TTARA
RESEARCH FOUNDATION

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Property Tax Relief: The $7 Billion Reality

In the spring of 2006, Texas lawmakers passed a massive package of school finance reforms. School tax rates for maintenance and operations were to be rolled back by one-third over the next two years in an initiative that was to provide $7 billion in annual property tax relief. Two years have now passed. The tax cuts are in place; and in fact, perhaps for the first time in history, total property taxes in 2007 fell from the previous year. Yet many Texas property owners have not seen the dramatic reductions in their tax bills they had expected. While the tax cut may not be readily apparent to many, the simple fact is that property tax relief is real, and Texans' property tax bills are indeed $7 billion less today than they would have been (Figure 1).

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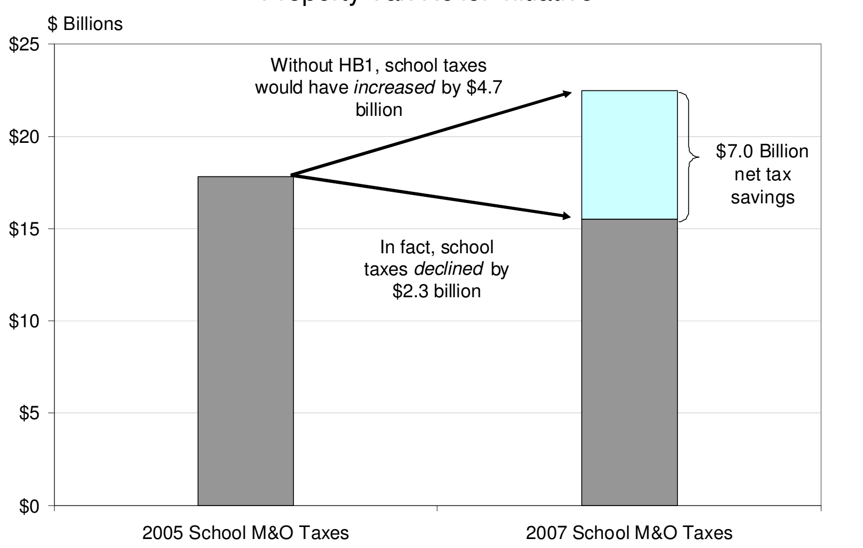
In this analysis the TTARA Research Foundation focuses on the property tax reduction piece of the 2006 reforms to evaluate how the initiative has fared. The various factors that impact Texas property tax bills are examined to determine how tax relief has taken place and why it has not been more noticeable to taxpayers.

Figure 1
What Might Have Been
School Maintenance and Operations Taxes with and without HB1, the Property Tax Relief Initiative



Source: TTARA Research Foundation.

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How the Estimates Were Made

It is difficult to predict the future and even more difficult to predict a future that never was, but in the case of Texas school finance, it is possible to reasonably project the taxesTexans would have faced had the old school finance system remained in place.

Under that system, tax rates for maintenance and operations were capped at $1.50 per $100 of value—a rate that over half of all Texas school districts already levied and would likely have had to continue to levy. For those districts not at the cap, they could have raised their tax rates up to 6 cents per year (without triggering a rollback election, which most districts had been careful to avoid).

For this analysis we increased 2005 school maintenance and operations tax rates by 6 cents each year unless the increase would have resulted in a rate above $1.50—at which point the rate was capped, as it would have been under the old school finance law. These rates were applied to actual taxable value in each school district to arrive at a projection of the property taxes the district would have levied. These taxes were compared to the actual school maintenance and operations taxes the district levied in 2007—the year the one-third rate rollback was fully implemented. The resulting statewide total reduction in school taxes was estimated at just under $7.0 billion.

After several years of failed efforts to reduce school property taxes and devise a school finance system that would satisfy court mandates, the lawmakers enacted a sweeping reform package in the spring of 2006. The plan was originally crafted by a select committee appointed by Governor Rick Perry and chaired by former Texas Comptroller John Sharp. It included a complete restructuring (and increase) of the state's business tax, an increase in the state's cigarette tax, and a commitment of surplus funds in the State Treasury sufficient to provide an overall net tax cut of roughly $2.5 billion a year. The lynchpin of the plan was a promise to reduce school maintenance and operations tax rates by one-third over two years—a near $7 billion promise which captured the public's imagination, though two years later critics have called the cuts only "a figment of the imagination."

Property tax relief has not been as noticeable as taxpayers may have expected.

Property tax relief has not been as noticeable as what taxpayers may have expected. The problem lies with the nature of what is called "the property tax." In fact, Texans do not pay **a property tax;** they pay a **myriad of property taxes** that are typically combined into a single tax bill. The maintenance and operations tax every property owner pays to their local school district was targeted for reduction. But property owners also likely pay a separate tax to their school district to retire voter-approved debt. And they pay a county tax; probably a city tax; and a number of property taxes to a handful of special districts, as well. While the Governor and Legislature were able to deliver rate relief on school maintenance and operations taxes, the average property tax bill contains so many moving parts that school tax relief has been obscured.

In fact, House Bill 1 provided Texas property taxpayers with a savings in 2007 of nearly $7 billion by reducing school maintenance and operations tax rates. Still, Texans are actually paying higher total property taxes today than they did in 2005—the year before the tax cuts began to take effect. A number of factors have combined to make it difficult for taxpayers to see the tax relief the Legislature provided:

Want to See What You Saved?

If you want to see how different your school property tax would have been in 2007 had the property tax relief initiative not passed, visit the webpage at www.tttara.org and follow the “Property Tax Relief Calculator” link.

All you need to know is the name of your school district and the taxable value of your property from your 2007 property tax statement. If you do not have your statement and do not know your property’s taxable value, you can get the exact figure by contacting your local appraisal district. Homeowners may make a rough estimate of the taxable value of their property as the property’s market value less $15,000 (for the state-mandated homestead exemption). Some school districts offer additional homestead exemptions—such as a twenty percent optional exemption, or exemptions for the disabled that should be deducted, as well.

The result will tell you how much lower your property tax bill was last year as a result of the property tax relief initiative.

Using the Calculator:

1. Select your school district from the drop-down menu.
2. Enter the taxable value of your property
3. See what you saved.

To calculate your school district tax savings:

1. Select school district in box 1 from drop-down menu
2. Enter TAXABLE value of your property in box 2 and press "enter"

Not For Duplication

1 Houston ISD

Click on cell and select your school district from dropdown list

2 $190,000

Enter 2007 ISD TAXABLE Value for your property in box above (eg. 200000)

2007 School Tax Savings = $937

Savings reflect the amount of additional school district property taxes that would have been paid if the Legislature had not passed HB 1 which reduced school district M&O tax rates by one-third. Savings do not reflect a 65+ tax freeze.

"No Relief" M&O Rate is an estimated rate arrived at by adding $0.06 to the district's 2005 M&O Rate (capped at $1.50 except for special law districts.) "No Relief" I&S Rate is the district's 2007 I&S Rate.

2007 M&O Rate	$1.01	2007 I&S Rate	$0.15	2007 Total Rate	$1.16
2007 "No Relief" M&O Rate	$1.50	2007 "No Relief" I&S Rate	$0.15	2007 "No Relief" Total Rate	$1.65

$2,198	2007 Actual School District Taxes Paid
$3,135	2007 School District Taxes If Tax Relief Had Not Been Passed

Data Source: ISD Self Reports, Comptroller's Property Tax Division

Texas Taxpayers and Research Association (TTARA)

- Almost all school districts have exercised their local authority to increase tax rates above the state-mandated one-third reduction,
- Local voters have approved additional debt service taxes to improve their school facilities,
- Property values continue to rise, and
- City, county, and special district taxes have continued to increase.

Texans may not have seen the dramatic drop in property taxes they had anticipated, but had the legislature not acted, taxpayers would have seen an estimated $4.7 billion tax increase to fund school maintenance and operations from 2005 to 2007 (assuming the courts would have allowed schools to continue to operate); instead taxpayers actually received a reduction of $2.3 billion—resulting in a total net savings of $7.0 billion. **That means the average Texan's *total* property tax bill in 2007 was 20 percent lower than what it likely would have been had there been no tax relief initiative.**

Property tax relief has been obscured by:

- *local option school tax increases,*
- *growing school debt service taxes,*
- *rising property values, and*
- *city, county and special district tax hikes.*

Local Discretion Spurs Local Tax Hikes

The 2006 reform package mandated that local school districts reduce their maintenance and operations tax rates in effect for 2005 by one-third over the next two years (debt service taxes were not affected). For 2006, M&O rates were to drop by 11.33 percent, with added cuts in 2007 bringing the total two-year reduction to 33.33 percent. With most of the state's school districts levying the maximum allowable $1.50 maintenance and operations tax rate per $100 of value in 2005, it was expected that these rates would drop to $1.00 by 2007, and even below $1.00 in those districts that had a 2005 tax rate under the $1.50 cap. Given that the average tax rate across the state for maintenance and operations was $1.48 in 2005, the rate reduction was to result in an average "compressed" tax rate of $0.987 by 2007 (Figure 2).

However, the tax relief legislation gave school districts the authority to raise taxes for local enrichment purposes above their compressed target tax rate. If districts had not been given some degree of local discretion over their ultimate tax rate, the courts would likely have viewed the result as a state property tax—something prohibited under the Texas Constitution. School districts were allowed to impose additional taxes up to a rate of $1.04 by a simple majority vote of the school board. And if local voters approved, districts could increase rates by an additional $0.13 to a new tax rate of $1.17. By 2007 1,006 of the state's 1,026 school districts had opted to raise taxes above their compressed rate. Of these, 121 were above the $1.04 tax rate and 98 were at the maximum allowable tax rate of $1.17.[1] On average, school districts (and their voters) have exercised their discretion to raise tax rates $0.045 above the compressed rate. That equates to additional taxes of about $675 million, thereby shaving planned tax relief by about ten percent. For property owners in a district that levies the maximum tax rate of $1.17, relief was reduced by one-third..

Do Tax Cuts Make Taxpayers More Generous?

One area of school finance that was not addressed in the effort to reduce property taxes dealt with taxes levied for the improvement and expansion of local facilities. Facilities demands increase as Texas schools add approximately 80,000 new students in average daily attendance each year. The costs of improvements are typically financed by bonds that are paid off by debt service

[1] Under certain extraordinary circumstances, a handful of districts were able to levy a rate higher than $1.17.

taxes that must be approved by local voters. Once the bonds are issued, the debt service tax is set at whatever rate is necessary to make that year's bond debt payments. For the 2005 tax year, of the $20.3 billion in school taxes levied, $2.4 billion, or one-eighth, was for bond payments—about the same proportion as over the past ten years.

Local option school taxes for enrichment have added $675 million in new property taxes since 2005.

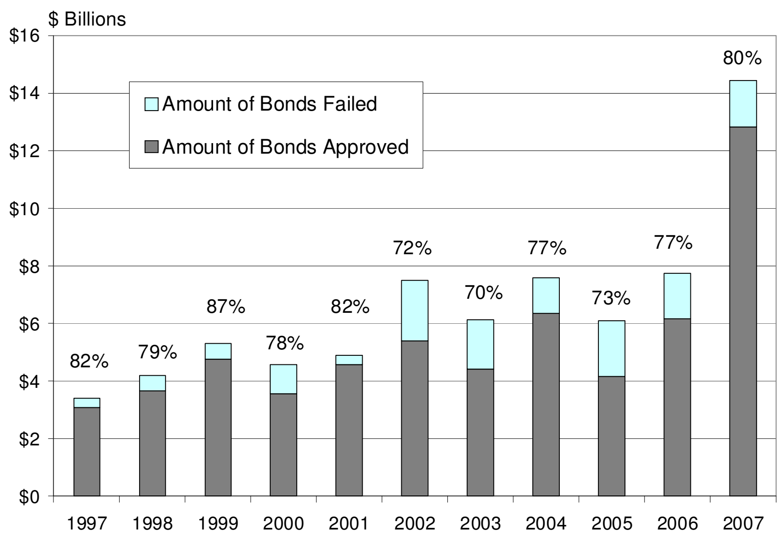
The advent of property relief coincided with additional taxes coming on line for debt service. From 2005 to 2007, taxes needed to repay bonds increased by $900 million to a total of $3.3 billion—a 37% increase.

Over the next several years debt service taxes will increase even more dramatically because local voters approved a record amount of bonds in 2007. These bonds have yet to show up on tax rolls.

Prior to the adoption of the tax relief initiative, bond elections were becoming harder to pass—perhaps in response to increasingly higher maintenance and operations tax rates. From 1997 to 2001, voters on average approved 88 percent of the roughly $4 to $5 billion per year of bonds submitted for their approval (Figure 2). From 2002 to 2006, voters approved only 76 percent of the $6 to $8 billion a year of bonds proposed. With lower maintenance and operations tax rates taking effect with the 2007 tax year, however, school districts submitted a record $14.5 billion of bonds to voters, of which a record $12.8 billion was approved (an 89 percent success rate)—almost three times the average amount of bonds authorized in prior years. The 214 bond elections in 2007 was the most in over ten years and the average bond package was also big—at $67 million it was almost twice the average of previous years. With lower tax rates taking effect, school districts submitted a record amount of bonds to voters who proved to be more willing to authorize them.

School debt service taxes have risen $900 million since 2005.

Figure 2
School Bonds Amounts Passed and
Failed and Election Success Rate, 1997-2007



Source: Derived from data compiled by the Texas Bond Review Board.

Rising Appraisals

There are two parts to calculating one's property tax liability—tax rates and taxable values. In Texas, property is assessed at its market value, though certain exemptions (particularly on one's homestead) reduce this value for tax purposes. In a growing economy such as Texas, property values can be expected to increase every year, and the past two years have been no exception. If a property's taxable value increases proportionately more than the percentage reduction in the overall tax rate, the property tax bill will go up. Many property owners have found that value increases have more than negated the impact of falling tax rates, leading to higher tax bills.

Some concerns have been expressed that appraisal officials took advantage of the falling school tax rates to increase values—though similar pressures would have existed had school tax rates been left at $1.50 (ironically, under the new school finance system, the lion's share of the benefit of rising property values accrues to the state, not to local school districts). The overall increases in the assessed value of property in Texas in 2006 (12.3 percent) and in 2007 (12.1 percent) were the highest in recent memory. The question is whether these increases actually reflected market conditions.

The overall increases in the assessed value of property in Texas in 2006 and 2007 were the highest in recent memory.

The property tax essentially applies to all real property, whether it is owned for residential purposes or for business purposes. In general, business property values (which includes both real and personal property) would be expected to follow the state's economic growth, while residential values would be expected to mirror the state's housing market.

From 1994 to 2005, Texas' business output as measured by gross state product increased at an annual rate of 6.7 percent. The assessed value of business property increased somewhat below that, at 5.1 percent (Figure 3). It is not unreasonable for business values to lag output growth because the modern economy is becoming increasingly based on services, which rely less on physical capital and property than does the traditional manufacturing base. From 2005 to 2007, however, annual economic growth has been a bit stronger in Texas—8.0 percent—thanks to rising oil and gas prices. But instead of registering growth slightly below that, as values historically had, the assessed market value of business property increased at a substantially higher 13.3 percent annually.

Figure 3
Growth in Property Values Relative to the Economic Measures

	Business		Homeowners	
Period	Economic Output	Appraised Value	Average Sales Price per Home	Average Assessed Price
1994-2005	6.7%	5.1%	5.3%	6.2%
2005-2007	8.0%	13.3%	5.2%	7.5%

Source: Economic output is gross state product as reported by the U.S. Bureau of Economic Analysis. Average home sales price is as reported by the Real Estate Research Center at Texas A&M University. Average appraised values are derived from school property tax data filed with the Texas Comptroller's Office.

Residential property values have accelerated over the past two years, as well, though not near as rapidly as business properties. From 1994 to 2005, the typical single family parcel increased in value at a 6.2 percent annual rate—about a percentage point higher than the 5.3 percent annual increase in the average sales price of a home. But from 2005 to 2007, while growth in the average sales price remained about the same, 5.2 percent, the average assessed value of the typical single family parcel increased at a higher annual rate of 7.5 percent.

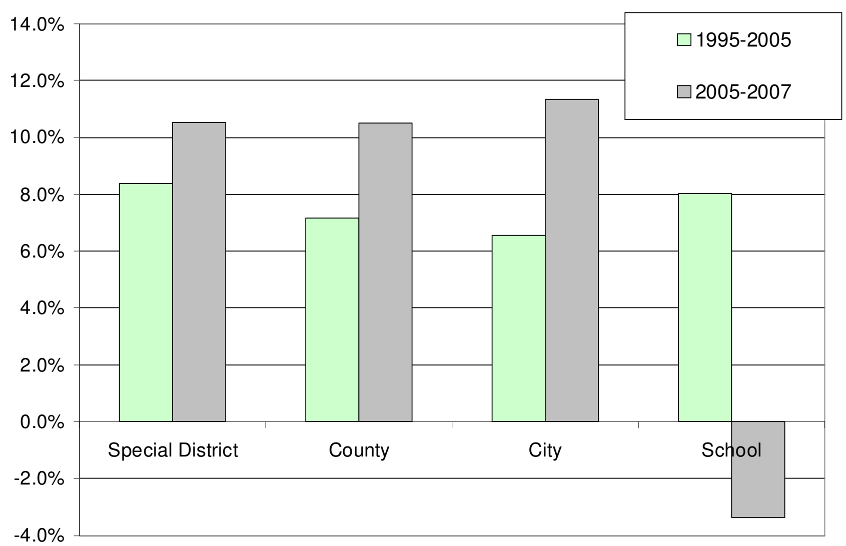
Granted, property appraisal is a complex process that cannot be condensed into a single economic measure or two. However, the fact that business and residential values have increased dramatically since 2005—perhaps by amounts greater than economic conditions might have suggested—is an issue that requires further study. Despite this focus on appraisals, it should be noted that rising values do not automatically translate into higher taxes. Rising values allow the same amount of tax dollars to be collected at lower tax rates. Local officials determine whether total taxes will increase and by how much when they adopt their tax rates.

The commonly referred to "one-third" reduction in tax rates applied to only half of all the property taxes Texans pay.

Other Pieces of the Tax Puzzle

While the state's 1,026 school districts are by far the largest users of the property tax, they are joined by 1,056 cities, 254 counties, and over 1,500 special districts. In 2005, before the tax relief effort took effect, school district maintenance and operations taxes accounted for just over half—53 percent—of all property taxes levied in Texas. Therefore, the commonly referred to "one-third" reduction in tax rates actually applied to only half of all the property taxes Texans pay. Whether total property taxes would rise or fall depended in large measure on what cities, counties, and special districts would do.

Figure 4
Property Tax Growth Before and After the
School Tax Relief Initiative
Average Annual Increase



Source: Based on annual levy data compiled by the Comptroller of Public Accounts.

Figure 5
Property Taxes in 2005 and 2007

Taxing Entity	2005 Levy	2007 Levy	Change
School Maintenance & Operations	$17.8	$15.5	($2.3)
School Debt Service	$2.4	$3.3	$0.9
City	$4.9	$6.1	$1.2
County	$4.8	$5.8	$1.1
Special District	$3.6	$4.5	$0.8
Total	$33.5	$35.2	$1.7

Note: Numbers may not add due to rounding.

Source: Comptroller of Public Accounts. Data for 2007 are preliminary and are subject to revision.

Since 2005 cities, counties, and special districts have raised their property taxes by roughly 11 to 12 percent each year—well above the 3.6 percent increase in the municipal cost index and the 2.2 percent growth in population.

It appears the answer is that they chose to accelerate their tax increases (Figure 4). During the previous 10 years, city, county, and special district taxes had risen with school taxes—with average annual increases of roughly 7 to 8 percent. Increases of that magnitude alone would have obscured school tax relief had they continued; but in fact, since 2005 average annual tax growth in these jurisdictions has accelerated to roughly 11 to 12 percent—well above the 3.6 percent inflation increase in the municipal cost index (American City and County Magazine) and the 2.2 percent average annual Texas population growth.

Conclusion

Basic tax rates for school maintenance and operations have been rolled back as lawmakers promised. However, they are but one of many moving parts that comprise the machinery of Texas' property tax system. Since the tax relief initiative took effect, additional school taxes have gone on the books, either authorized by local school boards or local voters; appraisals of property—both that of homeowners and of businesses alike—have risen at unusually high rates; and, cities, counties and special districts have approved substantial tax hikes. All of these factors combined to produce a total property tax bill for Texans $1.7 billion higher than came due in 2005, just before the school property tax relief initiative was undertaken.

Even so, there is no doubt the actions taken in 2006 have saved Texans an estimated $7 billion a year in property taxes. The average Texans' property tax bill may not be lower today than it was two years ago, but it is unmistakably much, much lower than it would have been.