
FY 2015 JLBC Baseline

Summary Version

January 17, 2014

JLBC

3-Year Budget Outlook

- ❑ The Baseline compares the 4-sector consensus revenue forecast with cost of current funding formulas through '17
- ❑ Under the Baseline scenario, the cash balance is \$327 M in '15, near \$0 in '16, and a \$(593) M shortfall in '17
- ❑ After adjusting the Baseline for the \$238 million HURF proposal, there are projected shortfalls of \$(256) M in '16 and \$(593) M in '17
- ❑ The cash balance estimates exclude the \$460 M available in the Budget Stabilization Fund

The Caveats

- ❑ The revenue forecast is based on moderate revenue growth – but assumes that a portion of ‘13 capital gain windfall was one-time
- ❑ Over 3 years, small percent changes in growth assumptions can have a substantial impact
 - Eliminating the 4-sector slow growth scenario, for example, could increase available revenues by \$468 M through ‘17
- ❑ Pending “budget” lawsuits could be significant. Retroactive K-12 inflation payments have a maximum exposure of \$1.26 B
- ❑ Baseline includes \$210 M to buy back debt in ‘17 under 2010 debt financing terms – but Executive could revise these terms

Legislative Considerations

- ❑ While there is a cash balance at least through '15, ongoing spending exceeds ongoing revenue in each year (a structural shortfall)
 - Through '17, the annual structural shortfall ranges from \$(328) M to \$(383) M
 - The \$895 M '13 carryforward keeps the cash budget balanced in the short term
- ❑ The state still annually suspends over \$300 M of funding formulas and rolls over \$1.2 B in spending (both primarily K-12)
- ❑ Among states, Arizona is tied for the 3rd lowest credit rating – but outlook has turned positive

Rating Agency Perspectives on Arizona – Revised from Stable to Positive Outlook

– Aa3 Moodys/AA- Standard and Poors

☐ Strengths

- Improving economy in terms of job and housing growth
- \$1.3 B budget balance and Rainy Day Fund at the end of '13
- Below average debt and pension liabilities

☐ Weaknesses

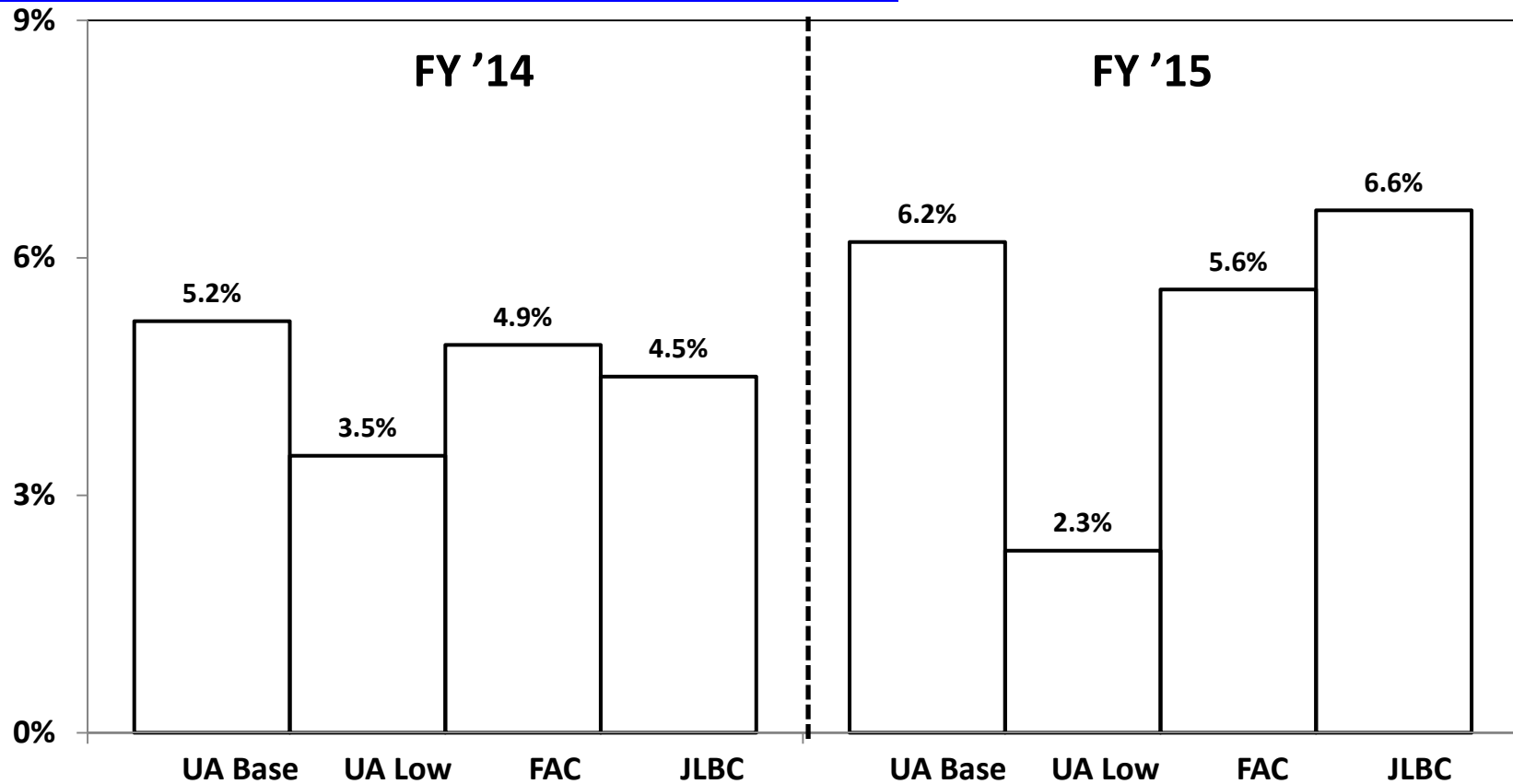
- Structural shortfall with expiration of 1 cent sales tax
- Constitutional restrictions on flexibility – Propositions 105 and 108
- Lack of financial “best practices” – statutory consensus forecasting and Executive mid-year budget reduction authority

Key Economic Measures

- Current Arizona Status Compared to Last Year

	December '12	December '13
Annual Jobs Added 10-yr Average = 73,700	50,900	47,500
Pending Maricopa Foreclosures Pre Recession Normal = 3,000	12,000	6,100
Arizona Annual Single Family Permits Pre Recession Normal = 40,000	15,900	17,700
Arizona Underwater Mortgages	39%	22%

Consensus Predicts Base Growth Rate of 4.3% in FY '14 and 5.3% in FY '15*



* After adjusting for small tax categories, the base growth rate is 4.3% in FY '14 and 5.3% in FY '15

Detail of FY '15 – FY '17 Revenue Changes

- Excludes Change in Beginning Balance

\$ in Millions

	<u>FY '15 Above FY '14</u>	<u>FY '16 Above FY '15</u>	<u>FY '17 Above FY '16</u>
Base Revenue Growth (5.3%/5.2%/5.6%)	477	480	544
Elimination of Fund Transfers	(154)	--	--
Previously Enacted Tax Legislation	(129)	(116)	(109)
Urban Revenue Sharing	<u>(48)</u>	<u>(11)</u>	<u>(31)</u>
Total	146	353	404
Net % Growth	1.7%	4.1%	4.5%

FY '15 – FY '17 Projected Spending Changes

	General Fund - \$ in Millions		
	<u>FY '15</u> <u>Above '14</u>	<u>FY '16</u> <u>Above '15</u>	<u>FY '17</u> <u>Above '16</u>
K-12 Formula	167	230	303
Medicaid Formula (AHCCCS/DHS)	15	83	93
DES Caseload/Backfill	45	27	29
University Parity	15	15	15
ADC Operating	25	11	3
Comm. Colleges Formula	(4)	2	2
Other	21	2	(3)
Additional Ongoing Spending	284	370	442
One-time Prison Capital	(50)	0	0
Debt Buyback	0	0	210
Total Spending	\$9,036 M	\$9,406 M	\$10,058 M

\$1.5 B 2010 Debt Financing Had Debt Buyback Provisions

- ❑ 2010 financing requires early buyback of debt if state generates large reserves – primarily the cash balance and Rainy Day Fund
- ❑ The projected '15 reserves requires the buyback of \$210 M – but would not occur until '17
- ❑ The Executive has the option of eliminating the buyback provision if it agrees to limit the investment yield on part of its portfolio to 4% - no legislative action required

Legislative Proposal

– 2-Year DPS/HURF Proposal

- ❑ Under permanent law, up to \$10 M of Highway User Revenue Fund can be used for DPS Highway Patrol expenses
- ❑ In 10 of the last 12 years, Legislature reduced DPS General Fund costs by using more than \$10 M of HURF
- ❑ The current Legislative proposal would entirely eliminate the HURF shift in '15 and '16 at a cost of \$238 M
- ❑ The proposal would increase local HURF by \$119 M over 2 years and increase statewide highway construction by a like amount

Updated FY '14 – '17 Budget Projections

Baseline

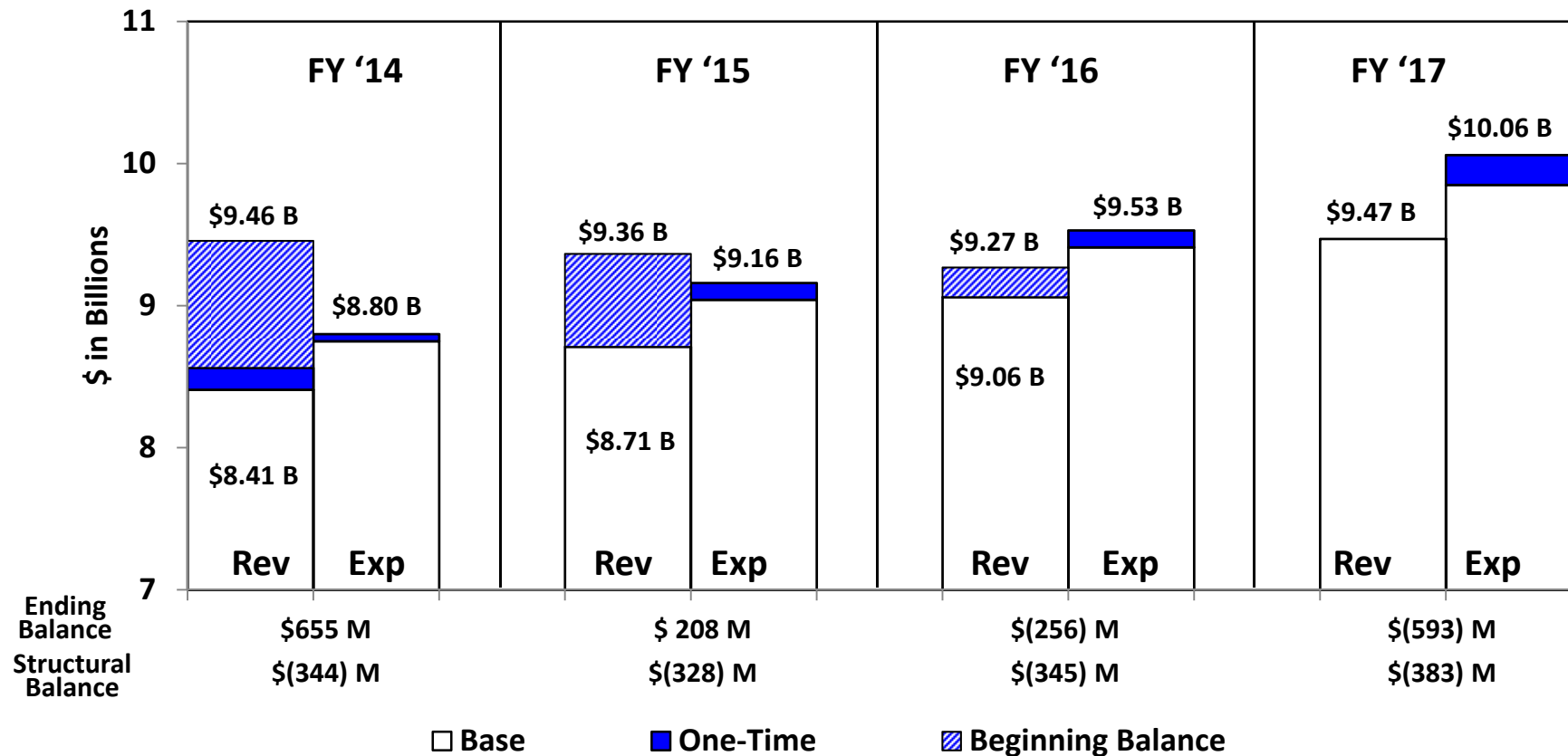
	<u>FY '14</u>	<u>FY '15</u>	<u>FY '16</u>	<u>FY '17</u>	
Balance Forward	\$895 M	\$655 M	\$327 M	\$0	\$(17) M
Baseline Revenues	\$8.56 B	\$8.71 B	\$9.06 B	\$9.47 B	
Baseline Spending	\$8.80 B	\$9.04 B	\$9.41 B	\$10.06 B	
Baseline Balance	\$655 M	\$327 M	\$(17) M	\$(593) M	\$(610) M

Baseline with HURF Proposal

Balance Forward	\$895 M	\$655 M	\$208 M	\$0	\$(256) M
Baseline Revenues	\$8.56 B	\$8.71 B	\$9.06 B	\$9.47 B	
Baseline Spending	\$8.80 B	\$9.04 B	\$9.41 B	\$10.06 B	
HURF Proposal	\$0	\$119 M	\$119 M	\$0	
Adjusted Balance	\$655 M	\$208 M	\$(256) M	\$(593) M	\$(849) M

FY'14 – '17 Revenues Compared to Expenditures

- Baseline Adjusted for HURF Proposal



JLBC Staff Suggested Process Improvements

- 1) Require independent contracted 3rd party oversight of significant information technology (IT) projects
- 2) Enhance and improve timeliness of income tax credit reporting through Department of Revenue IT improvements
- 3) Increase budget transparency
 - a) Line out Arizona State Hospital funding in DHS budget
 - b) Line out resources allocated for CPS in-home preventive services
- 4) Confirm school district charter conversion policy

**STAFF OF THE
JOINT LEGISLATIVE BUDGET COMMITTEE**

- Director Richard Stavneak
- Office Manager Linda Monsanto
- Deputy Directors Steve Schimpp
..... Stefan Shepherd
- Principal Economist Tim Everill
- Chief Economist..... Hans Olofsson
- Principal Fiscal Analysts..... Eric Billings
..... Jack Brown
..... Bob Hull
..... Art Smith
- Senior Fiscal Analysts..... Ben Beutler
..... Steve Grunig
..... Jon Stall
- Fiscal Analysts Henry Furtick
..... Matthew Gress
..... Ben Henderson
..... Micaela Larkin
..... Krista MacGahan
..... Tom Ritland
- Administrative Assistant/JLBC Clerk..... Kristy Paddack
- Administrative Assistant/JCCR Clerk..... Tera Scherer