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ARIZONA TAX RESEARCH ASSOCIATION

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Statewide Property Taxes Up Just 2.1%

Property value spikes tempered

Despite the 13% growth in market values statewide, Prop 117 limited the increase in taxable value to only 2.4% in tax year 2015. As a result, total primary and secondary property taxes rose just 2.1% this year, which is half of last year's growth.

Primary Taxes

Primary property taxes, which fund the operations of local governments, account for nearly 70% of total taxes levied. This year's 2.4% increase ($110 million) in primary property taxes brings the total to nearly $4.8 billion and county government is responsible for the majority of that increase at nearly $56 million.

Two counties, Pima ($12.7 million/4%) and Pinal ($6.1 million/8%), both increased their primary taxes substantially to offset the state cost shifts associated with the 1% cap issue (*see ATRA 2015 September Newsletter*). Gila County also caused a significant increase of $2.8 million in primary property taxes by leaving the tax rate the same despite 16% growth in the county's tax base.

The community colleges (CC) followed closely behind the counties with a 3.7% increase ($26 million) in primary

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Articles Inside:

Tax Rate Books Are In!

The 2015 Property Tax Rates & Assessed Values publication is now available. Please contact the ATRA office at 602-253-9121 or visit our website at www.arizonatax.org to order a copy.

ATRA FALL EVENTS CALENDAR

ATRA Golf Tournament: Nov 6 McCormick Ranch, 12:00pm
ATRA Outlook Conference: Nov 20 Scottsdale Hilton, 8:00am

Contact ATRA at (602) 253-9121 to sign up or for sponsorship info

Isaac Elementary's Tax Rate Soars 146%

Cash Balance Problem Befuddles Taxpayers

Taxpayers in West Phoenix with property in Isaac Elementary were shocked to find their total property tax rates spiked 27% this year. Most of that increase was from a 146% bump in the K-12 primary rate, from $2.60 to $6.40. It's all in the primary rate; unrelated to a bond or an override. The district's overall budget remained nearly the same as last year. The reason is complex and concerning.

The County School Superintendents office publishes a tax rate calculation worksheet which shows the problem. The district had previously been treating lines of credit as cash on hand which was artificially keeping their primary rate low for several years. Cash on hand will reduce the local property tax rate of a school district.

The last time the district levied enough to match their budgetary need was FY 2011. They under levied from 2012 to 2015, putting them in a significant deficit which their local property taxpayers will now cover with interest.

The FY 2016 K-12 qualifying tax rate (QTR) is $2.0977, which is the rate state law formulaically expects the local property taxpayer to contribute for elementary districts. Isaac's rate is fully $4.50 higher than contemplated by state law.

The dominant reason for a tax increase... is the primary school tax rate rose because of a change in the district's cash balance position.

Isaac Elementary is a district whose rate will unfortunately be significantly higher than the QTR because their school board chooses each year to levy for Deseg/OCR outside of their normal budget, which is levied on top of the QTR. The extra $5 million they levy each year costs local taxpayers roughly $4.20 per $100 of assessed value in property taxes- all on top of the QTR. The extra $5 million gives the district roughly $735 more per pupil. Neighboring districts such as Osborn, Fowler, Riverside, Murphy and Alhambra Elementary do not have access to the Deseg/OCR levy.

The dominant reason for a tax increase in many jurisdictions this year is the primary school tax rate rose because of a change in the district's cash balance position. The complexity that may drive year-to-year changes in K-12 primary property tax rates is one of the least understood elements of Arizona public finance.

A school district's secondary property tax rate is rather simple: it pays for voter approved bonds and overrides. The rate was advertised to the public and will fluctuate with changes in district assessed value. The levied amounts, which will also vary from year to year, cover the cost of the override and the annual debt service for the bonds.

Isaac Elementary certainly isn't the only district to under levy and cause a massive rate correction. Gilbert Unified under levied at least $15 million in FY 2012 and has been slowly crawling out of a deficit ever since with

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above average primary rates. It's worth mentioning that many primary rates this year decreased because of an increase in the districts cash balance situation.

The key policy problem is trying to ascertain the exact cash balance position of a district, which they certify in writing to the County School Superintendent on June 30 each year. That cash balance amount less encumbrances will offset their budget year primary tax rate. A district can spend into their budget authorization regardless of whether they levied enough because the district can access debt, which is intended to be short term only but in practice, is not.

A major part of the ongoing K-12 education finance discussions is how to manage property tax rates for school districts and how to level the playing field for taxpayers. Lawmakers will need to find a mechanism to avoid the rate spikes occurring as a result of cash mismanagement.

-Sean McCarthy

Maricopa County School District	Rate Increase from Cash Change
Aguila Elementary	11%
Alhambra Elementary	16%
Avondale Elementary	13%
Balsz Elementary	9%
Creighton Elementary	13%
Isaac Elementary	146%
Morristown Elementary	68%
Murphy Elementary	119%
Palo Verde Elementary	23%
Peoria Unified	11%
Phoenix Elementary	8%
Riverside Elementary	18%
Union Elementary	39%

Governor Appoints Sean McCarthy School Facilities Board Chairman

Over the summer, Governor Ducey appointed ATRA Senior Research Analyst Sean McCarthy to the School Facilities Board. State law calls for the board to include "one private citizen who represents an organization of taxpayers." McCarthy replaces ATRA Vice President Jennifer Stielow on the board. This October, Governor Ducey appointed McCarthy the Chairman of the nine-member board, which is charged with spending legislatively appropriated dollars for capital projects in school districts. The School Facilities Board expends roughly $16 million per year in Building Renewal Grants plus supplemental funding when appropriated ($10.1 million in FY 2015). It also grants funding for emergency deficiency corrections. The Board is also charged with new school facilities for qualifying districts.

Fire Districts Seek Tax Increase

Officially Request Unlimited Taxing Authority

The dramatic growth in fire district levies leading up to the Great Recession was unprecedented. Property values doubled between 2005 and 2009 and most fire districts failed to reduce tax rates to offset the increased values. During that time, tax rates dropped only 5.6%, causing an astounding 80% increase in property taxes. The failure of fire districts to adjust rates downward when values surged was the impetus that led the Legislature to enact levy limits on fire districts and the Legislature should reject any recommendation by the fire districts that exposes taxpayers to massive tax increases in the future.

In the year leading up to the peak in 2009, fire district levies grew 20% as a result of the districts leaving their tax rates virtually unchanged despite 28% growth in values. That year, there were approximately six districts that levied up to the $3.25 tax rate cap. With the dramatic value growth realized during the years leading up to the Recession, the fire districts had the perfect opportunity to reduce their tax rates and create future rate capacity; however, that was not at all the case. For example, the average tax rate dropped only 11 cents (5.6%) despite the twofold growth in property values between 2005 and 2009.

The massive tax increases inflicted on taxpayers by the districts prompted the ATRA-backed legislation in 2009 that imposed levy limits on fire districts. After much debate, ATRA and fire district representatives came to a compromise agreement to limit fire district levies to 8% plus the value associated with annexations while maintaining the $3.25 tax rate cap. Additionally and at the request of the fire districts, the Legislature authorized the districts to seek voter approval for either a permanent tax override within the $3.25 rate cap or a five-year override to exceed the rate cap but remain subject to a 5% annual levy limit, which would be restricted to districts that experience a 20% decrease in taxable value over two consecutive years. In 2012, the Legislature removed the voter approval requirement for districts that experienced a decline of 25% or more in value since 2008 to exceed the $3.25 rate cap, up to a maximum of $3.75, for tax years 2012 and 2013 only.

Over the years, ATRA has worked with the fire districts on various legislative proposals that increased their taxing capacity. In 1992, ATRA worked together with the districts to reform the Fire District Assistance Tax (FDAT), which set the distribution at 20% of the local district levy (rather than the budget) and capped the maximum distribution at $300,000. Additionally, the measure increased the local tax rate cap from $2.60 to $3.00. In 2005, the rate cap was increased again to the current rate cap of $3.25. In 2011, ATRA and the districts worked together again to address an inequity in the FDAT that was prompted by a merger between three districts in Tucson. At that time, districts that merged were held harmless from the $300,000 FDAT cap and these three districts used that provision to maximize their distribution to $900,000 in the first year of the merger. The action of those districts prompted the Legislature to remove the hold harmless provision for all districts to prevent similar abuse in the future. Additionally, the FDAT cap was increased to $400,000.

Following the crash in the real estate market, statewide full cash values (FCV) were nearly identical to statewide LPV. That scenario provided a unique opportunity to move from a dual valuation tax system that taxed both the

FCV and LPV to a single taxable value. In 2012, voters overwhelmingly passed the ATRA-backed measure that the Legislature referred to the ballot under Prop 117 that made the LPV the only taxable value and limited its annual growth to 5%. The property valuation limit implemented under Prop 117, along with the combination of levy limits and rate cap on fire districts, were designed to prevent districts from imposing dramatic tax increases on taxpayers similar to those prior to the Recession.

The recent decline in values have prevented many of the districts, particularly those at the rate cap, from implementing substantial tax increases. For instance, between 2010 and 2015, the tax base for fire districts dropped 26%. In response, the average tax rate for fire districts increased 50 cents to $2.40, yet levies still dropped 3.3%. Consequently, as a result of the recent increase in tax rates combined with failure of the districts to adjust rates when times were good, nearly one-third of the fire districts are now at the $3.25 rate cap.

During the 2015 legislative session, the Arizona Fire District Association (AFDA) proposed legislation that would expand the use of the temporary override to all districts without regard to a reduction in the tax base, in addition to extending the temporary override to eight years without an annual levy limit. ATRA opposed the measure and the bill was ultimately held in the House Ways & Means Committee. As often happens when bills fail, the Legislature created a joint legislative study committee to study the level of fire safety services provided to rural areas, the taxation levels in various counties, and the frequency of mergers and consolidations in rural areas.

The study committee met for the first time in October, in which several of the fire districts provided testimony regarding their current fiscal situations. Many questions were raised as a result of that testimony, such as why the districts neglected to reduce taxes during the real estate boom, how much cash the districts currently hold in reserves, and what kind of efficiency measures were taken by the districts over the last several years. At the conclusion of the meeting, the districts were unified in their recommendations to remove both the $3.25 local tax rate cap and the $400,000 cap on FDAT distributions. The committee is expected to meet again in November.

-Jennifer Stielow

Statewide Totals	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
NAV	11%	15%	33%	28%	2%	-8%	-15%	-9%	-7%	1%	1%
RATES	4%	2%	-4%	-2%	-2%	0%	7%	7%	5%	3%	2%
LEVIES	13%	18%	25%	20%	2%	-2%	-7%	-2%	0%	4%	2%

STATEWIDE PROPERTY TAXES, *Continued from Page 1*

taxes. Pinal CC led the way with an overwhelming increase of 23.5% ($9 million). Like Pima and Pinal Counties, Pinal CC is also subject to the state cost shifts associated with the 1% cap issue (Pima CC is not likely impacted by the 1% cap penalty). Yuma/La Paz CC decided to levy their maximum allowable levy, resulting in an increase of 9% ($2 million).

Arizona's cities increased primary taxes this year by 2.9% ($8.4 million). By increasing its tax rate from $2.49 to $3.69, the town of Clifton increased taxes 50% ($131,326) to $395,000. The City of Yuma increased taxes 12.4% ($1.2 million) as a result of increasing its tax rate 24 cents. The City of Tucson increased its primary tax rate 5

PRIMARY LEVIES

Jurisdiction	Tax Year 2005	Tax Year 2014	Tax Year 2015	1-yr Change	10-yr Change
State	$229,726,774	$315,410,700	$321,563,137	2.0%	40.0%
Counties	$799,358,200	$1,023,628,616	$1,079,509,657	5.5%	35.0%
Cities	$179,753,814	$286,858,146	$295,227,397	2.9%	64.2%
Comm. Colleges	$453,880,949	$709,009,453	$735,448,917	3.7%	62.0%
Schools	$1,931,610,896	$2,349,614,013	$2,362,930,895	0.6%	22.3%
Other	$0	$0	$0	-	-
TOTAL	**$3,594,330,633**	**$4,684,520,928**	**$4,794,680,003**	**2.4%**	**33.4%**

cents, thereby increasing taxes 11% or $11.7 million.

Primary levies for K-12 schools increased 0.6% ($13.3 million) this year to $2.4 billion although the Qualifying Tax Rate (QTR) decreased slightly due to the Legislature's adherence to truth-in-taxation (TNT). TNT requires an adjustment to the primary tax rate to offset any change in value. Since its enactment in 1998, the Legislature has consistently applied the TNT law to the two major property tax rates it controls, the QTR and the state equalization tax rate (SETR), both of which fund Arizona's education system (*see the Isaac Elementary article on page 2*).

State levies grew 2% ($6.2 million) this year to $321.6 million. The SETR was adjusted for TNT by the Legislature, and as a result, dropped 0.5%. Additionally, some school districts that receive no state aid are required to levy a Minimum QTR, which is based on a statutory calculation. Although both the SETR and the MQTR provide funding for schools, the levies are set by the Legislature and therefore fall under the category of state levies. The 4.8% growth in MQTR levies this year was offset by the reduction in the SETR, which resulted in a net increase in school funding.

Secondary Taxes

Secondary taxes, which are levied to fund voter-approved bonds and overrides, as well as special taxing districts, grew by 1.6% ($35.4 million) in 2015. However, the total increase would actually be lower if it wasn't for the 10.7% ($47 million) increase in the "other" category, which includes special taxing district levies for fire districts, countywide special taxing districts, and the like. The $47 million increase in this category was largely the result of Prop 480, in which voters approved $935 million in bonds for the Maricopa County Special Health Care District. As a result, the district levied an additional $37 million this year to fund the first year debt service payment. Fire districts made up the remaining increase in "other" levies, amounting to a total increase of $5.5 million.

SECONDARY LEVIES

Jurisdiction	Tax Year 2005	Tax Year 2014	Tax Year 2015	1-yr Change	10-yr Change
State	$0	$0	$0	-	-
Counties	$214,148,549	$254,591,524	$265,097,178	4.1%	23.8%
Cities	$260,387,742	$275,257,795	$276,856,885	0.6%	6.3%
Comm. Colleges	$73,801,560	$104,207,057	$101,310,698	-2.8%	37.3%
Schools	$1,010,037,991	$1,100,067,054	$1,079,354,765	-1.9%	6.9%
Other	$275,866,538	$438,124,969	$485,030,182	10.7%	75.8%
TOTAL	**$1,834,242,380**	**$2,172,248,399**	**$2,207,649,708**	**1.6%**	**20.4%**

County secondary levies grew 4.1% ($10.5 million) in tax year 2015. Maricopa County increased its tax rate for flood control 2 cents, which resulted in a 13% ($5.8 million) increase in secondary taxes. Gila County, as a result of substantial growth in value, increased its levy for library services 28% ($332,000) by not adjusting its tax rate to offset the value growth. Mohave County, on the other hand, offset the overall increase in county secondary levies by dropping the tax rate for its TV district 5 cents, thereby dramatically reducing the secondary levy 73% ($893,000). Additionally, Mohave County cut its tax rate for library services 10 cents, which resulted in a decrease in secondary taxes of 34% ($1.9 million).

Not all taxing jurisdictions increased secondary taxes this year. Overall, community colleges reduced their secondary levies by 2.8% ($2.9 million) and school districts by 1.9% ($20.7 million).

10-year levy growth

Total levies have grown 29% ($1.6 billion) since tax year 2005, with a 33% increase ($1.2 billion) in primary taxes and 20% increase ($373.4 million) in secondary taxes. Over the last ten years, the levies of the special taxing districts (other) have grown the most at nearly 76% ($209 million). The 59% increase ($309 million) in community college levies were mainly driven by the 62% growth ($282 million) in primary levies over that same time. Now that Prop 117 is in effect, double-digit levy growth may now be a thing of the past.

-Jennifer Stielow

TOTAL LEVIES

Jurisdiction	Tax Year 2005	Tax Year 2014	Tax Year 2015	1-yr Change	10-yr Change
State	$229,726,774	$315,410,700	$321,563,137	2.0%	40.0%
Counties	$1,013,506,749	$1,278,220,140	$1,344,606,835	5.2%	32.7%
Cities	$440,141,556	$562,115,941	$572,084,282	1.8%	30.0%
Comm. Colleges	$527,682,509	$813,216,510	$836,759,615	2.9%	58.6%
Schools	$2,941,648,887	$3,449,681,067	$3,442,285,660	-0.2%	17.0%
Other	$275,866,538	$438,124,969	$485,030,182	10.7%	75.8%
TOTAL	**$5,428,573,013**	**$6,856,769,327**	**$7,002,329,711**	**2.1%**	**29.0%**