

## SB 407, 80<sup>th</sup> Regular Session 2007

In the interim before the 81<sup>st</sup> Regular Session in 2009, there is much discussion of swapping property taxes for sales taxes. Therefore, it is relevant to address Senate Bill (SB) 407 from the 80<sup>th</sup> Legislature which was passed by the Texas Senate, but not by the House, in 2007.

The Senate's bill analysis stated, "As proposed, S.B. 407 authorizes cities and counties, contingent on voter approval, to impose an additional one-fourth percent sales tax for property tax relief. The sales tax revenue would reduce local property taxes through the existing 'Truth in Taxation' formula found in §26.041, Tax Code."<sup>1</sup> While this summary encapsulates the intent of the bill, it does not capture the full impact.

SB 407 would have reduced property taxes in two ways. First, §26.041(a) and (b)<sup>2</sup> of the Tax Code already requires cities and counties to reduce their property tax levies by one dollar for each dollar of revenue generated by the sales tax when calculating both their effective and rollback tax rates. Second, SB 407 would have reduced the multiplier used in calculating the rollback rate from 1.08 to 1.05 in those cities and counties that adopted the new sales tax. As a result, there would be significant impacts to local governments:

1. **Provide an alternative revenue source for some local governments.** Some counties and cities would be able to reduce their reliance on the property tax. However, many locations do not have significant retail activity, limiting the usefulness of a local sales tax. Also, in many of the areas with little retail activity, the amount of sales tax that could be collected would reduce the total property tax levy by only a relatively small amount. Estimates prepared by TAC using data on the *gross sales subject to the state sales tax for the period ending June 30, 2007*,<sup>3</sup> show that the potential sales tax revenue is less than five percent of the 2006 property tax levy in 131 counties.

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<sup>1</sup> Senate Research Center, *Bill Analysis of S.B. 407 as Filed*, (Austin, TX: SRC, 18 April 2007).  
<http://www.legis.state.tx.us/tlodocs/80R/analysis/html/SB004071.htm>

<sup>2</sup> §26.041(a) covers the first year a local sales tax is implemented and (b) covers subsequent years.

<sup>3</sup> Texas Comptroller of Public Accounts.

2. **Revenue cap reduced to five percent.** See the *Perryman Report*, for example, on the harmful impact of adopting a more stringent revenue cap/rollback rate.<sup>4</sup>
3. **Sales tax revenue is volatile.** Local governments that have a sales tax use estimates of the expected revenue to determine the rollback rate. The volatility of sales tax revenue could cause a ratchet effect during down periods of the business cycle that would be exacerbated by the reduced rollback rate multiplier.<sup>5</sup> A ratchet effect was best described by former Colorado Gov. Bill Owens in a newspaper article: "...It's as though a reservoir, drained during a drought, was not allowed to refill even after the rains returned."

As a last consideration, SB 407 would have allowed five percent of the registered voters to require the county to call an election to adopt the quarter cent sales tax.

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<sup>4</sup> The Perryman Group, *The Impact of Potential Restraints on Local Government Activity (Appraisal Caps, Expenditure Limits, and Revenue Limits) on the Economy of Texas*. (Waco, TX: TPG, March 2005)  
<http://www.county.org/taxcap/documents/PerrymanReport-Final-3-09-05.pdf>

<sup>5</sup> See the report from The Perryman Group for information on the ratchet effect of revenue caps.