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ARIZONA TAX RESEARCH ASSOCIATION

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## 2026 ATRA Legislative Update

The following summaries include a few of ATRA's top priorities of the 2026 session, as well as bills ATRA is opposing due to their bad policy objectives.

### ATRA SUPPORTS

#### **SB1293 GPLET (Mesnard)**

The Government Property Lease Excise Tax (GPLET) law allows cities to provide massive tax breaks to developers by entering into development agreements to build multi-million dollar projects. These agreements are mainly used by the cities, predominantly Phoenix and Tempe, for the development of major projects. To exempt property from the tax roll, the developer transfers title to the city once the project is completed and the city "leases" the property back to the developer through the GPLET agreement. Although the property is used for a private purpose, it is exempt from property tax because it is technically "owned" by a governmental entity.

In addition to not paying property taxes, the developer also dodges paying the excise taxes to the county, community college, and school districts during the abatement period. The only payments the developer is typically contractually obligated to make are "rent" payments to the city and "annual donations" to the school districts that represent only a fraction of what the property taxes or excise taxes would be otherwise. The schools are subsidized by all taxpayers from around the state through

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## Governor Vetoes Income Tax Conformity—Twice

As a static conformity state, Arizona policymakers are annually faced with the task of updating Arizona's income tax to either align with the federal tax code or decouple from changes they disagree with. In most years, this is relatively non-controversial legislation that is quickly acted upon and signed by the Governor. However, when Congress makes significant changes to federally adjusted gross income (FAGI), Arizona's starting point for calculating individual income taxes, conformity becomes a significant tax and budget issue for state policymakers.

Following Congress' passage of H.R.1 in July 2025, some states across the country reacted quickly to make adjustments to their income tax codes to either conform to or decouple from the federal changes. Acting early allowed those states to provide timely guidance to their state tax departments to ensure the income tax forms created in the fall of 2025 actually reflected state law.

Receiving no updated guidance from state policymakers, which would have only been possible through a special session called by Governor Hobbs or a two-thirds vote of the legislature, the Arizona Department of Revenue (ADOR) created Arizona income tax forms in the

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early fall assuming conformity on changes to FAGI. Importantly, the ADOR is directed by state statute (A.R.S. § 43-102) to presume conformity to federal changes to FAGI and created forms reflecting that. However, on November 20, 2025, Governor Hobbs released an Executive Order directing ADOR to make further changes to the 2025 personal income tax forms to reflect provisions of H.R. 1 that did not change FAGI. Those changes, which the Governor dubbed the “Middle Class Tax Cut Package,” addressed taxes on tips and overtime income, interest on car loans, and a senior tax deduction. The order also directed ADOR to increase the standard deduction to match the increased deductions in H.R. 1.

Despite knowing that ADOR had already incorporated those changes into the 2025 tax forms, Governor Hobbs’ Executive Order criticized several changes in H.R. 1 impacting Arizona businesses. The order also suggested it was standard procedure for those changes to FAGI be considered in conjunction with state budget negotiations. While fiscal policy is often a consideration in state budget negotiations, questions regarding conformity to federal income tax changes for a **previous** tax year is not common practice.

After a failed attempt in the first week of the legislative session to get the Governor to support a conformity bill, that itself would have required changes to the tax forms, the legislature pivoted to a clean conformity bill in HB2785 (Olson) and SB1638 (Mesnard). ATRA strongly supported that version because it was consistent with the forms taxpayers were already using to file their 2025 returns and would eliminate the chaos of requiring taxpayers to file amended returns.

Importantly for Governor Hobbs, those bills also made legal the form Arizona taxpayers were using to comply her Middle Class Tax Cut. Unlike the traditional above-the-line changes to FAGI directed in A.R.S. § 43-105, the subtractions from income on ADOR’s Middle Class Tax Cut form are not grounded in any legal foundation.

Following the second veto, House and Senate leadership publicly encouraged Arizona income taxpayers to begin filing their returns while committing to stand behind the forms ADOR made available. Governor Hobbs, who has continued to express strong opposition to the business provisions like full expensing of business property and research and development expenditures, continues to say this will be worked out in future budget negotiations.

The chaos and uncertainty facing Arizona taxpayers filing their 2025 income tax returns demonstrates the need for Arizona to pursue a mechanism that requires state policymakers to respond to major federal tax changes in a timely manner. House Ways and Means Chair Justin Olson introduced HB4029 to create a process for the state to at least acknowledge major federal tax changes. The bill would require the Governor’s Office of Strategic Planning and Budgeting and the Joint Legislative Budget Committee to both evaluate federal tax changes to determine if they cause state revenues to increase or decrease \$100 million or more. If the analysis reached the \$100 million threshold, the Governor would be tasked with deciding if a special session was necessary to either conform or decouple from the federal changes.

While not perfect, HB4029 would at least elevate a potential conformity crisis in a timelier manner and provide policymakers the opportunity to respond before ADOR income tax forms are published.

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additional “state aid” payments, costing the state general fund millions annually.

In addition to these major tax breaks, there remains the potential Gift Clause violations with each GPLET deal. Arizona’s Gift Clause states that a municipality may not “give or loan its credit in the aid of, or make any donation or grant, by subsidy or otherwise, to any individual, association, or corporation.” Taxpayers won a Gift Clause challenge when the Arizona Supreme Court ruled under *Schires v. Carlat* (2021) that consideration to a private entity was grossly disproportionate and therefore violated the Gift Clause. Prior to *Schires*, the Maricopa Superior Court found under *Engleborn v. Stanton* (2020) that the GPLET tax subsidy between the City of Phoenix and a developer to build a high-rise residential tower (Derby) in downtown Phoenix violated the Gift Clause. Specifically, the Court ruled that the benefits to the developer over the term of the lease were “grossly disproportionate” to the amount received by the public. Although the city argued that the GPLET was necessary for the project to be built, construction of the Derby was completed and is in full operation today- without the GPLET.

Despite taxpayer’s recent successful challenges, the cities continue to crank out these GPLET deals and it is unreasonable to require taxpayers to legally challenge every one of them. To reduce potential Gift Clause violations to future GPLET deals, SB1293 limits the abatement of excise taxes to all entities except for school districts. In addition to ensuring K12 schools are not negatively impacted by the lost revenue, SB1293 will reduce the size of the gift for gift clause purposes. *SB1293 has advanced through the process and currently awaits House 3<sup>rd</sup> Read.*

**SB1294 Destroyed Property (Mesnard)**

Arizona law permits property owners to have their taxes prorated when improvements—such as buildings or structures—are removed, demolished, or destroyed after the lien date. This ensures taxpayers aren’t taxed on property that no longer exists. Historically, this proration applied regardless of the cause of destruction.

During the 2024 legislative session, however, county assessors supported a change limiting the definition of “destroyed” to improvements lost due to an act of God (such as fire, flood, or natural disaster). The goal was to help homeowners who lost homes to wildfires and faced delays in rebuilding by allowing them to remain in the same, lower ratio property class for up to five years. But the change unintentionally eliminated proration relief for property destroyed for any other reason.

SB1294 restores the previous statutory language, ensuring that proration is again available for all destroyed property—no matter the cause—while still maintaining the 2024 Legislature’s intent to support homeowners affected by natural disasters. *SB1294 passed the Senate 26-1 and the House Ways & Means Committee on a 6-1 vote.*

**HB2289 TNT; Bonds; Property Tax Examples (Olson)**

HB2289 updates the property tax examples used in publicity pamphlets for bond and budget override elections, as well as in truth-in-taxation (TNT) notices that local jurisdictions must publish when proposing property tax increases. These notices are designed to help taxpayers understand the potential tax impacts of approving these measures.

Under current law, the residential property value examples included in these notices range from \$80,000 to

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\$250,000. Because residential values in Arizona have increased significantly over time—and vary widely across the state—these statutory examples no longer reflect today’s market.

HB2289 modernizes and standardizes the residential property tax examples by replacing them with two updated values: \$100,000 and \$300,000. For commercial property, existing bond election notices use a \$1 million valuation; HB2289 adds a second example based on a \$2 million commercial property to provide a more accurate range of potential impacts. *HB2289 passed the House and currently awaits a hearing in the Senate Finance Committee.*

**ATRA OPPOSES****HB4130 Municipal Budget Amendments (Blackman)**

The adopted strike-everything amendment to HB4130 would allow cities and towns to increase their adopted budgets at any time during the fiscal year. Current law requires counties, cities and towns to adopt their annual budget by the first Monday in August. This annual process provides for great transparency by requiring local governments to hold public hearings and publish detailed estimates of revenues and expenditures. These budgets account for all expected revenues, including beginning cash balances, state-shared and local taxes, bond proceeds, and anticipated state and federal grants. Just as importantly, the budget process provides taxpayers the opportunity to review and comment on spending plans before they are finalized. Allowing cities and towns to increase their adopted budgets would weaken the transparency and public accountability that is provided in the current process and diminishes taxpayers’ ability to meaningfully engage in local spending decisions. *HB4130 currently awaits a House floor vote.*

**HB2883 Small School Adjustment (Tsosie)**

The SSA provides a wholesale exemption from the school budget limits for small school districts. District’s that qualify have a student count of 125 or less elementary students or 100 or less high school students. Most of these small school districts are located in rural Arizona and those that qualify can levy an unlimited amount in primary property taxes, leading to some of the highest property tax rates in the state. HB2883 would have increased the SSA student-count threshold from 125 to 160 for both elementary and high school, significantly increasing the number of districts qualifying as a small school district. *HB2883 was held in the House Education Committee.*

**HB2918 Renewable Energy Equipment Valuation (Wilmeth)**

Current statute directs the ADOR to determine the full cash value of renewable energy and storage equipment based on 20% of the depreciated cost of the equipment (taxable original cost less depreciation) through December 31, 2040. As amended in the House, HB2918 would require the department to value such property at 100% of the depreciated cost for equipment placed in service from and after December 31, 2029. ATRA is opposed to the measure since it would impose a significant tax increase on the investment decisions already made by this industry in expectation of the favorable tax treatment. *HB2918 passed the House on 32-24-3 vote and currently awaits a hearing in Senate Finance.*

**Leg Update**, *Continued from page 4***HB2950 Tourism; Hotels (Wilmeth)**

HB2950 would allow a county or city to form a tourism improvement area on a petition signed by lodging business owners who represent at least 67% of the total lodging business rooms available within the area. The authority would be funded through an assessment on all lodging businesses in the area and the assessments may vary for the types or classes of lodging businesses, including the size of the property or number of rooms. Once formed, the governing body would be required to contract with its destination marketing organization (organization) to manage and implement the area activities, including advertising, promotion or business recruitment directly related to lodging businesses. The organization may levy an assessment up to \$5 per night or 5% of the room rental receipts. ATRA is opposed to the bill as it would set a precedent for granting quasi-governmental status and taxation authority to private entities. *HB2950 currently awaits a floor vote in the House.*

**SB1724 Property Splits (Mesnard)**

Under current law, property that is split, subdivided or consolidated requires the new limited property value (LPV) be calculated based on a percentage of full cash value comparable to that of other properties in the same classification (Rule B). As introduced, SB1724 would have Rule B apply only if the change results in the “creation of a new, independently usable and independently marketable economic unit or functional unit,” otherwise Rule A applies (5%). The reason provided by the county assessors for advancing this measure was to prevent taxpayers from submitting property splits solely for the purpose of reducing the LPV on properties with a higher LPV to FCV relationship compared to the current Rule B percentages. ATRA is supportive of tightening the statutory language to eliminate such loopholes but the challenge is in crafting the language in a way not to undermine the current purpose of Rule B, which is intended for property that experiences a significant physical change or change in use.

**SB1764 Property Definitions (Mesnard)**

SB1764 would have made major changes to some of the property tax definitions used in determining how locally and centrally valued property is assessed. One major change was to redefine the existing definition of “current use.” Under current statute, “current use” is defined as the use of the property at the time the assessor or department of revenue values the property. Instead, “current use” would be defined to mean the primary use of the property “as shown by objectively verifiable and economically substantive conditions.” The proposal further provided that the county assessor determine a property’s current use “from the totality of the circumstances, including the property’s objectively verifiable characteristics, information and functions.” ATRA opposed the effort since it would make sweeping changes to the property tax statutes that govern the assessment of all property. The bill sponsor agreed with ATRAs recommendation to have an ad hoc committee discuss over the interim that could include all stakeholders before making major changes to the property tax statutes included in SB1764, as well as SB1724.

**Leg Update**, *Continued from page 5***SB1504 PSPRS Retirement Enhancements (Gowan)**

SB1504, which failed on a 3-7 vote in the Senate Appropriations Committee, would have increased retirement benefits for Public Safety Personnel Retirement System (PSPRS) members in Tiers 2 and 3. The bill enhanced normal retirement benefits for both Tiers by adding eligibility at 25 years of service without regard to age. The minimum age requirement was a key provision of previous PSPRS reforms in 2011 and 2016.

In addition, the bill also significantly changed the new cost of living adjustment (COLA) for Tier 3 members. The COLA was another major provision of the 2016 reforms that created Tier 3. The current Tier 3 COLA applies to a retired member at the earlier of the first calendar year after the seventh retirement anniversary or when the retired member turns 60 years old. SB1504 reduced the current seven year waiting period to three years.

The 2016 PSPRS reforms included a statutory provision requiring future benefits adopted by the legislature to be fully paid for in the year of enactment of the benefit. The PSPRS actuary pegged the upfront costs in excess of \$450 million. Unsurprisingly, proponents advanced an amendment in the Senate Appropriations Committee to exempt the benefit increases in the bill from the prefunding requirement and shifted the bills impact to increased contribution rates over time. The bill failed despite the adoption of that amendment.