Senate Finance Committee
Interim Report on Texas Taxes

December 2002

P.O. Box 12068 • Austin, Texas • 78711 • 512/463-0370

Texas Senate Committee on Finance

Interim Report on Texas Taxes

December 2002

January 13, 2002

Lt. Governor Bill Ratliff

P.O. Box 12068

Austin, Texas 78711

Dear Governor Ratliff,

The Senate Finance Committee respectfully submits this report regarding our charge to survey and assess the current tax system in Texas. Also included, in response to our charge, is a listing of taxation authority given to units of local government and estimates of the economic value associated with all current taxes, exemptions, and abatements**.** We thank you for providing us this opportunity to address these important issues.

This report is submitted with consideration of the uncertainty the 78th Legislature will face in developing the 2004-2005 state budget. The Committee expects this report will provide a useful informational resource to its readers. Many of the issues discussed in this report include information that may have fiscal implications if adopted by the Legislature. Therefore, in an effort to provide the Senate flexibility in addressing this issue, a series of options with a variety of costs have been identified in leu of making recommendations. It is important to note that the members of the Committee have signed this report in an effort to forward the process of the Committee. In no way should a signature of a member be construed as an endorsement of any individual option or concept contained within this report.

I thank you for the opportunity to respond to this very important charge. The process from information and data gathering to final product has been challenging, informative, and rewarding for everyone involved.

Sincerely,

Rodney Ellis

Rodney Ellis

December 19, 2002

The Honorable Bill Ratliff
Lt. Governor of Texas
Capitol Room 2E.13
Austin, TX 78711

Dear Governor Ratliff:

The Senate Finance Committee submits its interim report for the consideration by the Seventy-Eighth Legislature.

The options outlined in this report are based on extensive testimony and suggestions from state agencies, organizations and other interested persons.

Respectfully submitted,

Senator Rodney Ellis Chair	Senator Chris Harris Vice Chair

Senator Gonzalo Barrientos	Senator Robert Duncan	Senator Troy Fraser
Senator Mike Jackson	Senator Jon Lindsay	Senator Eddie Lucio, Jr.
Senator Steve Ogden	Senator Todd Staples	Senator Carlos F. Truan

Senator John Whitmire Senator Judith Zaffirini

Acknowledgments

The Senate Finance Committee appreciates the opportunity provided by Lieutenant Governor William Ratliff to review state and local taxation issues that affect the lives of all Texans. We also appreciate greatly the leadership and sentiments of all who devoted their time and expertise to preparing this report.

We are grateful for the support and guidance of the Office of the Comptroller, the Legislative Budget Board and of the Senate Research. We particularly thank the following individuals for their support and guidance:
1. James Lebas, Revenue Estimating Division of the Comptroller of Public Accounts
2. John Heleman, Revenue Estimating Division of the Comptroller of Public Accounts
3. The Revenue Estimating Division of the Comptroller of Public Accounts
4. Don Warren, Texas Legislative Council
5. Koren Sherrill, Texas Legislative Council
6. Bill Allaway, George Christian, and Dale Craymer at the Texas Taxpayers and Research Association
7. Dick Lavine, Center of Public Policy Priorities
8. Michael Mazerov, Center on Budget and Policy Priorities

The Committee would also like to thank everyone who took the time to testify, submit written reports or otherwise assist in the interim study.

Most important, we acknowledge the hardworking and devoted staff members of the Senate Finance Committee and of Senator Rodney Ellis. They wrote this report, developing drafts for the Committee's review and feedback. The following staff members coordinated and wrote our interim study and were critical to meeting our charges: Kalunde Wambua and Blaine Brunson.

Senate Finance Committee
Interim Charge #1

Survey and assess Texas' current tax system, including taxation authority given to units of local government. The survey should identify the economic value associated with all current taxes, as well as current exemptions and abatements. The Committee's report should include information provided by the survey.

Hearings by the Senate Finance Committee on Taxes

Date	Location	Topic
December 5, 2001	Austin	Review interim charge
February 26, 2002	Austin	General Texas business taxes
June 4, 2002	Austin	Excise taxes

Note: Refer to Appendix B-D for hearing agendas and to Appendix E for a summary of industry priorities.

Executive Summary

The tax system in the State of Texas has provided the funding for operations benefitting its citizens since the first state tax was collected in 1836. Over time, the needs and economy in this state have evolved; at the same time, the tax system has also changed. According to the Comptroller of Public Accounts, in 1930, the State of Texas' major revenue sources were the Gasoline Tax, Ad Valorem Tax and a Gross Receipts Tax.

General Tax Information

As shown in the tables below, the tax landscape has changed dramatically, particularly with the creation of the Sales and Use Tax in 1961, which now accounts for more than 55% of the state's tax revenue.

1930 Texas Tax Revenue Mix[1]

1930 Tax Revenue Mix and Totals		
Gasoline Tax	$	32,221,624
Ad Valorem*	$	25,084,246
Occupation Tax	$	300,363
Gross Receipts Tax	$	11,185,153
Fur Tax	$	15,075
Inheritance Tax	$	775,532
Franchise Tax	$	1,524,833
Poll Tax	$	1,613,721
Total Tax Revenue	**$**	**71,106,826**

*Note: In 1930, the Ad Valorem Tax was a state property tax. The state property tax was repealed in 1968. The local property tax code was not enacted into law until 1979.

2002 Texas Tax Revenue Mix[2]

2002 Tax Revenue By Source		
Sales Tax	$	14,516,341,226
Motor Vehicle Sales/Rental, Mfg	$	2,949,540,192
Motor Fuels Taxes	$	2,833,607,460
Franchise Tax	$	1,935,709,140
Insurance Occupation	$	1,045,710,105
Natural Gas	$	628,496,630
Cigarette and Tobacco Taxes	$	540,038,314
Alcoholic Beverages	$	560,197,124
Oil Production Tax	$	338,661,102
Inheritance Tax	$	334,190,915
Utility Taxes	$	311,051,398
Hotel and Motel Tax	$	230,909,206
Other Taxes	$	54,649,681
Total Tax Revenue	**$**	**26,279,102,493**

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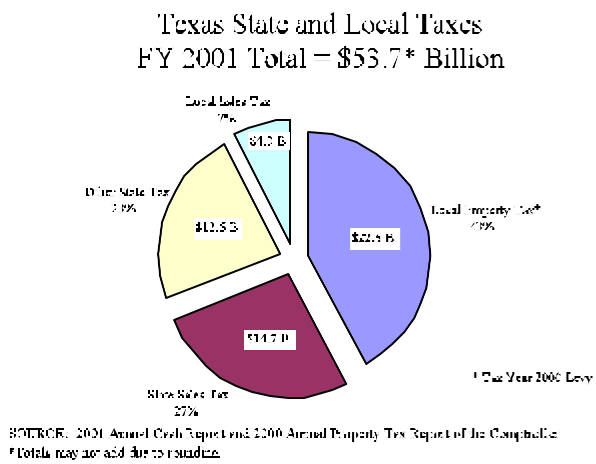
[1] Comptroller of Public Accounts, *Annual Report Of The Comptroller of Public Accounts of The State of Texas* 1930, p. 7

[2] Comptroller of Public Accounts, *State of Texas 2002 Annual Cash Report*, 2002.

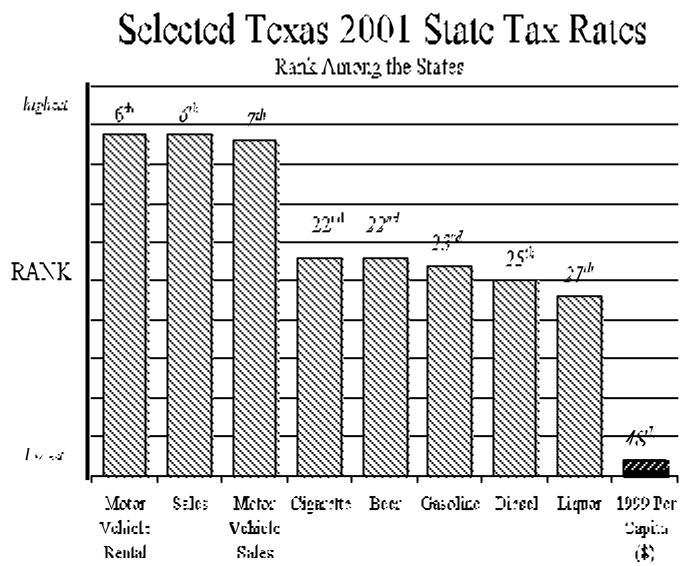
The combined Texas state and local tax systems generated a total of $53.7 billion of revenue in fiscal year 2001 as shown in the graph below.[3]



Generally, Texas is a low tax and low government spending state per capita. The bar chart below shows how Texas ranks among the states for several major taxes and overall taxation. **[4]**

[3] Carole Keeton Rylander, Comptroller of Public Accounts, December 2001.

[4] *Ibid*


Selected Texas 2001 State Tax Rates
Rank Among the States
highest
lowest
RANK
6th
6th
7th
22nd
22nd
23rd
25th
27th
48th
Motor Vehicle Rental
Sales
Motor Vehicle Sales
Cigarette
Beer
Gasoline
Diesel
Liquor
1999 Per Capita ($)

How to Read This Document

The primary purpose for this report is to compile information about each of the taxes collected by the state, the history of the tax, the monetary value of the tax, any exclusions, exemptions, deductions or abatements, and any other relevant information about each tax. This document is intended to be a reference guide of information on Texas taxes. The backbone of the report will outline each tax, give its history, and the amount of revenue an incremental increase would yield. There will also be additional sections on several topics which have been specifically requested by a member of the Senate Finance Committee or by the Lt. Governor.

Those expanded sections include:

This is not the first comprehensive report written on the Texas Tax System. A brief summary of the studies conducted in the past 15 years is available in Appendix G.

Taxes Paid by Texans

In order to have an idea of the overall picture of the Texas tax landscape, we need to look at the GSP (Gross State Product) of Texas, the taxable income, and all taxes paid by Texas citizens. Texas citizens pay federal, state and local taxes.

The following questions must be answered in order to see the big picture:

1. How large is the Texas economy?
2. How much do Texans pay in Federal taxes?
3. What are the major taxes that Texans pay?
4. Who pays more taxes, businesses or individuals?
5. What is the profile of the average Texas taxpayer?
6. Who is exempted or excluded from paying taxes?
7. How does Texas State taxes rank among the 50 states?
8. How are our tax dollars used?
9. How is the State's tax revenue generated?
10. How have taxes changed over time?
11. How much do tax exemptions cost the state?

How Large is the Texas Economy?

In calendar year 2000, Texans earned approximately $580 billion in personal income. In 2001, Texas had a Gross State Product of $620.4 billion, ranking above Russia, Canada, Spain and Austria. Only two states and three super powers' Gross State Product ranked above that of Texas (New York, California, United States, China and Japan).

How Much Do Texans Pay in Federal Taxes?

In 2001, the Internal Revenue Service collected a total of $2.1 trillion in federal taxes.[5] Of this amount, Texans paid $161.2 billion.

Internal Revenue Gross Collections Fiscal Year 2001 Amounts are in thousands of dollars]		
	Total United States	**Texas**
Total Internal Revenue collections	**2,128,831,182**	**161,178,329**
Corporation income tax	186,731,643	17,598,181
Individual Income and Employment Tax		
Total	419,408,308	28,949,632
Income tax withheld and SECA tax	1,429,257,729	98,169,830
Income tax withheld and FICA tax	4,702,645	98,061
Railroad retirement tax	7,064,093	521,335
Unemployment Insurance tax	25,289,663	1,242,130
Estate Tax	52,418,848	14,350,268
Gift Tax	4,758,287	N/A
Excise taxes	58,585,763	N/A

Texas was preceded by California and New York which paid approximately $265 billion and $195.5 billion in federal taxes, respectively. Illinois followed Texas with $113 billion paid in federal taxes.[6]

What Are the Major State Taxes that Texans Pay?

More than three quarters of our state and local tax burden consists of the property tax and the sales tax. "The largest tax paid by most Texans is the local property tax, which accounts for more than 40 percent of our total state and local tax load. State and local sales taxes account for another one-third of taxes paid by Texans." [7]

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[5] IRS Data Book, FY 2001, Publication 55b. Also, Chief Financial Officer, Revenue Accounting, Office of Revenue Systems N:CFO:R:S

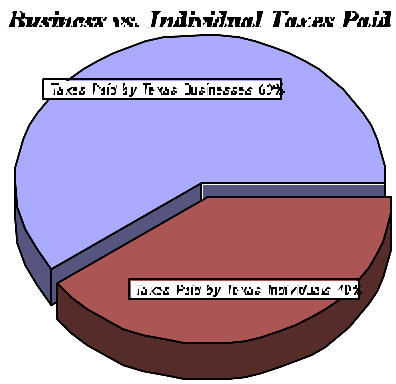
[6] IRS Data Book, FY 2001, Publication 55b. Also, Chief Financial Officer, Revenue Accounting, Office of Revenue Systems N:CFO:R:S

[7] Center for Public Policy Priorities, *Texas Taxes: The Basics*,1999. Available at http://www.cppp.org/products/reports/ttexecsum.html

Texas ranks 3rd among the states in personal income ($538 billion), yet also ranks 40th in per capita taxes of $2,247 (only 10 states tax less than Texas). Texas is one of seven states without a personal income tax and one of four states without a corporate state income tax. It also does not have a state property tax.

Who Pays More Taxes, Businesses or Individuals?

Business Taxes: Texas businesses pay approximately 60% of the taxes collected in the state. Property taxes constitute nearly half the taxes initially paid by business, and the sales tax accounts for another quarter. Of the business taxes collected, the corporate franchise tax accounts for 18% of taxes paid, making this the state's major business tax. Although businesses pay a high percentage of taxes, they are often able to pass on the cost of business taxation to consumers through price increases, to workers through lower wages, or to owners and shareholders through lower returns on investment.[8]



Sales Taxes: Initially, both individuals and businesses both pay the sales tax. However, businesses may shift sales taxes onto their consumers through higher prices. How much sales tax individuals pay depends on how much of their income they spend and what they buy. Because lower- and middle-

[8] *Ibid*

income individuals generally have to spend more of their income on necessities and can save less than persons with higher income, the sales tax takes a bigger share of their income than it does of a higher-income person.[9]

Property Taxes: Taxes on residential rental property may be borne by landlords or passed onto tenants through higher rents. Property taxes imposed on owner-occupied homes fall entirely on the homeowner, who cannot shift the tax onto someone else.[10]

[9] *Ibid*

[10] *Ibid*

Tax Incidence

The persons from whom a given tax is collected is not necessarily the one who ultimately pays the tax. It should be recognized that any tax levied directly on a business will ultimately be paid by consumers via higher prices, business owners via reduced profits or employees via reduced wages. Taxes may also be exported out of state, thereby relieving the tax burden in state. Of course, other states' taxes may end up being imported into Texas as well.

The table below is a tax incidence report and illustrates how taxes paid by businesses are borne by Texans.[11]

Taxes Initially Paid by Business in 2001: Distributional Assumptions for Final Incidence

	Borne by Texas Residents				
	Consumer Share	**Labor Share**	**Capital Share**	**Exported**	**Total**
Limited Sales and Use Tax	39%	16%	1%	44%	100%
Motor Vehicle Sales and Use Tax	54	23	1	22	100
School Property Tax					
rental property	87	0	7	6	100
agricultural property	10	34	10	46	100
commercial property	58	19	2	22	100
industrial property	17	41	2	41	100
utility property	90	3	1	6	100
mining property	10	29	4	57	100
Gasoline Tax	40	23	1	36	100
Natural Gas Tax	10	29	14	46	100
Franchise Tax					
agricultural sector	10	34	2	54	100
mining sector	10	29	2	59	100
construction sector	90	7	0	3	100
manufacturing sector	19	43	1	37	100
utility sector	90	4	0	6	100
trade sector	63	19	0	18	100
finance sector	47	16	1	37	100
services sector	84	7	0	9	100

In this chart, consumers are Texas households rather than individuals. Labor refers to Texas workers,

[11] Comptroller of Public Accounts, *Texas Exemptions and Tax Incidence*, January 2001, p.46. Available at http://www.window.state.tx.us/taxinfo/incidence/table46.html.

capital refers to business owners, and exported means the tax is shifted out of state and borne by non-Texans.

What is the Profile of an Average Taxpayer?

According to the Texas Workforce Commission, Texas statewide per capita income for the year 2002 is $26,834.[12] The Taxes Paid Table[13] shown below identifies five annual income groups, the state taxes paid by each income group, and the percent of income paid in taxes. Each income group contains approximately one-fifth of the households in Texas.[14]

Annual Family Income	Taxes Paid	% of Income Paid in Taxes
$10,915	$1,459	13.4%
$23,082	$2,111	9.1%
$35,299	$2,809	8.0%
$56,731	$3,818	6.7%
$144,954	$6,440	4.4%

The major state and local taxes paid by Texans constitute Franchise, Gas, Motor Vehicle Sales, School Property, and Sales & Use Tax. The following pie charts break down the amount paid in each of these state and local taxes by income level.

Note: These income group estimates do not include federal taxes paid.

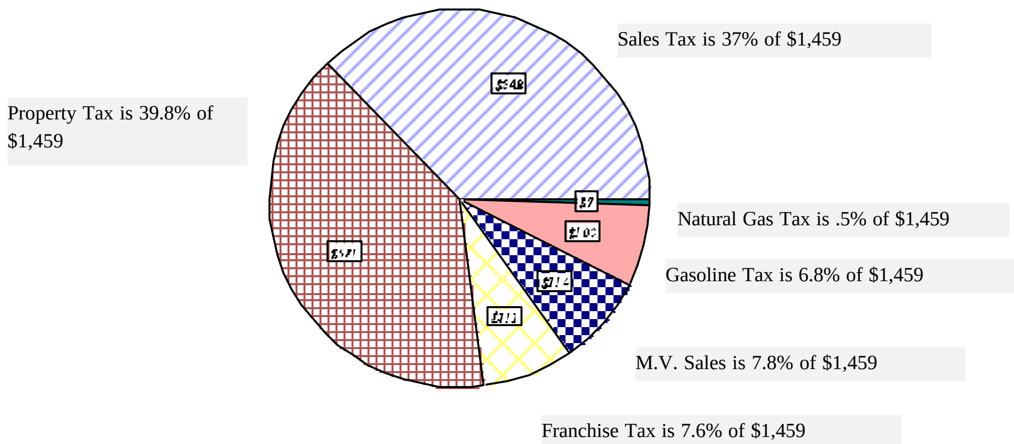
[12] Texas Workforce Commission, *Information Technology*, June 2002. Available at http://www.twc.state.tx.us/careers/infotech.html

[13] Center for Public Policy Priorities, *Who Pays Texas Taxes?* February 2001. Available at http://www.cppp.org/products/policypages/111-130/111-130html/PP115.html

[14] Income groups and taxes paid were calculated from the Texas Comptroller of Public Accounts, *Tax Exemptions and Incidence*, January 2001. Available at http://www.window.state.tx.us/taxinfo/incidence/txtax.html.

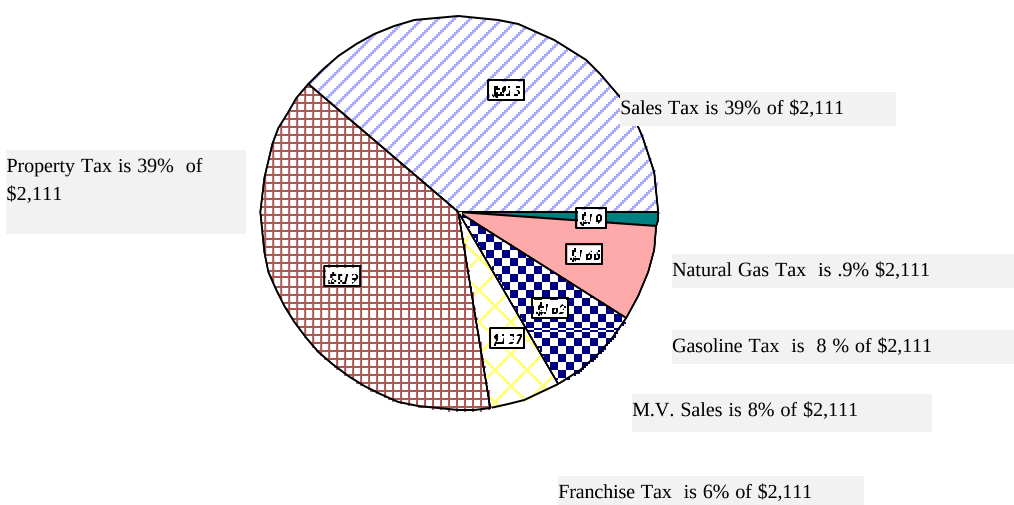
Income Level $10,915

Taxes paid are $1,459 or 13.4% of total income. Of the total taxes paid, the following pie chart breaks down the dollar amount paid in each tax.



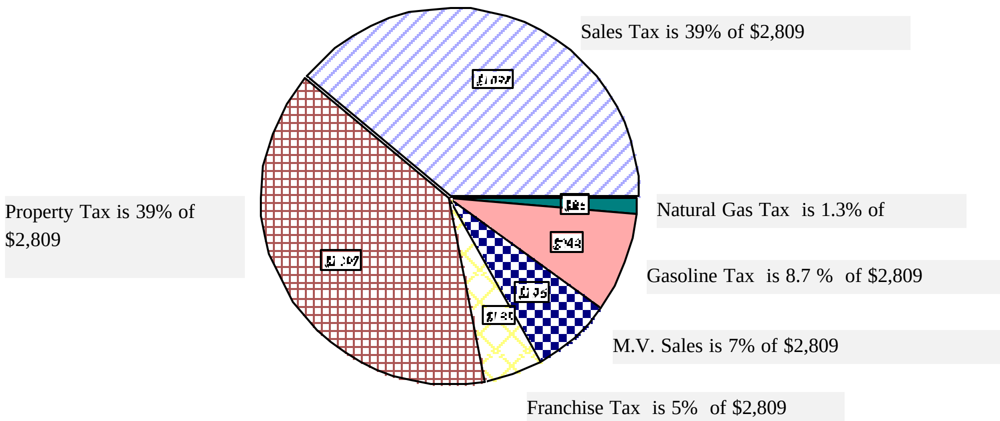
Income Level $23,082

Taxes paid are $2,111 or 9.1% of total income. Of the total taxes paid, the following pie chart breaks down the dollar amount paid in each tax.



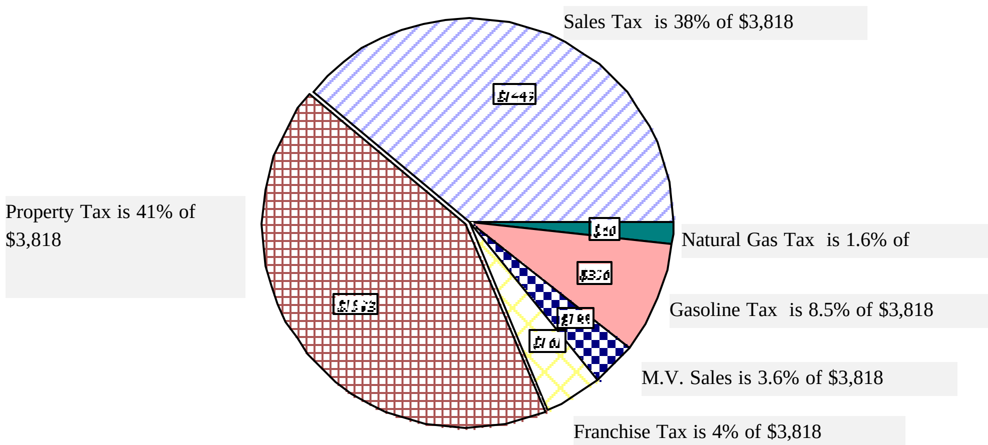
Income Level $35,299

Taxes paid are $2,809 or 8% of total income. Of the total taxes paid, the following pie chart breaks down the dollar amount paid in each tax.



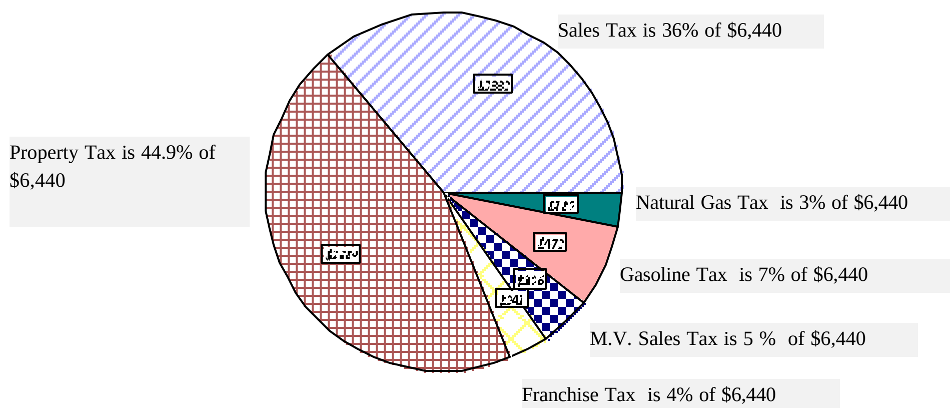
Income Level $56,731

Taxes paid are $3,818 or 6.7% of total income. Of the total taxes paid, the following pie chart breaks down the dollar amount paid in each tax.



Income Level $144,954

Taxes paid are $6,440 or 4.4% of total income. Of the total taxes paid, the following pie chart breaks down the dollar amount paid in each tax.



Regardless of income level, the majority of taxes paid are in sales and property taxes.

Who is Exempted or Excluded from Paying Taxes?

The Lt. Governor also asked the committee to examine the areas in current tax law where exemptions, exclusions and abatements have been granted. Generally, most types of taxes offer some type of provision that allows certain taxpayers to pay lower taxes or permits certain transactions to occur untaxed. The major school property tax exemptions are received by homeowners, owners of agricultural land, and businesses.

The sales tax exempts groceries and other necessities, which aid lower income Texans. Many services are exempt from the sales tax, such as legal, accounting, and stock brokerage fees. In this report, we will discuss exemptions, exclusions and abatements in the specific section to which they apply.

How Does Texas Taxes Rank Among the 50 States?

Texas taxpayers' total tax load is well below the national average. In fiscal year 1999, the state and local tax burden was $2,247 per capita, ranking 44th among the 50 states. In fiscal 2000, the state and local tax burden was $2,456. The following table compares Texas state and local taxes as a percentage of income to Texas total tax burden as a percentage of income and how each ranks among the states.

Texas State Local and Total Tax Burden as a Percentage of Income 1971-2002[15]

Total tax burden represents a combination of federal, state, and local tax burdens.

Texas Taxes as a Percentage of Income, State and Local Tax Burden vs. Total Tax Burden

	State and Local Tax Burden		Total Tax Burden				State and Local Tax Burden		Total Tax Burden		
Year	Tax Burden	Rank	Tax Burden	Rank	Change in Ranking	Year	Tax Burden	Rank	Tax Burden	Rank	Change in Ranking
1971	8.10%	47	27.00%	38	9	1987	9.50%	25	30.80%	11	14
1972	8.40%	48	28.10%	34	14	1988	9.70%	22	30.50%	14	8
1973	8.10%	46	28.30%	31	15	1989	9.60%	27	30.60%	15	12
1974	8.20%	47	29.20%	32	15	1990	9.50%	30	30.00%	23	7
1975	8.10%	48	27.50%	34	14	1991	9.70%	25	29.80%	22	3
1976	8.10%	48	28.00%	36	12	1992	9.80%	24	29.80%	24	0
1977	8.20%	46	28.60%	30	16	1993	9.80%	25	29.90%	24	1
1978	8.00%	46	28.60%	31	15	1994	9.70%	31	30.20%	24	7
1979	7.70%	48	28.60%	35	13	1995	9.60%	35	30.40%	28	7
1980	7.60%	47	29.00%	29	18	1996	9.50%	37	30.80%	25	12
1981	7.60%	48	30.00%	27	21	1997	9.20%	43	30.60%	35	8
1982	7.70%	47	29.70%	25	22	1998	9.00%	44	31.10%	31	13
1983	7.80%	47	29.10%	21	26	1999	9.00%	44	31.40%	30	14
1984	0.10%	44	28.90%	18	26	2000	8.90%	45	31.90%	33	12
1985	8.40%	40	29.30%	15	25	2001	9.00%	46	31.30%	34	12
1986	8.80%	37	29.80%	10	27	2002	9.00%	47	30.40%	36	11

[15]Tax Foundation, *Comparing the Total Tax Burden in Each State to Just the State/Local Tax Burden*, 1986-2002. Available at http://www.taxfoundation.org/statelocal70-02.html.

Although the state, local, and total tax burden is lighter than in other states, the property tax burden in Texas is heavier than in the average state, ranking 16th at $938 per capita. "Our property and sales tax rates are among the highest in the country, since most Texas government revenue comes from just these two taxes. One reason for high property tax rates is the shrinkage in the value of taxable property. Taxable property values have only recently surpassed their 1985 peak, in part because of the growth in residential, commercial, and industrial exemptions."[16]

How Are Our Tax Dollars Used?

About half of all tax revenue goes to the state government; the other half goes to local governments, primarily to school districts. The bulk of state taxes pay for public and higher education and health and human services, which together account for three quarters of the state budget. Local taxes are divided evenly between supporting public education and funding services of cities, counties and special districts. Schools receive about equal amounts of funding from state and local taxes.[17] The federal government has played an increasingly important role in supporting state services, but future federal funding is very uncertain, placing great pressure on state revenue sources.[18] This report offers an overview of the sources of Texas revenue, who pays them, how much they pay, and how they are allocated.

[16]Center for Public Policy Priorities, *Texas House Holds Tax Bills: Relatively Light, But Regressive, 2000*. Available at http://www.cppp.org/products/policypages/91-110/91-110html/PP104.html

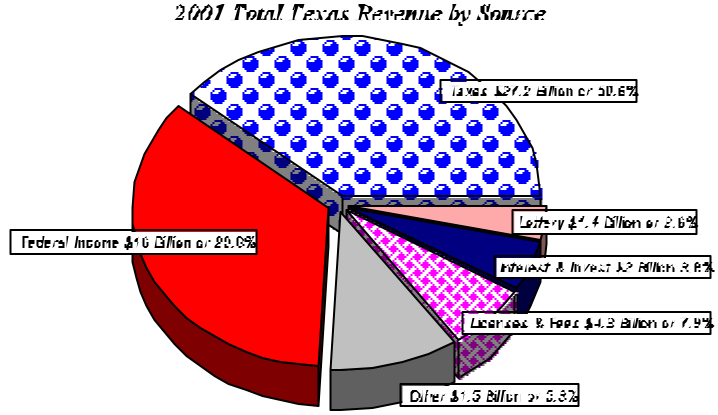
[17]Center for Public Policy Priorities, *Texas Taxes: The Basics*, 1999. Available at http://www.cppp.org/products/reports/ttexecsum.html

[18]*Ibid*

State Tax Assessment: A 2001-2002 Look at Texas Taxes

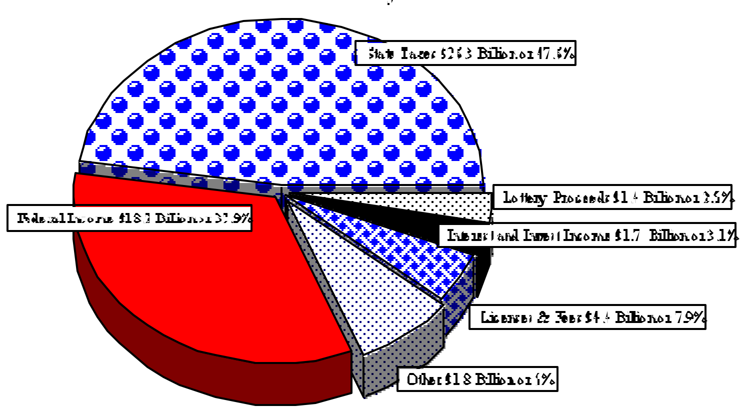
Total Texas revenue for fiscal year 2001 was $53.8 billion. This is an 8% increase in revenue from fiscal year 2000. Federal Income accounted for 29.8% of Texas revenue. Approximately 50.6% of total state revenue was generated through state and local taxes.

2001 Total Texas Revenue by Source



Total Texas revenue for fiscal year 2002 was $55.2 billion. This is an increase of 2.6% from fiscal year 2001. Federal Income accounted for 32.9% of Texas revenue. Approximately 47.6% was generated through taxes.[19]

2002 Total Texas Revenue by Source



[19] Texas Comptroller of Public Accounts, *State of Texas 2002 Annual Cash Report,* November 2002.

Note: Totals may not add due to rounding.

Texas relies primarily on the state's sales tax to generate revenue.

How is the State's Tax Revenue Generated?

As shown in the previous graphs, the majority of the state's revenues collected are from state taxes. Approximately 51% of the state's revenue comes from state taxes, 30% comes from federal income, 15% comes from various fees, and 4% comes from interest on investments and land income.

Overall, state tax collections for fiscal year 2002 were down by 3.5% from fiscal year 2001. The following table outlines the tax collection for both years as well as the percentage change in revenues. [20]

2001-2002 Tax Revenue By Source

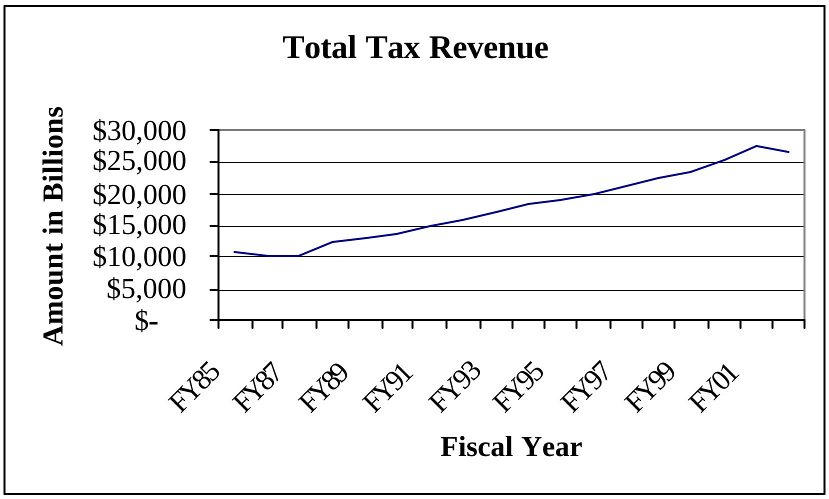
Tax	2001	% Change From 2000	2002	% Change From 2001
Sales Tax	$ 14,663,067,887	4.9%	$ 14,516,341,226	-1.0%
Motor Vehicle Sales/Rental, Mfg Housing Sale	$ 2,905,538,398	4.4%	$ 2,949,540,192	1.5%
Motor Fuels Taxes	$ 2,765,510,548	2.9%	$ 2,833,607,460	2.5%
Franchise Tax	$ 1,960,365,032	-5.1%	$ 1,935,709,140	-1.3%
Insurance Occupation Taxes	$ 820,045,596	2.9%	$ 1,045,710,105	27.5%
Natural Gas Production Tax	$ 1,596,885,766	128.9%	$ 628,496,630	-60.6%
Cigarette and Tobacco Taxes	$ 584,586,277	9.9%	$ 540,038,314	-7.6%
Alcoholic Beverages Taxes	$ 541,305,988	5.1%	$ 560,197,124	3.5%
Oil Production Tax	$ 442,580,206	6.2%	$ 338,661,102	-23.5%
Inheritance Tax	$ 322,354,926	15.8%	$ 334,190,915	3.7%
Utility Taxes	$ 339,403,570	28.4%	$ 311,051,398	-8.4%
Hotel and Motel Tax	$ 246,813,166	4.7%	$ 230,909,206	-6.4%
Other Taxes	$ 41,755,055	17.8%	$ 54,649,681	30.9%
Total Tax Revenue	**$27,230,212,416**	**7.7%**	**$26,279,146,493**	**-3.5%**

* Numbers may not add due to rounding.

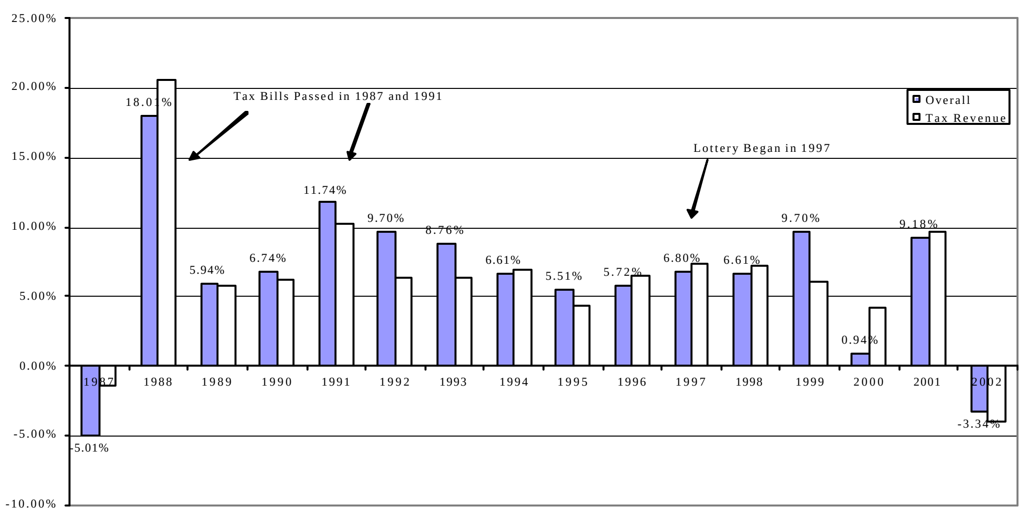
[20] Texas Comptroller of Public Accounts, *State of Texas 2002 Annual Cash Report,* November 2002.

Overall, total tax collections as well as total General Revenue collections in Texas have risen significantly from fiscal 1985 to fiscal 2001.

State Tax Revenue Over Time 1985-2002 (Total Texas Tax Collections in Billions)[21]



Overall General Revenue Income Changes 1987-2002



[21] *Ibid*

As Texas state tax revenues have steadily increased over time, so has the value of the tax exemptions granted.

Cost of Tax Exemptions to the State of Texas

In fiscal year 2001, exemptions from the sales, franchise, gasoline, and motor vehicle sales taxes amounted to $24.0 billion. Sales tax exemptions totaled $22.4 billion, while franchise tax exemptions totaled $1.3 billion. Gasoline tax exemptions amounted to $124 million, and motor vehicle sales tax exemptions were $161 million. Exemptions from local school district property taxes will amount to an additional $3.3 billion in fiscal 2002. These amounts include exemptions, exclusions, special rates, deductions, and discounts written into the tax law for these taxes and totaled $27.3 billion.[22]

2001 Tax Exemptions and the Associated Costs	
Tax	**Cost of Exemption**
Sales Tax	$22.4 Billion
Local Property Taxes	$3.3 Billion
Franchise Tax	$1.3 Billion
Motor Vehicle Sales Tax	$.2 Billion
Gasoline Tax	$.1 Billion
Total:	**$27.3 Billion**

In fiscal year 2001, the combined revenues from the sales tax, franchise tax, gasoline tax, and motor vehicle sales tax were $22.4 billion and accounted for almost 82 percent of the state's total tax revenue.[23]

[22]Comptroller of Public Accounts, *Tax Exemptions &Tax Incidence*, January 2001, p.1.

[23] Comptroller of Public Accounts, *State of Texas 2002, Annual Cash Report*, 2002.

The following sections of this report focus on each of the major state taxes, the associated exemptions and the cost of these exemptions to the state.

Discussion of Each Major Texas Tax

Sales and Use Tax

Sales and Use Tax Facts	
Date Enacted	1961
Rate When Enacted	2%
Current Rate	6.25%
Last Changed	1990
2001 Net Revenue**	$14.6 Billion
2002 Net Revenue**	$14.5 Billion
State Ranking	7th
Estimated Average Revenue Per Penny Increase*	$2.3 Billion

* Each of the 6.25 pennies that make up the current tax rate produced an average of $2.3 billion in revenue in fiscal 2001. It is important to note, however, that as the rate is changed, each additional penny produces less revenue than the preceding penny generates.

**Does not include the boat and boat motor sales tax.

Overview

The sales tax is a tax on certain transactions. In general, it is imposed on final sales, rentals, and lease of tangible personal property-physical goods and on sales of some services, such as the repair of tangible personal property, amusements and telephone services.

The Texas state sales and use tax is the 7th highest in the US (The US average sales tax is 5.14%). This is the state's single largest source of tax revenue, exceeding 55% of total tax collections.

Top Sales Tax Rates in the Nation

The following chart lists the 15 highest standard state level sales and use tax rates. The range of local taxes is included as a quick reference. The local use tax rate information can be used to determine whether the use tax also applies to local taxes. If this column contains a "YES", then local taxes apply to both intra-state and inter-state transactions. If this column contains a "NO", then local taxes only apply to intra-state transactions.[24]

2002 Top 15 Sales Tax Rates in the US			
State	**State Rate**	**Range of Local Rates**	**Local Rates Apply To Use Tax**
Mississippi (1)	7.00%	0% - .25% (4)	No
Rhode Island	7.00%	0%	N/A
Tennessee (1)	7.00%	1.5% - 2.75% (3)	Yes
Minnesota (1)	6.50%	0% - 1% (4)	Yes/No
Washington	6.50%	.5% - 2.4%	Yes
Illinois (1)	6.25%	0% - 3.00% (4)	No
Texas	**6.25%**	**0% - 2% (4)**	**Yes**
California	6.00%	1.25% - 2.75%	Yes
Connecticut (1)	6.00%	0%	N/A
Florida(1)	6.00%	0% - 1.5% (3), (4)	Yes
Kentucky (1)	6.00%	0%	N/A
Michigan (1)	6.00%	0%	N/A
New Jersey (2)	6.00%	0%	N/A
Pennsylvania	6.00%	0% - 1% (4)	No
West Virginia	6.00%	0%	N/A

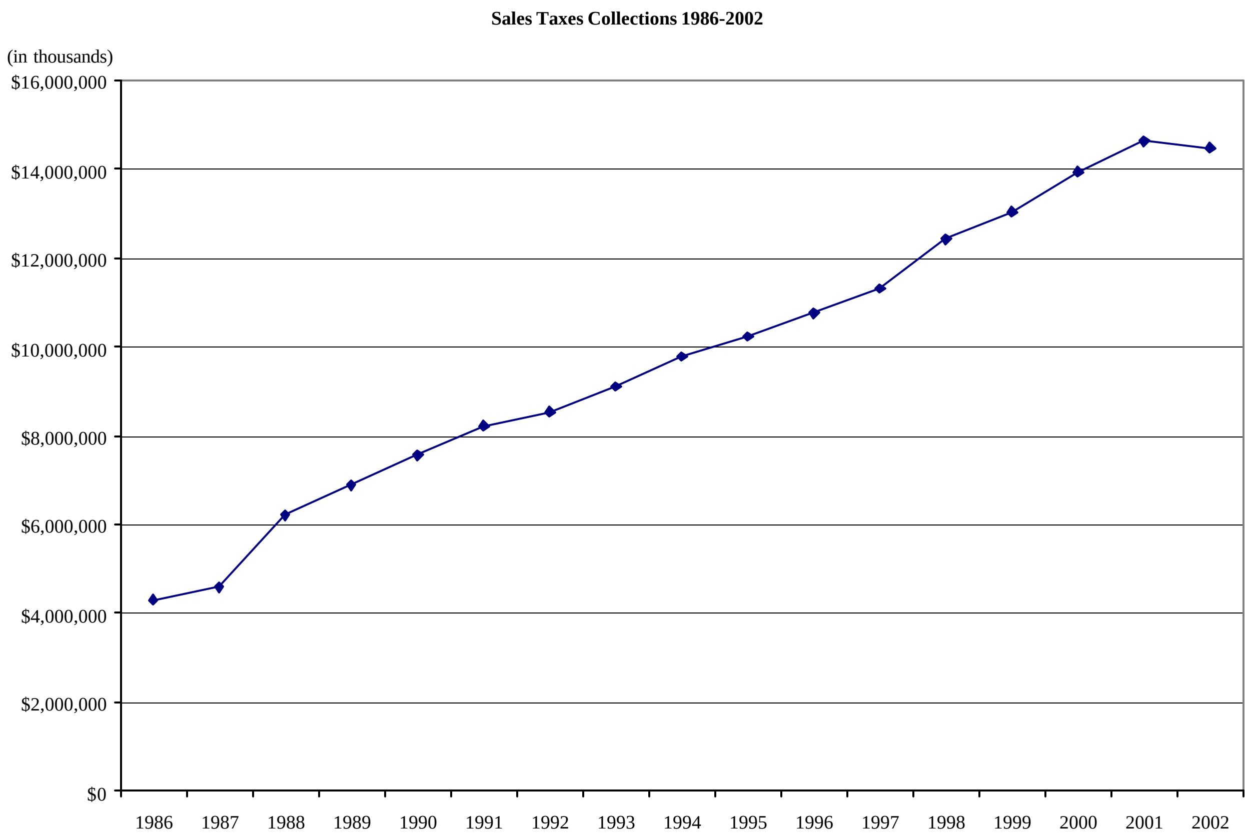
Notes:

1. The state has reduced rates for sales of certain types of items.

2. Effective 7/1/94, sales occurring in Salem County will be taxed at the reduced state sales tax rate of 3%.

3. A cap on the local sales/use tax applies on sales of any item of tangible personal property.

[24] Sales Tax Institute, *Sales and Use Tax Rates,* September 2002.



4. Some local jurisdictions do not impose a sales tax.

Sales Taxes Collections Over Time, 1986-2002

Sales Tax Revenue Allocation

Revenues from the limited sales and use tax are almost entirely deposited into the General Revenue Fund. The remainder consists of two allocations; one constitutionally mandated and the other statutory.

Sales tax revenue from the sale of motor lubricants for use in motor vehicles used on public roadways is credited to the State Highway Fund, as required by the Texas Constitution. Sales tax revenue from the sale of sporting goods, in an amount not to exceed $32 million per year, is transferred to the Texas Parks and Wildlife Department (TPWD). The Comptroller estimates sales tax collections on both motor lubricants and sporting goods, as provided by statute.

The transfers to TPWD are made up of three components. The state Parks Account and the Texas Recreation and Parks Account each receive $15.5 million per year. The Texas Parks and Wildlife Capital Account receives $1 million, bringing the total for all three accounts to the maximum of $32 million annually.

The following table shows the limited sales and use tax deposited to each fund/account for the past three years.

Revenue Distribution of Limited Sales and Use Tax[25]

Fiscal Year	General Revenue Fund	State Highway Fund	State Parks Acct.	Texas Recreation and Parks Acct.	Texas Parks & Wildlife Capital Acct.
2000	$ 13,910,473,000	$ 27,573,000	$ 15,500,000	$ 15,500,000	$ 1,000,000
2001	$ 14,600,046,239	$ 28,841,000	$ 15,500,000	$ 15,500,000	$ 1,000,000
2002	$ 14,446,771,647	$ 30,168,000	$ 15,500,000	$ 15,500,000	$ 1,000,000

[25] Comptroller of Public Accounts, 9/18/02.

Discussion of the Erosion of the Sales Tax Base

Overview

The sales tax base is made up of all the transactions upon which sales and use taxes are collected. Like many states, when the Texas sales tax was enacted in 1961, it applied predominantly to the sale of tangible goods and property, and at that time services accounted for a smaller portion of economic activity. Since services have grown rapidly and are generally not subject to the sales and use tax there has been a steady decline in the sales tax base. Numerous states have expanded exemptions to the sales and use tax, further chipping away at the base.

In 1960, American families spent about $0.41 of every dollar on services. By 2000, it was $0.58.[26] The inexorable shift in consumer expenditures from the purchase of goods and services to the purchase of services continues to raise concerns about the long-term vitality of retail sales taxes. This factor coupled with the decline in the economy caused sales tax collections for fiscal 2002 to be down from fiscal 2001 by $146,726,661.[27]

"While a stable and growing economy has improved Texas' fiscal conditions, slowed expansion to services, long-term fiscal pressures facing the state make it likely that the legislature may need to consider broadening the states sales tax to include various services in the future."[28]

[26] Business Weekly, *States: A Rebound Won't End Red Ink,* June 17, 2002.

[27] Texas Comptroller of Public Accounts, *State of Texas 2002 Annual Cash Report,* 2002.

[28] National Conference of State Legislatures, *Financing State Government in the 1990s,* ed. Ronald Snell, December 1993, pp.33-35.

Sales & Use Tax Exemptions, Exclusions and Discounts

Exemptions are provided for certain basic necessities, such as groceries, residential gas, electric utilities, and prescription and over the counter drugs. Sales tax exemptions are divided into three categories.

1. **Exemptions:** Protects items that would be taxable except for specific provisions, i.e groceries.

2. **Exclusions:** Transactions not taxed because they fall outside the general legal definition of taxable sale, i.e intangible items, stocks, bonds, etc.
   Note: currently only specified services are under the sales tax.

3. **Discounts:** Handling fees that tax law allows tax-permit holders to keep in exchange for collecting the sales tax and sending it to the state on time.

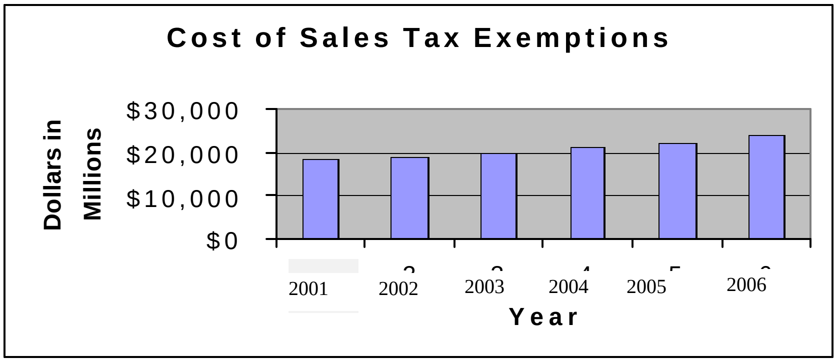
Cost of Sales Tax Exemptions, Exclusions, and Discounts[29]

Cost of Sales Tax Exemptions, Exclusions, and Discounts Fiscal Years 2001 to 2006 (in millions of dollars)						
	2001	2002	2003	2004	2005	2006
Exemptions	$18,231.50	$19,187.10	$20,161.50	$21,310.10	$22,546.10	$23,833.50
Exclusions	4,054.40	4,297.60	4,558.00	4,861.10	5,183.00	5,561.80
Discounts	116.7	120.5	126.7	132.9	138.2	143.7
Total	**$22,402.60**	**$23,605.20**	**$24,846.20**	**$26,304.10**	**$27,867.30**	**$29,539.00**
Note: Totals may not add due to rounding.						

[29] Texas Comptroller of Public Accounts, *Tax Exemptions and Tax Inferences, A Report to The Governor and the 77th Legislature,* 2001. Available at http://www.window.state.tx.us/taxinfo/incidence/table3.html

Cost of Limited Sales and Use Tax Exemptions

The following table lists the sales and use tax exemptions and the associated cost to the State of Texas.[30]



Even though exemptions total approximately $22.4 billion a year, the top 5 exemptions for 2002 totaled $15.6 billion. The associated amounts of each of the 5 exemptions are listed below:

1. Materials used in manufacturing - $8 billion. (Materials used in manufacturing are exempt in every state).
    a. Section 151.318 of the Texas Tax Code exempts the following:
        i. several types of items used in manufacturing products for sale, including materials that become part of the manufactured product.
        ii. tangible personal property that is necessary or essential to the manufacturing operation if it causes a physical or chemical change in the product being manufactured.
        iii. services performed directly on the manufactured product;
        iv. certain chemicals used during the manufacturing operation;
        v. wrapping and packaging materials;
        vi. certain equipment used to reduce water use and to reuse and recycle wastewater streams in the manufacturing process.
        vii. certain purchases by a person overhauling or repairing jet turbine aircraft engines; publishers of newspapers that are distributed free of charge; and purchases of semiconductor fabrication clean rooms and equipment.
    b. The exemption specifically excludes
        i. equipment rented for less than a year

[30] Comptroller of Public Accounts, *Windows on State Government,* August, 2002. Available at http://www.window.state.tx.us/taxinfo/incidence/limit.html,.

    ii. hand tools
    iii. office supplies
    iv. equipment and supplies used in maintenance and janitorial activities.
    v. items relating to sales or distribution activities,
    vi. storage and maintenance
    vii. research and development
    viii. transportation.

2. Insurance Premiums - $2.7 billion. (Insurance premiums are exempt due to the fact that they are taxed under other law).
    a. Section 151.308 of the Texas Tax Code exempts from sales tax items taxed under other Texas tax laws.
    b. It is assumed that if the sales tax were applied to insurance, buyers would pay sales tax on the purchase of insurance policies, with the revenue collected and remitted by insurance companies.
3. Motor Vehicles Sales - $2.5 billion. (Motor vehicles sales are exempt do to the fact that they are taxed under other law).
    a. Section 151.308 of the Texas Tax Code exempts from sales tax items taxed under other Texas tax laws.
    b. Motor vehicles are currently taxed under a separate sales tax at the same rate as the State sales tax.
4. Motor Fuels - $1.18 billion. (Motor fuels are exempt due to the fact that they are taxed under other law).
    a. Section 151.308 of the Texas Tax Code exempts from sales tax items taxed under other Texas tax laws.
    b. Motor fuels are taxed under the motor fuels tax.
5. Food for Home Consumption - $1.18 billion
    a. Section 151.314 of the Texas Tax Code exempts food products for human consumption, like cereals, milk, meat, poultry, fish, eggs, vegetables, fruit, spices, salt, sugar, coffee, and tea. It does not exempt meals sold in restaurants, vitamins, over-the-counter medicines, soft drinks, ice, and candy.
    b. The sales tax law has exempted food products since it was enacted in 1961.

Refer to Appendix H for a detailed listing of the cost of sales tax exemptions.

Revenue Generated from Repealing Exemptions[31]

The repeal of various sales and use tax exemptions could generate additional revenue. For illustrative purposes only, the table below shows additional revenue that may be realized through the repeal of certain sales and use tax exemptions.

Potential Revenue Generated from Repealing and Eliminating Select Sales and Use Tax Exemptions

Potential Changes to the Current Tax Code	**2004-05 Revenue in Millions**
Repeal exemption for prescription & O-T-C drugs, and medical devices	$ 848.5
Eliminate exemptions for agricultural items	$ 636.6
Repeal exemption for water	$ 454.9
Repeal exemption to include aviation fuel	$ 173.0
Repeal exemption for certain ships and ship equipment	$ 89.9
Repeal exemption for school lunches and food sold to hospital patients, residents of retirement homes or during church functions	$ 86.6
Repeal exemption for newspaper inserts	$ 57.2
Repeal exemption for railroad fuel and supplies	$ 16.9
Repeal exemption for subscription sales of magazines	$ 15.3
Repeal partial exemption for certain items of equipment used in timber operations	$ 19.4
Repeal provision authorizing refunds on certain items for a Texas Department of Economic Development designated enterprise project	$ 10.3
Repeal exemption to include agricultural containers	$ 0.8
Repeal partial exemption for food items sold through vending machines	negligible
Total	**$ 2,409.4**

Note: Unless specifically stated, estimates reflect full years; no adjustments for implementation of tax law changes assumed. Estimates reflect static changes only; no dynamic economic effects included.

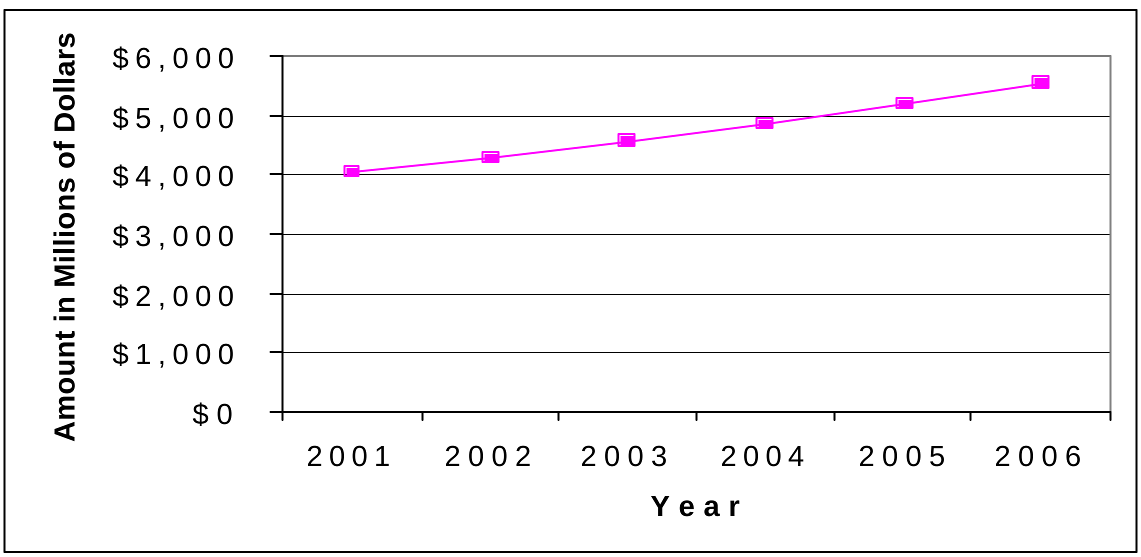
[31] Texas Comptroller of Public Accounts, 10/2002

Cost of Selected Service Exclusions from the Sales Tax[32]

The table and graph below estimates the cost of service exclusions, i.e. the total revenue generated if these services were taxed, from the sales tax for fiscal years 2001 through 2006.

Selected Service Exclusions from the Sales Tax Graph, 2001-2006

Fiscal Years 2001 to 2006 (in millions of dollars)						
	2001	**2002**	**2003**	**2004**	**2005**	**2006**
Business and professional services	$ 2,935	$ 3,124	$ 3,324	$ 3,555	$ 3,797	$ 4,084
Construction Labor	$ 551	$ 570	$ 596	$ 628	$ 666	$ 710
Other Services	$ 315	$ 342	$ 364	$ 389	$ 414	$ 446
Personal services	$ 248	$ 261	$ 274	$ 289	$ 305	$ 322
Total	**$ 4,054**	**$ 4,298**	**$ 4,558**	**$ 4,861**	**$ 5,183**	**$ 5,562**
Note: Totals may not sum because of rounding.						



[32] *Ibid*

Services Excluded from Sales and Use Taxes in Texas and Value in 2001:[33]

1. Business and professional services - $2.9 billion
    a. Physician services - $547.9 million
    b. Legal services - $346.1 million
    c. Other health care - $293.6 million
    d. Architectural and engineering services - $245 million
    e. Freight hauling - $213.5 million
    f. Financial services brokerage - $176.8 million
    g. Dental services - $176.2 million
    h. Accounting and audit services - $168.2 million
    i. Real estate brokerage and agency - $164.4 million
    j. Advertising media - $161.1 million
    k. Contract computer programming - $89.4 million
    l. Management consulting and public relations - $87 million
    m. Other financial services - $66 million
    n. Temporary labor supply - $44.5 million
    o. Research and development laboratory services - $36.8 million
    p. Testing labs - $36.6 million
    q. Veterinary services - $27.4 million
    r. Employment agency services - $25.5 million
    s. Economic and sociological research - $15.4 million
    t. Other transportation (except scheduled passengers) - $13.2 million

2. Residential Construction Labor - $550 million
    a. New residential construction - $252.5 million
    b. New nonresidential construction - $216.3 million
    c. Residential repair and remodeling - $81.8 million

3. Personal services - $248million
    a. Funeral - $427 million
    b. Child day care - $144.3 million
    c. Barber and beauty services - $48.3 million
    d. Miscellaneous personal services - $12.8 million

[33] Texas Comptroller of Public Accounts*: Tax Exemptions and Tax Incidences, A Report to the Governor and 77th Legislature*, 2001. Available at http://www.cpa.state.tx.us/taxinfo/incidence.

4. Automotive maintenance and repair - $221 million

5. Travel arrangement - $30.7 million

6. Private vocational education - $23.1 million

7. Other private educational services - $21.6 million

8. Car washes - $19 million

9. Interior design (no estimate provided for 2001)

The list above is from the Comptroller's Tax Exemption report for 2001. In addition, the Finance Committee asked the Comptroller's office to update the specific exemptions reviewed by the Joint Committee in 1997 to reflect values for FY 04-05 (refer to Appendix R for updates).

Expanding the Texas Sales Tax Base to Include Selected Services[34]

For illustrative purposes only, the table below shows additional revenue that may be realized by

Services	Revenue in Millions
Potential Changes to Current Tax Code	**2004-05**
Expand base to include physicians services	1,370.5
Expand base to include legal services	865.8
Expand base to include "other" health care services	734.3
Expand base to include engineering & architectural services	612.8
Expand base to include automotive maintenance and repair labor	552.8
Expand base to include dental services	440.8
Expand base to include accounting & audit services	420.8
Expand base to include advertising media services	402.8
Broaden base to include child day care services	336.2
Expand base to include contract computer programming services	223.7
Expand base to include management consulting & public relations services	217.6
Expand base to include barber & beauty services	120.7
Expand base to include vocational and other private education services	111.9
Expand base to include temporary labor supply services	111.2
Expand base to include commercial research & development laboratory services	92.0
Expand base to include coin-operated services	86.8
Expand base to include veterinary services	68.3
Expand base to include employment agency services	63.8
Expand base to include car wash services	47.5
Expand base to include commercial economic, social or educational research services	38.4
Expand base to include miscellaneous transportation services	33.0
Expand base to include miscellaneous personal services	32.7
Expand base to include interior design services	14.9
Broaden base to include mailing services (includes addressing, packaging and labeling services) & secretarial services (includes letter & resume writing services & proofreading services)	14.5
Broaden base to include appraisal services including real estate & other (insurance appraisal currently taxable)	12.9
Broaden base to include disinfecting services (includes sanitizing services)	1.2
Subtotal Sales & Use Tax on Additional Services	**$ 7,027.90**

expanding the sales tax base to include various services.

[34]Comptroller of Public Accounts, 10/2002

Note: Unless specifically stated, estimates reflect full years; no adjustments for implementation of tax law changes assumed. Estimates reflect static changes only.

Services Taxed in Other States

Given the fiscal straits that most states have encountered in recent years, many have started looking to the service industries for additional sources of sales tax revenues. According to speakers discussing sales and use taxes during the Multistate Tax Commission's 12th Business-Government Dialogue on State Tax Uniformity, “The states that collect sales tax should expand their bases to include taxes on at least some services. The services that are the easiest to make the case for taxing are those closely related to a tangible product, such as photo finishing, the management and labor components of construction costs, and repairs. In fact, taxing repairs is important to keeping the playing field level in the market, ‘otherwise you distort the decision, do we repair or replace.’ States that don't tax repairs are doing harm to their economies. Adding some of these services to the tax base could mean additional revenue of between 20 percent and 30 percent. Add business-to-business services, and we are talking an increases of up to 70 percent.”

Another program participant and former tax official pointed out that “Once people are used to taxes on services they are not inherently more controversial than any other taxes.” New Mexico is a good example of the above statement. New Mexico has a broad tax base which includes many services. “The taxes are not controversial because the law was enacted in 1935,” he said.

Currently, only Hawaii, New Mexico, and South Dakota generally impose their sales taxes on all services, subject to specified exceptions. In general, states have followed a piecemeal approach to taxing services. Colorado and Connecticut are good examples of states that did not include the taxation of services when enacting its sales tax, and over time have extended the sales tax to include services. Nebraska is another state that is expanding its tax base to services.

The following pages offer more detail on how each of the states mentioned address taxing services.

Hawaii

Taxing all services has been part of Hawaii's General Excise Tax (GET) since its enactment in 1935. When enacted Hawaii's GET rate was 1.25%; today, Hawaii's General Excise Tax rates are: [35]

1. Four percent for retail, rent, interest, sale of services (including medical, contracting, printing, commissions, telecommunications)
2. One-half percent for producing, manufacturing, wholesaling, selected intermediary services
3. One-fifteenth percent for insurance solicitors and agents

New Mexico

Unlike most other states, New Mexico has a Gross Receipts Tax (GRT) rather than a sales tax. The fundamental difference is the party liable for the tax. The Gross Receipts statewide tax rate is 5%, but county and municipal governments can and do impose local gross receipts taxes over the state rate of 5%. The tax rate therefore varies by location and currently ranges from 5.125% to 7.1875%.

The GRT is a tax on business for the privilege of doing business in this state, and the tax applies to transactions rather than items.

There are four kinds of transactions taxed:

1. Sale of property in New Mexico,
2. Sale of services performed in New Mexico,
3. The lease of property used in New Mexico, and
4. The sale of research and development services performed out of state when initial use of the product of the R&D services occurs in New Mexico. The tax here is on the seller, not on the buyer, although the seller is not stopped from recovering tax costs from the purchaser, just as it would any other overhead costs.

All transactions are presumed taxable unless a statute provides a specific exemption or deduction. The tax is on the gross amount billed to the customer, not net after business expenses.

The gross receipts tax was enacted in 1935, and services have been a part of the tax base since enactment. The taxation of the sale of services to the seller has been extremely successful as far as the economic impact on state revenues is concerned.

New Mexico is a state without a large amount of industry, thus the tax base must be broad enough to provide required public services. To date, the expected revenue has emerged, but there is constant

[35] Tax Foundation of Hawaii, *General Excise Tax FAQ*, October 2002. Available at http://www.tfhawaii.org/faq-get002.html.

chipping away by interests who want exemptions and deductions. The more that is chipped away, the greater becomes the pressure on other sources of revenue to make up the difference: property tax, personal income tax, corporate income tax, oil and gas taxes, etc.[36]

South Dakota

In South Dakota, the retail sales and service tax is imposed on the privilege of engaging in business as a retailer. The sales and service tax applies to retail sales in South Dakota of tangible personal property, consisting of goods, wares, or merchandise, to consumers or users. The tax is also imposed on the gross receipts of any person engaging in the practice of any business in which services are rendered. All services are taxable except those specifically exempted. (An example of tax exempt services are professional services relating to health.)

In addition, South Dakota imposes an excise tax upon the gross receipts of all prime contractors. The contractor must be engaged in realty improvement contracts with a building contract valued at over $100,000. The excise tax rate is 2 percent.

The South Dakota sales and use tax rate is generally 4 percent. Local governments in South Dakota are allowed to assess a local sales and use tax.[37]

Effective July 2001, South Dakota repealed service exemptions on waste disposal, veterinarian, and ground and air transportation services. However, as of January 1, 2006, when tangible personal property and/or passengers are transported, this service may only be taxed if the origin and destination are within the same municipality. (H.B. 1001).[38]

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[36] New Mexico Tax Research Office, October 2002

[37] South Dakota's Governors Office of Economic Development, *South Dakota's State Taxes*, October 2002. Available at http://www.sdgreatprofits.com/start-up/taxes2.htm.

[38] Sales Tax Institute, *Sales Tax News and Tips,* October 2002. Available at http://www.salestaxinstitute.com/news_and_tips.html#Services%20Arc.

Colorado

In January 1935, Colorado enacted the Emergency Retail Sales Tax Act, a 2% sales tax. The legislature passed the measure in a few weeks to satisfy the requirement to match federal unemployment relief dollars with a state contribution by the end of January. In 1936, it was amended to include a use tax; and in November 1936, voters approved extending the tax. In 1937, the sales and use tax were combined, and the expirations (sunsets) were deleted. In 1939, Colorado enacted a service tax, which was discontinued after WW II. The service tax applied to any services which were not already subject to sales tax, mainly personal services like auto repair, dry cleaning, plumbing, etc. The state sales tax increased to 3% in 1965, to 3.5% for 1983-4, back to 3% and then dropping to 2.9% on 1/1/2001.[39] Currently, Colorado taxes the following services:

1. Rooms and accommodations tax (enacted in 1959).

2. Catering tax was enacted in 1945 (As an offshoot of taxing restaurant meals at full price, whether cafeteria style or including far more service component with a white table cloth service.) Its enactment coincided with the repeal of the service tax.

3. Gas and electric service taxes were enacted in 1937. (State sales tax always allowed an industrial use exemption, and in 1979 also added a residential use exemption, so that only commercial/retail is left subject to state sales tax.)

4. The steam tax was enacted in 1964 (Steam has also allowed industrial use exemption since enacted in 1964, probably relatively little revenue derived from the Residential or commercial use of purchased steam from 1964 to 1979, and probably none now.)

5. Telephone and telegraph services taxes were enacted 1937. (While generating little revenue today, this provides any basis necessary to support taxation of telecommunication data-only lines or modern digital service.)

Extending the sales tax to services has been relatively successful in generating additional revenue. Particularly the telephone, gas and electric services which were franchised monopolies and relatively easy to obtain near complete tax compliance. Adding tax on commercial/retail use of steam in 1964 was probably fairly meaningless, centrally generated steam sold to users had been largely phased out.[40]

[39] Bill Speckman, Audit Group Manager, Colorado Department of Revenue, October 2002.

[40] Bill Speckman, Audit Group Manager, Colorado Department of Revenue, October 2002.

Connecticut

Connecticut enacted the state sales tax in 1947 at a rate of 3%, while the current rate is 6%. During the late 1980's Connecticut did not have an income tax (this was enacted in 1991) and in an attempt to avoid one, the General Assembly extended the sales tax to services. The anticipated revenue was initially realized. Yet over time, special interest groups began influencing the repeal of the services being taxed.[41]

A prime example is the taxation of computer data processing services. In 1989, the sales tax was extended to data processing services at 6%. The tax on computer and data processing services, including Internet access charges, is being phased out through a series of annual rate reductions. Currently, computer and data processing services (with the exception of Internet access charges) are taxed at 1% for services provided between July 1, 2001 until June 30, 2004. The tax will be fully repealed effective for services rendered on or after July 1, 2004.

Another example of the taxes on services slowly being repealed is the tax on renovation and repair services to residential property. This tax was repealed effective July 1, 2001. Yet, the tax on renovation and repair services to existing commercial, industrial and income producing property remains in effect at the rate of 6%.

Various notable services still subject to the Connecticut sales tax are listed below: [42] Refer to Appendix M for a complete list of services subject to the Connecticut sales tax.

1. Lobbying or consulting services for the purpose of representing a client's interests in relation to any governmental body.

2. Advertising, public relations services not related to the development of media advertising or cooperative direct mail advertising.

3. Business analysis, management, management consulting and public relations services.

4. Renovation and repair services to existing commercial, industrial and income producing property

5. Private investigation, protection, patrol work, watchman and armored car services, exclusive of

[41] State of Connecticut, Department of Revenue Services, October 2002.

[42] 2002 Conn. Pub. Acts 1, 65, 67 (May 9 Spec. Sess.); Conn. Agencies Regs. §12-407(2)

these services provided by off-duty police officers and fire fighters.

Nebraska

The Nebraska sales tax is collected on the gross receipts from retail sales in Nebraska. The tax is imposed on the transaction classified as a "sale," not the item sold. A retail sale being defined as the sale of goods or taxable services for consideration to the end user when the sale occurs. The Nebraska state sales and use tax rate is 5.5%. (The rate increase from 5% to 5.5% was effective October 1, 2002). In addition, local sales and use taxes can be set at 0.5%, 1%, or 1.5%.[43]

Services that are currently taxed in Nebraska are as follows:

1. Charges for services by a consultant that result in a transfer of software, whether canned or custom, are subject to tax. This includes:
   a. Programming
   b. Program development
   c. Systems analysis
   d. Software customization and modification and upgrading of programs.

2. Installation or furnishing of satellite programming and cable television

3. The Nebraska Legislature passed LB 947 during its regular 2002 legislative session to bring Nebraska into compliance with the federal Mobile Telecommunications Sourcing Act, P.L. 106-252. The new law provides for the taxation of "mobile telecommunications service" and further specifies that sales of such service is subject to tax at the customer's place of primary use. The tax on mobile telecommunication services, began August 1, 2002.[44]

4. The Nebraska Legislature passed LB 1085 in 2002. The provisions of this bill impose sales and use tax on nine new services beginning October 1, 2002. The new services are:[45]
   a. Building cleaning and maintenance services

[43] Nebraska Department of Revenue, *Nebraska and Local Sales Tax*, August 2002. Available at www.revenue.state.ne.us.

[44] Nebraska Department of Revenue, *Sales and Use Tax Revenue Rulings, Revenue Ruling 1-02-02: Sales and Use Tax - Mobile Telecommunications Service,* July 2002. Available at *http://www.revenue.state.ne.us/legal/slstax.htm*.

[45] Nebraska Department of Revenue, *Sales and Use Tax Revenue Rulings, Revenue Ruling 1-02-09: Sales and Use Tax - Gross Receipts Defined,* September 2002. Available at http://www.revenue.state.ne.us/legal/slstax.htm.

b. Pest control services
c. Security services
d. Motor vehicle washing and waxing
e. Motor vehicle towing
f. Motor vehicle painting
g. Computer software training. Separately stated charges for telephone support services are not taxable.
h. Installation and application labor; and
i. Labor associated with the sale of property by certain types of contractors

The most common services taxed in other states are shown in the table below[46]

Selective Services Taxed	State
Debt Collection	AK, OH, SD
Credit Information	AK, OH, SD
Janitorial	AK, OH, SD
Telephone Answering	AK, OH, SD
Health Clubs	AK, OH, SD
Exterminating Services	OH
Utilities: interstate telephone services	20 States
Personal Services: barber shops and tax return preparation	6 states
Business Services: Advertising services, maintenance & janitorial services	18 States
Professional Services: lawyers, accountants, engineers, doctors, medical related professions	HI, ND, SD
Professional Services: Land Surveyor	SD, TX, WV
Swimming Pool	AK, OH, SD
Limo services with driver	14 states
Aircraft rentals with pilot .i.e chartered flights	10 States

[46]Tax Administration News, Vol. 60, No 12, December 1996.

Options

According to participants (current and former state tax officials and tax consultants) at the Multistate Tax Commission's 12th Annual Business-Government Dialogue on State Tax Uniformity, October 2002, "Political considerations are what keep more states from taxing services more heavily. Despite 'real good efforts,' the fight to expand the sales tax base is lost as legislators chip away at the list of services to be taxed."

Some services are harder to tax than others. "One of the most difficult services to tax is advertising. It's the kind of tax proposal that can halt any attempts at reform. Businesses fight it on principle as an inter-business service. Businesses consider advertising [like] raw material. It's an input in the process of producing and selling a product."[47]

"In working to expand the tax base, the calculation needs to be made that the amount of revenue that will be generated is worth the political capital you're going to spend," said one tax consultant. "Revenue neutral is not politically neutral. The screams of the losers are far louder than the huzzahs of the winners."[48]

In Texas, a potential $15 billion could be realized in the 2004-05 biennium by broadening the sales tax base to include items and services not currently taxed while repealing various exemptions. Refer to Appendix R for a complete list of potential changes to the Current Tax Code and associated revenue.

The intent of this section is to list possible options and in no way represents an endorsement of any of the specific methods by the Senate Finance Committee or its individual members.

State Legislators are faced with various options**:**

1. Examine and re-evaluate the sales tax base.
2. Extend the sales tax base to include selected items not currently taxed.
3. Extend the sales tax base to include selected services not currently taxed.
4. Examine and re-evaluate specific sales tax exemptions the sales current sales tax exemptions, exclusions, special rate, deductions and discounts.

[47] Multistate Tax Commission's 12th Business-Government Dialogue On State Tax Uniformity said that states should tax services, Tax Analysts Electronic Citation: 2002 STT 202-2.

[48] Multistate Tax Commission's 12th Business-Government Dialogue On State Tax Uniformity said that states should tax services, Tax Analysts Electronic Citation: 2002 STT 202-2.

Sales Tax Holiday

Overview

Texas Legislature created a 3-day sales tax holiday in 1999.[49] The amount of sales taxes estimated to be saved due to the exemptions are shown below for fiscal years 1999 through 2006.[50]

State and Local Sales Tax Holiday Impact

State and Local Sales Tax Holiday Impact			
Fiscal Year	**State**	**Local**	**Total**
1999	$ 25,600,000	$ 7,000,000	$ 32,600,000
2000	$ 29,200,000	$ 7,800,000	$ 37,000,000
2001	$ 30,500,000	$ 8,100,000	$ 38,600,000
2002	$ 33,200,000	$ 8,800,000	$ 42,200,000
2003	$ 35,300,000	$ 9,500,000	$ 44,800,000
2004	$ 37,600,000	$10,200,000	$ 47,800,000
2005	$ 40,200,000	$10,900,000	$ 51,100,000
2006	$ 43,200,000	$11,700,000	$ 54,900,000

Estimates for fiscal years 1999-2001 are the result of post-holiday analysis. Currently, Texas is one of nine states to implement a state sales tax holiday. The differences among the various states' sales tax holidays are the length of the holiday, the type of items exempted, and the maximum cost of items exempt from the sales tax. The table on the following page outlines these differences.

[49] Texas Tax Code, Sec 151.326

[50] Texas Comptroller of Public Accounts, 9/18/02

How Does the Texas Sales Tax Holidays Compare to that of Other States?[51]

States' Sales Tax Holiday					
State	**Days**	**Items Included**	**Max. Cost of item Available for Exemption**	**1st Year**	**2002 dates**
NY	9	tangible personal property, calling card services, food, drink and rentals purchased in a liberty or resurgence zone	$500	2002 (for this type)	June 9-11; July 9-11; August 20-22
TX	3	clothing and footwear	$100	1999	August 2-4
CT	7	clothing and footwear	$300	2000	August 18-24
SC	3	clothing, computers, supplies	N/A	2000	August 2-4
PA	7	computers	N/A	2000	Feb. 17-24
IA	2	clothing and footwear	$100	2000	August 2-3
WV	3	clothing, school supplies, computers	$100	2002	August 2-4
NC	3	clothing, school supplies, computers	cl,ss - $100 cp - $3500	N/A	August 2-4
GA	4	Clothing, school supplies, computers	cl - $100, ss-$20, cp$1,500	2002	March 29-30, August 2-3

Citing budget shortfalls, the Florida legislature did not renew the sales tax holiday for 2002. Maryland is the only other state to have had a sales tax holiday (in 2000 and 2001) and not renew it for 2002. New York had a more "typical" sales tax holiday beginning in 1997, but the clothing exemptions were made permanent in 2000.

Not every state has embraced the program. Most recently legislatures in Kansas, Michigan, Ohio, Oklahoma and Virginia rejected the idea because of the considerable expense and administrative burdens involved. Another criticism is that in some geographic areas, a holiday would not lure shoppers from other states and thus would not actually increase sales for state merchants.[52]

[51] Federation of Tax Administrators, *Sales Tax Holidays Summarized*, June 2002. Available at http://www.taxadmin.org/fta/rate/sales_holiday.html.

[52] *Ibid*

Internet Sales Tax and the Streamlined State Sales Tax

Overview

Another reason the sales tax base for state and local government is shrinking is due to the growth of remote sales including those made through e-commerce, the telephone and catalogs. The gross sales tax that is typically imposed on retail sales of tangible personal property (unless specifically exempted) and services (if specifically enumerated), is not being collected on items sold through the Internet.

State sales tax loss estimates include both Business to Consumer (B2C) and Business to Business (B2B) sales, which together will make up more than 90 percent of the total e-commerce activity.

A recent study measuring all of the states' revenue losses from untaxed Internet transactions put the overall sales tax losses from Internet sales at $13.3 billion in 2001 and forecast a tripling of that loss to $45.2 billion in 2006.[53] By 2003 all states could lose more than $23 billion in uncollected sales tax on e-commerce purchases. California would take the biggest hit at $3.47 billion, while Florida would lose $1.76 billion. New York and Texas would each suffer about $1.9 billion in combined revenue lost.[54]

Texas State Comptroller's Projected Loss

The following table illustrates the amount in sales taxes not collected, in connection with "remote" sales. Remote refers to a seller with no physical presence in Texas and making sales into the state. Purchases made using catalogs and/or the Internet may be discussed together as remote sales due to the fact that the issue of sales tax being collected is conceptually the same in both cases.

[53] Donald Bruce & William F. Fox, *State and Local Tax Revenue Lossless from E-Commerce: Update Estimates*, 2001.

[54] Jennifer Jones, Infoworld, *Internet Sales Tax Unlikely to Hit Stride This Year*, February 2001.

Estimated Sales Tax not Collected by Remote Sellers[55]

Sales Tax Not Collected by Remote Sellers			
Fiscal Year	State Sales Tax Not Collected, Catalog Sales	State Sales Tax Not Collected, Internet Sales	Total, State Sales Tax Not Collected on Remote Sales
2001	$200 million	$150 million	$350 million
2002	$200 million	$150 million	$370 million
2003	$200 million	$192 million	$392 million

Inevitable Decisions to be made by States

The lack of required Internet sales tax collection will force states to make tough decisions in the future. In states that do not levy a personal income tax, such as Texas, the revenue loss is serious. The potential revenue loss for Texas by 2011, according to one study, will hit almost 10% of total expected tax collections. If Texas were to raise current sales tax rates to make up for the revenue loss, the rate would have to increase from 6.25% to 7.86%.[56]

To turn the sales tax situation around, states are working on the core of the argument behind the 1992 ruling in *Quill Corp v. North Dakota.* This case is one of the main reasons behind the U.S. Congress' refusal to mandate collection of the tax by remote-site retailers: the sales tax is overly complex and complicated, with hundreds of exemptions, special rules and differing definitions that vary from state to state and among localities within those states. Collecting the tax, the courts have ruled and Congressional leaders confirmed, was an overwhelming burden on out-of-state retailers.[57]

In practice, it is sometimes difficult to tell whether certain products (e.g., customized computer software) should be treated as tangible or intangible property. Sales tax issues relating to e-commerce activities are conceptually very similar to the jurisdictional and product classification issues that out-of-state catalog retailers and computer software vendors have been addressing for years.

[55] Texas Comptroller of Public Accounts, 9/18/02.

[56] Governing Magazine, *The Untaxables*, July 2002.

[57] Governing Magazine, *The Untaxables*, July 2002.

Accelerating e-commerce activities have put more pressure on the system and have led to efforts to simplify and rationalize the existing rules. These efforts began with the Internet Tax Freedom Act and culminated in the Streamlined Sales Tax Project.

The Internet Tax Freedom Act ("ITFA")

In the mid to late nineties, public acceptance and use of the Internet grew. Subsequently, dual state and local taxation of Internet access was one of the early justifications given for enactment of the Internet Tax Freedom Act (ITFA). Due to the fact that underlying telephone service is already taxed, several groups argued that Internet access delivered via telephone should be granted an exemption from sales tax. In addition, administering an Internet access tax proved too difficult for state and local governments. Finally, state and local taxing authorities had strained the application of preexisting sales tax statutes to apply them to Internet access. As of October 1, 1998, the ITFA placed a three-year moratorium on multiple taxes, discriminatory taxes and taxes on Internet access. In November 2001, President Bush signed a two-year extension of the ITFA moratorium, through November 1, 2003.[58]

The Streamlined Sales Tax Project ("SSTP")

The streamlining state sales tax project began as an effort to simplify the complexities in collecting interstate sales tax so they can be applied more easily to all purchasers, whether made in a store, through a catalog or on the Internet. Members of the streamlining effort include state legislators, tax administrators, governors' staff and private-sector retailers from nearly 40 states, including Texas.

The overall goal of this effort is to influence congress to require remote-site sales-tax collection by making it easier and less expensive for retailers to collect the tax. The hope is that if enough big states enact the compact, others will follow.

The monumental challenge the states face is to develop a Streamlined Sales Tax system that includes the following key features:

1. Uniform definitions within tax laws
2. Rate simplification
3. State tax administration of all state and local taxes
4. Uniform sourcing rules
5. Simplified exemption administration for use, and entity, based exemptions
6. Uniform audit procedures
7. State funding of the system

Deloitte & Touche Center for Multistate Taxation, University of Wisconsin, *A Lawmaker's Guide to the Streamlined Sales Tax Project*, 2002.

So far, thirty-nine states including Texas and the District of Columbia are involved in the project. Thirty-four states and the District of Columbia are voting participants in the project because their legislators have enacted enabling legislation or their governors have issued executive orders or similar authorizations. Five states are non-voting participants in commitment of the state executive or legislative branches, but are still participating. Forty-five states and the District of Columbia impose a sales and use tax.[59]

Texas' Role

The implementing states' organization has developed a model act, allowing state legislators the opportunity to enact the model act before the end of 2003. Those states that enact the provisions of the agreement in 2002 and 2003 will be the governing states of the Streamlined Sales Tax System.

Today, Texas is approximately 90% in compliance with the model act. To be in total compliance with the model act, Texas will have to enact legislation to:

1. Comply with streamlined project's uniform tax base requirements.

2. Change the Texas sourcing rule for local governments only, from origination to destination.

3. Change the Texas Communications Industry sourcing rule.

In order to continue to be at the front of this process the Texas Legislature will be faced with making the required changes during the 78th session. However, there is a grace period which lasts until Dec 2005. Currently only MN, NC, SD and Wyoming have made the legislative changes.

[59]Deloitte & Touche Center for Multistate Taxation, University of Wisconsin, *A Lawmaker's Guide to the Streamlined Sales Tax Project*, 2002.

Motor Vehicle Sales and Use Taxes

Motor Vehicle Tax Facts			
	Sales	**Seller Financed**	**Rental**
Date Enacted	1941	1993	1971
Rate When Enacted	1%	6.25% Gross Receipts	4% Gross Receipts
Current Rate	6.25%	6.25% Gross Receipts	10% Gross Receipts on rental 30 days or less;* 6.25 percent on rentals 31-80 days
Last Changed	1991	None	1991
2001 Net Revenue	$2.6 Billion	$79.2 Million	$176.5 Million
2002 Net Revenue	$2.7 Billion	$73.2 Million	$159.6 Million
State Ranking	4th		
Estimated Average Revenue Per Penny**	$420 Million	$12.7 Million	$17.7 Million

*The per penny rental figure is based upon the 0-30 day rate of 10 percent.

** Each of the 6.25 pennies that make up the current tax rate for the basic Motor Vehicle Sales Tax produced an average of $420 million in revenue in fiscal 2001. It is important to note, however, that as the rate is changed, each additional penny produces less revenue than the preceding penny generates.

Overview

The motor vehicle taxes consist of the motor vehicle sales and use tax, the motor vehicle sales and use tax on seller financed-motor vehicles, the motor vehicle rental tax and the manufactured housing sales and use tax.

Motor Vehicle Sales and Use Tax

This tax is levied on all retail sales of motor vehicles in Texas and motor vehicles purchased inside or outside of the state and will be used on Texas public highways by a Texas resident or an individual domiciled or doing business in this state.

The motor vehicle sales and use tax was enacted in 1941 at 1%. Since 1941, this tax rate has changed nine times. The current motor vehicle tax rate is 6.25% and ranks fourth among the 46 states imposing a motor vehicle tax. Exemptions to this tax are sales to governments, handicapped persons, licensed child care facilities, motor vehicle rental companies, used for religious purposes, farm use or taxed by other law or transported out-of-state. Some fire trucks and ambulance purchases are also exempt. Net collections for FY 2002 totaled $2.7 billion. One hundred percent of the revenue collected is allocated directly to the General Fund.

Motor Vehicle Sales and Use Tax on Seller Financed Motor Vehicles

This tax is imposed on a motor vehicle seller who holds a dealer license from the Texas Department of Transportation and finances the vehicles it sells and collects the motor vehicle sales tax on these vehicles as payments are collected. All revenue from this tax is allocated to the GR Fund. Exemptions to this tax are the same as those for the motor vehicle sales and use tax.

The Motor Vehicle Rental Tax

A gross rental receipts tax is imposed on motor vehicle rentals. The percent of tax imposed is based on the length of the rental contract. The motor vehicle rental tax was enacted in 1971 at 4% of gross receipts. Since 1971, the tax rate and base have changed three times. Today the tax has a two-tier rate structure:

1. 10 % for rental of 30 days or less (Note: this is the highest among the 45 states that impose this tax).
2. 6.25 % for rentals 31 -180 days

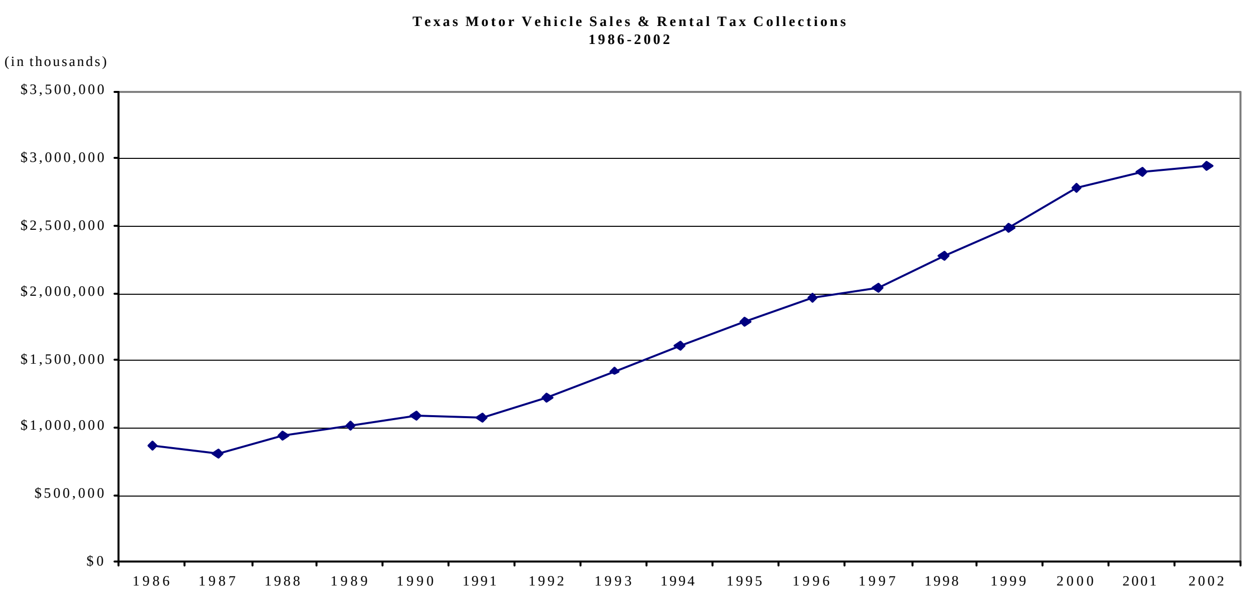
Exemptions to this tax are rentals to governments and rentals for re-rental.

Texas Total Motor Vehicle Tax Collections Over Time (1986-2002)

* Note: Graph includes all motor vehicle taxes, not just rentals

Net collections for the motor vehicle taxes in FY 2002 totaled $2.945 billion. Revenues from this tax are allocated to the General Fund.

The Manufactured Housing Sales and Use Tax



* Each of the 5 pennies that make up the current tax rate produced an average of $4 million in revenue in fiscal 2001.

Manufactured Housing Tax Facts	
Date Enacted	1982
Rate When Enacted	6.5% of 65% of Manufacturer's Selling Price from 3/82 to 3/83 and 5% of 65% of Manufacturer's Selling Price beginning 9/83
Current Rate	5% of 65% Manufacturer's Selling Price
Last Changed	none
2001 Net Revenue	$21.9 Million
2002 Net Revenue	$19 Million
Average Revenue per Penny Increase*	$4.37 Million
FY 2004-05 revenue generated from an increase to 6.25% of 65% Manu selling price	$108 Million

It is important to note, however, that as the rate is changed, each additional penny produces less revenue than the preceding penny generates.

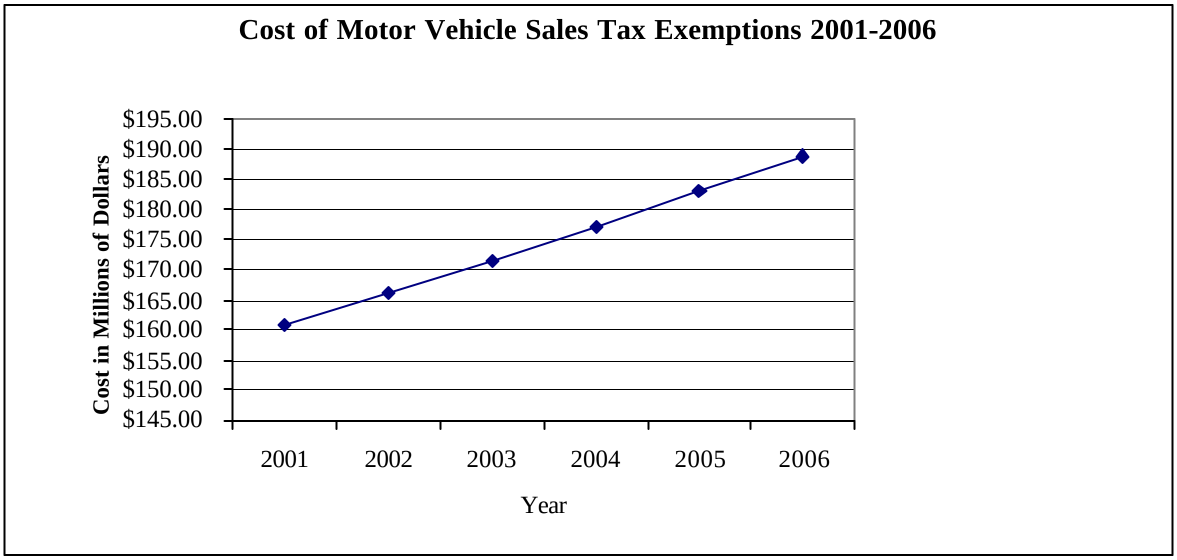
Overview

A sales tax is imposed on manufacturers of industrialized housing and manufactured homes for sale in Texas. A use tax is imposed on manufactured homes purchased new outside Texas and brought into Texas for use within 1 year of purchase date. The tax is due from the person to whom or for whom a new manufactured home is sold, shipped or consigned.

In 2002, net collections totaled $19 million. Revenue collected from this tax is allocated to the General Revenue Fund. Exemptions to this tax are sales to governments and certain non-profit entities.

Cost of Motor Vehicle Sales Tax Exemptions

In 2001, motor vehicle sales tax exemptions cost the State of Texas $160.9 million. This cost is estimated to grow to $189 million by 2006. Refer to Appendix I for a detailed list of the Cost of Motor Vehicle Sales Tax Exemptions for Fiscal 2001-2006 and the associated cost.



The five highest motor vehicle sales tax exemptions are listed below:

1. Vehicles taxed by other laws - $95.6 million
2. Sales to or use by a public agency - $28.5 million
3. Farm use - $21.9 million
4. Certain licensed child care facilities - $7.7 million
5. Driven by handicapped persons - $5 million

Motor Fuels Taxes

Motor Fuels Tax Facts			
	Gasoline	Diesel Fuel	Liquefied Gas
Date Enacted	1923	1941	1941
Rate When Enacted	$0.01/gallon	$0.08/gallon	$0.04/gallon
Current Rate	$0.20 / gallon	$0.20 / gallon	$0.15 / gallon
Last Changed	1991	1991	1989
2001 Net Revenues		$611 Million	$1.8 Million
2002 Net Revenues	$2.2 Billion	$607 Million	$1.8 Million
Estimated Average Revenue Per Penny Increase*	$107.6 Million	$30.6 Million	$124 Thousand
2004-05 revenue generated from an increase to $0.30/ gallon	$2.7 Billion		$2.5 Million

* Each of the 20 pennies that make up the current tax rate produced an average of $138 million--for all three taxes--in revenue in fiscal 2001. It is important to note, however, that as the rate is changed, each additional penny produces less revenue than the preceding penny generates.

Overview

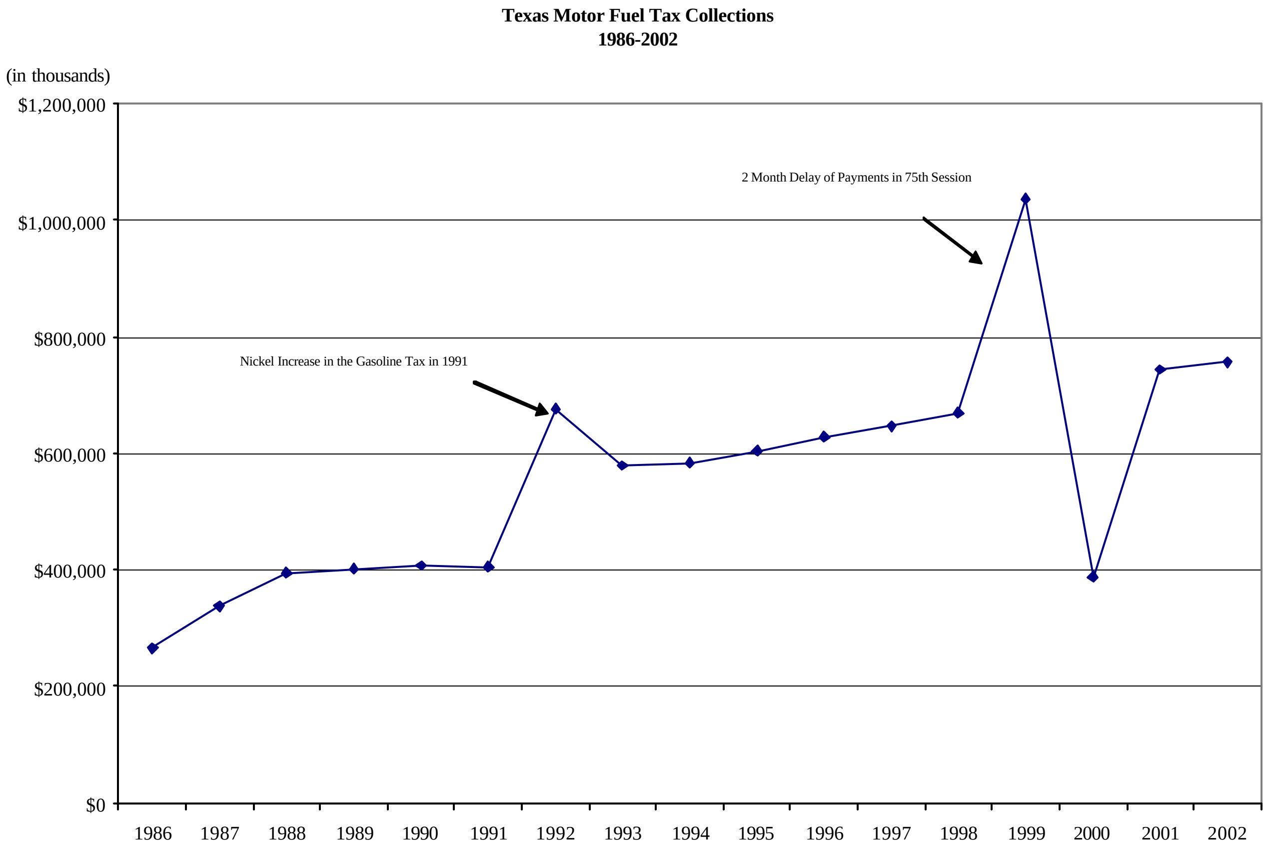
The motor fuels tax consists of the state's consumption taxes on gasoline, diesel fuel, and liquified gas. In 2002, the motor vehicle fuel tax revenue reached $2.8 billion.

After deductions for unclaimed motorboat fuel refunds, other unclaimed refunds, and enforcement, the motor fuels tax is allocated as follows:[60]

1. Available School Fund- 25% of the balance
2. State Highway Fund- 75% of the balance. In the case of gasoline tax revenue, the first $7.3 million of the money given to the State Highway Fund is transferred to the County and Road District Highway Fund.

[60]Texas Constitution, Article 8, Section 7-A.

Texas Motor Fuel Tax Collections Over Time (1986-2002)



Motor Fuels Tax Exemptions

Agricultural, industrial, commercial, marine, railway engine, scheduled inter city bus routes, and various off-road uses are exempt from the motor fuels tax.

A. Gasoline Tax

This tax was enacted in 1923 at $0.01 per gallon and is imposed on the first sale or use of gasoline in Texas. Since its enactment, the gasoline tax rate and base has changed six times. The current gasoline tax is $0.20 per gallon. The gasoline tax is the third largest source of tax revenue for Texas state government, bringing in just over 8.4 cents of every state tax dollar in fiscal 2000.[61] In general, the tax is charged on each gallon of gasoline sold in Texas which is used to propel vehicles on Texas' public roads.[62]

Gasoline Tax Exemptions

1. **Reduced tax rates:** The tax rate is reduced for gasoline sold to qualified transit companies. This applies to most metropolitan transit authorities for transit carriers designed for 12 or more passengers. The tax rate is reduced for gasoline sold to qualified transit companies. This applies to most metropolitan transit authorities for transit carriers designed for 12 or more passengers.

2. **Exceptions:** Exceptions are uses or sales of gasoline where the tax does not apply because the fuel is not used to propel a vehicle on Texas' public roads or because the sale is made to an excepted purchaser. Excepted purchasers include permitted gasoline distributors that buy gasoline to resell or export out of the state, the federal government, and Texas public school districts.

3. **Discounts:** Discounts are handling fees that those who have permits are allowed to keep in exchange for collecting the gasoline tax and sending it to the state treasury.

[61] Texas Comptroller of Public Accounts, *Sources of Revenue Growth*, 2001.

[62] Texas Comptroller of Public Accounts*: Tax Exemptions and Tax incidences, A Report to the Governor and 77th Legislature*, 2001. Available at http://www.cpa.state.tx.us/taxinfo/incidence/gaso.html

Cost of Gasoline Tax Reduced Rates, Exceptions, Discounts, and Refunds.[63]

Cost of Gasoline Tax Reduced Rates, Exceptions, Discounts, and Refunds Fiscal 2001 to 2006 (in millions of dollars)							
Section Texas Tax Code	**Item**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**
153.102	Tax rates (transit)	negligible	negligible	negligibl e	negligible	negligible	negligible
153.104	Exceptions and refunds						
153.119	Federal	$27.70	$28.40	$29.20	$29.90	$30.70	$31.50
	Schools and commercial school transportation companies	0.1	0.1	0.1	0.1	0.1	0.1
	Fuel sold by a permit holder to another permit holder	cbe	cbe	cbe	cbe	cbe	cbe
	Fuel for export	cbe	cbe	cbe	cbe	cbe	cbe
	Aviation use	5.9	6.1	6.2	6.4	6.5	6.7
	Fuel arriving in the tank of a motor vehicle (non-interstate trucker)	cbe	cbe	cbe	cbe	cbe	cbe
	Fuel lost by fire, theft or accident	3.2	3.3	3.3	3.4	3.5	3.6
	Marine use	11	11.3	11.6	11.9	12.2	12.5
	Agricultural use	12.7	13	13.4	13.7	14.1	14.5
	Construction use	3.9	4	4.1	4.2	4.3	4.4
	Industry and commercial use	11.2	11.5	11.8	12.1	12.4	12.7
153.105	Discount for tax collection	43.4	44.5	45.7	46.9	48.1	49.4
153.1195	Credits for bad debts	4.9	5.1	5.2	5.3	5.5	5.6
Totals		**$124.00**	**$127.30**	**$130.60**	**$133.90**	**$137.40**	**$141.00**
cbe: cannot be estimated. Note: Totals may not add due to rounding.							

[63] Texas Comptroller of Public Accounts: *Tax Exemptions and Tax incidences, A Report to the Governor and 77th Legislature*, 2001. Available at http://www.cpa.state.tx.us/taxinfo/incidence/table31.htm

B. Diesel Fuel Tax

The diesel fuel tax was enacted in 1941 at $0.08 per gallon and is imposed on the first sale or use of diesel fuel in Texas. Since its enactment in 1941, the diesel fuel tax rate and base has changed seven times. Currently the tax is levied at 20¢ per gallon (19 ½¢ - transit sales) on first sale or use. Exemptions to this tax are agricultural, industrial and commercial, marine railway engine, scheduled inter-city bus routes, public school districts, and various off road-uses.[64] Deductions are given to suppliers at 2%; bonded users at ½% (.005); and interstate truckers at ½% (.005). [65]

C. Liquified Gas Tax

A tax is imposed on the use of liquified gas (i.e. butane, propane, compressed natural gas) as a motor fuel. Motor vehicles licensed in Texas and equipped with a liquefied gas system are required to prepay the tax by purchasing a liquified gas tax decal. Motor vehicles licensed in other states, Mexico, or licensed under the IFTA pay the tax at the retail pump.

The liquified gas tax was enacted in 1941 at $0.04 per gallon. Since its enactment, the liquified gas tax rate and base has changed five times. The current liquified gas tax is levied at 15¢ per gallon.

Exemptions to this tax include agricultural, industrial and commercial uses, plus public school districts, and Texas counties, and various off-road uses.[66] Deductions are given to dealers at 1% and interstate truckers at ½% (.005). [67]

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[64] Texas Comptroller of Public Accounts, *Source of Revenue Growth 1972-2001*, p. 63.

[65] Texas Comptroller of Public Accounts, *Sources of Revenue Growth*, 2001. Available at http://www.cpa.state.tx.us/taxinfo/fuels/diesel.html

[66] Texas Comptroller of Public Accounts, *Source of Revenue Growth 1972-2001*, p. 76.

[67] Texas Comptroller of Public Accounts, *Tax Exemptions and Tax Incidence*, January 2001. Available at http://www.cpa.state.tx.us/taxinfo/fuels/lg.html.

Franchise Tax

Franchise Tax Facts	
Date Enacted	1907
Rate When Enacted	$0.50 per $1,000 of taxable capital
Current Rate	0.25% on taxable capital, plus the amount, if any, by which a tax of 4.5% on earned surplus exceeds the tax on capital
Last Changed	1991
2001 Net Revenue	$1.9 Billion
2002 Net Revenue	$1.9 Billion
Estimated Average Revenue Per Penny Increase*	$435.6 Million

*Arithmetically, per penny of earned surplus, or per .06 cents of capital, whichever is higher. Per penny calculation based on 4.5% earned surplus rate. Each of the 4.5 pennies that make up the current tax rate produced an average of $436 million in revenue in fiscal 2001. It is important to note, however, that as the rate is changed, each additional penny produces less revenue than the preceding penny generates.

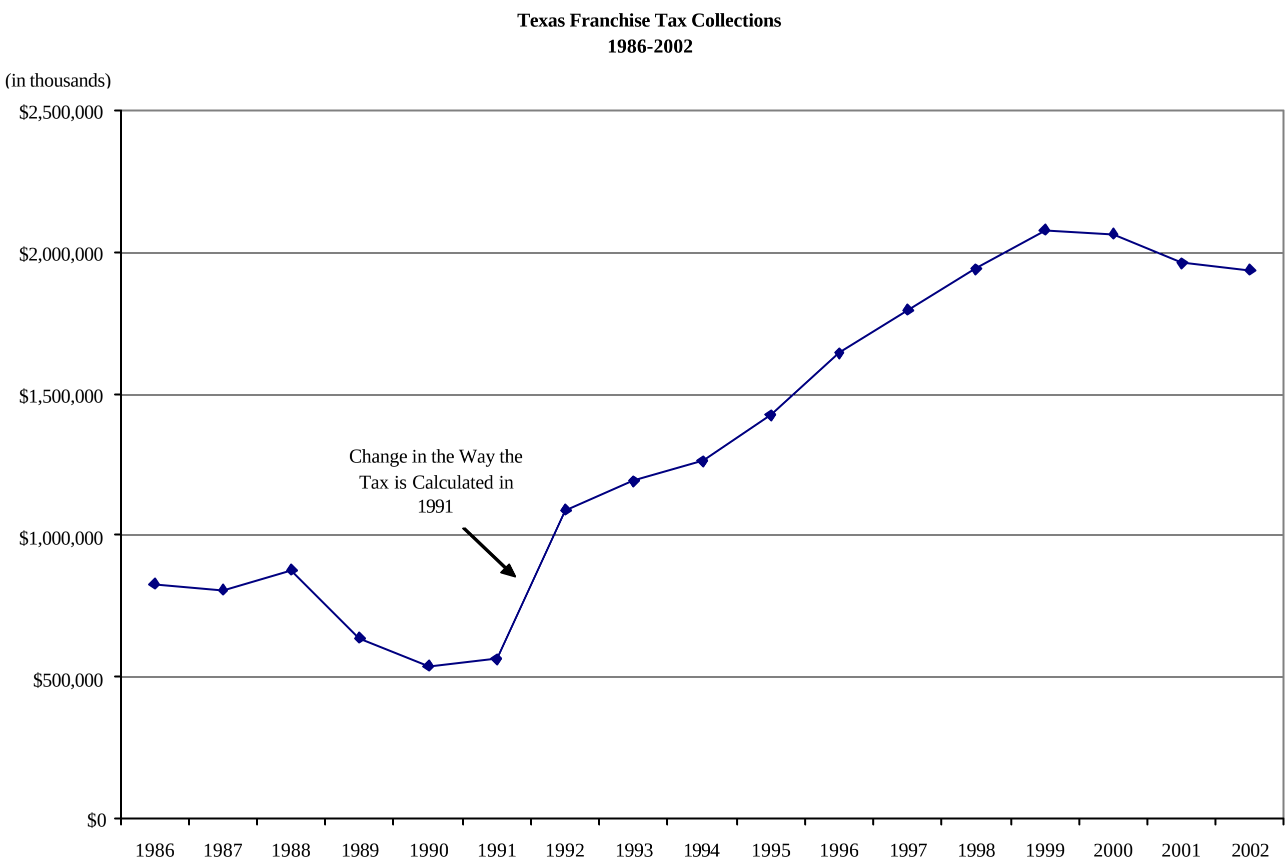
Overview

The Texas franchise tax was adopted in 1907. Originally the tax was levied as a tax on corporate wealth (i.e., as a percentage of corporate assets), the tax changed little but for the tax rate until the 1980s.

Legal challenges to the method of tax computation in the 1980s caused tax revenues to drop sharply.[68] From 1987 until 1991, the franchise tax rate was $5.25 basic rate plus $1.45 surtax-$150 minimum tax effective for 1989 reports; the rate then reverted to $5.25 with no surtax- $68 minimum tax for reports due in 1990.

[68] Texas Comptroller of Public Accounts: *Tax Exemptions and Tax Incidences, A Report to the Governor and 77th Legislature*, 2001. Available at http://www.cpa.state.tx.us/taxinfo/incidence/fran.html

Texas Franchise Tax Collections Over Time (1986-2002)



The franchise tax is Texas' primary business tax and is levied on corporations. The definition of a "corporation" includes regular corporations, S corporations, banks, savings and loan associations, and limited liability companies ("LLC").[69]

The franchise tax is a privilege tax, meaning corporations pay the tax in exchange for specific privileges granted by the state of Texas. Privileges include:

1. Access to the state's legal system
2. The right to accumulate property separate and apart from an individual's property, and
3. Limitation of personal financial liability for officers of the corporation.

[69] Texas Tax Code 171.001 (Vernon 1992)

In answer to the ensuing revenue shortfalls and to long-standing equity concerns, the Legislature reformulated the tax in 1991. Since 1992 the franchise tax has been computed on a dual tax base of capital (net worth) and earned surplus (modified net income). [70] The current franchise tax is .25 % on taxable capital, plus the amount if any, by which a tax of 4.5 percent on earned surplus exceeds that tax on capital.

Corporations Subject to the Franchise Tax

The Texas franchise tax is imposed on corporations and limited liability companies that are either:

1. Actually doing business in the state of Texas: A corporation does business in the state of Texas when its activity of business in Texas reaches certain minimum levels, or

2. Authorized to do business within the state: A corporation is authorized to do business in the state of Texas when it is incorporated here or when it has obtained a certificate of authority to conduct business here.[71]

Franchise Tax Exemptions

The franchise tax is not imposed on certain tax-exempt corporations.[72]
Exempt entities include:
1. Non-corporate business entities such as partnerships, associations, and proprietorships
2. Professional Associations. This exclusion arises from Comptroller Policy.[73]
3. Insurance companies[74]
4. Railway terminal corporations[75]

[70]Texas Tax Code 171.001 (Vernon 1992)

[71]Texas Tax Code 171.001 (Vernon 1992)

[72]Texas Tax Code 171.051 to .086 (Vernon 1992)

[73]Texas Franchise Tax 2002, James F. Martens, 2002, p. 2

[74]Texas Tax Code Ann. 171.052 (Vernon Supp.1995)

[75]Texas Tax Code Sec. 171.053 (Vernon 1992)

5. Open-end investment companies[76]
6. Certain non-profit corporations[77]
7. Corporations manufacturing, selling, or installing solar energy devices[78]
8. Electric and telephone cooperatives[79]
9. Certain trade show participants[80]
10. Credit unions[81]

Cost of Franchise Tax Exemptions[82]

Cost of Franchise Tax Exemptions Fiscal 2001-2006 (in millions of dollars)	
Year	**Estimated Cost**
2001	$ 637.30
2002	$ 662.20
2003	$ 690.10
2004	$ 721.10
2005	$ 755.90
2006	$ 792.30

There are numerous exemptions from the franchise tax. The Comptroller of Public Accounts estimates the

[76] Texas Tax Code Ann. 171.055 (Vernon 1992)

[77] Texas Tax Code Sec. 171.053 to 171.068 (Vernon 1992)

[78] Texas Tax Code Sec. 171.056 (Vernon 1992)

[79] Texas Tax Code Sections 171.079-80 (Vernon 1992)

[80] Texas Tax Code Sec. 171.084(Vernon 1992)

[81] Texas Tax Code Sec. 171.077 (Vernon 1992)

[82] Texas Comptroller of Public Accounts, 2001

cost of exemptions to the state at approximately $637 million per year. In 2001, 149,040 of the half million eligible corporations paid the tax.[83]

Refer to Appendix L for a detailed list of the Cost of Franchise Tax Exemptions for Fiscal 2001-2006.

Repealing Franchise Tax Exemptions[84]

For illustrative purposes only, the table below updates options by the 1997 Joint Committee and shows additional revenue that may be realized by repealing various franchise tax exemptions.

Franchise Tax - For Profit Corporations	Revenue in Millions
Potential Changes to Current Tax Code	**2004-05**
Repeal exemption for open-end investment companies (mutual funds)	$ 506.60
Repeal regulated investment company special apportionment method	$ 7.80
Repeal exemption for title insurance companies	$ 2.90
Repeal exemption for solar energy businesses	$ 1.00
Repeal temporary (FAS 96) credit	$ 0.60
Repeal exemption for trade show participants	negligible
Repeal exemption for sludge recycling firms	negligible
Total Franchise Tax - For Profit Corporations	$ 518.90

[83] San Angelo Standard-Times, *More Big Companies Dodge State Franchise Tax*, 4/28/02.

[84] Comptroller of Public Accounts, 10/2002.

Note: Unless specifically stated, estimates reflect full years; no adjustments for implementation of tax law changes assumed. Estimates reflect static changes only; no dynamic economic effects included**.**

Companies Avoiding Franchise Taxes

Current state law allows limited partnership companies not to pay franchise taxes. Texas corporations are becoming more aggressive with their tax planning by restructuring their companies to limited partnerships and "Delaware Subs" to avoid paying the state's franchise tax. When restructuring to a Delaware Sub, a company becomes a subsidiary of an out-of-state company based in a low-tax state, i.e Delaware, to avoid paying the Texas franchise tax. (Refer to the Delaware Sub section of this report).

Approximately one thousand corporations convert to limited partnerships each year.[85] Most of these conversions are small companies and do not have a significant impact on the state revenue. Yet, it is the few large companies that convert that have a significant impact on state revenue. According to the Texas State Comptroller, the state will lose as much as $143 million in 2003 because of the corporate restructuring.

Franchise tax revenues have grown from $1 billion to $1.9 billion in the past nine years, yet declined by over $100 million from 2000 to 2001. In 2002, the franchise tax generated $1.96 billion in revenue. Due to current franchise tax exemptions, only 149,040 of the half million corporations in Texas paid franchise taxes in 2001. Thus the taxes paid by 1% of Texas corporations constitutes 51% of the states franchise tax revenue. A change in these corporations' structure may drastically decrease franchise tax revenue.[86]

[85] Texas Comptroller of Public Accounts, 2002.

[86] San Angelo Standard-Times, *More Big Companies Dodge State Franchise Tax*, 4/28/02.

Franchise Tax Deductions

For many of the allowable deductions or special accounting methods, taxpayers are not required to alert the Comptroller when employing the deduction or accounting method. For this reason, the absolute number of taxpayers taking advantage of these forms of tax relief is not known. The fiscal impact of these tax benefits are estimated using a variety of computation methods, including comparison with federal tax information, if appropriate.[87] Other deductions or special accounting methods require the entry of data on the franchise tax report in a manner that allows the identification of each taxpayer using that deduction or method. Tax credits can also be identified on a taxpayer-specific basis.

Franchise Tax Deductions include:

1. Small business exceptions: corporations with gross receipts less than $150,000[88]
2. Reduction of taxable capital for investment in an enterprise zone[89]
3. Food and medical receipts[90]
4. Business loss carryover[91]
5. Officer/director compensation add-back exemptions for 35-or-fewer shareholder corporations[92]
6. Cost of solar energy device from taxable capital apportioned to this state[93]
7. Interest income from US obligations[94]

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[87] Texas Comptroller of Public Accounts: *Tax Exemptions and Tax Incidences, A Report to the Governor and 77th Legislature*, 2001. Available at http://www.cpa.state.tx.us/taxinfo/incidence/fran.html

[88] Texas Tax Code Sec. 171.002(d) (Vernon 1992)

[89] Texas Tax Code Sec. 171.1015 (Vernon 1992)

[90] Texas Tax Code Sec. 171.104 (Vernon 1992)

[91] Texas Tax Code Sec. 171.110(a)(4) (Vernon 1992)

[92] Texas Tax Code Sec. 171.110 (Vernon 1992)

[93] Texas Tax Code Sec. 171.107 (Vernon 1992)

[94] Texas Comptroller of Public Accounts: *Tax Exemptions and Tax Incidences, A Report to the Governor and 77th Legislature*, 2001. Available at http://www.cpa.state.tx.us/taxinfo/incidence/fran.html

Cost of Franchise Tax Deductions

Franchise Tax - For Profit Corporations	Revenue in Millions
Potential Changes to Current Tax Code	**2004-05**
Remove deduction for officer/director compensation add-back exemption for 35-or-less-shareholder corporations	$ 454.70
Remove deduction for business loss carryover	$ 416.20
Remove deduction for interest earnings on federal securities	$ 117.60
Remove deduction for firms with tax liability of less than $100	$ 114.90
Remove deduction for food and medicine receipts	$ 8.90
Remove deduction for investment in enterprise zones	$ 7.80
Remove deduction for purchase of solar energy devices	negligible
Total Franchise Tax - For Profit Corporations	**$ 1,120.10**

Cost of Franchise Tax Deductions, Special Accounting Methods, Credits, and Refunds Fiscal 2001-2006 (in millions of dollars)

	2001	2002	2003	2004	2005	2006
Business loss carryover	$ 208.1	$ 208.1	$ 208.1	$ 208.1	$ 208.1	$ 208.1
Officer compensation exclusion small corps	$ 187.8	$ 198.3	$ 207.2	$ 219.7	$ 235.0	$ 251.9
Small business exception	$ 46.4	$ 49.1	$ 52.2	$ 55.5	$ 59.4	$ 63.7
Interest earnings on federal securities	$ 53.7	$ 55.0	$ 56.5	$ 58.0	$ 59.6	$ 61.2
Enterprise zone investment	$ 3.9	$ 3.9	$ 3.9	$ 3.9	$ 3.9	$ 3.9
Food and medicine receipts	$ 3.6	$ 3.8	$ 4.0	$ 4.3	$ 4.6	$ 4.9
Solar energy device purchases	*	*	*	*	*	*
Total deductions	$ 503.5	$ 518.3	$ 531.8	$ 549.5	$ 570.5	$ 593.6

Elimination of Franchise Tax Deductions[95]

For illustrative purposes only, the table below updates options by the 1997 Joint Committee and shows additional revenue that may be realized by eliminating various franchise tax deductions.

[95] Texas Comptroller of Public Accounts, 10/2002.

Note: Unless specifically stated, estimates reflect full years; no adjustments for implementation of tax law changes assumed. Estimates reflect static changes only; no dynamic economic effects included**.**

Franchise Tax Special Accounting Methods

1. Special apportionment method for certain investment management companies[96]
2. Use of federal income tax (FIT) accounting method[97]
3. Transportation company apportionment for taxable capital[98]
4. Telephone company apportionment for taxable capital[99]
5. Telephone company apportionment for earned income[100]

Cost of Franchise Tax Special Accounting Methods

Cost of Franchise Tax Special Accounting Methods Fiscal 2001-2006 (in millions of dollars)						
	2001	**2002**	**2003**	**2004**	**2005**	**2006**
Investment management firm apportionment	$ 3.9	$ 3.9	$ 3.9	$ 3.9	$ 3.9	$ 3.9
GAAP accounting exemption	$ 13.9	$ 14.6	$ 15.3	$ 16.2	$ 17.3	$ 18.6
Transportation firm apportionment	$ 11.1	$ 11.7	$ 12.2	$ 13.0	$ 13.9	$ 14.9
Telephone firm apportionment	$ 8.9	$ 9.4	$ 9.8	$ 10.4	$ 11.1	$ 11.9
Total special accounting methods	$ 37.7	$ 39.6	$ 41.2	$ 43.5	$ 46.2	$ 49.3

[96] Texas Tax Code Sec. 171.106 and(d) (Vernon 1992)

[97] Texas Tax Code Sec. 171.113 (Vernon 1992)

[98] Texas Comptroller of Public Accounts*: Tax Exemptions and Tax incidences, A Report to the Governor and 77th Legislature*, 2001. Available at http://www.cpa.state.tx.us/taxinfo/incidence/fran.html

[99] *Ibid*

[100] *Ibid*

Franchise Tax Credits and Refunds

Franchise tax credits include:

1. Temporary credit for sales tax paid on property used for manufacturing[101]
2. Temporary (FAS96) credit net taxable earned surplus[102]
3. Wages paid to Texas Department of Criminal Justice work program participants[103]
4. Wages paid to children committed the Texas Youth Commission[104]
5. Child care centers or services[105]
6. Research and development[106]
7. Job creation[107]
8. Capital investment[108]
9. Contributions to before and after school care programs[109]

Franchise tax refunds may be obtained for job creation in an enterprise zone The refund is 25% of the firms tax liability, up to $45,000 maximum per firm.[110]

Cost of Franchise Tax Credits and Refunds Fiscal 2001-2006 (in millions of dollars)						
	2001	**2002**	**2003**	**2004**	**2005**	**2006**
Research and development credit	67.7	128.8	137	147.1	157.4	168.7
Investment credit	45.2	56.1	59.6	68.5	73.3	78.5
Job creation credit	22.7	28.1	29.9	34.3	36.7	39.3
Before- and after-school care contributions	4.3	5.2	5.5	5.9	6.3	6.8
Child care credit	3.9	4.7	5	5.3	5.7	6.1
Temporary (FAS 96) credit	0.4	0.4	0.4	0.3	0.3	0.3
Credit for wages paid to inmates of TDC	*	*	*	*	*	*
Credit for wages paid to persons committed to TYC	*	*	*	*	*	*
Refund for job creation in enterprise zones	*	*	*	*	*	*
Total credits and refunds	**$144.20**	**$223.30**	**$237.40**	**$261.50**	**$279.70**	**$299.80**

[101] Texas Tax Code Sec. 171.0021 (Vernon 1992)

[102] Texas Tax Code Sec. 171.111 (Vernon 1992)

[103] Texas Tax Code Sec. 171.651-171.657 Subchapter L (Vernon 1992)

[104] Texas Tax Code Sec. 171.681-171.687 Subchapter M (Vernon 1992)

[105] Texas Tax Code Sec. 171.701-171.707 Subchapter N (Vernon 1992)

[106] Texas Tax Code Sec. 171.721-171.730 Subchapter O (Vernon 1992)

[107] Texas Tax Code Sec. 171.751-171.761 Subchapter P (Vernon 1992)

[108] Texas Tax Code Sec. 171.801-171.811 Subchapter Q (Vernon 1992)

[109] Texas Tax Code Sec. 171.831-171.836 Subchapter R (Vernon 1992)

[110] Texas Tax Code Sec. 171.501 (Vernon 1992)

Revenue Generated from Changes in Special Accounting Methods, etc.[111]

For illustrative purposes only, the table below updates options by the 1997 Joint Committee and shows additional revenue that may be realized by making changes to special accounting methods that are not included in previous charts.

Franchise Tax - For Profit Corporations **Revenue Changes in Special Accounting Methods**	**Revenue in Millions**
Potential Changes to Current Tax Code	**2004-05**
Add non corporate entities with $100,000 owner deduction (excluding sole proprietors) (assumed eff. date: Jan. 1, 2004)	$ 556.7
Eliminate transportation company special apportionment method	$ 26.9
Eliminate telephone company special apportionment method	$ 21.5
Repeal regulated investment company special apportionment method	$ 7.8
Treat receipts from trademarks, licenses and franchises similarly to patents, royalties and copyrights - based on use in Texas	$ 6.0
Total Franchise Tax - For Profit Corporations	**$ 618.9**

Note: Unless specifically stated, estimates reflect full years; no adjustments for implementation of tax law changes assumed. Estimates reflect static changes only; no dynamic economic effects included.

[111] Texas Comptroller of Public Accounts, 10/2002.

Discussion of Franchise Tax "Loopholes"

Over the past few years, there has been much discussion concerning the variety of methods used to avoid paying the Texas Franchise Tax. Texas corporations are becoming more aggressive with their tax planning by taking advantage of income shifting loopholes and/or by restructuring their companies to avoid paying the state's franchise tax. This discussion is more related to corporate restructuring and less to income shifting loopholes which can be taken advantage of regardless of corporate structure.

Currently in Texas, partnerships are not subject to state franchise taxes. Lawmakers acknowledged this exemption under the premise that without an exemption, the franchise tax would be in violation of the state's constitutional prohibition on an income tax.[112]

Once lawmakers extended the franchise tax to corporate income as well as assets, a number of large corporations reorganized as partnerships to avoid the franchise tax. According to the State Comptroller office, it is projected that the state will lose as much as $143 million in 2003 because of corporate restructuring.[113] In 2002, the franchise tax generated $1.9 billion. The discussion of those "loopholes" breaks into two distinct segments: the Delaware Sub and the addition of partnerships in general to the franchise tax.

Effects on Texas Businesses

Texas businesses have reacted to the corporate franchise tax in a variety of ways. Many companies have paid and will continue to pay their franchise taxes, while others have chosen to avoid the tax by reorganizing their organizational structure. This reorganization process is often termed "Delaware Sub" because of the reorganization involves placing a portion of a company's business structure in the State of Delaware, which does not have an income tax or a franchise tax on holding companies. It should be noted that under current law, this change in structure is a legal option.

[112] Fort Worth Star-Telegram Oct. 29, 2000

[113] Texas Comptroller of Public Accounts, 2002.

How the Delaware Sub Works

1. Under the Delaware Sub conversion, many Texas corporations have merged their businesses with a newly formed shell corporation in Delaware.

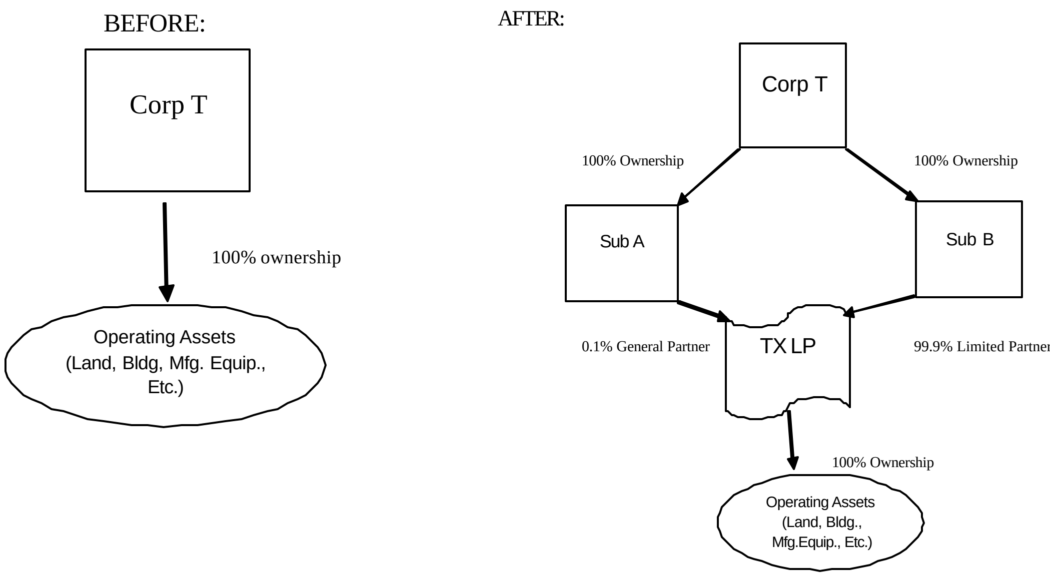
2. The Delaware corporation then creates a limited partnership in Texas.

3. The Delaware corporation then transfers its business to the Texas limited partnership while receiving almost 100% ownership of the partnership. Thus the Delaware corporation acting as the limited partner owns 99.9% of the Texas limited partnership and the Delaware corporation acting as the general partner owns .01% of the Texas limited partnership.

4. Although the Texas corporation's brick and mortar assets never physically leave the state, revenues are technically generated for the Delaware shell company. The Texas limited partnership is not subject to the Texas franchise tax because simply owning an interest in a Texas limited partnership as a limited partner is not equal to be doing business in Texas. Therefore the 99.9% of the Texas limited partnership's income that is allocable to the Delaware corporation acting as a limited partner is not subject to Texas franchise tax. Essentially, revenues are generated for the Delaware company and out of reach of the Texas tax system.[114]

[114] Fort Worth Star-Telegram Oct. 29, 2000.

5. On the other hand, the .01% of the Texas limited partnership's income allocable to Delaware corporations acting as its general partner will be subject to Texas franchise tax.



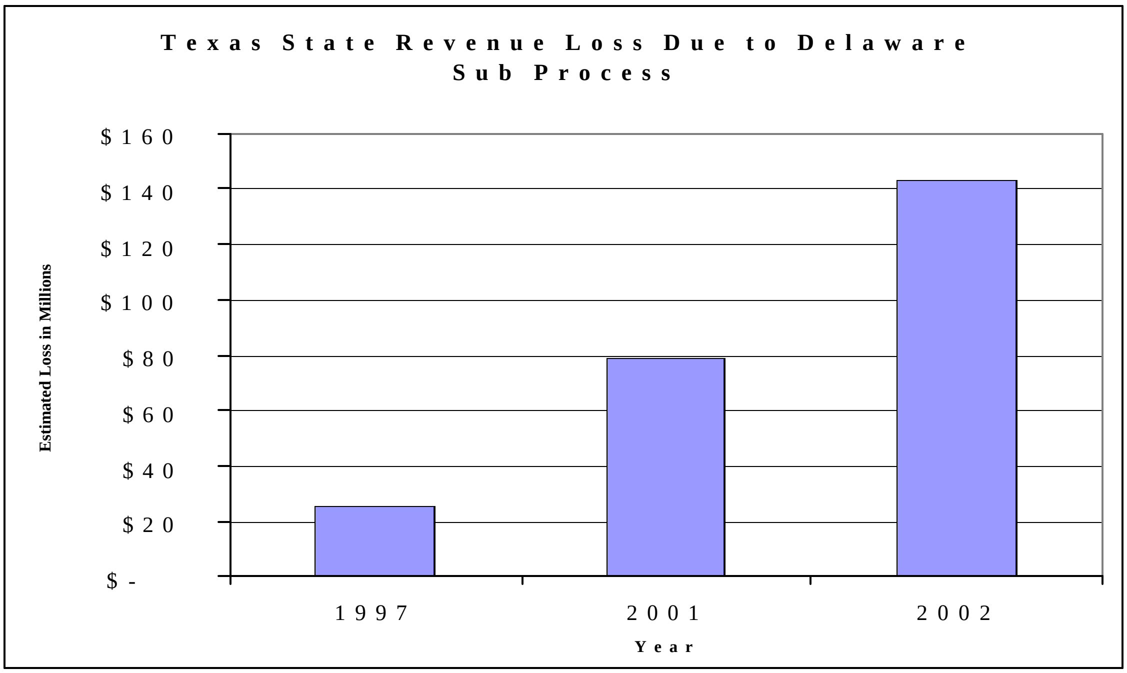
What This Means in Monetary Terms

As shown in the chart below, a company who has a Texas based net income of $20 million can reduce tax liability from $900,000 to only $900.

Example: Franchise Tax Liability		
	Prior to Restructuring to a Delaware Sub	Post Restructuring to a Delaware Sub
Company T Texas source-net income	$20,000,000	.01%*$20,000,000
Income Subject to Franchise Tax	$20,000,000	$200,000
Franchise Tax Rate	4.50%	4.50%
Franchise Tax liability	$900,000	$900

Effect on Texas Government Finance

The companies that reorganize as a Delaware Sub to avoid franchise taxes generally see a tax savings every year. According to the Texas Comptroller of Public Accounts, the state of Texas is estimated to have lost $26 million in 1997 and $79 million in 2001 due to the Delaware Sub process. By the year 2003, the Texas Comptroller estimates the loss to reach $143 million.[115]



[115] Texas Comptroller of Public Accounts, *Texas Taxes Prepared for the 77th Interim Study Senate Finance Committee*, Presented December 5, 2001.

According to the Texas Comptroller's Office, in 1999, 566 Texas companies reorganized as Delaware Subs to avoid the franchise tax. By the year 2000, the number of Texas companies that reorganized had grown to 1,318. Although the Delaware Sub has eliminated franchise taxes for more than 1,000 Texas firms, that number is out of approximately 500,000 companies statewide.[116]

Current Issues

Currently, Texas Legislators are faced with the task of trying to level the playing field for all Texas businesses, regardless of their structure, while continuing to encourage companies to locate in Texas.

Options to Close the Corporate Tax "Loopholes"

Over time, the discussion about the "Corporate Franchise Tax Loopholes" has taken two distinct paths: First the Delaware Sub Loophole, and secondly the general issue of applying the corporate franchise tax to all partnerships. Below is a brief overview of these discussions. The intent of this section is to list possible options and in no way represents an endorsement of any of the specific methods by the Senate Finance Committee or its individual members.

Close the Delaware Sub "loophole":

1. **Agency Rule Change** -
   The "Limited Partner Rule" is sanctioned by the franchise Tax Rules issued by the Comptroller of

[116] Texas Comptroller of Public Accounts, 2002

Public Accounts. 34 TAC Sec. 3.546 provides (in relevant) as follows:

> (a) A foreign corporation is liable for the franchise tax if it is...doing business in the state.
> ...
> (a) Some specific activities which constitute doing business in Texas are: ...
> ...
> (12) foreign corporations as partners:
> ...
> (B) acting as a general partner in a limited partnership which is doing business in Texas. (A foreign corporation which is a limited partner in a limited partnership is not doing business in Texas.)

The Delaware Sub loophole may be closed by reversing the Limited Partner rule. This would require that the Comptroller provide that a corporation is deemed to be "doing business" in Texas if it is a partner, whether general or limited, in a partnership doing business in Texas.

a. Assert Nexus over non residential limited partners. Mandate that ownership of a limited partnership interest in a Limited Partnership doing business in the state creates a nexus for a corporate limited partner which otherwise has nexus.

b. Perform a "Look through" of the various companies or "follow the money," from the mother company through the subsidiaries.

c. Disallow expenses or intangible charges, such as logos, trademarks and officer compensation. In many cases where corporations set up "tax-haven" subsidiaries, the subsidiary charges a royalty to the rest of the business for the trademark, or the patent. The royalty is a deductible expense for the corporation paying it, and reduces the amount of profit such a corporation has in the state in which it does business and is taxable. In some cases, the "profits" are loaned back to the rest of the corporation making the interest on the loan deductible.

2. **Statutory Change** - The Legislature may change the limited partner rule by statute. Section 171 of the Texas Tax Code may be amended by changing a "corporation" to a "taxable entity". The definition of a "taxable entity" could then be changed to include specific types of business formats desired by the legislature.

3. **Consistency Test** - Extend the franchise tax to include any entity that is classified as a corporation for federal income tax purposes. For federal purposes, limited partnerships are taxed

as corporations. This would prevent smaller privately held corporations that avoid taxes by maintaining a corporate structure for federal purposes and assume the form of a limited liability partnership for purposes of avoiding the state franchise tax.

Pennsylvania closed this loophole by amending their corporate net income tax and the capital stock/franchise tax law (HB 334, Act 23 of 2001), so that the term "corporation" now includes any entity that is classified as a corporation for federal income tax purposes. The legislation also expands the definition of "business income" to include all income derived when "either the acquisition or disposition of the property constitutes an integral part of the taxpayer's regular trade or business."[117]

[117] State Tax Notes, Vol.21, No.7, *Measure Closed 'Significant' Corporate Loophole*, August, 2001.

Extend Franchise Tax to Partnerships:

Extending the franchise tax to partnerships may require a constitutional amendment due to the state's constitutional prohibition against an individual income tax. Below are options which show the range or scope of possible changes.

1. **Across the Board Change** - Extend the reach of the franchise tax to include <u>all</u> corporations and partnerships that derive income in Texas. This method was contemplated in Enrolled verison of HB 4 of the 75th Legislative session. Refer to Appendix Q for the language used in HB 4.

2. **Personal Liability Test** - Make the tax applicable to all business structures which afford the owners, shareholders or partners with a shield from personal liability. This would not include general partnerships. However, it would assert nexus over out-of-state general partners.

3. **Occupational Tax Test -** Apply the franchise tax to partnerships in which the partners are not required to pay an occupational tax

Mandatory Combined Reporting

Require corporations to determine their state franchise tax liability using combined reporting. Combined reporting requires corporations to add together the profit of related businesses whether in-state or out-of-state, before the combined profit is subject to apportionment. Thus the corporation gains little or no advantage by shifting the profit between the various corporations/ subsidiaries in the corporate group. Combined reporting is a comprehensive long term solution to the corporate subsidiary problem.

Approximately one-third of the corporate income tax states require corporations to determine their state income tax liability using combined reporting- Alaska, Arizona, California, Colorado, Hawaii, Idaho, Illinois, Kansas, Maine, Minnesota, Nebraska, New Hampshire, North Dakota, Oregon, and Utah.[118] Some of these states, such as California, have required mandatary combined reporting for almost 70 years and have withstood significant legal challenges all the way to the U.S. Supreme Court.

[118] Center on Budget and Policy Priorities, *Closing Three Common Corporate Income Tax Loopholes Could Raise Additional Revenue for Many States,* April 9, 2002.

Natural Gas Tax

Natural Gas Tax Facts	
Date Enacted	1931
Rate When Enacted	2.0% of value
Current Rate	7.5% of the market value at the well head of natural and casing head gas produced and sold in the state
Last Changed	1969
2001 Net Revenue	$1.6 Billion
2002 Net Revenue	$628 Million
Estimated Average Revenue Per Penny Increase*	$212.9 Million

* In FY 2001 Each of the 7.5 pennies that make up the current tax rate produced an average of $213 million. It is important to note, however, that as the rate is changed, each additional penny produces less revenue than the preceding penny generates. Note that FY 2001 collections were unusually high due to high market prices that year; FY 2002 collections were considerably lower.

Overview

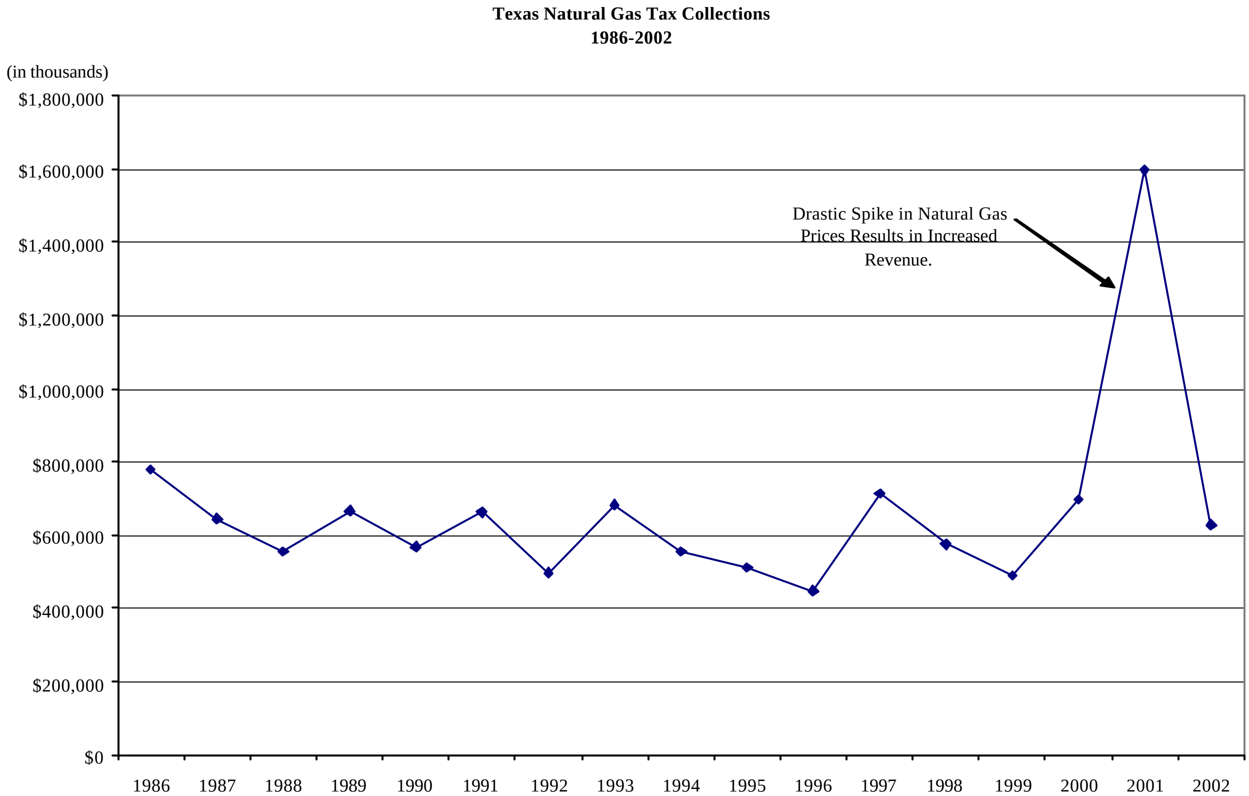
The natural gas tax was enacted in 1931 at 2% of value and is imposed on the market value of gas produced and sold in the state by the producer. Since 1931, the natural gas tax rate has changed seven times. Seven severance tax incentives have passed since 1989. The current tax rates are as follows:

1. Gas is taxed at 7.5% (.075) of natural and casinghead gas produced and saved in the state

2. Condensate is taxed at a crude oil rate of .046% and included in natural gas tax revenues[119]

[119] Texas Comptroller of Public Accounts, *Sources of Revenue Growth 1972-2001*, p. 91.

Texas Natural Gas Tax Collections Over Time (1986-2002)*



* Beginning with fiscal 1985, odd fiscal years have 13 months of revenue and even years have 11 months of revenue.

Revenue generated from the Natural Gas Tax is allocated as follows:

1. Foundation School Fund -25 percent
2. General Revenue Fund -75 percent[120]

In any year that the natural gas tax revenue exceeds $599.8 million, which is the amount from the tax in fiscal year 1987, seventy-five percent of the excess is allocable to the economic stabilization fund. For more detail, see the section on the economic stabilization fund.

[120] *Ibid*

Exemptions to the Natural Gas Tax

1. Section 201.057 of the Texas Tax Code exempts certain high-cost gas from taxes or makes it eligible for a reduced tax rate. The degree of the rate reduction increases with the relative drilling and completion cost of the well.

2. Section 202.056 of the Texas Tax Code exempts gas production from wells that have been inactive (non producing) for a period of at least two years. This exemption is for 10 years after resumption of production.

3. Section 202.056 of the Texas Tax Code exempts gas injected into the earth unless sold for that purpose.[121]

4. Section 201.053 of the Texas Tax Code exempts royalty interest owned by the federal government, the state or political subdivisions.[122]

5. Section 201.058 of the Texas Tax Code exempts natural gas production increased by marketing gas from oil wells that had been previously vented or flared for twelve months or more.[123]

6. Section 201 of the Texas Tax Code exempts Casinghead gas previously vented/flared for 12 months or more.

7. Section 201 of the Texas Tax Code exempts Casinghead production from a railroad commission certified incremental production oil lease.

[121] Sec.201.053, Texas Tax Code

[122] 34 TAC Pt.1, CH.3, Subchapter B, Rule 3.14

[123] Sec.201.058, Texas Tax Code

Oil Production and Regulation Taxes

Oil Production Tax Facts		
	Oil Production	**Oil Regulation**
Date Enacted	1905	1917
Rate When Enacted	1% of value	1/20 of 1% of value
Current Rate	4.6% crude oil produced in state	3/16 of one cent per barrel of crude oil produced in the state
Last Changed	1951	1935
2001 Net Revenue	$ 442 Million	$ 658 Thousand
2002 Net Revenue	$ 338 Million	$ 804 Thousand
2001 Estimated Average Revenue Per	$96 Million	$3.5 Million

* Each of the 4.6 pennies that make up the current oil production tax rate produced an average of $96 million in revenue in fiscal 2001. It is important to note, however, that as the rate is changed, each additional penny produces less revenue than the preceding penny generates.

Oil Production Tax

The oil production tax was enacted in 1905 at 1 percent. With the exception of 1907 when the tax was reduced to .05%, the rate has been increased seven times to 4.6% in 1951. Production from oil wells that were previously inactive for at least two years are exempt from the oil production tax. Revenues generated are allocated to the Foundation School Fund (25%) and the General Revenue Fund.[124] If any year the revenue exceeds $531.9 million (the dollar amount from the tax in fiscal year 1987), 75% of such excess is allocable to the economic stabilization fund. The tax revenue has only exceeded the threshold one time, in 1992.

All revenue generated is allocated to the General Revenue Fund.[125] Excess oil tax revenues are transferred into the Economic Stabilization Fund also known as the "Rainy Day" fund at the end of the biennium.[126] This will be discussed in further detail in the next section.

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[124] Texas Comptroller of Public Accounts, *Sources of Revenue Growth 1972-2001*, May 2002,p. 92

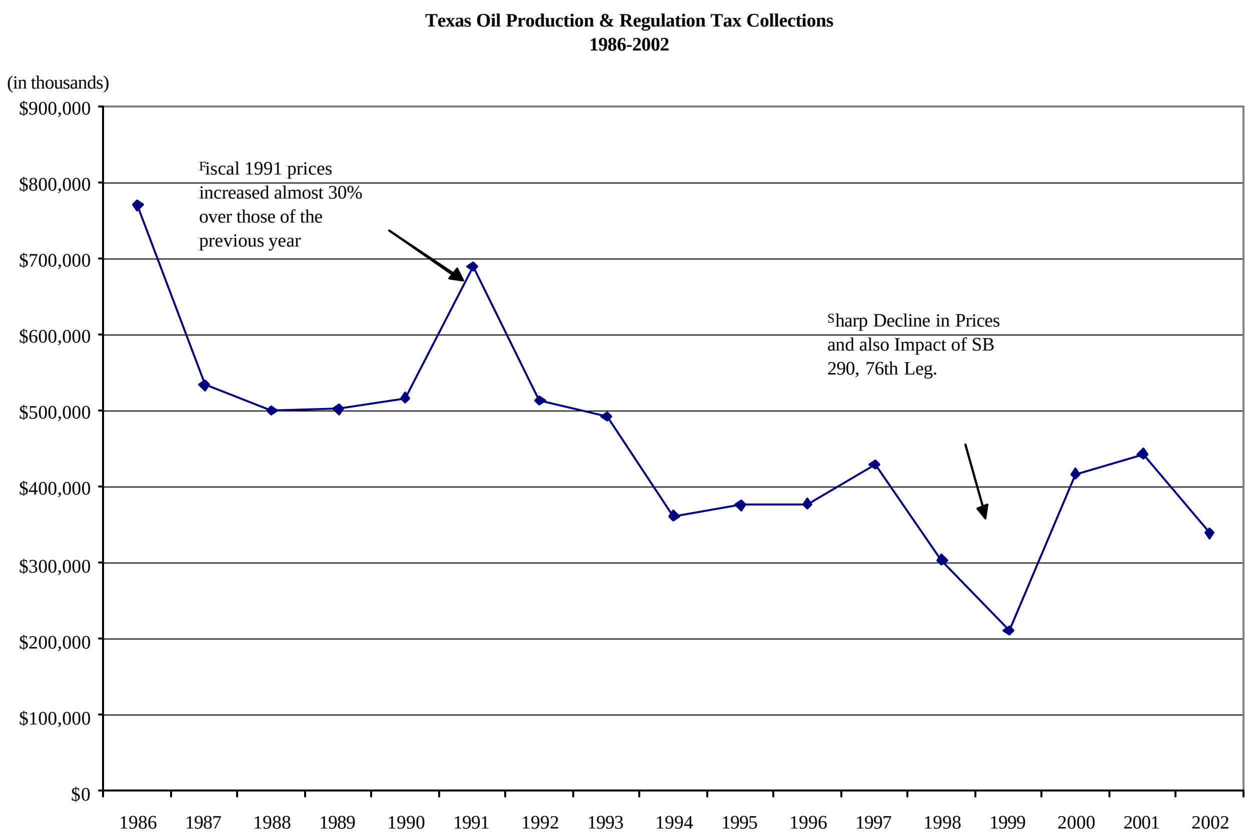
[125] Texas Comptroller of Public Accounts, *Sources of Revenue Growth 1972-2001*, p. 93

[126] Texas Comptroller of Public Accounts, *Fiscal Notes,* January 1999

Oil Production is Subject to Oil Regulation Tax

The oil regulation tax was enacted in 1917 at ½ percent of 1 percent value. Since its enactment, the rate and base has changed three times. The current rate is 3/16 of one cent per barrel of crude oil produced in the state.

Revenues from the oil regulation tax are allocable to the General Revenue fund to be used for administration of state oil and gas conservation laws.



Texas Oil Production & Regulation Tax Collections 1986-2002

* Note: Graph does not include revenue clean up fees.

Exceptions to Base or Rate of the Oil Production Tax

1. **Enhanced Recovery Project**: Oil production from an enhanced recovery project and the incremental oil production from an expanded enhanced recovery project is eligible for a reduced tax rate of 2.3% for a period of ten years.[127]

2. **Previously Inactive Wells:** Oil production from wells that have been inactive for at least 2 years are exempt for 10 years after resumption of production.[128] In FY 2000, 1.6% of reported production was from exempt previously inactive wells.

3. **Benefit of Government Subdivisions:** Royalty Interests in the value of production owned by municipalities, counties, school districts, public colleges and universities, and the federal government are exempt.[129]

4. **Incremental Production Techniques:** A tax credit for incremental production techniques equal to 50% reduction in tax for a period of five years was enacted in 1997. Qualifying incremental productions must have occurred after September 1997 and before December 31, 1998.[130]

5. **TERRA:** Oil production from wells subject to a Texas Experimental Research and Recovery Activity (TERRA).[131] No wells have ever been entered into the TERRA program.

6. **Temporary Severance Tax Relief:** Temporary severance tax relief was granted to leases with an average daily production of 15 barrels per well or less during October, November, and December of 1998. The exemption was scheduled to end in September of 1999 or the date when the cumulative value of exemptions equaled $45 million. The actual exemption occurred during the production months of February, March and April of 1999.

7. **Co-Production:** Co-Production projects also receive 50% exemptions.

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[127] Texas Tax Code, Section 202.054

[128] Texas Tax Code, Section 202.056

[129] TAC PT.1, CH.3, Subchapter C, Rule 3.34

[130] Texas Tax Code, Section 202.057

[131] Texas Tax Code, Section 202.059

Severance Taxes and the Economic Stabilization Fund

In 1988, voters ratified the "Rainy Day" fund and the Legislature approved the transfer of excess natural gas and oil production tax revenues into the fund at the end of the biennium.[132]

Adjustments must be made each year for natural gas taxes, however, to allow for speed-up provisions in state law. The state receives 13 months of natural gas tax in odd-numbered years and 11 months worth in even-numbered years. With this adjustment, the base for the natural gas tax is nearly $600 million. State law requires the Comptroller to transfer revenue from the natural gas tax within 90 days after the end of the fiscal year[133].

In 2001, natural gas prices were extraordinarily high which boosted tax revenue significantly and triggered an unusually large transfer into the fund.

Methods of Funding the Economic Stabilization Fund

There are four basic ways to put the money into this fund:

1. Fund Balances - At the end of each biennium, fifty percent of all undedicated and unencumbered balances are deposited into the fund.

2. Oil Tax Revenue - If this revenue exceeds the cap of $531.9 million set in 1987, the Comptroller deposits 75% of the amount above the cap into the fund.[134]

3. Natural Gas Tax Revenue - If this revenue exceeds the cap of $599.8 million set in 1987, the Comptroller deposits 75% of the amount above the cap into the fund.[135]

4. Appropriations - Money can be appropriated to the fund by the Legislature.

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[132] Texas Comptroller of Public Accounts, *Fiscal Notes,* January 1999.

[133] *Ibid*

[134] *Ibid*

[135] *Ibid*

Methods of Accessing this Fund[136]

There are two ways to access the money in this account:

1. A 3/5ths vote in both houses to remedy a deficit or if the Comptroller forecasts a decline in revenues for a biennium.

2. A 2/3rds vote in both houses if there is no deficit or decline in revenues projected for a biennium.

Note: There is a cap on the balance of the fund; it cannot exceed 10% of GR income for the previous biennium.

Past Expenditures

The Legislature has appropriated (by a 2/3rds vote) from the fund twice. The first time was the 72nd Legislature for $29 million and the second was the 73rd Legislature for $198 million.

Revenue

Due to the spike in natural gas prices in the last few years, the Comptroller of Public Accounts projects the Economic Stabilization Fund is projected will have $1.1 billion in it at the end of FY 2003.

[136] Comptroller of Public Accounts, *Fiscal Notes*, 1999. Available at http://www.window.state.tx.us/comptrol/fnotes/fn9901/fna.html#rainy

Insurance Premium Taxes

Insurance Premium Tax Facts						
	Foreign Life, Accident, and Health	Texas Life, Accident, and Health	Domestic Property and Casualty	Foreign Property and Casualty	Title	Unauthorized, independently procured, and surplus lines
Date Enacted	1907	1936	1907	1907	1985	
Rate When Enacted	0.5/1.0/3.0%	0.50%	2%	2%	1.1/1.8/2.5%	
Current Rate	1.75%	1.75%		1.60%	1.35%	4.85%
Last Changed	1989	1989	1999	1999	1999	1989 and 1993
2001 Net Revenues	$716.2 Million					
2002 Net Revenues	$920.4 Million					
Each 1% of FY 2001 Revenue Equals*	$7.2 Million					

* Revenue estimate based on 2001 Net Revenue. This addresses only the insurance premium tax; the maintenance tax not included. It is important to note, however, that as the rates are changed, each incremental increase produces less revenue than the preceding increment generates.

Overview

The insurance premium tax is Texas' oldest business tax dating back to 1862 and predating the Texas franchise tax by 50 years. Before 1907, insurance companies were assessed a flat $50 annual tax.[137]

In 1907, the "Robertson Law" was introduced. This law based rates off of a tiered rate structure based on gross premiums and the proportion of the insurer's investment in the state. Despite many subsequent rate changes, insurance premium taxes were based on these principles until 1989. In 1989, the Legislature adopted a flat tax rate of 1.75% of gross premiums. Flat tax rates for property and casualty and title insurance were enacted in 1999.

[137] Texas Comptroller of Public Accounts, *Sources of Revenue Growth 1972-2001*, p. 149

The insurance tax varies with the type of insurance provided:

1. Life and health insurance: the life, health, and accident insurance and HMO tax rate is 1.75% of gross premiums receipts. For life insurance premiums and HMO receipts, a half-rate applies to the first $450,000 in premiums or receipts.[138]

2. Property and Casualty Insurance: The tax rate is leveraged at 1.6% of gross premiums.[139]

3. Title Insurance: The tax Rates for title insurance is 1.35% of gross premiums.[140]

4. Other types of Insurance Tax Rates:
    a. Unauthorized Insurance Premium Rate: 4.85% of gross premiums charged.
    b. Surplus Lines Insurance Rate: 4.85% of gross premiums charged.
    c. Independently Procured Rate: 4.85% of gross premiums charged.[141]

Revenues generated from insurance premium taxes are allocated to the Foundation School Fund (25%) and the General Revenue Fund (75%).[142] Exemptions to the premium tax are Medicare/Medicaid premiums and public employee group coverage.

[138] Texas Insurance Code, Article 4.11

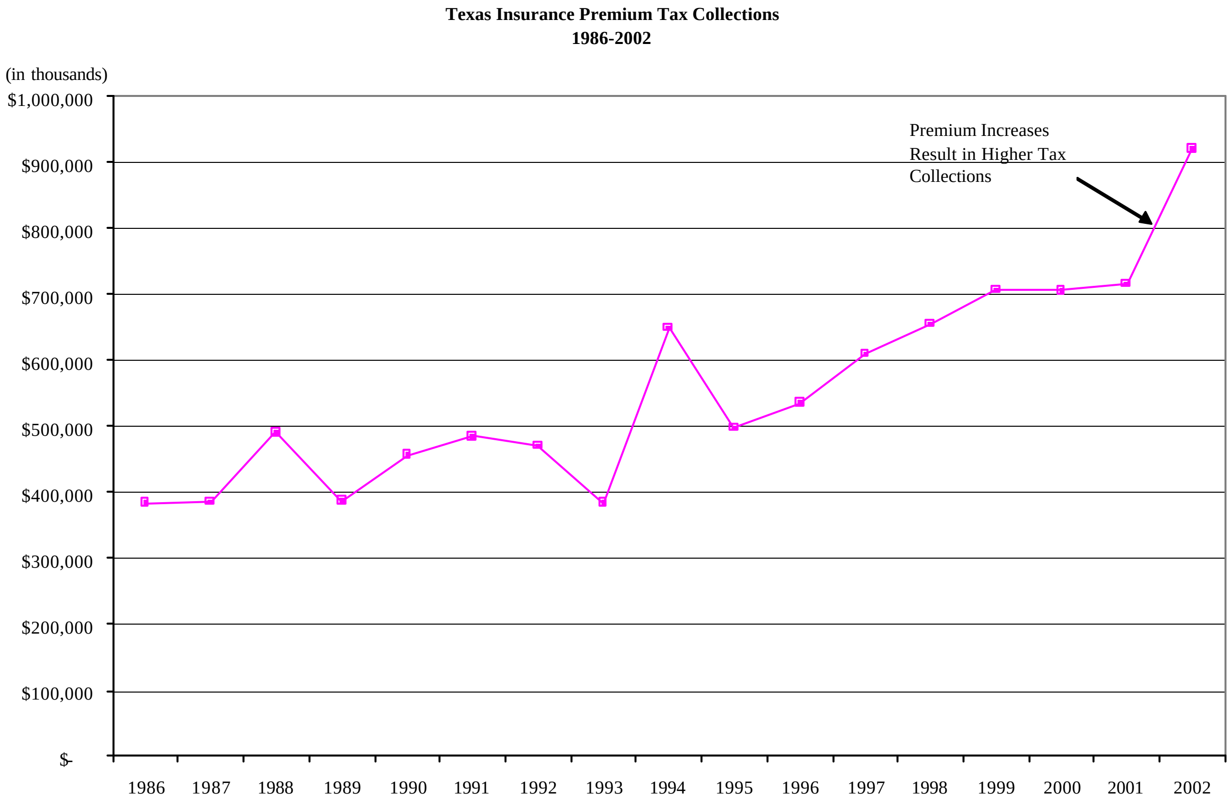
[139] Texas Insurance Code, Article 4.10

[140] Texas Insurance Code, Article 9.59

[141] Texas Insurance Code, Article 1.14-2 and Title 2, Section 101.251 and 101.252

[142] Texas Insurance Code, Article 1.31 A

Texas Insurance Premium Tax Collections Over Time (1986-2002)



Cigarette and Tobacco Taxes

Cigarette and Tobacco Tax Facts		
	Cigarettes Tax	Cigar and Tobacco Products Tax
Date Enacted	1935	1959 (prior to 1959, taxed under the cigarette tax)
Rate When Enacted	$0.03/pack of 20	$0.01/10 small cigars, $7.50/1000 on large cigars not more than 3.3 cents each (retail price), $15.00/1000 large cigars over 3.3 cents each (retail price)
Current Rate	$0.41/conventional pack of 20 cigarettes	Cigar weight varies with weight per 1,000, constituents, and price: from $0.01 per 10 cigars for weight under 3 lbs. to $15 per 1000 cigars for weight over 3 lbs.; chewing/smoking tobacco and snuff: 35.213 percent of factory price.
Last Changed	1990	1990
2001 Net Revenue	$543.7 Million	$40.9 Million
2002 Net Revenue	$472.8 Million	$ 67.3 Million
2004-05 revenue generated from a 40% tax on the manufacturer's list price to all tobacco products, including cigarettes,	$300 million	
2004-05 Estimated Revenue Generated from a $0.10 Per Pack Increase.	$197 Million	NA
Estimated Revenue Generated from a $1 increase in the per pack tax.	$1.5 billion	NA

Overview

A tax is imposed when a distributor receives cigarettes for the purpose of making a first sale in Texas. A stamp must be affixed to each package within 96 hours of receipt. This stamp is evidence that the state tax has been paid.

The Texas cigarette tax was first enacted in 1931 at 3 cents per pack. The rate as of 1950 was 4 cents. The tax increased in 1955 to 5 cents. From 1955 to 2002 it was increased nine times.[143]

[143] The Tax Burden On Tobacco, *Historical Compilation Volume 36*, 2001, p.9.

Taxes on Tobacco Products

In 1959, Texas and 6 other states (HI, MI, NY, SC, VT, WA) joined 11 states (AL, AZ, GA, LA, MN, MS, NH, ND, OK, SC, TN) in taxing both cigarettes and other tobacco products.[144] As of January 1, 2002, Texas taxes other tobacco products as follows:[145]

A tax is imposed on cigars and tobacco products when a permit holder receives them for the purpose of making a first sale in this state.

The tax on cigars is based on weight per 1,000 and the retail selling price.

1. Cigars weighing not more than 3 pounds per 1,000: 1 cent for each 10 cigars
2. Cigars weighing more than 3 pounds per 1,000 and retailing for not more than 3.3 cents each: $7.50 per 1,000.
3. Cigars with a factory price over 3.3 cents each without non-tobacco ingredients, per 1,000 Cigars.
4. Cigars of all description weighing more than 3 pounds per 1,000 and retailing for over 3.3 cents each, containing no substantial amount of non-tobacco ingredients: $15.00 per 1,000.
5. Chewing, pipe or smoking tobacco, and snuff: 35.213% of the manufacturer's list price exclusive of any trade discount, special discount, or deal.

Cigarette Tobacco Tax Exemptions

Exemptions include the importation from other states of up to 200 cigarettes, sales to Indian tribal facilities, and sales to all federal institutions.

Revenue collected from Texas Tobacco Taxes as of Fiscal Year Ending June 30, 2001[146]

Taxes	Gross Amount	Net Collections
Cigarettes Taxes	$ 495,713,837	$ 480,842,422
Other Tobacco Taxes	$ 55,551,335	$ 55,551,335
Total Cigarette and Other Tobacco Taxes	$ 551, 265,172	$ 536,393,757

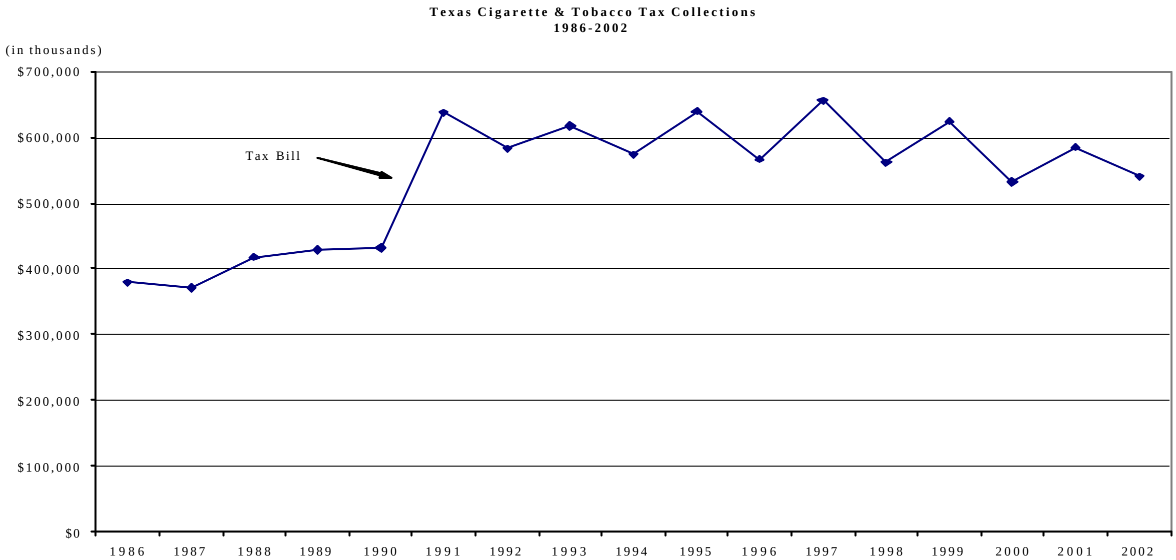
The percentage of total tobacco taxes from cigarettes was 89.9% while the percentage of total

[144] The Tax Burden On Tobacco, *Historical Compilation Volume 36*, 2001, p.41.

[145] The Tax Burden On Tobacco, *Historical Compilation Volume 36*, 2001, p.83.

[146] The Tax Burden On Tobacco, *Historical Compilation Volume 36*, 2001, p.82.

tobacco taxes from other tobacco products was 10.1%.



Texas Cigarette & Tobacco Tax Collections Over Time (1986-2002)

Texas Historical Cigarette Tax Data[147]

[147]Section 201 of the Texas Tax Code exempts Casinghead gas previously vented/flared for 12 months or more The Tax Burden On Tobacco, *Historical Compilation Volume 36*, 2001, p272

Tax Rate	Year	Gross State Cigarette Taxes (in thousands of dollars)	Net State Cigarettes Taxes (in thousands of dollars)	State tax-paid cigarette sales (millions of packs)	Per Capita sales (packs) Millions	Average Retail Price Cents	State & Federal Cigarette taxes as a percentage of retail price
$0.04	1955	36,016	34,936	900.4	109.3	22.3	53.8
$0.05	1956	43,329	42,029	866.6	101.3	247	52.6
$0.08	1960	74,556	72,815	995.5	105.3	28.7	55.8
$0.11	1966	125,156	122,214	1,120.0	106.1	33.8	56.2
$0.155	1970	169,554	165,739	1,190.2	106.4	40.4	58.2
$0.185	1972	226,504	220,649	1,244	108.6	46.9	56.5
$0.195	1985	360,500	347,500	1,873.3	115.9	102.1	34.8
$0.205	1986	373,507	358,783	1,845.9	113.7	105..5	34.6
$0.26	1988	399,060	384,281	1,630.1	96.5	128.0	32.8
$0.41	1991	552,917	542,829	1,363.8	79.4	173.6	32.8
$0.41	2001	495,714	480,842	1,294.7	62.1	311.2	24.1

National Cigarette Tax Increases in 2002[148]

In FY 2002, a number of states increased cigarette taxes.

[148]Information Compiled by Federation of Tax Administrators from various sources. And from State Tax Notes, CCH, Federation of Tax Administrators, and Tax Foundation, December 1,2002.

Like many states the 78th Texas Legislature will be presented with the option of examining the various taxes imposed on cigarettes and tobacco products.

Cigarette Tax Increases in 2002					
	Tax Increase Per Pack	New Tax Rate/Pack of 20	%Tax Increase Per Pack	Effective Date	Comment
Arizona	$ 0.60	$ 1.18	103%	11/26/2002	Proposition 303 passed by voters on November 2002 ballot
Connecticut	$ 0.61	$ 1.11	122%	4/3/2002	Passed by Legislature; signed by Governor
Hawaii	$ 0.20	$ 1.20	20%	10/1/2002	First of three step increase. Approved by Legislature; signed by Governor.
Illinois	$ 0.40	$ 0.98	69%	7/1/2002	Passed by Legislature; signed by Governor
Indiana	$ 0.40	$ 0.555	258%	7/1/2002	Passed by Legislature; signed by Governor
Kansas	$ 0.46	$ 0.70	192%	7/1/2002	Approved by Legislature; signed by Governor
Louisiana	$ 0.12	$ 0.36	50%	7/1/2002	Signed by Governor
Maryland	$ 0.34	$ 1.00	52%	6/1/2002	Approved by Legislature; signed by Governor
Massachusetts	$ 0.75	$ 1.51	99%	7/25/2002	Passed House + Senate; vetoed by Governor; Veto Overriden
Michigan	$ 0.50	$ 1.25	67%	8/1/2002	Passed by Legislature; signed by Governor
Nebraska	$ 0.30	$ 0.64	88%	10/1/2002	Rate returns to 34 cents 10/1/04
New Jersey	$ 0.70	$ 1.50	88%	7/1/2002	Passed by Legislature; signed by Governor
New York	$ 0.39	$ 1.50	35%	4/3/2002	Passed by Legislature; signed by Governor
Ohio	$ 0.31	$ 0.55	129%	7/1/2002	Passed by Legislature; signed by Governor
Pennsylvania	$ 0.69	$ 1.00	223%	7/15/2002	Passed by Legislature; signed by Governor
Rhode Island	$ 0.32	$ 1.32	32%	7/1/2002	Approved by Legislature; vetoed by Governor; veto Overridden
Tennessee	$ 0.07	$ 0.20	54%	7/15/2002	Passed by Legislature; signed by Governor
Utah	$ 0.18	$ 0.696	35%	5/6/2002	
Vermont	$ 0.49	$ 0.93	111%	7/1/2002	Signed by Governor
Washington	$ 0.60	$ 142.5	73.00%	1/1/2002	Referendum approved by voters
U.S. Median		$0.48		10/1/202	

Estimated Revenue Gains for Possible Changes in Texas Tobacco Tax for FY 04-05[149]

Shown below are additional specific 2004-05 revenue estimates that were requested by members of the Senate Finance Committee regarding tobacco taxes. The intent of this section is to look at the amount of revenue that could be realized through various changes and in no way represents an endorsement of any of the specific methods by the Senate Finance Committee or its individual members**.** Each estimate assumes the tax change would take effect in September 2004 and that each would be subject to tax planning structure similar to those in use for the OTP tax.

1. Imposing a cigar tax at the rate of "other tobacco products" (OTP) tax of 35.213 percent of the manufacturer's list price would raise $19 million.

2. Imposing on all tobacco products other than cigarettes, a tax of 40 percent of the manufacturer's list price would raise $26 million.

3. Imposing on all tobacco products, including cigarettes, a tax of 35.213 percent of the manufacturer's list price would raise $248 million.

4. Imposing on all tobacco products, including cigarettes, a tax of 40 percent of the manufacturer's list price would raise $300 million.

When discussing the issue of tobacco taxes, a prevalent question is, what has the state done with the proceeds of the tobacco settlement?

[149] Texas Comptroller of Public Accounts, September 2002.

Tobacco Settlement Funds

In November 1998, 46 states signed a landmark $246 billion Master Settlement Agreement with the tobacco industry (Florida, Minnesota, Mississippi and Texas settled separately). Texas' historic agreement with the tobacco industry compensated the state for funds expended treating tobacco related illnesses. Per the terms of the agreement, the state is scheduled to receive over $15 billion from the tobacco industry during the next 25 years. The settlement agreement does not restrict the state's use of the funds.

In addition to the tobacco settlement funds being deposited for the benefit of the state, an additional $2.275 billion will be set aside for political subdivisions in the state. For purposes of the agreement, the term political subdivisions means "all hospital districts, other local political subdivisions owning and maintaining public hospitals, and counties of the State of Texas responsible for providing indigent health care to the general public." These additional sums derive from the "Most Favored Nation" clause in the Texas settlement, which allows Texas to benefit from any subsequent agreement between the tobacco industry and the states that has terms more advantageous than those contained in the original settlement.

Based upon a memorandum of understanding between the state and representatives of the political subdivisions, tobacco industry payments destined for the political subdivisions are allocated to two fund pools. The first, a lump sum trust account, received its first $300 million installment in January 1999. Another $150 million was received both in fiscal year 2000 and 2001. The first $300 million of county funds was distributed to the political subdivisions in January 1999, on a per capita basis.

The two remaining lump sum payments were distributed to the political subdivisions based upon their "total unreimbursed health care expenditures for providing health care services to the general public for the calendar year immediately preceding the year of the lump sum distribution...."[150] The Texas Department of Health gathered data and determined the amount to be paid to each political subdivision.

An additional $1.825 billion (before adjustments) for the political subdivisions will be deposited over the a four year period to the second fund pool, a permanent trust account. The last installment will be paid in January 2003. The funds will be invested and the earnings from the permanent trust account will be distributed annually to the political subdivisions.[151]

[150] See Agreement Regarding Disposition of Settlement Proceeds, Paragraph 5(B), *The State of Texas v American Tobacco Company*, et al., No. 5-96CV-91 (filed July 24, 1998).

[151] Tobacco Settlement Funds, *Texas Government Accounting Information*- Volume 8, Number 4 - April 1999

Tobacco Settlement Income for Five Years[152]

Texas Tobacco Settlement Funds 1999-2003	
Fiscal Year	Tobacco Settlement Funds (in thousands)
1999	1.097 Million
2000	295.2 Million
2001	379.4 Million
2002	493.6 Million
2003	Estimated 523.0 Million

How Other States Are Using Tobacco Settlement Funds

Although most states have put at least a portion of their settlement dollars toward tobacco control and other health programs, the levels have been far below what the Center for Disease Control and Prevention (CDC) put forward in 1999 in a set of Best Practices that offers steps and recommended funding levels for implementing a comprehensive nine-part smoking prevention program.[153] The State of Texas funded prevention programs in the FY 2002-03 biennium at $10 million per year**.**

Five states-Arizona, Maine, Massachusetts, Minnesota and Mississippi- are funding the prevention programs at the recommended minimum level.[154] However, health care programs continue to consume a large share of settlement revenue. Over the last two years, states have spent $1 billion in settlement funds on smoking prevention programs and more than $8 billion on other care services.[155] <u>The State of Texas has spent all of its settlement money on healthcare issues, primarily the Children's Health Insurance Program (CHIP).</u>

As of June 2002, 15 states-Arizona, California, Idaho, Indiana, Kentucky, Maine, Michigan, Minnesota, Mississippi, Missouri, New Jersey, Ohio, Rhode Island and Washington**,** and the District of Columbia-have tapped into tobacco funds to balance their FY 2003 budgets.[156]

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[152] Texas Comptroller of Public Accounts, 9/02

[153] State Health Notes, *Filling Budget Holes: Tobacco Settlement Offers States a Tempting Source of Revenue*, June 17, 2002

[154] NCSL, *State Management and Allocation of Tobacco Settlement Revenue 1999 to 2001*, August 2002

[155] State Health Notes, *Filling Budget Holes: Tobacco Settlement Offers States a Tempting Source of Revenue*, June 17, 2002

[156] *Ibid*

Alcoholic Beverage Taxes

Alcoholic Beverage Tax Facts						
	Beer	**Liquor**	**Malt Liquor**	**Wine**	**Mixed Beverage**	**Airline/Passenger Train Beverage Tax**
Date Enacted	1935	1935	1935	1935	1971	1969
Rate When Enacted	$1.24/barrel	$0.80/gallon	$0.15/gallon	14% or less Alcohol- $0.02/gallon; greater than 14%, but not more than 24%-$0.50/gallon; greater then 24% alcohol- $0.5/gallon; Sparkling wine $0.25/gallon	10%	$0.05 per serving of an alcoholic beverage
Current Rate	$6.00/31 gallon barrel	$2.40/gallon	0.198/gallon	14% or less Alcohol- $0.204/gallon; greater than 14% - $0.408/gallon; Sparkling wine $0.516/gallon	14% of gross receipts	$0.05 per serving of an alcoholic beverage
Last Changed	1984	1984	1984	1984	1990	1993 (Limousine services excluded)
2001 Net Revenues	$101 Million	$47.8 Million	$4.7 Million	$6.6 Million	$380.6 Million	$609 Thousand
2002 Net Revenues	$102 Million	$49 Million	$4.5 Million	$6.9 Million	$396.8 Million	$443 Thousand
2001 Revenue Per Penny-Gallon or Penny of Gross Receipts	$5.2 Million*	$199 Thousand	$237 Thousand	$324 Thousand	$27 Million**	N/A
2004-05 Revenue	10% $21 million	10% $7.5 million	10% $1.2 million	10% $1.2 million	NA	N A

* Each of the 19.35 pennies that make up the current beer-per-gallon tax rate produced an average of $5 million in revenue in fiscal 2001. It is important to note, however, that as the rate is changed, each additional penny produces less revenue than the preceding penny generates.

* *Each of the 14 pennies that make up the current mixed beverage tax rate produced an average of $27 million in revenue in fiscal 2001. It is important to note, however, that as the rate is changed, each additional penny produces less revenue than the preceding penny generates. Also, local governments receive 21.4% of the revenue--divided evenly between counties and, as appropriate, cities.

Overview

In 2002, the Alcoholic Beverage Tax collections were approximately $560 million. In Texas, the alcoholic beverage tax includes separate taxes on liquor, beer, wine, ale, mixed beverages, and airline/passenger train beverages.

Beer Tax

The beer tax was enacted in 1935 at $1.24 per barrel. Since 1935, the beer tax rate has changed 6 times. Today, the tax is levied at $6.00 per 31 gallon barrel. Total net collections for FY 2001 were $101 million, with 100% of the money being allocated to the General Revenue Fund.[157] federal military facility sales are exempted from the beer tax.

Liquor Tax

The liquor tax was enacted in 1935 at $0.80 per gallon. Since its enactment, the liquor tax rate and base has changed seven times. Today, the state liquor tax is $2.40 per gallon. Exemptions to the liquor tax are to federal military facility sales. All revenues from this tax are allocated to the General Revenue Fund.[158]

Malt Liquor (Ale) Tax

The malt liquor tax was enacted in 1935 at $0.15 per gallon. Since its enactment, the rate and base has changed twice. The first increase occurred in 1951 to $0.165 per gallon, the second in 1984 to its current rate of $0.198 per gallon.[159] Exempted from this tax are sales to federal military facilities. All revenue generated from the malt liquor tax is allocated to General Revenue Fund.

Mixed Beverage Tax

The mixed beverage tax was enacted in 1971 at 10 percent. Since its enactment, the rate and base has changed twice. The first increase to this tax occurred in 1984 to 12 percent, the second increase occurred in 1990 to its current level of 14% of gross receipts. There are no exemptions for the mixed beverage tax.

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[157] Texas Comptroller of Public Accounts, Texas Alcoholic Beverage Commission, 2002.

[158] Texas Comptroller of Public Accounts, *Sources of Revenue Growth 1972-2001*, May 2002, p. 77

[159] Texas Comptroller of Public Accounts, *Sources of Revenue Growth 1972-2001*, May 2002, p. 79

Revenues generated from the mixed beverage tax are allocated to the General Revenue Fund:

1. 10.7143 percent dedicated for rebates to counties
2. 10.7143 percent dedicated for rebates to cities
3. Undedicated General Revenue-balance[160]

Airline/Passenger Train Beverage Tax

The airline/passenger beverage tax was enacted in 1969 at $0.05 per serving. Since its enactment, the rate has not changed, yet the base has changed three times. The first base change occurred in 1985 when passenger train service was included. The second change occurred in 1987 with the addition of limousine services. Limousine services were then excluded in 1993. There are no exemptions to this tax and all revenue generated from the airline/passenger train beverage tax is allocated to General Revenue Fund.[161]

Texas Alcoholic Beverage Tax Collections Over Time (1986-2002)

[160] Texas Comptroller of Public Accounts, *Sources of Revenue Growth 1972-2001*, May 2002, p. 81.

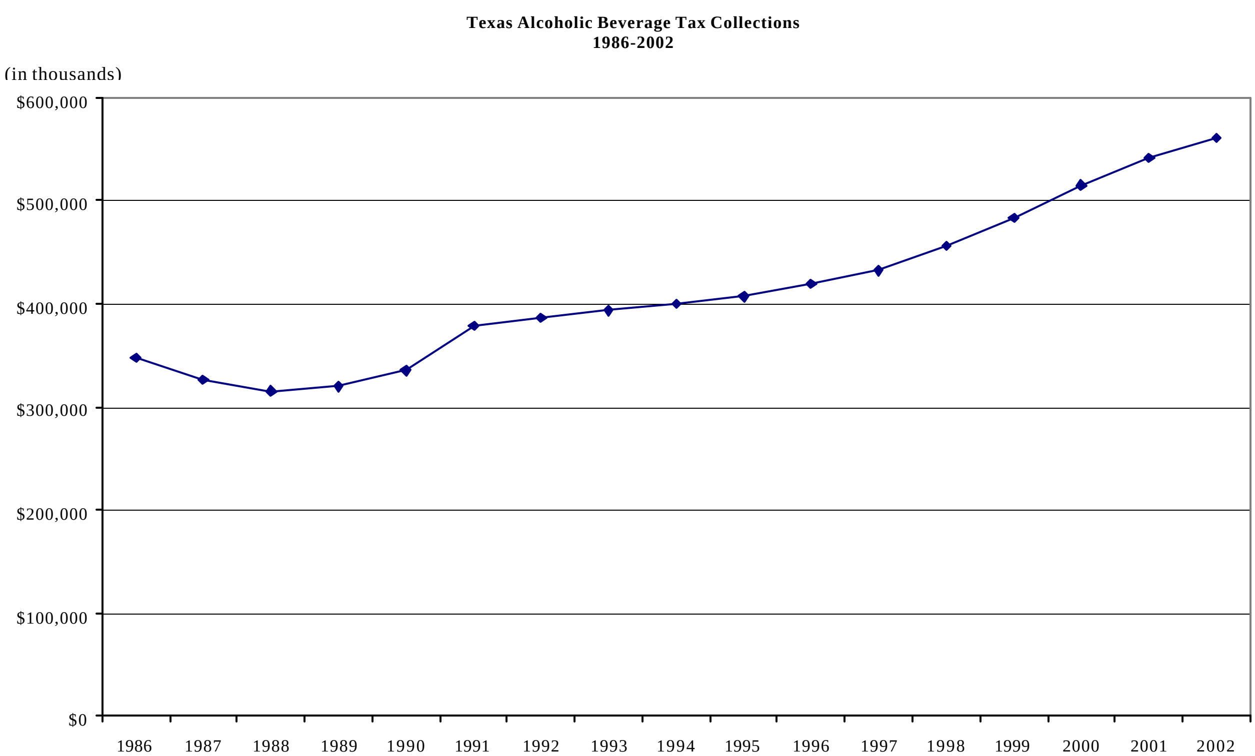
[161] Texas Comptroller of Public Accounts, *Sources of Revenue Growth 1972-2001*, May 2002, p. 47.

What Other States Have Done

Given current state budget difficulties, the following states have chosen to raise the tax on alcohol in the following ways:

1. Tennessee raised the tax rate on beer, wine, and distilled spirits by 10 percent across the board .

2. Alaska enacted the "dime a drink" tax, tripling the rate on beer from 35 cents a barrel to $1.07.[162]



[162]Governing Magazine, *Taxing Smoke and Beers,* September 2002.

Inheritance Tax

Inheritance Tax Facts	
Date Enacted	1923
Rate When Enacted	2% to 12%, based on the relationship of the beneficiaries and the amount of exemptions
Current Rate	Tax equivalent to the federal credit for state inheritance tax imposed on the transfer of property at death
Last Changed	2001-2002
2001 State Net Revenue	$ 334.2 Million
2002 State Net Revenue	$ 334.2 Million
Estimated Revenue Per Penny Increase from Decoupling	N/A

Note: The inheritance tax is being phased out by fiscal 2006 under federal law (HR 1836). The last date of death for which any state tax will be levied is Dec 31, 2004. The last year that federal tax would be collected is for deaths occurring in 2009.

Overview

The inheritance tax was enacted in 1923 at 2 percent to 12 percent, based on the relationship of beneficiaries and the amount of exemptions. In the late 1970s, the Legislature revised the laws governing the inheritance tax to establish a $200,000 estate exemption that gradually increased to $300,000 by 1985. Subsequent legislation in 1981 revamped the tax as a “piggy-back” on the federal estate tax.[163]

In fiscal 1999, collections surpassed $256 million. Today, the state tax is equivalent to the federal credit for state inheritance tax imposed on the transfer of property at death. The Federal inheritance tax is imposed on an estate with assets in excess of $1 million for deaths in calendar year 2002.[164]

The 107th U.S. Congress (2001-2002) passed H.R. 1836, which will gradually eliminate the federal estate tax by calendar 2010 and the state inheritance tax by fiscal 2006. This legislation gradually increases the federal estate value exemption and decreases the tax rates, thereby eliminating the state death tax credit by fiscal 2006 or calendar 2005.

[163] Comptroller of Public Accounts, *Sources of Revenue Growth 1972-2001*, p. 21

[164] Texas Comptroller of Public Accounts, *Sources of Revenue Growth 1972-2001*, p. 71

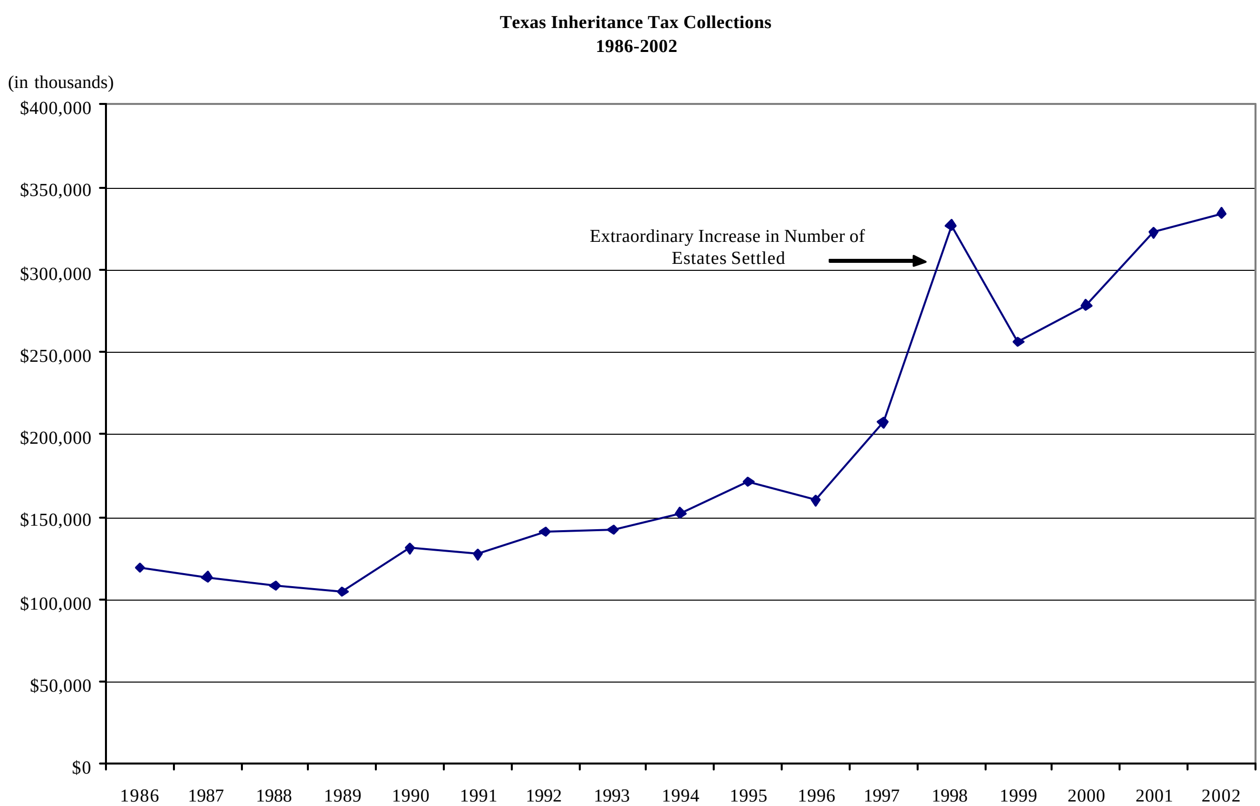
More specifically the phase out is accomplished in three ways:

1. The unified credit against the tax—basically an exclusion amount—is increased to $1 million in calendar 2002 and to $1.5 million in 2004. It becomes $2 million in 2006 and $3.5 million in 2009.
2. The maximum federal tax rate is gradually decreased.
3. The amount states can "pick up" under their taxes is reduced.

Unless the federal provisions are extended, the state and federal taxes would be reinstated in 2011.

In fiscal year 2002, the state inheritance tax generated $322.5 million, all of which was allocated to the General Revenue Fund. The gradual phase out of the tax will incrementally decrease the revenue estimate each year until 2010. Because of this change, many states are looking for alternative revenue sources to make up for the loss of revenue.

Texas Inheritance Tax Collections Over Time (1986-2002)



As one can see from the graph above, the inheritance tax represents a significant amount of revenue. This issue has also affected other states who have dealt with the issues in a variety of ways as shown in the next section.

How Other States "Levy" Death Tax

This discussion addresses how other states have levied the inheritance tax prior to the passage of H.R. 1836 (107th Congress), which gradually phases out and will completely eliminate the state inheritance tax by fiscal 2006. The trend in state death taxes has clearly moved in the direction of eliminating traditional taxes and imposing only pick-up taxes.[165]

Trend in State Death Taxes		
Type of Tax	**Number of States Imposing Respective Tax**	
	1989	**1999**
Inheritance Tax	18 states	14 states
Estate Tax	8 states	4 states
Solely "pick-up" tax	25 states & District of Columbia	34 states & District of Columbia

Inheritance Tax: Inheritance taxes are the oldest and most common form of death taxes and are typically levied at graduated rates based upon the amount of the bequest and upon the relationship between the deceased and the beneficiary.

Estate Tax: Generally, estate taxes are levied at graduated rates based upon the value of the estate. The rates generally are imposed on the estate as a whole and do not vary based upon the relationship of the beneficiary to the donor.

Pick-up Tax: A pick-up tax is a variation of the estate tax based on an important link between federal and state death taxes. Federal statutes allow taxpayers to claim a credit against state taxes paid up to certain amounts that depend on the estate's total value. In effect, this allows states to levy a tax and "pick-up" estate taxes that would be levied by the federal government anyway. This tax does not increase the total liability for the heirs since the state is realizing a portion of the federal estate tax revenue. As a result, all states impose a pick-up tax up to the allowable federal credit.

Gift Tax: A gift tax is a levy on wealth given by living donors. The rates imposed and the exemptions allowed under gift tax statutes are similar to rates and exemptions under the inheritance tax. Donors, rather than recipients, are liable for gift taxes.

[165] State Death Taxes, *Fiscal Affairs*, April 1999. Available at http://www.ncsl.org/programs/fiscal/deathtax.htm

Prior to H.R.1836

Since 1989, Delaware, Kansas, Louisiana (phasing-out over six years), Michigan, North Carolina and Wisconsin have repealed their inheritance taxes. Iowa and Kentucky eliminated the tax on lineal descendants, and Ohio and Pennsylvania exempted surviving spouses. Thirteen states now impose an inheritance tax, including Louisiana where the tax will be totally phased out by 2002.

Only Mississippi, New York, Ohio and Oklahoma have estate taxes in addition to the pick-up tax. Since 1989, Rhode Island, Massachusetts and South Carolina have eliminated estate taxes. In 1997, New York began reducing estate taxes by gradually increasing the estate tax deduction to $250,000 for a primary residence.

A decline in the use of gift taxes also has occurred in recent years. In 1980, 14 states levied gift taxes; in 1989, that number had dropped to seven; and by the end of 1998, only five states (Connecticut, Louisiana, New York, North Carolina and Tennessee) imposed gift taxes. New York reduced gift taxes in 1997 with a full repeal that took place on January 1, 2000.

State policymakers have lowered death taxes in four ways:

1. Eliminated them altogether solely in favor of a pick-up tax;
2. Increased exemptions or credits;
3. Decreased rates; or
4. Exempted certain classes of beneficiaries (e.g., spouses).

States that levy a death tax in addition to the pick-up tax often combine alternatives when reducing the burden. While all states have not cut death taxes, providing full exemptions for spouses gradually has become a more common feature. Of the 14 states imposing an inheritance tax, all exempt transfers to spouses. Oklahoma and Ohio exempt inter-spousal transfers under the estate tax. Of the six states that levy a gift tax, Louisiana, New York and North Carolina exempt transfers to spouses.[166]

[166] State Death Taxes, *Fiscal Affairs*, April 1999. Available at http://www.ncsl.org/programs/fiscal/deathtax.htm,

Death Taxes By State [167]

Death Taxes by Type and State									
State	**Inheritance & pick-up**	**Estate & pick-up**	**Pick-up only**	**Gift**	**State**	**Inheritance & pick-up**	**Estate & pick-up**	**Pick-up only**	**Gift**
Connecticut	X			X	Georgia			X	
Maine			X		Kentucky	X			
Massachusetts			X		Louisiana	X			X
New Hampshire	X				Mississippi		X		
Rhode Island			X		North Carolina			X	X
Vermont			X		South Carolina			X	
Delaware			X		Tennessee	X			X
Maryland	X				Virginia			X	
New Jersey	X				West Virginia			X	
New York		X		X	Arizona			X	
Pennsylvania	X				New Mexico			X	
Illinois			X		Oklahoma		X		
Indiana	X				Texas			X	
Michigan			X		Colorado			X	
Ohio		X			Idaho			X	
Wisconsin			X		Montana	X			
Iowa	X				Utah			X	
Kansas			X		Wyoming			X	
Minnesota			X		Alaska			X	
Missouri			X		California			X	
Nebraska	X				Hawaii			X	
North Dakota			X		Nevada			X	
South Dakota	X				Oregon			X	
Alabama			X		Washington			X	
Arkansas			X		District of Columbia			X	
Florida			X		Puerto Rico	X*			

*Resident of Puerto Rico are not subject to the Federal Estate Tax, therefore, no pickup tax is levied.

The Future of State Death Taxes Post H.R. 1836

While more and more states have abandoned traditional death taxes in favor of the pick-up tax, many states were reluctant to eliminate death taxes entirely because they provide a stable source of revenue. This is particularly noteworthy in an aging society given the growing use of income and property tax breaks provided to the elderly. However, the uncertainties surrounding federal tax reform and

[167] NCSL research based on data provided by the Commerce Clearing House, January 1999.

reduction in federal aid levels have prompted states to seek out all viable sources of revenue, and death taxes would become a more significant source of revenue as the population ages.[168]

Since the passage of H.R. 1836, many states have weighed their options to retain the large revenue stream provided by this tax. One such option is to detach or "decouple" the state inheritance tax from the federal portion and create a stand-alone tax.

Decoupling from the Federal Estate Tax Cut

States can protect themselves from this immediate and large revenue loss while the federal provision is in effect. States can choose not to conform to this federal change.[169] "Decoupling means protecting their relevant parts of their tax code from the changes in the federal tax code, in most cases by remaining linked to federal law as it existed prior to the change."[170]

What Various States are Doing about the Estate Tax

Sixteen states and the District of Columbia are currently decoupled and eleven states have acted to decouple from the federal changes. [171]

Most states can decouple through actions by the legislature.[172]

1. Seven states enacted legislation linking their estate taxes to the federal estate tax as in effect before the 2001 tax bill.
2. Minnesota elected not to change its estate tax to conform to Federal changes.
3. Maine decoupled for 2002.
4. Wisconsin decoupled through 2007.

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[168] *Ibid*

[169] Center on Budget and Policy Priorities, *States Can Avoid Substantial Revenue Loss by Decoupling from New Federal Tax Provision*, 2002. Available at http://www.centeronbudget.org/3-20-02sfp.htm

[170] Center on Budget and Policy Priorities, *Many States are Decoupling from the Federal Estate Tax Cut*, October 2002. Available at http://www.cbpp.org/statecrisis.htm

[171] Center on Budget and Policy Priorities, *Many States are Decoupling from the Federal Estate Tax Cut*, October 2002. Available at http://www.cbpp.org/statecrisis.htm

[172] *Ibid*

5. Oregon passed legislation that will freeze the estate tax at the 2001 level until 2005, at which time the tax would be repealed.

6. Nebraska decoupled by creating a separate state estate tax on estates that exceed $1 million based on the federal law prior to the 2001 changes.

Oklahoma is the only state that has no need to decouple. Its separate tax is designed in a manner that avoids the revenue loss from the federal changes. Some of the problems states face when attempting to decouple are as follows:

1. California- Decoupling would require a statewide referendum.

2. Alabama, Florida, Nevada- Constitutional provisions restricting the amount of estate tax levied would have to be changed.[173]

[173] *Ibid*

Utility Taxes

Utilities Tax Facts			
	Public Utility Gross Receipts Assessment	**Gas, Electric & Water Utility Tax**	**Gas Utility Pipeline Tax**
Date Enacted	1975	1907	1920
Rate When Enacted	1/6 of 1% of gross receipts	0.0% , 0.5%, and 1.0% for cities with populations listed below	.025% of gross receipts
Current Rate	1/6 of 1% of gross receipts	Cities with population over 1,000 to 2,499 -0.581% of gross receipts	1/2 of 1% of gross income (gross receipts less the cost of gas sold) of gas utilities
		Cities with population over 2,500 to 9,999 -1.07% of gross receipts	
		Cities with population over 9,999 - 1.997% of gross receipts	
Last Changed	N/A	1959	1989
2001 Net Revenues	$48.6 Million	$284.6 Million	$6.9 Million
2002 Net Revenues	$43.8 Million	$ 262.5 Million	$4.8 Million
Estimated Average Revenue Per Penny Increase*	$291.6 Million	$142.5 Million	$12.4 Million
2004-05 revenue generated from a 200% increase (of current law levels)	$510 Million		

* Each of the 1.997 pennies--using the rate for cities with populations of 10,000 or more--that make up the current G.E.&W. tax rate produced an average of $143 million in revenue in fiscal 2001. It is important to note, however, that as the rate is changed, each additional penny produces less revenue than the preceding penny generates.

Overview

Utility taxes in Texas include the Public Utility Gross Receipts Assessment, the Gas and Water Utility Tax, and the Gas Utility Pipeline Tax.

The Public Utility Gross Receipts Tax

The public utility gross receipts tax was enacted in 1945 at 1/6 of 1% of gross receipts. Since its enactment, the Public Utility Gross Receipts Assessment has not had a rate or base change. There are no exemptions to this tax and the net collections are allocated to the General Revenue Fund.

The Gas, Electric and Water Utility Tax

The Gas, Electric and Water Utility Tax was enacted in 1907 at 0.0% for cities with populations of 1,000 to 2,499, at 0.5% for cities with populations of 2,500 - 9,999 and at 1.0% for cities with populations over 9,999. Since its enactment, this tax has undergone four rate and base changes. There are no exemptions to this tax and the net collections are allocated to the Foundation School Fund at 25% and to the General Revenue Fund at 75%.

The Gas Utility Tax

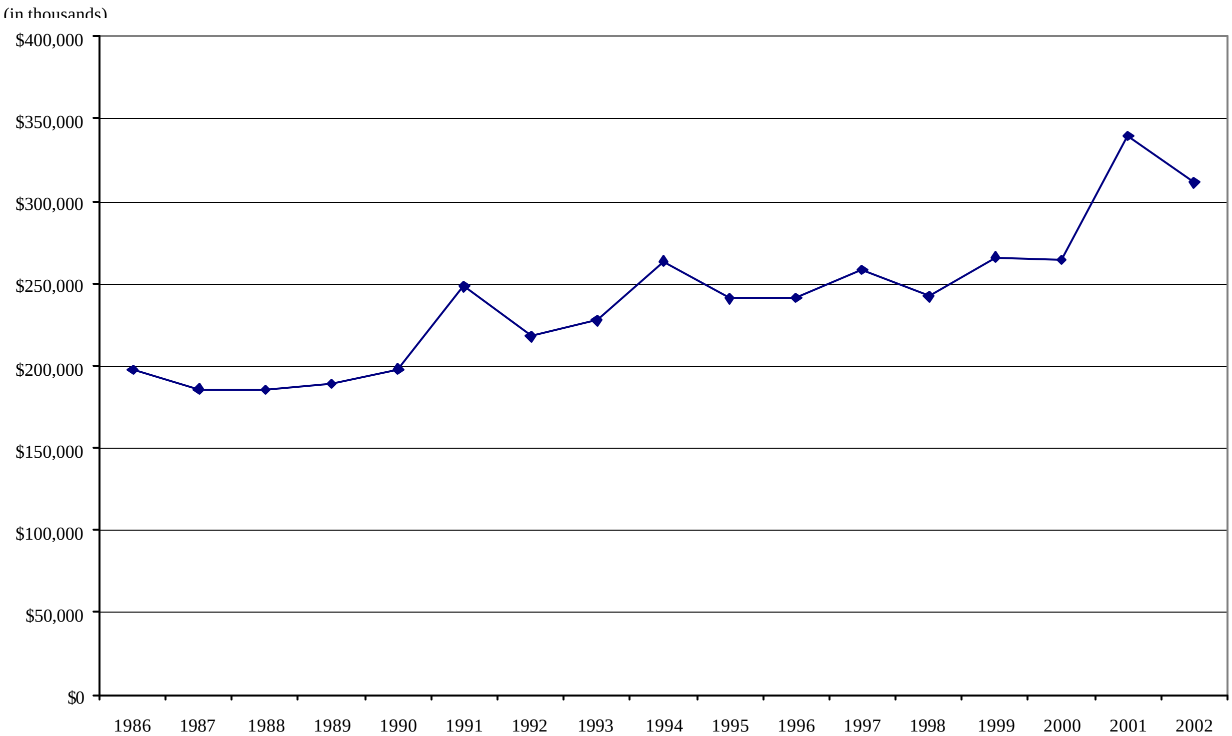
The Gas Utility Tax was enacted in 1920 at .25% of gross receipts. Since its enactment, this tax has undergone one rate and base change. There are no exemptions to this tax and the net collections are allocated to the General Revenue Fund.

Texas Utility Tax Collections Over Time (1986-2002)

Hotel Occupancy Tax

Hotel and Motel Tax Facts	
Date State Hotel Occupancy Tax Was Enacted	1959
Rate When Enacted	3%
Current State Rate	6% of room rate paid by occupant
Last Changed	1987
2001 Net Revenue	$246.8 Million
2002 Net Revenue	$230.9 Million
Estimated Average Revenue Per Penny Increase*	$41 Million
2004-05 revenue generated from a .25% Increase	$20.4 Million

Texas Utility Tax Collections
1986-2002



* Each of the 6 pennies that make up the current tax rate produced an average of $41 million in revenue in fiscal 2001. It is important to note, however, that as the rate is changed, each additional penny produces less revenue than the preceding penny generates.

Overview

The State Hotel Occupancy Tax was enacted in 1959 at 3% of the room rate paid by the occupant. Since its enactment, it has undergone two rate and base changes. Currently the tax is imposed on a person who pays for a room or space in a hotel costing $2 or more each day. Federal employees, long-term tenants and educational and religious organizations are exempt from the Hotel Occupancy Tax.

Local taxing authorities are also authorized to impose an additional local hotel tax.[174]

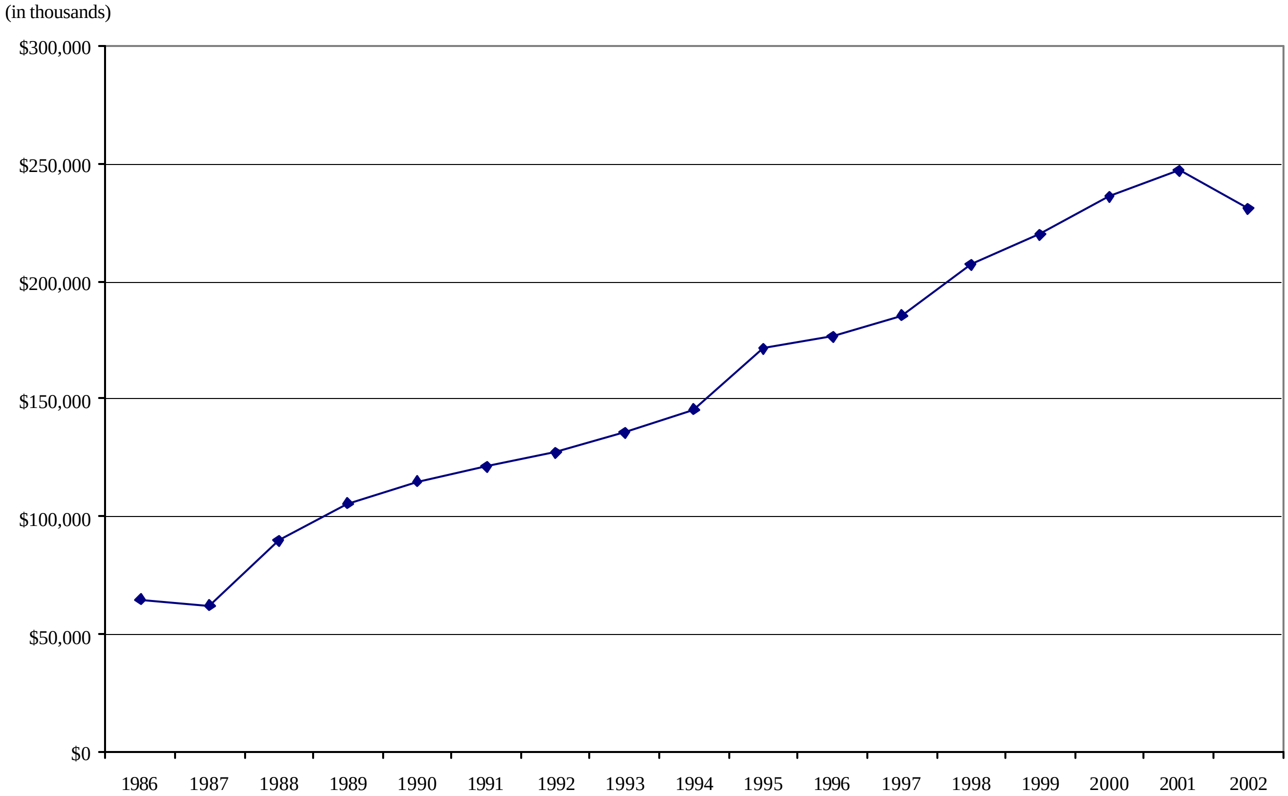
The county and city tax are collected by the local taxing authority.

Local Hotel Tax Facts		
	Counties	**Cities**
Date Hotel Occupancy Tax Was Enacted	1981	1971
Rate When Enacted	7%	7%
Current Rate (In addition to state rate)	Not to exceed 7% (8% in special cases)	Not to exceed 7% (9% in special cases)

Texas Hotel Occupancy Tax Collections Over Time (1986-2002)

[174]Texas Comptroller of Public Accounts, *Sources of Revenue Growth*, 2002.

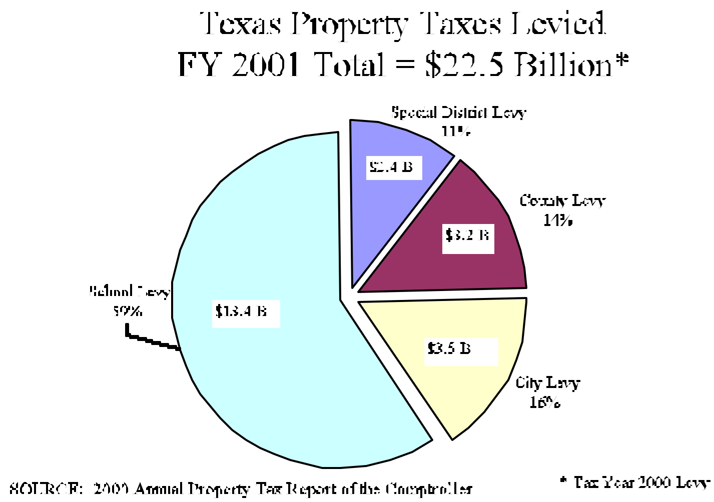
Texas Hotel Occupancy Tax Collections
1986-2002



91.67% of net collections are allocated to the General Revenue Fund and 8.33% to the Department of Economic Development Account.[175]

[175] Texas Insurance Code, Section 156.251 (a)

Property Tax



Overview

The Texas Constitution authorizes local governments to levy property taxes. Property taxes are levied by counties, cities, school districts, and special districts such as junior colleges, hospitals, rural fire districts, and flood control districts. School property taxes represent 59 percent of total property taxes levied.[176]

There is no state property tax, nevertheless, property taxes levied by school districts are important to the state because they help determine how much state General Revenue is sent to school districts to support public education.

It should be noted that the report submitted by the Joint Select Committee on Public School Finance will focus on the specifics of property taxes while this report will provide a brief overview of property taxes and address specific issues the Senate Finance Committee was asked to review.

[176] Texas Comptroller of Public Accounts*: Tax Exemptions and Tax incidences, A Report to the Governor and 77th Legislature*, 2001. Available at http://www.cpa.state.tx.us/taxinfo/incidence/school.html

Types of School Property Tax Levies in Texas

1. M&O: To cover maintenance and operating costs (M&O), and
2. I&S: To pay interest and sinking fund (I&S) debt service for financing building programs.

In 1999, the statewide weighted average M&O tax rate was $1.3848 per $100 valuation, and the I&S tax rate was $0.1560 per $100 valuation, for a combined statewide weighted average school tax rate of $1.5408 per $100 valuation.

All real and tangible personal property, unless required or permitted to be exempt by the Constitution, must be taxed in proportion to its value.

State taxes and local school tax values have risen substantially over the past several years. Local school taxes have increased from about 1.8 percent to about 2.3 percent of personal income.[177] In school year 1998-1999, local property taxes provided about 42.7 percent of public school funding, while the state's share was 39.2 percent. Other funding sources were the federal government, bond proceeds, and other minor sources.[178] In 2001, Texas school taxes increased more than 13 percent to reach $15 billion, as reported to the Comptroller's Property Tax Division by 1,034 independent school districts (ISDs). Texas business and residential properties paid almost equal shares of the total amount of school taxes, with businesses paying $6.9 billion and residential owners paying $7 billion.

Texas businesses paid almost 46 percent of 2001 local school taxes, about $694 million more than in 2000. Of all business properties, only the utilities' category experienced a tax decrease of almost $15 million.[179]

[177] Texas Taxpayers and Research Association, *Texas State Finances: The Current Picture*, June 2002.

[178] *Ibid*

[179] Carole Keeton Rylander, Comptroller of Public Accounts, 2001. Available at http://www.window.state.tx.us/taxinfo/proptax/stmt/stmt0205/

School Property Tax Collections 2000 to 2001[180]

Property Category	2000 School Taxes	% of Total	2001 School Taxes	% of Total	$ Change from 2000 to 2001
Residential Property					
Single-Family Homes	5,349,052,288	39.94	$6,168,813,110	40.83	$819,760,822
Multi-Family Residential	734,426,870	5.48	$820,830,720	5.43	$86,403,850
Residential Inventory	33,076,813	0.25	$50,704,338	0.34	$17,627,525
Subtotal, Residential	$6,116,555,971	45.67	$7,040,348,168	46.6	$923,792,197
Acreage/Lots					
Vacant Lots	362,911,605	2.71	$402,009,276	2.66	$39,097,671
Acreage	365,154,359	2.73	$375,830,689	2.49	$10,676,330
Farm and Ranch Improvements	227,718,402	1.7	$263,443,317	1.74	$35,724,915
Subtotal, Acreage/Lots	$955,784,366	7.14	$1,041,283,282	6.89	$85,498,916
Business Properties					
Commercial Real Estate	2,375,367,698	17.73	$2,621,397,117	17.35	$246,029,419
Commercial Personal	1,174,673,095	8.77	$1,253,195,870	8.29	$78,522,775
Industrial Real Estate	931,712,238	6.96	$1,028,551,949	6.81	$96,839,711
Industrial Personal	697,292,282	5.21	$769,134,760	5.09	$71,842,478
Oil & Gas	410,425,863	3.06	$613,446,419	4.06	$203,020,556
Utilities	618,892,126	4.62	$604,323,022	4	($14,569,104)
Special Inventory	36,317,428	0.27	$48,529,547	0.32	$12,212,119
Subtotal, Business	$6,244,680,730	46.62	$6,938,578,684	45.92	$693,897,954
Other Personal Property					
Vehicles	4,333,528	0.03	$3,261,345	0.02	($1,072,183)
Other Personal	72,669,446	0.54	$85,293,599	0.56	$12,624,153
Subtotal, Other Personal	$77,002,974	0.57	$88,554,944	0.59	$11,551,970
Total	**$13,394,024,041**	**100**	**$15,108,765,078**	**100**	**$1,714,741,037**

School Property Tax Exemptions

To receive most property tax exemptions, a person must file an application with the county appraisal district that serves the taxing units in which the property is located. If the property is in an area served by more than one appraisal district, a person must file the application in all affected appraisal districts, except for the residence homestead exemption application. The appraisal district will apply the exemption, when granted, in each of the taxing units in which the particular exemption is allowed and the property is located. For residence homestead exemptions, the homeowner may apply in the county appraisal districts in which the property is located.

[180] *Ibid*

Property tax exemptions include:[181]

1. Public property
2. Federal exemptions
3. Residence homestead
4. Personal property not used to produce income
5. Personal property income valued at less than $500
6. Mineral interest property valued at less than $500
7. Family supplies
8. Farm products
9. Implements of farming, ranching and timber
10. Cemeteries
11. Charitable organizations
12. Youth spiritual, mental, and physical development organizations
13. Private schools
14. Disabled veterans
15. Miscellaneous exemptions
    a. Veteran's organizations
    b. Federation of women's clubs
    c. Congress of parents and teachers
    d. Private enterprise demonstrations associations
    e. Bison, buffalo, and cattle
    f. Theater schools
    g. Community service clubs
    h. Medical center development
    i. Scientific research corporations
16. Historic or archaeological sites
17. Marine cargo containers
18. Freeport property-cotton stored in warehouse
19. School tax ceiling
20. Solar and wind energy devices
21. Abatements
22. Nonprofit water supply or wastewater service corporation
23. Pollution control property
24. Certain water conservation initiatives
25. Limitation on appraised value of residence homestead (10% cap)

[181] Comptroller of Public Accounts, Windows on State Government, 2001. Available at *http://www.window.state.tx.us/taxinfo/proptax/stmt/stmt0205/*

26. Productivity appraisals for agricultural and timberland
27. Tax increment financing

Estimated Cost Property Tax Exemptions

The estimated cost of all property tax exemptions for fiscal 2001 is $3.3 billion. This number is estimated to climb to $4.28 billion by fiscal year 2006. Listed below are the ten property tax exemptions with the highest estimated costs. (Refer to Appendix J for estimated costs of all property tax exemptions from 2001 through 2006).

School Property Tax Exemptions
Tax Year* 2001 to 2006
(in millions of dollars)

Item	2001	2002	2003	2004	2005	2006
Productivity value loss (Secs. 23.41, 23.52, 23.73 & 23.9803, Tax Code)	$ 1,162	$1,232.0	$ 1,306.5	$ 1,385.5	$ 1,469.4	$ 1,558.3
Residence Homestead: State mandated $15,000	$ 944.2	$ 982.3	$ 1,021.8	$ 1,063.0	$ 1,105.9	$ 1,150.4
Optional Homestead Percentage	$ 306.2	$ 330.0	$ 355.6	$ 383.2	$ 413.0	$ 445.0
65-and-over "tax freeze" on homestead	$ 288.9	$ 306.4	$ 324.9	$ 344.6	$ 365.4	$ 387.5
Residence Homestead: State mandated 65-and-over or disabled $10,000	$ 159.3	$ 165.7	$ 172.4	$ 179.3	$ 186.5	$ 194.1
Limitation on appraised value of homestead (10% cap)	$ 151.5	$ 160.7	$ 170.4	$ 180.7	$ 191.6	Not Available
Freeport Property	$ 101.4	$ 106.8	$ 112.6	$ 118.6	$ 124.9	$ 131.6
Residence Homestead: Optional over-65 or disabled	$ 79.0	$ 84.7	$ 90.9	$ 97.5	$ 104.5	$ 112.1
Pollution control property	$ 40.3	$ 42.2	$ 44.1	$ 46.2	$ 48.3	$ 50.6
Disabled veterans	$ 18.0	$ 19.0	$ 19.9	$ 20.9	$ 22.0	$ 23.1
Tax Increment Financing	$ 22.2	$ 20.9	$ 19.6	$ 18.4	$ 17.3	$ 16.3
Tax abatement	$ 25.5	$ 20.6	$ 16.6	$ 13.4	$ 10.9	$ 8.8
Solar and wind-powered energy devices	$ 1.5	$ 1.6	$ 1.6	$ 1.6	$ 1.6	$ 1.6
Historic sites	$ 0.9	$ 0.9	$ 0.9	$ 0.9	$ 0.9	$ 0.9

Property Tax and Business

Overview

Approximately 50% of all property taxes imposed are initially borne by business. The bulk of this is paid by manufacturers, transportation services, communications and utilities, and finance, insurance and real estate firms. Approximately three fifths of the property taxes paid by businesses is paid on the property they own other than land.[182] Thus capital intensive firms (agriculture, mining, manufacturing and utilities) tend to pay a proportionally higher tax burden than labor intensive firms.

Rendering of Business Property

Texas law requires businesses to declare their taxable personal property, items such as inventory, equipment, and machinery. However, many businesses do not report or render it. Businesses can misreport billions of dollars in taxable personal property by failing to provide tax appraisers lists of the property, by providing inaccurate lists or by simply not filing.

In 2001, $850 billion worth of business taxes were assessed by county appraisers, and $22.5 billion was collected. This is a collection rate of approximately 2.46%. In 2002, $866 billion was assessed, and using the same 2001 collection rate, potentially $23.39 billion could be collected. This is approximately $990 million more collected than last year..[183]

In 2001, 36 Texas appraisal districts sampled various properties by increasing the value of those properties and forcing them to come in and appeal the assessed value. On average, the property value not rendered was estimated to be $36 billion.[184] Based on historical ratios between overall value and property tax levy, the tax system is losing an estimated $900 million in property tax revenues.

It appears that the property tax system will be required to produce more revenue in the near future in order to more adequately fund public education in Texas.

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[182] Texas Taxpayers and Research Association, *Texas State Finances: The Current Picture*, June 2002

[183] Austin American-Statesman, *Business Loophole on Personal Property Costs Texas Taxpayers,* May 19, 2002.

[184] Austin American Statesman, *Fixing business taxes will pay off for Texas,* September 22,2002.

Options to collect taxes not being rendered by businesses

The rendering of business property taxes is considered to be an equity issue -- businesses that render pay the tax and those that do not evade the tax. Listed below are legislative options to remedy this problem. The intent of this section is to list possible options and in no way represents an endorsement of any of the specific methods by the Senate Finance Committee or its individual members.

1. Make the rendering of business property mandatory.

2. Pass a full sales disclosure law which would require all sales prices to be given to appraisal districts as well as the Comptrollers Property Tax Division, but otherwise kept confidential. This information would allow appraisal districts to more accurately appraise property since sales are the primary evidence needed in the appraisal process. Confidentiality would also allow the Comptroller's Property Tax Division to test appraisal districts without having to use information supplied to them by the appraisal districts.

3. Require businesses to provide rendered value based on approved statutory methods. Additionally, there should be in place exemptions to protect small business operators.

4. Allow appraisal districts to impose civil penalties on businesses that fail to render. This includes adding a provision which states if a business fails to render by a specific date, they waive certain rights to contest the appraiser-assessed value. This could include monetary and administrative penalties including but not limited to waiving right to contest values or waiving right to collect attorneys fees.

A Flat Tax

Texas is one of seven states without a personal income tax. However, in order to address questions posed about the estimated monetary value of personal income in Texas, the Committee includes this section for informational purposes only.

One question asked of the Senate Finance Committee is what a flat tax piggybacked on the Federal Income Tax would generate in revenue for the state of Texas. In 1999, the adjustable gross income for Texans totaled $380 billion while taxable income was $277 billion.[185] The following table estimates the amount of revenue that would be generated if a flat tax was based on Texans 1999 total taxable income.

Estimated Revenue Generated from a Flat Tax	
Percent of Texas 1999 Taxable Income	**Amount Generated for the State of Texas**
0.25%	$692.5 million
0.50%	$1.4 billion
1%	$2.8 billion
3%	$8.3 billion
5%	$13.8 billion
8%	$22.2 billion

To this point, this report has focused on the collection of tax revenue. One of the most important issues, if not the most important, that the Legislature will be facing in 78th Legislative session is the budget and whether or not the tax revenue discussed throughout this report will be adequate enough to cover spending demands.

[185] Internal Revenue Service, 2002

The Budget Today

The Legislature will convene in January 2003 to write the state budget for the 2004-05 biennium. Comptroller Rylander has warned that lawmakers next session could face a revenue spending gap in excess of $5 billion.[186]

There are concerns about the effect that the economic slowdown has had on revenue collections and there is a risk that the continued slowdown will drive the current state budget into a deficit. Another contributing factor to Texas' possible budgetary problems is ever increasing demands for services, many of them mandated by federal law. Current population and cost estimates put several state and federal programs over budget, including the Children's Health Insurance Program and Medicaid.[187]

These serious budget issues are not unique to this day and time, nor are they unique to Texas. This sentiment was best articulated by the late George Christian. "In 1949, when I was a young reporter covering the 51st Texas Legislature, the principal issues were public education, health care and transportation. In 2003, more than a half -century later, the principle issues for the 78th Legislature will be public education, health care and transportation. Goals change, and so do the faces, but our leaders must grapple with the same compelling issues."[188]

Many states are facing deficits for the current fiscal year. The sections that follow are an attempt to document the problems facing other states and the methods used in those states to address the issue. As you will see, other states have used a variety of methods including spending cuts, tax law changes and others.

What Revenue Generating Choices Do States Have in Slowing Times?

Ten years ago, shortfalls in state budgets were 6.5 percent of revenues, and 35 states cut their budgets. Now, 45 states expect shortfalls in their FY 2002 budgets; these shortfalls are estimated to

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[186] Carole Keaton Rylander, *Comptroller of Public Account, Rylander Certifies Budget; Warns of Potential $5 Billion Shortfall Next Session,* June 6, 2002.

[187] Health and Human Service Commission, 2002.

[188] Austin American Statesman, *In Retrospect; At 75, former LBJ aid George Christian Shares memories of remarkable life deeply rooted in the city and state of his birth, and voices confidence in the future of his country,* March 31, 2002.

be close to $40 billion, or 7.8 percent of estimated total general fund revenues.[189]
These circumstances are forcing states to re-evaluate both their revenue and expenditures. States are faced with tough choices. Typically in periods of recession, states cut expenditures, streamline via management strategy, devolve programmatic and fiscal responsibilities to local governments, and turn to revenue raising tactics.

To get out of this budget problem, 36 states have either made budget cuts, frozen spending, or have plans to do so. States could also raise taxes, but analysts say few lawmakers will try.[190]

Tax Revenue Sources Indicated as Top Three by States[191]

For most states, the top tax sources today are general sales, individual income tax, and motor fuels taxes. Although tax structures in different states vary greatly, the table below shows that the majority of states depend upon a very similar mix of taxes.

State Tax Revenue Sources		
1996	**Tax Source**	**2000**
44	General Sales and Gross Receipts	45
40	Individual Income Tax	41
29	Motor Fuels Tax	28
16	Corporate Net Income Tax	12
5	Other selective Sales Tax	8
4	Property Tax	6
3	Severance Tax	3
2	Motor Vehicles Licenses	2
2	Corporate and Other Licenses	2
1	Amusement Sales Tax	1
0	Documentary & Stock Transfer Taxes	1
0	Public Utilities	1

Upon slipping into a recession, 19 states cut $1.9 billion from their 2001 budgets. Strategies to close

[189] National Association of State Budget Officers (NASBO), *Fact Sheet: Quick Rebound? State Fiscal Recovery Could Be Gradual, Lag National Economy 12-18 Months.* (March 12, 2002). P.2 at *http://www.nasbo.org/Publications/PDFs/reboundlag.pdf.*

[190] Taxes& Budget, *State Line.org* Located at www.stateline.org.

[191] The Journal of State Government, *State Revenue Choices in Slow Times*, Spring 2002.

budget gaps included across-the-board cuts (10 states), dipping into rainy day funds (4 states), and a negligible use of layoffs, early retirement, and program reorganization.[192]

In addition to making budget cuts, states are faced with engineering effective revenue generating strategies. The table below generally reflects states efforts to jumpstart their economies by providing more ways for the public to keep more money in its pockets.

Tax Initiatives Mentioned in 2002 Governors' Addresses[193]

Governor's 2002 Tax Initiatives to combat Budget Deficits	State
Find new revenues	AK, KS, TN
Create earmarked revenues	CO, FL
Resumption/increase of income tax	AK, IN
Increase or create tax credits	KS, MA, RI, WV
Increase sales tax	KS, IN
Increase motor fuels tax	KS
Increase one or more "sin" taxes	AK, HI, IN, KS, MO, OR,
Increase to create fees	AK, KS, OR, WY
Expand gaming or lottery	KS, MO
Eliminate tax credits	WV
Reduce sales tax rates, but broaden the base	FL
Reduce unemployment insurance tax	WY
Reduce or eliminate fees	WV
Reduce property tax	GA, ND
Sales tax holiday or tax amnesty	GA, MO, WV
Create or increase tax credits	KS, MA, RI, WV
Income tax cut or other change (no Increase)	NM, PA
Restructure or streamline tax system	MO, OK
Redirect revenue	CO, MS, NE, OR, SC, WY

[192] *Ibid*

[193] *Ibid*

State Tax Cuts Resulting in Revenue Losses

In 2001, nine states made sales tax changes that are estimated to realize $119.5 billion in revenue losses for 2002. Fourteen states made individual income tax changes resulting in estimated revenue losses of $925.2 million. Nine states changed their corporate income tax laws to forego an estimated $151.4 million in 2002, while seven states made changes to realize an increase in such revenues by $533 million.[194]

2001 State Revenue Raising Tactics

The most popular revenue-raising tactic seems to be increasing "sin" taxes. The cigarette tax has become a quick fix for states that are struggling to make ends meet in a slumping economy. Sixteen states have either passed or already enacted cigarette tax increases in 2002, seven of which went into effect July 1, 2002. In New York City, smokers had been paying 8 cents a pack, but are now paying $1.50 a pack. The per-pack price of some premium brands jumped to more than $7. Even Indiana, long a bastion of cheap cigarettes because of its lower taxes, raised it tax-per-pack by 40 cents.[195]

Options States Face

The intent of this section is to list possible options and in no way represents an endorsement of any of the specific methods by the Senate Finance Committee or its individual members. State governments are in a precarious situation, facing difficult budget issues. Governors or legislatures are faced with the few following choices:

1. Reduce spending and leave current tax sources alone.

2. Seek various avenues of funding i.e., by increasing sin taxes, by imposing sales taxes on services, and by adding new or increasing current fee charges.

3. Continue aggressive appeals for federal funding.

4. Make more calculated use of debt.

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[194] *Ibid*

[195] Chicago Tribune, *Tax Increases Squeeze Smokers*, 07/01/02.

5. Remain aware of federal deliberations about electronic commerce and taxing remote sales as well as federal income tax changes.

Options for the Texas Legislature During the 2003 Session

Texas is facing a potential revenue shortfall for the next biennium. Like many of the states mentioned in this report, the Texas Legislature will be forced to look at all aspects of Texas taxes. Texas can employ a variety of cost savings measures such as accounting changes, tax changes, or expanded gaming to name a few options. These are all areas where the 78th Legislature must make choices. For the purposes of this report, we will only discuss options relating to the charge. Listed below are all of the options mentioned in this report.

The intent of this section is to list possible options and in no way represents an endorsement of any of the specific methods by the Senate Finance Committee or its individual members.

Options

When looking at any type of tax changes, the Legislature should examine approaches that would provide tax relief without requiring Texans to pay more in federal and state taxes or giving substantial tax breaks to non-Texans.

1. Sales Tax - p.49

   a. Examine and re-evaluate the sales tax base

   b. Extend the sales tax base to include selected items not currently taxed

   c. Extend the sales tax base to include selected services not currently taxed

   d. Examine and re-evaluate specific sales tax exemptions, exclusions, special rate, deductions and discounts.

2. Franchise Tax - p.-80

   a. Examine and assess Franchise tax loopholes

   b. Close the “Delaware Sub” loophole

   c. Extend the Franchise tax to partnerships

d. Require corporations to determine their state franchise tax liability using combined reporting

3. Property Tax - p.122

a. Make the rendering of business property mandatory.

b. Pass a full sales disclosure law which would require all sales prices to be given to appraisal districts as well as the Comptrollers Property Tax Division, but otherwise kept confidential. This information would allow appraisal districts to more accurately appraise property since sales are the primary evidence needed in the appraisal process. Confidentiality would also allow the Comptroller's Property Tax Division to test appraisal districts without having to use information supplied to them by the appraisal districts.

c. Require businesses to provide rendered value based on approved statutory methods. Additionally, there should be in place exemptions to protect small business operators.

d. Allow appraisal districts to impose civil penalties on businesses that fail to render. This includes adding a provision which states if a business fails to render by a specific date, they waive certain rights to contest the appraiser-assessed value. This could include monetary and administrative penalties including but not limited to waiving right to contest values or waiving right to collect attorneys fees.

4. Cigarette Tax - p.98
The intent of the cigarette options is to look at the amount of revenue that could be realized through various changes and in no way represents an endorsement of any of the specific methods by the Senate Finance Committee or its individual members**.** Shown below are additional specific 2004-05 revenue estimates.

a. Imposing a cigar tax at the rate of "other tobacco products" (OTP) tax of 35.213 percent of the manufacturer's list price would raise $19 million.

b. Imposing on all tobacco products other than cigarettes, a tax of 40 percent of the manufacturer's list price would raise $26 million.

c. Imposing on all tobacco products, including cigarettes, a tax of 35.213 percent of the manufacturer's list price would raise $248 million.

d. Imposing on all tobacco products, including cigarettes, a tax of 40 percent of the manufacturer's list price would raise $300 million.

Local Taxes

Overview of Local Taxes in Texas

Texans pay a multitude of different taxes to different levels of government, ranging from the federal income tax to the state gasoline tax to the local sales taxes. The purpose of this section is to provide an overview of taxes imposed by local governmental jurisdictions in Texas.

Local taxing jurisdictions in Texas consist of 254 counties, 1,034 school districts, 1,193 incorporated cities, and over 1,200 special-purpose districts.[196] The two main taxes imposed by local jurisdictions are the property tax (often referred to as an ad valorem tax in state law) and the local sales tax. Cities and counties may also impose a hotel occupancy tax. The number of jurisdictions that impose each of these taxes is shown in the table below.

LOCAL TAXING JURISDICTIONS IN TEXAS

		Number of Active Jurisdictions With		
Type of Jurisdiction	**Total Jurisdictions**	**Property Tax (2000)**	**Sales Tax '(2001)**	**Hotel Occupancy Tax (2001)**
Counties	254	254	121	20
Cities[1]	1193	1012	1117	392
School Districts	1034	1034	0	0
Transit Providers	8	0	8	0
Special Districts, Total[2]	1245	1179	75	5
Type of Special District:				
Community College Districts	64	64	0	0
Crime Control Districts	28	0	28	0
Development/Improvement Districts	25	12	13	0
Emergency Services Districts	67	67	5	0
Fire Control Districts	125	125	0	0
Hospital Districts[3]	127	127	8	0
Health Services Districts	10	0	10	0
Library Districts	10	1	10	0
Water-Related and Conservation-Related Districts	763	763	0	0
Other	26	20	1	5

[1] Number of cities from 2000 Census. Not all cities levied a property tax or a sales tax for the specified year.

[2] Special district counts include only active taxing districts that imposed either a sales tax or a property tax.

[3] Does not include hospital authorities created under Chapters 262 and 264, Health and Safety Code. These do not have taxing authority.

[196] Jurisdictional counts are as of 2000.

The taxing authority of all local governments is spelled out in the Texas Constitution and state law. Home-rule municipalities may impose other taxes not prohibited by any other law. The statutory authority for local jurisdictions to impose taxes is shown in the Constitutional/Statutory Authority and Allowable Tax Rates For Major Taxes Imposed by Local Jurisdictions in Texas Table in Appendix S.

In 1998-1999, the most recent year for which comprehensive data is available, taxes constituted about 39 percent of total revenue of local governments in Texas. Property taxes represented about 80 percent of total local government tax revenue, while sales taxes represented about 17 percent. [197]

Local Taxes

The following table shows sales tax and hotel occupancy tax collections for local jurisdictions for 2001 and property tax levies for 2000. (Property tax levies are not yet available for 2001). The property tax and the sales tax are the main sources of tax revenue for local governments.

LOCAL TAXING JURISDICTIONS IN TEXAS MAJOR TAX REVENUES

	Tax Revenues (million $)			**Per Capita Taxes**		
	Property	**Sales**	**Hotel Occupancy**	**Property**	**Sales Tax**	**Hotel Occupancy**
Type of Jurisdiction	**Taxes (2000)**	**Taxes (2001)**	**Taxes (2001)**	**Tax (2000)**	**(2001)**	**Taxes (2001)**
Counties	**$3,200.9**	**$221.9**	**$21.4**	**$154**	**$38**	**cbe**
Cities	**$3,530.9**	**$2,693.7**	**$279.8**	**$227**	**$168**	**cbe**
Independent School Districts	**$13,392.3**	**-**	**-**	**$642**	**-**	**-**
Transit Providers	**-**	**$993.7**	**-**	**-**	**cbe**	**-**
Special Districts, Total	**$2,387.6**	**$97.8**	**na**	**cbe**	**cbe**	**na**
Type of Special District:						
Community College Districts	$567.2	-	-	cbe	-	-
Crime Control Districts	-	$63.8	-	cbe	cbe	-
Emergency Services Districts	$44.7	$1.1	-	cbe	cbe	-
Fire Control Districts	$20.1	-	-	cbe	-	-
Hospital Districts	$1,063.3	$16.2	-	cbe	cbe	-
Health Services Districts	-	$3.1	-	cbe	cbe	-
Development/Improvement Districts	$10.5	$9.4			cbe	
Library Districts	$0.2	$3.0	-	cbe	cbe	-
Water-related and Conservation-related Districts	$680.5	-	-	cbe	-	-
Other	$1.1	$1.2	na	cbe	cbe	na
na: Not readily available.						
cbe: Cannot be estimated. Population estimates for districts are not available.						

[197] U.S. Census Bureau, *Federal, State, and Local Governments, State and Local Government Finances: 1998-99*. Available at http://www.census.gov/govs/www/estimate99.html. Other major components of local governments' revenues in that year were intergovernmental transfers and fee revenues.

Property Tax

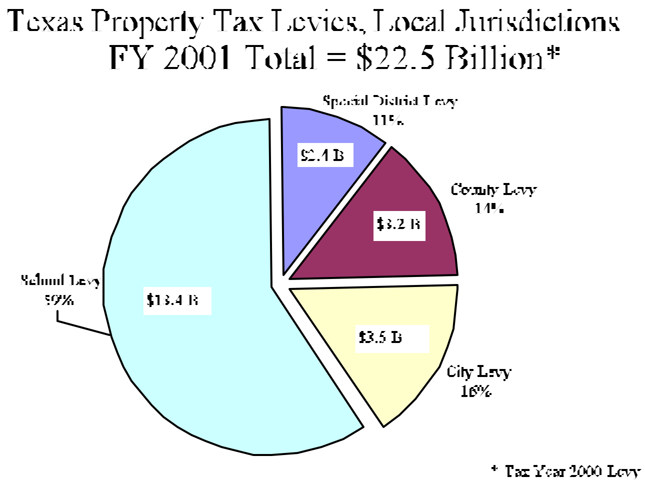
The Legislature does not have the constitutional authority to levy a state property tax.[198] The only allowable property taxes are property taxes levied by local jurisdictions.

All privately owned property in Texas, whether located in a big city or a sparsely populated rural area, is subject to property taxation by the county and school district in which it is located, unless specifically exempted by the Texas Constitution. However, most private property owners in the state pay property taxes to additional local jurisdictions. For example, in addition to county and school district property taxes, private property in a large city might be subject to city property taxes, hospital district property taxes, and junior college district property taxes.

Property tax revenues are the major tax revenue source for cities, counties, school districts, and many special districts.[199] In 2000, total property tax levies by local jurisdictions amounted to $22.5 billion. As shown in the figure below, 59 percent of this amount—$13.4 billion—was levied by school districts. Per capita levies ranged from $642 in school districts to $154 in counties.

[198] Article VIII, Section 1-e, Texas Constitution.

[199] Although some special districts only have sales tax authority, property taxes are the primary tax revenue source for special districts taken as a whole. Over 60 special districts impose a sales tax only.



Exemptions from property taxes are governed by the constitution and state law, and local jurisdictions do not have the authority to grant or deny an exemption unless permitted to do so by the constitution or by law.

The annual property tax cycle in Texas begins on January 1 of each year. County appraisal districts determine the value of properties, and local jurisdictions set the tax rates. Each appraisal district sets property values as of January 1 and sends those values to each local jurisdiction that levies taxes on property appraised by the appraisal district. The governing body of each local jurisdiction sets the tax rates for that jurisdiction that, when applied to property values, will generate the needed property tax revenues. The annual property tax levy in any jurisdiction is derived by multiplying the total taxable value in the jurisdiction by the total tax rate. The total tax rate may include a rate for debt service payments—often called the "I&S rate" or interest and sinking fund rate—and a rate for day-to-day maintenance and operations—the "M&O rate." Districts that do not have outstanding debt do not levy a debt service tax. Some special districts with other revenue sources do not levy a maintenance and operations tax.

Each taxing jurisdiction sends a property tax bill to each nonexempt property owner in the jurisdiction in the fall. A local taxing jurisdiction may collect its own taxes or may contract with another governmental jurisdiction or, for delinquent taxes, with a private entity to collect its taxes. Property tax collection operations tend to be consolidated in appraisal district offices and county tax offices.[200]

Sales and Use Tax

The sales and use tax (referred to herein as "sales tax") consists of both state and local taxes. The state sales tax rate is 6.25 percent of the sales price of taxable goods and services, and this rate is uniformly applied to taxable transactions throughout the state. Local jurisdictions, including cities, counties, and some special districts, may also impose a local sales tax after voter approval, but the aggregate local sales tax rate may not exceed two percent anywhere in the state. The maximum sales tax paid on a taxable item anywhere in Texas is 8.25 percent.

The imposition of a local sales tax must be approved by the voters residing in the jurisdiction in which the sales tax is to be imposed. Local sales tax revenues can be used for a variety of purposes, including general fund purposes, property tax relief, health care for the indigent, crime control, economic development, support of public libraries, emergency services, street maintenance, and support of public transit. Because of the variety in local sales tax options, not all Texans pay an 8.25 percent sales tax. Some might pay only a 6.75 percent rate; others might pay a 7.75 or 8.0 percent sales tax rate, depending on where they purchase a taxable item. This variation reflects the different kinds of services and levels of services approved by the voters to be funded by local sales taxes.

Cities may levy a local sales tax of up to two percent; counties, up to two percent; transit authorities, up to one percent; and special districts, up to two percent. State law governs the order in which these taxes take effect, so as not to exceed the two percent cap on the sum of all local sales taxes at any location in the state.

In 2001, local jurisdictions collected $4 billion in sales taxes. City sales taxes accounted for almost two-thirds of this amount. The relative shares of cities and other local jurisdictions are shown in the figure below.

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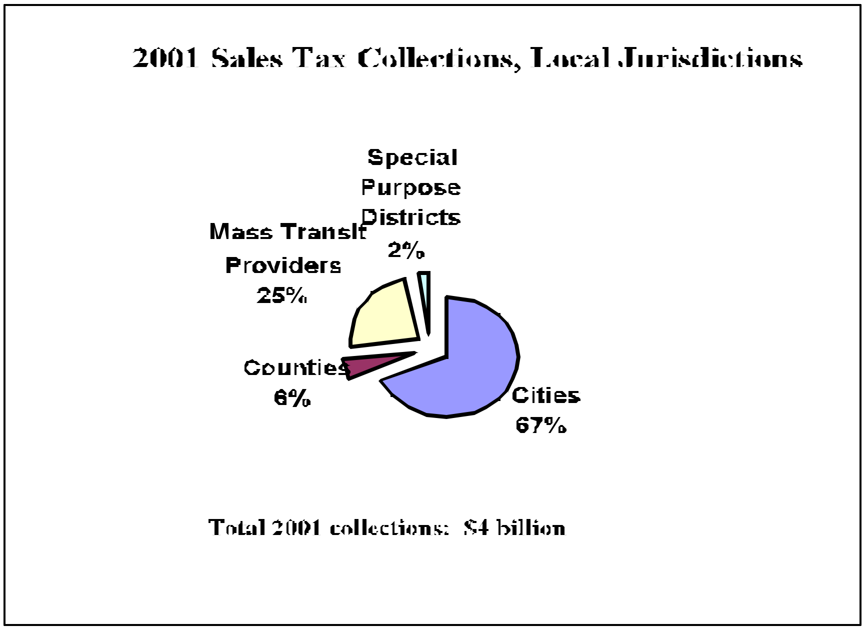
[200] Consolidated property tax collection information is available in Texas Comptroller of Public Accounts, *Texas Property Tax Annual Property Tax Report, Tax Year 2000,* Appendix G.



Local jurisdictions' authority to impose a sales tax is governed by state law. In general, items that are subject to the state sales tax are also subject to the local sales tax, and items that are exempt from the state sales tax are also exempt from the local sales tax. The taxation of a few items, such as the residual use of electricity, natural gas, and certain telecommunication services, may be subject to local option.

Sales taxes, both state and local, are collected by the retailer or other entity providing the taxable good or service and remitted to the Comptroller, either monthly, quarterly, or annually, depending on the amount of the collected. The Comptroller then remits to each local jurisdiction its share of sales tax collections for that period.

Hotel Occupancy Tax

The state hotel occupancy tax is six percent of the price of a hotel room costing at least $2 per day. "Hotel" is defined as a building that offers sleeping accommodations to the general public and includes hotels, motels, tourist homes, lodging houses, rooming houses, and bed and breakfasts.[201] Stays of at least 30 consecutive days are exempt from the tax.

[201] § 156.001, Tax Code.

All cities and some counties are eligible to adopt a hotel occupancy tax. Adoption of a hotel occupancy tax by a city or county requires a majority vote to adopt by the governing body, but it does not require voter approval. Hotel occupancy tax revenues must be used to directly promote tourism and the convention and hotel industry. Specifically, revenues must be used for a convention center, tourism advertising and promotion, programs to enhance the arts, and historic preservation projects that promote tourism. Tax revenues may not be used for general revenue purposes or activities not directly related to promoting tourism.[202]

In addition to the general hotel occupancy tax, cities, counties, and sports and community venue districts may impose a separate hotel occupancy tax to finance sports and community venue projects. Adoption of this tax requires voter approval. Finally, counties that have created county development districts may impose a hotel occupancy tax in the district and use the proceeds for district purposes. An election is not required to impose this tax.

Hotel occupancy taxes are collected by the hotels and remitted to the state and, if applicable, directly to cities and counties imposing a local tax.

[202] § 156.001, Tax Code.

Local Taxing Jurisdictions: Counties

All Texas Counties may levy a property tax or a sales tax, while several may also impose a hotel occupancy tax. In 2001, all 254 counties levied a property tax, 121 imposed a sales tax, and 20 imposed a hotel occupancy tax.[203]

County Property Taxes: The main source of tax revenue for counties is the property tax. For the tax year 2000, the state's 254 counties collectively levied $3.2 billion in property taxes, an average of $154 per person.

County Sales Taxes: Counties that are not located in a transit authority may impose a sales tax for property tax relief with voter approval. The county sales tax rate for property tax relief is one-half percent; the rate is one percent in a county with no territory in a city. In 2001, 121 counties imposed a sales tax for property tax reduction. The 2001 sales tax revenues for these 121 counties totaled $221.9 million, or $38 per capita.

Counties that meet one of various sets of population criteria may also impose a sales tax to support specific services. Certain small counties may impose a sales tax to support a health services district, a county development district, a landfill, or a criminal detention center. Large counties and most cities may impose a sales tax to support the operations of a crime control and prevention district. Some of these districts are discussed below under Local Taxing Jurisdictions.

County Hotel Occupancy Taxes: The conditions governing county eligibility to adopt the general hotel occupancy tax are more restrictive than those for cities. By law, counties must meet certain geographical or population criteria before they are eligible to adopt a hotel occupancy tax. The geographical criteria pertain to counties bordering Mexico, the Gulf of Mexico, and the Edwards Aquifer Authority. Population criteria range from county population to size of city located in a county bordering Mexico to the absence of a municipality in the county. The Texas Department of Economic Development has estimated that only 48 counties are eligible to adopt a general hotel occupancy tax.[204]

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[203] Texas Attorney General, *Handbook on Economic Development Laws for Texas Cities, 1999 Edition*, Chapter IV, "Economic Development Through Tourism, The Local Hotel Occupancy Tax." Available at http://www.oag.state.tx.us/AG_Publications/txts/econ_dev1.htm.

[204] Since there is no central repository of locally imposed hotel occupancy taxes, the figure for the number of counties imposing occupancy taxes is an estimate of the Texas Department of Economic Development. See Texas Department of Economic Development, Market Texas Tourism and Department of Recreation, Park and Tourism

As noted above, 20 counties imposed a hotel occupancy tax in 2001. County tax rates ranged from one percent (Webb County) to eight percent (unincorporated parts of Harris County). Total tax revenues amounted to $21.4 million. Harris County hotel tax revenues accounted for $17.3 million, 80 percent of the total.

Local Taxing Jurisdictions: Cities

Cities by statute may impose a property tax, a sales tax, a hotel occupancy tax, and a few other taxes. Home-rule cities may impose any other tax consistent with their charters if not prohibited by state law.

City Property Taxes: In 2000, 1,012 Texas cities collected approximately $3.5 billion in property taxes, which amounted to $227 per capita. Property tax rates ranged from $1.50 per $100 valuation to $0.019 per $100 valuation. The average tax rate was $0.47 per $100 valuation. The average tax rate in the 24 cities of at least 100,000 population was $0.59 per $100 valuation.

City Sales Taxes: As noted above, cities may adopt sales tax rates of up to two percent with necessary voter approvals, as long as the sum of all local sales taxes does not exceed two percent at any location within a city's boundaries. There are five different sales taxes that a city may adopt:

1. Sales tax for general fund purpose: one percent
2. Additional sales tax for property tax reduction: up to one-half percent
3. Sales tax for street maintenance: one-fourth percent (expires in four years unless reauthorized by voters)
4. Sales tax for industrial and economic development: up to one-half percent
5. Sales tax for sports and community venues: up to one-half percent

With voter approval, a city may also pledge up to 25 percent of the revenue received from the one percent general-purpose sales tax and the additional sales tax for property tax reduction to the payment of obligations of sports and community venue projects located in the city. Some cities may also adopt a sales tax for public transit, emergency services, and municipal development. However, they may have to meet certain population criteria before adopting one of those taxes. As of 2001, 1,117 cities collected $2.7 billion in sales tax revenues, which is $168 per capita.

Sciences, Texas A&M University, *Texas Local Hotel Tax Report 2001*, October 2001, available at http://research.travel.state.tx.us/tourism/hotelmot/Tax_Report_File.pdf.

City Hotel Occupancy Taxes: Any home-rule or general-law city may implement a general hotel occupancy tax of up to seven percent of the price of a hotel room. Some cities can implement a higher rate. Hotel occupancy taxes can be imposed by action of the governing body of a city without voter approval. In 2001, 383 cities collected $280 million in hotel occupancy taxes.[205] Tax rates ranged from two percent in a few small cities (Broaddus, Eden, Paducah, Stratford, and Van) to nine percent in large cities (Dallas, Fort Worth, San Antonio, Austin, and Corpus Christi) and 13 percent in one city (Pearland). Most cities imposed a seven percent tax, including the city of Houston.

With one exception, there is no maximum combined rate of the state, city, and county hotel occupancy tax.[206] The one exception concerns the extraterritorial jurisdiction (ETJ) of cities under 35,000 population. Cities meeting this criterion may impose a hotel occupancy tax in their ETJ, but the combined state, city, and county rate may not exceed 15 percent in the ETJ.

Local Taxing Jurisdictions: School Districts

The sole local source of tax revenue for school districts is the property tax. In 2000, the statewide school district tax collected amounted to $13.4 billion, or approximately $642 per capita.

School district property tax exemptions, abatements, and other limitations on taxes or appraisals have a major impact on the state's general revenue fund through the school funding process. However, local school boards have no control over many of these exemptions, abatements, and other limitations that are mandated by the Texas Constitution or statute. In 2000, the value of mandatory exemptions, abatements, and other limitations for school district property taxes amounted to $112.2 billion, or approximately $28,000 per student.[207] (This figure is the exempt property value per student, not the tax levy loss per student.)

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[205] See Texas Department of Economic Development, Market Texas Tourism and Department of Recreation, Park and Tourism Sciences, Texas A&M University, *Texas Local Hotel Tax Report 2001*, October 2001, available at http://research.travel.state.tx.us/tourism/hotelmot/Tax_Report_File.pdf.

[206] Texas Department of Economic Development, Market Texas Tourism and Department of Recreation, Park and Tourism Sciences, Texas A&M University, *Texas Local Hotel Tax Report 2001*, October 2001, available at http://research.travel.state.tx.us/tourism/hotelmot/Tax_Report_File.pdf.

[207] Texas Attorney General, *Handbook on Economic Development Laws for Texas Cities, 1999 Edition*, Chapter IV, "Economic Development Through Tourism, The Local Hotel Occupancy Tax." Available at http://www.oag.state.tx.us/AG_Publications/txts/econ_dev1.htm.

Local Taxing Jurisdictions: Public Transit Providers

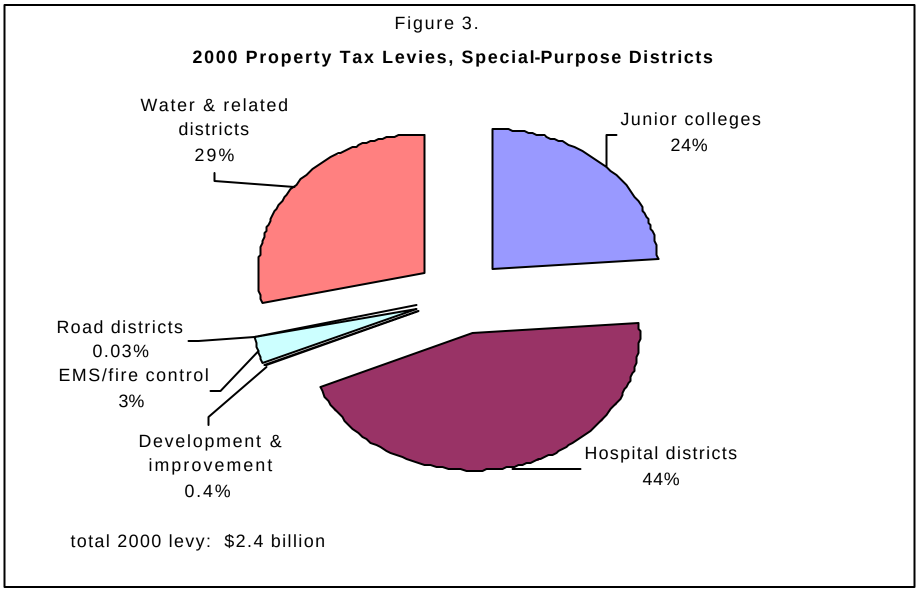
Texas has six regional transportation authorities and two city transit departments. Regional transportation authorities may impose a sales tax of up to one percent; city transit departments may impose a sales tax of up to one-half percent. All transit sales taxes must be approved by the voters.

Neither type of transit provider has the authority to levy a property tax.

The regional transportation authorities are located in the Austin, Corpus Christi, Dallas, Fort Worth, Houston, and San Antonio areas. The city transit departments imposing a sales tax are in El Paso and Laredo.

In 2001, sales tax revenues of the eight transit providers totaled nearly $994 million. Tax revenues of the Houston and Dallas transportation authorities amounted to $726 million, nearly 75 percent of the total sales tax collections of the eight transit providers.

Local Taxing Jurisdictions: Special-Purpose Districts



Special-purpose districts provide public infrastructure and various public services, ranging from the provision of water and water-related services to health services, libraries, community colleges, economic development, emergency medical services, fire control, and crime control. Since district residents often pay the taxes to support a district's provision of services, voters of a proposed district generally must approve creation of the district, along with the tax to be adopted and the proposed or maximum tax rate. Districts are usually governed by an elected board, such as a city council, commissioners court, or board of trustees, but in a few cases are governed by appointees of a city council or commissioners court.

Property taxes provide the bulk of special districts' tax revenues. In 2000, 1,179 special districts levied nearly $2.4 billion in property taxes, and in 2001, 75 districts collected approximately $98 million in sales tax revenue.[208] Twelve of the districts that imposed a sales tax also levied a property tax. These annual revenues are used to support district operations and to pay off district debt, which is incurred to build district infrastructure. As of 2000, the total outstanding debt (both general obligation and revenue-

[208] Calculated from property tax data in Texas Comptroller of Public Accounts, *Annual Property Tax Report, Tax Year 2001*, November 2001, p. B-104, and enrollment data in Texas Education Agency, *Snapshot 2000*, Winter 2001, p. 388. The $28,000 figure includes charter students and does not reflect property value losses from productivity valuation

supported) of special districts was $20.9 billion. About 75 percent of this debt was incurred by districts providing water and water-related services.

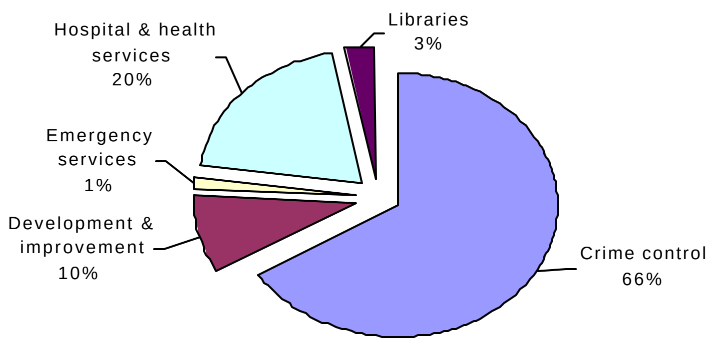
As noted earlier, the only special district that may impose a hotel occupancy tax is a sports and community venue district.

As shown in the graph above, hospital districts, junior college districts, and water-related districts together accounted for approximately 97 percent of the total 2000 special district property tax levy of $2.4 billion. Hospital districts levied $1.1 billion (44 percent of the total levy); water districts levied $680.5 million (29 percent); and junior college districts levied $567.2 million (24 percent).

The pie chart below shows the percentage distribution of the 2001 sales tax collections of $98 million among special districts. Crime control districts collected $64 million (66 percent) and hospital districts and health services districts collected $19 million (20 percent).

Figure 4.

2001 Sales Tax Collections, Special-Purpose Districts



total 2001 collections: $98 million

Special districts are mainly concentrated in metropolitan counties. In 2000, about 70 percent of the special districts that levied a property tax were in metropolitan counties; their combined levy amounted to over 90 percent of the total special district levy. A similar relationship holds for sales tax collections.

Junior College Districts

The creation and taxation authority of junior college districts is governed by Chapter 130 of the Education Code.

Junior college districts may be created by actions of school boards, county commissioners courts, or other local entities, which, after receipt of a petition and approval by the Texas Higher Education Coordinating Board, may call an election for creation of a junior college district. Taxing authority must also be approved by the voters. In 2001, about 45 percent of the nearly one million students enrolled in college or post secondary programs in Texas were in junior colleges.[209]

Junior college districts are funded by student tuition and fees, property taxes, state general revenue fund appropriations, and federal grants. As of the 2000 tax year, there were 64 junior college districts that collectively levied a total of $567 million in property taxes. Total tax rates ranged from $0.0178 per $100 valuation to $0.31 per $100 valuation. The average tax rate was approximately $0.10 per $100 valuation. The maximum property tax rate for junior college districts is $1 per $100 valuation, but no more than $0.50 of that rate may be used for debt service on bonds.[210] The election to approve the tax in each district may, and usually does, set a lower maximum tax rate.

Presently, no community college district had legal authority to impose a sales tax.

Local Taxing Jurisdictions Created to Provide Health Care

There are several different types of local entities that provide health care, including care to the indigent. These entities include hospital districts, hospital authorities, county hospitals, municipal hospitals, and joint municipal-county hospitals. They differ in two main respects: the source of local revenues to support their operations and the selection of oversight authorities.

Hospital Districts: Hospital districts are the only type of local health care jurisdiction that may impose taxes if approved by the voters. (Not all hospital districts levy property taxes or sales taxes.) Article IX of the Texas Constitution gives the Legislature the power to create hospital districts. Hospital districts are political subdivisions of the state and, depending on the statute under which they are created, may be governed by the county commissioners court or by an elected board of directors.
Districts may impose taxes (if approved by the voters) and may issue both tax-supported and revenue bonds. In 2000, property tax rates in the 127 hospital districts that levied a property tax averaged about

[209] The property tax data are from Texas Comptroller of Public Accounts, *Annual Property Tax Report, Tax Year 2001*, November 2001, p. 1. The sales tax data are available on the comptroller's website at http://ecpa.cpa.state.tx.us/allochist/allochist.htm.

[210] Percentage compiled from data in *Texas Almanac 2002-2003*, Dallas, Dallas Morning News, p. 525.

$0.22 per $100 taxable value, with rates ranging from about $0.01 to $0.75 per $100 taxable value. The total 2000 levy of hospital districts was approximately $1.1 billion.

In terms of the size of their 2000 property tax levy, the five largest hospital districts in the state were Harris County Hospital District, Dallas County Hospital District, Tarrant County Hospital District, Bexar County Hospital District, and R. E. Thompson General Hospital District in El Paso. Together, these five districts accounted for 85 percent of the total $1.1 billion hospital district levy in 2000.

Total bonded indebtedness of hospital districts increased from $399 million in 1999 to $444 million in 2001. Approximately $92 million of the $444 million was tax-supported debt.

As of May 2002, appraisal districts reported a total of 128 active hospital districts.[211]

With voter approval, hospital districts may also impose a sales tax of up to two percent for property tax relief. In addition, hospital districts in one or more counties each with a population of 75,000 or less may impose a sales tax for general purposes of up to two percent. As of October 2001, eight hospital districts imposed a local sales tax, with 2001 sales tax collections amounting to about $16.2 million.

County Health Services Districts: Counties with a population of 50,000 or less may call an election to adopt a sales tax of up to one-half percent to provide health services in the county. County health services districts are not independent taxing districts per se, since the county imposes the tax.

In 2001, sales tax revenues in 10 county health services districts amounted to $3.1 million. By law, these tax revenues may be allocated to a hospital authority, a hospital district, or a public health district, but they must be used to provide health services in the county.

Hospital Authorities: Hospital authorities do not have taxing authority. Their enabling legislation specifically denies taxing authority. They are mentioned here because they may be confused with hospital districts, which usually do have taxing authority if approved by the voters.

Hospital authorities may be created for the purpose of acquiring or operating one or more hospitals by either municipalities or counties under the provisions of Chapters 262 and 264, Health and Safety Code, respectively. An authority is governed by a board of directors whose members are appointed by the

[211] § 130.122(a), Education Code.

governing body of the sponsoring jurisdiction (either a municipality or a county). As of August 31, 2001, there were 39 active hospital authorities in Texas.[212]

Although hospital authorities do not have taxing authority, they may issue revenue bonds backed by revenues, fees, and liens on both real and personal property owned by the hospital authority. As of August 31, 2001, hospital authorities reported $595 million in outstanding debt.[213] Both their operating and debt service revenues come from fee-paying patients, federal and state funds, and funds from the city or county that created them.

Local Taxing Jurisdictions Created to Provide Public Safety Services

Emergency Services Districts: There are three different types of emergency services districts. Section 48-e, Article III, Texas Constitution, gives the Legislature the power to create emergency services districts and allow counties to levy a property tax up to $0.10 per $100 valuation to support a district if approved by the voters residing in the district. Districts may provide emergency medical and ambulance services, rural fire prevention and control, and other emergency services authorized by the Legislature.

Section 48-d, Article III, Texas Constitution, and Chapter 794, Health and Safety Code, govern the procedures for creation of rural fire prevention districts. A county commissioners court may call an election to create a district and approve a property tax at a rate not to exceed $0.03 per $100 valuation ($0.05 for districts wholly or partly within Harris County).

Fire control, prevention, and emergency medical services districts may be created pursuant to Chapter 344, Local Government Code. These districts may be created only by cities that meet certain population criteria. They may impose a sales tax of up to one-half percent with voter approval.

The total 2000 property tax levy for the 192 emergency services districts levying a property tax was $64.8 million. The 131 districts in metropolitan counties levied $59.3 million of this amount.

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[212] This information was reported to the comptroller's property tax division by Texas' 253 appraisal districts. Texas Comptroller of Public Accounts, *Texas Property Tax Appraisal District Directory, 2002 Edition*. This number may have changed since May 2002 due to district dissolution, creation, or consolidation.

[213] Number compiled from data available on the website of the Texas Bond Review Board at http://www.brb.state.tx.us/brbpages/db/db.html; select "Texas Health & Hospital Districts—FY 2001 data."

The 2001 sales tax collections of the five emergency services districts that imposed a sales tax were $2 million.

Crime Control and Prevention Districts: Chapter 363, Local Government Code, governs the creation of crime control and prevention districts. Counties of more than 130,000 population and cities in counties of more than 5,000 population may impose a sales tax of up to one-half percent to support a crime control district. Crime control districts do not have the authority to levy a property tax.

As of October 1, 2002, 28 crime control districts imposed a sales tax. Over half of these were in Tarrant County. Total 2001 sales tax collections of these 28 districts amounted to nearly $64 million which was operated by sales tax rates ranging from one-eighth percent to one-half percent.[214]

Local Taxing Jurisdictions Created to Provide Libraries

Chapter 326, Local Government Code, gives the commissioners court of a county of more than 100,000 population the authority to call an election to create and approve a sales tax rate for a library district proposed for the county. Library districts are governed by an elected board of trustees and may impose a sales tax of up to one-half percent if approved by the voters.

A library district may not include territory in more than one county, and it may not include territory in any municipality that operates a public library. As of October 1, 2002, 10 library districts imposed a sales tax. Sales tax rates in these districts ranged from one-fourth percent to one-half percent, and 2001 collections amounted to about $3 million.[215]

Local Taxing Jurisdictions Created to Provide Water and Water-Related Services

Texas has hundreds of local taxing jurisdictions whose main purpose is to provide water-related services to district residents. (Cities and counties may also provide water and water-related services, but this is not their main purpose.) Water districts include water improvement districts, water control and

[214] Number compiled from data available on the website of the Texas Bond Review Board at http://www.brb.state.tx.us/brbpages/db/db.html; select "Texas Health & Hospital Districts—FY 2001 data."

[215] Information compiled from the comptroller's website at http://www.cpa.state.tx.us/taxinfo/local/spd.html Data compiled from information available on the comptroller's website at http://www.cpa.state.tx.us/taxinfo/sales/index.html.

improvement districts, fresh water supply districts, municipal utility districts, municipal water districts/authorities, public utility districts, conservation and reclamation districts, drainage districts, flood control districts, levee improvement districts, and irrigation districts. Some development and improvement districts may also provide water-related services.

Water districts differ according to their constitutional and statutory authorization. All water districts are authorized by either Section 52, Article III, or Section 59, Article XVI, of the Texas Constitution. Section 52, Article III, provides for a limitation on the amount of bonds a district may issue, but does not limit the property tax to pay off the bonds. (The amount of bonds issued may not exceed one-fourth of the assessed value of real property in the district.) Section 59, Article XVI, does not limit the amount of bonds or the tax rate.

Title 4, Water Code, contains the general law applicable to water districts. In addition, there are numerous water districts created by or governed by local laws applicable to individual districts. Appendix S contains statutory references for the various water districts governed by general law.

Many water districts levy property taxes. For the 2000 tax year, 763 water districts located in 155 counties levied $680 million in property taxes. Harris County, with 305 water districts, had more than any other county in the state. The 2000 property tax levy of these 305 Harris County districts was about $353 million, slightly over half of the total levy of water districts.

As of October 1, 2002, no water district in the state imposed a sales tax.

Development and Improvement Districts

Texas law allows for the creation of numerous types of development and improvement districts for the general purposes of promoting economic development, improving public infrastructure, and improving the appearance of public areas. The law allows for both county and municipal development districts. Most are governed by the commissioners court or city council of the county or city in which they are located, or by an appointed board. The Legislature gave sales tax authority to some types of districts, and authority to levy a property tax or impose impact fees and assessments to others. However, some development and improvement districts have no authority to levy taxes or impose fees and assessments.

As of October 2002, 13 development and improvement districts imposed sales taxes with rates ranging from one-half percent to one percent. The 2001 sales tax collections of these 13 districts totaled $9.4 million. (Not all districts were collecting taxes in 2001.) Eleven of the 13 were in metropolitan counties.

Other Local Taxing Jurisdictions

There are other kinds of local taxing jurisdictions in addition to the ones discussed above. In 2000, there were 22 road and road utility districts, 18 navigation districts/port authorities, and 1 solid waste management district. Statutory references for these districts are provided in Appendix S.

The total property tax levies for these groups were:

- road and road utility districts: $871,000
- navigation districts/port authorities: $54.8 million
- solid waste management district: $246,000

As of October 1, 2002, none of these districts imposed a sales tax.

Appendices

Appendix A: Senate Committee on Finance Interim Charges

Charges from Lieutenant Governor William R. Ratliff to Senate Finance Committee on September, 2001. The Interim Committee on Demand was formed to answer charge 3 of the interim Finance Charges.

SENATE COMMITTEE ON FINANCE

Interim Charges

The Committee shall:

1. *Survey and assess Texas' current tax system, including taxation authority given to units of local government. The survey should identify the economic value associated with all current taxes, as well as current exemptions and abatements. The Committee's report should include the information provided by the survey.*

2. Study the issue of rising medical costs and its impact on the state budget, including health and human services, correctional managed health care, education and state employee benefits. The Committee may review private pay insurance. The Committee's report should recommend ways to control cost increases and identify best practices and opportunities for savings.

3. Evaluate the processes by which health and human services agencies assess the demand for services and allocate their appropriations to address program demands and requested rate increases.

4. Monitor the implementation of SB 813, 77th Legislature, the creation of the Spaceport Trust Fund.

5. Review the sources of revenue dedicated to the Crime Victims Compensation Fund and the purposes for which that Fund is expended. The Committee's report should recommend ways to ensure future revenues adequately address statutorily provided spending priorities.

6. Evaluate the infrastructure, capacity and funding of trauma care, and develop recommendations to address the state's trauma care needs.

Appendix A: Senate Committee on Finance Interim Charges Continued

Reports

The Committee shall submit copies of its final report as soon as possible, but no later than November 15, 2002. This date will allow the findings of the Committee to be considered when the Legislative Budget Board is developing performance and budget recommendations to the 78th Legislature. Copies of the final report should be sent to the Lieutenant Governor, Secretary of the Senate, Legislative Council and Legislative Reference Library.

The final report of the Committee should be approved by a majority of the voting members of the Committee and include any recommended statutory changes. Draft legislation containing recommended statutory changes should be attached to the report. Recommended agency rule changes should also be attached to the report.

Budget and Staff

The Committee shall use its existing staff and utilize the budget approved by the Senate Committee on Administration. Where appropriate, the Committee should obtain assistance form the Senate Research Center and legislative agencies, including the Legislative Budget Board, the Legislative Council, and the State Auditor. The Committee should also seek the assistance of appropriate Executive Branch agencies with responsibilities in the areas related to the Committee's interim charges.

Interim Appointments

Pursuant to Section 301.041, Government Code, it may be necessary to change the membership of a committee if a member is not returning to the Legislature in 2003. This will ensure that the work of interim committees is carried forward into the 78th Legislative Session.

Appendix B: Senate Committee on Finance December 5, 2001 Hearing Agenda

SENATE INTERIM COMMITTEE ON FINANCE

AGENDA

9:30 A.M., December 5, 2001
Capitol Extension, Room E1.036

I. Call to Order/Roll Call

II. General Comments from the Chair and Members

III. Discussion of Interim Charge #1, relating to a survey and assessment of Texas' current tax system.
   A. Overview of Texas Tax System
      1. Comptroller of Public Accounts - James LeBas

IV. Closing Comments

V. Other Business

VI. Recess

Appendix C: Senate Committee on Finance February 26,2002 Hearing Agenda

SENATE INTERIM COMMITTEE ON FINANCE

AGENDA

1:30 P.M., February 26, 2002
Capitol Extension, Room E1.036

I. Call to Order/Roll Call

II. General Comments from the Chair and Members

III. General Texas Business Taxes, including the Corporate Franchise Tax
A. Texas Strategic Economic Development Planning Commission Report - *Steve Stephens*
B. Texas Taxpayer's and Research Association - *Dale Craymer or Bill Allaway*
C. Industry Viewpoints on the Texas Tax System

1. Accountants
Texas Society of Professional Accountants - *Ira Lipstet*

2. Airlines
American Airlines - *Dan Hagan*
Continental Airlines - *Nene Foxhall*
Southwest Airlines - *Juan Ricks*

3. Chemical
TX Chemical Council - *Jim Woodrick*
Dow - *Ron Dipprey*
Dupont - *Greg Cardwell*

4. Health Care Industry
Robert Hogue, M.D.
Pat Carter, M.D.
Judson Somerville, M.D.

Appendix C: Senate Committee on Finance February 26, 2002 Hearing Agenda Continued

5. Insurance
   American Insurance Association - *Forrest Roan*
   Texas Association of Life and Health Insurers - *Will Davis*

6. Legal Profession
   Tax Attorney - *Cynthia Ohlenforst*

7. Oil/Gas
   EOG Resources - *Ed Segner*
   Hurd Enterprises - *JR Hurd*

8. Technology
   National Semiconductor - *Geoff Wurzel*
   Motive Software - *Pat Motalo*

9. Telecommunications
   SBC - *Shawn McKenzie*
   Verizon - *Cindy Gonzales*

10. Utilities
   Reliant - *Charles A. Smith, Jr.*
   TXU - *Mark Moseley*
   COOPs - *Eric Craven*

D. Public Testimony - Part I

IV. Closing Comments

V. Other Business

VI. Recess

Appendix D: Senate Committee on Finance June 4, 2002 Hearing Agenda

SENATE INTERIM COMMITTEE ON FINANCE

AGENDA

10:00 A.M., June 4, 2002
Capitol Extension, Room E1.036

I. Call to Order/Roll Call
II. General Comments from the Chair and Members
III. Streamlined State Sales Tax
    A. Legislative Budget Board - John Keel
    B. Comptroller of Public Accounts - Eleanor Kim
    C. Public Testimony
IV. Brief Revenue Update - Comptroller of Public Accounts Staff
    A. Overall Picture
    B. Franchise Tax Collections Update
    C. Lawsuits With Revenue Implications
V. Gasoline and Diesel Fuel Taxes
    A. Comptroller's Office
    B. Public Testimony
VI. Cigarette/Tobacco Taxes
    A. Comptroller's Office
    B. Public Testimony
VII. Alcoholic Beverage/Beer Taxes
VIII. LUNCH 12:00 - 1:30
IX. Inheritance Tax
    A. Comptroller's Office
    B. Public Testimony
X. Open Session on Alternative Funding Sources
XI. Closing Comments
XII. Other Business
XIII. Recess

Appendix E: Summary of Industry Testimony to Senate Finance Committee
Interim Charge #1 - The Texas Tax System

Purpose - The purpose of this section is to condense the testimony provided by different industry panels at the February 26, 2002, Senate Finance Committee hearing. This is not a representation of the views of the Senate Finance Committee or its members, it is a compilation of the testimony provided by the panel participants.

Accountants
Testimony by Ira Lipstet:

- Wages Paid: $689 million in total wages

- Presence in Texas: 6,900 public accountant firms
  1. 6,300 sole proprietors
  2. 2,139 professional corporations
  3. 473 practice partnerships
-
- Most states do not tax accountants and book keeping.
-
  1. Hawaii, New Mexico, South Dakota but none of the major states have tried it yet.

- Sales taxes on Accounting Services - ultimately the consumers would pay this tax.

Airlines
Testimony by the Airline Industry Panel:

- The primary taxes paid by the three Texas carriers are as follows for 2001:
  1. Sales: $38.2 million
  2. Corporate Franchise: $2.3 million
  3. Property: $65.5 million

- Airlines don’t have a wish list of changes to make to the Texas tax system.

- Airlines are both capital and employee intensive. You can’t make a better tax system for airlines by shifting the burden from one kind of industry to another.

- A study by the Texas carriers a few years ago based on a hypothetical hub airline operation suggested that among 17 states with airline hub operations Texas ranked 5th highest in tax burden. They are currently updating the study.

- No surprise, Texas ranked behind California for example. But some other states normally perceived as "high tax" like New York and New Jersey rank at the bottom of that list.

Chemical

Testimony from Jim Woodrick, President of Texas Chemical Council:

- Nearly 80,000 Texans are directly employed by chemical companies

- Texas accounts for over 20% of the nation's chemical production

- Most of the products made in Texas plants are either shipped to other states or exported to other countries

- Chemical plants account for 30+% of all new manufacturing investment in Texas, followed by the computer and semiconductor industry at around 20%

- Over $40 billion of appraised value in chemical manufacturing facilities, property taxes are a major business expense, estimate at some $1 billion annually. Roughly two-thirds of this goes to public education.

- Chemical industry is a significant source of revenue for the state from sales and franchise taxes, at approximately $200 million dollars per year.

- We support the state mandate to provide adequate funding for basic public education, however have concerns regarding the equity of any changes that may be contemplated if the state needs more revenue next year. Splitting property tax rolls or the expansion of sales taxes would present a hard blow to the chemical industry in Texas.

Dow Chemical
Testimony from Director of Government Affairs Don Dipprey and Greg Cardwell, representing DuPont:

- Last year DuPont paid $69 million in state and local taxes to various jurisdictions in Texas.
- DuPont's largest investment is in Texas with a 22% of investment with a 34% of tax burden.
- The exemption of manufacturing the equipment from sales & use tax is essential
- The exemption of manufacturing use natural gas and electricity is also a must for Texas to remain competitive
- Additional benefit is the direct pay permit allowed by Texas
- The franchise tax apportionment factor methodology is a positive as is the availability of a research and development credit
- Imposing the franchise tax on a non-consolidated basis is attractive to many corporate tax payers
- Texas offers fewer franchise/income tax based incentives than other states with a significant manufacturing base
- There continue to be some areas of concern such as the number of collecting entities, the difficulty and complexity of obtaining incentives, the tax on inventory and the tax burden on capital intensive industries. DuPont's property tax burden in Texas is 40% of the total paid by the company.
- 34% of DuPont's annual total state and local tax burden is paid in Texas

Health Care

Testimony by the Physicians Panel

- In today's environment, physicians have been subjected to increasing pressures to control the cost of medical care in order to facilitate patient access and limit the financial burdens on taxpayers, businesses, and patients.

- Insurers are putting strong downward pressure on physician reimbursement while increasing physician operating costs by increasing paperwork and imposing utilization controls that create compliance costs.

- Physician office operating costs have been increasing at a rate of 11% per year, while collection ratios (the percentage of billed charges that are collected) have declined continuously and are now down to 65%. Most other businesses measure payment timeliness in terms of days in receivables, but physician practices average 2.3 months of billings in receivables at any given time.

- More than half of physicians report cash flow problems as a consequence of these conditions and 19% of physicians have drawn from their own personal funds to pay the operating expenses of their practices.

- Nationally, multi-specialty practices report that they experienced a net loss of over $30,000 per physician in 2000. Physicians who are caught in the middle of this financial squeeze are increasingly unable to absorb cost increases without passing them through to consumers or otherwise altering their practices.

- Consequently, any tax increases or new taxes on medical practices would almost certainly increase the costs of medical care, and decrease access to medical services.

- Tax increases or new taxes on medical practices would almost certainly increase the costs of medical care, thus having adverse consequences on accessibility because of increased costs for taxpayers, businesses and patients.
- Additionally, physicians are already finding it increasingly difficult to continue to provide charity care and to subsidize the Medicaid program.

- Any proposed change in tax policy should be carefully scrutinized to assure a full understanding of the economic consequences in terms of equity and in terms of the cost of medical care and access for patients.

Biotech
Testimony by Biotech Industry Panel

- The life science industry in Texas currently comprises over 500 companies with more than $5 billion in annual sales. In 2000, the industry sector employed over 46,000 Texans at an average salary of $49,414, well above the state average of $34,660. The three major segments of the life science industry in Texas are laboratory/research services, medical devices and pharmaceuticals.

- In the development of intellectual property assets, Texas benefits from the wealth of intellectual resources generated within our renowned academic institutions. Newly released FY 2000 data from the National Science Foundation shows that Texas ranks third in the country in total R&D expenditures among our academic institutions. Over $2 billion from all sources was invested in R&D at Texas institutions in FY 2000, and $165 million of that came from industry sources.

- To remain competitive, the Texas Healthcare and Bioscience Institute recommends that companies with earned, unused tax benefits have the ability to sell those tax benefits to another company for cash. Companies can then invest the cash immediately back into R&D activities, rather than having to wait until the company is profitable.

Insurance
Testimony from the American Insurance Association:

- Insurers held $25.8 billion in Texas municipal bonds in 2000 (almost 30% of the total outstanding state and local debt.)

- The P&C insurance tax system in Texas was reformed in 1999 to substitute a simple, flat premium tax rate for the complex, investment-tiered premium tax rate structure that applied under prior law.

- Today P&C insurers are liable for the following taxes and other burdens (in lieu of franchise tax): Gross premium, maintenance, retaliatory, sales/use and property, fees to fund a number of state agencies and other assessments of taxes for the workers' compensation subsequent injury fund.

- In 2000, AIA members collectively wrote over $6.8 billion in direct premiums in Texas, comprising 43% of the commercial lines insurance market in Texas and including over 50% of such lines of business as workers' comp, commercial multi peril, and fidelity and safety.

- The 1999 tax reforms greatly simplified the complexities of the prior, investment-tiered rate structure, and also brought Texas within the mainstream of states that have reduced premium tax rates and streamlined their insurance tax systems in recent years.

- AIA and most of the insurance industry strongly support retaliatory taxation, which is inextricably tied to the premium tax system. Retaliation serves to protect Texas' domestic insurance industry from excessive or discriminatory taxation in other states. Thus, retaliation tends to have a leveling or moderating influence on premium tax rates nationwide.

Oil & Gas

Testimony given by Texas Oil and Gas Association:

- Exploration & production operations pay $2 billion annually ($4 billion per biennium) in state and local taxes.

- Oil and gas related industries pay $130 million annually in state sales and franchise taxes.

- Sales and use tax = $425,000,000
  Franchise tax = $91,000,000
  Property tax = $499,000,000
  Local sales & use taxes = $13,000,000
  Oil severance tax = $417,000,000
  Gas severance tax = $698,000,000
  Oil well service tax = $7,000,000

- Comptroller's Forecast for oil severance tax revenue:
  2002 = $334,900,000
  2003 = $323,200,000

- Comptroller's forecast for natural gas tax revenue:
  2002 = $913,800,000
  2003 = $846,8000,000

Independent Producers & Royalty Owners Association
Testimony given by J.R. Hurd, representing Texas

- In 1999, the average Texas oil well produced 6.9 barrels per day and the average gas well produced 216 thousand cubic feet of gas per day. At current prices, 6.9 barrels of oil generates $141.45 per day of revenue and 216 thousand cubic feet of gas generates $496.85 per day of revenue.

- Severance taxes and royalties are a particular stress because they are paid "off the top" without regard to weather the well is making a profit.

- Partnerships are an absolutely essential part of the capital formation process for the independent oil and gas producer. Texas needs to think about placing a burden on a vehicle that is so critical to continued exploration for oil and gas in Texas.

Technology
AeA testimony given by Geoff Wurzel

- 3 significant elements which enable Texas to be competitive with other states: single sales factor apportionment in the franchise tax, sales tax exemption for manufacturing equipment allows Texas to attract and retain high-wage manufacturing jobs, and R&D franchise tax credit, enacted in 1999, encourages companies to conduct research activities in Texas.

- Weak areas in the Texas tax system include; over-dependence on sales and property taxation, both of which disproportionately tax the capital-intensive industry. Texas is one of the only 16 states that subject business inventory to the property tax.

- Ideas to implement these principals:

1) State tax policy should encourage companies that compete in global markets to locate, expand, and retain their facilities and personnel in Texas
2) The business tax base should be applied fairly
3) The tax structure must consider the ability of the taxpayer to bear the burden of the tax

Testimony provided by Pat Motola, Vice President, Motive Communications and AeA Texas Council Executive Committee Member:

- Wants to emphasize the importance of attracting and nurturing startup and early stage companies in high tech.

- Tax policy should be integrated with high tech workforce policy and business development efforts of it is going to ultimately be successful.

- What policies are working for early stage high tech companies?
  1) Franchise tax because it does not impose a significant tax when a company is not profitable and doesn't have significant equity.
  2) The apportionment of the franchise tax based on the single factor of sales is also working well in that it is simple, fair, and consistent with what most states are doing in this area.
  3) The exclusion of franchise taxes for companies with less than $150,000 in receipts helps early stage companies preserve precious capital needed to grow their business.

- What tax policies can be improved?
  1) Using the 20-year carry forward allowed by Federal Tax law.
  2) Property taxes comprise the single biggest tax that early stage high tech companies typically pay other than Federal FICA matching.
  3) R&D sales tax exemption is particularly important to early stage high tech companies with significant R&D equipment outlays such as the biotechnology industry.
  4) Technology service businesses that provide information services and date processing are arguably the most rapidly growing segment of the economy. Information service providers are typically less capital intensive then they are

labor intensive. The "capital" of this industry is human capital, which makes it relatively easy to relocate to more competitive jurisdictions.

5) Data processing can be very capital-intensive. The legislature granted a 20% sales tax exemption for the information services and date processing. Great start.

Telecommunications
Testimony given by Cindy Gonzales, representing Verizon

- Telecommunications industry pays over $1 billion in state & local taxes.

- Verizon pays more than $200 million in Texas taxes annually.

- Texas has the highest total tax on telecommunications services of any state.

- The total number of Texas taxes imposed on telecommunications services is 13 versus 2 for general business.

- Taxes imposed include sales and use tax on the purchase and installation of telecommunications equipment, franchise tax imposed on the income of the provider and property tax assessed on both the value of telecommunications equipment and real property.

- In states like Texas, where investments made by manufacturers are exempt from sales tax, the telecommunications industry is subject to an inequitable tax burden when not granted similar treatment.

- Texas is one of the few states that taxes data processing, information services and Internet access.

- Last year the NCSL adopted a resolution recognizing the high level of tax and compliance burdens on telecommunications. That resolution provides that states need to simplify and modernize state and local telecommunications tax systems to encourage economic development, reduce impediments to entry and endure access to advanced telecommunications infrastructure and services throughout the states.

- Legislation was enacted in the past two years in Arkansas, Missouri, Connecticut and Kansas that clarifies how bundled services are taxed. Texas should follow the lead of these states and address the taxation of bundled services for all telecommunications carriers by allowing providers to apply tax to the individual components of the bundle.

- All business taxpayers would benefit greatly from the simplification of the administrative burden associated with filing and payment of property taxes to the multitude of taxing jurisdictions and with the enactment of meaningful appraisal appeal right at the Comptroller lever.
- In addition, the imposition of a property tax on inventory discourages investment in the state of inventory storage facilities that often can be located in one of the many states that do not impose a property tax on inventory.

Utilities

Testimony given by the Association of Electric Companies of Texas

- Investor-owned utilities (IOUs) are subject to state gas, electric and water gross receipts tax, public utilities gross receipts assessment, corporate franchise tax, state and local sales taxes, property taxes, municipal franchise charges, and a system benefit fee. In 2000 state and local tax remittances from investor-owned electric utilities totaled $1.647 billion, with these taxes exceeding 10% of retail electric sales.

- Municipally-owned utilities (MOUs) are exempt from all taxes save the obligation to collect sales tax on taxable sales of electricity; and rural electric cooperatives (RECs), while subject to property taxes, municipal franchise fees, and the public utilities gross receipts assessment, are exempt from the gas, electric and water gross receipts tax, corporate franchise tax, the system benefit fee, and payment of state and local sales taxes on purchases.

- Gas, Electric & Water Utility Tax:
  1) A tax is imposed on each utility company located in an incorporated city or town having a population of more than 1,000 according to the most recent federal census.
  2) Utility companies subject to tax include electric companies, natural gas distribution companies, and water utility companies that make local sale and distributions.

- Exceptions to the base:
  1) Utility companies owned and operated by a city, town, county, water improvement district, or conservation district is exempt.
  2) Electric cooperatives are exempt from the utility tax by dint of exemption from all excise taxes as provided in the Electric Cooperative Corporation Act.

- Corporate Franchise Tax:
  1) Corporation and limited liability companies doing business in Texas are subject to franchise tax for the privilage of the liability veil provided to those forms of business organizations by state law.
  2) Tax due is the greater of 0.25 percent of corporate net worth (taxable capital) or 4.5 percent of earned surplus (corporate net income plus compensation of

officers). Taxable capital and earned surplus from multi-state firms are apportioned to the state based on gross receipts from sales in the state.

3) The tax is paid to the comptroller and deposited to the state general revenue fund.

- Exceptions to Base or Rate
  1) An electric cooperative corporation under Chapter 161, Utilities Code, that is not a participant in a joint powers agency is exempted from the franchise tax.
  2) Municipally-owned utilities are exempt, as the state constitution bars state taxation of municipal corporations.
  3) As an incentive for renewable power, businesses engaged exclusively in manufacture, sales or installation of solar energy devices are exempt from franchise tax.

- Property Tax
  1) Electric companies have major investments in taxable property, principally generating plant and transmission and distribution infrastructure. Property taxes have been the largest state or local tax expense for investor-owned electric utilities, in excess of $400 million annually in recent years.
  2) After enactment of electric industry restructuring legislation (SB 7, 76th Leg,) generating plants in tax year 2000 were for the first time appraised on a stand-alone basis rather than as party of regulated monopolies.

Legal Profession

Testimony provided by Attorney Cindy Ohlenforst

- Texas collected $5.4 million in franchise tax from legal corporations in 2000.

- Over 60% of lawyers are in private practice and the majority are in small firms (1-5 attorneys).

- Taxes Paid: Property, sales and some franchise tax depending on how they are organized.

- Business Organization: Most are organized as partnerships.

- Sales Tax on this Service: Sales tax would end up as a consumer tax.

- Most states do not collect sales tax on attorneys fees.

Center for Public Policy Priorities
Testimony Provided by Dick Lavine

- Our basic problem is that state and local tax revenue does not keep up with the growth of the Texas economy.

- The sales tax applies to 40 percent of retail trade in goods, but only 30 percent of the sales of services. Over the past ten years, sales of services have grown at a pace one and one-half times faster than the growth in retail trade in goods.

- The state could generate additional revenue by expanding the sales tax to cover services that are currently untaxed, including most business and professional services.

- The way to get more revenue from the school property tax is to make it function better.

- The Legislature should create reasonable penalties to force businesses to report ("render") their personal property to appraisal districts. According to the appraisal districts, there is $36 billion in unreported business personal property in the state, which could generate $1 billion in school property taxes in 2004-05.

- The Legislature should also require disclosure of the sales price of all real estate transactions. Disclosure is required in 35 states; Texas is the only state so dependent on property taxes that tries to function without this type of information. Although no estimate has been made of the additional value that could be uncovered, there is no doubt that the property tax system could work more efficiently with more accurate information.

- Finally, the entire Tax Code should be subjected to a periodic Sunset review. Just as state agencies are reviewed every 12 years and made to justify their continued existence, each tax exemption should be periodically examined and, if its continued existence cannot be justified, removed from the Tax Code.

- The Center for Public Policy Priorities has calculated that a personal income tax, based on the Kansas model, in Texas could have generated $17.3 billion in total revenue in 2000.

Green Tax
Testimony of Cyrus Reed of the Texas Center for Policy Studies

- Presented a report entitled "New Ideas for Fair Taxation in Texas: Promoting Environmental Responsibility," which highlights a number of new tax and fee options that should encourage more environmentally responsible behavior.

- The report reviews a number of possible categories of environmentally responsible taxes, including new motor fuels and a "feebate" motor vehicle sales tax, a coal severance or use tax, repeal of some sales tax exemptions such as those on pesticides, fertilizers and agricultural chemicals, a limited carbon tax, electricity taxes and new pollution taxes on air emissions and toxic releases. [216]

New Tax	Current Rate	Proposed Rate	Expected Biennial Revenue
Coal Use Severance Tax	**None**	**7.5%**	**$100 million**
Electricity Efficiency Tax on Power Plants	**None**	**$0.15 per pound of NOx per Megawatt Hour Times Megawatt Hours**	**$200 million**
High-Sulphur Diesel and Gas Tax	**$0.20 gas and diesel motor fuels tax**	**Charge additional fee of $0.05 for high-sulfur diesel fuels**	**$300 million**
Feebate on New Motor Vehicles Sold	**Flat 6.25% sales tax on all vehicles**	**Sales tax differentiated between 2 and 10% depending upon emissions**	**$200 million**
Total of 4 New Taxes			**$800 million**

[216] Texas Center for Policy Studies, *New Ideas for Fair Taxation in Texas: Promoting Environmental Responsibility*, February 2002

High Diesel Sulphur Fee

In the coming years, Texas will be required to meet new national sulphur standards for gasoline and diesel fuels. Under Texas' Low -Emission Diesel Fuel Program, in June 1, 2006, the maximum sulphur content of diesel fuels used in on-road vehicles will be reduced from 500 to 15 ppm statewide, and the maximum standard of LED for non road equipment will also be reduced to 15 ppm in 110 counties in Central and East Texas. Through 2009, there will be some flexibility offered, with some refineries able to produce diesel at higher sulphur levels as long as the average reaches the standard (there will also be some hardship exemptions available for smaller refineries).

Producing low sulphur-fuels will raise diesel prices by five cents per gallon. Lowering Sulphur content in both gas and diesel is so important is because the lower the Sulphur, the lower the fine particulate matter-which can be inhaled directly into people's lungs and affect their health- the lower the toxicity and the lower the nitrogen oxides, one of the precursors of ozone.

Options

1. A Sulphur surcharge fee could be added to diesel-and even gas-fuels with a high sulphur content. This would be an incentive for refineries an importers to meet sulphur content requirements sooner than later.

2. One simple sulphur fee would put in place a surcharge of 5 or even 10 cents per gallon or $2.25 per barrel for any gas sold with a high Sulphur content, while providing an incentive for the production of low-sulphur fuels.

3. By applying the fee to the barrel rather than the pump the legislature will have more flexibility to earmark the funds to appropriate programs.

Appendix F: Selected News Clips History of Select State Taxes 1998- Present

The Corporate Franchise Tax: 1988-Present

1988-89

- State will lose money because energy companies have placed some of their assets in reserve to avoid paying franchise tax.[217]
- Fewer companies carry the weight of franchise tax and it is those companies that need the most help at this time, such as mining and manufacturing (May 10, 1988;
- Select Committee on Tax Equity reports that businesses pay more of the state's taxes then the national average; in addition, unincorporated businesses do not pay tax therefore causing the ones that do pay to shoulder too much of the burden.[218]
- House Ways and Means Committee hurriedly approves measure to clarify what is taxable under franchise tax; measure passed.[219]
- Tax bill in front of legislature would decrease expenses for a small group of businesses including Bass Brothers.[220]

1991-95

- Comptroller John Sharp and John Connally, chairman of the Governor's Task Force on Revenue, push for "business activity tax" to replace franchise tax.[221]
- Businesses dislike Richards' plan to "broaden" the tax base, plan does not include partnerships and sole proprietorships.[222]
- Democratic Senators write letter to Governor Richards and Speaker Lewis voicing concern over House proposal that would tax incomes of partnerships and proprietorships.[223]

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[217] Dallas Times Herald, Mar. 15, 1988

[218] Dallas Times Herald, Nov. 24,1988

[219] Dallas Morning News; et. al., Feb. 24, 1989

[220] Houston Chronicle, Apr. 1, 1989

[221] Dallas Morning News, Jun. 14, 1991

[222] Austin American-Statesman, July 16, 1991

[223] Houston Chronicle, July 27, 1991

- Facing a budget deficit, Gov. Richards and Chairman Hury call for reform to franchise tax saying it is a relic from Texas' past.[224]
- Rep. Ken Fleuriet urges business to fight expanded franchise tax bill which would add small businesses to the tax roll.[225]
- Bill proposed by Chairman Hury is called a "revision of the unfair franchise tax" but is more along the lines of an income tax.[226]
- Legislature approves tax on corporate profits in 1991.[227]
- In 1992, the GOP and several businesses begin to heavily attack the changes in the franchise tax saying it was now an income tax.[228]
- Alliance for Quality Education wants franchise tax and the school portion of property taxes eliminated and replaced by a single tax on business activity.[229]
- Rep. Roberto Gutierrez proposes cutting franchise tax by .25 percent to attract new business.[230]
- Lawsuit with Caterpillar Inc. over collection method of franchise tax could cost state $1 billion.[231]

1997-98

- Gov. Bush proposes elimination of corporate franchise tax and creation of business activity tax.[232]
- Rep. Paul Sadler as well as many others call the business activity tax an income tax.[233]

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[224] Dallas Times Herald, July 28, 1991

[225] Valley Morning Star, Aug. 2, 1991

[226] Austin American-Statesman; et. al, Aug. 4, 1991

[227] San Antonio Light, Aug. 14, 1991

[228] Dallas Morning News, May 16, 1992; and Austin American-Statesman, Sept. 18, 1992

[229] Austin American-Statesman, May 23, 1993

[230] Valley Morning Star, Jan. 12, 1995

[231] Wall Street Journal, Oct. 11, 1995

[232] Austin American-Statesman; et. al, Jan. 23, 1997

[233] Ft. Worth Star-Telegram, Feb. 4, 1997

- Rep. Tom Craddick opposes tax plan[234]
- Select Committee on Revenue and Public Education Funding and Gov. Bush agree on expand franchise tax to partnerships.[235]
- Comptroller Sharp proposes ending the franchise tax for companies that earn less than $250,000 a year.[236]

1999

- Senate passes tax exemption for businesses with revenue of $100,000 or less a year.[237]
- Bill proposed to offer tax credit to companies that do business in counties with high unemployment and low income.[238]
- House GOP decide to not favor Bush plan of cutting property taxes and instead seek sales and franchise tax cuts.[239]
- Franchise tax credits proposed for companies that do research and development in strategic investment areas and donate funds for after school programs.[240]
- Senate revives tax credit bill after it was killed by Rep. Sylvester Turner the day before, credit would go to companies who help build border economy.[241]

2000-Present

- Intel decides not to build plant in north Fort Worth citing state tax system as a major concern.[242]

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[234] Dallas Morning News, Mar. 29, 1997

[235] Austin American-Statesman; et. al, Mar. 29, 1997

[236] El Paso Times, Jan. 20, 1998

[237] Ft. Worth Star-Telegram, Feb. 26, 1999

[238] San Angelo Standard-Times, Mar. 11, 1999

[239] Dallas Morning News, Apr. 7, 1999

[240] Austin American-Statesman; et. al, Apr. 13, 1999

[241] El Paso Times; et. al, May 27, 1999

[242] Ft. Worth Star-Telegram, Jan. 31, 2000

- Gov Perry hints that there might be a way to tax companies that are currently exempt from the franchise tax.[243]
- Lt. Gov. Ratliff believes that loopholes in franchise tax must be closed.[244]

The Natural Gas Tax: 1981-Present

<u>1981-82</u>

- Attorney General Mark White calls for an increase in severance tax, tax on natural gas is at 7.5% and has not been moved since 1969.[245]
- Comptroller Bob Bullock opposes increase in severance tax saying it would hit Texans harder than out of staters.[246]
- Texas Energy and Natural Resources Committee recommends no increase in severance taxes.[247]
- States have been raising taxes on their exports prompting others to raise taxes on their goods in response.[248]

<u>1985-86</u>

- Governor Mark White proposes ending price controls to stimulate increased drilling among fears of shortage.[249]

<u>1989</u>

- Railroad Commission Chairman Kent Hance proposes a lifetime severance tax exemption for some new wells.[250]

<u>1994-95</u>

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[243] Austin American-Statesman, Oct. 20, 2001

[244] San Antonio Express-News, Feb. 1, 2002

[245] Dallas News, July 9, 1981

[246] Waco Tribune Herald, July 25, 1981

[247] Houston Post, Dec.4, 1981

[248] Houston Chronicle, July 8, 1982

[249] Bryan College Station Eagle, April 11, 1986

[250] Amarillo Daily News, March 15, 1989

- Railroad Commission says that tax incentives have spurred production of gas.[251]
- RCC Jim Nugent and Commissioner Mary Scott Nabers propose incentives to boost production from marginal wells.[252]
- Sen. Teel Bivins proposes lowering severance tax on natural gas and rasing it on coal; at this point Texas has highest severance tax on natural gas in the nation.[253]
- Sen. John Montford proposes measure meant to increase gas production and give incentives for marginal wells.[254]
- During 1995 session the majority of energy industry related bills have been bottled up in committee.[255]
- House may investigate extending tax break to drillers that look for "high cost" gas.[256]
- Three bills designed to aid energy industry are passed:[257]
  1) Railroad Commission can take over non-polluting wells that are no longer economically viable in hopes that they might be viable one day
  2) Renew an existing law that grants a 10 year severance tax exemption when producers reactivate inactive wells
  3) 10 year exemption to wells that are expensive to produce

1999-Present

- Rep. Warren Chisum and Sen. Teel Bivins co-sponsor bill to provide $45 million in emergency severance tax relief.[258]

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[251] Corpus Christi Caller Times, March 15, 1994

[252] Amarillo Daily News, Sept. 7, 1994

[253] Lubbock-Avalanche News, Jan. 18, 1995

[254] Amarillo Daily News, Jan. 22, 1995

[255] Corpus Christi Caller Times, April 26, 1995

[256] Austin American Statesman, May 2, 1995

[257] Houston Chronicle, May 24, 1995

[258] Amarillo Daily News, Jan. 28, 1999

- Legislation clears that would allow producers of expensive natural gas wells and inactive wells to continue receiving severance tax relief.[259]
- At Railroad Commission annual meeting, cuts urged to continue oil and gas rebound.[260]
- Sen. Bivins proposes sliding scale tax for oil and natural gas.[261]

The Gasoline Tax: 1980-Present

1980

- Gov. Clements calls for an increase to the state's 5 cent-per-gallon fuel tax to help for $300 million shortfall in highway construction fund.[262]
- Lt. Gov. Hobby says tax increase is not needed.[263]
- Gov. Clements switches position on gasoline tax hike 7 months after original proposal.[264]

1981

- Gov. Clements now says he would sign an increase because of increasing fuel conservation efforts leading to a possible $900 million shortfall in highway construction funds.[265]
- Panel finds that a one cent-per-gallon increase in the fuel tax would generate an additional $100 million per year for highways.[266]

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[259] Corpus Christi Caller Times, May 19, 1999

[260] Austin American Statesman, July 15, 1999

[261] Amarillo Daily News, May 26, 2000

[262] Dallas News, May 21, 1980

[263] Dallas Times-Herald, Sept. 23, 1980

[264] San Antonio Light, Oct. 15, 1980

[265] Ft. Worth Star-Telegram, March 6, 1981

[266] Austin American Statesman, March 13, 1981

- Gov. Clements says he would not approve an increase in tax unless there was also compensating tax relief.[267]
- Highways and roads across the nation are breaking down prompting an increase in many different states' fuel taxes.[268]

1983-1987
- Highways and Transportation Chairman Dedman proposes 10% gas tax; Gov. White counters with a 5% tax that contains a 5 cent floor.[269]
- In session, Gov. White and Senate attempt to make a compromise on a tax package with a 5-cent increase in fuel tax in exchange for more consideration of issuing highway bonds.[270]
- Both the Texas Municipal League and the Texas Good Roads/Transportation Association push the legislature to double fuel tax; the following year a coalition of civic groups and business associations in Houston bands together for tax hikes.[271]
- Texas Poll finds that tax increase is favored 53%-47%[272]
- Increase to 10 cent-per-gallon tax approved in 1984.[273]
- Temporary increase to 15 cents-per-gallon in 1986 made permanent in 1987

1990-1991
- In early 1990, call goes out for another increase in gas tax to repair roads.[274]
- Chairman Dedman proposes an increase to 25 cents-per-gallon.[275]

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[267] Houston Chronicle, March 14, 1981

[268] Wall Street Journal, Oct. 15, 1981

[269] Dallas Times-Herald; Feb. 17, 1983; Austin American Statesman, Feb. 16, 1983;

[270] Ft. Worth Star-Telegram, April 20, 1983

[271] Dallas Times-Herald, May 3, 1983

[272] Ft. Worth Star-Telegram, Feb. 29, 1984

[273] Houston Chronicle, Aug. 1, 1984

[274] San Antonio Express, April 15, 1990

[275] Amarillo Sunday Daily-News, June 17, 1990

- Decision to increase tax to 20 cents-per-gallon angers many motorists.[276]

[276] Austin American Statesman, Aug. 15, 1991

1998-Present

- Increase in fuel tax might be necessary so that the state can generate enough money to match funds from federal highway bill passed in 1998.[277]
- SB 1547 in 1999 changes fuel tax collection so loopholes can be closed and more revenue can be generated.[278]
- In the 77th session, Rep. Alexander D-Athens and Rep. Averitt R-Waco propose a 5 cent increase in fuel tax but it is left in pending in committee.[279]
- Sen. Ratliff calls for rise in gas tax in 1999 to repair and build roads but backs off of this in 200.[280]

The Income Tax History: 1989-Present

1989

- Several legislators consider state income tax, in present or future, for varying reasons:
  1) Rep. Richard Williamson for education.[281]
  2) Rep. Jack Vowell to alleviate property taxes.[282]
  3) GOP gubernatorial candidate Clayton Williams for war on drugs
- Lt. Governor Bill Hobby calls for implementation of 4% state income tax[283]
  1) includes dissolution of corporate franchise ax and decreases in property and sales taxes

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[277] Amarillo Daily News, Aug. 1, 1998

[278] San Antonio Express News, March 15, 1999

[279] Austin American Statesman, March 11, 2001

[280] Ft. Worth Star-Telegram, March 24, 2001

[281] Lubboock Avalanche, June 17,1989

[282] El Paso Times, Sept. 3, 1989

[283] Austin American Statesman and included opinions, Nov. 3 1989

1990

- El Paso poll finds that 67% oppose an income tax; 61% would *still* oppose it if it were coupled with other tax cuts.[284]
- Texas Poll finds that 58% would support income tax for education if property taxes were greatly reduced.[285]
- Poll of Common Cause of Texas members: with 634 responding, 394 support both personal and corporate income tax, 85 support corporate only, 17 support personal only, and 138 oppose both.[286]

1991

- Amidst growing interest in income tax from business and political groups, Lt Gov. Bob Bullock calls for a 5% personal and 8% corporate income tax.[287]
- Harris County Judge Jon Lindsay says he would support an income tax if it were to go towards new prisons.[288]
- Governor Ann Richards claims that phone calls to her office are 2-to-1 against an income tax; she later pledges that there would be no new tax.[289]
- Texas Association of Taxpayers supports income tax with reduction in property and sales taxes and elimination of franchise tax[290]
- Houston Chronicle poll shows 75% disapprove of income tax.[291]

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[284] El Paso Times, Feb. 24, 1990

[285] Houston Chronicle, Feb. 25, 1990

[286] Houston Post, April 3, 1990

[287] Dallas News, March 1, 1991; Dallas Times-Herald, March 7,1991

[288] Houston Chronicle, March 7, 1991

[289] San Antonio Express, March 16, 1991

[290] Corpus Christi Caller, April 12, 1991

[291] Houston Chronicle, July 4, 1991

1992

- Lt. Gov. Bullock changes his stance and now says he will "resist all efforts" to increase taxes.[292]
- Rep. Paul Sadler D-Henderson supports income tax for education funding.[293]

1993

- Lt. Gov. Bullock pushes amendment to prohibit income tax unless it is voted on in a statewide election, property taxes are reduced, and the revenue must be spent on education; amendment is approved overwhelmingly.[294]

1994-Present

- 1994- Support for income tax grows in El Paso in exchange for lower property taxes[295]
- 1995- 53% oppose state income tax.[296]
- 1997- 45% say they favor income tax, an increase of 11 points from a decade ago.[297]
- 2002- El Paso poll finds that 75% oppose income tax.[298]
- 2002- Voluntary income tax proposed; payment of income tax would allow for sales tax rebate and deduction from federal income tax.[299]

[292] Austin American Statesman, Jan. 24, 1992

[293] Austin American Statesman, November, 24, 1992.

[294] Austin American Statesman; et al., April 21, 1993

[295] El Paso Times, October 23, 1994.

[296] Corpus Christi Caller Times, August 27, 1995

[297] Corpus Christi Caller Times, May 11, 1999

[298] El Paso Times, March 1, 2002

[299] Ft. Worth Star-Telegram, May 17, 2002

Appendix G: Summary of Select Texas Tax Reports

The following is a brief chronology of Texas Tax studies and legislation between the years of 1987 and 2002.

1987, 70th Legislature
1. Adopted Franchise Tax exemptions
2. Sales Tax exemptions
3. "Build Texas" bond program
4. Creation of "Rainy day" fund for state government

1987, 70th Legislature special summer session
1. $39.5 billion budget and Passage of $5.7 billion tax bill (until then, the largest tax increase in the history of any state)
2. Increased sales tax rate to 6%. This accounted for additional $4.1 billion for 88-89 biennium
3. Expanded sales tax to services; credit reporting, debt collection, info and data processing services, real property services, insurance services, security, amusements and phone services.
4. Imposed temporary professional fees for the first time ($110)

1987, HB 2- Select Committee on Tax Equity named to conduct the Rethinking Texas Taxes study(1989)
1. This study looked at a number of different scenarios on taxes, including an increase on things recurrent
2. Recommendations:
    a. Sales tax should remain cornerstone of state tax system. Support expansion of tax base, but NOT and increase in the tax rate.
    b. State oil and gas should "seek their own rate", state should not adjust it to make up revenues.
    c. Expand franchise tax to non-corporate businesses and moving away from its focus on net worth as a tax base
    d. Conditions are not right for the consideration of an income tax, but should not be discarded as a future tax option.
    e. Local government finances, particularly property tax, should be reworked.

1991, 72nd legislature faced $4.6 billion revenue shortfall- amount required to keep state at current level.

1991, In accordance to Executive Order AWR 91-3, Governors Task force on Revenue was enacted (Charting a Course for Texas' Future). The task force looked at:

1. Overall State Spending
2. Local property Tax, Business Tax, Sales Tax, Income Tax, etc.
3. Recommendations:
    a. Relieve local property tax payers
    b. Reverse over dependance on sales tax: Rasing sales tax rate or broadening base serves to worsen an already regressive tax.
    c. Texas tax policy should max deductibility of state taxes from federal income tax.

1991, 72nd legislature

1. Expanded number of services taxed
2. Raised the sales tax rate to 6.25%
3. Imposed Permanent professional fees ($200/yr) affecting Opticians, Accountants, Architects, Engineers, Doctors, Lawyers.
4. Substantially modified Franchise tax

1996, Executive Order GWB 96-4 created, The Citizen's Committee on Property Tax Relief
Charge:

1. Assess effects of property taxation upon various segments of th estate's economy, and the public and the public sentiment relative to the need to provide property tax relief, and
2. To gather and evaluate public input on the Report of the Staff Work Group on Property Tax Relief

Effects of Property Tax Upon States' Economy:

1. Home ownership: Placing a substantial burden on home ownership, especially if home valuation rises faster than owners income.
    a. Prop tax discriminates against home owners by forcing them to pay for public schools versus non homeowners
    b. Suggest a broad-based and equitable means of taxation be substituted for current property tax.
2. Business Capital: If business making a profit property tax can absorb a tremendous portion of those returns. If business is not making a profit, property tax can drive it deeper into the red.

1998 Select Committee on Public Education.

1. Committee took a combined look at tax issues and public school finance.

Appendix H: Cost of Sales Tax Exemptions Table[300]

Cost of Sales Tax Exemptions, Fiscal 2001 to 2006 (in millions of dollars)							
Section*	**Exemption**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**
151.302	Sale for resale	cbe	cbe	cbe	cbe	cbe	cbe
151.303	Previously taxed items	cbe	cbe	cbe	cbe	cbe	cbe
151.304	Occasional sales	cbe	cbe	cbe	cbe	cbe	cbe
151.305	Coin-operated machine sales	negligible	negligible	negligible	negligible	negligible	negligible
151.306	Transfers of common interests in property	cbe	cbe	cbe	cbe	cbe	cbe
151.307	Exemptions required by prevailing law	cbe	cbe	cbe	cbe	cbe	cbe
151.3071	Installation of certain equipment for export	negligible	negligible	negligible	negligible	negligible	negligible
151.308	Items taxed by other law						
	Crude oil	0	0	0	0	0	0
	Motor vehicles	$2,417.10	$2,523.10	$2,635.80	$2,780.80	$2,947.70	$3,127.50
	Motor fuels	1,125.10	1,185.20	1,255.80	1,334.80	1,418.00	1,507.40
	Mixed drinks	186.9	192.7	197.8	202.3	208	213.6
	Cement	0	0	0	0	0	0
	Sulphur	0	0	0	0	0	0
	Aviation fuel	68.3	73.1	78.2	83.7	89.3	95.3
	Oil well services	20.2	19.2	18.2	17.3	16.4	15.6
	Insurance premiums	2,589.80	2,706.30	2,801.00	2,885.00	2,957.20	3,019.30
151.309	Sales to governmental entities	197.3	206.9	218.5	231.1	245.1	260.6
151.31	Religious, educational/public service organizations						
	Sales to nonprofits	16.1	17.2	18.3	19.5	20.8	22.4
	One day sales	3.7	3.9	4.2	4.5	4.8	5.1
151.3101	Amusement services	cbe	cbe	cbe	cbe	cbe	cbe
151.311	Property used for the improvement of exempt realty	15.5	16.1	16.8	17.7	18.8	20
151.3111	Certain personal property	cbe	cbe	cbe	cbe	cbe	cbe

[300] Comptroller of Pubic Accounts, Tax Exemptions and Tax Incidence, January 2001. Located at http://www.window.state.tx.us/taxinfo/incidence/table4.html

*** Texas Tax Code**

Appendix H: Cost of Sales Tax Exemptions Table Continued

Cost of Sales Tax Exemptions, Fiscal 2001 to 2006 (in millions of dollars)							
Section	**Exemption**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**
151.3141	Food stamp purchases	124	132	140.4	149.7	159.9	171.8
151.315	Water	210.1	214.9	219.4	224.6	230.3	236.4
151.316	Agricultural items						
	Agricultural feed, seed, chemicals and supplies	230.2	232.3	234.3	238.7	244.7	250.5
	Livestock for food	12.3	12.4	12.5	12.8	13.1	13.4
	Agricultural machinery and equipment	52.1	52.6	53	54	55.4	56.7
	Horses, mules and work animals	8.4	8.5	8.6	8.7	9	9.2
	Commercial fishing ice	0.1	0.1	0.1	0.1	0.1	0.1
151.3161/2	Timber operations (equipment)	2.6	5.2	6.5	8.8	10.6	13.7
151.317	Gas and electricity						
	Manufacturing	375.3	377.7	379.4	387.7	402.3	415.8
	Residential	520	530.5	539.6	549.8	562.6	577.3
	Agricultural	13.5	13.4	13.2	13.1	13.1	13.2
	Mining	36.9	36.5	36	35.6	35.7	35.9
151.318	Manufacturing						
	Materials used in manufacturing	7,535.70	8,020.60	8,523.50	9,137.20	9,800.80	10,484.70
	Manufacturing machinery and equipment	497.9	529.9	563.1	603.7	647.6	692.8
	Packaging and wrapping supplies	109.1	116.1	123.4	132.2	141.9	151.8
	Film equipment (151.3185)	*	*	*	*	*	*
151.319	Newspapers						
	Newspapers	16.8	17.9	19	20.4	21.9	23.4
	Newspaper inserts	22.8	24.2	25.8	27.6	29.6	31.7
	Newspaper manufacturing equipment	**	**	**	**	**	**
151.32	Magazine subscriptions	6.1	6.5	7	7.4	7.9	8.5
151.321	University student organizations	negligible	negligible	negligible	negligible	negligible	negligible

Appendix H: Cost of Sales Tax Exemptions Table Continued

Cost of Sales Tax Exemptions, Fiscal 2001 to 2006 (in millions of dollars)							
Section	**Exemption**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**
151.326	Clothing and footwear holiday	31.2	33.2	35.3	37.6	40.2	43.2
151.328	Aircraft						
	Certain aircraft	negligible	negligible	negligible	negligible	negligible	negligible
	Repair equipment for certain aircraft	16.3	17.5	18.9	20.6	22.5	24.5
151.329	Certain ships	34	36.5	39.5	43	46.9	51.1
151.3291	Boats and boat motors	52.7	56.1	59.7	63.7	68	73
151.33	Interstate shipments	cbe	cbe	cbe	cbe	cbe	cbe
151.331	Rolling stock						
	Railroad fuel and supplies	6.4	6.8	7.4	8.1	8.8	9.6
	Rolling stock and locomotives	1.9	2.1	2.3	2.5	2.7	2.9
151.332	Senior citizen organizations	negligible	negligible	negligible	negligible	negligible	negligible
151.335	Coin-operated services	34.8	37	39.4	42	44.8	48.2
151.336	Certain coins and metals	negligible	negligible	negligible	negligible	negligible	negligible
151.337	Sales by or to Indian tribes	cbe	cbe	cbe	cbe	cbe	cbe
151.338	Environment and conservation services	cbe	cbe	cbe	cbe	cbe	cbe
151.34	Official state coin	negligible	negligible	negligible	negligible	negligible	negligible
151.341	Development corporations	negligible	negligible	negligible	negligible	negligible	negligible
151.342	Agribusiness (agricultural containers)	0.4	0.4	0.4	0.4	0.4	0.4
151.343	Animal shelters	negligible	negligible	negligible	negligible	negligible	negligible
151.346	Intercorporate sales of services	cbe	cbe	cbe	cbe	cbe	cbe
151.347	Lawn and yard	negligible	negligible	negligible	negligible	negligible	negligible
151.348	Cooperative research ventures	cbe	cbe	cbe	cbe	cbe	cbe
151.349	Texas National Laboratory	0	0	0	0	0	0
151.35	Labor to restore property	cbe	cbe	cbe	cbe	cbe	cbe

Motor Vehicle Sales Tax Exemptions Fiscal 2001-2006 (in millions of dollars)							
Section Texas Tax Code	Item	2001	2002	2003	2004	2005	2006
152.081	Driver training motor vehicles	negligible	negligible	negligible	negligible	negligible	negligible
152.082	Sales to or use by a public agency	$28.50	$29.10	$29.70	$30.40	$31.10	$31.70
152.083	Lease to a public agency	*	*	*	*	*	*
152.086	Driven by handicapped persons	5	5.1	5.2	5.3	5.4	5.5
152.087	Fire trucks and ambulances	negligible	negligible	negligible	negligible	negligible	negligible
152.088	Used for religious purposes	2.2	2.3	2.3	2.4	2.4	2.5
152.089	Vehicles taxed by other law	95.6	99.4	103.4	107.5	111.8	116.3
152.091	Farm use	21.9	22.4	22.9	23.4	23.9	24.4
152.092	Transported out of state	cbe	cbe	cbe	cbe	cbe	cbe
152.093	Certain licensed child-care facilities	7.7	7.9	8	8.2	8.4	8.6
Total		$160.90	$166.20	$171.50	$177.20	$183.00	$189.00
cbe: cannot be estimated.							
*Cannot be separated from estimate of sales to a public agency. Included in the estimate for Sec. 152.082.							
Note: Totals may not add due to rounding.							

Appendix I: Cost of Motor Vehicle Sales Tax Exemptions Fiscal 2001-2006 (in millions of dollars)[301]

[301] Comptroller of Pubic Accounts, Tax Exemptions and Tax Incidence, January 2001. Located at http://www.window.state.tx.us/taxinfo/incidence/table4.html

Appendix J: Cost of School Property Tax Exemptions

School Property Tax Tax Year* 2001 to 2006 (in millions of dollars)							
Section Texas Tax Code	**Item**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**
203.2	Productivity value loss (Secs. 23.41, 23.52, 23.73 & 23.9803, Tax Code)	1,161.70	1,232.00	1,306.50	1,385.50	1,469.40	1,558.30
11.13(b)	Residence Homestead: State mandated $15,000	$944.20	$982.30	$1,021.80	$1,063.00	$1,105.90	$1,150.40
11.13(n)	Optional percentage	306.2	330	355.6	383.2	413	445
11.26	65-and-over "tax freeze" on homestead	288.9	306.4	324.9	344.6	365.4	387.5
11.13(c)	Resdidence Homestead: State mandated 65-and-over or disabled $10,000	159.3	165.7	172.4	179.3	186.5	194.1
23.23	Limitation on appraised value of homestead (10% cap)	151.5	160.7	170.4	180.7	191.6	
11.251	Freeport Property	101.4	106.8	112.6	118.6	124.9	131.6
11.13(d)	Residence Homestead: Optional over-65 or disabled	79	84.7	90.9	97.5	104.5	112.1
11.31	Pollution control property	40.3	42.2	44.1	46.2	48.3	50.6
11.28	Tax abatement	25.5	20.6	16.6	13.4	10.9	8.8
311.013	Tax Increment Financing	22.2	20.9	19.6	18.4	17.3	16.3
11.22	Disabled veterans	18	19	19.9	20.9	22	23.1
11.27	Solar and wind-powered energy devices	1.5	1.6	1.6	1.6	1.6	1.6
11.24	Historic sites	0.9	0.9	0.9	0.9	0.9	0.9

Appendix J: Cost of School Property Tax Exemptions Continued

School Property Tax Tax Year* 2001 to 2006 (in millions of dollars)							
11.146	Mineral interest having value of less than $500	0.8	0.8	0.8	0.9	0.9	0.9
11.145	Income-producing tangible personal property having value of less than $500	0.1	0.1	0.1	0.1	0.1	0.1
11.32	Certain water conservation initiatives	0	0	0	0	0	0
11.3	Nonprofit water supply or wastewater service corporation	cbe	cbe	cbe	cbe	cbe	cbe
11.271	Offshore drilling equipment not in use	cbe	cbe	cbe	cbe	cbe	cbe
11.25	Marine cargo containers	cbe	cbe	cbe	cbe	cbe	cbe
11.23	Miscellaneous exemptions	cbe	cbe	cbe	cbe	cbe	cbe
11.21	Private schools	cbe	cbe	cbe	cbe	cbe	cbe
11.2	Religious organizations	cbe	cbe	cbe	cbe	cbe	cbe
11.19	Youth spiritual, mental, and physical development organizations	cbe	cbe	cbe	cbe	cbe	cbe
11.183	Associations providing assistance to ambulatory health care centers	cbe	cbe	cbe	cbe	cbe	cbe

Appendix J: Cost of School Property Tax Exemptions

School Property Tax Tax Year* 2001 to 2006 (in millions of dollars)							
11.182	Community housing development organizations improving property for low- and moderate-income housing	cbe	cbe	cbe	cbe	cbe	cbe
11.181	Charitable organizations improving property for low-income housing	cbe	cbe	cbe	cbe	cbe	cbe
11.18	Charitable organizations	cbe	cbe	cbe	cbe	cbe	cbe
11.17	Cemeteries	cbe	cbe	cbe	cbe	cbe	cbe
11.161	Implements of farming, ranching, and timber	cbe	cbe	cbe	cbe	cbe	cbe
11.16	Farm products	cbe	cbe	cbe	cbe	cbe	cbe
11.15	Family supplies	cbe	cbe	cbe	cbe	cbe	cbe
11.14	Tangible personal property not producing income	cbe	cbe	cbe	cbe	cbe	cbe
11.12	Federal exemptions	cbe	cbe	cbe	cbe	cbe	cbe
11.111	Public Property used to provide transitional housing for indigent persons	cbe	cbe	cbe	cbe	cbe	cbe
11.11	Public property (state and local)	cbe	cbe	cbe	cbe	cbe	cbe
	Total	**$3,301.50**	**$3,474.40**	**$3,658.70**	**$3,854.70**	**$4,063.20**	**$4,284.50**

cbe: cannot be estimated because of insufficient appraisal data.
* Tax year means calendar year (January 1 through December 31).
Note: Totals may not add due to rounding.

Continued[302]

[302] Comptroller of Public Accounts, *Tax Exemptions and Tax Incidence*, January 2001. Located at http://www.window.state.tx.us/taxinfo/incidence/table36.html,

Appendix K: Cost of Selected Service Exclusions from the State Sales Tax

Cost of Selected Service Exclusions from the Sales Tax Fiscal Years 2001 to 2006 (in millions of dollars)						
	2001	**2002**	**2003**	**2004**	**2005**	**2006**
Construction Labor	$550.60	$570.20	$596.20	$628.20	$666.30	$709.90
Pesronal services	$248.10	$260.80	$274.20	$289.10	$304.60	$321.70
Business and professional services	$2,934.60	$3,124.20	$3,323.60	$3,554.80	$3,797.20	$4,083.80
Other Services	$315.40	$342	$363.60	$388.50	$414.30	$445.90
Total	**$4,054.40**	**$4,297.60**	**$4,558.00**	**$4,861.10**	**$5,183.00**	**$5,561.80**
Note: Totals may not sum because of rounding.						

Cost of Construction Labor Service Exclusions from the Sales Tax Fiscal Years 2001 to 2006 (in millions of dollars)						
	2001	**2002**	**2003**	**2004**	**2005**	**2006**
Construction labor						
New residential construction	$ 252.5	$ 261.5	$ 273.4	$ 288.1	$ 305.6	$ 325.6
New nonresidential construction	$ 216.3	$ 224.0	$ 234.2	$ 246.8	$ 261.7	$ 278.9
Residential repair and remodeling	$ 81.8	$ 84.7	$ 88.6	$ 93.3	$ 99.0	$ 105.4
	$ 550.6	**$ 570.2**	**$ 596.2**	**$ 628.2**	**$ 666.3**	**$ 709.9**
Note: Totals may not sum because of rounding.						

Appendix K:Cost of Selected Service Exclusions from the State Sales Tax Continued

Cost of Selected Service Exclusions from the Sales Tax Fiscal Years 2001 to 2006 (in millions of dollars)						
	2001	2002	2003	2004	2005	2006
Business and professional services						
Physicians services	$ 547.90	$ 583.80	$ 620.70	$ 663.10	$ 707.40	$ 761.20
Dental services	$ 176.20	$ 187.80	$ 199.60	$ 213.30	$ 227.50	$ 244.80
Other health care	$ 293.60	$ 312.80	$ 332.50	$ 355.30	$ 379.00	$ 407.90
Legal services	$ 346.10	$ 368.80	$ 392.10	$ 418.90	$ 446.90	$ 480.90
Accounting and audit services	$ 168.20	$ 179.20	$ 190.50	$ 203.60	$ 217.20	$ 233.70
Architectural and engineering services	$ 245.00	$ 261.00	$ 277.50	$ 296.50	$ 316.30	$ 340.30
Management consulting and public relations	$ 87.00	$ 92.70	$ 98.60	$ 105.30	$ 112.30	$ 120.90
Contract computer programming	$ 89.40	$ 95.30	$ 101.30	$ 108.20	$ 115.50	$ 124.30
Research and development laboratory services	$ 36.80	$ 39.20	$ 41.60	$ 44.50	$ 47.50	$ 51.10
Economic and sociological research	$ 15.40	$ 16.40	$ 17.40	$ 18.60	$ 19.80	$ 21.30
Testing labs	$ 36.60	$ 39.00	$ 41.50	$ 44.30	$ 47.30	$ 50.90
Advertising media	$ 161.10	$ 171.80	$ 182.60	$ 195.00	$ 207.80	$ 221.40
Employment agency services	$ 25.50	$ 27.20	$ 28.90	$ 30.90	$ 32.90	$ 35.40
Temporary labor supply	$ 44.50	$ 47.40	$ 50.40	$ 53.80	$ 57.40	$ 61.80
Financial services brokerage	$ 176.80	$ 188.40	$ 200.20	$ 213.90	$ 227.90	$ 242.90
Other financial services	$ 66.00	$ 68.90	$ 72.60	$ 77.10	$ 82.10	$ 87.90
Real estate brokerage and agency	$ 164.40	$ 171.60	$ 180.90	$ 192.00	$ 204.40	$ 218.80
Freight hauling	$ 213.50	$ 229.70	$ 248.80	$ 271.50	$ 295.70	$ 322.10
Other transportation (except scheduled passenger)	$ 13.20	$ 14.10	$ 14.90	$ 16.00	$ 17.00	$ 18.30
Veterinary Services	$ 27.40	$ 29.10	$ 31.00	$ 33.00	$ 35.30	$ 37.90
	$2,934.60	**$3,124.20**	**$3,323.60**	**$3,554.80**	**$3,797.20**	**$4,083.80**
Note: Totals may not sum because of rounding.						

Appendix K: Cost of Selected Service Exclusions from the State Sales Tax Continued[303]

Cost of Selected Service Exclusions from the Sales Tax Fiscal Years 2001 to 2006 (in millions of dollars)						
	2001	2002	2003	2004	2005	2006
Other Services						
Automotive maintenance and repair	$ 221.00	$ 235.50	$ 250.30	$ 267.50	$ 285.30	$ 307.00
Car washes	$ 19.00	$ 20.20	$ 21.50	$ 23.00	$ 24.50	$ 26.40
Travel arrangement	$ 30.70	$ 32.70	$ 34.80	$ 37.10	$ 39.60	$ 42.60
Private vocational education	$ 23.10	$ 24.60	$ 26.20	$ 28.00	$ 29.80	$ 32.10
Other private educational services	$ 21.60	$ 23.10	$ 24.50	$ 26.20	$ 27.90	$ 30.10
Interior design		$ 5.90	$ 6.30	$ 6.70	$ 7.20	$ 7.70
	$ 315.40	**$ 342.00**	**$ 363.60**	**$ 388.50**	**$ 414.30**	**$ 445.90**
Note: Totals may not sum because of rounding.						

Cost of Personal Service Exclusions from the Sales Tax Fiscal Years 2001 to 2006 (in millions of dollars)						
	2001	2002	2003	2004	2005	2006
Personal services						
Barber and beauty services	$ 48.3	$ 51.5	$ 54.7	$ 58.4	$ 62.3	$ 67.1
Funeral	$ 42.7	$ 45.2	$ 47.7	$ 50.6	$ 53.5	$ 56.7
Child day care	$ 144.3	$ 150.5	$ 157.2	$ 164.4	$ 171.8	$ 179.5
M iscellaneous personal services	$ 12.8	$ 13.6	$ 14.6	$ 15.7	$ 17.0	$ 18.4
	$ 248.1	**$ 260.8**	**$ 274.2**	**$ 289.1**	**$ 304.6**	**$ 321.7**
Note: Totals may not sum because of rounding.						

[303]Comptroller of Public Accounts, *Tax Exemptions and Tax Incidence,* January 2001. Located at http://www.window.state.tx.us/taxinfo/incidence/table6.html,

Appendix L: Cost of Franchise Tax Exemptions Fiscal 2001-2006[304]

Cost of Franchise Tax Exemptions Fiscal 2001-2006 (in millions of dollars)							
Section	**Exemption**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**
171.051	Grandfathered 1975	Included with IRS 501(c)(3)					
171.052	Insurance Companies	$139.00	$144.80	$151.20	$158.00	$165.10	$172.40
171.053	Railway Terminal Co	*	*	*	*	*	*
171.055	Mutual Funds	$204.60	$215.90	$229.10	$244.60	$262.00	$281.30
171.056	Solar Energy Co	$0.40	$0.40	$0.40	$0.50	$0.50	$0.50
171.057	Promote Local Area	Included with IRS 501(c)(6)					
171.058	Religious Orgs	Included with IRS 501(c)(3)					
171.059	Burial Organizations #	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
171.06	Agriculture Fairs	Included with IRS 501(c)(5)					
171.061	Educational Orgs	Included with IRS 501(c)(3)					
171.062	Public Charity	Included with IRS 501(c)(3)					
171.063	IRS Sec 501(c)(2)	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
	IRS Sec 501(c)(3)	$243.20	$249.20	$255.80	$262.80	$270.00	$277.10
	IRS Sec 501(c)(4)	$4.80	$4.90	$5.00	$5.20	$5.30	$5.50
	IRS Sec 501(c)(5)	$9.20	$9.50	$9.70	$10.00	$10.20	$10.50
	IRS Sec 501(c)(6)	$10.70	$11.00	$11.30	$11.60	$11.90	$12.20
	IRS Sec 501(c)(7)	$1.70	$1.80	$1.80	$1.90	$1.90	$2.00
	IRS Sec 501(c)(8)	$2.50	$2.60	$2.60	$2.70	$2.80	$2.90
	IRS Sec 501(c)(10)	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
	IRS Sec 501(c)(16)	*	*	*	*	*	*
	IRS Sec 501(c)(19)	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
	IRS Sec 501(c)(25)	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
171.064	Nature Conservation	Included with IRS 501(c)(3)					
171.065	Water Supply/Sewer	$0.60	$0.70	$0.70	$0.70	$0.70	$0.70
171.066	Natural Gas Facility	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
171.067	Convalescent Homes	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
171.068	Cooperative Housing	*	*	*	*	*	*
171.069	Ch 52 Ag Marketing	Included with IRS 501(c)(5)					
171.07	Lodges	Included with IRS 501(c)(8)					
171.071	Ch 51 Ag Coops	Included with IRS 501(c)(5)					
171.072	Housing Finance	Included with IRS 501(c)(3)					
171.073	Hospital Laundry	*	*	*	*	*	*
171.074	Development Corp	Included with IRS 501(c)(6)					
171.075	Health Coop	Included with IRS 501(c)(3)					
171.076	Ch 55 Ag Credit	$0	$0	$0	$0	$0	$0
171.077	State Credit Unions ##	$3.60	$3.80	$4.00	$4.20	$4.50	$4.80
171.079	Electric Coop	$13.50	$14.30	$14.90	$15.80	$16.90	$18.20
171.08	Telephone Coop	$0.80	$0.80	$0.90	$0.90	$1.00	$1.00
171.081	Title insurance firms	$1.20	$1.30	$1.30	$1.40	$1.50	$1.60
171.082	Homeowners Assn	$1.20	$1.30	$1.30	$1.40	$1.50	$1.60
171.083	EMS Corp	Included with IRS 501(c)(3)					
171.084	Trade Show	*	*	*	*	*	*
171.085	Sludge Recycling	*	*	*	*	*	*
171.086	Supercolider Org	$0	$0	$0	$0	$0	$0
171.087	Scholarship Org	Included with IRS 501(c)(3)					

[304] Comptroller of Pubic Accounts, Tax Exemptions and Tax Incidence, January 2001. Located at http://www.window.state.tx.us/taxinfo/incidence/table4.html

Appendix M: Services Subject to Connecticut Sales Tax[305]

[305] State of Connecticut of Department of Revenue, October 2002.

Service Subject to Connecticut Sales Tax		
Advertising, public relations services not related to the development of media advertising or cooperative direct mail advertising	Miscellaneous personal services, exclusive of services rendered by licensed massage therapists and licensed hypertrichologists	Renovation and repair services to existing commercial, industrial and income producing property
Business analysis, management, management consulting and public relations services	Locksmith services	Repair services to electrical or electronic devices, including, but not limited to, air-conditioning and refrigeration equipment
Cable television services	Maintenance services to real property	Repair or maintenance services to tangible personal property and contracts of maintenance, repair or warranty
Computer and data processing services	Storage Space: Effective October 1, 2002. The furnishing in Connecticut of space for storage of personal property by a person in the business of furnishing such space, excluding furnishing space used by a person for residential purposes, is subject to 6%	Sales agent services for selling tangible personal property, excluding the services of a consignee selling works of art or clothing, and the services of an auctioneer
Sales and Use Taxes on Access to the Internet and Other On-line Sales of Goods and Services, and Sales and Use Taxes on Computer-Related Services and Sales of Tangible Personal Property	Motor vehicle repairs, including any type of repair, painting or replacement to the body or operating parts of a motor vehicle	Services to industrial, commercial and income-producing real property, including, but not limited to, management, repair and renovation services, but excluding voluntary evaluation, prevention, treatment, containment or removal of hazardous waste or other
Contractor services	Painting and lettering services	Sign painting and lettering
Credit information and reporting;	Parking services, except metered space, in a lot with 30 or more spaces and valet parking at airports	Stenographic service
Employment agencies and agencies providing personnel services	Personnel training services when the training service provider is engaged by an employer to provide job-related training to personnel whose primary workplace is located in Connecticut.	Storage or mooring of any noncommercial vessel on land or in the water, except the non seasonal (November 1 through April 30) dry or wet storage or mooring of noncommercial vessels;
Exterminating services	Photographic studio services	Telecommunications services;
Flight instruction and chartering by a certificated air carrier	Piped-in music provided to business or professional establishments	Swimming pool cleaning and maintenance services
Furniture reupholstering and repair services	Prepaid Telephone Calling Services	Warranty and Service Contracts for any item of tangible personal property
Janitorial services (including the cleaning of homes, offices and commercial property)	Private investigation, protection, patrol work, watchman and armored car services, exclusive of these services provided by off-duty police officers and fire fighters;	Telephone answering services;
Landscaping and horticulture services	Radio or television repair services	Window cleaning services

State Tax Collections, FY 1985-1993									
Tax Collections	FY85	FY86	FY87	FY88	FY89	FY90	FY91	FY92	FY93
Sales Tax	4192	4330	4617	6243	6915	7589	8256	8552	9122
Oil Production Tax	1040	769	533	500	502	516	689	513	492
Natural Gas Production Tax	1123	779	645	556	667	568	663	497	683
Motor Fuels Taxes	987	1011	1273	1474	1501	1515	1509	1953	2086
Motor Vehicle Taxes	895	866	803	947	1015	1092	1073	1220	1421
Franchise Tax	856	901	874	933	680	587	597	1090	1193
Cigarette and Tobacco Taxes	374	379	371	417	428	432	637	583	617
Alcoholic Beverages Taxes	333	348	326	316	320	335	378	386	393
Insurance Companies Taxes	368	409	423	547	442	526	596	517	461
Utilities Taxes	210	198	186	185	189	198	248	218	227
Inheritance Tax	148	119	114	108	105	131	127	141	142
Hotel and Motel Tax	61	65	63	90	106	115	121	127	136
Other Taxes	136	58	40	50	37	28	28	52	38
Total Tax Collections	$10,721	$10,232	$10,266	$12,365	$ 12,906	$ 13,633	$ 14,922	$ 15,849	$ 17,011

Appendix N: Texas State Tax Collections Over Time 1985 - 2002 (Amount in billions)[306]

[306] Carole Keeton Rylander, Comptroller of Public Accounts, 2002.

Appendix O: Texas Total State Per Capita Tax Amount 2001 [307]

Total tax			Total tax per capita		
Rank	**State**	**Amount**	**Rank**	**State**	**Amount**
	United States…..	559,765,398		United States…..	1,969.44
1	California…..	90,453,746	1	Connecticut…..	3,091.99
2	New York…..	44,855,582	2	Hawaii…..	2,864.89
3	**Texas…..**	**29,422,936**	3	Delaware…..	2,731.14
4	Florida…..	24,938,748	4	Minnesota…..	2,722.00
5	Illinois…..	23,150,229	5	Massachusetts…..	2,700.18
6	Pennsylvania…..	22,562,195	6	California…..	2,621.76
7	Michigan…..	22,263,874	7	Vermont…..	2,532.64
8	Ohio…..	19,617,950	8	New York…..	2,359.41
9	New Jersey…..	19,253,297	9	Wyoming…..	2,273.96
10	Massachusetts…..	17,225,270	10	New Jersey…..	2,269.25
11	North Carolina…..	15,625,133	11	Alaska…..	2,250.30
12	Georgia…..	14,368,505	12	Michigan…..	2,228.43
13	Minnesota…..	13,534,585	13	New Mexico…..	2,188.04
14	Virginia…..	13,085,329	14	Wisconsin…..	2,178.53
15	Washington…..	12,679,410	15	Rhode Island…..	2,118.47
16	Wisconsin…..	11,768,235	16	Washington…..	2,117.48
17	Maryland…..	10,785,695	17	Maine…..	2,074.30
18	Connecticut…..	10,590,296	18	Maryland…..	2,006.58
19	Indiana…..	10,204,197	19	North Dakota…..	1,940.35
20	Missouri…..	8,837,196	20	Idaho…..	1,936.48
21	Arizona…..	8,456,739	21	Kentucky…..	1,931.08
22	Kentucky…..	7,850,908	22	North Carolina…..	1,908.70
23	Tennessee…..	[illegible]	23	West Virginia…..	1,899.58
24	Colorado…..	7,566,919	24	Illinois…..	1,854.64
25	Louisiana…..	7,193,998	25	Kansas…..	1,853.13
26	Alabama…..	6,368,026	26	Pennsylvania…..	1,836.24
27	Oklahoma…..	6,341,714	27	Oklahoma…..	1,832.81
28	South Carolina…..	6,147,594	28	Arkansas…..	1,824.21
29	Oregon…..	5,892,963	29	Virginia…..	1,820.51
30	Iowa…..	5,158,780	30	Nevada…..	1,819.61
31	Kansas…..	4,993,526	31	Utah…..	1,791.08
32	Arkansas…..	4,911,035	32	Nebraska…..	1,767.54
33	Mississippi…..	4,749,481	33	Iowa…..	1,764.71
34	Utah…..	4,065,364	34	Ohio…..	1,724.88
35	New Mexico…..	4,002,246	35	Georgia…..	1,713.82
36	Nevada…..	3,832,227	36	Colorado…..	1,712.86
37	Hawaii…..	3,507,770	37	Oregon…..	1,696.86
38	West Virginia…..	3,422,875	38	Indiana…..	1,668.79
39	Nebraska…..	3,028,204	39	Mississippi…..	1,661.80
40	Maine…..	2,668,938	40	Montana…..	1,653.86
41	Idaho…..	2,558,098	41	Louisiana…..	1,611.04
42	Rhode Island…..	2,243,295	42	Arizona…..	1,593.41
43	Delaware…..	2,174,440	43	Missouri…..	1,569.74
44	New Hampshire…..	1,775,810	44	Florida…..	1,520.98
45	Vermont…..	1,552,739	45	South Carolina…..	1,513.06
46	Montana…..	1,495,805	46	Alabama…..	1,426.42
47	Alaska…..	1,428,698	47	New Hampshire…..	1,410.29
48	North Dakota…..	1,231,049	**48**	**Texas…..**	**1,379.74**

State Tax Collections, FY 1994-2002

Tax Collections	FY94	FY95	FY96	FY97	FY98	FY99	FY00	FY01	FY02
Sales Tax	$ 9,810	$10,259	$10,791	$ 11,340	$ 12,459	$13,069	$ 13,997	$ 14,633	$ 14,476
Oil Production Tax	362	375	377	429	304	211	417	443	338
Natural Gas Production Tax	554	512	447	712	575	489	698	1,597	629
Motor Fuels Taxes	2170	2235	2321	2383	2506	2593	2688	2,743	755
Motor Vehicle Taxes	1617	1788	1965	2050	2277	2483	2782	2,906	2,946
Franchise Tax	1261	1423	1639	1797	1938	2078	2065	1,960	1,936
Cigarette and Tobacco Taxes	573	639	567	655	561	624	532	584	540
Alcoholic Beverages Taxes	400	407	419	432	456	483	515	541	560
Insurance Companies Taxes	767	608	627	706	747	812	797	820	1,046
Utilities Taxes	263	241	241	258	242	266	264	340	311
Inheritance Tax	152	172	160	208	327	256	278	322	334
Hotel and Motel Tax	146	171	176	186	207	220	236	247	231
Other Taxes	30	28	32	33	36	32	35	41	44
Total Tax Collections	$18,106	$18,859	$19,763	$ 21,188	$ 22,634	$23,615	$ 25,284	$ 25,177	$ 24,146

Appendix P: State Government Tax Collections[308]

State Government Tax Collections: 2001		
(Amounts in Thousands of Dollars Per Capita Amounts are in Dollars. Revised July 2002)		
Item	**Texas**	
	Amount	Per capita
Population (July 1, 2001, in thousands)	21,325	(X)
Personal income (Calendar year 2000, in millions)	580,736	(X)
Total taxes	29,422,936	1,379.74
Property Taxes	(X)	(X)
Sales and gross receipts	23,304,300	1,092.82
General sales and gross receipts	14,707,624	689.69
Selective sales taxes	8,596,676	403.13
Alcoholic beverages	541,305	25.38
Amusements	21,629	1.01
Insurance premiums	767,433	35.99
Motor fuels	2,766,028	129.71
Pari-mutuels	11,516	0.54
Public utilities	672,566	31.54
Tobacco products	584,461	27.41
Other selective sales	3,231,738	151.55
Licenses	3,751,486	175.92
Alcoholic beverages	32,490	1.52
Amusement	7,216	0.34
Corporation	2,030,756	95.23
Hunting and fishing	64,993	3.05
Motor vehicle	939,080	44.04
Motor vehicle operators	123,557	5.79
Public utility	16,676	0.78
Occupation and business, NEC	509,673	23.9
Other	27,045	1.27
Other taxes	2,367,150	111
Individual income	(X)	(X)
Corporation net income	(X)	(X)
Death and gift	322,355	15.12
Documentary and stock transfer	(X)	(X)
Severance	2,044,795	95.89
Other	(X)	(X)
Note: U.S. Totals, include the 50 State governments only. "X" = Not Applicable.		
Population source: Table ST-2001EST-01 - Time Series of State Population Estimates: April 1, 2000 to July 1, 2001, Population Division, U.S. Census Bureau, released December 2001.		
Personal income source: Survey of Current Business (October 2001) BEA, released September 2001		

[307] U.S. Bureau of the Cenus, and Bureau of Economic Analysis, 2001. Located at http://www.census.gov/ftp/pub/govs/statetax/01staxrank.html

[308] Tax Facts, http://www.taxpolicycenter.org/taxfacts/state/main.cfm, July 2002

Appendix Q: 75th Session, Engrossed Version H.B. No 4

ARTICLE 3. FRANCHISE TAX

SECTION 3.01. Sections 171.001(a) and (b), Tax Code, are amended to read as follows:

(a) A franchise tax is imposed on[~~:~~

[~~(1)~~] each taxable entity [~~corporation~~] that does business in this state or that is chartered, organized, or authorized to do business in this state[~~, and~~

[~~(2) each limited liability company that does business in this state or that is organized under the laws of this state or is authorized to do business in this state~~].

(b) In this chapter:

(1) "Banking corporation" means each state, national, domestic, or foreign bank, including a limited banking association, as defined by Section 1.002(a), Texas Banking Act (Article 342-1.002, Vernon's Texas Civil Statutes), and each bank organized under Section 25A [~~25(a)~~], Federal Reserve Act (12 U.S.C. Secs. 611-631) (edge corporations), but does not include a bank holding company as that term is defined by Section 2, Bank Holding Company Act of 1956 (12 U.S.C. Sec. 1841).

(2) "Beginning date" means:

(A) for a taxable entity [~~corporation~~] chartered or organized in this state, the date on which the taxable entity's [~~corporation's~~] charter or organization takes effect; and

(B) for any other taxable entity without regard to whether the entity is foreign or domestic or whether it is formally organized or chartered [~~a foreign corporation~~], the earlier of the date on which:

(I) the corporation's certificate of authority takes effect; or

(ii) the taxable entity [~~corporation~~] begins doing business in this state.

(3) "Business trust" means a trust for carrying on a business operation. [~~"Corporation" includes:~~

[~~(A) a limited liability company, as defined under the Texas Limited Liability Company Act; and~~

[~~(B) a state or federal savings and loan association.~~]

(4) "Charter" includes a limited liability company's certificate of organization, a limited partnership's certificate of limited partnership, and the registration of a limited liability partnership.

(5) "Compensation":

(A) means amounts paid to or for the benefit of an officer, director, or owner and that:

(I) are subject to withholding under the Internal Revenue Code; or

(ii) would be subject to withholding if the person were considered an employee and the amounts paid were considered salaries; and

(B) does not include funds that are received by:

(I) an entity that contracts with one or more insurance companies, health maintenance organizations, managed care organizations, employers, unions, trusts, or other public or private health care payors to arrange for the provision of health care services, directly or indirectly through contracts or subcontracts, or both, by physicians, providers, or organizations of physicians, providers, or organizations and that are retained by the entity as part of a withhold, shared fund, risk pool, stop loss, fee-for-service, risk-sharing, capitated risk, contingency reserve, or similar arrangement to be distributed to the participating physicians, providers, or organizations, except to the extent the participating physicians, providers, or organizations are not taxable under this chapter; or

(ii) an agent for a principal to the extent the funds are to be distributed to the principal.

(6) "Does business in this state" means the taxable entity is subject to taxation by this state without the state violating the United States Constitution and the federal law adopted under the United States Constitution.

(7) "Income or equity partner" includes a partner who is entitled to a distributive share of the partnership's income or loss or who becomes entitled to a share of the partnership's assets or liabilities on termination of the partnership.

(8) "Internal Revenue Code" means the Internal Revenue Code of 1986 in effect for the federal tax year beginning on or after January 1, 1996 [~~1994~~], and before January 1, 1997 [~~1995~~], and any regulations adopted under that code applicable to that period.

(9) [~~(6)~~] "Officer" and "director" include a limited liability company's directors and managers, [~~and~~] a limited banking association's directors and managers and participants if there are no directors or managers, and persons holding comparable positions of authority in a noncorporate taxable entity.

(10) "Owner" includes a shareholder, an income or equity partner of a partnership, and an owner of equity in any other taxable entity.

(11) "Passive income" means:

(A) interest;

(B) dividends;

©) rents;

(D) royalties, including overriding royalties;

(E) income from the disposition of a capital asset or property held for investment;

(F) income from any of the following entities or any entity controlled, directly or indirectly, by any of the following entities:

(I) a real estate investment trust;

(ii) a regulated investment company;

(iii) a real estate mortgage investment conduit; or

(iv) a common trust fund; or

(G) income from oil and gas working interests held by the taxable entity if the taxable entity is not an operator of oil and gas properties.

(12) "Passive income asset" means an asset owned by a taxable entity if any income generated by the asset, including on disposition of the asset, is passive income.

(13) "Passive income capital" for a taxable entity means an amount that is the product of the passive income ratio for the taxable entity and the entity's apportioned taxable capital under Section 171.101(d)(3).

(14) "Passive income ratio" means the ratio, expressed as a percentage, in which:

(A) the numerator is the aggregate cost of all of the taxable entity's passive income assets; and

(B) the denominator is the aggregate cost of the taxable entity's total assets.

(15) [~~(7)~~] "Savings and loan association" includes a state or federal savings bank.

(16) [~~(8)~~] "Shareholder" includes a limited liability company's member and a limited banking association's participant.

(17) "Taxable entity" does not include a sole proprietorship. "Taxable entity" means:

(A) a banking corporation;

(B) a business trust that is required to file a federal tax return as a corporation or a partnership other than a self-insurance trust not engaged in the business of insurance and formed under Article 21.49-4, Insurance Code;

©) a corporation;

(D) a limited liability company;

(E) a limited liability partnership;

(F) a limited partnership;

(G) a partnership that is required to file a federal tax return as a corporation or a partnership;

(H) a registered limited liability partnership;

(I) a state or federal savings and loan association;

(J) a professional association;

(K) a professional corporation; and

(L) any other kind of business association, joint venture, or other combination of entities or persons engaged in business, other than an oil and gas joint operating agreement.

Appendix R: Selected State Taxes: Changes in base and rate--an update, October 2002

Originally Prepared in 1997 for the House Committee on Revenue and Public School Finance. Update based on Comptroller Tax Exemptions & Tax Incidence publication (Jan. 2001), as well as extrapolations of estimates prepared in 1997.

Note: Unless specifically stated, estimates reflect full years; no adjustments for implementation of tax laws assumed. Estimates reflect static changes only, no dynamic economic effects included. Totals may not add due to rounding.

Selected State Taxes: Changes in base and rate--an update, October 2002					
			(in millions)		
	2003	**2004**	**2005**	**2004-05**	**2006**
Expand base to include accounting & audit services	190.5	203.6	217.2	420.8	233.7
Expand base to include advertising media services	182.6	195.0	207.8	402.8	221.4
Eliminate exemptions for agricultural items	308.5	314.3	322.3	636.6	329.9
Broaden base to include aircraft repair equipment	18.9	20.6	22.5	43.1	24.5
Expand base to include automotive maintenance and repair labor	250.3	267.5	285.3	552.8	307.0
Expand base to include barber & beauty services	54.7	58.4	62.3	120.7	67.1
Expand base to include car wash services	21.5	23.0	24.5	47.5	26.4
Expand base to include coin-operated services	39.4	42.0	44.8	86.8	48.2
Expand base to include contract computer programming services	101.3	108.2	115.5	223.7	124.3
Broaden base to include child day care services	157.2	164.4	171.8	336.2	179.5
Expand base to include dental services	199.6	213.3	227.5	440.8	244.8
Expand base to include employment agency services	28.9	30.9	32.9	63.8	35.4
Expand base to include engineering & architectural services	277.5	296.5	316.3	612.8	340.3
Repeal provision authorizing refunds on certain items for a Texas Department of Economic Development designated enterprise project	4.7	5.0	5.3	10.3	5.7
Expand base to include "other" health care services	332.5	355.3	379.0	734.3	407.9
Expand base to include physicians services	620.7	663.1	707.4	1,370.5	761.2
Expand base to include interior design services	6.7	7.2	7.7	14.9	8.3
Expand base to include legal services	392.1	418.9	446.9	865.8	480.9
Repeal exemption for subscription sales of magazines	7.0	7.4	7.9	15.3	8.5
Expand base to include management consulting & public relations services	98.6	105.3	112.3	217.6	120.9
Broaden base to include manufacturing machinery & equipment	563.1	603.7	647.6	1,251.3	692.8
Broaden base to include motor fuels now excluded under Tax Code, Section 151.308	1,255.8	1,334.8	1,418.0	2,752.8	1,507.4

Appendix R: Selected State Taxes: Changes in base and rate--an update, October 2002

Note: Unless specifically stated, estimates reflect full years; no adjustments for implementation of tax laws assumed. Estimates reflect static changes only, no dynamic

Selected State Taxes: Changes in base and rate--an update, October 2002					
			(in millions)		
	2003	**2004**	**2005**	**2004-05**	**2006**
Repeal exemption for newspaper inserts	25.8	27.6	29.6	57.2	31.7
Broaden base to include single copy and subscription sales of	19.0	20.4	21.9	42.3	23.4
Broaden base to include the sale of items to non-profit organizations other than governmental entities	18.3	19.5	20.8	40.3	22.4
Broaden base to include the labor costs on new non-residential construction	234.2	246.8	261.7	508.5	278.9
Expand base to include manufacturing use of packaging & wrapping materials	123.4	132.2	141.9	274.1	151.8
Expand base to include miscellaneous personal services	14.6	15.7	17.0	32.7	18.4
Repeal exemption for prescription & O-T-C drugs, and medical devices	375.1	407.1	441.4	848.5	478.6
Repeal exemption for railroad fuel and supplies	7.4	8.1	8.8	16.9	9.6
Expand base to include railroad rolling stock and locomotives used in the state	2.3	2.5	2.7	5.2	2.9
Expand base to include commercial research & development laboratory services	41.6	44.5	47.5	92.0	51.1
Expand base to include commercial economic, social or educational research services	17.4	18.6	19.8	38.4	21.3
Expand base to include labor costs for new residential construction	273.4	288.1	305.6	593.7	325.6
Expand base to include labor costs of repair or remodeling of residential real property	88.6	93.3	99.0	192.3	105.4
Repeal exemption for school lunches and food sold to hospital patients, residents of retirement homes or during church functions	39.3	41.9	44.7	86.6	48.0
Repeal exemption for certain ships and ship equipment	39.5	43.0	46.9	89.9	51.1
Expand base to include temporary labor supply services	50.4	53.8	57.4	111.2	61.8

Appendix R: Selected State Taxes: Changes in base and rate--an update, October 2002

Note: Unless specifically stated, estimates reflect full years; no adjustments for implementation of tax laws assumed. Estimates reflect static changes only, no dynamic economic effects included. Totals may not add due to rounding.

Selected State Taxes: Changes in base and rate--an update, October 2002					
			(in millions)		
	2003	2004	2005	2004-05	2006
Expand base to include testing services provided by non-medical laboratories	41.5	44.3	47.3	91.6	50.9
Repeal partial exemption for certain items of equipment used in timber operations	6.5	8.8	10.6	19.4	13.7
Expand base to include miscellaneous transportation services	14.9	16.0	17.0	33.0	18.3
Repeal partial exemption for food items sold through vending machines	negligible	negligible	negligible	negligible	negligible
Expand base to include veterinary services	31.0	33.0	35.3	68.3	37.9
Expand base to include vocational and other private education services	50.7	54.2	57.7	111.9	62.2
Repeal exemption to include aviation fuel	78.2	83.7	89.3	173.0	95.3
Repeal exemption to include agricultural containers	0.4	0.4	0.4	0.8	0.4
Repeal exemption for water	219.4	224.6	230.3	454.9	236.4
Broaden base to include refrigerated warehousing & storage (includes food locker rental, cold or frozen storage)	2.7	2.8	2.9	5.7	3.0
Broaden base to include general warehousing & storage (includes mini-warehouses and self-storage warehouses)	8.0	8.4	8.7	17.1	9.0
Broaden base to include special warehousing & storage	8.7	9.1	9.5	18.6	9.9
Broaden base to include marinas	1.4	1.5	1.6	3.1	1.7
Broaden base to include appraisal services including real estate & other (insurance appraisal currently taxable)	6.0	6.3	6.6	12.9	6.9
Broaden base to include mailing services (includes addressing, packaging and labeling services) & secretarial services (includes letter & resume writing services & proofreading services)	6.8	7.1	7.4	14.5	7.7
Broaden base to include disinfecting services (includes sanitizing services)	0.6	0.6	0.6	1.2	0.6
Broaden base to include amusement services of all entities except for school districts	2.8	2.9	3.0	5.9	3.1
Subtotal Sales & Use Tax	**6,962**	**7,405.2**	**7,877.7**	**15,282.9**	**8,415.1**

Appendix R: Selected State Taxes: Changes in base and rate--an update, October 2002

Note: Unless specifically stated, estimates reflect full years; no adjustments for implementation of tax laws assumed. Estimates reflect static changes only, no dynamic economic effects included. Totals may not add due to rounding.

Appendix R: Selected State Taxes: Changes in base and rate--an update, October 2002

Note: Unless specifically stated, estimates reflect full years; no adjustments for implementation of tax laws assumed. Estimates reflect static changes only, no dynamic economic effects included. Totals may not add sue to rounding.

Selected State Taxes: Changes in base and rate--an update, October 2002					
			(in millions)		
	2003	**2004**	**2005**	**2004-05**	**2006**
Add noncorporate entities with $100,000 owner deduction (excluding sole proprietors) (assumed eff. date: Jan. 1, 2004)	-	233.9	322.8	556.7	352.0
Repeal exemption for open-end investment companies (mutual funds)	229.1	244.6	262.0	506.6	281.3
Repeal exemption for title insurance companies	1.3	1.4	1.5	2.9	1.6
Repeal exemption for solar energy businesses	0.4	0.5	0.5	1.0	0.5
Repeal exemption for trade show participants	negligible	negligible	negligible	negligible	negligible
Repeal exemption for sludge recycling firms	negligible	negligible	negligible	negligible	negligible
Remove deduction for interest earnings on federal securities	56.5	58.0	59.6	117.6	61.2
Remove deduction for officer/director compensation add-back exemption for 35-or-less-shareholder corporations	207.2	219.7	235.0	454.7	251.9
Remove deduction for food and medicine receipts	4.0	4.3	4.6	8.9	4.9
Remove deduction for business loss carryover	208.1	208.1	208.1	416.2	208.1
Remove deduction for investment in enterprise zones	3.9	3.9	3.9	7.8	3.9
Remove deduction for purchase of solar energy devices	negligible	negligible	negligible	negligible	negligible
Remove deduction for firms with tax liability of less than $100	52.2	55.5	59.4	114.9	63.7
Repeal exemption from GAAP accounting methods for corporations with less than $1 million in taxable capital (partially taxed under Franchise Tax Item 1)	15.3	16.2	17.3	33.5	18.6
Repeal regulated investment company special apportionment method	3.9	3.9	3.9	7.8	3.9
Eliminate transportation company special apportionment method	12.2	13.0	13.9	26.9	14.9
Eliminate telephone company special apportionment method	9.8	10.4	11.1	21.5	11.9
Repeal temporary (FAS 96) credit	0.4	0.3	0.3	0.6	0.3
Treat receipts from trademarks, licenses and franchises similarly to patents, royalties and copyrights - based on use in Texas	3.0	3.0	3.0	6.0	3.0
Subtotal Franchise Tax - For Profit Corporations	**807.3**	**1,076.7**	**1,206.9**	**2,283.6**	**1,281.7**

Selected State Taxes: Changes in base and rate--an update, October 2002					
			(in millions)		
	2003	**2004**	**2005**	**2004-05**	**2006**
Gas, Electric & Water Utility Tax rates (3 applicable rates, all based on city population) increased to 200 percent of current-law levels.	255.0	255.0	255.0	510.0	255.0
Subtotal: Utility Taxes	**255.0**	**255.0**	**255.0**	**510.0**	**255.0**
Oil and Gas Well Servicing Tax (under sales tax)	8.6	9.0	9.4	18.4	9.8
Subtotal: Other Production and Gross Receipts Taxes	**8.6**	**9.0**	**9.4**	**18.4**	**9.8**
Interstate Motor Carriers Sales and Use Tax	25.7	27.0	28.1	55.1	29.2
Manufactured housing sales and use tax (rate at 6.25% of 65% of price)	13.3	14.0	14.6	28.6	15.2
Subtotal: Motor Vehicle Sales/Rental Manufactured Housing Sales	**39.0**	**41.0**	**42.7**	**83.7**	**44.4**
Hotel and motel tax rate increase to 6.25%	9.6	10.0	10.4	20.4	10.8
Repeal 30-day exemption	3.0	3.1	3.2	6.3	3.4
Subtotal: Hotel and Motel Tax	**12.6**	**13.1**	**13.6**	**26.7**	**14.2**
Rate increase of 10 cents per pack (assumed eff. date: Sept. 1, 2003)	-	88.3	108.9	197.2	96.0
Rate increase of 41 cents per pack (assumed eff. date: Sept. 1, 2003)	-	341.5	420.1	761.6	370.2
Rate increase of 50 cents per pack (assumed eff. date: Sept. 1, 2003)	-	406.6	499.6	906.2	440.3
Rate increase of 100 cents per pack (assumed eff. date: Sept. 1, 2003)	-	682.9	829.4	1,512.3	730.4
Subtotal: Cigarette and Tobacco Products Taxes	**-**	**n.a.**	**n.a.**	**n.a.**	**n.a.**
Increase alcohol excise tax for liquor by 10 percent	3.5	3.7	3.8	7.5	3.9
Increase alcohol excise tax for beer by 10 percent	9.8	10.3	10.7	21.0	11.1
Increase alcohol excise tax for wine by 10 percent	0.6	0.6	0.6	1.2	0.6
Increase alcohol excise tax for ale by 10 percent	0.6	0.6	0.6	1.2	0.6
Subtotal: Alcoholic Beverages Taxes	**14.5**	**15.2**	**15.7**	**30.9**	**16.2**

Appendix R: Selected State Taxes: Changes in base and rate--an update, October 2002

Note: Unless specifically stated, estimates reflect full years; no adjustments for implementation of tax laws assumed. Estimates reflect static changes only, no dynamic economic effects included. Totals may not add due to rounding.

Selected State Taxes: Changes in base and rate--an update, October 2002					
			(in millions)		
	2003	**2004**	**2005**	**2004-05**	**2006**
Broaden base to include religious, educational, charitable, civic and welfare. 501(c)(3)	255.8	262.8	270.0	532.8	277.1
Broaden base to include labor and agricultural. 501(c)(5)	9.7	10.0	10.2	20.2	10.5
Broaden base to include business development and promotion. 501(c)(6)	11.3	11.6	11.9	23.5	12.2
Broaden base to include social and recreational. 501(c)(7)	1.8	1.9	1.9	3.8	2.0
Broaden base to include co-operative organizations, nec. 501(c)(8)	2.6	2.7	2.8	5.5	2.9
Subtotal Franchise Tax - Non-Profit Corporations	**281.2**	**289.0**	**296.8**	**585.8**	**304.7**
Repeal exemption for aviation use - item taxable @ 1 cent/gallon	22.0	24.0	25.1	49.1	26.0
Repeal exemption for railway engine use - item taxable @ 1 cent/gal.	3.4	3.7	3.9	7.6	4.1
Repeal exemption for agricultural use - this item taxable @ 1 cent/gal.	2.4	2.6	2.8	5.4	2.9
Repeal exemption for industrial & commercial use - item taxable @ 1 cent/gal.	1.5	1.6	1.7	3.3	1.8
Repeal exemption for marine use - item taxable @ 1 cent/gal.	1.3	1.4	1.4	2.8	1.5
Repeal exemption for construction use - item taxable @ 1 cent/gal.	0.5	0.6	0.6	1.2	0.7
Subtotal Motor Fuel Taxes	**31.1**	**33.9**	**35.5**	**69.4**	**37.0**
Liquefied gas tax increase rate to 30 cents per gallon	0.8	0.7	0.7	1.4	0.7
Gasoline and diesel tax increase rate to $.30/gal.	1,304.1	1,349.5	1,391.6	2,741.1	1,431.3
Subtotal Motor Fuels Rates	**1,304.9**	**1,350.2**	**1,392.3**	**2,742.5**	**1,432.0**
Increase insurance premium tax rates	116.1	122.0	126.9	248.9	131.7
Examination fee and overhead assessment credits	9.2	9.7	10.1	19.8	10.5
Life and Health: Valuation fees (domestic life only)	2.9	3.0	3.1	6.1	3.2
Subtotal Insurance Premium Taxes	**128.2**	**134.7**	**140.1**	**274.8**	**145.4**
Cement tax rate increase from .0275 to .0375	2.5	2.6	2.7	5.3	2.8
Subtotal: Cement Tax	**2.5**	**2.6**	**2.7**	**5.3**	**2.8**

Appendix S: Constitutional/Statutory Authority and Allowable Tax Rates for Major Taxes Imposed by Local Jurisdictions in Texas

CONSTITUTIONAL/STATUTORY AUTHORITY AND ALLOWABLE TAX RATES FOR MAJOR TAXES IIMPOSED BY LOCAL JURISDICTIONS IN TEXAS				
Jurisdiction	**Name of Tax**	**Tax Rate**	**Taxing Authority**	**Comments**
CITIES	**City Sales and Use Taxes**			
	Sales tax for general revenue	1%	§321.101, 103 Tax Code	
	Sales tax for economic development	up to 0.5%	Art. 5190.6, §4A, §4B VTCS	
	Sales tax to reduce property taxes	up to 0.5%	§321.101, 103 Tax Code	
	Sales tax for street maintenance	0.25%	§327.003-004 Tax Code	Must be reauthorized by voters after 4 years
	Sales tax for venue project	up to 0.5%	§334.081, 083 Local Govt Code	
	Sales tax for mass transit	up to 0.5%	§453.401 Transportation Code	
	City Property Taxes			
	Property tax, general law cities (<= 5,000 pop when created)	up to $1.50/$100 valuation	Art. XI §4, Tx.Constitution	Some have more restrictive tax rate limits by statute
	Property tax, home rule cities (> 5,000 pop)	up to $2.50/$100 valuation	Art. XI §5, Tx.Constitution	
	Property tax--seawalls	none specified in Constitution	Art. XI §7, Tx.Constitution	Only for cities/counties along Gulf Coast
	Property tax--operation of port	up to $0.10/$100 valuation--M&O	§54.004 Transportation Code	Only for cities along Gulf Coast > 5,000 population
	City Hotel Occupancy Taxes			
	Hotel occupancy tax	up to 7%	§351.002, 0025, 003 Tax Code	Rate may be 9% for certain cities to fund convention facilities
	Hotel occupancy tax for venue project	up to 2%	§334.252, 254 Local Govt Code	
	City Miscellaneous Taxes			
	Admissions tax on tickets sold at venue project	up to 10%	§334.151-152 Local Govt Code	
	Facility use tax on members of sports teams	up to $5,000 per player per game	§334.302-303 Local Govt Code	
	Motor vehicle rental tax for venue project	up to 5%	§334.102-103 Local Govt Code	
	Parking tax on event parking at venue facility	up to $3 per vehicle	§334.201-202 Local Govt Code	
	Coin-operated machine occupation tax	up to $15 per machine per year	§2153.451 Occupations Code	Tax may not exceed 1/4 of state rate which is $60 per year

Appendix S: Constitutional/Statutory Authority and Allowable Tax Rates for Major Taxes Imposed by Local Jurisdictions in Texas

CONSTITUTIONAL/STATUTORY AUTHORITY AND ALLOWABLE TAX RATES FOR MAJOR TAXES IMPOSED BY LOCAL JURISDICTIONS IN TEXAS				
Jurisdiction	**Name of Tax**	**Tax Rate**	**Taxing Authority**	**Comments**
Counties	**County Sales and Use Tax**			
	Sales tax to reduce property tax--city present	0.5%	§323.101, 103 Tax Code	Only if county is not in territory of transit provider
	Sales tax to reduce property tax--no city present	1%	§323.101, 103 Tax Code	Only if county is not in territory of transit provider
	Sales tax for hospital/health services district	0.5%	§324.021-022 Tax Code	Only in counties <= 50,000 population
	Sales tax for crime control and prevention district	up to 0.5%	§323.105 Tax Code; §363.055 Local Govt Code	Only in counties > 130,000 population and in cities in counties > 5,000 population
	Sales tax for landfill and criminal detention center	0.5%	§325.021-022 Tax Code	Only in counties <= 48,000 population with cities > 22,000 bordering Rio Grande
	Sales tax for venue projects	up to 0.5%	§334.081, 083 Local Govt Code	
	County Property Taxes			
	Property tax--general fund (and other special levies)	up to $0.80/$100 valuation	Art. VIII §9, Tx.Constitution	
	Property tax--farm-to-market roads/flood control	up to $0.30/$100 valuation	Art. VIII §1-a, Tx.Constitution; §256.051, 054 Transportation Code	
	Property tax--special road and bridge tax	up to $0.15/$100 valuation	Art. VIII §9, Tx.Constitution; §256.052 Transportation Code	Also applies to road district or to portion of county specified by commissioners court
	Property tax--seawalls	no limit specified	Art. XI §7, Tx.Constitution	Only for cities/counties along Gulf Coast
	County Hotel Occupancy Taxes			
	Hotel occupancy tax for certain counties	2%-8%, depending on county	§352.002-003 Tax Code	Numerous conditions apply
	Hotel occupancy tax for venue project	up to 2%	§334.252, 254 Local Govt Code	
	County Miscellaneous Taxes			
	Admissions tax on tickets sold at venue project	up to 10%	§334.151-152 Local Govt Code	
	Facility use tax on members of sports teams	up to $5,000 per player per game	§334.302-303 Local Govt Code	
	Motor vehicle rental tax for venue project	up to 5%	§334.102-103 Local Govt Code	
	Parking tax on event parking at venue facility	up to $3 per vehicle	§334.201-202 Local Govt Code	
	Coin-operated machine occupation tax	up to $15 per machine per year	§2153.451 Occupations Code	Tax may not exceed 1/4 of state rate which is $60 per year

Appendix S: Constitutional/Statutory Authority and Allowable Tax Rates for Major Taxes Imposed by Local Jurisdictions in Texas

CONSTITUTIONAL/STATUTORY AUTHORITY AND ALLOWABLE TAX RATES FOR MAJOR TAXES IMPOSED BY LOCAL JURISDICTIONS IN TEXAS				
Jurisdiction	**Name of Tax**	**Tax Rate**	**Taxing Authority**	**Comments**
School	**School District Taxes**			
	Property tax	up to $1.50/$100 valuation for M&O; attorney general will not approve bonds if district's total debt rate will exceed $0.50/$100 valuation	§45.001-0031 Education Code	Voters may approve a higher M&O rate in certain districts
Special	**County Development Districts**			
	Hotel occupancy tax (outside municipality)	up to 7%	§352.107 Tax Code	Only for counties < 600,000 population
	Sales tax	up to 0.5%	§383.101 Local Govt Code	Only for counties < 400,000 population
	Emergency Services Districts			
	Emergency Services Districts: Property tax	up to $0.10/$100 valuation	Art. III §48-e, Tx.Constitution; §775.074, §776.075 Health & Safety Code	
	Property tax	up to $0.03/$100 valuation	§775.0741 Health & Safety Code	Only for counties > 2.4 million population
	Property tax	up to $0.06/$100 valuation	§775.0741 Health & Safety Code	Applies to a district converted from a rural fire prevention district in a county > 2.4 million population
	Emergency Services Districts: Sales tax	up to 2%	§775.0751, §776.0751 Health & Safety Code	
	Fire Control, Prevention, & Emergency Medical Services	up to 0.5%	§344.055 Local Govt Code	Only for cities with a population of 25,000-550,000 or a city >= 1.9 million
	Districts: Sales tax			population; applies only to districts created by cities
	Rural Fire Prevention Districts: Property tax	up to $0.03/$100 valuation	Art. III §48-d, Tx.Constitution; §794.031 Health & Safety Code	Up to $0.05/$100 in Harris County

Appendix S: Constitutional/Statutory Authority and Allowable Tax Rates for Major Taxes Imposed by Local Jurisdictions in Texas

CONSTITUTIONAL/STATUTORY AUTHORITY AND ALLOWABLE TAX RATES FOR MAJOR TAXES IMPOSED BY LOCAL JURISDICTIONS IN TEXAS				
Jurisdiction	**Name of Tax**	**Tax Rate**	**Taxing Authority**	**Comments**
Special	**Hospital Districts**			
	Property tax	up to $0.75/$100 valuation	Art. IX §9-11, Tx. Constitution; §281.121, §286.161 Health & Safety Code	
	Sales tax for property tax relief	up to 2%	§285.061 Health & Safety Code	
	Sales tax for general revenue	up to 2%	§285.161 Health & Safety Code	Only in counties < 75,000 population
	Jail Districts			
	Property tax	no limit specified	§351.158 Local Govt Code	
	Junior College Districts			
	Property tax	up to $0.50/$100-debt service; up to $1.00/$100 valuation total tax rate	§130.122 Education Code	Voters of each district set maximum tax rate not to exceed statutory limits
	Library Districts			
	Sales tax	up to 0.5%	§326.021, 093 Local Govt Code	Only in counties > 100,000 population; may not include city if city operates a public library; not allowed in certain transit
	Mosquito Control Districts			
	Property tax	up to $0.25/$100 valuation	§344.001 Health & Safety Code	
	Municipal Development Districts			
	Sales tax	up to 0.5%	§377.021, 103 Local Govt Code	Only in cities located in two or more counties
	Municipal Management Districts			
	Property tax	not specified	§375.091 Local Govt Code	District has same taxing powers as water districts, road districts, road district toll roads, and road utility districts

Appendix S: Constitutional/Statutory Authority and Allowable Tax Rates for Major Taxes Imposed by Local Jurisdictions in Texas

CONSTITUTIONAL/STATUTORY AUTHORITY AND ALLOWABLE TAX RATES FOR MAJOR TAXES IMPOSED BY LOCAL JURISDICTIONS IN TEXAS				
Jurisdiction	**Name of Tax**	**Tax Rate**	**Taxing Authority**	**Comments**
Special	**Transit and Transportation Authorities**			
	Sales tax	up to 1%; 0.5% in certain areas	§451.404, §452.401, §457.301, §460.551 Transportation Code	§457.301 limits tax to 0.5% in certain counties with cities > 500,000 population
	Water Districts and Water-related and Conservation-related Districts			Some such districts created by local law have their own property tax authority
	Drainage Districts--Property tax	unlimited rate	Chapters 49 and 56 Water Code	Numerous sections apply.Tax may not exceed 0.5% of total assessed value in districts operating under Art. III, §52 Tx. Constitution
	Fresh Water Supply Districts--Property tax	unlimited rate	§53.188 Water Code	
	Groundwater Conservation Districts--Property tax	$0.50/$100 valuation-M&O	Chapter 36 Water Code	Numerous sections apply
	Irrigation Districts--Property tax	unlimited rate	Chapters 49 and 58 Water Code	Numerous sections apply
	Levee Improvement Districts--Property tax	unlimited rate	§57.251, 57.258 Water Code	
	Municipal Utility Districts--Property tax	unlimited rate	Chapters 49 and 54 Water Code	Numerous sections apply
	Water Control and Improvement Districts--Property tax	unlimited rate	Chapters 49 and 51 Water Code	Numerous sections apply
	Water Import Authorities--Property tax	$0.50/$100 valuation	Chapters 49 and 64 Water Code	This is a local law district; district may not currently exist
	Water Improvement Districts--Property tax	unlimited rate	Chapters 49 and 55 Water Code	Numerous sections apply