Fiscal Note

BILL # HB 2552 **TITLE:** agricultural property tax classification; equine

SPONSOR: Carter **STATUS:** House Engrossed

PREPARED BY: Hans Olofsson

Description

According to the Department of Revenue's (DOR) Agricultural Property Manual, real property that is used primarily for equine (term refers to horses, mules, and burros) boarding or training, or for breeding equines for recreational use is considered commercial property and as such is assessed under Class 1, which uses a 20% assessment ratio. By contrast, real property that is used for the breeding of selective livestock for agricultural purposes, including equines, is considered agricultural property and assessed under Class 2, which uses a 16% assessment ratio.

HB 2552 would provide that all land and improvements devoted to commercial breeding, raising, boarding or training of equine be valued as agricultural property and assessed under Class 2. Additionally, the bill would also expand the definition of agricultural property to include equine rescue facilities registered with the Arizona Department of Agriculture.

Estimated Impact

HB 2552 could have a potential General Fund cost of $419,000, beginning in FY 2014. The bill would reduce statewide net assessed valuation (NAV), which increases the state's K-12 education formula cost. However, the fiscal impact associated with the NAV loss could be mitigated by offsetting savings resulting from automatic school tax rate adjustments under the state's truth-in-taxation (TNT) provisions. If the TNT savings are incorporated, the net General Fund cost would be an estimated $126,000, beginning in FY 2014. (Note that under the state's valuation statutes, the impact of HB 2552 would not be reflected on the tax rolls until the fall of 2013, or FY 2014 for budgetary purposes.)

Analysis

According to information provided by the county assessors of Cochise, Maricopa, Navajo, and Yavapai Counties, the expanded definition or agricultural real property under the bill would not only reduce the assessment ratio from 20% to 16%, but also result in a different valuation method than that applied to properties determined to have commercial uses. Unlike commercial properties, which are valued based on market value, agricultural property values are determined based on a statutory valuation method known as the "income approach." According to the county assessors, under the income approach where a property's value is based on the income it is expected to produce, a parcel's full cash value is significantly less than a comparable property valued under a market-based approach. For example, an analysis prepared by the Maricopa County Assessor's Office for a specific school district within the county shows that the bill could potentially reduce the district's full cash value from $42 million to $11 million. (While the other counties have not yet produced any estimates of the loss in full cash value, they all believed that the impact could be significant.)

Maricopa's estimated full cash value reduction translates into a NAV loss of $6.64 million [$42 million x 20% minus $11 million x 16%]. Since Maricopa's NAV represents 63% of the statewide total, this analysis assumes that the potential NAV loss for the state as a whole would be about $10.5 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 40% of residential school property taxes through the Department of Education's Homeowner's Rebate program. By reducing NAV by $10.5 million, the bill would result in a direct increase of the state share of K-12 funding by $419,000, beginning in FY 2014. This estimate includes the net impact on both Basic State Aid and the Homeowner's Rebate.

The fiscal impact may be mitigated by the state's Truth in Taxation (TNT) program. TNT changes the qualifying tax rate (QTR) and state equalization tax rate (SETR) to offset growth (or decline) in existing property values. These rate changes occur automatically unless the Legislature decides to forego the TNT adjustment. For example, under current law, the QTR

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is expected to be reduced by 0.4¢ in FY 2014. The lower NAV under HB 2552, however, would result in the tax rate reduction being 0.1¢ less than under current law, or 0.3¢, which yields a TNT savings of $293,000.

As noted above, the fiscal impact of this bill depends on whether the TNT impact is included or not. In the absence of a TNT adjustment, it is estimated that the cost to the General Fund would be $419,000, beginning in FY 2014. However, if the QTR and SETR are adjusted to account for TNT, the bill's General Fund cost would be reduced to $126,000.

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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