LFD Analysis of Proposed Spending Reductions
Overview

A Report Prepared for the

Legislative Finance Committee

By

Legislative Fiscal Division

September 29, 2017

MONTANA LEGISLATIVE BRANCH

Legislative Fiscal Division

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September 29, 2017

Members of the Legislative Finance Committee:

The legislature has provided a statutory requirement that the executive take action to reduce spending in the event of a general fund budget deficit. The executive announced a potential budget deficit on August 30, 2017, and submitted a spending reduction plan to bring the projected ending fund balance above the minimum required by 17-7-140, MCA when using the Governor's Budget Office revenue forecast.

In accordance with 17-7-140, MCA, I submit the Legislative Fiscal Division analysis of the executive spending reduction plan. It is our goal that this analysis will provide the information necessary for committees and legislators to provide informed input to the current budget situation. This report includes:

- An overview of the agency spending reduction recommendations
- Appendix A: The Budget Director's agency spending reduction recommendations in detail along with the Legislative Fiscal Division's analysis and comments on the various components of the executive reduction plan
- Appendix B: A legal memorandum from the Legislative Services Division legal staff summarizing the legal analysis of the proposed reductions
- Data tables

On behalf of the Legislative Fiscal Division, I want to thank the legal staff of the Legislative Services Division for their expert advice and assistance in drafting this document.

Please let me know if there is any further analysis that will be helpful to the committee.

Respectfully submitted,

Amy Carlson
Legislative Fiscal Analyst

INTRODUCTION

EXECUTIVE SUMMARY

Purpose of the Report - 17-7-140, MCA

The authority to appropriate state funds rests solely with the Montana legislature in accordance with the state constitution. That authority cannot be delegated. However, since the legislature only meets regularly in session for 90 days in a two-year period, the legislature adopted a law to ensure that there is a method available to the executive branch to prevent the occurrence of a budget deficit. In the 1993 legislative session, the legislature passed 17-7-140, MCA requiring the Governor to initiate spending reductions if there is a projected budget shortfall that threatens a deficit budget picture.

On August 30, 2017, the Governor's Office formally announced concerns about a budget deficit, and initiated proceedings to implement spending reductions in accordance with 17-7-140. The following describes the statutory requirements of 17-7-140, MCA.

The Governor is required by statute to implement spending reductions in the event of a projected deficit in the general fund ending fund balance, and must direct sufficient reductions to achieve a required minimum ending fund balance. The Governor's Budget Director submitted a spending reduction plan on September 19, 2017 and designated legislative committees are statutorily allowed 20 days to provide comments and recommendations on the proposed plan to the Governor. The Governor can then implement the reduction plan. The Legislative Finance Committee (LFC) will meet on October 4-5, 2017 to evaluate and comment on the executive proposed spending reductions. The Revenue and Transportation Committee (RTIC) met on September 14, 2017 to comment on the executive revenue estimates used to certify a deficit. The motion adopted by the RTIC follows:

> The committee acknowledges the importance of responding as soon as possible to this development, but also recognizes that estimating revenue early in the biennium introduces uncertainty into the estimates. Accordingly, the committee recommends the Governor and the Legislative Fiscal Division continue to monitor collections and projections closely.

The Governor tentatively plans to implement the spending reduction plan after taking into consideration the public comments and recommendations of the legislative committees.

The purpose of this report is to provide the Legislative Finance Committee with an independent analysis and summary of the proposed executive spending reduction plan, as required by 17-7-140, MCA. The report provides an overview of the proposed spending reductions, Appendix A provides a complete listing and description of the executive spending reduction plan by agency, as well as LFD staff analysis, comments, and issues on the spending plan. Appendix B includes a legal memorandum from the legislative legal staff summarizing the legal analysis of the proposed reductions.

Executive Ending Fund Balance

The executive projected ending fund balance for the current biennium is ($84.3) million. The executive revenue estimates used for the executive's projected ending fund balance are lower than HJ 2 by $282.0 million. For the purpose of implementing 17-7-140 spending reductions, the executive projection is used.

Executive Spending Reduction Plan

The executive spending reduction plan proposes $366.2 million in reductions including $227.9 million in general fund and $136.2 million in proposed reductions to federal matching funds.

The LFD analysis breaks the $366.2 million in reductions into three groups:

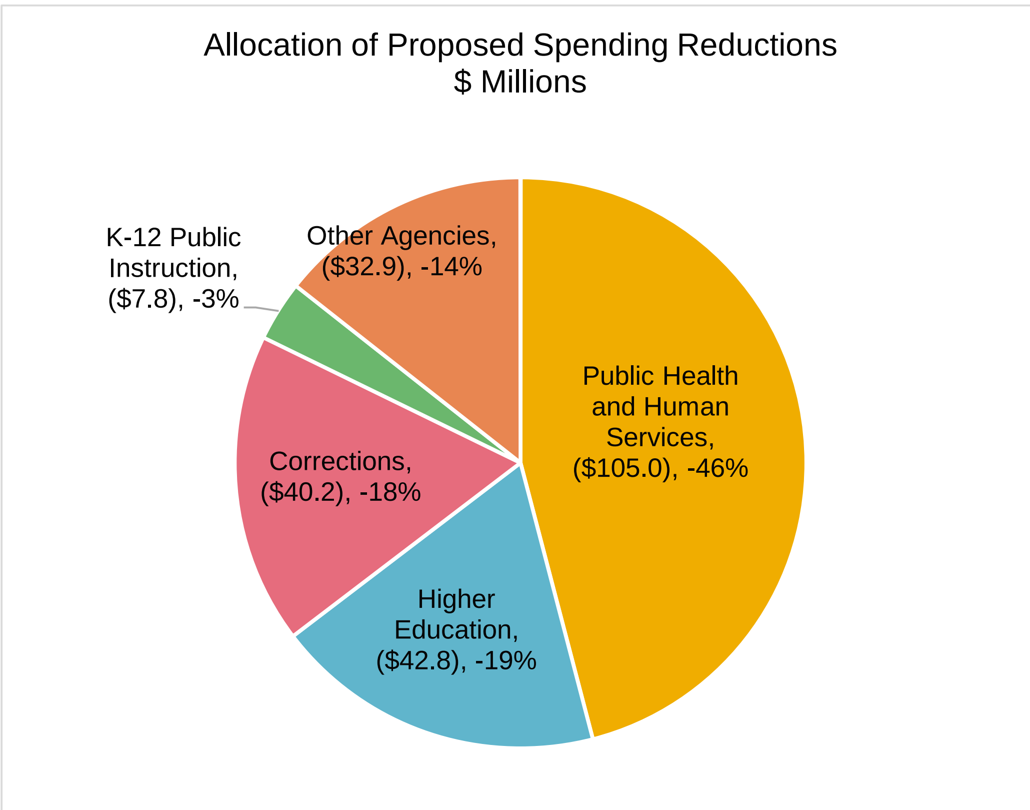
- $345.6 million of agency reductions per MCA 17-7-140

- $600,448 in reductions to non-general fund to increase general fund balance
- $20.0 million of reductions requiring legislative actions, see figure 2

Using executive assumptions of revenue and expenditures, if all proposed executive reductions were implemented, the executive's FY 2019 general fund ending fund balance would improve from ($84.3) million to $144.9 million. Statute requires the executive provide an ending fund balance above the minimum balance of 5%. The updated fund balance needs to be 6% or $142 million. The executive plan, when applying the executive's own revenue estimates and all the proposed executive reductions, meets the required minimum ending fund balance. This does not include legislative and judicial reductions noted on page

Under the executive analysis the reductions average 9.6% of eligible general fund appropriations for state agencies, with reductions of $105.0 million in human services (45.8% of total) and $42.8 million in higher education (18.7% of total). Federal funds would be reduced by nearly $136.2 million due to the loss of matching funds. Items requiring legislative action total $21.0 million.

The following chart shows the proposed reductions.



Limitations

The spending reduction statute (17-7-140, MCA) requires that general fund spending be reduced in order to ensure a minimum ending fund balance reserve, but provides a number of statutory limitations as to what reductions are allowed. The major limitations to the reductions the executive can make are as follows:

- An agency cannot be required to reduce spending in any program (as defined in the general appropriations act) by more than 10% during a biennium.
- Agencies headed by elected officials or the Board of Regents cannot be required to reduce spending by a percentage greater than that required of the average of all

other executive branch agencies.

- No reductions can be directed by the Governor in the following categories:
  - Payment of interest and principal and state debt
  - Legislative and Judicial Branch budgets
  - The school BASE funding program, including special education
  - Salaries of elected officials
  - Montana School for the Deaf and Blind

Legislative Role

The final assessment of the deficit projection and the required spending reductions are determined by the Governor, but statute requires specific communication with the Legislative Branch and an opportunity for legislative input prior to making the final directive. The Legislative Finance Committee must be afforded the opportunity to comment on planned spending reductions and the RTIC must be afforded the opportunity to comment on the revenue estimates used to determine the deficit. The statutory requirement for legislative interaction and input is summarized as follows:

- The Governor's Budget Director must notify the RTIC of the estimated amount of the general fund revenue shortfall below the revenue estimate established in the revenue estimating resolution for the affected biennium (this occurred September 14, 2017)
- The RTIC has 20 days from notification of the revenue shortfall to provide the Budget Director with any recommendations concerning the revenue estimates (this occurred on September 14, 2017)
- The budget director must consider the recommendations of the RTIC prior to certifying a projected general fund deficit
- Agencies must submit their assessment of spending reductions to the Legislative Fiscal Analyst (LFA) at the same time they are submitted to the Office of Budget and Program Planning (this submission occurred on September 8, 2017)
- The Governor's Budget Director shall provide a copy of his recommendations to the LFA at the same time they are submitted to the Governor (this occurred on September 19, 2017)
- The Legislative Finance Committee has 20 days from the time the planned reductions are submitted to the LFA to meet and make recommendations to the Governor (scheduled for October 4-5)
- The LFA must provide a copy of the LFD review of the proposed spending reductions to the budget director at least 5 days before the LFC meeting (scheduled for delivery on September 29, 2017)
- The Governor must consider the recommendations of the LFC prior to directing spending reductions

EXECUTIVE PROPOSED REDUCTION PLAN

OVERVIEW

This section provides a summary evaluation of the executive spending reduction plan. It also provides a summary view of the proposed reductions, intended to provide the reader with a general understanding of the major components of the reduction plan. It includes agency expenditure reduction highlights and types of reductions, plus a discussion of the impacts of those reductions.

AGENCY REDUCTION PLANS

The Budget Director is recommending that the Governor require agencies to reduce general fund spending by $227.9 million over the 2019 biennium. The LFD estimates this equates to an average reduction of 9.6% of general fund expenditures allowed to be reduced under 17-7-140, MCA, or 4.8% of the total 2019 biennium anticipated general fund expenditures.

When considering only HB 2 general fund appropriations for all branches of state government, after the impact of SB 261, the average reduction in total general fund expenditures is 5.9%. The following section discusses the proposed general fund spending reductions for the Executive Branch.

Please note that the School BASE Funding Program including special education expenditures in the Office of Public Instruction, the Montana School for the Deaf and Blind, and the Legislative and Judicial Branches are exempted from reductions by the Governor and are not included as part of the Budget Director's recommendations shown in Figure 1.

Figure 1

Executive Proposed Spending Reductions By Agency
General Fund
2019 Biennium

Agency	2019 Biennium General Fund*	2019 Biennium Reduction**	% Reduction
Governor's Office	$13,907,450	($1,290,839)	-9.282%
Commissioner of Political Practices	1,524,131	(152,414)	-10.000%
Office of Public Instruction	81,187,773	(7,770,617)	-9.571%
Crime Control Division	4,619,158	(461,916)	-10.000%
Department of Justice	68,542,177	(6,560,286)	-9.571%
Board of Public Education	298,995	(29,900)	-10.000%
Commissioner of Higher Education	449,281,893	(42,810,073)	-9.529%
Montana Arts Council	1,056,627	(105,663)	-10.000%
Montana State Library	4,418,359	(441,836)	-10.000%
Montana Historical Society	5,360,705	(230,731)	-4.304%
Department of Environmental Quality	10,389,281	(1,038,935)	-10.000%
Department of Livestock	5,108,311	(511,416)	-10.011%
Department of Natural Resouces and Conservation	54,339,812	(2,929,085)	-5.390%
Department of Revenue	105,641,482	(8,535,429)	-8.080%
Department of Administration	14,668,238	(1,459,332)	-9.949%
Office of the Public Defender	64,685,953	(6,471,590)	-10.005%
Department of Agriculture	1,520,586	(152,058)	-10.000%
Department of Corrections	402,028,523	(39,804,051)	-9.901%
Department of Commerce	7,255,023	(725,503)	-10.000%
Department of Labor and Industry	3,581,426	(358,270)	-10.004%
Department of Military Affairs	13,063,876	(1,071,022)	-8.198%
Department of Public Health and Human Services	1,050,308,010	(105,029,491)	-10.000%
Grand Total	$2,362,787,789	($227,165,457)	-9.614%

* SB 261 and workers' compensation appropriation reductions included.
** Program reductions above 10% included.

The overall reduction shown in Figure 1 is calculated using the weighted average. For reductions by agency and program refer Appendix A.

Included in the calculation above are pay plan and the SB 261 triggered general fund appropriation reductions of $53.6 million the FY 2017 revenues were lower than anticipated in HJR 2. All four trigger levels of reductions outlined in SB 261 were implemented in August 2017. Figure 1 shows each agency's reduction and percentage of the 2019 biennium HB 2 and SB 294 (pay plan) appropriations after the impacts of SB 261.

The Judicial Branch has voluntarily agreed to reduce its spending by $3.7 million over the biennium. The Legislative Branch intends to reduce its general fund spending by the same percentage as the average Executive Branch agency expenditure reduction required by the Governor.

Calculation of Percent of Reduction

Several Executive Branch agencies are headed by an elected official, including the Office of Public Instruction and the Department of Justice. The Montana University System (also part of the Executive Branch) is governed by the Board of Regents. According to 17-7-140, MCA, the Governor may not reduce the expenditures of an agency or department headed by an elected official or the Board of Regents "… by a percentage greater than the percentage of general fund spending reductions required for the total of all other Executive Branch agencies."

The calculation of this percentage is not specifically defined in statute, leaving the question of whether the executive has complied with statute open to different interpretations based on how the calculation is made. There are three separate types of issues:

- How to apply the percentage calculation[1] – weighted or non-weighted average
- Which general fund appropriations to include[2] – HB 2 appropriations only, HB 2 and statutory appropriations, or Executive Branch agency appropriations subject to reduction

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[1] ***Applying the Percentage Calculation***

There are two major ways to calculate the percentage reduction:

- Non-weighted average – using the percent reduction imposed on each agency equally applied. For example, the Department of Natural Resources and Conservation has HB2/SB 294 appropriations of $54.3 million in the 2019 biennium and is proposed to be reduced by 5.4%, and the Montana Arts Council with appropriations of $1.1 million is proposed to be reduced by 10.0%, the average reduction would be 7.7%.
- Weighted average – using the total reduction applied to all agencies to total appropriations. Using the above example the weighted average would be 5.4%

[2] ***General Fund Expenditures to Include***

General fund is appropriated in two primary ways: 1) temporary bills such as HB 2; and 2) statutory appropriations. The legislature also authorizes transfers from and to the general fund that do not require an appropriation. Within temporary appropriations, while HB 2 is by far the largest in most biennia, there are other bills that appropriate general fund for various purposes.

17-7-140, MCA, prohibits the Governor from directing reductions in spending for the following:

- School BASE Funding Program, including special education
- School for the Deaf and Blind
- Legislative Branch
- Judicial Branch
- Salaries of elected officials
- Payment of interest and principal on state debt
- Implied statutory appropriations

The School for the Deaf and Blind is considered an Executive Branch agency while the Legislative and Judicial Branches are not. Even though the Legislative and Judicial branches have indicated voluntary reductions in expenditures, statute does not specify if a portion or all of these appropriations should be included in the calculation of the percentage reduction.

SB 294 included general fund appropriations for a pay plan for state employees in both FY 2018 and FY 2019. While SB 261 decreased certain appropriations contained in this bill, a portion of appropriations within SB 294 remain in place. In addition to appropriations to provide for a 1% pay increase in FY 2019 the bill included appropriation for:

- $1.0 million to the Governor's Office for personal services contingencies that may arise during the biennium
- $75,000 to the Department of Administration for the Labor-Management Training Initiative
- $2.0 million to the Office of the Commissioner of Higher Education for retirement incentives for qualified employees

39-71-403, MCA requires that in any year a workers' compensation premium due from a state agency is lower than the previous year, the appropriation for that state agency must be reduced by the same amount that the workers' compensation premium was

- Which time period to employ[3] – beginning of the biennium or at the point in the biennium the reductions are proposed

Office of Budget and Program Planning (OBPP) Assumptions

The executive calculated the general fund spending reduction for the total of all Executive Branch agencies excluding MUS and elected official agencies at 9.571%. This calculation makes the following assumptions:

- Non-weighted average of Executive Branch agencies
- HB 2 and certain SB 294 appropriations were included in the calculation of the appropriations, statutory appropriations, other bills, and authorized transfers were not included
- School for the Deaf and Blind appropriations were excluded from the total appropriations of the Executive Branch
- Pay plan appropriations for the 1% pay increase, after SB 261 reduction impacts, are included but the additional appropriations for personal service contingencies, the Labor-Management Training Initiative, and the retirement incentives are not
- Proprietary reductions for the Liquor Control Division within the Department of Revenue were included. OBPP indicated that since any profits from the division are transferred to the general fund they included the reductions
- Workers' compensation premium reductions of $30,888 were included in the appropriation amounts. However, an additional $205,377 in Executive Branch workers' compensation premium reductions were not included in the calculation of Executive Branch appropriations
- Program reductions above the 10% statutory limit were included in the proposed reductions and in the calculation of the percentage of spending reductions. If these reductions are excluded from OBPP calculation the average Executive Branch reduction percentage is reduced. See the narrative on the following page for further information on requirements for reductions by program

Lack of Authority in 17-7-140, MCA

Legal review has identified several areas where the proposed reduction may be outside of the authority granted to the executive under 17-7-140, MCA, some of which necessitate legislative action to complete. Figure 2 lists those reductions by type of issue: 1) those that reduce non-general fund sources; 2) those that reduce programs by more than 10%; 3) those that would require a statutory change; 4) those that may impair a contract. Each are briefly discussed in this section and also discussed in the individual agency narratives. The complete text of the legal memorandum by Julie Johnson of the Legislative Services Division, dated September 29, 2017, is included as Appendix B.

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reduced. The statute does not outline the time period that this must occur. Appropriation reductions for workers' compensation premium reductions were made throughout August and September.

SB 261 required triggered reductions to reduce HB 2 general fund appropriations early in August 2017.

[3] ***Time Period to Employ***

OBPP has recommended expenditure reductions for both FY 2018 and FY 2019 after consideration of a changes to legislative appropriations that have occurred since the conclusion of the 2017 session. Statute does not specify a time period to employ when making the reductions.

Figure 2

Reductions Outside of 17-7-140, MCA			
Agency	Purpose	General Fund	Other Funds
Reduces Non-General Fund			
Department of Revenue	Liquor Transfers	$0	($600,448)
Department of Commerce	Brownfield Spills Transfer	0	(10,000)
Department of Commerce	Montana Manufacturing Extension Center	0	(200,000)
Subtotal		0	(810,448)
Reduces Program By More Than 10%			
Department of Revenue	Director's Office	(38,640)	0
Department of Revenue	Citizen's Services	(5,353)	0
Montana Historical Society	Museum Program	(180,728)	0
Montana Historical Society	Publications Program	(124,612)	0
Department of Corrections	Secure Custody Facilities - only in FY 19	(425,793)	0
Subtotal		(775,126)	0
Needs Statutory Change			
Department of Commerce	Brownfield Spills Transfer	0	(10,000)
Department of Commerce	Montana Manufacturing Extension Center	0	(200,000)
Montana State Library	Reducing FTE eliminates statutory program	Not determined	
Office of Public Instruction	Statute dictates distribution amount	(5,623,158)	0
Office of Public Defender	Reduction of contract attorneys	(6,471,590)	0
Department of Justice	Statute dictates lab in yellowstone county	(300,000)	0
Department of Corrections	SB 60 - 30 day PSI must be competed in 30 days	(720,000)	0
Department of Corrections	SB 63 - Making law retroactive and application	(6,530,484)	0
Department of Public Health and Human Services	Eliminate comprehensive case management for foster children in three counties. Potential conflict with Fostering Connections to Success and Increasing Adoptions Act of 2008, 110 P.L. 351, 122 Stat. 3949.	(348,840)	0
Subtotal		(19,994,072)	(210,000)
Potential Contract Impairment*			
Department of Public Health and Human Services	Cancels contracts with Child Advocacy Centers across the state	(204,000)	0
Department of Public Health and Human Services	Eliminates contract for orientation and mobility skill instruction	(175,576)	0
Department of Public Health and Human Services	Eliminates funding to support a contracted coordinator to facilitate pre-hearing conferences to engage families in the court process	(93,856)	0
Department of Public Health and Human Services	Eliminates contract that provides coordination activities between dentists and individuals	(60,000)	0
Department of Public Health and Human Services	Eliminates contract with Parents Let's Unite for Kids (PLUK)	(56,906)	0
Department of Public Health and Human Services	Eliminates funding used to provide mentoring services to eligible youth via eight Big Brother Big Sister contracts	(99,992)	0
Department of Public Health and Human Services	Eliminates unmatched general fund portion of contracts supporting domestic violence services.	(235,924)	0
Department of Public Health and Human Services	Eliminates unmatched general fund for In-Home / Prevention service providers. Contracts for providers in communities across the state would be limited to the federal grant amount, and the associated required general fund match.	(1,806,010)	0
Department of Public Health and Human Services	20% reduction in the service contract with Northrup Grumman for the maintenance and operation of the current system in use in Child & Family Services (CAPS)	(515,796)	(145,480)
Department of Public Health and Human Services	10% reduction in the service contracts with Deloitte, supporting the supporting CHIMES benefits eligibility system for Medicaid, SNAP and TANF	(951,016)	(4,260,000)
Department of Public Health and Human Services	Reduce Conduent MMIS & Flexible Rx contract(s) CONSIDERATION and PAYMENTS	(466,396)	(1,399,188)
Department of Public Health and Human Services	Eliminates the state-provided portion of the match required for tribes to draw down federal administrative funds from the Title IV-E program to support child welfare operations on tribal reservations.	(834,000)	0
Department of Public Health and Human Services	Reduces funding reduces provider grants in STARS and child care, reduces professional development incentives for providers; reduces child care and development fund contracts by 1%; and reduces CCUBS maintenance and operations contract with Northrup Grumman by one level of effort.	(994,492)	0
Department of Public Health and Human Services	Reduces contract for providing ongoing support services to persons with severe disabilities who work in a facility or a community-based employment setting.	(570,000)	0
Department of Public Health and Human Services	Reduces TANF Pathways contracts by 10%.	(3,839,224)	0
Department of Corrections	Reduction of MASC bed rate to $ 69 /day	(1,463,664)	0
Department of Corrections	Reduce treatment provider contracts by 5%	(1,872,344)	0
Department of Corrections	Reduce offender services contracts by 5%	(348,772)	0
Department of Corrections	Reduce pre-release contracts by 5%	(2,331,326)	0
Department of Corrections	Suspend $9.14 per day payment for Shelby	(3,336,100)	0
Department of Corrections	Reduce Shelby contract by 2%	(566,090)	0

* Listing reflects items that discuss changes to contracts in the description entered by the agency. Other proposals may impact contracts but not be identified by the agency in the description. Thus this listing is not comprehensive.

Non-General Fund Sources

One recommendation, to reduce spending in the Liquor Control Division within the Department of Revenue, would reduce non-general fund sources in order to add to the general fund balance. Review by legislative legal staff has concluded that 17-7-140, MCA specifically authorizes the Governor to reduce general fund spending only. However, it is within the management discretion of the executive to spend less than the appropriation. Therefore, the executive could make these reductions outside of the 17-7-140, MCA framework. Figure 2 shows the reductions outside of 17-7-140, MCA including non-general fund sources by agency. The other two items shown under non-general fund sources require legislative action to occur and are discussed under the category entitled "Need Statutory Change", below.

Program Reductions Above 10%

17-7-140, MCA limits the level of reductions the Governor may require to 10% during the biennium for each program within an agency. OBPP has proposed spending reductions in a number of programs that exceed this limit. Figure 2 shows the agency, program, and level of spending above the 10% statutory level.

The Budget Director included $775,126 in reductions above the statutory limit in his recommendation to the Governor for proposed spending reductions. These amounts were also included in the calculation used to determine the level of proposed spending reductions for the Office of Public Instruction, the Department of Justice, and the Montana University System. Excluding the spending reductions that are above the statutory limit for programs would reduce the allowed level of spending reductions for state agencies headed by elected officials or the MUS.

Need Statutory Change

The executive cannot implement reductions that require a statutory change.

- Two proposals within the Department of Commerce reduce state special revenue expenditures for grants funded through the big sky economic development fund and transfer that amount to general fund. Montana statute (90-1-205, MCA) specifies the allowable uses of this fund and transfers to the general fund are not included
- Reductions to personal services including FTE could impact statutory programs within the Montana State Library. To eliminate the programs would require changes in statute
- Spending reductions for combined block grants may conflict with 20-9-630, MCA, which outlines the calculation for the block grant amounts

Potential Contract Impairment

State agencies cannot unilaterally amend a contract without the potential of contract impairment. It is unclear from the description on the proposed reductions if the Department of Public Health and Human Services or the Department of Corrections are planning to renegotiate the contracts listed in Figure 2. It should also be noted that the list in Figure 2 may not be comprehensive as the description of the proposed reduction may not refer to existing contracts.

Impacts on Federal Funds

A number of proposals will have a direct impact on the level of federal funds available to the state. The largest is in the Department of Public Health and Human Services (DPHHS) which includes a proposed reduction of $67.2 million in FY 2018 and $69.0 million in FY 2019. About 81% is related to Medicaid funding for benefits and claims.

Potential Other Impacts

Other entities, including local governments, could be impacted by the proposed reductions. Please refer to the Part 2 of the report for narrative on other potential impacts.

PROPOSED GENERAL FUND REDUCTIONS BY FUNCTIONAL AREA

Figure 3 shows the general fund and all funds HB 2 appropriations and the proposed reductions by functional area of the HB 2 budget. Of the total HB 2 budget for the Executive Branch agencies, $1,521.7 million or 39.2% of the budget is for the K-12 BASE School Funding Program and is excluded for purposes of 17-7-140, MCA. As a result of the exclusion, Section E - Education percentage reduction goes from 53.1% of the total to 22.6%. As shown, Section B -Health and Human Services comprises 45.9% of the total general fund reductions while Education is 22.6% and Section D - Judicial, Law Enforcement, and Justice makes up 23.5% of the proposed general fund reductions.

Figure 3

HB 2 Appropriations - Executive Branch Agencies Subject to Reduction
Including Pay Plan and SB 261 Reductions

	Appropriations	% Appropriation	Proposed Reduction	% Reduction
General Fund				
General Government	$159,651,859	4.1%	($13,636,802)	6.0%
Health and Human Services	1,050,308,010	27.0%	(105,029,491)	45.9%
Natural Resources and Transportation	71,366,703	1.8%	(4,631,494)	2.0%
Judicial, Law Enforcement, and Justice	540,094,228	13.9%	(53,723,636)	23.5%
Education	2,063,270,687	53.1%	(51,694,160)	22.6%
All Funds				
General Government	494,966,282	5.9%	(14,476,754)	4.0%
Health and Human Services	4,235,428,721	50.5%	(241,663,689)	66.0%
Natural Resources and Transportation	323,142,990	3.9%	(4,631,494)	1.3%
Judicial, Law Enforcement, and Justice	710,425,427	8.5%	(53,723,636)	14.7%
Education	2,619,281,141	31.2%	(51,694,160)	14.1%

Impacts by Section

The following narrative discusses the impacts of the proposed spending reductions by section including costs shifts to other entities, reductions in federal funds, and proposals that may not be allowable without statutory changes. It should be noted that for the purposes of this discussion, the HB 2 budget reflects Executive Branch agencies, with statutory exclusions provided in 17-7-140, MCA and SB 261 reductions included.

Section A – General Government

General Government makes up 6.8% of the HB 2 appropriations in the 2019 biennium and has 6.1% of the total proposed reductions. Four agencies make up 91.2% of the recommended reductions in General Government: Department of Revenue (DOR), 64.1% of the reduction; Department of Administration, 10.4%; Governor's Office, 9.2%; and Department of Military Affairs, 8.2%.

<u>Department of Revenue</u>

The executive proposes $3.2 million each year in personal services reductions and $1.4 million each year in operating expense reductions for DOR. Impacts include:

- Personal services reductions for the:
    - o Director's Office with expenditures for 12.00 FTE reduced. As of September 26, 2017 the Director's Office had 5.00 FTE vacant
    - o Citizen Services and Resource Management Division with current vacancies left open and fewer temporary employees hired. The Citizen Services and Resource Management Division had 12.70 FTE vacant as of September 26, 2017

    - Property Assessment Division (PAD) with current vacancies maintained and personal services expenditures for 80.00 FTE reduced in FY 2018 and 52.00 FTE in FY 2019. PAD had 12.42 FTE vacant positions as of September 26 2017
- Operating expenses reductions by reducing property assessment office hours in various counties and closing other county offices, delaying equipment purchases, and contract renegotiations.

The Business and Income Tax Division, with $20.6 million in general fund, was excluded from the proposed reductions.

Proposed reductions for DOR also include $600,000 in proprietary expenditures in the Liquor Control Division. As profits from the division are transferred to the general fund, a reduction in spending should increase the transfer to the general fund.

Department of Administration

Of the $1.5 million in proposed general fund reductions, $1.1 million is shifted to proprietary funds. While increased costs to the proprietary funds may not increase rates charged to agencies in the current biennium, DOA has indicated that rate increases in the 2021 biennium may be forthcoming.

Governor's Office

The executive proposes to reduce expenditures by approximately $1.3 million over the biennium, which results in an 8.7% reduction in FY 2018 and 10.0% reduction in FY 2019. Proposed reductions in personal services total approximately $947,000 over the biennium and the office anticipates primarily holding positions open during the biennium. As of September 26, 2017 the Governor's Office had 5.50 FTE vacant. Proposed reductions in operating expenses total approximately $334,000. Decreases in operating expenses primarily include reductions to contract and consulting services, travel, tradeshow participation, catering and food expenses, and the maintenance operating budget in the Air Transportation Program. The executive is also proposing a reduction to expenditures for an econometric data subscription. This reduction will shift expenditures to other state agencies that use this subscription and could increase general fund expenditures for those agencies.

Department of Military Affairs (DMA)

The executive proposes reductions in expenditures of approximately $1.1 million over the biennium. Proposed personal services reductions total approximately $391,000 over the biennium and include reducing expenditures for several FTE. DMA had 5.36 FTE vacant as of September 26, 2017. Proposed operating expense reductions total $639,000 over the biennium and include reducing and/or eliminating maintenance and janitorial services, postponing small construction projects, eliminating the Veteran's Service Outreach Program, as well as other reductions in operating expenses. Proposed reductions in grants total $41,000 and are in the Scholarship Program.

The Disaster and Emergency Services Program, with $20.6 million in general fund, was excluded from the proposed reductions.

The Department of Military Affairs receives federal matching funds in several programs, including the ChalleNGe, Army National Guard, and Air National Guard Programs. Total estimated reductions in federal special revenue due to the loss of state matching funds are approximately $1.5 million over the biennium.

Section B – Health and Human Services

Department of Public Health and Human Services (DPHHS)

Health and Human Services makes up 44.4% of the HB 2 appropriations in the 2019 biennium and has 45.8% of the total proposed reductions. The Budget Director recommends the general fund expenditures for the DPHHS be reduced by 10.0% from the HB 2/SB 294 level. He also recommends a 10.0% reduction from each program within the department. The recommended general fund reduction is $105.0 million with

$136.6 million in matching federal funds. In total, the DPHHS reduction is $241.6 million over the 2019 biennium, 56.3% of which is general fund and 81.1% of which is benefits and claims. The remaining 18.9% is comprised of operating expenses (7.7%), personal services (6.9%) and grants (3.9%).
The majority of the reduction for DPHHS is comprised of three types of components, which make up almost 90.0% of the total reduction:

1. Elimination or reduction of optional Medicaid services
2. Reduced Medicaid provider rates

Elimination or Reduction of Optional Medicaid Services

OBPP recommends the elimination or reduction of certain optional Medicaid services. In order to participate in Medicaid states must offer about fifteen types of benefits to enrollees (mandatory benefits). States may also offer about thirty other optional Medicaid benefits to enrollees; services like dental care, eyeglasses, hospice, and prescription drugs.

OBPP has recommended the elimination or reduction of the following optional services:

- Targeted case management services (TCM)
- Reduction in certain high cost dental services
- Elimination of the Healthcare for Healthcare Workers Program
- Elimination of hospice services
- Elimination of personal assistance services
- Elimination of the Health Improvement Program
- Elimination of the Medicaid Passport to Health Program
- Reduction of services in the Big Sky Waiver

Almost 16.0% of the total general fund reduction is for Medicaid targeted case management services, $16.7 million in general fund and $32.0 million in federal funds over the 2019 biennium. Case management consists of services to assist eligible beneficiaries in obtaining medical and other necessary for treatment of their illness. Targeted case management refers to case management that is restricted to specific beneficiary groups. The programs primarily impacted by OBPP's recommendation are the Developmental Services Division (DSD) and the Addictive and Mental Disorders Division (AMDD). TCM services in DSD are proposed to be reduced by $8.2 million general fund and $16.5 million federal special revenue. The program effected will be the Children's Mental Health Program, the Developmental Disabilities Program and services for children with special health care needs. TCM services in AMDD could be reduced by $7.8 million general fund and $14.5 million federal special revenue. The services effected will be those to individuals with severe disabling mental illness and substance use disorders.

Reduced Medicaid Provider Rates

OBPP recommends the reduction of Medicaid provider rates for certain services. The most significant of these reductions involves payments for outpatient PPS (prospective payment system) hospitals, provider based clinic payments, durable medical equipment (wheelchairs and similar items), and payments for critical access (mostly rural) hospitals.

The remaining 10.0% of the DPHHS reduction is a combination of maintaining vacancies, enforcing furloughs, closing smaller offices, reducing services associated with IT projects, delaying IT projects and contract reductions and eliminations.

Several of the proposals may require contract. As discussed in the legal memorandum from the Legislative Services Division, the state cannot unilaterally amend a contract. To enact changes to contracts without the other party’s consent may raise contract impairment issues. For additional details refer to the legal memorandum by Julie Johnson of the Legislative Services Division, dated September 29, 2017, and included as Appendix B.

Section C – Natural Resources and Transportation

Natural Resources and Transportation makes up 3.0% of the HB 2 appropriations in the 2019 biennium and has 2.0% of the total proposed reductions. The Department of Natural Resources and Conservation and the Department of Environmental Quality make up 85.6% of the proposed reductions in Section C.

Department of Natural Resources and Conservation

The Forestry and Trust Lands Division, with $25.4 million in general fund, was, for the most part, excluded from the proposed reductions. Of the total reductions, 25.6% occurred in personal services, 49.7% in operating expenses, 13.3% in equipment and intangible assets, 9.1% in grants and, 1.1% in debt service. Reductions in personal services occur in the Director's Office and the Water Resources Division and include holding vacant positions open, voluntary furloughs without pay, and reductions to staff hours. The Director's Office has 1.00 FTE open as of September 26, 2017 and the Water Resources Division has 6.25 FTE vacant. Reductions in operating expenses occur in Conservation and Resources Development Division, Forestry & Trust Lands Management Division and Water Resources Division. Reductions in grants occur in Forestry and Trust Lands Management Division.

Department of Environmental Quality (DEQ)

OBPP recommends the general fund expenditures for the Department of Environmental Quality be reduced by 10.0% from the HB 2/SB 294 level. Of the total reductions, 52.0% occurred in operating expense and 48.0% in personal services. Reductions in personal services and operating expenses occur in the Enforcement Division, Waste Management & Remediation Division and the Air Energy & Mining Division. The Water Quality Division proposes to reduce personal services expenditures. DEQ will reduce support for Air Quality Programs in thirteen communities within eight counties.

OBPP proposes to shift the $70,000 per year cost of the State Recycling Program from the state general fund to solid waste management fees account in the state special revenue fund. The agency collects license fees from operators of solid waste management facilities. Other reductions in services may put pressure on existing fees charged for services.

Section D – Judicial, Law Enforcement, and Justice

Judicial, Law Enforcement, and Justice makes up 22.9% of the HB 2 appropriations in the 2019 biennium and has 22.4% of the total proposed reductions. Department of Corrections (DOC) makes up 74.9% of the proposed reductions with the Department of Justice (DOJ) at 12.2% and the Office of the Public Defender (OPD) at 12.0%.

Department of Corrections

The Budget Director proposes $40.2 million in reductions for the Department of Corrections. The larger reductions for the biennium include:

- $6.5 million from applying laws related to SB 63 retroactively – SB 63 reduces supervision for low risk offenders doing well in community programs
- $5.5 million slated for assistance in removing offenders from county jails – alternative placements and services for offenders would not be available as options
- $4.4 million for reduction in outside medical costs through pharmacy savings and medical evaluations
- $3.3 million for Shelby prison reduction in expenditures related to suspension of $9.14 payment on beds
- $3.2 million from closure of the Lewistown Infirmary – a 25 bed facility
- $2.3 million for reduction of pre-release contracts by 5%
- $2.0 million in expenditures of contingency funding related to county jail hold being below 250
- $1.9 million for reduction of treatment contracts by 5%
- $1.5 million for savings related to DOC contracts with Missoula County and rates of $69.00 per day
- $1.4 million for counseling and mental health services

- $1.4 million from cancellation of the 60 bed chemical treatment center at MSP
- $1.2 million for closure of Youth Transition Center in Great Falls

Several of the proposals may require contract changes to provide for suspension of $9.14 payment on beds at the Shelby prison, and reductions for pre-release contracts, treatment contracts and DOC contracts with Missoula County. As discussed in the legal memorandum from the Legislative Services Division, the state cannot unilaterally amend a contract. To enact changes to contracts without the other party's consent may raise contract impairment issues. For additional details refer to the legal memorandum by Julie Johnson of the Legislative Services Division, dated September 29, 2017, and included as Appendix B.

Department of Justice

The Budget Director proposes to reduce the Department of Justice spending by $6.6 million for the biennium. The Budget Director proposes program reductions in personal services, recognizing that as an elected official, the Attorney General has the flexibility to make the proposed reductions in other expenditure categories such as operating expenses. According to DOJ, reducing its general fund spending will require leaving vacant positions unfilled, eliminating overtime, and reducing employee work hours. As of September 26, 2017 DOJ had 29.29 FTE vacant. Of the 29.29 vacant FTE, 15.09 are Highway Patrol Officers, the majority of which became vacant in the last 2 months.

DOJ has indicated that to avoid a reduction in force, it will also be required to reduce operating expenses by reducing or eliminating employee travel, outside council costs, contracts such as 24/7 Program, equipment purchases, grants awarded for prosecution of crimes against children, testing and submission kits, and delay the timeline on current driver's modernization. Other potential reductions include closing the satellite chemistry laboratory in Billings and cancelling plans to build the morgue in Billings.

Office of the Public Defender

OBPP is proposing that the Office of the Public Defender reduce spending by $6.5 million for the biennium. All reductions are related to reducing OPD contract attorneys. This change will force caseloads to be shifted to existing attorneys and likely create wait times in the judicial system.

Section E – Education

Education also makes up 22.9% of the HB 2 appropriations in the 2019 biennium and has 22.6% of the total proposed reductions. The Commissioner of Higher Education (OCHE) comprises 82.8% of the proposed reductions within the Education agencies, the Office of Public Instruction (OPI) 15.0%, the Montana Historical Society (MHS) 1.0%, and the Montana State Library 0.9.

Commissioner of Higher Education

OBPP proposes general fund expenditure reductions of $42.9 million for the Office of the Commissioner of Higher Education.

With the exception of Workforce Development, the reduction was applied to all programs that have HB 2 general fund. Workforce Development general fund appropriations of $180,134 provide the general fund match for the Carl D. Perkins federal grant. The general fund appropriated is the minimum amount allowed for the federal maintenance of effort requirements for the federal grant.

The determination regarding specific reductions will be made at the discretion of the Board of Regents (BOR) once reduction figures are finalized, and impacts will be defined at that time. BOR's next scheduled meeting is November 16 & 17, 2017.

Office of Public Instruction

The Budget Director proposes $7.8 million in reductions for the Office of Public Instruction. In the State Level Activities Program these reductions are proposed to occur in operating expenses within the Superintendent's Office. Specifics of the reductions are at the discretion of the superintendent and have not been announced. In the Local Education Activities Program, expenditure reductions are proposed in the combined block grants, which is entirely local assistance for school districts.

Montana Historical Society

OBPP recommends expenditure reductions for the Montana Historical Society (MHS) totaling $536,071 for the biennium or a 10% reduction from the HB 2/SB 294 level. OBPP did not propose reductions in the Education or Historic Preservation Programs with $404,494 and $50,190, respectively, in general fund appropriations.

Over 60% of the HB 2 budget for MHS is in personal services. The reductions presented by OBPP will reduce personal services by $186,135 in FY 2018 and $236,641 in FY 2019. This would equate to a reduction of 3.00 FTE of their existing workforce. In addition, several employees have volunteered a reduction of hours and/or unpaid leave to fulfill the personal services reductions.

For the biennium, operating expenses would be reduced by $113,295. MHS will forego IT upgrades and travel and registration fees for the director, along with reducing hours of the museum and research center.

Montana State Library

OBPP recommends the general fund expenditures for the Montana State Library (MSL) be reduced by $441,836 over the biennium or a 10% reduction to the agency from the HB 2/SB 294 level.

Personal services will be reduced by $362,131 over the biennium. This will impact funding for 2.00 FTE. Operating expense reductions are 18% of the proposed reductions for both FY 2018 and FY 2019. The $79,705 in reductions to operating expenses will include cancelling electronic journal subscriptions, delaying payments for software maintenance contracts, and eliminating equipment purchases.

Reductions to personal services involving reductions in FTE could have an impact on statutory programs within MSL. Half of the general fund FTE in this agency are tied to statutorily mandated programs. The Library Commission would have to decide which of the following FTE would be reduced upon final executive decisions:

- State Library Commission Authority, 22-1-103, MCA (3.00 general fund FTE)
- Administration of state publications depository library program -- rulemaking, 22-1-212, MCA (1.00 general fund FTE)
- Natural Resource Information System, 90-15-101, MCA (2.00 general fund FTE)
- Additional operational support, 22-1-102, MCA (5.50 general fund FTE)

For additional details refer to the legal memorandum by Julie Johnson of the Legislative Services Division, dated September 29, 2017, and included as Appendix B.

The following section outlines the proposed reductions by agency and program.