GENERAL FUND REVENUE

FY 2014

FY 2014 General Fund Baseline revenues are projected to be $9.46 billion. As indicated in *Table 1*, the revised FY 2014 revenue estimate is $402.7 million higher than the estimate from the FY 2014 budget enacted June 2013.

Table 1

FY 2014 Revenue Forecast
($ in Millions)

Adopted FY 2014 Revenue Estimate	$9,054.4
Revised Revenue Forecast	$ 402.7
Revised FY 2014 Revenue Estimate	$9,457.1

The Baseline Revenue projection is $402.7 million higher than the original forecast due to:

- A gain of $100 million in ongoing revenues under the updated January consensus forecast, as discussed below.
- An increase of $101 million in the estimate for one-time financing sources, due primarily to the mortgage settlement litigation and several other smaller one-time sources which were not included in the original budget.
- Increased balance forward from FY 2013. The original budget assumed an ending balance of $694 million for FY 2013. The actual balance carried forward into FY 2014 was $895 million, an increase of $201 million. This increase was due to a combination of both higher than expected revenue collections and lower than expected expenditures in FY 2013.

The FY 2014 base revenue growth is based on the consensus forecasting process (*see FY 2015 section below*). "Base Revenues" reflect the underlying growth in the economy and do not include one-time adjustments, urban revenue sharing or new tax law changes. *Table 2* shows the FY 2014 base revenue growth rates for the "Big 3" General Fund revenue sources (sales tax, individual, and corporate income tax) provided by each of the components comprising the 4-sector consensus forecast.

Based on the weighted average of the components of the 4-sector consensus forecast, "Big 3" General Fund revenue would grow by 4.5% in FY 2014. After adjusting for small revenue categories, the base revenue growth rate would be 4.3%. After including tax law changes, the projected adjusted revenue growth would be 3.6%.

Table 2

FY 2014 4-Sector Forecast Percentages

	FAC	UA Low	UA Base	JLBC	Avg.
Sales	6.2%	4.4%	6.2%	6.5%	5.8%
Individual Income	6.3%	3.0%	4.7%	4.5%	4.6%
Corporate Income	(9.7)%	0.9%	1.9%	(7.0)%	(3.5)%
Weighted Average [1/]	4.9%	3.5%	5.2%	4.5%	4.5%

1/ Once adjusted for minor revenue categories, the base FY 2014 revenue increase is 4.3%.

The original FY 2014 budget assumed a revenue level of $9.05 billion, which represented base revenue growth of 4.9%. Due to a higher than expected FY 2013 collections, General Fund Revenues would need to increase by 3.1% to meet the original forecast. Relative to that projection, year-to-date results through December for the 3 major revenue categories are mixed. While sales tax revenues have grown 6.7%, individual income tax has increased 3.3%, and corporate income tax collections have decreased (14.5)%.

Based on preliminary tax collections through December, year-to-date ongoing revenues are 4.0% above the same period in FY 2013. While this growth rate includes tax law changes, this estimate is likely comparable to base revenues. Most tax law changes will affect the second half of FY 2014.

FY 2014 state revenue collections were also affected by the increase in capital gain and dividend taxes at the federal level on January 1, 2013. This change incentivized taxpayers to take capital gains and businesses to issue dividends in the 4th quarter of calendar year 2012 rather than wait until calendar year 2013 or beyond. As a result, income tax collections on these gains were accelerated into FY 2013 from FY 2014 through FY 2016. If this acceleration had not occurred, FY 2014 collections would have been higher. Rather than growing by 4.3%, base revenues would have increased 5.3%.

The individual revenue detail for FY 2014 is found in *Table 7* at the end of this section.

FY 2015

While base revenues are forecast to grow in FY 2015, one-time factors are forecast to reduce overall FY 2015 collections to $9.36 billion, or $(93.7) million below FY 2014. This net revenue loss includes:

- $477.2 million representing a 5.3% gain in base revenues under the 4-sector consensus forecast for FY 2014, as outlined below.
- $(240.3) million decrease in the balance forward from the previous fiscal year.
- $(153.6) million loss as a result of discontinuing fund transfers.
- $(47.9) million loss due to an increase in urban revenue sharing.
- $(129.1) million loss due to previously enacted legislation.

The FY 2015 Baseline estimated growth rates for the "Big 3" ongoing revenue categories were developed through a consensus process. The Baseline revenue estimate is based on averaging the results of the following 4 forecasts:

- Finance Advisory Committee panel forecast of January 2014. Consisting of 14 public and private sector economists, this independent panel meets 3 times a year to provide the Legislature with guidance on the status of the Arizona economy.
- The University of Arizona Economic and Business Research (EBR) General Fund Baseline model. The model is a simultaneous-equation model consisting of more than 100 equations that are updated on a regular basis to reflect changes in the economy. The model uses more than 200 variables related to Arizona's economy and is updated quarterly.
- EBR's conservative forecast model, and
- JLBC Staff projections.

The growth rates from each sector of the forecast are detailed in *Table 3*.

Table 3

FY 2015 4-Sector Forecast Percentages

	FAC	UA Low	UA Base	JLBC	Avg
Sales	6.1%	2.7%	6.6%	6.0%	5.4%
Individual Income	6.0%	2.3%	5.3%	6.3%	5.0%
Corporate Income	(0.4)%	0.2%	8.4%	11.9%	5.0%
Weighted Average	5.6%	2.3%	6.2%	6.6%	5.2% 1/

1/ Once adjusted for minor revenue categories, the base FY 2015 revenue increase is 5.3%.

Sales tax is expected to grow by 5.4%, and individual and corporate income tax collections are each expected to grow by 5.0%. After adjusting for small revenue categories, FY 2015 base revenues would grow by 5.3%, or in dollar terms, $477.2 million.

Risks to the Revenue Forecast

Growth in state revenue still faces uncertainty, but some of the major risks seen in past years have decreased. This improving environment is reflected in the Federal Reserve Board's (the Fed) announcement at the end of 2013 that it views the downside risk to the U.S. economy as diminishing and becoming more balanced with upside risk. Consequently, the Fed decided to lower its purchase of financial assets intended to stimulate economic activity. Bipartisan federal budget legislation passed in 2013 also partly averts the spending sequester (scheduled limits to government spending) in federal fiscal years 2014 and 2015 while reducing the chance of another government shutdown. Continued uncertainty is still reflected though in the Fed's new promise to retain the near 0% short-term interest rate if inflation remains low, regardless if the unemployment rate falls below the 6.5% threshold.

Some of the risks to the revenue forecast include:

<u>Unforeseen natural disasters and political events</u> – A U.S. invasion of Syria is a recent example of a potential event that would have had important economic consequences.

<u>International economics</u> – A fragile European economic recovery could be disrupted and negatively impact the U.S. economy if worries over sovereign debt in the region resurge.

<u>Monetary policy uncertainty</u> – Based on its economic outlook in December 2013, the Fed announced it will begin reducing its monthly purchases of U.S. Treasury bonds and mortgage-backed securities, from $85 billion to $75 billion. How they choose to time this tapering in the coming months or years, and the market's response, may have a large impact on lending and investment. If low inflation persists or economic performance slows, it is possible the Fed will choose to reverse tapering and extend its monthly purchases of financial assets.

<u>Federal fiscal policy uncertainty</u> – The federal government's current borrowing limit of $16.7 trillion may be reached in late February or early March of 2014, depending on temporary measures taken by the U.S. Treasury. Unless the debt ceiling is raised at that time, however, there would be immediate, steep reductions in government spending since the federal government will be able to spend only what it receives in revenues. Such a sharp reduction in government spending could cause the economy to contract and enter a new recession.

Apart from the possibility of another debt ceiling crisis, there is also long-run uncertainty associated with the spending sequester. While federal budget legislation passed in 2013 provides some sequester relief in federal fiscal years 2014 and 2015, it leaves intact spending caps scheduled to occur between federal fiscal years 2016 and 2021. The continued sequester would therefore limit some domestic and defense spending, which could especially affect Arizona defense contractors. Such impacts would, in turn, negatively affect the state's revenues after FY 2015; the January Consensus forecast includes revenue projections for FY 2014 through FY 2017.

Revenue Adjustments

Table 4 provides an overview of base revenue growth rates for FY 2014 and FY 2015 with budget legislation changes (which include a number of tax law changes and revenue adjustments described in more detail in *Table 6*) and one-time financing sources.

Table 4

General Fund Revenue Baseline For FY 2014 and FY 2015 ($ in Millions)

	FY 2014	%	FY 2015	%
Base Revenue	$8,969.0 [1/]	3.6%	$9,446.2	5.3%
Prior Budget Legislation	N/A		(129.1)	
Urban Revenue Sharing	(561.0)		(608.9)	
One-Time Financing				
Fund Transfers	153.6		0.0	
Balance Forward	895.5		655.2	
Adjusted Revenue	**$9,457.1**	**(1.1)%**	**$9,363.4**	**(1.0)%**

1/ The FY 2014 Base Revenue of $8.97 billion includes $(61.8) million in ongoing tax law and revenue changes. Adjusting for these changes, the FY 2014 base increase is 4.3%.

Prior Budget Legislation

Each year, statutory tax law and other revenue changes affect the state's revenue collection base. These may include tax rate or tax exemption changes, conformity to federal tax law changes, or the implementation of programs that affect revenue collections.

FY 2014

In FY 2014, ongoing budget legislation is expected to reduce General Fund revenues by $(61.8) million. *Table 5* provides a summary of previously enacted budget legislation changes with ongoing revenue impacts in FY 2014. As noted above, the FY 2014 base revenue growth of 4.3% excludes these changes.

Pre-2013 Tax Law Changes

In addition to the tax law and revenue changes enacted during the 2013 legislative session, the following changes (as described below) were enacted in prior sessions and will have an impact on FY 2014 revenue collections.

1) Job Tax Credit – Laws 2011, 2nd Special Session, Chapter 1 provides a $3,000 annual individual and corporate income tax credit for each net new qualifying job added by an employer in the state. To qualify for the 3-year credit, the new employment position must: (1) be full-time, (2) pay at least the county median wage, and (3) include health insurance paid by the employer. In addition, a business cannot claim the credit unless it meets certain minimum job creation and capital investment requirements. Laws 2012, Chapter 343 removed the 400 maximum job tax credit claims per employer established by Chapter 1. The job tax credit was originally estimated to reduce revenues by $(18.2) million in FY 2014. Based on actual credit data, however, the FY 2014 estimate has since been revised to $(4.0) million. *(For the revenue impact after FY 2014, see page 430.)*

Table 5

FY 2014 Budget Legislation Changes With Ongoing Revenue Impact ($ in Millions)

Pre-2013 Tax Law Changes (Year Enacted)	
1) Job Tax Credit (2011)	$ (4.0)
2) Corporate Sales Factor Change for Service Providers (2012)	0.0
3) Reduction of Long-Term Capital Gains (2012)	(10.2)
4) Income Tax Deduction for Federal Bonus Depreciation (2012)	0.0
5) Qualified Facility Credit (2012)	(4.0)
Subtotal	$ (18.2)
2013 Tax Law and Revenue Changes	
6) Prior FBLS Fee Increase	$ 0.3
7) IRS Conformity	9.1
8) Data Center TPT Exemption	(4.2)
9) Foster Care Credit	(0.9)
10) Interlock Device TPT Exemption	(0.6)
11) Increased 529 College Savings Plan Deductions	(4.0)
12) Expanding Working Poor Credit to Include Non-Itemizers	(18.0)
13) Exempts EZ Credit Certification Requirement	(0.5)
14) Business Expensing	(24.8)
Subtotal	$ (43.6)
Total – FY 2014 Revenue Impact	**$ (61.8)**

2) Corporate Sales Factor for Service Providers – Laws 2012, Chapter 2 allows multi-state service-providing companies to reduce their Arizona corporate income tax liability through a change in the calculation of the sales factor. To be eligible for the change, a company is required to derive at least 85% of its sales of services from out-of-state customers. The change in the calculation of the sales factor is phased in over 4 years, beginning in TY 2014. This provision was originally estimated to reduce corporate income tax collections by $(3.0) million in FY 2014. As a result of further review of the legislation, however, it has since been determined that the first-year impact will not occur until FY 2015. For this reason, the revised FY 2014 estimate shows no impact. *(For the revenue impact after FY 2014, see page 430.)*

3) <u>Reduction of Long Term Capital Gains</u> – Laws 2012, Chapter 343 reduces the individual income taxation of long term capital gains on assets acquired after TY 2011 by 25% over 3 years, beginning in TY 2013. This provision was initially estimated to reduce individual income tax collections by $(17.5) million in FY 2014. However, as a result of updated capital gains data, the estimated revenue reduction in FY 2014 has since been revised to $(10.2) million. *(For the revenue impact after FY 2014, see page 430.)*

4) <u>Income Tax Deduction for Federal Bonus Depreciation</u> – Laws 2012, Chapter 343 allows an Arizona individual income tax deduction equal to 10% of the bonus depreciation claimed on federal tax returns for assets placed in service after 2013. This provision was originally estimated to result in a one-time individual income tax loss of $(4.2) million in FY 2014. However, as a result of further review of this provision, it has since been determined that the fiscal impact will not occur until FY 2015. In addition, the impact is labeled as ongoing rather than one-time. Although the 50% federal bonus depreciation provision under the American Taxpayer Relief Act of 2012 expired on December 31, 2013, past actions by the U.S. Congress suggest that it is reasonable to assume that this provision may be extended retroactively (from January 1, 2014) in the early part of calendar year 2014. Finally, as a result of updated estimates by the federal Joint Committee of Taxation, the revenue reduction of this individual income tax provision has been revised to $(1.8) million, beginning in FY 2015. *(This is shown in Table 6 on page 430.)*

5) <u>Qualified Facility Tax Credit</u> – Laws 2012, Chapter 343 created a new individual and corporate income tax credit for businesses that expand or locate qualified facilities in the state, beginning in TY 2013. The credit is 10% of the lesser of (1) the capital investment in the facility or (2) $200,000 for each net new employee hired at the facility. To qualify for the credit, a company is required to devote at least 80% of its property and payroll at the facility to manufacturing, research, or a national or regional headquarter. There are also certain minimum requirements with respect to wage and health insurance coverage for new employees at the facility. The credit is refundable but no single taxpayer can claim more than $30 million per calendar year. The credit must be taken in equal installments over 5 years. The qualified facility credit is subject to an annual aggregate cap of $70 million, which it shares with the renewable energy credit enacted in 2009. This provision is estimated to reduce revenues by $(4.0) million in FY 2014. *(For the revenue impact after FY 2014, see page 430.)*

<u>2013 Tax Law Changes</u>

In the 2013 Session, the Legislature enacted the following ongoing tax law and revenue changes.

6) <u>Prior FBLS Fee Increase</u> – A.R.S. § 41-2144 and § 41-2146 authorize the Department of Fire, Building, and Life Safety (FBLS) to establish fees to support the State Fire Marshal and manufactured housing programs. A 2011 Auditor General performance audit found that the non-appropriated Mobile Home Relocation Fund was being charged more than its proportionate share to support the agency's operating budget. To reduce the Relocation Fund's share of administrative costs, the State Fire Marshal and manufactured housing programs raised fees in FY 2013. The Board of Manufactured Housing increased fees effective July 2012, and the State Fire Safety Committee increased fees effective September 2012. In total, ongoing revenue gain in FY 2014, the first full year that the fees are in effect, is estimated to be $270,000. These fees, however, are deposited into the General Fund. The department's budget includes an increase of $270,000 from the General Fund in FY 2014 for operation of the State Fire Marshal and manufactured housing programs. The increased appropriation is equivalent to the level of increased fees.

7) <u>Internal Revenue Code Conformity</u> – Laws 2013, Chapter 65 conforms Arizona tax statutes to the Internal Revenue Code (IRC) as of January 3, 2013 and establishes a tax credit for Tax Year 2013 in lieu of conforming to the retroactive provision of the Federal Aviation Administration (FAA) Modernization and Reform Act relating to rollover of amounts received in airline carrier bankruptcy. Chapter 65 is estimated to result in a revenue increase of $9.1 million in FY 2014 over and above the revenue gain of $4.6 million in FY 2013.

8) <u>Data Center TPT Exemption</u> – Laws 2013, 1st Special Session, Chapter 9 provides, effective September 1, 2013, Transaction Privilege Tax (TPT) and Use Tax exemptions, for equipment purchased by owners, operators, or co-location tenants of computer data centers certified by the Arizona Commerce Authority (ACA). To qualify for the exemption, newly constructed data centers located in Maricopa and Pima Counties must make a minimum investment of $50 million over 5 years. The corresponding minimum requirement in other counties is $25 million. Existing data centers, which made an investment of at least $250 million during the 6 years immediately preceding the act's effective date, are eligible for the same exemption with respect to future equipment purchases. The exemptions are expected to reduce General Fund revenues by $(4.2) million in FY 2014. *(For the revenue impact after FY 2014, see page 430.)*

9) <u>Foster Care Tax Credit</u> – Laws 2013, 1st Special Session, Chapter 9 expands (retroactive to January 1, 2013) the existing working poor credit to include qualifying foster care charitable organizations. The maximum credit for cash contributions to qualifying foster care organizations is $400 for individuals filing as single or head of household and $800 for married couples filing joint returns. The foster care credit is estimated to result in

an annual individual income tax reduction of $(850,000), beginning in FY 2014.

10) Interlock Device TPT Exemption – Laws 2013, Chapter 236 exempts the leasing or renting of certified interlock devices from state and municipal TPT, retroactive to September 1, 2004. This provision is estimated to result in an annual General Fund revenue reduction of $(600,000), beginning in FY 2014.

11) Increased 529 College Savings Plan Deductions – Laws 2013, Chapter 236 increases the 529 college savings plan contributions that are deductible from state income tax from $1,500 to $4,000 for married couples filing joint returns and from $750 to $2,000 for all other filers. This provision, which is retroactive to January 1, 2013, is expected to result in an annual individual income tax reduction of $(4.0) million, beginning in FY 2014.

12) Expanding Working Poor Credit to Non-Itemizers – Laws 2013, Chapter 236 removes the requirement that an individual income tax filer itemizes deductions in order to claim the working poor tax credit. This provision is estimated to reduce individual income tax collections by $(18.0) million annually, beginning in FY 2014.

13) Exempts Enterprise Zone Credit Certification Requirement – Laws 2013, Chapter 236 provides that businesses, which were certified by ACA and then claimed first year credits under the now repealed Enterprise Zone (EZ) Credit program, be exempt from the requirement to file for certification in order to claim second or third year credits. This provision, which is retroactive to July 1, 2011, is estimated to reduce General Fund revenues by $(500,000) in FY 2014. *(For the revenue impact after FY 2014, see page 430.)*

14) Business Expensing – Laws 2013, Chapter 256 removes the $25,000 cap on deductions from state income tax for qualified business equipment purchases under Section 179 of the Internal Revenue Code (IRC). Section 179 allows individual and corporate taxpayers to deduct, for income tax purposes, 100% of their qualified equipment purchases (up to a certain amount, which is $500,000 in TY 2013) in the year that the equipment was purchased rather than in smaller installments over several years according to a federal depreciation schedule. The $25,000 deduction cap was instituted in the state in 2004 as a result of the Legislature's decision (Laws 2004, Chapter 196) not to conform to the higher Section 179 deduction allowances provided under the federal Jobs and Growth Tax Relief Reconciliation Act of 2003. Chapter 256 effectively conforms state tax statutes to Section 179 of IRC for qualified equipment acquired in taxable years beginning after December 31, 2012. Under the American Taxpayer Relief Act of 2012, a business is allowed to fully expense (deduct for income tax purposes) the first $500,000 of qualified equipment purchases. This provision, however, expired December 31, 2013. For this reason, Chapter 256 was initially estimated to result in a one-time revenue loss of $(24.8) million in FY 2014. Since the U.S. Congress has retroactively extended expired provisions several times in the past, however, the Baseline now assumes that the federal $500,000 business expensing allowance will be ongoing rather than one-time. Under this revised assumption, income taxes will be reduced by $(24.8) million annually, beginning in FY 2014.

FY 2015 – FY 2017

In recent years, the Legislature has enacted a number of tax provisions with delayed effective dates. In some cases, there can be a 2- to 3-year period of time between the initial estimates developed by the JLBC Staff and the subsequent implementation of the provision. The JLBC Staff's general approach is to revisit the original estimate as the provision is about to be implemented. Any such revision, however, depends on the availability of new data. Thus, no revision has been made unless new data has been released since the original estimate of the provision was prepared. *Table 6* below compares the initial and revised revenue estimates of some of these provisions.

In FY 2015, General Fund revenue estimates have been adjusted downward by $(129.1) million relative to FY 2014 to reflect the start of a previously enacted tax law change or its ongoing phase-in. The FY 2016 estimates have been further adjusted downward by $(115.6) million relative to FY 2015 for additional phase-ins. In FY 2017, the Baseline revenues were reduced by another $(108.7) million relative to FY 2016 as the phase in continues. In total, the previously enacted tax law changes will reduce Baseline revenues by $(353.4) million compared to FY 2014.

As noted above, *Table 6* lists prior year tax law changes with ongoing revenue impact in FY 2015 through FY 2017 under both prior and current scoring. Below follows a description of each of the provisions included in *Table 6*.

15) Elimination of Small Business Capital Gains – Laws 2011, 2nd Special Session, Chapter 1 eliminates capital gains on income derived from small businesses certified by the Arizona Commerce Authority to receive credit-eligible angel investments, beginning in TY 2014. This provision was originally estimated to reduce individual income tax collections by $(11.6) million in FY 2015. However, as a result of updated capital gains data, the estimated revenue reduction in FY 2015 has now been revised to $(8.6) million. The FY 2016 estimate (relative to FY 2015) has been revised from $(0.7) million to $(0.4) million and the FY 2017 estimate (relative to FY 2016) has been revised from $(0.6) million to $(0.8) million.

Table 6

Prior Year Budget Legislation with Ongoing Revenue Impact in FY 2015 through FY 2017
($ Millions) [1/]

Bill/Description of Provision	Prior Estimates FY 15	Prior Estimates FY 16	Prior Estimates FY 17	Current Estimates FY 15	Current Estimates FY 16	Current Estimates FY 17
Laws 2011, 2nd SS, Ch. 1						
15) Eliminates capital gains on income derived from small businesses.	$(11.6)	$(0.7)	$(0.6)	$(8.6)	$(0.4)	$(0.8)
16) Phases down corporate tax rate from 6.968% to 4.9% over 4 years.	(53.8)	(62.2)	(67.5)	(50.4)	(60.7)	(61.7)
17) Phases in corporate sales factor from 80% to 100% over 4 years.	(24.6)	(22.7)	(20.5)	(39.3)	(37.9)	(31.7)
18) Creates a $3,000 new job tax credit claimed annually for 3 years. [2/]	(19.7)	(6.8)	(1.0)	(4.2)	(4.2)	(3.1)
19) Increases small business eligibility for 30% “angel” investment tax credit from $2 million to $10 million in assets through FY 2016.	(0.5)	4.5	0.0	(0.5)	4.5	0.0
Laws 2012, Ch. 2						
20) Provides a change in the calculation of the corporate sales factor for service companies. [3/]	(0.5)	(0.4)	(0.5)	(3.0)	(0.5)	(0.4)
Laws 2012, Ch. 343						
21) Phases in (over 3 years) a 25% reduction of long term capital gains on assets purchased after 2011. [4/]	(23.0)	(16.0)	(4.9)	(15.7)	(12.1)	(7.0)
22) Provides income tax deduction equal to 10% of federal bonus depreciation for assets placed in service in 2012. [5/]	4.2	0.0	0.0	(1.8)	0.0	0.0
23) Creates an income tax credit for capital investments in new/expanded manufacturing/ research facilities and commercial headquarters.	(4.0)	(4.0)	(4.0)	(4.0)	(4.0)	(4.0)
Laws 2013, Ch. 236						
24) Exempts certain Enterprise Zone income tax credit certification requirements.	0.2	0.3	0.0	0.2	0.3	0.0
Laws 2013, Ch. 255						
25) Exempts trade/service contractors from prime contracting tax. Instead, materials taxed as retail.	0.0	1.3	0.0	0.0	1.3	0.0
Laws 2013, Ch. 256						
26) Conforms state tax statutes to Section 179 (business expensing or “instant depreciation” provision) of the federal Internal Revenue Code. [6/]	24.8	0.0	0.0	0.0	0.0	0.0
Laws 2013, 1st SS, Ch. 9						
27) Exempts data center equipment from TPT. [4/]	(1.8)	(1.9)	0.0	(1.8)	(1.9)	0.0
Revenue Impact Over Prior Year	**$(110.3)**	**$(108.6)**	**$(99.0)**	**$(129.1)**	**$(115.6)**	**$(108.7)**

1/ Represents marginal pricing: All impacts are stated relative to the prior year. *See Table 5 for first 14 tax law changes*. Impact excludes property tax changes, which affect Department of Education spending rather than General Fund Revenues.

2/ Includes impact of Laws 2012, Chapter 343 provision, which eliminated individual company cap of 400 eligible employees. Impact of Chapter 343 began in FY 2014.

Table 6 Continued

3/ Original estimate assumed that the first-year impact would occur in FY 2014. Based on subsequent examination of the provision, however, it has been determined that the first-year impact will not occur until FY 2015.

4/ Impact began in FY 2014.

5/ Original estimate assumed a one-time loss of $(4.2) million in FY 2014. Based on subsequent examination of the provision, however, it has been determined that the first-year impact will not occur until FY 2015. Additionally, based on recent estimates by the federal Joint Committee of Taxation, the first-year impact has been reduced to $(1.8) million. Revised estimate assumes that federal bonus depreciation will be extended.

6/ Original estimate assumed that this provision would result in a one-time revenue loss of $(24.8) million in FY 2014. Revised estimate assumes that the federal Section 179 business expensing provision will be extended.

16) Phase-Down of Corporate Income Tax Rate – Laws 2011, 2nd Special Session, Chapter 1 reduces the corporate income tax rate from 6.968% to 4.9% over 4 years, beginning in TY 2014. This rate reduction was originally estimated to reduce corporate income tax collections by $(53.8) million in FY 2015. However, based on an updated forecast for corporate income tax, this estimate has been revised to $(50.4) million. The FY 2016 estimate (relative to FY 2015) has been revised from $(62.2) million to $(60.7) million and the FY 2017 estimate (relative to FY 2016) has been revised from $(67.5) million to $(61.7) million.

17) Phase-In of Single Corporate Sales Factor – Laws 2011, 2nd Special Session, Chapter 1 increases the optional sales factor, which is used to calculate the apportionment of taxable income for multi-state corporations, from 80% to 100% over 4 years, beginning in TY 2014. This provision was originally estimated to reduce corporate income tax collections by $(24.6) million in FY 2015. However, based on newer information provided by the Department of Revenue, this estimate has now been revised to $(39.3) million. The FY 2016 estimate (relative to FY 2015) has been revised from $(22.7) million to $(37.9) million and the FY 2017 estimate (relative to FY 2016) has been revised from $(20.5) million to $(31.7) million.

18) Job Tax Credit – Laws 2011, 2nd Special Session, Chapter 1. *For a detailed description of this provision, see 1) on page 427*. The job tax credit was originally estimated to reduce corporate and individual income tax collections by $(19.7) million in FY 2015 relative to FY 2014. However, based on actual credit usage to date, the FY 2015 estimate has now been revised to $(4.2) million. The FY 2016 estimate (relative to FY 2015) has been revised from $(6.8) million to $(4.2) million and the FY 2017 estimate (relative to FY 2016) has been revised from $(1.0) million to $(3.1) million.

19) Expansion of Small Business Eligibility for Angel Investment Credit – Laws 2011, 2nd Special Session, Chapter 1 provided certain changes to the state's angel investment tax credit program, beginning in FY 2012. Under this program, qualified "angel" investors are eligible to receive up to a 35% credit over 3 years on investments in small businesses certified by ACA. The credit program is capped at $20 million. Chapter 1 extended ACA's credit authorization by 4 years, through the end of FY 2016. Additionally, Chapter 1 also increased the asset cap of small businesses qualified to receive credit-eligible angel investments from $2 million to $10 million, beginning in FY 2012. This provision is estimated to reduce individual income tax revenue by $(0.5) million in FY 2015, after which time the $20 million in allowable credit authorization is assumed to be exhausted. The original estimate of this provision has not been revised.

20) Corporate Sales Factor for Service Providers – Laws 2012, Chapter 2. *For a detailed description of this provision, see 2) on page 427*. This tax law change was originally estimated to reduce corporate income tax collections by $(3.0) million in FY 2014. In addition, it was estimated to further reduce revenue by $(0.5) million in FY 2015 relative to FY 2014, $(0.4) million in FY 2016 relative to FY 2015, and $(0.5) million in FY 2017 relative to FY 2016. However, as discussed on page 427, under the revised estimate, the first-year impact of $(3.0) million is shifted from FY 2014 to FY 2015. The timing of the estimates after FY 2015, for scoring purposes, has been adjusted accordingly.

21) Reduction of Long Term Capital Gains – Laws 2012, Chapter 343. *For a detailed description of this provision, see 3) on page 428*. The reduction of long term capital gains subject to individual income taxes was originally estimated to reduce tax revenues by $(23.0) million in FY 2015 relative to FY 2014. As a result of updated capital gains data, however, the FY 2015 estimate has now been revised to $(15.7) million. The FY 2016 estimate (relative to FY 2015) has been revised from $(16.0) million to $(12.1) million and the FY 2017 estimate (relative to FY 2016) has been revised from $(4.9) million to $(7.0) million.

22) Income Tax Deduction for Federal Bonus Depreciation – Laws 2012, Chapter 343. *For a detailed description of this provision, see 4) on page 428*. This provision was originally estimated to result in a one-time individual income tax loss of $(4.2) million in FY 2014. However, as discussed on page 428, the revised estimate assumes that the fiscal impact will not occur until FY 2015. Moreover, as a result of newer federal data, the FY 2015 estimate has been reduced from $(4.2) million to

$(1.8) million. In addition, the impact is labeled as ongoing rather than one-time.

23) Qualified Facility Credit – Laws 2012, Chapter 343. *For a detailed description of this provision, see 5) on page 428*. This credit is estimated to reduce individual and corporate income tax collections by $(4.0) million over and above the reduction in the prior year in each year from FY 2015 through FY 2017. The original estimate of this provision has not been revised.

24) Exempts Enterprise Zone Credit Certification Requirement – Laws 2013, Chapter 236. *For a detailed description of this provision, see 13) on page 429*. This provision was originally estimated to reduce corporate income tax collections by $(500,000) in FY 2014 and $(300,000) in FY 2015. Thus, relative to the FY 2014 base, this provision results in a savings of $200,000 in FY 2015. The FY 2016 savings relative to the FY 2015 base is $300,000. The original estimate of this provision has not been revised.

25) TPT Simplification – Laws 2013, Chapter 255 makes numerous changes to the state and municipal TPT with respect to administration, collections, and auditing. In addition, effective from January 1, 2015, Chapter 255 exempts service and trade contractors from state and municipal contracting tax whenever they work directly for the property owners and such work is limited to maintenance, repair, or replacement of existing property. Instead, the materials purchased by such contractors will be subject to retail TPT. The changes under Chapter 255 are estimated to result in a TPT net increase of $1.3 million, beginning in FY 2016. The original estimate of this provision has not been revised.

26) Business Expensing – Laws 2013, Chapter 256. *For a detailed description of this provision, see 14) on page 429*. This provision was originally estimated to result in a one-time income tax revenue loss of $(24.8) million in FY 2014. Thus, under the original estimate, the General Fund would have incurred FY 2015 savings of $24.8 million relative to the FY 2014 base. For reasons discussed on page 429, however, the revised estimate assumes that the business expensing provision (and its associated fiscal impact) is ongoing rather than one-time.

27) Data Center TPT Exemption – Laws 2013, 1st Special Session, Chapter 9. *For a detailed description of this provision, see 8) on page 428*. This exemption is estimated to reduce TPT collections by $(1.8) million in FY 2015 (relative to FY 2014) and $(1.9) million in FY 2016 (relative to FY 2015). The original estimate of this provision has not been revised.

Temporary 1-Cent TPT Increase

At the May 2010 Special Election, voters approved a 1-cent increase of the TPT (more commonly referred to as sales tax) for 3 years, effective from June 1, 2010 through May 31, 2013. As shown in *Table 7*, the 1-cent sales tax generated additional General Fund revenues of $962.2 million in FY 2013, the third and final year of the temporary tax. The May 31, 2013 expiration of the 1-cent sales tax has the effect of reducing FY 2014 General Fund revenues by $(962.2) million relative to FY 2013.

Urban Revenue Sharing

The Urban Revenue Sharing (URS) program provides that a percentage of state income tax revenues (including both individual and corporate income tax) be shared with incorporated cities and town within the state. The amount that is currently distributed to cities and towns is 15% of net income tax collections from 2 years prior. As indicated in *Table 7*, total URS distributions will increase from $561.0 million in FY 2014 to $608.9 million in FY 2015. This URS increase results in a FY 2015 General Fund revenue loss of $(47.9) million relative to FY 2014.

One-Time Financing

As shown in *Table 7*, one-time financing sources are included in the budget for FY 2014 and FY 2015. The following is a discussion of these one-time financing sources.

FY 2014

The $1,049.1 million in one-time financing sources for FY 2014 includes:

Fund Transfers – The enacted FY 2014 budget provides for a total of $76.9 million in fund transfers. This amount includes:

- $6.0 million of the second year of Judiciary transfers.
- $68.0 million from the State Employee Health Insurance Trust Fund.
- $10.0 million from the Department of Education's Structured English Immersion Fund and
- $(7.1) million of General Fund monies transferred to the Automation Projects Fund.

Under the FY 2015 Baseline, this FY 2014 amount has been adjusted to $153.6 million. The $76.7 million increase in fund transfers under the Baseline is due to:

- Proceeds of $50.0 million from the National Mortgage Settlement. The FY 2013 General Appropriation Act required the Attorney General to distribute $50.0 million from the National Mortgage Settlement proceeds to the General Fund. These monies were placed on hold in FY 2013, however, due to ongoing litigation. The court case, which was finally resolved in September 2013, resulted in the transfer of $50.0 million from the Attorney General to the General Fund in October 2013.
- "Reconciliation payments" of $19.2 million from AHCCCS health care plans, which occur when the plans' profits exceed the statutory limit of 3%.

- Unbudgeted savings of $7.5 million related to unexpended proceeds of several state building lease-purchase agreements.

Balance Forward – The FY 2013 General Fund ending balance carried forward into FY 2014 was $895.5 million.

FY 2015

The $655.2 million in one-time financing sources for FY 2015 includes:

Balance Forward – The FY 2014 General Fund ending balance carried forward into FY 2015 is estimated to be $655.2 million. Compared to the $895.5 million FY 2014 beginning balance, the projected FY 2015 balance reflects a loss of $(240.3) million.

Fund Transfers - The FY 2015 Baseline does not continue the FY 2014 fund transfers.

Table 7

GENERAL FUND REVENUE - FY 2013-FY 2015

FORECAST REVENUE GROWTH

($ in Thousands)

	ACTUAL FY 2013	% CHANGE PRIOR YR	FORECAST FY 2014	% CHANGE PRIOR YR	$ CHANGE PRIOR YR	FORECAST FY 2015	% CHANGE PRIOR YR	$ CHANGE PRIOR YR
Sales and Use	3,778,863.7	3.5%	3,993,710.2	5.7%	214,846.5	4,207,622.7	5.4%	213,912.5
Income - Individual	3,397,545.1	10.1%	3,501,381.6	3.1%	103,836.5	3,675,771.0	5.0%	174,389.4
- Corporate	662,026.4	2.8%	634,979.6	-4.1%	(27,046.8)	666,946.1	5.0%	31,966.5
Property	13,202.5	-16.9%	16,000.0	21.2%	2,797.5	16,000.0	0.0%	0.0
Luxury - Tobacco	24,530.4	-1.6%	24,765.2	1.0%	234.8	24,300.2	-1.9%	(465.0)
- Liquor	31,654.2	0.7%	32,434.7	2.5%	780.5	33,234.4	2.5%	799.7
Insurance Premium	386,776.1	-1.8%	400,000.0	3.4%	13,223.9	438,681.0	9.7%	38,681.0
Other Taxes	1,567.3	-12.1%	1,600.0	2.1%	32.7	1,625.0	1.6%	25.0
Sub-Total - Taxes	8,296,165.8	5.7%	8,604,871.3	3.7%	308,705.5	9,064,180.3	5.3%	459,309.0
Other Non-Tax Revenues:								
Lottery	79,260.8	-3.3%	77,548.0	-2.2%	(1,712.8)	87,577.4	12.9%	10,029.4
Licenses, Fees and Permits	29,421.2	5.5%	30,570.0	3.9%	1,148.8	31,487.1	3.0%	917.1
Interest	12,019.0	18.1%	10,000.0	-16.8%	(2,019.0)	10,000.0	0.0%	0.0
Sales and Services	36,894.3	3.3%	38,000.0	3.0%	1,105.7	39,140.0	3.0%	1,140.0
Other Miscellaneous	94,387.8	7.3%	100,000.0	5.9%	5,612.2	104,000.0	4.0%	4,000.0
Transfers and Reimbursements	31,079.2	32.4%	32,000.0	3.0%	920.8	32,960.0	3.0%	960.0
Disproportionate Share Revenue	78,204.6	-18.3%	76,020.7	-2.8%	(2,183.9)	76,821.9	1.1%	801.2
Sub-Total - Other Non-Tax	361,266.9	-0.4%	364,138.7	0.8%	2,871.8	381,986.4	4.9%	17,847.7
Subtotal On-Going Revenue	**8,657,432.7**	**5.4%** [1/]	**8,969,009.9**	**3.6%** [2/]	**311,577.3**	**9,446,166.7**	**5.3%**	**477,156.8**
Previously Enacted Tax Law Changes	0.0	N/A	0.0	N/A	0.0	(129,100.0)	N/A	(129,100.0)
Budget Legislation	0.0	N/A	0.0	N/A	0.0	0.0	N/A	0.0
3-Year 1¢ TPT Increase	962,172.0	5.1%	0.0	-100.0%	(962,172.0)	0.0	N/A	0.0
Subtotal w/Tax Law Changes	**9,619,604.7**	**5.4%**	**8,969,009.9**	**-6.8%**	**(650,594.7)**	**9,317,066.7**	**3.9%**	**348,056.8**
Urban Revenue Sharing (URS)	(513,584.0)	21.0%	(561,001.2)	9.2%	(47,417.2)	(608,935.7)	8.5%	(47,934.5)
Subtotal w/Tax Law Changes/URS	**9,106,020.7**	**4.6%**	**8,408,008.7**	**-7.7%**	**(698,011.9)**	**8,708,131.0**	**3.6%**	**300,122.3**
One-Time Financing Sources:								
Fund Transfers	46,000.0	-85.0%	153,591.6	233.9%	107,591.6	0.0	-100.0%	(153,591.6)
DEQ Settlement	10,500.0	N/A	0.0	-100.0%	(10,500.0)	0.0	N/A	0.0
Sub-Total - One-Time Financing Sources	56,500.0	-84.3%	153,591.6	171.8%	97,091.6	0.0	-100.0%	(153,591.6)
Subtotal - Revenues	**9,162,520.7**	**1.1%**	**8,561,600.3**	**-6.6%**	**(600,920.3)**	**8,708,131.0**	**1.7%**	**146,530.7**
Balance Forward	396,960.0	12140.5%	**895,475.0**	N/A	498,515.0	**655,224.9**	-26.8%	(240,250.1)
Total - Resources	**9,559,480.7**	**5.4%**	**9,457,075.3**	**-1.1%**	**(102,405.3)**	**9,363,355.9**	**-1.0%**	**(93,719.4)**

1/ The 5.4% FY 2013 increase includes $(85.3) million in tax law and other revenue changes. Adjusting for these changes, base FY 2013 revenue growth was 6.4%.
2/ The 3.6% FY 2014 increase includes $(61.8) million in tax law and other revenue changes. Adjusting for these changes, base FY 2014 revenue growth is 4.3%.