



# Arizona State Senate *Issue Brief*

October 5, 2006

## Note to Reader:

The Senate Research Staff provides nonpartisan, objective legislative research, policy analysis and related assistance to the members of the Arizona State Senate. The *Research Briefs* series, which includes the *Issue Brief*, *Background Brief* and *Issue Paper*, is intended to introduce a reader to various legislatively related issues and provide useful resources to assist the reader in learning more on a given topic. Because of frequent legislative and executive activity, topics may undergo frequent changes. Additionally, nothing in the *Brief* should be used to draw conclusions on the legality of an issue.

## STATE SHARED REVENUES

### INTRODUCTION

Revenue sharing is generally based on one of three principals: population, point of origin and need. Sharing on the basis of population results in a per capita apportionment among counties or cities and towns; this implies that a person is worth the same level of revenue regardless of location. Point of origin sharing is based on the theory that revenue should be returned to the location in the proportion to which that location contributes to the state treasury. Revenue sharing according to need shares a portion of the tax yield based on the relative wealth of the political subdivision or based on the political subdivision's ability to raise revenues.

### ARIZONA'S STATE SHARED REVENUES

In Arizona, the state shares income tax (urban revenue sharing), state transaction privilege tax (TPT), Highway User Revenue Fund (HURF) monies, vehicle license tax (VLT) and Local Transportation Assistance Fund (LTAF) monies with incorporated cities and towns, and counties.

### Urban Revenue Sharing

The Urban Revenue Sharing Fund (Fund) was established by voter initiative in 1972. The initiative provided that a percentage of state individual and corporate income tax collections be distributed to incorporated cities and towns. With the creation of the Fund, counties, cities, towns and other political subdivisions were prohibited from levying an income tax. Monies are distributed each fiscal year based on net income tax collections from the two years prior. Each month the State Treasurer disperses to each city or town one-twelfth of its entitlement, which is based on the proportion of the city or town's population compared with the total incorporated population of the state based on the last decennial or special census.

The original distribution percentage was 15 percent of net income tax collections. Since the original enactment, the distribution percentage has been altered numerous times, from 12.8 percent in FY 1989-1990 to the current 15 percent for FY 2004-2005.

Laws 2006, Chapter 351, appropriates \$717,127,600 in FY 2008-2009 from the state General Fund to the Urban Revenue Sharing Fund to compensate for the two-year, 10 percent income

tax rate reduction enacted by Laws 2006, Chapter 354. This appropriation is a one-year, hold harmless provision for cities and towns that is based on the income tax revenue forecast before the rate reductions. As a result, the cities and towns are guaranteed \$717,127,600 regardless of actual income tax collections.

## ***Transaction Privilege Tax***

The Legislature authorized the first TPT to be levied in 1933. Depending on the type of business being conducted, the original rates have ranged from 0.5 percent to 2 percent. Counties received 25 percent on the total amount collected. In 1942, the voters approved an initiative to begin sharing TPT with cities and towns in proportion to the city's or town's population. The initial percentage distributed to the cities and towns was 10 percent of total collection; the counties' share was 45 percent. The distribution formula has been changed numerous times since the 1940s.

A portion of TPT collections is designated by statute for deposit into a distribution base, which is divided among the state, counties and incorporated cities and towns. The remaining monies (nonshared) are directly credited to the state General Fund.

Laws 1994, Eighth Special Session, Chapter 8, established the allocation of monies in the distribution base to the current percentage rates, which are 25 percent to the cities and towns, 40.51 percent to the counties and 34.49 percent to the state General Fund.

## ***Highway User Revenue Fund***

In 1946, the voters approved a ballot measure allocating to cities and towns a portion of gasoline taxes paid by motorists. Established in 1974, HURF consists of revenues from gasoline and use fuel taxes, motor carrier fees, motor vehicle registration fees, VLT and other miscellaneous fees.

Statute requires \$1 million in HURF monies to be transferred to the Economic Strength Project Fund, and up to \$10 million to be transferred to the Department of Public Safety (DPS) for highway patrol expenditures. In

recent years, the \$10 million cap has been suspended, and a higher amount has been transferred to DPS. The FY 2006-2007 budget provided a one-time increase from the state General Fund and a corresponding decrease from HURF, thereby reducing DPS' HURF allocation and restoring the \$10 million HURF statutory cap.

These statutory transfers to the Economic Strength Project Fund and DPS, as well as any legislative appropriations from HURF, are completed prior to the distribution to local governments and the State Highway Fund. The distribution of remaining HURF monies is as follows:

- Counties: 19 percent.
- Cities and towns: 27.5 percent.
- Cities (over 300,000 persons): 3 percent.
- State Highway Fund: 50.5 percent, of which 12.6 percent is divided between the Maricopa Association of Governments and the Pima Association of Governments.

## ***Vehicle License Tax***

In 1940, the voters approved an amendment to the Arizona Constitution that imposed the VLT, beginning January 1, 1941, in lieu of an ad valorem property tax, "on vehicles registered for operation upon the highways in Arizona." The constitutional provisions in existence today require the VLT to be collected as provided by law and authorize the Legislature to stagger registration periods to facilitate an even distribution of vehicles registered and collection of the tax.

Motor vehicle registration fees and a portion of the VLT are deposited into the HURF and are then distributed to the cities, towns, counties and the State Highway Fund. The remaining VLT revenues are distributed to the State Highway Fund and the state General Fund to aid school financial assistance, cities and towns, counties and LTAF.

## ***Local Transportation Assistance Fund***

Established by the Legislature in 1981 to address the public transportation needs of cities

and towns, LTAF receives its funding from the Arizona State Lottery and the VLT. LTAF distributions are based on the population of the city, town or county. Distributions to cities within Maricopa County with a population of 50,000 persons or more and to the County are to be used for transit purposes only. LTAF distributions to counties, cities and towns outside Maricopa County and cities and towns within Maricopa County with a population of fewer than 50,000 can be used for any transportation purpose. LTAF is distributed to county and local jurisdictions with a dollar for dollar match requirement for Maricopa County, Pima County and cities with a population of 50,000 persons or more. The remaining jurisdictions, those with a population of fewer than 50,000 persons, have a one dollar to four dollar match requirement.

### **ADDITIONAL RESOURCES**

- Department of Revenue, Annual Report [www.azdor.gov/](http://www.azdor.gov/)
- “State Shared Revenue,” League of Arizona Cities and Towns [www.azleague.org](http://www.azleague.org)
- Urban Revenue Sharing Fund Statutes: A.R.S. § 43-206
- Transaction Privilege Tax Distribution Base Statutes: Arizona Revised Statutes, Title 42, Chapter 5, Article 2
- Highway User Revenue Fund Distribution Statutes: Arizona Revised Statutes, Title 28, Chapter 18, Article 2
- Vehicle License Tax Distribution Statutes: Arizona Revised Statutes, Title 28, Chapter 16, Article 3
- Annual Appropriations Report, Joint Legislative Budget Committee [www.azleg.gov/jlbc.htm](http://www.azleg.gov/jlbc.htm)
- Tax Handbook, Joint Legislative Budget Committee [www.azleg.gov/jlbc.htm](http://www.azleg.gov/jlbc.htm)