

Fund Categories

State General Fund is the largest source of funding for the state operating budget; its primary revenue sources include state sales, income and corporate taxes. Monies in this fund are appropriated each fiscal year for general government purposes. For example, state tax collections are annually appropriated to state agencies to run state programs.

Other Appropriated State Funds consist of 273 separate funds that are earmarked for specific purposes by law through legislation or ballot proposition. Their revenues include fees and taxes. For example, the legislature imposes licensing fees on physicians; these fees are collected and deposited in the Medical Examiners Board Fund and are used for regulatory and oversight purposes. Even though, by law these monies are held in a separate fund for specific purposes, they must be appropriated each fiscal year. Through ballot propositions, the voters imposed a luxury tax on tobacco products; a portion of these monies are considered Other-Appropriated Funds and are deposited in the Tobacco Tax and Healthcare Fund. They are earmarked for healthcare services for the indigent, smoking prevention education and healthcare research.

Non-Appropriated State Funds are made available without legislative action unless the legislature takes action to alter the law that created the fund. An example of a non-appropriated fund is the Hazardous Waste Management Fund used by the Arizona Department of Environmental Quality. Monies in this fund are primarily derived from funds collected from hazardous waste generators and operators of hazardous waste facilities. These funds are used to support education, prevention and compliance related to hazardous waste management in Arizona.

Federal Funds are the second largest source of funding for the state operating budget. Federal funds come to the state from the federal government in multiple forms for numerous purposes. For example, AHCCCS receives matching funds from the federal government to support healthcare costs. In FY 2002 64% of AHCCCS's budget came directly from the federal government. In general, federal funds are not appropriated. However, there are some limited federal funds that are appropriated. Examples include: Department of Labor funds and child-care block grants.



Policy Brief

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Making Sense of the State Budget

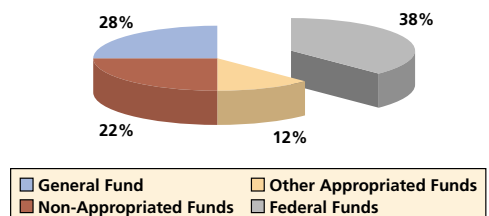
The State of Arizona's Operating Budget and Factors that Influence State Spending

The state budget is complex. There are various funds, multiple funding mechanisms and a long list of state spending requirements. Understanding the pieces that comprise Arizona's operating budget and the public policies that affect its construction are crucial prerequisites to understanding state spending. This brief provides an overview of Arizona's operating budget, examines its components and illustrates how the citizen initiative process, legislative actions and court decisions have influenced state spending over the last decade.

State Operating Budget

Recent state revenue shortfalls requiring cuts in agency operations and programs have received considerable attention. Previous analyses have focused largely on the \$6 billion General Fund. So much attention has been directed to the General Fund some may believe that the state's budget is \$6 billion. In fact, the General Fund actually represents only 38% of the state's \$16.4 billion operating budget in Fiscal Year (FY)ⁱ 2003 (*Figure 1*). When combined, the Other Appropriated Funds, Federal Funds and Non-Appropriated Funds make-up the remaining 62% of the FY 2003 operating budget. In order to provide a more comprehensive view of the state's budget, this analysis will examine total operating spending which includes all four fund categories.

Figure 1
FY 2003 State Operating Budget



Note: From JLBC Appropriations Report, FY 2003.

■ Budget Bills

For the purpose of unraveling the state's operating budget the General Appropriations Bill, also known as the "Feed Bill", and the Omnibus Reconciliation Bills (ORBs)ⁱⁱ are among the most useful budgeting documents. These bills are the principal vehicles through which the legislature appropriates monies and directs state policy. The General Appropriations Bill only appropriates monies for the operation of state government. The ORBs are sep-

ⁱ Arizona's fiscal year runs from July 1 of one year thru June 30 of the following year.

ⁱⁱ Typically there are three types of ORBs: Health & Welfare, Public Finance and Education.

rate bills effective for one year, that make temporary policy changes to enact the provisions of the General Appropriations Bill. It is easiest to think of the General Appropriations Bill as the bill that distributes the money and the ORB as the bill that implements budget policy.

■ Who Appropriates the Funds that Make-up the State's Operating Budget?

The Arizona Constitution has some unique features that empower the governor, the legislature and the people of the State of Arizona in the appropriations process. Article 9, Section 5 of the Arizona Constitution gives *almost* exclusive appropriation authority to the state legislature. However, Arizona gives the governor line-item veto authority, meaning the governor can veto a specific appropriation within a bill without vetoing the entire bill. Further, the Arizona Constitution, like that of 23 other states, provides for citizen-driven initiatives that can direct state policy and spending.¹

■ Governor's Ability to Direct Spending

As the presiding elected official in the State of Arizona, the governor is responsible for setting a public policy agenda that includes spending priorities. The State-of-the-State address, delivered at the opening of each legislative session, is where the governor outlines priorities for the coming year. The State-of-the-State address can be a powerful tool in setting the tone for budget deliberations. However, the governor only has the ability to propose a budget; the governor cannot introduce or enact a budget bill.

The governor's budget office, the Office of Strategic Planning and Budgeting (OSPB), works directly with the governor to put together the governor's budget proposal. State law² requires the governor to present a budget no later than five days after the beginning of the regular legislative session. After the governor presents a budget, the state legislature analyzes it and presents a budget of their own. The governor's budget can be very similar or vastly different from the legislature's budget – whatever the case, the legislature is given the ultimate authority to draft and approve a final budget bill for the governor's consideration. The governor then has the option to accept the bill in its entirety or to veto all or part of the bill. If the governor elects to veto a bill, a two-thirds vote of the legislature is required to override the governor's veto. If the governor fails to take action on the bill – i.e. doesn't veto the bill or sign the bill into law – it will automatically become law in five days if the legislature has not adjourned and ten days if the legislature has adjourned.

■ Legislature's Ability to Direct Spending

The state legislature has the primary responsibility for developing and adopting a state budget. Leadership in both houses generally set the policy direction while the chairs of the appropriations committees in both houses are responsible for overseeing the process. The Joint Legislative Budget Committee (JLBC) staff is the legislature's budget staff. They work directly with the appropriations chairs to analyze the governor's budget and develop a budget proposal for consideration by the state legislature.

Budget Tools

The two most obvious budgeting tools available to the legislature are cutting spending and raising taxes. However, there are other methods to balance the budget that include: transferring dedicated funds to the General Fund, deferring payment of financial obligations, conditionally appropriating monies for state programs or services, known as "triggers", and withdrawing monies from the Budget Stabilization Fund. In all cases, the legislature and governor review their decisions each fiscal year and use one or more of these tools depending upon the disparity between state revenues and expenditures.

Because legislators are responsible for introducing and voting on budget bills, they have a number of tools at their disposal that are not available to the governor.

Fund Sweeps: Notwithstanding Clause

The legislature may transfer monies from one fund to another using a *notwithstanding* clause. The notwithstanding clause is a budgeting tool that essentially suspends the law establishing a fund and allows the legislature to redirect monies collected for a specific purpose and transfer them to the General Fund. Use of the notwithstanding clause is typically found in the budget ORBs.

Notwithstanding Clause Example

Established within statute, the State Lake Improvement Fund (SLIF),³ administered by the State Parks Department, is an Other Appropriated Fund that receives funds from watercraft license taxes and motor vehicle fuel taxes. The SLIF is dedicated for use on projects at boating sites, lake improvements and construction, campgrounds, as well as a number of other uses. Over the past two fiscal years, the legislature, with the governor's approval, has transferred \$16 million (\$6 million in FY 2002⁴ and \$10 million in FY 2003⁵) from the SLIF to the General Fund.

In October 2002, the legislature used the notwithstanding clause to redirect more than \$141 million to the General Fund.⁶ It is important to note that when money is redirected from a specific fund to the General Fund, the underlying statute is generally left unaltered and the affected state agency is still required to provide services.

Expenditure Deferrals

Expenditure deferral is a common budgeting tool that defers a financial obligation from one fiscal year to the next. The legislature can defer payments, projects or programs without eliminating the statute that created them. This tool is a stop-gap or short-term solution to a budget shortfall because the state's financial obligation is not eliminated, it is simply postponed until a future date with the expectation that future revenues will be available to pay off the outstanding balance.

Expenditure Deferrals Example

In the FY 2003 First Special Session the legislature delayed a \$100 million appropriation to the School Facilities Board from FY 2003 to FY 2005. The \$100 million will be added to the FY 2005 obligation.⁷

Subject to Legislative Appropriations

Another budgeting tool at the legislature's disposal is the *Subject to Legislative Appropriations* clause. The Subject to Legislative Appropriation clause allows legislators to pass legislation and allocate funds without committing a future legislature to continue the appropriation. The language is interpreted exactly as written – funding for a program that the legislature approves today is subject to a future legislature's approval to continue it. Alternatively, the legislature can incorporate the term “shall” into the statute thereby obligating the state to provide funds in the future, unless the statute establishing the program is modified or repealed. Failure to provide adequate funding for a program that is statutorily

Arnold v. Sarn

In the early 1980's the legislature passed legislation stating the state “shall” provide community behavioral health services. In 1986 the trial court entered a judgment holding the state had violated its statutory duty because it had not adequately appropriated funds to support a community behavioral health program established by the state legislature. In 1989 the Supreme Court affirmed that decision.⁸ The final cost of *Arnold v. Sarn* is yet to be determined. However, in FY 2002, the legislature appropriated \$50 million from the tobacco litigation settlement to the Serious Mental Illness Fund to move the state towards meeting the requirements of the court.

prescribed leaves the legislature and governor open to legal challenges from affected parties. The courts are then given the power to direct the state to meet specific provisions based upon their interpretation of the law.

Contingency Appropriations: “Triggers”

A trigger is essentially a contingency appropriation and/or tax cut that occurs only if revenues exceed forecasts. If actual state revenue collections reach certain levels, funding is made available in the following fiscal year for predetermined agency programs or additional personnel.

The primary goal of contingency spending is to set funding priorities should additional funds be available at the close of the fiscal year. During economic downturns, revenue collections rarely exceed forecasts.

Triggers Example

There were three triggers in the FY 2002 budget. If revenues exceeded the forecast by \$50 million the first conditional appropriation would have triggered to pay for ten different state agency activities or personnel. The second trigger would have appropriated monies for various programmatic and capital expenditures. The third trigger would have implemented a reduction in the corporate income tax formula. Combined, the three triggers would have authorized \$75.4 million in additional spending. However, actual revenues fell short of FY 2002 forecasts therefore, no contingency spending was triggered.⁹

■ Legislative Strategies for Closing Annual Spending and Revenue Gaps

After revenues have been projected and the governor, the legislature, the public and the courts have sliced out their respective pieces of the budget, there remains a good deal of uncertainty about whether there will be enough money to meet all of the demands on state government. When the operating budget falls short, the legislature has turned to the Budget Stabilization Fund (BSF) and sale-leaseback transactions for cash infusions.

Budget Stabilization Fund

The Budget Stabilization Fund (BSF), also known as the *Rainy Day Fund*, was established in 1990. The BSF was designed to set revenues aside when the economy is prospering to be used when the economy is sluggish. The legislature has amended the amount of funding to the BSF five times since its inception. Monies deposited in the BSF

Recent Uses of the Budget Stabilization Fund

In FY 2002 \$173.5 million was transferred to the General Fund to balance the budget. In FY 2001 and FY 2002 combined, an additional \$130 million was transferred from the BSF to cover alternative fuels credits. From FY 2000 to FY 2003 \$77.5 million was transferred for the construction of the Arizona State Hospital, the BSF was later reimbursed \$40 million from the Tobacco Settlement Fund.¹⁰

have been used to balance the state budget, to fund state hospital construction and to help pay claims resulting from the alternative fuels legislation.

Sale-Leasebacks and Lease-Purchase of State Assets

The sale-leaseback of state assets allows the state to sell off assets, like government buildings, creating one-time infusions of cash to the General Fund. After the asset is sold, the state enters into a long-term lease agreement with the new owners and the cost of occupying the building is absorbed as an operational expense instead of a capital expense. Similarly, the state has entered into lease-purchase arrangements for the construction of buildings in which the state signs a long-term lease to occupy a building and then takes title to the building at the end of the lease. In both cases, the lease payments are subject to annual appropriation and are not considered long-term debt.

The reasons that sale-leasebacks and lease-purchases are important budgeting tools are two-fold. First, by freeing up money in the state's budget, the legislature and governor are able to fund new programs, meet ongoing expenses, purchase equipment or finance capital expenses without exceeding available revenues. Second, the lease options allow the state to purchase or utilize capital without violating the constitutional limit on borrowing money.ⁱⁱⁱ

Citizen's Ability to Direct Spending

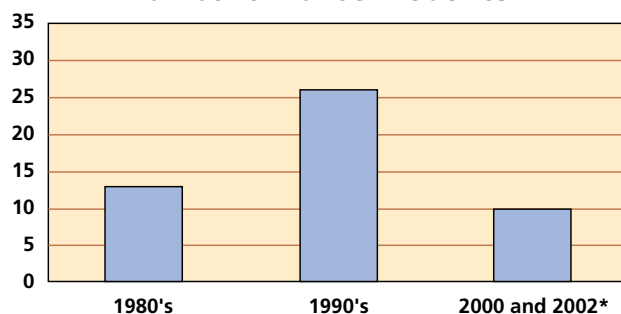
Since statehood, Arizona has used the citizen initiative and citizen referendum process as a means of checking the power of state government. And, with increased frequency, Arizona vot-

ⁱⁱⁱ The state constitution limits the aggregate amount of long-term debt held by the state to \$350,000 (Article 9, Section 5); financing strategies such as those described have allowed the state to accumulate approximately \$4.7 billion in long-term obligations at the close of FY 2002.

^{iv} Numbers do not include referenda sent to the ballot by the legislature.

ers have turned to the ballot to direct state policy and spending. During the 1990's there were 26 citizen-driven ballot measures^{iv}, double the number that appeared on the ballot in the 1980's (*Figure 2*). Over the same two decades, voters also passed a higher percentage of the measures on the ballot. During the 1980's, only 31% of the citizen-driven ballot measures were successful, while voters approved 50% in the 1990's.¹¹ In the 2000 and 2002 general elections, 50% of the proposed initiatives and referenda on the ballot passed.¹²

Figure 2
Number of Ballot Initiatives



Update, May 9, 2003 – Numbers have been changed to reflect petitions for Constitutional Amendments, Referendum Measures and Initiative Measures.

Note: From Arizona Legislative Council Memo, Constitutional Amendments, Referendum Measures, Initiative Measures, Salary Commission Recommendations, February 14, 2003

* While there have been ten initiatives on the ballots in this century, only two general elections have been held.

In the last decade, the ballot has been used to direct state spending and to limit the legislature's control of state spending. In 1992, voters passed Proposition 108 requiring a supermajority (two-thirds) of the legislature to pass a tax or fee increase, or to eliminate or reduce any existing tax deductions, exemptions or credits.¹³ Moreover, if the governor vetoes a tax increase, a three-quarters vote of the legislature is needed to override the veto. A second initiative known as the "Voter Protection Act" (*Prop. 105, 1998*) amended the constitution to prohibit the legislature and

Voter Protection Act

Since passing the Voter Protection Act voters have approved several ballot propositions that increase or divert state spending including: dedicating \$20 million annually for 11 years to purchase public land for conservation (*Prop. 303, 1998*); increasing the state sales tax to fund K-12 public education (*Prop. 301, 2000*); diverting certain revenues from the Permanent School Fund to the Classroom Site Fund (*Prop. 300, 2000*); and, expanding AHCCCS eligibility criteria (*Prop. 204, 2000*).

the governor from repealing any voter approved initiative or referendum.¹⁴ This combination of insulating spending increases and discouraging new taxes limits the flexibility of the legislature and governor to manage the budget.

■ Court's Ability to Direct Spending

Unlike the governor, legislature and the citizen initiatives, the courts do not make policy but instead are responsible for interpreting law. Over the past two decades the courts have authored multiple decisions that have affected the demands on the state's operating budget. Noteworthy among them is the requirement to equalize public school facilities (Roosevelt v. Bishop, 1994). In Roosevelt v. Bishop, the Arizona Supreme Court held that the state's statutory scheme for financing public school facilities and equipment violated the Arizona Constitution due to widespread disparities between school districts.¹⁵ The Court issued a judgment requiring the state to remedy the funding disparity. In 1997 the state legislature passed Students FIRST and created the School Facilities Board (SFB) to resolve the suit. Students FIRST shifted financial responsibility for public school construction and

Roosevelt v. Bishop

In FY 2002 the School Facilities Board (SFB) received more than \$384 million in General Fund appropriations to construct and maintain local schools. Since its inception the SFB has spent over \$1.5 billion – using a combination of General Fund monies and revenue bonding to finance school construction.¹⁶

maintenance from local property taxes to the state General Fund. The SFB was created to administer the statewide school capital program and was charged with “ensuring that school buildings and equipment meet the appropriate guidelines for Arizona pupils to achieve academic success...”¹⁷

In other cases, class action suits have resulted in settlement agreements that commit state funds and bind the state to a defined course of action. A recent example of such a case is Ladewig v. Killian (2002). The Ladewig settlement agreement requires the state to refund approximately \$350 million in taxes paid on dividends earned from out-of-state companies.¹⁸ In Bonn v. Waddell (1993), the Arizona Supreme Court held that the state could not impose income taxes on the retirement benefits of federal retirees if it exempted state retirees. Consequently, the state paid refunds totaling more than \$84 million.¹⁹

Growth in the State Operating Budget

The state operating budget directs the amount of monies available for the day-to-day operating expenses of state agencies and state programs. The operating budget does not generally include monies used for capital expenses.

Arizona's total operating budget in FY 1992 was \$8.4 billion,²⁰ compared to \$15.5 billion in FY 2002.²¹ A quick look at these numbers might lead some to believe that the state's operating

Examples of Capital Expenses

In addition to the \$3.4 billion K-12 operating budget, the state appropriated more than \$384 million from the General Fund to the School Facilities Board in FY 2002 for the purpose of building and maintaining local schools.²² The Arizona Department of Transportation (ADOT) is not among the top eight agencies in terms of operating expenses. However, when capital expenses are included ADOT is the state's fourth largest agency with a budget of about \$1.2 billion in FY 2002.²³

budget had almost doubled in a decade. However, these raw numbers do not take into consideration how the value of a dollar has changed. A dollar in FY 1992 was worth more than a dollar in FY 2002 and in order to compare FY 1992 spending to FY 2002 spending, the dollars have to be adjusted for inflation. Using the GDP Deflator, the state's total operating budget has outpaced population growth with a 54% increase in spending from FY 1992 to FY 2002 compared to a 42% increase in the state's population.

When considering how the state's operating budget has grown, it is important to take into account how spending has changed relative to the demand for state services that result

Inflation Adjustment

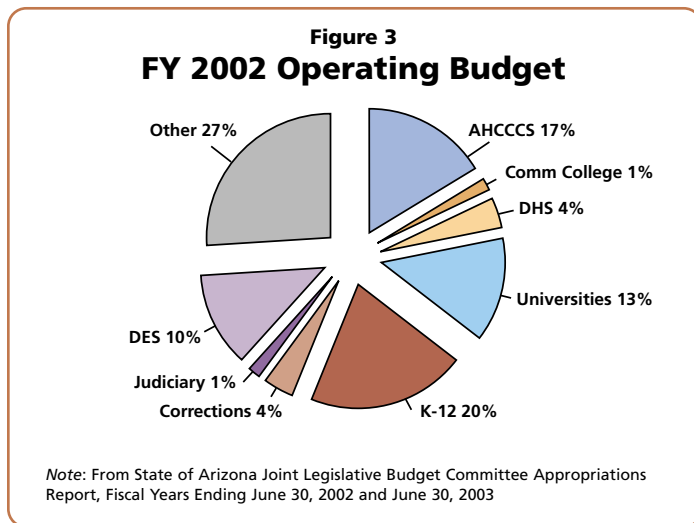
Economists often disagree on whether the Consumer Price Index (CPI) or the Gross Domestic Product (GDP) Deflator produces a more reliable figure for inflation. The annual difference between the CPI and the GDP Deflator is rather small. However, calculating inflation with the GDP Deflator generally results in lower inflation values than the CPI and the cumulative difference between the two measures creates different impressions of whether government spending has outpaced population growth over the past decade. When the CPI is used to adjust for inflation, the state's total operating budget has kept pace with population growth, with a 42% increase from FY 1992 to FY 2002. *Note:* The State of Arizona uses the GDP Deflator to adjust for inflation, while the federal government uses the CPI as a cost of living adjustment for federal programs.

from population growth. According to the Arizona Department of Economic Security,^v Arizona's population was 3,858,850 in 1992 and grew by 42% to 5,472,750 in 2002.²⁴ Spending relative to population growth is a measure that is often used to opine whether government is growing too fast. This measure, however, does not take into account how the state's population profile has changed or how service needs have shifted.

Agency Growth

There are 110 state agencies; however, 78% of the state's total operating budget in FY 2002 was consumed by just eight of those agencies.²⁵ A closer look at the eight agencies with the largest operating budgets provides a good picture of how ballot propositions, legislative actions and court mandates have altered the distribution of operating monies. Among the largest agencies there is broad disparity in how much the respective budgets have increased over the past decade. The difference results from the fact that state budgeting is a zero-sum game, that is, more funds for one agency means less for another, unless revenues are increasing.

There are two different methods used to examine agency growth. The first is percentage growth. Percentage growth measures how much an agency's operating budget has grown over time. In other words, how big an agency is today relative to its size ten years ago. The second is absolute dollar growth. Absolute dollar growth simply illustrates how much more money an agency is appropriated today than was appropriated ten years ago.



^v The DES population figures are estimates based on population projections – these projections have historically underestimated actual population growth.

Table 1
Changes in the Eight Largest Agency Budgets
Total Dollar and Percent Change Between FY 1992 – FY 2002
Adjusted for Inflation (GDP)

| Agency | \$ Change | % Change | % Ranking |
|---------------------------------------------|-----------------|----------|-----------|
| Arizona Department of Education | \$1,095,912,000 | 63% | 5 |
| Arizona Health Care Cost Containment System | \$891,050,000 | 77% | 4 |
| Department of Economic Security | \$444,108,000 | 45% | 6 |
| Arizona Department of Health Services | \$270,132,000 | 100% | 1 |
| Corrections | \$239,671,000 | 87% | 2 |
| Universities | \$209,712,000 | 14% | 8 |
| Judiciary | \$73,203,000 | 85% | 3 |
| Community Colleges | \$27,378,000 | 31% | 7 |

Education

K-12

The Arizona Department of Education (ADE) is responsible for providing public education to children in kindergarten through twelfth grades. Between FY 1992 and FY 2002, ADE funding lead all state agencies in absolute dollar growth, increasing by more than \$1 billion.²⁶ This amount represents a 63% increase in funding for maintenance and operation costs and does not include state expenditures for capital improvements to school facilities (*See "Examples of Capital Expenses" inset*).

The increase in expenditures over the past ten years can be attributed to three major causes. The first is a 35% increase in the number of school age children in the state over the last decade.²⁷ Second, Proposition 301, also known as Education 2000, increased the state sales tax by six-tenths of a percent for 20 years. These tax revenues are directed toward classroom spending in the K-12 system, as well as spending for the community col-

Voter Participation Affecting K-12

Prop 301, passed in 2000 raised more than \$439 million in FY 2001 and FY 2002 combined.²⁸ Approximately 85% of the revenues are dedicated to K-12 education, 12% to universities, and 3% to community colleges. In addition to dedicating a revenue stream, Prop 301 also required the legislature to increase the K-12 base support level from the General Fund by \$94.5 million, increasing annually by 2% or inflation, whichever is less.²⁹ In FY 2002 the increase cost the state over \$62 million.³⁰

leges and universities in the state. Third, federal funds increased by almost \$200 million between FY 1992 and FY 2002.³¹

Higher Education: Universities and Community Colleges

Of the top eight agencies, higher education budgets consistently rank among the lowest in percentage growth with 14% growth for universities and 31% for community colleges. However, the state’s contribution to higher education represents only a portion of total operating expenditures by the universities and community colleges. Universities and community colleges receive approximately 61% and 80% respectively, of their total funding from sources other than state appropriations (*Table 2*).

| Universities* | | Community Colleges** | |
|-------------------------------------------------|-----|-----------------------------|-----|
| General Fund Appropriations | 39% | Primary Property Taxes | 49% |
| Federal Government, Gifts, Grants and Contracts | 29% | Tuition and Fees | 23% |
| Tuition and Fees | 18% | General Fund Appropriations | 20% |
| Other Sources | 14% | Other Sources | 8% |

* FY 2002 State University Financial Statements
** State of Arizona Joint Legislative Budget Committee

As with K-12 education, a large portion of the increase in annual expenditures for higher education can be attributed to enrollment growth. The universities full-time student population^{vi} has grown by 16% between 1992 and 2002,³² while the community colleges have seen a 22% increase in full-time students.³³

■ Judiciary

Arizona’s judicial branch is an integrated system that consists of the Supreme Court, court of appeals, superior courts and limited jurisdiction city and county justice of the peace courts. In terms of percentage growth, the judiciary ranks third among the largest agencies. Much of

Legislative Action Affecting Judiciary

In 1988 the legislature established the Community Punishment Program, which increased the number of people on probation. The program was established to provide behavioral treatment dollars and allow for intensive supervision, such as electronic monitoring. In 1992 the legislature passed legislation to divert 408 offenders from the state corrections system and 275 offenders from the county jail system to the Community Punishment program.³⁴ Further, in 1993 the legislature provided more funding to hire probation officers thereby increasing the judiciary budget to defray the costs of the Community Punishment program.

the growth in the judiciary is directly attributed to the courts’ increased responsibility for the adult probation population. Prior to the mid-1980’s probation programs were funded almost exclusively by counties. In the 1980’s the legislature began appropriating significant state funds to the judiciary for adult probation as well as adding the Juvenile Intensive Probation Supervision program. In FY 2002 approximately 65% of the judiciary’s \$167 million operating budget was dedicated to providing probation services.³⁵

The voters have also played a role in increasing program responsibilities and consequently, funding for the judiciary. In 1996 voters passed Proposition 200, known as the Drug Medicalization, Prevention and Control Act. The Act expanded drug treatment and education to individuals convicted of drug possession for the first or second time and assigned administration of the new programs to the judiciary.

■ Department of Corrections

The Department of Corrections (DOC) is responsible for incarcerating and rehabilitating adult inmates in correctional facilities and for supervising parolees. DOC’s budget is primarily driven by an 80% increase in the inmate population from 1990 to 2000, almost double the state’s rate of population growth during the same period.³⁶ As of February 2003, there were 30,083 inmates in the state’s prison system.³⁷

Legislative policy related to criminal sentencing and parole have exacerbated prison population growth. During the 1980’s the legislature passed mandatory sentencing guidelines requiring certain offenders to be sentenced to a specified amount of time and by doing so removed some of the courts’ sentencing discretion. In 1994 the legislature passed “truth in sentencing” legislation requiring violent offenders to serve 85% of their prison sentence.³⁸ Mandatory sentencing coupled with truth in sentencing has increased the length of the actual prison sentence and ensured that inmates serve more of their sentence. Both mandatory sentencing and truth in sentencing legislation have contributed to the rise in the state’s prison population and the growth in the DOC budget.

■ Social Service Agencies: DES, DHS, AHCCCS

The social service agencies include the Department of Economic Security (DES), the Department of Health Services (DHS), and the Arizona Health Care Cost Containment System (AHCCCS). Each of these agencies is among the top growth agencies in

^{vi} The full-time student count is generated by calculating one full-time student for each 15 student credit hours produced in lower-division undergraduate courses, each 12 student credit hours produced in upper-division undergraduate courses, and each ten student credit hours produced in graduate courses.

Voter Participation Affecting Social Service Agencies

In 2000 voters passed Proposition 204 which raised AHCCCS income eligibility limits to 100% of the Federal Poverty Limit (FPL). The initiative has increased participation in all three social service agencies. Prior to Proposition 204, eligibility for health-care services was at 33% of FPL or \$2,963/year. Now, a person can qualify for AHCCCS at 100% of FPL if they earn less than \$8,980/year, the equivalent of \$4.32/hour. *Note:* This new population represents 9% of the total AHCCCS population. The remainder of the AHCCCS participants are eligible for services at higher levels of income ranging from 100-400% of FPL.³⁹

absolute dollars and percentage growth. More so than most, the social service agencies are subject to the ebb and flow of the economy. As the economy falters, enrollment in programs covered by these agencies tends to grow. However, voter participation and legislative actions have expanded enrollment eligibility and the growth in these agencies is greater today than it would have been given the same economic conditions a decade ago.

All three social service agencies have experienced enrollment growth that is directly attributed to the passage of Proposition 204 in 2000. Proposition 204 expanded the AHCCCS eligibility pool allowing more people to qualify for state-sponsored healthcare services.

DES

The Department of Economic Security (DES) is responsible for providing human service programs including employment assistance, job training, child and adult protection, childcare subsidies, cash assistance and services for the developmentally disabled. Unlike DHS and AHCCCS, DES' budget growth has basically kept pace with population growth.

DHS

The Department of Health Services (DHS) leads the eight largest agencies in percentage growth. DHS is responsible for

Legislative Action Affecting DHS

In 1989 Congress mandated that all states offer behavioral health services for Medicaid eligible persons under the age of 21. The state legislature authorized the addition of this population and began to phase-in eligible individuals in 1990. By the end of FY 2002 the state was delivering behavioral health services to approximately 91,000 people annually and was providing prevention services to 177,000 people annually.⁴⁰ The state spent more than \$571 million in FY 2002 providing behavioral health services.⁴¹

a whole array of services including public health, licensing health and childcare facilities, behavioral health and the operation of the Arizona State Hospital. The largest factor in the growth of DHS is the addition of behavioral health services that resulted from a 1989 congressional mandate adopted by the state legislature.

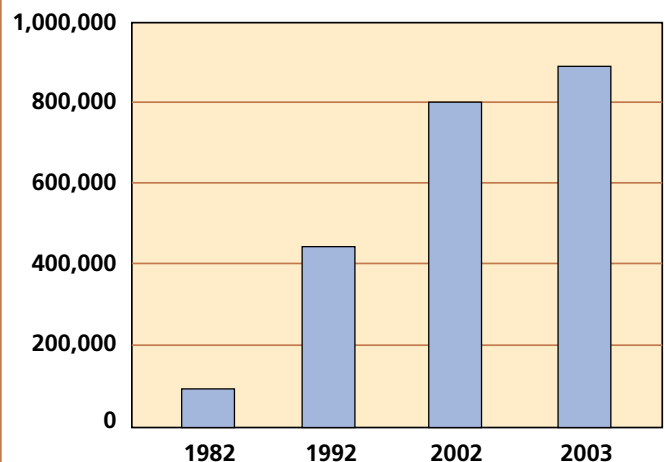
In addition to legislative action, DHS' operating budget has been significantly impacted by court decisions. The DHS was a party to the Arnold v. Sarn (1989) lawsuit in which the state Supreme Court entered judgment against Maricopa County, requiring the improved delivery of behavioral health services. More recently, the federal court approved a settlement agreement pursuant to a class action suit Jason K. v. Eden (2001) that calls for DHS to make a number of system reforms focused on the delivery of behavioral health services to children. Funding for behavioral health services currently makes up 80% of DHS' annual budget.

AHCCCS

The Arizona Health Care Cost Containment System (AHCCCS) is the second largest state agency. It is probably the most dynamic of the social service agencies because its budget has been impacted by a whole host of policy changes.

In 1982 Arizona entered into an agreement with the federal government to begin providing healthcare. Over the course of two decades, AHCCCS has gone from providing healthcare to 89,683 people, or 3% of the state's population, to providing healthcare to 786,763 people, or 16% of the state's population.⁴² Today, AHCCCS enrollment is over 889,953 individuals – almost ten times the number of people covered in 1982.⁴³

Figure 4
Growth in AHCCCS Population



Note: From <http://www.ahcccs.state.az.us>

Voter Participation Affecting AHCCCS

In 1994 voters passed Proposition 200 which increased the state luxury tax on tobacco products. Revenue generated from the tax is dedicated to healthcare and education research related to reducing/preventing tobacco use. To date, Proposition 200 has added more than \$843 million in healthcare funds to AHCCCS, DHS and DES.⁴⁴ Voters returned to the polls in 2002 to pass another tobacco tax to cover expanded eligibility in AHCCCS, emergency health services and health research and education. According to JLBC, the tax has generated over \$18 million in new revenues.

While some of the growth in AHCCCS has resulted from population growth, AHCCCS has experienced a good deal of growth as a direct result of an increased number of eligibility categories. In 1982 there were basically three eligibility categories. Today, there are 19 different ways to qualify for AHCCCS. Expanded eligibility has resulted from both legislative action and the passage of ballot propositions.

There have been a number of legislative policy decisions that affect how AHCCCS delivers service and to whom they are delivering service. The addition of long-term care services in 1988 and KidsCare in 1998 have had the most notable impact on AHCCCS costs and enrollment.

Legislative Action Affecting AHCCCS

As of June 30, 2002, the ALTCS population represented only 4% of AHCCCS participants, but consumed 21% of the agency's budget. KidsCare enrollment has grown by 70% since 1999 and cost the state almost \$141 million in FY 2002.

In 1987 the legislature established the Arizona Long-Term Care System (ALTCS) for the delivery of long-term care services. ALTCS began to phase-in service in December 1988.^{vii} The developmentally disabled were the first population to receive services and the physically disabled elderly were added shortly thereafter. Today, ALTCS provides services to more than 36,000 individuals.⁴⁵

Later, the legislature passed KidsCare, which expanded healthcare eligibility up to 200% of the FPL for the households of children 18 and under. KidsCare had a dual impact on AHCCCS enrollment. The intended impact was to enroll children who would not have otherwise been eligible for healthcare in existing AHCCCS programs. However, in identifying children who were eligible for KidsCare, approximately 120,000 children were found to be eligible for existing programs in AHCCCS while another 50,000 were eligible for healthcare services through KidsCare.⁴⁶

Citizen-driven referenda have had a dramatic impact on AHCCCS enrollment. In 1994 voters approved the first tobacco tax referendum by a slim margin – 51% of the vote. Revenues from the tax were largely earmarked for healthcare services. In 2002 voters approved a second tobacco tax that is also largely dedicated to healthcare services.

In carrying out the will of the voters, the legislature and the courts, the social service agencies have seen dramatic enrollment growth over the decade. As the voters, the legislature and the courts make decisions about who should receive services, the agencies must manage their resources to meet the ever-changing demand.

Wrap Up

In addition to providing a road map of the state budget, this brief also describes how the operating budgets of eight of the state's agencies have been impacted by the actions taken by key players. Generally speaking, the state's rapid population growth over the last decade is a major cause for the growth of these agencies' budgets. More specifically, changes to the scope of state programs have accelerated growth for the state agencies that provide criminal justice and social services.

This brief is a solid foundation to expand the analysis of the state budget. However, no discussion of the state's budget process is complete without a description of the revenue sources available to the state to fund the operations of state government.

The Arizona Center for Public Policy will build upon this brief to develop a comprehensive analysis of the state's budget to include issues such as the roles of state revenues and capital spending.

^{vii} Prior to 1988 the counties were responsible for providing long-term care services.

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