

# 2013 BIENNIUM BUDGET

Legislative Fiscal Division

# Nationwide States Are Struggling

## □ **Meredith Whitney on ‘The Largest Threat to the U.S. Economy’**

▣ By Matt Phillips, Wall Street Journal December 20th

▣ Meredith Whitney sat down with Steve Kroft on “60 Minutes” last night to rehash [her well-known views](#) about the threat the finances of states and localities pose for the economy. “It has tentacles as wide as anything I’ve seen. I think next to housing this is the single most important issue in the United States and certainly the largest threat to the U.S. economy,” she says

## □ **Meredith Whitney: ‘States Represent the New Systemic Risk’**

▣ By Matt Phillips, Wall Street Journal September 28th

▣ Yep. She’s at it again. This time influential Wall Street analyst Meredith Whitney is training her balance-sheet-picking-prowess on U.S. states and municipalities.

# Montana is **NOT** California, Illinois, New Jersey, New York, Arizona

## Montana

- ❑ Has not sold state assets to fund operating budget
- ❑ Does not, nor does our constitution allow an operating budget funded with debt
- ❑ Continues to maintain a healthy cash balance in our “checking account”
- ❑ No risk that Montana will default on debt in 2011

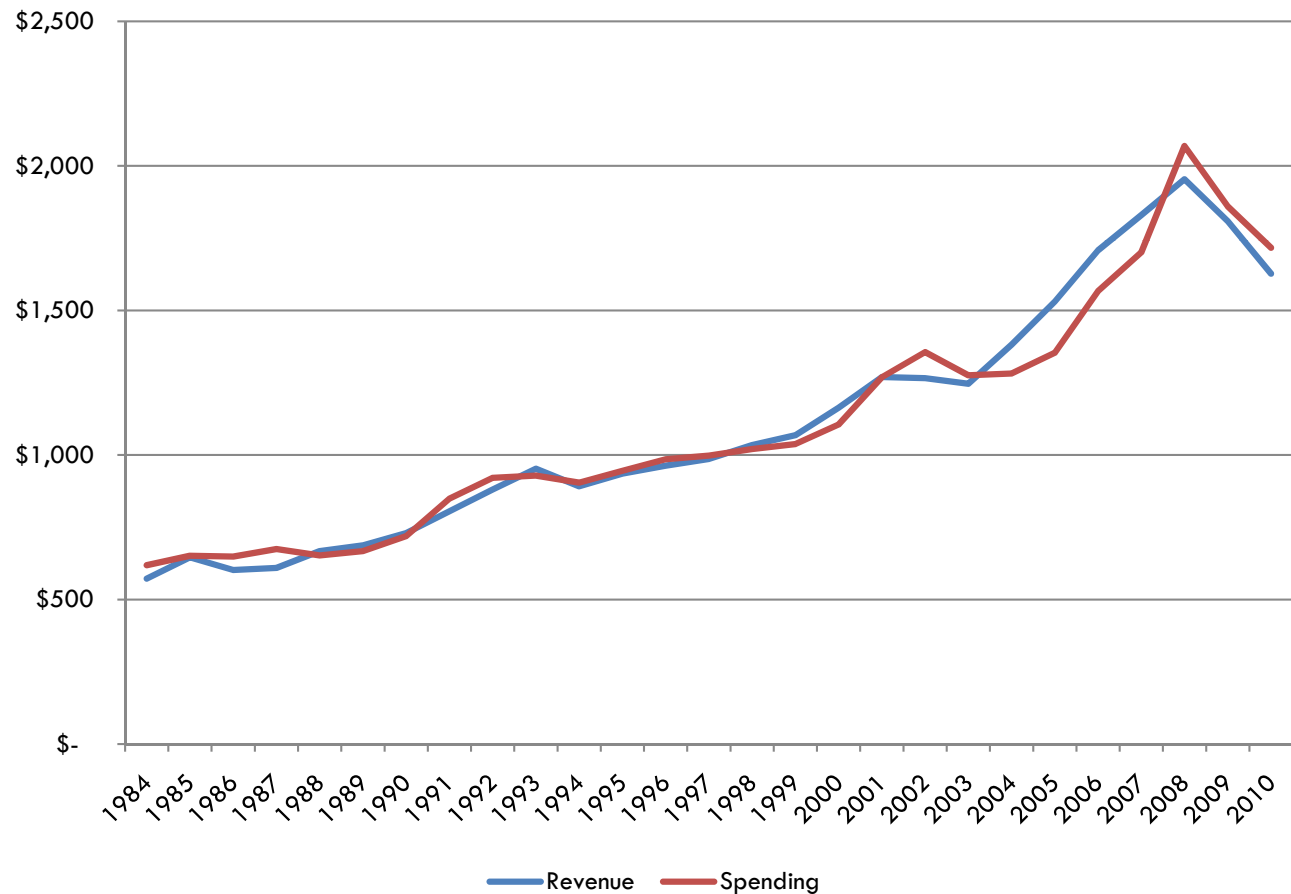
# Yet Montana Has Not Fully Escaped



- With the 2008 stock market fall, the retirement systems are not funded actuarially (i.e. unless something changes, likely to go broke some day)
- Revenues are 17% below the peak year of FY 2008
- Spending for current services exceeds the anticipated revenue in the next two years by about 10%

# General Fund Revenue and Spending

Overtime  
Revenues =  
Expenditures

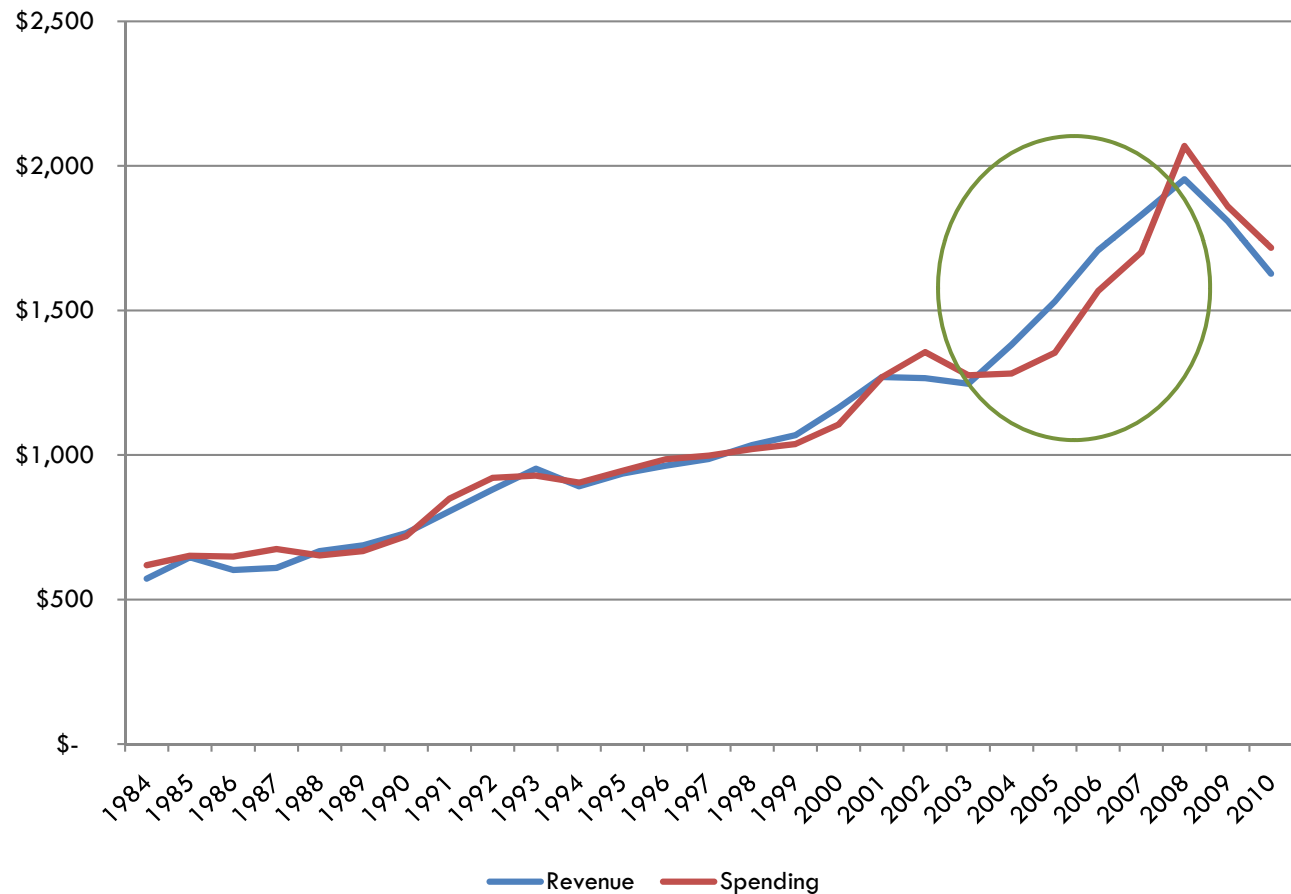


# General Fund Revenue and Spending

Revenues grew tremendously during the nation's housing bubble.

Revenues were underestimated during this period.

Ending fund balance grew.

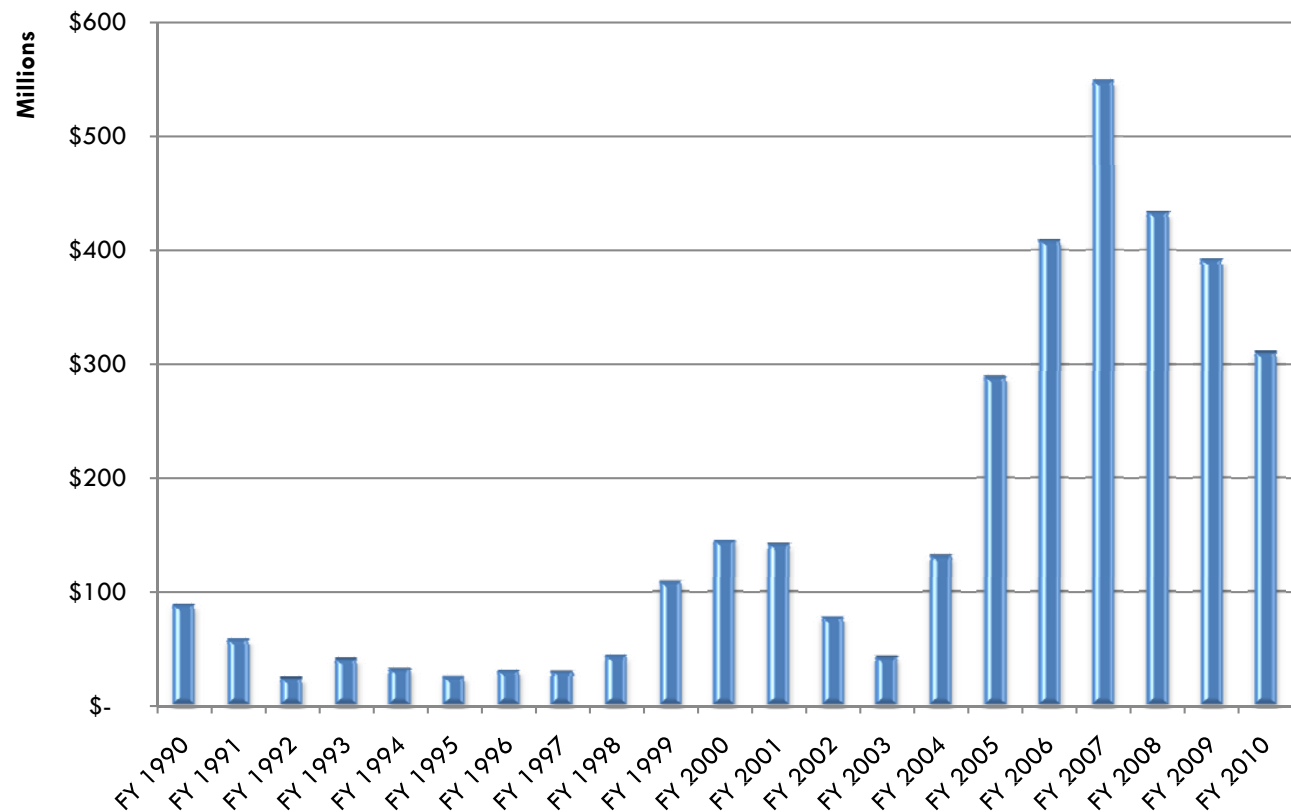


# Ending General Fund Balance

From FY 2004 to FY 2007 General Fund Balance grew to be in excess of \$500 million.

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**Ending General Fund Balance**



# Decline in Ending Fund Balance?



- Intentional: Legislature Chose to Invest in Montana through infrastructure and other investments
- Revenues less than estimate
  - ▣ Offset



# Montana Worked Hard + Got Lucky

Midsession forecast at -\$63 million

<i>Item</i>	<i>Amount (in millions)</i>
MCA 17-7-140 spending reductions of all three branches	\$41.0
Federal - Tier 3 FMAP	19.3
Federal - Tier 3 FMAP application to “claw back”	8.4
Federal - Enhanced FMAP extension to June 30, 2011	25.0
Federal - Additional Education ARRA (stimulus)	30.7
Otter Creek coal bonus payment	81.5
FY 2010 revenue higher than February estimate	34.9
FY 2011 revenue current estimate higher than February	10.5
Fund balance, prior year adjustments, and other	(9.0)
Supplemental Appropriations	(2.9)
Transfers proposed by the Executive	23.8
<b>Total</b>	<b>\$263.2</b>

# HJ2 General Fund Forecast

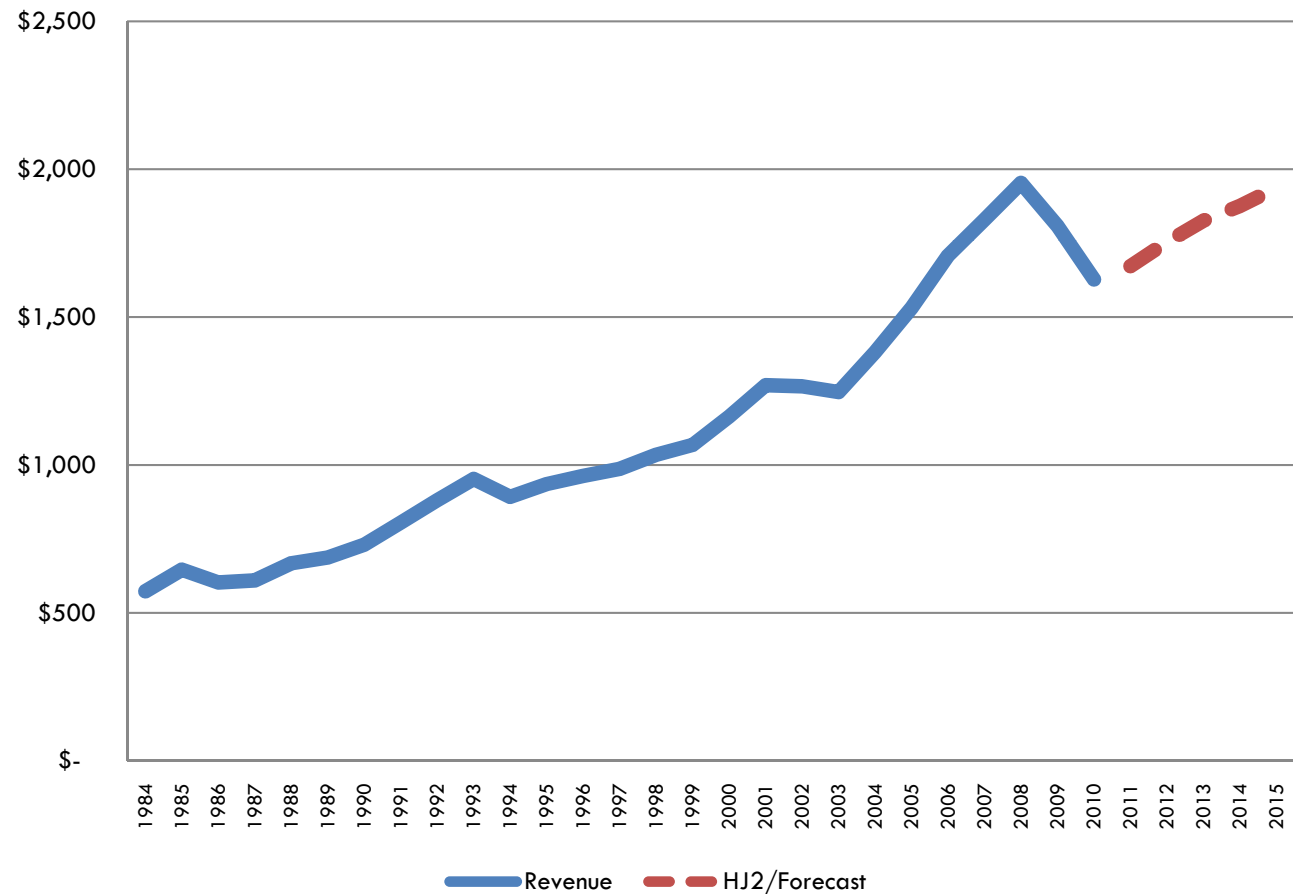
## Growth Forecast

FY 2011  
2.8%

FY 2012  
4.9%

FY 2013  
4.1%

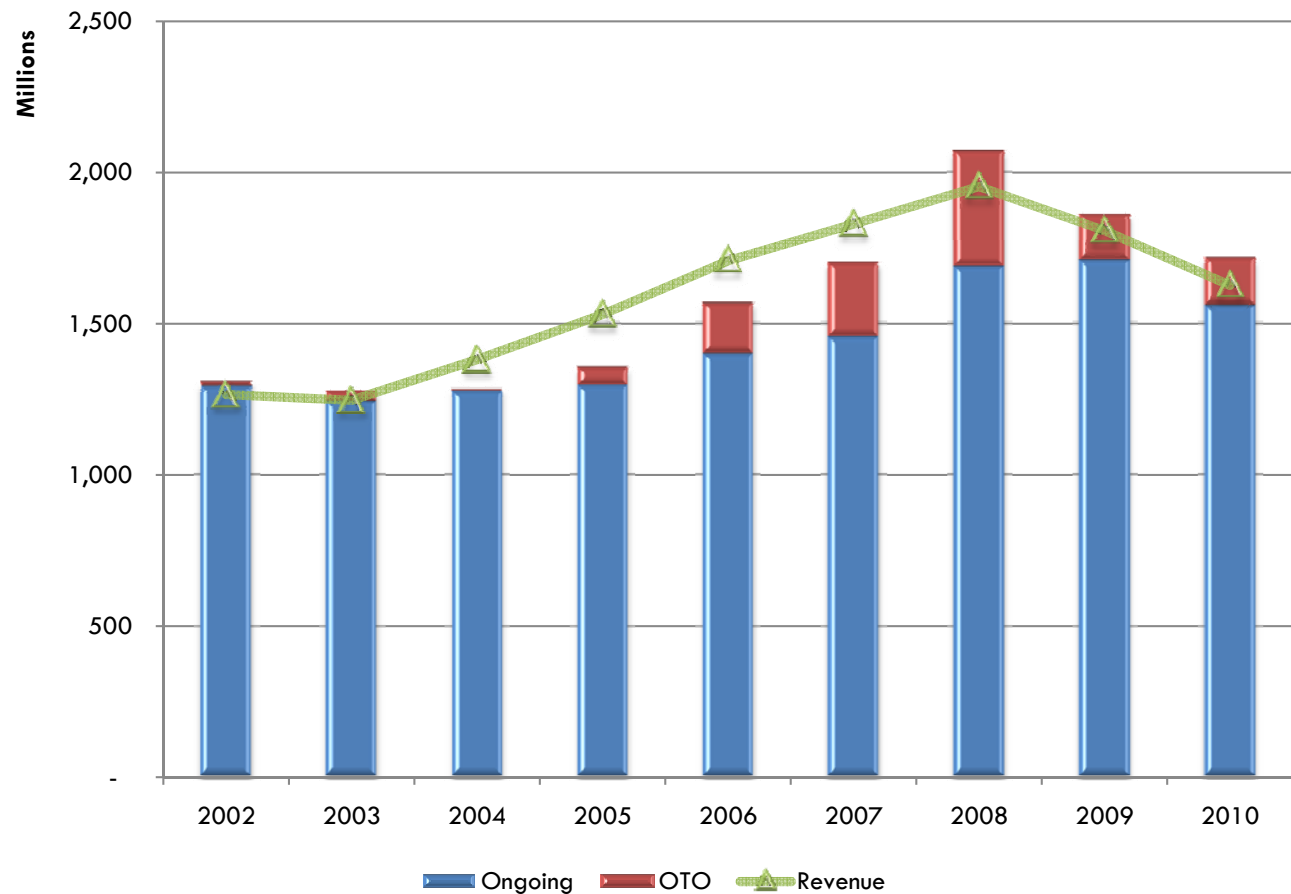
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# General Fund Spending: One-time / Ongoing

Spending increased with revenue, but significant portions of the increase were one-time only.

Yet, current service level is above the current level of revenue.



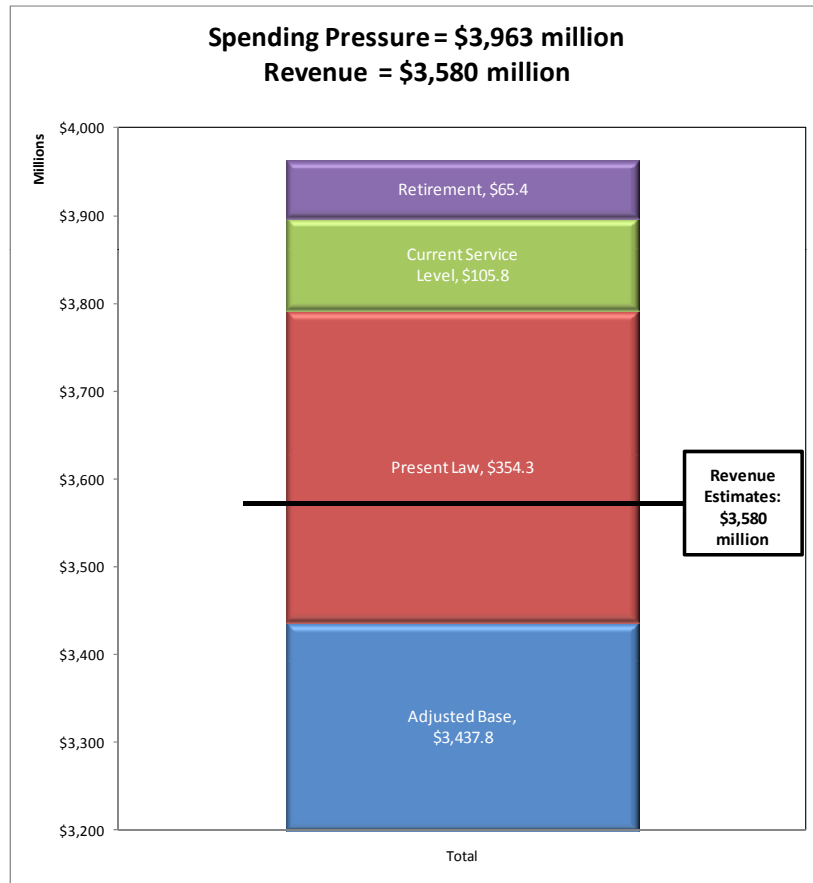


# Spending Pressure Gap

Analysis began March 2010

Third update

# Spending Pressure Gap



- Actuarially funding retirement systems
- Current level of services not considered ongoing
- Present level of services authorized by the previous legislature
- Adjusted Base – including statutory appropriations
- HJ2 Revenues



# Legislative Finance Committee

Rep. Llew Jones (Chair)

Sen. Carol Williams  
(Vice Chair)

Rep. Bill Glaser

Sen. Keith Bales

Rep. Cynthia Hiner

Sen. Steve Gallus

Rep. Galen Hollenbaugh

Sen. Dave Lewis

Rep. Jon Sesso

Sen. Rick Ripley

Rep. Janna Taylor

Sen. Dave Wanzenried

# LFC Preparation: Page 7



- Adopt the 5% plans
- Reference Book
  - ▣ Interim Committee Connections
  - ▣ Hearings over the summer

# What are the 5% Plans?

(3) Subject to subsections (7) and (8), the agency budget request must set forth a balanced financial plan for the agency completing the forms for each fiscal year of the ensuing biennium. The plan must consist of:

...

(f) for agencies with more than 20 FTE, a plan to reduce the proposed base budget for the general appropriations act and the proposed state pay plan to 95% of the current base budget or lower if directed by the budget director. Each agency plan must include base budget reductions that reflect the required percentage reduction by fund type for the general fund and state special revenue fund types. Exempt from the calculations of the 5% target amounts are legislative audit costs, administratively attached entities that hire their own staff under [2-15-121](#), and state special revenue accounts that do not transfer their investment earnings or fund balances to the general fund. The plan must include:

(i) a prioritized list of services that would be eliminated or reduced;

(ii) for each service included in the prioritized list, the savings that would result from the elimination or reduction; and

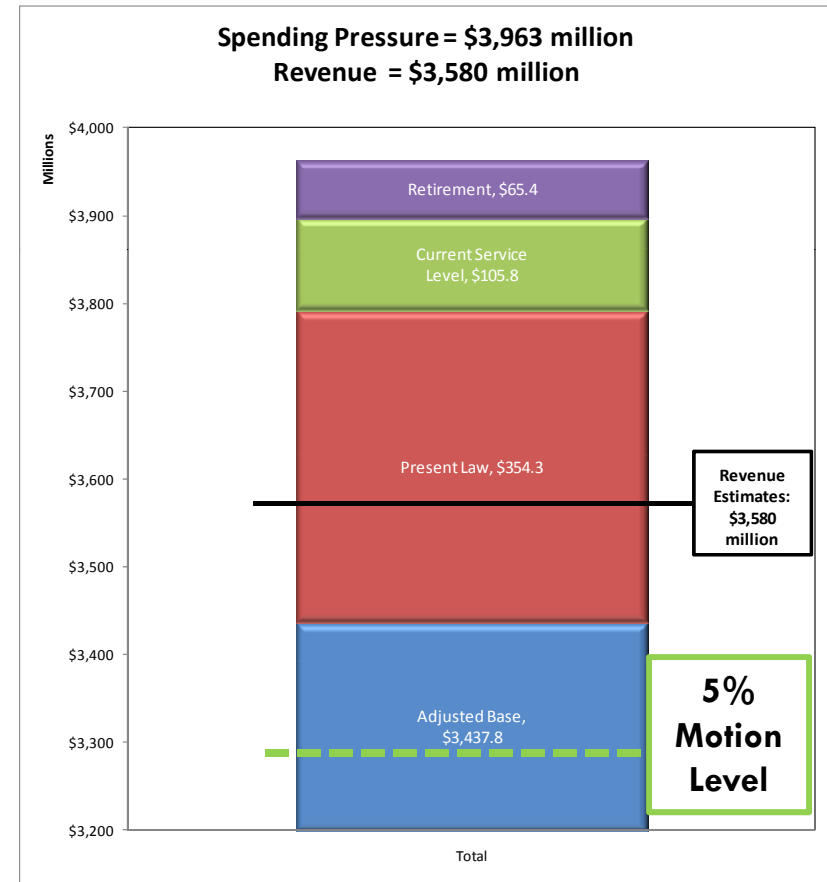
(iii) the consequences or impacts of the proposed elimination or reduction of each service.

- ❑ 5% plans are required by MCA 17-7-111(3)(f).
- ❑ The plans are submitted by the executive as a requirement of the budget submission
- ❑ DPs to reduce base by 5%



# Implementing the 5% Plan Motion

- This starting point is \$293 million below the HJ2 anticipated revenue level.
- Contains specific items outlined by the executive.
- Allow positive motions to increase budget from this level.



# Reference Book – LFC Work



- Legislative Fiscal Division developed initial items
- Work groups of legislators reviewed the items
  - ▣ Legislative Finance Committee members
  - ▣ Interim Committees
- Legislative Finance Committee members visited other interim committee meetings for feedback

# Remember



- ❑ Reductions are from Current Service Level: not the Governor's Budget
- ❑ Available on LFD website
- ❑ Joint subcommittee binders

# Reference Book Examples



- State Special Funds in general and specific
  - ▣ Fund balance transfers
  - ▣ Changes in allocations of revenue streams
- Specific to an agency
  - ▣ Discontinue K-12 schools 2% increase, At Risk, and Special Education MOE
  - ▣ Reduce General Fund Spending beyond Maintenance of Effort in some HCSD Programs (Department of Health and Human Services)

# Leadership Follow Up



- ☐ Statutory Appropriations
- ☐ Allocations of Revenue to State Special Funds
- ☐ Tax Credits

# Statutory Appropriations



- ❑ Statutory Appropriations are appropriations authorized by the legislature to be established each biennium without additional legislative action.
- ❑ Each legislature does not consider these appropriations as it considers spending in the general appropriations bill: HB 2.
- ❑ Examples:
  - ▣ Entitlement Share
  - ▣ Retirement payments on behalf of local government

# State Special Funds



- ❑ State special accounts are state funds designated in statute for specific purposes.
- ❑ In FY 2010, 44% of state funds were categorized as state special.
- ❑ State special funds have grown an average of 8.9% over the past 8 years.

# Tax Credits



- Tax Credits can be considered spending tax dollars to give incentives for certain private action.
  - ▣ Weatherization and energy efficiency
- Others rebate taxes for certain items
  - ▣ Capital gains
  - ▣ Elderly home owner tax credit



# Summary of Choices



- ☐ Ending fund balance
- ☐ Transfers from state special
- ☐ Retirement \$65.4 million
- ☐ Current Service Level \$105.8 million
- ☐ 4% Personal Services Reductions \$15.7 million
- ☐ 5% Plans \$96 million
- ☐ Reference Book
- ☐ Statutory Appropriations
- ☐ State Special Accounts
- ☐ Tax Credits



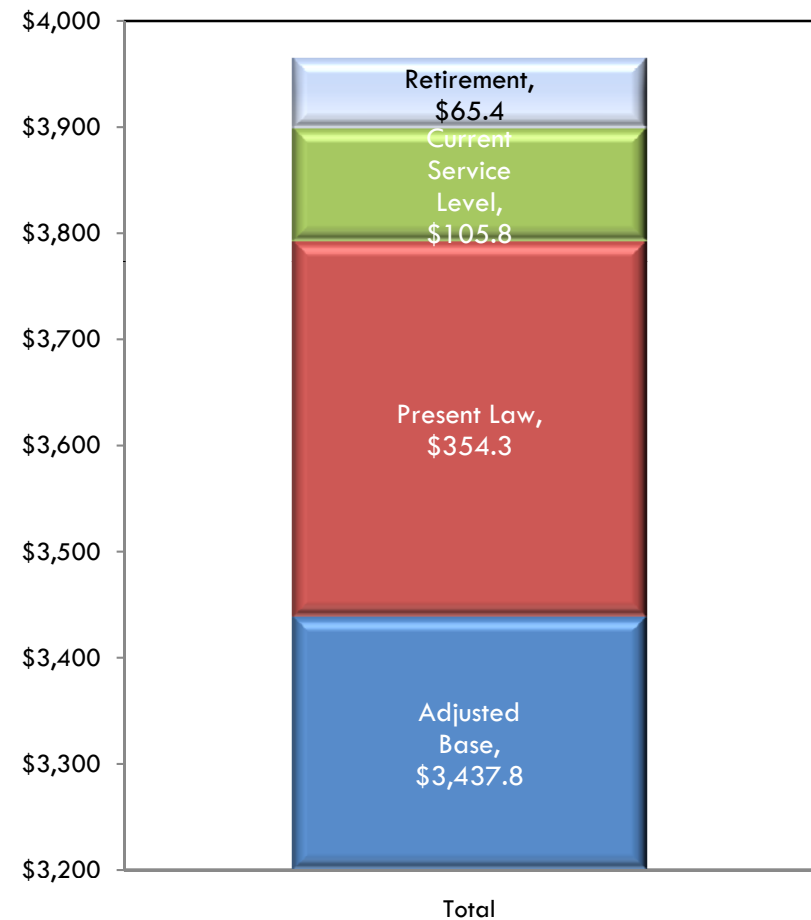
# Governor's Budget

Governor's recommended budget choices for  
closing the Budget Gap in the 2013 biennium

Beginning on page 10

# Retirement Systems

- ❑ Does not recommend addressing the retirement system actuarial funding issues this biennium
- ❑ Delaying addressing this issue compounds the problem



# Current Service Level & Present Law

Current Service Level and Present Law are difficult to distinguish at times in the Governor's budget so they are grouped.

- ☐ Shift spending to state special revenue funds
- ☐ Reduce Present Law Costs
- ☐ Reduce Current Service Level Costs

# Shifting Costs to State Special



- 90% of the local school district oil and gas revenues pay for the quality educator component of the school funding formula or \$72.9 million
- School facilities fund for state share of school debt service or \$17.2 million

# Current Service Level Reductions



- K-12 education: 2% inflation amounts \$22.7 million
- Economic development Department of Commerce: \$1.8 million reduction by not fully reinstating
- DPHHS 2% Provider Rates and direct care worker increases \$26.0 million

# Statutory: Present Law Reductions



- ❑ Optional Retirement Program (ORP) savings of \$1.1 million reduction
- ❑ Entitlement Share: \$10.5 million reduction in the statutory inflation rate to counties and cities

# HB 2: Present Law Reductions



- Selective 4% FTE reduction in general fund personal services or \$15.7 million;
  - ▣ Note that this 4% reduction is 1% greater than the additional 3% vacancy savings imposed last biennium on agencies, and applied only to general fund
- The proposal does not include updated school funding costs of \$15.0 million in the 2013 biennium



# Revenue and Transfers



- The Governor recommends using revenue estimates \$104.3 million higher than HJ2 (\$104.3 million is over two years, \$164 million over 3 years)
- The Governor recommends transferring \$71.4 million of state special fund balances to the general fund
  - ▣ Fires
  - ▣ School Facilities
  - ▣ Treasure State Endowment

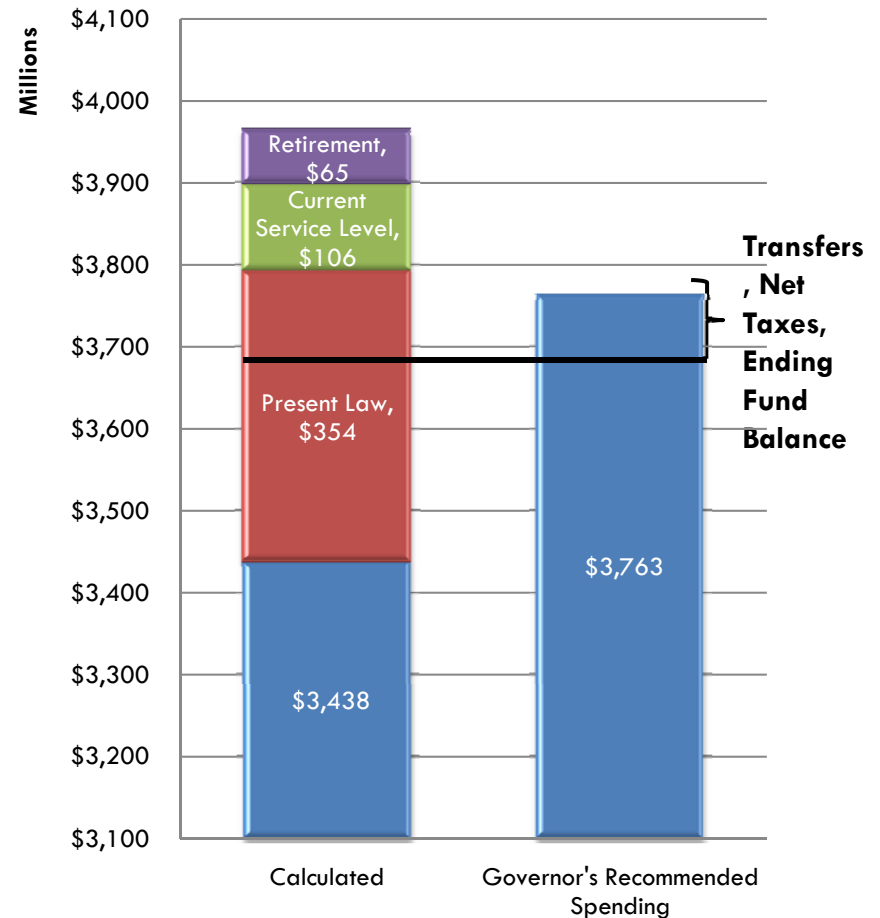
# Other Recommendations



- The above totals \$456.8 million, more than enough to balance the budget
- Other changes including the Governor's tax proposals leave the ending fund balance at \$238.5 million
- Proposed balance sheet page 10

# Governor's Budget

- Spending = \$3,763 million
- Revenue = \$3,684 million
- Transfers = \$71 million
- Net Taxes = -\$25 million
- Reduction in ending fund balance = \$33 million



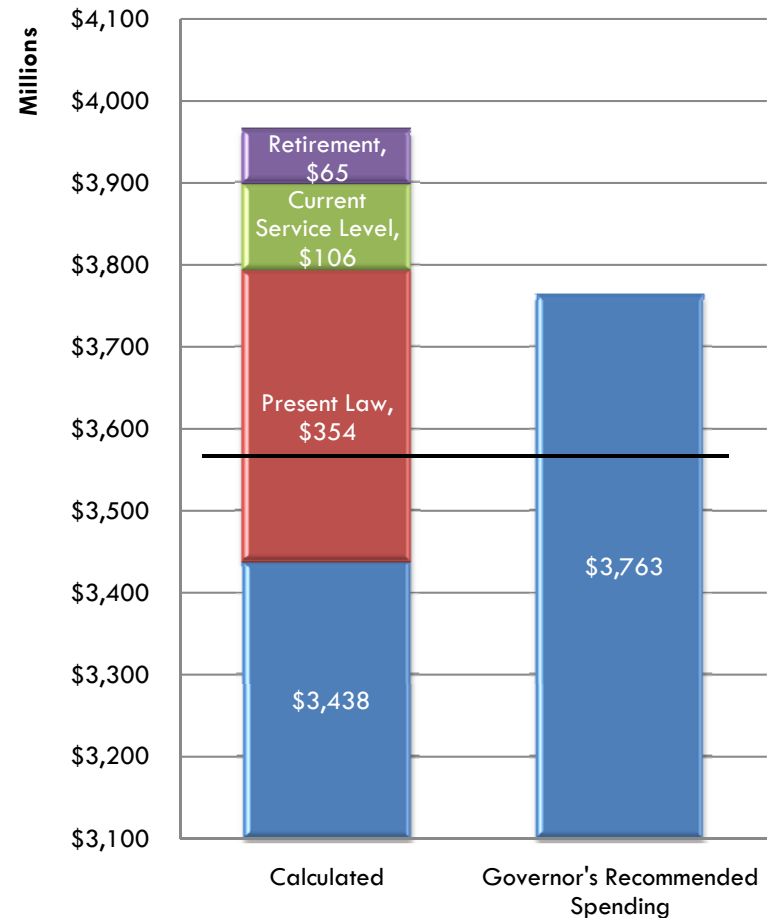
# HJ 2 Balance Sheet: Page 15



- HJ 2 Revenues
- Governor's Tax Proposals
- Governor's Spending Proposals
- Updated School funding costs
- Legislative Fiscal Division estimates for Statutory Appropriations, Transfers, Reversions, and Feed bill
- Ending Fund Balance: \$55.6 million

# Comparison of Spending

- Calculated Spending Pressure = \$3,963 million
- Governor's total spending recommendation = \$3,763 million
- HJ 2 Revenue = \$3,580 million
- Ending fund balance reduction = -\$145 million

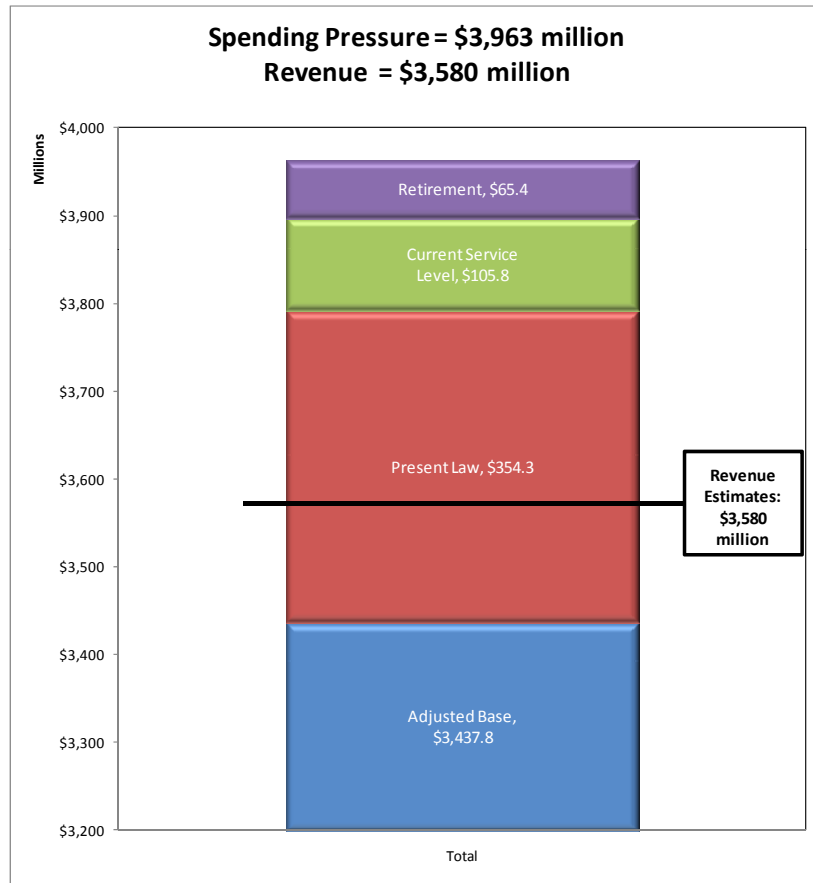




# Structural Balance

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# Structural Balance



- Spending Pressure Gap = \$383 million
- FY 2012 = \$199.3
- FY 2013 = \$183.3

**Structural Balance Comparison****FY 2012****FY 2013**

Underlying Structural Balance

\$ (199.3) \$ (183.3)

Governor's Revenue Assumptions

42.7 61.6

Net Governor's structural balance changes

55.0 44.0

Not Recognizing K-12 costs

5.6 9.4

Not addressing Retirement systems

29.8 35.7

**Governor's Structural Balance 12/15****\$ (66.3) \$ (32.7)****Structural Balance Comparison**

Table updated from page 12



# Risk of Structural Imbalance

## Positive Structural Balance

- May create opportunity for an increase in savings or capital investment. Has has been experienced by Montana in recent years.

## Negative Structural Balance

- May create continued financial strain, erosion of savings, less long term financial security
- Experience by Montana in the late 1980's and early 1990's.

# Appropriate Structural Balance?



- Savings available
- Fund balance
- Upside versus Downside risk of revenues
  - ▣ Downside risk to revenues in the 2009 Session –  
Structurally balanced and high ending fund balance
- 2007 Session positive structural balance
- Some structural imbalance may be appropriate in some circumstances

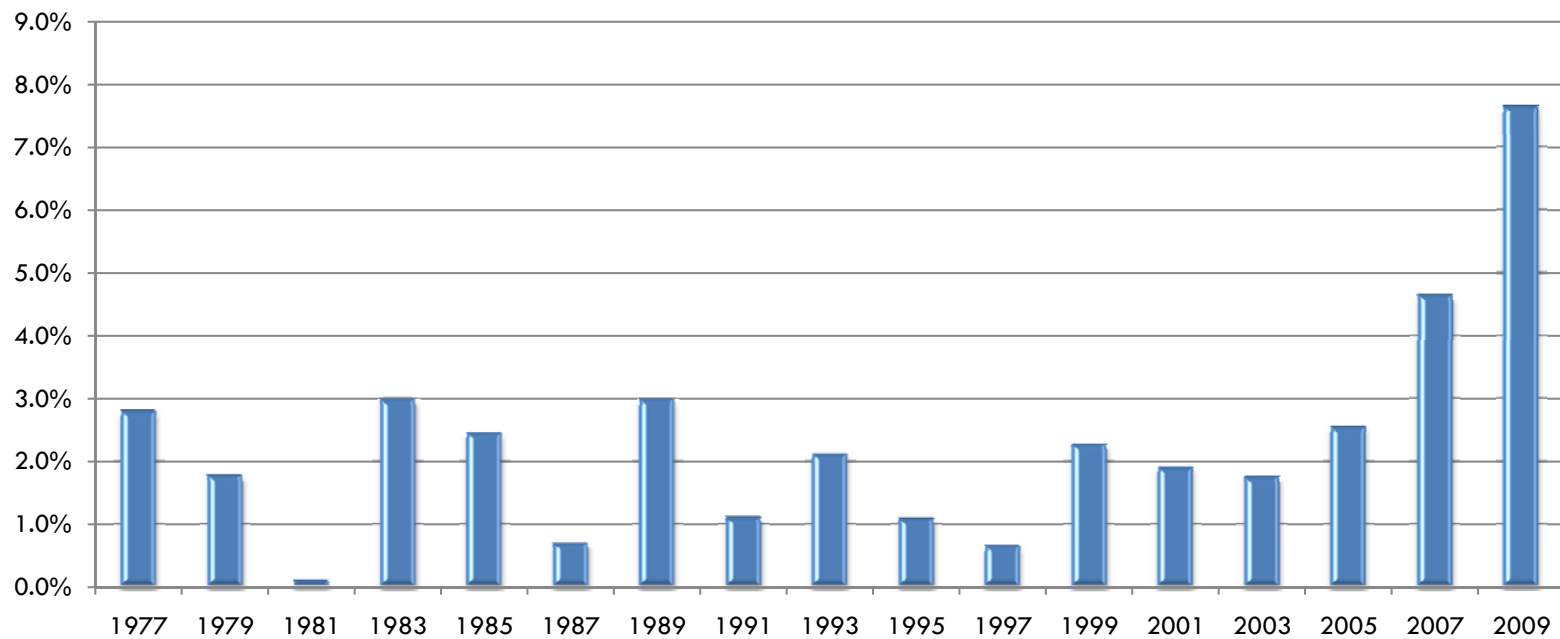


# Ending Fund Balance

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# Appropriate Ending Fund Balance?

**Legislative Projected Ending General Fund Balance  
as a % of Projected Biennial Expenditures**



**Legislative Session**

# Factors to Consider



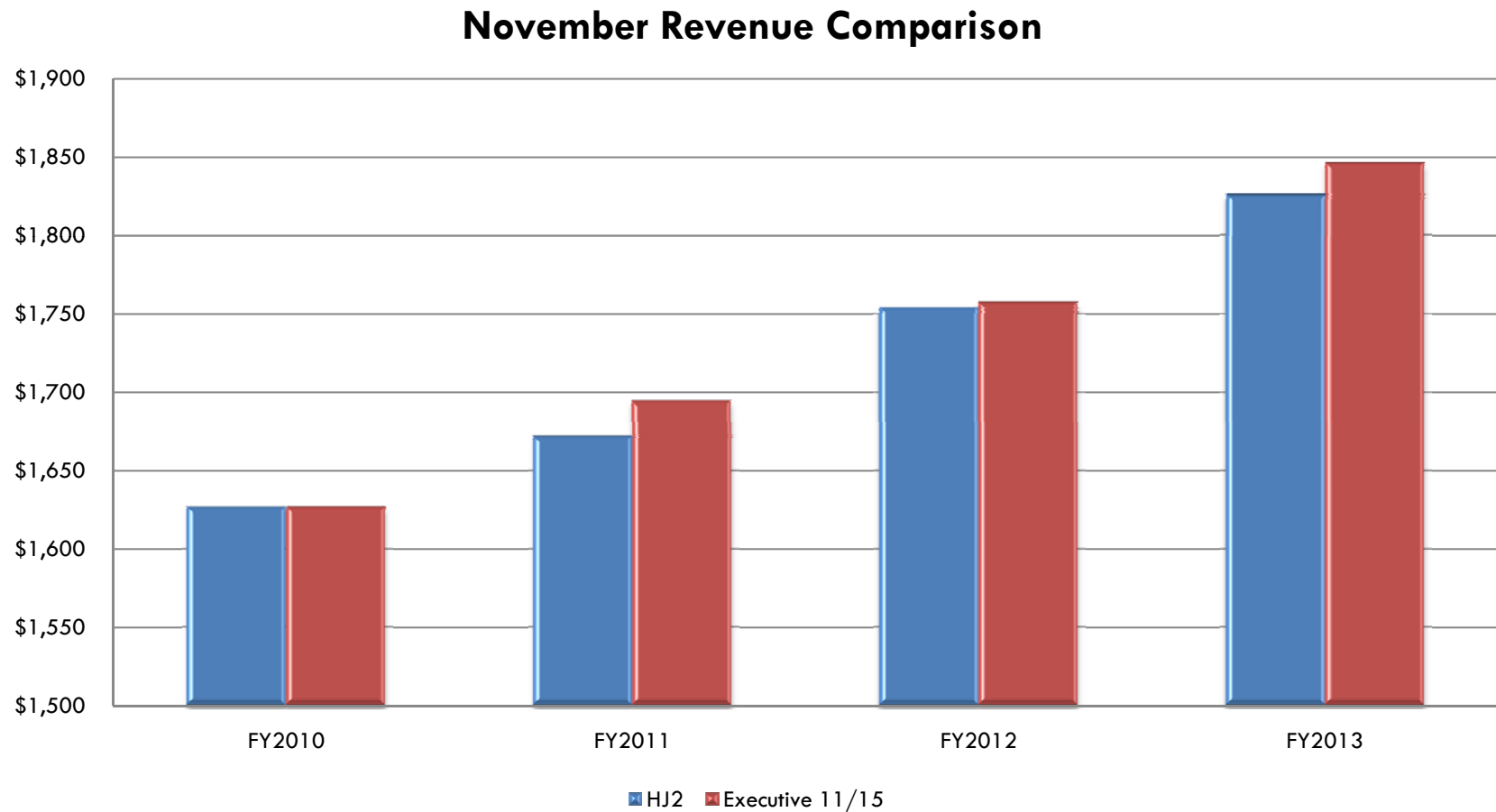
- Upside and downside risk to the revenue estimates
- Volatility of revenue estimates
- Availability of other savings funds



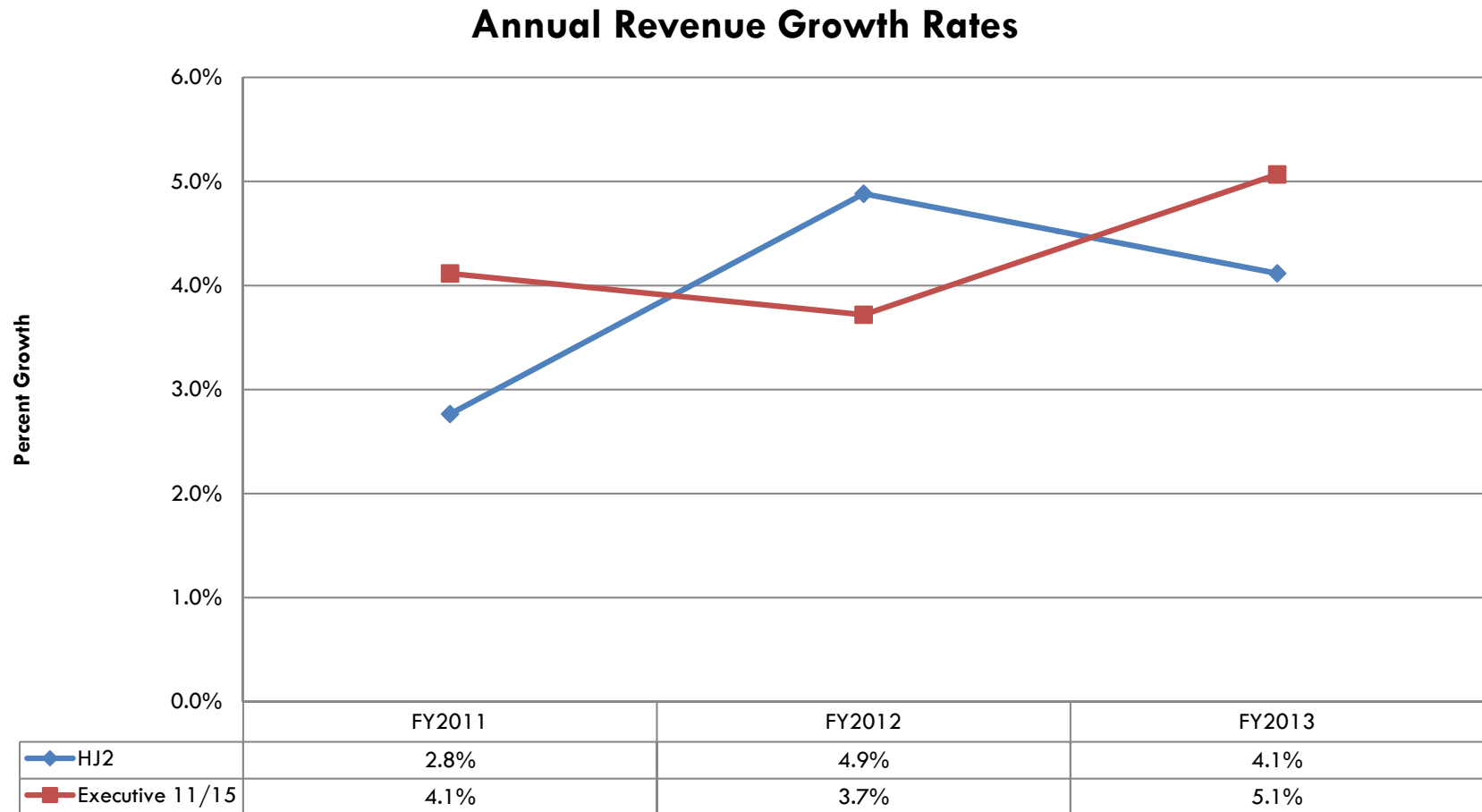
# Caution on Revenue Estimates

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# November Revenue Comparison



# November Growth Comparison





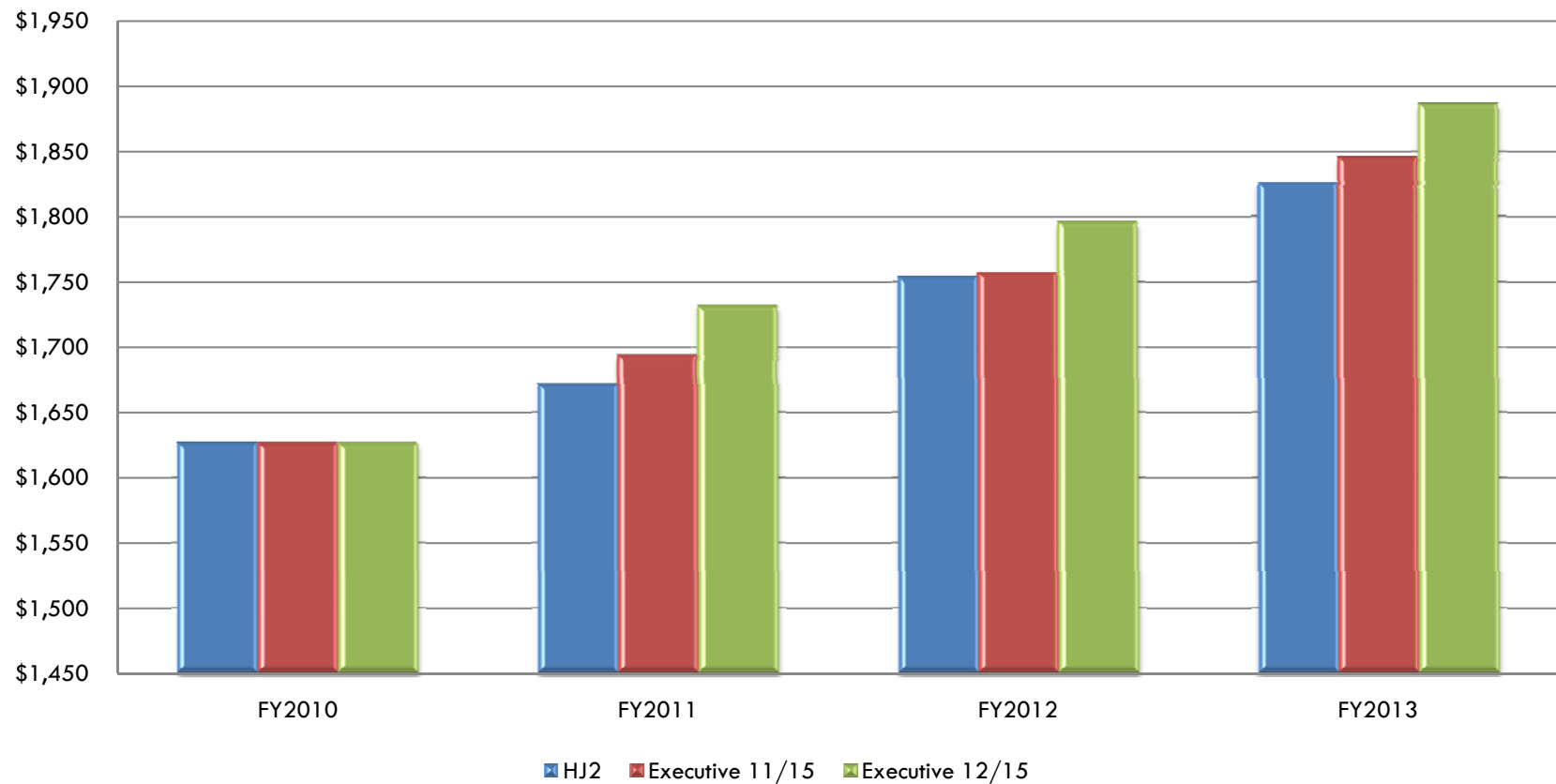
# Year to Date Revenue Comparison



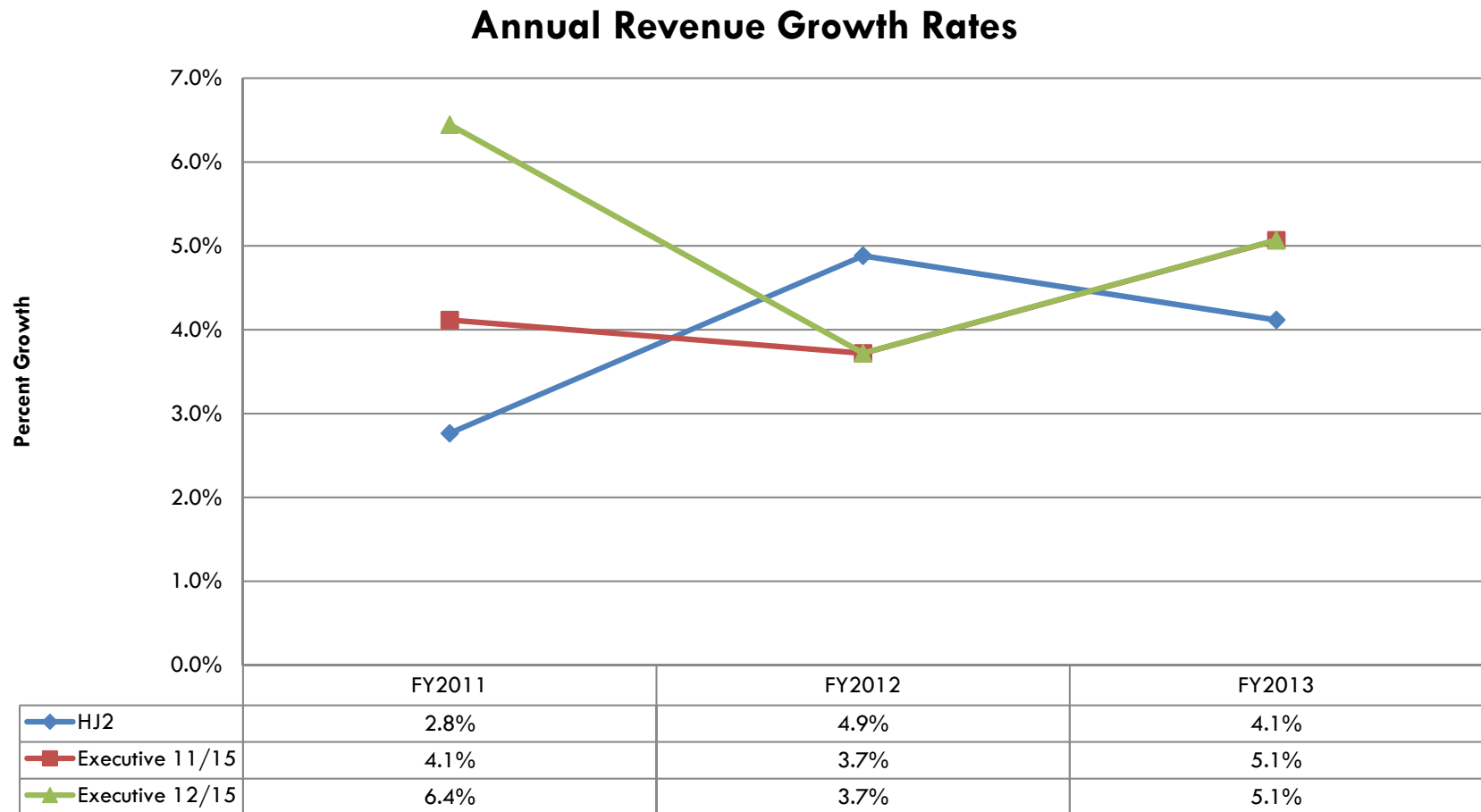
- ❑ Positive: Actual revenues at a snapshot in time
- ❑ Negative:
  - ▣ One data point does not necessarily make a trend
  - ▣ Collections could be affected by accounting or timing issues
  - ▣ Variability - \$281 million difference over 9 years
  - ▣ Month to month variable

# December Revenue Comparison

**Revenue Estimate Comparison**



# December Growth Comparison



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THE END

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