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ARIZONA TAX RESEARCH ASSOCIATION

NEWSLETTER VOLUME 76 NUMBER 4 MAY 2016

Several ATRA Bills Pass Legislature

The 52nd State Legislature completed its second regular session in 117 days, a plodding pace coming off of last year's brisk effort. Eleven of eighteen ATRA designated 'Good Bills' received final passage and were signed by the Governor.

ATRA's April newsletter discussed the first ATRA bill signed by the Governor this session, *SB1117 (Dial) school districts; adjacent ways; verification*. The Governor signed four other ATRA bills while a few never made it to his desk.

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MIHS Uses Bond Funds to Determine How to Spend Bond Funds

Maricopa Integrated Health System (MIHS), the county's government-run hospital, has hired a consulting firm to determine what it should do with nearly a billion dollars in capital bond monies. After telling voters in 2014 it had created a comprehensive plan with a 15-member Bond Advisory Committee to determine it needed precisely $935 million to refurbish their capital spaces, the district now admits it does not have a plan and is paying handsomely for it.

District records show MIHS has contracted with Navigant Healthcare for consulting services to the tune of $995,000 to

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Most ATRA 'Bad Bills' Fail in 2016

Before the Arizona Legislature adjourned *Sine Die* on May 7, twelve of fourteen ATRA designated 'bad bills' had failed to pass both chambers. While significant effort is dedicated to advancing a legislative agenda to improve state laws for taxpayers, ATRA expends a great deal of energy mitigating legislation deleterious to taxpayers. ATRA successfully convinced lawmakers not to undermine truth-in-taxation and audit laws critical to transparency in government. Bills increasing nonvoter approved access to the property tax for fire districts also did not advance. The following were bills ATRA spent considerable time advocating against.

SB1402 class six property; higher education (Yarbrough)

The third attempt in as many years to expand class six property to include for-profit higher education colleges failed in the House of Representatives 17-39 after narrowly passing the Senate. Grand Canyon University continues to push for this tax break, which would reduce their property tax assessment ratio from class one (businesses, corporations) at 18% to class six (foreign trade zones, historic property) at 5%. ATRA has long advocated against expanding class six property, which provides an unfair tax status to certain businesses over

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MIHS CONSULTANT SPENDING, *Continued from Page 1*

create a soup-to-nuts game plan. Naturally, this million dollar contract will be paid for with interest using bond funds.

Phase	Estimated Professional Fees
1. Mobilization and Strategic Validation	$110,000
2. Program, Service Configuration, Facilities Planning and Programming and Community Planning	$190,000
3. Ambulatory Care Network Plan Development	$235,000
4. Clinical Care Delivery Model Development	$180,000
5. Financial Impact Assessment / Modeling	$150,000
6. Implementation Framework Development	$130,000
TOTAL	$995,000

In November of 2014, Maricopa County voters authorized MIHS to "sell general obligation (G.O.) bonds in an amount not to exceed $935 million to fund capital projects" per the official informational ballot pamphlet. Nothing in the official ballot indicated the district did not have a plan or that it would use bond monies on consulting services to develop one. Instead, proponents insisted the district had conducted extensive research and knew precisely of the district's capital needs. MIHS is justifying this expense because the ballot question included using bond funds for the "development and improvement of any proposed facilities and equipment."

During the run up to the election, ATRA warned the ballot language was vague enough to be deemed a 'blank check' for MIHS, an accusation hotly refuted by proponents. The hiring of Navigant proves the point: MIHS did not and does not have a plan for how to spend the money.

Leveraging G.O. bonds for capital projects is a common strategy because the useful life of physical capital such as buildings outlive the debt-service payments, much like a mortgage. However, using bond funds to pay for consulting services is an irresponsible use of debt financing.

Fully 18 months after the authorizing election, MIHS has yet to demonstrate fiscal solvency or a legitimate use of bond funds. ATRA's July 2015 newsletter discussed the district's first draw on bond proceeds, which used $36 million as cash to supplant the hemorrhaging General Fund, which was justified as refunding the district for previous capital purchases. The remainder of the first $106 million bond issue was spent on soft capital items, none of which have a life expectancy longer than the total bond issuance. Finally, the first bond sale was conducted privately, which avoided the high-profile scrutiny of a public bond rating and incurred higher interest costs because the bonds weren't sold tax-free.

Despite drawing down bond funds for cash last year and paying for soft capital and consulting services with the same, the district continues to run a massive structural deficit. For FY2017, the district projects a negative operating budget of $19.1 million. District officials continue to lobby state lawmakers for higher distributions of state controlled revenues for indigent health care to help solve their deficit.

ATRA hopes MIHS will adhere to their public promise to not sell bonds until they find a sustainable fiscal horizon. MIHS should not leverage property tax dollars until it can find a manageable, niche role that doesn't require large infusions of taxpayer dollars. Attempting to compete with the private sector in the delivery of health care, even with shiny new digs, is unlikely to result in anything but a substantial drain on taxpayers.

Published by the Arizona Tax Research Association, a nonprofit organization whose purpose is to promote efficient and effective use of tax dollars through sound fiscal policies. Permission to reprint is granted to all publications giving appropriate credit to the Arizona Tax Research

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ATRA GOOD BILLS, *Continued from Page 1*

HB2054 debt limitations; net assessed value (Mitchell)

This law enshrines a recent Attorney General opinion by clarifying the calculation of local governments' debt limitations will use the net assessed of full cash values, as they have for many decades. ATRA will now refer to these values as the 'debt limit value.' Following the implementation of Proposition 117, there is no longer a taxable value based on full cash value. The debt limit value was formerly known as the secondary net assessed value. This was an important clarification because the elimination of the secondary net assessed value caused some in the bond financing community to claim jurisdictions should now be able to use full cash value to determine their debt limitation, which would have exponentially increased local governments access to debt and taxpayers' exposure to repaying it. *Chapter 117.*

HB2481 schools; primary property tax rates (Olson)

HB2481 changes the mechanism for setting K-12 primary school property tax rates from a floating rate that adjusts based on cash balances to a statutory formula. It explicitly states school districts will annually levy the lesser of the Qualifying Tax Rate or the amount to fund the equalization base plus any legal non-formulaic amounts. The biggest improvement is this formula provides rate stability and predictability for taxpayers. The bill provides equitable cash management policies for school districts by removing the four percent budget balance carryforward limitation. Charter schools already have such authority. This change also removes the incentive to expend remaining cash at the end of the fiscal year. *Signed by Governor.*

HB2476 school property; sales; leases; use (Norgaard)

Responding to a recommendation from the Governor's Classrooms First Initiative Council to fix the use of proceeds from the sale and lease of school property, ATRA helped craft legislation to make sense of a confusing area of school finance. The bill creates a new materiality test whereby all sales of items less than $100,000 can be expended without restriction. It frees up all existing school plant funds for use on capital projects by creating prospective rules for the use of sale proceeds beginning July 1, 2016. The bill ensures that "high-debt" school districts use a specific percentage of large sale proceeds to pay down bonded indebtedness. Low-debt school districts may expend all sale proceeds for capital. The bill creates new financial incentives for school districts to sell and lease school property to other schools by placing those monies in less restrictive funds. For taxpayers, the bill keeps the high and low debt delineation at a 50/50 split of a district's constitutional limit. *Signed by Governor.*

SB1523 truth in taxation; levy increases (Smith)

In response to Pinal Community College District's contested 21% tax increase last year, the Legislature enacted a new taxpayer protection for large property tax increases. SB1523 requires a jurisdiction that intends to increase taxes 15% or more above the truth in taxation (TNT) levy receive a unanimous vote of the board. TNT requires the governing body of a county, community college district, city, town, and school district to hold a public hearing and publish notice in a newspaper of the governing body's intent to increase primary property taxes, exclusive of growth associated with new construction. This law creates a higher level of scrutiny and public awareness of dramatic tax increases. *Chapter 173.*

HB2480 truth in taxation; levy increases (Olson)

One key piece of legislation which did not make it to the finish line, HB2480 was an attempt to provide improvements to the new manner in which the state manages the constitutional homeowner '1% Cap.' Arizona homeowners are limited to a $10 primary property tax rate and when the combination of state and local government tax rates exceeds $10 per $100 of assessed value, a revenue gap is created. Before FY2016, the State General Fund simply paid this amount by providing additional state aid to the K-12 school district. If the revenue gap was larger than the equalization base of the school district as is the case in several Pinal County jurisdictions, jurisdictions were simply shorted revenue. Last year the K-12 budget BRB included language which indicated the State General Fund would only subsidize each county up to $1 million. The ATRA May and December 2015 newsletters explained in greater detail.

HB2480 attempted to address the limitations of last year's law change. Chief among them was a property tax rate cap for affected jurisdictions with very high tax rates. Because these jurisdictions must now account for the revenue gaps, an obvious incentive was created to raise tax rates in order to generate new revenue for the payments, which further aggravates the 1% Cap penalties. This "prisoners dilemma" has the effect of causing property tax rate spiraling in affected jurisdictions and was witnessed in the first year in several affected jurisdictions. HB2480 would have placed a tax rate cap on jurisdictions with a tax rate more than 150% higher than the statewide average (defined). This would only affect a few jurisdictions with very high property tax rates. Pinal and Pima County, who would have faced a rate cap, opposed the bill.

The bill clarified that all jurisdictions who contribute to a 1% Cap problem will participate in paying penalties, to include the school districts. The current law limits penalty payments to municipalities, community college districts and counties with rates above their peer average. This would have the effect of distributing the penalty burden. The bill also clarified methodology for calculation of penalty payments, amongst other technical reforms.

Few at the Capitol have an appreciation for the depth of the current 1% Cap problem. ATRA attempted to build a compromise between local governments and taxpayers but different options faced new political hurdles. Until more lawmakers grapple with this highly complex aspect of Arizona's public finance, the problem will continue to fester. *Failed on Senate Third Read.*

BAD BILLS FAIL, *Continued from Page 1*

others. All businesses in Arizona grapple with the state's high business property taxes and finding loopholes for single entities to exit the policy debate undermines fair governance and uniform taxation.

HB2512 pensions; expenditure limit exemption (Coleman)

As amended, HB2512 would have created significant expenditure limit relief for jurisdictions who pay into the Public Safety Pension Retirement System (PSPRS). ATRA originally supported the underlying version of the bill, which was designed to allow jurisdictions to make lump-sum cash payments on existing PSPRS unfunded liability debt by excluding that payment from their constitutional expenditure limit. The bill was amended at the request of Maricopa County to include any payment associated with unfunded liability, which was written to the effect of excluding even parts of current year payments owed to PSPRS by the district. This was beyond the intent of the underlying bill and raised constitutional concerns. While the underlying bill had the effect of providing relief for both taxpayers and local governments, the amended version simply provided unwarranted, nonvoter approved expenditure limit relief. Senator Lesko was prepared to amend the bill on the floor of the Senate back to the underlying bill but it was never scheduled for a Senate Committee of the Whole. *Held in Senate COW*.

Favorably Amended:

HB2538 municipal bonds; tax levy (Mesnard)

Under current law, the annual secondary property tax levy for voter-approved bonds is limited to the amount necessary to make the annual debt service payment, plus a reasonable delinquency factor and any amount needed to correct prior year errors. As introduced, HB2538 would allow a political subdivision to also levy for any projected payments on new debt planned for the ensuing year and for the early defeasance of existing debt. ATRA offered an amendment that requires the current year levy to be net of any cash that remains in the debt service fund from the previous year. In addition, the amendment would require the amount levied for the various amounts be separately stated in the public entity's budget. ATRA was opposed to the underlying measure and believes the bill as passed both houses merely clarifies the authority municipalities already maintain. *Signed by Governor.*

HB2197/SB1244 fire districts; merger; consolidation (Coleman)/(Allen)

HB2197 and SB1244 were both favorably amended to address taxpayer concerns related to fire districts. In addition to local property tax levies, fire districts also receive Fire District Assistance Tax (FDAT). The tax is a countywide secondary property tax and the rate is limited to 10 cents per $100 of assessed value per county. The FDAT revenues are distributed based on 20% of each fire district's levy, not to exceed $400,000. Prior to 2011, the $400,000 cap did not apply to fire districts that merge or consolidate; however, a blatant abuse of the tax in 2008 in which three districts dramatically increased their local taxes to maximize their FDAT distribution in the year prior to the merger necessitated a remedy to protect taxpayers. As a result, ATRA and fire district representatives agreed to cap all districts in order to protect the integrity of the tax. In recent years, however, the cap has been an impediment for some districts to merge. As originally introduced, HB2197 would have simply reversed the 2011 reform by removing the $400,000 cap altogether for consolidated or merged fire districts. In recognition of the obstacle that the FDAT cap presents for merger districts, ATRA worked with fire district officials on an amendment that removes the cap for merger districts but requires the distribution to be based on a five-year average. Additionally, the amendment included a retroactive clause for mergers that occurred on or after July 1, 2014. As amended and signed by the governor, HB2197 removes the financial obstacle for districts to merge and protects taxpayers from a repeat abuse of the FDAT.

SB1244 had identical language as HB2197 related to FDAT but was amended to include a temporary voter-approved override. The override election can be held on a November election in 2016 or 2017 to ask district voters for a five-year override to exceed the $3.25 per $100 tax rate up to $3.50 per $100 of assessed valuation. This temporary override option was negotiated between ATRA and fire district representatives. The underlying bill called for a voter approved override in any amount without a rate limit. *Both signed by Governor.*