LFD ANALYSIS
SPENDING REDUCTIONS PROPOSAL
PART 1 - OVERVIEW

A Report Prepared for the

Legislative Finance Committee

By

Legislative Fiscal Division

February 26, 2010

Legislative Fiscal Division

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MONTANA LEGISLATIVE BRANCH

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Director
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February 26, 2010

Members of the Legislative Finance Committee:

The legislature has provided a statutory requirement that the executive take action to reduce spending in the event of a general fund budget deficit. The executive announced a potential budget deficit on January 8, 2010, and submitted a spending reduction plan to bring the projected ending fund balance above the minimum required by 17-7-140, MCA when using the Governor's Budget Office revenue forecast.

In accordance with 17-7-140, MCA, I submit the Legislative Fiscal Division analysis of the executive spending reduction plan. It is our goal that this analysis will provide the information necessary for committees and legislators to provide an informed input to the current budget situation. This three-part report includes:

Part 1: An overview of the current budget shortfall, including the statutory requirements for dealing with a deficit, the executive projected general fund deficit, the legislative staff projections, reasons for the declining balance, and the executive proposed spending reduction plan.

Part 2: The revenue estimates of the executive and LFD, the underlying economic assumptions, and an explanation of the differences between the executive and legislative estimates. It was presented to the Revenue and Transportation Committee in providing a response to the executive projections.

Part 3: The Budget Director's agency spending reduction recommendations in detail along with the Legislative Fiscal Division's analysis and comments on the various components of the executive reduction plan.

On behalf of the Legislative Fiscal Division, I want to thank the legal staff of the Legislative Services Division for their expert advice and assistance in drafting this document.

Please let me know if there is any further analysis that will be helpful to the committee.

Respectfully submitted,

Amy Carlson
Legislative Fiscal Analyst

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INTRODUCTION

EXECUTIVE SUMMARY

17-7-140, MCA

The Governor is required by statute to implement spending reductions in the event of a deficit in the general fund ending fund balance projection, and must direct sufficient reductions to achieve a required minimum ending fund balance. The Governor's Budget Director submitted a spending reduction plan on February 16, and designated legislative committees are statutorily allowed 20 days to provide comments and recommendations on the proposed plan to the Governor. The Governor can then implement the reduction plan. The Legislative Finance Committee (LFC) will meet on March 4-5, 2010 to evaluate and comment on the executive proposed spending reductions. The Revenue and Transportation Committee met on February 18-19 to comment on the executive revenue estimates used to certify a deficit. The Governor tentatively plans to implement the spending reduction plan after taking into consideration the comments and recommendations of the legislative committees, after March 5.

Budget Shortfall

State general fund revenues have shown continued signs of weakness as compared to the amount utilized by the legislature. Monthly reports since July 2009 issued by the Legislative Fiscal Division (LFD) have shown continuous erosion in general fund revenue collections. The latest report (February 8) discussed an overall revenue reduction of $349.9 million for the 2011 biennium and a preliminary estimate of the ending general fund balance was a negative $62.5 million. This balance is below the statutory trigger point in 17-7-140, MCA ($36.4 million). Individual and corporation income tax collections below the amount utilized by the legislature are the primary reason for the need to implement spending reductions.

The executive projected ending fund balance for the current biennium is $5.6 million. For the purpose of implementing 17-7-140 spending reductions, the executive projection is used. Therefore, the budget shortfall to be addressed by the executive proposal is not as large as legislative analysis shows.

Executive Spending Reduction Plan

The executive spending reduction plan proposes $92.92 million in budget balancers including:

- $40.46 million of agency reductions per MCA 17-7-140,
- $20.96 million of transfers,
- $23.14 million of federal increases in enhanced Medicaid match due to a higher unemployment calculation, and
- $8.36 million of other federal increased Medicaid match costs

The LFD analysis breaks the $40.46 reductions into three groups:

- $38.99 million of agency reductions per MCA 17-7-140,
- $0.65 million in increased general fund revenue resulting from management choices of the executive,
- $0.82 million of reduction changes requiring legislative changes

The detail of why these budget balancers do not fit the definition of 17-7-140, MCA is included in the expenditure analysis section. In addition to the reductions in the executive branch, the Judicial Branch has submitted reductions and the Legislative Branch directors will be submitting plans to their respective administrative committees. This additional savings totals $1.2 million.

The executive's analysis shows an improvement of the projected FY 2011 ending fund balance from $5.59 million to $98.51 million. Applying the executive budget balancers to the LFD projections shows an improvement in ending fund balance from negative $63.035 million to $31.09 million. The revised ending fund balance would be approximately $5.3 million short of the statutory minimum ending fund balance. Therefore, the plan would not achieve the requirements of 17-7-140, MCA when using LFD projections.

The executive plan, when applying the executive's own revenue estimates and other assumptions, provides a viable framework for addressing the shortfall, and provides well above the minimum budget balancers necessary to meet the required minimum ending fund balance, but assumes legislative endorsement of over $22.0 million of reductions in the next session. If actual events mirror the LFD projections, the vulnerability of the plan is clear. The possible need for another round of reductions if the plan is adopted as proposed is significant.

Under the OBPP analysis the plan averages 4.51 percent for state agencies, with reductions of $17.4 million in human services (43 percent of total) and $6.8 million in higher education (17 percent of total). Federal funds would be reduced by nearly $18.0 million due to the loss of match funds. Direct services reductions total $5.8 million. Items requiring legislative action total $22.0 million.

Legislative Options

The consequences of implementation of the executive plan can have a significant impact on legislative budget policy and priorities. The alternative is for the legislature to step in and take action, if there is a feeling that the policies and priorities in the executive plan are unacceptable, or if legislative action is necessary to preserve legislative policy and priorities. In evaluating the executive plan, the committees should consider:

1) Does the plan work?
2) Are policy choices in the executive plan consistent with legislative priorities and intent?
3) How effectively does the plan address Montana's underlying budget problem?

If the legislature were to intervene, it would almost certainly require a special session. Among the options the legislature could consider in addressing the shortfall would be program eliminations, spending suspension or deferrals, fund shifts, program efficiencies, increased fees or taxes, deferring tax incentives, fund balance transfers, and improving tax collections (audits).

2013 Biennium Outlook

The LFD has written a report titled the Preliminary Budget Outlook for the 2013 Biennium. Please see this report for information on how the reductions in the Budget Director's recommendation impact the 2013 budget.

PURPOSE OF REPORT

17-7-140, MCA, provides a procedure to be implemented by the Governor in the event of a general fund budget deficit. In the event of a budget deficit, the Governor is required to reduce spending in an amount sufficient to bring the projected ending fund balance for the year to at least 1 percent of all general fund appropriations for the biennium. On January 8, 2010, the Governor's Budget Director initiated preliminary action to implement spending reductions by requiring agencies to submit proposals for reductions. On February 16, as required by statute, the Budget Director issued a list of budget reduction recommendations both to the Governor and the Legislative Fiscal Analyst. The executive is required to allow the Legislative Finance Committee 20 days to provide a response regarding the proposed reductions before the Governor directs the reductions.

The purpose of this report is to provide the Legislative Finance Committee with an independent analysis and summary of the proposed executive spending reduction plan, as required by 17-7-140, MCA. Part 1 of the report includes an overview of the state fiscal situation and a summary of the executive response. Part 2 of the report provides a summary of the general fund revenue estimates as projected by the executive and by your LFD staff. Part 3 provides a complete listing and description of the executive spending reduction plan by agency, as well as LFD staff analysis, comments, and alternatives to the spending plan. It also discusses options the legislature may have to respond to this situation.

As mentioned throughout this report, there are a number of dynamic economic conditions that may change the final outcome of revenue and budget projections for the 2011 biennium. Of primary concern is the uncertainty of individual and corporation income tax collections, which have shown a significant downward trend. This report will be updated as needed should revenue projections or proposed spending reductions change significantly prior to the Legislative Finance Committee meeting.

17-7-140, MCA

BUDGET DEFICIT UNDER 17-7-140, MCA

The authority to appropriate state funds rests solely with the Montana legislature in accordance with the state constitution. That authority cannot be delegated. However, since the legislature only meets regularly in session for 90 days in a two-year period, the legislature adopted a law to ensure that there is a method to prevent the occurrence of a budget deficit. In the 1993 legislative session, the legislature passed 17-7-140, requiring the Governor to initiate spending reductions if there is a projected budget shortfall that threatens a deficit budget picture.

On January 8, the Governor's Office formally announced concerns about a budget deficit, and initiated proceedings to implement spending reductions in accordance with 17-7-140. The following describes the statutory requirements, projected deficit, reasons for the declining fund balances, and factors that may affect the projected deficits during FY 2011.

Statutory Requirements/Explanation

The requirements, limitations, legislative role, and implementation procedures are described below. The full text of 17-7-140, MCA (Reductions in Spending) is provided in Appendix A of this report.

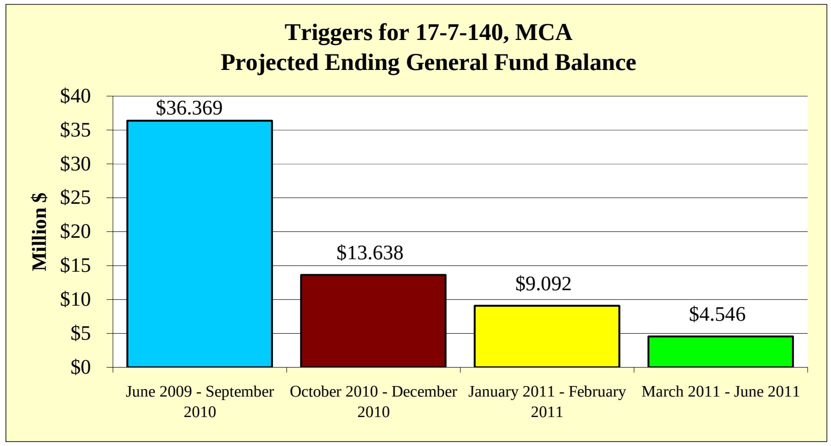
Requirements

Per 17-7-140, MCA, the statutory ending fund balance "floor" is computed to be $36.4 million. As specified in this statute, "the chief budget officer of the state (Governor) shall ensure that the expenditure of appropriations does not exceed available revenue." If the projected general fund deficit (as computed by the executive) falls below the budget "floor", the executive is required to submit proposed spending reductions to the Legislative Finance Committee (LFC) for their review and potential alternative recommendations. After review of all recommendations, the Governor determines the final reductions in agency spending.

Figure 1 shows the phased-in trigger points for the projected general fund budget deficit. The statute was designed to require a lower ending fund balance as the end of the biennium is approached.

The LFD projected balance of negative $62.5 million is $98.9 million below the statutory trigger amount of $36.4 million. However, a projection by the LFD is not required in statute because the projected general fund deficit is determined by the executive. As specified in a January 29 letter to Senator Gillan, chairperson of the Revenue and Transportation Interim Committee (RTIC), the executive has projected a general fund balance of $5.6 million, $30.8 million below the statutory trigger amount. The RTIC met to discuss the general fund revenue estimates on February 18 and the Legislative Finance Committee (LFC) is scheduled to discuss the proposed executive budget reductions on March 4.

Figure 1



The determination of the budget deficit projection, the revenue estimates, and the spending reductions lies entirely with the Governor, with the limitations and legislative input as described in the following two sections.

Limitations

The spending reduction statute (17-7-140, MCA) requires that general fund spending be reduced in order to ensure a minimum ending fund balance reserve, but provides a number of statutory limitations as to what reductions are allowed. The major limitations to the reductions the Governor can make are as follows:

- An agency cannot be required to reduce spending in any program (as defined in the general appropriations act) by more than 10 percent during a biennium.
- Agencies headed by elected officials or the Board of Regents cannot be required to reduce spending by a percentage greater than that required of the total of all other executive branch agencies.
- No reductions can be taken in the following categories:
    - Payment of interest and principal and state debt
    - Legislative and Judicial Branch budgets
    - The school BASE funding program, including special education
    - Salaries of elected officials
    - Montana School for the Deaf and Blind

For FY 2011, the above limitations exclude:

- Significant state general fund expenditures, most notably the K-12 BASE aid and special education program totaling over $500 million
- Statutory appropriations for certain general fund expenditures

Legislative Role

The final assessment of the deficit projection and the required spending reductions are determined by the Governor, but statute requires specific communication with the Legislative Branch and an opportunity for legislative input prior to making the final directive. The Legislative Finance Committee must be afforded the opportunity to comment on planned spending reductions and the RTIC must be afforded the opportunity to comment on the revenue estimates used to determine the deficit. The statutory requirement for legislative interaction and input is summarized as follows:

- The Governor's Budget Director must notify the RTIC of the estimated amount of the general fund revenue shortfall below the revenue estimate established in the revenue estimating resolution for the affected biennium (this occurred January 29).

- The RTIC has 20 days from notification of the revenue shortfall to provide the Budget Director with any recommendations concerning the revenue estimates (this occurred on February 19 with agreement that a deficit has occurred).
- The budget director must consider the recommendations of the RTIC prior to certifying a projected general fund deficit.
- Agencies must submit their assessment of spending reductions to the Legislative Fiscal Analyst (LFA) at the same time they are submitted to the Office of Budget and Program Planning (this submission occurred on January 29).
- The Governor's Budget Director shall provide a copy of his recommendations to the LFA at the same time they are submitted to the Governor (this occurred on February 16).
- The Legislative Finance Committee has 20 days from the time the planned reductions are submitted to the LFA to meet and make recommendations to the Governor (scheduled for March 4-5).
- The LFA must provide a copy of his review of the proposed spending reductions to the budget director at least 5 days before the LFC meeting (scheduled for delivery on February 26).
- The Governor must consider the recommendations of the LFC prior to directing spending reductions.

BUDGET SHORTFALL

PROJECTED GENERAL FUND DEFICIT

Since adjournment of the 2009 legislative session, state general fund revenues have shown continued signs of weakness as compared to the amount utilized by the legislature. In July 2009, the Legislative Fiscal Division (LFD) began to issue monthly reports that provided the legislature with data on general fund revenue monthly collections and other economic information. Each report showed a further erosion in year to date general fund revenue collections. The latest report (February 8) discussed an overall revenue reduction of $349.9 million for the 2011 biennium and a preliminary estimate of the ending general fund balance was a negative $62.5 million. This balance is below the statutory trigger point in 17-7-140, MCA ($36.4 million). Individual and corporation income tax collections below the legislature's estimate are the primary reason for the need to implement spending reductions. These two sources are projected to be $324 million below HJ2 revenue estimates, or 92.6 percent of the total projected reduction in general fund revenues.

This section provides an overview of the projected general fund balance at the end of the 2011 biennium as projected by the legislature at the end of the 2009 session, the LFD projection, and the executive projection included in their spending reduction plan submitted in February. The revised revenue projections from the executive and the LFD are explained in more detail in Part 2 of this report, along with an explanation of differences.

Legislative Projection, 2009 Session

As shown in Figure 2, the 61st Legislature projected a general fund ending fund balance of $282.4 million by June 30, 2011, which represents a reserve of 7.8 percent of general fund revenues for the biennium. The revenue projections adopted in HJ 2 assumed a $195.9 million decline (5.2 percent) from the 2009 biennium anticipated revenues. This decline was based on the continuation of the "Great Recession" until the end of FY 2010 with some improvement by FY 2011. The legislature understood that the revenue outlook was volatile and adopted the fiscal policy to maintain a minimum $250 million ending fund balance in the event of further revenue declines. With a projected balance of $282.4 million, most legislators felt there was an adequate cushion to absorb any additional revenue declines. However, as Figure 2 shows, the LFD and the executive projections have changed significantly from the legislative estimates.

Figure 2

2011 Biennium Differences
61st Legislature, Legislative Fiscal Division, and Executive
Figures in Millions

	Legislature Biennium	LFD Biennium	Executive Biennium	Biennial $ Diff.	Biennial % Diff.
Beginning Fund Balance	**$369.149**	**$391.964**	**$392.530**	**$0.566**	**0.1%**
Revenue					
Revenue Estimates	3,602.264	3,252.416	3,327.350	74.934	2.3%
Total Funds Available	$3,971.413	$3,644.380	$3,719.880	$75.500	2.1%
Disbursements					
General Appropriations	3,193.352	3,212.653	3,216.200	3.547	0.1%
Statutory Appropriations	360.984	360.830	360.150	(0.680)	-0.2%
Transfers	133.304	139.402	139.020	(0.382)	-0.3%
Supplemental Appropriations	-	-	-	-	
Feed Bill	13.398	13.537	9.460	(4.077)	-30.1%
Reversions	(12.040)	(12.298)	(10.540)	1.758	-14.3%
Total Disbursements	$3,688.998	$3,714.124	$3,714.290	$0.166	0.0%
Fund Balance Adjustments	-	6.709	-	(6.709)	-100.0%
Ending Fund Balance	**$282.415**	**($63.035)**	**$5.590**	**$68.625**	**-108.9%**
Executive Proposal					
17-7-140, MCA Spending Reductions	-	(38.989)	(40.460)	(1.471)	
Revenue Transfers	-	(0.653)	-	0.653	
Requiring Legislative Action	-	(21.778)	(20.960)	0.818	
FMAP Tier3 Medicaid Adjustment	-	(23.140)	(23.140)	-	
Federal Clawback	-	(8.363)	(8.363)	-	
Total Executive Proposal	**$0.000**	**($92.923)**	**($92.923)**	**$0.000**	
Legislative Spending Reductions	-	(0.586)	-	0.586	
Judical Spending Reductions	-	(0.619)	-	0.619	
Revised Ending Fund Balance	**$282.415**	**$31.093**	**$98.513**	**$67.420**	

LFD Projection

The economic conditions that have prevailed since late 2008 in the state, nation, and world economies have caused state revenues to plummet from the FY 2008 amounts. As revenues have fallen, the services funded by general fund dollars will need to be reduced to maintain a balanced budget.

General fund revenues declined by 7.5 percent in FY 2009 and are projected to decline an additional 12.0 percent in FY 2010. Such unprecedented back to back declines have not occurred for over four decades. The only period when two consecutive years of declines occurred was in FY 2002 and 2003, but at a modest 0.3 and 1.5 percent, respectively. Declines of this magnitude complicate the accurate prediction of future revenues and hence, complicate the budgeting process.

General fund revenues are expected to increase beginning in FY 2011 but at a more modest rate than observed from FY 2004 through FY 2008. These estimates are based on the IHS economic forecasts received in early February. The economic forecasts as prepared by IHS reflect an economic recovery that will be slow and gradual throughout the forecast period. Based in the current LFD revenue estimates, the general fund balance is projected to be a negative $63.0 million before any spending reduction proposals presented by the executive. It should be noted that two proposals included in the executive plan ("FMAP Tier3 Medicaid Adjustment" and "Federal Clawback") are expected to occur regardless of executive action. These amounts were included in the LFD balance sheet column for comparability with the executive amounts. When the executive spending reduction plan is included in the LFD balance sheet, the revised general fund balance would be $31.09 million or about $5.3 million below the statutory trigger specified in 17-7-140, MCA.

Executive Projection

The Governor's Budget Director submitted a spending reduction plan to the LFD on February 18 that assumed an ending general fund balance projection of a positive $5.6 million. This projected balance was before the implementation of any spending reductions and fund transfers. On February 25, the executive submitted a revised plan based on new information received from the federal government that had a positive impact on the projected ending fund balance. Figure 3 reflects the revised ending fund balance projection by the executive. If the 62nd Legislature adopts the $22.0 million of executive spending reductions that require legislative action, the general fund balance of the executive would be a positive $98.9 million.

Figure 3

Comparison of General Fund Balance Sheet Differences Executive vs. Legislative Fiscal Division In Millions	
	2011 Biennium
Beginning Balance	$0.566
Revenue Estimates	74.934
Disbursements	(0.167)
Fund Balance Adjustments	(6.709)
Total Difference	$68.624

LFD Projection/Differences from Executive Plan

The LFD projected general fund deficit for the 2011 biennium prior to implementation of any spending reductions is a negative $63.0 million. This compares to the executive's projection of a positive $5.6 million. A comparison of the two projections and the difference of $68.6 million are shown in Figure 3. Nearly all of the difference is due to revenue estimates and fund balance adjustments. The executive did not include any prior year adjustments that have occurred subsequent to the issuance of the CAFR (Comprehensive Annual Financial Report). A detailed LFD balance sheet can be viewed on page 10.

Revenue Estimates

The difference between the executive and the LFD general fund revenue estimates for the 2011 biennium is $74.9 million, or 2.3 percent of the total general fund revenue projected by the LFD ($3.3 billion). The LFD reviewed each revenue source in detail and made adjustments based on economic assumptions and year to date collections for FY 2010. The LFD requested the underlying assumptions developed by the executive but the executive has not provided the requested information. Figure 4 shows the primary differences between the two estimates by revenue components that have significant differences. Most of the difference is isolated to individual and corporation income taxes. Both of these revenue sources are highly influenced by estimated payments and refunds that will be processed in the next four months. For example, estimated tax payments are due April 15th and June 15th for both individual and corporation income taxes. These payments will not only impact final collections for FY 2010, but also may affect the outlook for FY 2011.

Figure 4

2011 Biennium Revenue Estimate Differences Executive vs. Legislative Fiscal Division In Millions	
	2011 Biennium
Individual Income Tax	$29.607
Corporation Income Tax	46.178
Vehicle Tax and Fees	13.796
Oil and Gas Production Tax	(14.805)
Remaining Sources	0.158
Total Difference	$74.934

Supplemental Appropriations

For purposes of calculating the general fund budget deficit under 17-7-140, MCA, anticipated supplemental appropriations are not included. Although this statute specifically excludes supplemental appropriations in determining the projected general fund deficit, the potential for supplemental funding exists for corrections, public defender, and public health. Supplemental appropriations will ultimately affect the ending fund balance for the 2011 biennium.

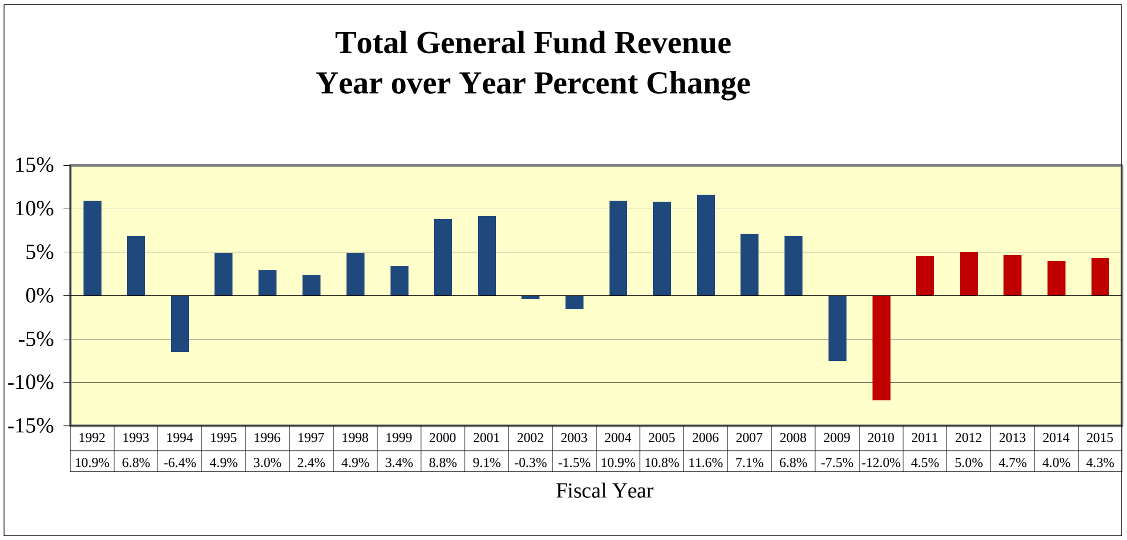
Anticipated Reversions

The LFD reversion estimates have not been adjusted due to the tight budget situation and the proposed spending reductions of the executive. Once the Governor finalizes the spending reductions (after the March 5th Legislative Finance Committee meeting), an adjustment may be necessary to the reversion amount. The executive balance sheet currently shows a reversion amount that is $1.1 million less than the LFD. The executive used a fixed percent of total expenditures to arrive at a reversion amount.

REASONS FOR DECLINING GENERAL FUND BALANCES

As stated major revenue contributors to the state general fund are experiencing significant declines from FY 2008 levels. These declines are expected to continue through FY 2010 before increasing, but will still be below the FY 2008 level by FY 2011. As shown in Figure 5, general fund revenue collections peaked in FY 2008 but have declined significantly in FY 2009 and FY 2010. General fund revenues are expected to begin to recover in FY 2011 but are not expected to reach FY 2008 levels until FY 2015.

Figure 5



The revenue stream for the state has undergone dramatic changes in the past seven months. In general terms, the revenue downturn can be attributed to a significant decline in individual and corporation income taxes. Both of these taxes are extremely sensitive to the state and national economies as well as many world economies. As the Bureau of Business and Economic Research has stated, "there are no sectors of the Montana economy that have not been affected by the Great Recession". In more detailed terms, the causes of the revenue drop-off are due to reduced wage incomes, corporate profits, interest incomes, dividend incomes, and capital gain incomes. Reduced individual and corporate income tax collections comprise about 92.6 percent of the total revenue shortfall. Combined, the individual and corporation income taxes are below FY 2009 amounts by 22.2 and 71.0 percent, respectively.

The decline in general fund revenues below projections is not unique to Montana – many states have had to take action to balance their budgets due to declining revenues. North Dakota is the only state with a projected positive ending fund balance. Montana would be on the positive side of the ledger if all of the spending reductions proposals are implemented. The primary factors contributing to the shortfall are discussed below, along with a comparison to other states.

Capital Gains

Capital gains income represents the net income from the sale of assets such as land and equities. Over a several year period, equity values have risen dramatically, and the state has seen net capital gains income become a significant portion of individual income tax revenues. Since the revenue generated from capital gain realizations was built into the state revenue base, a corresponding increase in the expenditure base also occurred.

With the decline in the equity markets beginning in late 2008, however, there has been a dramatic decline in net capital gains income which results in a reduced individual income tax base. What makes the problem worse is that even with an improved economy, the net capital gains income base is likely to be reduced to a new "benchmark" amount because of the change in real estate values. Since this equates to a reduced tax base, the result will be a lower level of revenues in the future.

Recession

The US economy entered an economic slowdown in late 2008 that has continued until the final quarter of 2009. Several of the state's major industrial facilities have faced a variety of challenges including volatile energy prices, bankruptcy, and/or temporary shutdowns. Montana has not escaped the Great Recession and the impacts on state revenues are significant. Wage growth has been down yet some improvement is expected in the near future. Business, capital gains, and investment incomes are presumed to be stable or declining with not much improvement in the short-term. And while the U.S. recession is unofficially over, the revenue impacts did not begin to show up until the second quarter 2009. This is due to the time lag between the impacts of economic changes and when tax revenues are actually received.

Comparison with other States

With some sign of brightening of the overall economic picture, states continue to struggle with large budget gaps. One significant reason for the gap is reduced tax collections. In a recent quarterly "State Revenue Flash Report" by the Nelson Rockefeller Institute of Government, it was noted that tax collections for the third quarter of 2009 show continued declines in most states for all three major sources of tax revenue (individual income tax, corporation income tax, sales tax), as well as for overall tax collections. However, analysts expect more states to begin to see growth in some revenue sources over the next few months, particularly the sales tax. It was also noted that tax collections are expected to "remain below the prerecession peak for quite some time." As reported in November by the National Conference of State Legislatures (NCSL), with 36 states reporting, almost 58.3 percent expect individual income tax collections to drop when compared to the previous year. Twenty-three states anticipated that corporate income tax collections would drop below last year's levels, with 13 of these forecasting double-digit declines. Lower revenues are the major reason for state budget difficulties, but spending pressures are also contributing to the problem in Montana as in other states. The cost of increasing caseloads as state residents seek out more state services and the need to manage the unfunded liability associated with the state pension funds increase the size of the budget gap in Montana.

FACTORS THAT MAY AFFECT PROJECTED BALANCES

There are other issues with potential impacts that may impact the 2011 biennium general fund balance. These items are explained in the following sections –"potential lawsuits" and "other fund balance issues".

Potential Lawsuits

No potential costs due to current or anticipated lawsuits are included in the 2011 biennium projections. However, three cases with the potential for additional state costs are highlighted below:

- South Pointe –The state is the sole defendant in a lawsuit filed due to the termination of three leases on what would have been the South Pointe subdivision in the Nob Hill area in Helena. The subdivision would have housed a portion of several state agencies. The state is currently in the discovery phase.
- Libby – The state is one of a number of defendants in a lawsuit brought on behalf of current and former residents of Libby for asbestos related damages. There are no current estimates of a resolution date.
- Blanton – A class action lawsuit challenges the right of the Department of Public Health and Human Services to assert a lien on payments from third parties to Medicaid recipients to compensate them for injuries or illness for which the Medicaid program has made payments to medical providers. As of this writing the court has determined that DPHHS must makes refunds, but no final judgment has been made and an appeal may be considered.

Other Fund Balance Issues

Other fund balance issues are areas that could affect the ending fund balance. None of these items affect the long-term budget gap but they could change the ending fund balance for the 2011 biennium.

- Otter Creek Coal leases – the Land Board has reissued a Request for Proposal at a lower bid requirement. If there is a successful bidder, the general fund balance is anticipated to increase by $82 million.

- PPL Inc., River Bed Lease Payments are currently being litigated before the state Supreme Court. If the state is successful in the litigation, the general fund balance will increase by between $18 million and $63 million
- Federal enhanced FMAP (Medicaid match) rate extension:
  - The method by which the federal government implements the enhanced FMAP for the period of July 1 through December 31, 2010 could increase the fund balance by $4.0 to $17.0 million
  - If Congress authorizes the extension of federal enhanced payments for Medicaid in the second half of FY 2011, it will reduce the general fund necessary to fund Medicaid. This extension could increase the general fund balance by up to $40.0 million
- Supplemental appropriations are uncertain at this time and are not included in the balance sheet

DETAILED GENERAL FUND OUTLOOK

Legislative Fiscal Division - General Fund Outlook

Figures in Millions

	Revised FY 2010	Revised FY 2011	2009 Biennium	2011 Biennium	Biennial $ Change
Beginning Fund Balance	$391.964	$138.285	$543.541	$391.964	($151.577)
Revenue					
LFD Revenue Estimate	1,590.833	1,661.583	3,761.508	3,252.416	(509.092)
Total Funds Available	$1,982.797	$1,799.868	$4,305.049	$3,644.380	($660.669)
Disbursements					
General Appropriations - HB2	1,498.930	1,565.832	3,398.123	3,064.762	(333.361)
Stimulus Approps. - HB645	53.069	57.052	-	110.121	110.121
Stimulus Transfers - HB645	79.247	38.209	-	117.456	117.456
Statutory Appropriations	179.451	181.379	422.348	360.830	(61.518)
Transfers	8.924	13.022	273.280	21.946	(251.334)
Other Appropriations	33.864	3.906	-	37.770	37.770
Feed Bill	2.929	10.608	-	13.537	13.537
Reversions	(5.193)	(7.105)	(164.732)	(12.298)	152.434
Total Disbursements	$1,851.221	$1,862.903	$3,929.019	$3,714.124	($214.895)
Fund Balance Adjustments	6.709	-	15.934	6.709	(9.225)
Ending Fund Balance Before Other Issues	$138.285	($63.035)	$391.964	($63.035)	($454.999)
Other Fiscal Issues					
Executive Spending Proposals					
Spending Reductions	11.063	28.706	-	39.769	39.769
Revenue Transfers	0.271	0.417		0.688	0.688
Reductions Requiring Legislation	-	20.960	-	20.960	20.960
Tier 3 FMAP Change	5.316	13.940	-	19.256	19.256
Tier 3 Revenue Change	1.094	2.790	-	3.884	3.884
Total Executive Proposals	$17.744	$66.813	$0.000	$84.557	$84.557
Legislative Spending Proposals	-	0.586	-	0.586	0.586
Judicial Spending Proposals	0.002	0.617	-	0.619	0.619
Federal Clawback	6.331	2.032	-	8.363	8.363
Total Disbursements	$ 1,828.509	$ 1,796.062	$ 3,929.019	$ 3,624.571	$343.822
Ending Fund Balance After Other Issues	$162.362	$31.090	$391.964	$31.090	($360.874)

Other Fund Balance Issues

Supplemental Appropriations
Pending Litigation
Otter Creek Coal Leases
PPL Inc., River Bed Lease Payments
Federal Enhanced FMAP Rate Extension

EXECUTIVE PROPOSED REDUCTION PLAN

OVERVIEW

This section provides a summary evaluation of the executive spending reduction plan and whether it fulfills the statutory objective of achieving the minimum required target ending fund balance. It also provides a summary view of the budget balancers proposed in the executive plan, intended to provide the reader with a general understanding of the major components of the reduction plan. It includes agency expenditure reduction highlights and types of reductions, plus a discussion of some of the impacts of those reductions.

AGENCY REDUCTION PLANS

The Office of Budget and Program Planning (OBPP) is recommending that the Governor require agencies to reduce general fund spending by $40.46 million. This total equates to an average reduction of 1 percent of all general fund subject to appropriation in the 2011 biennium. Voluntary reductions by the Judiciary and the Legislative Branch would voluntarily reduce spending by $1.2. Figure 6 shows each agency's reduction and percentage of the FY 2011 appropriation. Please note that K-12 BASE Aid expenditures are exempted from reductions by statute.

Figure 6

Executive Proposed Spending Reductions By Agency

Agency	Biennium Reduction	Percent Reduction
3101 Governor's Office	(307,102)	-5.00%
3202 Comm Of Political Practices	(23,044)	-5.00%
3501 Office Of Public Instruction	(3,938,206)	-4.54%
4107 Crime Control Division	(119,719)	-5.00%
4110 Department Of Justice	(876,412)	-3.30%
5101 Board Of Public Education	(11,379)	-5.00%
5102 Commissioner Of Higher Education	(6,824,435)	-4.51%
5114 Montana Arts Council	(23,010)	-5.00%
5115 Montana State Library	(138,958)	-5.00%
5117 Montana Historical Society	(136,901)	-5.00%
5301 Department Of Environmental Quality	(369,781)	-6.42%
5401 Department Of Transportation	(260,000)	-10.00%
5603 Department Of Livestock	(69,048)	-5.00%
5706 Dept Of Natural Resources & Conservation	(1,133,834)	-5.00%
5801 Department Of Revenue	(144,926)	-0.28%
6101 Department Of Administration	(251,162)	-3.99%
6108 Office Of The Public Defender	(7,479)	-0.04%
6201 Department Of Agriculture	(67,704)	-5.00%
6401 Department Of Corrections	(6,877,882)	-3.98%
6501 Department Of Commerce	(481,400)	-10.00%
6602 Department Of Labor & Industry	(216,659)	-8.29%
6701 Department Of Military Affairs	(291,258)	-5.00%
6901 Dept Of Public Health & Human Services	(17,198,297)	-4.50%
Grand Total *	($39,768,596)	-4.16%

* Excludes revenue transfers include in the executive plan

CALCULATION OF PERCENT OF REDUCTION

Several executive branch agencies are headed by an elected official. The Montana University System (also part of the executive branch) is governed by the Board of Regents. According to 17-7-140, MCA, the Governor may not reduce the expenditures of an agency or department headed by an elected official or the Board of Regents "…by a percentage greater than the percentage of general fund spending reductions required for the total of all other executive branch agencies."

The calculation of this percentage is not specifically defined in statute, leaving the question of whether the executive has complied with statute open to different interpretations based upon how the calculation is made. There are three separate types of issues:

- How to apply the percentage calculation
- Which general fund appropriations to include
- Which time period to employ

Applying the Percentage Calculation

There are two major ways to make this calculation:

- Non-weighted average – Using the percent reduction imposed on each agency equally applied. For example, if the Department of Revenue with HB 2/HB 13 appropriations of over $50 million in FY

2011 was reduced 5 percent, and the Montana Arts Council with appropriations of less than $0.5 million was reduced 7 percent, the average reduction applied to all agencies would be 6 percent

- Weighted average – Using the total reduction applied to total expenditures. Using the above example, the weighted average would be just over 5 percent

General Fund Expenditures to Include

General fund is appropriated in two primary ways: 1) temporary bills such as HB 2; and 2) statutory appropriations. The legislature also authorizes transfers from and to the general fund that do not require an appropriation. Within temporary appropriations, while HB 2 is by far the largest in most biennia, there are generally other bills that appropriate general fund for various purposes. The situation is complicated in the 2011 biennium due to the appropriation of the federal stimulus in HB 645. When the executive calculated the average reduction, it calculated the reduction compared to HB 2/HB 13 expenditures, even though some of those reductions were to expenditures from statutory and other appropriations bills.

Time Period to Employ

Reduction recommendations were made to both FY 2010 and FY 2011. The reduction calculation was made to FY 2011 appropriations, only.

The executive recommended reductions in spending for non-elected official agencies and the Montana University System include an average of 5.14 percent using a non-weighted average and 4.10 percent using a weighted average. The average calculated by the executive and used for elected officials was 4.51 percent.

How Permanent are the Proposed Reductions?

As stated elsewhere in this report, Montana faces a significant structural imbalance. Indications are also that long-term revenue growth prospects have diminished from the level experienced in prior years. Consequently, the legislature will likely be faced with the prospect of reducing budgets from the level that will be used to establish the 2013 biennium budget base (actual FY 2010 expenditures). In examining the proposed budget reductions, LFD staff also examined whether the reductions would be in FY 2010 expenditures for the purpose of determining the 2013 biennium budget base. Figure 7 provides a detailed listing of those reductions considered on-going in the 2013 biennium. As shown, of the total $40.46 million proposed reduction, $13.0 million (or $26 million over the biennium) can be considered ongoing.

Figure 7
Proposed OBPP Reductions Reducing the FY 2010 Base
2013 Biennium

Section/Agency/Purpose	FY 2010	FY 2011
Section A		
Revenue* - TIF Grants	$515,013	$515,013
COPP - General	469	469
DOLI - Travel	7,589	7,589
Governor - Travel	21,866	21,866
Governor - General	40,369	40,369
Military Affairs - Travel	2,585	2,585
Section B - DPHHS		
HB 645 - 2% Provider Rate**	5,682,335	5,682,335
HB 2 - Assisted Living Rate Incr.**	131,000	131,000
HB 2 - SLTC Waiver**	408,890	408,890
HB 645 - Match for SOCCS Grant**	333,500	333,500
HB 2 - Work Comp MH Institutions	1,275,663	1,275,663
HB 2 - HB 130's Reduction**	309,734	309,734
Prgm 4 - Operating efficiencies	9,302	9,302
Prgm 7 - Fund switch and op exp	25,800	25,800
Prgm 8 - Op efficiencies	10,983	10,983
Pgm 2 - Op efficiencies	61,345	61,345
Pgm 3 - Op efficiencies	56,163	56,163
Pgm 5 - Op efficiencies	119,493	119,492
Pgm 9 - Op efficiencies	67,993	67,993
Pgm 10 - Optimize fed funding	113,491	113,491
Pgm 11 - Op efficiencies	29,211	29,211
Section C		
Agriculture	26,250	26,250
DNRC	21,726	21,727
Section D		
Corrections		
BOPP reduction	5,000	5,000
HR/Training	15,000	15,000
Outside Medical	100,000	100,000
Advisory Councils	8,348	8,348
P&P Leased Vehicle Return	70,000	70,000
MSP Operating Budget	165,000	165,000
NW Prelease	1,226,984	1,226,984
PRC Per Diem Rate Increase	187,147	187,147
Treatment Per Diem Rate Incr	140,036	140,036
MASC per diem rate increase	65,441	65,441
CCA perdiem rate increase	215,348	215,348
Regional Prison per diem rate inc	199,219	199,219
Section E		
MUS - Ed Units	1,339,957	1,339,957
MUS - CCs	113,404	113,404
MAC - Leadership	22,703	22,703
MSL - Op expenses	30,000	30,000
OPI - Facilities and operating exp.	1,650,000	1,650,000
	$13,008,250	$13,008,250

*Recommended reduction is about $44k as remaining amount is in the projected reversions. Total amount available for reduction in future biennia.
**OTO considered current service level

Lack of Authority in 17-7-140, MCA

Legal review has identified several areas where the proposed reduction is outside of the authority granted to the executive under 17-7-140, MCA, some of which necessitate legislative action to complete. Figure 8 lists those reductions by type of issue: 1) those that reduce non-general fund sources; and 2) those that would require a statutory change. Each are briefly discussed in this section and also discussed in the individual agency narratives.

Non-General Fund Sources

A number of recommendations would reduce non-general fund sources in order to add to the fund balance. Review by legislative legal staff has concluded that 17-7-140, MCA specifically authorizes the Governor to reduce general fund spending only. However, it is within the management discretion of the executive to spend less than the appropriation. Therefore, the executive could make these reductions outside of the 17-7-140, MCA framework.

Needs Statutory Change

The executive cannot order reductions that require a statutory change. One proposed reduction would eliminate a rate increase for physicians that legislative legal staff has determined must be made under current law. Therefore, if this reduction is to be made a statutory change is required, and in the absence of a statutory change is subject to legal challenge.

Figure 8
Reductions Outside of 17-7-140, MCA

Agency	Purpose	- Biennial - General Fund	Other Funds
	- Reduces Non-General Fund -		
Administration	Lottery Transfers		$26,903
Revenue	Liquor Transfers		116,523
Justice	Consumer protection fund balance*		320,838
DPHHS	Vacancy savings at Veterans Home		187,767
	- Needs Statutory Change -		
DPHHS	Physicians Rate Freeze**	817,751	

*The entire amount of the proposed reduction is shown. However, only a portion would be generated through a reduction in expenditures, with the remainder from carryforward and ending fund balance.

**Would also reduce federal funds by $2.1 million.

Proposals Outside of 17-7-140 Authority

- Both the Lottery and Liquor Divisions are enterprise accounts that deposit any revenues beyond those expended for operations ("profits") to the general fund. Therefore, any reduction in anticipated expenditures would increase the amount deposited. OBPP recommends that expenditure of enterprise funds appropriated for operations be reduced.
- The ending general fund balance would be enhanced through deposit of fund balance from the Office of Consumer Protection state special revenue fund. A portion of these funds would be generated due to a reduction in expenditures from this fund.
- State special revenue cigarette tax revenue expended by the Montana Veterans Home would be reduced, increasing the amount of cigarette tax deposited to the general fund.
- Statute specifies how Medicaid physician rates must be established using a 3 factor formula that includes a 6 percent increase from the previous year. OBPP is proposing to eliminate the 2nd year increase.

Impacts on Federal Funds

A number of proposals will have a direct impact on the level of federal funds available to the state. The largest amount is in DPHHS, which LFD staff estimate to be around $18 million (the exact figure will depend upon where certain current unspecified reductions are made). All but about $3.3 million of this total, which will be reduced due to efficiencies in drug purchases, are due to program reductions, with about $11.4 million due to elimination of the second year of provider rate increases.

Potential Other Impacts

A number of the proposals could impact other entities, including local governments.

- OBPP recommends a reduction in school facility payments in the Office of Public Instruction greater than the amount OPI projects will be needed to provide 100 percent of qualified expenditures. This would increase the cost at the local level. For a further discussion, see the Office of Public Instruction in Section E of Part 3 of this analysis

- OBPP recommends a reduction in anticipated allocations to the Little Shell Tribe
- Funds for county juvenile detention and for local interoperability projects would be reduced

These and other potential service impacts are discussed in the individual agency narratives.

Reductions to ARRA Funds

Figure 9
Federal Stimulus (HB 645) Funds Reduced
OBPP Recommendations

Section/Agency	Purpose	Amount
Section A		
Admin	Local Gov't Interoperability	$26,903
Section B		
AMDD	HB 130, etc. OTO Reduction	458,228
Various	Provider rate increases	5,609,332
PHSD	HB 173	50,000
TSD	System Efficiencies	50,000
Section C		
DEQ	Open cut and water protection	369,781
DNRC	Administration Reduction	88,528
Total		$6,652,772

Several of the reductions proposed by the executive would be to funds made available to the state through the American Recovery and Reinvestment Act (ARRA) and appropriated by the legislature in HB 645. Of the total $40.46 million in proposed reductions, almost $6.7 million would come from funds appropriated in HB 645. Figure 9 illustrates.

CATEGORIES OF REDUCTIONS

The executive has proposed reductions that fall into a number of categories. In addition, the impacts of these proposed reductions vary, sometimes significantly, from agency to agency. Figure 10 shows the proposed reductions by category. Please note that these categories are as determined by LFD staff and are not precise. They are presented for discussion and illustrative purposes only, and serve to provide a focus for examination and discussion of impacts.

Figure 10
Proposed Reductions by Type
OBPP Recommendation
in Millions

Type of Reduction	Total
Reduction in Services	$5.8
Delay Program/Eliminate Expansions	6.6
Specific Efficiencies	4.6
Reduce/Freeze Provider Rates	7.2
Funding Shifts	2.0
Fund Balance and Carry forward	2.1
General/Unspecified	11.9
Other	0.3
Total	$40.5

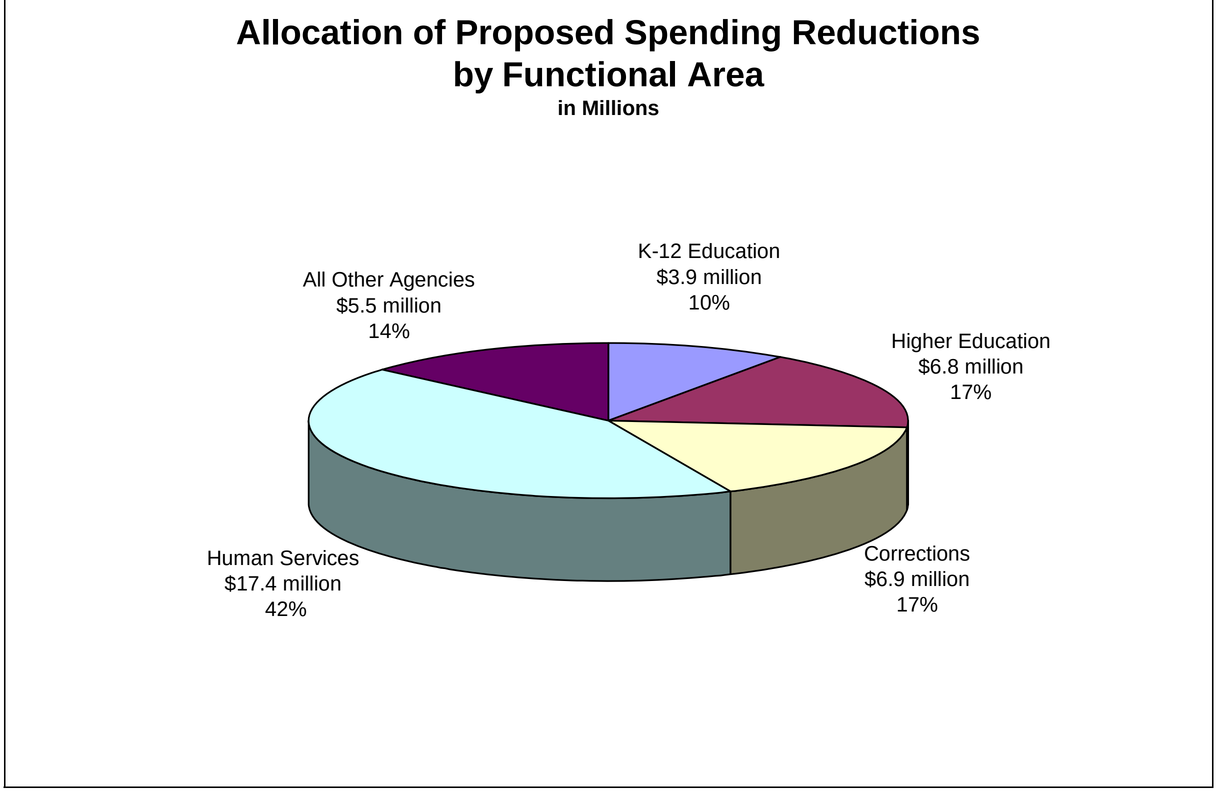
The following highlights some of the major reductions in each category. The list does not include all reductions in each category.

- Reduction in Services – School facility payments (which will also switch costs to local school districts), various proposals in DPHHS, and reductions in the Elkhorn meth treatment contract and juvenile delinquency incentive program funds in the Department of Corrections.
- Delay New Programs/Eliminate Expansions - Northwest Pre-release Center in the Department of Corrections, various programs in DPHHS including capping waiver programs and the Big Sky Rx program, reduction of the grant to the Little Shell Tribe in the Department of Commerce, and reduction of the meth watch grants in the Department of Justice.
- Specific Efficiencies – Multiple source drugs and a workers compensation mistake correction in DPHHS, various specific reductions in the Department of Corrections, including outside medical, and permit writers in the Department of Environmental Quality.
- Reduce/Freeze Provider Rates – All reductions are in DPHHS and the Department of Corrections for various Medicaid and correctional service provider (including regional jail) rates in FY 2011.
- Funding Shifts – Various fees collected in the Department of Corrections.
- Fund Balance and Carry forward – Various agencies, including deposits of fund balances, reduction of other funds to increase funds deposited to the general fund, and other adjustments. About $0.7 million of the fund balance enhancements are reductions in non-general fund.

PROPOSED REDUCTIONS BY FUNCTIONAL AREA

The following figure shows the allocation of the proposed reductions by functional area of state government. As shown, human services (DPHHS) is over 42 percent of the total reductions. K-12 education is less than 10 percent because BASE Aid is exempted from any spending reductions.

Figure 11



LEGISLATIVE OPTIONS

The executive has projected a general fund deficit as defined in 17-7-140, MCA and is required by statute to implement a plan to bring the general fund back in balance with a statutorily mandated minimum reserve. The executive has submitted a spending reduction plan and is statutorily required to allow for comment and recommendations from the Legislative Finance Committee on the spending reduction plan and from the Revenue and Transportation Committee on the revenue estimates used to project the general fund deficit.

The committee input to this process is clearly an advisory role, yet implementation of the executive plan can have a significant impact on legislative budget policy and priorities. The legislature has statutorily designated the two committees to be the spokesperson for the legislature in providing input to this significant policy and priority altering process, and it is the single opportunity for legislative influence in this process. The alternative is for the legislature to step in and take other action. The legislature needs to consider whether the policies and priorities in the executive plan are acceptable, or whether legislative action is necessary to preserve legislative policy and priorities.

This section is divided into two parts: 1) issues and considerations for the committees in evaluating the executive plan; and 2) options the legislature has to consider alternatives to implementing executive spending reductions. In either case, the principles suggested below for evaluating budget prioritization plans would be interchangeable regardless of which option is undertaken. As appropriate, agency discussions made to specific options by the LFD analyst for legislative consideration.

LEGISLATIVE EVALUATION OF EXECUTIVE PLAN

In evaluating the executive spending reduction plan, the committees may find it helpful to focus on three general questions:

4) Does the plan work?
5) Are the policy choices in the executive plan consistent with the priorities of the legislature?
6) How effectively does the plan address Montana's underlying budget problem?

Does the Plan Work?

This question addresses whether the executive plan adequately assesses the economic conditions in setting the revenue projections used to establish a shortfall, provides realistic budget balancing solutions, and is effective in resolving the problem. This is a difficult question to answer since separate committees are evaluating the two sides of the budget equation, yet a coordinated response is critical.

As discussed in our analysis of the executive plan on page 2, it is the assessment of LFD staff that the plan provides a basic framework for addressing the budget shortfall. And in general, the budget balancers recommended by the executive appear workable using the revenue estimates prepared by the executive. The plan, however, does not work if the revenue estimates prepared by the LFD are used. Staff has raised issues with some of the proposed reductions, and has pointed out that some of the proposals will require legislative concurrence in the form of a law change in order to be implemented. The plan is vulnerable in that it assumes a more optimistic revenue outlook for FY 2010 and FY 2011. Further erosion in general fund revenues could drop the ending fund balance below the required minimum. Additional budget balancers would be necessary to reach the required ending fund balance if the issues raised on revenue estimates and the viability of some planned budget balancers create a gap.

Are Policy Choices in the Executive Plan Consistent with Legislative Priorities?

The executive plan addresses the Budget Director's priorities for addressing a budget shortfall, and the question that needs to be addressed is whether the priorities and policies in the plan match up with legislative priorities and intent. This would include an assessment as to whether the plan is properly prioritized in terms of the impacts of spending reductions versus revenue solutions (however, the executive is clearly limited in the ability to use revenue solutions as part of the plan). It would also include an assessment of the specific solutions in the plan, the relative impact on government services, and how they are distributed among various categories of services. For example, the executive plan assesses 42 percent of the spending reductions to human services, 17 percent to higher education, 17 percent to corrections, and 14 percent to other government activities. The committee needs to assess if this is a reasonable distribution of reductions with the least impact on government services.

How Effectively Does the Plan Address Montana's Underlying Budget Problem?

The LFD staff has reported previously that the state faces not only a significant 2011 biennium shortfall, but that there is a longer-term structural imbalance between ongoing revenues and expenditures. Although the executive spending plan focused on addressing the current biennium budget shortfall, some of the reductions provide a permanent reduction that will help address the out-year problem. While providing a partial solution to the longer term budget gap, the executive approach was to concentrate on the immediate shortfall as required by statute, and defer permanent actions on long-term issues until a better assessment of the economic recovery can be determined.

LEGISLATIVE ALTERNATIVES TO EXECUTIVE PLAN

As discussed previously, the legislature established a statute to both require and allow the Governor to ensure the state budget remains balanced. When a shortfall requires a reprioritization of legislative budget policy in the form of budget reductions, the legislature needs to assess whether an executive plan reasonably addresses legislative priorities/intent, or whether the magnitude and priorities of the budget balancing measures simply compels legislative intervention to fulfill the legislature's role of setting budgets and budget priorities. This is a legislative prerogative. The purpose of this section is to address options the legislature has for legislative action to address a budget crisis should it be deemed imperative.

Budget Balancing Options

The following discussion lists different broad categories of spending, revenue, and hybrid options that could be considered to address budget prioritization, in particular a budget shortfall. Example options are for each broad category. Options already included in the executive plan are excluded from this list. This represents a "shopping list" of various options for committee consideration. The list is intended only as a starting point to address legislative prerogatives. It is not intended to be all encompassing, nor does it in any way represent staff recommendations. Broad categories of budget balancing options are presented, and specific options are provided only as examples for discussion purposes. Staff has not analyzed the merits/feasibility of these proposals. It should be noted that these options may also be viable in providing alternative recommendations to the executive in evaluating their plan, although legislative action would ultimately be required in nearly all cases.

Program Eliminations/Modifications

The focus should be on reviewing whether programs still serve a clear purpose, achieve their objectives, are cost effective, or are providing duplicative services.

- Non-statutory or Elective Programs
- Review all General Fund Statutory Appropriations and Transfers
- Review all Revenue Allocations or Diversions

Suspension of Cost of Living/Inflations Increases

- Employee benefit increase
- Provider Rate Increases
- Inflation Rate Adjustments in Budget Process
- Inflation Rate on Distributions to Local Government through the entitlement share
- Inflation Rate on school district BASE Aid

Spending Deferrals

- Postpone Some or all Capital Projects
- Postpone Some or all Economic Development Programs
- Statewide Hiring Freeze
- Statewide Work Furlough
- Travel, Equipment, Subscriptions, Etc.

Funding Shifts

This option would include funding shifts from the general fund to other sources such as fees, federal/local governments, or the private sector.

- Reduced State Contributions for Employee Health Benefits
- Reduce State Support for Higher Education/Shift to Student Tuition or Other University Funds
- Divert Cash Flows from Coal Tax Trust/Subtrusts

Program Improvements/Efficiencies/Economy

This option includes seeking ways to provide the same services at lower cost, economies of scale, improved coordination, and prioritization.

- Consolidate Programs
- Consolidate Economic Development Activities
- Agency Restructuring/Consolidation
- Consolidate School Districts
- Statewide Employee Reductions
- Change Laws Requiring Incarceration
- Debt Refinancing
- Explore Privatization Efficiencies
- Increase virtualization of servers in information technology

Tax Expenditures

This option involves examining whether tax deductions/incentives achieve their objectives/effectiveness.

- Eliminate or Adjust Deductions For Federal Taxes Paid on State Income Taxes
- Eliminate Tax Credits/Exemptions
- Eliminate Previously Enacted Tax Deductions/Incentives

Increase Fees

- Charge Interest on General Fund Loans within the State Treasury
- Increase Gambling Control Permit Fees
- Increase Child Support Enforcement Fees
- Increase Motor Vehicle Fees

Broadening Tax Bases/Raising Tax Rates

- Adopt Gross Proceeds Tax on Health Care Providers
- Increase Selected Taxes
- Restructure Tax Base
- Sales Tax

Temporary Revenue Enhancements

- Surtaxes

Fund Balance Transfers

- Transfer Funds from Tobacco Trust Fund (with some restrictions, must be used for healthcare-related expenditures)
- Transfer Funds From Trust Accounts
- General De-earmarking /Transfer of Fund Balances

Improved Tax Compliance/Collections

- Increase Audit Activity on Non-compliant Taxpayers

Asset Sales

- Sale of Future Revenue Streams
- Sale of State Lands that are not in trusts

APPENDIX

Appendix A

17-7-140. Reduction in spending. (1) (a) As the chief budget officer of the state, the governor shall ensure that the expenditure of appropriations does not exceed available revenue. Except as provided in subsection (2), in the event of a projected general fund budget deficit, the governor, taking into account the criteria provided in subsection (1)(b), shall direct agencies to reduce spending in an amount that ensures that the projected ending general fund balance for the biennium will be at least 1% of all general fund appropriations during the biennium. An agency may not be required to reduce general fund spending for any program, as defined in each general appropriations act, by more than 10% during a biennium. Departments or agencies headed by elected officials or the board of regents may not be required to reduce general fund spending by a percentage greater than the percentage of general fund spending reductions required for the total of all other executive branch agencies. The legislature may exempt from a reduction an appropriation item within a program or may direct that the appropriation item may not be reduced by more than 10%.

(b) The governor shall direct agencies to manage their budgets in order to reduce general fund expenditures. Prior to directing agencies to reduce spending as provided in subsection (1)(a), the governor shall direct each agency to analyze the nature of each program that receives a general fund appropriation to determine whether the program is mandatory or permissive and to analyze the impact of the proposed reduction in spending on the purpose of the program. An agency shall submit its analysis to the office of budget and program planning and shall at the same time provide a copy of the analysis to the legislative fiscal analyst. The office of budget and program planning shall review each agency's analysis, and the budget director shall submit to the governor a copy of the office of budget and program planning's recommendations for reductions in spending. The budget director shall provide a copy of the recommendations to the legislative fiscal analyst at the time that the recommendations are submitted to the governor and shall provide the legislative fiscal analyst with any proposed changes to the recommendations. The legislative finance committee shall meet within 20 days of the date that the proposed changes to the recommendations for reductions in spending are provided to the legislative fiscal analyst. The legislative fiscal analyst shall provide a copy of the legislative fiscal analyst's review of the proposed reductions in spending to the budget director at least 5 days before the meeting of the legislative finance committee. The committee may make recommendations concerning the proposed reductions in spending. The governor shall consider each agency's analysis and the recommendations of the office of budget and program planning and the legislative finance committee in determining the agency's reduction in spending. Reductions in spending must be designed to have the least adverse impact on the provision of services determined to be most integral to the discharge of the agency's statutory responsibilities.

(2) Reductions in spending for the following may not be directed by the governor:

(a) payment of interest and principal on state debt;

(b) the legislative branch;

(c) the judicial branch;

(d) the school BASE funding program, including special education;

(e) salaries of elected officials during their terms of office; and

(f) the Montana school for the deaf and blind.

(3) (a) As used in this section, "projected general fund budget deficit" means an amount, certified by the budget director to the governor, by which the projected ending general fund balance for the biennium is less than:

(i) 2% of the general fund appropriations for the second fiscal year of the biennium prior to October of the year preceding a legislative session;

(ii) 3/4 of 1% in October of the year preceding a legislative session;

(iii) 1/2 of 1% in January of the year in which a legislative session is convened; and

(iv) 1/4 of 1% in March of the year in which a legislative session is convened.

(b) In determining the amount of the projected general fund budget deficit, the budget director shall take into account revenue, established levels of appropriation, anticipated supplemental appropriations for school equalization aid, and anticipated reversions.

(4) If the budget director determines that an amount of actual or projected receipts will result in an amount less than the amount projected to be received in the revenue estimate established pursuant to 5-5-227, the budget director shall notify the revenue and transportation interim committee of the estimated amount. Within 20 days of notification, the revenue and transportation interim committee shall provide the budget director with any recommendations concerning the amount. The budget director shall consider any recommendations of the revenue and transportation interim committee prior to certifying a projected general fund budget deficit to the governor.