

# Fiscal Note

**BILL #** SB 1059

**TITLE:** TPT; use tax; education

**SPONSOR:** Allen S

**STATUS:** As Amended by Senate ED

**PREPARED BY:** Lydia Chew

## Description

SB 1059 would establish a new distribution formula for revenues from additional transaction privilege and use tax collections for education, beginning in FY 2022. This formula would apply to either of two circumstances:

- SCR 1002 is referred to the ballot and in November 2020 voters approve raising the existing 0.6% education sales tax to 1.0% beginning in FY 2022; or
- The rate remains at 0.6%, as under current law.

## Estimated Impact

The impact of SB 1059 on the revenue amounts distributed depends on the outcome of SCR 1002. While the revised distribution begins in FY 2022, *Tables 1* and *2* display the change in distributions under each scenario for a full year in FY 2023.

If no other funding source is identified for Arizona Department of Education (ADE) accountability costs, SB 1059 would result in a \$7.0 million cost to the General Fund beginning in FY 2022.

The General Fund impact of repealing the income tax credit in A.R.S. §43-1072.02 may be \$0 or a cost of \$25.0 million beginning in FY 2022, depending on interpretations of the relevant statutes.

The Department of Revenue has not yet provided an estimate of the bill's impact.

## Analysis

Proposition 301 (2000) established the original 0.6% additional transaction privilege and use tax rate for education, which will expire in FY 2021. Approximately \$64.1 million of these revenues are earmarked for School Facilities Board (SFB) debt service. Of the remaining funds, 12% are distributed to universities, 3% to community colleges, and a proportional amount based on enrollment to tribal community colleges. The measure also allocates \$86.3 million for additional school days, \$7.8 million for school safety, \$200,000 for the Character Education Matching Grant Program, \$7.0 million for accountability measures, \$1.5 million to the Failing Schools Tutoring Fund, and \$25.0 million for an income tax credit. The remainder is distributed to the Classroom Site Fund.

Laws 2018, Chapter 74 extends the 0.6% additional tax for education until FY 2041. The distribution formula is largely the same, but because SFB debt service expires in FY 2021, the initial \$64.1 million distribution will also go to the Classroom Site Fund.

SB 1059 would establish a new distribution formula for revenues from the education sales tax, beginning in FY 2022. If voters approve SCR 1002, the tax rate will be raised to 1.0%. Otherwise, the rate will remain at 0.6%, as under current law.

The tax levied by SCR 1002 would apply to a broader tax base than does the Chapter 74 tax. Under current law, the education sales tax applies to transaction privilege classifications with a tax rate of 5.0%. SCR 1002 would apply the education sales tax to classifications with a tax rate of 5.0% or greater, which includes the transient lodging and online lodging marketplace classifications. Therefore, if SCR 1002 is approved, the distributed revenues will increase by 0.4% for classifications under the Chapter 74 tax and by 1.0% for these two additional classifications.

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**JLBC**

Although SB 1059 would become effective July 1, 2021, tax revenues are received in the month following collection. As a result, if SCR 1002 is approved and the additional tax rate is increased, only 11 months of FY 2022 would reflect these higher tax rates. To simplify our comparison, we use FY 2023 projections for all calculations, as this is the first year in which collections at this higher rate would be reflected in all 12 months.

SB 1059 as amended by Senate ED would maintain distributions of \$86.3 million for additional school days and \$7.8 million for school safety. Of the remaining revenues, 82% would be distributed to the Classroom Site Fund, 13.25% to universities, and 4.25% to community colleges.

Tables 1 and 2 display projected revenues and distributions in FY 2023 under the Chapter 74 and SB 1059 distribution formulas. Table 1 assumes that the education sales tax remains at 0.6% and generates \$906.2 million; Table 2 assumes that voters approve SCR 1002 to increase the education sales tax to 1.0%, thereby generating a total of \$1.55 billion.

<b>Table 1</b>			
<b>0.6% Education Sales Tax: SCR 1002 Does Not Pass</b>			
<b>(\$ in Millions)</b>			
	<b><u>Current Law</u></b>	<b><u>SB 1059</u></b>	<b><u>\$ Change</u></b>
<b><u>Revenues</u></b>	906.2	906.2	0.0
<b><u>Distributions</u></b>			
Additional School Days	86.3	86.3	0.0
School Safety	7.8	7.8	0.0
Classroom Site Fund	650.8	665.9	15.2
Universities (including TRIF)	101.1	111.7	10.6
Community Colleges	25.3	32.1	6.8
Provisional Community Colleges	0.2	0.7	0.6
Tribal Assistance	1.2	1.7	0.6
Character Education	0.2	0.0	(0.2)
Accountability	7.0	0.0	(7.0)
Failing Schools Tutoring Fund	1.5	0.0	(1.5)
Income Tax Credit	25.0	0.0	(25.0)

SB 1059 would eliminate dedicated distributions for the Character Education Matching Grant Program and Failing Schools Tutoring Fund, although it would allow monies from the Classroom Site Fund to be used for these purposes. No General Fund backfill would be required for these programs.

The bill would also eliminate distributions for "accountability" under ADE and the \$25 income tax credit for low-income filers. These costs may require a General Fund backfill.

Accountability monies are used by ADE to develop A-F letter grades for schools and to support the Student Accountability Information System. If no other funding source is identified, these costs would shift to the General Fund. Therefore, SB 1059 may result in a \$7.0 million cost to the General Fund.

The elimination of the income tax credit may have a General Fund impact of \$0 or a cost of \$25.0 million, depending on legal and administrative interpretations of the relevant statutes. There are two potential scenarios, shown in Table 3.

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<b>Table 2</b>			
<b>1.0% Education Sales Tax: SCR 1002 Passes</b>			
<b>(\$ in Millions)</b>			
	<u>Current Law</u>	<u>SB 1059</u>	<u>\$ Change</u>
<u>Revenues</u>	1,553.8	1,553.8	0.0
<u>Distributions</u>			
Additional School Days	86.3	86.3	0.0
School Safety	7.8	7.8	0.0
Classroom Site Fund	1,200.7	1,196.9	(3.8)
Universities (including TRIF)	178.8	200.7	21.9
Community Colleges	44.7	58.9	14.2
Provisional Community Colleges	0.3	0.9	0.6
Tribal Assistance	1.5	2.2	0.7
Character Education	0.2	0.0	(0.2)
Accountability	7.0	0.0	(7.0)
Failing Schools Tutoring Fund	1.5	0.0	(1.5)
Income Tax Credit	25.0	0.0	(25.0)

<b>Table 3</b>					
<b>Tax Credit Scenarios</b>					
<b>(\$ in Millions)</b>					
	<u>Current Statute</u>		<u>SB 1059</u>		<u>General Fund Impact</u>
	<u>General Fund</u>	<u>Education Sales Tax Distribution</u>	<u>General Fund</u>	<u>Education Sales Tax Distribution</u>	
Prop 301 Credit	0.0	(25.0)	(25.0)	0.0	(25.0)
Chapter 74 Credit	0.0	(25.0)	0.0	0.0	0.0

Prop 301 included an income tax credit ("Prop 301 credit") and specified the intent for the credit to mitigate the effect of the education sales tax that the measure created. Although Prop 301 revenues will end in FY 2021, the tax credit does not expressly expire. According to Legislative Council, it is ambiguous whether this tax credit could still be claimed after FY 2021.

Laws 2018, Chapter 74 also included an income tax credit ("Chapter 74 credit") that becomes effective in FY 2022. SB 1059 would repeal this credit.

In one scenario ("Prop 301 credit scenario"), the Prop 301 credit is interpreted as continuing after FY 2021 under the original ballot proposition. SB 1059 would repeal the Chapter 74 credit and the distribution from the education sales tax, requiring the General Fund to cover the cost of the Prop 301 credit. In FY 2019, the total cost of the credit was \$26.3 million. Historically, the number of filers claiming the low-income tax credit has declined, in part because the income levels for eligibility are not indexed to inflation. As a result, we assume that the cost of the credit will be \$25.0 million. Therefore, SB 1059 would result in a \$25.0 million cost to the General Fund beginning in FY 2022.

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In a second scenario ("Chapter 74 credit scenario"), the Prop 301 credit is interpreted as expiring in FY 2021 under the original ballot proposition. SB 1059 would repeal both the Chapter 74 credit and the education sales tax distribution, eliminating all costs associated with low-income tax credits. Therefore, SB 1059 would result in no impact to the General Fund.

**Local Government Impact**

None

2/12/20