

# FY 2022 BASELINE SUMMARY

## Overview

The FY 2022 Baseline provides an estimate of the state's General Fund balances. The revenue projections reflect 2 different economic forecasts while the spending estimates represent active funding formula requirements and other obligations. The Baseline does not represent a budget proposal, but an estimate of available resources after statutory requirements.

The JLBC Baseline parameters are as follows:

- Projected FY 2022 revenues range from \$13.9 billion and \$14.3 billion:
  - ⇒ The lower end of the range represents the 4-sector estimate, including 2 University of Arizona econometric models, the Finance Advisory Committee panelists, and the JLBC Staff. The higher end of the range reflects just the JLBC Staff sector.
  - ⇒ The primary difference in the 2 forecasts revolves around FY 2021. After adjusting for the income tax deferral at the beginning of FY 2021, year-to-date revenue growth is 8.6%. To achieve the 4-sector forecast, revenues would have to decline (3.6)% for the remainder of this year. Revenues would grow by 1.3% under the JLBC Staff forecast.
  - ⇒ Given the year-to-date growth, the 4-sector forecast appears to be unrealistically low.
- FY 2022 General Fund Baseline spending is projected to be \$12.3 billion, an increase of \$602 million, or 5.1%, above FY 2021. This increase consists of:
  - ⇒ A \$729 million increase in ongoing spending.
  - ⇒ A \$(127) million decrease in one-time spending.
- Compared to the original FY 2021 budget, the revised FY 2021 Baseline spending level would decline by \$(298) million for federal Medicaid match rate savings and a \$(301) million reduction due to lower K-12 enrollment.
- The FY 2022 cash balance is projected to be between \$1.6 billion and \$2.0 billion. This amount is in addition to nearly \$1 billion available in the Budget Stabilization Fund (BSF) by the end of FY 2022.
- Under the Baseline projections, the Legislature would have the ability to dedicate \$300 million to \$400 million of the balance to ongoing initiatives without creating a shortfall through the 3-year planning period.
- The remaining \$1.3 billion to \$1.6 billion of the Baseline balance would be available for one-time purposes.

These estimates likely overstate the level of available resources in the FY 2022 budget. Some of the one-time spending in the FY 2021 budget has been labeled as such in the last 4 budgets. School facility building renewal grants (\$91 million) and the state employee health insurance subsidy (\$22 million) fall into this category.

## FY 2021

The FY 2021 budget is currently projected to have a \$1.5 billion to \$1.8 billion balance. Relative to the JLBC Staff forecast, this is an increase of \$1.1 billion from the enacted March budget. The net \$1.1 billion increase has 4 primary components:

- Higher revenue of \$600 million, almost entirely due to the deferral of income tax filing deadline from April 15 to July 15, 2020. After adjusting for this factor, the current FY 2021 revenue forecast is comparable to the enacted March budget.
- The carryover balance from FY 2020 to FY 2021 is \$(190) million less than anticipated in the enacted March budget.
- FY 2021 K-12 spending is projected to be \$(300) million less than the appropriation due to lower school enrollment.
- FY 2021 Medicaid spending is forecast to be \$(300) million less than budgeted due to a temporary higher federal match rate.

## FY 2022 Baseline Revenues

Total FY 2022 revenue collections would be \$13.9 billion to \$14.3 billion. Beyond overall forecast assumptions outlined above, other adjustments are:

- The state set-aside for urban revenue sharing formula distributions would decrease from \$828 million to \$756 million, thereby increasing state revenue by \$72 million.
- Repayment of a deposit for groundwater infrastructure required in the FY 2020 budget increases one-time revenues by \$20 million.
- Legislation enacted prior to the 2021 Regular Session is estimated to reduce ongoing revenue by \$(40) million.

Conformity with federal 2020 tax legislation would cost over \$500 million. The Baseline does not assume conformity as the JLBC Staff standard practice is to have the Legislature confirm with any new federal tax provisions before incorporating those changes into the Baseline.

**FY 2022 Baseline Spending**

Based on statutory funding formulas and other obligations, FY 2022 Baseline spending is projected to increase by 5.1% to \$12.3 billion, or \$602 million more than FY 2021 expenditures. The major adjustments are:

- Arizona Department of Education (ADE) formula spending would have a net increase of \$239 million due to 0.6% growth in student enrollment and a 1.2% inflation factor. The spending increase also includes the last step in returning to full funding of Additional Assistance as required by past budget plans. These growth factors would be partially offset by savings associated with higher K-12 property tax collections. These estimates do not account for changes in student enrollment associated with the COVID-19 pandemic.
- AHCCCS formula spending would grow by \$223 million, reflecting flat caseload growth for most populations, a 3.0% capitation rate increase. The increase does not presume that COVID-related enhanced federal match continues into FY 2022.
- The Department of Economic Security (DES) budget would increase by \$89 million, entirely for Developmental Disabilities Medicaid growth, reflecting 5.0% enrollment growth and a 3.0% capitation rate increase.
- Arizona Department of Corrections (ADC) spending is unchanged from FY 2020.
- University spending would increase by \$495,600 for adjustments to capital appropriations. Universities would also receive \$21 million in one-time monies for the cost of a 27<sup>th</sup> pay period in FY 2022.
- Community College spending would increase by \$1.8 million for formula growth.
- School Facilities Board funding would be reduced by \$(74) million, reflecting the elimination of \$(91) million of one-time building renewal monies offset by a \$17 million increase in new school construction costs. The Baseline includes a total of \$76 million for new construction, including \$12 million for the second and final year of FY 2021 authorizations and \$64 million for the first year of 5 new FY 2022 authorizations.
- Department of Public Safety spending would increase by \$161 million to backfill the lost revenues from the current-law repeal of the Highway Safety Fee effective June 2021.
- Agency budgets would be reduced by \$(65) million statewide to eliminate a one-time \$22 million state employer health insurance increase and a \$43 million increase for the non-University costs of a 27<sup>th</sup> pay period in FY 2021.

The \$12.3 billion spending level would support a Full-Time Equivalent (FTE) Position ceiling of 53,620.4 state employees from both General Fund and Other Appropriated Funds.

**Long-Term General Fund Estimates**

A.R.S. § 35-125 requires the annual General Appropriation Act to include 3-year revenue and expenditure projections. To assist in this effort, the JLBC Staff has developed General Fund Baseline estimates through FY 2024, as shown on page S-5. Based on the assumptions described below and depending on the forecast used, the Baseline ending balance is estimated to be \$232 million to \$323 million in FY 2023 and \$521 million to \$617 million in FY 2024. These figures assume that the \$1.6 billion to \$2.0 billion in the estimated FY 2022 ending balance is completely allocated.

These estimates exclude the Budget Stabilization Fund (BSF) monies. The BSF is estimated to have a fund balance of \$993 million by the end of FY 2022.

## Other Fiscal Challenges

There are both positive and negative risks to the JLBC Baseline revenue estimates:

- *Continued Threat from COVID-19:* The general assessment in the forecasting profession is the continued threat from the pandemic. In recent weeks, there has been a significant upturn in new cases of infections, hospitalizations and deaths, all of which could result in the reintroduction of measures aimed at containing the spread of the virus. The introduction of vaccines may stem the increase in cases, however. Consumer confidence may hinge on how quickly the number of cases, hospitalizations and deaths reverse course.
- *Federal Response to COVID-19:* In December 2020, the federal government passed the 2021 Consolidated Appropriations Act which will spend more than \$900 billion to address economic and health issues created by the pandemic. This should provide additional assistance to the economy through early spring. Many of the provisions, such as for Unemployment Insurance, will only last through early spring; if the pandemic continues to have a significant dampening effect on consumer confidence, additional federal response may further affect economic recovery.
- *Current Strong Revenue Growth:* As of now, however, Arizona's economy and its revenue growth are still strong compared to other states. The state ranks third overall in the country in terms of its economic momentum (personal income, population, and employment growth). While Arizona's revenues declined by (1.6)% in FY 2020, that amount would have been positive were it not for the deferral of income tax filing from April 15 to July 15, 2020. The 17.8% growth year-to-date in FY 2021 (8.6% after adjusting for the deferral of income tax filing) indicates revenues are still strong.

Because small percent changes in growth assumptions can have a substantial impact – over 3 years, a 1% change in revenue growth could change available revenues by \$750 million through FY 2024 – these risks could significantly change the final results of these budgets.

The state also faces ongoing litigation that may impact budgets such as:

- The K-12 Capital Funding litigation in Maricopa Superior Court.
- Litigation against the Department of Child Safety in United States District Court.
- Litigation against the Arizona Department of Corrections in United States District Court regarding inmate health care.

## Debt

At the end of FY 2022, the state's projected level of lease-purchase and bonding obligations will be \$6.1 billion. The associated annual debt service payment is \$748 million.

Of the \$6.1 billion in total obligations, the General Fund share is \$1.2 billion. The General Fund annual debt service is projected to be \$228 million in FY 2022 (*see the Debt and Lease-Purchase Financing section of the Capital Outlay narrative for additional information*).

As a remnant of the Great Recession, the state also pays \$931 million of current year K-12 obligations in the next year (the "rollover"). The Baseline reduces this amount to \$901 million pursuant to a decision in the FY 2020 budget's 3-year spending plan. The \$6.1 billion estimate of total obligations also does not include any unfunded retirement liability.

Arizona's current debt rating from Moody's is Aa1, which represents Moody's second-highest credit rating. Arizona's rating with Standard & Poor's is AA, which represents Standard & Poor's third-highest credit rating.

## Other Funds

Besides the General Fund, the state has dedicated special revenue funds. Only a portion of these monies is subject to legislative appropriation. The Baseline includes a FY 2022 Other Fund appropriated spending level of \$4.3 billion, or (3.5)% below FY 2021.

The level of FY 2022 non-appropriated state funds is expected to be \$11.3 billion, while non-appropriated Federal Funds are forecast to be \$22.1 billion. When all appropriated and non-appropriated fund sources are combined, total FY 2022 state spending would be \$50.0 billion.

**STATEMENT OF GENERAL FUND REVENUES AND EXPENDITURES  
WITH ONE-TIME FINANCING SOURCES**

**JLBC STAFF FORECAST**

	<b>FY 2021 Baseline JLBC Forecast</b>	<b>FY 2022 Baseline JLBC Forecast</b>	<b>FY 2023 Baseline JLBC Forecast</b>	<b>FY 2024 Baseline JLBC Forecast</b>
<b>REVENUES</b>				
Ongoing Revenues	\$13,321,390,400	\$13,264,774,500	\$13,848,405,600	\$14,448,918,800
Urban Revenue Sharing	(828,492,900)	(756,391,100)	(948,581,500)	(907,536,900)
Net Ongoing Revenues	<u>\$12,492,897,500</u>	<u>\$12,508,383,400</u>	<u>\$12,899,824,100</u>	<u>\$13,541,381,900</u>
One-time Financing Sources				
Balance Forward	\$372,457,000	\$1,776,502,000		
Water Infrastructure Repayment		20,000,000		
Other Fund Transfers	16,700,000	16,700,000	16,700,000	16,700,000
Subtotal One-time Revenues	<u>\$389,157,000</u>	<u>\$1,813,202,000</u>	<u>\$16,700,000</u>	<u>\$16,700,000</u>
<b>Total Revenues</b>	\$12,882,054,500	\$14,321,585,400	\$12,916,524,100	\$13,558,081,900
<b>EXPENDITURES</b>				
Ongoing Operating Appropriations	\$11,469,755,900	\$12,176,255,300	\$12,582,627,900	\$12,939,813,700
Administrative Adjustments	55,000,000	120,000,000	162,000,000	162,000,000
Revertments	(150,000,000)	(192,000,000)	(198,000,000)	(198,000,000)
Subtotal Ongoing Expenditures	<u>\$11,374,755,900</u>	<u>\$12,104,255,300</u>	<u>\$12,546,627,900</u>	<u>\$12,903,813,700</u>
One-time Expenditures				
Capital Outlay	\$11,000,000			
Reduce K-12 Rollover (Enacted)		30,000,000		
Operating One-Time Spending	275,373,600	152,015,300	46,402,500	37,427,000
AHCCCS/DES/DCS One-Time FMAP Savings <u>1/</u>	(297,940,800)			
ADE One-Time Enrollment Savings <u>2/</u>	(300,714,800)			
27th Pay Period (Enacted)	43,078,600	20,052,100		
Subtotal One-time Expenditures	<u>(\$269,203,400)</u>	<u>\$202,067,400</u>	<u>\$46,402,500</u>	<u>\$37,427,000</u>
<b>Total Expenditures</b>	\$11,105,552,500	\$12,306,322,700	\$12,593,030,400	\$12,941,240,700
<b>Ending Balance <u>3/</u></b>	<u>\$1,776,502,000</u>	<u>\$2,015,262,700 <u>5/</u></u>	<u>\$323,493,700</u>	<u>\$616,841,200</u>
<b>Ongoing Balance <u>4/</u></b>	<u>\$1,118,141,600</u>	<u>\$404,128,100</u>	<u>\$353,196,200</u>	<u>\$637,568,200</u>

1/ The federal Families First Coronavirus Response Act temporarily increases the regular Medicaid match rate by 6.2% retroactive to January 1, 2020, through the last quarter that the federal public health emergency is in effect. This amount reflects savings associated with the enhanced match rate for AHCCCS/DES/DCS, net of costs from increased caseload growth from the pandemic.

2/ This amount reflects the savings associated with lower-than-budgeted Basic State Aid expenses in FY 2021. The ex-appropriation would permit the Legislature to either return these monies to the General Fund or to redirect them into the school system through other adjustments.

3/ This calculation reflects the difference between total revenues and total expenditures. Excludes any Budget Stabilization Fund balance.

4/ This calculation reflects the difference between ongoing revenues and ongoing expenditures and excludes one-time adjustments. The Legislature makes the ongoing and one-time classifications as part of its 3-year spending plan. Excludes any Budget Stabilization Fund balance.

5/ The FY 2022 cash balance is presumed to be allocated as part of the FY 2022 budget process.

**STATEMENT OF GENERAL FUND REVENUES AND EXPENDITURES  
WITH ONE-TIME FINANCING SOURCES**

**4-SECTOR FORECAST**

	FY 2021 Baseline <u>4-Sector Forecast</u>	FY 2022 Baseline <u>4-Sector Forecast</u>	FY 2023 Baseline <u>4-Sector Forecast</u>	FY 2024 Baseline <u>4-Sector Forecast</u>
<b>REVENUES</b>				
Ongoing Revenues	\$13,020,834,800	\$13,116,515,000	\$13,721,972,000	\$14,337,921,400
Urban Revenue Sharing	(828,492,900)	(756,391,100)	(913,624,900)	(892,048,900)
Net Ongoing Revenues	<u>\$12,192,341,900</u>	<u>\$12,360,123,900</u>	<u>\$12,808,347,100</u>	<u>\$13,445,872,500</u>
One-time Financing Sources				
Balance Forward	\$372,457,000	\$1,475,946,400		
Water Infrastructure Repayment		20,000,000		
Other Fund Transfers	16,700,000	16,700,000	16,700,000	16,700,000
Subtotal One-time Revenues	<u>\$389,157,000</u>	<u>\$1,512,646,400</u>	<u>\$16,700,000</u>	<u>\$16,700,000</u>
<b>Total Revenues</b>	<b>\$12,581,498,900</b>	<b>\$13,872,770,300</b>	<b>\$12,825,047,100</b>	<b>\$13,462,572,500</b>
<b>EXPENDITURES</b>				
Ongoing Operating Appropriations	\$11,469,755,900	\$12,176,255,300	\$12,582,627,900	\$12,939,813,700
Administrative Adjustments	55,000,000	120,000,000	162,000,000	162,000,000
Revertments	(150,000,000)	(192,000,000)	(198,000,000)	(198,000,000)
Subtotal Ongoing Expenditures	<u>\$11,374,755,900</u>	<u>\$12,104,255,300</u>	<u>\$12,546,627,900</u>	<u>\$12,903,813,700</u>
One-time Expenditures				
Capital Outlay	\$11,000,000			
Reduce K-12 Rollover (Enacted)		30,000,000		
Operating One-Time Spending	275,373,600	152,015,300	46,402,500	37,427,000
AHCCCS/DES/DCS One-Time FMAP Savings <sup>1/</sup>	(297,940,800)			
ADE One-Time Enrollment Savings <sup>2/</sup>	(300,714,800)			
27th Pay Period (Enacted)	43,078,600	20,052,100		
Subtotal One-time Expenditures	<u>(\$269,203,400)</u>	<u>\$202,067,400</u>	<u>\$46,402,500</u>	<u>\$37,427,000</u>
<b>Total Expenditures</b>	<b>\$11,105,552,500</b>	<b>\$12,306,322,700</b>	<b>\$12,593,030,400</b>	<b>\$12,941,240,700</b>
<b>Ending Balance <sup>3/</sup></b>	<u><u>\$1,475,946,400</u></u>	<u><u>\$1,566,447,600</u></u> <sup>5/</sup>	<u><u>\$232,016,700</u></u>	<u><u>\$521,331,800</u></u>
<b>Ongoing Balance <sup>4/</sup></b>	<u><u>\$817,586,000</u></u>	<u><u>\$255,868,600</u></u>	<u><u>\$261,719,200</u></u>	<u><u>\$542,058,800</u></u>

<sup>1/</sup> The federal Families First Coronavirus Response Act temporarily increases the regular Medicaid match rate by 6.2% retroactive to January 1, 2020, through the last quarter that the federal public health emergency is in effect. This amount reflects savings associated with the enhanced match rate for AHCCCS/DES/DCS, net of costs from increased caseload growth from the pandemic.

<sup>2/</sup> This amount reflects the savings associated with lower-than-budgeted Basic State Aid expenses in FY 2021. The ex-appropriation would permit the Legislature to either return these monies to the General Fund or to redirect them into the school system through other adjustments.

<sup>3/</sup> This calculation reflects the difference between total revenues and total expenditures. Excludes any Budget Stabilization Fund balance.

<sup>4/</sup> This calculation reflects the difference between ongoing revenues and ongoing expenditures and excludes one-time adjustments. The Legislature makes the ongoing and one-time classifications as part of its 3-year spending plan. Excludes any Budget Stabilization Fund balance.

<sup>5/</sup> The FY 2022 cash balance is presumed to be allocated as part of the FY 2022 budget process.