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## ARIZONA TAX RESEARCH ASSOCIATION

TO: Arizona State Legislature

FROM: Kevin McCarthy

RE: Maricopa County Treasurer Hos Hoskins' letter attacking the Arizona Legislature and Arizona Tax Research Association (ATRA)

Maricopa County Treasurer Hos Hoskins used the taxpayer funded mailing of the 2015 property tax bills to attack state policymakers and ATRA for a series of property tax reform measures dating back to 1980. In addition to being an extraordinary abuse of taxpayer funds, this reckless attack is full of inaccuracies and intentionally ignores key points in a clear attempt to distort the truth. In an effort to respond in a timely manner, this memo will attempt to address just the major inaccuracies in his letter.

Hoskins primarily focused his attention on changes to the assessment ratios for class one (business) property as well as SCR1025 that was referred to voters as Proposition 117. While he conflates these issues, they have no material connection, so this memo will address them separately.

### **Assessment Ratios/Homeowner Rebate**

Arizona has long held the dubious distinction of having one of the most complicated property tax systems in the United States. One of the major complications is that Arizona classifies property based on use and shifts tax burdens across property types through the use of assessment ratios. For example, a \$100,000 business has an assessment ratio of 18.5% and therefore is taxed on a net assessed value of \$18,500. On the other hand, a residential property valued at \$100,000 has an assessment ratio of 10% and pays taxes on a net assessed value of \$10,000. Hoskins' attempt to suggest that tax burdens have shifted over time from business to residential uses data that is not only inaccurate but excludes major policy changes in an attempt to mislead Maricopa County taxpayers.

Hoskins' central argument is that state policymakers have systematically shifted property taxes from business to residential property over the last 35 years. He suggests those changes have resulted in residential taxes now being 20 to 30 percent higher as a result. However, in making this calculation, he either intentionally or unintentionally misleads on a variety of fronts including using the wrong assessment ratio in the base year of his analysis and ignoring multiple changes to the state-subsidized homeowner rebate that have occurred over the last 35 years.

Hoskins' incorrectly argues that the assessment ratio for homes has remained at 10% since 1973. He carries that error through his tax shift analysis that begins with the major property tax reforms passed in 1980. The truth is the assessment ratio on owner-occupied residential property was reduced 33% from 15% to 10% in 1980 at the same time as the reductions to the business assessment ratios he targets. Commercial and industrial property assessment ratios were reduced from 27% to 25%. The assessment ratios on centrally assessed utilities and telecommunications were reduced from 50% to 44% and mining property was reduced from 60% to 52%. Both utility and mining property assessment ratios were put on schedule to be reduced to 30% in 1987. Overall, the effect of the 33% reduction (which Hoskins' calculations omit) in the owner-occupied residential assessment ratio in 1980, coupled with a significant

increase in the homeowner rebate, was to significantly reduce tax liabilities for homeowners. (For context, these changes were made as Arizona lawmakers desperately attempted to dodge a version of California's Proposition 13 that was on the Arizona ballot in November of 1980.)

The next major change to assessment ratios targeted by Hoskins has an omission that clearly demonstrates his desire to mislead taxpayers. In 2005, in an attempt to address Arizona's top five ranking in highest business property taxes in the country, Arizona policymakers passed HB2779 that reduced the assessment ratio for class one property (business) from 25% to 20% over 10 years. Hoskins' analysis conveniently excludes that each percentage point reduction in the class one ratio was accompanied by a percentage increase in the state-funded homeowner rebate from 35% to 40%. Contrary to Hoskins' assertion that lawmakers were unwittingly shifting taxes from business to homeowners, the increase in the homeowner rebate was a clear reflection of lawmakers' desire to dampen or eliminate such shifts. In addition to the increase in the homeowner rebate, lawmakers also increased the cap on the rebate from \$500 to \$600.

Notwithstanding Hoskins' attempt to suggest that this reform was a nefarious attempt by ATRA to hoodwink state policymakers, HB2779 was supported by a huge coalition of businesses groups and received bipartisan support before being signed by then Governor Napolitano. This policy was revisited two years later in HB2784 where lawmakers shortened the phase down to six years. The final vote before being signed by Governor Napolitano was 57-2-1 in the House of Representatives and 28-0-2 in the Senate.

In 2011, the Legislature passed HB2001 and Governor Brewer signed, a four year phase down of business assessment ratios from 20% to 18% beginning tax year 2013 and concluding in 2016. Hoskins also omits that this legislation was accompanied by another increase in the homeowner rebate. This legislation has increased the homeowner rebate from 40% to the current 45% and will climb higher in tax year 2016. Another exclusion in Hoskins' analysis that would have conflicted with his narrative was the significant ratio reductions extended to rental residential property. Following the initial reduction from 21% to 18% in 1980, rental residential assessment ratios were phased down to 10% through a couple of legislative changes. The final phase down from 15% to 10% occurred between 1989 and 1994. Notwithstanding the fact that this change disproportionately shifted taxes to businesses, ATRA and most business taxpayers supported this change because it was good policy.

Finally, it is important to remember that the politics of class warfare have always been a part of the debates on the use of assessment ratios in Arizona's property tax system. Arizona is in the minority of states that use assessment ratios to shift taxes from one property type to another. Generally speaking, a \$100,000 business property will pay roughly twice the property taxes as a \$100,000 residential property in the same jurisdiction. Hoskins' focus on the potential tax shifts associated with incremental changes in assessment ratios conveniently ignores the massive tax shift that has always occurred through the policy of employing variable assessment ratios. In fact, for tax year 2014 (the last year information is available) business property taxes were \$934 million **higher** as a result of the 19% assessment ratio. Conversely, residential (owner occupied and rental) properties were \$832 million **lower** as a result of the 10% assessment ratio. In debating the impacts of assessment ratio changes it is simply intellectually dishonest to ignore the initial tax shifts associated with this long standing policy.

### **Proposition 117**

Hoskins is correct that ATRA was the primary author of SCR1025 that was referred to the ballot in 2012 after receiving bipartisan support in the Legislature. However, he publicly opposed Prop 117 and his complicated attempt to suggest that it isn't good for residential taxpayers is again full of inaccurate statements. However, before I address his criticism of Prop 117, it is important to note that his attack on

ATRA members and their support of Prop 117 might underscore his attempt to mislead more than anything else. He wades into his attack on ATRA by suggesting that “ATRA membership is comprised of lobbyists for owners of high value properties (mostly DOR valued), and they have been very successful in persuading the legislators to give tax breaks to their special interest clients.” The problem with this irresponsible accusation is that these large companies that are valued by the Department of Revenue (i.e. centrally valued) don’t receive the benefit of the 5% valuation limitation provided by Prop 117 since it only applies to locally assessed properties. These centrally valued companies supported Prop 117 for the same reasons that ATRA did – it simplified and stabilized a property tax system in desperate need of both.

Every study of Arizona’s complicated property tax system over the last 35 years has criticized the hyper complication of Arizona’s property valuation scheme. Prior to Prop 117, locally assessed business, residential and agriculture property would receive an annual value from the assessor reflecting the updated full cash (market) value. That full cash value became the basis for what was referred to as the secondary net assessed value. This value was used for the payment of all secondary property taxes (mostly voter approved bonds and overrides and special taxing districts). More importantly, this value could be annually increased without limit. In other words, a 60% increase in the value of a home during the spike in the real estate market would see a 60% increase in the secondary net assessed value. When rates were left the same, those homeowners saw 60% increases in secondary taxes to those jurisdictions.

In addition to the secondary net assessed value, locally assessed properties were also given a limited or primary value that was used to pay primary property taxes. The annual change to this primary value was limited to 10% or 25% of the difference between the current secondary value and the previous year’s primary value. After considerable debate with state policymakers, county assessors and other interested parties reached a consensus that the existing valuation system had to be simplified along with a meaningful and fair limitation on property valuation growth. Despite Hoskins’ suggestions to the contrary, Prop 117 was the subject of robust debate and evaluation at the Capitol prior to it being referred to the voters. To no surprise, voters overwhelmingly approved Prop 117: **locally assessed taxpayers would have one taxable value that would be limited to 5% in annual growth.**

Hoskins, along with some members of the property tax consulting industry that benefited handsomely from an overly complicated system, continue unsuccessfully to convince taxpayers they are actually worse off with a 5% cap on annual valuation growth versus no cap at all. Every property taxpayer that has witnessed the shell game of elected officials claiming they didn’t increase taxes because they left the tax rate the same knows that taxpayers are individually and collectively better off with a 5% cap on valuation growth.

As was the case with the assessment ratios, Hoskins spins a limited story on how Prop 117 might be impacting property taxpayers in its first year of implementation. Most notably, he leaves out the great news for property taxpayers that statewide property tax levies are only up 2.1% over 2014 levies. That is less than half the growth rate experienced in 2014. Moreover, Prop 117’s limitation on the growth of taxable values is perfectly timed to protect taxpayers from another round of large valuation increases as the real estate market continues to recover from the Great Recession.

For decades, Arizona policymakers have implemented policies that ensure that residential property taxes in Arizona remain in the lower quartile in the country. These important tax reforms that Hoskins criticized has not changed that low tax status for residential property taxpayers. However, they have helped decrease the major impediment to economic development and job growth in Arizona associated with high business property taxes.