

# **BUDGET STATUS REPORT AND REVENUE TRENDS**

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

By  
Legislative Fiscal Division Staff

March 13, 2014



## INTRODUCTION

The purpose of this report is to provide the Legislative Finance Committee with an update to the projected general fund ending balance for the 2015 biennium and to discuss emerging budget issues of all funding sources.

In this analysis, staff reviewed major state special revenue fund balances and statutory appropriation estimates. Comments are made regarding some of the major other sources throughout the report. Updated general fund statutory appropriation estimates are included in the fund balance discussion and in “Other Significant Budget Factors” section. While potential reversions or supplementals are discussed in the text of this report, no changes have been made to the anticipated general fund balance in this March update report. The June report will address these potential impacts.

## GENERAL FUND BALANCE DISCUSSION

The updated fund balance includes only changes in the anticipated statutory appropriations. For this budget update, staff examined each statutory appropriation and updated the analysis of these costs. Several statutory appropriations changed slightly, but a major adjustment was discovered. Public Employee Retirement System Statutory Transfers are estimated to be \$6.8 million less in the biennium than anticipated during session. For more information please see page 13 “Other Significant Budget Factors”.

As shown in the chart below, the final audited general fund unassigned balance for FY 2013 was \$537.6 million. This is \$0.3 million higher than the unaudited balance shown in December. The projected FY 2015 ending fund balance was \$347.1 million in December. The updated projected ending fund balance shown below is \$352.9 million, or an increase of \$5.9 million.

<b>General Fund Update March 2014</b>				
<i>(in Millions)</i>				
	Actual FY 2012	Actual FY 2013	Budget FY 2014	Budget FY 2015
Beginning Fund Balance	\$341.9	\$452.4	\$537.3	\$385.4
Revenue	1,871.0	2,077.6	2,056.4	2,136.6
<b>Total Funds Available</b>	<b>2,212.8</b>	<b>2,530.0</b>	<b>2,593.7</b>	<b>2,522.0</b>
Disbursements				
Ongoing				
HB 2, HB 13, and pension bills	1,577.9	1,613.5	1,755.6	1,832.3
Statutory	171.2	199.7	259.0	274.0
Transfers	15.5	15.9	13.6	12.1
Other (includes feed bill)	1.4	60.4	16.2	24.0
Reversions			(7.8)	(8.1)
OTO				
HB 2	10.1	13.7	22.7	23.0
Transfers (including \$51.7 wildland fire in FY 2014)	3.7	36.5	145.0	10.9
Other (includes carry forward)		58.3	4.1	0.9
<b>Total Disbursements</b>	<b>1,779.7</b>	<b>1,997.9</b>	<b>2,208.3</b>	<b>2,169.0</b>
Adjustments	19.2	5.5		
<b>Ending Fund Balance</b>	<b>\$452.4</b>	<b>\$537.6</b>	<b>\$385.4</b>	<b>\$352.9</b>

## **REVENUES**

This next portion of the report is designed to apprise interested members of the legislature on year-to-date general fund revenue collections, recent economic trends and the outlook for FY 2014 relative to the official estimate contained in SJ 2.

### **SUMMARY**

General fund revenue collections are nearly even with FY 2013 amounts, and are slightly above the overall growth estimate contained in SJ 2. Total individual and corporation income tax collections in FY 2013 reflected one-time activity that is not expected to continue in FY 2014. As a result, collections from these two sources—as well as total general fund collections—are expected to decrease from the FY 2013 level.

## YEAR-TO-DATE GENERAL FUND REVENUE

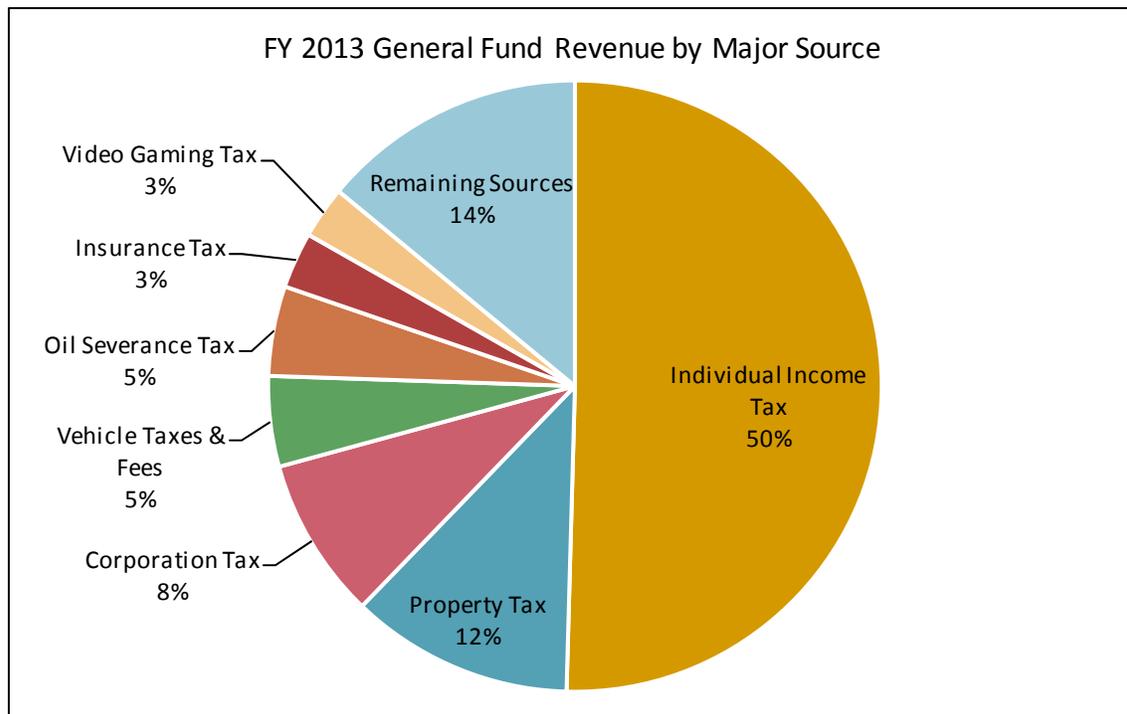
FY 2014 general fund revenues through the end of February are \$4.7 million or 0.4% ahead of FY 2013 revenues through the same period; this increase is slightly above the anticipated decline of 1.0%. All major revenue sources and any other sources with significant differences will be discussed in further detail in the next section.

General Fund Revenue Monitoring Report							
(in Millions)							
Revenue Source	Actual FY 2013	SJ2 Estimate* FY 2014	SJ2 Estimate % Change	2/28/2013 FY 2013	2/28/2014 FY 2014	YTD Difference	YTD % Change
<b>Largest Seven Sources</b>							
Individual Income Tax	\$1,047.790	\$1,039.082	-0.8%	\$712.025	\$746.664	\$34.639	4.9%
Property Tax	244.607	245.287	0.3%	137.125	136.313	(0.812)	-0.6%
Corporation Tax	177.497	154.096	-13.2%	100.136	68.539	(31.597)	-31.6%
Vehicle Taxes & Fees	99.352	102.659	3.3%	56.066	55.413	(0.653)	-1.2%
Oil Severance Tax	98.683	99.336	0.7%	23.736	29.201	5.465	23.0%
Insurance Tax	61.678	52.021	-15.7%	25.729	21.191	(4.539)	-17.6%
Video Gaming Tax	57.261	59.929	4.7%	28.211	27.980	(0.231)	-0.8%
<b>Other Business Taxes</b>							
Drivers License Fee	4.527	4.435	-2.0%	2.875	2.513	(0.361)	-12.6%
Investment Licenses	6.951	7.457	7.3%	6.181	6.557	0.376	6.1%
Lodging Facilities Sales Tax	16.720	18.365	9.8%	9.686	10.210	0.524	5.4%
Public Contractor's Tax	(0.138)	3.259	-2468.7%	0.114	1.609	1.495	1315.5%
Railroad Car Tax	2.179	2.320	6.5%	1.654	1.690	0.036	2.2%
Rental Car Sales Tax	3.523	3.632	3.1%	2.173	2.179	0.006	0.3%
Retail Telecom Excise Tax	20.652	23.236	12.5%	9.294	9.009	(0.285)	-3.1%
<b>Other Natural Resource Taxes</b>							
Coal Severance Tax	13.265	14.857	12.0%	7.674	7.684	0.009	0.1%
Electrical Energy Tax	5.067	4.521	-10.8%	2.404	2.016	(0.389)	-16.2%
Metal Mines Tax	10.049	10.595	5.4%	0.040	0.510	0.470	1179.4%
U.S. Mineral Royalties	29.205	30.953	6.0%	14.201	13.277	(0.924)	-6.5%
Wholesale Energy Trans Tax	3.558	4.140	16.4%	1.862	1.470	(0.393)	-21.1%
<b>Other Interest Earnings</b>							
Coal Trust Interest Earnings	24.153	24.354	0.8%	12.737	10.926	(1.810)	-14.2%
TCA Interest Earnings	2.465	2.346	-4.8%	1.562	1.108	(0.454)	-29.1%
<b>Other Consumption Taxes</b>							
Beer Tax	3.033	3.067	1.1%	1.820	1.825	0.006	0.3%
Cigarette Tax	31.011	30.433	-1.9%	20.201	19.375	(0.825)	-4.1%
Liquor Excise Tax	17.724	19.284	8.8%	10.700	11.020	0.320	3.0%
Liquor Profits	10.500	11.080	5.5%	-	-	-	-
Lottery Profits	13.084	14.342	9.6%	2.685	3.068	0.383	14.3%
Tobacco Tax	5.853	6.005	2.6%	3.513	3.597	0.084	2.4%
Wine Tax	2.195	2.218	1.0%	1.335	1.369	0.034	2.6%
<b>Other Sources</b>							
All Other Revenue	36.578	32.548	-11.0%	18.273	25.301	7.028	38.5%
Highway Patrol Fines	4.140	4.467	7.9%	2.333	2.325	(0.008)	-0.3%
Nursing Facilities Fee	4.928	4.740	-3.8%	3.495	2.475	(1.020)	-29.2%
Public Institution Reimbursement	16.212	17.802	9.8%	8.674	6.775	(1.899)	-21.9%
Tobacco Settlement	3.321	3.519	6.0%	-	-	-	-
Largest Seven Subtotal	\$1,786.868	\$1,752.411	-1.9%	\$1,083.029	\$1,085.302	\$2.273	0.2%
Remaining Sources Subtotal	290.754	303.974	4.5%	145.486	147.887	2.402	1.7%
<b>Grand Total</b>	<b>\$2,077.622</b>	<b>\$2,056.385</b>	<b>-1.0%</b>	<b>\$1,228.515</b>	<b>\$1,233.189</b>	<b>\$4.674</b>	<b>0.4%</b>

\* SJ 2, Adjusted for Legislative Impacts

## MAJOR SOURCES

In FY 2013, the largest seven revenue sources accounted for 86% of total general fund revenue. This section will highlight current trends with each source and further revenue detail if applicable.

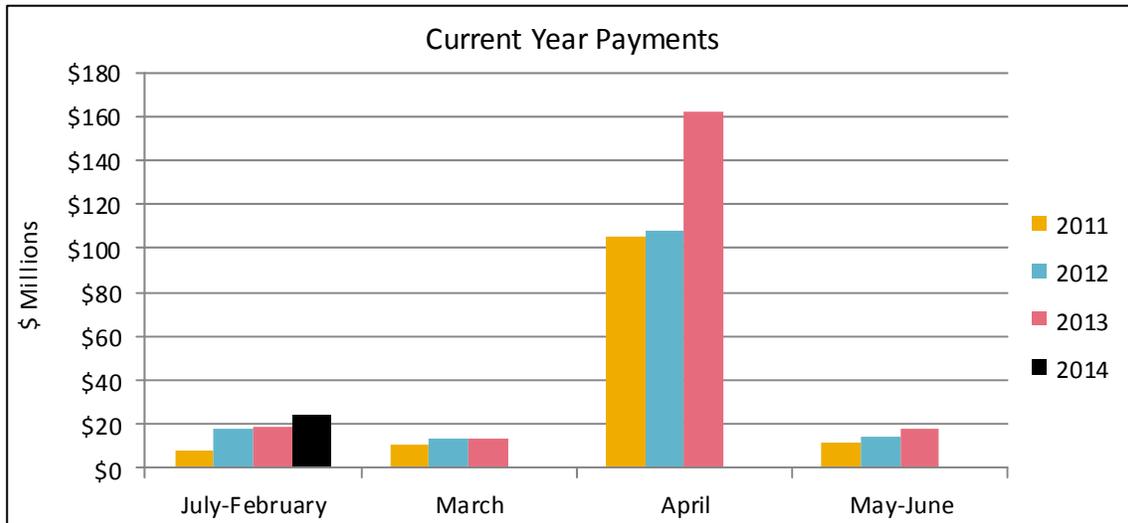


### Individual Income Tax: Above Estimate, but Slow Withholding Growth

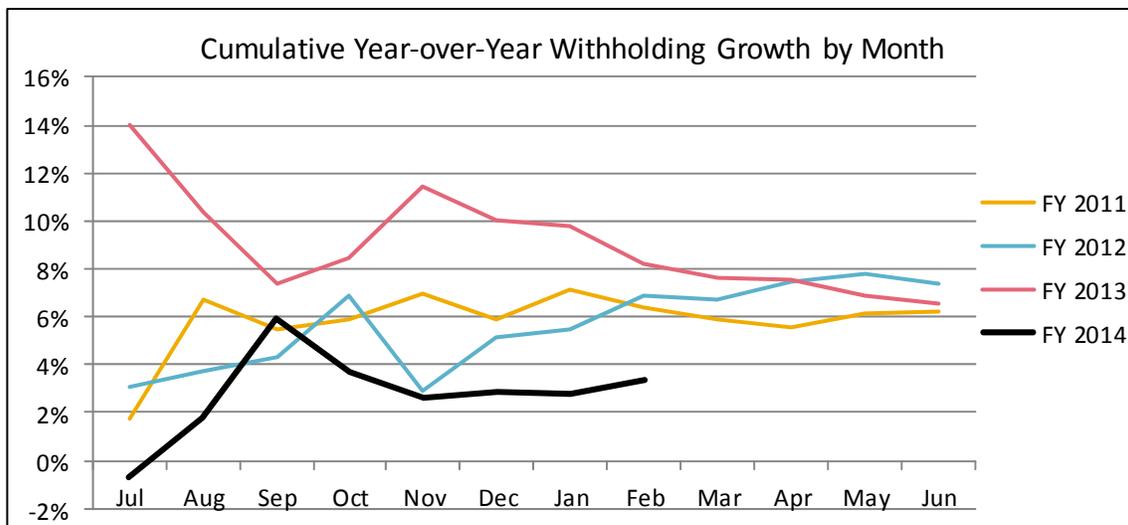
Individual income tax collections are \$34.6 million or 4.9% above last year, and above the anticipated decline of 0.8% contained in the official estimate. Withholding tax collections have slowed to 3.4% over last year through February; this growth is slightly up from last month.

Year-to-Date Individual Income Tax				
(\$ Millions)				
	FY 2014	FY 2013	Difference	% Difference
Withholding	\$517.2	\$500.3	\$16.8	3.4%
Estimated Payments	157.6	153.5	4.1	2.7%
Current Year Payments	23.8	18.4	5.4	29.4%
Audit, P&I, Amended	21.1	17.1	4.0	23.4%
Refunds	(118.0)	(114.0)	(4.0)	3.5%
Refund Accrual Reversal	129.1	124.8	4.3	3.4%
Partnership Income Tax	5.0	4.3	0.7	16.8%
Mineral Royalties	10.9	7.5	3.4	44.5%
<b>Total</b>	<b>\$746.7</b>	<b>\$712.0</b>	<b>\$34.6</b>	<b>4.9%</b>

The increase in current year payments reflect the tax due by tax year 2012 extension filers, rather than that of 2013 filers. About three-quarters of total current year payments are received in April, as shown in the following graph:



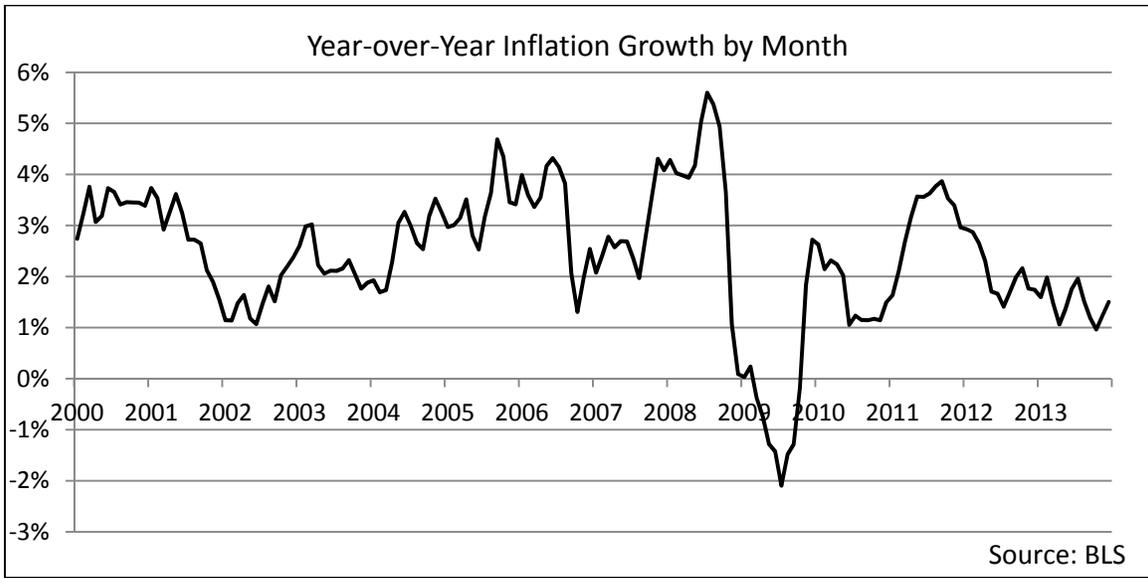
Withholding continues to increase slowly over last year. The graph below illustrates the slow growth when compared to the other post-recession years. The volatility of the first months of the fiscal year is expected; however, by February, the year-over-year growth seems to stabilize. Based on year-to-date revenue, withholding is not likely to attain the 6-8% growth of the last three years.



Withholding tax growth reflects wage growth, while wage growth is a reflection of employment growth and inflation. The chart below shows year-over-year nonfarm payroll employment growth. Note the employment recovery that finally occurred in 2012 and the subsequent slowdown in 2013:



The following chart shows year-over-year growth in inflation, as measured by the CPI. The weakened employment growth as depicted above, combined with the low inflation illustrated below, suggest sluggish wage growth in 2013—and this is likely resulting in the low withholding tax growth.



Although the slow rate of withholding growth is unlikely to bring total FY 2014 collections below the SJ 2 estimate, it will be closely monitored in the coming months. Individual income withholding tax accounts for about a third of all general fund revenue on average.

**Property Tax: Appears Low Due to Missing Payment**

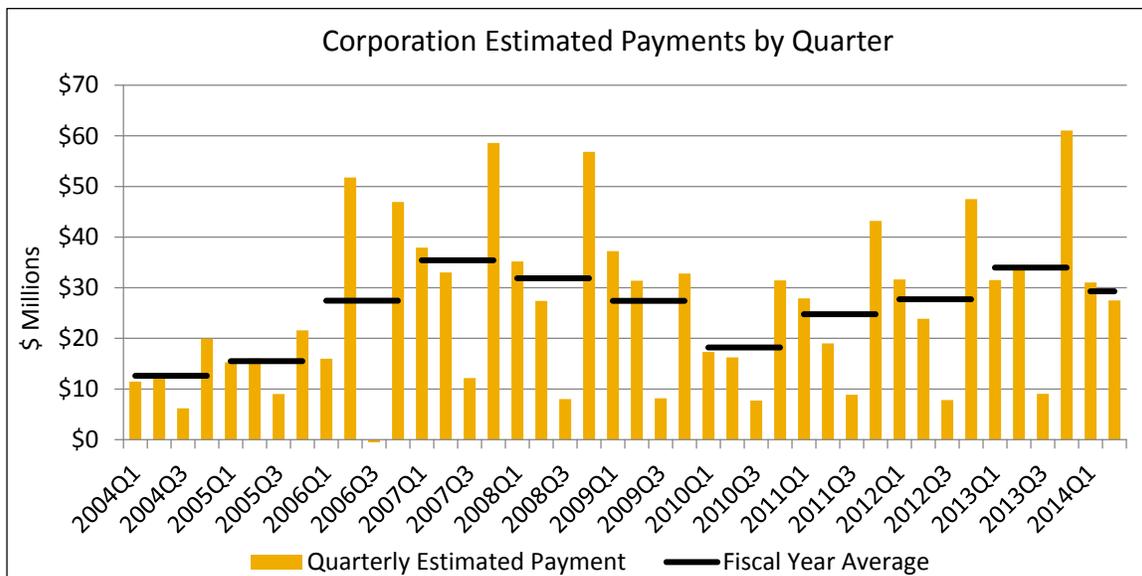
With the first of two property tax payments in, property tax collections are below last year by \$0.8 million or 0.6%. However, property tax revenue from Ravalli County came in late and had not been transferred to the property tax account by the end of February. That payment is approximately \$4.0 million, and shows up in All Other Revenue for this report. This addition puts the collections over the FY 2013 amount, and likely be slightly higher than the SJ 2 estimate.

## Corporation Income Tax: Below Estimate

Corporation income tax collections through the end of February are \$31.6 million or 31.6% below last year. All accounts are contributing to the reduction, as shown in the following table:

Year-to-Date Corporation Income Tax				
(\$ Millions)				
Account	FY 2014	FY 2013	Difference	% Difference
Corporation Tax	\$8.3	\$10.7	(\$2.5)	-22.8%
Estimated Payments	64.1	74.4	(10.3)	-13.8%
Refunds	(14.7)	(10.6)	(4.1)	38.5%
Refund Accrual Reversal	5.6	12.8	(7.2)	-56.0%
Audit, P&I, Amended	5.2	12.8	(7.7)	-59.6%
<b>Total</b>	<b>\$68.5</b>	<b>\$100.1</b>	<b>(\$31.6)</b>	<b>-31.6%</b>

The best indicator for corporation income tax collections is estimated payments, which account for nearly 80% of total corporation tax collections on average. As shown in the chart below, estimated payments have been quite volatile from year-to-year and quarter-to-quarter. Since the low point during FY 2010, estimated payments have (on average) been increasing. FY 2014 estimated payments through the second quarter are somewhat lower than the first two quarters of FY 2013; although it is difficult to infer a conclusive trend, total collections are likely to be below the FY 2013 level and may end up below the SJ 2 estimate.



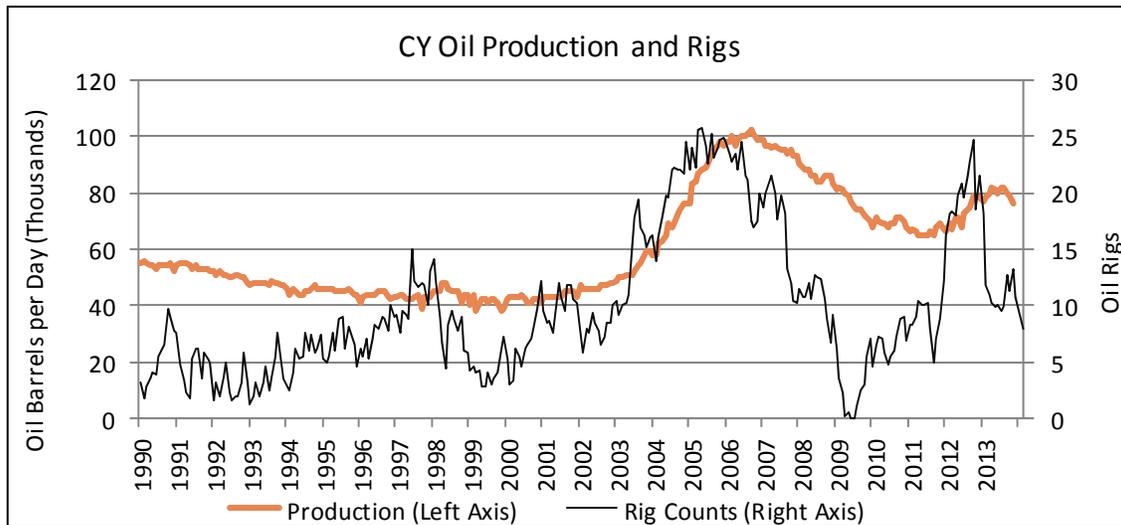
## Vehicle Fees & Taxes: Slightly Below Estimate

Eight months into FY 2014, vehicle taxes and fees have generated \$55.4 million in revenue. This is a 1.2% decrease from this time last year. Given past years' trends, this indicates that year-end revenue will be about \$3.0 million less than what was anticipated in SJ 2.

## Oil & Natural Gas Production Tax: Strong Growth but Production has Slowed

Revenue from the oil and natural gas production tax for the first quarter of FY 2014 was anticipated to be about 20% higher than the first quarter of FY 2013. It ended up being 23% or \$5.5 million higher, for a general fund total of \$29.2 million. Increased production and fairly steady prices since the adoption of SJ 2 are the main reasons for this increase. While only one quarter of data is available, this strong growth in revenue is expected to push oil and natural gas production tax revenue above the SJ 2 estimate. It should be noted however that strong

growth may not continue. Declines have occurred since the last LFC meeting in rigs and production, as shown below:



### **Video Gaming Tax: Slightly Below Estimate**

Revenue from video gambling is 0.8% less than this time last year. Current revenue in FY 2014 generated from video gambling taxes is \$28.0 million, compared to \$28.2 million at this time last year. Using past years' trends, year-end revenue from this source will likely finish around \$3.0 million less than was estimated in SJ 2.

### **Insurance Tax: Slightly Below Estimate, but Expected to Increase**

Current insurance tax collections are 18.2% or \$4.6 million below FY 2013 year-to-date. This is about 2.0% lower than the 15.7% decrease anticipated in SJ 2. The expected decline incorporated into the official SJ 2 estimate for FY 2014 general fund is due to the increased allocation to the Healthy Montana Kids state special revenue fund (increased to 33.3% from 16.7%).

At the time of the estimate, it was not known that Blue Cross Blue Shield (BCBS) would be bought out by Health Care Services Corporation (HCSC) and would be required to pay insurance tax from which it has previously been exempt. According to the State Auditor's Office, these new taxes are expected to start coming in at the end of this quarter. Total insurance tax is anticipated to exceed the SJ 2 estimate once the additional revenue is realized.

## **OTHER KEY DIFFERENCES**

### **U.S. Mineral Royalties: Closer to Estimate with Differences Likely Due to Timing**

U.S. Mineral Royalties came in at \$0.9 million or 6.5% below FY 2013 year-to-date revenues. This is much closer than in December, and similar to the year-to-date difference in January. Staff at the Department of Revenue think there is a timing issue, and total revenue still should end up close to the SJ 2 estimate.

### **Coal Trust Interest Earnings: Below Estimate**

Coal trust interest earnings are currently \$1.8 million, or 14.2% less than this time last year. Estimates contained in SJ 2 predicted that coal trust earnings would remain virtually unchanged from FY 2013 to FY 2014. However, due to the current low yields in the bond market this source will likely finish below the SJ 2 estimate.

## **Liquor Excise and License Taxes: Slightly Below Estimate**

Liquor excise and license taxes are currently 3.0% or \$0.3 million above FY 2013 year-to-date. The SJ 2 estimate indicates an increase of 8.8% or \$1.5 million at fiscal year-end, but based on the pattern of collections seen this fiscal year it is unlikely that total taxes will reach the \$19.3 million expected.

## **All Other Revenue: Stronger-than-Expected Growth**

In SJ 2, revenue from this source was expected to decrease by 11.0% from FY 2013 to FY 2014. However, year-to-date collections for all other revenue are \$7.0 million, or 38.5% larger than this time last year. This difference is expected to decrease by approximately \$4.0 million as this money was from past county collections for Ravalli County. The money was placed in miscellaneous revenue so it could be invested and earn interest. This amount has since been reclassified to the county collection clearing account. The remaining growth is primarily due to increases in abandoned property collections and fund transfers from the Department of Natural Resources and Conservation. These transfers were from the coal shared fund balances that were deposited into the general fund following the close of FY 2013.

## **EXPENDITURES**

At this point in the year, general fund budget pressure is being seen in the two largest general fund spending areas: K-12 education and the Department of Public Health and Human Services (DPHHS). In addition, the Office of the Public Defender has indicated it will seek a transfer of FY 2015 general fund appropriations to FY 2014 to cover projected shortfalls. Several state special revenue accounts are also showing signs that revenues may not meet expectations to fund all appropriations and/or not utilize fund balances.

## **HB 2 ANALYSIS INCLUDING ONE-TIME-ONLY APPROPRIATIONS**

The following table illustrates the HB 2 and related bills (HB 13, HB 377, and HB 454) general fund appropriation authority. For this analysis, both ongoing appropriations of \$1,755.6 million and one-time-only appropriations of \$22.7 million are included. The analysis following the table also includes SB 410, as it is associated with the HB 2 budget.

Staff analyzed the budgets relative to the portion of the fiscal year that has passed. Typically, through February 2014, 61.5% of personal services and 66.7% of other costs would be anticipated to be spent, leaving between 33.3% and 38.5% in remaining authority. Staff reviewed the spending for all agencies in the three main fund types (general fund, state special and federal) and investigated any anomalies. Emphasis was placed on HB 2 general fund, with additional examination of major state special revenue funds and general fund statutory appropriations. The following table compares the HB 2 general fund appropriation for each agency to expenditures through February 28. State special and federal revenue tables can be found in Appendix A.

FY 2014 HB 2 General Fund Spending Through February 28, 2014

Section Agency	Budget	Spending	Balance	% Remaining
A Legislative Branch	\$12,274,326	\$6,966,107	\$5,308,219	43.25%
Governor's Office	6,085,408	3,522,790	2,562,618	42.11%
Commissioner Of Political Practices	603,089	327,018	276,071	45.78%
State Auditor's Office	1,646,660	0	1,646,660	100.00%
Department Of Revenue	51,206,869	30,701,211	20,505,658	40.04%
Department Of Administration	6,449,061	3,754,066	2,694,995	41.79%
Department Of Commerce	6,527,744	2,456,954	4,008,720	61.41%
Department Of Labor & Industry	1,348,216	1,093,282	254,934	18.91%
Department Of Military Affairs	6,147,007	3,952,144	2,194,863	35.71%
A Total	<u>\$92,288,380</u>	<u>\$52,773,573</u>	<u>\$39,452,737</u>	<u>42.75%</u>
B Department of Public Health and Human Services	<u>\$447,180,713</u>	<u>\$265,372,056</u>	<u>\$181,808,258</u>	<u>40.66%</u>
C Department Of Fish, Wildlife & Parks	309,125	127,420	181,705	58.78%
Department Of Environmental Quality	5,358,621	2,800,191	2,558,430	47.74%
Department Of Livestock	1,536,904	872,232	664,672	43.25%
Department Of Natural Resources & Conservation	24,326,428	15,318,402	9,008,026	37.03%
Department Of Agriculture	997,371	554,467	442,904	44.41%
C Total	<u>\$32,528,449</u>	<u>\$19,672,711</u>	<u>\$12,855,738</u>	<u>39.52%</u>
D Judicial Branch	38,387,321	21,730,781	\$16,656,540	43.39%
Crime Control Division	2,376,839	1,444,964	931,875	39.21%
Department Of Justice	30,605,195	18,500,957	12,104,238	39.55%
Office Of The Public Defender	26,963,146	17,287,183	9,675,963	35.89%
Department Of Corrections	181,822,991	104,124,663	77,698,328	42.73%
D Total	<u>\$280,155,492</u>	<u>\$163,088,548</u>	<u>\$117,066,944</u>	<u>41.79%</u>
E Office Of Public Instruction	\$702,734,653	\$423,468,740	\$279,265,913	39.74%
Board Of Public Education	215,614	87,859	127,755	59.25%
Commissioner Of Higher Education	208,757,649	147,686,341	61,071,308	29.25%
School For The Deaf & Blind	6,579,992	3,934,221	2,645,771	40.21%
Montana Arts Council	584,062	330,017	254,045	43.50%
Montana State Library	3,284,828	2,156,339	1,128,489	34.35%
Montana Historical Society	3,610,464	1,874,343	1,736,121	48.09%
E Total	<u>\$925,767,262</u>	<u>\$579,537,860</u>	<u>\$346,229,402</u>	<u>37.40%</u>
	<u>\$1,777,920,296</u>	<u>\$1,080,444,747</u>	<u>\$697,413,078</u>	<u>39.23%</u>

### Agencies with Significant General Fund Appropriations

The following sections highlight the analysis of the agencies with highest general fund appropriation. In addition, any pressure points associated with non-general fund are also discussed.

## ***Office of Public Instruction***

In the previous report, staff outlined that appropriations were anticipated to be \$2.0 million less than anticipated expenditures due to an underestimation of guaranteed tax base aid (GTB) payments during the session. This anticipated shortfall remains.<sup>1</sup>

## ***Department of Public Health and Human Services (DPHHS)***

The budget status report submitted by DPHHS on February 15 continues to show a general fund shortfall in FY 2014. The department now projects a total shortfall of \$9.2 million general fund with \$7.0 million for Medicaid services. The general fund shortfall estimated by DPHHS in the February budget status report is \$1.0 million lower than the amount reported at the December LFC meeting. One of the primary reasons for the change is that DPHHS increased state special revenue from the Healthy Montana Kids account about \$1.5 million and offset some of the general fund spending for Medicaid services. In December, LFD staff had estimated that there would be an additional \$2.6 million available in HMK revenue that could be applied to reduce the general fund cost overrun.

The most significant shortfalls are projected in Medicaid services administered by:

- Health Resources Division - \$4.8 million
  - Medicaid hospital services - \$5.5 million
    - This amount is about \$2.1 million greater than estimated in the December report
    - Ongoing factors related to the projected short fall are higher reimbursement due to more complex patient acuity and an increase in the number of services
- Developmental Services Division - \$1.3 million
  - Children's mental health services - \$1.5 million due to growth in targeted case management services and reductions in prior authorization for utilization of some services
- Senior and Long Term Care Division - \$0.7 million
  - Nursing home services - \$0.8 million due to lower state special revenue collections in the nursing home utilization fee, which shifts costs to the general fund
- Addictive and Mental Disorders Division - \$0.1 million
  - Adult mental health services – \$0.1 million due to growth in case management and physician services

As of the writing of this report the department has not relayed any information on potential mitigation efforts or requested a transfer of funds from FY 2015 to FY 2014.

Staff has identified two primary potential mitigation options, including:

- 1) SB 410 state special revenue appropriated directly to the department as well as to the Governor's Office for distribution to agencies; and

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<sup>1</sup> To reiterate from the last report the reasons for the anticipated shortfall, a portion of the GTB payments are determined based on the district-anticipated funding from both fund balance reappropriated and non-levy revenue. These funds offset state general fund GTB payments and local levies. Any change in this area is shared between state general fund and local levies. State analysts estimate these funding amounts during session and both were overestimated as follows: 1) fund balance re-appropriated (\$5.0 million), which is very volatile and cannot be forecasted with certainty and 2) non-levy revenue (\$2.0 million) from oil and gas. The combined difference between expected and actual is \$7.0 million and resulted in both higher guaranteed tax base aid (GTB) payments from the state to districts and higher local BASE mills.

Two factors were observed in the district oil and gas revenue budgeting in the GTB area:

1. Overall districts budgeted less oil and gas revenue in the district general fund than anticipated.
2. In FY 2014, SB 175 allowed districts to use a portion of the non-levy revenue in the district general fund above BASE for the first time. The fiscal note assumed there would be no impact to the GTB payments from this provision.

The state special revenue funding available for school BASE aid, the guarantee account, is anticipated to be consistent with budgeted levels and are not anticipated to be available to offset this shortfall. In addition, the trigger set forth in SB 175 that would allocate "excess" guarantee account revenue to other school purposes is not expected to be met.

- 2) Federal CHIPRA grant moneys received in excess of anticipated levels.

For further information, see “Medicaid Monitoring Report – March LFC Meeting”.

#### Non-Medicaid Shortfall

In addition, the Disability Employment and Transitions Division (DETD) is currently projecting a shortfall of \$0.3 million in general fund (\$0.7 million total funds) mostly due to increased caseload in the Vocational Rehabilitation and Blind Services (VRB) program. To mitigate the potential shortfall, VRB anticipates entering into an Order of Selection (OOS), essentially a state-wide client waiting list, for the receipt of vocational rehabilitation services in FY 2014. DETD is awaiting federal approval to implement this process. While the shortfall will not increase, DETD cannot yet estimate the impact of the OOS.

#### State Special Revenue

The DPHHS state special revenue (SSR) account fund balances appear adequate to fund appropriations. The exception is nursing home utilization fee revenue, which is about \$0.8 million lower than anticipated, and which shifts Medicaid match from this source to the general fund contributing to the projected general fund shortfalls discussed above.

#### ***Department of Corrections***

At this point, the Department of Corrections appears to have sufficient appropriation authority to meet its obligations for FY 2014. The department has established the \$2.0 million appropriation from SB 410 in the Administrative and Financial Services Division but is still in the process of determining how the funding will be used.

Outside medical costs that caused significant budget challenges in FY 2013 are continuing to run below the same time period as last year. As of January 31 the department had expended 78% of the amount expended over the same period in the previous fiscal year and 67% of the FY 2014 appropriation remains unspent.

#### ***Office of the Commissioner of Higher Education (OCHE)***

The Montana University System (MUS) has significant tools to manage within their budgets due to the funding and budget control retained by the Board of Regents. Budget shortages on campuses are unlikely to directly impact the state budget. However, budget shortfalls, even in non-state areas of the budget, may impact budget policy and development in the next legislative session. The following analysis of the MUS budgets does not reflect immediate state budget impacts, but will likely be part of the budget discussion in the 2015 session.

### The University of Montana (U of M)

The U of M has experienced a shortfall in tuition revenue of \$3.0 million in the fall semester and another \$3.0 million in the spring semester due to declines in enrollment. Approximately \$3.5 million of the FY 2014 shortfall will be covered by adjustments within the general operating fund including savings within utilities, printing, and software purchases. Another \$2.5 million will come from various departments. The deans of the schools have identified a number of recommendations to provide additional savings that are being implemented throughout the spring including a hiring “chill” and restructuring.

In addition the U of M has identified a potential shortfall of up to \$9.0 million for FY 2015. U of M is examining next year’s budget with a conservative approach to crafting the budget.

### Montana State University (MSU)

The MSU research office has identified a \$3.5 million continued shortfall in revenue from scientific research. MSU anticipates the decline in revenues will continue in the short term. Factors include the end of stimulus funding, sequestration, fewer grants being requested, and lower award amounts for grants. University administration has pledged \$2.0 million from the university current unrestricted fund. The remaining reductions of \$1.5 million are being examined by a task force of faculty and staff to provide budget recommendations to solve the remaining \$1.5 million shortfall in FY 2014 and the ongoing shortage in future budget years.

### ***Office of the State Public Defender (OPD)***

On February 24, 2014 OPD indicated it was experiencing a \$2.4 million general fund shortfall in FY 2014 and would utilize three primary funding sources to augment the FY 2014 appropriation: 1) a general fund transfer from the FY 2015 appropriation of \$1.6 million; 2) utilization of \$0.6 million of the Governor’s total \$7.0 million SB 410 appropriation; and 3) utilization of \$0.2 million of the Governor’s HB 13 personal services contingency. Among the costs that are projected to be above budget include:

- Capital crimes where a death penalty sentence is being considered
- Unrealized vacancy savings
- Retirement payouts
- Caseload growth pressures on staff and contractor workloads

### **Other Significant Budget Factors**

The following section discusses other agencies as well as any identified issues or other budget factors not discussed above.

### ***Section A – General Government***

Department of Commerce – The 2013 Legislature eliminated the Energy Promotion Division, funding supporting 5.0 FTE, operating expenses, and related general fund from the Department of Commerce (Commerce) budget. The legislature provided a portion of the funding to support 2.0 FTE and operating costs to the Office of Economic Development in the Governor’s Office for energy promotion. In June 2013 the Governor’s Office transferred the general fund and related positions for this function to the Business Resources Division within Commerce. As of the end of January personal services for this program were 92.3% expended and operating costs were 63.9% expended. Commerce staff indicated that the program retained the 3.0 FTE that were in place at the time the legislature eliminated the program. As a result Commerce will need to use other funds to support the additional FTE costs.

State Auditor – The State Auditor’s Office operates the Insure Montana program, which offers health insurance premium subsidies and tax credits to employers offering health insurance to employees. The 2013 Legislature appropriated \$1.6 million general fund and \$8.1 million state special revenue on a one-time-only basis to fund Insure Montana in FY 2014. As of the February 1 none of the general fund and \$4.0 million of the state special revenue had been expended.

## ***Section C – Natural Resources and Transportation***

Fish, Wildlife, and Parks –With the exception of invasive species activities, the department does not use general fund for operations as it is heavily dependent on the general license account, both for operations costs and as matching funds for federal grants. Traditionally, the department has periodic license rate increases that are designed to collect more money than necessary in the initial years, but that then utilizes the ending fund balance in years when the license revenues are not sufficient on a year to year basis. The department has stated that a rate increase may be requested of the 2015 Legislature. The Environmental Quality Council is currently studying hunting and fishing licensing.

Department of Natural Resources and Conservation (DNRC) –The higher expenditure of general fund shown in the table on page 11 is largely due to the practice of recording some initial fire expenses to the department’s HB 2 general fund appropriation that are periodically transferred to the fire suppression account. As of the writing of this report, the fund has revenues of \$51.7 million, with total anticipated state responsibility expenditures through the end of FY 2014 of \$12.1 million, including \$500,000 of anticipated spring fire costs.

Montana Department of Transportation (MDT) – The highways state special revenue account that, along with matched federal funds, supports most functions of MDT. It is primarily funded from gas, diesel, and GVW taxes and fees.<sup>2</sup> Both expenditures and revenues are in line with anticipated levels, with an anticipated working capital balance at the end of FY 2015 in the restricted portion of the account of \$73.0 million and in the non-restricted portion of \$1.4 million.

### ***SB 410***

SB 410 transferred general fund to provide statutory appropriations of state special revenue for various operational costs for the following state agencies:

- Department of Corrections - \$2.0 million
- DPHHS - \$2.0 million
- Department of Labor and Industry (DOLI) - \$2.0 million
- Governor’s Office - \$7.5 million

Funding provided to the Governor’s Office can be transferred to the following state agencies for operational costs:

- Department of Public Health and Human Services
- Department of Natural Resources
- Department of Environmental Quality
- Department of Administration
- Department of Commerce
- Department of Revenue
- Department of Corrections
- Department of Labor and Industry
- Governor’s Office

Each department included the statutory appropriations within its budgets at the beginning of the biennium. The following table shows the programs, with the budgeted and allocated amounts for FY 2014. It should be noted that DOLI has split its authority between fiscal years with \$1.0 million in FY 2014 and \$1.0 million in FY 2015.

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<sup>2</sup> The fund also supports highways related activities in the Departments of Justice and Fish, Wildlife, and Parks.

SB 410 Appropriations by Program and Fiscal Year				
Agency	Program	FY 2014		Remaining Authority
		Budget	Expended*	
Governor's Office	Office Of Budget And Program Planning	\$7,500,000	\$0	\$7,500,000
Department of Justice	Narcotic Investigations In Eastern Montana	0	497,546	7,002,454
Office of the Public Defender	Offset Budget Overruns	0	625,000	6,377,454
Department of Corrections	Administration And Support Services	2,000,000	0	2,000,000
Department of Labor and Industry	Workforce Services Division	825,000	333,913	491,087
	Employment Relations Division	125,000	27,295	97,705
	Office Of Community Services	50,000	27,514	22,486
Department of Public Health and Human Services	Director's Office	2,000,000	0	2,000,000
		<u>\$12,500,000</u>	<u>\$1,511,268</u>	<u>\$10,988,732</u>

\* The Department of Justice has received an administrative appropriation from the Governor's Office but has not yet spent the funds, the Office of the Public Defender has indicated they will be receiving \$0.6 million from the Governor's Office for budget overruns.

Two of the agencies that would receive a portion of the Governor's funds – the Department of Justice and the Office of the Public Defender – are not on the list of agencies to which the Governor may transfer funds. According to the Governor's Office, they are providing those funds for the following reasons:

- o Department of Justice – the Governor's Office is contracting with the department to provide for additional narcotic investigation work in eastern Montana
- o Office of the Public Defender – The office is administratively attached to the Department of Administration, which is on the list

Julie Johnson, attorney with the Legislative Services Division, provided the following preliminary thoughts on both uses:

“While OPD may be administratively attached to DOA as a number of other agencies are (including PERS, MSF, TRS) OPD is not identified in SB 410. There is no precedent for treating funds transferrable to DOA as also being transferrable any of the agencies administratively attached to it. HB 2 separately identifies funds appropriated to DOA and OPD.

“DOJ is not identified in SB 410 either. The argument that the Governor's Office is contracting with DOJ to perform services for the Governor's Office would allow the Governor's Office to contract with any state agency to do any work. I do not believe this carte blanche authority to transfer to any and all agencies for any services is what was intended by the Legislature in passing this bill.”

***Public Employee Retirement System Statutory Transfers***

The current estimated transfers from the general fund to the Public Employee Retirement System are \$6.8 million lower for the biennium than anticipated during session due to current estimates of coal severance tax and coal interest income lower than SJ 2 forecast. Two factors contribute to this reduction:

- o Coal Severance Taxes: After the disposal of coal severance taxes pursuant to MCA 15-35-108(1) through MCA 15-35-108(8), approximately 24% of the total severance tax is left to be allocated to the general fund and statutorily appropriated to the public employees' retirement system. Given past coal severance tax trends, this amount is projected to be \$13.6 million dollars for FY 2014 or \$1.3 million less than SJ 2.
- o Interest income from the coal permanent trust is also allocated to the pension system pursuant to MCA 15-35-108(9)(b)(v). Total coal interest income deposited into the general fund is currently projected to be \$21.4 million. Assuming all other allocations under subsection (9)(b) are made first, \$18.3 million would transfer to the pension system or \$2.7 million less than the \$21 million anticipated.

The total of the two for FY 2014 is \$31.9 million or \$4.0 million less than the FY 2014 estimated transfer. The updated transfer estimate for FY 2015 is \$2.8 million less than anticipated for a total biennial reduction of \$6.8 million in the transfer to the public employees' retirement system.

## Statutory Appropriations

Statutory appropriations are those appropriations that are contained in the Montana Code Annotated to be established each year based on specific criteria in law. Spending is capped by the law establishing the appropriation and not through a legislative appropriation in the general appropriations act (HB 2). These appropriations are established on the SABHRS accounting system as needed by the executive and can be adjusted at any time in the fiscal year. Likewise, the executive establishes the Governor's emergency appropriations as needed.

FY 2014 Statutory General Fund Through February 28, 2014					
Section/Agency	Budget	Expenditures	Balance	% Remaining	
A Governor's Emergency Appropriations	\$8,250,000	\$332,864	\$7,917,136	95.97%	
State Auditor's Office	27,999,539	0	27,999,539	100.00%	
Department of Revenue	118,249,854	55,472,248	62,777,606	53.09%	
Department of Administration	98,844,167	69,855,852	28,988,316	29.33%	
Department of Commerce	<u>2,376,172</u>	<u>1,803,760</u>	<u>572,412</u>	<u>24.09%</u>	
A Total	255,719,732	127,464,724	128,255,008	50.15%	
C Department of Agriculture	690,000	318,505	371,495	53.84%	
D Department of Justice	4,568,241	2,982,012	1,586,230	34.72%	
E Commissioner of Higher Education	<u>1,360,541</u>	<u>825,896</u>	<u>534,645</u>	39.30%	
Grand Total*	<u>\$262,338,514</u>	<u>\$131,591,136</u>	<u>\$130,747,378</u>	49.84%	
*Total Statutory appropriations do not tie to Figure 1 since these levels reflect the amount of statutory appropriation levels established on SABHRS as of February 28, 2014 by the executive, plus half of the biennial emergency appropriation level. Figure 1 reflects LFD estimates of the final spending of the same.					

### ***Department of Administration (DOA)***

The primary statutory appropriations in DOA are for debt service and pension contributions on behalf of local governments. Two factors make the year to date spending appear higher: 1) the debt service payments are primarily paid in August; and 2) HB 377 required a payment of \$25 million to the Teachers' Retirement System which occurred in July.

### ***Department of Revenue***

The Department of Revenue statutory appropriations are primarily the entitlement share payments made to local governments. These payments are distributed in four installments and two quarters were paid as of February 28, 2014.

### ***Department of Commerce (Commerce)***

The statutory appropriations in Commerce include a \$1.275 million transfer to the research and commercialization account that was fully transferred at the beginning of the fiscal year and causes the percent remaining to be low.

## APPENDIX A

FY 2014 HB 2 State Special Revenue Spending Through February 28, 2014					
Section	Agency	Budget	Spending	Balance	% Remaining
A	Legislative Branch	\$2,573,718	\$1,205,735	\$1,367,983	53.15%
	Consumer Council	1,656,583	688,151	968,432	58.46%
	Governor's Office	8,409	0	8,409	100.00%
	State Auditor's Office	17,976,586	9,019,012	8,957,574	49.83%
	Department Of Revenue	1,120,063	578,634	541,429	48.34%
	Department Of Administration	6,139,622	3,454,547	2,685,075	43.73%
	Department Of Commerce	7,503,747	880,522	6,623,225	88.27%
	Department Of Labor & Industry	40,744,061	24,961,979	15,782,082	38.73%
	Department Of Military Affairs	<u>1,120,363</u>	<u>139,738</u>	<u>980,625</u>	<u>87.53%</u>
A	Total	<u>\$78,843,152</u>	<u>\$40,928,318</u>	<u>\$37,914,834</u>	<u>48.09%</u>
B	Department of Public Health and Human Services	<u>\$154,036,333</u>	<u>\$80,648,746</u>	<u>\$73,387,587</u>	<u>47.64%</u>
C	Department Of Fish, Wildlife & Parks	\$57,984,680	\$32,375,114	\$25,609,566	44.17%
	Department Of Environmental Quality	32,699,477	15,091,340	17,608,137	53.85%
	Department Of Transportation	249,491,549	145,300,912	104,190,637	41.76%
	Department Of Livestock	7,721,721	4,753,352	2,968,369	38.44%
	Department Of Natural Resources & Conservation	34,928,228	13,896,796	21,031,432	60.21%
	Department Of Agriculture	<u>13,817,392</u>	<u>6,255,974</u>	<u>7,561,418</u>	<u>54.72%</u>
C	Total	<u>\$396,643,047</u>	<u>\$217,673,487</u>	<u>\$178,969,560</u>	<u>45.12%</u>
D	Judicial Branch	\$2,559,834	\$1,413,461	\$1,146,373	44.78%
	Crime Control Division	236,806	62,451	174,355	73.63%
	Department Of Justice	54,354,449	31,910,973	22,443,476	41.29%
	Public Service Regulation	3,761,309	2,117,194	1,644,115	43.71%
	Office Of The Public Defender	281,544	166,432	115,112	40.89%
	Department Of Corrections	<u>5,925,529</u>	<u>2,377,908</u>	<u>3,547,621</u>	<u>59.87%</u>
D	Total	<u>\$67,119,471</u>	<u>\$38,048,420</u>	<u>\$29,071,052</u>	<u>43.31%</u>
E	Office Of Public Instruction	\$10,598,368	\$89,236	\$10,509,132	99.16%
	Board Of Public Education	171,810	87,649	84,162	48.99%
	Commissioner Of Higher Education	20,792,759	10,727,946	10,064,813	48.41%
	School For The Deaf & Blind	263,080	77,214	185,866	70.65%
	Montana Arts Council	223,492	119,402	104,090	46.57%
	Montana State Library	1,801,798	1,157,482	644,316	35.76%
	Montana Historical Society	712,724	382,504	330,220	46.33%
E	Total	<u>\$34,564,031</u>	<u>\$12,641,432</u>	<u>\$21,922,599</u>	<u>63.43%</u>
		<u>\$731,206,034</u>	<u>\$389,940,403</u>	<u>\$341,265,632</u>	<u>46.67%</u>

FY 2014 HB 2 Federal Revenue Spending Through February 28, 2014

Section	Agency	Budget	Spending	Balance	% Remaining
A	Secretary Of State's Office	\$128,000	\$52,238	\$75,762	59.19%
	Department Of Revenue	257,449	163,609	93,840	36.45%
	Department Of Administration	947,529	3,246	944,283	99.66%
	Department Of Commerce	17,613,162	2,483,900	15,129,262	85.90%
	Department Of Labor & Industry	37,273,751	16,229,462	21,044,289	56.46%
	Department Of Military Affairs	<u>37,746,089</u>	<u>17,354,433</u>	<u>20,391,656</u>	<u>54.02%</u>
A	Total	<u>\$93,965,980</u>	<u>\$36,286,889</u>	<u>\$57,679,091</u>	<u>61.38%</u>
B	Department of Public Health and Human Services	<u>\$1,325,705,560</u>	<u>\$743,993,153</u>	<u>\$581,712,407</u>	<u>43.88%</u>
C	Department Of Fish, Wildlife & Parks	\$19,525,151	\$10,961,622	\$8,563,529	43.86%
	Department Of Environmental Quality	20,329,768	10,005,199	10,324,569	50.79%
	Department Of Transportation	430,162,878	244,730,045	185,432,833	43.11%
	Department Of Livestock	1,429,924	741,192	688,732	48.17%
	Department Of Natural Resources & Conservation	2,010,224	1,040,537	969,687	48.24%
	Department Of Agriculture	<u>2,104,443</u>	<u>512,852</u>	<u>1,591,591</u>	<u>75.63%</u>
C	Total	<u>\$475,562,388</u>	<u>\$267,991,446</u>	<u>\$207,570,942</u>	<u>43.65%</u>
D	Judicial Branch	\$123,002	\$51,956	\$71,047	57.76%
	Crime Control Division	9,723,575	3,076,640	6,646,936	68.36%
	Department Of Justice	1,120,160	555,100	565,060	50.44%
	Public Service Regulation	73,334	73,334	0	0.00%
	Department Of Corrections	<u>16,005</u>	<u>240</u>	<u>15,765</u>	<u>98.50%</u>
D	Total	<u>\$11,056,076</u>	<u>\$3,757,269</u>	<u>\$7,298,807</u>	<u>66.02%</u>
E	Office Of Public Instruction	\$174,419,827	\$85,668,927	\$88,750,900	50.88%
	Commissioner Of Higher Education	57,407,158	30,245,207	27,161,951	47.31%
	School For The Deaf & Blind	71,760	12,069	59,691	83.18%
	Montana Arts Council	709,793	644,433	65,360	9.21%
	Montana State Library	1,664,665	596,609	1,068,056	64.16%
	Montana Historical Society	<u>742,841</u>	<u>467,118</u>	<u>275,723</u>	<u>37.12%</u>
E	Total	<u>\$235,016,044</u>	<u>\$117,634,363</u>	<u>\$117,381,681</u>	<u>49.95%</u>
		<u>\$2,141,306,049</u>	<u>\$1,169,663,121</u>	<u>\$971,642,928</u>	<u>45.38%</u>