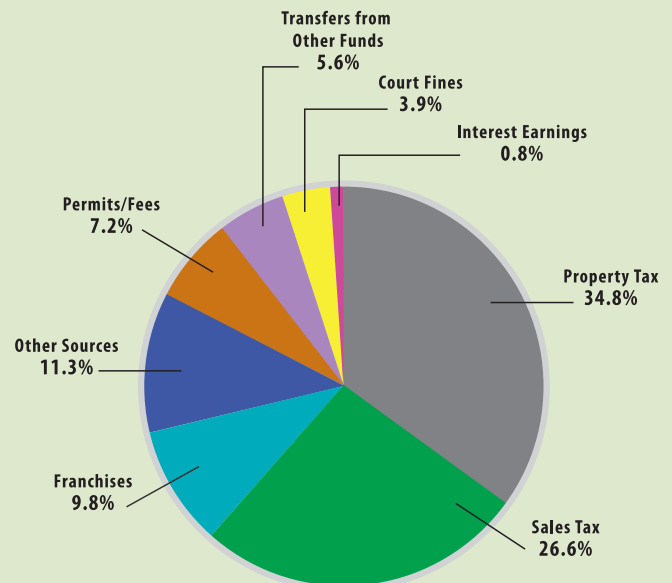


Where Do Texas Cities Get Their Money?

City government is where the rubber meets the road. Cities pave our streets, fight crime and fires, prepare us for disaster, bring water to our taps, take our trash away, build and maintain our parks—the list goes on and on. These services cost money. This article describes the sources of municipal revenue.

A TML survey shows that municipal general fund revenue in Texas is made up of the following sources:



Conspicuously absent from this list is financial assistance from the state. This is unusual—most states provide direct financial assistance to cities in recognition of the fact that cities provide basic services on which the entire state depends.

Instead of revenue, Texas cities receive something equally important from the state—broad authority to govern themselves, including the authority to raise their own revenue. This local authority has worked to the benefit of cities and the state for many decades and should continue into the future.



Here's more information on each source of municipal revenue:

Sales Taxes

Sales taxes are a leading source of city revenue. Nearly 93 percent of Texas cities levy a basic one-cent city sales tax. The revenue can be used for any purpose other than payment of debt. Many cities, though not all, also impose additional sales taxes in varying amounts of up to one cent. These additional sales taxes are known as dedicated taxes, because their proceeds may be spent only for certain purposes. Some popular dedicated sales taxes include mass transit, economic development, street maintenance, property tax relief, and sports venue taxes. All city sales taxes, including the basic one-cent sales tax, require a local-option election of the citizens. Collection of sales taxes is performed by the Texas comptroller, who "rebates" the city share on a monthly basis. The comptroller retains a small portion of the city tax revenue to cover the state's administrative costs.

Property Taxes

Property taxes are equal to sales taxes as a leading source of city revenue. Though crucial to city budgets, city property taxes make up just a fraction of a property owner's total property tax bill.

Most cities under 5,000 population have statutory authority to levy property taxes at a rate of up to \$1.50 per \$100 of assessed value. Most cities over 5,000 population have statutory authority to levy property taxes at a rate of up to \$2.50 per \$100 of assessed value. Despite this broad authority, the average city property tax rate was only \$.49 for tax year 2006.

City property tax levies are tied by law to fluctuating property tax values. As values increase, the city must adjust its rate or face potential rollback elections. In reality, such tax rollback elections are rare. City rates have held relatively steady for years, both in terms of actual rates and in terms of total levy as adjusted for inflation and rising income.

Franchises

When utilities and other industries use city property to distribute their services, cities are permitted by law to collect rental fees, also known as "franchise" fees, for the use of public property. Franchise fees are calculated by various methods, depending on industry type.

Permits and Fees

Cities may collect fees for issuing permits for building construction, environmental regulation, and for other services. Because cities incur costs to regulate in these areas, the permit fees must be tied to the cost of providing the service.

Court Fines

A city that operates a municipal court may impose fines for violations of traffic laws and city ordinances. Maximum fines typically range from \$200 for traffic violations, up to \$2,000 for city ordinance violations relating to health and safety. Much of a city's fine revenue offsets the costs of law enforcement and operation of the municipal court system.

Interest Earnings

When a city invests its funds, it must closely follow the mandates of the Public Funds Investment Act. Because of the twin concerns of safety and liquidity, investment income is a relatively small source of city revenue.

Transfers from Other Funds

Many cities operate utilities and other optional services that generate substantial gross revenues. By law, the fees for such services must closely offset the cost of providing the service. In addition to the cost factor, cities are permitted to retain a reasonable "return," which can then be transferred to the general fund. This return amounts to less than six percent of overall city revenue.

Other Sources

City revenue can take various other forms, including user fees for some services, amusement taxes, and hotel occupancy taxes.

The Bottom Line

The state could put municipal revenue at risk in at least two ways. First, the state could increasingly look to cities for revenue to fund state programs. When a state provides direct financial assistance to its cities, such trading of revenue might be workable. Texas is not such a state. Texas cities receive virtually no direct funding from the state, and cannot afford to fund the state's obligations. Second, the state could erode the statutory authority under which cities raise their own revenue. While cities are indeed subservient to the state, city officials hope that the respectful nature of the fiscal relationship between Texas cities and the state will continue for years to come. ★

Did You Know?

Many people mistakenly believe that cities derive substantial general revenue from their courts. In reality, the first \$82 of most traffic tickets goes directly to the state. What's left over, if any, can be used by the city. Unfortunately, city courts are increasingly being used as a backdoor revenue source for the state.