

OVERVIEW

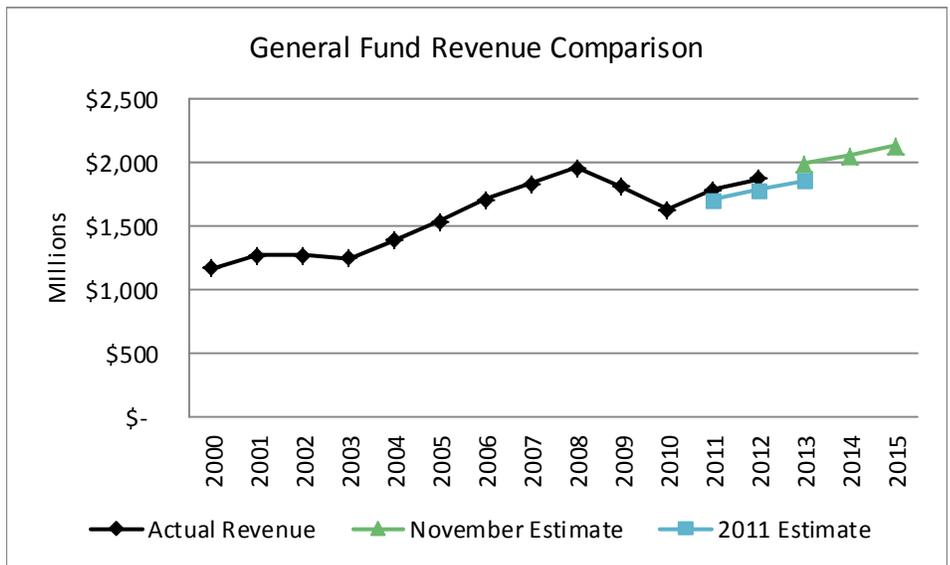
GROWING REVENUES AND BUDGET CHALLENGES

The 2013 legislative session will have the advantage of growing general fund revenue streams and a significant fund balance. The following analysis outlines the trends in revenue, structural balance and budget challenges for the 2013 legislative session. There are several budget challenges and significant policy issues that will be considered this session.

GROWING REVENUES

In FY 2009 and FY 2010, state revenues declined two years in a row. While two years ago, the legislature was confident that these declines were past, it was not clear how strong general fund revenues would return. The last two years has brought growth and stability to the general fund revenues. This stability gives confidence that the worst is behind us.

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



The chart above demonstrates the actual revenue collected from FY 2000 to FY 2012. The lower blue line for FY 2011 to FY 2013 shows the revenue anticipated at the end of the 2011 session and the green line shows the revenue estimated for FY 2013 to FY 2015 in November of 2012 by the Legislative Fiscal Division (LFD).

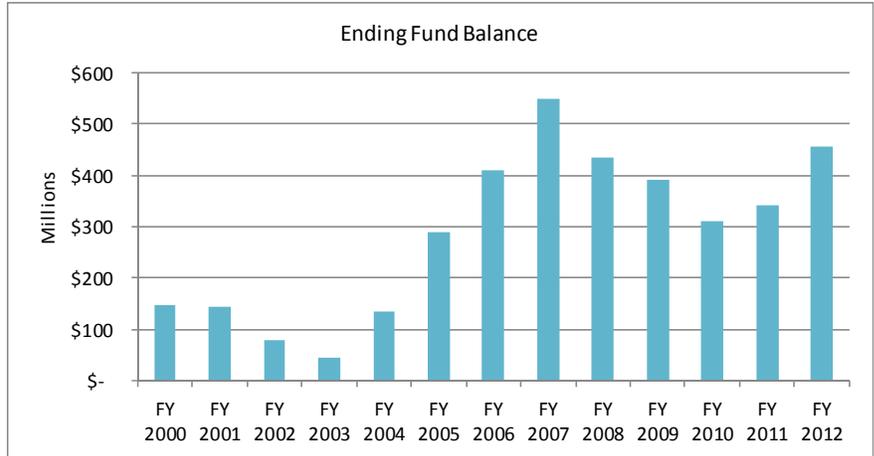
These additional revenues are based on an economic forecast from IHS Global Insight that shows slow economic growth of 4% as measured by gross state product (GSP). This growth in GSP is lower than recent growth in both the Montana and U.S. economies. Economists believe that the current slow growth patterns will continue for some time. For more information, see page 5 of Volume 2, the LFD revenue estimate analysis. Therefore, while the forecast level of revenue is higher and growing from recent years, it is below the long term revenue trend for Montana.

Structural Balance

The November revised revenue estimate for FY 2013 is \$143 million or 7.7% greater than the original FY 2013 estimate. In the 2011 session, the FY 2013 ongoing spending was set \$25 million above the revenue estimate. The net structural balance of \$118 million (\$143 million less \$25 million) from FY 2013 affords the legislature the opportunity to determine the use of this additional revenue for ongoing purposes if it so chooses.

Ending Fund Balance

In addition to this structural balance, a higher level of ending fund balance is available to the 2013 Legislature. Three years of higher revenues than anticipated adds up. While the 2011 session anticipated ending fund balance was \$150 million, even with the Governor's requested supplemental appropriations for the 2013 biennium the ending fund balance is currently anticipated to be nearly \$450 million. Some portion of this higher ending fund balance could be used by the 2013 Legislature for one time needs.



Several spending pressures face the 2013 Legislative session and Governor Schweitzer has offered solutions to many of these challenges in his budget proposal.

BUDGET CHALLENGES

Pension Funding Shortfall

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

Governor Schweitzer has proposals to fund the two largest systems' liabilities with a combination of employer, state, local government, and employee contribution increases. The annual general fund cost of these proposals is just less than \$50 million per year. While the proposals do not fully fund the additional amounts need to fund the Annual Required Contribution (ARC) as recommended by actuaries, it does turn the corner on the liabilities and they are forecast to close the funding gap in 37 to 45 years.

Personnel and Pay Plan

Employees of the state of Montana have not received an inflationary adjustment approved by the legislature in four years. Yet during this time period, many changes have occurred in market conditions and pay approved by the executive. LFD analysis has shown variance between agencies and types of employees how well employee pay compares to private and public sector counterparts. Since pay increases in the pay plan bill are in addition to the base HB 2 budget, the legislature may want to consider this variance when considering both base cost pay and the pay plan. For more information on state employee pay see:

http://leg.mt.gov/content/Publications/fiscal/interim/2012_financemty_Sept/Personal%20Services%20Rpt.pdf

Governor Schweitzer has proposed changes in the HB 2 budget to address some base pay concerns. Specifically these adjustments can be found in the Department of Corrections and the Office of the Public Defender. In addition, Governor Schweitzer and the unions have agreed to a 5% per year across the board pay increase and a 10% per year increase in employer contributions for health insurance for state employees that the legislature will be asked to approve. For a more detailed analysis on the Governor Schweitzer proposed pay plan see:

<http://leg.mt.gov/content/Publications/fiscal/ba-2015/Volume-1/Appendix-B-Executive-Pay-Plan-Proposal.pdf>

Rates Paid to Private Providers of Services

Some state government services are provided by private entities such as hospitals, nursing homes, private prisons, and other community providers. Similar to pay increases for state employees, private providers of services to citizens of Montana have generally not received an across the board increase in funding in four years. Governor Schweitzer has proposed an increase of 2% per year for most providers and statutorily calculated increases for other providers.

Federal Healthcare Reform and Montana's choices

Federal Affordable Care Act or ACA requires or allows Montana to make several changes in the funding and structure of state healthcare programs. Montana's choices include part of the expansion of Medicaid and the future of certain current state health programs that, in part, overlap with some new federal provisions. The program, law, and budget choices are interconnected and will need to be tracked carefully during session.

Governor Schweitzer recommends expanding Medicaid and phasing out Insure Montana, the state program that provides subsidies to small businesses that provide health care to employees.

Federal Fiscal Cliff

The federal government has plans to increase tax collections and decrease spending. Both impacts will affect Montana's budget and economy. The tax changes will slightly decrease Montana's income tax collections as additional federal taxes will be partially deductible from Montana's taxable income. On net, the direct tax impact from the tax changes considered in the Federal Fiscal Cliff are relatively small.

The larger impact on the revenue side will result in changes to the economy from changes to federal tax law and federal direct spending reductions. For these impacts, the LFD revenue estimate relies on IHS Global Insight, the state's economic forecast company. As the federal government makes decisions regarding addressing the federal deficit, IHS Global Insight will adjust their economic forecast accordingly. Currently, IHS Global Insight has assumed a partial implementation of the sequestration or fiscal cliff provisions. For more information see the Revenue Section of this volume.

In addition to tax and direct spending provisions, the Federal Fiscal Cliff contains budget reductions that will impact the state agency budgets directly. The largest and most difficult of these provisions is anticipated to be in K-12 education, the Department of Justice, and public health. Governor Schweitzer has no specific recommendations to address the anticipated reductions in federal funding. Details as to which fiscal cliff measures will be implemented may become clearer during session.

Wildfire Funding

Wildfire costs in FY 2013 are expected to reach \$59.4 million, a much higher than usual level. The seven year average wildfire costs are \$23.8 million per year. The fire suppression account established in the 2007 special session has been fully expended and both a supplemental appropriation for the current biennium and additional funds for the next biennium have been requested by the executive.

Energy Development Issues

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

In order to assist with these challenges, Governor Schweitzer recommends transferring \$12 million of state general fund to the Oil and Gas board to distribute to affected counties and cities. In addition, policies are being implemented to address recruitment and retention concerns for state employees in these areas.

Managing Budget Volatility

The 2013 legislature will determine how it addresses budget volatility. The general fund status sheets provided to the legislature illustrate structural balance and ending fund balance are both readily available. Governor Schweitzer proposes a positive structural balance (revenues exceeding spending) and an ending fund balance of \$414 million.

Questions before the 2013 Legislative session will include:

- 1) How much estimated ending fund balance does the legislature wish to budget for the 2015 biennium?
- 2) Are there other ways that the legislature will wish to manage potential budget volatility?

GOVERNOR SCHWEITZER'S BUDGET REQUEST

While the major budget issues shown above highlight some of the recommendations of the Governor Schweitzer budget, there are several more budget recommendations contained in the executive proposal.

Other major recommendations in the Governor Schweitzer's budget request include:

State Fund Worker's Compensation

Governor Schweitzer recommends a bill to combine the Montana State Fund "Old Fund" (claims for injuries resulting from accidents that occurred before July 1, 1990), with the current workers' compensation fund. This bill would have claims from the "Old Fund" paid from current workers' compensation insurance surplus and reserves rather than the general fund. This results in general fund savings of \$7.4 million in FY 2014 and \$5.7 million in FY 2015. The bill also includes a provision that the State Fund may not raise rates to pay for these amounts. Potential legal ramifications are described in the Appendix to Volume 1 under general fund transfers.

K-12 funding

The Executive proposes present law increases to fund K-12 school district BASE aid and special education factors by 0.89% in FY 2014 and 2.08% in FY 2015. The increase in general fund from the FY 2012 base appears largely due to the amount of school trust revenue in the guarantee account which was higher than normal, and reduced the level of general fund needed to fund schools in FY 2012. These unusually higher school trust revenue amounts will not continue in the 2015 biennium.

Montana University System funding

Governor Schweitzer recommends an 8.4% increase in the general fund budgets from the 2013 biennium to the 2015 biennium for educational units and agencies. The budget recommends returning \$2.6 million per year of student assistance funding to general fund after the temporary federal funding is no longer available. Additional recommendations include: Community college funding increases by 9% or nearly \$2 million in the biennium, additional University of Washington medical education slots for doctors, and continuing support for Montana's non-beneficiary tribal college students.

Department of Corrections

The Department of Corrections is funded primarily with general fund. The main increases in the Department of Corrections budget are to maintain current programs.

Long-Range Planning (HB 5)

The executive proposal for the LRBP would provide \$271.4 million of authority to expend non-state funds and appropriations of state funds. The LRBP proposal would construct seven new state buildings, including a new Low Side Prison Unit in Deer Lodge, the Heritage Center in Helena, and the College of Technology in Missoula, among others. The projects would be funded with a mix of all fund types, with additional project funding through a \$16.3 million transfer of general funds to the LRBP capital projects fund and \$87.9 million in bond proceeds.

Long-Range Information Technology (HB 10)

The executive proposal for the LRITP recommends \$18.2 million in appropriations for major information technology (IT) projects. The proposal includes six major projects which include upgrades to the Secretary of State's information system, which will allow the agency to better manage information on the state's registered businesses. Another large IT project is the Legislative Branch Session Systems Replacement project that would replace the operating systems underlying the LAWS system. Funding for the projects would come from most fund types and would require a transfer of \$8.8 million from the general fund to the LRITP capital projects fund.

More information on the LRBP and LRITP requests may be seen in Section F of the Legislative Fiscal Division Budget Analysis.

THE GOVERNOR SCHWEITZER BUDGET

The Governor Schweitzer recommended budget is structurally balanced and has an ending fund balance of \$414 million or 9.9% of the biennial budget. The following table shows the Governor's estimation of general fund revenues and proposed spending:

Executive Budget Proposal - General Fund (in Millions)								
	Actual FY 2012	Estimated FY 2013	Requested FY 2014	Requested FY 2015	2013 Biennium	2015 Biennium	Biennial \$ Change	Biennial % Change
Beginning Fund Balance	\$341.875	\$453.180	\$433.437	\$423.037	\$341.875	\$433.437	\$91.562	26.8%
Revenue								
Executive Revenue Estimates	1,870.954	1,978.755	2,056.447	2,119.016	3,849.709	4,175.463	325.754	8.5%
Executive Revenue Proposals	0.000	0.000	(17.297)	(18.391)	0.000	(35.688)	(35.688)	
Executive Revenue Adjustments	8.751	(1.500)	0.000	0.000	7.251	0.000	(7.251)	-100.0%
Total Funds Available	\$2,221.580	\$2,430.435	\$2,472.587	\$2,523.662	\$4,198.835	\$4,573.212	\$374.377	8.9%
Disbursements								
General Appropriations Act	1,587.917	1,642.280	1,752.962	1,797.234	3,230.197	3,550.196	319.999	9.9%
Feed Bill (HB1)	1.356	10.056	1.397	10.309	11.412	11.706	0.294	2.6%
Supplemental Appropriations (HB 3)	0.000	123.621	0.000	0.000	123.621	0.000	(123.621)	-100.0%
Long Range Building Proposals - Cash (HB 5)	0.000	0.000	16.300	0.000	0.000	16.300	16.300	
Long Range Information Technology (HB 10)	0.000	0.000	8.808	0.000	0.000	8.808	8.808	
Pay Plan (HB 13)	0.000	0.000	28.111	52.006	0.000	80.117	80.117	
Long Range Building Proposal - Bonds (HB 14)*	0.000	0.000	2.954	5.908	0.000	8.862	8.862	
School Funding	0.000	0.300	0.000	0.000	0.300	0.000	(0.300)	-100.0%
Pension Legislation	0.000	0.000	30.467	30.517	0.000	60.984	60.984	
Infrastructure Assistance	0.000	0.000	12.000	0.000	0.000	12.000	12.000	
Water Compact Obligations	0.000	0.000	2.420	4.840	0.000	7.260	7.260	
Medicaid Expansion	0.000	0.000	1.892	3.108	0.000	5.000	5.000	
Statutory Appropriations	171.229	207.692	197.095	211.141	378.921	408.236	29.315	7.7%
Statutory Appropriations - Economic Development Legislation	0.000	0.000	(3.000)	(3.000)	0.000	(6.000)	(6.000)	
Transfers	15.469	15.112	13.318	11.637	30.581	24.955	(5.626)	-18.4%
Transfers - Old Fund Legislation	0.000	0.000	(7.356)	(5.652)	0.000	(13.008)	(13.008)	
Other Appropriations	3.665	5.554	0.000	0.000	9.219	0.000	(9.219)	-100.0%
Reversions	0.000	(7.618)	(7.818)	(8.049)	(7.618)	(15.867)	(8.249)	108.3%
Prior Year Adjustments	(5.127)	0.000	0.000	0.000	(5.127)	0.000	5.127	-100.0%
Total Disbursements	\$1,774.509	\$1,996.997	\$2,049.550	\$2,109.999	\$3,771.506	\$4,159.549	\$388.043	10.3%
Fund Balance Adjustment	\$6.109	\$0.000	\$0.000	\$0.000	\$6.109	\$0.000	(\$6.109)	
Ending Fund Balance	\$453.180	\$433.437	\$423.037	\$413.663	\$433.438	\$413.663	(19.775)	-4.8%

GOVERNOR'S BUDGET ADJUSTED USING THE LFD ESTIMATES FOR REVENUE AND STATUTORY APPROPRIATIONS

The legislature has the authority to decide the level of revenue used to balance the state's budget. Using the November 15th Legislative Fiscal Division's revenue estimates, the final Governor Schweitzer's budget continues to be structurally balanced, meaning that ongoing revenues exceed ongoing spending.

The following balance sheet lays out the ongoing and one-time-only spending of the Governor Schweitzer budget submission with the LFD November revenue estimates. It illustrates the comparable and non-comparable items and allows for biennium to biennium comparisons.

2015 Biennium Ongoing Spending

The growth in ongoing spending in Governor Schweitzer's budget (adjusted for a school Base Aid supplemental in FY 2013) is 12.5% from biennium to biennium. The primary components of the increase are: HB 2 adjustments total 7.9%, pay plan 2.0%, and pensions (including revenue reductions and offsets to statutory appropriations) 2.5%.

2015 Biennium One-time Spending

Governor Schweitzer's proposed budget decreases spending on one-time items primarily due to no supplemental requirements anticipated in the 2015 biennium.

FY 2013

Supplemental appropriations for FY 2013 total \$123.6 million. These supplementals are primarily for: K-12 funding as anticipated with the veto of HB 316 after the 2011 session for \$34.7 million, wildland fire cost of \$50 million, and the Libby asbestos legal settlement for \$26.8 million. The school funding items of the supplemental have been considered ongoing spending as it is statutorily required spending.

Governor Schweitzer Budget adjusted using LFD revenue estimates and statutory appropriations:

17-7-151, MCA - General Fund Comparison								
(in Millions)								
	Actual FY 2012	Estimated FY 2013	Requested FY 2014	Requested FY 2015	2013 Biennium	2015 Biennium	Biennial \$ Change	Biennial % Change
Beginning Fund Balance	\$341.875	\$453.180	\$449.416	\$424.936	\$341.875	\$449.416	\$107.541	31.5%
Revenue								
Legislative Revenue Estimates	1,870.954	1,988.754	2,044.546	2,124.162	3,859.708	4,168.708	309.000	8.0%
Legislative Prior Year Revenue Adjustments	8.751	0.000	0.000	0.000	0.000	0.000	0.000	
Supplemental Appropriations (HB 3) - Tfr from Lottery Reduction	0.000	(1.500)	0.000	0.000	(1.500)	0.00	1.500	
Pension Legislation - Reduction to General Fund	0.000	0.000	(17.297)	(18.391)	0.00	(35.688)	(35.688)	
Total Funds Available	\$2,221.580	\$2,440.434	\$2,476.665	\$2,530.707	\$4,200.083	\$4,582.436	\$382.353	9.1%
Disbursements								
General Appropriations Act - Ongoing	1,577.269	1,628.666	1,744.213	1,790.052	3,205.935	3,534.265	328.330	10.2%
General Appropriations Act - OTO	10.648	13.614	8.749	7.182	24.262	15.931	(8.331)	-34.3%
Feed Bill (HB 1)	1.356	10.933	1.418	11.097	12.289	12.515	0.226	1.8%
Supplemental Appropriations (HB 3) - Ongoing	0.00	38.534	0.000	0.000	38.534	0.000	(38.534)	-100.0%
Supplemental Appropriations (HB 3) - OTO	0.00	85.087	0.000	0.000	85.087	0.000	(85.087)	-100.0%
Long Range Building Proposals - Cash (HB 5)	0.00	0.000	16.300	0.000	0.000	16.300	16.300	
Long Range Information Technology (HB 10)-OTO	0.00	0.000	8.808	0.000	0.000	8.808	8.808	
Pay Plan (HB 13) - Ongoing	0.00	0.000	24.036	52.006	0.000	76.042	76.042	
Pay Plan (HB 13) - OTO	0.00	0.000	4.075	0.000	0.000	4.075	4.075	
Long Range Building Proposal - Bonds (HB 14)* - Ongoing	0.00	0.000	2.954	5.908	0.000	8.862	8.862	
School Funding - OTO	0.00	0.300	0.000	0.000	0.300	0.000	(0.300)	-100.0%
Pension Legislation - Ongoing	0.00	0.000	30.467	30.517	0.000	60.984	60.984	
Infrastructure Assistance - OTO	0.00	0.000	12.000	0.000	0.000	12.000	12.000	
Water Compact Obligations - Bonds - Ongoing	0.00	0.000	2.420	4.840	0.000	7.260	7.260	
Medicaid Expansion - Ongoing	0.00	0.000	1.892	3.108	0.000	5.000	5.000	
Statutory Appropriations - Ongoing	171.229	200.950	199.266	213.143	372.179	412.409	40.230	10.8%
Statutory Appropriations - Legislation	0.000	0.000	(3.000)	(3.000)	0.000	(6.000)	(6.000)	
Transfers - Ongoing	15.469	14.998	13.306	11.779	30.467	25.085	(5.382)	-17.7%
Transfers - Old Fund Legislation	0.000	0.000	(7.356)	(5.652)	0.000	(13.008)	(13.008)	
Other Appropriations	3.665	5.554	0.000	0.000	9.219	0.000	(9.219)	-100.0%
Reversions	0.000	(7.618)	(7.818)	(8.049)	(7.618)	(15.867)	(8.249)	108.3%
Prior Year Adjustments	(5.127)	0.000	0.000	0.000	(5.127)	0.000	5.127	-100.0%
Total Disbursements	\$1,774.509	\$1,991.018	\$2,051.730	\$2,112.931	\$3,765.527	\$4,164.661	\$399.134	10.6%
Fund Balance Adjustment	6.109	0.000	0.000	0.000	6.109	0.000	(6.109)	
Ending Fund Balance	\$453.180	\$449.416	\$424.936	\$417.776	\$440.665	\$417.776	(22.890)	-5.5%
Biennial Comparison								
Total Ongoing	1,765.323	1,886.463	2,001.798	2,105.749	3,651.786	4,107.547	455.761	12.5%
Total OTO	9.186	104.555	49.932	7.182	113.741	57.114	(56.627)	-49.8%
Total Disbursements	\$1,774.509	\$1,991.018	\$2,051.730	\$2,112.931	\$3,765.527	\$4,164.661	\$399.134	10.6%
Structural Balance	\$105.631	\$100.791	\$25.451	\$0.022	\$206.422	\$25.473	(\$180.949)	-87.7%
For informational purposes only:								
Executive Budget Adjustments for Guarantee Account Revenue estimate difference								
Reduce School Funding Present Law Requirement for additional Guarantee Account revenue estimated by the LFD	\$0.000	(\$5.099)	(\$7.607)	(\$8.181)	(\$5.099)	(\$15.788)	(\$10.689)	209.6%
Adjusted Total Disbursements	1,774.509	1,985.919	2,044.123	2,104.750	3,760.428	4,148.873	388.44	10.3%
Adjusted Ending Fund Balance	453.180	454.515	437.642	438.663	454.515	438.663	(15.85)	-3.5%
Adjusted Structural Balance	\$105.631	\$105.890	\$33.058	\$8.203	\$211.521	\$41.261	(\$170.260)	-80.5%

Note that the balance sheet above adjusted all revenue estimates except the coal severance tax switch to fund pensions instead of being deposited in the general fund. The LFD estimate for coal severance tax is \$2.0 million less per year than estimated by the Office of Budget and Program Planning. Governor Schweitzer's proposal for pension funding requires a certain level of funding to achieve the actuarial goals outlined in his proposal; if these revenues were reduced the actuarial goals would not be achieved. This balance sheet assumes that Governor Schweitzer maintains his level of funding for pensions.

The graphic at right describes the past several years and the next biennium's budgets and revenues. The Governor Schweitzer budget increases total general fund spending to be roughly equivalent with anticipated revenues in FY 2013 through FY 2015.

Budget Analysis

Many more details are contained in the revenue estimates, the budget analysis, and the remaining sections of the overview. The LFD will give an update to this analysis when the Governor Bullock budget is prepared and available for session.

