
FY 2015 JLBC Baseline

**Summary Version with
Executive Budget Comparison**

Revised – January 29, 2014

JLBC

**Executive Comparisons Preliminary
and Subject to Change**

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
- ❑ Baseline does not address plaintiff proposal in K-12 inflation litigation – seeking \$1.7 B above the ‘15-’17 Baseline
- ❑ Baseline includes \$210 M to buy back debt in ‘17 under 2010 debt financing terms – but Executive could revise these terms

Department of Education

- Inflation Lawsuit Could Increase Baseline by \$1.7 B through FY17

- ❑ Plaintiffs seeking prospective “base level” increase of \$233 per pupil
- ❑ Also seeking back payments for unfunded inflation since FY09

Plaintiff Proposal (\$ in millions)

Fiscal Year	Base Level Increase	Back Payments	Total
2015	\$317	\$253	\$569
2016	321	253	573
2017	325	253	577
2018	329	253	582
2019	334	253	587
'15-'17 total	962	758	1,720
'15-'19 total	1,626	1,263	2,889

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

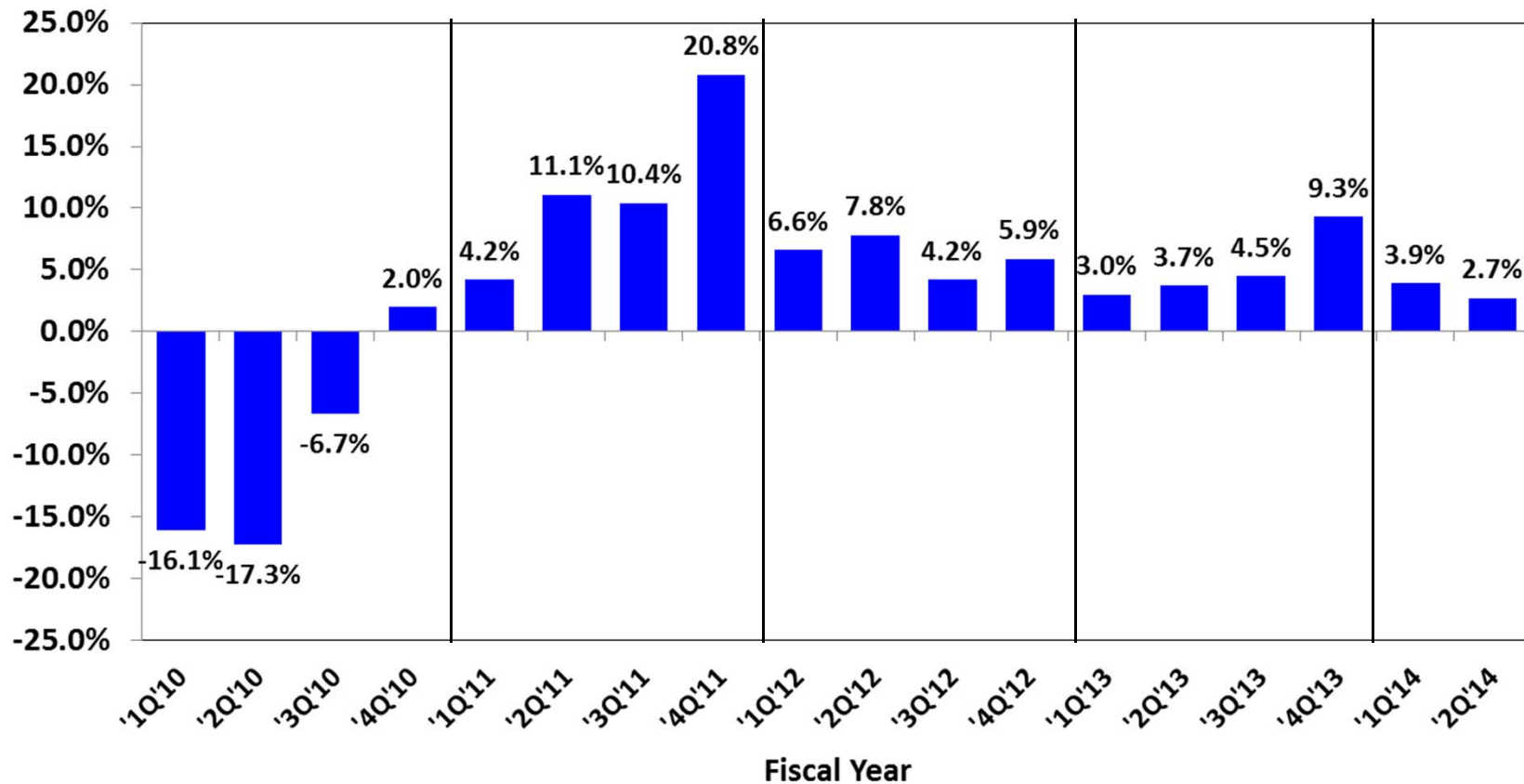
☐ Strengths

- 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

After Strong 4th Quarter of FY '13, Growth Has Slowed



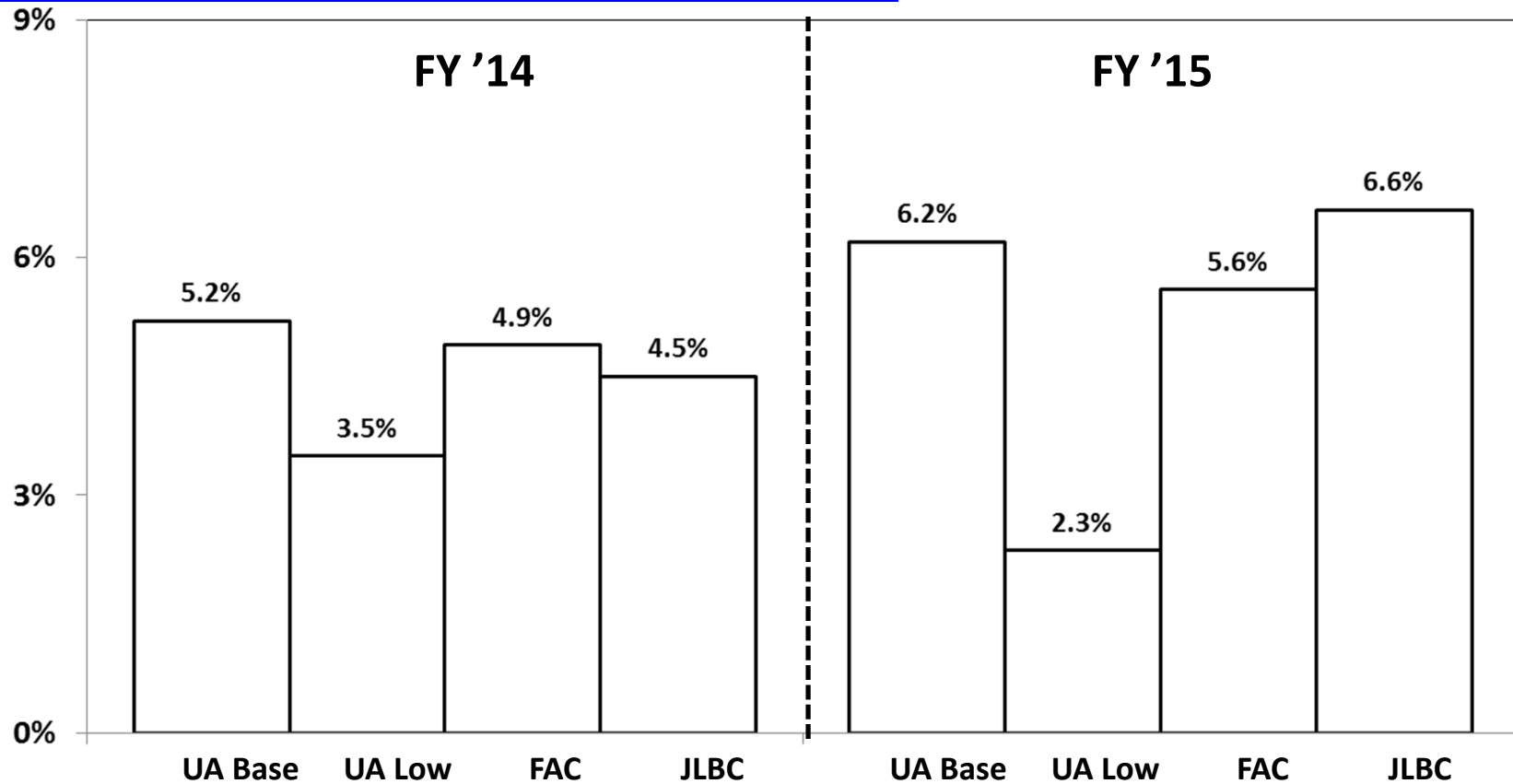
1st Half FY '14 Growth Rate 3.2%

- After Technical Adjustments, More Likely to be 4.0%
- \$10 M Above Original Budget Forecast

	Preliminary % Change over Prior Year
Sales Tax	6.7%
Individual Income Tax	3.4%
Corporate Income Tax	(14.8)%

- Strong sales tax growth led by retail and contracting
- Income tax withholding has increased by only 1.7%
- Increased use of tax credits may account for corporate decline

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

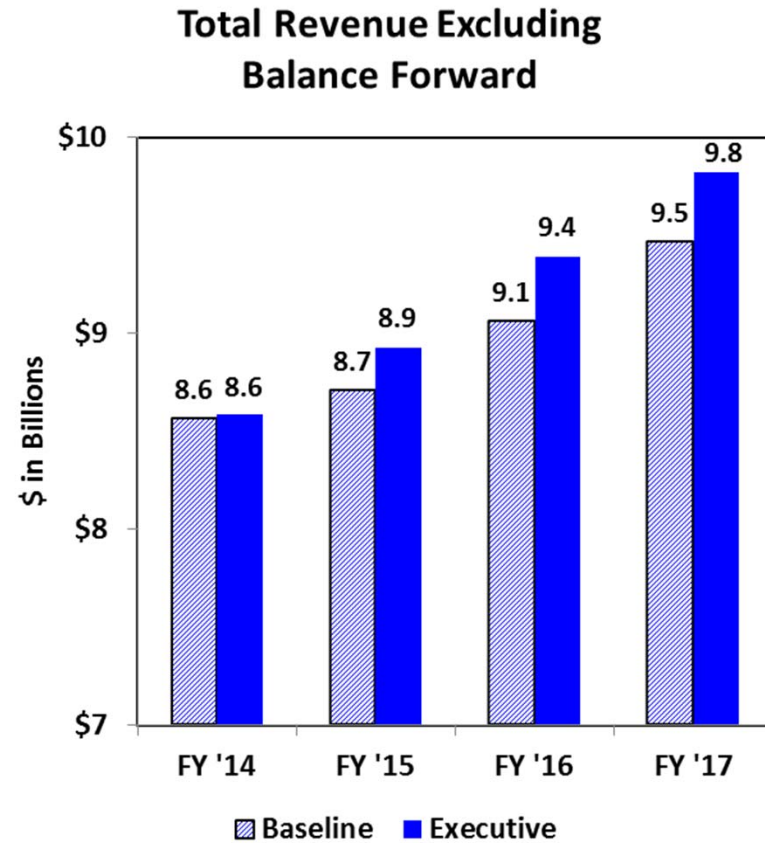
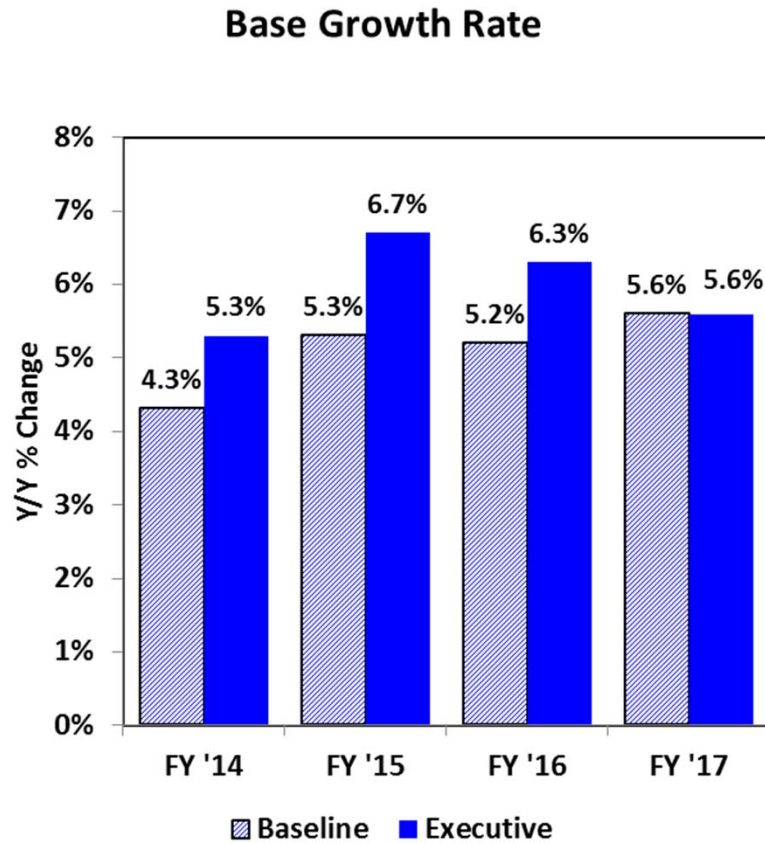
Baseline: FY '15 – FY '17 Revenue Changes

- Excludes Change in Beginning Balance

\$ in Millions

	FY '15 Above <u>FY '14</u>	FY '16 Above <u>FY '15</u>	FY '17 Above <u>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%

Executive Revenues Exceed Baseline By \$933 M Through '17



Baseline: FY '15 – FY '17 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 terms require buyback if state generates large cash balance and Rainy Day reserves
- ❑ The '15 reserves require the buyback of \$210 M in '17
- ❑ The Executive could change the terms and eliminate the buyback if it limits the investment yield to 4%
- ❑ Executive has not decided to change the terms, but includes no buyback

Legislative Proposal

– 2-Year DPS/HURF Proposal – No Executive Recommendation

- ❑ 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

Executive Caseloads \$(647) M Below JLBC Baseline

	'15-'17 <u>\$ in M</u>
<input type="checkbox"/> K-12	(329)
<ul style="list-style-type: none">● Executive does not fund charter conversion growth after '15● JLBC includes higher average cost per pupil	
<input type="checkbox"/> Medicaid	(318)
<ul style="list-style-type: none">● Executive assumes non-ACA population decline● Executive does not include 3% DD provider adjustment	

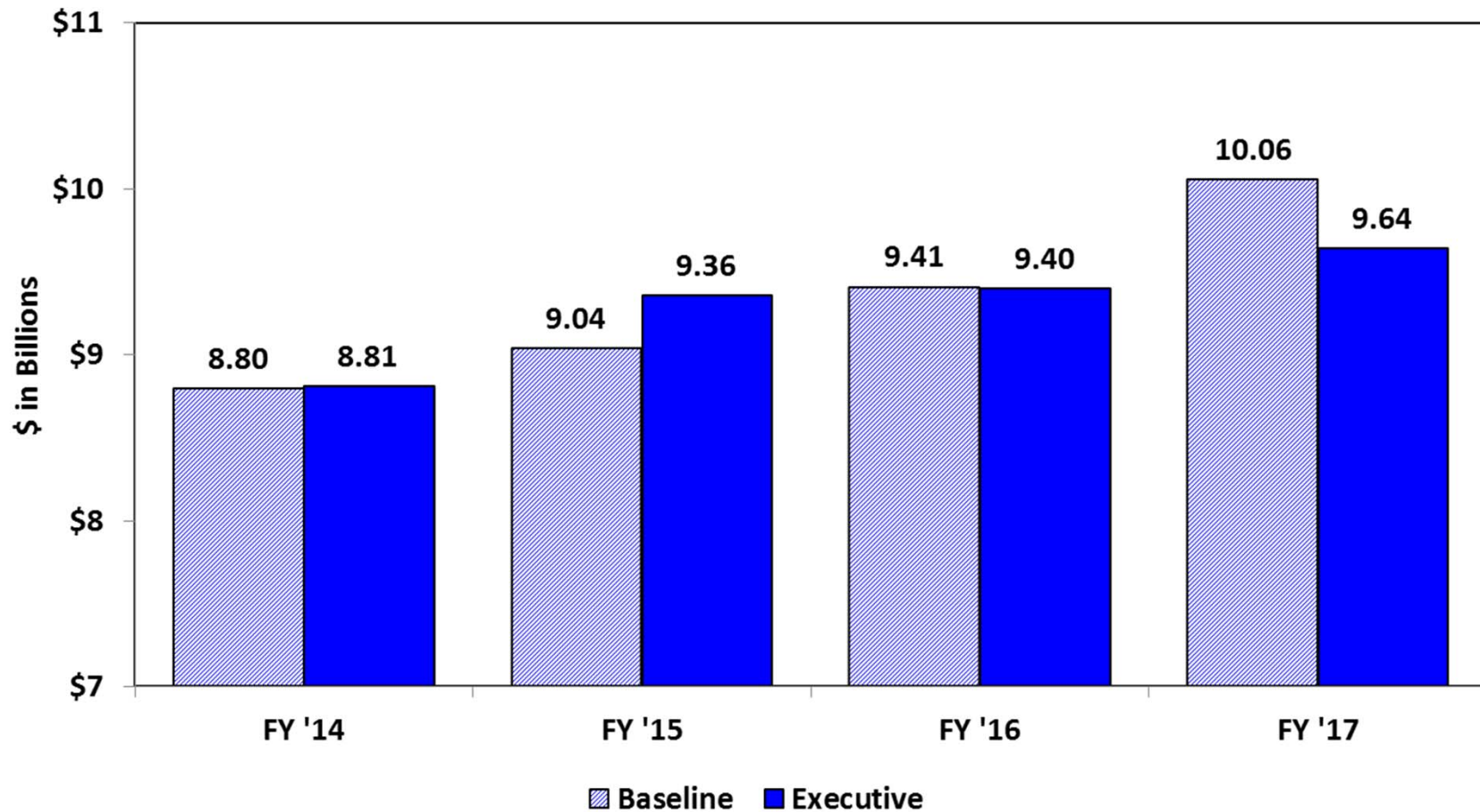
Major Executive Differences with JLBC

<u>Executive Proposals</u>	<u>'15 above '14</u> <u>(\$ in M)</u>
1. K-12 Education	96
• \$38 M for performance	
• \$31 M for small charters' hold harmless	
• \$14 M for new assessment and	
• \$9 M for data system funding	
2. Universities	27
• Parity: JLBC \$15 M, Exec \$27 M; Exec also adds \$15 M for TGen	
3. Community Colleges	4
• \$4 M to fully fund rural STEM formula	
4. DES Child Safety/Family Services	80
• 463 FTE and \$34 M	
- 212 caseworkers, 120 support, 93 OCWI, 30 records, 8 A.G.	
• \$12 M in new services	
• \$10 M for automation and	
• \$25 M in new agency transition (ADOA)	

Major Executive Differences with JLBC

<u>Executive Proposals</u>	<u>'15 above '14</u> <u>(\$ in M)</u>
5. Higher Retirement Rates (ADC, DPS) <ul style="list-style-type: none">• Exec funds employer share of increase	11
6. Capital/Infrastructure <ul style="list-style-type: none">• \$54 M building renewal• \$9 M Yuma veterans' home and• \$9 M DES data center	75
7. BSF Deposit	50

JLBC Baseline Versus Total Executive Spending



Updated FY '14 – '17 Budget Projections

Baseline

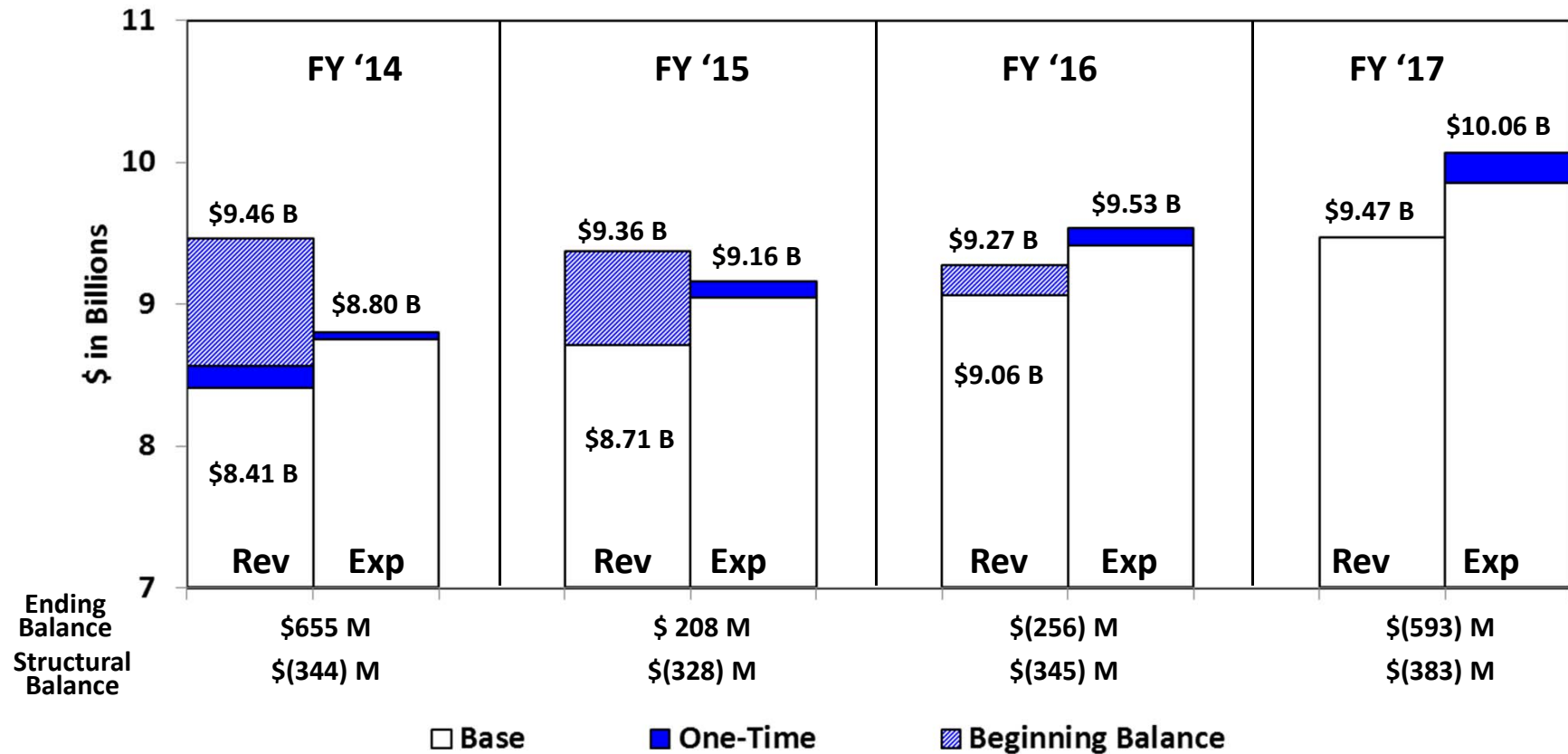
	<u>FY '14</u>	<u>FY '15</u>	<u>FY '16</u>	<u>FY '17</u>	
Balance Forward	\$895 M	\$655 M	\$327 M	\$0	\$(17) M
Baseline Revenues	\$8.56 B	\$8.71 B	\$9.06 B	\$9.47 B	
Baseline Spending	\$8.80 B	\$9.04 B	\$9.41 B	\$10.06 B	
Baseline Balance	\$655 M	\$327 M	\$(17) M	\$(593) M	\$(610) M

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

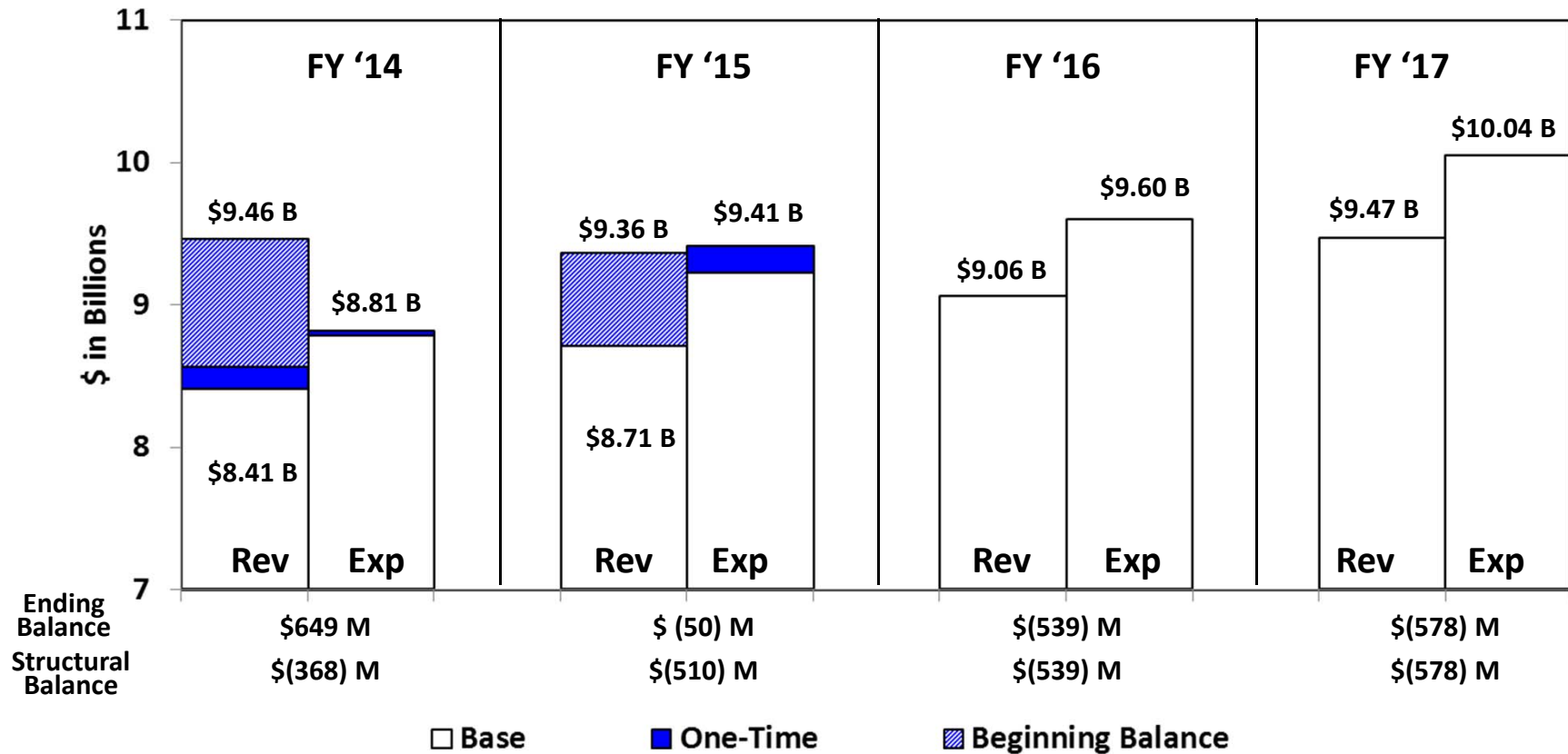
Baseline: Revenues Compared to Expenditures

- Adjusted for HURF Proposal



Comparing JLBC Revenues with Executive Spending

- Use JLBC K-12 and Medicaid Technical Estimates
- Exclude HURF Shift/Debt Buyback



FY '17: How JLBC's \$(849) M Shortfall Becomes Executive's \$421 M Surplus

<u>\$ in M</u>	
\$(849)	Baseline '17 shortfall
933	Higher Executive revenue – '14-'17
647	Lower Executive K-12 and Medicaid technical estimates – '15-'17
448	Executive removes HURF shift/debt buyback
<u>(758)</u>	Executive higher spending – '14-'17
\$ 421	Executive '17 Balance

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