



THE ARIZONA CENTER  
—FOR ECONOMIC PROGRESS—

# **In Search of a State Budget that Creates Opportunity for All**

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**Questions and Answers About  
Arizona's Budget and Taxes**

January 2018





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## Arizona Center for Economic Progress

The Arizona Center for Economic Progress advances thoughtful analysis and effective solutions to raise the economic power of all Arizonans with good jobs and strong communities and the policies that create them.

We engage a diverse group of partners toward a long term plan that includes great education, balanced tax and budget policies, and robust infrastructure.

## Acknowledgements

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# In Search of a State Budget That Creates Opportunity for All



## Table of Contents

<b>Introduction</b> . . . . .	1
<b>Section I:</b> Budget Basics . . . . .	3
<b>Section II:</b> Is Everyone Paying Their Fair Share? . . . . .	12
<b>Section III:</b> Investing in Arizona's Workforce and Communities . . . . .	23
<b>Section IV:</b> Looking Ahead . . . . .	37

Arizonans over the years have taken pride in being hardworking and fiercely independent, with a deep sense of taking personal responsibility in the care of our families, managing our finances, and diligently pursuing our education and careers. In exchange for meeting our obligations, we believe that we will be rewarded with the opportunities we seek to get ahead, to make a life for ourselves that builds on the generations that have come before us.

And for some in Arizona that works, and works well. Arizona is one of the fastest growing states in the nation and some parts of our economy are doing well. But for many of our neighbors—in every community across the state—the promise of opportunity, the hope to build a bright future, remains just a blueprint of ideas despite hard work, despite playing by the rules.

That's not right. It's not what Arizona has long represented. And it is time for us to build up and build out better opportunity for ourselves and those who will follow.



It can happen if we invest in the things we know build up strong families and communities, things like education and health care. It can happen if we invest in the things that build out a thriving economy, things like infrastructure and workforce training.

State budgets and taxes are the foundation for achieving our common priorities that will lead to more quality jobs and a more robust economy for all of us.

This publication provides information and analysis to help all Arizonans better understand how the state budget and tax decision made by the legislature and Governor impact our ability to achieve greater economic prosperity for all.





# Section I: Budget Basics

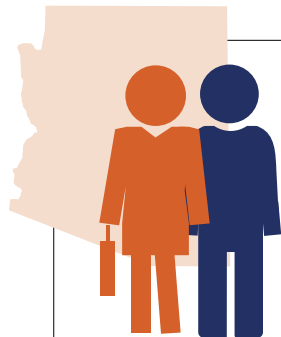
## In This Section:

- How well does this year's budget invest in priorities that will create jobs and a stronger economy?
- What is state government doing to help our communities thrive?
- Where do state revenues come from?
- How well is Arizona meeting the needs of our booming population?
- Does Arizona have limits on taxes and spending?



## How well does this year's budget invest in priorities that will create jobs and a stronger economy?

The most important job of the state legislature and governor is to pass a state budget each year that reflects the priorities of the state and is balanced so that spending from the general fund is less than available revenues. If those common priorities for the state include creating more quality jobs and greater economic opportunities for all of us, then the fiscal year 2018 budget takes only a few small steps toward helping us achieve those goals.



### What do Arizona's business leaders say our priorities should be?

#### What are the top challenges to doing business in Arizona?

1. The quality and availability of a skilled workforce
2. An underfunded public education system

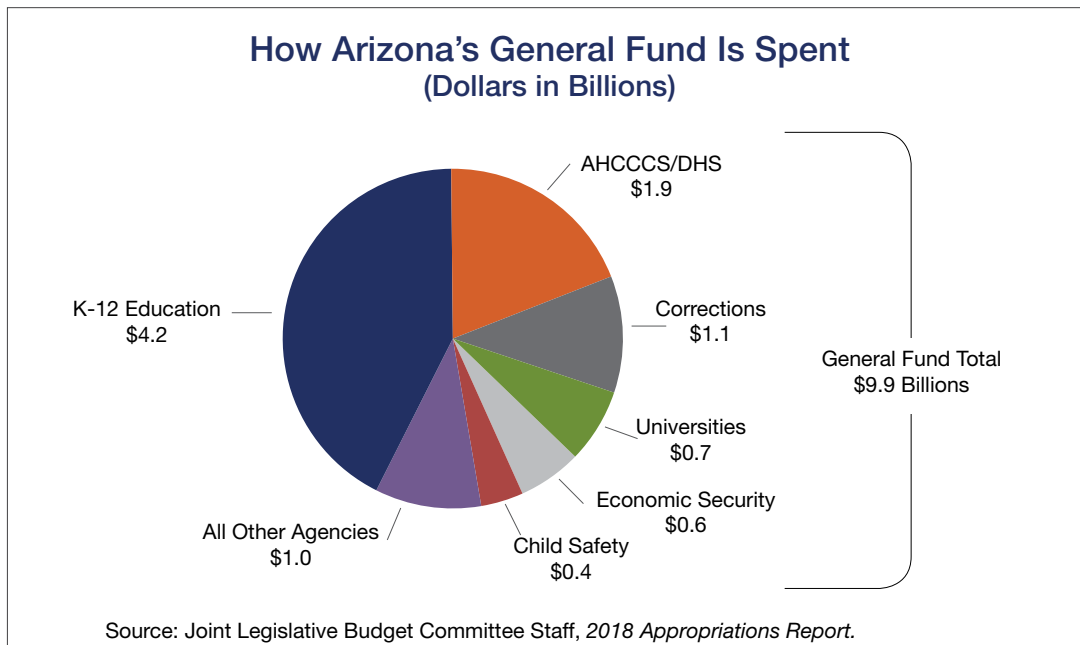
#### What should be the top priorities of local governments?

1. Improve K-12 public education system
2. Community college training/workforce development

#### What should be the number one priority of state government?

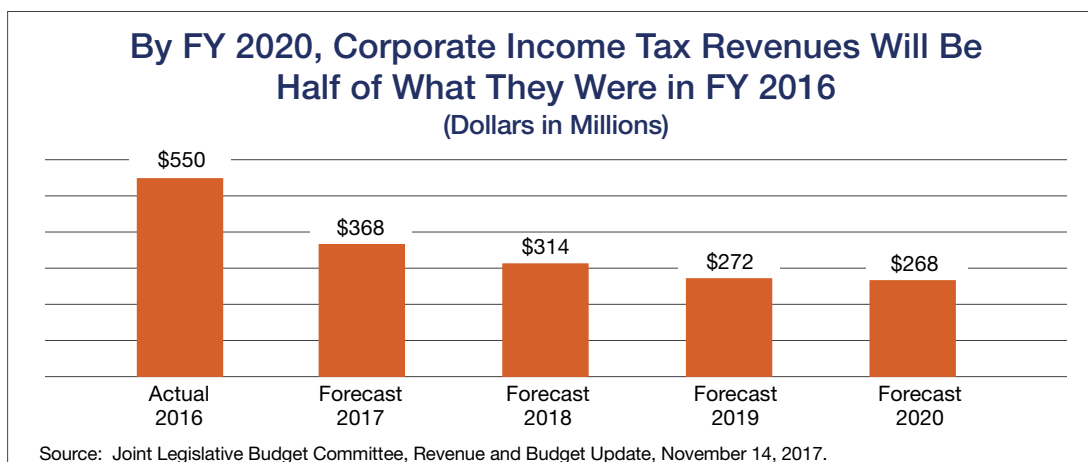
1. Increasing K-12 public education funding

Source: Highlights of a survey of over 500 Arizona business leaders from "2017 Alliance Bank of Arizona Leaders in Business Survey."



## Some Key Facts about the 2018 Fiscal Year Budget

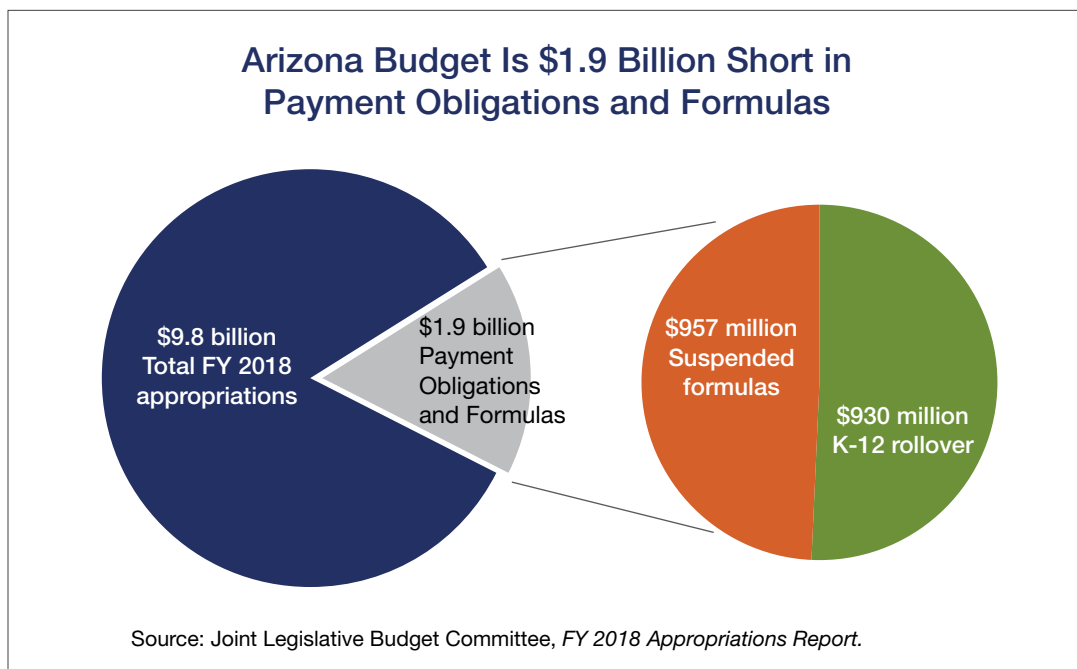
- Arizona's overall general fund expenditures are \$100 million less today than they were a decade ago, despite the fact that Arizona's population has grown by 736,000 during that time period.
- State lawmakers took no action and made no plan to close an annual deficit of \$1.1 billion in cuts to public schools that have not been restored, leaving Arizona families and business facing a teacher shortage, outdated textbooks and technology, and unsafe school buses and school facilities.
- Tax cuts passed in prior years are not fully phased in. In fiscal year 2018, tax revenues are projected to be \$76 million lower as a result of tax cuts passed since 2017; by fiscal year 2020, these same tax cuts are expected to result in \$28 million less in revenues.





## Additional Key Facts about the 2018 Fiscal Year Budget




- The state has built up \$2.5 billion in general fund debt with annual payments of principal and interest that must be funded every year—like paying a mortgage. The annual debt payments combined are \$326 million—\$6 million more than the state’s budgetary support to Arizona State University.
- Arizona’s Rainy Day Fund, the pot of money state lawmakers set aside to help us weather the next recession, has not received any new deposits, and is in fact \$217 million less than it was 10 years ago.
- Arizona also has \$1.9 billion in unfunded obligations. These include delayed payments, an accounting gimmick known as “rollovers,” that pushes the payment of certain bills into the following fiscal year. They can continue year after year until enough funds are available to reverse them. In addition, a number of budget formulas in state law are unfunded. These formulas are put into state law to automatically adjust specific types of spending for certain factors every year, such as inflation or growth in people needing the service. The legislature has eliminated some of these formulas from state law and they are not included in the \$1.9 billion. Others remain in state law, but go without funding in the state budget.






## What is state government doing to help communities thrive?

Arizona government is the largest employer in Arizona employing more than 52,000 people who staff a number of state agencies and boards. Collectively, these state agencies are responsible for utilizing our tax dollars to provide the day-to-day services that we need to live productive lives, such as having sustainable sources of water, protecting us from consumer fraud, keeping our roads safe and maintained, and countless other ways. But billions of dollars of tax cuts and credits since 1990 have drained state revenues to the point that most state agency budgets are smaller today than they were a decade ago. Many of these agencies will need additional investments in the coming years in order to maintain the services our communities need to keep us safe, increase property values, and attract the jobs, visitors and new residents that enable our economy to prosper for all of us.

### A Glimpse at a Few Key State Agencies

Agency	A Sample of What They Do	Recent Budget Impacts	2018 General Fund Appropriations compared to 2008 (Revised)
<b>Department of Public Safety</b>	Keep Arizonans safe on the roads and at events.	The time period from 8 pm to 6 am is referred to as the “Night Watch” for a patrol area covering most of Maricopa County. DPS reports that only about 16 troopers are on the road on average during this Night Watch patrol. With a disproportionate number of wrong-way driver incidents and 70% of all fatal collisions occurring during this Night Watch period, DPS reports additional officers are needed to patrol the roads during these hours.	-\$25 million  19%
<b>Department of Water Resources</b>	Ensures that all Arizonans have access to a secure long-term dependable water supply that will not only support our families but will also support businesses and a growing population so that Arizona can remain economically competitive in the Southwest desert.	Staffing at the Department of Water Resources remains 34% below 2008 levels as the Department deals with key issues like ensuring Arizona maintains its share of Colorado River water.	-\$7 million  30%
<b>Office of the Attorney General</b>	Prosecutes those who defraud Arizona consumers, abuse children, engage in public corruption, violate our civil rights, or harm our environment.	The Border Crimes Section prosecutes all cases within the Attorney General’s jurisdiction for southern Arizona, primarily focusing on complex white collar and criminal enterprise crimes. During 2017, the Border Crimes Section had 63 cases against 151 defendants that were not prosecuted, or prosecution was delayed, because attorneys were overburdened with existing cases.	+\$2 million  9%

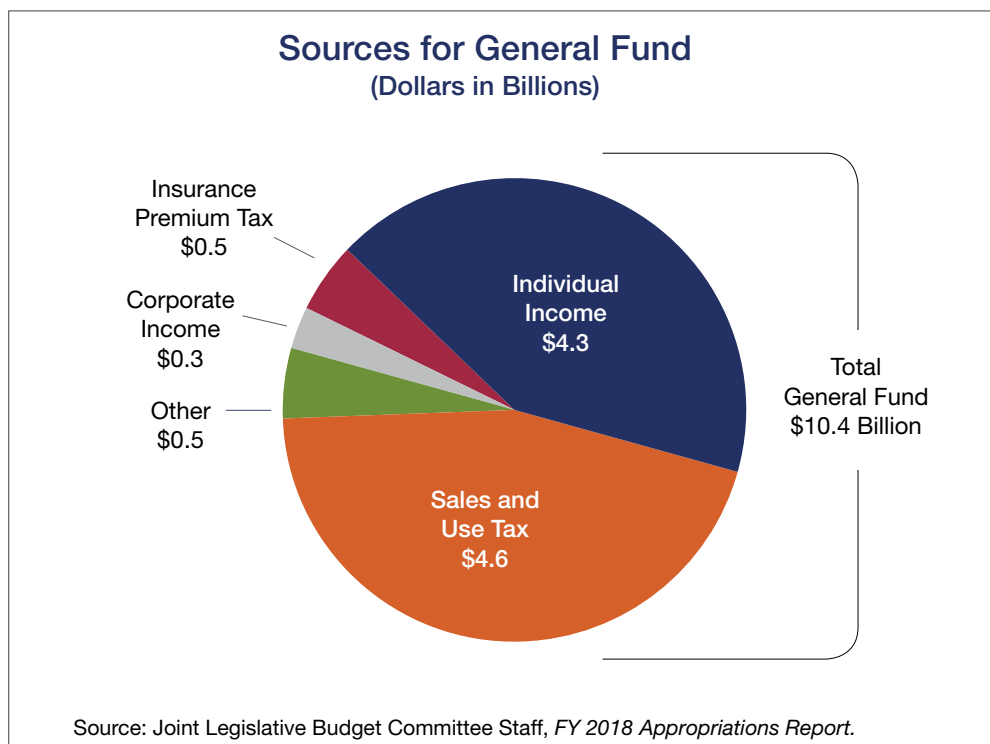
Agency	A Sample of What They Do	Recent Budget Impacts	2018 General Fund Appropriations compared to 2008 (Revised)
<b>Department of Veterans Services</b>	The Department of Veterans' Services assists veterans and their dependents obtain federal entitlements, such as claims for disability, pension and insurance. The Department also operates two Veteran Homes and helps to coordinate services across the private and public sector such as for homeless Veterans.	The US Department of Veterans Affairs formula for determining State long-term care needs indicates that Arizona will require 1,520 long-term care beds in order to serve its veteran population in the year 2020. If the state does not fund its share of development and construction costs for new facilities, it will have a 1,080-bed deficiency in 2020.	<p>-\$3 million</p>  <p>34%</p>
<b>Department of Transportation</b>	Builds, maintains and operates Arizona's highway system and bridges.	A September 2015 auditor general's report estimates the state's transportation system faces a \$62 billion shortfall to meet the state's highway transportation needs over the next 25 years. It further reported that driving on roads in need of repair costs Arizona drivers an estimated \$1.5 billion annually in extra vehicle repairs and operating costs, according to the American Society of Civil Engineers.	<p>-\$76 million total funds</p>  <p>-16%</p> <p>Capital funding - +\$24 million/+7%</p> <p>The Department of Transportation primarily relies on funds from state fuel taxes and motor vehicle registration taxes to fund highway construction and other capital projects. However, in recent years, the legislature has swept some of those funds into the general fund budget to cover for revenue shortfalls.</p>
<b>Department of Revenue</b>	Responsible for administering Arizona's tax laws including collecting much of the revenue that is deposited into the state's general fund.	At the beginning of fiscal year 2017, the department laid off 52 staff, many being tax auditors and collectors, meaning they have fewer staff to collect the revenue that is owed to the state. According to the department, the average collections generated is over \$1.5 million for each collector and between \$1 and \$2 million for each auditor.	<p>-\$43 million</p>  <p>58%</p>

## Where do state revenues come from?

State income taxes for individuals and corporations and sales taxes each make up nearly half of all revenue to the state general fund.

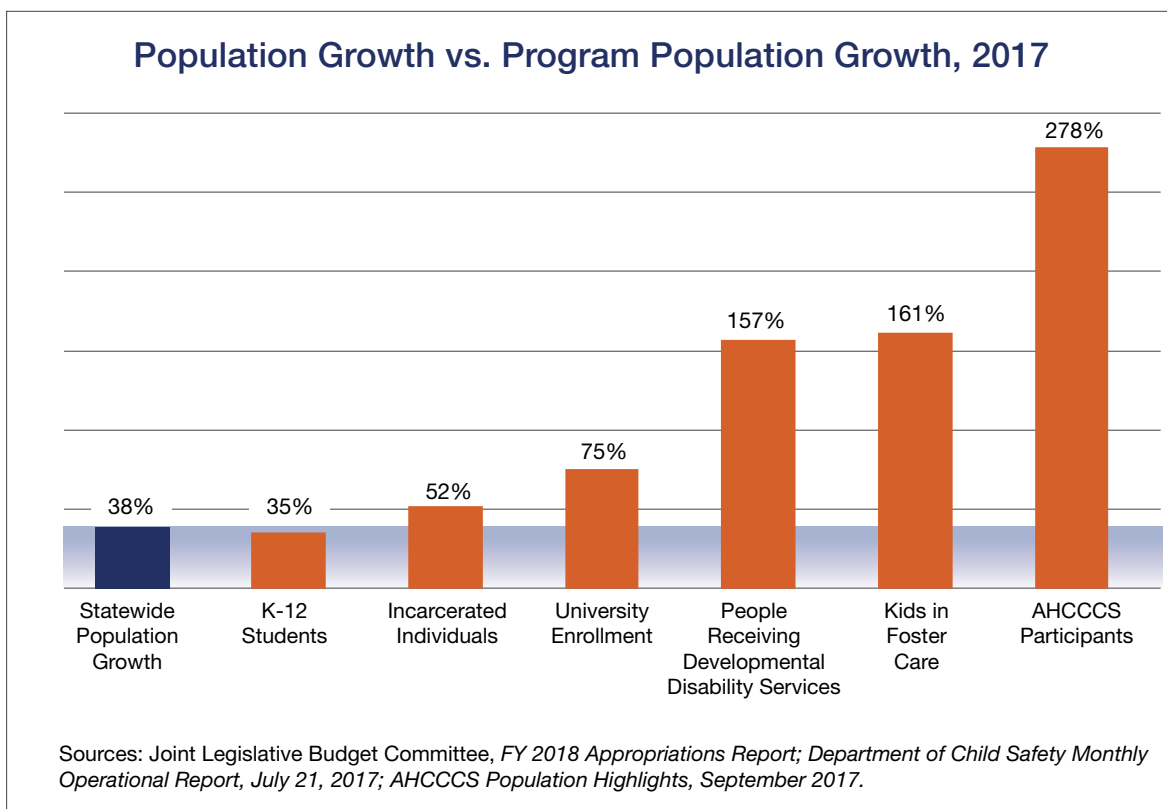
If Arizona were to eliminate the income tax, as some have proposed, and increase the sales tax to make up for the revenue loss, Arizona's sales tax rate would grow from the current 5.6 percent to 10.6 percent. Arizona's rate would become the highest in the nation, significantly higher than the current top spot of California at 7.5 percent.

The sales tax is generally less volatile than the income tax, which means it can be easier to forecast accurately from year to year. Since sales tax is the same regardless of income, such taxes are considered regressive because lower-income earners pay more as a percentage of their income. Also, as the economy moves toward technology and digital goods—things that Arizona generally does not tax—the sales tax base is capturing an increasingly smaller piece of what consumers are actually spending.

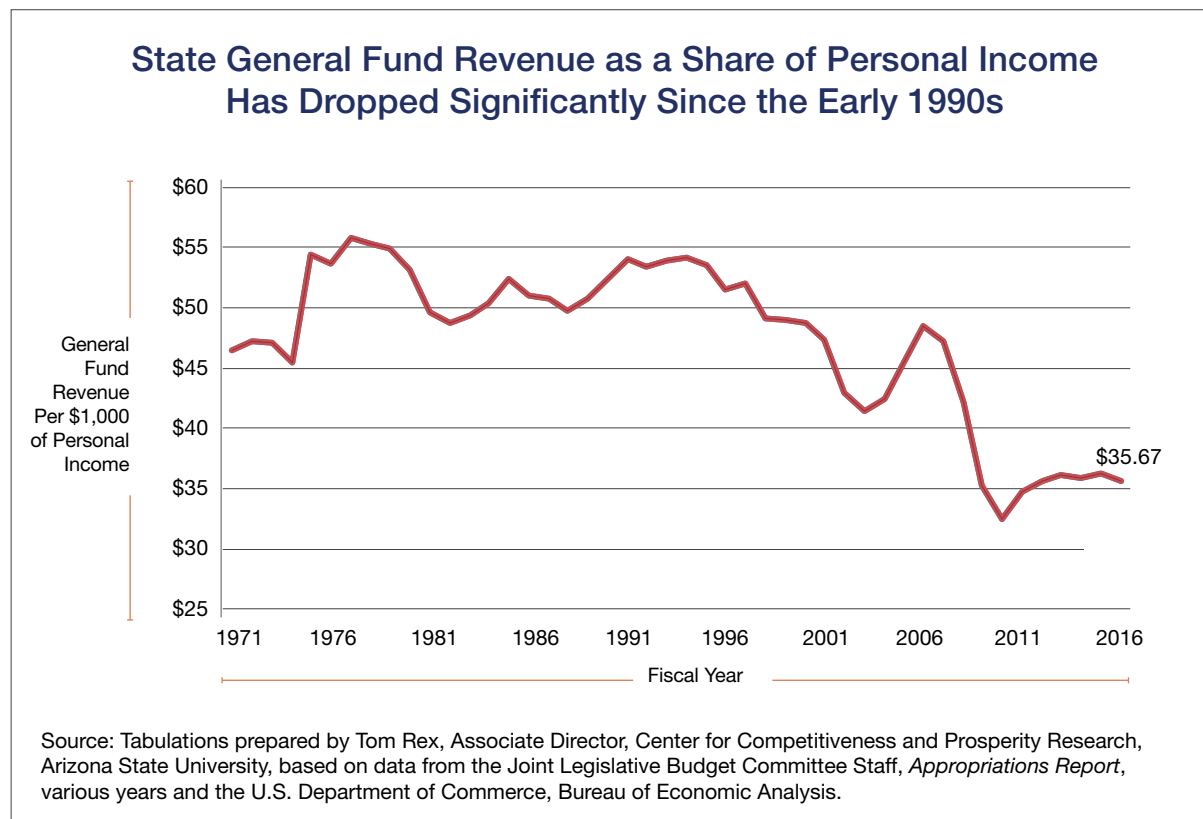


## How well is Arizona meeting the needs of our booming population?

Arizona's population has grown by 38 percent since 2000. A growing population creates a rising demand for public services which means more state revenues are needed to fund those services. In fact, many of the groups that drive the rising demand for state services are actually growing far faster than the statewide population, including incarcerated individuals, community college and university students, children in foster care, and children and adults participating in services for developmental disabilities.



Despite the increasing needs of a fast-growing population, the hundreds of millions of dollars in tax cuts enacted since 1990 have resulted in state general fund revenues that in 2016 were \$35.67 per \$1,000 of income—one-third lower than in 1990 and 15 percent lower than right before the Great Recession in 2008.



Arizona will likely continue to experience rapid growth over the next several years. Arizona had the eighth fastest growing population in the nation in 2016 according to the US Census Bureau and our population is expected to grow by 20 percent by 2030. All of this growth means it will be incumbent upon our state lawmakers and other elected leaders to govern with a long-term vision and plan to do a better job in ensuring that Arizona has the revenue and resources needed to maintain the public safety, education, health care, roads and other services need to keep us economically competitive and to build thriving communities.

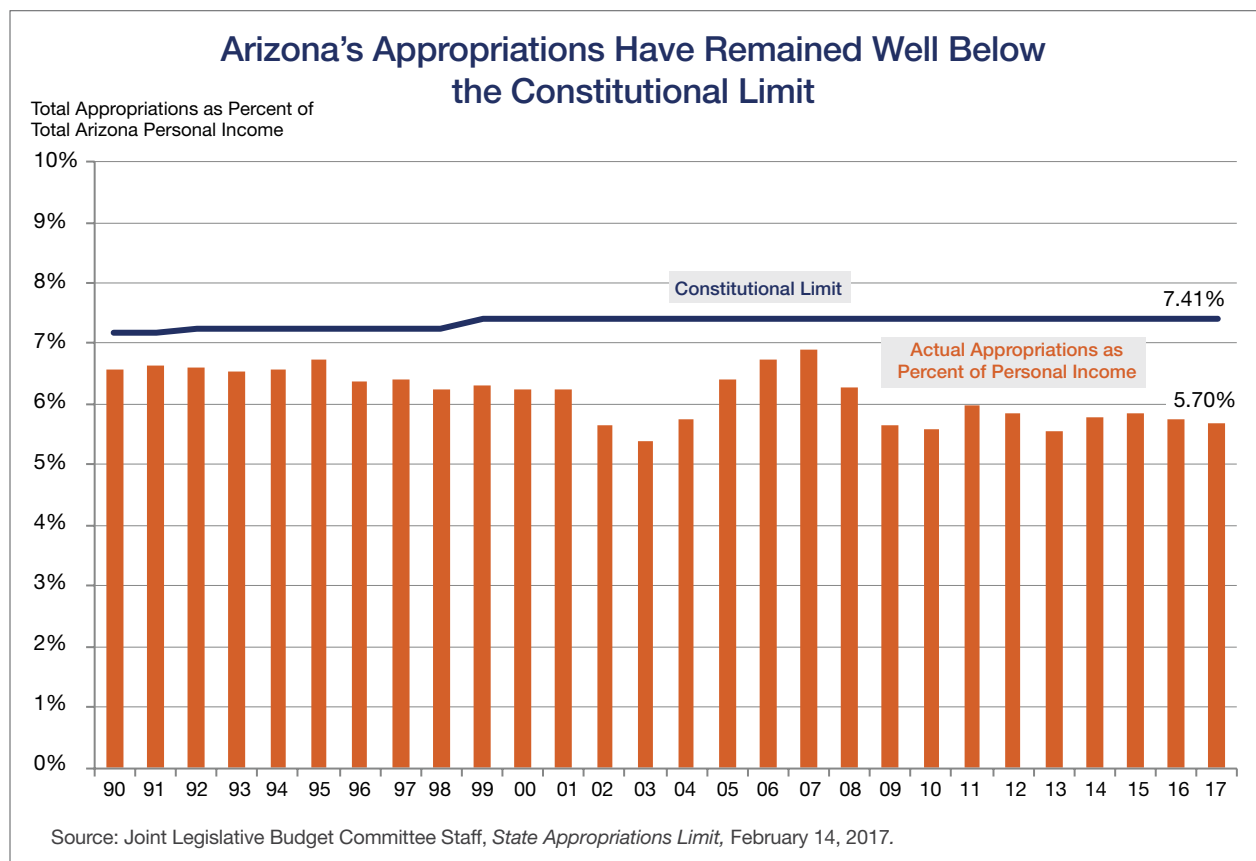


## Does Arizona have limits on taxes and spending?

Yes. Arizona has both constitutional and statutory limits on spending and revenue increases.

The Arizona constitution contains an appropriation limit that applies to all appropriated funds, not just the state's general fund. This limit is based on the size of the overall state economy. Currently the limit is 7.41 percent of the total state personal income. Arizona's appropriations have remained well below the constitutional limit with actual appropriations falling from 6.56 percent in 1990 to 5.7 percent in 2017.

- The Arizona constitution also requires that any legislation that would increase state revenues must be approved by a two-thirds majority of the legislature. This encompasses not only adopting new taxes or increasing rates on existing taxes, it also includes any reduction or elimination of tax deductions, credits, exemptions or exclusions. On the other hand, passing tax cuts, adopting or expanding new credits, or any other action that reduces state revenues requires only a simple majority.
- Article 9, Section 3 of the Arizona constitution requires the legislature to provide sufficient sources of revenue to defray the ordinary expenses of the state for each fiscal year. In other words, the state budget must be balanced every year.





## Section II: Is Everyone Paying Their Fair Share?

### In This Section:

- Has Arizona been cutting taxes?
- If Arizona has cut taxes every year since 1990, why do some Arizonans feel like they are paying more?
- Who doesn't pay state income taxes?
- What are tax credits doing to the state budget?
- How do we know if all of these tax giveaways are delivering the promised jobs and other economic benefits?



### Has Arizona been cutting taxes?

With the exception of 2003, the Arizona legislature has reduced tax rates and/or increased exemptions and credits every year since 1990. Even when factoring in statutory changes that have increased revenues, these tax cuts passed since 1990 have cost the state's general fund more than \$2.2 billion in revenues—more than double that when you adjust for inflation. The tax cuts include:

- Both the corporate and individual income tax rates have been reduced several times at a total cost to the general fund of \$1 billion, not adjusted for inflation. Today, the individual income tax rate for the highest income bracket is less than two-thirds of what it was in 1990. The corporate income tax rate recently completed a four-year phase down which results in the rate being just over half (52 percent) of what it was in 1992.
- 41 individual income tax credits have been adopted, with 33 of them still in affect. The total annual cost of these credits, excluding any carry forward amounts, is approximately \$235 million.
- 31 corporate income tax credits have been adopted, with 22 of them still being in effect. The annual cost of these tax credits, excluding any carry forward amounts, is approximately \$133 million.
- New exemptions and increased deductions for all types of taxes amount to \$452 million, not adjusted for inflation.
- Allowing multistate corporations to choose their preferred method for determining their taxable income, called single sales factor, means \$132 million less per year in state revenues.

#### Arizona Used to be A High Tax State— But Not Any More

In 1990, Arizona was ranked 10th highest for state and local taxes as a percentage of personal income. Due to the steady stream of tax cuts since then, Arizona ranked 38th as of 2014.

Source: Calculations based on Bureau of the Census and Tax Policy Center data. State and local taxes combined.

### How Arizona Ranks State and Local Revenue per \$100 of Personal Income

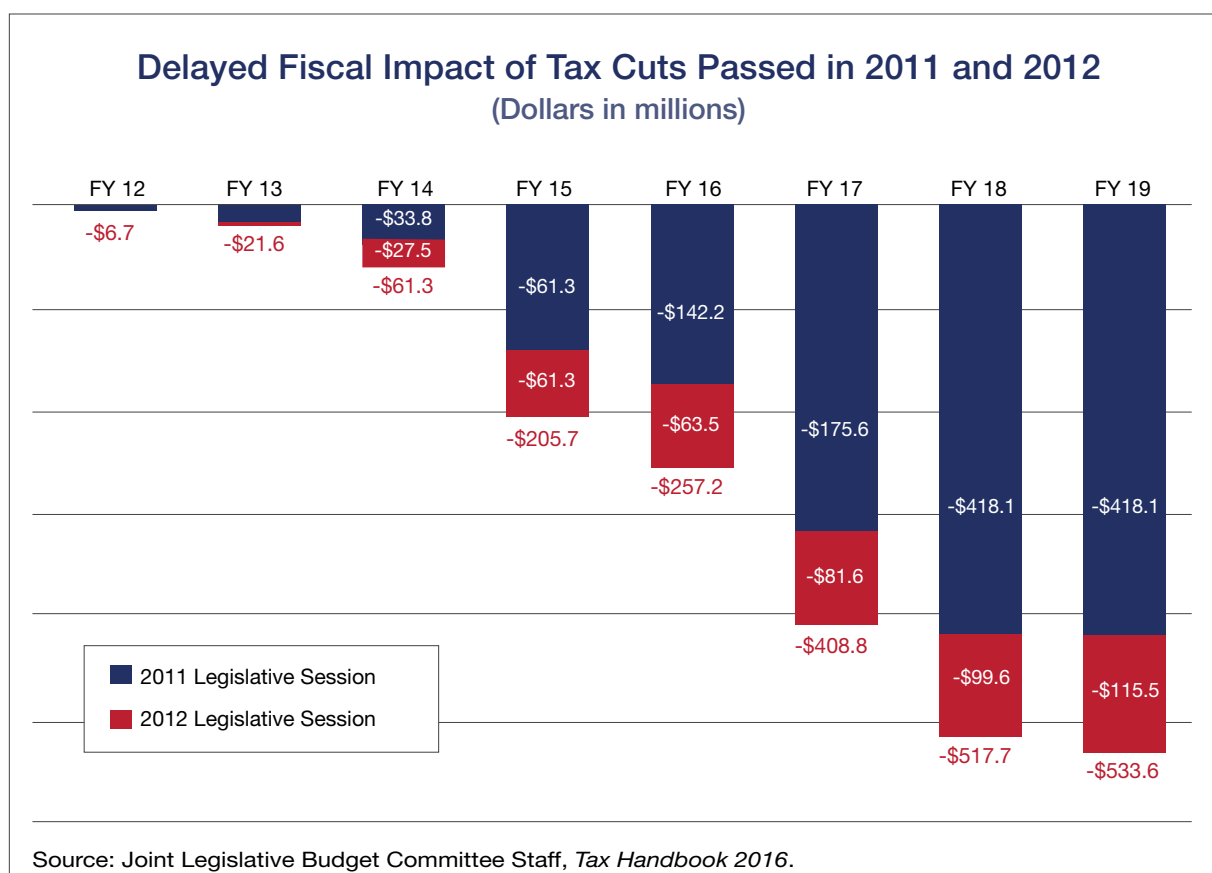
	2000	2014	Out of
Individual Income	38	40	43
Corporate Income	21	38	46
Property	22	33	50
General Sales	7	8	46
Selective Sales	39	45	50
Motor Vehicle	N/A	48	49
Other Taxes	47	47	50
Total Taxes	27	38	50
Fees/Miscellaneous	42	36	50
<b>Total – Taxes + Fees</b>	<b>37</b>	<b>40</b>	<b>50</b>

Source: US Census and Bureau of Economic Analysis

Between fiscal years 2007 and 2010, state general fund revenues fell by one-third and state spending was cut from \$10.1 billion to \$7.8 billion. In May 2010, voters approved a temporary 1 cent sales tax that raised approximately \$1 billion a year over three years and avoided even deeper spending cuts. For the first time in state history, Arizona ended the 2011 fiscal year with a shortfall—a negative balance of \$322 million was carried over into fiscal year 2012. Yet, in 2011 and again in 2012, the legislature and governor passed major taxes. In both instances, these tax cuts started off with a fairly small impact but included provisions to phase in larger cuts over a six-year period. By fiscal year 2019, the annual impact tax cuts passed during 2011 and 2012 will have increased from \$6.7 million to \$533.6 million.

#### Does cutting taxes stimulate the economy and result in boosting revenues?

A school of thought exists that tax cuts—particularly those that benefit corporations and wealthy individuals, produce greater economic growth by spurring investment and job creation. In circumstances where taxes make a state noncompetitive, reducing taxes may be warranted. But that is not the case in Arizona. With the exception of the general sales tax, the taxes that Arizonans pay are low compared to other states.

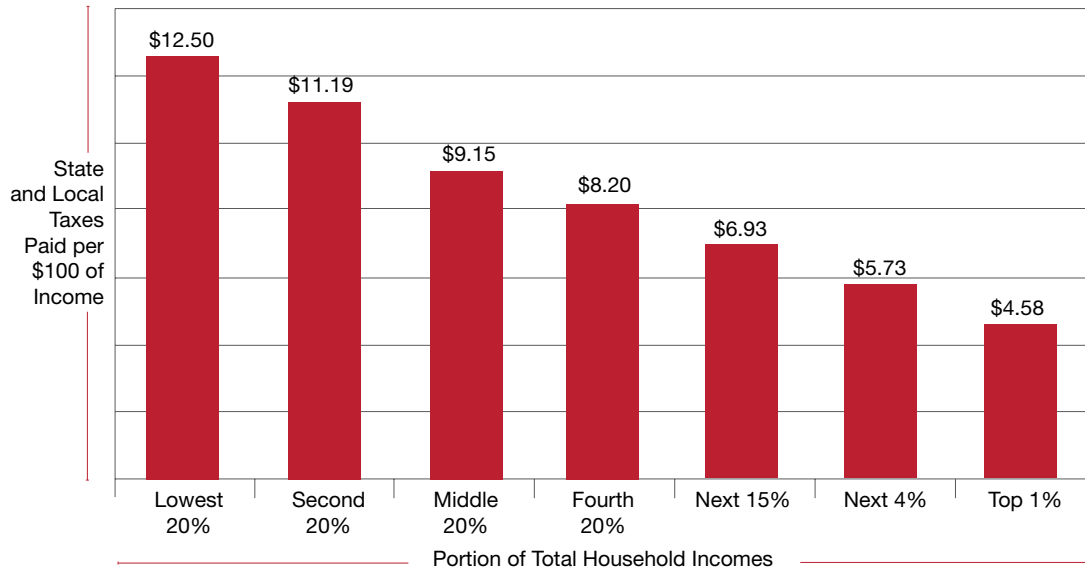


## If Arizona has cut taxes every year since 1990, why do some Arizonans feel like they are paying more?

While all families in Arizona help pay for health, education and public safety through state and local taxes, low-income and middle-income families pay a larger portion of their income in taxes than do wealthier families.

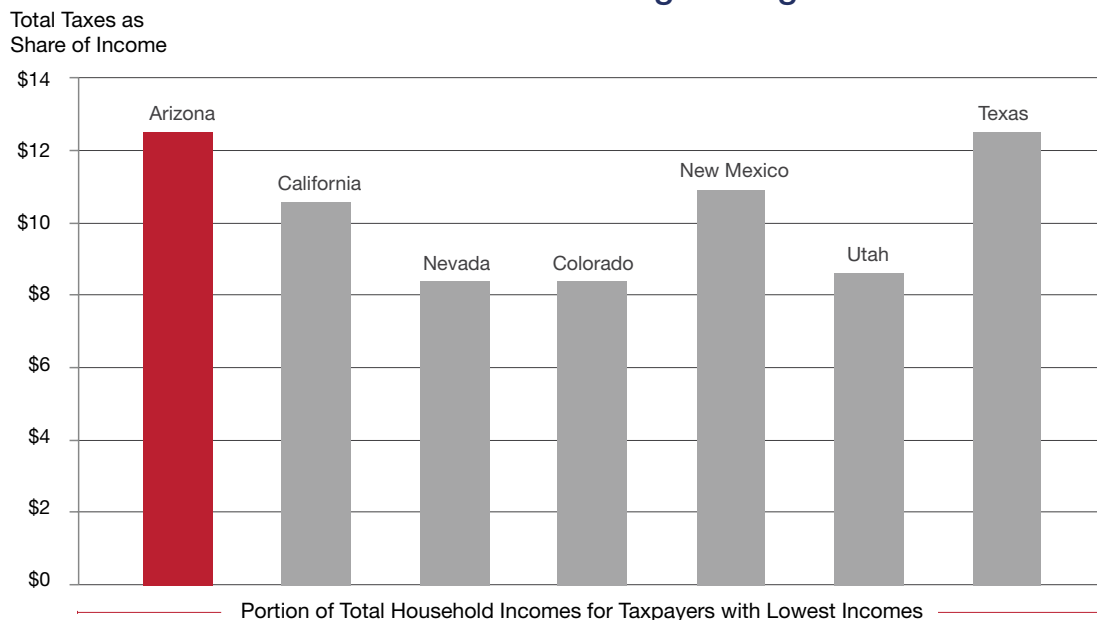
When all types of state and local taxes are combined—income, sales and property—families with incomes in the bottom fifth pay nearly three times what families in the top 1 percent do—\$12.50 for every \$100 of income and \$8.20 for middle income families compared to \$4.58 for the highest income families. Sales taxes make up the largest portion of the taxes paid by those with the lowest incomes. Families with the lowest incomes in Arizona also pay more of their income in state and local taxes than do the lowest income families in California, Colorado, Nevada, New Mexico, and Utah.

## Arizona Families with Lowest Incomes Pay a Higher Portion of Their Income in State and Local Taxes than Taxpayers with Higher Income



Source: Institute on Taxation & Economic Policy, *Who Pays?*, January 2015.

## Arizona's Low-Income Families Pay More than Low-Income Families in Neighboring States

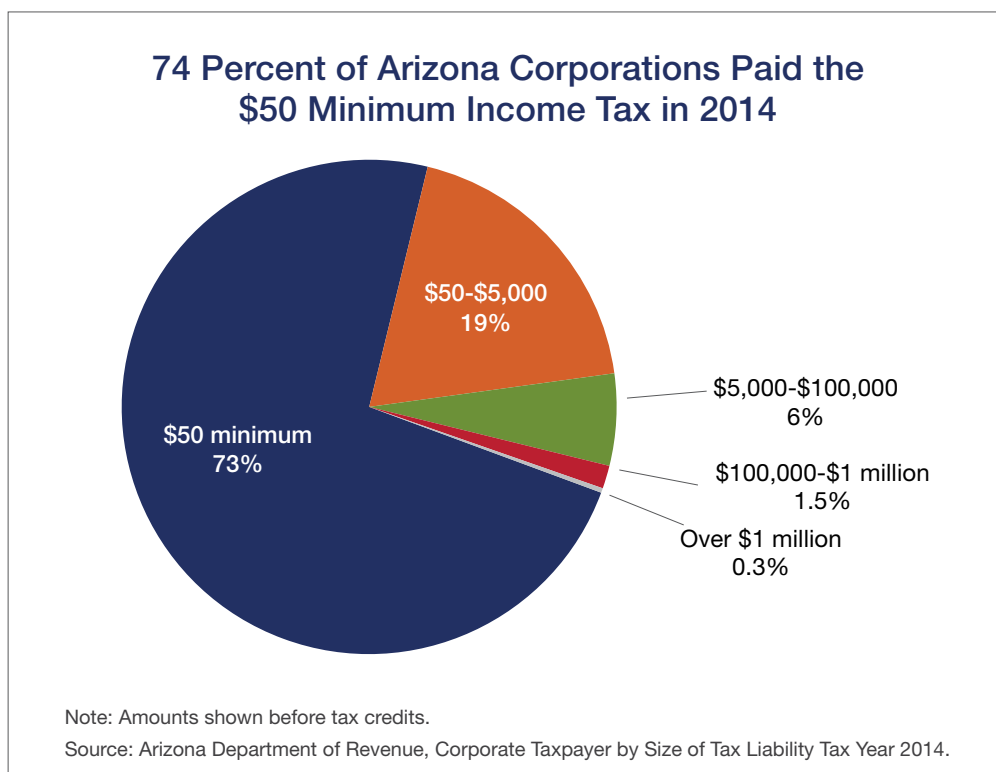


Source: Institute on Taxation & Economic Policy, *Who Pays?*, January 2015.

## Who doesn't pay state income taxes?

Many corporations end up paying little or no state income taxes. Three out of four corporations that filed income taxes in Arizona in 2014 (latest data available) had the minimum tax liability of \$50. Fewer than one in ten corporations paid \$5,000 or more in income taxes.

Corporations can significantly reduce or entirely eliminate their income tax bill through the use of tax credits. In 2015, corporations reduced their tax liability by \$139 million through the use of tax credits and carried another \$1.1 billion over to be used in future years.





Like corporations, individual taxpayers can also eliminate their state income tax bill through the growing number of exemptions, deductions and tax credits. Here is an example of how an Arizona family of four with an adjusted gross income of \$162,800 can end up owing no state income taxes through common deductions and tax credits.



### Arizona Income Tax Return for Family of Four

Federal adjusted gross income	\$162,800
Subtractions	
Standard deduction	-10,336
Personal exemptions	-6,300
Dependents (2)	-4,600
Taxable Income	141,414
Tax (Income x .0424 less \$1,219)	4,777
Credits	
Student Tuition Organization	-1,092
Student Tuition Organization — “Switcher”	-1,085
Qualifying charitable organization	-800
Qualifying Foster Care Charitable	-1,000
Public schools extracurricular activities	-400
Military Family Relief fund	-400
Subtotal - Credits	-4,777
<b>Taxes Owed</b>	<b>0</b>

## What are tax credits doing to the state budget?

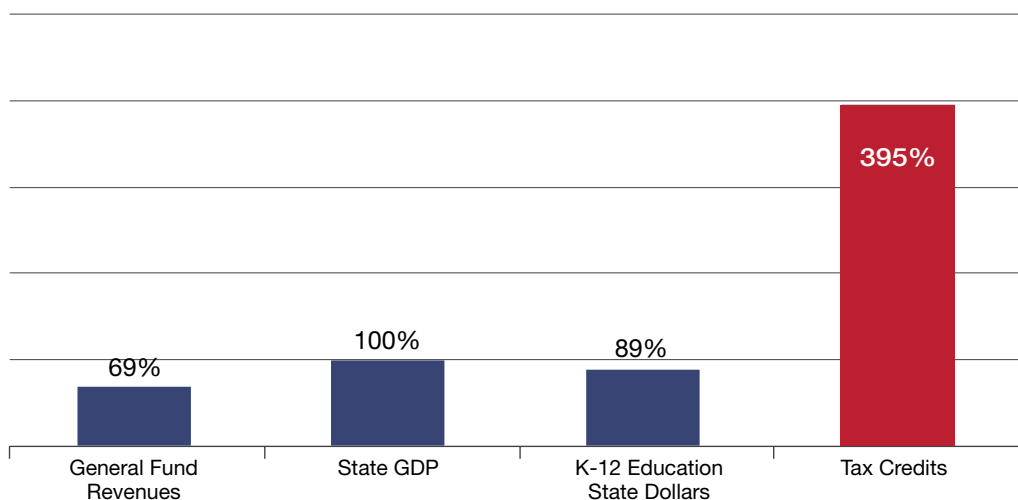
Tax credits cost the state budget \$393 million in fiscal year 2017 (excluding credits for taxes paid to other states) and have been growing fast. They compete with state agency budgets for the same pot of funding, but state lawmakers have virtually no accountability or control over tax credits once they are in state law.

A tax credit reduces the amount of taxes owed on a dollar-for-dollar basis—a \$400 tax credit can wipe out a \$400 tax bill. The dollar value of tax credits claimed is growing at a much faster rate than state revenues, the state's economy, or state spending on K-12 education. In each legislative session since 2005, at least one tax credit has been added or expanded. Between 2010 and 2017, even as state revenues remained low due to the recession, nine new tax credits were created and 12 existing credits were modified. Today there are 15 credits available to individuals, 12 available to corporations and 13 available to both individuals and corporations.

### A sample of what qualifies for a tax credit in Arizona

- Purchase of pollution control equipment
- Employing individuals to work for a healthy forest enterprise
- Investing in research and development activities
- Donations of school sites to school districts or charter schools
- Use of coal consumed in generating electrical power
- Contributions to a private school tuition organization
- For the construction costs of certain environmental technology facilities
- Purchase of agricultural water conservation systems

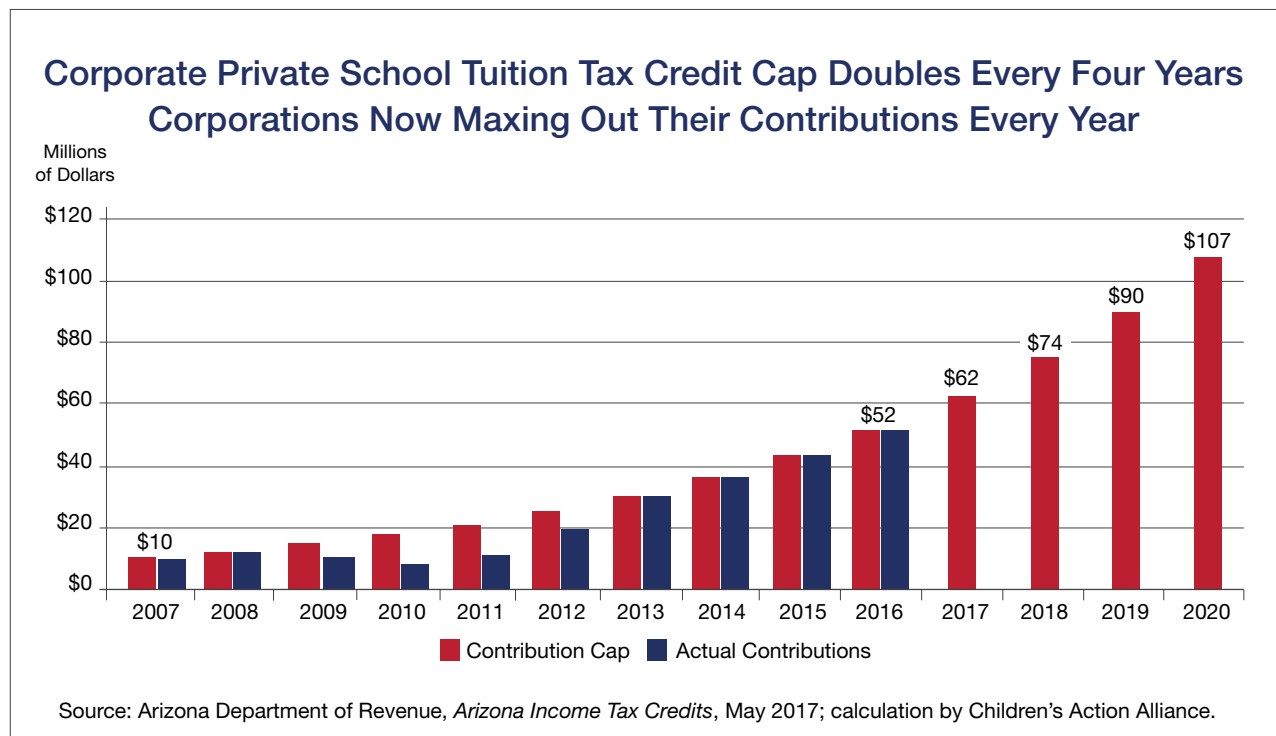
### Tax Credits Are Growing Fast - Percent of Growth 1999 to 2017



Source: Joint Legislative Budget Committee staff, *Appropriations Reports for FY 1999 and FY 2018*; Department of Revenue, *Arizona Income Tax Credits, October 2016*; and U.S. Bureau of Economic Analysis.

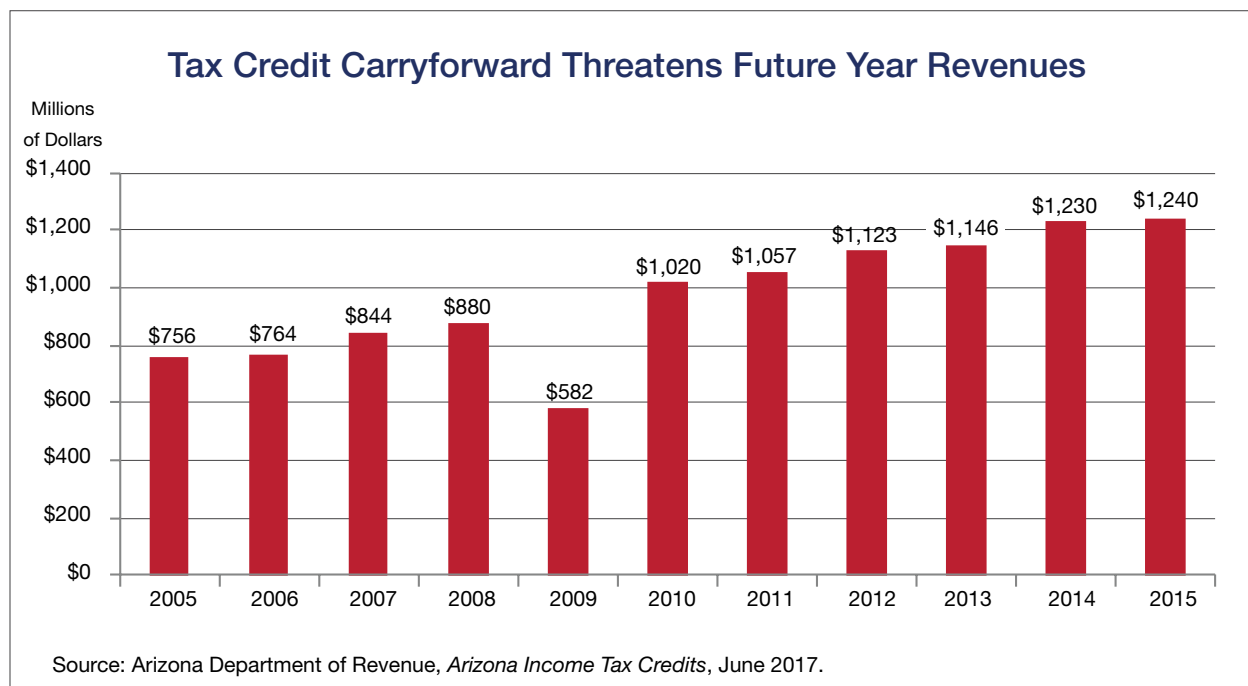
Tax credits lack the basic accountability and control that state spending has. Unlike agency budgets that must be approved by the state legislature every year, tax credits are reviewed only once every five years. Even after a review shows questionable results, tax credits continue forever unless a bill to repeal them passes with a two-thirds vote in both the house and senate. While state agency spending is capped at the appropriated amount, only 7 out of 55 credits have an aggregate cap. State legislators don't know what the fiscal impact of any tax credit will be in any particular year until after the credit has already been taken.

The expansion of the private school tuition tax credits in particular is having a significant impact on state revenues. Arizona now has two individual and two corporate tax credits for contributions to "student tuition organizations" that use the funding to grant scholarships for private school tuition. Combined, the amount claimed for these four credits rose from under \$14 million in 1999 to \$157 million in 2016. The largest of the corporate tax credits (shown below) has an aggregate cap that grows by 20 percent each year and has been maxed out in the last several years.



Another feature that puts tax credits outside legislative budget control is the carry forward balance that taxpayers are allowed to accumulate and use in future years. For most tax credits, if taxpayers don't owe enough income taxes to use the whole credit, they are allowed to save the unused portion of the credit and apply it against future tax liability. For instance, if a taxpayer owes \$300 in taxes and has contributed to the charitable organizations tax credit, the \$100 unused portion of the credit can be carried forward and used on next year's tax return. The number of years a tax credit can be carried forward ranges from 5 to 15 years.

Today, individuals and corporations are carrying forward a combined \$1.2 billion balance in tax credits that can hit the state budget at any time. This carry-forward amount is four times greater than the credits claimed in any single year. The carry-forward balance for corporations is expected to grow because the amount of corporate taxes due will decrease with the phase down of the corporate tax rate.



## How do we know if all of these tax giveaways are delivering the promised jobs and other economic benefits?

Arizona lawmakers do very little to measure whether we are actually gaining the jobs and other economic benefits that are often promised in exchange for tax cuts. When certain corporations and individuals do not have to pay their fair share in taxes, we should know whether the state is getting a justified return on its investment for providing that tax giveaway instead of investing those foregone tax dollars in other priorities that will lead to a stronger workforce and job creation.

Tax cuts don't get evaluated based on actual results, but tax credits have a mechanism in Arizona law to measure their effectiveness. The Joint Legislative Income Tax Credit Review Committee exists to "establish a standard for evaluating and measuring the success or failure of the tax credits." The statute governing the Joint Legislative Income Tax Credit Review Committee provides good standards for evaluating the effectiveness of tax credits:

- The history, rationale and estimated revenue impact of the credit;
- Whether the credit has provided a benefit to Arizona including, for corporate tax credits, measurable economic development, new investments, creation of new jobs or retention of existing jobs in this state; and
- Whether the credit is unnecessarily complex in the application, administration and approval process.

However, the failure to collect sufficient data from the recipients of the tax credits to effectively evaluate the credits, combined with the committee's lack of follow-through, often results in the continuation of many tax credits that are not delivering the promised results.



### Shortcomings of the Joint Legislative Income Tax Credit Review Committee

- Committee has recommended 11 tax credits be repealed since 2006 and to date the legislature has only repealed 3 of those credits.
- Committee did not meet in 2016 because it could not get a quorum.
- Committee members and staff often state that they do not have sufficient information to evaluate the ROI/effectiveness of the tax credits.

While there are at least some provisions in the law to evaluate tax credits, how and when to evaluate the effectiveness of other tax breaks is left to the discretion of the legislature. Requiring those businesses and individuals who benefit from the tax breaks to provide information on the new investments, new jobs, and other economic development that they have created as result of receiving the incentives (which they currently do not have to do), would enable lawmakers to more effectively evaluate whether existing and proposed tax breaks provide a good return on investment or whether those foregone tax dollars could more effectively grow our economy by being invested in other priorities.







# Section III: Investing in Arizona's Workforce and Communities

## In This Section:

- How does the state budget impact having a good public school in my neighborhood?
- How do vouchers provide less accountability to ensure we are sufficiently educating our future workforce?
- What is Arizona doing to ensure every Arizonan has access to affordable post-secondary education and job training opportunities?
- How does access to affordable childcare serve as a barrier to working and going to school?
- How have state budget cuts impacted the availability of affordable housing in Arizona?
- What impact does Arizona's criminal justice system have on our workforce?

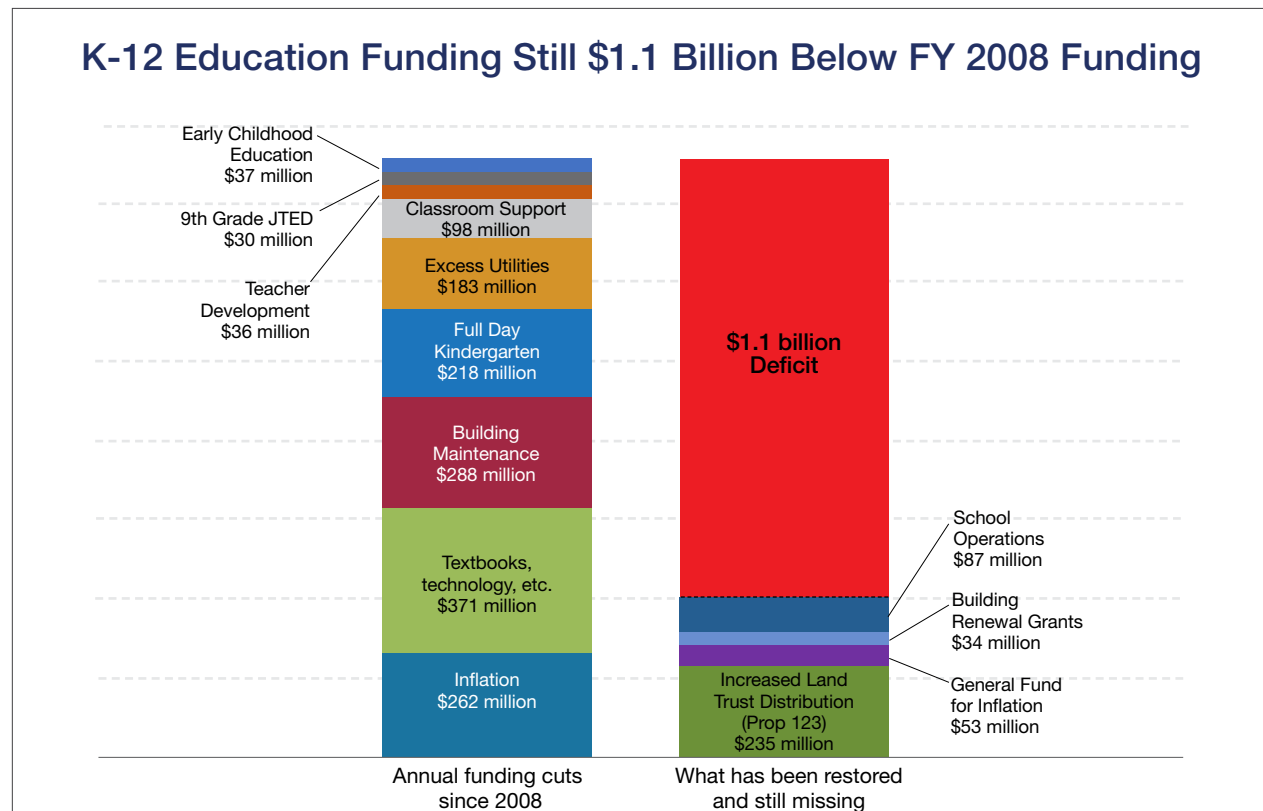


## How does the state budget impact having a good public school in my neighborhood?

Between 2008 and 2014, Arizona had the largest cuts to public education funding in the nation—\$1.8 billion in state funding was cut. These cuts lead to less resources for our neighborhood schools which impact the education our children receive. These cuts include:

- Lawmakers eliminated state funding for full-day kindergarten. Schools now receive funding for half-day kindergarten only; districts can offer full-day kindergarten but have to pay for it either by cutting spending somewhere else or charging tuition.
- The “building renewal” funding formula for schools to repair and maintain school buildings was repealed from state law as part of the fiscal year 2014 budget and replaced with a grants program that is less than one-tenth of what the formula called for. There is a pending lawsuit against the state filed by some school districts and taxpayers claiming the state's failure to adequately fund school facilities is a violation of the state constitution, has left Arizona school districts with over \$1 billion in unfunded school repairs, and has forced neighborhood school districts to ask their local voters to raise their property taxes to fund the unmet facility needs through the passage of bonds and overrides.
- The state budget suspends a portion of the additional assistance formulas that pay for textbooks, computers, technology, classroom supplies, etc. District schools will receive only \$73 million instead of the full \$455 million required by the formula, while charter schools will receive \$324 million instead of \$343 million.

The 2016 voter-approved settlement over inflationary funding, known as Proposition 123, only restored 18 percent of the cuts that had been implemented since 2008. There has been little effort to restore funding beyond the dollars allocated in Proposition 123. Though lawmakers appropriated some additional dollars for fiscal year 2018, **Arizona schools are still receiving \$1.1 billion less in funding than a decade ago**, resulting in overcrowded classrooms, an inability to fund new textbooks or technology, broken down school buses and leaky roofs, and a loss of critical support staff such as nurses and guidance counselors.



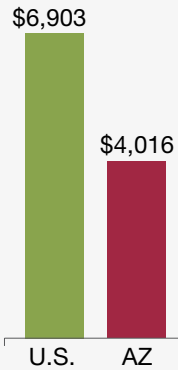
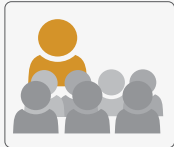
### Third Consecutive Year: Teacher Shortage Remains at Crisis Levels

- 1,328 vacant teaching positions at the start of 2017-2018 school year.
- 2,491 teaching positions filled with people who don't meet standard teaching requirements.
- More than 500 teachers abandoned their jobs or resigned during the school year, up 13 percent from previous year.
- Teacher pay is cited as the primary reason teachers leave the profession.
- Rural schools and those in lower socioeconomic levels are losing more teachers than those in more affluent areas.
- The 1 percent teacher pay bonus implemented for fiscal year 2018 does not change Arizona's teacher pay rankings or cover inflationary costs.

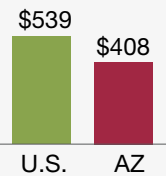
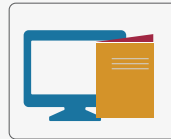
Source: Finding & Keeping Educators for Arizona's Classrooms (May 2017); ASU's Morrison Institute, and recent findings by the Arizona School Personnel Administrators Association.

## Arizona Spent Less Per Student than the National Average in ALL Categories in 2015

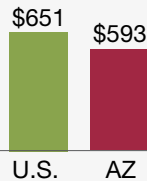
### Classroom Instruction



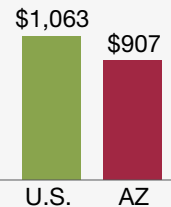
### Instructional Support



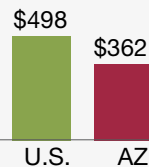
### Student Support



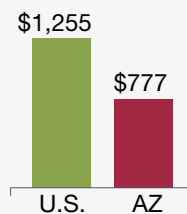
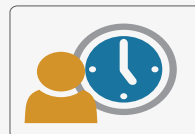
### Plant Operations



### Transportation



### Administration



Source: U.S. Census Bureau, Department of Commerce, Economics and Statistics Administration, Public Education Finances: 2015, issued June 2017.

## How do vouchers provide less accountability to ensure we are sufficiently educating our future workforce?

In the Alliance Bank 2017 CEO Survey, Arizona's business leaders said the availability of a trained workforce and the quality of our public education system are the top two challenges to doing business in Arizona. Similarly, those whose responsibility it is to recruit jobs and businesses to come to Arizona will often say that the top concerns that out-of-state businesses mention about coming to Arizona are the quality of our workforce and the quality of our public education system. Addressing those concerns will require all Arizona students upon graduation from high school to either be prepared with the education necessary to successfully obtain a college degree or to enter the workforce with the skills needed to have a successful career. For years, Arizona's public schools have been working to ensure they have the rigorous curriculum, standards, and accountability measures in place to ensure all Arizona students are moving toward those goals. Despite those efforts, when Arizona lawmakers expanded its school voucher program called Empowerment Scholarship Accounts (ESAs) in 2017 so that every student in Arizona is eligible to apply for a school voucher, it marks a shift away from accountability toward a system in which Arizona tax dollars are being diverted to religious and other private schools that are not required to follow Arizona's academic standards nor any other measure of accountability.

With ESAs, parents receive a debit card funded by state tax dollars in an amount based on the school funding formula (often around \$5,000) to pay for tuition for their child to attend religious or other private schools or for other education expenses. In addition to the lack of accountability, ESA vouchers also divert more dollars from our already underfunded public schools to private schools, thereby making the job of public schools to educate our future workforce that much more difficult. The public dollars diverted from public schools through private school tax credits and ESA vouchers has grown from \$14 million in 1999 to \$253 million in 2018.



ESA vouchers are also not a viable choice for many Arizona parents. Most rural areas have no private schools, and many low-income students will not be able to use the vouchers because their parents cannot afford transportation, uniforms, books and fees and tuition costs above the voucher amount. The tuition at many Arizona private schools is over \$10,000. The voucher expansion gives no priority to students with special needs, and high-income students are the primary users. This means the richest families in our state who can afford to send their children to private school from kindergarten through high school can now get subsidies from our tax dollars every year.

### Key Findings of Review of Arizona's School Voucher Program

The review looked at the 2,212 empowerment scholarship accounts (vouchers) that were awarded in fiscal year 2016 which at the time eligibility was limited to certain students with disabilities or who were attending public schools that were assigned a grade of D or F.

- Identified more than \$102,000 in misspending over a 5-month period including parents who accepted private school voucher money and then enrolled child in public school and parents who purchased items that are not allowed such as an account on a dating web site and groceries.
- Arizona Department of Education reported it did not have sufficient staffing to conduct timely reviews of monthly expense reports submitted by voucher recipients.
- Arizona Department of Education was only able to recover 14 percent of monies misspent.

Source: Arizona Auditor General, June 2016.

## What is Arizona doing to ensure every Arizonan has access to affordable post-secondary education and job training opportunities?

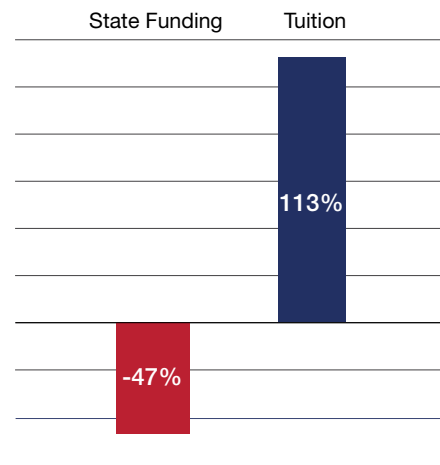
State funding for Arizona's three public universities has dropped 47 percent since 2008, when adjusted for inflation, and state funding for the state's two largest community college districts has been eliminated during that time period. The result is skyrocketing tuition and post-secondary education that is less accessible making it more difficult for Arizona to put forward the trained workforce it needs to attract quality jobs.

No state has cut funding more from higher education since 2008 than Arizona. Per student funding for Arizona's public universities is \$6,721 less than 2008 levels, when adjusted for inflation. Since 2003, base tuition and fees for Arizona residents at the state's universities has increased 315 percent to 370 percent. Comparatively, tuition and fees for in-state students have increased at Arizona's public universities by nine to ten times the rate of inflation and approximately twelve to thirteen times the rate of increase of median family income in Arizona over the same period of time.

Cuts to Arizona-funded financial aid have made post-secondary education out-of-reach to even more Arizona families. The FY 2018 budget reflects a decrease of 75 percent since 2008 in state-funded financial aid dollars available to Arizona's graduating high school seniors. According to Annie E. Casey's Data Center, 49 percent of Arizona's

K-12 students live at 200 percent poverty level, or below. These students have a critical need for student financial assistance in order to participate in a postsecondary education experience. Moderate-income students often face significant barriers to affording post-secondary education as well. Frequently, the expected family contribution for moderate-income students exempts them from federal and institutional need-based grant aid eligibility, leaving them with few options for grant aid if they do not meet qualifications for merit-based aid. At the same time, moderate-income students may not be able to afford to pay full price. The effect is one of having too much income and not enough.

### Tuition\* Has Increased While State Funding Has Fallen 2007-2008 to 2017-2018 (Adjusted for Inflation)



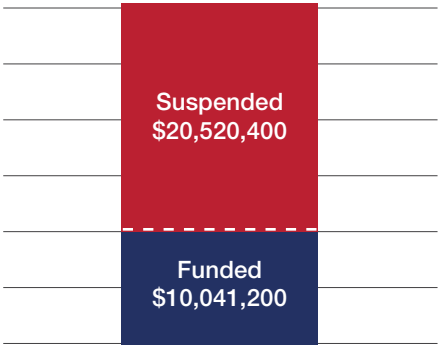
\* Average in-state tuition for ASU, NAU, and UA.  
Source: Joint Legislative Budget Committee Staff Appropriations Reports, FY 2008 and FY 2018.



Increased state-sponsored grant aid has the potential to markedly benefit moderate-income students as well as low-income students. With more state grant aid for low income students, some portion of tuition set-asides could be used to provide grant aid to moderate-income students, thereby creating access to post-secondary education for even more students.

State funding cuts are also having a significant impact on our community college systems. In 2015, state funding for the state’s two largest community college systems (Maricopa and Pima Community Colleges) was completely eliminated, a loss of almost \$80 million compared to what the two community college systems received from the state in 2008. In order to make-up for the lost funding, community colleges have had to increase tuition and raise local property taxes and have lost valuable faculty due to the inability to provide pay raises.

**Arizona’s University Financial Aid Trust Fund Receives Only One-Third of What the Statutory Formula Requires**



Source: Joint Legislative Budget Committee Staff Appropriations Reports, FY 2018.



## How does access to affordable child care serve as a barrier to working and going to school?

For many Arizonans, having access to affordable, quality child care is the most significant challenge they face to joining the workforce or going back to school to get the skills needed to get a good paying job. Arizona ranks the 3rd lowest state in the nation for women's participation in the workforce with 59 percent of all individuals of working age who are not in the workforce being women. For many women, access to affordable child care is the single biggest barrier to entering the workforce.

The monthly median cost of care in a full-time licensed child care center in Arizona is \$715. The monthly federal poverty level for a family of four with two children is \$2,050. That means the cost of unsubsidized child care for two children (\$1,430) equals 70 percent of their monthly income.

In Arizona, child care assistance is available through three state agencies.

- **First Things First** funds a limited number of scholarships to low-income families for children birth through age 5 who receive care at a center or in homes that are enrolled in the agency's Quality First Program. The scholarships are administered by the child care provider and are available on a first-come, first-serve basis to those families that meet the eligibility criteria. Ninety percent of First Things First's funding is from a dedicated tobacco tax.
- **The Arizona Department of Economic Security (DES)** administers child care assistance programs that are funded with state and federal monies. These programs help eligible families with the cost of child care to enable parents to work or to get education and training to help with employment. Children whose parents currently or previously participated in the Jobs program make up about one-third of the subsidies while children in low-income working families make up two-thirds. DES has a wait list for low-income working families due to the number of child care assistance requests they receive and lack of funding. As of October 2017, there were 4,317 children (2,540 parents) on the waiting list. The amount of subsidy that Arizona provides is based on market rates in existence in 2000, which is the oldest market rate used by any state.
- **The Department of Child Safety** provides child care assistance for children involved in the state's child welfare system.

In fiscal year 2008, 42 percent (\$84 million) of the \$198 million spent on child care subsidies (excluding First Things First) came from the state's general fund. Today, the only general fund dollars (\$7 million) are appropriated to the Department of Child Safety. The Department of Economic Security receives \$98 million in federal funds only which provide child care subsidies for families receiving education and training to help with employment as well as for low-income working families.

## State General Fund Monies for Child Care Subsidies Have Evaporated Over the Past Decade

	2008	2016	2018
State General Fund	\$85,583,900	\$5,000,000	\$7,000,000
Federal Funds	\$113,999,100	\$125,396,600	\$125,396,600
<b>Total</b>	<b>\$198,482,000</b>	<b>\$130,396,800</b>	<b>\$132,396,600</b>

In addition to decreasing state funding for child care subsidies, the federal funds the state receives in the form of a block grant for Temporary Assistance for Needy Families (TANF) that are to be used primarily for child-care for low-income families and for job training and other work-related activities have been increasingly diverted by the Arizona legislature to fill budget holes at the Department of Child Safety.

## Share of Arizona's Federal and State TANF Spending on Welfare Reform Activities

	2001	2015
Basic Assistance	31%	6%
Work Activities	11%	2%
Child Care	16%	0%
Child Welfare (considered a non-core activity)	N/A	49%





## How have state budget cuts impacted the availability of affordable housing in Arizona?

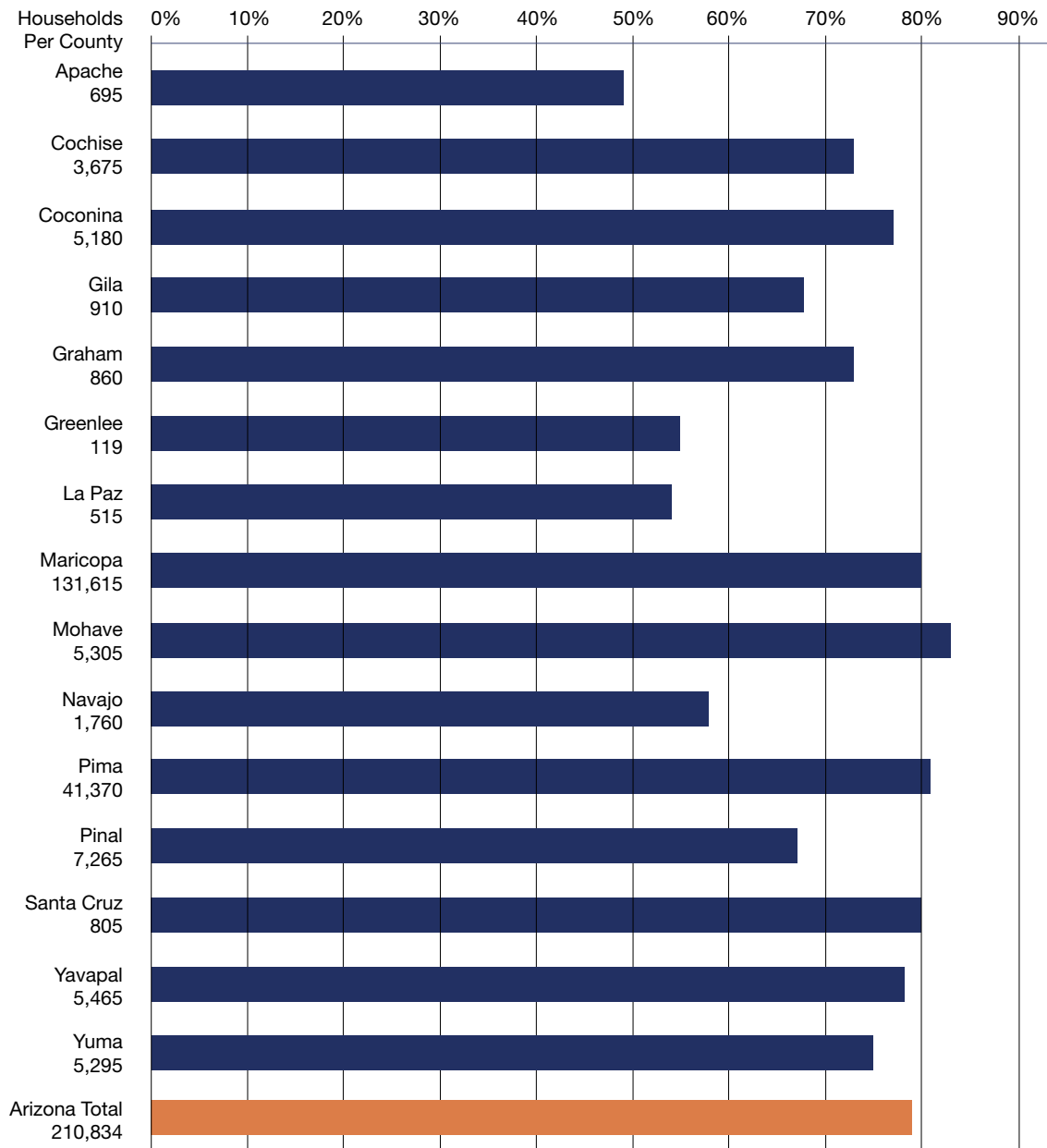
Having a sufficient supply of affordable housing for Arizonans at all income levels is a key element for fostering a strong workforce and economy. People living in homes they can afford have more to spend for other needs like education, food, clothing, and transportation which supports businesses in their communities. Children with stable homes will likely do better in school, and when people can count on their home, a stronger sense of community is created and neighborhoods are safer.

According to the Arizona Housing Alliance, approximately one-third of all Arizona households are renters. There are almost 270,000 very low-income renters in Arizona. More than 210,000 of these renters, or 78 percent, are paying significantly more than the recommended 30 percent of their income for housing costs.

The Housing Trust Fund is a state resource devoted to addressing Arizona's housing needs. Created in 1988, it is funded from the sale of unclaimed property, which is assets such as stocks or savings accounts abandoned by the owner, often due to death without a will. The Housing Trust Fund was initially funded by 35 percent of unclaimed property proceeds, and then increased to 55 percent to better address rural housing needs. Prior to the Great Recession in 2008, the Housing Trust Fund received over \$30 million, but in 2010 the Housing Trust Fund was capped at \$2.5 million as more of the unclaimed property funds have been diverted to replace general fund support for the Department of Revenue and to increase deposits into the general fund. Prior to these cuts, the Housing Trust Fund acted as a magnet for private investment, and leveraged over \$350 million in federal dollars annually. In past years, the Housing Trust Fund has helped build apartments and homes for seniors, people with disabilities, and in rural communities. It is estimated that an investment of \$550,000 of Housing Trust Funds in a 75-unit apartment complex generates over \$1.6 million in taxes and over 120 jobs.



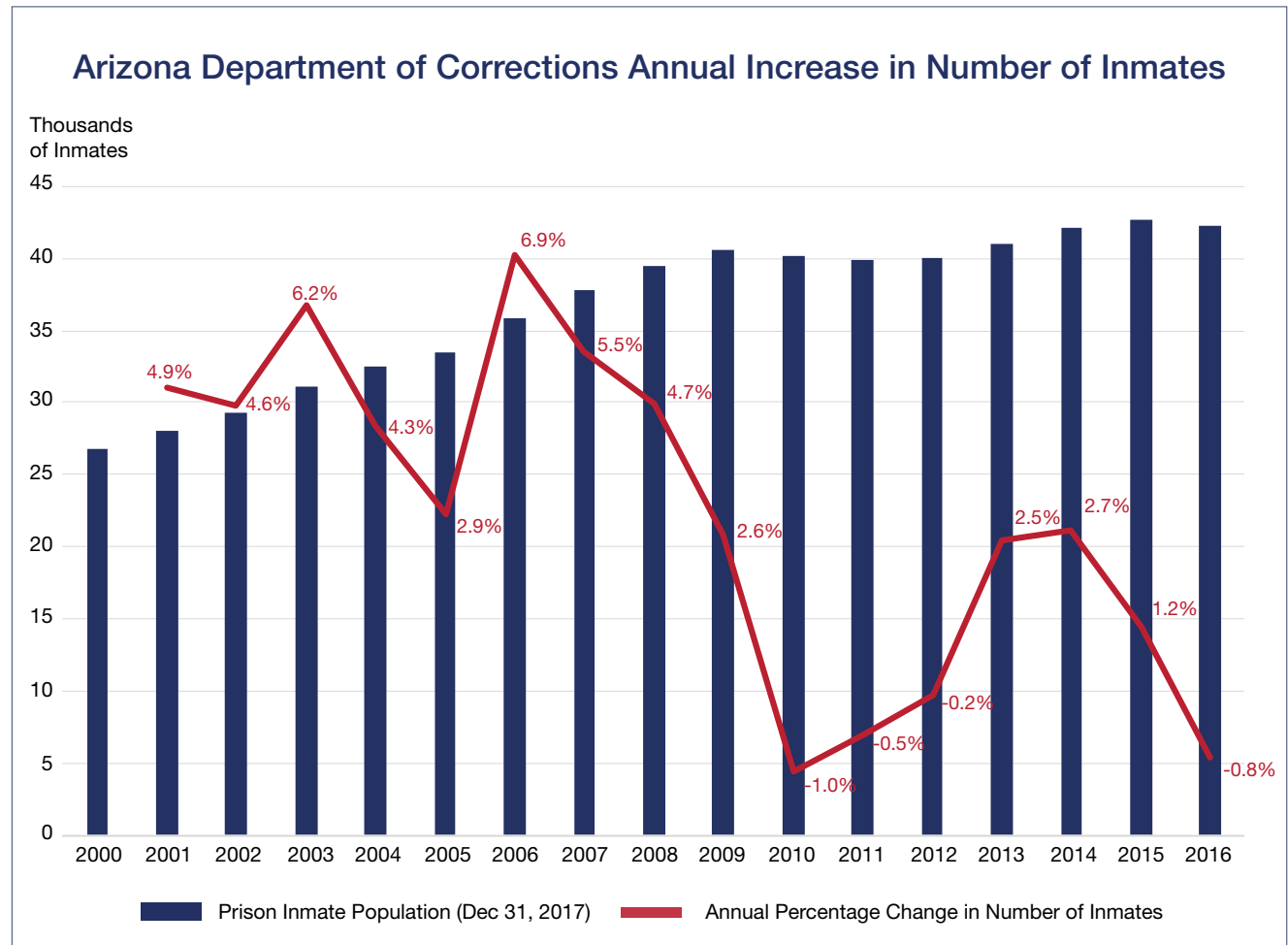
## Number and Percent of Low-Income Renter Households Paying More than 30 Percent of Income for Rent



Source: Arizona Housing Alliance

## What impact does Arizona's criminal justice system have on our workforce?

All Arizonans have an interest in a justice system that keeps us safe and is working to rehabilitate individuals reentering into our communities. Today, Arizona remains in the top five states with the highest incarceration rates in the nation, and recidivism rates are on the rise.



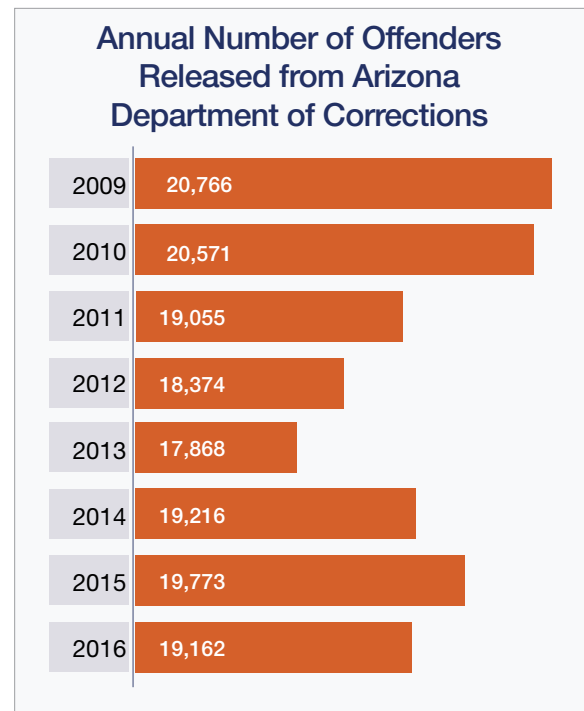
In 2016 over 43,000 adults became justice involved, resulting in 19,453 individuals being removed from society and sentenced to an average of 2.2 years of imprisonment, costing Arizonans at least \$900 million dollars.

Today the Arizona Department of Corrections' budget makes up 11 percent of the state's general fund and is well over \$1 billion. In the past 7 years, the Arizona Department of Corrections' budget has increased by 40 percent. According to the most recent National Association of State Budget Officers report, Arizona ranks fourth highest among all 50 states in the percentage of total general fund expenditures on corrections.

Incarceration and Alternative Costs	Cost per person, per year
Prison	\$24,229 (average \$66.38/day)
Jail*	\$32,985 (average \$90.37/day)
Drug Court*	\$3,309
Drug Treatment	\$3,085
Standard Probation*	\$1,919.90 (average \$5.26/day)
Intensive Probation*	\$7,442.35 (average \$20.39/day)

\*Note: Data for Maricopa County only.

With over 20,000 individuals leaving prison each year and joining the workforce, research has proven that access to career and technical services and substance abuse treatment programs while incarcerated is imperative to an offender successfully rejoining society with new skills. Yet, Arizona Department of Corrections provides less than 5 percent of the prison population with Career and Technical Education and even less with treatment services. At any given time, 75 percent of the prison populations is flagged for needing moderate to intensive substance abuse treatment, while only 2 percent of the prison population ever receives treatment prior to being released.





In 2017, Governor Ducey passed three executive orders in relation to drug abuse treatment and eliminating any questions on initial state job applications about whether a person has a criminal record. While these steps are important and necessary, it is notable that they are reactive rather than preventive measures.

Today the state continues to spend over half million dollars per day to incarcerate people whose most serious charge is a drug offense and over \$2.3 million a day to incarcerate at least 35,000 people a day. Through the investment in career and technical education and increasing access to substance abuse treatments in Arizona, its estimated that Arizonans could cut the prison budget by an estimate of at least 20 percent and better equip more than 20,000 people annually to enter the workforce.

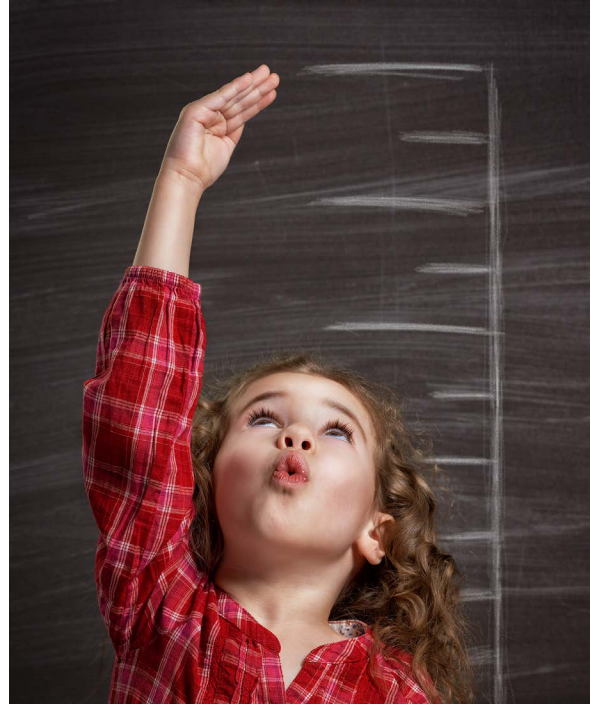




## Section IV: Looking Ahead

For almost three decades, tax cuts have been the tool of choice our legislature has used to attract new businesses and jobs to our state and to make us more economically competitive. It is time to ask whether those tax cuts are giving us a sound return on our investment or whether we could more effectively attract more jobs and produce better economic opportunities for all by instead using those foregone tax dollars to invest in other priorities like public education, post-secondary education and infrastructure. 2018 is a critical year

for our state as we decide who will lead Arizona into the future. We should all be asking those potential leaders what are their strategies and plans to ensure that Arizona is a place that is removing barriers to working and getting an education and is instead providing people with the opportunities that will reward their hard work with greater prosperity and thriving communities. Whether it is a new tax cut, or an expansion of a tax credit, or additional investments of tax dollars into our schools or other priorities, each of those decisions are related to the other, and can be the difference between a state government that picks winners and losers and one that creates opportunities for all.





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