

SUBJECT: Authorizing sale of local governments' tax receivables

COMMITTEE: Local Government Ways and Means — favorable, without amendment

VOTE: 4 ayes — Hill, Elkins, Laubenberg, Uresti
1 nay — Puente
2 absent — Hamilton, Quintanilla

SENATE VOTE: On final passage, May 3 — 26-4 (Ogden, Shapleigh, Wentworth, Williams)

WITNESSES: *(On House companion bill, HB 879 by Madden:)*
For — Cathy Douglas, Texas Association of School Boards; Mark Goldberg, City of Houston; Charles Smith, XSPand Inc.; Steve West, Allen ISD

Against — Ro'Vin Garrett, Texas Assessor-Collectors Association of Texas; Gerald "Buddy" West

On — Donald Lee, Texas Conference of Urban Counties

BACKGROUND: A "tax receivable" is money owed for delinquent real property taxes and from delinquent assessments or other charges secured by real property liens, both of which are imposed by local governmental entities.

DIGEST: SB 447 would authorize local governmental entities (municipalities, counties, school districts, special-purpose districts and authorities, or other political subdivisions) to sell all or any part, including undivided interests, of its tax receivables under their own terms and conditions, including the price at which the tax receivable was offered. Sale proceeds of tax receivables could not be included in calculations of local governmental entities' effective tax rates or rollback rates. Information related to the sale of tax receivables or the issuance of tax receivable certificates would be deemed public.

Amounts to be sold could include the original amounts of delinquent property taxes plus any unpaid penalties and interest through the date of sale and the original amounts of delinquent assessments or other charges plus any unpaid interest through the date of sale. Interest and penalties would continue to accrue on the unpaid original tax amount after the sale of delinquent property tax receivables. Local governmental entities could recover court costs and other expenses in lawsuits to recover the delinquent taxes.

Sales could be negotiated or made through competitive bidding or negotiated sale and would not affect existing relationships with private tax collectors. The local government could not sell a tax receivable to a private individual under contract to collect the tax or enter into such a contract with the purchaser of a tax receivable.

A sale through competitive bidding would require publication of a notice once a week for two weeks in a local newspaper 30 days before the sale. The notice would include the terms and conditions of the sale, the criteria by which bids would be evaluated, and a description of any other information or documents a bidder would be required to provide. It also would be required to include a description of the tax receivables for sale or specify that a copy of the list could be obtained upon request. The local government entity could reject any or all bids or accept a combination of bids. Local governmental entities would have to maintain affidavits attesting to the publication and mailing of all requisite advertisements and notices.

A negotiated sale also would require publication of a notice once a week for two weeks in a local newspaper 30 days before the sale. It would include where a request for statements of interest could be obtained and a description of the tax receivables for sale or information that a copy of the list could be obtained upon request.

If a property owner paid in full prior to the date of the sale, the sale could not proceed. The local government entity could postpone or cancel a sale and would not be liable for any resulting damages.

A purchase and sale agreement would be required to include the purchase price and any contingency amounts, as well as a waiver of liability for the local government against damages from failure to collect delinquent taxes. Failure to collect would not create a cause of action. The agreement also

could require the local government to repurchase or substitute equivalent value tax receivables under certain conditions of the agreement, sell to the original purchasers subsequent tax receivables associated with the property, and require that the local government enforce collections as if the tax receivable had not been sold.

The agreement could not require local governments to prohibit paying delinquent taxes in installments. Nor could it interfere with contracts for performance of services in lieu of taxes or with individuals' rights to defer or abate a delinquent tax lawsuit. The agreement could not demand different collection standards than are customary.

Upon sale of a tax receivable, the local governmental entity would be required to issue a certificate of sale to the purchaser. The certificate only would transfer and assign the tax receivable for the amount sold and interest that would continue to accrue after the sale.

Certificates would not transfer collections of other taxes, nor would they provide holders any recourse against the local government for non-collection. Certificates would be transferable to other persons. The certificate would be required to state the sale date; the aggregate amounts of tax receivables transferred; the amounts of unpaid taxes, penalties, and interest in each tax receivable and the applicable interest rates; and property descriptions. Tax collectors could issue replacement certificates if proof were presented that the originals had been lost and require applicants for replacements to post bonds. Tax receivables and certificates would be included in the definition of "intangible personal property" (Tax Code sec. 1.04(6)).

The holder of a tax receivable certificate would be entitled to receive proceeds from the sale or resale of property sold in a lien foreclosure lawsuit, regardless of whether the foreclosure suit was brought by the local government that sold the tax receivable. A local government would be required to pay promptly to tax receivable holders any money received in connection with tax receivables, including attorney's fees and other expenses.

Tax receivables sold by a school district would be required to meet a minimum price of 95 percent of the outstanding principal for receivables delinquent less than one year, 90 percent for receivables delinquent one to two years, and 75 percent for receivables delinquent more than two years.

The bill would take immediate effect if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it would take effect September 1, 2005.

SUPPORTERS
SAY:

SB 447 could make the budgeting of local governmental entities, especially school districts, more certain by allowing them to sell their tax receivables. School districts' budgets, in particular, are affected by tax receivables because they can alter the amount of state funding to which they are entitled through the school finance formulas. Allowing local governments to sell their delinquent tax rolls would help them be more fiscally stable as they would realize the value of the sale immediately, rather than projecting the collection of delinquent taxes that might never be paid. Approximately 30 states already allow this type of financing to help make local government budgeting more certain.

SB 447 would make tax receivables an attractive investment, while retaining the existing private contracting of delinquent tax accounts. The statutory penalties imposed on a delinquent tax bill would continue to accrue after the sale. After the first year of delinquency, the state imposes 18 percent annual interest, which would convey to the purchaser of the tax account. A potentially high return on investment would attract serious investors who could pay local government entities top dollar, if not full face value, for their uncollected taxes.

The sale of tax receivables reduces risk for schools and other local government entities. When receivables are sold, the local government realizes the income, and the receivables move off the local government's books. This reduces risk for the local government because it no longer matters to the local government if the tax is ever paid. All risk is borne by the purchasers.

If any school district currently is selling tax receivables, it is doing so without state regulation. Creating a statutory framework would encourage appropriate use of this financial tool. Tax receivable sales also would not affect local governments' ability to grant property owners penalty and interest waivers for mitigating circumstances, nor would they interfere with deferred or abated payments.

There is no need to notify property owners of the potential sale of a tax receivable. The property owner still owes the tax regardless of who will receive the payment.

OPPONENTS
SAY:

The authority to sell tax receivables could encourage local government entities to undersell their tax rolls for ready cash in a pinch. Across the state, local governments have experienced budget problems, and this new tool could seem like a windfall. Instead of conducting a thorough financial analysis of the potential lost tax revenues in relation to the cash generated by a sale, local governments could be tempted to rush forth with a sale of all outstanding tax receivables. Texas has no experience with this hybrid form of tax collection and should take its time embracing it.

Under this proposal, local governments would be stuck with the administrative costs of maintaining delinquent accounts on their tax rolls. Delinquent tax property must remain on local rolls for up to 20 years. Local tax offices must continue monitoring compliance, or lack thereof, maintain records, mail notices, and supervise collection efforts and payments. Under current law, local governments are compensated for enforcing their tax liens by the penalties and interest that accrue, but would lose that compensation if they sold the rights to their tax receivables.

Delinquency rates rarely exceed 3 percent, and most of that amount is collected the next year. So local governments would have relatively small and difficult accounts to sell, many of which would be bankruptcies or businesses that had closed. School districts would benefit only if they could anticipate in advance that their collection rates were going to decline.

OTHER
OPPONENTS
SAY:

Some school districts already are selling their tax receivables without problems, so this proposal is unnecessary. Local taxing entities are well versed in the basics of financial management tools and do not need extensive state regulation to tell them how to do something they may already do.

The bill should include notification requirements. Local government entities should have to notify property owners by mail at least 30 days prior to a proposed sale so that owners were aware of the amount of the taxes owed, and that the tax receivable on the property could be sold if the amount due remained unpaid.

NOTES:

The companion bill, HB 879 by Madden, was recommitted on a point of order on second reading in the House on May 12. A very similar provision appeared in HB 1 by Grusendorf during the fourth called session of the 78th Legislature in 2004.