

# **THE BIG TEXAS PROPERTY TAX RELIEF PACKAGE— WHAT’S DONE, WHAT NEEDS TO BE DONE AND THE CONFUSION TO FOLLOW.**

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After years of straining through tight budgets, the Texas Legislature found itself with a \$32.7 billion surplus. This windfall resulted from new sales tax revenue engendered by the \$2 trillion federal Coronavirus Aid, Relief, and Economic Security Act as well as a surge in oil and gas severance taxes. The legislature dedicated \$18 billion of the surplus to taxpayer school district property tax relief. (*Factually, only \$13 billion of the \$18 billion is from the surplus. \$5 billion of relief was mandated by legislation in 2019.*) But that was the *easy* part. It took legislators an entire regular legislative session and two special sessions to determine how and to whom to deliver tax relief. And even then, a significant portion of the relief is contingent on voter approval of a constitutional amendment at an election scheduled for November 7<sup>th</sup>, 2023. Thirteen other amendments are also on the ballot; many pertaining to how to spend the rest of the surplus budget.

## **RELIEF FOR EVERYONE!**

School district *ad valorem* property taxes are divided into two categories: (1) maintenance and operation taxes (M&O) and (2) interest and sinking taxes (I&O). M&O taxes are used to pay for day-to-day operations while I&O taxes are used for construction of school buildings and facilities. School district resident voters, not the legislature, determine whether their districts will issue bonds (the repayment of which is funded by I&O taxes) to build new facilities. M&O maximum tax rates are constrained by legislative action.

The new legislation “compresses” or reduces the maximum tax rate school district may use. State funds compensate school districts for any property tax revenue lost due to rate compression. The calculation of annual rate compression is specified in the new legislation. M&O tax rates vary by districts—but all M&O rates will be reduced by 10.7¢ for tax year 2023. This reduction applies to all property taxpayers: homeowners and businesses, and to both real and personal property. This relief does not require voter approval and is in place now.

## **BONUS RELIEF FOR HOMEOWNERS!**

Homeowners are entitled to reduce the market or taxable value of their homes through homestead exemptions. If the constitutional amendment is approved by the voters at the November election, the new homestead tax exemption will be \$100,000. If passed, this will be the third homestead tax exemption increase in eight years. In that period, voters have increased the exemption from \$15,000 to \$25,000 to \$40,000 and now, potentially to \$100,000. (*Although \$100,000 may seem like a significant exemption amount, exemptions of \$100,000 and higher are commonplace in other states.*) Currently, elderly and disabled homestead owners are entitled to an additional \$10,000 exemption. That will remain unchanged. If school districts currently offer additional homestead exemptions, they are prohibited from reducing them.

## **ADJUSTMENTS TO TAX FREEZES FOR THE ELDERLY AND DISABLED**

Texas recognizes the financial burdens faced by elderly (people aged 65 and older) and disabled homeowners. It affords them additional tax relief on their homesteads in the form of a tax freeze on school district taxes. (*Counties and cities are allowed to also grant tax freezes.*) This relief “freezes” or stops increases of the amount of property taxes due commencing in the year the owner turns 65 or becomes disabled. Unless an owner makes improvements to their home, the “frozen” taxes remain in place until they no longer reside in the homestead, regardless of any value increases of their homes. Following previous homestead exemption increases, voters opted to extend the benefit of the increased homestead exemptions to homeowners whose taxes were frozen. This did not occur after the most recent election when the homestead exemption was increased from \$25,000 to \$40,000. That will be cured if the constitutional amendment passes. Tax freezes will be retroactively adjusted to the increased exemptions from the last election and the current election.

## **YOU BETTER VOTE!**

The legislature has instructed tax assessors to bill 2023 taxes under the assumption that the constitutional amendment will pass. They are required to include an explanation that *if* the amendment fails, a supplemental tax bill will be sent to homestead owners for the additional taxes that would have otherwise been due. Regular taxes are due by January 31. Supplemental taxes, if needed, will become due by February 28.

## **PROTECTION OF SCHOOL DISTRICTS FROM LOSSES**

As a result of the compression of tax rates and increased homestead tax exemptions, some school districts will face a deficit in their operational budgets. The legislature has guaranteed school districts that the State will fund any shortfall attributable to lowered property tax revenue.

## **AN EXPERIMENT IN CONTROLLING THE RATE OF INCREASE OF BUSINESS REAL PROPERTY TAXES**

For decades, the legislature has been asked to deal with the contentious matter of restricting the growth rate of business property taxes. Restrictions on the growth rate of residential homesteads have been in place since 1998. The taxable value of homesteads may not be increased by more than 10% from their prior year value—regardless of economic or market influences. These restrictions, or “caps,” have not been demonstrably harmful to tax collections as residential values consistently trend upwards—ergo, there rarely exists a massive valuation drop that would reset a cap to an artificially low value. This is not true of the volatile commercial real estate and minerals markets. A sudden market change can create an artificially low base for a cap resulting in significant losses of property tax revenue. During the recent special session, Texas leaders rushed through a compromise to pass a relief plan. The compromise resulted in a three-year trial period for a pilot program (called *Circuit Breaker*) which expires at the end of 2026.

The enacted statute is somewhat confusing and problematic. Simply put, the program commences in tax year 2024 and is akin to the 10% residential homestead exemption cap—but with a cap of 20%. It applies to all real property including minerals—but not to personal property or any properties granted restricted valuations, such as agricultural land, open space land, timber land, recreational, park, and scenic land, and restricted airport use land. To qualify, properties must be valued at \$5 million or less—and the taxpayer must have owned said property on or before January 1<sup>st</sup>, 2023. Properties acquired after January 1<sup>st</sup>, 2023, qualify in the first year in which they are owned on January 1 (*e.g.*, if a property was acquired on June 1<sup>st</sup>, 2023, its appraised value for the 2024 tax year serves as the base year and the 2025 tax year is the first year to which the 20% valuation increase limitation is applied.) The \$5 million threshold will be adjusted annually based on the Consumer Price Index.

Unsure if a property qualifies? If a property was valued at \$5 million or less and a property owner acquired it on or before January 1<sup>st</sup>, 2023, it qualifies for the limitation for tax year 2024. The initial base valuation to determine qualification is the 2023 final appraised value of the property. If a property was valued at \$5 million or less, the 2024 taxable value can be no greater than the 2023 taxable value plus 20% of the 2023 value plus the value of any new improvements made to the property during 2023.

<b><u>EXAMPLE 1</u></b>	<b><u>EXAMPLE 2</u></b>
<p>A taxpayer acquired a property before January 1st, 2023, has made no improvements to it, and the appraisal district valued it at \$5 million (\$5,000,000) for tax year 2023.</p> <p>The maximum increase in value is:</p> <p style="padding-left: 40px;"><math>\\$5 \text{ million} \times 20\% = \\$1 \text{ million}</math></p> <p>Accordingly, the 2024 taxable value cannot exceed \$6 million even if the actual market value is much higher.</p>	<p>A taxpayer acquired a property before January 1st, 2023, has made no improvements to it, and the appraisal district valued it at \$5 million and \$1 (\$5,000,001) for tax year 2023.</p> <p>The value exceeds the threshold:</p> <p style="padding-left: 40px;"><math>\\$5 \text{ million} &lt; \\$5 \text{ million and } 1</math></p> <p>Accordingly, the 2024 taxable value can increase to its full market value, exceeding the 20% limitation.</p>

There is an open question as to what qualifies under the statute. The bill interchangeably uses the terms “property,” “real property” and “parcel of real property.” Does the limitation apply to each appraisal district account number? Or, to common economic units (such as apartment complexes or shopping centers)? Or, to an owner? This is not an issue for residential caps as the 10% limitation applies to the entirety of a homestead regardless of value.

**NEW AND IMPROVED APPRAISAL DISTRICT BOARDS OF DIRECTORS AND APPRAISAL REVIEW BOARDS**

Since their inception, appraisal districts have been run by boards of directors appointed by the taxing units for whom the appraisal districts value property.

Subject to voter approval of the constitutional amendment, in counties with a population of 75,000 or more, three members of the appraisal district board of directors will be elected. The tax assessor will serve as an ex officio voting member of the board, and five members of the board will be appointed by the constituent taxing units. Directors serve four-year staggered terms.

The power to select and appoint members to an appraisal district's appraisal review board is switched from the presiding district court judge to the appraisal district board of directors. Members of appraisal review boards serve two-year staggered terms. To qualify, appraisal review board members must be approved by a majority vote of the board of directors *with at least two of the elected members of the board voting with the majority.*

#### **CLOSING THOUGHTS**

The legislature had \$18 billion in surplus monies available to deliver the current monetary school district property tax relief. No apparent source of similar future surpluses exists after the current state budget expires in 2025. If no new monies come in, what happens to the “compressed” tax rates and who will pick up the tab for the increased homestead exemptions? Will property taxes skyrocket as a result?

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