
Finance Advisory Committee

Revenue and Budget Update

April 11, 2013

JLBC

Summary of April Forecast Update

- ❑ Forecast remains largely unchanged
 - 3 yr forecast base average annual growth declines from 5.7% to 5.5%
- ❑ While underlying fundamentals continue to improve, federal sequester has offset those gains
- ❑ Updated forecast reduces FY '16 General Fund Baseline by \$(30) M compared to January Baseline

Revenue Overview

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March Year-to-Date Growth Rate is 3.9% *

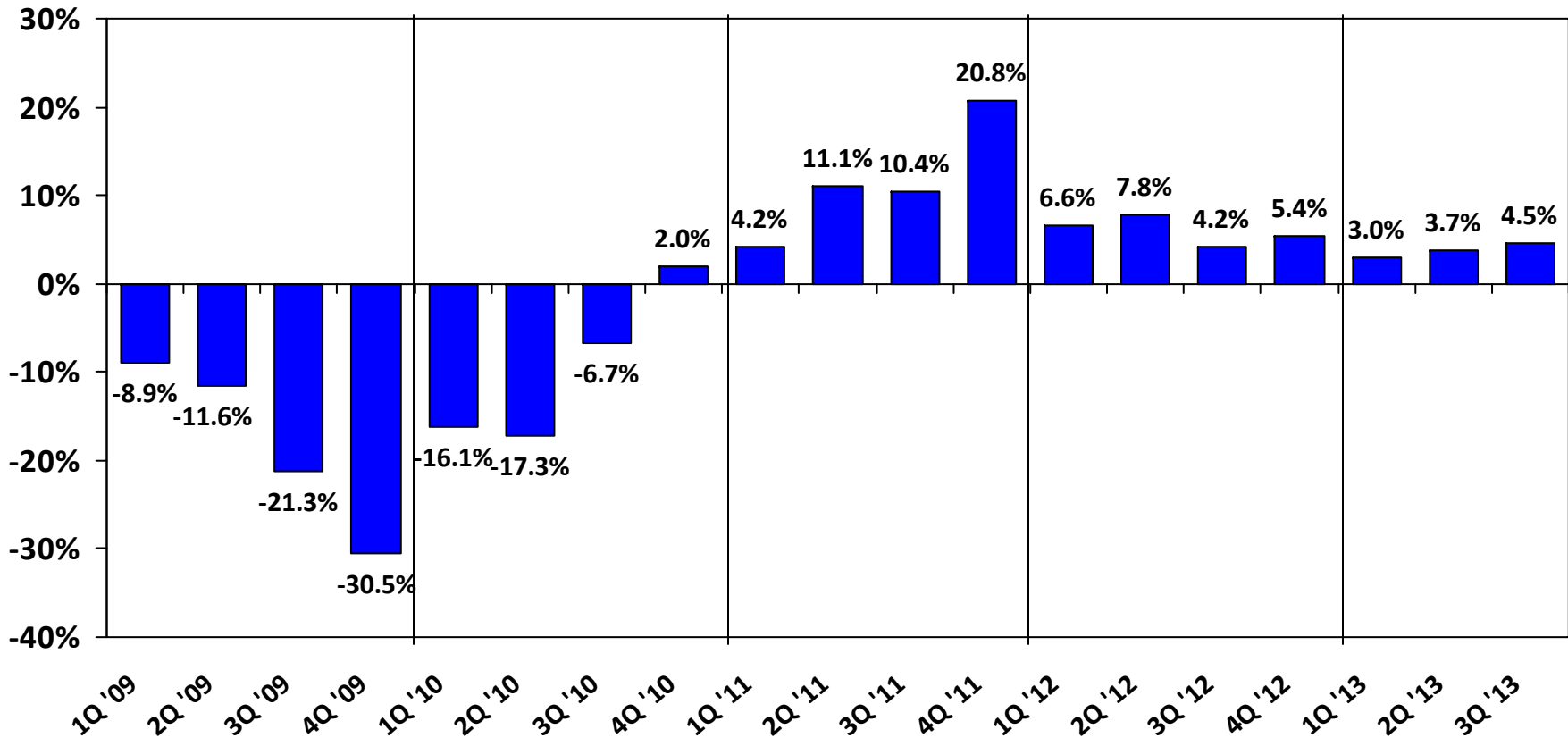
- \$29.4 M Above Forecast

	% Change over Prior Year *
Sales Tax (without 1-cent)	4.1%
Individual Income Tax	7.9%
Corporate Income Tax	(6.7)%

- ❑ Year-to-date is 0.4% above forecasted growth
- ❑ Difficult to interpret year-to-date individual income tax gain in the midst of tax filing season – most of individual income tax gain due to lower refunds

* Based on preliminary March numbers

FY '13 Quarterly Growth Rates Have Tapered Off From Growth Rates of FY '12



Percent Change in Adjusted Revenues Excluding
1-Cent Sales Tax



Key Economic Measures

- Current Arizona Status Compared to Last Year

	April '12	April '13
Withholding Growth 3 Month Average Compared to Prior Year	2.6%	0.6%
Retail Sales Tax Growth 3 Month Average Compared to Prior Year	5.1%	7.8%
Pending Maricopa Foreclosures Normal = 3,000	18,000	10,200
Arizona Annual Single Family Permits Normal = 40,000	11,400	16,500
Arizona Underwater Mortgages	48%	35%

Arizona Forecasters Are Optimistic Compared to Most Other Western States

Blue Chip Forecast CY '13 % Personal Income Growth

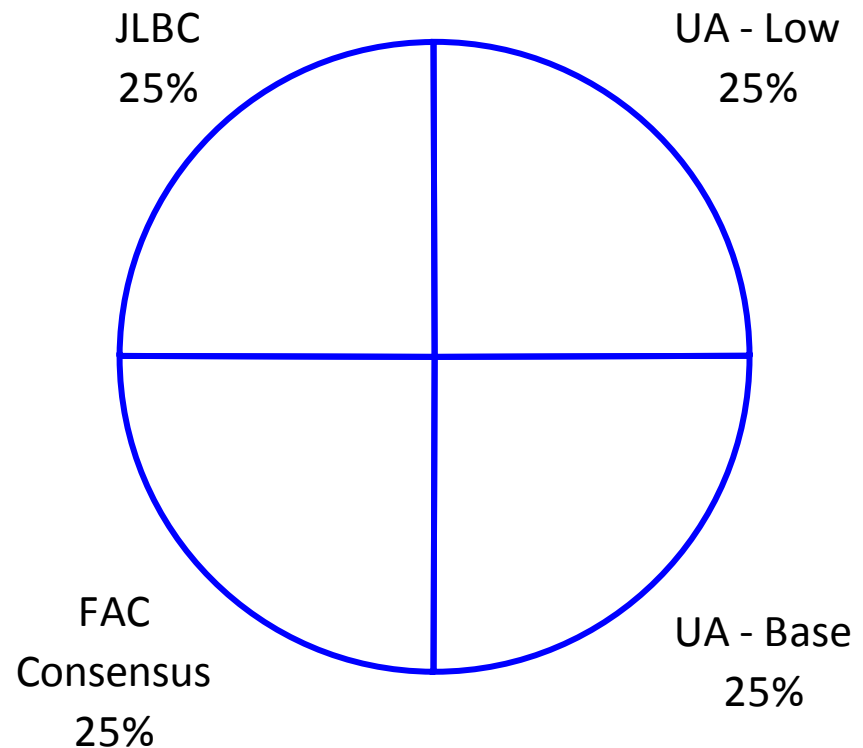
Texas	5.8%
Arizona	5.5%
Utah	4.3%
Washington	4.1%
California	3.9%
Colorado	3.8%
Oregon	3.8%
New Mexico	3.0%
Idaho	2.9%
Nevada	2.5%

Where Are We Headed Over the Next Few Years?

- Four-Sector Consensus Forecast Incorporates Different Economic Views, Including the FAC *

4-sector forecast equally weights:

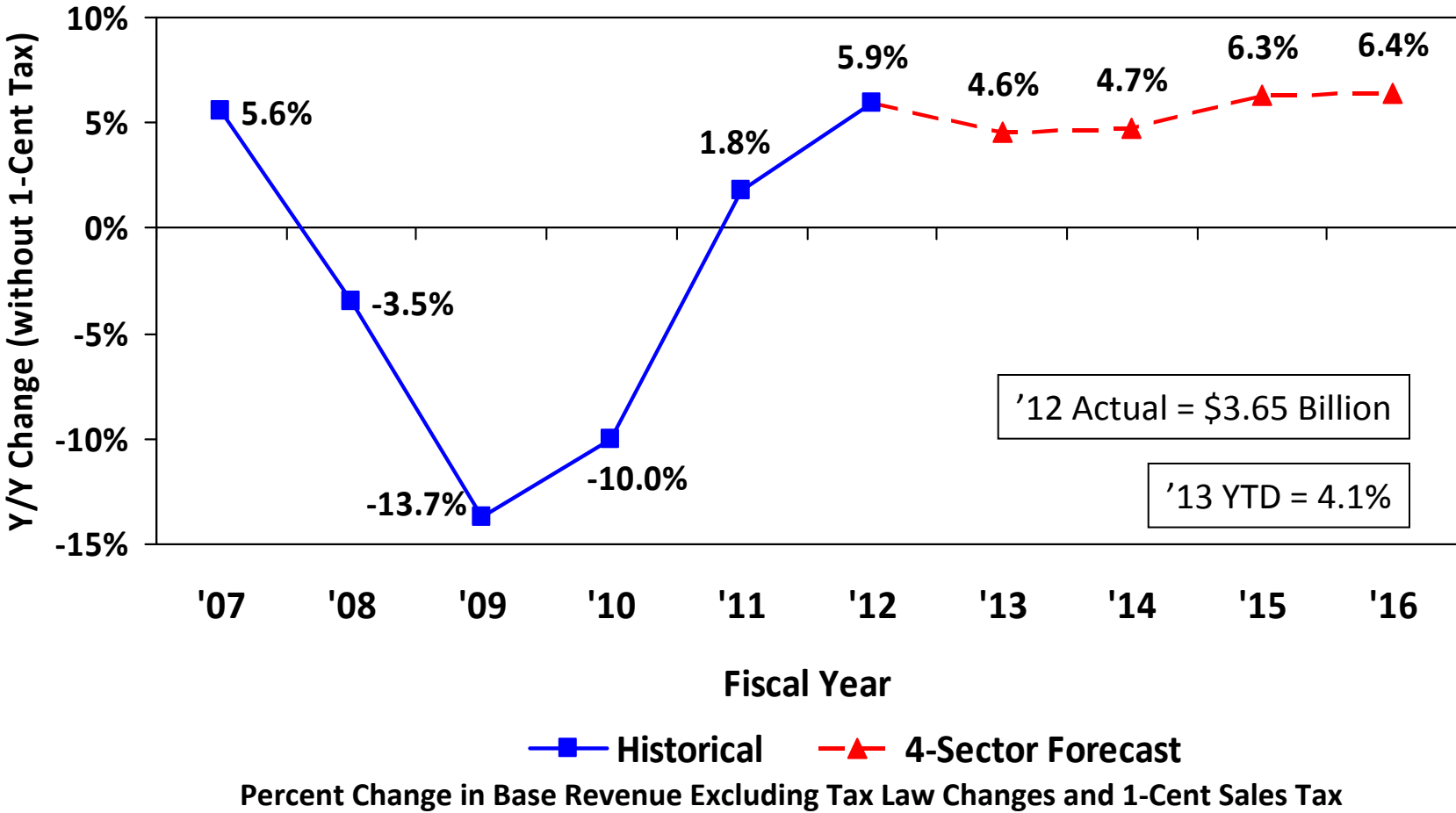
- FAC average
- UofA model – base
- UofA model – low
- JLBC Staff forecast
- Remaining revenues (9% of total) are staff forecast



* Includes Big 3 categories of sales tax, individual income and corporate income taxes (see Appendix A)

Sales Tax

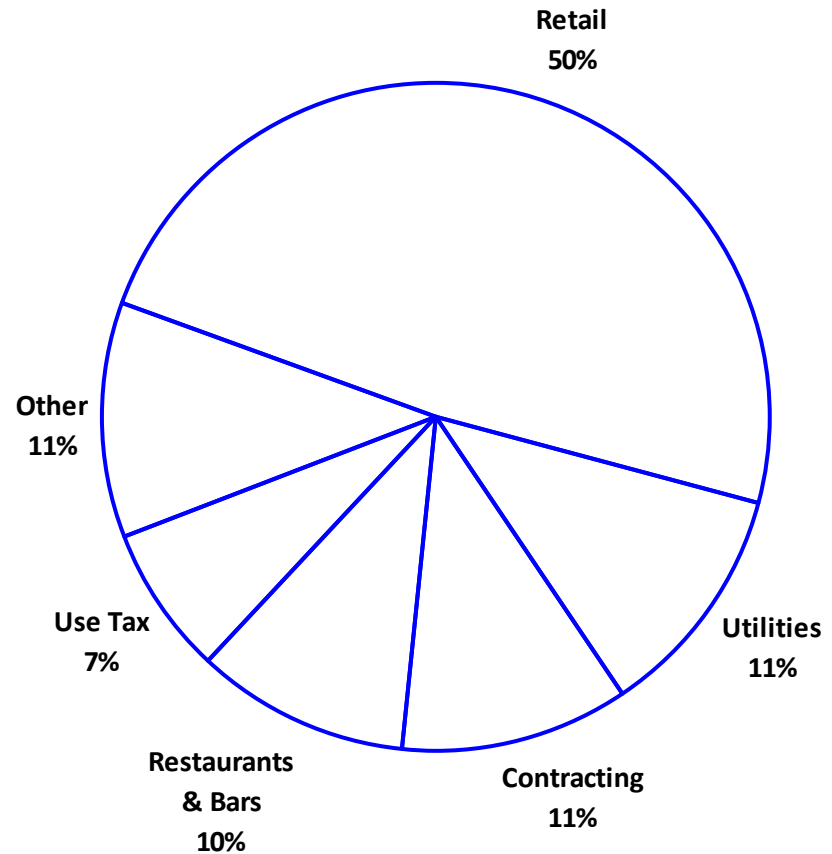
- Forecast Growth of 4.6% in FY '13 and 4.7% in FY '14



FY 2012 Total Sales Tax Collections = \$3.65 B

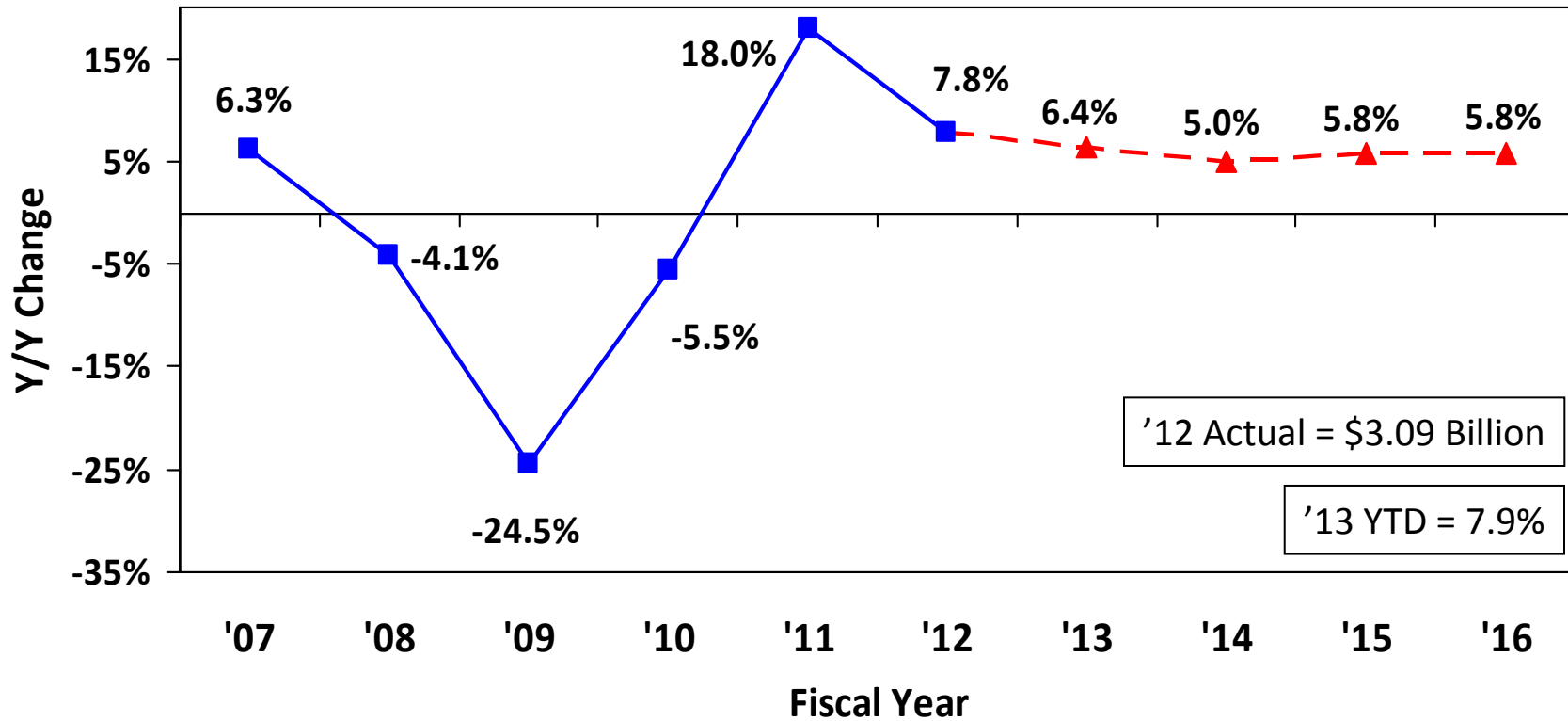
- Collections by Major Category

<u>Category</u>	<u>FY '12 Base (Millions)</u>	<u>YTD % Increase</u>
Retail	\$ 1,777.7	6.4%
Utilities	412.1	3.3%
Contracting	411.4	2.8%
Restaurants & Bars	368.9	6.4%
Use Tax	263.7	(1.6)%
Other	<u>418.4</u>	<u>4.8%</u>
TOTAL	\$ 3,652.2	4.4%



Individual Income Tax

- Forecast Growth of 6.4% in FY '13 and 5.0% in FY '14



—■— Historical -▲- 4-Sector Forecast

Percent Change in Base Revenue Excluding
Tax Law and One-Time Changes

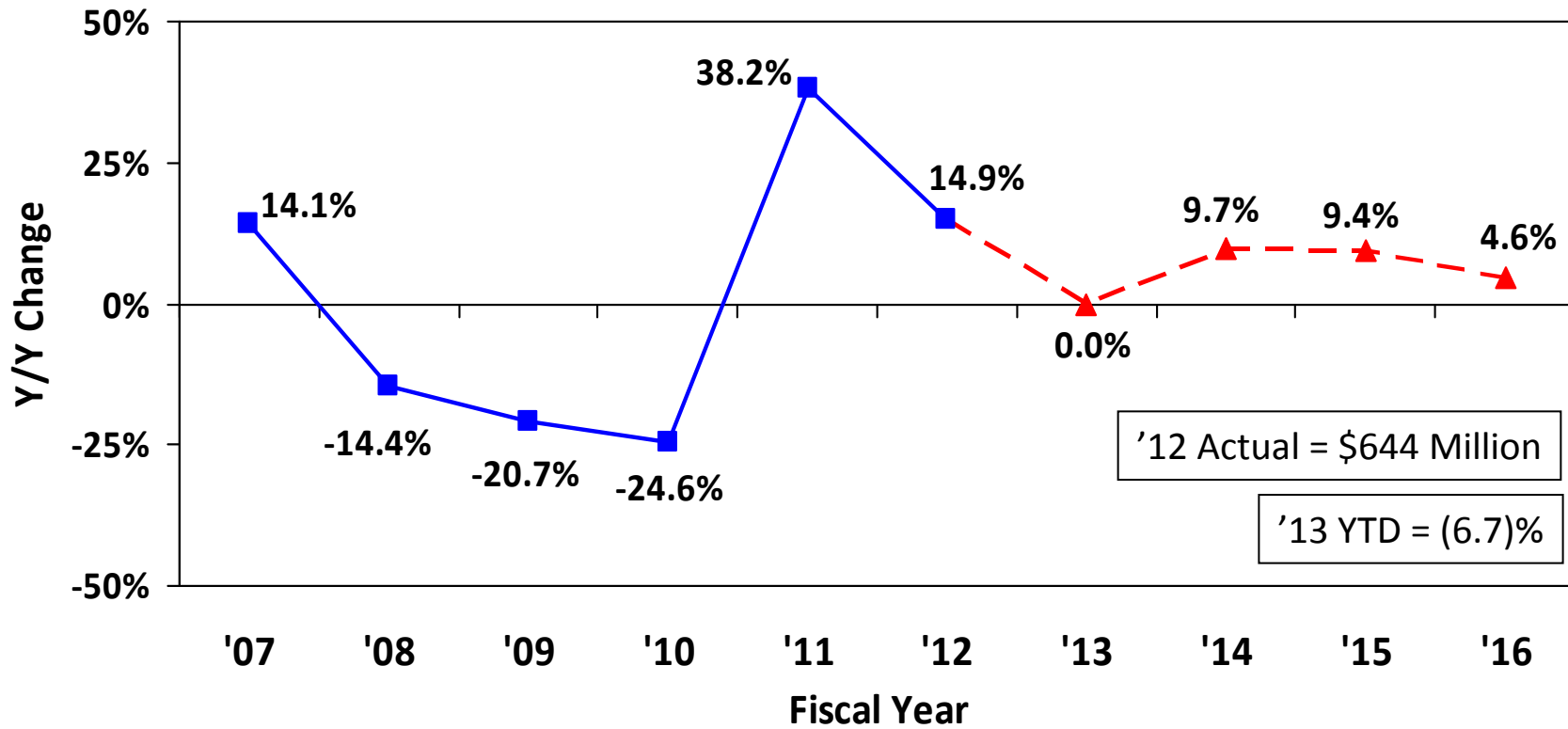


Potential One-Time FY '13 Tax Shift

- ❑ Federal fiscal cliff threat incentivized companies to issue dividends and stockholders to take capital gains
 - 4th quarter dividends 4 times higher than a year ago
 - May only accelerate, not increase, investment income
- ❑ Creates potential to shift future year collections into FY '13 – and reduce FY '14 by a corresponding amount
 - Very difficult to determine magnitude in advance – forecast does not incorporate
- ❑ Too early to tell what the magnitude of any tax shift might be
 - Will be clearer with April tax returns

Corporate Income Tax

- Forecast Growth of 0.0% in FY '13 and 9.7% in FY '14



—■— Historical -▲- 4-Sector Forecast

Percent Change in Base Revenue Excluding
Tax Law and One-Time Changes

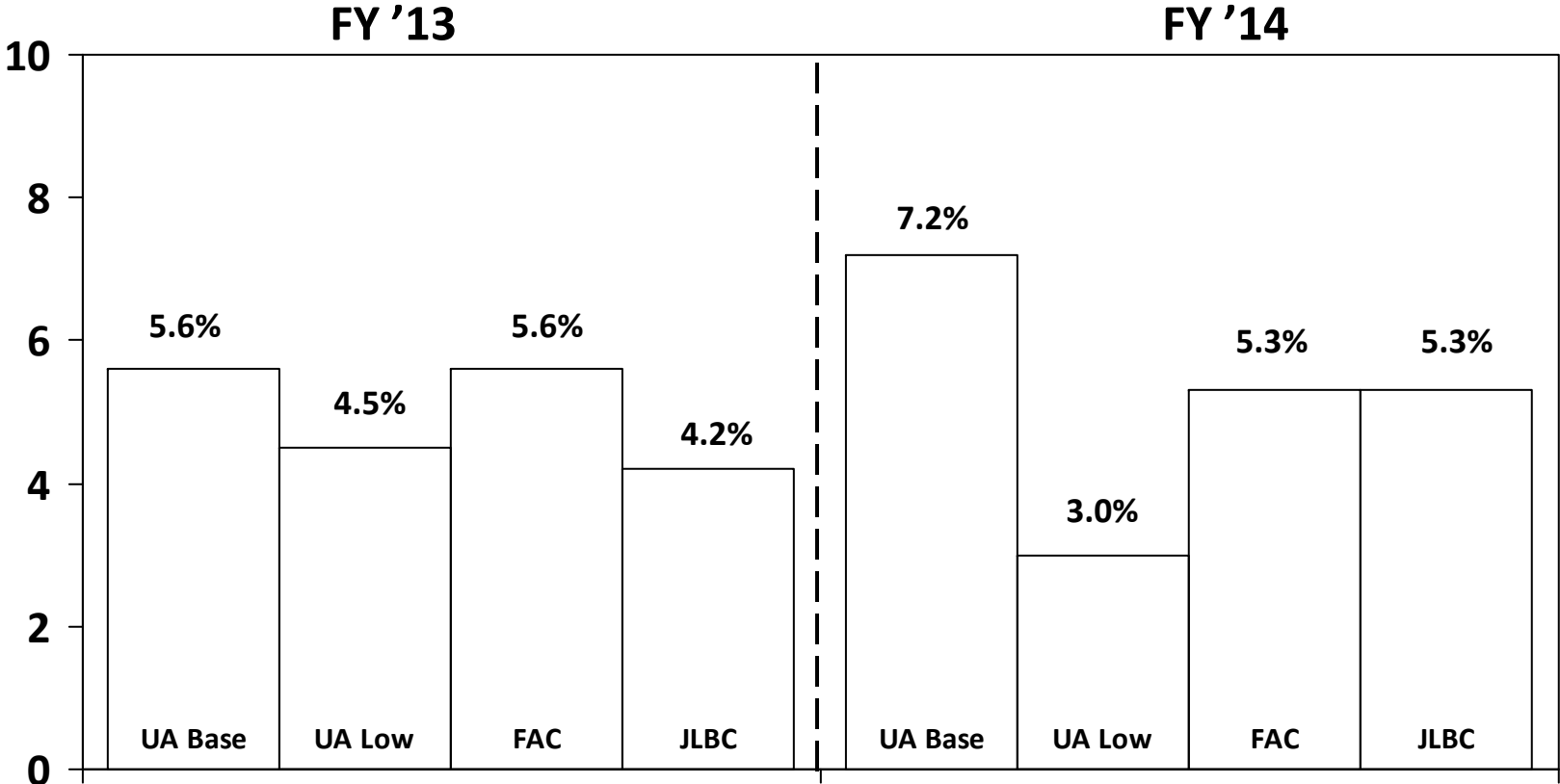


Corporate Income Tax Credits

- ❑ Corporate income tax credits totaled \$72 M in TY '10
- ❑ Credits are anticipated to total \$100 M or more when TY '11 data is finalized
- ❑ Expected to increase further as corporate profits increase
 - Increased profits increase potential tax liability
 - Increased tax liability allows for greater use of accumulated credits
- ❑ Difficult to predict the impact of credits on the consensus forecast for corporate income tax

Overall Consensus Growth Rate

- Forecast Growth of 4.0% in FY '13 and 4.9% in FY '14 *



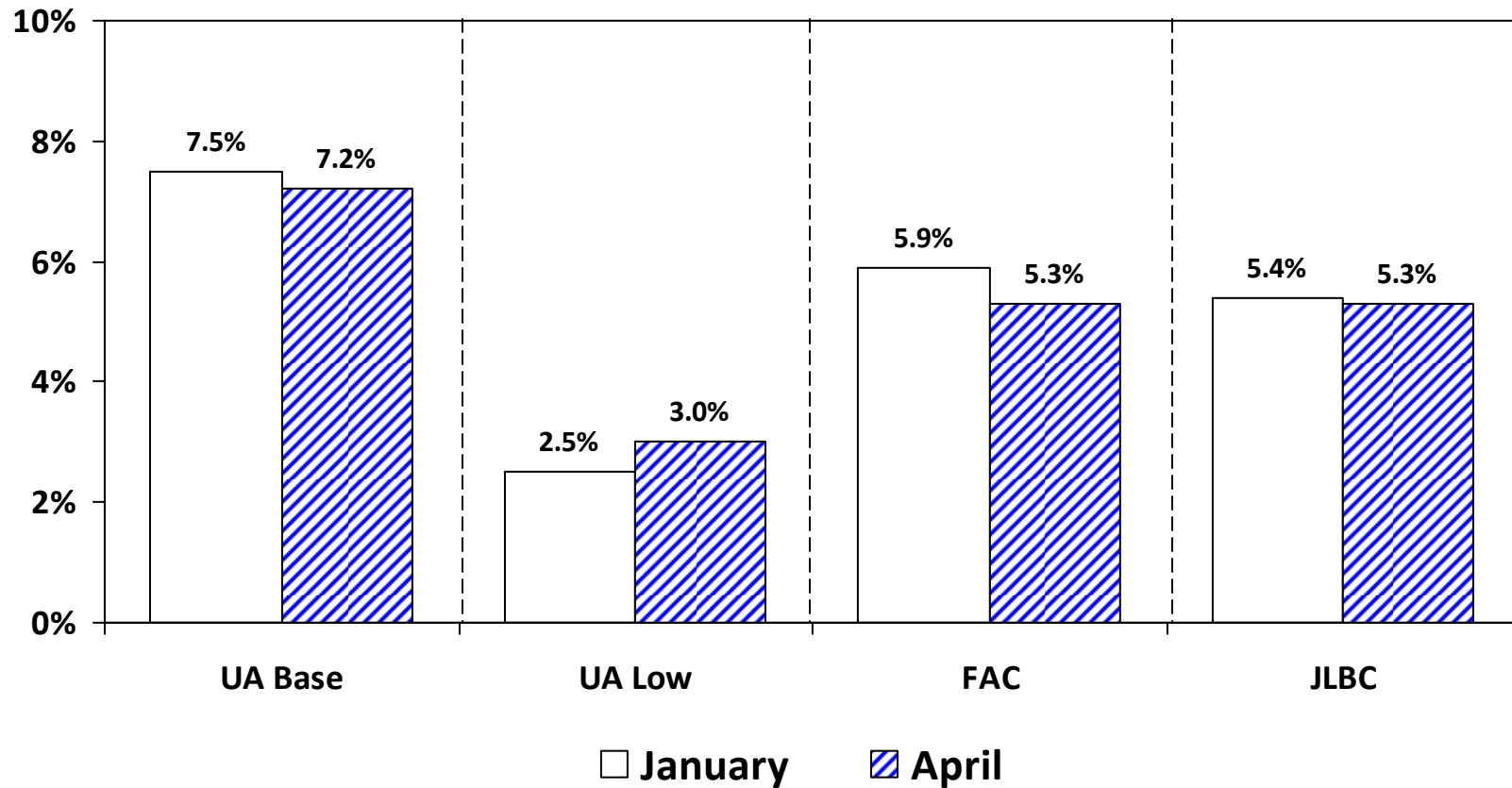
Details in Appendix A

* Weighted Big 3 average growth prior to 1-Cent sales tax is 5.0% in FY '13 and 5.2% in FY '14. After adjusting for small tax categories, the base growth rate is 4.0% in FY '13 and 4.9% in FY '14.



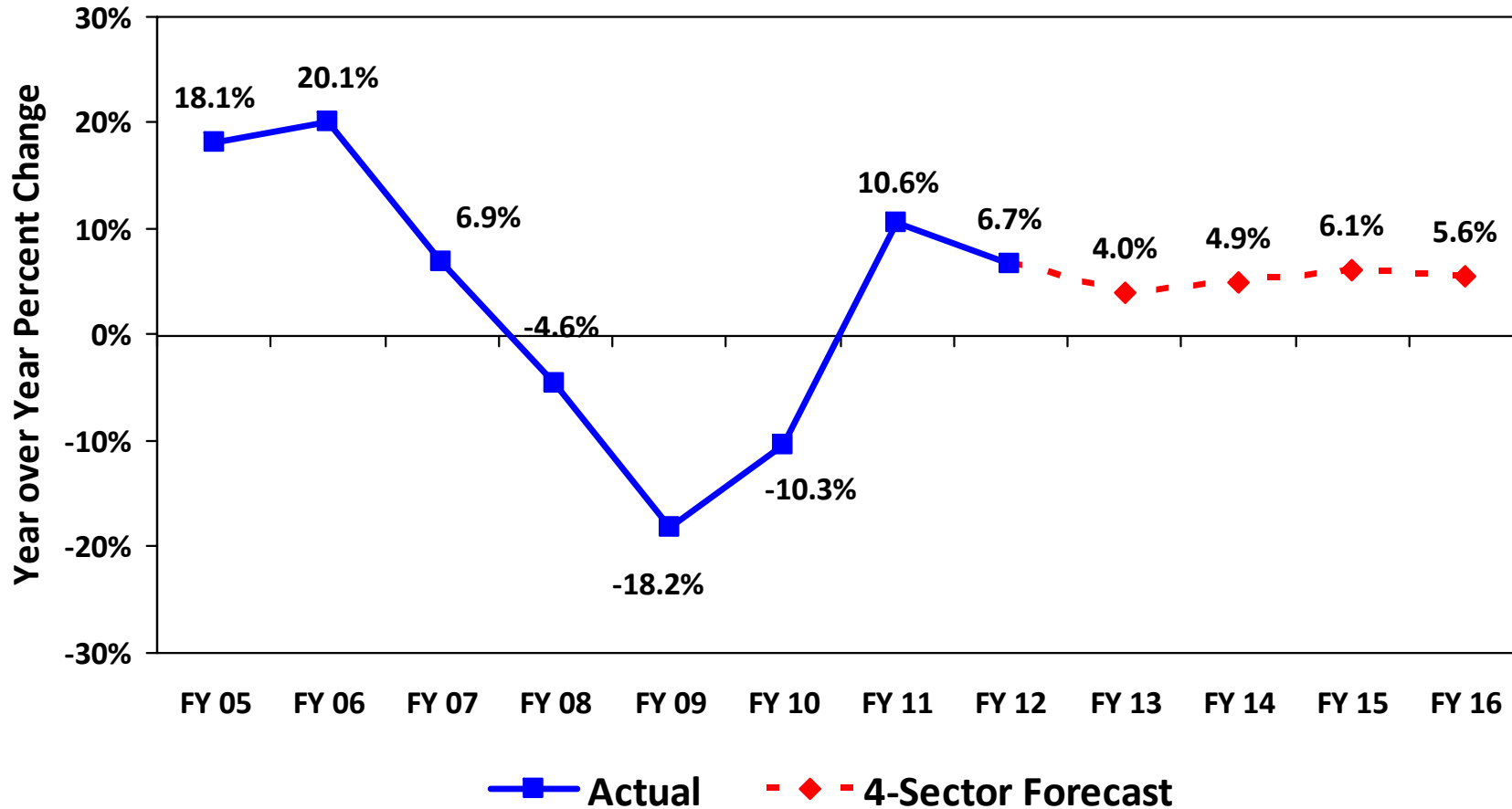
FY '14 4-Sector Forecast

- April Components Compared to January



Consensus Forecast Through FY '16

- Moderate Growth with Some Acceleration *

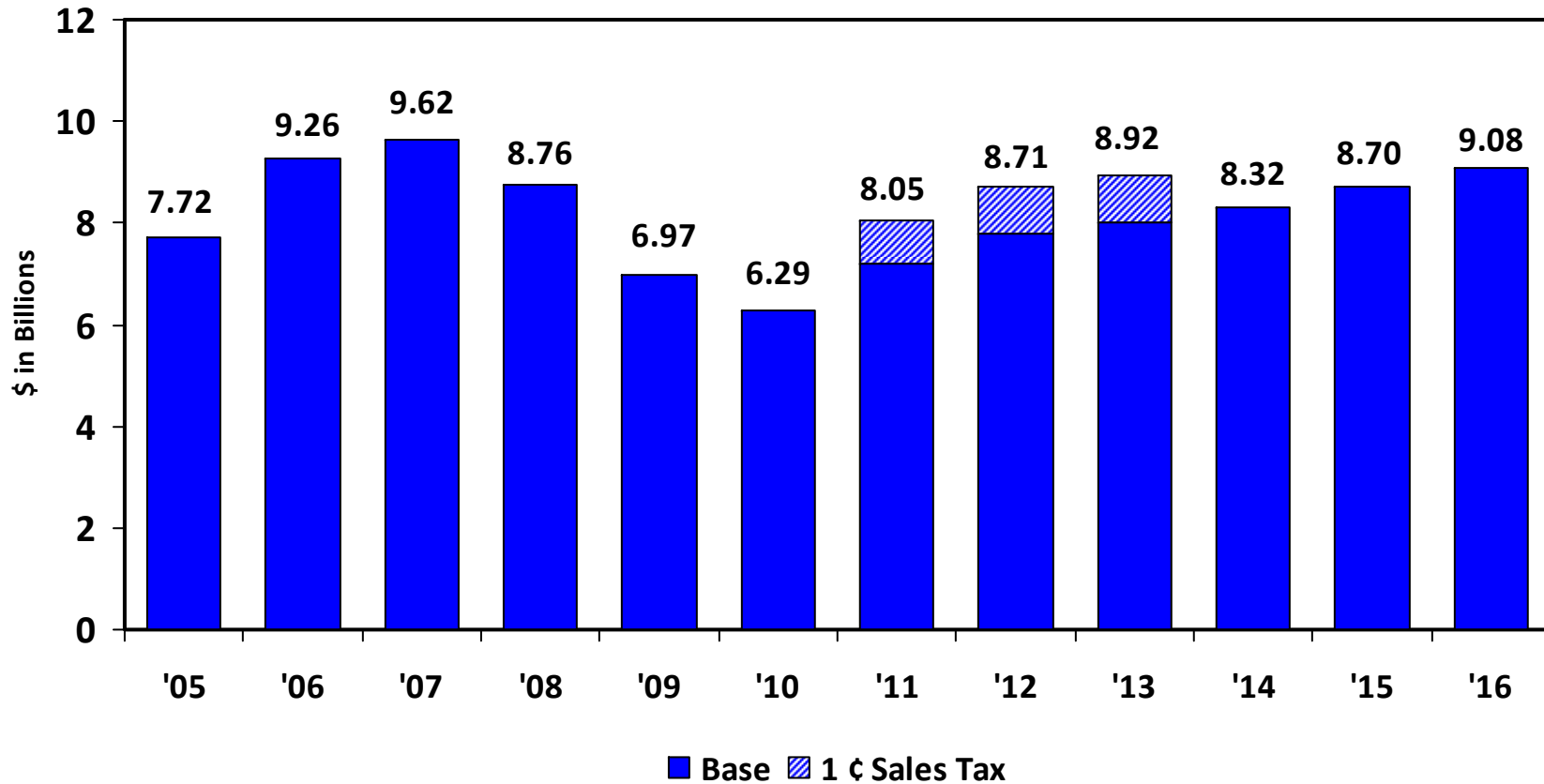


Percent Change in Base revenues excluding balance forward, tax law changes, one-time revenues, and URS (see Appendix B)

* Weighted Big 3 average growth is 6.3% in FY '15 and 6.0% in FY '16. After adjusting for small tax categories, the base growth rate is 6.1% in FY '15 and 5.6% in FY '16.



Consensus Forecasts Remains Below FY '07 High



Excludes balance forward and other one-time revenues. Includes tax law changes and Urban Revenue Sharing.

Projected Ending Balance Estimates

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FY '14 – '16 Baseline Projections

Baseline	'13	'14	'15	'16
Balance Forward	\$397 M	\$642 M	\$290 M	\$13 M
Revenues	\$9.0 B	\$8.3 B	\$8.7 B	\$9.1 B
Spending	\$8.7 B ^{1/}	\$8.7 B	\$9.0 B	\$9.2 B
Ending Balance	\$642 M	\$290 M	\$13 M	\$(120) M

- ❑ After statutory spending, effectively no money remains for discretionary spending without increasing out-year shortfall
- ❑ Excludes impact of K-12 inflation court ruling – would increase FY '16 shortfall by approximately \$(500) M
- ❑ \$450 M Rainy Day Fund available to offset shortfalls

^{1/} \$8.5 billion after adjusting for Rainy Day Fund deposit

Projected Ending Balance

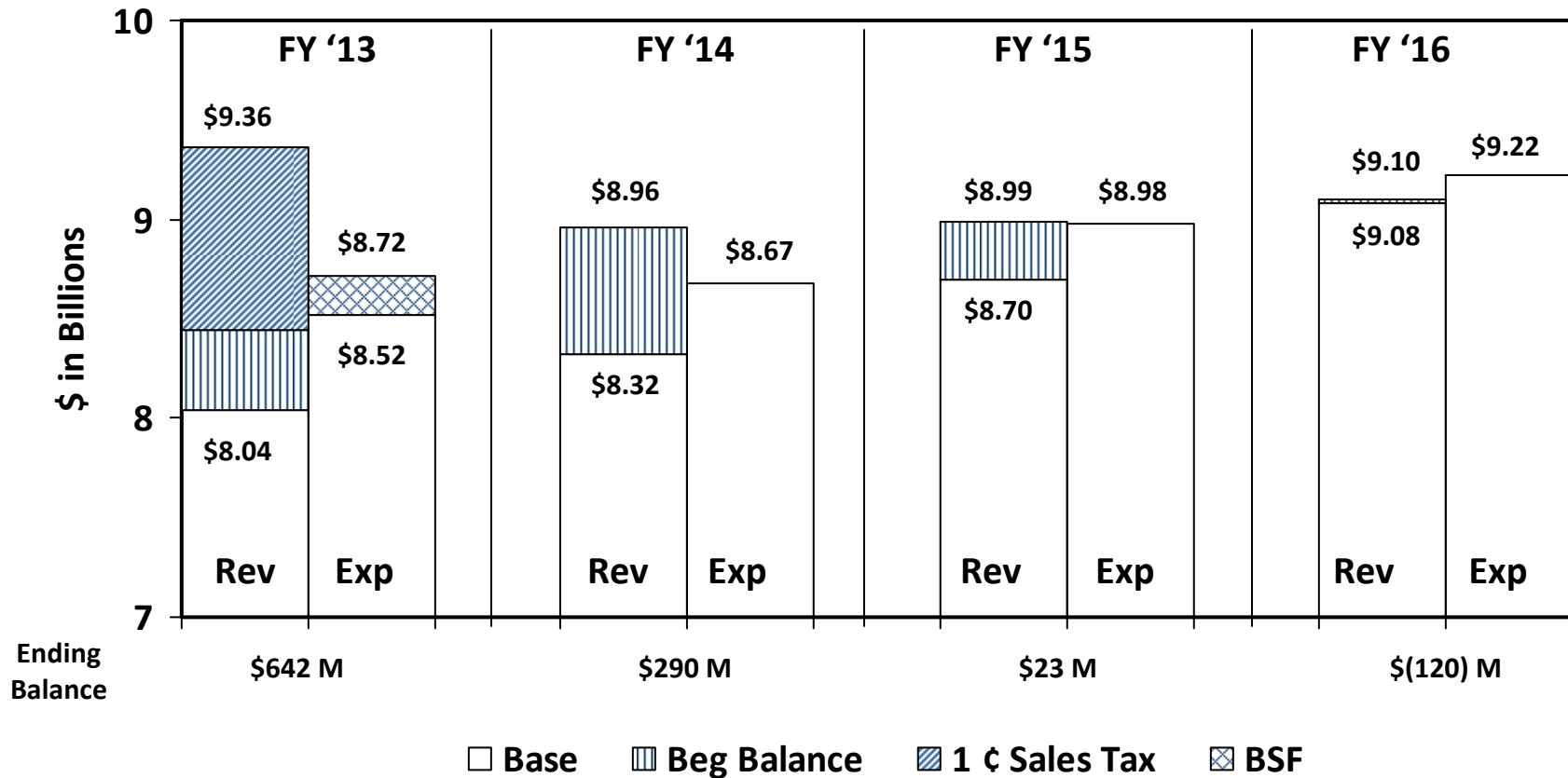
- Impact of April Forecast

	<u>'13*</u>	<u>'14</u>	<u>'15</u>	<u>'16</u>
January Ending Balance	\$646 M	\$299 M	\$9 M	\$(90) M
April Ending Balance	\$642 M	\$290 M	\$13 M	\$(120) M

* Adjusted for enacted legislation

JLBC Baseline Revenues Compared to Expenditures

- If No Discretionary Spending – \$(120) M FY '16 Shortfall



Forecast Risks

- 64% Consensus Probability of Exceeding Forecast

- ❑ 0% interest rate environment
- ❑ Federal budget
 - Funding levels set through September
 - 5% reduction in domestic programs, approximately \$103 M
 - 7.8% reduction in defense spending, approximately \$800 M
 - Full impact not felt for several years due to contracting cycle
 - Job loss estimate ranges up to 50,000
 - Effect on Arizona growth? FAC panelists range from 0% to 1% reduction in growth rate

Forecast Risks – State Specific Issues

□ Budget litigation

- If Arizona Supreme Court upholds Court of Appeals on K-12 inflation case, 3-year cost would be \$500 M

□ TPT simplification legislation

- In part, revenue neutrality depends on current level of noncompliance
- By its nature, level of noncompliance very difficult to determine
- On upside, legislation would facilitate internet taxation if Congress authorizes

Appendix A: April 2013 4-Sector Forecast

	<u>FY 2013</u>	<u>FY 2014</u>	<u>FY 2015</u>	<u>FY 2016</u>
Sales Tax				
JLBC Forecast	4.6%	5.5%	5.6%	5.7%
UA – Low	4.3%	2.6%	5.5%	6.7%
UA – Base	4.9%	5.8%	8.5%	7.8%
FAC	4.8%	4.8%	5.6%	5.3%
Average:	4.6%	4.7%	6.3%	6.4%
Individual Income Tax				
JLBC Forecast	5.4%	5.9%	6.7%	6.5%
UA – Low	5.4%	1.6%	3.7%	4.6%
UA – Base	7.4%	6.7%	6.3%	6.0%
FAC	7.4%	5.8%	6.3%	5.9%
Average:	6.4%	5.0%	5.8%	5.8%
Corporate Income Tax				
JLBC Forecast	(3.5)%	1.2%	5.0%	5.6%
UA – Low	1.1%	12.8%	10.4%	3.3%
UA – Base	1.1%	18.3%	16.4%	5.6%
FAC	1.4%	5.9%	4.7%	3.9%
Average:	0.0%	9.7%	9.4%	4.6%
JLBC Weighted Average	4.2%	5.3%	6.0%	6.0%
UA Low Weighted Average	4.5%	3.0%	5.2%	5.6%
UA Base Weighted Average	5.6%	7.2%	8.3%	6.9%
FAC Weighted Average	5.6%	5.3%	5.8%	5.4%
“Big-3” Weighted Average *	5.0%	5.2%	6.3%	6.0%
Consensus Weighted Average**	4.0%	4.9%	6.1%	5.6%
Adjusted Consensus Weighted Average**	3.6%	4.3%	4.6%	4.4%
* Adjusted for small revenue categories				
** Adjusted for tax law changes				



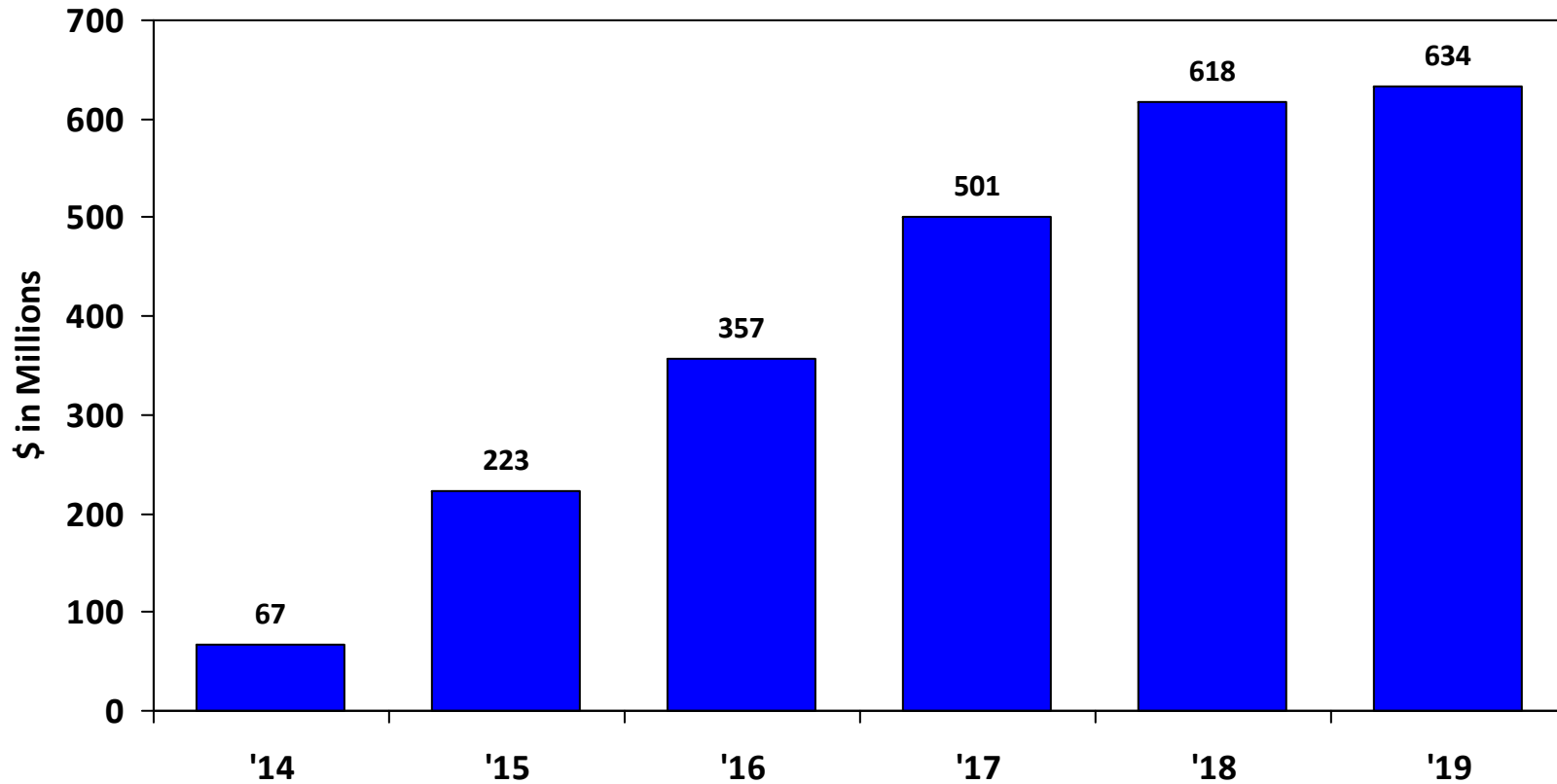
Appendix B

Additional Forecast Information

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Fiscal Impacts of Enacted Tax Laws

- Includes Property Tax Change Impact on K-12 Budget



Revenue Loss/Spending Increase Relative to Enacted FY 2013 Budget

Major Tax Provisions Affecting General Fund

Provisions	(\$ in Millions)		
	FY '14	FY '15	FY '16
Business Property Taxes / Homeowner Rebate	19	41	67
Corporate Rate Phase Down (FY '15 – FY '18)	0	54	116
Corporate Sales Factor Phase In (FY '15 – FY '18)	0	25	47
New Employee Tax Credit	18	38	45
Capital Gains Reduction	18	52	69

FY '14 – FY '16 Baseline Revenue Changes

General Fund - \$ in Millions

	FY '14 <u>Above '13</u>	FY '15 <u>Above '14</u>	FY '16 <u>Above '15</u>
Base Revenue Growth (4.9%/6.1%/5.6%)	415	542	520
TPT 1 ¢ Expires	(924)	--	--
Elimination of Fund Transfers	(90)	(6)	--
One-Time FY '13 Revenue Loss ^{1/}	52	--	--
Previously Enacted Tax Legislation	(47)	(134)	(108)
Urban Revenue Sharing	(47)	(25)	(27)
Change In Beginning Balance ^{2/}	<u>245</u>	<u>(352)</u>	<u>(276)</u>
Additional Revenues	(396)	25	109
Total Resources	8,964	8,989	9,098

^{1/} TPT early payment threshold

^{2/} Beginning balances: FY '13, \$397 M; FY '14, \$642 M; FY '15, \$290 M; FY '16, \$13 M



Revenue Changes Between FY '13 and FY '16

	<u>\$ in Millions</u>
FY '13 Total Revenue	\$9,360
Base Revenue Increase	1,477
Loss of 1 cent Sales Tax	(924)
Beginning Balance Reduction	(384)
Enacted Tax Reductions	(289)
Increased Urban Revenue Sharing	(98)
Other	(44)
FY '16 Total Revenue	\$9,098