

ARIZONA
MONTHLY FISCAL HIGHLIGHTS
 September 2004

General Fund revenue collections were \$705.7 million in September. This amount is \$46.6 million over the forecast for the month and 18.7% over September of last year. Collections for the first 3 months of the fiscal year total \$102.9 million over the budgeted forecast. The General Appropriation Act included a provision that any revenue exceeding the budgeted forecast for the first six months of FY 2005 will be dedicated for specific purposes. Any "excess" FY 2005 revenue will be divided evenly between the General Fund and the Budget Stabilization Fund.

September collections were \$111.0 over the same month last year. Sales tax collections continued the strong growth seen over the last several months with an increase of \$25.4 million (based on preliminary numbers) over last September. Individual income tax collections were \$27.3 million over last year, and corporate income tax collections were up \$34.4 million. In addition to strong growth in the three major revenue categories, September insurance premium tax collections were almost \$25 million above last year due to the full year implementation of the elimination of the Medicaid exemption.

This report also includes summaries of the October 14th JLBC and JCCR meetings.

General Fund Revenues			
Compared to Adopted Forecast and FY 2004 Collections			
(\$ in Millions)			
	<u>FY 2005</u>	<u>Difference</u>	<u>Difference</u>
	<u>Collections</u>	<u>From Forecast</u> ^{1/}	<u>From FY 2004</u>
September	\$ 705.7	\$ 46.6	\$ 111.0
Year-to Date	\$ 1,780.9	\$ 102.9	\$ 229.8

^{1/} Enacted FY 2005 budget (May)

Sales Tax revenue increased by 9.5% on a year-over-year basis in September and was \$13.6 million above the forecast for the month. Year-to-date, collections are 9.7% over the first quarter of last fiscal year and \$27.3 million over forecast for the period. The following is based on collections through August:

- Retail sales tax receipts have increased by 7.9%
- Contracting continues to exhibit the large increases begun last year, with a year-to-date increase of 16.6%.
- Restaurants and bars collections are up 9.7%.
- Use tax receipts (all of which is retained by the state) are up 19.5%.

Individual Income Tax collections for September were 11.8% above last year. Withholding tax collections increased by only \$4.9 million or 2.7%. However, net estimated/final payments and refunds were up by \$22.4 million, or 43.6% compared to September of last year. Year-to-date total individual income tax collections are 11.7% above last year, and \$32.9 million above the forecast for the year.

Corporate Income Tax revenue of \$122.4 million was almost 40% above September collections last year. This increase brings year-to-date corporate collections to \$27.2 million or 19.8% over forecast.

Insurance Premium Tax revenues were \$6.0 million over the forecast for the month. First quarter collections from the elimination of the exemption for Medicaid premiums were higher than anticipated.

Estate Tax collections were \$2.9 million over the forecast for the month, bringing the year-to-date variance to \$7.7 million. This is the final year of the phase-out of the estate tax, however collections are running significantly ahead of forecast.

Recent Economic Indicators: The revised real **U.S. Gross Domestic Product (GDP)** seasonally adjusted annual growth rate was 3.3% in 2004's second quarter. Improvements in non-residential fixed investment and exports contributed to the upward revision. At least some of the increased investment may have been driven by **U.S. semiconductor billings** (three-month moving average), which were running 29.0% above the level from a year ago after rising 2.0% in the latest three-month period.



Given rising concerns about oil prices, it was not surprising to see an increase in the overall average price level. The **U.S. Consumer Price Index (CPI)** rose 0.2% in September. Excluding the effects of food and energy costs, the core CPI increased 0.3% in September and was 2.0% higher than a year ago. Overall, the CPI has increased 2.7% in the last 12 months.

Meanwhile, consumer sentiment faltered for the second consecutive month. The **U.S. Consumer Confidence Index** dipped to 96.8 in September, down (1.9)% from August. Consumers’ assessment of a tough job market was the driving force behind their subdued expectations for the economy. The **U.S. Index of Leading Economic Indicators** provided corroborative evidence, dropping for the fourth month in a row in September. Vendor performance, interest rates, and unemployment insurance claims all contributed to the decline.

The Arizona economy continued to make progress. Total **non-farm employment** advanced 2.4% in September on a year-over-year basis, led by gains in health care and construction. These two segments accounted for 40% of the jobs added during the last 12 months.

The University of Arizona’s **Business Leaders Confidence Index** faded in the current quarter, dipping (4.1)% to 65.5. The survey’s participants reported reduced profit expectations and trimmed their projected capital spending plans from the prior quarter. Regardless, the overall index remained well

above the 50% mark associated with continued business expansion.

The **Arizona Business Conditions Index**, derived from a survey of supply chain managers, climbed by a solid 8.1% in September. The employment and price components were among the factors driving the increase.

Preliminary estimates showed **Arizona’s personal income** growth slowed in 2004’s second quarter, with the total rising 6.4% over last year’s results. The state’s 1.4% increase from the first quarter ranked 31st among the states.

On the state program front, the number of **TANF recipients** (three-month average) declined to 114,991 in August, a (2.1)% drop from the previous three months. The caseload was (11.0)% below the level reported a year ago.

The **AHCCCS caseload** continued to increase in September, with the average for the latest three months rising 3.8% from the prior period.

From July through September, the **Department of Corrections’ inmate population** increased by an average of 111 inmates from the previous three months. The average head count was more than 1,000 higher than the level from a year ago.

RECENT ECONOMIC 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				
- Unemployment Rate	September	4.8%	0.4%	(0.7)%
- Jobs	September	2.35 million	1.2%	2.4%
- Contracting Tax Receipts (3-month average)	June-August	\$53.2 million	10.0%	15.6%
- Retail Sales Tax Receipts (3-month average)	June-August	\$133.6 million	0.2%	7.5%
- Residential Building Permits - (3-month moving average)				
Single-unit	August	7,648	0.8%	30.4%
Multi-unit	August	710	9.7%	1.1%
- Arizona Tourism Barometer	May	97.0	5.8%	19.0%
- Phoenix Sky Harbor Air Passengers	August	3.37 million	(6.1)%	4.0%
- Arizona Average Natural Gas Price (\$ per thousand cubic feet)	July	\$5.60	(0.2)%	10.7%
- Leading Indicators Index	July	124.9	0.1%	2.9%
- Business Conditions Index (>50 signifies expansion)	September	67.0	8.1%	8.0%
- Consumer Confidence Index	3 rd Quarter 2004	101.1	12.2%	20.2%
- Business Leaders Confidence Index	4 th Quarter 2004	65.5	(4.1)%	5.1%
- Arizona Personal Income	2 nd Quarter 2004	\$158.8 billion	1.4%	6.4%
- Arizona Population	1 st Quarter 2004	5.76 million	0.9%	3.2%
- AHCCCS Recipients (3-month average)	July-September	759,552	3.8%	2.0%
- TANF Recipients (3-month average)	June-August	114,991	(2.1)%	(11.0)%
- DOC Inmate Growth (3-month average)	July-September	32,270	111 inmates	1,003 inmates
United States				
Gross Domestic Product	2 nd Quarter 2004	\$10.8 trillion	3.3%	4.8%
- (seasonally adjusted annual growth rate)				
- Consumer Confidence Index	September	96.8	(1.9)%	25.7%
- Leading Indicators Index	September	115.6	(0.1)%	2.0%
- U.S. Semiconductor Billings -(3-month moving average)	June-August	\$3.4 billion	2.2%	29.0%
- Consumer Price Index - (3-month moving average)	July-September	189.6	0.0%	2.7%

State of Arizona

General Fund Revenue: Change from Previous Year and January Revised Forecast September 2004

	Current Month					FY 2005 YTD (Three Months)					
	Actual	Change From				Actual	Change from				
		September 2004	September 2003	Percent	Revised Forecast		Percent	September 2004	September 2003	Percent	Revised Forecast
Taxes											
Sales and Use	\$292,308,100	\$25,360,100	9.5 %	\$13,555,152	4.9 %	\$877,053,493	\$77,368,309	9.7 %	\$27,312,683	3.2 %	
Income - Individual	258,308,001	27,327,153	11.8	12,342,863	5.0	646,585,268	67,846,873	11.7	32,850,994	5.4	
- Corporate	122,358,400	34,434,823	39.2	10,384,501	9.3	164,604,752	52,456,742	46.8	27,193,325	19.8	
Property	(244,459)	(330,521)	--	(289,691)	--	328,051	(6,056,995)	(94.9)	(313,716)	(48.9)	
Luxury	5,016,109	479,811	10.6	101,109	2.1	15,267,605	1,116,650	7.9	522,605	3.5	
Insurance Premium	26,414,309	24,657,478	--	5,962,272	29.2	100,436,016	30,519,600	43.7	6,409,746	6.8	
Estate	4,528,563	1,478,609	48.5	2,853,563	170.4	12,754,491	2,129,991	20.0	7,729,491	153.8	
Other Taxes	39,834	1,634	4.3	(830,166)	(95.4)	148,491	(74,163)	(33.3)	(2,461,509)	(94.3)	
Sub-Total Taxes	\$708,728,857	\$113,409,087	19.1 %	\$44,079,603	6.6 %	\$1,817,178,167	\$225,307,007	14.2 %	\$99,243,619	5.8 %	
Other Revenue											
Lottery	2,330,000	(989,800)	(29.8)	0	0.0	5,591,200	(3,712,600)	(39.9)	0	0.0	
License, Fees and Permits	2,845,046	1,189,399	71.8	1,055,021	58.9	7,715,915	1,538,879	24.9	2,128,691	38.1	
Interest	1,742,062	(11,135,630)	(86.5)	175,965	11.2	4,358,399	(9,470,544)	(68.5)	1,886,931	76.3	
Sales and Services	3,593,376	288,752	8.7	294,316	8.9	8,565,953	(714,049)	(7.7)	(530,542)	(5.8)	
Other Miscellaneous	1,501,401	(1,308,782)	(46.6)	(312,780)	(17.2)	2,886,613	(2,929,852)	(50.4)	(1,911,003)	(39.8)	
Disproportionate Share	0	(5,625,187)	(100.0)	0	--	0	(5,625,187)	(100.0)	0	--	
Transfers and Reimbursements	2,160,614	1,981,231	--	1,340,914	163.6	12,102,791	11,594,744	--	2,126,891	21.3	
Sub-Total Other Revenue	14,172,499	(15,600,017)	(52.4) %	2,553,436	22.0 %	41,220,871	(9,318,609)	(18.4) %	3,700,968	9.9 %	
TOTAL BASE REVENUE	\$722,901,356	\$97,809,070	15.6 %	\$46,633,039	6.9 %	\$1,858,399,038	\$215,988,398	13.2 %	\$102,944,587	5.9 %	
One-Time Revenue											
Urban Revenue Sharing	(31,089,381)	(667,284)	2.2	136	(0.0)	(93,268,143)	(2,001,852)	2.2	408	(0.0)	
Budget Balancing Transfers	0	0	--	0	--	0	0	--	0	--	
VLT Transfer	13,600,000	13,600,000	--	0	0.0	13,600,000	13,600,000	--	0	0.0	
Judicial Enhancement	274,000	274,000	--	0	0.0	2,207,000	2,207,000	--	0	0.0	
Sub-Total Transfers In	(17,215,381)	13,206,716	(43.4) %	136	(0.0) %	(77,461,143)	13,805,148	(15.1) %	408	(0.0) %	
TOTAL REVENUE	\$705,685,975	\$111,015,786	18.7 %	\$46,633,175	7.1 %	\$1,780,937,895	\$229,793,546	14.8 %	\$102,944,995	6.1 %	

VP% = Percent change from comparable period in prior year

VF% = Variance from forecast

F% = Forecast percent change for the fiscal year.

R% = Average percent change from comparable period in prior year which must be attained over remaining months to realize the forecast for year.

JLBC MEETING

At its October 14th meeting, the Joint Legislative Budget Committee considered the following issues:

Arizona Board of Regents – Review of FY 2005 Tuition Revenues and University Pay Plan – The Committee gave a favorable review to the Arizona Board of Regents (ABOR) expenditure plan for tuition revenue, which is estimated to be \$39.7 million above the appropriation. The higher revenue is due to increases in tuition approved by ABOR in March 2004 and will be used primarily to cover unfunded health and retirement increases, operating inflationary increases and unfunded enrollment from prior years.

ABOR also submitted a report on non-appropriated tuition. This “retained” tuition and fees increased \$12.1 million above original FY 2005 projections. Of the \$12.1 million, \$7.4 million was allocated for financial aid and \$5.6 million was allocated for debt service. ABOR also reported on the university pay plan. Of the \$16 million appropriated for university pay plans, ABOR allocated \$7.5 million to ASU, \$6.4 to U of A, \$2.1 to NAU and \$32,000 to the ABOR Central Office

Chairman Burns also requested that each university submit current and prior year information on the sources and dollar amounts allocated for funding Alumni Associations as well as the number of financial aid awards and the average dollar amount of those awards.

Arizona State Parks Board - Review of Additional FY 2005 Reservation Surcharge Fund Expenditures – The Committee approved the State Parks Board’s request to increase the FY 2005 expenditures from the Reservations Surcharge Fund by \$151,300 to \$460,300. The increase will be funded with \$141,000 in additional revenues and \$10,300 from the fund balance and would be used to fund 3 FTE positions to assist in taking reservations at Kartchner State Park seven days a week.

Arizona Department of Transportation – Review of Ports of Entry Report – The Committee gave a favorable review to the Arizona Department of Transportation’s (ADOT) report on how the 12 new FTE Positions funded for FY 2005 were distributed among the ports of entry. ADOT indicated that the 12 new FTE Positions were distributed as follows: 3 to Ehrenburg, 2 to Sanders, 3 to San Simon, 2 to Topock, and 2 to Yuma. ADOT also noted that none of the 12 positions have been filled. The Committee’s favorable review included a provision to report to the Committee by August 1, 2005 on several follow-up items.

Department of Emergency and Military Affairs – Report on Homeland Security – The Committee heard testimony on allocation and expenditure plans for homeland security grant monies in FY 2004 and FY 2005. The Office of Homeland Security (OHS) submission report indicated that in Federal Fiscal Year (FFY) 2003, Arizona received a total of \$34.5

million in State Homeland Security Program (SHSGP) funding. Of that total, \$22.3 million was appropriated to local governments and \$12.2 million was distributed among 14 state grantees. Total expenditures have reached \$7.6 million, which represents only 22% of the total.

OHS did not submit information for FFY 2004 because monies have not yet been distributed because the method for distributing monies is changing from specific entities to a regionally based model.

The Committee also requested that OHS submit the following future reports:

- A monthly report on the progress of expanding the remaining FFY 2003 funds
- A monthly report detailing the progress in establishing a new regionally-based funding model
- A FFY 2004 expenditure plan that includes plans for all homeland security grants received by the state and local entities

Arizona Department of Corrections – Report on new Beds and Projects – The Committee heard testimony on the status of several Arizona Department of Corrections (ADC) projects:

- ADC continues to utilize provisional beds in Oklahoma and Texas, filling 1,606 beds of the 2,064 available. The FY 2005 budget assumes that the number of inmates in out-of-state provisional beds will number 664 at fiscal year end.
- The private prison in Kingman opened 472 beds in August and expects another 928 beds to open in April 2005. The FY 2005 budget assumes that 1,400 beds will be open by fiscal year end.
- 1,000 in-state public beds are on-schedule for occupancy in December 2004. The FY 2005 budget assumes that 1,000 beds will be open by January 2005.
- The anticipated contract award date for the 1,000 in-state private beds of July 2004 was moved back to November 2004 to satisfy federal requirements for an environmental assessment. Vendors have estimated a construction timeline of 8 to 12 months after the contract award date. The FY 2005 budget assumes 1,000 beds will be open by June 2005.
- Privatization of inmate stores was scheduled to begin on January 15, 2005, but ADC now expects to award the contract mid to late January 2005 with a start-up date depending on the vendor’s ability to mobilize and begin providing services.
- The Community Accountability Pilot Program is projected to begin by the end of November 2004.

The Committee requested monthly updates on the privatization of inmate stores and the community accountability pilot program.

Department of Economic Security – Report on Child Protective Services Issues – The Committee heard testimony on a report submitted by the Department of Economic Security (DES) on financial and program accountability for Child Protective Services (CPS). The report indicated that:

- The number of caseworkers in training has increased significantly.
- DES did not provide caseloads of CPS caseworkers as required by Chapter 6, so we are unable to evaluate how much progress DES has been made in this regard. As a substitute, DES reports that it has a net staffing need of 101 positions, after adjusting for new positions approved for either the FY 2004 or FY 2005 budget.
- The turnover rate of CPS caseworkers is 19%. Since this data reflects a 6-month period from January to June, we are unable to evaluate progress over time.
- Measures on employee satisfaction and independent assessments of CPS actions will be available in the next 6-month report.

The Committee also requested that future reports include: 1) Actual CPS caseloads per investigator and ongoing case manager and 2) Monthly employee turnover data so as to permit tracking the progress of hiring CPS staff.

Arizona State Schools for the Deaf and Blind – Report on Additional Classroom Site Fund Monies – The Committee heard testimony on how the Arizona State Schools for the Deaf and Blind (ASDB) plans to spend the \$1.2 million increase in Proposition 301 Classroom Site Fund monies. According to ASDB, most of the additional \$1.2 million will be used for base salary and performance-based salary increases totaling \$3,600 per teacher. Remaining monies will be used to fund class size reductions and other maintenance and operation programs.

Department of Juvenile Corrections – Report on Federal Audit Issues – The Committee heard testimony on the progress made since the Department of Justice (DOJ) conducted a federal audit following three youth suicides and reports of sexual abuse in Arizona's juvenile correctional facilities. After audit findings were released, DOJ filed a federal lawsuit against the State. The lawsuit was conditionally dismissed, however, with the stipulation that the Department of Justice can reopen the case if the DJC does not comply to audit findings by the September 15, 2007.

DJC reported that the population is currently 100 juveniles below the FY 2005 budget amount. The Committee asked that DJC provide: 1) an estimate of the current FY 2005 savings from a lower-than-budgeted population, 2) a comparison of the FY 2005 savings to the Department's projection of \$1.9 million in savings from lower population in FY 2006, and 3) its plan for using the population savings in FY 2005 to address some of the remaining federal audit issues.

Department of Health Services/AHCCCS – Report on Health Crisis Fund – The Committee heard an update on expenditures from the Health Crisis Fund. At its August meeting, the Committee heard a report from the Department of Health Services (DHS) on the FY 2004 expenditures from the Health Crisis Fund, including expenditures for education and outreach for both Medicare prescription drug discount cards and the Healthcare Group program.

AHCCCS reports that \$57,056 of the Healthcare Group outreach money has been spent as of September 1, 2004, and that the remaining \$142,944 will be spent by December 2004. In addition, AHCCCS has indicated that it plans to revert the entire \$230,000 Medicare drug discount card outreach because other monies have become available for this purpose. AHCCCS also reports that it will only spend \$300,000 of its base budget for marketing and that the remainder of the base budget (\$800,000) will be used for other administrative costs.

Adoption of Revised Committee Rules and Regulations – The Committee approved the following changes to the Committee rules:

- Add a new requirement for an annual review of the JLBC Staff Director's performance by the Committee.
- Require the full Committee, rather than the Chairman and Vice-Chairman, to set the Director's salary.
- Permit the Chairman to name a subcommittee to make recommendations on the Director's salary.
- Revise the timeline for agencies to submit a request to appear on the JLBC agenda. A request must now be made 2 weeks prior to the meeting. The revision would require agencies to make the request 3 weeks in advance of the meeting. The rules would retain the existing language that allows the Chairman to place an item on the agenda if an agency has not met the submission deadline.

JCCR MEETING

At its October 14 meeting, the Joint Committee on Capital Review considered the following issues:

ADOA Building Renewal – The JCCR favorably reviewed a revised allocation plan for an additional \$366,000 of the \$3.5 million FY 2005 building renewal appropriation from the Capital Outlay Stabilization Fund. Combined with the previously favorably reviewed amount of \$2.3 million, the Committee has favorably reviewed \$2,666,000. The Committee review also included a provision that ADOA submit an allocation plan for the remaining \$834,000 of the \$3.5 million appropriation.

State Parks Lake Improvement Grants – The JCCR favorably reviewed 10 State Lake Improvement Fund (SLIF) grants and projects totaling \$1,468,400. Chairman Pearce also requested that the department provide information on the distribution of SLIF grants by city and county by October 27, 2004.

ADOT Parker Office Relocation – The JCCR favorably reviewed the Parker Motor Vehicle Field Office relocation, and included a provision that the Arizona Department of Transportation (ADOT) report to the Committee on updated expenditure estimates after construction contracts have been signed. ADOT received a \$500,000 appropriation from the State Highway Fund for this project.

ADOT Building Renewal – The JCCR favorably reviewed ADOT's FY 2005 Building Renewal Plan totaling \$2,715,000 from the State Highway Fund and \$65,900 from the State Aviation Fund. The Committee included provisions requiring ADOT to submit information on any allocations from the contingency amount and reallocation between the individual projects in the plan.

U of A La Aldea Student Housing Acquisition – The JCCR favorably reviewed the University of Arizona's (U of A) request for acquisition of La Aldea Student Housing Complex, which is to be financed with a \$21.9 million system revenue bond issuance. The Committee included a provision requiring the U of A to submit for review any changes in scope of the project. The Committee also noted that the favorable review does not constitute an endorsement of the use of a General Fund appropriation to offset any rent collection that may be required for debt service.

The JCCR also received a report on the reallocation of \$0.2 million from the \$1.3 million in the contingency allocation to remove undocumented underground utilities. The total project budget of \$46.1 million remains unchanged.

NAU Bond Projects – The JCCR favorably reviewed \$4.4 million of a \$15 million system revenue bond issuance request by Northern Arizona University (NAU) for cost and scope changes to the School of Communication renovation, the School of Engineering and Technology renovation, and the new College of Business Administration. NAU plans to request appropriations for debt service on the 30-year bonds, and plans to use tuition collections if appropriations are not authorized. The review included provisions noting that a favorable review did not constitute endorsement of General Fund appropriations for debt service or operating cost, and requiring reporting on the use of contingency allocations. The Committee also expressed its concern that such major scope changes were not anticipated in the original scope of the projects.

NAU System Revenue Bond – The JCCR favorably reviewed \$10.6 million of a \$15 million system revenue bond issuance for Building System Repair and Replacement and Wayfinding/Landscaping Infrastructure. NAU plans to request appropriations for debt service on the 30-year bonds, and plans to use tuition collections if appropriations are not authorized. The review included provisions noting that a favorable review did not constitute endorsement of General Fund appropriations for debt service or operating cost, requiring reporting on the use of contingency allocations, and that NAU should not use bonding to finance projects whose typical life span is less than the bond repayment period.

School Facilities Board Lease to Own Projects – The JCCR favorably reviewed \$50 million in potential new school construction projects financed through lease-purchase agreements, as well as a revised list of projects associated with previously reviewed \$200 million lease-purchase.

Chairman Pearce also requested the School Facilities Board (SFB) provide by October 27, 2004 information related to costs and status of the Qwest contract.

School Facilities Board Building Renewal – The JCCR favorably reviewed the proposed distribution of \$70 million of Building Renewal Allocation Fund monies for FY 2005.

Department of Public Safety Remote Housing – The JCCR favorably reviewed the remote officer housing projects in Ajo and Seligman, with an estimated cost of \$355,700. Chairman Pearce asked the department to provide by October 27, 2004, information regarding whether the assignment of officers to remote locations based on marital status might generate savings.

ASU Scottsdale Center for New Technology and Innovation (Los Arcos) – The JCCR reviewed a report on the proposed development of the new center by the Arizona State University (ASU) Foundation. Committee discussion focused on the role ASU would take in the project and whether there could be any financial liability for ASU and state in the future. Given that the development is still in the preliminary stages, the role of ASU is not yet defined.

Adoption of Revised Committee Rules – The Committee adopted a change to Rule 8, which sets the timeline for agencies to request to appear on the JCCR agenda. Previously, a request was required 2 weeks prior to the meeting. The adopted change would require agencies to make the request 3 weeks prior to the meeting.