



Office of Strategic Planning and Budgeting
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Phoenix AZ, 85003

July 18, 2025

Hobbs Cabinet,

I want to thank you for your hard work in securing passage of our FY 2025-2026 budget. Prior to outlining expectations regarding the upcoming FY 2026-2027 budget development process in this letter, I want to acknowledge your efforts in supporting the needs of the communities, residents, and economy of our state. Because of your work, we averted a state government shutdown and secured bipartisan investments that will set Arizona up for success for years to come. These policies and investments, including in workforce, childcare, public safety and homelessness, will continue to propel the state forward and enhance Arizonans' quality of life. We have shown that we can make progress in divided government, meet the needs of our residents, and help working families thrive and prosper.

Federal Uncertainty

Significant changes and uncertainty at the federal level will pose additional challenges in the budget development process this year. As you know, H.R. 1 was recently signed into law and will reduce state revenues, create extensive red tape and paperwork for our customers, all while driving up costs to comply with ever-growing federal mandates. Please continue to work with Director Sandigo to estimate the state impacts of this federal bill. In addition, the federal government has yet to pass a budget for Federal Fiscal Year 2026. The President's FY 2026 budget proposes even more cuts in federal resources, reducing the amount of Arizona tax dollars that are returned to the state.

Federal Fiscal Cliff

This uncertainty comes at a time that the flow of pandemic era and stimulus funds into the State are coming to an end. Our residents are going to feel the brunt of the impact as these dollars wane and eventually cease. Combined with the policy changes and rescissions we have experienced over the last several months, it is clear that we are at the edge of a cliff in federal funding unlike anything in recent history. Thank you for the work that you are currently identifying regarding the impact of this federal fiscal cliff and how it will change service delivery and daily operations in your agency.

As the Governor has made clear, it is impossible to backfill all of these federal resources with State dollars. We will do everything we can to mitigate the impacts of these decisions, but it is important to set an expectation with both your staff and stakeholders that the state is unable to shoulder such a large gap in federal support. Please keep OSPB up to date regarding additional changes in federal resources and the impacts to your operations and services.

FY 2027 Non-Caseload Requests 2% Maximum

This significant uncertainty makes reliably estimating FY 2027 state revenues incredibly difficult. To manage this forecasting challenge responsibly, we ask that you limit your FY 2027 (non-caseload) General Fund request to no more than 2% of your FY 2026 (non-caseload) General Fund appropriation. Mandatory spending for caseload growth, state employee health insurance, and court injunctions are likely to crowd out much (if not all) of any available new revenue. As a result, it is imperative that we approach FY 2027 with a sense of caution and realism. This is not the year to ask for significant investments from the General Fund.

Savings, Offsets, and Efficiencies

Arizona has long been a national leader in government innovation and efficiency. To navigate these unprecedented changes, we will need to utilize those skills more than ever before. We ask that each agency begin to develop proposals to find savings, offsets, and other efficiencies. This could include elimination of ineffective or outdated programs. It could include developing new nonprofit and private sector partnerships, and new earned revenue streams. We will have extensive conversations with your staff in the coming months on your ideas to operate both smarter and more efficiently while reducing General Fund strain. Please do not include savings proposals in your September 2 submission.

Fees

Last year, we conducted a comprehensive review of fees across the State. As a result, we anticipate very few fee-related requests this year. For any fee adjustment, please guarantee that it meets all statutory restrictions, including that it not be increased above inflation. We expect, as always, that any proposed fee adjustment would have the full support of any impacted stakeholders. Any fee increase will also need to be justified as being necessary from a fund balance perspective, and will need to result in improved performance. That improved performance must then be measured on your agency scorecard once the fee is implemented.

Pre-Budget Meetings

This year's annual Pre-Budget Meetings with agencies will begin the week of July 21, 2025 for FY 2027 budget development. These meetings are your chance to provide the Governor's Office with a preview of your September submissions for initial direction and consistency across the State. These meetings will include Cabinet members and staff, including the CFO, budget director, senior leadership, and any other staffers needed to fully explain budget request intentions. We will include the Governor's Office Senior Staff, budget analyst, policy advisor, operations advisor, and other staff to ensure we can make comprehensive decisions prior to the budget request publications on September 2, 2025. Your OSPB analyst will be providing additional details in the coming days for how to prepare for these meetings. But please note, you will be expected to send all materials to your OSPB analyst at least **48 hours prior** to this meeting.



Implementation of FY 2026 Budget Items

During these pre-budget meetings we will talk in detail about the implementation of any FY 2026 budget items. We have already had many discussions with your staff about the contractual, personnel, IT, reporting, and other requirements that will be necessary to ensure we implement the bipartisan FY 2026 budget. If you have implementation questions about any particular FY 2026 appropriation, please reach out to your OSPB analyst and Policy Advisor as soon as possible.

ABS Updates

Laws 2025, Chapter 93, Section 3 added reporting requirements for federal funding in agency budget submissions. The ABS User Guide has been updated to capture those requirements. Please attend ABS training on July 25 or July 31 for those updates.

Please don't hesitate to reach out to your OSPB analyst if you have questions about anything in this letter. And thank you for your commitment to making Arizonans' lives better each and every day.

-Ben Henderson