



REVENUE MANUAL FOR TEXAS CITIES

This manual covers nearly every known source of revenue available to Texas cities. The material is presented in a simple question-and-answer format. Many of the questions and answers presented come directly from questions routinely received by the TML Legal Department.

The manual is organized alphabetically by type of revenue. Within each section, very basic questions are addressed first: what is this revenue source; how is it adopted; which types of cities can adopt it; how much can it generate; etc. Accordingly, the manual should be useful to city officials and staff first as a source of new revenue ideas, and then as a basic how-to guide for each source of revenue. Extensive footnotes citing the location of each revenue source within Texas law should make the manual useful to city attorneys, as well.

Because debt must ultimately be repaid by a city, it isn't a source of revenue in the conventional sense. Nevertheless, this manual covers the basics related to various sources of debt funding or financing.

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HOTEL OCCUPANCY TAXES

What are hotel occupancy taxes?

Cities may levy a tax on a person who—under a lease, concession, permit, right of access, license, contract, or agreement—pays for the use or possession or for the right to the use or possession of a room that is in a hotel, costs \$2 or more each day, and is ordinarily used for sleeping.¹⁵³

How much hotel occupancy taxes may a city levy?

Generally speaking, a city may levy a hotel occupancy tax in any amount up to, and including, seven percent of the price paid for the room.¹⁵⁴ Select cities are authorized to levy up to eight-and-a-half or nine percent of the price of the room, so long as a portion of the revenue generated by the increased rate goes toward certain specified projects.¹⁵⁵ The price of the room does not include food and drink.¹⁵⁶

What is the definition of a hotel for purposes of hotel occupancy taxes?

A hotel is defined as a building in which members of the public obtain sleeping accommodations in return for money. It includes motels, lodging houses, inns, rooming houses, and bed and breakfasts.¹⁵⁷ It does not include, and thus no tax is due for, dormitories, hospitals, and nursing homes.¹⁵⁸ In 2015, legislation passed clarifying that the definition of “hotel” includes a residential short-term rental property for purposes of the imposition of hotel occupancy taxes.¹⁵⁹

Is the hotel occupancy tax limited to hotels within the city limits?

Ordinarily yes, except that a city with a population under 35,000 may extend the application of its hotel occupancy tax by ordinance to the extraterritorial jurisdiction (ETJ) of the city.¹⁶⁰

¹⁵³ TEX. TAX CODE § 351.002(a).

¹⁵⁴ TEX. TAX CODE § 351.003.

¹⁵⁵ TEX. TAX CODE §§ 351.003, 351.1055, 351.1065, and 351.107.

¹⁵⁶ TEX. TAX CODE § 351.002(b).

¹⁵⁷ TEX. TAX CODE § 156.001.

¹⁵⁸ TEX. TAX CODE § 156.001.

¹⁵⁹ TEX. TAX CODE § 156.001(b).

¹⁶⁰ TEX. TAX CODE § 351.0025(a).

However, a city under 35,000 population may not apply its hotel occupancy tax in the ETJ if, as a result of the adoption of the city tax, the combined rate of state, county, and city hotel taxes would exceed fifteen percent at hotels in the ETJ.¹⁶¹ Provided the combined tax does not exceed fifteen percent at the time the city levies its tax, the city's tax is unaffected by future taxes levied by counties or other entities that might have the effect of imposing a combined rate in excess of fifteen percent.¹⁶²

A city may extend its hotel occupancy tax to the ETJ by a provision in its hotel occupancy tax ordinance specifying that the tax extends to the ETJ.

How does a city levy a hotel occupancy tax?

A hotel occupancy tax must be levied by ordinance.¹⁶³ No election or other approval of the citizens is required. Sample hotel occupancy tax ordinances can be obtained from the TML Legal Department at (512) 231-7400 or legalinfo@tml.org.

Can a city change the rate of an already-established hotel occupancy tax, and if so, how?

Yes, a city can change the rate to any amount up to, and including, seven percent (with the exception of the few cities that can adopt a higher rate). A city would amend the portion of its hotel occupancy tax ordinance relating to rate in order to change the rate. If a city increases the rate of its hotel occupancy tax, the increased rate does not apply to the tax imposed on the use or possession, or the right to the use or possession, of a room under a contract that was executed before the date the increased rate takes effect and that provides for the payment of the tax at the rate in effect when the contract was executed, unless the contract is subject to change or modification by reason of the tax rate increase.¹⁶⁴

How may hotel occupancy tax revenues be spent by a city?

Hotel occupancy tax revenues are known as "dedicated revenues," as distinguished from general tax revenues such as property and sales taxes. General revenues may be spent on nearly any lawful pursuit of a city. Dedicated revenues, however, may only be spent on certain, statutorily-defined purposes.

Very generally speaking, all expenditures of city hotel tax revenue must promote tourism within the city. This general rule can be further broken down into two parts (often referred to as the "two-part test"):

- (a) all expenditures must promote tourism and the convention and hotel industry; and

¹⁶¹ TEX. TAX CODE § 351.0025(b).

¹⁶² Op. Tex. Att'y Gen. No. GA-408 (2006).

¹⁶³ TEX. TAX CODE § 351.002(a).

¹⁶⁴ TEX. TAX CODE § 351.007(a).

(b) all expenditures must further fall into one of nine statutory categories:

- (1) the acquisition of sites for and the construction, improvement, enlarging, equipping, repairing, operation, and maintenance of convention center facilities and visitor information centers;
- (2) expenses associated with registration of convention delegates;
- (3) advertising, solicitations, and promotions that attract tourists and convention delegates to the city or its vicinity;
- (4) promotion of the arts;
- (5) historical preservation projects;
- (6) sporting events that promote tourism in counties of less than one million population;
- (7) enhancing or upgrading existing sports facilities or sports fields (only in certain cities);
- (8) transportation systems that transport tourists from hotels to the commercial center of the city, a convention center, other hotels, or tourist attractions, provided the system doesn't serve the general public; and
- (9) signage directing the public to sights and attractions that are visited frequently by hotel guests in the city.¹⁶⁵

Further, the Tax Code has some fairly specific provisions relating to how the expenditures within the nine statutory categories should be allocated, depending on the population of the city. Generally speaking, funding of the arts is limited to no more than fifteen percent of total tax revenues, and a certain portion must be spent on promoting the city and/or on convention facilities, again depending on the size of the city.¹⁶⁶

Can a city fund a fireworks show using hotel occupancy taxes?

The prototype hotel tax controversy involves an event like a fireworks show or a parade. City officials frequently ask if they can fund a fireworks show with hotel tax money.

All expenditures must be subjected to the “two-part test” spelled out in the previous question. In the first place, a fireworks show must be shown to promote tourism and the convention and hotel industry. Put another way, does the expenditure “put heads in beds”? The answer is likely not.

¹⁶⁵ TEX. TAX CODE § 351.101.

¹⁶⁶ TEX. TAX CODE § 351.103.

Even if a fireworks show attracted overnight tourists to the city, hotel tax expenditures on such an event don't fit neatly into one of the nine statutory categories. Some may argue that such shows "advertise" the city, but this is likely not what that category means. "Advertising the city" literally means some sort of print or other media that explicitly promotes the city. Thus, direct funding of fireworks displays and the like is usually not a proper hotel tax expenditure.

May a city delegate the expenditure of hotel taxes to another entity?

Yes. A city may delegate expenditures of hotel taxes to another entity such as a chamber of commerce or convention and visitors bureau. So long as the chamber or other entity spends the money on projects that otherwise meet the two-part test mentioned above, such entities are legal agents to spend the city's hotel tax funds. There must be a written contract laying out the duties of the entity, and the entity must keep the hotel tax funds in an account separate from the general operating fund.¹⁶⁷ A sample hotel tax delegation contract with a chamber of commerce is available on the TML website at www.tml.org (go to: Legal – Finance/Economic Development – Example Documents).

What is the relationship between city and state hotel occupancy taxes?

The state collects its own hotel occupancy tax at the rate of six percent.¹⁶⁸ The state plays no part in collecting or enforcing the city's hotel occupancy tax, however. A city is responsible for its own levy, collection, and enforcement.

What can a city do if a hotel is delinquent or refuses to pay hotel occupancy taxes?

Cities have all of the following remedies available against hotels that don't collect the tax or are delinquent in collecting the tax: civil lawsuit, injunction against operation of the hotel until taxes are paid, a fifteen-percent civil penalty against the hotel when suit is necessary (if the tax has been delinquent for one complete municipal fiscal quarter), reasonable attorney's fees, misdemeanor prosecution against the hotel (assuming the city's ordinance provides for an offense), and audit powers.¹⁶⁹ If an audit conducted by the city shows a concurrent delinquency in state hotel occupancy taxes, the city must notify the comptroller of the delinquency, and if the state proceeds with collection and enforcement efforts, the comptroller must distribute an amount to the city to defray the costs of the audit.¹⁷⁰

¹⁶⁷ TEX. TAX CODE § 351.101(c).

¹⁶⁸ TEX. TAX CODE § 156.052.

¹⁶⁹ TEX. TAX CODE § 351.004.

¹⁷⁰ TEX. TAX CODE § 351.008.

Are cities required to annually report hotel occupancy tax information?

Yes. Legislation passed in 2017 that requires cities to annually report hotel occupancy tax information to the comptroller.¹⁷¹ Not later than February 20 of each year, a city that imposes a hotel occupancy tax must submit to the comptroller: (1) the rate of the city's hotel occupancy tax and, if applicable, the rate of the city's hotel occupancy tax supporting a venue project; (2) the amount of revenue collected during the city's preceding fiscal year from the city's hotel occupancy tax and, if applicable, the city's hotel occupancy tax supporting a venue project; and (3) the amount and percentage of hotel occupancy tax revenue allocated by the city for certain categories of expenditure during the city's preceding fiscal year.¹⁷² Cities must comply with the annual reporting requirements by either submitting the report to the comptroller on a form prescribed by the comptroller, or alternatively providing the comptroller a direct link to, or a clear statement describing the location of, the information required to be reported that is posted on the city's website.¹⁷³

IMPACT FEES

What are impact fees?

The Texas impact fee statute defines an impact fee as “a charge or assessment imposed by a political subdivision against new development in order to generate revenue for funding or recouping the costs of capital improvements or facility expansions necessitated by and attributable to the new development. The term includes amortized charges, lump-sum charges, capital recovery fees, contributions in aid of construction, and any other fee that functions as described by this definition.”¹⁷⁴

Put more simply, impact fees are a way for a city to charge developers for some of the cost that new development places on the infrastructure and resources of a city.

The state of Texas allows cities to impose impact fees pursuant to Chapter 395 of the Local Government Code. Within the code, what qualifies as an “impact fee” is defined, and specific guidelines are set forth in regard to utilizing impact fees.

What may impact fees be spent on?

To determine if an expenditure of impact fees is proper, two separate tests must be satisfied: (1) the expenditure must be for a *proper impact fee facility*; and (2) even if it is a proper impact fee facility, the expenditure must be a *permissive cost* that may be funded relative to that facility.

¹⁷¹ Senate Bill 1221, 85th Legislature, Regular Session (2017).

¹⁷² TEX. TAX CODE § 351.009(a).

¹⁷³ TEX. TAX CODE § 351.009(b).

¹⁷⁴ TEX. LOC. GOV'T CODE § 395.001(4).