

## BUDGET STABILIZATION FUND

### Background and Recent Developments

The Budget Stabilization Fund (BSF) for Arizona was enacted in 1990 (A.R.S. § 35-144). The fund is administered by the State Treasurer, who is responsible for transferring General Fund money into and out of the BSF as required by law. The BSF is designed to set revenue aside during times of above-trend economic growth and to utilize this revenue during times of below-trend growth.

### The Formula

The determination of the amount to be appropriated to (deposit) or transferred out (withdrawal) of the BSF is made using a formula based upon total annual Arizona personal income (excluding transfer payments) and adjusted for inflation.

The budget recommendations of the JLBC and the Governor include estimates of the amounts to be appropriated to or transferred from the BSF. The final determination of the amount to be appropriated or transferred is made based on calculations from the Arizona Economic Estimates Commission (EEC). The EEC determines the annual growth rate of inflation-adjusted total state personal income, the trend growth rate over the past 7 years, and the calculated appropriation to or transfer from the BSF. The EEC reports this calculation for the prior calendar year by June 1. The EEC calculations however, do not result in any automatic deposits or withdrawals, as they must be authorized by legislative action.

Key features of the BSF can be summarized as follows:

- The deposit into or withdrawal from the BSF for a given fiscal year is determined by comparing the annual growth rate of inflation adjusted Arizona Personal Income (AZPI) for the calendar year ending in the fiscal year to the trend growth rate of inflation adjusted AZPI for the most recent 7 years.
- Adjusted personal income in the BSF formula is defined as total Arizona personal income less transfer payments, adjusted by the gross domestic product price deflator index.
- If the annual growth rate exceeds the trend growth rate, the excess multiplied by General Fund revenue of the prior fiscal year would equal the amount to be deposited into the BSF.
- If the annual growth rate of Arizona personal income is both less than 2% and less than the trend growth

rate, the deficiency when multiplied by the General Fund revenue of the prior year would equal the amount to be withdrawn from the BSF. This 2% floor avoids withdrawing monies from the BSF when economic conditions are slowing but there is not a recession.

- By a two-thirds majority, the Legislature, with the concurrence of the Governor, can decrease a deposit or increase a withdrawal.
- The BSF's total balance cannot be larger than 7.0% of the prior year's General Fund revenues.
- In addition to the fixed income investments available to the Treasurer, the 1998 Legislature allowed the Treasurer to invest up to 25% of the BSF in equity securities (Laws 1998, Chapter 266).

### Alternative Uses

Laws 2000, Chapter 1 as amended by Laws 2000, 7th Special Session, Chapter 1 and Laws 2001, 2nd Special Session, Chapter 3, provided for the financing of construction of a new Arizona State Hospital (ASH) by appropriating a total of \$77.5 million from the BSF over 4 years, FY 2000 through FY 2003. Chapter 1 also provides for the reimbursement of the BSF from annual receipts from the Arizona share of the master tobacco settlement agreement.

Based on the passage of Proposition 204 and an Attorney General opinion, the reimbursement to the BSF for Arizona State Hospital construction costs is the last priority in the use of funds from the master tobacco settlement agreement. The reimbursement did not occur in FY 2002, nor will it occur in FY 2003.

Laws 2000, 7th Special Session, Chapter 1 required that the refund payments for alternative fuel vehicle tax credits and Consumer Loss Recovery Fund liabilities would be funded by the Budget Stabilization Fund up to \$200 million. This amount was to be reimbursed to the BSF by the General Fund at the rate of up to \$16 million annually. After FY 2001, however, this reimbursement provision was repealed.

To date, about \$114 million has been paid from the BSF for alternative fuel costs. A total of \$130 million has been set aside for this purpose.

**Table 1**

**Budget Stabilization Fund  
FY 2000 Through FY 2004  
(\$ in Thousands)**

	Actual FY 2001	Actual FY 2002	Estimate FY 2003	Estimate FY 2004
<u>General Fund Revenues</u>				
Adjusted Revenues	\$ 6,181,782.6	\$ 6,678,329.6	\$ 6,133,474.4	\$ 5,956,514.6
Statutory Limit of Revenues	7.000%	7.000%	7.000%	7.000%
Maximum Balance	432,724.8	467,483.1	429,343.2	416,956.0
<u>Arizona Personal Income in Prior CY</u>				
Real Adjusted Annual Income Growth	7.31%	2.10%	3.13%	3.02%
7-Year Average Income Growth	6.84%	5.78%	5.24%	4.86%
Annual Difference	0.47%	-3.68%	-2.11%	-1.84%
<u>BSF Transactions</u>				
Beginning BSF Balance	407,666.3	391,523.8	64,717.2	0.0
BSF Formula Recommendation	28,013.2	0.0	0.0	0.0
Actual / Recommended Deposit	0.0	0.0	0.0	0.0
ASH Construction Fund Payments	(20,000.0)	(20,000.0)	(17,500.0)	0.0
ASH Reimbursement from Settlement Fund <sup>1/</sup>	20,000.0	0.0	0.0	0.0
Payment of Alternative Fuel Credits <sup>2/</sup>	(49,425.3)	(61,942.9)	(18,631.8)	0.0
Alternative Fuel Repayment from GF to BSF	16,000.0	0.0	0.0	0.0
BSF Transfer to GF - 12/01 Session	0.0	(119,000.0)	0.0	0.0
BSF Transfer to GF - 3/02 Session - Part 1	0.0	(47,150.0)	0.0	0.0
BSF Transfer to GF - 3/02 Session - Part 2 <sup>3/</sup>	0.0	(84,400.0)	0.0	0.0
BSF Transfer to GF - 5/02 Reg. Session <sup>4/</sup>	0.0	0.0	30,085.4	0.0
Balance	374,241.0	59,030.9	0.0	0.0
Interest Earnings & Equity Gains/Losses	17,282.8	5,686.3	1,500.0	0.0
<b>Ending BSF Balance</b>	<b>\$ 391,523.8</b>	<b>\$ 64,717.2</b>	<b>\$ 0.0</b>	<b>\$ 0.0</b>
<b>Percent of Revenues</b>	<b>6.3%</b>	<b>1.0%</b>	<b>0.0%</b>	<b>0.0%</b>

Footnotes

<sup>1/</sup> Based on the passage of Proposition 204 and an Attorney General opinion, the reimbursement to the BSF for Arizona State Hospital construction costs is the last priority in the use of Tobacco Settlement Fund. This reimbursement is currently projected to not be made in either FY 2002 or FY 2003.

<sup>2/</sup> The Alt. Fuels payout of BSF money was \$(111.4) million combined between FY 2001 and FY 2002. Through the first 4 months of FY 2003, another \$(2.4) million has been paid out. It is currently estimated that the ultimate total will be \$(130) million.

<sup>3/</sup> Since revenues fell below the budgeted total in FY 2002, the BSF will be used to make up the difference. A total of \$84.4 million was withdrawn to balance the FY 2002 budget.

<sup>4/</sup> A total of \$50 million is supposed to be transferred from the BSF into the GF in FY 2003, but there will not be enough money available in the BSF to make the full transfer. The number displayed represents an estimate of monies available to be transferred, including interest earnings.

<b>Projected Deposits/Withdrawals</b>
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Based on the projections of a slowing economy, Table 1 shows that the difference between real adjusted annual personal income growth and the 7-year average is estimated to be (2.11)% in FY 2003. While the annual number is less than the trend figure, a BSF withdrawal is not triggered by statute since personal income growth is not less than 2%. Legislation passed in the 2nd and 3rd Special Sessions, as well as in the 2nd Regular Session, notwithstanding the existing provisions of law and specified transfer amounts. As shown in Table 1, the BSF is

estimated to be able to transfer \$30 million to the General Fund in FY 2003. There will not be enough money in the fund to make the entire \$50 million transfer that was specified in Laws 2002, Chapter 327.

In FY 2004, the annual personal income growth figure is estimated to be less than the trend growth, but personal income is expected to grow by more than 2%, thus not triggering a formula withdrawal. The BSF will have no money remaining at the end of FY 2003.