

Budget Considerations for a Proposed Transaction Privilege Tax (TPT) and Use Tax Increase

The City of Phoenix is the largest municipality in Arizona with close to 1.7 million residents and is the fifth largest in the United States. Phoenix has experienced significant growth in population and geographic size in the past forty years and relies heavily on local transaction privilege (sales) tax revenues to provide the resources necessary to pay for essential programs and services desired by our City Council and residents. The General Fund and Special Revenue Funds pay for critical core services the community relies on every day including but not limited to Police and Fire emergency response, Parks and Recreation, Libraries, Transit, Streets, Community and Senior Centers, Planning and Development, Neighborhood Services and Human Services including homelessness.

The table below provides comparison data from 1980 to the current fiscal year to demonstrate the significant growth experienced in the City of Phoenix.

Category	1980-81	2024-25
Population	789,704	1,692,268
Area (Square Miles)	325.1	519.3
Total Street Miles	3,084	4,876
Municipal Parks	137	203
Library Branches	7	17
Police Calls for Service	452,350	616,180
Fire Calls for Service	71,284	253,672
Equipment/Fleet Units	4,497	7,987
Building Inspections	196,356	285,000
Total City Full-time Employees	9,434.7	16,011.6
Total Employees per 1,000 population	11.9	9.5

Note: Data is from the City of Phoenix Budget Summary Documents.

The City of Phoenix has significant operational and infrastructure needs and has experienced high inflation in the past few years, increasing the cost-of-service delivery. Additionally, the State legislature has taken actions that limit local control and reduces ongoing TPT and state shared income tax revenue. To ensure the City of Phoenix can continue delivering exceptional services to the community and maintain a statutorily required balanced budget a local TPT and Use Tax increase may be considered by the City Council on March 18, 2025, to increase resources. Proposed budget reductions may also be considered to resolve forecasted structural imbalances. Detailed information on the forecasted General Fund Budget for FY 2025-26 and Multi-year Forecast will be presented to the City Council on February 25, 2025.

Phoenix's local TPT rate has not been increased since 1986 to support General Fund programs and services. Nonetheless, the General Fund programs and services costs have grown 486% from the adopted budget in FY 1985-86 to FY 2024-25. The last TPT rate increase was in 2016 and was dedicated to Transportation.

A history of Phoenix's TPT rate increases and the reason for the increase is provided in the table below:

TPT Rate	Effective Date	Fund
2.3%	January 1, 2016	Transportation
2.0%	December 1, 2007	Public Safety
1.8%	June 1, 2000	Transportation
1.4%	November 1, 1999	Parks & Preserves
1.3%	December 1, 1993	Public Safety
1.2%	July 1, 1986	General Fund

The State enacted Senate Bill 1131, which prohibits municipalities from collecting TPT on residential rental property starting January 1, 2025. This action by the State to eliminate an ongoing City revenue stream will have a significant negative impact to the General Fund, Public Safety Specialty Funds (PSSF), Parks and Preserves, and Transportation 2050 Funds. The total estimated impact for FY 2024-25 is approximately \$35.4 million and the ongoing annual impact beginning in FY 2025-26 is \$85.5 million. **The estimated cumulative impact to all funds beginning in 2024-25 through 2027-28 is \$302 million.**

The chart below provides the estimated revenue loss of residential rental TPT (in millions) by City fund for FY 2024-25 to FY 2027-28.

Fiscal Year	General Fund	Public Safety Specialty Funds	Parks & Preserves Fund	Transportation 2050	Total
24-25 Est*	18.5	4.6	1.5	10.8	35.4
25-26 Est	44.6	11.2	3.7	26.0	85.5
26-27 Est	46.2	11.6	3.8	27.0	88.6
27-28 Est	48.3	12.0	4.0	28.2	92.5
24-25 to 27-28	157.6	39.4	13.0	92.0	302.0

*SB 1131 eliminates local TPT on residential rental property effective January 2025. All values are subject to change based on updated TPT forecasts.

Additionally, in 2021 the State enacted Senate Bill 1828 which reduces individual income tax rates beginning in tax year 2022. The City receives state shared income tax based on actual collections from two years prior and is distributed entirely to the General Fund. B&R staff rely on projections from the Joint Legislative Budget Committee (JLBC) to estimate this revenue stream for budget development. This action by the State is expected to result in less ongoing state shared income tax revenue to the General Fund compared to prior projections had the tax rate not been decreased.

Other Budget Challenges and Unfunded Needs

Fire Department Emergency Response

The Phoenix Fire Department (PFD) provides lifesaving services to all Phoenix residents and visitors and includes emergency medical and transportation services, all-hazards incident management, property protection through fire suppression, and community risk reduction efforts. The recent fire catastrophe in Los Angeles, CA serves as a reminder the importance of adequately resourcing the Fire Department to ensure sufficient levels of staffing, equipment and facilities are ready to respond to emergencies. A critical measurement of the PFD effectiveness in operations is emergency response time and is measured from the time of dispatch of an emergency apparatus to when the unit arrives on scene. The National Fire Protection Association (NFPA) establishes the standard fire departments utilize to measure performance. Currently, the PFD's response times exceed the NFPA established standards. While the department continuously evaluates innovative ways to improve response times,

additional resources are needed to increase the number of fire stations and facilities, personnel, and equipment to keep pace with the significant growth in geographic area and population the department must serve.

Homelessness

The Office of Homeless Solutions (OHS) has made tremendous progress in addressing homelessness over the last two years. Investments in the infrastructure of the region's homeless services system have been monumental. As we move out of pandemic-era funding, OHS has unfunded needs necessary to continue its momentum and ensure the transformational projects and services implemented in the last two years can continue. Also important to note on November 5, 2024, voters passed Proposition 312 *Property Tax; Refund; Nuisance Enforcement* that allows property owners beginning in Tax Year 2025 to apply to the Arizona Department of Revenue for a property tax refund if the owner documents expenses caused by a city, town, or county that either (1) declines to enforce existing laws prohibiting illegal camping, obstructing public thoroughfares, loitering, panhandling, public urination or defecation, public consumption of alcoholic beverages or use of illegal substances, or (2) maintains a public nuisance. The City is unable to project the potential costs associated with Proposition 312 but will have to identify a funding source. The passage of this proposition furthers the need for the City of Phoenix to address and provide resources for homelessness.

Resources will be needed in 2025-26 for homelessness estimated at \$9.0 million due to the expiration of American Rescue Plan Act funding. Funding is necessary for a portion of OHS operational costs, operational costs at an affordable housing site for very low-income older adults, operational costs at three emergency shelters (Rio Fresco, North Mountain Healing Center, and the temporary Washington Shelter) and heat relief efforts. The need in 2026-27 and going forward is estimated at \$25.0 million and will fund a portion of OHS operational costs, the temporary Safe Outdoor Space, operational support for five emergency shelters (Rio Fresco, North Mountain Healing Center, the temporary Washington Shelter, Central Arizona Shelter Services, and the Phoenix Navigation Center), some operational costs at the Key Campus and heat relief efforts. Staff will continue to seek additional external funding for these programs, and evaluate other City funding sources, which if received would offset the need for a portion of the General Fund request.

Ongoing Operating Costs for the 2023 General Obligation Bond Program

Phoenix voters approved a \$500 million General Obligation (G.O.) Bond Program in November 2023 that will provide the resources necessary to build, rehabilitate, expand and enhance City facilities. The program includes resources for fire stations, parks, regional pools and splash pads, libraries, community and senior centers, police stations, affordable housing, arts and culture facilities, streets and storm drains. General Fund resources will be required beginning in 2025-26 for ongoing operating and maintenance costs for these projects. B&R is in the process of updating ongoing operating cost estimates with departments but based on information provided last fiscal year estimates range from \$2.2 million in 2025-26; \$10.7 million in 2026-27; \$18.4 million in 2027-28; and \$25.4 million annually starting in 2028-29.

Other budget challenges beyond the aforementioned include:

- Major facility maintenance needs for City buildings and rising costs to repair and replace vehicles, fire apparatus and equipment;
- Increased funding needs for critical information technology projects for cybersecurity, public safety, and criminal justice support;
- Demands from residents for additional or new General Fund services.

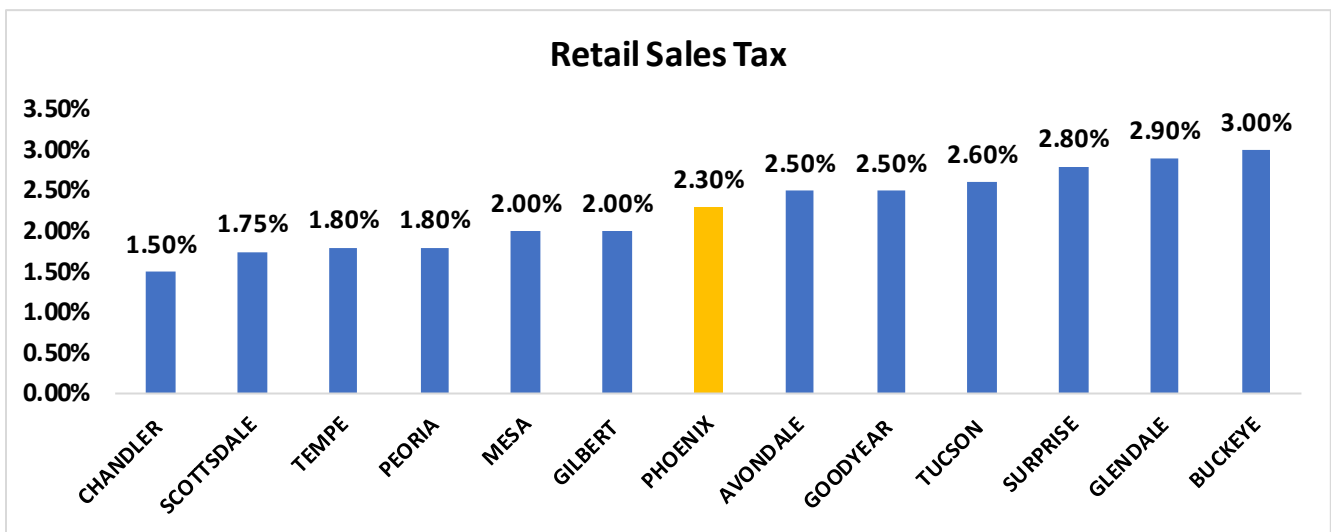
A TPT and Use Tax increase of up to 0.5% is proposed for consideration with an effective date of July 1, 2025, bringing the rate from the current 2.3% up to and including, but not exceeding, 2.8% for the business classifications below. This proposed amendment to Chapter 14 of the Phoenix City Code if

approved, is estimated to generate the revenue required to maintain City service levels and offset anticipated revenue decreases.

The table below provides the current TPT (and Use Tax) Rate and Proposed Rate (up to) by business classification.

Phoenix City Code Section	Business Classification	Current Rate	Proposed Rate (up to)
14-410	Amusements	2.3%	2.8%
14-415	Construction Contracting	2.3%	2.8%
14-416	Construction Contracting- Speculative Builders	2.3%	2.8%
14-417	Construction Contracting- Owner-Builders Who Are Not Speculative Builders	2.3%	2.8%
14-444	Hotel/Motel	2.3%	2.8%
14-425	Job Printing	2.3%	2.8%
14-427	Manufactured Buildings	2.3%	2.8%
14-435	Publishing (distribution only)	2.3%	2.8%
14-445	Rentals - Commercial Real Estate Property Rental, Leasing	2.3%	2.8%
14-450	Rentals - Rental, Leasing, Licensing of Tangible Personal Property (TPP)	2.3%	2.8%
14-455	Restaurant and Bars	2.3%	2.8%
14-460	Retail Sales Level 1 (first amount equal to or less than \$13,886 for a single item)	2.3%	2.8%
14-430	Timbering and Other Extraction	2.3%	2.8%
14-475	Transporting for Hire	2.3%	2.8%
14-610	Use Taxable Purchases & Out-of-State Vendors Level 1 (first amount equal to or less than \$13,886 for a single item)	2.3%	2.8%

Phoenix's largest TPT category is retail TPT. Phoenix's TPT rate on retail¹ purchases is lower than six other cities as shown in the following bar chart.



¹Tier 1 Retail < or = \$13,886 for a single item.

Estimated Revenue Increase by Category

The estimated amount of revenue that could be generated from a 0.5% TPT and Use Tax rate increase is provided in the table below by TPT category for the General Fund and Non-General Funds including the Phoenix Convention Center, Neighborhood Protection, Parks & Preserves, Public Safety Expansion and Transportation 2050.

A description of each fund and potential use of the increase is also provided below for reference.

TPT Category	Current Rate	Proposed Rate (up to)	Total Taxable Sales (estimate)*	General Fund \$ Increase (estimate)*	Non-General Fund \$ Increase (estimate)*
Amusements	2.3%	2.8%	\$818,831,913	\$2,136,083	\$1,958,076
Construction Contracting	2.3%	2.8%	6,208,931,435	9,448,374	21,596,283
Hotel/Motel	2.3%	2.8%	1,399,413,174	3,650,643	3,346,423
Job Printing	2.3%	2.8%	116,547,739	177,355	405,383
Publishing (distribution only)	2.3%	2.8%	13,063,565	19,879	45,438
Commercial Real Estate Property Rental, Leasing	2.3%	2.8%	4,756,086,391	12,407,182	11,373,250
Rental, Leasing, Licensing of Tangible Personal Property	2.3%	2.8%	2,839,370,478	7,407,053	6,789,799
Restaurant and Bars	2.3%	2.8%	5,477,797,739	8,335,779	19,053,210
Retail Sales Level 1	2.3%	2.8%	24,948,467,739	65,082,959	59,659,379
Timbering/Other Extraction	2.3%	2.8%	2,043	3	7
Transporting for Hire	2.3%	2.8%	1,350,522	2,055	4,697
Use Taxable Purchases & Out-of-State Vendors Level 1	2.3%	2.8%	1,412,251,391	3,684,134	3,377,123
Total			\$47,992,114,129	\$112,351,499	\$127,609,068

*Total taxable sales are estimated based on FY 2023-24 actuals. The Budget and Research Department is updating revenue estimates, which are subject to change.

Fund Description

General Fund: Resources are derived from taxes and fees used to provide the most basic of city services including police, fire, parks, library, municipal court, neighborhood and human services and street maintenance. The additional revenue generated from a potential TPT and Use Tax increase could provide funding to offset the loss of revenue due to the State's actions to eliminate residential rental TPT and lower the individual income tax rate to the current "flat tax", increase resources for the Phoenix Fire Department to improve emergency response times, continue efforts to address homelessness, and ensure the current level of General Fund programs and services can continue to be delivered to the community.

Phoenix Convention Center Fund: Resources are derived from a combination of rental and parking income and TPT. All resources are used for operating and capital infrastructure expenses and debt service for the convention center and venues. The additional revenue generated from a potential TPT increase could provide funding to invest in building infrastructure enhancements including audio visual,

lighting, technology, wayfinding, and sustainable features to make the Convention Center more competitive and desirable to meeting planners. Renovations to existing underutilized areas of the facility would also be made to create new rentable spaces to enhance the client and visitor experience. Planning for future expansion needs of the Convention Center would also be addressed.

Neighborhood Protection Fund: Resources are derived from a 1993 voter approved TPT increase earmarked for police and fire neighborhood protection programs, and police Block Watch programs. Revenues are allocated to the Police Department (70%), Fire Department (25%), and Block Watch Programs (5%). The additional revenue generated from a potential TPT increase could provide funding to offset the loss of revenue due to the State's action to eliminate residential rental TPT effective January 2025 and ensure fund solvency going forward as the cost of sworn personnel has increased significantly since 1993.

Parks & Preserves Fund: Resources are derived from a 2008 voter approved TPT increase earmarked to purchase state trust lands for the Sonoran Desert Preserve open space, and the development and improvement of regional and neighborhood parks to enhance community recreation. The additional revenue generated from a potential TPT increase could provide funding to offset the loss of revenue due to the State's action to eliminate residential rental TPT effective January 2025. Phoenix Parks and Preserve Initiative (PPPI) funds have played an instrumental role in providing Phoenix residents with a large and diverse parks and recreation system. Additional PPPI funding would be utilized to improve existing park facilities, community centers, and address aging infrastructure to ensure safe and accessible parks and recreation facilities across the city. Funding would also provide the resources needed to acquire and preserve land throughout the city expanding areas such as South Mountain Park and the Phoenix Sonoran Preserve, protecting open space and expanding the City's trail system.

Public Safety Expansion Fund: Resources are derived from a 2007 voter approved TPT increase earmarked for hiring additional police personnel and firefighters, hiring crime scene investigator teams to improve evidence collection, improving fire protection service and response times, and increasing other emergency services. Revenues are allocated to the Police Department (80%) and the Fire Department (20%). The additional revenue generated from a potential TPT increase could provide funding to offset the loss of revenue due to the State's action to eliminate residential rental TPT effective January 2025 and ensure fund solvency going forward as the cost of sworn personnel has increased significantly since 2007.

Transportation 2050 Fund: Resources are derived from a 2015 voter approved TPT increase to fund a comprehensive transportation plan. Revenues are allocated to the Public Transit Department (86.2%) and the Street Transportation Department (13.8%). The additional revenue generated from a potential TPT increase could provide funding to offset the loss of revenue due to the State's action to eliminate residential rental TPT effective January 2025 and implement the City's voter-approved Transportation 2050 Plan that improves multiple modes of transportation services for residents in all areas of the city. This includes local and commuter bus service, Dial-A-Ride, bus rapid transit, and light rail, as well as necessary funding to maintain street pavement, expand existing arterial roadways, and enhance safety for pedestrians, bicyclists, and vehicles in city streets and intersections. The funding will provide capital investments in critical transportation infrastructure projects, such as road widening projects, new transit park and ride facilities, and light rail extensions. It will also cover the costs of ongoing operations and maintenance, which are necessary to ensure transportation services are reliable and in a state of good repair. Additionally, the funding will help offset the loss of federal transportation infrastructure grants due to the upcoming expiration of the Infrastructure Investment and Jobs Act/Bipartisan Infrastructure Law.