

Mayor Bill White

To: F Michel  
FR: BW

From: Johnson, Judy Gray - F&A  
Sent: Tuesday, October 26, 2004 7:39 PM  
To: Mayor Bill White  
Cc: Michel, Arturo - LGL  
Subject: Prop 2 potential loophole

Feldstein might  
be interested.  
**RUSH**

In answering questions posed by Fitch Ratings service, who is reviewing the propositions, I realized that there may be a loophole in Prop 2 in regards to the tax levy for debt service.

Prop 2 defines combined revenues as the general fund, special revenue funds, and enterprise funds. There are other fund types, and one of these is the debt service fund. That fund is not included in the definition. (Neither are the capital project funds, fiduciary funds, & internal service funds—the prop 2 proponents probably chose to exclude these.)

The City of Houston deposits all tax revenues first into the general fund, then transfers the amount of the tax levied for debt service to the debt service fund. That way, any short-term risk of non-collection is born by the general fund rather than the debt service fund. When I researched this years ago I learned that this was not legally required, and that many cities do it the other way. They split the tax at the time of collection and deposit the tax levied for debt service directly into the debt service fund. (It doesn't make any difference over the long term—the truth in taxation law keeps cities from gimmicking this either way.) Unless something has changed in the past few years, there would be nothing to prevent the City from changing to the other method.

If the City of Houston were to change its method of depositing the tax as it is collected, the tax revenue for debt service wouldn't be a revenue of the general fund or the special or enterprise funds, and thus it would not be subject to the cap.

This potential loophole does not exist in Prop 1 which refers to the combined property tax rates.

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It does not do  
what Lemur thinks  
and says it would  
do.