

ARIZONA

MONTHLY FISCAL HIGHLIGHTS

November 2006

October General Fund revenue collections were \$730.3 million, or 20.7% above October 2005. This amount was \$88.2 million above the forecast for the month. The forecast comparison is based on projected FY 2007 revenues from the enacted budget. For the fiscal year-to-date, collections are \$97.7 million above the forecast. (See Table 3 on page 2.)

Of the major tax categories, October sales tax grew at a rate of 9.4%, individual income collections increased 24.7%, and corporate revenues were 88.7% above last year. Prior to October, collections in the first quarter of FY 2007 increased 7.6% over last year, a much slower level of growth compared to the overall growth in FY 2006 of 16.5%. With the surge in October revenues, however, year-to-date collections are now 10.5% above last year. (See Table 6 on page 11 for details.)

The JLBC and the JCCR met on November 15th (pages 4 – 6). Highlights included:

- The JLBC favorably reviewed a report from ASU on the operational and capital plans for the Downtown Phoenix Campus. In FY 2007, 2,766 students are enrolled in 1 or more courses at the campus. BY 2014, ASU expects this

number to increase to 15,000. To finance expansion of the campus, the City of Phoenix issued \$223 million in bonds, while ASU contributed \$20 million from its own budget. At the time of the meeting, ASU did not provide details on specific capital costs associated with the Schools of Journalism or Nursing, or its long-term plan for student housing. Regarding student housing, ASU expects the private sector to contribute \$135 million for the development of housing units.

- The JLBC favorably reviewed the Department of Commerce agreement with Science Foundation Arizona to manage \$35 million from the 21st Century Fund. Major spending items include \$23 million for research and development grants, \$2 million to convert research into startup companies, and \$7.5 million to promote science education at Arizona's public schools and universities.
- The JCCR favorably reviewed 2 university projects that will be built through a public-private partnership. NAU has partnered with a private company to build a 150 room on-campus hotel, while ASU has entered into an agreement with a private firm to develop student housing for over 3,500 students.

Table of Contents

<u>Page #</u>	<u>Page #</u>
October Revenues	2
Recent Economic Indicators	2
<u>November 15 JLBC Meeting Summary</u>	
- ADOA – Mileage and Travel Reimbursement	4
- ADOA – Statewide Telecommunications Contract	4
- ASU – Downtown Phoenix Campus	4
- ABOR – Enrollment Accounting Policies	4
- ADE – Information Technology Implementation Plan	5
- JLBC Staff – Condominium and Planned Community Administrative Hearing Filing Fees	5
- Land Dept. – Radio System Upgrades	5
- Commerce – 21 st Century Fund Expenditure Plan	5
<u>November 15 JCCR Meeting Summary</u>	
- ADOT – Capitol Mall Modular Buildings	5
- SFB – New Construction Report and Litigation Account	5
- SFB – FY 2007 Building Renewal Distribution	6
- Lottery – FY 2007 Building Renewal Allocation	6
- Parks Board – State Lake Improvement Fund Projects	6
- NAU – Hotel and Conference Center Indirect Financing	6
- ASU – Honors College and South Campus Academic Village Bond Projects	6
<u>November 15 JCCR Meeting Summary (cont'd)</u>	
- UA – Law Commons Bond Project	6
- UA – Athletics Facilities Bond Projects	6
<u>Summary of Recent Agency Reports</u>	
- ADOA – Alternative Fuel Vehicle Use	7
- ADOA – Projected FY 2007 Utilities Funding Shortfall	7
- AHCCCS – Hospital Inpatient Outlier Claims	7
- Community Colleges – Annual Report	7
- Community Colleges – Dual Enrollment	7
- Corporation Commission – Corporations Division Filings	8
- ADC – Monthly Expenditures Report	8
- ADC – Monthly Bed Plan Update	8
- ADE – Budget Status Report	8
- DES – Arizona Works Pilot Program	8
- DES – Projected FY 2007 Shortfall	9
- Commission of Indian Affairs – Indian Town Hall Fund	9
- City of Phoenix – Convention Center Expansion	9
- DPS – Staffing Levels	9
- ABOR – Credit Hour Threshold FTE Student Counts	10
- SFB – ASDB Capital Costs	10
- ADOT – MVD Wait Times	10

The Monthly Fiscal Highlights also include a summary of recent statutory reports to JLBC (*pages 6 – 10*). Of particular note, 3 additional state agencies are now projecting a FY 2007 General Fund budget shortfall.

- The Arizona Department of Administration anticipates a \$1.7 million shortfall associated with higher than budgeted utility costs (*page 7*).
- The Arizona Department of Education projects a \$9.7 million shortfall due to enrollment growth and achievement testing costs (*page 8*).
- The Department of Economic Security estimates a \$24 million shortfall as a result of CPS residential placement caseload growth and reduced federal funding for foster care (*page 8*).

In addition to these newly reported shortfalls, the Arizona Department of Corrections has increased its shortfall estimate, first reported in October as \$21.3 million, to \$28.5 million (*page 8*).

OCTOBER REVENUES

Sales Tax collections were \$376.9 million in October, or 9.4% above last October. The following table displays the October and year-to-date growth rates for the major categories.

Table 1		
Sales Tax Growth Rates		
	<u>October</u>	<u>Year-to-Date</u>
Retail	4.7%	5.0%
Contracting	21.9%	18.9%
Utilities	9.9%	12.6%
Use	1.4%	6.6%
Restaurant & Bar	8.8%	7.3%

Collections for some of the major sales tax categories continued to grow at a slower pace in October, including use tax collections. For the month, revenues were \$9.3 million above the forecast.

Individual Income Tax collections were \$305.1 million in October, or 24.7% above last year. *Table 2* at the top of the page displays the October and year-to-date growth rates for the individual income tax categories.

Table 2

Individual Income Tax Growth Rates

	<u>October</u>	<u>Year-to-Date</u>
Withholding	13.2%	7.1%
Estimated + Final Payments	139.6%	41.5%
Refunds	54.4%	38.1%

The large increase in overall monthly collections was driven by substantial growth in October final tax payments. These payments likely represent liabilities that were deferred from the spring of 2006. Taxpayers incurred large liabilities from prior year gains, and since the Internal Revenue Service allows an extension of 6 months for some payments, some taxpayers may have waited until October to make those payments. For these deferred liabilities, taxpayers are also required to make an interest payment.

In addition to the growth in final payments, October withholding collections rebounded from the slow performance of the past few months, while refunds continued to be above forecast. Net revenues, therefore, were \$41.3 million above the forecast for the month.

Corporate Income Tax collections were \$53.9 million in October, or 88.7% above last year. For the month, corporate income tax revenues were \$22.8 million above the forecast. Though this is a substantial increase, October accounts for only a small portion of overall collections. Year-to-date, revenues are 22.7% above last year.

RECENT ECONOMIC INDICATORS

Preliminary estimates for 2006's 3rd quarter indicated that **U.S. Gross Domestic Product (GDP)** growth slowed to a 1.6% annual rate, down from the 2.6% pace posted in the 2nd quarter. The decline in residential investment was the largest since the 1st quarter of 1991.

Other indicators suggested the 4th quarter was off to a somewhat better start. The **U.S. Index of Leading Economic Indicators** increased 0.2% in October, following a revised 0.4% gain in September. Manufacturing hours worked, stock prices, and declining unemployment insurance claims pushed the index higher, while vendor performance and building permits made negative contributions.

Table 3

General Fund Revenues Compared to Enacted Forecast and FY 2006 Collections

	<u>FY 2007</u>	<u>Difference</u>	<u>Difference</u>
	<u>Collections</u>	<u>From Forecast</u> ^{1/}	<u>From FY 2006</u>
October	\$ 730.3	\$ 88.2	\$ 125.3
Year-to-Date	\$ 3,026.3	\$ 97.7	\$ 286.5

^{1/} Enacted FY 2007 budget (June 2006)

Consumer sentiment faded slightly but remained at relatively high levels. After increasing by a revised 5.7% in September, the Conference Board's **U.S. Consumer Confidence Index** edged (0.5)% lower in October. Consumers' assessments of current conditions and the job market were responsible for the decline. Even so, consumer confidence remained 23.7% above its level from a year ago.

Electronics manufacturers continued to benefit from a banner year. **U.S. semiconductor billings** (3-month moving average) climbed 1.8% in September and were running 12.9% ahead of last year's results. The Semiconductor Industry Association (SIA) noted that the pending release of the Windows Vista operating system is driving sales of DRAM memory devices to PC producers. In a separate report, the SIA projected a 9.0% compound annual growth rate for semiconductor sales through 2009. In addition to PC sales, cell phones, MP3 devices, and digital televisions are expected to contribute to strong product demand for the next several years.

The good news on inflation continued. The **U.S. Consumer Price Index (CPI)** (3-month moving average) dipped (0.5)% in October, which reduced the year-over-year increase to 2.4%. Gasoline prices dropped (12.0)% from September while other transportation expenses continued to decline.

Meanwhile, food prices increased 0.4% from the prior month. Excluding food and fuel costs, the core CPI increased 0.1% in October and stood 2.7% higher than a year ago.

Arizona's job market posted another round of solid results in October. **Non-farm employment** expanded by more than 121,000 jobs in the last 12 months, a 4.7% increase. The goods-producing industries, led by construction, combined for a year-over-year growth rate of 6.5%. The retail and hospitality sectors added almost 9,000 employees over the prior month in anticipation of the holiday season. Although the seasonally adjusted statewide **unemployment rate** increased to 3.9%, it remained well below the 4.4% U.S. average.

Table 4

RECENT ECONOMIC INDICATORS

<u>Indicator</u>	<u>Time Period</u>	<u>Current Value</u>	<u>Change From Prior Period</u>	<u>Change From Prior Year</u>
Arizona				
- Unemployment Rate	October	3.9%	0.2%	(0.9)%
- Jobs	October	2.68 million	1.1%	4.7%
- Contracting Tax Receipts (3-month average)	Aug-Oct	\$81.3 million	(2.0)%	17.8%
- Retail Sales Tax Receipts (3-month average)	Aug-Oct	\$159.6 million	(5.6)%	4.4%
- Residential Building Permits - (3-month moving average)				
Single-unit	Jul-Sep	3,904	(16.7)%	(42.6)%
Multi-unit	Jul-Sep	629	(5.2)%	(43.6)%
- Greater Phoenix Existing Home Sales				
Single-Family	October	4,985	2.3%	(40.8)%
Townhouse/Condominium	October	915	(1.6)%	(46.6)%
- Greater Phoenix Median Home Sales Price				
Single-Family	October	\$257,000	0.0%	(1.1)%
Townhouse/Condominium	October	\$175,000	0.9%	8.0%
- Arizona Tourism Barometer	June	106.9	3.0%	4.9%
- Phoenix Sky Harbor Air Passengers	June	3.61 million	1.0%	1.1%
- Arizona Average Natural Gas Price (\$ per thousand cubic feet)	August	\$7.22	3.4%	(12.0)%
- Leading Indicators Index	September	119.2	0.9%	0.1%
- Business Conditions Index (>50 signifies expansion)	October	60.8	(3.1)%	(10.9)%
- Consumer Confidence Index	4 th Quarter 2006	105.3	2.5%	7.3%
- Business Leaders Confidence Index	4 th Quarter 2006	48.1	(3.0)%	(12.1)%
- Arizona Personal Income	2 nd Quarter 2006	\$194.3 billion	2.0%	9.8%
- Arizona Population	July 1, 2005	5.94 million	3.5%	3.5%
- AHCCCS Recipients	November	1,029,898	(0.0)%	(3.0)%
- TANF Recipients	September	87,605	(0.3)%	(12.3)%
- DOC Inmate Growth (3-month average)	Aug-Oct	35,397	253 inmates	2,365 inmates
United States				
- Gross Domestic Product (seasonally adjusted annual growth rate)	3 rd Quarter 2006	\$11.4 trillion	1.6%	2.9%
- Consumer Confidence Index	October	105.4	(0.5)%	23.7%
- Leading Indicators Index	October	138.3	0.2%	1.0%
- U.S. Semiconductor Billings (3-month moving average)	Jul-Sep	\$3.89 billion	1.8%	12.9%
- Consumer Price Index (3-month moving average)	Aug-Oct	202.9	(0.3)%	2.4%

The **Arizona Business Conditions Index** (BCI) decreased (3.1)% to 60.8 in October but remained within the range it has occupied for most of the current business expansion and above the mark of 50 associated with an expanding economy. Delivery times and materials prices were among the factors contributing to the decline, while the new order component was climbing. An increase in new orders is usually followed by rising production and employment.

The **Arizona Leading Economic Indicators Index** jumped 0.9% in September, its second increase following four consecutive declines. Production, employment and the money supply were among the factors pushing the index higher.

Arizona's housing market continued to slump. The number of **single-family residential building permits** issued (3-month moving average) declined (16.7)% in September and was (42.6)% below the number issued a year ago. The number of **multi-family housing units authorized** decreased (5.2)% in September and was down by (43.6)% from a year ago.

The Real Estate Center at Arizona State University reported that the Greater Phoenix **single-family median resale home price** was stable in October, rising by \$100 from the previous month to \$257,000. The number of existing single-family homes sold increased 2.3% from the prior month but was (40.8)% less than the number sold a year ago. The number of multi-family units sold plunged (43.6)% on a year-over-year basis, but the **townhouse-condominium median price** edged up 0.9% to \$175,000 and was 8.0% higher than a year ago.

The **Department of Corrections' inmate population** increased by an average of 253 inmates per month from August through October. The total population increased by 2,365 inmates from a year ago.

The number of **TANF** recipients decreased (0.3)% to 87,605 in September and was (12.3)% below the level from September 2005. The **AHCCCS caseload** was virtually unchanged in November from the prior month and was (3.0)% below the level from a year ago.

JLBC MEETING

At its November 15th meeting, the Joint Legislative Budget Committee considered the following issues:

Department of Administration – Approval of Maximum Mileage and Travel Reimbursement Rates – The Committee gave a favorable review to the Department of Administration's maximum reimbursement amounts for state travel by motor vehicle, meal and incidental expenses, and lodging expenses, effective immediately. These changes include: 1) increasing the personal vehicle mileage reimbursement rate from 40.5 cents to 44.5 cents per mile to conform to the federal government rate; 2) increasing the standard meals and incidental reimbursement rate from \$29.50 to \$34.00 per day; and 3) adjusting the lodging rates by keeping the standard overnight rate at \$60.00, and making several increases and a few decreases to the lodging rate in non-standard areas to conform to the federal government rate. The reimbursement

for non-standard areas will have an average increase of \$21.00 per day.

Department of Administration – Review of Telecommunications Contractor and Carrier Cost Rate Structure – The Committee gave a favorable review to the revised contractor and carrier cost rate structure of the Statewide Telecommunication Management Contract, with the provision that the favorable review does not constitute an endorsement of any FY 2008 General Fund appropriation to cover higher AZNet costs or the Department of Administration's (ADOA) expenditure plan. For FY 2008, ADOA is recommending a rate structure that would decrease the state's overall telecommunications budget by \$(654,600).

Arizona State University – Review of Downtown Phoenix Operational and Capital Plans – The Committee gave a favorable review to Arizona State University's (ASU) operational and capital plans for the ASU Downtown Phoenix Campus (DPC) with the provision that the favorable review did not constitute the endorsement of any level of General Fund appropriation for the DPC.

In March 2006, the citizens of Phoenix approved \$223 million in bond funds, of which \$188 million has been dedicated for campus construction projects and \$35 million has been designated for the development of civic space and street improvements within the campus district.

Since the city will be responsible for financing these projects, the cost of the debt service will not be applied toward the university's debt ratio. For each university, statute limits the amount of debt service to be paid on all outstanding bonds and certificates of participation to 8% of total annual university expenditures. If ASU had been responsible for financing the projects, the university's debt ratio would have increased from 5.3% to 6.1%.

Once the bonds are paid off, the City will transfer ownership of the facilities to ASU at no cost, on the condition that they continue to be used as educational facilities. Although ASU is not required to make any lease payments prior to taking possession of the facilities, the university has agreed to annually contribute, from FY 2009 to FY 2012, about \$1.5 million for repair costs. In addition, ASU will contribute \$20 million from its own budget for furniture and equipment costs. ABOR and ASU will also transfer ownership of the Downtown Center/Mercado property (currently valued at \$16 to \$23 million) to the City of Phoenix in 2024.

According to 21st day counts for the fall semester of 2006, 2,766 students are enrolled in one or more classes at the downtown campus. ASU expects the number of students to grow to 15,000 by 2014.

Arizona Board of Regents – Review of Enrollment Accounting Policies – The Committee gave a favorable review of the Arizona Board of Regents' (ABOR) assessment of the FTE student enrollment accounting policies and procedures.

The Committee also requested that ABOR submit information on students attending courses as part of their professional continuing education requirement.

Statute requires that ABOR make recommendations concerning the necessity of minimum requirements for students enrolled in classes to qualify as part of the FTE enrollment count. The FTE count is used as the basis to determine the state's contribution to enrollment funding. ABOR's report did not recommend any changes to its current enrollment policy.

Department of Education – Review of Information Technology Special Line Item Program – The Committee gave a favorable review to the Arizona Department of Education's (ADE) implementation plan for the Information Technology Project.

ADE's FY 2007 budget included a \$2.5 million one-time appropriation to develop and implement an Education Data Warehouse (EDW) that would integrate into a single database long-term historical data on student funding and achievement that currently reside in separate, non-interacting data "silos." ADE indicates that this would make its historical data much more accessible to users, enabling that data to be used more effectively for analysis and planning and allowing ADE to file required reports (such as for No Child Left Behind) more efficiently.

JLBC Staff – Review of Filing Fee for Administrative Hearing Pursuant to the Condominium and Planned Community Program – The Committee gave a favorable review to the Department of Fire, Building and Life Safety's (DFBLS) \$550 fee charged to parties for filing for an administrative hearing for disputes regarding Condominiums and Planned Communities. Laws 2006, Chapter 324 created a new program in the DFBLS, under which a homeowner or a homeowner association may file for an administrative hearing for a dispute involving the owner and a condominium or planned community association. After receiving the petition, the DFBLS refers cases to the Office of Administrative Hearings (OAH). Monies in the fund are used first to reimburse the OAH hearing costs, and second to offset the costs of the DFBLS administering case filings.

State Land Department – Review of Expenditure Plan for Radio System Upgrades – The Committee gave a favorable review to the State Land Department's plans to expend the one-time General Fund appropriation of \$96,000 during FY 2007 to upgrade its Statewide Radio Repeater System (SRRS). The SRRS expansion will increase the safety of flight crews by providing information on the exact locations of aircraft engaged in support or wildfire fighting missions, and by allowing dispatcher and flight crews to be in constant communication.

Department of Commerce – Review of Memorandum of Understanding for the Arizona 21st Century Competitive Initiative Fund – The Committee gave a favorable review to

the Memorandum of Understanding (MOU) between the Department of Commerce (DOC) and Science Foundation Arizona (SFAz). The MOU contained SFAz's expenditure plan for \$35 million in General Fund monies that was appropriated to the Arizona 21st Century Competitive Initiative Fund for the purpose of strengthening Arizona's medical, scientific, and engineering research programs and infrastructure. The \$35 million expenditure plan includes:

- \$23 million for research and development (R&D) grants with an emphasis on partnerships between industry and the universities and other research institutions;
- \$2 million for seed capital to develop research into startup companies that can win federal assistance and attract venture capital;
- \$4 million for competitive scholarships to 80 first-year graduate students in science and engineering fields to attend Arizona's research universities;
- \$1.5 million to expand programs that increase Arizona K-12 students' knowledge of math and science;
- \$2 million for a program of paid academic or business based summer research internships for high school science and math teachers; and
- \$2 million in discretionary monies.

In addition to the favorable review, the Committee also requested that SFAz provide the Committee with a specific list of performance measures with numeric goals for the first year in its first quarterly report as well as an update of its specific long-term goals and performance measures, including numeric goals, by October 31, 2007.

JCCR MEETING

At its November 15, 2006 meeting, the Joint Committee on Capital Review (JCCR) considered the following issues:

Arizona Department of Transportation Report on Modular Buildings – The Committee gave a favorable review to the use of operating budget monies to install and lease 2 modular buildings at 1611 and 1615 West Jackson Street with the following provisions: 1) Money is not spent from the Motor Vehicle Division, 2) ADOT negotiate with the vendor to count the lease payment toward the purchase price of the buildings, and 3) ADOT inform the Committee of the purchase price of the buildings by December 15, 2006.

School Facilities Board New School Construction and New School Facilities Fund Litigation Account – The Committee deferred its review of the New School Construction Report until May 1, 2007 when the School Facilities Board (SFB) will have completed its project approval process. The New School Construction Report details the demographic assumptions, proposed construction schedule, and new school construction cost estimates for the FY 2008 year.

The SFB estimates that new school construction will cost approximately \$401.8 million in FY 2008. Of this amount, \$366.8 million is projected to be for construction projects and \$35.0 million is projected for land costs. SFB is requesting a

\$399.0 million appropriation from the General Fund to pay for new school construction in FY 2008, with the remaining revenues coming from other sources.

The Committee gave a favorable review to the report on the Litigation Account. To date the account has not made any expenditure, nor has it received any revenues.

School Facilities Board FY 2007 Building Renewal – The Committee gave a favorable review to the proposed distribution of FY 2007 Building Renewal Fund monies in 2 equal installments of \$43.1 million in November 2006 and May 2007. Prior to receiving building renewal monies, statute requires districts to submit a 3-year building renewal plan. Due to many school districts not submitting building renewal plans, only \$8.4 million will be distributed November.

Arizona State Lottery Commission Building Renewal – The Committee gave a favorable review to the \$53,600 FY 2007 Building Renewal Allocation Plan. Of this amount, \$20,000 will be used to paint the interior of its Phoenix building, \$15,000 will be used to repair the roof of the Phoenix warehouse, and the remaining \$18,600 will be for project contingencies. The Committee requested that the Lottery Commission report on the use of the \$18,600 contingency prior to its expenditure.

Arizona State Parks Board State Lake Improvement Funds – The Committee gave a favorable review to 11 State Lake Improvement Fund (SLIF) capital grants and projects totaling \$2,223,800. The review excluded \$560,000 for the design and engineering of the Town of Buckeye Recreational Lake, and \$1,232,000 for the Bullhead City boat ramp launch. The Buckeye lake project was unfavorably reviewed due to questions regarding the appropriateness of using large amounts of SLIF money to create new lakes, and the Bullhead City boat ramp was unfavorably reviewed because as per statute, SLIF money is for use on waters that allow gasoline powered boats.

Northern Arizona University New Conference/Hotel Complex – The Committee gave a favorable review to the Conference/Hotel complex project. Northern Arizona University (NAU) has entered into 2 partnerships to indirectly debt finance a 150 room on-campus hotel, a 41,000 square foot conference center, and a 344 space parking structure.

Indirect debt financing includes bond issuances or lease-purchase agreements for capital projects located on university land or that will house university activities, whereby the financing is executed by a private developer or a tax-exempt non-profit organization affiliated with the university. When calculating their debt ratio, the universities do not include indirect debt financing. For each university, statute limits the amount of debt service to be paid on all outstanding bonds and certificates of participation to 8% of total annual university expenditures.

The parking structure and conference center are estimated to cost \$16 million. Of the \$16 million, a majority of the funding will be provided through a \$12.4 million bond issuance by the Northern Arizona Capital Facilities Finance Corporation (NACFFC). The NACFFC is a non-profit limited liability company (LLC) established to support university initiatives. The partnership for the hotel requires the hotel company to finance the hotel.

Arizona State University System Revenue Bond Project – The Committee gave a favorable review to the issuance of \$18.5 million in system revenue bonds. Of the total, \$12.5 will be used to move and expand to 38,000 square feet the Police Department Facility. The remaining \$6 million will be used to clear land to build housing for 3,550 students at the proposed site of Barrett College and the South Campus Academic Village.

A private entity, American Campus Communities (ACC) will construct the 3,550 units at a cost of \$230 million. ASU will not provide financing for construction of the housing units. Upon completion of the development, ACC will transfer title to ASU, and in exchange will receive a 65-year operating agreement with revenue sharing stipulations.

The Committee requested that ASU submit the following information by December 15, 2006: 1) ASU's options if ACC does not meet minimum operating standards for the residential facilities, and 2) room and board fees for the South Campus Academic Village and Barrett College.

University of Arizona Law School Expansion – The Committee gave a favorable review to the issuance of \$7 million in system revenue bonds for the expansion and renovation of the law school, contingent on approval from the Arizona Board of Regents. The \$7 million system revenue bond represents one-third of the total project cost for a total of \$21 million. The other \$14 million will be funded by gifts prior to groundbreaking. The project includes renovation of 71,000 square feet of existing library, student organization, faculty office, and instructional space; and adds 4,900 square feet of new office space.

University of Arizona Intercollegiate Athletics Facility – The Committee gave a favorable review to the issuance of \$19 million in system revenue bonds for the Intercollegiate Athletics Facility Additions and Renovations project. The \$19 million system revenue bond represents most of the \$20 million total project cost. The other \$1 million will be funded by current university gifts. The project includes a new 18,389 square foot indoor basketball and volleyball practice facility, a 1,930 expansion of the gymnastics training facility, and a new 8,210 square foot diving pool.

SUMMARY OF RECENT AGENCY REPORTS

Arizona Department of Administration – Report on the Use of Alternative Fuels and Clean Burning Fuels in the State Motor Vehicle Fleet – Pursuant to A.R.S. § 41-803R, the Arizona Department of Administration reported on the FY 2006 year-end inventory of state-owned alternative fuel vehicles. Of the 11,946 state vehicles 5,171, or 43.3%, are subject to the alternative fuel vehicle requirements found in A.R.S. § 41-803. The vehicles exempt from these requirements fulfill one or more of the following criteria: weigh over 8,500 pounds, are law enforcement vehicles, motorcycles, ambulances, fire suppression apparatus, or are all-terrain (4x4) vehicles.

Of the 5,171 state vehicles subject to the alternative fuel vehicle requirements 2,960, or 57.2%, are alternative fuel vehicles. This is an increase of 4.5% from the prior year, and exceeds the 40% target established by statute.

A.R.S. § 41-803K, which applies to state fleets operating primarily in counties with populations exceeding 1.2 million, requires 90% of the vehicles to be capable of using alternative fuels and clean burning fuels. The state reports that of its 2,694 vehicles operating primarily within Maricopa County 2,018, or 74.9%, are alternative fuel vehicles. This is an increase of 2.2% from the prior year, but falls below the statutory requirement of 90%.

Notwithstanding the quantity of vehicles capable of using alternative fuel, a relatively small percent of users actually utilize a vehicle's alternative fuel capabilities. Of the \$6,387,781 spent on fuel during FY 2006, only \$372,897 or 5.8% was for alternative fuels.

Arizona Department of Administration – Report on FY 2007 Utilities Appropriation Shortfall – Pursuant to A.R.S. § 35-131.D, the Arizona Department of Administration (ADOA) provided notification of an anticipated shortfall in the FY 2007 allocation for the Utilities Special Line Item (SLI). Based on current expenditure levels, ADOA is projecting utility costs of \$7,432,400 in FY 2007. This is \$1,698,600 more than the Capital Outlay Stabilization Fund appropriated amount of \$5,733,800 in FY 2007. ADOA is requesting a FY 2007 supplemental appropriation from the General Fund to cover the shortfall. Without a supplemental appropriation ADOA is considering entering into interagency service agreements to have tenant agencies pay for the increased utility costs.

AHCCCS – Report on Hospital Inpatient Outlier Claims – Pursuant to Laws 2006, Chapter 331, AHCCCS has submitted a report to the Committee on the methodology used to reimburse hospitals for outlier inpatient costs and has provided recommendations for revising this methodology based, in part, on the practices of other states. Outlier claims refer to services that exceed the average cost of services or are extremely more expensive than the average cost within the service's specific category.

Although the outlier threshold is adjusted annually for inflation, these adjustments have not kept pace with the increases in hospital charges, resulting in more claims falling above the outlier threshold. Once a claim has passed the threshold, a cost-to-charge ratio (CCR) is used to determine the payment. This ratio is meant to approximate the actual cost of the services compared to the amount charged by the hospital. AHCCCS reports that the CCRs have not been updated since 1998. While hospital costs have risen 21% from 2001 to 2005, hospital charges rose 48% during that same period, resulting in higher costs for outlier payments. In FY 2001, outlier payments totaled \$10 million, which represented 2% of the total value of all inpatient claims. In FY 2005, that figure rose to \$112 million.

Due to the high number of claims that qualify as outliers, AHCCCS has recommended that the current methodology be adjusted by utilizing updated Medicare CCRs for urban and rural hospitals, omitting routine maternity stays from outlier consideration, and researching procedures or services that should be omitted or paid under a different methodology. AHCCCS estimates these changes would slow the rate of growth of outlier reimbursement and result in approximately \$185 million in outlier payments in FY 2011 if phased in over 3 years. This is \$98 million below the current FY 2011 estimate of \$283 M. Any changes to the current methodology will require statutory changes, changes to administrative rules, and changes to AHCCCS' State Plan with the Centers for Medicare and Medicaid Services.

Arizona Community Colleges – Annual Report – Pursuant to A.R.S. § 15-1427, the Arizona Community Colleges are required to report on their progress during the previous year. The FY 2006 report includes the following summary information on the state system:

- 199,081 students (headcount) were enrolled for credit, resulting in a Full-Time Student Equivalent count of 118,506
- 89% of enrolled students resided within the district, while 10% did not reside within the district
- Total number of instructors employed was 10,232, of which 2,443 (24%) were full-time and 7,789 (76%) were part-time
- Total operating revenues were \$1.1 billion (this amount excludes bond proceeds and fund balance which total \$242 million).
- Total expenditures were \$1.2 billion.

In addition, each district provided a description of their major accomplishments in FY 2006.

Arizona Community Colleges – Report on Dual Enrollment – Pursuant to A.R.S. § 15-1821.01 the Arizona Community Colleges are reporting on dual enrollment courses offered in FY 2006. Students in a dual enrollment course can earn both high school and community college credit. The courses are taught at the high schools.

Highlights of the FY 2006 report include:

- 36,750 students were dual enrolled
- 937 courses were offered, of which 366 courses were classified as Academic and 571 were Occupational
- Courses were offered at 240 locations in 9 districts
- 35,181 students, or 98% of those enrolled, completed the course
- 33,729 students earned a C or better, qualifying those students for both high school and community college credit
- 3,571 freshman and sophomore students were dual enrolled

Corporation Commission – Report on Corporations Division Filings – Pursuant to a footnote in the General Appropriation Act, the Corporation Commission submitted a quarterly report on the status of reducing processing delays in its Corporations Division.

For expedited filings, the amount of time required to process the filings fell from an average of 42 business days on March 25, 2005 to 4.6 business days on September 30, 2006. At the end of the fourth quarter of FY 2006, the turnaround time was 3.8 business days. The commission's goal for processing expedited filings is 5 business days or less.

For regular filings, the amount of time required to process the filings fell from an average of 103 business days on March 25, 2005 to 28 business days on September 30, 2006. At the end of the fourth quarter of FY 2006, the turnaround time was 23 business days. The commission's goal for processing regular filings is 30 business days or less.

Arizona Department of Corrections – Report on Expenditures – Pursuant to Laws 2006, Chapter 344 (General Appropriation Act), the Arizona Department of Corrections (ADC) is required to report on the monthly and year-to-date expenditures for the current and prior fiscal year. The report is also to include potential shortfalls, any estimated surpluses to offset the shortfalls, and a plan for eliminating the shortfall.

Based on the report, the department is now estimating a FY 2007 shortfall exceeding \$28.5 million based primarily on overtime and compensatory time expenditures. This is an increase of \$7.2 million from last month, when the department projected a FY 2007 shortfall of \$21.3 million.

Arizona Department of Corrections – Report on Monthly Bed Plan Update – The Department of Corrections (ADC) has been providing monthly reports to JLBC Staff updating the status of several topics:

Bed Update

- Arizona inmates currently occupy all of the 2,064 available provisional beds located at out-of-state facilities in Oklahoma and Texas. As mentioned in prior reports, Geo Group, the operator of the Reeves County facility in Pecos, Texas, cancelled ADC's contract for 864 of these beds. The department anticipates returning these inmates to state beds by December 15, 2006. The Oklahoma provisional

contract for 1,200 inmates expires at the end of FY 2007. ADC is currently out to bid for all 2,064 beds.

- Coconino County canceled its contract with ADC for 44 beds, effective November 3, 2006. The department is currently using all of the 48 Navajo County jail beds available and ADC plans to renew that contract shortly.

Department of Education – Budget Status Report – Pursuant to A.R.S. § 35-131(D) and a footnote in the FY 2007 General Appropriation Act, the Arizona Department of Education (ADE) recently provided an update regarding its budget status for FY 2007. In that report, ADE estimates that it will experience a \$9.7 million net funding shortfall for FY 2007, which includes an estimated \$5.1 million shortfall for Basic State Aid and an estimated \$4.6 million shortfall for achievement testing. The estimated \$5.1 million shortfall for Basic State Aid is based mostly on reported FY 2006 Average Daily Membership (ADM) counts for school districts, since FY 2007 ADM counts are not yet available. Basic State Aid costs in FY 2007 will depend on both FY 2006 and FY 2007 ADM counts, since that funding is based on current year counts for growing districts and prior year counts for non-growing ones. ADE's \$9.7 million net shortfall estimate therefore is subject to considerable change once FY 2007 ADM counts become available and potentially could change to a surplus. FY 2007 ADM counts are not expected to be available until at least February 2007.

Department of Economic Security – Report on Arizona Works Pilot Program – Pursuant to A.R.S. § 46-342, DES has provided reports submitted by MAXIMUS, the program contractor for the Arizona Works program, along with comparable DES data, for May and June 2006. This job placement pilot serves clients in District I-E, which generally covers the eastern part of Maricopa County.

In June 2006, MAXIMUS placed a total of 94 Arizona Works clients in full-time paid employment in District I-E, an 8% increase from the June 2005 figure of 87. (Over the same time period, the total number of District I-E Arizona Works clients placed by MAXIMUS in all new employment placements, including unpaid work experience and community service positions, increased 9%.) In June 2006, the number of DES JOBS clients placed in full-time paid employment in the rest of Maricopa County was 223, a decrease of (12)% from the 253 clients placed in June 2005. (Over the same time period, total DES JOBS clients placed in all new employment placements in the rest of Maricopa County, including unpaid work experience and community service positions, increased 18%.) Because of potential differences in the demographic and economic makeup of both regions, it is difficult to draw conclusions about the relative effectiveness of both programs from this data.

DES is in the selection process for statewide contracts to privatize the JOBS program. Implementation of these contracts is expected by the end of FY 2007. The current MAXIMUS contract was originally extended to December

2006 and may be extended again until the privatization transition is complete.

Department of Economic Security – Projected FY 2007 Shortfall – The Department of Economic Security (DES) is projecting a \$24 million General Fund shortfall for FY 2007. DES indicates there are 2 sources of the shortfall. First, the department projects higher than budgeted caseload growth in the CPS Residential Placement line item at a cost of \$4.3 million. For FY 2007, the Legislature provided an additional \$14.4 million for in-home and out-of-home services growth and increased out-of-home placements.

The second source of the reported shortfall is the federal Deficit Reduction Act (DRA). The DRA changed the federal match requirements for administration and training expenses in the Federal Title IV-E program serving foster children. The 50% match on administration expenditures is no longer available for expenses associated with unlicensed foster families, unless that family is in the process of being licensed. In recent years, DES has been working to put more children in relative placements, which are generally unlicensed and unpaid. DES reports that about 40% of current Title IV-E eligible foster placements are unlicensed. DES estimates that the FY 2007 shortfall created by the DRA changes will be \$14 million. This provision became effective March 1, 2006, adding \$5.7 million in one-time FY 2006 costs to the shortfall. DES is increasing the number of licensed relative placements; however, when relatives are licensed, they receive a placement subsidy, eliminating some of the savings.

DES has indicated that it will look for sources to offset as much of the shortfall as possible, including a recently announced federal adoption bonus of \$1.0 million.

Arizona Commission of Indian Affairs – Report on Uses of Monies in the Arizona Indian Town Hall Fund – Pursuant to A.R.S. § 41-545, the Arizona Commission of Indian Affairs is providing the annual Indian Town Hall Fund expenditure report for FY 2006. The fund receives monies collected or received at Indian Town Halls as fees for Commission administration. The purpose of the fund is to defray administrative costs related to Indian town halls. Statute limits expenditures from the fund to \$15,000 per fiscal year.

New fund revenues during the 26th Annual Arizona Indian Town Hall totaled \$3,792. This amount does not include the \$1,798 balance carried forward from the prior year. As of October 2006, the Commission had not utilized any of the funds in the Indian Town Hall Fund. Expenditures for the Town Hall were funded from agency operating monies, sponsor donations and fees.

City of Phoenix – Report on the Phoenix Convention Center Expansion Project – The City of Phoenix has issued its fifth progress report on the Convention Center expansion project.

The state's obligation for the Convention Center expansion project is to pay the debt service and related costs on \$300

million in construction bonds. The City's report indicates that construction will be completed in 2008, with the first year of the state's obligation beginning in FY 2010.

Based on the City's report and subsequent correspondence with the City, the following items are highlighted:

Total Project Cost – A.R.S. §9-605 provides that, in order for a project to be eligible for the state's participation in the funding of the project, the project's total cost must not exceed \$600 million.

Documentation provided by the City indicates that the current estimate for total expenditures on the project is \$659 million. The City has moved \$59 million in "soft costs" out of the total project budget in order to keep the cost under \$600 million. These additional soft costs will be funded by the City with a combination of Convention Center operating revenues and interest proceeds from the City's expansion bonds. These additional soft costs include furniture, fixtures and equipment, city staff costs, and additional consulting services.

State's Total Financial Obligation – In June 2003, during the discussion of the enabling legislation, the City estimated that the state's total financial obligation could result in approximately \$625 million of payments from state funds, including principal and interest.

Based on the bonded debt service schedule included with the City's current report, the debt service payments on the \$300 million bonds would total approximately \$852 million. This amount did not include interest earnings from unexpended funds, and proceeds from the reserve fund.

Follow-up information provided by the City indicates that, accounting for the interest proceeds and the reserve fund, the state's total financial obligation on the project will be approximately \$630 million.

Bond Interest Rate/State's Financial Obligation – The estimate of a total state financial obligation of \$625 million from June 2003 was based on an assumed bond interest rate of about 5.25%. The actual bond sale was completed in October 2005, with an interest rate on the \$300 million state's portion of 4.73%.

As noted above, the state's total financial obligation on the project is currently estimated at \$630 million. It is unclear why the state's obligation is slightly higher than the June 2003 estimate of \$625 million, yet the bonds were sold with an interest rate of over 50 basis points below the estimate. JLBC Staff has requested clarification of this issue from the City.

Arizona Department of Public Safety – Report on Staffing – Pursuant to Laws 2006, Chapter 344 (General Appropriation Act), the Arizona Department of Public Safety (DPS) is required to report quarterly on staffing levels for both crime lab and sworn personnel. The department indicates they currently have 143 authorized crime lab positions. Of this

amount, 126 (or 88.1%) are filled. In FY 2006 and FY 2007, DPS received 22 new positions. All 11 positions authorized in FY 2006 were initially filled and they are compiling a hiring list for the additional 11 positions they received in FY 2007.

DPS currently has 1,259 authorized sworn full-time positions, of which 1,109 (or 88.1%) are currently filled. Of the 69 new positions funded in the last 2 years, DPS has experienced a net increase of 25 filled positions.

Arizona Board of Regents – Report on Credit Hour Threshold FTE Student Counts – Pursuant to A.R.S. § 15-1626, the Arizona Board of Regents (ABOR) is required to report on the number of students that met or exceeded the undergraduate credit hour threshold at universities under ABOR's jurisdiction during FY 2006. A.R.S. § 15-1626 states that the Legislature shall not appropriate monies to support, and ABOR may differentiate tuition paid by, university students who have exceeded 155 credit hours in FY 2006, 150 credit hours in FY 2007, and 145 credit hours in FY 2008 and each year thereafter. A.R.S. § 15-1626 exempts certain types of credits from the undergraduate credit hour threshold, such as credits earned in a degree program that requires credits above the threshold.

ABOR reports 183 full-time equivalent (FTE) students over the 155 credit hour threshold throughout the Arizona University System as of the 21st day of the fall 2005 semester. Table 1 below summarizes the number of FTE students in excess of the 155 credit hour threshold by campus:

Table 5

**Credit Hour Threshold FTE Students
Fall 2005**

<u>Campus</u>	<u>FTE Students</u>
ASU–Main	112
ASU–East	3
ASU–West	12
NAU	14
UofA - Main	42
UofA - HSC	0
Total	183

School Facilities Board – Report on Costs for Building Renewal and New Construction at the Arizona State Schools for the Deaf and the Blind – Pursuant to A.R.S. § 15-2002, the School Facilities Board (SFB) is required to biennially report on the resources needed to fulfill the building renewal and new construction requirements in A.R.S. § 15-2031 and § 15-2041 for the Arizona State Schools for the Deaf and the Blind (ASDB). ASDB operates 2 campuses, a campus in Phoenix and a campus in Tucson. According to SFB, the total cost for building renewal for ASDB is \$582,700 in FY 2008 and \$650,700 in FY 2009. SFB also estimates new construction costs totaling \$33,882,300 for ASDB to meet minimum space estimates through FY 2010.

Arizona Department of Transportation – Report on Motor Vehicle Division Wait Times – FY 2007, 1st Quarter – The Motor Vehicle Division (MVD) was appropriated an additional 25 FTE Positions in FY 2007 for MVD customer service staff to reduce customer wait time. Wait time had increased from 14.2 minutes in FY 2003 to 27.8 minutes in FY 2006, while the number of counter clerks had decreased from 866 in FY 2003 to 698 in FY 2006.

Laws 2006, Chapter 344, requires the Arizona Department of Transportation to report to the Legislature quarterly on customer wait times in MVD field offices and vehicle registration renewal by mail turnaround times. The number of MVD counter clerks increased by 57, or 8.2%, from 698 in FY 2006 to 755 in the 1st Quarter FY 2007, with a resultant decrease of (7) minutes, or (25.2)%, in customer wait time from receiving a ticket until arriving at the counter from 27.8 minutes in FY 2006 to 20.8 minutes in the 1st Quarter FY 2007. Transaction time at the counter was unchanged at 8.3 minutes. A pilot program at 4 MVD offices (South Mountain, Scottsdale, Northwest Phoenix and East Mesa) showed an additional wait time of 7.2 minutes from arrival at the office until receiving a numbered ticket.

State of Arizona

General Fund Revenue: Change from Previous Year and June Forecast

October 2006

	Current Month					FY 2007 YTD (Four Months)				
	Change From					Change from				
	Actual	October 2005		Revised Forecast		Actual	October 2006		Revised Forecast	
	October 2006	Amount	Percent	Amount	Percent	October 2006	Amount	Percent	Amount	Percent
<u>Taxes</u>										
Sales and Use	376,890,480	\$32,305,711	9.4 %	\$9,281,480	2.5 %	\$1,500,706,833	\$130,511,274	9.5 %	\$25,938,933	1.8 %
Income - Individual	305,050,149	60,333,005	24.7	41,259,349	15.6	1,177,025,584	121,696,531	11.5	18,557,784	1.6
- Corporate	53,938,585	25,350,276	88.7	22,752,085	73.0	316,151,511	58,475,017	22.7	38,846,111	14.0
Property	888,294	(701,080)	(44.1)	(1,011,706)	(53.2)	1,326,837	(722,215)	(35.2)	(1,473,163)	(52.6)
Luxury	7,321,134	2,244,421	44.2	1,696,134	30.2	23,604,967	2,503,706	11.9	1,104,967	4.9
Insurance Premium	9,738,387	9,498,493	--	9,738,387	--	114,312,668	4,855,103	4.4	3,012,668	2.7
Estate	(66,668)	(164,812)	--	(66,668)	--	78,551	(8,950,262)	(99.1)	(121,449)	(60.7)
Other Taxes	59,879	(5,346)	(8.2)	(5,246)	(8.1)	212,696	(4,664)	(2.1)	(47,804)	(18.4)
Sub-Total Taxes	\$753,820,240	\$128,860,668	20.6 %	\$83,643,815	12.5 %	\$3,133,419,647	\$308,364,490	10.9 %	\$85,818,047	2.8 %
<u>Other Revenue</u>										
Lottery	4,113,300	554,400	15.6	213,300	5.5	10,807,500	2,390,800	28.4	(992,500)	(8.4)
License, Fees and Permits	3,763,816	1,332,491	54.8	448,216	13.5	16,263,267	5,797,278	55.4	3,521,567	27.6
Interest	7,293,512	3,115,500	74.6	2,293,512	45.9	25,568,567	13,766,768	116.6	8,368,567	48.7
Sales and Services	3,266,904	(56,112)	(1.7)	(478,296)	(12.8)	13,167,952	(3,477,874)	(20.9)	(1,967,948)	(13.0)
Other Miscellaneous	3,812,952	2,014,433	112.0	2,643,052	225.9	9,847,542	4,304,838	77.7	5,786,642	142.5
Disproportionate Share	0	0	--	0	--	0	0	--	0	--
Transfers and Reimbursements	138,914	(4,951)	(3.4)	(561,086)	(80.2)	936,096	(2,607,904)	(73.6)	(2,863,904)	(75.4)
Sub-Total Other Revenue	22,389,398	6,955,761	45.1 %	4,558,698	25.6 %	76,590,924	20,173,906	35.8 %	11,852,424	18.3 %
TOTAL BASE REVENUE	\$776,209,638	\$135,816,429	21.2 %	\$88,202,513	12.8 %	\$3,210,010,571	\$328,538,396	11.4 %	\$97,670,471	3.1 %
<u>One-Time Revenue</u>										
Urban Revenue Sharing	(45,935,888)	(10,500,144)	29.6	0	0.0	(183,743,552)	(42,000,576)	29.6	0	0.0
'05 Budget Balancing Transfers	0	0	--	0	--	0	0	--	0	--
'07 Disproportionate Share	0	0	--	0	--	0	0	--	0	--
'06 In-Lieu Transfer	0	0	--	0	--	0	0	--	0	--
Sub-Total Transfers In	(45,935,888)	(10,500,144)	29.6 %	0	0.0 %	(183,743,552)	(42,000,576)	29.6 %	0	0.0 %
TOTAL REVENUE	\$730,273,750	\$125,316,285	20.7 %	\$88,202,513	13.7 %	\$3,026,267,019	\$286,537,820	10.5 %	\$97,670,471	3.3 %