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# Testimony before the House Committee on Ways and Means

Dale Craymer  
President, Texas Taxpayers and Research Association  
(512) 472-8838  
[dcraymer@ttara.org](mailto:dcraymer@ttara.org)  
[www.ttara.org](http://www.ttara.org)

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# Available Revenues for Certification

## Dollars are in Billions

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Item	2016-17	2018-19	Difference
Beginning Balance	\$8.3	\$1.5	(\$6.8)
Net Current Revenues	\$99.4	\$108.0	8.6
Sales Tax Dedication for Highways	\$0.0	(\$4.7)	(\$4.7)
Total	\$107.7	104.9	(\$2.9)

*Source: Comptroller of Public Accounts, Biennial Revenue Estimate for the 2019-19 Biennium, January 2017*

Texas lawmakers have about \$3 billion less to spend this session than what was available to them in the previous biennium.

The shortfall comes in spite of the fact that current state revenues are projected to grow a modest, but healthy, \$8.6 billion in the 2018-19 Biennium.

The state has less net revenue available for two key reasons—a dramatic drop in the beginning balance and a new dedication for funding state highways.

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# Business Assessments of Texas

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## **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

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# Tax Incidence

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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:

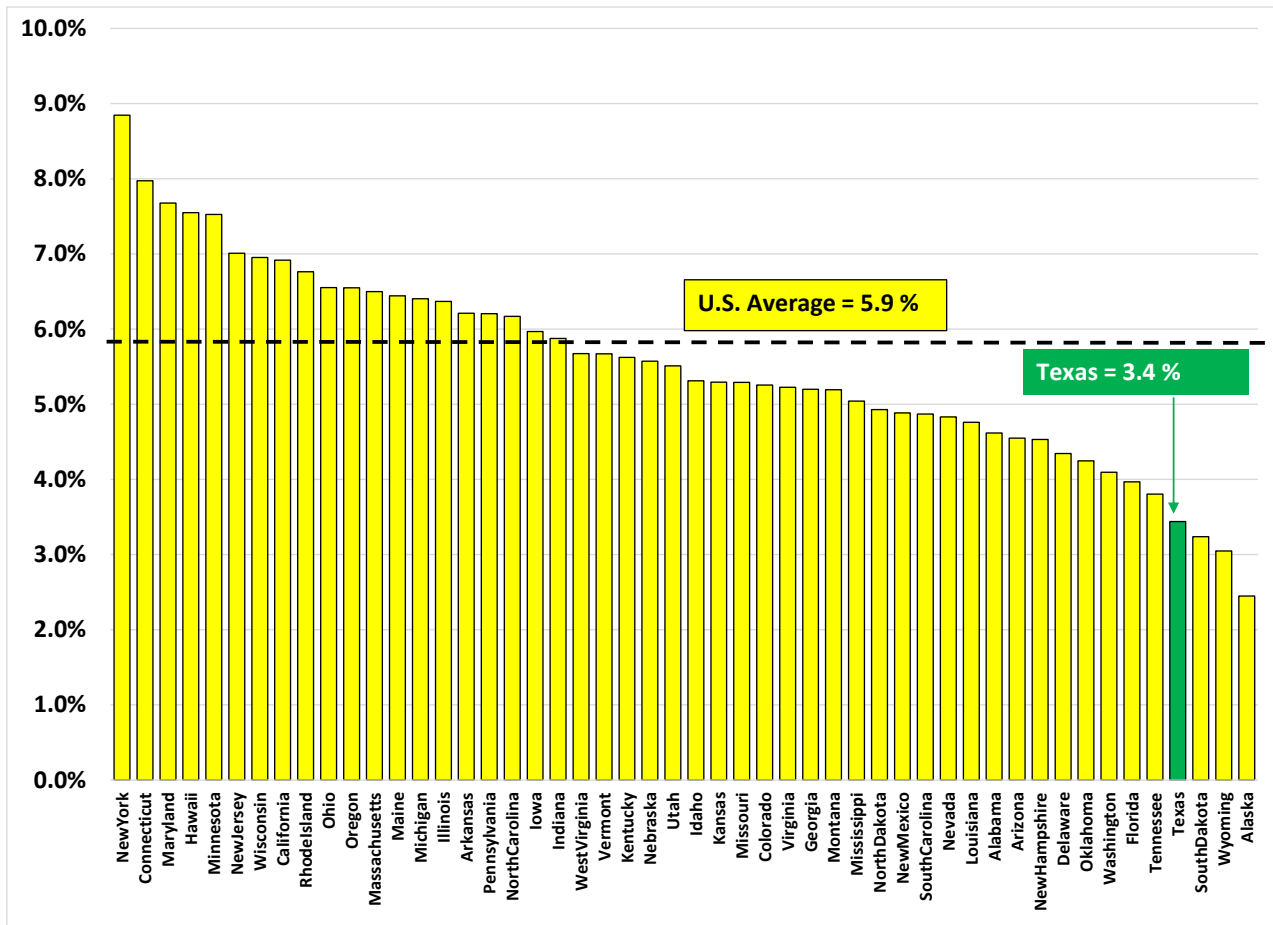
1. Pass the cost of the tax forward to individuals in the form of higher prices,
2. Pass the tax backward to owners in the form of lower profits, and/or
3. Pass the tax backward to individuals by reducing expenses, such as payroll or relocating or shifting investment to a lower cost location.

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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.
- Franchise tax is paid by the business entity.
- Severance taxes and industry gross receipts taxes are paid by the business.

# Individual Tax Burden Relative to Personal Income, 2015

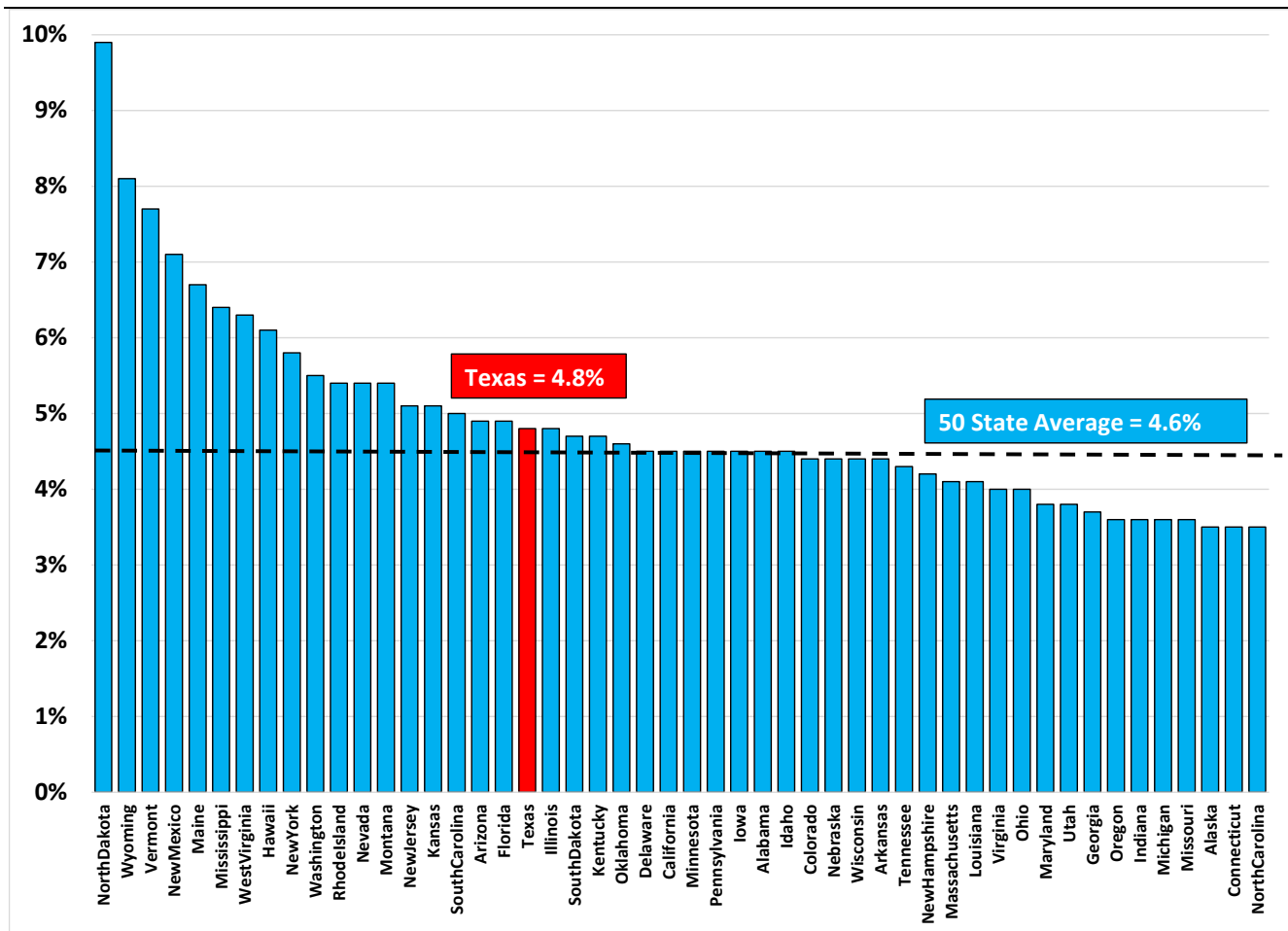


Texas ranks 47<sup>th</sup> among the states in terms of state and local taxes levied on individuals. Our state and local tax burden on individuals is 42% below the national average.

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 \$3,000 annually.

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

# Business Tax Burden Relative to Economic Output, 2015



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 19<sup>th</sup> among the 50 states.

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

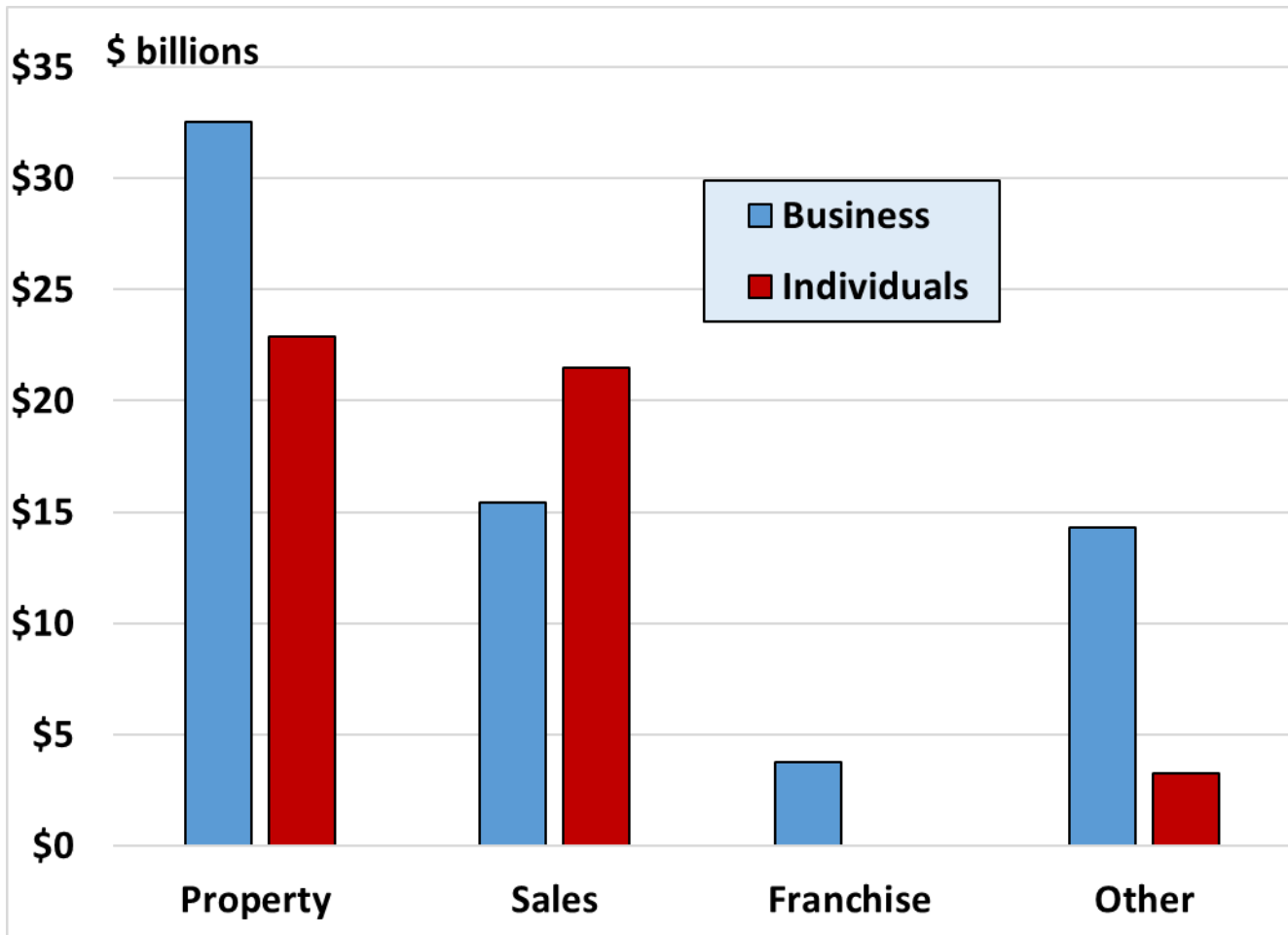
Texas' heavy reliance on property and sales taxes particularly impact both capital intensive and goods producing industries. In particular, for capital-intensive industries Texas is a very high tax state because of our high rates and broad-base property taxes.

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

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# The Taxes Business Pays in Texas, 2017

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Source: Derived from *Tax Exemptions and Tax Incidence*, Texas Comptroller of Public Accounts, February 2017, and the Texas Taxpayers and Research Association.

Texas state and local taxes will total about \$114 billion in 2017, with business paying roughly 3/5 of all taxes—the reverse of most states because of the lack of a personal income tax..

The largest tax business (and individuals) pays is the local property tax, paid to schools, cities, counties, and various special districts.

The second largest tax business (and individuals) pays is the sales tax—paid primarily to the state, but also to cities and other local governments.

While thought of as the state’s “general business tax,” businesses will actually pay \$13 in property and sales taxes for every dollar they pay in franchise tax.



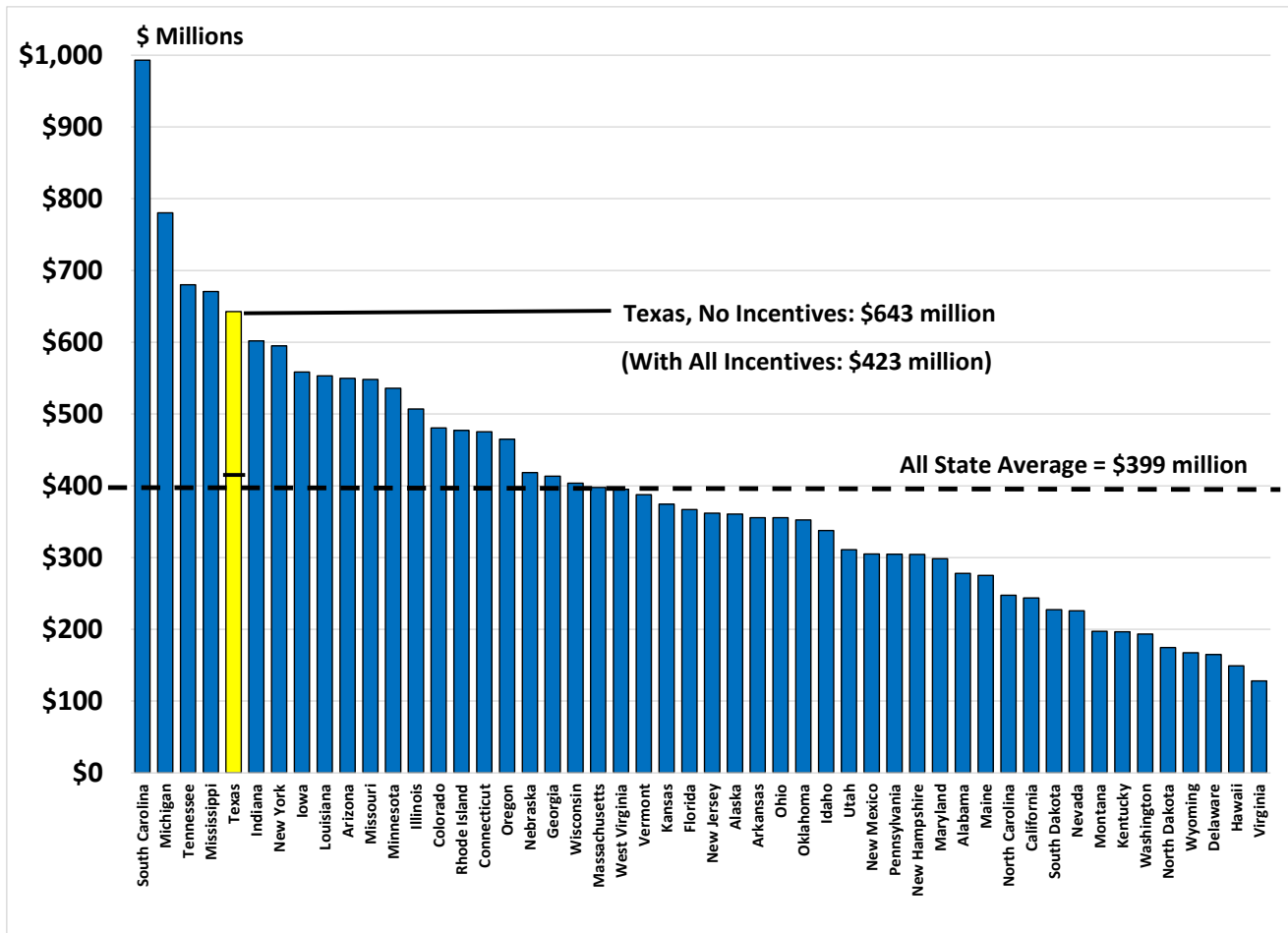
# Texas' Key Taxes Compared to Other States

Tax	Current Rate and Base	Comparison
<b>Sales Tax Rate</b>	<p>State Tax Rate: 6.25%</p> <p>Local Taxes: Generally capped at 2.0 %; average is 1.94%</p> <p>Average Combined Rate: 8.19%</p>	<p>State Rate: 13<sup>th</sup> highest</p> <p>Combined Rate: 12<sup>th</sup> highest</p>
<b>Sales Tax Base</b>	Generally applies to all sales of tangible personal property excluding food, medicine and residential or industrial utilities; and a number of services	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)
<b>Property Tax Rate</b>	<p><u>Residential property</u>: average effective tax rate in 2015 was 1.76 percent of market value</p> <p><u>Commercial property</u>: average effective tax rate in 2015 was 2.44 percent of market value</p> <p><u>Industrial property</u>: average effective tax rate in 2015 was 2.54% of market value</p>	<p><u>Residential property</u>: Texas' effective tax rates rank us 15<sup>th</sup> highest nationally, 17 percent above the national average</p> <p><u>Commercial property</u>: 19<sup>th</sup> highest nationally, 16 percent above the national average</p> <p><u>Industrial property</u>: Texas' effective tax rates rank us 5<sup>th</sup> highest nationally, or 62 percent above the national average</p>
<b>Property Tax Base</b>	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)	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 6 states (5 states partially tax inventories).
<b>Business Franchise Tax</b>	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.	Relative to economic output, Texas' franchise tax ranks 25 <sup>th</sup> highest among the states, about 14 percent <i>below</i> the national average; 2016 rates will drop Texas to 39 <sup>th</sup> place, about one third below the national average.

# The Good and the Not-So-Good About Texas Taxes

Good	Not-So-Good
<b>Property Tax</b>	
<ul style="list-style-type: none"> <li>• System of property appraisal is administered by licensed professionals</li> <li>• Each property has one appraised value based on a standard of market value (no split roll)</li> <li>• Process of disputing values is readily accessible to property owners</li> </ul>	<ul style="list-style-type: none"> <li>• Property tax rates are very high in Texas; the base of the tax is broader than other states, including, for example, business inventories—items commonly exempt in other states</li> <li>• Given the high property tax burden, tax abatements are critical in attracting many capital intensive projects</li> <li>• The quality of appraisal in small appraisal districts may be of a lower standard</li> <li>• Taxpayers do not always perceive Appraisal Review Boards as objective</li> <li>• Taxpayers confuse rising values with rising taxes—tax bills depend on the tax rates adopted by taxing jurisdictions</li> </ul>
<b>Sales Tax</b>	
<ul style="list-style-type: none"> <li>• Generally well understood issues of taxability given its long history</li> <li>• Generally perceived as the state’s fairest tax because everyone pays</li> <li>• Given the relatively broad tax base, the tax roughly matches the economy of the state</li> </ul>	<ul style="list-style-type: none"> <li>• Complex myriad of local sales taxes</li> <li>• Because everyone pays the tax, it is regressive, meaning lower income families see more of their incomes going to pay the tax</li> <li>• Inability to tax remote sales puts some sellers at a disadvantage to others and limits state revenue collections</li> <li>• High proportion of tax paid by business makes tax invisible to final consumers</li> </ul>
<b>Franchise Tax</b>	
<ul style="list-style-type: none"> <li>• Tax better tracks the composition of the state’s economy</li> </ul>	<ul style="list-style-type: none"> <li>• Tax is complex, requiring separate books from the federal tax return</li> </ul>

# Property Taxes on a \$1 Billion Industrial Investment Project (25 Year Life)

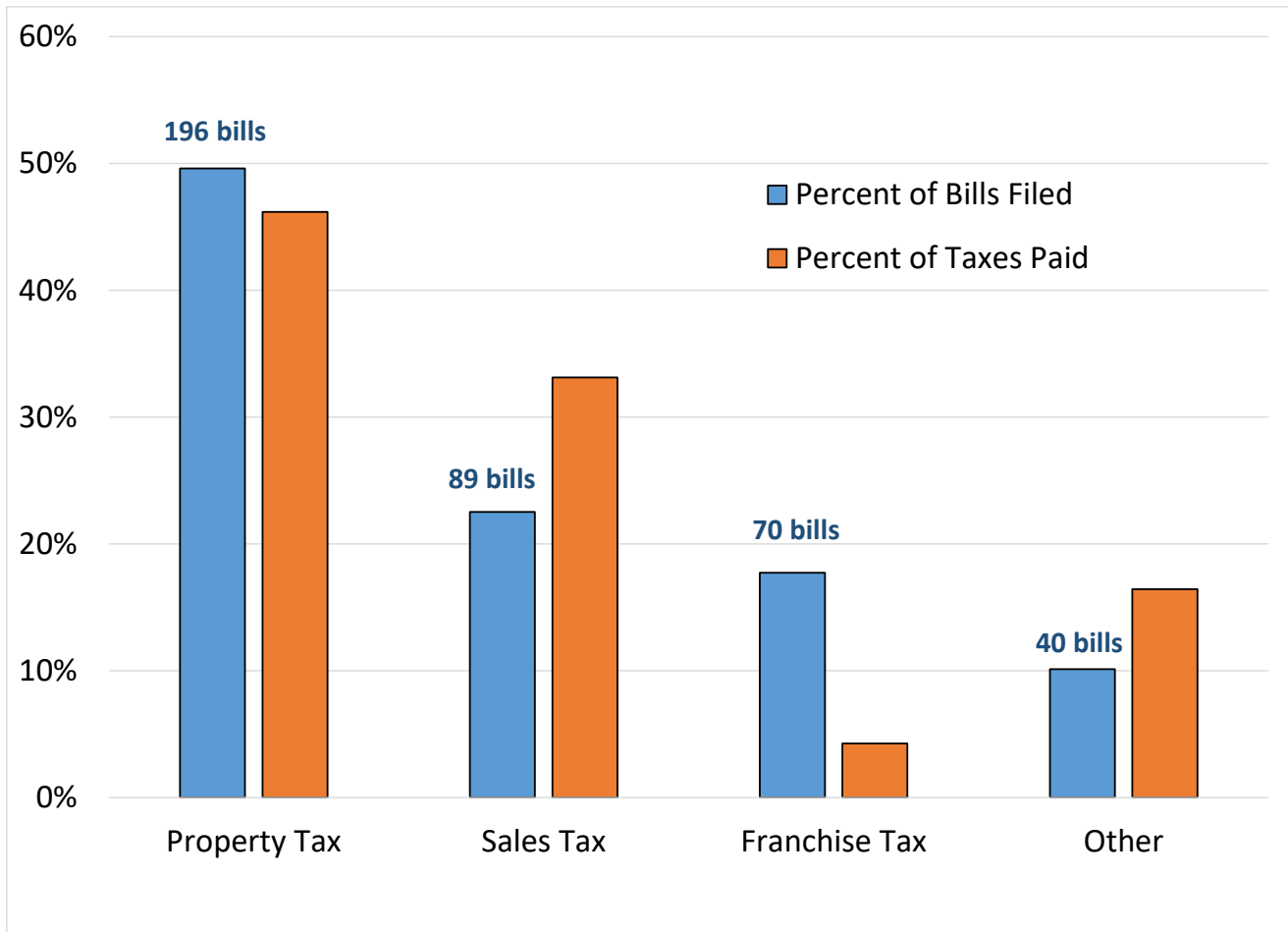


The above chart illustrates the total property taxes on an industrial facility valued at \$1 billion million over its 25 year lifespan across the various states. Texas’ property tax costs are shown both with and without property tax abatements and Chapter 313 limitations. *Based on 50 State Property 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.

# Bills Referred to Ways and Means Relative to Actual Taxes Paid, 2015



In 2015, a total of 395 bills were filed and referred to the Ways and Means Committee (including Senate bills).

Roughly half—196—of those bills related to property tax (about the same proportion the property tax represents of all state and local taxes paid).

About a fourth of those bills related to sales tax—proportionately less than the proportion the sales tax represents of state and local tax collections. This implies some degree of satisfaction with the sales tax, or at least the perception that it is in less need of change.

About 20 percent of bills referred to Ways and Means related to the franchise tax—even though the tax amounted to less than 5 percent of all state and local taxes. This implies a substantially high level of dissatisfaction with the tax.