

The Arizona Budget

The One Cent Sales Tax Proposal:
Where it came from and what it
means

Acknowledgements/Disclaimer

- This presentation was prepared by Peter Burns of Burns & Associates, Inc. and delivered to Project Civil Discourse on May 6, 2010
- The presentation is based on materials obtained from the Governor's Office of Strategic Planning and Budgeting (OSPB)
- Burns & Associates is grateful to OSPB for the use of their materials but is solely responsible for any errors, omissions or inaccuracy contained herein
- Comments on the presentation may be forwarded to pburns@burnshealthpolicy.com

Tonight's Topics

- How bad was it?
- What did “they” do?
- Why were these actions taken?
- What are the prospects?

HOW BAD WAS
IT?

How Bad Was It?

Current Year – FY 2010 – Deficit

- In January anticipated to be \$1.4 billion
- \$480 million left over from FY 2009

The \$1.4 billion deficit was approximately:

- 46% of the General Fund revenues anticipated for the rest of the year
- 36% of the remaining General Fund appropriations for the fiscal year

As of January, four Legislative sessions had addressed the problem

How Bad Was It?

Budget Year – FY 2011 - Deficit

In January, anticipated to be \$3.2 billion

The \$3.2 billion deficit was approximately:

- 47% of anticipated General Fund revenues
- 33% of the General Fund “continuation” budget for FY 2011.

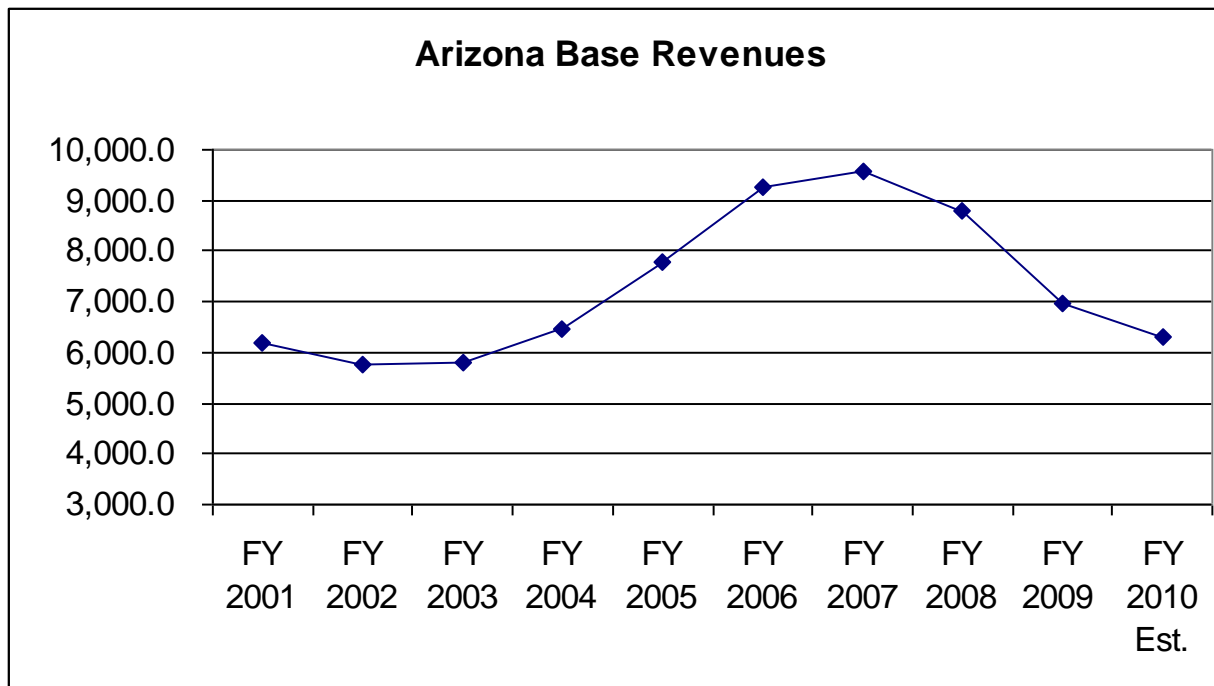
How Bad Was It?

Reduced Revenues

- Before the recession
 - A series of tax cuts in personal income and corporate income taxes.
- When the recession hit
 - Since FY 2007 Sales (TPT) Tax down 22%
 - Since FY 2007 Personal Income Tax down 38%
 - Since FY 2007 Corporate Income Tax down 57%

How Bad Was It?

State tax revenues have declined 34 percent in three years.



How Bad Was It?

Added Spending

- Before the recession
 - The State took on major expenditure programs without any adjustments to revenues, e.g. property tax reform shifted the support of the cost of K-12 to the General Fund; courts forced responsibility for building and maintaining school facilities; voter initiative expanded AHCCCS
- When the recession hit
 - Major increases in the AHCCCS population

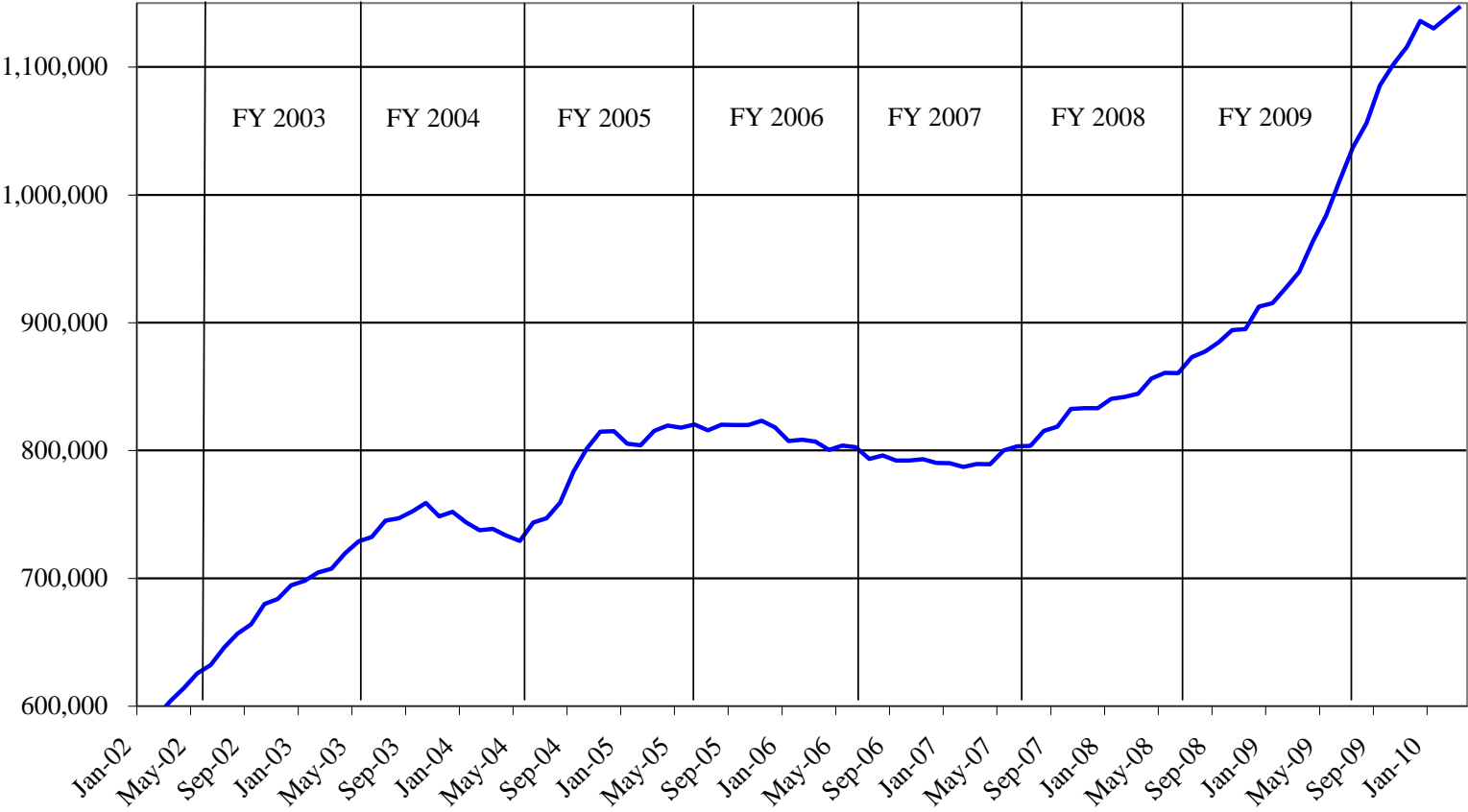
How Bad Was It?

Growing Populations – Current revenues = FY 2004

- Since FY 2004, Arizona has added 121,500 K-12 students and more than \$1.0 billion in annual costs to the K-12 system.
- Since FY 2004, enrollment in State universities has increased enrollment by 18,100 students and annual General Fund costs of \$393.5 million.
- Since FY 2004, Corrections has added 10,800 prisoners and annual General Fund costs of \$405.4 million.
- Since FY 2004, AHCCCS has added 475,000 new members and annual costs of nearly \$1.5 billion (General Fund).
-- In calendar 2009, AHCCCS has grown by 223,415 members --

How Bad Was It?

AHCCCS All TXIX Capitation Member Months
Actuals Only

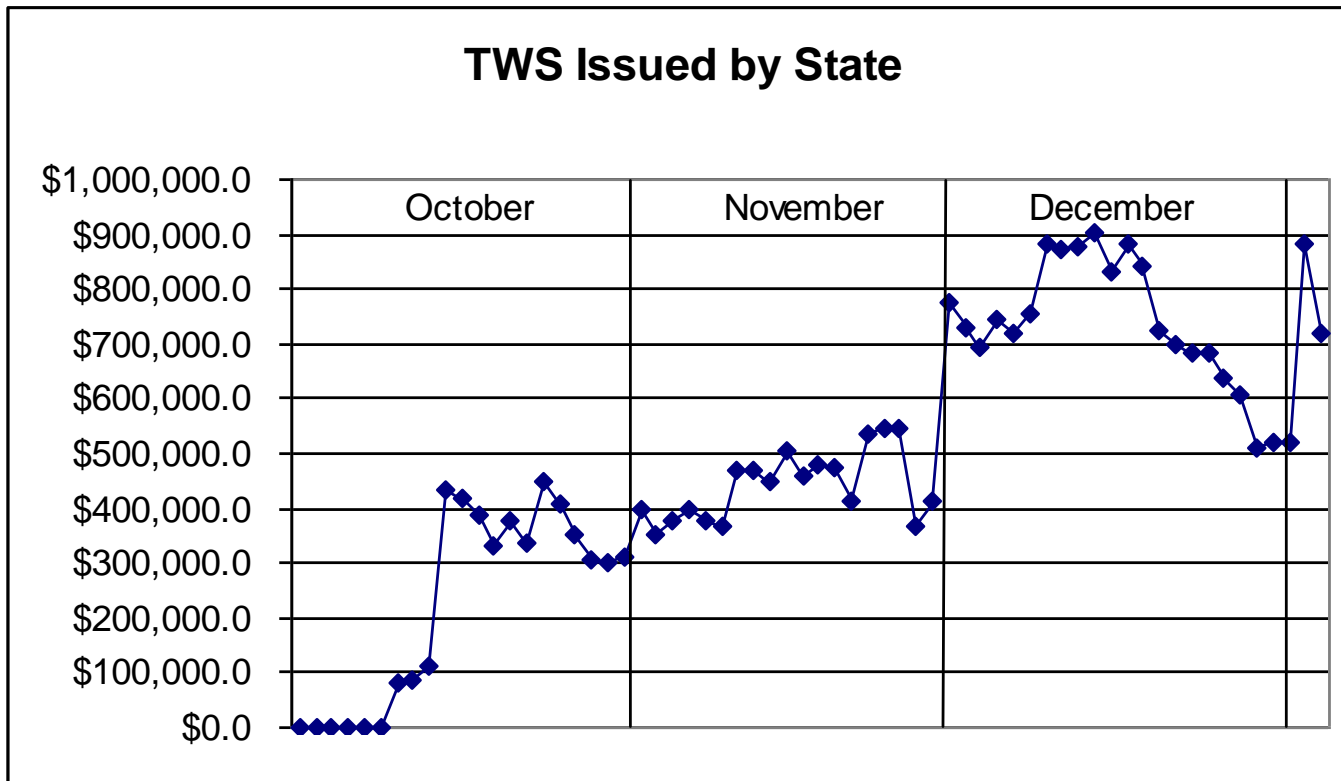


How Bad Was It?

Cash Flow Situation as of January

- Every day the General Fund was borrowing every dollar of uncommitted state cash in the State's custody: approximately \$1.5 billion.
- In addition, the State has created two facilities to borrow non state funds, an internal line of credit worth approximately \$500 million and an external line of credit with Bank of America worth \$700 million.
- The State was making daily calculations to determine if the State had sufficient cash to cover expenses.

How Bad Was It?



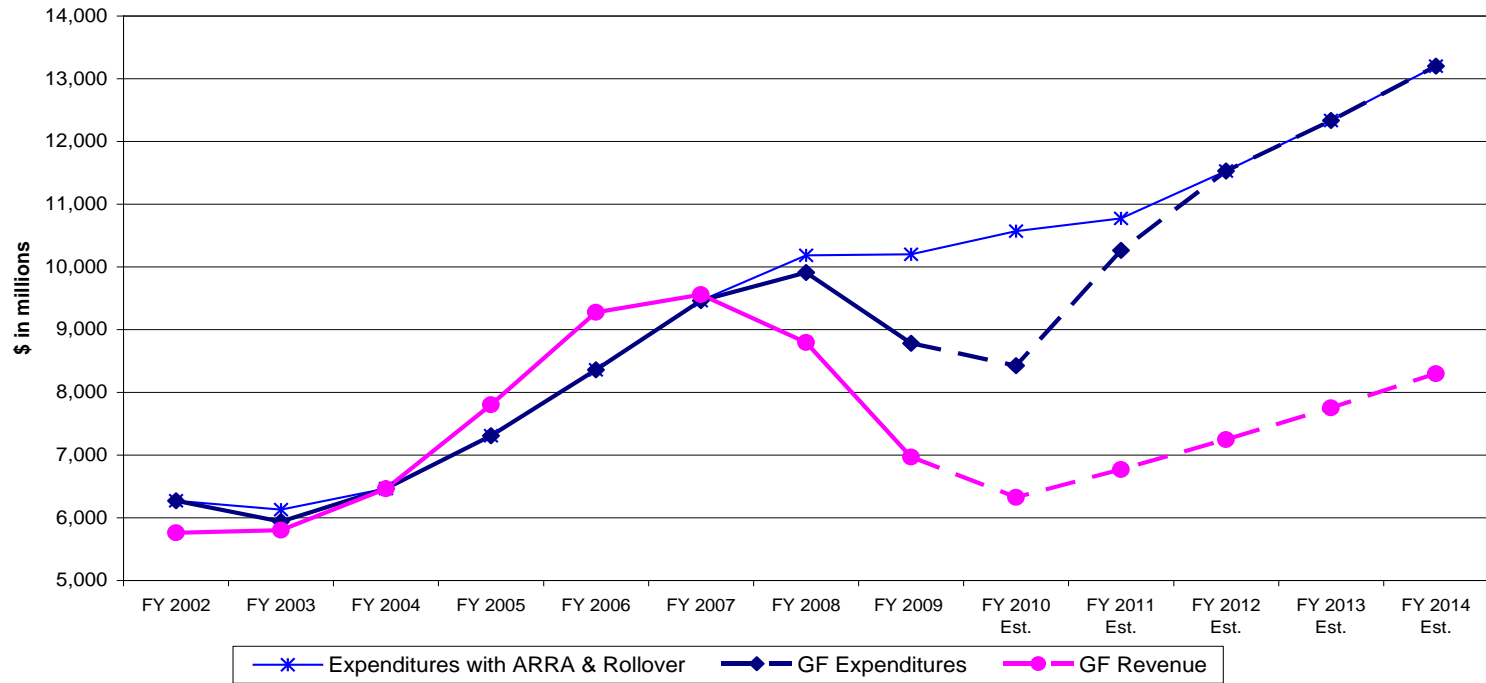
How Bad Was It?

The Bottom Line: Arizona Has a Structural Deficit

- Our ongoing revenues and ongoing expenditures are out of alignment.
- This misalignment produced a \$3.2 billion deficit for FY 2011 as of January.

How Bad Was It?

General Fund Ongoing Revenue and Expenditures before Solutions



Assumptions: **Revenue:** Ongoing revenue does not include one time items such as fund transfer, asset sales, etc. Growth rates assumptions: FY10: -9.2%, FY11:7%, FY12 and 7%. **Expenditure:** Ongoing expenditure does not include rollover or ARRA. FY10 and FY11 estimated Expenditure from most current S&U, FY12 and beyond assuming 7% growth.

What Did “They” Do?

What Did “They” Do?

First, Established Priorities

- Public safety is the core function of State government.
- Education funding is the key to long-term societal and economic development.
- Temporary revenue enhancements should be used only to protect core areas of State government.
- Budget reductions should be strategic and not arbitrary or across-the-board
- Use debt wisely and only as necessary

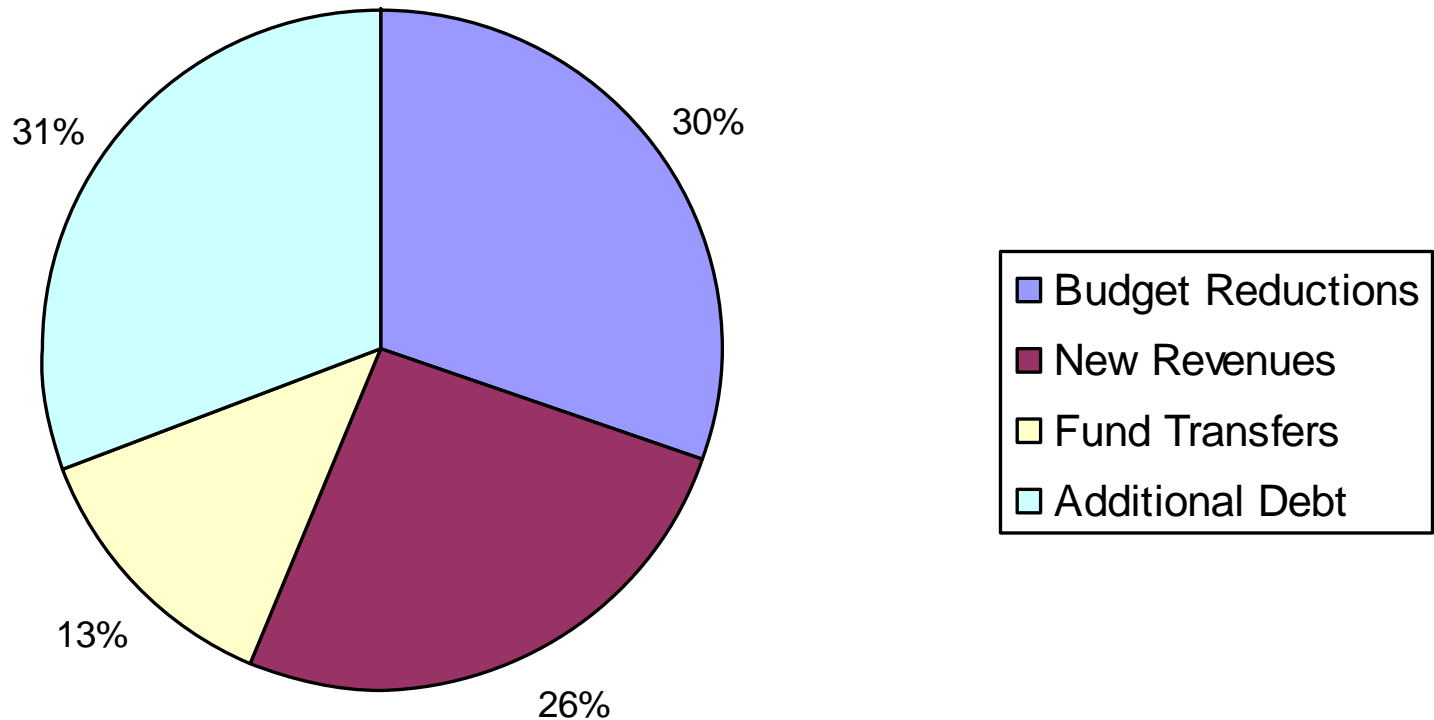
What Did “They” Do?

Strategy

- Attack structural deficit with permanent reforms
- Close deficit for FY 2010 and FY 2011 – no casual deficits
- Use real solutions
- Use temporary steps as necessary
- Quick action to avoid cash shortfalls

What Did “They” Do?

FY 2010 - FY 2011 Budget Solutions



What Did “They” Do?

Major Budget Reductions

	Savings	Impact
– Medicaid Reform*	\$380 MM	310,500
– Mental Health Reform	\$ 36 MM	14,400
– Welfare Reform	\$ 27 MM	10,000
– Childcare Limits	\$ 22 MM	10,000
– KidsCare*	\$ 18 MM	46,000
– Education (FY 06 Levels)	\$422 MM	
– Employee Salary Reduction	\$ 45 MM	
– Increase Prison Bed Deficit	\$ 25 MM	

* Overturned by Health Care Reform

What Did “They” Do?

Since FY 2008, the State has aggressively used one-time options.

Temporary Solutions	FY 2008	FY 2009	FY 2010	FY 2011	Total
K-12 & University Rollovers	\$602.6	\$100.0	\$450.0	-	\$1,152.6
BSF Sweep	\$560.0	\$150.0	-	-	\$710.0
Fund Transfers	\$290.2	\$813.1	\$372.5	\$180.3	\$1,656.1
SFB NC Recapture	-	\$344.0	-	-	\$344.0
SFB New Construction	-	\$237.0	-	-	\$237.0
K-12 Local Fund Balances	-	\$184.0	-	-	\$184.0
DES & AHCCCS Rollovers	-	\$25.0	\$159.9	-	\$184.9
Federal Funds	-	\$667.4	\$1,587.4	\$510.7	\$2,765.5
Sale Leaseback	-	-	\$1,035.4	-	\$1,035.4
Lottery Revenue Bonds	-	-	\$450.0	-	\$450.0
First Things First	-	-	-	\$325.0	\$325.0
Growing Smarter	-	-	-	\$123.5	\$123.5
Total (in millions)	\$1,452.8	\$2,520.5	\$4,055.2	\$1,139.5	\$9,168.1

What Did “They” Do?

Additionally, the State had made significant budget reductions:

Budget Reductions	FY 2009	FY 2010	Total	Reductions as a Percent of Unprotected Base
AHCCCS	\$19,000.0	\$20,000.0	\$39,000.0	18%
K-12	\$123,000.0	\$149,000.0	\$272,000.0	101%
Universities	\$90,000.0	\$0.0	\$90,000.0	9%
DES	\$203,000.0	\$143,000.0	\$346,000.0	53%
DHS	\$28,000.0	\$46,000.0	\$74,000.0	27%
Corrections	\$18,000.0	\$98,000.0	\$116,000.0	43%
Other	\$69,000.0	\$87,000.0	\$156,000.0	20%
Total (in thousands)	\$550,000.0	\$543,000.0	\$1,093,000.0	32%

As part of these reductions, the State has reduced its workforce by 10% since January 2008 (figure does not include universities or reductions made in the 5th SS).

What Did “They” Do?

FY 2010

Additional Rollovers	\$450 million
Additional Sell/Leaseback	\$300 million
Lottery Bonds	\$450 million
– Total FY 2010 new debt: \$1.5 Billion	
– Total FY 2010 Rollover: \$1.3 billion	

FY 2011

Refinance SFB Debt	\$60 million
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What Did “They” Do?

Other One Time Actions

- Eliminating Growing Smarter payments and sweeping the Land Conservation Fund (\$124 million)

What Did “They” Do?

If you are hunting elephants, go to Africa

What are the elephants in the state budget?

- K-12 Education
- AHCCCS
- DES
- DHS
- Universities
- Corrections

What Did “They” Do? K-12 Education

FY 2010 – Eliminate funding for non-formula programs

- AIMS Intervention
- Adult Education and GED
- Chemical Abuse
- Gifted Support
- Early Education Block Grant
- Vocational Education Block Grant
- Teacher Training

What Did “They” Do? K-12 Education

Protect Funding at FY 2006 Levels

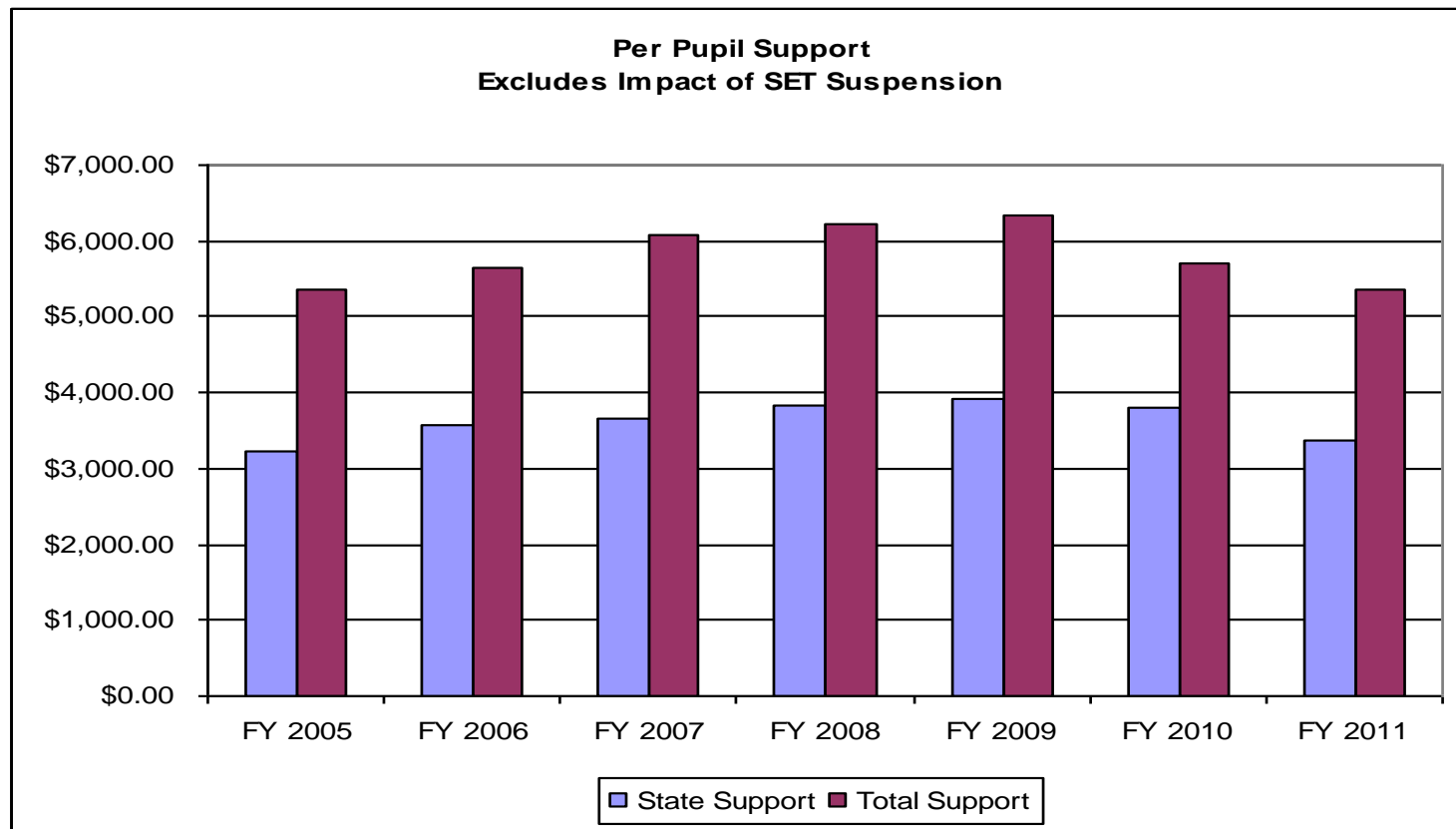
- Eliminate kindergarten funding weight (\$218 million)
- Reduce Charter Additional Assistance (\$10 million)
- Reduce Early Graduation (\$5 million)

Why FY 2006 Levels?

- More on that in a minute

What Did “They” Do? K-12 Education

Per pupil support for FY 2011 falls between FY 2005 and FY 2006 levels



What Did “They” Do? K-12 Education

School Facilities Board

New Construction

Building Renewal

- Minimal to no funding provided – what is provided is targeted to the most critical projects

What Did “They” Do? Higher Education

Universities

- Maintain support at FY 2006 levels
- Reduces per pupil support to \$7,100 per pupil (FY 2008 level was \$9,480)

Community Colleges

- Maintain support at FY 2006 levels

What Did “They” Do? Health and Welfare

AHCCCS Proposition 204

- Expanded Medicaid coverage to all populations under 100 percent of federal poverty limit (Approx. \$22,000 for family of four) including childless adults
- FY 2011 cost of the expansion

Tobacco	\$173.3 million
General Fund	\$744.7 million

Note: numbers exclude ARRA

What Did “They” Do? Health and Welfare

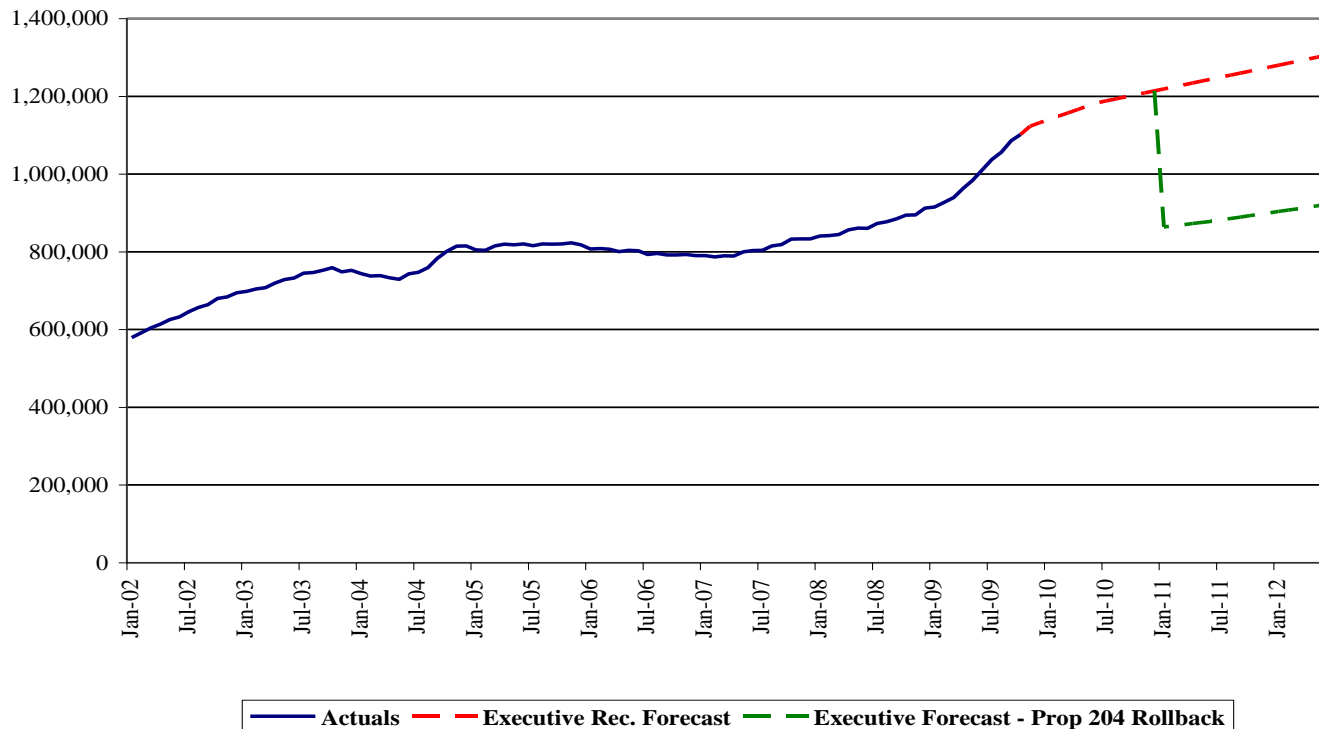
Proposition 204

The Original adopted budget eliminated General Fund support for this program as of January 1, 2011.

- Eliminate support for childless adults
 - Cap other populations at the support level covered by the Tobacco Settlement
-
- An estimated 310,500 people would lose coverage
 - State will lose \$737.6 million in Federal matching funds
 - GF will save \$382.5 million in FY 2011, \$1 billion in FY 2012

What Did “They” Do? Health and Welfare

AHCCCS TXIX Capitation Member Months
Actuals and Forecasts



Approximately 25 percent of the current Medicaid population will lose services.

What Did “They” Do? Health and Welfare

Other AHCCCS Issues (all receiving 2:1 or 3:1 federal match)

- The original budget eliminated the KidsCare program, saving \$22.9 million. KidsCare provides health coverage for 46,800 children with incomes below 200% of FPL.
- Medicaid capitation rate for growth held flat; will likely result in provider rate reductions, saving \$57.1 million.
- Optional benefits are eliminated under the Executive proposal for a \$6.3 million savings.
- The GME (doctors) and DSH hospital subsidies were scheduled to disappear, now minimal funding for DSH, option for governments to contribute to GME

What Did “They” Do? Health and Welfare

Arnold v. Sarn

- Reduce funding for Arnold v. Sarn, Non-TXIX SMI, and the Court Monitor
 - 14,400 Adults impacted
 - Saves \$37 million
 - Preserve \$21 million for new stand-alone Crisis Intervention and Supported Housing
 - Preserves \$37 million to fund medications for all Non-TXIX SMIs

What Did “They” Do? Health and Welfare

Department of Economic Security

Program Eliminations (FY 2010)

- Sight Conservation
- DD Provider Enhanced Rates
- Grandparent Kinship Care
- SSBG Planning Funds for local governments

Means Testing for all programs: Child Support fees, DD services, etc.

What Did “They” Do? Health and Welfare

Department of Economic Security

Cash Assistance Restriction (FY 2010)

- Reduces benefit from 60 months to 36 months
- Eliminates services for approximately 10,000 families
- Recommended for implementation July 1, 2010

What Did “They” Do? Other Areas

- The Parks Board may close several parks, discussion has ranged from 4 to 8 of the 30 state parks (The State is withdrawing support, but the parks remain open due to local support)
- Moving ADEQ, Water, Tourism to self funding
- Reducing state employee pay (5 percent)

What Did “They” Do? Other Areas

Impacts on Local Government

- Shift of Lottery funds
- Shift of Tourism funds
- Eliminate County Hold Harmless
- Charge counties for ASH costs
- Eliminate SSBG planning funds
- County Attorney Immigration Enforcement cut in half

What Did “They” Do? Revenue

Revenue Enhancements

Item	FY 2010	FY 2011
Lower Estimated Payment Threshold	\$48,000.0	-
1-Cent Sales Tax	-	\$918,000.0
Abandoned Vehicle Fees	-	\$12,061.2
First Things First Redirect	-	\$60,000.0
Tax Administration and Staff	-	\$18,539.9
Maricopa/Pima County Contributions	-	\$34,600.0
Total	\$48,000.0	\$1,043,201.1

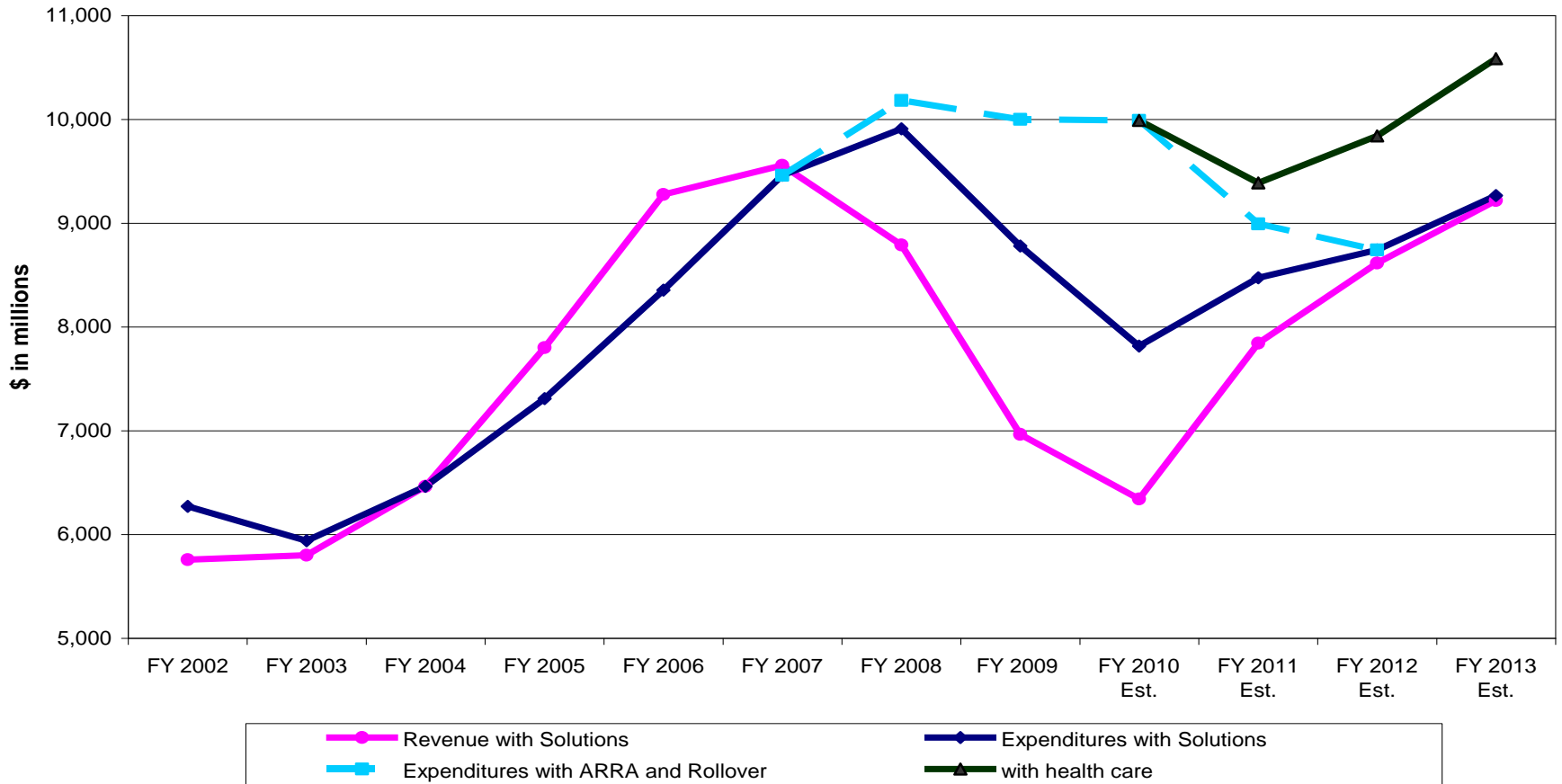
Represents a 14.2 percent increase in FY 2011 base revenues

What Did “They” Do? Conditional Budget

- K-12 Education \$428 million
- Higher Education \$120 million
- Public Safety \$100 million
- Health Care \$175 million
- Human Services \$25 million

What Did “They” Do? Outcome

General Fund Ongoing Revenue and Expenditures Adopted Budget



Why Were These
Actions Taken?

Why These Actions?

Time

There is not a lot of time to correct the problem.

- Half of FY 2010 was gone by the time the Legislature returned for its Regular Session.
- FY 2011 was to begin in less than six months.

Why These Actions?

Constraints Imposed by the Voters

Two primary areas

- “Proposition 108” - requires either a two thirds vote of the Legislature or a vote of the people to increase “State revenues”
- “Proposition 105” - effectively prohibits the legislature from modifying programs or revenues approved by the voters, e.g. portions of the AHCCCS, K-12 programs, and First Things First (preschool)

Why These Actions?

The Federal Government

- When the State accepted the ARRA money, it agreed to a maintenance of effort (MOE) requirement – through the end of FY 2011 for education, through December 2010 for AHCCCS.

Why These Actions?

The Federal Government (cont'd)

- The MOE for education prohibits reducing funding below the FY 2006 funding the state provided to education (K-12, Community Colleges, Universities).
- The MOE for AHCCCS provides that as long as we accept the ARRA funds for the program, we cannot reduce eligibility. ARRA funds for AHCCCS are currently scheduled to end on December 31, 2010.

What Are the Prospects

Prospects?

The Economy

Job Losses as of March

Peak Employment – 2.68 million jobs

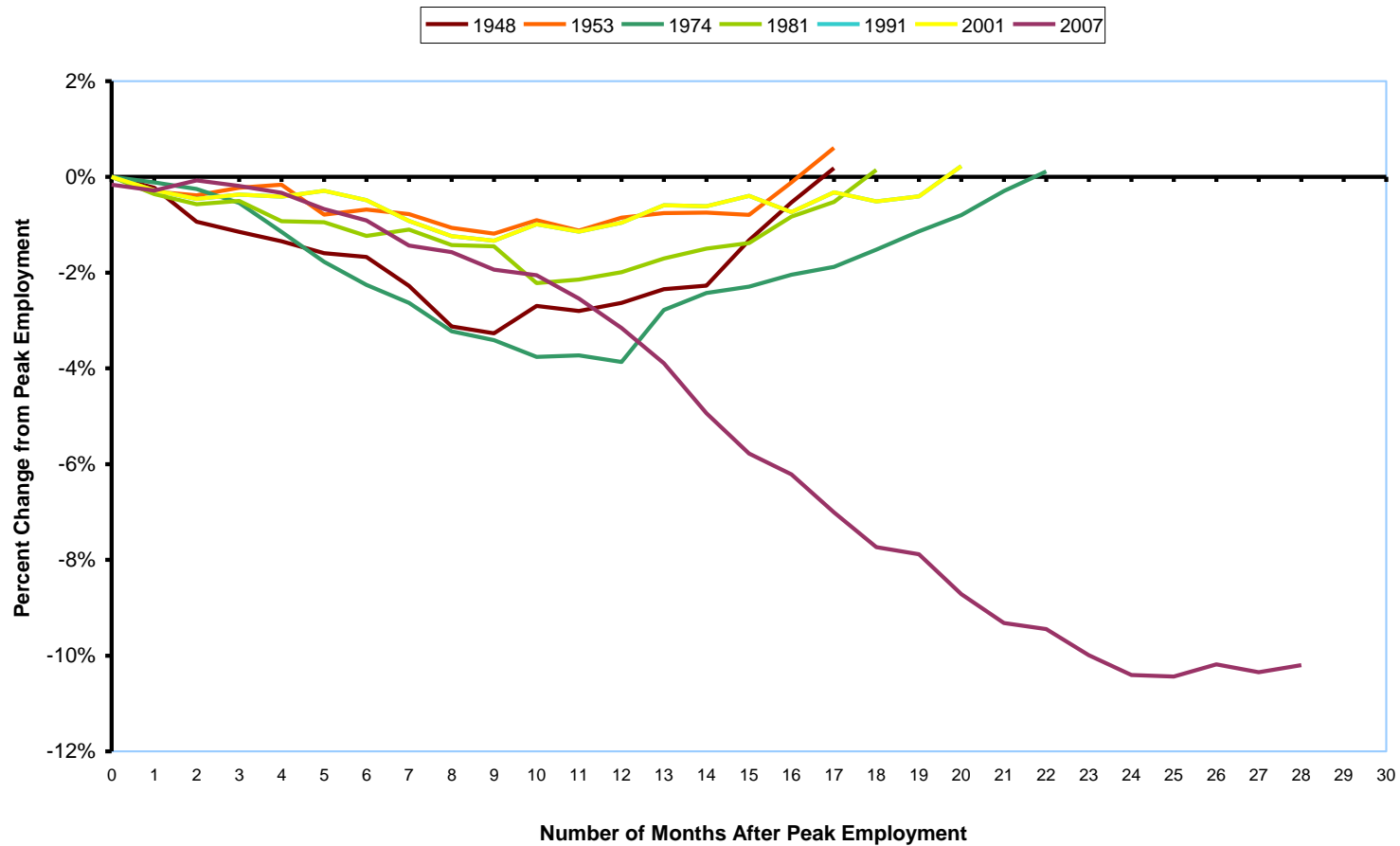
– August 2007

Current Employment – 2.36 million jobs

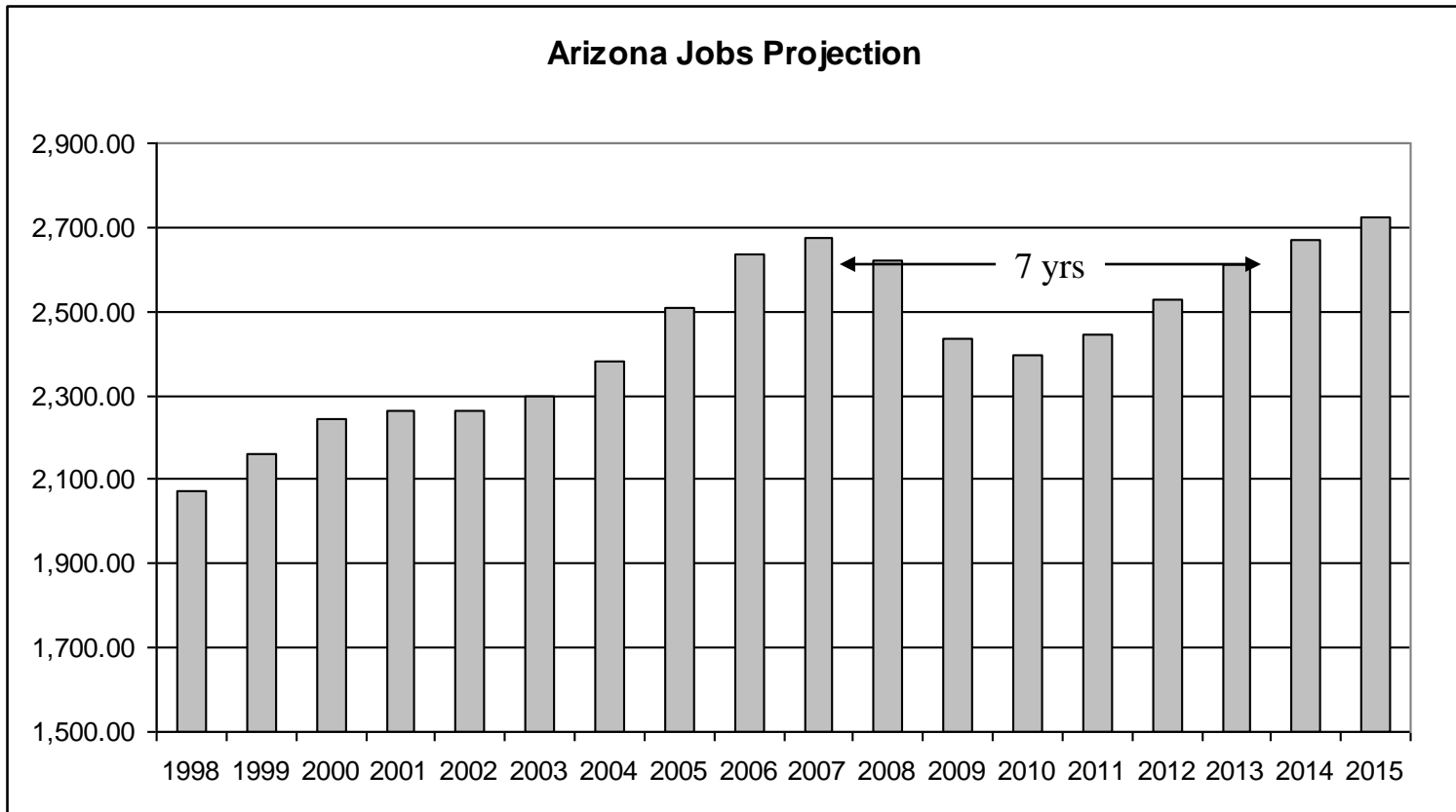
– Total loss of 323,700 jobs

Prospects?

Arizona
Number of Months needed to surpass a peak in employment.



Prospects?



Developed by the AZ Department of Commerce

Prospects?

- There is already talk that FY 2010 will not, in fact finish with a positive balance, However, OSPB is still confident that FY 2010 will end with a balanced budget.

Prospects?

The Federal Government

In FY 11, the majority of the ARRA funds will discontinue and the State will have to replace the funding that the federal government has provided in FYs 2009, 2010 and continuing into 2011.

The Table on the following page illustrates that in FY 2011 General Fund monies are to replace over \$900 million of ARRA funds.

Prospects?

The ARRA FY 2011 Cliff

AHCCCS	201,806.9
DHS	90,343.5
DES	105,151.6
K-12 Education	379,314.0
Universities	64,000.0
Community Colleges	20,000.0
Corrections	50,000.0
TOTAL	910,616.0

Prospects?

?