



TAX REFORM: A REALITY CHECK

WITH HR 1246, GEORGIA ABOUT TO PILE ON TO VIRGINIA FISCAL CAR WRECK

Speaker Richardson's latest version of his tax proposal focuses on removing the tax from motor vehicles and reimbursing local governments for that lost revenue – an action similar to Virginia's car tax reductions that led to a fiscal car wreck in the Commonwealth.

Virginia enacted a reduction in the car tag tax in FY 1999, with reimbursements made to local governments for their lost revenue. The cost of the reductions grew from \$181 million in 1999 to \$950 million by 2007. The costs grew so significantly that the state capped the reduction at 70 percent of the phase-out rate. As the car tax reduction was being phased in, the 2001 recession hit. A \$1 billion hole appeared in the state budget, which almost exactly matched the amount of money the state was sending to localities to reduce the car tax. Because of that continued budget gap, the state made significant cuts to agencies over several years —

- Eliminating 3,000 positions,
- Closing 12 Department of Motor Vehicle offices,
- Halting pay raises for state employees for 3 years and forcing local communities to pay for teacher raises,
- Providing no state funds for sheriffs to hire deputies,
- Cutting the community mental health system by 10 percent (2003),
- Cutting state psychiatric facilities' budget by 15 percent (2003),
- Making \$275 million in cuts to state colleges (2001), and
- Forcing George Mason University, for example, to increase tuition and fees by 16 percent to replace state funds (2002), among others.

In 2004, after years of significant cuts and a continued state budget gap, Governor Mark Warner (D) and Senate Finance Chair John Chichester (R) partnered to pass sweeping tax reform legislation. While the tax increase did not fully reverse the damage of the car tax costs, it signaled a recognition that the state could not continue on its course. Governor Warner and Senator Chichester jointly won *Governing Magazine's* 2004 Public Official of the Year for their fiscal responsibility and integrity.

Since 2001, the Government Performance Project has noted the negative consequences of the Virginia car tax reduction in every issue of its “Grading the States” —

- 2001: “The governor’s current budget proposal has attracted far more criticism than this state is accustomed to. The issues are complicated, but here’s the gist of it: Legislation was passed, taking effect in 1999, which promised a continuing reduction in car taxes if state revenues went up by 5 percent. That happened, but only because of cash from the tobacco-settlement windfall... Virginia has underestimated its ongoing revenues in the current year by \$450 million, and a solid argument can be made that this is not the time for tax cuts.”
- 2003: “Virginia’s fiscal status could be described as a car crash — both literally and figuratively. The estimated shortfall for the current budget is upwards of \$1 billion. And that’s about the same amount the state now sends cities and counties, thanks to the law passed by the previous Gilmore administration requiring the localities to phase out their property tax on automobiles. **When this decision was first made, pursuant to a Gilmore campaign promise, it looked like the state could afford to reimburse the localities for the lost revenues, and it vowed to do so. The vow was kept — but at the cost of opening a gaping hole in the state’s treasury.**”
- 2005: “Virginia has an ethos of good management that has genuinely been institutionalized. Even if a governor betrays that culture — as did Jim Gilmore when he opened a \$1 billion budget shortfall in the late 1990s with a cut in car taxes that was politically popular but fiscally unsound — the state seems able to find its way back to the path of good managerial sense.”
- 2008: “Virginia has worked hard to improve its long-term fiscal outlook over the past few years... Still, the state has to scramble relentlessly to attain structural balance. Virginia is constantly tweaking its revenue code — it has made tax changes in 15 of the past 20 years. **Many of the adjustments have been made in an attempt to undo the lasting budget effects of a poorly planned car-tax repeal and other tax cuts that were made just prior to the 2001-02 recession.** Virginia needs to continue working on a thoughtful plan to maintain structural balance in the future.”

(Sources: www.virginia.edu/coopercenter/vastat/publications/feature1.pdf, www.stateline.org/live/ViewPage.action?siteNodId=136&languageId=1&contentId=15164, <http://pn.psychiatryonline.org/cgi/content/full/38/1/33>, www.highbeam.com/doc/1P2-333916.html, www.highbeam.com/doc/1G1-120639153.html, www.governing.com/poy/2004/warner.htm, pewcenteronthestates.org/gpp.)