ATRA Presentation:
State Budget Outlook

November 21, 2008

JLBC
'08 General Fund Base Revenue Decline of (4.6)% Was Greater Than Budgeted

Excludes statutory and one-time changes.
Decline Accelerated in Second Half of FY ’08

Percent Change From FY 2007

- 1st Qtr: 1.6%
- 2nd Qtr: 0%
- 3rd Qtr: -3.9%
- 4th Qtr: -11.7%
FY ’09 Revenues Will Need to Grow By 6.1% to Meet $10.0 B Budgeted Level

- Original budgeted FY ’09 growth compared to enacted ’08 Budget 1.9%
- Growth adjusted for lower ’08 Base 6.1%
09 Revenue Collections Continuing to Decline
- First Quarter Decline = (8.9)%

Percent Change Below FY 2008

- Jul: -6.2%
- Aug: -11.1%
- Sep: -9.9%
Where Are We Headed Over the Next Few Years?
- Four-Sector Consensus Forecast Incorporates Different Economic Views

4-sector forecast equally weights:
- FAC average
- UofA model - base
- UofA model - low
- JLBC Staff forecast
- Remaining revenues (2% of total) are staff forecast

* Includes Big 3 categories of sales tax, individual income and corporate income taxes.
Sales Tax
- The Consensus Forecasts Declines of (3.3)% in '09
and Another (0.8)% in '10

FY 2008 Actual = $4.3 Billion

* 5.6% without the $(55.2) million estimated payment threshold change.
Construction and Vehicle Spending Have Declined Significantly

FY 2009 Year to Date – (Through September)
October 4-Sector General Fund Revenue Forecast
- Decline of (4.4)% in FY '09 and (0.7)% in FY '10

Weighted Big 3 Average
Prior to Tax Law Changes
Growth Remains Slow Until FY 2011

* 4-sector forecast weighted average growth.
On-Going General Fund Revenue
- Collections Below FY ’07 Level Until After FY ‘12

Includes Urban Revenue Sharing and enacted tax law changes
- excludes balance forward and other one-time revenues.

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What Is the General Fund Shortfall?

- $1.2 B in FY ’09, based on updated forecast.

- $2.2 B to $3.0 B in FY ’10, depending on ’09 resolution and other factors.
### ’09 Revenue and Expenditure Comparison

($ in Billions)

<table>
<thead>
<tr>
<th></th>
<th>On-going</th>
<th>One-time</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenues</strong></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>On-going</td>
<td>$ 8.1</td>
<td>0.7</td>
<td>8.8</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td><strong>Spending</strong></td>
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<tr>
<td>On-going</td>
<td>10.7</td>
<td></td>
<td>10.0</td>
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<tr>
<td>One-time</td>
<td>(0.7)</td>
<td></td>
<td></td>
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<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td>10.0</td>
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</tbody>
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**Balance** $(1.2)$
What Are the Possible Solutions?

- Revenue
- Spending
- Fund Transfers
- Borrowing
- Accounting
Another Perspective on the State Budget: State Spending Priorities and Voter Protection
5 Major Activities Account for 92% of State Spending

<table>
<thead>
<tr>
<th>Activity</th>
<th>$ in M</th>
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<tbody>
<tr>
<td>K-12</td>
<td>4,253</td>
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<tr>
<td>Medicaid</td>
<td>2,002</td>
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<tr>
<td>Higher Ed</td>
<td>1,228</td>
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<tr>
<td>Prisons</td>
<td>1,022</td>
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<tr>
<td>State Workers</td>
<td>604</td>
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<tr>
<td>Other</td>
<td>797</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$ 9,906</strong></td>
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</tbody>
</table>
What Spending is Voter Protected?

- Prop 105 prohibits legislative changes to propositions without a 75% vote to "further the purpose".
- Prop 301 Education and Prop 204 AHCCCS have greatest impact on state budget.
- This "voter protection" limits, but does not eliminate, our ability to modify ADE and AHCCCS.
- There has been no litigation to clarify the scope of Prop 105.
What is the Difference Between Voter Protected and Mandated Spending?

- Mandated spending is based on statutory formulas.
- Legislature can revise certain mandates.
- Voter-protected spending is a subset of mandates.
At Least $2.2 B of K-12 Spending is Not Subject to Prop 105

- State and local K-12 budget = $6 B.
- As funding expands or contracts, marginal impact is on the state.
- Non-base level spending is $2.2 B.

State and Local K-12 $  
State = $4.4 B  Local = $1.6 B
AHCCCS Non-Protected Share is at Least $435 M
- Feds May Permit Limited Adjustments to Rates

- Non-protected includes $237 M in drugs/ALTCS costs.
- California injunction against 10% rate cut.
Summarizing the General Fund Impact of Voter Protection

- **K-12**: At least $2.2 B of $4.4 B General Fund budget is not protected.
- **AHCCCS**: $435 M of $1.4 B is not protected
  - Limited ability to reduce remaining $1 B.
- **Parks Board**: $20 M Growing Smarter payments
  - Ends in FY 2011.
- **Clean Election Tax Credits**: $7 M
  - Offset by periodic reversions.
What Is Voter Protected Share of GF Spending?
- No Definitive Answer, But Near $3.5 B

$10.2 B GF Budget
Rollover-Adjusted

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