LEGISLATIVE BUDGET ANALYSIS 2023 BIENNIUM

VOLUME 1—STATEWIDE PERSPECTIVES

Preliminary Edition Based on Governor's November 15 Budget Submission

Legislative Budget Analysis
2023 Biennium
Volume 1 – Statewide Perspectives
Preliminary Edition Based on Governor's November 15 Budget Submission

Report from the Legislative Fiscal Division
To the Sixty-Seventh Legislature
January 2021

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Acknowledgements

The Legislative Budget Analysis report is the product of many hours of analysis by the staff of the Legislative Fiscal Division (LFD), a nonpartisan office which provides fiscal and policy information and advice to the legislature. The LFD thanks the many entities that assisted in its completion.

For information on this report and others, contact the Legislative Fiscal Division at (406) 444-2986 or visit the division's website at: https://leg.mt.gov/lfd/

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Director
AMY CARLSON

December 2020

Members of the Sixty-Seventh Legislature:

I submit for your consideration the high-level state budget outlook for the 2023 biennium as Statewide Analysis, Volume 1 Legislative Budget Analysis. The full budget analysis will be available in late December, just prior to session at https://leg.mt.gov/lfd/publications/. More details of the revenue estimates are found conveniently on the web, as well as, additional reference material, standard charts and tables. Access to the agency specific budget analyses are available online by choosing which agency budget analysis you are most interested in examining further. If you are unable to access the online version, please let staff know at karen.gilbert@mt.gov.

The Legislative Fiscal Division works for you, the legislators of Montana. We have no partisan alliance and seek to deliver high quality information and analysis of fiscal issues. A significant quantity of additional information is available online at our general website: https://leg.mt.gov/lfd/. Some specific resources that you may be interested in are reports on specific fiscal issues presented to the Legislative Finance Committee over the interim. Reports on financial modernization and stabilization, community college funding formulas, pension systems, local government budgets, and state information technology were some of the key areas researched this interim.

In addition to this analysis, the LFD has access to the state accounting system and other resources for researching specific fiscal questions. If a fiscal question arises, please feel free to contact either myself or any member of our staff to help answer your questions. Reach us through Microsoft Teams on the Montana Legislature 2021 Session Team, fiscal division channel or via e-mail. A staff listing can be found at the following: https://leg.mt.gov/lfd/staff-page/

We look forward to working with you all during the 2021 Session.

Sincerely,

Amy Carlson
Legislative Fiscal Analyst

VOLUME 1: THE OVERVIEW

The purpose of this report is to provide legislators with the information needed to assist them in crafting a balanced state budget and fiscal policy, and in reflecting their priorities in the 2023 biennium general appropriations act and other appropriations bills. It seeks to accomplish this by providing perspectives on the state's fiscal condition and the budget proposed by the Governor for the 2023 biennium, and identifying some of the major issues now facing the Legislature. As such, this document is intended to complement the entire Legislative Budget Analysis – 2023 Biennium online, which contains LFD's review of the 2023 Biennium Executive Budget by state agency and revenue estimates. In addition, this document is a reference document for all legislators, providing budget information for state government.

While the Legislative Budget Analysis – 2023 Biennium reports the results of LFD's detailed examination of revenue estimates and expenditures and proposed budgets of state programs, this document presents a broader, statewide, fiscal overview and discusses significant fiscal and policy issues which either cut across program or agency lines, or do not necessarily fall under the jurisdiction of a single fiscal subcommittee of the legislature. This report provides an updated general fund balance sheet, projects the general fund structural balance, compares biennial appropriations, and includes a summary of anticipated ongoing general fund revenues, ongoing present law expenditure requirements, including budget risks and budget pressures.

This volume is divided into five parts:

- Introduction - provides a summary of LFD's analysis of the proposed executive budget
- State Revenues - provides a review of the revenue assumptions adopted by the Revenue and Transportation Interim Committee
- State Expenditures - provides an overview of the Governor's state expenditure plan for the 2023 biennium
- Cost Pressures - highlights key underlying assumptions in revenues and expenditures, and also details some of the pressures that the legislature may face in the upcoming session
- Appendix - web only documents that provide additional information

LEGISLATIVE BUDGET ANALYSIS - 2023 BIENNIUM

REVENUE ESTIMATES

Volume 2 is a detailed reference of the state's major revenue sources and is available online. It provides the highlights of the underlying economic assumptions used in the revenue estimate adopted by the Revenue and Transportation Interim Committee, as well as historical collections and distributions for each revenue source. Also included are statutory references and estimate methodologies.

BUDGET ANALYSIS

The Budget Analysis offers detailed analyses of individual agency budgets, as proposed through the Governor's Executive Budget submitted in mid-November, but before the December 15 revisions were received. These volumes feature program-by-program detail, as well as the LFD analysis of each agency budget. Agency presentations are grouped in sections corresponding to the appropriations subcommittee addressing the agency.

- Section A – General Government
- Section B – Health and Human Services
- Section C – Natural Resources and Transportation
- Section D – Judicial Branch, Law Enforcement, and Justice
- Section E – Education
- Section F – Long-Range Planning

OTHER USEFUL LINKS

In addition to the Legislative Budget Analysis prepared for session, there are other financial documents online:

Understanding State Finances
HB 2 Guide
Legislative Finance Committee Reports

- Base Budget Examples – Sept. 2020
- Personal Services Memo – Sept. 2020
- Global Motions – Dec. 2020

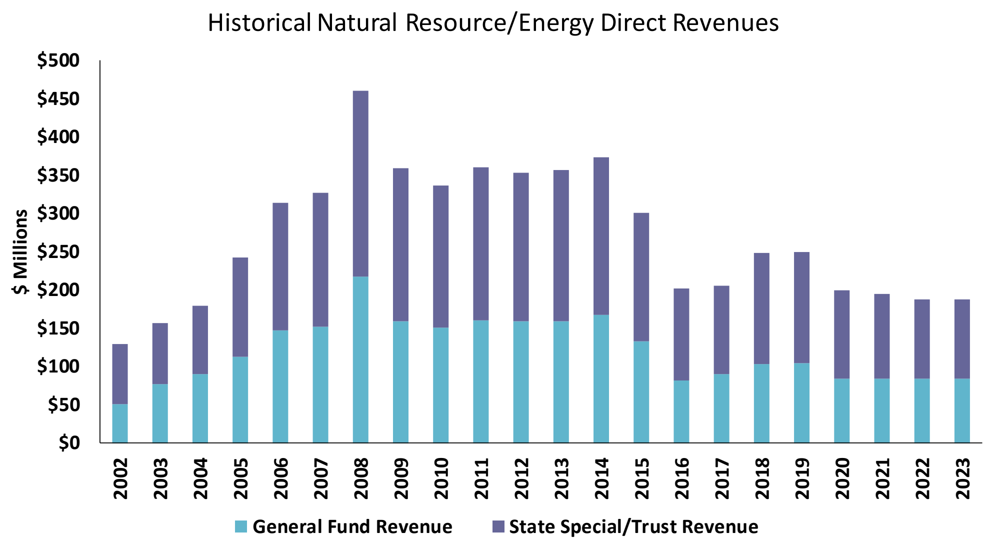
OVERVIEW

FOCUS ON GENERAL FUND

While there are many different funds that make up Montana's state finances, the general fund is the main fund used for state government operations. It is the primary measure for state finance and is the focus for the overview of the budget presented in this report.

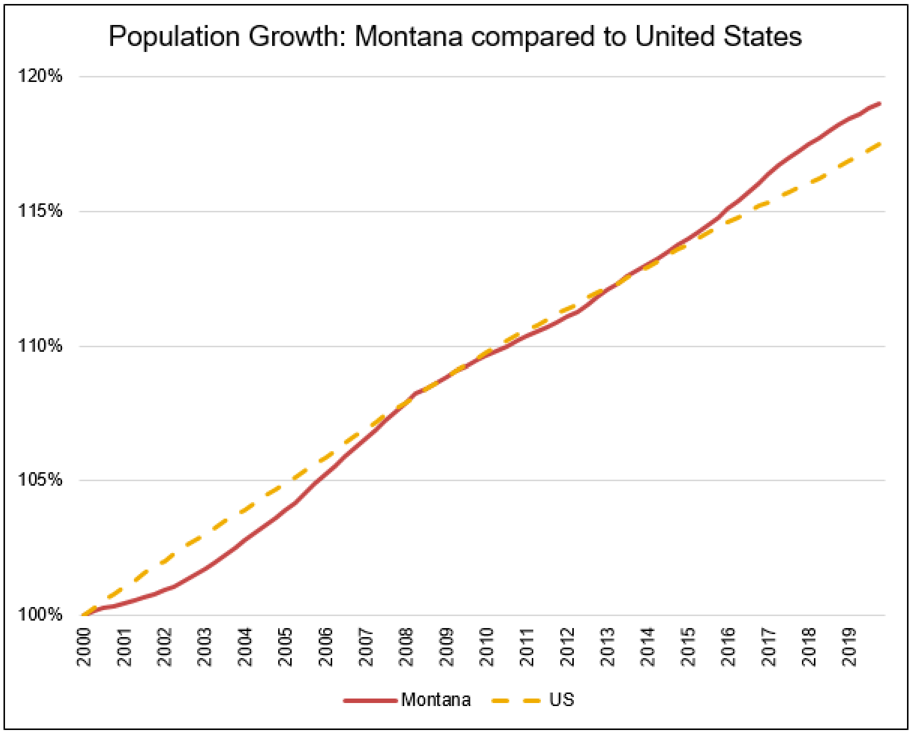
2023 BIENNIUM BUDGET UNCERTAINTY

The pandemic has caused disruption in workplaces and markets. This disruption has driven innovation that has temporarily and possibly permanently changed how we all do business and communicate across the country and around the planet. Changes in business practices have further economic impacts as they change where we choose to live and work. The pandemic has been described as accelerating trends that were already in the economy. Trends like automation of low skill work, more remote work, changing energy markets, and relocation of workplaces.



The first example of an accelerated trend impact on Montana's economy was the pandemic's contribution to already decreasing oil prices. Natural resource activity in the state had already been much lower than FY 2015 levels, and after a brief uptick in FY 2018 and FY 2019, these revenues fell again in FY 2020 and are expected to slowly decrease throughout the biennium. The graphic above shows the decline in revenue from natural resources and energy.

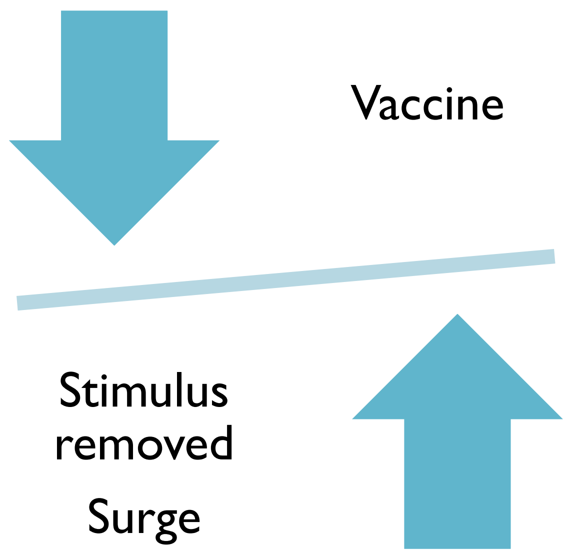
Another example, of accelerating trends in Montana is population growth. In recent years, prior to the COVID-19 pandemic, individuals moved to Montana from other states and population growth exceeded the national growth rate. There is anecdotal information that this trend has accelerated in 2020, but so far it is difficult to quantify with data to know how many people are moving to Montana, paying taxes, and need state and local services.



The graphic on the left is from on the bottom of page 5 of the Demographic Report Published for Legislative Week last January. It demonstrates the trend of the last several years when Montana's population growth has exceeded the growth of the country.

Population growth affects the cost of government services and the revenues from taxes of additional people. The associated report delves into more details about population growth.

In addition to the acceleration of change, the immediate economic effects of the pandemic continue to evolve. The revenue estimates were based on the October IHS Markit forecast that included a second stimulus, did not include a specific timeframe for a vaccine, nor did it account for the current surge in COVID cases and the economic impacts of the surge. At the same time IHS Markit has been analyzing the changing effects of people's reaction to the pandemic and are reevaluating how to incorporate the current surge into the forecast. Changes to the IHS Markit forecast are anticipated in coming months.



In addition to economic uncertainty, the CARES act tax provisions add additional variability to the forecast. The LFD has had conversations with Montana CPA's and were informed of various income and payment choices that taxpayers are considering that will impact how revenues flow to the state. From the tax payment information that will be available, it will be difficult to decipher what the actual income for taxpayers is and the ultimate tax payments the state will receive over the next several years.

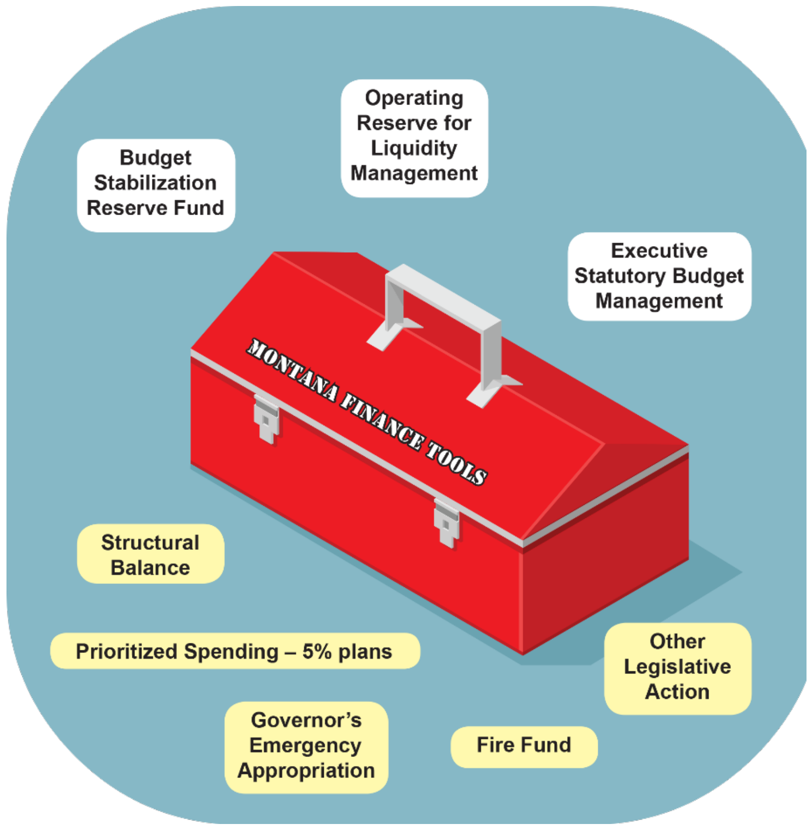
Current general fund revenues have remained relatively steady. Personal and corporate income tax collections are solid through November of 2020. While, accommodations, oil, gas, and coal taxes, and interest payments have been lower than previous years, the largest sources of general fund revenue in corporate and individual income taxes have been strong. In these tax sources, withholding and estimated taxes are above the levels of the previous year.

Timing of Income Realization and Tax Payments

At present, people are filing quarterly payments to be tax penalty free – aka "safe harbor". This may result in taxpayers pre-paying what they ultimately owe in taxes for calendar year 2020 and may pay less in calendar 2021. If significant pre-paying of taxes has occurred, February filing would be the first indication of this. On the other hand, individuals may accelerate income into calendar 2020 in anticipation of higher federal tax rates in 2021. Finally, the CPAs are uncertain what losses may occur. It appears that most businesses were doing relatively well through mid-October from the level of stimulus funds available through state and federal programs.

Montana's Toolbox for Uncertainty

Over the past decade, Montana has improved its toolbox for managing uncertain and potentially volatile revenue streams. Given the uncertainty in the current budget this toolbox will be important for risk management.



Tools available for liquidity management include minimum and ideal levels of general fund balances defined in statute; balances in the budget stabilization reserve; fire fund; and capital development fund. All of the previously mentioned tools allow cushions to variability in actual general fund revenues. Balances in other state special funds can also be used by the legislature to shore up the general fund when needed. In addition to balances, tools available also include reviewing the agency suggested 5% plan reductions, modifying laws to eliminate programs, or to increase tax rates, add new taxes or fees, and the ability to reduce the pay as you go infrastructure spending for bonded infrastructure investments.

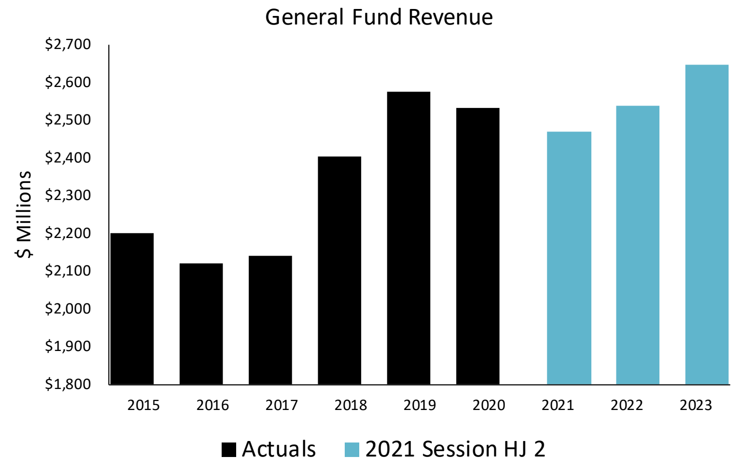
For more details on the financial tools please see the online training.

General Fund Beginning Balances and Other Reserve Balances

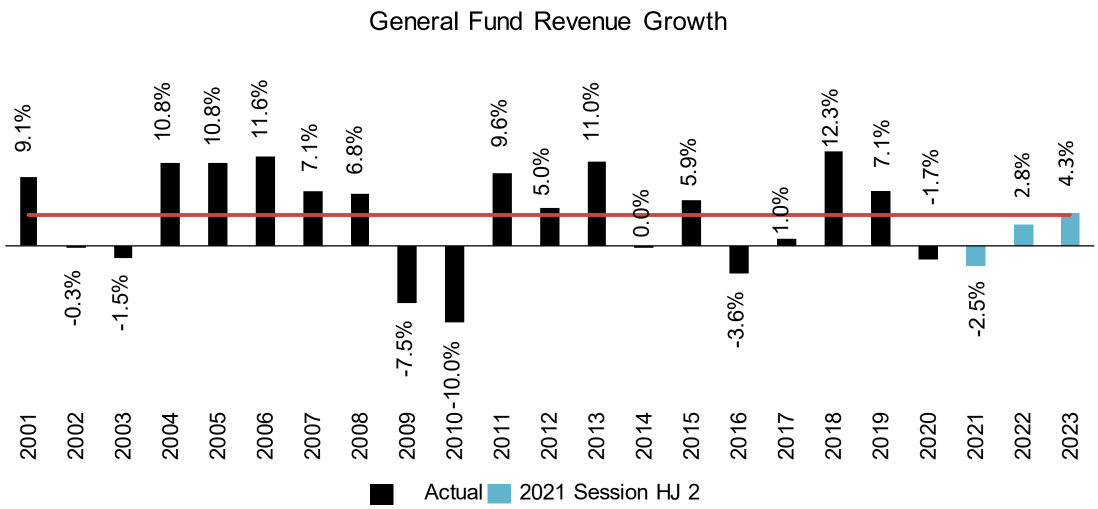
At the beginning of FY 2021, the state financial reserves were full and offered a solid cushion to begin FY 2021. The following chart shows the components of the reserves, which totaled $624.0 million, or 24.7% of annual general fund revenues. The FYE 2020 general fund ending fund balance contributed to reserve cushions, as the balance was higher than anticipated at $451.7 million. In addition, the budget stabilization reserve began FY 2021 with $117.8 million, and the wildfire suppression beginning fund balance for FY 2021 was $54.6 million.

The budget stabilization reserve fund reached its statutorily defined threshold, $4.7 million was transferred to the capital maintenance fund in early FY 2021.

The adjacent chart illustrates general fund revenue collections since FY 2015 and forecast HJ 2 revenues as adopted by the Revenue Interim Committee (RIC) through the 2023 biennium. Following stagnant growth in FY 2016 and FY 2017, revenue growth was extremely strong in the following two years before slowing in the second half of FY 2020.



The figure below shows the adopted revenue estimate compared to historical revenue growth rates. Currently, the adopted HJ 2 revenues are anticipated to decrease from FY 2020 levels by 2.5% in FY 2021, and then grow by 2.8% in FY 2022 and 4.3% in FY 2023. The past 20 years has an average growth rate of 4.0%, illustrated in the chart below by the red line.



As the following months ensue, the LFD will closely monitor the revenue picture as updated IHS forecasts and collection data becomes available. Given the extraordinary uncertainty with the current revenue picture, it is possible that revised forecasts from the LFD in the coming months may differ substantially from what was adopted in HJ 2. For additional information on the HJ 2, please refer to the LFD 2023 Budget Analysis, Volume 2.

Comparison to Governor Bullock's revenue assumptions

Governor Bullock's budget assumed slightly lower revenues. The three-year estimate (FY 2021 through FY 2023) is 0.7% lower than HJ 2. The additional revenue in HJ 2 offers slightly more cushion in developing the budget, but in a time of uncertainty as previously discussed.

BUILDING THE BUDGET

The budget is built according to statute. For information on budget rules, budgeted appropriation types, and a general understanding of state finances, please refer to the LFD publication Understanding State Finances. The details of all budgeted fund types are contained in the expenditure section of this report, and the overview of the general fund budget is contained in this section.

Base Budget

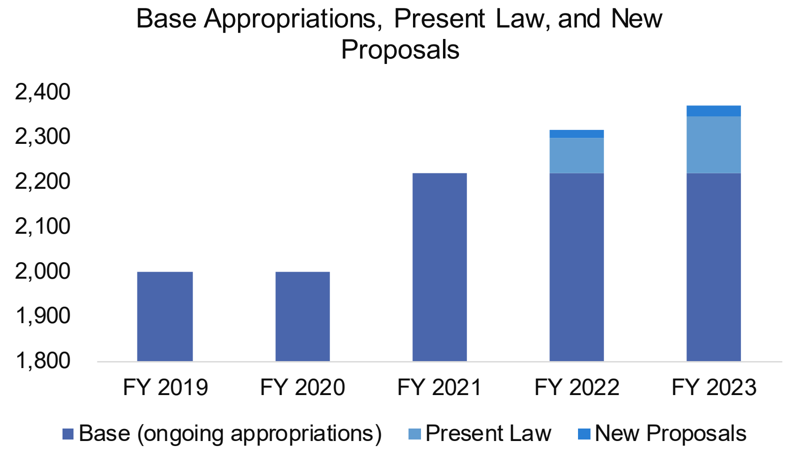
The base budget is defined as the resources authorized by the legislature for the ongoing operation of state government in FY 2021. The HB 2 base budget for the 2023 biennium including all fund types totals $12,345 million.

General Fund Base Budget

The HB 2 general fund base budget is $2,218 million per year or $4,437 million for the biennium.

General Fund HB 2 Base

The following chart shows the general fund base budget over time beginning with FY 2019, the previous biennium's base budget. The 2021 budget process began with the FY 2019 base budget at $1,998 million. The 2023 biennium budget process begins with the FY 2021 base at $2,218 million. Present law and new proposals increase the budget to $2,371 million by FY 2023.



General Fund Present Law Budget

When building the state's budget, the base level of funding is adjusted for present law changes. Statute provides a definition of the present law budget, as the level of funding necessary to maintain current government services. Present law gives the legislature a baseline budget presentation and provides the beginning point at which legislative budget decisions are made.

Budget building basics use the base budget and then adds the statutorily defined present law base 17-7-102, MCA which includes funding for continuation of ongoing programs.

Statute defines present law as the following:

(12) "Present law base" means that level of funding needed under present law to maintain operations and services at the level authorized by the previous legislature, including but not limited to:

(a) changes resulting from legally mandated workload, caseload, or enrollment increases or decreases;

(b) changes in funding requirements resulting from constitutional or statutory schedules or formulas;

(c) inflationary or deflationary adjustments; and

(d) elimination of nonrecurring appropriations.

General Fund HB 2 Present Law for the 2023 Biennium

General fund total base budget plus present law appropriations total $4,643 million. Present law adjustments from the base total $206.4 million.

Present Law

Present law adjustments include adjustments for enrollments in various programs, population changes, statutory changes, and inflationary like adjustments. The legislature will evaluate the executive proposed present law in detail during the budget deliberation process.

GOVERNOR'S GENERAL FUND BUDGET 2023 BIENNIUM NEW PROPOSALS

The Governor's general fund new proposals increase revenue by $8.7 million over the 2023 biennium and add one-time revenues by transferring $75.0 million from the budget stabilization reserve fund.

New proposals to increase spending by $43.5 million, plus $200,000 in general fund transfers total $43.7 million in the 2023 biennium. Details of expenditure proposals are included in the expenditure section of this report.

The significant new general fund expenditure proposals are in the following areas of the budget:

- Refinance Cyber security removes $6 million of general fund and replaces with rates
    - Reduces Dept of Administration HB 2 general fund by $6 million
    - Now paid by all agencies within the Enterprise Service Rate
        - GF – 39.5%
        - SSR – 23.8%
        - FSR – 17.6%
        - Other – 19.1% (internal service funds, enterprise, etc.)
    - HB 10 includes Montana cybersecurity enhancement appropriation of $4.9 million
- The two sources referenced above that are redirected to the general fund include some specific funding carve-outs from the coal severance tax and natural resources operations funding. Numerous agencies are impacted by these changes.
    - Coal Severance Tax:
        - Department of Commerce, Office of Tourism and Business Development, would eliminate $1.8 million in general fund statutory appropriations which is replaced with HB 2 general fund appropriations
        - Department of Agriculture, would eliminate $1.6 million general fund statutory appropriations for the following programs:
            - Growth through agriculture program: $900,000
            - Cooperative Development Center: $65,000
            - Montana food and agricultural development program: $600,000
        - The Department of Natural Resources and Conservation eliminates funding to a state special revenue fund which supports conservation districts. As proposed, funding is switched to general fund for $6.2 million for the 2023 biennium
    - Natural Resource operations
        - Proposed LC 851 eliminates the natural resources operations state special revenue fund impacting Department of Natural Resources and Conservation and the Department of Environmental Quality. More information on these impacts is in the HB 2 section of this report
- Department of Public Health and Human Services
    - Early Childhood Education would be funded with $10.0 million
    - A funding shift would increase general fund spending for the Children's Health Insurance Program (CHIP) by $8.4 million due to the spenddown of available fund balance
    - A variety of other funding shifts occur in present law within the Medicaid programs that increase general fund by $32.2 million, while reducing federal funding by $106.0 million and state special funding by $12.1 million
- Department of Corrections
    - Hepatitis C treatments for inmates would increase the general fund appropriation by $5.1 million

- Caseload increases and other factors are typically addressed in DOC with additional personnel. Funding has been requested for 39.00 FTE in Department of Corrections, and $4.2 million

General Fund Measurement
The general fund budget is measured in two ways: structural balance and ending fund balance.

Structural Balance
Structural balance is the measure of ongoing revenue to ongoing spending and is important since it sets the stage for the following biennium budget. For example, if the budget is at a structural deficit or spending more than current year revenue, the budget for the following biennium will likely be out of balance and require reductions to balance the budget.

Ending Fund Balance
Ending fund balance is the amount of funds anticipated to be in the general fund at the end of the biennium.

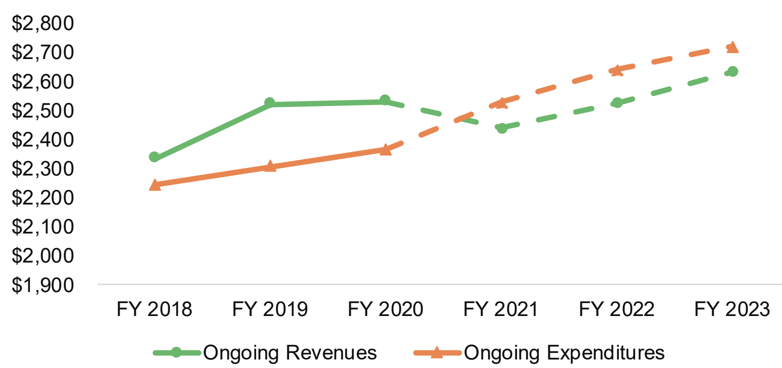
The [statutory minimum] projected ending fund balance is 4% of the second-year appropriations or approximately $105 million.

Operating Reserve
The [statutorily recommended] operating reserve for projected ending fund balance is 8.3% of the second-year appropriations or approximately $210 million.

General Fund Structural Balance Recommended by Governor Bullock

In the 2023 biennium, the executive's total present law budget, not just HB 2, is more than the HJ 2 revenues adopted by the Revenue and Interim Committee on November 19, 2020.

While one-time cost savings measures like higher federal match for Medicaid during the public health emergency and one-time infusions of funds from the budget stabilization reserve fund, bolster the ending fund balance of the general fund, the one-time occurrences have no impact on structural balance. Since structural balance is a measure of ongoing revenues against ongoing expenditures, expenditure projections remain above the level of anticipated ongoing revenue and therefore the budget is projected to be structurally imbalanced by 3.2% in FY 2023. As proposed by Governor Bullock, ongoing expenditures exceed ongoing revenues by $114 million or 4.5% in FY 2022 and $83 million or 3.2% in FY 2023.



With the adopted general fund HJ 2 revenues this structural imbalance shrinks to 2.6% in FY 2023. FY 2023 is the year to watch as it will be the base budget for the following biennium and thus be the starting point for decisions in the 2023 session.

THE EXECUTIVE PROPOSED GENERAL FUND BALANCE SHEET

The following table illustrates the proposed legislation and executive's revenue projections for the state general fund. Included in the proposed general fund balance for FY 2021 is proposed savings of $84.1 million for COVID-19 reimbursements and FMAP changes. The Department of Public Health and Human Services has since requested a budget change for FY 2021 that would utilize $7.5 million general fund for increased payments up to 200.0% of the Medicaid daily rate for COVID-19 isolated or quarantined patients. This budget change may lower the executive's proposed ($84.1) million savings by up to ($76.6) million. This change could impact the FY 2021 ending fund balance driving it down to $372.2 million. The change is one-time-only, so structural balance would not be impacted. The graphic shows the structural imbalance recommended by Governor Bullock at the end of FY 2023 at $83.4 million.

General Fund Balance Sheet
Includes Executive's Revenue Estimates and Expenditure Projections
($ Millions)

	Actual FY 2018	Actual FY 2019	Actual FY 2020	Estimated w/Gov revenues FY 2021	Estimated w/Gov revenues FY 2022	Estimated w/Gov revenues FY 2023
Beginning Fund Balance	$47.9	$186.7	$361.3	$452.4	$379.7	$297.8
Revenues						
Actual & Executive Estimates	2,333.6	2,519.6	2,529.2	2,439.6	2,520.0	2,629.3
Revenue legislation						
LC 851 Redistribute revenue to general fund					2.2	2.2
LC 943 Eliminate coal severance tax allocations					2.2	2.2
OTO	71.8	54.1	4.1			
Tobacco settlement				9.4		
LC 850, Transfer BSRF to General Fund					37.5	37.5
Adjustments - revenue	1.6	0.6	(3.5)			
Total Revenue Funds Available	2,455.0	2,760.9	2,891.2	2,901.5	2,941.5	2,968.9
Expenditures - Ongoing						
Statutory Approps	316.4	317.1	282.8	305.5	306.1	314.1
New Statutory Appropriation HB 14, Debt Service					0.4	2.0
General Fund Transfers	19.9	26.8	35.2	24.5	21.7	21.5
New Proposal Transfer, ongoing					0.1	0.1
HB 2 Agency Budgets (includes pay plan in current biennium)	1,904.3	1,951.6	2,014.5	2,142.4	2,314.7	2,370.2
HB 1	2.4	8.5	2.4	10.5	2.5	10.8
Other Appropriations (includes HB 715)	0.1	1.5	29.6	49.7		
HB 13 Payplan, proposed					1.2	7.2
Carryforward & other			0.4	2.9		
Reversions				(8.3)	(8.9)	(9.0)
Ongoing Expenditures	2,243.0	2,305.7	2,364.8	2,527.1	2,637.8	2,716.9
OTO						
HB 2 Agency Budgets	13.0	15.2		6.6	1.0	0.9
HB 3 Supplemental		12.2		16.4		
HB 10, Information Technology Transfer				7.3	5.0	
Estimated savings from increased FMAP & COVID reimbursements				(84.1)		
BSRF Transfers		60.7	57.1	1.1		
Fire Fund Transfers	25.3	21.5	30.3	46.7		
Other Appropriations	2.0			0.5		
Other	4.2					
Total Expenditures	2,287.5	2,415.3	2,452.2	2,521.7	2,643.8	2,717.8
Other Adjustments	19.2	15.1	16.1	0.1		
Anticipated CAFR Adjustments			(2.6)			
Ending Fund Balance	$186.7	$361.3	$452.4	$379.7	$297.8	$251.0
Structural Balance			$164.4	(87.5)	(113.5)	(83.4)

EXECUTIVE PROPOSED LONG-RANGE PLANNING SPENDING

Montana Infrastructure Proposal

The executive proposal entitled "Montana Infrastructure" is basically an aggregation of the traditional LRP infrastructure budgets. The proposal totals $499.4 million, including $91.3 million of non-state funds (university, proprietary, and donated funds). The proposal makes use of $238.0 million in state resources, including federal funds, $78.6 million of proceeds from coal-severance tax bonds, and $91.5 million in general fund general obligation bond proceeds to provide appropriations and grants for state and local government infrastructure investments.

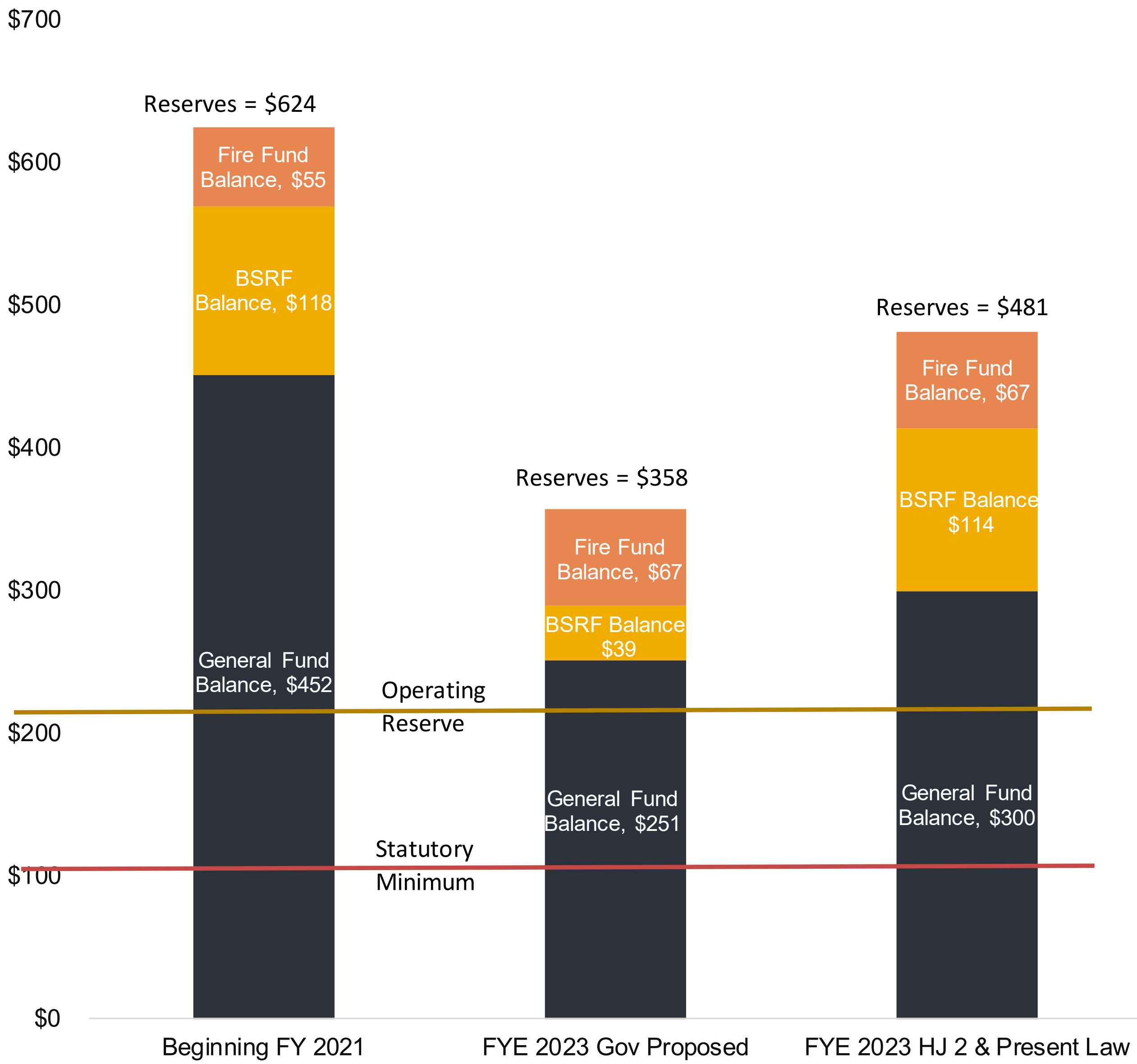
More information on the Long-Range Planning programs and the executive proposal for Montana Infrastructure is available in Section F of the Legislative Budget Analysis.

EXECUTIVE RESERVE BALANCE RECOMMENDATIONS AND HJ 2

The executive proposed ending fund balance for FY 2023 is $251.0 million which is above the recommended operating reserve by about $40.0 million. In order to end FY 2023 with a fund balance of $251.0 million, the executive proposed using $75.0 million from the budget stabilization reserve fund.

The table below shows the change in reserves from beginning FY 2021 to ending FY 2023 as proposed by the executive. General fund ending fund stays well above the statutorily required minimum of about $104.0 million, but the budget stabilization reserve fund declines by 66.9%. The total reserves are reduced from $624.0 million or about 24.6% of annual revenues to $358.0 million or 14.1% of annual revenues.

The Office of Budget and Program Planning balance sheet revenue is $54 million below HJ 2.



GENERAL FUND REVENUES THROUGH THE 2023 BIENNIUM

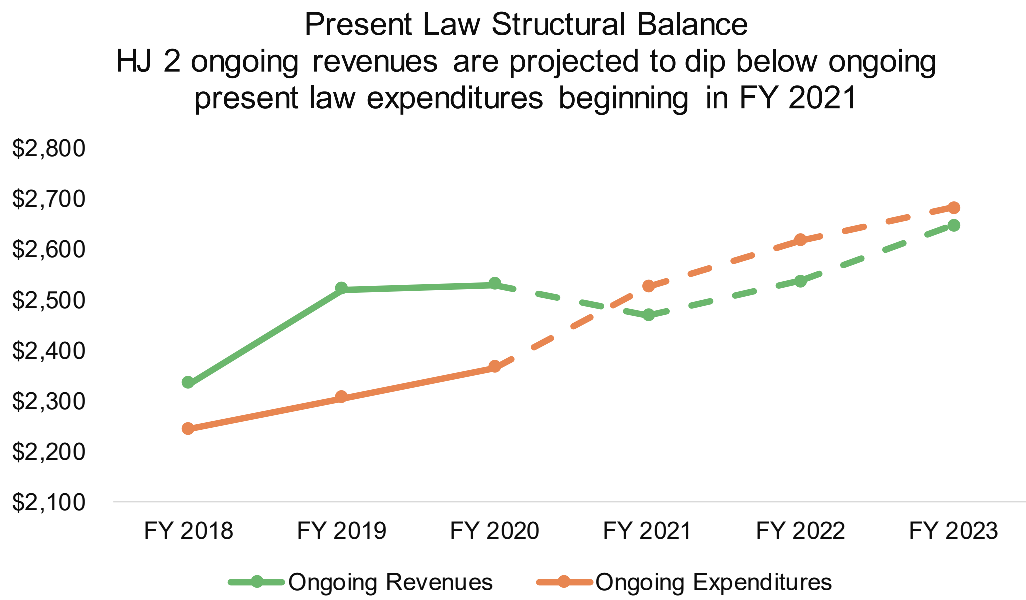
General fund revenue collections face a significant amount of uncertainty going into the 2023 biennium. This is driven by uncertainty associated with economic forecasts from IHS as well as how taxpayers will choose to utilize the tax provisions of the federal Coronavirus Aid, Relief, and Economic Security (CARES) Act.

Mitigating Expenditure and Revenue Risk

The ability of the state to mitigate both expenditure and revenue risk by using the budget stabilization reserve fund or other tools, like using the wildfire suppression fund, provide one-time options against financial risk. At present, the fire fund ending fund balance is anticipated to be $67.3 million at the end of FY 2023. Deposits into the fire fund are dependent on reversions of unspent appropriations from FY 2021 and each year after. The Governor has proposed limiting transfers into the fire fund in LC 850 and the LFD assumes no transfers of general fund into the fire fund on August 15, 2021.

STRUCTURAL BALANCE OF PRESENT LAW

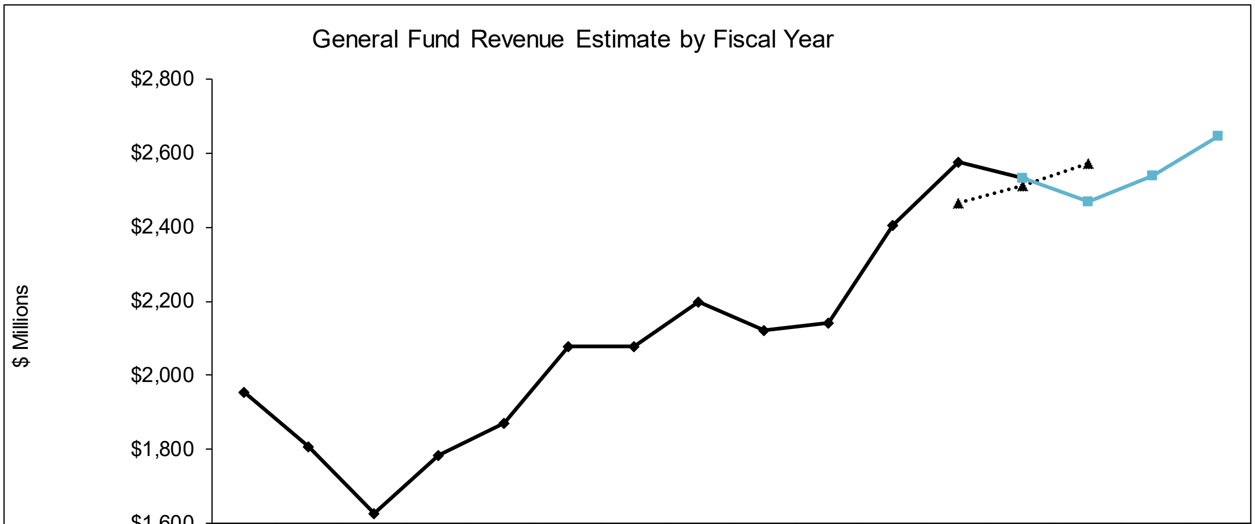
While Governor Bullock made recommendations for present law and new proposals, the legislature will evaluate both present law and new proposals during its budget deliberations. While the Legislative Fiscal Division will be describing issues with some of the present law items in the budget, it is closer to the minimum level of spending that the legislature will need to adopt without changing statute.



The structural balance using HJ 2 and the Governor Bullock's present law budget is ($36) million or (1.4%) in FY 2023. While a structurally balanced budget is ideal, in times of uncertainty a slight structural imbalance may be a reasonable financial approach to managing the budget.

General Fund Revenue Estimates Adopted by Revenue Interim Committee

In November 2020, RIC heard the revenue estimate recommendations from OBPP and LFD. The committee adopted the LFD estimate recommendation, with a few downward adjustments. The final, three-year HJ 2 estimate is $54 million higher than OBPP's balance sheet revenues.



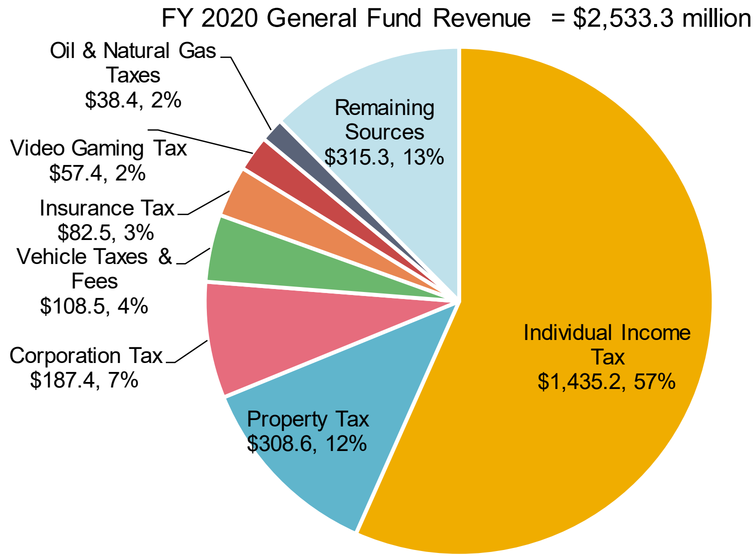
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Actual	1,954	1,808	1,627	1,783	1,871	2,078	2,077	2,200	2,121	2,141	2,405	2,576	2,533			
2019 HJ 2												2,466	2,513	2,573		
2021 HJ 2													2,533	2,469	2,538	2,648

The table below shows the annual detail for the top seven general fund revenue sources and subtotal of remaining sources, as well as a breakout of ongoing and one-time-only revenue.

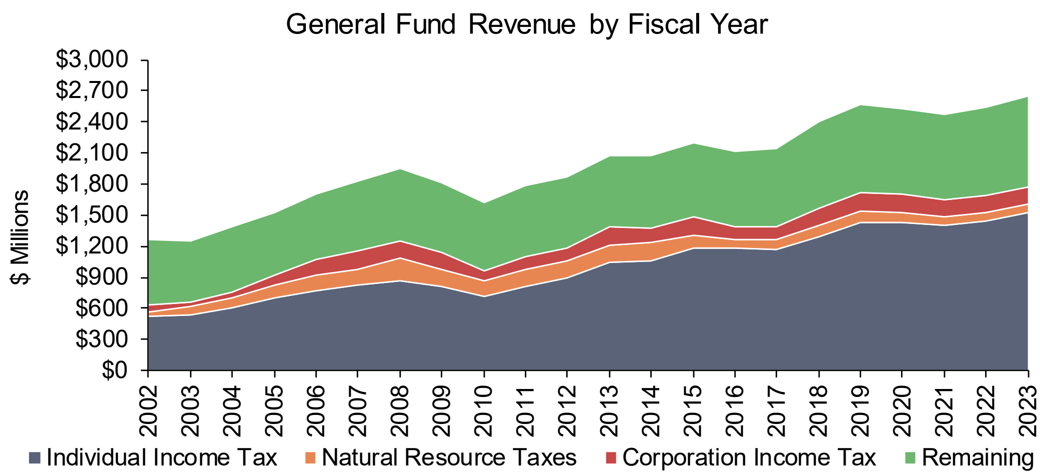
General Fund Revenue Estimates as Adopted by RIC ($ Millions)						
Source of Revenue	Actual FY 2020	Estimated FY 2021	Estimated FY 2022	Estimated FY 2023	Estimated 2021 Bien	Estimated 2023 Bien
Individual Income Tax	$1,435.2	$1,404.6	$1,443.8	$1,523.2	$2,839.8	$2,966.9
Property Tax	308.6	313.0	333.0	339.8	621.6	672.8
Corporation Income Tax	187.4	156.3	163.5	168.8	343.6	332.3
Vehicle Taxes & Fees	108.5	109.3	110.4	111.4	217.8	221.8
Oil & Natural Gas Production Tax	38.4	36.5	40.4	41.0	74.9	81.4
Insurance Tax & License Fees	82.5	86.1	84.8	87.8	168.6	172.5
Video Gambling Tax	57.4	60.3	63.3	66.5	117.8	129.8
Remaining Sources	311.2	303.2	298.5	309.2	614.4	607.7
Ongoing Revenue Subtotal	2,529.2	2,469.2	2,537.7	2,647.7	4,998.5	5,185.4
OTO Revenue & Transfers Subtotal	4.1				4.1	-
Total General Fund	$2,533.3	$2,469.2	$2,537.7	$2,647.7	$5,002.6	$5,185.4

GENERAL FUND REVENUE

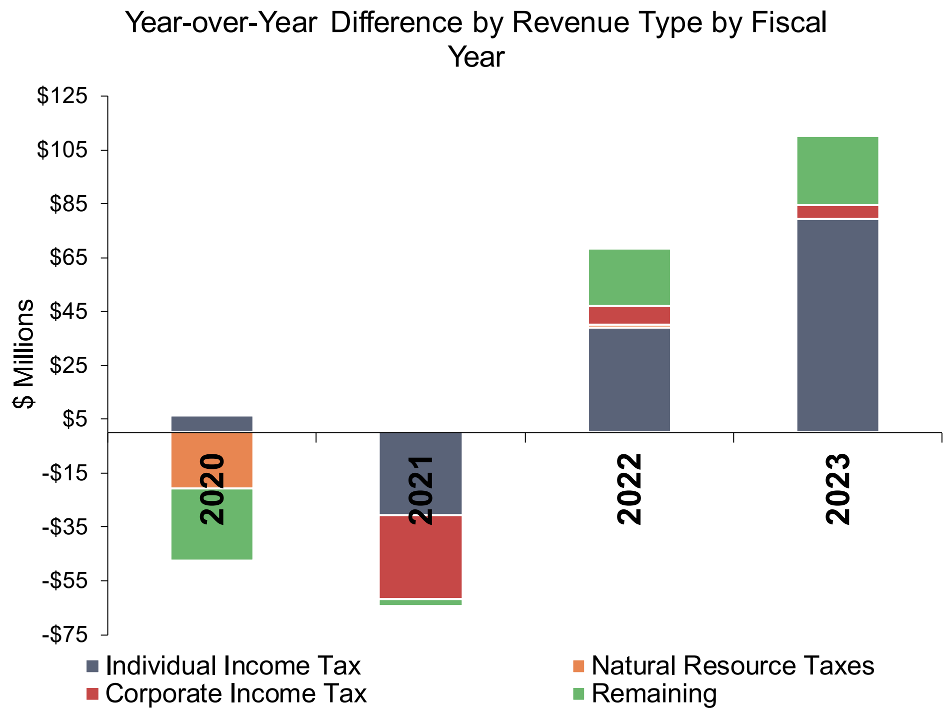
The largest seven sources of general fund revenue are individual income tax, property tax, corporation income tax, oil and natural gas taxes, vehicle taxes, insurance tax, and video gambling tax. In FY 2020, these sources accounted for 87.6% of general fund revenue. Details of all general fund and selected non-general fund revenue sources are contained in the Legislative Fiscal Division's [2023 Biennium Budget Analysis: Volume 2](#).



Individual income tax has been a growing share of total general fund revenue since FY 2002, as illustrated in the chart below. In FY 2002, it accounted for 40.9% of general fund revenue; by FY 2020, it grew to account for 56.7%. Based on the revenue estimates adopted by RIC, it is anticipated to grow to 57.5% of general fund revenue by FY 2023.

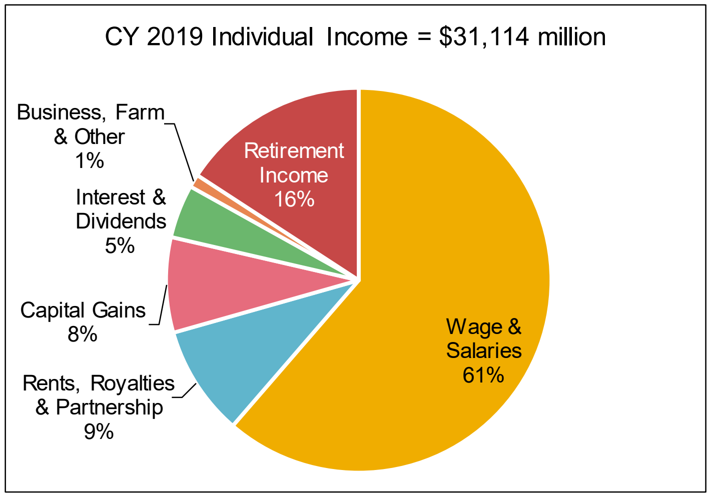


The following chart shows the year-over-year difference by the three largest contributing sources to volatility. Natural resource revenues declined substantially in FY 2020 and are expected to remain flat throughout the biennium. As a result, the year-over-year changes in HJ 2 are primarily due to growth/decline in income taxes.



The following section provides a brief summary on some of the significant economic drivers and their influence on the general fund of several key sources. More details on all sources of revenue can be found in the Legislative Fiscal Division's 2023 Biennium Budget Analysis: Volume 2.

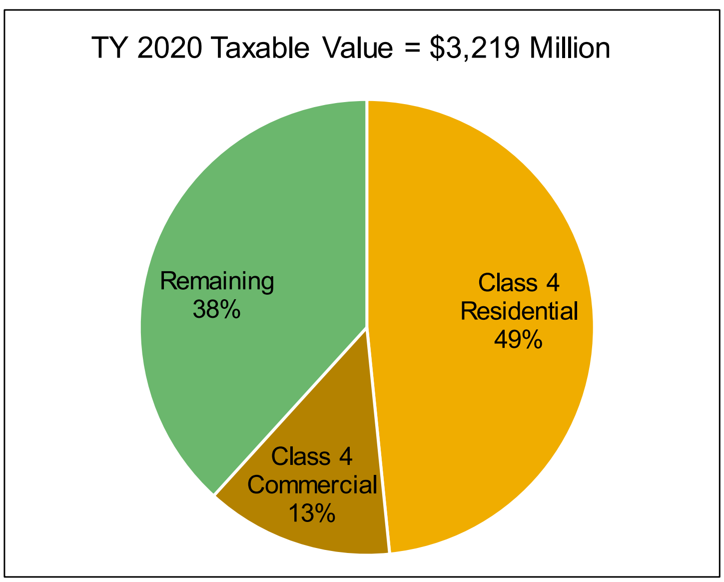
INDIVIDUAL INCOME TAX



The individual income tax is levied against taxable income, which is defined as total Montana income adjusted for exemptions and deductions. In 2019, full year resident income totaled $31.1 billion. Once tax liability is determined, the amount of tax due is computed by subtracting allowable credits. Tax rates vary from 1.0% to 6.9%, depending on the level of taxable income.

Tax brackets, personal exemption amounts, and the standard deduction are adjusted by the rate of inflation in each year. The effective tax rate on capital gains income is less than the tax rate on ordinary income by 2%, due to the 2% capital gains tax credit. Wage income accounts for over 60% of total individual income, while withholding tax on wages accounts for about one-third of total general fund revenue. Even in the midst of the COVID-19 public health emergency, wage growth is expected to remain fairly resilient, with only a modest drop of 0.6% in CY 2020 followed by growth rates approaching 4.0% in the out years. Other sources such as interest income, capital gains, and partnership income are expected to see steeper declines in CY 2020.

The Federal CARES Act provided additional tax provisions for corporations and small businesses to offset business losses. These provisions allow for net operating loss (NOL) carrybacks beyond what was previously allowed and removed the threshold on non-business income that could be offset with business losses. These provisions could result in large refunds in the spring of CY 2021. However, it is possible that the federal CARES Act stimulus money received by individuals may prevent significant losses from being realized. How taxpayers ultimately choose to use these provisions will likely not be known until the beginning of May after April revenues are known.



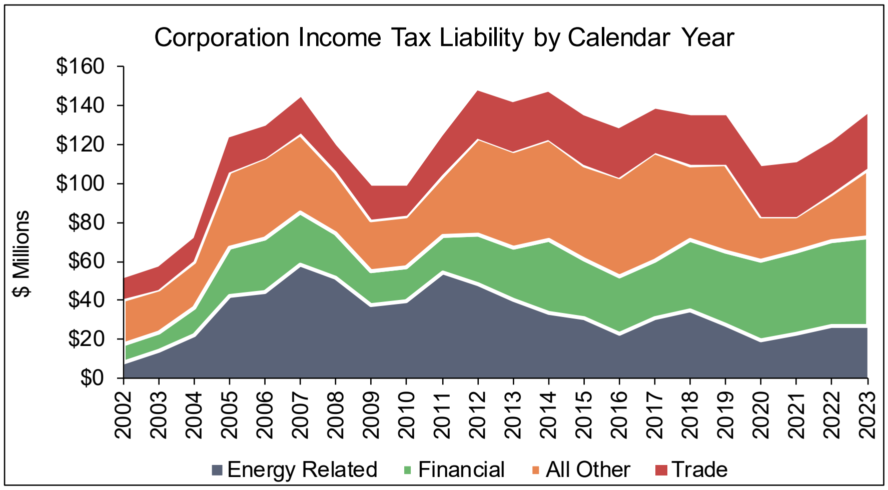
PROPERTY TAX

Montana law requires counties to levy a county equalization levy of 55 mills, a state equalization levy of 40 mills, and 6 mills for the university system against all taxable value in each county. A mill levy of 1.5 mills is also applied against all property in the five counties with a vocational technology (vo-tech) college. Taxable value is defined as the market value of statutorily defined property times a statutory tax rate.

Class 4 commercial and residential property, and class 3 agricultural property, are reappraised every two years with no phase-in of the new value. Class 10 timber land is on a six-year reappraisal cycle with a 1/6th phase in of value per year. Agricultural land and timberland continue to be valued on a productivity basis.

In addition to the tax on property, this revenue component includes collections from "non-levy" sources that are distributed based on mills levied by taxing jurisdictions. These non-levy sources include the state share of coal gross proceeds taxes, federal forest revenues, and other smaller revenue sources.

CORPORATE INCOME TAX



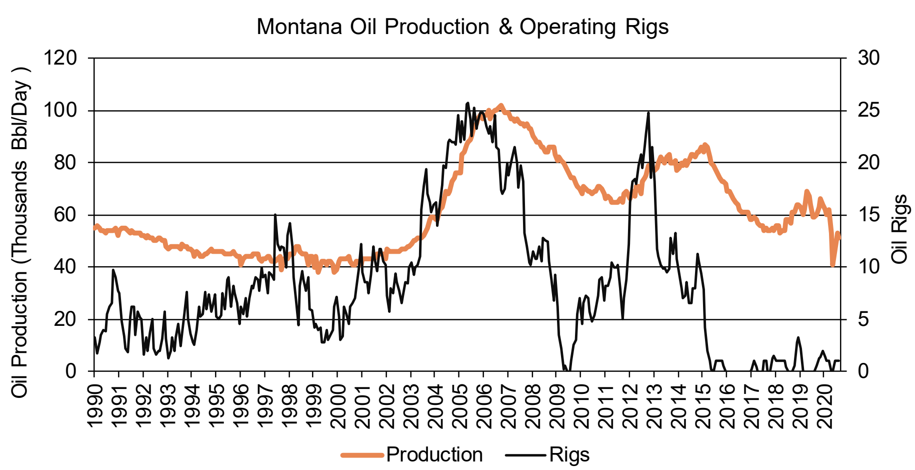
The corporate income tax is levied against a corporation's net income earned in or attributable to Montana, adjusted for allowable credits. Financial, retail, and energy related sectors are the largest sources of tax liability. Primary economic drivers of this source include oil prices, median house price, and retail sales. The tax rate is 6.75%, except for corporations making a "water's edge" election (see 15-31-322, MCA), who pay a 7.0% tax on their net income

Corporation income tax revenues are quite volatile from year to year, resulting in a revenue stream that is difficult to predict. The volatility can be attributed to many factors: sensitivity of corporation income to business cycles, industry composition in the state, reliance on a limited number of large taxpayers, and federal and state tax policy.

As noted in the individual income tax section, the CARES Act provides small businesses and corporations the ability to carry back net operating losses (NOL's) up to five years for losses in incurred in CY's 2018, 2019, and 2020. Prior to the CARES Act, these losses could be used to offset 80% of taxable income but can now offset 100% of taxable income.

In the 2017 Legislative Session, HB 550 was passed. This bill capped NOL carrybacks at $500,000 while allowing corporations to move losses back three years and forward ten years. As a result, the CARES Act provisions will not be nearly as influential for corporate income tax in terms of refunds this fiscal year, as significant losses exceeding $500,000 will need to be moved forward to future tax years.

OIL & NATURAL GAS PRODUCTION TAX



The oil and natural gas production tax is imposed on the production of petroleum and natural gas in the state. The gross taxable value of oil and natural gas production is based on the type of well and type of production, and whether the production occurs within the tax holiday.

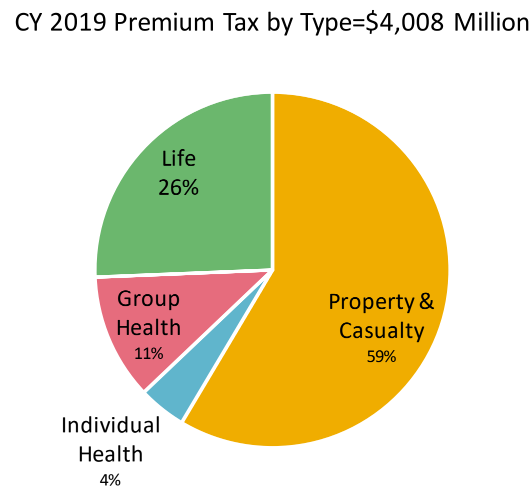
Since the beginning of FY 2016, there has been at most four drilling rigs operating in the state, as shown in the chart above. As prices increased in the fall of CY 2018, increased production followed. However, prices plummeted in the spring of CY 2020, causing a sharp drop in production before a recent rebound.

In the 2023 biennium revenue from this source is anticipated to remain relatively flat. HJ 2 assumes West Texas Intermediate oil prices per barrel of $42 in 2021, $51 in 2022, and $56 in 2023, but the increased prices are expected to be offset by a decrease in production.

INSURANCE TAX

Most insurance tax collections come from 2.75% tax on net premiums sold. There is an additional 2.5% tax levied on fire insurance premiums sold, and several small fees.

The adjacent chart illustrates the share of premiums written by major type of insurance. In CY 2019, property and casualty insurance accounted nearly 60% of premiums written.



Total taxes and fees are calculated by summing the forecasts for premium taxes and all other fees as estimated individually. Premium taxes are forecast with a regression model using the independent, IHS Markit-provided values for the Montana personal consumption expenditure (PCE) series for finance and insurance. Changes in health insurance spending due to the Affordable Care Act are assumed to be captured in the IHS Markit forecast of Montana PCE for finance and insurance. Estimates for the various fees are based on time trends or an assumption of no growth.

EXECUTIVE REVENUE PROPOSALS

LC 851: Eliminate Natural Resource Operations State Special Account and redirect funds to General Fund

LC 851 proposes to eliminate the natural resource operations state special revenue account and redirect all funding previously designated for that account towards the general fund. Funding is generated from revenue collections from the metal mines tax, oil and natural gas production tax, and resource indemnity trust fund interest. If passed, the general fund would receive approximately $2.1 million in additional revenue in both FY 2022 and FY 2023.

LC 943: Eliminate allocations of severance taxes to several state accounts

LC 943 proposes to eliminate funding from the coal severance tax to several state special revenue accounts, as well as eliminate the statutory appropriations of general fund revenue from the coal severance tax permanent trust fund interest. The state special revenue accounts that would be eliminated are the basic library services account and the conservation district account, while the eliminated general fund statutory appropriations would impact funding for the department of agriculture. If passed, the revenue that previously funded the eliminated state special revenue accounts would then be redirected to the general fund, per MCA 15-35-108. Additionally, the previously statutorily appropriated amount ($3.365 million) of general fund money from the coal permanent trust interest would be available for general use. The overall positive revenue impacts to the general fund would be approximately $2.08 million in FY 2022 and $2.04 million in FY 2023.

HB 2 FUNDING

HB 2 is the general appropriations bill, in which the executive proposes the majority of general fund and total funds appropriated by the legislature in the 2023 biennium.

An interactive data visualization product provides a look at funding charts and appropriation comparisons between the 2021 biennium legislative appropriated budget and the Governor's proposed 2023 biennium budget.

Use and view the data tool available at this location: https://app.powerbigov.us/groups/d45b719a-aa9b-4bdf-9af0-4b43ec0b4cbb/reports/c15684c0-f2a9-4015-a52b-e574f74b238f?ctid=5fc35298-4211-4054-8678-b3281c397267

Section A – General Government

Department of Administration

The 2019 Legislature adopted $6.3 million in general fund increases to fund the Montana cybersecurity enhancement project in the State Information Technology Services Division. The project included operating expenses and personal services related to 10.00 FTE. Governor Bullock proposes to refinance cybersecurity enhancement using proprietary fund rates instead of general fund. The new proposal reduces general fund by $3.0 million in FY 2022 and $3.0 million in FY 2023.

Section B – Public Health and Human Services

The DPHHS budget proposal increases by $109.7 million general fund in the 2023 biennium. However, as compared to the 2021 base, the growth is only $31.6 million.

Medicaid is often a major driver of budget increases in Section B. In the executive budget, the total biennial Medicaid present law change from the base is a ($33.7) million reduction. However, due to a variety of funding shifts occurring within the Medicaid present law request, the general fund increases by a slight $231,000 in spite of the overall decrease. For a more detailed analysis of these funding shifts, see the Agency Summary of the DPHHS Budget Analysis.

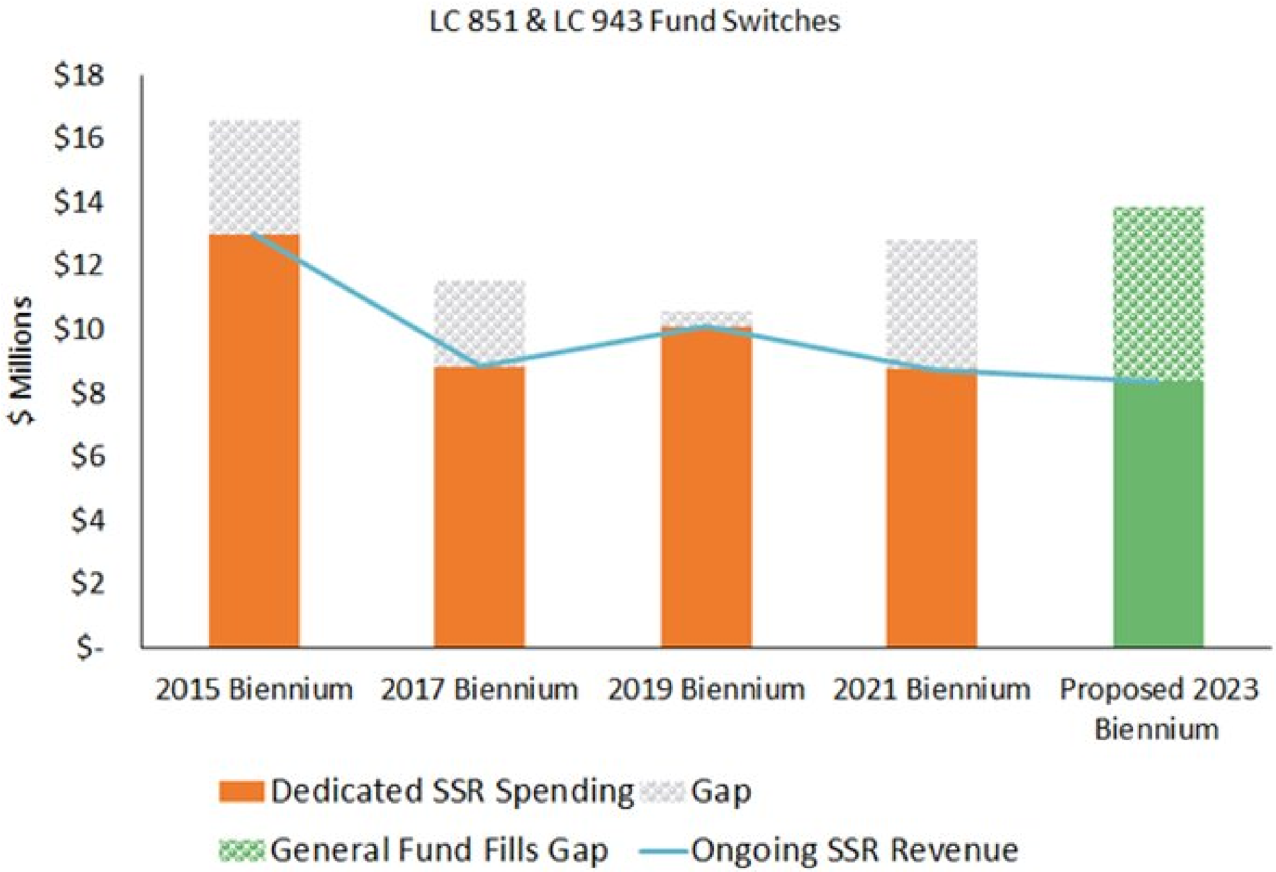
Another requested funding shift for the Children's Health Insurance Program (CHIP) has been discussed and anticipated by previous legislatures but will need to be considered by the 2021 Legislature. Due to a declining fund balance, $8.4 million would be shifted from the CHIP state special revenue fund to the general fund in FY 2023.

Early childhood education has again been included in the executive proposal at a cost of $10.0 million general fund in the biennium.

Also, of note is a proposal for an additional $6.4 million general fund to pay for operating costs associated with the MMIS/MPATH data systems for managing Medicaid information and an overall data warehousing application.

Section C – Natural Resources

Two proposals by Governor Bullock impact natural resource agencies. LC 851 proposes elimination of the natural resources operations state special funding and replace it with general fund revenue. Another proposal, LC 943 proposes to eliminate the distribution from coal severance taxes and replace it with general fund revenue. The following chart shows state special revenue derived from natural resources eroded over time. The chart also illustrates the gap between the state special revenues and the appropriations in gray. When state special revenue is not adequate for appropriations, spending must drop to match revenue or fund balances may be used to make up the difference. Once fund balances are exhausted, expenditures must stay in line with revenues. Finally, the chart shows how general fund will fill in the gaps between revenue and spending needs.



Section D –

Department of Corrections

With an overall proposed increase in general fund of $23.5 million, DOC has several significant requests.

Hepatitis C treatments for offenders in secure facilities is a national issue that is currently being considered required by states. This is a costly treatment for which DOC has requested $5.1 million for the 2023 biennium.

To provide security and services to a growing offender population often means adding personnel. DOC is requesting a total of 39.00 FTE at a general fund cost of $4.2 million.

Judicial Branch

Another area requesting FTE for the coming biennium, the Judicial Branch has proposed an increase of 19.75 FTE at a general fund cost of $1.3 million in the 2023 biennium. Some of these FTE would be phased in, so total ongoing biennial cost would be higher.

Office of the Public Defender

OPD has traditionally seen caseload growth drive budget increases, and in the 2023 biennium, the total general fund increase for this purpose is $2.4 million.

Section F – Long Range Planning and Infrastructure

Governor Bullock has proposed reducing capital development present law general fund transfers by approximately $30 million for the 2023 biennium. This reduces pay as you go infrastructure and replaces it with $91.5 million of state and local government capital development bonds with an estimated general fund debt service cost in the 2023 biennium of $2.4 million.

GOVERNOR'S PROPOSED OTHER LEGISLATION GENERAL FUND ONLY

Other than HB 2, Long-Range Building, statutory authority, and non-budgeted changes described in previous sections, the executive proposes other legislation that impacts general fund. The following figure illustrates the general fund executive proposals.

2021 Biennium Executive Proposed General Fund Legislation $ Millions			
General Fund Revenue Legislation	FY 2021	FY 2022	FY 2023
LC# 850 Transfer Budget Stabilization Reserve Fund to General Fund, one-time-only revenue		$37.5	$37.5
LC# 851 Redistribute revenue to general fund		2.2	2.2
LC# 943 Eliminate coal severance tax allocations		2.2	2.2
General Fund Revenue Legislation Total		$41.9	$41.8
General Fund Expenditures	FY 2021	FY 2022	FY 2023
HB 1	*$9.3*	*$2.5*	*$11.4*
HB 2 (language appropriations only) - unavailable at time of publication, estimated		*0.1*	*0.1*
HB 3 Supplemental Appropriations	16.4		
HB 10 Long Range Information Technology		5.0	
HB 13 Employee Pay Plan		0.7	7.8
HB 14 Funding and Authorization for Capital and Infrastructure (executive estimate for GO debt)		0.4	2.0
General Fund Expenditure Legislation Total		$8.7	$21.2
Note: HB 13 difference between executive balance sheet and this table is $75,000.			

Revenue Impacts

- LC 850 one-time transfer of $75.0 million to the general fund from the budget stabilization reserve fund
- LC 851 eliminate natural resource operations fund distribution, re-distribute to the general fund
- LC 943 eliminate coal severance tax allocations, retain in the general fund

Expenditure Impacts

- HB 1 Feed Bill – new proposal of $13.0 million (the table reflects the new proposal, plus funding from the 2019 session that carries into the 2021 session and estimated appropriations for the 2023 session)
- HB 2 Language Appropriations – Unavailable at the time of publication, estimated
- HB 3: The executive proposes supplemental appropriations that are discussed in further detail in a later section of this volume.
- Infrastructure bills: HB 10 proposals to transfer general fund to the long-range information technology. HB 14 proposes the issuance of bonds. The cost for the new general obligation debt as estimated by the executive is included in the table. More detail is provided in Section F of the 2023 Biennium Budget Analysis
- HB 13
    - The executive proposes a longevity increase for state employees with 25 years of uninterrupted service
    - Employee base pay as determined on June 30, 2021 to be increased by 55 cents per hour on November 15, 2022
    - $1.0 million has been proposed to provide for personal services shortfalls that may occur in the 2021 biennium and may be used at the discretion of the executive

References

The Governor's Budget is found on the Office of Budget and Program Planning's website: http://budget.mt.gov/Budgets/2023_Budget-Page

FY 2021 SUPPLEMENTAL REQUESTS

Executive Proposal

The executive is requesting $16.4 million general fund in HB 3 supplemental appropriations for FY 2021.

Department of Revenue

In anticipation of summary judgement in the case of L.L. Liquor v. State of Montana et al, United States District Court District of Montana, Case No. CV 15-71-H-SHE, the Department of Revenue is requesting $5.6 million general fund.

Anticipation of costs associated with implementation of state revenue collections for recreational marijuana, the department is requesting $6.3 million to update the tax database systems.

Office of Public Instruction

Due to projected revenue declines associated with the economic uncertainty, the Office of Public Instruction anticipates a decline in guarantee fund revenue that provides a portion of K-12 education funding and is requesting $4.5 million to cover the shortfall.

LAWSUITS

L.L. Liquor v. State of Montana et al, United States District Court District of Montana, Case No. CV 15-71-H-SHE

The Department of Revenue is requesting $5.6 million in supplemental appropriation authority for FY 2021 for summary judgement costs in the case of L.L. Liquor v. State of Montana et al, United States District Court District of Montana.

In 2015, the Legislature passed Senate Bill 193 (SB 193). The bill repealed the old commission rate structure for agency liquor stores, having a positive fiscal impact for 90 of the 96 agency liquor stores. One of the 6 stores that would see less profit from SB 193, L.L. Liquor, Inc. d/b/a Lolo Liquor, filed a Complaint in the First Judicial District Court on May 26, 2015, naming as Defendants: State of Montana; Steven Bullock, in his official capacity as the Governor of Montana; Montana Department of Revenue; and Mike Kadas, in his official capacity as the Director of the Montana Department of Revenue.

In the Complaint, Lolo Liquor alleged that SB 193: (1) violated the contracts clauses of the United States and Montana Constitutions; (2) breached the agency franchise agreements and breached the covenant of good faith; (3) resulted in an unconstitutional taking; and (4) violated Lolo Liquor's due process rights. On July 23, 2015, the department removed the case to the Montana Federal District Court based upon federal question jurisdiction as allowed in 28 U.S.C. § 1331.

As the named defendant, the department defended on the basis that the agency liquor store contract signed by LL Liquor indicated that the commission rates could change at any time based upon changes to those commission rates made by the Legislature.

The Federal Courts' Decisions

On April 25, 2017, Judge Haddon granted the department's summary judgment motion that there was no breach of contract, and on May 11, 2017, Lolo Liquor filed a Notice of Appeal with the 9th Circuit Court of Appeals.

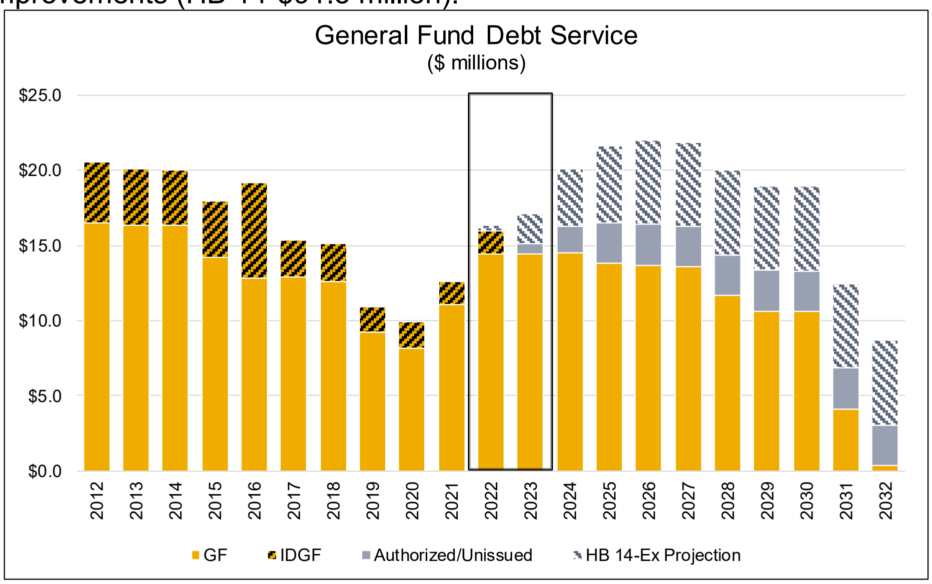
On December 28, 2018, the 9th Circuit upheld Judge Haddon's decision that SB 193 did not violate the contracts clauses of the Montana and United States Constitutions. However, the Court held, in an unpublished opinion, that the changes to the commission rates resulted in a breach of the Agency Franchise Agreement with Lolo Liquor and the Court remanded the case back to Judge Haddon to determine damages and statutory attorney fees.

DEBT SERVICE

Montana's debt liability is relatively low and unless additional bonds are issued or approved, the payment streams of the currently issued general fund general obligation bonds (GFGO) will end in FY 2041. Montana ranks well when compared to other states' tax supported debt, according to a report by Moody's Investor Services, the May 2020 Moody's Debt Medians Report. In comparison with the 50 states, with lower debt states having a higher rank, Montana ranks as follows:

- 47th in net tax supported debt (thousands); $113,753
- 47th in tax supported debt per-capita; $106
- 47th in net tax supported debt as a percent of personal income; 0.2%

The following table illustrates current debt service and includes projections for authorized but unissued debt service, as well as projections in the executive proposal to authorize bonds for state and local infrastructure improvements (HB 14-$91.5 million).



- Gold-GF – General obligation (GO) bonds paid by the general fund. The bond issues related to this debt service primarily funded the construction of state government buildings and beginning in FY 2019 local government infrastructure projects ($30.2 million in the 2023 biennium)
- Gold Hatched IDGF – This category includes special revenue bonds that are paid indirectly through the general fund. The related bond issue covered the costs of improvements at Montana State Hospital. Debt service on this bond is paid by funds that would otherwise flow into the general fund. The issue is expected to be paid in full in FY 2022 ($1.5 million in the 2023 biennium)
- Grey (Authorized/Unissued) – This category includes the projections for debt services costs on authorized but unissued bonds ($38.3 million of authority). The bonds are authorized for the costs of two tribal compacts, the St. Mary's diversion system improvements, and the balance of the bonds authorized by the 2019 Legislature (HB 652). With uncertainty for when these bonds may be issued, only the remaining authority for HB 652 is projected to be issued in the 2023 biennium, the remainder is projected to be issued in the 2025 biennium ($0.7 million in the 2023 biennium)

- Black Hatched (HB 14-Ex Projection) – This category illustrates the debt service costs of the HB 14 as shown on the executive balance sheet ($2.4 million in the 2023 biennium)

In the 2023 biennium, the debt service paid directly and indirectly through the general fund for existing bond issues is expected to be $16.0 million in FY 2022 and $15.1 million in FY 2023. The debt service for executive proposal in HB 14, as calculated by the executive, is based on 20-year maturities and are expected to be sold in five issues. The bonds are projected to have a general fund debt service cost of $0.4 million in FY 2022 and $2.0 million in FY 2023. Including HB 14, total debt service is expected to be $16.4 in FY 2022 and $17.1 million in FY 2023. Once all bonds are issued, the projected annual cost HB 14 debt service would be $5.6 million per year.

DEBT LIMITATIONS

In the work of the 2019 Legislature, 17-5-802, MCA now imposes two limits on the legislative ability to authorize GFGO bonds. The limits include:

1. A prohibition on the legislature from authorizing new GFGO bonds if state debt is greater than 0.6% of the fair market value of all property within the state ($1,114.5 million in the 2023 biennium), and
2. A prohibition on the legislature from authorizing new GFGO bonds if the annual fiscal year costs of the current and proposed GFGO debt service would exceed 1.5% of annual general fund revenues, measured at 7/1/2020 ($38.0 million).

In the 2023 biennium, the executive proposal for HB 14 is well within both limits.