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“Year-to-date, base General Fund revenues are 3.4% above the prior year, and are \$31.9 million above the Baseline forecast.”

This report has been prepared for the Arizona Legislature by the Joint Legislative Budget Committee Staff on March 21, 2016.

Summary

February 2016 General Fund collections of \$398.1 million were 11.7% above the prior year, and were \$38.4 million above the Baseline forecast.

Individual income tax was \$44.2 million above forecast in February, while all other tax categories were \$(5.8) million below forecast. While strong withholding growth of 8.8% contributed \$12.0 million of the forecast overage, the primary driver was a \$27.4 million gain from lower-than-expected refunds.

In the middle of tax filing season, however, it is difficult to draw any conclusions from the refund data. The refund gain may simply be due to the timing of tax return processing. For example, refund processing started in late January this year, while last year it did not begin until February. As a result, the lower level of February 2016 refunds may reflect spreading the returns over 2 months.

Transaction Privilege Tax (TPT) collections were 3.9% above February 2015, but were \$(4.9) million below forecast. The February data also provides us with the first opportunity in a year to review the subcategory Sales Tax detail on an “apples to apples” basis.

During the last 12 months, year-over-year retail and contracting subcategory growth rates have been misleading due to the implementation of the TPT simplification legislation in January 2015. That legislation essentially shifted a portion of TPT collections out of contracting and into retail, so the growth rates of these two subcategories have not been representative of economic activity over the past 12 months.

The year-to-date data demonstrates this point. Retail has grown 7.8% since July, but only 3.7% in February. That result is not surprising since the first half FY 2016 retail returns were boosted by the shift from contracting. February may then reflect a more normal level of activity.

In the opposite direction, year-to-date contracting sales are down (16.4)% as some of those transactions shifted to the retail subcategory. In February, contracting was still down (7.6)%. That result was surprising, however, since contracting activity was thought to be on the upswing. For example, construction employment has increased 5.4% in the last year. The contracting results bear watching in future months to see if this seemingly contradictory trend continues.

Year-to-date, base General Fund revenues are 3.4% above the prior year, and are \$31.9 million above the Baseline forecast.

In comparison to revenue collections of \$398.1 million, February 2016 spending was \$510.6 million, which is a decrease of \$(37.0) million from the prior year.

Fiscal year-to-date, General Fund revenues of \$5.79 billion have been offset by \$6.89 billion of expenditures.

The state's fiscal health can also be measured by the operating fund balance. The state pays its bills out of the operating fund balance, which consists of the General Fund and certain dedicated funds. The operating balance as of mid-March 2016 is \$1.9 billion. In addition, the state's Budget Stabilization Fund has a balance of \$460.0 million.

Table of Contents

Summary	
February Revenues	2
Monthly Indicators	4
JLBC Meeting	7
Summary of Recent Agency Reports	
• AHCCCS – Hospital Assessment Report.....	7
• AHCCCS – Interstate Agreement.....	7
• ADC – IT System Replacement Report	7
• DHS – Arnold v. Sarn Report	8
February Spending	9
Tracking Arizona's Recovery	Appendix A

February Revenues

	<u>FY 2016 Collections</u>	<u>Difference From Budget Forecast</u>	<u>Difference From FY 2015</u>
February	\$ 398.1	\$ 38.4	\$ 41.8
Year-to-Date	\$ 5,788.3	\$ 31.9	\$ 217.3

Sales Tax collections of \$337.9 million were 3.9% above February of last year but \$(4.9) million below forecast for the month. Year to date, sales tax collections are up by 2.8% compared to last year and \$(20.5) million below forecast.

Table 2 below includes the major categories of the state's sales tax, which together account for approximately 90% of total collections.

Among the major sales tax categories, only the restaurant and bar category performed well in February compared to the same month in the prior year. However, the 17.4% year-over-year increase in tax collections from restaurant and bar sales was overstated for 2 reasons: (1) a technical adjustment that understated February 2015 collections by \$3.2 million and (2) one-time increase from the College National Championship Game that overstated February 2016 collections by an unknown amount.

February represents the first full year since the implementation of the change in the taxation of construction materials under the 2013 "TPT Simplification" legislation. Materials used for maintenance, repair, replacement, and alteration of property are no longer taxed under prime contracting TPT but rather under retail TPT.

As discussed in the summary section, the continued decline in prime contracting tax revenue in February was somewhat surprising considering the simultaneous 5.4% year-over-year increase in construction employment. This suggests that there may be a "disconnect" between contracting tax collections and contracting employment.

	<u>February</u>	<u>YTD</u>
Retail	3.7%	7.8%
Contracting	(7.6)%	(16.4)%
Use	3.4%	(1.0)%
Restaurant & Bar	17.4%	5.5%
Utilities	2.5%	2.0%

Individual Income Tax net revenues were \$77.5 million in February, which were \$40.7 million more than the prior year and \$44.2 million above forecast for the month. Year-to-date, revenue has grown 6.6% over the prior year.

As indicated in Table 3, withholding increased by 8.8% above last year and was \$12.0 million above the

forecast. The strong monthly growth is partly explained by an increase in processing days relative to February 2015. Year-to-date withholding collections are 3.5% above FY 2015.

February estimated and final payments of \$25.4 million were 24.7% above last year and \$4.8 million above the forecast. Year-to-date, payments are 24.1% above those collected during the same period of FY 2015.

February Individual Income Tax refunds totaled \$(284.4) million – this compares to \$(292.9) million in February 2015 and a forecasted amount of \$(311.8) million. The drop in refunds during the month may have been the result of a timing issue that accelerated some refunds to January.

	<u>February</u>	<u>YTD</u>
Withholding	8.8%	3.5%
Estimated/Final Payments	24.7%	24.1%
Refunds	(2.9)%	7.8%

Corporate Income Tax net collections were \$12.3 million in February, which was \$11.1 million more than the prior year and \$11.2 million above the forecast. Year to date, collections are \$(36.1) million below prior year collections. This decrease is probably the result of the decline in the Corporate Income Tax rate.

The **Lottery Commission** reports that January ticket sales were \$138.4 million, which is \$67.8 million, or 95.9%, above sales in the prior year. Powerball ticket sales comprised \$62.4 million of the increase compared to last year, having been spurred by a \$1.5 billion record-breaking jackpot during the month. Year-to-date ticket sales are \$518.4 million, which is 26.7% above last year's sales. General Fund distributions associated with the January sales are not expected to occur until April.

Insurance Premium Tax collections of \$2.1 million in February were \$(3.1) million below the prior year and \$(3.0) million below the forecast. Year-to-date, collections are 6.6% above last year.

Due to the implementation of a new accounting system, DOR has made **technical adjustments** to prior month collection figures. For February, DOR has decreased the amount of prior General Fund revenue collections by \$(0.8) million, and the adjustment has been included in the reported year-to-date results.

Table 4

General Fund Revenue: Change from Previous Year and Budget Forecast February 2016

	Current Month					FY 2016 YTD (Eight Months)				
	Actual February 2016	Change From February 2015		Baseline Forecast		Actual February 2016	Change from February 2015		Baseline Forecast	
		Amount	Percent	Amount	Percent		Amount	Percent	Amount	Percent
Taxes										
Sales and Use	\$337,926,114	\$12,548,839	3.9 %	(\$4,854,888)	(1.4) %	\$2,856,590,327	\$77,104,445	2.8 %	(\$20,521,436)	(0.7) %
Income - Individual	77,521,976	40,713,948	110.6	44,189,339	132.6	2,612,612,480	161,156,379	6.6	56,502,320	2.2
- Corporate	12,260,403	11,124,188	--	11,177,459	--	290,739,438	(36,083,541)	(11.0)	13,443,963	4.8
Property	300,944	(203,906)	(40.4)	(491,605)	(62.0)	23,586,497	2,170,439	10.1	(179,429)	(0.8)
Luxury - Tobacco	1,823,275	1,194,145	189.8	347,267	23.5	15,950,226	1,276,249	8.7	240,329	1.5
- Liquor	3,276,932	1,057,039	47.6	1,096,561	50.3	21,860,591	280,161	1.3	22,902	0.1
Insurance Premium	2,067,262	(3,077,420)	(59.8)	(2,983,047)	(59.1)	193,086,786	12,000,693	6.6	(4,721,458)	(2.4)
Other Taxes	1,393,963	(153,998)	(9.9)	(84,113)	(5.7)	4,114,279	(747,427)	(15.4)	(400,110)	(8.9)
Sub-Total Taxes	\$436,570,868	\$63,202,835	16.9 %	\$48,396,973	12.5 %	\$6,018,540,623	\$217,157,397	3.7 %	\$44,387,080	0.7 %
Other Revenue										
Lottery	0	(9,263,200)	(100.0)	0	--	27,544,450	2,954,650	12.0	1,833,547	7.1
License, Fees and Permits	2,325,522	764,256	49.0	48,666	2.1	19,735,079	(931,072)	(4.5)	(308,452)	(1.5)
Interest	2,759	567	25.9	894	48.0	13,393	(7,970)	(37.3)	457	3.5
Sales and Services	936,105	(9,532,882)	(91.1)	(8,327,030)	(89.9)	10,517,906	(9,519,305)	(47.5)	(8,453,802)	(44.6)
Other Miscellaneous	2,347,449	1,249,992	113.9	1,262,577	116.4	20,225,852	4,184,318	26.1	(3,049,753)	(13.1)
Disproportionate Share	0	0	--	0	--	0	0	--	0	--
Transfers and Reimbursements	1,237,067	(2,819,768)	(69.5)	(3,007,366)	(70.9)	19,517,046	(11,517,674)	(37.1)	(2,471,079)	(11.2)
Sub-Total Other Revenue	\$6,848,901	(\$19,601,035)	(74.1) %	(\$10,022,259)	(59.4) %	\$97,553,727	(\$14,837,053)	(13.2) %	(\$12,449,081)	(11.3) %
TOTAL BASE REVENUE	\$443,419,769	\$43,601,800	10.9 %	\$38,374,714	9.5 %	\$6,116,094,350	\$202,320,344	3.4 %	\$31,937,999	0.5 %
Other Adjustments										
Urban Revenue Sharing	(50,469,528)	275,114	--	(6)	0.0	(403,756,222)	2,200,918	--	(6)	0.0
One-Time Transfers	5,168,200	(2,086,256)	(28.8)	0	0.0	75,943,900	12,820,398	20.3	0	0.0
Sub-Total Other Adjustments	(45,301,328)	(1,811,142)	4.2 %	(6)	0.0 %	(327,812,322)	15,021,316	-- %	(6)	0.0 %
TOTAL GENERAL FUND REVENUE	\$398,118,441	\$41,790,659	11.7 %	\$38,374,707	10.7 %	\$5,788,282,028	\$217,341,660	3.9 %	\$31,937,993	0.6 %
Non-General Funds										
Highway User Revenue Fund	\$113,786,424	\$4,652,421	4.3 %	\$3,591,977	3.3 %	\$889,925,825	\$46,514,920	5.5 %	\$6,470,787	0.7 %

Monthly Indicators

NATIONAL

According to the U.S. Department of Commerce Bureau of Economic Analysis, the **U.S. Real Gross Domestic Product (GDP)** increased at an annual rate of 1.0% in the fourth quarter of 2015. This estimate represents a slowdown from the 2.0% growth in the third quarter of 2015. The deceleration was primarily due to slower growth in consumption and decreases in business investment, exports and state and local government spending. Declining performance in these categories was partly offset by deceleration in imports and a pick-up in federal government spending.

The Conference Board's **U.S. Consumer Confidence Index** decreased (5.6) points in February to a level that is (6.7)% below the February 2015 level. The decrease reflected a widespread drop of consumer confidence in current economic circumstances and in the economic outlook six months in the future. Economists believe the monthly drop reflected anxiety over stock market volatility and an unimpressive employment report. As this negative activity have since eased, it is expected that consumer confidence will return to growth in the index's next release.

The Conference Board's **U.S. Leading Economic Index** decreased by (0.2)% in January but still stands 2.2% above its January 2015 reading. Of the index's 10 components, 5 made positive contributions in January while 4 made negative contributions and 1 was neutral. The greatest drag on the index came from stock prices and initial claims for unemployment insurance. These impacts were partly offset by movement in interest rates and improvement in manufacturing orders and hours worked.

According to the U.S. Department of Commerce Bureau of Economic Analysis, the **U.S. Personal Consumption Expenditure Price Index (PCEPI)** increased 0.1% in January, relative to December. The measure stands 1.3% above the January 2015 level. While this amount represents the index's strongest year-over-year growth since October 2014, it is still well below the Federal Reserve Bank's 2% annual inflation target. The low measure is largely due to a (5.2)% year-over-year decrease in energy prices. Annual growth in the core index (all items except food and energy), however, has grown by a steadier 1.7% through January.

ARIZONA

Housing

Single-family housing construction is accelerating, while multi-family construction has peaked. Arizona's 12-month total of **single-family building permits** is 22,971, or 31.3% more than a year ago. The comparable single-family permit growth rate for the entire U.S. is 9.7%. See *Appendix A – Tracking Arizona's Recovery for historical information.*

The 12-month total of multi-family building permits was increasing strongly compared to last year, but has recently leveled off. Arizona's total of 9,808 **multi-family building permits** is (5.2)% below 2015. Arizona's rate of increase is now significantly less than the comparable multi-family permit growth for the U.S. as a whole, which is 21.0% above 2015.

Employment

As a result of the annual benchmarking revision of establishment survey data, the Department of Administration (DOA) reported in March that Arizona added more nonfarm jobs in 2014 and 2015 than previous estimates indicated. By incorporating comprehensive data from unemployment insurance records, the federal Bureau of Labor Statistics (BLS) determined that the state added, on average, 2,000 and 5,900 more jobs per month in 2014 and 2015, respectively, than previously reported. On an average annual basis, the job growth in 2015 was 0.2% higher than previously estimated. Overall, the state had a net increase of 66,000 (+2.6%) nonfarm jobs in 2015, which was largest net gain since 2006.

The latest estimate of **nonfarm employment** showed that the state shed (48,600) jobs in January over December in the prior year. Job losses typically occur in January when the holiday season comes to an end. The average job reduction for the month of January in the prior 10 years was (57,000). Compared to January 2015, nonfarm employment was up by 3.0%, or 78,100 jobs.

In January, the **Average Weekly Hours** worked by individuals in Arizona's private sector was 34.2 hours. This workload is (0.3)% below the prior month level and (0.6)% below the January 2015 level.

The **Average Hourly Earnings** received by these private sector workers was \$23.42, which is 0.7% above the average in the prior month. January earnings were 2.2% above the average in January 2015 and represent the 10th consecutive month of positive year-over-year increases in average wages.

Monthly Indicators (Continued)

The household survey data used to estimate the state's **unemployment rate** was also recently revised. The historical revision, which included the period from 1976 through 2015, was relatively small on an annualized basis. The state's seasonally adjusted jobless rate fell from 5.9% in December to 5.6% in January. The U.S. unemployment rate in January was significantly lower at 4.9%.

Tourism

Revenue per available room reached \$75.82 in January, which was (6.3)% below the amount in January 2015.

Arizona state park visitation in December 2015 was up 3.6% from visitation in December 2014.

State Agency Data

At the beginning of March 2016, the total **AHCCCS** caseload was 1.8 million members. Since the federal health care expansion in January 2014, the overall AHCCCS population has grown by 546,400 members.

Total monthly enrollment increased by 3,300 members, or 0.2%, during February. The monthly increase offsets the majority of decreases experienced during the prior 2 months. The overall increase in February was spread among most enrollment populations. The Traditional population of lower income children and their parents increased 800 (0.1%) during the month to a level of 1,050,300 members. This was accompanied by an enrollment increase of 500, or 0.3%, in the Proposition 204 Parent population.

In January 2014, the state started accepting new enrollment to the Proposition 204 childless adults program. In February 2016, the childless adult population increased by 1,300, or 0.4%. At 308,400, this population is 10.5% higher than a year ago.

The state also opted to expand adult Medicaid coverage to 133% of FPL. Their enrollment increased by 400 in February and now totals 83,700 individuals. Enrollment is 99.4% higher than a year ago. The federal government is currently paying 100% of this cost.

There were 21,526 **TANF recipients** in the state in February, representing a (1.0)% decrease in monthly caseloads from January. The year-over-year number of TANF recipients has declined by (16.4)%. The statutory lifetime limit on cash assistance is 24 months.

The **Supplemental Nutrition Assistance Program (SNAP)**, formerly known as Food Stamps, provides assistance to low-income households to purchase food. This

February, there were 962,037 food stamp recipients in the state, representing a (1.3)% decrease from January caseloads. Compared to February of last year, food stamp participation declined by (4.7)%.

On February 29, 2016, ADC reported an **inmate population** of 42,663. Down by 22 inmates from January, this marked a decrease of (0.1)%. Since last February, the population increased by 1.4%.

Based on revised information that the Department of Child Safety provided for November 2015, **reports of child maltreatment** totaled 51,136 over the last 12 months, an increase of 5.8% over the prior year. There were 18,815 **children in out-of-home care** as of November 2015, or 10.5% more than in November 2015. Compared to the prior month, the number of out-of-home children decreased by (0.5)%.

Table 5

MONTHLY INDICATORS

<u>Indicator</u>	<u>Time Period</u>	<u>Current Value</u>	<u>Change From Prior Period</u>	<u>Change From Prior Year</u>
Arizona				
<u>Employment</u>				
- Regular Unemployment Rate	January	5.6%	(0.3)%	(0.8)%
- Total Unemployment Rate (discouraged/underemployed)	4 th Q 2015	12.8%	(0.8)%	(1.9)%
- Initial Unemployment Insurance Claims	January	19,143	19.5%	1.2%
- Unemployment Insurance Recipients	August	29,157	(23.0)%	(32.2)%
- Non-Farm Employment - Total	January	2,674,100	(1.8)%	3.0%
Manufacturing	January	160,100	(0.3)%	2.6%
Construction	January	129,100	(0.7)%	5.4%
- Average Weekly Hours, Private Sector	January	34.2	(0.3)%	(0.6)%
- Average Hourly Earnings, Private Sector	January	\$23.42	0.7%	2.2%
<u>Sales</u>				
- Retail Taxable Sales				
Motor Vehicles/Misc. Auto	November	\$976.0 million	5.1%	15.0%
Furniture/Home Furnishings	November	\$303.1 million	(11.5)%	(2.0)%
Building Material/Lawn & Garden	November	\$387.3 million	8.6%	16.1%
<u>Building</u>				
- Residential Building Permits (12-month avg)				
Single-family	January	22,971	1.7%	31.3%
Multi-family	January	9,808	7.5%	(5.2)%
- Maricopa County/Other, Home Sales (ARMLS)				
Single-Family (Pending Sales)	January	4,515	16.2%	2.5%
- Maricopa County/Other, Median Home Price (ARMLS)				
Single-Family (Pending Sales)	January	\$229,000	(0.4)%	8.8%
- Phoenix S&P/C Home Price Index (2000 = 100)	December	157.22	0.5%	6.3%
- Maricopa Pending Foreclosures	January	4,156	(2.5)%	(26.8)%
- Greater Phoenix Total Housing Inventory, (ARMLS)	January	25,886	13.1%	(4.5)%
<u>Tourism</u>				
- Phoenix Sky Harbor Air Passengers	December	3.71 million	4.8%	(0.7)%
- National Park Visitors	December	601,364	(5.5)%	0.0%
- State Park Visitors	December	121,800	(31.1)%	3.6%
- Revenue Per Available Hotel Room	January	\$75.82	46.3%	(6.3)%
<u>General Measures</u>				
- Arizona Consumer Confidence Index (1985 = 100)	1st Q 2016	81.6	0.5%	3.2%
- Arizona Coincident Index (July 1992 = 100)	December	223.38	0.6%	4.4%
- Arizona Leading Index -- 6 month projected growth	December	7.0%	0.1%	3.5%
- Arizona Personal Income	3 rd Q 2015	\$269.5 billion	1.4%	5.2%
- Arizona Population	July 2015	6,828,065	N/A	1.5%
- State Debt Rating				
Standards & Poor's/Moody's	May	AA / Aa2	N/A	N/A
Outlook	May	Stable	N/A	N/A
<u>Agency Measures</u>				
- AHCCCS Recipients	March 1 st	1,804,530	0.2%	13.2%
Acute Care Traditional		1,050,251	0.1%	10.1%
Prop 204 Childless Adults		308,445	0.4%	10.5%
Other Prop 204		188,476	0.3%	11.7%
Adult Expansion		83,745	0.5%	99.4%
Kids Care I		711	(2.6)%	(56.4)%
Long-Term Care – Elderly & DD		57,693	0.1%	1.8%
Emergency Services		115,209	0.2%	25.2%
- Department of Child Safety (DCS)				
Annual Reports of Child Maltreatment (12-month total)	Nov. 2015	51,136	0.0%	5.8%
DCS Out-of-Home Children	November	18,815	(0.5)%	10.5%
Filled Caseworkers (1406 Budgeted)	January	1,273	(36)	(80)
- ADC Inmate Growth	February	42,663	(0.1)%	1.4%
- Department of Economic Security				
- TANF Recipients	February	21,526	(1.0)%	(16.4)%
- SNAP (Food Stamps) Recipients	February	962,037	(1.3)%	(4.7)%
- Judiciary Probation Caseload				
Non-Maricopa	December	18,598	19	491
Maricopa County	December	27,559	118	1,060
United States				
- Gross Domestic Product	4 th Q, 2015	\$16.5 trillion	1.9%	1.0%
(Chained 2009 dollars, SAAR)	(2 nd Estimate)			
- Consumer Confidence Index (1985 = 100)	February	92.2	(5.7)%	(6.7)%
- Leading Indicators Index (2010 = 100)	January	123.2	(0.2)%	2.2%
- Consumer Price Index, SA (1982-84 = 100)	January	238.1	0.0%	1.3%
- Personal Consumption Price Index (2009 = 100)	January	110.0	0.1%	1.3%

JLBC Meeting

At its February 25, 2016 meeting, the Joint Legislative Budget Committee considered the following issues:

Arizona Department of Administration/Department of Child Safety – Review of CHILDS Automation Project -

The Committee gave a favorable review of the department's \$4.4 million expenditure plan from the transition appropriation for CHILDS infrastructure to migrate DCS data to a private vendor. The Committee included a provision in its review requiring DCS to report on any conditions required by the Information Technology Authorization Committee (ITAC) and to submit quarterly independent third-party reports.

Department of Economic Security – Review of Appropriation Transfers - The Committee gave a favorable review of a portion of the requested transfers into the Division of Developmental Disabilities (DDD) Operating Budget and Case Management lines. The Committee favorably reviewed \$11.5 million in transfers sufficient to align appropriations

with FY 2015 expenditures, to cover FY 2016 premium tax increases in the DDD Operating Budget line, and to fund FY 2016 case manager pay adjustments.

Summary of Recent Agency Reports

AHCCCS – Report on the FY 2015 Hospital Assessment – Pursuant to A.R.S. § 36-2901.08, the Arizona Health Care Cost Containment System (AHCCCS) is required to establish an assessment on hospital revenue, discharges, or bed days for the purpose of funding the state match portion of the Medicaid expansion (adults from 100%-133% of the Federal Poverty Level) and the entire Proposition 204 population. In addition, A.R.S. § 36-2903.08 requires AHCCCS to annually report the amount of estimated Medicaid payments each hospital received for services provided to populations whose coverage is funded by the assessment.

AHCCCS estimates that hospitals received coverage payments of \$795.9 million in FY 2015, or \$525.4 million above the \$270.5 million in assessments these hospitals paid. Out of 108 hospitals that served Medicaid enrollees in FY 2015, AHCCCS estimates that 103 received at least as much in coverage payments as they had paid in hospital assessments. The remaining 5 hospitals received an estimated \$3.0 million less in combined payments than they had paid in assessments.

Due to reporting lags between providers and AHCCCS health plan contractors, payments can take upwards of 3-6 months before paid claims appear in AHCCCS' database. Because of this lag, AHCCCS was not able to report the FY 2015 estimated Medicaid payments

each hospital received by the August 1 reporting date in A.R.S. § 36-2903.08. (Jon Stall)

AHCCCS – Report on Interstate Agreement with Hawaii – Pursuant to A.R.S. § 36-2925H, the Arizona Health Care Cost Containment System (AHCCCS) has submitted its annual report on the status of an Interstate Agreement with the State of Hawaii.

This report summarizes the continued activities associated with the agreement between AHCCCS and Hawaii for Medicaid data processing. In FY 2015, Arizona received \$8.8 million in revenues from Hawaii, of which \$8.1 million was expended for staffing and automation costs associated with implementing the agreement. The remaining \$761,700 was deposited into 2 funds with a combined balance of \$2.9 million. (Jon Stall)

State Department of Corrections – Third-Party Report on the Adult Inmate Management System (AIMS) Replacement – Pursuant to a FY 2015 General Appropriation Act footnote, the Arizona Department of Corrections (ADC) provided a quarterly update of the progress of the AIMS replacement project. The project has been appropriated \$16.0 million; both the JLBC Baseline and the Executive budget include \$8.0 million for FY 2017 to complete the project. The FY 2015

Summary of Recent Agency Reports (Continued)

appropriation required ADC to provide the third-party reports upon expenditure of the FY 2015 monies.

The third-party reviewer noted that ADC and the vendor continue to “collaborate efficiently and effectively” and the “project’s fiscal status remains good.” ADC is customizing an off-the-shelf system for the inmate management needs of the department. ADC and the vendor are simultaneously developing and testing different functions and areas of the new system. In order to facilitate this process, the report details how the vendor and department instituted tracking and decision-making procedures to ensure that the project is completed on time, and developed protocols for testing both newly-completed modules and the overall project.

The reviewer indicated that the vendor and ADC shifted the documentation, monitoring, and reporting standards to align with the communication and development processes that emerged as both parties worked on the project. ADC has accepted the risk associated with changing the initial standards.

The vendor and department continue to work to mitigate risk in the testing period, transfer legacy data, and develop the model for final testing and the full operational use by the department. The pilot implementation is still scheduled for February 2017 and the full implementation for March 2017. (Micaela Larkin)

Department of Health Services – Report on Arnold v. Sarn – Pursuant to a FY 2016 General Appropriation Act footnote, the Department of Health Services (DHS) has submitted the report for the first and second quarter of FY 2016 on implementing the *Arnold v. Sarn* joint agreement.

The state has been a longstanding defendant in the *Arnold v. Sarn* litigation concerning the level of services provided to the Seriously Mentally Ill (SMI) population. In January 2014, both parties filed a joint agreement with the court to terminate the lawsuit. The agreement, which received court approval in February 2014, requires expansion of certain services by June 2016. These services include Assertive Community Treatment (ACT), Peer Support, Supported Employment, and Supportive Housing.

Assertive Community Treatment (ACT): The joint agreement requires DHS to establish 8 additional ACT teams. ACT teams include more than 10 specialized health care professionals that provide community-based services that are tailored to the client’s needs. DHS estimates that the cost per team added is approximately \$1.5 million. As a result, DHS expects that the Total Fund cost of adding all 8 teams is \$11.6 million, including \$8.7

million from the General Fund. DHS added 1 team in September 2015, increasing the total number of ACT teams to 21. Since the beginning of FY 2015, DHS has added a total of 6 ACT teams.

Peer Support: The joint agreement requires DHS to provide peer support services to an additional 1,500 SMI clients. Peer support services are delivered in individual and group settings by individuals who have personal experience with mental illness, substance abuse, and recovery. DHS estimates that the cost per client for such services is approximately \$1,100. As a result, DHS expects that the Total Fund cost of adding 1,500 SMI clients is \$1.6 million, including \$1.2 million from the General Fund. DHS has added a total of 1,802 clients since the beginning of FY 2015, increasing the total number of Class Members receiving peer support services to 4,125.

Supported Employment: The joint agreement requires DHS to provide supported employment services to an additional 750 SMI clients. Supported employment services include assistance in attaining employment, job coaching, transportation, specialized job training and individually tailored supervision. DHS estimates that the cost per client for such services is approximately \$1,600. As a result, DHS expects that the Total Fund cost of adding 750 clients is \$1.2 million, including \$923,000 from the General Fund. DHS has added 741 clients since the beginning of FY 2015, increasing the total number of Class Members receiving supported employment services to 1,214.

Supportive Housing: The joint agreement requires DHS to provide supported housing services to an additional 1,200 SMI clients. Supportive housing includes financial assistance such as rental subsidies as well as support services to help clients obtain and maintain housing. DHS estimates that the cost per client for such services is approximately \$26,300. As a result, DHS expects that the Total Fund cost of adding 1,200 SMI clients is \$31.5 million, including \$26.8 million from the General Fund. DHS has added 2,805 clients since the beginning of FY 2015, increasing the total number of Class Members receiving supportive housing services to 2,805. (Patrick Moran)

February Spending

February 2016 General Fund spending of \$510.6 million was \$(37.0) million less than February 2015. Year to date, spending is \$6.89 billion, or \$(159.0) million below last year. (See Tables 6 & 7).

- Year to date, the Department of Education has spent \$44.2 million more than the prior year.
- Due to technical reporting issues with the newly-created Department of Child Safety (DCS) in FY 2015, the figures reported below for DCS and the Department of Economic Security do not accurately reflect changes in spending levels from the prior year.
- Even after accounting for issues relating to DCS, the significant decline in DES spending year-to-date is due to technical timing issues relating to the disbursement of Medicaid matching funds.
- During FY 2016, Universities spending has declined by \$(75.3) million. This is related to changes enacted in the FY 2016 budget, which contained a \$(99.0) million spending reduction for the Universities system.

	General Fund Spending (\$ in Millions)			
	Change From		Year-to-Date	YTD Change from FY 15
	Feb 16	Feb 15		
Agency				
AHCCCS	81.4	(44.6)	856.6	(84.0)
Corrections	77.9	1.3	690.7	44.9
Child Safety	14.0	14.0	260.8	181.0
Economic Security	4.4	(2.4)	418.5	(215.7)
Education	221.5	(5.8)	2,917.5	44.2
Health Services	15.5	(0.0)	544.5	(3.7)
Public Safety	1.8	(0.8)	56.8	1.1
School Facilities Board	23.9	6.7	185.9	12.6
Universities	36.5	(9.1)	511.3	(75.3)
Leaseback Debt Service	0.0	0.0	84.1	(0.0)
Other	<u>33.7</u>	<u>3.7</u>	<u>367.5</u>	<u>(64.1)</u>
Total	510.6	(37.0)	6,894.2	(159.0)

General Fund Spending				
(\$ in Thousands)				
Agency	Feb 16	Change from Feb 15	Year-to-Date	YTD Change from FY 15
Dept. of Admin./Automation Projects Fund	4,815.0	1,266.9	17,678.9	(26,152.3)
ADOA – Sale/Leaseback Debt Service	-	-	84,114.6	(7.1)
Office of Administrative Hearings	61.7	(3.8)	576.3	(25.9)
Commission of African-American Affairs	10.6	4.9	81.2	74.0
Department of Agriculture	282.5	(71.3)	5,253.3	172.2
AHCCCS	81,376.4	(44,646.9)	856,550.2	(83,959.0)
Attorney General	2,701.5	1,000.6	14,658.4	147.8
State Board of Charter Schools	75.5	14.2	716.9	140.2
Department of Child Safety	13,951.6	13,951.6	260,848.8	180,950.7
AZ Commerce Authority	2,283.3	(416.7)	17,891.4	(3,333.6)
Community Colleges	215.2	(90.1)	38,678.1	(14,853.1)
Corporation Commission	1.5	(51.9)	288.2	(118.4)
Department of Corrections	77,880.6	1,323.1	690,713.1	44,938.0
County Funding	-	-	6,000.5	(1,650.0)
AZ State Schools for the Deaf & Blind	1,911.7	1,078.2	18,178.3	4,072.6
Department of Economic Security	4,430.2	(2,360.4)	418,453.5	(215,655.7)
State Board of Education	86.4	86.4	743.0	743.0
Department of Education	221,538.4	(5,814.2)	2,917,546.0	44,207.1
DEMA	727.7	239.5	5,721.2	(206.4)
DEQ – WQARF	-	-	7,000.0	-
Office of Equal Opportunity	21.5	8.3	125.8	25.0
State Board of Equalization	22.3	(1.3)	380.5	10.2
Board of Executive Clemency	79.3	15.1	625.3	4.3
Department of Financial Institutions	207.0	(27.6)	1,990.5	(23.5)
Department of Fire, Bldg and Life Safety	212.0	41.6	1,465.4	37.9
State Forester	291.7	(732.5)	3,539.9	473.5
Department of Gaming	-	-	1,794.4	1,794.4
Arizona Geological Survey	79.6	26.4	685.2	37.9
Governor/OSP	692.6	124.5	6,326.0	(790.9)
Department of Health Services	15,515.2	(12.8)	544,521.9	(3,722.9)
Arizona Historical Society	195.3	(21.2)	2,265.4	15.8
Prescott Historical Society of AZ	88.4	(55.1)	587.8	32.5
Independent Redistricting Comm.	238.4	158.8	1,154.9	428.4
Commission of Indian Affairs	1.1	(0.1)	22.0	(19.0)
Department of Insurance	336.4	3.4	3,318.8	(205.5)
Judiciary				
Supreme/Superior Court	2,047.0	(584.8)	56,552.5	(3,308.5)
Court of Appeals	1,025.0	(65.4)	9,197.8	(34.1)
Department of Juvenile Corrections	1,534.2	(1,142.0)	16,960.6	(9,018.1)

Table 7 (Continued)

Agency	Feb 16	Change from Feb 15	Year-to-Date	YTD Change from FY 15
State Land Department	634.3	(91.1)	7,073.2	(927.5)
Legislature				
Auditor General	1,491.8	5.1	13,076.2	(128.8)
House of Representatives	1,247.8	(26.2)	9,130.4	555.2
Joint Legislative Budget Comm.	165.1	(43.6)	1,516.6	8.2
Legislative Council	495.3	62.1	4,249.3	(1,804.5)
Senate	613.5	(286.0)	4,977.3	(608.0)
Mine Inspector	85.8	11.3	743.1	(17.3)
Nav. Streams & Adjudication	7.8	(2.0)	79.8	(29.2)
Occupational Safety and Health Review	-	-	2.5	1.6
Arizona State Parks Board	2.5	2.5	277.8	277.8
Phoenix Convention Center	-	-	20,449.0	-
Pioneers' Home	-	(4.3)	-	(1,022.4)
Comm. for Postsecondary Ed.	-	-	1,396.8	-
Department of Public Safety	1,763.5	(849.7)	56,805.5	1,098.3
Public Safety Personnel Retirement System	-	-	6,000.0	-
Arizona Department of Racing	-	-	-	(1,869.6)
Radiation Regulatory Agency	6.5	(49.8)	1,190.3	158.4
Real Estate Department	169.7	9.5	1,663.4	(18.7)
Department of Revenue	4,058.4	2,239.3	27,484.1	(3,566.5)
Rio Nuevo Distribution	-	-	-	-
School Facilities Board	23,929.5	6,675.8	185,892.3	12,561.2
Secretary of State	2,994.3	1,330.0	9,036.0	(848.7)
Tax Appeals Board	17.1	0.4	180.3	(1.0)
Office of Tourism	-	-	6,399.4	(1,994.0)
Department of Transportation	-	(0.1)	-	(0.1)
Universities				
Board of Regents	22.2	1.8	19,078.4	(3,224.3)
Arizona State University	16,554.5	(5,004.7)	223,522.9	(39,526.1)
Northern Arizona University	5,826.9	(1,488.6)	77,110.0	(11,909.1)
University of Arizona	14,080.3	(2,586.1)	191,571.9	(20,689.1)
Department of Veteran Services	438.0	84.3	3,404.0	384.8
Department of Water Resources	866.5	(64.0)	6,933.2	(227.4)
Water Infrastructure Finance Authority	-	-	-	(1,000.0)
Department of Weights & Measures	4.2	(73.5)	820.9	(42.6)
Other - JP Salaries Distribution	89.1	(175.5)	817.7	131.7
Other	95.0	95.0	136.8	98.3
Total	510,596.5	(36,982.9)	6,894,225.5	(158,957.3)

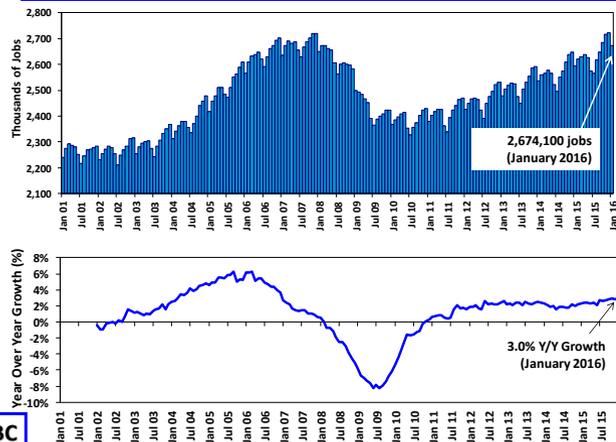
Tracking Arizona's Recovery

March 2016
Appendix A

Page:

- 2.....Total Non-Farm Employment
- 3.....Average Hourly Earnings – Private Sector
- 4.....Initial Claims for Unemployment Insurance
- 5.....State Sales Tax Collections – Retail Category
- 6.....State Sales Tax Collections – Contracting Category
- 7.....Residential Building Permits
- 8.....Economic Activity Index

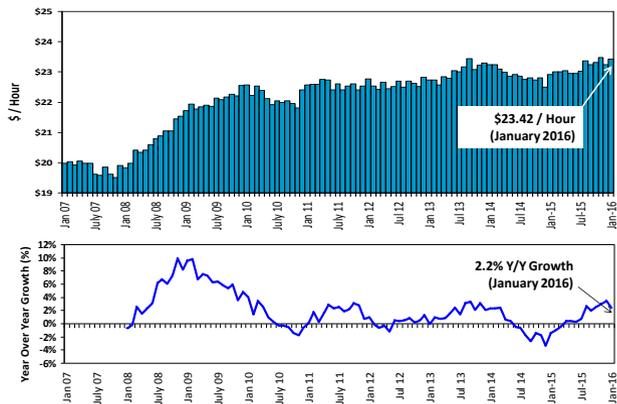
Total Non-Farm Employment



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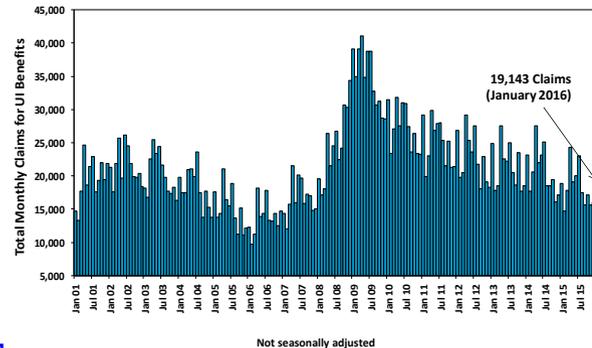
Average Hourly Earnings – Private Sector



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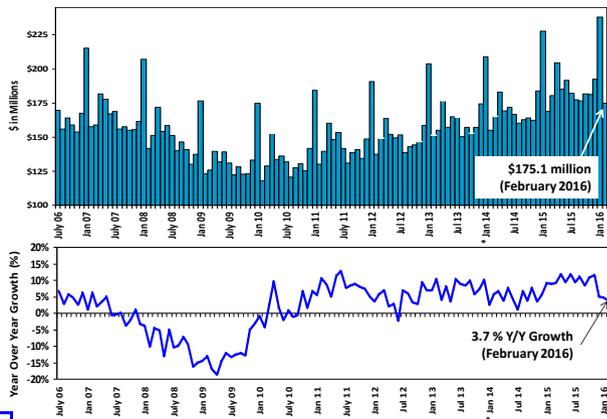
Initial Claims for Unemployment Insurance



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State Sales Tax Collections – Retail Category



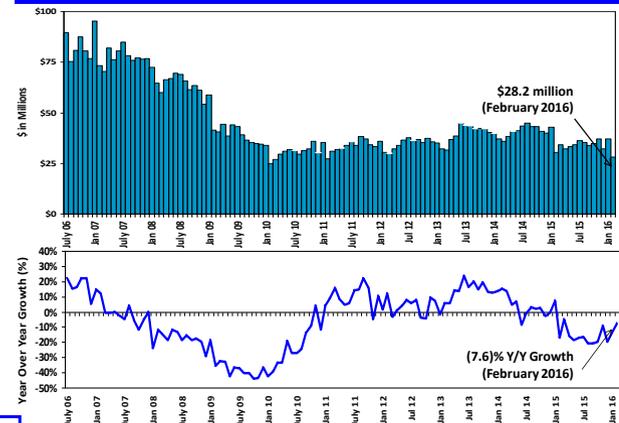
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Excludes temporary 1 ¢ sales tax

* January 2014 estimate adjusted downward by \$30 million to reflect one-time category shift.

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State Sales Tax Collections – Contracting Category

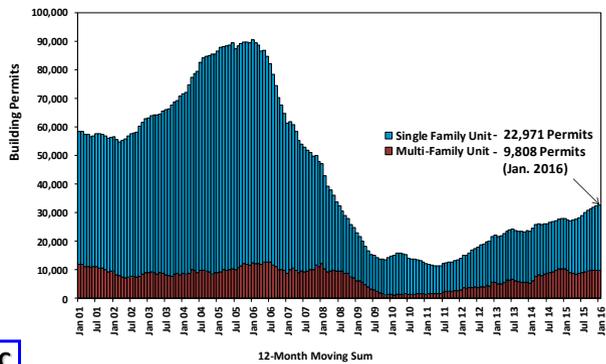


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Excludes temporary 1 ¢ sales tax

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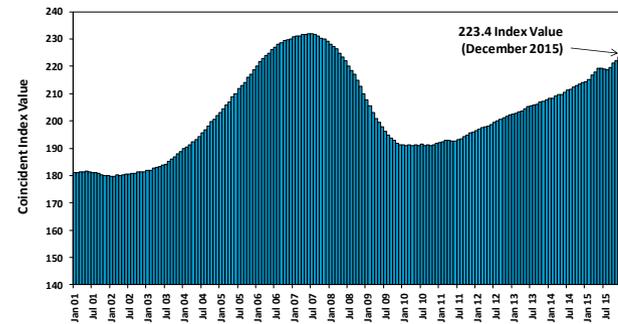
Residential Building Permits



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7

Economic Activity Index



JLBC

Source: Coincident Index – Federal Reserve Bank of Philadelphia. Combines four state-level indicators (employment, average hours worked in manufacturing, the unemployment rate, and wage and salary disbursements) to summarize current economic conditions.

8