

*Celebrating ATRA's 80th  
Anniversary as the  
Taxpayer's Watchdog*



**ATRA  
OUTLOOK  
CONFERENCE &  
ANNUAL MEETING**



Sponsored by:



**aps**



**FREEPORT-McMoRAN**



**University of Phoenix®**





# ATRA 2021 Outlook Conference

## Thursday, November 18th

Scottsdale Hilton Resort

Registration Begins at 7:45 a.m.

### ➤ State Budget Outlook 8:30 a.m.

The Director of OSPB will present a current report on the state's fiscal picture and FY 2023 budget challenges.

Matt Gress, Director, Governor's Office of Strategic Planning & Budgeting

### ➤ National Tax Perspective 9:15 a.m.

Erica Kenney of *COST* will provide updates on major tax issues in states around the nation and discuss proposed changes at the Federal level.

Erica Kenney, West Coast Tax Counsel, Council on State Taxation

### ➤ Break: 10:00 a.m.

### ➤ Litigation Update 10:15 a.m.

Lawyers from the Arizona Attorney General's Office and the Goldwater Institute will discuss key legal issues surrounding the *Gift Clause* and the AG's ability to enforce civil law.

Beau Roysden, OAAG  
Jon Riches, Goldwater Institute

### ➤ Key AZ Tax Issues 10:45 a.m.

ATRA staff will highlight the state and local public finance and taxation issues facing taxpayers in 2022.

Kevin McCarthy, ATRA President  
Jennifer Stielow, ATRA Vice President

### ➤ Legislative Update 11:15 a.m.

Key Arizona lawmakers at the center of fiscal policy debates will provide their views on the upcoming legislative session.

Senator J.D. Mesnard  
Representative Regina Cobb

## Keynote Speaker: Governor Doug Ducey

Individual: \$150; Table of 8: \$1,200

\*CLE & CPE Credits Available

For registration and sponsorship information, please call the ATRA office at (602) 253-9121

## 2021 Headline Sponsors:



**FREEPORT-McMoRAN**



University of Phoenix®







# State Budget Outlook

***Arizona Tax Research Association***

November 18, 2021

Governor's Office of Strategic Planning and Budgeting

November 18, 2021

1

## Roadmap

---

- **COVID-19 and Arizona's Response**
  - Data driven decision making
  - Preserving Arizonans' livelihoods
- **Arizona's Economic Success**
  - The Arizona economy remained resilient in the face of the pandemic
  - Arizona continues to be a model state for employment
  - Our economic success is drawing movers to AZ
- **Maintaining A Structurally Sound Budget**
  - New revenue streams are bolstering revenue performance
  - Helping to ensure future economic growth through historic income tax cuts
  - Carrying our strong cash and structural position into the future

November 18, 2021

2

# COVID-19

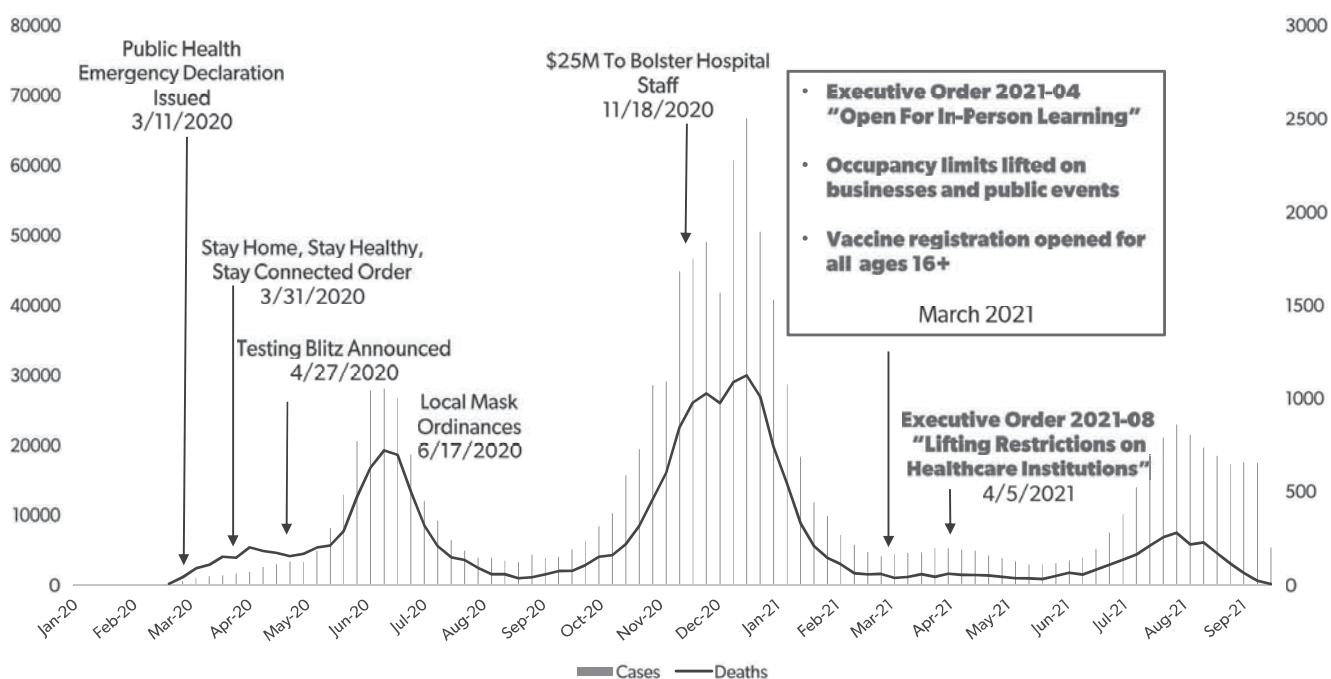
"Arizonans have the ability to protect themselves from COVID-19 thanks to the vaccine. Businesses are open, students are back in the classroom, loved ones are gathering and our economy is booming."

- Governor Doug Ducey

November 18, 2021

3

## COVID-19 In Arizona

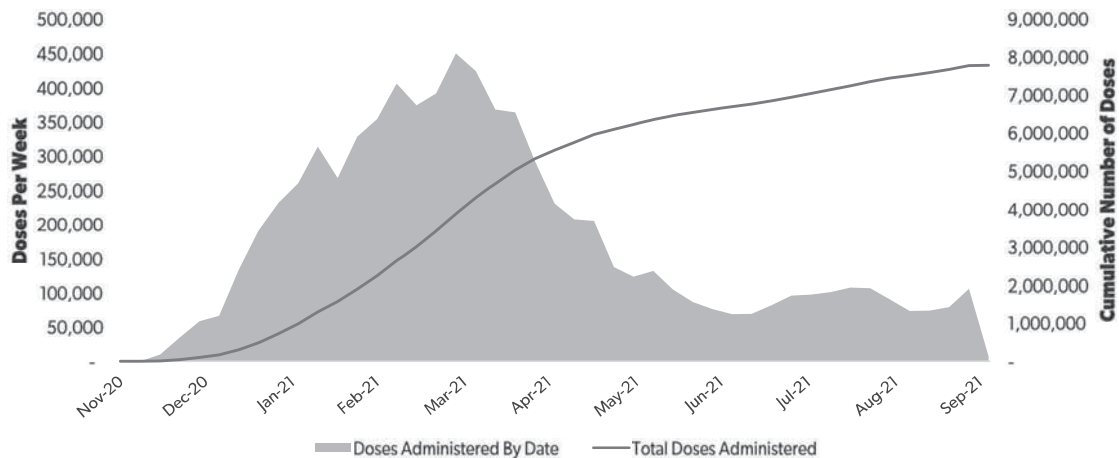


November 18, 2021

4

# Vaccine Distribution

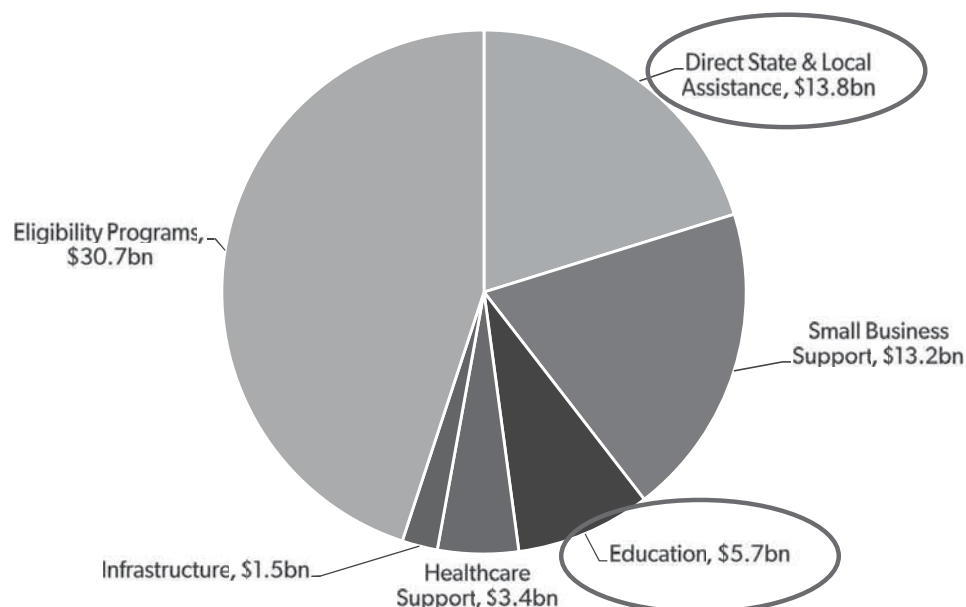
- As of the beginning of November 2021, **8.3 million** doses of the Coronavirus vaccine have been administered in Arizona
- **69.9%** (3,794,028) of eligible Arizonans are **fully vaccinated**, and **88.9%** of Arizonans 65 and older have received at least one dose



November 18, 2021

5

# Arizona Has Received Nearly \$70 Billion in Federal Support



November 18, 2021

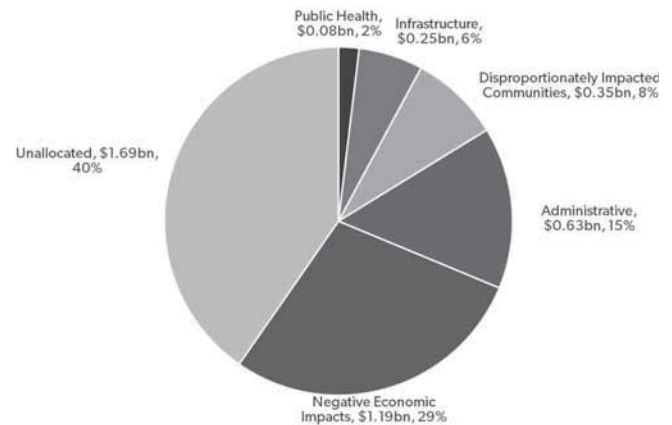
6

# About 40% of American Rescue Plan Act Monies Remain Unallocated

- Of the amounts received from GEER I and II, the "CARES" Act, and the American Rescue Plan Act (\$6.14B), roughly 29% remains unallocated, meaning the State has **\$1.79B** in additional resources to spend

Federal Funding Source Availability						
	Dec. 2025/2026		Dec. 2021		Sept. 2021/2022	
	State Fiscal Recovery Fund - ARPA		Coronavirus Relief Fund - CARES		GEER I & II	
Unallocated	\$1.69 B	40%	\$0.06 B	3%	\$40.8M	41%
Obligated	\$2.50 B	60%	\$1.79 B	97%	\$59.3M	59%

## ARPA Allocations To Date

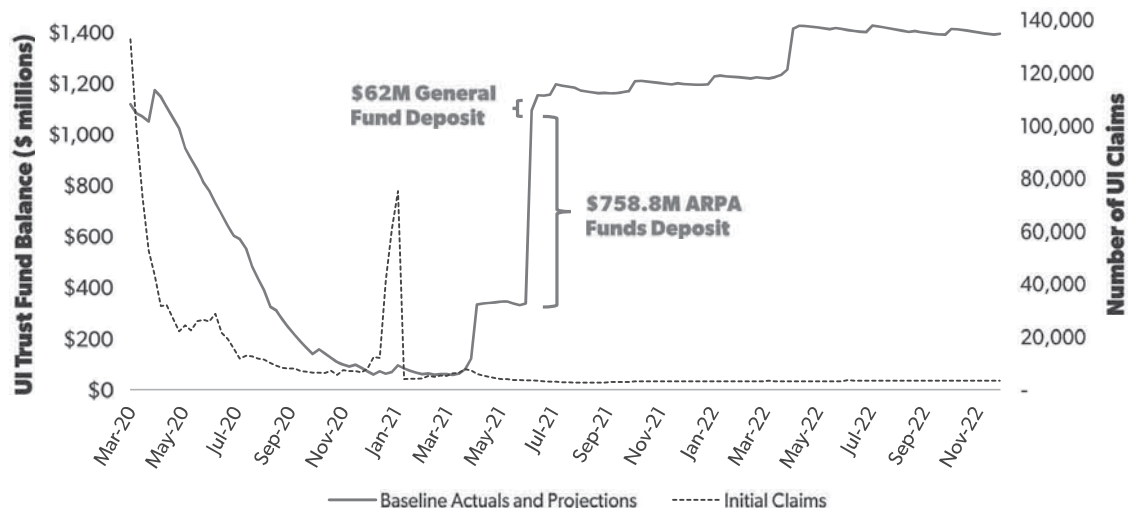


November 18, 2021

7

# Arizona Ensures Financial Security Of Unemployment Trust Fund

- Arizona leveraged federal funding from the American Rescue Plan Act (ARPA) State Fiscal Recovery Fund and General Fund monies to bolster the UI Trust Fund with \$820.8M in deposits



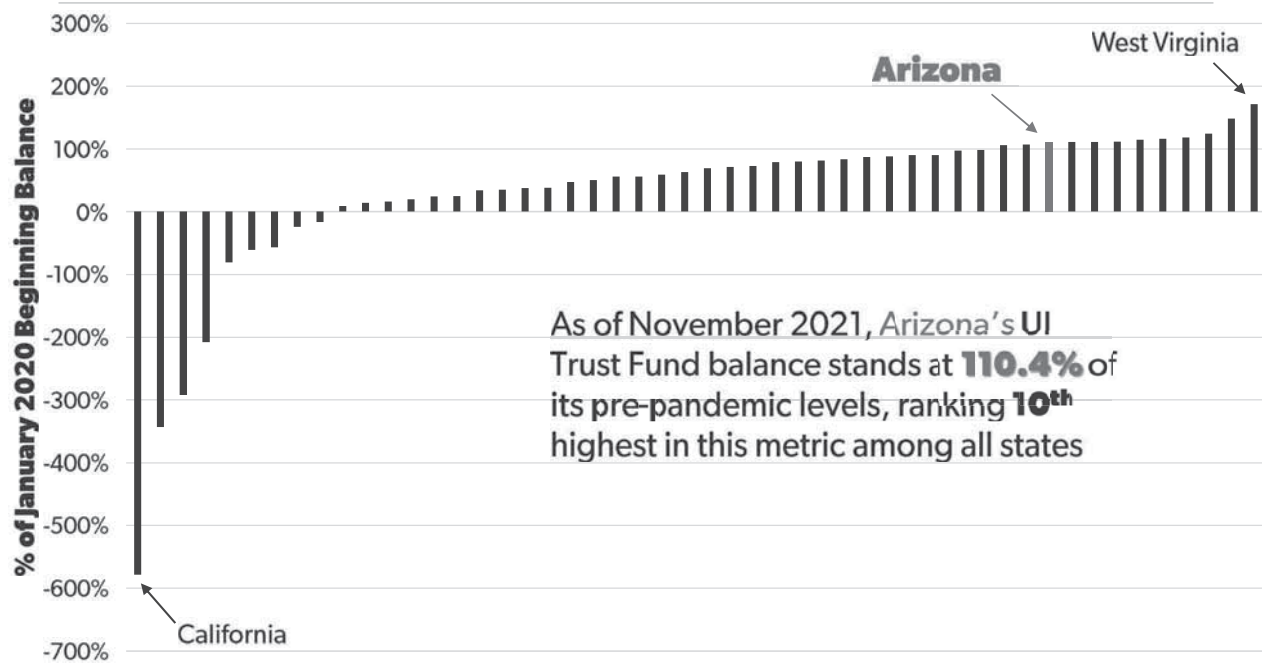
\*Data accurate as of 8/25/2021

November 18, 2021

8



# November 2021 Net UI Trust Fund Balance



Net balance is cash balance net of outstanding Title XII Advance debt

November 18, 2021

9

## Lessening The Burden On Arizona Businesses

- With over \$820M in deposits into the UI Trust Fund, the Department of Economic Security projects the employer UI tax rate to fall **.92% points** for CY 2022, saving Arizona businesses up to **\$64 per employee\***

**CY 2022 UI Tax Rate  
Before Deposit**

**2.4%**

**\$820.8M  
Deposit**



**Est. UI Tax Rate  
After Deposit**

**1.48%**

Per Employee Savings\*  
**\$64**



Total Non-Farm Employment\*\*  
**2,972,100**



Total Estimated Savings\*\*\*  
**\$190M**

\* Employees making at least \$7,000 in gross wages per calendar year.

\*\* September total non-farm employment

\*\*\* Estimate assumes all employees gross at least \$7,000 in annual wages.

November 18, 2021

10



# Changes To Unemployment Insurance

Increased Unemployment Benefits

**\$320**



**\$240**

**33%** Increase in the weekly unemployment benefits amount beginning in 2023

Increased Income Disregard

**\$160**



**\$30**

Increased the amount a person can earn from partial employment, moving AZ from last to **18<sup>th</sup> in the nation**

Expanded The Taxable Wage Base

**\$8,000**

Increased benefits will be funded by an increase in the wage base which UI taxes are applied; Arizona would be tied for **6<sup>th</sup> lowest** in the country

November 18, 2021

11

## Economy

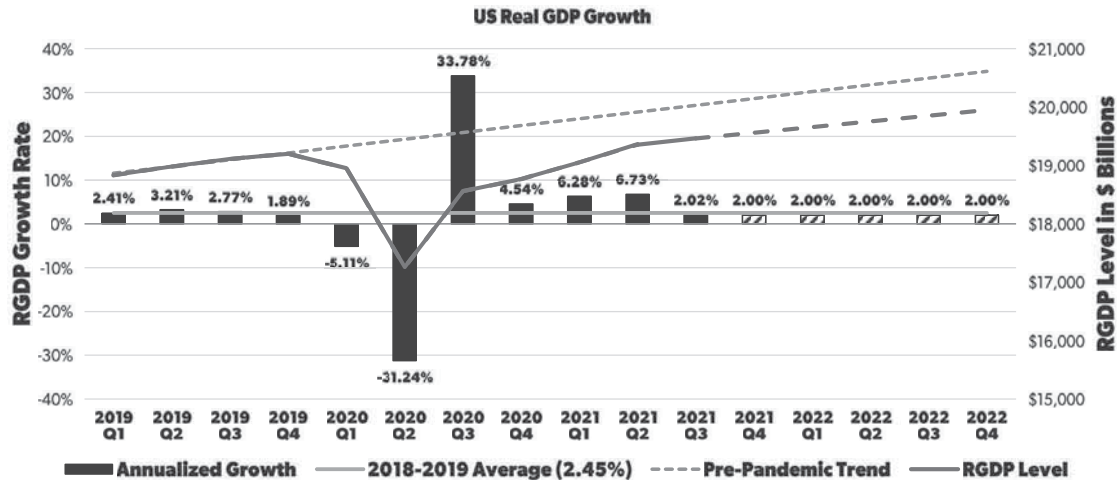
*"Arizona has emerged as the destination for key high-tech, high-wage industries like semiconductors, electric vehicle manufacturing, startups and more. Over the next decade, Arizona will remain a leader in the U.S. for people, businesses and jobs moving to our state."*

- Governor Doug Ducey

November 18, 2021

12

# Unprecedented GDP Volatility



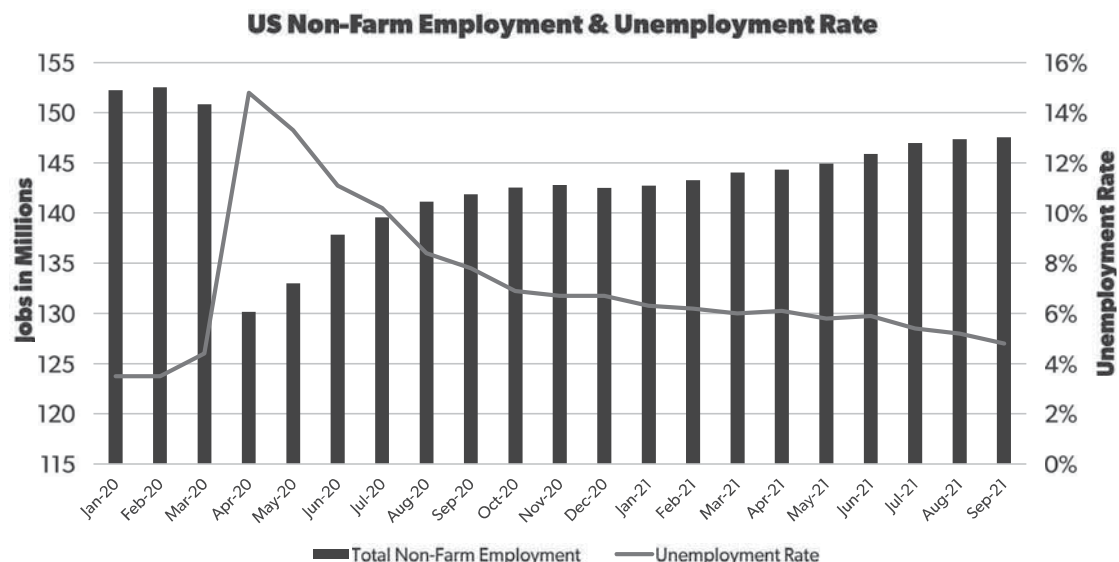
- After unprecedented volatility during the pandemic, **U.S. growth is slowing**
- It will take sustained growth well above 2.45% in order to reach the pre-pandemic trend

November 18, 2021

13

# US Employment Heavily Impacted By COVID-19

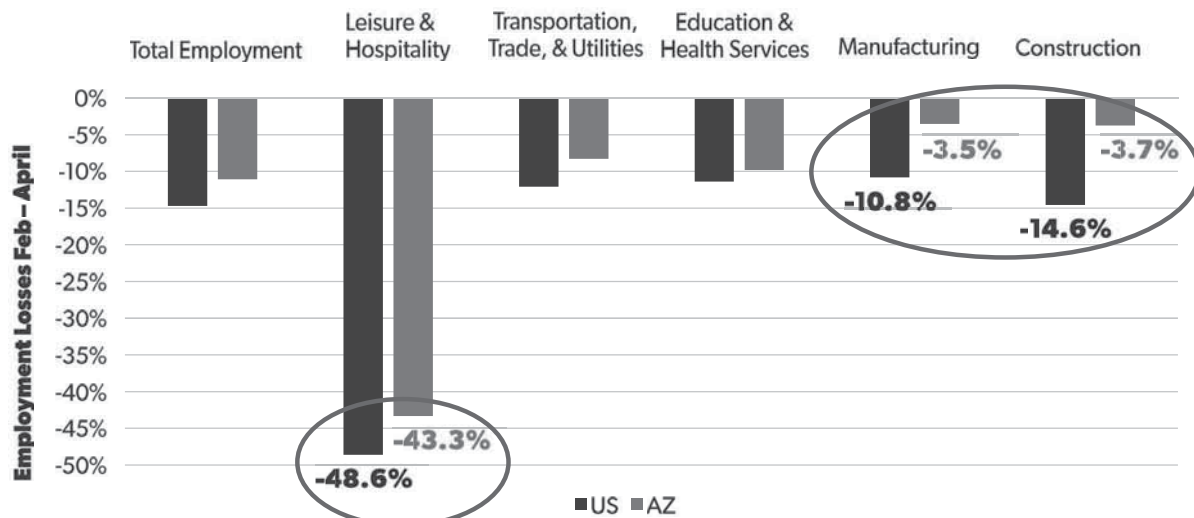
- After suffering enormous declines in the spring, US employment experienced sharp yet short-lived employment growth in the summer of 2020
- Employment gains picked up again in the summer of 2021 but have since tapered off



November 18, 2021

14

# Arizona Withstood Recession Better Than US



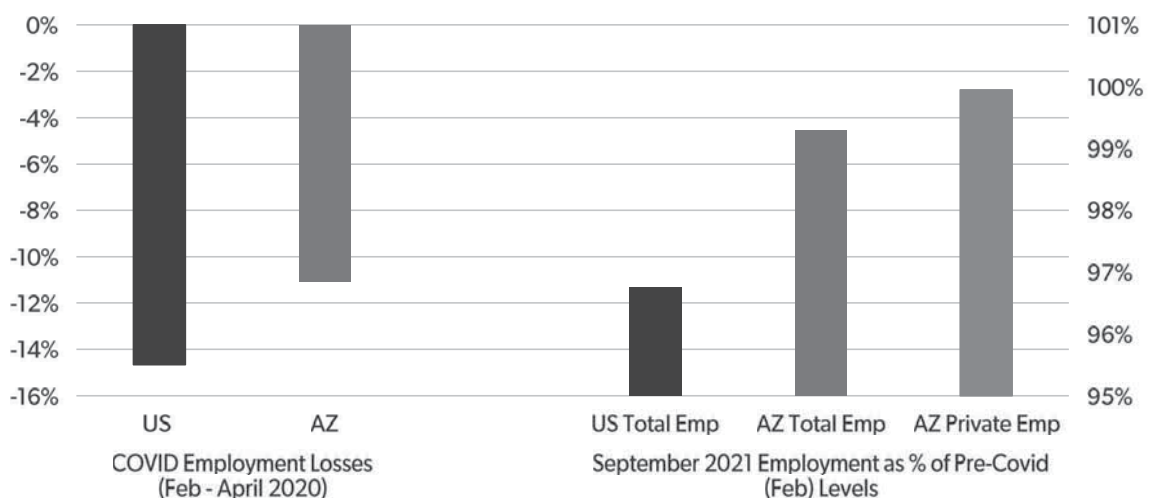
- Despite having similarly composed labor markets, Arizona experienced much lower employment declines than the nation as a whole during the COVID-19 recession
- Higher-wage industries like Manufacturing and Construction were also more insulated from the recession in Arizona relative to the US

November 18, 2021

15

# Arizona Stronger Than US In Jobs Retention And Recovery

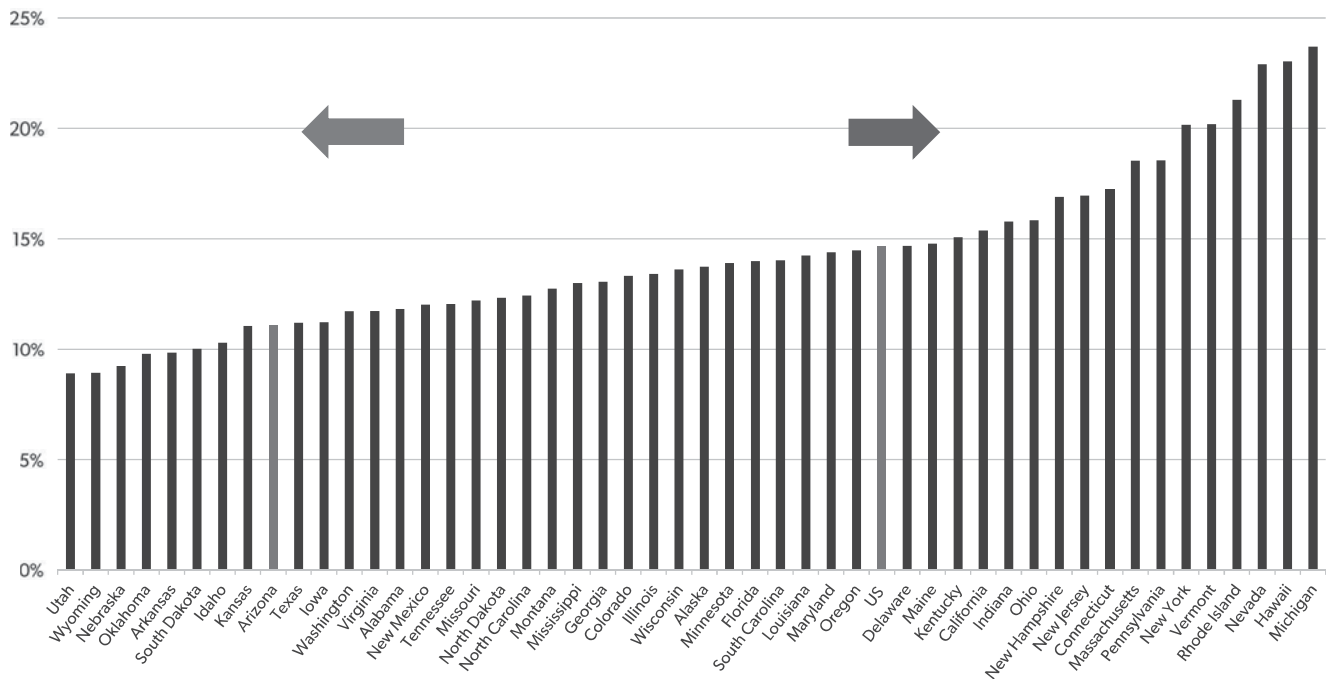
- As of September 2021, total employment in Arizona has recovered to over 99% of pre-COVID-19 levels, surpassing the nation by 3% and ranking an impressive **3<sup>rd</sup>** among all states
- Total private employment in Arizona is nearing pre-pandemic levels



November 18, 2021

16

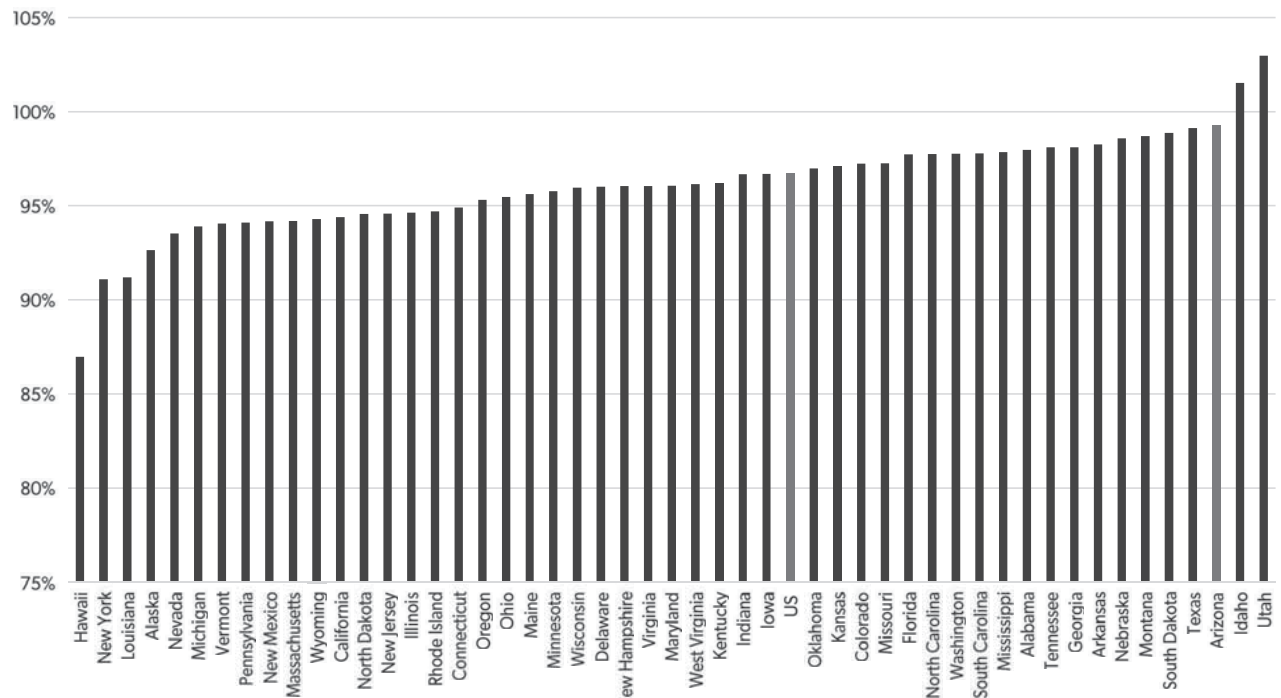
# COVID Recession Employment Losses by State



November 18, 2021

17

# September 2021 Share Of Pre-Pandemic Employment Levels



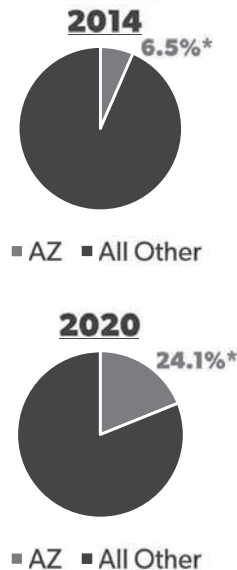
November 18, 2021

18



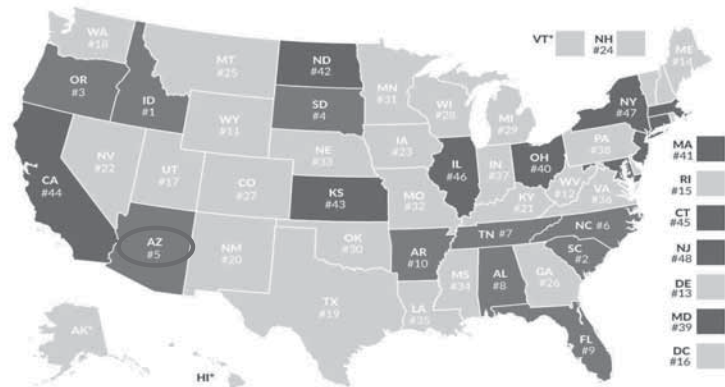
# Arizona Continues To Be A Top Choice For Movers In US

- Trend in migration is enduring; share of US total migration taken up by AZ continues to rise



## Where Did Americans Move in 2020?

State Migration Patterns, from Most Inbound to Most Outbound, 2020



TAX FOUNDATION

@TaxFoundation

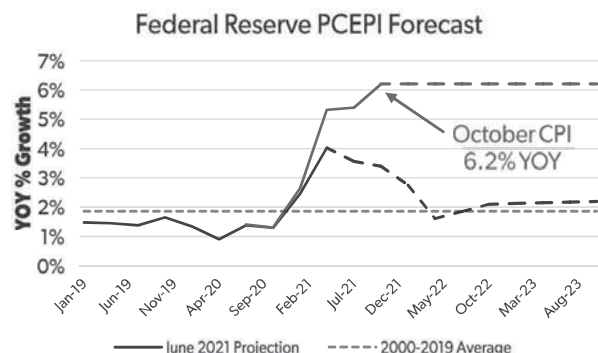
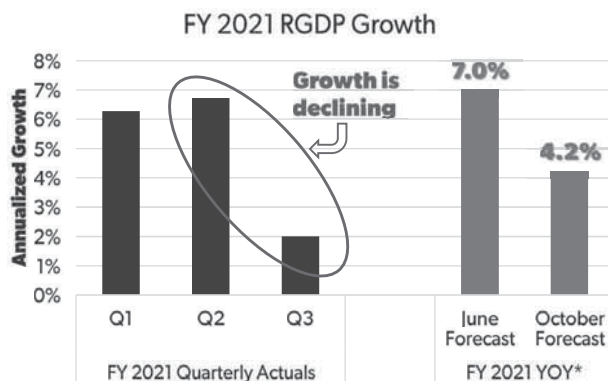
\*Source: U.S. Census Bureau State Population Totals: 2010-2020 net domestic migration

November 18, 2021

19

# Potential Economic Uncertainty In The Future

- Current Federal RGDP and inflation projections from the Federal Reserve Board and other national observers are **overly optimistic**; the US economy has slowed and is likely to continue slowing
  - The monthly CPI figure for October is at **6.2%** - the 5<sup>th</sup> month in a row over 5%, and the highest sustained rate of inflation in over 30 years
  - Growth experienced in Q3 is **less than 30%** of that experienced in Q2, and is **on target to miss the Fed's June forecast by 40%**



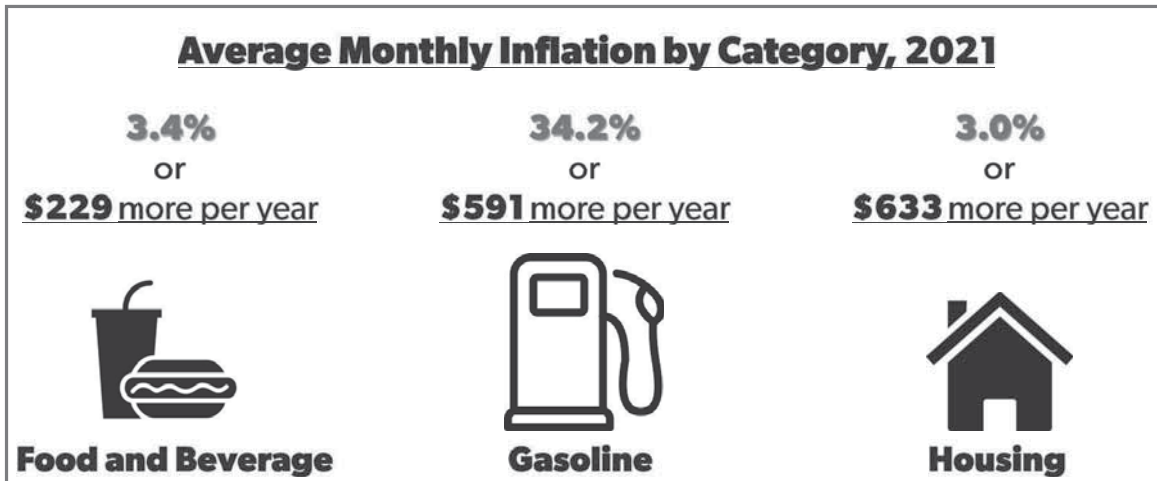
\* June forecast from June Federal Reserve Beige Book, October forecast OSPB projections

November 18, 2021

20

# Inflation Is Costing Arizonans

- While workers experienced a **2.8%** growth in earnings on average through 2021, the total cost of goods increased by **4.2%**, meaning the average household in the Phoenix Metro has seen their spending power erode by **\$2,600** in 2021
- Even after accounting for 10-yr avg inflation rates, Arizonans would still have to spend nearly **\$1,600** more per year for the same level of consumption

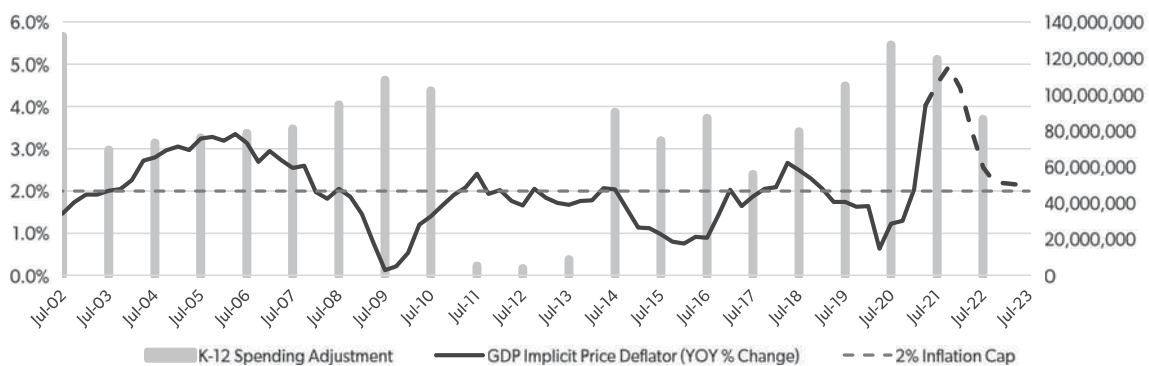


November 18, 2021

21

## Rising Inflation Presents Challenges For The State Budget

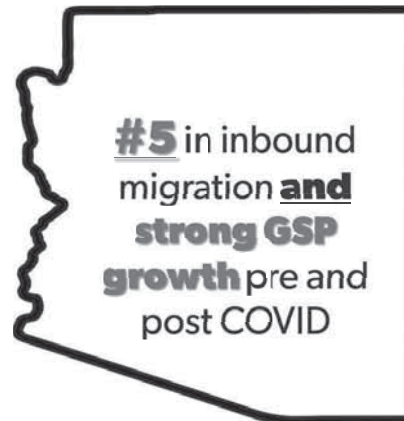
- Rising inflation may present budgetary challenges to the state in the form of:
  - Higher salary requirements
  - Larger budgets for State agencies (higher cost of doing business, i.e. goods and services)
  - Increases in baseline spending for K-12 is statutorily capped at 2%



November 18, 2021

22

# Arizona Is In A Strong Position Combat Economic Declines And High Inflation



- In addition to **business friendly policies, strong economic growth**, and **consistent inbound migration**, state governments collect revenues on a nominal basis, meaning revenues will be partially guarded from high inflation

\*For states who collect state income taxes

November 18, 2021

23

## High-Tech Businesses Flock To The Grand Canyon State

### Intel

In 2021, the largest semiconductor company broke ground on two new semiconductor fabrication plants in Arizona



**3,000** high-tech jobs  
**3,000** construction jobs  
**15,000** additional indirect jobs

### Taiwan Semiconductor

The world's largest dedicated independent semiconductor foundry has selected Arizona to house its new **\$12B** U.S. advanced semiconductor factory



**2,000** high-tech jobs  
**\$12B** investment into the state

### Lucid Motors

The up-and-coming electric vehicle manufacturer commissioned a new manufacturing facility in Arizona



**6,000** high-tech jobs  
**\$100M** projected additional annual tax revenue

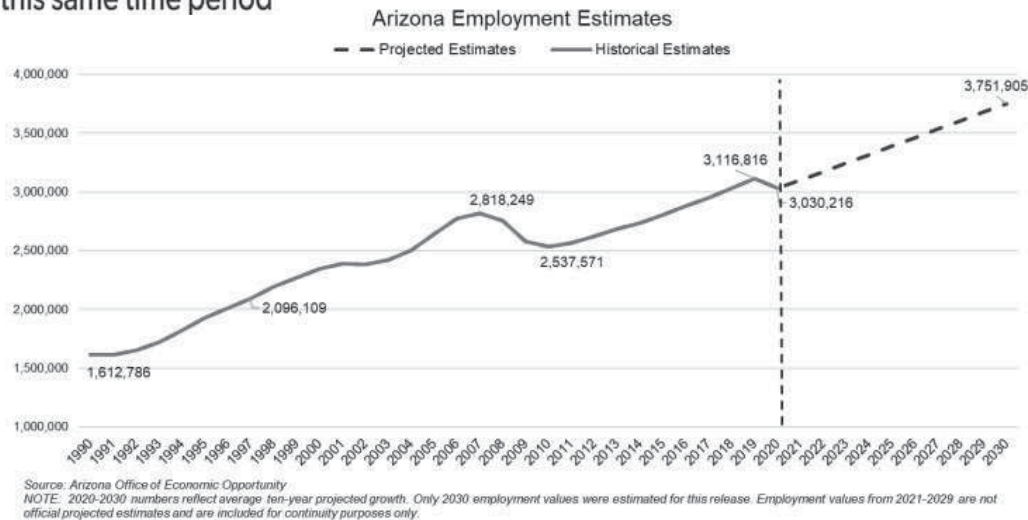
November 18, 2021

24



# Projections Put AZ Employment Growth Ahead Of Nation For 10 Years

- The Office of Economic Opportunity projects employment in Arizona to grow **2.2%** per year, translating to **over 700,000 new jobs** by 2030
- This growth dwarfs the 0.7% per-year growth estimate for the nation as a whole over this same time period



November 18, 2021

25

## General Fund Overview & Spending

*"While we're giving money back to taxpayers, this budget makes responsible, targeted and substantial investments in the things that matter."*

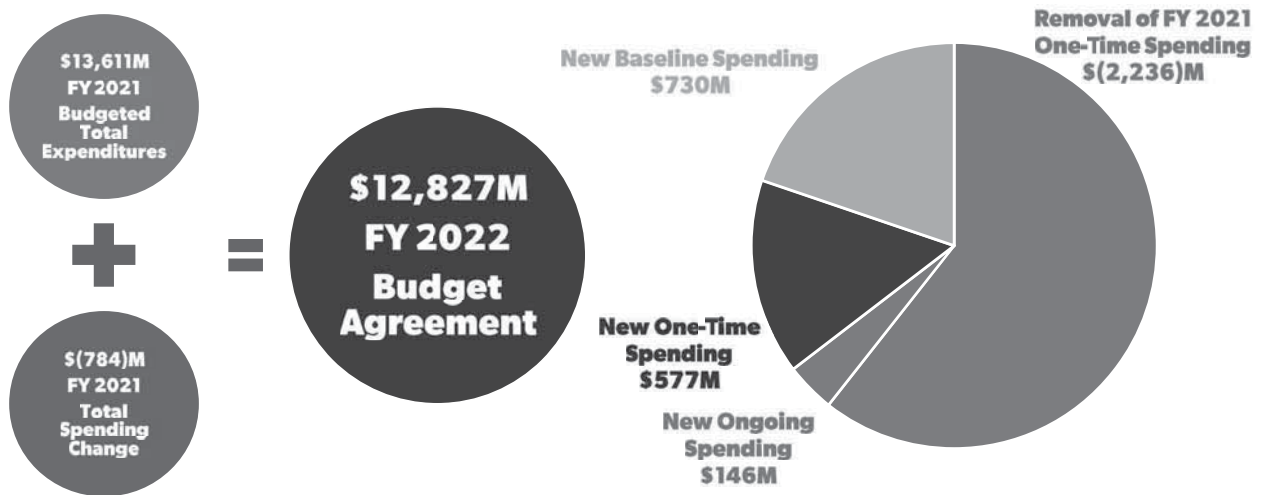
- Governor Doug Ducey

November 18, 2021

26



# FY 2022 Budget At-A-Glance

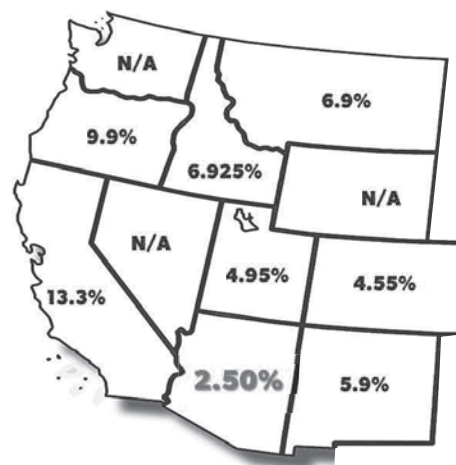


November 18, 2021

27

## Tax Cuts Ensure Arizona Remains Competitive

- The **2.5% flat tax** enacted in the FY 2022 budget will make the top marginal rate in Arizona over 2 percentage points lower than any other western state
- Additionally, the FY 2022 budget ushered in a **4.5% cap** on the top marginal rate paid by any Arizona taxpayer, preventing the nearly 78% increase in the top tax rate paid by Arizona small businesses as a result of Proposition 208

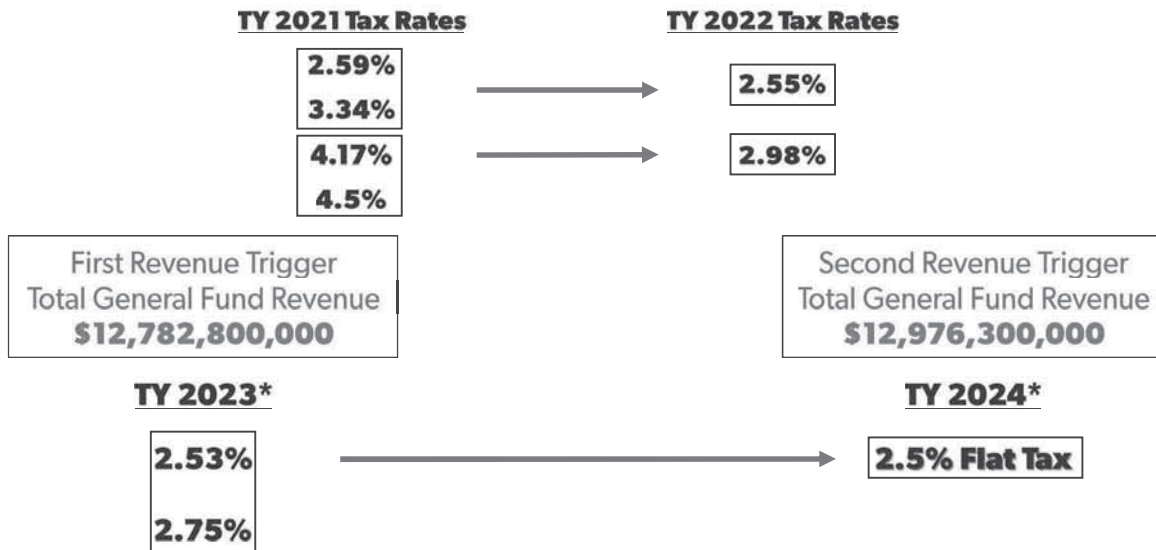


November 18, 2021

28

# Tax Cuts Contingent On Maintaining Strong Revenue Performance

- Income tax rates are reduced beginning in TY2022
- OSP is projecting that both revenue triggers will be hit in FY 2022, meaning rates will drop further in TY 2023 before reaching a **2.5% flat income tax rate** in TY 2024

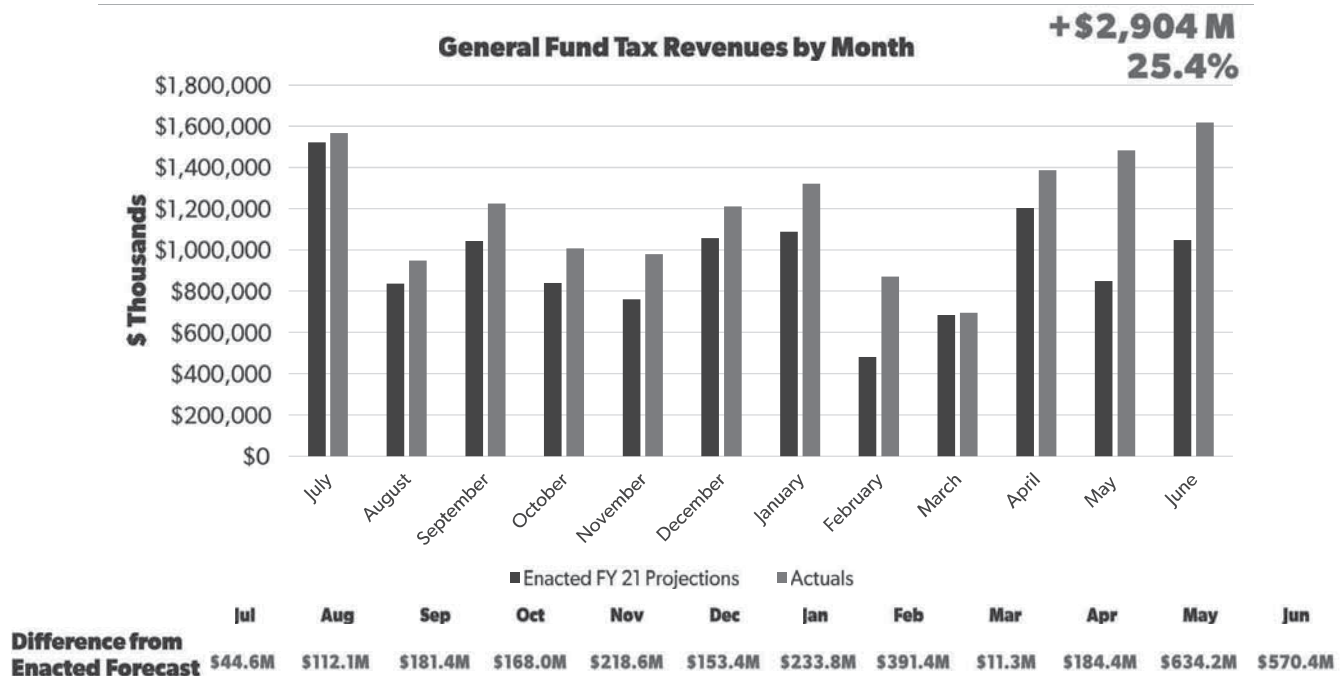


\*Not including 4.5% aggregate tax cap (including Proposition 208 surcharge)

November 18, 2021

29

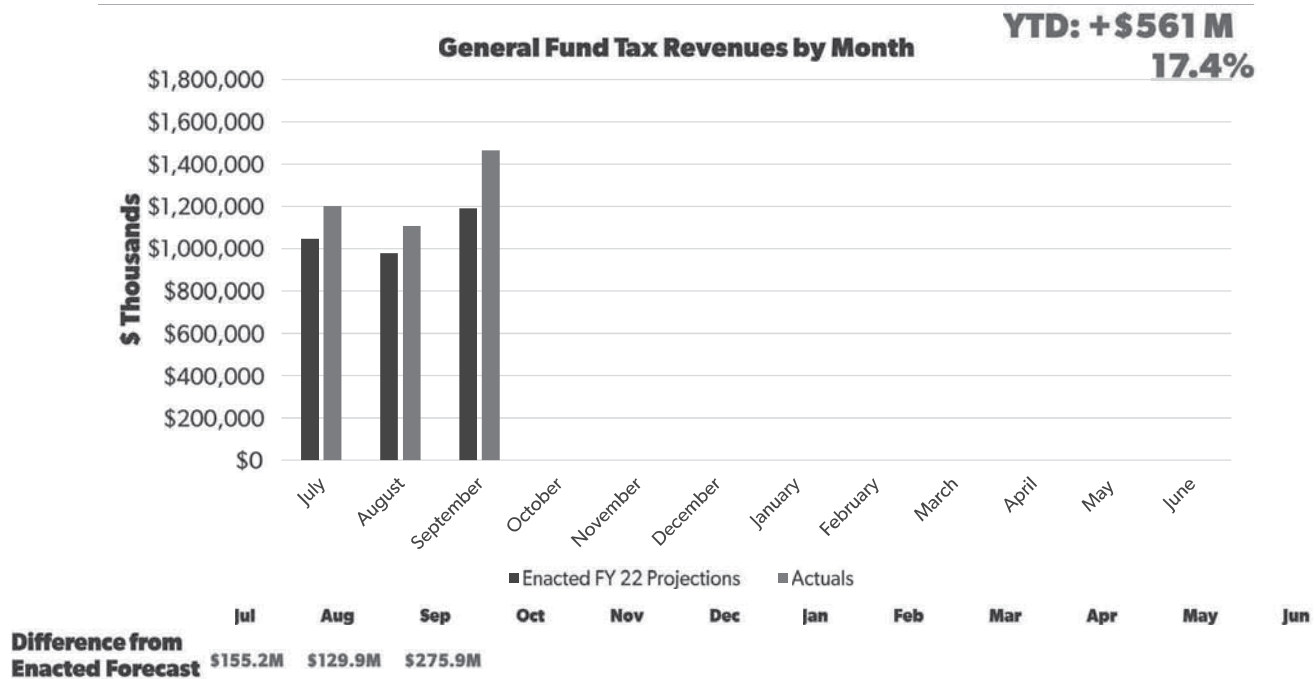
## FY 2021 General Fund Tax Revenues Performance vs Enacted Forecast



November 18, 2021

30

# FY 2022 Tax Revenues Continue To Outperform Conservative Forecasts



November 18, 2021

31

# Strong Tax Revenue Growth Continues Through September

**Current and Historical General Fund Revenue**  
\$ in millions

Tax Type	FY 2021 Prelim Actual	FY 2022 Budgeted	FY 2022 YTD Actuals	10-Year Avg
Sales	\$6,245	\$6,380	<b>15.6%</b>	2.8%
Individual	\$6,517	\$5,890	<b>(15.8)%*</b>	6.7%
Corporate	\$847	\$644	<b>23.5%</b>	(2.6)%
<b>Ongoing GF</b>	<b>\$14,061</b>	<b>\$13,403</b>	<b>(1.5)%</b>	<b>3.2%</b>

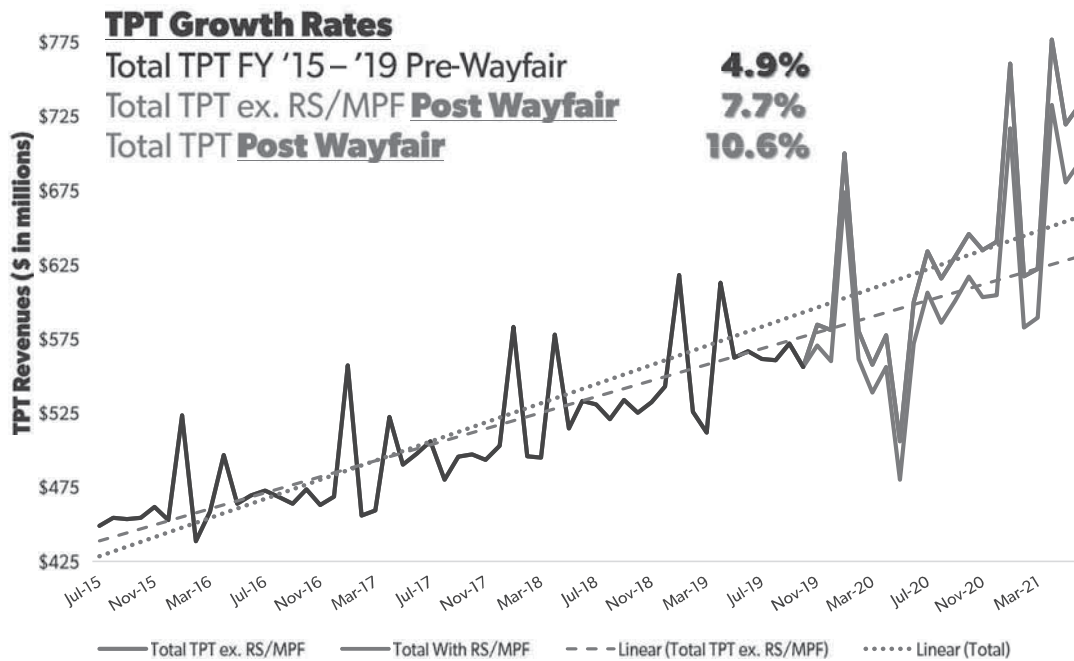
Source: Joint Legislative Budget Committee, FY 2022 Appropriations Report;  
JLBC Monthly Fiscal Highlights

\* Does not account for an estimated \$600M in deferred tax payments received in FY 2021. Correcting for this yields a **22.5%** growth in individual income taxes YTD

November 18, 2021

32

# Wayfair Changes Have Amounted To New Revenues For The State And Localities

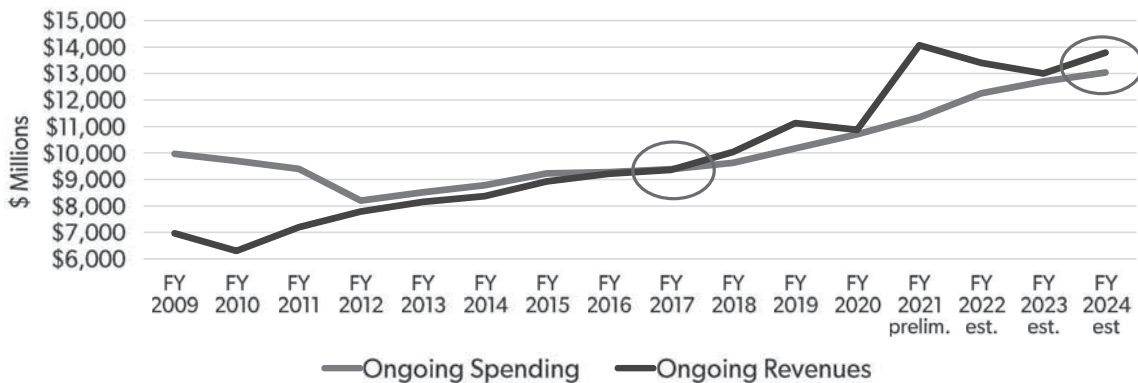


November 18, 2021

33

## FY 2022 Budget Outlook

- The Budget remains structurally and cash balanced through FY 2024
- This is achieved even in the midst of the largest tax cut in AZ history, along with over \$105M in increased funding for K-12 and \$42M for public safety



\$ millions	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024
Cash	\$372M	\$894M	\$1,096M	\$1,136M	\$1,554M
Structural	\$177M	\$2,716M	\$1,153M	\$300M	\$750M

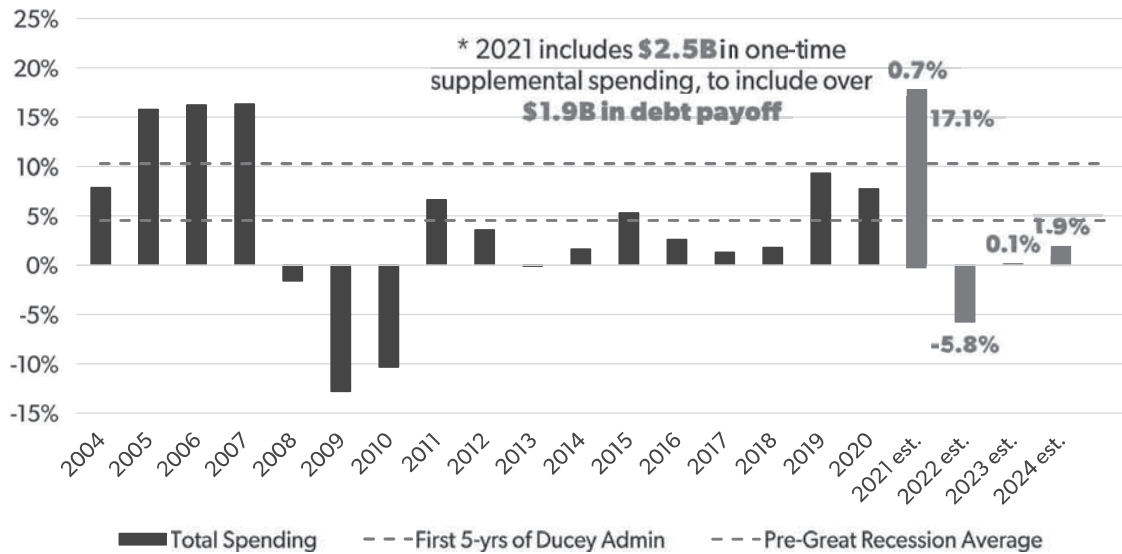
Source: Joint Legislative Budget Committee, FY 2022 Appropriations Report  
 Note: The FY 2022 Appropriations Report treats the effects of the 4.5% cap and SB 1783 as one-time

November 18, 2021

34



# Total General Fund Spending Growth



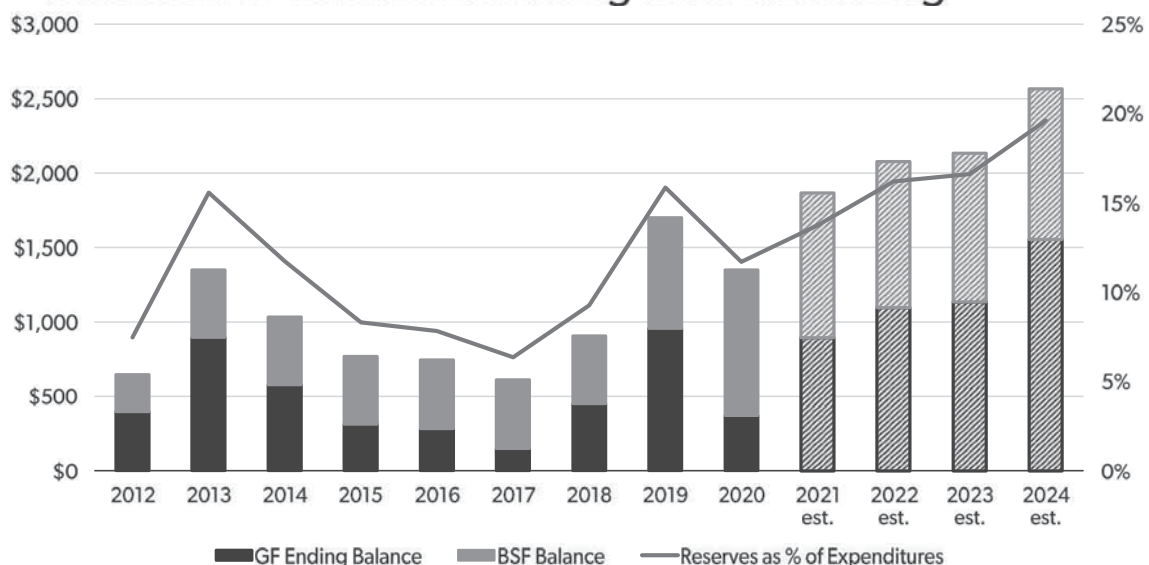
- Oh the **17.8%** total spending growth in FY 2021, **17.1%** (or nearly \$2B) is associated with **one-time debt reduction**

November 18, 2021

35

# State General Fund is Positioned Well

- Despite nation-wide economic instability, Arizona continues to set itself on strong financial footing



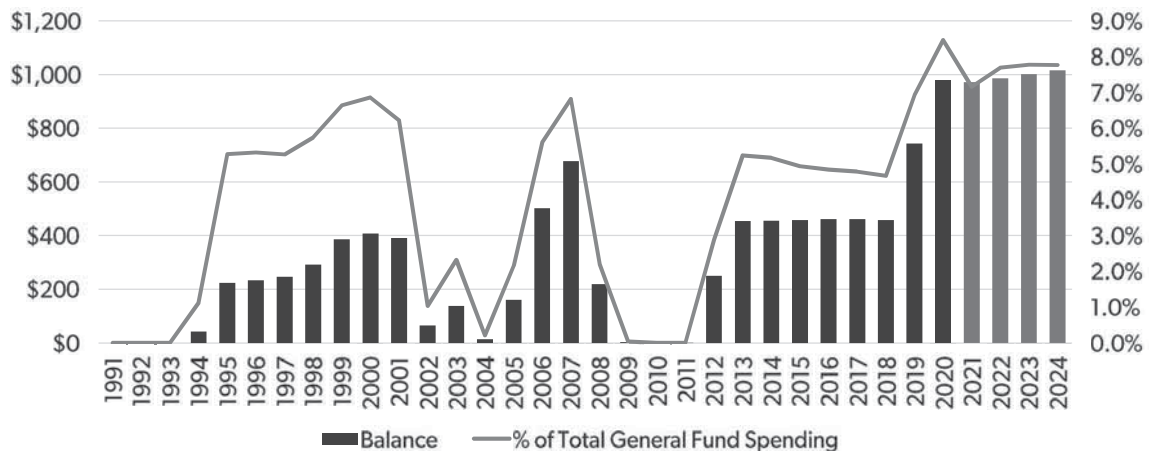
BSF amount for 2022 from FY 2022 Budget. Future amounts assume 1.5% growth.

November 18, 2021

36

# Arizona's Rainy Day Fund

- At the end of FY 2021, the Budget Stabilization Fund stood at \$972.2 million, or just over 7% of total General Fund Expenditures.



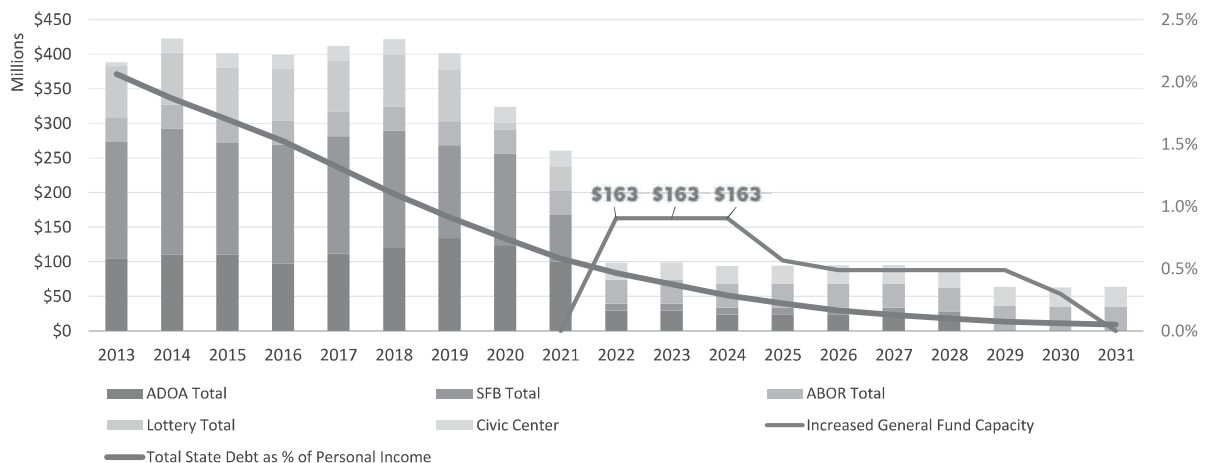
November 18, 2021

37

## FY 2022 Budget Includes Pay-Off Of 54% Of General Fund Debt Obligations

- By investing \$972.1M to pay off General Fund debt obligations, the FY 2022 budget frees up **\$163M** per year in General Fund capacity between FY 2022 and FY 2024.

Historical General Fund Outlays, FY 2013-2031 Projected

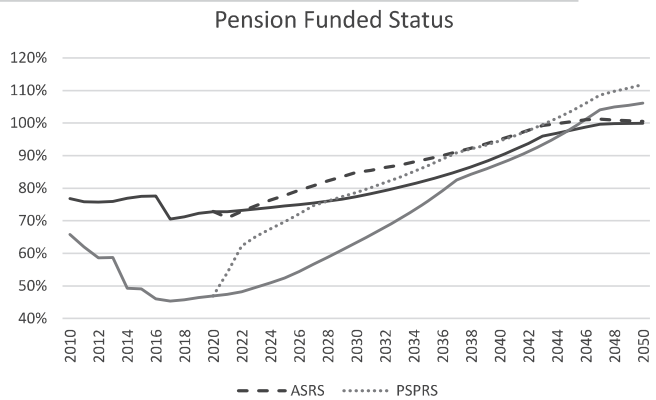


November 18, 2021

38

# State's Unfunded Liability

- Historic contributions to CORP and PSPRS
  - FY 2021: \$1.6 billion
  - FY 2022 (YTD): \$1.2 billion
- CORP
  - Reduced overall unfunded liability by 27%
  - Reduced State's portion of unfunded liabilities by 7.2 percentage points
- PSPRS
  - Reduced overall unfunded liability by 11%
  - Reduced State's portion of unfunded liabilities by 4.8 percentage points



Arizona Pension System Data

	ASRS	CORP	PSPRS	EORP
Active Members <sup>1</sup>	210,135	10,936	18,677	457
State Share	12.3%	70.9%	6.3%	20.6%
<b>Projected Funded Status</b>	<b>71.7%</b>	<b>65.0%</b>	<b>52.5%</b>	<b>32.1%</b>

<sup>1</sup> Data Source: ASRS – Actuarial Valuation Report June 30, 2020; CORP, PSPRS, and EORP – Comprehensive Annual Financial Report - June 30, 2020.

<sup>2</sup> Data Source: Actuarial Valuation Report, June 30, 2020 for ASRS, CORP, PSPRS, and EORP. Adjustments were made to CORP and PSPRS to reflect additional contributions through June 30, 2021. These numbers exclude the health insurance plans which are all funded over 100%.

November 18, 2021

39

## State Retirement Contributions

- A **\$1 billion** investment into the State's retirement systems to ensure benefits for critical public safety employees
  - \$500 million to CORP on behalf of the Department of Corrections, Rehabilitation & Reentry
  - \$500 million to PSPRS on behalf of the Department of Public Safety
- The deposit will result in an estimated savings to the State of **\$109 million** in FY 2023
- Cumulative savings are projected to be **\$1.9 billion**

	PSPRS - DPS		CORP - ADCRR	
	June 30, 2020	Reduced Unfunded Liability Estimate	June 30, 2020	Reduced Unfunded Liability Estimate
Unfunded Liability	897,835,692	397,835,692	1,043,641,543	543,641,543
Funded Percent	32.0%	69.9%	51.0%	74.5%

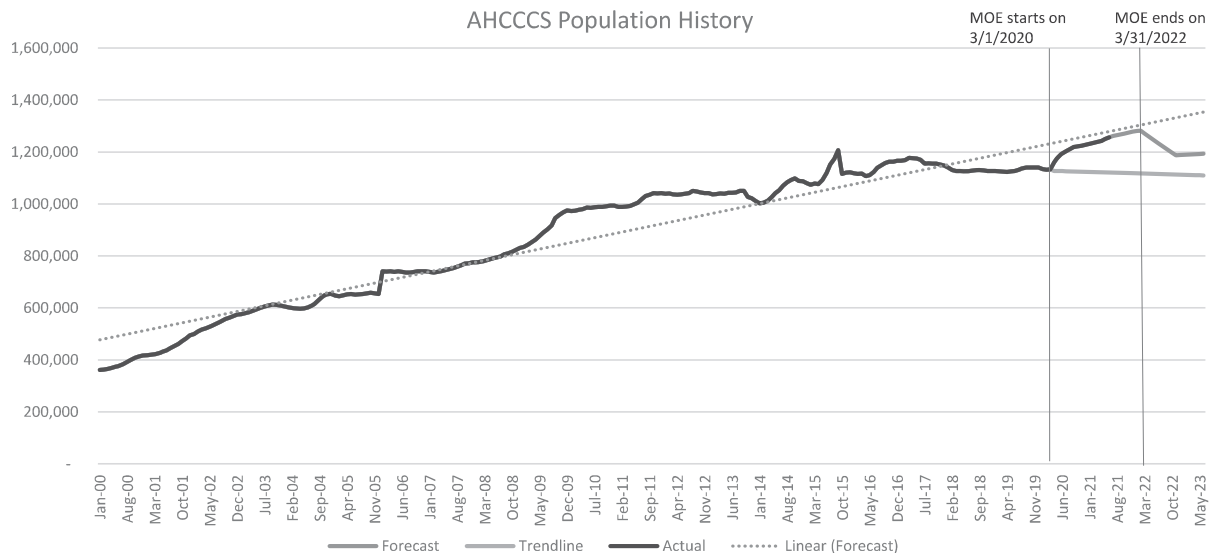
Data Source: PSPRS and CORP Consolidated Actuarial Valuation, June 30, 2020

November 18, 2021

40

## Caseloads - Medicaid

- Higher than linear forecast caseload growth due to COVID-19 and the Maintenance of Efforts (MOE).

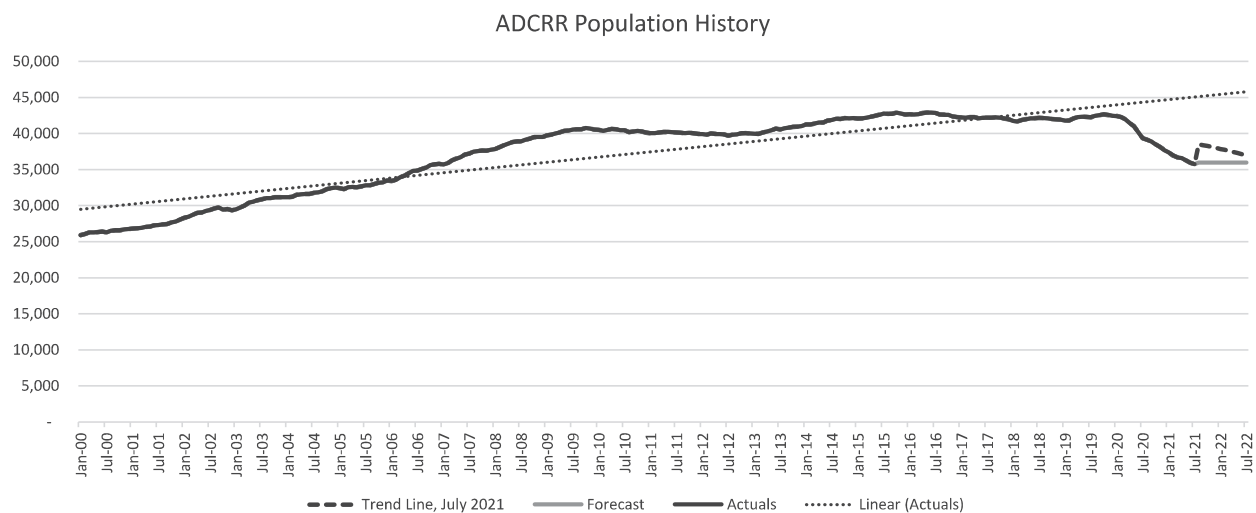


November 18, 2021

41

## Caseloads - Corrections

- Corrections inmate population has continues to decline since the beginning of the Ducey administration, alleviating a General Fund cost pressure
- The focus will remain on "2<sup>nd</sup> Chance" programs to sustain lower levels



November 18, 2021

42



# Education

- Continued investments to increase teacher pay, improve school capital, and otherwise roll back Recession-era cuts have enjoyed widespread public support
- The positive impact of Proposition 123, shown by the permanent land trust being in its best position ever with record breaking disbursements and market value, has been felt by schools across the state.

K-12 Spending			
	FY 2015	FY2022	
Per Pupil Funding <sup>1</sup>	\$8,798	\$12,371	✓
Flexible School Capital Funding (Additional Assistance)	\$254.6 million in formula funding suspensions	Fully restored ahead of schedule in FY 2022 Enacted Budget	✓
Proposition 301 – TPT Revenue	Revenue source expires FY 2021	Revenue source extended FY 2041	✓
New School Construction Funding	After capacity is reached	2 years before capacity is reached	✓
Basic State Aid Funding Timelines	Shifted to payment dates during recession and begun rollover gimmick	In FY 2022 Enacted Budget, rolled dates back and began paying down rollover at \$65 M	✓

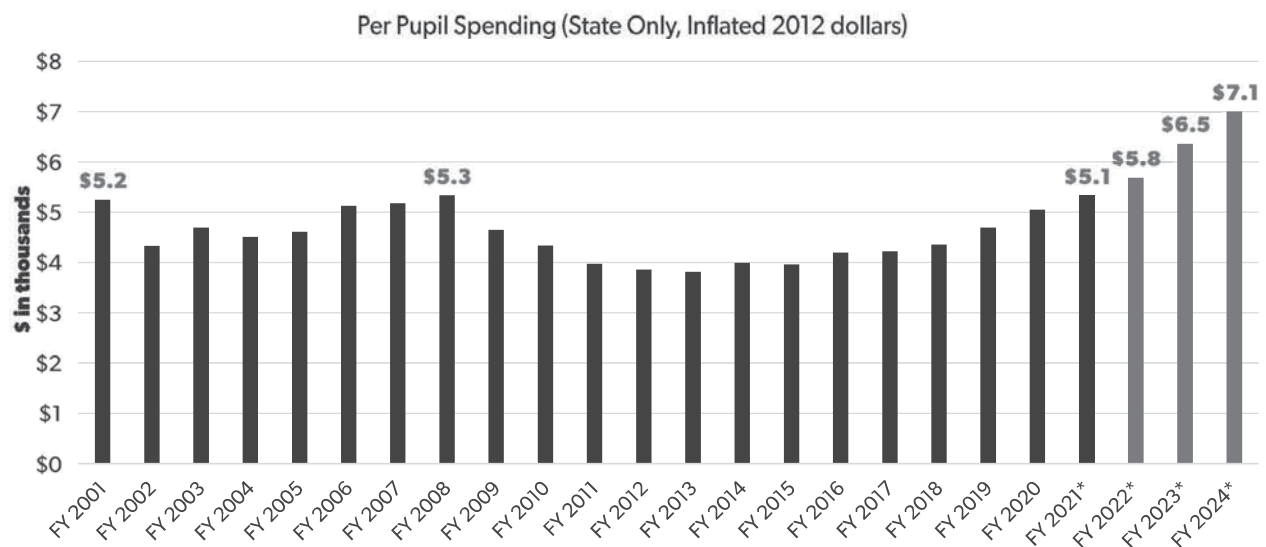
1. J.B.C All K-12 Funding History-2021

November 18, 2021

43

# Education

- This school year Arizona is estimated to be at an **all time high per pupil spending**, since the enactment of the school funding formula, after adjusting for inflation.



November 18, 2021

44

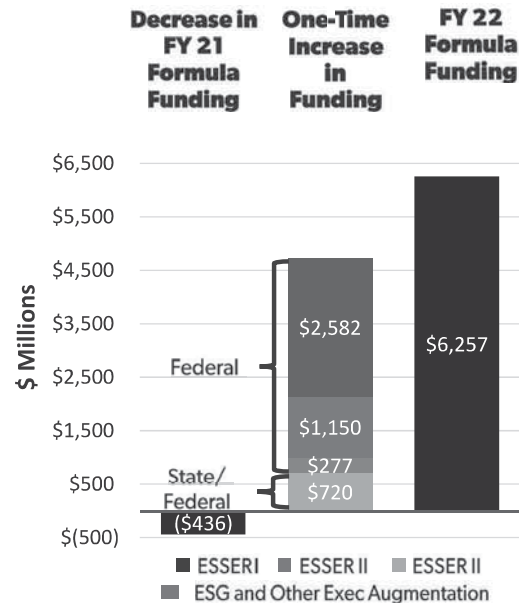
# Education

The FY 2022 Enacted Budget has **\$(436) M** of estimated K-12 formula savings in FY 2021 due to enrollment declines

In addition to state adjustments, there is **\$4.70 B** of strategic funding allocations to help students get back on track

- **\$720 M** from Enrollment Stabilization Grant (ESG) and Education Plus-Up
- **\$277 M** from Elementary and Secondary School Emergency Relief (ESSER I) Fund
- **\$1,150 M** from ESSER II Fund
- **\$2,582 M** from ESSER III Fund

This is in addition to the Enacted Budget projecting enrollment growth with **\$6.26 B** of formula funding



# Arizona Is Investing In Its Infrastructure

## • Revenue Growth

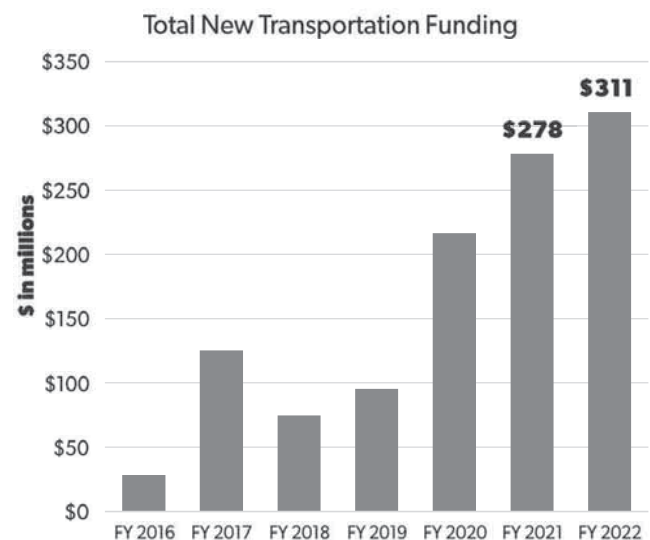
- Smart and Safe Arizona Act has led to **\$9M** in additional revenues to date

## • One-Time Preventive Maintenance

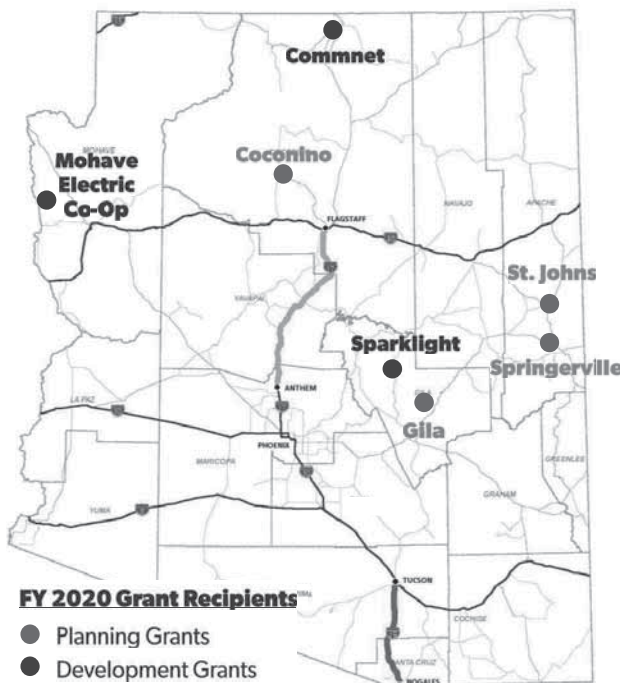
- **\$207** million in new funding to improve over 1000 highway lane-miles across the State

## • One-Time Transportation Funding

- **\$504** million in new funding on strategic transportation projects across the State



# Investing In Broadband



## I-19 & I-17 Broadband Corridors:

**\$100M** in ARPA funding for two broadband corridors to serve as the backbone in providing fast, affordable, and reliable internet to Arizonans

## Last Mile Broadband Grants:

**\$100M** in ARPA funding to provide entities grants for last mile development and planning

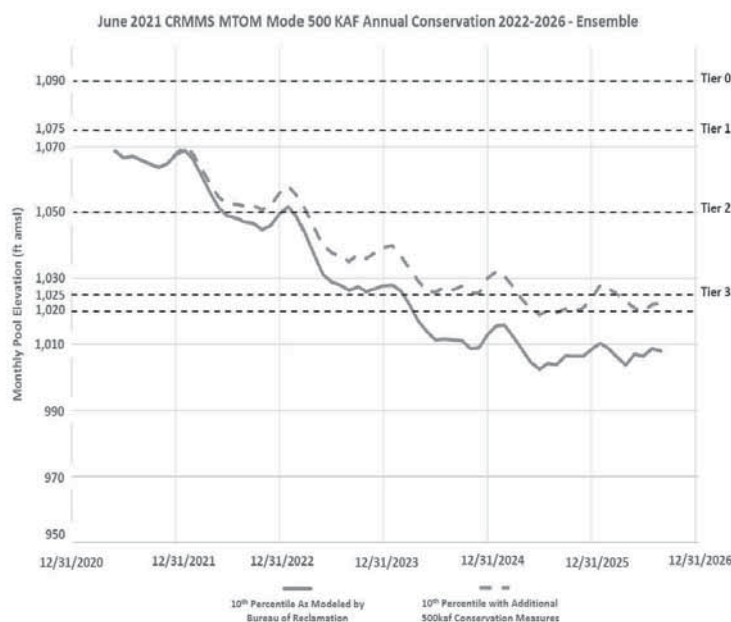
## State Park Broadband Initiative:

**\$5M** in ARPA funding to provide internet connections to visitors at multiple State Parks

November 18, 2021

47

# Arizona's Water Future



November 10, 2021

## Arizona Investments Since 2015

- **\$312 million** total state and federal dollars invested into water supplies, infrastructure, and safe drinking water since 2015
  - **\$150M** for general drought mitigation
  - **Up to \$44.2M** for AZ Water Bank conservation payments
  - **\$52M** for rural water supply development
  - **\$31M** for groundwater augmentation
  - **\$28.5M** to WIFA for wastewater treatment and water conservation
  - **\$4M** to provide adequate staff and equipment to the Department of Water Resources

November 12, 2021

64

# Key Takeaways

---

- **Arizona experienced tremendous fiscal and policy uncertainty over the past two years**
  - Passage of Prop 208 threatened fiscal policy flexibility and State economic competitiveness
  - The public health emergency put unprecedented strain on our State Government and economy
  - As recently as April 2020 the Finance Advisory Committee was projecting \$1.1 billion General Fund deficits by this year
- **Prudent fiscal and public health management has left Arizona in its strongest position ever**
  - 7+ years of structurally balanced budgets – including a \$900M cash and **\$2.7B** structural surplus this year
  - Comprehensive tax reform has protected Arizona's economic competitiveness without reducing K-12 (or other) spending
  - On track to have the highest General Fund cash reserves and lowest debt levels in recent State history

November 18, 2021

49

## Q&A

---

November 18, 2021

50





# National Tax Perspective

ATRA 2021 Outlook Conference  
November 18, 2021  
*Scottsdale, AZ*

Erica Kenney  
West Coast Tax Counsel  
Council On State Taxation  
[ekenney@cost.org](mailto:ekenney@cost.org)



## Agenda

- Pandemic Impact on State Revenues
- Select State Tax Legislation and Trends
  - Income & Franchise Taxes
  - Digital Services Taxes
  - Sales & Use Taxes
    - Marketplace Facilitators
- On the Horizon: Federal and International Activity Impacting State Taxes
- State and Local Business Tax Burden
- Discussion and Questions



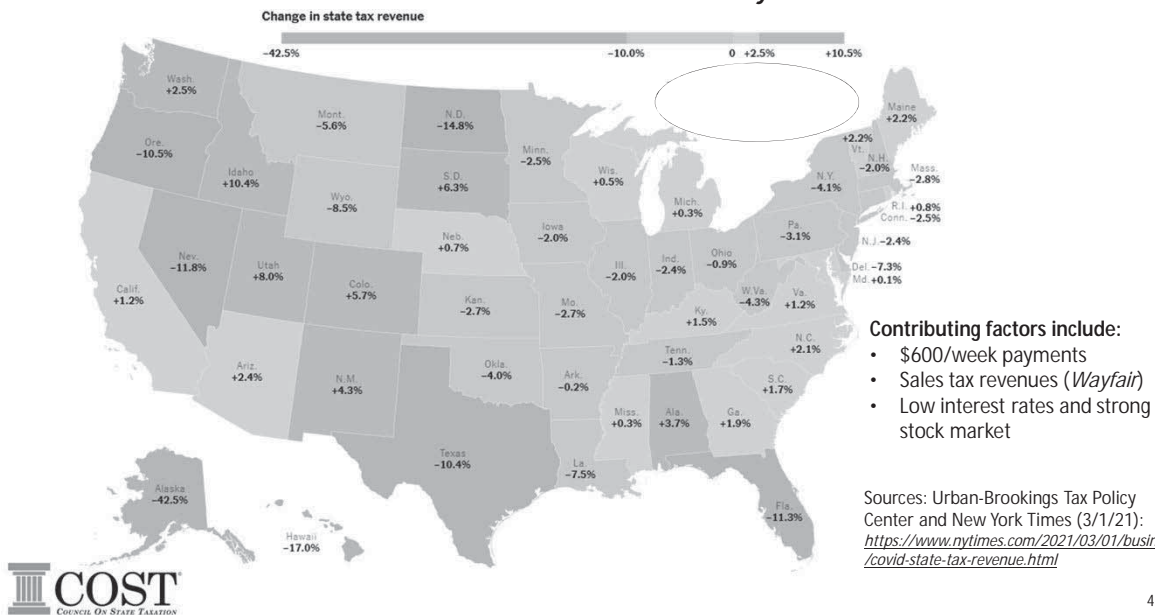


# Pandemic Impact on State Revenues

3



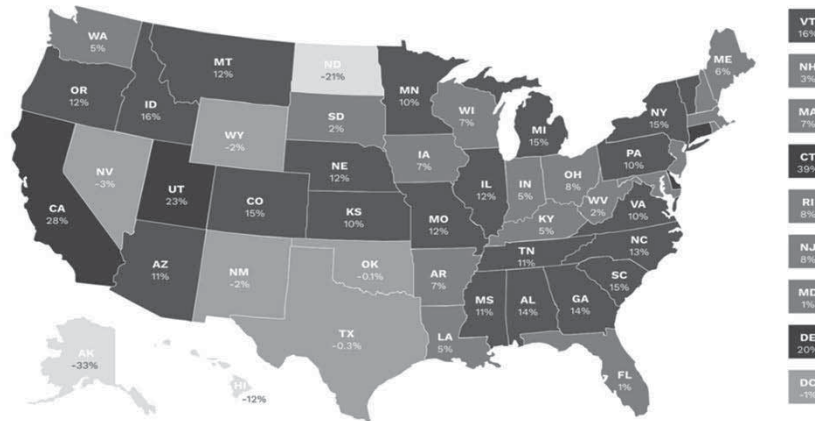
Change in Tax Revenue During "Pandemic Period," April-December 2020 Compared with April-December 2019:  
*Overall state revenues were down just 1.8%*



4

### How Did State Revenue Compare During the First Three Quarters of FYs 20 and 21?

-10% or worse    -5%    5%    10%    +20%



Source: MultiState. Data from Census Bureau (as of June 24, 2021).



5



## Federal Stimulus and Relief Spending During the COVID-19 Pandemic

- Federal Government pandemic-related stimulus and relief spending totaled about \$6 trillion in 2020 and 2021 resulting in the two highest years of federal deficits since World War II
- The key federal stimulus and relief spending programs included:
  - The Coronavirus Aid, Relief, and Economic Security (CARES) Act (April 2020)
  - The Response and Relief Act (December 2020)
  - The American Rescue Plan Act (March 2021)
- State and Local Governments benefited from many provisions in the federal legislation, particularly from the \$350 billion in state and local aid provided in the American Rescue Plan Act

6





## Select Legislation and Trends

7



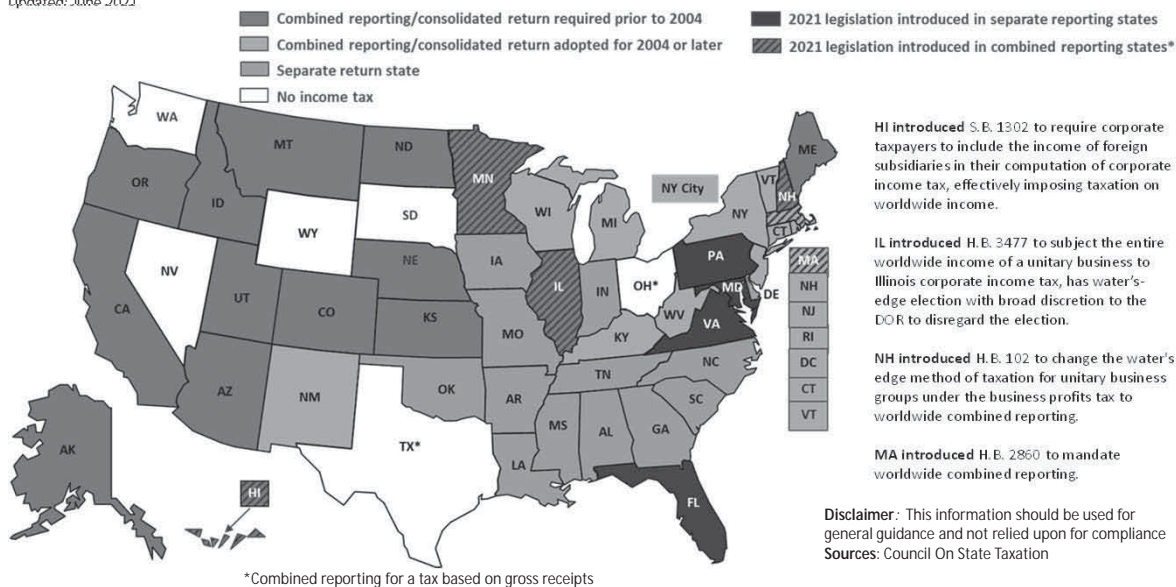
## Income & Franchise Taxes



# Combined Reporting Adoption and 2021 Proposals



Updated: June 2021



## Mandatory Unitary Combined Reporting

### Enacted Legislation:

- **Colorado H.B. 1311**
  - Tax haven "list": presumptive tax avoidance
  - *Joyce* method to *Finnigan* method
- **Virginia H.B. 1800**
  - Requires corporations that are members of a "unitary business" to file an informational report by July 1, 2021
  - HJR 563 (2021 Special Session 1) directs the Division of Legislative Services and the Department of Taxation to establish a work group to study the administrative feasibility and the projected impact on Virginia's tax revenue of adopting mandatory unitary combined reporting
  - The group must submit its findings to the Chairmen of the House Committee on Finance and the Senate Committee on Finance and Appropriations by November 1, 2021
- **Legislation Introduced But Not Enacted:**
- Mandatory Unitary Combined Reporting: **Florida** H.B. 999, **Maryland** H.B. 172, S.B. 123, S.B. 511, **Virginia** S.B. 1353, HJR 563, **Pennsylvania** H.B. 1222
- Mandatory Worldwide Combined Reporting: **New Hampshire** H.B. 102, **Hawaii** S.B. 1302, **Massachusetts** H.B. 2860,
- "Backdoor" Worldwide Combined Reporting: **Illinois** H.B. 3477, S.B. 2126, **Minnesota** H.F. 991, H.F. 2114, H.F. 2228
- Expansion of taxation of foreign source income: **California** A.B. 71

10





## Other Trends: Select 2021 Enacted Income Tax Legislation

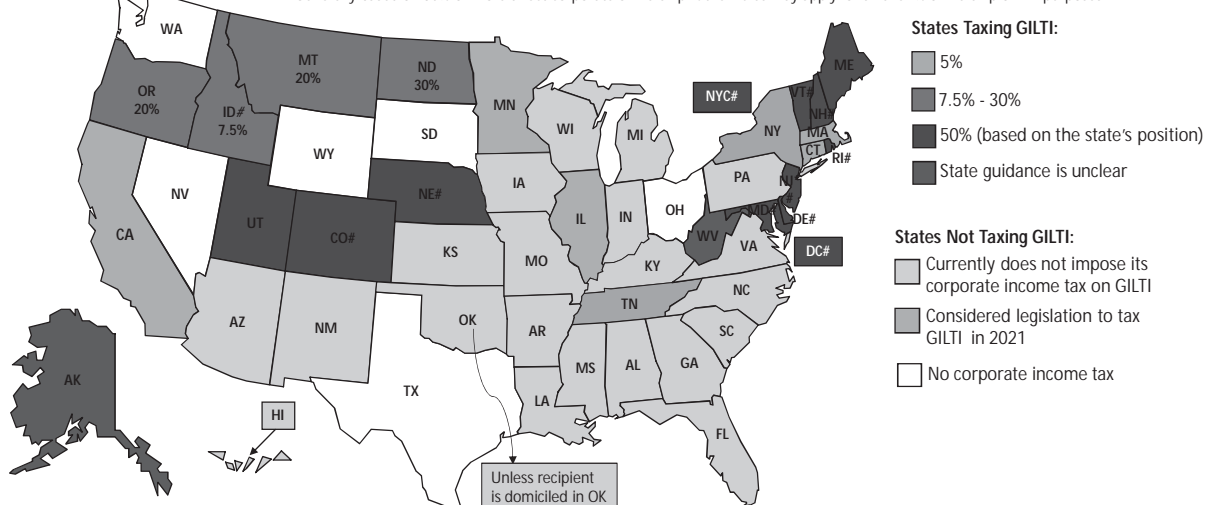
- **Rate Changes:**
  - **Rate Reductions:** Idaho, Louisiana, Nebraska, New Hampshire, Oklahoma
  - **Rate Increases:** New York
- **SALT Cap "Workarounds":** Alabama, Arizona, Arkansas, California, Colorado, Georgia, Idaho, Illinois, Massachusetts, Minnesota, New York, Oregon, South Carolina
- **Federal Conformity:**
  - **Alabama H.B. 170:** Decouples Alabama from IRC § 951A (GILTI) and remove Alabama's throwback rule. The bill also changes the apportionment factor for most corporate income taxpayers from a three-factor apportionment formula with a double-weighted sales factor to a single sales factor formula
  - **Kansas S.B. 50:** Beginning tax year 2021, decouples from GILTI and 163(j), eliminates the 10-year NOL carryforward cap for tax year 2018 or later
  - **Illinois S.B. 2017:** Freezes the corporate franchise tax phaseout; imposes an annual \$100,000 net operating loss cap for any taxable year ending on or after December 31, 2021, and prior to December 31, 2024; rolls back the Tax Cut and Jobs Act 100 percent accelerated depreciation deduction; and aligns the domestic and foreign-source dividend deduction
  - **Iowa S.F. 619:** Decouples the State from the IRC Sec. 163(j) interest expense limitations, effective retroactively to January 1, 2021, for tax years beginning on or after that date. Couples Iowa with federal bonus depreciation for qualified equipment and other capital assets purchased on and after January 1, 2021
  - **Maine LD 220/HP 155:** The bill contains provisions dealing with IRC conformity (Part B); GILTI (Part U, Part EE); the credit for income tax paid to other taxing jurisdictions (Part I); IRC Sec. 163(j) (Part E); and net operating loss (Part D) among others
  - **Utah H.B. 39:** Amends the definition of "unadjusted income" under Utah Code Ann. § 59-7-101 to mean federal taxable income as determined on a separate return basis before intercompany eliminations as determined by the IRC, before the net operating loss deduction and special deductions.

11



## GILTI: State Corporate Income Tax Conformity in 2021

Generally based on 80% or more direct corporate ownership. Other rules may apply for smaller % ownership or PIT purposes.



12

# Digital Services Taxes



## Digital Services Tax: Overview

- Digital economy has led to large revenue base erosion for states and localities
  - Digital goods and services are often not captured by state sales tax
- Attempts to recapture lost revenue in the form of sales tax base expansion or gross receipts taxes
- States attempting to tax digital services:
  - New taxes on the sale of digital advertising services
  - New taxes on the collection/sale of personal information or user data
  - Expanding the existing sales tax base to include sale of digital advertising services and/or personal information



## Maryland: H.B. 732 (2020) and S.B. 787 (2021) – Enacted

### New Digital Advertising Gross Revenues Tax

- Tax imposed on a person's annual gross revenues derived from digital advertising services in Maryland
- Tax imposed at rates of 2.5% to 10% depending on annual gross revenues.
- Additional 2021 amendments
  - Excludes digital interfaces owned, or operated by, or operated on behalf of, a broadcast entity or news media entity; and
  - Prohibit a person from directly passing the cost of the tax to a customer by means of a separate fee, surcharge, or line item
  - Moves the state date to tax year 2022
- Litigation pending in both Maryland court and federal district court
- Draft proposed regulations released in Sept. 2021

### "Things Not Worth Doing Are Especially Not Worth Doing Poorly"

- Constitutional and federal law challenges (Internet Tax Freedom Act non-discrimination provisions)
- Issues with the underlying tax policy

15



## Maryland Digital Advertising Services Tax Litigation

### *U.S. Chamber of Commerce et al. v. Franchot*

- February 18, 2021 complaint filed by four trade associations (U.S. Chamber of Commerce, Internet Association, NetChoice and Computer & Communications Industry Association) in Maryland U.S. District Court
- Seeking declaratory judgment and permanent injunctive relief

### *Comcast of California / Maryland / Pennsylvania / Virginia / West Virginia, LLC et al. v. Comptroller*

- April 15, 2021 complaint filed by taxpayers in Maryland Circuit Court for Anne Arundel County seeking to declare that the digital advertising gross revenues tax is unconstitutional on its face
- Seeking declaratory judgment

16





## Sales & Use Taxes



## States Enactment of Taxes on Digital Products

- States are continuing to look at taxing the “new” digital economy where products are only transferred electronically (no physical download)
- Sellers’ platforms differ - is a level playfield (*i.e.*, neutrality) possible?
  - Full price to consumer (*e.g.*, Netflix)
  - Paid by advertisers (*e.g.*, Facebook)
  - Hybrids (*e.g.*, YouTube & Spotify)
- Prof. Bill Fox at an NCSL conference, raised the question of how to tax these services:
  - Impose tax on the non-monetized value of the social media services
    - *E.g.*, head tax on number of customers located in a state
  - Impose sales tax on all social media companies’ revenue
    - *E.g.*, tax on revenue based on revenue from customers in a state

Source: Prof. Fox presentation Sept. 28, 2021 to the NCSL Fiscal Leaders Seminar

19



## States Enactment of Taxes on Digital Products

- Issues with State Taxes on Digital Products
  - Definitions are critical
    - Need legislation and not administrative positions
    - Imposition language needs to be clear
  - Sourcing can be a problem
    - Digital products delivered electronically can technically be sold without a seller directly knowing a “delivery” or “billing” address
    - Default rule in many states with no delivery or billing address (especially SSUTA states) is the origin (*i.e.*, the seller’s) location – which for sellers located in a non-sales tax state or foreign country equates to no state imposing the tax on the sale (use tax may apply to the consumer)
    - Can states require some type of address from a customer and/or does that also create privacy issues?
  - B2C imposition versus B2B
    - Taxation on business inputs creates pyramiding of the tax

20





## States Enactment of Taxes on Digital Products and Services

- **What is a 'digital product'?**
  - Narrow vs. broad definitions
- **Maryland** H.B. 932 **Enacted** 2/12/21 and effective 3/14/21; Tax Tip #29, issued 3/11/21, revised June
  - A 'digital product' is a product that is obtained electronically by the buyer or delivered by means other than tangible storage media through the use of technology having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities
  - Under the Comptroller's expansive interpretation, many additional service providers—including those offering online video game services, software as a service (SaaS), and online courses, among other services—could be required to collect and remit sales tax
  - S.B. 787, enacted 5/30/21 and retroactive to 3/14/21, provides certain exclusions and amends 'custom' software services definition; revised Tax Tip issued 6/3/21
- **Colorado** H.B. 1312 "codifies the department of revenue rule that the definition of 'tangible personal property' includes 'digital goods'" (**Enacted** 6/23/21)
  - 'Digital good' means any item of TPP that is delivered or stored by digital means (example of 'computer files' stricken by amendment)
- Proposals in multiple other states (e.g., Georgia, Kansas, Nevada)
- Application to software and digital services

21



## Sales Taxes on Business-to-Business Transactions and Other Business Inputs

- State sales taxes are designed to tax household consumption
- True consumption taxes are least harmful to economic growth and capital investment
- Taxation of business inputs leads to harmful tax pyramiding
- Pyramiding creates inefficiencies and a lack of transparency
- On average, 42% of the tax base of state sales tax systems is levied on business inputs
- Most professional services are business to business transactions

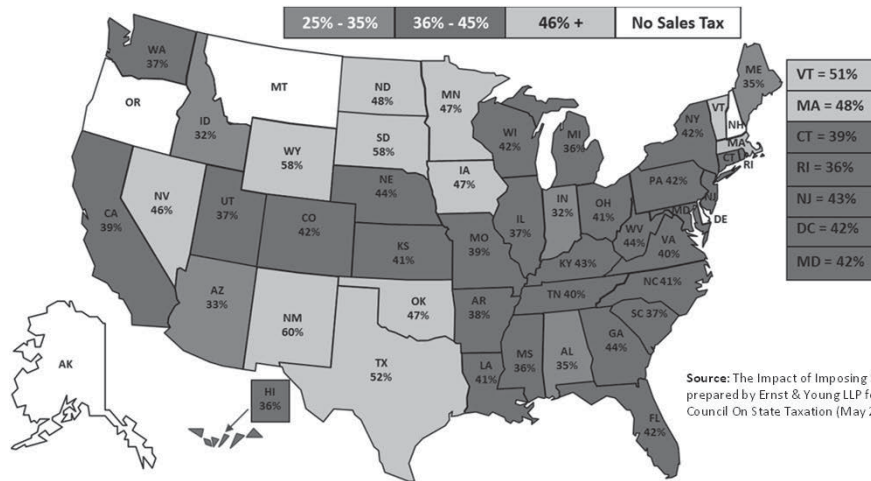
22



# Business Inputs Make up Between 32% and 60% of Total Sales Tax Collected in the U.S., with an Average of 42%



Business Inputs Share of Total Sales Tax Collected



Source: The Impact of Imposing Sales Taxes on Business Inputs, study prepared by Ernst & Young LLP for the State Tax Research Institute and the Council On State Taxation (May 2019)



## Legislative Proposals to Tax Business Inputs with Income Tax Reductions

### Ohio H.B. 110 - Enacted

- In contrast to other states, Ohio eliminated a tax on business inputs by eliminating its sales tax on employment services

### Legislation Not Enacted:

#### Iowa S.F. 149

- Eliminate Iowa's personal income tax 1/1/2023 by increasing State's sales/use tax rate from 6% to 11%
- Iowa's corporate income tax would remain in place

#### Mississippi H.B. 1439

- Increase sales tax rates and phase-out personal income tax
- Increase sales taxes on various business inputs

#### Nebraska EPIC Bill, L.B. 133

- Bill would Eliminate Property, Income, and Corporate income taxes starting 1/1/2024 (inheritance tax also eliminated)
- Sales tax technically eliminated and replaced with 10.64% broad-based consumption tax
- Exemptions for land, *property and services used for business purposes*, investments, education, and used property

#### West Virginia S.B. 600 and H.B. 2027

- Phase-in elimination of personal income tax with sales tax increase from 6.0 percent to 7.9 percent
- Expand the sales tax base to include professional services and repeal exemptions for internet advertising and electronic data processing
- Create a luxury tax and increase various severance tax rates

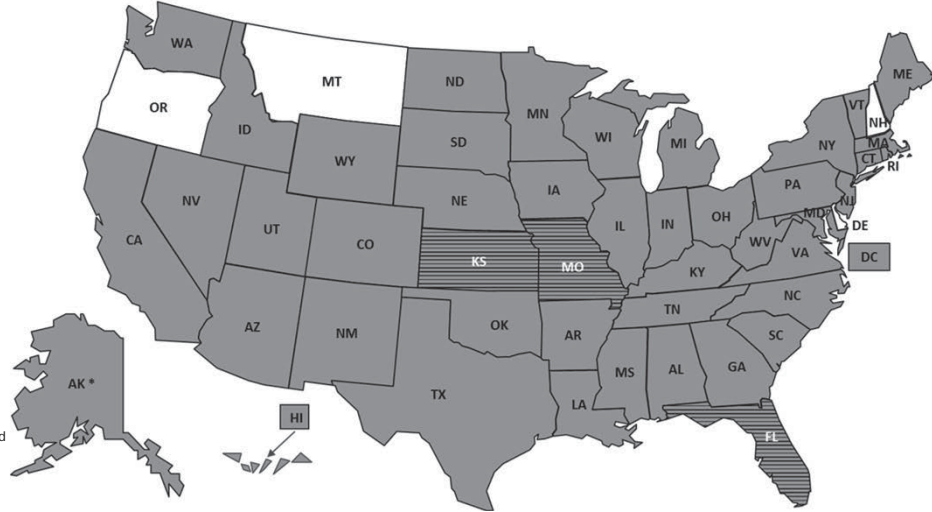


## State Sales Tax Adoption of Economic Nexus Threshold

■ States with economic nexus laws   ■ States that enacted this year   □ States with no sales tax

\* = Alaska has no state sales tax, based on Alaska Remote Seller Sales Tax Commission Uniform Code

**Disclaimer:** This information should be used for general guidance and not relied upon for compliance.  
**Source:** Council On State Taxation

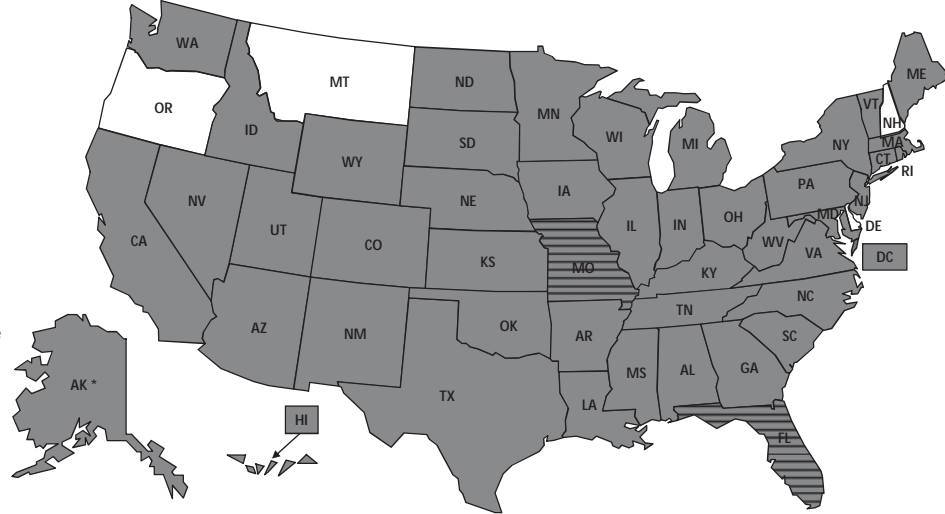


## Marketplace Facilitators

## State Adoption of Marketplace Facilitator Laws



■ States with marketplace facilitator laws ■ States that enacted this year □ States with no sales tax



\* = Alaska has no state sales tax, based on Alaska Remote Seller Sales Tax Commission Uniform Code

**Disclaimer:** This information should be used for general guidance and not relied upon for compliance.  
**Source:** Council On State Taxation



## On The Horizon: Federal and International Activity Impacting State Taxes

28





## The Acceleration of Federal Tax Reform 1986-2021

- **Tax Reform Act of 1986**
- **Tax Cuts and Jobs Act of 2017**
  - Shift from a worldwide/deferral system towards a territorial system, but also adds GILTI
  - CIT tax cuts and base broadening – e.g., interest expense limitation
- **The Coronavirus Aid, Relief, and Economic Security Act of 2020**
  - Part of \$6 trillion of federal pandemic relief and stimulus over a several year period
  - NOL limitation and carryback changes; Interest expense limitation changes
- **The American Rescue Plan Act of 2021**
  - Federal limitation of state tax reductions
- **The Made in America Tax Plan of 2021 (Proposed)**
  - \$2.3 trillion net CIT and PIT tax increase over 10 years (combined for both Biden proposals)
  - Raises CIT rate, overhauls GILTI, and establishes a minimum book tax
- **The American Families Plan of 2021 (Proposed)**
  - Tax increases on ordinary income and capital gains for high income households

29



Key Biden Administration 2021 Federal Tax Reform Proposals	House Ways and Means Bill	State Tax Implications
Raise CIT rate to 28%	Raise top CIT Rate to 26.5%	None
Raise GILTI rate to 21%. Expand GILTI tax base by eliminating QBAI deduction and adopting CbC	Raise GILTI tax rate to 16.56%. Expand GILTI tax base by reducing QBAI deduction to 5% and adopting CbC	Yes. Could expand the tax base and “effective” tax rate for some states that tax GILTI
Enact a 15% minimum tax on book income	No provision	None
Replace BEAT with SHIELD	Increase tax rate and tax base of BEAT	Yes. Possible conformity with SHIELD
Further limit interest expense deduction using a U.S.-to-worldwide ratio calculated based on financial statements	Further limit interest expense deduction for domestic co. that are part of international financial reporting group. Limit interest expense carryforward to five years.	Yes. Could further limit interest expense deductions for many states that conform to Sec. 163.
Eliminate FDII and replace it with a different investment incentive	Reduce FDII deduction from 37.5% to 21.875%	Yes. Could limit (or eliminate) FDII deduction for many states that conform to FDII
Raise top PIT rate to 39.6%	Same as Biden	None
Increase top capital gains rate to 39.6% for high income households	Increase top capital gains rate to 25% for high income households	None

30



## The OECD/G-20 Pillar One and Two Project

- The OECD/G-20 inclusive framework is one of the most ambitious international tax projects ever undertaken, with participation by 139 nations making up over 90% of the world's GDP
- **Pillar One** addresses issues relating to **digitalization**
  - **Key proposal:** partially applies 1/ economic presence, and 2/ market sourcing rules to large MNCs over 20 billion euros (about 100 MNCs)
  - New rules apply to profits over 10% of revenue and reallocate 20-30% to market countries
- **Pillar Two** addresses issues relating to **globalization**, focusing on profit shifting and low tax rate competition
  - **Key proposal:** a global minimum (top-up) tax imposed on each country's MNCs at a rate of at least 15%
- The Biden administration supports both pillars, with some key modifications.
- The Pillar One and Two proposals were endorsed in July 2021 by the G-7 nations, the G-20 nations, and 133 of the 139 members of the OECD's inclusive framework
- **Timeline** A more detailed plan is expected to receive approval this fall. Complex and interconnected single country legislation, multilateral agreements and changes to bilateral treaties are expected in 2022 and 2023

31



## The American Rescue Plan State Tax Cut Limitation Provision

*"A State or territory shall not use the funds provided under this section or transferred pursuant to section 603(c)(4) to either directly or indirectly offset a reduction in the net tax revenue of such State or territory resulting from a change in law, regulation, or administrative interpretation during the covered period that reduces any tax (by providing for a reduction in a rate, a rebate, a deduction, a credit, or otherwise) or delays the imposition of any tax or tax increase."*

- **May 10, The U.S. Treasury issued a Fact Sheet and Interim Final Rule addressing the states use of the federal funds and how it would address the limitation on states reducing any tax**
  - Congress did not want federal funds (est. \$195.3 billion for the state governments) to be used to pay for states to decrease their taxes (only applies to state and not local taxes)
  - Treasury will use fiscal year 2019 as the base year of net state tax revenue collected (inflation adjusted) to create a safe harbor for the calculation and conformity to IRC would not count as a reduction along with tax redeterminations
  - There is a one percent *de minimis* threshold that would not trigger recoupment
- **Litigation and federal legislation:**
  - Broad call for clarification from state associations, state attorneys general and taxpayer community – State Attorney General litigation
  - Ohio legal challenge – federal district court held provision was unconstitutionally too ambiguous under the Spending Clause
  - Federal legislation: S. 730 – Let States Cut Taxes Act, introduced March 11, 2021
  - H.R. 2189 – State Tax Freedom Act, introduced March 26, 2021

32







# State and Local Business Tax Burden

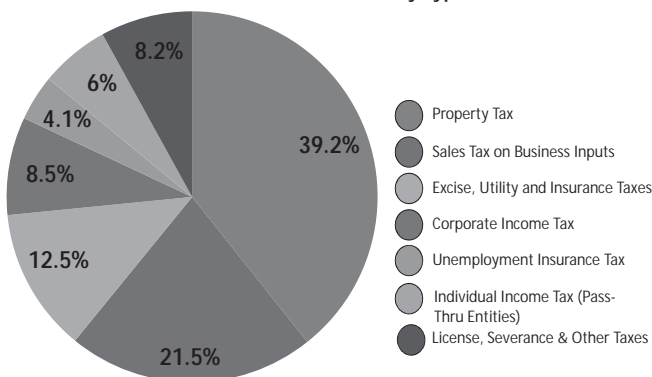
33



## FY 2020 State and Local Business Tax Burden Study



State and Local Business Taxes by Type, FY20



Source: *Total State and Local Business Taxes: State-by-State Estimates for Fiscal Year 2020*, study prepared by Ernst & Young LLP for the State Tax Research Institute and the Council On State Taxation (October 2021)

### How Much Do Businesses Pay?

- Businesses paid more than \$839 Billion in U.S. state and local taxes in FY20, an increase of 0.5% from FY19
- State business taxes decreased by 1.9% and local business taxes grew by 3.1%
- In FY20, business tax revenue accounted for 44.3% of all state and local tax revenue
- Remarkably, the business share of SALT nationally has been within approximately 1% of 44% since FY03

34

## FY 2020 State and Local Business Tax Burden Study

### State and Local Business Taxes, FY19-FY20

Revenue Source	FY20 Q1-Q3, % Change from Prior Year	FY20 Total % Change from FY19
Property	5.3%	3.8%
Individual	5.3%	-5.6%
Corporate	9.7%	-6.3%
Sales	5.6%	1.9%
Total	5.5%	0.5%

Source: *Total State and Local Business Taxes: State-by-State Estimates for Fiscal Year 2020*, study prepared by Ernst & Young LLP for the State Tax Research Institute and the Council On State Taxation (October 2021)

35

## FY 2020 State and Local Business Tax Burden Study

### Arizona State and Local Business Taxes, FY19-FY20

Revenue Source	FY 19 (\$ billions)	FY20 (\$ billions)
Property	5.1	5.0
Individual Income Tax on Business	0.5	0.4
Corporate	0.5	0.5
Sales	4.1	4.2
Excise	1.3	1.3
UI	0.5	0.4
License and other taxes	0.7	0.7
Total	12.7	12.6

Sources: *Total State and Local Business Taxes: State-by-State Estimates for Fiscal Year 2020*, study prepared by Ernst & Young LLP for the State Tax Research Institute and the Council On State Taxation (October 2021); *State-by-State Estimates for Fiscal Year 2019*, study prepared by Ernst & Young LLP for the State Tax Research Institute and the Council On State Taxation (October 2020)

36



## Discussion and Questions

37



Thank you!

38



## ARIZONA TAX RESEARCH ASSOCIATION

---



Kevin McCarthy, *ATRA President*

Jennifer Stielow, *ATRA Vice President*

*The taxpayer's watchdog for over 80 years*

## Update on Major Tax Issues

---



- Impact of the pandemic on state and local budgets and revenues
- Considerable uncertainty: What will the state budget and income tax code look like in early 2022?
- Update on impacts of ATRA reforms on property tax system
- School finance reform

*The taxpayer's watchdog for over 80 years*



## State & Local Budget Growth & Cash Balances

- Billions in federal payments into AZ since beginning of pandemic
- An estimated \$54 billion to individuals, businesses, and state & local governments

### State & Local Budget Growth

- State general fund up 18.4%, FY 2020-2022
- County budgets up 26%
- Community College budgets up 2%
- City budgets up 29%

### State & Local Cash Balances

- State cash balance ?
- County cash balances up 38% to \$3.6b
- Community College cash balances up 115% \$971m
- City cash balances up 56% to \$2.8b

*The taxpayer's watchdog for over 80 years*

## Sales, Income, and Property Tax 2-YR Growth

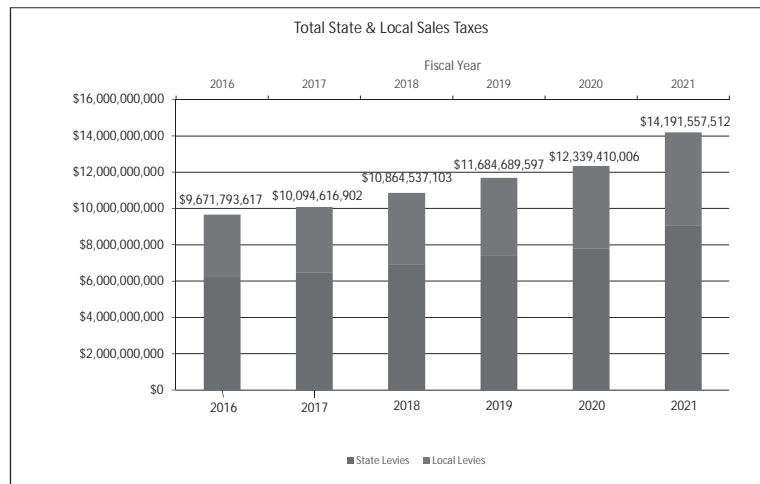


	FY 2019	FY 2021	% Growth
<b>Sales Taxes</b>	\$11,684,689,598	\$14,191,557,512	21.5%
<b>Property Taxes</b>	\$8,211,077,312	\$8,819,313,818	7.4%
<b>Income Taxes</b>	\$5,010,333,489	\$6,534,601,660	30.4%
<b>Totals</b>	<b>\$24,906,100,399</b>	<b>\$29,545,472,990</b>	<b>18.6%</b>

*The taxpayer's watchdog for over 80 years*



## Total State & Local Sales Taxes



Fiscal Year	State	Local	Total
2021	\$9,080,204,891	\$5,111,352,621	\$14,191,557,512
2020	\$7,820,211,649	\$4,519,198,357	\$12,339,410,006
2019	\$7,395,576,415	\$4,289,113,182	\$11,684,689,597
2018	\$6,904,474,633	\$3,960,062,470	\$10,864,537,103
2017	\$6,497,193,500	\$3,597,423,402	\$10,094,616,902
2016	\$6,226,596,835	\$3,445,196,782	\$9,671,793,617

FY 2020 to FY 2021: 15% Growth!

*The taxpayer's watchdog for over 80 years*



## Remote Seller/Marketplace Facilitator Revenues

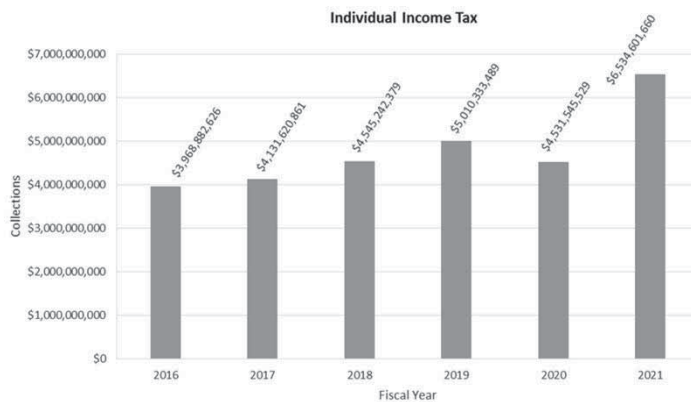
Fiscal Year	State Revenue Sharing						Total Revenue
	State GF	Education	County	City	City Taxes	County Taxes	
FY 2020 (8 mos.)	\$128,626,160	\$20,915,836	\$28,243,513	\$17,429,964	\$58,052,074	\$25,392,133	\$278,659,680
FY 2021	\$307,484,901	\$49,720,905	\$67,517,011	\$41,666,879	\$149,797,140	\$60,373,721	\$676,560,557
FY 2022 (4 mos.)	\$109,915,329	\$17,661,874	\$24,135,021	\$14,894,483	\$53,510,587	\$21,438,432	\$241,555,726
TOTALS	\$546,026,390	\$88,298,615	\$119,895,545	\$73,991,326	\$261,359,801	\$107,204,286	\$1,196,775,963

- \$1.2 Billion in total State & Local online remote sale revenues
- Total state GF revenues \$546 million vs. county and city revenues (including state revenue sharing) of \$562 million
- First four months of FY 2022 show trend to exceed FY 2021 revenues

*The taxpayer's watchdog for over 80 years*



## Individual Income Taxes



FY 2021	\$6,534,601,660
---------	-----------------

FY 2020	\$4,531,545,529
FY 2019	\$5,010,333,489
FY 2018	\$4,545,242,379
FY 2017	\$4,131,620,861
FY 2016	\$3,968,882,626

\$550M Income Tax Deferral from FY 2020 to FY 2021	
---	--

*The taxpayer's watchdog for over 80 years*



## State & Local Policy Choices?

- **State – Historic tax cut.** Package included individual income tax cuts & reductions to business property tax assessment ratio
- **Counties** – 9 of the 15 increased property taxes (primary taxes & secondary taxes to support countywide special taxing districts)
- **Colleges** – Half increased primary property taxes
- **Cities** – 21 of the 51 cities that levy a primary property tax increased taxes

*The taxpayer's watchdog for over 80 years*



## AZ Supremes Rule on Prop 208

- P208s exemption language from the constitutional K-12 AEL is unconstitutional
  - Facially unconstitutional: "a statute cannot circumvent or modify constitutional requirements"
  - Labeling P208 revenues 'grants' does not exempt the revenues; that exemption is for private grants, not public ones; further the context of exemption suggests "donative intent," not a tax
- Not severable, cites *Randolf* (1999) test
  - "we will uphold it unless doing so would produce a result so irrational or absurd as to compel the conclusion that an informed electorate would not have adopted one portion without the other."
  - The objective of the initiative was to increase spending in K-12. Impounding the revenues in an account unable to be spent renders the remaining statutes irrational.
- Remanded to determine whether the P208 revenues are likely to exceed the const. spending limit
  - 22: "[I]f the trial court finds that A.R.S. § 15-1281(D) will result in the accumulation of money that cannot be spent without violating the expenditure limit, it must declare Prop. 208 unconstitutional and enjoin its operation."
  - Prop 208 revenues are projected to far exceed the expenditure limit cap
  - May not be heard before January???

*The taxpayer's watchdog for over 80 years*



## Prop 208 continued

- Ruling clarifies P301 monies for K-12 no longer excludable from AEL
  - Constitutional exemption: "(v) Any revenues derived from an additional state transaction privilege tax rate increment for educational purposes that was authorized by the voters before January 1, 2001."
- Education tax no longer authorized by voters; reauthorized by Legislature with a 2/3 vote in 2019
- Ergo, Ed sales tax monies are now "local revenues" subject to AEL
- FY22 K-12 estimate for Ed Sales Tax: ~\$768m (80% to districts, \$614m )
- FY22 AEL: \$6.0b, reports K-12s will already be over their limit plus adding Ed Sales Tax puts K-12 well over AEL not counting P208 ~\$600m to districts
- K-12 AEL will be a major issue during 2022 legislative session

*The taxpayer's watchdog for over 80 years*





## Citizen Referendum on Tax Package (SB1828)

### SB1828 (Tax Omnibus) Refers Sections 13 & 15

New income tax brackets and rates depending on revenue triggers:

- 2.53% (0-\$27,272) and 2.75% (\$27,273+) for single filers
- Flat tax rate of 2.5%

*The taxpayer's watchdog for over 80 years*



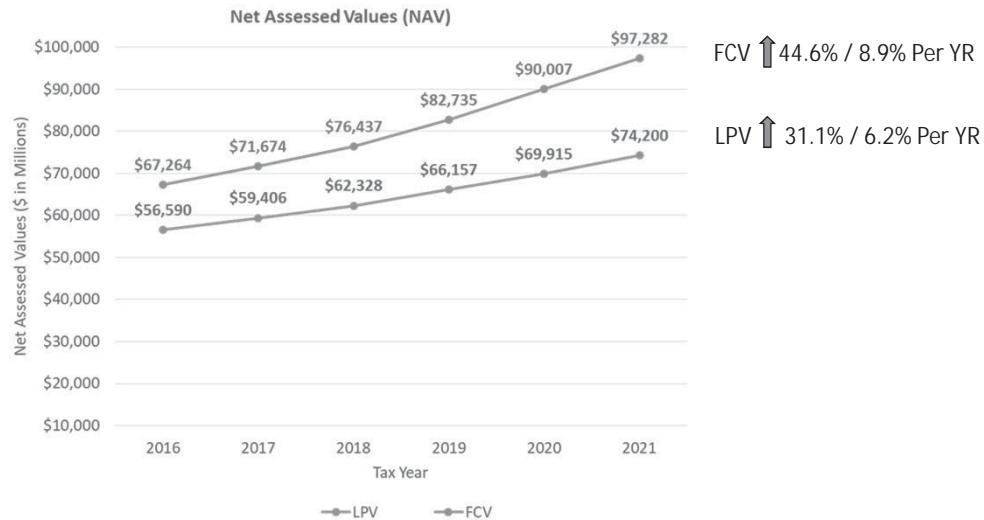
## Property Tax Update

- 5 Year Look back - How has system performed? Prop 117 continues to provide stability to AZ's property tax system
- Impact of ATRA reforms – Class 1 (business) Assessment Ratio reductions
- Foreign Trade Zones (FTZ) – Over 70% Tax Break... Indefinitely

*The taxpayer's watchdog for over 80 years*



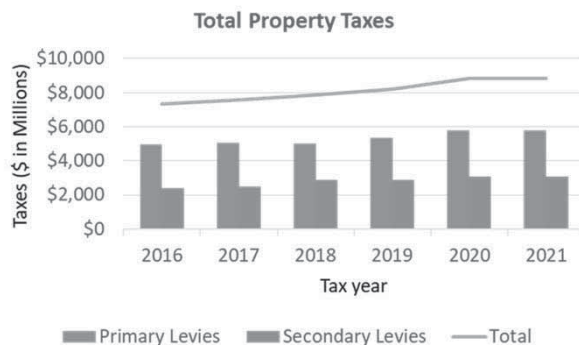
## FCV vs. LPV – 5 YR Change



*The taxpayer's watchdog for over 80 years*



## Total State & Local Property Taxes - 5 YR Change



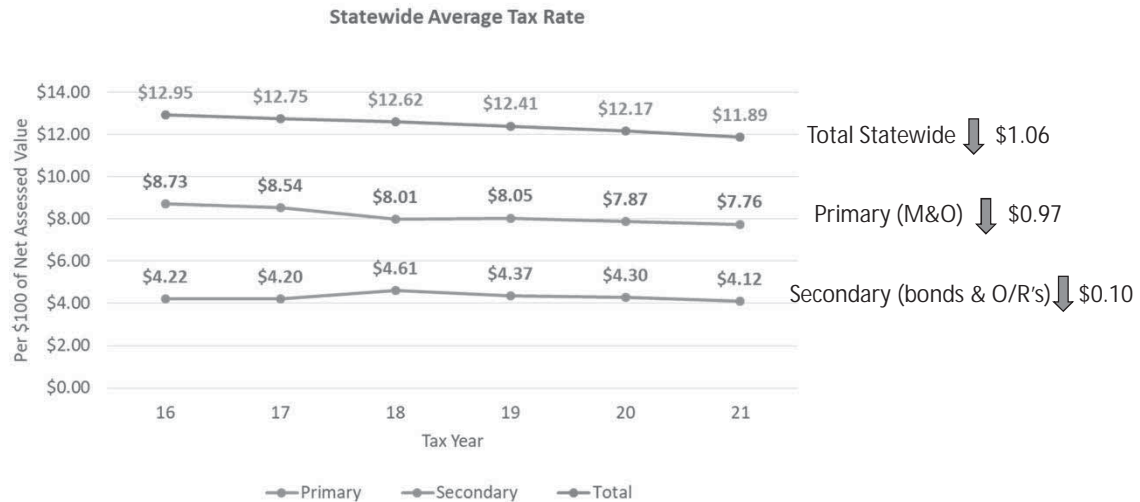
Tax Year	Primary	Secondary	Total
2021	\$5,760,593,434	\$3,058,720,384	\$8,819,313,818
2020	\$5,504,573,639	\$3,004,729,390	\$8,509,303,029
2019	\$5,323,167,423	\$2,887,909,889	\$8,211,077,312
2018	\$4,993,083,403	\$2,870,726,238	\$7,863,809,641
2017	\$5,077,107,680	\$2,498,947,880	\$7,576,055,560
2016	\$4,938,785,065	\$2,389,483,977	\$7,328,269,042

- Total Taxes ↑ 20% / 4% Per YR
- Primary Taxes ↑ 17% / 3.4% Per YR
- Secondary Taxes ↑ 28% / 4.5% Per YR

*The taxpayer's watchdog for over 80 years*



# Statewide Average Tax Rate – 5 YR Change



*The taxpayer's watchdog for over 80 years*

# TY 2005 vs. 2020 Effective Tax Rates (ETR)

## TY 2005 ETR's

Class	Assessment Ratio	Total Taxable Full Cash Value	Percent of Total	Total Yield	Percent of Total	Effective Rate
1	25%	77,639,438,613	20.99%	2,067,055,937	40.74%	2.66%
2	16%	24,871,825,014	6.73%	381,472,409	7.52%	1.53%
3	10%	230,354,442,559	62.29%	2,206,080,931	43.48%	0.96%
4	10%	33,300,215,237	9.00%	374,976,334	7.39%	1.13%
5	21%	1,354,696,047	0.37%	31,126,393	0.61%	2.30%
6	5%	2,267,257,439	0.61%	13,012,748	0.26%	0.57%
7	25%/1%	24,753,707	0.01%	440,071	0.01%	1.78%
8	10%/1%	10,413,991	0.00%	88,785	0.00%	0.85%
9	1%	15,731,377	0.00%	11,482	0.00%	0.07%
<b>Total</b>		<b>369,838,773,984</b>	<b>100.00%</b>	<b>5,074,265,089</b>	<b>100.00%</b>	<b>1.37%</b>

## TY 2020 ETR's

Class	Assessment Ratio	Total Taxable Full Cash Value	Percent of Total	Total Yield	Percent of Total	Effective Rate
1	18%	157,474,354,302	20.27%	2,774,678,108	34.30%	1.76%
2	15%	28,634,763,379	3.69%	340,231,943	4.21%	1.19%
3	10%	384,724,534,914	49.51%	3,194,863,898	39.49%	0.83%
4	10%	196,455,693,981	25.28%	1,706,415,967	21.09%	0.87%
5	14%	2,155,280,389	0.28%	33,760,595	0.42%	1.57%
6	5%	7,069,367,584	0.91%	37,651,269	0.47%	0.53%
7	18%/1%	63,669,468	0.01%	762,850	0.01%	1.20%
8	10%/1%	22,702,792	0.00%	233,272	0.00%	1.03%
9	1%	424,713,434	0.05%	1,792,740	0.02%	0.42%
<b>Total</b>		<b>777,025,080,244</b>	<b>100.00%</b>	<b>8,090,390,643</b>	<b>100.00%</b>	<b>1.04%</b>

- ETR Improved dramatically from reductions in Class 1 (business) A/R's from 25% to 18%
- TY 2005 ETR of 2.66% vs. TY 2020 ETR of 1.76%

*The taxpayer's watchdog for over 80 years*

## Effective Tax Rate (ETR) Improves with reduction to CI-1 (business) assessment ratio to 16%

Minnesota Study - Phoenix Average

Residential Property Taxes Payable 2020 \$150,000 Land and Building			
Rank	State	NET TAX	ETR
23	Arizona	\$1,822	1.215%
	U.S. Average	\$1,974	1.316%

Industrial Property Taxes Payable 2020 \$25,000,000 Land and Building \$12,500,000 Machinery and Equipment \$10,000,000 Inventories \$2,500,000 Fixtures			
Rank	State	NET TAX	ETR
8	Arizona	\$1,112,837	2.226%
	U.S. Average	\$718,840	1.438%

Statewide Average Tax Rate: \$12.17 per \$100

Residential Property Taxes Payable 2020 \$150,000 Land and Building			
Rank	State	NET TAX	ETR
42	Arizona	\$1,274	0.849%
	U.S. Average	\$1,974	1.316%

Industrial Property Taxes Payable 2020 \$25,000,000 Land and Building \$12,500,000 Machinery and Equipment \$10,000,000 Inventories \$2,500,000 Fixtures			
Rank	State	NET TAX	ETR
21	Arizona	\$815,214	1.630%
	U.S. Average	\$718,840	1.438%

Class 1 A/R = 16%

Industrial Property Taxes Payable 2020 \$25,000,000 Land and Building \$12,500,000 Machinery and Equipment \$10,000,000 Inventories \$2,500,000 Fixtures			
Rank	State	NET TAX	ETR
24	Arizona	\$724,635	1.449%
	U.S. Average	\$718,840	1.438%

*The taxpayer's watchdog for over 80 years*

## Targeted Tax Breaks – Foreign Trade Zones (FTZ)



- FTZ – Designated locations within or adjacent to U.S. Customs and Border Protection (CBP) ports of entry to encourage U.S. activity in competition with foreign companies
- Benefits: Duty exemption & deferral, Inverted tariff's, Logistics
- Lengthy application process: Degree & nature of foreign & domestic competition, effect on exports & imports, overall employment impacts, public benefits, etc. Retail only activity prohibited within zones
- State statute provides massive and indefinite property tax incentive to users:
  - Class 6 @ 5% (vs. Class 1 @ 18%) = **Over 70% tax break**
  - LPV diverted from Class 1 to Class 6 over last 15 years grew from \$1B to \$4.7B

*The taxpayer's watchdog for over 80 years*



# SCHOOL FINANCE REFORM

*The taxpayer's watchdog for over 80 years*



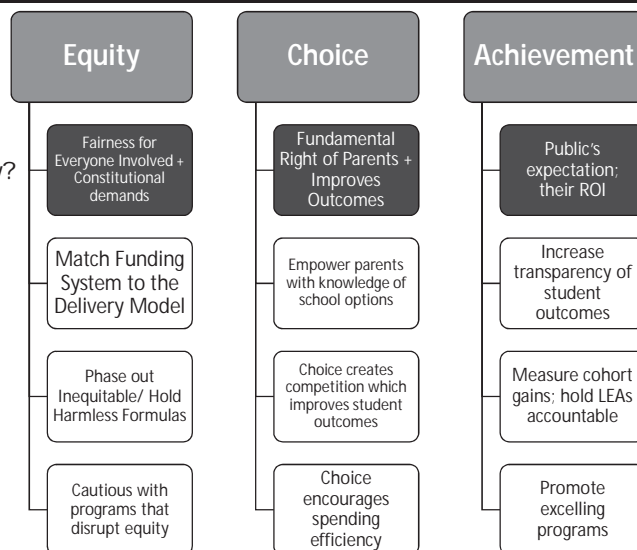
## Level Set: What's the Intent?

- Additional funding cannot be the only discussion
- Solutions should
  - Be in line with policy maxims
  - Be data driven
  - Reduce state's legal liability

Taxpayers should not agree to increased funding unless its paired with and consistent with policy maxims

Maxims

Why?



*The taxpayer's watchdog for over 80 years*





## Reform Goals: What's the Vision?

- Pursue funding formula changes to create greater equity
  - Fairness issue: kids should be worth the same in the same system
  - Funding should follow student as much as possible
  - Only fair under an open enrollment system
  - Undermines the 'Our outcomes are bad because of funding' argument
- Make system less ripe for litigation
  - System must provide adequate capital facilities by law
    - Adequacy lawsuits far less successful; tough to prove
  - Funding must be equitable
    - Courts ruled charters and districts may be funded differently
    - State most liable in an equity lawsuit between districts

*The taxpayer's watchdog for over 80 years*



## Statewide Formula

- Problem:
  - Lowest funded LEAs are ~35 districts w/out nonformula \$, bonds, overrides
  - Without a secondary, they usually have the lowest prop taxes
- Policy Idea: Allow districts with no secondary tax switch to Charter Formula
  - Cost: ~\$13m to State GF (Assuming 13 switch, \$1200 per pupil addition on average)
  - Offset? Additional rate on top of the QTR (\$0.35 per K-8, 9-12) = \$11.7M
  - Catch: These districts could not seek local tax options or nonformula \$\$
  - Winners: Rural AZ, ie: Somerton, Chino, Camp Verde, Santa Cruz, Res schools, Globe, Page
- 2<sup>nd</sup> Phase? Allow districts w/ expiring bonds & no overrides to "switch"
  - Why? Most Districts w/ low debt service have spent bond proceeds already; in a phase down
  - Cost: \$85m to State GF (includes 1<sup>st</sup> phase); Prop Tax offset rate= \$39m
  - Many districts w/ 1 or small override would likely switch: additional \$107m cost

*The taxpayer's watchdog for over 80 years*



## Statewide Formula: continued

- Benefits:
  - Improved equity while avoiding the \$1.3b+ cost to put all districts on Charter Add'l Assistance
  - More LEAs on a "statewide formula" but on a graduated plan & pace
  - Predictability for local taxpayers, board retains local control: they choose...
  - The \$0.7 rate will be netted out with decreases in nonformula tax rates, sometimes a wash
- Issues:
  - Districts may want to keep Adjacent Ways and SFB access
  - Notice & time for State to prepare for those who "switched"; what about switching back?
  - Voter approval required to "switch" and increase local taxes
- Sunnyside Example:
  - 15K students, expiring bond program, M&O override rate is \$3.50 per \$100; fails each time
  - "Statewide formula" = \$19m additional funding, \$0.7 rate local offset = \$3.6m

*The taxpayer's watchdog for over 80 years*



## Transportation Reform

- Issue: Districts who have contracted get more per-pupil \$ than others
- Local "hold harmless" tax
- As districts contract in size or drive fewer miles, the TRCL-TSL delta (& the tax levy) grows
  - FY09: \$60m
  - FY14: \$75m
  - FY20: \$90m
  - FY22: \$178m
- Un-equalized; monies levied outside the RCL
- Paid 100% by local property taxpayers

*The taxpayer's watchdog for over 80 years*



## Transportation Reform

- Districts want acknowledgement that many costs are fixed
- Taxpayers want a more fair system
- Policy Ideas:
  - Phase out TRCL
  - Transition to a per pupil allotment
  - Eliminate the bureaucracy and incentive of route miles
- Cost: Completely up to policymakers (no standard)

*The taxpayer's watchdog for over 80 years*



## FY 2020 TRCL – TSL Levies & Tax Rates

### FY 2020 TRCL - TSL Levies

	TRCL - TSL Levy	% Eq Base	TRCL - TSL Tax Rate	Total Primary Tax Rate	District's QTR	Amount Primary Rate Exceeds QTR
<b>Top 3 Districts w/ Highest TRCL - TSL Levies:</b>						
Tucson Unified	\$4,312,130	1.6%	\$ 0.13	\$5.82	\$3.79	\$2.03
Scottsdale Unified	\$3,667,537	2.7%	\$ 0.07	\$2.59	\$2.39	\$0.21
Mesa Unified	\$3,659,412	0.9%	\$ 0.11	\$4.20	\$3.79	\$0.41

### FY 2020 TRCL - TSL Tax Rates

	TRCL - TSL Levy	% Eq Base	TRCL - TSL Tax Rate	Total Primary Tax Rate	District's QTR	Amount Primary Rate Exceeds QTR
<b>Top 3 Districts w/ Highest TRCL - TSL Tax Rates:</b>						
Redington Elementary	\$62,997	153.2%	\$4.46	\$7.37	\$2.91	\$4.46
Santa Cruz Elementary	\$433,302	21.7%	\$4.14	\$7.44	\$3.79	\$3.65
Vernon Elementary	\$472,160	41.0%	\$2.90	\$6.33	\$2.97	\$3.36

*The taxpayer's watchdog for over 80 years*



## Adjacent Ways Reform

- Issue: Districts with property value use AW to subsidize bonds
- Local property tax designed for public right-of-way projects
- Un-equalized; monies levied outside the RCL
- Paid 100% by local property taxpayers
- Districts with low-value have limited access
- Used aggressively in new construction jobs to add \$ to project
- FY22: \$37m levied statewide

*The taxpayer's watchdog for over 80 years*



## Adjacent Ways Reform

- AW may not be used:
  - in combination with construction of improvements unless voter approved
  - in combination with SFB NSF funds unless voter approved
- Voter Approval: similar to DAA override
  - District must advertise the total amount of AW levy by year and estimated tax rate in each, not to exceed 7 years
  - Approved AW levies must be expended as advertised to voters
  - Voter approval would remove SFB validation for usage
  - AW levies do not count towards debt cap, as they are pay-as-you-go
- Unapproved AW levies renamed Adjacent Ways Maintenance Fund (AWMF)
- AWMF may not exceed \$2 million in levy per year
- AWMF expenditures must be validated by SFB. Increase materiality threshold from \$50k to \$100k.
- Allow SFB BRG to fund certain AWMF activities such as emergency lane repaving? Equity issue

*The taxpayer's watchdog for over 80 years*



Questions?

**ARIZONA  
TAX RESEARCH  
ASSOCIATION**



1814 W. Washington Street  
Phoenix, Arizona 85007  
(602) 253-9121

[www.arizonatax.org](http://www.arizonatax.org)  
[atra@arizonatax.org](mailto:atra@arizonatax.org)

*The taxpayer's watchdog for over 80 years*





# Special Thanks To Our:

---

## Silver Sponsors



LUMEN®



SOUTHWEST GAS

---

## Bronze Sponsors

**Lewis Roca**  
ROTHGERBER CHRISTIE



**TEP**  
Tucson Electric Power



**FENNEMORE.**

