BILL # HB 2263 **TITLE:** assessed valuation; class one property

SPONSOR: Huffman **STATUS:** As Amended by House Ways & Means

REQUESTED BY: House **PREPARED BY:** Steve Schimpp and Hans Olofsson

FISCAL ANALYSIS

Description

Beginning on January 1, 2005, this bill would change the assessment ratio of Class 1 property from 25% to 24% of the full cash value or limited valuation. (Class 1 includes locally assessed and centrally valued commercial and industrial property.) To prevent K-12 Basic State Aid costs from increasing due to a loss of K-12 "local share" tax collections from Class 1 properties under the bill, HB 2263 would require the Truth in Taxation (TNT) (A.R.S. §41-1276) tax rates for FY 2006 (the first year of bill implementation) to be computed in a manner that compensated for any loss of revenue.

Estimated Impact

The JLBC Staff estimates that the 1% reduction in the Class 1 assessment ratio would increase state General Fund assistance to K-12 schools by $24 million in FY 2006. The bill would also reduce expected growth in the state's FY 2006 General Fund cost for "Truth in Taxation" property tax adjustments by the same amount. If an adjustment is made for the TNT savings, the bill would have no net General Fund fiscal impact.

At the local level, $14 million in school property taxes related to Basic State Aid would be shifted from Class 1 to other classes of property.

Analysis

A district-by-district analysis indicates that reducing the assessment ratio on Class 1 property from 25% to 24% in FY 2006 would reduce K-12 "local share" tax collections by about $(24) million that year if the K-12 Qualifying Tax Rate (QTR) and County Equalization Tax Rate (CETR) remained unchanged. (The QTR and CETR are the two tax rates that generate "local share" funding under the K-12 equalization funding formula.) This would cause Basic State Aid costs to increase by $24 million, since A.R.S. § 15-971 requires Basic State Aid to offset changes in "local share" funding on a dollar-for-dollar basis.

The bill, however, would require the QTR and CETR to be adjusted in order to offset losses in "local share" revenues under the bill. We estimate that this would require the QTR for unified school districts to be approximately 8¢ higher (4¢ higher for elementary and high school districts) under the bill and the CETR to be about 1¢ higher. It is likely that the 8¢ adjustment would be a reduction in the planned decline in the QTR rather than an actual increase above the prior year rate.

Our TNT provisions require annual QTR reductions to offset the growth in existing property values. In FY 2004, for example, TNT reduced the QTR by about 14¢. Therefore if HB 2263 had been in effect for FY 2004, TNT would have reduced the QTR by about 6¢ rather than 14¢, with the 8¢ difference being used to offset the Class 1 NAV loss for FY 2004 under the bill.

Increasing the K-12 QTR in order to offset higher Basic State Aid costs under the bill would cause Homeowner's Rebate costs to rise as well because the state would pay 35% of the estimated 8¢ QTR increase for homeowners (100% if they were in 1% cap districts). This would require the QTR to be further increased in order to generate enough Basic State Aid savings to offset higher Homeowner's Rebate costs. Since Class 3 (homeowner occupied) property currently accounts for about 43% of total statewide NAV, we estimate that the Homeowner's Rebate would cost about $3.5 million more under the bill than under current law ($24 M total QTR "increase" X 43% X 35% rebate = $3.5 M). As a rough guess, we speculate that a total QTR "increase" of about 9¢ would be required in order fully fund changes in Basic State Aid and Additional State Aid costs under the bill in FY 2006.

Analysis (Cont'd)

In addition, if counties, cities & towns and community colleges in 1% cap districts decided to raise their primary property tax rates in order to offset Class 1 NAV reductions under the bill, the homeowner cost of those increases would be shifted to the Homeowner's Rebate as well. (The state would not pay for them in school districts that are below the 1% cap because the Homeowner's Rebate only applies to K-12 property taxes unless a district is above the 1% cap.) This potentially could require a QTR adjustment of more than the speculative 9¢ amount cited above. The Homeowner's Rebate impact of this aspect of the bill cannot be determined because we do not know the extent to which other taxing jurisdictions would increase their tax rates (if at all) under the bill. Currently (in FY 2004) counties, cities and towns, and community college districts collectively levy about $1.4 billion in primary property taxes versus about $1.8 billion collectively for school districts statewide.

We estimate that a 9¢ adjustment in the QTR for FY 2006 would increase statewide property tax collections by roughly $28 million. About $24 million of this total would be paid by local taxpayers and $4 million would be paid by the Homeowner's Rebate. The state would recoup the $4 million Homeowner's Rebate cost, however, because the estimated 9¢ QTR adjustment would lower Basic State Aid costs by about $28 million.

Local Government Impact

Class 1 property itself would pay for part of the estimated $24 million net increase in local property tax collections under the bill in FY 2006 because the estimated 9¢ QTR adjustment would apply to it as well. Since Class 1 property currently accounts for about 40% of statewide NAV, we estimate that Class 1 property owners would pay about 40% of the $24 million net estimated 9¢ adjustment in local property taxes under the bill, or about $10 million. The remaining $14 million would be paid by owners of other classes of property and would represent the net "tax shift" to those classes of property from Class 1 under the bill.

In addition, K-12 "local share" taxes account for only about 50% of total primary property taxes collected, so it is possible that the total "tax shift" to other classes of property for primary property taxes would be twice that amount, or about $28 million. The latter impact would occur if counties, cities & towns, school districts, special districts and community colleges all increased their primary property tax rates proportionately in order to offset the loss of Class 1 property value under the bill.

Local taxing jurisdictions also levy *secondary* property taxes, and it is possible that they would all increase their secondary property tax rates as well under the bill in order to offset reductions in Class 1 property values. Currently (in FY 2004) local taxing jurisdictions (including school districts) collectively levy about $1.6 billion in *secondary* property taxes, which is roughly the same as the amount collected for K-12 "local share" taxes for which we estimate a $14 million "tax shift". This suggests a potential additional "tax shift" of about $14 million under the bill, for a combined total potential shift of about $42 million ($28 million primary + $14 million secondary = $42 million total).

2/24/04