TEXAS PUBLIC POLICY FOUNDATION

Testimony

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Center for Fiscal Policy

Eliminating Texas' Rising Property Tax Burden

Testimony before the House Ways & Means Committee on HB 285

by Vance Ginn, Ph.D.

Chairman Bonnen and Members of the Committee:

My name is Dr. Vance Ginn, and I am an economist in the Center for Fiscal Policy at the Texas Public Policy Foundation, a 501(c)(3) non-profit, non-partisan free market think tank based here in Austin. Thank you for the opportunity to speak today on HB 285, which would swap property taxes for school district M&O with an increase in the state sales tax rate. We appreciate the work on this bill and other similar proposals heard today. The Foundation finds the best way to reduce the burden of local property taxes is to eliminate all of them and replace them with a more conservative, efficient, and simple reformed sales tax with an adjusted base and rate. This pro-growth reform would help Texans finally own a home and achieve greater prosperity. Given recent trends, this cannot happen soon enough.

From 2000 to 2015, property taxes levied statewide soared by 132 percent, outpacing combined population growth and inflation that grew just 82 percent. Excessive property tax levy increases have been fueled by oftentimes subjective appraisals and more than 4,100 local governments that collect more than $52 billion from homeowners and businesses statewide, or roughly $8,000 per family of four.

While school districts account for 54 percent of this burden, more state tax dollars into public education will not solve the problem. State spending on public education has continued to increase since 2004-05 and now comprises roughly 40 percent of general revenue (GR) expenditures. Moreover, spending more state tax dollars could exacerbate the problem by giving school districts room to raise property taxes even higher. School district property taxes are not the only part nor the fastest growing portion of property taxes levied.

From 2005 to 2015, total property taxes levied statewide increased by 4.9 percent on an average annual basis. Separating levies into major categories, average annual growth increases were 7 percent by special purpose districts, 6.3 percent by counties, 5.6 percent by cities, and 4 percent by school districts. There is room for reform across the board, but just increasing public education spending or replacing school district M&O property taxes with a higher sales tax rate, as in HB 285, leaving the potential for other local jurisdictions to raise tax levies more, would not sufficiently mitigate the rising property tax burden.

Higher property tax bills negatively affect all Texans by limiting investment decisions especially in the case of home ownership, discouraging economic activity, and affecting employment creation. But property taxes tend to put the most burden on low- and middle-income individuals by forcing many of them out of their homes as their tax bill increases faster than their income. Property taxes do not just affect homeowners, they are also a detriment to renters as landlords pass higher tax bills to their tenants.

Given these costs, the Foundation is encouraged by HB 285 and the other bills heard today that consider eliminating certain property taxes. Although most Texans think in terms of local and state funding for schools separately, such is only true for facilities funding. Local school district property taxes collected for M&O purposes actually perform like a state property tax. Moreover, Texas' local property tax burden ranks 14th highest nationally and weighs heavily on homeowners and businesses statewide; but research suggests that relief may be only a few modest reforms away.

To more efficiently collect taxes to fund the school finance system and all local governments while reducing the burden on property owners, we recommend eliminating all property taxes and funding taxing entities with a reformed sales tax. The Foundation's 2015 study *The Freedom to Own Property: Reforming Texas' Local Property Tax* notes that

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of all the major taxes, a consumption tax (or sales tax) is the most preferable for at least three reasons: simplicity, transparency, and levied only on the end-user, which provides some discretion over one's tax liability.

The Foundation's 2012 study *Enhancing Texas' Economic Growth through Tax Reform* co-authored by economist Dr. Arthur Laffer shows that by reasonably adjusting the state's sales tax base and rate, which includes the 6.25 percent state and max 2 percent local portions, the following scenarios could provide a revenue neutral swap:

- 19.5 percent, if the current sales tax base is used excluding real estate;
- 15.7 percent, if the current sales tax base is used including real estate;
- 11.0 percent, if all services that are taxed in at least one state are taxed in Texas including real estate; and
- 5.5 percent, if the GDP tax base is used.

While sales tax revenue tends to fall more during a recession, it also tends to rise faster during an expansion with slower tax revenue growth over time than with subjective property taxes. Of course, effectively limiting government spending best restrains government, but providing a potentially more conservative funding source could also help. For example, the Foundation's 2015 study notes increases from 2000 to 2013 of 101.1 percent in property taxes and 86.2 percent in state sales taxes compared with a 70.3 percent increase in compounded population growth plus inflation. Swapping all property taxes with one of the sales tax reforms above along with limiting government spending would provide meaningful tax relief, and strengthen the state's economy by encouraging economic growth and job creation.

If this property tax-sales tax swap happened, the Foundation's 2012 study estimates that personal income in Texas might increase on a cumulative basis over five years as much as $63 billion thereby encouraging more job creation of as much as 337,400 new jobs above baseline growth. Another benefit of this reform has nothing to do with tax relief, creating wealth, or adding new jobs; it has to do with liberty. So long as Texas' property tax remains in place, no Texan who purchases a home, operates a business, or has property of any kind, will ever truly own these. Today, Texans effectively rent from the government, indefinitely. Instead of paying the government in perpetuity, the ability to lump the sales tax amount into your mortgage if so desired would allow you to own your home after it is paid off.

Given these benefits, the Foundation recommends the following:

- Swap property taxes with a reformed sales tax that includes the broadest base and lowest rate.
- Reform the school finance system to a student-centered funding approach with education choice, and impose a local spending limit on taxing entities based on population growth plus inflation. Tax burdens will always be excessive until government spending is effectively restrained.
- Until abolishing property taxes, local voters should get a louder voice in the property tax-setting process by requiring local voter approval when property tax revenue increases by more than 4 percent or population growth plus inflation, whichever is less.

Thank you for your time, and I look forward to answering your questions. ✯

Vance Ginn, Ph.D., is an economist in the Center for Fiscal Policy at the Texas Public Policy Foundation. He is an expert on Texas' state budget, franchise tax, tax and expenditure limit, and other fiscal issues. Before joining the Foundation in September 2013, Ginn was a Koch Fellow, and taught at three universities and one community college in Texas. He has published peer-reviewed articles in academic journals, as well as commentaries in major media outlets across Texas and the nation.