

TTARA Webcast Update

November 9, 2017

TEXAS TAXPAYERS
TTARA
AND RESEARCH ASSOCIATION

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We will enter the State Bar of Texas credit, but accountants and tax professionals need to submit their credit to those organizations.

Agenda

- 1. TTARA Dates of Interest**
- 2. Budget/Finance Update**
- 3. School Finance**
- 4. Property Tax**
- 5. Sales Tax**
- 6. Franchise Tax**
- 7. Economic Development**

TTARA Annual Meeting

November 30 & December 1
at the JW Marriott Austin

We will feature speakers on a broad range of prominent tax and fiscal issues, including the following elected officials:

- Lt. Governor Dan Patrick
- Comptroller Glenn Hegar
- Speaker of the House Joe Straus
- Sen. Select Committee on Property Tax Reform Chair Paul Bettencourt
- House Appropriations Chair John Zerwas
- House Ways and Means Chair Dennis Bonnen
- House Economic & Small Business Development Chair Angie Chen Button
- Harris County Judge Ed Emmett



TTARA Annual Meeting Cont..

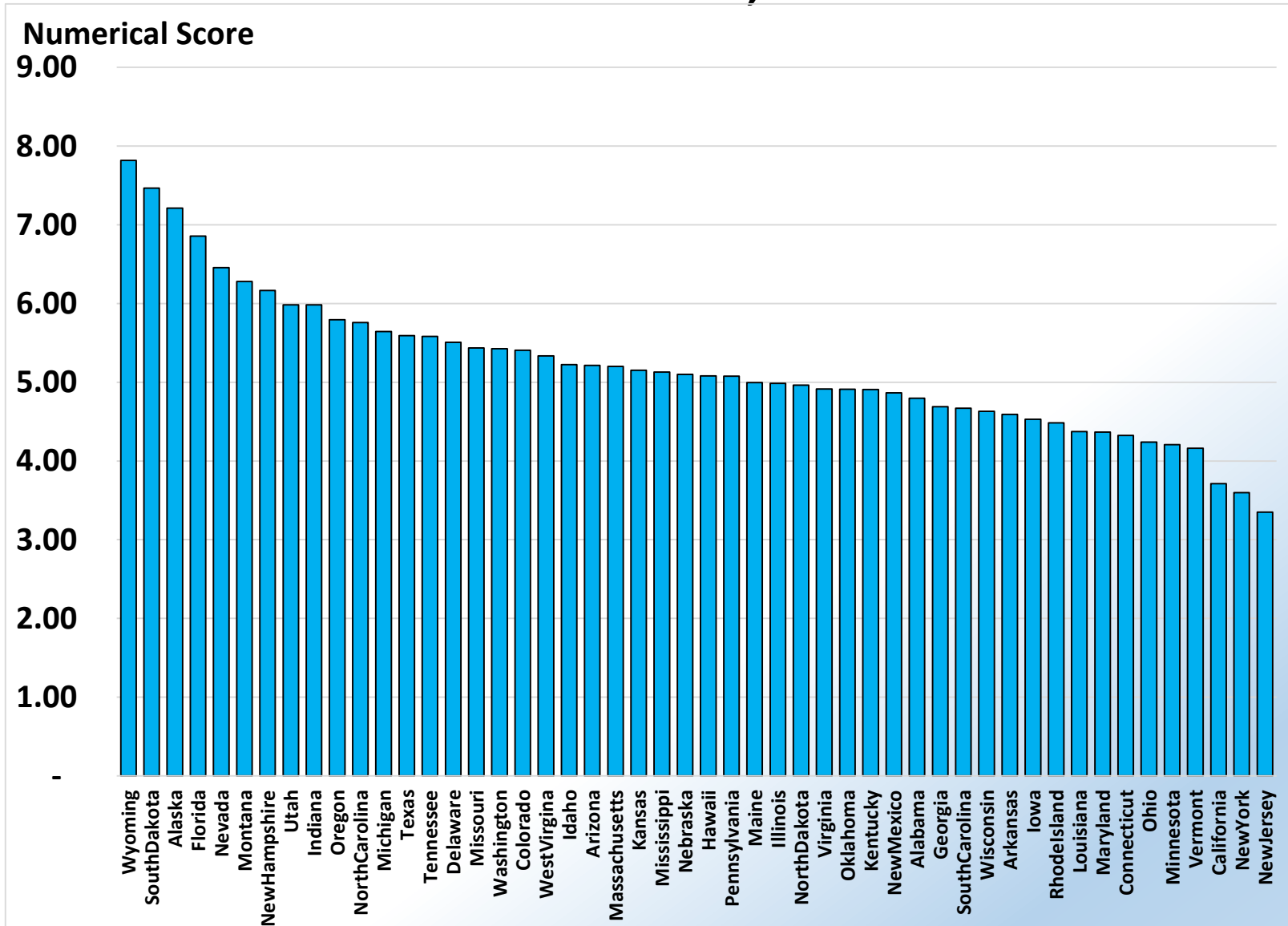
- Registration information is available on our website at <http://www.ttara.org/?q=page/annualmeetingregistration>
- You can still reserve a room at the JW Marriott by calling (844)473-3959

Budget/Finance



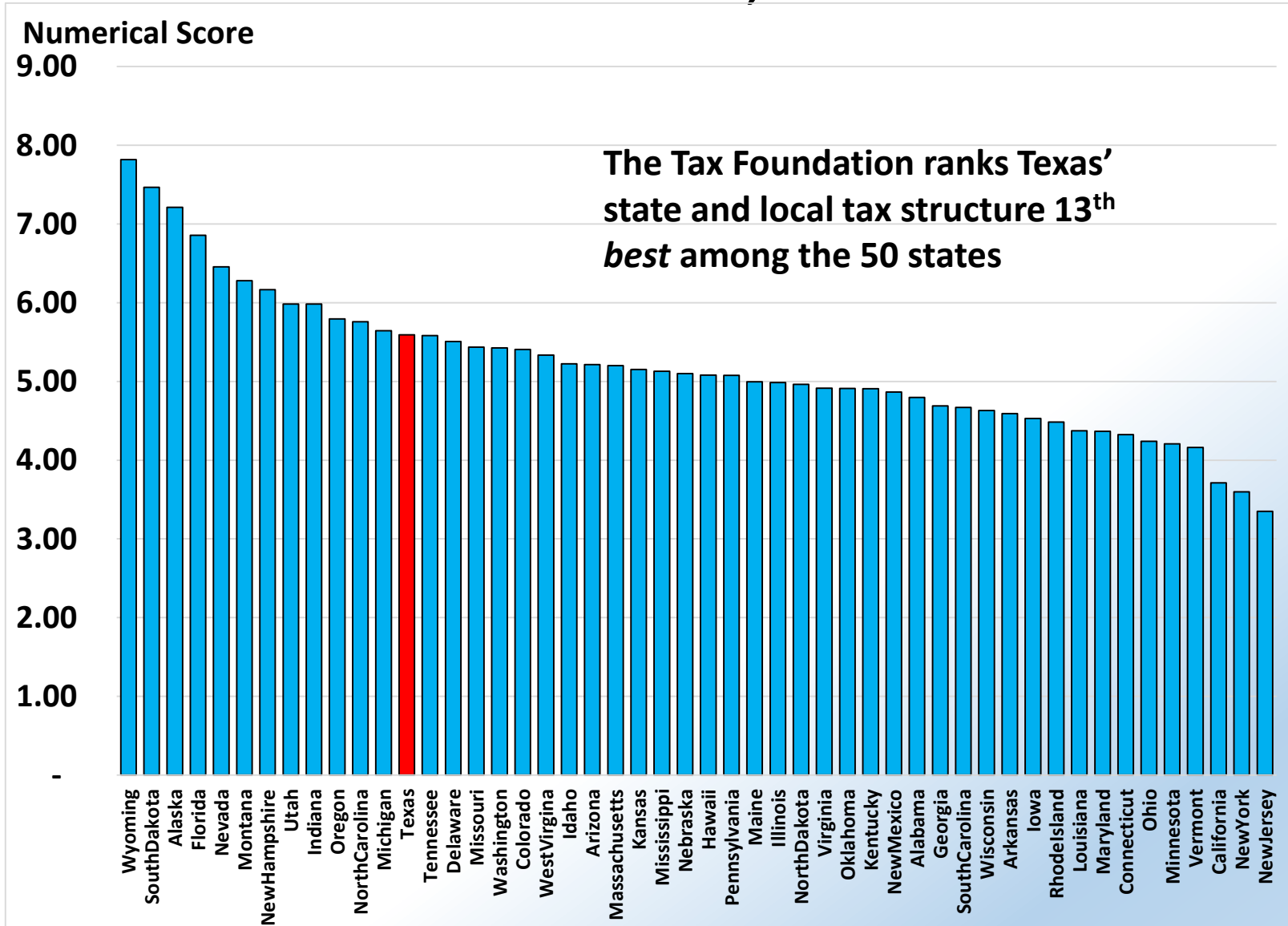
State Business Tax Climate

Tax Foundation, 2018



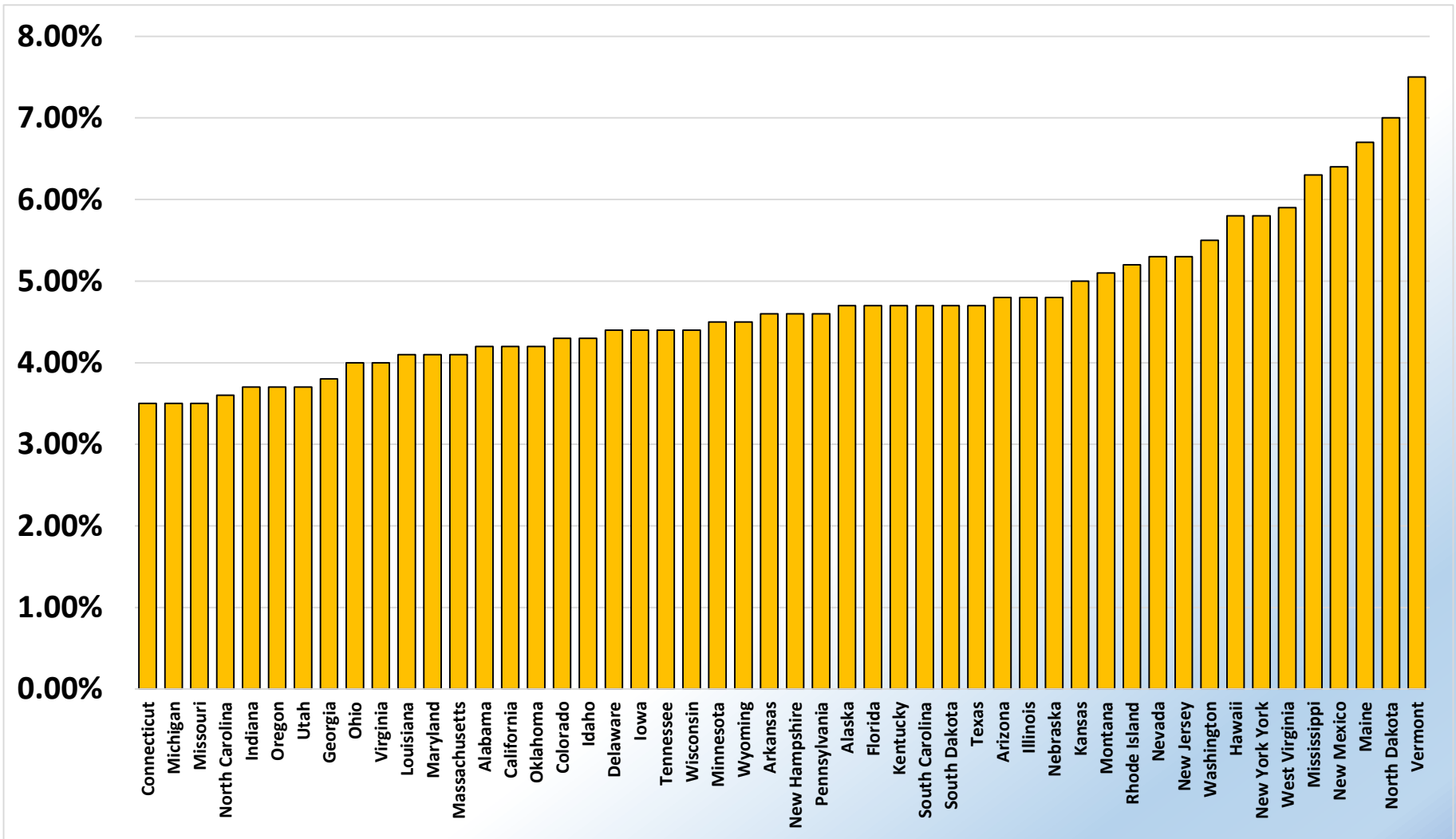
State Business Tax Climate

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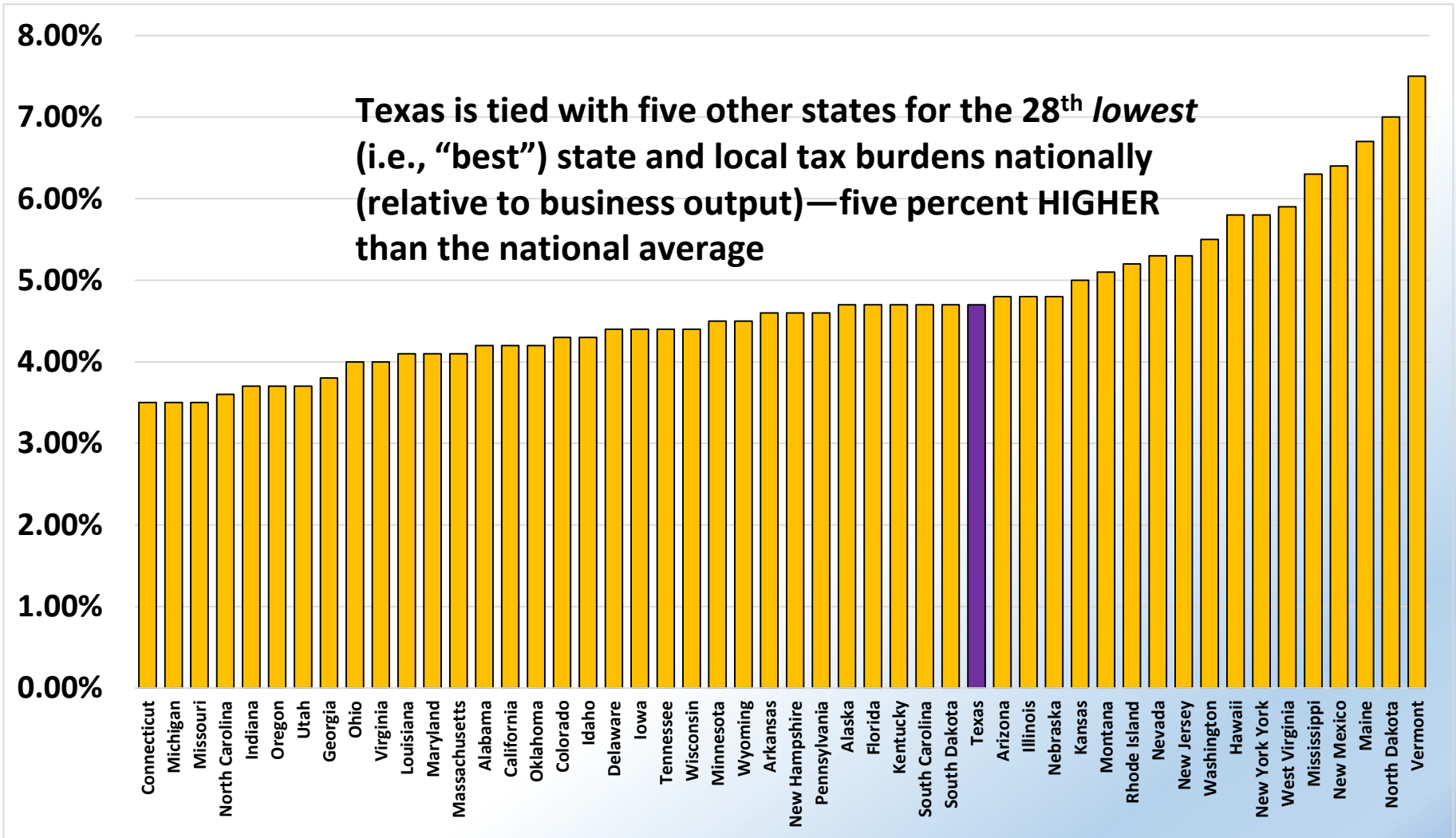
States Ranked by S&L Taxes Paid

Relative to Economic Output



States Ranked by S&L Taxes Paid

Relative to Economic Output

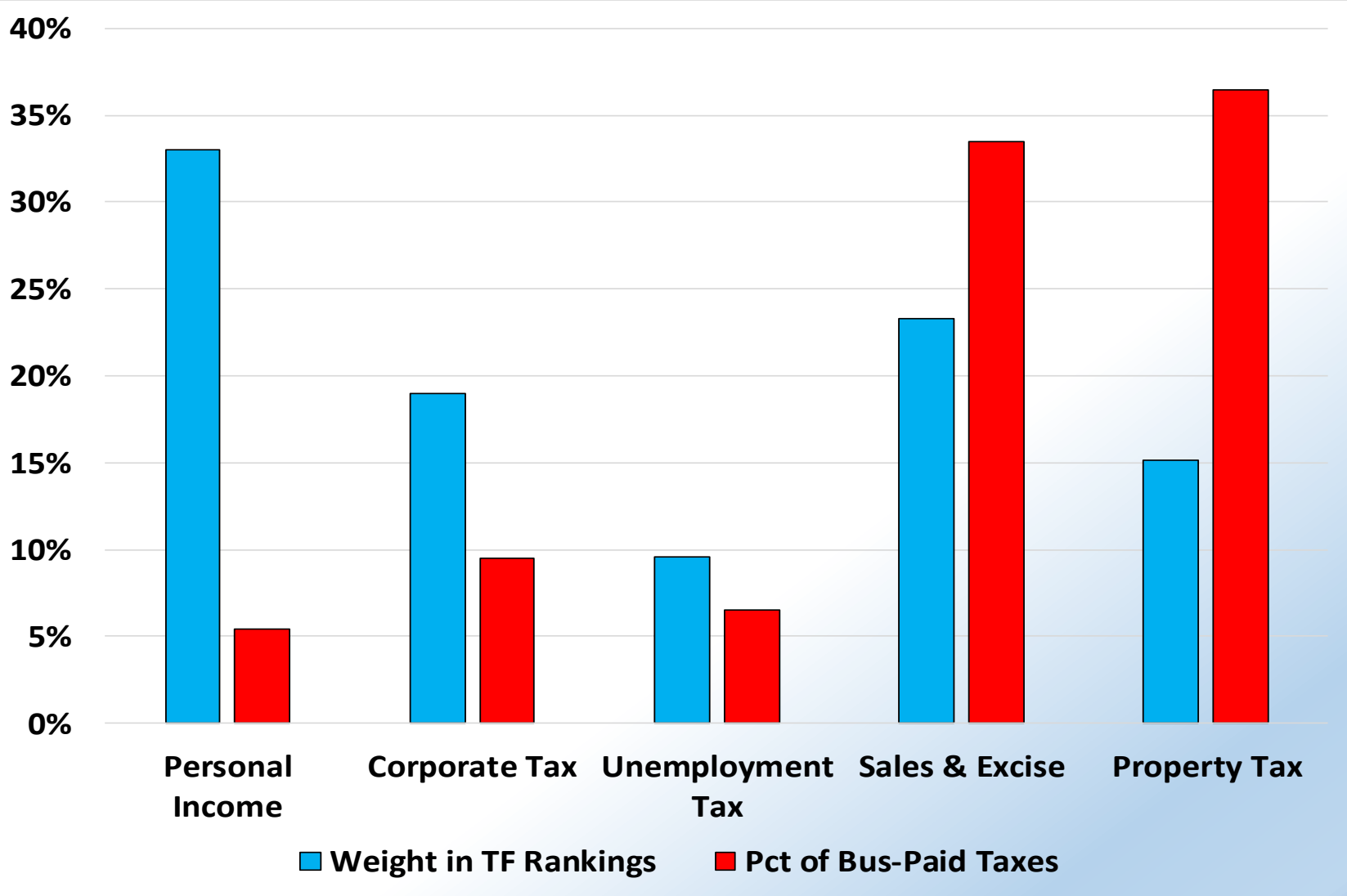


Why does Texas rank so well with the Tax Foundation when actual state and local tax liabilities are so high relative to other states?

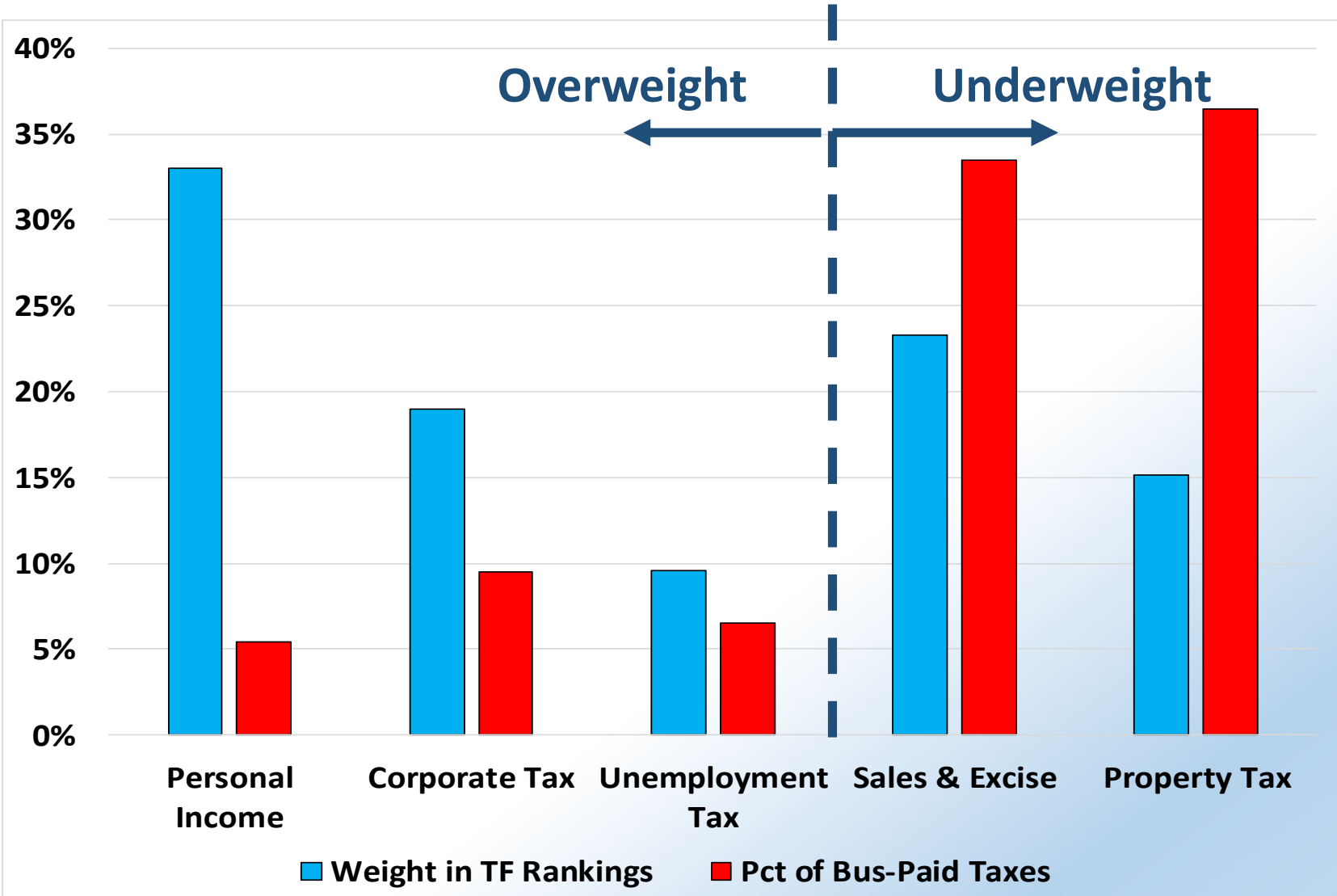
Key Points About the TF Rankings

- The Tax Foundation does not include certain taxes and revenues, such as natural resource and gaming taxes in their assessment
- States without a major tax (particularly a personal income tax) are rewarded in the rankings
- The rankings look only at the *structure* of a tax and do not take into direct account the *size of the tax check*.
- Texas, which scores well because of the lack of a personal income tax (a tax which business generally does not pay), is penalized by the franchise, or “margin,” tax, rated as the 49th best corporate tax.

Tax Foundation Weights

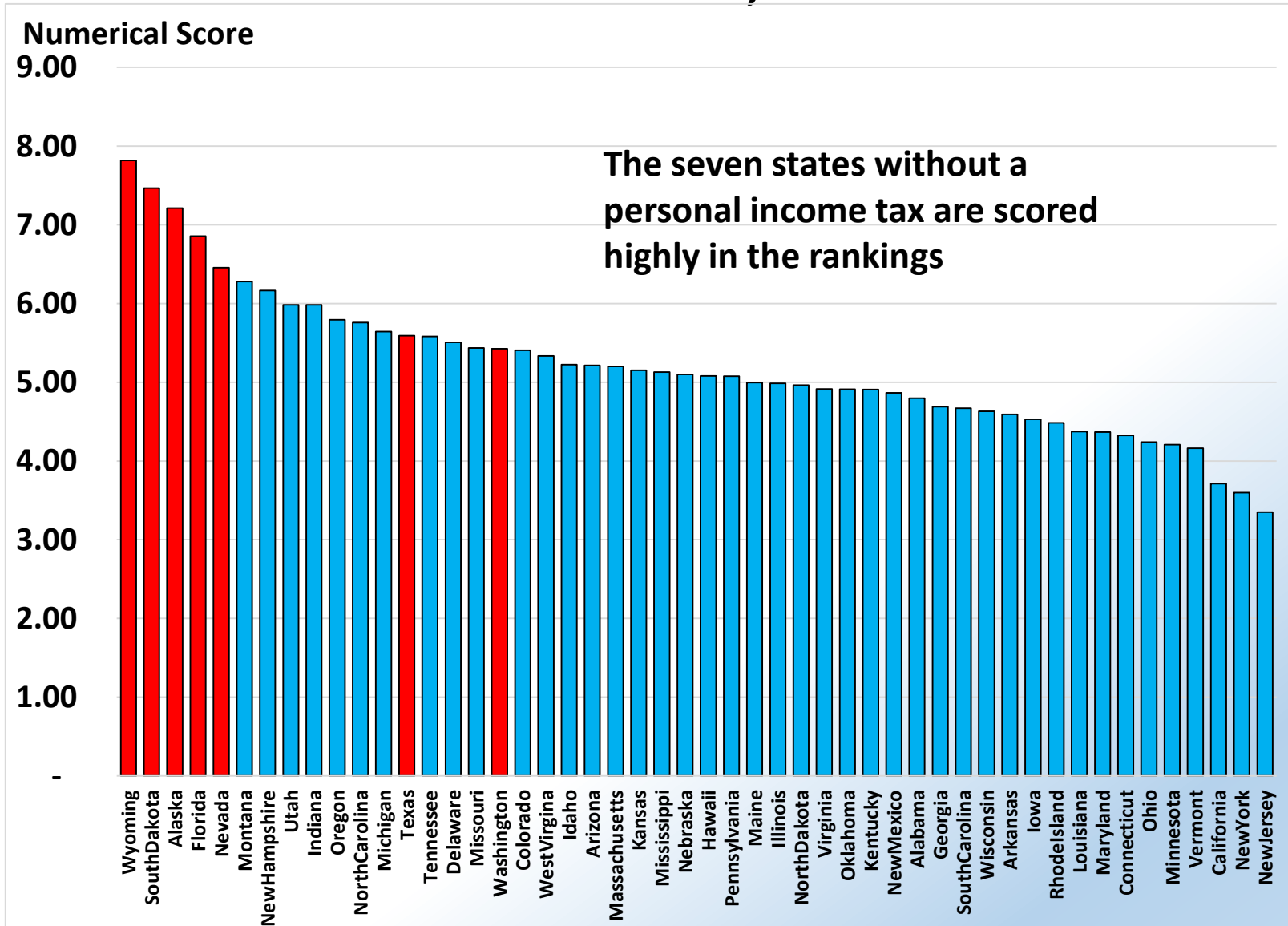


Tax Foundation Weights



State Business Tax Climate

Tax Foundation, 2018



2018-19 Budget and Certification Revenues

Beginning Balance	\$8.3	\$0.9	(\$7.4)
Current Revenues	103.1	111.8	8.8
Reserve for ESF/Hwy Transfer	(\$2.3)	(\$3.4)	(1.0)
Hwy-Dedicated Sales Tax	\$0.0	(\$3.2)	(\$3.2)
Change in Dedicated Account Balances	<u>(\$0.5)</u>	<u>\$1.2</u>	<u>\$1.7</u>
Total Available Revenues	\$108.5	\$107.3	(\$1.2)
Total Spending	<u>(\$107.6)</u>	<u>(\$107.2)</u>	(\$0.4)
Ending Balance	\$0.9	<\$0.1	

Source: Comptroller's Certification Revenue Estimate for 2018-19.

Two “Must-Do” Items Before the State Closes the Books on 2018-19

1. Medicaid: The budget does not fully fund the projections of Medicaid costs—an item which could cost roughly an additional \$2 billion or more, and
2. Disruption from Hurricane Harvey could trigger additional public education costs by near \$2 billion (more on this later).

Implications for the 2019 Legislature

- A supplemental appropriations bill totaling in the billions of dollars drawn from the Economic Stabilization Fund
- A VERY tight budget session as lawmakers wrestle with the overhang of using one-time measures to balance the current budget
- No property tax relief unless other taxes are raised to pay for it
- No further “hard number” franchise tax reductions likely

Interim Charges

An interim charge is the assignment of a particular research topic to a committee, often in anticipation of future legislation.

Charges are assigned to committees by each chambers presiding officer—the Speaker and the Lt. Governor.

House and Senate charges show heavy focus on Hurricane Harvey, aftermath and recovery

House Select Committee on Economic Competitiveness

Byron Cook, Chair

Senfronia Thompson

Angie Chen Button

Sarah Davis

Charlie Geren

Joe Moody

Rene Oliveira

The committee will look at issues such as workforce readiness, infrastructure and state and local economic development tools. The committee will also study the reasons that employers give for choosing, or not choosing, to do business in a particular state.

2 hearings anticipated: November 15 and December 5; invited testimony only.

Final report due by December 12, 2017.

Selected House Interim Charges of General Interest

Appropriations

- Use of the Economic Stabilization Fund
- Use of one-time funding and deferral measures in the 2018-19 Budget

Economic and Small Business Development

- Evaluate long term workforce needs of the state's businesses and how to address them
- Analyze current data on the regional distribution of the use of incentives
- Study how to enhance aerospace and defense manufacturing in Texas (with Defense & Veterans' Affairs)

Selected House Interim Charges of General Interest, *continued*

Energy Resources

- Examine how commercial wind facilities are decommissioned and whether landowner property rights are protected
- How to improve roads impacted by energy exploration and development

Selected Senate Interim Charges of General Interest

Finance

- Examine options to increase the investment earnings of the Economic Stabilization Fund
- Evaluate disparity of interest charged on delinquent taxes versus interest on refunds of taxes overpaid

Natural Resources and Economic Development

- Assess unnecessary regulatory barriers to economic growth

School Finance



Senate Interim Committee Charges

Senate Education Committee

- **Teacher Compensation** - Study compensation strategies for classroom teachers and make recommendations to elevate the teaching profession and to attract, retain, and reward teachers.
- **Mandate Relief/Innovation** - Review, modify, or abolish chapters of the Education Code. Specifically study cost-drivers, unnecessary mandates, reduction/elimination of inefficiencies, focus on policies or opportunities targeted to improving student outcomes, and better utilization of taxpayer resources.

House Interim Committee Charges

House Appropriations Committee

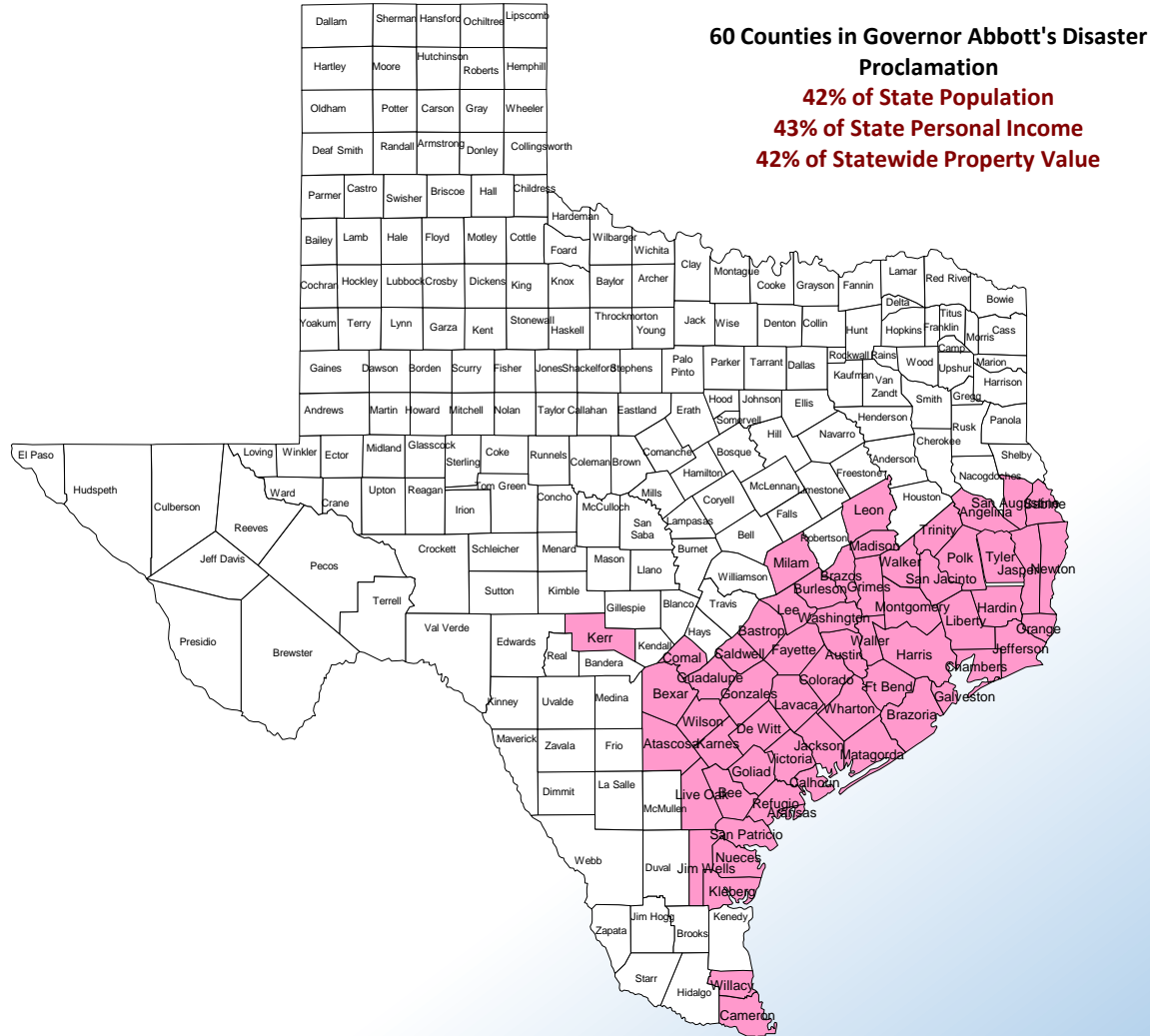
- **Hurricane Harvey** - Examine use of federal funds.
- **TRS Care** - Study the sustainability of TRS-Care and consider options for funding retired teacher health care in Texas, especially as it pertains to contributions being based on active employee payroll rather than the cost of health care.
- **Monitor the Impact of TEA's Reinterpretation of Regulations Related to the Local Option Homestead Exemption.**
 - * Stems from Commissioner's decision to deduct 50% of local option homestead exemption value when calculating property wealth level for recapture, but not for purposes of state aid for non property wealthy districts.
 - * La Feria ISD, Joaquin ISD and Equity Center v. Mike Morath, No. D-1-GN-17-001385. Currently in Third Court of Appeals.

House Interim Committee Charges

House Public Education Committee

- Determine the scope of financial losses resulting from **Hurricane Harvey** and recommend state actions to mitigate negative impacts on school districts.
- Recommend measures to prevent unintended consequences in the state **accountability system as a result of Hurricane Harvey**.
- Review mechanisms for identifying and **rewarding educators** through state-level strategies.
- Examine research-based options for **evaluating student achievement** beyond standardized test scores.
- Review the **charter school system**.

Hurricane Harvey Disaster Area-60 Counties



School Districts and Charters in Disaster Area

	# Districts and Charter Schools	# Students (millions)	\$ Recaptured (millions)	\$ State Aid (millions)
Disaster Area	363	2.09	\$581.6	\$7,865.5
Statewide	1,234	5.03	\$2,023.6	\$20,563.3
Percentage in Disaster Area	29%	41%	29%	38%

State Education Costs due to Hurricane Harvey

	FY 2018 Est. Cost (millions)	FY 2019 Est. Cost (millions)	Supplemental Appropriation Request (millions)
Increased state aid for taking in displaced students . Districts must apply to TEA.	\$380.0	(\$380.0)	\$380.0
Hold harmless for decline in students . One-time adjustment for 2017-2018 school year. \$150 million lost recapture \$250 million state aid <i>Education Code Sec. 42.0051</i>	0	\$400.0	\$250.0
Replace lost M&O property tax collections <u>not due to reappraisals</u> with state aid.	TBD Feb. 2018	0	TBD Feb. 2018

State Education Costs due to Hurricane Harvey

	FY 2018 Est. Cost (millions)	FY 2019 Est. Cost (millions)	Supplemental Appropriation Request (millions)
<p>Replace lost M&O property tax collections due to reappraisals of 2017 property values.</p> <p>Spring Branch ISD, Conroe ISD, Katy ISD, Lamar CSD, La Porte ISD</p> <p><i>Education Code Sec. 42.2523</i></p>	0	TBD	TBD
<p>Property wealthy districts that owe recapture can deduct from the recapture owed repairs to facilities and other costs <u>not reimbursed by insurance or FEMA.</u></p> <p><i>Education Code Sec. 41.0931</i></p>	\$474.0 (max. est.)	\$500.0 (max. est.)	\$974.0 (max. est.)

State Education Costs due to Hurricane Harvey

	FY 2018 Est. Cost (millions)	FY 2019 Est. Cost (millions)	Supplemental Appropriation Request (millions)
<p>Districts that do not owe recapture are entitled to a reimbursement for repairs to facilities not reimbursed by insurance or FEMA only if excess funds are available or the Legislature makes a specific appropriation.</p> <p><i>Education Code Sec. 42.2524</i></p>	\$0	\$0	TBD

State Education Costs due to Hurricane Harvey

	FY 2018 Est. Cost (millions)	FY 2019 Est. Cost (millions)	Supplemental Appropriation Request (millions)
Additional students eligible for free and reduced price lunch (comp. ed. weight). All for two months and thereafter being classified as homeless.	\$186.0	\$80.0	\$266.0
Additional students eligible for pre-k due to being classified as homeless.	TBD	TBD	TBD
Education Service Center assistance to school districts	\$1.0	\$1.0	\$2.0
TOTAL ESTIMATED COST 2018-2019 Biennium (millions)			\$1,872 (Maximum)

Rollback Rate Calculation in Disaster Area

- **Section 26.08(a) of the Tax Code** exempts school districts in Disaster Zone from Tax Ratification Elections:

... “When increased expenditure of money by a school district is necessary to respond to a disaster, including a tornado, hurricane, flood, or other calamity, but not including a drought, that has impacted a school district and the governor has requested federal disaster assistance for the area in which the school district is located, **an election is not required under this section to approve the tax rate adopted by the governing body for the year following the year in which the disaster occurs.**”

- Cannot exceed \$1.17 M&O tax rate cap.
- The **exemption would apply to the 2018-19 school year.**
- If you have property in one of these school districts, you may want to monitor the tax rate adoption process next summer.

Texas Commission on Public School Finance

- HB 21 by Huberty created a **13-member “Texas Commission on Public School Finance”** to make recommendations for improvements to the current public school finance system. The Commission’s report is due on December 31, 2018.

? 4 Governor appointees

1. At large member
2. Current or retired classroom teacher w/10+ yrs. exp.
3. Member of the business community
4. Member of the civic community

✓ 4 Lt. Governor appointees – three Senators and one school administrator or school board member

1. Senate Education Chair **Larry Taylor** (R-Friendswood)
2. Senator **Paul Bettencourt** (R-Houston)
3. Senator **Royce West** (D-Dallas)
4. Dr. **Doug Killian**, Superintendent, Pflugerville ISD

Texas Commission on Public School Finance (continued)

- ? **4 Speaker appointees** – three House members and one school administrator or school board member

- ✓ **One State Board of Education member**, appointed by the SBOE chair
 1. **Keven Ellis**, Chiropractor from Lufkin

Property Tax

Disaster Recovery

Reappraisals Authorized by Taxing Units

Cities: Fulshear, Katy, The Woodlands, Montgomery, and Shore Acres

Counties: Fort Bend and Montgomery

School Districts: Katy ISD, LaPorte ISD, and Spring Branch ISD

Special Districts: MUD 346 (Harris County), Montgomery County Emergency Services District #8, and Montgomery County Hospital District

Hypothetical Reappraisal Timeline

- September 14 webcast—eight month period suggested
- Included delivery of new notices of appraised value
- Tax Code Section 25.19 appraised value notice required if value increases, property on roll for the first time, or an exemption is canceled or reduced
- No statutory requirement for new notices for disaster reappraisal when values **decrease**
- Due process: Texas Constitution Art. VIII, Sec. 21(c) requiring the legislature to provide, with reasonable exceptions, notices of “revaluation”; also Sec. 20 prohibiting property tax assessment at a “greater value than its fair cash market value”

Senate Interim Committee Charges

Select Committee on Property Tax Reform

- **Hurricane Harvey Response** - Evaluate how property tax law can advance disaster recovery and ensure taxpayer protection from excessive taxation and spending; and study statutory changes to allow disaster spending from TIRZ funds for infrastructure recovery
- **Voter Engagement** – Study ways to enhance voter engagement in local government decisions around budgets and property tax rates through digital and social media

Senate Interim Committee Charges

Select Committee on Property Tax Reform (continued)

- **Tax Rate and Appraisal Reform** – Evaluate the effective tax rate and rollback tax rate calculations and identify modifications; evaluate the operations of appraisal review boards and training of board members; determine whether ARBs and/or chief appraisers should be elected
- **Property Tax Data** – Evaluate whether existing libraries of property tax data and collection methods are adequate

Senate Interim Committee Charges

Select Committee on Property Tax Reform (continued)

- **Lowering Property Tax Burden** – Study the feasibility of replacing property tax with sales tax or other consumption tax, with emphasis on school maintenance and operations tax; evaluate whether some local property taxes lend themselves to a swap more than others; quantify the short-term and long-term economic impact of a tax swap; and identify a target property tax rate and evaluate how to reach the target with a consumption tax swap

Senate Interim Committee Charges

Senate Finance Committee

- **Property Tax on Business Personal Property** – Evaluate the tax as it applies to bpp and the current \$500 exemption; quantify the economic impact of property tax on bpp; and evaluate the burden on taxpayers and local governments of administering the tax
- **Interest Rate Disparity** – Evaluate the rate of interest charged on delinquent property taxes as compared to the rate of interest paid on property tax refunds; identify best practices among other states; and recommend a plan and timeline to reduce interest rate disparity

Senate Interim Committee Charges

Senate Intergovernmental Relations Committee

- **Special Purpose District Bond Reform** – Study state agency review of tax exempt bonds issued by special purpose and public improvement districts used to finance water and sewer infrastructure; examine disparity in feasibility review of bonds backed by property-based assessments and those backed by ad valorem taxes; and make recommendations to ensure continued stability of Texas tax-exempt bond market
- **Municipal Management District Uniformity** – Determine whether standardized language for the creation of municipal management districts would provide conformity to accepted standards and contain appropriate taxpayer oversight

House Interim Committee Charges

House Special Purpose Districts Committee

- **Water District Bonds** - Review state approval and oversight of water district bonds that finance utility, infrastructure, and other projects; and identify improvements to state oversight
- **Dissolution of Special Purpose Districts** - Investigate feasibility of dissolving special purpose districts; and make recommendations for requirements and procedures
- **Municipal Management Districts** - Identify best practices in creation of municipal management districts; and study the feasibility and make recommendations for creating standard language for the creation of these districts through special law

House Interim Committee Charges

House Ways and Means Committee

- **Review Impact of Hurricane Harvey** – Feasibility of requiring reappraisal after disasters for property tax purposes and identify improvements to the tax-rate setting process
- **Review Property Tax System** – Identify improvements to:
 1. Transparency and communications with taxpayers
 2. Tax-rate setting process
 3. Training and expertise of appraisal review boards
 4. Composition, structure, and process of ARBs
 5. Appeals of ARB orders

Recent Judicial Activity

EXLP Leasing LLC and EES Leasing LLC v. Galveston County Appraisal District (Case # 15-0683)

- Oral arguments before Texas Supreme Court on Oct. 10
- Principal issue: whether special appraisal for dealers' heavy equipment inventory (Tax Code Section 23.1241) that is held for rental or lease is constitutional
- Distinction raised between Art. VIII, Section 1(a) dealing with property being taxed "in proportion to its value" as determined by law and Art. VIII, Section 20 stating that property shall not be assessed "at a greater value than its fair cash market value"
- Possible expansion of legislative authority to dictate value in ways different than market value as defined by Tax Code

Recent Judicial Activity

EXLP Leasing LLC and EES Leasing LLC v. Galveston County Appraisal District (continued)

- Issues addressed in argument
 1. Rational basis for inventory appraisal methodology
 2. Precedent establishing market value meaning of constitutional language
 3. Use of “fair cash market value” term
 4. Situs
- Impact on hundreds of other cases and valuation of compressors and other heavy equipment inventory

Sales Tax

Sales Tax Interim Charges

House Ways & Means Committee

- Monitor litigation to overturn the Bellas Hess and Quill decisions, thereby granting states the authority to collect sales and use taxes from remote retailers.

Senate Select Committee on Property Tax Reform

- Lowering Property Tax Burden: Study the feasibility of replacing the property tax with sales tax or other consumption tax revenue, with emphasis on school maintenance and operations tax. Evaluate whether some local property taxes lend themselves to a swap more than others. Quantify the short-term and long-term economic effects of a tax swap. Identify a target property tax rate and evaluate how to reach that target with a consumption tax swap.

Remote Seller Use Tax Collection

- Colorado reporting law (“rat-em-out”) upheld in 2016 by 10th Circuit (*Direct Marketing Association v. Brohl*) – Supreme Court denied *cert.*
- Justice Kennedy stated it was time to revisit *Quill* and Justice Gorsuch in 10th Circuit concurring opinion predicted that many if not all states could be expected to follow Colorado’s lead
- Ten states have enacted reporting law and half of those have taken effect since the Colorado ruling: AL, LA, RI, VT, WA joining CO, KY, OK, SD, TN
- SB 1713 by Uresti
 - Filed version required sales “facilitators” to collect and established “economic nexus” test – \$500,000 or 1,000 sales
 - In response to TTARA’s Senate Finance testimony, committee sub removed economic nexus test and added out-of-state seller notices to buyers and reporting of sales to Comptroller
 - Floor amendment changed bill to require report by Comptroller but it died in Ways & Means

Sales Tax for Property Tax Swap

The Numbers

- Property Taxes
 - Total \$56.1 B
 - City 9.2
 - County 9.0
 - School 29.9 – 23.7 M&O – 6.2 I&S
- Sales Tax
 - All State Taxes \$49.6 B
 - Sales Tax 28.9
 - Per 1¢ Tax Rate 4.6
- HB 285 by Murr (1st C.S.) – 12% state sales tax to replace school M&O
- HJR 21 by Darby (1st C.S.) – Prohibited school districts from levying an M&O property tax beginning Jan. 1, 2021.

Sales Tax for Property Tax Swap

The Numbers

- Exemptions \$34.6 B
 - Taxed by Other Law 13.8
 - Manufacturing 13.0
 - Groceries/Drugs/Utilities 5.1
 - Agricultural 0.7
 - Government/Non-Profits 0.4
 - Everything Else 1.6
- Exclusions 7.1 B
 - Health Care 2.3
 - Legal 0.5
 - Architectural 0.5
 - Auto Repair 0.4
 - Labor 0.9
 - Everything Else 2.5

Sales Tax for Property Tax Swap

Policy Issues

- Economic Impacts
 - Individuals – Businesses – Competitiveness
- State and Local Finance
 - State or local tax?
 - Local financial control
 - Revenue distribution
 - Revenue volatility
 - Debt service
- Tax Administration
 - Avoidance
 - Compliance
- Key Issues Summary – <http://www.ttara.org/files/document/file-56c4aa5e370e0.pdf>
- Policy Briefing – <http://www.ttara.org/files/document/file-56c4aaa29ce95.pdf>



Proposed Comptroller Rules Update

§3.308. Computers – Hardware, Computer Programs, Services, & Sales

- Published in Texas Register July 30 (42 TexReg 3346)
- Comment period ended August 30
- Agency has been evaluating comments received
- Planned release in near future

Franchise Tax

Franchise Tax Interim Charges

Senate

- No interim charge directly related to the franchise tax

House

- Committee on Ways & Means
 - Review the franchise tax and identify any changes that would improve the state's business climate

Future Franchise Tax Legislation?

Senate Bill 17 (85:R)

- Phased out the franchise tax incrementally and proportionally reduced all rates of the tax
- One-half of future revenue growth in excess of 5 percent each biennium

House Bill 28 (85:R)

- Phased out the franchise tax incrementally and proportionally reduced all rates of the tax
- The first \$3.5 billion of any cash balance at the end of future biennia

Comptroller Rule Drafts

Proposed Franchise Tax Rule Amendment

- 3.588 Margin: Cost of Goods Sold:
 - Incorporates language from HB 500 (83:R) by Hilderbran relating to movie theaters and pipelines
 - Adopts definitions of “labor,” “material,” and “project”
 - Provides that “ownership” of goods may be based on legal title
 - Clarifies that rental or leasing companies may deduct as cost of goods sold only expenses relating to the items the company rents or leases (from the court decision in *Hegar v. Sunstate*)

Comptroller Rule Drafts, *continued*

3.588 Margin: Costs of Goods Sold (*continued*):

- This proposed rule amendment was published in the Texas Register on September 29th
- The published rule incorporates our suggestions by removing a new definition of “production,” adjusts the “legal title” ownership language, and explains how the new definitions of “labor” and “materials” comply with the recent court decisions in *CGG Veritas* and *Newpark*

Comptroller Rule Drafts, *continued*

3.588 Margin: Cost of Goods Sold (*continued*):

- The public comment period is over and the Comptroller is currently reviewing additional requested changes from other parties
- By the end of November, the Comptroller's office expects to complete its review and determine whether it will hold a roundtable discussion on the proposed changes

Tax Amnesty

State Budget, Article 9, Sec. 17.11

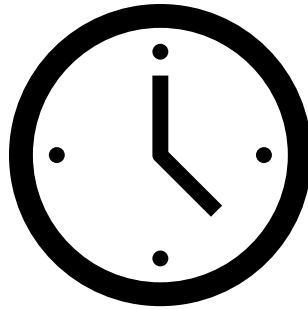
- Comptroller will implement a tax amnesty program allowing a waiver of penalty and/or interest for voluntary reporting by delinquent taxpayers who owe taxes
- Comptroller's office is still reviewing how this program will be implemented and it is expected to start sometime next year

Economic Development

Economic Development

- Interim charges not as far reaching as previous legislatures
- No direct charges on:
 - **Chapter 313** (school tax abatements: expires December 31, 2022) or
 - **Chapter 312** (city/county tax abatements) expires September 1, 2019.
- Texas 2050, a coalition of business associations, chambers of commerce, and cities and counties is working to inform legislators of the benefits of Chapter 312

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If you have trouble locating the certificate, contact Ryan at ryan@ttara.org and he will send you a copy.

Thanks for Joining Us!

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

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