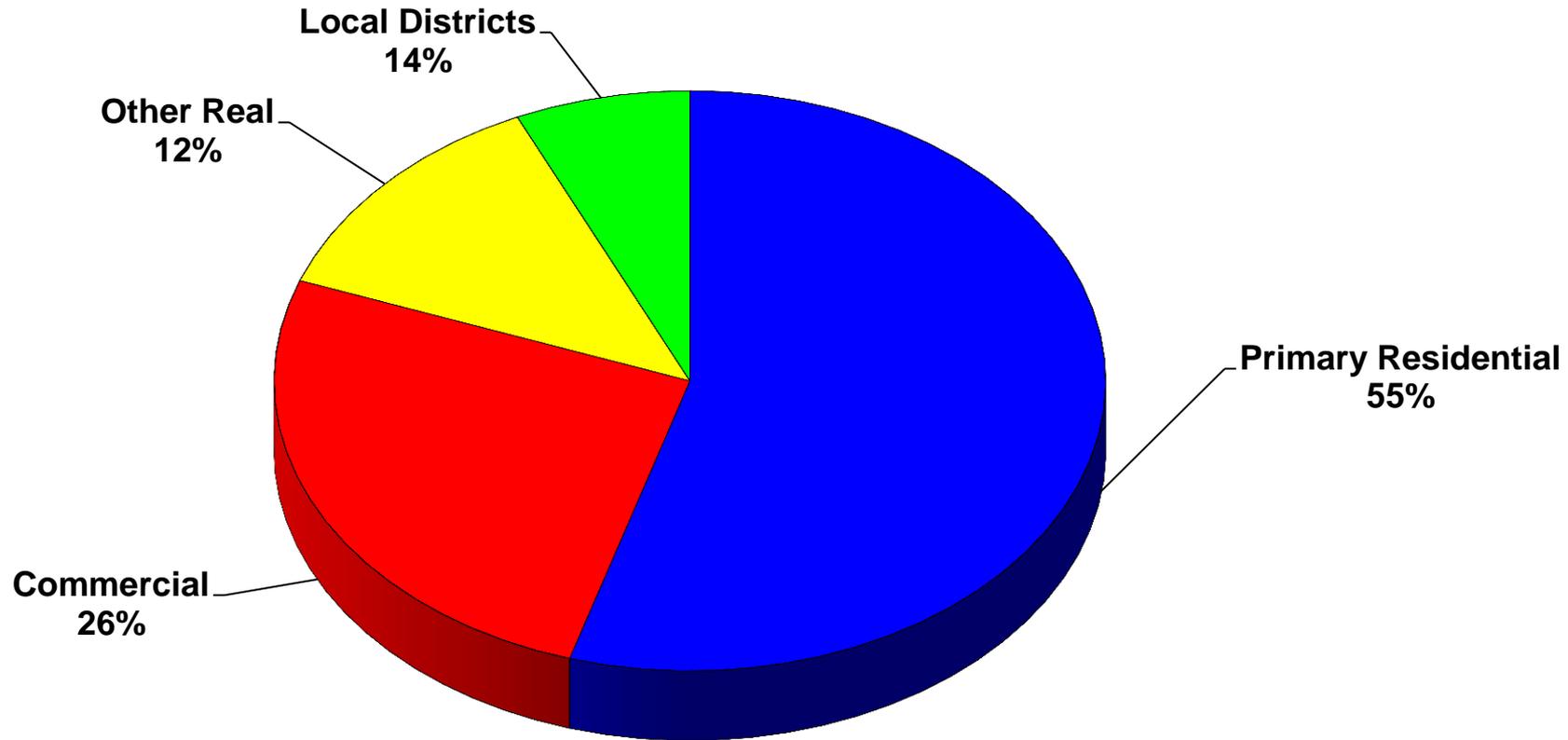
Selected Discretionary Property Tax Exemptions

- Inventory
- Up to 45% of residential property value
- Household furnishings, furniture, and equipment
- Tangible personal property that generates an inconsequential amount of revenue
- Property owned by a disabled veteran or unmarried surviving spouse or orphan

Property Taxes

Where Does the Money Come From?

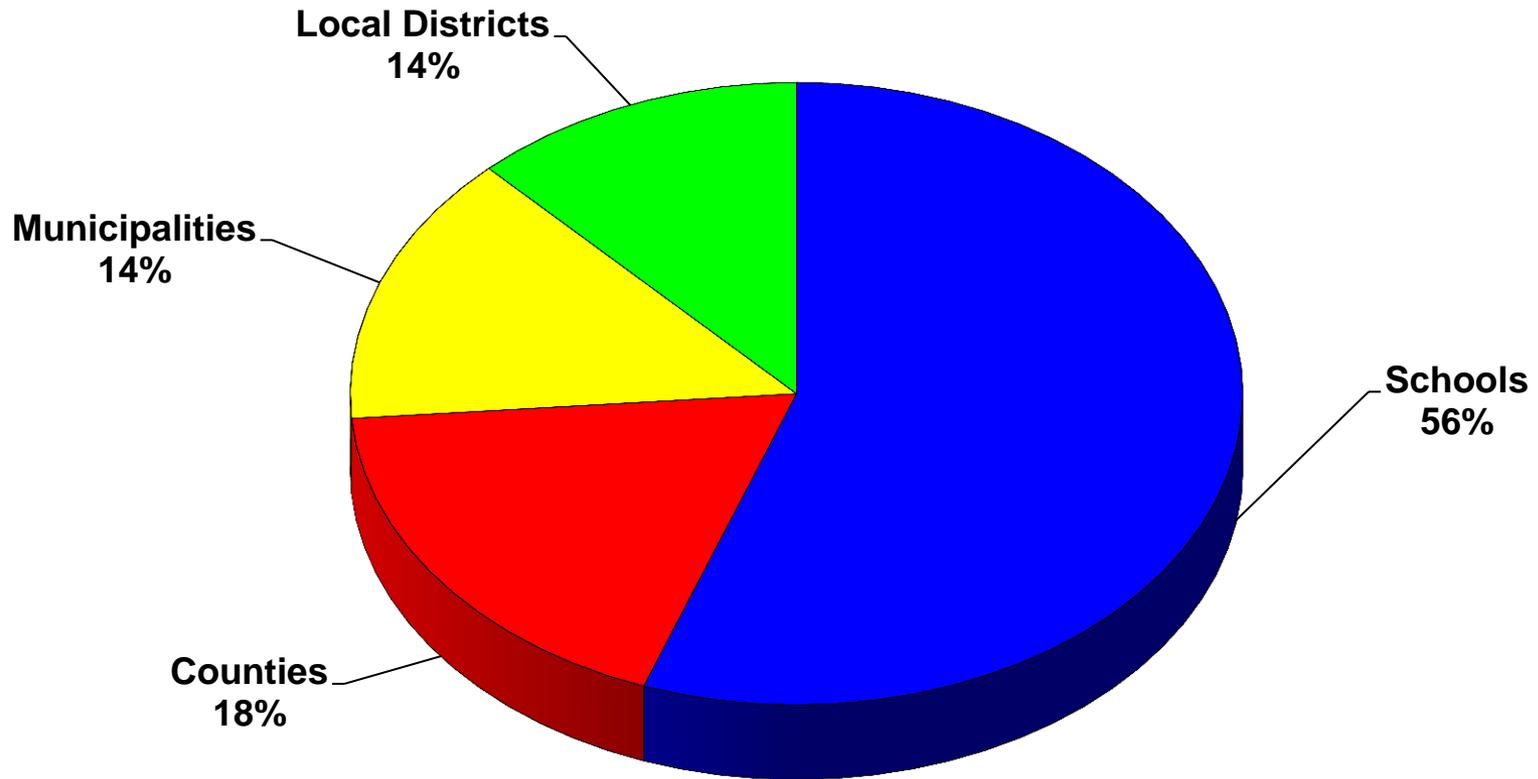
2011 Tax Year



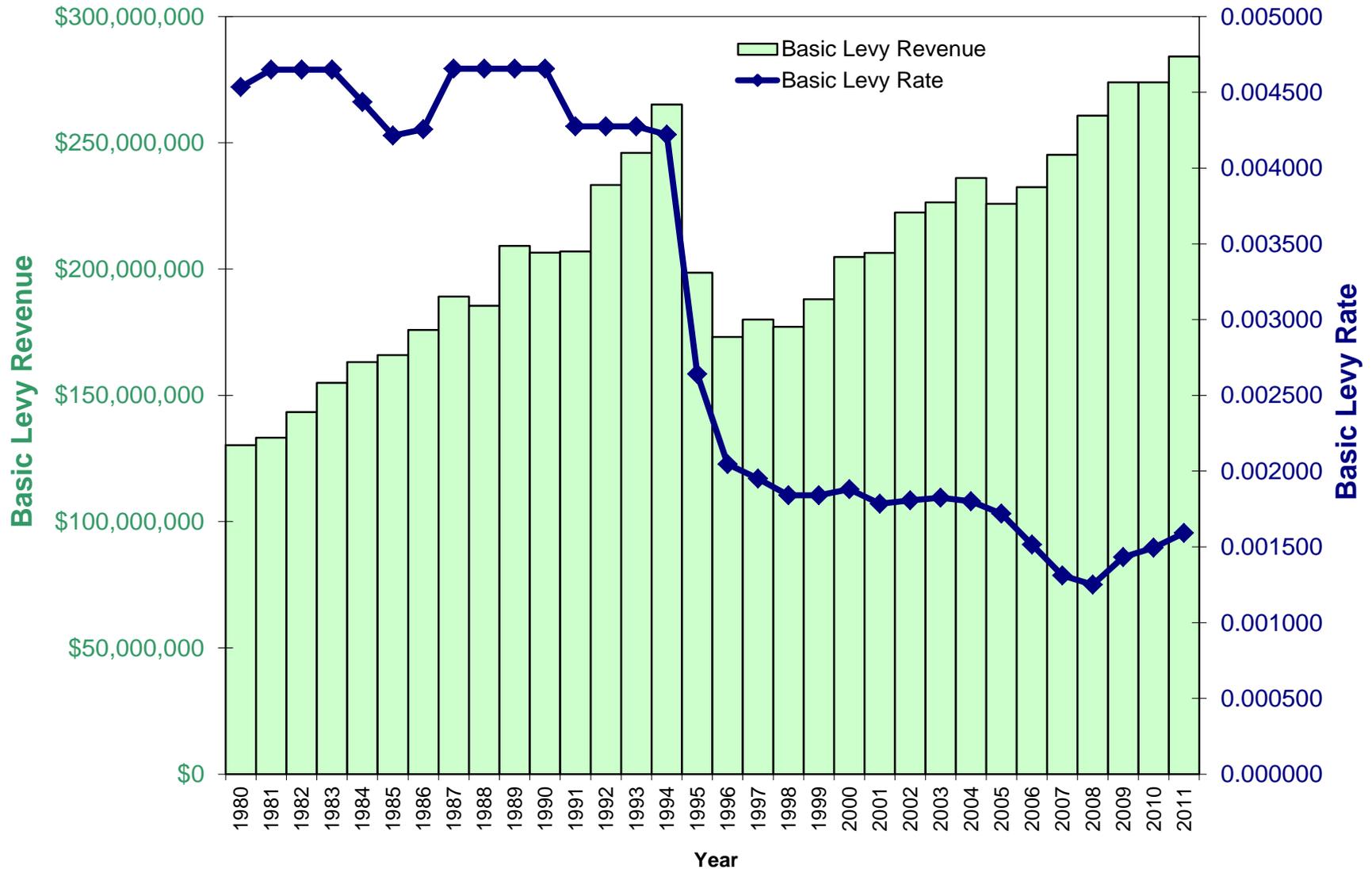
Property Taxes

Where Does the Money Go?

2011 Tax Year



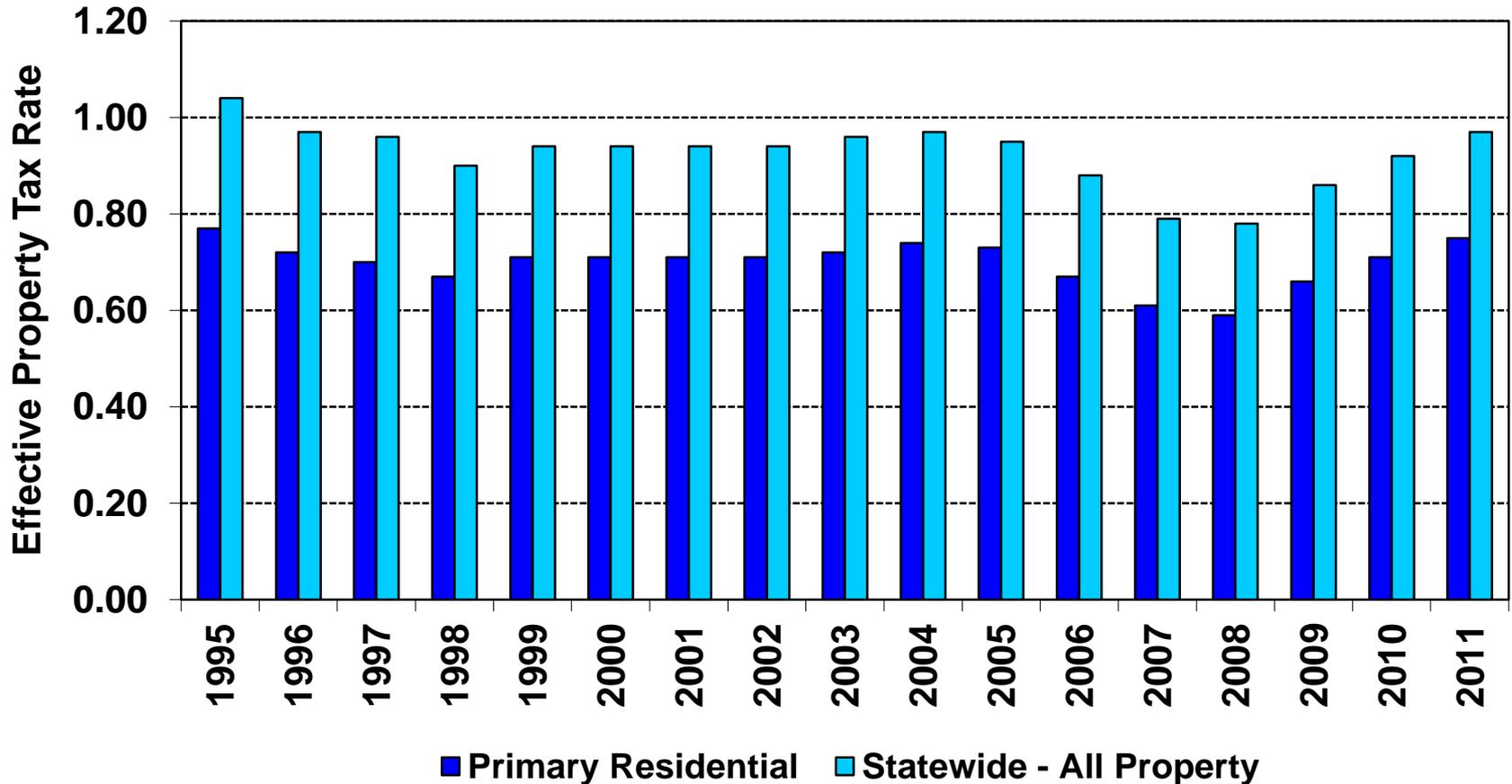
School Basic Levy History



Effective Property Tax Rates

Primary Residential Property and All Property

1995 – 2011 Tax Years



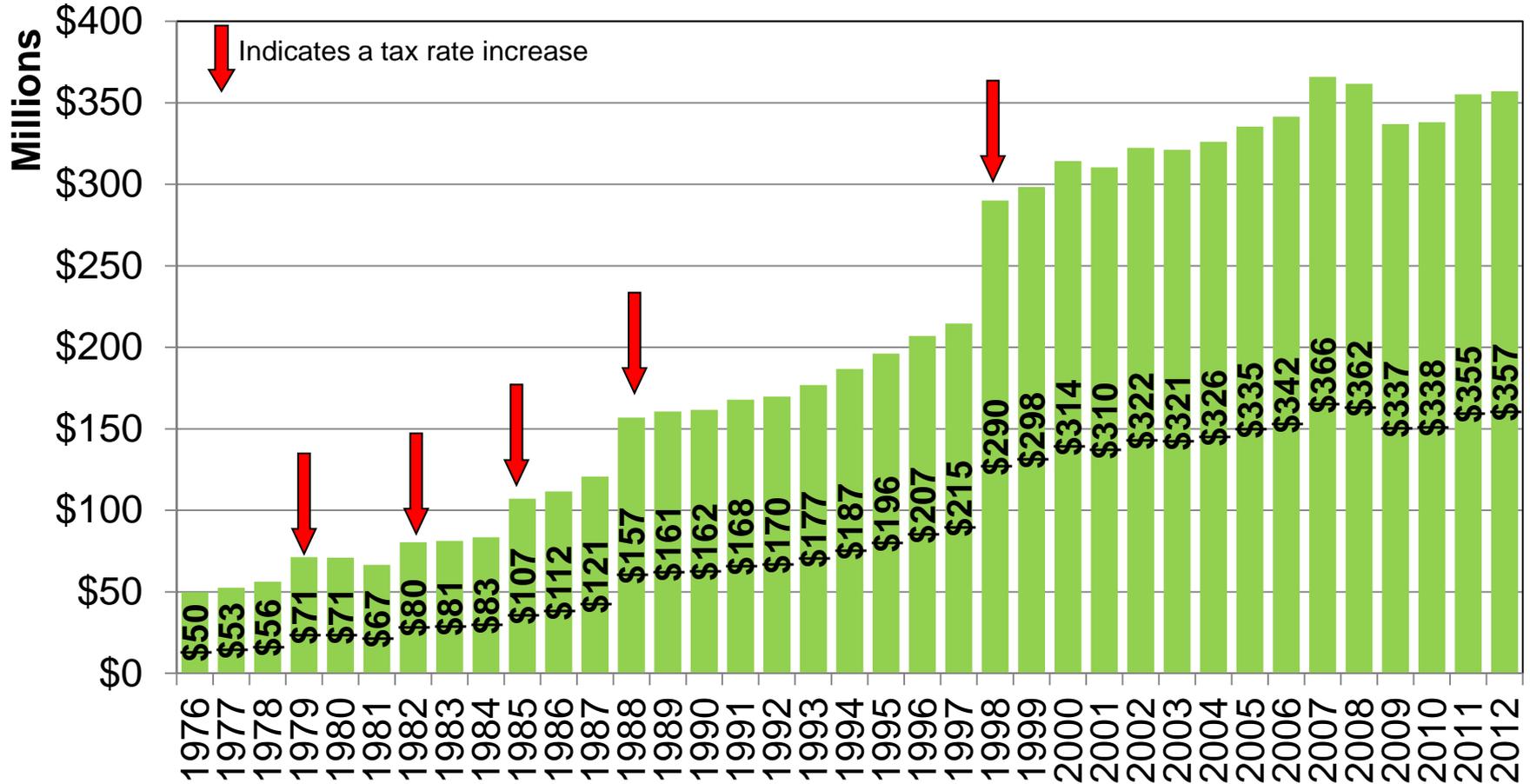
Why Does the Property Tax Matter?

- Tax on wealth and capital
- Source of revenue for schools and other local government entities
- Oldest state and local tax
- Stability
- Transparent
- Unpopular tax
- Provides political accountability

Motor & Special Fuel Taxes

Combined Motor and Special Fuel Tax Revenue

FY 1976 to FY 2011



Where Does the Money Go?

- Constitutionally earmarked for highway purposes (construction and maintenance)
- 70% to UDOT
- 30% to cities and counties (B&C Road Fund)
 - Used under the direction of UDOT
 - Distributed based on road length and pavement type

Why Do Motor and Special Fuel Taxes Matter?

- Significant source of revenue for maintaining state highway system
- Politically unpopular
- Somewhat like to a user fee - taxes use of public highways
- Taxed on a per-unit basis, so adjusts with consumption amount, not price

**Please feel free to contact us with any questions at
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