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ARIZONA TAX RESEARCH ASSOCIATION

NEWSLETTER

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GRETCHEN KITCHEL REELECTED 2006 ATRA CHAIRMAN

Gretchen Kitchel, Senior Public Affairs Manager for Pinnacle West Capital Corporation, was reelected to a second term as the Chairman of the Board of the Arizona Tax Research Association (ATRA) at the association's 65th Annual Meeting on November 18, 2005.

Also elected as ATRA officers were Larry Lucero, *Tucson Electric Power*, first vice-chair; Amy Barron Etkorn, *Meritage Homes*, second vice-chair; Barb Dickerson, *Deloitte Tax LLP*, third vice-chair; and Dave Minard, *Individual*, secretary/treasurer.



Gretchen Kitchel

The following ATRA members were also elected to seats on the ATRA Board of Directors for terms expiring in 2010: Nick Balich, *Individual*; Jeff Barnett, *Pinnacle West Capital Corp*; Jim Brodnax and Joy Gomez, *B&G Property Tax*; Richard Heltzel, *El Paso Corporation*; Amy Barron Etkorn, *Meritage Homes*; Jason Bagley, *Intel*; Manny Lerma, *Qwest Communications*; C.A. Howlett, *U.S. Airways*; Dave Stevens, *Circle K Stores*; and Jason Creed, *Schuff Steel*. Elected to terms expiring in 2009 were Susan Anable, *Cox Communications*; and Tim Lawless, *NAIOP*. For terms expiring in 2008: Michael Galloway, *Bancroft, Susa, and Galloway*.

KEY LEGISLATORS ADDRESS ATRA OUTLOOK CONFERENCE

Speeches from Senate President Ken Bennett and House Speaker Jim Weiers, as well as the Chairman of the two tax writing committees, highlighted ATRA's 2005 Outlook Conference.

House Ways and Means Chairman Steve Huffman and Senate Finance Chairman Dean Martin joined ATRA Vice President Michael Hunter on a panel to discuss school capital finance reform. Michael presented ATRA's recommendations, which included turning the School Facilities Board into an executive agency and eliminating the Board as well as limiting access to K-12 property tax levies for capital.



Jim Weiers, Arizona House Speaker

Both Rep. Huffman and Sen. Martin offered their general support for ATRA's school capital finance reforms. The two chairs suggested that a thorough review of the state's Student's FIRST program, created in 1998, was now in order.

The tax chairs also provided some insight into their priorities for the two tax committees next session. Rep. Huffman expressed concern that growing property valuations will lead to considerable pressure on lawmakers to react to increasing property taxes. He said his preference in dealing with the



Ken Bennett, Arizona Senate President

See **LEGISLATIVE OUTLOOK**, page 4

GOVERNOR'S BUDGET DIRECTOR OFFERS FISCAL PERSPECTIVE

Gary Yaquinto, Director of the Office of Strategic Planning and Budgeting (OSP), addressed attendees at the 2005 ATRA Outlook Conference, providing a fiscal analysis of the state budget.

Mr. Yaquinto discussed some of the reasons for the increases in the state general fund expenditures, which he mainly attributed to population growth, specifically in the K-12 budgets.

Although Gary's overall message was that Arizona is not a high spending state, he pointed out that Arizona's general fund revenues, as a percentage of personal income, have steadily increased over the past few years, from 3.9% in FY 2003 to 4.6% in FY 2005.

Mr. Yaquinto informed conference attendees that Arizona's general fund spending has been well under the state's constitutional spending limit. For FY 2006, the state's spending level is at 6.39% while the limit is 7.41%.

Mr. Yaquinto's presentation also showed Arizona ranking 50th among K-12 spending per pupil in FY 2003 and 45th on a per capita basis.

He criticized the legislative decisions made in the 90's that reduced taxes, suggesting that those decisions resulted in a \$1.2 billion drop in general fund revenues in FY 2006. (This analysis excluded the Prop 301 tax increase.)



Gary Yaquinto, Director of the Office of Strategic Planning and Budgeting (OSP)

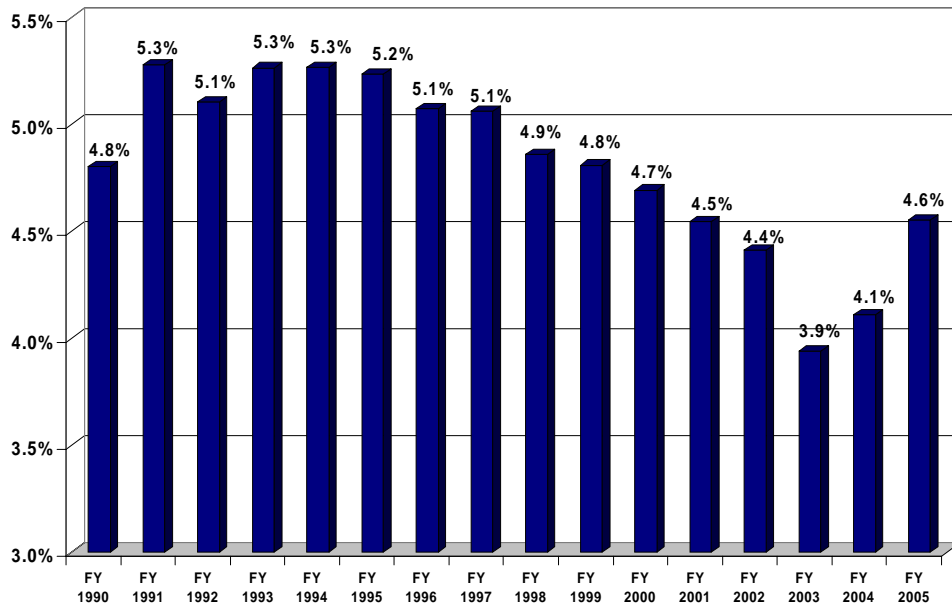
Lastly, Mr. Yaquinto outlined the Executive Branch's opposition to a potential TABOR initiative. He reviewed some of the problems

that Colorado experienced, beginning with tying the consumer price index to inflation rather than using an inflation deflator tied to government purchases.

Addressing the potential problems that arise when tying population growth to TABOR spending limits, he briefly discussed the dynamics that exist in various subgroups, such as the aging baby boomers. His point was that various subgroups will experience different levels of costs, which may not be representative of the entire population.

His final criticism of TABOR was that it assumes that base level expenditures are both adequate and appropriate.

General Fund Revenues as a Percentage of Personal Income



Source: OSPB and Bureau of Economic Analysis

ARIZONA TAX RESEARCH ASSOCIATION
 Gretchen Kitchel.....Chairman
 Kevin J. McCarthy.....President
 Jennifer Scholdt.....Senior Research Analyst
 Carmen Florez-Lucero.....Office Manager

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1814 W. Washington Street
 Phoenix, Arizona 85007
 (602) 253-9121
 FAX (602) 253-6719
 www.arizonatax.org
 atra@arizonatax.org



McCarthy, Keith Russell Focus On Property Taxes

With Arizona’s hot real estate market showing little sign of cooling off, Maricopa County Assessor Keith Russell and ATRA President Kevin McCarthy addressed how increasing property valuations will affect property tax bills next year.

Mr. Russell noted that Arizona’s constitution requires assessors to value property at its full cash value, which, unless a statutory formula for the property type is provided, is synonymous with market value. The statutory oversight authority provided to the Department of Revenue (DOR) ensures that county assessors keep assessed values within acceptable ranges of market value. Russell noted that the DOR standards typically keep assessed values slightly below sales prices.

In addressing the question of whether or not increases in property values will translate into increases in property taxes, Mr. Russell said that depended primarily on the budgetary decisions of elected officials. He said that the amount budgeted by a jurisdiction should be based on the needs and expectations of the citizens not on the value of the property.

While Russell strongly encouraged those in attendance to focus their concerns regarding increasing property taxes on the elected officials making the budget decisions, he narrowed the ultimate responsibility for increasing property taxes on the citizenry. He stressed that the decisions of voters on who they elect to

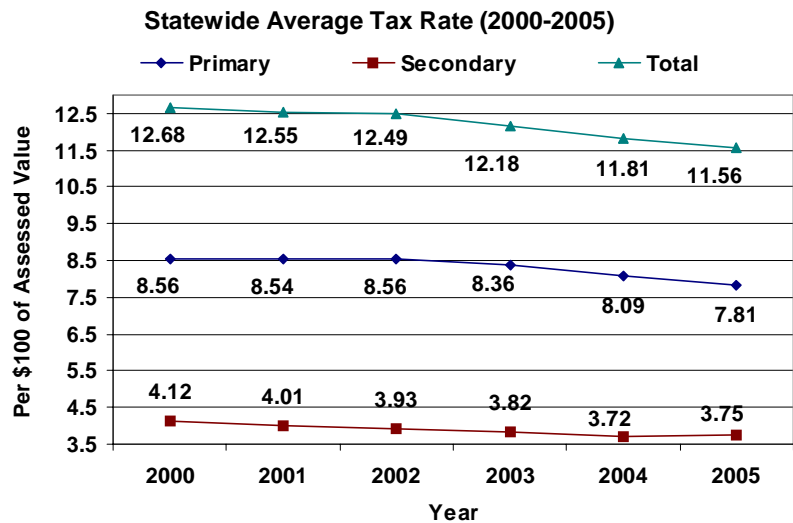


Keith Russell, Maricopa County Assessor

office and how they vote in bond and override elections has the greatest impact on property taxes.

ATRA President Kevin McCarthy followed Keith Russell with an overview of the current trends in Arizona property taxes with a specific focus on which jurisdictions are generally responsible for increasing taxes. He noted that ATRA’s efforts to control the growth of property taxes over the last decade have been mostly successful. Arizona’s state average

See **Property Taxes**, page 5



ATRA Honors Cathy Connolly

ATRA took the occasion of the annual Outlook Conference to present a special recognition award to Cathy Connolly, the Executive Director of the Arizona League of Cities and Towns. 2005 marks the end of Cathy’s 34-year career with the League, the last eight as the Executive Director.

In presenting the award to Cathy, ATRA President Kevin McCarthy said “When Cathy announced her retirement earlier this

year, city officials knew they were losing a huge asset. However, what was less understood was the effect of Cathy’s retirement on the taxpayers of the cities that Cathy worked for over the last 34 years. Cathy’s unparalleled knowledge of city government saved time and resources for Arizona City governments on a daily basis.” ATRA congratulates Cathy on 34 years of outstanding service!



Cathy Connolly

Lori Daniels, Allan Stanton

ATRA Outstanding Members

On behalf of the ATRA Board of Directors, Chairman Gretchen Kitchel presented ATRA members Lori Daniels and Allan Stanton with the 2005 ATRA Outstanding Member Awards.



In presenting the award to Allan, Gretchen said that it was a pleasure to recognize one of ATRA's longest standing members. Allan has been an ATRA member for decades and a member of the ATRA Board of Directors for the last 15 years. One of Arizona's most respected lobbyists at the Capitol, Allan is a regular at ATRA's Legislative Policy Committee meetings. "As one of the most respected voices on tax matters at the Capitol, Allan has devoted many hours assisting ATRA staff and members in their efforts to improve Arizona's property tax system," said Gretchen Kitchel in presenting the award.

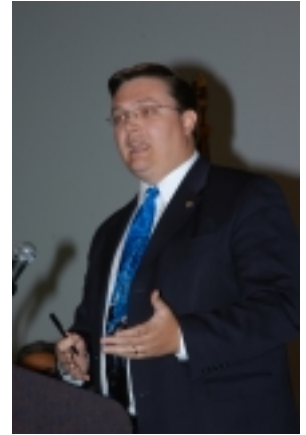


ATRA's second Outstanding Member Award for 2005 was presented to Lori Daniels. Lori joined ATRA following a long and successful career in the Arizona Legislature where she served as the Chairman of the House Ways and Means Committee and House Majority Leader. While in the Legislature, she developed a strong reputation for her expertise in tax policy and championed many ATRA proposals to improve Arizona's tax system. Following her public service, Lori joined ATRA and quickly became a member of the ATRA Board of Directors. In presenting the award to Lori, Gretchen Kitchel said, "Lori has demonstrated her genuine commitment to the development of sound tax policy both in the Legislature and as a member of ATRA. I hope this Outstanding Member Award serves as encouragement to continue that fine work."

LEGISLATIVE OUTLOOK

Continued from page 1

tax implications of a hot real estate market would be to focus on tax rates as opposed to value limits. He said he agreed in large measure with ATRA's property tax recommendations for next session.



Senator Dean Martin

Senator Martin indicated that, in addition to property tax cuts, he will also push for reductions in personal income taxes. He noted that Nevada, one of Arizona's competitors for economic development, has no personal income tax.

Legislative Leadership wrapped up the Outlook Conference with Senate President Ken Bennett providing an excellent overview of the state's current fiscal position. President Bennett warned that despite the current upswing in general fund revenue, it is important to remember that at least some of those revenues have to be viewed as temporary. He said the state's improved fiscal picture should set the stage for the Legislature to close the current structural deficit between on-going revenues and expenditures.

House Speaker Jim Weiers closed the morning program by making a strong pitch for the Legislature to address the potential property tax increases that could result from increasing property values. The Speaker pointed out that Truth in Taxation (TNT) has been successful at the state level but most local governments have opted not to adopt the TNT rate. He closed by telling the ATRA audience that, while he didn't always agree with ATRA's policy positions, he appreciated the strong taxpayer advocacy role ATRA plays at the Capitol.



Representative Steve Huffman



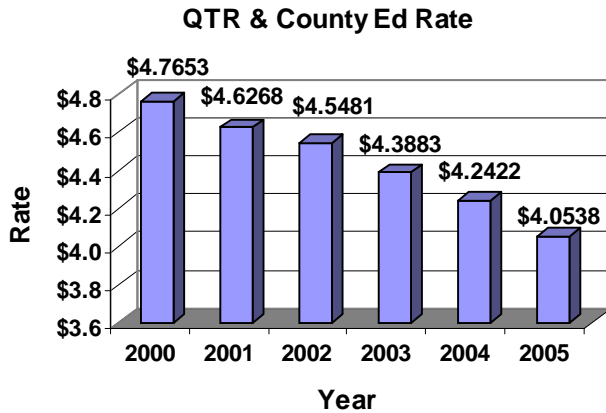
Larry Lucero (left), ATRA's Legislative Policy Committee Chairman, introduces the School Capital Finance Reform panelists at the 2005 ATRA Outlook Conference.

PROPERTY TAXES *Continued from page 3*

tax rate dropped from \$13.27 per \$100 of assessed value in 1995 to \$11.56 this year. However, recent growth in the real estate market will result in significant growth in property valuations, creating opportunities for taxing jurisdictions to ride those valuation increases to huge tax increases.



Kevin McCarthy, ATRA President



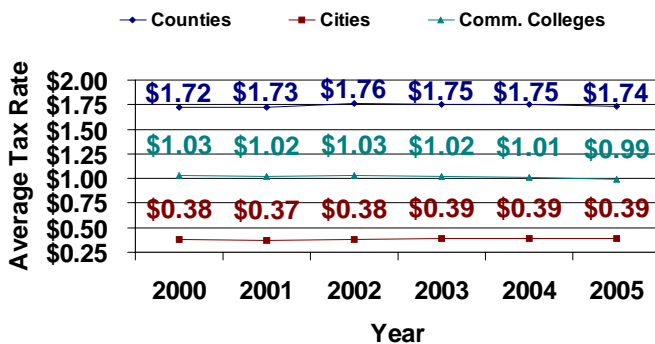
McCarthy pointed out that an attempt to stop property tax increases by simply limiting growth in valuations, which is often debated at the Capitol, would not only not solve the problem but it is also fraught with unintended consequences. Recent proposals to limit valuation growth have been void of any prescriptions for stopping the growth in levies. Inevitably, limiting valuations would create upward pressure on tax rates, exacerbating Arizona's current problem of high business property taxes as well as increasing the number of jurisdictions at the 1% constitutional cap on residential taxes.

McCarthy argued that Arizona's response to potential tax increases in a hot real estate market should be to reduce tax rates. By focusing on the real problem, which is taxes and not value, policymakers could provide more assurance to property taxpayers that they will not experience dramatic growth in their tax bills.

K-12 Statewide Primary Average Tax Rate



Local Government Avg. Tax Rates



McCarthy closed by providing the following ATRA legislative recommendations on controlling property taxes:

Tax Relief: Target state general fund tax relief to property taxes through reductions in the K-12 Qualifying Tax Rate (QTR) or the County Education Rate. The current county education rate of \$0.4358 will raise approximately \$204 million in FY 2006.

Stop the Backfill: For FY 2007, each county, city, and community college district would be required to adopt their Truth in Taxation (TNT) tax rates.

TNT Compliance: Beginning in FY 2008, counties, cities and community colleges would be required to receive voter approval before exceeding their TNT limit for two consecutive years.

Bob Robb, Bob Schuster Highlight Outlook Luncheon Program



Bob Schuster, East Valley Tribune

The Outlook Conference luncheon program was highlighted by remarks from two of Arizona's top editorial writers on fiscal policy.

Bob Schuster, Editorial Page Editor of the East Valley Tribune, and Bob Robb, Columnist with The Arizona Republic, shared their views on major policy issues facing the state and federal government in 2006.



Bob Robb, Arizona Republic

Hunter Leaves ATRA for ABOR

ATRA Vice-President Michael Hunter recently resigned his position with ATRA to accept a position with the Arizona Board of Regents (ABOR). Michael will serve as Assistant Executive Director for Government Affairs for ABOR.

Michael leaves ATRA after eight years of dedicated service, the last five as ATRA's Vice-President. During his tenure with ATRA, Michael served as the association's expert on K-12 and higher education finance.

In making the announcement, ATRA President Kevin McCarthy said "As the association's Vice-President, Michael was an outstanding representative for ATRA. While we will greatly miss Michael's outstanding work, the entire organization wishes him the best of luck at ABOR."



Michael Hunter