

ARIZONA HOUSE OF REPRESENTATIVES  
Fiftieth Legislature – First Regular Session

**COMMITTEE ON WAYS AND MEANS**

Minutes of Meeting  
Monday, February 7, 2011  
House Hearing Room 1 -- 2:00 p.m.

Chairman Harper called the meeting to order at 2:00 p.m. and attendance was noted by the secretary.

**Members Present**

Mr. Chabin  
Mr. Farley  
Mr. Gallego

Mr. Gray R  
Mrs. Lesko  
Mr. Mesnard

Mr. Olson  
Mr. Vogt, Vice-Chairman  
Mr. Harper, Chairman

**Members Absent**

None

**Committee Action**

HB2207 - DPA S/E (6-3-0-0)  
HB2338 - DPA (7-2-0-0)  
HB2503 - DPA (6-3-0-0)  
HB2504 - DPA (6-2-0-1)  
HB2516 - ~~DPA~~ FAILED (4-5-0-0)

HB2552 - DPA (9-0-0-0)  
HB2557 - DISCUSSED AND HELD  
HB2564 - DISCUSSED AND HELD  
HCR2006 - NOT ASSIGNED

**TECHNICAL DIFFICULTIES OCCURRED WITH THE AUDIO.**

**CONSIDERATION OF BILLS**

**HB2552 - agricultural property tax classification; equine. - DO PASS AMENDED**

Alexander Blount, Majority Intern, stated that HB2552 modifies the statutory definition of *agricultural real property* to include land or improvements devoted to the commercial breeding, raising, boarding or training of equine (Attachment 1).

Mr. Blount explained that the Olson three-line amendment dated 2/4/11 (Attachment 2) adds equine rescue facilities registered with the Department of Agriculture (Department) to the definition of Class 2 equine property.

Chairman Harper asked if HB2552 changes the interpretation of assessments back to what it was originally. Mr. Blount stated that he is not familiar with how the Department assessed equine properties previously.

Representative Heather Carter, sponsor, stated that HB2552 clarifies statutes to include equine properties as agriculture. Representative Carter explained that equine properties are currently treated as agricultural properties and HB2552 ensures that is reflected in the Arizona Revised Statutes (A.R.S.). She asked the Members to consider that in the agriculture classifications for different types of livestock, horses are mentioned as livestock.

Representative Michelle Ugenti, cosponsor, stated her support of HB2552.

Philip Bashaw, Arizona Farm Bureau Federation, Arizona Farm Bureau, testified in support of HB2552 and the Olson amendment, stating that the Department of Revenue (DOR) includes equine in its definition of livestock and that equine property previously held a Class 2 agriculture qualification but has since been revoked and assessed as Class 1 commercial property. He stated that the result is an increase in property taxes, putting equine properties out of business.

Chairman Harper asked if HB2552 returns the interpretation of the legislation to the status prior to the County Assessor's Office change; Mr. Bashaw answered in the affirmative.

Mr. Chabin asked if there is any impact on zoning requirements; Mr. Bashaw answered in the negative. Mr. Chabin asked if there is a significant property tax shift involved. Mr. Bashaw stated that there is no tax shift and that land used for equine is traditionally assessed as Class 2 agricultural property and HB2552 would maintain that assessment.

Bas Aja, Director of Government Relations, Arizona Cattlemen's Association, testified in support of HB2552 and the Olson amendment, stating that equine is used for agricultural purposes and should be treated equitably and fairly relating to property tax assessments. He stated that HB2552 is a clarifying bill.

Chairman Harper announced the names of those who signed up in support of HB2552 but did not speak:

Robert Shuler, Arizona Horse Council  
Sean Englund, representing self  
Sharon Dorociak, representing self  
Jeannette Fish, representing self  
Elaine Arena, Arizona Thoroughbred Breeders Association  
Jose Borrajero, representing self  
Kevin McCarthy, President, Arizona Tax Research Association  
Joe Sigg, Lobbyist, Arizona Farm Bureau  
Phyllis Bunch, representing self

Chairman Harper announced the names of those who signed up in opposition to HB2552 but did not speak:

Bryan Ginter, representing self  
Keith Russell, Maricopa County Assessor  
Paul Petersen, Attorney/Assessor Representative, Maricopa County Assessor

**Vice-Chairman Vogt moved that HB2552 do pass.**

**Vice-Chairman Vogt moved that the Olson three-line amendment dated 2/4/11 (Attachment 2) be adopted. The motion carried.**

**Vice-Chairman Vogt moved that HB2552 as amended do pass. The motion carried by a roll call vote of 9-0-0-0 (Attachment 3).**

**HB2207 - special health care districts; procurement - DO PASS AMENDED S/E**  
**S/E: same subject**

Daniel Gonzalez-Plumhoff, Majority Research Analyst, stated that HB2207 requires certain services under contract with the Maricopa County Special Health Care District (District) to be procured by requests for proposals and a ranking system rather than a process that limits competition or excludes certain bidders (Attachment 4).

Mr. Gonzalez-Plumhoff explained that the Harper five-page strike-everything amendment dated 2/3/11 (Attachment 5) requires that the District adopt competitive procurement rules that are at least equal to or more stringent than those adopted by the Board of Supervisors for the county.

Mr. Mesnard asked for clarity regarding the use of the term *stringent*, and asked who would be making the decision. Mr. Gonzalez-Plumhoff stated that the language is silent regarding a definition.

Chairman Harper announced that testimony was heard on HB2207 in the previous Committee so he will not be hearing additional testimony.

Chairman Harper announced the names of those who signed up in opposition to HB2207 but did not speak:

John MacDonald, Lobbyist, Maricopa Integrated Healthcare System  
Bryan Ginter, representing self

**Vice-Chairman Vogt moved that HB2207 do pass.**

**Vice-Chairman Vogt moved that the Harper five-page strike-everything amendment dated 2/3/11 (Attachment 5) be adopted. The motion carried.**

**Vice-Chairman Vogt moved that HB2207 as amended do pass.**

Discussion ensued between Mr. Mesnard, Mr. Gallego and Chairman Harper regarding the necessity of additional testimony from John MacDonald on behalf of the Maricopa Integrated Healthcare System. Chairman Harper ruled that he will not be hearing additional testimony from Mr. MacDonald.

**Question was called on the motion that HB2207 as amended do pass. The motion carried by a roll call vote of 6-3-0-0 (Attachment 6).**

**HB2338 - special districts; secondary levy limits - DO PASS AMENDED**

Daniel Gonzalez-Plumhoff, Majority Research Analyst, stated that HB2338 establishes statutory levy limits for secondary property taxes that are levied by county library, jail and public health services districts (Attachment 7).

Mr. Gonzalez-Plumhoff explained that the ten-line Olson amendment dated 02/03/2011 (Attachment 8) removes reporting and compliance requirements related to the duties assigned to the District, county assessors and the Commission, and specifies that levy limitations imposed on county free library districts do not apply to debt service on district bonds.

Mr. Olson, sponsor, explained that the amendment applies the current levies for counties, community colleges and cities, which are limited to two-percent growth each year, to the area in statute without levy limits for maintenance and operations levies, which are special taxing districts.

Chairman Harper stated that there is no emergency measure within the bill; Mr. Olson answered that is correct.

Kevin McCarthy, President, Arizona Tax Research Association, testified in support of HB2338, echoing Mr. Olson's comments.

Mr. Chabin asked if all of the special taxing districts have a board of directors; Mr. McCarthy answered in the affirmative. Mr. Chabin asked if that includes fire districts. Mr. McCarthy stated that a bill passed in a previous Session put limitations on fire districts. Mr. Chabin asked if limitations are added to the boards of supervisors within a jail district, to address the added pressure and needs for expanded services within the existing taxing authority; Mr. McCarthy answered in the affirmative. Mr. Chabin asked where the districts go for the additional funding if needed. Mr. McCarthy stated that there is override authority in the current system that allows for additional growth; discussion ensued.

Mr. Gallego asked which states have the limits described in HB2338 in place. Mr. McCarthy stated that few states have no property tax limitations, while others have Proposition 13 in place. He further stated that other states have an Arizona tax model. Mr. Gallego asked what the override provision is in HB2338. Mr. McCarthy stated that the counties have override authority, which is used to a limited extent.

Mark Barnes, County Supervisors Association, testified in opposition to HB2338, stating that it targets four districts and that the levy limit is two percent plus new construction, which is not reliable in the current economy, making the limit severe. He stated that the County Supervisors Association needs to maintain the authority at a local level to raise revenue.

Mr. Chabin asked if counties collect fees if tax revenues do not cover expenses; Mr. Barnes answered in the affirmative.

Chairman Harper announced the names of those who signed up in support of HB2338 but did not speak:

Gretchen Kitchel, Senior Public Affairs Representative, Arizona Public Service  
Farrell Quinlan, State Director, National Federation of Independent Business  
Russell Smoldon, Lobbyist, Salt River Project  
Larry Lucero, Manager, Governmental Affairs, Tucson Electric Power Company  
Michelle Ahlmer, Executive Director, Arizona Retailers Association  
Steve Voeller, President, Arizona Free Enterprise Club

Chairman Harper announced the names of those who signed up in opposition to HB2338 but did not speak:

Barry Aarons, Lobbyist, representing self  
Bryan Ginter, representing self  
Joanne Keene, Government Relations Director, Coconino County  
Michael Racy, Lobbyist, Pima County  
Kristen Boilini, Lobbyist, Arizona Library Association  
Brenda Brown, Legislative Chair, Arizona Library Association  
Jessica Stall, Arizona Library Association

**Mr. Olson moved that HB2338 do pass.**

**Mr. Olson moved that the Olson ten-line amendment dated 02/03/2011 (Attachment 8) be adopted. The motion carried.**

**Mr. Olson moved that HB2338 as amended do pass. The motion carried by a roll call vote of 7-2-0-0 (Attachment 9).**

### **HB2503 - reduce corporate income tax rate - DO PASS AMENDED**

Daniel Gonzalez-Plumhoff, Majority Research Analyst, stated that HB2503 reduces the corporate income tax rate from 6.968 percent to 5 percent of net income (Attachment 10).

Mr. Gonzalez-Plumhoff explained that the Harper 13-line amendment dated 2/3/11 (Attachment 11) reduces the corporate income tax rate from 6.968 percent to 4.9 percent of net income by increments of .517 percent as follows:

- For Tax Year (TY) 2014, 6.451 percent of net income.
- For TY 2015, 5.934 percent of net income.
- For TY 2016, 5.417 percent of net income.
- For TY 2016 and beyond, 4.9 percent of net income.

Mr. Gallego asked if a fiscal note is attached to HB2503. Mr. Gonzalez-Plumhoff stated that a fiscal note has been requested but not drafted.

Mr. Chabin asked why an entire Special Session was devoted to this. Chairman Harper explained that Representative Carl Seel's bill is being amended to reflect agreements made during negotiations between leadership and Governor Brewer during Special Session.

Chairman Harper announced the names of those who signed up in support of HB2503 but did not speak:

Walter F. Dudley, Accountant, Arizona Society of Practicing Accountants  
Jeff Sandquist, National Association of Industrial and Office Properties (NAIOP)  
Farrell Quinlan, State Director, National Federation of Independent Business  
Heather Bernacki, Government Relations Associate, East Valley Chambers of Commerce Alliance  
Michelle Ahlmer, Executive Director, Arizona Retailers Association  
Steve Voeller, President, Arizona Free Enterprise Club  
Tom Dorn, Lobbyist, East Valley Chambers of Commerce Alliance

Chairman Harper announced the names of those who signed up in opposition to HB2503 but did not speak:

Bryan Ginter, representing self  
Suzanne Schunk, Director, Family Support Services, representing self  
Dana Naimark, President/CEO, Children's Action Alliance  
Kay Martin, Chaplain, representing self

Chairman Harper announced the names of those who signed up as neutral on HB2503 but did not speak:

Rene Guillen, Legislative Associate, League of Arizona Cities and Towns

Chairman Harper announced that he will be hearing testimony on HB2504 until Representative Carl Seel, sponsor of HB2503, is available for testimony.

#### **HB2504 - capital gains tax phase-out - DO PASS AMENDED**

Daniel Gonzalez-Plumhoff, Majority Research Analyst, stated that HB2504 subtracts individual and corporate net capital gains included in federal adjusted gross income (FAGI) from the computation of Arizona gross income (Attachment 12).

Mr. Gonzalez-Plumhoff explained that the Harper three-line amendment dated 2/3/11 (Attachment 13) removes the corporate subtraction.

Mr. Chabin asked if a fiscal note is available for HB2504; Mr. Gonzalez-Plumhoff replied in the negative but provided information from a fiscal note from the previous year from the Department of Revenue.

Chairman Harper announced that Representative Carl Seel is present to testify to HB2503 and the Committee will go back to hearing testimony on HB2503 and then resume testimony on HB2504.

#### **HB2503 - reduce corporate income tax rate - DO PASS AMENDED (continued)**

Mr. Chabin asked if a fiscal note is available for HB2503. Mr. Gonzalez-Plumhoff explained that no fiscal note is available for HB2503, but utilizing information from a fiscal note for SB1162 provided the following information for HB2503 as amended:

- Tax Year 2014, Fiscal Year 2015 - \$60 million annual impact

- Fiscal Year 2016 - \$100.4 million annual impact
- Fiscal Year 2017 - \$194 million annual impact
- Fiscal Year 2018 - \$270 million annual impact

Mr. Gallego asked what the estimated time frame is when Arizona will grow out of its current budget deficit. Mr. Gonzalez-Plumhoff stated that the net collections for corporate income taxes in the current fiscal year forecast \$674 million dollars per the Finance Advisory Committee in the January Session; discussion ensued.

Representative Carl Seel, sponsor, stated that the goal of HB2503 is to reduce the tax burden and is designed to reflect Governor Brewer's plan regarding the budget. He stated that many economic experts recognize the need to reduce taxes to promote job growth.

Mr. Chabin asked if it is Representative Seel's intention to reduce the number of Department of Public Safety (DPS) officers currently on the roads. Representative Seel replied in the negative, stating that his intention through HB2503 is to uphold the Arizona Constitution's core interests of public safety, public health, and public education by making state government more efficient and to reduce criminals in public systems such as the Arizona Health Care Cost Containment System (AHCCCS), in order to ensure that the General Fund is properly funded. Mr. Chabin asked if Representative Seel is aware that DPS has had a loss of 100 patrol officers on the roads within the last year. Representative Seel stated that he is aware that many agencies are dealing with significant budget reductions and commended DPS for finding ways to reduce in size by more than 20 percent early on in the budget crisis. Mr. Chabin stated that DPS has reduced in size, but cannot operate at the same level as it did two years prior; discussion ensued.

Mr. Farley asked if Representative Seel would be interested in supporting Representative Chad Campbell's bill that reduces loopholes in the corporate tax system. Representative Seel stated that he would review the bill and give it consideration.

Mr. Gallego stated his concern with passing legislation based on the assumption that the budget crisis will resolve and asked if passing HB2503 requires a vote of 50 percent plus one and to reverse the passing of HB2503 would require a two-thirds vote. Representative Seel stated that he is not sure about the numbers, but stated that the amendment to the bill does adjust for growth; discussion ensued.

**Vice-Chairman Vogt moved that HB2503 do pass.**

**Vice-Chairman Vogt moved that the Harper 13-line amendment dated 2/3/11 (Attachment 11) be adopted. The motion carried.**

**Vice-Chairman Vogt moved that HB2503 as amended do pass. The motion carried by a roll call vote of 6-3-0-0 (Attachment 14).**

#### **HB2504 - capital gains tax phase-out - DO PASS AMENDED (continued)**

Chairman Harper stated that the Harper three-line amendment (Attachment 13) eliminates the phase-out, phase-down of the corporate capital gains in HB2504.

Representative Carl Seel, sponsor, stated that his testimony is not necessary on HB2504, but he is available for questions; there were none.

Chairman Harper announced the names of those who signed up in support of HB2504 but did not speak:

Walter F. Dudley, Accountant, Arizona Society of Practicing Accountants

Steve Voeller, President, Arizona Free Enterprise Club

Chairman Harper announced the names of those who signed up in opposition to HB2504 but did not speak:

Bryan Ginter, representing self

Dana Naimark, President/CEO, Children's Action Alliance

Rene Guillen, Legislative Associate, League of Arizona Cities and Towns

Kay Martin, Chaplain, representing self

**Vice-Chairman Vogt moved that HB2504 do pass.**

**Vice-Chairman Vogt moved that the Harper three-line amendment dated 2/3/11 (Attachment 13) be adopted. The motion carried.**

**Vice-Chairman Vogt moved that HB2504 as amended do pass. The motion carried by a roll call vote of 6-2-0-1 (Attachment 15).**

### **HB2516 - use tax declaration - DP FAILED**

Alexander Blount, Majority Intern, stated that HB2516 requires individuals to file *use tax* returns annually on a form provided by the Arizona Department of Revenue (DOR) (Attachment 16).

Representative Matt Heinz, sponsor, stated that enacting HB2516, to couple the use tax declaration form with the annual income tax packet, will precipitate an increase in collection of an existing tax. He clarified that Arizona currently has a state sales tax and a use tax, and this is not a new tax, but a way to assist individuals with the calculation and declaration of what they owe on an annual basis. Representative Heinz stated that a fiscal note for HB2516 indicates that the bill will bring in an additional \$473,000 annually through the increased facility of collecting an existing tax liability.

Chairman Harper requested clarification, stating that an individual will be required to look at a form and declare that they do not have a use tax that was omitted in their tax filing, and that currently they do not see a form, and are not prompted to declare use taxes. Representative Heinz stated that Chairman Harper's assessment is correct.

Mr. Olson asked if an individual is filing taxes and incorrectly affirming that they have currently paid the correct taxes, would be made a felon because the average filer would not know the complexities of Arizona's use tax system. Representative Heinz stated that there would be instruction and an explanation provided by DOR, within the packets, of exactly what the use tax currently owed is and how to fill out the form. Mr. Olson stated that his concern is that when an individual makes many small purchases from Amazon.com, for example, it is difficult to

remember and keep track of those purchases accurately for filing purchases at the end of the year. Representative Heinz stated that individuals may not include every purchase, but that HB2516 is a step in the right direction toward making individuals aware that they have this existing liability.

Mr. Gray requested the cost that would be added to include these forms in the packets that DOR sends out to individuals. Representative Heinz stated that the cost would be very minimal because the materials are already distributed, so this would not create a new mailer. Mr. Gray stated that his concern is that there is no way to monitor whether or not individuals are complying.

Mr. Mesnard inquired the specific problem that HB2516 addresses. Representative Heinz stated that many individuals are not aware of any use tax liability, so including the form with instructions in DOR's packet will prompt them to comply.

Mr. Olson queried what the penalty would be for an individual who saw the form regarding use tax and forgot a purchase made previously in the year and did not report it. Representative Heinz stated that no additional penalty is specified in the bill other than the existing tax law penalties. Mr. Olson asked if filing the additional tax form is voluntary. Representative Heinz stated that it is voluntary in that DOR cannot enforce that every single filing has been done correctly.

Sean Laux, Legislative Liaison, Department of Revenue, testified as neutral to HB2516, stating that DOR does not mail tax forms to all Arizona taxpayers any longer, so an additional cost for mailing out the use tax form described in HB2516 would be accrued. He stated that HB2516 adjusts the timing that the state receives its use tax revenues and that currently most use tax revenues received are from business-to-business transactions. This shifts the burdens until April 15<sup>th</sup> onto most businesses except retailers, so an adjustment of cash flow into the General Fund will be seen.

Chairman Harper asked Mr. Laux if software companies typically produce electronic copies of new tax forms the year after a new form is introduced; Mr. Laux answered in the affirmative. Chairman Harper asked if the new requirement would be effective for calendar year 2011; Mr. Laux answered in the affirmative. Chairman Harper asked if DOR would be ready to send and then process the new forms by January of 2012; Mr. Laux replied in the negative, stating that tax forms must be ready by October 2011; discussion ensued.

Mr. Olson asked Mr. Laux to address possible penalties for filing a tax form incorrectly and not paying the required use tax. Mr. Laux stated that depending on the degree of the offense, interest and penalties are most likely on the owed amount. Mr. Olson requested the maximum penalty that could be received by an individual for not paying use tax. Mr. Laux stated that he would do research and get back to Mr. Olson.

Chairman Harper announced the names of those who signed up in support of HB2516 but did not speak:

Michelle Ahlmer, Executive Director, Arizona Retailers Association

Chairman Harper announced the names of those who signed up in opposition to HB2516 but did not speak:

Bryan Ginter, representing self

**Vice-Chairman Vogt moved that HB2516 do pass. The motion failed by a roll call vote of 4-5-0-0 (Attachment 17).**

**HB2564 - sales tax; pipes and valves - DISCUSSED AND HELD**

Alexander Blount, Majority Intern, stated that HB2564 removes the transaction privilege tax (TPT) and use tax exemption for certain pipes and valves (Attachment 18).

Mr. Farley, sponsor, stated that HB2564 eliminates one tax exemption among many, that drive up the overall tax rate. He stated that by ridding the system of tax exemptions such as the four-inch pipe exemption it will reduce the overall corporate tax rate. He stated that the four-inch pipe exemption represents about \$18.7 million a year from Arizona's tax revenues. Mr. Farley stated that if any Member would like to add an amendment to eliminate any other corporate tax exemption, he would support that amendment.

Chairman Harper stated that about half of the country pays no federal income taxes, so whenever there is a proposal to increase taxes, the burden falls on businesses. He stated that one way for the state to ensure that all individuals are paying for services etc. in state government, is to eliminate the TPT exemption on groceries.

Chairman Harper announced the names of those who signed up in opposition to HB2564 but did not speak:

Bryan Ginter, representing self

Gretchen Kitchel, Senior Public Affairs Representative, Arizona Public Service

Russell Smoldon, Lobbyist, Salt River Project

Penny Allee Taylor, Specialist of Government Affairs, Southwest Gas Corporation, in opposition to HB2564, stated that the exemption, added in 1981, was originally intended to clarify that the four-inch pipes, the valves, compressors and regulators were never intended to be taxed. She stated that if these pieces of equipment are taxed, it will be considered double taxation since the policy of the state has been to tax at the level of the last user, or where the product is put into use, where it is currently taxed. Ms. Taylor stated that if the exemption is removed, consumers would be taxed twice for that portion of the service they are using.

Mr. Farley asked if Southwest Gas sells four-inch pipes; Ms. Taylor replied in the negative. Mr. Farley asked why it would be considered double taxation to tax the vehicle by which the product gets to the consumer. Ms. Taylor stated that sales tax is collected from the consumer on the gas that comes through the pipes. She provided that when a customer purchases a computer, they pay sales tax on the entire computer and not every single part of that computer individually. Mr. Farley stated that based on the example, that computer company pays sales tax on each piece of equipment used to build that computer; discussion ensued.

Mr. Chabin asked if all industries that use pipe as a vehicle to distribute their services have exemptions on those pipes. Ms. Taylor deferred to DOR or staff, stating that she cannot speak for other industries.

Mr. Farley stated that statute clearly defines that all pipes measuring four inches and greater are exempt. Pipes measuring less than four inches are subject to tax.

Mr. Chabin asked if Southwest Gas has to pay sales taxes for motor vehicles that it purchases for business purposes; Ms. Taylor answered in the affirmative; discussion ensued.

**Chairman Harper announced that HB2564 will be held.**

### **PRESENTATION ON TRANSACTION PRIVILEGE TAX**

Kevin McCarthy, President, Arizona Tax Research Association (ATRA), provided a copy of the presentation, Arizona State and Local Sales Taxes, to the Members (Attachment 19). Mr. McCarthy stated that ATRA tracks all state and local taxes in Arizona and the top collection, if the volume of taxes is added, not withstanding exemptions, is sales tax, which is \$7.4 billion. He provided the following information regarding Arizona's tax system:

- Arizona's tax system is a three-legged stool including sales tax, property tax and income tax.
  - Arizona's three-legged tax stool saw minimal changes between 1980 and 2000.
- Arizona ranks number 6 nationally for general sales tax collections, both in state and local taxes.

Mr. McCarthy stated that Arizona's Transaction Privilege Tax (TPT) is recognized as one of the most complicated and administratively burdensome sales taxes in the United States. He also stated that Arizona's independent municipal sales tax structure dramatically increases compliance costs for both the taxpayer and the government. Mr. McCarthy stated that the TPT is a tax that measures the gross income of a company or an industry that falls into one of the many classifications that are set. He provided the following information regarding the TPT system:

- Tax on the privilege of doing business in Arizona
- Measured by gross receipts, gross income, or gross proceeds of sales
- Taxed not on activities but on the act of engaging in business
- Presumed that all gross proceeds comprise the tax base until the contrary is established
- There are 16 taxable business classifications (State):
  1. Retail
  2. Transporting
  3. Utilities
  4. Telecommunications
  5. Publication
  6. Job Printing
  7. Pipeline
  8. Private Car
  9. Transient Lodging
  10. Personal Property Rental
  11. Mining
  12. Amusement
  13. Restaurant
  14. Prime Contracting
  15. Owner Builder Sales

## 16. Commercial Lease

Mr. McCarthy provided the following information about Arizona's Use Tax:

- Imposed on the storage, use or consumption of tangible personal property purchased from a retailer or utility business
- Complement to retail and utility classifications
- Measured by purchase price

Mr. McCarthy provided the following information regarding the Model City Tax Code:

- Arizona is one of a few states in the country that allows for an independent, municipal sales tax system.
- The tax base at the city level does not mirror the state base.
- Examples of differences in codes and interpretations: Advertising, Speculative Builders, Rental Occupancy, Food, Commercial Leases.
- Interpretation of exemptions is a major issue.
- Independent municipal system has created significant administrative and compliance issues for taxpayers in Arizona.

Mr. McCarthy stated that the total FY 2010 state and local sales tax collected for Arizona is \$4,858,187,467, and of that, \$900 million is shared with cities and towns.

Mr. McCarthy provided the following average sales tax rates for Arizona:

### 1980 - Retail

- State Rate: 4 percent
- Average City Rate: 1.2 percent
- Total Average Rate: 5.2 percent

### 1990 - Retail

- State Rate: 5 percent
- Average City Rate: 1.6 percent
- Average County Rate: 0.5 percent
- Total Average Rate: 7.4 percent

### 2010 - Retail

- State Rate: 6.6 percent
- Average City Rate: 2.4 percent
- Average County Rate: 0.7 percent
- Total Average Rate: 9.7 percent

Mr. McCarthy stated that the following major issues face Arizona:

- Ongoing challenge to create greater uniformity in state and city sales tax base
- Continued movement of cities out of the state collection system creating higher compliance costs
- The League of Cities and Towns encouraging cities to leave the state system and contract out collection and audit functions to Revenue Discovery Systems (RDS)
- Approaching upward limit on rates

Michelle Ahlmer, Executive Director, Arizona Retailers Association, provided the Members with a copy of the 2008-2010 State Budget Gaps Estimates to accompany her presentation (Attachment 20). Ms. Ahlmer stated that there are 35 states that collect some form of sales tax and of those 35 states, four of them, including Arizona, cost more to collect than the remaining 31 states combined.

Ms. Ahlmer provided one example of Arizona's complicated sales tax system, Southwest Gas. She stated that Southwest Gas does not supply service to the entire State of Arizona, but it does provide service to all of Nevada. She stated that in Nevada, Southwest Gas writes nine monthly sales tax collection checks, and in Arizona it writes 1,100; she stated that this is a burden to companies doing business in Arizona.

Ms. Ahlmer stated that Arizona will have an estimated \$708.6 million in uncollected sales tax revenue in FY 2010, partly due to online only retailers that are not collecting sales taxes. She stated that creating a more uniform base to the sales tax system is a significant step toward recovering those lost revenues. Ms. Ahlmer stated that in addition, the *fairness issue* is significant. She explained that Arizona businesses are losing sales to retailers such as Amazon.com that do not collect sales tax. Arizona's businesses are required to collect sales tax.

Mr. Olson asked Ms. Ahlmer to provide more information about the Streamlined Sales Tax and Use Agreement among 12 states. Ms. Ahlmer stated that there are actually 24 states involved in a voluntary participation by a group of tax administrators who go to the project meetings. She stated that the states that are fully compliant with the Streamline Sales Tax and Use Agreement have collected a total of \$380 million. She stated that the agreement is a living, breathing document that is continuously being revised. Mr. Olson asked if the states that adopt this agreement have a single point of contact for the collection of sales tax; Ms Ahlmer stated that is correct and clarified that the businesses within those 24 states would write only one check to each of the states. Discussion ensued.

Mr. Chabin asked if Arizona law would have to conform to reflect one local sales tax rate, in order to comply with the Streamlined Sales Tax and Use Agreement; Ms. Ahlmer replied in the affirmative, stating that there would be one sales tax rate for food and one for other merchandise and all cities would have the same rate. Mr. Chabin stated that due to local choice, each city decides where taxes are applied. He asked if this streamlining would allow for a local rate to be collected, which is then distributed to cities and counties, while leaving intact the existing local rates. Ms. Ahlmer replied in the negative, stating that the more layers added to the sales tax system, the more complicated compliance becomes.

### **HB2557 - sales tax on medical marijuana - DISCUSSED AND HELD**

Daniel Gonzalez-Plumhoff, Majority Research Analyst, stated that HB2557 creates a nonprofit medical marijuana dispensary transaction privilege tax classification and imposes a transaction privilege tax (TPT) and a use tax on dispensaries (Attachment 21).

Mr. Gonzalez-Plumhoff explained the Farley 14-line amendment dated 02/04/2011 (Attachment 22).

Mr. Farley, sponsor, stated that HB2557 is an important bill to consider, given the nature of Arizona's deficit, and the difficulty of the decisions regarding the deficit. He stated that the estimates that he has received regarding the cost of obtaining marijuana on the streets is between \$80 and \$100 an ounce, which can produce between 60 and 120 joints, depending on the strength of the marijuana. Mr. Farley stated that at dispensaries, the cost will be between \$350 and \$450 per ounce. He stated that the Attorney General's Office estimates revenue with a 100 percent sales tax on marijuana would be approximately \$600 million dollars annually. He stated that the 100 percent tax would make a \$4 joint an \$8 joint, but that money would be used not only to solve some of the fiscal crisis of the state, but also for ensuring that the product people are buying is free from pesticides and is medical grade product.

Mr. Chabin asked if Mr. Farley is amenable to amending his bill to lessen an increased financial burden on medical users. Mr. Farley stated that he is open to discussion regarding the concern.

Mr. Mesnard asked if drugs and medications are currently taxed. Mr. Farley stated that over-the-counter medication is currently taxed, but prescription medication is not currently taxed. He stated that medical marijuana is not accepted by the Food and Drug Administration and is not considered a prescription medication. Mr. Mesnard asked if this would be taxed with a standard sales tax; Mr. Farley responded in the affirmative.

Mr. Olson asked if marijuana is currently illegal under the Controlled Substance Act; Mr. Farley replied in the affirmative. Mr. Olson asked if there is currently any other drug that is taxed that falls under the Controlled Substance Act; Mr. Farley replied in the negative.

Mr. Harper stated that previously, the Legislature passed a law that made income derived from drug trafficking subject to income tax.

Discussion ensued regarding the appropriateness of taxing medical marijuana.

Jay Fleming, representing self, testified in opposition to HB2557 as a member of Law Enforcement Against Prohibition, stating that he recognizes the appropriateness of the need to tax medical marijuana, but stated that need must be balanced with the need to protect patients.

Mr. Chabin asked what the cost of a single joint is on the streets. Mr. Fleming stated that an ounce of Mexican cartel marijuana costs between \$80 and \$100, but from a dispensary, the cost ranges from \$300 to \$400 an ounce. Discussion ensued regarding the federal limits on plants per dispensaries and ounces that must be produced per plant.

Chairman Harper stated that the price of the product will be whatever the market will bear and that the state government will do whatever it can to lower prices in order to stay competitive with the cost of the illegal marijuana.

Andrew Myers, Executive Director, Arizona Medical Marijuana Association, testified in opposition to HB2557, stating that it is full of unintended consequences. He stated that a dispensary cannot take regular business deductions because under federal law marijuana is still an illegal substance. He stated that the dispensaries are taxed on gross income and not on operating profit as other businesses, making it extremely difficult for dispensaries to produce at a rate less than \$300 an ounce. He stated that patients will not pay an increase of that proportion in

order to obtain the same product that they can obtain on the streets. He stated that patients, who already have cards permitting possession of marijuana for medical use, will not be arrested if caught with the drug, and will not be willing to pay hundreds of dollars in a premium to have a legal access point to purchase the drug.

Chairman Harper asked if the 100 percent sales tax markup is automatically proper without legislation. Mr. Myers stated that an Attorney General ruling was that medical marijuana sales are subject to standard TPT without any action by the Legislature. Chairman Harper asked if the Arizona Medical Marijuana Association would concede that point; Mr. Myers answered in the affirmative.

Mr. Myers continued his presentation stating that Arizona should not be balancing the budget on the backs of medical marijuana patients.

Mr. Myers answered questions regarding the following:

- varying levels and quality of marijuana available on the illegal market
- illegal market prices compared to dispensaries
- a possible mandate for testing produced by the Arizona Medical Marijuana Association by the Department of Health Services
- the costs associated with growing medical marijuana

**Chairman Harper announced that HB2557 will be held.**

Without objection, the meeting adjourned at 5:20 p.m.

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Charly Laube, Committee Secretary  
March 4, 2011

(Original minutes, attachments and audio on file in the Office of the Chief Clerk; video archives available at <http://www.azleg.gov>)