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ARIZONA TAX RESEARCH ASSOCIATION

NEWSLETTER VOLUME 80 NUMBER 7 OCTOBER 2020

Fire District Levies Mirror 6% NAV Growth

Fire District (FD) levies increased 6% this year to \$319 million. This year's increase is the result of a 5.8% increase in the Net Assessed Value (NAV) and an approximate 1% increase in the average tax rate levied by FDs. In the fifth year since Prop 117 has been in effect, this year's growth appears to be the new trend.

Net Assessed Value (NAV)

In FY 2021, FD NAVs grew 5.8% to \$11.3 billion. The largest percentage of NAV growth occurred in Alpine and Quartzsite by 59% and 49%, respectively. Other FDs that experienced significant growth included Timber Mesa (12.8%), Buckeye Valley (11.2%), Rincon Valley (10.6%), and Golden Valley (9.8%).

See Fire District Levies, Page 3

ATRA Outlook Conference:

Nov 19 @ 8:30am

Sign up at our website or call the office at 602-253-9121

Prop 208 Draws Negative National Attention

The proposal to increase Arizona's top marginal income tax rate 77.7% is gaining national attention, a surprising trend during a chaotic presidential election year. The Tax Foundation, Wall Street Journal editorial board, and economists with the American Legislative Exchange Council have weighed in, signaling that such a tax increase in Prop 208 has raised eyebrows across the country. The big question on everyone's mind: is Arizona trending towards being a far less business-friendly state?

The Tax Foundation, which focuses on state, local, and international taxation issues, wrote an analysis on Prop 208, pointing out that the measure "...is a huge shift that reverts decades of reforms which lowered the top marginal rate from a high of 7 percent." Walcsak and Cammenga of the Tax

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10 Years On, The Frozen Tax Rate Protects Rural AZ

Ten years after becoming state law, the maximum school tax rate law has proven to be a vital shield for taxpayers, particularly in remote parts of rural Arizona. Often overlooked, peculiarities in the tax system can be particularly harsh in rural areas with smaller tax bases. For years, ATRA sounded the alarm that unlimited budget rules in small schools allowed for unlimited local tax rates, creating inequitable tax burdens.

See FROZEN RATE PROTECTS RURAL AZ, Page 5

PROP 208 EARNS ATTENTION, *Continued from Page 1*

Foundation suggest the measure, which increases the top rate from its current 4.5% to 8%, will hurt the state's tax climate and its regional competitiveness with peers that have low or no income tax rates. They remind that studies suggest income taxes cause more economic distortions than other taxes and this increase could interfere with an economic recovery from COVID-19. <https://taxfoundation.org/arizona-proposition-208-education-funding/>

Economists Steven Moore, Art Laffer, and Erwin Antoni penned a lengthy economic analysis of Prop 208, titling it "Arizona's Prop 208 Tax Hike Loses Jobs and Harms Small Businesses." They point out that from an economic competitiveness standpoint, Arizona would immediately fall from 10th best in the nation to 16th in the ALEC-Laffer index, largely a result of going from having low income tax rates to having the 9th highest top marginal rate in the country.

Moore, Laffer, and Antoni estimate Prop 208 would cause 200,000 jobs to be eliminated and a 700,000 loss in net migration in the first ten years. The resulting personal income losses total \$25.5 billion in 10 years. They remind that this tax increase ends up impacting far more than the wealthy and business owners, as the economic impacts reverberate statewide, and will cause average household incomes to drop \$6,000 with the tax hike.

On the revenue side, the economists estimate that the proposition raises "at most...half the static \$1 billion in tax revenue gains that proponents of 208 advertise." The State JLBC estimates the static tax increase would be in the neighborhood of \$827 million in total dollars, \$702 million of which goes to school districts and charters, and does not estimate a dynamic revenue amount. The reality is this revenue source is so volatile that it will be difficult to measure the negative economic impacts, though they undoubtedly will occur.

Finally, the economists remind that all the modeling that exists today uses data from pre-Tax Cuts and Jobs Acts (TCJA), which limited the State and Local Tax Deduction (SALT) to \$10,000. "This means that no longer can filers deduct up to 40% of their state income tax payments from their federal taxes. As such, all of the evidence in this study UNDERSTATES the negative effects of the proposed income tax increase." <https://tinyurl.com/yyze85qx>

The Wall Street Journal editorial board found it worth their time to weigh in on a state ballot proposition, calling Prop 208 a tax increase that harms recipients of government funding like schools because it would "slow investment and spending far into the future." They correctly point out that Arizona is a choice state for retirees but that could easily change for wealthy filers if 208 passes. They argue wealthy filers moving from places like California, New York, and Illinois have been a boon for Arizona over the past 30 years, adding billions in taxable wealth to the state.

The WSJ points out most of the money funding the Yes side is coming from out of state, from Stand for Children and the national teachers union and that polling data has shown 208 to have started off quite popular but slowly seems to be showing less favorability with voters. <https://www.noprop208az.com/news/ws-j-tax-raid-in-arizona>.

ATRA continues to work with the No on Prop 208 campaign, actively supporting grassroots efforts, speaking at clubs and other organizations, and writing on the topic. ATRA encourages all Arizonans to talk to their friends and neighbors about this historically bad idea and encourage people to vote no.

- Sean McCarthy

FIRE DISTRICT LEVIES, *Continued from Page 1*

Since the 5% limit under Prop 117 has been in effect, the annual percentage growth in statewide NAV has hovered around the single-digits. However, the NAV of some districts can grow at greater than average rates as a result of annexations and new construction, or if they carry a higher concentration of centrally valued property since the NAV of these properties are not limited by Prop 117. Over the last five years, NAV has grown 25% or 5% on average per year.

This year’s 6% growth in FD levies is consistent with the growth-trend over the last five years, which has been limited to 31.2% or 6.24%.

In addition to the benefits associated with Prop 117, the 8% levy limits and the \$3.25 tax rate cap on FDs have kept the growth in their annual levies in check.

In FY 2021, the average tax rate levied by FDs increased slightly to \$2.7059. Currently, more than 60 districts are at the \$3.25 rate cap; however, 24 other FDs decreased their tax rates this year. Three of the 24 FDs that reduced their rates were actually at the rate cap last year, which included Flagstaff Ranch (\$2.7400), Junipine (\$3.0420), and Sun Valley (\$3.1686).

Although FDs are subject to levy limits and a rate cap, they do have the authority to ask voters for a tax override. FDs that are under the \$3.25 rate cap can seek a permanent override to exceed the 8% levy limit but remain within the \$3.25 rate cap. A temporary override is allowed for FDs that experience 20% or more decline in NAV over two consecutive years to exceed the \$3.25 rate cap. If approved, the override is good for five years and the FD is subject to an annual levy limit of 5%. During the 2016 legislative session, however, FDs were provided temporary authority during 2016 and 2017 only to ask voters for a five-year override to increase their tax rates to \$3.50. Five districts currently levy up to the \$3.50 tax rate as a result of this legislation. The overrides approved in Pinewood, Pine-Strawberry, and Superstition expire in tax year 2021 and in tax year 2022 for Avra Valley and Tusayan.

Fire District Assistance Tax (FDAT)

In addition to the local property taxes levied by FDs, every county with a fire district is required to levy a countywide property tax. The Fire District Assistance Tax (FDAT) is annually levied to equal 20% of each FDs local levy, not to exceed a 10-cent tax rate. The FDAT distribution is limited to \$400k per FD in most cases, except for FDs that consolidated after July 1, 2014. In these cases, the FDs continue to receive the sum of the average amount of FDAT each district received in the five years prior to the consolidation. The FDAT is now levied statewide since Yuma County was required to levy the FDAT for the first time this year. The FDAT increased 2.6% to nearly \$20M in FY 2021 and has grown 12% over the last five years, an average 2.4% per year.

| Statewide Totals | TY 2015 | TY 2019 | TY 2020 | 1-Yr. chg | 5-Yr. chg |
|------------------|-----------------|------------------|------------------|-----------|-----------|
| NAV | \$9,004,415,751 | \$10,638,273,553 | \$11,254,708,527 | 5.8% | 25.0% |
| Avg Tax Rate | \$2.5642 | \$2.6871 | \$2.7059 | 0.7% | 5.5% |
| Levies | \$242,853,058 | \$300,508,206 | \$318,609,242 | 6.0% | 31.2% |

| | | |
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Public Safety Personnel Retirement System (PSPRS)

Over 60 FDs participate in PSPRS and they collectively carry over \$340M in Unfunded Actuarial Accrued Liability (UAAL). It is clear that the mounting PSPRS UAAL continues to weigh down FD budgets as half of the districts that participate in PSPRS levy to their maximum tax rate.

In 2017, legislation was enacted to allow participating employers of PSPRS to lengthen the amortization of their UAAL ten years to 30 years. Similar to a home mortgage, extending the amortization period over a longer period of time reduces the annual payment but it also increases the total liability as a result. Twelve FDs have opted to increase their amortization period to 30 years- Timber Mesa, Daisy Mountain, Superstition, Sun City, Green Valley, Arizona FMA (North & South County), Lake Mohave Ranchos, Pine-Strawberry, Tubac, Pinetop, Highlands, and Fry.

Four FDs have contribution rates in excess of 50% and they include Bullhead City (59.40%), Sun City (58.75%), Buckskin (52.66%), and the Joint Powers Authority of Chino Valley and Central Yavapai (52.61%). In fact, only half of the 62 districts currently have contribution rates that are less than 30% of payroll.

Only three of the 24 districts that decreased tax rates this year participate in PSPRS.

General Obligation (G.O.) Bond Debt/Secondary Levies

Twenty of Arizona’s FDs carry approximately \$150M in G.O. bond debt. In FY 2021, these districts levied \$15.5M in secondary property taxes to repay the annual debt service on G.O. bonds. The combined levy of four districts account for approximately half of the total and they include Northwest (\$3.7M); Golder Ranch (\$1.4M); CAFMA (\$1.3M); and Daisy Mountain (\$1.1M).

At least two FDs are asking voters to approve an additional \$32M in G.O. debt this November.

Up in the Show Low area, Timber Mesa is asking voters to approve \$19M in G.O. debt, partly to pay off \$3.5M in existing debt and to relocate and remodel existing facilities. If approved, the FD estimates that an additional tax rate of \$0.33 will need to be levied to pay the annual debt service. Since the FDs current tax rate of \$2.9964 is below the \$3.25 rate cap, Timber Mesa could increase its tax rate to as high as \$3.58 if approved due to the existing capacity within the rate cap. Put into perspective, Timber Mesa’s new tax rate would rival the primary tax rates levied for the school districts of Blue Ridge Unified (\$3.5839), Show Low Unified (\$3.8608) and Snowflake (\$4.0060) in that area.

In the southern part of the state, Green Valley is requesting voters to approve a \$13M bond package. The district estimates the additional tax rate to be \$0.24 if approved, which would increase the total tax rate to \$2.7698. Similar to Timber Mesa, Green Valley will use the bonds to pay off existing debt, construct a new fire station, etc.

Fire Districts with Largest PSPRS Unfunded Liability

| Fire District | PSPRS FUNDED % | Unfunded * Liability | Contribution Rates |
|----------------------------|----------------|----------------------|--------------------|
| CAFMA (Chino/C. Yavapai) | 52.90% | \$41,290,988 | 48.51% |
| Northwest | 67.40% | \$36,698,057 | 33.32% |
| Sun City | 41.70% | \$34,061,758 | 58.25% |
| AFMDA (North/South County) | 62.20% | \$29,203,426 | 32.27% |
| Bullhead City | 59.40% | \$24,123,006 | 54.53% |
| Sedona | 57.00% | \$21,617,759 | 38.37% |
| Golder Ranch | 71.00% | \$19,712,924 | 24.84% |
| Superstition | 66.40% | \$19,078,668 | 31.56% |
| Fry | 44.90% | \$15,252,172 | 49.51% |
| Green Valley | 59.40% | \$13,901,183 | 31.65% |
| Drexel Heights | 64.70% | \$13,048,314 | 35.14% |
| Daisy Mountain | 74.40% | \$12,267,929 | 24.44% |

*PSPRS FY 2019 Consolidated Actuarial Valuation-UAAL Tier 1 & Tier 2.

FROZEN RATE, *Continued from Page 1*

In the 2009 special session, an updated state budget included a reform that then Representative Lesko had previously introduced as HB2466. The adopted “maximum tax rate” (A.R.S. 42-17151) is rather simple: if half the homeowners inside a school district fall into the 1% Cap because of high primary property tax rates, and the school primary tax rate is 150% of the Qualifying Tax Rate (QTR) set by the legislature, then the school may not exceed that rate in the following year. It’s commonly referred to as a frozen tax rate.

The combination of the property tax limitations from the constitutional 1% Cap and the unlimited nature of taxation in very small school districts had long caused significant challenges. The school district equalization formula allows very small schools to set an additional tax rate on top of the normal formula, called Small School Adjustment (SSA, A.R.S. 15-949) to provide whatever funding their board deems necessary. This was done because statewide per pupil amounts don’t scale well in particularly small schools, even after adjusting for additional weights for being small and remote.

The hope was school boards in these rural areas wouldn’t abuse homeowners with high rates. However, homeowners are insulated from the combination of particularly high primary rates because total primary rates are capped at \$10 per \$100 of assessed value. In several areas, homeowners became immune to increases in SSA, leaving renters, ranchers, and other business owners to pay alone.

Between 1999 and 2009, the amounts for SSA increased statewide from \$9.6 million to \$24.6 million. While these amounts are tiny in the statewide K-12 budget, they amounted to large tax rates in rural Arizona, and in some cases have been exorbitant (see ATRA May 2019 and January 2018 newsletters). Largely thanks to this reform, the amounts stopped their dramatic growth and were just \$22.5 million last year.

SSA districts are found across the state but are concentrated in Yavapai and Cochise counties, where they have an abundance of tiny school districts. Cochise County has eleven SSA districts and Yavapai County has eight.

As proof that many districts would otherwise exceed and sometimes dramatically exceed their capped rate, several districts often spike their SSA at every turn to keep their “frozen” tax rate at the maximum level. In FY 2021, seven small districts significantly increased their SSA amount, despite the significant increases in K-12 formula funding over the last several years.

Riding a net assessed valuation (NAV) increase of 80% in their district, Ash Creek Elementary in Cochise County increased its SSA 128% this year, with a \$290k levy that doubled their formula funding for its 23 students.

In Gila County, Hayden-Winkleman Unified made use of a 54% increase to its NAV by raising its SSA 71% to \$2.4 million, doubling their formula funding. Hayden isn’t nearly as small as others in this category, but technically qualifies because it has less than 100 high schoolers.

In La Paz County, Salome Elementary increased their SSA 60% to \$800k, more than doubling their formula funding to educate its 98 students. Bouse Elementary increased their SSA 39% to \$606k which doubles their

formula budget for their 37 students.

In Santa Cruz County, Sonoita Elementary increased their SSA 31% to \$600k, an amount worth roughly 2/3 of their formula budget for their 102 students.

In Yavapai County, Kirkland Elementary increased their SSA 28%, a result of keeping their primary rate flat amidst decreased enrollment. Yarnell Elementary increased their SSA 11% to keep their primary rate flat.

No part of funding rural schools is pretty. The state formula adjustments for small and rural clearly do not work for tiny districts. However, there is no uniformity between similarly small districts, with funding and taxation showing wide disparities—looking a lot like education funding before equalization efforts 40 years ago. While the maximum tax rate law is a blunt instrument, it has successfully curbed some of the excesses, slowed the growth of SSA, and kept rates from becoming worse in some corners. For taxpayers, it has been a useful tool that should continue at least until lawmakers decide to do something about the unlimited SSA.

To the right is the review of the maximum tax rates as conducted annually by the Property Tax Oversight Commission, which is staffed by Darlene Teller at the Department of Revenue.

- Sean McCarthy

| 2020 Review of Primary Property Tax Rate Limits per § 42-17151 | | | | | | | | |
|--|---------------------------|------------------------|-------------|-------------------------|-------------------------|-------------|-------------------------|--|
| County | School District | 2019 Adopted Tax Rates | | | 2020 Expected Tax Rates | | | Does the 2019 Tax Rate Exceed 2018 Rate? |
| | | Elementary District | High School | Unified School District | Elementary District | High School | Unified School District | |
| Cochise | | | | | | | | |
| 1 | Elfrida ESD #12 | 4.5790 | | | 4.5790 | | | No - Okay |
| 2 | Bowie USD #14 | | | 10.8023 | | | 10.8023 | No - Okay |
| 3 | San Simon USD #18 | | | 8.9393 | | | 8.9393 | No - Okay |
| 4 | Pearce ESD #22 | 4.1597 | | | 4.1597 | | | No - Okay |
| 5 | Douglas USD #27 | | | 6.1244 | | | 5.1875 | No - Okay |
| 6 * | Double Adobe ESD #45 | 8.5783 | | | 8.5783 | | | No - Okay |
| 7 | Ash Creek ESD #53 | 5.1239 | | | 5.1239 | | | No - Okay |
| 8 * | McNeal ESD #55 | 8.0630 | | | 8.0630 | | | No - Okay |
| 9 * | Pomerene ESD #64 | 6.5088 | | | 6.5088 | | | No - Okay |
| 10 | Valley Union High #201 | | 3.1994 | | | 3.1164 | | No - Okay |
| Coconino | | | | | | | | |
| 11 | Grand Canyon USD #4 | | | 12.0990 | | | 12.0990 | No - Okay |
| Gila | | | | | | | | |
| 12 * | Young ESD #5 | 6.5216 | | | 6.2887 | | | No - Okay |
| 13 * | Tonto Basin ESD #33 | 6.8236 | | | 6.8236 | | | No - Okay |
| 14 | Hayden-Winkelman USD #41 | | | 11.8875 | | | 11.8875 | No - Okay |
| Graham | | | | | | | | |
| 15 * | Bonita ESD #16 | 6.4410 | | | 6.4410 | | | No - Okay |
| La Paz | | | | | | | | |
| 16 | Wenden ESD #19 | 5.3886 | | | 5.3886 | | | No - Okay |
| Maricopa | | | | | | | | |
| 17 | Isaac ESD #5 | 5.3378 | | | 5.3378 | | | No - Okay |
| 18 * | Mobile ESD #86 | 7.8876 | | | 7.8876 | | | No - Okay |
| Pima | | | | | | | | |
| 19 | Tucson USD #1 | | | 5.8229 | | | 5.6429 | No - Okay |
| 20 | Redington ESD #44 | 7.3742 | | | 7.3742 | | | No - Okay |
| Pinal | | | | | | | | |
| 21 | Mammoth-San Manuel USD #8 | | | 6.0739 | | | 5.9015 | No - Okay |
| Santa Cruz | | | | | | | | |
| 22 | Patagonia ESD #6 | 4.2363 | | | 4.0417 | | | No - Okay |
| 23 | Sonoita ESD #25 | 4.6271 | | | 4.6271 | | | No - Okay |
| 24 | Santa Cruz ESD #28 | 7.4375 | | | 7.4375 | | | No - Okay |
| Yavapai | | | | | | | | |
| 25 | Ash Fork USD #31 | | | 8.3880 | | | 7.4630 | No - Okay |
| 26 | Seligman USD #40 | | | 7.7237 | | | 7.7237 | No - Okay |

* Elementary Districts not located within a High School District.