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ARIZONA TAX RESEARCH ASSOCIATION

NEWSLETTER

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ATRA's 2006 Legislative Program Moving

The ATRA staff has been aggressively pursuing the 2006 legislative agenda adopted by the Board of Directors.

ATRA has aggressively monitored and publicized Arizona's on-going state general fund structural deficit. For the last six fiscal years, the state Legislature and Governor have adopted spending plans that exceeded on-going revenue. Fortunately, the fiscal year (FY) 2006 budget reduced the overall deficit from \$534 million in the adopted FY 2005 budget to \$273 million for FY 2006. Arizona's state spending continues to climb at a rapid clip, with FY 2006 spending up 14% over FY 2005. (When the \$250 million cash financing for SFB is excluded, state spending growth drops to 10.7%.) Current revenue estimates will again provide the Legislature and Governor the opportunity to close the budget deficit and avoid the budget gimmickry that has characterized recent state budgets.

ATRA will again make specific recommendations to the Legislature where opportunities exist for better financial management and to clean up sloppy state spending practices. In addition to adopting a truly balanced budget, ATRA recommends that the Legislature make a serious effort in 2006 to improve its budgeting process.

The following is an overview of the major issues ATRA will advocate for this session:

Property Tax

Both commercial and residential property values have increased dramatically in the last two years. Without some legislative action taken to prevent it, those increased property values will result in property tax

increases across Arizona. In the last five years, Arizona's net assessed valuation has climbed \$17.1 billion or 54%. Recent market activity will force county assessors to increase taxable valuations at an even higher percentage.

TAX RELIEF: When property values increase, the only way to protect property taxpayers from significant increases in their tax bills is to reduce tax rates. ATRA recommends that the Legislature direct tax relief this year to property taxes by either eliminating or significantly reducing the county education equalization rate. The Legislature could provide roughly \$205 million in property tax relief through the elimination of this rate, which is currently set at \$0.4358. (Although labeled a "county education" rate, this tax rate is controlled by the state and its elimination would not affect the funding for either county government or K-12 schools.)

STOP THE BACKFILL: The fear of most property taxpayers is that local governments will ride the significant property valuation growth to huge tax increases by failing to adjust tax rates downward. In order to ensure that taxpayers see the effect of the state's effort to reduce rates, ATRA recommends that the Legislature mandate that each county, city or town and community college district adopt their Truth-in-Taxation (TNT) rate for tax year 2006. This provision does not require local governments to reduce taxes. It simply requires them to participate in the effort to mitigate the damage that could be done with huge property tax increases.

TNT COMPLIANCE: Arizona's TNT laws, passed in the late 1990's, have had varied

Hawkeye Wilson Joins ATRA Staff



This month, Hawkeye Wilson accepted a Senior Research Analyst position with ATRA, serving as a specialist in K-12 and higher education finance issues. Mr. Wilson replaces former Vice President Michael Hunter who became an Assistant Executive Director for Government Affairs at the Arizona Board of Regents.

Hawkeye previously worked at UpSlope Solutions, an Arizona-based K-12 professional development firm, and was responsible for marketing and selling its program to the state's public, private and charter school districts. Prior to that, he co-founded a consulting firm in Washington, DC, The Consilium Group, which provided knowledge management solutions to educational organizations across the country.

Hawkeye's classroom experience reaches to Tianjin, China, where he taught English as a Second Language at Nankai University. He also worked in Washington, DC on Capitol Hill, initially as an intern

ATRA Legislative Program

success. TNT at the state level (the state's requirement to adjust to the qualifying tax rate (QTR) for K-12 schools and the county education equalization rate) has been very successful. The state has adopted the TNT rates every year since the law has been in effect; however, at the local level, TNT has been less successful. Despite dramatic growth in property values, the primary tax rates of counties, cities and community colleges have not decreased accordingly. ATRA recommends that, beginning in tax year 2007, counties, cities and community colleges be required to receive voter approval before exceeding their TNT limit two consecutive years in a row.

ATRA property tax relief bills are SB1289, sponsored by Senator Dean Martin, and HB2685, sponsored by Representative Steve Huffman. SB1289 has cleared the Senate Finance Committee.

School Finance

◆ **Tax Rate Cap/1% Districts** – For the third year in a row, ATRA will pursue this recommendation from the Tax Reform for Arizona Citizens Committee (TRAC). Last year's bill (HB2143) was vetoed by Governor Napolitano. This legislation would cap the primary tax rates of school districts with a combination of 50% or more of their residential taxpayers at the 1% cap and a primary rate that is 150% of the QTR. Enforcement would be given to the Property Tax Oversight Commission (PTOC). SB1206 is sponsored by Senator Robert Burns and has cleared both the Senate Finance and Senate K-12 Education committees and waits a floor vote in the Senate.

◆ **Capital Outlay Overrides** – ATRA will again pursue legislation to limit the taxing authority of school districts levying for capital outlay overrides. That limit would

be placed at 75% of the districts soft capital allocation.

◆ **Transportation Spending** – A major flaw in Arizona's school finance system results in significant property tax burdens in some school districts. Statewide, Arizona property taxpayers are saddled with \$54 million in levies to fund the transportation costs for students who are no longer in the school district. School districts have one transportation funding limit that tracks the actual students in the district – the transportation support level (TSL). However, a second transportation limit, the TRCL, tracks the highest level for transportation spending for the district since the early 1980's. In many school districts, the TRCL is two to three times higher than the TSL. Because the state only provides funding for the TSL, the gap between the TSL and the TRCL is funded solely by the local property tax.

ATRA will pursue legislation to prohibit increases in a school district's transportation revenue control limit (TRCL) if the calculated amount exceeds 120% of the transportation support level (TSL). SB1205, sponsored by Senator Burns, cleared Senate Education and Senate Appropriations.

Sales Tax

◆ **Prime Contracting** – Tax compliance continues to be difficult for taxpayers that are required to pay Arizona's prime contracting tax. Further, what constitutes the tax base for prime contracting continues to evolve. This session, ATRA is supporting SB1068 (Martin) that excludes from the prime contracting tax base the development fees charged by local governments. This exemption will eliminate the current double taxation that occurs when development fees become a part of the taxable contract under prime contacting. SB1068 passed the Senate and has been transmitted to the House.

Corporate Income Tax

◆ **Net Operating Loss Carryforward** – ATRA will support legislation to mirror Federal law and extend the current five-year limit on net operating loss carryforwards to 20 years. HB2341 was introduced by Representative Steve Huffman and was also amended onto the Federal Conformity bill (SB1156) in the Senate by Senator Martin.

◆ **Federal Conformity** – ATRA will continue to support full state conformity with the Federal IRC. Introduced by Senator Martin (SB1156), this bill cleared the Senate and has been transmitted to the House.

Public Finance

◆ **Students FIRST Reform** – ATRA has proposed comprehensive reforms to Arizona's school capital finance program. For a complete version of ATRA recommendations, visit the legislative advocacy page on ATRA's website at www.arizonatax.org.

◆ **Public Health Service Districts** – Arizona counties have the authority to create Public Health Service Districts without voter approval. To date, Navajo and Yuma Counties have created such districts by a unanimous vote of the Board of Supervisors. ATRA will pursue legislation that would require a county board to receive voter approval prior to creating a Public Health Service District. Senator Martin is the sponsor to SB1392 and has scheduled it for the Senate Finance Committee.

◆ **Unpublished Tax Decisions** – ATRA will pursue legislation to require state and local agencies to publish substantive tax decisions on their website. Representative Steve Yarbrough is the sponsor of HB2712, which passed the House Ways & Means Committee and is waiting to be heard in the House Judiciary Committee.



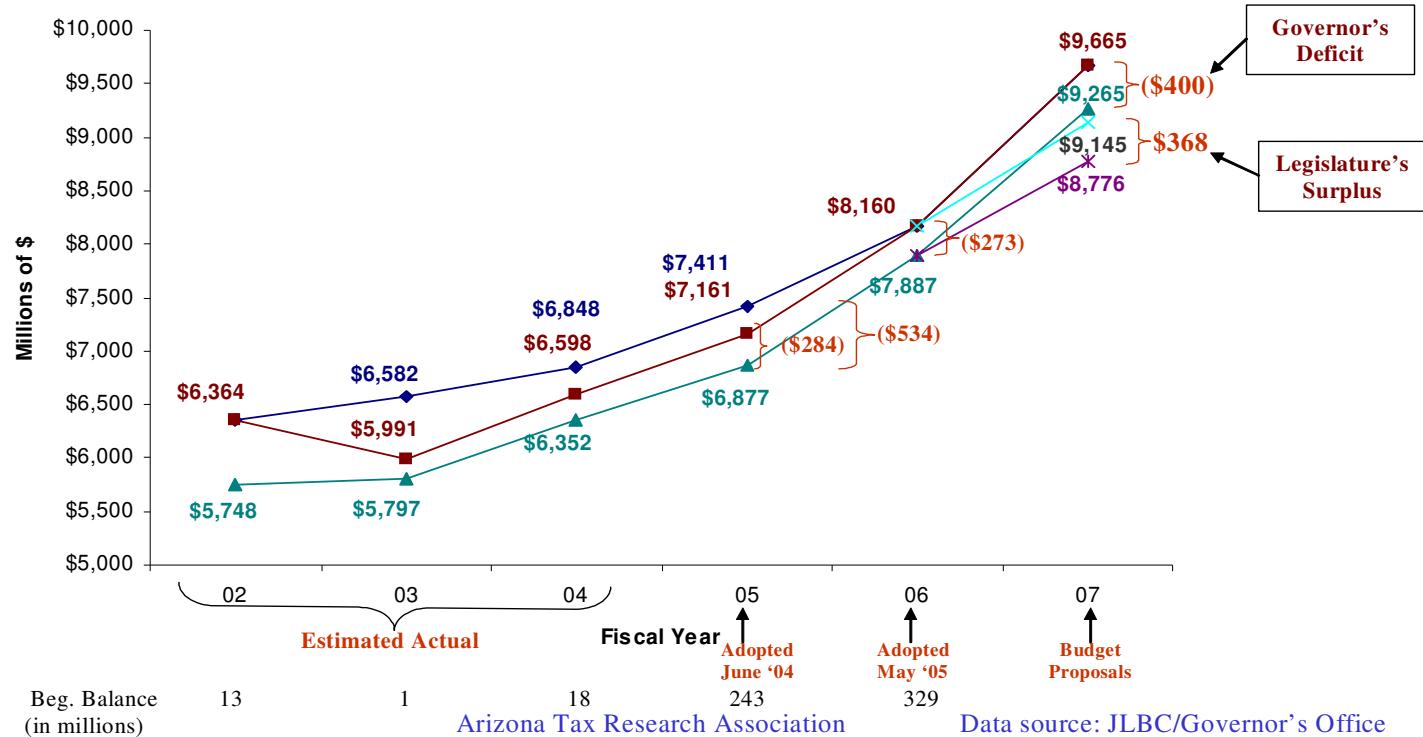
GOVERNOR, LEGISLATURE OFFER DRAMATICALLY DIFFERENT BUDGETS

Governor/Legislature's FY '07 Budget Proposals

Comparison of On-going General Fund Revenues & Expenditures

Excludes beginning balance, one-time revenues & expenditures, & Prop 301

- Expenditures [Includes K-12 rollover (FY '03 only) & SFB debt financing]
- Expenditures
- ▲— Base Revenues



Governor's Budget Proposal:

- ✓ Budget represents an 18.4% increase (\$1.5 billion) in on-going spending over FY 2006 = \$400 million dollar structural deficit.
- ✓ \$180 million BSF deposit in FY 2007.
- ✓ Beginning balance = \$1.047 billion.

Legislature's Budget Proposal:

- ✓ Budget represents a 7.5% increase (\$616 million) over FY 2006 = \$368 million structural surplus.
- ✓ \$450 million in BSF payments in FY 2006 and FY 2007.
- ✓ Beginning balance = \$610 million.

Note: The Executive budget is a complete recommendation and identifies new policy initiatives such as funding for full day kindergarten, higher teacher pay, border enforcement, and tax reductions. The JLBC budget sets aside \$368 million for on-going policy initiatives.

Two County's Provide Employee Mid-year Raises

Pima County

On November 15, 2005, the Pima County Board of Supervisors made the decision to award county corrections officers with an 18.6% pay increase. The increase was applied to each level in the step pay scale, as well as collapsing the steps from eight to five years before reaching the top of the salary range, effective April 2, 2006. The cost of the increase in FY 2006 is \$377,194, with an estimated annual cost of \$1.6 million.

The decision to increase corrections officers salaries follows a long list of increases awarded at the beginning of FY 2006, including a 2.5% COLA (excluding deputies and corrections officers), plus an additional 1.7% to offset the increase in the ASRS retirement contribution rate. Sheriff's office deputies and sergeants received a 14.5% average market adjustment (effective April 2005). In addition, the corrections staff received step increases on their anniversary date. The total annualized cost of raises, not including the \$1.6 million allocated for the increase to corrections officers, amounts to approximately \$9.1 million in FY 2006.

Mohave County

The Mohave County Board of Supervisor's approved a 10% mid-year market adjustment for county and superior court employees, effective January 7, 2006. The Board of Supervisor's contracted with an outside vendor to conduct a market study last year and set aside \$1 million at the time of the FY 2006 budget adoption while waiting for the results; however, the market adjustment will end up costing \$2.2 million, just through the end of the fiscal year. The Board also decided to fund step increases for employees, effective July 2007. In addition, the county manager was given the authority to apply market premium adjustments, at an unspecified amount, for the recruitment of identified "hot jobs."

Hawkeye Wilson

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and staff assistant to a Leadership office and then as a congressional investigator on the Committee on House Oversight for Chairman Bill Thomas.

Mr. Wilson graduated from Northwest Missouri State University's College of Mass Communications with a baccalaureate degree in journalism.

ATRA President Kevin McCarthy, remarking on Mr. Wilson's addition to the staff to the Board of Directors, "Hawkeye brings an excellent combination of skills and talents to the organization that we intend to use to the fullest. His communication skills will be a great asset in our efforts to convey ATRA's message to the largest audience possible."

ATRA NEWSLETTER CORRECTION

ATRA's October/November newsletter article on county budgets incorrectly implied that the "additional" pay check awarded to Graham County employees in FY 2005 served as a bonus to employees. The "additional" pay check was simply a matter of the county's accounting schedule when in fact, no pay raises were awarded to employee's that fiscal year.

