CHAPTER IV MUNICIPAL BUDGETING

by

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4.1 Municipal Budgeting

4.1 MUNICIPAL BUDGETING

4.101 Budget Defined

A municipal budget is a legally required plan of expenditures 7-6-4001, MCA, that is balanced by anticipated revenues during the government's fiscal year which, in Montana, runs from July 1 through June 30. The budget format and fund structure must conform to the requirements of the Montana Department of Administration's Budgeting, Accounting and Reporting System (BARS). The BARS Chart of Accounts is administered by the Local Government Services section of the Statewide Accounting Bureau. By law, the required annual municipal budget resolution must:

1. Be approved by the city/town council by the later of the first Thursday after the first Tuesday in September, or within 30 calendar days of receipt of the municipality's taxable value from the Department of Revenue;
2. Include a specific *appropriation of public funds* (the government's annual spending authority);
3. Set the annual *property tax mill levy* that will be borne by the owners of all taxable property within the municipal jurisdiction.

Beyond its legal, financial management and accounting functions, a municipal budget also serves as historic documentation of the civic problems that confront a community and the city or town government's plan to address those problems. Moreover, the budget probably reveals the governing body's political compromises and agreed upon-goals for the future. Hence, the final adoption of the annual budget marks the culmination of the council's *policy-making process* and the beginning of the executive branch's *resource management process.*

4.102 Annual Budget Required

An annual budget is required for all fund entities, including those funds supported by property taxes (e.g. the general fund) and those funds supported by non-tax revenues (fees) such as the water fund and the wastewater fund. (See Section 4.106 for a more detailed description of governmental fund accounting and the various types and purposes of municipal funds.)

4.103 Budgeting Limitations

There are a number of provisions included in the Local Government Budget Act 7-6-4001, MCA ,that impose significant limitations upon municipal officials. Among the more significant of these budgeting limitations are:

- A municipal official may not make an expenditure of public funds or incur an obligation to expend public funds *in excess of the total appropriation approved by the governing body.* An official who violates this limitation is *personally liable* for the amount of the expenditure, 7-6- 4005, MCA.
- The final budget must be balanced so that planned appropriations do not exceed the available resources and anticipated revenues during the fiscal year, 7-6-4030, MCA.

4.104 Budgeting Terminology

Appropriation – an authorization by the governing body enabling local government departments to make expenditures or to incur financial obligations for a specific public purpose. The expenditure authorization is limited to the fiscal year of the approved budget *and may not be exceeded except by lawful amendment of the budget by the governing body*.

Budget – the plan of expenditures and revenues approved and authorized by the annual budget resolution of the governing body to meet the essential public safety, public health and public well-being needs of the city/town or county during a specific fiscal year. A "line item budget" is formatted by object code to document the source of revenues as well as the departmental origin and purpose of expenditures. A "program/performance budget" includes the necessary accounting detail but is expanded to provide documentation of the funded program objectives and the associated performance measures that will be used to evaluate the outcomes and public benefits to be derived from the budgeted expenditures.

Capital Improvement Program (CIP) – a method provided by law 7-6-616, MCA for funding the replacement, improvement or acquisition of local government property, facilities and equipment that costs in excess of $5,000 and has a life expectancy of five years or more.

Enterprise Fund – a governmental fund type used to account for the revenues and expenses (including depreciation) of proprietary services provided by a local government on a "fee for service" basis, similar to private business enterprises, rather than on a tax-supported basis. Water, wastewater (sewer) and solid waste (garbage) and ambulance services are typical examples of municipal enterprise activities.

Fiscal Year – a twelve-month governmental accounting period limiting the authorization of expenditures and enabling annual reconciliation of the government's financial position. The fiscal year for state and local governments in Montana is July 1 to June 30.

Unrestricted Fund Balance and Net Position – for governmental funds, the fiscal year end cash, less outstanding liabilities (Cash Available) that is not restricted by an outside third party. For enterprise funds, the unrestricted fund equity is designated the Unrestricted Net Position. Restrictions must be made by a third-party outside of the government. The government itself can only commit fund balance or net position. This is an important trend indicator of the financial soundness of a governmental fund or unit of government.

G.A.A.P. – "Generally Accepted Accounting Principles" recognized by the accounting profession and by the Government Accounting Standards Board (GASB).

General Fund – a fund used to account for the ordinary operations of a local government which are financed by property taxes and other non-tax, general revenues and not accounted for in another governmental fund.

Property Tax Mill – one thousandth of the total property certified taxable valuation of a taxing jurisdiction. The mill is used to apportion the costs of providing government services in proportion to the taxable value of property owned by the taxpayer. Thus, if the total *taxable valuation* of a city is $2,000,000, a one mill levy would yield $2,000 in property tax revenue ($2,000,000/1,000). By the same token, if a residence has a *taxable* value of $5,000, a one mill levy on the property would yield $5 in property tax revenue. If the mill levy required to balance the city/town budget is 100 mills, the municipal property tax on that same residence would be 100 X $5, or $500 which would be *added* to the county, school and state mill levies.

Certified Taxable Valuation – the portion (percentage) of the "appraised value" of any property that is subject to a property tax mill levy. Both the "appraised value or market value" and the resulting "certified taxable value" are determined by periodic, appraisals conducted by the Montana Department of Revenue applying a "tax rate" enacted by the legislature and furnished to all units of local government as annual, certified "taxable values" lying within the local government's jurisdiction. The taxable value is the basis for the local government's mill value which, as noted above, is the taxable value of the jurisdiction divided by 1,000.

4.105 The Budget Process

A basic grasp of *governmental fund accounting* is the first step in making sense of the municipal government's budget and the budgeting process.

Governmental Fund Accounting

The Montana Budgetary, Accounting and Reporting System (BARS) implements *governmental fund accounting* for local governments in conformance with *generally accepted accounting practices, or GAAP*. (See Montana Code Annotated Title 7, Chapter 6, Part 40 for the Local Government Budget Act.)

Unlike private business, a unit of local government must be able to demonstrate that *an expenditure of public funds was for the purpose intended by the law* that enabled the government to collect its revenue from taxpayers and rate payers. Also, the government must be able to document that *the expenditure was within the limits of the lawful spending authority (appropriation)* that must have been approved annually by the governing body. For example, a municipal government must be able to show that property tax dollars derived from a mill levy for the library were spent only for the library and no other purpose and that the annual expenditures for the library did not exceed the municipal appropriation for the library, which can only be made by the city or town council. Similarly, a municipal government must operate its water and wastewater systems on the *fee for services* received from its *rate paying* customers and it should do so without relying upon its *general fund* tax dollars.

Each stream of revenue and the associated expenditures must be accounted for within a specific governmental fund. In Montana municipal government, there are some required governmental funds, always the property tax supported *general fund*, if applicable, the *enterprise funds* used to account for the rate-based utilities (such as water and wastewater), and perhaps a bond debt service fund. *Each of these different funds requires its own annual budget*. In Montana, all of these budgets must be approved and adopted by the later of the first Thursday after the first Tuesday in September, or within 30 calendar days of receipt of the municipality's taxable value from the Department of Revenue, even though the state and local fiscal year commences on July 1.

The Budget Structure

A municipal government's finances revolve around four basic questions:

1. *How much money do we have to start the budget year? (beginning cash available)*
2. *How much money do we expect to receive during the budget year? (revenue estimates)*
3. *How much money do we expect to spend during the budget year? (appropriations)*
4. *How much money do we expect will be left at the end of the budget year? (anticipated ending cash available)*

These four questions should enable a newly elected municipal official to grasp the "big picture" of governmental budgeting. However, the actual budgeting process and the structure of the Montana BARS budget are made somewhat more complicated by law, presumably for the purpose of standardized preparation and reporting, thereby enabling review and oversight by state government. Moreover, few municipal clerks (the individuals who are most frequently responsible for assembling the budget) are certified public accountants and, therefore, they need some standardized guidance in budget assembly and documentation. To these ends, state law specifies the structure and elements of the Department of Administration's BARS standardized budget format, briefly described here.

The annual operating budget *for each governmental fund* is comprised of the same basic elements, which commonly include:

1. Detailed listings of proposed expenditures by department and further categorized in terms of personnel costs, operations costs and capital costs. (See ATTACHMENT 4.1 at the end of this chapter for a model of the BARS tabulation of expenditures);
2. A comparison of proposed expenditures with present year actual expenditures;
3. A listing of anticipated revenues by source;
4. A comparison of anticipated revenues with present year actual revenues; and
5. The Tax Levy Requirements Schedule summarizing the proposed spending, the required financial resources and the consequent property tax impacts, if any, for each governmental fund. (See Attachment 4.2 at the end of this chapter for a model of the BARS *Tax Levy Requirements Schedule*, which is a particularly useful document in summarizing the entire budget.)

Each of these five components of a local government budget is required by law and serves a specific accounting or management purpose and each reveals a different aspect of the municipal government's financial future. For example, the mayor of a small town may be most interested in the detailed listing and comparison of his departmental staffing and expenditures, while a prudent municipal council member may be focused on any changes in the proposed property tax mill levy, or the finance officer of a large city may be eager to track any downward trend in the government's year-end "fund balances".

Learning what questions to ask of a local government's budget and where to find the answers in the budget is the first and perhaps most important step in understanding the financial health of that government. Familiarity with this basic structure of a municipal government's budget is the key to understanding the capacity of a particular government to deal with the financial challenges it will face in its immediate future.

4.106 The Budget Cycle

Perhaps because the municipal budget is usually developed in May and June for final approval by early September, there is an understandable tendency to think of the budget primarily as a governmental "rite of spring". In fact, the four stages of the annual budget cycle are (or at least should be) continuous throughout the year. Each of these four stages in the budget process is described next.

1. ***Data Collection and Assembly***

This is usually thought of as the first step in producing the annual budget, even though it might also be usefully characterized as the continuation of the preceding year's budget. In either case, the primary activity involved at this stage is gathering of factual data and estimates *concerning proposed expenditures and anticipated revenues*. Typically, the heads of the operating departments (such as a city police department) are asked to provide their best estimates of the department's resource needs and any anticipated revenues for the coming fiscal year. These departmental estimates are collected by the organization's budget or finance officer who is most often the municipal clerk-treasurer. The budge officer then combines the departmental estimates with other financial data, such as anticipated tax revenues and carry-over fund balances from the preceding fiscal year, to assemble a working draft budget. The draft budget is then further developed, usually in direct consultation with the several department heads by the chief-executive officer, who may be the mayor or city manager. The end product of this stage of the budget cycle is a *preliminary annual operating budget* for each of the governmental funds 7-6-4020, MCA.

2. ***Legislative Review, Modification and Adoption***

The process of reviewing, modifying and finally adopting the annual budget is primarily the business of the governing body and it is inherently an exercise in local government politics. As one of America's earliest pioneers in the development of political theory would have observed, this step in the budget process is about answering the political question, *"Who gets how much of what?"* The ever-increasing needs of the several departments usually exceed available resources and must be disciplined by the reality of too few dollars. The imperative of the council or commission to assure the protection of the public's health and safety may be contradicted by a nagging concern about electoral consequences of constituent discomfort with any increase in taxes or fees. And, the urgent need for repairs to the water system or the roof on the city hall must be balanced with a prudent concern for incurring too much debt that will limit the financial flexibility of the government for years of future uncertainty.

After a series of internal meetings with department heads, followed by the required public hearing (which may be seldom attended by the public), the municipal government's annual operating budgets, along with appropriations and tax levies, will be adopted by majority vote of the governing body by the later of the first Thursday after the first Tuesday in September, or within 30 calendar days of receipt of the municipality's taxable value from the Department of Revenue.

3. ***Implementation***

Following commission or council approval, the departments of the executive branch have their *spending authority* for the new fiscal year. They may now set about managing available financial resources to accomplish plans of work. They must be mindful that it is *unlawful for them or any official in the government to authorize an expenditure of public funds in excess of the department appropriation* made by the governing body in the annual budget. However, should the need arise to augment a departmental budget, the governing body is free to do so by means of a formal *budget amendment*, which, like the original budget itself, requires a public hearing, and the affirmative vote of a majority of the governing body, 7-6-4031, MCA.

4. ***Monitoring***

Too often the budget/finance officer or clerk-treasurer is the only person in local government who seems to remember that a budget is based almost entirely upon *estimates of revenues and expenditures*. If a municipal government has based its planned expenditures on an estimate that it will receive $500,000 in non-tax revenue and, at the end of the year, discovers that it only received $400,000, there will be a challenge. Clearly, the remedy for overly optimistic estimates is regular *monitoring of revenues and expenditures*. The governing body and the executive must know whether projected revenues are on track during the year so that, if necessary, they can adjust actual expenditures downward, irrespective of the original appropriation, and do so in a timely manner. An additional precaution employed by prudent municipal officials is the maintenance of an ample cash reserve position (perhaps 25 percent) to buffer unexpected revenue shortfalls. For smaller units of local government, *quarterly monitoring of revenue and expenditure trends and reporting the trends to the council or commission is probably sufficient to head off financial surprises*. However, modern and increasingly inexpensive computer technology has made *monthly monitoring and reporting relatively easy and prudent*. The data collected in the process of monitoring execution of the annual budget will also provide the baseline data for next year's budget.

Additionally, the habit of periodically monitoring revenues and expenditures throughout the budget year will make it easier to construct longer term *financial trend indicators* so that local officials and the public can track changes in the financial health (structural balance) of the government. Financial trend monitoring can be as simple as graphing year---end fund balances (working capital balance for the enterprise funds), total revenues by source, total expenditures by fund type and perhaps the level of debt. The result is a snapshot of the financial condition of the government for a given year which will, in turn, provide an early warning of any significant changes from year to year that may need to be remedied. (See ATTACHMENT 4.3 at the end of this chapter for a simple model of a financial trend indicator.)

4.107 Alternative Budget Strategies

A well-tested improvement in the traditional *line item, incremental budget* strategy used by most of Montana's local governments is some version of a *program and performance budget* model. Additionally, the practice of including a long-term *capital improvement program (CIP)* as an integral part of the local government budgeting process is, by no means, a common practice of Montana's city and towns *even though it should be*. Both of these budgeting innovations are briefly described below.

Program and Performance Budgeting

The standard BARS budget format is typical of a governmental line item budget which is designed primarily as an accounting document rather than as a management tool. While the line item format details the personnel, operations and capital costs of each department and therefore helps account for and limit expenditures, it will not help the executive, the governing body or the attentive citizen-taxpayer understand what specific public service benefits will be provided and at what cost to the taxpayer. How many blocks of city streets will be graded and resurfaced for the $500,000 budget for the street department? How many kids will be taught to swim by the $50,000 property tax subsidy to the community swimming pool? Which expenditure will have the most beneficial impact on the community's public safety, a new fire engine OR four new police cruisers?

Performance budgeting and its precursor called "program budgeting" focus on the specific *programs and measurable outcomes* produced by governmental expenditures. For example, in preparing his annual departmental budget proposal the fire chief may be asked to estimate the number of fire inspections that will be made as a service of the fire department's fire *prevention program*, as distinct from the department's *firefighting program*. All of the budgeted costs of the fire prevention program can then be linked to the number of fire prevention inspections that are planned and subsequently performed as measurable service delivery *outcomes*. As a result, a rational basis for resource allocation, planning and improved service delivery can be achieved during the annual budgeting process. (See ATTACHMENT 4.4 at the end of this chapter for an example of a department's program budget with performance measures included.)

Capital Improvement Program (CIP)

Montana budget law provides that municipal governments may appropriate money to a *capital improvement fund* from any source, including funds that have been allocated in any year but have not been expended or encumbered by the end of the fiscal year, 7-6-616, MCA. The CIP must be formally adopted by resolution of the governing body and should include a prioritized schedule for replacement of *capital equipment or facilities with a minimum $5,000 value and a five-year life span*, as well as the estimated cost of each item. The purpose of the CIP is to identify long-term capital replacement priorities of the local government and to earmark some portion of the annual operating budget to fund the replacement or acquisition of capital items on a systematic basis, as approved by the governing body. It is, in essence, a way for the local government to "pay as it goes" by building the costs of capital replacement into the annual operating budget and, therefore, into the annual property tax mill levy or utility rate structure.

4.108 Roles and Responsibilities

The annual budget of a municipal government invites conflict between the legislative and executive branches. At stake, of course, is nothing less than whose "good ideas" will get funded? Which department will get a budget increase, and which will be cut? Which ward or commission district will get its streets or roads paved next year and which in five years? The local government's annual struggle to answer these and a thousand other locally relevant questions can be made economically rational, politically defensible and certainly less stressful by means of a clear understanding of the appropriate budgeting roles to be filled by the *governing body* and by the *executive*.

The Governing Body

The final budget must, in theory, be approved by the governing body before any public money can be spent. (See 7-6-4025, MCA for an important exception.) Therefore, a strong case can be made that the budget should, in substantial measure, reflect the *goals* and priorities of the governing council or commission, even if those goals are, in fact, developed by the executive branch for consideration and possible adoption by the governing body. Despite the self-evident virtue of this proposition, the practice in too many Montana municipalities is to treat the budget process as the mechanical, four-step sequence described above (data collection, legislative review, implementation and monitoring) and to do so without taking the time to formulate, articulate, and agree upon the *council or commission's specific goals and priorities for the coming budget year*. As a result, very scarce local resources could end up allocated to the municipal department with the best argument, to the neighborhood or citizen group with the most political clout, as a compromise between feuding council members or, worse, "pretty much the way we did it last year". Perhaps this mechanical approach to budgeting is the reason that so few municipal budgets are accompanied by a *budget message* explaining the public purposes (goals) to be accomplished by the local government with taxpayer dollars.

The mechanical budgeting style mentioned above will, in fact, produce a budget for the coming year. What it will not produce is orderly, predictable and affordable improvements in the well-being of the community. Nor will it generate much trust in the ability of the municipal government to address and solve community problems with the available resources, which is, after all, the reason to have a local government in the first place. In short, the members of the governing body simply must take the time to formulate, articulate and agree upon their fundamental goals and priorities *before* they start allocating public resources.

The Executive

To emphasize what ought to be the important role of the governing body in goal setting, there was but passing reference to the involvement of the executive branch in the process described above. In reality, it is more often true than not that the executive side of the municipal government will play a key role in defining the goals to be funded in the annual budget. Even in the commission-manager form of government wherein the boundary between the policy---making role of the commission and the policy implementation role of the manager is most clearly defined, the expertise, time and staff support available to the chief executive makes executive involvement virtually imperative in the commission's goal setting process. In the traditional commission-executive (mayor-council) form of municipal government, executive involvement in setting the goals of the legislative branch is unavoidable and is probably essential simply because the mayor usually serves as the council's presiding officer.

The typical dependence of the governing body on the executive branch for information, analyses, expert opinion, assessment of viability and resource availability when setting its budget goals is the friction point that can, and too often does, lead to conflict between the two branches of municipal government. For example, the role of the chief executive in virtually all forms of Montana's municipal government includes the legal responsibility and authority to prepare the budget for commission or council consideration and adoption. Moreover, virtually any chief- executive at any level of government (or in business for that matter), is very likely to have his or her own notion of the appropriate goals and priorities for the organization. It should come as no surprise that the executive's goals may or may not be in harmony with the goals of the governing body. Unless there is an opportunity for the governing body to formulate, discuss and then communicate its goals and priorities to the executive *before* they complete their version of the budget, the executive budget will reflect only the resource allocation recommendations of the chief executive. In this common situation, the members of the governing body are confronted with the typical dilemma of trying either to second guess and micro-manage the executive budget or, in order to avoid conflict, simply rubber-stamp the spending recommendations of the executive. The result is not likely to be either a good budget or an example of good government in action.

4.109 Establishing Budget Goals

Fortunately, the remedy to a fragmented budgeting process is remarkably simple. The governing body and the chief-executive must establish a routine that enables the governing body to undertake and complete an *annual goal-setting process*, however formal or informal the process may be, prior to the time the chief-executive must initiate the assembly of the executive budget. This essential and prerequisite step to effective budgeting may not always be free of conflict but it is likely that the conflict will focus on competing goals and priorities rather than on the micro-management details of budget implementation. In short and as stated at the outset, effective budgeting in local government requires that the members of the governing body simply must take the time to formulate, articulate and agree upon their fundamental goals and priorities before they approve the allocation of public resources. In doing so, they will find preparation of the budget and the annual budget message is much easier to accomplish and that the publics' trust in their government is more forthcoming.

The governing body's *goal setting process* can be as simple as a scheduled and noticed discussion of next year's top two or three goals of each member of the governing body, along with input from the mayor or manager or department heads. These relatively informal, intra- governmental discussions should, of course, be followed by an opportunity for public comment and input. Of utmost importance, however, is that some formalized process (voting) should be undertaken to find agreement by the commission or council on its collective goals and priorities for the coming year. The agreed upon and written goals and priorities, whether the result of informal discussions or of a more rigorous, facilitated and multi-year goal setting process, should then be provided to the executive branch early enough in the budget cycle (February or March) to serve as guidance to the mayor or manager as they go about assembling the preliminary budget for council approval.

4.110 Municipal Government Revenue Sources

In the most general terms, the two sources of revenue available to municipal governments are local *tax revenue* (primarily from local property tax) and *non-tax revenue*. In Montana, approximately half of municipal general fund expenditures are funded by locally-imposed property taxes. The balance of the annual city or town budget is typically funded by non-tax revenues. Each of these two sources of revenue for local government is described below.

1. Local Taxes

Locally-imposed *property tax* usually provides the largest single source of a municipal government's operating revenue. The actual amount of property tax revenue available to a particular local government depends upon two variables:

1. the *taxable value* of property located within the municipal jurisdiction; and
2. the amount of the municipal government's annual *mill levy*.

The average mill levy for municipal governments in FY 2017 was approximately 185 mills. However, the average mill value (taxable value divided by 1,000) for FY 2017 of 127 municipalities (not including the two consolidated governments) was $7,065 but varied from a low of $51 in Ismay, Montana's smallest town, to a high mill value of more than $183,817 in Billings, Montana's largest city. Needless to say, low property tax mill values usually equate to modest revenues available to fund local services.

Even though Montana's municipalities derive most of their operating revenues from property tax, local governments *are not free to impose whatever amount of property tax they may wish.* Montana law 15-10-420, MCA sets strict mill levy limits, some exceptions are allowed as permissive levies and others may only be exceeded by a favorable vote of the local electorate as provided in 15-10-425, MCA.

In addition to local property tax revenues, *resort taxes* provide an important supplementary source of local tax revenue for those resort communities that are enabled by law, 7-6-1501, MCA and their local voters to impose this 3 percent sales tax on the sale of luxury goods and resort related services. In at least one of these resort communities (West Yellowstone) the resort tax generates well in excess of $1 million per year to provide significant property tax relief and to help fund the town's aggressive capital improvements program to handle millions of visitors, as well as its yearly operations budget.

2. Non- Tax Revenue

In addition to the revenue derived from local taxation, municipal governments in Montana also have access to a number of additional revenue sources. These additional revenues are usually categorized as:

- *Fees for services*, primarily for municipal utilities such as water, wastewater and solid waste collection and disposal, but also for other fee supported services such as swimming pools.
- *Fines and forfeitures*, resulting primarily from traffic tickets, imposed by city courts or as forfeited bond by the offender.
- *Interest* earned on idle funds deposited in interest bearing, demand accounts and from direct investment in government securities, or in the state's pooled, Short Term Investment Program, commonly referred to as STIP.
- *Inter-governmental revenues* from the state and federal governments which include a wide range of payments directly to city governments such as federal and state grants, especially the federally-funded Community Development Block Grant (CDBG) program or Montana's Treasure Sate Endowment Program (TSEP) for infrastructure renewal. Additionally, a number of state revenue sharing programs (derived, for example, from state taxes on electronic gambling, gasoline, liquor and motor vehicles) have were consolidated into a single "entitlement distribution" to local government as a result of the enactment of HB 124 during the 2001 legislative session.

4.111 Municipal Debt

(See also Section 5.2 for a more detailed analysis of the types of debt)

The Montana constitution requires that the legislature enact laws limiting the indebtedness that may be incurred by municipal governments. Under state law, no debt may be incurred to balance a local government's annual operating budget which, as noted above, must balance proposed expenditures with cash reserves and anticipated revenues. However, state law does enable a local government to undertake *debt for long term capital improvements* such as streets and roads, government buildings and similar public facilities. (See 7-7-4101, MCA for a listing of the purposes for which a municipality may incur bonded indebtedness.) The amount of debt that may be incurred by a local government is, however, limited to a specified percentage of the jurisdiction's property tax valuation. *With some exceptions, a municipality may incur debt up to 2.5% percent of the assessed value of the taxable property within the city or town* (7-7-4201, MCA). *Municipal debt may be further increased for construction of water and sewer systems if the revenue from these systems is devoted to servicing that additional debt* (7-7-4202, MCA).

Municipal government debt for capital improvements is most often undertaken by issuing either *general obligation (G.O.) bonds or revenue bonds*. However, in Montana smaller scale capital projects may be funded by shorter-term loans available to local governments from the state revolving loan program known as INTERCAP, operated by the Board of Investments in the Montana Department of Commerce.

General Obligation Bonds

General obligation (G.O.) bonds are guaranteed by the *full faith and credit* of the local government issuing the bonds. By pledging the jurisdiction's full faith and credit, the government undertakes a legally binding pledge to repay the principal and the interest by relying upon its *taxing authority,* 7-7-4204 MCA. This obligation must therefore be ratified by an affirmative vote of the citizens before the bonds may be issued (7-7-4221, MCA). Due to the relative security of repayment of G.O. bond principal and interest and because the interest paid to the bond holders (lenders) *may be* exempt from state and federal taxes, lenders are usually willing to accept a lower rate of interest. As a result, the cost of the capital project will be somewhat less for the local government and for their taxpayers.

Revenue Bonds

Revenue bonds, on the other hand, *are not* guaranteed by the taxing authority of the local government entity issuing the bonds and they are, therefore, somewhat less secure than G.O. bonds. Even though the bond-holders interest earnings on revenue bonds *may* also be tax exempt, the bond market will usually demand somewhat higher interest rates to attract lenders. As suggested by their name, revenue bonds are backed only by the revenues from *fees* paid by the users of the capital facility, such as a municipal water or wastewater system or Special Improvement District (SID) for neighborhood improvements such as streets and sidewalks. Because revenue bonds *do not involve a pledge of the full faith and credit (taxing authority) of the municipal government, revenue bonds do not require voter approval,* 7-7-4104 and 7-7-4426, MCA.

To Borrow or Not to Borrow

Taking on local government debt by issuing either G.O. or revenue bonds involves a fairly complex process that always requires the legal competence of "bond counsel" and the marketing expertise of a brokerage firm that specializes in government bonds. Additionally, some municipal governments engage the services of a "financial advisor" to assist with the process and to represent the government's interests in negotiating a large bond issue with a brokerage firm. However, before deciding to proceed, even before actually engaging professional consultation, it is important that the governing body understand the implications of funding a capital project with long-term debt.

- ***Affordability*** -We refer here not just to a municipal government's ability to meet the monthly debt service payments while funding operations costs of the new project but, in doing so, to retain sufficient long-term liquidity to meet unforeseen, future demands on its revenues, including the effects of inflation on the costs of capital projects.

- Competing ***Capital Projects*** -Debt undertaken now reduces the government's debt funding capacity (legal limit) for the life of the bonds, which is often 20 years. What other capital projects at what cost (the opportunity costs) will be required by the local government during that period? Moreover, the community's *total debt burden must be considered*. A $20 million school bond to upgrade the local high school proposed on the ballot at the same time as a $10 million municipal bond proposal for a new city library are not likely to be well received by the taxpaying voters, no matter how much they may be inclined to support either one of the projects. Intergovernmental communication, coordination and cooperation among the governing bodies and executives are essential to avoid overloading the debt service capacity of the community.

- ***Who Pays for Capital Project?*** Long term debt financing of capital facilities means that those who will use the facility in the future, during the course of the indebtedness, will be those who pay the cost of the facility. It will be their *additional* tax dollars or fees paid to service the debt that will pay for the project. Alternatively, a capital depreciation fee built into the present tax or rate structure might be used to accumulate the capital necessary to replace the facility at the end of its useful life, thereby reducing the need for debt financing along with the attendant interest costs. In doing so, however, the present generation of users will be paying the capital costs of the facility they are now using and, by means of the capital depreciation fee included in their present tax or utility bill, they will also be paying the capital costs of a future facility they may not need nor even have access to. In short, debt financing means that those citizens who will be using the facility will pay for the facility, which is usually sound public policy. However, in this case, sound public policy also has a fairly steep price tag, called "interest," on the public debt.

- ***Grants and Debt*** -Finally, if a municipal government wishes to seek federal or state grant assistance in funding capital projects, such as Montana's Treasure State Endowment Program (TSEP), the local government itself must demonstrate a need for the capital facility and financial need. In this regard, financial need includes a consideration of the debt capacity of the local government, which is to say the ability and willingness of that government and its taxpayers (or rate payers) to participate in funding the project by assuming its reasonable and affordable share of the costs through debt financing. Most TSEP projects are, for example, funded by a package of state and federal grants, along with a substantial debt obligation undertaken by the municipal government.

4.112 Principal Statutes Related to municipal Budgeting

1. 7-6-4001, MCA Local Government Budget Act
2. 7-7-4201, MCA Bonded indebtedness
3. 7-7-4401, MCA Municipal Revenue Bonds
4.

Attachment 4.1
Model BARS Budget Expenditure Format

FUND Title: General Number: 1000		EXPENDITURES BY ACTIVITY AND OBJECT			City/Town/County of Municipal Model)_Fiscal Year:				
ACCOUNT NO.	**ACCOUNT**	**Previous Year F.T. E.**	**Previous Year Budget**	**Previous Year Actual**	**Auth orize**	**(100) Personnel Services**	**(200---800) Operating & Maintenance**	(600-699) Principal & Interest	**(900) Capital Outlay**	**Final Budget**
420000	Public Safety									
420100	Law Enforcement	10	300,000	275,000	11	275,000	50,000		25,000	350,000
420200	Detention and Correction									
420300	Probation and Parole									
420400	Fire Protection	.5	75,000	60,000	.5	15,000	50,000		10,000	75,000
420500	Protective Inspections	.5	25,000	20,000	.5	15,000	10,000			25,000
420600	Civil Defense									
420700	Other Emergency									
	Other (List)									
SUBTOTAL		**11**	**400,000**	**355,000**	**12**	**305,000**	**110,000**		**35,000**	**450,000**

NOTES:
1. Note increase of one Full Time Equivalent (F.T.E.) approved for next year's budget.
2. This is a volunteer fire department in a Third City with only a full-time, paid chief whose duties are split between two- budgeted functions.
3. The blank rows are for typical county functions.

Attachment 4.2
Tax Levy Requirements Schedule
Non-Voted Levies

City/Town/County of ***(Model of Municipal Form)***

Assessed Valuation 650,000,000

Tax Valuation 5,500,000

1 Mill Yields (10) **5,500**

Fiscal Year ______________

Page No ______________

*Column (3) Total Requirements must equal Column (8) Total Resources

Fund #	Fund Name	(1) Appropriation	(2) Budgeted Cash Reserve	(3)=(1)+(2) Total Requirements	(4) Cash Available (Less Current Liabilities)	(5) Non-Tax Revenues	(6)=(9)x(10) Property Tax Revenues	(7)=(5)+(6) Total Revenues	(8)=(4)+(7) Total Resources	(9)=(6)÷(10) Mill Levy	(11)=(4)-(1)+(7) Estimated Cash Balance
1000	General Fund	1,000,000	300,000	1,300,000	450,000	300,000	550,000	850,000	1,300,000	100.00	300,000
2250	Planning Board	10,000	3,000	13,000	2,000	1,000	10,000	11,000	13,000	1.82	3,000
2370	Insurance	75,000	0	75,000	1,000	4,000	70,000	74,000	75,000	12.73	0
3040	G.O. Bond (Pool)	26,000	5,000	31,000	1,000	0	30,000	30,000	31,000	5.45	5,000
7111	Police Retirement	50,000	500,000	550,000	500,000	25,000	25,000	50,000	550,000	4.55	500,000
	TOTAL	1,161,000	808,000	1,969,000	954,000	330,000	685,000	1,015,000	1,969,000	124.55	808,000

NOTES:

1. An amount up to 1/2 of the appropriation (column 1) may be budgeted as a Cash Reserve (column 2) to assure cash flow & liquidity between receipt of first and second half property tax revenues.
2. Non-tax revenues (column 5) include fines, fees, forfeitures, interest earnings and transfer payments from the state and federal governments.
3. Total Requirements (column 3) must equal Total Resources (column 8) to establish the “balanced budget” required by law.

Attachment 4.3
Model Program/ Performance Budget

FUND: *General*	DEPARTMENT: *Fire*	PROGRAM: *Protective Inspections*
FUND No: *420500*		

OBJECTIVES:

1. Conduct fire prevention inspections on 20% of all businesses in the city to achieve 100% during a five-year inspection cycle.
2. Conduct fire prevention inspections on 100% of all schools, churches and other public assembly buildings.
3. Conduct one 2-hour fire prevention talk and demonstration per year to each elementary school.
4. Conduct 2 fire drills per year in each school and in all other occupied city and county buildings.
5. Complete HAZMAT inspection training for 5 fire fighters.

ANNUAL PERFORMANCE MEASURES:

1. Percentage of business fire inspections completed?
2. Percentage of school/church fire inspections completed?
3. Number of fire prevention talks/demos to schools?
4. Number of fire drills conducted at schools and city/county buildings?
5. Number of fire fighters trained to do HAZMAT inspections?

Budget Category	FY 2011 F.T.E.	FY 2012 Appropriation	FY 2012 Actual	FY 2013 Department Proposal	FY 2013 Proposed F.T.E.	FY 2013 Approved F.T.E.	FY 2013 Appropriation	FY 2013 Mid---Year Amendments
Personnel	2	100,000	95,000	150,000	3	2	95,000	
Operations		50,000	45,000	50,000			50,000	
Capital		35,000	35,000	25,000				
Debt Service		15,000	15,000	15,000			15,000	
Inter-Fund Transfers								
Program Total	2	200,000	190,000	240,000	3	2	160,000	