TEXAS PUBLIC POLICY FOUNDATION

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LEGISLATOR'S
GUIDE
to the issues

TEXAS PUBLIC POLICY
FOUNDATION

The Texas Public Policy Foundation is a 501(c)3 non-profit, non-partisan research institute.

The Foundation's mission is to promote and defend liberty, personal responsibility, and free enterprise in Texas and the nation by educating and affecting policymakers and the Texas public policy debate with academically sound research and outreach.

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The public is demanding a different direction for their government, and the Texas Public Policy Foundation is providing the ideas that enable policymakers to chart that new course.

Eliminating the School M&O Property Tax

The Issue

Texas has some of the highest property taxes in the nation. In 2014, the Tax Foundation reported that Texas had the sixth highest effective property tax rate. In 2016, more than 5,100 local tax jurisdictions levied $56.1 billion in property taxes, or $2,000 on average for every Texan—man, woman, and child. And property taxes continue to increase. The overall property tax levy increased by 233% between 1996 and 2006, while personal income only increased by 199%. Texans risk losing their house—and sometimes do—because of an out-of-control growth of local governments. An excessive growth of government also discourages investment, job creation, and economic growth in general.

Out of the total property tax levy (from all local governments), school districts' maintenance and operations (M&O) property tax revenues represented almost half of the burden to taxpayers in 2016. The M&O tax levy amounted to nearly $25 billion in 2018. Although the state has explored options to reduce the overall property tax burden, one obstacle has remained: The Texas Constitution prohibits the state from levying a property tax.

Nonetheless, multiple legislatures explored different options. One of them was raising the homestead exemption for school district property by $10,000, first in 1997 and again in 2015. These exemptions may have benefited those with a homestead but not those without. The overall property tax burden also continued to increase.

In 2006, the Legislature tried to reduce property taxes and increase state funding for education by increasing the Texas franchise tax, the motor vehicle sales tax, and taxes on tobacco products. The goal was to use the additional revenue, combined with changes in the school funding formulas and property tax caps to both bring the school finance system into compliance with the Texas Constitution (the Texas Supreme Court had ruled the system unconstitutional in 2005) and provide relief to property taxpayers. This solution failed to bring effective, broad-based, and long-term relief to Texans.

A different approach could bring relief to property taxpayers and limit government growth. This approach encourages state and local governments to exercise fiscal restraint through tax and expenditure limits to progressively eliminate the M&O tax while reducing the growth of government. The state surplus created could be used to replace the M&O tax.

Using the past rate of growth (10.08%) of general revenue-related (GRR) state revenue, Texans could eliminate district-level education M&O taxes and cut property taxes almost in half in as little as 11 years. This can be accomplished by restraining state spending growth to 4% biennially and using 90% of the surplus state revenue this produces to ratchet down local property tax rates. Under this plan, every dollar not spent by the state or school districts would produce a 90-cent property tax cut for Texans.

Within the 4% limit on GRR appropriations growth, the Legislature could appropriate money for any purposes legally available, including education funding. If circumstances required for the plan to be adjusted—e.g., due to lower-than-expected economic growth, or a natural disaster that would require additional

spending—the Legislature could exceed the appropriations limits and/or reduce the property tax replacement surplus by a majority vote of both houses. If the property tax replacement payment was reduced during certain years, the replacement plan would be extended but would continue until full elimination of the M&O property tax.

At the local level, each year school districts would set their M&O tax rate to reduce property tax revenue by the same amount they received from the state's replacement funding. On average, property taxpayers in districts across the state would see the same percent reduction in their taxes, though that might vary from one district to another. At the end, every taxpayer's M&O property tax burden would be equal to zero.

If school districts wanted to exceed the replacement rate, they could do it with the approval of a majority of voters in an election with at least a 20% turnout. However, additional funds raised through a voter-approved tax increase would be fully recaptured by the state. So all increases in education funding each year under the plan would come from the state.

The Facts

- Texas has one of the highest property tax burdens in the nation. The Tax Foundation ranked the state's effective property tax rate sixth highest in 2014.

- Texas school districts' M&O property tax accounts for almost half of the overall property tax burden, representing nearly $25 billion in 2018.

- Only local governments in Texas can levy a property tax. The Texas Constitution prohibits the state from levying the tax.

- Past attempts by the Legislature to provide relief to property taxpayers by increasing the homestead exemption or by increasing other taxes have failed.

- The overall property tax levy increased by 233% between 1996 and 2006. Personal income increased by only 199%.

Recommendations

- Restrain state spending growth by imposing a limit of 4% on GRR appropriations growth.

- Restrain local government spending growth by imposing a limit of 2.5% of property tax revenue growth.

- Use the surplus generated by the new state spending restraint to progressively replace and eliminate the M&O property tax, while school districts progressively decrease their M&O property tax rate by the replacement rate.

Resources

Abolishing the "Robin Hood" School Property Tax by Kara Belew, Emily Sass, and Bill Peacock, Texas Public Policy Foundation (June 2018).

Experts

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