



City of Galveston

FINANCE DEPARTMENT

PO Box 779 | Galveston, TX 77553-0779
mloftin@galvestontx.gov | 409-797-3562

July 22, 2021

To: City Manager Brian Maxwell
Honorable Mayor and City Council

From: Michael W. Loftin, Assistant City Manager – Finance

RE: Consider a proposed amendment to the Memorandum of Understanding between the Rosenberg Library and the City of Galveston to provide for payments by the Library to the City that address an inequitable distribution of property tax revenue caused by the combined effect of City Charter requirements and State property tax laws approved in 2019.

Prior Council Action

In 2018, the City and the Library approved the Memorandum of Understanding formalizing the process of administering the City Charter provision that provides for the Rosenberg Library to receive a specific portion of the City's annual property tax revenue. By the time this is before City Council on July 22, the Library Board will likely not have met and approved it. But it is being presented for Council approval because of initial favorable responses from Library representatives.

Background

1. The City is severely limited in its property tax administration by the State property tax that effectively limits the City to an annual increase in revenue of 3.5% over the prior year, not including new construction. If the City's total taxable value excluding new construction as certified by the Galveston County Chief Appraiser increases by more than 3.5%, the City has two choices: reduce its property tax rate to offset the taxable value increase and/or request the voters to approve a higher property tax rate before beginning tax collections for the Budget year already underway.
2. The City chooses to adhere to the 3.5% limit on its revenue increase which is handled through the setting of its tax rate. By State law, the City's rate is comprised of two parts:



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- A. A debt service rate that is levied to retire principal and interest on previously sold general obligation bonds;
 - B. A maintenance and operations rate intended to cover all operating needs normally funded as a part of a jurisdiction's General Fund.
3. The City's debt service repayment schedule is generally flat so the debt service rate is held constant over time to meet bond covenant requirements. Therefore, the maintenance and operations portion of the rate must be reduced in order to comply with the 3.5% revenue increase limit. And the M&O rate is also the portion of the rate that must include the Library's property tax portion.
 4. This year, the Galveston County Appraisal District has raised the City taxpayers' values by an initial rate of 35% overall. The after-protest taxable value is certain to increase by well over 3.5%. The current estimate is around 15%, but it could easily be 20% when values are certified to the City. Because of the City Charter language, none of the rate reduction can be taken out of the Library's share of the M&O rate.
 5. The City Charter includes the following language under Article VIII Taxation, Section 2 Powers of Taxation:

“(2) Effective January 1, 1979, for the conduct, maintenance, improvement and extension of Rosenberg Library, a tax rate which will yield that amount which would be derived by the levy of a Five Cent (\$0.05) tax, or at the discretion of the City Council, an additional amount up to a maximum total of an Eight Cent (\$0.08) tax, per \$100.00 of assessed valuation based upon a one hundred (100) per cent assessment ratio.”
 6. For the last number of years, the City has based its payment under the charter language above on the minimum property tax rate of \$0.05. This will mean in the upcoming FY2022 Budget, that the Library will receive an increase in its share of City property tax revenue that is equal to the taxable value increase received from the CAD. Whatever the taxable value is, 15 or 20% more, the Library is mandated to receive its five-cent rate's worth of the revenue produced.



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General Fund Rate Drops with Increases in Taxable Value

Fund	FY 2020 Actual	FY 2021 Actual	FY 2022 3.5% Increase in TV	FY 2022 10% Increase in TV	FY 2022 15% Increase in TV	FY 2022 20% Increase in TV
General Fund	\$0.47739	\$0.45750	\$0.45750	\$0.42750	\$0.40750	\$0.38950
Debt	\$0.05250	\$0.05250	\$0.05250	\$0.05250	\$0.05250	\$0.05250
Library	\$0.05000	\$0.05000	\$0.05000	\$0.05000	\$0.05000	\$0.05000
Total *	\$0.57989	\$0.56000	\$0.56000	\$0.53000	\$0.51000	\$0.49200

General Fund Revenue (\$Thousands) Drops with Increases in Total Revenue

Fund	FY 2020 Actual	FY 2021 Projected	FY 2022 3.5% Increase in TV	FY 2022 10% Increase in TV	FY 2022 15% Increase in TV	FY 2022 20% Increase in TV
General Fund	\$29,102	\$31,473	\$32,554	\$32,131	\$31,825	\$31,550
Debt	\$3,205	\$3,587	\$3,722	\$3,933	\$4,088	\$4,242
Library	\$3,046	\$3,418	\$3,547	\$3,748	\$3,898	\$4,042
Total *	\$35,353	\$38,477	\$39,823	\$39,812	\$39,809	\$39,834

Note: Totals do not match because of complexity of tax calculation (freeze, P&I, et al).

Increase/(Decrease) from Prior Year (\$Thousands)

Fund	FY 2020 Actual	FY 2021 Projected	FY 2022 3.5% Increase in TV	FY 2022 10% Increase in TV	FY 2022 15% Increase in TV	FY 2022 20% Increase in TV
General Fund	\$2,618	\$2,371	\$1,082	\$659	\$353	\$78
Debt	\$166	\$382	\$135	\$346	\$501	\$655
Library	\$159	\$372	\$129	\$330	\$480	\$624
Total *	\$2,944	\$3,124	\$1,346	\$1,335	\$1,332	\$1,357



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General Fund Percent Share Drops with Growth in Tax Roll

Fund	FY 2020 Actual	FY 2021 Projected	FY 2022 3.5% Increase in TV	FY 2022 10% Increase in TV	FY 2022 15% Increase in TV	FY 2022 20% Increase in TV
General Fund	9.9%	8.1%	3.4%	2.1%	1.1%	0.2%
Debt	5.5%	11.9%	3.8%	9.7%	14.0%	18.3%
Library	5.5%	12.2%	3.8%	9.7%	14.0%	18.3%
Total	9.1%	8.8%	3.5%	3.5%	3.5%	3.5%

7. Note the following:
 - A. In FY 2020, the General Fund share increased by a larger percentage than the Library (9.9% versus 5.5%). This occurred because the City increased the M&O tax rate and this raised the General Fund portion of that rate only.
 - B. In FY 2021, the 3.5% limit on growth in revenue from properties on the tax roll in the prior year took effect. As a result, the M&O portion of the tax rate was reduced \$0.01988 and this reduced the General Fund's rate only.
 - C. In FY 2022, as the potential taxable value increase gets larger, the General Fund revenue share of total revenue gets smaller. If the taxable roll goes up by 20%, which is highly possible, the General Fund share of the total will go up \$78,000 or only 0.2%. This would lead to significant cuts in the General Fund budget in order to maintain public safety budgets intact.
 - D. Differences in the percent increase for Debt and the Library from year to year are rounding differences.

Issues

1. Clearly, changing the City Charter language to something more equitable is needed; however, this will require some time and will be too late for this year's Budget problem caused by the unusually high taxable value increases. And the Charter provision will have to be complied with until it is changed.
2. A simple interim solution is to implement an agreement between the City and the Rosenberg Library whereby each shares equally in the overall percentage increase in property tax revenue.
 - A. The inside cover page of the Proposed Budget is required to have the following language by the State of Texas Budget Law, Section 102.007 of the Local Government



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Code. The statement shown was in the FY 2021 Adopted Budget document because the final certified roll was not available until after the Proposed Budget was released.

“This budget will raise more revenue from property taxes than last year’s budget by an amount of \$3,156,000, which is a 8.95 percent increase from last year’s budget. The property tax revenue to be raised from new property added to the tax roll this year.”

This calculation was based on the following numbers found in the chart on page 37 of the Adopted Budget.

PROPERTY TAX REVENUE GROWTH FY 2021 ADOPTED BUDGET ESTIMATE

By Fund	FY 2020 Estimate	FY 2021 Adopted	Amount of Increase	Percent Increase
General Fund Operations	\$29,031,300	\$31,381,600	\$2,350,300	8.10%
Debt Service Fund	\$3,196,200	\$3,608,900	\$412,700	12.91%
Rosenberg Library	\$3,045,900	\$3,438,900	\$393,000	12.90%
Total	\$35,273,400	\$38,429,400	\$3,156,000	8.95%

- B. If the City and the Library shared equally in the overall increase in taxable value, the resulting payment by the Library to the City would have been \$120,392, netting the Library a revenue gain of \$272,608 over FY 2020.

PROPERTY TAX REVENUE GROWTH CALCULATION OF LIBRARY PAYMENT FOR FY 2021

By Fund	FY 2020 Estimate	FY 2021 Adopted	FY 2021 Equitable Shares	Percent Increase	Amount of Increase
General Fund Operations	\$29,031,300	\$31,381,600	\$31,629,601	8.95%	\$2,598,301
Debt Service Fund	\$3,196,200	\$3,608,900	\$3,482,260	8.95%	\$286,060
Rosenberg Library	\$3,045,900	\$3,438,900	\$3,318,508	8.95%	\$272,608
Total	\$35,273,400	\$38,429,400	\$38,430,369	8.95%	\$3,156,969

- C. In FY 2022, if the roll increases by 16.5%, including new construction at 1.5%, the two-step process would look like this:
- (1) Calculate the Proposed Budget based on the City Charter mandated \$0.05 cent tax levy for the Library. The Budget disclosure language required by State law would indicate that the overall increase in the property tax revenue would be \$1,333,000 or 3.46% growth. The Budget would reflect the allocations shown below, and the City



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would make its property tax payments to the Library as it always has under the Charter.

PROPERTY TAX REVENUE GROWTH PROSPECTIVE FY 2022 BUDGET ESTIMATE

By Fund	FY 2021 Estimate	FY 2022 Proposed	Amount of Increase	Percent Increase Over FY 2021
General Fund Operations	\$31,473,000	\$31,825,000	\$352,000	1.12%
Debt Service Fund	\$3,587,000	\$4,088,000	\$501,000	13.97%
Rosenberg Library	\$3,418,000	\$3,898,000	\$480,000	14.04%
Total	\$38,478,000	\$39,811,000	\$1,333,000	3.46%

(2) Calculate the equitable share of the overall property tax revenue increase of 3.46% not including new construction. The result is a net increase for the Library of \$118,263 over FY 2021 (see below) instead of the \$480,000 increase in the Charter mandated budget calculation (see above). The PILOT payment to the City would be \$361,737 (\$480,000 less \$118,263). Should new construction equal 1.5%, the overall increase in the property tax for the City and the Library would be five percent. In this case, the Library revenue amount would be \$3,589,000, constituting an increase over FY 2021 of \$171,000.

PROPERTY TAX REVENUE GROWTH CALCULATION OF LIBRARY PAYMENT FOR FY 2022

By Fund	FY 2021 Estimate	FY 2022 Proposed	FY 2022 Equitable Shares	Percent Increase	Amount of Increase over FY 2021
General Fund Operations	\$31,473,000	\$31,825,000	\$32,561,966	3.46%	\$1,088,966
Debt Service Fund	\$3,587,000	\$4,088,000	\$3,711,110	3.46%	\$124,110
Rosenberg Library	\$3,418,000	\$3,898,000	\$3,536,263	3.46%	\$118,263
Total	\$38,478,000	\$39,811,000	\$39,809,339	3.46%	\$1,331,339

(3) In the above example, the City's overall share of the increase in property tax revenue would grow 3.46% for the total of the Debt Service Fund and the General Fund. For policy reasons, the City may decide to leave its debt service rate where it is which would



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reduce the General Fund rate somewhat. The options in this regard will not be known until the property tax roll is delivered and the Proposed Budget is sent to City Council in August.

- (4) Also, the Library's total shown in the above box does not include new construction. This could raise the Library's full payment by as much as \$35,000 to \$75,000 depending on how much new construction is a part of the final certified tax roll.

Recommendation: Implementation in FY 2022

1. Approve an amendment to the existing Memorandum of Understanding between the Library and the City that recognizes the proposed payment as a form of revenue sharing or payment in lieu of taxes (PILOT). Secure approval of the Council and Library Board prior to the submission of the budget to Council.
2. The City would make payments to the Library as it always has using the five-cent tax levy amount budgeted (estimated in the table above at \$3,898,000 not including new construction).
3. In turn, the Library would make payments in the table above to the City totaling \$361,737 in equal monthly installments of \$30,145. Again, this is not including new construction.
4. At the end of the fiscal year, actual property tax amounts collected would be audited and "trued up" using the same distribution rules used to formulate the budget. The first step would entail using the percent actual property tax increase for the year just closed over the actual amount for the prior year.

Recommendation: Adopt the Memorandum of Understanding as proposed.