



ATRA

Legislative Review



2020

Action without information is dangerous

Information without action is futile

ATRA’s 2020 LEGISLATIVE REVIEW

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The ATRA Legislative Policy Committee meets every Friday during the legislative session to review the impact of all proposed legislation on taxpayers and Arizona's public finance system. ATRA coordinates its advocacy efforts in the Legislature on important public finance and tax bills. Through testimony in committees and dissemination of information to legislators, ATRA serves as the only statewide taxpayer advocate at the Legislature.

The ATRA staff would like to express our gratitude to the members of ATRA's Legislative Policy Committee and Chairman Michelle Bolton for their guidance and effort during the 2020 legislative session. Special appreciation also goes out to members of ATRA's Tax Policy Committee whose knowledge, under the leadership of Chairman Bill Molina, has consistently proven to be indispensable to this organization's success during the legislative session and throughout the year.

During the Second Regular Session of the 54th Legislature, 1,734 bills and resolutions were introduced. Of the 1,607 bills introduced, only 90 passed and were signed into law while none were vetoed by the Governor. Six of the 127 resolutions introduced were adopted by the Legislature. This document summarizes key legislation ATRA supported, opposed, and monitored.

Additionally, ATRA would like to thank ATRA board member Steve Trussell, Executive Director of Arizona Rock Products Association, and his staff for graciously hosting the Legislative Policy Committee meetings.

HIGHLIGHTS OF THE 2020 LEGISLATIVE SESSION

This document summarizes key legislation ATRA actively supported, opposed or monitored during the Second Regular Session of Arizona's 54th Legislature. However, due to the pandemic, the Legislature adjourned in March after passing the FY 2021 budget. The Legislature passed only a small number of bills, two of which were ATRA-sponsored bills that moved early in the process and were ultimately signed by the Governor. Many other bills failed due to the brief session. All of the bills ATRA opposed failed to pass as well.

ATRA staff advocated for several reforms in the areas of Transaction Privilege Tax (TPT), individual income tax, and property tax. ATRA opposed several legislative proposals that would have damaged the state's public finance system or decreased government transparency.

The major legislative issues where ATRA played a key role included the following measures:

- ATRA successfully advocated for legislation under SB1113 that requires county treasurer's to include detailed tax information on the tax notices mailed to property owners. This legislation was necessary following the Maricopa County Treasurer's decision to mail tax statements to property owners with mortgaged property that failed to include any tax information. Rather, these property owners were directed to the county website to obtain such information.
- Following the 2018 Wayfair court ruling that eliminated the physical presence test for the requirement to collect TPT on remote sellers, the cities' quick response to pass an amendment to the Model City Tax Code (MCTC) to apply an economic nexus standard exposed the flaws in the existing process. ATRA led the successful effort in SB1121, which improves the transparency in the process to amend the MCTC.
- Due to the brief session, two ATRA-backed bills that received broad support failed to pass. HB2354 would have extended Arizona's corporate income tax filing deadline on extensions one month after the federal filing due date. HB2106 would have improved the transparency of school financial reporting by requiring school boards to publicly accept their audits.

All bills ATRA actively opposed during the legislative session failed to pass and the following are a few examples:

- Another proposal was introduced to refer to the voters a proposal to raise the 0.6% sales tax for education to a full penny and change the current formula. ATRA opposed this latest effort under SCR1002 because it lacked reforms to the current school finance system. Additionally, the revenue distribution formula put much of the new revenue into higher education and added only a fraction for K-12.
- ATRA opposed an effort by Maricopa County that was designed to circumvent the constitutional expenditure limits by defining public pension unfunded accrued liability as long-term debt obligations. SB1280 would have allowed the exclusion of all pension liability of ASRS, PSPRS, EORP, and CORP to be excluded from the expenditure limits for all counties, cities and towns.
- ATRA successfully opposed legislation that would have provided a targeted tax break to qualified businesses in rural areas of the state for projects that meet certain investment and salary thresholds. Specifically, HB2814 would have classified such property under class 6, which is assessed at 5%, rather than class 1, which is assessed at 18%.

LEGISLATION LISTED BY BILL NUMBER

LEGEND FOR ATRA'S POSITION:

S = Supported FA = Favorably Amended M = Monitored

BILL NUMBER, SHORT TITLE, AND PRIMARY SPONSOR	POSITION	FINAL STATUS/CHAPTER #	PAGE
HB2106 schools; audits; financial records; budgets (Udall)	S	Held in Senate	8
HB2115 JLAC; auditor general (Kern)	S	Held in Senate	8
HB2124 S/E: fire district assistance tax; override (Thorpe)	O	Held in House Technology	7
HB2352 centrally assessed property; valuation; pipelines (Toma)	M	Held in Senate	10
HB2354 income tax; returns; filing extension (Toma)	S	Held in Senate	8
HB2404 TPT; prime contracting; exemptions; certificates (Cobb)	S	Held awaiting House Third Read	8
HB2500 SFB; procurement; building renewal grants (Weninger)	O	Held awaiting House COW	6
HB2681 DOR; administrative rulings; procedures (Toma)	FA	Held in Senate	9
HB2761 property value determination; modifications; verification (Shah)	M	Held House Rules	11
HB2779 state equalization assistance; rate; appropriation (Petersen)	S	Held in Senate	9
HB2814 rural economic development; project certification (Dunn)	O	Held in House Rules	7
HB2823 ambulance service; interfacility transfers (Weninger)	M	Held in House COW	11
SB1113 mortgaged property; tax statements; information (Leach)	S	Chapter 11	6
SB1121 model city tax code; procedures (Leach)	S	Chapter 71	6
SB1280 pensions; unfunded liability; expenditure limits (Mesnard)	O	Held Senate Rules	7
SB1398 tax omnibus (Mesnard)	S	Held in House	9
SB1490 short-term rental properties; classification (Mesnard)	M	Held in House	10
SCR1002 education; TPT; use tax (Brophy McGee)	O	Held in Senate	7

PASSED LEGISLATION ATRA SUPPORTED

SB1113 mortgaged property; tax statements; information (Leach)

Chapter 11

In 2019, the Legislature passed SB1033, which required all fifteen county treasurers mail property tax statements to every property owner. ATRA advocated for this legislation after learning that a handful of county treasurers had ceased sending tax statements to property owners of mortgaged property. Consequently, the property owner was never notified of their property tax liability. Although all county treasurers complied with the mailing requirement during the 2019 tax cycle, the Maricopa County Treasurer failed to provide any tax information for the various amounts owed to each jurisdiction taxing property as other counties. Instead, the only information provided on the notice were the total taxes due, and instead, taxpayers were directed to logon to the county treasurer's website to find any detail on the taxes imposed by the jurisdictions taxing their property. SB1113 requires tax statements mailed to all property owners separately list the primary and secondary taxes due to all taxing jurisdictions and that the statement list the additional amount of the homeowner rebate for class 3 property. *See ATRA position paper in Appendix.*

SB1121 model city tax code; procedures (Leach)

Chapter 71

Following the Wayfair court ruling in 2018 that eliminated the physical presence test for the requirement to collect TPT on remote sellers, the cities quickly proposed an amendment to the Model City Tax Code (MCTC) to apply an economic nexus standard. Regrettably, taxpayers had only one month to consider the MCTC 80-page amendment while simultaneously reacting to legislation at the Capitol to address Wayfair. The cities urgency to rush a lengthy and complicated amendment through the Municipal Tax Code Commission (MTCC) exposed the flaws inherent in the current process.

SB1121 was an ATRA-backed measure that made several changes to improve the transparency in the MTCC process. The bill clarified that a taxpayer or the Department of Revenue (DOR) may propose amendments to the MCTC, in addition to cities and towns. Requires DOR to post the proposed amendment, meeting notice and meeting agenda on its website at least 30 days before an informational public hearing is set, if one is requested. Requires DOR staff to provide the legal analysis on the proposed amendment. Based on comments provided at the informational hearing, the Commission may require changes to the proposed amendment, and if so, DOR is required to post the proposed amendment with any changes on its website within five days of the informational hearing. At least 60 days after the MTCC receives a proposed amendment, the Commission is required to hold a public hearing to consider any information and testimony for consideration to adopt the amendment. The Commission is required to meet in response to any proposed amendment rather than on the second Friday of every other month. *See ATRA position paper in Appendix.*

FAILED LEGISLATION ATRA OPPOSED

HB2500 SFB procurement; building renewal grants (Weninger)

Held House COW

Removed from SFB the authority to have procurement requirements associated with SFB building renewal grants. Allowed SFB to approve BRG projects to proceed using local funds if SFB does not have sufficient appropriations in the BRG fund, which may be reimbursed based on future disbursements. ATRA was opposed because school district procurement code is not prescriptive and allows for uncompetitive procurement strategies. In order to ensure wise use of taxpayer

monies, the scope of projects should not be severed from procurement decisions, and the state ultimately has a considerable interest in the scope of projects where it is providing 100% of the funding. Furthermore, allowing SFB to approve projects based on IOUs is poor publicly policy because it is an advanced appropriation which promises money of future legislatures.

HB2814 rural economic development; project certification (Dunn) Held House Rules

Allowed a county with less than 800,000 persons or a municipality in such a county the ability to create an incentive district which qualifies new projects for Class 6 property if certain investment and salary thresholds are met. The AZ Commerce Authority must approve the district and annually certify the projects qualify for the incentives. Class 6 property is assessed at 5% instead of an 18% ratio under class 1, meaning their property taxes are cut by roughly 73%. ATRA has historically opposed all expansions to Class 6. *See ATRA position paper in Appendix.*

SCR1002 education; TPT; use tax (Brophy McGee) Held in Senate

There were companion referrals in the House and Senate to ask voters to raise the current 0.6% sales tax for education to 1% and revise the appropriation formula. The existing formula sends roughly \$623 million total to K-12 education, \$83 million to Universities and \$25 million to community colleges, although it is rather complex and has several buckets. This referral would eliminate the existing buckets in the Classroom Site Fund and allocate 82% for K-12 classroom education purposes, 13.75% for Universities and dedicated to keeping in state tuition in concert with the Arizona Constitution, and 4.25% workforce development at community colleges.

ATRA opposed this sales tax increase primarily because it lacked reforms to the school finance system. Also, the dilution of the Prop 301 formula, by putting so much revenue in the higher education buckets, added only a fractional amount of money for K-12, eliminating the ability to derive reforms from the funding increase. The bills were heard in the Senate but not in the House. *See also SB1059/HB2742/HCR1032. See ATRA position paper in Appendix.*

SB1280 pensions; unfunded liability; expenditure limits (Mesnard) Held in Senate Rules

SB1280 would have amended statute to define any public pension unfunded accrued liability as a long-term debt obligation as it pertains to the constitutional expenditure limits of counties, cities and towns. This change would have allowed local jurisdictions to exclude the unfunded accrued pension liability of ASRS, PSPRS, EORP, and CORP from their expenditure limits. ATRA viewed this as an attempt by local governments to circumvent the constitutional expenditure limits and opposed the bill in Senate Finance. Sponsor Sen. Mesnard agreed with ATRAs position and explained to the proponents of the bill during the committee hearing that he would only allow the bill to move forward if the relief was limited to lump-sum payments that reduce the total unfunded liabilities and not the required annual payment.

HB2124 S/E: fire district assistance tax; override (Thorpe) Held in House Technology

The strike-everything amendment to HB2124 would have allowed fire districts to seek a permanent property tax override at a regularly scheduled general election to exceed the current tax rate cap of \$3.25. If approved by voters, the tax rate would increase 2% each year until it reached a new tax rate cap of \$4.25. The bill was scheduled to be heard in the House Technology Committee; however, the sponsor held the bill so it was never discussed. The strike-everything amendment to HB2124 was identical to HB2794, which was never assigned to a committee.

FAILED LEGISLATION ATRA SUPPORTED

HB2106 schools; audits; financial records; budgets (Udall)

Held in Senate

HB2106 was an ATRA bill that proposed several changes related to all public school audits and compliance questionnaires. There were four major changes: The bill required LEAs (instead of private auditors) provide the uniform system of financial records (USFR) questionnaire (along with all financial audits) to the Department of Education who will make them publicly available on their website, as they already do with budgets and annual financial records (AFR), improving transparency. It required audits and questionnaires be publicly accepted by school boards to improve board awareness and public accountability. Finally, it required the Auditor General provide the same details it provides ADE to the State Board of Education SBE so they can make audit discrepancy decisions with full context. The bill passed the House unanimously.

HB2115 JLAC; auditor general (Kern)

Held in Senate

HB2115 would have allowed the Office of the Auditor General (OAG) to have access to employees of state agencies, boards, commissions, departments, institutions, programs, advisory councils and committees or political subdivisions of the state in the performance of its official duties. Although this change would have conformed with national auditing standards, this provision was opposed by the community colleges and universities. HB2115 would have also required the OAG to conduct annual, rather than biennial, financial and compliance audits of financial transactions and accounts kept by state agencies subject to federal single audit requirements. Additionally, the bill would have required JLBC staff to notify all the members of the Legislature regarding the cost for any legislative measure that requires the OAG to perform a special audit. Further, the bill required the OAG to conduct a performance audit every five years rather than ten years after a county transportation excise tax is adopted. Due to the opposition to the bill, HB2115 was held in the Senate Government Committee.

HB2354 income tax; returns; filing extensions (Toma)

Held in Senate

Before changes were made to federal filings in the tax cuts and jobs act, corporate filers had one month to process state taxes after federal extended filings were due. For nearly all corporate filers, an extension is sought so their filing is not due until six months after the April deadline. Arizona's corporate filing is due on the same day as the extended federal filing, meaning corporate tax departments must complete the federal and all state filings at the exact same time, causing considerable challenges particularly for multi-state filers. Because state income taxes are based on the federal income tax code, the state filing cannot begin until after the federal filing is complete. HB2354 was an ATRA bill that simply proposed to extend the extended filing date by one month to avoid this timeline complication. The bill passed the House unanimously.

HB2404 TPT; prime contracting; exemptions; certificates (Cobb)

Held in House

The complexities inherent in Arizona's prime contracting classification has led to a high rate of noncompliance. Consequently, the recent reforms that moved maintenance, replacement, repair, and alteration (MRRA) activities out of prime contracting has added confusion for contractors that perform contracts under both activities. HB2404 would have simplified prime contracting by eliminating the thresholds under alteration projects, and instead, contracts that do not add or expand square footage would be subject to tax under retail (MRRA) instead of prime contracting. To reduce the noncompliance rate, HB2404 would have required exemption certificates to be renewed

annually to limit the number of exemption certificates in circulation. Despite the fiscal note from the Joint Legislative Budget Committee (JLBC) fairly noting that the fiscal impact could not be determined without knowing how many alteration projects involve the addition of square footage, the Arizona League of Cities & Towns opposed the bill in the House Ways & Means Committee. The League has continued to argue that any improvements to our burdensome prime contracting class must hold cities harmless, regardless of whether or not its good policy. HB2404 was held awaiting House Third Reading. *See ATRA position paper in Appendix.*

HB2779 state equalization tax; rate; appropriation (Petersen)

Held in Senate

HB2779 was a proposed \$100 million property tax cut by reducing the statewide property tax rate to \$0.2974 in tax year 2020. The bill would have appropriated \$100 million from the state general fund to the Department of Education for state aid, which was an offset to hold school district budgets harmless.

SB1398 tax omnibus (Mesnard)

Held in House

SB1398 attempted several changes in the tax code, with reducing the assessment ratio for business property from 18% to 17% over two years being the most significant change. Effective tax rates in Arizona for commercial property are roughly double those of most states in the region primarily because Arizona shifts property tax burdens through assessment ratios. These assessment ratios have been decreased significantly in the past to neutralize this impact however there are still large discrepancies between classes of property. In order to dull the impact of reducing Class 1 (commercial, industrial) assessment ratio, the bill made slight decreases in the statewide property tax rate (State Equalization Tax Rate) in order to prevent tax shifts between classes.

In addition to property tax reform, the bill made several other changes. It repealed the Highway Safety Fee six months earlier than originally planned, effective January 1, 2021. It added a \$120 annual tax on each vehicle propelled by electricity, natural gas, or propane (or \$44 for a hybrid), which was an effort to create equity between these types of vehicles and gas-powered ones. The maximum tax rate for fire districts increased from \$3.25 to \$3.3750 in tax year 2021 and \$3.50 in tax year 2022 to offset losses of value from the property tax reform.

For income tax, the bill exempted 50% of income attributable to long-term capital gains from assets acquired after Dec 31, 2019 (from current 25%). It further conformed Arizona to the new federal bonus depreciation allowance for C corporations. It raised the dependent tax credit to match the new federal tax credit from \$100 to \$120 per child if under 17 (from \$25 to \$30 for those older than 17). SB1398 passed the Senate 17-12. *See ATRA position paper in Appendix.*

LEGISLATION ATRA FAVORABLY AMENDED

HB2681 DOR; administrative rulings; procedures (Toma)

Held in Senate

HB2681 was a Department of Revenue (DOR)-backed proposal that would have codified a 1996 General Tax Ruling (GTR). Under GTR 96-1, DOR has the authority to interpret the law through the issuance of Tax Rulings and Tax Procedures. ATRA opposed codification of this authority because DOR does not have the authority to make law, rather, it only has authority to administer and enforce existing laws. Due to ATRA's opposition, DOR agreed to remove this provision from the bill.

Another provision in the bill would have amended the section of law that authorizes taxpayers to seek private taxpayer rulings (PTR) from DOR. Specifically, HB2681 would have required DOR to meet with the requestor of a PTR within 30 days after receiving a written request to discuss the facts and circumstances pertaining to the request unless waived by the requestor. At least 30 days before issuing a ruling, DOR would be required to provide the requestor with a draft of the letter ruling. If requested by the requestor, DOR would be required to meet with the requestor within 14 days after providing the draft ruling to discuss the contents of the draft ruling. HB2681 would have also increased the number of days in which DOR must issue a PTR after a request is submitted, from 45 to 90 days, unless both DOR and the requestor agree to delay the ruling. In cases in which DOR declines to issue a ruling, the Department would be required to issue appropriate written assistance or advice to explain the reason issuance of the ruling is declined and to provide a general discussion of relevant tax principles or applications. *Same as SB1347.*

SELECTED LEGISLATION ATRA MONITORED

SB1490 short-term rental properties; classification (Mesnard)

Held in House

Senator Mesnard proposed SB1490 to provide statutory guidance as a result of the inequitable classification of short-term rentals by county assessors across the state. The Senate engrossed version of SB1490 would have classified residential property solely rented to lodgers for periods of less than 30 days and for at least 120 days in a calendar year under class 1, otherwise the property would be classified under class 4. The bill would have excluded rental property in which the owner attests to the county assessor that the property is occupied by the owner for at least 60 days in a calendar year. The bill was held in the House since stakeholders could never reach an agreement.

HB2352 centrally assessed property; valuation; pipelines (Toma)

Held in Senate

The current statutory valuation formula for pipelines is the “base value,” which is the full cash value of the system plant in service in the preceding valuation year before it goes into operation. If not subject to valuation in this state in the preceding year, the value is the net book value of plant in service plus the valuation of construction work in progress, materials and supplies, noncapitalized leased operating property and gas stored underground. In response to many years of litigation involving Transwestern Pipeline that resulted in millions in refunds, HB2352 would have allowed flexibility for the Department of Revenue (DOR) to adjust the “base value” to more accurately reflect the market value of pipeline property. Circumstances to adjust the “base value” used to determine the full cash value (FCV) consisted of the following: a final court ruling that the FCV of a pipeline is more than the market value of the property using standard appraisal methods and techniques, in which case the FCV determined by the court would be the base value for subsequent tax years; when there is an agreement between a pipeline company and DOR resulting from a pending tax appeal in which the parties enter into a binding stipulation that is approved by a court of competent jurisdiction to adjust the base value; an agreement between a pipeline and DOR to correct a material error or omission in the calculation of the base value that is the result of using inaccurate or incorrect information in the past and that has not been corrected. HB2352 was retroactive to tax years beginning from and after December 31, 2015. *Same as SB1204.*

HB2761 property value determination; mods.; verif. (Shah)

Held in House Rules

Current statute requires a Rule B calculation when determining the Limited Property Value (LPV) for property that is modified by construction, destruction or demolition when the total value of the modification is equal to 15% or greater of the full cash value. HB2761 would have required county assessors to physically inspect and verify the total value of the modification to real property before applying Rule B. The bill was opposed by the county assessors in the House Ways & Means Committee on the basis that they rely on aerial photography to determine modifications to real property.

HB2823 ambulance service; interfacility transfers (Weninger)

Held in House COW

HB2823 would have allowed an ambulance service in a county with population of at least three million to apply for a “certificate of operation” from the Department of Health Services (DHS) to provide interfacility transfers. To qualify for the certificate, the applicant would have to own and operate an ambulance service that provides interfacility transports at the location where the applicant’s ambulance company is accredited for the same level of service in another state. Additionally, the applicant would have to obtain a hospital system sponsorship, contract with a third-party vendor to capture and report performance data to DHS, pay the appropriate fees, and file a surety bond. After the initial issuance, the certificate would be for a term of three years, with three-year renewal terms. The bill received heavy opposition and was ultimately held in House COW.

PASSED LEGISLATION ATRA OPPOSED

None.

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2020 LEGISLATIVE PROGRAM

Introduction/State Budget

ATRA's legislative program is developed each year with recognition that the Legislature and Governor's highest priority for the session should be passing a state budget that is not only balanced but sustainable. The preeminent challenge facing state policymakers is ensuring that the Fiscal Year (FY) 2021 budget is structurally balanced – meaning ongoing spending does not exceed ongoing revenue and that one-time revenue (rainy day fund and cash balance) is not appropriated for ongoing spending.

Strong economic growth has driven state tax collections above budgeted estimates for two fiscal years, dramatically improving the state's fiscal condition. The Joint Legislative Budget Committee (JLBC) is estimating that lawmakers will have access to significant one-time revenues for the FY 2021 budget. It is imperative that Governor Ducey and lawmakers carefully distinguish between appropriations that create on-going expectations from obvious one-time expenditures like capital outlays and debt retirement.

ATRA will provide updated state budget recommendations to the Legislature after the JLBC and the Office of Strategic Planning and Budgeting (OSPB) have submitted their recommendations for the FY 2021 budget.

Taxation

Property Tax

Property tax reform. ATRA has led the effort to reform Arizona's property tax system and reduce the disparity in tax treatment between business and residential property. As a result of previous ATRA-backed legislation passed in 2005, 2007, 2011, steady progress has been made in reforming the underlying policies that drive Arizona's high business property taxes. That progress is the direct result of policymakers addressing the root cause of that problem: the shift of taxes from residential property to business through higher assessment ratios on business property.

Most legislative sessions include debates surrounding reforms to Arizona's tax code. ATRA believes any effort to reform Arizona's tax system should include further reductions to the class one assessment ratio with the ultimate goal of 15%. Despite the progress that has been achieved in this area, Arizona's high effective tax rates continue to be the number one tax impediment to industry growth in Arizona.

Prevent greater access to the property tax. For the 2020 session, ATRA will oppose efforts on the part of Arizona State and local governments and special districts to increase access to the property tax base. Despite widespread recognition that Arizona's business property taxes are a major obstacle to economic development, there is considerable pressure each year at the Capitol to increase access to the property tax.

In addition, ATRA will advocate for the continued compliance with the state's Truth-in-Taxation (TNT) law. Since its passage in 1998, the state has consistently complied with the TNT law. For the last five years, the Qualifying Tax Rate and the State Equalization Tax Rate have fallen as a result of the TNT law. While that rate has both risen and fallen with the fluctuations in the real estate market, ATRA believes adherence to the TNT law is an important principle that will benefit taxpayers over time.

Targeted Property Tax Breaks. For decades, ATRA has led the effort at the Capitol to oppose rifle-shot property tax breaks to specific industries. ATRA will continue to support policies that provide for equitable treatment among property taxpayers and oppose efforts that undermine that important policy principle.

For the 2020 session, ATRA will pursue the following legislation:

Reduce the assessment ratio on class one property below the current 18%.

ATRA will support legislation to reduce the assessment ratio on class one property below the current 18% level. The timing and details associated with this proposal remain a work in progress. (Senator J.D. Mesnard)

Mailing Property Tax Bills to Mortgagor

During the 2019 session, ATRA successfully pursued legislation requiring all county treasurers to mail a statement reflecting the current property bill to every mortgagor. Regrettably, the Maricopa County Treasurer chose to only send every mortgagor the total amount of taxes due without any detailed information on the taxes levied by the various jurisdictions. ATRA will pursue legislation making it clear that the tax statement include a breakdown of the taxes owed to each legal entity taxing the property. (Senator Vince Leach)

Sales Tax

Model City Tax Code Transparency

Arizona businesses are burdened with one of the most complicated sales tax systems in the country. Much of that burden is grounded in Arizona's independent municipal sales tax structure that allows cities to levy taxes on a different tax base from the state and counties. In an attempt to address the chaos associated with various city tax structures, Arizona cities created the Model City Tax Code (MCTC) in 1987, and in 1988, Arizona policymakers created the Municipal Tax Code Commission (MTCC) to oversee amendments to the MCTC. In 1999, lawmakers stripped cities and towns of the authority to adopt tax ordinances not included in the MCTC. Following confusion regarding the responsibility and location of the official version of the MCTC, Arizona lawmakers passed legislation in 2011 requiring the Arizona Department of Revenue (ADOR) to maintain the official version of the code. In 2013, led by Governor Brewer, lawmakers preempted cities on local collection of sales and consolidated audit authority at the state level.

In 2020, ATRA will pursue legislation to simplify, streamline and create transparency for the process to amend the MCTC. The legislation will clarify that any party can pursue amendments to the MCTC as well as simplifying the public notification requirements for ADOR that currently staffs the MTCC. (Rep. Ben Toma)

Prime Contracting Simplification

In 2012, Governor Brewer’s TPT Simplification Task Force recommended the state “aggressively” transition from the current prime contracting tax to a tax on materials at retail. In the years following that recommendation, the Legislature changed how TPT is applied to activities involving maintenance, repair, replacement, and alteration (within certain thresholds) from prime contracting to a tax on materials at the point of sale, now known as MRRA.

MRRA simplified tax compliance for contractors that only work on MRRA projects; however, those complications were shifted to contractors involved in both MRRA and prime contracting activities. In 2017, Rep. Regina Cobb sponsored legislation that required ADOR commission a study to determine the noncompliance under prime contracting. The study showed that the state lost approximately \$1 billion in tax revenue between 2006 and 2010. ATRA will support legislation to simplify the tax compliance for MRRA and prime contracting projects. (Rep. Regina Cobb)

Corporate Income Tax

Extending Arizona’s corporate income tax filing deadline

ATRA will pursue legislation to extend Arizona’s corporate income tax filing deadline by 30 days. Currently the deadline for filing Arizona’s corporate income tax returns coincides with the deadline for filing the federal corporate income tax return. This change will provide considerable administrative compliance relief to Arizona corporations as well as improve the quality of their Arizona corporate tax filings. (Rep. Ben Toma)

Public Finance

Transparency of K-12 School Audits

In an effort to drive more transparency over the state’s largest expenditure, ATRA will pursue legislation to make it easier for private citizens to access public school audits and compliance questionnaires. Presently, many districts and charters (LEAs) do not make these available and they must be requested through FOIA. Audits often do not describe compliance with state laws and rules, making compliance questionnaires a critical tool for monitoring these agencies. Additionally, it is reported that governing board members are often unaware of the results of these audits and are either not discussed at board meetings or quietly adopted in consent agendas. If an LEA is reported by the Auditor General for noncompliance, little detail is presently provided to the State Board of Education, who is charged with enforcing remedies for noncompliance.

State law should demand important documents such as audits and questionnaires be made easily accessible to the public. The Department of Education already publishes budgets and the annual financial reports on their website for each district and charter; audits and questionnaires should be similarly accessible. Governing Boards should publicly accept these documents by roll call vote, closing the accountability loop on these important reviews. It also gives the board and the public the opportunity to discuss them. Finally, the bill would require the Auditor General detail in writing the deficiencies of noncompliant LEAs to the State Board and Department of Education to empower their decision making. (Rep. Michelle Udall)



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ATRA SUPPORTS HB2106

Closing the Accountability Loop on School Audits

HB2106 makes several changes in Title 15 related to all public school audits and compliance questionnaires. There are four major changes:

1. **Compliance Questionnaire transparency:** All school districts and charters (LEAs) must complete an annual compliance questionnaire with their auditor to ensure compliance with state laws related to the uniform system of financial records (USFR). However, they are often difficult to find if a district has not made them available on their website. Also, independent auditors were not always making them available to county school superintendents as required by law. HB2106 requires LEAs (instead of private auditors) provide these documents (along with all financial audits) to the Department of Education who will make them publicly available on their website, as they already do with budgets and annual financial records (AFR).
2. **Board Awareness:** Elected school board members should be aware of all audits and compliance questionnaires. The public should also have the opportunity to see and comment on these reports at board meetings. HB2106 requires audits and questionnaires be publicly accepted by school boards.
3. **State Board of Education (SBE) Awareness:** When the SBE is brought a problem from the Auditor General on LEA misspending or noncompliance, there is little detail of the extent of the problem. This is the only meaningful opportunity for these issues to be made public, and the SBE should have the detail to understand the nuance of the situation. The change in 15-271 requires the Auditor General provide the same details it provides ADE to the SBE so they can make decisions with full context.
4. **Requirement simplification:** A.R.S. §15-905 is changed to no longer require school districts file their budgets with the county school superintendent, which is a historical requirement that is no longer necessary. Budgets are electronically passed to ADE for acceptance, where counties can easily access them.

Public documents like audits and questionnaires should be publicly available and easy to find. HB2106 helps close the accountability loop on these documents. Importantly, it will help the SBE make decisions how to manage noncompliant LEAs by providing them more context. Lastly, it removes an outdated requirement for school districts related to budget posting. **ATRA encourages lawmakers to vote Yes on HB2106.**



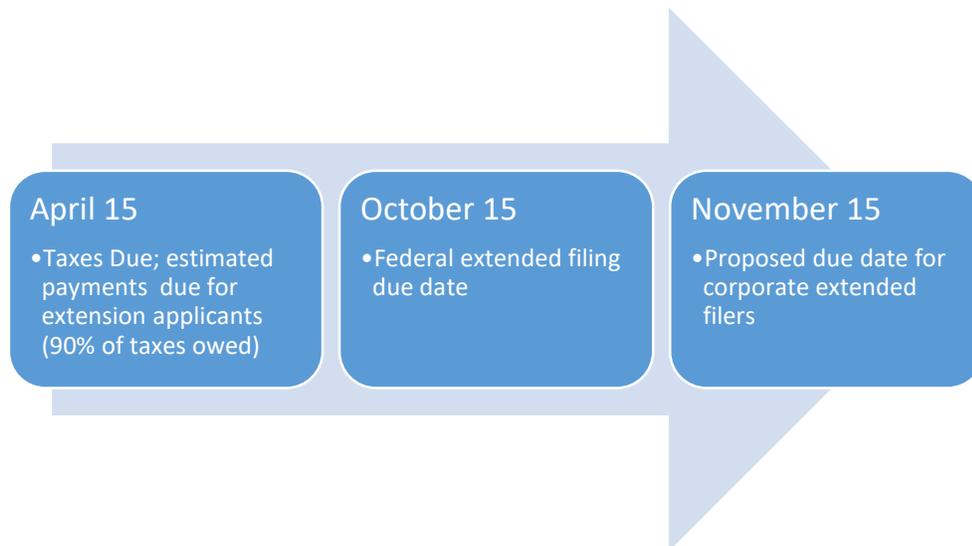
The taxpayer's watchdog for 80 years

ARIZONA TAX RESEARCH ASSOCIATION

ATRA SUPPORTS HB2354

Provide Filers a 1-Month Cushion for Extended Filers

Before changes were made to federal filings several years ago, corporate filers had one month to process state taxes *after* federal extended filings were due. For nearly all corporate filers, an extension is sought so their filing is not due until six months after the April deadline. Arizona's corporate filing is due on the same day as the extended federal filing, meaning tax departments must complete the federal and all state filings at the exact same time, causing considerable challenges particularly for multi-state filers. Because state income taxes are based on the federal income tax code, the state filing cannot begin until after the federal filing is complete.



HB2354 simply adds one month to the due date for extended corporate state filings, meaning they will be due seven months after the original due date instead of six. This will give corporate filers enough time to file their federal taxes and then finish state taxes with improved fidelity. This will have little to no impact on revenues, because those who apply for an extension must pay 90% of their estimated taxes in April, so the amounts paid after the extensions are rather small and would only be delayed by a maximum of one month and will occur in the same fiscal year. **ATRA encourages lawmakers to vote Yes on HB2354!**



The taxpayer's watchdog for 80 years

ARIZONA TAX RESEARCH ASSOCIATION

ATRA SUPPORTS HB2404

Simplifying MRRA under Prime Contracting

Background

Arizona's prime contracting tax is generally regarded as the most complex and inefficient area of Arizona's transaction privilege tax (TPT) system. Unlike most other states that tax materials at retail, Arizona's prime contracting tax system allows contractors to purchase materials tax-free at retail with the use of exemption certificates, and instead, pay taxes on 65% of the gross proceeds of the contract upon completion of the project. The ability to purchase materials tax-free on an honor system can certainly lead to noncompliance- not an ideal feature of any tax system.

In 2012, Governor Brewer's TPT Simplification Task Force recommended the state "aggressively" transition from the current prime contracting tax to a tax on materials at retail. Although a total elimination of prime contracting was not accomplished, the Legislature did achieve carving out certain activities from the contracting tax to a tax on materials at retail that involved maintenance, repair, replacement, and alteration (within certain thresholds), now known as MRRA.

All maintenance, repair, and replacement activities were moved from prime contracting to retail. However, for "alteration" projects to qualify under MRRA and remain subject to the retail tax, certain thresholds could not be exceeded. For residential property, the contract price for the alteration cannot exceed 25% of the property's full cash value and for commercial property if all of the following are true: 1) the contract amount is \$750,000 or less; 2) scope of the work is 40% or less of the existing square footage; and 3) scope of the work includes an expansion of 10% or less of the existing square footage. For either a residential or commercial contract, a 25% cushion was provided to accommodate changes to contracts that may initially qualify under MRRA without being pulled back into prime contracting.

MRRA simplified tax compliance for contractors that only work on MRRA projects; however, those complications were shifted to contractors involved in both MRRA and prime contracting activities. At the urging from this new hybrid of contractors, President Karen Fann introduced legislation in 2018 to eliminate MRRA and shift all contractors back into prime contracting. ATRA strongly opposed that effort since it would have reversed the progress made under MRRA. After much negotiation, legislation was agreed upon that simplified MRRA for commercial alteration projects to contract amounts of \$750,000 or less, regardless of square footage.

Based on a legislative appropriation requested by Rep. Regina Cobb in 2018, ADOR was required to commission a study to determine the noncompliance under prime contracting. That study was released in January 2019 and reported that noncompliance was as high as 19% between 2010 and 2016. Utilizing similar methods as the IRS and augmented by state-provided tax returns and audit results, the state lost approximately \$1 billion in tax revenue over that period of time. Specifically

as it pertains to the use of exemption certificates in which there is no third-party information to substantiate against, the noncompliance rate can be as high as 63%.

ATRA supports HB2404 since it will greatly simplify prime contracting by allowing projects to remain under MRRA if the activity doesn't involve adding or expanding square footage. Furthermore, the provision to limit exemption certificates to one-year will help to reduce the current noncompliance in the system.



The taxpayer's watchdog for 80 years

ARIZONA TAX RESEARCH ASSOCIATION

ATRA SUPPORTS SB1113

Require Property Tax Statements Include Tax Information

Arizona's property tax system is one of the most complicated in the country, and therefore, taxpayer education is imperative.

The county assessor annually determines both the Full Cash Value (FCV) and the Limited Property Value (LPV), and no later than March 1st each year, is required to mail the property notice of valuation (NOV) to all property owners.

During the budget process, local governments make tax and expenditure decisions to determine their annual budgets. Counties, in particular, go to great lengths to educate taxpayers how much of their tax bill is levied by the various taxing entities. More importantly, local jurisdictions are required to publish notice and hold Truth-in-Taxation (TNT) hearings when they intend to increase property taxes.

Once those budgeting decisions are made, tax rates and levies are adopted in August. The county treasurer is then responsible for collecting the applicable taxes after applying the adopted tax rates to all taxable values. The tax statement is the only place a homeowner sees their bill, plus information about their "homeowner rebate," where the state pays 48% of the K-12 primary property tax obligation.

In 2019, the Legislature passed SB1033, which required all fifteen county treasurers mail property tax statements to every property owner. ATRA advocated for this legislation after learning that a handful of county treasurers had ceased sending tax statements to property owners of mortgaged property. Consequently, the property owner was never notified of their property tax liability.

Although all county treasurers complied with the new requirement this last tax cycle, one county treasurer failed to provide any tax information for the various amounts owed to each jurisdiction taxing the property as other counties. Instead, they only provided the total amount of tax due. Rather, property owners were directed to log on to the county treasurer's complex website to find the taxes imposed by the jurisdictions taxing their property.

The property tax statement serves as a transparent link between government and taxpayers. It reflects the final decisions made by the various taxing jurisdictions during the budgeting process. Property owners should not be told to log in to a website in order to retrieve information that can easily be printed on the notice they receive in the mail.

ATRA ASKS LAWMAKERS TO VOTE YES ON SB1113!



The taxpayer's watchdog for 80 years

ARIZONA TAX RESEARCH ASSOCIATION

ATRA SUPPORTS SB1121

Model City Tax Code Transparency

Background

Arizona businesses are burdened with one of the most complicated sales tax systems in the country. Much of that burden is grounded in Arizona's independent municipal sales tax structure that allows cities to levy taxes on a different tax base from the state and counties.

In an attempt to address the chaos associated with various city tax structures, Arizona cities created the Model City Tax Code (MCTC) in 1987, and in 1988, Arizona policymakers created the Municipal Tax Code Commission (MTCC) to oversee amendments to the MCTC. In 1999, lawmakers prohibited cities and towns from adopting tax ordinances that were not included in the MCTC. Following confusion regarding the responsibility and location of the official version of the MCTC, Arizona lawmakers passed legislation in 2011 requiring the Arizona Department of Revenue (DOR) to maintain the official version of the code.

Prior to January 2019, the MTCC had not met for four years. However, following the *Wayfair* court ruling in June 2018 that eliminated the physical presence test, the cities quickly proposed to amend the MCTC to apply an economic nexus standard to impose sales tax on remote sellers. Regrettably, taxpayers had only one month to consider this 80-page amendment. At the same time, the Legislature was considering legislation to address *Wayfair*. Consequently, taxpayers had little time to consider and react to the MCTC proposed amendment, while simultaneously deliberating on the *Wayfair* legislation at the Capitol. And under the current MTCC process, taxpayers are only provided one opportunity to formally address the MTCC regarding proposed amendments and that is on the day the Commission is scheduled to adopt the amendments. The cities urgency to rush a lengthy and complicated amendment through the MTCC magnified the flaws inherent in the current MCTC amendment and hearing process.

Basis for ATRA's Support

SB1121 seeks to simplify, streamline and create transparency for the process to amend the MCTC. SB1121 will accomplish the following:

- ❖ Meetings are called by the chairman of the MTCC in response to any proposed amendment instead of the second Friday of every other month.
- ❖ Clarifies that DOR and any taxpayer may propose an amendment to the MCTC, in addition to a city or town.
- ❖ Requires proposed amendments to be submitted to DOR at least 60 days prior to adoption by the MTCC.
- ❖ Requires DOR to post the proposed amendment, meeting notice, and agenda to its website at least 30 days prior to the MTCC holding an informational hearing.

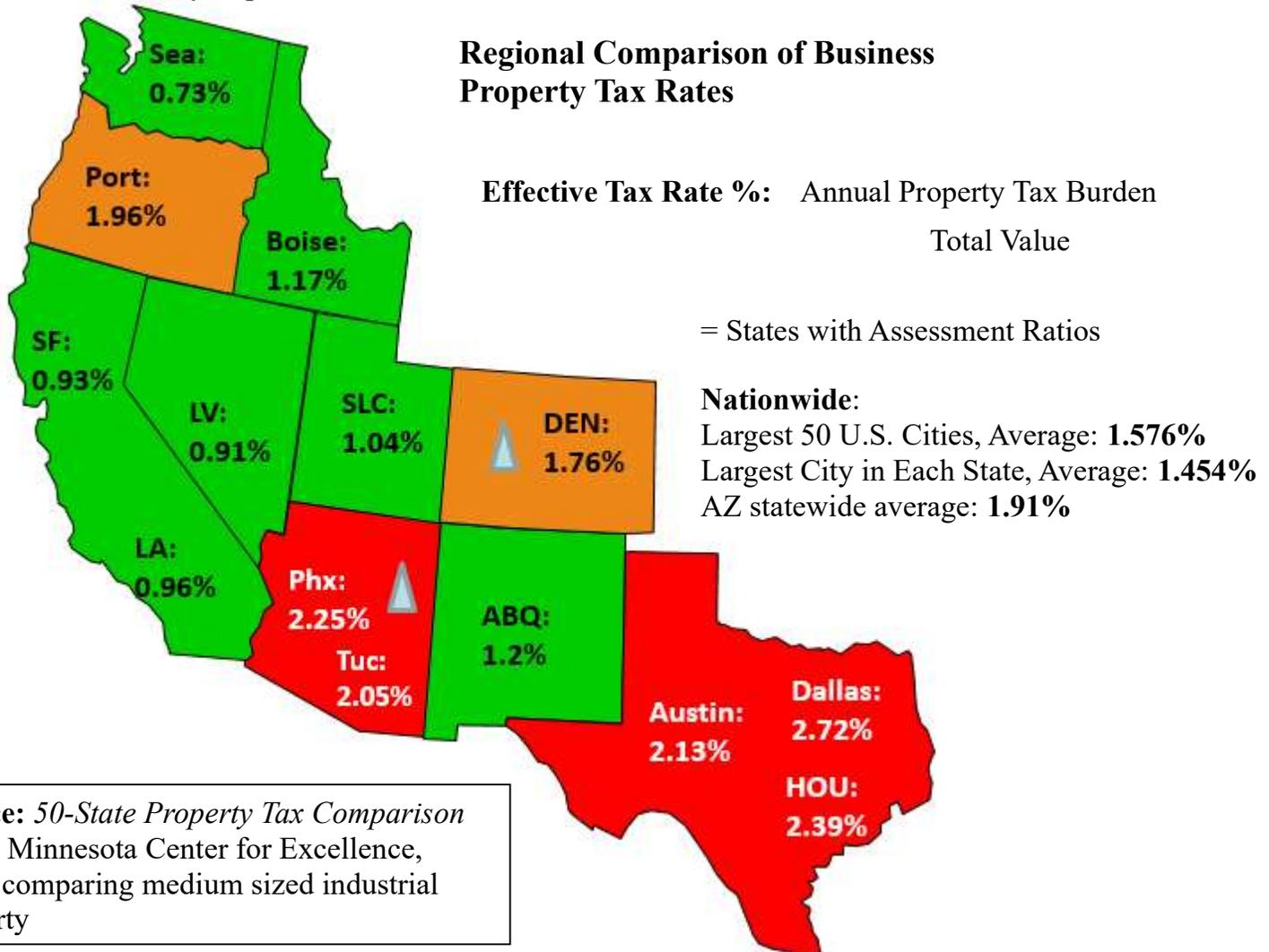
- ❖ At the informational hearing, DOR staff is required to provide the legal analysis to the MTCC.
- ❖ Following an informational hearing, any changes to the proposed amendment must be posted to the DOR website within five days following the hearing.
- ❖ At least 60 days after receiving a proposed amendment, the MTCC is required to hold a hearing to consider adoption of any amendment.

ATRA ASKS LAWMAKERS TO VOTE YES ON SB1121!

THE ARIZONA BUSINESS COMMUNITY SUPPORTS PROPERTY TAX REFORM – SB1398

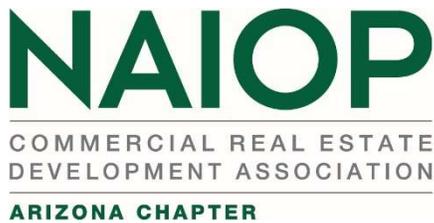
Right Size Arizona’s Business Property Tax

- Lowering the Class 1 Assessment Ratio from 18% to 17% continues to move the state towards a more equitable, sustainable property tax base
- Arizona’s business property taxes are uncompetitive
- AZ ranks high both regionally and nationally in business property taxes
 - Creates demands for incentives for well-connected or new businesses
 - Masks homeowners to the true cost of government
- Lowering the State Equalization Rate avoids tax shifts, gives all taxpayers a small tax cut, & avoids any impact to K-12 education formula



Source: 50-State Property Tax Comparison Study, Minnesota Center for Excellence, 2019, comparing medium sized industrial property

ORGANIZATIONS IN SUPPORT



WHAT ARE ASSESSMENT RATIOS?

After property is valued, a ratio is applied to determine how much will be subject to tax

At 18%, business property in Class 1 pays nearly double that of homeowners and renters

Business property subsidizes other classes of property by roughly \$829 million annually

Though Class 1 only makes up 21% of statewide total value, it pays 35.6% of total property taxes

WHAT'S THE DEAL WITH FOREIGN TRADE ZONES, CLASS 6, GPLET, & OTHER LEASEBACK DEALS?

The desire to avoid Arizona's high business property taxes is strong

Businesses seek shelter in lower tax areas, or request incentive deals to develop property

Policymakers can either reform the system, or face more demands for targeted tax breaks



ATRA OPPOSES HB2814

Providing targeted property tax breaks is bad policy

Background

HB2814 allows counties, cities and towns to provide targeted property tax breaks for businesses that have specific levels of investment in counties with population less than 800,000.

In counties with population of 250,000 but less than 800,000, the minimum capital investment is \$25 million. In a county with population of less than 250,000 and for cities and towns in counties with population of 250,000 or more but less than 800,000, the minimum investment is as follows: For cities with population of 80,000 or more, \$10 million; for cities with population of at least 15,000 but less than 80,000, and in unincorporated areas of the county, \$5 million; for cities with population less than 15,000, \$1 million. The minimum number of employment positions is determined by the city, town or county and must be paid an average of 100% of the county median wage.

Upon meeting the above requirements, the real and personal property of the qualified business is classified under class 6, which is assessed at 5% for ten years or until the development costs have been recouped, compared to all other business property, which is classified under class 1 and assessed at 18%.

Basis for ATRA's Opposition:

Arizona has considerably higher business property taxes compared to other states as a result of Arizona's long-standing policy to shift the burden from residential property (class 3), which is assessed at 10%, to business property (class 1), which is currently assessed at 18%. Based on a 2018 study published by the Minnesota Taxpayer's Association, the property tax burden on Arizona industrial property ranks 6th highest compared to other states. Lawmakers have made considerable progress in reducing the assessment ratio over the years, from 25% in 2005 to the current ratio of 18%. Furthermore, Arizona statutes provide additional depreciation on business personal property, commonly referred to as "accelerated" depreciation, within the first five years of acquisition. The Legislature has enhanced the accelerated depreciation schedule several times over the last decade in an effort to encourage businesses to purchase new equipment. Factoring in the benefits of accelerated depreciation for businesses dramatically improves Arizona's ranking compared to other states.

Proponents are correct that Arizona's high business property taxes are an impediment to economic development in Arizona. Those high business property taxes are the result of the inequities in Arizona's property tax system. However, their misguided approach to dealing with high business property taxes by creating targeted tax breaks actually creates more inequities in the property tax system and higher taxes on all other taxpayers, including existing businesses and homeowners. Arizona's high business property tax problem should not be solved by targeted relief to select businesses thereby making taxes even higher for other business taxpayers.

Additionally, the Arizona Constitution under Article 9, Section 1, states that “all taxes shall be uniform upon the same class of property within the territorial limits of the authority levying the tax.” While the courts have given the Legislature broad discretion in creating different classes of property, they have also cautioned that those distinctions in use, purpose or industry must be “real” and not be “arbitrary, specious or fanciful.” In addition to being bad policy, ATRA believes that creating such disparate tax treatment between identical companies in the same taxing jurisdiction based solely on the size of the investment is unconstitutional.

The only thing worse than passing this legislation is to have the law pass and have businesses make the required level of investments with the anticipation of receiving huge tax incentives, only to have the law invalidated by the courts.

ATRA believes that the property tax breaks provided in HB2814 are bad policy and serve to exacerbate problems in Arizona’s property tax system.



ATRA OPPOSES SCR1002

The proposed “full penny” TPT (sales) tax increase proposal is poor public policy for three distinct reasons: 1) the tax increase provides no necessary education reforms, 2) it undermines the Classroom Site Fund, and 3) unnecessarily dilutes the K-12 share.

A full penny sales tax could raise a conservative \$1.2 billion ongoing. The following is a breakdown of

	FY2020 (Est)	Penny Tax Proposed			
SFB Debt Service	\$ 64,125,400				
Universities	\$ 86,469,200	\$ 222,743,900			
Community Colleges	\$ 21,617,300	\$ 55,585,975			
Tribal Assistance	\$ 806,900	\$ 2,000,000			
Additional School Days	\$ 86,280,500	\$ 86,280,500			
School Safety	\$ 7,800,000				
Character Grants	\$ 200,000				
SAIS	\$ 7,000,000				
Failing Schools Fund	\$ 1,500,000				
Income Tax Credit	\$ 25,000,000				
Classroom Site Fund	\$ 483,903,100	\$ 835,289,625			
			Delta	% increase	% of new funds
K-12 Total	\$ 650,809,000	\$ 921,570,125	\$ 270,761,125	42%	61%
Universities Total	\$ 86,469,200	\$ 222,743,900	\$ 136,274,700	158%	31%
Comm College Total	\$ 22,424,200	\$ 57,585,975	\$ 35,161,775	157%	8%

Source: JLBC; ATRA estimations using JLBC data + new formula
FY2019 JLBC data.

Penny Tax Proposal Includes No Education Spending Reforms

For decades, education leaders have sought to reform uneven policies such as arcane hold harmless formulas, which allow the same pupil to draw different funding depending on which school they enroll. This is unfair and likely unconstitutional. There is widespread agreement that bringing equity to Arizona’s school system will cost money. **The conclusion of the two-year Classrooms First Council was that while reforms are necessary, they will not be achieved without new funding.** To bypass another opportunity at reform is a critical misstep. Opportunities for tax increases are rare and should include something for everyone, including taxpayers. Taxpayers deserve a system that is fairer and less susceptible to lawsuits. Parents deserve a system where their pupil is worth roughly the same no matter the public school they attend. This proposal simply adds money to an outdated and outmoded finance system.

Proposal Removes Performance Funding

One of the major selling points in Prop 301 was the addition of performance based funding for teachers. Lawmakers proposed and voters approved a portion of Classroom Site Fund dollars be set aside for performance based bonuses. **Removing this feature signals a return to bureaucratic teacher pay**, where teachers are paid only according to a traditional pay scale. Teachers should be acknowledged and rewarded for making gains in student achievement, not saddled with a one-size-fits-all pay scale.

New Formula Dilutes the K-12 Share

The new formula adds to K-12 schools just shy of \$300 million more than they would get from the existing formula (this accounts for maturing SFB debt service, which adds to the Classroom Site Fund at the end of FY 2020). **A sales tax increase which moves Arizona near the top of the nation in total rates should buy more than a 2.5% bump in K-12 funding** (using JLBCs FY 20 \$12.2B estimate). While it's understandable that advocates want to "spread the money" to all public education, it's hard to argue university and community college needs require 158% and 157% increases in their sales tax funding.

With Prop 123, the 20x2020 plan, and District Additional Assistance restoration, **the state has committed \$1.3+ billion to K-12 education in the last several years without any finance reform**. This doesn't account for increases in population and inflation funding, School Facilities Board increases and other new funds. This ~\$300M increase to K-12, which amounts to roughly 61% of new available funds, amounts to less than \$265 per pupil statewide and creates little opportunity for reform.

The Juice Isn't Worth the Squeeze

Convincing taxpayers to open their wallet is always a challenge. They should be respected enough to offer reforms which improve Arizona schools, not simply add funds. Among other reforms, Prop 301 phased out the expensive and unequal Excess Utilities fund. This one-cent sales tax plan lacks reform, sends the wrong message to teachers and won't solve budgetary challenges for schools.