OTHER FISCAL ISSUES

INTRODUCTION TO OTHER FISCAL ISSUES

This section discusses several fiscal issues not directly related to the Executive Budget, but that will potentially have an impact on the budget passed by the legislature and/or the budget process. The purpose of this section is to provide legislators with an overview of each of these issues. The issues discussed in this section are listed below and are discussed in more detail in the pages that follow.

- ?? **Tax Policy Initiatives – Non-Executive.** There are proposals for tax reform that are not in the Executive Budget, that address income tax, local government funding, and court funding.
- ?? **Tobacco Settlement Funds.** The state expects to receive $63.5 million in the 2003 biennium, at least 40 percent of which will be deposited into a trust.
- ?? **Montana Power Sales – Revenue Impact.** The Montana Power Company is in the process of selling off its energy businesses, including its utility, as it changes its focus to its telecommunications subsidiary. It expects to complete the sale in the first half of 2001.
- ?? **Mental Health Services: Interim Study.** The Legislative Finance Committee has proposed a number of bills to implement recommendations of the HJR 35 subcommittee.
- ?? **Earmarked Revenues/Statutory Appropriations: Interim Study.** The Legislative Finance Committee performed a review and recommended changes of certain dedicated revenues and statutory appropriations.
- ?? **Fund Balance Adequacy/Reserves.** The legislature will again need to determine what amount of ending fund balance is sufficient to ensure budget stability, particularly as Montana's economic outlook has become so fraught with uncertainty.
- ?? **HB 64: 15 Percent Budget Reduction Options.** This is the first Executive Budget that includes a new requirement of base reduction options as part of the budget submission.
- ?? **Unified Computer Budget.** HB 2 of the 1999 session directed OBPP to submit information technology actual expenditures and budget requests in a consolidated presentation. This information will be reviewed by a select committee at the beginning of the session.
- ?? **Information Technology Governance.** The Legislative Finance Committee, through an interim study, recommended creation of a Department of Information Technology.
- ?? **Other Major Funds**
  - ✍ **Highway Special Revenue Account.** The 2001 legislature is faced with a declining working capital balance in the highways state special revenue account.
  - ✍ **Resource Indemnity Account.** Of seven accounts that have historically received portions of RIT allocations or interest earnings, four are projected to have negative balances by the end of the 2003 biennium.

TAX POLICY INITIATIVES – NON EXECUTIVE

INCOME TAX PROPOSAL – REVENUE AND TAXATION COMMITTEE

The Revenue and Taxation Committee has approved a committee bill to simplify the state personal income tax. The committee identified Montana's high marginal rate of 11 percent as a disincentive to economic development. The proposal would:

- ?? make the tax base equal to federal taxable income, subject to adjustments,
- ?? provide additions to income for:
  - ✍ early withdrawal of funds from medical savings accounts, family education savings accounts, and first-time homebuyers accounts;
  - ✍ non-Montana local bonds; and

Provide exemptions to income for:

- ?? interest on U.S. Government bonds;
- ?? native American income earned on a reservation;
- ?? retirement income, phased-out at levels higher than $60,000;
- ?? active duty military income;
- ?? tip and unemployment income;
- ?? medical savings account contributions;
- ?? family educations savings account contributions;
- ?? first-time homebuyers account contributions; and
- ?? regular and long term medical care insurance premiums

The proposal reduces the number of tax rate brackets to four, as shown in Figure 1.

The income bracket boundaries for married joint filings are twice those for single filers and married single filers. Head of household brackets are set at 80 percent of the married joint filing brackets. All households filing a married joint return at the federal level would be required to file a married joint return under the proposed changes to state income tax laws. The income brackets would be adjusted for inflation. Because the tax base is equal to federal taxable income which has no deduction of federal taxes paid during the tax year, the proposed Montana taxable income would also not allow for deduction of federal taxes paid. Existing state income tax credits would be continued. The proposed law would become effective January 1, 2002. It is estimated that the proposed law would reduce revenues to the general fund by $6.2 million in fiscal 2003.

Figure 1
Tie to Federal Taxable Income
Proposed Law Tax Rates

If MT Taxable Income is over	but not over	Multiply by	and substract
Married Joint			
$0	$6,000	4.0%	$0
$6,000	$41,000	5.0%	$60
$41,000	$125,000	6.0%	$470
$125,000	Unlimited	6.6%	$1,220
Head of Household			
$0	$4,800	4.0%	$0
$4,800	$32,800	5.0%	$48
$32,800	$100,000	6.0%	$376
$100,000	Unlimited	6.6%	$976
Single Filers			
$0	$3,000	4.0%	$0
$3,000	$20,500	5.0%	$30
$20,500	$62,500	6.0%	$235
$62,500	Unlimited	6.6%	$610
Married Separate			
$0	$3,000	4.0%	$0
$3,000	$20,500	5.0%	$30
$20,500	$62,500	6.0%	$235
$62,500	Unlimited	6.6%	$610

LOCAL GOVERNMENT STRUCTURE AND FUNDING COMMITTEE

SB 184, passed by the 1999 legislature, created an interim committee to study the funding and structure of local governments. The committee contained ten members including two senators, two representatives, a city manager, a city councilman, two county commissioners, a county treasurer, and the director of the Department of Revenue.

The committee developed the following goals:

1. Simplify billing, collection, accounting, distribution and reporting of all revenue.

2. De-earmark revenue and eliminate expenditure mandates for local government.
3. Create a rational, dependable, stable funding structure for cities and counties.

The committee met several times, received testimony from county, city and school representatives and the public. The committee will propose 6 pieces of legislation:

1. A proposal to change the flow of revenue between state, local governments, and schools and create an entitlement share program to make local governments and school districts whole;
2. A proposal to change the budgeting and accounting laws;
3. A proposal to extend earmarking laws to local governments;
4. A proposal to establish a local option sales tax;
5. A proposal to establish a local option realty tax; and
6. A proposal to establish a state and local relationship committee

The goal of the committee was to make the financial impacts on state and local government balance sheets neutral. The committee estimated the impacts shown in Figure 2.

Figure 2
Impact of Local Government Proposal
on State and Local Governments
Annual, in Millions

Government Account	State General Fund	State Special Revenue	Local Governments
Revenue Impacts	$ 155.0	$ (20.7)	$ (199.1)
HB2 Sate Expenditure Impacts	(49.1)	14.3	-
Statutory Appropriations	(24.1)	6.4	82.4
Local Cost Savings			34.8
Local Entitlements	(81.8)	-	81.8
Total	$ -	$ -	$ -

Notes:-------------------------------------

--Based on Nov 3, 2000 publication of Local Government Funding and Structure Committee; based on fiscal 2001 numbers. Schools are in Local Governments.

-- Tax Revenue lost to local government is in text. Revenue gain to general fund is same but includes 9 mill revenue and excludes property tax reimbursements. Revenue loss to state special accounts include 9 mill revenue, vehicle fees and licenses and other fees.

-- HB2 - increased state expenditures on district court and welfare programs.

-- Increased Statutory Appropriations are made to state special accounts, TIF's, school districts and county education funds for two years. SA savings are HB20 reimbursements and SB184 reimbursements.

-- Local cost savings are due to state assuming costs for district courts and welfare

-- Local Entitlements are ongoing statutory appropriations to counties and cities.

State and Local Revenue Changes

Beginning in fiscal 2002, the proposal with the largest funding impact reallocates revenue received by local governments, and school districts, and some state special revenue accounts to the general fund. The proposal replaces foregone revenue with state entitlement grants out of the state general fund. The revenue sources which local governments and school districts (and some state special revenue accounts) would relinquish are as follows:

- ?? Motor vehicle registration fees, but not local option vehicle taxes or GVW fees;
- ?? Vehicle license fees;
- ?? Petition for adoption fee
- ?? Dissolution of marriage fee
- ?? Gaming revenue;
- ?? District court fines and forfeitures;
- ?? Financial institutions tax;
- ?? Federal Taylor Grazing revenue;
- ?? Aeronautics fee;
- ?? State land payments in lieu of taxes;
- ?? Department of Fish, Wildlife and Parks payments in lieu of taxes;
- ?? Alcohol related taxes;
- ?? All state personal property tax reimbursements; and
- ?? 9-mill levy revenues

Except for personal property reimbursements, these revenues would be deposited in the state general fund.

Personal property tax reimbursement revenues lost by local governments and school districts would become a cost savings to the state general fund. Major tax sources for which the present law allocation would remain in force include federal forest revenues and natural resource revenue which the state and local governments would continue sharing. All non-levy revenue associated with the 6-mill levy would be deposited in the general fund. All fees and other revenue collected at the local level for local use would remain at the local level.

For fiscal 2001, the committee estimated that the revenue reductions to local government and school districts would be $200.0 million. 67.4 percent would be borne by counties, cities and towns, and tax increment financing districts (TIF's) and the remaining revenue loss would be borne by school districts. This amount does not include the state special revenue account losses of $6.4 million.

Counties would have two functions replaced by state funding, thus reducing in part local revenue requirements. The state would take over funding of almost all functions performed by district courts (except for clerk of court) and by county welfare and protective services programs. The committee estimated that for fiscal 2001, counties would save $34.8 million in costs associated with these programs and the state would experience a like amount in increased spending obligations to fund district courts and local welfare programs.

The state would replace the net revenue losses borne by counties, cities, and miscellaneous taxing districts by establishing for each jurisdiction an entitlement share. Each jurisdiction's entitlement share would be the sum of net revenue bst in that jurisdiction in the base year as calculated by the Department of Revenue. The revenue loss borne by state special accounts, TIF's, school districts, county transportation funds, and county retirement funds would be made up by the state through statutory appropriations or block grants with a statutory life of two years. The calculation of the block grants would be the same as for the entitlement shares for counties and cities. The Office of Public Instruction would disperse the block grants to the school related accounts at the district and county levels.

The entitlement share to counties and cities would be a statutory appropriation from the general fund to the local jurisdiction. Once the base amount is known, the entitlement share would be increased each year by an inflation adjustment.

The proposal would also change the property tax limits for each local government. Under current law, each local government may not levy more property taxes than in the prior year, unless the revenue is attributable to newly taxable property. Under the proposal, the following would be allowed:

?? A provisional limit for fiscal 2002 to provide at least 2 percent growth in the total of property tax and entitlement share revenue;
?? Establishment of a long term property tax limit calculated as the fiscal 2002 amount of property tax assessed plus a growth factor of ½ of the last three year average rate of inflation;
?? Preserve the right of local governments to use the full property tax limit without using it every year;
?? Clarify the definition of "newly taxable property; and
?? Eliminate all local mill levy caps (except for 2-mill emergency levy).

Budgeting and Accounting Changes

The committee also proposed several additions and changes to laws regarding local government budgets and accounting. Most of the changes increase local government flexibility. Some changes require local governments to follow more uniform accounting standards. The proposal extends and strengthens the Department of Commerce's reporting and audit responsibilities.

Earmarking and Mandate Guidelines

This proposal establishes guidelines for earmarking revenue to local government and a process to continuously review earmarked revenue by the Legislative Finance Committee. The proposal also clarifies the process of establishing and funding state mandates for local government.

Local Option Sales Taxes

This proposal authorizes a local option sales tax not to exceed 4 percent on the same goods as the existing statute governing resort taxation (7-6-1501, MCA). In addition, the resort tax is expanded to include the taxation of tourism related services. Any municipality or county may impose the local option sales tax, subject to approval by the voters. If the tax is imposed by a county, 50 percent of the revenue is divided between the county and its municipalities based on population ratios, and 50 percent must be distributed based on the origin of the transaction. If the tax is imposed by Billings, Bozeman, Butte, Great Falls, Helena, Kalispell or Missoula, or the counties in which each of these cities is located, then 25 percent of the local option tax revenue must be remitted to the Department of Revenue for redistribution. The department would distribute these monies to each county, city and town (except the large trade center cities listed above) based on the ratio of the population of the jurisdiction to the total population of the state, unless that jurisdiction has its own local option sales tax.

Local Option Realty Transfer Tax

This proposal authorizes counties or municipalities to impose a local option realty transfer tax up to 1 percent on the sale and transfer of real estate, excluding agricultural land, government property, and certain other transfers. The tax must be approved by voters and may only be used by the governing entity for infrastructure. The taxing jurisdiction imposing the tax would retain 80 percent, and must forward the remainder to the state, where it would be deposited in the treasure state endowment special revenue account.

State Local Government Relationship Committee

This proposal would create a four year state and local government relationship committee, composed of four Senators, four Representatives, three representatives of county government, two representatives of city governments, one representative from K-12 education, and one nonvoting member each from the Departments of Revenue and Commerce. The committee would be staffed by the Legislative Services Division. The purpose of the committee would be to provide oversight of state and local government relations, and produce recommendations to further streamline and rationalize revenue flows and simplify administrative practices.

DISTRICT COURT FUNDING AND STRUCTURE COMMITTEE

The interim committee on district court funding and structure will recommend that the state take over almost all functions of all district courts in the state, beginning in fiscal 2002. Only the duties of the district clerk of court and staff will remain local responsibilities. All other district court personnel would become state employees. The state general fund would receive $6.2 million per year in motor vehicle fees that currently are allocated to the district court special revenue account. In addition, nearly $1.9 million in district court fines and forfeitures would be deposited in the general fund. The committee estimated that the state's district court costs would increase by $23.1 million in fiscal 2002 and by $24.4 million in fiscal 2003.

The net cost to the state would be offset by proposals made by the local government funding and structure committee. If that legislation passes, the net cost to the state general fund would be an increase of $1.7 million in fiscal 2002 and $2.3 million in fiscal 2003. These increases are due to increases in salaries for the new state employees and higher costs anticipated for equipment.

TOBACCO SETTLEMENT

Montana receives revenue as a settling party to a Master Settlement Agreement with four original tobacco companies and 19 subsequent companies, thus ending a four-year legal battle that included 46 states, Puerto Rico, American Samoa, the U.S. Virgin Islands, the North Mariana Island, Guam and the District of Columbia. All told, there were 52 total settling entities. Montana is eligible for four types of payment: 1) reimbursement for legal costs (received December 1999); 2) five initial payments (two received in fiscal 2000 with an additional one per year expected in fiscal 2001, 2002, and 2003); 3) on-going annual payments; and 4) strategic contribution payments (from fiscal 2008 through 2017). The Master Settlement Agreement places no restrictions on how the money is to be spent.

REVENUE

The total amount of tobacco settlement funds available to Montana may be affected by a number of adjustments.

Figure 3
Tobacco Settlement Revenue

Fiscal Year Year	Initial Payment	Annual Payment	Legal Costs	Total
2000 Actual	$19,622,462	$15,138,724	$43,225	$34,804,411
2001 Estimate	9,099,634	17,029,269		26,128,903
2002 Estimate	9,219,820	22,321,091		31,540,911
2003 Estimate	9,325,903	22,586,519		31,912,422

The two most important are the adjustments for inflations and volume of cigarettes shipped nationally. The amount of Montana's share will increase if inflation is positive and decrease with deflation. The amount will also decrease if the number of cigarettes shipped nationally decreases and will increase if the number increases. Figure 3 shows the revenue Montana has received in fiscal 2000 and the amounts to be received through the fiscal 2003 as estimated by the Revenue and Taxation Committee.

DISTRIBUTION

In fiscal 2000, the revenue received from the Master Settlement Agreement was deposited to the general fund. However, due to passage of Montana Constitutional Amendment 35 by the electorate in November 2000, beginning in January 2001, the legislature is required to dedicate not less than 40 percent of tobacco settlement money to a permanent trust fund. The remainder of the money will continue to be deposited into the general fund.

Since the legislature has not yet determined the exact percentage to be distributed to the trust fund, the revenue estimate assumes 40 percent. Figure 4 shows the amounts estimated to be distributed between the general fund and the trust fund through fiscal 2003.

As stipulated in the new constitutional amendment, interest earnings from the trust fund are to be distributed: 1) 90 percent for appropriation by the legislature for disease prevention programs and state programs providing benefits, services, or coverage related to the health care needs of the people of Montana; and 2) 10 percent to the trust. Money in the trust fund can be spent if approved by 2/3 of each house of the legislature. Appropriations of principal, income, or interest from the trust fund cannot be used to replace state or federal money that support tobacco disease prevention programs that existed on December 31, 1999.

Figure 4
Tobacco Settlement Revenue Distribution

Fiscal Year	General Fund 60%	Trust Fund 40%	Total	Trust Interest Earnings 90 Percent	10 Percent	Total
2000 Actual	$34,804,411	$0	$34,804,411			
2001 Estimate	15,677,342	10,451,561	26,128,903	$452,946	$50,327	$503.273
2002 Estimate	18,924,547	12,616,364	31,540,911	1,241,879	137,987	1.379.866
2003 Estimate	19,147,453	12,764,969	31,912,422	2,083,744	231,527	2,315,271

MONTANA POWER SALES – REVENUE IMPACT

On March 28th, 2000, the Montana Power Company (MPC) announced that it would divest itself of all energy businesses, including its utility, and invest the proceeds in telecommunications under its subsidiary, Touch America. Once the sale of the utility business is complete, the Montana Power Company will ask its investors to allow its subsidiary, Touch America, to become the parent corporation.

On August 28th, 2000, MPC announced the sale of its oil and gas properties to PanCanadian Petroleum Limited of Calgary for $475 million. Though some of these properties are in Montana, many are in other states and Canada. This sale was completed on October 31, 2000.

On September 15th, MPC announced the sale of its coal properties to Westmoreland Coal Company of Colorado Springs for $138 million in cash. The properties include a mine and a coal enhancement plant in Rosebud County, Montana, and a mine in Texas. The sale is expected to be complete sometime during the first quarter of calendar 2001.

On September 20, 2000, MPC announced the sale of its subsidiary Continental Energy and its power assets to BBI Power Corporation of Maryland for $84.5 million in cash. The properties include seven electrical generating plants, nationally and in foreign countries. Also transferred is a 500 megawatt plant under development outside of Butte, Montana. The sale is expected to be completed sometime during the first quarter of calendar 2001.

On October 2, 2000, MPC announced the sale of its electric and natural gas utility business to Northwestern Corporation of South Dakota for approximately $1.1 billion. The assets transferred include MPC's electrical, natural gas transmission and distribution assets, as well as MPC's lease interest in Colstrip 4. Northwestern is expected to accept the contracts MPC has made with qualifying facilities. MPC will also transfer $488 million in existing Montana Power debt. The net cash payment to MPC will be in the range of $611 million. MPC has stated that it expects the sale to be complete during the first half of calendar 2001.

The announced total of these sales is $1.8 billion, with a cash total of around $1.3 billion. MPC has not announced the federal or state corporation capital gains tax liability that will be associated with the sale of these properties. Whatever the amount of the tax liability, three of the sales will probably be complete before the end of the first quarter of calendar 2001, thus producing a tax liability to state and federal governments in fiscal 2001.

The timing of the fourth sale, the utility business, is much less certain. The sale requires approval by the Federal Energy Regulatory Commission (FERC) and of the buyer by the Montana Public Service Commission (PSC).

A factor that may delay the utility sale is the recent Supreme Court case involving MPC and the PSC. The PSC had scheduled initial hearings on the request for sale in October 2000, but the hearings were deferred until resolution of *Montana Power Company vs. Montana Public Service Commission* before the Montana Supreme Court. The case appeals a district court judgment in favor of Montana Power Company. The issue applies to methodology used to calculate the transition costs associated with transition to deregulation of the power generation industry in Montana as authorized in SB390 and passed by the 1997 legislature. The initial suit in district court was brought by MPC against the PSC in the spring of 2000, after the PSC denied legality of MPC's proposed transition cost methodology in January 2000. This methodology was based on the future tracking of several classes of transition costs over an indefinite period of time.

The district court found that denial by the PSC of MPC's transition methodology was a "regulatory taking" of its property under US and State Constitutions. The district court found that because the statute created in SB 390 did not exclude the tracking methodology for recovering transition costs, the denial exceeded the PSC's authority. The PSC asserts that: 1) state law requires a final settlement of the net verifiable costs of transition by a certain date; 2) the methodology proposed by MPC would not allow netting the benefits of transition with the costs; and 3) the district court erred in failing to defer to the expertise of the PSC in interpreting a statute administered by the PSC.

In summary, the sale of the four MPC properties may generate additional capital gains tax revenues for Montana. The amount of the additional revenue and timing of the sale of MPC's utility property is uncertain. The general fund revenue estimates, as adopted by the Revenue and Taxation Committee for the 2003 biennium, do not contain the fiscal impact of the MPC sales.

INTERIM STUDY OF PUBLIC MENTAL HEALTH SERVICES

The 1999 legislature passed House Joint Resolution 35 (HJR 35) directing an interim study of public mental health services. The study was undertaken by a subcommittee of the Legislative Finance Committee (LFC) with membership drawn from: 1) the LFC; 2) the Interim Committee on Children, Families Health and Human Services; and 3) the Legislative Audit Committee.

SUMMARY OF LFC RECOMMENDATIONS

The LFC:

- Recommended adoption of six bills, as summarized in the narrative below;
- Requested that the Health and Human Services Joint Appropriation Subcommittee consider

several issues relative to public mental health services expenditures and budgets; and

?? Requested that the Legislative Audit Committee undertake a performance audit of DPHHS internal management processes in order to ensure compliance with federal criteria in the administration of programs funded by Medicaid.

PROPOSED LEGISLATION

The six bills recommended by the LFC are summarized as follows.

LC0369 is an act revising the laws relating to the public mental health system and managed care. This bill:

?? Rescinds requirements that DPHHS incrementally implement mental health managed care and retain a mental health managed care consultant;

?? Changes the definition of the managed care community network to clarify what type of contracts and services constitute managed care;

?? Removes the requirement that a Medicaid-managed health care entity be subject to licensure and financial solvency provisions of the insurance code;

?? Requires that a Medicaid-managed care contractor demonstrate to the Insurance Commission that it can bear the level of financial risk under a managed care contract prior to DPHHS entering into the contract;

?? Changes existing statutory requirements for a system of integrated health care services from passive to active voice; and

?? Moves the authority for a mental health services program for persons ineligible for Medicaid to a section of statute separate from the Medicaid statutes.

LC0368 is an act defining professional persons, to include advanced practice registered nurses, and providing that advanced practice registered nurses have certain rights and responsibilities similar to physicians. This bill:

?? Includes advanced practice registered nurses with a psychiatric specialty as a professional person within mental health system statutes;

?? Allows an advanced practice registered nurse (with prescriptive authority) to prescribe and administer medication at MSH; and

?? Allows advanced practice registered nurses to testify as a professional in court proceedings.

LC0367 revises the statutes relating to the mental health managed care ombudsman. This bill:

?? Requires the ombudsman to prepare an annual report;

?? Clarifies that the ombudsman may not provide legal advice; and

?? Provides for confidentiality of information associated with an individual and compiled by the ombudsman in the course of conducting an investigation. The act also provides for exceptions relative to confidentiality, including disclosure when a court has determined that information is subject to a compulsory legal process or discovery.

LC0514 would allow the use of video teleconferencing in certain court proceedings dealing with mental illness, and would provide for the costs thereof. This bill would:

Allow courts to use video teleconferencing for certain hearings; and

?? Provide that the payment for the video proceedings become the responsibility of the party who has custody of the person subject to the court proceedings.

LC0370 is a resolution directing DPHHS and the Department of Corrections to coordinate and collaborate with state agencies, local governments, and the judiciary relative to training and education programs on issues involving persons with serious and disabling mental illnesses and the criminal justice and corrections systems. The resolution also directs other state agencies to cooperate and coordinate in training and education programs focusing on mental illness.

LC0513 would provide for the continuance of the study of the public mental health system, and would include representatives from the LFC and other appropriate legislative interim committees. Several interim legislative standing committees are considering study topics related to mental health services in the 2003 biennium. This bill directs that the study committee be set up as a subcommittee of the LFC and that membership be drawn from each of the interim committees interested in reviewing mental health issues. Such a structure would provide for an efficient, integrated and less duplicative approach to legislative consideration and the oversight of public mental health services.

DIRECTION TO HEALTH AND HUMAN SERVICES JOINT APPROPRIATION SUBCOMMITTEE

The LFC requests that the Health and Human Services Joint Appropriation Subcommittee consider six issues during hearings on the 2003 biennium appropriation for DPHHS. These issues are:

?? Review options to expand eligibility for Mental Health Services Plan and impose the cost sharing initiated during the HJR 35 study;
?? Establish MHSP financial eligibility for children eligible for both MHSP and CHIP at the same level as financial eligibility for CHIP;
?? Review DPHHS estimates of: 1) the average cost of providing mental health services by system component and age of recipient; and 2) the average cost of a high-end mental health services user by system component and age of recipient;
?? Closely evaluate the appropriation request for MSH, and particularly the estimate of the average daily population for the facility;
?? Review the DPHHS implementation of federal Medicaid matching reimbursement to local governments for transporting Medicaid eligible persons to medical treatment; and
?? Review the DPHHS case management model developed at the request of the LFC.

ENDORSEMENT OF MENTAL HEALTH OVERSIGHT ADVISORY COUNCIL RECOMMENDATIONS

The LFC reviewed recommendations made to DPHHS by the Mental Health Oversight Advisory Council (MHOAC). The LFC endorsed several recommendations including:

?? Funding 1.0 FTE to help develop training for law enforcement personnel and interfacing groups in recognition of mental illness and of the issues involved in dealing with persons with a mental condition;
?? Developing standardized screening for mental illness to be used in the context of the correctional system; and
?? Supporting and providing for family and provider education and contracts for peer-to-peer education.

The Executive Budget includes 1.00 FTE and $85,000 general fund ($135,000 total funds) over the biennium to implement this recommendation. The purpose and scope of this recommendation is covered in resolution LC9003, recommended by the LFC.

REQUEST FOR PERFORMANCE AUDIT

The LFC reviewed several mental health services established by DPHHS during the 2001 biennium and concluded that processes used to establish, implement and fund the services may not comply with federal regulations governing Medicaid Program administration. The LFC did not question the value or integrity of the services, but focused its concern on the implementation and cost development processes used to authorize and fund the services using Medicaid funds. The LFC also recognized a change made during reorganization of human services programs in 1995, which spread Medicaid administration among four divisions. Two divisions had previously provided Medicaid administration.

The LFC had concerns that spreading Medicaid administration among more divisions, given the inevitable turnover in management personnel, would dilute administrative knowledge of a very complex program.

The LFC requested that the Legislative Audit Committee (LAC) undertake a performance audit of the internal management processes used by DPHHS to ensure compliance with federal Medicaid criteria.

EARMARKED REVENUES AND STATUTORY APPROPRIATIONS: INTERIM STUDY

BACKGROUND

SB 378 (enacted by the 1993 legislature) requires the Legislative Finance Committee (LFC) to review dedicated revenue provisions during the biennium interim in order to ensure that the provisions :

- ?? are based on sound principles of revenue dedication;
- ?? reflect legislative priorities for state spending; and
- ?? are terminated when no longer needed.

The LFC is also directed to review statutory appropriations in order to determine whether the appropriation should be made by legislative appropriation. Emphasis is placed on those appropriations that fund administrative costs. Specific evaluation criteria to be used for purposes of the review are provided in statute. The law directs the LFC to establish procedures that facilitate the review and evaluation process; the committee's findings are to be reported to the legislature. This report for the 2001 legislature is available from the Legislative Fiscal Division (LFD).

Summary

SB 378 exempts certain categories of accounts from future review. The 1995 biennium committee review exempted 98 accounts from future review, the 1997 biennium committee review exempted 10, and the 1999 biennium committee review exempted 1, although this last was for a four-year period only.

The SB 378 Subcommittee chose to narrow its review of dedicated revenue accounts in the 2001 biennium to the analysis of state special revenue accounts in which the revenue source is fines or forfeitures. To facilitate the review, the LFD and the Department of Administration surveyed the administering agency of each state special revenue account to be reviewed.

Statute defines revenue from fines and forfeitures as a "general revenue source." The statute states that programs funded through dedicated revenue provisions for "general revenue sources" must be reviewed to the same extent that programs funded from the general fund are. For that reason, if funds are derived from a general revenue source but benefit only a select group of people, the legislature needs to determine whether the funds should be de-earmarked and deposited to the general fund. The function would then be funded with general fund money, and thus would compete with all other functions funded from the general fund.

The subcommittee narrowed the scope of its review of statutory appropriations in the 2001 biennium to the statutory appropriations added by the 1999 legislature. In past biennia, the subcommittee has reviewed each statutory appropriation.

Proposed Legislation

Legislation has been drafted (LC0270) at the request of the LFC to implement the recommendations that follow.

State Special Revenue

The LFC recommends that the following accounts be de-earmarked and the revenue deposited to the general fund:

1. **Fines and Penalties** (82-4-311, MCA) – Revenues received by the Department of Environmental Quality from fines and penalties imposed for violations of metal mine reclamation laws would be de-earmarked to the general fund.
2. **Forfeitures** (81-5-111, MCA) – Revenues received by the Department of Livestock from the proceeds of the sale of property used for the theft or transportation of stolen livestock would be de-earmarked to the general fund.

Statutory Appropriations

The Legislative Finance Committee recommends the following changes:

1. Appropriate by statute the funds derived from the timber harvest on common school trust lands, which go to the technology acquisition fund (20-9-534, MCA); and
2. Appropriate by statute the transfer of money segregated by county in the Hard-rock Mining Impact Trust Account following allocation to the hard-rock mining impact trust reserve account (90-6-331, MCA);

3. Eliminate the statutory appropriation of proceeds gained from the sale of forfeited property used for the theft or transportation of livestock (81-5-111, MCA).

Changes enacted by the 1997 legislature allow the Legislative Finance Committee to exempt statutory appropriations from future review. The following statutory appropriations have already been exempted from future review by the LFC. Of these:

1. Six are exempt from all future reviews (5-13-403, 10-3-203, 17-3-106, 20-8-107, 80-2-222, and 80-4-416, MCA); and
2. Nine are exempt from future reviews until fiscal 2002 (sections 23-5-136, 23-5-306, 23-5-409, 23-5-610, 23-5-612, 23-5-631, 44-13-102, 67-3-205, and 87-1-513).

FUND BALANCE ADEQUACY/RESERVES

The economic outlook for the state is very tenuous. Employment and wage indicators continue to demonstrate slow to moderate growth. In addition, the state's fiscal stability is not immune to economic and political changes, globally and nationally. General economic factors that have had an impact resulting in slower growth in state revenues during fiscal 2001 include the price depression of natural resources and farm products. Some of the effects of higher interest rates and energy prices are beginning to show, although the impact of these factors may not reach full realization until after adjournment of the legislative session. As a result, the outlook for the 2003 biennium is even less certain.

Attaining general fund budget stability means more than setting appropriations equal to anticipated revenues, with a positive ending fund balance serving as a safety net. The **adequacy** of the state's fund balance can signify the difference between whether or not the state is forced to confront the unpleasant consequences of fiscal instability.

Montanans are all too familiar with the consequences of general fund balance inadequacy. In the late 1980's and early 1990's, the state general fund experienced a deficit between revenues and disbursements. Much of the growth in the disbursement rate is a result of natural growth in expenditures due to inflation and/or caseload and enrollment increases, as well as supplemental spending for such contingencies as fire suppression or growing corrections caseloads. Revenue growth in the state has not always keep pace with expenditure growth.

The 56th Legislature adjourned from the May 2000 Special Session with a projected 2001 biennium general fund ending balance of $67.9 million. This amounts to approximately 3 percent of total expenditures. Within just a few months, the projection picture changed as the state incurred significant fire costs and became aware of projected human services and corrections increases. Together these factors contributed to a reduction in the projected fund balance of $66.0 million for the 2001 biennium. This reduction occurred in spite of some apparent increases on the revenue side. Overall, this situation demonstrates the volatility of state revenues and expenditures. At the same time, there existed the possibility that the fund balance would be further reduced through the approval of three voter initiatives. Ultimately, all three of these initiatives passed in the November 2000 election.

Recognizing that budgetary imbalances occur, the state can either take a reactive or a proactive approach. During the 1993 and 1995 biennia, the state held three special legislative sessions to deal with budget shortfalls. Although special sessions allow lawmakers the ability to address issues relative to revenues and expenditures, special sessions can cost the taxpayers as much as $45,000 per day. The need for special sessions is also closely scrutinized by the national agencies that rate the state's debt. Rating agencies also use a state's general fund balance as a percent of revenues as one of the key financial indicators for credit analysis.

Again from a reactive stance, budgetary fluctuation can be temporarily resolved through spending reductions. In accordance with 17-7-140, MCA, the Governor can authorize spending reductions: "...in an amount that ensures that the projected ending general fund balance for the biennium will be at least 1 percent of all general fund appropriations during the biennium." Essentially, the executive branch assumes control of the budget decision-making process by implementing spending reductions. Further, budgetary imbalances can be addressed only from one side of the equation -- expenditures. This means that legislative priorities could potentially get lost in the process.

Because of the cost and disadvantages of taking a reactive approach to budget imbalances, the more effective method is to approach these issues proactively through provision of adequate fund balance reserves. National fiscal experts such as the National Conference of State Legislatures (NCSL) recommend a reserve fund balance of 3 to 5 percent of total appropriations or revenues. Because Montana's budget is implemented on a biennial basis -- resulting in considerably more risk than an annual budgeting process -- the 3 to 5 percent should be applied to biennial totals. At a minimum, the budget process should include a general fund ending fund balance of 2.5 percent of total biennial appropriations or revenues. For Montana, with a total general fund budget of $2.4 billion, this equates to a $60.0 million ending fund balance.

The provision of an adequate general fund balance is essential to achieving a sound financial foundation. The level of fund balance reserves must be sufficient to offset the volatility of revenues and the potential for unforeseen expenditure increases. To this end, the legislature will again need to determine what amount of ending fund balance is sufficient to ensure budget stability.

HB 64: 15 PERCENT BASE BUDGET REDUCTION OPTIONS

Section 17-7-111(3)(g), MCA, enacted through HB 64 by the 1999 legislative session, directs those agencies of state government with more than 20 FTE to provide "a plan to reduce the proposed budget to 85% of the current base budget." This plan must be constructed as part of the budget submission to the budget director, and must include:

- a prioritized list of services that would be eliminated or reduced;
- the savings that would result from each service elimination or reduction listed; and
- the consequences or impacts of each elimination or reduction proposed.

Reduction scenarios are prepared in response to the question: If an agency's appropriation is to be less than the current level, or if there are new services that should be implemented within limited resources, what services would not be provided? Completing this analysis prior to the session and in context with the budget preparation process is the optimum time for this type of analysis. This exercise is intended to provide "what if" scenarios that provide the legislature and the Governor with information for use in assessing agency priorities.

The target amount for the reduction plan is 15 percent of the base budget. This requirement does not specify which fund types are to be targeted. Agencies are asked to develop the list of services for all funding sources. Since a given program/service is not usually funded in the same proportion as the whole agency, some latitude is allowed relative to non-general fund sources. Even so, every plan must include a general fund reduction equal to at least 15 percent of the agency's total general fund appropriation in the base budget.

Agencies were told that this information would not constitute an automatic "cut list," and agency plans are not included in this publication. The information will be maintained and presented separately for use as a tool by legislative analysts in support of the deliberations of legislative committees. This information will primarily be used when considering revenue shortfalls or when seeking funding methods for any new services proposed. These scenarios provide one opportunity by which the legislature can examine the base.

Agencies do not find identifying programs or portions of programs for inclusion in the base reduction plan an easy exercise. Responding is difficult, because elimination of any specific service impacts program beneficiaries (constituents) as well as agency staff. Ultimately, both the legislature and agency management must weigh costs and benefits relative to other programs or services.

Regardless of whether or not the program is ultimately cut, an exercise of identifying programs that might be cut can be problematic. The consequences of reducing or eliminating services mean hardships for constituents and potential unemployment for staff. Suggesting that a given program is expendable can be discouraging to constituents who have strong feelings about the importance of the services provided. Staff may receive the message that the work they do is not very important, which can impact morale and productivity. For these reasons, all parties concerned need to be sensitive to these repercussions and consider how they might affect the decision-making process.

UNIFIED COMPUTER BUDGET

This section discusses the requirement for a "unified computer budget" as provided for by HB 2 passed by the 1999 session. This bill provides that requests for funding for information technology (IT) expenditures be presented in a consolidated form. Therefore, information technology requests are reflected in two ways: 1) as part of the specific agency and program requests in volumes *3* and *4* of the *Legislative Budget Analysis*, and 2) in a single consolidated report in the *2003 Biennium Executive Budget*. This section provides background, a summary of information technology requests, a summary of the "significant" IT decision packages, and a discussion of related issues for consideration by the legislature.

BACKGROUND

The use of technology in the everyday operations of state government has grown, and almost every announcement of new hardware or software is designed to enhance the ability of workers to perform. Consequently, information technology is an area of expenditure in state government that has seen considerable growth in recent years. Budgets for various technology-related items have demanded a larger and more significant share of the overall budget. It has become increasingly difficult for legislators to sort through this category of the budget and make decisions that represent a clear path to the most efficient and effective use of information technology and state funds. While there have been various efforts over the years to develop policies and guidelines and to coordinate the application of technology within state government, the legislature has continued to experience difficulty in "getting their arms around" this budget area.

Figure 5
Fiscal 2000 Actual Information Technology Expenditures
By Source of Authority and Funding
(in millions)

Source of Authority	Information Technology Expenditures	Operating Expenditures	Percent IT is of Operating Expenditures	Total State Expenditures	Percent IT is of Total
Expenditures					
HB 2 Expenditures [1]	$ 77.9	$ 983.2	7.9%	$ 2,382.3	3.3%
Non-HB 2 Expenditures	47.6	297.6	16.0%	750.5	6.3%
Non-Budgeted Activity - State Funds	1.0	103.0	1.0%	1,551.3	0.1%
U-System General Operating Fund Expenditures	12.3	240.9	5.1%	242.4	5.1%
U-System Other Fund Expenditures	26.5	396.1	6.7%	454.0	5.8%
Total State Government Expenditures	$ 165.5	$ 2,020.8	8.2%	$ 5,380.6	3.1%
Funding					
General Fund	$ 29.2	$ 282.6	10.3%	$ 1,105.6	2.6%
Other Funds	136.2	1,738.2	7.8%	4,275.0	3.2%
Total Funding	$ 165.5	$ 2,020.8	8.2%	$ 5,380.6	3.1%

The 1999 legislature took a couple of steps that were intended to solve this dilemma. First, in HB 2, it required the Office of Budget and Program Planning (OBPP) to "provide to the legislature no later than November 15, 2000, by agency and program, a report showing information technology-related actual and adjusted expenditures in fiscal year 2000 and budgeted amounts for each year of the 2003 biennium." Second, in HB 2, it established an interim study of information technology management and policies, and the presentation of budget requests in a form that better enables the legislature to review and make policy decisions for this area of budget and policy. A subcommittee of the Legislative Finance Committee (LFC), with aid from the Legislative Fiscal Division (LFD) and executive branch staff, has performed the interim study. A final report was issued September 15, 2000. This report is available upon request from the Legislative Fiscal Division.

FISCAL 2000 INFORMATION TECHNOLOGY EXPENDITURES

Information technology is defined as hardware, software, and the associated services and infrastructure used to store or transmit information in any form, including by voice, video, and electronically. Expenditure and budget data for these costs are extracted from the accounting and budgeting systems based upon a select group of account codes (objects of expenditure) corresponding to this definition. According to the OBPP report, and as summarized in Figure 5, actual fiscal 2000 IT expenditures as appropriated in HB 2 total $77.9 million, or 7.9 percent of HB 2 operating expenditures.

Operating expenditures include personal services, operating expenses, and equipment. IT expenditures appropriated in HB 2 were 3.3 percent of total state expenditures. Total state expenditures include operating expenditures plus capital outlays, local assistance, grants, benefits and claims, transfers, and debt service. Figure 6 shows the seven agencies with the largest differences between operating expenditures and total expenditures.

Figure 6
HB 2 Agencies with Large Differences
Operating Expenditures to Total Expenditure
(in million)

Agency		Local Assistance	Grants	Benefits & Claims	Transfers	Total
3501	Office of Public Instruction	$ 477.2	$ 74.2			$ 561.1
4107	Crime Control Division		8.7			10.8
5102	Commissioner of Higher Education	5.3	9.9	18.5	131.9	172.3
6401	Department of Corrections			8.8		91.5
6501	Department of Commerce		26.8			48.8
6602	Department of Labor & Industry		15.9			46.1
6901	Department of Public Health & Human Services		37.9	558.4		766.8
	Total Expendiiture Accounts	$ 482.5	$ 173.4	$ 585.7	$ 131.9	$ 1,697.4
	Percentage of Total Expenditures	28%	10%	35%	8%	81%

In these agencies, nearly 81 percent of total expenditures were found in non-operating expenditures.

An error was identified on Table I-1 as presented in the *2003 Biennium Executive Budget*. The presentation for the Department of Transportation (MDT) on Section 1 of that table shows $194.8 million in operating expenditures and $424.1 million in total expenditures. In reality, MDT operating expenditures should be roughly $404.0 million. If the proper amount of operating expenditures had been reported for MDT, the IT expenditures would have been 7.9 percent of the operating expenditures for HB 2 appropriations and 8.2 percent of operating expenditures for all sources.

SUMMARY OF INFORMATION TECHNOLOGY REQUESTS FOR THE 2003 BIENNIUM

Figure 7 summarizes the HB 2 information technology requests for each year of the 2003 biennium. The total request for fiscal 2002 is $87.7 million and for fiscal 2003, $83.9 million. These requests represent increases of 15.8 percent and 10.8 percent over the base for fiscal years 2002 and 2003. During the analysis of the *2003 Biennium Executive Budget,* instances were identified in which IT budget requests were understated because the appropriate accounting code was not used to record requests for IT-related budget requests. As such, the IT-related budget requests as presented by the executive are understated. For example, $1.1 million of understated IT-related request were found in five requests made by one agency that misused one expenditure code.

Figure 7
Information Technology Requests
House Bill 2
2003 Biennium (in millions)

Budget Components	Fiscal 2002	Fiscal 2003
Base IT Expenditures - Fiscal 2000	$ 75.8	$ 75.8
Present Law Adjustments	5.8	4.4
New Proposals	6.2	3.7
Total Annual Request	$ 87.7	$ 83.9
Total Request for Biennium		$ 171.6

Figure 8 presents the total HB 2 IT-related requests in a different way. This figure shows the total requests by grouping the requests into similar expenditure categories. This illustration by expenditure groups gives the reader a perspective of the magnitude of the specific types of expenditures relative to the whole request. For agencies funded in HB 2, consulting and professional services is the largest category. Computer processing and personal services are categories with the next largest amount of IT-related requests. What this shows is that the majority of IT-related requests would go to developing and supporting computerized management systems and databases. A review of the IT-related budget requests listed in Section I of the *2003 Biennium Executive Budget* identified some common factors as viewed from a statewide perspective:

- Geographic Information Services (GIS);
- Conversion to Oracle standards;
- Compatibility with Statewide Accounting, Budgeting, and Human Resource System (SABHRS); and
- Electronic imaging.

Figure 8
2003 Biennium IT-Related HB 2 Requests
By Expenditure Category
(in millions)

Expenditure Categories	Fiscal 2000 Base	Fiscal 2002 Request	Fiscal 2003 Request	2003 Biennium
Personal Services	$ 11.6	$ 12.3	$ 12.2	$ 24.5
Consulting/Professional Svcs	20.4	27.7	23.9	51.6
Computer Processing	20.7	24.3	25.0	49.3
Telecommunications	9.0	9.3	9.3	18.6
Hardware Purchases	9.3	9.4	8.8	18.2
Software Purchases	1.5	1.7	1.8	3.5
System Support Services	1.6	1.7	1.6	3.3
System Development	0.6	0.7	0.7	1.4
Computer Maintenance	0.4	0.4	0.4	0.8
Software Leased	0.5	-	-	-
Computer Paper	0.1	0.1	0.1	0.2
Educ/Training of IT Staff	0.1	0.1	0.1	0.2
Hardware Leased	-	-	-	-
	$ 75.8	$ 87.7	$ 83.9	$ 171.6

Note: This table does not include the proprietary agencies, not budgeted within HB 2. The Information Systems Division is the largest of these.

Although the above factors were common to several requests, they were primarily observed in a small number of agencies that manage large numbers of databases and management systems.

Significant Decision Packages

Figure 9 lists the most "significant" IT-related decision packages (i.e., IT-related decision packages with requests of $300,000 or more for the biennium) as identified in the unified information technology report of the *2003 Biennium Executive Budget*. These present law adjustments and new proposals total $14.3 million for the biennium, and represent over 70 percent of all IT-related HB 2 requests. They do not incorporate the IT-related budgets included in the base.

Statewide Information Technology Issues

HB 2 of the 1999 legislature directed that a committee made up of members of the House Committee on Appropriations and the Senate Finance and Claims Committee review the Unified Computer Budget Summary provided by OBPP. The Legislative Finance Committee, as directed by HB 2, made the following recommendations:

- Hear and approve internal service fees and charges for the Information Services Division of the Department of Administration; and
- Provide policy direction for the IT-related issues identified in the LFD analysis of the *2003 Biennium Executive Budget.*

A review of the *2003 Biennium Executive Budget* has identified two IT-related budgetary issues with statewide implications:

- Oracle enterprise licensing costs; and
- SABHRS operating costs.

Oracle Enterprise Licensing Costs

Oracle has been used for the last several biennia as the state standard for database software. During the base year, a five-year licensing agreement expired and subsequently was renegotiated and renewed. The annual cost of the Oracle licensing agreement went from $200,000 to $920,000 (4.6 times the previous cost). The Oracle enterprise licensing increase would add $5.63 per month per computer to all agencies' operating costs. This increase is significant given the magnitude of change and statewide impacts. A significant number of IT-related budget requests involve converting existing management systems to Oracle standards. The legislature may wish to have the executive explain:

- Benefits to the state realized from adopting a statewide standard, such as Oracle;
- Factors that have caused the increase in Oracle licensing costs;
- Estimated investment in technology and costs associated with changing the state standard; and
- Factors that would cause the state to change the standard, including the likeliness of such a change.

SABHRS Operating Costs

Annual costs to operate and maintain the state accounting and human resource systems increase significantly from the 1999 biennium to the 2001 biennium. Requests included in the *2003 Biennium Executive Budget* would increase the annual cost for SABHRS by an average of 24.4 percent. By law (Section 17-1-102, MCA), agencies must record their financial activities on SABHRS. Consequently, all agencies are affected by increasing costs for this system. Please refer to: 1) Executive Budget – Other LFD Issues in this volume for a discussion of SABHRS, page 78; and 2) *Volume 3* of the *Legislative Budget Analysis*, beginning on page A162, for a more detailed discussion of issues regarding SABHRS operating costs. The legislature may wish to have the executive explain:

- ?? The factors causing the increase in SABHRS costs;
- ?? The status of SABHRS implementation;
- ?? Outstanding SABHRS implementation issues and plans to address those issues; and
- ?? How the state has or will benefit from replacing the Statewide Budgeting and Accounting System (SBAS) with SABHRS.

Figure 9
Unified Computer Budget
Significant IT-Related Decision Packages
2003 Biennium

Agency	Decision Package	Funding	Fiscal 2002	Fiscal 2003	2003 Biennium
Legislative Branch	Present Law Adjustment - Computer Systems Plan - Legislative Services Division	GF	$ 592,258	$ 666,893	$ 1,259,151
Comm. Of Higher Education	New Proposal - Banner Ongoing Costs	GF	185,540	185,540	371,080
	Present Law Adjustment - Guaranteed Student Loans - Increase Service Fees	FSR	155,000	158,100	313,100
Dept. of Environmental Quality	Present Law Adjustment - One Stop Grant for Information Technology - Biennial Appropriation	FSR	350,000		350,000
Dept. of Transportation	Present Law Adjustment - PC & Laser Printer Replacement	SSR	296,119	296,119	592,238
	Present Law Adjustment - Contracted Services to Create Customized Applications to be Integrated with Existing Systems	SSR	492,654	492,654	985,308
	Present Law Adjustment - Lockheed Martin Contract for Services/Systems Support	SSR	462,929	474,645	937,574
	New Proposal - IT Personnel for Services and Support Activities	SSR	191,028	191,709	382,737
	New Proposal - Governmental E-Commerce	SSR	250,000	200,000	450,000
Dept. of Revenue	New Proposal - GIS Maintenance	GF	261,084	189,600	450,684
Dept. of Administration	Present Law Adjustment - Statewide GIS Data Base - Biennial Appropriation	FSR	800,000		800,000
Dept. Public Health & Human Svcs	New Proposal - FAIM Phase II - Biennial Appropriation	FSR	3,500,000		3,500,000
	New Proposal - SEARCHS Level of Effort Increase	SSR & FSR	540,000	540,000	1,080,000
	Present Law Adjustment - MT Medicaid Info System FM Contract	GF & FSR	322,329	479,640	801,969
	New Proposal - Upgrade/Replace WIC Eligibility & Benefits System	FSR	500,000	1,530,000	2,030,000
Total			$ 8,898,941	$ 5,404,900	$ 14,303,841

Funding Codes:
GF = general fund
FSR = federal special revenue
SSR = state special revenue

INFORMATION TECHNOLOGY GOVERNANCE

INTERIM STUDY

HB 2 Requirements

HB 2, as passed by the 1999 legislature, required an interim study of the governance and management of information technology (IT) in the state. The study was authorized to address legislative concerns relative to state agencies' investments in and expenditures for information technology hardware, software, and services. Language in HB 2 assigned the study to the Legislative Finance Committee (LFC).

HB 2 authorized the LFC to review and assess Montana's governance, policy, planning, and budgeting structures, as well as the processes associated with the state's investment in IT. The LFC was then to recommend appropriate changes and define processes that would enable the legislature to make policy decisions relevant to IT budget issues. The focus of the study was to recommend: 1) the framework for dealing with the IT budget issues during the 2001 legislative session; and 2) a governance structure that enables future policy decisions that minimize cost, reduce duplication, and maximize efficiency while providing the greatest possible service to Montana's citizens. This section discusses the IT governance portion of the interim study. For a discussion of the framework for dealing with the IT budget issues during the 2001 legislative session, please refer to the "Unified Computer Budget" discussion in this volume; page 91.

IT Governance

The LFC recommended that the following structure be implemented for governing IT:

- The legislature should enact "***legislative guiding principles***" statements to steer the development of IT resources in state government.
- The legislature should create a ***Department of Information Technology,*** using existing staff in the
  - Information Services Division (ISD) of the Department of Administration (DOA). The director of the department should carry the title and function as the ***Chief Information Officer*** (CIO) for the state. The CIO and department should be responsible for:
    - developing and maintaining a statewide strategic IT plan;
    - reviewing and approving agency IT plans;
    - establishing statewide policies and standards for IT;
    - evaluating IT budget requests;
    - coordinating the development of shared IT systems and applications; and
    - reporting to the legislature.
- The legislature should create an ***Information Technology Board*** to advise the CIO. The membership and appointing authority of the IT Board should be included in statute. The IT Board should also have representatives from all three branches of state government and representatives from local and federal government and private industry.
- The legislature should accomplish ***oversight of IT*** during the interim through use of an existing interim standing committee, the Legislative Finance Committee, and during legislative sessions with the Long-Range Planning Subcommittee.
- ***IT-related governance statutes should be consolidated*** into one section of law and specific content requirements should be codified for agency and statewide IT strategic plans.

Legislation to implement the recommendations of LC0076 will be presented to the Legislature for consideration.

HIGHWAYS STATE SPECIAL REVENUE ACCOUNT

The 2001 legislature is faced with a declining working capital balance in the highways state special revenue account. The account is projected to end fiscal 2002 with a negative working capital balance of $2.4 million. Projections indicate that expenditures will exceed revenues by $10.1 million in the 2003 biennium, with the imbalance continuing in future biennia.

Revenues to the account, which are from highway users fees primarily comprised of motor fuel tax collections and gross vehicle weight fees, are expected to increase at an annual growth rate of 1.5 percent. However, revenue growth is not expected to keep pace with rising expenditure levels and inflationary increases associated with highway construction and related programs. The inelasticity of program revenues has contributed to the chronic deficit spending imbalance of this program. During the 1999 biennium, federal-aid highway construction funding was significantly increased when the act that authorizes federal highway funding, "Transportation Equity Act for the 21st Century" (TEA-21), was renewed for six years. Increased demand for state funds needed to match the increased federal funds will continue to stress the account working capital balances through the 2003 biennium and into the 2005 biennium.

In the 2003 biennium, projections indicated that expenditures from the account would exceed revenues by $10.1 million. Deficit spending is a key contributor to the projected decline in working capital balance. Void actions to bring revenue and expenditure growth rates more in line with each other, the account is projected to continue to decline and could begin to impact the ability of the Department of Transportation to provide for the needs of the state highway infrastructure.

The Executive Budget addresses the issue, in the short-term, through program cutbacks aimed at keeping the account solvent through the 2003 biennium. Until this point, the executive has reduced the expenditures in the state-funded construction program to maintain the account in a positive condition. This strategy has been virtually exhausted as the state-funded construction program has been reduced to a level at which further reductions would move the state into a position requiring higher percentages of state funds to match federal-aid highway construction funds. This is a losing proposition for Montana.

The Executive Budget includes initiatives that would potentially increase motor fuel revenues over the long-term. However, the initiatives also increase annual administrative costs by more than $0.5 million without providing measures for assessing the impacts of the initiatives. Besides these initiatives directed at enforcing motor fuel tax laws, the executive provides no long-term remedies for reversing the imbalance between revenues and expenditures.

This issue is presented in more detail in the Department of Transportation budget discussion in Volume 3, General Government and Transportation Section of this report; page A-64.

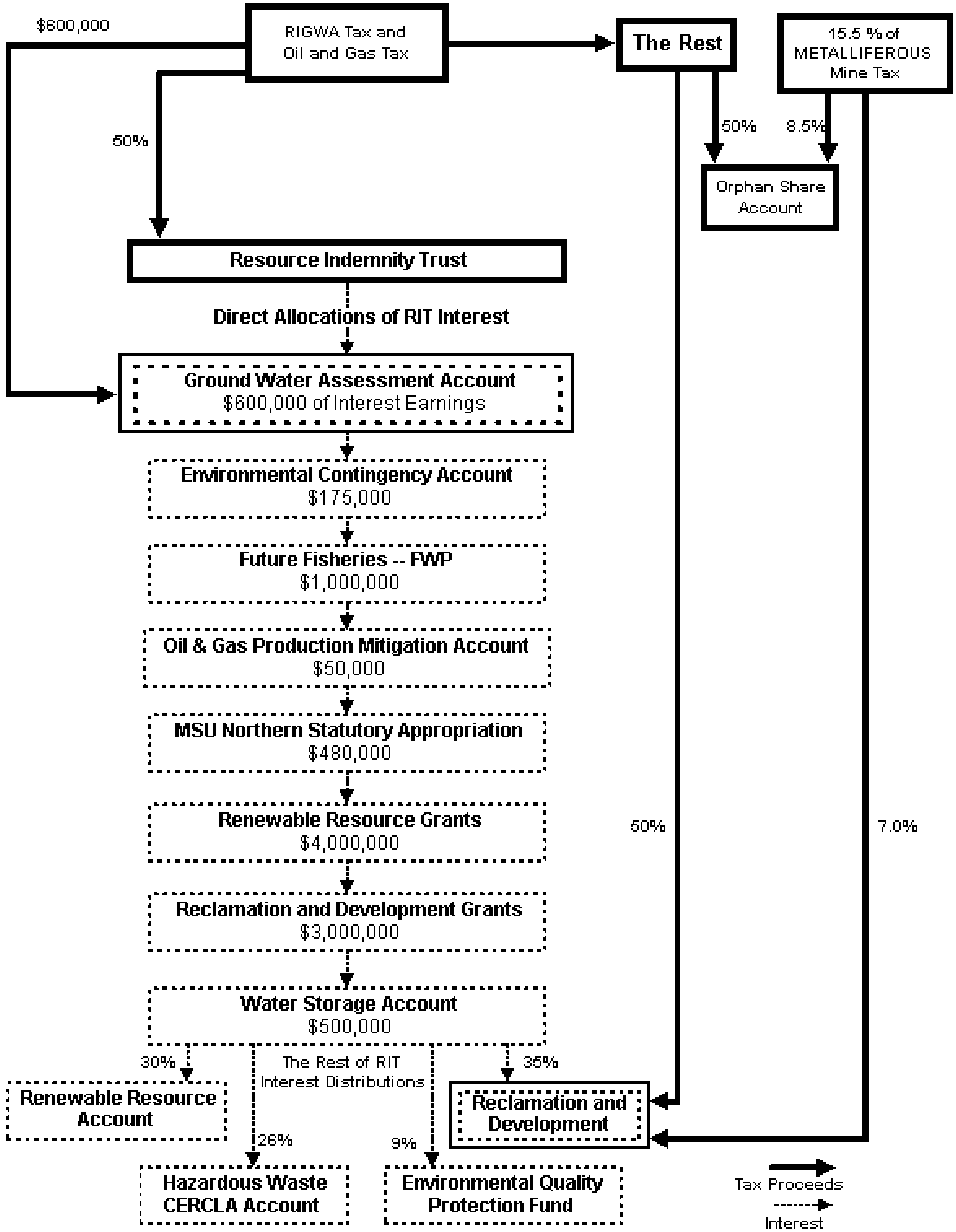
RESOURCE INDEMNITY TRUST

The Montana Constitution (Article IX, Section 2) requires the existence of the Resource Indemnity Trust (RIT), stating, "The principal of the resource indemnity trust shall forever remain inviolate in an amount of one hundred million dollars ($100,000,000) guaranteed by the state against loss or diversion." In the 2003 biennium, the executive is requesting the expenditure of $24.6 million from accounts funded with tax revenue and interest, including $8.3 million in grants.

After $600,000 per biennium is deposited to the Groundwater Assessment Account, the trust receives 50 percent of the revenue from the: 1) Resource Indemnity and Groundwater Assessment (RIGWA) Tax paid by mineral producers; and 2) portions of oil and natural gas production taxes allocated for distribution under RIT statutes. The remaining taxes are deposited into accounts established for various purposes. Chart 1 shows the flow of RIT proceeds and interest to expenditure accounts prior to the time the trust reaches $100 million.

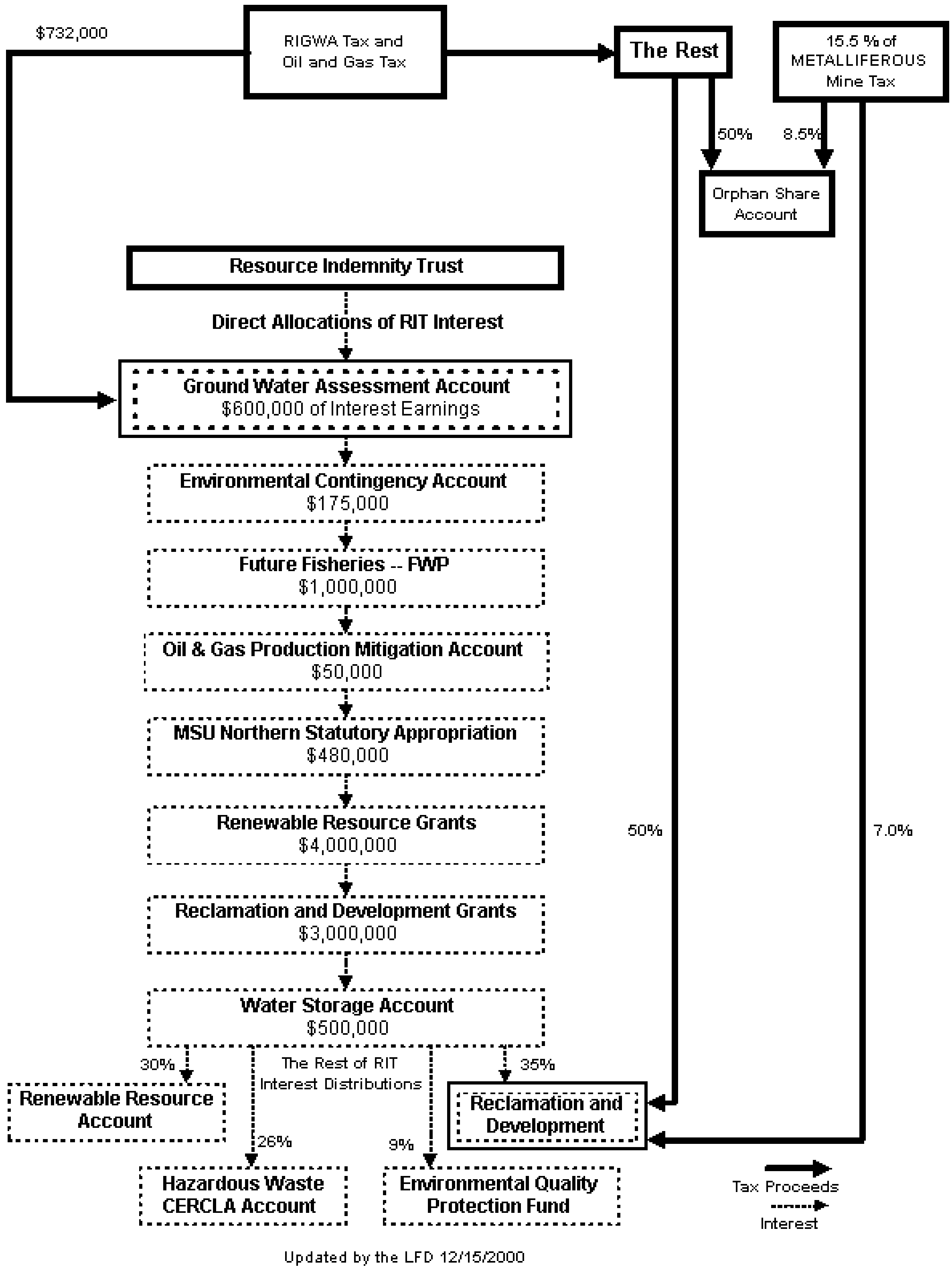
Based on Revenue and Taxation Committee estimates, the trust should exceed the $100 million threshold during fiscal 2002. When this occurs, the RIT will no longer receive any revenue. Instead, the money will be allocated to the groundwater assessment, reclamation and development, and orphan share accounts. These changes will become effective July 1 of the first year following the date that the Governor, by executive order to the Secretary of State, certifies that the RIT balance has reached $100 million. Chart 1A shows the flow of the RIT after the trust reaches $100 million.

Chart 1
Flow of RIT Proceeds and Interest
2003 Biennium (prior to the RIT reaching $100 Million)



Updated by the LFD 12/15/2000

Chart 1A
Flow of RIT Proceeds and Interest After the RIT reaches $100 Million



TRUST INTEREST

The Constitution does not restrict the spending of interest from the RIT. For the 2003 biennium, statute allocates $9.8 million of the interest for eight purposes. Figure 10 shows the direct allocations of interest from the RIT, as well as the source of appropriation authority from each account.

After direct allocations are made, any interest remaining is allocated as follows:

- ?? 30 percent to the renewable resource account that funds programs in the Judiciary, Department of Natural Resources and Conservation, State Library Commission, MSU Northern, and the Governor's Office;
- ?? 35 percent to the Reclamation and Development Account, which funds programs in the Department of Environmental Quality, Department of Natural Resources and Conservation, and the State Library Commission. This account also receives portions of the RIGWA and Metalliferous Mines Tax proceeds;
- ?? 26 percent to the Hazardous Waste/CERCLA Account that funds remediation activities in the Department of Environmental Quality; and
- ?? 9 percent to the Environmental Quality Protection Fund that provides for remediation activities in the Department of Environmental Quality.

The funds in the four accounts, along with other income, are appropriated by the legislature in HB 2 to fund operational costs of six agencies. All accounts receive revenue from various other sources, including natural resource taxes. The percentages of natural resource taxes allocated to the accounts are:

- ?? Resource indemnity and groundwater assessment taxes – After a 50 percent distribution to the RIT, $0.6 million is distributed to the groundwater assessment account, 50 percent each of the remaining RIGWA tax is distributed to the reclamation and development account, the orphan share account; and
- ?? Metaliferous mines taxes – 7.0 percent is deposited to the reclamation and development account, and 8.5 percent to the orphan share account.

Figure 11 on page 106 shows four elements of RIT. The first and second elements show the RIT revenues and trust balance for the past four fiscal years, as well as Revenue and Taxation Committee (RATC) projections for fiscal years 2001, 2002, and 2003. Based upon RATC estimates, the trust balance will be $99.6 million in fiscal 2001 and $101.1 million in fiscal 2002. Since the trust will not receive any further distributions after it tops $100.0 million in 2003, the trust balance will remain at $101.1 million. The third element shows the amount of interest generated by the RIT as well as amounts allocated by

Figure 10
Environmental Quality
Direct Allocation of RIT Interest

	Purpose	Source of Appropriation Authority	Amount
1	Groundwater Assessment Account	HB 2	$ 600,000
2	Environmental Contingency Account	Statutory	175,000
3	Future Fisheries	HB 5	1,000,000
4	Oil & Gas Production Mitigation Account	Statutory	50,000
5	MSU Northern Statutory Appropriation	Statutory	480,000
6	Renewable Resource Grants	HB 6	4,000,000
7	Reclamation and Development Grants	HB 7	3,000,000
8	Water Storage Account	HB 2	500,000
	Total Direct Allocation of Interest From RIT		$ 9,805,000

statute for specific purposes in the 2003 biennium. The allocations to accounts receiving a portion of the tax increase in fiscal 2003 when tax revenues are no longer deposited to the trust are shown. The fourth section details the seven primary accounts receiving RIT interest and other revenues. The calculations used to determine available fund balances at the beginning of fiscal 2002 are shown for each account, as are a list of revenue sources and a list of expenditures proposed by the executive.

Several revenue figures used in RIT calculations for fiscal 2000 are overstated. Due to erroneous entries on the state accounting system, revenue estimates are just over $1.8 million too high in fiscal 2000. To remedy the problem, the Legislative Fiscal Division received revenue corrections made by the Department of Revenue.

Because fiscal 2000 is closed for accounting purposes, accounting rules dictate that a prior period adjustment be made in fiscal 2001. Consequently, the fiscal 2001 figure is understated to compensate for the error in fiscal 2000.

FUND BALANCES

Of the seven funds that derive income from the RIT, four are projected to have a negative balance at the end of the 2003 biennium. Positive fund balances are projected for the other three. Similar to the error correction to the trust, revenue errors in 5 of the funds have resulted in significant negative impacts to the ending fund balances in the 2003 biennium. These error adjustments are shown in Figure 11on the following page.

The executive has proposed base, present law, and new proposal adjustments to funds that derive income from the RIT. The legislature may wish to consider not approving decision packages that use the Renewable Resource, Reclamation and Development, Hazardous Waste/CERCLA, and the Water Storage funds as funding sources.

In contrast, the Orphan Share Account is projected to have an ending-fund balance of $2.2 million. The legislature may wish to 1) increase appropriations to this fund; or 2) reallocate the distribution to the Orphan Share Account among funds projected to have negative ending fund balances.

For additional RIT information, please see the agency summary section of the Department of Natural Resources and Conservation in Volume 4.