Montana League of Cities and Towns
Legislative Report
2010 District Meetings

The National Economy and State and Local Finance

As the nation begins to stagger away from the wreckage of the most destructive economic collapse since the Great Depression, state and local governments will be challenged to balance budgets with revenues that have been stunted by the decline in almost every category of economic activity across all regions of the land.

Montana has avoided the catastrophic deficits and desperate tax patches that have been required to balance budgets in most other states. This favorable position is the result of careful budgeting and management and a tax system that is more stable than those in California and other states based on the fantasy of endless economic expansion.

At the end of April, the Governor announced the state was sitting on a $400-million budget cushion that was the combination of $41-million in spending cuts, $85-million in one-time coal lease payments, almost $300-million in cash left over from the good times and $26-million in a fire suppression fund. The Governor will propose a "hold the line budget" to the 2011 Legislature that will limit new programs and expenditures, including wage increases for state workers.

The Legislative Fiscal Division offers a more troubling prophesy. Forecasts released last week indicate that the general fund will pile up a $400-million deficit over the next two years. These projections are based on the bleak view that the economic recovery will be long and slow, particularly here in Montana. In this situation, a 10% reduction in all general fund spending categories would be required to balance the state budget.

At this time, the most optimistic revenue projections will do nothing more than cover a flat-line, subsistence budget. It is obvious that the 2011 Legislature will focus on public finance issues, and the challenge for cities and towns next winter is to assure that their interests are effectively promoted and fairly considered. This is the nice way of saying that cities and towns will fight like fiends to maintain state transfer payments and kill any bills that increase the cost of local government operations.

Entitlement Program

The Entitlement Program was approved by the 2001 Legislature as part of the notorious "Big Bill". Under this measure cities, towns and counties agreed to relinquish claim to gambling, motor vehicle, financial institutions and wine, beer and liquor taxes in return for guaranteed payments from the state treasury. These payments are adjusted each year in accordance with a formula that considers increases in per capita income and gross state product over the previous four years.

In the time since the program was adopted, distributions to cities and towns have increased from $41.8-million to $55.1-million in FY-2010. **The entitlement formula will increase payments to municipal governments by 5.14 percent up to almost $58-million for FY2011.** This is a significant increase during a difficult business cycle, and it occurs because of strong economic performance at the beginning of the four-year period on which the percentages are calculated.

Cities can figure out their quarterly entitlement payments by adding 5.14 percent to the amounts received in September, December, March and June of the current fiscal year.

Local governments are allowed to increase property tax collections by one-half the rate of inflation averaged over the previous three years. **The allowable adjustment for 2011 is 1.412%.**

If state revenue collections fall further behind projections, and there is a deep budget hole when the Legislature comes to town next January, it may be necessary for cities to tenaciously defend the Entitlement Program. There is a fist full of strong arguments to support this position:

1. Entitlement payments are made through a statutory appropriation that is not included in the general fund.
2. The state has collected more under this law than it has disbursed.
3. The law requires a 60% majority of both Houses to reduce entitlement payments.
4. Most of the Senators and Representatives who worked to promote and develop this program have been benched by term limits, but there is an understating that any reduction in payments will likely lead to higher local mill levies.
5. The growth rates will decrease in the coming biennium because two years of marginal economic growth will be worked into the formula.
6. Finally, this is Montana and a commitment still has some real value.

An interim legislative committee is also considering a bill draft that would simplify some of the provisions of the Entitlement Program. Most of the changes are being offered in the interests of cleanliness and clarity. There is, however, a policy issue that must be considered. The original bill had a two-part formula that considered population and the amount contributed in the base year by each city or town. The proposed change in the committee bill would adjust the payments from one year to the next by applying the growth rate and adjusting the population factor. This change would favor those cities with higher population growth.

Revenue Alternatives

In 2005, a bill that would have authorized a local option tourist tax passed the Senate by a 30-20 margin, but was bottled up on a tie vote in a House committee. This was the political zenith for the idea that Montana voters should have the right to decide local tax policy. Since that time, support has deteriorated and a new version of the same idea might be nothing more than an annoyance or curiosity in 2011.

Cities and towns have argued for many years that a portion of the state bed tax should be returned to the places where it is collected to help pay for the services that tourists use every day they are in Montana. This argument is fair and logical, but it has no practical meaning if the Legislature is working to salvage the general fund budget from an economic shipwreck.

The League has researched some of the revenue options that are being used in other states to balance budgets decimated by the recession. The most common solution is an increase in sales tax rates, which is not now and probably never will be the answer in Montana. Some states have increased tax rates and fees on utility services. Again, this is a difficult proposition in Montana where there would not appear to be much interest in new taxes or fees that would be collected through residential and commercial utility bills.

Reappraisal

The state is required by law to conduct periodic reappraisals of residential and commercial property. The most recent revaluation covered the six-year period from 2003 through 2008. It indicated that the value of residential property had increased an average of 55% across the state. At the same time, commercial values rose an average of 34%.

The 2009 Legislature passed House Bill 658 to mitigate the impacts of reappraisal. The intent of this measure was to pull off the great balancing act of any political circus -- "revenue neutrality". The new values will be phased in over six years, tax rates will be cut back and exemptions will be boosted. In addition, if values increase more than the statewide average in an area, local governments are required to ratchet down millage to stay within the parsimonious limit in 15-10-420. If values decrease, cities and counties can add mills to raise collections up to the tax ceiling.

The formula in HB-658 works well with local government levies. It falls to pieces when applied to statewide levies, because the mills cannot be adjusted to account for variations above or below the median value increases across the state.

This bill was the subject of constant discussion, debate and disagreement for most of the 90 days of the 2009 Legislature. It probably suggested more questions than it answered, and it may be the root cause of the high level of property tax protests that have been filed in the last year.

The Department of Revenue recently issued the results of a sales assessment ratio study that verified the accuracy of the 2008 reappraisal. This report along with the passage of time may diminish the volume of appeals and free up tax revenues being held in escrow accounts.

The 2010 Census and Legislative Redistricting

A lot of work has been done to encourage people to stand up and get counted during the 2010 National Census. The data that is collected is used to apportion federal and state revenues to local governments. It is also vital in grant and loan applications and many other functions of city and town government.

The census data is also used to set new boundaries for legislative districts across the state every 10 years. If the population estimates that have come out annually since the last census are an indication of the results of the final count, a very interesting trend will become apparent. In 2005, the Department of Commerce released a report that said Missoula was the only city that grew faster than the population of the unincorporated area of the county in which it was located. Now, the numbers tell a completely different story. From 2000 to 2008, Montana saw a population increase of almost 65,000 people. The number of those people living in cities and towns increased by 54,000 . Over the same period, the population of the unincorporated areas of the counties increased by about 11,000.

The population is also shifting to the West and into Billings. Most of the population growth, almost 95%, occurred in Flathead, Lake, Ravalli, Missoula, Lewis and Clark, Gallatin and Yellowstone Counties. Even in these areas, the population increased at a higher rate in cities than in the outlying areas of the counties.

If legislative redistricting is done right, there may be a whisper of hope that more members of the Legislature will begin to understand that cities and towns of all sizes and locations are the foundation of government in Montana.

Land Use

The Legislature is the theatre where the war between private property rights and public purposes is waged every two years. The battles in this war are fought along a skirmish line that ranges from annexation through impact fees, planning and subdivision regulations, all the way to zoning. In each session of the Legislature, local governments defend their authority to manage land use and promote logical community development. This seems to be an endless battle, because the Legislature has become the next level of authority for every land use issue that cannot be settled back home at city hall or the court house.

Water Quality

Senate Bill 95, as approved by the 2009 Legislature, allows the Department of Environmental Quality to set "temporary" nutrient standards for public and industrial wastewater systems over the next 20 years.

The law recognizes that cities and towns across Montana, and the people served by their utilities, cannot afford costly sewage treatment improvements that are not justified by economics, technology, or common sense. The law, if it works as intended, will give the state time to develop a regulatory plan that reduces nutrients in Montana waters through technology that actually works at a cost that is reasonably affordable. These objectives cannot be reached until all sources of nitrogen, phosphorous and other nutrients are regulated and the costs of compliance fairly apportioned.

A member of the League's Water Quality Committee has suggested amendments to the 2009 law that would set up load trading policies. This approach would assign credits to cities that extend sanitary sewer service to outlying areas, which would reduce the use of septic systems. Load trading would be an important step in the right direction. It would move the focus to reducing nutrient loads in an entire basin instead of concentrating on cities and industries that are the only nutrient sources currently regulated. These are simple questions of balance and arithmetic. Nutrient loads come from many sources and every property owner, business, industry and public agency that contributes to the problem must pay a proportional share of the costs of compliance.

Medical Marijuana

In 2004, Montana voters passed an initiative that legalized the use of marijuana for medical purposes. This act did not draw much attention until last year when the U.S. government backed away from the enforcement of a federal law that banned the use of medical marijuana. Now, more than 15,000 people in Montana have acquired or are applying for green cards that allow them to purchase marijuana.

Purveyors of medical marijuana have buried cities across the state with applications for business licenses and other permits to allow them to set up businesses to grow and dispense the drug. Some cities have refused to issue licenses because the sale of marijuana is not legal under federal law. Other cities have imposed moratoriums on new marijuana businesses to allow time to study all aspects of a complicated and emotional issue. Bozeman is holding community forums to determine how its citizens want to handle this issue.

At a forum last month in Helena, representatives of state agencies, local law enforcement, the medical profession and marijuana advocacy groups agreed that the drug must be regulated. The challenge will be to adopt rules that allow the use of marijuana for legitimate medical reasons under effectively controlled circumstances. There will be numerous bills in the 2009 Legislature to deal with this issue.

Public Pension and Employee Benefits

Actuarial reports indicate that most of the state's public employee pension programs do not have the money that will be needed to cover long-term obligations. Investment earnings fell sharply in the previous two years, and while equity markets have recovered, the bounce was not sufficient to change the direction of the adverse trend lines. As recently as 2007, the Legislature pumped more the $100 million from the general fund into the pension accounts. This option is off the table in a tough budget year, but there are possibilities of limited value the Legislature may consider:

1. Increases in employer contributions, which would include local governments and state agencies and require additional appropriations.
2. Reductions in benefits for newly hired employees, because payments to those already in the system are constitutionally protected.
3. A quiet prayer, a lighted candle and the hope that the equity market will produce the returns necessary to stabilize the systems.

Paid firefighters may arrange for the introduction of a bill that would include overtime, holidays and even payments for unused sick leave in the calculation of pension benefits. A similar bill was tabled in a House committee last year.

There also may be an attempt to include heart disease, cancer and other chronic medical conditions under the Occupational Disease Act. This change would likely lead to significant increases in workers' compensation.

Health Care

Most of the major provisions of the federal health care law will not go into effect until 2014. There are changes, like maintaining family coverage for dependents up to the age of 26, that could cause a slight increase in premiums for existing insurance plans, Last month, the MMIA Board of Directors voted to increase health insurance premiums by 5% for the coming fiscal year. This program has worked to stabilize and keep the lid on health insurance costs for more than 60 cities across the state.

In the coming months, MMIA will begin collecting claims data, under strict confidentiality protection, that will allow it to more effectively monitor and manage health care expenditures. Cost containment is the factor that will determine the success or failure of health care reform. Unfortunately, this responsibility now belongs to state and local governments.

Figure 3

General Fund Revenue Monitoring Report

Revenue Source	Actual Fiscal 2009	HJ2 Estimate Fiscal 2010	Through 4/30/09	Through 4/28/10	Difference	% Change	HJ2 Estimate % Change
GF0100 Drivers License Fee	3,478,285	3,920,000	2,158,094.45	3,282,814.06	1,124,719.61	52.12%	12.70%
GF0200 Insurance Tax	50,038,468	58,762,000	25,239,536.65	26,503,049 01	1,263,512 36	5.01%	17 43%
GF0300 Investment Licenses	6,461,446	6,210,000	5,681,092 21	5,557,298 11	(123,794 10)	-2 18%	-3 89%
GF0400 Vehicle License Fee	89,334,878	92,247,000	67,899,315 82	64,263,927 23	(3,635,388 59)	-5.35%	3 26%
GF0500 Vehicle Registration Fee	15,345,099	17,970,000	11,953,479 41	9,483,944 32	(2,469,535 09)	-20.66%	17 11%
GF0600 Nursing Facilities Fee	5,468,766	5,213,000	3,402,017.16	3,373,712.17	(28,304.99)	-0.83%	-4.68%
GF0700 Beer Tax	3,114,729	3,218,000	2,291,405.41	2,257,499 69	(33,905 72)	-1.48%	3 32%
GF0800 Cigarette Tax	34,320,412	32,007,000	27,004,758 02	25,068,051.43	(1,936,706 59)	-7.17%	-6 74%
GF0900 Coal Severance Tax	13,028,228	10,846,000	7,397,132 19	6,078,100 86	(1,319,031 33)	-17.83%	-16.75%
GF1000 Corporation Tax	166,354,514	115,638,000	125,922,275 53	58,383,904 48	(67,538,371 05)	-53.63%	-30.49%
GF1100 Electrical Energy Tax	4,824,659	4,717,000	3,155,206.56	2,245,761.84	(909,444.72)	-28.82%	-2.23%
GF1150 Wholesale Energy Trans Tax	3,864,771	3,931,000	2,721,366 86	1,791,514 48	(929,852 38)	-34.17%	1.71%
GF1200 Railroad Car Tax	2,099,454	2,295,000	1,574,971 58	1,977,856 00	402,884 42	25 58%	9.31%
GF1300 Individual Income Tax	815,138,193	840,263,000	683,186,478 27	550,113,738 63	(133,072,739 64)	-19.48%	3 08%
GF1400 Inheritance Tax	217,097	29,000	174,859 67	70,564 95	(104,294 72)	-59 64%	-86 64%
GF1500 Metal Mines Tax	5,992,923	3,248,000	2,818,391.21	3,456,374 78	637,983.57	22.64%	-45 80%
GF1700 Oil Severance Tax	100,490,971	66,930,000	65,055,130 93	45,506,077 61	(19,549,053 32)	-30 05%	-33 40%
GF1800 Public Contractor's Tax	5,929,999	4,322,000	4,504,098 41	5,882,490 50	1,378,392 09	30 60%	-27 12%
GF1850 Rental Car Sales Tax	2,904,340	3,182,000	2,022,461 55	1,837,057 28	(185,404.27)	-9.17%	9 56%
GFxxxx Property Tax	217,042,057	228,853,000	129,862,136 52	132,205,997 44	2,343,860 92	1.80%	5 44%
GF2150 Lodging Facilities Sales Tax	12,477,461	13,376,000	8,688,129.37	7,815,566.17	(872,563.20)	-10.04%	7.20%
GF2200 Telephone Tax	-	-	-	-	-		
GF2250 Retail Telecom Excise Tax	22,250,383	21,672,000	11,588,991 09	12,954,942 42	1,365,951 33	11 79%	-2 60%
GF2300 Tobacco Tax	4,990,497	4,738,000	3,637,171 31	4,013,444 93	376,273 62	10 35%	-5 06%
GF2400 Video Gaming Tax	62,458,106	69,003,000	47,132,880 43	39,788,189 96	(7,344,690 47)	-15.58%	10.48%
GF2500 Wine Tax	1,936,052	2,043,000	1,468,681.90	1,456,788.60	(11,893.30)	-0.81%	5.52%
GF2600 Institution Reimbursements	14,100,804	16,047,000	12,377,982.80	12,830,446.10	452,463 30	3.66%	13 80%
GF2650 Highway Patrol Fines	4,179,882	4,055,000	3,168,602 88	3,459,735 06	291,132 18	9 19%	-2 99%
GF2700 TCA Interest Earnings	15,506,889	7,967,000	13,618,235 70	2,076,062 15	(11,542,173 55)	-84.76%	-48 62%
GF2900 Liquor Excise Tax	12,650,902	16,581,000	11,533,189 17	8,673,481 42	(2,859,707 75)	-24.80%	31.07%
GF3000 Liquor Profits	7,250,000	7,039,000	-	-	-		-2.91%
GF3100 Coal Trust Interest Earnings	26,958,378	28,574,000	17,866,454.41	18,127,510 76	261,056 35	1.46%	5 99%
GF3300 Lottery Profits	10,136,213	10,969,000	5,480,013.00	5,558,657.00	78,644 00	1.44%	8.22%
GF3450 Tobacco Settlement	4,127,609	4,007,000	4,127,609.08	3,468,623.20	(658,985 88)	-15.97%	-2.92%
GF3500 U S Mineral Leasing	31,573,364	27,796,000	23,053,757.59	17,293,517 71	(5,760,239.88)	-24.99%	-11 96%
GF3600 All Other Revenue	31,921,805	35,247,000	19,912,802.84	22,051,830.07	2,139,027.23	10.74%	10.42%
Grand Total	1,807,967,634	1,772,915,000	1,357,678,709 98	1,108,908,530 42	(248,770,179.56)	-18.32%	-1 94%

* Plus impacts of enacted legislation

TO: Kay Gray, Department of Administration

FROM: Vern Fogle, Economist

DATE: April 13, 2010

RE: Inflation Factor for Mill Levy Calculation in 15-10-420, MCA for **FY 2011**

I have calculated the inflation factor to be used in the mill levy calculation as prescribed by 15-10-420, MCA for FY 2011. Under that statute the Department of Revenue is required to

> "calculate one-half of the average rate of inflation for the prior 3 years by using the consumer price index, U.S. city average, all urban consumers, using the 1982-84 base of 100, as published by the bureau of labor statistics of the United States department of labor".

The rate of inflation for the three years prior to 2010 can be measured from December 2006 to December 2009. The U.S. City average CPI-U, not seasonally adjusted, was 201.8 for December 2006 and 215.949 for December 2009. These values can be found at

http://data.bls.gov.

The average annual inflation rate over this period is 2.2845%. That is, if you grow the value of **201.8** three times at 2.2845% each time, the result will be **215.949**.

1	201.800 x 1.022845 = 206.410
2	206.410 x 1.022845 = 211.126
3	211.126 x 1.022845 = 215.949

One-half of 2.2845% is 1.142%. **The value to use in the mill levy calculation for fiscal year 2010 is 1.142%.**

This is an increase from the 1.112% value used in the mill levy calculation for fiscal year 2010.

If you have any other questions please contact me at 444-1821.

Cc: Harold Blattie, MACo
Alec Hansen, MLCT
Cynthia Moore, DOR PAD
Ralph Franklin, OBPP
Ed Caplis, TPR
Alan Peura, DOR

Table 3

Computation of Growth Rates

Growth Component		FY 2010		FY 2011	
Montana Gross State Product		(3)(a)(i)(B)	7.950%	(3)(a)(i)(A)	7.629%
Montana Personal Income		(3)(a)(ii)(B)	6.498%	(3)(a)(ii)(A)	7.049%
		Total	14.448%	Total	14.678%
		Avg	7.224%	Avg	7.339%
Apply Jurisdiction Factors to Avg					
Jurisdiction	Factor				
Counties	54%		3.900%		3.960%
Consolidated	62%		4.480%		4.550%
Cities/Towns	70%		5.060%		5.140%

Table 4

Entitlement Share Payment Growth Percentages

	Growth Percentages		
Jurisdiction	2009 Biennium	Actual FY2010	Actual FY2011
Counties	3.285%	3.900%	3.960%
Consolidated	3.770%	4.480%	4.550%
Cities/Towns	4.255%	5.060%	5.140%

Counties	3.285%	average of fy08 and fy09
Consolidated	3.770%	average of fy08 and fy09
Cities/Towns	4.255%	average of fy08 and fy09

C:\Users\Alec\AppData\Local\Microsoft\Windows\Temporary Internet Files\Content.Outlook\6G0SM2MF\[Entitlement Share Pool Amounts FY10 FY11 (2).xls]table 3 and 4

Table 1
Changes In Value Due To Reappraisal

Type of Property	Full Market Value: 2003 Reappraisal	Full Market Value: 2009 Reappraisal	Full Market Value: Difference in Value	Full Market Value: % Change in Value
Class 3 Agricultural Land	4,383,310,771	5,642,225,118	1,258,914,347	29%
Class 4 Residential	50,886,118,523	79,127,262,478	28,241,143,955	55%
Class 4 Commercial	11,463,907,618	15,368,908,254	3,905,000,636	34%
Class 10 Forest Land	1,975,410,723	2,997,054,968	1,021,644,245	52%

Economic News Release

Consumer Price Index Summary

Transmission of material in this release is embargoed until
8:30 a.m. (EDT) Wednesday, April 14, 2010

Technical information: (202) 691-7000 Reed.Steve@bls.gov
www.bls.gov/cpi
Media Contact: (202) 691-5902 PressOffice@bls.gov

Consumer Price Index - March 2010

On a seasonally adjusted basis, the Consumer Price Index for All Urban Consumers (CPI-U) increased 0.1 percent in March, the U.S. Bureau of Labor Statistics reported today. Over the last 12 months, the index increased 2.3 percent before seasonal adjustment.

The seasonally adjusted increase in the all items index was mostly due to an increase in the fresh fruits and vegetables index, which rose 4.6 percent in March and accounted for over 60 percent of the all items increase. Other food at home indexes were mixed and the index for food away from home was unchanged.

The index for energy and for all items less food and energy were both unchanged in March. Within energy, an increase in the electricity index was offset by declines in the indexes for gasoline and natural gas. Within all items less food and energy, the indexes for medical care, new vehicles, and used cars and trucks posted increases, while the indexes for shelter, household furnishings and operations, and apparel declined.

Table A. Percent changes in CPI for All Urban Consumers (CPI-U): U.S. city average

	Seasonally adjusted changes from preceding month							Un-adjusted 12-mos. ended Mar. 2010
	Sep. 2009	Oct. 2009	Nov. 2009	Dec. 2009	Jan. 2010	Feb. 2010	Mar. 2010	
All items..................	.2	.2	.2	.2	.2	.0	.1	2.3
Food......................	-.1	.0	.1	.1	.2	.1	.2	.2
Food at home.............	-.3	.0	.0	.2	.4	.1	.5	-.7
Food away from home (1)..	.1	.1	.2	.1	.1	.1	.0	1.2
Energy....................	.6	.6	2.2	.8	2.8	-.5	.0	18.3
Energy commodities.......	1.1	.4	3.0	1.6	4.9	-1.3	-1.0	39.6
Gasoline (all types)....	.9	.3	2.7	2.3	4.4	-1.4	-.8	41.4
Fuel oil (1)...........	-.3	2.2	7.4	.0	6.1	-2.4	.7	27.2
Energy services..........	-.1	.8	1.1	-.3	.0	.5	1.4	-1.8
Electricity.............	.3	.8	1.2	-.2	-1.1	-.5	2.1	-.5
Utility (piped) gas service..............	-1.5	.7	.9	-.7	3.5	3.9	-.7	-5.5
All items less food and energy.................	.2	.2	.0	.1	-.1	.1	.0	1.1
Commodities less food and energy commodities....	.3	.4	.2	.1	.1	-.1	-.1	1.9
New vehicles............	.3	1.4	.5	-.2	-.5	.1	.1	3.0
Used cars and trucks....	1.7	3.1	1.9	2.2	1.5	.7	.5	16.3
Apparel.................	.2	-.3	-.3	.4	-.1	-.7	-.4	-.4
Medical care commodities (1)..................	.6	.2	.1	-.1	.7	.8	.4	3.7
Services less energy services.............	.1	.1	.0	.1	-.2	.1	.1	.8
Shelter.................	.0	.0	-.2	.0	-.5	.0	-.1	-.6
Transportation services	.7	.5	.5	.3	-.3	.4	.4	3.8
Medical care services...	.3	.2	.3	.2	.5	.4	.3	3.8

1 Not seasonally adjusted.