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# **FY 2014 JLBC Baseline With Executive Budget Comparison**

**January 22, 2013**

**JLBC**

# Positive Budget Developments

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- ❑ Arizona economy continues in recovery mode, albeit at a slow pace
- ❑ Legislature required to provide 3-year projection in its annual budget bill
  - Does not require individual FY '15 and '16 agency budgets, but does require state to set out-year targets
- ❑ FY '13 budget established reserves of \$450 M
  - Represents 5.5% of budget – statutory cap is 7%
  - Not intended to be used for ongoing programs
  - Formula would deposit another \$266 M, but 7% cap would limit to \$125 M – Baseline does not add

# Forecast Risks

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- Uncertain economy in 0% interest rate environment
- Unknown outcome of Federal Fiscal Cliff 2
- Unpredictable disaster – environmental or political
- Budget litigation
- A 3-year forecast comes with risks – a 1% change would affect the balance by \$500 M in the third year

## 2 Factors Influencing Budget Outlook through '16

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- How much revenue forecast risk in an uncertain economic environment?
- How much discretionary spending above the Baseline?

# Baseline Balance Represents Available Resources After Fulfilling Mandates

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## □ Consensus revenue

- 3-year annual 5.7% base growth – excluding tax changes
- Loss of \$(924) M 1-cent sales tax
- \$(283) M in enacted tax reductions by FY '16
- 65% probability of reaching forecast

## □ Statutory spending

- Growth required by statute – primarily K-12 and Medicaid
- Adds \$157 M in FY '14 and \$701 M by FY '16

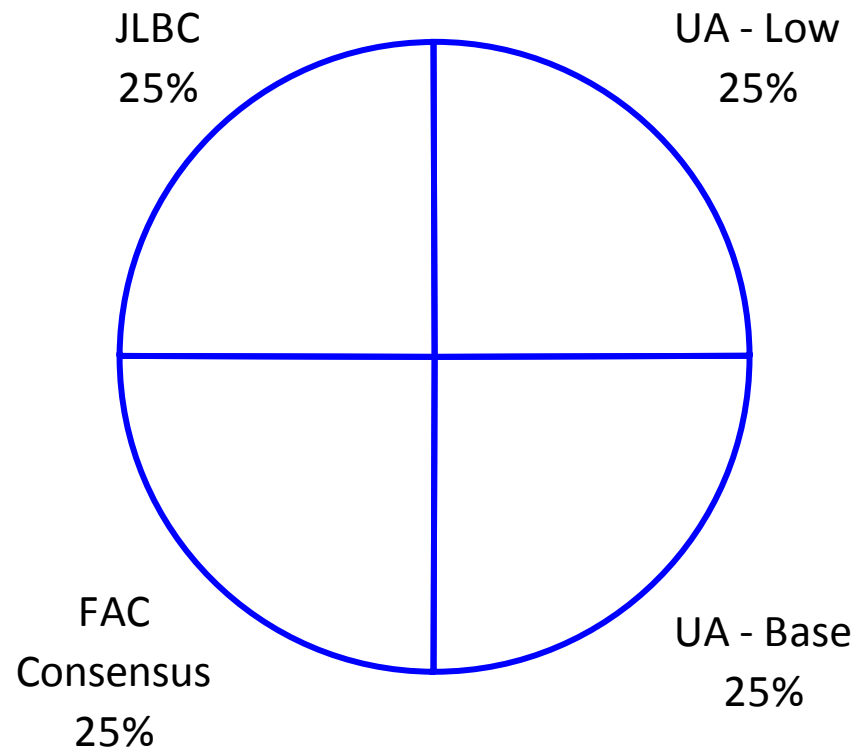
# Where Are We Headed Over the Next Few Years?

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

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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

# 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%/5.9%/6.2%)	416	526	575
TPT 1 ¢ Expires	(924)	--	--
Elimination of Fund Transfers	(90)	(6)	--
One-Time FY '13 Revenue Loss <sup>1/</sup>	52	--	--
Previously Enacted Tax Legislation	(47)	(134)	(108)
Urban Revenue Sharing	(45)	(28)	(35)
Change In Beginning Balance <sup>2/</sup>	<u>254</u>	<u>(341)</u>	<u>(285)</u>
<b>Additional Revenues</b>	<b>(384)</b>	<b>17</b>	<b>147</b>
<b>Total Resources</b>	<b>8,979</b>	<b>8,996</b>	<b>9,143</b>

<sup>1/</sup> TPT early payment threshold

<sup>2/</sup> Beginning balances: FY '13, \$397 M; FY '14, \$651 M; FY '15, \$310 M; FY '16, \$25 M



# FY '14 – FY '16 Baseline Spending Changes

	General Fund - \$ in Millions		
	<u>FY '14</u> <u>Above '13</u>	<u>FY '15</u> <u>Above '14</u>	<u>FY '16</u> <u>Above '15</u>
K-12 Formula	55	54	82
Medicaid Formula (prior to expansion)	(97)	115	128
Medicaid Mandatory Expansion	74	140	22
One-Time FY '13 Caseload Savings	76	--	--
ADC Operating – phase-in approved beds	9	19	7
Debt Service	20	--	--
Land Department Fund Source	11	--	--
Other	9	(26)	3
<b>Additional Spending</b>	<b>157</b>	<b>302</b>	<b>242</b>
<b>Total Spending</b>	<b>8,669</b>	<b>8,971</b>	<b>9,214</b>



# FY '14 – '16 Baseline Projections

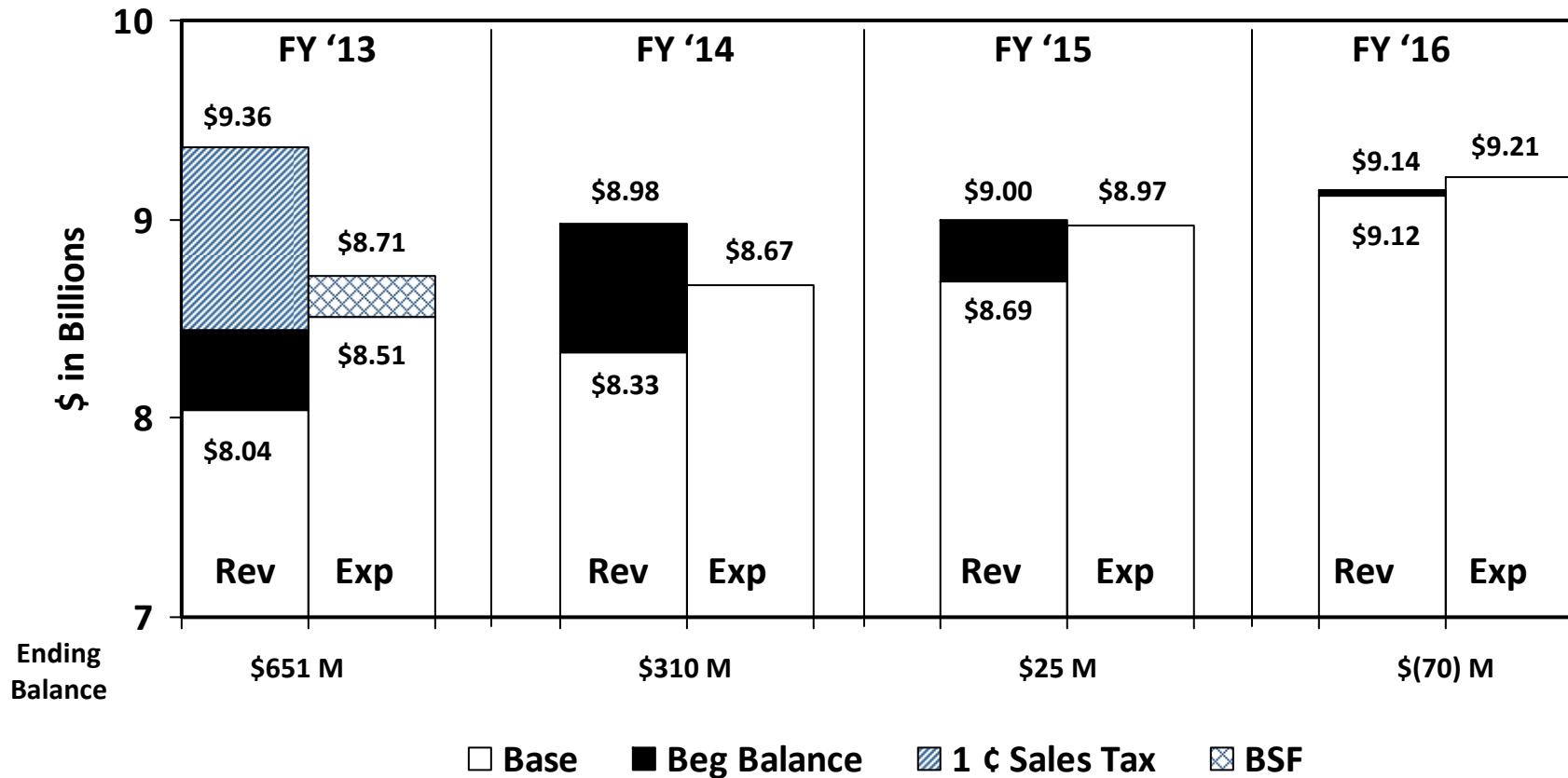
Baseline	'13	'14	'15	'16
Balance Forward	\$397 M	\$651 M	\$310 M	\$25 M
Revenues	\$9.0 B	\$8.3 B	\$8.7 B	\$9.1 B
Spending	\$8.7 B <sup>1/</sup>	\$8.7 B	\$9.0 B	\$9.2 B
<b>Ending Balance</b>	<b>\$651 M</b>	<b>\$310 M</b>	<b>\$25 M</b>	<b>\$(70) M</b>

- ❑ After statutory spending, effectively no money remains for discretionary spending without increasing out-year shortfall
- ❑ Excludes impact of K-12 inflation court ruling – would add a new \$80 M+ to budget each year. If funded, would result in \$(223) M FY '15 shortfall and \$(346) M FY '16 shortfall
- ❑ \$450 M Rainy Day Fund available to offset shortfalls

<sup>1/</sup> \$8.5 billion after adjusting for Rainy Day Fund deposit

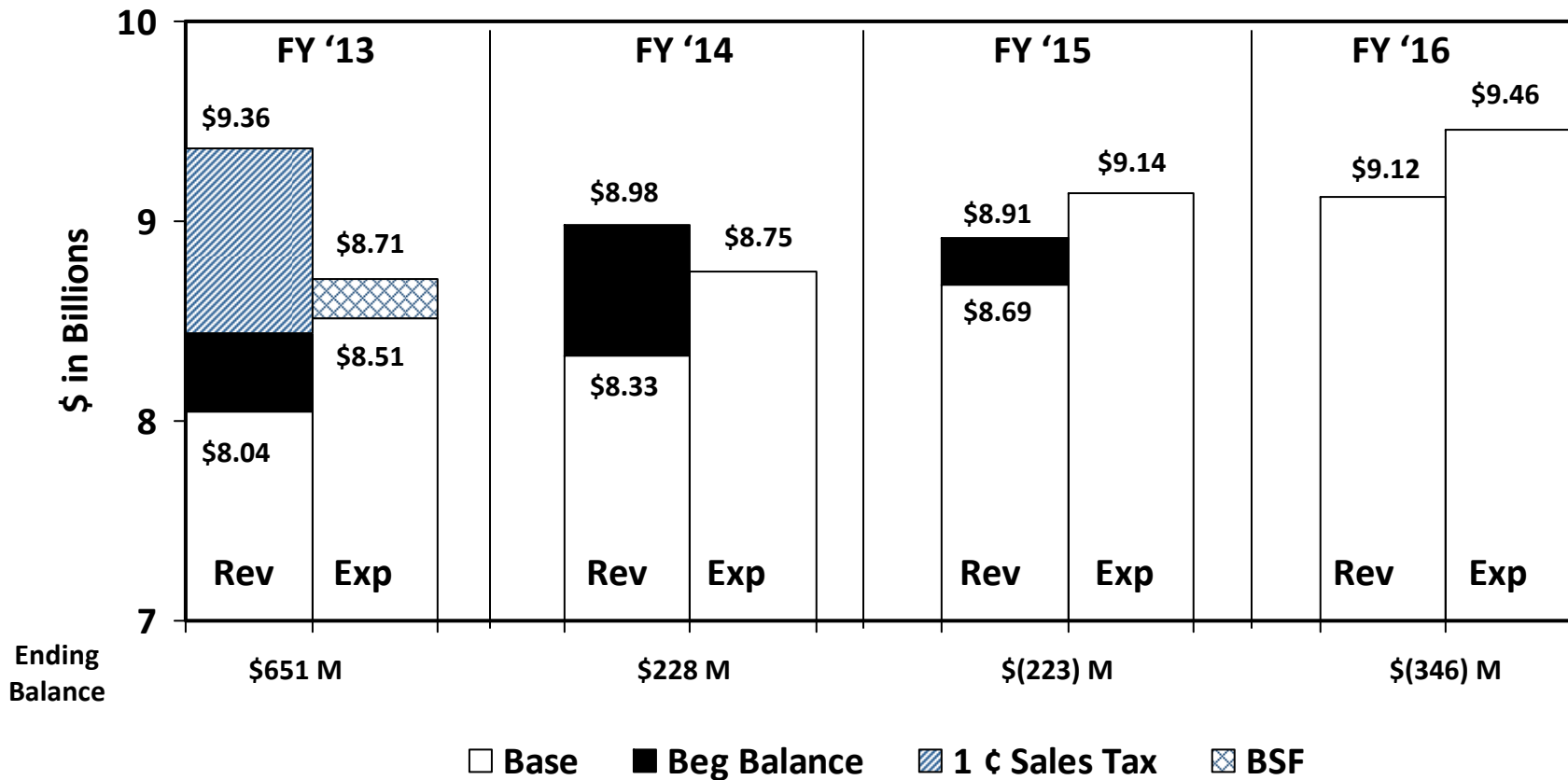
# JLBC Baseline Revenues Compared to Expenditures

## - If No Discretionary Spending – Small FY '16 Shortfall



# JLBC Baseline Adjusted for K-12 Inflation Ruling

## - Extra \$1 Spent in '14 Increases '16 Shortfall by At Least \$3



# Budget Concerns

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- ❑ Arizona has third lowest credit rating among states
- ❑ Budget has ongoing structural shortfalls – permanent revenues less than spending
- ❑ State still suspends \$678 M in annual formula spending – if funded, would worsen structural gap
- ❑ Labeling spending as one-time reduces 3-year impact, but is it likely to continue?

# JLBC Staff Suggested Process Improvements

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- 1) Strengthen independent review of K-12 automation
- 2) Confirm school district charter conversion policy
- 3) Enhance K-12 override/bonding reporting
- 4) Increase CPS funding oversight – 45% of \$ are non-appropriated
- 5) Specify intent of 1,500 authorized prison beds – supplant or supplement temporary beds?
- 6) Establish expectation of university performance measures – can they be used to determine total funding?
- 7) Improve accounting of 1-time monies – April '13 investment income windfall

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# Executive Budget Comparison

# Executive Has \$261 M More in Higher Revenue Than JLBC Baseline in FY '14

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## General Fund Revenue

- FY '13 - \$84 M
- FY '14- \$261 M
  - \$74 M: higher Beginning Balance
  - \$125 M: higher revenue growth rates
  - \$62 M: employee Health Insurance Fund transfer
  - \$7 M: insurance premium
  - \$(7) M: new lottery distributions – counties/parks

# Besides \$261 M in Higher Revenue, Executive has \$258 M in Higher Spending

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## General Fund Spending

- ❑ FY '13 - \$15 M (CPS supplemental)
- ❑ FY '14 - \$258 M



# Executive and JLBC Baseline FY '14 Spending Changes

		\$ in M Above FY '13	
<u>Executive Proposals</u>		<u>JLBC</u>	<u>EXEC</u>
1.	<p>K-12 Education</p> <ul style="list-style-type: none"> <li>• Adds \$40 M for common core and \$36 M for performance</li> <li>• Executive estimates current formula will cost \$(10) M less than '13 compared to JLBC \$55 M increase</li> </ul>	55	70
2.	<p>School Facilities Board</p> <ul style="list-style-type: none"> <li>• Adds \$22 M for maintenance/\$20 M for school automation</li> </ul>	5	51
3.	<p>Universities</p> <ul style="list-style-type: none"> <li>• Adds \$15 M parity, \$15 M performance, \$20 M technology, \$8 M Phoenix Med School</li> </ul>	0	59
4.	<p>Corrections</p> <ul style="list-style-type: none"> <li>• Both add new bed requirements</li> </ul>	9	9

# Executive and JLBC Baseline FY '14 Spending Changes

		\$ in M Above FY '13	
<u>Executive Proposals</u>		<u>JLBC</u>	<u>EXEC</u>
5.	AHCCCS <ul style="list-style-type: none"> <li>• Both reduce overfunded base, while Exec adds optional group and shifts costs to provider assessment</li> </ul>	(30)	(86)
6.	DHS <ul style="list-style-type: none"> <li>• Adds \$8 M for base and \$8 M for research grants/ASH IT</li> </ul>	(10)	16
7.	DES <ul style="list-style-type: none"> <li>• Both add DD growth, Exec adds \$68 M for CPS-related issues</li> </ul>	17	87
8.	Department of Administration <ul style="list-style-type: none"> <li>• Adds statewide automation funding</li> </ul>	1	42
9.	Retain 1-Time State Employee Pay <ul style="list-style-type: none"> <li>• Retains October 2012 5% + \$6 M for new merit</li> </ul>	(17)	8
10.	Retirement Expenses <ul style="list-style-type: none"> <li>• Adds funding for higher employer rate</li> </ul>	0	16

# Executive and JLBC Baseline FY '14 Spending Changes

<u>Executive Proposals</u>	<u>\$ in M Above FY '13</u>	
	<u>JLBC</u>	<u>EXEC</u>
11. Debt Buyback	0	40
• Adds funding for projects to be determined		
12. Civic Center Debt Payment	15	15
• Both add funding to raise payment to \$20 M		
13. Unspent Appropriations (Revertments)	76	37
• Both reduce level, but different assumptions		
14. Land Department Fund Source Shift	11	11
15. Eliminate 1-Time Health Insurance Savings	25	25
16. Other	(1)	14
<b>Additional Spending</b>	<b>157</b>	<b>415</b>

# Baseline vs. Executive Budget Spending Levels

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	<b>\$ in Billions</b>		
	<u>FY '14</u>	<u>FY '15</u>	<u>FY '16</u>
JLBC Baseline	\$ 8.67	\$ 8.97	\$ 9.21
Executive *	\$ 8.93	\$ 9.08	\$ 9.30

\* Adjusted for comparability for Civic Center debt payment

# What Is The Margin For Error?

## - Ending Balance Projections

	<b>\$ in Millions</b>			
	<u>FY '13</u>	<u>FY '14</u>	<u>FY '15</u>	<u>FY '16</u>
JLBC Baseline	651	310	25	(70)
Executive	725	313	122	139
Executive – Modified*	725	123	(322)	(263)

\* Modified to include JLBC's FY '14 – '16 base revenue forecast and ADE statutory formula estimate

# How Different Assumptions Affect Executive's FY '15 Estimate

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<u>\$ in M</u>	<u>Changes to Ending Balance</u>
\$313	'14 Executive ending balance
(65)	'14 JLBC higher ADE formula costs
<u>(125)</u>	'14 JLBC lower revenue
\$123	'14 revised Executive ending balance
(190)	'15 lower beginning balance (\$122 M rather than \$313 M)
(85)	'15 JLBC higher ADE formula costs
<u>(170)</u>	'15 JLBC lower revenue
\$ <u>(322)</u>	'15 revised Executive ending balance

# Executive Revenues Compared to Expenditures

## - As Adjusted for JLBC Revenues and ADE Formula

