



# MONTANA LEGISLATIVE BRANCH

## Legislative Fiscal Division

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Legislative Fiscal Analyst  
AMY CARLSON

DATE: November 5, 2010

TO: Legislative Finance Committee

FROM: Jon Moe, Fiscal Specialist

RE: Global Fiscal Issue Recommendations for Consideration of the Legislative Finance Committee

Prior to each session, the Legislative Finance Committee (LFC) is directed in statute to make recommendations to the House Appropriations and Senate Finance and Claims committees regarding the activities of the joint appropriations subcommittees and various procedural issues related to developing the state budget. For the upcoming 2011 session, two items have already been adopted and an additional six items are included in this report for your consideration. They are listed and discussed in two attachments.

- The first is described as a “decision matrix” which simply lists the items that the LFC should consider in its November 16 meeting. This document provides the item number, a description of the item with a proposed recommendation highlighted, and a brief history if there is one, or indicates that it is a first time item.
- The second is a more descriptive write-up of the same issues, intended to provide more background in most cases. Some of these global issues can get confusing, so hopefully this more descriptive version can answer some of the question you might have on specific items.

In the absence of even further background information, feel free to contact me at [jonmoe@mt.gov](mailto:jonmoe@mt.gov) or Amy Carlson at [acarlson@mt.gov](mailto:acarlson@mt.gov) or either of us at (406) 444-2986 for additional information.

## 2013 Biennium Budget Global Decisions and Direction for Budget Process Decision Matrix

#	Decision Item	Description	History	LFC Decision
1	Starting Point for Subcommittee Deliberation	<p><b>Adopted June 2010: The initial motion in all appropriation subcommittees for a starting point for budget deliberations shall include: the adjusted base to include personal services adjustments, statewide fixed costs, and inflation; any decision packages necessary to implement the two percent reductions approved in the 2009 session in an ongoing manner; and the five percent reduction plans provided in 17-7-111 (3)(f), MCA.</b></p> <p>The adoption of the base and statewide present law adjustments as the starting point does not prevent a subcommittee, the full committees, or the legislature from reducing the budget later in the process.</p> <p>Also adopted in June 2010, <b>the LFC requests that the LFD and the LSD draft a bill that includes all statutory changes required to implement the five percent reduction plans...</b> A bill is presently being drafted to implement the five percent plan.</p>	<p>This is a change from prior practices due to the unique nature of this budgeting cycle and the anticipated level of scrutiny that will be applied to all elements of the budget.</p>	<p>Adopted June 2010</p>
2	Vacancy Savings	<p><b>Direct the appropriations subcommittees to adopt a global level of a personal services reduction (vacancy savings) as a starting point:</b></p> <p style="padding-left: 40px;"><b><u>Option A</u> – 4% as proposed in the Executive Budget;</b>  <b><u>Option B</u> – 7% as adopted last session; or</b>  <b><u>Option C</u> – Another specified level.</b></p> <p>From that point, an individual appropriations subcommittee might determine that a certain group of positions within a program under their purview should be exempted from the reduction or allowed a reduced level of vacancy savings, or even determine that a higher level of vacancy savings be applied.</p>	<p>This is consistent with the way vacancy savings has been handled since the 1999 biennium. For the 1997 biennium and before, varying methods were applied or vacancy savings was not applied at all.</p>	

**2013 Biennium Budget  
Global Decisions and Direction for Budget Process  
Decision Matrix**

#	Decision Item	Description	History	LFC Decision
3	Fixed Costs in the Budget	<b>Direct subcommittees to consistently apply fixed costs in agency budgets as included by the executive budget request. Adjustments to fixed cost rates shall be determined by the subcommittee examining the service provider (e.g., ITSD costs as reviewed by the General Government Subcommittee) and shall be globally adjusted on a consistent basis.</b> For tracking purposes, these types of adjustment would occur as decision packages.	This option has been consistently applied.	
4	Inflation or Deflation Factors in the Budget	<b>Direct subcommittees to not vary from the executive budget proposed inflation or deflation factors.</b> If the full appropriations committee wishes to vary from the executive budget proposal of inflation/deflation factors, it should establish approved inflation/deflation rates (if any) by individual object of expenditure and direct subcommittees to apply these rates to all budget adjustment recommendations. For tracking purposes, these types of adjustment would occur as decision packages.	This option has been consistently applied.	
5	Proposals Requiring Legislation	Implementation of some proposals that require general appropriations act (HB 2) appropriations will require implementation of complementary legislation. The question is: How will changes in HB 2 that are dependent upon the passage of other bills be made? <b><u>Option A</u> - Subcommittees make recommendations regarding the proposal. Build all changes requiring legislation into the HB 2 line-items, and include contingency language striking the change if the legislation does not pass.</b> <b><u>Option B</u> - Do not include the changes requiring legislation in HB 2 line items, but include contingency language enacting the change if the legislation does pass.</b> <b><u>Option C</u> - Make no recommendations or adjustments to HB 2 until required legislation passes, except for K-12 inflation which is present law.</b>	The handling of appropriations contingent on legislation can have a significant impact on the general fund status sheet tracking system. Option A was utilized in the 2003 session due to the severe deficit situation. Prior to the 2003 session and the last two sessions, Option C was the traditional method adopted for dealing with pending legislation.	

**2013 Biennium Budget  
Global Decisions and Direction for Budget Process  
Decision Matrix**

#	Decision Item	Description	History	LFC Decision
6	Separate Legislation to implement the General Appropriations Act	<b>Appropriations committee leadership shall request legislation to provide a vehicle for enacting substantive language related to the implementation of appropriations in HB 2.</b>	This was included in the items discussed for the 2007 session, and discussed for the 2009 session and adopted.	
7	Integrate “Goals and Objectives” into the Appropriations Process	<p><b>Direct performance measurements to be included in the decisions of the appropriation subcommittees:</b></p> <ul style="list-style-type: none"> <li>• <b>Review of the starting point and discussion of anticipated outcomes given the new base. This allows for legislative discussion on current program performance, the effects of reducing the previous base and the impacts on related performance measurements</b></li> <li>• <b>Decisions on a few critical measurable performance measures for each agency made at each step of the appropriation process and formalized as part of a bill(s) or resolution</b></li> </ul>	This process has evolved over the past several biennia. A report was written and approved that outlines the process.	Adopted June 2010
8	Internal Service Funded Proprietary Programs	<b>Direct joint appropriation subcommittees that review proprietary rates not to approve decision packages of internal service funded proprietary programs unless quantifiable rate impact information is provided.</b> “Internal service funded proprietary programs” refer to state programs that provide services to other state programs for fees based upon rates approved by the legislature	This recommendation by the Legislative Finance Committee’s budget and appropriation subcommittee was first adopted for the 2009 session.	

# **GLOBAL FISCAL ISSUES: LFC RECOMMENDATIONS TO THE 2011 LEGISLATURE**

A Report Prepared for the  
**Legislative Finance Committee**

By  
**Jon Moe**  
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November 5, 2010

**Legislative Fiscal Division**



[www.leg.mt.gov/css/fiscal](http://www.leg.mt.gov/css/fiscal)

## PURPOSE

The structure of the executive budget proposals is specified in statute. This defined structure is the backbone of a process that involves months of preparation by executive and legislative staff, and months of legislative deliberation. It is the defined structure that allows for a sophisticated level of automation but which also dictates a need for consistency among groups of decision makers. It is the issues of consistency and equity that are addressed here.

The purpose of this report is to provide, in accordance with statute, options for a procedural framework for the legislature in dealing with global fiscal issues, issues that impact the deliberation of most, if not all, agency budgets. Because the legislative budget process employs six appropriations subcommittees reviewing the same components of different agency budgets, a common approach to addressing certain overarching issues is desirable. With global decisions in hand, the subcommittees can proceed with their individual budget reviews knowing that there is equity and consistency in key decisions regarding those overarching issues of the total budget.

## BACKGROUND

A bill passed by the 1997 Legislature revised 5-12-205, MCA (powers and duties of the Legislative Finance Committee) to require that the LFC make recommendations to appropriations committee leadership prior to each session on global budget issues. The statute is as follows:

*5-12-205 (7) [The Legislative Finance Committee] shall, before each regular and special legislative session involving budgetary matters, prepare recommendations to the house appropriations committee and the senate finance and claims committee on the application of certain budget issues. At a minimum, the recommendations must include procedures for the consistent application during each session of inflation factors, the allocation of fixed costs, and the personal services budget. The committee may also make recommendations on other issues of major concern in the budgeting process, such as estimating the cost of implementing particular programs based upon present law.*

Over a period time, a variety of issues have lent themselves to this discussion. In the following pages, there are eight items suggested for global recommendations that are a product of past Legislative Finance Committee and Legislative Fiscal Division experience or proposals from interim studies of the budget. A few of these items are based on budget computer system structure and limitations. From the perspective of the Legislative Fiscal Division (LFD) staff and its ability to efficiently and effectively assist the legislature in the formulation of the state budget, the importance of these recommendations and the ultimate acceptance, by the appropriations committee leadership and the joint appropriations subcommittees, is paramount.

However, if the members of the committees that discuss these recommendation are concerned that the acceptance of anyone of these results in a budget or portion thereof being “set in stone” or considered “off-limits”, it needs to be made clear that this does not occur. Regardless of the acceptance of these recommendations, any aspect of the budget (base, present law base, or new proposals, vacancy savings, personal service budgets, fixed costs, or inflationary/deflationary factors) is still open to amendment. Member or members, that wish to pursue changes to the budget in these areas, should work with their respective staff to determine how to achieve the desired result. LFD staff has the knowledge of the programs, budget components, and automated budgeting system (MBARS) to provide advice on how to achieve the desired result.

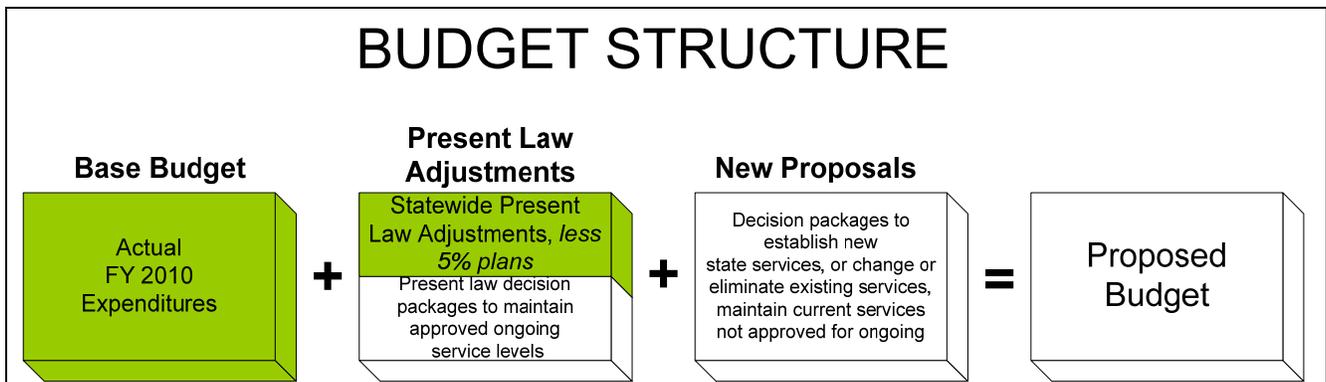
The following sections summarize the identified global issues and provide options or recommendations for consideration by the Legislative Finance Committee in formulating a recommendation to appropriations committee leadership in preparation for the 2011 legislative session.

## DECISION ITEMS FOR APPROPRIATION COMMITTEES ACTION

The following items (numbered 1 through 8) are presented to the Legislative Finance Committee (LFC) for purposes of developing recommendations to the House Appropriations and Senate Finance and Claims Committees at the beginning of the 2011 session, as required in 5-12-205(7), MCA.

### STARTING POINT FOR SUBCOMMITTEE DELIBERATIONS (ITEM #1 – ADOPTED BY LFC IN JUNE 2010)

For consistency and clarity of the budget process, the subcommittees should start from the same starting point. In order to discuss this point, a graphic of the budget structure may help.



The components of the budget are shown above. The recommendation is that every subcommittee start at the same point for each agency in their section of the budget. For the upcoming 2011 session, additional components are included in the directions provided to the appropriations subcommittees for its starting points. The initial motion of each subcommittee for each agency under its purview will require the starting point to include the adjusted base budget and the statewide present law adjustments, plus any decision packages necessary to implement the 2 percent reductions approved in the 2009 session (as ongoing) and the 5% reduction plans that are submitted by agencies with the executive budget requests. This change was discussed and adopted by the Legislative Finance Committee in its June 2010 meeting.

Actual FY 2010 expenditures, excluding the one-time expenditures, are the base budget and are the first step in this process to build the budget. The next step is to identify the funding that is necessary to fund the budget in FY 2012 and FY 2013 at the same level of services, defined as “present law”. This is not about new programs. It simply maintains existing programs and services at levels consistent with requirements of “present law.” There are two components of present law adjustment: 1) statewide present law adjustments, and 2) all other present law adjustments.

Statewide present law adjustments relate to a specific group of expenditures that have broad impact because these expenditures impact every state agency. These items include:

- Personal Services – adjustments which fully fund the existing positions of state government by:

- Restoring amounts unfunded in the previous session because of vacancy savings or other reductions;
  - Funding employee pay plan costs that result from delayed implementation of pay schedules or employer benefit contributions;
  - Accounting for changes in position costs that result from market adjustments or the reclassification of positions to meet agency needs; and
  - Accounting for changes in employer costs resulting from rate changes such as for workers compensation insurance.
- Vacancy Savings – adjustments for the vacancy savings factor applied in the executive budget, 4 percent for the 2013 biennium or other level adopted by the committee (see decision item #2).
  - Fixed Costs – Adjustments proposed in rates charged to state agencies by other state agencies for services provided such as warrant writing services and office space rent.
  - Inflation/Deflation – adjustments for a select group of expenditure accounts that are expected to see marked increases or decreases during the upcoming biennium (e.g., natural gas costs).

The statewide present law adjustments are presented as such because it avoids hundreds of decision packages requiring the same decision, but more importantly, because it represents items that are usually treated the same for all agencies and programs and, therefore, should be handled at one time and not by each subcommittee independently. These key elements of every agency budget should be consistently applied as an equity issue among agencies and, to a lesser degree, because of budget system constraints.

By choosing to adopt a starting point that includes the base budget, the statewide present law adjustments, plus the aforementioned 2 percent reductions and 5 percent reduction plans, the legislature is not precluded from making changes to the base budget or to elements of the statewide present law budget. As will be discussed in the next section, there are ways to make changes to those items within an individual agency or globally. Options to do so will be explained.

As for the starting point for the subcommittees, there is really only one option. Taking another approach risks inconsistency and inequity in the budget process and poses significant workload issues for subcommittee members and staff.

**Adopted Recommendation for Item 1 - Adopted June 2010: The initial motion in all appropriation subcommittees for a starting point for budget deliberations shall include: the adjusted base to include personal services adjustments, statewide fixed costs, and inflation; any decision packages necessary to implement the two percent reductions approved in the 2009 session in an ongoing manner; and the five percent reduction plans provided in 17-7-111 (3)(f), MCA.**

Also adopted at the June meeting was a motion to draft the necessary bill that includes all statutory changes required to implement the 5% reduction plan.

## **HOW SUBCOMMITTEES CAN AFFECT STATEWIDE PRESENT LAW**

For each of the elements of the statewide present law adjustments, there are methods for addressing concerns about the level of funding or services provided. By the action described in the preceding section, these elements are fully funded except for the application of vacancy savings, which reduces the funding of personal services for each agency by a predetermined percent of the agencies personal services budget. In this section is a discussion of how the elements of the budget can be changed.

## **Vacancy Savings (Item #2)**

Although the executive budget will include application of a vacancy savings factor of 4%, the legislature can choose to change it as it is a policy decision for the legislature to make. Usually, the subcommittees start their deliberations with vacancy savings as proposed in the executive budget and that has been agreed to by the Legislative Fiscal Analyst. In the current budget, no agreement has been discussed. Therefore, the options below offer the legislature some choices as to what level of vacancy savings it wishes as a starting point. Thereafter, the legislature (beginning at the joint subcommittee stage of the process) may choose to change the vacancy savings rate for one or more agencies. The LFC committee may also want to discuss whether vacancy savings should be consistently applied among all agencies/programs, or whether subcommittees should consider vacancy savings on a case-by-case basis. With a few exceptions, the 2009 Legislature applied an across-the-board 7 percent vacancy savings for agencies with 20 or more FTE.

**Recommendation for Item 2 – Direct the appropriations subcommittees to adopt a global level of a personal services reduction (vacancy savings) as a starting point:**

**Option A – 4% as proposed in the Executive Budget;**

**Option B – 7% as adopted last session; or**

**Option C – Another specified level.**

## **Fixed Costs (Item #3)**

Fixed costs include such items as audit, payroll, capitol grounds maintenance, rent, and computer network and data processing charges. These interagency services are provided by a service agency and fees are charged to agencies on a uniform basis via various formulae or estimates of actual costs. Since agencies must pay all billed fixed costs, the appropriation can be adjusted only by the rates charged by the agency providing the service. Any changes in fixed costs could be applied uniformly based upon the recommendation of the subcommittee examining the service provider's budget.

Note: The budgets of agencies/programs providing the services upon which the rates are determined would continue to be examined by subcommittees (primarily general government), and the rates would be adjusted globally by that subcommittee.

**Recommendation for Item 3 - Direct subcommittees to consistently apply fixed costs in agency budgets as included by the executive budget request. Adjustments to fixed cost rates shall be determined by the subcommittee examining the service provider (e.g., ITSD costs as reviewed by the General Government Subcommittee) and shall be globally adjusted on a consistent basis.**

## **Inflation/Deflation (Item #4)**

The executive budget will include and identify expenditure categories that are inflated or deflated based upon analysis of those items. The subcommittees would determine the appropriate level of expenditures in each of the expenditure categories prior to inflation/deflation, and allow

inflation/deflation to be automatically calculated based on globally determined inflation rates. If the full appropriations committee wishes to vary from the executive budget proposal inflation/deflation factors, it should establish approved inflation/deflation rates (if any) by individual object of expenditure and direct subcommittees to apply these rates to all budget adjustment recommendations. For tracking purposes, these types of adjustment would occur as decision packages.

**Recommendation for Item 4 - Direct subcommittees to not vary from the executive budget proposed inflation or deflation factors.**

## **ISSUES RELATED TO HB 2 PROCEDURES**

### **Proposals Requiring Legislation (Item #5)**

Implementation of some proposals that require general appropriations act (HB 2) appropriations will require implementation of complementary legislation. The question is: How will changes in HB 2 that are dependent upon the passage of other bills be made?

**Option A - Subcommittees make recommendations regarding the proposal. Build all changes requiring legislation into the HB 2 line-items, and include contingency language striking the change if the legislation does not pass.**

**Option B - Do not include the changes requiring legislation in HB 2 line items, but include contingency language enacting the change if the legislation does pass.**

**Option C - Make no recommendations or adjustments to HB 2 until required legislation passes, except for K-12 inflation which is present law.**

Note: The handling of appropriations contingent on legislation can have a significant impact on the general fund status sheet tracking system. Option A was utilized in the 2003 session due to the severe deficit situation. Prior to the 2003 session and last session, Option C was the traditional method adopted for dealing with pending legislation.

### **Bill(s) to implement HB 2 (Item #6)**

Legislation to implement HB 2 can serve a number of purposes by providing a vehicle for the legislature to enact provisions related to appropriations that are not appropriate for inclusion in HB 2. Among the potential uses are to:

- Provide statutory changes necessary to implement provisions of the budget
- Provide special instructions on use of or access to appropriations
- Require agency action

If the committee, and ultimately the appropriations committees leadership, wishes to pursue this recommendation, it needs to recognize that other decisions will be required, i.e. number of bills and timing of bill(s).

**Recommendation for Item 6 - Appropriations committee leadership shall request legislation to provide a vehicle for enacting substantive language related to the implementation of appropriations in HB 2.**

## **PROCEDURES OF THE APPROPRIATIONS SUBCOMMITTEES**

### **Integrate “Goals and Objectives” into the Appropriations Process (Item #7 – Adopted by LFC in June 2010)**

State law requires agency and program goals and objectives to be specific and quantifiable to enable the legislature to establish appropriations policy. The LFD has established language within the budget analysis to remind legislators of this requirement. Reviewing goals and objectives may demonstrate to the legislature where budgetary adjustments are warranted and where the legislature might direct resources accordingly.

The Legislative Finance Committee adopted a recommendation that appropriation committee leadership integrate a few critical agency performance measures for each agency into the appropriations process, thereby setting the stage for discussing outcomes and linking appropriation decisions to goals and objectives.

#### **Adopted Recommendation for Item 7 – Adopted June 2010: Direct performance measurements to be included in the decisions of the appropriation subcommittees:**

- **Review of the starting point and discussion of anticipated outcomes given the new base. This allows for legislative discussion on current program performance, the effects of reducing the previous base and the impacts on related performance measurements**
- **Decisions on a few critical measurable performance measures for each agency made at each step of the appropriation process and formalized as part of a separate bill(s) or resolution(s).**

### **Internal Service Funded Proprietary Programs (Item #8)**

For budgets of state programs that provide services to other state programs, the main decision the legislature has is to approve the maximum level of fees (the rates) the providers can charge to users for its services. Key to evaluating the rates is an understanding of the costs to provide the service, the factors and risks behind changes in costs, and the relationship between cost and rate changes.

Historically, the executive has not included information to quantify the impacts decision packages have on rates for most provider programs, even though the requirement has been included in the executive budget instructions for the last several biennia. The quantitative rate impact information is critical for the legislature to understand how approving a decision package will impact costs in user programs and for the legislature to approve rates for provider programs. When the quantifiable impacts of a decision packages on the provider rates are not included in the executive budget, the legislature is left without a key piece of information needed to approve rates for the programs.

**Recommendation for Item 8 - Direct joint appropriation subcommittees that review proprietary rates not to approve decision packages of internal service funded proprietary programs unless quantifiable rate impact information is provided.**