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ARIZONA TAX RESEARCH ASSOCIATION

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MANAGING THE CRISIS:

ATRA'S 2008 LEGISLATIVE PROGRAM MAJOR FOCUS ON PROPERTY TAX REFORMS

ATRA's Board of Directors adopted its 2008 Legislative Agenda in December and ATRA is aggressively pursuing those goals in the second regular session of the 48th Legislature. As in past years, ATRA offers the Legislature a list of solutions to help address the FY 2008 and FY 2009 state budget deficit as well as improve the state's financial management. In addition, ATRA has recommended a package of property tax reforms that focuses on protecting property taxpayers from unreasonable increases associated with property valuation growth.

ATRA's Budget Recommendations

The state budget deficit is estimated at approximately \$1 billion in FY 2008 and nearly \$1.7 billion in FY 2009. ATRA has consistently emphasized to legislators that budget shortfalls provide a rare opportunity to fix flawed funding formulas that exist, most notably in the K-12 and higher education systems. Additional funding formulas that would be beneficial to review are the formulas in the corrections, health care, and particularly, in the state retirement systems (*A detailed list of ATRA's Budget Recommendations can be viewed online at www.arizonatax.org*).

ATRA'S 2008 Legislative Program

In 2006, the Legislature reduced state property taxes by temporarily eliminating the state equalization rate and at the same time, preempted local governments from increasing primary property taxes with the enactment of HB2856. During that same session, the Legislature referred, and the voters approved, Prop 101 that eliminated more than \$185 million in excess levying capacity, thereby requiring local

governments to reduce tax rates to offset the growth in property values.

As a result of the one-year lag in the establishment of property valuations and taxation of those values in the following year, the large valuation increases that were mailed to taxpayers in 2006 were taxed for the first time in 2007. For the most part, the efforts to reduce primary tax rates produced positive results with total primary levies limited to 7.1% growth, and as a result, the average primary tax rate was reduced by 51 cents (7%) statewide. In fact, primary levies rose only 9.2% with the average rate falling \$1.08 (13.8%) over the last two years.

Secondary levies, on the other hand, grew at a much greater rate of 28% over the last two years, which in most instances, represented voter-approved bonds. The increases in secondary property taxes have fostered considerable unrest among taxpayers while also providing fertile ground for Prop 13-style property tax limitation initiatives.

Specifically, ATRA will pursue the following recommendations in property taxation.

Primary Property Tax Relief ***Permanent Repeal of the State Equalization Rate***

Although ATRA advocated for the permanent repeal of the state equalization rate during the 2006 legislative session, the final budget agreement resulted in only a temporary repeal in 2006, 2007, and 2008. The Legislature's actions to reduce tax rates in the face of growing property

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ARIZONA STATE AND LOCAL DEBT CLIMBS \$3 BILLION (11%) TO \$32.1 BILLION

As the Legislature considers proposals to borrow its way to a balanced budget, the Department of Revenue's Debt Oversight Commission released a timely analysis of the debt owed by Arizona's state and local governments. At the close of fiscal year (FY) 2007, the aggregate outstanding debt increased \$3 billion (11%) over the previous year. Arizonans currently owe \$32 billion in outstanding principal on government bonds; this equates to approximately \$5,204 for every man, woman, and child that calls Arizona home. In addition to the bond debt, public entities hold 1,343 lease-purchase contracts totaling \$663 million of outstanding obligations.

Arizona's bonded indebtedness results primarily from six political subdivisions. Cities and towns hold the largest portion of the debt (\$13 billion) followed by state agencies and state universities (\$8 billion). Voters in school districts are responsible for \$4 billion of the bonds, and the remaining \$6 billion is held by special districts, counties, community colleges, and other public entities.

Cities and Towns

While the debt of cities and towns has grown significantly over the last five years (85%/\$6 billion), this growth rate appears to have recently slowed relative to the other political subdivisions. Nevertheless, city debt still grew by 8% from FY 2006 to FY 2007.

Notwithstanding this reduction in the rate of growth, cities and towns hold the largest portion of Arizona's debt. The ten cities with the highest amounts of debt account for 88% of the total debt held by all Arizona cities and towns. The cities with the most debt are,

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predictably, the state's larger cities: Phoenix, Mesa, and Tucson. Comparing individual cities' per capita debt provides a better indication of which cities proportionally rely most heavily on borrowed revenues. Queen Creek has the highest amount of outstanding debt per capita (\$7,671) with Cave Creek (\$7,227) and Tolleson (\$6,705) not far behind.

State Agencies and Universities

Like cities and towns, state agencies and universities experienced relatively lower growth in the last year (9%) but considerable growth over the last five years (152%). The majority of the \$8

billion of state agency debt is held by the Health Facilities Authority (\$3 billion), the Department of Transportation (\$2 billion), and the School Facilities Board (\$1 billion). The three state universities together hold \$2 billion in outstanding debt.

School Districts

Of the \$4 billion of school district debt, more than half belongs to only ten of Arizona's 218 school districts. As nine of these ten districts are also the largest in the state, these districts account for 39% of all district school students. Among these districts, however, there is surprisingly little correlation between

debt and district size. For example, five school districts have more debt than the largest district, Mesa Unified, and three districts have more debt than the second largest district, Tucson Unified. Scottsdale Unified and Phoenix Union rank eighth and ninth in district size; yet, in outstanding debt, these districts rank first and second, respectively. These discrepancies in proportional debt earned the Scottsdale and Phoenix districts a place among the ten districts with the most debt per student. Scottsdale Unified ranks third with a per student debt of \$15,378, and Phoenix Union ranks seventh with \$13,339 per student. Bicentennial Union carries the most debt per student (\$22,115) followed closely by Wickenburg Unified (\$17,079).

Special Districts

Special districts are responsible for \$1 billion in outstanding debt. Of the 491 reporting districts, 157 carry an outstanding debt balance. The combined debt balance of only ten of these districts made up one half of the total special-district debt. The districts with the most debt include the Tucson Airport Authority in Pima County (\$114 million), the Electrical District #3 in Pinal County (\$86 million), and Vistancia CFD in Maricopa County (\$66 million).

With a one-year change of 26% (\$251 million), special districts saw the second largest percent increase of debt in FY 2007. Two of the districts mentioned above are also among the three special districts most responsible for this year's increase in special district debt. Electric District #3 had the largest increase in special district debt (\$43 million), and Tucson Airport Authority had the third largest increase (\$27 million) just behind Bullhead City Sewer Improvement (\$30 million). The ten special districts with the largest one-year increase accounted for 87% of the statewide increase in special-district debt.

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Jurisdiction	FY 2001-02	FY 2005-06	FY 2006-07	1-Year Change	5-Year Change
Counties	\$735,118,470	\$820,303,073	\$1,028,985,713	25.4%	40.0%
Cities/Towns	\$7,197,608,359	\$12,351,627,900	\$13,305,513,076	7.7%	84.9%
Comm Colleges	\$514,880,000	\$587,220,000	\$807,100,000	37.4%	56.8%
Schools	\$4,134,971,264	\$3,854,788,208	\$4,411,744,958	14.4%	6.7%
Special Districts	\$973,542,496	\$948,651,115	\$1,199,158,313	26.4%	23.2%
State & Univ.	\$3,189,303,100	\$7,338,710,876	\$8,027,332,500	9.4%	151.7%
Other	\$3,654,246,677	\$2,993,930,199	\$3,312,457,982	10.6%	-9.4%
Total	\$20,399,670,366	\$28,895,231,371	\$32,092,292,542	11.1%	57.3%

Top 10 Cities in Total Outstanding Debt	Debt per Capita	
Phoenix	\$5,986,207,047	\$3,977
Mesa	\$1,120,462,840	\$2,482
Tucson	\$1,030,779,592	\$1,928
Scottsdale	\$927,291,642	\$3,911
Glendale	\$779,059,130	\$3,199
Tempe	\$581,595,000	\$3,506
Gilbert	\$434,595,000	\$2,349
Chandler	\$402,754,500	\$1,711
Peoria	\$261,756,821	\$1,804
Lake Havasu City	\$154,103,573	\$2,822

Top 10 Cities in Debt Per Capita	Total Debt	
Queen Creek	\$7,671	\$143,366,468
Cave Creek	\$7,227	\$35,158,693
Tolleson	\$6,705	\$43,715,000
Williams	\$6,580	\$20,859,501
Sedona	\$5,230	\$57,579,138
Phoenix	\$3,977	\$5,986,207,047
Scottsdale	\$3,911	\$927,291,642
Cottonwood	\$3,632	\$39,675,000
Tempe	\$3,506	\$581,595,000
Glendale	\$3,199	\$779,059,130

Top 10 School Districts in Total Outstanding Debt	Debt Per Student	
Scottsdale USD	\$388,660,000	\$15,378
Phoenix UHSD	\$319,995,000	\$13,339
Paradise Valley USD	\$285,660,000	\$8,767
Tucson USD	\$255,460,000	\$4,498
Peoria USD	\$248,368,000	\$6,857
Mesa USD	\$239,315,000	\$3,478
Deer Valley USD	\$189,500,000	\$5,546
Chandler USD	\$174,040,000	\$5,441
Gilbert USD	\$147,920,000	\$4,137
Tempe UHSD	\$117,540,000	\$9,012

Top 10 School Districts in Debt per Student	Total Debt	
Bicentennial UHSD	\$22,115	\$2,300,000
Wickenburg USD	\$17,079	\$20,000,000
Scottsdale USD	\$15,378	\$388,660,000
Saddle Mountain USD	\$15,314	\$17,550,000
Madison ESD	\$13,828	\$66,485,000
Osborn ESD	\$13,553	\$48,125,000
Phoenix UHSD	\$13,339	\$319,995,000
Riverside ESD	\$13,205	\$10,260,000
Mingus USHD	\$12,107	\$15,000,000
Apache Junction USD	\$11,728	\$66,805,000

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Counties

The combined debt of Arizona’s 15 counties is just over \$1 billion. Like special districts, county debt has also grown significantly over the last year (25%). All of the year’s increase in county debt resulted from new debt in Pima (\$132 million) and Maricopa (\$100 million). The new Pima debt included issues of G.O. bonds (\$95 million), revenue bonds (\$71 million), and certificates of participation (\$30 million). All of Maricopa’s new debt resulted from issuing \$140 million in revenue bonds. Each of the other counties paid down their aggregate debt balances over last year.

Pima’s outstanding debt of \$628 million greatly surpasses every other county. Together with Maricopa (\$178 million) and Pinal (\$160 million), these three counties hold nearly 94% of statewide county debt. While Maricopa has the second largest outstanding debt balance, the county ranks above only two of the 11 indebted counties in terms of per capita debt. In contrast, Pima and Pinal, respectively, rank first and second in per capita debt. Pima carries \$640 of debt for every county resident and Pinal carries \$535. Coconino County ranks a distant third with \$122 of debt per capita.

Community Colleges

From FY 2006 to FY 2007, community colleges saw the greatest percent increase (37%) in outstanding debt. Only three community college districts (CCDs) contributed to the increase. The three districts with new debt include the Maricopa CCD (\$185 million), Yuma/La Paz CCD (\$52 million), and Mohave CCD (\$1 million).

The total outstanding debt of the community colleges currently reaches \$807 million. More than 70% of this balance is held by the Maricopa CCD (\$578 million). Significant amounts are also held by the Yuma/La Paz (\$76 million) and Yavapai (\$57 million) CCDs. The Yuma/La Paz and Yavapai districts also significantly surpass all other districts in the amount of debt they carry per student—more than \$16,200. The Coconino CCD has the third highest amount of per student debt with \$8,850 of debt for every full-time student equivalent.

Justin Olson

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valuations was the correct policy response in order to avoid huge property tax increases. However, reversing that policy by reinstating the state equalization rate in 2009 will undermine and reverse all of the previous efforts to manage a crisis in Arizona’s property tax system. During the 2008 legislative session, ATRA will again aggressively advocate to make this tax cut permanent. The Senate version of the bill is sponsored by Senate Finance Committee Chairman Jim Waring and Senate President Tim Bee (SB 1002). The House version is sponsored by Speaker of the House Jim Weiers and House Ways and Means Committee Chair Steve Yarbrough (HB 2220).

Continued adherence to Truth-in-Taxation (TNT)

Truth-in-taxation (TNT) has been highly successful at the state level. The Legislature and Governor have adopted the TNT rates for the qualifying tax rate (QTR) for K-12 schools and the county education equalization rate (state equalization rate) every year since 1998. State policymaker’s compliance with TNT has helped mitigate the annual

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Top 10 Special Districts in Outstanding Debt

Tucson Airport Authority (Pima)	\$113,945,000
Electical District #3 (Pinal)	\$85,590,000
Vistancia CFD (Maricopa)	\$66,085,000
Verrado CFD (Maricopa)	\$55,600,000
Metropolitan Domestic WID (Pima)	\$54,930,000
Bullhead City Sewer Imp. (Mohave)	\$51,019,407
Maricopa County Stadium District	\$50,050,000
Watson Road CFD (Maricopa)	\$49,000,000
Hospital District No. 1 (Maricopa)	\$42,980,000
Sundance CFD (Maricopa)	\$30,030,000

Top 10 Special Districts in 1-Year Debt Increase

Electical District #3 (Pinal)	\$43,120,000
Bullhead City Sewer Imp. (Mohave)	\$29,691,376
Tucson Airport Authority (Pima)	\$27,125,000
Tangerine Farms Road Imp. (Pima)	\$25,774,000
Vistancia CFD (Maricopa)	\$22,010,000
Flagstaff Special District (Coconino)	\$18,999,000
Verrado Community Facilities (Maricopa)	\$18,600,000
Northwest Fire District (Pima)	\$13,470,000
Metropolitan Domestic WID (Pima)	\$12,110,533
Apache Junction Fire District (Pinal)	\$8,690,000

County	Outstanding Debt	Debt Per Capita	One-Year Change
Pima	\$627,885,713	\$639.86	\$132,183,640
Maricopa	\$177,865,000	\$46.90	\$100,200,000
Pinal	\$160,420,000	\$534.96	-\$4,280,000
Mohave	\$16,410,000	\$82.75	-\$3,670,000
Coconino	\$16,180,000	\$122.33	-\$2,000,000
Yuma	\$11,885,000	\$60.52	-\$8,321,000
Cochise	\$7,605,000	\$56.27	-\$560,000
Navajo	\$5,635,000	\$49.66	-\$280,000
Apache	\$2,040,000	\$27.38	-\$3,060,000
Gila	\$1,840,000	\$32.39	-\$205,000
La Paz	\$1,220,000	\$57.40	-\$725,000
Graham	\$0	\$0.00	\$0
Santa Cruz	\$0	\$0.00	\$0
Yavapai	\$0	\$0.00	\$0
Greenlee	\$0	\$0.00	-\$600,000

CCD	Total Debt	Debt Per Student	One-Year Change
Maricopa	\$577,995,000	\$6,644	\$185,315,000
Yuma/La Paz	\$76,280,000	\$16,230	\$52,200,000
Yavapai	\$57,390,000	\$16,212	-\$2,970,000
Pima	\$51,455,000	\$2,510	-\$12,265,000
Coconino	\$19,425,000	\$8,850	-\$1,030,000
Mohave	\$12,210,000	\$3,964	\$1,190,000
Pinal	\$8,165,000	\$1,886	-\$580,000
Navajo	\$3,620,000	\$1,293	-\$1,725,000
Cochise	\$560,000	\$85	-\$255,000
Graham	\$0	\$0	\$0
Gila	\$0	\$0	\$0

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growth in property taxes associated with valuation growth. ATRA will once again advocate for continued TNT compliance at the state level.

Secondary Property Tax Reforms

The majority of secondary property taxes consist of voter-approved bonds and overrides that have some protections in place for taxpayers; however, additional reforms are necessary. During the 2008 legislative session, ATRA will recommend that legislators adopt the following reforms in secondary property taxes, both of which will be sponsored by Rep. Steve Yarbrough and Sen. Bob Burns:

Special District Levy Limits

Almost identical to last year's legislative proposal under HB2656, ATRA will advocate to have the same levy limits that currently exist on primary property taxes of counties, cities, and community colleges (2% plus

new construction) apply to all countywide special district levies. The countywide special districts that will be affected include flood control districts, library, public health services, jail, and television districts. This year's proposal will also include placing the levy limits on fire districts.

In addition, flood control districts and fire districts will be given the authority to levy a secondary property tax override with the approval of voters, as long as the rate levied for maintenance and operation purposes, together with the rate levied for the override, remain within the existing tax rate caps.

G.O. Debt Service Reform

The dramatic growth in property values over the past few years has led to dramatic growth in property tax levies for debt service on general obligation bonds. During a time when rates should have been dropping due to the growth in

property values, many local governments kept rates the same, resulting in significant tax increases. In order to prevent such abuse in the future, ATRA believes the following reforms are in order:

1. Prohibit local government from asking voters to authorize debt in excess of the jurisdictions' constitutional debt limit.
2. Limit G.O. bond refinancing to interest rate savings only and prohibit changes in the debt service schedule for the payment of outstanding principal unless approved by the voters.
3. Prohibit local governments from levying secondary property taxes for debt service in excess of the debt service requirement for the current fiscal year.