BILL # SB 1131 **TITLE:** property tax exemption; disabled veterans

SPONSOR: Blendu **STATUS:** As Introduced

PREPARED BY: Hans Olofsson

FISCAL ANALYSIS

Description

Conditional upon voter approval of SCR 1005 in the next general election, SB 1131 would provide a property tax exemption for disabled veterans. The amount of the exemption would be in direct proportion to the percentage rating of a veteran's service connected disability. For example, a veteran with a 50% service connected disability who meets the requirements under the proposed legislation would receive an exemption equal to 50% of his or her primary residence's assessed valuation.

SCR 1005, which is the companion bill to SB 1131, requires that a veteran's service connected disability must be at least 10% in order to be eligible for the exemption. The proposed exemption would also apply to the surviving spouse of a disabled veteran who dies or the surviving spouse of a soldier who is killed in action while serving in the U.S. Armed Forces.

To qualify for the property tax exemption, the household income of the disabled veteran, or surviving spouse, cannot exceed (1) $30,000 if the household includes up to 2 children, (2) $36,000 if the household includes 3 children, (3) $42,000 if household includes 4 children, or (4) $48,000 if the household includes 5 or more children.

Estimated Impact

The fiscal impact of this legislation cannot be determined with certainty due to a lack of income data. Based on a set of simplifying assumptions, however, the impact is not expected to be greater than a cost of $5.0 million or a savings of $(1.0) million beginning in FY 2008. The bill will reduce statewide net assessed valuation (NAV), which will increase the state's K-12 education formula cost. That impact, however, could be offset by reducing the cost of automatic school tax rate reductions. Lower assessed value requires less of a tax rate reduction.

Analysis

According to the Arizona Department of Veterans' Services (ADVS), 563,800 veterans resided in Arizona in 2005. Of these veterans, 57,900 received disability compensation. This figure represents the potential maximum amount of veterans in the state that would be eligible for the proposed property tax exemption.

SCR 1005 stipulates that for a disabled veteran to qualify for the exemption, he must own (or "possess an equity interest in") the property that he lives on. This property must also be the veteran's primary dwelling place. This provision will make some of the state's disabled veterans ineligible for the exemption. In an attempt to quantify the impact of this provision, the 2005 U.S. homeownership rate of 68.9% (provided by the Census Bureau) was applied to the 57,900 potential property tax exemptees identified above. This calculation reduces the maximum number of disabled veterans eligible for the exemption to about 39,900.

As noted above, to be eligible for the exemption, the household income of the disabled veteran, or surviving spouse, is not allowed to exceed a certain amount depending on the number of children residing in the home. However, it should be noted that the definition of household income under the bill does not include certain benefits and payments, such as Social Security benefits and veterans' disability compensation and pension. This suggests that the effective or "real" income limits could be significantly higher than those prescribed in the bill. To provide some perspective, ADVS estimates that about $686 million in disability compensation and pensions was disbursed to the state's 57,900 disabled veterans in 2005. This equates to an average disability payment of slightly less than $12,000. This suggests that the "real" income limits could be at least $12,000 higher than the aforementioned amounts. After Social Security benefits are also taken into account, it is not unlikely that the "real" income limits could exceed the prescribed limits by $20,000 to $30,000. Thus, after all earnings are factored in, it is not unreasonable to assume that the effective or “real” income limits could vary between at least $50,000 and $68,000, depending on the size of the family.

Because of the narrow definition of household income under the bill, it is likely that only a relatively small number of disabled veterans will be disallowed the exemption. However, the exact number cannot be inferred from the income tax data provided by the Department of Revenue. The department does not currently compile data for specific groups, such as veterans.

While the income requirement is likely to reduce the maximum amount of potential exemptees somewhat, the 39,900 figure derived above is used as a starting point for determining what the “high end” estimate of this bill could be.

Data provided by ADVS shows the breakdown of the degree of service-connected disability among Arizona veterans. This percentage distribution was applied to the 39,900 potential Arizona property tax exemptees identified above. It was further assumed that the average assessed value of the homes owned by eligible veterans is $13,513, which is based on the statewide average full cash value for residential property of $135,132. Since the amount of the exemption is proportionate to the percentage rating of a veteran’s service-connected disability, the average exemption amount was computed for each degree of disability. Based on these calculations, the bill would generate a statewide property tax exemption of $204.6 million.

Under the Basic State Aid formula, the state pays for the cost of K-12 education not generated through local property taxes. The state also pays 37% (in FY 2008) of residential property taxes through the Arizona Department of Education (ADE) Homeowner’s Rebate program. By reducing NAV by $204.6 million, the bill will result in a direct increase of the state share of K-12 funding by about $5.0 million. This includes the net impact of both Basic State Aid and the Homeowner’s Rebate.

This NAV reduction will also generate savings in the cost of the state’s Truth in Taxation (TNT) program. TNT reduces the school Qualifying Tax Rates (QTR) to offset growth in existing property values. This reduction occurs automatically unless the Legislature decides to forego the TNT adjustment. Prior to the passage of SB 1131, the school tax rate is expected to be reduced by 11¢ in 2008, which will increase the state’s Basic State Aid cost. The 11¢ reduction was built into the FY 2008 JLBC Baseline cost estimates for ADE. By reducing NAV, the legislation would result in the tax rate reduction being 1.3¢ less than expected, which will save $6.0 million relative to the JLBC Baseline.

The proposal will also have a small impact on state General Fund revenues. Although the state property tax was repealed in 1996, the General Fund still receives property tax revenues from unorganized districts and school districts that levy the minimum qualifying tax rate. The impact cannot be determined but is expected to be small.

A definitive estimate of the legislation’s impact cannot be determined due to data limitation. With some simplifying assumptions, however, a maximum cost can be derived. The fiscal impact of this bill will also depend on whether the TNT impact is included. In the absence of a TNT adjustment, the net cost to the General Fund will be about $5.0 million. If the QTR is adjusted to account for TNT, however, the bill would have a General Fund savings of $(1.0) million. This amount reflects the net impact of a $5.0 million increase in the state’s share of K-12 funding and a $(6.0) million saving from a lower than expected tax rate reduction.

Local Government Impact

This bill would shift the tax burden to property owners not affected by this legislation and/or result in property tax losses for local governments.

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