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# Testimony before the House Committee on Ways and Means

## Property Tax Relief

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# Committee Charge

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*Study and consider methods of providing additional property tax relief, including the use of \$3 billion in available American Rescue Plan Act funds that were held for future tax relief by the 87th Legislature, and other sources of revenue. Explore options to reduce business property tax burdens and options for limiting the growth of property tax bills.*

It is unresolved as to whether ARPA funds may be used for tax relief. ARPA states:

*A state cannot use ARPA funds to “either directly or indirectly offset a reduction in the net tax revenue of such State or territory resulting from a change in law, regulation, or administrative interpretation during the covered period that reduces any tax (by providing for a reduction in a rate, a rebate, a deduction, a credit, or otherwise) or delays the imposition of any tax or tax increase.”*

West Virginia and twelve other plaintiff states sued challenging this provision. On November 15, 2021, the US District Court of the Northern District of Alabama Western Division ruled in favor of the plaintiffs, however that decision is on appeal. Until a final decision in the case is reached, there is a risk that the use of ARPA funds for tax relief may be invalid.

# What Property Is Taxed in Texas?

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Type of Property	Business	Individually Owned
Real Property	Taxed	Taxed
Personal Property	Taxed	Not Taxed

Texas' property tax applies to all real estate (land and improvements). Texas's property tax also applies to tangible personal property (furniture, machinery, supplies, inventories, etc.) used in the "production of income," i.e., business-owned property. Personal property owned by individuals is specifically exempt. Though most, 29, states include business personal as part of the property tax base, it is fully exempt in eight states, and partially exempt in another 13.

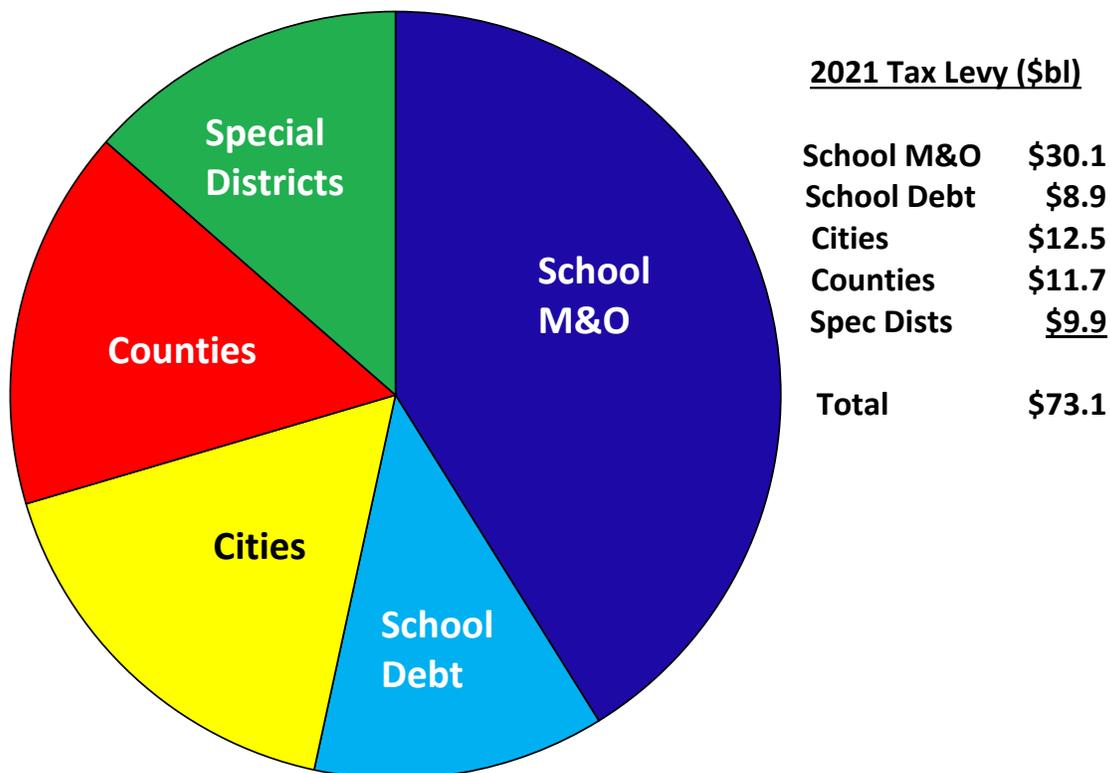
Inventories of raw materials and finished products is a key part of business tangible personal property. Texas is one of the few states that subjects inventories to property taxation. Inventories are exempt in 36 states, partially taxed in four, and fully taxed in 10.

Provisions governing the property tax are found in the Texas Constitution, which provides (Article 8, Section 1(b) and (d)):

*All real property and tangible personal property in this State, unless exempt as required or permitted by this Constitution, whether owned by natural persons or corporations, other than municipal, shall be taxed in proportion to its value, which shall be ascertained as may be provided by law. The Legislature by general law shall exempt from ad valorem taxation household goods not held or used for the production of income and personal effects not held or used for the production of income.*

# Who Levies the Property Tax in Texas, 2021

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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.

# Strategies for Property Tax Relief

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## The Property Tax Equation:

$$\begin{aligned} & \text{Appraised Value} \\ * & \text{Tax Rate} \\ = & \text{Tax Revenue} \end{aligned}$$

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<sup>1</sup>
- 8.0% for Junior Colleges and Hospital Special Districts
- 2.5% for School Districts<sup>2</sup>

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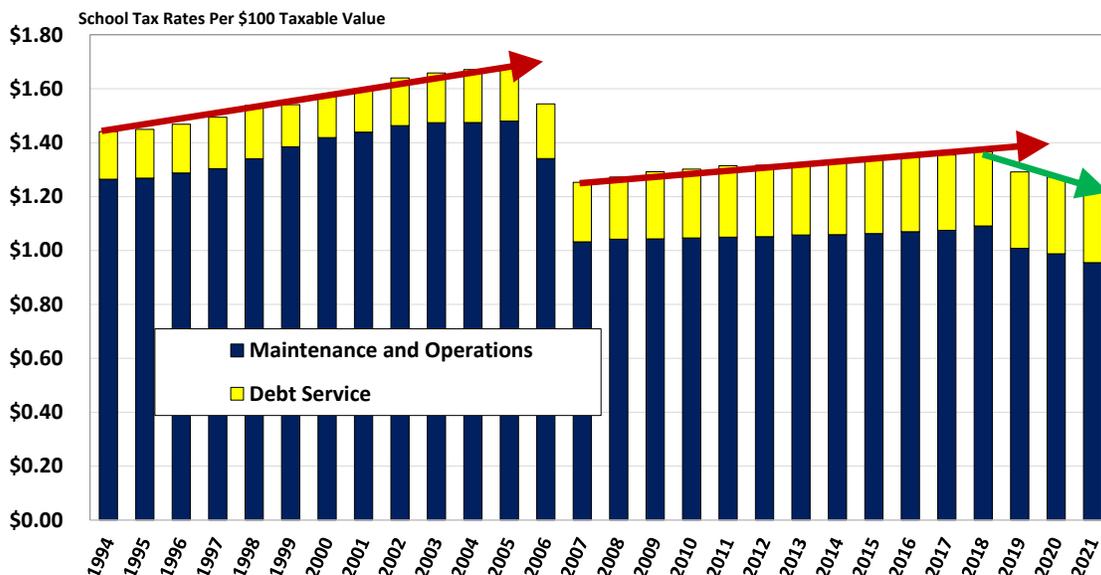
<sup>1</sup> Jurisdictions may generally exceed these percentages without voter approval if the tax rate raises less than \$500,000, which is defined as a “de minimis” amount.

<sup>2</sup> 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

School Tax Rates, 1994 - 2021



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):

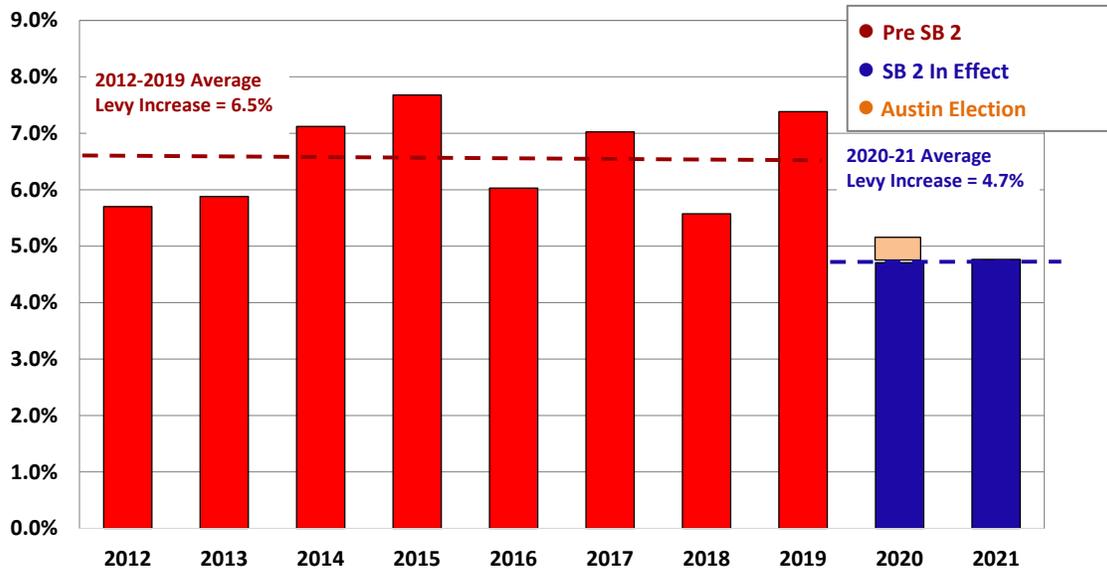
Prior Year Tax Rate per \$100 (excluding enrichment and debt service)		\$0.9300
State Value Growth Threshold (as an index)	1.025	
Current Year Value Growth (as an index)	÷ 1.100	
Equals Compression Percentage		<u>x 0.9318</u>
Current Year Base M&O Tax Rate		= 0.8666

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.

# SB 2 Is Working

## City/County/Special District Levies Are Falling

Percent Increase in the Statewide Property Tax Levy of Cities, Counties, and Special Districts, 2012 - 2021



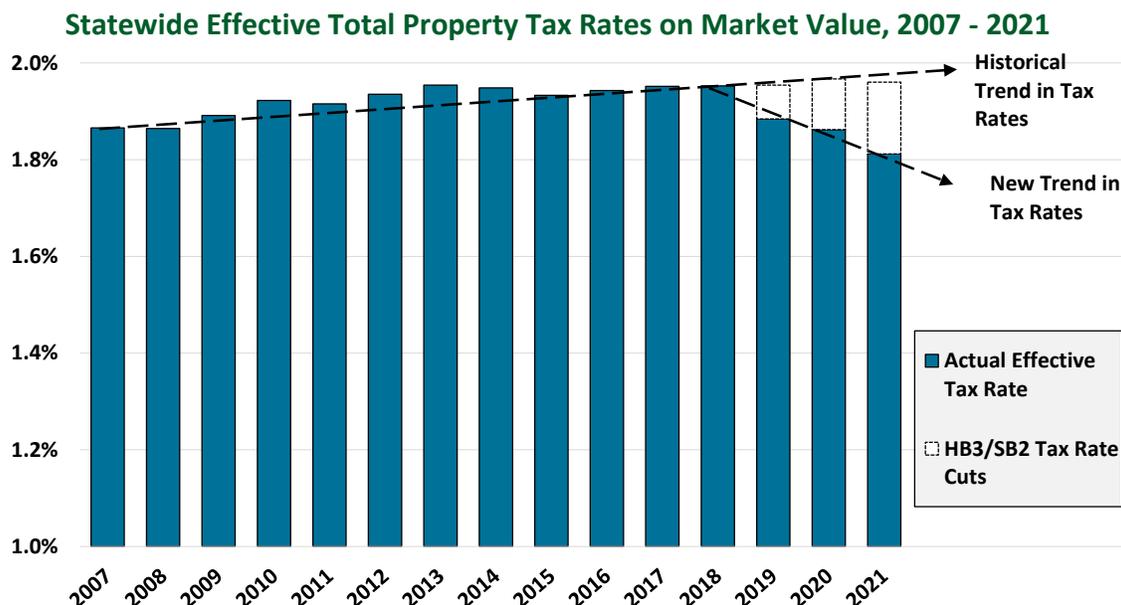
SB 2 limited the ability of cities, counties, and special district to raise their property taxes without voter approval. The bill passed in 2019 but did not take effect until the 2020 tax year.

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 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<sup>3</sup> 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.

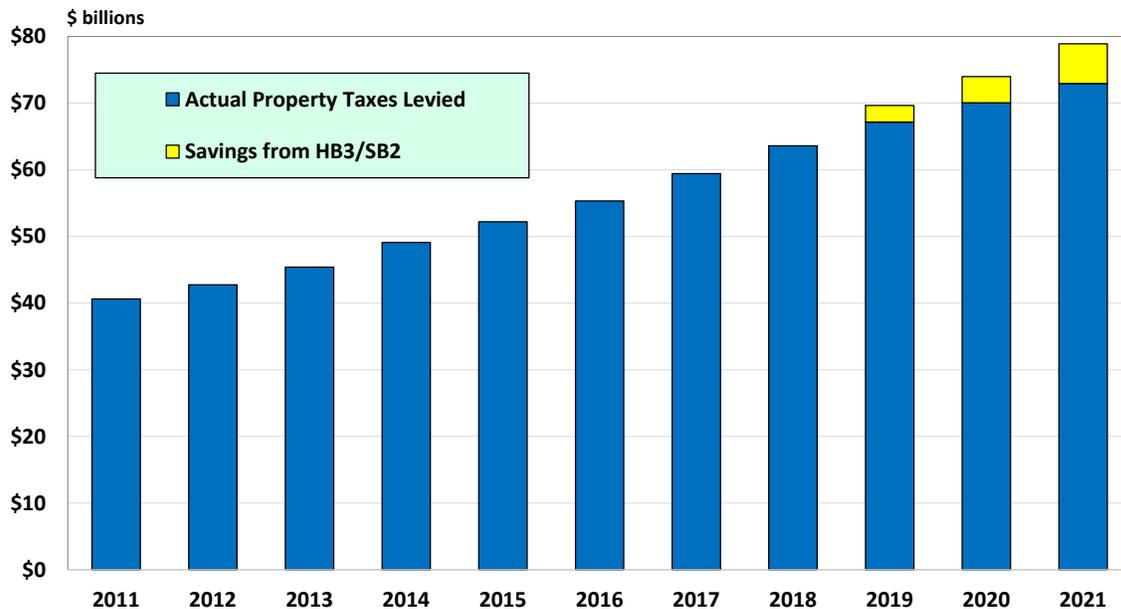
Since 2019, the statewide average effective property tax rate has dropped from 1.95% to 1.81% -- a decline of more than 7 percent in just three years.

<sup>3</sup> 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

## The Growth in Taxes Levied Has Noticeably Slowed

Statewide Total Property Tax Levy, 2011 - 2021



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.

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.

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

# 2022 Appraisal Shock ≠ Tax Bill Shock

## Three Reasons 2022 Tax Bills May Not Be So Bad

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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 on the May ballot, if approved, will 1) raise the homestead exemption, saving the average homeowner roughly \$175, and 2) reduce school taxes on those over 65.***

# 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
<b>Tax Base</b>			
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
<b>M&amp;O Tax Rate Calculation</b>			
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
<b>M&amp;O Taxes Due on:</b>			
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.

# Concluding Thoughts & Recommendations

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- SB 2 from 2019 is proving to be an effective tool in reducing property tax rates and limiting city, county, and special district tax increases.
- HB 3 from 2019 is proving to be an effective tool in reducing school property tax rates and limiting tax increases. If the legislature has additional funds available, using the mechanisms HB 3 has put in place to reduce school tax rates would provide uniform tax relief for all property taxpayers in the state.
- Appraisal caps, and any measures that remove existing property from the tax rolls, do not provide overall tax relief. They do not constrain the ability of local governments to raise additional revenue. Instead, 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. One 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.