

GENERAL FUND REVENUE

FY 2003

The recommendation is based on a FY 2003 General Fund revenue estimate of \$5.69 billion, prior to any new policy changes to balance the FY 2003 budget. This estimate is based on \$5.52 billion of revenue and \$169.6 million of fund transfers.

The changes to the revenue estimates from the FY 2003 budget adopted in the spring of 2002 are as follows:

Table 1	
FY 2003 Revenue Forecast	
(\$ in Millions)	
Adopted FY 2003 Revenue Estimate	\$6,173.8
Revised Revenue Forecast	(508.3)
Transfer Shortfall	<u>(25.0)</u>
Subtotal	5,640.5
6 th Special Session Transfers	<u>50.9</u>
Revised FY 2003 Revenue Estimate	\$5,691.4

The FY 2003 estimate assumes a revenue decline of (3.9)% compared to the prior year. Year-to-date through December revenues have declined (3.3)% compared to FY 2002.

The individual revenue detail is found in [Table 7](#) and [Table 8](#) at the end of this section.

New FY 2003 Policy Changes

The FY 2003 General Fund recommended revenue level, including policy changes to balance the budget, is \$6.01 billion. This amount consists of \$5.58 billion of base revenue, and \$431.7 million of fund transfers.

There are 3 policy changes to generate additional revenue:

- \$262.2 million in new fund transfers (*see Fund Transfer section in the Proposed Budget volume for more detail*).
- \$15 million in county payments for restoration to competency treatment at the Arizona State Hospital, pretrial care of the sexually violent person population, and probation.
- \$45 million from reversing the “Ladewig” set-aside from \$75 million to \$30 million.

Based on the 2001 Arizona Supreme Court decision in the *Ladewig v. State of Arizona* case, the state is required to refund individual income taxes paid on non-Arizona dividends earned for the years 1986 through 1989. Payments and costs associated with this case are expected to total approximately \$348 million over the next 5 years.

Laws 2002, Chapter 321 provides a \$75 million “set-aside” for FY 2003 for first year payments and costs associated with the *Ladewig* case. The JLBC recommendation reduces this set-aside for FY 2003 to \$30 million. As noted in [Table 2](#) below, the set-aside would remain at \$75 million in FY 2004, and increase each year through FY 2007 to cover the total payments and costs associated with the case.

Table 2			
Ladewig Settlement			
(\$ in Millions)			
<u>Fiscal Year</u>	<u>Budget</u>		<u>Balance</u>
	<u>Allocation</u>	<u>Cost</u>	
2003	30.0	13.5	16.5
2004	75.0	7.3	84.2
2005	77.5	161.7	0.0
2006	81.4	81.4	0.0
2007	84.1	84.1	0.0

In summary, the FY 2003 policy changes are as follows:

Table 3	
FY 2003 Policy Changes	
(\$ in Millions)	
Revised FY 2003 Revenues	\$5,691.4
• Fund Transfers	262.2
• Additional Revenue - County Contributions	15.0
• Ladewig Reversion	<u>45.0</u>
Recommended FY 2003 Revenues	\$6,013.6
• Base Revenues	5,581.9
• Transfers	431.7

FY 2004

The recommendation is based on a FY 2004 General Fund revenue estimate of \$5.51 million, prior to any new policy changes to balance the FY 2004 budget. The estimate includes only base revenue. The changes to the FY 2004 revenue estimate from the revised FY 2003 estimate are as follows:

Revised FY 2003 Revenue Estimate	\$5,691.4
One-time FY 2003 Fund Transfers	(169.5)
Disproportionate Share Reduction	(61.7)
Urban Revenue Sharing Reduction	65.5
Estate Tax Reduction	(19.3)
Flight Property Tax	(7.0)
Revenue Growth @ 0.2%	<u>11.0</u>
FY 2004 Revenue Estimate	\$5,510.4

As noted in the table above, the FY 2004 estimate is \$181.0 million below estimated collections for FY 2003. The reduction is based primarily on the one-time transfers in FY 2003 and reduced federal disproportionate share revenues. In addition, estate tax estimates have been reduced to reflect the second year of the 4-year phase-out of the estate tax (based on federal tax law changes), and the estimated impact of depositing all of the flight property tax into the Aviation Fund (based on Laws 2001, Chapter 286).

These reductions are partially offset by a reduction in Urban Revenue Sharing (URS) to local cities. The annual URS distribution to cities is normally 15% of state income tax collections from 2 years prior. Laws 2002, Chapter 344 reduced this rate from 15% to 14.8% for FY 2003 and FY 2004. FY 2002 state income tax collections fell significantly below FY 2001 collections. Due to the 2 year lag in the URS distribution, this decline will begin to affect local distributions in FY 2004. The URS distribution will fall from \$430.6 million in FY 2003 to \$365.1 million in FY 2004, which will result in a relative increase in General Fund revenues compared to the previous year.

The estimated baseline revenue growth for FY 2004 is 0.2% compared to FY 2003. Note that the baseline revenue estimate reflects the forecasted “natural” growth in revenues, prior to accounting for any tax law changes or legislative actions.

JLBC Staff hosted a meeting of the Finance Advisory Committee (FAC) in December 2002. The FAC consists of 18 economists and financial experts which meet at least 3 times a year to advise the Legislature on the economy.

In light of the current (3.3)% decline in FY 2003 revenues, JLBC Staff presented a “no growth” scenario where baseline FY 2004 revenues would grow by only 0.2%, and a “slow growth” scenario, with baseline revenue growth of 2.5%. The FAC panel noted that they anticipated a slow recovery over the next year, but that there were currently no existing signs of a recovery in the state. Based on this outlook, the majority of the panel generally supported a FY 2004 revenue forecast in the no growth to slow growth range.

The JLBC Chairmen have opted to use the no growth forecast, with baseline revenue growth of 0.2%, for the FY 2004 JLBC recommendation.

The individual revenue detail for FY 2004 is found in [Table 7](#) and [Table 8](#) at the end of this section.

FY 2004 Policy Changes

The FY 2004 General Fund recommended revenue level, including policy changes, is \$6.09 billion. This amount consists of \$5.56 of base revenue and \$528.8 million of fund transfers and asset sales.

There are 3 policy changes to generate additional revenue:

- \$46.1 million in various revenue provisions. They include \$9.8 million related to drug treatment and education (*see Judiciary Section – Supreme Court*), \$1.8 million related to Medicaid reimbursement (*see AHCCCS Section*), and \$1.75 million related to sales tax distribution to qualified Indian tribes (*see Community College Section*). In addition, there would be \$25.7 million in county payments for pretrial care of the sexually violent population at the Arizona State Hospital (*see Department of Health Services Section*), and for probation costs (*see Judiciary Section*). These payments would continue a policy of billing for these services begun in FY 2003.

Finally, there is \$7.0 million from the deferral of the implementation of flight property tax transfer from the General Fund to the Aviation Fund. As noted above, Laws 2001, Chapter 286 provides for all of flight property tax revenues to be deposited into the Aviation Fund beginning in FY 2004. The JLBC recommendation would delay this transfer until FY 2006.

- \$178.8 million in fund transfers (*see Fund Transfer section in the Proposed Budget volume for more detail*).
- \$350.0 million in asset sales. The state’s 3 building systems consist of 5,165 facilities with a total replacement value of \$6.8 billion. The following table shows the facility information for each building system.

Table 5**State Facilities
(\$ in Millions)**

	<u>ADOA</u>	<u>Univ.</u>	<u>ADOT</u>	<u>Total</u>
Number of Facilities	2,793	971	1,401	5,165
Replacement Value	\$2,034.7	\$4,535.2	\$277.2	\$6,847.1

In addition, state agencies also have other types of assets such as computer and telecommunication equipment, airplanes, and other specialized and heavy equipment.

In summary, the FY 2004 policy changes are as follows:

Table 6**FY 2004 Policy Changes
(\$ in Millions)**

FY 2004 Revenues	\$5,510.4
• Additional Revenues	46.1
• Fund Transfers	178.8
• Asset Sales	<u>350.0</u>
Recommended FY 2004 Revenues	\$6,085.3
• Base Revenues	5,556.5
• Transfers	528.8

GENERAL FUND REVENUE JLBC STAFF FORECAST FY 2003 - FY 2004

BASELINE REVENUE GROWTH ^{1/}							
(\$ in Thousands)							
	BASELINE ESTIMATE FY 2002	BASELINE FORECAST FY 2003	% CHANGE FY 2002 ACTUAL	\$ CHANGE FY 2002 ACTUAL	BASELINE FORECAST FY 2004	% CHANGE FY 2003 ADJUSTED	\$ CHANGE FY 2003 ADJUSTED
Taxes:							
Sales and Use	3,002,148.4	3,020,240.0	0.7%	19,856.2	3,039,900.0	0.7%	19,700.0
Income -Individual	2,066,823.4	2,009,695.9	-3.7%	(76,952.8)	2,009,082.4	-0.3%	(5,048.0)
-Corporate	383,740.0	262,733.0	-24.1%	(83,547.4)	278,500.0	-2.3%	(6,500.0)
Property	37,916.5	35,038.3	-1.8%	(643.3)	32,000.0	-3.9%	(1,300.0)
Luxury	66,069.6	66,104.0	0.1%	34.4	66,427.0	0.5%	323.0
Insurance Premium	195,333.0	217,845.7	11.5%	22,512.7	217,656.2	-0.1%	(189.5)
Motor Vehicle License	0.0	0.0	N/A	0.0	0.0	N/A	0.0
Estate	80,552.2	86,000.0	6.8%	5,447.8	67,170.0	0.0%	0.0
Other Taxes	2,223.5	2,262.8	1.8%	39.3	2,262.8	0.0%	0.0
Sub-Total - Taxes	5,834,806.6	5,699,919.7	-1.9%	(113,253.1)	5,712,998.4	0.1%	6,985.5
Other Non-Tax Revenues:							
Lottery	21,000.0	31,000.0	0.0%	0.0	25,000.0	0.0%	0.0
Licenses, Fees and Permits	128,751.5	106,995.2	-1.6%	(1,756.3)	106,795.2	0.0%	0.0
Interest	33,023.7	15,000.0	-54.6%	(18,023.7)	20,000.0	33.3%	5,000.0
Transfers and Reimbursements	95,056.8	77,784.3	-19.4%	(18,672.2)	24,359.5	-3.7%	(940.6)
Disproportionate Share Revenue	64,200.7	87,623.9	0.0%	(1.0)	149,301.1	0.0%	0.0
Sub-Total - Non-Tax	342,032.7	318,403.4	-10.8%	(38,453.2)	325,455.8	1.3%	4,059.4
Subtotal Base Revenue	6,176,839.3	6,018,323.1	-2.5%	(151,706.3)	6,038,454.2	0.2%	11,044.9
Urban Revenue Sharing (URS)	(421,876.6)	(426,288.8)	1.0%	(4,412.2)	(369,215.5)	-14.2%	61,349.4
Litigation/Other Set-Aside	0.0	0.0	N/A	0.0	(75,000.0)	0.0%	0.0
Base Revenue w/URS/Litigation	5,754,962.7	5,592,034.3	-2.7%	(156,118.5)	5,594,238.7	1.3%	72,394.3
2nd SS Revenue Enhancements	0.0	337,911.2	0.0%	0.0	0.0	N/A	0.0
3rd SS Revenue Enhancements	0.0	153,261.1	0.0%	0.0	0.0	N/A	0.0
2nd RS Revenue Enhancements	0.0	0.0	N/A	0.0	118,624.4	0.0%	0.0
6th SS Revenue Enhancements	0.0	0.0	N/A	0.0	50,928.0	0.0%	0.0
Total Base Revenue	5,754,962.7	6,083,206.6	-2.5%	(156,118.5)	5,763,791.1	1.3%	72,394.3

^{1/} The baseline forecast represents revenue growth prior to accounting for tax law changes.

GENERAL FUND REVENUE JLBC STAFF FORECAST FY 2003 - FY 2004

ADJUSTED REVENUE GROWTH ^{1/}							
(\$ in Thousands)							
	ACTUAL FY 2002	ADJUSTED FORECAST FY 2003	% CHANGE FY 2002 ACTUAL	\$ CHANGE FY 2002 ACTUAL	ADJUSTED FORECAST FY 2004	% CHANGE FY 2003 ADJUSTED	\$ CHANGE FY 2003 ADJUSTED
Taxes:							
Sales and Use	3,000,383.8	3,020,200.0	0.7%	19,816.2	3,039,900.0	0.7%	19,700.0
Income -Individual	2,086,648.7	2,014,130.4	-3.5%	(72,518.3)	2,009,082.4	-0.3%	(5,048.0)
-Corporate	346,280.4	285,000.0	-17.7%	(61,280.4)	278,500.0	-2.3%	(6,500.0)
Property	35,681.6	33,300.0	-6.7%	(2,381.6)	25,000.0	-24.9%	(8,300.0)
Luxury	66,069.6	66,104.0	0.1%	34.4	66,427.0	0.5%	323.0
Insurance Premium	195,333.0	217,845.7	11.5%	22,512.7	217,656.2	-0.1%	(189.5)
Motor Vehicle License	0.0	0.0	N/A	0.0	0.0	N/A	0.0
Estate	80,552.2	67,170.0	-16.6%	(13,382.2)	47,860.0	-28.7%	(19,310.0)
Other Taxes	2,223.5	2,262.8	1.8%	39.3	2,262.8	0.0%	0.0
Sub-Total - Taxes	5,813,172.8	5,706,012.9	-1.8%	(107,159.9)	5,686,688.4	-0.3%	(19,324.5)
Other Non-Tax Revenues:							
Lottery	31,000.0	25,000.0	-19.4%	(6,000.0)	25,000.0	0.0%	0.0
Licenses, Fees and Permits	108,751.5	106,795.2	-1.8%	(1,956.3)	106,795.2	0.0%	0.0
Interest	33,023.7	15,000.0	-54.6%	(18,023.7)	20,000.0	33.3%	5,000.0
Transfers and Reimbursements	96,456.5	25,300.1	-73.8%	(71,156.4)	24,359.5	-3.7%	(940.6)
Disproportionate Share Revenue	87,624.9	149,301.1	70.4%	61,676.2	87,623.9	-41.3%	(61,677.2)
Sub-Total - Non-Tax	356,856.6	321,396.4	-9.9%	(35,460.2)	263,778.6	-17.9%	(57,617.8)
Subtotal Adjusted Revenue	6,170,029.4	6,027,409.3	-2.3%	(142,620.1)	5,950,467.0	-1.3%	(76,942.3)
Urban Revenue Sharing (URS)	(421,876.6)	(430,564.9)	2.1%	(8,688.3)	(365,065.1)	-15.2%	65,499.8
Litigation/Other Set-Aside	0.0	(75,000.0)	N/A	(75,000.0)	(75,000.0)	0.0%	0.0
Adjusted Revenue w/URS/Litigation	5,748,152.8	5,521,844.4	-3.9%	(226,308.4)	5,510,401.9	-0.2%	(11,442.5)
2nd SS Revenue Enhancements	337,911.2	0.0	-100.0%	(337,911.2)	0.0	N/A	0.0
3rd SS Revenue Enhancements	153,261.1	0.0	-100.0%	(153,261.1)	0.0	N/A	0.0
2nd RS Revenue Enhancements	0.0	118,624.4	N/A	118,624.4	0.0	-100.0%	(118,624.4)
6th SS Revenue Enhancements	0.0	50,928.0	N/A	50,928.0	0.0	-100.0%	(50,928.0)
Total Adjusted Revenue	6,239,325.1	5,691,396.8	-8.8%	(547,928.3)	5,510,401.9	-3.2%	(180,994.9)

^{1/} The adjusted revenue forecast includes tax law changes and represents a "bottom line" revenue growth estimate.

BASELINE REVENUE ADJUSTMENTS BY CATEGORY		
(\$ in Thousands)		
Summary By Category:	FY 2003 ^{1/}	FY 2004 ^{1/}
Tax Law Changes		
Sales & Use Tax	(40.0)	0.0
Individual Income Tax	4,434.5	0.0
Corporate Income Tax	22,267.0	0.0
Property Tax	(1,738.3)	(7,000.0)
Estate Tax	(18,830.0)	(19,310.0)
Subtotal - Tax Law Changes	6,093.2	(26,310.0)
Other Revenue Adjustments		
Disproportionate Share	61,677.2	(61,677.2)
Litigation/Other Set-Aside	(75,000.0)	0.0
Licenses and Fees	(200.0)	0.0
Transfers & Reimbursements	(52,484.2)	0.0
URS Hold Harmless ^{2/}	(9,960.0)	4,968.4
URS Reduction ^{3/}	5,683.9	(818.0)
Lottery (3rd Special Session)	(6,000.0)	0.0
Balance Transfers (2nd Special Session)	(337,911.2)	0.0
Balance Transfers (3rd Special Session)	(153,261.1)	0.0
Balance Transfers (2nd Regular Session)	143,624.4	(143,624.4)
Balance Transfer Adjustment ^{4/}	(25,000.0)	25,000.0
Balance Transfers (6th Special Session)	50,928.0	(50,928.0)
Subtotal - Other Revenue Adjustments	(397,903.0)	(227,079.2)
TOTAL REVENUE CHANGES	(391,809.8)	(253,389.2)

ADJUSTMENTS BY INDIVIDUAL PROVISION

Ch.	Reference Title	FY 2003	FY 2004	Revenue Category
<u>45th Legislature - 6th Special Session:</u>				
1	Fund Transfers/ASH	50,928.0	(50,928.0)	Bal Transfers
	Session Total	<u>50,928.0</u>	<u>(50,928.0)</u>	
<u>45th Legislature - 2nd Regular Session</u>				
327	Fund Transfers/BSF	143,624.4	(143,624.4)	Bal Transfers
	Balance Transfer Adjustment ^{4/}	(25,000.0)	25,000.0	Bal Transfers
na	Prison Funding	3,800.0	0.0	Transfers
328	Equine Fees	(200.0)	0.0	Licenses/Fees
328	VLT Enforcement	3,500.0	0.0	Transfers
329	Dispro Share	61,677.2	(61,677.2)	Dispro Share
50	Repeal Dividends Income Tax Subtraction	11,200.0	0.0	Corporate
344	IRC Conformity/Revenue Sharing	5,610.0	0.0	Corporate
		(14,480.0)	0.0	Individual
		(18,830.0)	(19,310.0)	Estate
		5,683.9	(818.0)	URS ^{3/}
	Subtotal - Chapter 344	<u>(22,016.1)</u>	<u>(20,128.0)</u>	
	Session Total	<u>176,585.5</u>	<u>(200,429.6)</u>	

Table 9

<u>Ch.</u>	<u>Reference Title</u>	<u>FY 2003</u>	<u>FY 2004</u>	<u>Revenue Category</u>
<u>45th Legislature - 3rd Special Session:</u>				
328	Lottery-Increase Powerball to GF	(6,000.0)	0.0	Lottery
327	Fund Transfers/BSF	(153,261.1)	0.0	Bal Transfers
na	Litigation/Other Set-Aside	(75,000.0)	0.0	Other
	Session Total	<u>(234,261.1)</u>	<u>0.0</u>	
<u>45th Legislature - 2nd Special Session:</u>				
2	ORB-Finance; Withholding ^{5/}	(60,000.0)	0.0	Individual
2	ORB-Finance; Tax Amnesty	(10,000.0)	0.0	Individual
328	Sale of Airplane	(500.0)	0.0	Transfers
327	Fund Transfers/BSF	(337,911.2)	0.0	Bal Transfers
	Session Total	<u>(408,411.2)</u>	<u>0.0</u>	
<u>45th Legislature - 1st Regular Session:</u>				
232	Supplemental Appropriations; (Corrections Fund Transfer)	(15,000.0)	0.0	Transfers
261	Department of Revenue; Confidentiality	(100.0)	0.0	Individual
277	Nuclear Emergency Appropriation/Assessment	15.8	0.0	Transfers
286	Flight Property Tax Revenues	0.0	(7,000.0)	Property
296	Internal Revenue Code Conformity	(217.0)	0.0	Corporate
		(105.0)	0.0	Individual
	Subtotal - Chapter 296	<u>(322.0)</u>	<u>0.0</u>	
370	Enterprise Zone Program; Extension	cannot be determined		Corporate
na	Water Banking Fees	700.0	0.0	Transfers
na	Sale of Assets (revenue increase)	(15,000.0)	0.0	Transfers
na	Alt Fuel Refunds (Individual Income Tax) ^{6/}	26,700.0	0.0	Individual
na	Alt Fuel Refunds (Corporate Income Tax) ^{6/}	3,300.0	0.0	Corporate
na	BSF Alt Fuel Reimbursement ^{6/}	(30,000.0)	0.0	Transfers
na	Federal Tax Bill/Withholding ^{5/}	60,000.0	0.0	Individual
	Session Total	<u>30,293.8</u>	<u>(7,000.0)</u>	
<u>44th Legislature - 7th Special Session:</u>				
1	URS Hold Harmless	(9,960.0)	4,968.4	URS ^{3/}
<u>44th Legislature - 5th Special Session:</u>				
1	Education 2000; Programs			
	Tuition Tax Credit	(97.5)	0.0	Individual
	Proposition 301 Sales Tax	^{7/}	^{7/}	
<u>44th Legislature - 2nd Regular Session:</u>				
214	Renewable Energy; Tax Incentive	(2.2)	0.0	Sales
		(57.0)	0.0	Individual
		(8.8)	0.0	Property
	Subtotal - Chapter 214	<u>(68.0)</u>	<u>0.0</u>	
239	Technology Training; Tax Credit	2,400.0	0.0	Corporate
		300.0	0.0	Individual
	Subtotal - Chapter 239	<u>2,700.0</u>	<u>0.0</u>	
252	Internal Revenue Code Conformity	2,624.0	0.0	Individual
		(26.0)	0.0	Corporate
	Subtotal - Chapter 252	<u>2,598.0</u>	<u>0.0</u>	

Table 9

Ch.	Reference Title	FY 2003	FY 2004	Revenue Category
258	Cemeteries; Property Tax Exemption Process	(7.3)	0.0	Property
372	Tourism and Sports Authority	(350.0)	0.0	Individual
		(37.8)	0.0	Sales
	Subtotal - Chapter 372	(387.8)	0.0	
384	Property Tax; Electrical Generation Facilities	(1,722.2)	0.0	Property
	Session Total	<u>3,112.7</u>	<u>0.0</u>	
	TOTAL - All Sessions	<u>(391,809.8)</u>	<u>(253,389.2)</u>	

1/ Adjustments for FY 2003 reflect estimated change from FY 2002 and FY 2004 from FY 2003.

2/ The URS hold harmless amounts for FY 2003 and FY 2004 are \$(9,960,000) and \$(4,991,600) respectively. The FY 2004 amount noted on the table of \$4,968,400 reflects the incremental difference between these amounts.

3/ The URS reduction amounts (gain to the General Fund) for FY 2003 and FY 2004 are \$5,683,900 and \$4,865,900 respectively. The FY 2004 amount noted on the table of \$(818,000) reflects the incremental difference between these amounts.

4/ The adopted FY 2003 budget included a \$50 million transfer from the BSF. This adjustment reflects a reduction of \$20 million in the amount that is available to be transferred from the BSF, plus \$5 million for a contingency for other transfer shortfalls

5/ The \$(60.0) million impact of reduced federal withholding rates included with the Federal Tax Bill are offset by an increase in state withholding rates approved by the Legislature.

6/ Alternative Fuel refunds, which are reimbursed from the Budget Stabilization Fund, were \$(66.4) million in FY 2001, and, as of June 2002, were estimated to be \$(30.0) million in FY 2002, and \$0 in FY 2003. The amounts indicated reflect the incremental net gain each fiscal year as the refunds are reduced, or \$36.0 million in FY 2002 and \$30.0 million in FY 2003.

7/ Proposition 301 sales tax increase of 0.6%. While this revenue is part of the General Fund, it is dedicated to be used exclusively for education related expenditures. Estimates for FY 2003 and FY 2004 are \$442.1 million and \$445.2 million respectively.