

Treasurer Dean Martin's Budget Reform and Debt Restructuring Proposal

Arizona's General Fund Budget began the year facing a \$1.45 billion shortfall in FY 2010 and \$2.5 billion Shortfall in FY 2011. The deficit is the result of poor fiscal management since March of 2007. Spending continued to increase for two consecutive years following the decline in revenues. Further, solutions to date have been to defer major decisions resulting in budget deficits that appear insurmountable. Thus, the only options that Arizona has been provided are proposals that reduce services and increase taxes and leave the state with billion dollar shortfalls for years to come.

However, there is a better way. Treasurer Dean Martin is proposing a solution taken from the best practices of turning around a failed business to profitability. A key solution is for the state to restructure its debt and reform the budget process so the state will not be put in the position of being on the brink of insolvency.

While the Recession of 2007-2009 has contributed to the state's fiscal woes, much of the budget problems in Arizona were self-inflicted. When a private company gets into financial trouble one of the first things it does is restructure its existing debt, re-work its contracts, eliminate expenses and streamline its operations. In short, the company changes the way it operates to improve its operation. Now is the time for Arizona to do the same.

BUDGET REFORM

First, the current budget process suffers from a lack of transparency, long-term planning, poor accounting, the use of gimmicks and one-time solutions, and a lack of cooperation between the Governor and Legislature.

This has led to budgets with a negative balance seven out of the last 10 years creating uncertainty on state tax and budget policy matters. This uncertainty makes the state less attractive to businesses to expand or locate here. Further, the lack of long-term planning has left the state short on capital to address critical infrastructure needs. Rather than wait until the current budget problems are over, the Legislature and Governor need to fix some of the institutional problems that plague the state's budget process.

- The Legislature should pass and the Governor should sign legislation that says all funds from all sources should be appropriated by the Legislature with the Governor's approval or veto. Right now, only one-third of all State Government spending is subject to the appropriations process. No functioning business would keep two-thirds of funds off the table when setting budgets. Currently, the Legislature is trying to balance a \$2.5 billion deficit on a General Fund revenue base of \$6.7 billion, instead of trying to balance a \$2.5 billion problem in the context of more than \$30 billion in revenues from all sources.

- In connection with the appropriation of all funds, the Legislature should refer to the voters a constitutional amendment eliminating the ability of the Governor and Legislature from using other funds for general fund uses. When the private sector raids such funds in their own businesses it is generally against the law. The same should apply to State Government. When taxpayers pay a fee or tax for one purpose, it should remain for that purpose and not be diverted to the General Fund. (They may borrow funds only, and must pay the prevailing interest rate for its use.)
- Currently, the state's accounting system allows the general fund to run a negative balance throughout the year while all other funds must have cash in their accounts before a check can be written. The same should apply to the General Fund. As a result, when the General Fund decreases to a negative balance, or can't pay its bills, the Governor and Legislature will have immediate knowledge of the deficit and can act accordingly.

DEBT RESTRUCTURING

Currently, about \$452 million in tax revenues are dedicated to service more than \$4.5 billion in state debt for the Department of Administration, School Facilities Board, the Phoenix Convention Center and one type of debt issued for the state's universities. So with a constitutional debt limit of \$350,000, the Governor and Legislature have borrowed \$4.5 billion, largely in the last 10 years.

It is time to be honest with the voters and get this debt properly authorized. Restructuring and refinancing that revenue stream for 20 to 25 years will allow the state to access the one time revenue needed to close the FY 11 budget shortfall. This proposal could provide the state with one-time savings and revenues of \$820 million FY 11 and \$361 million in FY 12. If revenues increase beyond the current forecast then the amount of borrowing would be reduced accordingly. Interest only payments will be made in FY 12 and full payment would begin in FY 13 and conclude no later than FY 35. There is no new annual cost to taxpayers and some of the debt will be issued on a taxable basis. With interest rates at a historical low, this is a good time to refinance this debt in a proper fashion.

Proposal

The Arizona Legislature should refer to the ballot the following measures:

- Amend the Constitution to approve the refinancing of existing debt and allowing for cash out financing for the FY11 deficit.
- Amend the Constitution to prohibit the Legislature and Governor of approving any form of debt in the future without voter approval first. Just as cities, counties, and school districts in Arizona need voter approval before they issue debt; the same requirement should apply to the state.
- By law, require all debt issuance to be managed by the State Treasurer's office.
- By law, require all repayments of Federal Funds owed to the state for imprisoning illegal immigrants in our prisons from prior years to be used to pay down debt.

The benefits of the two measures:

- No new taxes required.
- Provides one-time savings and revenues of \$802 million FY 11 and \$362 million in FY 12 as the debt is restructured.
- No need to trigger further budget cuts if the sales tax increase doesn't pass in May.
- Prohibits any new debt without voter approval.
- Provides lower cost financing for existing debt.
- Potential pay down of debt of up to \$1 billion from federal funds owed to the state for imprisoning illegal immigrants.