FY 2014 JLBC Baseline
Summary Version
January 18, 2013
Positive Budget Developments

- Arizona economy continues in recovery mode, albeit at a slow pace
- Legislature required to provide 3-year projection in its annual budget bill
  - Does not require individual FY ’15 and ’16 agency budgets, but does require state to set out-year targets
- FY ’13 budget established reserves of $450 M
  - Represents 5.5% of budget – statutory cap is 7%
  - Not intended to be used for ongoing programs
Forecast Risks

- Uncertain economy in 0% interest rate environment
- Unknown outcome of Federal Fiscal Cliff 2
- Unpredictable disaster – environmental or political
- Budget litigation
- A 3-year forecast comes with risks – a 1% change would affect the balance by $500 M in the third year
2 Factors Influencing Budget Outlook through ’16

- How much revenue forecast risk in an uncertain economic environment?

- How much discretionary spending above the Baseline?
Baseline Balances Represent Available Resources After Fulfilling Mandates

- **Consensus revenue**
  - 3-year annual 5.7% base growth – excluding tax changes
  - Loss of $(924) M 1-cent sales tax
  - $(283) M in enacted tax reductions by FY ’16
  - 65% probability of reaching forecast

- **Statutory spending**
  - Growth required by statute – primarily K-12 and Medicaid
  - Adds $157 M in FY ’14 and $701 M by FY ‘16
## FY ’14 – FY ’16 Baseline Revenue Changes

<table>
<thead>
<tr>
<th>Description</th>
<th>FY ’14 Above ’13</th>
<th>FY ’15 Above ’14</th>
<th>FY ’16 Above ’15</th>
</tr>
</thead>
<tbody>
<tr>
<td>Base Revenue Growth (4.9%/5.9%/6.2%)</td>
<td>416</td>
<td>526</td>
<td>575</td>
</tr>
<tr>
<td>TPT 1 ¢ Expires</td>
<td>(924)</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>Elimination of Fund Transfers</td>
<td>(90)</td>
<td>(6)</td>
<td>--</td>
</tr>
<tr>
<td>One-Time FY ’13 Revenue Loss 1/</td>
<td>52</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>Previously Enacted Tax Legislation</td>
<td>(47)</td>
<td>(134)</td>
<td>(108)</td>
</tr>
<tr>
<td>Urban Revenue Sharing</td>
<td>(45)</td>
<td>(28)</td>
<td>(35)</td>
</tr>
<tr>
<td>Change In Beginning Balance 2/</td>
<td>254</td>
<td>(341)</td>
<td>(285)</td>
</tr>
<tr>
<td>Additional Revenues</td>
<td>(384)</td>
<td>17</td>
<td>147</td>
</tr>
<tr>
<td><strong>Total Resources</strong></td>
<td><strong>8,979</strong></td>
<td><strong>8,996</strong></td>
<td><strong>9,143</strong></td>
</tr>
</tbody>
</table>

1/ TPT early payment threshold  
2/ Beginning balances: FY ’13, $397 M; FY ’14, $651 M; FY ’15, $310 M; FY ’16, $25 M
## FY ’14 – FY ‘16 Baseline Spending Changes

<table>
<thead>
<tr>
<th></th>
<th>General Fund - $ in Millions</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>FY ’14 Above ’13</td>
</tr>
<tr>
<td>K-12 Formula</td>
<td>55</td>
</tr>
<tr>
<td>Medicaid Formula (prior to expansion)</td>
<td>(97)</td>
</tr>
<tr>
<td>Medicaid Mandatory Expansion</td>
<td>74</td>
</tr>
<tr>
<td>One-Time FY ’13 Caseload Savings</td>
<td>76</td>
</tr>
<tr>
<td>ADC Operating – phase-in approved beds</td>
<td>9</td>
</tr>
<tr>
<td>Debt Service</td>
<td>20</td>
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<tr>
<td>Land Department Fund Source</td>
<td>11</td>
</tr>
<tr>
<td>Other</td>
<td>9</td>
</tr>
<tr>
<td><strong>Additional Spending</strong> (excludes Rainy Day)</td>
<td><strong>157</strong></td>
</tr>
<tr>
<td>Total Spending</td>
<td>8,669</td>
</tr>
</tbody>
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## FY ’14 – ’16 Baseline Projections

<table>
<thead>
<tr>
<th></th>
<th>‘13</th>
<th>‘14</th>
<th>‘15</th>
<th>‘16</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance Forward</td>
<td>$397 M</td>
<td>$651 M</td>
<td>$310 M</td>
<td>$25 M</td>
</tr>
<tr>
<td>Revenues</td>
<td>$9.0 B</td>
<td>$8.3 B</td>
<td>$8.7 B</td>
<td>$9.1 B</td>
</tr>
<tr>
<td>Spending</td>
<td>$8.7 B (^1/)</td>
<td>$8.7 B</td>
<td>$9.0 B</td>
<td>$9.2 B</td>
</tr>
<tr>
<td>Ending Balance</td>
<td>$651 M</td>
<td>$310 M</td>
<td>$25 M</td>
<td>$(70) M</td>
</tr>
</tbody>
</table>

- After statutory spending, effectively no money remains for discretionary spending without increasing out-year shortfall
- Excludes impact of K-12 inflation court ruling – would add a new $80 M+ to budget each year. If funded, would result in $(223) M FY ’15 shortfall and $(346) M FY ’16 shortfall
- $450 M Rainy Day Fund available to offset shortfalls

\(^1/\) $8.5 billion after adjusting for Rainy Day Fund deposit
JLBC Baseline Revenues Compared to Expenditures
- If No Discretionary Spending – Small FY ’16 Shortfall
JLBC Baseline Adjusted for K-12 Inflation Ruling
- Every Extra $1 Spent in ’14 Increases ’16 Shortfall by $3
Budget Concerns

- Arizona has third lowest credit rating among states
- Budget has ongoing structural shortfalls – permanent revenues less than spending
- State still suspends $678 M in annual formula spending – if funded, would worsen structural gap
JLBC Staff Suggested Process Improvements

1) Strengthen independent review of K-12 automation
2) Confirm school district charter conversion policy
3) Enhance K-12 override/bonding reporting
4) Increase CPS funding oversight – 45% of $ are non-appropriated
5) Specify intent of 1,500 authorized prison beds – supplant or supplement temporary beds?
6) Establish expectation of university performance measures – can they be used to determine total funding?
7) Improve accounting of 1-time monies – April ’13 investment income windfall
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