
Summary of FY 2015 Year-End Impacts

Revised
August 20, 2015

JLBC

Summary of FY 2015 Year-End Impacts

- ❑ Based on preliminary estimates, '15 General Fund revenues were \$381 M above forecast.
- ❑ Gains driven by Individual Income capital gains tax receipts along with Corporate collections.
- ❑ Compared to these 2 volatile revenue sources, the state's core sales and withholding revenues grew much more modestly.
- ❑ While book closing normally takes 6 months, the early results are even more tentative this year due to implementation of the state's new accounting system on July 1.

Updated Ending Balance Estimates

- ❑ Given higher revenues and lower spending, a projected \$(132) M shortfall is now a \$325 M balance at the end of '15. As a result, no Rainy Day Fund transfer will be needed.
- ❑ The '15 results create a larger beginning balance for '16. As a result, a budgeted \$(35) M shortfall turns into a \$278 M balance by the end of '16.
- ❑ These are one-time monies and would not support permanent initiatives.

One-time Ending Balance Resources

	(\$ in M)	
	<u>'15</u>	<u>'16</u>
Budgeted	\$(132)	\$(35)
Preliminary Re-estimate	\$325	\$278

- The enacted '15 budget had an estimated \$(132) million shortfall.
- The budget filled that gap with a Budget Stabilization Fund (Rainy Day) transfer.
- Given uncertainty about shortfall, BSF transfer was allowed to fluctuate so as to produce a \$12 million balance.
- Given added revenues, however, BSF transfer will not occur.
- BSF balance will remain \$460 M.

Possible Ongoing Revenues

- ❑ The higher '15 revenue base likely to result in higher '16 collections and result in some permanent gain in state resources.
- ❑ Given the volatile sources of the revenue windfall, the potential ongoing gain is still being evaluated and will be addressed at the October FAC meeting.
- ❑ As a very early estimate, at least \$250 M of the \$381 M overage is likely to continue into '16 and beyond.
- ❑ An ultimate ruling in favor of K-12 inflation plaintiffs could cost over \$250 M and offset the potential revenue gain.

'15 Revenue Above Forecast in 3 Main Categories

- Includes Statutory Revenue Changes

	<u>'15 Budget Above '14</u>	<u>'15 Above '14</u>	<u>\$ Above Forecast</u>
Sales	3.1%	4.7%	\$63 M
Individual Income	2.3%	8.6%	\$219 M
Corporate Income	(0.8)%	15.3%	\$93 M

- ❑ Overall '15 net revenue growth was 6.1%
- ❑ '15 revenues were \$381 M above forecast

Individual Income Tax Growth

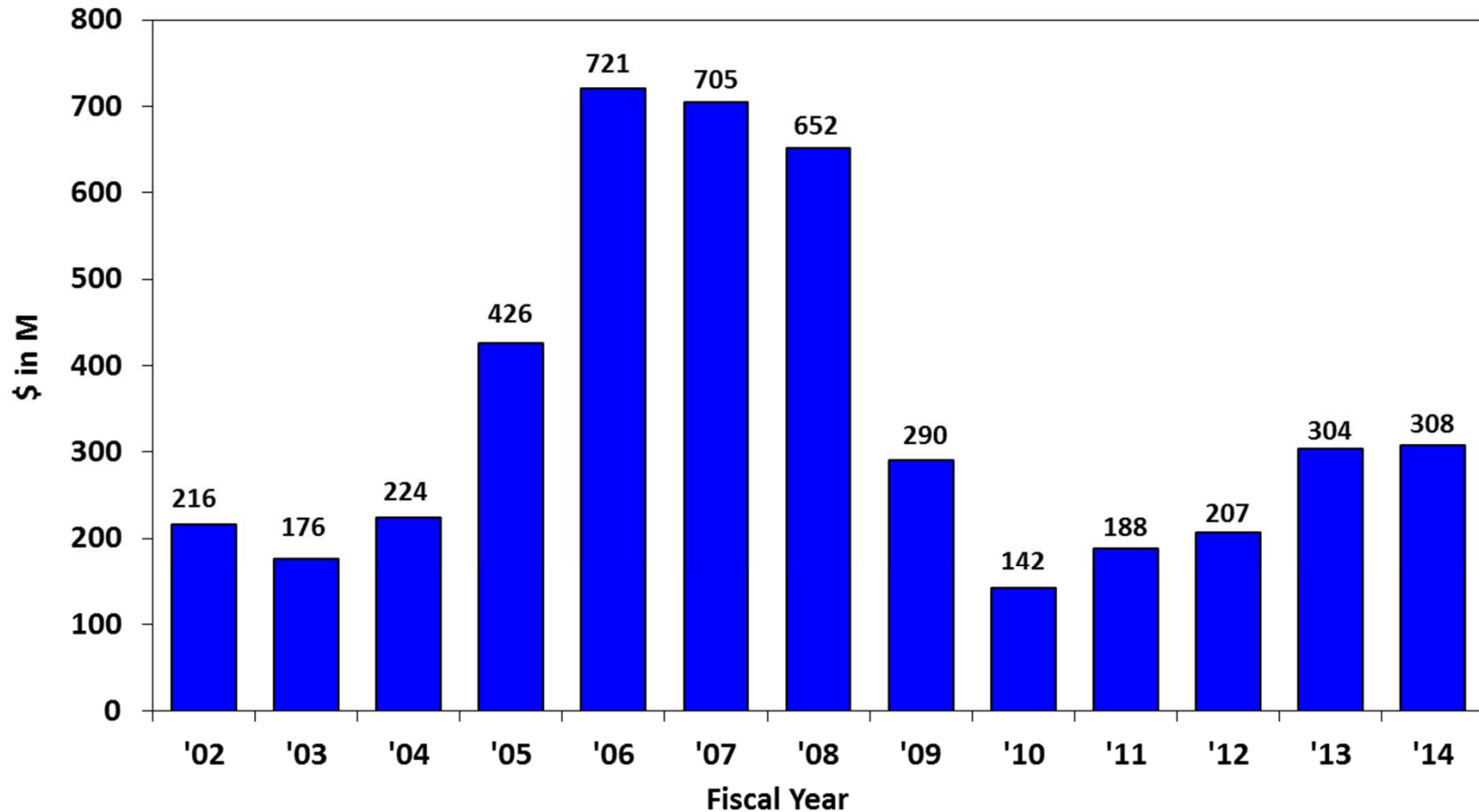
- \$219 M Forecast Overage Likely Fueled by Capital Gains

	<u>'14</u>	<u>'15</u>
Withholding	3.4%	3.4%
Payments	(3.4)%	14.8%
Refunds	1.1%	(0.8)%
Net	<u>1.9%</u>	<u>8.6%</u>

- ❑ Withholding growth remains sluggish at 3.4%
- ❑ Annual withholding growth has not been above 3.5% since '11
- ❑ 14.8% payment growth likely driven by capital gains
- ❑ Stock market growth of 19.2% in CY 13 and 17.5% in CY 14 helped generate payment increase

Volatility of Capital Gains Complicate Forecasting

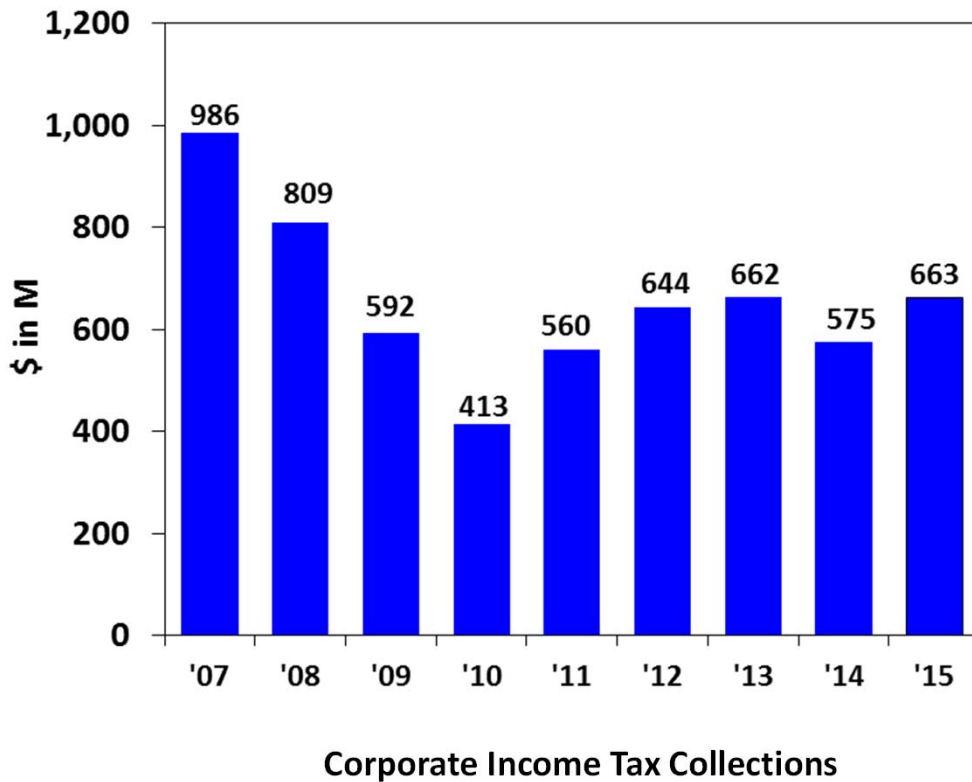
- Final '15 Capital Gain Receipts to be Determined – May Not be Ongoing



Individual Income Tax Capital Gains Revenue

Corporate Gains May Also Not Be Sustainable

- Past History of Significant Revenue Shifts



- ❑ Corporate net gain of 15.3% was unexpected.
 - \$93 M above forecast
- ❑ National corporate profits increased by 4.6% in CY '13 and 8.3% in CY '14.
- ❑ Forecast overage likely caused by delay in filing for \$72 M in tax cuts.

Corporate Filing Pattern Delayed Impact of Reduction

- ❑ The 4-year phase in of corporate tax reductions began with Tax Year 2014 at estimated '15 cost of \$72 M
- ❑ If a company's tax year began in January 2014, it would file taxes in April 2015
- ❑ Based on further research, however, many large corporations file a 6-month extension (October 2015)
- ❑ As a result, the primary impact of the initial corporate reductions likely delayed until '16
- ❑ As a result, '15 corporate receipts higher than forecast

Enacted Budget Estimates

	'15	'16	'17	'18
Balance Forward	\$577 M	\$12 M	\$0 M	\$0 M
Revenues	\$8.63 B	\$9.09 B	\$9.24 B	\$9.51 B
Rainy Day Transfer	\$144 M	\$0 M	\$0 M	\$0 M
Spending	\$9.34 B	\$9.13 B	\$9.29 B	\$9.52 B
Ending Balance	\$12 M	\$(35) M	\$(50) M	\$(8) M

- ☐ Represents enacted budget estimates from Regular Session

Impact of Year-End Data on '15 and '16

	'15		'16	
	Budget	Actual	Budget	Revised
Balance Forward	\$577 M	\$577 M	\$12 M	\$325 M
Revenues	\$8.63 B	\$9.01 B	\$9.09 B	\$9.09 B
BSF	\$144 M	\$0 M	\$0 M	\$0 M
Spending	\$9.34 B	\$9.26 M	\$9.13 B	\$9.13 M
Ending Balance	\$12 M	\$325 M	\$(35) M	\$278 M

- ❑ Higher '15 ending balance improves '16 ending balance as well
- ❑ '15 spending \$(76) M less than projected – but some may be shifted to '16 due to implementation of new accounting system
- ❑ Does not include impact of ongoing revenue gain or possible K-12 inflation ruling

Status of K-12 Inflation Litigation

- ❑ In '09 – '13, State did not fully inflate K-12 formula
- ❑ AZ Supreme Court has ruled that full inflation is required
- ❑ In response, State fully inflated in '14 and '15, but made no retroactive adjustments.
- ❑ Case returned to Superior Court to determine whether other adjustments are required

What Is Potential Cost of K-12 Litigation?

- ❑ In July 2014, Superior Court concurred with plaintiffs' request to reset the formula for foregone inflation
 - "Reset" would cost \$336 M in '16

- ❑ '16 Budget included \$74 M in added inflation
 - If these monies are taken into account, net cost of ruling would be \$262 M

- ❑ Timetable for resolution of case is unclear

More Background

- [July Monthly Fiscal Highlights](#)
- [August Monthly Fiscal Highlights](#)