

ATRA

Legislative Review



2023

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Information without action is futile

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ATRA’s 2023 LEGISLATIVE REVIEW

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ATRA is Arizona's only statewide taxpayer organization dedicated to protecting taxpayers and advocating for sound fiscal policy. A considerable amount of ATRA's work on behalf of taxpayers is done at the state capitol during the annual legislative session. Each year, through its legislative program adopted by the Board of Directors, ATRA advocates for tax and fiscal policies to improve Arizona's public finance system.

The ATRA Legislative Policy Committee meets every Friday during the legislative session to review the impact of all proposed legislation on taxpayers and Arizona's public finance system. ATRA coordinates its advocacy efforts in the Legislature on important tax legislation. Through testimony in committees and dissemination of information to legislators, ATRA serves as the leading taxpayer advocate at the Legislature.

ATRA staff would like to thank the members of ATRA's Legislative Policy Committee and Chairwoman Rebecca Hudson-Nunez for their guidance and combined efforts during the 2023 legislative session. Special appreciation also goes out to members of ATRA's Tax Policy Committee whose knowledge, under the leadership of Chairman Bill Molina, has consistently proven to be indispensable to this organization's success during the legislative session and throughout the year.

During the First Regular Session of the 56th Legislature, 1,788 bills and resolutions were introduced. Of the 1,675 bills introduced, 348 passed but only 205 were signed into law and the remaining 143 vetoed. Thirty two of the 113 resolutions introduced were adopted by the Legislature. This document summarizes key legislation ATRA supported, opposed, and monitored.

Additionally, ATRA would like to thank ATRA board member Steve Trussell, Executive Director of Arizona Rock Products Association and the Arizona Mining Association, and his staff for not only continuing to host the Legislative Policy Committee meetings at their office, but for providing a hybrid virtual option for ATRA as well.

HIGHLIGHTS OF THE 2023 LEGISLATIVE SESSION

This document summarizes key legislation ATRA actively supported, opposed or monitored during the First Regular Session of Arizona's 56th Legislature. This year's legislative session lasted through July 31st, setting the General Effective date to October 30, 2023.

Most bills that passed the Legislature that were subsequently signed by the Governor were non-controversial. Bills that carried a fiscal impact and that were not negotiated with the budget failed to advance.

Only one bill on ATRA's Legislative Program became law and most of the bills ATRA opposed were unsuccessful.

The major legislative issues in which ATRA supported that ultimately became law included the following:

- Senator J.D. Mesnard successfully sponsored SB1172 on behalf of ATRA to limit the amount a fire district can request in General Obligation (G.O.) bonds from its voters to 120% of the district's debt capacity.
- ATRA supported legislation sponsored by Senator Borelli under SB1650 that expanded the powers, duties, and oversight of the Office of the Auditor General.
- ATRA supported the legislation allowing K-12 schools to exceed their aggregate expenditure limit (AEL) by \$1.4 billion in FY 2023.

ATRA successfully opposed an effort under HB2013 that would have allowed the Pinal County regional transportation authority to retain the transportation sales taxes that the court ultimately deemed illegal.

LEGISLATION LISTED BY BILL NUMBER

LEGEND FOR ATRA'S POSITION:

S = Supported M = Monitored O = Opposed

BILL NUMBER, SHORT TITLE, AND PRIMARY SPONSOR	POSITION	FINAL STATUS/CHAPTER #	PAGE
HB2003 corporate income tax; rates (Livingston)	M	Held in Senate Rules	9
HB2013 transportation tax; deposit; regional fund (Cook)	O	Held in House WM	8
HB2014 STOs; scholarships; corporate tax credits (Livingston)	M	Held in Senate Rules	9
HB2025 community colleges; expenditure limitation (Dunn)	O	Held in House ED	9
HB2028 PSPRS; contribution rates (Livingston)	M	Chapter 102	9
HB2060 NOW: schools; requirements; revisions (Grantham)	M	Chapter 170	9
HB2064 property tax exemption; disability; qualifications (Carter)	M	Chapter 79	10
HB2145 dude ranches; historical markers (Dunn)	M	Chapter 171	10
HB2252 NOW: motor vehicle manufacturers; TPT; exemption (Wilmeth)	M	Vetoed	10
HB2501 dependent tax credit; additional amount (Gress)	M	Held in the House	10
HB2534 mortgaged property; tax statements; email (Carter)	S	Chapter 100	6
HB2623 NOW: unclaimed property; information; registration (Biasiucci)	M	Vetoed	10
HB2807 TPT; prime contracting; exemption; alterations (Carbone)	S	Held in the House	7
HB2809 public infrastructure improvements; reimbursement (Carbone)	M	Chapter 181	11
HCR2001 school district expenditures; authorization (Cook)	S	Transmitted to SOS	6
SB1013 colleges; universities; free speech zones (Kavanagh)	O	Chapter 184	8
SB1063 food; municipal tax; exemption (Borrelli)	M	Vetoed	11
SB1082 community colleges; expenditure limitation (Shope)	O	Not assigned	9
SB1102 transportation excise tax; Maricopa County (Carroll)	M	Chapter 203	11
SB1131 residential leases; municipal tax exemption (Petersen)	M	Chapter 204	12
SB1172 fire district bonding; limitation (Mesnard)	S	Chapter 19	6
SB1189 NOW: municipal tax code commission; continuation (Mesnard)	M	Chapter 192	12
SB1190 NOW: department of revenue; administration (Mesnard)	M	Chapter 7	13
SB1230 tax exemptions; affidavit (Mesnard)	M	Chapter 14	13
SB1260 small businesses; income tax; rate (Mesnard)	S	Chapter 67	6
SB1263 NOW: property tax; revisions (Mesnard)	S	Held in House WM	7
SB1276 assessed valuation; class one property (Mesnard)	S	Held in House Rules	8
SB1281 NOW: income tax rebate (Shamp)	M	Held in House Rules	13
SB1400 NOW: community colleges; noncredit workforce training (Wadsack)	M	Chapter 198	13
SB1416 county excise tax; rate reduction (Wadsack)	M	Held in TAT	13
SB1495 K-12; school funding; revisions (Bennett)	S	Held in House ED	8
SB1577 income tax rate; reduction; surplus (Mesnard)	M	Failed House Third Read	14
SB1650 auditor general; duties; access (Borrelli)	S	Chapter 40	6
SB1717 dual enrollment; revisions; appropriations (Kaiser)	M	Held in House Rules	14
SB1734 taxation; 2023-2024 (Kavanagh)	M	Chapter 147	14

PASSED LEGISLATION ATRA SUPPORTED

HB2534 mortgaged property; tax statements; email (Carter)

Chapter 100

HB2534 eliminates the requirement for county treasurers to mail property tax statements to mortgagors if the mortgagor requests the statement be emailed instead. However, upon a change in ownership, the county treasurer is required to mail the tax statements to the property address until the new mortgagor requests to receive the statement via email.

HCR2001 school district expenditures; authorization (Cook)

Transmitted to SOS

HCR2001 authorizes Arizona school districts to exceed the aggregate expenditure limitation (AEL) by \$1.4 billion in FY 2023. The AEL was created by Prop 109 in 1980 to limit school district expenditures to an amount determined by the Economic Estimates Commission (EEC) and the State Board of Education (SBE). If the local revenues of a school district exceed the AEL, the Legislature must approve the expenditures by March 1 with a two-thirds approval in the Legislature. If the Legislature does not authorize the expenditures, then the SBE must inform each school district of the amount they must reduce their expenditures. For FY 2023, the EEC determined the AEL to be \$6.4 billion and the Arizona Department of Education (ADE) calculated that school districts will exceed the AEL by \$1.4 billion.

SB1172 fire district bonding; limitation (Mesnard)

Chapter 19

State statute limits the amount of general obligation (G.O.) debt fire districts (FD) may issue to 6% of the District's net assessed value. However, there is no limitation on how much G.O. debt districts may *request* from voters. ATRA advocated for this measure in response to a recent election in Crown King FD that asked its voters to approve G.O. bonds in an amount that was five times the District's debt limit. Voters approved the bond question, but due to the creative way in which the bonds were structured, the District's property tax rate more than tripled. As amended in the Senate, SB1172 limits the amount a FD may request in G.O. debt to 120% of the district's debt capacity (debt limit, less outstanding debt). The bill also expands the information that must be provided in the bond election order, including the minimum number of years the bonds may run, the current outstanding G.O. debt, and the statutory debt limitation of the District. *See ATRA position paper in Appendix.*

SB1260 small businesses; income tax; rate (Mesnard)

Chapter 67

During the 2021 session, legislation was enacted to allow small businesses to pay at the entity level in order to be taxed at the same rate as all other individual income taxpayers. This legislation was in response to Prop 208, which at the time, would have implemented a 3.5% surcharge on small businesses that file individual income tax returns. The original legislation phased the tax rate down to 2.5% beginning in tax year 2025, but since Prop 208 was struck down by the courts, SB1260 simply accelerates the tax rate to 2.5% beginning in tax year 2023.

SB1650 auditor general; duties; access (Borrelli)

Chapter 40

SB1650 makes the following enhancements to the statutes that govern the powers and duties of the Office of the Auditor General (OAG). Requires an audit of a county transportation excise tax occur every fifth year instead of every tenth year. Any legislative measure that requires the OAG to perform a special audit, the Joint Legislative Budget Committee (JLBC) staff must

notify all members of the Legislature as soon as practicable of the cost to conduct the audit. Requires all state and local government agencies, boards, and commissions to provide reasonable space and make records available for the OAG to carry out its duties. Makes the penalties for counties, community college districts, and school districts the same as all other entities who knowingly obstruct or mislead the OAG in the execution of its official duties to a class 2 misdemeanor (instead of a class 5 felony) and requires the attorney general to supervise the prosecution of all offenders. Requires school districts to submit a status report regarding implementation of OAG performance audit recommendations upon request of the OAG and within two years following the audit. Adds the county treasurer and recipients of a county transportation excise tax to the list of entities that must cooperate with and provide necessary information to the OAG. Requires the OAG to conduct annual (rather than biennial) financial and compliance audits of financial transactions and accounts kept by state agencies subject to federal single audit requirements. For a county or community college district that is required to comply with the federal single audit requirements, audits must include compliance audits of financial transactions and applicable accounts, be conducted in accordance with generally accepted governmental auditing standards and include tests of the accounting records and other auditing procedures as may be considered necessary under the circumstances.

FAILED LEGISLATION ATRA SUPPORTED

HB2807 TPT; prime contracting; exemption; alterations (Carbone) Held in the House
HB2807 was yet another attempt by ATRA to simplify the taxation of MRRA (maintenance, repair, replacement, alteration) activities under Arizona's complex prime contracting system. HB2807 was identical to last year's effort that addressed only residential contracts and specified that a contract would be taxable under prime contracting only when square footage is added to an existing structure. All other contracts that do not expand the square footage of the home, such as remodels, would remain taxable under MRRA where the tax is paid on the materials at retail.

Once again, testimony by a representative from the Arizona League of Cities and Towns provided an inaccurate description of the current law, which was subsequently debunked in a memo by the Arizona Department of Revenue (ADOR) to the bill sponsor. The erroneous testimony provided by the League is cause for great concern, not only because some lawmakers relied on that testimony but more disturbing is the possibility that city auditors may be taking a position contrary to the law and in conflict with DOR. HB2807 did not have the votes to pass the House despite industry and taxpayer support. *See ATRA position paper and DOR memo in Appendix*

SB1263 business personal property; tax exemption (Mesnard) Held in House WM
SB1263 would have eliminated the locally assessed business personal property (BPP) tax, effective beginning in tax year 2024. For decades, ATRA has been a strong advocate for reducing the tax burden on locally assessed BPP. The BPP not only discourages capital investment, but it is also a tax that is not well understood and therefore many businesses fail to self-report. Had SB1263 been enacted, Arizona would have joined twelve other states that do not tax BPP. Ultimately SB1263 did not advance in the House because of the fiscal note. *See ATRA position paper in Appendix*

SB1276 assessed valuation; class one property (Mesnard)**Held in House Rules**

As a result of legislation sponsored last year by Senator J.D. Mesnard, ATRA's long-term goal of reducing the class 1 (business) assessment ratio to 15% was achieved and scheduled to drop by one-half percentage points each year until reaching 15% in tax year 2027. A separate measure was also enacted last session to require the county assessor to use a valuation factor of 2.5% on all locally assessed business personal property (BPP) that is initially classified or acquired during or after tax year 2022 and that would otherwise receive accelerated depreciation.

Senator Mesnard sponsored this year's effort under SB1276 to speed up the class 1 assessment ratio reduction to 15% by tax year 2025. Furthermore, the measure adjusted the current accelerated depreciation schedule for all existing BPP (personal property initially classified before tax year 2022) by reducing the percent good 15% each year in the second through fifth years. This provision was included in order to increase the equity between existing BPP that is on a scaled depreciation schedule and newly acquired BPP that is only valued at 2.5%. Like most other proposals with an on-going state general fund impact, SB1276 was held. *See ATRA position paper in Appendix*

SB1495 K-12; school funding; revisions (Bennett)**Held in House ED**

SB1495 was an ATRA-backed bill that was sponsored by Senator Ken Bennett, Chairman of the Senate Education Committee, intended to support a more equitable school finance system by instituting a new optional funding formula for public school districts. Districts would be able to opt into a more streamlined and secure funding formula currently used by charter schools. In return for the funding increase, these districts would forgo locally funded bonds and overrides. The bill cleared the Senate on a 16-12 vote but failed to receive a hearing in House Education. JLBC estimated the state GF costs at \$26.2 million for FY 2025.

PASSED LEGISLATION ATRA OPPOSED

SB1013 colleges; universities; free speech zones (Kavanagh)**Chapter 184**

An amendment was added to SB1013 in the House that provided expenditure limit relief to Arizona's community college districts. Despite appearing to establish penalties for community colleges exceeding the expenditure limits, the penalties established in this bill are de minimis and render the limits meaningless. This bill marks the third straight year that the Legislature has passed the identical expenditure limit relief for the community colleges. This year's bill extends the expenditure limit side-step for both the FY 2024 and FY 2025 budgets, thereby eliminating the need to return to the Capitol next year for similar relief.

FAILED LEGISLATION ATRA OPPOSED

HB2013 transportation tax; deposit; regional fund (Cook)**Held in House WM**

In early 2022, the Arizona Supreme Court ruled that the Pinal County transportation sales tax that was approved by voters in 2017 under Prop 417 was illegal. Since the final judgment, taxpayers have been patiently waiting for direction from ADOR regarding how to apply for a refund from the approximate \$85 million that was collected over the four-year period. HB2013

would have required any amount not refunded to taxpayers to be distributed to the regional transportation authority. ATRA was strongly opposed to allowing the entities that the Court ruled against to keep the sales tax that was ultimately deemed illegal. HB2013 never received a committee hearing. *See also SB1416*

HB2025 community colleges; expenditure limitation (Dunn)

Held in House ED

Mirror bill to SB1082, which was never assigned to a committee in the Senate. HB2025 would have established penalties for community colleges exceeding their constitutional expenditure limits in FY 2024, FY 2025, and FY 2026 by withholding a corresponding amount of state aid. *See also SB1013*

SB1082 community colleges; expenditure limitation (Shope)

Not assigned

Mirror bill to HB2025. Would have established penalties for community colleges exceeding their constitutional expenditure limits by withholding a corresponding amount of state aid.

SELECTED LEGISLATION ATRA MONITORED

HB2003 corporate income tax; rates (Livingston)

Held in Senate Rules

Would have decreased the corporate income tax rate from the current rate of 4.9% to 4% of net income in tax year 2023, 3.5% of net income in tax year 2024, 3% of net income in tax year 2025, and 2.5% of net income in tax 2026 and onward. Retroactive to tax years beginning in 2023.

HB2014 STOs; scholarships; corporate tax credits (Livingston)

Held in Senate Rules

The cap on the corporate income tax credit for contributions to school tuition organizations (STO) would have been raised to \$10 million for FY 2023, \$15 million for FY 2024, and \$20 million for FY 2025 and subsequent fiscal years, up from the previous limit of \$6 million. Additionally, the scholarship amount provided by the STO would have been limited to the state aid calculated for the student, rather than being set at 90% of the state aid amount or the cost of tuition for the student to attend the qualified school.

HB2028 PSPRS; contribution rates (Livingston)

Chapter 102

Reduces the PSPRS contribution rate for Tier 2 members (hired on or after June 20, 2011 through July 1, 2017) from 11.65% to 7.65% beginning in FY 2024. Furthermore, HB2028 eliminates the requirement that an employer be fully funded before using the excess contributions above the 7.65% to reduce the employer's contributions. *Emergency clause*

HB2060 NOW: schools; requirements; revisions (Grantham)

Chapter 170

Gives school districts and charter schools the option to fulfill any legal obligation of posting, displaying, or including specific information on their websites by providing a link to that information on their home page. They are also now permitted to consolidate all the required information on a single webpage and are not obligated to display it directly on the home page.

HB2064 property tax exemption; disability; qualifications (Carter)**Chapter 79**

The definition for a person with a “total and permanent disability” to qualify for a property tax exemption is added to mean someone who is unable to engage in any substantial gainful activity, for pay or profit, by reason of any physical or mental impairment that is expected to last for a continuous period of at least 12 months or result in death within 12 months as certified by a competent medical authority.

HB2145 dude ranches; historical markers (Dunn)**Chapter 171**

Classifies real and personal property of a qualified guest ranch that is included in the Arizona Dude Ranch Heritage Trail Program (Program) under class 4, assessed at 10%. All other guest ranches that don’t qualify are classified under class 2, assessed at 15%. Specifies under the Program that the horse herd of the guest ranch must be present only during the operating season in which guests are present. When a guest ranch is reclassified, a change in the classification is not a change in use, in and of itself, for assessment purposes of applying Rule A or B in the calculation of the limited property value (LPV).

HB2252 NOW: motor vehicle manufacturers; TPT; exemption (Wilmoth)**Vetoed**

Current law provides a TPT exemption of motor vehicle sales to non-residents of this state who have secured a 90-day permit as long as the vehicle is delivered out of state. HB2252 was a late session strike-everything amendment that would have expanded that exemption to non-residents that secure a 30-day permit but could also take delivery in this state. The bill limited the number of 30-day permits each motor vehicle dealer could issue to 500 per year beginning in FY 2024, increased by 10% each fiscal year thereafter. If a purchaser registers the vehicle in this state within one year of issuance, the purchaser is liable for the tax, penalty and interest that the dealer or authorized third party would have otherwise been required to pay.

Although the legislation would have provided a TPT exemption at the state and county level, HB2252 would have allowed the cities the option of exempting these sales at the municipal level. The Governor stated her concerns regarding unintended consequences as to the fiscal impact the legislation would have in her veto letter.

HB2501 dependent tax credit; additional amount (Gress)**Held in the House**

Beginning in tax year 2023, a taxpayer or a taxpayer’s spouse who is pregnant in the year before the taxable year in which the dependent is born would be eligible to an increased dependent tax credit. The increase would be calculated based on a prorated amount according to the number of months of pregnancy during the preceding tax year.

HB2623 NOW: unclaimed property; information; registration (Biasiucci)**Vetoed**

HB2623 would have allowed DOR to disclose confidential information to a “locator” that is registered with the Department. A locator would be required to register with DOR, and upon written request, DOR would be required to provide unclaimed property account information for all unclaimed accounts to a locator in a searchable electronic or digital format. The unclaimed property account information would be required to include the contact information of the apparent owner, the type and cash value of the property, if the property is securities or mutual fund shares, the number of shares or items and the exchange ticker symbol or fund name, and a general description of the safe deposit box contents and the liquidation amount. Required that

an agreement between a property locator and a customer must include a disclosure agreement that states the fee charged is negotiable and is capped at 20%.

The Governor vetoed HB2623 because it would have been “an abuse and misuse of public records” by providing confidential taxpayer information to third party entities for commercial purposes.

HB2809 public infrastructure improvements; reimbursement (Carbone) Chapter 181

The maximum amount in TPT distribution to all cities, towns or counties for the reimbursement of public infrastructure improvements for the benefit of a manufacturing facility is increased from \$100 million to \$200 million. The amount of reimbursement is the lesser of the Prime Contracting TPT revenues collected from contracts to construct manufacturing facilities and associated improvements or 80% of the total cost of the public infrastructure improvements.

SB1063 food; municipal tax; exemption (Borrelli) Vetoed

SB1063 would have exempted from municipal TPT the sale of food for home consumption, effective from and after June 20, 2025. According to a JLBC fiscal note, 65 of Arizona’s 91 cities and towns tax food for home consumption and estimated that the impact would be approximately \$160 million.

The Governor vetoed the bill stating that “local leaders” said the bill would lead to “potential cuts to service-including public safety-to increased property taxes.”

SB1102 transportation tax; Maricopa County (Carroll) Chapter 203

SB1102 reflects a compromise between the Governor and legislative leadership following several attempts on the Maricopa County Prop 400 transportation sales tax extension. As a result of its passage, Maricopa County voters will have the opportunity to vote on the ½-cent transportation sales tax extension in November 2024 for another twenty years.

If approved by the voters, the sales tax allocation is as follows: 40.5% for freeways and other routes in the state highway system; 37% for public transit, but not more than 3.5% may be used for light rail capital rehabilitation; and 22.5% for major arterial streets. Specifically prohibits any monies collected from funding any light rail, commuter rail, streetcar or trolley extension. Further prohibits monies from being spent on any project that will result in the reduction in existing highway lane miles, with some exceptions (outlined). No more than 5% of total revenues collected may be used for regional transportation infrastructure, which is defined to mean transportation projects selected through a performance-based process for non-motorized mobility infrastructure, emerging technologies, and air quality measures.

Another provision in the bill requires the regional public transportation authority (Authority), in coordination with the regional planning agency, to conduct a farebox recovery audit of operating costs and revenues for the previous fiscal year for all public transportation. Part of the audit must determine a farebox recovery ratio, which must achieve 10% in FY 2027 through FY 2028, 15% in FY 2029 through FY 2031, and 20% in FY 2032 and thereafter. If the Authority fails to meet the performance standards in any year, the Authority must demonstrate through the farebox recovery audit that monies from sources other than the sales tax will make up the difference. If the Authority cannot satisfy the requirements prescribed, the excess costs are allocated between affected jurisdictions according to the proportion of service in that jurisdiction that falls below

the percentage requirement. The affected jurisdictions shall pay monies from revenue sources other than the sales tax to the public transportation fund within two fiscal years following completion of the audit.

Other provisions include prohibiting the state or any city, town, county or political subdivision of this state from restricting the use or sale of a vehicle based on the vehicle's energy source and prohibits the use of public monies to extend a light rail loop around the Capitol Mall. Furthermore, the speed limit for all types of motor vehicles is at least 65 miles per hour on the interstate highway system in Maricopa County, with some exceptions. Expands membership in the transportation policy committee, including one member who represents a taxpayer organization and one member who represents residential housing development. Includes a legislative intent clause that development of SR 30 between SR 85 and Loop 303 will begin in the first phase of the plan.

SB1131 residential leases; municipal tax exemption (Petersen) Chapter 204

SB1131 preempts cities, towns or other taxing jurisdictions from levying a transaction privilege tax (TPT) or fee on residential rental property, from and after December 31, 2024. A landlord of real property that is in a city, town or other taxing jurisdiction that levies TPT on the property shall no longer charge the tenant for the tax. In any civil action challenging the lawfulness of a charge, assessment or other amount, the landlord has the burden of proving by a preponderance of the evidence that the challenged charge, assessment or other amount is not attributable to and does not represent any portion of TPT on the rental of residential property.

Requires the Arizona Department of Revenue (ADOR) to notify each residential rental TPT licensee on or before September 30, 2024, to no longer levy the tax from and after December 31, 2024, and to post the notice on its website. Requires municipalities to use revenue generated from the TPT collections of remote sellers for public safety before any other municipal purpose. A legislative intent clause directs affected cities and towns to reduce nonessential government spending, including spending on lobbyists and out-of-state travel, to address any revenue shortfall as a result of eliminating the tax.

SB1189 NOW: municipal tax code commission; continuation (Mesnard) Chapter 192

Extends the MTCC sunset date through July 1, 2027. Requires ADOR to incorporate changes to the Model City Tax Code (MCTC) that are required to conform the MCTC with a statutory change within 30 days of the effective date of the statutory change. Requires a two-thirds vote of the Municipal Tax Code Commission (MTCC) to adopt a proposed amendment to the MCTC that either repeals a model or local option that provides an exemption from taxation or which expands the types of business activities that are considered taxable. SB1189 included a purpose clause stating that the Legislature continues the MTCC to promote uniformity and consistency among the excise tax bases of municipalities through the MCTC and to provide a forum for both taxpayers and municipalities to present recommendations for changes to the code and to listen to general taxpayer concerns.

SB1190 NOW: department of revenue; administration (Mesnard)**Chapter 7**

For TPT purposes, “audit” is defined to mean a review or examination of a taxpayer’s accounts, financial information, books and records and any other document to ensure information is reported correctly on a return and to verify the reported amount of tax is correct. For property tax purposes, the Director of ADOR may extend the county assessor’s March 1st deadline for mailing the annual notice of value to taxpayers when a state of emergency is declared.

SB1230 tax exemptions; affidavit (Mesnard)**Chapter 14**

A TPT exemption certificate that is obtained by a qualifying community health center, qualifying health care organization or qualifying hospital or any other entity that is recognized as a 501(c) nonprofit is valid until the entity no longer qualifies. For any entity that no longer qualifies, written notification must be provided to ADOR otherwise the entity is liable for any tax, penalty and interest. Clarifies that a person claiming a property tax exemption must only initially claim the exemption by filing an affidavit with the county assessor. However, if a person no longer qualifies, the person must notify the county assessor in writing if all or part of the property is conveyed to a new owner, the property is no longer used for the purpose for which it qualified, or there is any event that otherwise disqualifies the person or property from the exemption. Specifies that an individual is not entitled to a property tax exemption as a widow or widower, a person with total and permanent disability or a veteran with a disability under more than one category, rather than being limited to the aggregate maximum.

SB1281 NOW: income tax rebate (Shamp)**Held in House Rules**

ADOR would have been obligated to provide a one-time rebate for individual income tax in the 2022 tax year. This rebate would have applied to Arizona residents who file an individual income tax return and remain residents as of December 31, 2022. The rebate amount would have been \$200 for single individuals or those who file separately if married, and \$400 for married couples filing jointly or heads of households. ADOR would have been mandated to disburse all rebates within 90 days from the effective date had the law been enacted.

SB1400 community colleges; noncredit workforce training (Wadsack)**Chapter 198**

"Noncredit workforce training" full-time equivalent student enrollment from a community college district (CCD) is now considered when calculating the total full-time equivalent student enrollment for the CCD. This calculation is used to determine state aid and the expenditure limitation for the CCD. Additionally, specific requirements are established for noncredit workforce training or career and technical education courses offered by community colleges, where contact hours are used instead of credit hours. By December 31, 2023, each CCD must provide the necessary data to the Economic Estimates Commission to determine the student population of the CCD for FY1979-80.

SB1416 county excise tax; rate reduction (Wadsack)**Held in TAT**

SB1416 was a competing legislative proposal to HB2013 to address the illegal tax collected in the Pinal County transportation sales tax case. Under this proposal, the county would have been required to reduce the county’s existing sales tax rate by an amount equal to the net revenues remaining after all refunds during the first year of the refund period.

SB1577 income tax rate; reduction; surplus (Mesnard)**Failed House Third Read**

SB1577 would have required JLBC to determine an income tax rate reduction when there is a state general fund (GF) structural surplus. Specifically, JLBC would be required to calculate the “growth limit” (*ongoing state GF revenues adjusted for population & inflation*) and excess state tax collections (*the amount of ongoing state GF revenues that exceed the growth limit*) and determine the structural surplus if ongoing state GF revenues are more than the growth limit. If a surplus is determined, ADOR would be required to reduce the individual income tax rate equal to 50% of the structural surplus in the following fiscal year. SCR1035, which was an identical measure but that would have required voter approval at the next general election, was held in House Rules.

SB1717 dual enrollment; revisions; appropriations (Kaiser)**Held in House Rules**

Would have established the Dual Enrollment Incentive Program under the Arizona Department of Education (ADE). The program aims to offer bonus incentives to teachers, school districts, and charter schools when their students successfully pass a qualifying dual enrollment course. To support the implementation of the program, an allocation of \$5 million from the general fund would be earmarked for the newly formed Dual Enrollment Incentive Fund in FY 2024. Additionally, \$500,000 from the general fund in the same fiscal year is designated for the newly established Dual Enrollment Development Fund, which provides incentive bonuses to teachers instructing at least one dual enrollment course. Furthermore, an appropriation of \$15 million from the general fund in FY 2024 would have been allocated to the newly created Dual Enrollment Student Fund. This fund is dedicated to extending financial assistance to students who successfully complete a qualifying dual enrollment course and meet other specified criteria. Lastly, an appropriation of \$5 million from the general fund in FY 2024 is designated for the program itself.

Despite failing in the House, the K12 BRB included some of the same incentives. In the 2023-24 and 2024-25 school years, ADE will provide a \$500 incentive bonus to teachers for every student who achieves a passing grade in a remote course that results in college credit (CCEIP exam). Two continuous appropriations were also in the BRB, including a \$1,000 bonus to each teacher teaching a dual enrollment course and reimbursement payments to students of \$50 per dual enrollment course credit (\$300 max for grades 9 or 10, \$600 for grades 11 or 12).

SB1734 taxation; 2023-2024 (Kavanagh)**Chapter 147**

As part of the FY 2024 state budget: *Individual income tax rebate*: Requires ADOR to issue a onetime individual income tax general welfare rebate (Arizona Families Tax Rebate) to an Arizona taxpayer who filed a full-year resident tax return for tax year 2021, claimed a dependent tax credit on the return, and who meets one of the following qualifications: 1) Had a tax liability of at least \$1 for TY 2021; 2) If no tax liability in 2021, filed a full-year resident tax return for TY 2020 under identical filing status used on the taxpayer’s TY 2021 tax return with tax liability of at least \$1 for TY 2020; 3) If no tax liability in 2021 or 2020, filed a full-year tax return for TY 2019 under the identical filing status used for TY 2020 and 2021 and had tax liability of at least \$1 for TY 2019. The rebate is equal to \$250/dependent under age 17 and \$100/dependent who was at least 17, limited to a maximum of three dependents. If more than three, dependents under age 17 are counted first. ADOR is required to issue rebates between October 15, 2023

and November 15, 2023. A taxpayer who does not receive the rebate on or before November 15, 2024 may file a claim application with ADOR. Prohibits a letter relating to the rebate from being sent from the Governor's office, being sent on the Governor's letterhead or referencing the Governor's office.

Individual income tax subtraction for adoption expenses: Increases the Individual Income Tax subtraction for unreimbursed adoption expenses from \$3,000 to \$40,000 effective for tax years 2023 through 2025.

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The taxpayer's watchdog for over 80 years

ARIZONA TAX RESEARCH ASSOCIATION

2023 LEGISLATIVE PROGRAM

Introduction/State Budget

ATRA's legislative program is developed each year with recognition that the Legislature and Governor's highest priority for the session should be passing a Fiscal Year (FY) 2024 state budget that is balanced and sustainable.

The 2022 session saw an extraordinary increase in state spending due to skyrocketing state revenue growth. However the current three-year JLBC budget predicts much slower revenue growth for the FY 2024 budget year.

Current estimates suggest that the state's cash position continues to outpace budget estimates. The Governor's Office of Strategic Planning and Budgeting (OSPB) estimates the structural surplus this year at \$2.7 billion.

ATRA will provide updated state budget recommendations to the Legislature after the JLBC and the OSPB have submitted their recommendations for the FY 2024 budget.

Taxation

Property tax reform. ATRA has led the effort to reform Arizona's property tax system and reduce the disparity in tax treatment between business and residential property. As a result of previous ATRA-backed legislation passed in 2005, 2007, 2011, 2021, and 2022, ATRA achieved its decade's long goal of reducing the class one assessment ratio to 15% beginning in 2027. In addition, the historic reductions in the business personal property tax, coupled with the passage of Proposition 130 this November, now provides a realistic opportunity for its complete elimination.

Prevent greater access to the property tax. For the 2023 session, ATRA will oppose efforts on the part of Arizona state and local governments and special districts to increase access to the property tax base.

In addition, ATRA will advocate for the continued compliance with the state's Truth-in-Taxation (TNT) law. Since its passage in 1998, the state has consistently complied with the TNT law and state controlled tax rates have declined in each of the last eight years. While those rates have both risen and fallen with the fluctuations in the real estate market, ATRA believes adherence to the TNT law is an important principle that has and will continue to benefit taxpayers over time.

Targeted Property Tax Breaks. For decades, ATRA has led the effort at the Capitol to oppose rifle-shot property tax breaks to specific industries. ATRA will continue to support policies that provide for equitable treatment among property taxpayers and oppose efforts that undermine that important policy principle.

For the 2023 session, ATRA will pursue the following legislation:

Property Tax

Property Tax Reform. The 2021 and 2022 legislative sessions saw significant progress in the area of business property tax reform. In 2021, legislation was passed to reduce the class one assessment ratio from 18% to 16% over four years. In 2022, legislation passed to further reduce the class one assessment ratio to 15% through half-percent decreases beginning in 2026. The 2022 session was further highlighted by a significant prospective reduction in the locally assessed personal property tax by reducing the taxable value of new property to 2.5%. 2022 was wrapped up with the passage of ATRA supported Proposition 130 in November giving Arizona lawmakers the statutory authority over business personal property tax exemptions.

In 2023, ATRA will support an effort to accelerate the class one assessment ratio reduction to 15% from 2027 to 2025. This acceleration should be combined with further personal property tax relief under the new authority provided to the Legislature, which will consist of increasing the personal property exemption from \$207,366 to \$500,000 and enhancing the accelerated depreciation schedule for property enrolled prior to tax year 2022.

Sales Tax

Clarify Taxation of Digital Goods and Services. Following a 2017 legislative study committee which found the state lacks statutory authority to tax digital goods and services, the Legislature attempted a legislative fix in 2018 and 2019 to provide the state the legal authority to tax digital goods and exempt digital services. The bill established definitions for software, digital goods, and digital services in a new classification of TPT. It made licensed prewritten software and all digital goods subject to TPT, regardless of transfer method. Licensed software is software where the user has the right to electronic transfer; in essence the user has a right to a full copy as opposed to remote access. For digital goods, such as ebooks, movies, television shows and audio files, they are taxable if transferred electronically or accessed remotely. Though this made streaming audio and video taxable, there were exemptions for scheduled programming, such as live linear broadcast, which have never been subject to TPT. ATRA will again pursue legislation to update Arizona's tax code related to the taxation of digital goods and services.

Prime Contracting Simplification. Arizona's prime contracting tax is generally regarded as the most complex and inefficient areas of Arizona's transaction privilege tax (TPT) system. Some improvement was achieved through TPT Simplification in 2013 that transitioned activities involving maintenance, repair, replacement, and alteration (within certain thresholds) from prime contracting to a tax on materials at the point of sale, now known as MRRA. MRRA simplified tax compliance for most contractors that only work on MRRA projects; however,

contractors involved in residential home remodels, for instance, can unknowingly get pulled into prime contracting. For example, tax guidance published by the Arizona Department of Revenue considers moving interior walls or adding a kitchen island as “modification” activity, which will make the entire contract taxable under prime contracting if the cost of the modification activity exceeds 15%. ATRA will pursue legislation to simplify residential remodels by eliminating the current thresholds for alteration projects, and instead, only tax contracts under prime contracting that add or expand square footage regardless of the amount of modification activity performed within the existing roof and exterior walls of the home.

Public Finance:

Fire District Debt Limits. Current statute limits the amount of general obligation debt that a fire district can absorb to six percent of the net assessed value of the district. However, current statute does not limit the amount that a fire district is able to request from district voters. ATRA will pursue legislation to limit the amount that a district can request from voters to the amount of their current debt capacity under their debt limits.

School Finance Reform: For decades, ATRA has advocated for a school finance system that is equitable and reflective of Arizona’s K12 system that encourages and promotes parental choice. ATRA has also argued that a more equitable school finance system reduces that state’s exposure to the continuous litigation facing the state. ATRA will pursue the following school finance reforms in the 2023 session:

Create a state student funding formula. This proposal would allow any school district with no secondary property tax (no bonds or overrides) to switch to a new state funding formula similar to the current charter funding system. Upon the approval of district voters, eligible districts would opt into the new state funding system (an average of \$1,200 more per pupil) and agree to forgo bond and override funding. In order to offset some of the state general fund impacts of the new state funding formula, district voters would also be required to approve an additional property rate tax of \$0.35 for elementary and union districts or \$0.70 for unified districts.

Reform the current district transportation formula. Arizona’s long standing formula to provide transportation funding to school districts is both flawed and antiquated. Among other problems, the current system actually provides more per-pupil transportation funding to districts that are losing students and actually experiencing decreased demand for transportation dollars. What would normally be a rather simple transportation funding system (approved daily route miles multiplied by the per-mile support level) is complicated by a formula to hold districts harmless at their highest historical transportation expenditure.

The formula funding on actual route miles is called the Transportation Support Level (TSL). The historical high water mark is the Transportation Revenue Control Limit (TRCL). The state is only liable for the actual route miles or the TSL. For districts with higher TRCL’s, those expenditures are funded through a local district property tax.

ATRA will pursue legislation to phase out the TRCL and transition districts to a more equitable per pupil allotment.

County Flex Language. Beginning in FY 2009, counties were provided the broad authority to shift revenues from their special revenue funds, including countywide special taxing districts, to their general funds. The initial intent of this broad authority was to offset state cost shifts that began during the Great Recession. This “flexibility” language exists both in state statute and has been included in session law in the state budget every year. To date, the counties have shifted more than \$68 million from their special revenues that were intended for a specific purpose into their general funds to fund any county fiscal obligation. Although the state cost shifts have ceased, this broad authority remains. ATRA will pursue legislation to repeal the authority in state statute and discourage lawmakers from continuing this practice as they negotiate the FY 2024 state budget.

ATRA SUPPORTS SB1172 – *As Amended*

Fire District G.O. Bond Reform

Summary

SB1172 limits the amount a fire district may request in General Obligation (G.O.) bonds from its voters. As introduced, SB1172 would have limited the amount a fire district could request in G.O. debt to the district's current debt capacity (debt limit less outstanding G.O. debt). A compromise amendment between ATRA and the Arizona Fire District Association increased the amount that may be requested to 120% of the district's debt capacity instead of 100%.

Basis for ATRA's Support

Current statute limits the amount of G.O. debt a fire district can absorb to six percent of the net assessed value of the district. However, there is no limitation on how much a fire district can *request* from its voters. Without limitation, this means that a fire district could request an amount that far exceeds its debt limit. This can create significant exposure to taxpayers if a jurisdiction opts for a very short term schedule to defease a bond sale in order to evade their debt limit.

Regrettably, this scenario played out recently in Crown King Fire District (FD). In 2021, voters in the Crown King FD approved \$1 million in G.O. bonds although the District's debt limit was only approximately \$200k. To remain within the District's debt limit, the bonds were structured so that \$200k would be issued annually over six years. However, due to the District's small tax base, the annual tax rate to service the debt payments are projected at \$6.73 per \$100 of assessed value over the six-year repayment schedule. Consequently, the fire district's total tax rate for operations and debt service in tax year 2022 more than tripled, from \$3.25 to \$9.7739. **As a result, the annual tax increase on a residential property valued at \$100,000 is estimated at \$673 and \$12,116 on commercial property valued at \$1 million.**

Typically, bonds are defeased over a long period of time, like 15 to 20 years. **In contrast, these bonds are being defeased all in one year over six consecutive years.**

SB1172 is a necessary reform that will provide financial guardrails for fire districts, but more importantly, will protect taxpayers from punitive tax rates.

ATRA ASKS LAWMAKERS TO SUPPORT SB1172!



ARIZONA TAX RESEARCH ASSOCIATION
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ATRA SUPPORTS HB2807

Simplifies Residential Contracts under Prime Contracting

Arizona's prime contracting tax is generally regarded as the most complex and inefficient area of Arizona's transaction privilege tax (TPT) system. Unlike most other states that tax materials at retail, Arizona's prime contracting tax system allows contractors to purchase materials tax-free at retail with the use of exemption certificates, and instead, pay taxes on 65% of the gross proceeds of the contract upon completion of the project. **The ability to purchase materials tax-free has led to serious noncompliance concerns for many years. [A 2019 study commissioned by the Arizona Department of Revenue determined that the noncompliance under the prime contracting tax could be as high as 19% (*Prime Contracting Study, ASR Analytics*).]**

In 2012, Governor Brewer's TPT Simplification Task Force recommended the state "aggressively" transition from the current prime contracting tax to a tax on materials at retail. Although a total elimination of prime contracting was not accomplished, the Legislature did achieve carving out certain activities from the contracting tax to a tax on materials at retail that involved maintenance, repair, replacement, and alteration (within certain thresholds), now known as MRRA.

Under MRRA, all materials included in a contract for maintenance, repair, and replacement activities are subject to tax at retail regardless of the contract amount. However, the contract cost for "alteration" activities must remain within specific thresholds for the materials to remain taxable at retail, otherwise the contract may be taxable under the prime contracting tax. For residential alteration projects, the contract price cannot exceed 25% of the property's full cash value.

While the intent of MRRA was to simplify tax compliance for contractors, the lines remain blurred for contractors that enter into contracts for jobs that involve alteration activities. **This area of taxation is so complicated that the guidance provided by the Department of Revenue (DOR) is over 20 pages long and includes over 30 scenarios (*TPN 18-1*).** For example, according to this guidance, a residential contract to remodel a kitchen that includes adding a kitchen island (modification) could move an alteration project under MRRA into prime contracting if the total contract price exceeds 25% of the home value.

Examples of Specific Scenarios

- 1. Scenario:** A homeowner decides to remodel her kitchen. The owner hires a contractor and has him replace all of the existing appliances and flooring. Additionally, the homeowner decides to have the contractor install a new island that did not previously exist. The full cash value of the home at the time of bid is \$200,000. The contract price is \$40,000.

Result: This contract is not subject to prime contracting TPT. The addition of the kitchen island causes this project to be treated as either an alteration project or a modification project. Because the contract price is only 20% of the of the full cash value of the property, the project meets the definition and criteria for an alteration and is therefore exempt from TPT. The materials to be used in this MRRA contract are subject to retail TPT.

DOR TPN 18-1

HB2807 will simplify residential MRRA projects under the Prime Contracting class so that residential contracts that do not involve adding or expanding the square footage of the structure will pay tax on the materials at retail rather than be subject to the prime contracting tax.

ATRA ASKS LAWMAKERS TO VOTE YES ON HB2807!



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STATE OF ARIZONA

Department of Revenue



March 1, 2023
Rep. Michael Carbone
AZ House of Representatives
District 25

Katie Hobbs
Governor

Robert Woods
Director

Dear Rep. Carbone:

This letter is written in response to your request to the Department for clarifying information related to contracting. More specifically, you inquired about certain statements made by Mr. Nick Ponder of the League of Cities and Towns during testimony for HB2807, as follows:

1. A kitchen remodel would be considered an "alteration" under MRRA because it is a change of one system, whereas a remodel of an entire home would be considered prime contracting since it entails the remodel of more than one system.

Short Response: This statement apparently introduces a new interpretation of alteration that is unsupported by the law. Below, the existing law is summarized with a couple of examples.

2. All of the revenues generated for materials incorporated into MRRA contracts go to the places where the materials are sold and not to the location of the project.

Short Response: This statement is simply inaccurate. The law requires TPT licensed contractors that purchase MRRA materials tax-exempt to report taxes on those materials based on the location of the project. In fact, according to data collected by the Department, cities have collected \$4,516,085.75 of tax on materials for MRRA projects for fiscal 2022, which has been paid to the cities where the construction activity took place. Assuming an average city tax rate of 2.3%, this means that approximately \$196m of taxable materials used in MRRA projects have been reported to the cities where the work is being performed.

Discussion

In relation to the first statement, whether a kitchen remodel is considered an alteration under MRRA, depends on what that remodel entails. A kitchen remodel where the scope of work includes only the replacement of items in the kitchen would indeed be considered MRRA, but it would be *replacement* MRRA, not *alteration* MRRA; therefore, the *alteration* thresholds will not apply and, as a result, the cost of the project is irrelevant.

If, on the other hand, the remodel requires that the kitchen be laid out differently and/or the square footage of the kitchen changes, then it is likely that some components of the project would be *alteration* and others would be *replacement*. It all depends on what is required to

be done in each case. In addition, while the statute defines an *alteration* as any activity or action that causes a direct physical change to existing property, it also specifies that *alteration* does not include maintenance, repair or replacement. As you may recall, maintenance, repair and replacement do not have thresholds, whereas alteration does. As a result, it is very important that all the elements of the project be categorized correctly.

In relation to the second statement, a special emergency bill, Laws 2015, Chapter 4, Section 6 (SB 1446), was passed to overhaul and make workable the newly bifurcated method of taxing the construction industry. One key issue that was addressed in this bill of particular relevance here relates to contractors' inventory and materials procurement. In the prior approaches to the new bifurcated taxing scheme (2013 and 2014 legislation), all MRRA materials were to be purchased with tax paid (i.e., taxable sales), whereas all prime contracting materials were to be purchased tax-exempt. This reality created significant concern among many contractors. Here's why: contractors tend to purchase materials in bulk for quantity discounts and for the convenience of having certain regularly used materials on hand. The problem was that if some items of inventory were purchased with tax paid (for MRRA jobs) and some were purchased without tax (for traditional prime contracting jobs), inventory control would have become significantly more complicated and the risk of error much greater than previously had been the case.

Accordingly, these issues were addressed by specifically allowing contractors the choice of (1) paying tax on MRRA materials at the time of purchase, or (2) purchasing MRRA materials tax-exempt (consistent with their purchases of materials for prime contracting jobs) and then, when the tax-exempt materials are used in a MRRA project, the contractor would report and pay retail TPT *to the jurisdiction in which the project is located*. This is specifically provided by § 42-5008.01(A)(1) as follows:

The amount of liability shall be calculated **and reported based on the location of the [MRRA] project** and the taxes imposed under this chapter and chapter 6 of this title.

For proper reporting purposes, contractors are required to state the cost of MRRA materials and to calculate the retail equivalent TPT on those materials based on the location of the project. Tax returns for contractors indicate that, for fiscal 2022, cities where MRRA projects have taken place have collected \$4,516,085.75 of tax on MRRA materials. Assuming an average city tax rate of 2.3%, this means that approximately \$196m of taxable MRRA materials were reported to the cities where the work was performed.

Rep. Michael Carbone
AZ House of Representatives
District 25
March 1, 2023
Page 3

I hope this information is of assistance to you. If you have any further questions, feel free to contact the Department again.

Sincerely,

Lisa Querard

Lisa Querard
Research & Policy Administrator
Taxpayer Services Section
Arizona Department of Revenue

ARIZONA BUSINESSES SUPPORT SB1263

Locally Assessed Business Personal Property Elimination

Arizona has passed many bills over the last 30 years to reduce the tax burden on business personal property (BPP).

- The Legislature initially enacted “accelerated depreciation” for newly acquired BPP in 1994 and has adjusted the accelerated depreciation schedule twice since its initial enactment. Accelerated depreciation front-loads the depreciation on newly acquired equipment in order to encourage economic development in our state.
- The voters approved a constitutional amendment in 1996 to exempt the first \$50,000 in BPP per taxpayer. That exemption is now \$207,366 due to adjustments for inflation.
- Legislation enacted in 2022 limited the taxation of newly acquired BPP to a valuation factor of 2.5%.
- Voters’ passage of Prop 130 last November provided the Legislature with the authority to fully exempt the tax on locally assessed BPP.

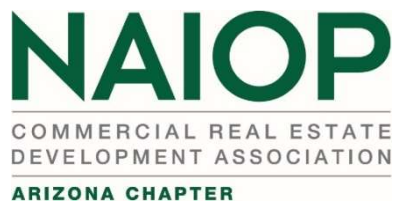
Historically, in addition to being a tax that discouraged capital investment in Arizona, the BPP was complicated and inefficient. Worse, many business taxpayers often fail to self-report because they are unaware they owe the taxes.

Previous actions by the Arizona Legislature and the voters have slowly reduced the reliance on the BPP tax and Arizona can now move to completely eliminate the compliance burden on both taxpayers and county government to administer this tax. **In fact, locally assessed BPP currently accounts for less than 3% of the total property tax base.**

Passage of SB1263 will allow Arizona to join 12 other states that have eliminated the BPP tax:

- Delaware, Hawaii, Illinois, Iowa, Minnesota, New Hampshire, New Jersey, New York, North Dakota, Ohio, Pennsylvania, South Dakota.

ORGANIZATIONS IN SUPPORT



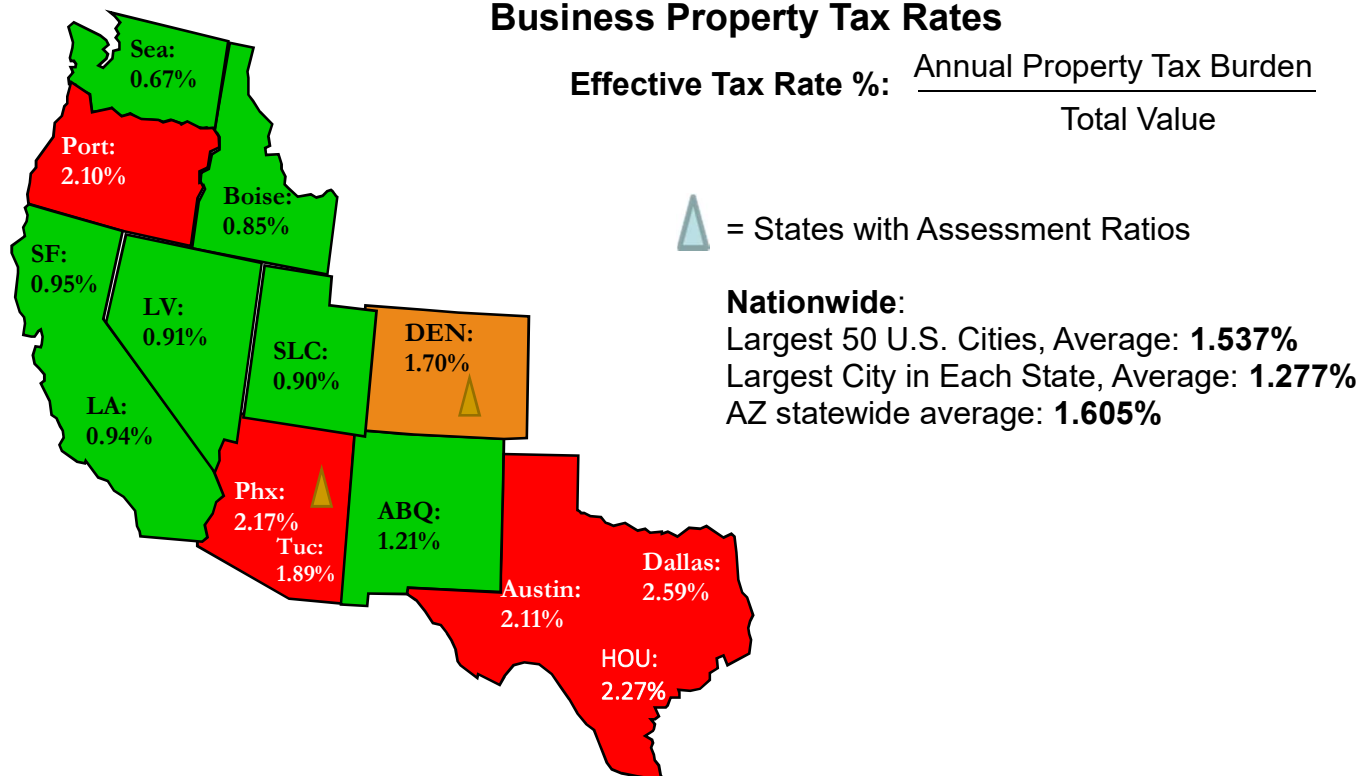
THE ARIZONA BUSINESS COMMUNITY SUPPORTS PROPERTY TAX REFORM – SB1276

2023

Right Size Arizona's Business Property Tax

- Accelerating the Class 1 Assessment Ratio reduction to 15% moves the state towards a more equitable, sustainable property tax base
- Reduces the tax burden on newly acquired locally assessed business personal property
- Arizona's business property taxes are uncompetitive
- AZ ranks high both regionally and nationally in business property taxes
- As opposed to targeted tax breaks for well-connected or new businesses, this policy path creates greater equity for all Arizona businesses

Regional Comparison of Business Property Tax Rates



Source: 50-State Property Tax Comparison Study, Minnesota Center for Excellence, Tax Year 2021, comparing medium sized industrial property.

ORGANIZATIONS IN SUPPORT

