

## COMPARISON OF EXECUTIVE BUDGET PROPOSAL AND JLBC BASELINE

The JLBC Book II supplements information on the FY 2008 Baseline budget in JLBC Book I. As required by A.R.S. § 41-1273, the JLBC Staff is providing information on the Executive budget proposal. Book II compares the FY 2008 JLBC Baseline and Executive budget changes to the FY 2007 budget for each state agency. This comparison also includes the line item detail for both the JLBC Baseline and Executive budget estimates. In addition, the JLBC Baseline displays the line item detail for non-appropriated funds.

### The JLBC Baseline Budget

The JLBC has already released its FY 2008 General Fund Baseline estimates (*see JLBC Book I*). This General Fund Baseline provides an estimate of the cost of statutory funding formulas and other obligations in comparison to a projection of available revenues. The Baseline does not represent a budget proposal. The FY 2008 JLBC General Fund estimates do not generally include discretionary changes in either spending and tax policy. These types of policy issues will be considered by the full Legislature during the Legislative session.

The FY 2008 JLBC General Fund Baseline spending estimate is \$10.42 billion. When compared to projected FY 2008 General Fund revenues of \$10.47 billion, the Baseline has \$45 million in net available resources.

The FY 2008 JLBC Baseline includes recommended Other Appropriated Fund spending levels for operating and capital expenditures. Unlike the General Fund Baseline, these Other Fund estimates may include discretionary changes.

Since the JLBC Baseline is not a complete budget, it is not totally comparable to the Executive proposal. The estimates, however, can be adjusted to provide an estimate of net available resources for discretionary purposes. In comparison to the \$45 million in the JLBC Baseline, the Executive budget would have \$498 million in net available resources, or \$453 million above the JLBC Baseline. This difference is due to:

- The Executive budget includes \$20 million more in General Fund Baseline revenue across FY 2007 and FY 2008. (*See General Fund Revenue section below.*)
- Compared to the JLBC Baseline, the Executive frees up \$389 million in School Facilities Board Funding (SFB), primarily by using debt rather than cash financing of new school construction.

- The Executive shifts \$89 million of Department of Public Safety (DPS) Highway Patrol funding from the General Fund to the Highway User Revenue Fund (HURF) and the State Highway Fund (SHF).
- Offsetting these gains, the Executive budget includes \$(45) million less in net revertsments (unspent appropriations) across FY 2007 and FY 2008.

### The Executive Budget Proposal

#### General Fund Revenues

Revised FY 2007 - The Executive budget proposal includes a revised FY 2007 General Fund revenue estimate of \$10.82 billion, due to higher-than-expected collections combined with a greater balance forward from FY 2006. This amount is \$(64) million lower than the revised JLBC Baseline estimate. The Executive proposal would result in 6% growth in ongoing revenues compared to the JLBC's estimated 7.1% growth without Urban Revenue Sharing. (The Executive estimates have been adjusted to display Ladewig Litigation expenses as spending for comparability with the JLBC Baseline.)

Proposed FY 2008 - The FY 2008 Executive proposal includes a General Fund revenue estimate of \$10.42 billion. This amount consists of \$10.06 billion in ongoing revenue and \$366 million in one-time revenues.

The Executive's revenue estimates reflect a 6.4% growth rate in current revenues, excluding the impact of previously enacted tax law changes and Urban Revenue Sharing. In comparison, the JLBC Baseline revenues would grow by 4.7%. The higher Executive growth rate generates \$84 million more in FY 2008 base revenues than the JLBC. Between FY 2007 and FY 2008, Executive base revenues are \$20 million higher than the JLBC Baseline.

See page S-73 for the detailed revenue category comparison.

#### General Fund Spending

Revised FY 2007 - The FY 2008 Executive budget includes a revised FY 2007 General Fund spending estimate of \$10.40 billion. In comparison, the JLBC Baseline is \$10.34 billion. There are 2 reasons for this \$64 million difference:

- While the JLBC Baseline does not include supplemental funding, the Executive is proposing \$45 million in supplementals. The adjustments include \$1.7 million for the Arizona Department of Administration, \$14

million for the Department of Corrections, \$20 million for the Department of Economic Security, and \$10 million for the Department of Education.

- In addition to the supplemental proposals, the Executive has net reversion savings that are \$19 million lower than JLBC. Reversions reflect an estimate of unspent appropriations at the end of the fiscal year. These reversion savings are expended in the following year as an administrative adjustment if a claim was submitted but not paid by the end of the fiscal year. Net reversion savings are gross reversion savings less administrative adjustments.

FY 2008 - In FY 2008, the Executive is proposing a General Fund spending level of \$10.36 billion. In comparison, the JLBC Baseline spending estimate is \$10.42 billion, which is \$60 million more than the Executive.

The JLBC Baseline has a higher spending level since it retains SFB cash financing for new school construction and does not shift DPS funding to the Highway Funds. Without these changes, the Executive budget is \$478 million higher than the JLBC Baseline. The Executive's major spending above the JLBC Baseline is as follows:

- \$90 million in the Department of Education, including teacher compensation and math/science education.
- \$87 million in the Department of Corrections, including 2,000 beds above the JLBC Baseline.
- \$70 million for the Universities, including teacher compensation and bio-medical education.
- \$44 million in the Department of Economic Security, primarily for Child Protective Services and federal funds backfill.
- \$35 million for deposit into the Arizona 21<sup>st</sup> Century Fund. This provides a second year of funding to the fund and would bring total deposits up to \$70 million.
- \$31 million in the Department of Health Services, including a federal funds backfill and for mental and public health expansions.
- \$5 million for Burke lawsuit litigation expenses.
- \$5 million for deposit into the Greater Arizona Development Authority Fund.

The Executive budget includes \$28 million in AHCCCS program funding that includes partial year funding to expand KidsCare from 200% to 300% of the Federal Poverty Level (FPL), graduate medical education expansion, and to retain funding for KidsCare Parents. However, these increases are offset by lower caseload growth projections as compared to the JLBC Baseline.

#### *Debt Financing*

The FY 2008 Executive budget includes \$1 billion in new debt financing. This is comprised of 4 different issues as follows:

- \$500 million in the Department of Transportation by increasing the financing term of highway bonds from 20 years to 30 years. The Executive also proposes to shift \$89 million in the DPS budget from the General Fund to the HURF/Highway Fund in FY 2008, which would reduce HURF/Highway Fund monies available for road construction. As a result, the net impact of the Executive budget is to provide \$411 million in additional highway construction in FY 2008.
- The Executive proposal includes funding of \$408 million in debt financing in SFB. This amount includes \$399 million for new construction, \$8 million for kindergarten space, and \$1 million for energy efficiency enhancements.
- \$79 million for new buildings in the Arizona Department of Administration building system. This will provide \$40 million for improvements to the Capitol Mall, \$32 million to rebuild the forensic unit at the Arizona State Hospital, and \$7 million for prison sewer treatment.
- \$20 million to build the Arizona State University College of Construction.

#### **Ending Balance and Ongoing Revenues and Expenditures Estimates**

After comparing the Executive's projected General Fund revenues and spending, the FY 2008 Executive budget has a \$62 million ending cash balance while the JLBC has a \$45 million cash balance.

The budget can also be viewed from the perspective of its difference in ongoing revenues and ongoing expenditures. The state can have a deficit when comparing ongoing revenues and expenditures but have a balanced cash budget through the use of one-time revenue increases and/or expenditure savings.

In the JLBC Staff calculation, ongoing revenues exclude any one-time monies, including any carry forward balance of funds from the prior year. This "balance forward" has varied widely in the last several years, from \$1 million at the beginning of FY 2003 to \$1 billion at the beginning of FY 2007.

Under the FY 2008 JLBC Baseline, ongoing spending exceeds ongoing revenues by \$(408) million, or 4.0%. Unless these one-time items unexpectedly reoccur in FY 2009, the state would need to resolve this gap in preparing the FY 2009 budget.

In comparison, the Executive is proposing a FY 2008 budget with ongoing revenues of \$10.06 billion and ongoing expenditures of \$10.42 billion. In calculating ongoing Executive spending, the JLBC Staff has labeled the following items as one-time.

- 1) \$5 million for Burke litigation costs
- 2) \$22 million for capital outlay (excluding ongoing lease-purchase payments) and

- 3) \$(88) million in savings for the shift of DPS expenses from the General Fund to the HURF/Highway Fund. In accordance with permanent law, the Executive eliminates this savings in FY 2009.

With these adjustments, the Executive's ongoing revenues fall short of ongoing spending by \$(365) million in FY 2008.

This list should not be considered as comprehensive. The Executive's FY 2008 budget has other items labeled as one-time, but they are typically a small dollar amount. In addition, the Executive may have not labeled a FY 2008 initiative as one-time, but may subsequently decide to discontinue funding in future years.

As noted above, the Executive funds \$408 million in SFB new construction with debt financing. If this item is viewed as an ongoing commitment of the General Fund, the Executive Budget's ongoing spending would exceed revenues by \$(773) million.

#### **FY 2009 and FY 2010**

The JLBC has already provided General Fund Baseline estimates through FY 2010 to assist the Legislature in evaluating the state's long-run fiscal condition (*see page 65 of the JLBC Summary Book*). These projections include estimates of both the ending cash balance as well as the difference between ongoing revenues and expenditures.

Given the multiple years involved in these calculations, long-run estimates are especially sensitive to small percent changes in revenue and spending growth. For example, a 1% change in the growth rate of either revenue or spending in FY 2008 through FY 2010 would change the ending balance calculations by almost \$600 million. As a result, the following projections are subject to considerable change.

Under the JLBC Baseline, the projected FY 2009 and FY 2010 ending balance and the difference between ongoing revenues and expenditures are a product of both Baseline revenue and spending projections for those 2 years as well as legislative decisions. The difference between ongoing revenues and expenditures ranges from a deficit of \$(519) million in FY 2009 to a deficit of \$(413) million in FY 2010.

In developing estimates of the FY 2009 and FY 2010 impacts of the Executive budget proposal, the JLBC Staff applied long-run revenue and spending growth rates to the Executive's FY 2008 budget. These are the same rates used to project the FY 2009 and FY 2010 impact of the JLBC Baseline. (*See page 65 of the Summary Book for further details on these long-term assumptions.*)

As the next step, JLBC Staff reviewed the Executive's FY 2009 biennial agency estimates and possible annualizations of FY 2008 annual budget proposals. Beyond normal caseload growth, these items appear to add \$150.7 million to spending in FY 2009 and \$203.6 million in FY 2010.

The major components of these increases are listed below:

- As noted above, the Executive does not continue to shift General Fund expenditures in DPS to the HURF/SHF in FY 2009, resulting in an additional \$89 million General Fund cost in FY 2009 and FY 2010.
- Proposed growth for biennial budget agencies in FY 2009 would add \$5 million in additional General Fund costs above FY 2008.
- The Executive proposal recommends \$408 million in debt financing to pay for SFB new construction costs in FY 2008. JLBC Staff assumes the Executive continues this proposal in FY 2009 and FY 2010. The SFB new construction debt service payments are estimated to cost \$25.8 million from the General Fund in FY 2009 and \$51.6 million in FY 2010.
- The Executive proposes to expand the KidsCare population from 200% of the FPL to 300% of the FPL. The Executive proposal provides half year funding for this initiative in FY 2008 and phases in the expansion of the current KidsCare population. According to an AHCCCS estimate, this will result in additional General Fund costs above FY 2008 of \$26.9 million in FY 2009 and \$54.0 million in FY 2010. The JLBC Staff is currently reviewing the AHCCCS methodology for these estimates.
- The Executive proposal adds 2,000 new prison beds above the JLBC Baseline. The cost to annualize these beds is estimated to be \$4 million in FY 2009 and FY 2010.

As noted earlier, the difference between ongoing revenues and expenditures in the Executive budget is projected to be a \$(365) million deficit in FY 2008. After applying the long-run growth rates, the difference between the Executive's ongoing revenues and expenditures is expected to be a \$(507) million shortfall in FY 2009 and \$(462) million shortfall in FY 2009.

The Executive budget proposal includes lease-purchase financing to construct additional space associated with full day kindergarten. Beyond \$7.9 million in FY 2008, the cost would be \$43 million in FY 2009 and \$58 million in FY 2010 according to SFB and \$49 million after FY 2010. This would increase the total new construction debt financing from \$408 million in FY 2008 to \$443 million in FY 2009 and \$466 million in FY 2010. If the SFB new construction debt financing in FY 2008–FY 2010 is factored into these calculations, the Executive budget's shortfall in ongoing funds grows from \$(773) million in FY 2008 to \$(950) million in FY 2009, and \$(920) million in FY 2010.

**STATEMENT OF GENERAL FUND REVENUES AND EXPENDITURES  
WITH ONE-TIME FINANCING SOURCES** <sup>1/</sup>

	<b>FY 2007 Executive</b>	<b>FY 2007 JLBC Baseline</b> <sup>2/</sup>	<b>FY 2008 Executive</b>	<b>FY 2008 JLBC Baseline</b>
<b>REVENUES</b>				
Ongoing Revenues	\$10,298,001,900	\$10,383,440,400	\$10,958,351,300	\$10,873,544,300
Enacted Tax Law Changes	0	0	(215,910,000)	(215,910,000)
Urban Revenue Sharing	(551,230,700)	(551,315,800)	(684,559,600)	(684,538,900)
Revised On-going Revenues	9,746,771,200	9,832,124,600	10,057,881,700	9,973,095,400
One-time Revenues				
Balance Forward	1,074,935,100	1,053,935,000	421,651,100	549,958,000
Corporate Consolidated Returns	(4,000,000)	(4,000,000)	(55,500,000)	(55,500,000)
Revised June Estimated TPT Threshold	(55,200,000)	(55,200,000)	0	0
Other Bills - Revenue	450,000	450,000	0	0
Fund Transfers	60,080,500	60,080,500	0	0
Subtotal One-time Revenues	1,076,265,600	1,055,265,500	366,151,100	494,458,000
<b>Total Revenues</b>	<b>\$10,823,036,800</b>	<b>\$10,887,390,100</b>	<b>\$10,424,032,800</b>	<b>\$10,467,553,400</b>
<b>EXPENDITURES</b>				
Operating Budget Appropriations	9,615,555,900	9,616,414,200	10,448,028,900	10,431,924,100
FY 2007 Supplementals	45,245,400	0	0	0
Maximizing Federal Fund Savings	0	(5,000,000)	0	0
Administrative Adjustments	70,000,000	79,684,300	35,000,000	74,263,000
Revertments	(90,000,000)	(114,250,800)	(60,000,000)	(125,183,100)
Subtotal Ongoing Expenditures	9,640,801,300	9,576,847,700	10,423,028,900	10,381,004,000
One-time Expenditures				
Capital Outlay	325,354,200	325,354,200	21,895,600	41,234,400
Litigation Payments	109,800,100	109,800,100	5,000,000	0
HURF/Highway Fund Shift <sup>3/</sup>	0	0	(88,266,400)	0
Pay off K-12 Rollover	191,000,000	191,000,000	0	0
Budget Stabilization Fund Deposits	9,808,600	9,808,600	0	0

	<b>FY 2007 Executive</b>	<b>FY 2007 JLBC Baseline <sup>2/</sup></b>	<b>FY 2008 Executive</b>	<b>FY 2008 JLBC Baseline</b>
Other General Fund Transfers <sup>4/</sup>	56,350,000	56,350,000	0	0
Other One-time Expenditures <sup>4/</sup>	68,271,500	68,271,500	0	0
Subtotal One-time Expenditures	760,584,400	760,584,400	(61,370,800)	41,234,400
<b>Total Expenditures</b>	\$10,401,385,700	\$10,337,432,100	\$10,361,658,100	\$10,422,238,400
<b>Ending Balance <sup>5/</sup></b>	\$421,651,100	\$549,958,000	\$62,374,700	\$45,315,000
Ongoing Revenues and Expenditures <sup>6/</sup>	\$105,969,900	\$255,276,900	(\$365,147,200)	(\$407,908,600)
Ongoing Revenues and Expenditures with SFB <sup>7/</sup>	--	--	(\$772,947,100)	--

<sup>1/</sup> Significant one-time revenues and expenditures are separately detailed so as to permit the calculation of ongoing revenue and expenditures.

<sup>2/</sup> Reflects the current status of FY 2007, including updated revenues.

<sup>3/</sup> Executive only uses the shift to HURF/Highway Fund in FY 2008.

<sup>4/</sup> Please see the Summary of One-time Operating Budget Items in the JLBC Summary for a detailed list of the individual items.

<sup>5/</sup> This calculation reflects the difference between total revenues and total expenditures.

<sup>6/</sup> This calculation reflects the difference between ongoing revenues and expenditures.

<sup>7/</sup> Calculation if SFB debt financing of \$408 million in FY 2008 is considered as an ongoing expenditure.

**STATEWIDE ISSUES**  
**JLBC Baseline - Executive Comparison**

	<b>JLBC BASELINE</b>	<b>EXECUTIVE</b>
<i>Overall Budget</i>		
Total General Fund Spending	<ul style="list-style-type: none"> <li>• \$10.42 B</li> </ul>	<ul style="list-style-type: none"> <li>• \$10.36 B</li> </ul>
FY 2007 Supplementals	<ul style="list-style-type: none"> <li>• Does not include</li> </ul>	<ul style="list-style-type: none"> <li>• \$45.2 M</li> </ul>
<i>Statewide Expenditures</i>		
State Employer Health Insurance	<ul style="list-style-type: none"> <li>• \$31.0 M for 12.8% increase in the state employer share of employee health insurance costs</li> <li>• Employee contribution would remain the same on average</li> </ul>	<ul style="list-style-type: none"> <li>• \$20.2 M for 9.8% increase in the state employer share of employee health insurance costs</li> <li>• Employee contribution would remain the same on average</li> </ul>
State Employer Retirement	<ul style="list-style-type: none"> <li>• \$5.2 M for increases in the state employer share of employee retirement costs, which consists of: <ul style="list-style-type: none"> <li>-- \$16 M for new increases as a statewide amount to be distributed at a later time</li> <li>-- \$(10.8) M in reductions for overfunded FY 07 rates which are reflected in individual agency budgets</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• \$10.0 M for increases in the state employer share of employee retirement costs <ul style="list-style-type: none"> <li>-- This is a single statewide amount reflecting both new FY 08 rates and savings from overfunded FY 07 rates</li> </ul> </li> </ul>
Statewide Employee Pay Increase	<ul style="list-style-type: none"> <li>• \$58 M for an average 2.5% state employee pay raise, beginning July 2007</li> </ul>	<ul style="list-style-type: none"> <li>• \$69.7 M GF for 3.5% pay raise. Agency budgets also include \$10.7 M in pay adjustments for specific positions</li> </ul>
Net Revertments	<ul style="list-style-type: none"> <li>• Net revertments of \$(34.6) M in FY 07 and \$(50.9) M in FY 08</li> <li>• Net revertments based on historical averages for administrative adjustments and revertments</li> </ul>	<ul style="list-style-type: none"> <li>• Net revertments of \$(20.0) M in FY 07 and \$(25.0) M in FY 08</li> </ul>
Maximize Federal Fund Savings	<ul style="list-style-type: none"> <li>• No savings in FY 08; retains \$(5.0) M savings in FY 07</li> </ul>	<ul style="list-style-type: none"> <li>• No savings in FY 08; not separately delineated from regular revertments in FY 07</li> </ul>
<i>Revenues</i>		
Baseline Growth Rate	<ul style="list-style-type: none"> <li>• 4.7% (prior to tax law changes)</li> </ul>	<ul style="list-style-type: none"> <li>• 6.4% (prior to tax law changes)</li> </ul>
<i>Other Expenditures</i>		
New Capital Facilities	<ul style="list-style-type: none"> <li>• \$41.2 M, including: <ul style="list-style-type: none"> <li>-- \$18.8 M for University Building Renewal at 26%</li> <li>-- \$7.3 M all funds (\$2.8 M GF) for ADOA Building Renewal at 26%</li> <li>-- \$8.5 M for lock and door replacement in Corrections</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• \$29.3 M, including: <ul style="list-style-type: none"> <li>-- Does not include</li> <li>-- \$19.7 M all funds (\$14.3 M GF) for ADOA Building Renewal at 72%</li> <li>-- \$5.2 M for lock and door replacements in Corrections</li> </ul> </li> </ul>

	<b>JLBC BASELINE</b>	<b>EXECUTIVE</b>
New Capital Facilities, con't.	<ul style="list-style-type: none"> <li>-- \$8.0 M to complete Archives building (previously appropriated)</li> <li>-- Does not include</li>   <li>-- Does not include</li> </ul>	<ul style="list-style-type: none"> <li>-- \$8.0 M to complete Archives building (previously appropriated)</li> <li>-- \$2.4 M for repairs at Tucson Office Complex and Juvenile Corrections' Black Canyon housing unit</li> <li>-- \$7.4 M for 3 new Certificates of Purchase for Arizona State Hospital Forensic Unit, Corrections water and sewage treatment facilities, and Capitol Mall renovations</li> </ul>
AZNet	<ul style="list-style-type: none"> <li>● \$(6.2) M to reflect one-time FY 2007 funding for AZNet</li> </ul>	<ul style="list-style-type: none"> <li>● Retains the funding</li> </ul>
Burke Settlement	<ul style="list-style-type: none"> <li>● Does not include</li> </ul>	<ul style="list-style-type: none"> <li>● \$5.0 M for plaintiffs' legal fees</li> </ul>
<b><i>Budget Stabilization Fund</i></b>		
FY 07 Deposit	<ul style="list-style-type: none"> <li>● \$10 M FY 07 General Fund deposit. In combination with interest, balance will reach 7% cap of \$685 M.</li> </ul>	<ul style="list-style-type: none"> <li>● \$10 M FY 07 General Fund deposit</li> </ul>
FY 08 Deposit	<ul style="list-style-type: none"> <li>● No deposit. Interest earnings will be sufficient to reach 7% cap of \$694 M.</li> </ul>	<ul style="list-style-type: none"> <li>● No deposit.</li> </ul>