

TTARA
Webcast Update
on Tax & Fiscal Issues

September 9, 2016

Continuing Education Credits

We are pleased to offer 1 hour of continuing education credit for attorneys, accountants, and professionals in taxation with the State Bar of Texas, the Texas State Board of Public Accountancy, and the Institute for Professionals in Taxation.

Certificates of participation have been uploaded and can be found on the Gotowebinar toolbar on the right side of your screen under the “Handout” menu. You can download and place a copy in your files. If you have trouble locating the certificate, contact Ryan at ryan@ttara.org and he will send you a copy. We will enter the State Bar of Texas credit, but accountants and tax professionals need to submit their credit to those organizations.



Agenda

1. Upcoming TTARA Meetings and Events
2. Fiscal Update and Outlook
3. Economic Development
4. School Finance
5. Sales Tax
6. Property Tax
7. Franchise Tax
8. Administrative Rules Proposals

Upcoming 2016 Meetings & Events

- **TTARA Property Tax Meeting:** Tuesday, September 20, 9:30 a.m. to noon, at 400 West 15th Street, 3rd Floor Auditorium, Austin, TX.
- **Annual Meeting:** Thursday, October 6 and Friday October 7 at the Sheraton Austin Hotel at the Capitol. **Deadline to make hotel reservations at discounted rate is Sept. 12.**
- **Webcast:** November 3. Start at 9:30 a.m. and last no longer than an hour.
- **Legislative Preview:** Wednesday, December 14, 9:30 a.m. to noon, at 400 West 15th Street, 3rd Floor Auditorium, Austin, TX.

2017 Legislative and Tax Committee Meeting Schedule

Meetings will be held in the third floor auditorium at 400 West 15th Street, Austin, TX

| Date | Legislative 9:00-10:00 am | Property Tax 10:00 am-12:00 pm | State Tax 10:00 am-12:00 pm |
|-------------|------------------------------|-----------------------------------|--------------------------------|
| January 11 | ✓ | ✓ | |
| January 26 | ✓ | | ✓ |
| February 8 | ✓ | ✓ | |
| February 22 | ✓ | | ✓ |
| March 8 | ✓ | ✓ | |
| March 22 | ✓ | | ✓ |
| April 5 | ✓ | ✓ | |
| April 19 | ✓ | | ✓ |
| May 3 | ✓ | ✓ | |
| May 17 | ✓ | | ✓ |
| May 31 | ✓ | ✓ | |
| June 14 | ✓ | | |

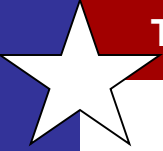


2017 Webcast Schedule

(All webcasts will begin at 9:30 a.m. on the second Thursday of the month and last approximately one hour)

- January 12
- February 9
- March 9
- April 13
- May 11
- June 8
- September 14
- November 9

All data and information is the property of TTARA and we ask that in sharing this data you credit TTARA with the source of information.



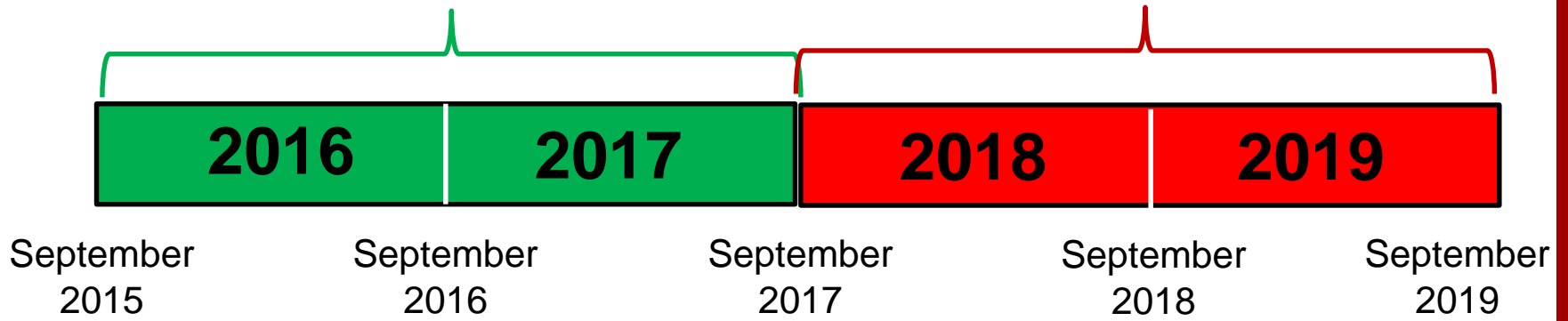
Fiscal Update



Assessing the Timeline

Current State Budget Passed in 2015

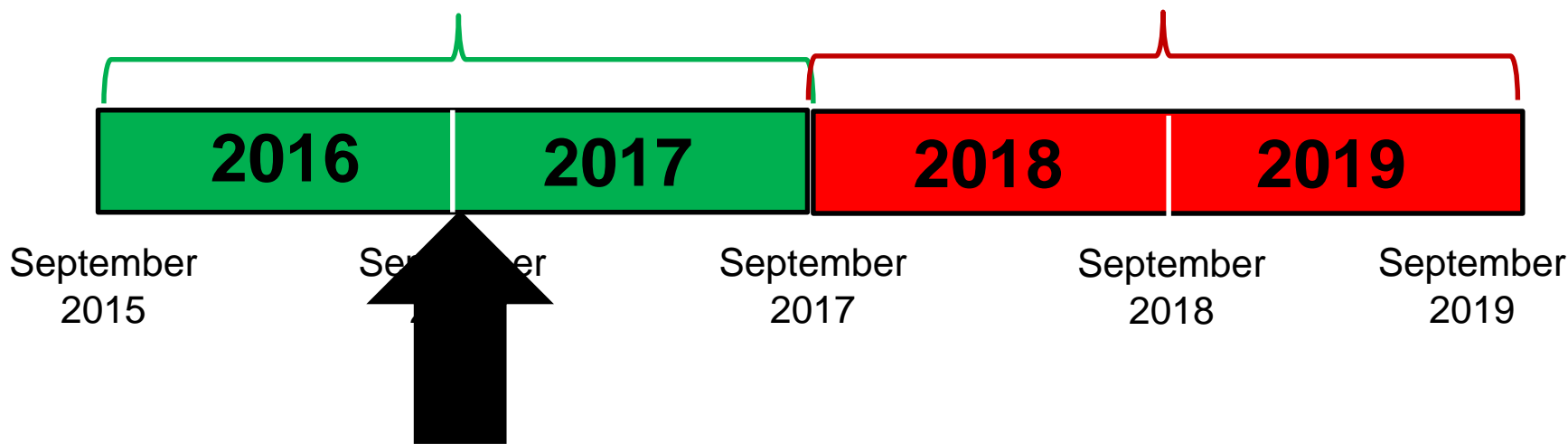
Next State Budget 2017 Legislative Session



Assessing the Timeline

**Current State Budget
Passed in 2015**

**Next State Budget
2017 Legislative
Session**

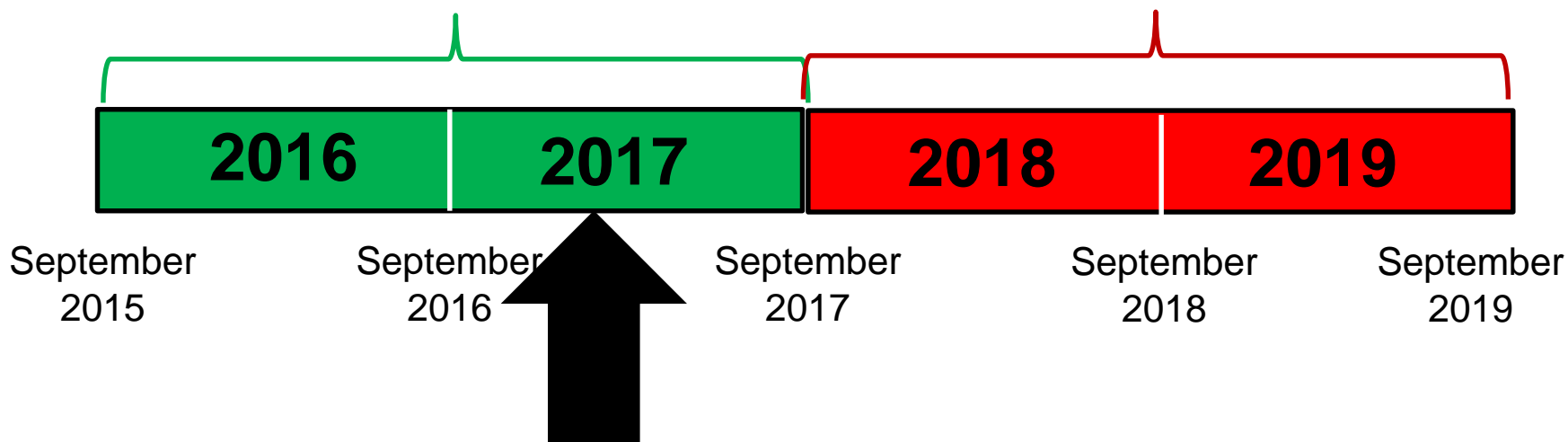


We are here

Assessing the Timeline

**Current State Budget
Passed in 2015**

**Next State Budget
2017 Legislative
Session**



**Legislature meets
here**

State General Revenues

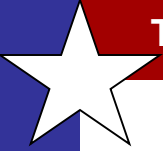
Fiscal 2016

| | 2016 Projected Revenues | Actual 2016 Revenues | Difference |
|-------------------------|-------------------------------|-------------------------|------------------|
| Sales Tax | \$ 29.1 b | \$ 28.1 b | (\$1.0) b |
| Motor Vehicle Sales Tax | \$ 4.8 b | \$ 4.6 b | (\$0.2) b |
| Franchise Tax | \$ 3.5 b | \$ 3.9 b | \$0.4 b |
| Severance Taxes | \$ 2.7 b | \$ 2.3 b | (\$0.4) b |
| Other Taxes | \$ 6.8 b | \$ 6.8 b | \$0.0 b |
| Non Tax Revenue | <u>\$ 6.3 b</u> | <u>\$ 7.0 b</u> | <u>\$ 0.6 b</u> |
| Total | \$ 53.3 b | \$52.6 b | (\$0.6) b |

State General Revenues

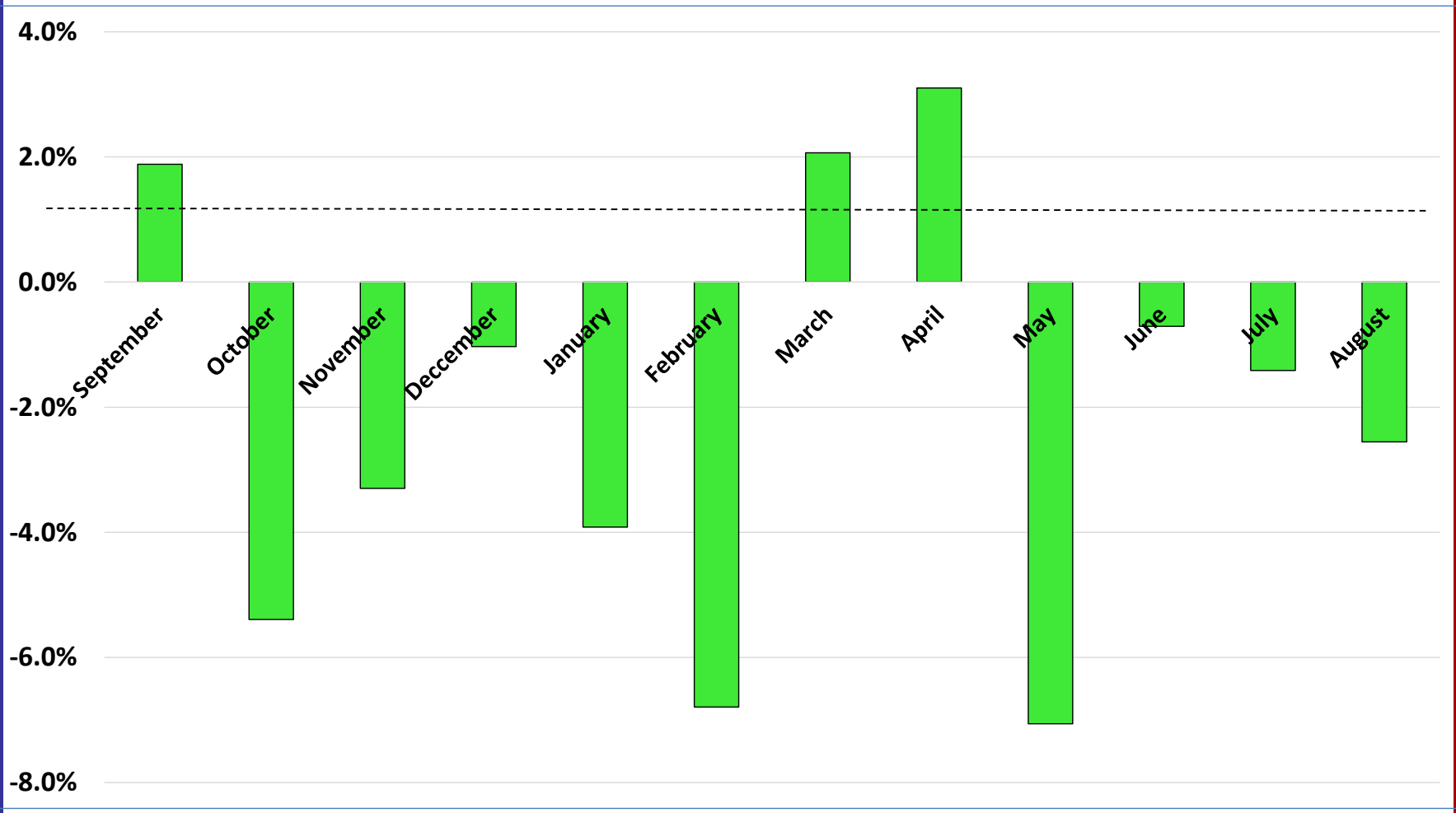
Fiscal 2016

| | 2016 Projected Revenues | Actual 2016 Revenues | Difference |
|-------------------------|-------------------------------|-------------------------|------------------|
| Sales Tax | \$ 29.1 b | \$ 28.1 b | (\$1.0) b |
| Motor Vehicle Sales Tax | \$ 4.8 b | \$ 4.6 b | (\$0.2) b |
| Franchise Tax | \$ 3.5 b | \$ 3.9 b | \$0.4 b |
| Severance Taxes | \$ 2.7 b | \$ 2.3 b | (\$0.4) b |
| Other Taxes | \$ 6.8 b | \$ 6.8 b | \$0.0 b |
| Non Tax Revenue | <u>\$ 6.3 b</u> | <u>\$ 7.0 b</u> | <u>\$ 0.6 b</u> |
| Total | \$ 53.3 b | \$52.6 b | (\$0.6) b |



Monthly Sales Tax Growth, FY 2016

Percent Change from the Same Month in the Prior Year



State General Revenues

Fiscal 2016

| | 2016 Projected Revenues | Actual 2016 Revenues | Difference |
|-------------------------|-------------------------------|-------------------------|-----------------|
| Sales Tax | \$ 29.1 b | \$ 28.1 b | (\$1.0) b |
| Motor Vehicle Sales Tax | \$ 4.8 b | \$ 4.6 b | (\$0.2) b |
| Franchise Tax | \$ 3.5 b | \$ 3.9 b | \$0.4 b |
| Severance Taxes | \$ 2.7 b | \$ 2.3 b | (\$0.4) b |
| Other Taxes | \$ 6.8 b | \$ 6.8 b | \$0.0 b |
| Non Tax Revenue | <u>\$ 6.3 b</u> | <u>\$ 7.0 b</u> | <u>\$ 0.6 b</u> |
| Total | \$ 53.3 b | \$52.6 b | (\$0.6) b |

State General Revenues

Fiscal 2016

| | 2016 Projected Revenues | Actual 2016 Revenues | Difference |
|-------------------------|-------------------------------|-------------------------|-----------------|
| Sales Tax | \$ 29.1 b | \$ 28.1 b | (\$1.0) b |
| Motor Vehicle Sales Tax | \$ 4.8 b | \$ 4.6 b | (\$0.2) b |
| Franchise Tax | \$ 3.5 b | \$ 3.9 b | \$0.4 b |
| Severance Taxes | \$ 2.7 b | \$ 2.3 b | (\$0.4) b |
| Other Taxes | \$ 6.8 b | \$ 6.8 b | \$0.0 b |
| Non Tax Revenue | <u>\$ 6.3 b</u> | <u>\$ 7.0 b</u> | <u>\$ 0.6 b</u> |
| Total | \$ 53.3 b | \$52.6 b | (\$0.6) b |

State General Revenues

Fiscal 2016

| | 2016 Projected Revenues | Actual 2016 Revenues | Difference |
|-------------------------|-------------------------------|-------------------------|-----------------|
| Sales Tax | \$ 29.1 b | \$ 28.1 b | (\$1.0) b |
| Motor Vehicle Sales Tax | \$ 4.8 b | \$ 4.6 b | (\$0.2) b |
| Franchise Tax | \$ 3.5 b | \$ 3.9 b | \$0.4 b |
| Severance Taxes | \$ 2.7 b | \$ 2.3 b | (\$0.4) b |
| Other Taxes | \$ 6.8 b | \$ 6.8 b | \$0.0 b |
| Non Tax Revenue | <u>\$ 6.3 b</u> | <u>\$ 7.0 b</u> | <u>\$ 0.6 b</u> |
| Total | \$ 53.3 b | \$52.6 b | (\$0.6) b |

State General Revenues

Fiscal 2016

| | 2016 Projected Revenues | Actual 2016 Revenues | Difference |
|-------------------------|-------------------------------|-------------------------|-----------------|
| Sales Tax | \$ 29.1 b | \$ 28.1 b | (\$1.0) b |
| Motor Vehicle Sales Tax | \$ 4.8 b | \$ 4.6 b | (\$0.2) b |
| Franchise Tax | \$ 3.5 b | \$ 3.9 b | \$0.4 b |
| Severance Taxes | \$ 2.7 b | \$ 2.3 b | (\$0.4) b |
| Other Taxes | \$ 6.8 b | \$ 6.8 b | \$0.0 b |
| Non Tax Revenue | <u>\$ 6.3 b</u> | <u>\$ 7.0 b</u> | <u>\$ 0.6 b</u> |
| Total | \$ 53.3 b | \$52.6 b | (\$0.6) b |

Comptroller Hegar Comments

We finished fiscal 2016 with \$651 million less for general purpose spending than we estimated in the CRE. While that's a significant number, it's only 1.3 percent below estimate. Texas continues to grow, only at a more moderated pace.

Looking to 2017

- Official state projections estimate an ending balance of \$4.1 billion in general revenues, which the Comptroller advises may be lower
- Very little risk of an actual deficit, however...
- Medicaid will likely require a supplemental appropriation near \$1 billion of general revenue



Looking Ahead to 2018-19

\$ Billions

2016-17 2018-19 Difference

| | | | |
|--------------------|-------|-------|---------------|
| Beginning Balance | \$8.3 | \$4.1 | (\$4.2) |
| Highway Dedication | \$0.0 | \$5.0 | (\$5.0) |
| Average "Growth" | | | ~ \$5.0 - 6.0 |

The Outlook for 2018-19

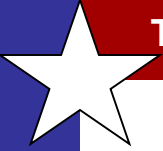
(i.e. the 2017 Legislature)

- The state will have less money available than it did last session (although it didn't spend all it had then)
- The state will be several billions of dollars short of the cost of maintaining existing service levels
- With \$10 billion in the Rainy Day Fund, the big political fights will be over:
 - Which programs to cut,
 - Whether to use budget “gimmicks”,
 - How to raise money without “raising taxes,” and
 - Whether to use the Rainy Day Fund.

Economic Development

Chapter 313

- Chapter 313 of the Tax Code allows school districts to offer a temporary limitation on the taxable value of new investment projects,
- Chapter 313 is the subject of tremendous criticism as “costly corporate welfare”
- TTARA has a review draft available of a study demystifying Chapter 313



School Finance



Interim Charges to House Public Education and Appropriations Committees

- **Two-day hearing** of House Public Education and Appropriations Committees will be held on **September 28-29** in the Appropriations Committee hearing room.
- Invited testimony on September 28.
- Public testimony on September 29.



Additional State Aid for Tax Reduction “ASATR”

- **“ASATR”** is state aid sent to school districts to enable them to maintain the level of state and local revenue per weighted student they had before their rates were compressed by a third in 2006.
- ASATR will **expire on September 1, 2017**.
- ~800 districts have recouped the revenue through the formulas coupled with increased values.
- ~ 200 districts still receive **\$236 million**.



Additional State Aid for Tax Reduction “ASATR”

- School districts still receiving ASATR (~200) will see their available revenue drop.
- There will be efforts to **extend ASATR** and/or phase it out. There will also be a large effort to **let it expire** on schedule.
- If ASATR expires on September 1, 2017, taxpayers in districts receiving a large percentage of revenue from ASATR will more than likely see a **tax increase in the 2017-2018 school year.**

Additional State Aid for Tax Reduction “ASATR”

| School District | Percent of Funding from ASATR | Current M&O Tax Rate | Tax Rate to Recoup ASATR w/o Recapture |
|-----------------------|-------------------------------|----------------------|--|
| Webb CISD | 49% | \$0.80 | \$0.50 |
| Franklin ISD | 46% | \$0.93 | \$0.29 |
| Seminole ISD | 43% | \$1.04 | \$0.24 |
| Kelton ISD | 38% | \$0.71 | \$0.07 |
| Driscoll ISD | 37% | \$1.04 | \$1.42 |
| Goliad ISD | 32% | \$1.04 | \$0.41 |
| Leon ISD | 30% | \$0.88 | \$0.32 |
| Wink-Loving ISD | 29% | \$1.04 | \$0.16 |
| Loop ISD | 22% | \$0.85 | \$0.11 |
| Glen Rose ISD | 19% | \$0.84 | \$0.10 |
| Grandview Hopkins ISD | 18% | \$0.97 | \$0.15 |

Data Source: TEA ASATR17dpe and FM17dpe files; TTARA calculations

Recapture

- **Houston ISD** will be subject to recapture in the 2016-2017 school year for the first time. Initial estimate is **\$175 million**.
- Houston ISD has to obtain **voter approval** to send a payment to the state and has put a proposition on the **November 8** ballot.
- If voters do not approve the payment, the Commissioner of Education must **detach business property** to other school districts until the required wealth level is met.

Recapture

If the election on November 8 fails it is unclear when “detachment” would finally take effect.

1. After votes are canvassed (by Nov. 22), Commissioner orders detachments. Preliminary numbers indicate **\$20.4 billion value** to detach **out of approx. \$51 billion** real commercial, industrial, utility value (**40%**). Property is detached for **M&O and I&S purposes**.
2. Commissioner notifies each affected school district and the appraisal district in which the property is located.
3. Chief appraiser sends a notice to the owner of properties **taxable in a different school district as a result of the detachment and annexation.**
4. Annexing district's tax rate can be up to **\$0.15 higher.**

Recapture

- Legislative options to remove Houston ISD from recapture:
 1. Raise the recapture threshold without raising the basic allotment – would increase equity gap;
~hundreds of millions of dollars annual state cost
 2. Raise the recapture threshold and the basic allotment equally; **~\$4 billion annual state cost**
 3. Deduct **optional homestead exemption** value from school district's value for state funding purposes;
~\$400 million annual state cost for existing exemptions

School Facilities

- Fast Growth school districts will be seeking relief from the “**\$0.50 test**”
- May be an effort to combine \$1.17 M&O rate and \$0.50 debt rate into **\$1.67 rate** that can be allocated between M&O and I&S at the school board’s discretion



School Choice

Tax Credit for Scholarship

- Allows a taxable entity to make a contribution to a “certified organization” to be used for educational scholarships for students to attend a public or private school, and claim a credit against the entity’s franchise tax or state premium tax liability.
- Limited to low income and foster care students.
- Limited to \$100 million in first year with 10% increase each subsequent year.

Bills in 84th Legislature

- SB 4 by Larry Taylor** - Passed Senate; left pending in House Ways and Means
- SB 642** by Bettencourt - Rolled into SB 4
- HB 895** by Rick Miller - Left pending in House Ways and Means
- HB 1043** by Bohac-Miller - Left pending in House Ways and Means
- HB 3594** by Rick Miller - Left pending in House Ways and Means

Nevada and Florida have this program

Taxpayer Savings Grant

- Establishes a program to reimburse parents for private school tuition. Grant amount is 75% of the state average maintenance and operations expenditures per student (~\$6,100).
- Limited to low income and foster care students.
- Limited to \$50 million per year.

Bills in 84th Legislature

- SB 4 by Larry Taylor** - Passed Senate; left pending in House Ways and Means
- SB 276** by Donna Campbell - Rolled into SB 4

Similar to the Nevada Educational Savings Account Program which is under a court injunction

SB 1760 and Dallas ISD

- **SB 1760:** Order by a school board setting a tax rate that exceeds the sum of the effective M&O tax rate of the district and the district's current debt rate must be a **record vote, and at least 60 percent of the members of the school board must vote in favor of the ordinance,** resolution, or order. Sec. 26.05(b) Tax Code
- On August 18 **Dallas ISD** school board **voted 5-4** to raise the M&O rate from \$1.04 to \$1.17 which would have triggered a tax ratification election.
- **Needed a vote of 6-3** to comply with provisions of SB 1760, so the measure failed. Adopted a rate of \$1.04.

SB 1760 and Dallas ISD

- School Board President was the swing vote that prevented the TRE election
- A new school board member had to be sworn in the next week which triggered re-election of officers
- School board members **voted to replace the President** who prevented the TRE



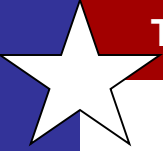
Sales Tax

O&G Compressor Taxability

- March 15, 2016 – Audit division memo to all audit personnel concerning gas compressors
 - Exempt
 - Boost pressure for sales purposes
 - Connected to multiple pieces of equipment that do more than extract water
 - Taxable
 - Stand-alone – no other equipment in immediate vicinity
 - Used to enhance production
 - Connected to dehydrator or other equipment that removes water or condensation

O&G Compressor Taxability Cont..

- June 1 Revision
 - Taxpayers will be given opportunity to provide evidence on the purpose and location of each compressor and other equipment and to calculate divergent use if the compressor performs both an exempt processing and a non-exempt transportation function
 - Compressors that support equipment that removes water or condensation for the purpose of transporting the gas will be considered taxable
 - Not a statement of agency policy but procedural guidance to improve audit consistency in certain common situations
 - If there is uncertainty, the case along with any evidence produced by the taxpayer is to be submitted to Audit Division's upper management for a final determination
- TTARA letter expressing concerns, especially with the lack of guidance on acceptable documentation and a methodology measuring compressor "output"
- Meeting to discuss in the works



Property Tax

Appellate Cases Status Update

- Scheduled for Supreme Court oral argument:
 - Nov. 9 – *Valero Refining v. Galveston CAD* (Case #15-0492)
 - Can pollution control property be excluded in the valuation methodology in an equal and uniform appeal of refinery property accounts that did not include such property?
 - 14th Court of Appeals reversed the trial court by holding that evidence was insufficient to exclude pollution control property because Valero's valuation method did not provide a basis for doing so and the fact that pollution control property was not included in the accounts at issue and was partially exempt was no basis for exclusion

Appellate Cases Status Update Cont..

- *Dec. 6 – ETC Marketing v. Harris CAD (#15-0587)*
 - Is natural gas temporarily stored in Texas during its transport out-of-state taxable or exempt as goods in interstate commerce?
 - 1st Court of Appeals upheld trial court by ruling the gas was taxable even if it was in interstate commerce because the taxpayer failed to demonstrate a lack of substantial nexus as required by the first prong of the *Complete Auto* standard
 - TTARA filed *amicus* in support of the review petition so the Court could address the issue of improperly considering factors pertinent to income and sales tax nexus in determining nexus for property tax purposes

Appellate Cases Status Update Cont..

- Supreme Court Request for Consolidated Briefing on the Merits:
 - *EXLP & EES Leasing v. Galveston CAD* (Case #15-0683)
 - *Ward CAD v. EXLP & EES Leasing* (Case # 15-0965)
 - *Reeves & Loving CADs v. MidCon Compression* (Case # 15-0969)
 - *Reeves & Loving CADs v. Valerus Compression* (Case # 15-0970)
 - *Loving CAD v. EXLP & EES Leasing* (Case # 15-0971)
- Trial courts held valuation methodology unconstitutional as applied and determined situs to be in county where compressors were in use
- 8th and 14th Court of Appeals upheld situs ruling
- 8th Court reversed unconstitutional valuation ruling saying that CADs had not meet burden of proof on valuation issue and the legislature has discretionary authority to enact a special valuation methodology for heavy equipment inventory
- 14th Court reversed and remanded valuation issue because evidence was not presented to conclusively resolve valuation
- AG *amicus* asserted that a statute is presumed constitutional and that constitutional reasonableness is a question of law and not of fact to be determined by a jury

Appellate Cases Status Update Cont..

- 3rd Court of Appeals oral argument scheduled Sept. 28:
 - *City of Austin v. Travis CAD* (Case #03-16-00038-CV)
 - Appeal of District Court ruling of lack of jurisdiction to hear challenge of level of appraisal of commercial real property and vacant land and constitutionality of equal and uniform appeals

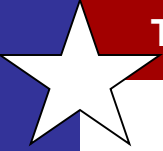
Senate Select Committee Update

- Additional hearings under consideration
- TTARA testimony at San Antonio hearing emphasized our high property taxes and the taxation of business personal property
- TTARA Houston hearing testimony, including recommendations for improvement, addressed two issues: problems with the administration of transportation reinvestment zones and deficiencies of the current TNT process
- Indications are that Committee's report is likely to include:
 - Lowering the rollback limit and requiring a ratification election to exceed it
 - Improving ARBs, especially requiring more training
 - Eliminating the ability of taxing jurisdictions to contest the level of appraisal of a class of property
 - Preservation of equal and uniform appeals
 - Tightening provisions relating to the creation, operation and oversight of special districts



Notable Events

- TTARA “Truth-in-Taxation” research report explaining the how local governments set their property tax rates
- Emphasized the TNT process:
 - provides an important checks-and-balances mechanism
 - does not provide automatic protection from rising taxes
 - requires active taxpayer participation in the rate setting process
- TTARA op-ed stressing that protesting valuations is only first part of controlling property taxes and that participation in budget and tax rate adoption hearings is essential
 - Published in a number of newspapers including Dallas and Austin
- Lawsuit challenging the validity of Dimmit County’s 2015 tax rate due to miscalculation of incremental value in transportation reinvestment zones being prepared
- TTARA Property Tax Committee Meeting Sept. 20



Franchise Tax

Franchise Tax Rule 3.584

- Standards for who is a “wholesaler/retailer” and eligible for the half rate
- Wholesaler/Retailer cannot “produce” more than half of what they sell
- Taxpayer is the “producer” of an item if:
 - You process it in such a way to add 10 percent to its value, or
 - You produce any tangible personal property that is incorporated into the final product

Franchise Tax Rule 3.584

- Comptroller held roundtable discussion on August 4 at TTARA's request
- TTARA, COST, and other associations and taxpayers shared comments
- TTARA commented that the 10 percent test should apply to the value of TPP added
- COST commented on the disparity of how software is treated relative to other TPP

Franchise Tax Rule 3.584

- Agency is still evaluating comments, but is not likely to substantially change its proposed language

Draft Rules Proposals



Draft Comptroller Sales Tax Rules Proposals

- 3.280 Aircraft (new)
- 3.292 Repair, Remodeling, Maintenance and Restoration of Tangible Personal Property
- 3.297 Carriers, Commercial Vessels, Locomotives and Rolling Stock



Thanks for Joining Us!

If you have any questions or comments, please feel free to contact TTARA staff.

| | |
|--|---|
| Franchise Tax & State Budget: Dale Craymer | <u>dcraymer@ttara.org</u> |
| Sales & Property Tax: John Kennedy | <u>jkennedy@ttara.org</u> |
| School Finance: Sheryl Pace | <u>space@ttara.org</u> |
| Property Tax: Debbie Cartwright | <u>dcartwright@ttara.org</u> |
| Property Tax: George Christian | <u>gchristian@ttara.org</u> |
| Communications: Ryan Ash | <u>ryan@ttara.org</u> |
| Office Manager: Betty Wranischar | <u>bwranschar@ttara.org</u> |
| Membership: Nancy Shields | <u>nshields@ttara.org</u> |