EXECUTIVE BUDGET OVERVIEW

This chapter is an overview of the budget submitted for the 2003 Biennium by Governor Racicot, pursuant to statute. This overview provides an executive summary of the more detailed agency budget presentation contained in Volumes 3 and 4 of the Legislative Budget Analysis. It is intended to provide the reader with a general understanding of the major components of the budget, and includes the following sections:

- Highlights of revenue and expenditure proposals;
- Comparisons with the previous biennium;
- Executive revenue and tax policy proposals.
- Executive expenditure proposals;
- Statewide budget proposals and issues; and
- Other Executive Budget issues identified through Legislative Fiscal Division analysis.

As the reader reviews this material, it should be noted that Governor-elect Martz is likely to submit changes to this budget. Those changes are due to the legislature by January 7, 2001. An addendum to this report will be prepared by the LFD at that time.

HIGHLIGHTS

The Governor's budget reflects a 10.2 percent general fund increase and a 16.3 percent increase in total funds over the 2001 biennium. The largest increases appear in the areas of human services, higher education, and corrections. As a percentage of the total general fund budget, education has decreased as a result of declining enrollment, while other programs have experienced growth. All told, this causes the percentages of the total general fund allocated to other program categories to increase.

The highlights of the proposed budget are:

- **Human Services.** Human services would increase $410.5 million, or 25.6 percent (including almost $150 million in accounting changes). General fund would increase $70.6 million, or 15.3 percent. Major general fund increases are for increased Medicaid costs and the annualization of provider rate increases, a new provider rate increase, increased child protective services staffing and services, and enhancements to and/or annualization of cost increases in several other programs, including mental health, disabilities services, and the Children's Health Insurance Program.

- **Education.** General fund for K-12 education would increase $18.7 million, or 1.9 percent, and $50.8 million in total funds, or 4.5 percent. Declining enrollments cause BASE aid expenditures to decline by $2.8 million. The executive proposes a special education adjustment and increases the BASE aid schedules by 3 percent in fiscal 2003 at a cost of $14.4 million.

- **Higher Education.** Governor Racicot would increase general fund by $28.4 million (11.3 percent), and total funds by $31.1 million (10.9 percent). The general fund includes replacement of revenue lost by a 6 mil-levy reduction amounting to $5.8 million and an accounting change to total funds, which adds $14.5 million in federal funds. Neither of these adjustments adds additional funding. Enrollment growth is expected to be low in the 2003 biennium. The executive proposes enhanced student

assistance, replacement of the 6 mil levy revenue reduction, and increased state funding equivalent to $100 per student in fiscal 2002 and an additional $100 per student in fiscal 2003.

?? **Corrections.** Governor Racicot proposes adding general fund of $31.6 million, or 17.6 percent. Increases of $19.9 million are provided for increasing populations; costs relative to additional staff and pay exceptions account for $9.4 million.

?? **Long-Range Building Program** (LRBP). The LRBP request is for $163.7 million. Of this amount, $81.3 million is for bonded projects, which include $40.7 million for construction of a new building for the Department of Public Health and Human Services. $82.4 million is requested for the cash projects, including $4.3 million from the Long-Range Building Program Account. The Executive Budget also includes a proposal for $3.0 million in additional spending on cash projects, provided that an increase to the cigarette tax is approved.

?? **Local Government Reimbursements.** The Governor provides full funding for local government reimbursements as a result of the passage of SB 184 by the 1999 legislature. Appropriations in the 1999 biennium were $70.6 million. The Governor proposes $109.9 million in the 2003 biennium, which amounts to an additional $39.3 million.

?? **Cigarette Tax Increase.** The executive proposes an increase in the tax on cigarettes and tobacco products, which is estimated to generate $51.4 million.

BIENNIAL BUDGET COMPARISON

This section summarizes executive recommendations in comparison to expenditures for the preceding biennium.

The executive is recommending a 2003 biennium budget that includes an additional $234.0 million from the general fund, a 10.2 percent increase. Total requested increases amount to $891.2 million, a 16.3 percent spending increase. The executive proposal for general fund and total spending increases is supported by existing sources of revenue, in combination with revenues from proposed tax increases on cigarettes and tobacco products. The increased spending includes significant new proposals/initiatives that account for nearly $365 million of the budget for the 2003 biennium.

COMPARISON METHODOLOGY

The state budget is highly complex, and the methods used to compute comparisons within context of that budget can vary considerably. Without consistent comparison methodology, the comparisons can also be subject to manipulation. The Legislative Finance Committee (LFC) developed a budget comparison methodology that measures budget performance using total state expenditures for state general operations funded by taxpayer taxes, licenses, and fees. This method helps ensure proper representation, fairness, balance, and consistency. Adopted by the 1997 legislature, use of the comparison procedures became a statutory requirement at that time. These procedures provide consistency of application and help avoid the potential for manipulation when comparing information.

The comparisons on the following pages were prepared using the statutory methodology. A discussion of budget comparison methodology and the statutory requirements is included in the Budget Basics Section of this volume, on page 125.

COMPARISON TO 2001 BIENNIUM

Figures 1 and 2 compare expenditures between the 2001 to 2003 biennia for general and total funds. As shown in the tables, the largest general fund increases are found in the departments of Public Health and Human Services, Education, and Revenue. Public Health and Human Services accounts for nearly 33 percent of the entire general fund increase.

The following tables (Figures 1 and 2) are divided into three sections:

1. The top part of the table includes all appropriations recommended for inclusion in HB 2 (the General Appropriations Act) by agency.

2. Because HB 2 does not include all appropriations authorized by the legislature, the second part of the table includes additional executive recommendations. This section is referred to as "Comparable Adjustments," because the items can be compared across biennia. The total shown in the "Total Executive Budget Fiscal 02-03" (2003 biennium) column represents all recommendations made by the executive, with the exception of the non-cash portion of Long-Range Building proposals and statutory appropriations. Long-Range Building proposals are specifically excluded because spending and timing vary considerably on most building projects. The building expenditures are reflected by the debt service paid over the term of any bonding/leasing agreement. Statutory appropriations represent the executive request with adjustments made by the Legislative Fiscal Division for Revenue and Taxation Committee estimates and updated information. (Note: The total in the "Total Adjusted Fiscal 00-01" (2001 biennium) column does not represent all contingent appropriations in that biennium, which are included in the third section.)

3. The third section, "Non-comparable Adjustments," includes all 2001 biennium appropriations, including budget amendments, supplemental appropriations, and disaster/emergency costs that cannot be estimated for the next biennium. Excluded from the comparable adjustments total are probable 2003 biennium expenditures that belong in this category. Consequently, the increases of 6.1 percent for general fund and 12.3 percent for total funds do not represent a true picture of potential growth between biennia.

House Bill 2 Comparisons

Although general fund recommendations increase over 10 percent, federal special revenues reflect the greatest increase, one of more than 27.6 percent. This is primarily due to additional expenditures in:

1. Department of Commerce - $73.3 million;
2. Department of Transportation - $66.9 million; and
3. Department of Public Health and Human Services (DPHHS) – $339.7 million.

The increase in the DPHHS expenditures is largely the result of an increase in Medicaid costs and utilization, FAIM Phase II, numerous grants, and accounting changes. Expenditure increases are discussed in more detail in the "Expenditure Proposals" section of this volume, page 43.

As shown in Figure 1, the executive general fund recommendations for HB 2 increase by $216.2 million, or 10.0 percent, from the 2001 biennium. This includes $67.3 million in new proposals and $148.9 million in other adjustments.

Total funds (Figure 2) increase by $819.4 million, or 16.2 percent, including $364.7 million in new proposals and $454.7 million in other adjustments. See page ?? of this volume for a table and discussion of present law adjustments and new proposals. The largest general fund increases are in: 1) Public Health and Human Services; 2) Education; 3) Department of Revenue; and 4) Department of Corrections. The increase in total funds is due to these same factors, plus $576.1 million in additional federal funds, primarily in human services, education, Department of Transportation, and Department of Commerce.

Total Comparable Adjustments

Total comparable adjustments include all miscellaneous appropriations including the employee pay plan bill and other appropriations bills, statutory appropriations, and other expenditures and adjustments. The executive recommends $234.0 million in increased general fund expenditures for the 2003 biennium as compared to the 2001 biennium, an increase of 10.2 percent. The increase in total state funds spending over comparable 2001 biennium spending is $891.2 million, or 16.3 percent.

Non-Comparable Adjustments

Non-comparable Adjustments, the third section, shows increases of 6.1 percent general fund and 12.3 percent total funds between biennia. As stated earlier, this comparison tends to be distorted by the lack of comparable information for the 2003 biennium. This section and these comparisons are shown for

Figure 1
General Fund Comparison
01 Biennium Versus Executive Budget 03 Biennium

Agcy Code	Agency Name	Total Adjusted Fiscal 00-01	Total Exec. Budget Fiscal 02-03	Difference 03 Biennium - 01 Biennium	% Change 01 Biennium 03 Biennium
1104	Legislative Branch	$13,727,995	$16,642,699	$2,914,704	21.23%
2110	Judiciary	16,698,450	19,727,747	3,029,297	18.14%
3101	Governor's Office	6,107,847	6,533,445	425,598	6.97%
3202	Commissioner of Political Prac	685,090	701,703	16,613	2.42%
3401	State Auditor's Office	3,434,473	712,603	(2,721,870)	-79.25%
3501	Office of Public Instruction	977,050,861	995,773,196	18,722,335	1.92%
4107	Crime Control Division	5,065,023	5,212,475	147,452	2.91%
4110	Department of Justice	43,595,932	48,675,530	5,079,598	11.65%
5101	Board of Public Education	275,865	312,335	36,470	13.22%
5102	Commissioner of Higher Ed	251,633,474	280,072,935	28,439,461	11.30%
5113	School for the Deaf & Blind	6,547,437	6,850,398	302,961	4.63%
5114	Montana Arts Council	559,153	712,434	153,281	27.41%
5115	Library Commission	3,221,395	4,300,874	1,079,479	33.51%
5117	Historical Society	3,226,445	4,776,153	1,549,708	48.03%
5201	Dept. of Fish,Wildlife & Parks	836,514	867,110	30,596	3.66%
5301	Dept of Environmental Quality	6,813,027	9,516,059	2,703,032	39.67%
5401	Department of Transportation	500,000	500,000	0	0.00%
5603	Department of Livestock	1,216,622	1,318,147	101,525	8.34%
5706	Dept Nat Resource/Conservation	33,541,571	37,827,663	4,286,092	12.78%
5801	Department of Revenue	123,147,652	166,390,098	43,242,446	35.11%
6101	Department of Administration	8,173,649	7,951,032	(222,617)	-2.72%
6102	Appellate Defender	0	0	0	
6201	MT Dept of Agriculture	2,292,434	1,519,177	(773,257)	-33.73%
6401	Dept of Corrections	179,593,417	211,174,885	31,581,468	17.58%
6501	Department of Commerce	4,365,703	5,411,763	1,046,060	23.96%
6602	Labor & Industry	3,042,147	4,300,621	1,258,474	41.37%
6701	Dept of Military Affairs	5,747,977	8,910,080	3,162,103	55.01%
6901	Public Health & Human Services	461,349,673	531,923,915	70,574,242	15.30%
	Total	$2,162,449,826	$2,378,615,077	$216,165,251	10.00%
Comparable Adjustments					
	Employee Pay Proposal	In Above	31,100,000	31,100,000	
	Statutory Appropriations	83,291,000	90,000,000	6,709,000	8.05%
	Legislative Session Costs	6,700,000	7,028,000	328,000	4.90%
	Miscellaneous Appropriations	18,764,000	21,480,000	2,716,000	14.47%
	One-Time Only Costs	22,222,000		(22,222,000)	-100.00%
	Anticipated Reversions	(5,197,000)	(6,027,000)	(830,000)	15.97%
	Total With Comparable Adjustments	$2,288,229,826	$2,522,196,077	$233,966,251	10.22%
Non-Comparable Adjustments					
	Budget Amendments	0		0	
	Supplementals	38,760,000		(38,760,000)	-100.00%
	Disaster/Emergency Costs	49,497,000		(49,497,000)	-100.00%
	Total With All Adjustments	$2,376,486,826	$2,522,196,077	$145,709,251	6.13%

Figure 2
All Funds Comparison
01 Biennium Versus Executive Budget 03 Biennium

Agcy Code	Agency Name	Total Adjusted Fiscal 00-01	Total Exec. Budget Fiscal 02-03	Difference 03 Biennium - 01 Biennium	% Change 01 Biennium 03 Biennium
1104	Legislative Branch	$17,567,733	$20,886,993	$3,319,260	18.89%
1112	Consumer Counsel	1,966,309	2,214,209	247,900	12.61%
2110	Judiciary	19,990,657	23,903,847	3,913,190	19.58%
2115	Mt.Chiropractic Legal Panel	27,732	30,000	2,268	8.18%
3101	Governor's Office	6,697,076	9,384,079	2,687,003	40.12%
3202	Commissioner of Political Prac	685,090	701,703	16,613	2.42%
3401	State Auditor's Office	8,924,075	7,234,647	(1,689,428)	-18.93%
3501	Office of Public Instruction	1,140,286,401	1,191,102,011	50,815,610	4.46%
4107	Crime Control Division	25,954,645	25,908,521	(46,124)	-0.18%
4110	Department of Justice	89,475,184	100,193,761	10,718,577	11.98%
4201	Public Service Regulation	4,827,953	5,681,284	853,331	17.67%
5101	Board of Public Education	625,026	661,546	36,520	5.84%
5102	Commissioner of Higher Ed	359,740,711	398,797,029	39,056,318	10.86%
5113	School for the Deaf & Blind	7,166,362	7,498,324	331,962	4.63%
5114	Montana Arts Council	1,664,138	1,945,679	281,541	16.92%
5115	Library Commission	6,688,754	8,656,482	1,967,728	29.42%
5117	Historical Society	6,171,904	8,661,876	2,489,972	40.34%
5201	Dept. of Fish,Wildlife & Parks	87,017,798	103,005,504	15,987,706	18.37%
5301	Dept of Environmental Quality	119,526,345	115,457,590	(4,068,755)	-3.40%
5401	Department of Transportation	873,022,157	965,940,763	92,918,606	10.64%
5603	Department of Livestock	14,674,853	17,214,181	2,539,328	17.30%
5706	Dept Nat Resource/Conservation	63,653,545	77,590,695	13,937,150	21.90%
5801	Department of Revenue	131,437,558	175,795,117	44,357,559	33.75%
6101	Department of Administration	10,438,689	11,351,570	912,881	8.75%
6102	Appellate Defender	363,318	363,635	317	0.09%
6201	MT Dept of Agriculture	23,668,166	19,745,867	(3,922,299)	-16.57%
6401	Dept of Corrections	184,687,310	217,752,559	33,065,249	17.90%
6501	Department of Commerce	118,720,160	199,334,165	80,614,005	67.90%
6602	Labor & Industry	94,125,936	102,598,115	8,472,179	9.00%
6701	Dept of Military Affairs	18,398,742	27,494,119	9,095,377	49.43%
6901	Public Health & Human Services	1,607,156,894	2,017,636,629	410,479,735	25.54%
	Total	$5,045,351,221	$5,864,742,500	$819,391,279	16.24%
Comparable Adjustments					
	Employee Pay Proposal	In Above	72,976,359	72,976,359	
	Statutory Appropriations	366,049,000	384,848,000	18,799,000	5.14%
	Miscellaneous Appropriations *	18,764,000	21,480,000	2,716,000	14.47%
	Legislative Session Costs	6,700,000	7,028,000	328,000	4.90%
	One-Time Only Costs *	22,222,000		(22,222,000)	-100.00%
	Anticipated Reversions	(5,197,000)	(6,027,000)	(830,000)	15.97%
	Total With Comparable Adjustments	$5,453,889,221	$6,345,047,859	$891,158,638	16.34%
Non-Comparable Adjustments					
	Budget Amendments	35,363,000		(35,363,000)	-100.00%
	Supplementals	66,579,000		(66,579,000)	-100.00%
	Disaster/Emergency Costs	94,825,000		(94,825,000)	-100.00%
	Total With All Adjustments	$5,650,656,221	$6,345,047,859	$694,391,638	12.29%

* Only the general fund portion is shown. All funds cannot be determined based on existing budgeting and accounting records.

informational purposes only and to complete the listing of 2001 biennium expenditures.

COMPARISON CAUTION

Comparisons vs. Budget Base Adjustments

This volume compares the 2003 biennium Executive Budget to actual expenditures and adjusted fiscal appropriations for the 2001 biennium. The methodology used is that prescribed by the budget comparison statute, and upholds the concept of a comparison of the total state budget from biennium to biennium. This is a particularly useful practice due to the cyclical nature of annual budgets. However, because the Executive Budget is prepared using a different statutorily-defined process, there is a difference between the total changes indicated in this volume and those indicated in the individual agency and program budgets discussed in the Agency Budgets and Analysis Section in Volumes 3 and 4.

Because present law adjustments are added to the base year (fiscal 2000) to determine a present law budget for the 2003 biennium and budget growth as prescribed by total adjustments, the intermediate year (fiscal 2001) is ignored. This method facilitates budget development from a vantage point of recent, actual experience, but overstates true budget growth because all increases are measured from the base year.

Conversely, using the base year plus fiscal 2001 appropriations for budget comparisons more accurately reflects true budget growth. This is because the increases/decreases are measured from a biennial perspective that takes into account the annual increase from the base year as compared to the fiscal 2001 appropriated amount.

While consideration of increases over the base year is necessary to making budgetary decisions, the adjustments should not be used as measures of growth or for comparative purposes. When making comparisons, the total recommended budget for the 2003 biennium should be examined in comparison with the total 2001 biennium, as described above.

LFD ISSUE

Although statute requires that budget comparisons be completed by the Office of Budget and Program Planning and the Legislative Fiscal Division, no comparisons were provided in the Executive Budget. Therefore, no analysis of executive comparisons could be completed.

EXECUTIVE REVENUE AND TAX POLICY PROPOSALS

INTRODUCTION

EXECUTIVE GENERAL FUND REVENUES

The Executive Budget is based on estimated revenues in excess of those adopted by the Revenue and Taxation Committee on November 17, 2000. The executive included $25 million more than the Revenue and Taxation Committee for telecommunications excise tax revenues and a difference in all other categories of $1.8 million. This places the executive general fund revenue estimates $23.2 million below the $3.586 billion adopted by the committee for a three year period. For a complete discussion of revenue estimates, see "General Fund Revenue Estimates" on page 22 of this report and Volume 2 – Revenue Estimates of the LFD Budget Analysis.

TAX REFORM PROPOSALS

The Executive has proposed four initiatives that will alter taxation rates or otherwise impact the revenue in the general fund and other state funds. They are as follows:

Cigarette and Tobacco Tax Increase – The executive proposes to increase the state tax on cigarettes from 18 to 56 cents per pack, and increase the tax on tobacco from 12.5 percent of retail value to 45 percent of retail value. The distribution of cigarette tax revenue is also changed and the revenue increase to the general fund is $47.0 million during the 2003 biennium.

Cultural Heritage Loans – This proposal provides heritage tourism loans from a trust controlled by the Board of Investments for construction and maintenance of sites of historical significance. The debt service on the loans is financed by an increase from 4 percent to 5 percent in the lodging facility use tax. The revenue loss to the general fund is estimated to be $2.7 million for the 2003 biennium.

Eliminate the Termination provision for the Qualified Endowment Credit – The executive proposes to make the qualified endowment credit against income and corporate tax liability permanent by eliminating the current sunset date of December 31, 2001. The amount of the credit would also be reduced from 50 percent of the qualified gift amount to 25 percent. The revenue loss to the general fund is expected to be $5.2 million only in fiscal 2003.

Micro-Business Loans – The executive proposes to appropriate $2.5 million from the coal tax permanent trust to the Department of Commerce for additional loan authority for the micro-business finance program. The revenue loss to the general fund is estimated to be $0.4 million for the 2003 biennium.

Figure 3 shows the biennial impact of the four executive proposals, both for general fund and total funds. The table shows the dollar impact as reported in the Executive Budget report and as determined in the LFD analysis, and the difference between the two. The following discussion provides additional detail on each of these proposals.

Figure 3
Executive Budget Tax Policy Proposals
Biennial Impact
(in millions)

Executive Proposal	General Fund Executive	General Fund LFD	General Fund Difference	All Funds Executive	All Funds LFD	All Funds Difference
Cigarette & Tobacco Tax Increase	$ 47.2	$ 47.0	$ (0.2)	$ 50.8	$ 51.4	$ 0.6
Cultural Heritage Loans-Increase Bed Tax	(1.5)	(2.7)	(1.2)	4.7	3.5	(1.2)
Qualified Endowment Credit	(5.2)	(5.2)	-	(5.2)	(5.2)	-
Microbusiness Loans	(0.3)	(0.4)	(0.1)	(0.3)	(0.4)	(0.1)
Total Impacts	$ 40.2	$ 38.8	$ (1.4)	$ 50.0	$ 49.4	$ (0.6)

CIGARETTE AND TOBACCO TAX INCREASE

The Executive Budget proposes increasing the state tax on cigarettes from 18 cents per pack to 56 cents per pack. The tax on other tobacco products would also be increased, from 12.5 percent of the wholesale price to 45 percent. The act would be effective on all sales of cigarettes and tobacco products after June 30, 2001. The Legislative Fiscal Division estimates that $51.4 million in additional revenue would be raised by this proposal, $47.0 million of which would be deposited into the general fund.

The executive asserts that this tax increase is needed to:

1. help pay for prevention and treatment of tobacco illnesses;
2. deter tobacco use;
3. maintain existing state and university buildings;
4. increase revenue to fund veterans' services; and
5. account for inflationary impacts since the tax was instituted.

LFD ISSUE

Because the Executive Budget lacks specific details about this proposal, the Legislative Fiscal Division analyzed the draft legislation and conducted its own economic impact analysis. The Executive Budget estimate for the impact of the proposal is slightly lower for the 2003 biennium, showing a revenue gain of $50.4 million. This is probably due to slightly different assumptions regarding the consumption response to higher prices. The Executive Budget, however, contained no detail with which to compare consumption response assumptions

Figure 4
Executive Cigarette and Tobacco Tax Proposal
LFD Assumptions

Distribution	Current Law	Proposed Law	Revenue in Fiscal 2002 Current Law	Revenue in Fiscal 2002 Proposed Law	Revenue in Fiscal 2002 Difference
Cigarettes	**$0.18/pack**	**$0.56/pack**	----Millions----		
Tribal	Upfront Distribution		$0.291	$0.821	$0.530
DPHHS	11.11%	4.78%	1.226	1.486	0.260
LRBP	15.85%	10.25%	1.748	3.186	1.438
General Fund	73.04%	84.98%	8.057	26.411	18.354
	100.00%	100.01%	$11.322	$31.904	$20.582
Tobacco (general fund)	**12.50%**	**45.00%**	$2.294	$7.480	$5.186
Total General Fund			$10.351	$33.891	$23.540
Total Revenue			$13.616	$39.384	$25.767

Distribution	Current Law	Proposed Law	Revenue in Fiscal 2003 Current Law	Revenue in Fiscal 2003 Proposed Law	Revenue in Fiscal 2003 Difference
Cigarettes	**$0.18/pack**	**$0.56/pack**	----Millions----		
Tribal	Upfront Distribution		$0.287	$0.807	$0.521
DPHHS	11.11%	4.78%	1.200	1.455	0.255
LRBP	15.85%	10.25%	1.712	3.120	1.408
General Fund	73.04%	84.98%	7.889	25.862	17.972
	100.00%	100.01%	$11.088	$31.244	$20.156
Tobacco (general fund)	**12.50%**	**45.00%**	$2.431	$7.926	$5.495
Total General Fund			$10.320	$33.788	$23.468
Total Revenue			$13.519	$39.170	$25.651

TAX REVENUE CHANGES

The impact of the executive's proposal on cigarette and tobacco revenues is shown in Figure 4. The increase in total general fund revenue would be $47.0 million for the 2003 biennium. Biennial revenue would increase by $0.5 million to the Department of Health and Human Services (DPHHS), and $2.8 million to the Long Range Building Program (LRBP). Revenue to Indian tribes that have agreements with the state would increase by more than $1.0 million for the biennium. These estimates are based on the assumption that cigarette prices, at $2.80 per pack under current law, would increase by $0.38 per pack, or 13.6 percent, due to the tax increase. A decrease of 9.4 percent in cigarette consumption is presumed as a result of the higher price, decreased in-state purchases by nonresidents, and increased out-of-state purchases by residents. The same decline in consumption was assumed for all tobacco products.

DISTRIBUTION CHANGES

The proposal changes the distribution of cigarette tax revenue, but leaves the distribution of revenue from tobacco products unchanged. The proposed changes in the distribution of cigarette revenue follows:

- the DPHHS share would decrease from 11.11 to 4.78 percent;
- the LRBP share would decrease from 15.85 to 10.25 percent; and
- the general fund share would increase from 73.04 to 84.98 percent.

Figure 4 shows the impact of the proposal on these distributions, as well as on the revenue shared with Indian tribes. Each of the three distributions receives more revenue, but, proportionately, the general fund increase is largest. Please note that the proposed distribution percentages are over-allocated by .01 percentage points. It is assumed in Figure 2 that the percentage devoted to the general fund would be 84.97 and not 84.98 percent.

Currently, Montana has the 12th lowest cigarette tax rate in the nation. The proposal would make Montana's cigarette tax rate the 34th lowest, tied with New York. As of July 2000, surrounding states had the following cigarette tax rates:

- Montana - 18 cents;
- North Dakota - 44 cents;
- South Dakota - 33 cents;
- Wyoming - 12 cents;
- Idaho - 28 cents;
- Oregon - 58 cents; and
- Washington - 82.5 cents.

ACCOMMODATIONS TAX – CULTURAL HERITAGE LOANS

The executive is seeking approval to increase the lodging facility use tax to 5 percent from 4. The executive proposes the creation of a refundable income tax credit equivalent to 20 percent of the lodging facility use tax paid during a tax year. Money from the additional 1 percent tax rate would be deposited in a new Heritage Tourism Accommodation Tax Account (HTAA) for:

1) administrative costs;
2) debt repayment of loans made by the board of investment (BOI) for specific projects that enhance tourism facilities; and
3) other heritage tourism projects.

The executive's stated purpose for the legislation is to provide funds to enhance and maintain the sites and facilities associated with Montana's historical and cultural heritage. The Heritage Tourism Loans would be made pursuant to applications to the BOI for support. The loan recipients are limited to:

- Virginia City/Nevada City
- Daly Mansion
- Moss Mansion
- Original Governor's Mansion
- A new Historical Society Museum Center
- Local Communities
- State Park Heritage Properties
- Lewis and Clark Bicentennial Commission

The amount of each loan would be approved by a Heritage Tourism Oversight Committee. The loans would be issued incrementally over a period of 10 years and

structured for payback over a period not to exceed 20 years. The total accumulated amount of loans provided through this program could not exceed $40 million during the period between July 1, 2001 and June 30, 2011.

The following analysis of this proposal is based on draft legislation (LC1221). The Executive Budget did not contain details of this proposal.

The repayment of principal and interest associated with these loans would not be made by the loan recipients. Instead, repayment would be made by the HTAA, using proceeds from the 1 percent increase in the lodging facilities use tax. It is estimated that the tax increase would generate over $3.0 million per year. The interest charged to the HTAA over the life of the loan would reflect the short term-investment pool (STIP) rate that the BOI earns on its short term investments. The amount generated by the 1 percent tax increase should be enough to pay the principal and interest on the loans, with some left over with which to support other tourism projects.

The proposal contemplates loaning $14.5 million of the $40 million during the 2003 biennium. The executive does not specify the source of the principal. The proposed legislation allows the BOI to loan the money, but does not specify whether the money would come from the permanent coal trust, the treasure state endowment fund, the treasury cash account, or the state employee's retirement system.

This proposal would reduce general fund revenues during the 2003 and future biennia if the funds for the loan were removed from the permanent coal trust. The interest lost to the general fund would be the difference between the amount loaned multiplied by the long-term interest rate the trust normally earns, and the STIP rate at which the payback would be assessed. This would amount to approximately $0.194 million during the 2003 biennium. The general fund will not lose this interest if the source of the loans is some other trust fund.

LFD ISSUE The Executive Budget includes estimates that the revenue lost as a result of this proposal would be $580,000 in fiscal 2002 and $940,000 in fiscal 2003. This reflects the loss in interest earnings for the amount removed from the coal trust permanent fund at long-term interest rates, and does not account for return of interest at STIP rates. The net loss in interest should be $194,000 for the biennium.

LFD ISSUE The Executive Budget does not estimate the cost to create an income tax credit for payment of the increased tax. According to the Institute for Tourism and Recreation Research at the University of Montana, the amount of the Accommodations Tax paid by residents is 40 percent. Assuming all residents who pay the increased tax also claim these expenses as an income tax credit, the loss in income tax revenue deposited in the general fund would be $2.5 million during the 2003 biennium.

LFD ISSUE If the executive contemplates making the loans from the permanent coal tax trust, the Executive Budget is silent on whether or not this legislation would require a three-quarters vote of each house of the legislature. The loans from the permanent trust would be made to the HTAA and be used to pay for the projects. The projects themselves would not contribute any payback on the loans. Instead, the loans would be paid back by the HTAA account to the permanent trust with lodging facilities use tax revenues. Additionally, the return on the "loans" will be less than could be earned if the money were left in the trust from which the money would be taken.

ELIMINATE TERMINATION PROVISION OF THE QUALIFIED ENDOWMENT CREDIT

The Executive Budget includes a provision that would eliminate the termination date for the Qualified Endowment Credit against state individual and corporate income tax liability. The act authorizing the credit was passed by the 1997 legislature and has been applied to tax years since in January 1, 1997. Under current law, the act is scheduled to terminate December 31, 2001. The executive proposes permanent elimination of the termination date, which means that the credit would become permanent. The executive also proposes reducing the amount of the credit from 50 percent to 25 percent of the charitable gift portion of a planned gift.

Though the details of the proposal were included in draft legislation, the Executive Budget contains no justification for the extension of the qualified endowment credit. The following analysis is based upon that legislation.

The amount of the qualified endowment credit claimed against state income tax liability has grown significantly since it was instituted. For tax year 1997, the credit was $1.3 million and rose to $5.5 million in tax year 1999. The estimated credit for tax year 2001, the last year before scheduled termination, is $9.0 million.

LFD ISSUE The Executive Budget claims that the cost of the proposal would be $5.2 million in fiscal 2003, and assumes that the last time the current credit will be taken in its full amount would be fiscal 2002. Many users of this credit decrease withholding or estimated payments in order to reflect the expectation that their final liability will be reduced. To the extent that this is true, the loss in revenue in the 2003 biennium could be as much as $7.5 million.

EXECUTIVE MICRO BUSINESS LOAN PROPOSAL

The Executive Budget proposes the appropriation of $2.5 million from the Coal Severance Tax Permanent Fund to the Department of Commerce for the Microbusiness Finance Program. The funds would be used by certified microbusiness development corporations to make development loans. The corporations make or guarantee loans to small businesses based upon statutory conditions specifying maximum loan amounts and minimum required equity stakes, (17-6-407, MCA).

The Executive Budget gives no justification for increasing the amount of loan authority in the Micro business Program. The executive does not assert that past micro business loans have been good investments, nor is any information provided on the payback success of past loans.

LFD ISSUE The Executive Budget contains no detail relative to this proposal. The Executive Budget characterizes the impact of this proposal as a general fund expenditure increase in the amount of $150,000 per year during the 2003 biennium. The impact will be a general fund revenue reduction, not an expenditure increase. The amount by which general fund interest earnings from the coal trust permanent fund will fall is approximately $184,000 per year during the 2003 biennium.

The $2.5 million in additional loan authority would bring the total outstanding Micro business Loan Program authority to $7.5 million. It is expected that the $2.5 million would be transferred on July 1, 2001. Removing $2.5 million from the principal of the permanent trust would reduce general fund interest earnings by

approximately $184,000 in each year of the 2003 biennium.

The micro business development program has been in existence since 1991. In the past, the legislature has granted authority to make $5.0 million available to the program. Principal and interest payments are deposited into a revolving fund, which are then made available for other loans.

The decision to add $2.5 million to the Micro business Development Loan Authority will require a three quarters vote of each house of the legislature.

EXECUTIVE EXPENDITURE PROPOSALS

INTRODUCTION

This section discusses the major changes in expenditures in the 2003 biennium proposed by Governor Racicot. The purpose of this document is to provide the reader with a summary view of major trends and policies proposed. A detailed discussion of each agency's proposed budget is included in Volumes 3 and 4 of the Legislative Budget Analysis.

The discussion is confined to HB 2, which appropriates over 90 percent of all general fund expended by state government. It does not include a discussion of other major initiatives, such as the state employee pay plan, supplemental appropriations, and the cultural heritage loan program, which are discussed in the section of this report entitled "Statewide Executive Budget Proposals."

HIGHLIGHTS AND SUMMARY

Governor Racicot is proposing a budget of $2.4 billion general fund and $5.9 billion total funds over the 2003 biennium.

The eight primary policy trends in the Governor's budget are summarized below. Each is discussed in more detail in the sections that follow.

1. General fund would increase $216.2 million, or 10 percent, above the 2001 biennium.
2. The allocation of general fund would resume a shift toward human services, continue a shift towards corrections, and shift away from (K-12) education as a percentage of the total general fund budget.
3. While there are several major new initiatives (and one significant present law adjustment) prepared by the Governor, they do not dominate the increase. The overall increase in general fund is due to a number of general increases across a broad spectrum of government for on-going costs.
4. Total funds would increase $819.4 million, or 16.3 percent over the 2001 biennium.
5. Total funds increases are dominated by increases in federal funds. Federal funds total $576.1 million (27.6 percent increase), or over 70 percent of the total funds increase (including required accounting changes).
6. Increases in the Department of Public Health and Human Services dominate the change in federal funds (including required accounting changes).
7. Governor Racicot would add 541.54 FTE, or an additional 5.2 percent over the fiscal 2001 level anticipated by the 1999 legislature.
8. The state government funding structure would continue a shift toward federal funds as the largest and increasing share.

1. General fund would increase $216.2 million, or 10 percent, from the 2001 biennium.

Figure 5 shows total increases by major component.

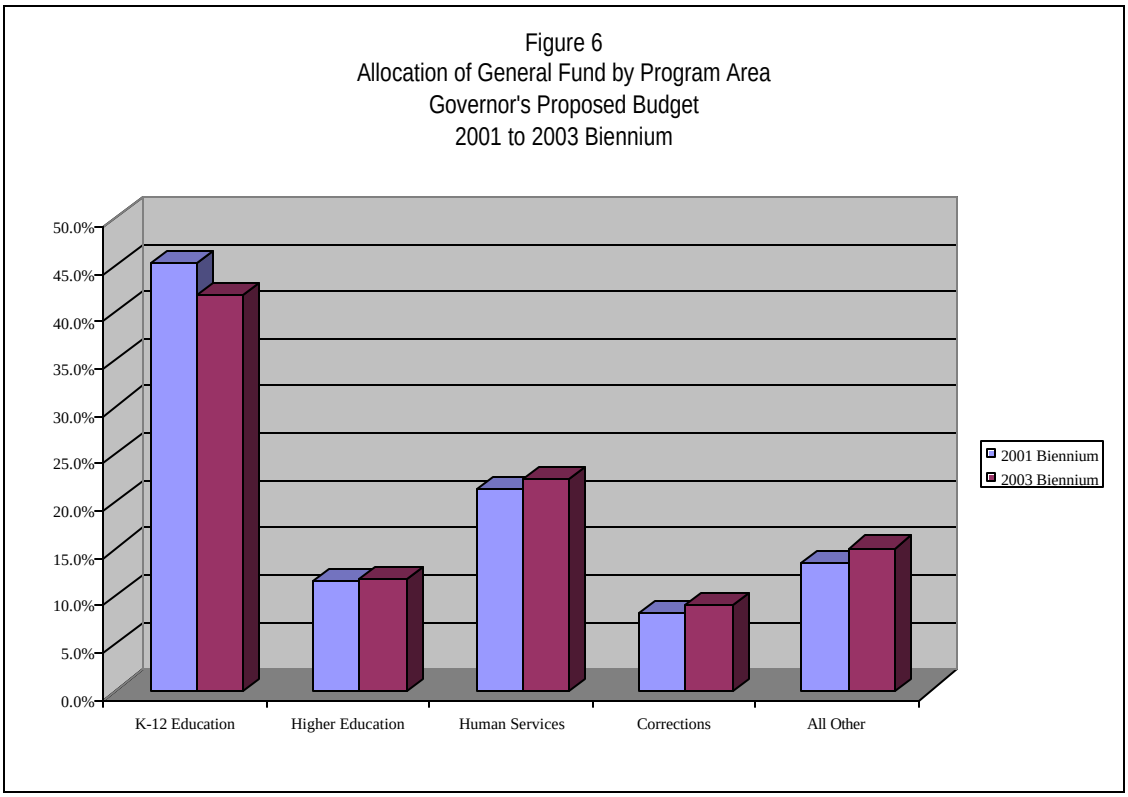
Figure 5
General Fund Increases by Major Component
2003 Biennium (in Millions)

Component	Executive Budget	Increase Over 2001	Percent Increase	Percent of Increase
K-12 Education*	$995.77	$18.72	1.9%	8.7%
Higher Education	280.07	28.44	11.3%	13.2%
Human Services	531.92	70.56	15.3%	32.6%
Corrections	211.17	31.58	17.6%	14.6%
All Other	359.68	66.87	22.8%	30.9%
Total	$2,378.62	$216.17	10.0%	100.0%

* Office of Public Instruction only

2. *The allocation of general fund in state government would resume a shift toward human services, continue a shift towards corrections, and shift away from (K-12) education as a percentage of the total general fund budget. ("All Other" is dominated by local government reimbursements in the Department of Revenue and the percent of general fund would be stable without that component.)*

Figure 6 shows the allocation of general fund increases by program area.



3. *While there are several major new initiatives (and one significant present law adjustment) prepared by the Governor, they do not dominate the increase. The overall increase in general fund is due to a number of general increases across a broad spectrum of government.*

Major new initiatives proposed by the Governor

- Provider rate increases ranging from 1.5 percent to 35 percent in human services programs – $12.8 million
- Child Protective Services enhancements and reductions in the Disability Services waiting list- $3.4 million and $2.0 million
- K-12 BASE aid increases of 3 percent and additional special education funds in fiscal 2003 - $14.4 million
- Additional state support equal to $100 per student in fiscal 2002 and an additional $100 per student in fiscal 2003 in the Montana University System – $7.5 million
- Continuations of the Project Challenge and National Guard Scholarship Programs - $2.6 million.

Because of the "stepped" implementation of several major new proposals, costs in the 2005 biennium will be significantly higher than 2003 biennium costs.

Major present law adjustments[1]

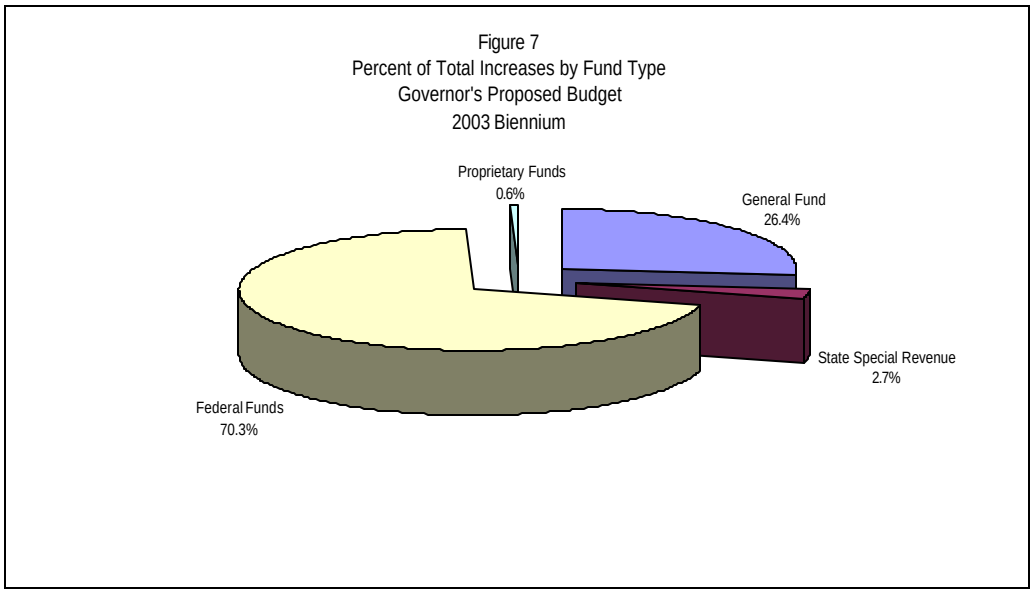
- Medicaid increases, utilization, and annualization of 2001 biennium provider rate increases – $24.0 million
- Annualization of mental health services, disability services, and the Children's Health Insurance Program (CHIP) - $16.0 million

[1] As categorized by the Governor

- Corrections population increases and pay adjustments – $19.9 million
- Pay exceptions and additional FTE in the Department of Corrections - $9.4 million
- Department of Revenue local government assistance (SB 184) – $39.3 million
- Higher Education enrollment increases and replacement of 6 mill levy – $8.4 million

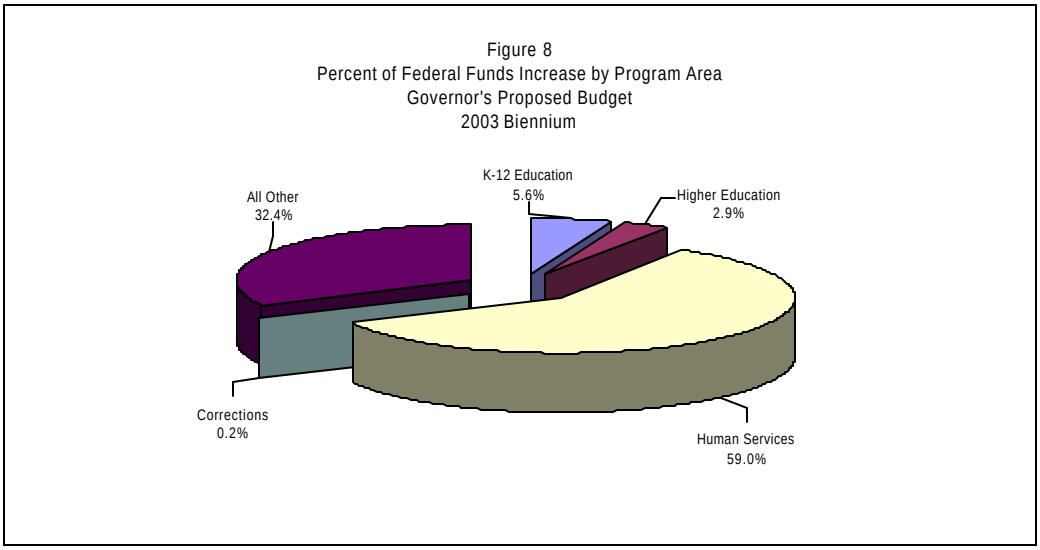
4. *Total funds would increase $819.4 million, or 16.3 percent from the 2001 biennium*

Figure 7 shows the allocation of the total increase by fund type.



5. *Total funds increases are dominated by increases in federal funds. Federal funds total $576.1 million (27.6 percent increase), or over 70 percent of the total funds increase.*

Figure 8 shows the allocation of the anticipated increase in federal funds by program area.



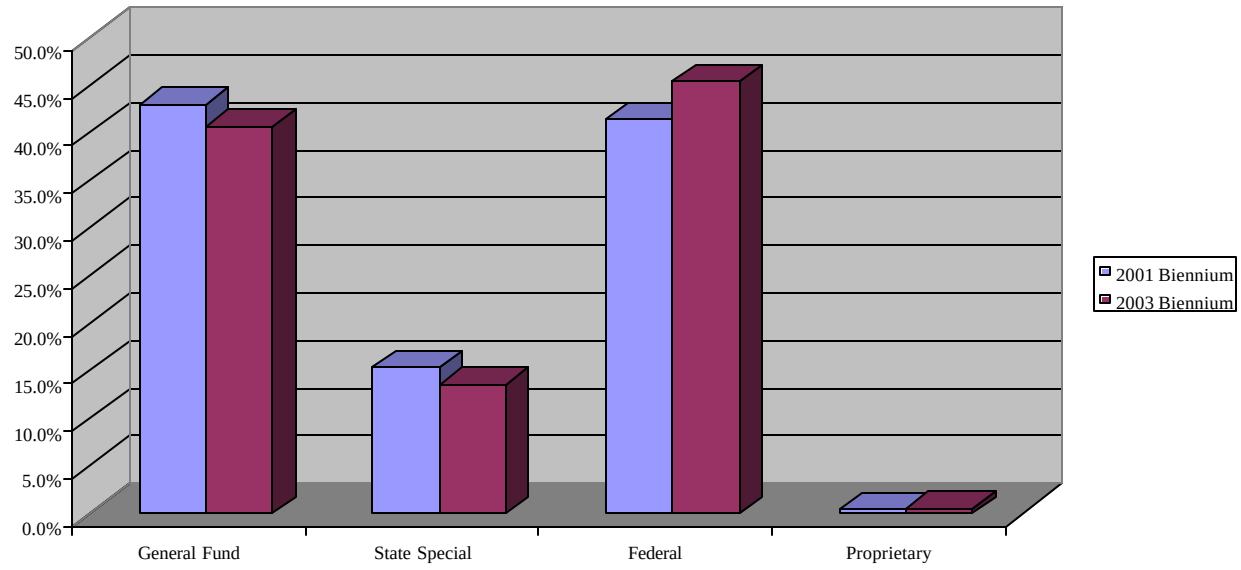
6. *Increases in the Department of Public Health and Human Services dominate the change in federal funds (including required accounting changes).*
   - ?? Medicaid and other human services programs (non-accounting changes) – $192.8 million
   - ?? Section 8 housing in the Department of Commerce – $73.1 million
   - ?? Additional construction and maintenance assumption in the Department of Transportation - $66.9 million
   - ?? Accounting changes required by the Legislative Audit Division - $161.4 million

7. *Governor Racicot would add 541.54 FTE, or an additional 5.2 percent over the fiscal 2001 level anticipated by the 1999 legislature. Major increases include:*
   - ?? 145.9 FTE in the Department of Public Health and Human Services
   - ?? 96.85 FTE in the Department of Corrections
   - ?? 111.05 FTE in the Montana Department of Transportation

8. *The structure of how state government is funded would continue a shift toward federal funds as the largest and increasing share.*
   - ?? Federal funds increase to 45.4 percent of the budget compared to 41.4 percent in the 2001 biennium.
   - ?? General fund, though increasing by 10 percent, falls to 40.6 percent of the total budget compared to 42.9 percent in the 2001 biennium.

Figure 9 shows the allocation change from the 2001 to the 2003 biennia.

Figure 9
Percent of Budget by Fund Type
Governor's Proposed Budget
2001 to 2003 Biennium



The following sections go into additional detail about Governor Racicot's expenditure proposals from several perspectives:

1. By type of fund, including general fund, state special revenue, and federal revenue.
2. By program area.
3. By present law and new proposals.

EXECUTIVE PROPOSALS BY FUND TYPE

This section discusses major proposals of Governor Racicot by fund type.

TOTAL FUNDS

Governor Racicot proposes an increase in total spending of $819.4 million, or 16.2 percent, in the 2003 biennium compared to the 2001 biennium.

Figure 10 shows the change in relative share of the state budget among the four fund types appropriated in HB 2.

Figure 10
Proposed Change by Fund Type
2003 Biennium
in Millions

Fund Type	2001 Biennium	Percent of Total	2003 Biennium	Percent Of Total
General Fund	$2,162.45	42.9%	$2,378.62	40.6%
State Special	771.51	15.3%	793.35	13.5%
Federal	2,089.26	41.4%	2,665.32	45.4%
Proprietary	22.13	0.4%	27.45	0.5%
Total	$5,045.35		$5,864.74	

- Despite a general fund increase of 10.0 percent, the 27.6 percent increase in federal funds results in general fund as a percent of the state budget falling to 40.6 percent in the 2003 biennium, compared to 42.9 percent in the 2001 biennium.

- Since state special revenue grows at a lower rate than either general fund or federal revenue, it continues to become a smaller part of state government, comprising only 15.3 percent of all HB 2 expenditures. The low growth rate is the result of a combination of increases in some agencies partially offset by decreases in others.

- The funding structure of state government would continue a shift toward federal funds as the largest and increasing share. Federal funds would increase from 41.4 percent to 45.4 percent of the total budget.

Figure 11 compares HB 2 expenditures by fund type from the 2001 to the 2003 proposed budget. The table shows the change in funding requested, and adjustments in each fund type as a percentage of total proposed expenditures. As shown, federal funds dominate all funding increases.

Figure 11
Proposed Increases by Fund Type
2003 Biennium
in Millions

Fund Type	2001 Biennium	2003 Biennium	Total Increase	Percent Increase	Percent of Total
General Fund	$2,162.45	$2,378.62	$216.17	10.0%	26.4%
State Special	771.51	793.35	21.84	2.8%	2.7%
Federal	2,089.26	2,665.32	576.07	27.6%	70.3%
Proprietary	22.13	27.45	5.32	24.0%	0.6%
Total	$5,045.35	$5,864.74	$819.39	16.2%	

Figure 12 shows the distribution of fund types among program areas of state government. As shown, distinctive program areas are funded differently. For example, corrections and K-12 education contain significant general fund. In contrast, human services receives significant federal funds, as does transportation maintenance and construction. Virtually no general fund supports transportation-related activities. The increase in federal funds is predominantly in those areas, fueling the overall increase in state government funding and in those agencies.

Figure 12
Program Area Funding By Source
2003 Biennium

Program Area	General Fund	State Special	Federal Funds	Proprietary
K-12 Education	83.6%	0.2%	16.2%	0.0%
Higher Education	70.2%	6.5%	23.3%	0.0%
Human Services	26.4%	4.1%	69.6%	0.0%
Corrections	89.8%	1.5%	0.8%	7.9%
Transportation	0.1%	36.5%	63.5%	0.0%
All Other	34.0%	31.0%	34.1%	0.8%

GENERAL FUND

Governor Racicot proposes to increase general fund spending by over $216.2 million, or 10.0 percent, in the 2003 biennium compared to the 2001 biennium. The increase is distributed across a wide range of government and is for on-going costs.

Figure 13 shows proposed changes in general fund in the major areas of state government.

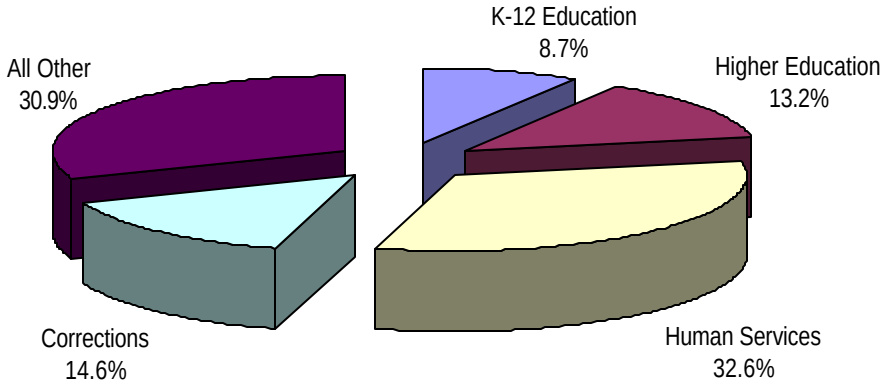
Figure 13
General Fund Increases by Major Component
2003 Biennium (in Millions)

Component	Executive Budget	Increase Over 2001	Percent Increase	Percent of Increase
K-12 Education*	$995.77	$18.72	1.9%	8.7%
Higher Education	280.07	28.44	11.3%	13.2%
Human Services	531.92	70.56	15.3%	32.6%
Corrections	211.17	31.58	17.6%	14.6%
All Other	359.68	66.87	22.8%	30.9%
Total	$2,378.62	$216.17	10.0%	100.0%

* Office of Public Instruction only

Figure 14 provides a visual representation of the proposed increases.

Figure 14
Allocation of General Fund Increases
Governor's Proposed Budget
2003 Biennium



1. Over 32 percent (almost 1/3) of the increase in general fund supports human services.
   - ?? Increased Medicaid costs and annualization of provider rate increases - $24.0 million
   - ?? Annualization of other programs, including disability services and the Children's Health Insurance Program - $10.1 million
   - ?? New Provider rate increases – $12.8 million
   - ?? Montana State Hospital and other mental health costs - $5.9 million
   - ?? Child Protective Services and a reduction in the disability services waiting list - $5.4 million

2. "All Other" accounts for over 30 percent of the growth in general fund.
   - ?? Local government assistance in the Department of Revenue as a result of the passage of SB 184 by the 1999 legislature - $39.3 million
   - ?? Present law adjustments in the Departments of Justice, Environmental Quality, and Natural Resources and Conservation - $8.9 million

3. K-12 increases by 1.9 percent, although its base size means it consumes 8.7 percent of the increase.
   - ?? A combination of enrollment declines, a fiscal 2001 schedule increase, and change in tax bases results in negative growth in the costs to maintain the current BASE aid payments – ($2.8 million)
   - ?? Proposed 3 percent increase in BASE aid schedules and an additional special education adjustment in fiscal 2003 - $14.4 million

4. While no longer dominating increases in general fund spending, the Department of Corrections continues to increase in cost above the state average.
   - ?? Increases in correctional population - $19.9 million
   - ?? Increases in staff and funding of a pay exception for correctional officers - $9.4 million

5. The Montana University System would increase by 11.3 percent.
   - ?? Enhanced state support equal to $100 per student in fiscal 2002 and an additional $100 per student in fiscal 2003 - $7.5 million
   - ?? Replacement of reduced 6 mil levy revenue - $5.8 million
   - ?? Increased enrollment and student assistance - $5.7 million

STATE SPECIAL REVENUE

State special revenue would increase $21.8 million, or 2.8 percent. This rate of growth is a combination of increases in some agencies and partially offsetting decreases in others.

- ?? The Department of Transportation, for construction, maintenance, and administration - $26.1 million. The department also replaces some maintenance costs with federal funds.
- ?? Fish, Wildlife, and Parks, for a number of general increases to operations - $5.9 million
- ?? The Department of Environmental Quality for potential bond forfeitures – ($36 million)
- ?? The Department of Natural Resources and Conservation, for state owned water projects rehabilitation - $3.6 million
- ?? The Commissioner of Higher Education to replace reduced 6 mill levy revenue with general fund - ($5.8 million)

FEDERAL FUNDS

Governor Racicot proposes an increase in federal funds of $576.1 million, or 27.6 percent. Of this total, 28 percent ($161.4 million) is due to accounting changes required by the Legislative Auditor. Figure 15 shows the proposed allocation, by program area. The Department of Public Health and Human Services would receive $339.7 million, or almost 60 percent of the total. However, if required accounting changes were removed, DPHHS would receive $192.8 million, or 33.5 percent of the total. The "All Other" program area is dominated by adjustments in the Montana Department of Transportation and the Department of Commerce.

Figure 15
Proposed Allocation of Federal Funds
By Program Area
2003 Biennium (in Millions)

Program Area	2001 Biennium	2003 Biennium	Total Increase	Percent Increase	Percent of Total
K-12 Education	$ 160.73	$ 193.16	$ 32.43	20.2%	5.6%
Higher Education	76.39	92.91	16.52	21.6%	2.9%
Human Services	1,063.93	1,403.65	339.72	31.9%	59.0%
Corrections	1.04	1.95	0.91	87.3%	0.2%
All Other	787.17	973.65	186.48	23.7%	32.4%
Total	$ 2,089.26	$ 2,665.32	$ 576.07	27.6%	

The major increases in federal funds for the Department of Public Health and Human Services are:

- ?? Implementation of Families Achieving Independence in Montana (FAIM) Phase II - $29.3 million
- ?? Funding changes and adjustments in public assistance benefits and administration - $5.3 million
- ?? Medicaid caseload, utilization growth, and annualization of provider rate increases - $126.0 million
- ?? Additional provider rate increases - $25.5 million
- ?? Increases in child care funding - $12.9 million
- ?? Increases in numerous federal grants and federally funded programs - $25.0 million

Other major increases in federal funds include:

- ?? Increases in construction and maintenance in the Department of Transportation - $66.9 million
- ?? Federal grants in the Office of Public Instruction - $32.4 million
- ?? Section 8 housing in the Department of Commerce - $73.1 million
- ?? Accounting changes required by the Legislative Auditor - $161.4 million

EXPENDITURE PROPOSALS BY PROGRAM AREA

Governor Racicot proposes the following changes in state government expenditures, by program area.

Figure 16
General Fund Increases by Major Component
2003 Biennium (in Millions)

Component	Executive Budget	Increase Over 2001	Percent Increase	Percent of Increase
K-12 Education*	$995.77	$18.72	1.9%	8.7%
Higher Education	280.07	28.44	11.3%	13.2%
Human Services	531.92	70.56	15.3%	32.6%
Corrections	211.17	31.58	17.6%	14.6%
All Other	359.68	66.87	22.8%	30.9%
Total	$2,378.62	$216.17	10.0%	100.0%

* Office of Public Instruction only

Each program area is discussed in detail in the narrative that follows.

HUMAN SERVICES (DEPARTMENT OF PUBLIC HEALTH AND HUMAN SERVICES)

The Department of Health and Human Services 2003 biennium budget request is $410 million greater than the 2001 biennium expenditures and appropriation. The majority of the increase, $340 million, is in federal funds. General fund increases $70.5 million and state special revenues remain essentially unchanged.

General fund support for the department decreases from 28.7 percent of the 2001 biennium appropriation to 26.4 percent of the 2003 biennium budget request. The decrease in general fund as a percentage of total funding is primarily due to requests that are funded entirely with federal and other funds. The largest of the requests are:

- ?? Federal funds for food stamp benefit costs - $103.3 million
- ?? Federal and state special revenue to budget for expenditures supported by drug rebates in the Medicaid program - $37 million

- Federal funds to implement the second phase of welfare reform known as FAIM Phase II - $29.3 million

The increases for both food stamp benefits and the drug rebate revenue are due to accounting changes requiring an appropriation for expenditures that have historically been non-budgeted expenditures.

Another reason that general fund comprises a smaller share of the 2003 biennium increase shown in the agency-wide budget table is the change in the matching rate the state must pay for Medicaid benefits. The state Medicaid matching rate decreases from 27.84 percent in fiscal 2000 to 27.12 percent fiscal 2002 and 26.98 percent in fiscal 2003. Each 1 percent change in the federal matching rate for Medicaid benefits results in about a $4 million change in state Medicaid funding annually.

Although many of the significant increases included in the 2003 biennium budget request are funded with federal funds, general fund support for the department still rises about 15 percent ($70.5 million) above the 2001 biennium. Nine items comprise 84 percent of the general fund increase:

- Medicaid caseload, utilization growth, and annualization of 2001 biennium provider rate increases - $24 million general fund ($151 million total funds)
- 2003 biennium provider rate increases - $12.8 million general fund ($41.2 million total funds)
- Annualization of 2001 biennium mental health services cost overruns - $5.9 million general fund and 27 FTE ($35.8 million total funds)
- Annualization of changes made in disability services programs during the 2001 biennium - $5.6 million general fund and 20.0 FTE ($11.1 million total funds)
- Annualization of 2001 biennium start up and expansion of financial eligibility the Children's Health Insurance Program (CHIP) in fiscal 2003 - $4.5 million general fund ($23.6 million total funds)
- Child protective service enhancements - $3.4 million general fund and 26.0 FTE ($4.5 million total funds)
- Reductions to the waiting list for developmental disability services - $2.0 million general fund ($4.5 million total funds);
- Overtime, holiday, and shift differential pay at state mental health institutions - $2.0 million general fund
- General fund to offset federal fund reductions for foster care services - $1.9 million

In addition to the three most significant federally funded proposals that comprise 50 percent of the increase in federal funds between the 2003 and 2001 biennia, federal funds also increase due to:

- Childcare funding increases - $12.9 million and 3.0 FTE
- Federal block grants for alcohol prevention, treatment, and needs assessments - $10.7 million and 5.0 FTE
- Federal funding for infant formula rebates and computer system enhancements in the Women, Infants, and Children nutrition program - $8.2 million
- Funding changes and adjustments in public assistance benefits and administration - $5.3 million and 6.0 FTE
- Child and adult food care program - $3.3 million and 3.0 FTE
- Commodity and energy assistance grants - $2.8 million and 2.0 FTE

K-12 EDUCATION

The Executive Budget includes a $50.8 million increase for K-12 public school education from the 2001 biennium to the 2003 biennium. The general fund increase is $18.7 million over the biennium as compared to the 2001 biennium. Federal funds increase $32.1 million between the two biennia. The general fund increase is due primarily to three factors:

- An increase in BASE aid schedules of 3 percent in fiscal 2003 and a separate proposal to increase special education – $14.4 million
- Greater school facility payments, a new loan repayment program for teachers, establishment of a statewide mentoring and induction program for teachers, and increases in administrative costs - $4.3 million

?? Continuance of the Improving Montana Schools project - $2.2 million

Offsetting the new proposals in the general fund for education is a decline of $2.8 million between the 2001 biennium the 2003 biennium. The reduction is a combination of enrollment declines, a 6.6 percent schedule increase in fiscal 2001, changes in district tax bases in fiscal 2001, and declines in timber revenue for spending on technology[2].

Federal funds increase $32.1 million between the 2001 biennium and the 2003 biennium due to: 1) a $14.1 million increase in present law federal grants; and 2) $18.0 million in additional federal aid for reduced class-size initiative to hire more classroom personnel, an advanced placement initiative, and a school reform initiative to help low performing students.

HIGHER EDUCATION

The Executive Budget proposes a $39.1 million, or 10.9 percent, increase in total state-appropriated funding for the Montana University System. The increase is driven primarily by the factors listed below.

?? Increased state support of $100 per student for resident students in fiscal 2002 and an additional $100 per resident student in fiscal 2003 - $7.5 million

?? Additional funding for new and expanded student assistance programs - $2.2 million; and cost increases in other student assistance programs - $0.9 million

?? Increased instruction and fee waiver costs resulting from a projected biennial resident student enrollment increase of 735 in the 2003 biennium - $2.6 million

?? Annualization of fiscal 2001 salaries and other statewide present law adjustments - $4.8 million

?? Increased federal grants administered in the Office of the Commissioner of Higher Education - $2.0 million

?? An accounting change recommended by the Legislative Auditor in the Guaranteed Student Loan program requiring the agency to record defaulted student loan dollar collections at gross value, rather than net, and the amount remitted to the U.S. Department of Education as an expenditure - $14.5 million

DEPARTMENT OF CORRECTIONS

For the 2003 biennium, the department is requesting total funds of $217.8 million, of which $211.2 million is general fund. This represents an increase in total funds of 17.9 percent (17.6 percent general fund) from the 2001 to the 2003 biennia. The majority of the requested increase of $33.1 million is to fund additional contract beds in private and regional facilities and to increase the number of pre-release beds. Adult male inmates are projected to increase by 947 from the actual fiscal 2000 year-end inmate population of 7,024 to 7,971 in fiscal 2003. The adult female inmate population is projected to grow from an actual fiscal 2000 year-end total of 1,990 to 2,247 at the end of fiscal 2003, an increase of 257.

The major increases are:

?? House inmates in contract beds - $10.5 million over a base of $31.3 billion. Regional prison beds are projected to increase from 406 in fiscal 2000 to 536 in fiscal 2002 and 560 in fiscal 2003. The population at the private prison in Shelby will be increased from 426 in fiscal 2000 to 492 in fiscal years 2002 and 2003. At the end of the 2003 biennium, the executive budget projects that 44 percent of the adult male secure custody population will be housed in non-state operated prison facilities, up from 38 percent in fiscal 2000.

?? Expand the number of pre-release beds - $6.9 million. The executive is proposing to add 30 additional male beds in pre-existing facilities in fiscal 2002. In addition, the proposal provides for an additional 40 regular and 40 chemical dependency beds for males, and 20 new chemical dependency beds for females in fiscal 2003. Further, the executive added a 2.0 percent increase for inflation in fiscal 2002 and 4.0 percent in fiscal 2003 for prerelease costs.

?? Add 59.0 modified FTE (28.0 in Probation & Parole and 31.0 at MSP) and a probation and parole treatment plan, added by the department in the fall of 1999 - $4.6 million.

[2] Because the distribution to schools program will require a supplemental of $10.4 million in fiscal 2001, the actual decline between present law costs in the 2003 biennium and actual expected total costs in the 2001 biennium is $13.2 million.

- Fund a pay exception provided to correctional officers to address recruitment and retention issues - $3.4 million.
- Pine Hills Youth Correctional Facility - $2.5 million; the majority intended to cover increased operating costs due to increased populations.
- Montana Women's Prison for 21.0 new FTE to staff the prison expansion - $1.4 million.

"ALL OTHER" (GENERAL GOVERNMENT)

"All Other" consists of those agencies that do not fall into any of the categories listed above. General fund increases 22.8 percent, and total funds increases 16.3 percent in this category.

The increase in general fund is dominated by one adjustment.

- The Department of Revenue for local government reimbursements as a result of the passage of SB 184 - $39.3 million
- The Department of Military Affairs - $3.2 million general fund for multiple purposes, including continuation of the Project Challenge and the National Guard Scholarship Programs (both were made one-time-only by the 1999 legislature and were removed from the base for comparison purposes)
- The Departments of Environmental Quality, Natural Resources and Conservation, and Justice - $12.1 million for a variety of adjustments, primarily in present law

Major adjustments in other funds include:

- Department of Transportation increased construction and maintenance - $92.9 million total funds
- Department of Commerce federal Section 8 Housing grants - $73.1 million
- Department of Environmental Quality potential bond forfeitures – ($36.0 million)

FTE

Governor Racicot proposes to add 541.54 FTE, a 5.2 percent increase over the FTE level funded by the 1999 legislature. (This figure does not include any FTE that would be added in proprietary funded programs.) The increase is predominantly in three agencies.

- The Department of Corrections would add 96.85 FTE by fiscal 2003, which would increase department total FTE by almost 9.5 percent. The major increases are:
  - 59.0 FTE additional correctional officers added as modified positions in the 2001 biennium
  - 21.0 FTE to staff the expanded Montana Women's Prison
- The Department of Public Health and Human Services would add 145.9 FTE. Because this agency has a base of 2701.79 FTE, this increase is 5.4 percent. The major increases are:
  - 18.75 FTE for child protective services, and an additional 4.0 FTE for adult protective services
  - 27.0 FTE (added as modified positions in the 2001 biennium) for the Montana State Hospital based on a higher than anticipated population, and an additional 6.0 FTE for the general fund portion of mental health services
  - 20.0 FTE for the Montana Developmental Center, based on a higher than anticipated population
- The Montana Department of Transportation adds 111.0 FTE, including 26.0 temporary FTE for maintenance

EXPENDITURE PROPOSALS BY LEVEL OF SERVICE

This section discusses the Executive Budget from the viewpoint of present law adjustments and new proposals.

Figure 17 shows the proposed increases by level of service.[3]

[3] As categorized by the executive.

Figure 17
Executive Proposal
New Proposals and Present Law Adjustments
2003 Biennium, in Millions

Component	General Fund	Total Funds
Present Law Adjustments	$148.9	$454.7
New Proposals	67.3	364.7
Total	$216.2	$819.4

PRESENT LAW ADJUSTMENTS

Present law is defined in statute as "the level of funding needed under present law to maintain operations and services at the level authorized by the previous legislature…"

Since present law is, by definition, for those changes in costs due primarily to workload/caseload issues, most adjustments should be minor. There are three primary exceptions: 1) the Department of Public Health and Human Services, since all increases in benefits due to caseload and inflation growth are considered present law; 2) the Department of Corrections, where changes to respond to increasing populations are generally considered present law; and 3) K-12 and higher education enrollment changes.

K-12 and higher education enrollments are either expected to grow slowly or, in the case of K-12, actually decrease. After several biennia of uncharacteristically low growth, Medicaid caseloads in the Department of Public Health and Human Services appear to be increasing. Department of Corrections populations are also continuing to increase. In the 2003 biennium, a fourth element is added by the local government reimbursements authorized by SB 184. The significant increases in these four areas are summarized below:

- Medicaid cost increases and annualization of provider rate increases provided by the 1999 legislature will cost $151.0 million ($24.0 general fund)
- Increases in corrections populations are budgeted at $19.9 million general fund
- Increases to fund the addition of FTE in the Department of Corrections cost $9.4 million
- Enrollment increases in the Montana University System are budgeted at $2.6 million
- Full funding of local government reimbursements in the Department of Revenue total an additional $39.3 million

Present law also includes the costs to annualize the pay plan adopted by the 1999 legislature, to fully fund other personal services (minus a vacancy savings rate), and a large number of adjustments made to individual agencies. For a discussion of issues identified with the classification of some of these proposals, please see the Executive Budget – Other LFD Issues section, page 79.

NEW PROPOSALS

New proposals are defined as "requests to provide new non-mandated services, to change program services, to eliminate existing services, or to change sources of funding…" The executive is proposing $364.7 million total funds (including $67.3 million general fund) over the biennium in new proposals. An accounting change accounts for over $103 million of this adjustment.

Figure 18 shows the distribution of general fund new proposals in the Racicot budget. As shown, education and human services receive 85.9 percent of all proposed increases.

Figure 18
Distribution of General Fund New Proposals
Proposed Executive Budget
2003 Biennium

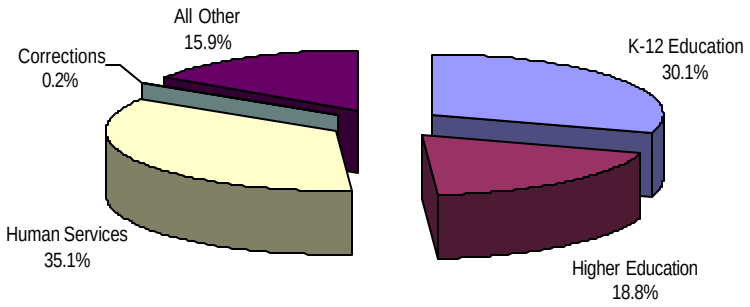
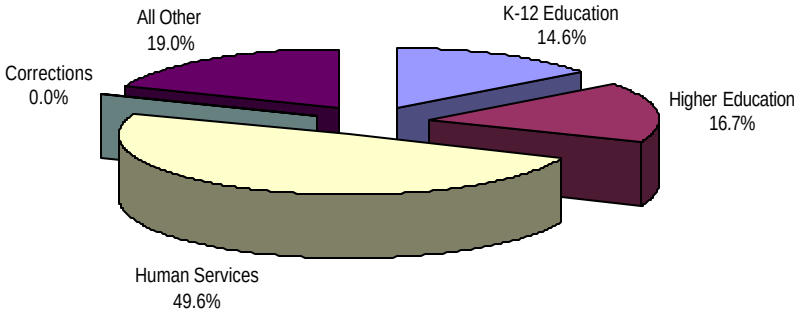


Figure 19 shows the distribution of all new proposals, minus accounting adjustments, in the Executive Budget. This figure shows that the Department of Health and Human Services receives almost half of all requested increases.

Figure 19
Distribution of Total Funds New Proposals
Proposed Executive Budget
2003 Biennium



Major new initiatives proposed by the Governor and funded with general fund include the following:

- Provider rate increases in the Department of Public Health and Human Services - $12.8 million ($41.2 million total)
- Child Protective Services and reduction in the disability services waiting list - $5.4 million
- An increase in state support for the Montana University System equal to $100 per student in fiscal 2002 and an additional $100 per student in fiscal 2003 - $7.5 million
- A 3 percent increase in fiscal 2003 in the BASE aid schedules in the Office of Public Instruction, and a separate special education increase - $14.4 million
- Continuation of the Project Challenge and the National Guard Scholarship programs in the Department of Military Affairs (the 1999 legislature made both of these program one-time-only) - $2.6 million

Several major new proposals are structured so that the full biennial cost of implementation is not realized until the next biennium. Provider rate increases, additional student support in the Montana University System, and an increase in K-12 BASE aid will all place a greater burden in the 2005 biennium than in the 2003 biennium, as shown in Figure 20 below.

Figure 20
2005 Biennium Implementation Costs
Selected Proposed New Proposals
2003 Biennium

	--- General Fund ---	
New Proposal	2003 Biennium	2005 Biennium
Provider Rate Increases*	$12.8	$16.9
MUS Increased Student Support**	7.5	10.0
K-12 BASE Aid**	14.4	28.8
Total	$34.7	$55.7

*Assumes constant caseload.

**Actual 2005 biennium costs dependent upon enrollment.

STATEWIDE EXECUTIVE BUDGET PROPOSALS/ISSUES

INTRODUCTION/HIGHLIGHTS

INTRODUCTION

This section discusses several stand-alone features of the Executive Budget that either do not pertain to any one agency, or which impact several agencies. These proposals are listed below and discussed in more detail in the following pages.

HIGHLIGHTS

- **Supplemental Appropriations – Fiscal 2001**. The executive's preliminary supplemental recommendation totals $108.6 million, of which $80.8 million is general fund, the highest supplemental request in the last eight biennia.
- **Executive Pay Plan.** The executive is proposing a $72.0 million ($30.1 million general fund) pay plan for state employees in the 2003 biennium.
- **Vacancy Savings.** The executive has applied a 3 percent vacancy savings rate to all personal services except insurance contributions. Vacancy savings reductions total $28.6 million over the 2003 biennium, of which about $12.0 million would come from the general fund.
- **Governor's Economic Development Program.** The economic development plan in the Executive Budget is, for the most part, a continuation of initiatives approved by the legislature in the May 2000 Special Session.
- **Fixed Costs.** In each agency budget, fixed costs refers to costs for services from several programs within state government that provide services to other functions of state government, for which they charge a fee. Fixed costs increase by over $17 million in the 2003 biennium.
- **Inflation/Deflation.** Applying inflation to only selected expenditure categories and underestimating others does not maintain the same level of buying power for state agencies as fiscal 2000 and, therefore, statutory present law is not maintained.
- **Long-Range Planning Proposals.** The Governor's request for Long-Range Planning includes a total of $255.8 million for grants, loans, capital projects, and information technology.

SUPPLEMENTAL APPROPRIATIONS

Supplemental appropriations are used to increase existing spending authority for a fiscal year. The supplemental appropriations requested by the executive are for additional funding applicable to the current year, fiscal 2001. The original budget for fiscal 2001 was approved by the 1999 legislature.

The executive's preliminary supplemental recommendation totals $108.6 million, of which $80.8 million comes from the general fund. As shown in Figure 21, with the exception of the 1987 biennium, this is the highest supplemental request made during the last eight biennia. However, as discussed in the LFD Issue, a portion of the funds included for fire suppression will not be needed in this bill.

Figure 21
General Fund Supplementals
1987 to 2001 Biennia

Biennium	Millions
1987	$32.7
1989	17.1
1991	20.4
1993	82.2
1995	19.9
1997	14.2
1999	11.5
2001 - Requested	80.8

Figure 22 provides detail on the executive's requested supplemental appropriations. As shown, funds are being requested for a number of agencies.

Three supplemental appropriations make up almost 99 percent of the general fund requests and the request totals:

1. Mental health and Medicaid cost increases in the Department of Public Health and Human Services;
2. Fire suppression costs in the Department of Natural Resources and Conservation; and
3. K-12 BASE Aid and timber harvest expenditures in the Office of Public Instruction.

Because fire suppression costs are not budgeted by the legislature, fire costs are expected in some degree each biennium (total costs were over $10 million in the 1999 biennium). However, this fire season was especially severe. Supplemental requests from DPHHS and OPI, however, have not been "standard" occurrences in recent bienna.

Figure 22
Proposed Supplemental Appropriations
Fiscal 2001

Agency/Purpose	General Fund	State Special	Federal Special	Total
Governor's Office				
Change in Administration	$ 144.748			$ 144.748
State Auditor				
Change in Administration	3,582	62,517		66,099
Revenue				
Change in Administration	35,575			35,575
Administration				
Day Care Center		17,500		17,500
Public Health and Human Services				
Medicaid Primary Care	2,815,616		7,554,977	10,370,593
Mental Health	11,212,392		20,090,240	31,302,632
Natural Resources and Conservation				
Fire Costs*	13,183,707			13,183,707
Other Fire and Rehabilitation Costs**	42,000,000			42,000,000
Change in Administration	12,260			12,260
Agriculture				
Change in Administration	23,154	23,154		46,308
Justice				
Change in Administration	134,927	60,056		194,983
Labor and Industry				
Change in Administration			10,360	10,360
Military Affairs				
Change in Administration	18,251			18,251
Office of Public Instruction				
K-12 BASE Aid\Timber Harvest	10,422,800			10,422,800
Change in Administration	153,249			153,249
Montana Historical Society				
Scriver Collection	249,923			249,923
Archive Change in Administration	350,000			350,000
Total	$ 80,760,184	$ 163,227	$ 27,655,577	$ 108,578,988

*Of the total, $7.1 million is requested in HB 3 (the general supplemental bill) and $6.05 million is requested in HB 17 (a proposed "emergency" supplemental bill).
**Includes $20.8 million in unknown fire and forest rehabilitation costs.

MENTAL HEALTH AND MEDICAID

The Department of Public Health and Human Services seeks a supplemental appropriation for increases in:

1. Non-mental health Medicaid services - $4.2 million;
2. Mental health Medicaid services - $7.5 million; and
3. Montana State Hospital and community mental health services - $8.5 million.

The department estimates that various cost savings measures will save $6.1 million, for a net general fund cost of $14.0 million.

A complete discussion of the supplemental request is included in the narrative for the Department of Public Health and Human Services in *Volume 3* of the *Legislative Budget Analysis*.

FIRE SUPPRESSION

The legislature does not appropriate for the costs of fire suppression in the General Appropriations Act and does not assume any costs when projecting the ending fund balance. Instead, all costs of fire suppression are requested of the next legislature as supplemental appropriations. Figure 23 shows that fire suppression costs have fluctuated widely in the last several biennia.

Figure 23
Wildfire Suppression Costs
General Fund
in Millions

Biennium	Supplemental Appropriations	Statutory Appropriations	Total
1983	$0.80		$0.80
1985	2.90		2.90
1985	3.74		3.74
1989	12.64		12.64
1991	3.00	0.05	3.05
1993	7.94	1.96	9.90
1995	15.50	8.92	24.42
1997	4.47	3.10	7.57
1999	10.55		10.55
2001*	$55.18	$6.20	$61.38

*Executive request

The amount requested by the executive represents anticipated state costs for fire suppression that must be met in the 2001 biennium fire season, and consists of 3 parts:

1. $6.1 million in HB 17 to replace $4.1 million in funding to the Department of Natural Resources and Conservation, which was transferred to fiscal 2000 to meet fire costs. An additional $2.0 million was transferred from the Water Resources Division. The executive will ask for expedited passage of this legislation;
2. $7.1 million for known costs not reimbursable by other parties; and
3. $42.0 million for other costs

LFD ISSUE

The third category includes two kinds of funds: 1) reimbursements from the Federal Emergency Management Agency (FEMA) – approximately $37 million; and 2) other costs not yet identified. The total net cost to the state for fires in the 2001 biennium is anticipated to total approximately $17 million.

There are two levels of FEMA reimbursements: 1) funds already received; and 2) funds anticipated but not yet received. Some FEMA funds will not be received until fiscal 2002. Because agencies must pay bills in fiscal 2001 prior to receipt of FEMA reimbursements, the supplemental bill must contain general fund authority to allow payment. However, the supplemental bill does not need to contain authority for expenses already reimbursed by FEMA. These costs have been accounted for in statutory appropriations, with a corresponding increase in general fund revenue. Therefore, the supplemental bill can be reduced by those payments.

The actual amount of FEMA reimbursements received by the state prior to adjournment of the legislature will be updated throughout the session.

A complete discussion of the anticipated supplemental costs resulting from fire costs is included in the narrative for the Department of Natural Resources and Conservation in *Volume 4* of the *Legislative Budget Analysis*.

K-12 BASE AID AND TIMBER HARVEST

The executive is recommending the addition of $8.9 million with which to meet statutorily-set spending amounts for BASE aid to school districts. The costs are the result of legislative changes in taxable value and in non-levy revenues. The executive also adds $1.5 million in authority to expend state lands timber harvest monies for technology acquisition, as there has been an increase in revenue from that source.

A complete discussion is included in the narrative of the Office of Public Instruction in *Volume 4* of the *Legislative Budget Analysis*.

CHANGE IN ADMINISTRATION

Figure 24 isolates the supplemental appropriations requested to pay staff termination costs in certain agencies resulting from the change in administration.

Figure 24
Change in Administration Proposed Supplemental Appropriations
Fiscal 2001

Agency	General Fund	State Special	Federal Special	Total
Agencies Headed by Elected Officials				
Governor's Office	$ 144,748			$ 144,748
State Auditor	3,582	62,517		66,099
Justice	134,927	60,056		194,983
Office of Public Instruction	153,249			153,249
Other Agencies				
Revenue	35,575			35,575
Natural Resources and Conservation	12,260			12,260
Agriculture	23,154	23,154		46,308
Labor and Industry			10,360	10,360
Military Affairs	18,251			18,251
Total	$ 525,746	$ 145,727	$ 10,360	$ 681,833

Please note that the amount requested for the Montana Historical Society would not be utilized for termination costs, but instead would be used for archival costs relative to the cumulative change in administration. The remaining costs would cover the termination costs of personnel.

The executive has indicated that these are preliminary figures and therefore subject to change as staff termination implications become better known. The amounts requested represent "worst case scenarios" for these agencies. Staff turnover is not anticipated at "worst case" levels in most instances. However, the legislature may wish to closely examine the necessity of *any* supplemental appropriation in most of these instances before making its final determinations on this bill. Because term limits ensured turnover in elected officials, the potential for termination costs was not unknown. Some planning for these costs could have been accomplished. Additionally, in some instances the requested amounts represent a very small portion of the budgets experiencing the impact.

REQUIREMENT TO REDUCE EXPENDITURES

The 1993 legislature passed legislation requiring that, in order to receive a supplemental appropriation in the first year of the biennium, agencies must detail how expenditures in the second year of operation would be reduced to contain total expenditures within the biennial appropriation. In fiscal 2000, among the programs requesting that appropriation authority be moved from the first year to the second was the Montana Historical Society. Since the executive is requesting $249,923 for this program in fiscal 2001, this program did not reduce expenditures in fiscal 2001 to cover the costs of the supplemental appropriation in fiscal 2000. The Montana Historical Society had indicated to the Legislative Finance Committee that it would seek a supplemental appropriation in order to replace those funds.

The individual supplemental requests are discussed in more detail in the individual agency narratives in the *Agency Budget Analysis* section of the *Legislative Budget Analysis*.

OTHER POTENTIAL SUPPLEMENTAL APPROPRIATIONS

Since the finalization of the Executive Budget, three other issues have surfaced that may impact the amount requested in supplemental legislation.

Department of Corrections

At the time of publication, the executive had not recommended a supplemental appropriation for the Department of Corrections, even though the department anticipates that as much as $4.5 million may be requested.

The department made several decisions relative to the 2001 biennium that may have contributed to the potential supplemental, including the addition of 59.0 FTE and providing a pay exception for correctional officers. Additionally, the distribution of male inmates to private, contracted beds and away from less expensive custody types contributed to the cost overrun.

A complete discussion is contained in the narrative for the Department of Corrections in *Volume 4* of the *Legislative Budget Analysis*.

Public Health and Human Services

As stated earlier, the Executive Budget includes a request for $14.0 million from the general fund to accommodate

increased Medicaid and mental health expenditures. Subsequent to publication of the Executive Budget, the department produced documents showing additional cost overruns of $1.4 million. Neither the department nor the executive has indicated whether an additional supplemental appropriation will be requested.

The additional projected cost overruns fall into the following areas:

1. increased Medicaid costs - $85,635;
2. Child and Family Services Division administration - $264,660;
3. additional programming costs - $246,463;
4. additional community services in the Disability Services Division - $611,133; and
5. other miscellaneous costs - $176,064.

A complete discussion is contained in the narrative for the Department of Public Health and Human Services in *Volume 4* of the *Legislative Budget Analysis*.

Department of Justice - Extradition and Transfer of Prisoners

At the time of this writing, the Governor was examining a possible over-expenditure in this program, the amount of which would fall between $14,000 and $25,000. The program reimburses county sheriffs for allowable expenses associated with transporting prisoners to Montana detention centers, as well as for expenses associated with extraditing prisoners to Montana. The Governor's Office oversees these expenditures and bills the Department of Justice.

EXECUTIVE PAY PLAN PROPOSAL

The executive is proposing a $72.0 million ($30.1 million general fund) pay plan for state employees in the 2003 biennium. This pay plan is the highest requested by the Racicot administration in four biennia and consists of two components.

1. An across-the-board 4 percent increase in salary for all employees, beginning October 1, and
2. An increase in insurance contributions of $30 per month in calendar 2002.

Figure 25 shows the total cost of the proposed pay plan in the 2003 biennium, by component

Figure 25
Proposed Executive Pay Plan
2003 Biennium

Component	Biennium General Fund	Biennium Total Funds
4 Percent Salary	$24,040,604	$57,486,594
Insurance	6,059,396	14,489,765
Total	$30,100,000	$71,976,359

Figure 26 shows the allocation of proposed funding by element and year.

Figure 26
Total Appropriations by Branch
2003 Biennium

	Fiscal 2002 General Fund	Fiscal 2002 Total Funds	Fiscal 2003 General Fund	Fiscal 2003 Total Funds	Biennium General Fund	Biennium Total Funds
Legislative Branch	$ 150,307	$ 180,867	$ 402,024	$ 482,912	$ 552,331	$ 663,779
Consumer Counsel	0	9,829	0	25,902	0	35,731
Judiciary	95,711	106,499	261,444	290,914	357,155	397,413
Executive Branch*	4,477,047	12,811,309	12,114,365	34,588,256	16,591,412	47,399,565
Teacher Pay Plan**	42,272	42,272	108,334	108,334	150,606	150,606
University System	3,539,813	6,633,832	8,908,683	16,695,433	12,448,496	23,329,265
Total	$ 8,305,150	$ 19,784,608	$ 21,794,850	$ 52,191,751	$ 30,100,000	$ 71,976,359

*Appropriated to OBPP for allocation among agencies.
**Appropriated to OBPP.

The executive also includes a biennial appropriation comprised of $1.0 million from the general fund and $3.0 million in other funds. This appropriation would be used as a contingency in the event that agencies have insufficient appropriations to meet all personal services costs.

BACKGROUND

State statutes contain pay matrices from which the salaries of individual employees are derived. The matrix currently in use for most state employees was instituted by the 1991 legislature and consists of three elements:

1. **The employee's grade.** Grade is a function of the type of work performed, and the skills and knowledge necessary to meet the requirements of the job.
2. **Entry salary.** Entry salary is the salary at which someone newly hired by the state would begin (exceptions exist for medical professionals and those in occupations with demonstrated recruitment and retention difficulties).
3. **Market salary.** Market salary is defined in statute as "the midpoint in a pay grade… based on the average base salary that other employers pay to employees in comparable occupations as determined by the department's salary survey of the relevant labor market."

There are currently 13 grades in the pay matrix by which most state employees are paid. Figure 27 illustrates the principles involved by using a sample using current (fiscal 2001) matrix elements.

Figure 27
Sample of State Pay Matrix
Fiscal 2001*

Grade	Entry Salary	Market Salary
8	$15,748	$18,834
13	24,286	29,403
17	35,036	42,833

As stated above, the Department of Administration is required to conduct a survey to determine market salaries as paid by other employers. The department contracts with a private firm, which samples Montana private and local government employers. The department also receives data on the salaries of state employees in the four contiguous states.

4 PERCENT SALARY INCREASE

The executive proposes a 4 percent raise in all state employees' salaries during fiscal 2002, with a further 4 percent increase during fiscal 2003, regardless of grade or type of work. The only exception would be those employees currently within 4 percent of the maximum salary for their grade; these employees would receive a smaller increase. The increase would take effect:

- ?? during the first full pay period that includes October 1 for all employees who began employment prior to September 30, 1994; and
- ?? on the employee's anniversary date of employment for all others.

For purposes of calculating costs, the executive calculated the average date for the increase as November 1.

The entry and market salaries in the pay matrices would be adjusted by 4 percent. Therefore, employees would receive an increase, but would not progress closer to market salary.

Figure 28 uses the grades shown in Figure 27 to show the pay matrix that would be in effect on October 1, 2001 (fiscal 2002).

Figure 28
Sample of State Pay Matrix
Proposed Adjustment
Fiscal 2002*

Grade	Entry Salary	Market Salary
8	$16,283	$19,474
13	25,112	30,403
17	36,227	44,289

ISSUES FOR LEGISLATIVE CONSIDERATION

There are several issues for consideration by the legislature in examining the pay plan.

Insurance

According to the executive, due to increases in health insurance costs, the additional cost to make employees "whole" (maintain the same level of coverage at the same out-of-pocket expenses) would be $51 per month in fiscal 2002 and a further $55 per month in fiscal 2003. The average state employee would see a greater out-of-pocket cost if he/she is to maintain consistent health insurance coverage. (Please be advised that these are average numbers. A number of factors influence the totals as well as the impact on any individual employee.)

Future Costs

As stated, the 4 percent general increase for state employees and the increase for insurance are phased in over the biennium. Consequently, the full biennial cost of implementing the plan is not reflected in the requested appropriation. Figure 29 shows the costs of full implementation for the 2005 biennium, as well as the projected increase over the requested 2003 biennium appropriation.

Figure 29
Costs of Proposed Pay Plan
2005 Biennium

	Salary Adjustment	Insurance	Total	Executive Request	Difference
General Fund	$40,016,006	$11,212,067	$51,228,073	$30,100,000	$21,128,073
Other Funds	55,912,983	16,467,733	72,380,716	41,876,359	30,504,357
Total	$95,928,989	$27,679,800	$123,608,789	$71,976,359	$51,632,430

Contingency Fund

As stated, the executive is proposing a biennial contingency fund of $1.0 million general fund and $3.0 million other funds. The Office of Budget and Program Planning would provide funds to agencies unable to meet personal services expenditures.

The legislature has provided a contingency fund for several biennia. The 1999 legislature established a $700,000 general fund and $950,000 other funds contingency. Figure 30 shows allocations of the contingency fund through December 1, 2000. As shown, little of the fund has been used.

Figure 30
Allocations of the Personal Services Contingency
2001 Biennium

Agency	General Fund	Other Funds
Crime Control Division	$20,000	$0
Montana Arts Council	11,768	-
Montana Historical Society	25,591	-
Total	$57,359	$0

1. Under appropriations law, as long as the purpose for which the appropriation is provided is met, any excess funds can be transferred to other uses (the Legislative Finance Committee must review proposed transfers if certain conditions are met, but cannot prevent transfers from taking place). Given the proposed size of the contingency fund, if approved, the legislature may wish to place restrictions on the appropriation to prevent the transfer of any excess funds to other uses.
2. The proposed pay plan bill contains the following language:

"The [contingency fund] if appropriated for the biennium to the Office of Budget and Program Planning to be distributed to other agencies when personnel vacancies do not occur, retirement costs exceed agencies resources, *or other contingencies arise*. [emphasis added]"

This language allows the contingency to be used for any circumstance under which the agency is unable to meet personal services expenses. As a consequence, uses of the fund may not conform to legislative action or concerns. For example, in the 1999 biennium, the contingency was used to fund pay increases in Governor's Office personal staff specifically reviewed but not funded by the legislature. Nor does the executive propose that any interim legislative committee review allocations.

The legislature may wish to specify the circumstances under which the contingency fund may or may not be used, and assign review of the allocations of the fund to the Legislative Finance Committee.

Recruitment and Retention

When the entry and market salary matrix was established, one of the legislature's goals was to address recruitment and retention issues. Their intent was to provide a means by which employees with the requisite experience could move closer to market salary levels over a period of time. The 1995 legislature instituted a "market grid" mechanism that, in part, allowed the legislature to target and differentiate certain grades for increases.

As stated, the executive proposes (as it did in the 2001 biennium) to provide a uniform, general increase to employees, without regard to grade or type of work. Consequently, the pay plan does not address issues of retention and recruitment. At the same time, the state has other mechanisms by which to address recruitment and retention difficulties. Most notably, section 2-18-303, MCA provides the mechanisms that follow.

?? The Department of Administration may develop and implement an alternate pay and classification plan for certain classes, occupations, and work units. Pay of these employees can be established and changed based on demonstrated competencies and accomplishments and other situations as identified by the Department of Administration. (Currently, statute allows for this mechanism through demonstration projects. The department is requesting elimination of the "demonstration" requirement.)

This concept is known as "broad banding". While broad banding is not designed specifically to address recruitment and retention issues, it does provide greater flexibility to employers facing these issues. Therefore, while broad banding does not inherently result in higher salaries, the experience of state government as of this writing is that salaries in general have increased.

?? The Department of Administration can develop programs that enable it to mitigate problems associated with recruitment, retention, transfer, or other exceptional circumstances. If, after review, the department finds that substantial problems exist relative to recruitment and retention because of "inadequate salaries when compared to competing employers," it can establish criteria allowing an adjustment in pay or classification through which to mitigate the problem.

The department provided an alternate pay plan for:

?? information technology professionals throughout state government, but primarily in the Department of Administration's Information Services Division; and

?? engineers in the Department of Transportation.

The legislature has provided these mechanisms in part to provide flexibility to state government with which to address emergent and systemic issues of retention and recruitment. Therefore, the legislature should be aware that adjustments in salary for a class of employees upon which a review has been conducted under these statutes could take place during the interim. Such adjustments are not overtly reviewed by the legislature prior to enactment. Additionally, once these adjustments have been made, the legislature cannot reduce employee salaries, though it can take other budgetary actions that would have the effect of requiring the agency to fund the increase without accessing additional funds.

Changes in Recent Biennia

A number of changes have taken place in the last two biennia that are not reflected in the actual pay plan legislation presented to the legislature. These changes must be funded within an agency's existing appropriations during the interim, but are built into the personal services budgets in the following biennium. Two of the most notable examples include:

1. The Department of Corrections provided an increase of $1 per hour in fiscal 2001 with an additional $1 per hour in fiscal 2002 for all corrections officers. Total costs of the adjustment are estimated at $5.9 million general fund in the 2003 biennium. For a further discussion, see the narrative for the Department of Corrections in *Volume 4, Section D* of the *Legislative Budget Analysis*.
2. The Department of Fish, Wildlife, and Parks conducted an agency-wide broad band study, after which it provided an increase to most of its employees. The overall cost of this increase was over $850,000 each year. For a further discussion of this pay plan, please see the narrative for the Department of Fish, Wildlife, and Parks in *Volume 4, Section C* of the *Legislative Budget Analysis*.

According to the Department of Administration, it is currently working on a number of broad brand projects within context of a number of agencies, including the Departments of Revenue and Commerce.

Teachers Pay Matrices

Under current statute, teachers' pay at state facilities is included by statute in pay matrices. The current matrices provide for pay based upon experience and education levels, practices common to local school districts. Generally speaking, teachers have received the same increases provided other state employees during the last two biennia. Exceptions have been made by the legislature in some instances in which disparities between state salaries and those of competing local districts were addressed. The executive includes funding (HB 13) with which to provide teachers with the same 4 percent increase that will be provided other state employees.

The executive proposes eliminating the pay matrix for teachers, instead allowing the alternative practice of establishing teachers' salaries through administrative rule and collective bargaining.

VACANCY SAVINGS

Vacancy savings is the difference between the cost of fully funding a position for the entire year and the actual cost of authorized employee positions during that period. A vacancy savings reduction, usually a percentage reduction from full funding, has been applied to budgets in prior years in recognition of the fact that staff turnover and vacancies often result in personal services expenditures lower than appropriated. This section outlines the executive's proposal for vacancy savings, and raises an issue as to whether the legislature wishes to apply further vacancy savings on certain positions.

EXECUTIVE PROPOSED VACANCY SAVINGS

The executive has applied a 3 percent vacancy savings rate to all personal services except insurance contributions. The rate is applied to all positions in the state government with the following exceptions.

1. Agencies with fewer than 20 FTE;
2. University system faculty;
3. Elected officials;
4. The legislative branch; and
5. The judicial branch.

The executive has applied vacancy savings to on-going positions and those proposed for inclusion by present law adjustments or new proposals.

Vacancy savings reductions total $28.6 million over the 2003 biennium, of which about $12.0 million would come from the general fund.

PERSONAL SERVICES CONTINGENCY

Vacancy savings are assessed against personal services budgets on the assumption that actual vacancy savings will be sufficient to cover the reduction. Sometimes, agencies don't generate enough actual vacancy savings, which results in a budget shortfall.

In order to assist agencies that have insufficient authority to meet all personal services costs in the 2003 biennium, the executive is proposing a contingency fund including $1.0 million general fund and $3.0 million other funds. Agencies experiencing this problem would have to apply to the Office of Budget and Program Planning for these funds during the biennium.

The legislature provided $700,000 general fund and $950,000 other funds for a contingency fund for the 2001 biennium. The following figure shows the allocations of general fund from the contingency through December 1, 2000 (fiscal 2001).

As shown in Figure 31, only three agencies received funding, which totaled $57,355 from the general fund contingency. No funds have been allocated from the "other funds" contingency.

Figure 31
Allocations of the Personal Services Contingency
2001 Biennium

Agency	General Fund	Other Funds
Crime Control Division	$20,000	$0
Montana Arts Council	11,768	-
Montana Historical Society	25,591	-
Total	$57,359	$0

VACANCY SAVINGS ON NEW POSITIONS

LFD ISSUE

The Executive Budget proposes an additional 493.46 FTE in fiscal 2002 and a further 48.08 (total 541.54) FTE in fiscal 2003 over the 2001 level anticipated by the legislature through new proposals and present law adjustments. (Please note that a portion of this increase consists of FTE added by the executive during the interim.) The executive applies the 3 percent vacancy savings rate to these positions, but in essence assumes that all positions will be filled on the first day of fiscal 2002 (July 2, 2001).

Since the hiring process is often time consuming, some vacancy savings (at times significant) can be presumed during the hiring process or while programs are being established.

The 1997 legislature applies a 25 percent vacancy savings rate on all new positions during the 1999 biennium.

Options:
1. Apply a 25 percent vacancy savings rate to all new positions authorized in HB 2 in fiscal 2002
2. Do not apply a vacancy savings rate.

GOVERNOR'S ECONOMIC DEVELOPMENT PROGRAM

During the May 2000 Special Session, the legislature passed HB 1. This bill provided $13.3 million in the 2001 biennium and $16.4 million in each of the 2003 and 2005 biennia for various activities designed to encourage economic development. The stated purpose of the bill was to implement programs that had not received funding because of the court's invalidation of the Coal Producers' License Tax contained in HB 260 and passed by the 1999 legislature. The bill also funded several initiatives proposed but not funded during the 1999 regular session.

The legislature made several appropriations exclusive to the 2001 biennia. The legislature also provided for statutory appropriations and transfers from the general fund through the 2005 biennium, at which time the appropriations sunset – and the programs – would be required to receive specific authorization from the legislature in order to continue. The statutory appropriations and transfers are funded from the general fund and linked to the interest income from $140 million of the permanent Coal Trust. Figure 32 summarizes the appropriations. (Note: Because the law is silent on how the appropriations will be affected if interest income does not generate the full amount of the linked appropriations, Chief Counsel of the legislative branch has stated that the law assumes a pro-ration of those appropriations.)

The legislature also made a statutory appropriation of $425,000 in each of the 2003 and 2005 biennia from the Treasure State Endowment Special Revenue Account with which to provide grants allowing communities to fund water and sewer pre-engineering work.

Figure 32
Appropriations in HB 1
2001 through 2005 Biennia

Activity	2001 Biennium	2003/2005 Biennia (Each)
Agriculture and Commerce		
Growth Through Agriculture Grants and Loans	$896,000	$1,792,000
Marketing and Business Assistance (Ag)	354,000	708,000
Business Recruitment	350,000	700,000
Certified Communities	425,000	850,000
Export Trade Enhancement	300,000	600,000
Small Business Development Centers	125,000	250,000
Small Business Innovative Research	50,000	100,000
Industrial Infrastructure Reimbursement	600,000	1,200,000
Cooperative Development Center	65,000	130,000
Manufacturing Extension Center	200,000	400,000
University System EPSCoR Grant Match	4,400,000	0
Board of Research and Commercialization		
Grants and Loans	2,350,000	9,700,000
Board Administration*	150,000	0
Treasure State Endowment	$3,000,000	$0
Total General Fund	$13,265,000	$16,430,000
Water and Sewer Pre-Engineering	0	425,000
Total Treasure State Endowment Funds	$0	$425,000

*Board expenses must be requested and funded in HB 2 after the 2001 biennium. The Executive Budget requests $150,000 for each year of the 2003 biennium for Board of Research and Commercialization administrative costs.

Departments of Agriculture and Commerce

The legislature funded a number of programs within the departments of Agriculture and Commerce.

Growth Through Agriculture Grants and Loans – These funds will be used to provide grants and loans through the Agriculture Development Council for projects designed to enhance value-added agriculture, including feasibility studies and marketing plans. The legislature approved $896,000 per year through fiscal 2005.

Marketing and Business Assistance – The Department of Agriculture received funding to hire additional staff (4.0 FTE) for agricultural product promotion ($170,500 each year) and agricultural business assistance ($183,500 each year).

Business Recruitment – The Department of Commerce received $350,000 per year to improve the perception of Montana's business climate by marketing Montana as a business location. A total of 2.0 FTE were included.

Certified Communities – The legislature added $425,000 per year through fiscal 2005 for grants to local economic development organizations in certified communities and counties. The maximum grant allowed to any one of the 43 certified communities was $25,000, the minimum, $5,000. The funds are designed to establish and maintain an active network of local development organizations trained and prepared to respond to economic development opportunities and concerns.

Export Trade Enhancement - $300,000 was provided for each year through fiscal 2005 with which to hire staff and maintain foreign offices designed to enhance and expand the state's efforts to develop and maintain export trade.

Small Business Development Centers – The legislature provided $125,000 per year to help provide matching funds for the federal funds available to support the Small Business Development Center Program and maintain its certification. These funds were intended to be used in conjunction with locally-generated funds.

Small Business Innovation Research - $50,000 per year was appropriated to provide technical assistance to Montana companies, thereby enabling them to compete for federal funds. The funds are targeted at building the technology business base.

Industrial Infrastructure Reimbursement

The legislature appropriated $600,000 per year through fiscal 2005 for Industrial Tax Increment Financing Districts. These funds were provided to reimburse tax revenues lost when SB 200, passed by the 1999 legislature reduced the taxable value of business equipment Industrial Tax Increment Districts were specifically excluded from reimbursement in SB 184, which was also passed by the 1999 legislature. Language provides that reimbursement will be made to qualifying Industrial Tax Increment Districts on a basis proportional to the loss of taxable value resulting from SB 200 and as documented by the Department of Revenue.

Cooperative Development Center

The Cooperative Development Center is located on the campus of Montana State University – Northern in Havre. The center, which has been in operation since January 2000, works to promote cooperatives and cooperative action geared to provide economic development in rural Montana. The legislature appropriated $65,000 per year through fiscal 2005 with which to match federal grants. The funds are used to support the director's salary, and for communication and travel expenses. If additional grants are received, the funds will be used to hire additional staff.

Manufacturing Extension Center

General fund authority of $200,000 per year through fiscal 2005 was provided to the Department of Commerce in order to provide additional support for the Manufacturing Extension Center on the campus of Montana State University – Bozeman. The center provides financial and managerial support to Montana manufacturers.

Montana University System

The legislature appropriated $4.4 million in the 2001 biennium to the Montana University System with which to match National Science Foundation EPSCoR grants. Federal EPSCoR grants are used to fund specific research projects and to provide the research infrastructure necessary to enable the campuses to win federal grants and to attract and maintain a research faculty. The appropriation was provided for the 2001 biennium only, and was meant to provide match funds for grants already accepted by the Montana University System.

Board of Research and Commercialization

The Board of Research and Commercialization was established in HB 260 by the 1999 legislature. Its purpose, within statutory guidelines, is to oversee grants and loans from the newly-created Research and Commercialization Expendable Trust Fund. Grants can be made only to provide match for grants from non-state sources, and that must be used for research and commercialization projects at research and commercialization centers in Montana.

1. $150,000 for administrative expenses of the board and $2.35 million for grants in the 2001 biennium; and
2. $4.85 million per year for grants to be made during the 2003 and 2005 biennia.

The legislature directed the Department of Commerce to request administrative expenses for the board as they apply to the 2003 biennium in HB 2. The Executive Budget requests $150,000 for each year of the 2003 biennium in support of providing for administrative costs sustained by the board. In the 2001 biennium, the funds were used primarily to hire an executive director and a support staff.

Treasure State Endowment

The legislature appropriated $3.0 million in the 2001 biennium to allow funding of all but $300,000 of the 1999

legislature's approved list of Treasure State Endowment Projects. Projects will be funded as communities complete preliminary work. It is not known at this time which projects may or may not be fully funded. The 1999 legislature made provision in HB 11 for any projects not funded in this biennium, stating that these projects would move to the top of the approved list for the next biennium. Further information on the Treasure State Endowment fund can be found on page F-7 in *Volume 4*.

Water and Sewer Pre-engineering

The legislature statutorily appropriated $425,000 from the Treasure State Endowment Special Revenue Account for each of the 2003 and 2005 biennia. These funds are to be used to provide grants to communities for water and sewer pre-engineering work. The object is to provide the resources sufficient to allow communities to accomplish the preliminary work necessary to apply for Treasure State Endowment Project Grants. The Treasure State Endowment Special Revenue Account is funded by a set amount of the Coal Severance Tax. Because the legislature traditionally appropriates all anticipated funds for projects, this appropriation will reduce the number of projects the legislature can fund.

THE 2003 BIENNIUM EXECUTIVE ECONOMIC DEVELOPMENT PLAN

Economic development was a topic that came under frequent debate during the recent election campaigns. Legislators have also identified economic development as one of the top priorities of the upcoming legislative session. The definitions of economic development are varied, as are the approaches taken to measure economic success. The Executive Budget defines the 2003 biennium economic development plan as a continuation of measures funded in HB 1. There is not a new economic development plan available for analysis, although several new initiatives relate to economic development. As an example, the Executive Budget proposes, under Long-Range Planning, a new initiative titled "Cultural Heritage Initiative." This proposal is discussed on page F-31 in *Volume* 4, and is consistent with the definition of economic development. Discussions of other specific initiatives can be found in individual program narratives.

The incoming administration has identified economic development as a key priority for the upcoming term. Although changes to the executive's economic development plan are expected, none have yet been presented. Changes can, however, be expected during the 2001 legislative session.

Funding for economic initiatives was provided in May 2000, so many programs either remain in the start-up phase, or are just starting to realize results. The legislature may wish to ask the affected departments for updates on current and projected results of particular economic development initiatives, in support of assessing the effectiveness of the initiatives approved in HB 1.

FIXED COSTS

Several programs within state government provide services to other functions of state government, for which they charge a fee. The legislature budgets funds so that the agencies receiving services can meet the costs of those services. The legislature does not appropriate funds for the provider programs because they are utilizing internal service funds, which do not require appropriations.

In those cases, the legislature approves the rates charged by provider programs.

Figure 33 details each of the internal service programs and the total fixed costs included in the Executive Budget in support of funding those functions. The figure also compares total costs in the Executive Budget in the 2003 biennium with costs budgeted in the 2001 biennium.

Figure 33
Fixed Costs*
Comparison 2001 Biennium Appropriated to 2003 Biennium Proposed (in Millions)

Subcommittee/Agency	Function	2001 Biennium	2003 Exec Budget	Percent Change***
General Government				
Administration	Insurance and Fees	$13.11	$16.71	27.4%
	Warrant Writing Fees	1.35	1.68	24.3%
	Payroll Service Fees	0.62	0.73	17.8%
	Data Network Services	15.74	19.07	21.2%
	SABHRS Operating	5.40	8.35	54.6%
	MTPRRIME Bonds	5.00	4.52	-9.5%
	Messenger Services	0.33	0.34	4.0%
	Rent - Building	9.55	10.81	13.2%
Legislative Audit Division	Audit Fees	2.65	2.97	12.0%
Transportation**	State Motor Pool	New Fixed Cost	5.88	--
Natural Resources and Commerce				
Fish, Wildlife and Parks	Grounds Maintenance	0.60	0.64	7.6%
Various	State Fund Allocation Plan	1.16	1.29	11.3%
Total		$55.50	$72.98	20.9%

*Includes all funds, including non-budgeted proprietary funds.
**Does not include $1.94 million contained in individual agency decision packages.
*** Total percentage change does not include the State Motor Pool.

As shown, fixed costs increase by over $17 million in the 2003 biennium. With the exception of messenger services and MTPRRIME bond costs, all fixed costs show significant increases over the levels appropriated for the 2001 biennium. The large increase in the requested total is primarily due to four factors.

1. Most agencies have been required by the executive to lease vehicles from the State Motor Pool in the Montana Department of Transportation instead of purchasing new cars. The Executive Budget proposes the inclusion of these leases as a fixed cost in agency budgets. Please note that the figure in the table includes only that portion contained in the statewide present law adjustments. Any new leases proposed are included as new proposals within agency budgets (Note: The State Motor Pool is discussed in more detail in the Montana Department of Transportation Budget Narrative in *Volume 3* of the *Legislative Budget Analysis*.)
2. Insurance and fees increase by 27.4 percent. The program attempts to ensure that rates will be sufficient to sustain losses in each year of the biennium equal to the average losses sustained in the last three years. The state experienced high losses in fiscal 2000, which increased the sustainable loss. (Note: This program is discussed in more detail in the Department of Administration Budget Discussion in *Volume 3* of the *Legislative Budget Analysis*.)
3. .Statewide Accounting, Budgeting, and Human Resources Systems (SABHRS) operating costs increase by 54.6 percent. This increase is due to two factors: a) assumption of licensing costs paid through a direct general fund appropriation in the 2001 biennium as part of the fixed cost; and b) proposed additional costs of operation, including vendor.
4. Maintenance, LAN upgrade and production support. (Note: SABHRS and all requested increases to operations are discussed in the Department of Administration, Information Services Division Budget Discussion in *Volume 3* of the *Legislative Budget Analysis*.)
5. Costs to operate the Information Services Division in the Department of Administration increase primarily as a result of the proposed addition of an Oracle Enterprise Licensing Agreement and in conjunction with various requests to enhance SUMMITNET, the statewide information-sharing network. (Note: The Information Services Division is discussed in more detail in the Department of Administration Budget Narrative in *Volume 3* of the *Legislative Budget Analysis*.)

Each of the fixed costs and related issues enumerated above are discussed in greater detail in the respective agency budget narratives included in Volumes 3 and 4 of the *Legislative Budget Analysis*.

INFLATION/DEFLATION

The Executive Budget does not include a general inflation factor for all operating expenses, but instead applies an inflation or deflation factor to fiscal 2000 expenditures for eight specific items.

Figure 34 shows Executive Budget inflation and deflation factors and the items to which they are applied. Of the eight items, "electricity" and "natural gas" are the only two purchased outside of state government. The other items or services are purchased from other state agencies, and payments for these items or services go into a proprietary account. The legislature sets the rates that other state agencies must pay for these items or services, and thus determines the fund levels maintained in the proprietary accounts.

Figure 34
Inflation and Deflation Factors

				Dollar Change					
		Change from Fiscal 2000		State Agencies		University System		Total	
Account	Item Name	Fiscal 2002	Fiscal 2003	Fiscal 2002	Fiscal 2003	Fiscal 2002	Fiscal 2003	Fiscal 2002	Fiscal 2003
Inflation									
2171	Mid-tier Processing	14.00%	8.00%	$43	$25	$0	$0	$43	$25
2193	Photocopier Pool	11.00%	20.00%	64,023	116,406	0	0	64,023	116,406
2404	In-state State Motor Pool	18.00%	28.00%	380,366	591,681	7,630	11,869	387,996	603,550
2601	Electricity	7.00%	9.00%	263,867	339,258	234,848	301,948	498,715	641,205
2603	Natural Gas	18.00%	10.00%	312,024	173,347	354,312	196,840	666,336	370,187
Subtotal				$1,020,325	$1,220,717	$596,790	$510,656	$1,617,115	$1,731,373
Deflation									
2172	Computer Service Charges	-20.00%	-20.00%	($1,254,443)	($1,254,443)	($1,149)	($1,149)	($1,255,592)	($1,255,592)
2175	System Development DofA	-15.00%	-15.00%	(19,683)	(19,683)	(441)	(441)	(20,124)	(20,124)
2385	Long Distance Charges DofA	-7.00%	-7.00%	(149,142)	(149,142)	(38,636)	(38,636)	(187,779)	(187,779)
Subtotal				($1,423,268)	($1,423,268)	($40,227)	($40,227)	($1,463,495)	($1,463,495)
Net Change				($402,944)	($202,552)	$556,563	$470,430	$153,620	$267,878

Deflation amounts exceed inflation amounts for all state agencies except the university system. The opposite is true in the University System where inflation amounts exceed deflation amounts. When compared with the total fiscal 2000 base operating spending of $613.1 million, net inflation by all agencies is only 0.03 percent in fiscal 2002 and 0.04 percent in fiscal 2003. This is because the number of items to which the inflation factor is applied is small, as is the resultant net inflationary increase.

Items that experience the largest increases in inflation are natural gas and electricity. These items add $1.2 million in fiscal 2002 and $1.0 million in fiscal 2003 to the Executive Budget. The largest reductions due to deflation occur in the Information Services Division (ISD): computer service charges reduce the budget by $1.3 million each fiscal year. Overall, the net change in all items due to inflation and deflation is $0.2 million in fiscal 2002 and $0.3 million in fiscal 2003.

COMPUTER SERVICE CHARGES

Computer processing rates charged by ISD will continue to decline in the 2003 biennium. Mainframe computer processing costs for the 2003 biennium are reduced 20 percent below the base expenditures made in fiscal 2000. This compares to 2001 biennium reductions of 19 percent in fiscal 2000 and 17 percent in fiscal 2001.

IN-STATE STATE MOTOR POOL

The Department of Transportation operates and maintains a fleet of vehicles available to all state employees for short-term use or for lease on extended assignments. The rental rate structure has been changed and is now based on actual miles driven and the number of hours the vehicle is under possession. The mileage rate is designed to recover "direct operation costs" such as repair labor and parts, fuel, lubricants, tires, and tubes. The possession rate is designed to recover "fixed costs" such as insurance, interest, principal payment, depreciation, and indirect expenses. Inflation has only been applied to the short-term use of vehicles. The increases in the Executive Budget for leased vehicles are requested as fixed costs. The increase in rates is primarily due to a new rate structure that includes a rate for time of possession in addition to a per mile charge. This rate structure will allow the Department of Transportation to more accurately recover fixed costs from users. The fleet of short-term use vehicles is expected to remain at 165 vehicles, consistent with fiscal 2000 numbers. Funds raised from the rates charged are deposited into a proprietary fund. For this reason, the legislature will be asked to approve these increased rates. (Note: See "Petroleum Products" below for another cause for the rate increase.)

ELECTRICITY AND NATURAL GAS

Although inflationary increases are included in the budget request, the amounts requested may not reflect market conditions. The Department of Administration has entered into a new contact for natural gas that began in September 2000 and will extend until June 30, 2002. This contract is 39.8 percent higher than the previous contract. Another indicator is that the Montana Power Company has filed for a 14.3 percent rate increase for natural gas with the Public Service Commission, which approved an interim rate increase in November 2000. Electricity prices are even more volatile. The state is paying $27.90/MWH, but Pacific Power and Light has quoted the University of Montana prices between $75/MWH and $98/MWH for fiscal 2003 and beyond. Spot prices for electricity have soared by absurd amounts. The Montana Power Company has filed for a 21.2 percent rate increase in the rates charged for electricity with the Public Service Commission, which approved an interim rate increase in November 2000.

PETROLEUM PRODUCTS

Even though the prices of gasoline and diesel have risen substantially since fiscal 2000, the Executive Budget does not provide for general inflationary increases. Instead, it appears that agencies are requesting additional funding for price increases through present law adjustments. The Department of Transportation and the Department of Justice, two of the state's largest users, are requesting present law increases for fuel that amount to $1.0 million over the biennium. The Department of Transportation includes the increases in the proprietary fund, which, if the present law adjustments are approved by the legislature, will increase the rates charged users of the state motor pool. In addition, although the Department of Transportation spent $2.2 million in fiscal 2000 for road oil, the Executive Budget does not include any increases for the 2003 biennium to meet price increases.

LFD ISSUE

1. Applying inflation to only selected expenditure categories and underestimating others does not result in the same level of buying power for state agencies as they had in fiscal 2000 and, therefore, statutory present law is not maintained. If all fiscal 2000 operating costs ($613.1 million) had been adjusted by the Consumer Price Index (CPI) in order to maintain consistent buying power in the 2003 biennium, inflated present law expenditure requests for the 2003 biennium would have increased by $82.5 million for all funds. The statutory definition of "present law adjustments" includes adjustments for inflation. The Executive Budget effectively understates present law by $82.5 million (compared to CPI) on a statewide basis, because it does not apply full inflation rates to all operating costs. For this reason, budget requests for agencies do not include true present law adjustments and will not provide the level of services provided in fiscal 2000. Because money appropriated by the legislature for other uses will have to be used to pay these unbudgeted costs, program outcomes may not be as good as expected. Full inflation has not been applied to agency expenditure requests for several biennia.
2. Using a general inflationary increase is a means to budget consistently for increased present law costs across all agencies. These increases are usually approved by the legislature as a global statewide issue. However, there appears to be a trend away from using general inflation factors in the budgeting process and relying more on individual agencies to request funding to meet cost increases in present law adjustments. This increases the number of issues that the legislature must consider and causes inconsistency among agencies. The legislature may want to consider requiring the executive branch to submit budgets that include global inflationary increases in all items for which costs are expected to increase, and to disallow inflationary increases as present law adjustments.

LONG-RANGE PLANNING PROPOSALS

The Governor's request for Long-Range Planning includes a total of $255.8 million for grants, loans, capital projects, and information technology. The request is summarized in Figure 35.

The most significant funding request for the Long-Range Planning includes a total of $166.7 million for projects included under the Long-Range Building Program (LRBP). This request, if approved, would represent the second largest Long-Range Building Program in the state's history. The Governor's LRBP bonding request for the 2003 biennium comes to a total of $81.3 million. Assuming phased issuance of the bonds, preliminary estimates show that the debt service would be $3.0 million in the 2003 biennium, but $6.8 million per year over most of the 20-year life of the bonds. Over the term of 20 years, the total cost for this bonding proposal would be approximately $136.1 million.

The Governor's Long-Range Planning package includes a request for bonding that will provide for information technology (computer hardware, software and systems development) applications. The request totals only $3.3 million, as compared to $43.0 and $18.8 million for the 1999 and 1997 biennia, respectively. The debt service for a $3.3 million bond issue, assuming a ten-year period, is estimated to cost $420,132 per year.

The Long-Range Planning package also includes a new item referred to as the "Cultural Heritage Initiative." This request proposes a $40.0 million loan from the Coal Tax Trust to be used for historic preservation and to prepare for the upcoming Lewis and Clark Bicentennial.

Section F, in *Volume 4*, includes detailed information regarding each of the programs related to Long-Range Planning.

Figure 35
Executive Budget Request
Long-Range Planning
2003 Biennium (in millions)

Program/Project	Amount	Program Total
Long-Range Building Program		$ 166,689,910
Projects Funded with Cash/Current Revenues	82,401,610	
Projects Funded with Bonded Debt	81,310,000	
Projects Funded by Proposed Cigarette Tax Increase	2,978,300	
Treasure State Endowment Program		14,803,047
Grants	14,803,047	
Loans	-	
Oil Overcharge Program		563,000
State Building Energy Conservation Program		3,000,000
Resource Indemnity Trust Grant & Loan Programs		26,440,448
Renewable Resource Grants	4,225,000	
Renewable Resource Loans	19,215,448	
Reclamantion & Development Grants	3,000,000	
Cultural & Aesthetic Grant Program		959,755
Grants	944,755	
Capitol Mural Restoration	15,000	
Information Technology Bonds		3,300,000
Coal Tax Trust Loan - Cultural Heritiage Initiative		40,000,000
Total		$ 255,756,160

EXECUTIVE BUDGET – OTHER LFD ISSUES

INTRODUCTION

This section contains LFD issues related to the Executive Budget as a whole. These issues are in addition to specific issues raised in the agency budget presentations. Each item is listed here and discussed in further detail in the following pages.

HIGHLIGHTS

Structural Balance. Structural balance refers to the matching of ongoing expenditures of government with ongoing revenues. If revenues equal or exceed expenditures, then structural balance is achieved. The legislature is facing a structural imbalance in the proposed Executive Budget.

State Accounting System (SABHRS). In July 2000, SABHRS completed its first full year of operation. Many of the problems experienced with this new system have been addressed. There are still a few long-term issues to be resolved.

Present Law and New Proposals. The distinction between what constitutes a present law adjustment and what constitutes a new proposal is an important one. Statute requires a delineation as to whether existing services or new initiatives are being funded. The LFD identified instances in which the decision packages reported as present law adjustments should be have been considered new proposals.

Budget Detail. The Executive Budget, in many instances, lacks sufficient detail to allow LFD staff to perform an effective budget analysis.

STRUCTURAL BALANCE

GENERAL FUND

Structural balance refers to the matching of *ongoing* expenditures with *ongoing* revenues. If revenues equal or exceed expenditures, then structural balance is achieved. If expenditures exceed revenues, then structural imbalance occurs. General fund expenditures chronically exceeded ongoing revenues for several biennia in the 1980s and early 1990s (see Figure 36). In order to keep the account solvent, the legislature approved numerous one-time transfers from other accounts into the general fund. They also enacted several temporary revenue increases throughout that time.

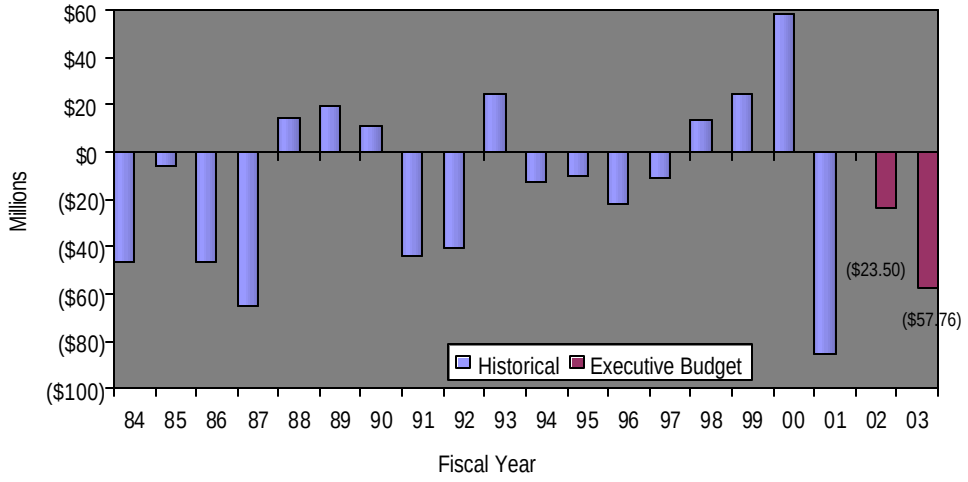
During the 1993 session, the legislature began to make progress toward addressing the problem of continuing structural imbalance in the general fund. In setting revenue and expenditure targets, the House adopted language prohibiting use of "one-time revenue...for any purpose other than creating an ending fund balance" and "temporary solutions to the state's chronic fiscal woes." This effort continued into future sessions, and final legislative actions taken during the 1993 and subsequent sessions have reflected these objectives. However, supplemental appropriations, including those made to meet unbudgeted fire suppression costs, have contributed to a small negative cash flow each biennium.

Figure 36
Revenue and Disbursement History
General Fund & School Equalization Accounts
In Millions

	Fiscal Year	General Fund Revenue	General Fund Disburse.	Surplus / Deficit	School Equalization Revenue		School Equalization Disburse.	Surplus / Deficit	GF/SEA Revenue	GF/SEA Disburse.	Surplus / Deficit
A	84	$330.305	$357.387	($27.082)	$242.384		$261.753	($19.369)	$572.689	$619.140	($46.451)
A	85	364.522	380.359	(15.837)	281.275		271.016	10.259	645.797	651.375	(5.578)
A	86	349.541	366.815	(17.274)	252.899		282.166	(29.267)	602.440	648.981	(46.541)
A	87	346.690	391.325	(44.635)	263.052		283.428	(20.376)	609.742	674.753	(65.011)
A	88	391.152	370.853	20.299	276.216	*	281.886	(5.670)	667.368	652.739	14.629
A	89	411.729	388.270	23.459	275.589	*	279.536	(3.947)	687.318	667.806	19.512
A	90	447.962	432.323	15.639	282.389		287.393	(5.004)	730.351	719.716	10.635
A	91	420.257	457.612	(37.355)	385.031		391.500	(6.469)	805.288	849.112	(43.824)
A	92	487.036	523.072	(36.036)	393.591	*	398.059	(4.468)	880.627	921.131	(40.504)
A	93	539.955	523.553	16.402	412.903		405.067	7.836	952.858	928.620	24.238
A	94	480.021	497.921	(17.900)	411.834		406.388	5.446	891.855	904.309	(12.454)
A	95	646.149	535.461	110.688	289.199	*	409.822	(120.623)	935.348	945.283	(9.935)
A	96	963.193	984.997	(21.804)					963.193	984.997	(21.804)
A	97	986.570	997.835	(11.265)					986.570	997.835	(11.265)
A	98	1,034.382	1,020.591	13.791					1,034.382	1,020.591	13.791
A	99	1,068.111	1,043.418	24.693					1,068.111	1,043.418	24.693
A	00	1,163.641	1,105.598	58.043					1,163.641	1,105.598	58.043
F	01	1,185.331	1,270.888	(85.557)					1,185.331	1,270.888	(85.557)
F	**02**	**1,215.572**	**1,239.068**	**(23.496)**	**Executive Budget Proposal**				**1,215.572**	**1,239.068**	**(23.496)**
F	**03**	**1,225.363**	**1,283.128**	**(57.765)**	**Executive Budget Proposal**				**1,225.363**	**1,283.128**	**(57.765)**

* Excludes education trust & general fund transfers.
Note: The 1995 Legislature de-earmarked school equilization revenue to the general fund.

Figure 37
General Fund Structural Balance



On the expenditure side, legislators have faced the ever-present difficulty of holding down budget growth when confronted with double-digit percentage growth in corrections costs, increased human services demands, rising enrollments and funding requirements in education, and a larger debt service obligation. In the 1993 and subsequent sessions, the legislature enacted measures to contain costs in programs growing faster than revenues, such as Medicaid and foster care. These measures were designed to slow expenditure growth, and to help the legislature reach structural balance in the general fund in future biennia.

The effort to minimize use of one-time revenues and to enact measures through which to permanently control expenditure growth has begun to show success in recent biennia. However, as we head toward the 2003 biennium, there is reason for concern. Figure 37 shows that the expenditures proposed in the Executive Budget would exceed revenues during the 2003 biennium by $81.3 million. Included in the anticipated revenue is the impact of all executive revenue proposals. In addition, some unknowns remain. The following are some fiscal concerns that may impact the general fund structural balance:

- One-time revenues – The Executive Budget includes $20.6 million in one-time revenues. Excluding these revenues from the structural balance equation, as should be done, would result in a structural imbalance of $101.9 million. In addition, if the Montana Power Company sale generates revenues, these revenues would be one-time-only and should not be included in efforts to attain structural balance.
- One-time expenditures – Although none have been identified in the Executive Budget, it is possible that some exist and/or might be proposed as the session progresses. The legislature needs to be cognizant of the potential impact of such expenditures.
- Vacancy savings – The Executive Budget recommends applying a 3 percent vacancy savings reduction to agency personal services budgets in the 2003 biennium. This tactic would be used as a measure to recoup vacancy-generated savings during the biennium. Vacancy savings reductions are temporary, but the concept has been applied during most of the last several biennia. If the vacancy savings concept were not applied, approximately $12.0 million from the general fund would be included in the base in the 2005 biennium.
- Expenditure proposals – There are three ways in which structural balance can be adversely impacted:
  - Expanded expenditure growth – such as that proposed by the Executive Budget and reflected in the proposed HB 2 general fund increase of 10 percent;
  - Realization of delayed implementation of expenditures, including the pay plan, the 3 percent BASE aid increase, and a $100 increase each year per student in the University System proposal. (For example, the 2003 biennium Executive Pay Plan would require a total $51.2 million general fund expenditure during the 2005 biennium.); and
  - Growth in services rising from expansions in such programs as Medicaid or from increases in populations addressed by the Department of Corrections. For any increase in annual expenditures, there must be ongoing revenue with which to fund it. In order to attain or maintain a structural balance, this means new revenues or revenue enhancers (e.g., tax increases), or offsetting expenditure reductions.

It is important to remain aware of structural balance (or imbalance) as the legislature considers the 2003 biennium budget. Certainly, achieving and maintaining a general fund structural balance for the 2003 biennium will make the budget process less problematic in subsequent biennia.

OTHER FUNDS

In addition to issues of structural balance in the general fund, there are issues of structural balance in some of the state special revenue accounts included in the Executive Budget. A number of functions of state government are funded from accounts that receive their income from dedicated fees and other charges. One example is the highway special revenue account, which funds highway construction and maintenance, and safety related costs.

This fund is in a state of structural imbalance. Throughout the Executive Budget, the legislature will find instances in which the executive has proposed levels of operation that exceed revenue. By budgeting from these accounts at expenditure levels that exceed ongoing revenues, the executive draws down the fund balance and creates program expenditure levels that cannot be sustained. Therefore, future legislatures would be faced with reducing program expenditure levels or increasing revenue. In agency sections of the *Budget Analysis*, staff has identified those instances in which expenditures from an account exceed anticipated ongoing revenues.

STATEWIDE ACCOUNTING BUDGETING, AND HUMAN RESOURCE SYSTEM (SABHRS)

HISTORICAL REVIEW

During July 2000, when the state accounting records for fiscal 2000 were closed, the Statewide Accounting, Budgeting, and Human Resource System (SABHRS) completed its first full year of operations. SABHRS replaced the Statewide Budgeting and Accounting System (SBAS) and the Payroll/Personnel/Position Control System (PPP). SABHRS was implemented under the project name "Montana's Project to Re-engineer the Revenue and Information Management Environment" (MT PRRIME).

The 1997 legislature funded MT PRRIME with $16.0 million of general obligations bonds when it passed HB 188, commonly referred to as the Information Technology Bonding Bill. SABHRS serves statewide accounting, budget control, and human resource functions through an enterprise supported by a proprietary fund of the Department of Administration. The system is funded with revenues from fixed costs paid by all state agencies. SABHRS is a customized version of an off-the-shelf accounting product of the PeopleSoft Corporation. Montana, through the SABHRS Services Bureau of the Department of Administration, provides operating support for the system and implements routine vendor upgrades.

SYSTEM IMPLEMENTATION

SABHRS was implemented during fiscal 2000 and received a generous amount of news coverage, largely because of well-publicized implementation problems. SABHRS did experience its share of problems during the implementation process, as most system implementations of this magnitude do. Because of the importance of the system relative to state financial records and its impact on public and private entities, the Legislative Finance Committee (LFC) monitored system implementation throughout the interim. The LFC received regular updates on system implementation from the Legislative Fiscal Division and the Department of Administration. System implementation problems identified to the LFC included:

- payroll problems;
- vendor payment problems;
- federal reporting inadequacies;
- data access problems; and
- system performance problems.

For the most part, these system implementation problems have been addressed or will be addressed with vendor upgrades. Some long-term issues have been identified, however, that may have an impact on the system at some point in the future:

- data management and archiving issues;
- system infrastructure impacts on performance; and
- system support costs.

DATA MANAGEMENT AND ARCHIVING ISSUES

SABHRS was implemented with the goals of improving efficiency and access to information. The system uses a database as a repository for the data necessary to account for the financial transactions of state entities. This data is in a constant state of being updated, queried, and used to manage state programs. The system design has resulted in a nearly four-fold increase in the volume of system-stored data, as compared to the old systems. The increased amount of data will provide management challenges in achieving system goals. Providing system access to historical data will compound data management challenges. This is different from the old systems on

which only current-year data was available. The Executive Budget includes a request for resources to develop and implement an archival plan to address this issue.

SYSTEM INFRASTRUCTURE IMPACTS ON PERFORMANCE

During seasonal periods when user demand is high (e.g., the fiscal year-end closing period), and because of the increase in database size, system infrastructure constraints have had an impact on system performance and have slowed processing times. The executive's solution to this problem is to house the various system modules on separate database servers and to change the way data is shared among users. Housing the modules on different database servers addresses the system performance issues and provides the advantage of redundancy, but increases the costs relative to purchase, operation, maintenance, and replacement that are inherent in duplicate systems.

SYSTEM SUPPORT COSTS

The 1999 legislature transferred funding and SBAS support staff from the Accounting Bureau to the SABHRS Services Bureau. Prior to the transfer, SBAS was funded with general fund. When the functions were transferred, general fund increased by nearly $0.6 million overall; proprietary funding increased by $5.3 million. For the 2001 and 2003 biennia, Figure 38 shows funding for the functions first served by SBAS and then by SABHRS. The cost to support SABHRS grew by 25.2 percent from the amount approved by the 1999 legislature when compared to the amount requested for the 2003 biennium in the Executive Budget. General fund would decrease by roughly $1.0 million due to a funding shift proposed in the Executive Budget. Proprietary costs would be allocated to agencies using an allocation method based on FTE levels. This allocation method reflects a change from the methodology used in the 2001 biennium. A more detailed discussion of the SABHRS cost growth and the allocation methodology change is provided in the program budget section for the Information Services Division of the Department of Administration, in *Volume 3* of this report; starting on page A-162.

Figure 38
SABHRS Support Costs

	2001 Biennium			2003 Biennium			
	General Fund	Proprietary	Total Funds	General Fund	Proprietary	Total Funds	Growth
Reduce SBAS Functions	$ (408,190)		$ (408,190)				
SABHRS Support Bureau	969,184	5,311,944	6,281,128	$ -	$ 7,865,955	$ 7,865,955	25.2%
Growth - SBAS to SABHRS	$ 560,994	$ 5,311,944	$ 5,872,938				

PRESENT LAW AND NEW PROPOSALS

Present law is defined in statute as "that level of funding needed under present law to maintain operations and services at the level authorized by the previous legislature, including but not limited to:

- ?? Changes resulting from legally mandated workload, caseload, or enrollment increases or decreases;
- ?? Changes in funding requirements resulting from constitutional or statutory schedules or formulas;
- ?? Inflationary or deflationary adjustments; and
- ?? Elimination of nonrecurring appropriations."

New proposals are defined as "requests to provide new non-mandated services, to change programs services, to eliminate existing services, or to change sources of funding."

Statute also states that the distinction between new proposals and adjustments to the base will be based on constitutional and statutory requirements. If either is

absent, the requested change should be requested in a new proposal.

The concept of present law versus new proposals allows the legislature to examine requested adjustments to the budgets by determination of what constitutes a change necessary or desired because of decisions already made and currently in place, versus changes desired to implement new programs or a change in direction, or because of changing financial circumstances. As such, the legislature can determine whether underlying and current decisions, policies, or statutes must be changed in order to avoid or reduce the requested adjustment, or whether the decision is significantly more discretionary. Subsequently, new proposals are generally given more scrutiny than present law adjustments because of the increased discretion they embody. There are two primary rationales for why it is imperative that requested adjustments be appropriately categorized between new proposals and present law adjustments.

1. If new programs or other policy decisions are inappropriately categorized as present law, they may not be examined with the same scrutiny as new proposals because of this inherent assumption. In addition, it is imperative to maintain the integrity of the present law adjustment concept as one that truly reflects what is needed to maintain operations.
2. New proposals are used to determine the rate or level of expansion of state government into new areas, both as requested by the executive and as implemented by the legislature. Therefore, inappropriate categorization clouds the determination of the "real" costs of providing services as currently required by law and the cost of something new. Consequently, the distinction begins to lose meaning.

The distinction between a present law adjustment and a new proposal will often be nebulous for certain types of adjustments. However, there should be little doubt in most instances, and no doubt when statutes specifically direct the type of adjustment.

The executive has generally maintained an appropriate distinction between general fund present law adjustments and new proposals. However, two adjustments with major general fund impact were inappropriately classified, as discussed below. In addition, Volumes 3 and 4 of the Legislative Budget Analysis contain a number of instances where staff has alerted the legislature to obviously inappropriate classifications in both general fund and other funds in individual agencies.

1. Department of Corrections Additional Staff – In the 2001 biennium the Department of Corrections added 59.0 FTE correctional officers without legislative review. These FTE were added to the 2003 biennium request in a present law adjustment, despite explicit expectations by the Legislative Finance Committee that they would be appropriately requested in a new proposal. Total cost is $5.9 million in the 2003 biennium
2. Local Government Reimbursements - As a result of the passage of SB 184, the 1999 legislature provided general fund to reimburse local governments for lost revenue. The 1999 legislature in special session in May, 2000 added a $37 million general fund "reserve" for increased 2003 biennium costs, but did not appropriate the funds. The legislature's chief legal counsel issued an opinion that present law for the 2003 biennium was the total appropriation provided in the 2001 biennium, or $70.6 million general fund. The executive included $109.9 million in present law, or $39.3 million more than present law.

Two major funding adjustments were made to the base, rather than segregated in decision packages for legislative review.

1. Matching Rate for Medicaid Funds – The state receives significant funding from the federal government for various Medicaid programs, for which it must pay a matching rate to receive. Due to changes in Montana's relative per capita income and other factors, Montana has to pay a smaller matching rate than was paid in fiscal 2000. The reduction in general fund and increase in federal funds was included in base funding adjustments by the executive, masking the true increase in general fund costs in several divisions of the Department of Public Health and Human Services.
2. Replacement of 9 mil and 6 mil levy revenue with general fund – Due to changes enacted by the 1999 legislature, the state will receive less revenue from the 9 mil levy collections used to fund various human services programs and the 6 mil levy used to fund the

Montana University System. The executive replaced funding from both of those sources, estimated at about $8.9 million, in base funding adjustments.

BUDGET DETAIL

Statute addresses the need of the legislature and its staff for early submission of budget detail of the entire Executive Budget, and establishes a November 15 deadline for this submission. This provides the legislature an opportunity for analysis and review of the budget proposal in preparation for the session.

Major portions of the published Racicot Budget are either presented in only outline or conceptual form, with little explanation of the policies needed to implement the proposed change or the mechanics of implementing the initiatives. In some instances, initiatives are not discussed at all in the November 15 budget document. The LFD has raised this same concern in the last three budget analyses, and while there has been some improvement over prior budget submissions, this continues to be an area that should be of concern to legislators.

The lack of budget detail made it difficult for staff to analyze many proposals thoroughly, and in many cases staff could only raise questions, since budget details were insufficient to reach conclusions and provide options. In some cases, the core details of initiatives were still being developed well after November 15. Therefore, the opportunity for the legislature to obtain a clear understanding or analysis of these issues in advance of the session is impaired.

The following list provides examples of the areas where budget detail was considered incomplete.

Long Range Planning proposals – The November 15 budget provided only summary data, and access to detailed information was unavailable. As of December 15, the publications detailing these proposals were still not available.

General Fund Balance Sheet – A number of the entries to the Executive general fund balance sheet had no explanation of their origin, and required significant follow-up to analyze their impact and issues.

Tax Policy Proposals – The Executive Budget included four tax policy proposals, but very little information was provided in the published Executive Budget. Specifics of the proposals were not available until draft bills were prepared. Further, the draft bills in some cases differ substantively from the published proposals.

Expenditure Limitation – Statute sets a growth limitation on state budget expenditure levels. The executive budget was submitted without documenting the calculation of compliance with the expenditure limitation.

OTHER MAJOR FUNDS

Governor Racicot's budget proposes the provision of funding in excess of available account funds from several state special revenue accounts with dedicated revenue sources. LFD analysts have raised issues in the agency budget analysis narratives in volumes 3 and 4 of the *LFD Budget Analysis Report* with these funds . Two significant issues of precarious or over-committed balances occur in the Highways Special Revenue Account and the resource indemnity trust accounts. These issues are described briefly below.

HIGHWAYS STATE SPECIAL REVENUE ACCOUNT

The Highways State Special Revenue Account is used to fund highway construction, maintenance, and safety activities of the departments of Transportation and Justice. The account has experienced erosion of its working capital balance due to structural imbalances between revenues and expenditures. The historical lag of revenue behind expenditure growth has driven the account to a

precarious financial position. The executive has included an initiative in the 2003 Biennium Executive Budget aimed at reversing this situation by increasing motor fuel revenues through tighter enforcement of motor fuel tax laws. However, the initiatives also increase annual administrative costs by more than $0.5 million without providing measures for assessing initiative impacts. For a further discussion, see the Highways Special Revenue Account discussion on page 100 of this volume, and in the narrative for the Department of Transportation on page A-64 in *Volume 3* of the *Legislative Budget Analysis*.

RESOURCE INDEMNITY TRUST ACCOUNTS

Seven funds derive income from the resource indemnity trust (RIT). The executive is asking for appropriations that would drive four of these funds into negative balance situations. Additionally, accounting errors have reduced the available beginning balance in 5 of the 7 funds. These errors will have a $5.3 million impact over the 2003 biennium. For a further discussion of the RIT, see the Other Fiscal Issues Section of this volume, page 100. The discussion is also contained in the narrative for the Department of Natural Resources and Conservation on page C-130 in *Volume 4* of the Legislative Budget Analysis.