Tax Reform for Arizona Citizens Committee

Final Report

December 2003

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Tax
Reform for
Arizona
Citizens
Committee

Final Report
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Tax Reform for Arizona Citizens Committee

Introduction:

The Tax Reform for Arizona Citizens Committee (TRACC) was established by Laws 2002, Chapter 289, Sec. 3. The Committee consists of legislators, local government officials, a school district representative and private citizens representing taxpayers and business. The Committee was established to examine the current tax structure, focus on short-term problems and provide recommendations that can be immediately implemented to improve the state's competitiveness. The Committee was given the following duties:

1) study and make recommendations on the fiscal policy and laws of this State, including specific consideration of expansion of State resources and economic development strategies;
2) study and make recommendations on the tax policies of this State and local jurisdictions, including counties, municipalities, school districts and special taxing districts, to assure that the policies are adequate, equitable, competitive and consistent with economic development strategies;
3) develop a comprehensive report and recommendations, including recommendations concerning the appropriate tax structure for this State and local jurisdictions and a strategy for transition to the appropriate tax structure.

TRACC has analyzed proposals that affect both individuals and corporations. The recommendations of this committee will focus on the deficiencies of state tax policy towards creating new jobs while still protecting individual taxpayers.

Property Tax Findings:

Arizona has a complicated property tax system. Not only does the state have two sets of values and two rates, but Arizona also has nine classes of property with several "subclasses". In addition, many properties have their own valuation method to determine full cash value. Non-profit properties may be exempt from property tax if allowed by the Legislature.

While Arizona does not have a state property tax rate, the Legislature does determine the level of primary property taxes paid by local school districts through the qualifying tax rate (QTR) formula. However, the county education equalization rate is a de-facto state property tax because the rate is set by the Legislature and the county is mandated to levy the tax. The state aid to education formula is directly impacted by property values throughout the state. Any valuation changes directly affect the state general fund. The state has a constitutional requirement to cap homeowner's primary property taxes at 1% of the value of the home. In addition, the Legislature subsidizes homeowner's primary school taxes by 35% (maximum $500).

It has been shown that this system discourages capital-intensive, high wage manufacturing in this state. Arizona business property taxes are some of the highest in the nation. To encourage businesses to move here, additional classes, or subclasses, have been added to provide incentives to relocate. This only exacerbates the underlying problem and then penalizes the good corporate citizens and small businesses that have been in Arizona without the benefit of economic development property tax incentives.

Secondary taxes are voter-approved taxes that were designed to bring some accountability to the property tax system by having voters approve any "extra" property taxes to pay for bonds or other long-term obligations not funded through the general property tax. However, due to the inequities in the assessment ratio system, homeowners are not aware of the full impact of the cost of the taxes; and as such over the last 20 years, the voters (homeowners) have routinely approved secondary taxes. Business taxes are two and one-half times higher than homeowner taxes. Secondary taxes have grown over 750% since 1980 – more than twice as much as primary taxes, which have grown 321% during the same time period.

Property Tax Reforms:

- **Reduce assessment ratios for class 1 (business and industrial) properties**

  This recommendation would reduce the assessment ratio for property tax purposes for class 1 properties from 25% to 20% over five years.

  Class one properties are currently assessed at the highest assessment ratio of 25%. These properties include commercial and industrial property (not included in other classes), mines and mining claim property, standing timber, local telecommunications service, gas water and electric utility company property, pipeline company property and producing oil and gas property.

  Several studies show that Arizona business property taxes are high relative to other states. A Minnesota study of a state comparison of property tax burden ranks Arizona

3rd in the nation for industrial properties, while the residential property tax burden in Arizona ranks 31st. In addition, a Utah State Tax Commission study of seven western states shows Arizona ranks 2nd in business tax burden as a percentage of gross state product.

Fiscal Impact: The changing assessment ratios would not result in lost revenue for local government. The drop in net assessed value could be offset by increases in property value. A percentage of the growth in new commercial and industrial property value could be used to buy down the assessment ratio without raising homeowners' property taxes. The change from 25% to 20% would be the lesser of either 1% or the revenues derived from growth in property values (from the new growth percentage which would be set aside to buy down the assessment ratio). The impact to the state general fund for the increased cost for basic state aid is estimated by JLBC to be approximately $28 million in the first year. When the assessment ratio phase-down is fully implemented, the estimated additional basic state aid cost is approximately $172 million.

❖ **Reduce the number of assessment ratios for future bonds and overrides to two: 20% for class one properties and 10% for all other properties**

Currently, property in Arizona is divided into different property classes for taxation purposes, with some classes of property having higher assessment ratios than others.

These ratios apply to both primary property and secondary taxes. The primary taxes are used to fund the general operations of counties, cities and school districts, and secondary property taxes are used to pay for voter-approved bonds. While several states have property classifications, Arizona has the second highest number of classes. Most other states typically use a single assessment ratio to calculate property taxes and no other state has two sets of values. The proposed recommendation would require collapsing the current assessment ratios down to two for future secondary property taxes.

This proposal would ensure that the assessment ratio for class 1 (commercial and industrial properties) would be no more than twice the amount of class 3 (owner-occupied residential properties).

Fiscal Impact: The impact to political subdivisions varies depending on the distribution of the different classes of property in each district. However, this would not affect any existing bonds or overrides that are currently issued or approved. In the future, each jurisdiction will have to take into account the variation of their district's property to determine future impacts.

❖ **Single Assessment Ratio**

This proposal is similar to the proposal to reduce the number of assessment ratios for future bonds and overrides to two. This proposal is the same except that all classes of property would have a single assessment ratio for any future voter-approved bonds and overrides.

Fiscal Impact: The impact to political subdivisions varies depending on the distribution of the different classes of property in each district. However, this would not affect any existing bonds or overrides that are currently issued or approved. In the future, each jurisdiction will have to take into account the variation of their district's property to determine future impacts.

- **Reduce Business Personal Property**

This proposal would reduce or eliminate the locally assessed business personal property tax.

All businesses (commercial, industrial, mining, utilities and agricultural) pay a property tax on the assessed value of their machinery and equipment. This proposal would be limited to locally assessed properties and would not apply to centrally valued properties (mines and utilities). The reason for excluding centrally valued properties is due to the fact that most of the property tax paid by these entities are on personal property and not real property. In 2003, 88% of centrally valued property is personal property. The locally assessed business personal property tax is self-reported and the county assessor then applies depreciation tables for various types of personal property.

The Arizona constitution requires that all property is subject to tax, unless specifically exempt. In 1996, the Legislature referred to the ballot, and the voters passed, a $50,000 exemption for each taxpayer's business personal property. This amount is adjusted for inflation each year and the exemption for 2003 is now $54,465. Additionally, the Legislature has lowered personal property taxes by allowing accelerated depreciation for the first five years and lowering the minimum value from 10% to 2.5%.

While Arizona is not unique in taxing business personal property, there has always been interest in exempting this from taxation because of the high burden this imposes, especially on capital intensive companies. A reduction in assessment ratios for business real property will also reduce the business personal property tax burden. A separate class of property could be created just for business personal property with a low assessment ratio. An elimination of this tax would require a change in the constitution.

Fiscal Impact: The fiscal impact of the proposal would depend on the actual recommendation. An elimination of locally assessed business personal property would have a negative impact on the state general fund through the school finance formula and the use of the QTR and the county education equalization rate. The impact would be approximately $78 million for the QTR and $9.4 million for the county rate. Current TNT law would allow rate adjustment to recoup most of the lost property tax revenue for local governments.

- **Control Future Growth of Property Tax Levies**

  This proposal would require the *voters* to approve any property tax rates that would raise more revenue than what would be allowed under the Truth-In-Taxation (TNT) rate for cities, counties and community college districts. The current TNT law requires public hearings if the proposed primary property tax levy, exclusive of amounts attributable to new construction, is greater than the amount levied by the jurisdiction in the preceding tax year. Publication requirements are set forth in the law and the governing body must take a roll call vote on the action.

  TNT is designed to make property owners aware of the fact that when valuation increases occur, and the rate remains the same, more money is collected through the tax rate. Increases in the value of property will increase revenue to governments if the tax rate remains the same as the previous year. There could even be revenue increases when the rate drops, if the rate is not adjusted accordingly.

  Fiscal Impact: Local jurisdictions that wish to levy a property tax in excess of the TNT rate would have increased costs associated with the election.

- **Address high primary property tax rates of school districts**

  This proposal will cap the primary property tax rate of any school district that has 50% or more of the homeowners at the 1% cap <u>and</u> the tax rate is 150% of the Qualifying Tax Rate set by the Legislature.

  This proposal would address some of the gross disparities that exist between school districts that are allowed to budget for items outside their revenue control limit. School districts that are permitted to budget for these items impose higher primary property taxes than other school districts. Since the funding comes from the primary tax, without voter approval, it is also subsidized by the state two ways. First, the state subsidizes primary property taxes for any homeowner whose taxes exceed 1% of the value of their home. The second subsidy is the Homeowner's Rebate program that pays for 35% of homeowner's primary school tax rate.

  This proposal will cap the primary school tax rate for those districts with extremely high tax rates.

Long-term – issues that need further study and reform:

Possessory interests and Government Lease Excise Tax
Levy Limits and Special Districts
Elimination of two values: Full Cash Value vs. Limited Value

Transaction Privilege Tax Findings:

Arizona has a transaction privilege tax instead of a true sales tax. The main difference is that the burden of the tax is actually on the business doing the transaction rather than on the purchaser. As a result, the law defines what is a taxable activity and then states the deductions or exemptions from the taxable transaction.

In comparison to other states, Arizona has a heavy reliance on sales tax revenue. This is due to a combination of state and local tax rates and the fact that Arizona has a fairly broad base.

Arizona is also one of the few states that allow municipalities to determine their own sales tax base. While there are many similarities between the state and the municipalities, there are significant differences. In addition, each city or town may tailor their code by choosing local or model options that differ from the Model City Tax Code base. The different sales tax base for the state and cities complicates the move toward national simplification of the sales tax.

The national movement toward simplification is called the Streamlined Sales Tax Project (SSTP). The SSTP would radically simplify sales tax collections by remote vendors, but local governments would lose their tax-collecting autonomy under the current plan.

Transaction Privilege Tax Reforms:

- **Require voter approval for rates higher than a maximum allowable rate for cities and towns.**

  This proposal would limit the maximum sales tax rate that municipalities could impose on most taxable activities. Currently, the highest rate levied by any city is 3.5%. To exceed the maximum rate, voter approval would be required.

  All of the incorporated cities and towns in Arizona levy a general sales tax. Most cities range from 1% - 2.5%. Fourteen municipalities levy over that amount and one city has a rate as high as 3.5% (Winkelman). Despite population and inflation growth of the transaction privilege tax, cities have grown their sales tax rates considerably more than the state over the past two decades. In 1980, the highest rate was 2%, with most municipalities well below that rate and several cities with no sales tax. Today, all incorporated cities and towns impose a general sales tax. Combined rates (state, county and city) are typically over 8% with some locations over 10%. A limit on municipal rates will deter future rate increases. The state is responsible for its own rate and the rates set by counties.

  This proposal would allow municipalities to exceed a maximum amount if the rate increase was submitted to the voters for approval. Currently, some charter cities require voter approval of any sales tax increase.

  Fiscal Impact: The cap could limit some municipalities from further increases, unless voters approve higher rates. This recommendation would not have an impact at the county or state level.

Long-term issues that need further study and reform:
Analysis of the impact to Arizona of adopting the SSTP
Regardless of SSTP, require uniformity of state and municipal tax base

Income Tax Findings:

Arizona imposes a corporate and personal income tax. Under the personal income tax, the state has a graduated rate structure ranging from 2.87% to a maximum rate of 5.04%. The corporate income tax rate is a flat 6.968%, with a minimum tax of $50. The corporate income tax is the most volatile tax stream. During the 1990's, the Legislature drastically increased the number of tax credits available for both individuals and corporations. In 2001, due to the concerns regarding the costs of these tax credits to the state, the Legislature established an Income Tax Review Committee. This Committee met for the first time last year and it is anticipated that scheduled reviews of these credits will result in improvements to the income tax code as credits are analyzed for their effectiveness in promoting their original purpose.

For multi-state or multi-national corporations, Arizona, like other states, uses an income allocation formula to determine Arizona taxable income. The allocation formula uses property, payroll and sales factors to determine how much income is attributable to Arizona. In 1991, Arizona adopted a double-weighted sales factor. Studies show that weighting the sales factor encourages investment in capital and/or labor intensive corporations. The recent trend in corporate income taxes shows that some states are moving to a single-factor sales formula to promote manufacturing activity.

Income Tax Reforms:

❖ **Allow multi-state and multi-national corporations the option of a 100% sales factor allocation**

This recommendation would allow multi-state and multi-national corporations the option to use a single factor sales apportionment formula instead of a three-factor formula. The recommendation would phase-in the new apportionment formula over five years.

Corporations doing business in more than one state must apportion income for state income tax purposes. Each apportionment formula may include three factors: payroll, property, and sales. Arizona law, like other states, requires an apportionment formula for corporations who have income from both in and outside of the state in order to determine the amount of income that is attributable to Arizona. Prior to 1991, Arizona employed an evenly weighted three-factor approach. In 1991, Arizona adopted a double weighted sales factor apportionment formula. The corporation completes the following calculations to determine Arizona tax liability:

1. Payroll paid in Arizona divided by payroll paid everywhere.
2. Value (original cost) of property situated in Arizona divided by value (original cost) of property everywhere.
3. Sales that occur in Arizona times two, divided by sales everywhere.

4. The three percentages are added together and are divided by four to produce a ratio to apportion total taxable income to Arizona.

Currently, eight states (Massachusetts, Connecticut, Illinois, Iowa, Missouri, Nebraska, Texas, and Maryland) have adopted the 100% sales factor apportionment formula and six states (Minnesota, Oregon, Michigan, Ohio, Pennsylvania, and Wisconsin) have adopted sales apportionment formulas with sales factors varying from 60-90%. Oregon and Wisconsin are phasing-in the 100% sales factor and both states will be at 100% by 2008. The sales factor only approach favors companies with most of their employment and manufacturing within the state and but have out of state sales.

Fiscal Impact: During the 2003 regular session, DOR estimated the first year impact to be $5 million. However, since corporate returns are generally paid over a three-year period, the full impact of increasing the sales factor option in the first year from 50% to 60% is estimated at $25 million. The proposal would increase the sales factor option to 100% in the fifth year. When fully implemented, the cost is estimated at $100 million. This estimate is a static estimate and does not take into account any dynamic modeling.

❖ **IRS Conformity**

This recommendation would encourage the state to conform to all income tax changes that flow through to Arizona from the federal government.

Each year, the Legislature adopts an updated statutory definition of the Internal Revenue Code to include any federal provisions that became effective in the previous year. This is because Arizona, like many states, stipulates that individual taxpayers use federal adjusted gross income as a starting point for state income tax and corporations use federal corporate taxable income. For this reason, any change to federal tax legislation that affects either corporate taxable income or federal adjusted gross income constitutes a conformity issue for the state. The state has the option of conforming or not conforming to federal tax law changes, however, if the state does not conform, it has to add adjustments to state tax forms to add back the income excluded under federal law. In many cases this can substantially complicate state income tax filings.

Recently, the federal government has passed various tax reductions and economic stimulus packages to encourage job creation that have an impact on Arizona tax liability.

Arizona has conformed to all provisions except the special accelerated bonus depreciation and more recently, has not yet addressed the small business expensing provisions.

The Job Creation and Workers Assistance Act of 2002, which was signed by President Bush on March 9, 2002 provided for special accelerated depreciation for businesses that purchase equipment between September 11, 2001 through September

11, 2004. This provision allows for 30% accelerated depreciation of these purchases in the first year. Conformity to this provision would have had an impact of approximately $27.7 million to the state general fund.

In March of 2003, Congress passed the Jobs and Growth Tax Relief Reconciliation Act. This act increased the bonus depreciation from 30% to 50%. The revenue impact to the state is unknown but considered significant. In addition, the Act provided an increase in small business expensing from $25,000 to $100,000. This permits a higher level of capital expenses to be written off in the first year rather than depreciated over time. This item has yet to be addressed by the Legislature but would have an impact to the state general fund of approximately $11 million.

The impact to Arizona taxpayers of not conforming is substantially increased complexity and confusion associated with depreciating assets. By continuing to not conform, Arizona taxpayers will have to keep two sets of books on all assets, one for Arizona depreciation and one for federal depreciation.

- **Income tax credit review adjustments - require state corporate income tax credit information to be used for the evaluation of these credits**

This recommendation would encourage the Legislature to continue to improve information received on tax credits by allowing the exchange of certain state income tax credit information to be used by JLBC for evaluation of the credits.

In 2002, the Legislature established a Joint Legislative Income Tax Review Committee to examine the effectiveness of various tax credits. All individual and corporate income tax credits are now reviewed on a five-year cycle and the first meeting took place last year. The Committee is charged with determining the original purpose of the credits and setting a standard to evaluate and measure the success or failure of the tax credits. The Committee then recommends continuing the current credit, modifying the credit or elimination of the credit. At the first meeting, it became apparent that the strict confidentiality of the income tax credit information constrains what can be evaluated and recommended.

A recent Auditor General report on the Department of Commerce noted the same limitations to evaluating tax credits. The Auditor General also noted that some other states now require full disclosure of corporations taking advantage of tax credits that are intended as business incentives.

This recommendation would require a change in the statute to allow the Department of Revenue to release corporate income tax credit information related to state incentive programs to elected policy makers and their staff in executive session.

Fiscal Impact: No significant fiscal impact is anticipated.

Appendix A

General Information

ARIZONA LEGISLATIVE COUNCIL

MEMO

June 25, 2003

TO: Members of the Tax Reform for Arizona Citizens Committee

FROM: Elizabeth Johnston, Research Analyst

RE: Arizona demographics

This memo compares Arizona's demographics to that of the United States as a whole. Arizona's population is increasing more rapidly than the population of the United States. Its elderly population continues to grow faster than that of the nation. Although Arizona's population is as racially diverse as the U.S., it has fewer African American and more Native American residents. A large portion of Arizona's population is Hispanic and this group will continue to increase faster than the national rate. The percentages of Arizona residents who are graduates of high school or college are almost the same as that of the United States as a whole, but the percentage of non-English speakers in Arizona is much greater.

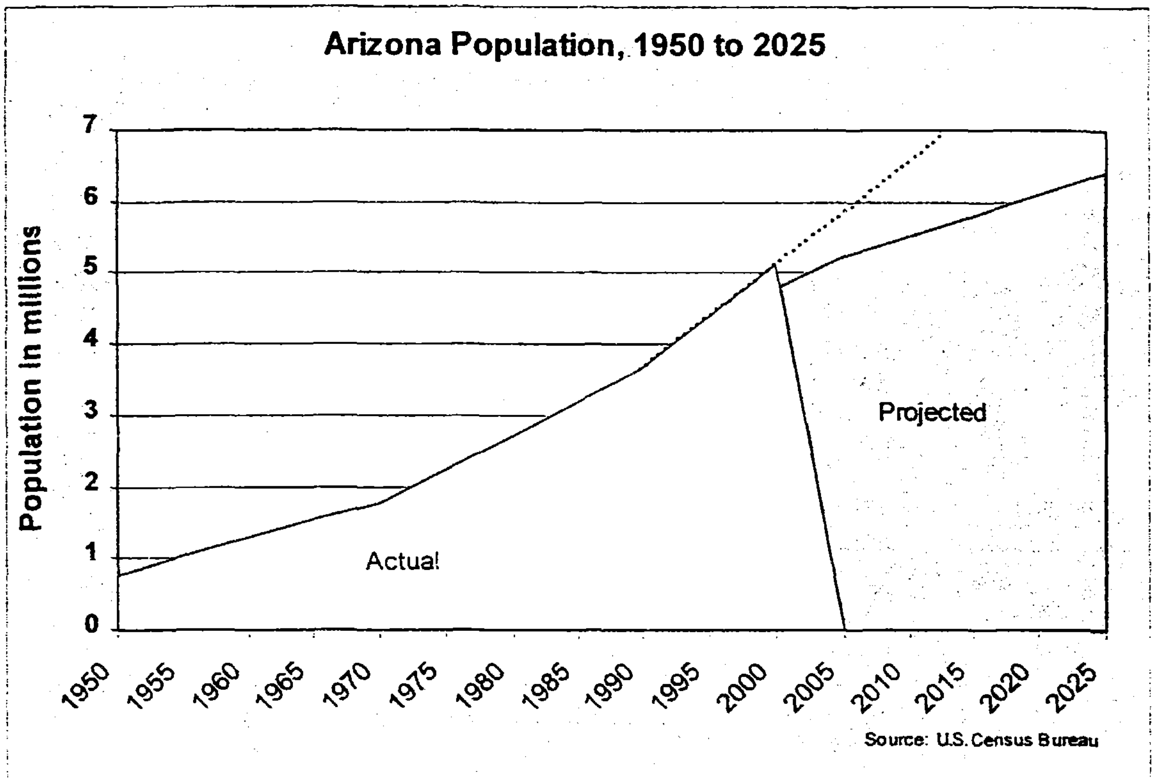
In 2000, 1.8% of the nation's population lived in Arizona. Among the 50 states and the District of Columbia, Arizona ranks as the 20th most populous state. The state had a net increase of almost 1.5 million people during the last decade, the 5th largest net increase in the nation. Its population increase of 40%, ranks as the 2nd largest in the nation.

Arizona's 2000 population of 5,130,632 ranks in just under that of Maryland (population 5,296,486) and just above that of Minnesota (population 4,919,479). However, demographically and in terms of overall growth Arizona has more in common with western mountain states, especially Nevada, Colorado and New Mexico. The states with most rapid population growth over the last decade were Nevada-66.3%, Arizona-40%, Colorado-30.6%, Utah-29.6% and Idaho-28.5%. Elderly residents of western states continue to remain a large part of the overall population increases in these areas. Arizona's population, like other western states, is in large part white, but has growing racial minority groups. Like New Mexico, Arizona has a significant Native American population, ranked 5th in the nation. Arizona also has a large portion of residents of Hispanic descent and an increasing number of residents who speak a language other than English at home. The language other than English most often spoken at home is Spanish.

POPULATION

Arizona's rapid population growth continues to exceed expectations.

Arizona's population was 5,130,632 in 2000. This was a 40% increase over the 1990 census figure of 4,781,468. Based on the 1990 actual population figures, the U.S. Census Bureau projected growth of only 31% during the last decade. The U.S. Census' projections for future growth to over 5.8 million by 2015 and 6.4 million by 2025 appear low when contrasted with Arizona's recent growth. Using 1995 Arizona special census figures in combination with the U.S. Census Bureau figures, the Arizona Department of Economic Security projected that Arizona's population would have increased to more than 6.7 million by 2015 and almost 8 million by 2025. At this rate, Arizona's population would more than double by year 2050.

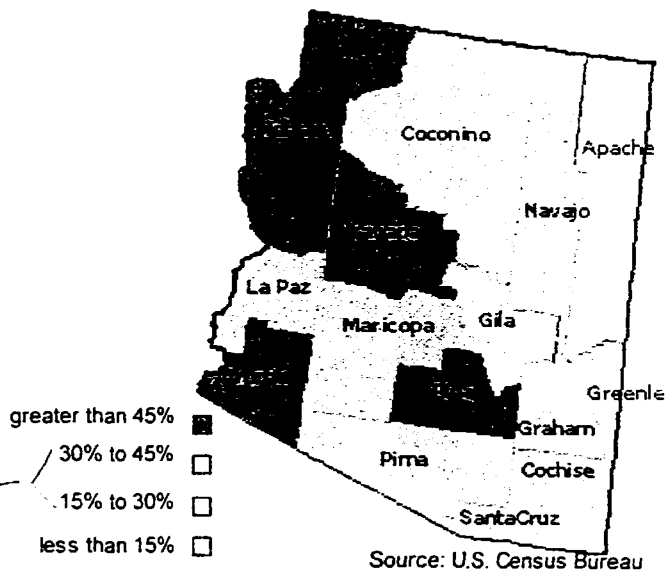


The graph above shows Arizona's population from 1950 using decadal census counts and mid-decade estimates. Beginning in the year 1995, population values are estimates made by the U.S. Census Bureau based on 1990 population figures. These projections understated Arizona's growth during the last decade by 9% and probably understate Arizona's future growth. Projections based on the 2000 census are expected to show larger increases in Arizona's future population.

The United States 2000 population was 281,421,906, an increase of 13.2% since 1990. The nation's population is expected to increase another 23% by year 2025. Arizona's population is growing at a rate double that of the United States as a whole.

Maricopa County is experiencing the majority of Arizona's population growth, some of its cities more than doubling their population between 1990 and 2000.

County Population Growth, 1990 to 2000

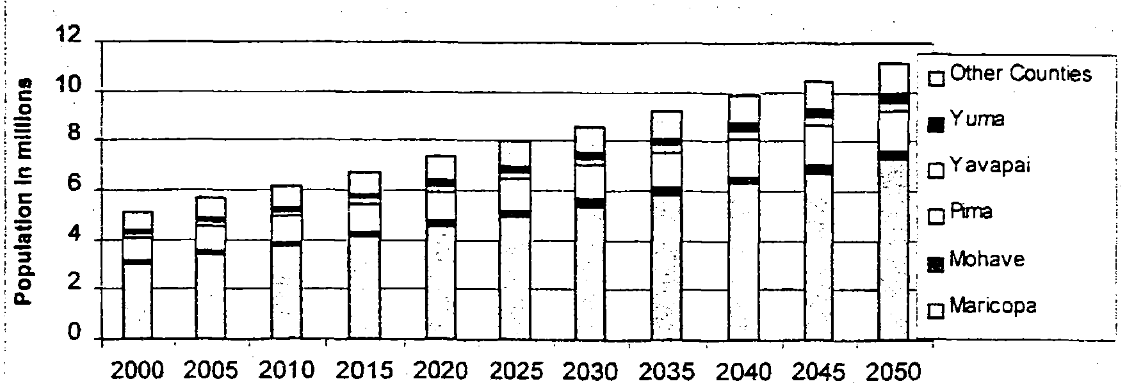


Source: U.S. Census Bureau

Maricopa County can be credited with the majority of the state's increased population, growing by almost 1 million people from 2,122,101 in 1990 to 3,072,149 in 2000. While the total gain in population was enormous, its increase of almost 45% was less than that of four other Arizona counties. Mojave County grew by 66%, Yavapai County by 56%, Pinal County by 54% and Yuma County by just under 50%. La Paz County's growth of 42% seems low in comparison, but was still much larger than the growth of Coconino, Navajo, Gila, Graham, Pima, Cochise and Santa Cruz counties, which grew between 15% to 30%. Only Apache and Greenlee counties grew by less than 15%.

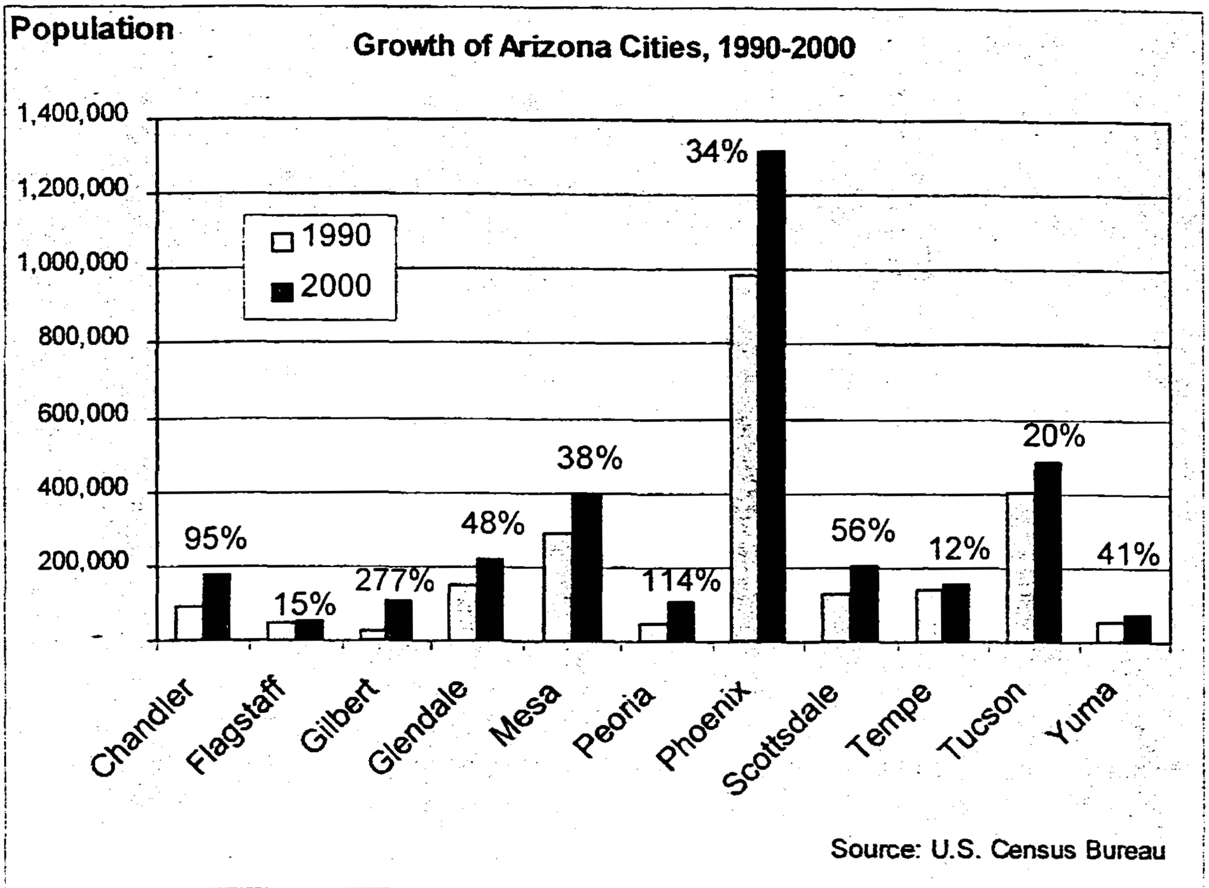
Arizona's population will continue to grow, especially in Maricopa County. The chart below uses Arizona Department of Economic Security special census figures to illustrate the projected growth of Arizona's counties from 2000 to 2050.

Population Projection by Counties, 2000 to 2050



Source: Arizona Dept. of Economic Security, Research Administration, Population Statistics Unit

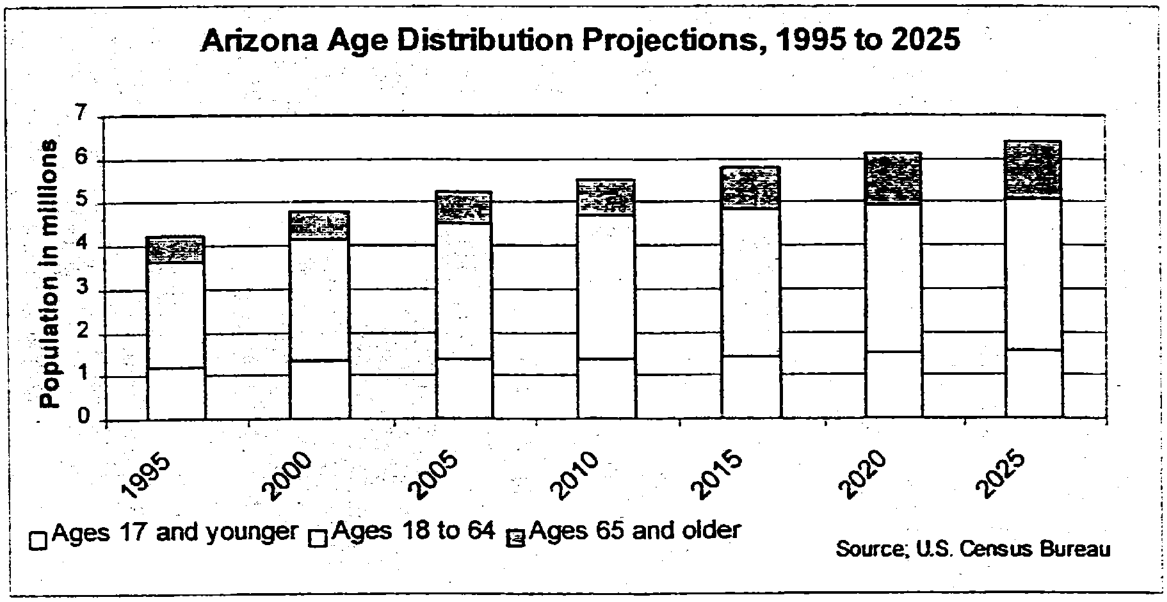
Arizona's population increase can be attributed to the explosive urban growth, especially cities in the Phoenix Metropolitan area. The chart below illustrates the growth of Arizona cities with populations of 50,000 or more.



AGE

Arizona's population is aging and becoming more dependent.

In 2000, the median age in Arizona was 34.2 years. 73.4% of the population was 18 years or older and 13% of the population was 65 years or over. The median age in the United States is 35.3 years. 74.3% of the U.S. population is 18 years or over and 12.4% is 65 years or older. Arizona's elderly, 65 years or older, population is expected to increase to 21.3% by 2025.



Using U.S. Census projections for age distribution in Arizona, the above chart shows a shrinking working-age population in comparison to youths and elderly. These figures are based on 1990 population data.

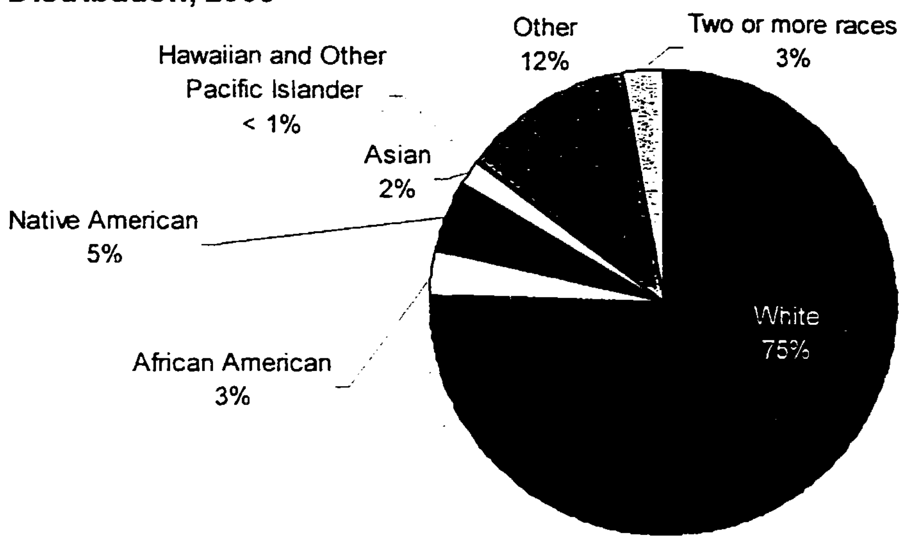
The impact of Arizona's aging population can be understood best by looking at the increase of Arizona's dependency ratio, the proportion of dependent (ages younger than 20 or 65 or older) to active population (ages 20 to 64). For Arizona, the dependency ratio is projected to rise to 94.5 in 2025, the fourth largest dependency ratio in the United States. This means that for every 100 working adults there will be 94.5 dependent individuals in Arizona in 2025.

RACE

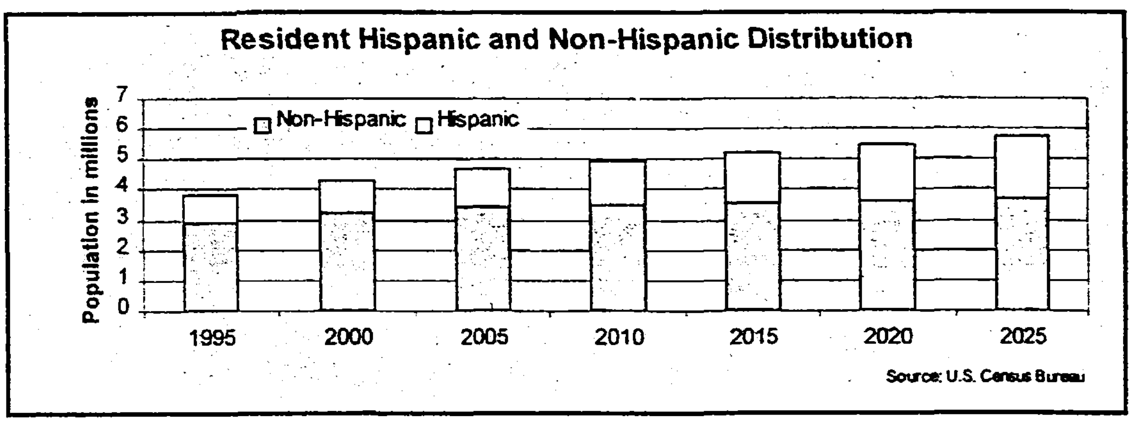
Arizona is racially diverse and its Hispanic population is increasing rapidly.

Approximately 75.5% of Arizona's population is White, 5% Native American, 3.1% African-American, 1.8% Asian, less than 1% Pacific Islander and 11.6% some other race. 2.9% of Arizona's general population describe themselves as members of more than one race. Arizona's racial distribution will change little over the next few decades.

Arizona's Racial Distribution, 2000



Arizona's distribution of residents of Hispanic and non-Hispanic descent will change dramatically. In 2000, 25% of Arizona's population was Hispanic. This number is expected to grow to 32.2% of the state's population by 2025.



In the United States as a whole, 75.1% of the population is White, 12.3% is African-American, .9% is Native American, 3.7% is Asian or Pacific Islander and 5.5% some other race. 2.4% of the United States population describe themselves as members of more than one race. Only 12.5% of the U.S. general population is Hispanic. This population is expected to grow to 16.8% of the nation's population by 2025.

LABOR FORCE AND HOUSEHOLD INCOME

Arizona's labor force looks similar to that of the nation.

Just over 61% of Arizona residents over the age of 16 are in the labor force compared to almost 64% of the nation's labor force. Almost 33% of Arizona's labor force works in management, professional or related occupations, about 29% work in sales or office occupations, 16% are employed as construction, extraction and maintenance employees, almost 11% work in production, transportation or material moving occupations while less than 1% work in farming, fishing and forestry occupations.

The table below lists Arizona's workers by industrial category and compares the percentage in each category to the nation as a whole. Arizona's work force looks similar to that of the nation. However, the nation as a whole does have a greater percentage of manufacturing workers than does Arizona.

Industry	Arizona	% of Arizona Labor Force	% of National Labor Force
Educational, health and social services	402,183	18%	20%
Retail trade	273,864	12%	12%
Professional, scientific, management, administrative and waste management services	229,660	10%	9%
Manufacturing	228,590	10%	14%
Arts, entertainment, recreation, accommodation and food services	225,129	10%	8%
Construction	193,464	9%	7%
Finance, insurance, real estate and rental and leasing	175,311	8%	7%
Public administration	121,618	5%	5%
Transportation, warehousing and utilities	111,186	5%	5%
Other services	103,305	5%	5%
Wholesale trade	73,441	3%	4%
Information	62,577	3%	3%
Agriculture, forestry, fishing, hunting and mining	32,676	1%	2%
Total	2,233,004	100.0%	100.0%
			Source: U.S. Census Bureau

Arizona is slightly behind the nation in terms of median household income.

The median household income in Arizona in 1999 was $40,558 and the median family income was $46,723. This was slightly lower than the national average of $41,994 for households and $50,046 for families. The median earnings for Arizona's full-time, year-round workers were $35,184 for males and $26,777 for females. Nationwide, earnings for full-time, year-round workers were $37,057 for males and $27,194 for females. 9.9% of Arizona's families are below the poverty level while 9.2% of the nation's families are at this level.

EDUCATION

Arizona's percentage of high school and college graduates is on par with national levels.

As of March 2002, 84.6% of Arizona's population 25 years and over had completed high school. 26.3% of the population had a bachelor's degree or higher. This population is almost identical to the United States general population where 84.1% have graduated from high school and 26.7% have a bachelor's degree or higher.

LANGUAGE

Non-English speakers represent a significant and growing portion of Arizona's population.

Significant portions of Arizona's population speak a non-English language at home. In 1990, 20.8% of Arizona's population spoke a non-English language at home, but that number rose to 25.9% in 2000. The non-English language most often spoken in Arizona is Spanish, with 19.5% of Arizona's population speaking it. 2.1% speak other Indo-European languages and 1.3% speak Asian and Pacific Island languages.

Nationwide, 17.9% of the population speak a non-English language at home. This figure rose from 13.8% in 1990.

"THEN AND NOW" - FY 1993 vs. FY 2003 General Fund Revenue and Carry-Forward Balances

General Fund Revenue, Expenditures and Carry Forward Balances
($ in Millions)

Fiscal Year	Revenue	Expenditures	Carry Forward	Carry Forward as a % of Revenue
1993	3,790.0	3,704.0	86.0	2.3%
1994	4,159.3	3,930.1	229.2	5.5%
1995	4,694.6	4,425.1	269.5	5.7%
1996	4,932.5	4,532.6	399.9	8.1%
1997	5,410.3 1/	4,894.3	516.0	9.5%
1998	5,745.4	5,232.0	513.4	8.9%
1999	6,148.7	5,893.3	255.4	4.2%
2000	6,215.7	6,012.3	203.4	3.3%
2001	6,381.0	6,367.7	13.3	0.2%
2002	6,342.2	6,341.2	1.0	0.0%
2003	6,174.9	6,168.8	6.1	0.1%

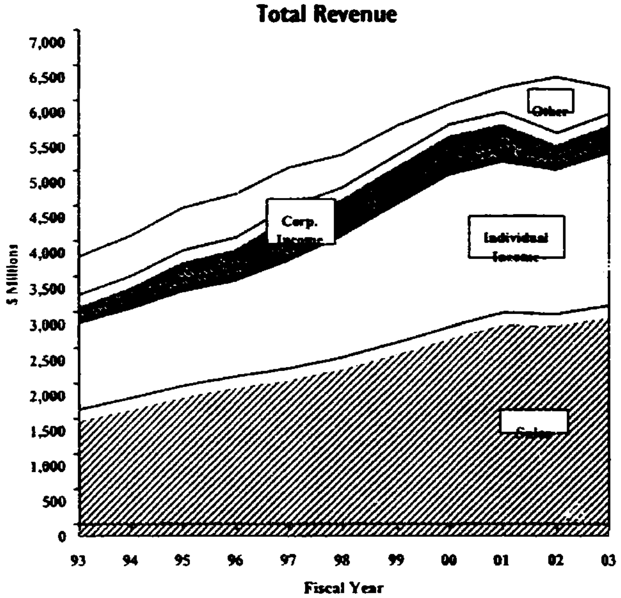
1/ Includes carry-forward of $370.4 million.

General Fund Major Tax Sources as a Percent of Total Base Revenue

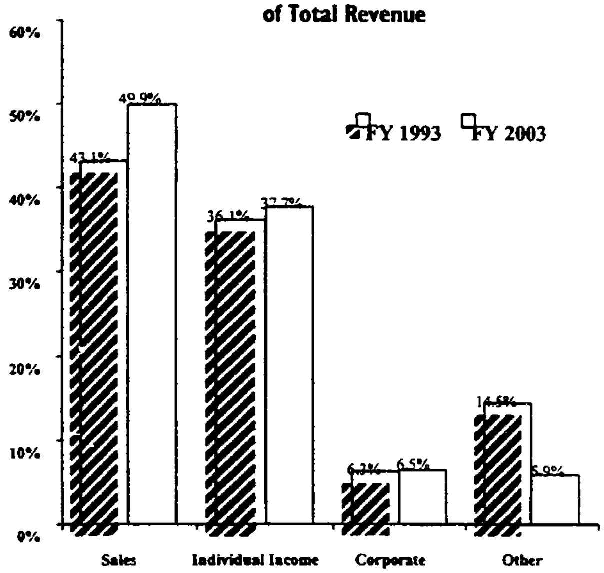
Fiscal Year	Sales	Individual Income	Corporate Income	Other
1993	43.1%	36.1%	6.3%	14.5%
1994	44.0%	34.5%	7.4%	14.1%
1995	44.1%	33.1%	9.3%	13.5%
1996	45.1%	32.0%	9.6%	13.3%
1997	43.9%	33.1%	11.9%	11.1%
1998	45.3%	35.6%	10.1%	9.0%
1999	45.7%	37.2%	9.7%	7.4%
2000	46.9%	38.9%	9.3%	4.8%
2001	48.3%	37.2%	8.8%	5.8%
2002	46.9%	34.8%	5.7%	12.6% 1/
2003	49.9%	37.7%	6.5%	5.9%

1/ Includes $547.2 million in one-time revenue enhancements.

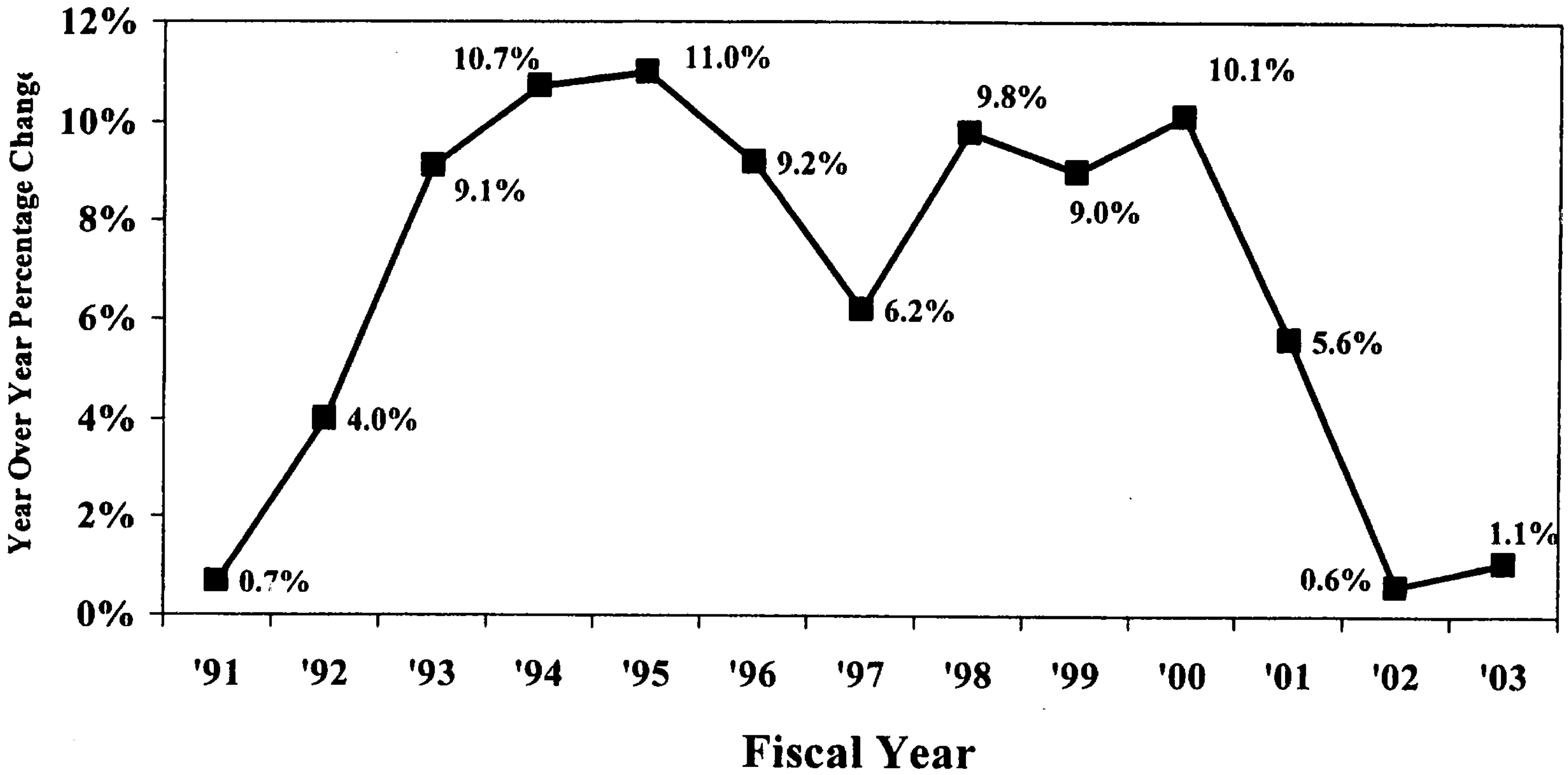
General Fund Major Tax Sources as a Share of Total Revenue



FY 1993 vs. FY 2003 Major Tax Sources as a Percent of Total Revenue



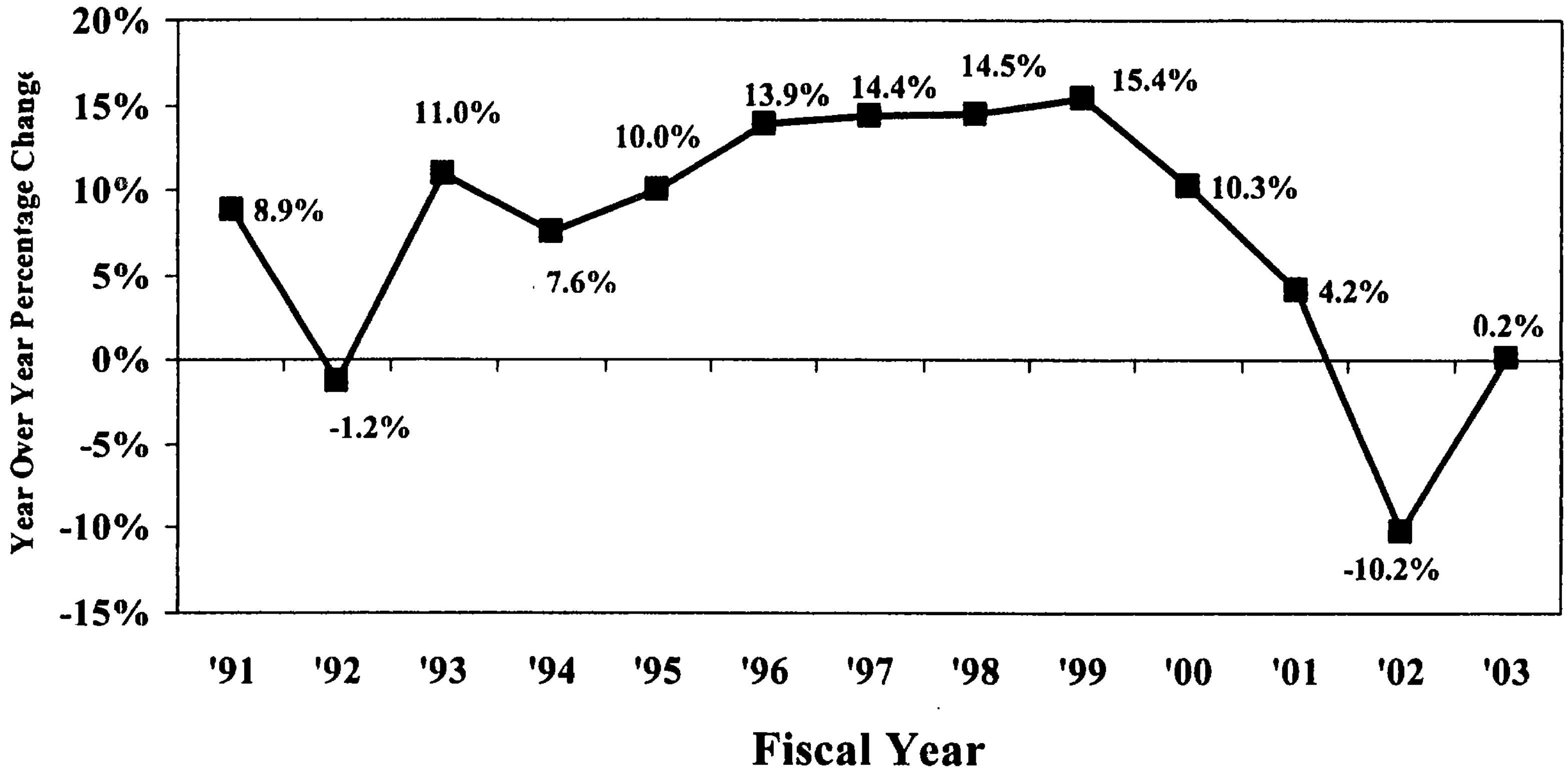
Sales Tax
Baseline % Change



9/9/03

Individual Income Tax

Baseline % Change



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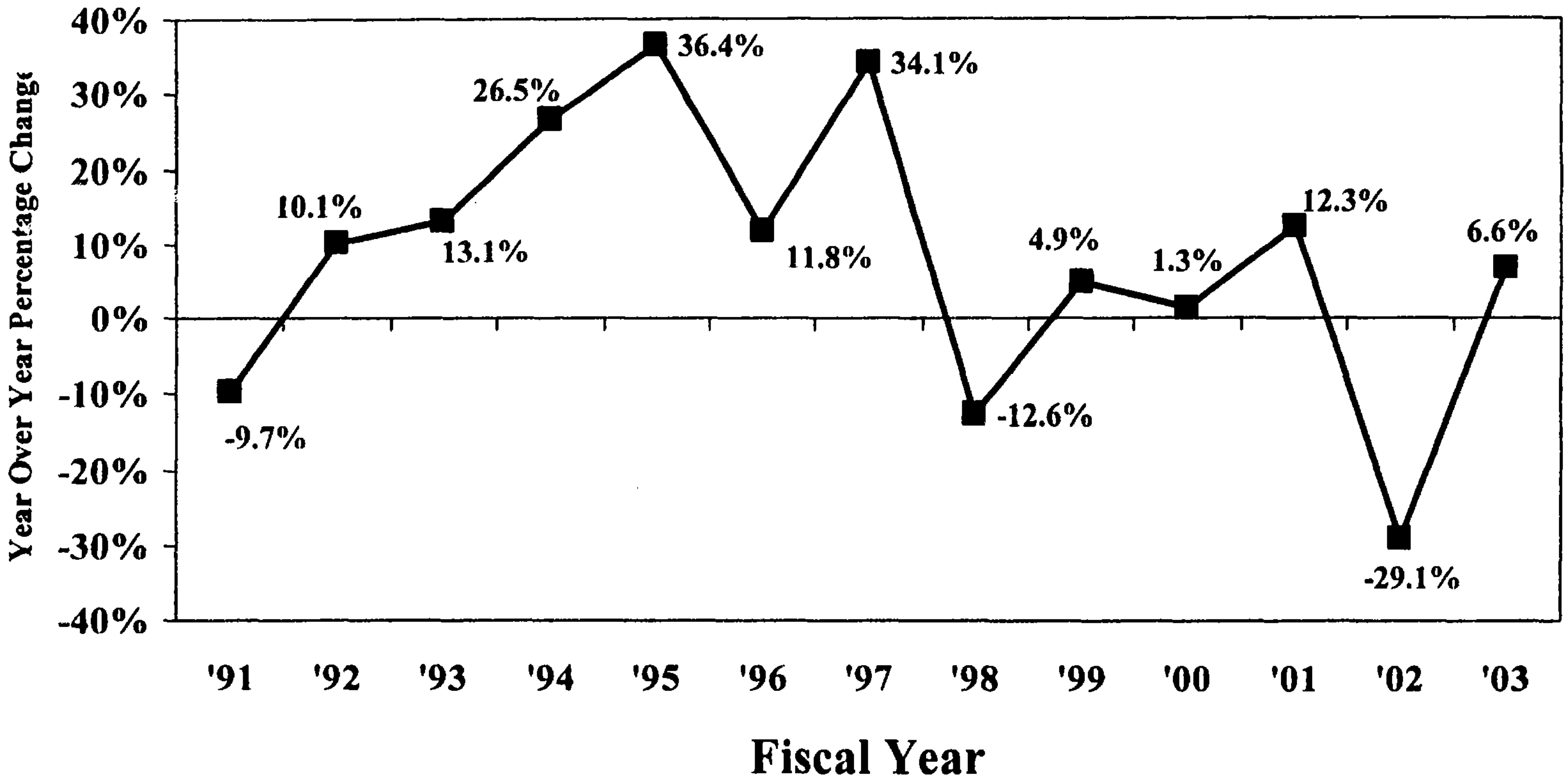
Corporate Income Tax

Baseline % Change



9/9/03

PRINCIPLES FOR EVALUATING STATE TAX SOURCES

In 1991, a bipartisan group of state legislators, legislative staff, and other public and private sector representatives identified nine principles to evaluate the quality and effectiveness of state revenue systems.[1] Six of these nine principles are especially appropriate for evaluating individual tax sources within the state revenue mix, while the remaining three principles address the interrelationships of tax systems within the state revenue system as a whole.

This handbook evaluates major state revenue sources by the six principles—reliability, equity, compliance and administration, responsiveness to interstate and international competition, economic neutrality, and accountability—that are appropriate for evaluating individual tax sources. These six principles are described below.

Reliability

Reliability has three primary components: stability, certainty and sufficiency. Stability implies that revenues are relatively constant over time and not subject to unpredictable fluctuations. Certainty means that the number and type of tax changes are kept at a minimum to allow businesses and individuals to plan for the future. Sufficiency requires that revenue sources provide the revenue growth necessary to finance the desired rate of growth of spending. The reliability of different types of tax sources varies greatly, depending on the type of activity being taxed. States can improve the reliability of their tax systems by imposing a balanced mix of taxes.

Equity

Equity has two primary components—horizontal equity and vertical equity. Horizontal equity means that taxpayers with similar economic circumstances have similar tax burdens. Vertical equity refers to the distribution of tax burdens among taxpayers with different economic circumstances. In a progressive tax system, the share of income paid in taxes increases as income rises. In a regressive tax system, the share of income paid in taxes is greatest for low-income taxpayers and falls as income rises. States rely on many consumption tax sources that are regressive by nature; it is very difficult to design a progressive state tax system. However, many tax policy experts believe that, at a minimum, a fair state tax system minimizes both regressivity and the tax burden on low-income households.

Compliance and Administration

A quality tax system facilitates taxpayer compliance by minimizing the time and effort necessary to comply with the law. It also minimizes the cost of the state administrative apparatus necessary to collect revenue, enforce the law, and audit to ensure compliance with the law. Complex taxes that are expensive to enforce reduce the yield of the tax system and result in wasted taxpayer resources.

Responsiveness to Interstate and International Competition

A state tax system does not operate in a vacuum—lawmakers must recognize that the tax policies of surrounding states can limit the revenue potential of some taxes. Businesses that sell in a national or global marketplace can relocate if state business taxes are too burdensome. Individuals may choose to shop in neighboring states if specific state consumption tax differentials are high.

Economic Neutrality

Taxes, by their very nature, are not economically neutral. Tax policy can encourage or discourage consumption of goods and services, influence decisions to save and invest, and affect fundamental business decisions about the use of labor and capital. A quality tax system tries to minimize the effect of the tax system on the allocation of resources in the economy. When lawmakers decide to use the tax system to make budget decisions or influence behavior, these decisions should be explicit and subject to frequent evaluation and review. Taxes with broad bases and low rates, spread across a wide range of sources and economic activities, reduce the effect of taxation on economic decisions.

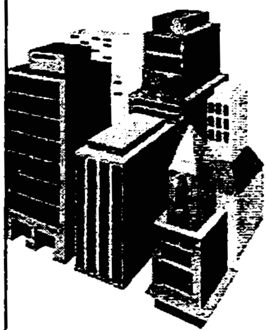
Accountability

The essence of accountability is that tax burdens should be explicit, not hidden. This principle can be applied to state taxes in two ways. First, credits and exemptions in the tax code should be minimized and reviewed frequently to determine their cost (in lost revenue) and to determine whether they are unfairly benefiting some taxpayers at the expense of others. Second, taxes that are designed to be "passed through" to consumers provide less accountability than taxes that are paid directly and openly by taxpayers.

Appendix B

Property Tax Information

Property Taxation In Arizona



Tax Reform for Arizona
Citizens Committee
June 2003

State & Local Property Taxes

FY 1999 Census

Per capita:	$750	Ranking: 33
Per $1,000 of Income:	$ 31.82	Ranking: 25

Industrial Property Tax Rankings

2000 Ranking: 3rd

Net Tax $1,542,236 ETR 3.084%

U.S. Average $864,752 ETR 1.730%

Residential Property Tax Rankings

2000 Ranking: 31st

Net Tax $1,741 ETR 0.871%

U.S. Average $2,271 ETR 1.136%

Secondary Values

- Track Full Cash Value of the Property
- No Limit on Growth of Taxes
- Pays Secondary Taxes:
  - General Obligation Bonds
  - Overrides
  - Special Districts

Primary or Limited Values

- Limit on Growth in Value
- Limit on Homeowner's taxes

  Valuation Limit

  ❖ 10% a Year

  OR

  ❖ 25% of the difference between the past Primary Value and the new Secondary Value

Assessment Ratios

Class	Description	Assessment Ratio
1	Commercial, Industrial, Utilities, & Mines	25%
2	Agricultural & Vacant Land	16%
3	Owner-occupied Residential	10%
4	Rental Residential	10%
5	Railroad, Private car, airline flight	21%
6	Residential historic, Enterprise zones	5%
7	Commercial Historic	1%
8	Rental Residential Historic	1%
9	Possessory Interests	1%
Total		

Valuation
The starting point

Full Cash Value (FCV) synonymous with market value

Three Approaches to value:

- Cost
- Income
- Market

Valuation
The starting point

Statutory Formulas:

- -- Electric Utilities
- – Telecommunications
- – Pipelines
- – Golf Courses
- – Shopping Centers
- – Agricultural Property
- – Locally Assessed Personal Property

Property Tax Exemptions

- Article 9, Section 2 - Arizona Constitution
  - – exempts all federal, state, county and municipal properties
  - – allows exemptions "by law" for property of educational, charitable and religious association not used or held for profit
  - – other specific exemptions

Personal Property Reductions

- Accelerated depreciation for first 5 years
- Minimum value reduced from 20% to 10% - then again to 2 1/2 %
- 1% assessment ratio for certain amounts of personal property
- Replaced 1% AR for ballot-approved exemption in 1996 for first $50,000 of personal property (indexed for inflation each year)

Personal Property Reductions

- Work-in-progress/Livestock, poultry, aquatic animals and honeybees
- Personal property also subject to same reductions as real property:
  - assessment ratio phase down for mines and utility properties
  - elimination of state property tax rate
  - reductions in QTR

Truth-In-Taxation

- Truth-in-Taxation is designed to make property owners aware of valuation increases effect on property taxes.
  - When value increases and the property tax rate remains the same, more taxes are collected
  - Government must adjust rate downward to collect same amount of revenue
- Requires public hearings if a government entity is going to collect higher taxes than the previous year through their property tax rate

State Property Tax Rate

- Repealed in 1996
- Two rates
  - general purposes (zero rate)
  - education (47 cent rate/capped at $1.25)
- Combination of rates could not exceed $1.60
- Used to offset state aid

County Education Tax Rate

- Statutory rate mandated since 1981
- Used to offset state education aid in each county
- Funds distributed to each school based on need for additional education aid within the county
- Originally 50 cents, increased to 53 cents, reduced through TNT compliance

Qualifying Tax Rate

- The Qualifying Tax Rate - QTR - is a statutory property tax rate used in the school finance formula to determine the mix of state and local monies used to fund the maintenance & operations costs of school districts

Qualifying Tax Rate

- District determines expenditure budget
- QTR is applied to the district's primary assessed valuation to determine what amount is raised
- Local effort from QTR is subtracted from expenditure budget
- County revenue from county education equalization rate is provided based on percentage of need for each district in the county
- Remaining amount provided by basic state aid

Effect of QTR changes

- If the QTR is *increased* the local portion of revenues is increased and the state portion is decreased
- If the QTR is *decreased* the local portion of revenues is decreased and the state portion is increased
- Regardless of QTR changes - total revenue to school districts remains the same

Minimum QTR

- Is applied to school districts NOT receiving state aid
- First implemented in 1989
- Changed over the years
- Current MQTR is 50% of the QTR applied to all classes of property
  - homeowner property receives homeowner's rebate

Property Outside School Districts

- Property not located in a school district must also pay 50% of QTR
- First enacted in 1988
  - Full QTR applied to all property except homeowners
  - homeowner's phased-in starting at 50 cents per $100 of AV
- Homeowner property also receives the homeowner's rebate

Additional State Aid Programs

- Homeowner's "Rebate"
  - 35% of owner-occupied residential properties primary school rate is paid by state
- 1% constitutional cap
  - owner-occupied residential properties primary taxes are capped at 1% of home's FCV - anything above cap is paid by state

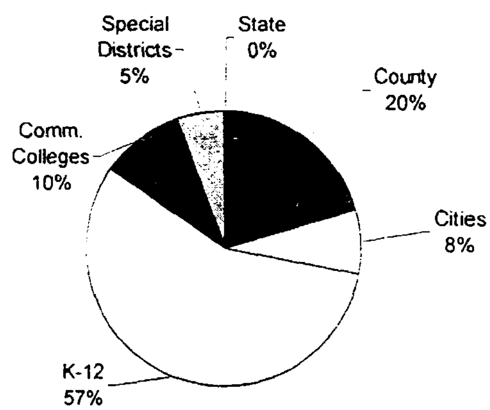
Items Outside School Budget Limits

- Desegregation Expenses
- Excess Utilities
- Adjacent Ways
- Small School Adjustments
- Liabilities in Excess
- Budget Balance Carry Forward
- Dropout Prevention
- Registered Warrants

2002 Total Levies

Jurisdiction	Total Levies	% of Total
State	$13,801,961	0%
County	$890,737,029	20%
Cities	$333,649,560	8%
K-12	$2,519,747,805	57%
Community Colleges	$428,207,414	10%
Special Districts	$242,408,564	5%
Totals	$4,428,552,333	100%

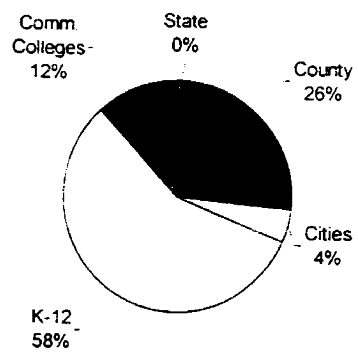
2002 Total Levies



2002 Total Primary Levies

Jurisdiction	2002 Primary Levies	% of Total
State	$13,801,961	0%
County	$782,078,487	26%
Cities	$130,659,803	4%
K-12	$1,697,031,236	57%
Community Colleges	$360,156,006	12%
Totals	$2,983,727,493	100.00%

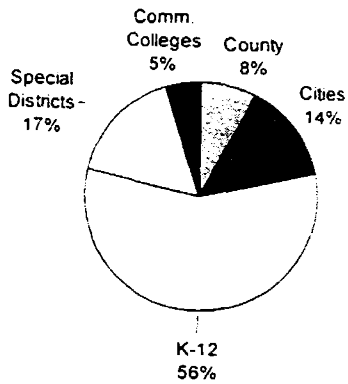
2002 Total Primary Levies



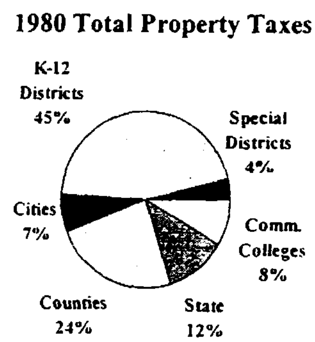
2002 Total Secondary Levies

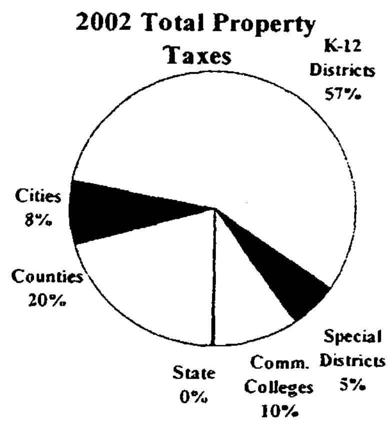
Jurisdiction	2002 Secondary Levies	% of Total
County	108,658,542	8%
Cities	202,989,757	14%
K-12	822,716,569	57%
Special Districts	242,408,564	17%
Community Colleges	68,051,408	5%
Totals	1,444,824,840	100%

2002 Total Secondary Levies



Growth in total levies 1980-2002

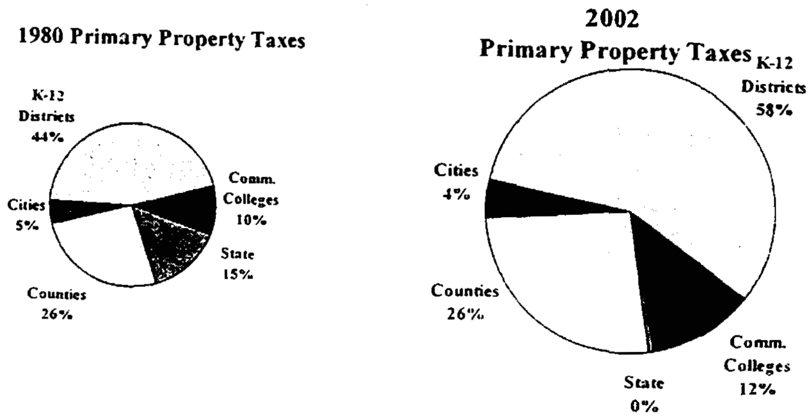




Growth in total levies 1980-2002

Jurisdiction	Totals 1980	Totals 2002	$ Change	% Change
State	$96,260,779	$13,801,961	-$82,458,818	-85.7%
County	$196,264,468	$890,737,029	$694,472,561	353.8%
Cities	$56,466,423	$333,649,560	$277,183,137	490.9%
School Districts	$372,198,427	$2,519,747,805	$2,147,549,378	577.0%
Special Districts	$32,391,567	$242,408,564	$210,016,997	648.4%
Community Colleges	$68,014,378	$428,207,414	$360,193,036	529.6%
TOTALS	$821,596,042	$4,428,552,333	$3,606,956,291	439.0%

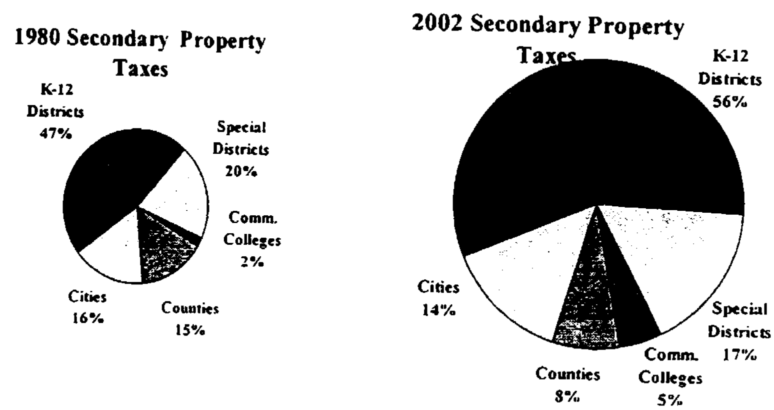
Growth in Primary Levies 1980-2002



Growth in Primary Levies 1980-2002

Taxing Jurisdiction	Primary 1980	Primary 2002	$ Change	% Change
State	96,260,779	13,801,961	(82,458,818)	-85.7%
County	171,912,244	782,078,487	610,166,243	354.9%
Cities	30,962,718	130,659,803	99,697,085	322.0%
School Districts	295,918,623	1,697,031,236	1,401,112,613	473.5%
Special Districts	-	-		-
Community Colleges	64,697,154	360,156,006	295,458,852	456.7%
Totals	659,751,518	2,983,727,493	2,323,975,975	352.3%

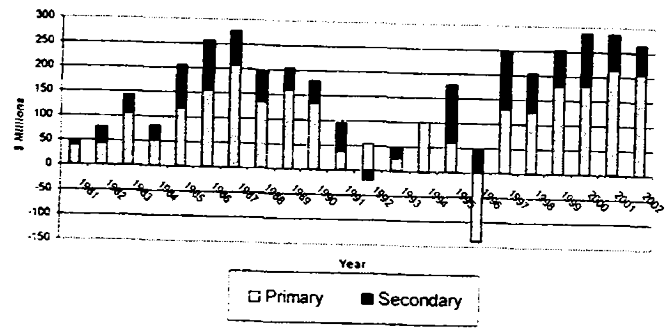
Growth in Secondary Levies 1980-2002



Growth in Secondary Levies 1980-2002

Jurisdiction	Secondary 1980	Secondary 2002	$ Change	% Change
State				
County	$24,352,224	$108,658,542	$84,306,318	346.2%
Cities	$25,503,705	$202,989,757	$177,486,052	695.9%
School Districts	$76,279,804	$822,716,569	$746,436,765	978.6%
Special Districts	$32,391,567	$242,408,564	$210,016,997	648.4%
Community Colleges	$3,317,224	$68,051,408	$64,734,184	1951.5%
TOTALS	$161,844,524	$1,444,824,840	$1,282,980,316	792.7%

Growth in Levies, 1980–2002 Primary & Secondary

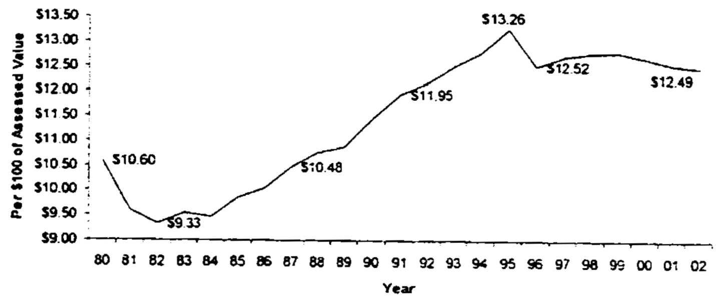


Per Capita Property Tax Collections 1980-1990-2000

Inflation adjusted to 1980 $

Year	Collections	Per Capita	Decade change	%	Inflation adjusted	Decade change	%
1980	$821,596,042	$302.28			$302.28		
1990	$2,506,010,794	$680.83	$378.55	125.2%	$444.11	$141.83	46.9%
2000	$3,874,688,668	$767.68	$86.85	12.8%	$408.25	-$35.85	-8.1%
	1980 to 2000 growth:		$465.40	154.0%		$105.97	35.1%

Statewide Average Combined Property Tax Rate



2001 Effective Tax Rates

Class	Description	Effective Rate
1	Commercial, Industrial, Utilities, & Mines	2.90%
2	Agricultural & Vacant Land	1.66%
3	Owner-occupied Residential	1.05%
4	Rental Residential	1.25%
5	Railroad, Private car, airline flight	2.48%
6	Residential historic, Enterprise zones	0.59%
7	Commercial Historic	2.26%
8	Rental Residential Historic	0.02%
9	Possessory Interests	0.10%
Total		**1.55%**

Fiscal 2000

- Official name - Arizona Joint Select Committee on State Revenues and Expenditures
- Members were legislators and private sector representatives
- Hired separate Director and staff
- Study completed for the Arizona Legislature in November 1989

Fiscal 2000

- The Committee summarized their findings and implications
- The Committee made recommendations for closing the structural deficit
- The Committee first determined criteria
  - The purpose of defining a set of criteria for evaluating a fiscal system is to provide a common, general framework that policymakers can refer to when policy options are considered.

Since the Fiscal 2000 Report

- Criteria for judging a fiscal system remains valid and useful
- Many of the findings are still accurate
- Legislature has enacted some of the revenue recommendations

Fiscal 2000 Property Tax Recommendations

- Only 3 classes of property:
  - residential
  - vacant land and agriculture
  - commercial and industrial
- The highest assessment ratio should be no more than twice the lowest assessment ratio
- The distinction between full cash value and limited value should be eliminated

This information is deemed reliable; however, is subject to audit

Property Tax Exemption	Eligibility	Number	Exempt Assessed Value
42-11102	Government property: county, state, municipal and federal property	23,468	15,717,530,760
42-11103	Government bonds		
42-11104	Non-profit library and school property, or property leased from school districts	130	132,565,748
42-11105	Non-profit health care facility property	265	681,205,851
42-11106	Non-profit residential apartment housing property for elderly or handicapped persons either adjoined to a non-profit health care facility or supported by public funding.	173	185,637,727
42-11107	Non-profit charitity property used for the relief of indigent or afflicted persons	566	262,712,605
42-11108	Non-profit agricultural society land if it is only used for that purpose	1	823,476
42-11109	Non-profit religious land used for worship	3,062	1,793,597,818
42-11110	Cemetary property	43	31,146,300
42-11111	$3,000 exemption for property of widows, widowers and disabled persons if the total assessment does not exceed $10,000, and they earn less than the income threshold (Article IX, Section 2.3)	9,567	16,096,873
42-11112	Non-profit observatory property used for astronomical research and education	6	30,540,665
42-11113	Non-profit animal shelter or humane society property	6	908,924
42-11114	Property held by charitable organizations that will be donated to the government as parkland, if the property does not receive rent or valuable consideration	35	5,755,780
42-11115	Property held by charitable organizations to preserve and protect scientific, biological, geological, paleontological, natural or archaeological resources	37	16,209,377
42-11116	Non-profit property of musical, dramatic, dance and community arts groups, botanical gardens, museums and zoos if qualified as nonprofit charitable organizations	31	18,162,406
42-11117	Volunteer fire department property if the property is used exclusively for fire suppression and prevention activities and is not used for the benefit of any person	2	377,654
42-11118	Property owned by a volunteer nonprofit organization that is operated exclusively to promote social welfare and provide community quasi-governmental services in an unincorporated area of a county	4	2,913,932
42-11119	Non-profit property owned by a volunteer organization that is used exclusively for the purpose of performing roadway cleanup and beautification on a gratuitous basis		
42-11120	Non-profit property owned by a United States veterans' organization that uses the property for charitable purposes	58	22,208,883
42-11121	Non-profit property owned by a community service organization if the community service organization is primarily engaged in delivering services on that property consisting of fitness programs, camping programs, health and recreation services, etc.	130	72,135,629

This information is deemed reliable; however, is subject to audit

42-11122	A commodity, as defined in 7 United States Code section 2, that is consigned for resale in a warehouse in this state in or from which the commodity is deliverable on a contract for future delivery subject to the rules of a commodity market regulated by the United States commodity futures trading commission		
42-11123	Animal and poultry feed, including salts, vitamins and other additives, for animal or poultry consumption		
42-11124	A non-profit possessory interest consisting of property or improvements pursuant to a lease from this state if it is used by an association or institution involved in educational or charitable activities and its annual gross revenues do not exceed fifty thousand dollars		
42-11125	Stocks of raw or unfinished materials, unassembled parts, work in progress or finished products that constitute the inventory of a retailer, wholesaler or manufacturer that is located in this state and that is principally engaged in reselling the materials, parts or products		
42-11126	Livestock and poultry, aquatic animals and bee colonies		
42-11127	$50,000 exemption on business or agricultural personal property (Article IX, section 2)	52,268	135,120,560
42-11128	Personal property in transit in this state		
42-11129	Non-profit property owned by a fraternal society or organization, if the net earnings of the fraternal society or organization are devoted exclusively to religious, charitable, scientific, literary, educational or fraternal purposes	45	17,104,761
Article IX, Sec 2	Several exemptions covered by statute; household goods used for non-commercial purposes; stocks of raw or finished materials constituting the invertory of a retailer for resale; property of honorably dischaged military personnel living in AZ since 1945, in varying amounts; widows who make a certain amont of money, in varying amounts.		
Article IX, Sec 18	Senior Property Freeze	15,160	1,448,668

Total		**105,057**	**19,144,204,397**

Home vs. Business Taxes - Selected Districts
2002 Tax Rates

Note:
Assumes primary and secondary values are the same
All rates are per $100 of assessed value

Phoenix/Phoenix Elem/Phoenix Union/Maricopa County					
Taxing Jurisdiction	Tax Rates	$150,000 Home	Additional State Aid	$150,000 adjusted for add'l aid	$150,000 Commercial
Primary Rates:					
Elem School	$4.4679	670.19	$234.56	435.62	$1,675.46
High School	$3.5323	529.85	$185.45	344.40	$1,324.61
County Ed	$0.4889	73.34		73.34	$183.34
Com College	$0.9634	144.51		144.51	$361.28
City	$0.7982	119.73		119.73	$299.33
County	$1.2108	181.62		181.62	$454.05
Total Primary	$11.4615	1,719.23		1,299.21	$4,298.06
Secondary Rates:					
Elem School	$2.5791	386.87		386.87	$967.16
High School	$0.8449	126.74		126.74	$316.84
Com College	$0.1493	22.40		22.40	$55.99
City	$1.0218	153.27		153.27	$383.18
County	$0.0800	12.00		12.00	$30.00
Flood Control	$0.2119	31.79		31.79	$79.46
Library	$0.0421	6.32		6.32	$15.79
CAP	$0.1300	19.50		19.50	$48.75
FDAT	$0.0091	1.37		1.37	$3.41
Total Secondary	$5.0682	760.23		760.23	$1,900.58
TOTAL TAXES	$16.5297			2,059.44	$6,198.64
				1.4% of value	4.1% of value

Gilbert/Gilbert Unified/Maricopa County					
Taxing Jurisdiction	Tax Rates	$150,000 Home	Additional State Aid	$150,000 adjusted for add'l aid	$150,000 Commercial
Primary Rates:					
Gilbert Unifed	$4.6805	702.08	$245.73	456.35	$1,755.19
County Ed	$0.4889	73.34		73.34	$183.34
EVIT	$0.0561	8.42		8.42	$21.04
Com College	$0.9634	144.51		144.51	$361.28
City	$0.0000	0.00		0.00	$0.00
County	$1.2108	181.62		181.62	$454.05
Total Primary	$7.3997	1,109.96		864.23	$2,774.89
Secondary Rates:					
Gilbert Unifed	$3.6739	551.09		551.09	$1,377.71
Com College	$0.1493	22.40		22.40	$55.99
City	$1.1500	172.50		172.50	$431.25
County	$0.0800	12.00		12.00	$30.00
Flood Control	$0.2119	31.79		31.79	$79.46
Library	$0.0421	6.32		6.32	$15.79
CAP	$0.1300	19.50		19.50	$48.75
FDAT	$0.0091	1.37		1.37	$3.41
Total Secondary	$5.4463	816.95		816.95	$2,042.36
TOTAL TAXES	$12.8460			1,681.17	$4,817.25
				1.1% of value	3.2% of value

Tucson/Tucson Unified/Pima County					
Taxing Jurisdiction	Tax Rates	$150,000 Home	Additional State Aid	$150,000 adjusted for add'l aid	$150,000 Commercial
Primary Rates:					
Tucson Unified	$7.6124	1,141.86	$399.65	742.21	$2,854.65
County Ed	$0.4889	73.34		73.34	$183.34
Com College	$1.1530	172.95		172.95	$432.38
City	$0.2089	31.34		31.34	$78.34
County	$4.0720	610.80		610.80	$1,527.00
Total Primary	$13.5352	2,030.28	$130.73		
		2,030.28	$530.38	1,499.90	$5,075.70
Secondary Rates:					
Tucson Unified	$1.6656	249.84		249.84	$624.60
Com College	$0.3803	57.05		57.05	$142.61
City	$0.9113	136.70		136.70	$341.74
County	$0.8150	122.25		122.25	$305.63
Flood Control	$0.3546	53.19		53.19	$132.98
Library	$0.2124	31.86		31.86	$79.65
CAP	$0.1300	19.50		19.50	$48.75
FDAT	$0.0458	6.87		6.87	$17.18
Total Secondary	$4.5150	677.25		677.25	$1,693.13
TOTAL TAXES	$18.0502	$2,707.5300		2,177.15	$6,768.83
				1.5% of value	4.5% of value

Oro Valley/Amphitheater/Pima County					
Taxing Jurisdiction	Tax Rates	$150,000 Home	Additional State Aid	$150,000 adjusted for add'l aid	$150,000 Commercial
Primary Rates:					
Amphitheater Unified	$4.9565	743.48	$260.22	483.26	$1,858.69
County Ed	$0.4889	73.34		73.34	$183.34
Com College	$1.1530	172.95		172.95	$432.38
City	$0.0000	0.00		0.00	$0.00
County	$4.0720	610.80		610.80	$1,527.00
Total Primary	$10.6704	1,600.56		1,340.34	$4,001.40
Secondary Rates:					
Amphitheater Unified	$2.0642	309.63		309.63	$774.08
Com College	$0.3803	57.05		57.05	$142.61
City	$0.0000	0.00		0.00	$0.00
County	$0.8150	122.25		122.25	$305.63
Flood Control	$0.3546	53.19		53.19	$132.98
Library	$0.2124	31.86		31.86	$79.65
CAP	$0.1300	19.50		19.50	$48.75
FDAT	$0.0458	6.87		6.87	$17.18
Total Secondary	$4.0023	600.35		600.35	$1,500.86
TOTAL TAXES	$14.6727	2,200.91		1,940.69	$5,502.26
				1.3% of value	3.7% of value

Flagstaff/Flagstaff Unified/Coconino County					
Taxing Jurisdiction	Tax Rates	$150,000 Home	Additional State Aid	$150,000 adjusted for add'l aid	$150,000 Commercial
Primary Rates:					
Flagstaff Unified	$5.3210	798.15	$279.35	518.80	$1,995.38
County Ed	$0.4889	73.34		73.34	$183.34
Com College	$0.4083	61.25		61.25	$153.11
City	$0.7326	109.89		109.89	$274.73
County	$0.4153	62.30		62.30	$155.74
Total Primary	$7.3661	1,104.92		825.56	$2,762.29
Secondary Rates:					
Flagstaff Unified	$1.4380	215.70		215.70	$539.25
Com College	$0.1726	25.89		25.89	$64.73
City	$0.9801	147.02		147.02	$367.54
County	$0.0000	0.00		0.00	$0.00
Library	$0.1899	28.49		28.49	$71.21
FDAT	$0.1000	15.00		15.00	$37.50
Total Secondary	$2.8806	432.09		432.09	$1,080.23
TOTAL TAXES	$10.2467	1,537.01		1,257.65	$3,842.51
				.8% of value	2.6% of value

Globe/Globe Unified/Gila County					
Taxing Jurisdiction	Tax Rates	$150,000 Home	Additional State Aid	$150,000 adjusted for add'l aid	$150,000 Commercial
Primary Rates:					
Globe Unified	$3.5750	536.25	$187.69	348.56	$1,337.05
County Ed	$0.4889	73.34		73.34	$182.85
Com College	$0.0000	0.00		0.00	$0.00
City	$1.3300	199.50		199.50	$497.42
County	$4.4100	661.50		661.50	$1,649.34
Total Primary	$9.8039	1,470.59		1,282.90	$3,666.66
Secondary Rates:					
Globe Unified	$1.6171	242.57		242.57	$604.80
Com College	$0.5823	87.35		87.35	$217.78
City	$0.0000	0.00		0.00	$0.00
County	$0.0000	0.00		0.00	$0.00
Library	$0.2000	30.00		30.00	$74.80
FDAT	$0.1000	15.00		15.00	$37.40
Total Secondary	$2.4994	374.91		374.91	$934.78
TOTAL TAXES	$12.3033	1,845.50		1,657.81	$4,601.43
				1.1% of value	3.1% of value

Hayden/Hayden-Winkleman Unified/Gila County					
Taxing Jurisdiction	Tax Rates	$150,000 Home	Additional State Aid	$150,000 adjusted for add'l aid	$150,000 Commercial
Primary Rates:					
H-W Unified	$7.8742	1,181.13	$413.40	767.73	$2,952.83
County Ed	$0.4889	73.34		73.34	$183.34
Com College	$0.0000	0.00		0.00	$0.00
City	$15.0700	2,260.50		2,260.50	$5,651.25
County	$4.4100	661.50		661.50	$1,653.75
Total Primary	$27.8431	4,176.47	$2,263.07		
			$2,676.47	1,500.00	$10,441.16
Secondary Rates:					
H-W Unified	$16.0355	2,405.33		2,405.33	$6,013.31
Com College	$0.5823	87.35		87.35	$218.36
City	$0.0000	0.00		0.00	$0.00
County	$0.0000	0.00		0.00	$0.00
Library	$0.2000	30.00		30.00	$75.00
FDAT	$0.1000	15.00		15.00	$37.50
Total Secondary	$16.9178	2,537.67		2,537.67	$6,344.18
TOTAL TAXES	$44.7609	6,714.14		4,037.67	$16,785.34
				2.7% of value	11.2% of value

Kingman/Kingman Unified/Mohave County					
Taxing Jurisdiction	Tax Rates	$150,000 Home	Additional State Aid	$150,000 adjusted for add'l aid	$150,000 Commercial
Primary Rates:					
Kingman Unified	$4.0508	607.62	$212.67	394.95	$1,519.05
County Ed	$0.4889	73.34		73.34	$183.34
Com College	$0.9398	140.97		140.97	$352.43
City	$0.0000	0.00		0.00	$0.00
County	$1.7500	262.50		262.50	$656.25
Total Primary	$7.2295	1,084.43		871.76	$2,711.06
Secondary Rates:					
Kingman Unified	$0.8684	130.26		130.26	$325.65
Com College	$0.0000	0.00		0.00	$0.00
City	$0.3183	47.75		47.75	$119.36
County	$0.0000	0.00		0.00	$0.00
Flood Control	$0.5000	75.00		75.00	$187.50
T.V.	$0.0867	13.01		13.01	$32.51
Library	$0.3236	48.54		48.54	$121.35
FDAT	$0.1000	15.00		15.00	$37.50
Total Secondary	$2.1970	329.55		329.55	$823.88
TOTAL TAXES				1,201.31	$3,534.94
				.8% of value	2.4% of value

Prescott/Prescott Unified/Yavapai County					
Taxing Jurisdiction	Tax Rates	$150,000 Home	Additional State Aid	$150,000 adjusted for add'l aid	$150,000 Commercial
Primary Rates:					
Prescott Unified	$3.6222	543.33	$190.17	353.16	$1,358.33
County Ed	$0.4889	73.34		73.34	$183.34
Com College	$1.5835	237.53		237.53	$593.81
City	$0.2522	37.83		37.83	$94.58
County	$1.6072	241.08		241.08	$602.70
Total Primary	$7.5540	1,133.10		942.93	$2,832.75
Secondary Rates:					
Prescott Unified	$0.3583	53.75		53.75	$134.36
Com College	$0.3954	59.31		59.31	$148.28
City	$0.4707	70.61		70.61	$176.51
County	$0.0000	0.00		0.00	$0.00
Flood Control	$0.2179	32.69		32.69	$81.71
Library	$0.1117	16.76		16.76	$41.89
FDAT	$0.1001	15.02		15.02	$37.54
Total Secondary	$1.6541	248.12		248.12	$485.93
TOTAL TAXES	$9.2081			1,191.05	$3,318.68
				.8% of value	2.2% of value

Yuma/Yuma Elem/Yuma Union/Yuma County					
Taxing Jurisdiction	Tax Rates	$150,000 Home	Additional State Aid	$150,000 adjusted for add'l aid	$150,000 Commercial
Primary Rates:					
Yuma Elementary	$2.5956	389.34	$136.27	253.0710	$973.35
Yuma Union	$2.7563	413.45		413.45	$1,033.61
County Ed	$0.4889	73.34		73.34	$183.34
Com College	$1.8267	274.01		274.01	$685.01
City	$1.8621	279.32		279.32	$698.29
County	$2.3180	347.70		347.70	$869.25
Total Primary	$11.8476	1,777.14		1,640.87	$4,442.85
Secondary Rates:					
Yuma Elementary	$1.4277	214.16		214.16	$535.39
Yuma Union	$0.7880	118.20		118.20	$295.50
Com College	$0.2550	38.25		38.25	$95.63
City	$0.0000	0.00		0.00	$0.00
County	$0.0000	0.00		0.00	$0.00
Flood Control	$0.3500	52.50		52.50	$131.25
Library	$0.5040	75.60		75.60	$189.00
Total Secondary	$3.3247	498.71		498.71	$1,246.76
TOTAL TAXES	$15.1723	2,275.85		2,139.58	5,689.61
				1.4% of value	3.8% of value

Comparing Arizona's Effective Property Tax Rate...

Real and Personal Property Taxes on Large Commercial Properties
(Taxes and Effective Tax Rates on $30 Million Property)

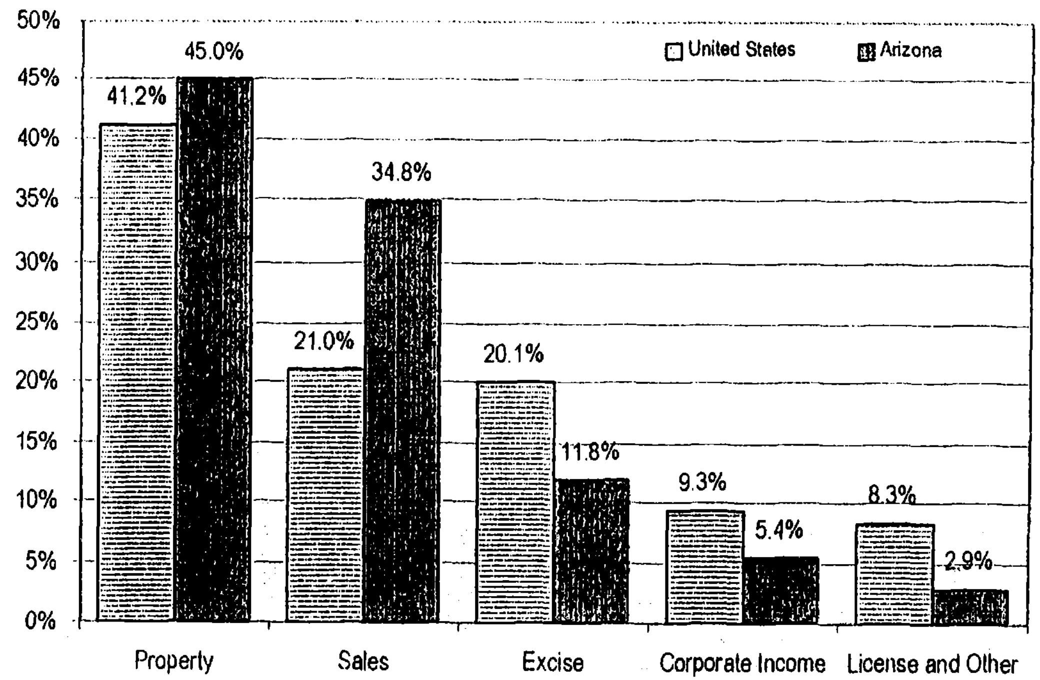
State	Total Net Tax	Total ETR	State	Total Net Tax	Total ETR
1. Illinois	$1,687,863	5.63%	26. Indiana	612,981	2.04%
2. Connecticut	1,232,400	4.11%	27. Nebraska	599,811	2.00%
3. Michigan	1,177,585	3.93%	28. South Dakota	597,562	1.99%
4. Arizona	*1,077,349*	*3.59%*	29. New Hampshire	584,220	1.95%
5. New York	1,048,884	3.50%	30. North Dakota	531,814	1.77%
6. Rhode Island	1,018,562	3.40%	31. Colorado	511,082	1.70%
7. Iowa	956,169	3.19%	32. Georgia	495,399	1.65%
8. Minnesota	877,107	2.92%	33. Ohio	494,252	1.65%
9. Massachusetts	856,823	2.86%	34. Alaska	493,638	1.65%
10. Maryland	843,900	2.81%	35. Idaho	466,410	1.56%
11. Texas	843,211	2.81%	36. Virginia	461,025	1.54%
12. Missouri	829,454	2.77%	37. West Virginia	455,528	1.52%
13. Tennessee	807,346	2.69%	38. Montana	425,607	1.42%
14. Wisconsin	806,700	2.69%	39. Utah	420,118	1.40%
15. Kansas	793,567	2.65%	40. New Mexico	417,867	1.39%
16. Florida	772,445	2.58%	41. Alabama	416,580	1.39%
17. Mississippi	760,686	2.54%	42. Arkansas	380,708	1.27%
18. New Jersey	737,896	2.46%	43. California	375,000	1.25%
19. Vermont	706,205	2.35%	44. Oklahoma	372,289	1.24%
20. South Carolina	702,612	2.34%	45. North Carolina	362,871	1.21%
21. Maine	700,870	2.34%	46. Nevada	333,588	1.11%
22. Louisiana	684,263	2.28%	47. Washington	294,323	0.98%
AVERAGE	*646,146*	*2.15%*	48. Delaware	290,554	0.97%
23. Pennsylvania	642,237	2.14%	49. Kentucky	280,688	0.94%
24. Oregon	636,300	2.12%	50. Hawaii	231,713	0.77%
25. District of Columbia	630,800	2.10%	51. Wyoming	216,600	0.72%

Source: Minnesota Taxpayers Association, *50-State Property Tax Comparison Study: Payable Year 2002.*

Estimated State and Local Business Taxes, FY2002

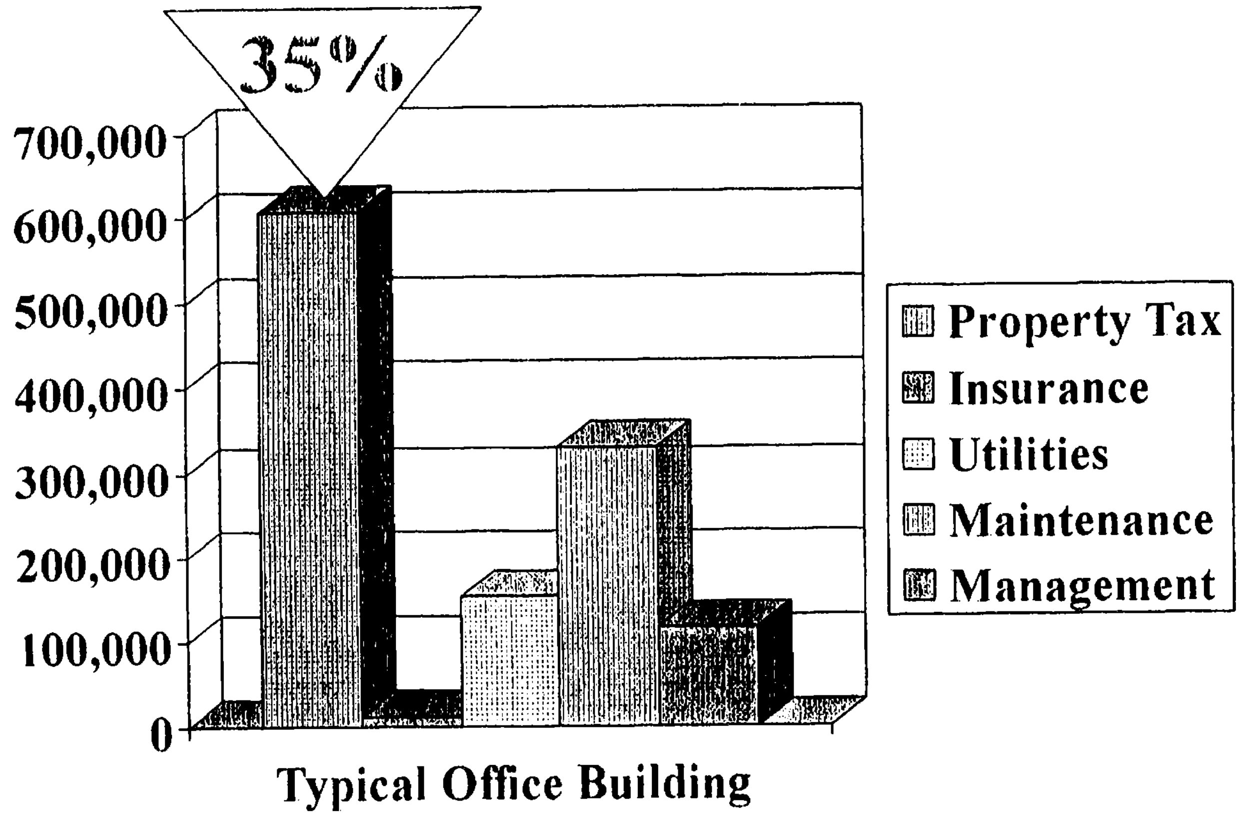
Arizona Tax	2002 Business Taxes
Property	$2,761,745
Total General Sales	2,135,446
Motor Fuels Sales	395,009
Corporation Net Income	329,659
Insurance Premiums	199,516
Public Utilities	131,069
Motor Vehicle License	96,399
Occupation and Business License	62,435
Other License	8,617
Corporation License	8,450
Alcoholic Beverage License	3,921
Amusement License	24
Other Taxes and License	21,012
Business Taxes	**$6,132,290**
Total State and Local Taxes	**13,722,644**
Business Share	**44.7%**

Figure 1
Composition of Business Tax Liabilities, Arizona vs. U.S.



Arizona's Business Property Taxes. Ernst & Young LLP. July 2003.

Typical AZ Office Operating Expenses...



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Typical AZ Industrial Operating Expenses...

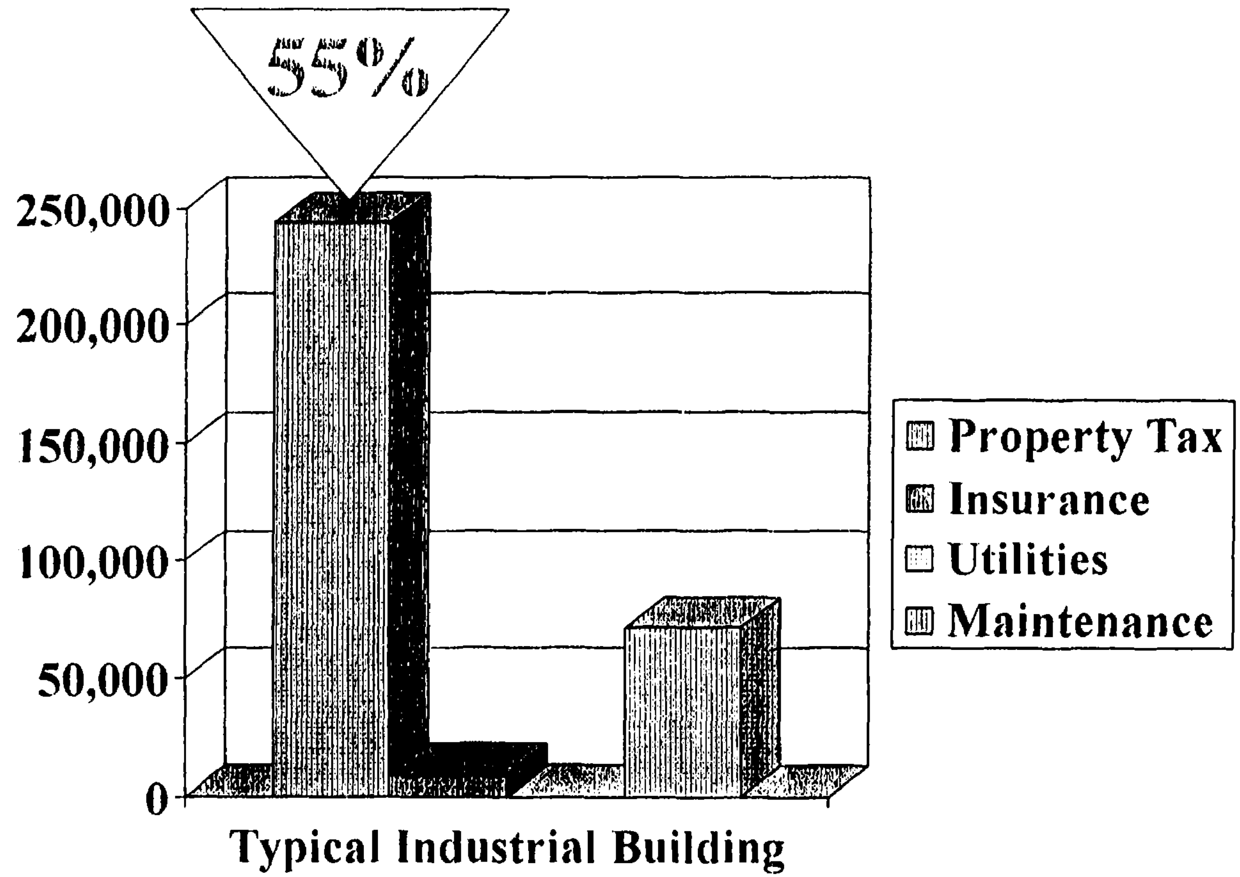


FIGURE 1
REDUCE COMMERCIAL/INDUSTRIAL ASSESSMENT RATIO

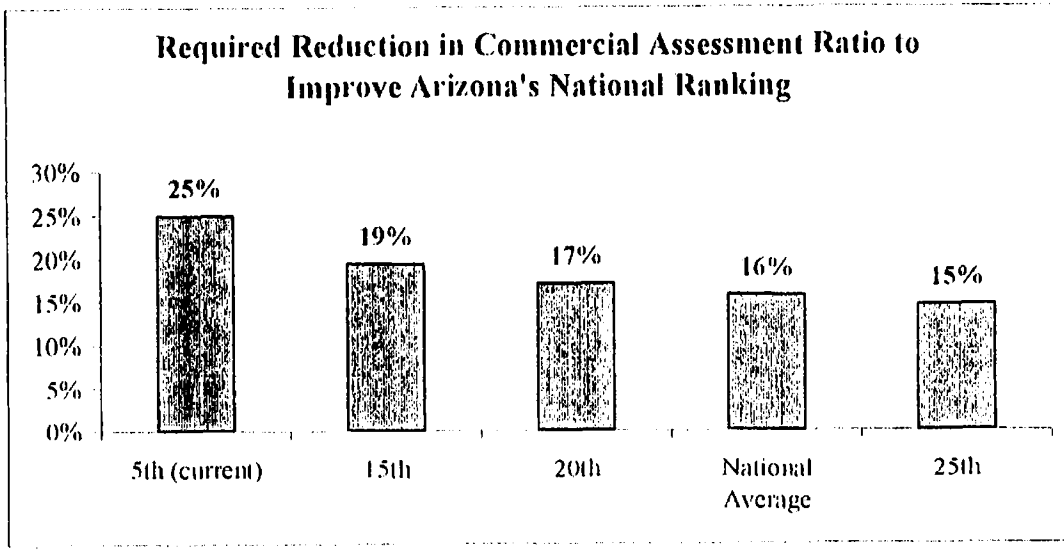
Current Effective Tax Rates:

Commercial/Industrial (25% Assessment Ratio)	3.41%
Residential (10% Assessment Ratio)	1.25%

Arizona's Current National Rank (50 = best)*: 5th

Reduced Assessment Ratio Required to Improve Arizona's Rank

Rank	Assessment Ratio	Effective Tax Rate
5th (current)	25%	3.41%
15th	19%	2.65%
20th	17%	2.34%
National Average	16%	2.14%
25th	15%	1.99%



Property Tax Burden Analysis, Part I. Applied Economics. July 2003.

*Based on average effective tax rate for commercial property valued at $1 million in largest urban areas from "50-State Property Tax Comparison Study," Minnesota Center for Public Finance Research, May 2003.

ARIZONA LEGISLATIVE COUNCIL

MEMO

July 1, 2003

TO: Members
Tax Reform for Arizona Citizens Committee

FROM: Kenneth C. Behringer
General Counsel

RE: Railroad, Private Car and Flight Properties (R-46-44)

QUESTION

Is the special treatment of railroad, private car and flight properties for property tax purposes, as prescribed in Arizona Revised Statutes (A.R.S.) section 42-15007, required by federal law?

ANSWER

Yes, this treatment is required by federal law.

A state may not discriminate against rail transportation property in assessing property taxes. These properties include private cars. 49 U.S.C. § 11501(a). This discrimination includes assessing rail transportation property at a higher assessment ratio than that applied to other commercial and industrial property. 49 U.S.C. § 11501(b).

In 1982, Congress enacted several limitations on state taxation concerning air commerce. Included in this act was a prohibition nearly identical to that for rail transportation against discrimination in the property taxation of air carrier transportation. 49 U.S.C. § 40116(d).

Compliance with these prohibitions is implemented through A.R.S. section 42-15007. This section prescribes that the assessment ratio for railroad, private car and flight properties is the weighted average of the assessment ratios for all mine, utility, commercial and industrial properties and all personal property used for agricultural purposes or by certain nonprofit organizations.

Any changes to the assessment of railroad, private car or flight properties would have to be consistent with the limitations prescribed by federal law.

Full Cash Value (Secondary)
Limited Value (Primary)

Arizona has a unique property tax system because it is the only state with two sets of values and two sets of property taxes. The dual values and taxes have been in place since 1980. The values are determined prior to the application of assessment ratios.

Secondary or "Full Cash" Value: Secondary values are synonymous with the full cash value (FCV) of property, or market value. There is no limit on the amount of growth, since it is based on the current value the market will bear. Some properties have a statutory valuation formula that is used to determine their FCV. The FCV or secondary value is used for secondary property taxes.

Primary or "Limited" Property Value: The primary value, used for primary property taxes, cannot exceed the full cash value. Limited property values are determined by using one of the following methods:

- For parcels in existence in the previous year that did not undergo any modifications for any reason, the limited value may not increase by more than 10 per cent, or 25 per cent of the difference between the past year's primary value and the new secondary value, whichever is greater.

- For parcels that were modified because of construction, destruction, change in use or new parcels resulting from a spit or combination, the limited value is established by applying a ratio of full cash to limited property values of existing properties of the same use or classification.

Consolidation of values:
The concept for having two sets of values was established in response to the high inflationary times of the 1970's and the national movement to limit property taxes. The limited value insulates taxpayers from drastic increases in value that is then applied to the tax rates for general government. The unlimited values, or full cash values, are used for voter-approved taxes.

If the Legislature were to eliminate the limited value, then Arizona would be similar to other states in which the full cash value is used for all property taxation purposes. This would simplify the property tax system for both administrators and the taxpayers. In tax year 2002, the total statewide limited value was 94.7% of the full cash value.

The effect would be an increase in valuation for primary tax purposes. Theoretically, tax rates would be adjusted down to raise the same amount of revenue. However, this impact would vary by taxing jurisdiction.

October 2003
House Majority Research Staff

ARIZONA DEPARTMENT OF REVENUE
2002
ABSTRACT BY COUNTY FOR THE STATE OF ARIZONA

TAX AUTHORITY	PARCEL COUNT	TOTAL VALUE	TOTAL ASSESSED VALUE	EXEMPT AMOUNT	NET ASSESSED VALUE
		LIMITED PROPERTY VALUE (PRIMARY)			
TOTALS	**2,538,244**	**277,501,955,967**	**38,964,150,164**	**4,107,604,109**	**34,856,546,055**
APACHE	49,861	1,814,982,470	358,100,453	82,231,971	275,868,482
COCHISE	111,667	3,976,031,059	571,233,044	33,492,435	537,740,609
COCONINO	66,437	7,597,237,728	1,134,904,881	86,401,142	1,048,503,739
GILA	37,368	2,721,627,688	359,147,863	27,521,675	331,626,188
GRAHAM	14,496	760,478,436	105,032,017	8,062,662	96,969,355
GREENLEE	5,530	891,302,484	184,645,902	4,289,502	180,356,400
MARICOPA	1,214,539	180,904,151,657	25,458,209,944	2,502,345,062	22,955,864,882
MOHAVE	234,191	8,504,255,855	1,175,881,465	128,353,814	1,047,527,651
NAVAJO	76,153	5,049,758,994	768,715,043	205,546,437	563,168,606
PIMA	343,524	39,872,513,521	5,350,930,643	683,565,846	4,667,364,797
PINAL	122,014	6,502,308,541	890,485,510	73,583,380	816,902,130
SANTA CRUZ	40,486	1,701,682,209	251,899,426	23,836,366	228,063,060
YAVAPAI	136,560	11,043,648,857	1,454,085,413	64,512,815	1,389,572,598
YUMA	67,233	4,862,103,982	694,988,347	98,483,034	596,505,313
LA PAZ	18,185	1,299,872,486	205,890,212	85,377,968	120,512,244

ARIZONA DEPARTMENT OF REVENUE
2002
ABSTRACT BY COUNTY FOR THE STATE OF ARIZONA

TAX AUTHORITY	PARCEL COUNT	TOTAL VALUE	TOTAL ASSESSED VALUE	EXEMPT AMOUNT	NET ASSESSED VALUE
		FULL CASH VALUE (SECONDARY)			
TOTALS	**2,538,244**	**294,570,850,907**	**41,704,891,060**	**4,893,901,830**	**36,810,989,230**
APACHE	49,861	1,881,792,774	367,089,002	83,794,929	283,294,073
COCHISE	111,667	4,109,642,113	591,848,033	37,627,178	554,220,855
COCONINO	66,437	7,860,165,430	1,173,560,562	88,681,743	1,084,878,819
GILA	37,368	2,926,766,725	385,852,577	28,691,231	357,161,346
GRAHAM	14,496	780,675,729	108,051,232	8,436,568	99,614,664
GREENLEE	5,530	895,038,694	185,072,125	4,301,683	180,770,442
MARICOPA	1,214,539	194,235,322,146	27,665,309,021	3,208,261,739	24,457,047,282
MOHAVE	234,191	8,970,945,148	1,238,281,334	163,316,236	1,074,965,098
NAVAJO	76,153	5,282,750,488	799,970,459	207,365,975	592,604,484
PIMA	343,524	41,095,365,469	5,537,775,629	700,691,581	4,837,084,048
PINAL	122,014	6,916,354,005	947,898,517	84,033,356	863,865,161
SANTA CRUZ	40,486	1,755,655,889	259,341,989	24,286,419	235,055,570
YAVAPAI	136,560	11,528,423,702	1,520,358,683	68,156,131	1,452,202,552
YUMA	67,233	5,017,610,685	716,632,240	100,712,011	615,920,229
LA PAZ	18,185	1,314,341,910	207,849,657	85,545,050	122,304,607

ARIZONA DEPARTMENT OF REVENUE
2002
ABSTRACT BY LEGAL CLASS FOR THE STATE OF ARIZONA

TAX AUTHORITY	LEGAL CLASS	PARCEL COUNT	TOTAL VALUE	TOTAL ASSESSED VALUE	EXEMPT AMOUNT	NET ASSESSED VALUE
STATE OF ARIZONA		**2,538,244**	**277,501,955,967**	**38,964,150,164**	**4,107,604,109**	**34,856,546,055**
(LIMITED PROPERTY VALUE)	CVP 01	6,105	1,823,174,009	454,794,503	98,789,930	356,004,573
	01.P		16,772,027,532	4,194,007,393	586,758,406	3,607,248,987
	02.R	20	188,816	30,211		30,211
	05	722	514,898,599	103,380,239		103,380,239
	06		42,473,392	2,123,670		2,123,670
	LAP 01	77,037	34,697,065,227	8,674,271,514	93,189,271	8,581,082,244
	01.P		8,458,520,166	2,114,632,550	304,370,523	1,810,262,027
	02.R	831,485	33,141,192,574	5,302,507,259	2,907,991,623	2,394,515,636
	02.P		242,345,667	38,775,324	6,349,923	32,425,401
	03	1,446,068	155,889,445,438	15,597,875,762	86,070,127	15,511,805,635
	04	200,963	23,654,089,828	2,365,931,154	23,798,824	2,342,132,330
	06	3,416	2,237,754,760 0	111,905,296 0	208,333 0	111,696,963
	07.B	52	12,270,496 0	3,058,858 0	68,084 0	2,990,774
	07.H	24	6,833,873 0	68,337 0	0	68,337
	08.B	28	7,684,429	768,181		768,181
	08.H	1	8,977	90		90
	09	5	1,982,184 0	19,823 0	9,065 0	10,758

ARIZONA DEPARTMENT OF REVENUE
2002
ABSTRACT BY LEGAL CLASS FOR THE STATE OF ARIZONA

TAX AUTHORITY	LEGAL CLASS	PARCEL COUNT	TOTAL VALUE	TOTAL ASSESSED VALUE	EXEMPT AMOUNT	NET ASSESSED VALUE
STATE OF ARIZONA		**2,538,244**	**294,570,850,907**	**41,704,891,060**	**4,893,901,830**	**36,810,989,230**
(FULL CASH VALUE)	CVP 01	6,105	1,823,174,009	454,794,503	98,789,930	356,004,573
	01.P		16,772,027,532	4,194,007,393	586,758,406	3,607,248,987
	02.R	20	213,931	34,228		34,228
	05	722	540,664,578	108,550,958		108,550,958
	06		44,000,000	2,200,000		2,200,000
	LAP 01	77,037	38,008,273,593	9,502,073,501	128,025,967	9,374,047,534
	01.P		8,472,401,972	2,118,103,001	304,406,915	1,813,696,086
	02.R	831,485	42,244,903,820	6,759,064,752	3,635,867,921	3,123,196,831
	02.P		250,857,457	40,137,209	6,387,322	33,749,887
	03	1,446,068	159,226,548,609	15,931,634,429	106,225,281	15,825,409,148
	04	200,963	24,624,869,052	2,463,042,104	27,134,885	2,435,907,219
	06	3,416	2,531,718,033 0	127,003,763 0	213,306 0	126,790,457
	07.B	52	13,431,848 0	3,348,073 0	82,802 0	3,265,271
	07.H	24	7,397,163 0	73,970 0	0	73,970
	08.B	28	7,997,157	799,455		799,455
	08.H	1	11,496	115		115
	09	5	2,360,657 0	23,606 0	9,095 0	14,511

STATE SUMMARY BY LEGAL CLASS

Property Tax Levy Limits
Expenditure Limits

On June 3, 1980, voters approved several constitutional limits regarding property taxes and expenditures for various levels of government. This was the result of a national property tax limitation movement due to the high inflationary times of the 1970's that led to rapidly increasing property values.

Property Tax Levy Limitation:

Proposition 107 established a 2% levy limit on counties, cities, towns and community college districts beginning with tax year 1982. Article IX, Section 19 was added to the state constitution. The levy limit allowed a growth of levies equal to 2% growth per year plus new value. The limit was designed to limit the growth in property tax levies. It does not limit individual property tax bills, limit property tax collections or equalize tax rates between jurisdictions.

The limit does not apply to special district taxes, school district taxes or other voter-approved long-term debt.

Expenditure Limitation:

Proposition 108 established expenditure limits for counties, cities and towns. Article IX, Section 20 was added to the state constitution. The expenditure limit requires the Economic Estimates Commission to determine the limit prior to April 1 for the following fiscal year. The limit is determined by adjusting the 1979-80 base to reflect changes in population and inflation. The limit was designed to limit increases in spending to population and inflation. The limit can be overridden for disasters, for voter-approved specific amounts or for a voter-approved alternative expenditure limit for four years.

In 1986, SCR 1017 proposed an amendment to this section. The proposed amendment (Proposition 102) was rejected by the voters at the November 4, 1986 general election. The amendment would have allowed these jurisdictions to seek a voter-approved "permanent adjustment" in their expenditure limit at a general election as well as at elections where governing board members were nominated or elected.

Prepared by: KD/House Majority Research Staff
October 2003

19. Limitation on ad valorem tax levied; exceptions

Section 19. (1) The maximum amount of ad valorem taxes levied by any county, city, town or community college district shall not exceed an amount two per cent greater than the amount levied in the preceding year.

(2) The limitation prescribed by subsection (1) does not apply to:

(a) Ad valorem taxes or special assessments levied to pay the principal of and the interest and redemption charges on bonded indebtedness or other lawful long-term obligations issued or incurred for a specific purpose.

(b) Ad valorem taxes or assessments levied by or for property improvement assessment districts, improvement districts and other special purpose districts other than counties, cities, towns and community college districts.

(c) Ad valorem taxes levied by counties for support of common, high and unified school districts.

(3) This section applies to all tax years beginning after December 31, 1981.

(4) The limitation prescribed by subsection (1) shall be increased each year to the maximum permissible limit, whether or not the political subdivision actually levies ad valorem taxes to such amounts.

(5) The voters, in the manner prescribed by law, may elect to allow ad valorem taxation in excess of the limitation prescribed by this section.

(6) The limitation prescribed by subsection (1) of this section shall be increased by the amount of ad valorem taxes levied against property not subject to taxation in the prior year and shall be decreased by the amount of ad valorem taxes levied against property subject to taxation in the prior year and not subject to taxation in the current year. Such amounts of ad valorem taxes shall be computed using the rate applied to property not subject to this subsection.

(7) The legislature shall provide by law for the implementation of this section.

20. Expenditure limitation; adjustments; reporting

Section 20. (1) The economic estimates commission shall determine and publish prior to April 1 of each year the expenditure limitation for the following fiscal year for each county, city and town. The expenditure limitations shall be determined by adjusting the amount of actual payments of local revenues for each such political subdivision for fiscal year 1979-1980 to reflect the changes in the population of each political subdivision and the cost of living. The governing board of any political subdivision shall not authorize expenditures of local revenues in excess of the limitation prescribed in this section, except as provided in subsections (2), (6) and (9) of this section.

(2) Expenditures in excess of the limitations determined pursuant to subsection (1) of this section may be authorized as follows:

(a) Upon affirmative vote of two-thirds of the members of the governing board for expenditures directly necessitated by a natural or man-made disaster declared by the governor. Any expenditures in excess of the expenditure limitation, as authorized by this paragraph, shall not affect the determination of the expenditure limitation pursuant to subsection (1) of this section in any subsequent years. Any expenditures authorized pursuant to this paragraph shall be made either in the fiscal year in which the disaster is declared or in the succeeding fiscal year.

(b) Upon the affirmative vote of seventy per cent of the members of the governing board for expenditures directly necessitated by a natural or man-made disaster not declared by the governor, subject to the following:

(i) The governing board reducing expenditures below the expenditure limitation determined pursuant to subsection (1) of this section by the amount of the excess expenditure for the fiscal year following a fiscal year in which excess expenditures were made pursuant to this paragraph; or

(ii) Approval of the excess expenditure by a majority of the qualified electors voting either at a special election held by the governing board or at a regularly scheduled election for the nomination or election of the members of the governing board, in the manner provided by law. If the excess expenditure is not approved by a majority of the qualified electors voting, the governing board shall for the fiscal year which immediately follows the fiscal year in which the excess expenditures are made, reduce expenditures below the expenditure limitation determined pursuant to subsection (1) of this section by the amount of the excess expenditures. Any expenditures in excess of the expenditure limitation, as authorized by this paragraph, shall not affect the determination of the expenditure limitation pursuant to subsection (1) of this section in any subsequent years. Any expenditures pursuant to this paragraph shall be made either in the fiscal year in which the disaster occurs or in the succeeding fiscal year.

(c) Upon affirmative vote of at least two-thirds of the members of the governing board and approval by a majority of the qualified electors voting either at a special election held by the governing board in a manner prescribed by law, or at a regularly scheduled election for the nomination or election of the members of the governing board. Such approval by a majority of the qualified electors voting shall be for a specific amount in excess of the expenditure limitation, and such approval must occur prior to the fiscal year in which the expenditure limitation is to be exceeded. Any expenditures in excess of the expenditure limitation, as authorized by this subdivision, shall not affect the determination of the expenditure limitation pursuant to subsection (1) of this section, in subsequent years.

(3) As used in this section:

(a) "Base limit" means the amount of actual payments of local revenues for fiscal year 1979-1980 as used to determine the expenditure limitation pursuant to subsection (1) of this section.

(b) "Cost of living" means either:

(i) The price of goods and services as measured by the implicit price deflator for the gross national product or its successor as reported by the United States department of commerce or its successor agency.

(ii) A different measure or index of the cost of living adopted at the direction of the legislature, by concurrent resolution, upon affirmative vote of two-thirds of the membership of each house of the legislature. Such measure or index shall apply for subsequent fiscal years, except it shall not apply for the fiscal year following the adoption of such measure or index if the measure or index is adopted after March 1 of the preceding fiscal year.

(c) "Expenditure" means any authorization for the payment of local revenues.

(d) "Local revenues" includes all monies, revenues, funds, fees, fines, penalties, tuitions, property and receipts of any kind whatsoever received by or for the account of a political subdivision or any of its agencies, departments, offices, boards, commissions, authorities, councils and institutions, except:

(i) Any amounts or property received from the issuance or incurrence of bonds or other lawful long-term obligations issued or incurred for a specific purpose, or collected or segregated to make payments or deposits required by a contract concerning such bonds or obligations. For the purpose of this subdivision long-term obligations shall not include warrants issued in the ordinary course of operation or registered for payment, by a political subdivision.

(ii) Any amounts or property received as payment of dividends or interest, or any gain on the sale or redemption of investment securities, the purchase of which is authorized by law.

(iii) Any amounts or property received by a political subdivision in the capacity of trustee, custodian or agent.

(iv) Any amounts received as grants and aid of any type received from the federal government or any of its agencies.

(v) Any amounts received as grants, aid, contributions or gifts of any type except amounts received directly or indirectly in lieu of taxes received directly or indirectly from any private agency or organization or any individual.

(vi) Any amounts received from the state which are included within the appropriation limitation prescribed in section 17 of this article.

(vii) Any amounts received pursuant to a transfer during a fiscal year from another agency, department, office, board, commission, authority, council or institution of the same political subdivision which were included as local revenues for such fiscal year or which are excluded from local revenue under other provisions of this section.

(viii) Any amounts or property accumulated for the purpose of purchasing land, buildings or improvements or constructing buildings or improvements, if such accumulation and purpose have been approved by the voters of the political subdivision.

(ix) Any amounts received pursuant to section 14 of this article which are greater than the amount received in fiscal year 1979-1980.

(x) Any amounts received in return for goods or services pursuant to a contract with another political subdivision, school district, community college district or the state, and expended by the other political subdivision, school district, community college district or the state pursuant to the expenditure limitation in effect when the amounts are expended by the other political subdivision, school district, community college district or the state.

(xi) Any amounts expended for the construction, reconstruction, operation or maintenance of a hospital financially supported by a city or town prior to January 1, 1980.

(xii) Any amounts or property collected to pay the principal of and interest on any warrants issued by a political subdivision and outstanding as of July 1, 1979.

(xiii) Any amounts received during a fiscal year as refunds, reimbursements or other recoveries of amounts expended which were applied against the expenditure limitation for such fiscal year or which were excluded from local revenues under other provisions of this subsection.

(xiv) Any amounts received collected by the counties for distribution to school districts pursuant to state law.

(e) "Political subdivision" means any county, city or town. This definition applies only to this section and does not otherwise modify the commonly accepted definition of political subdivision.

(f) "Population" means either:

(i) The periodic census conducted by the United States department of commerce or its successor agency, or the annual update of such census by the department of economic security or its successor agency.

(ii) A different measure or index of population adopted at the direction of the legislature, by concurrent resolution, upon affirmative vote of two-thirds of the membership of each house of the legislature. Such measure or index shall apply for subsequent fiscal years, except it shall not apply for the fiscal year following the adoption of such measure or index if the measure or index is adopted after March 1 of the preceding fiscal year.

(4) The economic estimates commission shall adjust the base limit to reflect subsequent transfers of all or any part of the cost of providing a governmental function, in a manner prescribed by law. The adjustment provided for in this subsection shall be used in determining the expenditure limitation pursuant to subsection (1) of this section beginning with the fiscal year immediately following the transfer.

(5) The economic estimates commission shall adjust the base limit to reflect any subsequent annexation, creation of a new political subdivision, consolidation or change in the boundaries of a political subdivision, in a manner prescribed by law. The adjustment provided for in this subsection shall be used in determining the expenditure limitation pursuant to subsection (1) of this section beginning with the fiscal year immediately following the annexation, creation of a new political subdivision, consolidation or change in the boundaries of a political subdivision.

(6) Any political subdivision may adjust the base limit by the affirmative vote of two-thirds of the members of the governing board or by initiative, in the manner provided by law, and in either instance by approval of the proposed adjustment by a majority of the qualified electors voting at a regularly scheduled general election or at a nonpartisan election held for the nomination or election of the members of the governing board. The impact of the modification of the expenditure limitation shall appear on the ballot and in publicity pamphlets, as provided by law. Any adjustment, pursuant to this subsection, of the base limit shall be used in determining the expenditure limitation pursuant to subsection (1) of this section beginning with the fiscal year immediately following the approval, as provided by law.

(7) The legislature shall provide for expenditure limitations for such special districts as it deems necessary.

(8) The legislature shall establish by law a uniform reporting system for all political subdivisions or special districts subject to an expenditure limitation pursuant to this section to insure compliance with this section. The legislature shall establish by law sanctions and penalties for failure to comply with this section.

(9) Subsection (1) of this section does not apply to a city or town which at a regularly scheduled election for the nomination or election of members of the governing board of the city or town adopts an expenditure limitation pursuant to this subsection different from the expenditure limitation prescribed by subsection (1) of this section. The governing board of a city or town may by a two-thirds vote provide for referral of an alternative expenditure limitation or the qualified electors may by initiative, in the manner provided by law, propose an alternative expenditure limitation. In a manner provided by law, the impact of the alternative expenditure limitation shall be compared to the impact of the expenditure limitation prescribed by subsection (1) of this section, and the comparison shall appear on the ballot and in publicity pamphlets. If a majority of the qualified electors voting on such issue vote in favor of the alternative expenditure limitation, such limitation shall apply to the city or town. If more than one alternative expenditure limitation is on the ballot and more than one alternative expenditure limitation is approved by the voters, the alternative expenditure limitation receiving the highest number of votes shall apply to such city or town. If an alternative expenditure limitation is adopted, it shall apply for the four succeeding fiscal years. Following the fourth succeeding fiscal year, the expenditure limitation prescribed by subsection (1) of this section shall become the expenditure limitation for the city or town unless an alternative expenditure limitation is approved as provided in this subsection. If a majority of the qualified electors voting on such issue vote against an alternative expenditure limitation, the expenditure limitation prescribed pursuant to subsection (1) of this section shall apply to the city or town, and no new alternative expenditure limitation may be submitted to the voters for a period of at least two years. If an alternative expenditure limitation is adopted pursuant to this subsection, the city or town may not conduct an override election provided for in section 19, subsection (4) of this article, during the time period in which the alternative expenditure limitation is in effect.

(10) This section does not apply to any political subdivision until the fiscal year immediately following the first regularly scheduled election after July 1, 1980 for the nomination or election of the members of the governing board of such political subdivision, except that a political subdivision, prior to the fiscal year during which the spending limitation would first become effective, may modify the expenditure limitation prescribed pursuant to subsection (1) of this section, by the provisions prescribed by subsections (2) and (6) of this section, or may adopt an alternative expenditure limitation pursuant to subsection (9) of this section.

A county may conduct a special election to exceed the expenditure limitation prescribed pursuant to subsection (1) of this section for the fiscal years 1982-1983 and 1983-1984, on the first Tuesday after the first Monday in November in 1981.

(11) "City", as used in this article, means city or charter city.

County Levy Limits - 2003

County	2002 levy limit	2003 levy limit	2003 actual levy	over/under	tax rate
Apache	$1,242,236	$1,295,610	$1,106,418	($189,192)	$0.3696
Cochise	$22,077,872	$23,671,986	$16,754,694	($6,917,292)	$2.9373
Coconino	$5,349,451	$5,662,626	$5,307,525	($355,101)	$0.4753
Gila	$20,469,627	$21,589,342	$15,298,550	($6,290,792)	$4.4100
Graham	$3,128,718	$3,286,581	$2,276,045	($1,010,536)	$2.2629
Greenlee	$1,039,574	$1,208,203	$1,208,203	$0	$0.8492
La Paz	$4,186,594	$4,325,816	$2,795,660	($1,530,156)	$2.2500
Maricopa	$296,291,348	$320,821,058	$308,122,580	($12,698,478)	$1.2108
Mohave	$20,467,592	$22,914,901	$20,296,378	($2,618,523)	$1.7379
Navajo	$3,515,298	$3,842,125	$2,976,547	($865,578)	$0.4772
Pima	$233,382,157	$247,260,787	$204,515,149	($42,745,638)	$4.0651
Pinal	$65,334,004	$76,163,085	$42,386,646	($33,776,439)	$4.4532
Santa Cruz	$7,805,688	$8,212,733	$8,039,398	($173,335)	$3.3487
Yavapai	$29,880,283	$32,315,582	$25,495,163	($6,820,419)	$1.6808
Yuma	$14,620,814	$15,621,633	$14,648,440	($973,193)	$2.3180

Source: PTOC worksheets/DOR

County Levy Limits - 2003

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Source: PTOC worksheets/DOR

FISCAL YEAR 2002/03 FINAL EXPENDITURE LIMITS: COUNTIES

COUNTY	POPULATON** 2001	POPULATON** 1978	POPULATION FACTOR	INFLATION FACTOR*	1979/80 BASE LIMIT	FY 2002/03 EXPENDITURE LIMITATION
APACHE	69,880	49,800	1.4032	2.2673	$3,890,847	**$12,378,535**
COCHISE	127,876	80,200	1.5945	2.2673	$13,340,485	**$48,226,730**
COCONINO	122,770	70,000	1.7539	2.2673	$10,268,127	**$40,830,714**
GILA	52,420	35,200	1.4892	2.2673	$9,205,084	**$31,080,187.82**
GRAHAM	34,065	20,800	1.6377	2.2673	$2,944,049	**$10,931,798**
GREENLEE	8,590	11,300	0.7602	2.2673	$2,785,635	**$4,801,097**
LA PAZ	19,935	10,905	1.8281	2.2673	$2,242,748	**$9,295,496**
MARICOPA	3,192,125	1,435,000	2.2245	2.2673	$156,635,737	**$789,987,771**
MOHAVE	161,580	49,700	3.2511	2.2673	$15,297,556	**$112,759,929**
NAVAJO	99,780	65,600	1.5210	2.2673	$7,686,035	**$26,505,960**
PIMA	870,610	502,200	1.7336	2.2673	$93,755,872	**$368,508,021**
PINAL	186,795	86,800	2.1520	2.2673	$17,905,497	**$87,364,185**
SANTA CRUZ	53,010	19,500	2.7185	2.2673	$2,306,973	**$14,218,940**
YAVAPAI	175,305	61,000	2.8739	2.2673	$11,175,381	**$72,816,254**
YUMA	173,715	68,095	2.5511	2.2673	$9,582,768	**$55,426,135**
TOTAL	**5,348,456**	**2,566,100**	**2.0843**		**$359,022,794**	**$1,685,131,753**

* INFLATION FACTOR = (2001 GDP Deflator)/(1978 GDP Deflator) BEA actuals, Feb. 2002 = 109.35/48.23
** FIGURES AS OF JULY 1 (SOURCE: DEPARTMENT OF ECONOMIC SECURITY). The population in Cochise, Santa Cruz and Yuma counites has been adjusted pursuant to A.R.S. 41-563.05.

ARIZONA LEGISLATIVE COUNCIL

MEMO

July 14, 2003

TO: Members
Tax Reform for Arizona Citizens Committee

FROM: Kenneth C. Behringer
General Counsel

RE: Property Tax Limitations in Other States (R-46-45)

Legislatures have attempted to limit the growth of property taxes using several methods that address different aspects of property taxation. These methods include limitations on the increase of property values, limitations on overall property tax rates, specific property tax rate limits, property tax levy limits and expenditure limitations. The methods used in the various states are summarized in the attached chart.

Valuation Growth Limits

Eighteen states place limits on the increase in assessed value of properties. Generally, these limits specify the maximum annual percentage increase in property values. Among the states, these increases range from two to ten percent. In several states, the increase is the lower of a set percentage and the consumer price index.

While most of these limits apply to specific properties, Iowa applies the limit statewide on classes of properties. Therefore, some individual property values may increase more than the limit as long as the total valuation of the class of properties does not increase more than the limit.

Most states exclude the value attributable to improvements and new construction from the limits. Also, some states allow a reassessment of the property at market value when the property is sold.

Property Tax Rate Limits

Overall Property Tax Rate Limits

Overall property tax rate limits prescribe maximum amounts of property tax that may be assessed against a property by all jurisdictions. Arizona has such a restriction for residential property. The amount of primary property taxes that may be assessed against a residential property cannot exceed one percent of its full cash value.

The overall property tax rate limits in the ten other states apply to more than one property tax classification. These limits range from one to five percent of the value of the property. Several states allow the voters to override the limits.

Specific Property Tax Rate Limits

The most common form of property tax limitation is the specific property tax rate limit. This method sets tax rate limits for specific types of local jurisdictions, such as counties, municipalities and school districts. The requirements of these limits vary widely across the states. Most states allow the voters to approve taxes in excess of these limits.

Levy limits

Levy limits restrict the total revenue that may be raised by a jurisdiction from property tax, independent of the property tax rate. These limits specify the maximum allowable increases in revenue. Arizona limits levies by counties, municipalities and community college districts from growing more than two percent of the amount levied in the preceding year.

The amount of growth allowed varies greatly among the states, from zero to fifteen percent. Colorado and Michigan use a shifting percentage that is determined by changes in inflation.

Fifteen states allow voters to override the levy limits for different lengths of time. Most states provide exemptions from the levy limits. These exemptions include new construction, improvements, annexations, amounts for emergency situations, expenditures mandated by state or federal law and offsets for the loss of non-property tax revenue.

Expenditure limits

While levy limits restrict what a jurisdiction may take in, expenditure limits restrict what a jurisdiction may spend. These limits are generally based on a set percentage increase over expenditures for the prior year. This base amount is adjusted by a number of factors, including inflation, growth in the property tax base or, for school districts, growth in the number of pupils.

Because expenditure limits are complex, they are least used method of limiting property tax liability. Eight states have expenditure limits.

LIMITATIONS ON FACTORS AFFECTING PROPERTY TAX

State	Assessment Increases	Rates		Levy Limits	Expenditure Limits
		Overall (%)	Specific		
Alabama	X	1 - 2	C, M, S		
Alaska			M	X	
Arizona	X	1		X	X
Arkansas	X		C, M	X	
California	X	1			X
Colorado			C, M, S	X	X
Connecticut					
Delaware				X	
Florida	X		C, M, S		
Georgia	X		S		
Hawaii					
Idaho			C, M, S	X	
Illinois	X		C, M, S	X	
Indiana				X	
Iowa	X		C, M, S		X
Kansas			S	X	X
Kentucky			C, M, S	X	
Louisiana			C, M, S	X	
Maine					
Maryland	X				
Massachusetts			M	X	
Michigan	X	1.5 - 5	M	X	
Minnesota					X
Mississippi				X	
Missouri			C, M, S	X	
Montana			C, M, S	X	
Nebraska			C, M, S	X	X
Nevada	X	3.64	M, S	X	
New Hampshire					
New Jersey	X			X	X
New Mexico		2	C, M, S	X	
New York	X		C, M, S		
North Carolina			C, M		
North Dakota			C, M, S	X	
Ohio		1		X	
Oklahoma	X	1.5			
Oregon	X	1.5	S	X	
Pennsylvania			C, M, S	X	
Rhode Island				X	
South Carolina	X				
South Dakota			C, M, S	X	
Tennessee					
Texas	X		C, M, S	X	
Utah			C, M, S		
Vermont					
Virginia					
Washington	X	1	C, M, S	X	
West Virginia		.5 - 2	C, M, S	X	
Wisconsin			C		
Wyoming			C, M, S		

*(C = county, M = municipality, S = school district)

Source: Mikhalov, N.: "Types of Property Tax and Assessment Limitations and Tax Relief Programs", Lincoln Institute of Land Policy, Sept. 1999 (rev'd 2001) and review of state statutes.

Appendix C

Income Tax Information

CORPORATE INCOME TAX CREDITS CLAIMED BY TAX YEAR

		2001	2000	1999	1998	1997	1996	1995	1994
Agricultural	# of claims		0						
Pollution	credit available	Not	$0	Not					
Control	credit used	Releasable	$0	Releasable					
Equipment	carry forward		$0						
Agricultural	# of claims	0							
Preservation	credit available	$0							
District	credit used	$0							
	carry forward	$0							
Agricultural	# of claims								5
Water	credit available	Not	Not	Not	Not	Not	Not	Not	$147,276
Conservation	credit used	Releasable	Releasable	Releasable	Releasable	Releasable	Releasable	Releasable	$35,531
	carry forward								$111,745
Alternative	# of claims	0	4	8	3				
Fuel Delivery	credit available	$0	$831,419	$2,435,383	$1,287,994				
System	credit used	$0	$50	$1,377,215	$1,083,345				
NONREFUNDABLE	carry forward	$0	$831,369	$1,058,168	$204,649				
Alternative	# of claims	0	5						
Fuel Delivery	credit available	$0	$679,992						
System	credit used	$0	$314,676						
REFUNDABLE	credit refunded	$0	$363,316						
	carry forward	$0	$0						
Alternative	# of claims		9	23	12	4		4	
Fuel	credit available	Not	$653,566	$1,407,058	$190,258	$11,150	Not	$61,000	Not
Vehicles	credit used	Releasable	$284,971	$324,234	$36,231	$4,805	Releasable	$61,000	Releasable
NONREFUNDABLE	carry forward		$368,595	$1,082,824	$154,027	$6,345		$0	
Alternative	# of claims	10	181						
Fuel	credit available	$186,006	$15,636,705						
Vehicles	credit used	$17,653	$488,150						
REFUNDABLE	credit refunded	$168,353	$15,129,164						
	carry forward	$0	$19,391						
Construction	# of claims		4	7	5	10	11	8	
Materials	credit available	Not	$630,976	$1,161,103	$1,567,984	$2,018,694	$2,162,591	$5,880,673	Not
	credit used	Releasable	$204,184	$419,071	$1,039,178	$878,822	$944,392	$4,868,089	Releasable
	carry forward		$426,792	$746,279	$581,925	$1,139,782	$1,218,199	$1,012,584	
Correctional	# of claims			0	0	0	0	0	0
Industries	credit available			$0	$0	$0	$0	$0	$0
	credit used			$0	$0	$0	$0	$0	$0
	carry forward			$0	$0	$0	$0	$0	$0

CORPORATE INCOME TAX CREDITS CLAIMED BY TAX YEAR

		2001	2000	1999	1998	1997	1996	1995	1994
Defense	# of claims		3	4	4	4	4		
Contracting	credit available	Not	$17,805,857	$18,278,121	$43,605,454	$41,879,669	$32,539,670	Not	Not
	credit used	Releasable	$2,659,007	$751,956	$116,500	$748,881	$3,551,214	Releasable	Releasable
	carry forward		$15,146,850	$17,526,165	$43,488,954	$39,112,041	$28,988,456		
Donation of	# of claims	0	0	0					
Motor Vehicles	credit available	$0	$0	$0					
To Work	credit used	$0	$0	$0					
Program	carry forward	$0	$0	$0					
Employer	# of claims								5
Dependent	credit available								$6,963
Day Care	credit used								$6,839
	carry forward								
Employment of	# of claims	4	6	5	3				
TANF	credit available	$60,627	$41,996	$49,653	$35,325				
Recipients	credit used	$49,080	$27,598	$47,189	$35,325				
	carry forward	$11,547	$14,398	$2,464	$0				
Enterprise	# of claims	58	71	82	87	87	73	35	29
Zone	credit available	$7,171,682	$12,046,325	$16,063,664	$13,657,130	$10,699,928	$6,345,410	$3,298,657	$1,332,567
	credit used	$3,558,339	$4,883,910	$10,284,361	$7,249,708	$4,958,092	$3,849,101	$2,339,841	$1,080,017
	carry forward	$3,613,343	$7,162,415	$5,779,303	$6,407,422	$5,741,836	$2,496,309	$958,815	$252,549
Environmental	# of claims				4	3	6	5	4
Technology	credit available	Not	Not	Not	$36,520,479	$34,966,768	$35,649,281	$41,754,468	$16,245,878
Facility	credit used	Releasable	Releasable	Releasable	$365,267	$38	$2,556,477	$15,821,459	$2,329,787
	carry forward				$36,155,212	$34,966,730	$33,092,804	$25,933,009	$13,916,091
Military	# of claims	3	3	3		3	3	0	0
Reuse	credit available	$131,312	$136,702	$175,336	Not	$34,888	$18,000	$0	$0
Zone	credit used	$109,373	$120,440	$170,634	Releasable	$11,888	$4,731	$0	$0
	carry forward	$21,939	$16,262	$4,702		$23,000	$13,269	$0	$0
Neighborhood	# of claims	8	37	43					
Electric Vehicles	credit available	$686,822	$2,059,055	$1,658,593					
	credit used	$14,258	$1,142,629	$1,311,887					
	carry forward	$672,564	$916,426	$346,706					
Pollution	# of claims	11	32	32	23	25	29	21	
Control Device	credit available	$1,487,080	$10,472,253	$12,797,002	$8,746,561	$3,861,844	$6,937,066	$3,226,099	
	credit used	$890,624	$3,806,949	$6,761,571	$4,211,037	$2,172,166	$4,498,473	$1,577,433	
	carry forward	$596,456	$6,665,304	$6,317,628	$4,451,236	$1,948,803	$2,438,593	$1,648,666	
Recycling	# of claims	4	5	4	4	4	4	5	3
Equipment	credit available	$218,919	$238,422	$250,210	$274,352	$161,315	$142,144	$122,676	$85,919
	credit used	$21,442	$15,626	$16,028	$12,660	$10,672	$11,167	$14,851	$14,920
	carry forward	$197,477	$222,796	$234,182	$261,692	$150,643	$130,977	$107,825	$70,999

CORPORATE INCOME TAX CREDITS CLAIMED BY TAX YEAR

		2001	2000	1999	1998	1997	1996	1995	1994
Research &	# of claims	59	105	132	124	132	111	86	89
Development	credit available	$29,216,092	$19,900,992	$18,516,226	$18,566,480	$19,462,303	$15,358,856	$9,559,521	$5,445,055
	credit used	$5,866,557	$6,624,306	$9,044,648	$8,298,441	$11,212,168	$9,637,067	$6,297,972	$3,062,056
	old carry forward	$104,638,904	$317,668,240	$288,753,015	$189,780,443	$81,537,496	$100,583,439	$49,857,808	$26,466,029
	new carry forward	$22,888,560							
School Site	# of claims								
Donation	credit available	Not							
	credit used	Releasable							
	carry forward								
Solar Hot Water	# of claims	0		0	0				
Plumbing Stub	credit available	$0	Not	$0	$0				
Outs & Electric	credit used	$0	Releasable	$0	$0				
Vehicle Recharge	carry forward	$0		$0	$0				
Summer	# of claims						0		
School	credit available						$0	Not	
& Jobs	credit used						$0	Releasable	
	carry forward								
Taxes Paid for	# of claims			4	4				
Coal Consumed	credit available	Not	Not	$1,305,513	$909,319				
In Generating	credit used	Releasable	Releasable	$803,476	$671,375				
Electrical Power	carry forward			$502,037	$237,944				
Underground	# of claims	0	0	0	0			0	
Storage	credit available	$0	$0	$0	$0	Not	Not	$0	Not
Tanks	credit used	$0	$0	$0	$0	Releasable	Releasable	$0	Releasable
	carry forward								
Vehicle Refueling	# of claims		4	7					
Apparatus &	credit available	Not	$8,712	$29,765					
Infrastructure	credit used	Releasable	$2,180	$13,630					
NONREFUNDABLE	carry forward		$6,532	$16,135					
Vehicle Refueling	# of claims	0	12						
Apparatus &	credit available	$0	$138,940						
Infrastructure	credit used	$0	$46,332						
REFUNDABLE	credit refunded	$0	$92,608						
	carry forward	$0	$0						

CORPORATE INCOME TAX CREDITS CLAIMED BY TAX YEAR

		2001	2000	1999	1998	1997	1996	1995	1994
TOTAL	# of claims	*171*	492	365	281	276	249	174	141
	credit available	*$57,740,439*	$106,241,707	$98,338,641	$130,092,555	$117,777,849	$103,923,447	$90,972,700	$38,162,370
	credit used	*$12,387,227*	$20,923,149	$31,659,806	$23,260,940	$20,140,960	$25,208,106	$32,335,117	$7,096,834
	credit refunded	*$168,353*	$15,585,088						
	old carry forward	*$126,474,228*	$374,123,024	$346,246,716	$286,312,850	$169,162,965	$173,576,991	$105,233,474	$55,148,008
	new carry forward	*$22,888,560*							

Notes:
1. Shaded areas indicate that the credit was not in effect during the tax year.
2. "Not Releasable" indicates that the credit information cannot be released due to confidentiality restrictions.
3. "Total" includes credits for which information was "not releasable" individually.
4. DATA IN *ITALICS* IS PRELIMINARY.

INDIVIDUAL INCOME TAX CREDITS CLAIMED BY TAX YEAR

		2001	2000	1999	1998	1997	1996	1995	1994
Agricultural	# of claims		9						
Pollution	credit available	Data Not	$77,096	Not					
Control	credit used	Available	$17,562	Releasable					
Equipment	carry forward		$59,534						
Agricultural	# of claims								
Preservation	credit available	Data Not							
District	credit used	Available							
	carry forward								
Agricultural	# of claims		*86*	121	88	63	75	54	35
Water	credit available	Data Not	*$5,886,179*	$7,933,712	$4,188,037	$3,752,833	$4,247,392	$2,600,000	$1,800,000
Conservation	credit used	Available	*$1,289,513*	$922,072	$576,761	$430,131	$721,093	$923,000	$382,000
	carry forward		*$4,553,700*	$6,696,194	$3,618,953	$3,323,906	$3,524,790	$1,700,000	$1,400,000
Alternative	# of claims		7	12					
Fuel Delivery	credit available	Not	$49,812	$64,607	Not				
System	credit used	Releasable	$41,417	$21,864	Releasable				
NONREFUNDABLE	carry forward		$8,395	$42,743					
Alternative	# of claims		19						
Fuel Delivery	credit available	Not	$2,863,157						
System	credit used	Releasable	$192,848						
REFUNDABLE	credit refunded		$2,670,309						
	carry forward		$0						
Alternative	# of claims	9	176	246	71	33	35	24	51
Fuel	credit available	$71,601	$2,729,449	$2,215,687	$79,855	$32,703	$33,050	$14,000	$36,000
Vehicles	credit used	$46,911	$322,257	$736,134	$60,447	$23,409	$23,773	$11,000	$29,000
NONREFUNDABLE	carry forward	$24,690	$2,400,243	$479,553	$19,408	$9,294	$9,277	$3,000	$7,000
Alternative	# of claims	151	4,891						
Fuel	credit available	$2,558,844	$94,166,701						
Vehicles	credit used	$322,352	$13,072,594						
REFUNDABLE	credit refunded	$2,236,492	$81,038,418						
	carry forward	$0	$55,689						
Clean Elections	# of claims	26,757	23,717	8,585					
	credit available	$639,427	$564,312	$546,255					
	credit used	$599,485	$537,345	$502,151					
	carry forward								
Construction	# of claims				0	0	0	0	
Materials	credit available	Not	Not	Not	$0	$0	$0	$0	
	credit used	Releasable	Releasable	Releasable	$0	$0	$0	$0	
	carry forward				$0	$0	$0	$0	

INDIVIDUAL INCOME TAX CREDITS CLAIMED BY TAX YEAR

		2001	2000	1999	1998	1997	1996	1995	1994
Contributions	# of claims		*5,705*	6,712	2,856				
To Charities	credit available	Data Not	*$1,017,604*	$1,161,162	$475,438				
Providing Help	credit used	Available	*$1,000,257*	$1,147,485	$472,502				
To Working Poor	carry forward		*$17,347*	$13,677	$2,936				
Defense	# of claims		0	0	0	0	0	0	0
Contracting	credit available	Data Not	$0	$0	$0	$0	$0	$0	$0
	credit used	Available	$0	$0	$0	$0	$0	$0	$0
	carry forward		$0	$0	$0	$0	$0	$0	$0
Donation of	# of claims		461	92					
Motor Vehicles	credit available	Data Not	$610,576	$121,698					
To Work	credit used	Available	$546,758	$102,327					
Program	carry forward								
Employer	# of claims							0	
Dependent	credit available							$0	Not
Day Care	credit used							$0	Releasable
	carry forward								
Employment of	# of claims	0	0						
TANF Recipients	credit available	$0	$0	Not	Not				
	credit used	$0	$0	Releasable	Releasable				
	carry forward	$0	$0						
Enterprise	# of claims	153	146	143	132	124	74	32	25
Zone	credit available	$2,690,716	$3,004,889	$2,519,312	$2,084,378	$1,358,636	$775,687	$835,696	$595,894
	credit used	$1,619,102	$1,596,521	$1,417,307	$1,277,788	$725,178	$307,551	$667,005	$337,581
	carry forward	$1,071,614	$1,408,368	$1,102,005	$806,620	$633,458	$468,135	$168,691	$258,313
Environmental	# of claims	0	0	0	0	0	0	0	0
Technology	credit available	$0	$0	$0	$0	$0	$0	$0	$0
	credit used	$0	$0	$0	$0	$0	$0	$0	$0
	carry forward	$0	$0	$0	$0	$0	$0	$0	$0
Family Tax	# of claims	402,094	335,253	327,974	312,768	345,223	340,790	340,844	
Credit	credit available	$33,377,585	$28,924,670	$28,374,663	$27,669,951	$20,483,252	$20,526,564	$20,600,000	
	credit used	$7,356,939	$7,799,840	$7,925,721	$7,390,406	$4,637,593	$5,071,340	$5,150,000	
	carry forward								
Income Taxes Paid	# of claims	*28,156*	27,831	26,317	25,794	25,325	23,379	22,496	20,917
To Other States	credit available	*$57,741,188*	$57,403,404	$51,433,659	$53,091,928	$42,910,138	$40,570,806	$29,203,587	$31,611,330
or Countries	credit used	*$57,741,188*	$57,403,404	$51,433,659	$53,091,928	$42,910,138	$40,570,806	$29,203,587	$31,611,330
	carry forward								
Increased Excise	# of claims	428,189							
Taxes Paid	credit available	$22,612,548							
	credit used	$22,612,548							
	carry forward								

INDIVIDUAL INCOME TAX CREDITS CLAIMED BY TAX YEAR

		2001	2000	1999	1998	1997	1996	1995	1994
Military	# of claims		0	0	0			0	0
Reuse Zone	credit available	Data Not	$0	$0	$0	Not	Not	$0	$0
	credit used	Available	$0	$0	$0	Releasable	Releasable	$0	$0
	carry forward		$0	$0	$0			$0	$0
Neighborhood	# of claims	*1,370*	*3,258*	1,146					
Electric Vehicle	credit available	*$8,525,940*	*$31,117,750*	$11,505,375					
	credit used	*$2,850,991*	*$17,010,923*	$6,770,641					
	carry forward	*$5,674,949*	*$14,106,827*	$4,734,735					
Pollution	# of claims						0	0	
Control Device	credit available	Data Not	Not	Not	Not	Not	$0	$0	
	credit used	Available	Releasable	Releasable	Releasable	Releasable	$0	$0	
	carry forward						$0	$0	
Private School	# of claims	46,546	38,084	31,892	4,248				
Tuition	credit available	$24,838,082	$17,620,022	$13,716,791	$1,816,299				
Organization	credit used	$24,838,082	$17,620,022	$13,716,791	$1,816,299				
	carry forward								
Property	# of claims	15,213	14,593	15,862	17,237	18,644	19,983	22,091	23,743
Tax	credit available	$5,014,476	$4,653,837	$4,987,796	$5,290,628	$5,581,477	$5,819,917	$6,342,285	$6,614,161
	credit used	$5,014,476	$4,653,837	$4,987,796	$5,290,628	$5,581,477	$5,819,917	$6,342,285	$6,614,161
	carry forward								
Public School	# of claims	166,468	149,215	109,748	74,242				
Extra	credit available	$20,004,715	$17,526,299	$14,775,353	$8,990,042				
Curricular	credit used	$20,004,715	$17,526,299	$14,775,353	$8,990,042				
Activity	carry forward								
Recycling	# of claims		6			5			
Equipment	credit available	Data Not	$26,303	Not	Not	$17,757	Not	Not	Not
	credit used	Available	$4,605	Releasable	Releasable	$7,007	Releasable	Releasable	Releasable
	carry forward		$21,698			$10,750			
Research &	# of claims								
Development	credit available	Data Not							
	credit used	Available							
	carry forward								
School Site	# of claims								
Donation	credit available	Data Not							
	credit used	Available							
	carry forward								
Solar	# of claims		2,532	2,757	2,147	1,827	1,632	1,924	
Energy	credit available	Data Not	$1,029,183	$994,981	$784,656	$550,128	$534,174	$655,000	
	credit used	Available	$902,637	$913,984	$685,645	$524,600	$512,838	$593,000	
	carry forward		$139,075	$149,253	$102,745	$103,893	$66,634	$63,000	

INDIVIDUAL INCOME TAX CREDITS CLAIMED BY TAX YEAR

		2001	2000	1999	1998	1997	1996	1995	1994
Solar Hot Water	# of claims	Data Not Available	35	35	23				
Plumbing Stub	credit available		$21,308	$16,859	$12,352				
Outs & Electric	credit used		$11,566	$7,944	$8,874				
Vehicle Recharge	carry forward		$9,742	$8,915	$3,478				
Summer	# of claims						3	Not Releasable	
School	credit available						$837		
& Jobs	credit used						$837		
	carry forward								
Technology	# of claims	Not Releasable							
Training	credit available								
	credit used								
	carry forward								
Underground	# of claims	0	0	0	0	0	0	0	Not Releasable
Storage Tanks	credit available	$0	$0	$0	$0	$0	$0	$0	
	credit used	$0	$0	$0	$0	$0	$0	$0	
	carry forward								
Vehicle Refueling	# of claims	0	120	73					
Apparatus &	credit available	$0	$260,428	$199,489					
Infrastructure	credit used	$0	$208,315	$101,753					
NONREFUNDABLE	carry forward	$0	$52,113	$97,736					
Vehicle Refueling	# of claims	12	670						
Apparatus &	credit available	$33,750	$3,192,104						
Infrastructure	credit used	$25,456	$395,877						
REFUNDABLE	credit refunded	$8,294	$2,796,227						
	carry forward	$0	$0						
TOTAL	# of claims	*1,115,124*	*606,820*	531,731	439,618	391,246	385,974	387,473	44,780
	credit available	*$178,146,915*	*$272,277,257*	$140,746,247	$104,604,472	$74,690,366	$72,526,475	$60,266,064	$40,686,808
	credit used	*$143,068,911*	*$142,166,517*	$105,605,106	$79,736,314	$54,840,919	$53,033,668	$42,895,373	$38,979,592
	credit refunded	*$2,244,786*	*$86,504,954*						
	carry forward	*$6,772,630*	*$22,963,361*	$13,503,233	$4,600,054	$4,083,357	$4,081,371	$1,944,691	$1,675,788

Notes:
1. Shaded areas indicate that the credit was not in effect during the tax year.
2. "Not Releasable" indicates that the credit information cannot be released due to confidentiality restrictions.
3. "Total" includes credits for which information was "not releasable" individually.
4. DATA IN *ITALICS* IS PRELIMINARY.

Corporate Income Tax Credits

Tax Reform for Arizona Citizens Committee

October 22, 2003

JLBC Staff

Corporate Income Tax Credits

- There are 19 Arizona income tax credits available to corporations.
- In 2000, (the latest data available), corporations used or had refunded to them $33.0 million in tax credits.
- Another $355.1 million in unused corporate tax credits were carried forward. Some may never be used without sufficient offsetting tax liability.

Issues Affecting Tax Credit Evaluation

- Under Arizona law, DOR will not release any information on income tax credits.
- Timeliness: data for corporate income tax credits extend only through 2000.
- Lack of performance measures: there are few reporting requirements for economic benefits, such as payrolls generated or jobs created.

Confidentiality

- DOR interprets ARS 42-2001 as prohibiting release of company-specific tax credit data, unless otherwise permitted by law.
- So few companies take some credits that we have no financial data on them at all.
- Several other states require tax credit data to be made public. No state releases entire returns or income information.

Confidentiality

- Minnesota and Maine have laws allowing full disclosure of income tax credits claimed.
- Connecticut, North Carolina, West Virginia and Ohio allow publication of some company-specific income tax information.
- Nebraska requires publication of credits claimed and related performance measures.

Data Availability

- DOR summary reports are only available through 2000 for corporations.
- Current information systems are limited. Tax credit data must be compiled from hard-copy returns.
- DOR's new automated tax system (BRITS) should improve the quantity, quality and timeliness of the tax credit data.

Tax Credit Objectives and Performance Measures

- Some credits, such as the defense contracting credit, have clearly stated performance measures and objectives.
- Some credits do not have an objective or measurable goal in statute.
- Some credits, like the research and development credit, have goals but lack performance measures.

Joint Legislative Income Tax Credit Review Committee Was Established in 2002 to Address These Issues

- By statute, the Committee shall determine the purpose of <u>existing</u> tax credits and establish a standard for evaluating them.
- The Committee is required to measure the success or failure of the tax credits.
- Since 2002, statute requires any <u>new</u> credits to include "a purpose clause that explains the rationale and objective of the tax credit."

Potential Tax Credit Objectives

- Economic development.
- Investment.
- Environmental improvement.
- Incentives and behavioral changes.

Statute Outlines Performance Standards for Tax Credits

- Performance standards may include:
  - Estimated revenue impact.
  - Job creation or retention.
  - New investments.
  - Measurable economic development.
  - Complexity of application, administration and approval.
- Other objectives may be defined specific to the purpose of the credit.
- Confidentiality and timeliness issues will continue to pose a challenge in evaluating the credits.

Appendix D

Transaction Privilege Tax Information

ARIZONA TRANSACTION PRIVILEGE & USE TAX OVERVIEW

Revenues from state transaction privilege tax (TPT) and use tax:

FY 2001-2002:

Distribution Base:	$1,246,773,262
Nonshared:	$2,379,509,616
Use Tax:	$ 162,751,987
Education Tax :	$ 439,004,543
TOTAL	$4,228,039,408

FY 2002-2003:

Distribution Base:	$1,265,625,175
Nonshared:	$2,400,432,714
Use Tax:	$ 190,186,057
Education Tax:	$ 447,841,034
TOTAL	$4,304,084,980

Note: The use tax goes directly to the state general fund and is not shared with local government. Revenue figures are from the Arizona Department of Revenue.

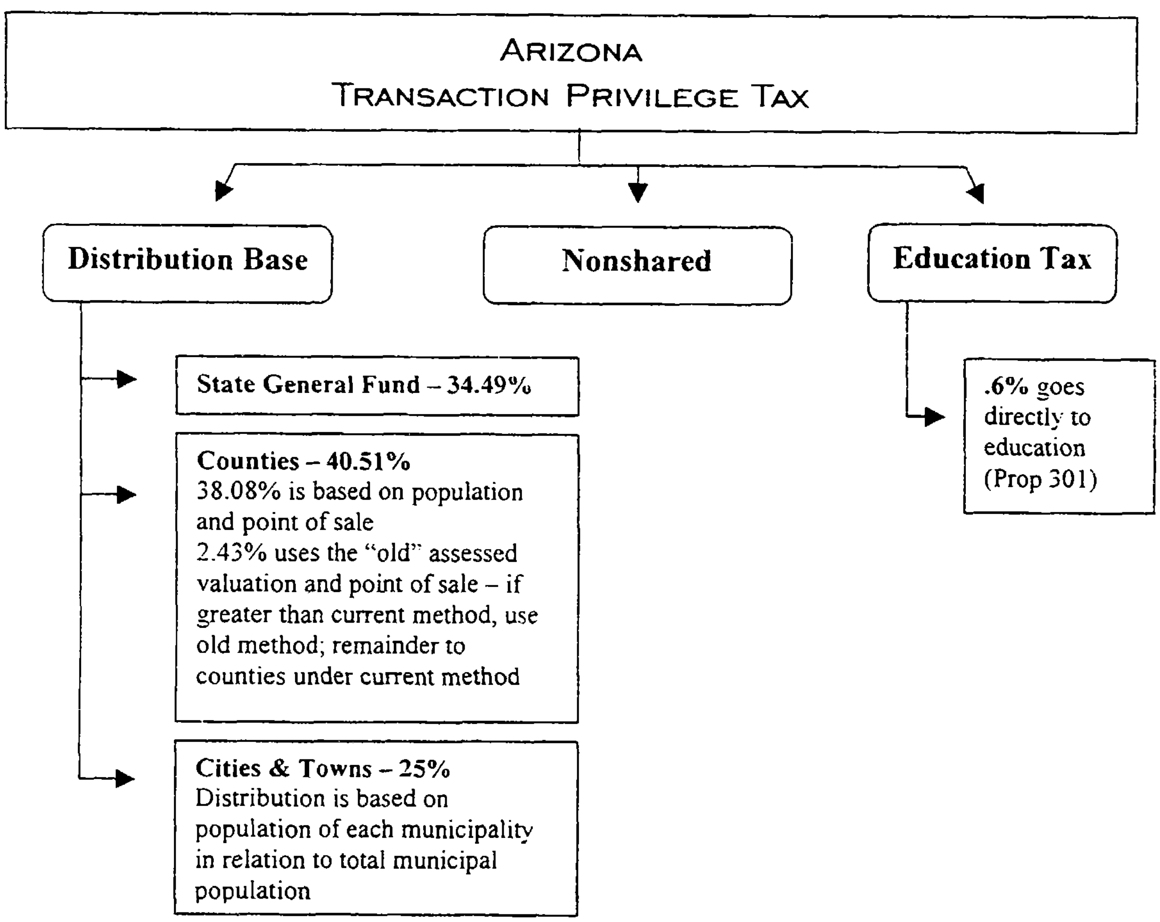


TABLE 5
STATE TRANSACTION PRIVILEGE, USE AND SEVERANCE TAX RATES
FISCAL YEAR 2001-02

TAXABLE ACTIVITIES	DISTRIBUTION BASE	NONSHARED	EDUCATION	TOTAL TAX
1. Transporting and Towing	1.0%	4.0%	0.6%	5.6%
2. Nonmetalliferous Mining, Oil and Gas Production	1.0%	2.125%	0.0%	3.125%
4. Utilities	1.0%	4.0%	0.6%	5.6%
5. Communications	1.0%	4.0%	0.6%	5.6%
6. Railroads and Aircraft	1.0%	4.0%	0.6%	5.6%
7/8. Private Car/Pipelines	1.0%	4.0%	0.6%	5.6%
9. Publishing	1.0%	4.0%	0.6%	5.6%
10. Printing	1.0%	4.0%	0.6%	5.6%
11. Restaurants and Bars	2.0%	3.0%	0.6%	5.6%
12. Amusements	2.0%	3.0%	0.6%	5.6%
14. Personal Property Rentals	2.0%	3.0%	0.6%	5.6%
15. Contracting (1)	1.0%	4.0%	0.6%	5.6%
17. Retail	2.0%	3.0%	0.6%	5.6%
19. Mining Severance	2.5%	0.0%	0.0%	2.5%
21. Timbering Severance - Ponderosa (per thousand board feet)	$1.704	$0.426	$0	$2.13
22. Timbering Severance - Other (per thousand board feet)	$1.208	$0.302	$0	$1.51
25. Hotel/Motel Tax	2.75%	2.75%	0.0%	5.5%
28. Rental Occupancy Tax	2.0%	1.0%	0.0%	3.0%
29/30. Use and Use Inventory Tax	0.0%	5.0%	0.6%	5.6%
47. Membership Camping	2.0%	3.0%	0.6%	5.6%
49. Jet Fuel (per gallon)	$0.0122	$0.0183	$0	$0.0305
51. Jet Fuel Use (per gallon)	$0	$0.0305	$0	$0.0305

(1) Most Contracting activity is covered under class 15, at a 5.6% total tax rate. Other classes at lower rates exist.

Source: Arizona Department of Revenue 2002 Annual Report

TABLE 7

TRANSACTION PRIVILEGE, USE AND SEVERANCE TAX COLLECTIONS BY CLASS (1)

FISCAL YEAR 2001-02

CLASSIFICATION	DISTRIBUTION BASE	NONSHARED	TOTAL COLLECTIONS
Transporting and Towing	$575,672	$2,302,688	$2,878,360
Nonmetal Mining, Oil and Gas	2,083,100	4,426,588	6,509,688
Mining Severance	(85,598)	(20,993)	(106,591)
Timbering Severance	9,196	2,299	11,495
Timbering Severance - Ponderosa	718	180	897
Timbering Severance - Other	1,114	278	1,392
Utilities	59,192,731	236,770,926	295,963,657
Communications	29,456,814	117,827,256	147,284,070
Railroads and Aircraft	387,889	1,551,556	1,939,445
Private Car and Pipelines	71,342	285,368	356,709
Publishing	828,432	3,313,728	4,142,161
Printing	3,511,419	14,045,679	17,557,098
Restaurants and Bars	128,574,246	192,861,370	321,435,616
Amusements	14,876,008	22,314,011	37,190,018
Commercial Lease (3)	303,101	271,413	574,514
Rentals of Personal Property	72,150,374	108,225,567	180,375,941
Contracting	118,205,962	472,823,862	591,029,823
Feed Wholesale (2)	(4,518)	(3,954)	(8,471)
Retail	768,614,485	1,153,028,514	1,921,642,999
Hotel/Motel	45,643,489	45,643,365	91,286,854
Rental Occupancy Tax	119,358	59,670	179,029
Use Tax	0	162,022,998	162,022,998
License Fees	0	475,424	475,424
Membership Camping	54,823	82,234	137,057
Jet Fuel Tax	2,259,054	3,388,581	5,647,634
Jet Fuel Use Tax	0	728,989	728,989
Non Sufficient Funds	0	36,558	36,558
Telecommunications Service Assistance	(55,948)	(223,793)	(279,742)
Miscellaneous Fees	0	20	20
Agriculture Equipment (4)	0	21,064	21,064
Utility Credit/Reimbursement	0	157	157
TOTAL	**$1,246,773,262**	**$2,542,261,603**	**$3,789,034,865**

(1) Does not reflect the balance of undistributed estimated payments at the end of FY02.

(2) Feed Wholesale dropped to 0% effective July 17, 1994 and was repealed effective October 1, 1994.

(3) Commercial Lease rate dropped to 0% effective July 1, 1997.

(4) Agriculture Equipment was phased out July 1, 1988 and is not a current business classification.

Figures may not add to total due to rounding.

Source: Arizona Department of Revenue 2002 Annual Report

TABLE 4
GROSS TRANSACTION PRIVILEGE, USE AND SEVERANCE TAX COLLECTIONS
FISCAL YEAR 1997-98 THROUGH FISCAL YEAR 2001-02

SOURCE	FY1997-98	FY1998-99	FY1999-00	FY2000-01	FY2001-02
Distribution Base	$1,015,306,840	$1,089,625,165 (5)	$1,195,140,016	$1,248,485,639	$1,246,773,262
Nonshared	1,875,579,736	2,042,232,511 (5)	2,230,332,220	2,356,788,664	2,379,509,616
Use Tax	136,868,591	148,043,174 (5)	176,566,264	196,887,927	162,751,987
SUBTOTAL	**$3,027,755,167**	**$3,279,900,850**	**$3,602,038,500**	**$3,802,162,230**	**$3,789,034,865**
Education Tax (9)	-----	-----	-----	100,682 (1)	439,004,543
Undistributed Estimated	5,262,078	11,668,636	12,392,607	1,894,841	28,766,081
911 Wireline/Excise Tax	7,652,326	8,084,729	7,846,057	9,201,049	14,998,348
Telecommunications Devices	4,908,914	5,158,289	4,960,224	5,514,542	6,395,057
Poison Control Fund	1,815,626	1,907,860	1,834,603	2,039,625	2,365,295
911 Wireless Service	722,736 (1)	1,181,481	1,507,573	2,136,015	6,928,990
Municipal Water	1,891,072	1,957,725	2,081,879	2,120,483	2,213,435
Environmentally Hazardous Products (2)	784	536	980	5,909	14
Waste Tire Accounts					
Receivable Collections	105,094	62,946	25,739	109,948	71,330
Less Collection Fees	(2,255)	(1,521)	(2,682)	(4,084)	(888)
GROSS STATE COLLECTIONS	**$3,050,111,543**	**$3,309,921,530**	**$3,632,685,479**	**$3,825,281,241**	**$4,289,777,071**
Municipal Privilege Tax	180,932,433	202,218,016	230,976,587	257,706,985	280,950,442
Pima County Hotel Tax	2,378,163	2,437,787	2,625,508	2,823,410	2,495,830
Maricopa County Rental Car Surcharge	5,376,877	5,405,493	5,734,678	5,636,907	5,396,445
Pima County Rental Car Surcharge	1,384,659	1,388,744	1,476,750	1,557,354	1,377,083
Pima County R.V. Surcharge	182,205 (1)	218,359	212,849	197,598	189,838
Apache County Excise Tax	582,718	638,649	1,862,479	1,130,977	903,381
Cochise County Excise Tax	4,058,429	4,311,066	4,853,891	5,123,754	5,698,660
Coconino County Excise Tax	7,742,012	8,085,596	8,876,866	9,054,404	8,793,909
Coconino County Jail Tax	4,121,136	4,793,744	5,261,397	5,358,317	5,486,442
Gila County Excise Tax	2,357,618	2,350,334	2,311,624	2,596,028	2,617,971
Gila County Hospital Tax (3)	3,054	7,003	92	38,499	509
Gila County Transportation	2,396,123	2,423,201	2,377,944	2,612,288	2,718,050
Graham County Excise Tax	1,128,771	1,172,236	1,188,238	1,206,320	1,192,075
Greenlee County Excise Tax	632,440	546,749	563,020	645,168	562,389
La Paz County Excise Tax	691,178	777,423	806,441	820,780	885,465
La Paz County Jail Tax	692,383	776,444	807,563	821,969	885,694
Maricopa County Road Tax	209,263,453	229,470,201	248,595,990	264,722,440	267,563,343
Maricopa County Stadium Tax (4)	50,550,929	437,677	150,336	280,370	145,148
Maricopa County Jail Tax	-----	34,290,683 (1)	91,054,451	97,603,200	98,372,053
Mohave County Excise Tax	-----	-----	1,608,620 (1)	4,114,594	4,446,472
Navajo County Excise Tax	3,964,486	4,372,839	4,655,169	4,831,327	4,993,912
Pinal County Excise Tax	5,076,787	5,698,428	6,149,485	6,492,013	6,763,454
Pinal County Road Tax	5,232,966	6,072,244	6,575,202	6,750,294	6,965,671
Santa Cruz County Excise Tax	1,725,137	1,847,305	1,918,653	2,092,940	2,114,505
Yavapai County Excise Tax	7,696,746	8,565,735	9,571,900	10,054,989	10,799,358
Yavapai County Jail Tax (6)	-----	-----	-----	3,627,698	4,294,368
Yuma County Excise Tax	6,252,408	6,638,969	6,965,025	7,417,302	7,665,873
Yuma County Jail Tax	6,241,927	6,617,655	6,950,571	7,412,145	7,653,390
Yuma County Capitol Projects Tax (7)	-----	-----	-----	3,150,273 (1)	7,582,374
Tourism/Sports Authority (8)	-----	-----	-----	5,579,087 (1)	16,504,732
COUNTY AND CITY COLLECTIONS	**510,665,036**	**541,562,578**	**654,131,327**	**721,459,433**	**766,018,836**
TOTAL DEPARTMENT OF REVENUE RECEIPTS	**$3,560,776,579**	**$3,851,484,108**	**$4,286,816,806**	**$4,546,740,674**	**$5,055,795,907**

(1) The tax was in place for only a portion of the first fiscal year. This figure does not represent a full year's collection.
(2) Environmentally Hazardous Products was repealed September 1, 1992. All amounts received are for prior tax periods.
(3) Gila County Hospital Tax ended effective March 31, 1993.
(4) Maricopa County Stadium Tax ended effective December 1, 1997.
(5) Corrected Figure.
(6) Yavapai County Jail Tax began on July 1, 2000
(7) Yuma County Capitol Projects Tax Began on January 1, 2001
(8) Tourism/Sports Authority Tax became effective March 1, 2001.
(9) Education Tax became effective on June, 1, 2001.

Source: Arizona Department of Revenue 2002 Annual Report

State and Local Transaction Privilege Taxes
(or similar excise taxes)

STATE:

Reliance: Arizona has a heavy reliance on sales tax as a source of general fund revenues.

FISCAL YEAR	% OF GF REVENUES
1993	43.1%
1994	44.0%
1995	44.1%
1996	45.1%
1997	43.9%
1998	45.3%
1999	45.7%
2000	46.9%
2001	48.3%
2002	46.9%
2003	49.9%

Rates: The current state rate is 5.6%. This rate consists of 5% for general purposes and .6% for education funding.

Base: The state tax base for the TPT and use tax is set forth in Title 42 of the Arizona Revised Statutes. Exemptions and deductions to the tax are provided for in the statute. (see attached chart)

Procedure for raising/lowering tax rate: As with all tax rate decreases, the Legislature needs only a majority vote of its members to decrease the tax rate or add exemptions. However, since 1992, with the passage of Proposition 108, the Legislature needs a super majority vote – two-thirds of the House and Senate – to increase the tax rate or eliminate exemptions if it results in a net increase of state revenues. If passed, the measure is immediately effective upon signature of the Governor.

COUNTIES:

Reliance: Arizona county reliance on sales taxes is varied. The reliance ranges from a low of 23% of the general fund revenue to over 60%. Information below was provided the County Supervisors Association.

FY 2001-2002	TPT state shared revenue	County sales tax revenue	Total GF revenue	Total % reliance on sales tax
Apache	$3,801,000	$903,380	$10,703,763	43.95%
Cochise	$9125,000	$3,950689	$37,748,103	34.64%
Coconino	$14,352,000	$9,082,000	$36,770,498	63.73%
Gila	$4,070,030	$2,615,000	$28,893,306	23.14%
Graham	$2,370,358	$1,193,503	$12,129,848	29.38%
Greenlee	$1,586,000	$575,066	$4,464,127	48.41%
La Paz	$1,522,048	$891,813	$9,890,890	24.40%
Maricopa	$341,524,693	*	$853,837,343	40.00%
Mohave	$13,729,713	$4,446,472	$50,518,689	35.98%
Navajo	$8,030,297	$5,042,256	$23,805,272	54.91%
Pima	$75,500,000	*	$311,945,406	24.20%
Pinal	$12,439,193	$6,648,534	$71,952,928	26.53%
Santa Cruz	$3,260,749	$1,242,156	$16,965,358	26.54%
Yavapai	$16,500,000	$2,180,000	$54,637,000	34.19%
Yuma	$12,511,319	$7,561,623	$43,072,315	46.60%

*Pima County does not levy a general county sales tax and Maricopa County is not permitted to levy a general county sales tax.

Rates: ARS 42-6103 allows all counties, except Maricopa, to levy a general excise tax (sales tax). The tax is limited to one-half percent (10% of the 5% state rate). In addition, statutes allow sales tax at the county level to fund specific activities.

Base: The counties use the same tax base as the state. However, this rate is usually tied to the base at a particular point in time. For example, the Maricopa County transportation tax is tied to the state tax base that was in effect January 1, 1990. The base at that time included commercial rentals. The commercial rental state tax was phased-out and the state no longer collects this tax. However, it is still collected as part of the Maricopa County transportation tax (and is an issue in discussions to extend the tax.)

Procedure for raising/lowering tax rate: The rate for general purposes can only be imposed by a unanimous vote of the board of supervisors. The taxes are collected by DOR. The statute is silent on lowering or eliminating the tax rate. County excise taxes that are levied for a specific purpose generally require a vote of the people.

STATUTE	PURPOSE	RATE	ESTABLISHED BY	RESTRICTIONS
42-6103	General	Up to .5%	Unanimous vote of the Board of Supervisors (BOS)	Only applies to counties with a population < 1.5 million population.
42-6104	Transportation	.5%	County special election	Maricopa County only – limited to 20 years
42-6106	Transportation	.5%	County special election or general election	Pima County only – rate can only be modified by a vote of the people
42-6107	Transportation	.5%	County special election or general election	All counties except Pima & Maricopa
42-6108.01	Hotels	.055%	Any county election	Pima County only. The rate is 1% of the state transient lodging classification (5.5%) Funds used for tourism.
5-840	Hotels	.055%	Election for the Tourism & Sports Authority	For Tourism & Sport Authority District (Maricopa County). The rate is 1% of the state transient lodging classification (5.5%). Limited to 30 years.
42-6109 & 42-6109.01	Jails	Up to .2%	County general election	Maricopa County only – originally in effect for only 9 years or until $900 M raised and could be used only for capital facilities. Rate can be adjusted by resolution of the BOS. 2002 legislation allowed county to call another election, use funds for M&O and extend tax for 20 years.
42-6111	Capital Projects	Up to .5% when combined with other co. rates	County special election or general election after unanimous vote of the BOS	Applies only to counties with < 2 million population – limited to 20 years

MUNICIPALITIES:

Reliance: According to the Arizona League of Cities and Towns, most cities have a 25 – 45% reliance on sales taxes for their general fund. When combined with the TPT revenue sharing from the state, the reliance is higher. Selected city examples:

City	Local sales tax revenues	% of GF	TPT state shared revenue	% of GF	Total % reliance on sales tax
Phoenix	$335,441,000	42.3%	$108,225,000	13.6%	55.9%
Tucson	$104,096,980	30.8%	$58,013,060	17.2%	48.0%
Mesa	$107,219,000	49.4%	$30,884,000	14.2%	63.6%
Glendale	$42,900,000	35.1%	$17,500,000	14.3%	49.4%
Yuma	$13,833,000	27.8%	$6,039,610	12.2%	40.0%
Flagstaff	$11,432,104	23.4%	$4,121,256	8.4%	31.8%
Sierra Vista	$5,493,136	25.4%	$3,049,062	14.1%	39.5%
Kingman	$8,218,000	35.9%	$1,563,684	6.8%	42.7%

Rates: Arizona municipalities set their own tax rates. The rates currently range from 1% to 3%. (see chart) Some of the rate may be dedicated for specific purposes within the city. Some taxable activities within a city may have a higher rate. For example, most cities tax transient lodging (hotels/motels) at a higher rate. The state does not put any limit on the sales tax rates that are set by the municipalities.

Base: The municipalities have their own sales tax base, referred to as the Model City Tax Code (MCTC). The Municipal Tax Code Commission regulates the provisions of the MCTC and the Commission membership and duties are set forth in state statute.

Procedure for raising/lowering tax rate: The sales tax rates are generally set by the city councils, but may be referred to the voters. Some charter cities require a vote of the people for any tax increases. Those cities that have this provision in their charter would need an election to increase their tax rate.

TAXING SERVICES:

Arizona has a broad TPT base that includes the taxation of some services. There are several other states that tax more services and three states - South Dakota, New Mexico and Hawaii – that tax a wide variety of services. The debate of taxing services has been around since the mid-1980's when Florida drastically expanded it's sales tax to services, but subsequently repealed it due to it's unpopularity and the exodus of service industries that can easily move.

A comprehensive report on the taxation of services by the states is provided in the Federal of Tax Administrators research report *"Sales Taxation of Services: 1996 Update."*

The following chart shows what effect the taxation of services would have on the tax rate in Arizona. These figures are provided by DOR and show how the tax rate will change compared to the 5% rate. See *"Transaction Privilege and Use Tax Expenditures"* provided by DOR for list of services.

Effect of changing the 5% rate for the taxation of services

Tax base expanded to:	revenue neutral	raise $100 M	raise $500 M	raise $1 B
All Services	3.82%	3.93%	4.33%	4.83%
Professional Services	4.37%	4.49%	4.95%	5.5%
Business Services	4.39%	4.5%	4.96%	5.5%
Personal Services	4.9%	5.04%	5.6%	6.2%

ARIZONA TAX RESEARCH ASSOCIATION

State and Local Retail Sales Tax Rates by City

May, 2003

Cities by County	State	County					City	Total Rate
		GF	Road	Jail	Capital	Health		
Apache County								
Eagar	5.60	0.50	-	-	-	-	3.00	**9.10**
St. Johns	5.60	0.50	-	-	-	-	2.00	**8.10**
Springerville	5.60	0.50	-	-	-	-	3.00	**9.10**
Cochise County								
Benson	5.60	0.50	-	-	-	-	2.50	**8.60**
Bisbee	5.60	0.50	-	-	-	-	2.50	**8.60**
Douglas	5.60	0.50	-	-	-	-	2.50	**8.60**
Huachuca City	5.60	0.50	-	-	-	-	1.50	**7.60**
Sierra Vista	5.60	0.50	-	-	-	-	1.50	**7.60**
Tombstone	5.60	0.50	-	-	-	-	2.50	**8.60**
Willcox	5.60	0.50	-	-	-	-	3.00	**9.10**
Coconino County								
Flagstaff	5.60	0.50	-	0.30	0.125	-	1.574	**8.099**
Fredonia	5.60	0.50	-	0.30	0.125	-	2.00	**8.53**
Page	5.60	0.50	-	0.30	0.125	-	2.00	**8.53**
Sedona	5.60	0.50	-	0.30	0.125	-	3.00	**9.53**
Williams	5.60	0.50	-	0.30	0.125	-	3.00	**9.53**
Gila County								
Globe	5.60	0.50	0.50	-	-	-	1.50	**8.10**
Hayden	5.60	0.50	0.50	-	-	-	1.00	**7.60**
Miami	5.60	0.50	0.50	-	-	-	2.50	**9.10**
Payson	5.60	0.50	0.50	-	-	-	2.00	**8.60**
Winkelman	5.60	0.50	0.50	-	-	-	3.50	**10.10**
Graham County								
Pima	5.60	0.50	-	-	-	-	2.00	**8.10**
Safford	5.60	0.50	-	-	-	-	2.00	**8.10**
Thatcher	5.60	0.50	-	-	-	-	2.00	**8.10**
Greenlee County								
Clifton	5.60	0.50	-	-	-	-	2.00	**8.10**
Duncan	5.60	0.50	-	-	-	-	2.00	**8.10**
La Paz County								
Parker	5.60	0.50	-	0.50	-	0.112	2.00	**8.71**
Quartzsite	5.60	0.50	-	0.50	-	0.112	2.50	**9.21**
Maricopa County								
Apache Junction	5.60	-	0.50	0.20	-	-	2.20	**8.50**
Avondale	5.60	-	0.50	0.20	-	-	2.00	**8.30**
Buckeye	5.60	-	0.50	0.20	-	-	2.00	**8.30**
Carefree	5.60	-	0.50	0.20	-	-	2.00	**8.30**
Cave Creek	5.60	-	0.50	0.20	-	-	2.50	**8.80**
Chandler	5.60	-	0.50	0.20	-	-	1.50	**7.80**
El Mirage	5.60	-	0.50	0.20	-	-	3.00	**9.30**
Fountain Hills	5.60	-	0.50	0.20	-	-	2.60	**8.90**
Gila Bend	5.60	-	0.50	0.20	-	-	3.00	**9.30**
Gilbert	5.60	-	0.50	0.20	-	-	1.50	[illegible]
Glendale	5.60	-	0.50	0.20	-	-	1.80	**8.10**
Goodyear	5.60	-	0.50	0.20	-	-	2.00	**8.30**
Guadalupe	5.60	-	0.50	0.20	-	-	2.00	**8.30**
Litchfield Park	5.60	-	0.50	0.20	-	-	2.00	**8.30**
Mesa	5.60	-	0.50	0.20	-	-	1.50	**7.80**
Paradise Valley	5.60	-	0.50	0.20	-	-	1.40	**7.70**
Peoria	5.60	-	0.50	0.20	-	-	1.50	**7.80**
Phoenix	5.60	-	0.50	0.20	-	-	1.80	**8.10**

Cities by County	State	County					City	Total Rate
		GF	Road	Jail	Capital	Health		
Maricopa County								
Queen Creek	5.60	-	0.50	0.20	-	-	2.00	8.30
Scottsdale	5.60	-	0.50	0.20	-	-	1.40	7.70
Surprise	5.60	-	0.50	0.20	-	-	2.00	8.30
Tempe	5.60	-	0.50	0.20	-	-	1.80	8.10
Tolleson	5.60	-	0.50	0.20	-	-	2.00	8.30
Wickenburg	5.60	-	0.50	0.20	-	-	1.00	7.30
Youngtown	5.60	-	0.50	0.20	-	-	2.00	8.30
Mohave County								
Bullhead City	5.60	0.25	-	-	-	-	2.00	7.85
Colorado City	5.60	0.25	-	-	-	-	2.00	7.85
Kingman	5.60	0.25	-	-	-	-	2.00	7.85
Lake Havasu City	5.60	0.25	-	-	-	-	2.00	7.85
Navajo County								
Holbrook	5.60	0.50	-	-	-	-	3.00	9.10
Pinetop-Lakeside	5.60	0.50	-	-	-	-	2.50	8.60
Show Low	5.60	0.50	-	-	-	-	2.00	8.10
Snowflake	5.60	0.50	-	-	-	-	2.00	8.10
Taylor	5.60	0.50	-	-	-	-	2.00	8.10
Winslow	5.60	0.50	-	-	-	-	3.00	9.10
Pima County								
Marana	5.60	-	-	-	-	-	2.00	7.60
Oro Valley	5.60	-	-	-	-	-	2.00	7.60
Sahuarita	5.60	-	-	-	-	-	2.00	7.60
South Tucson	5.60	-	-	-	-	-	2.50	8.10
Tucson	5.60	-	-	-	-	-	2.00	7.60
Pinal County								
Apache Junction	5.60	0.50	0.50	-	-	-	2.20	8.80
Casa Grande	5.60	0.50	0.50	-	-	-	1.80	8.40
Coolidge	5.60	0.50	0.50	-	-	-	2.00	8.60
Eloy	5.60	0.50	0.50	-	-	-	3.00	9.60
Florence	5.60	0.50	0.50	-	-	-	2.00	8.60
Kearny	5.60	0.50	0.50	-	-	-	2.00	8.60
Mammoth	5.60	0.50	0.50	-	-	-	2.00	8.60
Superior	5.60	0.50	0.50	-	-	-	2.00	8.60
Winkelman	5.60	0.50	0.50	-	-	-	3.50	10.10
Santa Cruz County								
Nogales	5.60	0.50	-	-	-	-	1.25	7.35
Patagonia	5.60	0.50	-	-	-	-	3.00	9.10
Yavapai County								
Camp Verde	5.60	0.50	-	0.20	-	-	2.00	8.30
Chino Valley	5.60	0.50	-	0.20	-	-	2.00	8.30
Clarkdale	5.60	0.50	-	0.20	-	-	2.25	8.55
Cottonwood	5.60	0.50	-	0.20	-	-	2.20	8.50
Jerome	5.60	0.50	-	0.20	-	-	3.00	9.30
Prescott	5.60	0.50	-	0.20	-	-	2.00	8.30
Prescott Valley	5.60	0.50	-	0.20	-	-	2.33	8.63
Sedona	5.60	0.50	-	0.20	-	-	3.00	9.30
Yuma County								
San Luis	5.60	0.50	-	0.50	0.50	-	2.50	9.60
Somerton	5.60	0.50	-	0.50	0.50	-	2.50	9.60
Wellton	5.60	0.50	-	0.50	0.50	-	2.50	9.60
Yuma	5.60	0.50	-	0.50	0.50	-	1.70	8.80

Sources: League of Arizona Cities & Towns; Arizona Department of Revenue

TABLE 24
STATE TRANSACTION PRIVILEGE AND SEVERANCE TAX DISTRIBUTION TO COUNTIES
FISCAL YEAR 1997-98 THROUGH FISCAL YEAR 2001-02

COUNTY	FY1997-98	FY1998-99	FY1999-00	FY2000-01	FY2001-02	% CHANGE FROM FY2000/01
Apache	$3,384,940	$3,565,934	$5,473,442	$4,445,431	$3,808,535	-14.3%
Cochise	7,886,873	8,390,958	9,229,981	9,594,853	9,111,850	-5.0%
Coconino	12,183,683	12,695,530	13,841,588	13,978,278	13,695,680	-2.0%
Gila	4,156,713	4,067,599	3,882,098	4,443,907	4,087,916	-8.0%
Graham	2,139,621	2,247,541	2,412,735	2,462,318	2,366,529	-3.9%
Greenlee	3,813,256	3,226,878	3,098,540	3,003,365	1,794,359	-40.3%
La Paz	1,316,162	1,421,105	1,486,269	1,495,379	1,525,956	2.0%
Maricopa	256,008,018	277,695,556	306,464,900	322,426,596	325,710,325	1.0%
Mohave	11,639,836	12,194,408	12,938,817	13,012,998	13,293,460	2.2%
Navajo	6,690,773	7,136,959	7,748,173	7,932,049	7,990,618	0.7%
Pima	65,670,660	70,057,426	76,273,737	79,516,015	76,759,008	-3.5%
Pinal	10,457,557	11,018,980	11,582,587	12,511,593	12,467,448	-0.4%
Santa Cruz	2,793,965	2,968,377	3,180,054	3,346,986	3,275,822	-2.1%
Yavapai	13,324,088	14,218,059	16,154,370	16,629,440	16,504,368	-0.8%
Yuma	9,834,655	10,495,286	11,358,869	11,861,866	12,675,627	6.9%
	$411,300,801	**$441,400,596**	**$485,126,158**	**$506,661,075**	**$505,067,501**	-0.3%

Figures may not add to totals due to rounding.

TABLE 25
STATE TRANSACTION PRIVILEGE AND SEVERANCE TAX
DISTRIBUTION TO MUNICIPALITIES
FISCAL YEAR 2001-02

CITIES	AMOUNT	COUNTY TOTAL
APACHE		
Eagar	$310,785	
St. Johns	243,343	
Springerville	160,531	$714,658
COCHISE		
Benson	363,032	
Bisbee	469,298	
Douglas	1,102,889	
Huachuca City	134,933	
Sierra Vista	2,910,958	
Tombstone	115,899	
Willcox	287,667	5,384,675
COCONINO		
Flagstaff	4,076,034	
Fredonia	79,835	
Page	524,704	
Williams	219,006	4,899,579
GILA		
Globe	576,874	
Hayden	68,738	
Miami	149,189	
Payson	1,049,563	
Winkelman	34,138	1,878,502
GRAHAM		
Pima	153,273	
Safford	711,422	
Thatcher	309,937	1,174,632
GREENLEE		
Clifton	200,049	
Duncan	62,573	262,622
LA PAZ		
Parker	241,970	
Quartzsite	258,461	500,430
MARICOPA		
Avondale	2,765,159	
Buckeye	654,782	
Carefree	225,556	
Cave Creek	287,281	
Chandler	13,607,407	
El Mirage	586,353	
Fountain Hills	1,559,318	
Gila Bend	152,580	
Gilbert	8,453,298	
Glendale	16,861,747	
Goodyear	1,457,290	
Guadalupe	402,872	
Litchfield Park	293,600	
Mesa	30,544,828	
Paradise Valley	1,052,954	
Peoria	8,350,576	
Phoenix	101,800,295	
Queen Creek	$332,593	
Scottsdale	15,620,534	
Surprise	2,377,160	
Tempe	12,223,711	
Tolleson	383,299	
Wickenburg	391,621	
Youngtown	231,952	$220,616,766
MOHAVE		
Bullhead City	2,602,254	
Colorado City	256,919	
Kingman	1,546,526	
Lake Havasu City	3,231,760	7,637,459
NAVAJO		
Holbrook	378,906	
Pinetop-Lakeside	276,030	
Show Low	592,980	
Snowflake	343,690	
Taylor	244,744	
Winslow	733,615	2,569,965
PIMA		
Marana	1,044,631	
Oro Valley	2,288,695	
Sahuarita	249,830	
South Tucson	423,062	
Tucson	37,505,234	41,511,452
PINAL		
Apache Junction	2,451,601	
Casa Grande	1,943,772	
Coolidge	599,993	
Eloy	799,502	
Florence	1,113,215	
Kearny	173,309	
Mammoth	135,780	
Superior	250,755	7,467,926
SANTA CRUZ		
Nogales	1,608,868	
Patagonia	67,890	1,676,758
YAVAPAI		
Camp Verde	728,298	
Chino Valley	603,768	
Clarkdale	263,701	
Cottonwood	707,338	
Jerome	25,353	
Prescott	2,615,277	
Prescott Valley	1,813,617	
Sedona	785,400	7,542,752
YUMA		
San Luis	1,180,720	
Somerton	559,921	
Wellton	140,944	
Yuma	5,973,339	7,854,924
TOTAL	**$311,693,101**	**$311,693,101**

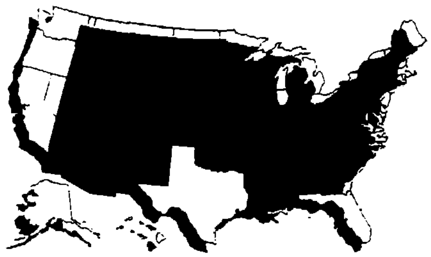
City Distributions are based on relative population.
Figures may not add to total due to rounding.

TPT Revenue Sharing to Counties
FY 2002-2003
preliminary figures

County	FY03
APACHE	3,878,392.37
COCHISE	9,344,322.77
COCONINO	13,903,148.98
GILA	4,058,749.59
GRAHAM	2,381,978.69
GREENLEE	1,750,472.88
LA PAZ	1,523,806.14
MARICOPA	329,197,351.73
MOHAVE	13,839,978.79
NAVAJO	8,287,880.01
PIMA	77,729,082.91
PINAL	13,328,797.90
SANTA CRUZ	3,357,504.83
YAVAPAI	17,000,258.92
YUMA	13,121,507.53
TOTAL	512,703,234.04

TPT Revenue Sharing to Cities & Towns
FY 2002-2003
preliminary figures

APACHE		*GREENLEE*		*MOHAVE*		*SANTA CRUZ*	
Eagar	315,412	Clifton	203,027	Bullhead City	2,640,999	Nogales	1,632,823
Springerville	154,226	Duncan	63,505	Colorado City	260,745	Patagonia	68,901
St. Johns	263,061	TOTAL	266,532	Kingman	1,569,552	TOTAL	1,701,724
TOTAL	732,699			Lake Havasu City	3,279,879		
		LA PAZ		TOTAL	7,751,175	*YAVAPAI*	
COCHISE		Parker	245,573			Camp Verde	739,142
Benson	368,437	Quartzsite	262,309	*NAVAJO*		Chino Valley	614,984
Bisbee	476,286	TOTAL	507,881	Holbrook	384,548	Clarkdale	267,627
Douglas	1,177,950			Pinetop-Lakeside	280,140	Cottonwood	717,869
Huachuca City	136,942	*MARICOPA*		ShowLow	601,809	Jerome	25,730
Sierra Vista	2,954,300	Avondale	2,806,331	Snowflake	348,807	Prescott	2,654,216
Tombstone	117,625	Buckeye	664,532	Taylor	248,388	Prescott Valle	1,840,621
Willcox	291,950	Carefree	228,914	Winslow	744,538	Sedona	797,094
TOTAL	5,523,489	Cave Creek	291,559	TOTAL	2,608,230	TOTAL	7,657,284
		Chandler	13,810,012				
COCONINO		El Mirage	595,083	*PIMA*		*YUMA*	
Flagstaff	4,136,724	Fountain Hills	1,582,535	Marana	1,060,185	San Luis	1,198,300
Fredonia	81,023	Gila Bend	154,851	Oro Valley	2,322,772	Somerton	568,258
Page	532,517	Gilbert	8,579,161	Sahuarita	253,550	Wellton	143,042
Williams	222,267	Glendale	17,112,806	South Tucson	429,361	Yuma	6,062,278
TOTAL	4,972,530	Goodyear	1,478,988	Tucson	38,063,659	TOTAL	7,971,878
		Guadalupe	408,870	TOTAL	42,129,527		
GILA		Litchfield Park	297,972			**TOTAL**	**316,405,353**
Globe	585,464	Mesa	30,999,618	*PINAL*			
Hayden	69,761	Paradise Valley	1,068,631	Apache Junction	2,488,103		
Miami	151,410	Peoria	8,474,910	Casa Grande	1,972,714		
Payson	1,065,190	Phoenix	103,316,027	Coolidge	608,926		
Winkleman	34,646	Queen Creek	337,545	Eloy	811,406		
TOTAL	1,906,472	Scottsdale	15,853,113	Florence	1,132,895		
		Surprise	2,412,554	Kearny	175,889		
GRAHAM		Tempe	12,405,713	Mammoth	137,802		
Pima	155,555	Tolleson	389,006	Superior	254,488		
Safford	722,014	Wickenburg	397,452	TOTAL	7,582,224		
Thatcher	314,552	Youngtown	235,405				
TOTAL	1,192,122	TOTAL	223,901,587				



Streamlined Sales Tax Project

Executive Summary

February 2003

The Streamlined Sales Tax Project is an effort created by state governments, with input from local governments and the private sector, to simplify and modernize sales and use tax collection and administration. The Project's proposals include tax law simplifications, more efficient administrative procedures, and emerging technologies to substantially reduce the burden of tax collection. The Project's proposals are focused on improving sales and use tax administration systems for both Main Street and remote sellers for all types of commerce.

Thirty-nine states and the District of Columbia are involved in the Project. Thirty-six states and the District of Columbia are voting participants in the Project because their legislators have enacted enabling legislation or their governors have issued executive orders or similar authorizations. Three states are non-voting participants in the work of the Project because they do not have the formal commitment of the state executive or legislative branches, but are still participating. Forty-five states and the District of Columbia impose a sales and use tax.

The Project was organized in March 2000. The Project is conducting its work through a steering committee with co-chairs, four work groups, and a number of sub-groups. Project participants are generally state revenue department administrators but there are also representatives of state legislatures and local governments. Businesses — including national retailers, trade associations, manufacturers, direct marketers, telecommunications companies, leasing companies, technology companies, printers, accounting firms, and others — have actively participated in the Project by offering expertise and input, reviewing proposals, suggesting language, and testifying at public hearings.

The goal of the Streamlined Sales Tax Project is to provide states with a Streamlined Sales Tax System that includes the following key features:

- **Uniform definitions within tax laws.** Legislatures still choose what is taxable or exempt in their state. However, participating states will agree to use the common definitions for key items in the tax base and will not deviate from these definitions. As states move from their current definitions to the Project's definitions, a certain amount of impact on state revenues is inevitable. However, it is the intent of the Project to provide states with the ability to closely mirror their existing tax bases through common definitions.

- **Rate simplification.** States will be allowed one state rate and a second state rate in limited circumstances (food and drugs). Each local jurisdiction will be allowed one local rate. A state or local government may not choose to tax telecommunications services, for example, at one rate and all other items of tangible personal property or taxable services at another rate. State and local governments will accept responsibility for notice of rate and boundary changes at restricted times.

- **State level tax administration of all state and local sales and use taxes.** Businesses will no longer file tax returns with each local government within which it conducts business in a state. Each state will provide a central point of administration for all state and local sales and use taxes and the distribution of the local taxes to the local governments. A state and its local governments will use common tax bases.

- **Uniform sourcing rules.** The states will have uniform and simple rules for how they will source transactions to state and local governments. The uniform rules will be destination/delivery based and uniform for tangible personal property, digital property, and services.

- **Simplified exemption administration for use- and entity-based exemptions.** Sellers are relieved of the "good faith" requirements that exist in current law and will not be liable for uncollected tax. Purchasers will be responsible for paying the tax, interest and penalties for claiming incorrect exemptions. States will have a uniform exemption certificate in paper and electronic form.

- **Uniform audit procedures.** Sellers who participate in one of the certified Streamlined Sales Tax System technology models will either not be audited or will have limited scope audits, depending on the technology model used. The states may conduct joint audits of large multi-state businesses.

- **State funding of the system.** To reduce the financial burdens on sellers, states will assume responsibility for funding some of the technology models. The states are also participating in a joint business – government study of the costs of collection on sellers.

The Project proposes that states change their sales and use tax laws to conform with the simplifications as proposed by the Project. Thus, the simplifications would apply to all sellers. Sellers who do not have a physical presence or "nexus" are not required to collect sales and use taxes unless Congress chooses to require collection from all sellers for all types of commerce. Sellers without a physical presence can volunteer to collect under the proposed simplifications. Registration by sellers to voluntarily collect sales and use taxes will not infer that the business must pay business activity taxes, such as the corporate franchise or income tax.

The Streamlined Sales Tax System will provide sellers the opportunity to use one of three technology models. A seller may use Model 1 where a Certified Service Provider, compensated by the states, will perform all of the seller's sales tax functions. A seller may use Model 2, a Certified Automated System, to perform only the tax calculation function. A larger seller with nationwide sales that has developed its own proprietary sales tax software may use Model 3 and have its own system certified by the states collectively. However, some sellers may choose to continue to use their current systems and still enjoy the benefits of the Project's simplifications.

The Streamlined Sales Tax Project envisions two components to the legislation necessary to accomplish the Project's goals. First, states would adopt enabling legislation referred to as the Uniform Sales and Use Tax Administration Act ("Act"). The Act allows the state to enter into an agreement with one or more states to simplify and modernize sales and use tax administration in order to reduce the burden of tax compliance for all sellers and all types of commerce. The Act does not require any amendments to a state's sales and use tax law.

Secondly, states would amend or modify their sales and use tax laws to achieve the simplifications and uniformity required by the participating states working together. The Project refers to this legislation as the Streamlined Sales and Use Tax Agreement ("Agreement"). Some states will require only minor changes to current law to implement the requirements of the Agreement. Other states with more complicated sales tax laws may require significant changes to current law to be in accord with the Agreement.

A certificate of compliance will document each state's compliance with the provisions of the Agreement and cite applicable statutes, rules or regulations, or other authorities supporting such compliance. Public notice and comment will be provided before a state becomes part of the interstate Agreement. A state is in compliance with the Agreement if the effect of the state's laws, rules or regulations, and policies is substantially compliant with each of the requirements of the Agreement. If a state is found to be out of compliance with the Agreement, it will not be accepted into the interstate Agreement or will be sanctioned or expelled by the other participating states. In a voluntary system, sellers who are voluntarily collecting sales taxes for participating states may decide to no longer collect for the expelled state. Also, that state may not have a vote on changes in the Agreement.

A governing board will be comprised of representatives of each member state of the Agreement. Each member state is entitled to one vote on the governing board. The governing board is responsible for interpretations of the Agreement, amendments to the Agreement, and issue resolution. A State and Local Government Advisory Council and a Business and Taxpayer Advisory Council from the private sector will advise the governing board.

On November 12, 2002, thirty states and the District of Columbia approved the interstate Agreement provisions. States will move forward in 2003 and enact the conforming legislation. The Agreement will become effective when at least ten states with twenty percent of the total population of all states imposing a state sales tax have enacted the conforming legislation and are found to be in compliance with the requirements of the Agreement.

It's anticipated that states that enact the conforming legislation and are found to be in compliance with the Agreement will continue as the governing states of the interstate Agreement of the future.

The project website is www.streamlinedsalestax.org.

Appendix E

Miscellaneous Tax and Budget Information

Budget Stabilization Fund

Tax Reform for Arizona Citizens Committee

October 22, 2003

JLBC Staff

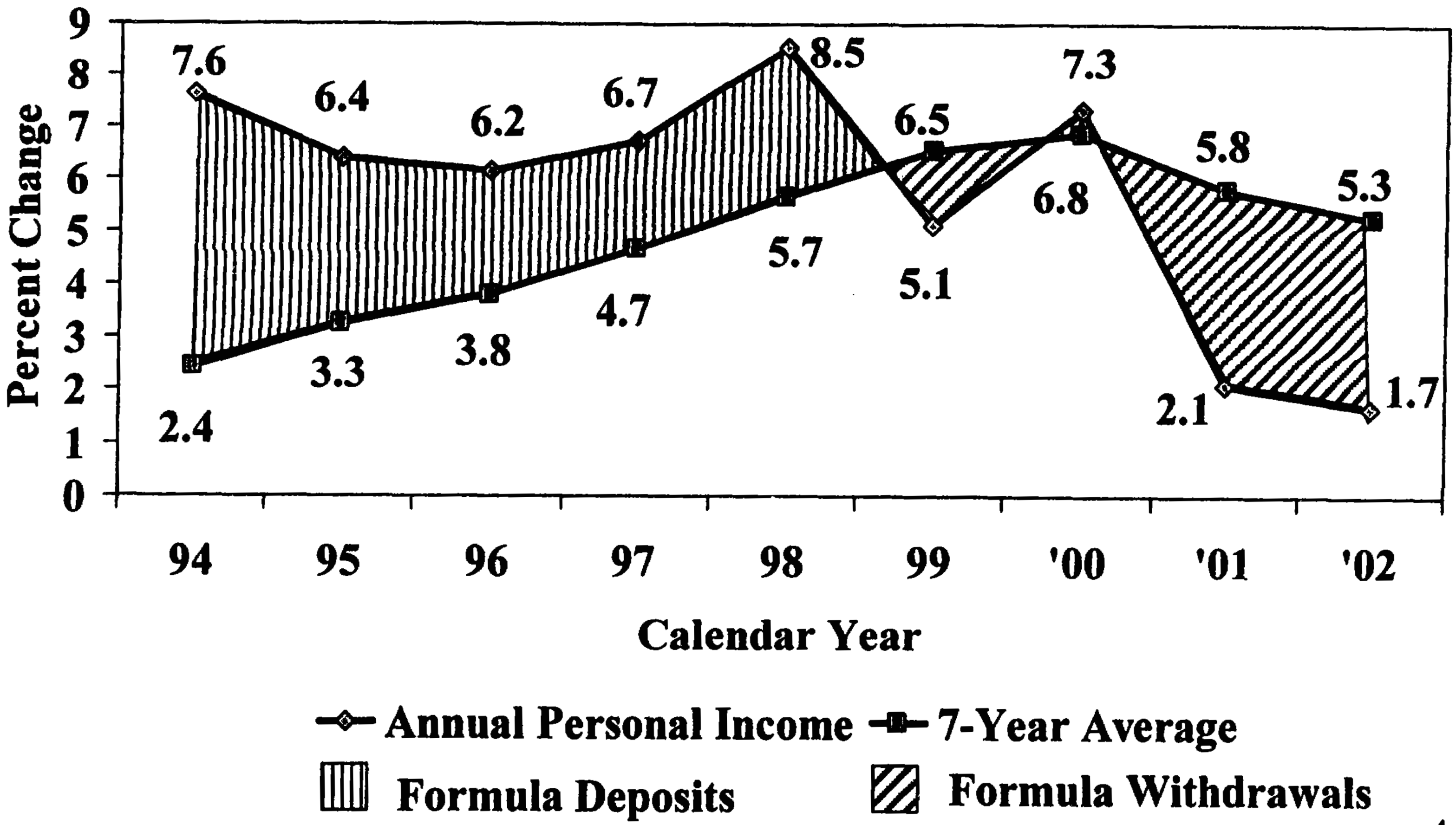
Background

- The BSF was created in 1990 to stabilize the state budget from the ups and downs of the business cycle.
- Withdrawals and deposits from the fund are governed by a statutory formula – but require legislative authorization.
- Maximum BSF balance is limited to 7% of General Fund revenues.

BSF Formula

- Deposits occur when annual personal income growth exceeds the 7-year average.
- Withdrawals occur when annual personal income growth is both less than the 7-year average and less than 2%.
- Size of deposit/withdrawal is tied to gap between personal income and 7-year average – if personal income were 6% and 7-year average was 5%, 1% of General Fund revenues would be deposited.

Annual Personal Income vs. 7-Year Average



Comparison to Other States

- In 1995, all but 5 states had a rainy day fund.
- According to NCSL, 6 states have established their BSF in their state constitution.
- 7 states have a BSF cap of more than 7% of General Fund revenues.
- At least 10 states do not use a formula for making BSF deposits.

History of BSF

- Created in 1990, first funded in 1994.
- Full formula deposit made only once. 1995
- Maximum size of the BSF was $405 million in FY 2000 (6.8% of General Fund).
- Used for alternative fuels ($16 million of $130 million repaid) and Arizona State Hospital ($40 million of $77 million repaid).
- $280 million used to balance budget since FY 2002.

Summary of Deposits and Withdrawals

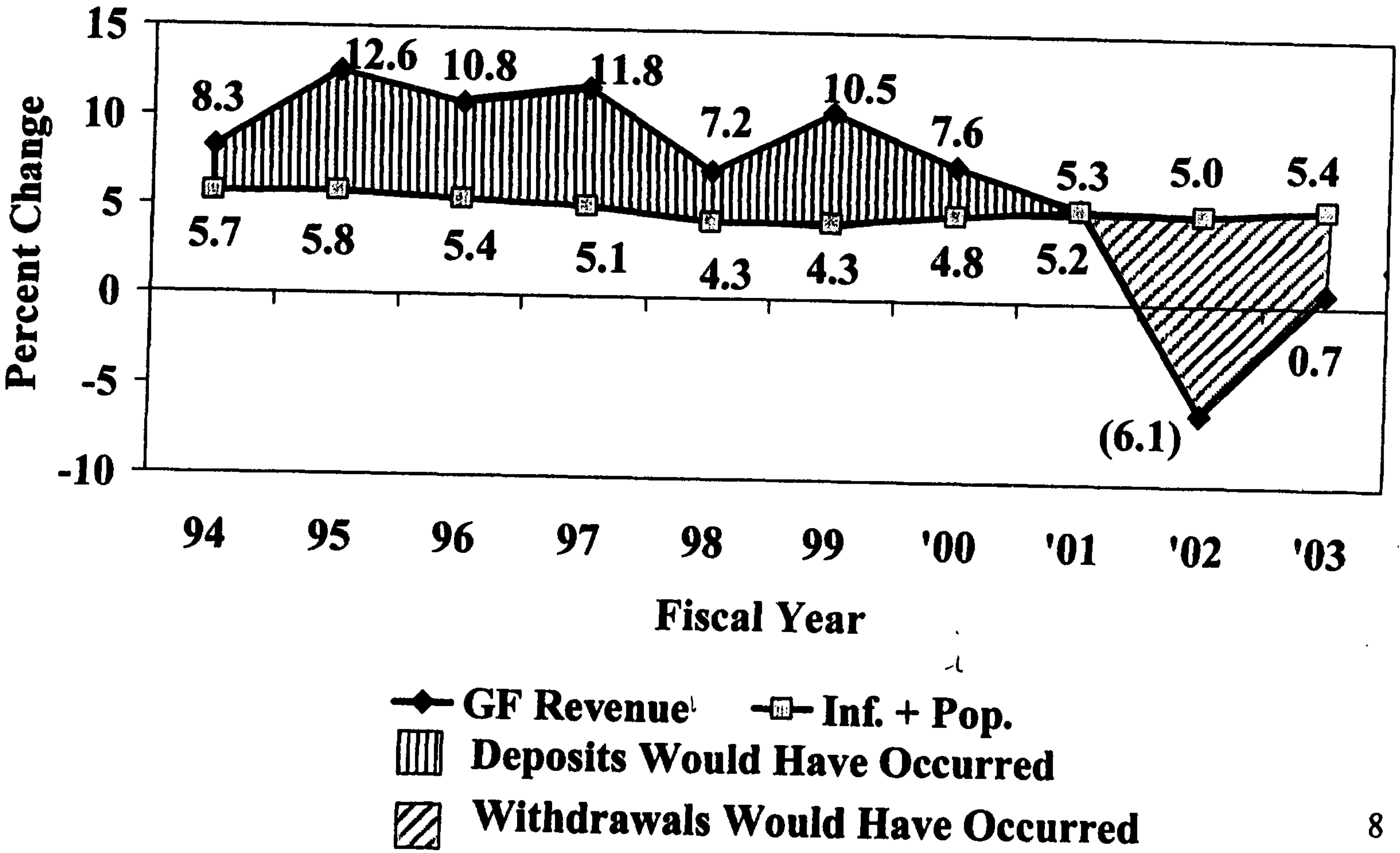
	Formula Recommendation	Actual Deposit/(Withdrawal)	Balance [1/]
FY 1994	$78,346,000	$42,000,0000	$42,200,000
FY 1995	178,817,000	178,816,944	223,187,000
FY 1996	223,196,380	0	233,130,000
FY 1997	127,766,000	0	245,810,900
FY 1998	60,478,000	30,000,000	291,670,000
FY 1999	104,588,000	75,115,000	383,560,400
FY 2000	0	0	405,960,500
FY 2001	28,013,200	(33,425,300) [2/]	391,523,800
FY 2002	0	(332,490,800) [2/]	64,719,300
FY 2003	(224,085,400)	(53,028,700)	13,765,700 [3/]

1/ The balance does not equal the amounts deposited and withdrawn because the fund also earns interest and realizes some equity gains.

2/ Of these amounts, a total of $130 million has been set aside for payment of alternative fuel income tax credits.

3/ The balance remaining in the fund at the end of FY 2003 has been reserved for future alternative fuel costs.

An Alternative BSF Formula:
Compares Revenue to Population and Inflation Growth



Real Estate Transfer Taxes
November 2001
NCSL Study

The National Conference of State Legislators provided the following 50-state information. Arizona is one of thirteen states that do not provide for these taxes. The full report is approximately 33 pages and contains specific state-by-state information. The full report will be provided to you upon request.

REAL ESTATE TRANSFER TAXES

State	**Transfer Fee**	**Transfer Fee Rate**
Alabama	Deeds $.50/$500 Mortgages $.15/$100	0.1% 0.15%
Alaska	None	
Arizona	$2 per deed or contract	
Arkansas	$3.30/$1,000	0.33%
California (local)	$.55/$500	0.11%
Colorado	$.01/$100	0.01%
Connecticut	Varies	0.5% up to $800K and 1% of value over $800K; plus 0.11%
Delaware		1.5% - 2%
District of Columbia		1.1%
Florida	$.70/$100	0.7%
Georgia	$.10/$100	0.1%
Hawaii	$.10/$100	0.1%
Idaho	None	
Illinois	Chicago - $3.75/$500 Cook County - $.25/$500	0.75% 0.05%
Indiana	None	
Iowa	$.80/$500	0.16%
Kansas	Mortgage $.26/$100	0.26%
Kentucky	$.50/$500	0.1%
Louisiana	None	
Maine	$2.20/$500	.44%
Maryland		0.5% (0.25% for first-time buyers)
Massachusetts	$2/$500	0.456% (0.4% plus 14% surtax); also $10-$20 surcharge
Michigan	State - $3.75/$500 County - $.55/$500 - $.75/$500 depending on population	0.75% 0.11% - 0.15% depending on population
Minnesota	$1.65/$500	0.33%
Mississippi	None	
Missouri	None	
Montana	None	
Nebraska	$1.75/$1,000	0.175%
Nevada	$.65/$500 up to 400K county population $1.25/$500over 400K county population	0.13% up to 400K county pop. 0.25% over 400K county pop.
New Hampshire	$.75/$100	0.75%
New Jersey	$1.75/$500 up to $150K $2.50/$500 over $150K	0.35% up to $150K 0.5% over $150K

		County up to 0.1% additional tax
New Mexico	None	
New York	Property transfer - $2/$500 up to $1 million; 1% additional over $1 million Mortgage recording New York City	0.4% up to $1 million value; addl. 1.0% over $1 million 1.0% 1% up to $500K value; 1.425% over $500K
North Carolina	$1/$500	0.2%
North Dakota	None	
Ohio		0.1% plus 0.3% local
Oklahoma	$.75/$100	0.75%
Oregon	None	
Pennsylvania	Local varies	1% plus $2
Rhode Island	$1.40/$500	0.28%
South Carolina	$1.85/$500 ($1.30 state, $.55 county)	0.37% (state-county combination)
South Dakota	$.50/$500	0.1%
Tennessee	$.37/$100	.37%
Texas	None	
Utah	None	
Vermont	Property Transfer Tax Tax on gains; varies with length of time owned	1.25% of the value of the property transfered unless the property will be used as a principal residence in which case, the tax is .5% on the first $100,000 of value and 1.25% on any value over $100,000. There are other exemptions as well.
Virginia	$.15/$100 on sales up to $10 million; varies thereafter	0.03% - 0.15% depending upon sales price
Washington		1.28% of sales price plus local taxes
West Virginia	$1.65/$500 ($1.10 state, $.55 county)	0.33% (state-county combination)
Wisconsin	$.30/$100	0.3%
Wyoming	None	

Sources: *Assessment Journal*, International Association of Assessing Officers, November/December 1997; Commerce Clearing House *State Tax Guide* 2001. Compiled by National Conference of State Legislatures Fiscal Affairs Program.

Joint Legislative Budget Committee
Staff Memorandum

1716 West Adams
Phoenix, Arizona 85007

Telephone: (602) 542-5491
Facsimile: (602) 542-1616

DATE: August 22, 2003

TO: Kitty Decker, Research Analyst

FROM: Hans Olofsson, Senior Economist HO

SUBJECT: ALTERNATIVE REVENUE SOURCES

As you requested, we have prepared an analysis to determine the amount of monies that could be raised by imposing either a statewide development impact fee or a real estate transfer tax. To this end, the JLBC Staff estimates that a statewide development fee of $1,000 per single-family unit (as suggested) would generate $53 million in FY 2004. A recent analysis prepared for the Citizens' Finance Review Commission (CFRC) suggests that a real estate transfer tax in Arizona could generate an amount between $49 million and $270 million in FY 2004. It should be noted, however, that the revenue estimates vary considerably under different fee and tax rate assumptions.

Development Impact Fee

Impact fees are used to assure that new residential developments share or assume responsibility for the infrastructure necessary to support them. Impact fees can also be used to fund public services such as libraries and fire protection.

Many of the larger cities in Arizona levy impact fees on new developments. For example, the City of Phoenix is currently charging impact fees in 6 of its 14 village areas. The net development impact fee for single-family units in these areas range from $1,868 in the Ahwatukee Foothills to $10,354 in the Black Canyon Corridor.

Many cities also charge impact fees for multi-family units and non-residential projects. However, the net development impact fee for such property does not solely depend on the location but also on other factors such as square footage and acreage and is therefore more difficult to compute. Because such data is not readily available, we omitted such property from our analysis. Instead, we only considered the amount of revenues that could be generated by single-family homes.

Data from the Arizona Real Estate Center indicates that 55,600 single-family housing units were authorized in Arizona in 2002. The Arizona Blue Chip Forecast Panel expects this figure to decline to 53,000 in 2003. Using the Arizona Blue Chip projection, we therefore estimate that if the state charges a $1,000 development fee for each single-family building permit issued, $53 million could be raised in FY 2004. Similarly, a statewide development fee of $2,000 would generate an estimated $106 million in new revenues.

It should be noted, however, that higher impact fees are likely to have an adverse effect on new home construction since some potential buyers will be priced out of the market. Such "dynamic" estimates would require a separate analysis, however.

(Continued)

Real Estate Transfer Tax

Real estate transfer taxes (RETT) are taxes imposed on the transfer of title of real property. In most cases it is an ad valorem tax that is based on the value of the property transferred. According to the National Conference of State Legislators (NCSL), only 13 states, including Arizona, are currently not imposing this tax. Generally, RETT applies to the transfer of both residential and commercial real estate. The rate varies widely by state, from 0.01% in Colorado to 2% in Delaware. Generally, certain categories of transactions are exempt from RETT, such as transfers between spouses or between parents and children. Some states also exempt a specified amount of the property's value from taxation (e.g., the first $100,000 of the property's sales price).

A recent report co-authored by Leezie Kim (CFRC) and Tom Rex (ASU) shows that a real estate transfer tax in Arizona could bring in between $49 million and $270 million in new revenues for the state. These estimates were computed based on 11,001 residential and 478 commercial real estate transactions in Maricopa County in March 2003. Each recorded transaction included information regarding property characteristics, sales price, etc. The statewide estimate was calculated by applying U.S. Census data to the Maricopa estimate. The March estimate was then annualized to obtain a fiscal year impact. The estimated tax collections were calculated under 6 different sets of tax rates and exemptions, as shown below.

Estimated Real Estate Transfer Taxes Collected in Arizona in FY 2004

Scenario	Tax Rate	Exemption	Taxes Collected
1	0.25%	None	$125 million
2	0.25%	First $50,000 of Sales Price	$ 92 million
3	0.25%	First $100,000 of Sales Price	$ 67 million
4	0.25%	First $150,000 of Sales Price	$ 49 million
5	1.00%	First $100,000 of Sales Price	$270 million
6	(A) 0.25% of Sales Price between $100,000 and $250,000. (B) 1.00% of Sales Price Exceeding $250,000.	First $100,000 of Sales Price	$165 million

As the table above demonstrates, the RETT revenue estimate is highly sensitive to both the tax rate and exemption amount assumed. Under scenario 4, which exempts the first $150,000 of the sales price from taxation and then applies a 0.25% tax on the remaining amount, the state would only collect an estimated $49 million in FY 2004. Scenario 5, which only exempts the first $100,000 of the sales price but applies a much higher tax rate (1.00%), would generate $270 million in new revenues. For the JLBC Staff to produce its own estimates independent of the CFRC, individual transaction data would be required. However, such data is currently not available.

If you have any questions, please call me at 542-8970.

HO:ss

xc: Richard Stavneak, Director

League of Arizona Cities & Towns 2003 Municipal Impact/ Development Fee Survey

City/Town	Impact Fees	One Fee Schedule	Year Effective	Have fees been updated	Dates Fees Updated	Escalation Element	Types of inflationary adjustment factors	Fire	Police	Library	Parks	Public Facilities	General Government	Administration Charges	Arterial Street/Transportation	Traffic Signal	Sanitation/Garbage Collection	Water	Water Resources	Waste Water	Reclaimed Water	Sewer Tap	Sewer Development	Utility Deposits	School Impact Fee	Other	Total Impact Fee
Apache Junction	Y	Y	1997	Y	Aug-03	Y	CPI- Western States	$0	$133	$262	$564	$83	$0	$0	$1,485	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$2,527.00
Avondale	Y	Y	1996	Y	Oct-03	N	N/A	$489	$187	$264	$791	$0	$585	$0	$873	$0	$0	$3,289	$0	$267	$0	$0	$3,254	$0	$0	$0	$9,999.00
Benson	Y	N	1999	Y	Jul-03	N	N/A	$440		$0	$245	$0	$0	$0	$0	$0	$0	$600	$0	$600	$0	$0	$0	$0	$0	$ 500 flat rate for units in impact fee in-fill zone	$2,045.00
Bisbee	N																										
Buckeye	Y	Y	2001	N	N/A	N	N/A	$379	$0	$0	$0	$0	$0	$0	$0	$0	$0	$1,331	$0	$3,252	$0	$0	$0	$0	$0	$0	$4,962.00
Bullhead City	Y	N	Various	Y	May-03	N	N/A	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$590	$0	$0	$100	$482	$90	$0	Sewer development only for one development	$1,262.00
Camp Verde	N																										
Carefree																											
Casa Grande	Y	Y	2001	N	n process	Y	CPI & ENR	$331	$236	$209	$519	$0	$116	$0	$96		$0	$0	$0	$0	$0	$0	$1,416	$0	$0	$0	$2,925.00
Cave Creek	Y	Y	2000	Y	Jun-00	N	N/A	$0	$0	$0	$300	$760	$0	$0	$250	$0	$0	$0	$0	$1,635	$0	$0	$0	$0	$0	$0	$2,945.00
Chandler	Y	Y	1997	Y	Mar-02	N	N/A	$108	$163	$70	$696	$0	$237	$0	$1,574*	$15*	$148	$1,514	$595*		$899					Fee May or May Not Be Assessed Based on Location	$7,201* if water resource and arterial street fee apply
Chino Valley	N																										
Clarkdale																											
Clifton	N																					$175					$175.00
Colorado City																											
Coolidge	N																										
Cottonwood																											
Douglas	N																										
Duncan	N																										
Eager																											
El Mirage																											
Eloy	Y	Y	2002	In Process		N	N/A	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$1,000	$0	$1,008	$0	$0		$0	$0	$0	$2,008.00
Flagstaff	Y	Y	Not Provided	Y	Jan-03	Y	N/A	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$1,440	$0	$0	$0	$275	$1,475	$25	$0	$0	$4,690.00
Florence	N*					N	N/A	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$900	$0	$680	$0	$0	$0	$0	$0	$0	$1,580* Proposed Impact Fees
Fountain Hills	Y	Y	2001	N	N/A	N	N/A	$0	$32	$0	$1,130	$0	$488	$0	$609	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$3,495.00
Fredonia																											
Gila Bend	N																										
Gilbert	Y	Y	1997	Y	Jan-03	N	N/A	$334	$395	$0	$1,015	$0	$332	$0	$0	$143	$0	$2,463	$316	$2,463	$0	Included with wastewater		$0	$0	$0	$7,560.00
Glendale	Y	Y	1997	Y	Jan-02	N	N/A	$339	$359	$514	$1,091	$0	$660	$0	$613		$264	$2,370 for 3/4" meter				$1,677 for 3/4" meter		$0	$0	$0	for 3/4" meter
Globe	N																										
Goodyear																											
Guadalupe																											
Hayden																											
Holbrook	N																										
Huachuca City																											
Jerome	N																	$5,000				$5,500					
Kearny	N																										
Kingman																											
Lake Havasu City	N																										
Litchfield Park	N																										
Mammoth																											
Marana	Y	Y	2001	N	N/A	N	N/A	$0	$0		$0	$0	$0	$0	$2,475	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$2,475.00
Mesa	Y	Y	1997	Y	Apr-03	N	N/A	$145	$226	$378	$831	$0	$0	$0	$0	$0	$100	$907	$0	$1,050	$0	$0	$0	$0	$0	$0	$3,646.00
Miami	N																										
Nogales																											
Oro Valley (Roadways)	Y	N	1994	Y	Jun-00	N	N/A	$0	$0	$0	$0	$0	$0	$0	$2,008	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$2,008.00
Oro Valley (Water System)	Y	Y	1996	Y	Jul-00	N	N/A	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$1,774	$0	$300	$0	$0	$0	$0	$0	$0	$2,074.00
Page	N																										
Paradise Valley	Y	Y	1999	N	N/A	N	N/A	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$18,532	$0	$0	$0	2 for 1" meter
Parker	N																										
Patagonia	N																										
Payson																											
Peoria	Y	N	1991	Y	Jan-02	N	N/A	$275	$186	$294	$1,361	$0	$518	$0	North $3,975 and $53		$381	$3,237	$558	$1,996	$0	$0	$0	$0	$0	$0	$9,612.00
Peoria															Central $757 and $49												
Peoria															South $302 and $54												
Phoenix (Estrella)	Y	N	1988	Y	Provided	N	N/A	$25	$30	$240	$1,517	$0	$0	3% of gross	$1,254	$0	$132	$952	$0	$854	$0	$0	$0	$0	$0	$37 Equipment Repair $356 Storm Drainage	$5,397.00
Phoenix (Laveen)	Y	N	1988	Y	Provided	N	N/A	$149	$127	$353	$2,319	$0	$0	$0	$1,069	$0	$132	$929	$0	$403	$0	$0	$0	$0	$0	$72 Equipment Repair $881 Storm Drainage	$6,434.00
Phoenix (Desert View)	Y	N	1988	Y	Provided	N	N/A	$111	$86	$367	$2,622	$0	$0	$0	$2,784	$0	$125	$2,590	$0	$1,226	$0	$0	$0	$0	$0	$76 Equipment Repair $0 Storm Drainage	$9,996.00

League of Arizona Cities & Towns 2003 Municipal Impact/ Development Fee Survey

City/Town	Impact Fees	One Fee Schedule	Year Effective	Have fees been updated	Dates Fees Updated	Escalation Element	Types of inflationary adjustment factors	Fire	Police	Library	Parks	Public Facilities	General Government	Administration Charges	Arterial Street/Transportation	Traffic Signal	Sanitation/Garbage Collection	Water	Water Resources	Waste Water	Reclaimed Water	Sewer Tap	Sewer Development	Utility Deposits	School Impact Fee	Other	Total Impact Fee
Phoenix (North Gateway)	Y	N	1988	Y	Provided	N	N/A	$160	$88	$297	$2,872	$0	$0	$0	$2,700	$0	$134	$2,647	$0	$1,380	$0	$0	$0	$0	$0	$78 Equipment Repair $0 Storm Drainage	$10,354.00
Pima																											
Pinetop-Lakeside	N																										
Prescott	Y	Y	1995	Y	Mar-02	N	N/A	$167	$84	$253	$1,116	$275	$0	$0	$469	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$2,364.00
Prescott Valley	Y	Y	1999	Y	May-03	N	N/A	$0	$405	$0	$795	$51	$0	$0	$1,252	$0	$0	$1,650	$1,300	$1,755	$0	$0	$0	$0	$0	$208 Cultural	$7,416.00
Quartzite																											
Queen Creek	Y	Y	1999	N	N/A	Y	Not Provided	$0	$185	$616	$3,229	$600	$0	$0	$0	$0	$0	$0	$0	$2,679	$0	$0	$0	$0	$0	$0	$7,308.00
Safford	N																										
Sahuarita	N																										
St. Johns																											
San Luis	Y	Y	2003	N	N/A	N	N/A	$149	$238	$0	$705	$0	$0	$258	$0	$0	$0	$760	$0	$715	$0	$0	$0	$0	$0	$0	$2,825.00
Scottsdale (Zone A)	Y	N	1997	Y	Jul-02	Y	CPI and Cost of Infrastructure											$617 and $2.84 for admin.	$630 and $2.90 for admin.				$844 and $3.88 for admin				$2,100.82
Scottsdale (Zone B	Y	N	1997	Y	Jul-02	Y	CPI and Cost of Infrastructure											$2,617 and $12.04 for admin.	$712 and $3.28 for admin.				$2806 and $11.99 for admin				$5,962.31
Scottsdale (Zone C)	Y	N	1997	Y	Jul-02	Y	CPI and Cost of Infrastructure											$2,617 and $12.04 for admin.	$712 and $3.28 for admin.				$2806 and $11.99 for admin				$5,962.31
Scottsdale (Zone D)	Y	N	1997	Y	Jul-02	Y	CPI and Cost of Infrastructure											$2,617 and $12.04 for admin.	$712 and $3.28 for admin.				$2806 and $11.99 for admin				$5,962.31
Scottsdale (Zone E)	Y	N	1997	Y	Jul-02	Y	CPI and Cost of Infrastructure											$2,617 and $12.04 for admin.	$712 and $3.28 for admin.				$2806 and $11.99 for admin				$5,962.31
Sedona	Y	N	1999	N	N/A	N	N/A	$0	$06	$0	$2,378	$153	$0	$0	$811.30		$0	$0	$0	$0	$0	$4,525	$0	$0	$0	$369.05 Storm Drainage	$8,301.71
Show Low	Y	Y	2000-2002	N	N/A	N	N/A	$0	$0	$140	$293	$0	$0	$0	$0	$0	$0	r 3/4" meter			$0	$0	$2,108	$0	$0	$62 Open Space $78 Rec Fac	$3,588.00
Sierra Vista	Y	Y				Not provided		$0	$0	$0	$350	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$350.00
Snowflake																											
Somerton	Y	Y	1995	N	N/A	N	N/A	$0	$0	$0	$100	$0	$0	$0	$0	$0	$75	$210	$480	$700	$0	$200	$650	$75	$0	$475 for Water Connect	$2,965.00
South Tucson	N																										
Springerville	N																										
Superior	N																										
Surprise	Y	N	1987	Y	Jun-00	N	N/A	$308	$137		$1,358	$0	$354	$0	$0	$0	$0	$1,770	$824	$0	$0	$0	$1,916	$0	$0	Northern Sewer Zone has additional fee $320 and $524 Public Works Development Fee	$7,189.00
Taylor	N																										
Tempe																											
Thatcher	Y	Y	1981	Y	Jul-00	N	N/A	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$8	$0	$1,000	$500	$90	$0	$0	$1,597.50
Tolleson	Y	Y	1998	N	N/A	N	N/A	$347	$287	$0	$0	$0	$161	$0	$644	$0	$0	$900	$0	$0	$0	$0	$574	$0	$0	$204 for Public Works	$3,114.00
Tombstone	N																										
Tucson	Y	Y	2003	N	N/A	N	N/A	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	for 1" meter	$0	$0	$0	$0	$0	$0	$0	$0	$1,418.00
Wellton																											
Wickenburg																											
Willcox	Y	Y	1986	N	N/A	N																					
Williams	Y	Y	1987	Y	Aug-98	N	N/A	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$1,580	$0	$0	$0	$0	$864	$0	$0	$0	$2,444.00
Winkleman	N																										
Winslow	N																										
Youngtown	Y	N	1996	N	N/A	N	N/A	N/A	$92	$50	$100	$0	$100	$0	$0	$0	$0	N/A	N/A	N/A	N/A	N/A	N/A	I/A	$0	Water, Sewer and Fire not provided by town	$342.00
Yuma	Y	N	1986 and 1995	Y	2000	N	N/A	$0	$0	$0	$0-$500	$0	$0	$0-$55	$0-$1,000	$0-$50	$0	$1,600	$0	$0	$0	$0	$1,950	$0	$0	$0-$1,250 Trans/collect $0-$70 Trans/bikeways	$3,550-6,475

ARIZONA LEGISLATIVE COUNCIL

MEMO

August 11, 2003

TO: Members
Tax Reform for Arizona Citizens Committee

FROM: Kenneth C. Behringer
General Counsel

RE: Government Property Lease Excise Tax (R-46-52)

Arizona law requires certain political subdivisions to impose an excise tax on the lease of property owned by the political subdivision. This requirement was enacted in 1996 and was the result of the Legislature's continuing attempts to balance the various interests involved in the taxation of leases of government properties.

These leases are referred to as possessory interests. All property in Arizona is subject to property tax unless it is exempted from the tax by the Arizona Constitution or federal law. Constitution of Arizona article IX, section 2. However, prior to 1986, Arizona statutes did not provide for the taxation of possessory interests.

Despite the lack of specific statutory authority, Maricopa County attempted to assess property tax on the Fox Theater's leasehold interest in land owned by the City of Phoenix. The court found that these interests were not exempted from taxation by the constitution and could be taxed. However, the court held that the Legislature had not exercised this power by providing a mechanism for taxing possessory interests. The court noted that "there are many classes of taxation which the state may provide for but does not." *Maricopa County v. Fox Riverside Theater Corp.*, 57 Ariz. 407, 114 P.2d 245 (1941).

In 1985, the Legislature did provide for the property taxation of possessory interests effective for the 1986 tax year. The statutes provided fifteen exemptions from the tax. Included in these exceptions were exemptions for contracts entered into before April 1, 1985. *See* Laws 1985, chapter 264.

In January 1993, the Arizona Tax Court invalidated the exemptions contained in former Arizona Revised Statutes (A.R.S.) section 42-684 (1991). The court stated that the statutory exemptions went beyond the property tax exemptions allowed by the Arizona Constitution. *Scottsdale Princess Partnership v. Maricopa County*, 185 Ariz. 368, 916 P.2d 1084 (Ariz.App. 1995). The Legislature responded by establishing class 12 properties, which were possessory interests that were assessed at one percent of their full cash value. In addition, the Legislature revised the exemption provisions.

Maricopa County challenged the validity of the revised exemptions. The Arizona Tax Court agreed that the new exemptions were also invalid. *Maricopa County v. State of Arizona*, Arizona Tax Court No. TX 93-00217. The next year the Legislature again revised the possessory interest statutes by placing in class twelve several of the properties that were invalidly exempted by the prior law. Laws 1994, chapter 293. The county challenged the 1994 changes on a number of constitutional grounds. The Arizona Court of Appeals upheld the statutes in *Cutter Aviation v. DOR*, 191 Ariz. 485, 958 P.2d 1 (Ariz.App. 1997).

In 1995, the Legislature repealed the statutory provisions to assess property tax to possessory interests. Laws 1995, chapter 294, section 8. The legislation also established a study committee to recommend whether possessory interests should be taxed and the best method of taxing these interests.

Based on the study committee's recommendation, the Legislature provided for the government property lease excise tax, stating:

> A. The joint legislative study committee on possessory interest that was established by Laws 1995, chapter 294, section 10 met several times during the summer and fall of 1995.
>
> B. After much consideration and deliberation, the legislature intends by this act to reaffirm its decision that possessory interest will not be subject to any type of ad valorem tax and to establish a non-ad valorem excise tax as successor to prior section 42-162, subsection A, paragraph 11, sections 42-681 through 42-685 and section 42-687, Arizona Revised Statutes, repealed by Laws 1995, chapter 294 and for the act to apply prospectively beginning in 1996.
>
> C. This act addresses the issues and deficiencies that became evident in the prior law, the evident constitutional problems with the prior law and the concerns of the affected public and private parties, and this act attempts to make whole the taxing jurisdictions that depended on revenues under the prior law.

Laws 1996, chapter 349, section 1.

Cities, towns, counties and county stadium districts must impose the tax. A.R.S. sections 42-6201 and 42-6202. The tax revenues are split according to a statutory formula among the county, the city or town, the community college district and the elementary school district. A.R S. section 42-6205.

The general tax rates range from fifty cents to one dollar seventy-five cents per square foot of gross building space. The rates depend on the number of floors in the building, the use to which the property is put, the age of the improvements and whether particular statutory reductions apply. A.R.S. section 42-6203. The tax does not apply to the following interests:

1. Property that is used for a governmental activity.
2. Property that is used for public housing.

3. Easements and rights-of-way of railroads and gas, electric, water, pipeline and telephone utilities.

4. Interests in all or any part of a facility that is owned of record by a government lessor and used primarily for athletic, recreational, entertainment, artistic, cultural or convention activities if the interest is used for those activities or activities directly related and incidental to these uses including concession stands.

5. Property that is located on municipal airports and airports, if the property is used for or in connection with aviation, including hangars, tie-downs, aircraft maintenance, sale of aviation related items, charter and rental activities, commercial aircraft terminal franchises, parking facilities and restaurants, stores and other services that are located in a terminal.

6. The use by a commercial airline of the runways and terminal facilities of state, city, town or county airports and certain public airports.

7. Leases of property or interests in a transportation facility that is constructed or operated pursuant to A.R.S. title 28, chapter 22, article 1 or 2.

8. Interests in property held in trust for an Indian or an Indian tribe by the United States government.

9. Interests in property that is defined as "contractor-acquired property" or "government-furnished property" in the federal acquisition regulations and that is owned by the government and used to perform a government contract.

10. Property of a corporation that is organized by or at the direction of a county, city or town to develop, construct, improve, repair, replace or own any property, improvement, building or other facility to be used for public purposes that the county, city or town pledges to lease or lease-purchase with county or municipal special or general revenues.

11. Interests in property used by a chamber of commerce recognized under section 501(c)(6) of the United States internal revenue code if the property is used predominately for those federal tax exempt purposes.

12. Interests in property used by organizations that are exempt from taxation under section 501(c)(3) of the internal revenue code.

13. Interests in parking garages or decks if the parking garages or decks are owned and operated by a government lessor or operated on behalf of a government lessor, by an entity other than the prime lessee, pursuant to a management agreement with the government lessor.

14. Residential rentals if the prime lessee is the occupant.

A.R.S. section 42-6208.

The attached chart was prepared by the Arizona League of Cities and Towns. The chart shows collections of the excise tax as reported in a survey conducted by the League.

GPLET Collections

CITY/TOWN	FY99	FY00	FY01	FY02
APACHE JUNCTION	$ -	$ -		
AVONDALE	$ -	$ -	$ -	$ -
BENSON	$ -	$ -	$ -	$ -
BISBEE	$ -	$ -		
BUCKEYE	$ -	$ -		
BULLHEAD CITY	$ -	$ -	$ -	$ -
CAMP VERDE	$ -	$ -	$ -	$ -
CAREFREE	$ -	$ -		
CASA GRANDE	$ -	$ -	$ -	$ -
CAVE CREEK	$ -	$ -	$ -	$ -
CHANDLER	$ -	$ -	$ -	$ -
CHINO VALLEY	$ -	$ -		
CLARKDALE	$ -	$ -	$ -	$ -
CLIFTON	$ -	$ -	$ -	$ -
COLORADO CITY	$ -	$ -	$ -	$ -
COOLIDGE	$ -	$ -	$ -	$ -
COTTONWOOD	$ -	$ -	$ -	$ -
DOUGLAS	$ -	$ -	$ 23,621.00	$ 23,621.00
DUNCAN	$ -	$ -	$ -	$ -
EAGAR	$ -	$ -		
EL MIRAGE	$ -	$ -		
ELOY	$ -	$ -	$ -	$ -
FLAGSTAFF	$ -	$ -	$ -	$ -
FLORENCE	$ -	$ -		
FOUNTAIN HILLS	$ -	$ -	$ -	$ -
FREDONIA	$ -	$ -	$ -	$ -
GILA BEND	$ -	$ -		
GILBERT	$ -	$ -	$ -	$ -
GLENDALE	$ 510.00	$ 510.00	$ 13,694.36	$ 46,089.52
GLOBE	$ -	$ -	$ -	$ -
GOODYEAR	$ -	$ -	$ -	$ 688.00
GUADALUPE	$ -	$ -		
HAYDEN	$ -	$ -		
HOLBROOK	$ -	$ -		
HUACHUCA CITY	$ -	$ -		
JEROME	$ -	$ -	$ -	$ -
KEARNY	$ -	$ -	$ -	$ -
KINGMAN	$ -	$ -	$ -	$ -
LAKE HAVASU CITY	$ -	$ -		
LITCHFIELD PARK	$ -	$ -	$ -	$ -
MAMMOTH	$ -	$ -		
MARANA	$ -	$ -	$ -	$ -
MESA	$ 6,441.50	$ 6,357.07	$ 192.60	$ 4,750.67
MIAMI	$ -	$ -		
NOGALES	$ -	$ -		
ORO VALLEY	$ -	$ -	$ -	$ -
PAGE	$ -	$ -		
PARADISE VALLEY	$ -	$ -	$ -	$ -
PARKER	$ -	$ -	$ -	$ -

PATAGONIA	$ -	$ -	$ -	$ -
PAYSON	$ -	$ -	$ -	$ -
PEORIA	$ -	$ -		
PHOENIX	$ 1,767,493.00	$ 2,225,710.71	$ 2,026,099.08	$ 1,989,101.93
PIMA	$ -	$ -	$ -	$ -
PINETOP-LAKESIDE	$ -	$ -		
PRESCOTT	$ 69,000.00	$ 69,000.00	$ 69,000.00	$ 69,000.00
PRESCOTT VALLEY	$ 4,260.00	$ 1,901.23	$ -	$ -
QUARTZSITE	$ -	$ -	$ -	$ -
QUEEN CREEK	$ -	$ -	$ -	$ -
SAFFORD	$ 26,369.40	$ 10,766.70	$ -	$ -
SAHUARITA	$ -	$ -	$ -	$ -
ST. JOHNS	$ -	$ -		
SAN LUIS	$ -	$ -	$ -	$ -
SCOTTSDALE	$ 3,921.89	$ 942.30	$ 818.33	$ 777.00
SEDONA	$ -	$ 6,334.00	$ 6,334.00	$ 6,334.00
SHOW LOW	$ -	$ -	$ -	$ -
SIERRA VISTA	$ -	$ -	$ -	$ -
SNOWFLAKE	$ -	$ -		
SOMERTON	$ -	$ -		
SOUTH TUCSON	$ -	$ -		
SPRINGERVILLE	$ -	$ -		
SUPERIOR	$ -	$ -		
SURPRISE	$ -	$ -	$ 13,320.00	$ 8,520.00
TAYLOR	$ -	$ -	$ -	$ -
TEMPE	$ 44,175.60	$ 44,175.60	$ 63,483.60	$ 559,442.00
THATCHER	$ -	$ -	$ -	$ -
TOLLESON	$ 13,500.00	$ 13,500.00	$ 13,500.00	$ 13,500.00
TOMBSTONE	$ -	$ -		
TUCSON	$ -	$ -	$ -	$ -
WELLTON	$ -	$ -		
WICKENBURG	$ -	$ -	$ -	$ -
WILLCOX	$ -	$ -		
WILLIAMS	$ -	$ -	$ -	$ -
WINKELMAN	$ -	$ -	$ -	$ -
WINSLOW	$ -	$ -	$ -	$ -
YOUNGTOWN	$ -	$ -	$ -	$ -
YUMA	$ -	$ -		
TOTALS	$ 1,935,671.39	$ 2,379,197.61	$ 2,230,062.97	$ 2,721,824.12

HISTORY OF SCHOOL FUNDING LAWSUITS AND THE LEGISLATIVE RESPONSES

Arizona Constitution - Article 11, Section 1:

> *The Legislature shall enact such laws as shall provide for the establishment and maintenance of a general and uniform public school system, which system shall include kindergarten schools, common schools, high schools, normal schools, industrial schools and universities . . .*

Original Lawsuit:
Four school districts and several individuals filed suit in Maricopa County Superior Court against the Superintendent of Public Instruction and the State of Arizona on the grounds that the statutory scheme for financing public education in this state violated the Arizona Constitution. Superior Court Judge Stanley Goodfarb specifically noted that enormous disparity exists between the capital facilities of various school districts due, at least in part, to the local property taxation scheme imposed by statute. However, in dismissing the school districts' complaint, Judge Goodfarb concluded that, as a matter of law, the school districts had failed to state a claim under the Arizona Constitution.

The school districts appealed the decision to Division 1 of the Arizona Court of Appeals and subsequently filed a petition to transfer the case to the Arizona Supreme Court. The Supreme Court agreed to hear the case.

July 21, 1994: Supreme Court declares the school capital finance system unconstitutional.

The Arizona Supreme Court ruled in Roosevelt Elementary School District No. 66 v. Bishop that the historical funding system of using general obligation bonds as the main revenue source for building, renovating and remodeling school facilities and purchasing other capital equipment was unconstitutional. Historically, voters were required to approve bonds, to be paid with a secondary property tax.

The plaintiffs claimed that the property tax system was unfair to children living in low property-wealth districts. These districts had difficulty issuing bonds because voters had to approve the bonds and the secondary tax in low property-wealth districts resulted in higher tax rates than districts with high property-wealth.

The Arizona Supreme Court, in a 3-2 decision, declined to rule on the school districts' claim that Arizona's school funding formula violated the equal protection clause of the Arizona Constitution, Instead, the Court found that school capital funding violated the Constitution's "general and uniform" provision. The Court found that "the undisputed record showed enormous facility disparities among various school districts and traced these disparities to the statutory scheme, which relies in large part on local property taxation for public school capital requirements. . ."

While the Court concluded that the Constitution allows the Legislature to rely on school districts and counties to help finance public education, it is the responsibility of the state for financing public education and the end result must produce a general and uniform financing scheme.

The Court state two fundamental principles in its effort to define the term "general and uniform" under the Constitution. First, the court concluded that individual entities within a "general and uniform" system need not be exactly the same, identical or equal. Second, the court concluded that as long as the system the Legislature chooses to fund the public schools is not itself the cause of substantial disparities, local political subdivisions, such as school districts and counties, may opt to take steps to provide an education system that is better than the general and uniform system created by the state.

The Court further directed the Legislature to create a financing system that did not violate the constitution. They also stated that the trial court shall retain jurisdiction to determine whether, within a reasonable time, legislative action has been taken.

March 21, 1996 & July 18, 1996: Legislature enacts and appropriates money for a State Board for School Capital Facilities.

The legislature passed legislation that established the State Board for School Capital Facilities and a School Capital Fund, commonly referred to as the Cap-Fac plan. This fund provided $30 million in grants and loans to help poor schools with health and safety emergencies. The School Capital Facilities Board distributed the funds to school districts.

In July 1996, the legislature appropriated an additional $70 million for two years. $30 million of the fund was used for statewide bond issues that were estimated to raise $300 million for school facilities over 10 years.

November 19, 1996: Superior Court Judge Albrecht declares that this plan is unconstitutional.

The ruling by Judge Albrecht stated that the "cap-fac" plan did not attempt to remove any disparities created by the school funding system and that there was no assurance that the needs of a particular district will be addressed or met.

The plan did not assure the distribution of funds to educate children on substantially equal terms. The cap-fac plan also contained automatic repeals. Therefore, the Court determined that it was simply an overlay of the existing funding and did nothing to reform the funding system that was previously declared unconstitutional.

The Superior Court ruled that the legislature must develop a new system by June 30, 1998 and threatened to cut off state aid to education if an acceptable plan was not developed by the deadline.

January 15, 1997: Supreme Court affirms Judge Albrecht's decision.

Governor Symington requested that the Arizona Supreme Court reverse the decision, but it was upheld.

March 5, 1997: Legislature enacts the Assistance to Build Classrooms (ABC) plan.

Several proposals to address funding were proposed during the 1997 session, but ultimately, the Legislature passed the Assistance to Build Classrooms (ABC) plan. This plan provided a funding formula that guaranteed all districts $350 per growth weighted school student ($525 per high school student). Grants would be provided by subtracting the local effort, which was funded with local secondary property taxes. This system was designed to give more funding to low property wealth districts.

Additionally, the plan provided a mechanism for fast growing districts to receive state grants conditional on local effort requirements. It also capped the bonding ability of high property wealth districts.

Grant monies received by the school districts could be used to issue revenue bonds, buy down existing or future general obligation bond debt, or to pay cash for new facilities. No voter-approval was needed, unless revenue bonds were issued. The cost of ABC was estimated to be $32.5 million per year over 10 years.

It should also be noted that attempts were made to include facility standards in this plan, but ultimately, those attempts failed.

August 20, 1997: Superior Court Judge Albrecht declares the ABC plan is also unconstitutional.

Judge Albrecht ruled that ABC does not support a finding that a school district is assured funding levels that will make the alternative of revenue bonds viable. Because voter approval is required, the ABC plan cannot assure that the bonds would be issued.

The ruling did note that the ABC plan did work toward reducing disparities, but it cannot assure that the State system of school finance will provide a general and uniform education system.

December 23, 1997: Supreme Court also declares the ABC plan unconstitutional and describes a broad outline of constitutional options.

Governor Symington resigned in September of 1997 and Governor Hull was sworn in as the new Governor. Governor Hull appealed Judge Albrecht's decision to the Arizona Supreme Court. The Court upheld Judge Albrect's ruling on October 24, 1997 and a decision was not issued until December 23, 1997.

The Court stated that the Constitution mandates adequate capital facilities statewide and the ABC system does not create or meet an adequate capital facilities standard. The current system does not fix the variations in property values in different school districts. *The legislature may not delegate to school districts the responsibility to provide adequate capital facilities.*

The Court further maintained that the legislature must establish standards for adequate capital facilities, against which equalization may be judged. Then it must choose a funding mechanism that does not cause substantial disparities and that does not allow any school to fall below the standard. *A constitutional adequate system will provide minimum quality and quantity standards for buildings and provide financing for facilities and equipment necessary to enable students to master established educational goals.*

The baseline must establish a level of funding to:

- Bring existing facilities up to an adequate standards
- Construct new and adequate facilities for growing districts
- Maintain all capital facilities at the adequacy level

The Court also outlined alternative funding approaches:

- Substantial equalization of district property taxation to meet state standards
- State sales or income taxes to fund the standards
- State property tax to fund the state standards
- School district consolidation into districts with comparable valuation

The Court also allowed for local control. Local control includes the power to choose facilities beyond the state standards. Local option taxation may be permitted to go beyond state standards. *Local control does not include the power to choose substandard facilities by defeating bonds.* Caps on local option taxes are not constitutionally required and do not effectively promote equalization. Caps limit the ability of districts to go beyond state standards and thereby jeopardize the future of public schools. (This comment by the Court discouraging caps seems to be in the nature of policy advice, rather than constitutional interpretation.)

Although the dissent in the 4-1 decision urged that the ABC system be given some period of time to work, the majority found that the ABC funding does not make the system constitutional. It found that it is a very small fund that merely supplements the current system. The 4:1 ratio is hardly substantial equalization. The dollar amount is arbitrary and bears no relation to actual need.

April 9, 1998: Legislature enacts Students FIRST

The Legislature responded to the latest Court decision by crafting a plan that followed the guidelines outlined in the decision. A statewide funding system was established, but due to lobbying from some of the property wealthy school districts, an "opt-out" provision was allowed. The opt-out provision allowed any school district to refuse state funding and continue to use the traditional method of funding their schools with local property taxes. However, even the opt-out districts would still have to adhere to state adequacy standards.

The original Students FIRST program established the following:

- State adequacy standards for existing school facilities
- State funding for schools
- Established a School Facilities Board to oversee and administer the Students FIRST funding
- Four funds to address school capital needs:
  - Deficiency Corrections Fund (temporary)
    Funding to be used to correct both square footage deficiencies and quality deficiencies.
  - Building Renewal Fund
    Established a formula for school districts to receive funds for maintenance of buildings. The formula takes into account the age of the building, major renovations and the capacity of the building.
  - New Construction Fund
    Established a formula to school districts to receive funding for new schools. The formula is based on the number of students, square footage requirements and the cost per square foot. If insufficient funds are available on a "pay-as-you-go" basis, then the state could issue revenue bonds.
  - Soft Capital Funding
    Provided funding on a flat per-student amount for short-lived materials and equipment needed to assist students in mastering educational skills. Includes items such as textbooks, library resources, computer software and other instructional aids, furniture, equipment and transportation vehicles.

June 16, 1998: Supreme Court upholds part of Students FIRST and declares part unconstitutional.

In a unanimous opinion, the Court held that the establishment of adequacy standards and the state funding of school district capital needs up to the adequacy standards is constitutional.

The Court also held that optional local property tax funding of capital needs by school districts is constitutional, but only if whichever bonding, override and property tax assessment ratio states that are available to locally funded – "opt out" – districts for going above and beyond state adequacy standards apply equally to state funded districts for them to go above and beyond state adequacy stands with local fund is they can. In other words, if districts are allowed to "opt out" and use bonds or overrides to go above and beyond state adequacy standards, then state funded districts must be allowed to use bonds or overrides to go above and beyond state adequacy standards under the same terms and conditions.

The problem described by the Court was that the Students FIRST act establishes different local funding systems for state funded districts and locally funded – opt out – districts to go above and beyond the state adequacy standards. Differences in the availability of bonding and differences in overrides and assessment ratios create significant distinctions between the two types of districts.

The legislature must fund public schools through a financing system that does not itself cause substantial disparities between districts. Differently enabling two classes of districts to access their respective property bases results in systemic, structural difference in the ability of districts to exceed state minimums through local funding. Because of these structural differences, the act as a whole continues to formalize and perpetuate a structure that fails the general and uniform test. Students FIRST will necessarily cause substantial disparities between public school districts. The legislature cannot allow some districts to employ local funding mechanisms that it withholds from other districts.

The Court held that unconstitutional provisions relating to bonding, assessment ratios and the opt out provisions are not severable from the rest of the Students FIRST act, and the entire act is void. The Court did extend the deadline for the stoppage of state funds to public schools from June 16, 1998 until August 15, 1998.

July 9, 1998: Legislature amends the unconstitutional part of Students FIRST.

The Legislature reenacted Students FIRST with modifications to address the unconstitutional aspects. The bill maintained the adequacy standards and the various funds, but eliminated the "opt-out" provision for school districts. Each school district is required to participate, but can supplement these funds with capital overrides. The overrides cannot be used for soft capital and new debt limits were put in place for these overrides.

July 20, 1998: Supreme Court declares that Student's FIRST, as amended, is constitutional.

Governor Hull requested that the Supreme Court declare Students FIRST constitutional. The Governor's attorney and Mr. Tim Hogan, the plaintiffs' attorney and Superintendent of Public Instruction Lisa Graham Keegan, filed a joint motion supporting Students FIRST.

The Court issued an order stating that the petitioner and real parties in interest have now filed a joint motion in which they agree that the school finance legislation is valid and that no constitutional challenges to the statutes remain. The plaintiffs did file a separate motion asking the Supreme Court to send the case back to the Superior Court, thereby leaving the case open until Students FIRST was fully implemented and funded. The Supreme Court denied this motion and the case was finally closed.

PART II: LAWSUITS RELATED TO FUNDING OF THE BUILDING RENEWAL FORMULA (BRF)

FY 1998-1999 – First year of funding for Students FIRST. The BRF is funded at $75 million.

FY 1999-2000 – Instead of using the formula, the FY 1999-2000 amount was simply set at ten percent more than the first year of funding by the Legislature. The formula called for a payment of $109.1 million and funding of $82.5 million was received. The difference is a deficit of $26.6 million.

October 1999 - Roosevelt Elementary School District V. State - Four school districts sued to enforce the state's funding obligations established under Students FIRST. The suit asked the Superior Court to order the Legislature to fully fund the BRF for 1998-1999 and 1999-2000 and future years and to instruct the state treasurer in future years to credit the BRF in an amount necessary to fund the formula.

The state prevailed as to funding for the first fiscal year 1998-1999. However, the Superior Court found that failure to use the formula for 1999-2000 violated Students FIRST. The Court did note that there was no evidence present that the funding provided a shortage of deficiency funds.

FY 2000-2001 – Legislature fully funds BRF at $122.7 million

FY 2001-2002 – The SFB used the statutory formula to calculate the BRF distribution and made the first half payment in November 2001. However in December 2001, The Legislature transferred $34.9 million from the BRF to the state general fund. In March 2002, the Legislature increase the amount transferred from the BRF to approximately $70 million. The May 2002 BRF distribution to the school districts was $672,093.

May 2002 – Plaintiffs motion for summary judgment is granted in part: The Superior Court concluded that the school districts had "produced uncontroverted evidence that the State's failure to follow the formula in funding the BRF in FY 1999-2000 had an impact on the districts' ability to meet academic standards and therefor was unconstitutional."

FY 2002-2003 & FY 2003-2004 – Original BRF calculation was $128.3 million. During the 2nd regular session (HB 2710) the formula was changed to exclude buildings that were to be replaced under the Deficiencies Correction Fund (DCF). The result was that the Legislature directed the State Treasurer to disregard the SFB request and instead transfer $38.3 million, a difference of approximately $90 million.

The Legislature also suspended the use of BRF for FY 2002-2003 and FY 2003-2004 because the money necessary for school facilities required to meet academic standards will be provided from the DCF.

New Lawsuit – Somerton Elementary School District v. State: Six school districts challenged the latest funding reductions based on the premise that the BRF is the only source of long-term funding of capital needs for schools and that the Legislature acted unconstitutionally. The Superior Court ordered the Legislature to restore full funding by June 30, 2003.

Issues on appeal were:

- Whether the Court erred in determining that school districts adequately demonstrated that the reduced funding impacted student's ability to meet academic standards for FY 1999-2000.
- Whether the Court erred in concluding that school districts did not have to demonstrate that the reduced funding in FY 2001-2002 affected their ability to meet academic standards.
- Whether the Court erred in ordering the BRF to be fully funded in FY 2002-2003 because no evidence was submitted of current deficiencies impacting academic standards.

January 2003: State filed notice of appeal and plaintiffs filed a motion to consolidate the *Roosevelt* appeal with the *Somerton* case. The Arizona Court of Appeals agreed to consolidate the cases.

August 2003: **Somerton Case**: Arizona Court of Appeals reversed the Superior Court's decision because school districts have not shown that they have current unmet needs related to academic achievement. The Court further stated that while a cut in funding may require future expenditures that may possibly be greater than what the formula requires, it is legislative discretion and not a constitutional violation. They remanded the case back to Superior Court for further proceedings.

JLBC case: Also in late August, a separate case has been filed by the Center for Law in the Public Interest over the construction index used by JLBC to determine the inflation rate for the new construction formula. ARS 15-2041(D)3(c) requires JLBC to annually adopt an inflation index for the construction of new facilities. JLBC did not adopt a construction index and the lawsuit is asking the Court to order JLBC to do so. The Attorney General's office will respond by October 1.

Prepared by:
KD/House Majority Research Staff
August 2003

School district capital spending: We're #1

In 1998, state leaders described Students FIRST as "the biggest property tax cut in Arizona history." By 1999, the School Facilities Board (SFB), a creation of Students FIRST, began spending enormous sums of money on school construction, renovations, and equipment.

As of FY 2003, the SFB has spent or encumbered $2.7 billion: $1.1 billion in new school construction; $1.3 billion to correct deficiencies; and another $380.5 million in building renewal.

In 1998, the prospect of such new spending on school capital was the rationale state leaders had for their claim that the new system would result in meaningful tax cuts.

At the time, ATRA expressed skepticism that it would indeed reduce school district property taxes. The evidence so far has not assuaged that skepticism.

Data from the Department of Revenue shows that in FY 1997-98, 162 school districts statewide were carrying a total of $4.1 billion in outstanding debt for general obligation (G.O.) bonds. In FY 2001-02, the Commission reported that 150 districts had $4.1 billion in outstanding G.O. bonds.

Of course, those totals do not include newly authorized G.O. bonds yet to be issued. Since 1999, $776.9 million of new bonds (called "Class B" bonds to distinguish from the older "Class A" bonds issued prior to Students FIRST) have been approved at the polls. Over S352 million of those class B bonds were approved by voters just last November in 12 school districts.

Five districts that are impacted by federal land, such as reservations, have been using the new authority to issue "impact aid revenue bonds," of which $57.4 million were approved in the last two November elections.

Infrequently used in the years prior to Students FIRST, districts appear to be turning to capital override elections more often in recent years. Between 1999 and 2002, 14 districts have sought voter approval for $155.6 million in capital outlay overrides. All but $24 million, however, have been rejected at the polls. Under current law, these tax levies are unlimited, can exist for up to seven years, and can overlap previous overrides. According to data from the Arizona Department of Education, 17 districts budgeted $48.8 million statewide for capital overrides.

There are several other funds designated for capital as well. The capital outlay revenue control limit (CORL), the main capital component of K-12 funding formulas, produced approximately $214 million in FY 2002-03, the vast majority of which is spent for maintenance and operations (M&O).

In FY 1998-99, districts statewide budgeted about $32 million in property taxes for capital projects under adjacent ways. Adjacent ways budgets for FY 2002-03 totaled $50.7 million.

Some districts that levy property taxes under state law for desegregation and OCR earmarked nearly $15.7 million of those revenues for capital projects in FY 2002-03.

Students FIRST also provided additional revenue as part of the soft capital allocation (SCA). Replacing the old capital levy revenue limit (CLRL), which produced about $134 million in 1998, the SCA was projected to add an additional $36.5 million by 1999. District budgets for FY 2002-03 showed $190.3 million was generated by the SCA formula.

Prior to the enactment of Students FIRST, data from the U.S. Department of Education's National Center for Education Statistics (NCES) ranked Arizona 7th nationally in per-pupil spending for capital (FY 1996-97).

Given the levels of capital spending since that time, it will likely come as no surprise to learn that the most recent NCES data (FY 1999-00) ranks Arizona *first in the U.S. in per-pupil expenditures for capital.*

Michael Hunter

BOND ELECTIONS

Year	District	Requested	Result
1999	Cave Creek Unified	$12,715,000	Pass
1999	Cave Creek Unified	$15,775,000	Fail
1999	Fountain Hills Unified	$16,000,000	Pass
1999	Paradise Valley Unified	$106,835,000	Pass
1999	Marana Unified	$38,825,000	Pass
1999	Ray Unified	$2,750,000	Pass
1999	Toltec Elementary	$1,620,000	Pass
1999	Hyder Elementary	$400,000	Pass
2000	Cave Creek Unified	$41,600,000	Pass
2000	Riverside Elementary	$15,000,000	Pass
2000	Tolleson Elementary	$3,000,000	Pass
2000	Kayenta Unified	$8,300,000	Pass
2000	Vail Unified	$10,000,000	Pass
2001	Deer Valley Unified	$77,500,000	Pass
2001	Ganado Unified	$5,500,000	Pass
2001	Globe Unified	$3,600,000	Pass
2001	Pendergast Unified	$13,938,000	Pass
2001	Scottsdale Unified	$155,000,000	Fail
2001	Tuba City Unified	$3,000,000	Pass
2001	Washington Elementary	$64,000,000	Pass
2002	Agua Fria Union	$17,845,000	Pass
2002	Agua Fria Union	$3,620,000	Pass
2002	Buckeye Union	$37,700,000	Pass
2002	Chandler Unified	$59,950,000	Pass
2002	Coolidge Unified	$5,700,000	Pass
2002	Dysart Unified	$74,040,000	Pass
2002	Peoria Unifed	$93,500,000	Pass
2002	Queen Creek Unified	$16,800,000	Pass
2002	Saddle Mountain Unified	$25,000,000	Pass
2002	Somerton Elementary	$4,200,000	Pass
2002	Wickenburg Unified	$9,980,000	Pass
2002	Winslow Unified	$4,000,000	Pass
	Total	**$947,693,000**	
	Total Passed	**$776,918,000**	
	Total Failed	**$170,775,000**	

CAPITAL OUTLAY OVERRIDES

Year	District	Requested	Result
1999	San Carlos Unified	$5,000,000	Pass
1999	Cave Creek Unified	$1,640,000	Fail
1999	Fountain Hills Unified	$750,000	Pass
1999	Paradise Valley Unified	$8,330,174	Pass
1999	Wilson Elementary	$975,000	Pass
1999	Kayenta Unified	$1,000,000	Pass
2000	San Carlos Unified	$7,000,000	Pass
2000	Cave Creek Unified	$2,200,000	Fail
2000	Cedar Unified	$1,000,000	Pass
2001	Deer Valley Unified	$43,695,750	Fail
2001	Scottsdale Unified	$70,749,000	Fail
2002	Dysart Unified	$1,802,000	Fail
2002	Peoria Unified	$10,000,000	Fail
2002	Saddle Mountain Unified	$1,500,000	Fail
	Total	**$155,641,924**	
	Total Passed	**$24,055,174**	
	Total Failed	**$131,586,750**	

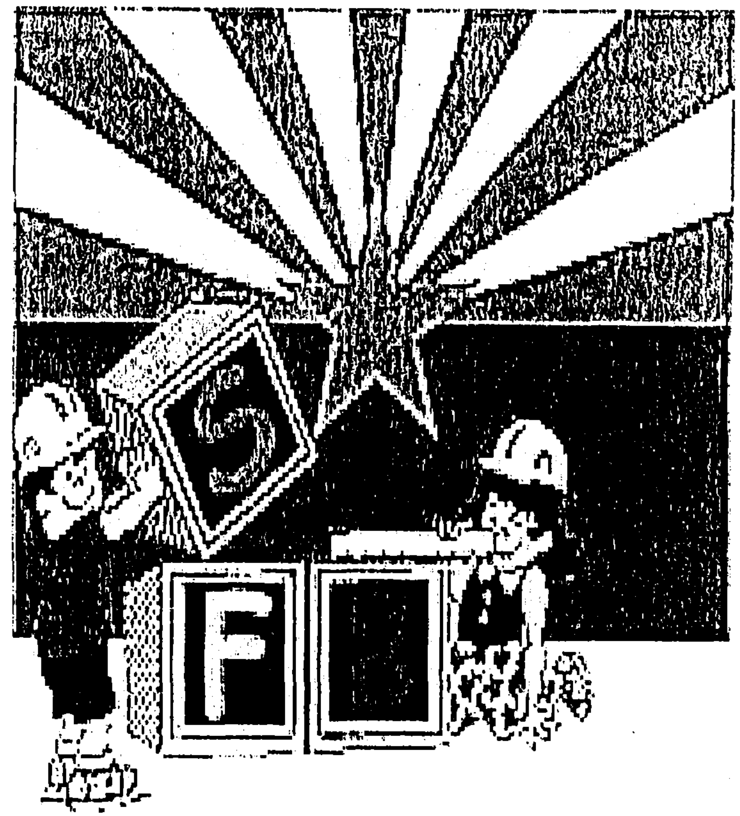
IMPACT AID REVENUE BONDS

Year	District	Requested	Result
2001	Indian Oasis-Baboquivari Unified	$16,000,000	Pass
2001	Red Mesa Unified	$1,640,000	Pass
2001	Tuba City Unified	$14,500,000	Pass
2002	Dysart Unified	$3,260,000	Pass
2002	Ganado Unified	$22,000,000	Pass
	Total	**$57,400,000**	

School Facilities Board

Edward E. Boot
Interim Executive Director

Tax Reform for Arizona
Citizens Committee
Arizona Students FIRST



July 15, 2003

School Facilities Board

Edward E. Boot
Interim Executive Director

Tax Reform for Arizona
Citizens Committee
Arizona Students FIRST

July 15, 2003

SFB BACKGROUND

- The School Facilities Board was created after a lengthy law suit established Students FIRST, a centralized school finance system with the State having primary responsibility. Students FIRST was established to create equitable access to facilities and capital resources for all school districts.
- The Supreme Court Ruled the State must bring existing facilities up to standards; Construct new facilities for growth; maintain all capital facilities at the adequacy level, and ensure the funding systemdoes not cause substantial disparities between districts.

The Supreme Court Ruled

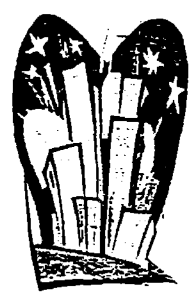
The State Must:

✓ Establish minimum adequate facility standards and provide funding to:
  - 1) Bring existing facilities up to standards.
  - 2) Construct new facilities for growing districts.
  - 3) Maintain all capital facilities at the adequacy level.

✓ Ensure that the funding system chosen does not in itself cause substantial disparities between districts.

What Has the SFB Accomplished

since July 1, 1999



- 98 New Schools Opened
  - 6.6 million Square Feet
- 101 New Schools In Progress
  - 7.5 million Square Feet
- 5,780 Deficiencies Being Corrected
  - Most Improve the Ability to Educate
- $380 million of Building Renewal
- Provided a Focus on Facilities

DEFICIENCIES CORRECTION

a one Time Program

- The Deficiency Correction Program is to correct all pre-existing quantity and quality deficiencies.
- All existing deficiencies were required to be awarded for construction by 6/30/03 and are to be corrected by 6/30/04.
  - Bill in FY 2003Session delayed some projects and extended completion in 3 districts until to FY 2005
  - Mesa, Tucson, Glendale have had 296 projects delayed ($41.5M)
- Arizona is the first state to undertake this type of program for schools statewide.

THE DEFICIENCY NUMBERS

- **5,780 projects** (1210 schools)
- $1,012 million of deficiency projects
- $ 168 million of technology
- $ 58 million of Equipment
- $ 46 million of Operations Cost
  - includes Project Management

- *Total Estimated Program Cost is*

$ 1,284,000,000 ($10M under Projection)

New Construction

an ongoing Program

- The Law established a formula to calculate each District's need
- Student Capacity is based on Square Footage Requirements that are set in Statue
- The SFB then compares District Capacity to Projected ADM
- The District Qualifies for Space if:
  - K-6 projected ADM exceeds capacity within two years
  - 7-12 projected ADM exceeds capacity within three years

Calculating an Award

- Determine the number of students lacking space for each grade configuration.
- Multiply the students by the statutory per student sq. footage amounts to get total sq. feet.
- Multiply the the total sq. feet by the cost per sq. foot.
- The cost per sq. foot is set by statute and indexed by JLBC.

New Construction Example

District A projects a K-6 ADM of 8,000 within two years.
Current K-6 space in the district is 620,000 sq. feet.
Square footage divisor is 85 per K-6 student.
580,000 / 85 = 7,294
8,000-7,294 = 706 ADM

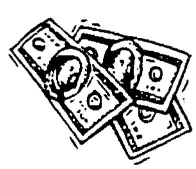
When building new space, statute awards 90 sq. feet per K-6 student (this allows for growth in new facilities).
706 * 90 = 63,540
The current per sq. foot cost for K-6 space is $98.01.
63,540 * $98.01 = $6,227,555
District A is awarded $6,227,555 to build a new school!

School Openings By Fiscal Year

Open FY	# of Projects	# of Students	Square Feet
2004	61	37,460	3,535,802
2005	23	17,984	1,806,226
2006	26	20,570	1,762,224
2007	25	20,395	1,773,209
2008	27	20,611	1,861,185
2009	31	18,427	1,985,875
Total	193	135,447	12,724,521

Projected New Construction Needs

- FY 2003 $261,057,000
- FY 2004 $248,396,000
- FY 2005 $194,936,000
- FY 2006 $185,003,000
- FY 2007 $197,210,000
- FY 2008 $215,432,000
- FY 2009 $234,224,000



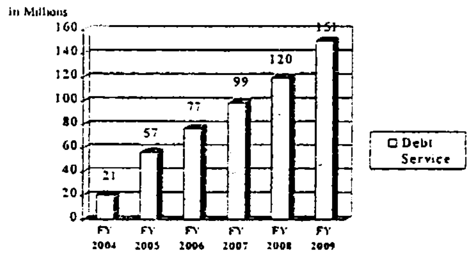
* Projections are based on submitted capital plans

Projected Land Costs

- FY 2003 $31,145,350
- FY 2004 $35,000,000
- FY 2005 $28,000,000
- FY 2006 $33,000,000
- FY 2007 $25,000,000
- FY 2008 $35,000,000
- FY 2009 $30,000,000

Note: The SFB has achieved over $81 million in Land Donations

Lease To Own Impact



Note: Debt Service based on 100% use of LTO for projected funding need

BUILDING RENEWAL

- Building Renewal formula
  - A building's square footage, age, improvements, and student capacity are used in the building renewal calculation.
- The SFB distributes building renewal
  - monies in two equal installments in November and May of each year.

Projected Building Renewal

	Current Formula
FY 2003 *	$117,817,000
FY 2004 *	$121,950,000
FY 2005	$126,229,000
FY 2006	$132,551,000
FY 2007	$139,190,000
FY 2008	$146,161,000
FY 2009	$153,481,000

* The formula is suspended for these years.

School Facilities Board

Total Projected Needs

	New Construction	Land	Building Renewal	Total
FY 2004	$248,396,000	$35,000,000	$121,950,000	$405,346,000
FY 2005	$194,936,000	$28,000,000	$126,229,000	$349,165,000
FY 2006	$185,003,000	$33,000,000	$132,551,000	$350,554,000
FY 2007	$197,210,000	$25,000,000	$139,190,000	$361,400,000
FY 2008	$215,432,000	$35,000,000	$146,161,000	$396,593,000
FY 2009	$234,224,000	$30,000,000	$153,481,000	$417,705,000

Note: Total Projected Needs does NOT include and potential LTO Debt Service

School Facilities Board

- Students FIRST has benefited educators, students, and taxpayers by fixing long neglected facilities and has also focused school districts on the condition of their physical plants.

- While Students FIRST is a complex and complicated Program with little political or Legislative support and is a BIG cost financial burden for the State, the derived benefits have been significant as the SFB has been effective in correcting existing deficiencies, in building new schools and in its stewardship of public money.

Appendix F

Minutes

ARIZONA STATE LEGISLATURE
Forty-fifth Legislature – First Regular Session

TAX REFORM FOR ARIZONA CITIZENS COMMITTEE

Minutes of Meeting
Monday, June 16, 2003
House Hearing Room 3 -- 9:00 a.m.

Mr. Huffman called the meeting to order at 9:10 a.m. and attendance was noted by the secretary.

Members Present

Senator Waring
Senator Martin, Cochairman
William Arnold
Lori Daniels
Bob Flach
Representative Clark
Representative Tully
Representative Huffman, Cochairman
Elaine Scruggs
Russell Smoldon

Members Absent

Senator Brown
Senator Giffords
Andrew W. Kunasek
Representative Jackson, Jr.
Kevin McCarthy

Speakers Present

Kitty Decker, Senior Economist/Majority Research Staff, Ways and Means Committee

Opening Remarks

Mr. Huffman conveyed that the Committee was created through legislation last year and noted that some of the Members are different due to an election that occurred afterward. He cited the following goals of the Committee:

- Develop potential legislation for next session by utilizing available resources to determine how to make the tax code more competitive and viable enough to take care of the needs of the state without causing financial hardship.
- Develop resources to educate Members not on the Committee to have the necessary expertise when reforms to the tax code are suggested next year.

Senator Martin encouraged the Members to review the minutes of the meeting held prior to reformation of the Committee, which can be provided by staff or accessed on-line. He added that much work needs to be accomplished in a short time frame, but he believes a good team has been assembled that will do well.

Mr. Huffman pointed out that the Members were provided with a list of potential items to discuss at future meetings (Attachment 1), which will be held alternately between the House and Senate.

Elect Chairman

> **Mr. Smoldon moved, seconded by Mayor Scruggs, that Mr. Huffman and Senator Martin be elected as Cochairs of the Tax Reform for Arizona Citizens Committee. The motion carried.**

At the request of Cochairman Huffman, the Members introduced themselves.

Overview of Property Taxation in Arizona

Kitty Decker, Senior Economist, Majority Research Staff, reviewed the following handouts:

- Property Taxation in Arizona (Attachment 2).
- Home vs. Business Taxes – Selected Districts 2002 Tax Returns (Attachment 3).
- Portions of the Tax Policy Handbook for State Legislators dated April 2003 (Attachment 4).

She advised Mr. Smoldon that the assessment ratio for Class 5 (railroad, private car, airline flight) is determined annually by the Arizona Department of Revenue based on a formula.

Noting that Arizona is unique by having a primary and secondary value, Mr. Clark asked how other states limit growth of taxes. Ms. Decker responded that in other states, whether voter approved or not, taxes are assessed against the same value, but she will have to research how growth of taxes is limited. She noted that the value of a home in California is not changed unless the owner moves, which is the most onerous system as far as not providing equal valuation.

Cochairman Huffman remarked that discussions about the property tax system and limiting growth should include not only how money is generated, but where the money goes, other sources of revenue, and how to pay for what is needed while maintaining some control.

Ms. Decker related to Senator Martin that in 1980, the 1 percent constitutional cap was divided into primary and secondary values. Primary was used for government with the idea that if the voters want to impose additional taxes upon themselves, it could be done, but the value would not be limited. Any change would require a constitutional amendment.

Referring to Mr. Clark's previous question, Ms. Decker advised that there is a homeowner's rebate on the primary school value. Many states have some type of homeowner protection such as exempting the first $50,000 for homes, which applies to all tax rates, not just the school tax rate.

Discussion of Future Meetings

Ms. Decker noted that some Members and other people would prefer not to meet on Monday. She related that in addition to legislative staff, the statute provides for utilization of

Joint Legislative Budget Committee staff, and Legislative Council has a research arm that can be utilized.

Senator Martin requested information on the correlation between different assessment ratios and economic activity.

Mr. Smoldon remarked that from a public policy standpoint, 70 percent of all property is residential, yet businesses pay the lion's share of property taxes when, in fact, residential properties generate the children who attend the schools. The Legislature probably does not have the intestinal fortitude to address that by increasing residential property taxes and decreasing reliance on business personal property taxes, but the matter could be reviewed at least from an educational standpoint. He said a major goal would be to make sure the gains that have been made to improve the property tax system over the last decade, especially in terms of assessment ratios and eliminating state property taxes, remain in place. Prior to 1980, mines paid 60 percent assessment ratio and utilities paid 50 percent. Those costs are passed on to customers who also pay residential property taxes, as well as property taxes from surrounding businesses that make up as much as possible in the cost of goods and services. A system that is fair, equitable, and reasonable should be structured, but knowing the political realities, he would be happy just to do no harm.

Ms. Daniels requested information on the amount of growth experienced in the last few years in enterprise zones. She said there have been discussions about eliminating some zones, which could not be done overnight, but there could be a phase-out or freeze on allowing other properties into a zone if much growth occurred; or if no growth occurred, the zone could be eliminated to simplify the system. She noted that the 5 percent assessment ratio made a huge difference in her district when Intel located a new plant. The zones were created to boost economic development in rural Arizona, but she has no idea how much growth occurred.

Senator Martin revealed that he was told by a financial person from Intel a few weeks ago that if the 5 percent assessment ratio were eliminated, Intel would abandon the billion investment because it would be cheaper to rebuild somewhere else than go to the 25 percent rate.

Ms. Daniels remarked that in order not to devastate businesses, it is necessary to plan for growth. It is important not only to do no harm, but to consider the possible consequences to everyone involved.

Mr. Clark expressed interest in finding a way to move from the 25 percent assessment ratio to parity with the personal property tax rate, but speculated that could only occur if homeowners received some benefit during the transition, such as a credit when taxes are done at the end of the year.

Chairman Huffman asked if more money is paid out in voter-approved secondary property taxes where businesses do not have a vote per se. Ms. Decker replied that the amounts would vary by district, but the charts on pages 16 and 17 (Attachment 2) show that growth in primary levies has been just over 350 percent during the 22 years while secondary levies doubled. For community colleges, special districts, and school districts there has been a rise in the use of secondary levies. There are many new special districts, which has the effect of not only applying that to the voters to approve more taxes when they are paying such a lower rate compared to businesses, but local governments also take that away from the primary rates, expenditure limits, levy limits, etc.

Ms. Daniels, referring to legislation that recently passed relating to special districts utilizing a sales tax levy and the hospital special district, wondered if more special districts will make the same request since a sales tax levy is easier to sell than a property tax levy. Ms. Decker responded that there has been some movement in that direction. The jail districts in Maricopa County and a few other counties use the sales tax, and now hospitals want to. That was one concern raised by the Arizona Tax Research Association during testimony on the hospital bill and others.

Mr. Smoldon suggested a review of the property tax system in relation to Students FIRST. Ms. Decker pointed out that the issue will be discussed at the next meeting.

Mayor Scruggs asked if the large percentage change in the primary and secondary levels for the cities could be attributed to a tremendous annexation of land from counties into cities during the time span shown. Ms. Decker acknowledged that would be part of the reason. She has not reviewed population changes, etc., but there are more incorporated cities now than in the 1980s, and many are larger, although population should offset some of that, but there are certainly many needs within the cities, especially expanding cities.

Mayor Scruggs opined that in viewing a 695 percent increase in cities' secondary levy, the percentage of growth of land within incorporated boundaries in 2002 compared to 1980 might be considered. The west valley and probably much of the southeast valley were not city during that time period so she believes the percentage gives a false impression.

She added that a comment was made that there is a large growth in secondary taxes and businesses do not get to vote on projects that are paid for with the secondary property tax. The other side is that many times businesses would not choose to locate in an area if the services provided by the secondary taxes were not available, such as police facilities, fire facilities, etc. Many businesses look for quality of life situations and do not vote other than employees who are residents of the area, but there is a direct benefit to the businesses.

Cochairman Huffman indicated that the recommendations made so far will be put in memo form and sent to the Committee. He asked that additional input be provided to Ms. Decker. Referring to the list of potential agenda issues (Attachment 4), he noted the Committee would probably not have that many meetings, but asked the Members to review and prioritize areas to review and let Ms. Decker know. He also requested that the Members advise Ms. Decker of any travel/vacation plans.

He asked if the Members would like to meet once every three weeks or once a month with work groups, pulling in other resources to work on suggestions from the broader Committee. If the Members prefer the latter, attending the meetings should be a priority so a substantial amount of work can be done. He added that statute states that the Committee is supposed to complete the work by September 2003, which will not happen, so the Committee will meet until session begins in January 2004.

Mr. Smoldon opined that the second option would be preferable for meetings, noting that most of the information is available, but decisions need to be made from a public policy standpoint what the Members are willing to fight for.

Mr. Tully said he would be interested in obtaining demographic information of Arizona versus other states, which would affect tax rates such as on a per capita basis, as well as projections on demographic expectations for the next 10 to 20 years. He added that the information would not have to be discussed during a meeting, but he could read it on his own.

Cochairman Huffman indicated that the Governor's Task Force will speak to the Members at some point, noting that the Task Force made some preliminary recommendations. In meeting with the group early in the process, interest was expressed to collaborate with the Committee.

Senator Martin stated that Bill Post, Chairman of the Governor's Task Force, indicated that his design for the Task Force is a long-term tax solution, whereas the Committee will be working not only on long-term, but also very short-term solutions. There will be some overlap, but the Task Force's efforts will not dictate what the Committee does.

Ms. Decker advised that the preliminary recommendations of the Task Force can be accessed on the Arizona Department of Commerce web site (azcommerce.com) on the research link, but she can also provide a copy with the memo to be distributed.

Without objection, the meeting adjourned at 10:25 a.m.

Linda Taylor

Linda Taylor, Committee Secretary
June 20, 2003

(Original minutes, attachments, and tape are on file in the Office of the Chief Clerk.)

ARIZONA STATE LEGISLATURE

TAX REFORM FOR ARIZONA CITIZENS COMMITTEE

Minutes of Meeting
Tuesday, July 15, 2003 – 1:30 p.m.
Senate Hearing Room 1

Members Present:

Senator Martin, Co-Chair	Representative Huffman, Co-Chair
Senator Waring	Representative Jackson, Jr.
Hon. Lori Daniels	Representative Tully
Bob Flach	Kevin McCarthy
Russell Smoldon	

Members Absent:

Senator Brown	Representative Clark
Senator Giffords	Hon. Elaine Scruggs
William Arnold	Hon. Andrew Kunasek

Staff: Denisse Gee, Senate Research Finance Analyst
Kitty Decker, House Majority Research Ways and Means Analyst

Co-Chair Martin called the meeting to order at 1:38 p.m., and roll call was taken.

PRESENTATIONS

Students FIRST Overview

Ed Boot stated he has been **Interim Director, School Facilities Board (SFB),** for the past year. Prior to that time he was with SFB for three years as Deputy Director. He noted that **John Arnold, Deputy Director of Finance,** is also present to answer any questions. Mr. Boot distributed a handout entitled "School Facilities Board" (Attachment A) and described the background and purpose of the Students FIRST program. He said SFB works with 220 of the 239 school districts in the State. He said that after a lengthy lawsuit, the Supreme Court ruled and directed the State of Arizona to do the following:

- Conform to certain school guidelines and criteria to bring existing facilities to standards.
- Construct new facilities as required for growing districts.
- Provide funding to maintain all school facilities at the adequacy level.

Mr. Boot indicated that SFB assessed over 8,000 buildings and 1,300 schools, and a significant number of problems and projects were discovered in the school districts. He described some of the deplorable conditions and the improvements that have since been made. He commented that Students FIRST became both a constitutional and a controversial issue. Mr. Boot highlighted the accomplishments of SFB since July 1999, and the requirements of the Deficiencies Correction Program. He indicated at this point SFB's estimate to complete the program is $1,284,000,000, which is $10,000,000 less than what was committed two years ago. He said all of the work has either been completed or under construction with the exception of certain projects mentioned.

Mr. Boot commented that the new construction fund is a revolving fund, which means it is ongoing. He said the new construction fund is based on student capacity and square footage, and he explained the mechanism and process for calculating an award for space. He also explained the difference between an urban and rural school district classification.

In response to Mr. McCarthy, Mr. Boot stated that all of the standards and guidelines were established by SFB. He explained that the amount of space per student is included in statute; however, SFB has a choice of where the square footage is applied. In response to Senator Martin, Mr. Boot explained the student/square foot classification makeup and the reconfiguration of space.

Mr. Boot commented on the new construction program and provided data in the handout on projected school openings. In response to Representative Huffman, Mr. Boot said that the law allows up to ten years in advance to purchase real estate for school construction, but generally SFB uses a three to four year timetable. He commented that an exception would occur in a fast-growth district where SFB attempts to stay at least one site ahead of what has been approved, and he provided examples of how that type of situation would occur. He said that SFB does not take any action to purchase land until a school district solicits SFB for a parcel of land based on the capital plan. He explained the timeline procedure for the approval and opening of schools. Representative Huffman voiced his concerns regarding the purchase of land in advance for schools that may never materialize. Mr. Boot responded that SFB is able to provide a list of every site purchased, and he explained the complexities of purchasing sites for new schools. He said it is anticipated that 193 schools will be opened by the Fall of 2009, with a projection of 136,000 new students moving into the State.

Mr. Boot explained the lease-to-own process and financing obligations. He noted that lease-to-own is good to use as a short-term method in a particular situation, but should not be viewed as the method to finance schools on a long-term basis because of the interest rates.

In response to Senator Martin, Mr. Boot explained that the school districts conduct population estimates and demography. The districts also provide a percentage growth rate by grade configuration for past years. He said SFB also has an on-board demographer as well as an outside demographer to assist and crosscheck to verify those numbers. In response to Mr. McCarthy, Mr. Boot elaborated on other school district funding mechanisms in addition to State funding as outlined in Students FIRST.

Representative Jackson asked Mr. Boot to explain any distinctions for schools located on Tribal lands. Mr. Boot responded that first of all, they are more expensive. He said although the law only classifies two designations "urban" and "rural," a third designation was included in the deficiency program called "remote." He noted that the price in the "remote" areas typically run 20% to 25% more. The second differential is that many of the Tribal lands have impact aid and federal funds, but do not have any taxability. He said SFB does not believe a lease-to-own program could be implemented. He said if a new school is required to be built as a result of growth in those areas, some legislative action will be necessary.

Mr. Boot explained that the building renewal formula was put into place statutorily to provide the school districts a sum of money every year to be used for capital repairs in their schools and facilities. He provided typical examples of how the formula works and explained the projections for future financial needs of SFB as outlined in the handout.

Mr. Boot concluded that although SFB is a controversial program, many accomplishments have been made in the last five years. He said he believes Students FIRST has benefited educators, students and citizens of the State, and the program has caused the school districts to focus on the condition of their physical plants.

Mr. Smoldon asked Mr. Boot how SFB oversees deficiencies going forward and any problems that may occur. Mr. Boot explained when deficiencies are concluded, there are several events that occur:

- Building renewal is in place for the districts to handle capital maintenance over time.
- SFB has requested all school districts to submit a five-year building renewal plan.
- SFB has implemented a preventive maintenance program for facilities in the districts.
- SFB has begun an inspection program of the schools, and a report will be compiled for the Legislature and the school districts.

Mr. Boot said SFB does not supplant local control, and the school districts have the ultimate choice of how to use the building renewal funds.

In response to Representative Tully regarding statistics on the affects of new schools and fixing deficiencies on school test scores for students, Mr. Boot indicated that SFB is in the process of concluding a second study of the affect of facilities on productivity and educational gains. He said SFB is also looking at whether the size of a school has any influence on test scores. At the request of Senator Martin, Mr. Boot said he would provide the results of the studies to the Committee upon completion.

Representative Huffman asked Mr. Boot to comment further on the adequacy of the statutory framework in place, and whether he believes further steps need to be taken. Mr. Boot responded that remarkable progress has been made through the Students FIRST and SFB. However, he said there are still problems with respect to preventive maintenance in the schools. He emphasized that it is within the purview of SFB to advise the appropriate individuals regarding the issues, but not in its purview to be able to fix all the problems. In response to Mr. Flach, Mr. Boot commented on the work being done to correct deficiencies. Mr. Flach commented that steps need to be taken to focus on managing the energy systems to reduce the utility costs, particularly in new schools.

Education Funding Lawsuits

Tim Hogan, Center for Law in the Public Interest, stated he would focus on property tax implications. He explained the original lawsuit was brought in 1991 because the old system forced school districts to finance their capital needs 100% from their local property tax base, which meant there were many disparities from district to district. Mr. Hogan described the two approaches to school finance throughout the country, which is the "equity" versus the "adequacy" approach. He provided an overview of the Court's decision in the Roosevelt versus Bishop lawsuit, and said the core requirement is that the State is responsible for ensuring that school districts have the schools that are necessary and appropriate for students to achieve the State's academic standards. He said that the minimum adequacy guidelines are derived from the core requirement in the Court's decision. He said that although there are some concerns of the districts to exceed the standards, he noted that the program is still in the early stages to know whether it will be a problem over time.

In response to Senator Waring regarding student achievement, Mr. Hogan explained the Court's legal requirements. He commented on the various guidelines and the research undertaken regarding the proper environment necessary for student achievement in the classroom. Mr. Hogan said the SFB program is about a fair financial system within all school districts and has dramatically changed the level of having decent schools for all children to attend. Mr. Hogan indicated he is also working on the maintenance and operation funding issues. In response to Senator Martin, Mr. Hogan stated that there is a trend nationally toward a cost-based system in the school districts that will most facilitate achievement of academic standards. In response to Representative Tully, Mr. Hogan explained the meaning of a "cost-based system," whereby policy decisions are being made throughout the country to arrive at what it takes to fund different variables in the school districts. In response to Representative Tully, Mr. Hogan explained how it is determined that a certain amount of dollars will be needed to educate students over a certain timeframe.

Senator Martin questioned whether the method of attacking the problem through the courts has prevented the State's ability to try other methodologies. Mr. Hogan responded with an offer that if the leadership of the Legislature is convened, he will place a hiatus on all the litigation and will figure out the proper methodology. He said he has made that offer for twelve years to the Legislature, but has never been taken up on his offer.

In response to Senator Waring regarding funds being spent, Mr. Hogan stated that voters were willing to support Students FIRST through tax dollars. He said the issue increases in importance to taxpayers when they realize that schools are in critical need of repairs, and safety in schools is essential for every child in the State. Mr. Hogan said that after allocating $1.3 billion to repair the schools, as a taxpayer he would question why money would not be provided to maintain those facilities and protect that investment. He said it just makes good economic sense. Mr. Hogan commented on the building renewal funding issue, and he noted that something will need to be done to address that problem.

Mr. Hogan commented on the dedicated funding source issue; however, he said each time a funding source is found, it is called a "tax increase." He said the real problem that the Supreme Court identified in its decisions is that the local property tax base has nothing to do with capital means. He noted that any time an attempt is made to relate property taxes with capital means, there will be disparities. He explained that if equalization is implemented using the same taxing authority in the wealthy and poor districts, then the problem is minimized. However, equalization becomes very expensive to implement, which is why there has been a struggle for years on this issue. He said a possible solution would be "power equalizing," which requires higher wealth districts to tax themselves more than needed when issuing bonds and to give the excess to the State for redistribution to poorer school districts. He commented that regardless of the approach utilized, it would be a new tax to someone. He suggested possible proposals such as a qualifying tax rate, a reinstatement of a statewide property tax, or a county tax, all of which would not be labeled a tax increase at the Legislature under a Constitutional amendment. However, obviously, for those paying, it would constitute a tax increase regardless of the legality associated with that type of tax increase. Mr. Hogan remarked that the property tax is a mathematical problem that will always exist, and that is why the Supreme Court identified other possible funding sources such as income tax or sales tax.

Mr. Flach commented he has researched other states regarding including maintenance as part of the general operating budget. He indicated that several states have resolved the problem by establishing a separate fund, such as Arizona has done with the building renewal fund and even combining the funds. He asked whether there is any legal concern with handling the funds in that manner. Mr. Hogan responded "no," and that the concept has been supported previously. He said the idea has always been to target the funding to where it should be applied. He commended SFB for its five-year plan and said it appears to be working well.

Mr. McCarthy commented that there is a misunderstanding among some people that when they talk about using property taxes to fund this program, they think about that in terms of returning accountability that existed in the old system of voter participation. He asked Mr. Hogan to comment on that issue as it relates to proposals that would have voter participation. Mr. Hogan responded he has only commented on one level of difficulty in using property taxation as a basis for a dedicated funding source. He said voter approval is a key problem using property taxation and for issuance of bonds or capital overrides. He noted that situations have occurred in the past where voters would not approve necessary capital projects in particular districts, which is problematic.

Senator Martin asked Mr. Hogan how to create a long-term funding mechanism that would not be affected by the economic cycles. Mr. Hogan responded the bottom line is that the State will need to take care of short-term problems. However, a substantial amount of funding could be deferred by excluding those short-term items. He said unless the funding is recycled, that method could quickly fall apart.

SFB Current Financing Structure and Possible Future Reforms

Michael Hunter, Vice President, Arizona Tax Research Association (ATRA), distributed a handout from the January 2003 issue of the ATRA publication (Attachment B) and provided a slide presentation (Attachment C). He commented that as Mr. Hogan pointed out, the State is now facing ongoing responsibility for facility construction and maintenance. He said since the general fund does not have the resources to fund these programs on a pay-as-you-go basis, the State resorted to debt financing. He talked about future debt financing, which includes lease-to-own and land trust debt financing. Mr. Hunter presented an overview of the current status of school district capital spending and a report of secondary property taxes since 1998. He offered options for resolving some of the problems. He said the State could either return to local funding by going back to the system prior to Students FIRST, or live with the Court's decision and simply finance Students FIRST. He highlighted the pros and cons of the various funding options as outlined in the handout.

Mr. Hunter pointed out that it is important to maintain State oversight and control, which is essential if the State is to keep Students FIRST. He said districts deciding when they qualify for new construction and levying taxes without a vote would be regrettable. He indicated that ATRA's recommendations are to keep, revise and fund the Students FIRST program.

Public Testimony

Jan Vincent Marino, individual, commented on a personal situation involving his residence in the Hayden Winkleman school district and the problems that he has endured because of the high taxes. He pointed out he has contacted various officials regarding the disturbing situation. He emphasized that tensions are mounting in the Hayden area because of the fear of homeowners in the school district of losing their homes. He said the Hayden school district is small with less than 500 students. The residence census is between 600 and 700 people total, and the bulk of them are elderly or poor. He noted that most of the students come from poverty-stricken families and need assistance. Also, most of the businesses in Hayden and Winkleman are gone and the area is in poverty with abandoned buildings. He said the situation has caused many residents to move to mobile homes or to leave the area and the State. Mr. Marino said his dream was to retire in rural Arizona; however, this situation has changed his goal.

Mr. Marino indicated that two out of five schools in the Hayden district are receiving failing grades. He said the student/teacher ratio is 7.6 students per teacher and the

State average is 21; however, the students are still receiving failing grades. He said this is a perfect example of a need for the State to take over control of the school district because it is not being handled properly at the local level. He stated that before consideration is given to raising property taxes, the State should look at the situation and tax burden in Hayden and Winkleman. He stressed that the people need assistance because it has become a dire situation for the residents. Mr. Marino suggested that the district boundaries be revised because there are not enough funds in the small district to support the school. He said he recently spoke to the new school superintendent who agrees that the high school needs to be closed. He commented that the school bond issue is a major problem. He noted that the total amount of dollars is approximately $29 million for an $8.5 million principle. He said the school owns property, which needs to be sold. Also, the school district needs to be consolidated with other schools and the high school is not necessary. He said community pride and investment needs to be encouraged in order to establish a tax base because the tax base has been eroded with more debt than equity in that school district. He urged the Committee to take a look at the entire sad situation.

Senator Martin thanked Mr. Marino and indicated the Committee is aware of the situation and noted at a recent meeting it was pointed out that Hayden Winkleman has the highest property tax rates in the State at 2.7% of value.

John Mitchell, individual, commented on his personal experience in purchasing a retirement home in the Winkleman school district. He said the taxing situation is ridiculous, and he emphasized that something needs to be done to correct the problem. He suggested combining all the school districts in the area into one school district with one administrative group, which would result in substantial savings. He said it may also be appropriate to consider eliminating local bonding and have one unified State school tax with everyone paying the same percentage. Mr. Mitchell said he has taken the steps to hire attorneys to bankrupt the entire school district under Title IX, and he explained the process. He said under the present circumstances, he does not see any other recourse. He commented that the debt will not go away, and a ghost town will be created if nothing is done.

In response to the question of ownership of the school, Senator Martin explained it is his understanding that once the school is built, title of ownership is turned over to the school district.

Mr. McCarthy stated that there are a number of statutes that allow school districts to do things differently. He said an example is the extra tax cost attributed to the transportation system in a declining school district, such as Hayden. He commended Mr. Mitchell for his interest, and encouraged more people to become involved in the process so changes can be made to improve the situation.

Gabriel Sandoval, individual, commented on a personal situation in the purchase of a home in Winkleman. He said the taxes are too high, and it is forcing his family and others out of the area. He asked the Committee for their advice on what to do. Mr.

McCarthy said the residents of Hayden are somewhat responsible for their fate and allowing bad decisions to occur over the past several years. He suggested making an effort to do everything possible to change the bad decisions in the past that led to the high taxes.

Roger Anstine, individual, referred to the comment made of mismanagement. He said most of the bond debt occurred as a result of the lost mines. He commented that next year the property taxes for businesses will be 50% over market value and other properties over 20%. He said he and others have attended school board meetings and conducted an audit of the school. He indicated as taxes increase, it also presents a problem in selling properties. He said he has a strong heritage and he is committed to this issue.

Mr. McCarthy clarified that there were many decisions in the past in the school district and town that should not have been made, when it became apparent that the bottom was falling out of the tax base of that town. He cited examples that took place in the sale of bonds, which was the result of mismanagement in the district.

Mr. Anstine stated he supports the decision to force the school into bankruptcy to correct the situation.

Senator Martin asked at what point did Mr. Anstine or others realize this situation was becoming a problem. Mr. Anstine responded he purchased his property in 1996 and soon thereafter problems developed. He said the current residents are in a dilemma while other wealthier individuals are purchasing depressed properties and stand to gain once the situation turns around.

Jean Slater, individual, commented on her personal situation regarding a business that she and her husband have owned for many years in the Hayden Winkleman school district. She said she noticed that her taxes were beginning to rise in 1997. At that point she and her husband decided to consolidate their two businesses in Kearny and Hayden because it was not economically feasible to maintain two locations. She commented on the taxes she has had to pay in both locations, indicating that Hayden costs three times as much. She noted that people moving to the area from out of State do not purchase properties in that area because of the high taxes. She commented that the bonding indebtedness for that school district far exceeds property values of that district. She cited examples of the deterioration of buildings in the area, and said the town of Hayden refuses to do anything. She pointed out that the total tax rate for the Hayden Winkleman school district and the town of Hayden is $44.81. She said at a recent meeting, the tax assessor informed her that the new tax rate would probably be a minimum of $50 or more. She stated that 99 properties out of 304 in the Hayden Winkleman area are currently in default because they have not paid the property taxes. She noted that many residents are either retired, widowed, widowers or disabled, and very few have children of school age; however, they are expected to foot the bill. She said many attempts have been made to discuss this situation with the school board; however, nothing is being done. She said on June 30, a payment was due on the bond for $99,000 and the trust only has $77,000. She indicated that the County had to borrow from another fund, which now has to be repaid.

Ms. Slater commented the residents are looking to the Committee for help because they have nowhere else to go.

Mr. McCarthy commented that there are communities in Arizona, larger than the town of Hayden, that does not have a municipal government. As a result, there is no tax burden associated with a government that does not exist. He said in the case of the school district, there are limited options as to whether or not the residents want the governmental entity that is taxing the residents. He said one option may be to consolidate with neighboring districts. Mr. McCarthy commented that if the residents disincorporate the town and become a part of the unincorporated area of Gila County, the residents are entitled to county services as county taxpayers. He said another option would be to take over the management of the town to reduce the expenses. Ms. Slater asked for assistance to find a way to help conduct a complete audit of the school system. She said the bonds were approved when the large mines were producing; however, the situation is different today with one mine remaining.

Senator Martin commented he would look into the situation and will meet with the residents after the meeting today to discuss it further.

Senator Martin thanked everyone for participating today. He announced that the next meeting has not been finalized. He said the third meeting on the updated schedule (Attachment D) will include an overview of the transaction privilege tax, use taxes, streamlined sales taxes and other issues. He said that meeting will take place in the House of Representatives in approximately three to four weeks and a meeting notice and agenda will be distributed. He suggested that if anyone has any questions to forward them to staff members.

There being no further business, the meeting adjourned at 5:30 p.m.

Respectfully submitted,

Nancy L. DeMichele

Nancy L. DeMichele, Committee Secretary

(Tapes and attachments on file in the Secretary of the Senate's Office/Resource Center, Room 115)

ARIZONA STATE LEGISLATURE
Forty-sixth Legislature – First Regular Session

TAX REFORM FOR ARIZONA CITIZENS COMMITTEE

Minutes of Meeting
Monday, August 25, 2003
House Hearing Room 3 -- 10:00 a.m.

Chairman Huffman called the meeting to order at 10:05 a.m. and attendance was noted by the secretary.

Members Present

Senator Brown	Representative Clark
Senator Waring	Representative Jackson
Senator Martin, Cochair	Representative Tully
William Arnold	Representative Huffman, Cochair
Lori Daniels	Kevin McCarthy
Honorable Andrew W. Kunasek	Honorable Elaine Scruggs

Members Absent

Senator Giffords	Russell Smoldon
Bob Flach	

Speakers Present

Kitty Decker, Senior Economist, Majority Research Staff
Michelle Ahlmer, Executive Director, Arizona Retailer's Association
Cathy Connolly, Executive Director, League of Arizona Cities and Towns

Opening Remarks

Chairman Huffman thanked everyone for taking time to attend the meeting.

Overview of State and Local Transaction Privilege Taxes

Kitty Decker, Senior Economist, Majority Research Staff, reviewed the following documents:

- Arizona Transaction Privilege & Use Tax Overview (Attachment 1).
- State and Local Transaction Privilege Taxes [or similar excise taxes] (Attachment 2).

Chairman Huffman requested an explanation for the growth of 43.1 percent to 49.9 percent in the general fund from transaction privilege tax (TPT) collections from 1993 to 2003 relative to other revenue sources (First Page, Attachment 2).

Senator Martin asked for information regarding elasticity of the different types of taxes over the last 10 to 20 years in order to know the volatility of the revenue sources.

Ms. Decker reviewed a handout regarding Transaction Privilege Tax (TPT) Exemptions (Attachment 3).

Ms. Daniels asked if data is available on whether specific businesses expanded because an exemption was provided. Ms. Decker responded that it would be a major undertaking to review legislation to see what was proposed, which has not been done in terms of the TPT; however, the Legislature did establish the Income Tax Review Committee last year to determine whether credits had an impact on the economy and should be retained.

Ms. Decker briefly described the following handouts provided to the Members:

- Transaction Privilege and Use Tax Expenditures (Attachment 4).
- Sales Taxation of Services: 1996 Update (Attachment 5).
- Streamlined Sales Tax Project Executive Summary (Attachment 6).
- Memo from Kenneth C. Behringer, Arizona Legislative Council, regarding Government Property Lease Excise Tax (R-46-52) (Attachment 7).
- Memo from Hans Olofsson, Joint Legislative Budget Committee, regarding Alternative Revenue Sources (Attachment 8).

In response to Mr. Clark's query about the progress of taxing Internet sales, Ms. Decker advised that since taxing is not done on Internet sales because of the Interstate Commerce Clause, representatives of various states formed the Streamlined Sales Tax Project (SSTP) to develop a uniform definition for taxing those sellers, etc. Since Arizona has a TPT with the burden on business rather than the consumer, Arizona is in a better position than other states to try to collect tax for all sales over the Internet. It is an issue, though, because it is not actually done on a uniform basis.

Mr. Jackson asked how much of the TPT collected on tribal reservations is returned to the state. Ms. Decker replied that she will check with the Arizona Department of Revenue (DOR). She is not sure the information can be obtained for all tribes, but a breakdown can probably be provided in some instances.

Chairman Huffman suggested that the Members consider developing guidelines as to whether or not something should be taxed, implications on the economy, and enforcement.

Ms. Decker remarked that most individual industry exemptions encouraged more activity, which was intended by the Legislature. For example, interstate phone calls are not taxed, but in-state phone calls are, so call centers located in Arizona because of the tax exemption, although some may argue that those are not the preferred jobs to attract.

Ms. Decker acknowledged that 13 states currently do not have a real estate transfer tax and indicated that she will provide further information.

Chairman Huffman stated that while working on the budget, he noticed that real estate was one of the industries still "rolling along" through the downturn in the economy. He advised caution when discussing potential revenue gains in comparison to the impact on the long-term health of the economy.

Ms. Decker recalled that the Fiscal 2000 Committee in 1989 recommended imposing a real estate transfer tax in Arizona, which resulted in boxes of postcards from people opposed to the idea. It was very unpopular and never "got off the ground."

Mr. McCarthy speculated that states with a real estate transfer tax do not have a prime contracting tax like Arizona. He added that people should not get the impression there is no taxation of construction when a significant amount of tax revenue is generated.

Mr. Clark asked Ms. Decker to advise of states with a real estate transfer tax and a construction tax. He would ultimately like to see data on the economic benefit of the present tax credits and exemptions. Ms. Decker replied that the latter would be very difficult to obtain, but she will provide whatever information is available.

Elaine Smith, Arizona Department of Revenue (DOR), advised that most of the numbers presented in the report relating to Transaction Privilege and Use Tax Expenditures (Attachment 4) were derived from census data brought forward to the current year. The census is conducted every five years and the most recent census published is from 1997. The 2002 census should be ready in the next year or two. In the report, information is available on services that are well represented. Information was obtained from the back of returns for the other exemptions, but no data is available on services with no information.

She indicated to Mr. McCarthy that opinions vary about what is considered an expenditure or exemption, but this information is available and can be characterized by people in whatever manner they would like. She surmised that a group effort with the Joint Legislative Budget Committee, legislative staff, etc., would be necessary to distinguish the expenditures in a manner that is more acceptable to more people. There are a variety of different reasons why each was established and researching those would be a helpful, but time-consuming exercise.

Chairman Huffman questioned if time would be better spent researching the policy behind whether something should be taxed rather than trying to quantify how much is not collected.

Mr. McCarthy agreed, but pointed out that this report influenced the debate in general about the amount of exemptions in the state sales tax system. People should understand, when looking at a report that suggests there is $6 billion in exemptions, but only $4 billion collected, that this is an exhaustive list of the economy, not the sales tax system.

Senator Martin remarked that a document showing the policy behind the expenditures would be invaluable to tax preparers. Also, a written published policy as to what qualifies as a tax would be a much better guideline. He added that many of the exemptions in the report were clarifications by the Legislature.

Chairman Huffman expressed interest in reviewing municipalities that collect the prime contracting tax and development impact fees for new construction, but have no property tax. Ms. Decker agreed to provide pertinent information.

Senator Martin requested national comparisons of the different revenue sources the state has per capita and tax burden data. He asked if the tax base is fixed at 2000 for Proposition 301 revenue.

Ms. Decker responded that the second page of the DOR report (Attachment 1) does not show the education .06 percent sales tax on a few taxable activities such as hotel/motel, and she does not know why. For the most part, it is tied to the tax base, and if the tax base were expanded, the education .06 percent sales tax would have to be expanded to any other services of interest. Whether the tax base automatically adjusts whenever changes are made would depend on how the language is written. She would have to obtain a legal opinion on whether the purpose of the act would be furthered and a three-quarters vote required as opposed to a two-thirds vote.

Senator Martin referred to the list of TPT exemptions (Third Page, Attachment 3) and questioned if "pipes or valves four inches in diameter used to transport oil, natural gas, artificial gas, water, or coal slurry" should be changed to read "four inches OR LARGER" considering the recent incident involving the gas pipeline from Tucson.

Streamlined Sales Tax Project

Michelle Ahlmer, Executive Director, Arizona Retailer's Association, expressed support of the SSTP and the agreement adopted last November, which allowed a group of tax administrators to develop a framework from which states and local jurisdictions can determine the tax policy that should be in place. She said this is not an effort to eliminate tax policy decisions from the state or local jurisdictions, but people who collect sales tax on a multi-jurisdictional basis, whether across state lines, county lines, or city lines, would have a definite framework to work within. Some of the items provided are:

- Uniform definitions.
- Uniform bases between states and local jurisdictions.
- Rate simplification.
- Taxing at the point of destination.
- State level administration of the tax.

She noted that the Members were provided with the "Streamlined Bible" written by members of the SSTP who will probably be on the governing body within the project (Attachment 9).

Ms. Ahlmer stated that the SSTP provides ease of a burden that is overwhelming to people with multi-state sales tax collection responsibility and the opportunity to collect Internet sales tax. The Internet is doing a remarkable increase in business, which is going to continue. It has been a huge benefit for individuals, but has caused competition for Main Street retail that is difficult to overcome. The SSTP would allow retailers to take advantage of certified collection by third party administrative-type businesses that would handle sales tax collections and allow the retailers to sell. She added that it is also a fairness issue for the taxpayer and local jurisdictions. It is important to her to support the small community she lives in, not only the small independent retailers, but by sending sales tax dollars back to the city where she drives on the streets and sends her daughter to school, which is supported by Proposition 301 funds. It would be inappropriate for her to purchase items from the Internet and still drive back and forth to work on the roads and send her daughter to school, which she would not be financially supporting.

Ms. Ahlmer clarified that under the SSTP, if merchandise is purchased and carried out of the retail establishment, the sales tax would be paid at the point of sale. If the item were delivered, the sales tax would be paid at the point of destination. This would be a dramatic change for prime contracting and even pizza delivery. If someone lives in Mesa and shops in Scottsdale, if the item is taken from the store, the Scottsdale rate would be paid, but if that person buys a refrigerator that is delivered, the Mesa rate would apply.

When Chairman Huffman asked if every retailer would be legally responsible for knowing the tax rates for every possible taxing jurisdiction, including special districts for jails, hospitals, etc., for items that are delivered, Ms. Ahlmer agreed. She added that if Arizona enters into the agreement, there would be a certified third-party administrator (if that route is chosen) for which a software program was created that is ready for distribution. DOR would be responsible for having a database available for certified providers or large retailers that wish to create their own system, which would be approved by DOR, to submit the sales tax. DOR would be responsible for keeping the database up to date.

When Chairman Huffman asked how the TPT distinction for Arizona can be dealt with since theoretically businesses collect the sales tax as part of a transaction, Ms. Ahlmer agreed that Arizona is unique in that factor. She understands the most significant potential damage would occur with any contract or sale made to the federal government; however, that would be captured in Internet sales taxes. She indicated that major employers would not lose the contracts or revenue because the TPT is passed through. Arizona may be pushed to change to a sales tax state, but the distinction is what the court would require. The State of California was operating enough like a sales tax state that the court required the change from TPT to a sales tax.

Chairman Huffman asked, since there would be a reliance on capturing much money from Internet sales, what could be done to make sure retailers conducting transactions in other states and jurisdictions collect and send the taxes to DOR. There could potentially be situations where transactions originate in foreign countries and products are delivered to Arizona. Under the SSTP, it would be done through the auditing process in the state where the retailers' headquarters are located and there is a physical presence. Regarding offshore retail distribution, etc., from what she has been told, the hoops that would have to be jumped through to go through Customs would not be worth the effort.

Chairman Huffman asked if the federal government contemplates hiring federal agents to make sure people are actually paying the taxes. Ms. Ahlmer responded that she does not believe the federal government would be dedicating resources for that purpose. There would still be local authority at the state level to administer this so enforcement would be required by DOR if the company is located in Arizona, and any auditing performances after that.

Mayor Scruggs observed, as a consumer, that she is not sure it is true that businesses over the Internet have a competitive advantage over a Main Street business, for example, because the shipping and handling charges are high when a tax is added. There must also be a reason why she constantly receives e-mails from Wal★Mart to buy on-line, perhaps an easier distribution system.

Mayor Scruggs noted that many cities have additional incremental tax rates through citizen initiatives and ballot votes, and it sounds like there could only be one rate and not a combination under the SSTP. She questioned if the streamlined tax rate would override all previous citizen initiatives and whether citizens would lose the right to bring forward initiatives for taxation for specific purposes. Ms. Ahlmer answered that citizens would not lose the ability to bring forward initiatives. Cities could have as large a rate as they want or a combination of the existing rates created by initiatives, but there would be one rate, and as new initiatives appear, those rates would be added. If an initiative ends at a specific time, the rate would be reduced by that amount. The difficulty would be if a product or transaction is currently taxed at one-tenth of a percent, it would be assessed at the overall rate. The state has the opportunity to have two rates, but cities can only have one.

Regarding competitive disadvantage on the Internet, Ms. Ahlmer opined that it depends on the industry. For example, many furniture manufacturers have Internet presence and are not charging shipping or tax so the furniture store is basically becoming a showroom. Meanwhile, that main street retailer is contributing to the tax base through income taxes, property taxes, employee taxes, Little League contributions, etc., which is where the competitive disadvantage occurs.

Mr. Clark questioned if having the sales tax collected at the point of delivery would give states the incentive to import. Ms. Ahlmer responded that she does not believe so because while it is convenient, many people prefer to try on clothes, and therefore do not want to buy clothes on-line. There is still the incentive of shopping generated by tourists, and even though somebody would go to the store and carry the item out, if it is shipped to their home, the tax would be paid at the point of destination where it is currently not paid. There would still be an incentive to have storefronts.

Senator Martin commented that multiple tax bases are probably the greatest impediment, other than high rates, to business growth in the state. That aspect needs to be reviewed and reformed whether or not the SSTP is adopted.

Cathy Connolly, Executive Director, League of Arizona Cities and Towns, asked the Members to keep in mind that virtually nothing can be done as a Committee looking at the tax structure that does not have some impact on local government in Arizona. She stated that arguments for the SSTP are that it would be easier for businesses to comply and the "pot of gold at the end of the rainbow" called Internet sales tax is enough for the state to totally change the tax structure in relation to the current TPT. This would be a massive change. A group of people at the national level would decide on tax policy for the State of Arizona, and it is unbelievable that the Legislature would be willing to give up that kind of authority to people who are not elected. There is no question that the sales tax would be easier to administer with one national base, one set of uniform definitions, etc., but there would be a tremendous cost to the state and an even bigger cost to local governments. Currently, a business has one set of administrative procedures, including joint auditing with DOR, and lots of different items that make it easier for businesses to comply with the local sales tax, so there is already much ease in administration in terms of the tax structure in Arizona.

Ms. Connolly related that in regard to the "pot of gold at the end of the rainbow," there is no particular reason to believe Congress will authorize a tax on Internet sales. Congress is currently in the process of passing a permanent extension of the moratorium on the tax on access to the Internet. Senator John McCain is one of the principal proponents of the extension and strongly believes that if Internet access is taxed, the Internet process will be damaged. She added that she has seen figures on what changing from a TPT state to a sales tax state would mean, which is a quantum leap for Arizona. Moving from point of sale to point of destination is a huge jump that would have all types of different impacts. Local governments are particularly concerned about other items that relate primarily to the TPT issue:

- Arizona receives much money from the TPT on contracting, which fast-growing local governments depend on to fund basic services for new home construction. Some communities have very small retail bases that receive huge dollars from the contracting TPT at the local level. That disruption alone would really be an issue for many of the communities.
- There are small and large communities in Arizona and the vast majority of cities and towns still tax food. In some of the small communities, such as the White Mountain area, the only large business is a grocery store, which is utilized by people in the community and people passing through, etc., so a huge percentage of the local sales tax is derived from the sales tax on food. The SSTP does allow states, in order to accommodate the local sales tax on food, to pass a sales tax on food at a zero rate, but she does not know if the Legislature would pass that because there is a great deal of sentiment against it. Cities would be at the mercy of a future Legislature possibly repealing that.
- It appears from the SSTP documents that there will be a lot less auditing than is currently done to the point that some transactions may not even be audited, which should be considered.
- Regarding administration of the tax, 12 of the 87 cities and towns in Arizona still administer their own local sales tax under the same administrative procedures, processes, etc. Under the SSTP, there would have to be a single source of administration, which presumably would be the state, and that is an issue. There is strength in local enforcement of the tax.

Ms. Connolly added that ease of administration and the potential "pot of gold at the end of the rainbow" are not enough for the state to be jumping into any SSTP legislation. There is no particular detriment to being the last state to adopt the SSTP because the board is already seated and there is no more room on the board. The potential detriment to the state and local government in Arizona is an argument against the SSTP. Arizona is different, which is good.

Mr. McCarthy pointed out that the Supreme Court could reverse the decision that Internet sales is a violation of the Commerce Clause instead of action being taken by Congress. He questioned if the cities' local auditing teams would be auditing Arizona taxpayers to find out what liability they may have as a result of the court decision being reversed. Ms. Connolly replied that there is much evidence that Arizona might lose more even if the "pot of gold" is authorized than would be gained by the SSTP; but if the Supreme Court were to reverse the decision, she presumes the state and cities would tax Internet sales. Currently, any business can ask for a joint audit, although it is not required, but a single auditor audits for the state and all of the jurisdictions, so she would not anticipate hordes of tax auditors arriving on anybody's doorstep.

Mr. McCarthy asked about the burden on the state by having the cities become part of the state system. Ms. Connolly answered that some taxpayers are probably not on the state rolls so certain categories would probably be lost by cities with a streamlined sales tax. The sales tax accounts of the cities would have to be checked to see who is not on the state rolls but may be on the local rolls. For example, the vast majority of cities still tax commercial real estate transactions, and there may be the possibility under the SSTP for that to remain taxable, but the state will not reimpose the tax.

Senator Martin asked if there is a policy in place so that if the state were to broaden the tax base, cities and towns would follow suit with similar equitable reductions, or legislation would be needed. Ms. Connolly answered that in the last five to seven years, when a change has happened to the state base, the cities and towns worked with the business community to decide if the Model City Tax Code (MCTC) should be changed as well. The vast majority of changes the state has made to the tax base have consequently been made to the MCTC. Changes to the MCTC go through the Municipal Tax Commission established by the Legislature, even on issues of conformity, and individual cities conform their tax codes within about eight months.

Ms. Connolly stated that nothing would require cities to reduce the rates so there might be very different results depending upon the jurisdiction. In larger broader-based communities, the impact of broadening the base on the state would probably be the same, but in some other communities, depending on what the base is broadened to, there might not be any impact on a particular jurisdiction. The local jurisdiction needs to analyze the probable impact and decide if a reduction is merited in the local TPT tax rate.

Ms. Daniels remarked that when this process began three years ago, she said Arizona would probably be the last state to ever pass this because of the unique structure with the local governments. Ms. Connolly is proud the state has kept local control in the TPT arena. She would be also if the state were in the bottom in the rate structure, but it is in the top five, and she is not very proud of that.

Next Meeting

Chairman Huffman conveyed that a report is due in September 2003, but he and Senator Martin would like to continue meeting through the next Legislative Session. Discussions will be held prior to the next meeting to develop some method of gathering the information provided and developing recommendations to forward to the full Committee. He added that the next meeting date has not yet been chosen, but the Committee will probably meet next month.

Without objection, the meeting adjourned at 12:09 p.m.

Linda Taylor

Linda Taylor, Committee Secretary
September 11, 2003

(Original minutes, attachments, and tape are on file in the Office of the Chief Clerk.)

ARIZONA STATE LEGISLATURE
Forty-sixth Legislature – First Regular Session

TAX REFORM FOR ARIZONA CITIZENS COMMITTEE

Minutes of Meeting
Wednesday, October 22, 2003
House Hearing Room 4 -- 9:00 a.m.

Chairman Huffman called the meeting to order at 9:15 a.m. and attendance was noted by the secretary.

Members Present

Senator Brown
Senator Giffords
Senator Waring
Senator Martin, Cochair
Lori Daniels
Representative Jackson
Representative Huffman, Cochair
Bob Flach
Kevin McCarthy
Russell Smoldon

Members Absent

William Arnold
Honorable Andrew W. Kunasek
Honorable Elaine Scruggs
Representative Clark
Representative Tully

Speakers Present

Brian Schmitz, Fiscal Analyst, Joint Legislative Budget Committee
Richard Stavneak, Director, Joint Legislative Budget Committee
Ken Behringer, General Counsel, Arizona Legislative Council
Alan Maguire, President, Maguire Company
Kitty Decker, Senior Economist/Majority Research Staff

Opening Comments

Chairman Huffman anticipated that two more meetings will be held, with the next meeting focusing on public input and recommendations from the Members. He expressed hope to have a final meeting and report in early December 2003. He noted that information from the previous hearings is intended as a starting point for discussion, and he will be talking to individual Members and others about developing recommendations for December. He added that if anyone would like to have research done, questions answered, or make recommendations for consideration, it should be done now.

PRESENTATIONS

Brian Schmitz, Fiscal Analyst, Joint Legislative Budget Committee, reviewed a handout regarding the Budget Stabilization Fund (BSF) (Attachment 1). He advised Ms. Daniels that if the BSF formula had been based on inflation plus population, the balance at the end of FY 2003 would be $688 million. The maximum size of the BSF would have been about $1.7 billion at the end of FY 2001; in FY 2002, $692 million would have been withdrawn; and in FY 2003, $292 million would have been withdrawn, so $688 million would still remain.

Richard Stavneak, Director, Joint Legislative Budget Committee, related that the numbers were constructed to provide a perspective of baseline revenues before any tax law changes, so all of the money was not actually available during that period of time.

Mr. Smoldon referred to the statement that the maximum BSF balance is limited to 7 percent of general fund revenue and asked what the highest cap is. Mr. Schmitz responded that the highest cap he has seen is 10 percent. He offered to provide a study by the National Conference of State Legislatures (NCSL) describing BSFs in other states.

Mr. Stavneak reviewed a handout regarding Corporate Income Tax Credits (Attachment 2), noting that a memo describes the findings in a more narrative fashion (Attachment 3). He related to Chairman Huffman that due to the confidentiality situation, the only data available to JLBC is the number of companies claiming a credit, the total dollar value of the credit, and the total amount of the unused carry forward. There are a few other specific examples where the statute makes it clear that companies are to record the number of jobs created, such as the enterprise zone or defense restructuring, but in most circumstances, that kind of individual information is not available.

He clarified for Ms. Daniels that due to confidentiality restrictions, the Arizona Department of Revenue (DOR) still provides accumulative information on credits that may be tied to a specific company as long as there are enough companies claiming the credit that he could not tell specifically who is receiving the credit.

Chairman Huffman commented that in attempting to repeal a tax credit for recycling equipment last year, the credit was claimed by so few people that data could not be obtained. Additionally, Proposition 108 applied because repealing the credit added about $1,500 to the general fund. Legislators who signed no tax increase pledges had to be convinced to vote for the repeal.

Mr. Stavneak advised Senator Giffords that the Joint Legislative Income Tax Credit Review Committee met last year, but has not met this year. The intent is to meet annually to review four or five credits on a cycle. Emphasis in this discussion includes corporate credits, but individual income tax credits can also be included. Last year, the Committee reviewed credits and legislation was passed placing those credits at the end of the cycle, but he does not believe any changes were made other than the one mentioned.

Kitty Decker, Senior Economist/Majority Research Staff, agreed that the Committee met once, and related that since it was the first year, issues were raised about how much data is available and the usefulness of the data. The recycling tax credit had already been repealed at the corporate level, but not the individual level, so the credit was being claimed by only a few people. There were some other glitches, such as what to do with the credits that were reviewed and no action is taken, so legislation this year placed those back on the schedule and attempted to clarify other issues in terms of running the Committee.

Senator Martin added that the Committee also has not met this year because Members need to be reappointed due to losses from the previous year.

Ms. Decker stated that another issue is that DOR does not release new credit information until mid-November, so a meeting will be scheduled in late November or early December 2003.

Chairman Huffman conveyed that it was important to set up a reasonable process so everyone knows what is going on and avoid the appearance of instability that could cause companies not to make changes in investments.

Mr. Stavneak advised Mr. McCarthy that in 2000, due to confidentiality issues, information could not be obtained on credits for agricultural water conservation, alternative fuel delivery systems, environmental technology facilities, solar hot water, and taxes paid for coal consumed in generating electric power. He agreed that the total of those is the difference between what is reported to JLBC and the $33 million used or refunded to companies, which he can provide.

Mr. Smoldon, referring to pollution control devices and coal consumption, submitted that there may be instances where certain types of manufacturing or power production, etc., could not continue to operate without some type of credit. Mr. Stavneak responded that the original purpose of the credits has gotten lost over time, and part of the purpose of the Joint Legislative Income Tax Review Committee is to memorialize some of the purposes and decide if there is a means for reevaluation. He added that the credits scheduled for review this year are research and development, pollution control, coal consumed in generating electric power, and underground storage tanks.

Senator Martin asked if other states grant special inclusion within the confidentiality laws for elected officials. Mr. Stavneak answered that he will follow-up with the NCSL to see if there are examples in other states.

Government Lease Excise Tax and Possessory Interest Tax

Ken Behringer, General Counsel, Arizona Legislative Council, stated that property owned by a government entity is exempt from taxation under the constitution, but if the property is mostly leased with a private entity, there is an issue as to whether the property should be subject to tax. On one side, the entity is using its tax advantage to promote public good, such as tourism, spring training baseball, or economic development, but on the other side is the question of what it does to the property tax base. If the property tax burden is shifted away from the private entity to competitors or individuals, some of the liability for school property taxes could be shifted to the state in state aid.

He related that there was no property tax on possessory interests for years. Maricopa County filed a suit and tried to assess the tax against the Fox Theater downtown, which was located on city land. The court acknowledged that possessory interests is a taxable interest, but the Legislature did not set up a mechanism to tax possessory interests; therefore, Maricopa County cannot assess the tax.

Mr. Behringer said in the mid-1980s, there was an expansion of activities by cities and towns to purchase property to use for economic development, etc., but because of the concern that it would negatively affect the tax base, in 1985, effective in 1986, the first property tax on possessory interests was enacted. As part of that, the Legislature exempted certain types of possessory interests, and under the constitution, every property is subject to tax unless it is exempt. About six years after the possessory interest tax went into effect, one of the taxpayers challenged it dealing with state, city, and private properties where the Scottsdale Princess is located. The Scottsdale Princess claimed discrimination. One of the exemptions allowed was from prior existing leases before April 1, 1985, and the Scottsdale Princess said it is not any different than the property used by a competitor with a tax exemption while they did not have an exemption. Instead of granting the tax exemption to the Scottsdale Princess, the court struck down all tax exemptions, so the Legislature tried several times to find a solution that was constitutional but met the policy requirements of exempting certain properties.

Mr. Behringer related that a few court cases went back and forth while the Legislature was working, and finally, the Legislature eliminated the possessory interest tax and assigned a Committee to study the issue, which resulted in a recommendation for the government property lease excise tax. It is an excise tax, not a property tax, that was created to mimic the property tax by assessing the tax on the lease based on approximation of value. The approximation is determined based on square footage of the building, which varies depending upon whether it is an office building, the number of floors in the office building, use of the building, and reductions for the age of the building. It is a rough approximation of an ad valorem tax, but it is an excise tax, which moves it out of the constitutional restrictions. He added that included in the government excise tax are exemptions similar to what the Legislature was attempting with the property tax on possessory interest.

After some discussion, Mr. McCarthy asked if the county assessor or someone with expertise could address the Committee and calculate what would be paid for a particular project in ad valorem taxes versus the government property lease excise tax to determine if the government property lease excise tax, which was put into effect to stop cities from using the tax exemption for redevelopment or economic development, is actually accomplishing that purpose.

State Bonding and the Constitution

Alan Maguire, President, Maguire Company, stated that in Arizona, like most states, the constitution limits the general obligation debt issued by the state, county, and cities, and two characteristics constitute a debt: 1) an obligation secured and repaid by general revenues (property taxes); 2) a multi-year obligation. The State of Arizona, through various authorities and commissions, borrows a significant amount of money, but those borrowings are not limited by the Arizona Constitution since they fail to meet one portion of the two-legged standard.

He explained that a number of borrowings are undertaken that are not perceived as secured and repaid by general revenues called special revenues, which is derived from the source of payment or segregation of those monies into a special fund, and those are not debt under the Constitution. For example, the highway user revenue fund (HURF) is routinely bonded against by the

State Transportation Board, and that has been upheld by the courts because it is a dedicated source in the Constitution, i.e., money collected from streets, roads and highways are dedicated to the HURF. It is a separate source from the general fund, and therefore, not general revenues, and it is constitutionally dedicated. Another example is the Arizona Board of Regents (ABOR), which is the issuing agent on behalf of system revenue bonds issued by the universities. The bonds are secured by the university system, primarily tuition payments. The courts, in permitting those bonds to be issued and not counted as debt under the Constitution, said there is a separation that exists between the general State of Arizona and the ABOR because the ABOR is specifically established in the Arizona Constitution as separate from the general fund and general operations of government; therefore, it is not subject to the constitutional provisions on debt.

Mr. Maguire related that many borrowings fall outside the Constitution because they are not multi-year obligations, instead the repayment is subject to annual appropriations. The most common examples are lease-purchase agreements or lease-to-own arrangements.

He added that the tradition of the two-tiered test has held fairly strong in Arizona. Cases are now quite old and have not been overturned, but in other states, efforts have been made to redefine both of the standards to constitute a debt.

When Mr. Smoldon asked how SFB bonding meets the general revenue test, Mr. Maguire answered that the argument has been that those are special dedicated revenues, but there is some lease purchasing as well, so the SFB uses one standard to exempt portions of activity and the other standard to exempt other portions of activity.

Mr. Maguire responded to further questions posed by the Members.

Discussion

Ms. Decker remarked that about a month ago, an article appeared in the *New York Times* regarding the fact that due to September 11, projects with 30-year debts could not be paid off, but had to be refinanced and now will not be paid off until 2024.

She reviewed handouts regarding Property Tax Levy Limits/Expenditure Limits (Attachment 4), County Funding Structure (Attachment 5), and Full Cash Value (Secondary)/Limited Value (Primary) (Attachment 6).

Mr. McCarthy pointed out that any recommended changes relating to full cash value and limited value would require a constitutional amendment.

Mr. Maguire related that he wrote the language of the constitution for levy and expenditure limits for special districts in 1980 due to a clear, almost uniformly broad-based perception that in the absence of a specific act by the Legislature, Proposition 13 would pass in Arizona. While the effects in California were fairly substantial, there would have been a much more dramatic impact in Arizona by virtue of the property classification system. In addition to constraining future collection of taxes, it would have also equalized all valuation processes, tremendously shifting taxes between businesses and individual homeowners. Since those effects would have been fairly dramatic, the Legislature spent two years determining how to deal with the issue, and ultimately, enacted different, fairly complicated measures.

Mr. Maguire stated that tremendous inequities exist in California now as a consequence of the way Proposition 13 was written. When Arizona was confronted with that, there was an extensive policy debate and a significant difference in the views of the House and Senate on how to do those limitations, which is why the provisions ended up as they did. Each component of the expenditure limitations and levy limitations can be tied to some aspect of Proposition 13.

He conveyed that one of the clearest errors of the 1980 enactments was the 1 percent limitation on residential values, which was strictly an attempt to echo Proposition 13, and has proven to be a mess. It causes the same kind of distortions between taxpayers that everyone wanted to avoid through the complex levy limit process and not the Proposition 13 model. He recalled a lengthy debate in the basement conference room that lasted for several days as to how long the combination of expenditure limitations on local government and the levy limitations would last. Most people thought that putting the system in place for seven or eight years to get past the groundswell of anti-tax fever coming out of California would be sufficient to allow for a reasonable debate about how to structure fiscal policy in Arizona and implement something else; however, the system still exists 23 years later.

Ms. Daniels asked if the possibility was ever discussed that once the 1 percent constitutional cap was put into place, the chances of going back to the voters and eliminating it would be slim to none. Mr. Maguire responded that there was extensive debate at the drafting and policy level on the Floor of the House and Senate as to what provisions ended up in the constitution and what did not, and a wide variety of laws were initially enacted in statute upon passage of the constitution to avoid problems. There was a perception by some very important individuals that if the 1 percent wording was not in the constitutional language, people would view it as being different than California.

Closing Remarks

Mr. Huffman encouraged everyone to review the information provided, noting that a short summary of what the Committee has been working on is included (Attachment 7). He said he will be talking to people to begin the process of putting together recommendations to take action in early December 2003.

Senator Martin requested feedback before the next meeting.

Without objection, the meeting adjourned at 10:55 a.m.

Linda Taylor

Linda Taylor, Committee Secretary
October 24, 2003

(Original minutes, attachments, and tape are on file in the Office of the Chief Clerk.)

ARIZONA STATE LEGISLATURE

TAX REFORM FOR ARIZONA CITIZENS COMMITTEE

Minutes of Meeting
Tuesday, November 25, 2003 – 9:30 a.m.
Senate Hearing Room 1

Members Present:

Senator Martin, Chairman
Senator Giffords
Senator Waring
Senator Brown
Ms. Lori Daniels
Hon. Andrew Kunasek
Representative Clark
William Arnold
Russell Smoldon
Bob Flach
Kevin McCarthy
Hon. Elaine Scruggs

Members Absent:

Representative Jackson, Jr.
Representative Tully
Representative Huffman

Staff:

Denisse Gee, Senate Research Finance Analyst
Kitty Decker, House Majority Research Ways and Means Analyst

Chairman Martin called the meeting to order at 9:36 a.m. and attendance was noted. He announced the purpose of the meeting is to take public comments on the draft report recommendations (Attachment A).

Public Testimony

Barry Aarons, Americans for Tax Reform (ATR), stated his remarks would also include comments from clients who have a specific interest in this issue. He commended the Committee for its work thus far and indicated that in a recovering economy increasing taxes tend to impede capital formation. As a result, job creation is stifled creating a situation of providing a restriction of the recovery. He noted that there appears to be a tremendous reliance in the State on sales taxes, which is a very difficult tax to manage. Mr. Aarons stated he has been working with a coalition of 17 to 24 organizations and corporations that have been meeting recently to oppose the possibility of expanding the tax base with a service tax.

Mr. Aarons pointed out that according to the League of Arizona Cities and Towns, the actual average State rate for an aggregate transaction privilege tax (TPT) is 8.47%. He noted that he served for a brief period as a member of the Model City Tax Code Commission, which was a potential solution to the concept of a uniform tax base.

Mr. Aarons provided examples of the impact of service or consumer taxes on the health services industry, pest control industry, legal services, and personal services. He indicated that taxing some consumer services would add additional costs to industries that are in the process of recovering and would be placed in a competitive disadvantage such as with hotels or the tourism industry. He referred to property tax and said ATR would endorse a unification of the assessment ratio because over the long-term there would be more opportunities.

Mr. Aarons commended the Committee on resisting the temptation of moving in the direction of expanding the sale tax base and urged the members to avoid any discriminatory aspect on this issue.

Mr. McCarthy commented that it would be a bad thing to add the service tax only to the State tax base versus adding it at the same time to both the State and City tax base. Mr. Aarons responded that he agrees with that concept and provided examples, such as with the "mom and pop" small businesses.

Mayor Scruggs pointed out that significant improvements have been made as the result of Senator Daniels' committee of a few years ago regarding the auditing procedure; therefore, it no longer is a horrendous experience. She said a uniform document has been established and is available over the Internet that treats every city the same. Mr. Aarons responded that he is happy to know that the auditing procedure has improved and thanked the Honorable Scruggs for her comments.

Mr. Smoldon referred to a presentation by Elliott Pollack recently where he said there would not be a significant impact if the service tax was only limited to personal services, such as food or nail and hair salons. He asked Mr. Aarons to comment on how that concept would affect the small entrepreneur. Mr. Aarons responded that an 8.5% service tax increase on consumer activities would be very dramatic. He said despite the fact that there may not be major auditing problems, the cost of collecting and remitting taxes for a small business is very dramatic. He said assessing that service tax on small businesses would perpetuate the same discriminatory sales tax practice that is generally opposed. He suggested the decision is whether to impose a flat gross receipts tax statewide including all political subdivisions with a possible rebate on certain items to end the discrimination, but not to impose it piecemeal on certain industries. Mr. Aarons noted that Dr. Pollack generally talks about the macro economic theory, whereas he is referring to the micro economic theory that affects the average individual's pocketbooks.

In response to Mr. Flach, Mr. Aarons explained the concept of assessment ratio unification and flexibility.

John Colton, general contractor, commended the Committee for the great job it is doing and said tax reform is a critical area. He noted he has attended many meetings where the focus is on more revenue and reform on taxes, but not much is discussed on the critical issue of the excessive cost of government. He believes each department head should be accountable for cost control.

Mr. McCarthy said he agrees with Mr. Colton. He said the State is approaching a billion dollar deficit and there are two committees studying taxes, but no one is studying spending.

Senator Martin noted many hours have been expended in the Special Session in an attempt to learn what is being spent on Child Protective Services (CPS) issues, and it is almost impossible to obtain the necessary information needed to be able to determine where to control costs.

Mark Minter, Executive Director, Arizona Builders Alliance (ABA), commented on the application of sales tax on design in the construction industry. He said it is not included in the report, but ABA believes the Arizona Department of Revenue (DOR) is misapplying the tax code. He noted that the Legislature has designed a tax code, and construction is defined as a taxable activity. However, the Legislature has determined that "design" is not taxable as a service. He added that architecture and engineering services are design services. He commented that several years ago some project owners began combining construction and design called "design-build construction," which has worked quite well. He remarked that in the early 1990's DOR assessed a contractor who had a design-build contract for the design portion of the contract; therefore, taxing architectural services. He said the case went through the court system, which further confused the issue. He pointed out that the Legislature recently changed the procurement code in Arizona to allow the use of design-build along with other forms of procurement, and the Arizona Department of Transportation (ADOT) is probably the largest user of this system today. Mr. Minter is hopeful that legislation will be introduced dealing with this issue, and hopes that this Committee addresses it in its final report by recommending adoption of clarification in this area.

Mr. Smoldon commented on a situation pertaining to purchase of appliances at a major outlet and noted that contractors purchase the same appliances tax-free. He asked whether there is a more uniform way to collect those types of sales taxes. Mr. Minter responded that Arizona is only one of two states that uses the system of indirect taxing of material that is incorporated in a construction project. He said New Mexico is the other state. He pointed out that most other states tax the contractor at the point of sale the same as a consumer. He noted that Arizona's system operates more like a value-added tax. Mr. Smoldon commented that it is important to fix the problems as discussed and make taxes as transparent as possible so that people will realistically know the costs of running the government.

John McNamara, Regional Tax Director, American Telephone and Telegraph (ATT) referred to the section in the draft report regarding the Committee's recommendation that the reductions or elimination of the business personal property tax not be applicable to centrally assessed telephone companies (Page 3, second paragraph under "Reduce Business Personal Property." He said, obviously, ATT is centrally assessed. He said by treating ATT differently for tax purposes than the general business community would be a step backward in terms of tax policy. In response to Mr. Smoldon, Mr. McNamara stated that generally throughout the country cable companies are locally assessed.

Senator Martin stated this is an issue that needs to be reviewed further because centrally assessed was originally a way to deal with utilities, and now industries that are not utilities are being classified in the same monopolistic way .

Kevin DeMenna, Arizona Society of Certified Public Accountants, stated he was present at the request of Senator Martin to specifically address conformity issues. He explained that Arizona has been a conformity state for the past several years, which means that previous to that time two sets of books were required to be maintained for taxes. He noted that by being a conformity state, generally a bill is passed into law annually that changes the definition of the Internal Revenue Code in Title 43. As a result, the federal adjusted gross income for Arizona taxpayers, in effect, conforms to the changes made to federal tax law in the prior year. Mr. DeMenna explained the events that have occurred in the past few years, and he encouraged the Committee to recommend full conformity.

Senator Martin stated that the conformity issue will be addressed during the next session, and recommendations will need to be made.

McCarthy commented that conformity is very important to maintain consistency for administrative purposes.

Elizabeth Hudgins, Senior Program Associate, Children's Action Alliance (CAA), stated she would focus on the issues of expanding the sales tax base, single sales factor and the income tax credit review adjustment. She commented that expanding the sales tax base to include services expands the sales tax base into the 21st century and makes sense. She said CAA opposes the single sales factor because there would be less money available. She noted DOR estimates that when fully phased, the single sales factor would cost the State between eighty and a hundred million dollars per year. She said if this tax policy was implemented, there would have to be strong accountability measures. Ms. Hudgins referred to the income tax credit review adjustment and said CAA strongly supports the concept of knowing the effectiveness of tax policy as outlined in the draft recommendations.

Mr. McCarthy commented that as a revenue producer, the Arizona sales tax system produced excellent results. Ms. Hudgins responded that the overall base that is taxed should be reflective of the overall base that people consume.

In response to Mr. Smolden, Ms. Hudgins said that CAA does not support a statewide sales tax on basic necessities. In addition, she responded that the property tax assessment ratio is something that needs to be reviewed in a broader package of tax reform issues.

Mr. Smoldon asked whether CAA has specific tax credits that it believes should be reviewed. Ms. Hudgins responded that in reviewing the draft report, the overall concept of being able to determine if tax credits are doing the job is a great direction. She said at this time CAA does not have any specific tax credits in mind, but collecting information to determine whether tax credits are achieving a goal is a positive step. Ms. Hudgins commented that the goal is to provide the services that Arizonans would like. She said they consistently support education, health, safety issues, and spending for child protective services.

In response to Senator Martin, Ms. Hudgins said CAA provided language regarding accountability in the past, and she would be willing to provide that information to the Committee for possible future legislation.

Senator Waring asked Ms. Hudgins to comment on her thoughts as to the reasons why the State has gone from a surplus of a few years ago to the deficit that currently exists. Ms. Hudgins responded that many different factors contributed to the current situation. She noted that the Fiscal 2000 Report projects a structural deficit in the future. She said the past economic boom prior to September 11, 2001 and the economic downturn was very strong. She indicated that income tax collection far exceeded expectation, but a structural deficit had been projected for a long time.

Mayor Scruggs commented she would like to offer some observations. She said Glendale's district council members have been holding meetings with constituents, and she was invited to participate to discuss global issues. She said she discussed recommendations offered by this Committee as well as those of the Governor's Committee. She said the result was that they support performance-based incentives as well as economic development incentives for new businesses. She said the citizens sensed that perhaps it was a shift to benefit existing businesses at the expense of the residential property owners, particularly in the property tax area. She referred to Ms. Hudgins remarks regarding job creation, and said the citizens support job creation incentives.

Mayor Scruggs commented on remarks made earlier by Mr. Smoldon regarding projects such as the Civic Plaza, the University Research Facilities, and the six-tenths of a percent increase in the State sales tax to fund education. She said she and the majority of people believe that those items passed solely on the basis of very strong lobbying of the business community. She referred to the growth of sales tax collections, and believes it is somewhat tied to the significant number of people migrating to Arizona. She said she wanted to share these comments made by people in her community.

Senator Martin commented that a bill is moving through the House of Representatives, which should be at the Senate next week. He said he would like the suggested performance measure language for the proposed bills, and requested the language be drafted for CPS as well as the other agencies.

Mr. McCarthy referred to an earlier comment regarding effective population growth. He said the Arizona Tax Research Association (ATRA) looked at Arizona State and local taxes over two decades - 1980 through 2000 - controlled for population growth. He said inflation was granted every year, and the tax system produced revenues over and above population and inflation growth plus 52%. He indicated it is impossible to make the argument that the system is flawed in terms of being a revenue producer over all of the economic cycles.

Ms. Daniels asked Ms. Hudgins to elaborate on her earlier remark regarding services being 25% of people's income spent in the 20th century, which has now risen to 40%. She asked whether data was available to determine how much of that amount was spent in health care or insurance. Ms. Hudgins said she would be glad to provide that data to the Committee.

Jack Lunsford, testified as an individual. Mr. Lunsford commented that he would like to reflect on the discussions from 1979/1980 regarding tax reforms, particularly property tax reforms in the State. He said he wanted to comment on the recommendations being offered by the various groups, particularly those referring to collapsing of assessment ratios. He indicated that it would not be appropriate to make the recommendations without looking at the levy and expenditure limits and explained it would constitute nothing more than a shift as to who would be paying the taxes. He pointed out that every aspect needs to be reviewed, but in a comprehensive way. He noted that the Arizona Town Hall recently published a report indicating that local government levy and expenditure limits have not been comprehensively reviewed since 1980.

Mr. Lunsford stated that his role at the Legislature in 1979/1980 as a county assessor was to reflect on the impact of Proposition 13 as it was being proposed in Arizona, and the adoption of Proposition 106. He emphasized that by not looking at the impact in the change of assessment ratios, plus not looking at the impact of assessment ratios in the context of the homeowner's rebate is lacking at the least. He said he would suggest that those recommendations be handled in a comprehensive way.

Mr. Lunsford referred to the Draft Report, Page 2, Property Tax Reforms, Fiscal Impact, which states "The changing assessment ratios would not result in lost revenue for local government." He said that possibly is a true statement; however, he is curious as to how that statement was derived. He emphasized that the difference in those counties where there is a high ratio of centrally-assessed properties, the impact on the change of assessment ratios and the shift to homeowners' property taxes would be significant. The impact would be even more significant than in those counties where there is a different ratio between the business and the homeowner's size of property taxes.

Mr. Lunsford referred to the issue regarding controlling future growth of property tax levies. He said the issue refers to requiring voters to approve any property tax rate increase that would raise more revenue than would be allowed under truth in taxation. He said he questions how statute in this particular instance could pre-empt the Constitution.

Senator Martin explained the assessment ratio works without impacting the homeowners because the cost is borne by new investment in Arizona. Mr. Lunsford responded he respectfully disagrees because of the way the levy limit is calculated, especially in those districts and political subdivisions that are at a levy limit. He indicated that new construction does not offset what happens to the assessment ratio. Senator Martin said there is still enough time to review the calculations, and Mr. Lunsford responded he would be happy to work with the Committee on those numbers.

Mr. McCarthy referred to Mr. Lunsford's comment regarding his reference to the Constitution and noted that the Constitution prohibits local governments from exceeding 2% plus growth. He said he believes the Constitution does not put any prohibition on any statutory limit less than that, but legal scholars could debate that point. Mr. McCarthy asked Mr. Lunsford whether he believes there is a problem facing the State with the effective tax rates on business property. Mr. Lunsford replied that he believes it needs to be reviewed in a comprehensive way rather than being segmented. Discussion took place regarding ideas or suggestions of how to reduce the effective tax rate on business property. Mr. McCarthy said the reality and conclusion is that collectively all of the taxpaying community, business and homeowners alike, will help resolve the problems by addressing taxes.

Mr. Lunsford commented that the time has arrived to review this issue comprehensively, and he believes everyone is willing to come to the table to take a strong look at this issue.

Mayor Scruggs commented that many of Mr. Lunsford's remarks as an individual citizen are similar to discussions that took place in the supportive and encouraging meetings of Arizona League of Cities and Towns. She said she personally is distressed by the generalizations being discussed regarding municipalities. She said she would like some additional information as to how the conclusion has been drawn that cities are taking advantage of the increases in property values. She commented she takes pride as Mayor of the City of Glendale in reducing the City's primary property tax 15% within six years, which is significant for a growing city. She said she would like to encourage more discussion on this issue, and extended appreciation for the opportunity to extend her remarks. Senator Martin thanked Mayor Scruggs for her participation on this important issue.

Mr. Flach stated he agrees that this issue should not be approached without clearly being aware of the impact. He noted that growth has some impact on infrastructure and that infrastructure generally has an initial cost that declines over time. He asked Mr. Lunsford whether he had any comments regarding infrastructure and growth.

Mr. Lunsford responded that due to the fact he is commenting as an individual citizen, he would reply in general. He said the State has been facing those kinds of growth issues for many years, but it has increased dramatically within the past two decades. He concurred that initial costs are substantial, and said assessment ratios are part of that scenario. He said after the initial costs are met, he believes there needs to be an awareness of what is occurring throughout the country and to be responsive to the maintenance of facilities, such as the schools, bridges, highways and other projects.

Senator Martin announced that this concludes the public testimony. He stated there would be a final meeting in December to vote on the recommendations and adopt the report.

Mr. Arnold asked whether each recommendation would be voted independent. Senator Martin responded that the details have not been finalized. He said members will be notified of the exact procedure of how it will be handled.

There being no further business, the meeting adjourned at 11:30 a.m.

Respectfully submitted,

Nancy L. DeMichele

Nancy L. DeMichele, Committee Secretary

(Tapes and attachments on file in the Secretary of the Senate's Office/Resource Center, Room 115)

ARIZONA STATE LEGISLATURE

TAX REFORM FOR ARIZONA CITIZENS COMMITTEE

Minutes of the Meeting
September 23, 2003
1:30 p.m. Senate Hearing Room 1

Members Present:

Senator Martin, Cochair	Representative Huffman, Cochair
Senator Brown	Representative Clark
Senator Waring	Representative Tully
William Arnold	Kevin McCarthy
Bob Flach	Hon. Elaine Scruggs
Hon. Andrew Kunasek	Russell Smoldon

Members Absent:
Senator Giffords
Representative Jackson Jr.
Ms. Lori Daniels

Staff:
Denisse Gee, Senate Research Analyst
Kitty Decker, House Research Analyst

Senator Martin called the meeting to order at 1:40 p.m. and attendance was noted.

Presentation on the Effects of Arizona's Tax Structure on Economic Growth and Job Creation:

Sandy Abalos, Abalos & Associates, testified on how taxation affects small business, in relation to real property tax, business personal property tax and corporate income tax. She explained that there are C-corporation, S-corporation, partnership, limited liability company (LLC), single member LLC and full proprietorship tax structures. She stated that the primary difference between C-corporation structure and the other structures is that C-corporation structure is taxed at the entry level. All of the other structures have a flow-through level of taxation and are taxed at individual income tax rates. The C-corporation structure is a graduated federal rate from 15 to 39 percent and Arizona has a flat rate of 6.968 percent with a current $50 minimum tax per year per C-corporation. The other structures have a graduated federal rate structure from 10 to 38.6 percent and Arizona rates from 2.87 to 5.04 percent. Traditionally, the larger businesses operate as C-corporations, manufacturers or those entities that need to accumulate working capital within the business entity structure for growth. Most small businesses operate as flow-through entities.

Ms. Abalos commented that there is a perception that small business owners are "rolling in dough" but the reality is that margins are very tight and over the last three years, have become even tighter. She noted that small business owners are the first to arrive in the morning, the last leave at the end of the day and for this, they are the last ones who get paid with whatever is left over. Sometimes this is good, and many times it is not so good. This is the reality of owning a small business. She said that the two words that best describe being a small business owner is hazardous and exhilarating.

Ms. Abalos remarked that there are two proposals from the Citizens Finance Review Commission that will have a huge impact on the business tax structure. One is the increase in the minimum tax on corporations from $50 to $200. The Second is an expansion in the application of that minimum tax to the flow through entities, specifically S corporations and partnerships. The result of these two proposals to a C-corporation is no increase in their tax provided that they have taxable income in excess of $2,870 per year. For every S-corporation and partnership, regardless of their amount of income, it would be an increase of $200 per year.

Ms. Abalos commented that the issue of conformity and the accompanying compliance burden is another concern. She stated that she would like to see Arizona conform to federal tax policy as much as possible. She noted that in 2001, Congress adopted a 30% bonus depreciation on fixed assets while Arizona did not. She stated that decision had a major impact on small business owners because of the six possible methods of depreciation that currently exist.

Ms. Abalos stated that more and more small business owners are purchasing commercial real estate, because the interest rates are so low. The real property tax is extremely expensive and many small business owners are not aware of that ratio and or do not understand it, which necessitates the hiring of advisors to complete the forms.

In response to Mr. Smoldon, Ms. Abalos remarked that there is some latitude with the use of business expenses for tax write-off purposes that is a benefit for small business owners, but opined that it is not a large enough benefit for most small business owners.

Representative Huffman asked how significant the tax burden is on small businesses relative to other factors such as legal liability and government regulation. Ms. Abalos remarked that developing a plan for establishing a small business and the consideration of what the tax burden would be, as well as the compliance that is mandated is a major factor in the decision.

Dick Foreman, Arizona Chamber of Commerce, distributed a handout entitled Arizona Chamber of Commerce, The Voice of Arizona Business, 3 Paths to Budget Success, Principles and Recommendations for Reforming Arizona's Budget Process, Tax Structure and Initiative and Referendum System (Attachment A).

Highlights from the presentation:

Budget Process

Reform Recommendations:

Bring Every Dollar into the Budget Process
- General Fund
- Other annually Appropriated State Funds
- Non-appropriated Funds
- Federal Funds

Increase Agencies' Responsibilities and Accountabilities in the Budget Process
- Link Agency missions statement and strategic objections to budget
- Prioritize activities and identify costs of each
- Hold Agencies accountable for:
  - Meeting mission statement and strategic objectives
  - Spending consistent with their prioritization

Establish a Single Independent Process for Developing Revenue Projections
- Establish and utilize an independent entity to formulate revenue projections following input from JLBC and OSPB and other interested parties
- Require that the product of the entity be the projection utilized by both executive and legislative budget staffs
- Refinements of projections would utilize the same process during budget negotiations
- The "fiscal note" process should be reformed to provide greater reliability and consistency in terms of how such notes are derived and relied upon

Define Line Item Veto Authority and the Appropriate Use of Omnibus Reconciliation Bills (ORBs)
- The Arizona Supreme Court will provide guidance in Bennett v. Napolitano

Key Principles of Taxation
- A well designed tax system at both the state and local levels will promote healthy growth, job creation and economic expansion
- Taxes should be broad-based, visible to the taxpayer, simple, stable and predictable
- The terms and terminology of taxation should be uniform and consistent

Property Tax Reform

- Reform recommendations
  - Equalization of assessment ratios
    - Reconsider 35% Homeowner Rebate and 1% Cap on residential property

- Enterprise Zones
- Elimination of raids on the General Fund

Enterprise Zones (Map generated by Arizona Department of Commerce)

Income Tax

No tax should penalize Arizona business for its growth in employment, sales or capital expansions

- Reform recommendations
  - Lower corporate tax rates
  - Acknowledge competitive realities
  - Adopt 100% sales factor
  - Review income tax credits

Map of States that have increased sales factor above 50% for manufacturing and other industries

Transaction Privilege (TPT) & Use Tax

- Reform recommendations
  - Uniform statewide definitions and interpretations
  - Accurate TPT terminology
  - No Value-added taxes

Other Key Taxation Reforms

- Avoid Fund Sweeps
- Bonding
  - The business community supports bonding for long term capital needs with the following principles:
    - The debt instrument should be consistent with the Arizona Constitution
    - Expenditures should be limited to long term capital improvements, not operational or maintenance expenses
    - The revenue source and purpose of the expenditure must be specifically related to the benefit

Constitutional Reform; Initiative and Referendum

The Arizona initiative process requires reform. Special interests have successfully mandated spending at unprecedented levels. The legislative ability to respond to budgetary crises is now unreasonably limited.

- Increase the percentage and geographic distribution of signatures required to place an initiative on the ballot
- Revenue streams must be identified and/or created for program spending increases mandated by initiative or referendum

- Reform Prop 105 "Voter Protection Act"
- Require double enactment of new spending mandates

Senator Martin expressed his excitement regarding the number of items that are in the report.

Jim Lentine, National Association of Industrial Office Properties (NAIOP), distributed a binder entitled A Competitive Evaluation of Proposed Changes in Arizona's Commercial Property Tax Burden (Attachment B).

Mr. Lentine's PowerPoint presentation is included in the handout, following the cover page.

Highlights from the presentation:

- Two Serious Threats to Arizona's Future Economic Development
  - Statewide Property Tax
  - Real Estate Transfer Tax

- Comparison or Arizona's Effective Property Tax rate against other states
- Breakdown of estimated State and local business taxes, FY 2002
- Composition of business tax liabilities, Arizona vs. U.S.
- Summary of Estimated tax on properties by metropolitan statistical area (MSA)
- Comparison of employee salaries/taxes in Nevada, California, Arizona and Utah
- Graph of new office and industrial projects built in Maricopa County between 1997 and 2002 valued at $587 million
- Graph of new office and industrial development over the last six years
- Office Leases – full service lease rate minus operating expenses equal the net rent paid to landlord
- Industrial Leases – net rent to landlord plus property taxes, insurance, utilities and maintenance equal triple net lease cost
- Graph of typical Arizona office operating expenses – 35% spent on property taxes
- Graph of typical Arizona industrial operating expenses – 55% spent on property taxes
- Comparison of expenses and control measures
- Graph of property tax burden analysis
- Comparison ranking of states by transfer tax rate
- Comparison of capital investment strategies – "good years"
- Comparison of capital investment strategies – "bad years"

Deron Webb, Managing Principal, Wentworth, Webb and Postal, testified that he works for a state and local tax consultancy that practices predominately in Arizona as well as performing nationwide site selection and settlement negotiations work for clients. He stated that Arizona taxes are significant factors in the decision making process for many businesses that are contemplating expanding or moving to the State.

Mr. Webb remarked that California dissolved its Trade and Commerce Board, which will give Arizona an opportunity to move forward in targeting California operations. Texas, Nevada, Idaho and Colorado are currently marketing for California businesses for relocations.

Mr. Webb noted that meaningful discretionary incentives and tax abatements are also attractive to businesses looking to relocate or expand. In comparison to other states, the perception of Arizona's business climate is one of high taxation and relatively low incentives.

Michelle Ahlmer, Arizona Retailers Association, testified that taxes are less a consideration than other things such as transportation and demographics. She stated that if the tax structure within the State will not allow a good transportation system to be created, many businesses have concern with getting their goods to a location as well as consumers.

Ms. Ahlmer remarked that Arizona retailers would like the Legislature to take them into consideration when advantages or incentives are being offered to bring other businesses into the State, which the established retailers end up paying for.

Ms. Ahlmer noted that the taxes that impact retailers differently than other industries are:

- Single sales factor, which would adversely affect some retailers and not others
- "Pass through" taxes that affects shopping center tenant, affect retailers significantly
- The eliminated State commercial lease tax has been a great benefit, but retailers are still impacted by city and county commercial lease taxes
- Business personal property

Kevin McCarthy, Arizona Tax Research Association (ATRA), gave a PowerPoint presentation to the Committee. A copy of the presentation is attached to the minutes (Attachment C).

Highlights from the presentation:

National Statistics & Arizona Policy Decisions

- National comparisons are inevitable when analyzing a state and local fiscal system, however, be careful with the data
- Aggregate per capita or personal income statistics have limited value in analyzing tax burdens

How Arizona Compares

- Bureau of Census is the primary source of data on aggregate tax burdens
- However, ATRA's research indicates significant errors in Arizona's data, some confirmed by the Census Bureau

ATRA's View of how Arizona Compares

- In the aggregate, Arizona's tax collections are in the mid range compared to other states
- At a minimum, the data should not lead to the conclusion that overall taxes are low and should therefore be increased

Snapshot of Arizona's Tax System

Average overall reliance

- High Sales Taxes
- Average Property Taxes
  - High Business Property Taxes
  - Low Homeowner Property Taxes
- Low Personal Income Taxes

Performance of Arizona's Tax System – Two Decade Analysis 1980-2000

- Arizona's tax system is far from perfect and in need of reform in some key areas
- However, as a revenue producer the system has performed quite well over the last two decades

Graphs demonstrating how the system has performed

- Per Capita Tax Collections (1980-1990-2000)
- Per Capita Property Tax Collections (1980-1990-2000)
- Per Capita Sales Tax Collections (1980-1990-2000)
- Per Capita Individual Income Tax Collections (1980-1990-2000)

ATRA Recommendations:

General Comments Tax Reform

- "Tax reform" has been an on-going process for ATRA for the past decade
- Many improvements have been made in property and sales tax systems
- ATRA's recommendations will continue to focus on both sound fiscal policy as well as realistic expectations

Property Tax

- ATRA believes the most pressing issue in Arizona's tax system is the effect of the classification system on business property taxes (As high as third in the country)
- There are two ways to deal with this problem:
  - Reduce property taxes overall
  - Create equity across the classes
  - Considering the importance of the property tax for both State and local government significant reductions in the property tax are unrealistic

- That leaves equity as the only other avenue to begin addressing the problem of high business property taxes

Key Property Tax Recommendations:

- Single Assessment Ratio for all future voter approved bonds and overrides
- Control future growth of property tax levies (for all classifications)
- Address high school district primary property tax rates (desegregation, small schools, etc.)
- Manage 1% cap

State Property Taxes

- Recommendations to levy a new "State" property tax will clearly exacerbate our current problems
- While the State does not have a statewide property tax rate for general fund purposes it very much relies on and benefits from property taxes

ATRA Recommendations:

Sales Tax

- Uniformity of the State and municipal sales tax base
- Maximum rate caps should be considered
- Exemptions not "loopholes"

Income Tax

- Arizona should consider conformity with the federal government, for both corporate and personal income taxes
- Arizona should change the corporate apportionment formula to 100% sales with an election for corporate taxpayers to stay with the current three-factor formula

Senator Martin remarked that the Committee needs to create its final report with recommendations by the end of December. He reminded the members to submit requests for information to staff as soon as possible so recommendations can be discussed and approved for the final report.

Without objection, the meeting was adjourned at 4:00 p.m.

Respectfully submitted,

Tracey Moulton

Tracey Moulton
Committee Secretary

(Tapes and attachments on file in the Secretary of the Senate's Office/Resource Center, Room 115.)

ARIZONA STATE LEGISLATURE

TAX REFORM FOR ARIZONA CITIZENS COMMITTEE

Minutes of Meeting
Tuesday, December 16, 2003 – 1:30 p.m.
House Hearing Room 4

Members Present:

Senator Dean Martin, Cochair
Senator Jim Waring
William G. Arnold
Lori Daniels
Bob Flach
Russell Smoldon
Representative Steve Huffman, Cochair
Representative Ken Clark
Representative Jack Jackson
Representative Steve Tully
Kevin McCarthy

Members Absent:

Senator Jack Brown
Senator Gabrielle Giffords
Honorable Andrew W. Kunasek
Honorable Elaine Scruggs

Staff:
Kitty Decker, House Majority Research Ways and Means Analyst
Denisse Gee, Senate Research Finance Analyst

Chairman Huffman called the meeting to order at 1:45 p.m. and attendance was noted.

Public Testimony

There was no public testimony, due to time constraints.

Discussion and Votes on Proposed Recommendations

Representative Huffman referred to the Draft Report (Attachment A) and the recommendations for reducing assessment ratios. He stated the Committee would adopt recommendations to be forwarded to the Speaker of the House of Representatives and the President of the Senate to review for possible tax reform legislation.

> **Senator Martin moved that the Committee adopt the following recommendation:**

Reduce assessment ratios for class 1 business and industrial properties, to include the assessment ratio for property tax purposes for class 1 properties, from 25% to 20% over five years or at a rate to be determined.

Mr. McCarthy referred to page 2 of the Draft Report and requested an explanation of the change from 25% to 20%. Representative Huffman stated the Joint Legislative Budget Committee (JLBC) was asked to do an analysis of the potential impact of the change on local governments and the general fund through basic State aid. He added the municipalities have the statutory authority to change those rates in terms of reaching their budgets, however, they would not actually see a decrease in net assessed valuation at any time during that five-year proposal period. Mr. McCarthy stated it is also important to note the fiscal impact on local governments.

Senator Martin stated there may not actually be a full 1% reduction each year if property value growth is being used to pay for the reduction and there is not enough.

Representative Huffman clarified that the motion is to drop assessment ratios and class 1 property from 25% to 20% over five years. He indicated the recommendation is to ensure that the State is viable and competitive with other communities that the State will be competing against. He noted that Reno, Nevada, distributed information citing Phoenix as the worst case scenario for property taxes and questioning why anyone would want to locate here.

Representative Huffman called for a vote on the motion.

The motion PASSED by voice vote.

Representative Huffman stated the next recommendation regards dropping assessment ratios on secondary property taxes, which are voter-approved taxes, for class 1 properties down to 20% and 10% for all other classes of property.

Senator Martin moved that the Committee adopt the following recommendation:

That the assessment ratios for future bonds and overrides on secondary property taxes be reduced to 20% for all class 1 properties and 10% for all other properties for future bond and override elections.

Mr. McCarthy asked if the motions were mutually exclusive of one another because each of the members may be supportive of them individually, but not necessarily all of them. Representative Huffman stated that the general goal is to make several recommendations to the Legislature, which will assist in moving in the right direction and that all of the recommendations may act independently of each other.

Ms. Daniels stated her preference would be a single assessment ratio and asked whether she should make a substitute motion.

Senator Martin clarified that the recommendation was derived from suggestions by Committee members.

Representative Huffman stated he would be agreeable to a substitute motion to combine the two and emphasized that something needs to be done on this issue.

Mr. McCarthy stated his understanding that the recommendations are mutually exclusive, however, he did not think the first recommendation applies just to the primary, but rather the entire system, which makes the second recommendation duplicative.

Mr. Smoldon said the first recommendation is about class 1 property, which results in an increase in historical properties and rental properties and that they are two separate issues.

Representative Clark agreed they were separate and remarked that he had a problem with the recommendation. He stated historic property taxes generate a lot of activity in his district in central Phoenix and downtown and to go the other way would result in a 900% increase in taxes for historic commercial or residential property owners. He believes that this is absolutely the wrong direction to be heading.

Mr. Smoldon suggested the owners of the expensive property that have experienced a tax decrease by half, which are located near the Heard Museum and the Central Corridor, should be paying over time what everyone else in that school district is paying.

Representative Clark stated he did not totally disagree with the issue but right now the area is in the growth stage and it would be unwise to change the trend.

Mr. Smoldon stated a homeowner of a house worth $1 million dollars is paying taxes at 10% while a homeonwer of a $100,000 house is paying at 25%. He said that is not an equitable system in terms of property value and it does not benefit school districts in those areas.

Ms. Daniels offered that the reason for a single assessment is because the other way is unfair and is devastating to small and medium-sized businesses. She added that to make the assumption that all businesses can pass on the cost of those taxes is a non-issue because we live in a global economy and businesses have to be competitive.

Representative Clark stated the vast majority of historic property values do not exceed $150,000.

Representative Huffman questioned if the members would be more comfortable with a substitute motion to reduce the assessment ratio for future bonds and override elections from class 1 business property to not more than twice the assessment ratio placed on class 3 owner occupied residential.

Representative Clark stated he would need more time to make a decision regarding the substitute proposal.

Mr. McCarthy suggested re-voting the first recommendation and only have it apply to future voter-approved bonds and overrides.

Representative Huffman called for a vote on the motion.

The motion passed by voice vote.

Senator Martin moved that the Committee adopt the following recommendation:

Reduce or eliminate the locally assessed business personal property tax.

Mr. McCarthy explained this recommendation increases taxes on real property, which has a number of benefits that do not currently exist on personal property.

In response to Representative Huffman, Mr. McCarthy explained that if value is pulled out of the tax system there is a whole variety of rippling effects, including rate increases. Real property owners will pay higher taxes than they are now paying.

Representative Huffman stated there is nothing in the State's property tax system that can be done in isolation and that personal property is the purist form of capital investment in businesses and the government should stay out of the way of capital investment decisions.

Representative Huffman called for a vote on the motion.

The motion passed by voice vote.

Representative Huffman stated the next area for review is the transaction privilege tax (TPT) and the recommendation is that the Legislature place some kind of overall cap across the board on municipalities for raising TPT and requiring voter approval for any increases above that cap.

Senator Martin moved that the Committee adopt the following recommendation:

Require voter approval for rates higher than a maximum allowable rate for cities and towns.

The motion PASSED by voice vote.

Representative Huffman moved that the Committee adopt the following recommendation:

That counties be allowed to implement a general excise tax or raise their rate by a super majority instead of a unanimous vote of the board of supervisors.

The motion FAILED by voice vote.

In response to Mr. Arnold, Ms. Decker explained that it takes three fiscal years for the 60% impact because of the way corporations file returns. Representative Huffman added that the tax calendar year is different from the fiscal year and the $5 million refers to the fiscal year in which it was implemented.

Senator Martin moved that the Committee adopt the following recommendation:

Allow multi-state and multi-national corporations the option of a 100% sales factor allocation.

The motion PASSED by voice vote.

Senator Martin moved that the Committee adopt the following recommendation:

Require the State to conform to all changes that flow through to Arizona from the federal government to re-establish conformity to the IRS statutes in the State to the greatest extent possible.

Representative Huffman expressed concern with the word "conformity", which requires that it be mandatory, and made the recommendation that the State conform as much as possible, but not mandatory.

Senator Martin stated that was not the intent and withdrew the previous motion.

Senator Martin moved that the Committee adopt the following recommendation:

To encourage the State to conform to all changes that flow through to Arizona from the federal government to conform to Internal Revenue Service tax laws.

The motion PASSED by voice vote.

Representative Huffman stated the next issue regards income tax credit review adjustment and the reporting of income tax credit information. The purpose is to provide the Legislature with enough information to make sound policy decisions regarding the issue. Mr. Arnold was concerned that this recommendation makes the information public, which he thought was dangerous. Ms. Decker explained that only information specific to the tax credit itself would be public.

Mr. Smoldon asked if that was something that should be open to the public or just to JLBC. Representative Huffman suggested the motion be narrowed.

Representative Huffman moved that the Committee adopt the following recommendation:

To continue to improve the information available to the Legislature and staff to better analyze the value of existing and future tax credits.

The motion PASSED by voice vote.

Senator Martin asked if the Committee would be interested in recommending the reinstatement of indexing standard deductions to inflation. Senator Martin added that the indexing factor was repealed in 1990. Representative Huffman suggested that at this late date Senator Martin should pursue that subject as Chairman of the Senate Finance Committee.

Senator Martin moved that the Committee adopt the following recommendation:

Move the Budget Stabilization Fund into the Constitution to provide a more stable source of revenue for the State.

Senator Martin explained that a large percentage of the State's budget is out of the Legislature's control because of voter-required mandates and funding increases.

Representative Huffman stated he did not agree that this concept should be in the Constitution as it is proposed.

Mr. Arnold agreed that the Budget Stabilization Fund formula should be reworked.

Representative Huffman stated the Legislature routinely disregards the statutory mandate and there is no need to do anything other than follow the law and start putting money into the Fund.

Representative Tully said it would be more appropriate to have a Constitutional Convention to fix the whole Constitution.

Senator Brown stated even though mistakes have been made in the past regarding the Fund, he did not want the State's hands tied any more than they already are and cautioned members regarding amending the Constitution in this area.

Representative Huffman called for a vote on the motion.

The motion FAILED by voice vote.

Representative Huffman referred to page 10 of the Draft Report and noted the recommendations were suggested by members of the Committee.

Mr. McCarthy moved that the Committee adopt the following recommendation:

Include a single commercial assessment ratio for future voter-approved bonds and overrides.

Senator Martin said he could not support this motion because it is not realistic nor politically viable and the implementation of this would be a direct shift to residential rates.

Ms. Daniels said she did not see this as a shift to homeowners but rather puts everyone on a level playing field.

Mr. Arnold stated he would like to amend the motion to eliminate the word "commercial".

Representative Huffman called for a vote on the motion.

The amended motion PASSED by voice vote.

Mr. McCarthy moved that the Committee adopt the following recommendation:

The requirement that cities, counties, and community college districts receive voter approval before exceeding their truth in taxation levies.

The motion PASSED by voice vote.

Mr. McCarthy moved that the Committee adopt the following recommendation:

The cap of the primary tax rate of any K-12 school district with 50% or more of their homeowners be a 1% cap that has a primary tax rate of 150% of the qualifying tax rate.

Mr. McCarthy explained this would have a narrow impact on districts with extraordinarily high primary tax rates, because they are using items outside the revenue control limit and are drawing down State general fund monies as a result of that.

Representative Huffman called for a vote on the motion.

The motion PASSED by a voice vote.

There being no further business, Representative Huffman adjourned the meeting at 3:05 p.m.

Respectfully submitted,

Rosetta B. Cutty
for
Nancy L. DeMichele, Committee Secretary

(Tapes and attachments on file in the Secretary of the Senate's Office/Resource Center, Room 115)