TTARA
Texas Taxpayers and Research Association
Working for fiscal responsibility in state government

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Property Tax: Focus on Appraisals May be Misplaced

Over the past few months, a number of Texas newspapers have written in a critical tone about Texas' property tax appraisal system—particularly as it relates to commercial real estate. The articles point to anecdotal evidence of undervalued properties as being indicative of a widespread problem. In response, there is discussion about a wide range of "fixes," including lowering the cap on annual increases in residential homestead.

The failure to correctly assess a piece of property has serious consequences for the integrity of the property tax system. If a property is under-appraised, that error is offset by other taxpayers paying more than they should. On the other hand, if a property is over-appraised, the owner of that property pays more than they should. Taxing jurisdictions are NOT losing or gaining scads of revenue as a result. Taxing jurisdictions set their tax rates at the level required to produce the budgeted amount of revenue when levied on final certified values. Those values simply reflect who is going to pay how much of that predetermined total.

The valuation of commercial properties has come under particular scrutiny as a result of taxpayers receiving reductions by challenging their values based on the use of comparable properties. The Texas Constitution mandates that all property be taxed at market value and that taxes be "uniform and equal." Under Texas law, if a taxpayer can demonstrate that their value is higher than that of comparable properties, they may get relief. This puts comparable properties on a level playing field. Appraisal districts accuse taxpayers of "cherry picking" undervalued properties for comparison, although the values on those properties were either set by the appraisal district or its own appraisal review board.

In response to the hubbub over commercial values, the Harris County Commissioner's Court recently hired a consultant to review the county's commercial values but no major discrepancies were found:

> *The independent appraisal ratio study, which was authorized by Commissioners' Court several months ago, reviewed the appraisal district's preliminary values on several commercial categories including office buildings, retail properties, apartments and vacant land. The preliminary results indicate that the initial 2014 HCAD values of all of those categories, with the exception of vacant land, are close enough to their January 1 market value to be within the study's statistical margin of error. (Harris County Commissioner's Court Press Release, June 2014)*

The Comptroller's value study does suggest vacant lots in Houston ISD are undervalued, but by just less than five percent (which is within allowable tolerances). If so, the impact on other taxpayers adds one tenth of one percent to their tax bill. But before taxpayers bank that savings, it should be noted that the Comptroller says Houston utility property is *overvalued* by more than seven percent (an issue Harris County Commissioners are not investigating). Correcting that error would cost all other taxpayers far more than any savings realized by upping vacant lot values.

Travis County Commissioners also considered challenging the commercial property tax roll, but decided against it. They noted their information on value discrepancies was only anecdotal and the estimates of the resulting reduction for other taxpayers ranged from $5 to $10 a year.

So in fact, all available information does not offer widespread evidence of undervaluation of commercial property. That is not to say there is no need for procedural change. However, proponents of such need to be honest and state those changes won't yield a noticeable impact on overall tax bills.

There is growing public dissatisfaction with the property tax as the Texas economy shifts into overdrive and homeowners and businesses are hit with rising appraisals. Homeowners, in particular, are suffering the tax consequences (but also reaping the rewards) of a hot real estate market.

Over the past 20 years, residential property has become a bigger part of the property tax. Residential property (of which perhaps 80 percent is homestead property) accounted for 39.5 percent of school taxes in 1994. By 2013 that number had risen to 47.7 percent. This shift is not because of any significant changes in tax law or practice. It's because of significant changes in our economy.

On the business side, we have become more of a services-based economy. Property-intensive industries are relatively declining in our economy as labor-intensive industries are growing. Over the past 20 years, Texas has lost 94,000 manufacturing jobs and gained 3 million services jobs. Those services jobs require much less property to support a productive worker than those at an industrial plant. As the jobs in our economy become less property intensive, the taxes employers pay lags overall economic growth, putting more pressure on homeowners and industrial

properties. Further, a big part of the business tax base is personal property—which, unlike real estate, depreciates over its useful life.

There are shifts on the residential end, as well. In the past 20 years Texas has not only seen a 45% increase in the number of single-family homes, those homes are more expensive, even adjusting for inflation. People today are more urban than they were 20 years ago, and homes in the cities cost more than comparable homes in rural areas. Homes built today are generally bigger than they were 20 years ago, too, and that extra square footage translates into higher cost and higher taxable value.

Appraisal caps, while popular politically, are not the solution. They may seem sweet, but they have no nutritional value. They do nothing to stem the tide of rising property taxes, they only impact who must pay them. As noted earlier, taxing jurisdictions adopt tax rates based on the amount of money they need to fund their budget. One taxpayer's break is another taxpayer's burden.

Ironically, appraisal caps over time create a tax spiral back to homeowners. They raise the Texas tax burden on industrial properties, already among the highest in the nation, placing them at a competitive disadvantage and accelerating their move to other states and overseas. In turn, this furthers the shift of the tax base onto residential property.

The real reason property taxes are rising is not because of increasing appraisals. It's because of increasing budgets.

Values are only one part of the tax equation; rates are the other. The product of values multiplied by tax rates equals total property tax revenue. Taxing jurisdictions who blame rising tax bills on someone else's appraisal are playing "hide the ball." Property taxes are rising because schools, cities, counties, and special districts are spending more. People should certainly pay attention to their values, and contest them if they appear too high, but that will not put a dent in property taxes as long as spending continues to rise. Attention is better focused on the local budget process. Until people connect the costs of the services they want to the taxes they pay, there cannot be a rational discussion of fiscal policy.

A recent Austin American Statesman article included a telling quote from a homeowner concerned about their rising home appraisal: "I have voted for every park, every library, all the school improvements, for light rail, for anything that will make this city better. But now I can't afford to live here anymore."

Perhaps the problem is not the appraisal.

Surplus Ahead: State Revenues Continue to Roll

State revenue collections through May continue to exceed expectations. Now nine months into the 2014 fiscal year it is obvious Texas is headed towards a sizeable budget surplus by the end of this biennial budget. With the economy in good health and no foreseeable slowdown, state lawmakers next year will be welcomed with a multibillion dollar surplus.

Sales tax continues to roll and the past few months have actually seen growth accelerate well above the officially projected rate. The Comptroller expects growth in 2015 to slow, but no such trend currently appears on the horizon. The May data also gives us our first peek at franchise tax revenues, which were due May 15 (most taxpayers made a preliminary filing). Because of rate cuts and new provisions favorable to taxpayers, the state projected franchise tax revenues would be down 2.6 percent this year, though so far the tax is only down 1.2 percent.

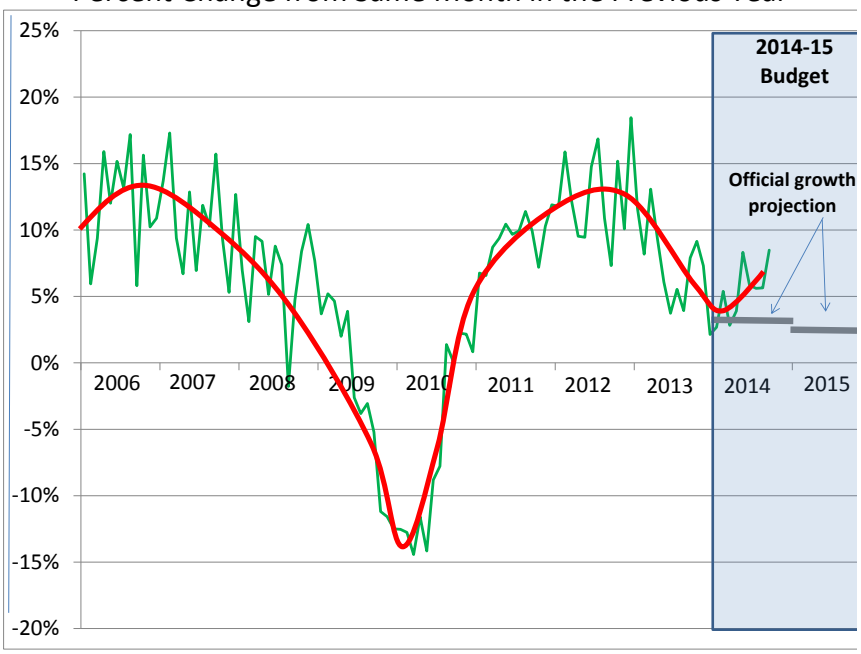
Tracking Key State Revenues through May 2014

Tax Source	Percent of All "Certification" Revenues	Actual Year- to-Date Growth	State's Official Projection for 2014
Sales Tax	51.6 %	5.4 %	3.5 %
Auto Sales Tax	7.8 %	7.3 %	5.3 %
Oil Severance Tax	6.3 %	31.3 %	9.1 %
Natural Gas Tax	3.0 %	20.8%	4.3 %
Franchise Tax	9.0 %	(1.2 %)	(2.6 %)
Total*	77.7 %	4.9 %	0.8 %

Notes: * A portion of the excess is dedicated to the "Rainy Day Fund."

Sales Tax Growth:

Percent Change from Same Month in the Previous Year



Note: The green line reflects actual monthly data. The red line smoothes monthly fluctuations.

Revisiting State Tax Appeals

TTARA's state tax appeals working group, chaired by Eleanor Kim, will next meet **September 16 at 10:00 am** in the 3rd floor conference room of our building. We will continue to discuss the development of a preferred position regarding policy options for improving the appeals process. Since the Sunset Commission began its review of the State Office of Administrative Hearings (SOAH) last week, hopefully we also will be able to discuss the progress of their examination of the agency. So, we hope everyone interested in this effort will enjoy the lazy, hazy, crazy days of summer but then put your thinking caps on and join in the lively deliberations on September 16. We look forward to seeing you then.

Mark Your Calendars: TTARA's 2014 Annual Meeting October 22nd and 23rd

TTARA's 2014 annual meeting will take place at the Sheraton Austin Hotel at the Capitol, on Wednesday October 22nd and Thursday October 23rd. Detailed program and registration information will be forthcoming later this summer. If you are interested in sponsoring this year, please check out the various levels of sponsorships available here or contact Ryan Ash at 512-472-8838 / ryan@ttara.org .

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