

FY 2014
Baseline Book

January 2013

JLBC

FY 2014 JLBC Baseline Summary

January 2013

The FY 2014 Baseline provides an estimate of the state's annual General Fund balances through FY 2016. Beyond adopting the annual FY 2014 budget, the Legislature is required to provide 3-year revenue and spending projections in the budget bill. The JLBC Baseline revenue projections reflect a consensus economic forecast while the spending estimates represent active funding formula requirements. The Baseline is not a budget proposal, but an estimate of available resources after statutory requirements.

The 3-Year Baseline Budget Outlook

- In the FY 2014 Baseline, ongoing General Fund revenues are projected to be \$8.32 billion. In contrast, projected FY 2014 Baseline formula spending is \$8.67 billion – well above the ongoing revenue level.
- The FY 2014 Baseline, however, is balanced by using \$651 million of one-time monies remaining from the end of FY 2013. After adjusting for these funds, FY 2014's projected ending balance is \$310 million.
- During FY 2015 and FY 2016, the structural shortfall between ongoing revenues and spending remains. The projected FY 2015 cash balance is \$25 million, followed by a \$(70) million shortfall in FY 2016.
- The large projected FY 2014 ending balance may create an incentive for new initiatives above the Baseline. Any such proposals would effectively result in turning the \$25 million FY 2015 balance into a shortfall and increasing the FY 2016 shortfall.
- The Baseline does not include the impact of the Court of Appeals' K-12 inflation ruling. If upheld, the ruling would result in a FY 2015 shortfall of \$(223) million and a FY 2016 shortfall of \$(346) million.

General Fund Revenues

Total FY 2014 General Fund revenues are projected to be \$8.98 billion, including both ongoing revenues and the beginning balance. This amount is \$(385) million less than FY 2013.

- Based on the 4-sector consensus, FY 2014 base revenues are projected to grow by \$416 million, or 4.9%. This gain, however, would be more than offset by the loss of the temporary 1 cent sales tax.
- Given that 3-year projections are uncertain, a forecast's probability establishes the potential risk level. The likelihood of meeting or exceeding the Baseline forecast is 65%.
- Base revenue growth will be offset by transferring an additional \$(46) million to cities as part of the urban revenue sharing formula and by \$(47) million for previously authorized tax reductions.

General Fund Spending

At \$8.67 billion, the FY 2014 Baseline would increase spending by \$157 million, or 1.8%:

- K-12 spending would grow \$55 million due to the statutory funding formula. If the state concurs with the K-12 inflation court ruling, the cost would further increase by \$82 million in FY 2014.
- Prior to mandatory federal health care changes, Medicaid spending is projected to decline by \$(97) million due to overfunded FY 2013 caseloads and a higher federal match rate.
- Mandatory federal health care requirements are forecast to increase Medicaid costs by \$74 million, primarily due to greater participation by currently eligible non-participants. The Baseline does not include the optional expansion to 133% of poverty.
- Corrections' costs would increase \$9 million as 1,500 public and private prison beds begin to open.
- Debt service payments increase by \$20 million, primarily for the Phoenix Convention Center.

Budget Concerns and Risks

- Arizona continues to have the third lowest credit among the states, in part due to its structural shortfall.
- The state suspends \$678 million in annual formula spending – if funded, the structural gap would grow.
- As a remnant of the recession, the state continues to "rollover" \$1.2 billion in annual payments.
- Several factors create economic uncertainty: 1) the current slow growth/0% interest rate environment, 2) the outcome of "federal fiscal cliff 2" and 3) unforeseen natural disasters and political events.
- As a result, 3-year budget forecasts come with risks. A 1% change in revenue or spending growth rates could affect the balance by more than \$500 million in the third year.

Alternate Budget Scenario

- Given the budgetary risks, JLBC Staff has developed an Alternate budget scenario to allow the Legislature to evaluate the impact of a different set of assumptions.
- The Alternate reduces the long term revenue growth by 1% and adds \$500 million in spending above statutory formulas over 3 years, or an annual average increase of \$167 million.
- In this Alternate scenario, the state has a shortfall of \$(411) million in FY 2015 and \$(572) million in FY 2016. These shortfall estimates have not accounted for the state's \$450 million Rainy Day reserve.

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