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Tax Lien Lending Benefits Property Owners and Consumers

Senate Bill 525

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In a recent Texas Public Policy Foundation publication, *Tax Lien Transfers: A Reasonable Means of Rectifying Property Tax Obligations*, Kathleen Hunker discusses the high cost of Texas property taxes:

> Texas has the 15th highest property taxes in the nation, capturing nearly 5 percent (approx. $2,500) of an average household's earnings each year—and that burden has only grown heavier. Over the last two decades, Texas residents have seen local property tax levies jump by 205 percent, almost three-times faster than the median household income (Hunker 2015, p. 2)

The rapid growth of property taxes is not surprisingly due to the rapid growth in local government debt and spending financed by property taxes. In fiscal year 2014, local government debt totaled more than $333 billion, or approximately $12,500 per Texan, according to the Texas Bond Review Board Since fiscal 2009, the total debt owed by Texas' cities, counties, school districts, and special districts grew by almost $35 billion (Quintero 2015). Spending per pupil by school districts has increased 140 percent, adjusted for inflation, since 1972 (Grusendorf 2015, p. 1). City and county spending is also increasing. And all efforts to slow the growth of local spending dependent on property taxes are met with strong resistance by local governments in the Texas Legislature.

Tax lien transfers, commonly referred to as property tax loans, provide a market-based, consumer-friendly way for Texas taxpayers overwhelmed by high property taxes to pay their taxes and avoid the costly fees and penalties associated with delinquent taxes and the collection process—not to mention foreclosure. Hunker explains how the process works:

> the transfer begins when a property owner elects to enter into a written contract, which authorizes a third party—commonly called a property tax lender—to pay the owner's delinquent taxes in exchange for a multi-year payment agreement secured by the government's priority tax lien on the property. Once the lien has been assigned, the property tax lender directly pays the local tax assessor all the property owner's outstanding taxes, fees, and penalties, removing the property owner from the delinquent tax roll. The owner then pays off the lien using a flexible payment schedule that was negotiated at the start of the transaction (Hunker, p.4).

Opposition to Tax Lien Lending

The primary opposition to tax lien transfers comes from delinquent tax collectors, banks, and other mortgage lending institutions. Banks and other mortgage lenders claim that current law gives an unfair advantage by providing a government lien to one business at the expense of impairing the rights of another business. Specifically, the bankers claim that property owners that use tax lien transfers have breached their mortgage contracts. However, these claims are demonstrably false.

First, mortgage lenders claim that tax lien transfers result in a breach of contract because mortgages require that property taxes and assessments be paid before delinquency. They base this claim on the fact that mortgages generally require that owners pay property taxes and assessments before delinquency. Of course, it is true that a property owners with this provision in their mortgage would be in breach of contract if they become delinquent on their taxes. But becoming

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delinquent on taxes is a completely separate transaction from entering into a tax lien transfer that in no way involves a breach of the provision in the mortgage contract. In fact, it is a provision in the Texas Tax Code that prevents property owners from getting a tax lien transfer *before* taxes become delinquent that forces many property owners into delinquency and breach of contract.

Sec. 32.06(a-2), Texas Tax Code, reads as follows:

> (a-2) Except as provided by Subsection (a-8), a tax lien may be transferred to the person who pays the taxes on behalf of the property owner under the authorization described by Subsection (a-1) for
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> (1) taxes that are delinquent at the time of payment; or
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> (2) taxes that are due but not delinquent at the time of payment if the property is not subject to a recorded mortgage lien.

Unlike property owners without a mortgage, property owners with a mortgage are prohibited from entering into a tax lien transfer before taxes become delinquent. If mortgage lenders are serious about helping property owners avoid both delinquent property taxes and breach of contract, they would support eliminating Sec. 32.06 (a-2)(2), of the Texas Tax Code. Doing so would allow many property owners to avoid the costs and embarrassment of being delinquent on this taxes.

Additionally, bankers claim that entering into tax lien transfer violates another provision in most mortgages that require the borrower to protect the lien position of the mortgage lender. Again, this is a false claim that misrepresents the bankers' lien position relative to a tax lien. According to Sec. 32.01, Texas Tax Code, Texas law automatically attaches a lien onto private property on January 1 each year in order to secure payment (Hunker, p. 4). The lien remains in place until the property taxes are paid. Therefore, as of January 1, mortgage holders already occupy a secondary lien position behind the local government entity that holds the tax lien. Thus tax lien transfers do not affect or alter the secured interests of other creditors. They simply transfer an existing lien from one entity to another, while allowing property owners to restructure their existing debt in a way that better reflects their financial situation (Hunker, p.4).

Conclusion

Claims by mortgage lenders that entering into a tax lien transfer is a breach of contract are untrue. Neither do tax lien transfers represent unfair competition to mortgage lenders, who are free to engage in the same marketing and lending practices of tax lien lenders. However, they choose not to incur those costs and expenses. SB 525 is a protectionist measure promoted by mortgage lenders that would use government to reduce competition, increase profits, and harm consumers.

Sources

Grusendorf, Kent, *Are Government Monopolies Inherently Inefficient?*, Texas Public Policy Foundation (2015).

Hunker, Kathleen, *Tax Lien Transfers: A Reasonable Means of Rectifying Property Tax Obligations*, Texas Public Policy Foundation (2014).

Quintero, James, *Reform Local Debt Issued Without Voter Approval*, Texas Public Policy Foundation (2015).