TAXATION IN ARIZONA:
AN OVERVIEW

PREPARED FOR THE
ARIZONA LEGISLATURE

MAY 31, 1979

This report was prepared by the staff of the Joint Select Committee on Tax Reform and School Finance.

ERRATA

Taxation in Arizona: An Overview May 31, 1979

Section Three

p. III-7, Figure III-2, Income Taxes and Sales Taxes should be switched in box insert. Should read:

	1967	1977	Total Percent Increase (67-77)	Average Annual Percent Increase
Sales Taxes	77.91	264.07	238.95	12.98
Income Taxes	16.22	105.57	550.98	20.60

p. III-8, Figure III-3, Income Taxes and Sales Taxes should be switched in box insert.

p. III-31 through p. III-56, Income Taxes and Sales Taxes should be switched in the box insert.

Section Five

p. V-10 Strike "not" in last line. Should read "The amounts shown are collections after refunds."

p. V-13 Table V-4 title Strike "Transaction Privilege" and insert "Sales". Should read "Distribution of State Sales Tax Collections".

p. V-13 TABLE V-5 should read:

TABLE V-5

Sales Tax Revenues As a
Percentage of Total State Revenue, 1977-78

Tax	Amount	Percent of Total** State Revenues
Transaction Privilege Tax	$247,570,254	14.3%
Education Excise Tax	240,563,322	13.9
Special Education Excise Tax	81,056,526	4.7
Use Tax*	8,577,759	.5
Rental Occupancy	169,562	.01

(Corrections to p. V-13 TABLE V-5 cont'd)

*One-half of the Use Tax is earmarked for the Education Excise Tax fund. In total, $17,155,518 was collected for tangible personal property purchased outside the state.

**Total state revenues here include all state general and special revenue and aid collections before distribution to local governments in the amount of $1,725,466,329.

FOREWORD

This report is the first in a series of documents to inform the Legislature about the present taxation and education finance structures in Arizona, in preparation for the 1979 Special Session on Tax Reform and School Finance.

"Taxation in Arizona: an Overview" consists of several sections that describe:

- the major principles or tenets of taxation
- comparisons of tax burdens in Arizona and other states in the Western U.S.
- the administration and level of collections of the major taxes imposed by state and local governments in Arizona

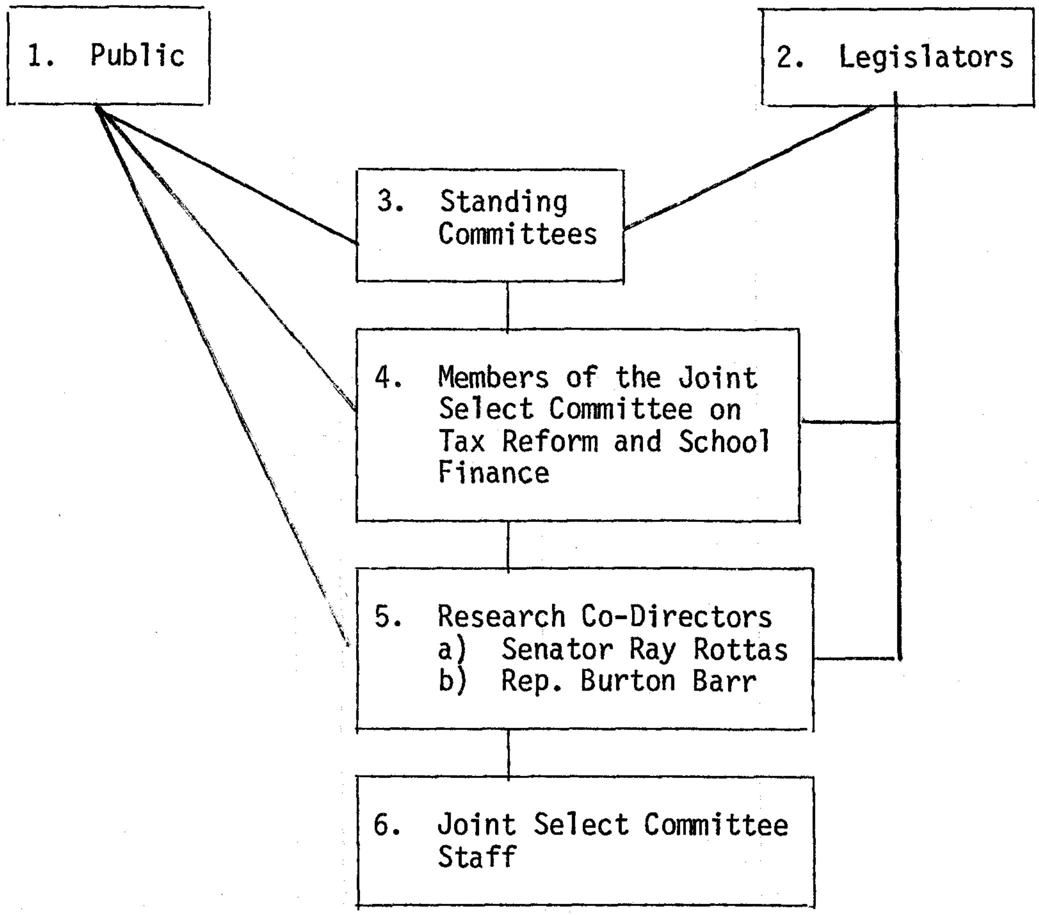
In order to best serve the interests of Arizona in arriving at decisions to alter the present tax and education finance structures, it is necessary that the Legislature give consideration to all ideas, plans and options. It is hoped that legislators and other citizens who wish to have their ideas researched and examined by the Joint Select Committee, submit them as soon as possible in accordance with the procedures outlined in this report.

SENATOR RAY ROTTAS
Cochairman
JOINT SELECT COMMITTEE ON
TAX REFORM AND SCHOOL FINANCE

REPRESENTATIVE BURTON BARR
Cochairman
JOINT SELECT COMMITTEE ON
TAX REFORM AND SCHOOL FINANCE

SUBMISSION OF EDUCATION AND TAX PLAN ALTERNATIVES

Each of you are encouraged to submit any viable alternative plan in the areas of taxation or school finance which you believe should be considered during the forthcoming special session of the Legislature. In order to insure that each proposal is properly researched and investigated in the most expeditious manner, the following procedure has been established.



The PUBLIC (1) prepares alternative education and tax plans, <u>in writing,</u> and submits these to either a member of the Joint Select Committee on Taxation and School Finance or the Research Co-Directors.

LEGISLATORS (2) who are not members of the Joint Select Committee on Taxation and School Finance may submit their research requests and alternative taxation and school finance plans through a (3) STANDING COMMITTEE or to a member of the Joint Select Committee or the Research Co-Directors. STANDING COMMITTEES (3) should submit plans to the Joint Select Committee. All requests submitted must be in writing.

MEMBERS (4) of the Joint Select Committee will submit their research requests and alternative taxation and school finance plans in writing along with requests received from the public or other legislators to the Co-Directors.

The RESEARCH CO-DIRECTORS (5) will compile all requests, determine the amount of time necessary for research and investigation and assign these to the staff, in priority order. Priorities will be established based upon the order in which requests are received, the amount of work estimated to research and investigate the request and the availability of staff time.

At the time the Research Co-Directors assign the request to the staff they will notify the person making the request as to when it can reasonably be expected that the work will be completed. The Research Co-Directors will monitor the progress of the request to insure that it is returned to the originator as rapidly as possible.

The STAFF (6) of the Joint Select Committee will perform the research tasks as assigned by the Research Co-Directors.

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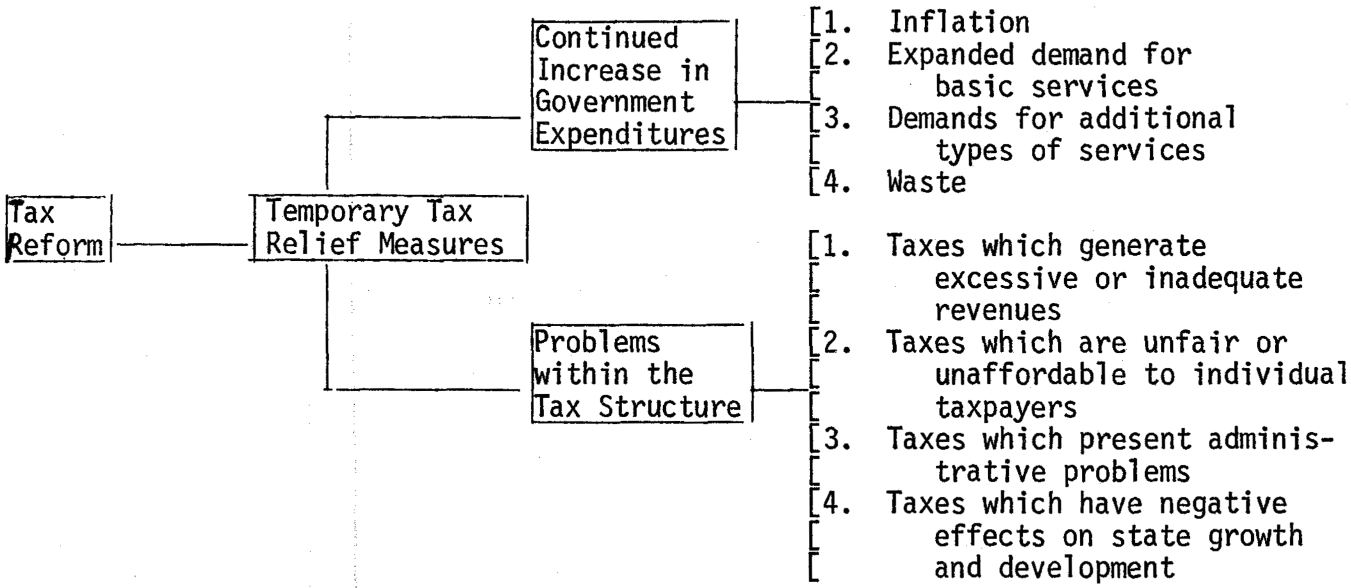
SECTION ONE

PROBLEMS LEADING TO TAX REFORM

One of the major purposes of the special session is to address the issue of tax reform. In order to deal with this issue, it is important to understand some of the reasons why tax reform has become a major issue. The diagram that follows illustrates the chain of causes which has culminated in the need for a special session on tax reform.



The immediate reason for the proposed special session on tax reform is to improve the current tax structure in order to eliminate the need for temporary tax relief measures such as the rebate. The rebate and other temporary tax relief measures were enacted in order to relieve taxpayers from the effects of continued increases in government expenditures and problems within the tax structure.

The underlying factors which have contributed to the increase in government expenditures and the underlying factors which cause problems within the tax structure are shown in the right portion of the diagram. These factors are discussed below:

FACTORS CONTRIBUTING TO INCREASED GOVERNMENT EXPENDITURES

1. INFLATION - According to the Bureau of Business and Economic Research at the Arizona State University, the inflation rate in the Phoenix area during 1978 was greater than 10%. This means that the amount of money required to pay for services provided by the government during 1978 was 10% higher than the amount of money required to pay for the same services in 1977. This added funding requirement is further translated into an increase in government expenditures. For example, teachers may demand a salary increase of 10% in order to maintain the purchasing power of their incomes. If this increase is granted, schools will be required to raise the salary portion of their budgets by 10% in order to retain the current staff.

2. EXPANDED DEMAND FOR BASIC SERVICES - The Department of Economic Security has estimated that the population in the State of Arizona increased by about 4.6% between July 1, 1977 and July 1, 1978. Individuals moving into the state will expect to receive the same government services currently provided to residents. In order to provide services to more individuals, government entities may increase staffing and may require larger facilities. To pay for the expansion government expenditure will have to increase. For example, new schools may have to be built and staffed in order to accommodate children moving into the district. This may result in a substantial increase in the school district budget.

3. DEMANDS FOR ADDITIONAL TYPES OF SERVICES - Taxpayers who are unsatisfied with the types of services currently provided by the government, may demand that new programs be initiated which will better meet their particular needs. If additional programs are initiated, government expenditures are likely to increase in order to meet the resource requirements of the new program. For example, the Department of Economic Security during the current operating year initiated a major program to deinstitutionalize the care of the mentally retarded. In order to implement this program, the DES budget was increased substantially.

4. WASTE - Waste occurs whenever resources are expended unnecessarily in providing services to the public. For example, the assessment process, which takes place at the county level, must occassionally be repeated because of errors which occur in compiling the tax rolls.

Additional funds may be required to pay for resources expended in repeating this process, which would otherwise have been unnecessary.

FACTORS CAUSING PROBLEMS WITHIN THE TAX STRUCTURE

1. TAXES WHICH GENERATE EXCESSIVE OR INADEQUATE REVENUES - Taxes are levied in order to fund government services demanded by the taxpayer. If the revenues raised from taxes exceed the amount required to pay for government services, the burden on the individual taxpayer will be unnecessarily high. If the revenues raised from taxes are not sufficient to cover the cost of government services, cutbacks in the services provided to taxpayers may be necessary. In Arizona, the current tax structure would appear to generate revenues in excess of those required to pay for government services. In order to prevent the individual taxpayers from paying taxes which are unnecessarily high, revenues not used to provide government services are returned to taxpayers in the form of a rebate.

2. TAXES WHICH ARE UNFAIR OR UNAFFORDABLE TO INDIVIDUAL TAXPAYERS - Individuals with limited incomes may have difficulty paying taxes to which they are subject. Thus, taxes which are levied without reference to personal income may place an undue hardship on individuals in the lower income ranges. The property tax is an example of a tax which may be unaffordable to the individual. In Arizona, individuals above the age of 65 who have low incomes, are given an income tax credit for property taxes paid in recognition of the burden which is placed on low-income individuals by the property tax.

3. TAXES WHICH PRESENT ADMINISTRATIVE PROBLEMS - Substantial amounts of resources may be expended in the administration of taxes. The amount of resources required will increase as the tax becomes more difficult to administer. An example of a tax which is difficult to administer is the property tax. The Department of Revenue was given an additional appropriation for the current operating year to improve the administration of the tax.

4. TAXES WHICH HAVE NEGATIVE EFFECTS ON STATE GROWTH AND DEVELOPMENT - Because taxes reduce the amount of funds which are available to the taxpayer for expenditure, taxes which are levied at excessive rates may substantially

decrease the level of economic activity within the state. Individuals overburdened by taxes may lose their incentive to work or may be forced to curb their spending, and businesses overburdened by taxes may become unprofitable. The problem may be compounded if businesses also suffer the effects of reduced demand by individuals who are overtaxed. In Arizona, the state's portion of the parimutuel tax was recently reduced in order to increase the profitability of the racing industry and allow it to expand.

SECTION TWO

CRITERIA FOR EVALUATING TAXES

The objective of tax reform is to produce a tax structure which is an improvement over the current system. In order to achieve this objective, it is important to establish criteria which can be used to evaluate both the current tax structure and any new alternatives under consideration. Because these criteria serve as a basis for determining whether a given tax will better meet the demands of the taxpayer, it is important to identify exactly what it is that the taxpayer expects from a tax and incorporate these demands within the criteria. Basically, these demands can be narrowed to the four major objectives outlined below:

1) Revenue Generation - The revenues produced by the tax should be sufficient to pay for the services demanded by the taxpayer.

2) Social Equity - The tax should be fair and should not become too great a burden to the individual taxpayer.

3) Ease of Administration - The tax to be paid by the individual taxpayer should be easy to determine.

4) Consistency with State Goals - To the greatest extent possible, taxes should be exported and should promote a rational pattern of development within the state.

Taking each of these in turn, it is helpful to identify the characteristics which a tax must possess in order to meet the objectives outlined above.

Revenue Generation

In the case of revenue generation, a tax must satisfy two characteristics in order to consistently produce enough revenues to pay for the services demanded by the taxpayer.

First, the revenues produced by the tax must expand over time as the demand for services increases. A good illustration of a tax which possesses this characteristic is the local property tax. Ordinarily, property taxes are levied at the local level primarily for the purpose of financing school expenditures. New families with school age children that move into the district will raise the total level of school expenditures, thereby increasing the need for additonal revenues. However, the in-migrant families may require new housing, thereby adding property value to the tax base and generating additional revenues. The individual income tax, on the other hand, does not possess this characteristic. With the income tax, increases in the demand for government services and increases in the tax base tend to follow different cycles. During a recession, for example, the level of unemployment will increase and the number of individuals demanding welfare services is likely to expand. At the same time, however, the level of income may be falling and the amount of revenues produced by the income tax may also decline.

A second characteristic which a tax must possess in order to continually produce enough revenues to pay for the services demanded by the taxpayer is that the revenues must expand over time as the price of the service demanded increases. The sales tax is a good example of a tax which possesses this characteristic. Because a sales tax is levied on the gross receipts from the sale of goods, a general increase in the price of goods will result in an increase in the revenues produced by the sales tax. This increase in revenues can then be used to pay for the higher cost of government services which is also associated with a general increase in the price of goods.

A good example of a tax that does not possess this characteristic is the fuel tax. Currently, the Arizona fuel tax is levied on the number of gallons of gasoline purchased, not on the receipts from the sale of gasoline. Therefore, a general increase in the price of goods, which will increase the cost of government services, will not necessarily result in an increase in revenues from the fuel tax.

Social Equity

In the case of social equity, three characteristics must be present if taxes are to be fair and are not to become too great a burden to the individual taxpayer.

First, the tax burden borne by the individual taxpayer should be affordable from current cash flow without undue hardship.

The best example of a tax that possesses this characteristic is the individual income tax. Because a percentage of income is withheld from each individual's paycheck at the time of receipt, the bulk of the individual's total tax liability is automatically paid from current cash flow.

The property tax, on the other hand, may not possess this characteristic. If an individual who owns property is unemployed at the time when property taxes become due, he will be liable for payment of the tax regardless of the fact that he may be unable to pay the tax from current cash flow.

A second characteristic that a tax must possess in order to meet the objective outlined for social equity is that the tax burden borne by individuals with common circumstances must be equivalent. Again, the individual income tax is a good example of a tax that possesses this characteristic. Because income is generally regarded as a fairly good measure of circumstance and individuals falling within the same income range are taxed at the same rate, it is relatively safe to assume that individuals with common circumstances have roughly equivalent income tax burdens.

The school district property tax is a prime example of a tax which does not possess this characteristic. Because the tax rate levied on a given property depends upon the level of school expenditures and in particular on the total amount of assessed valuation subject to tax within the district, two parcels of equal value located within separate school districts may have totally different tax burdens. Differences in appraisal techniques may also result in two property parcels of comparable value being subjected to different tax liabilities.

The third characteristic that taxes should possess if they are to be considered equitable, is that, all other things being equal and given that an individual can afford to pay a tax, the taxpayer receiving more services should be taxed at a higher level. Economists refer to this tenet of taxation as the "benefits of taxation." Some caution must be used in evaluating taxes according to this characteristic because of the difficulty of identifying specific benefits which are derived from the levy of a given tax. Particularly in the case of taxes which are designed to raise large amounts of general revenue, it is difficult to determine the relationship between costs to the taxpayer and benefits received.

The fuel tax is a good example of a tax that possesses this characteristic. Receipts from fuel taxes are generally used for road maintenance and construction. We can probably assume that individuals who travel a greater number of miles will ordinarily demand more road construction and maintenance services. Because the fuel tax is levied on gallons of gasoline sold, these same individuals will likely pay greater fuel taxes as well, as the number of gallons purchased increases. Conversely, the individual income tax does not possess this characteristic. Ordinarily, individuals with lower incomes require more government services (welfare, unemployment compensation, etc.). These individuals will not be required to pay greater income taxes to finance these services, because the income tax is designed so that individuals with lower incomes will pay lower income taxes.

Ease of Administration

Basically, only one characteristic must be present if a tax is to satisfy the objective outlined for ease of administration - the value of the tax base should be relatively easy to determine.

The sales tax is a good example of a tax which possesses this characteristic. The sales tax is a direct tax on the gross selling price of a good. Because this price is fixed prior to sale, no discretion is necessary in determining the value of the tax base.

The property tax, on the other hand, is levied on the assessed valuation of a property which is based on the property's current market value. If the property has not been sold recently, no direct measure of the current market value of the property will be readily available and therefore, the exact value of the tax base will be somewhat difficult to determine.

Consistency with State Goals

The final criteria established for evaluating taxes is consistency with state goals. If a tax is to meet the objective outlined for this criteria, two characteristics will ideally be present.

First, a substantial portion of the total tax levy will be paid by the residents of other states. A good example of a tax which possesses this characteristic is the sales tax on hotels. The sales tax on hotels represents an added cost to the business which will probably be recouped in the form of an increase in the price of the accommodations. Because hotels are normally frequented by the residents of other states and these individuals will pay the price of the accommodations, a substantial portion of the sales tax on hotels will be paid by non-residents. The individual income tax is a good example of a tax which does not possess this characteristic. Non-residents are taxed on income only to the extent that that income was derived from sources within the state.

In addition to this characteristic, a tax should not inhibit the growth of business or discourage new businesses from locating in the state, if it is to be consistent with state goals.

A good example of a tax which possesses this characteristic is the estate tax. This tax is levied on the personal possessions of deceased individuals and therefore, has no direct effect on the growth of business.

Other taxes such as the unemployment insurance tax, are paid directly from the proceeds of businesses subject to the tax and, therefore, may serve to inhibit the growth of the business if they become excessive.

Although it is unlikely that any given tax will satisfy all of the above criteria, it is nevertheless helpful to evaluate tax alternatives in terms of these criteria in order to identify strengths and weaknesses of the options under consideration. In so doing, it may be possible at times to eliminate elements of a tax which are contrary to the objectives of the taxpayer. By levying the fuel tax on gross receipts from the sales of fuel instead of levying the tax on gallons sold, for example, it may be possible to assure that revenues from the fuel tax will expand over time as prices of government services continue to increase.

It is also possible that a tax which satisfies a given set of criteria may be more suitable for certain purposes, and evaluating all tax alternatives in terms of a standard set of criteria will provide some basis for selecting the best tax for the purposes at hand. For example, if a tax is needed for the primary purpose of raising large amounts of general revenues, it might be a good idea to select a tax which is affordable to the individual taxpayer from current cash flow, because the larger the revenue requirements, the more likely it becomes that payment of the tax will represent a hardship to the individual. Thus, the income tax might be the best tax to levy when large amounts of general revenues are required.

In the case of the general tax reform currently underway, it is hoped that evaluating all of the alternatives under consideration in terms of a standard set of criteria, will serve as a basis for developing a mix of taxes which satisfies all of the criteria to the greatest degree possible in order to produce a tax structure which more fully meets the demands of the taxpayer.

	PROBLEM	CRITERIA	POSITIVE CHARACTERISTICS	POSITIVE EXAMPLES / NEGATIVE EXAMPLES
Revenue Generation	Taxes Which Generate Excessive Or Inadequate Revenues	Revenues Produced Should Be Just Sufficient To Pay For Services Demanded By Taxpayers	Revenues Should Expand As The Demand For Services Increases	Property Tax / Individual Income Tax
			Revenues Should Expand As The Price Of Services Increases	Sales Tax / Fuel Tax

	PROBLEM	CRITERIA	POSITIVE CHARACTERISTICS	POSITIVE EXAMPLES / NEGATIVE EXAMPLES
Consistency With State Goals	Taxes Which Have Negative Effects On State Growth And Development	To the Greatest Extent Possible Taxes Should Promote A Rational Pattern of Development Within The State	A Significant Portion Of The Total Tax Levy Should Be Paid By Residents Of Other States	Sales Tax On Hotels / Individual Income Tax
			Tax Should Not Inhibit The Growth Of Business Or Discourage New Business From Locating Within The State	Estate Tax / Unemployment Insurance Tax

	PROBLEM	CRITERIA	POSITIVE CHARACTERISTICS	POSITIVE EXAMPLES / NEGATIVE EXAMPLES
Ease of Administration	Taxes Which Present Administrative Problems	The tax to be paid By the individual Should not be Difficult to Determine	The value of The tax base Should not be Difficult to Determine	Sales tax / Property tax

	PROBLEM	CRITERIA	POSITIVE CHARACTERISTICS	POSITIVE EXAMPLES / NEGATIVE EXAMPLES
Social Equity	Taxes Which Are Unfair Or Unaffordable To The Individual Taxpayer	Taxes Should Be Fair And Should Not Become Too Great A Burden To The Individual Taxpayer	Tax Burden Borne By Individuals Should Be Afford-Able From Current Cash Flow Without Undue Hardship	Individual Income Tax / Property Tax
			Tax Burden Borne By Individuals With Common Circumstances Should Be Relatively Equivalent	Individual Income Tax / School District Property Tax
			Assuming That Taxes Are Affordable Taxpayers Receiv-ing More Services Should Be Taxed At Higher Levels	Fuel Tax / Individual Income Tax

SECTION THREE

TAX BURDEN AND RELIANCE

INTRODUCTION

State and local governments in the U.S. finance the vast majority of their expenditures by taxation and direct charges imposed on citizens and businesses. Each state, moreover, fashions its unique taxation system within guidelines that are established by its social, political, and economic institutions. These boundaries consist of: (1) the conditions (i.e. economic, political and social) under which particular types of taxes may be imposed and (2) the goals and objectives that the overall tax system must meet. As a result of these influences, states come to rely upon certain tax sources to a greater or lesser extent in the generation of revenue. Furthermore, it is the nature and mix of taxes imposed within each state that establish the final tax burdens borne by particular family and income groups.

This chapter will compare the tax reliance of own source revenues of state and local governments for the contiguous block of eleven western states and examine the changes in the average per capita tax burden between FY 1966-67 and FY 1976-77. Average family tax burdens of income, property and sales tax will also be examined.

A. COMPARISON OF TAX BURDEN AND RELIANCE OF ELEVEN WESTERN STATES

In this section, state and local taxation in the eleven western states will be analyzed to determine the incidence, or burden of taxation on individuals, and the extent to which the various state and local governments are dependent on particular taxes for revenue.

1. TAX BURDEN

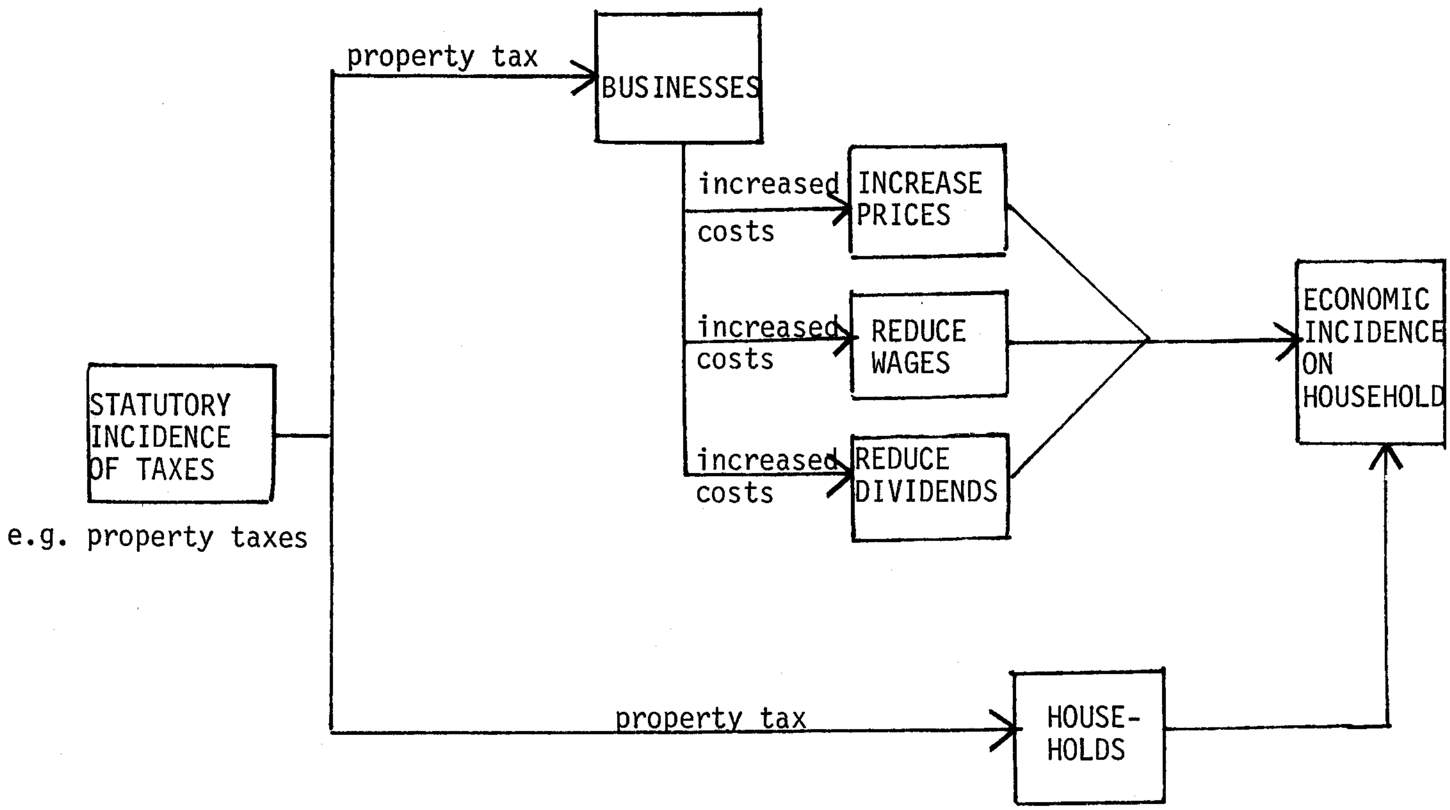
Economists usually distinguish between the statutory incidence of taxation and the economic incidence of taxation. Statutory incidence refers to the legal liability for payment of a particular tax, and is usually of primary interest to government officials who must collect the taxes and the firms who must pay them. However, once a tax is enacted, taxpayers will attempt to transfer or shift the burden of the tax onto others. A tax on business, for example, may be shifted onto consumers through higher prices. Business taxes may also be borne, in part, by the factors of production through lower wages paid to workers or reduced dividends to shareholders. The final burden of a tax after all shifting has taken place is called the economic incidence of taxation. Ultimately, the economic incidence of all taxes rests with individuals in their capacity as taxpayers, consumers, workers and shareholders. This is illustrated in Figure III-1.

The individual is confronted with the prospect of paying those direct taxes for which he is legally responsible and the indirect taxes which are ultimately shifted onto him. While direct taxes are relatively easy to compute or ascertain, indirect taxes are "hidden" and their computation is highly uncertain. The final incidence of indirect taxes is difficult to determine because the extent of tax shifting to individuals is dependent upon a number of factors, including; the nature of demand and supply for the commodity being taxed, how much of the product is consumed locally and how much is exported outside the state, and the type of tax imposed.

It is, therefore, not surprising that data do not exist that detail comparisons of the economic incidence of taxation among states and among taxpayer classes. Nevertheless, there are several sources of information available that will provide general insight into the incidence of direct and indirect taxation among states.

Figure III-1

THE BURDEN OF TAXATION



In this section, two types of data are used to analyze and compare tax burdens in the eleven western states. The first data are taken from the Census Bureau publication, "Governmental Finances." The data are per capita own souce revenue collections by tax source. These data show the average per capita tax burden of direct and indirect taxes for each of the eleven states. They do not, however, provide information about how the taxes impact family and income groups, nor do they account for taxes that might be exported to residents and businesses located in other states.

The second data series describes the tax burdens of particular family and income groups resulting from three direct taxes--individual income, sales and property taxes. These data are taken from several detailed tax burden studies prepared by researchers over the past several years.

a. Combined State and Local Per Capita Own Source Revenue

Table III-1 shows combined state and local per capita own source general revenue collections in 1967 and 1977 for the eleven western states. The data were taken from U.S. Census Bureau publications of state and local government finances in each of the study years.* Own source general revenue as defined by the Census Bureau includes all revenue of state and local governments exclusive of intergovernmental transfers, utility revenue, liquor stores revenue, and insurance trust revenue.

The figures presented in Table III-1 allow comparison of changes in per capita revenues in both current dollars and constant 1967 dollars. By examining the change in revenues expressed in current dollars, it is possible to gain insight into the absolute magnitude of changes in per capita revenues that occurred during the period. The sources of the change in per capita revenue include both real growth and inflationary growth. Real growth refers to the increase in revenues due to increases in population, increases in economic productivity, and government changes in tax rates and bases. Inflationary growth is the result of the general increase of prices of goods and services. By removing the inflationary effects from the change in per capita income, it is possible to show the "real" growth in tax revenues. In removing the effects of inflation, the 1977 per capita figures have been deflated by the amount of the increase, between 1967 and 1977, of the state and local

*Sources: U.S.Dept. of Commerce, Bureau of the Census, 1977 Census of Governments; Government Finances; Compendium of Government Finances, No.5, U.S.G.P.O., 1969.

U.S. Dept. of Commerce, Bureau of the Census, Governmental Finances in 1967-77, U.S.G.P.O., 1978.

Table III-1

Per Capita Own Source General Revenue

State	1967	1977 Current Dollars	1977 Rank (Western U.S.)	1977 Constant 1967 Dollars	1967-77 Current Dollars	1967-77 Constant 1967 Dollars
	Per Capita Own Source General Revenue				Average Annual Rate of Change	
United States	$385	$1,032		518	10.4%	3.0%
Arizona	406	1,033	7	519	9.8	2.5
California	496	1,320	2	663	10.3	2.9
Colorado	440	1,093	6	549	9.5	2.2
Idaho	378	830	11	417	8.2	1.0
Montana	388	1,006	8	505	10.0	2.7
Nevada	503	1,219	3	612	9.3	2.0
New Mexico	393	952	9	478	9.2	5.8
Oregon	418	1,094	5	549	10.1	2.8
Utah	372	864	10	434	8.8	1.6
Washington	468	1,121	4	563	9.1	4.6
Wyoming	499	1,766	1	887	13.5	5.9
Western State Average*	469	1,208		607	9.9	2.6

*Weighted Average

Sources: U.S. Department of Commerce, Bureau of the Census, 1967 Census of Governments: Compendium of Government Finances, No. 5, U.S.G.P.O., 1969

U.S. Department of Commerce, Bureau of the Census, Governmental Finances in 1976-77, U.S.G.P.O., 1978 government purchases index of the GNP implicit price deflator,* In this way, 1977 per capita revenues can be expressed in terms of equivalent 1967 dollars.

Major findings from examination of Table III-1 are as follows:

- The average annual rate of increase of per capita state and local own source general revenue between 1967 and 1977 in Arizona was 9.8% in current dollars and 2.5% in constant 1967 dollars.

- The average annual rate of real increase of per capita own source general revenue in Arizona was below that of the entire U.S. (3.0%) and that of the western states as a whole (2.6%).

- 1977 per capita revenue in Arizona was $1,033--almost identical to the U.S. average of $1,032, but considerably lower than the western states average of $1,208.

- In 1977, Arizona ranked seventh in per capita own source general revenue among the eleven western states.

A more detailed account of own source general revenue in Arizona is presented in Figures III-2 and III-3.

Figure III-2 is a bar graph showing changes in the components of combined state and local per capita own source general revenue, expressed in current dollars. Figure III-2 indicates that taxes account for $887 or 86% of total own source general revenue. Figure III-2 also shows that per capita tax collections more than doubled during the ten-year period. In relative terms, income taxes have grown at a faster pace than other types of taxes.

The rapid growth in per capita income tax collections is a reflection of the state's increasing, or progressive, income tax rate schedule. Since the tax is levied at progressively higher rates on income, as income increases, taxpayers are pushed into higher tax brackets. As a result, income tax collections grow at a faster rate than per capita income and collections from other types of taxes.

Figure III-3 presents similar information for Arizona after accounting for inflation. As shown in the figure, once inflation is removed, the resulting "real" increase in per capita taxes is substantially lower.

The reader is referred to Appendix III-1 where similar graphs can be found for the other ten western states.

*U.S. Dept. of Commerce, Bureau of Economic Analysis, Survey of Current Business, January 1976.

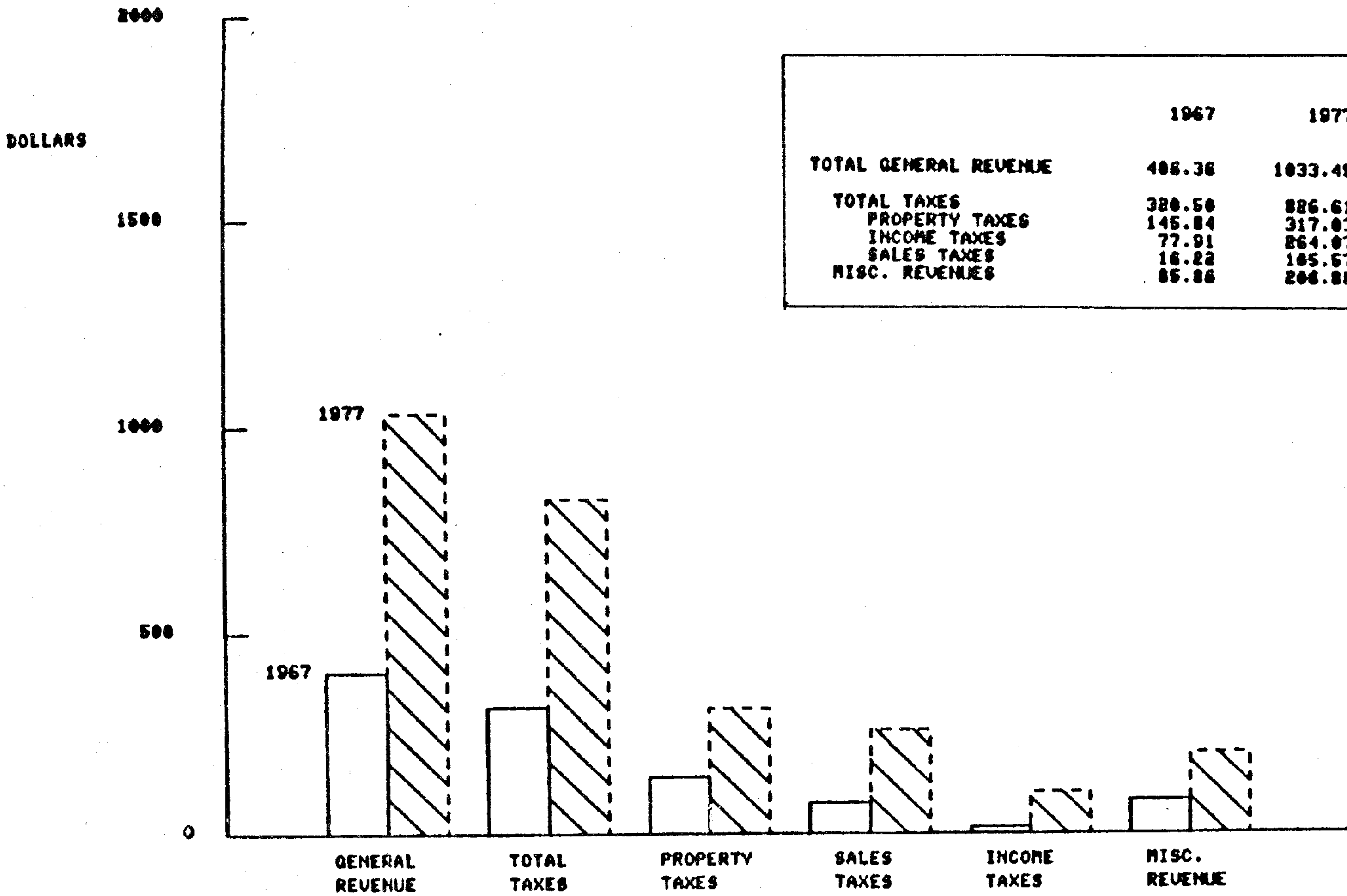
Figure III-2

PER CAPITA OWN SOURCE REVENUE

STATE AND LOCAL GOVERNMENTS

ARIZONA 1967 VS. 1977

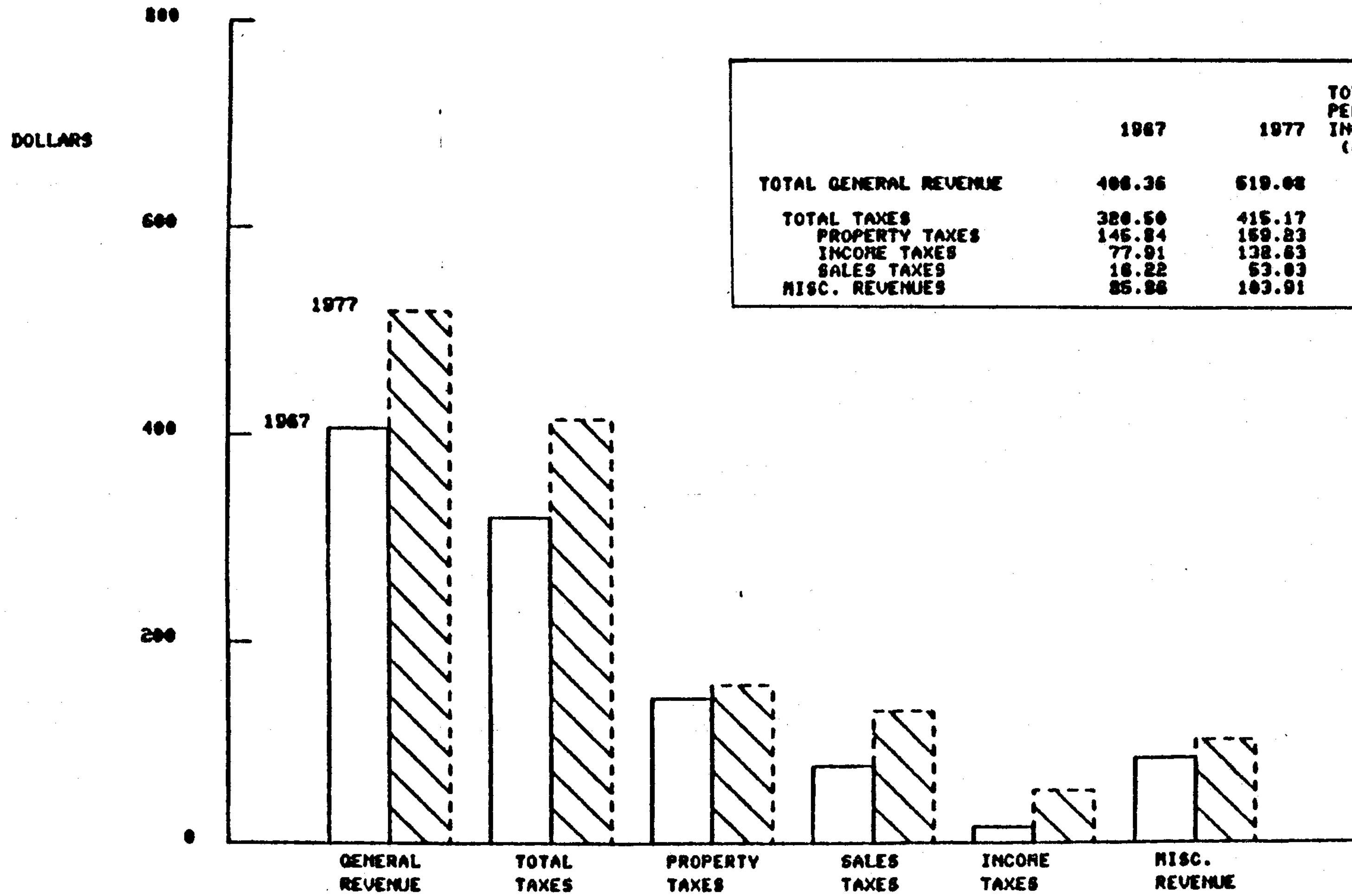
CURRENT $$



	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	406.36	1033.49	154.33	9.78
TOTAL TAXES	320.50	826.61	157.91	9.94
PROPERTY TAXES	145.84	317.03	117.38	8.07
INCOME TAXES	77.91	264.07	238.95	12.98
SALES TAXES	16.22	105.57	550.98	20.60
MISC. REVENUES	85.86	206.88	140.94	9.19

Figure III-3

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
ARIZONA 1967 VS. 1977
CONSTANT 1967 $



	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	406.36	519.08	27.74	2.48
TOTAL TAXES	320.50	415.17	29.54	2.62
PROPERTY TAXES	146.84	160.23	9.12	.88
INCOME TAXES	77.91	132.63	70.24	5.46
SALES TAXES	16.22	53.03	226.96	12.58
MISC. REVENUES	85.86	103.91	21.02	1.93

b. Direct Tax Burden of Families. An interesting comparison of state taxation structures is that of the average tax burden of direct taxes or statutory tax burdens confronting families in each state. Although direct taxes comprise only a portion of the total tax burden of individuals, they are certainly the most visible sources of taxation and provoke the greatest taxpayer concern.

Several studies have been reported in recent years that estimate the direct tax burden of individuals residing in different states. In this section, the results of two such studies are presented.

One study, undertaken by Dr. Stephen E. Lile for the Kentucky Department of Revenue*, computes 1976 payments of income tax, sales tax, property tax, motor vehicle tax and cigarette taxes for families based on six classes of adjusted gross income. The second study examined in this section was prepared by the Minnesota Department of Revenue and reports income tax liabilities for 23 income levels and four family types.

Table III-2, taken from the Lile study, presents estimated tax liabilities for the eleven western states by type of tax for six income levels. The estimates are based on taxes in effect during 1976 with the exception of state income taxes which are estimated for 1977. Each family income group is assumed to consist of four family members with one wage earner. Income is assumed to come exclusively from wages and salary. Each family is assumed to reside in the state's largest city.

Based on the figures in Table III-2, Arizona ranks first among the eleven states in total family tax burden for the $7,500 and $10,000 income brackets; second at the $15,000 income level; third at the $17,500 level; fourth at the $25,000 level; and fifth at the $50,000 income level. As a matter of comparison, the State of Oregon ranks eleventh at the $7,500 income level and second at the $50,000 level. California ranks second at the $7,500 income level and first at the $50,000 income level.

The states of Nevada, Washington and Wyoming do not impose an income tax, while Oregon and Montana do not levy sales taxes. Nevada, Washington and Wyoming rank low in total tax liability at all six income levels. Montana's lack of a sales tax is offset with its income tax, so that in terms of total

*Stephen E. Lile, Interstate Comparisons of Family Tax Burdens with Residence Location Based on Each State's Largest City, Kentucky Department of Revenue, June 30, 1978, 56 pp.

TABLE III-2

TOTAL DIRECT TAX BURDENS
ELEVEN WESTERN STATES

1976

$7,500 Adjusted Gross Income

	Income Tax[a]	Sales Tax[b]	Property Tax	Other Taxes[c]	Total	Rank	Total Taxes As % of Adjusted Gross Income
Arizona	$ 90	$ 188	$296	$224	$798	1	10.64%
California	4	134	460	193	791	2	10.55
Colorado	56	218	269	175	718	3	9.57
Idaho	-3	105	308	158	568	7	7.57
Montana	151	-	271	207	629	5	8.39
Nevada	-	116	265	164	545	9	7.27
New Mexico	-127	170	269	145	457	10	6.09
Oregon	176	-	109	128	413	11	5.50
Utah	107	182	184	200	673	4	8.97
Washington	-	183	178	248	609	6	8.12
Wyoming	-	116	243	196	555	8	7.40
Western States Average[d]	$57	$157	$259	$185	$614		8.19%

Source: Stephen E. Lile, "Interstate Comparison of Family Tax Burdens with Residence Location Based on Each State's Largest City," Kentucky Department of Revenue, June 1978.

TABLE III-2

TOTAL DIRECT TAX BURDENS
ELEVEN WESTERN STATES

1976

$10,000 Adjusted Gross Income

	Income Tax[a]	Sales Tax[b]	Property Tax	Other Taxes	Total	Rank	Total Taxes As % of Adjusted Gross Income
Arizona	$161	$219	$350	$224	$954	1	9.54%
California	0	165	545	193	903	2	9.03
Colorado	138	256	319	175	888	3	8.88
Idaho	102	123	364	158	747	6	7.47
Montana	279	-	322	207	808	5	8.08
Nevada	-	135	314	164	613	10	6.13
New Mexico	-91	200	319	145	573	11	5.73
Oregon	299	-	297	128	724	7	7.24
Utah	201	214	218	200	833	4	8.33
Washington	-	216	211	248	675	8	6.75
Wyoming	-	136	288	196	620	9	6.20
Western States Average[d]	$136	$185	$293	$185	$758		7.58%

Source: Stephen E. Lile, "Interstate Comparison of Family Tax Burdens with Residence Location Based on Each State's Largest City," Kentucky Department of Revenue, June 1978.

TABLE III-2

TOTAL DIRECT TAX BURDENS
ELEVEN WESTERN STATES

1976

$15,000 Adjusted Gross Income

	Income Tax[a]	Sales Tax[b]	Property Tax	Other Taxes[c]	Total	Rank	Total Taxes As % of Adjusted Gross Income
Arizona	$200	$271	$460	$278	$1,155	2	7.7%
California	171	220	715	193	1,299	1	8.7
Colorado	164	320	419	335	1,078	3	7.2
Idaho	271	155	479	158	1,063	4	7.1
Montana	332	-	442	207	961	6	6.4
Nevada	-	168	413	164	745	10	5.0
New Mexico	13	251	419	145	828	7	5.5
Oregon	301	-	622	128	1,051	5	7.0
Utah	308	268	287	200	1,063	4	7.1
Washington	-	272	277	248	797	8	5.3
Wyoming	-	172	378	196	746	9	5.0
Western States Average[d]	$220	$233	$445	$205	$980		6.5%

Source: Stephen E. Lile, "Interstate Comparison of Family Tax Burdens with Residence Location Based on Each State's Largest City," Kentucky Department of Revenue, June 1978.

TABLE III-2

TOTAL DIRECT TAX BURDENS
ELEVEN WESTERN STATES

1976

$17,500 Adjusted Gross Income

	Income Tax[a]	Sales Tax[b]	Property Tax	Other Taxes[c]	Total	Rank	Total Taxes As % of Adjusted Gross Income
Arizona	$298	$296	$511	$224	$1,329	3	7.59%
California	273	248	795	193	1,509	2	8.62
Colorado	293	350	465	175	1,283	5	7.33
Idaho	434	170	532	158	1,294	4	7.39
Montana	477	-	469	207	1,153	7	6.59
Nevada	-	184	458	164	806	10	4.61
New Mexico	89	274	465	145	973	8	5.56
Oregon	581	-	819	128	1,528	1	8.73
Utah	456	293	318	200	1,267	6	7.24
Washington	-	298	308	248	854	9	4.88
Wyoming	-	187	420	196	803	11	4.59
Western States Average[d]	$363	$256	$505	$185	$1,164		6.65%

Source: Stephen E. Lile, "Interstate Comparison of Family Tax Burdens with Residence Location Based on Each State's Largest City," Kentucky Department of Revenue, June 1978.

TABLE III-2

TOTAL DIRECT TAX BURDENS
ELEVEN WESTERN STATES

1976

$25,000 Adjusted Gross Income

	Income Tax[a]	Sales Tax[b]	Property Tax	Other Taxes	Total	Rank	Total Taxes % of Adjusted Gross Income
Arizona	$616	$278	$ 657	$294	$1,845	4	7.38%
California	636	295	1,021	193	2,145	2	8.58
Colorado	653	205	598	380	1,836	5	7.34
Idaho	906	200	684	158	1,848	3	7.79
Montana	907	-	603	207	1,717	7	6.87
Nevada	-	217	589	164	970	11	3.88
New Mexico	355	322	588	145	1,420	8	5.68
Oregon	1,066	-	1,053	128	2,247	1	8.99
Utah	841	344	409	200	1,794	6	7.18
Washington	-	352	396	248	996	9	3.98
Wyoming	-	220	540	196	956	10	3.82
Western States Average[d]	$748	$270	$650	$210	$1,625		6.50%

Source: Stephen E. Lile, "Interstate Comparison of Family Tax Burdens with Residence Location Based on Each State's Largest City," Kentucky Department of Revenue, June 1978.

TABLE III-2

TOTAL DIRECT TAX BURDENS
ELEVEN WESTERN STATES

1976

$50,000 Adjusted Gross Income

	Income Tax[a]	Sales Tax[b]	Property Tax	Other Taxes[c]	Total	Rank	Total Taxes As % of Adjusted Gross Income
Arizona	$1,712	$405	$1,095	$325	$3,537	5	7.07%
California	2,818	429	1,702	193	5,142	1	10.28
Colorado	1,787	298	997	473	3,555	4	7.11
Idaho	2,574	291	1,140	158	4,163	3	8.33
Montana	2,246	-	1,005	207	3,458	6	6.92
Nevada	-	315	982	164	1,461	9	2.92
New Mexico	1,808	469	987	145	3,419	7	6.84
Oregon	3,103	-	1,755	128	4,986	2	9.87
Utah	1,988	501	682	200	3,371	8	6.74
Washington	-	512	660	248	1,420	10	2.84
Wyoming	-	320	900	190	1,416	11	2.83
Western States Average[d]	$2,255	$416	$1,083	$221	$3,265		6.53%

Source: Stephen E. Lile, "Interstate Comparison of Family Tax Burdens with Residence Location Based on Each State's Largest City," Kentucky Department of Revenue, June 1978.

[a]Combined state and local income taxes - income taxes are based on 1977.
[b]Combined state and local sales taxes.
[c]Includes motor vehicle taxes and cigarette excise tax.
[d]Unweighted average based only on those states that levy a particular tax. Those states that do not levy a tax are excluded from average.

liability, Montana ranks about the middle of the eleven states. Oregon's highly progressive income tax is the highest of the eleven states at the $25,000 and $50,000 income levels. As a result, even though Oregon does not impose sales taxes, it ranks first and second in terms of total liability at the $25,000 and $50,000 income levels.

Further examination of total tax liabilities in Arizona indicates that total liability falls as a percentage of income, as income increases. This relationship is shown in the table below.

Arizona Total Direct Taxes

Income	Total Tax Liability	Rank Among 11 Western States	Total Tax Liability as Percent of Income
$ 7,500	$ 798	1	10.6%
10,000	954	1	9.5
15,000	1,155	2	7.7
17,500	1,329	3	7.6
25,000	1,845	4	7.4
50,000	3,537	5	7.1

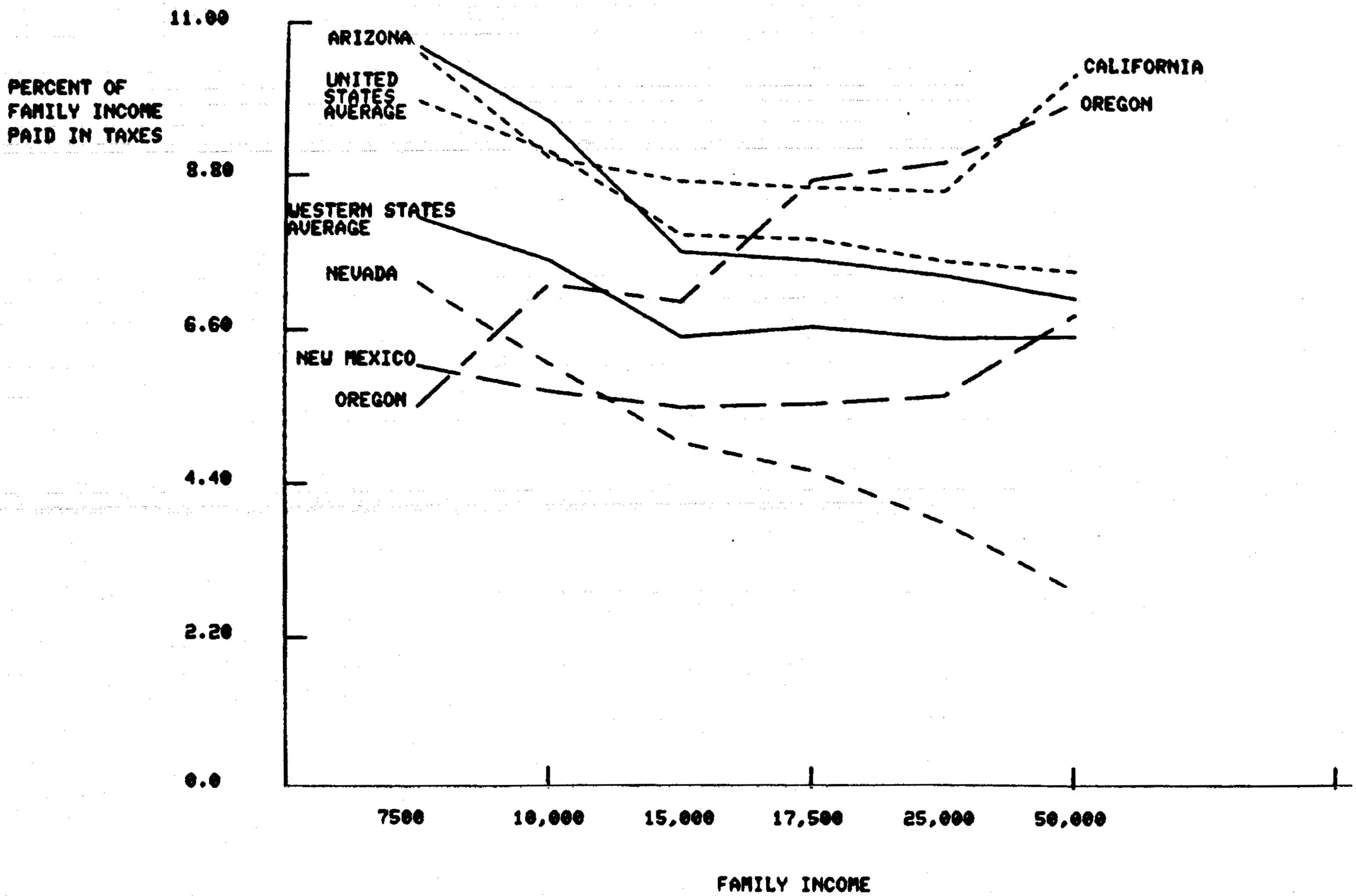
Figure III-4 graphically displays the tax bite as a percentage of family income for five of the eleven western states. Three of the states, Oregon, California and New Mexico have relatively progressive tax systems. In these states', tax liability as a percentage of income increases, as family income increases. In Arizona and Nevada, taxes are somewhat regressive, as tax liability declines as a percentage of family income. For the western states region as a whole, taxes are regressive up to $15,000 of family income, and relatively proportional between $15,000 and $50,000.

Property Taxes. According to the Lile study, Arizona ranks third among the eleven western states in payments of property taxes, at the $7,500 and $10,000 income levels, and fourth for the four upper income brackets. The study also indicates that the property tax diminishes as a percentage of income as income increases.

It should be noted, however, that the property tax liability estimates provided in the Lile study do not account for the homeowner property tax reduction program in Arizona. During 1976, the tax year considered in the

Figure III-4

MAJOR STATE AND LOCAL TAXES
AS A PERCENTAGE OF FAMILY INCOME
SELECTED STATES



Lile study, the rebate program in Arizona reduced residential property taxes an average of 14% on a statewide basis. Although the omission of the homeowners' rebate from the Lile study results in an overestimation of the total amount of property taxes paid by a family in Arizona, it does not alter the conclusion that the property tax may be regressive with respect to income.

Income	Property Tax Liability	Rank Among 11 Western States	Property Tax Liability as Percent of Income
$ 7,500	$ 296	3	3.95%
10,000	350	3	3.50
15,000	460	4	3.07
17,500	511	4	2.92
25,000	657	4	2.63
50,000	1,095	4	2.19

Income Taxes

According to the Lile study, the income tax liability in Arizona ranks low among the western states that impose an income tax.

Table III-3 was constructed from the data in Table III-2, and shows effective income tax rates for the eight western states that levy an income tax. The Table also displays a U.S. income tax liability index for each state. The liability index indicates the extent to which a particular state's income tax liability is greater or less than the average of all states in the U.S. that impose an income tax. The index is calculated by dividing the tax liability of each state, at each income level by the average U.S. liability. If the resulting number is greater than one, this indicates that the particular state's liability is greater than the average of all states. An index number less than one indicates that the state liability is less than the U.S. average.

From the figures in Table III-3, it can be seen that the Arizona income tax takes an increasing percentage of family income at all income levels except $15,000. This is evidenced by the effective tax rates* calculated for each income level. Examination of the liability index at each income level also indicates that the Arizona income tax is below the U.S. average for all income groups examined.

*The effective tax rate is computed by dividing the state income tax liability for each state by family income.

Table III-3

EFFECTIVE 1977 INCOME TAX RATES

ELEVEN WESTERN STATES

State	$7,500 Family Income Effective Tax Rate	$7,500 Family Income U.S. Liability Index	$10,000 Family Income Effective Tax Rate	$10,000 Family Income U.S. Liability Index	$15,000 Family Income Effective Tax Rate	$15,000 Family Income U.S. Liability
Arizona	1.20%	.95	1.61%	.84	1.33%	.64
California	0.05	0.04	0.00	0	1.14	.55
Colorado	0.75	.59	1.38	.72	1.09	.52
Idaho	0.00	0	1.02	.53	1.81	.87
Montana	2.01	1.59	2.79	1.46	2.21	1.06
New Mexico	0.00	0	0.00	0	0.09	0.04
Oregon	2.35	1.85	2.99	1.56	2.01	.96
Utah	1.43	1.13	2.01	1.05	2.05	.98

State	$17,500 Family Income Effective Tax Rate	$17,500 Family Income U.S. Liability Index	$25,000 Family Income Effective Tax Rate	$25,000 Family Income U.S. Liability Index	$50,000 Family Income Effective Tax Rate	$50,000 Family Income U.S. Liability
Arizona	1.70%	.68	2.46%	.76	3.42%	.76
California	1.56	.62	2.54	.79	5.64	1.25
Colorado	1.67	.67	2.61	.81	3.57	.79
Idaho	2.48	.99	3.62	1.12	5.15	1.14
Montana	2.73	1.09	3.63	1.13	4.49	1.00
New Mexico	0.51	.20	1.42	.44	3.62	.80
Oregon	3.32	1.33	4.26	1.32	6.21	1.38
Utah	2.61	1.04	3.36	1.04	3.98	.88

Similar conclusions about the income tax can be derived from a study prepared by the Minnesota Department of Revenue. The Minnesota study estimated income tax liabilities for tax year 1977 for twenty-three income levels and four filing types.* Data from the Minnesota study are summarized in Table III-4 for three of the four filing classes defined in the study.

In analyzing the data from the Minnesota study the following conclusions can be drawn:

- For the two married filing types, the effective Arizona Tax rate increases with respect to gross income up to $50,000 gross income. For the two highest income brackets, the rate declines. For the single filer, the effective tax rate increases up to $30,000 and declines thereafter.

- For the single tax filer, the Arizona income tax liability is greater than the average of all states up to the $20,000 income level, and below the average of all states between $20,000 and $50,000 of family income.

- For the single tax filer, the Arizona income tax liability is below the western states' average at all income levels.

- For the married filers, the Arizona tax liability is equal to or below that of all the western states except in one instance--married with two wage earners, and married with one wage earner earning $6,000 gross income.

- Comparing Arizona income tax liability to average U.S. income tax liability, the Arizona tax liability index is above 1 for all filing types at the $6,000 income bracket. However, the index falls to between .69 and .74 at the $100,000 bracket. This is an indication that the Arizona income tax is far less progressive than the U.S. average, and especially so at the highest income bracket.

2. TAX RELIANCE

As mentioned previously, a state's taxation structure is shaped by many factors. Economic, political and social infrastructure all play vital roles in determining the mix and types of taxes imposed in a state.

a. Aggregate State and Local Reliance

Figures III-5 and III-6 present the distribution of own source general revenue in 1967 and 1977 by major level of government for the State of Arizona. The distribution chart in the upper right hand portion of Figures III-5 and III-6 shows combined state and local revenues, while the two distribution charts at the bottom of each figure show the state and local government revenues separately.

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*Minnesota Department of Revenue Research Office, "A Comparison of Individual Income Tax Liabilities: Tax Year 1977," 1978.

Table III-4

Effective Income Tax Rates

Arizona
1977

	Single Filer	Married, One Wage Earner	Married, Two Wage Earners - 75/25 Earnings Split
$6,000			
Effective tax rate	.20%	.62%	.62%
U.S. Index	1.06	.71	1.56
Western States Index	.96	2.31	2.64
$12,000			
Effective tax rate	3.19%	1.56%	1.52%
U.S. Index	1.05	.81	.96
Western States Index	.92	.88	.98
$15,000			
Effective tax rate	4.38%	1.88%	1.88%
U.S. Index	1.08	.80	.94
Western States Index	.97	.82	.87
$20,000			
Effective tax rates	3.81%	3.17%	2.37%
U.S. Index	1.04	.83	.96
Western States Index	.94	.84	.90
$30,000			
Effective tax rate	3.94%	3.16%	3.16%
U.S. Index	.91	.89	1.00
Western States Index	.87	.87	.92
$50,000			
Effective tax rate	3.78%	3.53%	3.53%
U.S. Index	.80	.83	.90
Western States Index	.77	.80	.82
$70,000			
Effective Tax Rate	3.66%	3.49%	3.49%
U.S. Index	.74	.75	.81
Western States Index	.72	.74	.76
$100,000			
Effective tax rate	3.57%	3.45%	3.45%
U.S. Index	.69	.70	.74
Western States Index	.69	.70	.72

Source: Minnesota Department of Revenue, Research Office, "A Comparison of Individual Income Tax Liabilities: Tax Year 1977," 1978.

From Figures III-5 and III-6, the following general conclusions can be drawn:

- Between 1967 and 1977 dependence on the property tax has declined somewhat for state and local govenments combined--36% to 31%. Dependence on the property tax has decreased at the state level--from 12% to 10% and at the local level--66% to 59%.

- Dependence on the income tax has increased at the state level from 7% in 1967 to 18% in 1977. This resulted in a change in dependence for combined state and local governments from 4% in 1967 to 10% in 1977.

- Dependence on sales taxes and other gross receipts taxes has increased between 1967 and 1977 for combined state and local governments--from 19% to 26%.

For a comparison of 1977 distribution of own source general revenue for the ten other western states, the reader is referred to Appendix III-2.

b. State, Counties and Municipalities in Arizona

Distribution of revenue collections of the state, counties and municipalities in Arizona is shown in greater detail in Figures III-7, III-8 and III-9.

In Figure III-7, 1977-78 revenue collections of the state are shown. The data were derived from several sources including: 1977-78 Annual Financial Report, Department of Administration, Finance Division, p. 4; 1977-78 Annual Report of the Arizona Department of Revenue; 1978 State of Arizona Tax Handbook; Department records of the Arizona Department of Transportation; Department records of the Arizona Department of Administration.

From Figure III-7, the state derives over 33% of its revenue from combined sales and use taxes. Almost 17% of the state's revenue is generated by individual and corporate income taxes. The general property tax accounts for 6.3% of total revenue, and property taxes from all sources contributes about 8%. Aid from the federal government accounts for 16.9%.

Figure III-8 shows revenue sources for all Arizona counties and for Maricopa County in 1975-76. In aggregate, counties rely on the property tax for about 47% of total general revenue. State shared revenues and state transfers account for 27% of total county general revenue, while the federal government supplies over 10% of total county revenue in Arizona. The distribution of revenue collections in Maricopa County shown in the right pie chart of Figure III-8 is similar to that of all counties.

In Figure III-9, distribution of city revenue collections in 1975-76 is presented. The left hand chart shows revenue collections for all Arizona cities, while the right hand chart shows the distribution of collections for the City of Phoenix. On the average, Arizona cities derive 10.8% of total general revenue from property taxes; 20.5% from revenue transfers from the state; 14.2% from revenue transfers from the federal government; 15.6% from municipality operated utilities; and 37.2% from other taxes, charges and miscellaneous revenues.

The City of Phoenix derives 14% of its total general revenue from property taxes. Phoenix also is more dependent on federal aid (17.4%) than are other cities in the state. Phoenix depends on general sales taxes for 13.14% of its revenues and selective sales taxes for another 6.4%.

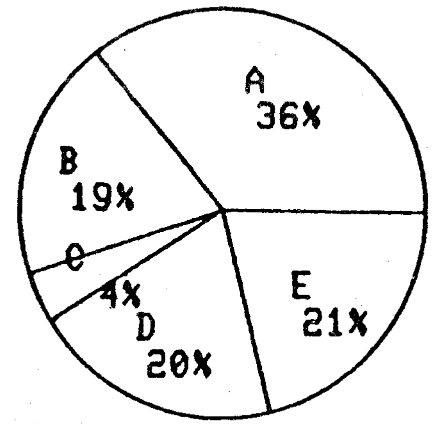
Figure III-5

TAX REVENUE BY SOURCES 1987
ARIZONA

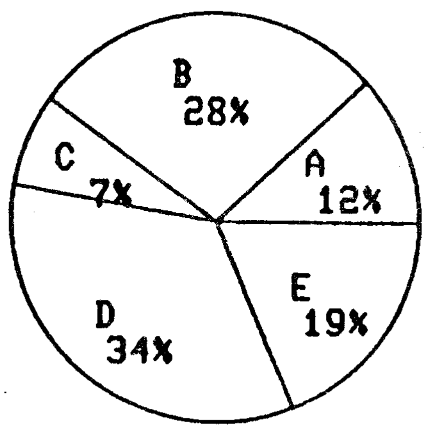
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $684.00 million
STATE OWN SOURCE GENERAL REVENUE = $388.00 million
LOCAL OWN SOURCE GENERAL REVENUE = $296.00 million

STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

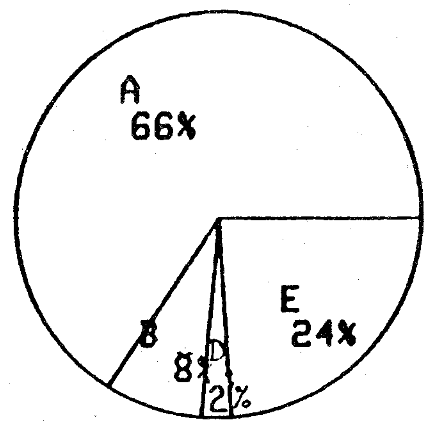


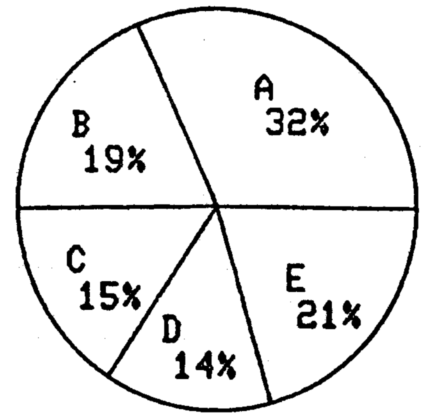
Figure III-6

TAX REVENUE BY SOURCES 1977
WESTERN STATES

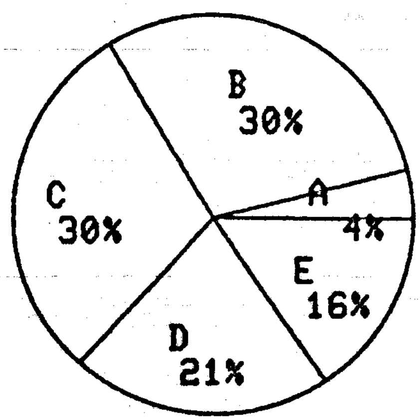
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $45869.00 MILLION
STATE OWN SOURCE GENERAL REVENUE = $24008.80 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $21860.20 MILLION

STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

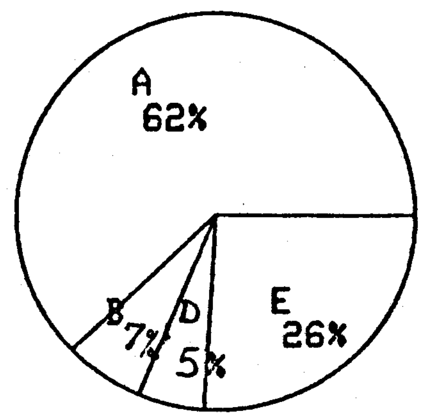
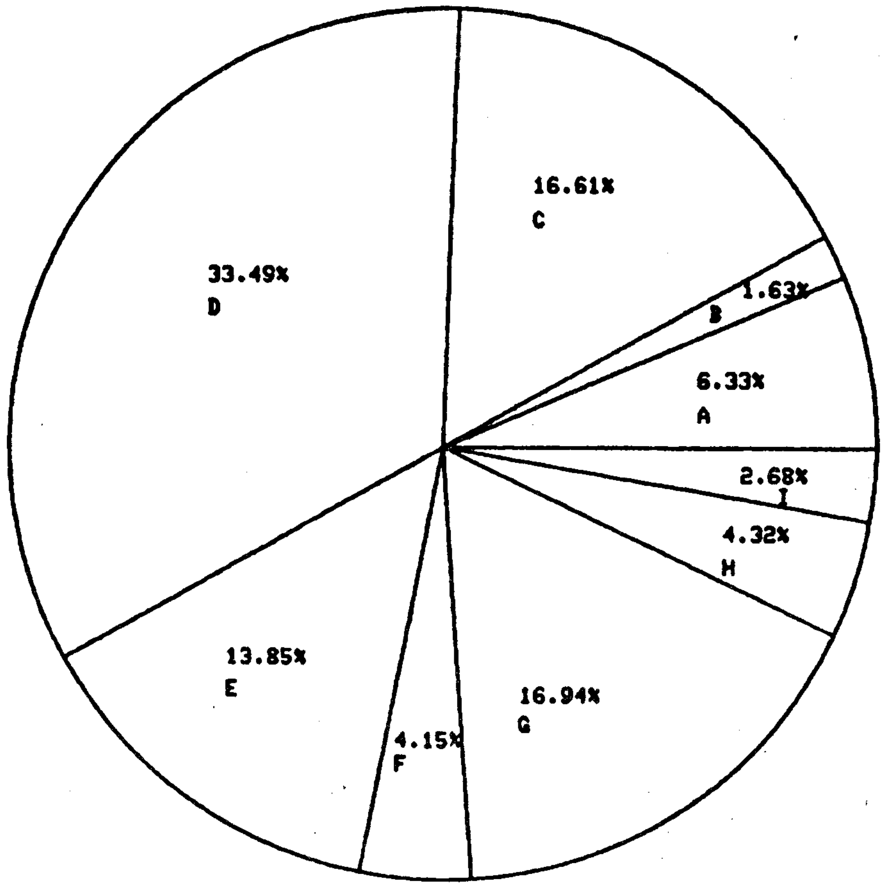


Figure III-7

SOURCES OF ARIZONA STATE REVENUE

BEFORE DISTRIBUTION TO LOCAL GOVERNMENTS

1977-78



A = GENERAL PROPERTY TAXES

B = OTHER PROPERTY TAXES

C = INCOME TAXES

D = SALES AND USE TAXES

E = OTHER TAXES

F = LICENSES, FEES AND PERMITS

G = FEDERAL AID

H = SALES AND SERVICES

I = MISCELLANEOUS

TOTAL REVENUE = $1,725,466,329

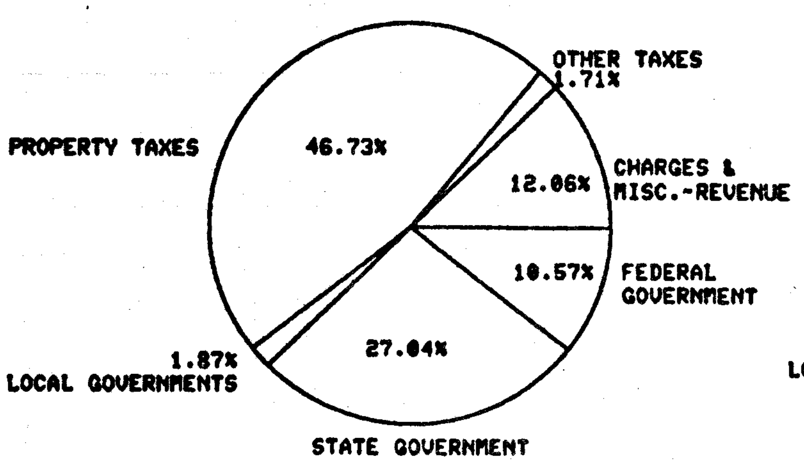
SOURCES: 1977-78 ANNUAL FINANCIAL REPORT, DEPARTMENT OF ADMINISTRATION, FINANCE DIVISION, OCTOBER 1978, P.4. 1977-78 ANNUAL REPORT OF THE ARIZONA DEPARTMENT OF REVENUE; 1978 STATE OF ARIZONA TAX HANDBOOK; ARIZONA DEPARTMENT OF TRANSPORTATION, DEPT. RECORDS; ARIZONA DEPARTMENT OF ADMINISTRATION, DEPT. RECORDS.

Figure III-8

COUNTY REVENUE SOURCES
ARIZONA COUNTIES
1975-76

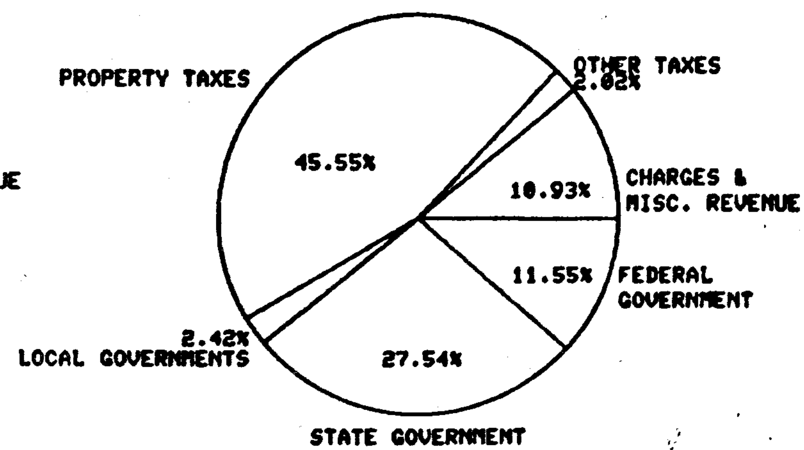
ALL COUNTIES

TOTAL REVENUE: $380,500,000



MARICOPA COUNTY

TOTAL REVENUE: $190,198,000



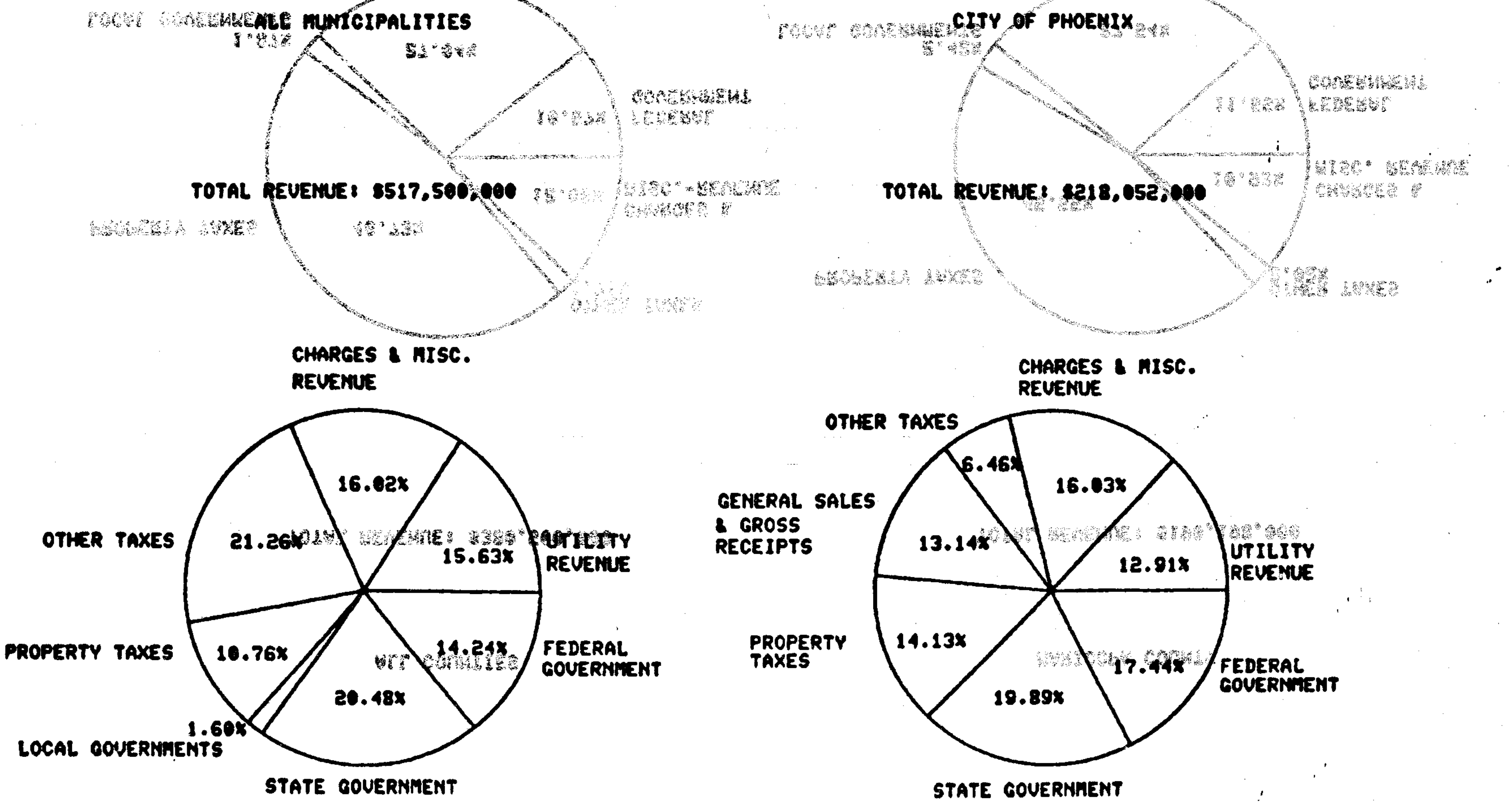
SOURCES: GOVERNMENTAL FINANCES IN 1975-76, U.S. BUREAU OF THE CENSUS, GOVERNMENTS DIVISION, SEPTEMBER 1977, P.30.
COUNTY GOVERNMENT FINANCES IN 1975-76, U.S. BUREAU OF THE CENSUS, GOVERNMENTS DIVISION, OCTOBER 1977, P.10.

Figure III-9

MUNICIPAL REVENUE SOURCES

ARIZONA CITIES

1975-76



SOURCES: GOVERNMENTAL FINANCES IN 1975-76, U.S. BUREAU OF THE CENSUS, GOVERNMENTS DIVISION, SEPTEMBER 1977, P.30.
LOCAL GOVERNMENT FINANCES IN SELECTED METROPOLITAN AREAS AND LARGE COUNTIES:1975-76, U.S. BUREAU OF THE CENSUS, GOVERNMENTS DIVISION, NOVEMBER 1977, P.92.

APPENDIX III-1

PER CAPITA OWN SOURCE GENERAL REVENUE:

1967-1977 IN CURRENT DOLLARS AND CONSTANT

1967 DOLLARS

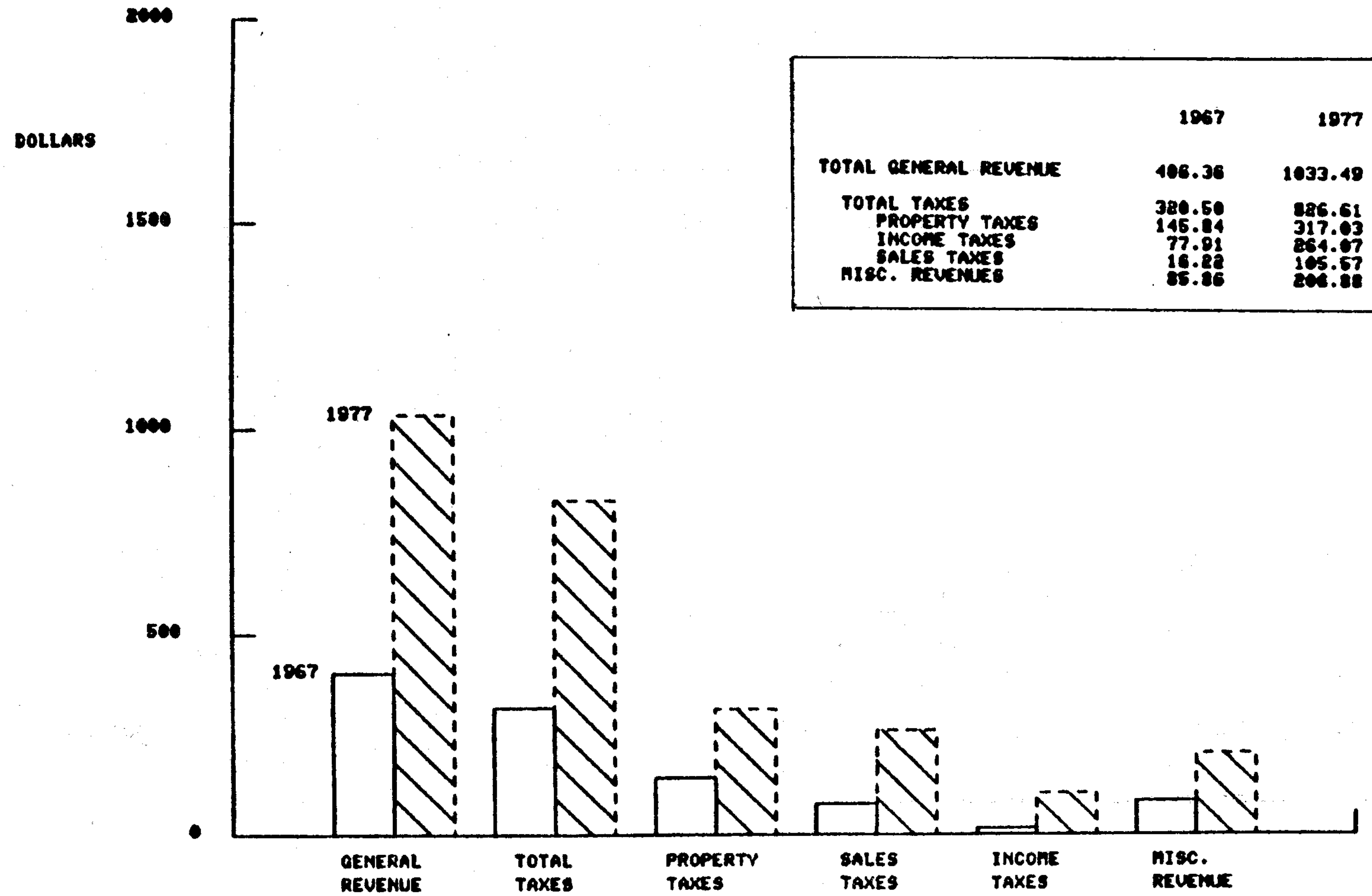
WESTERN STATES

PER CAPITA OWN SOURCE REVENUE

STATE AND LOCAL GOVERNMENTS

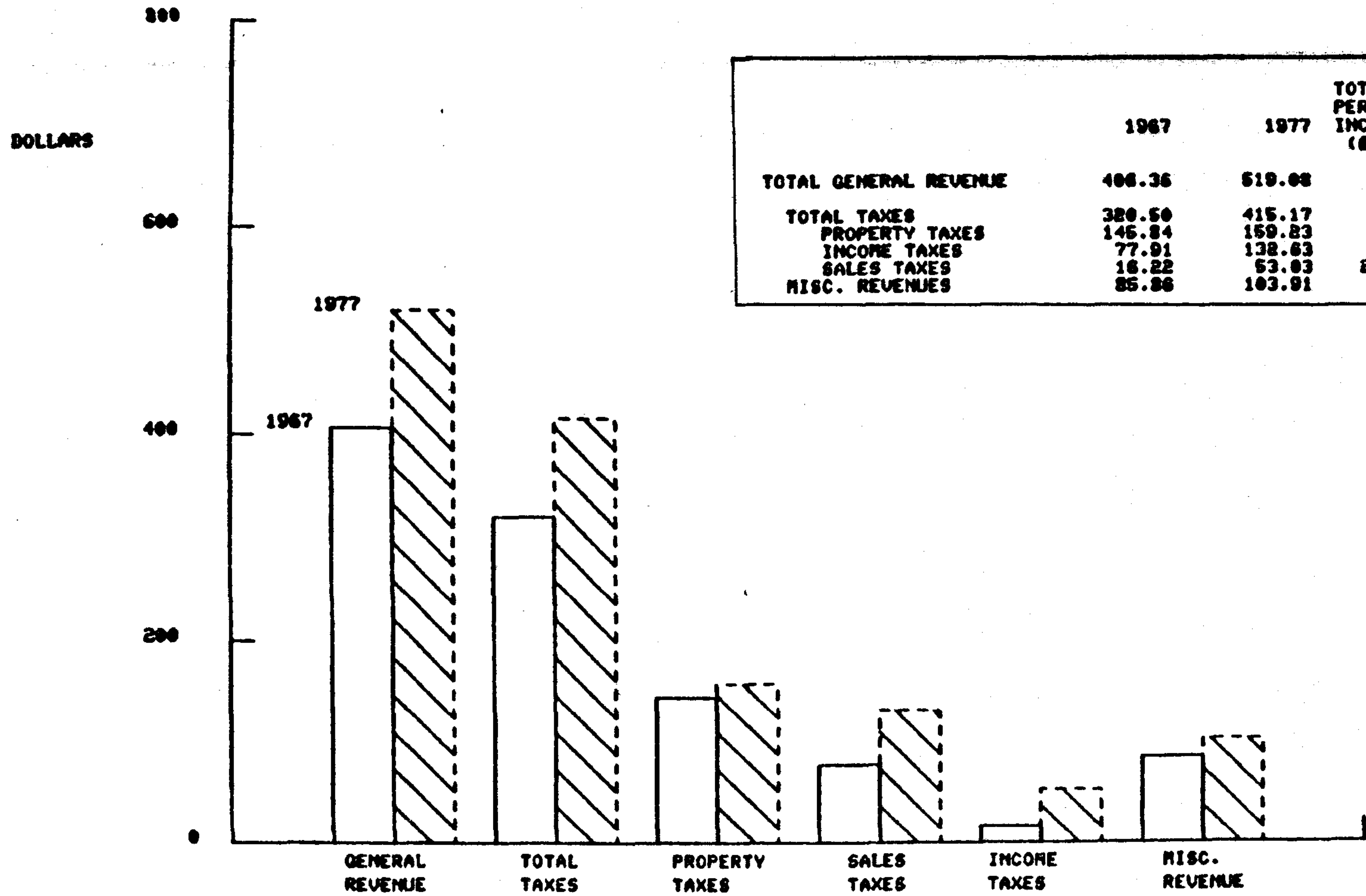
ARIZONA 1967 VS. 1977

CURRENT $$



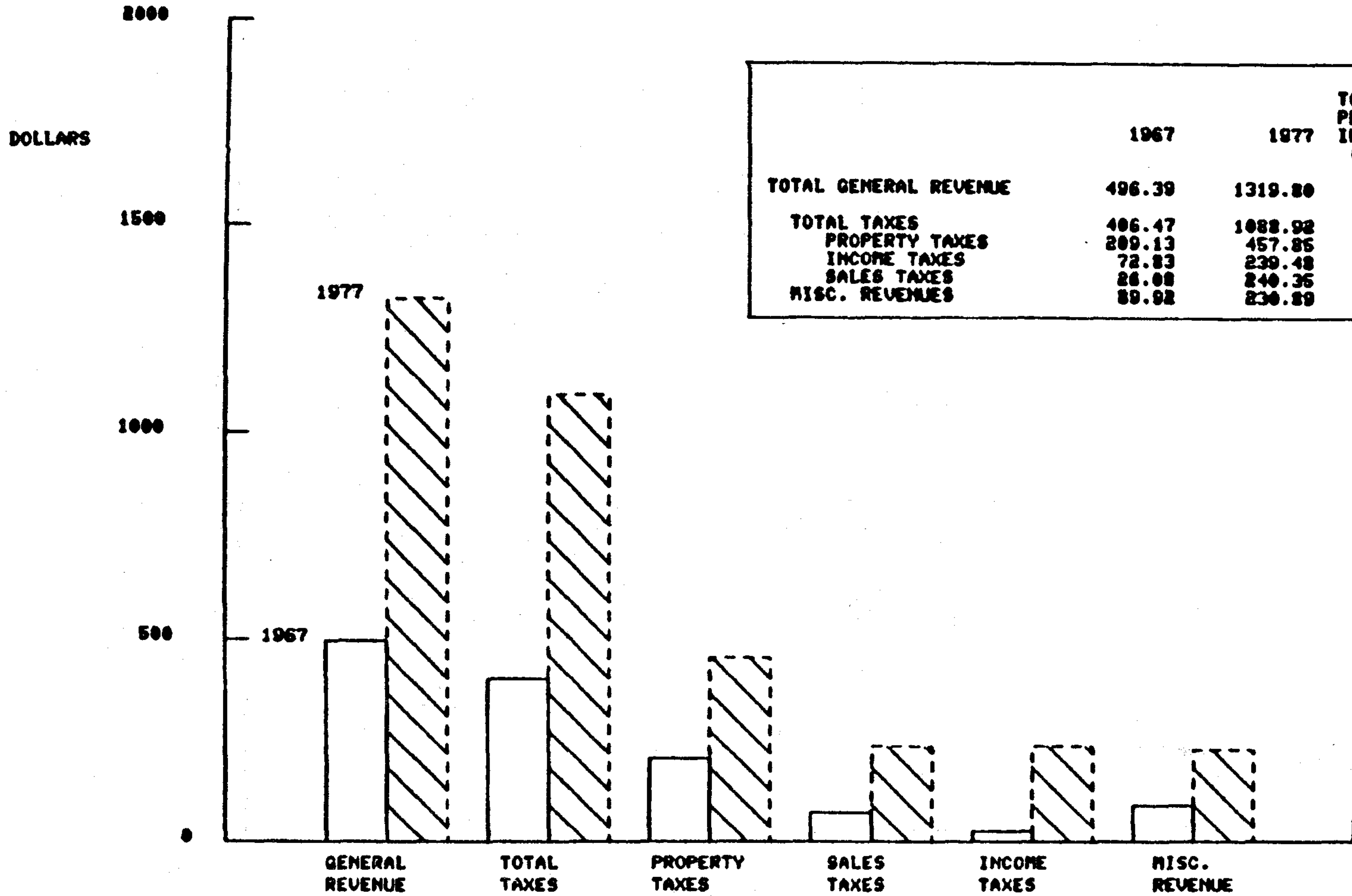
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	406.36	1033.49	154.33	9.78
TOTAL TAXES	320.50	826.61	157.91	9.94
PROPERTY TAXES	145.84	317.03	117.38	8.07
INCOME TAXES	77.91	264.07	238.95	12.98
SALES TAXES	16.22	105.57	550.98	20.60
MISC. REVENUES	85.86	206.88	140.94	9.19

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
ARIZONA 1967 VS. 1977
CONSTANT 1967 $



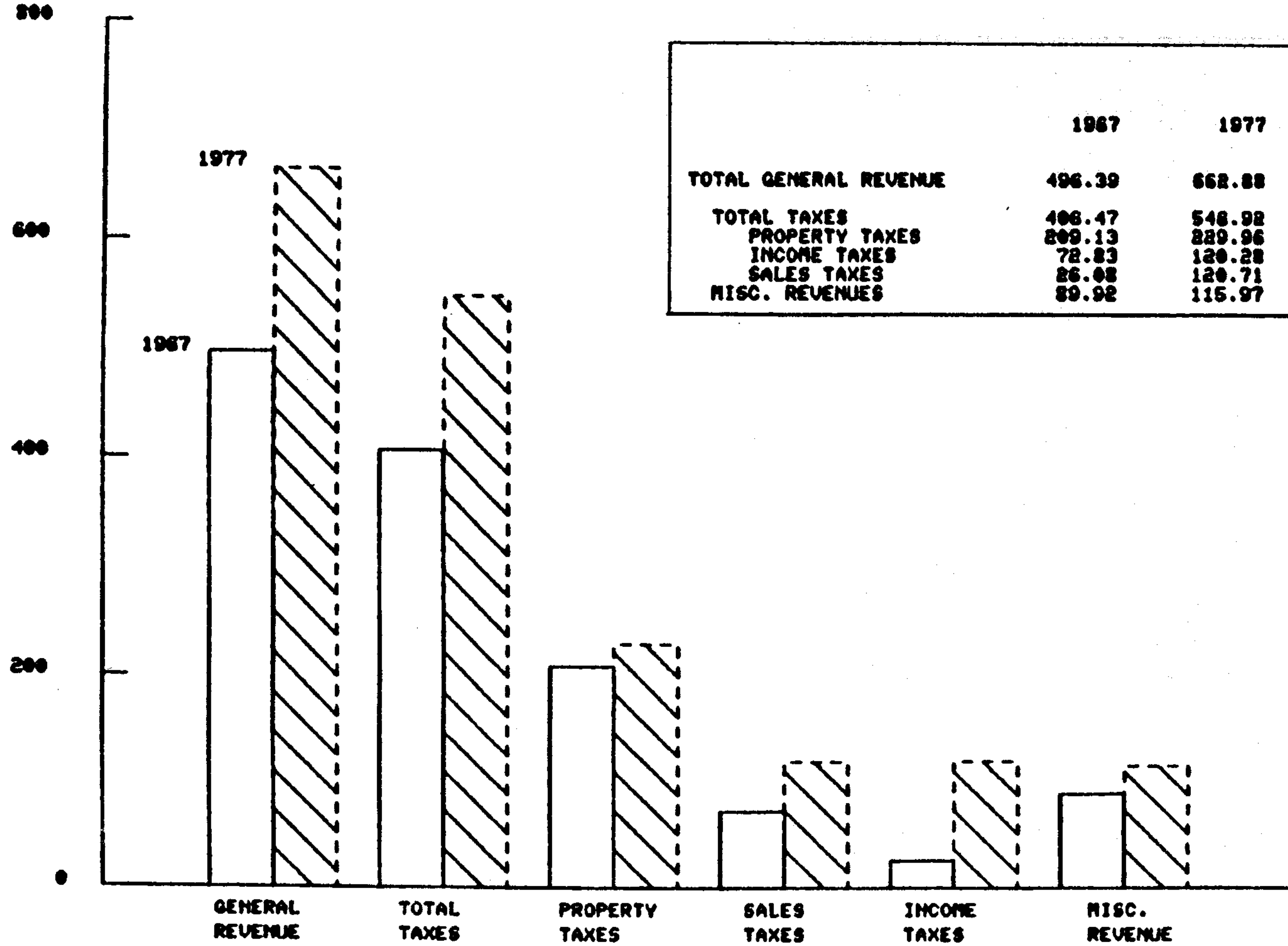
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	406.36	519.08	27.74	2.48
TOTAL TAXES	320.50	415.17	29.54	2.62
PROPERTY TAXES	146.84	159.83	9.18	.88
INCOME TAXES	77.91	132.63	70.24	5.46
SALES TAXES	16.22	53.03	226.96	12.58
MISC. REVENUES	85.86	103.91	21.02	1.93

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
CALIFORNIA 1967 VS. 1977
CURRENT $$



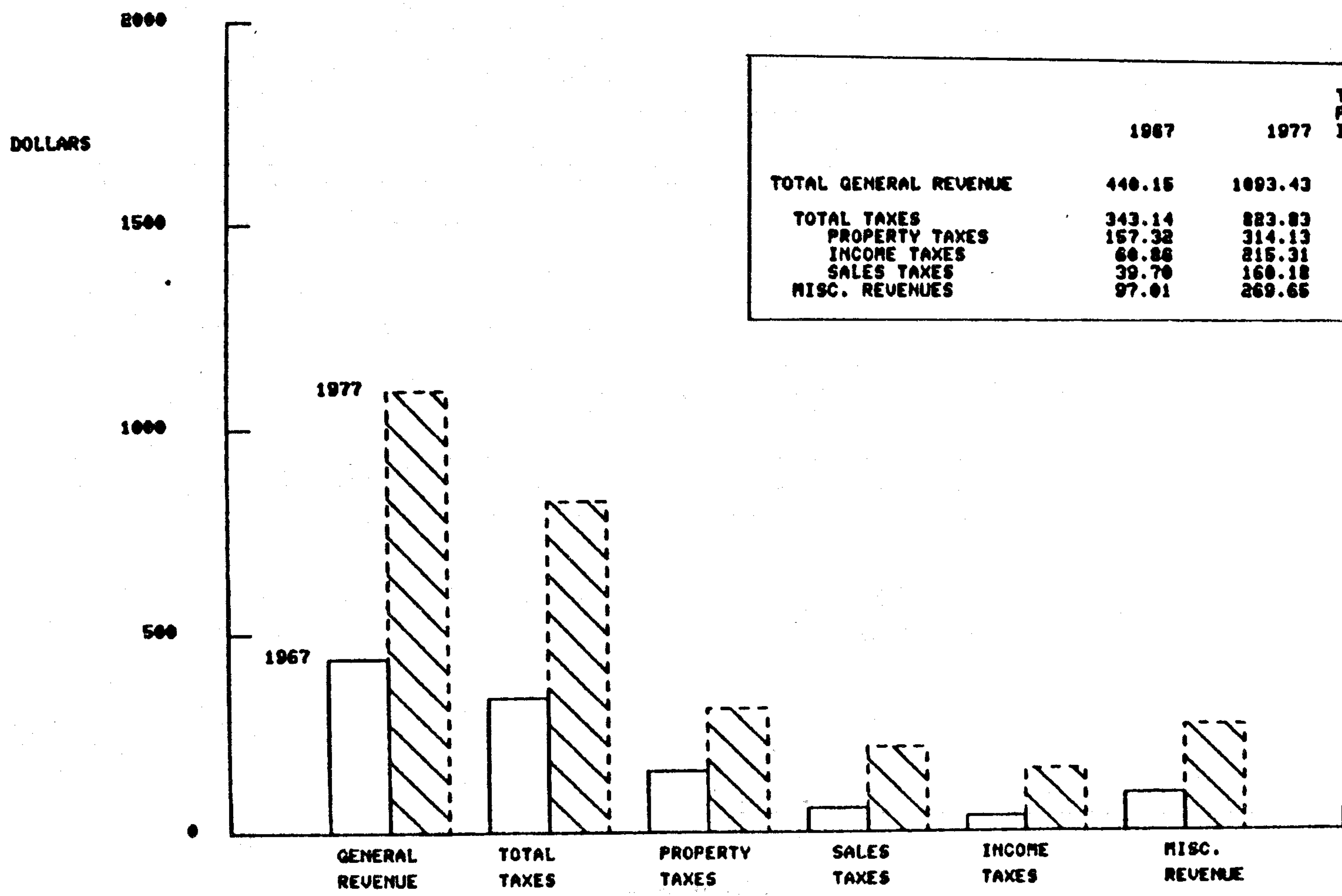
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	496.39	1319.80	165.88	10.27
TOTAL TAXES	406.47	1088.92	167.89	10.36
PROPERTY TAXES	209.13	457.85	118.93	8.15
INCOME TAXES	72.83	239.48	228.80	12.64
SALES TAXES	26.08	240.36	821.57	24.87
MISC. REVENUES	89.92	230.89	156.77	9.89

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
CALIFORNIA 1967 VS. 1977
CONSTANT 1967 $



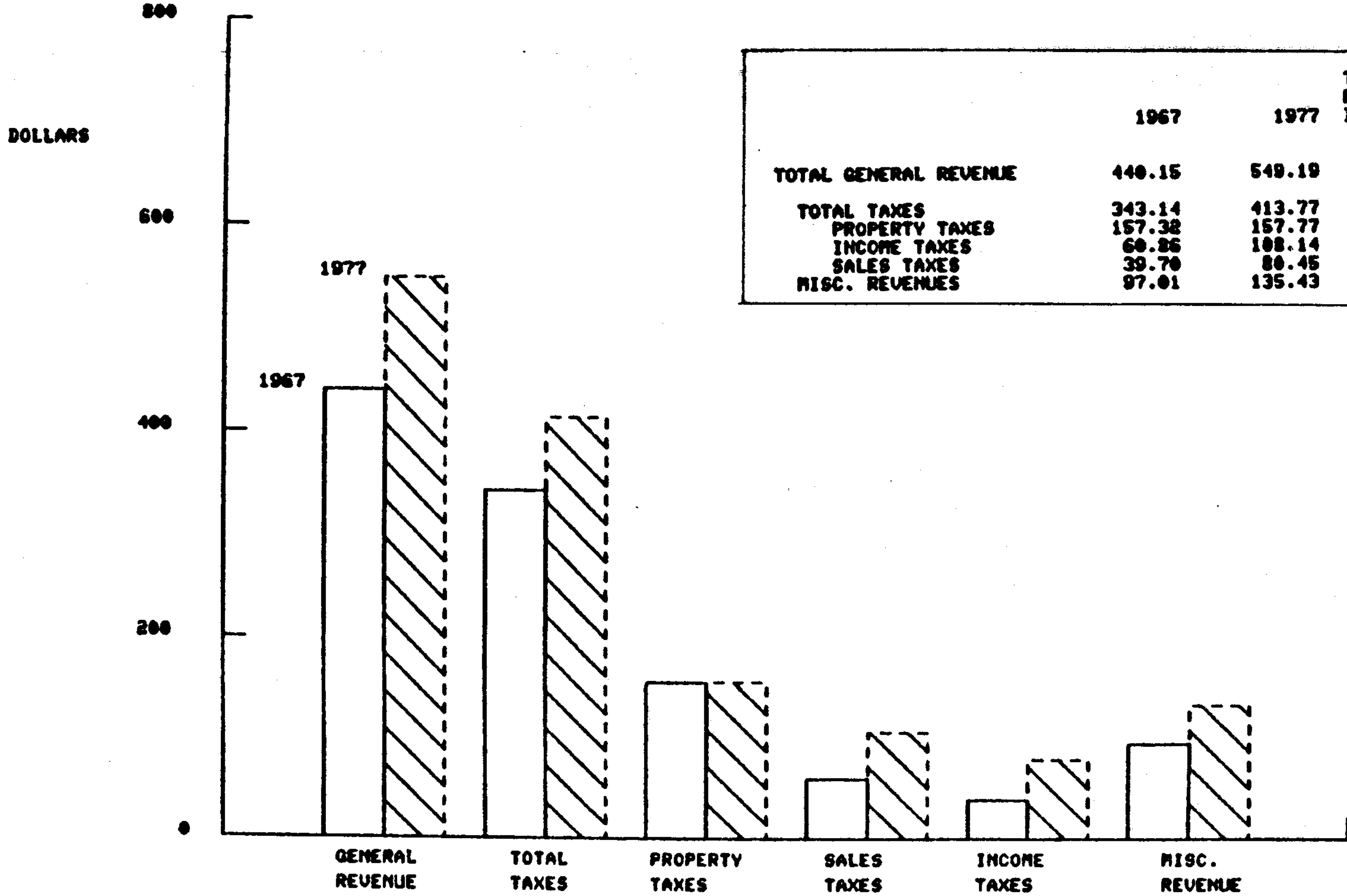
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	496.39	662.88	33.54	2.93
TOTAL TAXES	406.47	546.92	34.55	3.01
PROPERTY TAXES	209.13	229.96	9.96	.95
INCOME TAXES	72.83	120.28	65.14	5.14
SALES TAXES	26.08	120.71	362.87	16.56
MISC. REVENUES	89.92	115.97	28.97	2.58

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
COLORADO 1967 VS. 1977
CURRENT $$



	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	440.15	1093.43	148.42	9.53
TOTAL TAXES	343.14	823.83	140.09	9.15
PROPERTY TAXES	157.32	314.13	99.68	7.16
INCOME TAXES	60.86	215.31	253.78	13.47
SALES TAXES	39.70	160.18	303.50	14.97
MISC. REVENUES	97.01	269.65	177.95	10.76

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
COLORADO 1967 VS. 1977
CONSTANT 1967 $



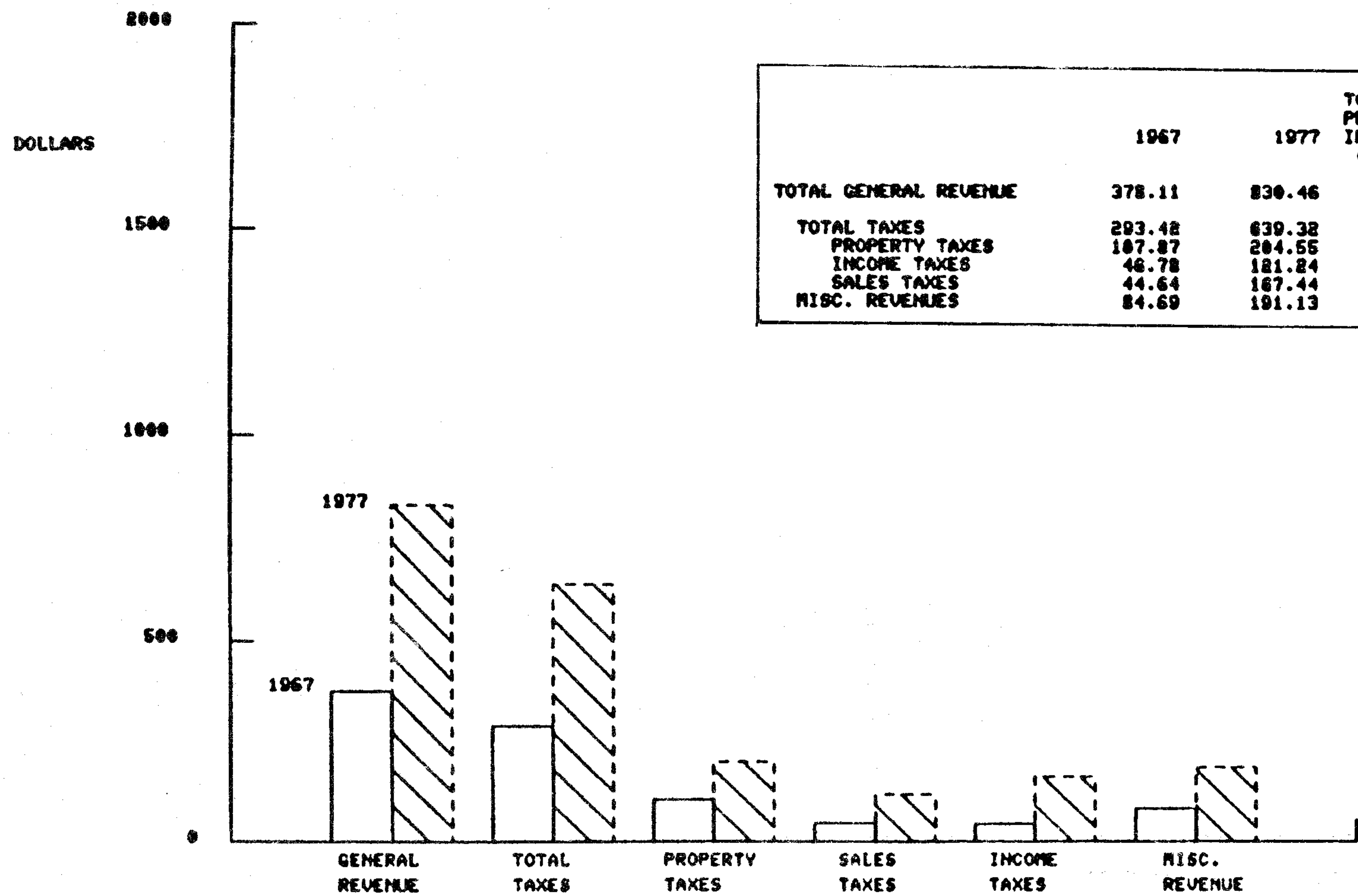
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	440.15	549.19	24.77	2.24
TOTAL TAXES	343.14	413.77	20.59	1.89
PROPERTY TAXES	157.38	157.77	.29	.03
INCOME TAXES	60.86	108.14	77.69	5.92
SALES TAXES	39.70	80.45	102.66	7.32
MISC. REVENUES	97.01	135.43	39.60	3.39

PER CAPITA OWN SOURCE REVENUE

STATE AND LOCAL GOVERNMENTS

IDAHO 1967 VS. 1977

CURRENT $$



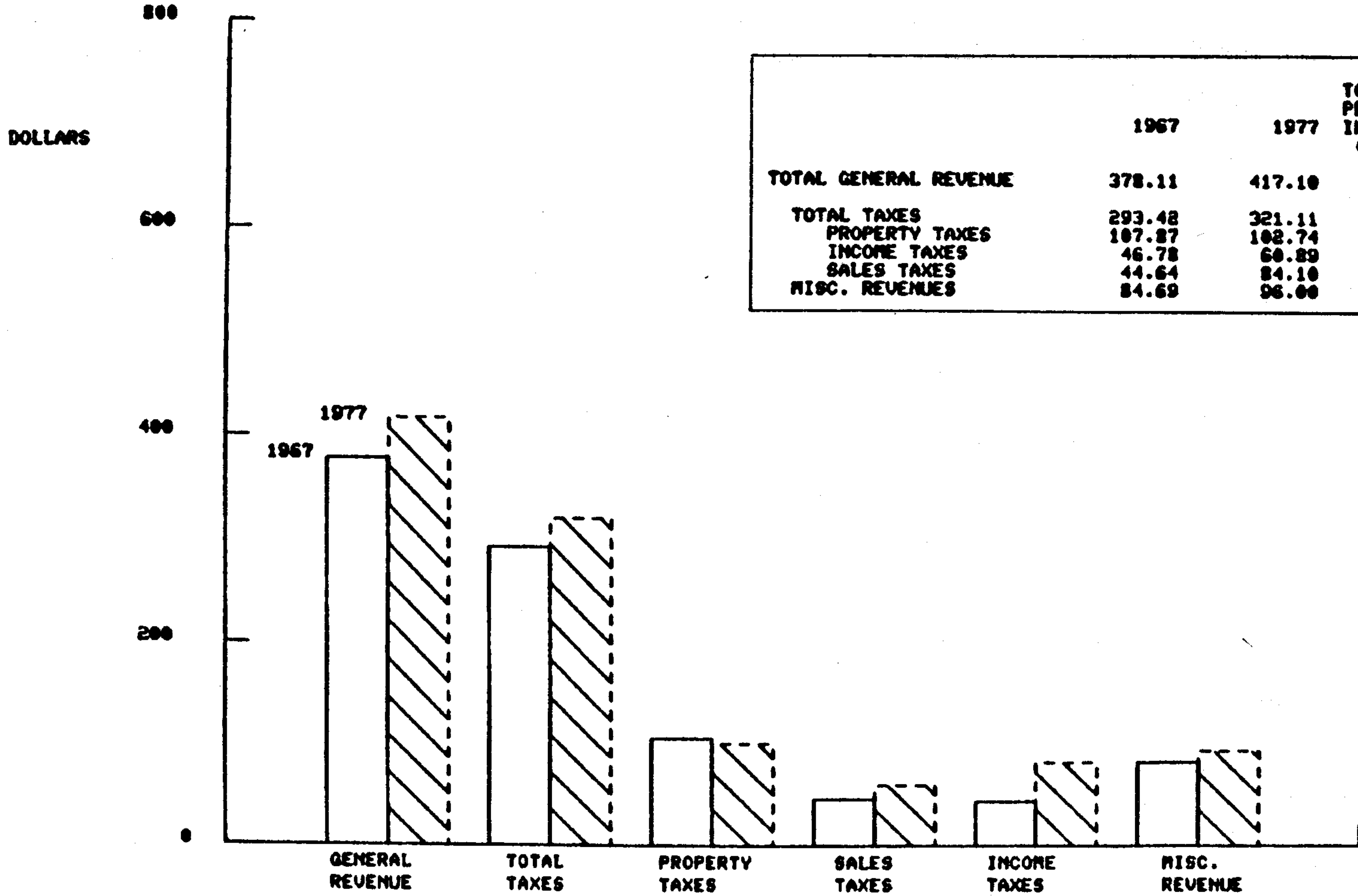
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	378.11	830.46	119.63	8.19
TOTAL TAXES	293.42	639.32	117.89	8.10
PROPERTY TAXES	107.87	204.55	89.63	6.61
INCOME TAXES	46.78	121.24	159.16	9.99
SALES TAXES	44.64	167.44	275.14	14.14
MISC. REVENUES	84.69	191.13	125.68	8.48

PER CAPITA OWN SOURCE REVENUE

STATE AND LOCAL GOVERNMENTS

IDAHO 1967 VS. 1977

CONSTANT 1967 $



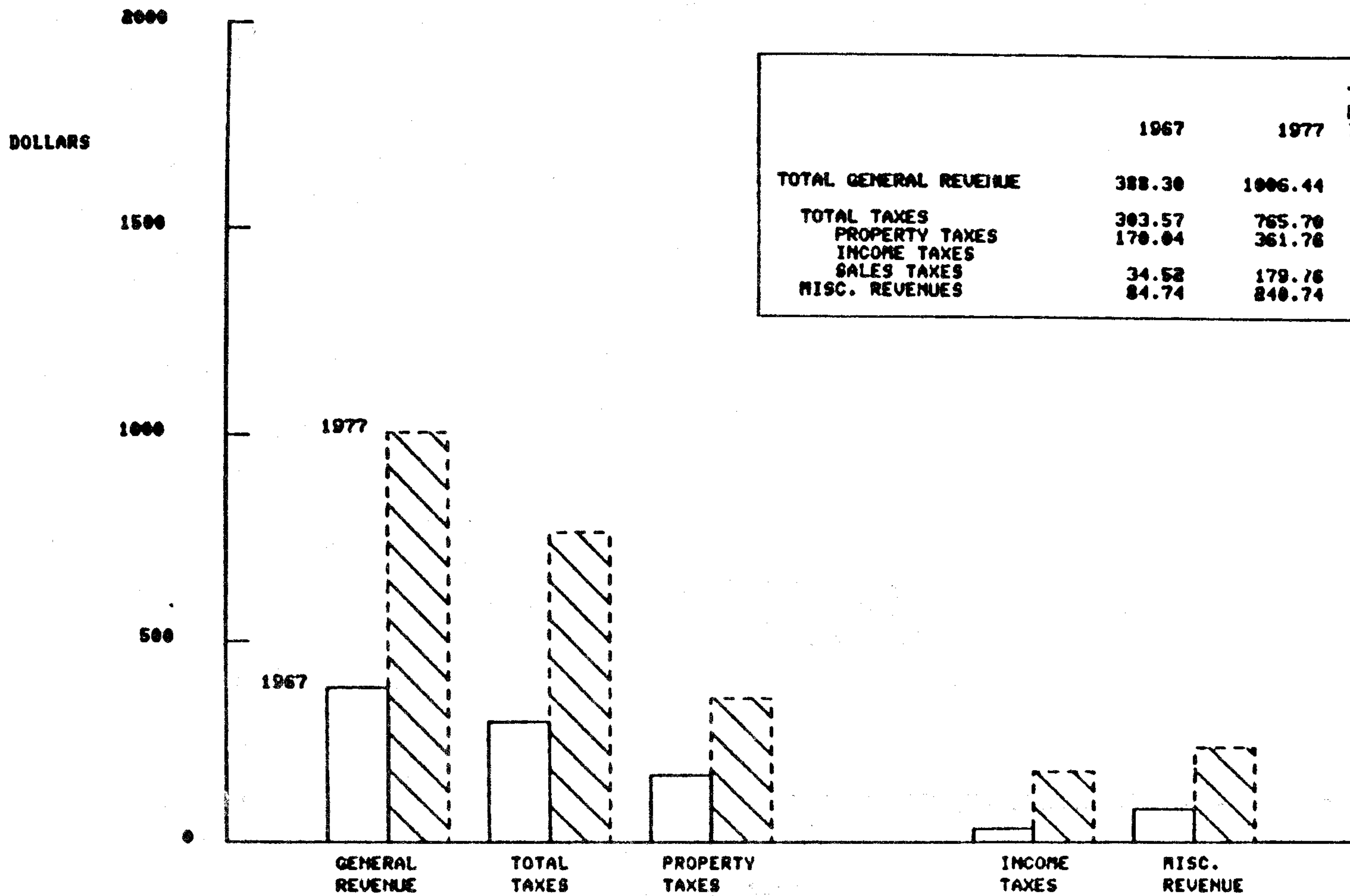
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	378.11	417.10	10.31	.99
TOTAL TAXES	293.48	321.11	9.44	.91
PROPERTY TAXES	107.87	102.74	(4.76)	(.49)
INCOME TAXES	46.78	60.89	30.16	2.67
SALES TAXES	44.64	84.10	88.42	6.54
MISC. REVENUES	84.69	96.00	13.35	1.26

PER CAPITA OWN SOURCE REVENUE

STATE AND LOCAL GOVERNMENTS

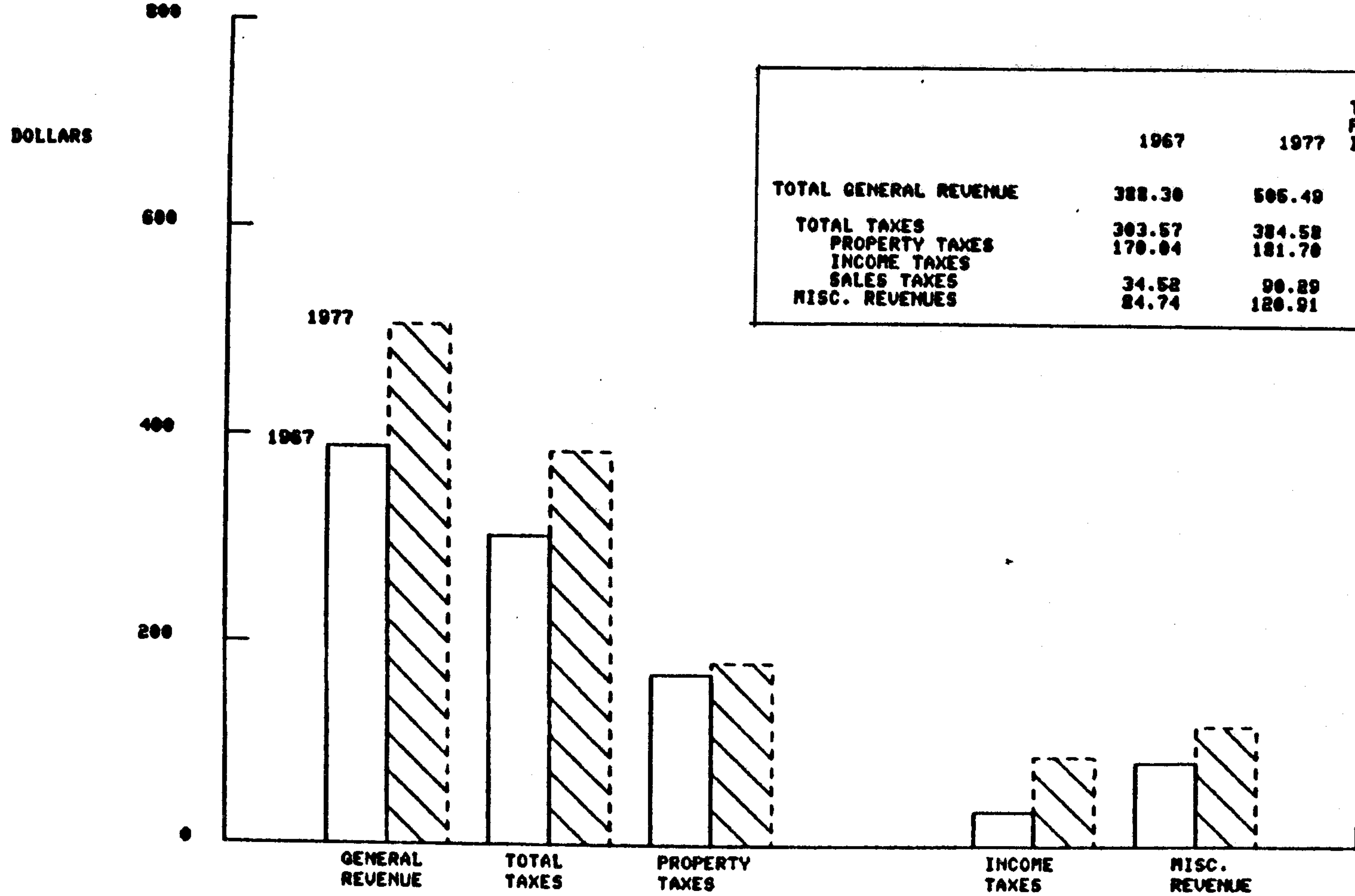
MONTANA 1967 VS. 1977

CURRENT $S



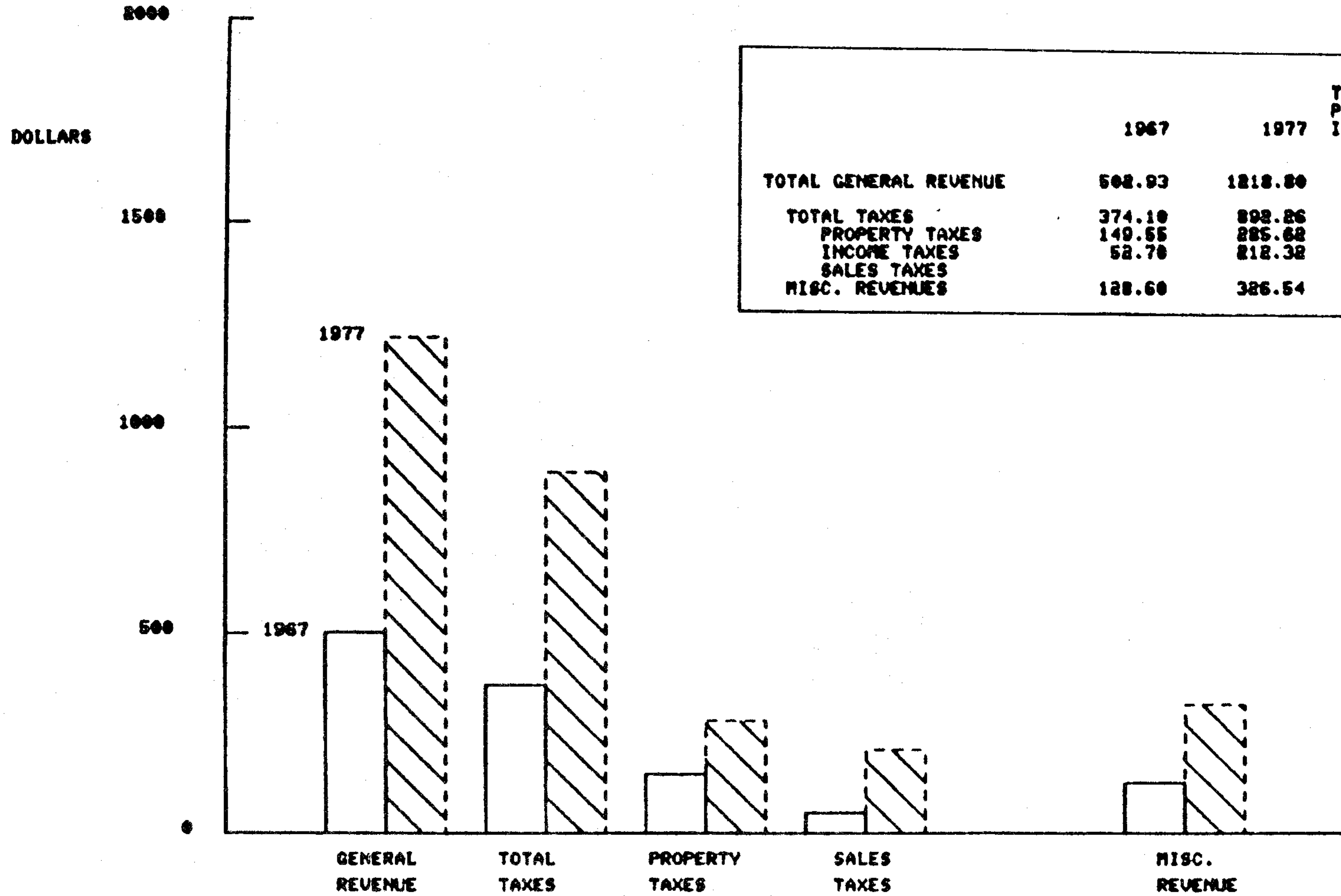
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	388.30	1006.44	159.19	9.99
TOTAL TAXES	303.57	765.70	152.24	9.69
PROPERTY TAXES	170.04	361.76	112.75	7.84
INCOME TAXES				
SALES TAXES	34.52	179.76	420.72	17.94
MISC. REVENUES	84.74	240.74	184.10	11.01

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
MONTANA 1967 VS. 1977
CONSTANT 1967 $



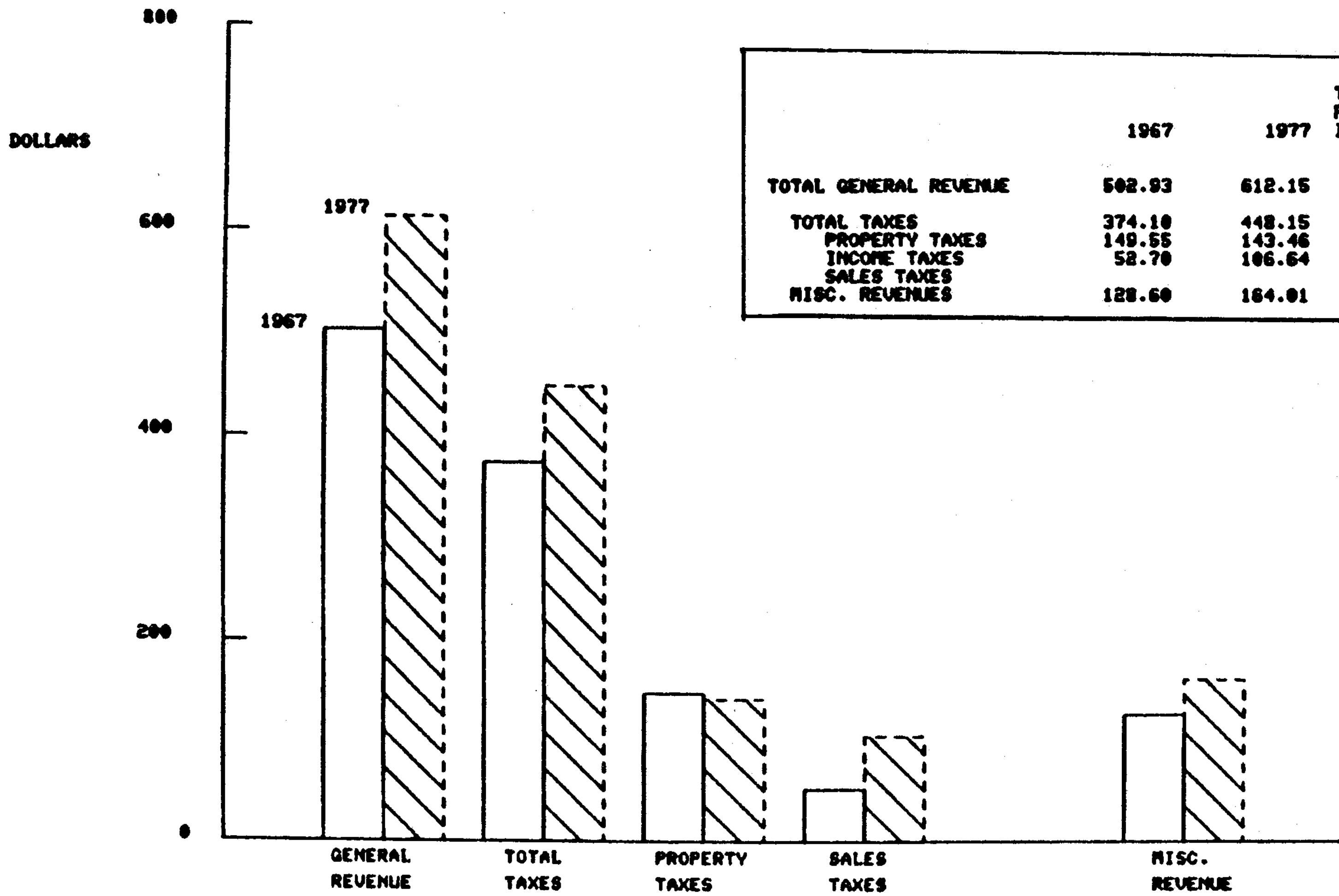
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	388.30	505.49	30.18	2.67
TOTAL TAXES	303.57	384.58	26.69	2.39
PROPERTY TAXES	170.04	181.70	6.85	.67
INCOME TAXES				
SALES TAXES	34.58	90.29	161.54	10.09
MISC. REVENUES	84.74	120.91	42.69	3.62

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
NEVADA 1967 VS. 1977
CURRENT $S



	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	502.93	1218.80	142.34	9.26
TOTAL TAXES	374.10	892.26	138.51	9.08
PROPERTY TAXES	149.55	285.62	90.99	6.68
INCOME TAXES	52.70	212.32	302.87	14.95
SALES TAXES				
MISC. REVENUES	128.60	326.54	153.91	9.77

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
NEVADA 1967 VS. 1977
CONSTANT 1967 $



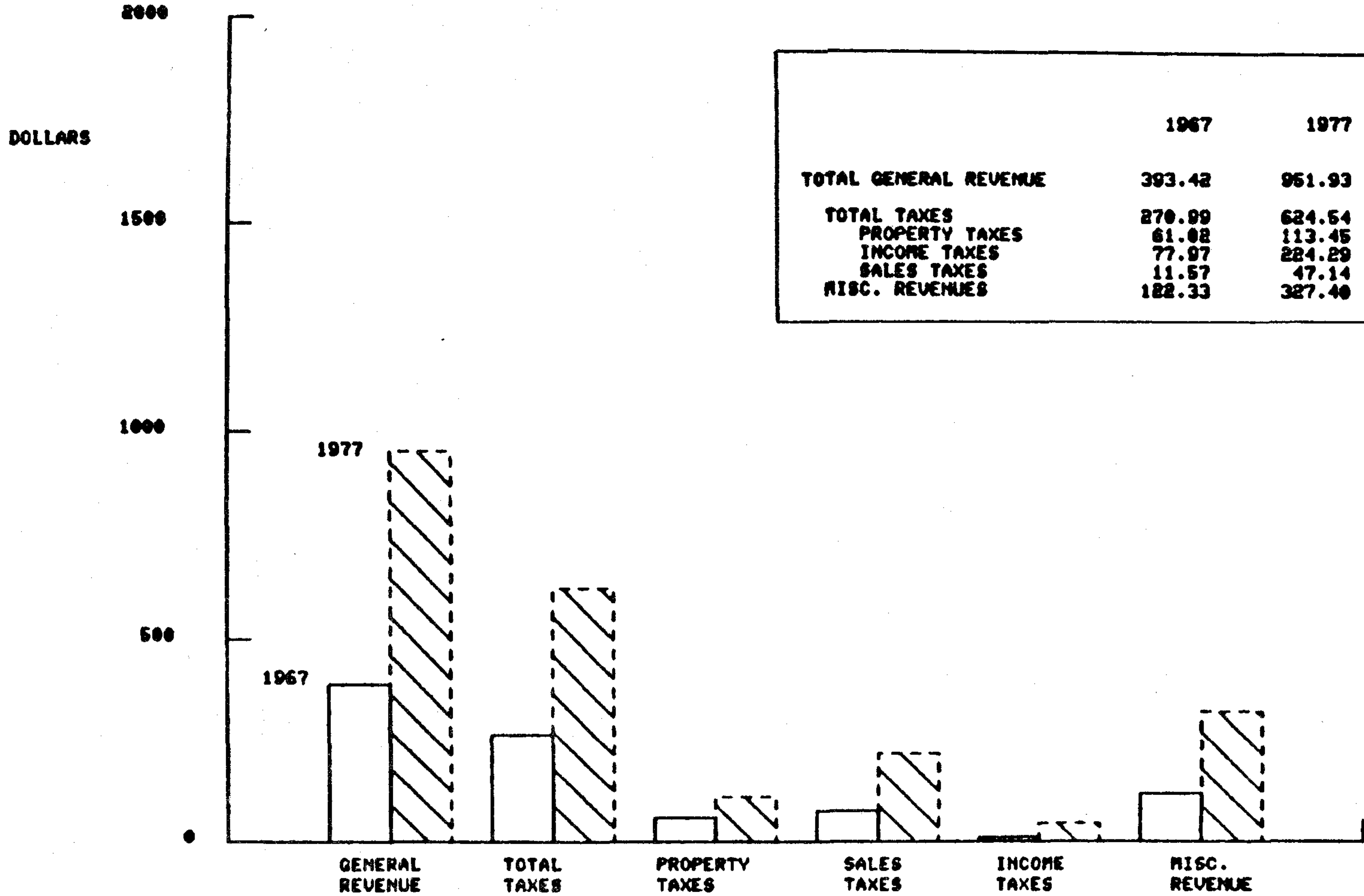
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	502.93	612.15	21.72	1.98
TOTAL TAXES	374.10	448.15	19.79	1.82
PROPERTY TAXES	149.55	143.46	(4.07)	(.42)
INCOME TAXES	52.70	106.64	102.34	7.30
SALES TAXES				
MISC. REVENUES	128.60	164.01	27.53	2.46

PER CAPITA OWN SOURCE REVENUE

STATE AND LOCAL GOVERNMENTS

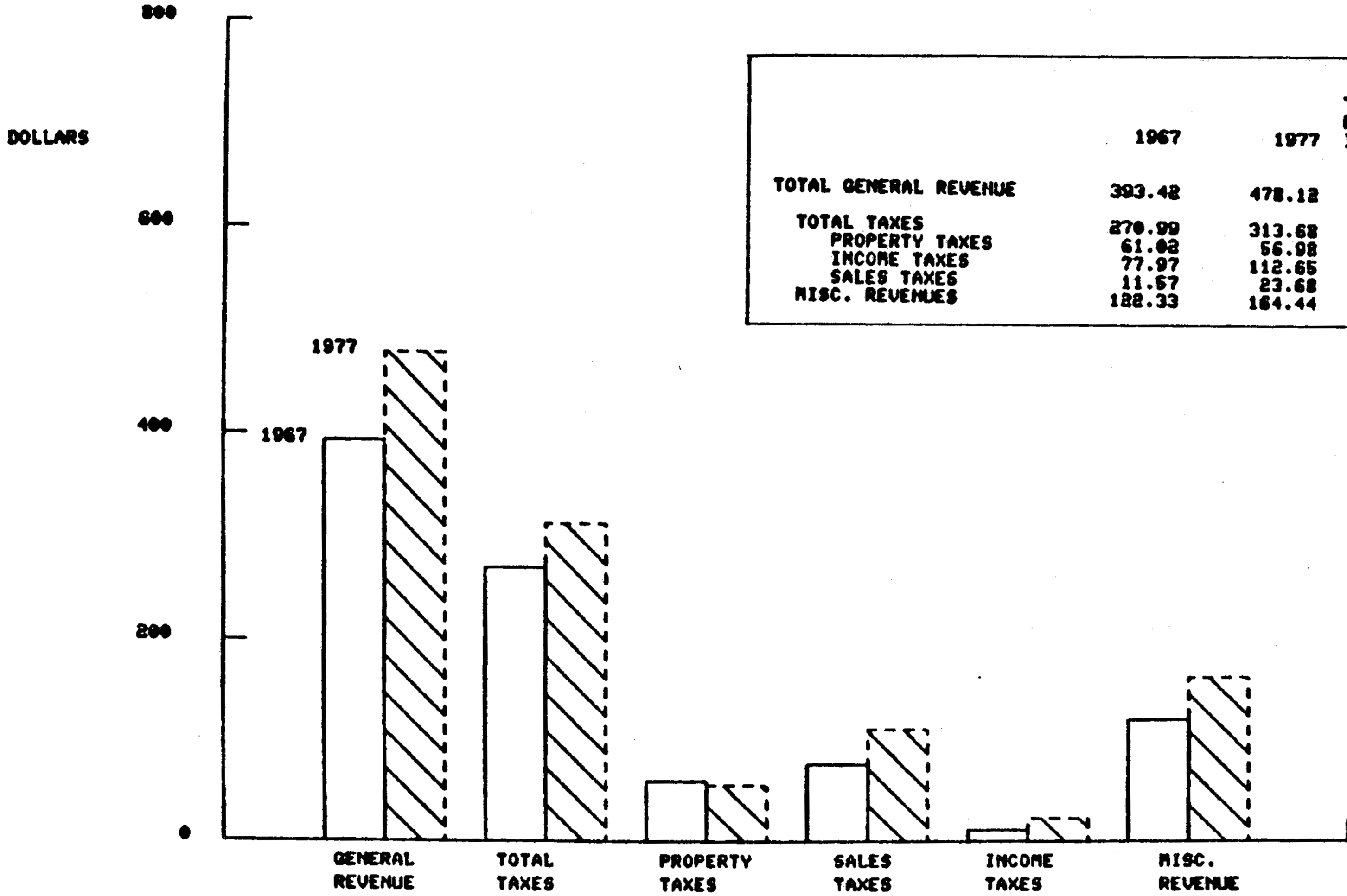
NEW MEXICO 1967 VS. 1977

CURRENT $$



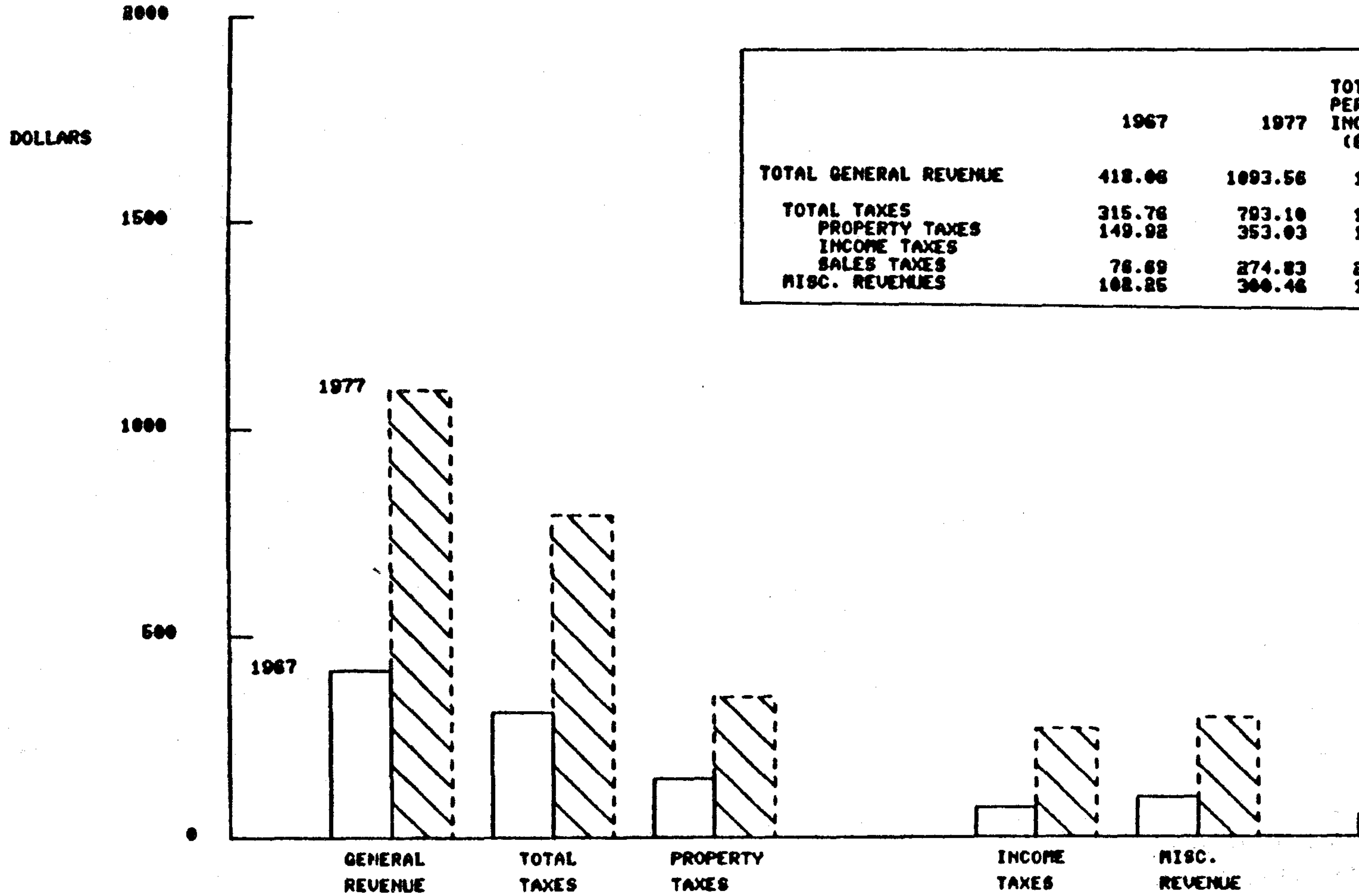
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	393.42	951.93	141.96	9.24
TOTAL TAXES	270.99	624.54	130.47	8.71
PROPERTY TAXES	61.02	113.45	85.92	6.40
INCOME TAXES	77.97	224.29	187.67	11.14
SALES TAXES	11.57	47.14	307.62	15.09
MISC. REVENUES	122.33	327.40	167.63	10.35

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
NEW MEXICO 1967 VS. 1977
CONSTANT 1967 $



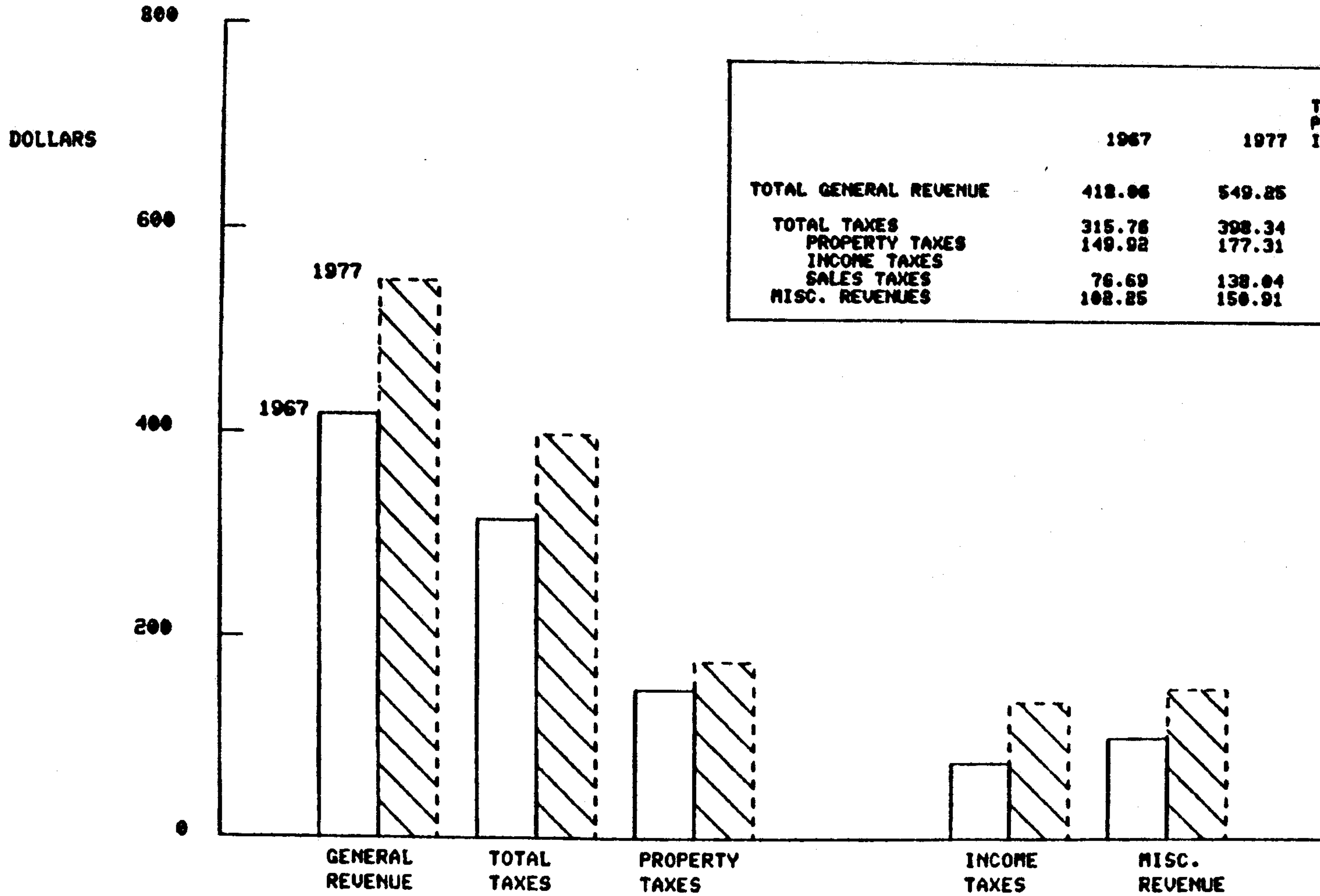
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	393.42	478.12	21.53	1.97
TOTAL TAXES	270.99	313.68	15.75	1.47
PROPERTY TAXES	61.02	56.98	(6.62)	(.68)
INCOME TAXES	77.97	112.65	44.49	3.75
SALES TAXES	11.57	23.68	104.73	7.43
MISC. REVENUES	122.33	164.44	34.42	3.00

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
OREGON 1967 VS. 1977
CURRENT $$



	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	418.08	1093.56	161.58	10.09
TOTAL TAXES	315.78	793.10	151.17	9.65
PROPERTY TAXES	149.92	353.03	135.47	8.94
INCOME TAXES				
SALES TAXES	76.69	274.83	258.37	13.61
MISC. REVENUES	102.25	300.46	193.85	11.38

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
OREGON 1967 VS. 1977
CONSTANT 1967 $



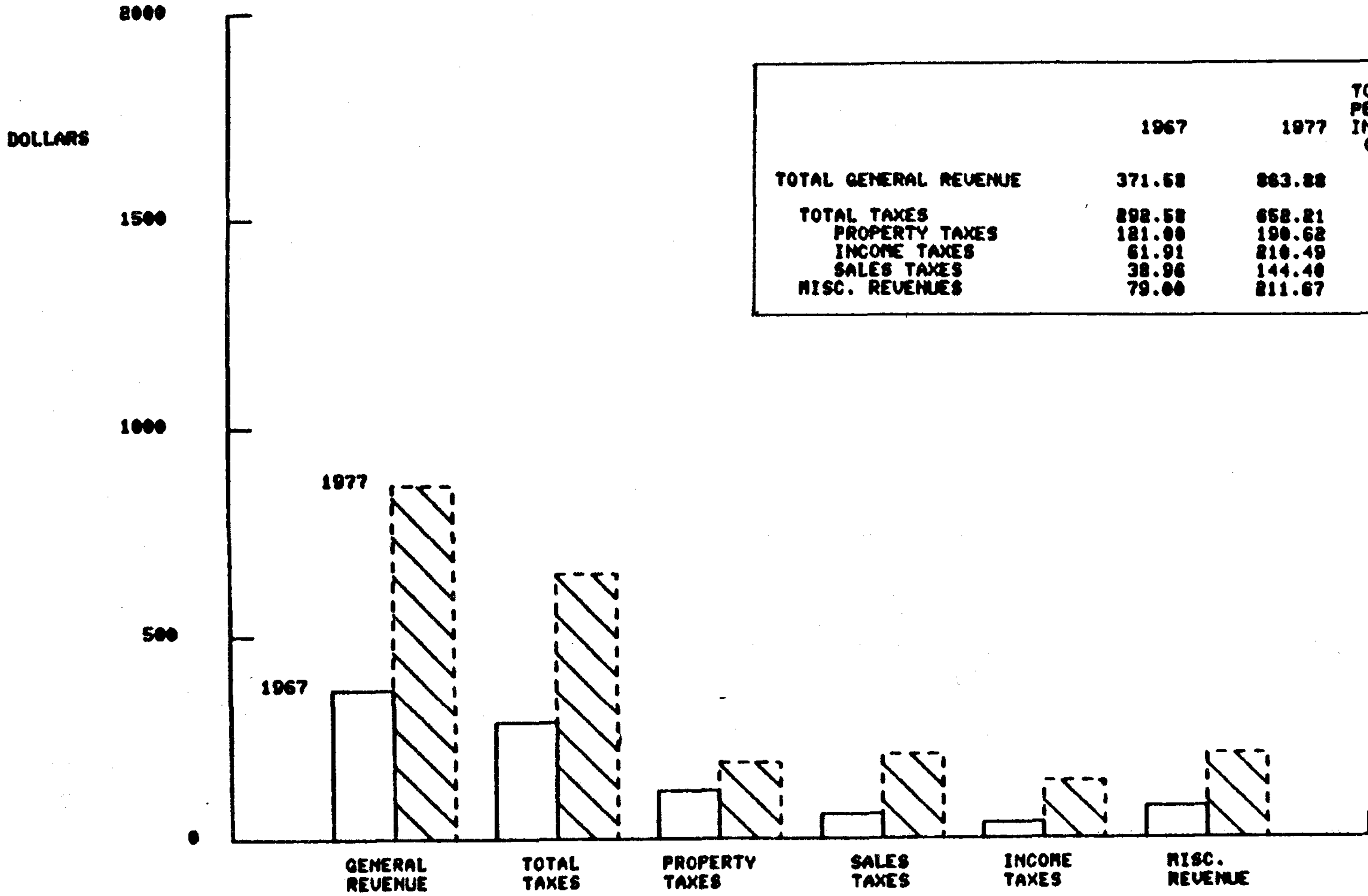
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	418.06	549.25	31.38	2.77
TOTAL TAXES	315.76	398.34	26.15	2.35
PROPERTY TAXES	149.92	177.31	18.27	1.69
INCOME TAXES				
SALES TAXES	76.69	138.04	80.00	6.05
MISC. REVENUES	102.25	150.91	47.59	3.97

PER CAPITA OWN SOURCE REVENUE

STATE AND LOCAL GOVERNMENTS

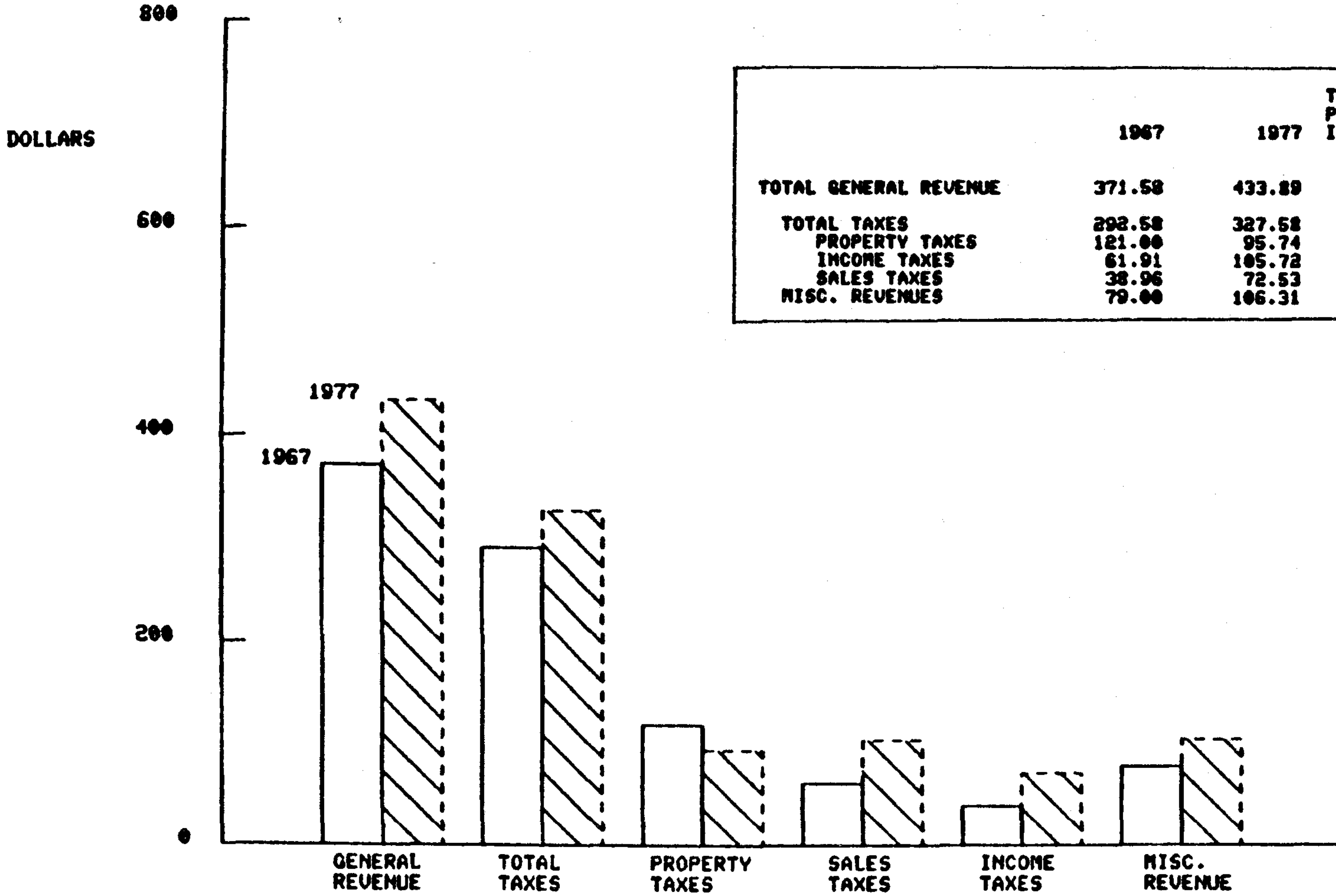
UTAH 1967 VS. 1977

CURRENT $$



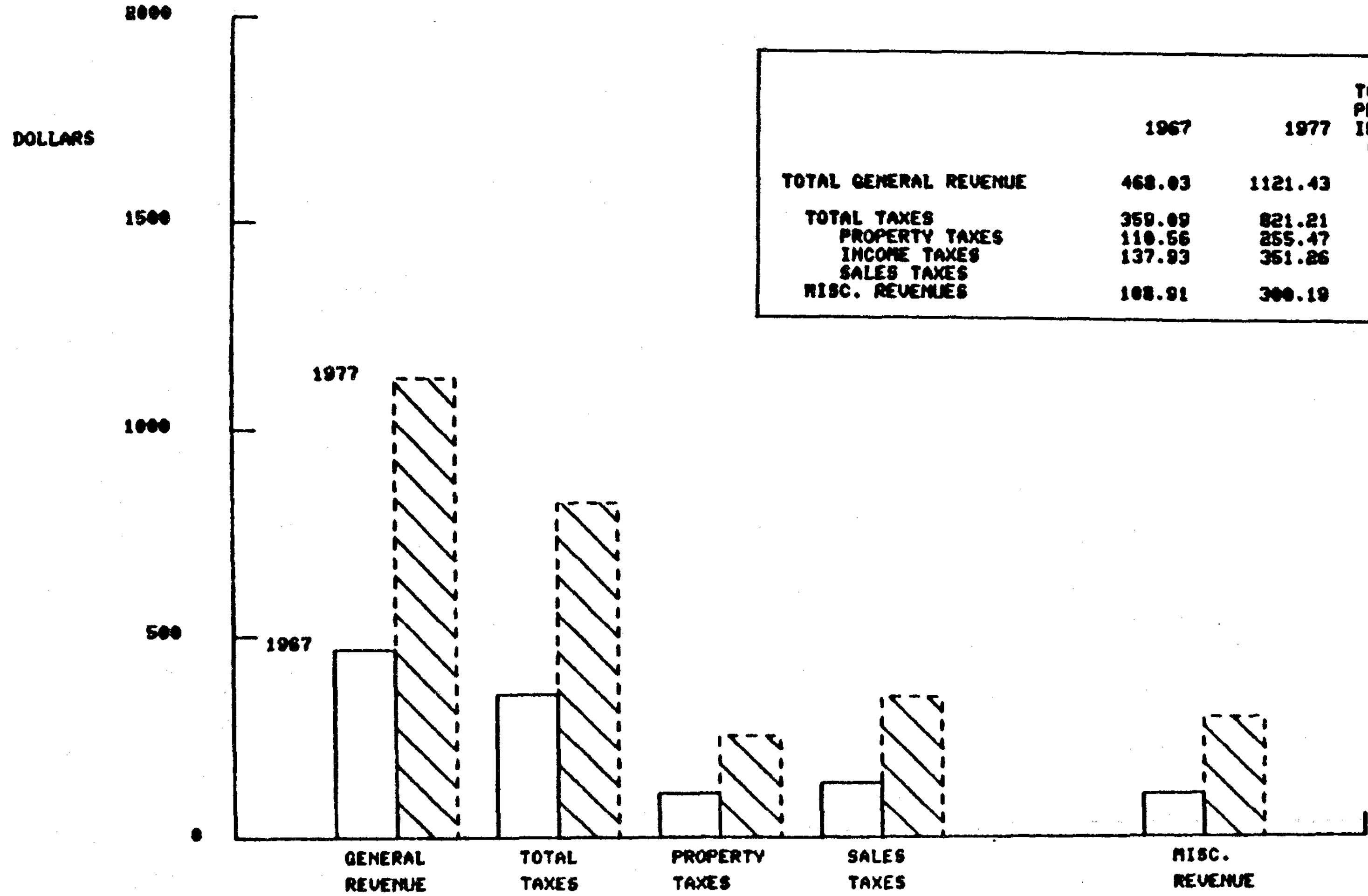
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	371.58	863.88	132.49	8.80
TOTAL TAXES	292.58	652.21	122.98	8.35
PROPERTY TAXES	121.00	190.62	57.54	4.65
INCOME TAXES	61.91	210.49	239.97	13.02
SALES TAXES	38.96	144.40	270.59	14.00
MISC. REVENUES	79.00	211.67	167.93	10.36

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
UTAH 1967 VS. 1977
CONSTANT 1967 $



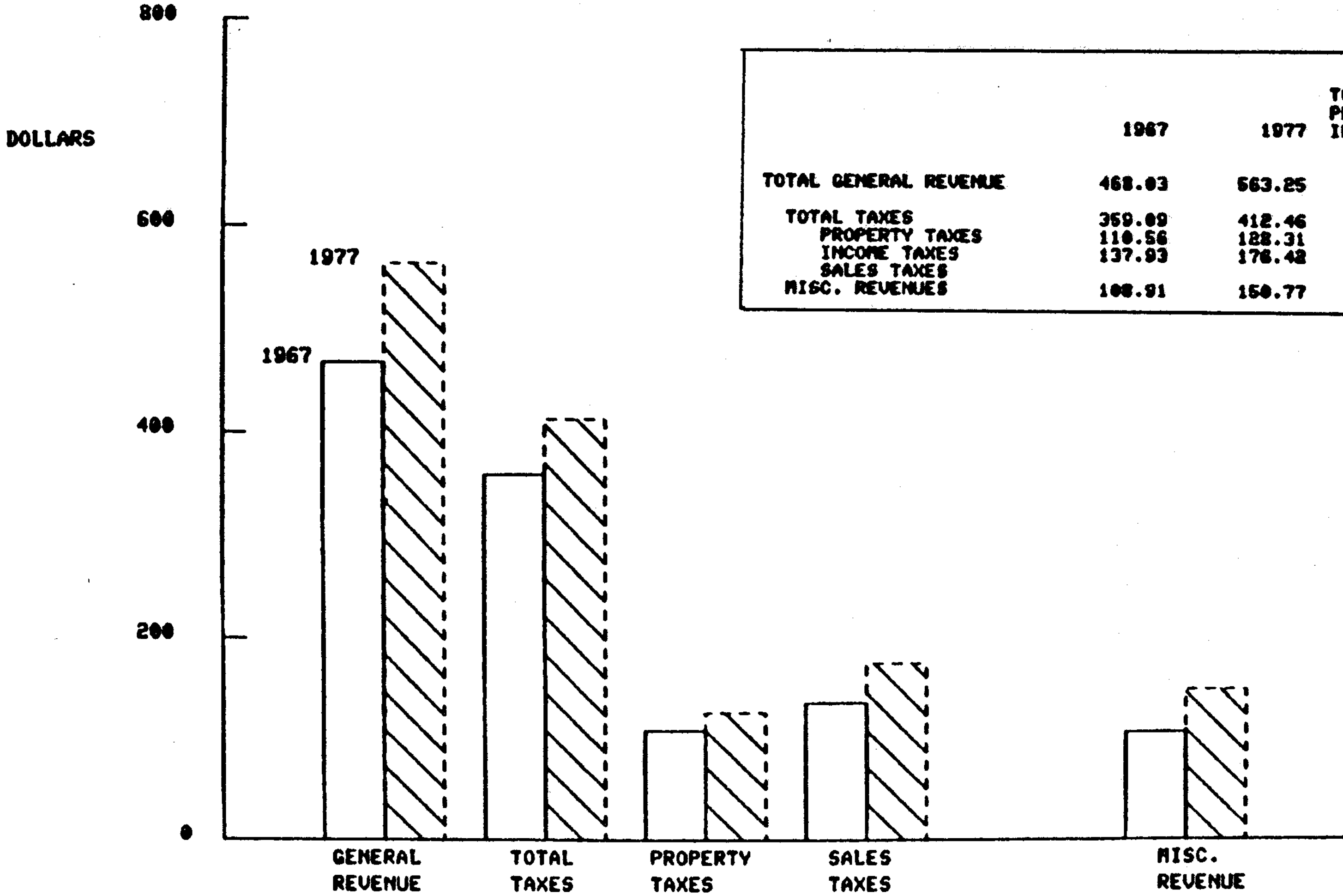
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	371.58	433.89	16.77	1.56
TOTAL TAXES	292.58	327.58	11.96	1.14
PROPERTY TAXES	121.00	95.74	(20.87)	(2.31)
INCOME TAXES	61.91	105.72	70.75	5.50
SALES TAXES	38.96	72.53	86.13	6.41
MISC. REVENUES	79.00	106.31	34.57	3.01

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
WASHINGTON 1967 VS. 1977
CURRENT $S



	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	468.03	1121.43	139.61	9.13
TOTAL TAXES	359.09	821.21	128.70	8.62
PROPERTY TAXES	110.56	255.47	131.07	8.74
INCOME TAXES	137.93	351.26	154.66	9.80
SALES TAXES				
MISC. REVENUES	108.91	300.19	175.64	10.67

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
WASHINGTON 1967 VS. 1977
CONSTANT 1967 $



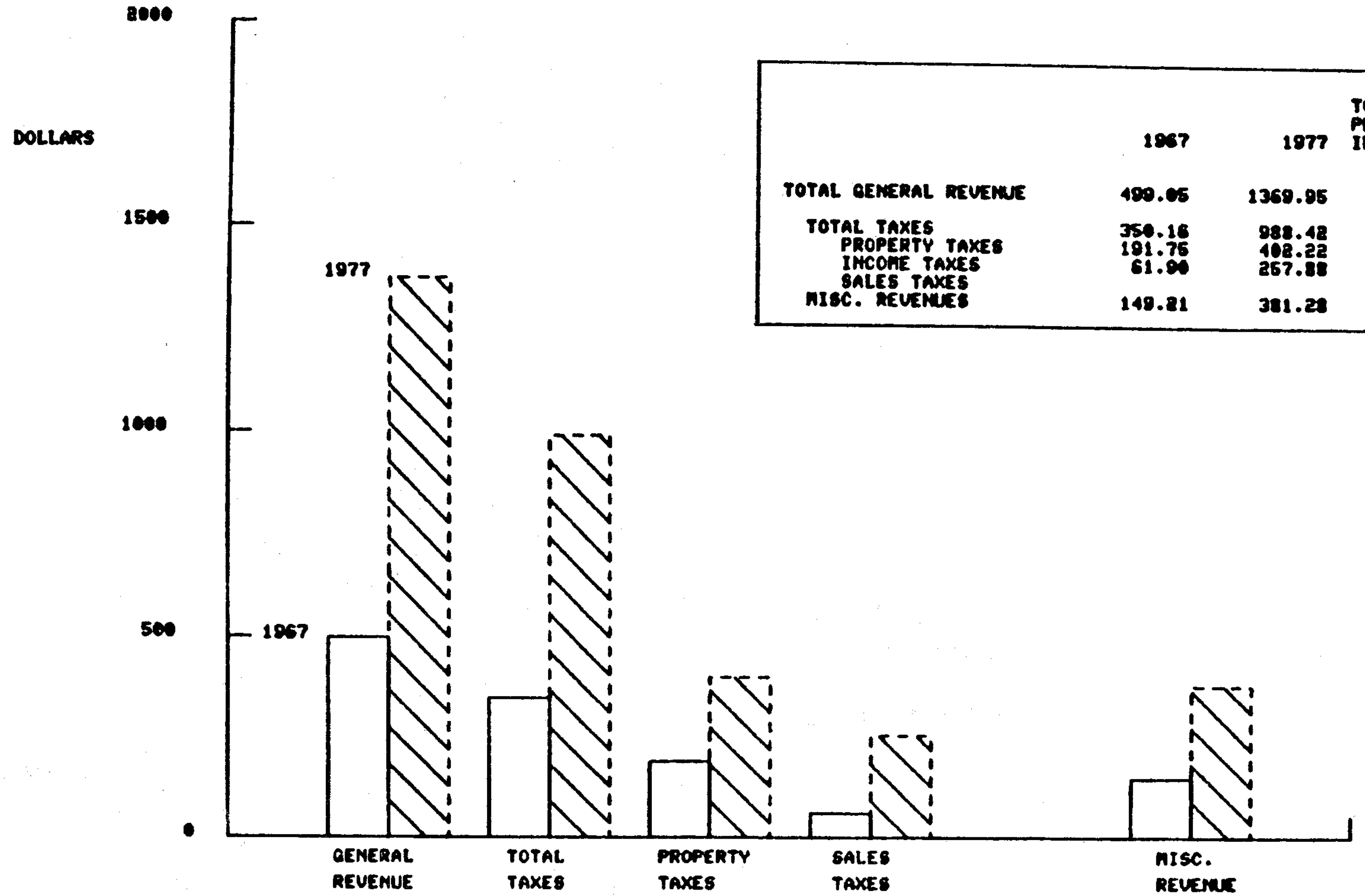
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	468.03	563.25	20.35	1.87
TOTAL TAXES	359.09	412.46	14.88	1.40
PROPERTY TAXES	110.56	128.31	16.06	1.50
INCOME TAXES	137.93	176.42	27.90	2.49
SALES TAXES				
MISC. REVENUES	108.91	150.77	38.44	3.31

PER CAPITA OWN SOURCE REVENUE

STATE AND LOCAL GOVERNMENTS

WYOMING 1967 VS. 1977

CURRENT $$



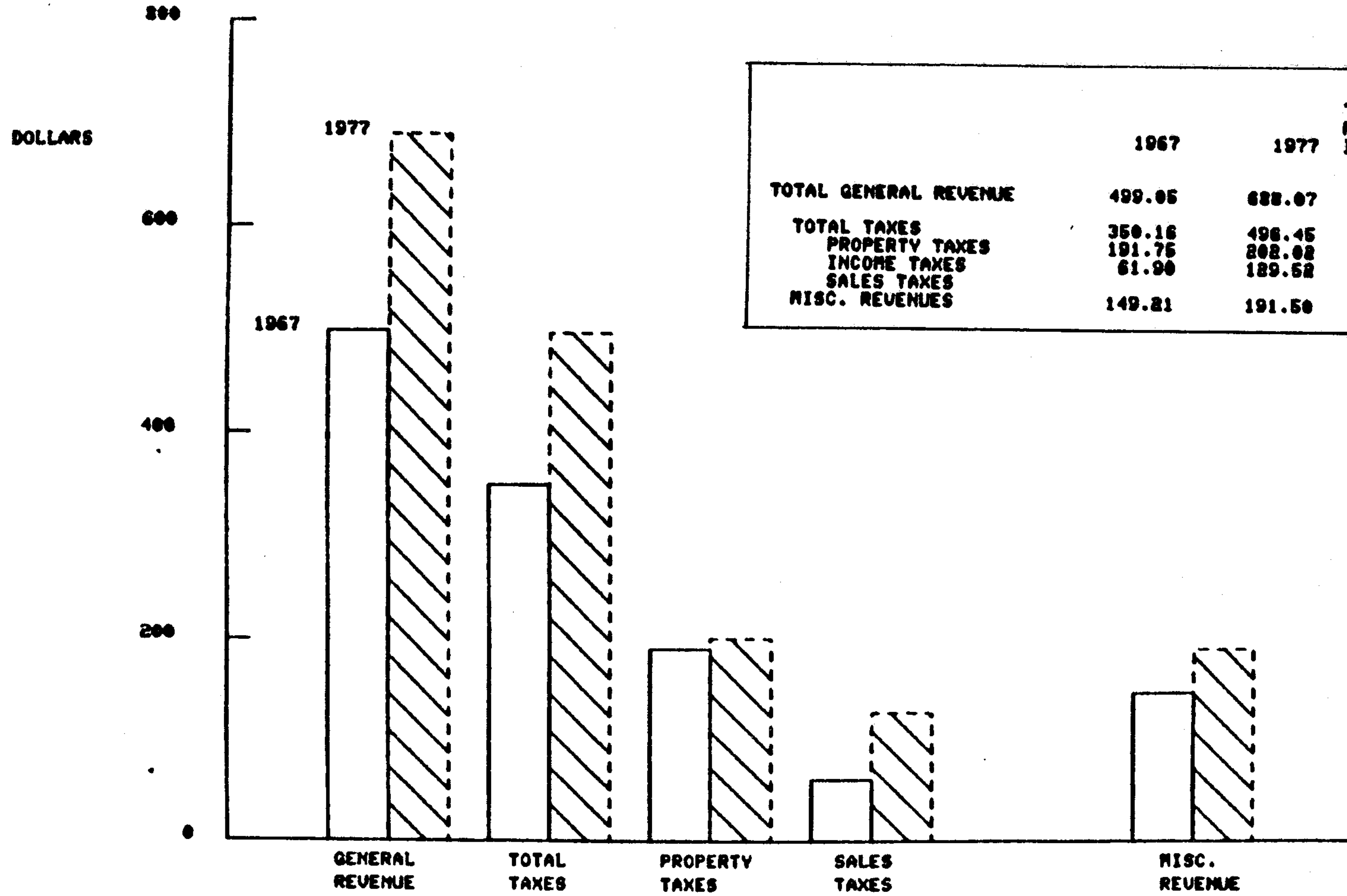
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	499.05	1369.95	174.51	10.63
TOTAL TAXES	350.16	988.42	182.28	10.93
PROPERTY TAXES	191.76	402.22	109.77	7.69
INCOME TAXES	61.90	257.88	316.58	15.34
SALES TAXES				
MISC. REVENUES	149.21	381.28	155.54	9.84

PER CAPITA OWN SOURCE REVENUE

STATE AND LOCAL GOVERNMENTS

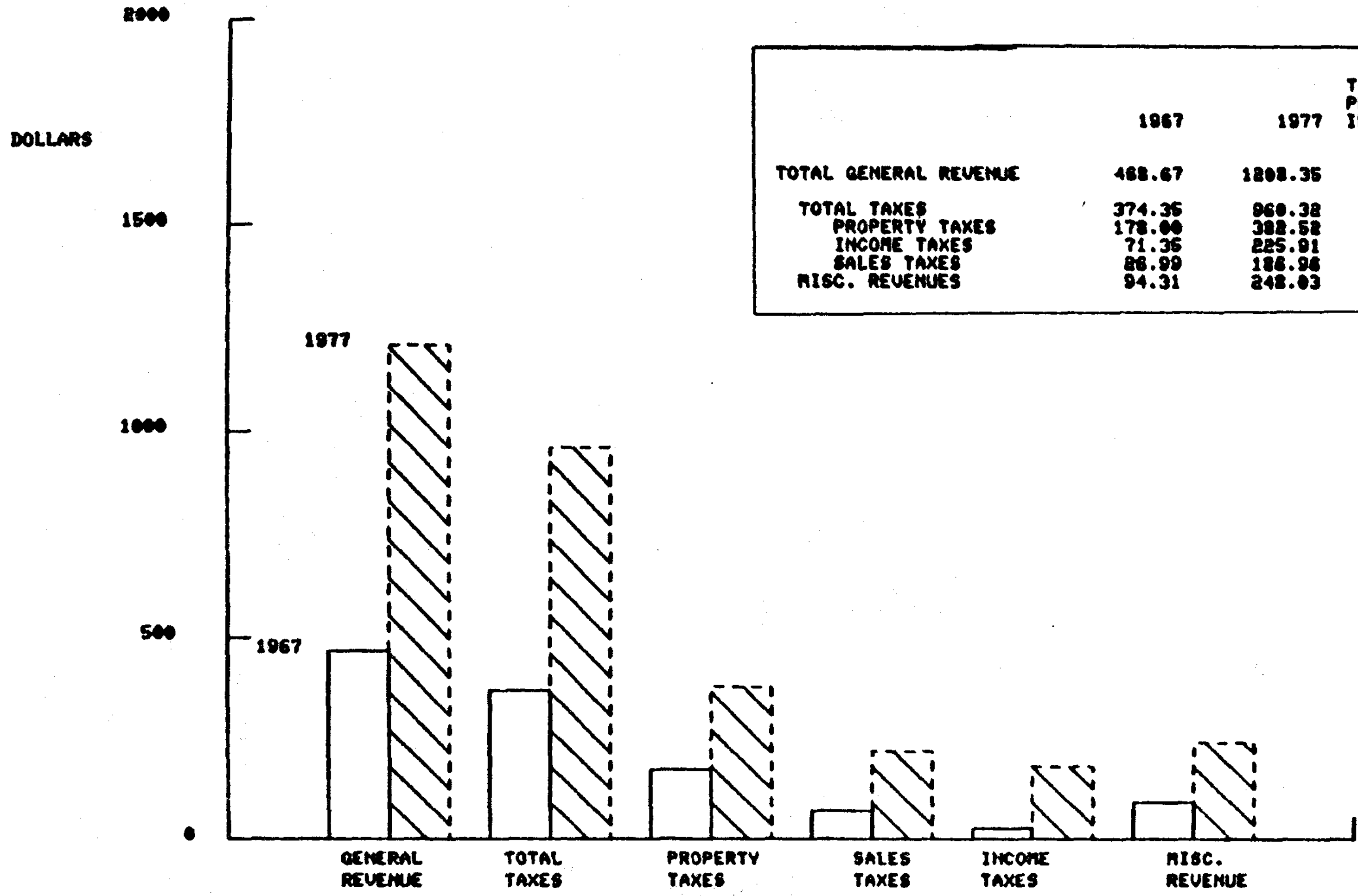
WYOMING 1967 VS. 1977

CONSTANT 1967 $



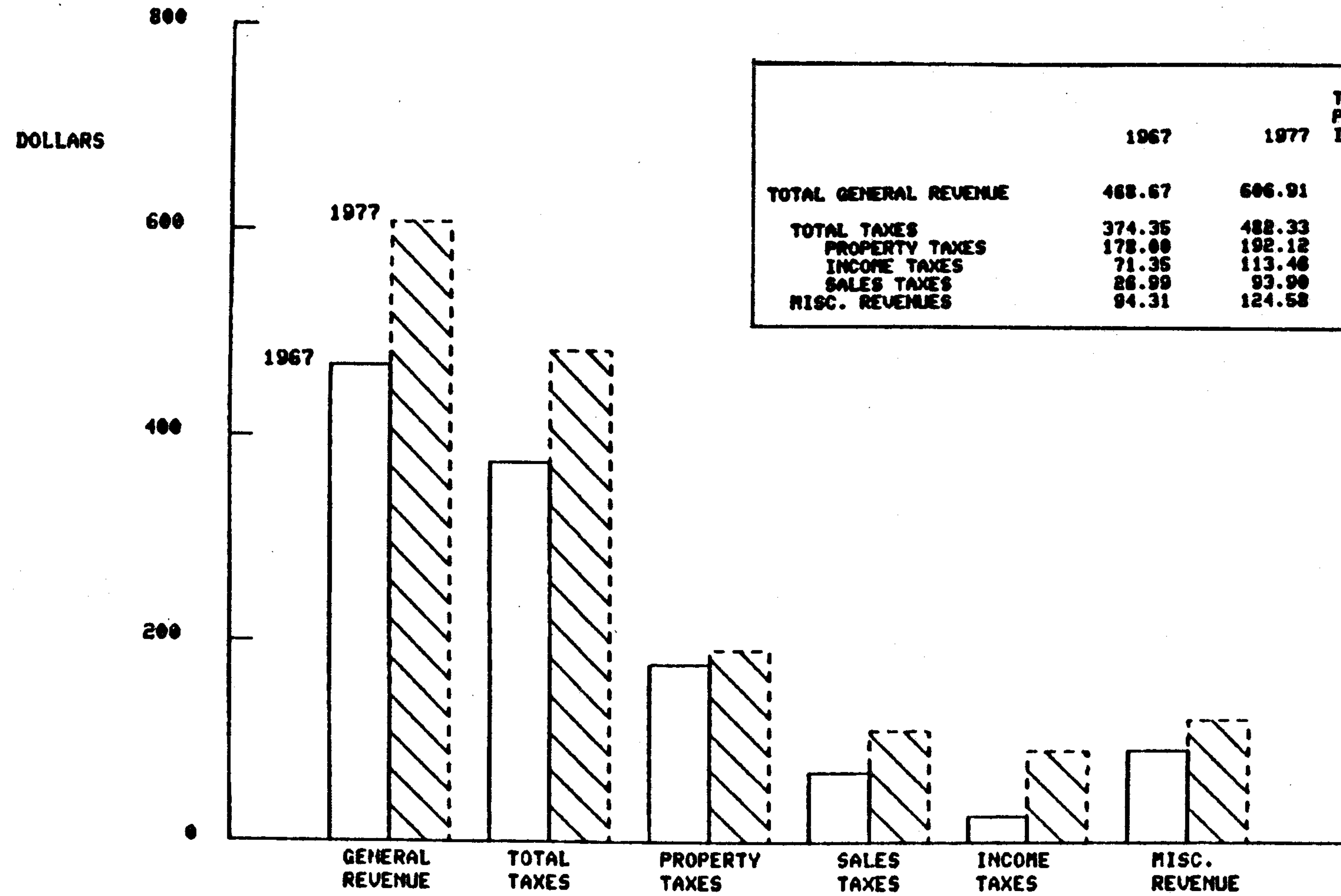
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	499.05	688.07	37.88	3.26
TOTAL TAXES	350.16	496.45	41.78	3.55
PROPERTY TAXES	191.75	202.02	5.36	.52
INCOME TAXES				
SALES TAXES	61.90	129.52	109.23	7.66
MISC. REVENUES	149.21	191.50	28.35	2.53

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
WESTERN STATES 1967 VS. 1977
CURRENT $S



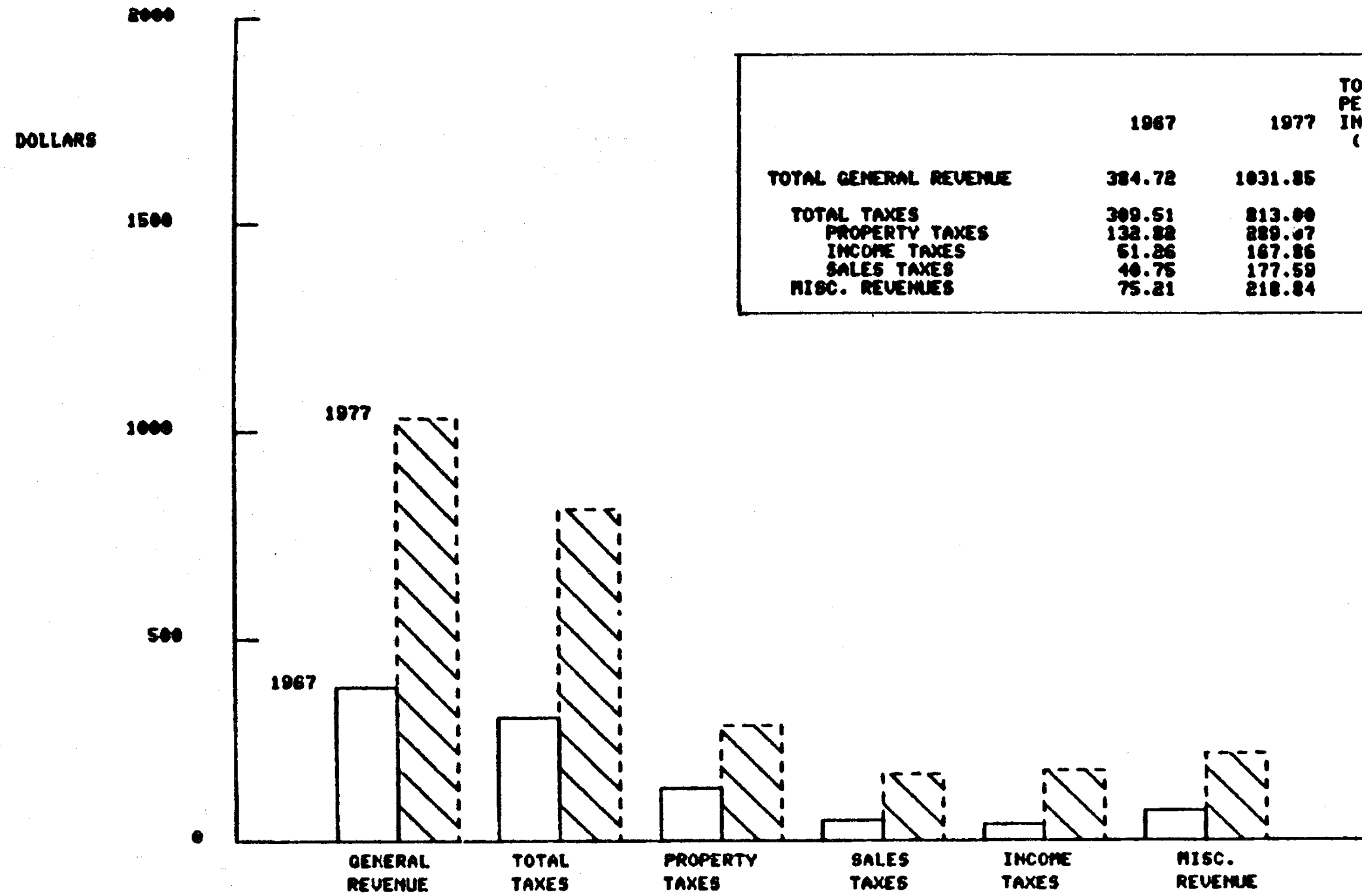
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	468.67	1208.35	157.83	9.93
TOTAL TAXES	374.35	960.38	156.53	9.88
PROPERTY TAXES	178.00	382.52	114.90	7.95
INCOME TAXES	71.36	225.91	216.64	12.22
SALES TAXES	26.99	186.96	592.69	21.35
MISC. REVENUES	94.31	248.03	163.00	10.15

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
WESTERN STATES 1967 VS. 1977
CONSTANT 1967 $



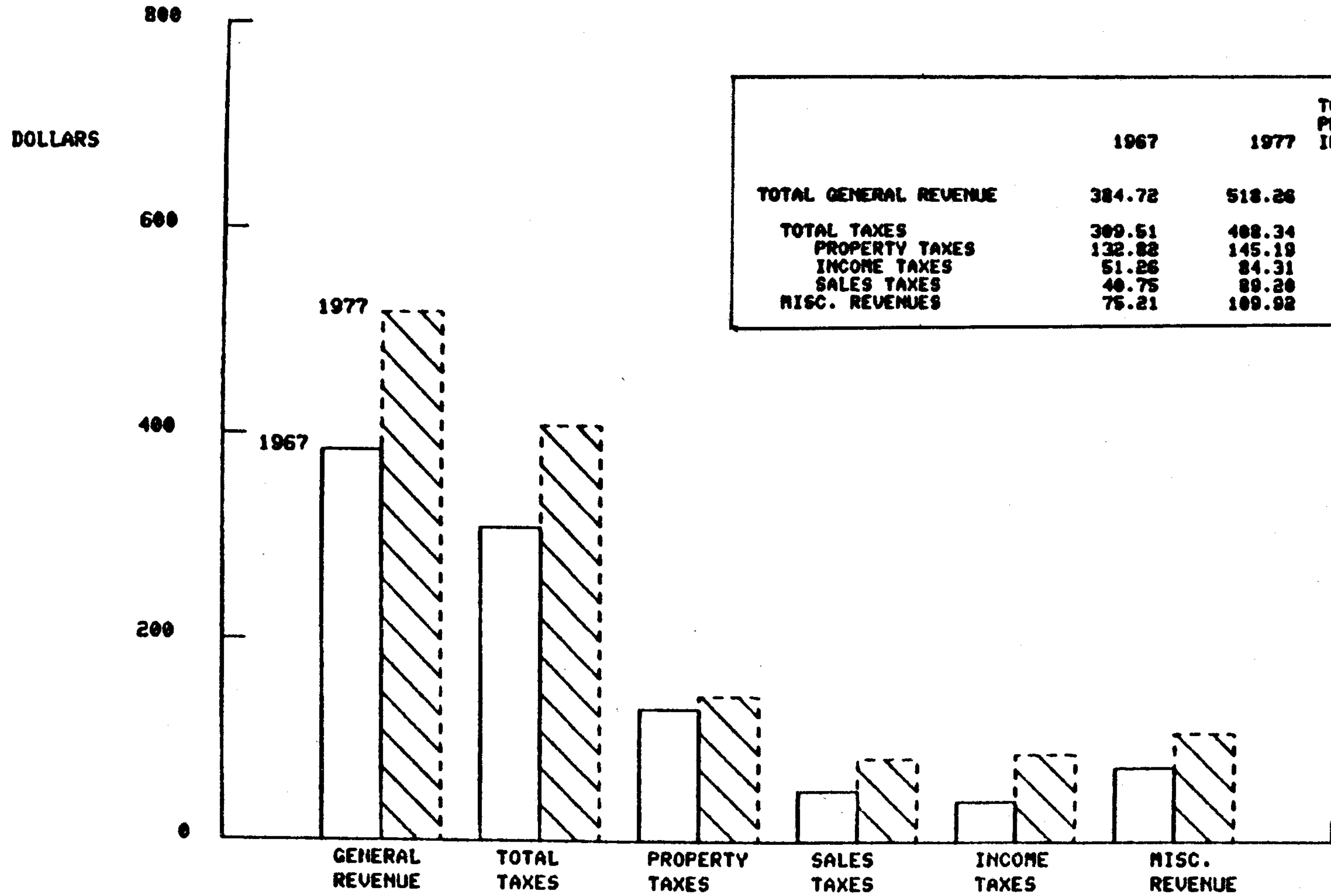
	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	468.67	606.91	29.50	2.62
TOTAL TAXES	374.35	482.33	28.84	2.57
PROPERTY TAXES	178.00	192.12	7.94	.77
INCOME TAXES	71.35	113.46	59.03	4.75
SALES TAXES	26.99	93.90	247.91	13.28
MISC. REVENUES	94.31	124.58	32.10	2.82

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
UNITED STATES 1967 VS. 1977
CURRENT $$



	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	384.72	1031.85	168.21	10.37
TOTAL TAXES	309.51	813.00	162.67	10.14
PROPERTY TAXES	132.82	289.07	117.64	8.09
INCOME TAXES	51.26	167.86	227.44	12.59
SALES TAXES	40.75	177.59	335.86	15.86
MISC. REVENUES	75.21	218.84	190.98	11.27

PER CAPITA OWN SOURCE REVENUE
STATE AND LOCAL GOVERNMENTS
UNITED STATES 1967 VS. 1977
CONSTANT 1967 $



	1967	1977	TOTAL PERCENT INCREASE (67-77)	AVERAGE ANNUAL PERCENT INCREASE
TOTAL GENERAL REVENUE	384.72	518.26	34.71	3.02
TOTAL TAXES	309.51	408.34	31.93	2.81
PROPERTY TAXES	132.82	145.19	9.31	.89
INCOME TAXES	51.26	84.31	64.46	5.10
SALES TAXES	40.75	89.20	118.91	8.15
MISC. REVENUES	75.21	109.92	46.15	3.87

APPENDIX III-2

TAX RELIANCE OF OWN SOURCE GENERAL REVENUE IN 1977: STATE AND LOCAL GOVERNMENTS

WESTERN STATES

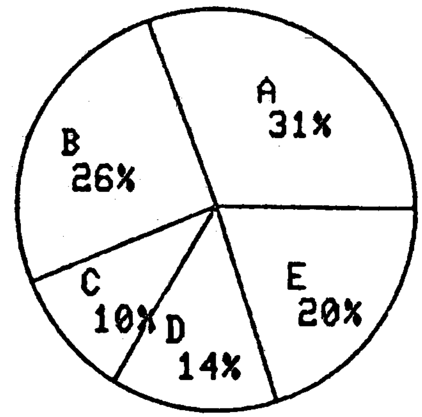
TAX REVENUE BY SOURCES 1977

ARIZONA

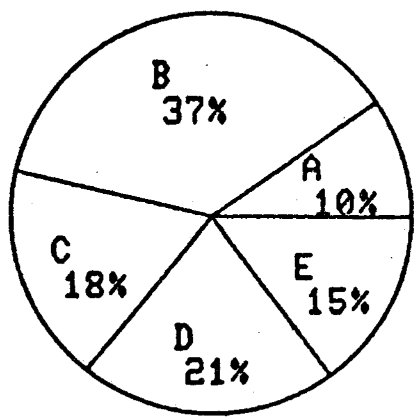
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $2372.90 MILLION
STATE OWN SOURCE GENERAL REVENUE = $1364.10 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $1008.80 MILLION

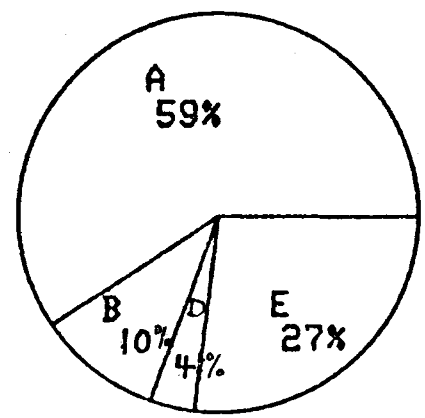
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

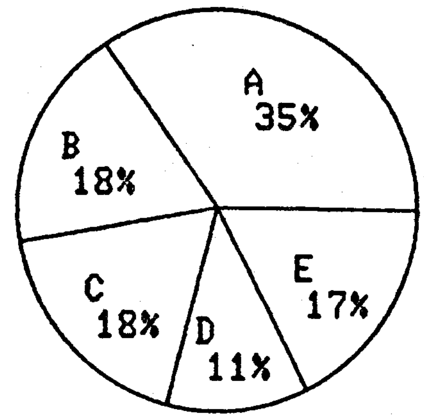


TAX REVENUE BY SOURCES 1977
CALIFORNIA

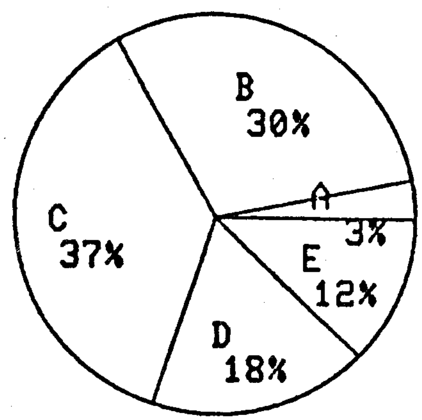
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $28898.40 MILLION
STATE OWN SOURCE GENERAL REVENUE = $14343.20 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $14555.20 MILLION

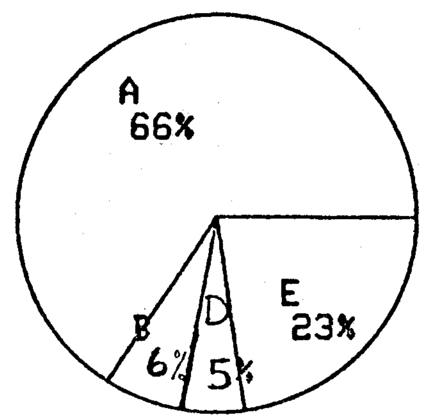
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

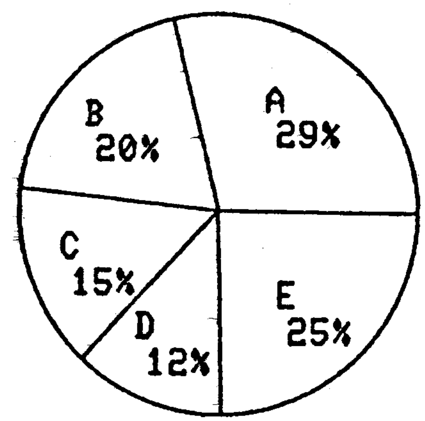


TAX REVENUE BY SOURCES 1977
COLORADO

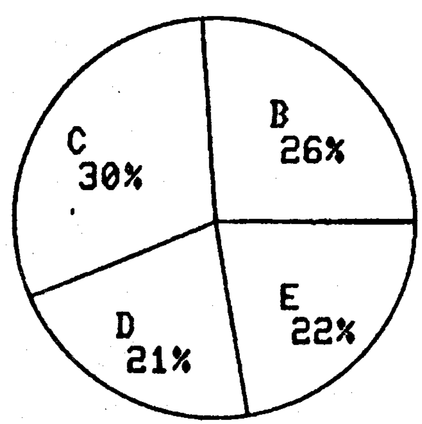
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $2863.70 MILLION
STATE OWN SOURCE GENERAL REVENUE = $1388.80 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $1474.90 MILLION

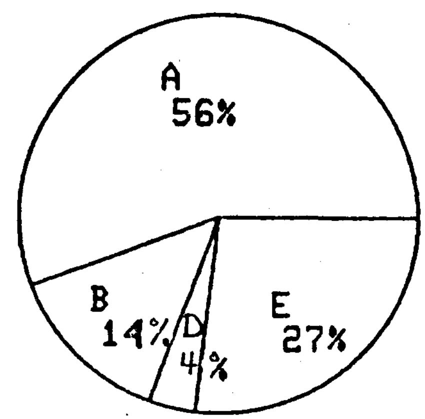
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

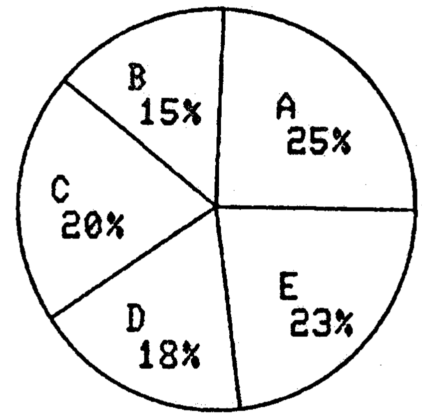


TAX REVENUE BY SOURCES 1977
IDAHO

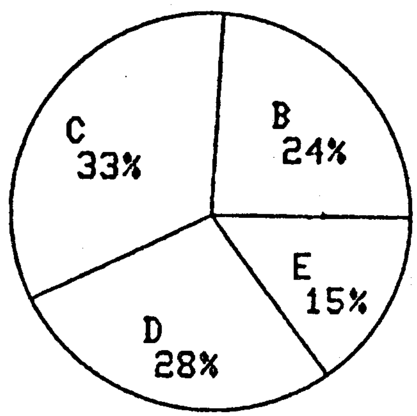
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $711.70 MILLION
STATE OWN SOURCE GENERAL REVENUE = $433.10 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $278.60 MILLION

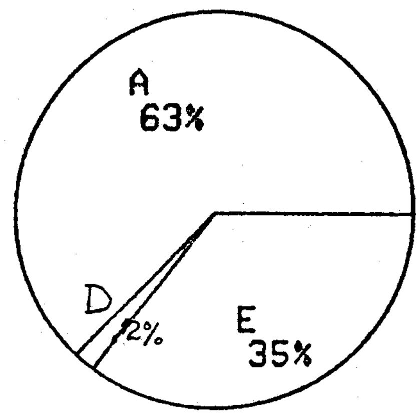
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

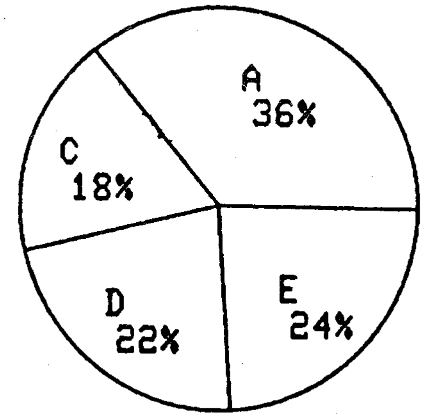


TAX REVENUES BY SOURCES 1977
MONTANA

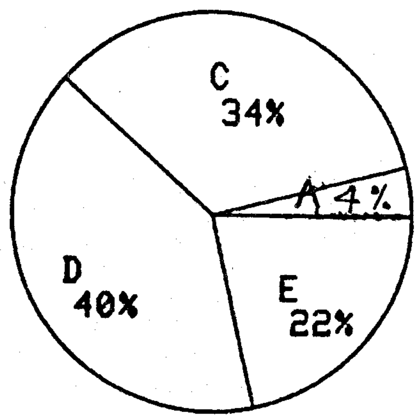
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $765.90 MILLION
STATE OWN SOURCE GENERAL REVENUE = $399.00 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $366.90 MILLION

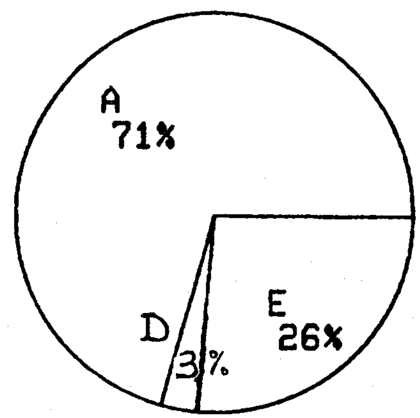
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

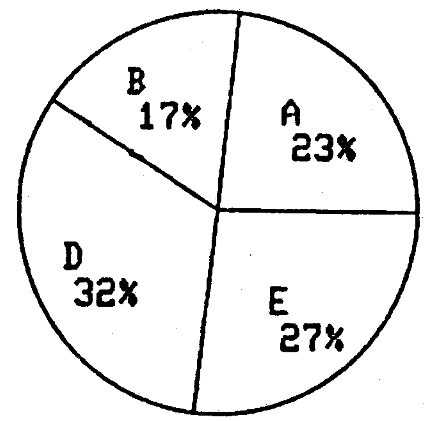


TAX REVENUES BY SOURCES 1977
NEVADA

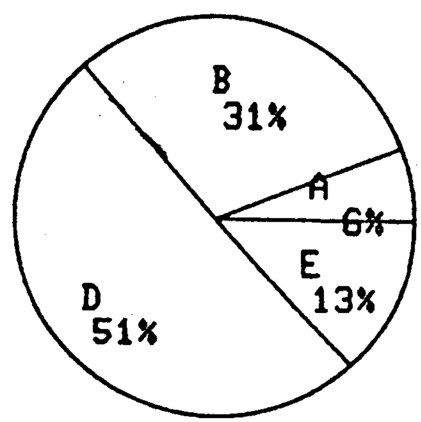
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $771.50 MILLION
STATE OWN SOURCE GENERAL REVENUE = $378.60 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $392.90 MILLION

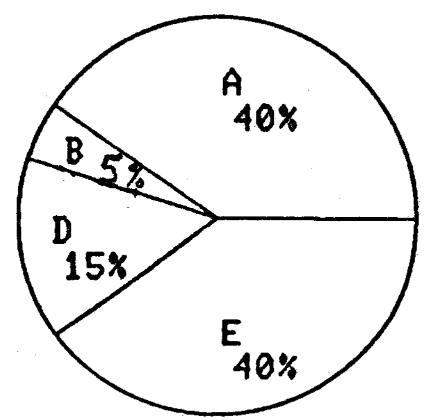
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE



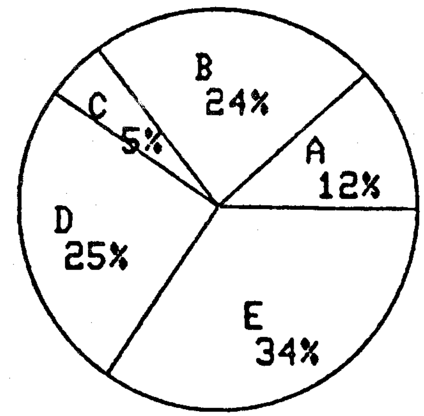
TAX REVENUE BY SOURCES 1977

NEW MEXICO

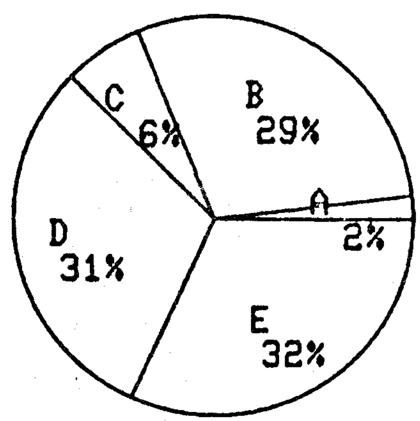
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $1132.80 MILLION
STATE OWN SOURCE GENERAL REVENUE = $877.60 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $255.20 MILLION

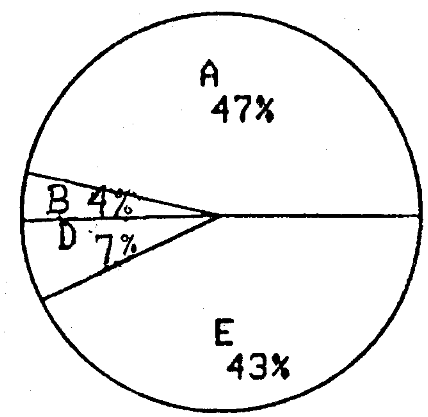
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

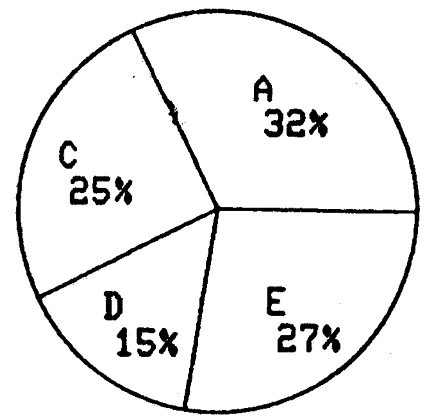


TAX REVENUE BY SOURCES 1977
OREGON

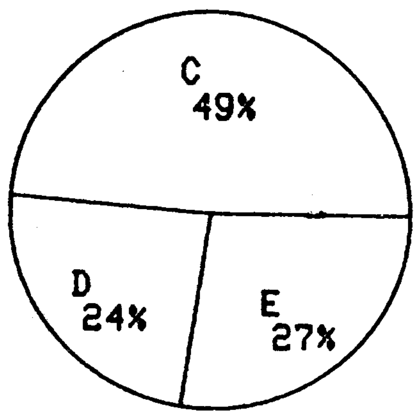
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $2598.30 MILLION
STATE OWN SOURCE GENERAL REVENUE = $1340.30 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $1258.00 MILLION

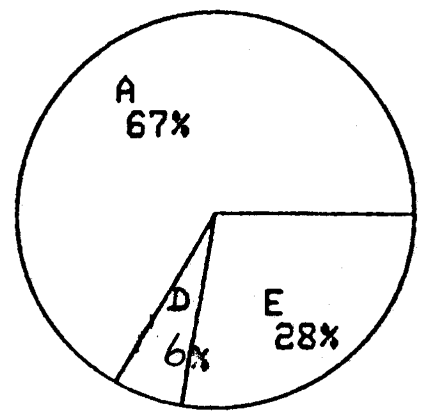
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

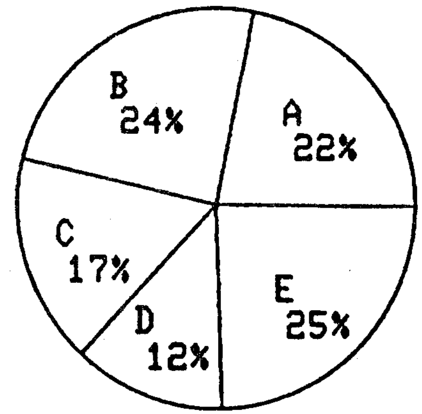


TAX REVENUE BY SOURCES 1977
UTAH

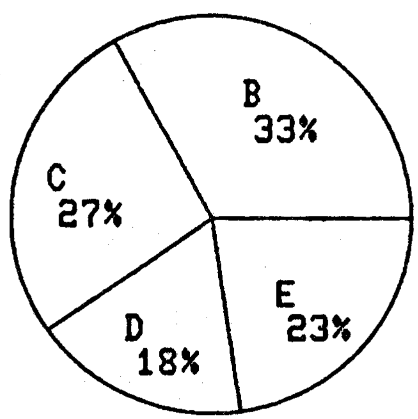
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $1095.4 MILLION
STATE OWN SOURCE GENERAL REVENUE = $688.20 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $407.20 MILLION

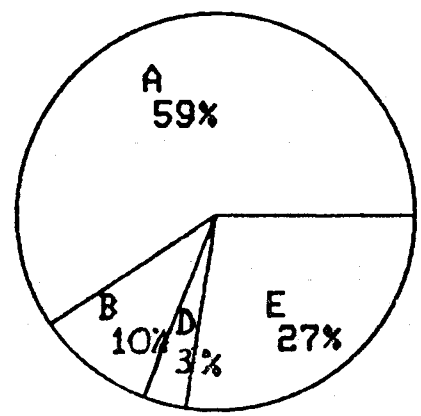
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

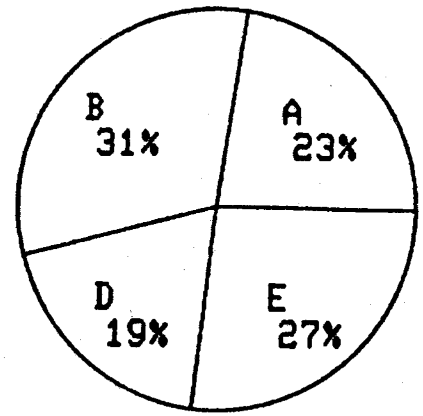


TAX REVENUE BY SOURCES 1977
WASHINGTON

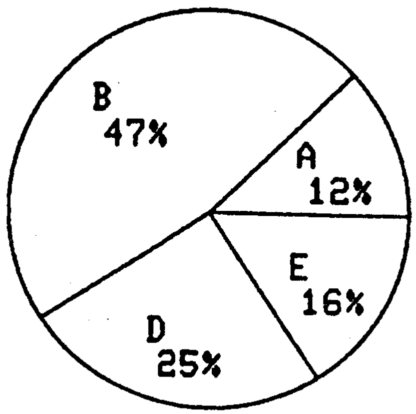
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $4102.20 MILLION
STATE OWN SOURCE GENERAL REVENUE = $2492.70 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $1609.50 MILLION

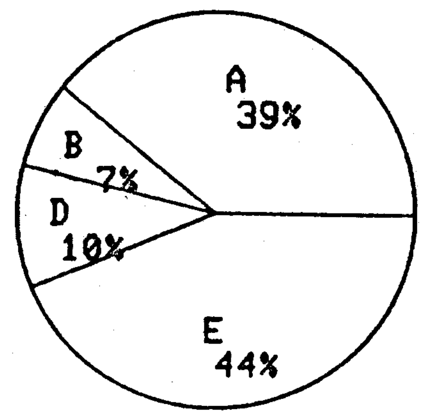
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

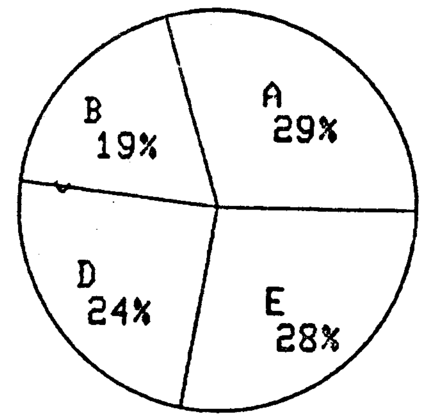


TAX REVENUE BY SOURCES 1977
WYOMING

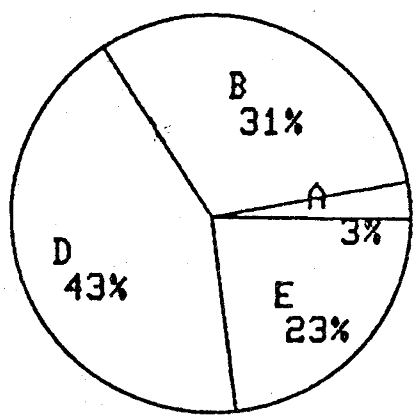
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $555.20 MILLION
STATE OWN SOURCE GENERAL REVENUE = $303.20 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $253.00 MILLION

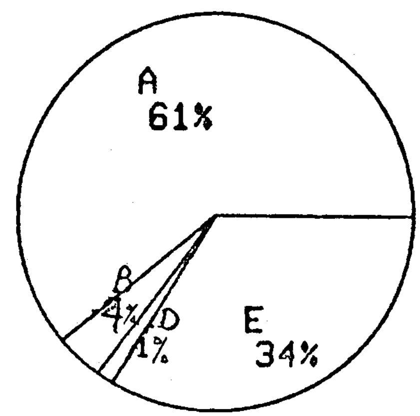
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

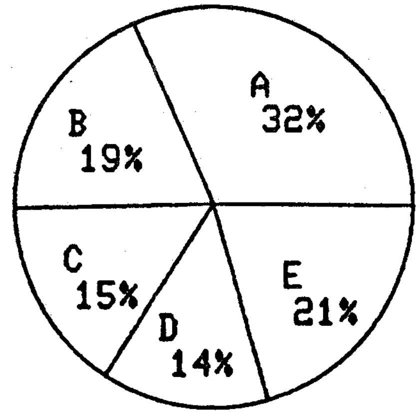


TAX REVENUE BY SOURCES 1977
WESTERN STATES

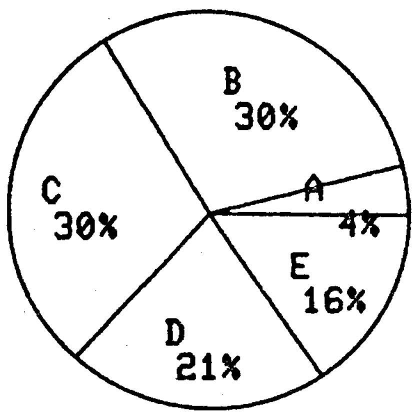
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $45869.00 MILLION
STATE OWN SOURCE GENERAL REVENUE = $24008.80 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $21860.20 MILLION

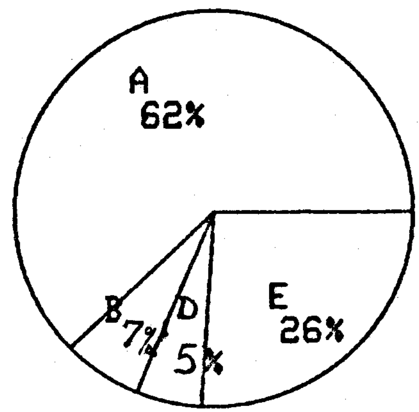
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE

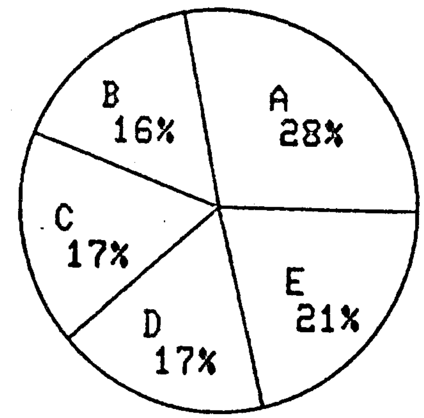


TAX REVENUE BY SOURCES 1977
UNITED STATES

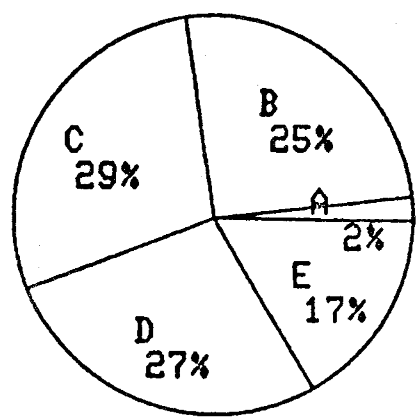
A = PROPERTY TAXES
B = SALES TAXES
C = INCOME TAXES
D = OTHER TAXES
E = MISC. REVENUE

TOTAL OWN SOURCE GENERAL REVENUE = $223221.3 MILLION
STATE OWN SOURCE GENERAL REVENUE = $121199.6 MILLION
LOCAL OWN SOURCE GENERAL REVENUE = $102039.7 MILLION

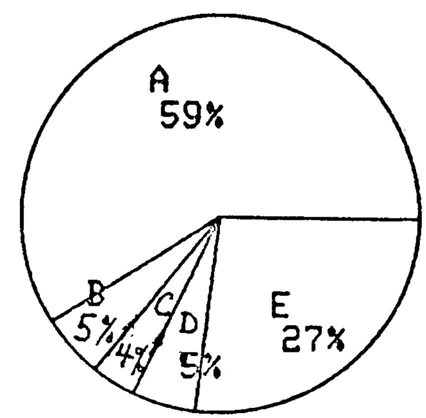
STATE AND LOCAL GOVERNMENT REVENUE



STATE GOVERNMENT REVENUE



LOCAL GOVERNMENT REVENUE



SECTION FOUR

PROPERTY TAX

In this section, the Arizona property tax will be described and examined with respect to the following characteristics:

- administration
- incidence
- collections and distribution
- comparison with evaluative criteria

A. Description

1. Property Tax Base

a. Current Base. The property tax is levied on the assessed valuation of properties within the state. Assessed valuation is equal to a percentage of the full cash value of all land, improvements and personal property, both secured and unsecured. The full cash value of property is the market value of the property as appraised by the County Assessor or Department of Revenue. Secured property is personal property affixed to the land such as buildings, while unsecured property is generally equipment or movable personal property.

For any parcel of property, the percent of full cash value which is subject to taxation will depend on the classification of the property. The property tax base in Arizona is unique in that it is defined by several classes of property, each with a separate assessment rate. The assessment rate defines the percent of full cash value which is subject to taxation.

Classification allows the state to treat the several types of property differently for taxation, thereby influencing the proportion of taxes paid by each class of property. To date, only eight states, including Arizona, have adopted comprehensive classified tax systems. Eighteen other states have implemented partial classification schemes.

In Arizona, there are eight classifications of property for taxation as shown below:

PROPERTY CLASSIFICATIONS FOR TAXATION

Class	Assessment Ratio	Property Types
1	60%	flight property; private car company property, railroads, producing mines and timber
2	50%	telephone and telegraph company property; gas, water, and electric company property; pipeline company property
3	27%	commercial and industrial property
4	18%	agricultural property
5	15%	residential property; non-profit handicapped or elderly care facilities
6	23%*	rental residential property
7	8%	historic property
C**	100%	producing oil and gas company property

b. Exemptions. Exemptions reduce the amount of taxable valuation, thereby reducing tax liability. Exemptions are usually given for one of the following reasons:

- For social purposes - for religious, charitable or educational institutions
- As rewards for services rendered to the public - veterans exemptions
- To eliminate hard-to-tax property - intangible personal property
- To refrain from taxing property that is immune to taxation - government property
- To provide incentives - exemptions for certain industries or new industries
- To redistribute the wealth - exemptions for the aged and low income.

In addition to the general exemptions listed above, the Arizona Constitution provides for property tax exemptions for widows and veterans:

*The assessment ratio for class 6 properties is 23% for 1978 and 21% for 1979.

**The full cash value of producing oil and gas wells in any year is equal to the value of the gross receipts of production in the preceding year.

Widows exemption:

The first $2,000 of assessed valuation is exempt from the property tax if total assessed valuation does not exceed $5,000, and total income is no more than $3,500, or $5,000 if children reside in the home.

Veterans exemption:

The first $2,000 of assessed valuation is exempt from the property tax if total assessed valuation does not exceed $5,000. To qualify for this exemption, the veteran must have been honorably discharged, served at least 60 days during time of war, and have been an Arizona resident prior to September 1, 1945.

In 1978, approximately $33.3 million of assessed valuation in residential property was exempted under these provisions.

c. Historic Development of the Base.* Historically, the appraisal of property was a very arbitrary process and dependent upon the discretion of the local appraiser. Prior to statehood in Arizona, the county sheriff was authorized as the tax assessor and collector. Under the early system, each property owner was responsible for filing an affidavit of his property with the county sheriff. The resultant list of property values within the county comprised the property tax base.

In 1912, the year of statehood, the State Tax Commission was formed to supervise the collection of property taxes. All similar properties were to be valued equally at full cash value. The Tax Commission was authorized to appraise all producing mines, railroads, telegraph and telephone companies, express companies and private car companies in the state. Appraisal of all other properties was charged to the counties.

The Tax Commission immediately discovered that property appraisals varied widely across the state, ranging from 25% to 70% of full cash value. In an attempt to equalize appraisals, the Commission ordered that all property be assessed equally, at 50% of its full cash value. Although an effort was made to comply with this order,which resulted in a substantial increase in assessed valuation, not all counties conformed fully. To give the State Tax Commission the power to supervise the county boards of equalization, an amendment to the Constitution was presented to the voters in the 1912 election. The amendment passed, and in 1913 the State Tax Commission was granted broader powers.

*For a more detailed description of the historical development of the property tax, see "A Historical Review of the Property Tax in Arizona," prepared by House Staff, October 1977.

By 1913, statutory classes existed for express companies, private car companies, banks and general property. Properties in each of these classes were treated differently. Express companies were taxed on gross proceeds in lieu of ad valorem taxes. Private car companies were also subject to a separate tax in lieu of the state property tax. Banks were taxed on capital stock, and general properties were assessed and taxed under general law. Each taxing mechanism was selected for purposes of simplicity and convenience.

In 1933, the Intangible Property Tax Act created seven classes of intangible property, each bearing a different tax rate. This law represented the first attempt to use the classification system to modify the burden of taxes among taxpayers. In the following year, however, the act was struck down by the State Supreme Court on the grounds that the classification system that was established was arbitrary and that there was no mechanism for taxpayers' appeals. It is interesting to note, however, that although the act was declared unconstitutional, the court did rule that a classification system was constitutional as were different tax rates for different classes.

In 1950, the Legislature distinguished between manufactories and other types of property, and as a result modified the tax burden of businesses. The 1950 act provided that machinery used in the operation and maintenance of any manufactory could be assessed for tax purposes at 50% of its book value. Excluded from the definition of a manufactory were businesses engaged in the following activities:

- mining, smelting, quarrying, etc.
- furnishing utilities to consumers
- telephone or telegraph service
- pipeline operations
- publication
- job printing or advertising
- slaughtering
- contracting

Thus, while the State Tax Commission was trying to establish uniformity of assessments, the state was providing for differences in the treatment of properties by altering the assessment ratios applicable to different types of property. Differences in assessments persisted, thereby altering the relative property tax burden, both between and within counties, and between classes of property.

In 1959, the Southern Pacific Railroad challenged the property tax assessment system in court on the grounds that the railroads were being assessed higher than other properties. The Arizona Supreme Court ruled that the system was discriminatory and must be prohibited in the future since it was not provided for in statute. The legislature, concerned by the decision, ordered a reappraisal of all properties within the state in preparation for reform. The revaluation was to be conducted by the newly established Division of Appraisal and Assessment Standards which became the Department of Property Valuation in 1967.

In 1968, after the revaluation was completed, the legislature began research to develop a classification system which would essentially preserve the existing tax burden. The 26 classes of property existing at the time were merged into four classes, each to be appraised at full cash value. A separate assessment ratio was then applied to each classification to determine assessed valuation. The four classifications of property established in 1967 and their assessment ratios are as follows:

Class 1: Assessment ratio - 60%
Flight property, private car companies, railroad property used in the continuous operation of the line, producing mines, and standing timber

Class 2: Assessment ratio - 40%
Telephone and telegraph companies, gas water and electric utilities and pipelines

Class 3: Assessment ratio - 25%
Commercial or industrial property other than that included in Class 1, 2 or 4, including residential rental property

Class 4: Assessment ratio - 18%
Agricultural property and all other property not included in Class 1, 2 or 3

This classification system was protested by the railroads to the Arizona Supreme Court in 1969. The Supreme Court, however, upheld the classification system.

Legislation in 1968 required that the county assessors update property valuations annually. This was found to be very expensive in terms of personnel and budgets. The Director of the Department of Property Valuation wanted to update one-third of all properties each year, thus revaluing each piece of property every three years. An Attorney General's opinion concluded that such a system would be permissable. The three-year revaluation was challenged in court, however, on the grounds that it was unfair to those taxpayers revalued in the first and second years, and was found to be unconstitutional. The case, however, was appealed and overturned in 1975.

The number of property classifications was expanded during the period from 1973 to 1977. Currently, eight classes of property are defined in statute, each with a separate assessment ratio.

2. Property Tax Rates

a. State Property Tax Rate. The state property tax rate is set annually by the Joint Legislative Tax Committee on or before the second Monday in August of each year. The property tax rate is technically composed of two tax rates, one for general purposes and one for educational purposes. The combined state tax rate cannot exceed $1.60 per $100 of assessed valuation.

The state property tax rates for the years 1968 through 1978 are shown below:

State Property Tax Rates*

Year	Tax Rate	Year	Tax Rate
1968	$2.16	1974	$1.50
1969	2.20	1975	1.60
1970	1.65	1976	1.60
1971	1.90	1977	1.60
1972	1.55	1978	1.10
1973	0.75		

b. Local Property Tax Rates. Local property tax rates are set by the governing board of each county, city or town by the third Monday in August. School district and community college property tax rates are set by the county board of supervisors within the same time limit.

The tax rate may vary substantially between taxing areas. In 1978, for example, for all school districts comprised of both an elementary and a high school, the high tax rate was $22.05 in Union No. 62 in Maricopa County, and the low rate was $2.825 for Morenci Unified District No. 18 in Greenlee County. The tax rate is a function of the budgeted needs of the community, and the

*Tax rate is defined as a rate per $100 of assessed value.

amount and type of property in the districts.

1978 Average Aggregate Property Tax Rates by County*

County	Average Tax Rate per $100 Assessed Valuation
Apache	7.63
Cochise	10.43
Coconino	7.09
Gila	9.33
Graham	10.08
Greenlee	3.54
Maricopa	11.86
Mohave	11.26
Navajo	6.67
Pima	13.43
Pinal	13.01
Santa Cruz	11.69
Yavapai	10.36
Yuma	11.59

*The average combined rate applied to property within the county includes state, county, city, school district and special district rates.

Administration

1. Property Tax Base

a. Appraisal. Property is required by law to be appraised annually, as of January 1 of each year. There are two levels of property tax administration in Arizona. The county assessors appraise standing timber listed in Class 1, and all properties in Classes 3, 4, 5, 6, and 7.

All other properties are appraised centrally by the Department of Revenue's Division of Property and Special Taxes. All centrally appraised properties are income producing properties which often cross county lines and are difficult to appraise.

The Department of Revenue is directed by statute to "adopt standard appraisal methods and techniques for use by the department and county assessors in determining the valuation of property." There are three general ways to appraise property: the Cost Method, the Sales Comparison Method, and the Income Capitalization Method. These methods are described below.

Cost Method

The cost method determines the market value of property by adding the cost to replace the house or building, less depreciation, to the value of the land. This method is used for all locally valued commercial property, and for some single family residences. In order to revalue all property annually, the method has been computerized.

The cost model developed by the Department of Revenue is a statewide model and is implemented as described below:

At time of construction, a county assessor makes a physical inspection and notes all the physical characteristics of a piece of property. The assessor then assigns the property a rating denoting quality. Based upon construction data, a typical home of a given rate is estimated to cost a specific number of dollars per square foot. The number of square feet in the property being assessed is then multiplied by this dollar amount to reach a replacement cost. Any physical characteristics not accounted for in a home of this rating are then valued and added to the base price. These characteristics are termed "add-items." The age of the property is then taken into consideration and the property is depreciated. By feeding this information into a computer, the appraised value of the home during subsequent years may be calculated simply by changing the cost values assigned to physical characteristics to reflect current market value. The land value is then added to the market value of the improvements.

The primary advantages of the cost model are as follows:

1) The mechanics of the cost model are easy to explain to taxpayers.

2) The cost model works best for the appraisal of dissimilar properties for which there is relatively little sales data.

The primary disadvantages of the cost model are as follows:

1) The cost of add-items is not often changed.

2) A typical house isn't typical anymore. 35% of the value of property improvements are add-items.

3) It is difficult to continually update manuals to reflect changed base factors and add-on values.

4) It is difficult to estimate depreciation without looking at market values.

5) Cost does not necessarily reflect market value.

Sales Comparison Method

The sales comparison method estimates the market value of a piece of property based upon the sales prices of similar properties which have recently sold in the same geographic area.

To expedite the annual reappraisal of homes, the Department of Revenue began a computerized appraisal system, using a statistical technique called Multiple Linear Regression (MLR) which measures the relationship between property characteristics and sales price. The MLR is used only for single family residential homes because it requires a large volume of sales data from similar properties and properties in other classifications do not turn over rapidly. The MLR is a statewide model, but reflects differences between counties. Eight counties use the MLR model. Some use it exclusively for single family residential properties, while others use MLR in urban areas and the cost model in rural areas. At this time, the original MLR model is used as follows:

At the time of construction, a county assessor makes an inspection and lists the physical characteristics of a home which are related to sales price by one of the 24 equations of the MLR model. These physical characteristics include square feet, number of rooms, patios, etc. This information is then fed into the Department of Revenue's computer.

To determine the level at which a given physical characteristic is to be valued, the Department utilizes data from recently sold homes. After a piece of property is sold, a sales affidavit must be sent to the county assessor. The county assessor then sends the affidavits to the Department of Revenue. Sales affidavits which do not represent market value transactions, such as sales between relatives or foreclosures, are not used by the Department. These types of sales often do not accurately reflect market value and would distort the data base. The sales affidavits include information about the characteristics which are related to sales price by one of the 24 equations of the model. Based upon the number and type of physical characteristics and the sales price, the computer calculates the portion of the sales price which may be attributed to each of the characteristics listed on the sales affidavit. This value is termed a "coefficient."

For purposes of the annual reappraisal of property, the values derived for a property characteristic from the sales affidavits of a given area are used only to calculate the value of properties within that area. The base price of a property is calculated by summing the values determined for each characteristic of the property. The base price is then adjusted by a "neighborhood factor" which represents market differences attributable to the differences. between neighborhoods. The neighborhood factors are also derived from the sales affidavit data and primarily reflect differences in land value.

The first appraisal of homes made in 1973 with the MLR system produced values that were approximately 25 percent higher than those derived under the old system. To compensate the homeowner for the sudden increase in valuation, the Legislature began the homeowner property tax rebate program.

The primary advantages of the MLR model are as follows:

1) Provided that sales information is current, the MLR model should produce values as close as possible to actual market value.

2) If applied correctly, the MLR model reduces human error.

3) The MLR model uses sales data and property data to statistically generate appraisal values.

4) The MLR model works best for similar properties, with abundant sales data.

The primary disadvantages of the MLR Model are as follows:

1) The MLR model is very technical and the mechanics are difficult to explain. In-house statistical expertise is required to monitor and update the system.

2) The equations in the model could be simpler and more logical.

3) The number of variables has not been expanded since construction of the model. Physical characteristics, such as fireplaces, fences, and lot sizes are not represented in the equations.

4) The coefficients are not always internally consistent. For example, a piece of property in "excellent" physical condition may have a lower value than if it were in "good" condition.

5) Any improvements made after the time of construction will not be reflected unless a building permit was recorded, or a county assessor noted the construction.

Income Capitalization Method

The Income Capitalization Method appraises property on the basis of its income generating capability. This is translated into current worth to reflect market value, or what the enterprise would be worth to an investor in the open market. Historical data and future expectations are taken into account to estimate a future income stream for the property. In contrast, an appraisal based solely on the value of the physical property and the land will not reflect earning potential. This method is used primarily for centrally valued properties, but can also be used in the appraisal of commercial properties.

Primary advantages of the Income Capitalization Method of appraisal are as follows:

1) Distinctive type businesses can be treated individually.

2) The income capitalization method works best for dissimilar properties for which there is relatively little sales data.

Primary disadvantages of the income capitalization method are as follows:

1) The estimation of a future earning stream is difficult.

2) For multi-state companies, the allocation of in-state value is difficult.

3) The method requires highly skilled appraisers familiar with accounting and economic principles as well as current industry data.

b. <u>Tax Processing</u>. Administration of the property tax also involves the recording of property values after they have been appraised, classified, and assessed, making further adjustments to the value such as reductions for exempt amounts or deflation factors; notifying taxpayers of property value, and the appeals process.

For locally valued property, the county assessor must identify all property in the county that is subject to taxation by November 30. By January 1, the county assessor must determine the owner and the full cash value of the property.

By February 10, each property owner must be notified as to the valuation of the property. If the owner does not agree with the valuation of his property, he has until February 15 to file a petition for review with the county assessor. The county assessor then has 15 days to determine if an adjustment should be made and submit a correction to the Department of Revenue if necessary.

By April 20, the county assessor must deliver the property tax roll to the county board of supervisors. The roll must include the assessed valuation of property, and any change in assessed valuation over the previous year must be reported to the Department of Revenue.

The board of supervisors must then give a public notice of the meeting of the county board of equalization. The board of supervisors also acts as the county board of equalization. The county board of equalization meets on the first Monday in May to consider any changes in assessed valuation.

If a taxpayer has filed a petition with the county assessor, and has been denied a change, in whole or in part, he may then appeal the decision to the county board of equalization within 15 days. The county board then has 10 days from the date the petition is heard, to make any adjustments. If any increase in valuation is to be made, the county board of equalization must notify the taxpayer and the Department of Revenue at least 5 days prior to the June meeting of the county board.

The county board of equalization then meets on the first Monday in June, and must equalize the tax roll no later than the second Monday in June. Any taxpayer dissatisfied with the decision of the county board of equalization may appeal to the superior court before November 1, or petition the state board of tax appeals within 15 days of the mailing of the decision by the county board of equalization. The state board of tax appeals meets on the first Monday after July 15. Before this time, the board must examine and compare the valuations of property in each county. The board may equalize property between and within counties and classes. If the valuation of a property is to be increased, a hearing must be held in the county or counties where the property to be affected is located. A public notice must be issued at least ten days prior to the hearing. The state board of tax appeals then has 30 days to decide upon the petition. This must be done no later than July 25, at which time the state board must submit a statement of any changes in valuation to the county board of supervisors and the Department of Revenue.

Before the first Monday in August the county board of equalization must submit the property tax abstract to the county board of supervisors, the state board of tax appeals, and the Department of Revenue. It is then the Department of Revenue's responsibility to prepare a statewide abstract containing the valuation of property by county and taxing district, and submit copies to the state board of tax appeals and each county board of supervisors. At this time the amount of assessed valuation for every jurisdiction is established for purposes of setting the tax rate.

When the rates have been established for all taxing jurisdictions, the county board of supervisors prepares the assessment and tax roll, and submits it to the county treasurer. The county treasurer must then publish for four consecutive weeks a notice of the due and delinquent dates for payments of taxes. The first one-half of taxes are due on October 1, and delinquent on November 1. The second one-half of taxes are due on March 1 and delinquent on May 1.

2. Rate

a. Rate Determination. Once the assessed valuation base has been established, and the budgets for the coming year proposed by the taxing jurisdictions, all taxing jurisdictions that have the right to levy a tax may establish their tax rates. The rate applied to a particular parcel of property will equal the rates levied by each taxing jurisdiction in which the parcel of property is located.

The rate setting procedure for each jurisdiction is essentially the same. The tax rate is expressed as dollars per $100 of assessed valuation. The tax rate when applied to assessed valuation should produce adequate funds to meet the revenue requirements of the taxing jurisdiction. The revenue requirements are known from the proposed budget. Revenues from any source other than the property tax are subtracted from the revenue requirements to determine the necessary property tax levy. The amount of assessed valuation per jurisdiction is also known. Because the tax rate is established as dollars per one hundred dollars of assessed valuation, the assessed valuation is divided by 100. This number is then divided into the net revenue requirements of the jurisdiction to determine the tax rate.

In summary, the property tax rate is set in the following manner:

Total Revenue Requirements
- Funds Other Than Property Tax
Necessary Property Tax Levy

$$\frac{\text{Necessary Property Tax Levy}}{\text{Assessed Valuation} \div 100} = \text{Tax Rate}$$

b. Property Tax Jurisdictions. A parcel of property may fall within several political jurisdictions that have the power to levy a property tax. For example, a property owner is liable for taxes levied by the state, the county, a city, a school district, and perhaps, one or more special districts. There are approximately 15 types of special districts in Arizona, formed for the purpose of supplying a locally needed facility or service. Types of special districts include:

Antinoxious (weed) districts
Electrical districts
Fire districts
Flood control districts
Hospital districts
Improvement districts
Irrigation districts
Irrigation and water districts
Library districts
Road districts
Sanitation districts
Street lighting and improvement districts
Sidewalk districts
Water districts
Water conservation districts

To determine the property tax liability of a particular parcel subject to different taxing jurisdictions, a tax area code is assigned. The tax area code represents a specific geographic boundary in which several tax jurisdictions exist. The tax area code is used to identify the tax rates applicable to the assessed value of a property.

Incidence

The responsibility for payment of the property tax rests, by statute, with the legal owner of the property. The incidence of the property tax varies with the classification of property due to the differences in assessment ratios. An equal value of Class 1 property, assessed at 60 percent of market value, pays more property tax than a residential home in the same taxing jurisdiction assessed at 15 percent of market value.

The ultimate economic incidence of the property tax is dependent upon the types and use of the property being taxed, and the ability of the property owner to pass the tax on to others.

The burden of the property tax upon residential property falls almost without exception upon the homeowner. The property tax represents a loss of income to the homeowner which will rarely be passed to others. The tax burden on the individual homeowner is commonly measured as a ratio of property tax liability to income.

The incidence of the property tax on business is not easily defined. The property tax will represent an additional cost to business, which must be covered by a reduction in other costs or by an increase in the price of the product or service provided. Thus, the tax burden upon commercial properties may be borne by the owner(s) in the form of reduced profits or dividends, by factors of production, such as labor, in the form of reduced wages, or be passed along to consumers in the form of higher prices for the goods and services they purchase. If the good produced is sold out of state, the property tax is said to be "exported," or paid by out-of-state residents. Ultimately, individuals bear the burden of all commercial taxes. The ability of a business to pass taxes forward and the percentage of the tax that can be passed forward is dependent upon the demand for and supply of the particular good or service provided by the business. For this reason, it is difficult to do more than generalize about the economic incidence of property taxes upon commercial properties.

Total collections from the property tax during 1977-78 amounted to $778 million. The distribution of property tax collections among taxing districts is shown below:

	Amount	% of Total
State*	$ 75,701,324	9.73%
Counties	177,199,062	22.76
Cities	52,490,423	6.74
School Districts	395,961,952	50.87
Community Colleges	56,457,874	7.25
Special Districts	18,830,759	2.42
Unorganized Territory	1,775,431	0.23
TOTAL	$778,416,825	100.00%

Source: Arizona Tax Research Association, 1978 Arizona Property Tax Rates and Assessed Valuations

*the state rebated $57.5 million back to homeowners during 1977-78

A large portion of the total tax levied on property owners is never collected or is returned to taxpayers because of the effects of several tax relief programs. These programs are discussed below:

Current Property Tax Relief Programs

a) Property Tax Relief through the Arizona Income Tax

Homeowners Property Tax Deduction - When computing Arizona income tax liability, property taxes paid are a deductible expense from adjusted gross income.

Property Tax Credit - for homeowners age 65 or older, with sole income of less than $3,750 or a joint income of less than $5,000, there is a property tax credit that is dependent upon the level of income. The maximum credit is $225.

Renters Credit - each renter may receive an income tax credit of ten percent of rent paid, or $75, whichever is less. This figure represents the amount of property taxes paid indirectly as rent.

b) Property Tax Rebate

The property tax rebate originated in 1973 when legislation was enacted to relieve homeowners from the effects of significantly increased property valuations caused by the statewide revaluation of residential property under the MLR appraisal system. As the program currently operates, monies are appropriated to the county treasurers to pay a portion of the school district property tax levy which would otherwise be paid by homeowners. The property tax rebate was originally made possible by revenues received from the Federal Revenue Sharing Program. Total funds appropriated for this purpose are shown below for each year in which the program has been in effect.

Property Tax Rebate Totals

1973 -	$42M
1974 -	40M
1975 -	39M
1976 -	35M
1977 -	40M
1978 -	57.5M

c) Property Valuation Limits

In an attempt to reduce the inflationary impact on housing values, the Legislature in 1977 required that for tax year 1978, prior to computing property tax liability, the assessed value of residential property was to be divided by 1.05. This will deflate the assessed value by 5%. For tax year 1979 assessed values will be deflated by a factor of 1.15.

Criteria

1. Revenue Generation:

   a. Will revenues from the property tax expand as the demand for government service expands?

   As the population grows, new demands are placed upon government. The increase in population will probably require the construction of new homes, which will add to the property tax base. The expanded base will, in turn, produce new revenues which can be used to finance the growth in government services associated with an increase in population.

   b. Will revenues from the property tax expand as the price of government services increases?

   Market values of property consistently increase as the general level of prices within the economy rises. Property tax liability is based upon the market value of property, and therefore, is a growing source of revenue in an inflationary economic period. Problems may result if the added revenues resulting from the growth of market value exceed the revenue needs of the government.

   As property values increase due to inflation, the same tax rate will result in a growing property tax levy regardless of the requirements of the taxing jurisdiction. The property owner's tax liability will continue to grow under these conditions unless the tax rate is reduced commensurately or the property tax revenue is rebated back.

2. Social Equity:

   a. Is the property tax affordable to the individual taxpayer?

   Everyone pays property tax in some form. A property owner pays the tax directly or as part of a mortgage payment. A renter pays property taxes within the price of the rent. Tax liability is dependent upon assessed valuation, which is a percentage of market value. The market value represents potential profit to the property owner at the time of sale, but may not bear a relationship to the current income of the individual occupying the property or his ability to pay taxes. As market values rise, the assessed valuation and resultant tax liability also rises, unless the tax rate is reduced to offset the higher assessed value. If property tax liability increases more than income, the property owner will be paying a relatively larger percentage of income in property taxes regardless of his ability to pay.

   In 1976, the average new home was bought for $48,400. The latest national figures for the U.S. show the average new home price to be $62,900. This increase in market values has outpaced growth in income for many people.

b. Is the property tax borne by individuals with common circumstances equivalent?

Differences in appraisal techniques and flaws within the appraisal system can result in unequal tax burdens for similar properties, both within and between taxing jurisdictions. Sales ratios have been developed by the Department of Revenue to show the relationship between appraised property values derived by the MLR method and current sales prices in the several counties.

The most recent study showed that the state's median sales ratio for residential property was .83, which means that the appraised full cash value was 83% of the estimated current market price. These sales ratios range from 65% in Navajo County to 85% in Graham County.

Disparities in sales ratios can be between properties in the same legal class, between properties in different legal classes, or between counties. If two identical homes are appraised differently, it will result in the homeowners bearing different tax burdens. Here is an example, using a $40,000 home in two different counties, to illustrate the possible inequities. In order to isolate the effects of the differences in appraisal, the example assumes the same tax rate for each home.

Navajo County		Graham County	
$40,000	market value	$40,000	market value
.65	sales ratio	.85	sales ratio
$26,000	full cash value	$34,000	full cash value
.15	assessment ratio	.15	assessment ratio
$ 3,900	assessed value	$ 5,100	assessed value

Navajo County: $\frac{\$\ 3,900}{100} \times \$11.31^* = \$441.09$

Graham County: $\frac{\$\ 5,100}{100} \times \$11.31^* = \$576.81$

*Average state tax rate.

Unequal tax burdens within the same class of property can also be a result of different tax rates between jurisdictions. As mentioned earlier, tax rates are dependent upon: 1) the needs of the community, as expressed in the proposed budget, and 2) the amount and type of property in the community. The difference in tax rates will greatly affect the tax burden.

Consider two taxpayers with homes valued at $40,000 in two school districts with greatly divergent tax rates as shown below:

	Home A	Home B
Market value	$40,000	$40,000
Assessment ratio	.15	.15
Assessed value	$ 6,000	$ 6,000
Assessed value ÷ 100	$ 60.00	$ 60.00
Tax rate	x 22.05	x 2.82
Tax liability	$1,323.00	$169.50

The distribution of the tax burden is clearly different for each of the homes in the example. It must be remembered, however, that although the tax liabilities are different for each home, the differences may be due in part to the different level and type of services required by the individuals of the two districts. The "benefits" principal of taxation is another measure of social equity.

c. Will individuals who receive greater benefits from government services pay greater property taxes?

Properties located in a community with a high property tax rate will be subject to greater taxes than properties of similar value located in communities with a low property tax rate. A high tax rate could reflect a greater willingness on the part of the community to provide funding for government services, in which case the level of property taxes may bear a relationship to benefits received. A high tax rate may also exist because the amount of assessed valuation in the district is low. Property owners in districts with low valuation may be required to pay a proportionately higher tax rate to finance services similar to those purchased in other districts which levy a smaller tax rate albeit on a greater assessed valuation.

3. Ease of Administration:

Can the property tax base be determined without difficulty?

The property tax is levied on the assessed valuation of a property which is based on the property's current market value. If the property has not been sold recently, no direct measure of the current market value of the property will be readily available and the value of the tax base will have to be determined by one of the three methods discussed above. Because of the complexity of these methods of appraisal, the exact value of the tax base will be somewhat difficult to determine.

Estimating the value of the property tax base is further complicated by the use of a separate assessment rate for each classification of property. Properties are classified according to use. As usage changes or properties are subdivided, valuation assessment is made more difficult. In addition, a parcel of property may contain two or more legal classes of property which complicates assessment. For example, a farm may be comprised of a home (class 5) and agricultural land (class 4). Such a parcel is termed a "split parcel." For assessment purposes, an assessor must determine how much of the total value of the property is represented by each use, in order to determine the value which is subject to each assessment rate.

4. Consistency with State Goals:

   a. Will a substantial portion of the property tax be paid by the residents of other states?

      Residential property taxes are borne by homeowners and renters. The vast majority of homeowners and renters are Arizona residents. Due to the growth in tourism, however, some taxes on residential property may be paid by non-residents.

      Commercial property taxes represent an added cost to business. In order to cover this additional cost, businesses may reduce purchases of supplies or wages paid to employees; they may raise the price of goods and services provided; or they may reduce the profits or dividends available to owners and shareholders. Thus, firms which are owned by out-of-state residents, which purchase supplies from out-of-state vendors and which produce a good or service consumed in whole or in part out of state, will provide the best opportunity to export the property tax.

   b. Will the property tax produce revenues without detrimentally affecting business?

      The ability of commercial properties to pass the property tax to others is dependent upon the demand for and supply of the good or service provided. If the sales of the good or service are sufficient to cover all costs of production including the cost of paying property taxes, there will be no detrimental effect to business.

      The in-migration of new businesses to Arizona is dependent upon the supply and price of labor, materials, transportation, land and the existence of markets for the product. The property tax is generally not a sufficiently large percentage of unit costs to weigh heavily on the decision of firms to relocate. Studies indicate that the property tax is probably not a major determinant in the location decisions of firms.

SECTION FIVE

SALES AND USE TAXES

This section presents an overview of the sales and use taxes levied within Arizona. Included are:

A. SALES TAXES

   1. Transaction Privilege Tax
   2. Education Excise Tax
   3. Special Excise Tax for Education

B. USE TAX

C. RENTAL OCCUPANCY TAX

A. SALES TAXES

In Arizona, the sales tax, that tax which is imposed upon the gross proceeds of sale or gross income from sales, is composed of three individual taxes: a transaction privilege tax; an educational excise tax; and a special excise tax for education. For purposes of evaluation and examination, in this section, these three taxes are grouped together because of certain commonalities in the areas of administration, collection and incidence. The use tax and the rental occupancy tax are addressed individually.

The Transaction Privilege Tax. The Transaction Privilege Tax, a sales tax, was first authorized in 1933. The tax is based upon the privilege extended to the seller to engage in the business of selling tangible personal property. The liability for the tax lies with the seller and is applied to the gross receipts of specified activities. The rates of the Transaction Privilege Tax are set by statute and range from ¼% to 2%. Tax revenue is shared with cities, towns and counties. Transaction Privilege Tax collections, including penalties, interest and licenses, during 1977-78 amounted to $247.6 million. The revenue from the Transaction Privilege Tax is to be used to pay for obligations of the state and county governments, to pay for the expenses of the state and the counties, to reduce the levy on property for public school education, and to reduce or eliminate the state and county property tax rate.

Education Excise Tax. Another sales tax, the Education Excise Tax was authorized in 1959. This tax is also imposed upon the gross proceeds of sales or gross income from the activities of various businesses. For most business classifications, the education excise tax rate is set by statute at 100% of the transaction privilege tax rate. Exceptions are mining, timbering, rental of real property, and feed wholesaling, on all of which the rate is 50% of the privilege tax rate. The Education Excise Tax is earmarked for educational purposes. Collections in 1977-78 amounted to $240.6 million, including penalties and interest.

Special Excise Tax for Education. A third sales tax was enacted in 1968, the Special Excise Tax for Education. This special excise tax is also levied on the gross receipts of selected business classifications at rates set by statute of 1% or 2%. The tax rate for copper mining, copper smeltering and copper production is 1 %, but has been reduced to ½% for the period June 1, 1978 through June 30, 1980. Receipts from the Special Excise Tax for Education are deposited to the State General Fund but are not dedicated to any specific purpose. In 1977-78, collections amounted to $81.1 million. These three taxes together produced collections of $569.2 million for nearly one-third of total state revenues. The aggregate rate for each business classification against which any one of the three sales taxes is levied and the component parts of the total rate are shown in Table V-1.

Exemptions

The following activities and commodities are exempt from payment of the sales tax by statute:

1. The sale of stocks and bonds.
2. Personal or professional services.
3. A service provided in connection with the retail sale of tangible personal property, other than mining, utility, communications, private car, pipelines, transportation, publishing, job printing, advertising, prime contracting, and the provision of services in connection with the sale of food or drink.

TABLE V-1

TAXABLE ACTIVITIES

TAXABLE ACTIVITIES	PRIV-ILEGE TAX	ED. EXCISE TAX	SP. EXCISE TAX FOR EDUCATION	COMBINED TAX
MINING-OIL & GAS PROD.	1%	½%	1%	2½%
TRANSPORTING & TOWING	1	1	2	4
UTILITIES	1	1	2	4
COMMUNICATIONS	1	1	2	4
RAILROADS & AIRCRAFT	1	1	2	4
PUBLISHING	1	1	2	4
PRINTING & ADVERTISING	1	1	2	4
PRIVATE CAR, PIPELINES	1	1	2	4
CONTRACTING	1	1	2	4
TIMBERING	1	½	-	1½
RESTAURANTS & BARS	2	2	-	4
AMUSEMENTS	2	2	-	4
RENTALS OF REAL PROP.	2	1	-	3
RENTALS OF PERSONAL PROP.	2	2	-	4
FEED WHOLESALE	¼	1/8	-	3/8
RETAIL	2	2	-	4

*EFFECTIVE JUNE 1, 1978 THROUGH JUNE 30, 1980, THE SPECIAL EDUCATION EXCISE TAX IS REDUCED BY ONE-HALF (½%) PERCENT FOR COPPER MINING, COPPER SMELTERING AND COPPER PRODUCTION FOR ANY PURPOSE.

4. The sale of a warranty or service contract with a term factor cost of $400 or less.

5. The sale of prescription drugs.

6. The sale of prescribed prosthetic appliances.

7. The sale of insulin and the sale of insulin syringes if purchased with insulin.

8. The sale of prescription eyeglasses or contact lenses.

9. The sale of hearing aids.

10. The sale of prescribed hospital beds, braces, crutches, wheelchairs, or corrective shoes.

11. Sales of gasoline on which a fuel tax has been levied.

12. Common or contract motor carriers subject to the Motor Carrier License Tax.

13. Sales of tangible personal property to a licensed contractor for subsequent inclusion in a structure in fulfillment of a contract.

14. Sales in interstate or foreign commerce, which are exempted from a sales tax by the U.S. or Arizona Constitution.

15. Personal property purchased, leased or rented by a non-profit charitable hospital or a hospital operated by the state or political subdivision.

16. Sales of tangible personal property by non-profit charitable institutions.

17. Sales made directly to the U.S. Government by manufacturers, modifiers, assemblers, or repairers, and sales to the manufacturers, etc., when such sales are a component part of subsequent sales to the U.S. Government.

18. Sales to the U.S. Government by other than manufacturers, modifiers, assemblers, or repairers are exempt to the extent of 50% of the tax.

19. Printing, when sold for resale.

20. The cost of labor employed in construction improvements or repairs, which shall be established as thirty-five percent of gross proceeds from sales.

21. The sale price of land paid by contractors not to exceed the fair market value.

22. Subcontracting, when performed under the control of a prime contractor.

23. Events sponsored by the Arizona Coliseum and Exposition Center Board or County Fair Commissions.

24. Theatre films (which are not taxed as personal rental property) if the theatres in which they are run are taxed under the transaction privilege tax statute.

25. Property constructed or improved by an owner-builder, if held for at least two years prior to sale.

26. Use of coin-operated washing, drying, dry cleaning, or car washing machines.

27. The leasing or renting of residences which have been continuously occupied by the same person for at least 30 days.

28. Amusements, exhibitions, etc., sponsored by religious or charitable institutions.

29. Sales of electricity, power, gas, or water for resale.

30. The publishing of books.

31. The lease or rental of properties which would be exempt from transaction privilege taxes if owned by the lessee.

32. The following categories of machinery and equipment:

    a. Used directly in manufacturing, processing, fabricating, job printing, refining or metalurgical operations.

    b. Used directly in mining, including equipment needed to prepare materials for extraction, and the handling, loading, or transportation of such materials to the surface.

    c. Tangible personal property consisting of central office switching equipment, switchboards, private branch exchange equipment, coaxial cable, micro-wave radio and carrier equipment of telephone and telegraph companies.

d. Tangible personal property used directly in the production or transmission of electrical power, including transformers and control equipment used at transmission substation sites. (This does not include machinery and equipment used in the distribution of such power.)

e. Pipelines four inches in diameter or larger, used to transport oil, natural gas, artifical gas, water or coal slurry.

f. For airlines holding a federal or state certificate of public convenience and necessity or foreign air carrier permit for air transportation, tangible personal property consisting of airplanes, navigational and communications instruments and related accessories and equipment used in conjunction with aircraft used in transporting persons or property for hire.

g. Tangible personal property consisting of rolling stock, rails, ties, and signal control equipment used directly in railroad transport.

h. Machinery and equipment used directly in drilling for or extracting oil and gas for commercial purposes.

i. A system or series of mechanisms designed as a solar energy device.

j. Buses or tangible personal property used directly in the transportation of persons pursuant to a government program.

33. Machinery and equipment delineated in Number 33 (above) which is exempt if sold is also exempt if leased or rented.

34. Charges from a landlord to a tenant for utilities, when the landlord has installed individual meters for each rental and charges each tenant on the basis of the individual reading.

B. USE TAX

In 1956, a Use Tax was imposed upon individuals making purchases outside the state at retail for use, storage or consumption within Arizona and not paying a transaction privilege tax on those purchases. Such a situation occurs primarily when purchases are made out of state and no sales tax is paid to the other state; or a sales tax at a lower rate is paid to that state. In both instances, when property is brought to Arizona for storage, use or consumption, a use tax is levied equal to the difference between the Arizona sales tax rate and the rate which was paid on the item when purchased. The person making the purchase is liable for the tax. The maximum Use Tax rate is 4%. In 1977-78 use taxes amounting to $17.2 million were collected. Revenues collected from the Use Tax are divided equally between the Use Tax Receipts Fund and the Educational Excise Tax Fund. The educational excise funds collected under Use taxes are allocated to the General Fund and dedicated for education. The Use Tax Fund is transferred to the State General Fund at the end of each calendar month.

Exemptions

Tangible personal property is exempt from payment of the Use Tax when:

1. Taxed under the provisions of the Transaction Privilege Tax.
2. Taxed under the provisions of the Motor Vehicle Fuel Tax.
3. Prohibited from taxation by federal law.
4. Incorporated as an ingredient or component of any manufactured, fabricated or processed article, substance or commodity for sale in the regular course of business.
5. Subject to an excise tax imposed by another state, at a rate equal to or greater than the rate levied by the Arizona Use Tax.
6. Incorporated into a building or structure by a licensed contractor who holds a Transaction Privilege Tax License.
7. Brought into the state by a nonresident for his own storage, use, or consumption while temporarily within the state, unless such property is used in conducting a business in Arizona.
8. Brought into Arizona from outside the continental limits of the United States for personal use; however, property imported at a rate in excess of $200 retail value per month is not exempt.
9. Purchased outside the state by hospitals organized and operated exclusively for charitable purposes or by hospitals owned and operated by the state or a political subdivision.
10. Used or consumed in the businesses of farming, ranching and feeding livestock or poultry, not including equipment, fertilizers, herbicides and insecticides.
11. Directly used as machinery or equipment in manufacturing, processing, fabricating, job printing, refining or metallurgical operations.
12. Directly used as machinery or equipment in extracting ores or minerals from the earth for commercial purposes, including equipment required to prepare the materials for extraction and handling, loading or transportation of such extracted materials to the surface.

13. Used as telephone company or telegraph company central office switching equipment, switchboards, private branch exchange equipment, microwave radio and carrier equipment, and coaxial cable.

14. Directly used as machinery or equipment in the production or transmission of electrical power, excluding machinery or equipment used for distribution of electricity, transformers and equipment used at transmission substation sites.

15. Consisting of pipes or valves four inches or greater in diameter, used for transporting or distributing gas, oil, water or coal slurry.

16. Consisting of airplane, navigational and communications instruments and other accessories and related equipment acquired and used in transporting for hire, owned by airlines holding a federal or state certificate of public convenience.

17. Consisting of rolling stock, rails, ties, signal control equipment used directly in transporting for hire.

18. Used directly as machinery or equipment in drilling for oil or gas or used directly in the process of extracting oil or gas from the earth for commercial purposes.

19. Consisting of solar energy devices.

20. Consisting of buses used directly in transporting for hire and owned by bus companies holding a certificate of public convenience.

21. Consisting of prosthetic devices acquired by prescription, insulin, syringes purchased with insulin, eyeglasses, contact lenses, hearing aids, braces, etc.

C. RENTAL OCCUPANCY TAX

The Rental Occupancy Tax is levied at a rate of 2% against real property that is on a long-term lease, which was entered into prior to December 1, 1967. This tax is in lieu of the sales tax on the rental of real property. The Rental Occupancy Tax is to raise money to liquidate the outstanding obligations of state and county government; to defray the necessary and ordinary expense of state and county government; and to reduce the tax burden on property. Tax revenues are shared with state, county and local jurisdictions. Collections in 1977-78 amounted to $169,500.

Exemptions

The following situations are exempt from the Rental Occupancy Tax:

1. Occupancy by any tenant who is exempt from taxation under the constitution or laws of the United States or Arizona.

2. Occupancy under a lease entered into prior to December 1, 1976 which the constitution or laws of the United States or Arizona would prohibit from taxing if the landlord were the tenant.

3. Leasing or renting of property when such property is used by the lessee as a principal place of residence.

4. Occupancy under a lease or rental agreement entered into prior to December 1, 1967, if the length of the term of the lease or the size of the premises is subsequently changed.

5. Occupancy under a lease or rental agreement for the following businesses: hotels, guesthouses, dude ranches, resorts, rooming houses, apartment houses, office buildings, automobile storage garages, parking lots, and tourist camps.

ADMINISTRATION

The Transaction Privilege Tax, Educational Excise Tax, and the Special Excise Tax for Education are paid to the Department of Revenue by various businesses. Any person or business receiving income or proceeds from a sale upon which a Transaction Privilege Tax is levied must have a privilege tax license. This license is available from the Department of Revenue for one dollar. The license is valid for five years unless the ownership or location of the business changes.

Collections for the three taxes that make up the sales tax are remitted on a monthly basis. They are due and payable on or before the 15th day of the month following the month in which the tax accrues. The tax is delinquent five days later. Extensions of up to 60 days may be granted by the Department of Revenue for good cause. The laws of Arizona provide penalty and interest provisions for failure to file a tax return or for failing to remit the proper amount. The statutes also outline administrative procedures for contesting the tax liability.

The Use Tax is paid by the persons making retail purchases of tangible personal property in other states that have lower, or no sales tax. The Department of Revenue collects the tax revenue on or before the 15th day of each month, and credits fifty percent of the revenue to the Use Tax receipts fund and fifty percent to the Education Excise Tax fund. At the end of the calendar month all monies in the Use Tax receipt fund are deposited to the General Fund.

The Rental Occupancy Tax is paid by the landlords, who collect the tax from the tenant together with the rent of any tenant from whom no tax has been collected. These taxes are remitted to the Department of Revenue on or before the last day of each month.

Sales and use taxes are also levied by various cities and towns at rates set by their respective governing bodies. Counties do not have the statutory authority to impose such taxes. In 1973, Proposition 300 authorized the Department of Revenue to administer the sales tax program of any Arizona city or town on a contract basis. This service is performed by the Department without charge to the cities. In 1977-78, $16.1 million was collected on behalf of 40 cities and towns.

INCIDENCE

The incidence of sales and use taxes varies by taxable activity, tax rate, percentage of income spent on particular commodities, and income group. The incidence of the tax will increase as the portion of household income spent on the taxable commodity increases.

The Use Tax is imposed to avoid the loss of business and resultant tax revenue that would occur if there were differences in tax rates within a market area.

The incidence of the Rental Occupancy Tax was statutorily shifted to the tenant.

COLLECTIONS

Table V-2 has been prepared to show the collections from the three tax sources normally referred to as the sales tax. The revenue is shown by taxable activity and includes penalty, interest, and licenses fees. The amounts shown are not collections after refunds.

COLLECTIONS BY CLASSIFICATION FOR 1977-78

TAXABLE ACTIVITY	TRANSACTION PRIVILEGE TAX	EDUCATION EXCISE TAX	SP. EXCISE TAX FOR EDUCATION	COMBINED TAX
Mining - Oil and Gas Production	$ 11,744,222	$ 5,872,111	$ 11,744,222	$ 29,360,555
Transporting and Towing	39,420	39,420	78,840	157,680
Utilities	11,155,771	11,155,771	22,311,542	44,623,084
Communications	3,355,066	3,355,066	6,710,132	13,420,264
Railroads and Aircraft	201,218	201,218	402,436	804,872
Publishing	1,312,945	1,312,945	2,625,890	5,251,780
Printing and Advertising	1,396,057	1,396,057	2,792,114	5,584,228
Private Car, Pipelines	17,706	17,706	35,412	70,824
Contracting	17,263,856	17,263,856	34,527,712	69,055,424
Timbering	735,444	367,722		1,103,166
Restaurants and Bars	18,303,688	18,303,688		36,607,376
Amusements	2,003,279	2,003,279		4,006,558
Rentals of Real Property	17,144,577	8,572,288		25,716,865
Rental of Personal Property	2,434,706	2,434,706		4,869,412
Feed Wholesale	366,963	183,482		550,445
Retail	158,232,519	158,232,519		316,465,038
	$245,707,437	$230,711,834	$ 81,228,300	$557,647,571
*Use Tax		8,577,759		8,577,759
Subtotal	$245,707,437	$239,289,593	$ 81,228,300	$566,225,330
Adjustment			(171,774)	(171,774)
Penalty and Interest Collected	1,834,638	1,273,730		3,108,368
Licenses, fees collected	28,179			28,179
TOTAL	$247,570,254	$240,563,323	$ 81,056,526	$569,190,103

Source: Department of Revenue

*Represents one-half of Use Tax collections dedicated to the Education Excise Tax.

In order to see more clearly the total effect of the sales and use taxes which are being discussed in this section, Table 3 has been prepared which incorporates the Use Tax and the Rental Occupancy Tax. This table also compares the 1977-78 collections with amounts collected 10 years ago or 1967-68.

TABLE V-3

Sales Tax Collections
1967-68 and 1977-78

Source	1967-68	1977-78
Transaction Privilege	$ 68,564,160	$247,570,254
Education Excise	35,007,281	240,563,323
Special Education	2,057,752	81,056,526
Use*	769,748	8,577,759
Rental Occupancy**		169,562
SUBTOTAL	$106,398,941	$577,937,424

*an equal amount is accounted for in the Education Excise Tax Fund.
**effective 1-1-1975.

As previously noted, the Transaction Privilege Tax revenue is shared with cities, towns, and counties. The Education Excise Tax and the Special Excise Tax for Education revenues are not shared. 25% of the Transaction Privilege Tax collection is distributed to the various municipalities in the state in proportion to their population. 4% is earmarked for the Department of Revenue's License Fee and Privilege Tax Administration fund, and 15% is earmarked for the Department of Economic Security, to be used for public welfare programs. The State General Fund is allocated 22.4% and 33.6% goes to the counties.

The revenue is distributed to the counties based upon the average that the percentage of assessed valuation bears to the total state assessed valuation, and the percentage that the Transaction Privilege Tax revenues collected in the county bears to the total state Transaction Privilege Tax revenues. This allocation formula results in the distribution of 41.4% of the revenue to the state, 33.6% to the county and 25% to the cities and towns. For 1977-78 the distribution was as follows:

TABLE V-4

Distribution of State Transaction
Privilege Tax Collections

General Fund*	$432,761,892
Counties	83,240,578
Cities	61,934,954
TOTAL	$577,937,424

*The Education Excise Tax of $240,826,672 is earmarked for education.

a. Distribution of Transaction Privilege Tax Revenues to the State

The following table shows the components of the Privilege Tax revenues as percentages of total state revenue:

TABLE V-5

Transaction Privilege Tax Revenues As
a Percentage of Total State Revenue, 1978

Tax	Amount	Percent of Total** State Revenues
Transaction Privilege Tax	$247,570,254	16.7%
Education Excise Tax	240,563,322	16.2
Special Education Excise Tax	81,056,526	5.5
Use Tax*	8,577,759	0.6
Rental Occupancy	169,562	0.01

*One-half of the Use Tax is earmarked for the Education Excise Tax fund. In total, $17,155,518 was collected for tangible personal property purchased outside the state.

**Total state revenues here include all state general and special revenue and aid collections of $1,482,291,323. Source DOR annual report.

b. Distribution of State Transaction Privilege Taxes to Counties

The 1977-78 allocation of $83,240,578 for counties was distributed as follows:

TABLE V-6

Distribution of State Transaction Privilege Taxes to Counties

Apache County	$ 556,930
Cochise County	2,145,803
Coconino County	3,363,605
Gila County	1,742,998
Graham County	540,270
Greenlee County	1,626,678
Maricopa County	44,139,149
Mohave County	2,028,230
Navajo County	2,252,406
Pima County	15,832,025
Pinal County	3,671,236
Santa Cruz County	567,424
Yavapai County	2,200,116
Yuma County	2,573,707
TOTAL	$83,240,578

The revenue from the Transaction Privilege Tax is required by statute to be used to retire county bonds and pay outstanding warrants. If there is a surplus, the money may then be credited to the general fund of the county. In preparation of the budget, each county board of supervisors includes an estimate of expected sales tax revenues. Any obligation paid from the tax revenues must be a specific item of the county's budget. The Transaction Privilege Tax revenues represent an average of 17% of each county's revenues. (Source: Arizona Association of Counties)

Distribution of Sales Tax Collections for 1977-78

COUNTY/ CITY-TOWN	AMOUNT	% TO TOTAL DISTRIBUTION*
APACHE		
Eagar	$ 73,165.14	.118
Springerville	42,902.29	.069
St. Johns	68,546.52	.111
COCHISE		
Benson	127,261.57	.205
Bisbee	310,570.28	.501
Douglas	464,673.68	.750
Huachuca City	63,050.47	.102
Sierra Vista	750,271.63	1.211
Tombstone	46,266.10	.075
Willcox	100,833.96	.163
COCONINO		
Flagstaff	1,169,727.42	1.889
Fredonia	29,748.10	.048
Page	219,703.18	.355
Williams	88,958.59	.144
GILA		
Globe	273,432.61	.442
Hayden	47,840.93	.077
Miami	126,575.57	.204
Payson	107,763.54	.174
Winkelman	36,332.51	.059
GRAHAM		
Pima	53,760.23	.087
Safford	221,751.68	.358
Thatcher	106,865.65	.173
GREENLEE		
Clifton	189,688.01	.306
Duncan	28,819.08	.047
MARICOPA		
Avondale	247,066.94	.399
Buckeye	96,905.62	.156
Chandler	747,015.55	1.206
El Mirage	145,737.47	.235
Gila Bend	66,936.24	.108
Gilbert	134,341.46	.217
Glendale	2,509,397.42	4.052
Goodyear	87,286.37	.141
Guadalupe	159,796.75	.258
Mesa	3,757,244.83	6.066
Paradise Valley	340,121.10	.549
Peoria	289,283.29	.467
Phoenix	24,945,760.43	40.277

COUNTY/ CITY-TOWN	AMOUNT	% TO TOTAL DISTRIBUTION*
MARICOPA cont.		
Scottsdale	$ 2,910,865.60	4.700
Surprise	123,866.67	.200
Tempe	3,500,666.37	5.652
Tolleson	144,722.53	.234
Wickenburg	108,406.19	.175
Youngtown	70,316.18	.114
MOHAVE		
Kingman	290,129.00	.468
NAVAJO		
Holbrook	189,924.29	.307
Showlow	125,960.91	.203
Snowflake	95,941.11	.155
Taylor	55,985.20	.090
Winslow	300,765.24	.486
PIMA		
Marana	54,813.12	.089
Oro Valley	43,950.52	.071
South Tucson	231,935.48	.374
Tucson	11,336,961.79	18.305
PINAL		
Casa Grande	507,040.33	.819
Coolidge	250,244.95	.404
Eloy	242,112.15	.391
Florence	109,095.30	.176
Kearny	105,498.40	.170
Mammoth	76,138.02	.123
Superior	187,463.02	.303
SANTA CRUZ		
Nogales	337,930.85	.546
Patagonia	23,492.66	.038
YAVAPAI		
Chino Valley	75,332.91	.122
Clarkdale	39,800.89	.064
Cottonwood	133,857.47	.216
Jerome	10,812.19	.017
Prescott	629,725.54	1.017
YUMA		
Parker	72,634.25	.117
Somerton	115,443.47	.186
Wellton	36,053.98	.058
Yuma	1,121,665.20	1.811
TOTAL	$61,934,953.93	100.000%

*The percentage of revenue received by each city or town is based on population.

CRITERIA

1. Revenue Generation:

   a. Will revenues from the sales tax expand as the demand for government services expands?

      The sales tax is a good source of increased revenue during periods in which the population of the state is experiencing significant growth.

      Individuals moving into the state will expect to receive the same government services that are currently provided to residents of the state. This will increase the revenue requirements of the government. Individuals moving into the state will also expend significant sums of money to purchase products sold by Arizona businesses. Because these additional sales will increase the taxable receipts of businesses, the revenues from the sales tax will expand to meet the additional revenue requirements of the government.

      However, if the demand for government services (welfare, unemployment, etc.) is increasing due to a decline in the level of economic growth, the sales tax may not be a good source of increased revenues, since individual purchases will ordinarily decline if personal income is reduced.

   b. Will revenues from the sales tax expand as the price of government services increase?

      A general increase in the price of goods will result in an increase in government expenditures in order to maintain current levels of services. Because the sales tax is levied on the gross receipts from the sale of goods, a general increase in the price of goods will also result in an increase in the revenues produced by the sales tax.

2. Social Equity:

   a. Is the sales tax affordable from current cash flow?

      The sales tax is effectively paid by individuals in the form of increased prices for goods at the time of purchase. Thus, if the taxpayer has sufficient income available to purchase taxable commodities, the sales tax will be paid from current cash flow at the time the purchase is made. If income is not available to pay the full price of taxable items with the tax included, the individual may limit his purchases and thereby avoid tax liability. However, if the taxpayer is unable to limit his purchases of goods beyond a basic minimum amount required for subsistence, he will be subject to the tax on this amount regardless of his income or the hardship which this liability may represent.

b. Is the sales tax borne by individuals with common circumstances equivalent?

The state sales tax rate on any given item is consistent throughout the state. Thus, individuals who purchase the same types of commodities in comparable quantities will pay equivalent state sales taxes. The total sales tax burden may differ for individuals whose purchases are similar, however, because of differences in the sales tax rate levied on selected commodities by local jurisdictions.

c. Will individuals who receive greater benefits from government services pay greater sales taxes?

Because sales taxes are not earmarked for particular government services, it is difficult to determine to what extent individuals who pay the tax benefit from government services provided.

3. Ease of Administration:

Can the sales tax base be determined without difficulty?

The sales tax is based on the gross selling price of a commodity. The tax is effectively paid at the time of sale. Because the price of commodities is fixed prior to sale, a direct measure of the value of the tax base is available at the time the tax is paid.

4. Consistency with State Goals:

a. Is a substantial portion of the sales tax paid by the residents of other states?

The sales tax is effectively paid by individuals in the form of increased prices for goods at the time of purchase. Non-residents who visit the State of Arizona will pay sales taxes on all taxable items that they purchase from businesses within the state during their stay. In 1977-78, state sales tax revenues attributed to non-resident tourists were estimated at $96,700,000.

b. Will the sales tax produce revenues without detrimentally affecting business?

Because the sales tax is paid from the gross receipts of taxable businesses, the tax could have a negative impact on the growth of business if it cannot be passed to individuals in the form of a price increase or otherwise recovered through a reduction in costs.

SECTION SIX

INCOME TAX

The income tax is designed to extract revenues from individuals and corporations in Arizona, based upon their level of taxable income, for the purpose of funding the general operations of state government. Generally speaking, all individuals and corporations must pay income taxes to the State of Arizona based upon that portion of their income that is derived from taxable sources within the state.

Historical Overview

The first income tax in Arizona was enacted by the Eleventh Legislature in 1933. Chapter 39, Laws of 1933, imposed the income tax and stated the object of the newly imposed tax. The object of the original tax and the purpose for its imposition as stated in Section Three of the 1933 act are as follows:

> "The object for which the said tax is imposed is to assist in defraying the cost of maintenance of the State Government, and to lessen the burden in this regard resting upon tangible property."

It appears that the drafters of this original income tax in Arizona were concerned about the reliance of government on the property tax.

This first income tax imposed different rates upon individuals and corporations, which were subject to the tax. The rate schedule for individuals started at one per cent on the first thousand dollars of net income and progressed to five and one-half per cent on all net income in excess of ten thousand dollars. Corporations were subject to a tax of two per cent on the first one thousand dollars of net income, with the maximum rate of six per cent on all income over six thousand dollars. The tax was repealed shortly after its enactment and replaced with an income tax in which the individual tax rates rose more slowly and stopped at four and one-half per cent, while the overall rates for corporate income were reduced between one-half and one per cent on all levels of income.

Adjustments to the basic income tax code were made until 1954 when the

Income Tax Act of 1933 was repealed and replaced with the Income Tax Act of 1954. The 1954 Act was modeled closely after the Federal Income Tax Code. At the same time, the corporate and individual income tax rates were also increased.

Numerous amendments were made to the "Income Tax Act of 1954" from the time of its enactment through 1978. In 1965 and again in 1967, the income tax rate schedules for both individuals and corporations were changed. The rates for individuals, enacted in 1967, still apply. They range from two per cent on the first thousand dollars of taxable income to eight per cent on all income in excess of six thousand dollars. The Laws of 1974 changed the corporate income tax rates. These rates range from two and one-half per cent on the first thousand dollars of taxable income to ten and one-half per cent on all taxable income in excess of six thousand dollars.

The most recent recodification of the income tax statutes in Arizona occurred in 1978. This law became effective January 1, 1979 and its impact will be felt for the first time during the filing year, 1980. The law provided for a reorganization of the income tax statutes and the adoption of federal adjusted gross income as the starting point for calculating Arizona income tax liabilities. Under the new code, federal adjusted gross income is equal to "Arizona gross income." This is commonly referred to as "piggybacking." Certain adjustments are then made to "Arizona gross income" to compensate for differences between the Federal Income Tax Code and the Arizona Income Tax Code. After these adjustments are made, the resulting amount is Arizona adjusted income, which is fundamentally equivalent to the amount that would have been calculated in the absence of the new law. Thus, the recodification and new filing procedure did not substantially impact upon the nature or intent of the income tax code in Arizona. The legislation also provided for an extension of the optional tax table and the development of a shortened income tax form, both of which would further simplify the filing process for many Arizona residents.

Another recent enactment of particular interest was the passage in 1978 and the extension in 1979, of the "inflation indexing" of the Arizona income tax. The purpose for the legislation was to, at least partially, offset the impact that continued inflation and a progressive income tax structure have on taxpayers. This is accomplished by indexing the standard deduction, personal exemptions and the various tax credits to the consumer price index. In other words, the value of these deductions and credits increases as inflation continues.

Specifically, for the tax year 1978, the standard deduction, the personal exemption, the credit for taxpayers over 65 years of age, the renters' credit, and the credit for dependents, were all increased by a factor of 10.1 per cent. Ten and one-tenth per cent is the amount that the Phoenix Metropolitan Consumer Price Index, as computed by the Bureau of Business and Economic Research at Arizona State University, increased from the second quarter of 1977 to the second quarter of 1978. For example, the impact that the legislation had on the personal exemption was such that it was increased from $1,000 to $1,101.

In addition to the extension of "inflation indexing" for an additional year, several other changes were made to the Arizona Income Tax Code during the 1979 regular legislative session. Chapter 145 provided for the adoption of several changes that were made to the Federal Income Tax Code during 1978 into the Arizona income tax code. Chapter 164, in addition to extending "inflation indexing," provided for the renters' credit to be increased from a base of fifty dollars to seventy-five dollars. Chapter 191 provided for an income tax deduction of up to one hundred dolars for an individual or two hundred dollars for a married couple filing jointly, for contributions made to state and local political campaigns. Chapter 136 clarified the statutory sections relating to solar energy income tax credits and extended the expiration date of those credits by five years, until 1989. Further, the Chapter provided for commercial buildings to qualify for the credit until 1986 and extended the sales tax exemption for solar energy devices until 1989. Chapter 43 increased the allowable end-of-year carryover within the Income Tax Fund from two hundred thousand dollars to five hundred thousand dollars. Chapter 14 conformed the treatment of certain qualified small business corporations, under the Arizona income tax statutes to the treatment provided in the Federal income tax statutes.

Description of the Arizona Income Tax

The Arizona income tax is levied upon individuals and corporations earning income within the State of Arizona. Single individuals with an adjusted gross income in excess of one thousand dollars, or two thousand dollars if married, or whose gross income is in excess of five thousand dollars, are required to file an income tax return with the Department of Revenue.

Fiduciaries are required to file income tax returns on behalf of any individual for which they are responsible if such individual would otherwise have been required to file a return. Fiduciaries are also required to file a return for every estate which has taxable income in excess of one thousand dollars during the tax year; or any trust which has taxable income in excess of one hundred dollars during the tax year; or any trust or estate which has a gross income in excess of five thousand dollars during the tax year. Finally, fiduciaries are responsible for the filing of an income tax return for every decedent, for the year in which death occurred if the decedent would have otherwise been required to file an income tax return. Partnerships are required to file an annual return and the income of the partnership is taxable as if it had been distributed to each of the individuals who are entitled to share in the income of the partnership. Corporations are required to file an annual return regardless of their level of income. Generally, governmental entities and non-profit organizations are exempt from the filing requirements of the Arizona income tax. Additionally, insurance companies subject to the insurance premium tax are exempt from the Arizona income tax. All exempt organizations, with the exception of religious organizations and organizations related to religious or certain educational organizations, are required to file an informational return.

Tax Base

The base used for determining tax liability under the Arizona income tax is net taxable income. Net taxable income is determined by means of several calculations. The first of these calculations is a determination of gross income. In the absence of "piggy-backing" legislation such as was enacted in 1978, the determination of gross income is usually made by inspection of all the various amounts of income received by a taxpayer from various sources. Certain categories of income are includable within gross income and certain categories of income are excludable from gross income.

Once gross income has been determined, adjustments are made to gross income to arrive at "adjusted gross income." The primary purpose these adjustments serve is to allow the partial exclusion or inclusion of certain categories of income . For example, prior to the enactment of the "piggy-backing" legislation in Arizona, military pay was included in the definition of Arizona gross income; however, any military pay received while on active duty, up to one thousand dollars per year, was to be excludable from gross income for tax purposes. Thus, the entire amount of military pay was included as a part of gross income and an adjustment for up to one thousand dollars of active duty pay was allowed.

However, due to the enactment of the "piggy-backing" legislation in 1978, the two steps used to calculate adjusted gross income, are no longer required. Instead, federal adjusted gross income is equal to Arizona gross income. To this amount certain adjustments are then made to compute Arizona adjusted gross income. These adjustments have two purposes. The first purpose is to compensate for types of income that are includable in federal gross income and excludable under the Arizona income tax code _or_ for amounts which are excludable from federal gross income but are includable under the Arizona income tax code. The second purpose is to compensate for differences between the adjustments made to gross income in determining adjusted gross income pursuant to the Federal income tax code and the Arizona income tax code. For example, certain adjustments are allowed under the federal law which have traditionally not been allowed under Arizona law. Such an adjustment would have been used when computing federal adjusted gross income and therefore the amount deducted must be added back when computing Arizona gross income.

A listing of the adjustments that must be made to federal adjusted gross income in order to arrive at Arizona adjusted gross income is provided in Appendix VI-1.

As discussed above, if the "piggy-backing" legislation had not been enacted in 1978, it would be necessary to first determine Arizona gross income, based upon certain includable and excludable types of income, and then compute Arizona adjusted gross income by making certain prescribed adjustments.

In Arizona, gross income is defined as "all income from whatever source derived" except for that which is specifically excluded. In the broad sense, gross income means all wealth which flows in to the taxpayer, other than a mere return of capital or an unrealized appreciation in value. Appendix VI-2 presents a listing of included and exempt sources of income in Arizona.

The next step after determining Arizona adjusted gross income, is the deduction of certain amounts in order to determine net taxable income. These deductions are allowed for certain specified expenses that are incurred by the taxpayer during the tax year. Individual taxpayers have the option of calculating the deductible amount in either of two ways. Individuals may claim the standard deduction or may itemize their deductions. For the tax year 1978, the standard deduction was equal to 11 per cent of Arizona adjusted gross income minus federal income taxes paid and certain other special deductions, up to a maximum of $551 for a single individual or $1,101 for a married couple filing jointly. The standard deduction is one of the amounts impacted by "inflation indexing;" therefore, the amount of the standard deduction is subject to change due to the rate of inflation, as measured by the Metropolitan Phoenix Consumer Price Index.

Appendix VI-3 presents a listing of itemized deductions that are allowed for taxpayers who do not claim the standard deduction.

Tax Rates

Once the allowable amounts, discussed above, have been deducted from Arizona adjusted gross income, the resulting figure is net taxable income. The next step in determining Arizona income tax liability is the application of the appropriate tax rate. Two sets of tax rates exist in Arizona. One is applied to the net taxable income of corporations and the other is applied to the net taxable income of all other persons. The following table shows the income tax rates for both corporate and individual taxpayers.

ARIZONA INCOME TAX RATES

Corporate Tax Rates	Net Income	Individual Tax Rates
2.5%	$0 - 1,000	2.0%
4.0	1 - 2,000	3.0
5.0	2 - 3,000	4.0
6.5	3 - 4,000	5.0
8.0	4 - 5,000	6.0
9.0	5 - 6,000	7.0
10.5	over 6,000	8.0

Tax Credits

The figure that results from the application of the appropriate tax rate to net taxable income is gross tax liability. The next step in determining

Arizona income tax liability is the subtraction of certain allowable credits from gross tax liability in order to determine net tax liability. Net tax liability is the final amount of tax that is levied upon the taxpayer. This is the same amount that individual taxpayers typically compare to the amount that was withheld from wages, in order to determine if they will receive a refund or owe additional tax. Generally speaking, tax credits are granted for the same reason as deductions.

Appendix VI-4 presents a listing of the credits allowed individual taxpayers.

ADMINISTRATION

Income tax returns are required to be filed on or before the fifteenth day of the fourth month following the close of the tax year. All individuals are required to base their tax year on the calendar year and thus are required to file on or before the fifteenth day of April. Corporations may base their tax year on their fiscal year.

The Arizona income tax is administered by the Arizona Department of Revenue, which is responsible for promulgating rules and regulations for its application.

The proceeds of the Arizona income tax are shared with the incorporated cities and towns within Arizona. The amount shared is equal to fifteen per cent of the net proceeds of the income tax, which was collected two years prior to the current fiscal year. This amount is annually deposited into the Urban Revenue Sharing Fund and distributed among the incorporated cities and towns within the state, based upon population. Additionally, sixteen per cent of the gross proceeds of the income tax are annually deposited into the State Income Tax Fund. The amounts within this fund are used to pay refunds and adjustments. All amounts in the State Income Tax Fund in excess of five hundred thousand dollars at the end of each fiscal year are deposited into the State General Fund. Aside from the deposits into these two funds, all collections from the income tax are deposited into the State General Fund.

During fiscal year 1977-78, the income tax resulted in net deposits to the State General Fund of $254,741,577 and distributions to the incorporated cities and towns within the state of $31,405,355. The amount deposited into the State General Fund was equal to approximately thirty per cent of all revenues received in the State General Fund or approximately eighteen per cent of all revenues received by the state.

INCIDENCE

When examining any tax, it is important to analyze the incidence of that tax on taxpayers. Generally speaking, the incidence of a tax is meant to indicate exactly what individuals or groups bear the ultimate burden of the tax.

The income tax on individuals is designed to impact more heavily on high income individuals than on low income individuals. The final incidence of the income tax on individuals, of course, rests with the individuals legally responsible for the tax.

The final incidence of the corporate income tax is not as clear. Three major alternatives exist with respect to the incidence of the corporate income tax. The burden of the corporate income tax can be passed along to the consumers of the corporation's products in the form of higher prices. Alternatively, the incidence of the corporate income tax may be borne by the shareholders of the corporations's stock, in the form of lower dividends; or the corporation may reduce its retained earnings as a result of being required to pay the corporate income tax. A reduction in retained earnings ultimately impacts upon the holders of the corporation's stock. A firm may also attempt to recoup the tax by reducing its total wage bill through lay-offs or reduced work weeks.

CRITERIA

1. Revenue Generation:

   a. Will revenues from the income tax expand as the demand for government services expands?

      The income tax is a good source of increased revenues during periods in which the population of the state is experiencing significant growth.

      Individuals moving into the state will expect to receive the same government services that are currently provided to residents of the state. This will increase the revenue requirements of the government. Individuals moving into the state will also receive earnings which will add to the income tax base. Thus, income tax revenues will increase to meet the additional requirements of the government.

If the demand for government services (welfare, unemployment, etc.) is increasing due to a decline in the level of economic growth, however, the income tax will be a poor source of additional revenues, since a decline in personal income will result in fewer income tax receipts.

b. Will revenues from the income tax expand as the price of government services increases?

A general increase in the level of prices will ordinarily result in a demand for increased wages. As the level of wages increases, the income tax base will expand producing additional revenues. These revenues can then be used to pay for the increased cost of providing government services which also will result from increases in the price level.*

2. Social Equity:

a. Is the income tax affordable from current cash flow?

The income tax is based on the level of income received by the individual. Because a percentage of income is withheld from each individual's paycheck at the time of receipt, the bulk of the individual's total tax liability is automatically paid from current cash flow.

b. Is the income tax borne by individuals with common circumstances equivalent?

Because income is generally regarded as a fairly good measure of circumstance and individuals falling within the same income range are taxed at the same rate if they have similar deductions, it is safe to assume that individuals with common circumstances have roughly equivalent income tax burdens.

c. Will individuals who receive greater benefits from government services pay greater income taxes?

Because income taxes are not earmarked for particular government services, it is difficult to determine to what extent individuals who pay the tax benefit from government services provided.

3. Ease of Administration:

Can the income tax base be determined without difficulty?

The gross income received by individuals is relatively easy to verify because of the requirement that a W-2 form showing wages paid by each employer be included with each income tax form filed. Income received by individuals other than wages may be more difficult to verify, however. The accuracy of amounts claimed as deductions, credits, etc. may also be difficult to determine.

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*It should be noted, however, that the inflation tracking ability of the income tax has been reduced somewhat due to inflation indexing.

4. Consistency with State Goals:

   a. Is a substantial portion of the income tax paid by residents of other states?

      Non-residents are taxed on income only to the extent that that income was derived from sources within the state.

      Corporate income taxes represent an added cost to business. In order to cover this additional cost, businesses may reduce purchases of supplies or wages paid to employees; they may raise the price of goods and services provided; or they may reduce the profits or dividends available to owners and shareholders. Thus, firms which are owned by out-of-state residents, which purchase supplies from out-of-state vendors and which produce a good or service consumed in whole or in part out of state, will provide the best opportunity to export the income tax.

   b. Will the income tax produce revenues without detrimentally affecting business?

      Corporate income taxes are paid directly from the proceeds of businesses. The ability of commercial properties to pass the income tax to others is dependent upon the demand for and supply of the good or service provided. If the sales of the good or service are sufficient to cover all costs of production including the cost of paying income taxes, there will be no detrimental effect to business.

APPENDIX VI-1

ADJUSTMENTS TO FEDERAL ADJUSTED GROSS INCOME TO ARRIVE AT ARIZONA ADJUSTED GROSS INCOME

I. INDIVIDUALS

A. Additions to federal adjusted gross income.

1. The dividend exclusion which is allowed by the internal revenue code. ($100 single, $200 joint return)

2. Moving expenses when moving into or out of the State (moving expenses incurred on moves within the State need not be added back).

3. A beneficiary's share of trust or estate income when the trust or estate has subtracted the amount from its Arizona gross income. Also those amounts of trust or estate income which are allowed as deductions by the internal revenue code. (reference subtraction number 4).

4. The amount of gain related to an outstanding installment receivable, which had not previously been recognized as income, upon the death of the taxpayer (reference subtraction number 23).

5. The income that must be recognized due to a difference between the loss carryover computed under the Arizona code and the federal loss carryover upon the effective date of the Arizona income tax act of 1978 (reference subtraction number 23).

6. The interest income received from bonds and other obligations of political subdivisions of the United State, which are located outside of Arizona.

7. Federal income tax refunds that were part of the federal income tax deduction on the Arizona return in a previous year.

8. The income that must be recognized due to a difference in the adjusted basis of depreciable property computed under the Arizona code and the federal code upon the effective date of the Arizona income tax act of 1978 (reference subtraction number 11).

9. The amortization of pollution control devices, solar energy devices, and child care facilities, deducted pursuant to the federal code when the taxpayer elects to amortize over a period of 5 years for purposes of the Arizona income tax (reference subtraction number 14).

10. The amount by which the adjusted basis of nondepreciable property computed pursuant to the internal revenue code exceeds the adjusted basis computed pursuant to the Arizona code upon the sale of the property (reference subtraction number 13).

11. The "ordinary income" portion of a lump sum distribution of certain annuity plans which was excluded from federal adjusted gross income.

(Ordinary income = (taxable amount of distribution X $\frac{\text{no. years in plan since 12/31/73}}{\text{total number of years in plan}}$)

12. The portion of military active duty pay which is exempted income by the internal revenue code (certain pay while in a combat zone, while hospitalized because of service in a combat zone, or while in a missing or prisoner of war status).

13. Net operating losses taken pursuant to the internal revenue code (subtracted according to different rules under the Arizona code, reference subtraction number 9).

14. Annuity income received during the taxable year which, along with all benefits received in all tax years, was in excess of the taxpayer's total contributions to the plan (applies only to those annuities with respect to which the first payment was received prior to December 31, 1977, reference subtraction number 14).

15. The excess of a partner's share of partnership income as defined by the Arizona code over the income as defined by the internal revenue code (reference subtraction number 16).

16. The excess of a partner's share of partnership losses as defined by the internal revenue code over the losses as defined by the Arizona code (reference subtraction number 17).

17. The percentage depletion deduction taken pursuant to the internal revenue code (subtracted according to different rules under the Arizona code, reference subtraction number 18).

18. Deferred exploration expense, determined pursuant to the internal revenue code, that exceeds $75,000 when the election has been made to defer those expenses not in excess of $75,000 (subtracted on a ratable basis later as the ores or minerals are sold, reference subtraction number 19).

B. Subtractions from federal adjusted gross income.

1. The exemptions for blind persons ($500 base), persons over 65 ($1,000 base) and dependents ($600 base).

2. Contributions made to, and the benefits of the state retirement system, state retirement plan, judge's retirement fund, public safety personnel retirement system, or a county or city retirement plan.

3. Annuity income from the U.S. civil service retirement system retirement and disability fund, up to a maximum of $2,500.

4. A beneficiary's share of trust or estate income recognized by the internal revenue code (reference addition number 3).

5. Distributions from an individual retirement account or a similar qualifying retirement plan equal to the total contributions made to the plan prior to December 31, 1977, which were included in computing Arizona taxable income.

6. The first $1,000 of compensation received by an individual for his services as a member of the armed forces (includes reserves, national guard, etc.)

7. Interest income from U.S. government obligations.

8. Federal income taxes withheld, paid or accrued during the taxable year.

9. Net operating loss carryovers computed pursuant to the Arizona code (reference addition number 13).

10. The amount of any income tax refunds received from states other than Arizona which was included in federal adjusted gross income.

11. The amount by which the Arizona adjusted basis of depreciable property exceeds the federal adjusted basis upon the effective date of the Arizona income tax act of 1978 (reference addition number 8).

12. Deferred exploration expenses that were added to Arizona gross income may be subtracted on a ratable basis as the ores or minerals are sold.

13. The amount by which the adjusted basis of nondepreciable property computed pursuant to the Arizona income tax code exceeds the adjusted basis computed pursuant to the internal revenue code upon the sale of the property (reference addition number 10)

14. The cost of solar energy devices, pollution control devices, and child care facilities amortized over five years (reference addition number 9).

15. Annuity income included in federal adjusted gross income pursuant to the internal revenue code if the first payment from the annuity was received prior to December 31, 1977. (The federal code governing the treatment of annuity income differs from the Arizona code, this subtraction plus addition number 14 effectively taxes the income received that exceeds the contributions made by the taxpayer.)

16. The excess of a partner's share of partnership income as defined by the internal revenue code over the income as defined by the Arizona code (reference addition number 15).

17. The excess of a partner's share of partnership losses as defined by the Arizona code over the losses as defined by the internal revenue code (reference addition number 16).

18. The percentage depletion allowance that is permitted under the Arizona code. The percentage allowed varies with the type of mineral or ore being mined (reference addition number 17).

19. The amount of expense and expense recapture included in income pursuant to the internal revenue code for mine exploration expense (addition number 18 and subtractions numbers 12, 18 and 19 reject federal treatment of exploration expense and establish Arizona's code on their treatment for income tax purposes).

20. The expenses and depletion connected with the development of geothermal resources.

21. The amount of income from a "domestic international sales corporation" included in the income if its shareholders pursuant to the internal revenue code (taxed as corporate income pursuant to the Arizona code).

22. The amount of retired or retainer pay received after December 31, 1977 and all amounts received as benefits of the survivor benefit plan or the retired serviceman's family protection plan by a retired member of the uniformed services or his survivor, to the extent that Arizona income taxes were paid on the amount of the reduction in the participant's retirement or retainer pay due to participation in either plan.

23. The gain realized on an installment receivable upon the death of a taxpayer which has already been recognized (reference addition number 4).

24. The difference between capital loss carryovers computed pursuant to the Arizona code and the internal revenue code when the Arizona carryover is larger (reference addition number 5).

II. CORPORATIONS

A. Additions to Federal Adjusted Gross Income.

1. Additions to Arizona gross income - individuals, items 6 through 10 and 13 through 18.

2. The amount of dividend income received from domestic corporations which the internal revenue code allows as a deduction. The deduction can vary from approximately 60% to 100% depending upon the ownership and nature of the business, and the type of dividend.

3. Income taxes paid to other states, local governments, and foreign governments which were deducted in computing federal taxable income.

4. Charitable contributions as defined by the internal revenue code (subtracted according to different rules under the Arizona code, reference subtraction number 3).

5. Expenses, that would otherwise be deductible, which were incurred by financial institutions in the production of tax-exempt income. The amount of the non-deductible expense is calculated pursuant to a formula included in the Arizona code which proportions expenses according to type of income received (reference subtraction number 6).

6. Amounts paid to a domestic international sales corporation which is controlled by the payor corporation if the domestic international sales corporation is not required to report its taxable income to the state because its income is not attributable to the state.

B. Subtractions from Federal Adjusted Gross Income.

1. Subtractions from Arizona gross income - individuals, items 7 through 21.

2. The dividend income received from Arizona corporations.

3. Charitable contributions as defined by the Arizona income tax code (reference addition number 4).

4. The amount of a capital loss carryover computed according to the Arizona code, not to exceed $1,000.

5. The amount of the foreign tax credit, allowed by the internal revenue code, used to offset the federal income tax liability.

6. The amount of expenses relating to tax-exempt income as calculated pursuant to the internal revenue code (reference addition number 5).

7. Dividends received from a corporation that is controlled by the recipient corporation.

SOURCES OF INCOME SUBJECT TO INCOME TAX AND EXEMPT SOURCES OF INCOME

A. INCLUDED SOURCES OF INCOME

1. Compensation for services - includes wages, salaries, commissions, bonuses, termination or severance pay, rewards, jury fees, tips, pensions, retirement pay, fees, compensation based on a percentage of profit, prizes, awards, distributions from employee trusts, and compensation for children's services;

2. Gross income derived from business - generally means total sales less the cost of goods sold, plus any other "outside" income;

3. Gains derived from dealing in property - the gain on the sale or exchange of property (both tangible and intangible) is generally the excess of the amount realized over the cost or adjusted basis of the property;

4. Interest income - includes interest on savings or bank deposits, coupon bonds, open accounts, promissory notes, mortgages, corporate bonds and debentures, condemnation awards, legacies, life insurance proceeds, refunds of federal taxes, and usurious interest;

5. Rents - includes rentals received or accrued for the rental of real or personal property;

6. Royalties - includes royalty receipts from books, stories, plays, copywrights, trademarks, formulas, patents, and from the exploitation of natural resources;

7. Alimony and separate maintenance payments - these payments are generally included in the gross income of the recipient;

8. Annuities - generally, all annuity payments constitute gross income, including annuities paid by religious, charitable and educational corporations;

9. Income from life insurance and endowment contracts - generally included except for death benefits;

10. Income from discharge of indebtedness - income may be realized when a taxpayer's indebtedness is discharged, the discharge of indebtedness may take the form of a realized gain or compensation;

11. Distributive share of partnership gross income - includes the net amount of gross income that a partner must recognize based upon his ownership percentage or other agreement;

12. Income in respect of a decedent - gross income items must be recognized by the recipient if they are not properly includible in the decedent's gross income;

13. Income from an interest in an estate or trust - distributions from an estate or trust are includible in the gross income of the recipient.

14. Dividends - Gross income includes cash dividends, dividends in kind, stock dividends, stock redemptions. In certain cases, dividends will include a distribution of stock or right to acquire stocks.

15. Pensions and retirement pay - Pensions and retirement allowances paid by Government or private persons are not included in gross income when the taxpayer did not contribute to the pension or the cost of the pension was not deductible to the employer.

B. EXCLUSIONS FROM GROSS INCOME

1. Certain Death Benefits - The law excludes from gross income death benefits paid under a private life insurance contract and death benefits up to $5,000 paid under a life insurance contract of an employer for employees.

2. Gifts and Inheritances - The value of property acquired by gift, bequest, devise or inheritance is excludable in reporting gross income.

3. Compensation for Injuries or Sickness - The law excludes from gross income amounts received from accident or health insurance, or workmen's compensation as compensation for personal injuries or sickness plus amounts received for damages for such injuries or sickness. Under certain limitations gross income will not include amounts received under accident or health plans.

4. Contributions by an Employer to Accident and Health Plans - Gross income does not include contributions by the employer to accident or health plans for compensation (through insurance or otherwise) to his employees for personal injuries or sickness.

5. Rental Value of Parsonages - The law excludes the rental value of a home or the rental allowance provided to a minister as part of his compensation.

6. Income from Discharge of Indebtedness - No amount is included in gross income by reason of discharge of indebtedness if the indebtedness was incurred or assumed by a corporation or by an individual in connection with property used in his trade or business.

7. Improvement by Lessee on Lessor's Property - Gross income does not include income, other than rent, derived by a lessor of real property upon the termination of a lease representing the value of property attributable to improvements made by the lessee.

8. Income Taxes Paid by Lessee Corporation - If a lessee corporation pays income taxes imposed on the lessor, the lessor shall not include the amount of payment in gross income.

9. Recovery of Bad Debts, Prior Taxes, Delinquency Amounts - A taxpayer may exclude from gross income amounts received attributable to a recovery during the tax year of a bad debt, prior tax, or delinquency amount, to the extent of the recovery exclusion of such debt, tax or amount.

10. Income of State, Municipalities, Etc. - Income derived from any public utility or the exercise of any essential governmental function occurring to the Federal government or any state and political subdivision of the state or Federal government.

11. Scholarship and Fellowship Grants - Subject to various provisions, an individual's gross income need not include amounts received under scholarships and fellowships. The amount excluded is limited to an amount equal to $300 times the number of months the fellowship or scholarship is in effect.

12. Contributions to the Capital of a Corporation - Any amount of money or other property received from any person by a regulated public utility which provides water or sewage disposal services is not included in the gross income of the corporation. The contribution is subject to certain requirements.

13. Meals or Lodging Furnished for the Convenience of the Employer - The employee may exclude from gross income the value or amount of any meal or lodging furnished to him for the convenience of the employer, if the meals are furnished on the premises and the lodging is required as a condition of employment.

14. Amounts Received under Qualified Group Legal Services Plan - Gross income of an employee, spouse or his dependents does not include amounts contributed by an employer on behalf of the employee for qualified group legal services plan or the value of legal services provided or paid for under the plan.

15. Gain from the Sale or Exchange of Residence of An Individual 55 Year or Older - At the election of a taxpayer, who has attained the age of 55 years, a one time exclusion from gross income is allowed of up to $100,000 of the profit resulting from the sale of a personal residence, under certain conditions.

16. Certain Reduced Uniformed Services Retirement Pay - In the case of a member or former member of the uniformed services of the United States, gross income does not include the amount of any reduction in his retired or retainer pay.

17. Amounts Received Under Insurance Contracts for Certain Living Expenses - Gross income does not include those amounts provided by an insurance contract for living expenses of a person whose principla residence was destroyed by fire, storm or other casualty.

18. Welfare and Retraining Programs - General benefit payments made to individuals under the Area Redevelopment Act or Manpower Development and Training Act of 1962 are not included in the gross income of the recipient. Also excluded are certain benefits received under Social Security, Disaster Relief Act, Housing and Community Development Act, and Medicare benefits.

19. Unemployment and Layoff Benefits - Unemployment compensation is taxable to a single taxpayer with income over $20,000 and married taxpayers filing a joint return with income over $25,000. The amount of unemployment compensation includible in income would be the lesser of the unemployment compensation received or one half of the amount by which the taxpayer's income exceeds the above limits.

20. Veterans Compensation and Benefits - Certain veterans benefits are not included in gross income. These include educational benefits, mustering out pay and compensation received for injuries incurred while serving in a combat zone.

21. Retirement Benefits - Retirement benefits of certain programs are excluded from gross income.

C. OTHER ADJUSTMENTS

1. Trade or Business Deductions - All ordinary and necessary expenses attributable to trade and business. This deduction does not include the items noted in the deduction employees business expenses. See A.R.S. 43-1054.

2. Trade or Business Deductions for Employees - Expenses incurred by an employee in carrying out his business. This adjustment is handled as a deduction under A.R.S. 43-1055.

3. Long-Term Capital Gains - This adjustment was further adjusted under A.R.S. 43-1025 relating to net operating loss. The amount allowed as a deduction from the loss in the sale or exchange shall not exceed the amounts includible from such sales or exchanges.

4. Losses from Sale or Exchange of Property - A deduction is allowed for the losses realized from the sale or exchange of property. See A.R.S. 43-1025, paragraph 5.

5. Deductions Attributable to Rents and Royalties - Certain amounts are deductible relating to the expenses and losses incurred to property held for the production of rents and royalties.

6. Certain Deductions of Life Tenants and Income Beneficiaries of Property - Certain depletion and depreciation deductions are allowed for life tenants of property and income beneficiaries of an estate or trust. See A.R.S. 43-1027 and A.R.S. 43-1021, paragraph 17.

7. Pensions, Profit Sharing, Annuity and Bond Purchases Plans of Self-Employed Individuals - Various deductions are allowed for contributions made on behalf of certain employees to the pension, profit sharing, annuity and bond purchase plans of self-employed individuals.

8. Moving Expenses Deduction - Certain expenses may be deducted from gross income. A.R.S. 43-1021, paragraph 2, adds to Arizona gross income the moving expenses for persons moving in and out of the state to the extent that the expenses deducted in computing federal adjusted gross income exceed the reimbursement for such expenses included in federal adjusted gross income.

9. Pension, Profit Sharing Annuity and Stock Bonus Plans of Small Business Corporations - A deduction of the excess of amounts included in gross income as part of the payments to such plans over the payments which were made after the person no longer belongs to the plan.

10. Retirement Savings - Deductions are allowed for certain retirement savings.

11. Lump Sum Deduction - Certain portions of lump sum distributions from pension plans may be deducted.

12. Penalties Forfeited Because of Premature Withdrawal of Funds from Time Savings Accounts or Deposits - Various deductions are allowed due to losses incurred from transactions entered for profit, although not connected with business or made to the extent that such losses include amount forfeited due to premature withdrawal from time savings accounts or deposits.

13. Alimony - Taxpayer may deduct alimony payments included in the gross income of his former spouse subject to certain limitations.

APPENDIX VI-3

ITEMIZED DEDUCTIONS FROM ADJUSTED GROSS INCOME

A. DEDUCTIONS

1. Optional Standard Deduction (43-1041) - The law allows elective deductions of $500 if adjusted gross income is $5,000 or more; 10% of the taxpayer's adjusted gross income if it is under $5,000; two times 10% of one-half of the total adjusted gross income of both joint taxpayers if it is less than $10,000; $1,000 on a joint return if the gross income if $10,000 or more.

2. Interest (43-1042) - 100% of the interest paid or accrued on indebtedness may be deducted from gross income. However, the deduction will not be allowed on interest connected with indebtedness on non-taxable income.

3. Taxes (43-1043) - The law allows a deduction from gross income for taxes or licenses paid or accrued during the year. The deductions will not include:

a) Income taxes imposed by any other state, country or territory (other than Arizona);
b) Estate, inheritance, legacy, succession, and gift tax;
c) Taxes tending to increase the value of property, such as street improvement taxes, except in cases where the improvement is for the entire district;
d) Employee contributions to social security, railroad retirement, and self employment contributions; amounts levied for old age, survivors, disability, and hospital insurance;
e) Sales taxes on items purchased (provided the tax is separately stated at the time of purchase) if the item is not purchased in connection with the consumer's trade or business.

4. Deduction for Casualty Losses (43-1044) - Losses of property by an individual due to casualty or theft and not connected with the property of a trade or business are deductible. The loss deductible is determined by the excess adjusted basis of the property over the amount realized from the property.

The "amount realized" is the sum of the amount received from the disposition of the property plus the fair market value of the property. The "adjusted basis" of the property is the cost of the property altered by certain factors depending on the particulars of the property.

5. Wagering Losses (43-1045) - The losses from wagering are deductible to the extent of the gains of the wagering.

6. Contributions and Gifts (43-1046, 43-1123) - Contributions and gifts are deductible up to 20% of adjusted gross income for individuals and 5% for corporations.

7. Political Contributions (new this year) - A deduction of up to $100 for an individual or $200 for a joint return is allowed for contributions to State and local political campaigns and organizations.

8. Adoption Expenses (43-1047) - The law allows a deduction for adoption expenses in excess of 5% of the adjusted gross income with a maximum of $2,500 for joint returns and $1,250 on separate returns. (43-1047)

9. Deduction for Estate Tax (43-1048) - An individual receiving an amount or item from a decedent's estate must include the amount or value of the item in gross income. However, a percentage of such income is deductible to avoid paying a tax twice on the same income; once under gross income and once under the estate tax (43-1312). The amount deductible is equal to the ratio of the Arizona Estate Tax which resulted from the net value of the items or amounts included in gross income bears to the value for estate tax purposes of the items or amounts from the decedent's estate.

10. Medical Expenses (43-1049) - A deduction will be allowed for all medical expenses, including certain amounts paid for medical insurance, not compensated by insurance or otherwise.

11. Deduction for the Care of Qualified Dependents (43-1050) - The law allows a deduction for the wages paid to a housekeeper, nursemaid, licensed nursery school or rest home for the care of dependents up to 16 years of age; or any dependent physically or mentally incapable of self care; if such care allows the taxpayer to be gainfully employed and if the household income does not exceed $6,000 per year. The deduction shall not exceed $100 per

12. Taxes and Interest Paid to Cooperative Apartment Corporations (43-1051) - A tenant-stockholder may deduct amounts representing certain taxes and interests of the corporation.

13. Dividends Received (43-1052) - Dividends are deductible if they are received from a corporation whose income is subject to Arizona's income tax.

14. Expenditures Incurred in Installation of Solar Energy Devices (43-1053) - A taxpayer may elect to amortize the adjusted basis of any solar energy device to the extent that such a deduction has not been taken in arriving at Arizona adjusted gross income.

15. Expenses in the Collection or Production of Income (43-1054) - The law allows a deduction for all ordinary and necessary expenses incurred in the production of income or for the management, conservation or maintenance of property for such purpose.

16. Deduction for Employee Business Expense (43-1054) - The law allows a deduction for all ordinary and necessary expenses incurred by an employee in the course of business except:

a) Expenses incurred by an employee but reimbursed by the employer;
b) Expenses of travel, meals, lodging while away from home, pair or incurred by the taxpayer in connection with employment;
c) Transportation expenses;
d) Expenses incurred by the employee as the result of a service which requires the employer to solicit business away from the employer's place of business.

17. Amortizable Bond Premium (43-1056) - The amount of an amortizable bond premium for a taxable year shall be allowed as a deduction. In the case of tax-exempt bonds, the amortizable bond premium shall not be allowed as a deduction.

18. Personal Exemptions (43-1057) deduction - The law allows an exemption of $1,000 for an individual; married couples or the head of the household are allowed $2,000 (43-1057).

B. ADJUSTMENTS*

1. Net Operating Loss Deduction (included in adjusted gross income 43-1021) - Operating losses in excess of the allowable deduction over gross income may be carried over 5 years and deducted after reduction by certain adjustments to prevent deductions of losses absorbed by income not taxed.

2. Depreciation (all depreciations included in adjusted gross income) - The law allows a reasonable allowance for exhaustion, obsolescence, wear and tear of business and income producing property. The allowance is that amount set aside in a taxable year in accordance with a reasonable consistent plan so that the aggregate of the amounts set aside, plus the salvage value, will, at the end of the estimated useful life of the depreciable property, equal the cost or other basis of the property. Depreciation on certain items include:

a) Depreciation of Tangible Property - This depreciation allowance applies only to that part of the property which is subject to wear and tear, to decay or decline from natural causes, etc. The allowance does not apply to inventories or stock in trade, to land, apart from the improvements or physical development added to it, to natural resources which are subject to allowances for depletion.
b) Depreciation of Intangibles - Intangible assets which have a limited life in the production of income may be depreciated. For example, copyrights or patents.
c) Leased Property Depreciation - Capital expenditures for the erection of permanent structures on leased property are recoverable through depreciation or amortization.
d) Depreciation in Special Cases - Special provisions are made for the depreciation of patents, copyrights and farm property.
e) Capital Losses (adjustment under net operating loss 43-1025) - The law allows deductions to individuals and corporations for losses incurred in the sale of capital assets. The amount deductible, because of losses from sales or exchanges of capital assets, shall not exceed the amount includible because of gains from such sales or exchanges. Losses from securities which became worthless are deductible as the exchange or sale of a capital asset. Capital losses may be carried forward to succeeding years.

*Originally, these items were deductions from adjusted gross income, but with piggy-backing they become adjustments to gross income.

3. Depletion (adjustment under net operating loss 43-1025 and 43-1028) - The law allows a deduction of a reasonable allowance in the case of mines, oil, gas and geothermal resource wells, other natural deposits for depletion and depreciation improvement. The deduction for depletion shall not exceed the amount which would be allowable if computed without reference to discovery value or to percentage depletion.

4. Pollution Control Facilities (included in adjusted gross income 43-1030) - Any taxpayer may elect to amortize the adjusted basis of a water or air pollution control facility over a 60-month period.

5. Moving Expense (included in adjustments to gross income 43-1021) - Moving expenses deductible in connection with commencement of employment or self-employment, in a new location (reimbursement must be included in income).

6. Blind Exemptions (included in adjustments to gross income 43-1023) - The law allows a $500 exemption for the taxpayer or spouse who is blind.

7. Exemption for those 65 or Older (included in adjustments to gross income 43-1023) - A $1,000 exemption is allowed for a taxpayer or spouse who has attained the age of sixty-five.

8. Dependency Credit (included in adjustments to gross income 43-1023) - A $600 exemption to the taxpayer is allowed for each dependent.

9. Exemption for Estates and Trusts (included in adjustements to gross income 43-1332) - The exemption for an estate is $1,000 and for a trust $100, except in cases where the net taxable income of a trust is $200 or less, the exemption shall be $200.

APPENDIX VI-4

INCOME TAX CREDITS

I. Residents

A. <u>Credits for Income Taxes Paid to Another State or Country</u> (43-1071)
The law allows a 100% credit to residents for income taxes paid other states or counties on income derived from sources within that state or country which is taxed irrespective of the domicile of the taxpayer. No credit is allowed if the other state or country permits Arizona residents credit against its taxes for Arizona income taxes paid. The allowable credit may not exceed that proportion of the Arizona tax which the income taxable by both states bears to the entire income taxed by Arizona.

1. <u>Credit for Income Taxes Paid to Another State or Country by an Estate or Trust</u> (43-1071)
A credit is allowed estates and trusts or the resident beneficiary of a trust or estate, for net income taxes paid other states or countries, with limitations contingent upon the proportion taxable by both jurisdictions.

2. <u>Credit for Income Taxes Paid to Another State or Country by a Parnership</u> (43-1071)
A credit is allowed to resident partnerships for net income taxes paid another state or country subject to proportional limitations based on the partner's distributive share. When the income of a parnership is taxable to the partners, a credit will be allowed to the partners for taxes paid to another state or country. The partner's credit is limited to his percentage interest in the income of the partnership and a fraction, the numerator of which is his partnership income and the denominator of which is his Arizona gross income.

B. <u>Senior Citizens Credit for Property Taxes</u> (43-1072)
A credit is allowed to senior citizens, certain disabled persons, or persons receiving Social Security under Title 16 for property taxes or rent paid, or both, on the homestead. The tax credit is computed from a credit schedule based on household income. The tax credit will not exceed $225.

C. <u>Renter's Credit</u> (43-1073)
Renters are allowed a credit of 10% of rent paid or $75, whichever is less.

D. <u>Solar Energy Devices Credit</u> (43-1074)
A credit will be allowed to residents for solar energy devices installed in their Arizona residences. The credit will be equal to thirty-five percent of the cost of such device in 1978 and such credit shall decrease at a rate of 5% per year. The maximum credit will not exceed $1,000. Couples who file separate returns but could file a joint return will only be allowed to claim one-half the credit that would have been allowed for a joint return. Devices installed in commercial buildings may qualify for a 20% income tax credit until 1986. A credit for the installation of solar energy and/or cooling devices under R15-2-128.03 may be used in lieu of the solar energy devices credit. The deduction is computed in the same manner.

E. <u>Credit for Installation of Residential Insulation and Devices</u> (43-1075)
A credit will be allowed to residents for the installation of insulation and certain devices. The credit shall be equal to 25% of all improvements and shall not exceed $100.

II. Non-Residents

<u>Credit for Income Taxes Paid to Home State by Non-Resident</u> (43-1096)
Non-residents are allowed a 100% credit for taxes paid to their home state only if the home state does not tax income from Arizona residents derived from sources within the home state or allows Arizona residents a credit against its income taxes, but not if a double credit would be allowed; the credit will be subject to the proportional limitations noted in the provisions for residents.

III. Taxes Withheld From Wages

The amount withheld from wages is allowed as a credit against the tax owed on the taxpayer's income.

use fuel, the vendor) are responsible for collecting the tax and submitting payment to the Motor Vehicle Division of the Department of Transportation.

Incidence

In practice, the fuel and use fuel taxes are added directly to the price of the fuel. The tax on gasoline is thus paid wholly by individuals who consume gasoline. Use fuels, on the other hand, are consumed primarily by motor carriers (trucks, buses, etc.) who are liable for the entire tax but may be able to pass this expense to their customers in the form of a price increase for transport services.

Collection and Distribution

All fuel taxes, other than those collected from fuel used in watercraft and aircraft, are deposited in the Highway User Revenue Fund. During 1977-78 fuel taxes in the amount of $119,835,512 were distributed to the Highway User Revenue Fund. This is equal to 6.95% of total state revenues. Under law all monies deposited in the Highway User Revenue Fund are distributed as follows:

11% to the State Highway Patrol Fund
57% to the State Highway Fund
15% to the counties
17% to the incorporated cities and towns

Revenues allocated to the counties are further distributed based on the proportion that the sale of motor vehicle fuel and the estimated consumption of use fuel in each county bears to the total sales of motor vehicle fuel and the estimated consumption of use fuel throughout the state during the preceding calendar month.

One half of the revenues allocated to the incorporated cities and towns is distributed on the basis of the population that each bears to the population of all cities and towns within the state. The remaining half is apportioned first on the basis of the county origin of sales of motor vehicle fuels within the state. This amount is further apportioned among the several incorporated cities and towns within each county by the proportion that the population of each city or town bears to the total population of all cities and towns within the county.

Criteria

1. Revenue Generation:

   a. Does the revenue from fuel taxes increase as the demand for government services expands?

      The fuel tax was originally levied on a per gallon basis because the number of gallons of fuel purchased increased relative to the distance traveled. Thus, the tax base increased with the amount of road use and provided additional revenues for road repairs. However, in recent years, the number of gallons of fuel required to travel a given distance has begun to decline and the fuel tax revenues available for a given amount of road use are declining as well.

   b. Will revenues from the fuel tax expand over time as the price of government services increases?

      Fuel tax revenues will not expand as the general price of goods increases because fuel taxes are levied on a per unit basis and do not reflect the effects of any increase in the purchase price of fuel.

2. Social Equity:

   a. Is the fuel tax affordable from current cash flow?

      The fuel tax is effectively paid by individuals in the form of increased fuel prices at the time of purchase or in the case of use fuel taxes it may be paid in the form of increased prices for goods transported by motor carrier. Thus, if the taxpayer has sufficient income available to purchase fuel or goods transported by motor carrier, the fuel tax will be paid from current cash flow at the time the purchase is made. If income is not available to pay the full price of fuel with the tax included, the individual may limit his purchase of fuel or goods and thereby avoid tax liability. However, if the taxpayer is unable to limit his purchase of fuel or goods beyond a basic minimum amount, he will be subject to the tax on this amount regardless of his income or the hardhsip which this liability may represent.

   b. Is the fuel tax borne by individuals with common circumstances equivalent?

      Because the tax rate levied per gallon is equal throughout the state, all individuals who travel the same number of miles will be subject to tax liabilities which are roughly equivalent if they own vehicles with similar mileage ratings. However, the taxes paid by an individual who gets 12 miles to the gallon will be twice as much for a given distance traveled as the taxes paid by an individual who gets 24 miles to the gallon over the same distance.

   c. Will individuals who receive greater benefits from government services pay greater fuel taxes?

      Because fuel taxes are dedicated to use for a specific government service (road construction and repair and highway safety enforcement) it is possible to distinguish relationships between taxes paid and benefits received. In the case of fuel taxes and use fuel taxes, individuals who travel a greater number of miles and/or drive heavier vehicles will ordinarily demand more road construction and repair. Usually, these same individuals will purchase a greater number of gallon of fuel and will thus pay greater fuel taxes. Thus, benefits received and taxes paid will bear a direct relationship to each other.

3. Ease of Administration:

   Can the fuel tax base be determined without difficulty?

   Because the fuel tax and use fuel tax are levied on a per unit basis, the tax base is relatively easy to determine. Some difficulties are experienced in administering the use fuel tax, however, because of the provision that interstate motor carriers are subject to the tax only on fuel used for miles traveled within the state.

4. Consistency with State Goals:

   a. Are substantial portions of the fuel tax and use fuel tax paid by the residents of other states?

      To the extent that non-residents using roads within the state purchase gasoline or consume user fuel during their travels, they will be subject to the fuel or use fuel taxes, the revenues from which can be used to pay for increased road repairs associated with the additional mileage traveled by non-residents. However, non-residents will not pay any part of the costs of increased road repairs caused by increased travel by residents.

   b. Will the fuel tax produce revenues without detrimentally affecting business?

      To the extent that the cost of gasoline is a cost of doing business, the profitability of businesses will be directly affected by a change in the price of gasoline. Thus, if an increase in the fuel tax or use fuel tax paid by fuel distributors is subsequently added to the price of fuel, the profitability of businesses which rely on this source of fuel will decline or the business will raise its prices to cover the cost of the increase in fuel prices. The impact of such an increase will be most directly realized by the transportation industry.

B. VEHICLE LICENSE TAX

Description

The vehicle license tax is levied in lieu of property taxes on the assessed valuation of vehicles registered within the state. The assessed valuation of a vehicle is defined by statute as 60 percent of the manufacturer's base retail price during the year in which the vehicle is initially registered, and thereafter the value is reduced by 25 percent in each successive year.

The license tax on vehicles is provided for in the Arizona State Constitution though administrative provisions are prescribed in statute.

The effective tax rate has been $4 per $100 of assessed valuation since 1947.

Administration

The vehicle license tax is collected by the county assessor's office each year at the time vehicles are registered. The county assessors' offices use schedules of the factory advertised delivery price published by the National Auto Dealers Association to determine the base value of vehicles subject to the tax. All collections received by the county assessor from the tax are transferred to the County Treasurer for further distribution.

Incidence

The vehicle license tax is a direct tax on owners of vehicles. Because the assessed valuation of vehicles is reduced substantially each year after purchase, owners of new vehicles will pay a relatively large proportion of the total tax collections. For example, the owner of a new car with a base retail price of $5,000 will pay a license tax of $120 in 1979, while the owner of an automobile with a base retail price of $5,000 in 1975 will pay a license tax of $38 in 1979. Vehicle license taxes paid by motor carriers and other vehicles owned by businesses will likely be passed to consumers of goods transported by the carrier in the form of a price increase.

Collection and Distribution

The vehicle license is authorized by statute but collected at the county level. Total tax collections from this source amounted to $52,777,676 during

1977-78. Of this amount $23,516,096 was distributed to the state's general fund. State general fund collections of the vehicle license tax account for 1.36% of total state revenues.

Beginning with fiscal year 1977-78, collections from license taxes levied on vehicles within each county were distributed in the following manner:

- 20 percent to the state general fund*.
- An additional 25 percent to the state general fund to be used for school financial assistance
- 25 percent to the county general funds
- 25 percent to the incorporated cities and towns within each county apportioned on the basis of population
- 5 percent to the county assessor's office for registration and titling expenses*

A separate formula provides for the distribution of license taxes levied on motor carriers operated in interstate commerce. Collections from interstate operators are distributed in the following manner:

- 25% to the state general fund
- 25% to the county general funds
- 25% to the several common and high school districts
- 25% to the several incorporated cities and towns

However, it would appear that in practice, the interstate collections are distributed in the same fashion as are the "intrastate" collections.

Criteria

1. Revenue Generation:

   a. Will revenues from the vehicle license tax expand as the demand for government services expands?

      Generally, the vehicle license tax base will expand if the number of vehicles licensed within the state increases. This may be related to increases in the demand for government services in two ways. First, a greater number of vehicles will require greater expenditures for highway construction, traffic services, etc. Although vehicle license taxes are not specifically dedicated to road repair and construction, it would be possible to use any increase in revenues resulting from an increased number of licensed cars to fund expansions in road construction, highway safety enforcement or other services which are required as a result

*If the county assessor's office elects to transfer vehicle registration and titling duties to the Department of Transportation, the 5 percent of collections allocated to the county assessor's office will be surrendered to the state general fund.

of additional vehicles on the road. New vehicles traveling on state highways may also be indicative of an increase in the number of people living within the state. The additional revenues obtained from licensing of new vehicles on the tax rolls can be used to finance the additional government services associated with population increases in general.

b. Will vehicle license tax revenues expand as the cost of government services increases?

Generally, an increase in the overall price level will be accompanied by an increase in the price of vehicles. Such an increase in the price of vehicles will result in an expansion in the base value subject to the vehicle license tax and may result in increased revenues from this source, assuming that the purchase of new vehicles does not decline. Any increase in revenues can then be used to fund the added cost of government services, which is also related to a general increase in the level of prices.

2. Social Equity:

a. Is the vehicle license tax affordable from current cash flow?

To the extent that the vehicle license tax may be regarded as an added cost of purchasing a new vehicle during the first year of purchase, it may be argued that the purchase would not be made if sufficient income were not available to pay all associated costs. However, to the extent that motor vehicle license taxes are similar to property taxes and are not paid at the time of purchase in ensuing years, the taxpayer will be liable for vehicle license taxes on any vehicle owned, regardless of income. The vehicle license tax differs from the property tax, however, in that vehicle license tax liability decreases automatically over time.

b. Is the vehicle license tax borne by individuals with common circumstances equivalent?

Because the rate of taxation levied on vehicles is consistent throughout the state and the taxable value is standardized for any given type of vehicle, owners of any two vehicles which were comparable in value during the year in which they were originally produced will be subject to equivalent tax liabilities during all subsequent years. The respective tax liabilities borne by individuals may be inequitable, however, to the extent that individuals purchasing vehicles with optional equipment are taxable upon the same value as individuals purchasing a comparable vehicle without optional equipment.

c. Will individuals who receive greater benefits from government services pay greater vehicle license taxes?

To the extent that individuals who own a greater number of vehicles are likely to require a greater amount of government services in the form of road construction, highway safety enforcement, etc., it may be argued that those individuals who pay the most vehicle license taxes also receive greater benefits from government services. However, vehicle license tax revenues are not specifically dedicated to road construction and repair and highway safety enforcement, thus any connection which does exist between benefits received from government services and vehicle license taxes paid must be viewed as indirect. Also, because the tax liability for any given vehicle declines as the age of the vehicle increases, the revenues from the vehicle license tax may decline while the demand for government services (road construction, etc.) remains constant or increases.

3. Ease of Administration:

   Can the vehicle license tax base be determined without difficulty?

   Because the National Auto Dealers' Association publishes schedules of the factory advertised delivery price, which are used by county assessors to determine the manufacturer's base retail price, a measure of the vehicle license tax base is readily available. The counties are, therefore, able to administer the tax without any serious difficulty.

4. Consistency with State Goals:

   a. Is a substantial portion of the vehicle license tax paid by residents of other states?

      Registration of vehicles is primarily restricted to residents and only those individuals required to register their vehicles with the State of Arizona are subject to the vehicle license tax. However, vehicle license taxes levied on motor carriers and other vehicles used for business purposes may be partially paid by non-residents, if added to the price of goods sold to individuals in other states.

   b. Will the vehicle license tax produce revenues without detrimentally affecting business?

      Because the vehicle license tax is a significant cost of business to the transportation industry and may be passed to other businesses which purchase services from the transportation industry, the profitability of the purchasers may be detrimentally affected by an increase in the vehicle license tax. The detrimental impact on businesses may be reduced or eliminated, however, if the tax can be passed to individuals purchasing goods in the form of a price increase without an offsetting decline in demand.

C. MOTOR CARRIER LICENSE TAX

Description

The motor carrier license tax is levied on the gross receipts of common or contract carriers of passengers or property, operating within the state*. When any carrier operates partly within and partly outside the state, all receipts of business beginning and ending within the state are taxable. The ratio of mileage within the state to the entire mileage over which business is done,taken times the receipts from all business passing through, into or out of the state,is also taxable. The rate at which the receipts of carriers of property are taxed is 2.5 percent. The rate applied to the gross receipts of passenger carriers is 2.25 percent. Private carriers (those owned by the business for which goods are transported) are not subject to the tax.

Administration

The motor carrier license tax is payable to the Motor Vehicle Division of the Department of Transportation. Owners of motor carriers are required to file returns identifying their taxable receipts and must submit payment by the 25th of each month for the tax liability incurred during the previous month. Collections received by the Motor Vehicle Division are transferred to the Highway User Revenue Fund, which is further distributed by the State Treasurer.

Incidence

The motor carrier license tax is effectively a sales tax on the service of transporting property and passengers. The tax may not be added to the price of the service provided without being subject to further taxation. Because the tax represents an additional cost of doing business, however, the carrier industry will attempt to increase the price of services provided in order to recoup as much of this cost as possible. In this case, the taxpayer will be required to pay a portion of the tax in the form of increased prices for carrier services or goods transported by carrier.

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*The motor carrier license tax is scheduled to be replaced by a ton-mile tax in 1982 according to legislation passed in the 1979 regular legislative session. The ton-mile tax will apply to private carriers as well as common and contract carriers.

Collections and Distribution

The motor carrier license tax is levied only at the state level. During 1977-78 total collections from the tax amounted to $15,386,441 or .89 percent of total state revenues. All collections from this tax are deposited in the Highway User Revenue Fund. This fund is distributed as follows:

- 11 percent to the State Highway Patrol Fund (D.P.S.)
- 57 percent to the State Highway Fund (A.D.O.T.)
- 15 percent to the counties
- 17 percent to the incorporated cities and towns

Revenues allocated to the counties are further distributed based on the proportion that the sale of motor vehicle fuel and the estimated consumption of use fuel in each county bears to the total sales of motor vehicle fuel and the estimated consumption of use fuel throughout the state during the preceding calendar month.

One half of the revenues allocated to the incorporated cities and towns is distributed on the basis of the population that each bears to the population of all cities and towns within the state. The remaining half is apportioned first on the basis of the county origin of sales of motor vehicle fuels within the state. This amount is further apportioned among the several incorporated cities and towns within each county by the proportion that the population of each city or town bears to the total population of all cities and towns within the county.

Criteria

1. Revenue Generation:

   a. Will the motor carrier license tax expand as the demand for government services expands?

   Motor carrier license tax receipts are specifically devoted to road construction and repairs, and highway safety enforcement. Generally, demand for these services will increase as the number of motor carriers using Arizona roads increases. To the extent that an increase in the number of carriers results in increased receipts from carrier services, the revenues available from the carrier tax will also increase. An increase in demand for road construction services, etc., could also result from an increase in miles traveled by carriers within the state. This, too, would probably be accompanied by an increase in gross receipts as more goods were transported, thus increasing the taxable base from which revenue will be derived.

b. Will the revenues from motor carrier license taxes expand as the price of government services increases?

A general increase in the price of goods, which will cause an increase in the cost of government is likely to be accompanied by an increase in the cost of services, including motor carrier services. Because gross receipts from motor carrier services are the base on which the motor carrier license tax is levied, an increase in revenues from this tax will follow.

2. Social Equity:

a. Is the motor carrier license tax affordable from current cash flow?

Because the motor carrier license tax is an added cost of doing business, it will be added to the price of carrier services, if possible, and therefore will be borne by the consumer in the form of increased prices for passenger services or goods transported by motor carrier. Thus, if the taxpayer has sufficient income available to purchase passenger services or goods transported by motor carrier, the motor carrier license tax will effectively be paid from the taxpayer's current cash flow at the time the purchase is made. If income is not available to pay the full price of these goods and services, with the tax included, the individual may limit his purchase and consequently avoid tax liability. However, if the taxpayer is unable to limit his purchase of such goods and services beyond a basic minimum amount, he will be subject to the tax on this amount regardless of his income or the hardship which this liability may represent.

b. Is the motor carrier license tax borne by individuals with common circumstances equivalent?

All common carriers transporting passengers are taxed at the same rate. Thus, the increase in passenger fare borne by individuals using the same type of passenger services should be roughly equivalent but may vary depending on the ability of each carrier service to absorb the cost of paying this tax without increasing prices. All motor carriers transporting property are also taxed at the same rate. Thus, individuals whose total consumption of goods transported by motor carrier is roughly equivalent in value should experience comparable increases in the price of these goods when the price is adjusted to reflect the increased cost of transporting these goods due to payment of the carrier tax. This, too, may vary depending on the ability of the carrier to absorb the tax without a price increase.

c. Will individuals who receive greater benefits from government services pay greater motor carrier license taxes?

Revenues from motor carrier license taxes are specifically dedicated to road construction and repair and highway safety enforcement. Because the motor carrier license tax is based on gross receipts, carriers who receive greater benefits will pay higher license taxes if it can be assumed that industries which receive the greatest income from regular road use benefit most from highway construction and repair.

3. Ease of Administration:

   Can the motor carrier license tax base be determined without difficulty?

   Motor carrier license taxes are levied on the gross receipts of motor carriers. As the price of motor carrier services is established prior to sale, a measure of the taxable base is readily available if accurate records are kept of the amounts received for carrier services which are subject to the tax. Motor carrier companies must keep accurate records of receipts in the course of business, and are required by law to furnish reports of these receipts and other related information to the Department of Transportation. Some difficulty may be experienced, however, in determining the taxable base because of the provision that interstate motor carriers may apportion their receipts according to the percent of miles traveled within the state.

4. Consistency with State Goals:

   a. Is a substantial portion of the motor carrier license tax paid by residents of other states?

      Motor carriers operating in both interstate and intrastate commerce are subject to the motor carrier license tax only on that portion of gross receipts derived from passengers or goods transported within the state. The percentage of miles traveled by carriers within Arizona to total miles traveled, will be used to determine the proportion of gross receipts derived from passengers or goods transported within the state. Thus, non-residents will be subject to the tax on passenger miles traveled by carriers within Arizona and on goods transported by motor carriers which use Arizona roads, to the extent that motor carrier taxes are incorporated into the price of these goods and services.

   b. Will the motor carrier license tax produce revenues without detrimentally affecting business?

      Because the motor carrier license tax is a direct cost of doing business to the motor carrier industry, the profitability of this industry will be affected by a change in the tax. If the motor carrier industry is not able to absorb this additional cost without a price increase, then the cost of goods transported by motor carrier will also increase and the profitability of industries producing these goods may be affected as well.

      On the other hand, the beneficial impact on business from road repairs and construction, etc. may more than compensate the industry for the cost of the tax.

D. LUXURY TAXES

Description

1. Tobacco Products:

   Luxury taxes on tobacco products are levied at the following rates:

   - 13¢ on each 20 cigarettes or fractional part thereof
   - 1¢ on each ounce of smoking or chewing tobacco
   - ¼¢ on each ounce of plug or twist tobacco
   - 2¢ on each 20 small cigars weighing not more than three pounds per thousand
   - 1¢ on every three cigars retailing at five cents or less each
   - 1¢ on cigars retailing at more than five cents each

The effective rate of taxation on cigarettes is actually slightly less than stated because cigarette wholesalers must purchase tax stamps to indicate payment of the tax and these stamps are discounted in order to compensate the wholesaler for the administrative cost of attaching these stamps to each package of cigarettes.

2. Liquor:

   Luxury taxes on liquor are levied at the following rates:

   - 15¢ on each 16 ounces, or fractional part thereof, for malt extracts
   - $2.50 on each gallon of spirituous liquor with a proportionate rate for greater or lesser quantities
   - 12 ½¢ on each 8 ounces, or fractional part thereof, for vinous liquor having an alcohol content greater than 24 percent
   - 42¢ per gallon and at a proportionate rate for any lesser or greater quantity for vinous liquor having an alcohol content of less than 24 percent
   - 8¢ on each gallon of malt liquor

Administration

Luxury taxes levied on alcohol and tobacco products other than cigarettes, are paid monthly to the Department of Revenue by wholesalers purchasing such products for resale. Wholesalers are liable for the tax on all such luxury items sold during the preceding month and a sworn statement must accompany the payment attesting to the accuracy of the tax remittance.

Luxury taxes on cigarettes are paid when wholesalers purchase stamps from the Department of Revenue. These stamps must be affixed to each package of cigarettes by the wholesaler before resale, to indicate payment of the tax. Metering machines may also be used for this purpose, if more practical.

Incidence

The luxury tax is required by statute to be added to the sales price of tobacco products and liquor and is therefore borne wholly by the consumers of these products.

Collections and Distribution

Legislation was passed in 1973 to preempt taxation of luxuries to the state alone. During 1977-78, $36,790,865 or 2.13% of total state revenues was received from the luxury tax on tobacco products. Collections from the luxury tax on liquor amounted to $19,149,392 or 1.11% of total state revenues. All collections from luxury taxes on tobacco products and liquor are deposited in the state general fund. According to statute, 3.5¢ of the 13¢ tax levied on each 20 cigarettes is to be used for state school aid. The remaining collections from the luxury tax on cigarettes and tobacco products are to be used for unemployment compensation, welfare relief and other purposes as provided by law. Three and one-half cents of the tax collected on each gallon of spirituous liquor and each 8 ounces of vinous liquor with an alcohol content greater than 24 percent is also specifically dedicated to state school aid. The remaining revenues from the luxury tax on liquor are to be used for unemployment compensation, welfare relief and other purposes prescribed by law. The statutes outlining the purposes for which luxury tax revenues are to be used are largely ignored in practice.

Criteria:

1. Revenue Generation:

   a. Will revenue received from the luxury tax on tobacco products and liquor expand as the demand for government services expands?

      Because luxury tax revenues are not specifically dedicated to any particular government service, it is difficult to determine if revenues from these taxes expand in relation to increases in the demand for government services. It may be possible, however, to establish a relationship between increases in some government provided services and increases in luxury tax revenues. This relationship can be shown if the increased consumption of luxuries, which produces additional revenues, will itself create a demand for additional government services.

For example, if the demand for health related services increases with the consumption of cigarettes and alcohol or if more traffic safety enforcement is required as alcohol consumption increases, some increase in luxury tax revenues may be experienced as the demand for government services increases. However, if an increase in the consumption of certain luxuries is more closely related to a higher level of personal income, then revenues from these items may increase during times of economic prosperity when demands for government services (welfare, unemployment, etc.) are relatively low.

b. Will revenues from luxury taxes increase as the price of government services increases?

Luxury taxes are levied on a per unit basis and are not based on receipts from the sale of luxuries. Although the price of luxuries may increase as the general level of prices rises, this will not result in increased luxury tax revenues if the number of units purchased remains constant. Thus, an increase in the price of government services resulting from an increase in the general price of goods will not be met by increased luxury tax revenues.

2. Social Equity:

a. Is the luxury tax affordable from current cash flow?

The luxury tax is effectively paid by individuals in the form of increased prices at the time of purchase. Thus, if the taxpayer has sufficient income available to purchase tobacco products and liquor, the tax will be paid from current cash flow. If income is not available to pay the full price of luxuries with the tax included, the individual may limit his purchase of luxuries and thereby avoid tax liability.

Because luxuries, by definition, are items which are generally considered to be unnecessary for subsistance, it is unlikely that taxpayers will be necessarily subjected to payment of the luxury tax.

b. Is the luxury tax burden borne by individuals with common circumstances equivalent?

Because the tax rate levied on any given luxury is consistent on a statewide basis, individuals who purchase the same types of luxury items in comparable quantities will be subject to equivalent tax burdens.

c. Will individuals who receive greater benefits from government services pay greater luxury taxes?

It is possible that some relationships exist between benefits received from government services and luxury taxes paid. For example, cigarette smokers may rely more heavily on government-provided health services, individuals who consume alcohol may be arrested for D.W.I..

These relationships are probably tenuous, however, and in general luxury taxes paid probably bear little direct relationship to benefits received from government services.

3. Ease of Administration:

Can the luxury tax base be determined without difficulty?

Because the luxury tax is levied on the number of units purchased and the rate applied to each unit is well-defined, the value of the taxable base is relatively easy to determine.

4. Consistency with State Goals:

a. Is a substantial portion of the luxury tax on alcohol and tobacco products paid by residents of other states?

Any non-resident purchasing luxuries in the State of Arizona will be taxed on the amount purchased. If it can be assumed that individuals visiting the state consume significant amounts of liquor and tobacco products, then it follows that a portion of the total luxury tax burden will be borne by non-residents.

b. Will the luxury tax generate revenues without detrimentally affecting business?

Because the luxury tax is relatively large and statutorily required to be added to the price of luxury products sold, the demand for liquor and tobacco products has probably been reduced and the profitability of the liquor and tobacco industries may be somewhat limited as a result. Aside from these two industries, however, it is unlikely that there has been any significant impact on the growth of business within the state due to the luxury tax.

E. INSURANCE PREMIUM TAXES

Description

The insurance premium tax resembles a sales tax in that it is levied on the gross receipts of insurance companies from the sale of insurance policies. The insurance premium tax is levied only on premiums derived from policies covering liabilities existing within the state. Title insurance annuities and reinsurance programs are not subject to the tax. Cancellations, returned premiums and refunds are deductible from gross receipts for purposes of taxation.

In the State of Arizona, the rate at which the net receipts from insurance policies are taxed depends upon the type of insurance purchased and the type of insurance company from which the policy was procured. The following rates are applicable:

- 1.0% of net premiums paid to domestic insurance carriers maintaining a home office within the state, and premiums (other than those paid by government entities) which are paid to hospital, medical, dental and optometric service corporations organized under the laws of this state.

- 2.0% of net premiums, except motor vehicle insurance premiums, paid to foreign and alien insurance carriers and domestic insurers who fail to maintain a home office in Arizona.

- 2.5% of net premiums for motor vehicle insurance paid to foreign and alien insurance carriers and domestic insurers who fail to maintain a home office in Arizona.

- 3.0% of net premiums paid to brokers selling surplus line insurance and on net premiums paid by corporations insured under contracts procured from unauthorized insurers.

A domestic insurance carrier is an insurer formed under the laws of this state. A foreign insurance carrier is an insurer formed under the laws of another state of the United States. A surplus line insurance carrier is an insurer selling policies not readily available from authorized insurers. (For example, a pianist may insure his hands through Lloyd's of London.) An unauthorized insurance carrier is any insurer which has not been issued a certificate of authority from the director of the insurance department of this state.

Retaliatory taxes and fees are imposed on insurance carriers chartered by states or foreign countries which impose taxes and fees on Arizona insurance carriers in excess of those which Arizona imposes on similar forms of insurance. Retaliatory rates equal the rates imposed on Arizona insurance carriers by the respective states or countries. Retaliatory rates are also levied by other states when Arizona rates exceed the rates charged by other states on comparable forms of insurance.

GUARANTY FUNDS

A separate assessment is levied against property and casualty insurance companies to reimburse the property and casualty insurance guaranty fund for the payment of claims against insolvent insurers. Additional assessments are also levied against life and disability insurance companies in amounts sufficient to reimburse the life and disability insurance guaranty fund for the payment of claims against insolvent insurers. Each insurer subject to these assessments is granted a decrease in premium tax liability equal to twenty percent of the assessments for the year in which they are levied and twenty percent of the assessments per year for each of the succeeding four years.

Administration

Each year, insurance companies must file annual statements showing total direct premium income received during the previous calendar year. Authorized domestic insurers are liable for taxes on or before March 31, on premiums received during the previous calendar year. All other insurers are liable for payment of taxes on or before March 1. The Insurance Department is responsible for collection and administration of the tax.

Incidence

Because the insurance premium tax is levied on insurance companies, it represents an additional cost of doing business which will be recouped by insurance companies through increases in the rates charged for insurance policies. To the extent that an insurance company is able to raise its rates without substantially reducing the demand for insurance, the premium tax will effectively be paid by purchasers of insurance.

Collections and Distribution

Insurance premium taxes are collected only at the state level. The bulk of the taxes collected are deposited to the state's general fund; however, taxes on fire insurance premiums are donated to the Firemen's Relief and

Pension Fund. The Public Safety Personnel Retirement System receives 20% of the tax collected on motor vehicle insurance premiums paid to foreign and alien insurance carriers and domestic insurance carriers who fail to maintain a home office in this state. Monies deposited in the Firemen's Relief and Pension Fund are prorated among the several incorporated cities and towns and legally organized fire companies in proportion to the amount of fire insurance tax collected from insurance on property therein.

Insurance premium tax collections during 1977-78 amounted to $26,623,007 or 1.54% of total state tax collections. Of this amount, $1,655,017 was distributed to the Public Safety Personnel Retirement System and $1,247,847 was distributed to the Firemen's Relief and Pension Fund. The remaining amount ($23,720,143) was deposited to the state general fund.

Criteria

1. Revenue Generation:

   a. Will revenues from the insurance premium tax expand as the demand for government services expands?

      Insurance premium taxes are general revenues and are not dedicated to any specific purpose. Therefore, it cannot be determined if revenues from this source will expand to sufficiently finance the particular area of government expenditures to which they are dedicated. Increases in revenues from this source may have some connection with increased demands for general government services insofar as increases in insurance purchases are at times related to new taxpayers coming into the state and new taxpayers will require expanded government services. However, to the extent that insurance serves as a substitute for government services (e.g. health insurance may alleviate the for government-provided health services), an increase in the premium tax may be associated with a decline in demand for government services. Also, if it may be said that insurance purchases are related to income and that outlays for insurance will increase as personal income rises and will decrease as income falls, then tax revenues from insurance premiums will not expand as the demand for government services increases since low-income families usually require more government services (welfare, unemployment, etc.) and will pay fewer premium taxes. Overall, there is probably little connection between expanded demand for government services and expanded revenues from this source.

   b. Will revenues from the insurance premium tax expand as the price of government services increases?

      A general increase in the price of goods will probably be accompanied by an increase in the price of insurance. Because the insurance premium tax is levied on gross proceeds from sales of insurance, increasing insurance prices will probably result in greater tax revenues from this source which can be used to help finance the increased cost of government services also associated with a general price increase.

2. Social Equity

   a. Is the insurance premium tax affordable from current cash flow?

   The insurance premium tax is effectively paid by the individual in the form of increased prices at the time of purchase of insurance. Thus, if the taxpayer has sufficient income available to purchase insurance, the tax on insurance premiums will be paid from current cash flow. If income is not available to pay the full price of insurance with the tax included, the individual may limit his purchase of insurance and thereby avoid tax liability. However, if the taxpayer is unable to limit his purchase of insurance beyond a basic minimum amount, he will be subject to the tax on this amount regardless of his income or the hardship which this liability may represent.

   b. Is the insurance premium tax burden borne by individuals with common circumstances equivalent?

   Individuals with equivalent incomes who purchase comparable insurance policies may be subject to different levels of insurance taxes depending upon the nature of the company from which the insurance is purchased (domestic, foreign, alien, etc.). The amount paid for insurance, and consequently the tax, will also vary depending upon the element of risk involved in providing a given form of insurance policy.

   c. Will those individuals who receive greater benefits from government services pay greater insurance premium taxes?

   Again, because insurance premium taxes are general revenues and are not dedicated to any specific purpose, it is difficult to relate revenues from this source to any specific benefit. It is also unlikely that increases in the purchase of insurance which are the basis for increases in revenues from this source give rise to any requirements for increased government services. In fact, fewer government services may be needed because of the ability to substitute insurance for certain government services. Therefore, there is probably little relation between taxes paid and benefits received.

3. Ease of Administration:

   a. Can the insurance premium tax base be determined without difficulty?

   The insurance premium tax is levied on gross receipts from sales of insurance policies; as the price of insurance is established prior to sale, a measure of the taxable base is available before payment of the tax if accurate records are kept of the premiums paid for policies subject to the tax.

4. Consistency with State Goals:

   a. Is a significant portion of the insurance premium tax paid by the residents of other states?

      The insurance premium tax is levied only on policies covering liabilities existing within the State of Arizona. Policies covering liabilities existing within other states or countries are taxable under Arizona law only in retaliation for taxes imposed on Arizona insurance carriers or if they are not subject to taxation in the state or country where they are located. Because all states levy insurance premium taxes of some form, the Arizona insurance premium tax is rarely applied to policies covering liabilities existing outside of Arizona, except in the case of retaliation, and thus the tax burden borne by non-residents is relatively insignificant.

   b. Does the insurance premium tax raise revenues without affecting business detrimentally?

      The only industry directly affected by the insurance premium tax is the insurance industry. Because the tax is levied on insurance companies, it is a cost of doing business and could have a detrimental effect if levied at an excessive rate causing insurance prices to increase to a level which is intolerable to the consumer.

SOURCES OF ARIZONA STATE REVENUE
BEFORE DISTRIBUTION TO LOCAL GOVERNMENTS
BREAKDOWN OF OTHER TAXES
1977-78

E = OTHER TAXES

E1 = FUEL TAXES 7.03%

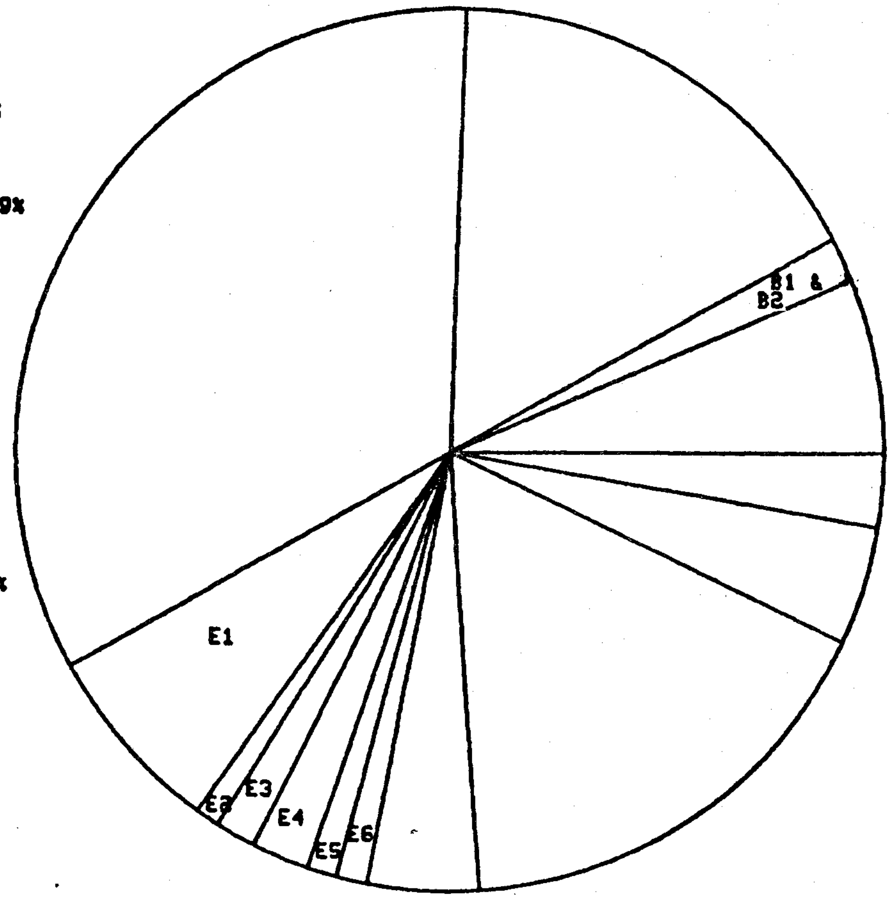
E2 = MOTOR CARRIER LICENSE TAXES .89%

E3 = INSURANCE PREMIUM TAXES 1.54%

E4 = LUXURY TAXES ON TOBACCO 2.13%

E5 = LUXURY TAXES ON ALCOHOL 1.11%

E6 = MISCELLANEOUS OTHER TAXES 1.15%



B = OTHER PROPERTY TAXES

B1 = MOTOR VEHICLE LICENSE TAXES 1.36%

B2 = MISCELLANEOUS OTHER PROPERTY TAXES .27%

TOTAL REVENUE = $1,725,466,329

SOURCES: 1977-78 ANNUAL FINANCIAL REPORT, DEPARTMENT OF ADMINISTRATION, FINANCE DIVISION, OCTOBER 1978, P.4; 1977-78 ANNUAL REPORT OF THE ARIZONA DEPARTMENT OF REVENUE, 1978 STATE OF ARIZONA TAX HANDBOOK; ARIZONA DEPARTMENT OF TRANSPORTATION, DEPT. RECORDS; ARIZONA DEPAPTMENT OF ADMINISTRATION, DEPT. RECORDS.