
Testimony before House Committee on Business & Industry

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Summary

Texas cannot take economic growth for granted. With the recent drop in oil and natural gas prices, Texas' economic growth has lagged the nation as a whole. Most recently, with oil and gas prices stabilizing, Texas is again growing faster than most other states, but only barely.

There are many reasons businesses find Texas an attractive place to invest and expand; however, among the negatives are the fact that Texas is a relatively high tax state for business.

Texas' lack of a personal income tax saves the average Texas family roughly \$3,000 annually, making Texas one of the lowest taxing states for individuals. However, state and local tax systems are shared by individuals and businesses alike. Though Texas' general business tax—the franchise tax—with last session's tax cut is low relative to other states, Texas sales and property taxes fall heavily on business. Both Texas' sales and property taxes are characterized by high rates and relatively broad tax bases. In particular Texas's property tax extends to business personal property and inventories—items exempted in many other states.

Given our high property and sales tax liabilities on business, Texas offers a number of tax and grant incentives so that we can compete for new investment with other states.

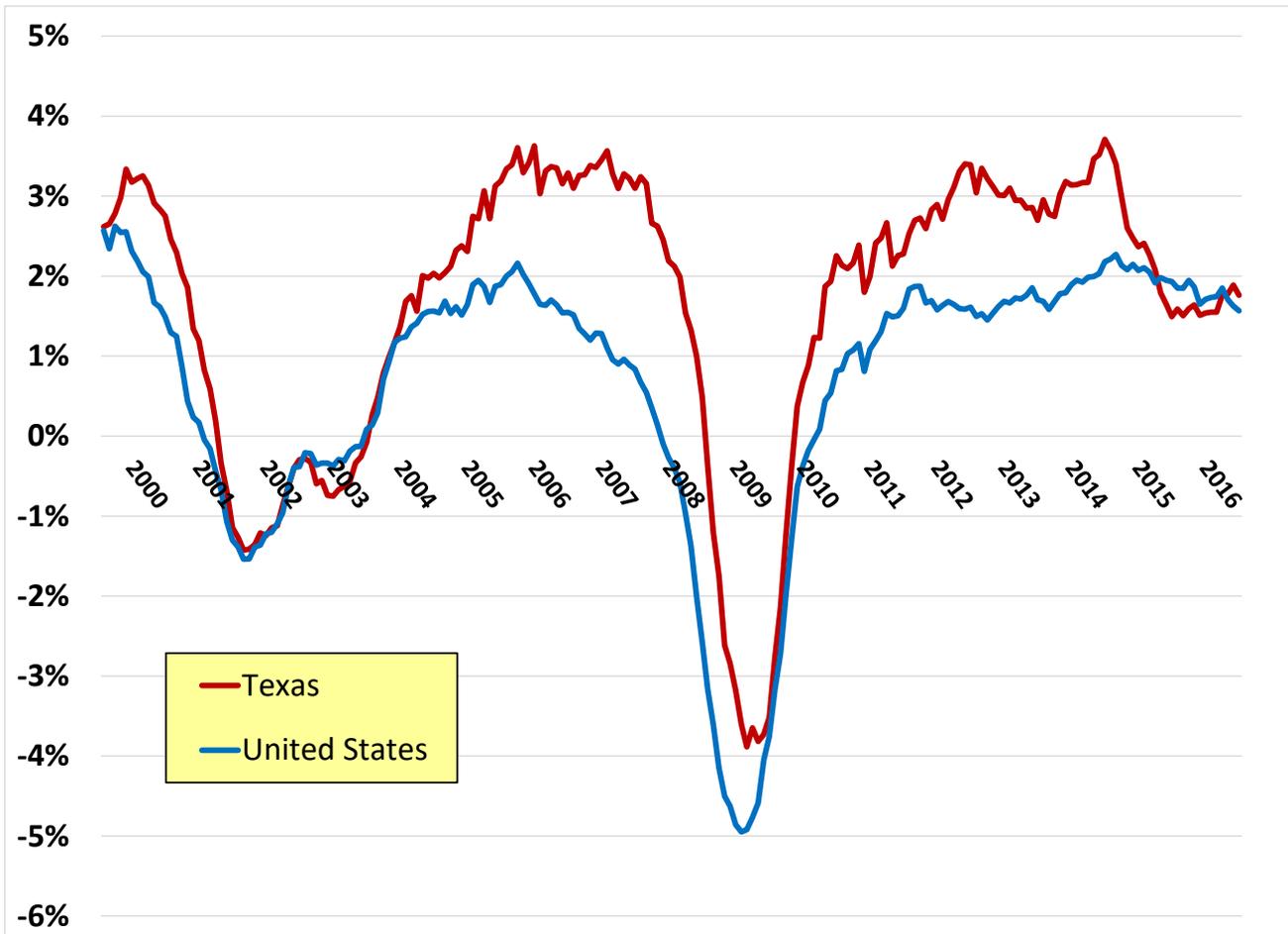
The most important of these are local property tax abatements under Chapter 312 of the Tax Code and school tax limitations under Chapter 313 of the Tax Code. Also along the state's key incentive program are the Governor's Texas Enterprise Fund grants and Skills Development Fund grants offered by the Texas Workforce Commission.

At best, these incentives programs generally get Texas “close enough” in terms of net tax liability to other states, allowing our other positive factors to sway the investment our way. While Texas' economic incentives are among the most transparent among the 50 states, these programs are characterized by incredibly high reporting requirements that served to diminish their net benefit. Businesses often must contract with consultants at substantial cost to complete the necessary paperwork associated with these incentives.

Texas' economic incentives are also spread across a number of different state and local agencies—unlike many other states which offer “one-stop shopping.” This makes Texas' process rather cumbersome when compared to other states.

In evaluating our incentive programs Texas tends to focus on the amount of benefits received by the taxpayer; however, businesses typically focus less on the amount of taxes discounted and instead focus on the bottom line of the actual amount of taxes they will pay. A better way to assess the value of the state incentive programs would be to look at the economic activity and taxes generated by new projects.

Texas Job Growth Lagging the US



For much of the past two years, with oil and gas weak, Texas job growth has been dragged down below the rate of growth of the US economy. Only recently, as oil prices have stabilized, has job Texas once again topped the national growth rate.

Still our rate of growth is more anemic than what the state is used to. Dallas, Austin, and the Gulf Coast are the state's most vibrant areas. Houston, the Permian Basin, and the Eagle Ford area of South Texas have been the weakest.

Business Assessments of Texas

Viewed Positively

- A Right-to-Work State (i.e. one may not be compelled to join a labor union as a condition of employment)
- Available land at generally reasonable cost
- A growing state with a generally ample supply of labor
- Reasonable regulatory and judicial environment
- Stable and affordable energy resources
- Centrally located to both coasts
- Lack of a personal income tax

Viewed Negatively

- Long term water availability is a concern, but is being addressed
- Transportation networks are strained, but is being addressed
- While labor is in good supply, certain categories of skilled workers may be more limited
- State and local taxes, particularly property and sales taxes, are higher than average and are particularly burdensome for capital intensive industries

Tax Incidence

There are two basic types of taxpayers:

1. *Businesses*, and
2. *Individuals*.

In Texas, *individuals* incur direct taxes on many of their purchases and their real estate, but unlike most states, not on their income.

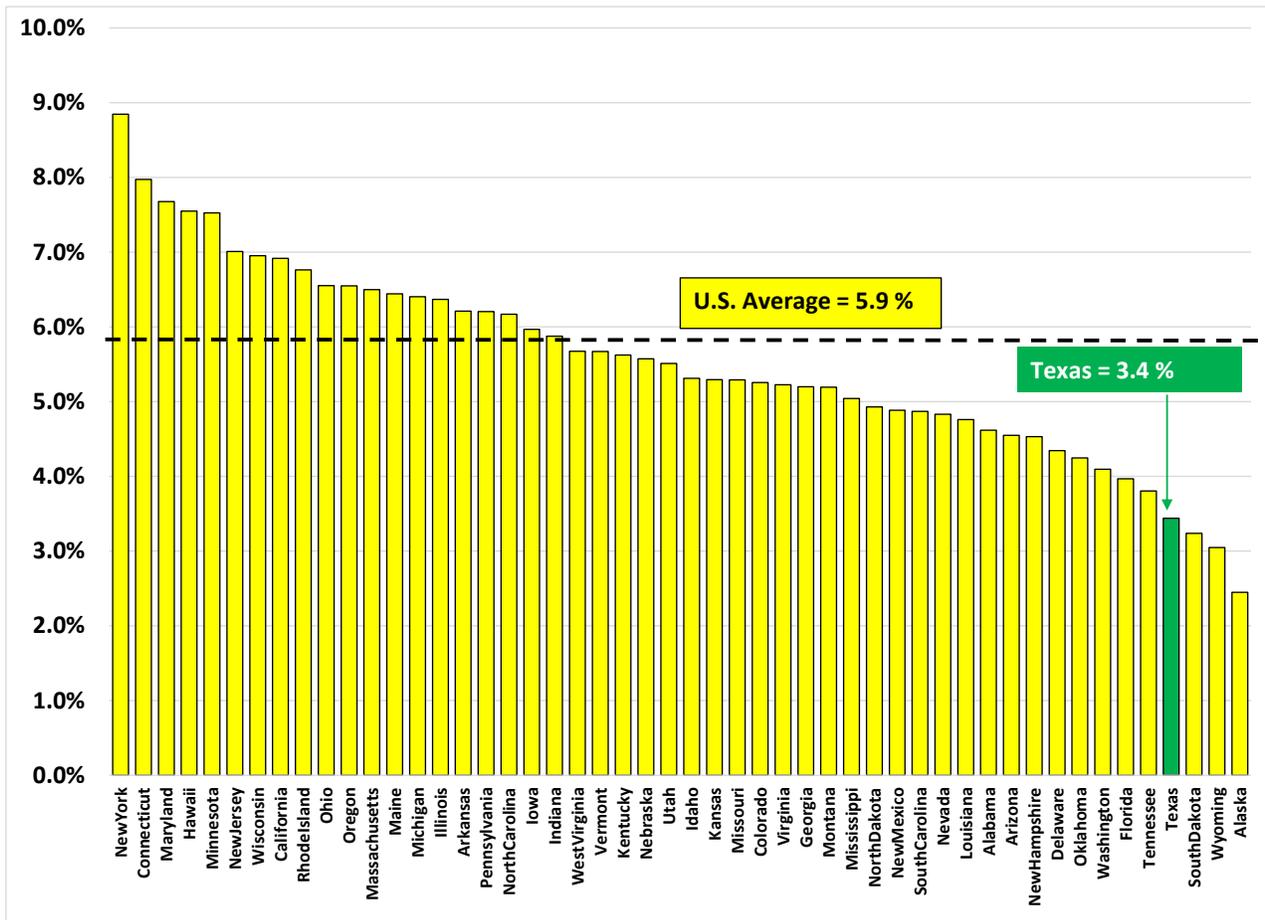
Businesses may incur taxes on their purchases (e.g. sales tax, fuels taxes), their real estate and personal assets (e.g. property tax), and be subject to special industry taxes on gross receipts (e.g. utilities, insurance). Businesses respond to taxes in one of three ways:

1. Pass the cost of the tax forward to individuals in the form of higher prices,
2. Pass the tax backward to owners in the form of lower profits, and/or
3. Pass the tax backward to individuals by reducing expenses, such as payroll or relocating or shifting investment to a lower cost location.

Note about the initial incidence assignments in this analysis...

- Sales and motor vehicle sales taxes: tax due is on the sale of a taxable item and is paid by the *purchaser*. For example, while a retailer collects the tax and remits it to the state, the tax is paid by the purchaser of the item.
- Property tax is paid by the *owner* of the property, whether an individual or a business.
- Though assessed on the refiner, motor fuels taxes are assigned to the consumer, since state law requires the tax be passed on to the consumer.
- Franchise tax is paid by the business entity.
- Severance taxes and industry gross receipts taxes are paid by the business.
- Excise taxes on consumer products (tobacco and alcohol) are predominately paid by the consumer.

Individual Tax Burden Relative to Personal Income

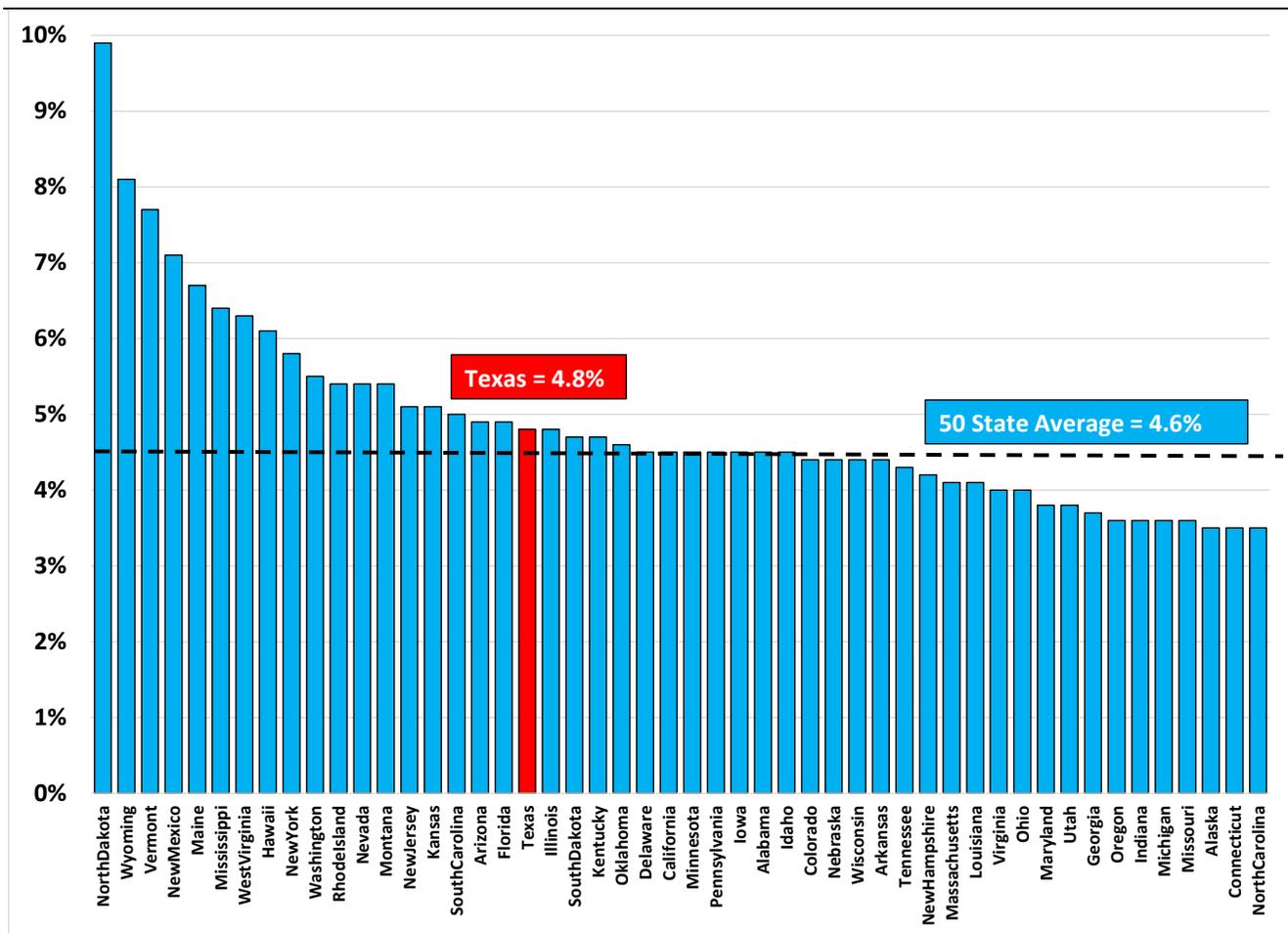


Texas ranks 46th among the states in terms of state and local taxes levied on individuals. Our state and local tax burden on individuals is 42% below the national average.

While Texas has relatively high property and sales taxes the absence of a personal income tax makes Texas a very low tax state for individuals. The absence of a personal income tax saves the average Texas family roughly \$3000 annually.

Source: Derived from Council on State Taxation: Total State and Local Business Taxes, 2015.

Business Taxes Relative to Economic Output



Texas state and local taxes on business are equivalent to 4.8% of gross state product ranking 4% above the average state. That makes Texas a relatively high tax state business—ranking 19th among the 50 states.

While the ranking is not extraordinarily high by no means is Texas a low tax state for business.

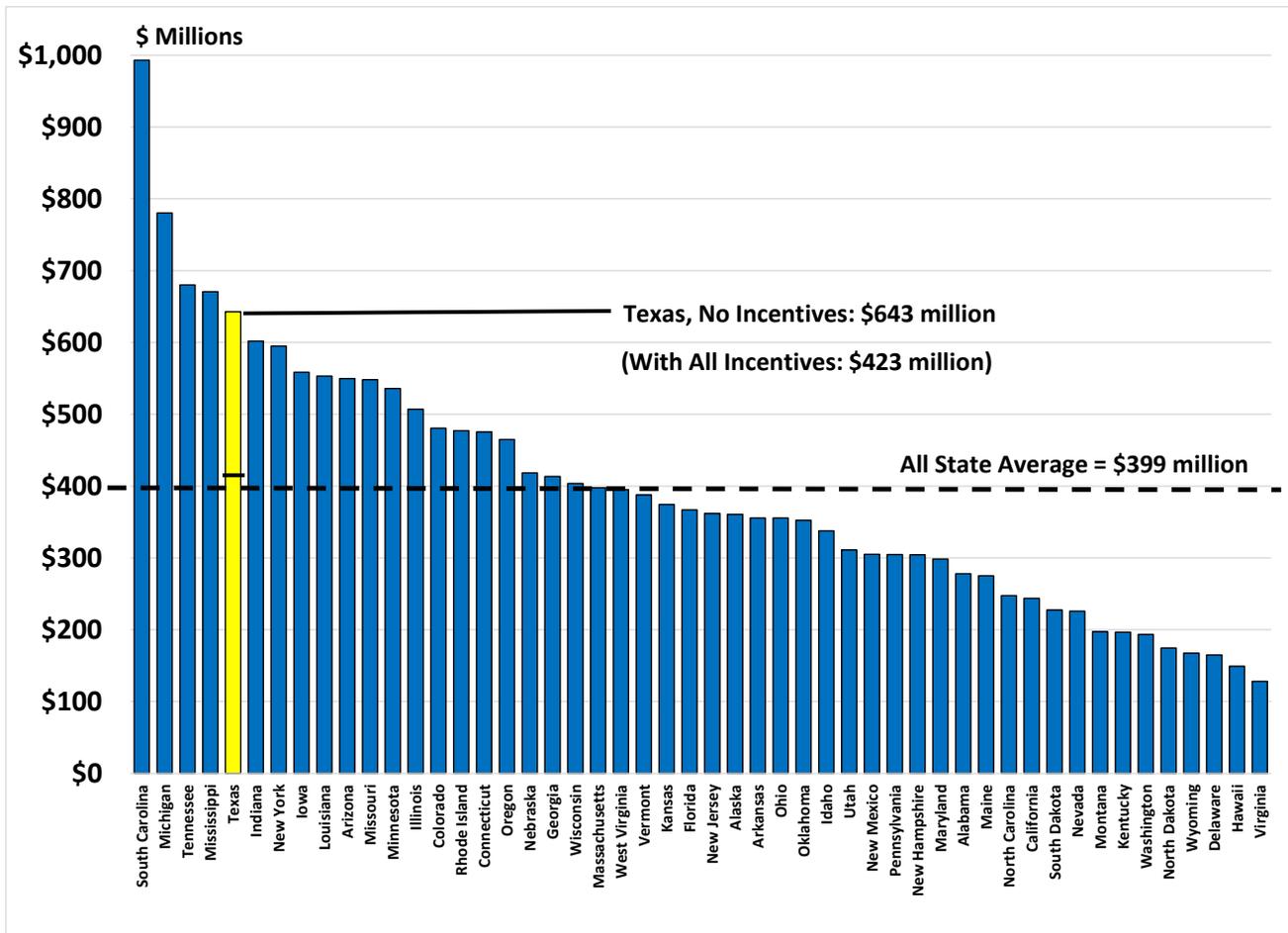
Texas' heavy reliance on property and sales taxes particularly impact both capital intensive and goods producing industries. In particular, for capital-intensive industries Texas is a very high tax state because of our high rates and broad-base property taxes.

Source: Council on State Taxation: Total State and Local Business Taxes, 2015.

Texas' Key Taxes Compared to Other States

Tax	Current Rate and Base	Comparison
Sales Tax Rate	<p>State Tax Rate: 6.25%</p> <p>Local Taxes: Generally capped at 2.0 %; average is 1.9%</p> <p>Average Combined Rate: 8.17%</p>	<p>State Rate: 13th highest</p> <p>Combined Rate: 12th highest</p>
Sales Tax Base	<p>Generally applies to all sales of tangible personal property excluding food, medicine and residential or industrial utilities; and a number of services</p>	<p>Texas' base is generally broader than that of other states because we tend to tax more services than other states (only 7 states tax more services)</p>
Property Tax Rate	<p><u>Residential property</u>: average effective tax rate in 2014 was 1.85 percent of market value</p> <p><u>Industrial property</u>: average effective tax rate in 2014 was just under 2.6% of market value</p>	<p><u>Residential property</u>: Texas' effective tax rates rank us 15th highest nationally, 25 percent above the national average</p> <p><u>Industrial property</u>: Texas' effective tax rates rank us 5th highest nationally, or 61 percent above the national average</p>
Property Tax Base	<p>Texas taxes all real estate plus any tangible personal property used for business purposes (equipment and inventory); goods in interstate commerce are exempted at local option (i.e. Freeport property)</p>	<p>Texas' base is generally broader than that of other states: 11 states exempt all business tangible personal property; inventories are generally exempt in all but 7 states.</p>
Business Franchise Tax	<p>Texas' franchise tax is unlike the net business income tax levied by most other states; Texas' effective tax rate relative to economic output was 0.33% in 2015—a number that will drop with the 2016 tax cut.</p>	<p>Relative to economic output, Texas' franchise tax ranks 25th highest among the states, about 14 percent <i>below</i> the national average; 2016 rates will drop Texas to 39th place, about one third below the national average.</p>

Comparative Property Taxes on a \$1 Billion Industrial Plant



The above chart illustrates the total property taxes on an industrial facility valued at \$1 billion million over its 25 year lifespan across the various states. Texas’ property tax costs are shown both with and without property tax abatements and Chapter 313 limitations. *Based on 50 State Property Tax Comparison Study by the Minnesota Center for Fiscal Excellence and the Lincoln Land Institute.*

The average state and local property taxes paid over the life of the facility nationwide is roughly \$400 million. In Texas, the facility, if it received no city/county property tax abatements or Chapter 313 school tax limitations, would pay over \$640 million in property taxes—60 percent higher than the national average.

If the facility received a ten year city/county property tax abatement and a ten year 313 value limitation of \$80 million, the project’s lifetime property tax bill would still be over \$400 million—roughly equal to the average of other states, but excluding any incentives those states might offer.

Selected Texas Economic Development Programs

Office of the Governor & Texas Economic Development Bank

- Texas Enterprise Fund (Government Code, Chapter 481.078)
- Texas Enterprise Project Designation
- Governor's University Research Initiative
- Defense Economic Adjustment Assistance Grants (Government Code 2310.403)
- Texas Moving Image Industry Incentive Program (Government Code, Chapter 485)
- Events Trust Fund (V.A.C.S., Article 5190.14)
- Major Events Reimbursement Program (V.A.C.S., Article 5190.14)

Office of the Comptroller

- **School Tax Limitations (Tax Code, Chapter 313)**
- **Enterprise Zone Sales Tax Refunds**

Texas Workforce Commission

- **Skills Development Fund (Labor Code Chapter 303)**
- Skills for Small Business Program (Labor Code Chapter 303)

Texas Department of Agriculture

- Rural Economic Development and Incentive Program (Agriculture Code (12.0271))
- Texas Rural Investment Fund Program (Agriculture Code 12.046)
- Texas Agricultural Finance Authority (Agriculture Code, Chapter 58)
- Agricultural Loan Guarantee Program (Agriculture Code, Chapter 58)
- Texas Capital Fund (Government Code 487.351)

Local Governments

- County Assistance Districts (Tax Code, Chapter 387)
- City Economic Development Sales Tax (Local Government Code, Chapters 501-505)
- City or County Enterprise Zones (Government Code Chapter 2303)
- City and County Property Tax Abatements (Tax Code, Chapter 312)
- School Property Tax Limitation (Tax Code, Chapter 313)
- City and County Tax Increment Financing (Tax Code, Chapter 311)

Chapter 313 Forms

Application Forms	Pages
<ul style="list-style-type: none"> • Form 50-296A Application for Appraised Value Limitation on Qualified Property To be filled out by an applicant seeking an appraised value limitation and submitted to the school district. The school district submits a completed application to the Comptroller for review and approval. 	9
<ul style="list-style-type: none"> • Form 50-300 Application for Tax Credit on Qualified Property (PDF) To be filled out by an agreement holder after paying property tax for the last complete tax year of the qualifying time period and submitted to school district. 	4
Agreement Forms	
<ul style="list-style-type: none"> • Form 50-286 Texas Economic Development Act Agreement (PDF) To be used by the applicant and school district as a template for a value limitation agreement. The school district submits a draft agreement to the Comptroller for review and approval. <i>Only applies to agreements resulting from applications determined to be complete after Jan. 1, 2014.</i> 	29
Reporting Forms	
<ul style="list-style-type: none"> • Form 50-772A Annual Eligibility Report (PDF) To be filled out by agreement holders and submitted by an authorized representative of each company to the school district by May 15th of every year using information from the previous tax (calendar) year. School districts should review the submitted forms, retain the original and submit PDF scans of the completed and signed forms and any attachments to the Comptroller's office by June 15th of every year. 	4
<ul style="list-style-type: none"> • Form 50-773A Biennial Progress Report (PDF) To be filled out by agreement holders and submitted by an authorized representative of each company to the school district by May 15th of each even-numbered year. The Comptroller's office requests that companies complete the spreadsheet version of this form, submitting both an unsigned electronic version and a signed hard copy version—with any attachments—to the school district. School districts should forward to the Comptroller's office by June 15th of each even-numbered year. 	7
<ul style="list-style-type: none"> • Form 50-287 Biennial School District Cost Data Request (PDF) School districts are also requested to submit the Biennial School District Cost Data Request Form to the Comptroller's office by July 15th of each even-numbered year, indicating—for each project—actual and estimated property values, tax rates, payments in lieu of taxes, extraordinary educational expenses, and revenue protection payments. 	1
<ul style="list-style-type: none"> • Form 50-825 Job Creation Compliance Report (PDF) To be filled out by agreement holders and submitted by an authorized representative of each company directly to the Comptroller's office annually. <i>Only applies to agreements resulting from applications determined to be complete after Jan. 1, 2014.</i> 	4

Texas Enterprise Fund Forms

Nominating Forms	
<ul style="list-style-type: none"> • Nominating Ordinance or Order or Resolution City must make take formal action to nominate a project as an “enterprise project,” and provide documentation to the Office of the Governor, Economic Development Bank. . 	5
<ul style="list-style-type: none"> • Corporate Resolution Board of Directors must adopt a resolution approving the Enterprise Project Application to be submitted to the Office of the Governor, Economic Development Bank. 	1
Application Forms	
<ul style="list-style-type: none"> • Texas Enterprise Project Application To be filled out by applicant and submitted to the Office of the Governor, Economic Development Bank with application fee ranging from \$750 to \$2,250. Application MUST be filed in a three-ring binder with supporting materials. 	31
<ul style="list-style-type: none"> • Form JCF-01 Application for Program Benefits To be filled out by a designated enterprise project to receive certification that the applicant has met the criteria making it eligible for file for benefits. The application is to be filed with the Office of the Governor, Enterprise Zone Program and must be accompanied with a non-refundable check for \$500. Required back-up documents include: <ul style="list-style-type: none"> ○ Verification of Zone Resident Status ○ Verification of Economically Disadvantaged status ○ Qualified Business Recertification forms ○ Documentation of “Contribution to Community” ○ Copy of Power of Attorney (if required) ○ Spreadsheet of qualified jobs 	5
Benefits Forms	
<ul style="list-style-type: none"> • Enterprise or Defense Readjustment Project Claim for Refund of State Sales and Use Tax To be filled out by enterprise project and filed with the Comptroller’s Office. Sales tax refund is \$2,000 per job for enterprise projects. Refund only applies to state sales taxes. 	1

Texas Skills Development Fund Forms

Application Forms	
<ul style="list-style-type: none"> • Proposal Submission Form Application is made to the Texas Workforce Commission per requirements set in the Texas Labor Code, Chapter 36. 	6
<ul style="list-style-type: none"> • Private Partner Information Form A separate form must be completed for each private partner participating in the proposed project. Information must include title of each occupation, standard occupational classification, hourly wage range, and the number of new workers receiving training. 	5
<ul style="list-style-type: none"> • Curricula and Budget Management Forms. The applicant must report all training courses by category, training hours, and administrative and direct program costs for the propose project. Separate forms include: <ul style="list-style-type: none"> ○ Business Technical Training Curricula and Direct Training Cost Detail: Program Services ○ General Technical Training Curricula and Direct Training Cost Detail: Program Services ○ Non Technical Training Curricula and Direct Training Cost Detail: Program Services ○ Training Curricula and Direct Training Cost Detail Summary ○ Equipment Purchases ○ Curricula & Budget Management Form 	14
<ul style="list-style-type: none"> • Local Workforce Development Board Review and Comment Form This form must be completed and signed by the Local Workforce Development Board in the workforce area where project participants will be employed at the completion of the training project. 	1
<ul style="list-style-type: none"> • Signed Agreement Between the Applicant and Private Partner This agreement must outline each entity's roles and responsibilities if a grant is awarded and must be included as an appendix to the Proposal Submission Form 	1

A Rational Matrix for Evaluating Incentives and Projects

Projects seeking incentives should provide some type of benefit to the state, be it:

- economic,
- fiscal, or
- intangible.

In evaluating those incentives, the state should look not just to the **operational** period of the project, but also the impact of **construction**. Further, the state should consider the **ancillary** (indirect and induced) economic impacts of the project. In evaluating the “cost” of a project, the state should look at the cost of providing public services to the project and the population it attracts.

Factors for Evaluation	Benefits		Costs	
	Direct Project	Ancillary Activity	Direct Project	Ancillary Activity
1. Economic Factors				
Investment				
Business Activity (Output)				
Jobs				
Wages and Income				
2. Fiscal Factors				
Tax and Other Revenues				
Public Service Costs				
Grants and Financing				
3. Intangible Factors				
Prestige				
Publicity				
Lifestyle Considerations				
Diversification/ Infrastructure/ Other Issues				