
Finance Advisory Committee

Revenue and Budget Update

October 28, 2021

JLBC

Key Points

- ❑ General Fund revenues are growing rapidly
- ❑ The outcome of referenda, litigation and federal policy decisions will affect available resources
- ❑ Numerous scenarios possible, but we project an available ongoing balance of \$700 M and one-time balance of \$1.7 B in '23

October FAC: “Maximum Commitment” Scenario

- Not a Prediction of Litigation/Referenda Results

- Proposition 208 is upheld in litigation
- Set aside \$918 M of General Fund income tax revenues to transfer to the Prop 208 fund or for taxpayer refunds
- The enacted income tax reductions, including the triggers, go into effect
- The federal government does not extend the enhanced Medicaid match rate past March 2022

Forecasting State Revenues

4-Sector Forecast: Modest Growth after '22

4-Sector Components

- Finance Advisory Committee
- UA model – base
- UA model – more cautious
- JLBC Staff

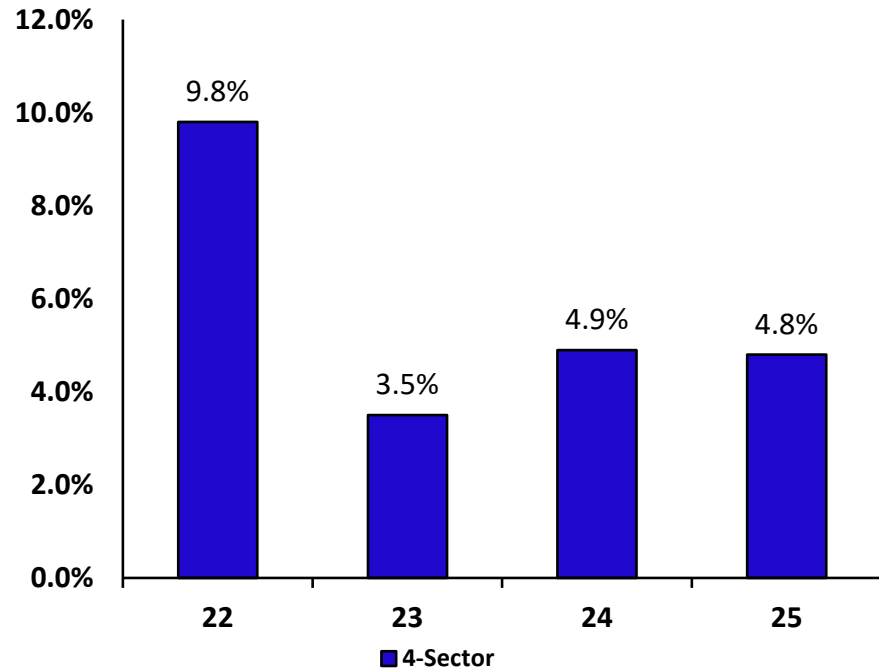
Represents Base Growth

- Prior to Enacted Tax Reductions

Income Tax Deferral

- '22% adjusted to remove 7/20 income tax deferral

Net % Revenue Growth



Excludes balance forward, one-time transfers, tax law changes and urban revenue sharing

See Appendix A

Summary of Forecasted Growth Rates

- Follows 18% Deferral-Adjusted Growth in '21

	<u>'22 YTD</u>	<u>'22 full year</u>	<u>'23</u>
TPT	15.6%	9.1%	3.5%
IIT w/out Deferral	18.1	9.6	4.9
CIT	23.5	8.8	3.5
IPT	29.7	6.5	2.6
Other	<u>104.3</u>	<u>21.2</u>	<u>(7.4)</u>
Total	19.3%	9.8%	3.5%

YTD Revenues are \$639 M above enacted forecast

Why Are Revenues Growing by 18% to 19%?

- ❑ AZ Personal Income grew by 8%+ in the last year
- ❑ Pandemic-accumulated savings are being spent over time
- ❑ Corporate profitability has been very strong
- ❑ % growth being measured from a “low” pandemic base

Major TPT Categories Exceed Pre-Pandemic Level

Sales Tax (TPT) % Change FY 22 Q1 over FY 20 Q1

Retail/Remote Sales	38%
Contracting	15
Restaurant/Bar	19
Lodging	11
Amusements	7

Individual Income Tax Rate Changes

- Current 4 Brackets Range from 2.59% to 4.5%

- Chapter 412 reduced 4 brackets to 2

Percent Income Tax Rates

<\$27k/\$55k >\$27k/\$55k

TY 22/FY 23	2.55	2.98
TY 23/FY 24	2.53	2.75
TY 24/FY 25	2.50	

- TY 23 & TY 24 contingent upon exceeding enacted budget trigger levels
- October revenue forecast exceeds trigger levels, but formal determination made in September '22 and '23

Other Individual Income Tax Changes

- ❑ 4.5% maximum income tax rate, starting in TY '21
 - Otherwise would be 8.0%, including Prop 208
 - Prop 208 receives 3.5%, General Fund 1%

- ❑ Alternative tax rate for certain income
 - Dividend/Interest/Business Income
 - Starts at 3.5% in TY '21 and declines to 2.5% in TY '25
 - Not subject to Prop 208

October FAC Projected Tax Reductions

- Base Growth Increases Level of Tax Reduction

	(\$ in M)			
	'22	'23	'24	'25
Income Tax Reduction Rate				
- Reduce to 2.55%/2.98% rate		(1,183)	(1,246)	(1,309)
- Reduce to 2.53%/2.75% rate			(282)	(297)
- Reduce to single 2.5% rate				(365)
Total Rate Reduction		(1,183)	(1,528)	(1,971)
4.5% Maximum IIT Rate	(918)	(545)	(507)	(457)
Alternative Tax Rate (SB 1783)	229	192	182	191
Other Enacted Reductions	(48)	(38)	(41)	(44)
Total Reductions	(737)	(1,574)	(1,894)	(2,281)

IIT Referenda and Litigation Status

- ❑ Ballot props would refer rate reductions to voters – signatures currently being checked
 - Results in up to \$2 B in tax cuts being on hold pending November '22 election results

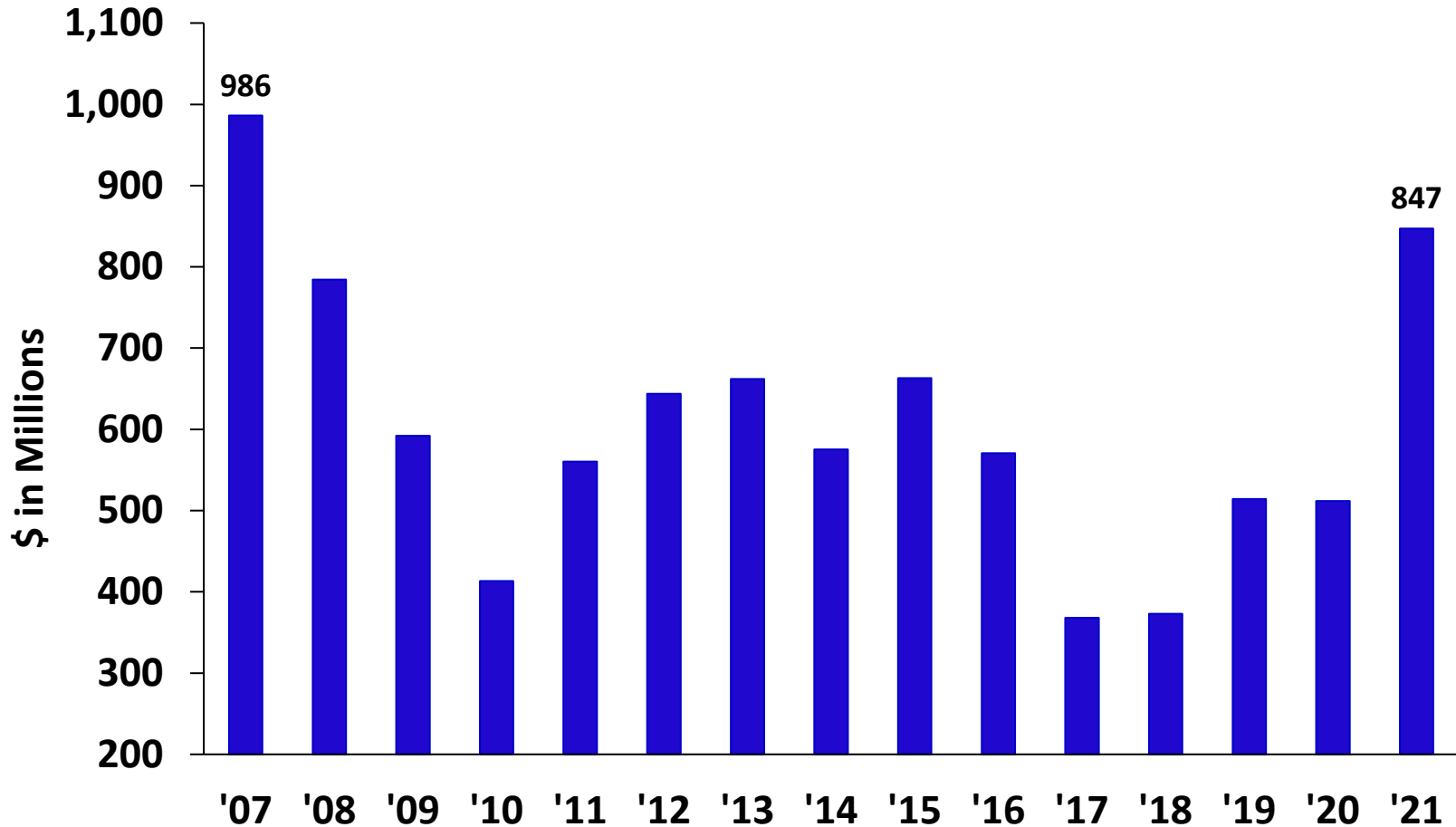
- ❑ AZ Supreme Court ruled that Prop 208 surcharge invalid if K-12 Aggregate Expenditure Limit exceeded
 - Trial court to make determination
 - If declared invalid, General Fund no longer pays cost to hold taxpayers to 4.5% maximum rate
 - Saves \$700 M in '22, declining to \$275 M by '25

Prop 208 Proceeds Currently in the General Fund

- ❑ 3.5% surcharge was effective as of January 2021
- ❑ If individuals increased their withholding/payments, those dollars are in the General Fund balance
- ❑ We do not think that Prop 208 share can be identified until taxpayers file returns in spring 2022
 - If 208 valid, \$ would move to Prop 208 fund
 - If 208 invalid, \$ would be refunded
- ❑ We suggest setting aside \$918 M of General Fund balance for either purpose.

Corporate Income Tax – Up 65% in '21

- Reflects Substantial increase in Profitability



JLBC's Updated Gaming Revenue Forecast

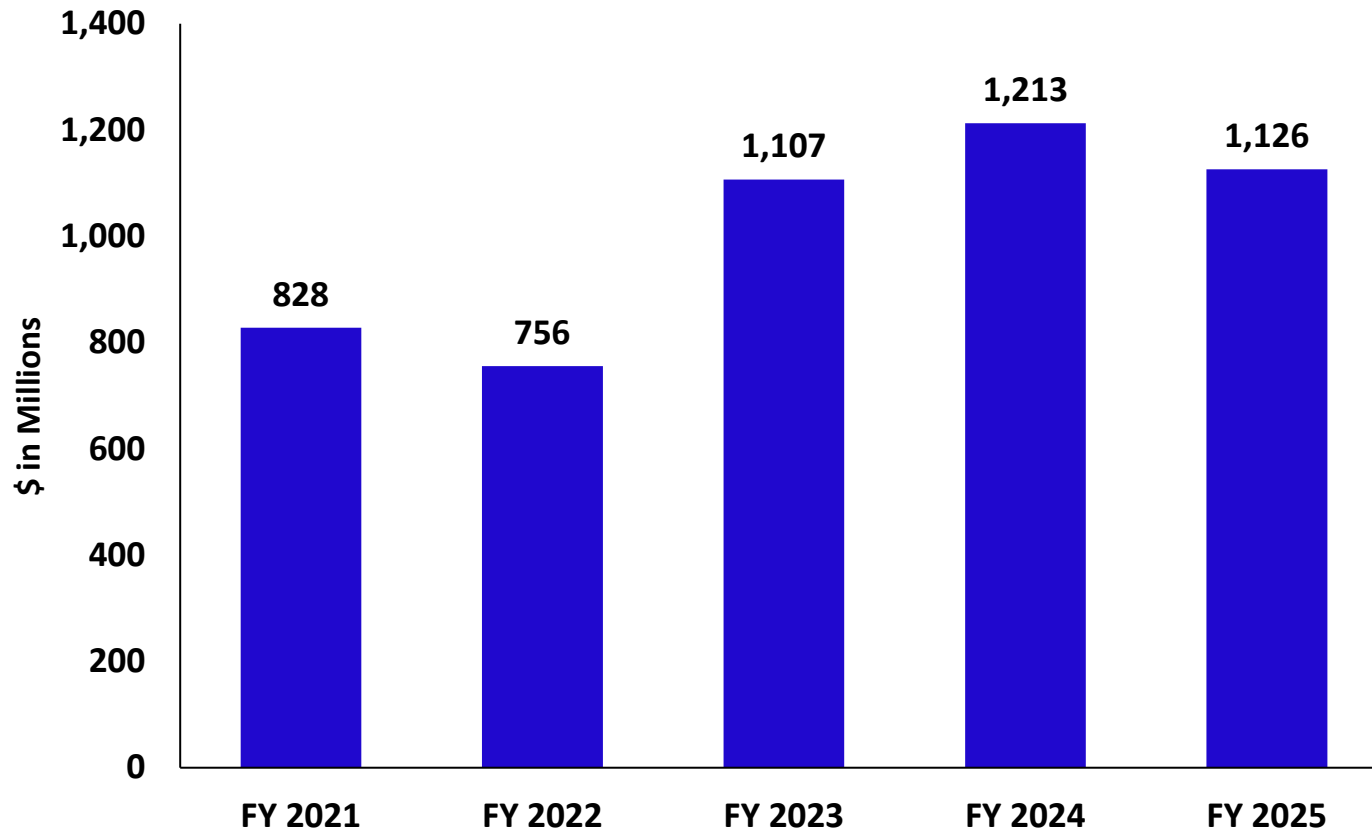
- February Fiscal Note estimated GF collections of \$34 M by '24

	\$ in M		
	<u>'22</u>	<u>'23</u>	<u>'24</u>
Lottery Keno/Mobile Draw	0	17	18
Event Wagering	25	18	19
Fantasy Sports Betting	<u>1</u>	<u>1</u>	<u>1</u>
Total	26	36	38

- Higher '22 event wagering revenue due to licensing fees
- Enacted budget assumed \$200 M in '23 and \$300 M in '24

Urban Revenue Sharing Distribution Increases

- Based on 15% of Income Taxes 2 Year Prior; Goes to 18% in '24



Spending Adjustments

Baseline Spending Projections

- ❑ Baseline reflects changes to active statutory/other funding formulas - no discretionary additions
- ❑ Assumes \$865 M in K-12 “rollover” at end of '23
- ❑ Assumes spending classified as one-time in '22 budget does not continue
 - Approximately \$180 M appears ongoing in nature

Baseline Spending Projected To Increase by \$277 M

'23 Ongoing Spending Changes

\$ in M

Medicaid Formula	129
ADE – K-12 Formula	317
Pension Contribution Savings	(110)
Fire Mitigation Initiatives	35
Other	<u>35</u>
Total	406

'23 One-Time Spending Additions/Deletions

\$ in M

Loss of Medicaid Match Savings	400
Universities	(46)
Community Colleges	(30)
SFB – Building Renewal Grants	(91)
SFB – Fewer New Buildings	(80)
Other Agency Spending	(190)
Capital Projects	<u>(92)</u>
Total	(129)

Total Spending Changes	\$277 M
Total Spending	\$12,821 M
% Change	2.2%

Federal Medicaid Match Generates State Savings

- Been in Place Since January 2020

- ❑ Feds have increased their share of costs while federal health emergency is in place
- ❑ Enacted budget assumed higher match would end in 12/21; feds have just extended to 3/22
- ❑ FAC forecast includes this new \$133 M of savings
- ❑ Feds may extend again past 3/22 – generates \$133 M of savings every quarter

Projected Ending Balances

Excludes \$970 M in Budget Stabilization Fund

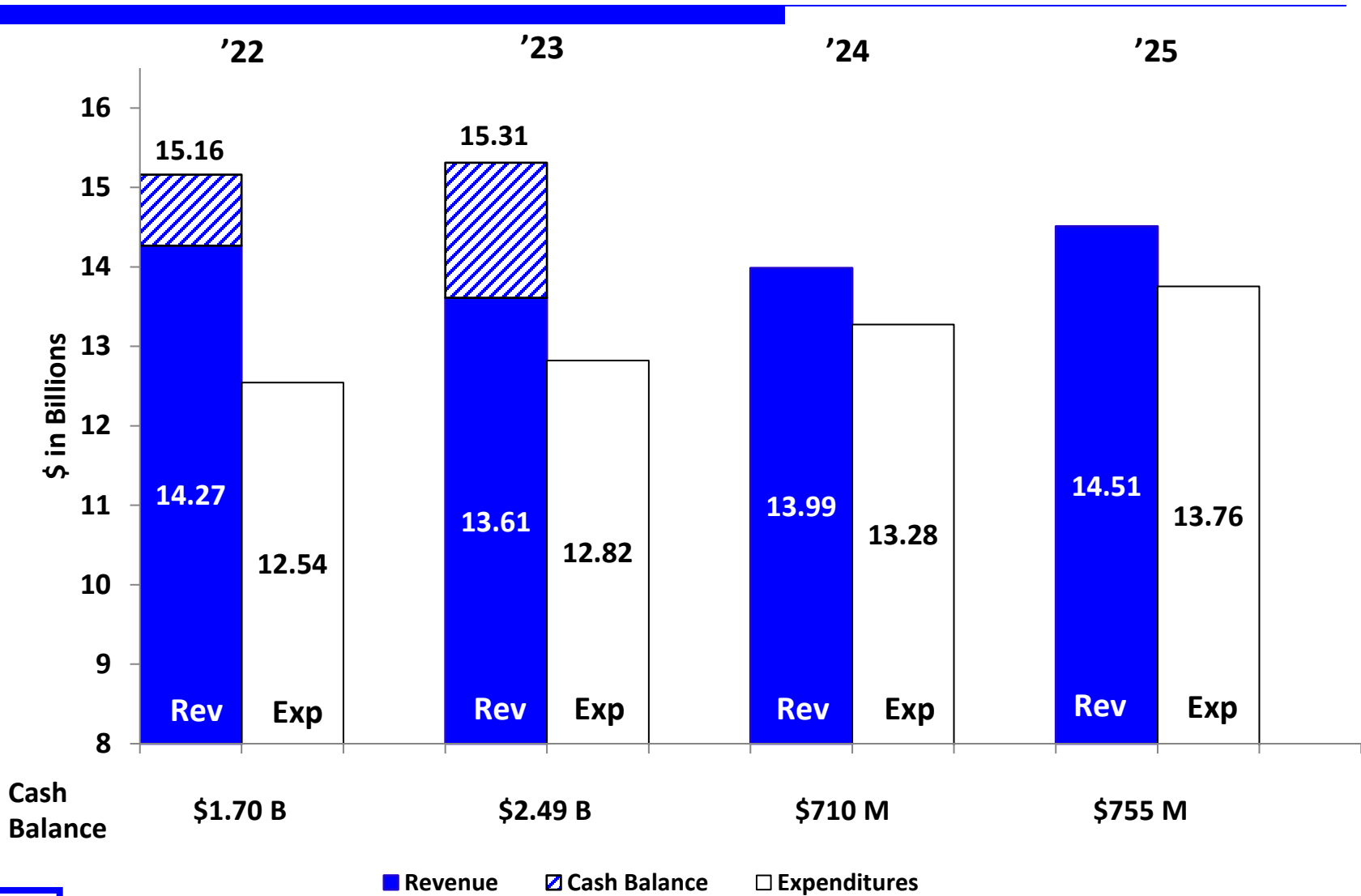
More Information in Appendix C

'21 Ending Balance Higher Than Projected

- ❑ The enacted budget projected a '21 ending balance of \$442 M
- ❑ The preliminary actual estimate is \$894 M due to unexpected 18% '21 revenue growth
- ❑ The preliminary results are \$452 M above the enacted forecast
- ❑ These additional revenues roll into '22

FAC Balances: \$700 M Ongoing & \$1.7 B One-Time

- \$1.7 B '22 Balance After \$918 M Set Aside for Prop 208 Reserve



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Appendix A: Revenue Forecasts with Deferral

	<u>2022</u> *	<u>2023</u>	<u>2024</u>	<u>2025</u>
Sales Tax				
JLBC Forecast	10.8%	3.5%	4.0%	4.0%
UA – Low	7.4%	1.2%	4.4%	4.8%
UA – Base	9.7%	3.0%	5.4%	5.1%
FAC	8.5%	6.1%	5.8%	5.3%
Average:	9.1%	3.5%	4.9%	4.8%
Individual Income Tax with Deferral				
JLBC Forecast	2.1%	3.6%	4.2%	4.3%
UA – Low	-1.2%	4.7%	5.0%	4.9%
UA – Base	0.1%	5.3%	5.4%	5.2%
FAC	0.4%	6.0%	6.6%	5.8%
Average:	0.4%	4.9%	5.3%	5.1%
Corporate Income Tax				
JLBC Forecast	10.0%	2.5%	4.0%	4.4%
UA – Low	10.0%	3.3%	4.2%	5.1%
UA – Base	11.4%	4.6%	5.1%	6.4%
FAC	3.9%	3.5%	5.1%	5.1%
Average:	8.8%	3.5%	4.6%	5.3%
Insurance Premium Tax				
JLBC Forecast	7.0%	1.5%	3.3%	3.4%
UA – Low	6.3%	1.6%	0.9%	3.2%
UA – Base	7.1%	3.0%	1.4%	3.4%
FAC	5.6%	4.5%	3.5%	3.8%
Average:	6.5%	2.6%	2.3%	3.5%

JLBC Weighted Average	6.6%	3.4%	4.1%	4.1%
UA Low Weighted Average	3.6%	2.9%	4.5%	4.8%
UA Base Weighted Average	5.3%	4.1%	5.2%	5.2%
FAC Consensus Weighted Average	4.4%	5.8%	6.0%	5.4%
“Big-4” Weighted Average	5.0%	4.1%	4.9%	4.9%
Consensus Weighted Average*	5.7%	3.5%	4.9%	4.8%

* Represents ongoing revenue adjusted for small revenue categories.

Appendix B: Revenue '21 - '23 with Deferral

FORECAST REVENUE GROWTH

(\$ in Thousands)

	PreI. ACTUAL FY 2021	% CHANGE PRIOR YR	FORECAST FY 2022	% CHANGE PRIOR YR	\$ CHANGE PRIOR YR	FORECAST FY 2023	% CHANGE PRIOR YR	\$ CHANGE PRIOR YR
Sales and Use	6,243,648.6	15.8%	6,811,703.5	9.1%	568,054.9	7,047,609.4	3.5%	235,905.9
Income - Individual	6,532,753.2	44.2%	6,507,862.3	-0.4%	(24,891.0)	5,655,722.5	-13.1%	(852,139.8)
- Corporate	847,020.8	65.5%	921,625.2	8.8%	74,604.4	953,679.0	3.5%	32,053.8
Property	22,380.0	-7.3%	21,500.0	-3.9%	(880.0)	20,581.8	-4.3%	(918.2)
Luxury - Tobacco	21,687.1	3.9%	21,412.0	-1.3%	(275.1)	21,191.5	-1.0%	(220.5)
- Liquor	43,150.6	19.0%	43,443.4	0.7%	292.8	44,217.3	1.8%	773.9
Insurance Premium	616,251.4	15.2%	656,282.1	6.5%	40,030.7	673,608.5	2.6%	17,326.4
Other Taxes	15,290.3	6.1%	15,519.7	1.5%	229.4	15,985.3	3.0%	465.6
Subtotal - Taxes	14,342,182.1	29.6%	14,999,348.1	4.6%	657,166.0	14,432,595.2	-3.8%	(566,752.9)
Other Non-Tax Revenues:								
Lottery	104,740.4	1.1%	232,701.3	122.2%	127,960.9	208,509.5	-10.4%	(24,191.8)
Gaming Revenue	0.0	N/A	26,101.3	N/A	26,101.3	18,467.0	-29.2%	(7,634.3)
Licenses, Fees and Permits	38,901.1	11.8%	40,680.4	4.6%	1,779.3	41,778.8	2.7%	1,098.4
Interest	(58.1)	N/A	39,414.5	N/A	39,472.6	25,000.0	-36.6%	(14,414.5)
Sales and Services	26,049.0	16.2%	27,038.9	3.8%	989.9	27,985.3	3.5%	946.4
Other Miscellaneous	147,887.4	17.4%	153,063.5	3.5%	5,176.1	156,185.9	2.0%	3,122.4
Transfers and Reimbursements	129,876.4	11.5%	94,320.6	-27.4%	(35,555.8)	63,805.3	-32.4%	(30,515.3)
Public Safety Transfers	23,357.7	0.1%	0.0	-100.0%	(23,357.7)	0.0	N/A	0.0
Disproportionate Share Revenue	84,858.6	-0.1%	82,729.0	-2.5%	(2,129.6)	95,417.3	15.3%	12,688.3
Subtotal - Other Non-Tax	555,612.6	0.8%	696,049.5	25.3%	140,436.9	637,149.0	-8.5%	(58,900.4)
Net Ongoing Revenue	14,897,794.7	28.2%	15,695,397.5	5.4%	797,602.9	15,069,744.2	-4.0%	(625,653.4)
Urban Revenue Sharing (URS)	(828,492.9)	N/A	(756,388.3)	N/A	72,104.6	(1,106,966.1)	N/A	(350,577.8)
Net Ongoing Revenue w/ URS	14,069,301.8	29.3%	14,939,009.2	6.2%	869,707.5	13,962,778.1	-6.5%	(976,231.2)
One-Time Financing Sources:								
Prescription Drug Rebate Fund Transfer	16,700.0	-75.8%	0.0	-100.0%	(16,700.0)	0.0	N/A	0.0
DPS Highway Patrol Fund Transfer	24,205.7	N/A	0.0	-100.0%	(24,205.7)	0.0	N/A	0.0
Water Infrastructure Repayment	0.0	N/A	20,000.0	N/A	20,000.0	0.0	-100.0%	(20,000.0)
4.5% Maximum Tax Rate	0.0	N/A	(917,862.7)	N/A	(917,862.7)	(544,607.4)	N/A	373,255.4
SB 1783 Impact	0.0	N/A	228,810.1	N/A	228,810.1	191,987.8	-16.1%	(36,822.2)
Subtotal - One-Time Financing Sources	40,905.7	-55.0%	(669,052.7)	N/A	(709,958.4)	(352,619.5)	N/A	316,433.1
Subtotal - Revenues	14,110,207.5	28.6%	14,269,956.5	1.1%	159,749.1	13,610,158.6	-4.6%	(659,798.1)
Balance Forward	372,457.0	-61.1%	893,700.0	139.9%	521,243.0	1,702,060.2	90.5%	808,360.2
Total - Resources	14,482,664.5	21.4%	15,163,656.6	4.7%	680,992.1	15,312,218.8	1.0%	148,562.1

Appendix B: Revenue '24 - '25

FORECAST REVENUE GROWTH						
(\$ in Thousands)						
	FORECAST FY 2024	% CHANGE PRIOR YR	\$ CHANGE PRIOR YR	FORECAST FY 2025	% CHANGE PRIOR YR	\$ CHANGE PRIOR YR
Sales and Use	7,392,786.0	4.9%	345,176.6	7,747,445.1	4.8%	354,659.1
Income - Individual	5,672,996.4	0.3%	17,273.9	5,328,770.5	-6.1%	(344,225.9)
- Corporate	997,476.5	4.6%	43,797.5	1,049,974.0	5.3%	52,497.5
Property	20,250.0	-1.6%	(331.8)	20,000.0	-1.2%	(250.0)
Luxury - Tobacco	21,203.8	0.1%	12.4	21,492.1	1.4%	288.3
- Liquor	45,280.9	2.4%	1,063.6	46,551.7	2.8%	1,270.8
Insurance Premium	688,912.8	2.3%	15,304.4	712,775.2	3.5%	23,862.3
Other Taxes	16,528.8	3.4%	543.5	17,107.3	3.5%	578.5
Subtotal - Taxes	14,855,435.2	2.9%	422,840.1	14,944,115.8	0.6%	88,680.5
Other Non-Tax Revenues:						
Lottery	228,286.5	9.5%	19,777.0	240,334.9	5.3%	12,048.4
Gaming Revenue	20,110.2	8.9%	1,643.2	21,421.2	6.5%	1,311.0
Licenses, Fees and Permits	43,324.6	3.7%	1,545.8	44,970.9	3.8%	1,646.3
Interest	27,500.0	10.0%	2,500.0	30,000.0	9.1%	2,500.0
Sales and Services	28,964.7	3.5%	979.5	29,978.5	3.5%	1,013.8
Other Miscellaneous	160,678.3	2.9%	4,492.4	165,334.7	2.9%	4,656.4
Transfers and Reimbursements	64,536.1	1.1%	730.8	64,591.1	0.1%	55.0
Public Safety Transfers	0.0	N/A	0.0	0.0	N/A	0.0
Disproportionate Share Revenue	95,474.3	0.1%	57.0	95,644.9	0.2%	170.6
Subtotal - Other Non-Tax	668,874.8	5.0%	31,725.7	692,276.2	3.5%	23,401.5
Net Ongoing Revenue	15,524,310.0	3.0%	454,565.8	15,636,392.0	0.7%	112,082.0
Urban Revenue Sharing (URS)	(1,213,278.3)	N/A	(106,312.2)	(1,126,220.7)	N/A	87,057.5
Net Ongoing Revenue w/ URS	14,311,031.7	2.5%	348,253.6	14,510,171.3	1.4%	199,139.5
One-Time Financing Sources:						
Prescription Drug Rebate Fund Transfer	0.0	N/A	0.0	0.0	N/A	0.0
DPS Highway Patrol Fund Transfer	0.0	N/A	0.0	0.0	N/A	0.0
Water Infrastructure Repayment	0.0	N/A	0.0	0.0	N/A	0.0
4.5% Maximum Tax Rate	(506,927.4)	N/A	37,679.9	0.0	N/A	506,927.4
SB 1783 Impact	181,972.5	-5.2%	(10,015.4)	0.0	-100.0%	(181,972.5)
Subtotal - One-Time Financing Sources	(324,955.0)	N/A	27,664.5	0.0	N/A	324,955.0
Subtotal - Revenues	13,986,076.8	2.8%	375,918.1	14,510,171.3	3.7%	524,094.5
Balance Forward	-	-100.0%	(1,702,060.2)	-	N/A	0.0
Total - Resources	13,986,076.8	-8.7%	(1,326,142.1)	14,510,171.3	3.7%	524,094.5

Appendix C: General Fund Balance Sheet

	FY 2022 October FAC	FY 2023 October FAC	FY 2024 October FAC	FY 2025 October FAC
REVENUES				
Ongoing Revenues	\$15,743,697,500	\$16,290,377,400	\$17,093,134,100	\$17,915,973,600
Enacted Rate Reduction (2.55%/2.98%)		(1,182,733,200)	(1,245,593,100)	(1,308,636,600)
Tier 1 Trigger Rate Reduction (2.53%/2.75%)			(282,431,000)	(296,725,700)
Tier 2 Trigger Rate Reduction (2.5% Flat Rate)				(365,200,900)
4.5% Maximum Tax Rate				(456,501,100)
SB 1783 Impact				191,182,700
Other Enacted Tax Reductions	(48,300,000)	(37,900,000)	(40,800,000)	(43,700,000)
Urban Revenue Sharing	(756,388,300)	(1,106,966,100)	(1,213,278,300)	(1,126,220,700)
Net Ongoing Revenues	\$14,939,009,200	\$13,962,778,100	\$14,311,031,700	\$14,510,171,300
One-time Financing Sources				
Balance Forward	\$893,700,000	\$1,702,060,200		
4.5% Maximum Tax Rate (Ongoing in FY 25)	(917,862,700)	(544,607,400)	(506,927,400)	
SB 1783 Impact (Ongoing in FY 25)	228,810,100	191,987,900	181,972,500	
Water Infrastructure Repayment	20,000,000			
Subtotal One-time Revenues	\$224,647,400	\$1,349,440,700	(\$324,954,900)	\$0
Total Revenues	\$15,163,656,600	\$15,312,218,800	\$13,986,076,800	\$14,510,171,300
EXPENDITURES				
Ongoing Operating Appropriations	\$12,321,812,800	\$12,700,916,300	\$13,251,748,500	\$13,731,644,100
Administrative Adjustments	120,000,000	158,000,000	158,000,000	158,000,000
Reversions	(192,000,000)	(203,000,000)	(203,000,000)	(203,000,000)
Subtotal Ongoing Expenditures	\$12,249,812,800	\$12,655,916,300	\$13,206,748,500	\$13,686,644,100
One-time Expenditures				
Capital Outlay	\$92,632,900			
Reduce K-12 Rollover (Enacted)	65,000,000			
Operating One-Time Spending	666,235,900	165,243,100	69,117,200	68,596,500
New Medicaid Federal Match Reversion <u>1/</u>	(400,000,000)			
New ADE Formula Funding Reversion <u>1/</u>	(150,000,000)			
27th Pay Period (Enacted)	20,052,100			
Subtotal One-time Expenditures	\$293,920,900	\$165,243,100	\$69,117,200	\$68,596,500
Total Expenditures	\$12,543,733,700	\$12,821,159,400	\$13,275,865,700	\$13,755,240,600
Proposition 208 Reserve <u>2/</u>	\$917,862,700			
Ending Balance <u>3/</u>	\$1,702,060,200	\$2,491,059,400 <u>4/</u>	\$710,211,100	\$754,930,700

1/ Reflects reversion of savings for a higher federal Medicaid match rate and lower K12 formula costs.

2/ Reflects Proposition 208 uncertainty. If surcharge upheld, revenue would be transferred to Proposition 208 fund. If surcharge not upheld, state would refund revenue.

3/ Reflects the difference between total revenues and total expenditures. Excludes any Budget Stabilization Fund balance.

4/ The FY 2023 cash balance is presumed to be allocated as part of the FY 2023 budget process.