

Executive Summary



SUMMARY

BACKGROUND

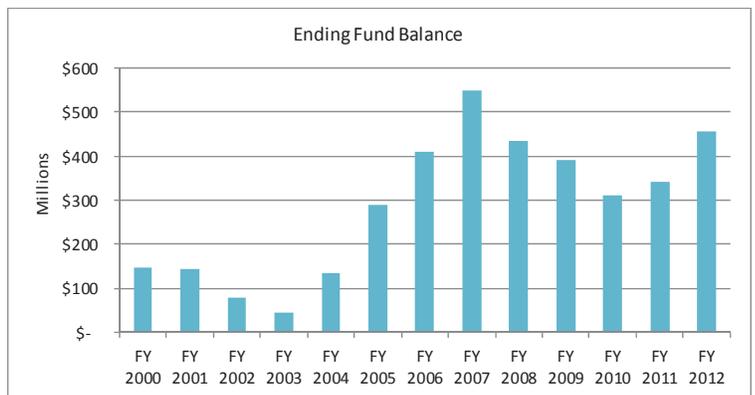
After several years of budget challenges, the 2013 Legislature had the advantage of growing general fund revenue streams and a significant general fund balance. At the same time, there were a number of budget challenges and other pent-up financial demands before the 2013 Legislature, including pensions, employee pay, provider reimbursement rates, and more.

STRONG ENDING FUND BALANCE

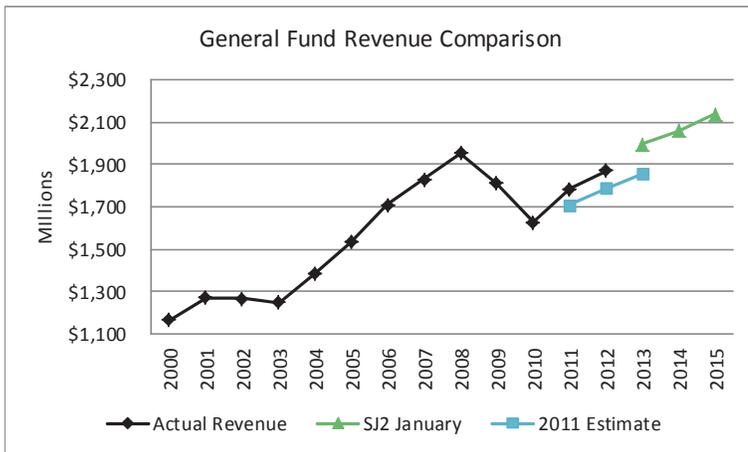
A high level of ending fund balance was available to the legislature. While the 2011 session anticipated an ending fund balance of \$150 million, with approved supplementals and other legislation in the 2013 biennium the ending fund balance is currently anticipated to be well over \$400 million at the end of the 2013 biennium.

GROWING REVENUES

In FY 2009 and FY 2010, state revenues declined two years in a row. While two years ago it appeared these declines had ended, it was not clear how strongly general fund revenues would return. The last two years have brought growth and stability to the general fund revenues. This stability gives confidence that the worst is behind us.



The next two years are anticipated to have continued growth in general fund revenue, although not at the same rate as the past two years. Growth patterns are anticipated to even out to just under the long term growth trend in FY 2014 and FY 2015.



The chart shows the actual revenue collected from FY 2000 to FY 2012. The lower blue line for FY 2011 to FY 2013 shows the revenue anticipated at the end of the 2011 session and the green line shows the revenue estimated for FY 2013 to FY 2015 in SJ 2, the official revenue estimate of the 2013 legislative session.

There is a 15.3% increase in anticipated revenues from the amount projected by the 2011 Legislature for the 2013 biennium to the current anticipated 2015 general fund revenues. The 2013 Legislature had this 15.3% increase in revenues and the strong ending fund balance to respond to the budget challenges described in the pages that follow.

BUDGET CHALLENGES

Pension Funding Shortfall

Over the past several years the unfunded liability of all Montana public pensions in Montana increased to \$4.3 billion. Collectively Montana public employers and employees were making payments on about \$2.0 billion of this liability, while the remaining portion (\$2.3 billion) of this liability needed to be funded or amortized over 30 years as generally recommended by experts. The additional annual funding needed was approximately \$121 million per year. Without measures to close this funding gap, the liabilities were estimated to continue to grow to the point where 39 to 41 years from now there would be no assets to pay required pension payments, and state and local governments would be liable for funding these costs out of current operating expenses.

The legislature adopted legislation to fund the two largest systems' liabilities with a combination of state general fund, state and local employer contribution rate increases, employee contribution increases, and reductions in the inflationary increases in retiree benefits to close this gap. The general fund cost of these proposals is \$127 million in the 2015 biennium, which accounts for 25% of the additional ongoing general fund commitment in the 2015 biennium in comparison to the 2013 biennium. For more detail on pension funding click the following link:

www.leg.mt.gov/content/Publications/fiscal/Vol-1/4-State-Expenditures/Major-Budget-Issues/Pensions.pdf

Personnel and Pay Plan

Employees of the state of Montana have not received an inflationary pay adjustment approved by the legislature in four years. Yet, during this time period many changes have occurred in market conditions and pay approved by the executive. Given the previous increases provided by the executive, the legislature approved a pay increase subject to the priorities set forth in HB 13. The priorities are designed to target the areas of greatest compensation need in state government. The specifics of the pay increase are outlined in the Overview of State Expenditures section.

This pay increase accounts for \$58 million or 11% of the increase in the ongoing biennial general fund increase.

For more detail on pay plan funding use the following link:

www.leg.mt.gov/content/Publications/fiscal/Vol-1/4-State-Expenditures/Major-Budget-Issues/Pay-Plan.pdf

Rates Paid to Private Providers of Services

Some state government services are provided by private entities such as hospitals, nursing homes, private prisons, and other community providers. Similar to pay increases for state employees, private providers of services to citizens of Montana have generally not received an ongoing across the board increase in funding in four years. Governor Bullock

proposed an increase of 2% per year for most providers and statutorily calculated increases for other providers. In addition to accepting these provider pay increases, the legislature authorized select additional rate increases for providers of children's mental health Medicaid services, children's mental health targeted case management, and developmental disabilities services.

Federal Healthcare Reform and Montana's Choices

The federal Patient Protection and Affordable Care Act or ACA included several policy choices that were considered by the legislature. The ACA makes several changes to Medicaid programs that all states are required to implement and includes provisions that allow Montana to opt to expand Medicaid and implement provisions related to the private health insurance market.

- The executive did not request any funding adjustments to HB 2 for the changes to the state Medicaid program that are required by ACA. Some of the changes increase costs, while some reduce costs. The legislature determined that the executive will need to accommodate Medicaid program changes due to ACA within HB 2 and SB 410 appropriations.
- The legislature considered but did not adopt any of several bills to implement the option allowed under ACA to expand Medicaid eligibility for adults who are between the ages of 10 and 64 and who are not disabled or pregnant, and have household income up to 138% of the federal poverty level.

Federal Deficit Reduction

The federal government has deficit reduction requirements that will result in a combination of increased tax collections and decreased spending. Both will impact Montana's budget and economy. The tax changes will slightly decrease Montana's income tax collections as additional federal taxes will be partially deductible from Montana's taxable income. The direct tax impacts from the tax changes are relatively small.

The larger impact on the revenue side will result in changes to the economy from changes to federal tax law and federal direct spending reductions. For these impacts, the LFD revenue estimate relies on IHS Global Insight, the state's economic forecast company. IHS Global Insight estimated changes to the Montana economy were included in the January update of SJ 2.

In addition to tax and direct spending provisions, the deficit reduction requirements contain budget reductions that will impact state agency budgets directly, although during legislative budget deliberations the precise amount of the direct reductions and their impact were not entirely clear. The legislature chose not to backfill any potential reductions in federal money or provide any other means during the interim for replacement of any reduced funding.

Wildfire Funding

Wildfire costs in FY 2013 are expected to reach \$60.3 million, a much higher than the usual level of \$23.8 million per year based on a seven year average. The fire suppression fund established in the 2007 special session has been fully expended and both a supplemental appropriation for the current biennium and additional funds for the next biennium were requested by the executive. The legislature adopted two measures to assist in funding fires in the current and future biennia. HB 3 (the supplemental bill) provided funding for the shortfall in FY 2013. In addition, HB 3 provided approximately \$14.2 million for transfer to the fire suppression fund to use in future biennia. HB 354 provides additional revenues to the fire suppression fund through two mechanisms: 1) reversions (or appropriations that were underspent) in excess of 0.5% of the annual appropriations; and 2) corporate income tax revenues in excess of levels anticipated. For more detail on wildfire funding use the following link:

www.leg.mt.gov/content/Publications/fiscal/Vol-1/4-State-Expenditures/Major-Budget-Issues/Fires.pdf

Energy Development Issues

Local and state governments are being challenged with finding personnel and resources to provide services in the energy development areas of the state. Housing costs have increased dramatically. Water and sewer systems are over their limits. Police, fire, and other public safety systems are stretched. School districts face challenges of quickly expanding enrollments with children from all over the country with varying educational needs. The legislature reviewed many choices this session to address some of these challenges.

Two primary means of funding solutions in these energy development areas were passed by the legislature - one for schools (SB 175) and one for local governments (HB 218). Of these, HB 218, the local government infrastructure bill, was vetoed by the Governor.

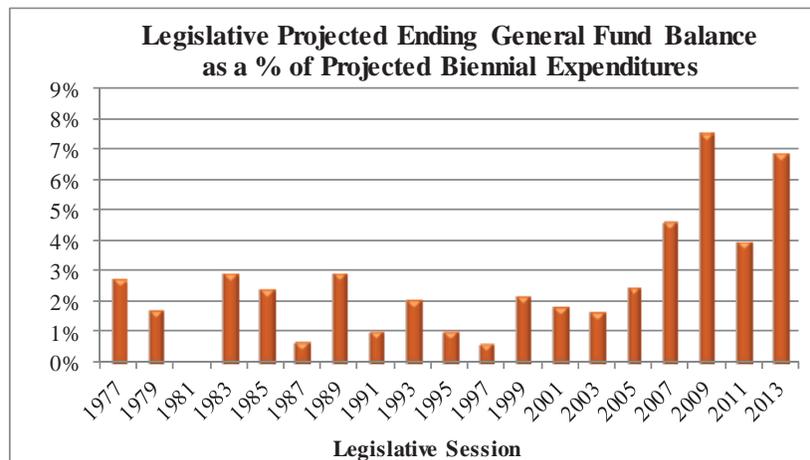
In addition to these two primary bills, HB 6 provided funding for regional water projects. Some of these projects include infrastructure for some areas impacted by energy development. For more detail on funding for energy development areas use following link:

www.leg.mt.gov/content/Publications/fiscal/Vol-1/4-State-Expenditures/Long-Range/Energy.pdf

Managing Budget Volatility

The legislature primarily used the ending fund balance as the means for managing potential budget volatility in either expenditures or revenues. Governor Bullock proposed a structural balance (revenues equal to or exceeding spending) and an ending fund balance of \$300 million. The Governor’s vetoes brought budgets to these levels with the official revenue estimate of the session, SJ 2. While no other revenue estimates passed the legislature, at the end of session the Legislative Fiscal Division and the Governor’s Budget Office had revenue estimates that would have brought the final ending fund balance to approximately \$350 million.

Historically, projected ending fund balances have varied from nearly zero to as high as 7.7% of biennial spending. The 2015 biennium budget anticipates an ending fund balance of \$297 million, or 6.9% of biennial spending. The following table illustrates the budgeted ending fund balances of the past as a percent of the anticipated expenditures.



Legislatures frequently spend one-time ending fund balances on one-time investments in infrastructure or other projects. For a list of the current biennium one-time investments please see Appendix A.

LEGISLATIVE BUDGET FOR THE 2015 BIENNIUM

The status sheet at the end of session had an ending fund balance anticipated at \$182 million and a negative structural balance of \$20.9 million. However, the Governor vetoed a number of bills that impacted both the overall and structural balances. The following table details the Governor's vetoes. All vetoes that qualified for polling for potential override were upheld by the legislature.

Vetoed Bills--General Fund			
In Millions			
HB0002	General Appropriations Act	Vetoed, line-item	2.621
HB0012	Appropriate funds for provider payments	Vetoed, override attempt failed	6.482
HB0019	Revise penalty and interest provisions related to tax law enforcement	Vetoed, override attempt failed	1.094
HB0218	Require Board of Oil and Gas to administer grant program for oil and gas impacts	Vetoed, override attempt failed	35.318
HB0556	Revise laws related to coal severance tax allocations	Vetoed, override attempt failed	1.322
HB0604	Create Select Committee on Medicaid Innovation, Reform, and Expansion	Vetoed	0.100
HB0633	Provide for an interim select committee on efficiency in government	Vetoed, override attempt failed	0.080
SB0081	Provide tax credits for contributions to scholarship organizations	Vetoed	6.024
SB0114	Eliminate certain charges for motor vehicle registration	Vetoed	4.708
SB0236	Increase coal board funding until June 30, 2019	Vetoed, override attempt failed	3.010
SB0240	Revise taxation of pollution control equipment	Vetoed, override attempt failed	0.157
SB0256	Making FWP liable for private property damages caused by wild buffalo/bison	Vetoed	0.040
SB0265	Extend the reserved water rights compact commission	Vetoed	0.040
SB0282	Generally revise taxation of income, including the corporate license tax	Vetoed	3.685
SB0394	Generally revise income tax laws and decrease taxes	Vetoed	47.003
SB0401	Revise disposition of metalliferous mines license tax	Vetoed, override attempt failed	<u>3.620</u>
Total			\$115.304
HB 5 is not included on the list as the line item veto did not have a monetary impact.			

The final adopted general fund budget included an ending fund balance anticipated at \$297.9 million and a negative structural balance of \$4.55 million. This general fund budget is illustrated on the following page in accordance with the requirements for content and comparison to the previous biennium contained in 17-7-151, MCA.

17-7-151, MCA - General Fund Comparison									
(in Millions)									
	Actual 2012	FY Estimated FY 2013	Legislative FY 2014	Legislative FY 2015	2013 Biennium	2015 Biennium	Biennial \$ Change	Biennial % Change	
Beginning Fund Balance	\$341.88	\$452.37	\$435.00	\$337.87	\$341.88	\$435.00	\$93.12	27.2%	
Revenue									
Legislative Revenue Estimates - SJ 2	1,870.95	1,995.08	2,056.20	2,137.40	3,866.03	4,193.60	327.57	8.5%	
Legislation		0.27	0.13	(0.81)	0.27	(0.68)	(0.95)		
Legislative Prior Year Revenue Adjustments	8.75	-	-	-	-	-	-		
Total Funds Available	2,221.58	2,447.72	\$2,491.33	\$2,474.46	\$4,208.18	4,627.92	419.74	10.0%	
Disbursements									
General Appropriations Act Ongoing	1,577.86	1,628.67	1,734.64	1,786.23	3,206.53	3,520.87	314.34	9.8%	
General Appropriations Act OTO	10.06	13.61	20.80	23.20	23.67	44.00	20.33	85.9%	
Feed Bill (HB 1) Ongoing	1.36	10.06	1.30	11.10	11.41	12.40	0.99	8.7%	
Supplemental Approps (HB 3) Ongoing	-	53.57	-	-	53.57	-	(53.57)	-100.0%	
Supplemental Appropriations (HB 3) OTO	-	65.22	-	-	65.22	-	(65.22)	-100.0%	
Long Range Building (HB 5) OTO	-	-	49.55	-	-	49.55	49.55		
Renewable Resources Grants (HB 6) OTO	-	-	20.47	-	-	20.47	20.47		
Long Range Information Tech (HB 10) OTO	-	-	11.45	-	-	11.45	11.45		
Treasure State Endowment (HB 11) OTO	-	-	10.85	10.85	-	21.70	21.70		
Pay Plan (HB 13) Ongoing	-	-	16.98	41.02	-	58.00	58.00		
Pay Plan (HB 13) OTO	-	-	0.55	0.55	-	1.10	1.10		
K-12 Education Legislation Ongoing	-	-	13.08	14.47	-	27.55	27.55		
K-12 Education Legislation OTO	-	23.25	0.01	0.01	23.25	0.01	(23.24)	-99.9%	
Pension Legislation Ongoing	-	-	62.57	64.20	-	126.77	126.77		
Statutory Appropriations Ongoing	171.23	200.95	199.80	214.10	372.18	413.90	41.72	11.2%	
Statutory Appropriations Bills Ongoing	-	-	(0.03)	5.92	-	5.89	5.89		
Statutory Appropriations Bills OTO	-	-	3.79	-	-	3.79	3.79		
Transfers Ongoing	15.47	15.00	13.48	12.09	30.47	25.57	(4.90)	-16.1%	
Transfers - Legislation OTO	-	13.50	1.08	-	13.50	1.08	(12.42)		
Other Appropriations OTO	3.67	-	0.90	0.89	3.67	1.79	(1.87)	-51.1%	
Reversions	-	(11.10)	(7.82)	(8.05)	(11.10)	(15.87)	(4.77)	42.9%	
Total Disbursements	\$1,779.64	\$2,012.73	\$2,153.46	\$2,176.57	\$3,792.36	\$4,330.03	\$537.67	14.2%	
Fund Balance Adjustment and Prior Year	10.43	-	-	-	10.43	-			
Ending Fund Balance	\$452.37	\$435.00	\$337.87	\$297.89	\$426.24	\$297.89			
Biennial Comparison									
Total Ongoing Spending	1,765.91	1,897.14	2,034.01	2,141.08	3,663.06	4,175.09	512.03	14.0%	
Total OTO Spending	<u>13.72</u>	<u>115.58</u>	<u>119.45</u>	<u>35.50</u>	<u>129.30</u>	<u>154.94</u>	<u>25.64</u>	<u>19.8%</u>	
Total Disbursements	1,779.64	2,012.73	2,153.46	2,176.57	3,792.36	4,330.03	537.67	14.2%	
Total Ongoing Revenue	1,870.95	1,995.35	2,056.26	2,136.52	3,866.03	4,193.46			
Total OTO Revenue	-	-	0.07	0.07	-	0.14			
Structural Balance	\$105.04	\$98.21	\$22.25	(4.56)	\$202.98	\$18.37			

2015 Biennium Ongoing Spending

The increase in ongoing general fund spending as adjusted per MCA 17-7-151 is 14.0%. As show in the preceding pages, a number of significant budget challenges were addressed by the 2013 Legislature. The following table illustrates the primary components of this spending:

2015 Biennial Ongoing General Fund Increase			
Item	Millions	% of Increase	% of 2013 Biennial
Pension Legislation	\$126.8	25%	3.5%
HB 13 Pay plan	58.0	11%	1.6%
K-12 Total	141.5	28%	3.9%
K-12 guarantee account replacement	56.7	11%	1.5%
K-12 increased present law and other	60.1	12%	1.6%
K-12 tax relief (SB 372, SB 96, SB 175)	24.7	5%	0.7%
Tax Relief - entitlement share (2011 SB 372, SB 96)	32.2	6%	0.9%
DPHHS Medicaid, provider rates, and other	84.2	16%	2.3%
Montana University System (\$14 million is replacement)	32.9	6%	0.9%
Other (DOC \$12.6; Justice \$4.8; DOR \$2.0; OPD \$4.2)	<u>37.1</u>	<u>7%</u>	<u>1.0%</u>
Total	\$512.0	100%	14.0%

The following section provides additional detail of each of the components of the increase.

DETAIL OF ONGOING GENERAL FUND INCREASE

K-12 Funding

K-12 funding accounts for over 40% of the total general fund spending in the 2015 biennium.

The increase in ongoing K-12 general fund spending was \$141.5 million or 28% of the total general fund ongoing increase in spending. This is comprised of three major components:

1. A replacement of \$56.7 million of funding that was available in the guarantee account (primarily school trust revenue) in the 2013 biennium that is not anticipated in the 2015 biennium. Since this funding is not anticipated in the 2015 biennium, general fund must be used to replace it.
2. Increased present law and other funding increases comprised \$60.1 million of the total. This includes the present law increases to fund K-12 school district BASE aid and special education factors by 0.89% in FY 2014 and 2.08% in FY 2015, as well as increases contained in SB 175 and all other adjustments.
3. Tax relief distributed \$24.7 million through the school funding formula from SB 372 from the 2011 session, and SB 96 and SB 175 from the 2013 session.

Note in addition to these amounts, K-12 benefits from the general fund spending in the pension legislation. Additional information on school funding begins on page E-1 of Volume 4.

Montana University System Funding -- Tuition

The 2013 Legislature increased general fund appropriations for Montana's postsecondary education institutions and agencies by \$44.2 million for the 2015 biennium. Of this increase, \$11.2 million funds one-time only expenditures,

HB 2 General Fund Increase (in millions)	
State Share Funding for Present Law Adjustments	\$28.2
Ongoing New Programs & Other Program Increases	4.8
Ongoing Expenditures Total	\$33.0
One-Time-Only Expenditures	<u>11.2</u>
Total Increase	\$44.2

leaving \$33.0 million, or 75%, of the general fund biennial increase for ongoing expenditures.

Tuition Cap Agreement (in millions)	
HB 2	
State Share Funding for Present Law Adjustments	\$28.2
Student Assistance Program (OTO)	5.2
WICHE/WWAMI/Dental (OTO)	<u>0.6</u>
HB 2 Total	<u>\$34.0</u>
HB13 Pay Increase for Educational Units	<u>18.7</u>
Total	<u>\$52.7</u>

Most of the \$28.2 million general fund increase for the state share funding of present law adjustments will be allocated to the Montana University System education units to implement a Tuition Cap Agreement reached between the Governor and the Board of Regents and approved by the legislature to freeze resident student tuition rates each year of the 2015 biennium. (At its May 2013 meeting the Board of Regents maintained tuition rates at the prior level.) Included in the agreement in HB 2 is \$5.2 million general fund restored to the Student Assistance Program that was part of a funding switch in the

2011 legislative session and \$0.6 million general fund for inflationary increases in the WICHE/WWAMI/Minnesota Dental program. In addition to HB 2 appropriations, the Tuition Cap Agreement includes HB 13 appropriations for the state share of the educational units’ pay plan costs. The estimated general fund allocation is \$18.7 million for pay raises and increased state contribution toward health insurance premiums. The agreement also commits the Montana University System to incorporating a performance funding component into the allocation model used by the Board of Regents for distributing funds to the MUS education units.

Additional information begins on page E-76 of Volume 4.

Business Equipment Exemption

SB Bill 96 reduces the taxes assessed on class 8 business equipment by providing a tax rate of 1.5% on the first \$6 million of taxable market value and 3% for all taxable market value in excess of \$6 million. The legislation also exempts the first \$100,000 in market value of this property owned by a taxpayer, up from \$20,000. The exemption is available for all owners of class 8 business equipment tax. Reimbursements are provided to the university system, local governments, local schools, and tax increment financing districts from the general fund for reductions in property tax revenue due to the legislation. The net cost of SB 96 is \$18.5 million over the 2015 biennium. A further discussion is in Volume 2.

FY 2013 Supplemental Appropriations

Supplemental appropriations for FY 2013 total \$117.2 million. These supplementals are primarily for: 1) K-12 funding of \$34.7 million, which had been anticipated with the veto of HB 316 after the 2011 session; 2) wildland fire costs of \$50 million, which includes \$14.2 million to replenish the fire suppression fund for future fire costs; and 3) \$13.4 million for half the cost of the Libby asbestos legal settlement. The school funding items of the supplemental have been considered ongoing spending as it is statutorily required. A further discussion is in Appendix A of this volume.

2015 Biennium One-Time-Only Appropriations

The legislature provided a total of \$45.9 million in one-time-only (OTO) general fund appropriations, including \$44 million in HB 2 and an additional \$1.9 million in other legislation. The HB 2 appropriations include \$5.8 million in present law and \$38.2 million in new proposals over a large number of agencies for a number of different purposes. A discussion of all OTO appropriations is included in Appendix A.

The legislature also made a number of general fund transfers for OTO projects, including \$49.55 million for long-range building and maintenance projects. A further discussion is under “General Fund Transfers” and in the Long Range Planning section in the Overview of State Expenditures section of this volume.

Department of Corrections

The Department of Corrections is funded primarily with general fund. The main increases in the Department of Corrections budget are to maintain current programs. The budget addresses average annual offender population increases of 1% and 4.4% for female offenders as well as a 10% annual growth of medical costs. To accommodate these factors, the legislature funded the department at \$21.0 million, or 6.0% higher than the 2013 biennium, to increase staffing by 2.00 FTE and add 10 female pre-release and transitional living beds. When the biennial comparison includes supplemental appropriations in the 2013 biennium and ongoing appropriations only, the increase in the biennium is reduced to \$12.6 million.

In addition to general fund appropriations, SB 410 appropriated \$2.0 million of state special revenue specifically for the department and an unspecified portion of \$7.5 million that will be shared by nine agencies including the department to address operating costs in the 2015 biennium.

Additional information begins on page D-71 of Volume 4.

Office of Public Defender

The legislature increased funding for the Office of Public Defender by \$8.4 million or 18.9% over the previous biennium funding, which included increasing staffing by 8.00 FTE or 3.8% to address double digit growth in cases and factors contributing to high levels of staff turnover. Significant increases also included \$3.7 million to contract for staff augmentation and \$2.6 million to fund a career ladder for attorneys. Like the increases in the Department of Corrections, when the biennial comparison includes supplemental appropriations in the 2013 biennium and ongoing appropriations only, the increase in the biennium is reduced to \$4.2 million.

Additional information begins on page D-62 of Volume 4.

Department of Public Health and Human Services

Health and Human Services programs account for 25% of the total general fund budget. General fund increases \$86.2 million over the biennium for two primary reasons: 1) Medicaid increases in caseload and utilization add \$65 million; and 2) provider rates increase \$17 million. When adjusted to include ongoing appropriations only, this increase is \$84.2 million or 16% of the ongoing general fund biennial increase.

Additional information begins on page B-1 of Volume 3.

Long-Range Planning

The 2013 Legislature approved total one-time spending (appropriations and authorizations) of \$325.5 million for the LRP budgets. The largest source of state funding is general fund at \$103.2 million, taking the form of transfers to the various program funds. In the upcoming biennium, the highest amount of appropriations was provided for the Long-Range Building Program - \$175.6 million (\$116.7 million of state and federal funds).

More information on the LRP programs and projects may be seen in Section F of the 2015 Biennium Legislative Fiscal Report.

Water Compacts

Water compacts are formal agreements for the equitable division and apportionment of waters between the state and the several Indian tribes claiming reserved water rights within the state, and between the state and the federal government claiming non-Indian reserved waters within the state. All compacts must be approved by the legislature and Congress prior to implementation.

The executive proposed HB 629 as a vehicle to adopt the Reserved Water Rights Compact Commission recommendation for settlement of the Confederated Salish and Kootenai Tribes (CSKT) Water Compact, as well as additional funding for the Fort Belknap and Blackfeet compacts. HB 629 was not adopted by the 2013 Legislature. Instead, the legislature provided \$17 million of appropriations in HB 6 toward the state's financial obligation for the

two existing/authorized tribal water compacts: the Fort Belknap Tribal Compact (\$3 million) and the Blackfeet Tribal Compact (\$14 million).

The consequences of the failure of HB 629 are unclear. The Reserved Water Rights Compact Commission plans to issue a report on issues raised during the session to the Water Policy Interim Committee.