HOUSE RESEARCH ORGANIZATION bill analysis | 5/7/2007 | HB 438 Hochberg, Crabb (CSHB 438 by Elkins)

SUBJECT: Enabling annual 10 percent cap on increases in homestead taxable value

COMMITTEE: Local Government Ways and Means — committee substitute recommended

VOTE: 7 ayes — Hill, Creighton, Elkins, C. Howard, Puente, Quintanilla, Villarreal

0 nays

WITNESSES: For — (*Registered, but did not testify:* Daniel Gonzalez, Texas Association of Realtors; Paula Johnson, Texas Silver-Haired Legislature #13; John Kroll, Town of Little Elm)

Against — Bennett Sandlin, Texas Municipal League (*Registered, but did not testify:* Craig Pardue, Dallas County; Chris Scotti, College Station; Becky Miller)

BACKGROUND: Tax Code, sec. 23.23, authorized by Texas Constitution, Art. 8, sec 1-i, mandates that the appraised value of a residence homestead be no higher than either the lesser of the market value or the sum of:

- 10 percent of its appraised value for the last year in which it was appraised multiplied by the number of years since the last appraisal;
- the appraised value of the property as of its last appraisal; and
- the market value of any new improvements.

Any improvement to a residence homestead made after the previous year's appraisal that increases its market value is considered a new improvement. Ordinary maintenance of an existing structure or landscape would not be considered a new improvement.

Tax Code, sec. 25.18 requires each appraisal office to create a plan for conducting periodic appraisals of property in the district at least once every three years.

DIGEST: CSHB 438 would amend Tax Code, sec. 23.23 to allow an appraisal office to increase the appraised value of a residence homestead for one tax year to an amount that would not exceed either the lesser of the property's market value in the most recent tax year in which it was assessed or the sum of:

- 10 percent of the appraised value in the preceding tax year;
- the appraised value the preceding tax year; and
- the market value of all new improvements.

These provisions would apply despite any requirements under Tax Code, sec. 25.18 and regardless of whether the appraisal office had appraised the property and determined its market value of that tax year.

The bill also would specify that any improvement to a residence homestead made after the most recent appraisal that increased its market value and whose value was not included in the appraised value of the property for the previous tax year would be considered a new improvement. Repairs would be added as a category ineligible for inclusion as an improvement.

The bill would take effect January 1, 2008, but only if the Legislature adopted and voters approved during the November 6, 2007, election HJR 40 by Hochberg. If that proposition was not approved by voters, the bill would have no effect. The bill would apply only to residence homestead appraisals that began on or after January 1, 2008.

SUPPORTERS SAY:

CSHB 438 would align the statutory language in the Tax Code with the intent of the Legislature when it approved the 10 percent cap on increases in homestead appraisal valuations in 1997. The bill would prevent sticker shock by ensuring that no taxable value could increase by more than 10 percent, preventing the current scenario under which some homeowners who are appraised every three years can see a 30 percent increase in their tax bill. It also would ensure each taxpayer was treated equally and would create a more comprehensible property tax system.

Texas voters and the Legislature endorsed the idea of appraisal caps in 1997, setting a 10 percent limit on the increase in average annual homestead appraisal values. It was designed to provide an element of relief to taxpayers whose property taxes were skyrocketing. It also reduced the backdoor method of increasing tax revenue without having to increase tax rates by limiting how much a district could increase a homestead's taxable value. The measure was supposed to be a circuit breaker for taxpayers, who would be able to budget and plan without being hit with enormous tax increases they would be required to pay in one year's time.

CSHB 438 would provide the full relief intended by the initial measure by tying the 10 percent cap to the residence homestead's last appraisal. If anything, it would make the concept behind the current appraisal cap even easier for a taxpayer to understand. Many people believe they can be assessed taxes on only a 10 percent increase in taxable value in any given year. They do not know that the 10 percent limit is based on the number of years since a property's last appraisal and could in fact be as high as a 30 percent hike for a property whose value was increasing and that was being reappraised every three years. This bill would not change the effect of allowing the taxable value to catch up to the market value, so a residence homestead whose taxable value increased 15 percent in one year and 5 percent the following year still would see successive years of 10 percent increases in taxable value.

Most districts have moved to either one- or two-year appraisal cycles, so it is unlikely this bill would have any great effect on reducing revenue. Larger districts have been conducting annual reappraisals to comply with Government Code, sec. 403.302, which requires that a school district's reported value fall within a 5 percent margin of error above or below the district's taxable value as estimated by the comptroller.

While some districts might opt to reappraise property more frequently, the associated expenses of doing so would be disbursed among all the taxing units in a county, and no one entity would bear a significant financial burden. If more counties did annual appraisals, it would have the further benefit of creating a more accurate appraisal value that, while still lagging a year behind the market, would not reflect values from two to four years ago. Although an annual appraisal could lead to quicker reductions in taxable value during a housing slump, less frequent appraisals would create a similar problem when the market recovers and appraised values do not capture tax revenue derived from this growth for several years.

OPPONENTS SAY:

Given current requirements governing a school district's appraised value, this bill is unnecessary because most large districts in which appraisal values increase at a rate in excess of 10 percent already appraise properties annually. CSHB 438 could compel smaller appraisal districts to reappraise property more often, which could expedite reductions in taxable value in a market downturn, potentially leading to an increase in tax rates.

Large districts that have typically seen the greatest increases in property values already conduct annual reappraisals. Potential penalties of falling outside the 5 percent margin of error in the comptroller's property value study, such as a reduction of state funding for school districts, provide incentive to areas in which property values are rapidly changing. These districts typically see the type of property value growth and increases in taxable value that benefit the most from appraisal caps.

Smaller districts that decided annually to reappraise property could face financial burdens, which could result in a tax increase on property. In a housing slump, frequent appraisals would create a reduction in value more quickly, resulting in a reduction of the tax base that could necessitate an increase in tax rates for a district unable proportionately to reduce its budget. An appraisal district would have to hire more staff, and associated costs would be borne by school districts, cities, counties, and other taxing units.

To the extent that this bill would reduce the burden for some taxpayers, it could shift the burden to other taxpayers, such as commercial property owners and those whose residence homesteads were not increasing in value at a rate at which they could take advantage of an appraisal cap.

OTHER OPPONENTS SAY:

CSHB 438 would not go far enough in protecting taxpayers from large increases in their tax bills and should reduce the appraisal cap below the current 10 percent. An annual 10 percent increase in taxes is still a significant burden to taxpayers and provides a disincentive to home ownership.

NOTES:

The Legislative Budget Board, using the statewide average number of years between reappraisals (1.4 years) and projected growth and tax rates, estimates the incremental value loss under this bill would result in an almost $15 million negative impact to general revenue-related funds in fiscal years 2008 and 2009.

The original version of CSHB 438 included reference to the year of the most recent tax appraisal, rather than the preceding tax year as specified in the committee substitute.

HJR 40 by Hochberg, which would amend Texas Constitution, Art. 8, sec. 1-i to authorize the Legislature to limit the increase in appraised taxable value of a residence homestead to 10 percent since the property's most recent appraisal, is on today's Constitutional Amendments Calendar.

The companion bill, SB 391 by Hegar, is pending in the Senate Finance Committee. SJR 17 by Hegar, which is identical to CSHJR 40, was reported favorably, as substituted, by the Senate Finance Committee on May 4.