

Reducing School M&O Taxes After 2008

There's a Way; Texas Only Needs the Will

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What if it were possible to nearly eliminate school property taxes in Texas? After the special session last spring the reaction to such a question is likely either a moan of dread or sigh of disbelief that such a fairy tale could ever come true.

It turns out, however, that there is a possible formula for eliminating school maintenance and operations property taxes in fewer than 15 years. The formula? Fiscal discipline.

During the 1990s, inflation ran about 2.5 percent per year. Texas' population grew at about 2 percent per year. We could expect our state and local governments to grow, on average, about 4.5 percent per year in order to keep up with rising costs due to inflation and with increased demands on government from population growth.

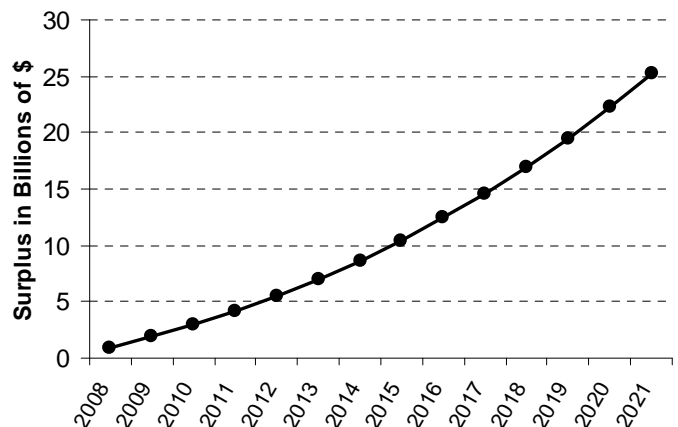
State spending financed only with Texas revenue sources—i.e. excluding federal funding—grew by about 6.5 percent per year, and except for the anomalous 2003 session it continues to grow faster than inflation and population growth. Public education spending, which is substantially funded through local property tax revenues, grew even faster.

But what if we held state-financed spending growth to the sum of population growth and inflation? Then did the same with school maintenance and operations (M&O) spending? We could use the excess growth in state revenues to buy down school M&O taxes.

In the graph at right, the potential for state surpluses with a solid spending limit is illustrated. With state revenues grow-

ing at 6.5 percent per year—a rate of growth that has not required any tax increases—and spending growing at the sum of population growth and inflation—about 4.5 percent, the state's surplus in 2016 would be \$12.4 billion. In 2021 the surplus would be \$25.3 billion. Over the period illustrated, over \$152 billion in surplus monies could cumulatively be used to reduce school property taxes.

Projected Texas State Surplus with Spending Growth Limit



The two graphs on the following page illustrate one possible scenario. It is assumed that population growth and inflation continue at the 1990s rates.

Although inflation is currently picking up and population growth is slowing down, the same principle will be at work in the future as in the past. Inflation will push up tax

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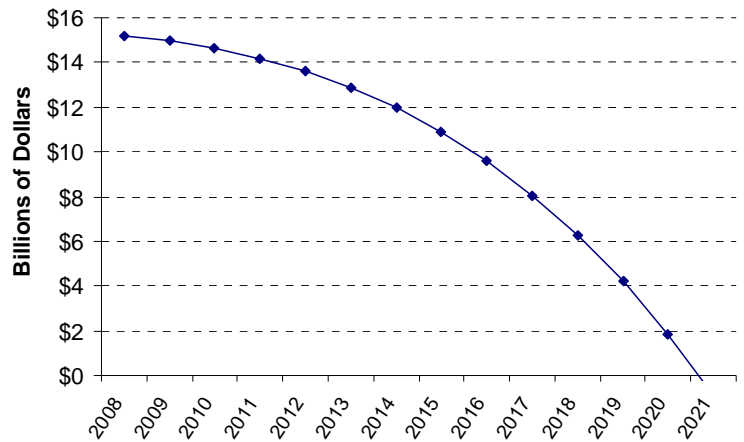
revenues in absolute terms the same way it pushes up prices, and an increasing population will push up revenues, too. Under the current tax system, this regularly produces surpluses—most of which have been spent on expanded government.

Back to the graphs, we can see the possibilities. If beginning in 2008 both state spending and school spending were not allowed to grow faster than population growth and inflation, and the resultant state surpluses were dedicated to buying down the school M&O property tax, the local revenues from this tax would fall from a little over \$15 billion in 2008 to less than \$10 billion in 2016. The school M&O tax rate would fall from a dollar to a little more than 50 cents. There would be no school M&O levy and no school M&O tax by 2021—a span of only 13 years from implementation to fruition.

In fact, the school M&O tax rate might fall even faster. As taxes on real property are reduced, property values will increase. With the limit on expenditures, the increased property values would not result in the sort of levy increases we have seen in recent years. The state would have that much more money to buy rates down further.

Sound policy might dictate that some local taxation is necessary. Economic circumstances can also interrupt the smooth buy-down of the school M&O tax. In this case, however, there is a way. All that needs to be found is the will. ★

Projected M&O Property Tax Levy with Buy-Down Using State Surplus and Spending Limits



M&O Property Tax Rates with State Buy-Down of Rates with State and School Spending Limits

