Testimony before the Senate Committee on Finance

Property Tax Relief

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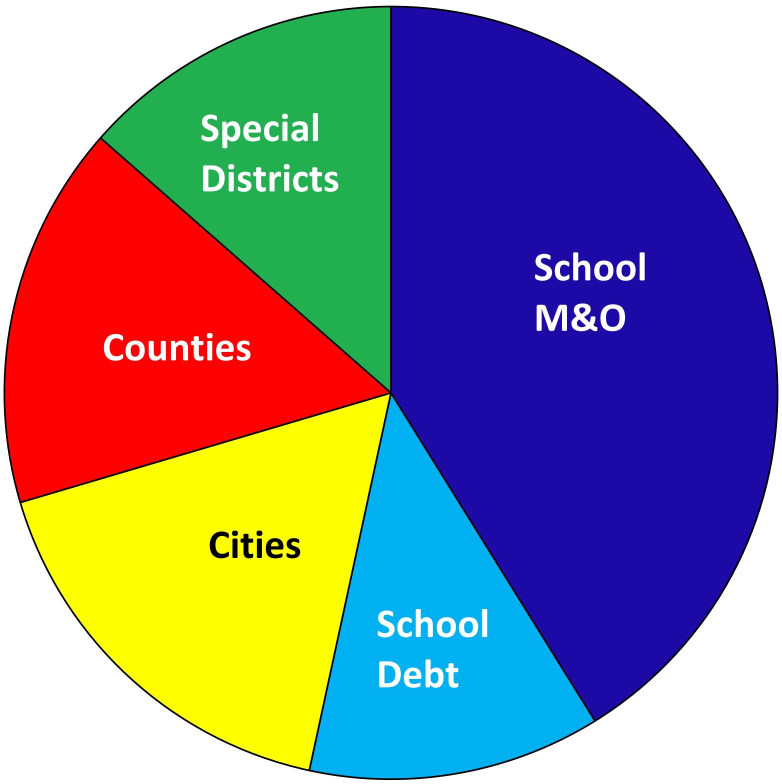
Committee Charge

Property Tax Relief: *Examine and recommend ways to reduce Texans' property tax burden. Review and report on proposals to use or dedicate state revenues in excess of the state spending limit to eliminate the school district maintenance and operations property tax.*

Tax Exemptions: *Examine Texans' current tax exemptions and report on whether adjustments are merited because of inflation or any other factors.*

Who Levies the Property Tax in Texas, 2021



2021 Tax Levy ($bl)	
School M&O	$30.1
School Debt	$8.9
Cities	$12.5
Counties	$11.7
Spec Dists	$9.9
Total	$73.1

In Texas, the property tax is the domain of local governments. The Constitution prohibits the state from levying a property tax.

In 2021, Texas property taxes totaled $73.1 billion, over half of which (53 percent) was levied by school districts for both maintenance and operations and for debt service.

City property taxes were $12.5 billion, or 17 percent of the total.

County property taxes were $11.7 billion, or 16 percent of the total.

Property taxes levied by special purpose districts (districts for the support of hospitals, junior colleges, water, wastewater, etc.) were $9.9 billion, or 13.5 percent of the total.

The Property Tax Equation:

Appraised Value
*** Tax Rate**
= Tax Revenue

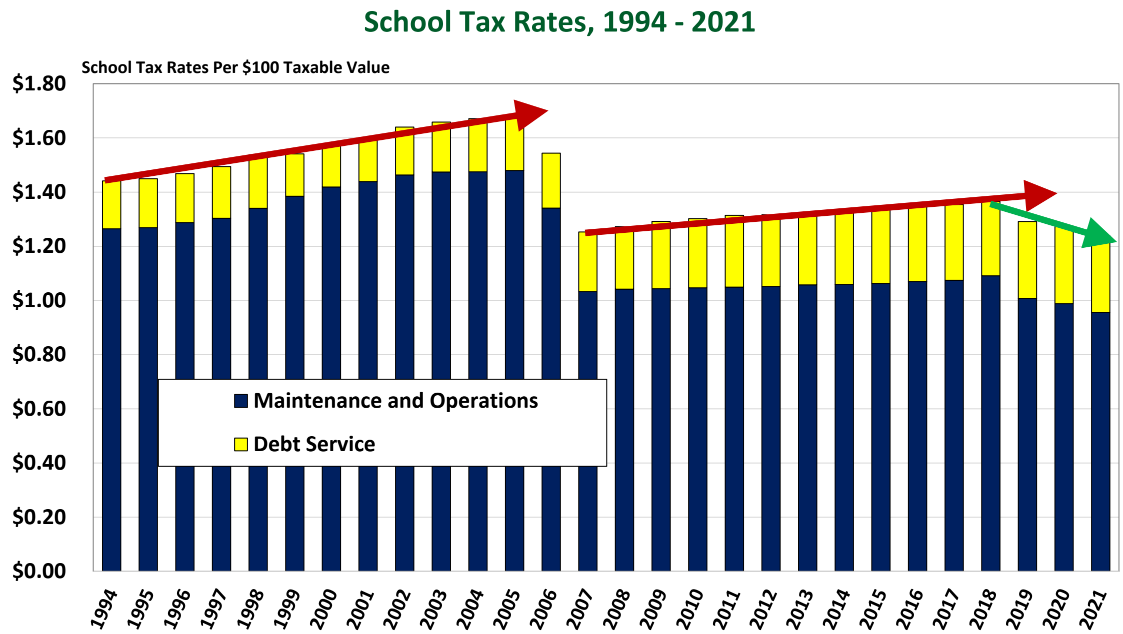
In recent years, the legislature has acted to restrain the ability of local governments to raise tax revenue – the product of the equation. In 2019, lawmakers passed HB 3 by Huberty/Taylor, which reformed school finance and school property taxes, and SB 2 by Bettencourt/Burrows, which limited the ability of cities, counties, and special districts to raise property taxes without voter approval. As a result of the two bills, jurisdictions must get voter approval before they can impose a property tax rate that raises their revenues by more than:

- 3.5% for Cities, Counties, and Most Special Districts[1]
- 8.0% for Junior Colleges and Hospital Special Districts
- 2.5% for School Districts[2]

[1] Jurisdictions may generally exceed these percentages without voter approval if the tax rate raises less than $500,000, which is defined as a "de minimis" amount.
[2] School districts may impose an additional tax rate up to $0.05 without voter approval, which most have done. With voter approval an additional $0.12 of tax rate may be levied.

HB 3 Is Working

School District Tax Rates Are Falling



HB 3 generally maintains the state share of public education funding while compressing, or cutting, local school district property tax rates. This is a departure from the prior school finance system in which local value growth made districts "property-wealthier" resulting in lower state aid rather than lower tax rates.

Essentially, a school district's value growth above 2.5 percent per student is used to compress their tax rate for maintenance and operations (excluding enrichment). For example, a district's property value per student grows by 10 percent. Its compression percentage is calculated at 1.025/1.100, or .9318. That is multiplied by the school district's tax rate from the previous year to determine the base M&O rate they are to levy this year (enrichment and debt taxes are then added to yield the total tax rate):

Prior Year Tax Rate per $100 (excluding enrichment and debt service)		$0.9300
State Value Growth Threshold (as an index)	1.025	
Current Year Value Growth (as an index)	÷ 1.100	
Equals Compression Percentage		x 0.9318
Current Year Base M&O Tax Rate		= 0.8666

Note: The above is a simplification. An additional calculation applies to districts in which the taxable value increases less than the state's projected value growth.

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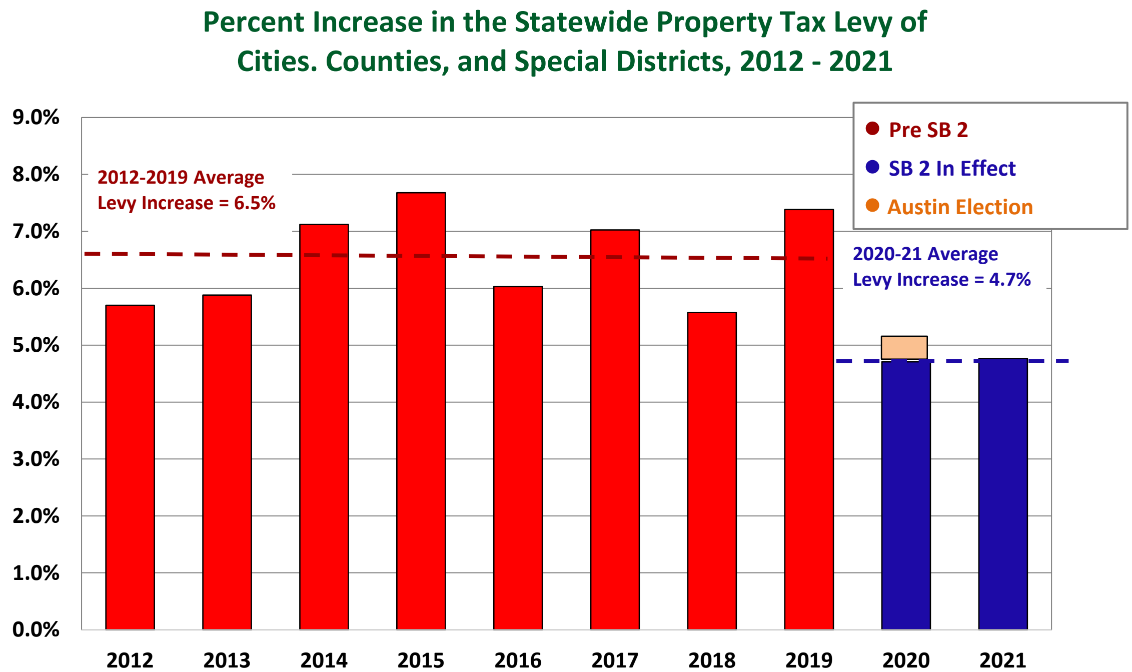
SB 2 Is Working

City/County/Special District Levies Are Falling



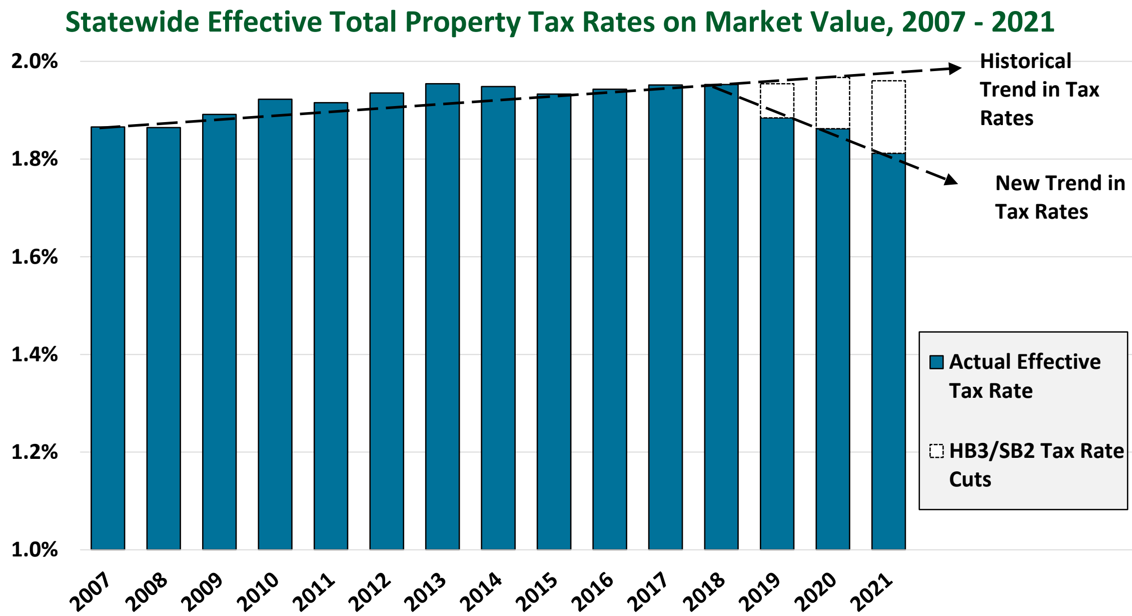
SB 2 limited the ability of cities, counties, and special district to raise their property taxes without voter approval. The bill passed in 2019 but did not take effect until the 2020 tax year.

From 2012 through 2019, cities, counties, and special districts raised property taxes on an annual basis by an average of 6.5%.

Excluding a voter-approved 24% tax hike in Austin in 2020 for a major transportation initiative, city, county, and special district levies increased at an annual average of 4.7% in 2020 and 2021 – almost two percentage points below the historical trend.

HB 3 and SB 2 Are Working

Property Tax Rates are Dropping



Texas properties have a single market value assigned it; however, because of differing exemptions allowed or authorized by the various types of taxing jurisdictions across the state, a single property may have multiple taxable values. To provide a uniform evaluation of tax rates, the above chart is based on the total taxes levied by year against the total market value of property before *exemptions are applied* – essentially presenting an effective property tax rate on market value.

From 2007[3] to 2018, the effective total tax rate on property levied by all jurisdictions rose from 1.87 percent to 1.95 percent, even as appraised values increased.

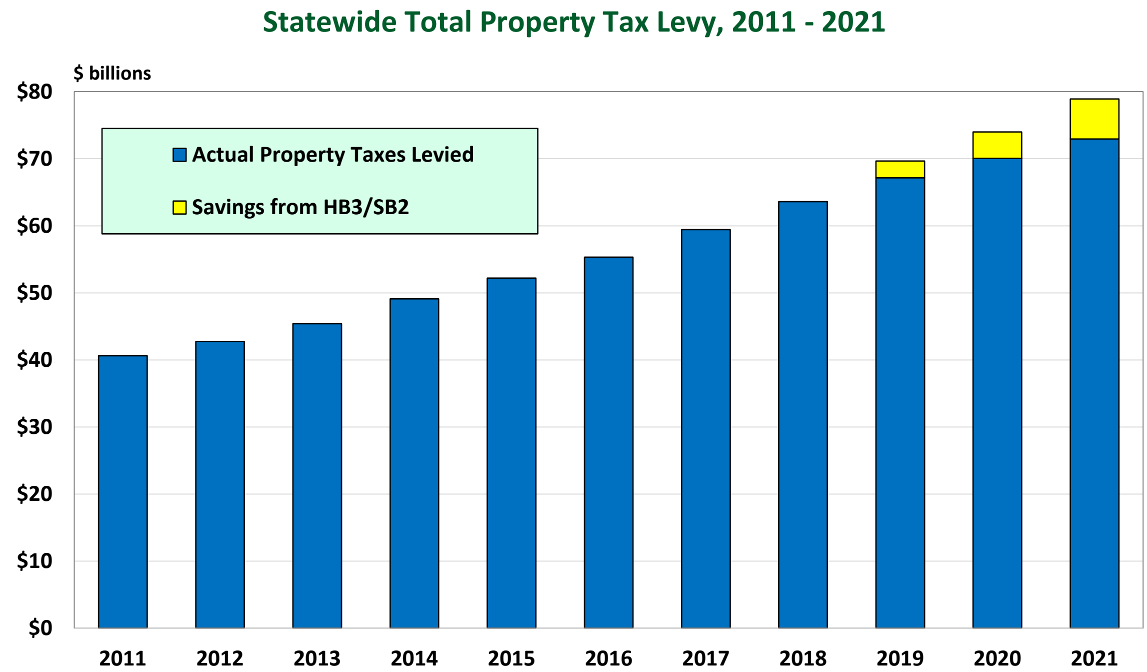
HB 3 in 2019 reduced school tax rates and put in place a mechanism in which future school tax rates would be cut. SB 2, which constrained the ability of cities, counties, and special districts to raise property taxes without voter approval, took effect with the 2020 tax year.

Since 2019, the statewide average effective property tax rate has dropped from 1.95% to 1.81% -- a decline of more than 7 percent in just three years.

[3] In 2006 the legislature passed school finance and tax reforms that reduced school property taxes for maintenance and operations by one-third, phased in over two years. Using 2007 as a base year provides a consistent comparison of tax rates.

HB 3 and SB 2 Are Working In Tandem

The Growth in Taxes Levied Has Noticeably Slowed



Property tax levies continue to rise but are substantially less than they would have been absent the passage of 2019's HB 3 and SB 2.

In combination, the savings from the two bills has grown with each passing year and will continue to do so in the future. In 2021 the bills saved taxpayers $6 billion, shaving 8% from what tax bills would have been.

In 2022, the two bills will provide taxpayers with substantial protection from rising appraisals.

Savings from 2019 Reforms
$ billions

Year	HB 3	SB 2	Total
2019	$2.5	n.a.	$2.5
2020	$3.4	$0.6	$4.0
2021	$4.8	$1.2	$6.0

Source: Texas Taxpayers and Research Association

Property taxes, though increasing, are growing at a slower rate than personal income in Texas and are likely to grow less than the rate of inflation in 2022.

1. ***HB 3 and SB 2 are working*** *to force down tax rates as values rise – the greater the increase in values the lower tax rates must be, absent voter approval*
2. ***A 10% appraisal cap*** *exempts any value increase above 10% from the previous year (note: this protection only applies to homesteads, and does not extend to business or rental properties)*
3. ***Propositions approved on the May ballot****, will:*
   - *raise the homestead exemption, saving the average homeowner roughly $175, and*
   - *reduce school taxes on those over 65 and certain disabled persons.*

In Spite of Rising Appraisals, Many Home-Owners Will Enjoy a ***Lower*** 2022 Tax Bill

An Example from Travis County

	2021	2022	% Cng
Calculate 2022 Tax Rate			
Preliminary (May) Tax Roll	$ 239 bl	$308 bl	29%
Less: New Value	$n.a.	$6 bl	n.a.
Less: Reduced by Appeals (estimated)	$0	$15 bl	n.a.
Estimated Final Value	$239 bl	$287 bl	20%
2021 Tax Revenue	$703 ml		
2022 Revenue (2021 *1.035)		$727 ml	3.5%
M&O Tax Rates	$0.307	$0.253	- 18%
Calculate Homeowner Tax Bill			
Median Home Value	$411,658	$632,208	54%
Less: Exempt by 10% Cap		-$179,384	
Less: 20% Exemption	- $82,332	- $90,565	10%
Taxable Value	$329,326	$362,259	10%
M&O Tax Rates	$0.307	$0.253	- 18%
Tax Bill	$1,011	$917	- 9%

Travis County homeowners, as most across the state, have been stunned by appraisal notices, with the average homestead in Travis County up 54% in 2022 from last year. However, much of that value increase will be exempt due to a 1987 constitutional amendment limiting the growth in a tax appraisal to no more than 10%. Further, those robust appraisals coupled with 2019's SB2, many jurisdictions may not increase their property tax revenues by more than 3.5 percent (and HB 3 limiting school district property tax increases to no more than 2.5 percent), many jurisdictions will be required to cut their tax rates by MORE than 10 percent. Because tax rates may fall faster than taxable values are increasing, tax bills will come down. **Taxes will still likely rise on non-capped residences and on business property,**

Appraisal Caps Shift the Tax Burden

How the City of Austin Raised Taxes in the Name of Tax Relief

Item	2021 with w/ 10% Homestead Exemption (HSE)	2021 w/HSE Increased to 20%	Impact of Raising the Homestead Exemption
Tax Base			
Single Family Residential ($bl)	$86.8	$78.6	- $8.0 bl
Business & Other Property ($bl)	$103.4	$103.4	$0.0 bl
Total Taxable Value ($bl)	$190.1	$182.1	- $8.0 bl
M&O Tax Rate Calculation			
M&O Revenue Desired ($ml)	$779.3	$779.3	$ 0.0
M&O Tax Rate (per $100 of value)	$0.410	$0.428	$0.018
M&O Taxes Due on:			
Single Family Residential ($ml)	$355.8	$337.2	- $18.6
Business and Other ($ml)	$423.5	$442.1	$18.6
Total Taxes Due ($ml)	$779.3	$779.3	$0.0

In 2021 the City of Austin raised their local option homestead exemptions. The standard exemption went from 10% of a homestead's value to 20%. Per the city's estimate, this removed $8 billion of residential property from the tax rolls. The city required a property tax levy of $779 million to fund its adopted budget for maintenance and operations (M&O).

Had the city left the homestead exemption at 10%, its tax roll would have been $190 billion, and it could have raised the desired $779 million with a tax rate of $0.410 per $100 of taxable value.

By raising the homestead exemption to 20%, the city removed an additional $8 billion of residential value from the tax rolls, resulting in a total tax base of $182 billion. In order to raise the desired levy of $779 million, the city adopted a tax rate of $0.428 – a 4.4% higher tax rate because of the homestead exemption.

The net impact of the homestead exemption and the corresponding tax rate was to save homeowners an estimated $18.6 million; however, that savings was not the result of budget cuts, it was financed by $18.6 million in higher property taxes on businesses, rental properties, and other non-homestead properties.

Pros and Cons of Tax Relief Strategies

Tax "Relief" Mechanism	Positive	Negative
School Tax Rate Compression	• Uniform, proportionate relief for all taxpayers. • Does not pick one group of taxpayers as winners over others.	• State must pay 100% of the cost of cutting tax rates.
Increase/Index Homestead Exemption	• Provides some relief to homeowners • More visible to homeowners than rate compression. • Low cost to state because cost may be shifted to other property owners	• May shift taxes rather than cutting them. • Cost of the exemption is offset by higher tax raising taxes on non-homestead properties.
Reduce homestead appraisal cap	• Provides some relief to homeowners that stay in their homes. • More visible to homeowners than rate compression. • Low cost to state because cost may be shifted to other property owners	• Shifts taxes rather than cutting them. • Could create a permanent split roll in which homes are valued differently from other properties. • Cost of the exemption is offset by higher tax raising taxes on non-homestead properties. • Could "lock" people into their homes because selling home loses the exemption.
Extend the appraisal cap to all properties	• Limits growth in certain tax appraisals. • Low cost to state because cost may be shifted to other property owners	• Shifts taxes rather than cutting them. • Similar properties are taxed differently solely based on when property was purchased or put in service. • May create tax avoidance opportunities through ownership structures.

Concluding Thoughts & Recommendations

- **SB 2 and HB 3** from 2019 are proving to be **an effective tool in reducing property tax rates** and limiting city, county, and special district tax increases by forcing down tax rates.

- Despite astronomical increases in single family housing appraisals, **many homeowners will actually see their property tax bills decline in 2022** as a result of a cap on homestead appraisals while appraisals rise on other properties. The costs of the homestead cap will be borne by other property owners.

- **The most effective way to provide proportionate property tax relief for all Texans is to reduce school tax rates**, an approach the Senate took with the engrossment of SB 1 from the 3rd called session of 2021. This could be done by appropriating additional state money to schools using state general revenues to substitute for local property taxes.

- Dedicating revenues in excess of the state's spending limit for school property tax rate reduction is an appropriate and desirable use of state revenues; however, it should not be viewed as a path to eliminating school taxes.

- **Appraisal caps**, and any measures that removes *existing* property from the tax rolls, **do not provide overall tax relief**. They simply shift taxes from one group of taxpayers to another.

- With regards to business taxation, Texas is one of the few states that includes business inventories as a part of the property tax base. Exempting business inventories from the property tax would make Texas more competitive with other states; however, like appraisal caps, the exemption would shift taxes from one group of taxpayers to another. An alternative method of providing inventory tax relief would be to follow Louisiana, which provides tax relief on inventories taxed at the local level by **offering a state corporate income tax credit for local property taxes paid on inventories**.