



# MONTANA LEGISLATIVE BRANCH

## Legislative Fiscal Division

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Legislative Fiscal Analyst  
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DATE: September 20, 2002

TO: Legislative Finance Committee

FROM: Jon Moe, Fiscal Specialist

RE: SB 162 Subcommittee: Final Recommendations

The attached report is the same distributed to the Legislative Finance Committee (LFC) members at the June 2002 meeting. While the report is the same, there are a couple comments that need to be added.

First, the subcommittee recommended in Recommendation #1 that fines and penalties that are deposited into the gambling license fee account be instead deposited into the general fund. This recommendation became unnecessary when HB 18 of the August 2002 Special Session was enacted. HB 18, which addressed certain problems or oversights of HB 124 (2001 session), included a provision to make this change.

Second, although the subcommittee's report was not orally presented to the full LFC (being delayed to the October 2002 meeting), the LFC did approve a committee bill request for the drafting of legislation to implement the recommendation in the report. The draft committee bill is expected to be available for committee consideration at the October meeting.

If there are questions concerning this report or the above comments, please contact Jon Moe at [jonmoe@mt.gov](mailto:jonmoe@mt.gov) or (406) 444-4581.

**SENATE BILL 162 SUBCOMMITTEE:  
REVIEW OF REVENUE DEDICATED  
TO LOCAL GOVERNMENT  
FINAL RECOMMENDATIONS**

A Report Prepared for the

**Legislative Finance Committee**

by  
Jon Moe, Fiscal Specialist  
June 12, 2002

**Legislative Fiscal Division**



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## PURPOSE

Section 17-1-603, MCA, enacted in SB 162 by the 2001 legislature, provides that “the Legislative Finance Committee shall review dedicated revenue provisions” in which revenues are dedicated to local government. The same section provides criteria for the review and provides that the committee report a summary of its finding to the full legislature.

The Legislative Finance Committee (LFC) established a subcommittee to perform the review process for the 2001-02 interim. The subcommittee members are **Senator Tom Zook (chairman), Senator Linda Nelson, Representative Dave Kasten, and Representative Gary Forrester**. This report is a summary of the work of the subcommittee and contains the resulting recommendations for the LFC’s consideration.

## BACKGROUND

### SENATE BILL 162

Senate Bill 162 is shown in Attachment A. It consists of three sections that include definitions, guidelines for review of dedicated revenue provisions, and the section that directs the review processes. The definitions are as follows:

- 1) *“Dedicated revenue provision” means an administrative or legislative action that allocates the revenue from a tax, fee, assessment, or other source to a local government.*
- 2) *“General revenue source” means a source of revenue not governed by established or implied restrictions based on the source or limited use of the revenue. The term includes taxes, interest earnings, investment earnings, fines, and forfeitures.*

These imply a broad range of potential statutory provisions that might be subject to the review process. The predominant limiting factor affecting the scope of the review comes from the fact that the provisions must allocate revenues to local government and that a number of significant relevant provisions were de-earmarked by another piece of 2001 legislation, House Bill 124 (the “big bill”), which made wide-reaching changes to how local governments are funded. The Senate Bill 162 review was a recommendation of the same 1999-2000 interim committee that developed House Bill 124. That committee simply was looking for a mechanism to provide for an ongoing review of provisions that dedicate revenue to local government, and Senate Bill 162 is that mechanism.

## **IDENTIFYING REVENUES DEDICATED TO LOCAL GOVERNMENT**

Legislative Fiscal Division (LFD) staff attempted to identify all remaining instances in which state revenues are dedicated to local government. These efforts resulted in identifying 32 provisions to be reviewed by the subcommittee. The following methods were used to identify the various provisions:

- A query was performed of state accounting records for fiscal 2001 to identify any state special revenue account from which expenditure were made to local governments, either as a local assistance or grants. This resulted in a list of 27 statutory provisions. These 27 items are discussed under the section on the review results and recommendations.
- A query was performed of an electronic version of the 2001 Session Laws in an attempt to identify new legislation that might include de-earmarking revenue provisions. Only one instance relevant to the Senate Bill 162 review was identified in this process. House 531 established a new \$50 fee and allocates \$25 of it to the county road fund. This same bill had previously been identified by the Department of Revenue as needing review. (However, in preparation for the subcommittee discussion, it was determined by LFD staff that House Bill 124 had included a change that sends the \$25 to the state general fund instead. Therefore, no action was necessary for this item.)
- LFD staff developed a list of provisions that dedicate revenues to local entities, in which the revenue is collected at the local level and never passes through the state accounting system. From this list, two items were identified that relate to the operation of the district courts. In the final report of the interim committee that studied court funding and structure, only four fees were identified as those that the district court clerks would retain. Neither of the two previously identified items (marriage license recording fee and probationer/parolee supervisory fee) was identified as being fees retained by the district court clerks.
- Two other dedicated revenue provisions were identified by the Department of Revenue. One relates to the distribution of Taylor Grazing Act fund. The second is a \$4 fee that is collected at the local level and sent to a state special account that is dedicated to creation and support of a motor vehicle information system.

While these searches were extensive, there is no guarantee that all applicable provisions were identified. There certainly may be other provisions that would warrant review, but which were not identified by these queries. However, as provided by 17-7-603, MCA, legislative staff, Governor's budget office staff, and future review subcommittees are to be vigilant in their ongoing tasks of budget analysis, audit, and drafting of legislation, to identify and review provisions that dedicate revenue to local government.

## **GUIDELINES FOR THE REVIEW PROCESS**

The guidelines to be applied are listed in Section 17-7-602(1), MCA:

- (1) *It is the policy of the legislature that a revenue source may be dedicated for a specific purpose when one or more of the following conditions are met:*
- (a) *The person or entity paying the tax, fee, or assessment is the direct beneficiary of the specific activity that is funded by the tax, fee, or assessment, and the tax, fee, or assessment is commensurate with the costs of the program or activity.*
  - (b) *The entire cost of the activity is paid by the beneficiary, and the tax, fee, or assessment is commensurate with the costs of the activity, including reasonable administrative costs.*
  - (c) *There is an expectation that funds donated by a person or entity will be used for a specified purpose. Grants from private or public entities are considered donations under this subsection.*
  - (d) *There is a legal basis for the revenue dedication. A legal basis is a constitutional mandate, federal mandate, or statutory requirement in which a source of funds is designated for a specific purpose.*
  - (e) *There is a recognized need for accountability through a separation of funding from the general fund consistent with generally accepted accounting principles.*

However, criteria listed in Section 17-7-603(3), MCA, provide additional guidance for the review process, although these are duplicative in some ways:

- (3)...*The use of a dedicated revenue provision may be justified if it satisfies one or more of the following:*
- (a) *The program or activity funded provides direct benefits for those who pay the dedicated tax, fee, or assessment, and the tax, fee, or assessment is commensurate with the costs of the program or activity.*
  - (b) *The use of the dedicated revenue provision provides special information or other advantages that could not be obtained without the revenue dedication.*
  - (c) *The dedicated revenue provision involves collection and allocation formulas that are appropriate to the present circumstances and current priorities of state and local government.*
  - (d) *The dedicated revenue provision does not impair the legislature's ability to scrutinize budgets, control expenditures, and establish priorities for state spending.*
  - (e) *The dedicated revenue provision results in an appropriate projected ending fund balance.*
  - (f) *The dedicated revenue provision fulfills a continuing need recognized by both local government and the legislature.*
  - (g) *The dedicated revenue provision does not result in accounting or auditing inefficiency.*

It is a combination of the guidelines and the criteria list above that the subcommittee applied in their discussion of dedicated revenue provision. At the conclusion of the review process, the subcommittee discussed the effectiveness of the criteria and the review process. A recommendation related to the review process is discussed later in this report.

## REVIEW RESULTS AND RECOMMENDATIONS

The SB 162 Review Subcommittee reviewed 32 provisions in statute that “dedicate” state revenue to local government. The majority was determined by the subcommittee to be appropriate dedications of revenue in the context of the SB 162 review criteria. Attachment B lists these items in an array that includes the subcommittee’s recommendation. Of the 32 items listed, four are discussed below with recommendations shown for two. The subcommittee recommendations are as follows:

- Gambling License Fee Account (DOJ/Gambling Control) – The subcommittee was concerned about the allocation of fines and penalties (currently 50 percent to the general fund and 50 percent to gambling license fee account for distribution to local government). The subcommittee voted to recommend that, in the spirit of HB 124, the 50 percent local share go to the general fund and be replaced by a like amount in the entitlement moneys that go to local government in HB 124. In fiscal 2001, fines and penalties totaled nearly \$70,000 and in fiscal 2000 it totaled \$76,500.

***Subcommittee Recommendation #1:** That the distribution of fines and penalties currently deposited in the gambling license fee [state special revenue] account be instead deposited to the general fund, and that the amount that would have been distributed to local government be added to the entitlement appropriation to local government (as established in HB 124 of the 2001 session).*

- Taylor Grazing Act Funds – The state treasurer (Department of Administration) receives this money and deposits it in a federal special revenue account for distribution. Current law provides that 50 percent of these monies go to the county general fund and 50 percent to the elementary BASE funding programs of the school districts in the county. The latter distribution is subsequently sent to the state general fund. In 2001, this share amounted to slightly more than \$100,000. The Office of Public Instruction and the Department of Administration Financial Services Division agree that it would be simpler to deposit this share directly into the general fund.

***Subcommittee Recommendation #2:** Deposit 50 percent of the Taylor Grazing Act funds directly into the state general fund “to be used for elementary BASE funding programs of the county”, instead of sending it to the school districts only to have it returned to the general fund.*

Recommendations were considered for two other provisions that were mentioned earlier in this report. The marriage license recording fee and probationer/parolee supervisory fee which are collected by district court clerks, under current law, are retained by the district court clerks. These fees were not included in the list of fees that were identified by the Court Funding and Structure Committee (1999-2000 biennium) as being retained by district court clerks. It was therefore suggested that these fees should go to the state general fund. The subcommittee

concurrent with a suggestion that these two fees be addressed in legislation being prepared by the Department of Revenue for cleanup of HB 124 omissions.

Recommendations accepted by the full Legislative Finance Committee (LFC) will be incorporated into legislation for the 2003 legislative session. A draft bill will be prepared for approval at a future LFC meeting.

## **ASSESSING THE PROCESS OF REVIEWING DEDICATED REVENUE PROVISIONS**

As part of the SB 162 review for this biennium, it is appropriate to consider the review process itself. There are two aspects that need discussion. First, is a review by a Legislative Finance Committee (LFC) subcommittee the most effective way to perform the review? Second, regardless of how the review is performed, does the criteria in statute provide the guidance that is consistent with the underlying purpose of the review?

### **IS A REVIEW BY A LFC SUBCOMMITTEE THE MOST EFFECTIVE WAY TO PERFORM THE REVIEW?**

The requirement for the review is contained in Title 17, Chapter 1, Part 6, which was enacted by the 2001 legislature in SB 162. The genesis of this legislation occurred in the Local Government Funding and Structure Committee of the 1999-2000 interim. As this committee completed its work on what became HB 124 (the "big bill"), which streamlined state and local government funding, it felt that there needed to be an ongoing effort to catch any local government funding provisions that might have been missed by the committee and to ensure that future legislatures do not dilute the effects of HB 124 by adding additional unnecessary dedicated revenue provisions. The enactment of SB 162 placed the review of revenues dedicated to local government with the LFC, which appointed this subcommittee.

SB 162 was modeled after Title 17, Chapter 1, Part 5, Dedication of Revenue to State Special Revenue Fund (enacted in SB 378 of the 1993 session). The review criteria are almost identical. The SB 378 review process was performed by an LFC subcommittee during four interims from 1993 to 2001. The 2001 legislature, however, deleted the requirement that the LFC review these provisions. Instead, the review is to be performed by various agencies in the course of their work (budget analysis, audits, etc.) and issues identified are to be presented in their work products (i.e., Legislative Budget Analysis or the audit report). This would be an option also for the SB 162 review.

What is the most effective way to determine whether revenues should be dedicated for local government (for a specific purpose, to a specific entity, etc.), or to determine whether provisions that dedicate revenue to local government are in concert with the principles of HB 124? There are a couple of options. In either case, the guidelines and criteria for the review process are established in statute by the legislature.

Option 1 – Continue to have a subcommittee of the LFC oversee the review process. This represents the status quo. The subcommittee’s staff member would continue to perform the research necessary to identify provisions that need to be considered. Information on each provision would be presented to the subcommittee for discussion and potential action. The advantages of this option are: 1) the more direct involvement of a few legislators in the actual application of the policy established in SB 162; 2) that it can be an education tool for new LFC members; and 3) it allows for a few members to participate rather than taking the time of the full committee. The disadvantages are: 1) there is duplicate effort because many of the same provisions would be reviewed by the subcommittee interim after interim; and 2) there is duplicative effort because the same statute requires various agencies to perform similar reviews in the course of their work.

Option 2 – Have the legislature establish the policy regarding dedicated revenue and leave the review with the various agencies that are designated to identify issues regarding these provisions in the course of their respective duties. The current statute provides that the Office of Budget and Program Planning, the Legislative Fiscal Division, the Legislative Services Division, the Legislative Audit Division, and the Department of Administration shall do this now, in addition to the LFC review. The nature of the SB 162 review, and its relationship to HB 124, would suggest that the Department of Revenue be added. Issues could be provided to the LFC as a “required report” submitted to the Legislative Fiscal Division. Training is suggested for the various agencies on the purpose of the review and the criteria that are to be applied, and to ensure compliance with this requirement. The advantage of this option is that: 1) the legislature establishes the policy in the statutory guidelines and criteria but allows its staff and/or the executive to make sure policy is followed, and 2) it eliminates the duplicative effort. The LFC must consider the relative priority of this activity when compared to other items on the work plan for the LFC and its staff. Each interim, a number of tasks either do not make the work plan or do not get completed because they rank lower in priority to this statutory requirement. Removing this statutory requirement of a subcommittee would allow other tasks or activities to rank higher in priority. Option 2 would require a change in statute to: 1) remove the LFC review which has been a subcommittee review process, and substituting a report to the full LFC by the legislative fiscal analyst; and 2) add the Department of Revenue to agencies that review such provisions.

***Subcommittee Recommendation #3:*** *The subcommittee recommends Option 2 which provides that the listed agencies identify dedicated revenue provisions based upon the statutorily established criteria and report occurrences of suspected non-compliance to the Legislative Fiscal Analyst (LFA), and requiring that these issues be the subject of a report by the LFA to the full Legislative Finance Committee at the October meeting preceding the regular session.*

Subcommittee recommendation #3 is incorporated into a conceptual draft of potential legislation, which is Attachment C. The subcommittee approved the conceptual draft. It includes the following revisions to statute:

- Incorporates the changes related to Recommendation #3, that would change the nature of the review process (as performed in response to SB 162).

- Combines Title 17, Chapter 1, Part 6 (regarding dedication of revenue to local government) with Part 5 (regarding dedication of revenue to state special revenue fund), conforming the latter to include requirements of the former.

## **DOES THE CRITERIA IN STATUTE PROVIDE THE GUIDANCE THAT IS CONSISTENT WITH THE UNDERLYING PURPOSE OF THE REVIEW?**

The criteria that is to be applied is included in this excerpt from 17-1-603, MCA:

*The expenditures from a dedicated revenue provision must be based on requirements for meeting a legislatively established outcome. Statutorily mandated programs or activities funded through dedicated revenue provisions from general revenue sources must be reviewed to the same extent as programs or activities funded from the general fund. The use of a dedicated revenue provision may be justified if it satisfies one or more of the following:*

- (a) The program or activity funded provides direct benefits for those who pay the dedicated tax, fee, or assessment, and the tax, fee, or assessment is commensurate with the costs of the program or activity.*
- (b) The use of the dedicated revenue provision provides special information or other advantages that could not be obtained without the revenue dedication.*
- (c) The dedicated revenue provision involves collection and allocation formulas that are appropriate to the present circumstances and current priorities of state and local government.*
- (d) The dedicated revenue provision does not impair the legislature's ability to scrutinize budgets, control expenditures, and establish priorities for state spending.*
- (e) The dedicated revenue provision results in an appropriate projected ending fund balance.*
- (f) The dedicated revenue provision fulfills a continuing need recognized by both local government and the legislature.*
- (g) The dedicated revenue provision does not result in accounting or auditing inefficiency.*

As mentioned earlier, SB 162 was a bill brought forward by the Local Government Funding and Structure Committee as an extension of the work done to develop and implement HB 124 (the “big bill”). The principles of HB 124 seem to revolve around a desire to simplify and stabilize local government funding, and de-earmark revenues.

A difficulty of the SB 162 review process has been the fact that its guidelines and criteria were taken almost verbatim from the other review process. If the intent of SB 162 is to police “earmarking”, then the criteria would probably be fine with some minor changes. But if the intent also is to simplify and stabilize local government funding, then the criteria needs to be further clarified. If the SB 162 review is closely related to the HB 124 implementation, then the criteria should more clearly provide that direction. Some of the listed criteria miss the mark while others seem vague for the intended purpose. As the SB 162 subcommittee attempted to apply the criteria, it seems that the criteria is satisfied in every instance, as it only requires that one of the listed criteria be satisfied in order for the dedicated revenue provision to be validated. As a result, of all the provisions reviewed to date by the subcommittee, only two revenue sources have been identified as recommended for de-earmarking.

The subcommittee discussed the review criteria in statute and suggested no changes in the criteria. The criteria are continued in the above mentioned draft legislation with only minor changes.