

September 2005

T E X A S

LEGISLATIVE

Update

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IN THIS UPDATE: FOCUS ON 2005 LEGISLATION

Our focus in this **Legislative Update** is a summary of the changes in Texas tax laws arising from legislation passed in the 2005 regular session of the 79th Texas Legislature. The summaries are organized alphabetically by tax.

- General Provisions (All Taxes)
- Boat and Boat Motor Sales and Use Tax
- Crude Oil, Natural Gas, and Minerals Taxes
- Franchise Tax
- Hotel Tax
- Insurance Tax
- Motor Vehicle Sales and Use Tax
- Sales and Use Tax
- Telecommunications Infrastructure Fund Assessment
- 911 Emergency Communications Services

GENERAL PROVISIONS (ALL TAXES)

Senate Bill 150 Effective September 1, 2005

Motor Sports Racing Trust Fund

The Motor Sports Racing Trust Fund is intended to attract and support motor sports racing events, such as races by the Automobile Competition Committee of the United States (the U.S. affiliate of the Federation Internationale de l'Automobile), the Champ Car organization, and the American Le Mans Series. The program is funded from the incremental increase in state and local revenue from sales, motor vehicle, hotel, mixed beverage, and alcohol excise taxes attributed to hosting the racing event, as estimated by the Comptroller.

Senate Bill 1038 Effective June 17, 2005

Other Events Trust Fund continued; U.S. Olympic Sporting Events added

The Other Events Trust Fund, established by the 2003 Legislature, was set to expire on January 1, 2007, but the legislation continues the program and expands its scope, making certain sporting events and training programs sanctioned by the U.S. Olympic Committee or the Committee's Community Olympic Development Program eligible for funding.

The purpose of the trust fund is to recruit and retain sporting events, including the Super Bowl; NCAA Final Four; NBA, MLB, and NHL All-Star games; NCAA BCS games; World Cup Soccer; and World Games. The trust fund receives the incremental increase in state and local revenue from sales, motor

vehicle, hotel, mixed beverage, and alcohol excise taxes attributed to hosting the games, as estimated by the Comptroller.

Senate Bill 1570 Effective September 1, 2005

Senate Bill 1863 Effective September 1, 2005

Interest Rate for Refunds

For tax refund claims filed on or after September 1, 2005, the interest rate paid will be the lesser of:

- the annual rate earned on deposits in the state treasury during December of the previous calendar year, as determined by the Comptroller; or
- the rate of prime plus 1 percent, as published in *The Wall Street Journal* on the first business day of the current calendar year.

Tax refund claims for taxes due prior to January 1, 2000 are not eligible for interest.

BOAT AND BOAT MOTOR SALES AND USE TAX

House Bill 2032 Effective September 1, 2005

Rewards for Information on Boat Sales Tax Violations

A person may apply for a reward for furnishing information that leads to the arrest and conviction of another person for violating Tax Code Chapter 160 (Boat and Boat Motor Sales and Use Tax). The program is administered by the Parks and Wildlife Department with the assistance of the Operation Game Thief Committee.

CRUDE OIL, NATURAL GAS, AND MINERALS TAXES

NATURAL GAS PRODUCTION TAX

House Bill 2161 Effective September 1, 2005

Credits for Qualifying Low-Producing Wells

Taxpayers will be eligible for a credit for gas from a low-producing well, defined as one that produces no more than 90 mcf per day for a three-month period. The amount of the production tax credit is based on the average price of gas per mcf for the three months prior to each reporting month, adjusted to 2005 dollars. For each reporting month, the credit will be 25 percent of the tax due on the

gas if the average price is more than \$3.00 but not more than \$3.50. The credit rises to 50 percent if the average price is more than \$2.50 but not more than \$3.00, and 100 percent if the average price is \$2.50 or less. There is no credit if the average price is more than \$3.50 per mcf. The credit is set to expire September 1, 2007.

Exemption for Gas from Reactivated Orphaned Wells

The bill creates an exemption for gas and casinghead gas from a well certified as an "orphan well" by the Texas Railroad Commission. An orphan well is defined in Section 89.047(a)(3) of the Natural Resources Code as one that has a commission permit, has not reported production for the preceding 12 months, and whose current operator's commission-approved organization report has lapsed. When a certified orphan well is put back into production by a certified orphan well operator, the well will be eligible for a 100 percent exemption from natural gas production tax and the oilfield cleanup fee for as long the certified operator operates the well. This portion of the bill takes effect January 1, 2006.

Change in Definition of Cash Sales

The bill amends Section 201.102 of the Tax Code to reinstate the definition of cash sales that was in place prior to September 1, 2003. Under this definition, "payments from a purchaser of gas to a producer for the purpose of reimbursing the producer for taxes due under this chapter are not part of the gross cash receipts."

CRUDE OIL PRODUCTION TAX

House Bill 2161 Effective September 1, 2005

Credits for Qualifying Low-Producing Wells

Producers will be eligible for a credit for crude oil from a low-producing oil well, defined as one that produces no more than 15 barrels of oil per day for a three-month period. The amount of the production tax credit is based on the average price of oil per barrel for the three months prior to each reporting month, adjusted to 2005 dollars. For each reporting month, the credit will be 25 percent if the average price is more than \$25 but not more than \$30. The credit rises to 50 percent if the average price is more than \$22 but not more than \$25, and 100 percent if the average price is \$22 or less. There is no credit if the average price is more than \$30 per barrel. The credit is set to expire September 1, 2007.

Exemption for Oil from Reactivated Orphaned Wells

The bill creates an exemption for crude oil from a well certified as an "orphan well" by the Texas Railroad Commission. An orphan well is defined in Section 89.047(a)(3) of the Natural Resources Code as one that has a commission permit, has not reported production for the preceding 12 months, and whose current operator's commission-approved organization report has lapsed. When a certified orphan well is put back into production by a certified orphan well operator, the well will be eligible for a 100 percent exemption from crude oil production tax and the oilfield cleanup fee for as long the certified operator operates the well. This portion of the bill takes effect January 1, 2006.

Tax Credit for Enhanced Efficiency Equipment

Producers are eligible for a tax credit for marginal oil wells when they purchase and install enhanced efficiency equipment that reduces energy use by 10 percent or more when compared to commonly available alternative equipment. "Enhanced efficiency equipment" does not include a motor or downhole pump. To qualify as having enhanced efficiency, the equipment must be evaluated by a Comptroller-approved Texas institute of higher education that has an accredited petroleum engineering program. The tax credit will be 10 percent of the cost of the equipment or \$1,000, whichever is less. To qualify for the credit, the well must be producing an average of 10 barrels or less of oil per day during a month, and the equipment must be installed between September 1, 2005 and September 1, 2009. The number of applications approved each state fiscal year cannot be more than 1 percent of the total of producing marginal wells as of September 1 of that year.

The University of Texas, Texas A & M, and Texas Tech have accredited programs.

Senate Bill 1863 Effective September 1, 2005

Petroleum Product Delivery Fee to Continue at Current Rate

The petroleum products delivery fee continues at the current rate. The fee will apply to petroleum products withdrawn from a bulk facility and delivered into a cargo tank or barge, or imported into Texas. The expiration date of the reimbursement program is changed from September 1, 2006 to September 1, 2008, and the fee cannot be collected on transactions made on or after September 1, 2007.

Senate Bill 1863 Effective August 29, 2005

Reduction in Coastal Protection Fee

The Coastal Protection Fee is reduced from two cents per barrel to one and one-third cents per barrel of crude oil or condensate transferred to or from vessels at a marine terminal located in Texas. The bill also lowers the maximum allowable amount of unencumbered balance in the Coastal Protection Fund from \$25 million to \$20 million and the minimum from \$14 million to \$10 million.

FRANCHISE TAX

House Bill 2201 Effective June 18, 2005

Clean Coal Projects

A corporation may deduct: (a) the amortized cost of qualifying equipment used in a clean coal project from its apportioned taxable capital, or, (b) 10 percent of the amortized cost of qualifying equipment used in a clean coal project from its apportioned taxable earned surplus.

HOTEL TAX

House Bill 352 Effective September 1, 2005

State Tax Reports Used to Estimate City Hotel Tax; Hotels Liable for Cost of City Audit

A municipal attorney will be able to use a hotel's state hotel tax return from the previous year to estimate local hotel tax. The estimate is prima facie evidence of the amount due. A hotel that is delinquent in taxes for at least two quarters will be liable to the municipality for the cost of an audit. The authority given to a city to conduct an audit is in addition to any other audit authority already provided by law.

INSURANCE TAX

House Bill 7 Effective September 1, 2005

Texas Workers' Compensation Commission Abolished

The Texas Workers' Compensation Commission (TWCC) will be abolished and replaced by the Division of Workers' Compensation within the Texas Department of Insurance (TDI) and the Office of Injured Employee Counsel. As was the case with TWCC, the Division of Workers' Compensation and Office of Injured Employee Counsel will be funded by maintenance taxes. TDI will set the tax rate and the Comptroller's office will collect the tax from insurers.

House Bill 532 Effective September 1, 2005

Title Insurers Can Invest in CAPCOs

Current law allows all licensed insurers except title companies to invest in certified capital companies (CAPCOs). House Bill 532 removes this exception, although title companies will not be able to invest in CAPCOs until the Legislature authorizes additional credits for the program. All CAPCO tax credits are deferred until 2009.

House Bill 2883 Effective September 1, 2005

Guaranty Association Changes

The Life, Accident, Health, and Hospital Service Insurance Guaranty Association will become the Texas Life, Accident, Health, and Hospital Service Insurance Guaranty Association. The maximum assessment per insurer will increase from 1 percent to 2 percent of an insurer's premiums on policies covered during the three years preceding the year in which an insurer becomes impaired or insolvent. Currently, assessments are allowed as a credit against premium taxes at the rate of 10 percent per year for 10 years. For an insurer who becomes insolvent on or

after September 1, 2005, the credit rate will be 20 percent per year for five years.

Senate Bill 1691 Effective September 1, 2005

Coverage of School Employees

Plans that provide coverage for active school employees will no longer be subject to any state tax, regulatory fees, or surcharges, including premium and maintenance taxes and fees.

Senate Bill 14 Effective September 1, 2005

Senate Bill 1863 Effective August 29, 2005

Excessive Automobile and Property Insurance Rates

The bill amends Article 5.144, Insurance Code, to allow the TDI commissioner to determine if an insurer has used an excessive or unfairly discriminatory rate to determine premiums for personal automobile or residential property insurance. The commissioner may order such an insurer to refund the excessive or discriminatory portion of the premium plus interest. Once the commissioner makes a determination that a refund is due, the insurer cannot claim any premium tax credit to which it is entitled unless the insurer has complied with Article 5.144.

MOTOR VEHICLE SALES AND USE TAX

House Bill 120 Effective September 1, 2005

Optional \$1 Vehicle Registration Fee for Organ Donor Programs

A person registering a vehicle can pay an optional \$1 fee to the local county tax assessor-collector to help organ donor programs. Proceeds from the fee will help fund the Donor Education, Awareness, and Registry Program of Texas and the Texas Organ, Tissue, and Eye Donor Council.

House Bill 2481 Effective September 1, 2005

Extension of Texas Emissions Reduction Plan Surcharges to 2010

The Texas Emissions Reduction Plan surcharge imposed on the purchase or use of certain diesel-powered motor vehicles, set to expire in 2008, has been extended to September 30, 2010. The surcharge is 1 percent on 1997 and newer models and 2.5 percent on older models. Also extended is the surcharge on off-road diesel-powered equipment subject to sales tax. Other changes were made to the program under the Health and Safety Code.

Senate Bill 338 Effective September 1, 2005

New Residents' Antique Vehicles

Effective September 1, 2005, use tax on an antique vehicle brought into the state by a new Texas resident will be the lesser of either \$90 or 6.25 percent of the vehicle's purchase price. In order to qualify, the vehicle cannot carry advertising and must be at least 25 years old; a collector's item; and used exclusively for exhibitions, club activities, or parades.

Senate Bill 867
Effective September 1, 2005

Exclusion of Certain RVs from the Texas Emissions Reduction Plan Surcharge

Beginning September 1, 2005, the purchase or first use in Texas of many recreational vehicles will not be subject to the Texas Emissions Reduction Plan motor vehicle tax surcharge. "Recreational vehicle" as defined by Section 522.004(b) of the Texas Transportation Code is one designed as temporary living quarters for recreational camping or travel. The exclusion does not apply to diesel-powered units over 14,000 pounds gross vehicle weight used for the production of income.

SALES AND USE TAX

House Bill 135
Effective September 1, 2005

Regulation of Health Spas

Health spa operators are required to include a copy of their certificate of registration when they apply for a Texas sales and use tax permit. Health spa operators are currently required to obtain a certificate of registration from the Texas Secretary of State and post a bond. More information is available from the Secretary of State's office at 512/463-6906 or online at <http://www.sos.state.tx.us/statdoc/healthspas/index.shtml>.

House Bill 1531
Effective September 1, 2005

Telematics Service Providers

Telematics service providers can be exempt from licensing as investigations companies and thus their basic charges will no longer be taxed as security services. Telematics service providers as defined in the bill (electronic stolen vehicle tracking services, for example) pay an annual fee of \$2,500 to the Texas Department of Public Safety and must meet certain business practice and procedure guidelines.

Telematics services also include telecommunications and information services that are subject to sales tax. Consequently, the taxability of monthly charges depends upon the specific services actually provided to the customer.

House Bill 3140
Effective June 18, 2005

Exemption of Certain Electronic Access Control Devices from Private Security Regulation

The term "alarm system" as defined in Section 1702.002, Occupations Code, does not include a telephone entry system, an operator for opening or closing a residential or commercial gate or door, or an accessory used only to activate a gate or door if not connected to an alarm system. If the services are exempted from private security regulation, then they are not taxable security services within the meaning of Tax Code sections 151.0075 and 151.0101(a)(14).

Senate Bill 568
Effective September 1, 2005

Personal Emergency Response Services

A new service under Chapter 1702.331 of the Occupations Code is created. As defined

in the bill, "personal emergency response systems" are systems installed in a residence and monitored by an alarm system company that will dispatch aid when a person signals a medical or personal emergency, but are not burglar or fire alarms. Companies selling, installing, servicing, monitoring, or responding to personal emergency response system services must be licensed by the Health and Human Services Commission. These services are not subject to sales and use tax as security services.

Personal emergency response system services can also include telecommunications services, however, that are subject to sales tax. Consequently, the taxability of monthly charges depends upon the specific services actually provided to the customer.

Senate Bill 877
Effective Date Varies by Provision

Transportation and Delivery of Wine in Texas

The provisions relating to winery permit requirements and shipping penalties are effective August 29, 2005, while the other provisions are effective May 9, 2005.

A winery permit holder or the holder of an out-of-state winery direct shipper's permit may ship wine to ultimate consumers, including those in dry areas. Shipments to each consumer cannot total more than 3 gallons in a 30-day period. The shipments must be in packages conspicuously labeled as containing wine and can only be delivered to: the person buying the wine; a recipient the purchaser designates in advance; or someone at the delivery address who is at least age 21, has valid proof of identity, and signs a delivery acknowledgement receipt. A permitted out-of-state winery direct shipper can only sell wine it produces or bottles and cannot sell more than 35,000 gallons of wine annually to ultimate consumers. Anyone who ships wine to consumers in Texas is subject to criminal penalties if they do not hold an out-of-state winery direct shipper's permit.

The fee for an out-of-state winery direct shipper's permit is \$75 per year. The permit can only be issued to an out-of-state winery that is in the U.S. and holds all state and federal permits necessary to operate the winery; holds a Texas sales tax permit; expressly submits to personal jurisdiction in Texas state and federal courts and to venue in Travis County, Texas for any proceeding concerning the Texas Alcoholic Beverage Commission (TABC); and does not directly or indirectly have a financial interest in a Texas wholesaler or retailer. The permitted out-of-state direct shipper must also maintain certain books and records that can be made available to TABC or any other appropriate state agency. TABC will establish rules requiring direct shippers to periodically file reports.

Sales by a permitted out-of-state direct shipper are deemed to have been made in Texas for delivery in Texas. Additionally, the permit holder is responsible for paying applicable state excise taxes and state sales and use taxes, all payable at the same rates and in the same manner as if the permittee were a Texas winery.

Senate Bill 1253
Effective September 1, 2005

Special Events Funds for Cities and Counties

A host community is authorized to use a portion of the sales tax revenue generated by a special event to assist in paying expenses related to the event. A "host community" is one or more cities or counties authorized by their governing bodies to host or assist a special event as defined in the bill.

To be eligible, a host community must conduct an economic impact study of the area expected to benefit. The community must send the study to the comptroller, who will review it within 30 days. If the comptroller determines the estimate is accurate, the study is certified. Otherwise, the comptroller will prepare a preliminary determination and give the community the opportunity to respond or submit a new or amended study.

At least six months before the special event begins, the host community must submit a special event plan containing certain specified information to the Texas Economic Development and Tourism Office (TEDTO). The plan must include a request for a sum of money to be made available in a special event trust fund. The amount of money requested cannot exceed the lesser of (1) one-half the amount of the total estimated expenses that each political subdivision within a host community will incur in hosting the event, or (2) one-half the amount of the anticipated increase in tax receipts to the state according to the economic impact study. TEDTO will forward the plan to the governor, lieutenant governor, and speaker of the house of representatives. For the plan to be approved, all three must give written approval not later than 90 days after TEDTO received it.

Once a special event plan is approved and the host community is selected as the site, the comptroller will deposit the amount requested into a special event trust fund. The community can use the money only for a public purpose specified in the bill. To receive payment, each political subdivision within the host community must request reimbursement from the comptroller. Within 180 days after the end of the special event, the comptroller will transfer any money remaining in the trust fund to the general revenue fund. Each political subdivision must provide any information the comptroller may need, including providing an audited financial statement to verify that all expenditures from the fund were authorized by law.

House Bill 132
Effective June 17, 2005

Increase in County Health Services Sales and Use Tax Rate

Counties with populations of 50,000 or less may adopt, increase, or decrease a health services sales and use tax at a rate between one-half and 1 percent in increments of one-eighth percent, so long as the total combined local rate of local sales taxes does not exceed the 2 percent cap at any location within the county.

House Bill 1458
Effective June 17, 2005

Airline Improvement District

A new Chapter 3847 is added to the Special Districts Local Laws Code, creating an airline improvement district as a political subdivision in Harris County. The district can impose a sales tax, upon approval by a majority of voters, so long as the total combined rate of local sales taxes does not exceed the 2 percent cap at any location within the district.

House Bill 2235
Effective June 18, 2005

Merger of Emergency Service Districts

Two or more emergency service districts can merge into one with the approval of the districts' boards of directors and an affirmative vote by the residents of the affected areas. The merged district assumes all powers, rights, duties, assets, and liabilities of the former districts without a change in status. The maximum tax rate imposed by a merged district cannot exceed the maximum rate authorized for any of the previous districts.

Senate Bill 1199
Effective May 20, 2005

Tax Increment Funds

A municipality or local government corporation formed under Chapter 431 of the Transportation Code can now deposit a portion of its sales and use tax proceeds into a tax increment fund. The taxes deposited into such a fund can only be used to:

- satisfy claims of holders of tax increment bonds, notes, or other obligations issued for the reinvestment zone;
- pay project costs for the zone; or
- make payments in accordance with an agreement under Section 311.010(b) dedicating revenue from the tax increment fund.

Senate Bill 1205
Effective June 17, 2005

Multi-Jurisdictional Library Districts

Multi-jurisdictional library districts, each of which is a special district and a political subdivision, may be created. A city or county can, by resolution, become the "lead governmental entity" and propose the creation of such a district for contiguous counties and cities that agree to have their territory in the district.

The governing body of the lead governmental entity will determine whether the district will be supported by a sales tax or a property tax or both, and can order an election to confirm the tax. If a majority of the voters favor the creation of the district and the tax, the lead governmental entity shall declare that the district is created. If the district imposes a sales and use tax, Tax Code Chapter 323 generally governs its imposition, administration, and governance, excepting, however, as otherwise provided for in the bill. The permissible sales and use tax rate is from one-eighth to one-half percent, in one-eighth percent increments.

Senate Bill 1339
Effective June 17, 2005

Advanced Transportation Districts

Communities that did not participate in the initial election authorizing an advanced transportation district (ATD) can now call for an election to participate in the district. An ATD can deny service to a community if it determines that doing so would create a financial hardship for the district.

Senate Bill 1518
Effective June 18, 2005

Rockwall County Public Safety and Fire Assistance District

Rockwall County Public Safety and Fire Assistance District is authorized to adopt a one-half percent sales tax in those areas of Rockwall County where doing so would not exceed the 2 percent cap on combined local taxes.

Senate Bill 1813
Effective June 17, 2005

Pearland Municipal Management District No. 1

Pearland Municipal Management District No. 1, a special district and political subdivision, is created. The district must hold an election to obtain voter approval before imposing a sales and use tax or an ad valorem tax, or before issuing bonds payable from ad valorem taxes.

Senate Bill 1866
Effective June 17, 2005

Dickinson Management District No. 1

Dickinson Management District No. 1, a special district and political subdivision, is created and has the authority to impose or abolish a sales tax with the consent of the governing body of the City of Dickinson, Galveston County.

**TELECOMMUNICATIONS
INFRASTRUCTURE FUND
ASSESSMENT**

Senate Bill 1863
Effective September 1, 2005

Telecommunications Infrastructure Fund Assessment Continues Through 2011

The Telecommunications Infrastructure Fund (TIF) assessment has been extended until 2011 at a rate of 1.25 percent. Revenue from the assessment will be deposited to general revenue. The TIF assessment is based on revenue from telecommunications services on which the seller is required to collect and remit Texas sales tax.

**911 EMERGENCY
COMMUNICATIONS SERVICES**

Senate Bill 621
Effective September 1, 2005

Emergency Communications Services for Fort Bend County

The Greater Harris County 911 Emergency Network is authorized to administer emergency communications services in the unincorporated areas and cities of Fort Bend County that are not partially located in Harris County. With the approval of the board of managers of the Greater Harris County network, Fort Bend County, by resolution, may withdraw from the Houston-Galveston Area Council, which is administered under the statewide 911 emergency communications program, and join the locally-administered Greater Harris County network. When this realignment takes effect, local exchange carriers with customers in the affected areas of Fort Bend County must begin collecting and remitting those customers' 911 Emergency Service Fees in the manner prescribed by the Greater Harris County 911 Emergency Network. After realignment, such fees should be remitted directly to the locally administered network rather than to the Comptroller.

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