

An Arizona Revenue and Tax System for a Competitive 21st Century Economy: Report Overview

The main report goals are to:

- Analyze Arizona's fiscal structure and economic infrastructures, relative to key states against which Arizona must compete for 21st Century prosperity.
- Evaluate Arizona's current revenue system in light of widely accepted criteria for high-quality revenue/tax systems.
- Develop revenue-neutral reform proposals (consistent with the same widely accepted criteria) to replace Arizona's defective system.
- Evaluate the proposals in light of the long-term interests of Arizona as a whole.
- Provide options that *might be* politically feasible (rather than theoretically "ideal", but politically impossible).

Arizona's current revenue/tax system is defective for a number of reasons that are problematic for Arizona's competitive position in the 21st century economy. Thus, broadly based rather than piecemeal reform is the only reasonable approach for substantial improvement. Needless to say, any system reform entails costs and benefits. Because these proposals are intended to benefit Arizona as a whole, some interest groups will object to certain aspects of the reform proposals. There surely are proposal elements that will raise objections from both "conservative" and "liberal" political camps, but they likely will support other elements. Nonetheless, the key is to view the proposals as a package—not individual pieces—for improving Arizona's overall revenue/tax system. Broadly based reform, along the lines of the following proposals, is crucial for both fiscal responsibility and Arizona's prosperity in the 21st century.

Many factors are involved in becoming a leading 21st Century economy, including a comprehensive overhaul of Arizona's state and local revenue system that emphasizes the following: 1) a greatly simplified system, 2) a substantially broadened tax base, 3) lower tax rates, 4) expansion of user fees, 5) low-income tax relief, and 6) lower and fairer business taxes. The vitality of Arizona's economy depends importantly on the structure of its revenue system, because the competition for increasingly mobile businesses, workers, and citizens is at least nationwide.

The following overview highlights some key report findings, summarizes widely accepted criteria for a high-quality revenue system, and uses those criteria to evaluate Arizona's current revenue system and to propose comprehensive reforms. The report chapters and appendices provide detailed data and analysis to support the summary highlights, as well as other facts and analysis not summarized in this overview.

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How Does Arizona Match Up With Its Competitors?

Because Arizona must compete nationally to become a leading 21st Century economy, this report views Arizona in a national context, rather than in isolation. Although the competition to attract quality workers and jobs is national in scope, this report selects sixteen states for detailed comparisons. For comparability, these comparisons use U. S. Census Bureau data, so data for 2000 are the most recent available for this report. The states selected—referred to as Competitor States—are Arizona’s direct competitors for prosperity in the 21st Century:

California	Georgia	Nevada	Texas
Colorado	Maryland	New Jersey	Virginia
Connecticut	Massachusetts	New Mexico	Utah
Florida	Minnesota	Oregon	Washington

Perhaps surprisingly, Arizona ranked among the lowest of the Competitor States in output—Gross State Product (GSP)—produced per person in 1982, 1992, and 2000, as shown below.

	<u>1982</u>	<u>1992</u>	<u>2000</u>
Arizona Output (GSP in 2000 \$) per Person.....	\$19,249	\$23,487	\$29,712
> Competitor States with Higher Output.....	16 of 16	15 of 16	14 of 16
> Competitor States within 17% of Arizona's Output....	7 of 16	5 of 16	3 of 16

How did Arizona fall behind, given that its population and employment growth were among the very highest in the nation over the last three decades? The reason, of course, is that only growth in high productivity jobs delivers rapidly rising living standards. Arizona’s job-growth engine has delivered high quantity, rather high-quality job growth. Thus, Arizona’s per capita GSP has fallen behind that of the Competitor States over the last three decades.

The report’s detailed benchmark comparisons with Arizona’s Competitor States reveal that, **as a percentage of total state output (Gross State Product):**

- Generally, Arizona ranks near the average for total revenue and expenditures.
- From 1972 to 2000, Arizona’s relative position changed from above average revenue collections and expenditures to below average.
- The change in Arizona’s relative position was especially large in recent years (1992 to 2000), as the compound annual growth in revenues averaged 1.58% less in Arizona than in the Competitor States.

The report’s detailed benchmark comparisons with Arizona’s Competitor States reveal that, **on a per capita basis:**

- Generally, Arizona ranks well below the average for the Competitor States in both revenues and expenditures.

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- Arizona's per capita revenue collections were lower than those in any of the 16 Competitor States in 1972, 1992, and 2000.
- In 1972, Arizona spent considerably more on education than the average spending in the Competitor States.
- By 2000, Arizona spent substantially less on education than all but two of its 16 Competitor States, despite the fact that one key feature of a competitive economy is a strong educational system.
- Arizona consistently ranks well below the average spending on health and welfare by the Competitor States—lower than the spending in at least 15 of its 16 Competitor States in both 1972 and 2000.

Arizona's currently low rankings for spending on education are matched by low rankings on educational outcome measures. **Arizona's national rankings reveal that:**

- Arizona's per capita spending on education (K12 and higher education) was 8th in 1972, and 24th in both 1982 and 1992.
- Arizona's per capita spending on education (K12 and higher education) had fallen to 47th by 2000.
- Arizona's high school graduation rate was 47th in 2001.
- Arizona's percentage of its population over 25 years of age with at least a bachelor's degree ranked 30th in 2001.

In the knowledge economy of the 21st Century, policymakers face a stark choice: substantially increase Arizona's public investment in education—an expensive proposition, especially because Arizona is a relatively low-income state—or accept continuing deterioration in the state's competitive position. Needless to say, a world-class educational system and a sensible state revenue system are only two ingredients for success. But they are major ingredients that can be affected directly by Arizona's policymakers. Because the policy decisions on funding levels for a competitive infrastructure are beyond the scope of this report, the primary focus is on an improved revenue system for funding whatever level of spending is chosen by Arizona's citizens.

Grading Arizona with Criteria for a High-Quality Revenue/Tax System

Specific criteria for a high-quality revenue system are widely accepted among scholars and policymakers, and some of which can be traced back to Adam Smith's, The Wealth of Nations (1776). Thus, relying on extensive literature, this report derives three Primary and twelve Supporting Principles for evaluating the quality of Arizona's overall revenue system. A high-quality system must satisfy the three Primary Principles, but the twelve Supporting Principles require policymakers to make some tradeoffs because the Supporting Principles are closely interrelated but sometimes conflicting.

Primary Principle A: Adhere to Widely Accepted Theories of Taxation

The first five Supporting Principles sum up major features of the economic and public finance views of taxation.

1. Equity or “Fairness” to taxpayers is essential, especially equal treatment for those in similar circumstances. A subjective element of “fairness” suggested by many is adopted for this report—the **overall system should not be regressive** (in a regressive system, taxes represent a higher percentage of the incomes of low-income than of high-income persons).

Fairness is difficult to achieve in the context of Arizona’s currently complex system. Equal treatment of those in similar circumstances is problematic in a system that includes so many exceptions, credits, and ad hoc tax benefits for some business taxpayers but not others. The current system also is regressive.

2. The overall system should be fair, effective, and efficient, largely by adhering to the other principles.

The current system has deteriorated due to the plethora of exemptions and credits introduced over the years. Probably because the nominal tax burden on business is relatively high, policymakers make special deals to attract business expansion. The result is further complexity and less fairness.

3. Avoid tax distortions, to the extent possible (recognizing that all taxes tend to change economic behavior).

Tax distortions can be minimized, within limits, by using low marginal tax rates on a broad tax base and including an effective system of user fees. Arizona’s tax base—especially for sales/use taxes and income taxes—is too narrow. Arizona also relies too heavily on tax revenue because of underutilized user fees.

4. Direct beneficiaries should pay for some services, as feasible and in light of equity concerns.

As of 2000, Arizona ranked last in the nation for user fees, charges, and miscellaneous revenue. As a result, many services that could be paid for by users instead are subsidized from general tax revenues. This implies that some services undoubtedly are “overused” because they are under-priced, increasing public use. In turn, higher funding levels to support such services add to the overall distortion of the tax system by requiring more tax revenue.

5. A broad tax base with the low rates is desirable.

In general, Arizona’s tax base has been narrowed by many exemptions, credits, and special deals for business. The tax base could be broadened and tax rates lowered across the board by eliminating most tax exemptions/credits/special deals and by appropriately pricing/expanding user fees for many services now subsidized by taxpayers.

Primary Principle B: Ease of Administration

Supporting Principles 6 through 9 relate to the administrative concerns and accountability features of a high-quality revenue system.

6. Consider **complementary Intergovernmental features** to create a cohesive fiscal system that is fiscally sound at all levels of government.

State and local policy decisions often do not view the revenue system as an integrated whole, resulting in less than optimal decisions for the system as a whole. Property taxes are extremely complex because of many differences among taxing jurisdictions. System complexity is compounded by caps in state law on collections and legislated refunds for homeowners that together create unusual incentives for local property tax initiatives.

7. The tax system should have **High compliance rates and low compliance costs.**

Complexity in Arizona's system reduces taxpayer compliance rates and increases compliance costs for both taxpayers and tax collectors.

8. The revenue system normally should entail **independence from spending decisions** to maintain fiscal flexibility.

Arizona has a history of misusing tax credits and exemptions to direct resources to particular purposes (alternative fuels is perhaps the most notable example). A related problem arises from earmarked expenditures that have no identified funding sources. These problems restrict legislators' ability to administer appropriate fiscal policy, especially in unexpected situations or in the case of a revenue shortfall.

9. The system should be **transparent and accountable to taxpayers.**

Complexity and multiple exemptions/credits/special deals reduce the possibility that taxpayers can monitor the overall system. Arizona publishes an expenditure budget, but it does not publish a detailed revenue budget that allows citizens to monitor tax "expenditures." Thus, it is nearly impossible to determine the extent to which policymakers spend taxpayer funds through the various tax breaks, exemptions, and special deals.

Primary Principle C: Ability to Foster Economic Growth

The prosperity of a state can be approximated by the level and growth of the state's output of goods and services, referred to as gross state product (GSP). A pro-growth fiscal environment must not have excessive taxes, but it also must include quality infrastructure features, such as quality education, hospitals, roads, and public safety. Supporting Principles 10, 11, and 12 aim for an adequate revenue system to support critical services and necessary infrastructure investments, while protecting/enhancing Arizona's competitive position.

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10. Reliability and certainty through time and over the business cycle are essential for sound fiscal planning.

Arizona's overall revenue system is highly unreliable, as especially highlighted by large fluctuations in revenue streams for Fiscal Years 2000-2004. The Corporate Income Tax is an extremely volatile revenue source. Also, Arizona exempts many services and all food for home consumption from the sales tax base, thus narrowing the base and making the revenue stream even less reliable. User fees are a usually reliable revenue source, but they are underutilized in Arizona.

11. Balance among system revenue sources is important.

Arizona's balance is similar to many states, but Arizona does an especially poor job in collecting user fees to cover the costs of many services (shifting the funding burden of such services to tax revenue). Narrow bases for income and sales taxes and underutilization of fees/charges reduce system balance.

12. To the extent possible, Arizona's Competitive position should be protected/enhanced by the overall revenue system.

Arizona scores especially low on this dimension because of the relatively high (*stated or nominal*) tax burden on business, especially given that Arizona's infrastructure funded by its revenue system is not competitive with other states. Probably because the nominal tax burden on business is relatively high, policymakers often make special deals to attract business expansion. The result is further complexity and less fairness, without addressing Arizona's fundamental competitive disadvantage that results from a relatively high (nominal) tax burden on business.

A Plan for Improving Arizona's Overall Revenue System

Arizona needs to upgrade its infrastructure to effectively compete in the 21st Century, yet the exact level of spending required is a policy decision. Thus, the baseline reform proposals are for revenue-neutral changes, with the FY 2003 revenue level as the starting position. Arizona's current revenue system is fundamentally flawed, so the proposals are for comprehensive rather than piecemeal reform. The proposals view revenues for state and local governments at three levels:

- The State's General Fund revenues.
- All State revenues, fees, and charges, including the local property tax revenue raised as a direct result of State mandates to fund education.
- All State and Local revenues, fees, and charges.

The proposals focus on the percentages of revenue raised from the various sources, but dollar estimates also are provided to anchor orders of magnitude. The revenue numbers and estimates are based on Arizona's JLBC figures, simulations by 21st

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Century Business Tools, estimates from Arizona's Department of Revenue, and estimates from Arizona's 2003 Citizens' Finance Reform Commission. Arizona's current and improved revenue compositions are reported on the following page (Table 7.2 in the report). The main features of these revenue-neutral changes are summarized below.

Sales Taxes. Sales tax rates are lowered by expanding the tax base to include personal services, food for home consumption, a select number of "domestic/local" business services, casual (used) private auto sales, and construction services provided in prime contracting. A modest real estate transfer fee of .0035 of the value of the real estate transaction, which is commensurate with the other service functions, is included. The net result of these proposals is illustrated by the following changes in the target shares for sales/use taxes:

- For the General Fund, from about 50% to 60% of the total.
- For Total State revenue, from about 44.5% to 50% of the total.
- For State and Local Combined revenue, from about 36% to 40% of the total.

Individual Income Taxes. The proposed income tax base is broadened and simplified by eliminating most exemptions, deductions, and credits. Any remaining deductions should be for general and well understood policy purposes. The broadened base makes it possible to reduce tax rates across the board. The magnitude of the income tax relief—an estimated \$460 million—can be illustrated by the following changes in the target revenue shares for personal income taxes:

- For the General Fund, from about 34% to 27% of the total.
- For Total State revenue, from about 18% to 14% of the total.
- For State and Local Combined revenue, from 11% to 9% of the total.

Because the reliance on sales taxes increases, the proposed plan targets most—if not all—of the \$460 million in personal income tax relief for those at the bottom of the income distribution to offset the regressive nature of other parts of the system, including the sales tax on food for home consumption. In the end, the broadening of the sales tax helps "fund" income tax reductions that would make Arizona's overall revenue system far more progressive than the current one.

Eliminate or Substantially Reduce Corporate Income Tax. The proposed changes reduce the aggregate corporate liability by one-half (\$180 million). However, since many corporations currently pay no tax, this proposal results in a considerable shift in the burden on corporations, with sharp reductions for firms with historically high tax liability and modest increases for those that historically have paid little or nothing. The proposals for a franchise fee or modified corporate income tax involve:

- A much broader base and much lower marginal tax rates (about one-half lower) for all current and prospective filers.

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Revenue Neutral Simulations

Current Picture							
	Percentages			Dollars (Billions)			
	General Fund	Total State	State and Local	General Fund	Total State	State and Local	
Sales	49.83%	44.53%	36.31%	Sales	\$3.03	\$5.28	\$6.89
Indiv	34.55%	17.71%	11.07%	Indiv	\$2.10	\$2.10	\$2.10
Corp	6.41%	3.29%	2.05%	Corp	\$0.39	\$0.39	\$0.39
Prop	0.00%	16.01%	21.97%	Prop	\$0.00	\$1.90	\$4.17
Other	9.21%	18.46%	28.60%	Other	\$0.56	\$2.19	\$5.43
Total	100.00%	100.00%	100.00%	Total	\$6.08	\$11.86	\$18.98

Improved							
	Percentages			Dollars (Billions)			
	General Fund	Total State	State and Local	General Fund	Total State	State and Local	
Sales	60.00%	50.00%	40.00%	Sales	\$3.65	\$5.93	\$7.59
Indiv	27.00%	13.85%	8.65%	Indiv	\$1.64	\$1.64	\$1.64
Corp	3.00%	1.55%	0.95%	Corp	\$0.18	\$0.18	\$0.18
Prop	0.00%	13.70%	18.65%	Prop	\$0.00	\$1.63	\$3.54
Other	10.00%	20.90%	31.75%	Other	\$0.61	\$2.48	\$6.03
Total	100.00%	100.00%	100.00%	Total	\$6.08	\$11.86	\$18.98

Recommended Changes							
	Percentages			Dollars (Billions)			
	General Fund	Total State	State and Local	General Fund	Total State	State and Local	
Sales	10.17%	5.47%	3.69%	Sales	\$0.62	\$0.65	\$0.70
Indiv	-7.55%	-3.86%	-2.42%	Indiv	-\$0.46	-\$0.46	-\$0.46
Corp	-3.41%	-1.74%	-1.10%	Corp	-\$0.21	-\$0.21	-\$0.21
Prop	0.00%	-2.31%	-3.32%	Prop	\$0.00	-\$0.27	-\$0.63
Other	0.79%	2.44%	3.15%	Other	\$0.05	\$0.29	\$0.60
Total	0.00%	0.00%	0.00%	Total	\$0.00	\$0.00	\$0.00

Note: This table is Table 7.2 in the report. The **General Fund** numbers are taken directly from the JLBC appropriations report for FY 2003 (excluding any one-time revenue enhancements). **Total State** collections are estimated from Census data, allowing the 2000 census figures to grow at the same rate as total TPT collections from 2000 to 2003. The Total State figures also include local property tax money earmarked for funding State education initiatives and the effects of proposition 301. **State and Local** combined revenues are estimated from Census data by using the same growth factor used for estimating the **Total State** numbers.

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- A new minimum fee or tax of \$250.00 per year on all partnerships, LLCs, C-Corps, and S-Corps that would generate approximately \$35 million per year.
- The elimination of virtually all corporate income tax credits, even if phased in over a long period (because of large adjustment costs for currently favored corporations).
- The resulting franchise fee/corporate tax burden would be among the lowest in the nation, with low marginal tax rates and far fewer tax distortions due to the elimination of ad hoc credits/exemptions.

Property Taxes. Arizona's current property tax maze should be greatly simplified, and uniformly trained assessment professionals should be used throughout the State. The proposal includes major property tax relief of \$630 million at the combined State and Local level. The proposal targets the property tax relief mainly for owners of business property, but delivers broad based relief as well. The proposal realigns the reliance on the property tax as follows:

- For the General Fund, no change, at 0%, unless a statewide property tax for education replaces a large portion of local property taxes for education.
- For Total State revenue, from about 16% to 14% of the total.
- For State and Local Combined revenue, from 22% to 19% of the total.

Again illustrating the need to view reform comprehensively, maintaining revenue neutrality requires offsetting reduced property taxes with increases in either sales taxes or fees and miscellaneous revenues.

Miscellaneous Fees and Charges. According to Census data for 2000, Arizona ranks last among the states (combined State and Local level) in per capita revenue for this category. Analysis suggests that General Fund tax revenue—via revenue sharing transfers to local governments or appropriations to State agencies—currently subsidizes areas that should be funded by charges paid by the direct beneficiaries. Other States, including Arizona's Competitor States, assess far higher fees.

The proposal includes a substantial increase of about \$600 million in fees and miscellaneous revenue (net of associated cost increases for improved service). The target shares for this revenue source change as follows:

- For the General Fund, from about 9% to 10%.
- For Total State revenue, from about 18.5% to 21% of the total.
- For State and Local Combined revenue, from about 29% to 32% of the total.

For perspective, this increase would increase Arizona's rank for miscellaneous fees and charges from last among the states to about 37th.

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Changing Revenue Levels from Revenue-Neutral Plan. Changing revenue levels from the revenue-neutral plan can be accomplished easily, as follows:

- As just noted, user fees could be increased considerably more than is included in the base proposal. Also, the state could increase the reliance on “indexed” user fees that grow with Arizona’s overall economy. Then, tax rates could be adjusted down to partially or fully offset the increased flow from user fees, depending on whether the objective is to increase or decrease total revenue.
- With the new plan in place, it would be easy to modestly raise or lower rates on any or all of the tax sources to obtain the desired revenue changes.
- A third way would be to implement all of the proposals for broadening the sales tax base, accompanied by the appropriate changes in rates to increase/decrease the total revenue flow.

Other Features of a High-Quality System

Other features of a high-quality system include:

- Detailed revenue budgets.
- “Rainy Day” funds.
- Avoiding customized tax incentives for individual businesses.
- Avoiding misguided limits on revenues and expenditures.
- Bonding for school construction.
- Reviewing the use of federal funds.
- Balancing taxes and critical Infrastructure needs.

Revenue Budget. It is essential that Arizona enact and follow an “open records” law that requires annually published disclosures of complete revenue budgets. These reports should include figures on the revenues *not* received because of exemptions, credits, and all other special deals, including the continuing costs of any “one-time” tax breaks. A detailed budget is required to assure accountability to Arizona’s citizens.

Rainy Day Fund. The State should adopt a 10-year fiscal period to plan for a well-funded Budget Stabilization fund. An amount approximately at the original 1990 statutory level of 15% of the General Fund probably is a prudent balance for the fund. History suggests that, after funding the BSF, “windfalls” in revenue should be rebated to taxpayers in “one-time” tax rebates or spent on “one-time” projects. Making permanent commitments, based on temporary revenue surpluses, is not sound financial planning—as shown by the fiscal mistakes of the 1990s that largely led to the fiscal crisis faced by the State for the 2002-2004 fiscal years.

Avoid Customized Tax Incentives for Individual Businesses. Some make the simplistic argument that Arizona should adopt a policy of targeted tax relief for “export-based” firms and for firms with relatively mobile capital. Such proposals,

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whether intentionally or not, actually are attempts to resurrect the *failed* Mercantilist notions of the 17th-19th Centuries. If Arizona or any other state attempts to create an industrial policy of targeted tax relief—rather than general fiscal reform—it runs the risk of:

- Picking the wrong targets for subsidies, as governments are prone to do, in response to intense and expensive lobbying efforts.
- Ignoring the correct targets, as governments are prone to do, often because the targets are unknown to even the most informed citizens, politicians, and economic development professionals, especially in a world of dynamic technological change.
- Imposing a stifling tax burden on the owners of “un-favored” businesses, thus inhibiting their expansion.
- Not having an adequate tax base to competitively fund the services and infrastructure investments crucial for quality business expansion, especially in the knowledge economy of the 21st Century.

Avoid Misguided Limits for Revenues and Expenditures. Limiting the growth of government is politically appealing and intellectually sound, when properly implemented. But correctly choosing such a limit is vital. Some claim that government should be tied to the rate of growth in population plus inflation. That proposal is referred to as the Taxpayer’s Bill of Rights (TABOR), and it actually has been proposed in the Arizona legislature and enacted in Colorado. However, this report shows that the proponents of this superficially appealing notion either are misguided or they intend to implement a policy that ultimately would virtually eliminate the government sector.

Bond School Construction. Financing school construction with bonding or current funds is essentially a capital budgeting question akin to the investment decisions made in the private sector on a daily basis. Efficient capital budgeting also applies to school finance, even though schools do not (directly) provide net revenues. Debt financing is appropriate because schools do yield future benefits that extend far beyond the year in which the school is constructed.

Review Use of Federal Funds. Federal funds are a major source of revenue for all states, but these funds are not shown in this overview. Nonetheless, state and local governments should undertake a careful review of all major federal fund sources to make sure that federal sources are utilized efficiently and to ensure that Arizona taxpayers are not fully funding programs that instead could rely on federal funds.

Balancing Taxes and Critical Infrastructure Needs. Arizona faces some large challenges in reaching the qualities of the infrastructures and workforces found in many of its Competitor States. Once a state reaches a critical mass of quality investments and

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job opportunities, it is much easier to maintain momentum than it is to get to that critical mass initially. Because Arizona clearly has not reached that critical mass, as shown by the comparisons of economic growth in this report, the implication is that the state must spend and invest even more just to “enter the game.” This is a daunting challenge because entering this highly competitive and dynamic game will be expensive, but not entering it probably precludes a prosperous future for Arizona.

Why Proposed System is Superior

Although the percentage changes in the distribution among state and local sources in the proposed plan are not large ones, the changes are important, especially when combined with the other reforms. The proposed system would be superior to Arizona’s currently flawed revenue system for many reasons:

Simpler. It is a much simpler system, with most credits, exemptions, and special deals eliminated.

More Balanced. It is a more balanced system in relying on broader tax bases and more user fees.

Improved System Efficiency. It makes taxes easier to administer and more difficult to avoid. A broader base, lower rates, and increased user fees reduce the economic distortion of taxes.

Increased User Fees. More services are paid for by the direct users of those services than by taxpayers as a whole. This shift from taxes to fees for services makes possible tax relief for all taxpayers through lower rates, specific tax relief for low-income groups, and a reduced tax burden for businesses.

Fairer for Persons with Lower Incomes. It delivers massive tax relief for low-income persons, and it offsets the regressivity in the current system.

Fairer for Business. It takes a major step in mitigating the large disparity that currently exists between owners of commercial and residential real estate properties. It also replaces special deals for some business taxpayers with much lower business tax rates across the board.

Improves Arizona’s Competitive Position. It makes Arizona more competitive for business expansion by reducing Arizona’s currently high (nominal) business taxes. It replaces ad hoc business tax relief with much lower tax rates and fewer distortions.

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Increased Accountability. It includes a transparent revenue budget that details all revenue flows, including tax “expenditures” in the form of tax credits, exemptions, and special deals.

More Stability. Stability is improved by the broader bases for sales and income taxes, as well as reduced reliance on the corporate income tax.

Exports Some Costs. The broadened sales tax base exports more of the tax burden to visitors and non-residents (and helps stabilize the revenue base).

Improves Uniformity. It provides for more uniformity and simplicity in property tax assessments by using uniformly trained assessors and simplified rules.

Revenue Growth with Economic Growth. It provides a stable revenue base that more closely matches the growth in Arizona’s economy, giving policymakers a stronger foundation to make critical infrastructure investments and meet important service needs.

Rainy Day Fund. It includes a rainy day fund to deal with inevitable fluctuations in Arizona’s annual revenue flows.

Matches Revenues and Commitments. It avoids using one-time revenue “windfalls” for permanent tax cuts or expenditure commitments. It includes bonding for school construction, consistent with capital budgeting practices of private-sector firms.

Avoids Misguided Limits. It avoids misguided limits that eventually result in the virtual elimination of the government sector.

Comprehensive System Reform. Arizona’s current revenue/tax system is seriously flawed, eroding Arizona’s competitive position in the 21st century economy. Thus, comprehensive system reform, along the lines of the proposals in this report, is crucial for both fiscal responsibility and Arizona’s prosperity in the 21st century.

Balances Taxes and Critical Infrastructure Needs. Success for states in the 21st Century will require a balancing act of sorts to maintain a competitive tax structure with incentives for quality investments, while funding the services and infrastructure investments needed to attract quality job growth. The states that can accomplish this balancing act will be positioned to prosper in the 21st Century. Arizona can and should be one of those states.