

DAILY ROLL CALL.

HOUSE RULES COMMITTEE

50th LEGISLATIVE SESSION -- 1987

Date January 21, 1987

[illegible]

MINUTES OF THE MEETING
RULES COMMITTEE
50th LEGISLATIVE SESSION

January 21, 1987

The fifth meeting of the House Rules Committee was called to order by Chairman Tom Hannah on Wednesday, January 21, 1987 at 5:15 p.m. in Room 428-A of the State Capitol.

ROLL CALL: All members were present.

CONSIDERATION OF HJR 7: A JOINT RESOLUTION OF THE SENATE AND THE HOUSE OF REPRESENTATIVES OF THE STATE OF MONTANA RECOMMENDING PRIORITY OF FISCAL MATTERS BEFORE THE LEGISLATURE.

Rep. Tom Asay, chief sponsor of HJR 7, said the purpose of this resolution was to address certain questions the legislature has to face when it comes to knowing the appropriations picture. The problem is not limited to just the general fund but the entire \$2 billion cost of operating government. Before any meaningful decisions are made, the legislature must find out what it is going to do with the money. He further said we need to know how to handle the Workmen's Comp situation among other things. He referenced several statements from an analysis of earmarking revenues compiled by the Legislative Finance Committee a copy which is attached hereto (Exhibit 1).

There were no proponents or opponents. The hearing was opened to questions.

Rep. Quilici asked Rep. Asay how he intended to implement this. Rep. Asay said he didn't have all the mechanics worked out, but he feels there is enough information available to get the job done. Rep. Quilici asked how this would affect the subcommittees' workload and how they would be able to compile all the essential information required. Rep. Asay replied that he did not know how far the subcommittees would have to get into this matter to find out.

Rep. Marks commented that there are some mechanical things that create some situations that make the legislative intent of this bill a little less possible. He pointed out that it takes time to get fiscal notes prepared. The Budget Office has already requested extensions of time on the preparation of some fiscal notes.

Referring to page 3, line 8 of the bill, Rep. Marks asked Bob Person, Legislative Council, if the House is bound to review and adopt rules. Mr. Person said the House would be morally binding to itself. He said the House could go as far as restructuring its committees.

Rep. Ramirez said he did not know if a review of appropriations and finances by the House committees will really do much. It won't help us immediately. He also said that if we give all the fiscal matters priority, we might have people sitting around waiting on other non-fiscal matters. Rep. Asay responded by saying his main concern is facing these issues before the 75th or 80th legislative day rolls around.

In response to a question asked by Rep. Vincent, Judy Rippengale, Legislative Fiscal Analyst, said that earmarked funds have been a high priority with more legislators over the past four years. There is a \$154 million balance in earmarked funds. It does restrict your ability to make some appropriations. She said there is a little bit of money from these funds worth getting your hands on, but they are mostly reserved for special interest groups. In response to a question asked by Rep. Eudaily, Rep. Asay said many of these funds would have to have special legislation in order to be touched.

There being no further questions, Rep. Asay closed. The hearing closed on HJR 7.

CONSIDERATION OF HB 149: AN ACT REQUIRING THAT LEGISLATIVE COMMITTEE OF THE WHOLE PROCEEDINGS OF LEGISLATIVE SESSIONS BE SOUND RECORDED.

Rep. Kelly Addy, sponsor of HB 149, said this bill was introduced for a three-fold purpose: 1) to provide more authority in legal proceedings; 2) to provide a historical record; 3) to provide access to the public. He said he is frequently frustrated in the way the courts interpret our legislation. The supreme court has begun to take our summary minutes and cite them in their court proceedings. He said he is not asking that all floor business be recorded -- he is simply talking about recording floor proceedings. In this way, we would be providing at least one authentic repository of the floor debates. Every once in a while, a momentous floor debate should have been preserved. He pointed out that Montana is a large state that is sparsely populated, and we need to provide those interested people access to what is going on in the mind of the legislature.

PROPONENTS:

Bob Archibald, from the Montana Historical Society, testified that this legislation provides a real need from a historical perspective. He said future generations need to understand what took place. Present records only tell us what happened to legislation. They provide us with very little about the "flesh and emotions" part of what happened. We need to know more of why things happened.

Brenda Schye, representing the Montana Cultural Advocacy, stated she supports the collection of historical records for future generation use. A copy of her written testimony was marked Exhibit 2 and is attached hereto.

OPPONENTS: none

Chairman Hannah opened the hearing up to questions and discussion. Rep. Ramirez brought up some technical questions concerning the implementation of this bill: 1) the identification of the voice; 2) much of what is being recorded is unintelligible due to the quality of the recording system. He wanted to know how the system would be set up. Mr. Archibald said they have done some experimenting with different kinds of sound equipment, and he feels the job could be done. He said they have developed a system of indexing which can guide the listener very quickly to the interested portions referenced in the tape.

Rep. Ramirez asked if the microphones would be directly connected to the recorder. Mr. Archibald replied yes.

Rep. Hannah inquired as to the use of a court reporter. Rep. Addy said court reporters wouldn't work because of the high cost of employing one and because of the potential mechanical problems that might be created. Mr. Archibald again pointed out that he hoped to capture the feelings and emotions of a floor debate that only a tape could provide.

Rep. Brown commented that he heartily supports this bill because of the courts' interpretations of what the legislature does. The court has a habit of using the committee minutes to support its findings. He said this is a low-cost alternative.

Rep. Eudaily questioned if any equipment is available for the purposes of a trial run. Mr. Archibald said they didn't have any equipment at the present time. In response to a question asked by Rep. Mercer, Mr. Archibald said there was no money in the Historical Society's budget to fund this.

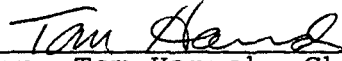
In closing, Rep. Addy said this would affect next session. It would go into effect this October, and it would be a line item in the feed bill. The fiscal impact is there but can be handled as clearly as other expenses.

The hearing closed on HB 149.

Chairman Hannah informed the committee that action on these two bills would be delayed until tomorrow afternoon, January 22nd, on adjournment of the House.

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ADJOURN: A motion having been made by Rep. Quilici, the meeting
adjourned at 6:00 o'clock p.m.



Rep. Tom Hannah, Chairman



JUDY RIPPINGALE
LEGISLATIVE FISCAL ANALYST

STATE OF MONTANA
Office of the Legislative Fiscal Analyst

STATE CAPITOL
HELENA, MONTANA 59620
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Exhibit 1
7/21/87
HJR 7

September 12, 1986

TO: Legislative Finance Committee

FROM: Clayton Schenck, Senior Fiscal Analyst *Clayton Schenck*
Jim Haubein, Principal Analyst *Jim Haubein*

SUBJECT: An Analysis of Earmarking Revenues and State Special Revenue Accounts in Montana

INTRODUCTION

Earmarking revenues is broadly defined as the allocation of designated revenues to finance a specific government function or service. At fiscal year end 1986, over 50 percent of the state of Montana's tax and license revenues are "earmarked" for a specific purpose. Earmarking revenues is a widespread yet very controversial practice in government budgeting. There is legislative concern over the proliferation of earmarked revenues, the resulting loss of budgetary flexibility, and the lack of a method for reviewing and evaluating earmarked accounts. Subsequent to the last legislative session, the Legislative Finance Committee requested the Legislative Fiscal Analyst to present a report to the committee on the feasibility of reducing the amount of earmarked revenue.

The purpose of this report is to review earmarked revenues to determine the value of earmarking all, some, or none of the current earmarked revenues and to develop an objective set of criteria against which the merits of individual earmarked (state special revenue) accounts may be measured. This report looks at earmarked revenues in Montana, both historically and in comparison to other states, discusses the pros and cons of earmarking and its effect on the budget process, proposes criteria for

evaluation of state special revenue accounts, provides a functional evaluation of those accounts, and makes recommendations for (1) de-earmarking state revenue and (2) establishing controls over the future earmarking of state revenue and designation of state special revenue accounts.

EARMARKED REVENUES IN MONTANA

Scope

As defined in the introduction, earmarking revenues is a device for tying revenues from specific taxes and other fees to the financing of a specific government function. In reality, however, the relationship is not usually very clear-cut. Most commonly, special funds outside the general fund are created to serve as depositories for collections from earmarked revenue sources, with expenditures to be made from these funds for designated purposes only. In Montana, they are most frequently placed in an account within the state special revenue fund. While some revenues that may technically be defined as "earmarked" may go to special fund designations other than state special revenue funds (such as designated federal revenue funds, proprietary funds, enterprise funds, and fiduciary funds), the scope of this report will be limited to an analysis of the great majority of earmarked funds that are designated as state special revenue funds. It is important to note, however, the distinction made here when referring to earmarked revenues versus state special revenue accounts. Our discussion and statistics on earmarked revenues include some revenues that go into accounts other than state special revenue accounts, but our analysis and recommendations will be limited to those revenues that are deposited in state special revenue accounts.

Establishment of Earmarked Revenues/State Special Revenue Accounts

A revenue source may be earmarked either by constitution or by statute to finance a particular government program. In Montana, the constitution earmarks revenues for highway programs, the coal tax trust fund, public schools and universities, livestock inspection and control, animal health programs, and operation of the Consumer Counsel. All other earmarked revenues were established by statute.

State special revenue accounts, set up as depositories for earmarked revenues, are usually designated in the statute that established the earmarked revenue. Where an earmarked revenue is established by statute but the statute is silent on the account establishment, the account is established on the basis of legislative intent. The interpretation of the statutes has often been taken very liberally in justifying establishment of special revenue accounts. Some state special revenue accounts are established for administrative purposes, commonly an income transfer account set up for accounting purposes only, and they have no statutory basis. To set up a state special revenue account, an agency submits a request to the Accounting Division of the Department of Administration. The Department of Administration is designated by statute (MCA 17-2-106) as the authority for the creation and abolition of new accounts. New account assignment is decided within the guidelines of generally accepted accounting principles and the state fund structure (MCA 17-2-102). Once established, appropriations from the account must be made by the legislature. Periodically, the Accounting Division reviews the state special revenue accounts for possible deletions.

Historical Review of Earmarked Accounts in Montana

In fiscal 1984 approximately 61 percent of all state tax, license and fee revenues were earmarked for specific programs and functions. At

June 30, 1986 there were 212 state special revenue accounts, with a total fund balance of \$154.1 million and total receipts for fiscal 1986 of \$449 million. Table 1 shows the number of earmarked accounts, the total receipts, and the fund balance for the past fourteen years. The table shows that earmarked revenues and accounts have more than doubled in the past seven years. The major reason for the proliferation of the number of state special revenue accounts in recent years can be attributed to the increased use of administratively assigned accounts.

Table 1
Earmarked Accounts - Historical Data
Fiscal 1973 - 1986

<u>Fiscal Year</u>	<u>Number of Accounts</u>	<u>Total Receipts (Millions)</u>	<u>Fund Balance End of Year (Millions)</u>
1973	103	\$110.8	\$ 18.4
1974	92	136.6	18.0
1975	111	137.0	55.6
1976	94	171.8	55.3
1977	120	184.2	59.1
1978	110	196.4	49.0
1979	100	226.9	58.2
1980	113	225.5	97.8
1981	116	261.3	123.9
1982	129	340.0	183.8
1983	125	249.2	92.6
1984	162	426.4	194.5
1985	171	444.5	286.5
1986	212	449.0	154.1

In Montana, revenues were earmarked for education beginning in the 1860's. Earmarking became a predominant factor in Montana budgeting in the 1920's and 1930's with the establishment and earmarking of highway funds and fish and game licensing revenues. When the state individual income tax was first enacted in 1933, 50 percent of the revenues from the

tax were earmarked. The most significant recent addition to earmarked revenues was coal severance taxes, enacted in 1975.

Table 2 shows a comparison of the disposition of major tax and license revenues in Montana in the years 1963, 1979, and 1984. The table provides a comparison of what revenues were earmarked in those years and what effects it has had on the general fund percentages. Note that in the majority of cases, the percentage placed in the general fund has decreased.

Table 2
Comparison - Disposition of Major Tax and License Revenues
Fiscal 1963, 1979, 1984

Revenue Classification	Total Revenues Collected (Millions)			Percent Earmarked			Percent to General Fund		
	1963	1979	1984	1963	1979	1984	1963	1979	1984
Sales or Gross Receipt Taxes									
Insurance	\$ 2.5	\$14.4	\$19.5	8	25	30	92	75	70
Tobacco Products	6.4	11.4	12.6	40	66	100	60	34	0
Alcoholic Beverages	4.1	11.7	14.8	17	30	43	83	70	57
Income									
Individual Corporation	13.9	141.4	170.3	25	36	36	75	64	64
	4.7	36.1	35.4	25	36	42	75	64	58
Highway User									
Motor Fuel	19.7	48.4	79.2	100	100	100	0	0	0
Motor Vehicle Registration	4.2	14.8	25.9	100	100	100	0	0	0
Operator License	.6	1.2	1.3	15	5	40	85	95	60
Licenses									
Hunting and Fishing	2.1	7.8	13.5	100	100	100	0	0	0
Occupation and Business			8.6			49			51
Miscellaneous									
Severance	2.8	50.9	144.8	3	59	63	97	41	37
Property	6.4	24.4	38.8	77	97	100	23	3	0
Inheritance	2.1	6.4	6.0	0	0	0	100	100	100

Comparison to Other States

The purpose of this section is to compare Montana's proportion of earmarked revenues with those of other states. This will provide some insight as to where Montana's earmarking policies are in relation to earmarking in the other states.

As a basis for the comparison, we used the results of four nationwide surveys of state tax and license collections taken by various organizations over a thirty year period from 1954 through 1984. The four surveys are the only known studies of revenue dedications among the states. Surveys taken in 1954 and 1963 were conducted by the Tax Foundation. A follow-up study was conducted in 1979 by the State of Montana Legislative Fiscal Analyst, and a survey of earmarking in 1984 was conducted by the National Conference of State Legislatures. The data for the 1984 survey is preliminary, and final data was not available at the time of this report.

Comparisons of tax data between the states or the comparison of data for any one state in differing years must be interpreted with caution. All four past studies reported many difficulties in compiling data on earmarking and in computing a percentage of total revenues that were earmarked. Problems were encountered due to differences in each state's accounting and reporting procedures, including the way they allocate and classify special funds. Most state accounting reports are difficult to interpret when attempting to identify earmarked taxes, and it becomes a matter of interpretive latitude in deciding how to classify some funds and whether to include them as earmarked taxes.

All four studies used Bureau of the Census data on state tax collections in their reports to provide the best available uniformity of measurement and definition for comparability. Earmarked revenues shown in the reports may vary from perceptions in some states due to the adjust-

ments required to make the data comparable, although Montana's reporting methods are quite consistent with Bureau of the Census interpretations. Despite difficulties in interpreting data between states, it is felt that the data provided gives an accurate reflection of the relationships between the states in the use of earmarking revenues.

Table 3 provides a summary of the percent of tax revenues earmarked by the states as compiled for the years 1954, 1963, 1979, and 1984 and provided by the four prior reputable studies. For the purposes of these statistics, the definition of earmarked taxes included licences as well as motor vehicle fees.

Table 3
Percent of Total Tax Revenues Earmarked by States
Fiscal Years 1954, 1963, 1979, and 1984

State	Percentage of State Tax Collections Earmarked*			
	1954	1963	1979	1984
1. Alabama	89	87	88	89
2. Alaska	**	6	1	2
3. Arizona	47	51	31	29
4. Arkansas	41	36	21	18
5. California	42	28	14	13
6. Colorado	75	51	17	25
7. Connecticut	26	23	0	1
8. Delaware	0	3	0	5
9. Florida	40	39	28	28
10. Georgia	29	22	11	9
11. Hawaii	**	7	5	5
12. Idaho	51	44	38	33
13. Illinois	39	43	14	18
14. Indiana	49	39	43	34
15. Iowa	51	44	19	***
16. Kansas	77	66	29	25
17. Kentucky	46	29	***	***
18. Louisiana	85	87	5	4
19. Maine	46	39	19	19
20. Maryland	47	40	34	36
21. Massachusetts	56	54	41	40
22. Michigan	67	57	38	39
23. Minnesota	73	74	12	13
24. Mississippi	40	37	***	22
25. Missouri	57	40	20	29
26. MONTANA	61	53	55	61
27. Nebraska	55	53	41	***
28. Nevada	55	35	34	49
29. New Hampshire	53	54	31	25
30. New Jersey	7	2	25	39
31. New Mexico	80	31	36	44
32. New York	13	10	0	6
33. North Carolina	38	30	20	7
34. North Dakota	73	43	29	21
35. Ohio	48	48	21	18
36. Oklahoma	62	59	***	43
37. Oregon	47	36	23	19
38. Pennsylvania	41	63	15	***
39. Rhode Island	6	4	0	1
40. South Carolina	69	62	56	52
41. South Dakota	59	54	33	33
42. Tennessee	72	77	60	24
43. Texas	81	66	54	20
44. Utah	74	62	52	49
45. Vermont	42	39	23	23
46. Virginia	39	32	27	25
47. Washington	35	30	29	27
48. West Virginia	57	39	21	22
49. Wisconsin	63	61	***	12
50. Wyoming	61	64	54	69
Average	51.1	41.1	23.0	24.0

* 1954 and 1963 figures are from Earmarked State Taxes, Tax Foundation, 1965.
1979 figures are from Dedicated Revenue Study, Office of the Legislative
Fiscal Analyst, State of Montana, 1980.

1984 Figures are from Earmarking of State Tax Revenue (Rough draft).
National Council of State Legislatures, June 1986. Data was preliminary,
but a followup with NCSL in September 1986 indicated that no major changes
to data was anticipated.

** 1954 study did not include Alaska and Hawaii.

***Information was not received in time to compile the report.

As shown in table 3, there was a significant decrease in earmarking nationally between 1954 and 1979. The average percentage of taxes earmarked by the states went from 51 percent in 1954 to 41 percent in 1963, and down to 23 percent in 1979. The most recent study indicates a leveling off of the downward trend in earmarking between 1979 and 1984, with 24.0 percent of state's taxes earmarked in 1984, nearly the same percentage as five years prior. Authors of the studies between 1954 and 1979 attributed the reduction in earmarking to two factors. The first factor was a concerted effort by several states to remove existing earmarking provisions and to limit the addition of new ones. There was a general feeling among legislatures during those years that earmarking limited legislative control over state spending. The state of Alaska went so far as to constitutionally prohibit any new earmarking provisions. The second factor was that non-earmarked revenue sources grew faster than earmarked sources. As an example, sales tax revenues grew rapidly during this period, and tended to be less often earmarked than other forms of taxes. The leveling off of earmarking between 1979 and 1984 has been attributed to offsetting factors. Earmarking increased in frequency, with several states, including Montana, adding earmarking provisions, and with very few provisions reduced or removed. This was apparently offset, however, by non-earmarked revenue sources continuing to grow faster than earmarked sources.

Montana has consistently ranked well above average among the states in the percentage of total tax revenues earmarked. In 1954, Montana earmarked 61 percent of its total tax revenues, 10 percent above the average for the states. In 1963, Montana showed a decline in the percent of tax revenues earmarked, but remained high at 53 percent. In the

period between 1963 and 1979, while the national average percent of earmarked tax revenues dropped 18 points to 23 percent, Montana's percentage actually increased, albeit by only two percentage points, to 55 percent. Montana was one of only five states that showed an increase during that period, and Montana's ranking among the states jumped from 15th and 17th in 1954 and 1963 respectively to 4th in 1979 for highest percent of earmarked to total tax revenues. The 1984 survey showed that Montana had continued its upward trend in earmarking at a time when the national average had levelled off, and the state's 61 percent earmarking level had earned it a ranking of 3rd highest amongst the 46 reporting states. The only states with a higher percentage of earmarking than Montana were Alabama (89 percent) and its neighbor, Wyoming (69 percent). The only other state with greater than 50 percent earmarking was South Carolina (52 percent).

Montana's modest upward trend between 1963 and 1979 while most states were reducing earmarking can largely be attributed to the enactment of the coal severance tax in 1975 and the earmarking of the majority of those receipts as well as the addition of other smaller earmarking provisions. The rapid growth in coal severance tax revenues contributed significantly to the increase between 1979 and 1984.

Table 4 shows the types of tax collections most commonly earmarked by the states in 1984. Please note that four states are not included in the survey. The table is comprised of any tax which is earmarked by at least ten states, and is broken down into five major categories of taxes and licenses and sixteen detailed categories. Montana's high percentage of earmarking to total tax revenues is emphasized by the fact that Montana earmarks every major category of taxes and earmarks 15 of the 16 detailed

categories of taxes. While all states earmark at least one of these categories of taxes, Montana's is very comprehensive, earmarking at least part of the vast majority of taxes it levies.

Table 4
Number of States Earmarking Selected Taxes* Compared to
Taxes Earmarked by Montana
Fiscal 1984

<u>Tax</u>	<u>Number of States Earmarking Tax</u>	<u>Earmarked in Montana</u>
I. Sales/Gross Receipts		
1. General Sales	28	No**
2. Public Utilities	10	Yes
3. Tobacco Products	25	Yes
4. Insurance	22	Yes
5. Parimutuels	14	Yes
6. Alcoholic Beverages	25	Yes
II. Income		
7. Individual	17	Yes
8. Corporation	16	Yes
III. Highway User		
9. Motor Fuel	43	Yes
10. Motor Vehicle Registration	39	Yes
11. Motor Vehicle Sales	11	Yes
12. Operator License	32	Yes
IV. Licenses		
13. Occupation and Business	19	Yes
14. Hunting and Fishing	40	Yes
V. Miscellaneous		
15. Property	10	Yes
16. Severance	17	Yes

*Survey based on preliminary results of survey by National Council of State Legislatures. Four states were not included in survey results.

**Montana does not levy this tax.

Table 5 provides a summary of all the taxes levied in Montana, the total amount collected, the amount of each tax earmarked, the percent earmarked, and the recipient in fiscal 1984.

Table 5
Summary of Tax Revenues Collected in Montana and
Disposition of Amounts Earmarked
Fiscal 1984

----- Total Tax -----				
<u>Tax</u>	<u>Revenues Collected (Millions)</u>	<u>Amount Earmarked (Millions)</u>	<u>Percent Earmarked</u>	<u>Recipient</u>
<u>Sales or Gross Receipts</u>				
Public Utilities	7.0	.7	10.0	Consumer Council
Tobacco Products	12.6	12.6	99.7	Building Fund
Insurance	19.5	5.9	30.0	City Police, Firemen
Alcoholic Beverages	14.8	3.6	24.0	Alcohol Treatment
Other	1.6	--	--	
<u>Income</u>				
Individual	170.3	42.6	25.0	K-12 Education
		18.7	11.0	Building Fund
Corporation	35.4	8.1	23.0	K-12 Education
<u>Highway User</u>				
Motor Fuel	79.2	58.6	74.0	State Highways
		12.7	6.0	Local Highways
		5.5	7.0	Highway Safety
		1.6	2.0	Debt Service & Admin.
		0.8	1.0	FW&P
Motor Vehicle Reg.	25.9	16.8	65.0	State Highways
		3.6	14.0	Local Highways
		3.1	12.0	Debt Service & Admin.
		2.3	9.0	Highway Safety
Operator License	1.3	0.5	40.0	Highway Safety
<u>Licenses</u>				
Occupation and Business	8.6	4.2	49.0	Licensing Boards
Hunting and Fishing	13.5	13.5	100.0	FW&P
Alcoholic Beverages	1.5	--	--	
Corporation	.5	--	--	
Other	1.1	--	--	
<u>Miscellaneous</u>				
Severance	144.8	47.8	33.0	Permanent Trust Fund
		4.3	3.0	K-12 Education
		39.1	27.0	Other
Property	38.8	20.9	54.0	K-12 Education
		12.8	33.0	Higher Education
		3.1	8.0	Livestock Program
		2.0	5.0	Vo-Ed
Death and Gift	6.0	--	--	
Other	.9	.9	100.0	Fire Protection
Totals/Average Per- cent Earmarked	583.3	355.8	61.0%	

Trends

While the percent of earmarking nationwide appears to have leveled off in recent years, it is still a popular practice, with approximately one-fourth of total state tax revenues earmarked. A recent survey of the states indicates that one-third of all states have added new earmarking provisions since 1984, while only one state has reduced earmarking provisions. Montana has added earmarking provisions recently, with the most recent provision added during the June 1986 special session (utility tax to support the Public Service Commission). Barring a systematic effort to reverse the current trend, it appears that earmarking of revenues will continue to thrive both nationally and particularly in Montana.

EVALUATION OF EARMARKING

Earmarking of state revenues is controversial, and it has become a widespread practice despite the fact that nearly all analyses and reports by officials and specialists have been highly critical of the practice. However, literature on the subject has generally recognized that there are both advantages and disadvantages. The following discussion provides a look at some of the most common criticisms and advocations of the practice, as well as some of the effects that they impart on the allocation of state fiscal resources.

Advantages of Earmarking

1. Earmarking can serve to pass the cost of providing a government service to the group or persons who are benefitting from it.

This is the most common and perhaps the strongest justification for earmarking revenues. In those cases where the service provided is a distinct benefit for a certain group of users and the cost and users can be

easily identified, tying revenues to the special use can provide for an efficient use of resources. The earmarked tax source acts as a "user" fee, and establishes a budgetary linkage that may enhance fairness. Motor fuels taxes used for highway improvements are good examples of an earmarked revenue that has this characteristic.

2. Earmarking can provide for individual participation in expressing attitudes and preferences for a service and thus have a part in collective decision-making.

Where revenues can be linked to a specified service, an individual has a degree of choice as to whether he chooses to support certain government services. By use or non-use of a particular service, an individual can influence spending and future use of that service based on demand. Hunting and fishing licenses are an example of where this argument might apply.

3. Earmarking can contribute to assuring a minimum level of expenditures for a particular program or service.

Where there is concern that the normal budgetary process can't be relied on to provide a minimum level of expenditure authorization for a program, earmarking a revenue source tends to assure more stability by providing a minimum outlay for the program. While it doesn't assure the most efficient allocation of resources between programs, it can provide managers and supporters of a particular program with the benefit of an ability to anticipate revenues and do long-range planning.

4. Earmarking can provide an incentive for program managers to be more conscientious and prudent in the management of "their own" funds.

Program managers who have access to a special fund may be motivated to better manage and conserve those funds if they know that it can lead to increased resource availability for their program. This would be less

likely to be true if the program were general funded.

5. Earmarking can serve to increase public support for a particular tax by allocating its revenue toward a program for which there is strong public support.

Earmarking has been used to overcome resistance to the passage of a new tax by tying it to a popular program. It can be argued that in this respect, earmarking can increase the total tax revenues available to a state. In other cases, however, it tends to mislead the public into supporting a tax when it may not have any effect on the allocation of resources.

Disadvantages of Earmarking

1. Earmarking can seriously impair the budgetary review process, reduce controls, and undermine state priorities.

An optimal budget management system permits legislators to see the "big picture," so that they can weigh the relative merits of each program in terms of the total funding available. But the setting aside of earmarked accounts, which in Montana amounts to 61 percent of tax and license revenues, results in fragmentation of funding policy and frustrates attempts to set optimum levels on a statewide basis. Desired priorities for state spending can be undermined by a separate system of previously committed revenues. This criticism is the most prevalent and most obvious condemnation of the practice of earmarking. This impairment was clearly present during Montana's June 1986 budget crisis special session, when across the board cuts were necessary and desired, yet so many programs were protected by earmarking and were difficult to manipulate to help resolve the crisis equitably.

2. Earmarking revenues contributes to the misallocation of funds,

resulting in over-funding some programs and under-funding others.

There is no necessary, or even probable, relationship between the optimal level of expenditures on a program and the formula established yield from an earmarked source. This will result in maldistribution of funds, with some earmarked programs undersupported while others are oversupported, or in excessive fund balances that either cannot be diverted or are difficult to divert to priority areas. This dilemma frustrated legislators in the recent budget crisis, where some earmarked fund balances that could be considered excessive were difficult or impossible to divert to share in solving the budget shortage.

3. Earmarking can reduce legislative and executive scrutiny by removing earmarked programs from effective periodic review and control.

In Montana, programs with dedicated revenues must still go through biennial review and appropriation, providing some scrutiny of those programs. However, there is a tendency for less scrutiny when it has a dedicated revenue source, particularly when it is not competing for or making a demand on the always scarce general fund. Dedicated revenue programs tend to fall "out of the limelight," and the limited discretion in manipulating earmarked revenues provides an obstacle that dampens efforts for closer review. With limited evaluation, earmarked programs can tend to become imbedded in the financial structure, sometimes even after their need ceases or has changed substantially.

4. Earmarking contributes to inflexibility of the revenue structure, making it difficult to adapt to changing conditions.

Earmarked provisions, anchored in the constitution or statute and often with complex funding structure, impart a rigidity that is impervious to shifts in needs for state programs. This inflexibility was obvious and created numerous headaches in the recent special session.

5. Earmarking complicates and introduces inefficiencies in the administration of state programs.

Earmarked revenue provisions often contain complicated formulas and procedures, making it cumbersome to identify revenue patterns and establish comprehensive revenue estimates. Further, in addition to requiring approval of an appropriation, it adds the requirement for determining revenue sources and cash balances. It requires a separate account and the costs associated with accounting for the separate fund. Earmarked funding for education and long-range building are an example of the complexity that they impart.

Effects of Earmarking

The above discussion of the pros and cons of earmarking revenues has pointed out many of the potential effects that the practice has on the budgeting process and the allocation of resources. The advantages of earmarking discussed above are primarily at the program level - it can provide a level of stability, security, and support to a particular program. On the other hand, the disadvantages of earmarking are primarily at the statewide level - it can contribute to a misallocation of resources and to the rigidity, complexity, lack of control, and inefficiency of the statewide budget process.

It is important to note, however, that simple generalizations about the impacts of earmarking could at times be misleading. The impacts on resource allocation will vary dependent upon the nature of the earmarked revenue source and the particular purpose for which the revenue is dedicated. The discussion which follows highlights some of the forces that may alter the effect of earmarking on a particular program.

One key factor that may impact how effective earmarking is in influencing resource allocation is whether the fiscal needs for a particular program are more or less than the amount of the earmarked revenue. If they are less, then earmarking may have the effect of increasing available revenues for the program. If the fiscal needs are more, however, earmarking provisions may have no effect at all on the total allocation of resources to a program, especially if the amount of the appropriation does not take into consideration the amount of earmarked revenues and the general fund makes up the difference. In a case like this, earmarking would serve no useful purpose, and would only tend to complicate and cripple the budget process. An example of this might be earmarking for support of public schools. This function, which is a major budget item and is a popular program to the public, will tend to receive a certain level of appropriation regardless of the amount of anticipated earmarked revenues. In Montana, the general fund is tasked to make up the difference in funds not provided by earmarked sources, so it is reasonable to ask what benefits are received from a complicated system of earmarking for such a program when the amount appropriated bears little or no relationship to the amount earmarked for that purpose. Although oversimplified, it appears likely that putting the revenues earmarked for education into the general fund and funding the program in full from the general fund would yield the same result.

Another effect of earmarking is that it can contribute to the expansion of total fiscal resources available to the government by increasing public support for new or increased revenue sources. The public may approve increased revenues that are attached to a popular program that it wouldn't otherwise accept, even though the majority of the additional revenues collected may never go to the benefit of the program to which it

was earmarked. Using the example of public school support discussed above, additional earmarking of revenue sources for public schools might be offset by a reduction in general fund support, and the general fund that was freed up would go to the support of other programs. In the June 1986 special session, the passage of a new utility tax to fund the Public Service Commission had the effect of creating new state revenues, but it simply shifted the support of the commission from the general fund to a state special revenue account, while the general fund that was freed up went to fund other programs. Another example from the June 1986 special session was in Highway Department, where the earmarked gas tax was increased, but state special revenue funds were diverted from other highway accounts into the general fund, resulting in no benefit to the Highway Department. These examples point to another way that the impacts of earmarking can be affected.

One additional factor that can alter the effects of earmarking is to simply manipulate and avoid its restrictive provisions. This procedure can reduce or completely eliminate the practical impacts of earmarking. There are two very common ways of accomplishing this goal. One way is to redirect accumulated balances in earmarked accounts to other purposes without repayment. A recent example of this tactic in Montana was the redirection of junk vehicle fees into the general fund and to another state special revenue fund. Another way is to expand the definition of the designated purpose to include more programs than presently included or intended. An example of this procedure occurred during the June 1986 special session. The Highway Department was 100 percent funded by other than general fund, which under standing provisions shielded it from contributing to solutions of the general fund shortage. The provisions were circumvented by expanding the definition of highway special use

earmarked funds to include the highway patrol, which had previously been general funded. As a result, the highway patrol program was placed under highways state special revenue funding, leaving fewer funds for the previously earmarked highway programs. General funds freed up went for other purposes, amounting to over \$3 million. Depending on general fund demands, the highway patrol costs have had this funding switch in previous sessions also.

Summary

The preceding discussion pointed out the pros and cons of earmarking and the effects that might be expected on the allocation of resources. Further, it demonstrated that there are other forces which will vary the impact on resource allocation dependent upon the peculiarities of that particular revenue source and program. The factors presented were not intended to be all-encompassing, but simply to demonstrate the variables which must be considered when evaluating the impacts of earmarking. Effective use of earmarking provisions requires a careful assessment of the pros and cons as well as the effects of the provisions on the allocation of resources.

Recommendation

There are clearly both advantages and disadvantages inherent in any earmarking provision. The majority of writers and organizations that have written analytical reports on the practice of earmarking have concluded that the practice is, on balance, undesirable. A number of the negative effects of the practice have been identified in this report, including many which plague the Montana budgeting and resource allocation process in varying degrees of severity. To minimize those negative impacts, in situations where the advantages of earmarking do not clearly overcome the

disadvantages, earmarking should be avoided. Further, it is suggested that the advantages of earmarking are heavily dependent on the benefit theory of taxation and that as a minimum earmarked revenues should provide a link between service costs and benefits. In situations where that link is not clearly obvious, earmarking provisions should be considered for elimination. Montana has several earmarking provisions where a user/benefit relationship is not present.

The points made above, along with the recognition that the number and fund balances of Montana's earmarked accounts have mushroomed in the past few years demonstrate that a need exists to examine the value of current state special revenue accounts. With this in mind, all state special revenue accounts and their corresponding revenue dedications are reviewed within functional categories to evaluate the advantages versus the disadvantages and the corresponding effects on the budget process, with an eye toward reducing earmarked accounts and provisions to only those which are considered to be predominantly advantageous.

EVALUATION OF STATE SPECIAL REVENUE ACCOUNTS

Criteria for Evaluation

There are 212 state special revenue accounts as of June 30, 1986. It is a monumental task to evaluate the merits of each account, recognizing that there are such complex political and analytical issues involved. To provide a framework for the decision process, we have developed a suggested set of objective criteria against which individual or groups of accounts can be analyzed. The criteria reflect the effects most commonly attributed to earmarking that can be measured with a reasonable degree of objectivity. The criteria questions are designed such that a "no" answer identifies a potentially negative aspect of earmarking. The answer to each

criteria do not carry equal weight, nor is there a finite number of "yes" or "no" answers or a formula for making an evaluation. As was demonstrated in the previous section of this report, the validity of the assumptions inherent in these criteria regarding the effects they impart varies from situation to situation depending on the particular manner in which the accounts are earmarked. In addition, decisions about earmarking, just like any other public policy issue, will necessarily include value judgments. The criteria provide the framework for an objective analysis upon which to attach value judgments in reaching a decision as to the disposition of the account.

The criteria could be used for any of the following purposes: (1) a one-time analysis of existing state special revenue accounts, (2) a periodic review of state special revenue accounts, or (3) when examining the merits of establishing a new state special revenue account.

The suggested criteria are presented below. Each one is followed by an explanation of what the criteria is intended to contribute to the analysis.

1. Is there a direct user/benefit relationship (i.e., does it satisfy the benefit theory of taxation)?

The principle and basic tenets of earmarking are built upon the benefit theory of taxation. It should be a minimum requirement that there be a direct relationship between user/service costs/benefits. A "no" answer to this question should result in serious consideration for elimination of the account and the earmarking provision. A possible exception might be investment contributions to a trust fund.

2. Do the earmarked revenues generate funds at a level which is at or near the required expenditure?

This would identify those earmarked provisions which contribute to misallocation of resources by undersupport or oversupport of a program.

3. Is the program self-sufficient, i.e., does it operate without supplemental general funds?

This would identify those programs whose fiscal needs exceed the amounts generated by its earmarked sources. The program should be carefully reviewed to ascertain whether appropriation levels bear any relationship to the amount earmarked for that purpose. If not, there appears to be no purpose for earmarking funds.

4. Do ending balances at year end transfer to the general fund?

If not, is carryover of the fund balance necessary and appropriate?

This would identify accounts where transfer of all or part of year end balances to the general fund might be appropriate. At a minimum, state special revenue accounts for programs which are supplemented by general funds should have ending balances revert to the general fund. In other circumstances it may be necessary to allow carryover of ending balances, but in cases where fund balances become excessive, they should be considered for either transfer to the general fund or for adjustment of the tax or fee downward. Provisions for automatic transfer of ending balances should be implemented wherever appropriate, making the accounts act more like a general fund, and reducing inefficiency and misallocation of resources.

5. Is the state special revenue account required by either statute or the constitution?

If not, is it essential that the account be classified as a state special revenue account?

This would identify the legal basis for the state special revenue account classification, and would single out those accounts which are administratively classified. The administratively classified accounts, many of which are simply transfer accounts, should be carefully scrutinized and in many cases can probably be reclassified or eliminated. The statutes appear to have been liberally interpreted in the past and many which are identified as having legal basis in statute may not deserve that status.

6. Is the account appropriately classified as a state special revenue account (as opposed to a more appropriate type of account classification, other than general fund)?

This would identify accounts which may be improperly classified as a state special revenue account. Criterion number 5 above should have already accomplished this for accounts not based in statute or the constitution, but even some of those based in statute may have a more appropriate classification, and action should be taken to have them reclassified.

7. Is it cost effective to operate the account as a separate special revenue fund? Determine by answering the following questions:
 - a. Are total revenues collected at least \$50,000 per year?
 - b. If not, are the incremental accounting costs, budgeting costs, and legislative efforts in reviewing and appropriating for a separate accounting entity justified and reasonable?
 - c. Can the funds be accounted for by means other than using a state special revenue account?

This would identify accounts which are not cost effective to operate as a state special revenue account from a budget management perspective. A significant number of state special revenue accounts have a low volume of activity, making separate account management difficult to justify.

8. Is the original legislative intent of the earmarking provision and program still valid, i.e.:

a. Does it comply with statute?

b. Does the original need for the earmarked account still exist?

This would identify accounts that have strayed from their original purpose and have avoided close scrutiny.

9. Is the account active, i.e., has it been used within the past year?

If not used for over a year, can the administering agency justify the need for the account?

This would identify accounts which have become inactive and are no longer required, but haven't been deleted.

10. Is the account permanent, i.e., is the funding for a continuing program?

This would identify accounts that had been set up as state special revenue accounts to administer temporary programs, such as grants, or other programs that simply don't need a long range, dedicated funding source.

Account Classification/Evaluation

For the purpose of a general analysis of the 212 state special revenue accounts at June 30, 1986, the accounts were broken down into 17 functional classifications. The classifications, table reference, the number of accounts classified in each category, and the fund balance at June 30, 1986 are listed in table 6.

Table 6
State Special Revenue Accounts - Fiscal 1986
Functional Classification

<u>Table</u>	<u>Type of Account</u>	<u>Number of of Accounts</u>	<u>Fund Balance</u>
7	Regulatory	43	\$ 7,219,467
8	Business Regulation	32	1,578,690
9	Canteen	9	157,349
10	Donations	13	80,837
11	Distribution	7	1,715,415
12	Grant Administration	5	7,686,759
13	Loan Administration	6	23,021,771
14	Program Administration	5	(368,832)
15	Insurance Proceeds	8	3,411
16	Local Assistance	2	(1,643,204)
17	Reimbursement	7	589,577
18	Trusts	4	570,181
19	User Fees	28	78,170,172
20	Education	15	8,375,559
21	Highway	3	23,401,814
22	Social Services	3	362,516
23	Natural Resources	14	3,202,583
24	Unclassified - Delete	8	12,210
	Total	<u>212</u>	<u>\$154,136,275</u>

Tables 7 through 24 provide an account by account listing of all state special revenue accounts by their functional classification. The tables show the account name, the administering agency, the fiscal 1986 revenues, expenses, and year end fund balance. A brief narrative of the functional classification precedes each table. In those cases where collective action on a particular functional category may be appropriate, an options is also presented. The majority of categories, however, collectively fit the parameters of a state special revenue account, and no additional comment is provided.

The following general analysis is not intended to take the place of an account by account analysis using selected criteria. Within each functional category, there may be individual accounts which should be considered for

Table 7
State Special Revenue Accounts
Regulatory

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02801	Consumer Counsel	D of R Consumer Counsel Tax	\$ 811,769	\$ 461,316	\$ 718,019
02426	Livestock	Animal Health Emergency	37,462	78,000	10,181
02425	Livestock	Inspection & Control	2,324,381	2,182,510	1,863,511
02427	Livestock	Animal Health	1,042,275	963,441	745,169
02069	Administration	Passenger Tramway Receipts	17,628	-0-	17,628
02452	Agriculture	Commercial Fertilizer	158,213	136,645	117,521
02453	Agriculture	Grain Services	295,135	241,061	89,225
02071	Agriculture	Anhydrous Ammonia Account	12,457	-0-	12,457
02454	Agriculture	Commercial Feed	101,213	135,994	67,196
02461	Agriculture	Alfalfa Seed Assessment	8,595	15,193	11,701
02448	Commerce	Construction Regulation	866,941	1,088,920	113,878
02077	Commerce	Financial Institutions Div.	804,545	691,119	113,426
02081	Commerce	Montana Lemon Law SSRA	-0-	-0-	-0-
02817	Commerce	Milk Control	297,971	288,815	116,486
02836	Commerce	Milk Testing	996	-0-	794
02079	Commerce	Fireworks' Wholesalers	715	30	685
02413	FW&P	F & G Motorboat Cert. Id.	45,228	48,220	8,580
02414	FW&P	Snowmobile Regulations	39,449	36,113	11,200
02059	Health	EMT Certification	18,843	14,991	3,265
02806	Health	Environmental Fees EIS	-0-	-0-	10
02421	Health	Water Testing	117,514	88,480	134,525
02462	Health	Local Board Inspection Fund	204,408	203,796	1,377
02064	Health	PKU Testing	91,270	17,897	73,373
02417	Health	Environ. Quality Variance Review	12,877	12,574	303
02418	Health	Subdivision Plat Review	127,370	42,850	84,945
02845	Health	Junk Vehicle Disposal	715,897	836,866	1,437,904
02420	Health	Bd. of Cert. for W & WW Op.	27,208	18,938	40,940
02804	Justice	Escheated Estates	9,014	20,118	238
02441	Revenue	Cigarette Enforcement	15,035	15,078	(42)
02074	Revenue	Gambling License Fee Account	2,389,843	1,876,006	513,837
02838	State Lands	DSL Env. Impact Statements	257,387	278,122	(16,646)
02073	State Lands	Forestry - Slash Disposal	37,342	54,670	89,083
02837	State Lands	Slash & Brush Disposal	194,607	315,946	159,002
02431	DNRC	Water Adjudication	9,282	-0-	137,522
02430	DNRC	Water Rights Appropriation	77,278	76,850	80,675
02429	DNRC	Weather Modification	827	-0-	6,163
02825	DNRC	Water Well Contractors	27,817	33,978	23,937
02428	DNRC	Motor Facility Siting	200,288	188,936	165,751
02438	DNRC	Floodway Obstruction Removal	-0-	-0-	400
02432	DNRC	Oil & Gas ERA	736,137	900,825	220,173
02036	Labor	Private Employment Agencies	1,722	3,250	(1,528)
02044	State Auditor	Securities Regulatory Account	1,986,908	1,982,715	4,193
02060	State Auditor	Insurance Regulatory Account	1,094,173	1,051,764	42,410

Business Regulation Accounts

The business regulation accounts are set up to fund the professions and occupational boards that license and regulate those professional and occupations as deemed necessary for the protection and well-being of the public. License fees assessed the members of those professions and occupations are designed to pay for the costs of regulation and related costs of the boards. A state special revenue account is an appropriate means of budgeting and accounting for this program. The 32 accounts classified as business regulation accounts are listed in table 8.

Table 8
State Special Revenue Accounts
Business Regulation

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02029	Commerce	Board of Horse Racing	\$236,871	\$202,263	\$ 81,117
02818	Commerce	Electrical Board	79,027	63,593	129,260
02830	Commerce	Board of Dentists	80,934	46,883	57,081
02841	Commerce	Board of Athletics	2,656	5,784	2,006
02840	Commerce	Board of Social Workers	2,300	13,013	(9,731)
02816	Commerce	Board of Sanitarians	7,035	4,694	14,495
02835	Commerce	Board of Barbers	27,471	24,466	42,005
02814	Commerce	Brd of Hearing Aid Dispen.	7,557	10,745	7,103
02834	Commerce	Board of Veterinarians	23,100	21,711	24,563
02812	Commerce	Physical Therapists	23,570	11,749	35,440
02833	Commerce	Board of Nursing	144,383	160,482	158,610
02810	Commerce	Bd. of Radiologic Technologists	28,577	11,751	26,590
02832	Commerce	Board of Pharmacy	94,675	96,089	60,390
02808	Commerce	Board of Landscape Architects	5,023	6,861	9,338
02831	Commerce	Board of Optometrists	28,230	19,391	30,800
02446	Commerce	Board of Psychologist Exam	14,215	15,120	13,309
02843	Commerce	Board of Denturety - Special Rev.	6,900	5,899	2,621
02842	Commerce	Board of Polygraph Licensing	2,505	2,810	1,070
02821	Commerce	Board of Morticians	18,970	21,018	16,698
02819	Commerce	Real Estate	213,541	272,628	74,740
02815	Commerce	Board of Public Accountants	110,955	123,155	214,308
02829	Commerce	Private Investigators	25,516	27,658	(10,019)
02811	Commerce	Board of Podiatry Exam	-0-	-0-	-0-
02078	Commerce	Occupational Therapists	5,440	2,025	3,415
02820	Commerce	Board of Architects	38,116	35,914	56,531
02828	Commerce	Board of Plumbers	88,769	81,093	49,298
02823	Commerce	Professional Engineers	117,482	97,677	102,434
02822	Commerce	Board of Chiropractors	17,835	21,916	1,741
02809	Commerce	Board of Speech Pathologists	3,515	6,299	9,184
02813	Commerce	Board of Nursing Home Admin.	17,635	18,767	16,052
02824	Commerce	Board of Medical Examiners	109,495	142,500	112,958
02826	Commerce	Cosmetology Board	233,352	116,880	245,283

Canteen Accounts

Canteen accounts are separate state special revenue accounts set up for canteen operations at state institutions. The canteens sell drink and food items, and in some cases they sell clothing and other merchandise. The accounts are used for the purchase and sale of canteen items, but they do not fund most of the personal services and overhead of operating the canteens. Staff support and other overhead costs are paid out of the general fund.

Since the canteen operations are supported by general fund, the committee may wish to consider transferring the canteen operations to general fund. Revenues from each operation could still be tracked in general fund correspondent with individual revenue estimates, and compared to expenditures to ensure that revenues generated are at the desired level and/or require the Department of Institutions to recover the cost of goods sold.

The nine state special revenue accounts classified as canteen accounts are listed in table 9.

Table 9
State Special Revenue Accounts
Canteens

<u>SBAS</u>	<u>Administering</u>				
<u>A/C #</u>	<u>Agency</u>	<u>Account Name</u>	<u>FY 86 Rev.</u>	<u>FY 86 Exp.</u>	<u>F/B 6/30/86</u>
02914	Center for Aged	CFA - Canteen	\$ 4,409	\$ 3,959	\$10,575
02846	MT Devel. Center	MDC - Canteen	4,123	7,844	210
02921	MT State Hospital	MSH - Canteen	125,422	116,924	49,644
02917	MT State Prison	MSP - Canteen	428,016	404,014	55,557
02915	Mtn View School	MVS - Canteen	1,538	982	556
02916	Pine Hills School	PHS - Canteen	14,619	13,758	861
02918	SRV Forest Camp	SRVFC - Canteen	27,026	26,465	3,656
02919	SRV Forest Camp	SRVFC - Clothing Account	27,171	26,000	35,837
02920	Veterans' Home	Veterans' Home - Canteen	15,791	15,338	453

Donation Accounts

Donation accounts reflect moneys donated to specific programs from private sources. Donations are given by the donors for a specified purpose and often with restrictions on spending. The 13 state special revenue accounts classified as donation accounts are listed in table 10.

Table 10
State Special Revenue Accounts
Donations

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02924	Center for Aged	CFA - Donations	\$ 105	\$ -0-	\$ 105
02061	FW&P	Non-Game Wildlife Account	25,890	37,528	48,158
02089	Revenue	Child Abuse & Neglect Program	47,926	1,983	45,943
02087	Revenue	Public Campaign Fund	2,611	3,274	3,275
02925	Estmnt. Train Ctr	Eastmont - Donations	707	2,933	(2,226)
02012	Governor's Office	Statehood Centennial Office	46,578	45,847	1,369
02922	Institutions	ICO - Donations	625	175	449
02923	MDC	MDC - Donations	8,633	20,764	(12,132)
02035	MDC	MDC - Donations - Prevoc. Ctr.	-0-	-0-	-0-
02929	MSH	MSH - Donations	5,247	7,777	(4,584)
02926	Mtn View School	MVS - Donations	1,004	733	271
02927	Pine Hills School	PHS - Donations	4,110	3,901	209
02928	SRY Forest Camp	SRYFC - Donations	-0-	-0-	-0-

Distribution Accounts

The accounts classified as distribution accounts are primarily administrative convenience accounts. They function as a collection device for certain revenues which are then transferred to other accounts for their end use purpose. The most common example, as evidenced by the table below, are tax collection accounts, where earmarked tax revenues are collected for distribution to an end-use purpose. The seven state special revenue accounts classified as distribution accounts are listed in table 11.

Table 11
State Special Revenue Accounts
Distribution

<u>SBAS</u> <u>A/C #</u>	<u>Agency</u>	<u>Administering</u> <u>Account Name</u>	<u>FY 86 Rev.</u>	<u>FY 86 Exp.</u>	<u>F/B 6/30/86</u>
02027	Revenue	RIT Fund Interest	\$4,152,305	\$4,852,061	\$1,398,311
02046	Revenue	Corporation Tax - Fin. Inst.	5,639,762	5,639,762	-0-
02083	Revenue	Oil & Gas Local Assistance Tax	-0-	-0-	-0-
02442	Revenue	Alcohol Taxes - Local Assist.	2,506,044	2,521,012	(17,267)
02401	State Auditor	Police/Fire Retirement Fund	5,300,000	5,009,340	334,273
02802	State Auditor	Firemen/Pension Adjustment	930,748	959,100	-0-
02416	FW & P	Wardens Retirement - Fines	221,123	221,265	98

Grant Administration Accounts

Grant administration accounts are those which are set up to administer a grant program. They receive grant funds which are then awarded and distributed from that account to grant recipients. Two of the accounts, water development and alternative energy research, are significantly devoted to grant administration, although other activities related to natural resource programs are also funded by those accounts. The five state special revenue accounts classified as grant administration accounts are listed in table 12.

Table 12
State Special Revenue Accounts
Grant Administration

<u>SBAS</u> <u>A/C #</u>	<u>Administering</u> <u>Agency</u>	<u>Account Name</u>	<u>FY 86 Rev.</u>	<u>FY 86 Exp.</u>	<u>F/B 6/30/86</u>
02445	Commerce	Local Impact - Coal Sev. Tax	\$2,526,516	\$5,271,012	\$2,677,816
02435	DNRC	Water Development	2,525,352	2,235,898	1,396,429
02458	DNRC	Natural Resources Grant Prog.	619,644	829,192	(209,548)
02434	DNRC	Conservation District Grants	210,659	231,287	(3,888)
02437	DNRC	Alt. Energy Research, Dev.	1,134,922	1,711,464	3,825,950

Loan Administration Accounts

Loan program accounts are those established to administer loan programs that are offered by state agencies. The account receives loan funds from bonds and other sources, disburses funds in the form of loans and debt retirement, and receives loan payoffs from borrowers. The six state special revenue accounts classified as loan administration accounts are listed in table 13.

Table 13
State Special Revenue Accounts
Loan Administration

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02062	Admin.	Airport Loans Special Revenue	\$ 1,897,144	\$ 318,999	\$2,655,779
02439	DNRC	Water Dev. GO Bond Proc.	1,987,944	13,570	1,337,983
02087	DNRC	CST Bond Proc. - 1985 Ser A	16,982,581	11,811,446	5,171,135
02091	DNRC	1985 Ser B Var Rate CST Bonds	11,534,443	1,481,603	8,780,340
02052	DNRC	Rangeland Improvement Loans	137,704	11,910	859,367
02094	DNRC	1984 Coal Sev. Tax Proceeds	49,871	131	4,217,167

Program Administration Accounts

Program administration accounts were established to pay the cost of administering programs and to recover the administrative costs of providing that service from moneys that fund the overall program. As an example, the Professional Occupational Administrative Services account in Department of Commerce pays the costs of administering the professional and occupational licensing boards and recovers a proportionate share of the costs from each board.

For two of the accounts listed in the table below, drivers license collections and unclaimed property, the programs are at least partially funded out of general fund. For simplicity, the committee may wish to consider transferring the administrative accounts to the general fund, resulting in funding the entire program from the general fund and avoiding the need to have two separate accounts and recover administrative costs. For example, if the appropriation amounts for administration of unclaimed property were added to the general fund, the entire fund would be general funded, and no cost recovery would be required. The six state special revenue accounts classified as program administration accounts are listed in table 14.

Table 14
State Special Revenue Accounts
Program Administration

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02030	Administration	Arch/Engineering Construction	\$ 537,337	\$ 531,160	\$ 25,596
02028	Commerce	Prof. Occupational Admin. Svcs	128,811	134,586	16,577
02017	Justice	Drivers License Collections	47,557	46,023	7,475
02025	Revenue	Unclaimed Property	53,455	53,455	-0-
02455	Labor	Workers' Compensation Division	5,756,583	6,249,939	(450,798)
02068	Agriculture	Noxious Weed Admin. Account	40,387	8,069	32,318

Insurance Proceeds Accounts

Insurance proceeds accounts have been set up by several agencies as a means of accounting for receipt of revenues from insurance claims and the cost of repair or replacement of damaged property utilizing those funds. The account acts as a clearing account for this process. The difficulty with classifying the account as a state special revenue account is that expenditure of funds must go through the appropriation process, which is not practical where insurance losses and the resulting claim receipts and replacement costs are both unpredictable and inestimable by agency.

The executive branch, in Montana Operations Manual Management Memo number 2-87-1, entitled "Accounting For Insurance Proceeds," set up a centralized payment process for repair/replacement of insured state property through the Tort Claims Division. Claims by agencies will be paid from a central agency fund, thus eliminating the requirement for separate agency state special revenue accounts and the need to request appropriation authority. It will not eliminate the need for separate accounts for agencies who have policies for property not covered under the state policy.

The eight state special revenue accounts classified as insurance proceeds accounts are listed in table 15.

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The eight state special revenue accounts classified as insurance proceeds accounts are listed in table 15.

Table 15
State Special Revenue Accounts
Insurance Proceeds

SBAS	Administering			
<u>A/C #</u>	<u>Agency</u>	<u>Account Name</u>	<u>FY 86 Rev.</u>	<u>FY 86 Exp.</u> <u>F/B 6/30/86</u>
02098	Administration	Insurance Proceeds	\$ -0-	\$ -0- \$ -0-
02023	FW & P	Insurance Proceeds	3,500	3,500 252
02847	Health	Insurance Proceeds	-0-	-0- -0-
02014	Justice	Justice Insurance Clearing A/C	4,308	8,129 207
02839	Institutions	ICO Insurance Proceeds	-0-	-0- 705
02911	MT Dev. Ct.	BRSB Insurance Proceeds	-0-	-0- 2,247
02913	MT State Hosp.	MSB Insurance Proceeds	-0-	-0- -0-
02912	MT State Prison	MSP Insurance Proceeds	-0-	-0- -0-

Local Assistance Accounts

Local assistance accounts are those set up to administer the distribution of program funds to local governmental entities. The two state special revenue accounts classified as local assistance accounts are listed in table 16.

Table 16
State Special Revenue Accounts
Local Assistance

<u>SBAS</u>	<u>Administering</u>				
<u>A/C #</u>	<u>Agency</u>	<u>Account Name</u>	<u>FY 86 Rev.</u>	<u>FY 86 Exp.</u>	<u>F/B 6/30/86</u>
02090	Commerce	Local Government Block Grant	\$13,690,695	\$15,342,690	\$(1,643,345)
02444	Commerce	County Land Plan	421,086	420,945	141

Reimbursement Accounts

Reimbursement accounts are established to simply recoup the costs or part of the costs of a program. Most commonly, it involves a service or product provided to an individual or entity for which actual costs are calculated and billed to the recipient. They do not qualify as proprietary funds since they do not recover some overhead costs. Those overhead costs are supported by general fund or other funds.

The seven state special revenue accounts classified as reimbursement accounts are listed in table 17.

Table 17
State Special Revenue Accounts
Reimbursement

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02047	Comm Pol. Prac.	Copying Fees	\$ 264	\$ 48	\$ 519
02019	Justice	MT Highway Patrol ID Card	1,842	1,494	1,763
02015	Justice	Criminal Lab	2,102	-0-	8,355
02093	Judiciary	Westlaw	17,793	17,781	565
02800	Leg. Council	Montana Codes Annotated	745,736	312,743	550,149
02008	OPI	Indirect Cost Reimbursement	388,365	409,795	20,896
02001	OPI	School Lunch Program	16,777	14,000	7,330

Trust Accounts

Trust accounts are set up for assets held in a trustee capacity or as an agent. A fiduciary relationship exists between the administering agency and the trustor. The three accounts listed in table 18 appear to involve a fiduciary relationship, and since there appears to be property held in trust, it may be inappropriate to classify them as state special revenue accounts, although all three accounts are designated in statute as a state special revenue fund. The committee may wish to consider taking action to transfer the accounts to a trust fund designation.

The three state special revenue accounts classified as trust accounts are listed in table 18.

Table 18
State Special Revenue Accounts
Trusts

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02049	Commerce	Hard-Rock Mining	490,141	89,830	400,311
02084	Commerce	Hard-Rock Mining Impact A/C	-0-	-0-	-0-
02082	Commerce	Real Estate Recovery Account	169,870	-0-	169,870

User Fee Accounts

The 28 accounts classified as user fee accounts are those in which there is a direct user-benefit relationship. The revenues are generated by those who benefit from a service or product, such as hunting licenses. The state special revenue accounts classified as user fee accounts are listed in table 19.

Table 19
State Special Revenue Accounts
User Fees

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02447	Administration	Workers' Comp. Court Sr.	\$ 316,030	\$ 311,966	\$ 53,333
02072	Agriculture	Training Fund	4,135	6,938	2,821
02827	Commerce	Aeronautics Division	432,555	526,772	648,544
02415	FW&P	Fishing Access Site Acq.	383,871	485,480	933,721
02085	FW&P	Waterfowl Stamp Spec. Rev.	2,609	-0-	2,609
02412	FW&P	Motorboat Fuel Tax	584,571	788,964	281,162
02086	FW&P	Mountain Sheep Account	71,100	-0-	71,100
02407	FW&P	Snowmobile Fuel Tax	334,405	303,295	85,316
02409	FW&P	FW&P General License	15,861,011	15,668,000	8,975,755
02095	Health	Laboratory Fees	193,214	215,416	80,221
02419	Health	Vital Statistics	85,813	69,804	27,309
02422	Highways	Highways Special Revenue	118,009,744	134,823,840	63,760,022
02016	Justice	Criminal Justice Info. System	185,055	188,000	57,640
02013	Justice	Law Enforcement Academy	59,924	65,753	10,177
02404	Justice	Motor Vehicle	3,401,138	4,104,317	1,267,630
02018	Justice	Driver Rehabilitation	30,901	27,500	20,559
02450	State Lands	State Lands Res. Dev.	453,352	993,933	602,723
02449	State Lands	Timber Stand Improvement	214,660	278,564	139,220
02451	State Lands	Reclamation Hardrock	12,115	7,080	70,695
02031	State Lands	Foresters Nursery	122,570	108,223	28,111
02433	DNRC	Grazing District Fees	7,099	4,813	7,708
02034	Institutions	Alcoholism Treatment - Rehab.	3,749,833	3,716,323	381,288
02042	Leg. Auditor	Legislative Audit	1,036,692	866,543	332,414
02456	OPI	Audiovisual and Media Library	130,760	148,177	23,606
02457	OPI	Resources and Assessment	2,004	1,478	14,857
02464	Sec. of State	AG Lien Filing Fees	208,915	163,987	44,928
02400	Sec. of State	Administrative Rules	165,800	158,869	42,545
02803	State Auditor	Central Payroll Operating	242,342	303,976	204,158

Education Accounts

Education accounts are those used primarily for educational purposes, including millage, public education funds, cultural programs, and other individual accounts set up to provide an educational service for a specific program. The 15 state special revenue accounts classified as education accounts are listed in table 20.

Table 20
State Special Revenue Accounts
Education

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02022	Board/Regents	Regents Coal Tax Fund	\$ 2,586,493	\$ 2,421,328	\$1,340,127
02443	Comm Higher Ed.	University Millage	14,666,191	14,384,000	3,986,721
02045	Mtn View School	Staff Development Program	-0-	-0-	-0-
02403	OPI	Public School Equalization	140,082,929	170,921,544	86,877
02402	OPI	Traffic and Safety Education	1,265,048	1,197,913	1,268,648
02053	OPI	Dist-Adult Basic Education	1,361,293	147,523	1,322,450
02075	OPI	Coal Invest. Earnings - Vo-Techs	895,000	895,000	-0-
02900	OPI	State Deficiency Levy	8,955	-0-	88,922
02076	OPI	Millage - Vo-Techs	903,288	903,288	-0-
02066	Agriculture	Agriculture in MT Schools	5,173	502	4,671
02406	Historical Soc.	Cultural and Aesthetic Project	39,646	188,367	(148,721)
02026	Library Comm.	State Funds - Other	75,000	74,972	28
02405	Library Comm.	State Library	421,086	430,614	15,341
02009	MT Arts Council	Cultural & Aesthetic Project	840,931	530,360	410,495
02930	Revenue	Property Value Training Program	37,760	28,760	-0-

Highway Accounts

The highways state special revenue accounts are those set up for highway construction and highway improvements and maintenance, funded from earmarked revenue sources including gas taxes, coal severance taxes and mineral regulation taxes. The three state special revenue accounts classified as highway accounts are listed in table 21.

Table 21
State Special Revenue Accounts
Highway

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02050	Highways	Highway Revenue Bond Proceeds	\$ 3,226,023	\$14,589,386	\$12,787,354
02424	Highways	Highway Reconstruction	22,598,722	29,586,713	86
02100	Highways	Construction Account No. 2	1,833,879	12,896,700	10,614,374

Social Services

Social Services accounts include those which fund a particular social service program from earmarked revenues. The three state special revenue accounts classified as social services accounts are listed in table 22.

Table 22
State Special Revenue Accounts
Social Services

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02011	Labor	DWC - Crime Victims Compensation	\$ 407,241	\$ 922,940	\$251,537
02048	SRS	Public Assistance County Levy	7,111,347	7,111,347	-0-
02440	SRS	Industrial Accident Rehab.	657,310	666,181	110,979

Natural Resources Accounts

The accounts classified as natural resources include those set up to account for programs in parks, reclamation, renewable resource, and other natural resource management programs. The 14 state special revenue accounts classified as natural resources accounts are listed in table 23.

Table 23
State Special Revenue Accounts
Natural Resources

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02067	Agriculture	DNR Weed Control	\$ 260,571	\$ 249,203	\$ 11,367
02099	Highways	Energy Grants	-0-	-0-	-0-
02463	State Lands	Renewable Resource Development	3,125	3,125	-0-
02436	DNRC	Renewable Resources	1,588,364	467,798	1,682,522
02088	Library Comm.	DSL - Office of Surface Mining	75,000	22,805	52,195
02070	Health	RIT - DHES	375,312	133,442	241,870
02063	Health	Legacy Grants	115,000	115,000	-0-
02096	State Lands	Reclamation - Bond Forfeitures	342,071	42,623	299,448
02010	DNRC	Oil & Gas Surety Bond Default	-0-	-0-	12,678
02024	DNRC	DNR Resource Industrial Trust	-0-	-0-	-0-
02097	Governor's Ofc.	Resource Indemnity Monies - DNRC	18,000	18,000	-0-
02410	FW&P	Real Estate Trust Earnings	69,694	53,476	78,377
02408	FW&P	Coal Tax Trust Earnings	1,682,115	1,120,434	711,988
02411	FW&P	State Park Miscellaneous	427,137	426,468	112,138

Unclassified

The eight accounts listed in table 24 were not classified inasmuch as they are inactive and should be deleted from the accounting system.

Table 24
State Special Revenue Accounts
Inactive - To Be Deleted

SBAS A/C #	Administering Agency	Account Name	FY 86 Rev.	FY 86 Exp.	F/B 6/30/86
02080	Commerce	Science & Tech. R & D Account	\$-0-	\$-0-	\$ -0-
02002	OPI	Traffic Ed Mobile Simulator	-0-	-0-	-0-
02051	Highways	Maintenance A/R's	-0-	-0-	-0-
02423	Highways	Coal Area Highway Improvement	-0-	-0-	-0-
02459	Highways	Stores Inventory	-0-	-0-	-0-
02032	State Lands	Forest - Resource Indemnity Trust	-0-	-0-	-0-
02033	State Lands	Lands - Resource Indemnity Trust	-0-	-0-	-0-
02043	Administration	Merit System Council	-0-	-0-	12,210

GENERAL CONTROLS

There are several possible possible methods of establishing better general controls over both existing and future earmarking provisions and state special revenue accounts. These methods and their merits are discussed below.

1. Review and eliminate, to the fullest extent possible, restrictions against the transfer of unobligated balances in state special revenue accounts to the general fund.

This provision would eliminate some of the protective covenants that earmarking traditionally provides, but it would improve flexibility and the opportunity for effective allocation of resources. In the case of earmarked accounts whose programs are supplemented by general fund, the transfer of year end unobligated balances could be made automatic. Some states even have provisions that certain earmarked accounts and their revenues are restricted only until certain obligations are met. Once those obligations are met, the balances in those accounts are transferred to the general fund.

2. Establish the requirement for a biennial review of all state special revenue accounts using prescribed criteria for evaluation such as the criteria suggested in this report.

Although Montana includes state special revenue accounts in the biennial budget process, it can be argued that it doesn't receive the same scrutiny that a general fund appropriation would. In addition, the many variables impacting on the behavior of a state special revenue account make periodic review prudent.

3. Establish the requirement that new earmarking of revenues be enacted only after referral to the House Appropriations and Senate Finance and Claims Committees to consider the impact of budget flexibility, controls, and other implications.

This provision provides a forum for consideration of the side effects of earmarking provisions that may easily be overlooked in the normal decision process.

SUMMARY

The controversial and frequently criticized practice of earmarking revenues for specific programs thrives in Montana's budgeting system. Over the past 30 years, when most other states have shown a decline in the percentage of total tax revenues earmarked, Montana continues to use the practice extensively, ranking third amongst the states for percentage of tax revenues earmarked (61 percent). While there are some benefits derived from earmarking, there can be many damaging effects including distortion of the budget process, misallocation of funds, loss of flexibility and controls over the budget process. Several examples of these negative effects have been pointed out in this report. Most positive effects of earmarking accrue to the benefit of the programs which enjoy their protective covenants and to the special interests which support those programs. The damaging effects on the other hand generally impact the statewide level, interfering with the fiscal management process. Several examples of negative impacts of earmarking during the recent general fund budget crisis were pointed out in this report. The high percentage of earmarking severely eroded budgetary flexibility as protected revenues and programs were either untouchable or required confusing manipulative measures to include them in the solution to the crisis. It can be argued that the budget shortfall crisis would have been substantially easier to resolve had

it not been for the myriad of restrictive earmarking provisions. At the end of fiscal 1986, Montana had over \$154 million tucked away in protected state special revenue accounts.

In view of the many problems earmarking can and has created in Montana's budget process, an analysis of earmarking provisions appears to be appropriate to reduce the practice to only those cases where the advantages clearly outweigh the disadvantages. A suggested set of criteria has been presented to assist in an objective review of the state special revenue accounts, which serve as a depository for the majority of Montana's earmarked revenues. The current accounts have been classified by function. In addition, several possible general controls over earmarking provisions and state special revenue accounts have been presented.

ISSUES AND OPTIONS

ISSUE 1: Does the committee want to implement a procedure for review of all current state special revenue accounts?

Option 1: Adopt the evaluation criteria suggested in this report and establish a subcommittee or task force to review all state special revenue accounts and make recommendations for their disposition to the committee.

Option 2: Develop and adopt an alternate set of evaluation criteria and assign a subcommittee to review all state special revenue accounts and make recommendation for their disposition to the committee.

Option 3: Request that the Department of Administration take the evaluation criteria suggested in this report under consideration and report back to the committee on streamlining the earmarked revenue accounts.

Option 4: Take no action.

ISSUE 2: Does the committee want to develop a set of general controls for establishing future state special revenue accounts and earmarking revenues?

Option 1: Adopt the suggested general controls presented in this report and develop legislation to implement those controls for introduction at the 1987 legislative session.

Option 2: Develop and adopt an alternate set of general controls and develop legislation to implement those controls for introduction at the 1987 legislative session.

Option 3: Take no action.

COMMITTEE

DATE January 21, 1987

PLEASE LEAVE PREPARED STATEMENT WITH SECRETARY.

Testimony of Brenda Schye
Montana Cultural Advocacy
on HB 149

I represent the Montana Cultural Advocacy, which is a broad cross-section of Montanans who are committed to the development of this state's cultural and artistic resources. Included in that broad goal is our support for the collection and preservation of historic records for use by future generations.

A serious gap exists in the information that Montanans have about the legislative decisions that have shaped this state. While there's not much we can do about that lack of information from the past, we can have the foresight to ensure that future generations will be in a better position to understand what brings you to your decisions in the present.

The Legislative Council librarian can attest to the heavy use of existing committee minutes, which are extremely valuable in helping to establish legislative intent, and determining where the support and opposition came from, and what arguments were set forth by each side. But the majority of legislators must base their

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voting decisions on the arguments set forth during the committee of the whole debate, as only a small number of them hear the public testimony. If legislative decisions are based on Second Reading debate, it seems only reasonable that there should be a record of those proceedings.

From our perspective, these proposed recordings will have major historical significance, and for that reason we urge your support of this bill.