

STATE FISCAL RELIEF
From The
Federal Jobs and Growth Relief Reconciliation Act

A Report Prepared for the
Legislative Finance Committee

By
Taryn Purdy
and
Lois Steinbeck

June 12, 2003

Legislative Fiscal Division



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INTRODUCTION

Under the Federal Jobs and Growth Tax Relief Reconciliation Act of 2003 (the Act), Montana will receive an estimated \$73.0 million additional federal funds for two purposes:

- **Flexible Distribution** - A flexible grant of \$25.0 million in federal fiscal 2003 and \$25.0 million in federal fiscal 2004
- **FMAP Increase** - An increase in the Federal Medical Assistance Percentage (FMAP) rate used to determine Montana's contribution to Medicaid costs, estimated at about \$23.0 million

FLEXIBLE DISTRIBUTION

States will receive flexible "fiscal relief" funds totaling \$5.0 billion in each of federal fiscal 2003 and 2004 based upon population, with a minimum distribution of \$25.0 million each year. Montana and 12 other states will receive the minimum distribution of \$50.0 million over two years.¹

MECHANISM

All states are required to provide a letter of certification to the federal Department of the Treasury that the funds will be used in accordance with the federal law (Attachment A). Montana is eligible to receive the federal fiscal 2003 payment as soon as the federal government receives the signed certification letter. As of this writing, the Governor has not yet provided that certification.

USES

The federal act requires that the funds be used for the following purposes (Attachment B):

- To provide essential government services; or
- To cover the costs to the state of complying with any unfunded federal mandates.

The funds can only be used for expenditures "permitted under the most recently approved budget for the state", meaning they cannot be used for fund new programs not already funded.

As indicated, the uses defined by Congress are extremely broad, and it appears as of this writing that interpretation of the uses will largely be left to the states. In a nationwide conference call on June 3, Undersecretary Peter Fisher of the federal Department of the Treasury stated that uses of the funds were essentially only limited by the very broadly stated purposes in the act, and by state law and its interaction with federal law.

Undersecretary Fisher was specifically asked to comment on three potential uses:

- "Rainy day fund" (bankroll the money for current and future economic uncertainty)
- Provision of maintenance of effort for federal funds
- Match for federal funds

Mr. Fisher did not rule out any of those potential uses, although he did say that use of the funds for a "rainy-day fund" would be dependent upon an examination by the state of its laws and how they interact with the Act (see below). However, he indicated that the state, rather than the federal government, would make that examination and consequent determination.

¹ Territories and commonwealths are also eligible. With the exception of Puerto Rico, all will receive the minimum distribution for those entities of \$5.0 million.

Potential for Change in Requirements or Federal Audit of Use

The federal government has on occasion provided little or no guidance on the expenditure of funds, or has provided funds with rules pending, only to provide further guidance or requirements that contradicted what the states were already doing. Legislative Fiscal Division staff asked Michael Bird, senior federal affairs counsel for the National Conference of State Legislatures (NCSL) in Washington, D.C, what potential existed for a change in requirements or rules at a later date, and whether he thought it likely the federal government would audit the state's expenditure of the funds. In an email on June 5, 2003, Mr. Bird stated he did not "foresee any rules or regulation[s] or even guidance regarding the flexible money."

Distributions to Local Governments

The Senate version of this legislation had included a provision for distribution of funds to local governments. This provision was removed entirely in conference committee. According to Mr. Bird in the same email, "[t]here will be no mandate whatsoever that states apportion any of these funds to localities."

LEGISLATIVE OPTIONS

This section of the report specifically examines two questions:

- What are potential uses for the funds?
 - Can the funds be used to increase the ending fund balance? What programs could the funds be used to support?
- Given Montana's constitution and statutes, what mechanisms exist to provide appropriation authority to spend the funds?
 - Can the Governor appropriate and spend these funds, or must the legislature meet and act?

Greg Petesch, Code Commissioner for the State of Montana, was asked to provide a legal opinion on a number of points (Attachment C). That opinion is attached (Attachment D) and, along with communications with the federal authorities, forms the framework and substance of the following discussion.

Potential Uses of the Funds

Ending Fund Balance

According to Mr. Petesch, the legislature can use the funds to increase the general fund ending balance by adding federal authority and reducing general fund authority. The Governor would not be able to increase the ending fund balance without legislative action (see below).

Current or Deleted Programs

This funding could be used to supplement funding for any program for which the legislature provided funding. No new programs could be established with the funds. The only limitation on use of the funds is that they be "essential government services", a definition that is being left to the states.

Mechanisms to Provide Appropriation Authority

Two sources of potential authority to spend the money exist: 1) the legislature; and 2) the Governor's authority to authorize additional spending under the budget amendment laws (Sections 17-7-401-405)²

Legislative Authority

The legislature could appropriate these funds in special session. Further, the legislature could either enhance or restore current services, or reduce general fund appropriations to provide a further ending fund balance cushion. The only restrictions are those imposed by the federal government in its very broad guidelines.

Executive Authority

The following uses the structure of questions and answers to examine the executive authority to add these funds, and the consequences for the general fund ending fund balance.

- Can the executive add the funds through a budget amendment without legislative involvement? Yes, but only if it is for an “additional service”, which is a requirement of the budget amendment law. “Additional service” is generally defined fairly broadly to mean not only a brand new function, but also an expansion or enhancement of broad types of services already provided. Consequently, “additional service” as interpreted in the budget amendment law would not necessarily conflict with the requirement that no new programs be funded with these funds.
 - As a consequence, can the executive determine priorities for spending the funds? Yes. Therefore, given the legislature's power and duty to determine public policy and the magnitude of the issues involved, it may wish to either determine those priorities through direct action or at the least provide direction and guidance to the executive.
- Section 17-2-108 requires that the approving authority reduce general fund by the amount of non-general fund received for similar purposes. Does the requirement that it be an additional service allow the executive to make this reduction³, thereby increasing the ending fund balance? It depends upon the plan for use of the funds. However, section 17-2-108 appears to give the executive too much authority to reduce an appropriation, according to Mr. Petesch⁴.
- Could the executive add the funds and simply order an agency to not spend the general fund? Yes, as long as the funds were for an additional service and all requirements of HB 2 and other appropriations were met. This action, however, does not technically increase the ending fund balance because the authority to spend the funds still exists. An appropriation is law while an order is not. Also, the appropriated level would count in determining “shortfall in revenue” under 17-7-140.
- Can the executive deposit the funds directly in the general fund to increase the ending fund balance? No, this is clearly in violation of state statute.

² Approving authorities are the Governor for all executive agencies, the respective legislative committees (i.e. the Legislative Finance Committee) for legislative divisions, the Supreme Court for the Judiciary, and the Board of Regents for the Montana University System.

³ Section 17-2-108 states, in part, that “...the approving authority...shall authorize the decrease of the general fund appropriation of an agency by the amount of money received from federal sources in excess of the appropriation in an appropriation act...unless the approving authority certifies that the services to be funded by the additional money are significantly different than those for which the agency received the general fund appropriation...[if] the general fund appropriation of an agency is decreased pursuant to this section, the appropriation for the fund in which the money is received is increased in the amount of the general fund decrease.”

⁴ The Montana Supreme Court in *Nicholson v. Stephens*, 1991 determined that it was an unconstitutional delegation of legislative authority to allow the executive to reduce appropriations. Instead, the executive could order agencies to reduce spending. However, any general fund authority would remain and could conceivably still be expended. Consequently, the ending fund balance would not be impacted by an order to reduce expenditures.

In summary, the executive could budget amend these funds and determine the priorities for their use, but does not appear to have the authority and the means to increase the general fund ending fund balance.

Other Approving Authorities

Statute provides authority to add budget amendments to multiple approving authorities.⁵ Multiple approving authorities raise the issue of just who would decide the allocation of these funds in the absence of direct legislative action. According to Greg Petesch, because the Governor must certify how the funds are going to be spent, the executive controls these funds.

SUMMARY

The federal government has left the door wide open for the use of these flexible grant funds. The executive can determine the allocation and priorities and add authority through the budget amendment process. However, if the legislature wishes the funds to be used to increase the ending fund balance as a cushion against revenue uncertainty, the Governor does not have this authority and the legislature would have to meet in special session, according to Greg Petesch. Also, given the legislature's power and role to determine public policy, the magnitude of the issues involved, and the lack of requirement that any other approving authority be involved in allocation of the funds if they are added through budget amendment, the legislature may wish to determine those priorities itself through direct action or at the least through provision of guidance to the executive.

FMAP INCREASE

The FMAP rate is the percent of Medicaid services costs that the federal government will pay.⁶ This rate differs for each state depending upon the change in its personal per capita income compared to per capita income changes in other states and is determined annually for each federal fiscal year. Under federal law, the FMAP rate can be no lower than 50 percent and no greater than 80 percent.

The Act raises the federal match rate by 2.95 percent annually and holds states harmless if the FMAP would have declined from one year to the next. Including the 2.95 percent bump and hold-harmless provision, the Montana FMAP rate increases from 72.93 percent in the last quarter of fiscal 2003 and from 72.88 percent in fiscal 2004 to 75.91 percent.

The Act specifies that states may not change Medicaid eligibility standards to be more restrictive than those in effect September 1, 2003 in order to be eligible for the enhanced match rate. Since the date regarding eligibility changes is prospective, the changes made by the executive during the legislative session and accepted by the legislature will remain in effect.

STATE FUNDS SAVED

The increase in federal match rates for most Medicaid services is estimated to offset about \$23 million in state matching funds, assuming that legislative Medicaid appropriations are fully expended, there are no increases in Medicaid costs, and general fund is not diverted to other uses. The amount of general fund saved, however, remains appropriated to DPHHS unless specific action is taken by the approving authority or legislature.

⁵ Approving authorities are the Governor for all executive agencies, statutory committees (i.e. the Legislative Finance Committee) for the respective legislative divisions, the Supreme Court for the Judiciary, and the Board of Regents for the Montana University System.

⁶ The federal cost share for a limited number of Medicaid services is higher than the FMAP rate, for instance reimbursements for Indian Health Services Medicaid benefits are fully paid from federal funds.

APPROPRIATION AUTHORITY MECHANISM

According to the legal analysis by Greg Petesch (Attachment D), the executive could use the budget amendment process for additional federal Medicaid appropriation authority. The legislature would not need to provide increased authority or approve the change.

CONSTRAINTS ON USE OF FREED UP GENERAL FUND

DPHHS could use the freed up general fund from enhanced FMAP without legislative involvement assuming several conditions:

- During the 2003 biennium, if general fund were moved from benefits appropriations to fund operating costs, it would need the approval of the Office of Budget and Program Planning
- During the 2005 biennium, general fund use must comply with statutory and appropriation statutes, and so could be used to fund numerous services or potential shortfalls including:
 - Offsetting vacancy savings requirements at state institutions
 - Maintaining cash assistance benefit levels
 - Funding unknown cost overruns

Legal Authority of Executive to Reduce Service Levels if Appropriation is Sufficient

Some statutes provide guidance on conditions under which DPHHS may reduce or alter services or service levels. For instance, DPHHS may reduce the amount, scope or duration of Medicaid services if the appropriation is insufficient. However, not all statutes governing DPHHS activities provide such guidance. And in most instances statutes are not strictly specific on the types, amounts, and eligibility conditions for DPHHS services. For instance, statutes allowing DPHHS to establish mental health benefits for individuals who are not eligible for Medicaid services, establish eligibility at no greater than 160 percent of the federal poverty level, but allow DPHHS wide latitude in determining eligibility and service levels within that broad constraint.

It is unclear whether it would be legal for the executive to take the following actions under the following circumstances. At this point, the Governor's Budget Office staff has indicated a desire "bank" general fund saved due to federal fiscal relief, pending analysis of federal statutes. If Medicaid program service costs during the 2005 biennium are higher than estimated and approved during the 2003 legislature (similar to the situation during the 2003 biennium), it is unclear whether the executive could reduce services as it did in some instances during the 2003 biennium if there is sufficient general fund appropriated by HB 2 to cover the state match needed to fully fund the cost over run.

Federal Regulations Not Final

While the Act seems fairly straightforward regarding the change in FMAP, staff from the NCSL has informed states that the federal Center for Medicare and Medicaid services has not yet finalized regulations to implement the change. Administrative rules may impact implementation of the Act in ways unknown at this time.

CURRENT DPHHS FISCAL SITUATION

The Department of Public Health and Human Services (DPHHS) has identified several state fund appropriation shortfalls within the past several months. General fund saved from the enhanced federal Medicaid match rate could be used to offset these shortfalls.

The shortfalls total \$2.6 million and need to be funded prior to the end of fiscal 2003 (June 30). Specifically the shortfalls are:

- Child support enforcement - \$2.1 million ⁷
- Fiscal 2002 Medicaid accrual shortfall - \$0.5 million

⁷ The 2003 legislature was aware of the child support enforcement program shortfall in matching funds and appropriated general fund and state special revenue from the Prevention and Stabilization Fund to offset some of the shortfall expected during the 2005 biennium. However, the \$2.1 million is the amount needed for the past and current fiscal year (2003 biennium). During the session, DPHHS anticipated requesting a general fund loan to offset the shortfall in child support enforcement state match shortfall.

If a loan cannot be made or the fiscal 2002 accrual shortfall cannot be deferred, it is extremely late in the fiscal year to undertake service reductions or other measures to reduce expenditures.