Circuit Breaker Limitation on Increases in Value of Real Property Other Than Residence Homestead

Beginning tax year 2024, a new property tax law passed in 2023 (S.B. 2, 88th Legislature, 2nd special session) created a 3-year "circuit breaker" pilot program introducing a 20 percent limitation on taxable value increases for non-homestead real property. In theory this is similar to the 10% appraisal cap that's been in place for homestead real estate property (people's homes, or residences) for many years now, but with a couple of key distinctions:

- **The "circuit breaker" value limitation only applies to non-homestead real property with an appraised market value of $5 million or less. The law isn't clear on whether this $5 million threshold value is meant to be the current year's value or the previous year's value, but most appraisal districts are interpreting the law to mean the current year's value. This threshold value will be indexed to inflation for tax years 2025 and 2026. [NOTE: When the law says "appraised value" it is referring to *taxable* or tax roll value, the value that you actually pay taxes on, and not the appraisal district's appraised *market value*.]**
- **This pilot program will expire ("sunset" in Legislative terminology) at the end of 2026, whereas any further "circuit breaker" value limitation scheme will have to be considered by the Legislature at that time.**

**The Legislature's detailed "bill analysis" of S.B. 2 can be found at:
https://capitol.texas.gov/tlodocs/882/analysis/html/SB00002H.htm.**

This bill was extensive, so you'll need to scroll down about halfway through the document to see the discussion on "circuit breaker limitation."

EXCEPTIONS TO VALUE LIMITATION: S.B. 2 establishes that the circuit breaker limitation doesn't apply to agricultural land, timber land or restricted-use timber land, recreational or park or scenic land, or public access airport property. Also, the market value of all new improvements to a property that otherwise qualifies for a value limitation is NOT subject to that value limitation – i.e., only the property that existed both last year and this year is subject to the value limitation. In addition, the value limitation doesn't apply to property being taxed under a new owner's name for the first time.

HOW THE LAW PERTAINS TO OIL AND GAS MINERAL INTERESTS: The definition of "Real property" can be found in the Texas Property Tax Code, §1.04(2): "...(A) land; (B) an improvement; (C) a mine or quarry; (D) a mineral in place; (E) standing timber; or (F) an estate or interest... in a property enumerated in Paragraphs (A) through (E) of this subdivision."

A mineral (oil and gas) interest qualifies as real property per §1.04(2)(F) above. It's not clear if the legislature understood the unique nature of an estate or interest being the subject property, or how

appraisal districts derive their opinions of market value for oil and gas mineral interests each tax year, because unfortunately this "circuit breaker" law failed to specify or address in any way what constitutes an "improvement" (to a mineral interest) that would not be subject to the value limitation. This has created much confusion within appraisal districts, and probably for taxpayers too, when new wells are drilled and production brought online within the last 12 months that's greatly "improved" the income for all the fractional interest owners under a lease. *The well is not the subject property, and neither is the income generated by a well's production.* The subject property is the *mineral interest*, the thing that's bought and sold in the marketplace of potential willing buyers and willing sellers. Unless the taxpayer's mineral interest *itself* has increased from the previous year (for example, the taxpayer's decimal net revenue interest ownership amount has become larger though acquisition, inheritance, etc.), additional income from one or more new wells cannot be considered an improvement to the taxpayer's property. This is merely an example of an existing property becoming more valuable, and sometimes very much so, in a short period of time, whereas the "circuit breaker" value limitation will come into play and possibly negate much of this increase in value from reaching the tax roll.

Another way that a mineral interest value can materially increase from the previous tax year is when the outlook for oil and gas price for the current tax year materially improves from the price forecast used for last year's appraisal. Again, just as with the example above for unexpected additional oil and gas production since the previous year's appraisal, a higher (and previously unforecasted) price environment does not legally constitute an improvement to the subject property (the mineral interest). The additional income generated by the higher price(s) only constitutes an improvement to the fortunes of those who own this mineral interest. Any additional market value due to an unexpectedly higher price environment is going to create vast opportunity for more taxable value limitation under this hastily conceived "circuit breaker" law. We doubt the legislature intended this result, particularly as this will shift the property tax burden back to other properties such as residential homestead.

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