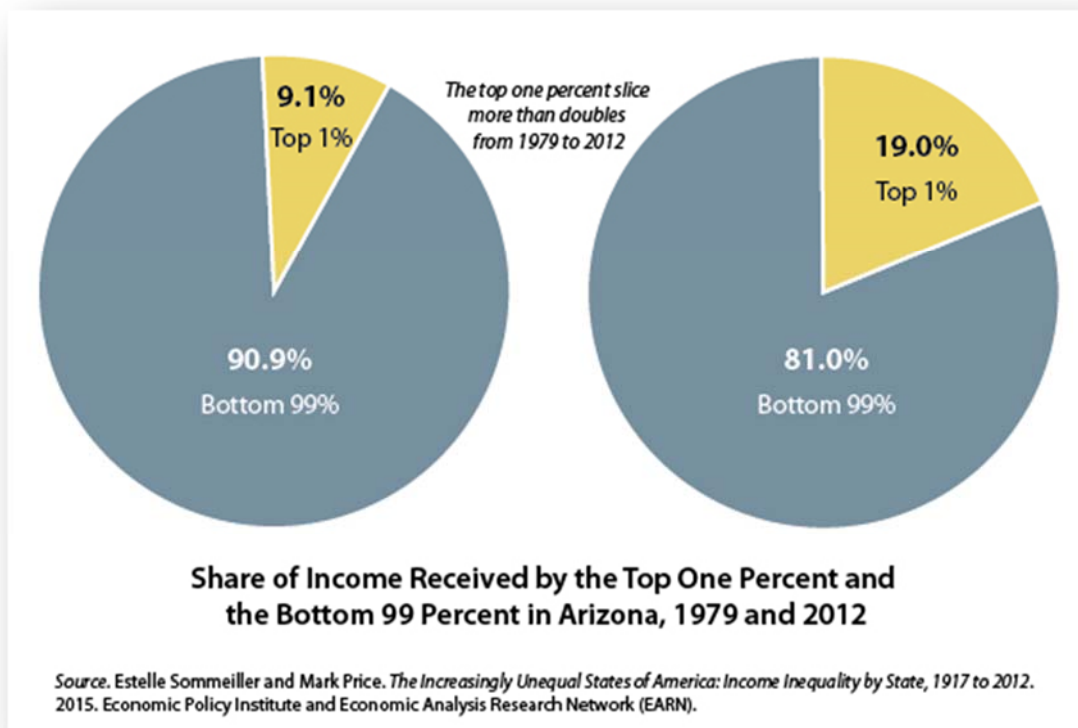


Tax Fairness: An Answer to Arizona's Budget Problems

In Arizona, income inequality is getting worse: the top one percent—those with incomes averaging \$877,466 in 2012—now get nearly *a fifth* of all the state's income. They also pay lower tax rates than everyone else—*half* the rate of the middle class. If the top one percent paid taxes at the same rate as middle-income Arizonans, the state could solve many of its budget problems—raising \$1.2 billion a year for education, infrastructure, health care, pensions and job creation. If the top fifth paid the same tax rate as the middle fifth, Arizona would have \$2.74 billion more to meet state revenue needs.

Income Inequality is More Severe than Ever

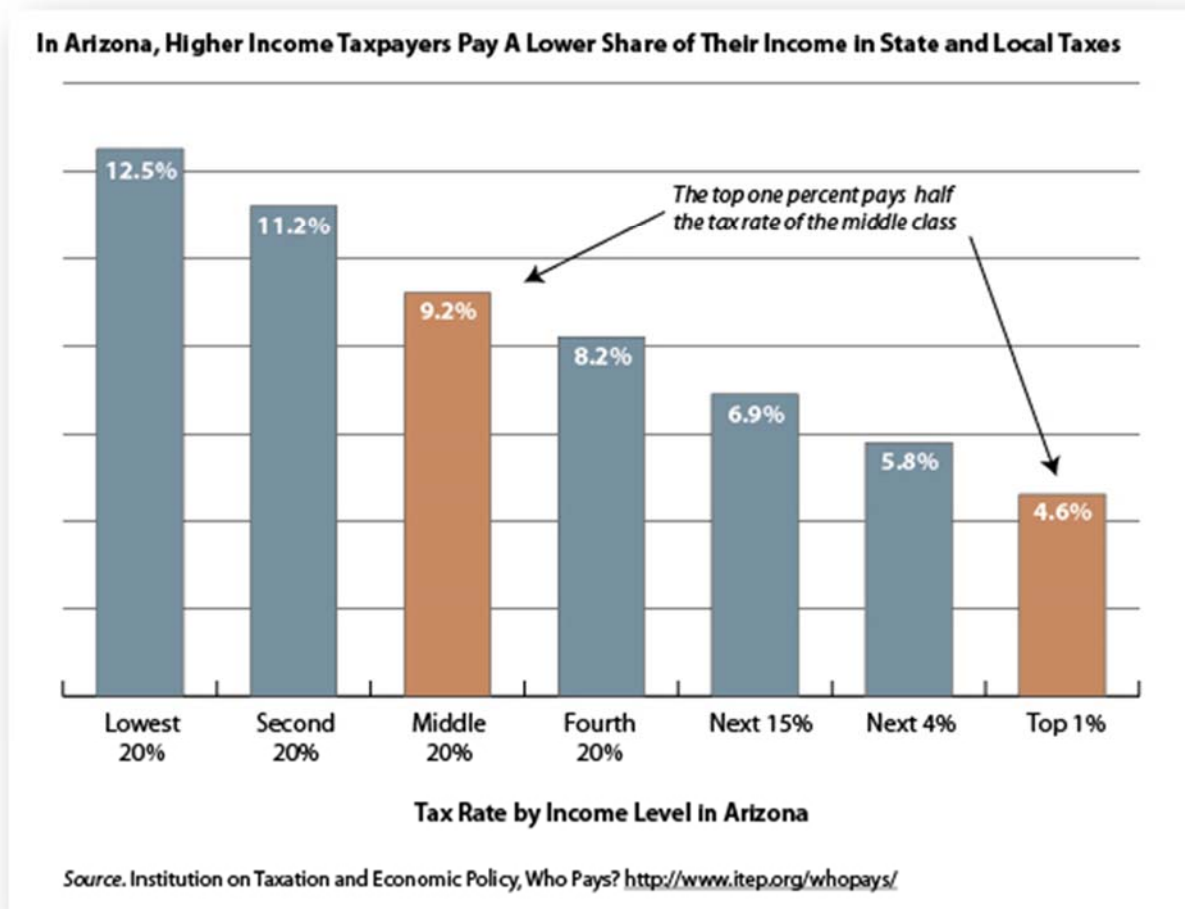


In the 1970s, the top one percent of taxpayers received less than 10 percent of total income in Arizona. By 2012, their share of Arizona's total income had more than doubled, to nearly 20 percent. This shift means that, every year, about \$29 billion in income now goes to just one percent of Arizonans.¹

For context, \$29 billion is more than three times the Arizona state general fund budget and 60 times the annual cost of paying down the state's pension debt.²

High-Income People Pay Far Less of Their Income in Taxes than the Rest of Us

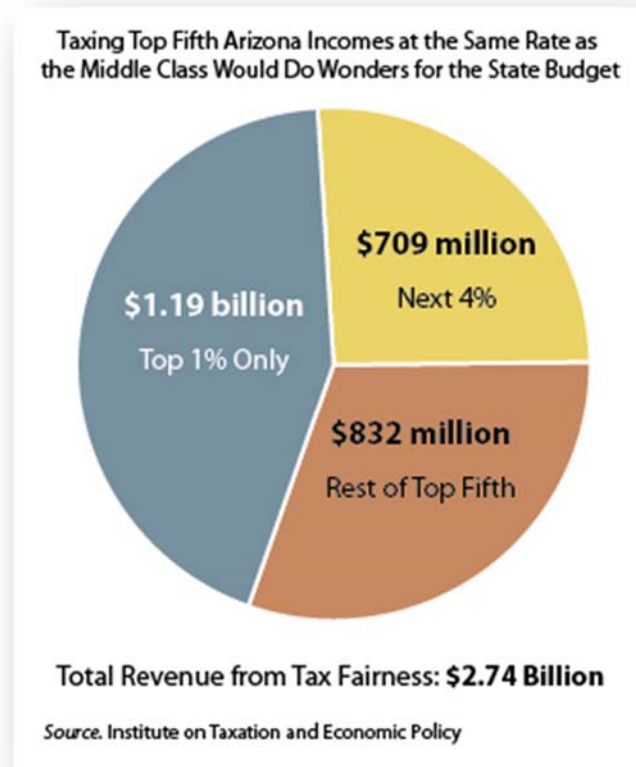
The Institute on Taxation and Economic Policy ranks Arizona one of the “Terrible Ten” for its extremely regressive tax system. High-income residents pay a far smaller share of their income in state and local taxes than middle-income residents. The high-income one percent of Arizonans pay just 4.6 percent of their income in taxes, while the middle fifth pay twice that rate: 9.2 percent. Arizona’s lowest income families pay even more: 12.5 percent.



There are a few basic reasons Arizona’s tax system is so inequitable, and the solutions are simple.

- Arizona has a low top income tax rate of 4.54 percent, the 12th lowest among the 41 states that have an income tax.
- Arizona excludes some capital gains income from the state income tax.
- Arizona lacks two common tax features that benefit low-income taxpayers: a refundable state Earned Income Tax Credit (EITC) and limits on property taxes for low-income taxpayers
- Arizona taxes groceries.

Taxing the One Percent at Middle-Class Rates Would Do Wonders for the Budget



Taxing upper-income groups at the same overall tax rate as middle-class Arizonans would relieve pressure on the state's budget. Taxing just the highest one percent at the rate that the middle fifth pays would raise \$1.2 billion in new revenue. That would more than fill Arizona's budget hole (which could grow to \$1 billion by FY 2016).³ The annual cost of paying down Arizona's pension debt (\$479 million) would cost only about two fifths of the annual revenue from tax fairness on the top one percent.

Extending tax fairness to the top fifth would generate an estimated *\$2.74 billion* in additional revenue each year, roughly 30 percent of Arizona's General Fund budget. This amount could fill Arizona's budget hole, pay off pension debt, restore funds cut from Arizona higher education since 2007-08 (\$425 million), and still leave a third of the revenue for other education funding, job creation, or infrastructure.

Tax Fairness is Not Rocket Science

There are many ways that Arizona could embrace tax fairness. It could emulate other states by making the income tax more progressive, in part by taxing all capital gains.

After 30 years of a middle-class squeeze, it's time to restore balance. One percent of Arizonans get twice the share of income they got 30 years ago—taxing them at half the middle-class rate is the wrong

direction. Solving the budget deficit through tax fairness while restoring education and infrastructure will help revitalize Arizona's economy.

END NOTES

¹ Since this report relies on Internal Revenue Service taxable income data, total income (for the 100 percent) is considerably less than total personal income by state, which also includes transfers such as Social Security payments and other social safety net payments. This is the main reason why the 20 percent of income received by the top one percent each year is well below 20 percent of "personal income" in the state.

² This assumes that Arizona's cumulative \$14.4 billion in unfunded pension liabilities is paid off in equal installments over 30 years. Estimate of unfunded pension liabilities from Pew Charitable Trusts, *The Fiscal Health of State Pension Plans*, March 2014, online at

<http://www.pewtrusts.org/~media/Assets/2014/03/31/PewStatesWideningGapFactsheet2.pdf>

³ For an estimate of Arizona's budget deficit, see Arizona Joint Legislative and Budget Committee (JLBC), "FY2016 JLBC Baseline," January 16, 2015, online at <http://www.azleg.gov/jlbc/16BaselineSlideshowFull.pdf>