



**Minnesota Budget Basics
Key Processes and Glossary of Terms**

MINNESOTA SENATE
OFFICE OF COUNSEL, RESEARCH, AND FISCAL ANALYSIS

December 2010

BUDGET PROCESS BACKGROUND

The Minnesota Constitution states that “no money shall be paid out of the state treasury of this State except in pursuance of an appropriation by law.” It also provides for the power to contract public debt, issue bonds, collect taxes, establishes certain funds, and dedicates certain revenue streams. It also requires a balanced biennial budget by prohibiting general fund borrowing across biennia. There is, however, little specific direction for the state budgeting process.

The major budget processes reflect statutory requirements that have been enacted into law over many years. Those process requirements apply primarily to the Executive branch and Minnesota Management and Budget, but the budget process is also guided by requirements upon other state agencies, as well as by tradition and other factors.

The Legislature further defines the budgetary process through the adoption rules and deadlines - some are adopted jointly by the House and Senate, while others are unique to each body.

Biennial Budget. Minnesota operates on a two-year (biennial) budget enacted in odd-year legislative sessions. Budget revisions and major capital investments tend to be the budgetary focus of even-year legislative sessions. Typically, the Legislature appropriates money for agencies and programs for each of the two fiscal years through the passage of omnibus appropriation bills.

State Funds. The state budget is managed through a variety of funds and accounts within those funds. The largest and most common fund is the general fund, which is required by the Minnesota Constitution to be balanced. The term “All Funds” refers to the 39 or so funds, including the general fund, from which money for the ongoing operations of state agencies and programs is appropriated. The State manages many other funds not used for the annual operations of the state, such as pension trust funds, revolving loan funds, and internal service funds.

Budget Background and Performance Information. As required by state statute, Minnesota Management and Budget develops budget forms and instructions, including requirements for

performance measures, to be used by state agencies when developing biennial budget information and budget recommendations. This information is used both by the Governor and the Legislature to develop an overall state budget. *See M.S. §§ 16A.10.*

Forecast of Revenue and Expenditures. In November and February of each year, the Commissioner of Minnesota Management and Budget is required to complete a state budget forecast, including consultation with relevant legislators and legislative staff. The budget forecast assumes the continuation of current law revenues and spending, with the resulting forecast projections often referred to as the “base” budget. *See M.S. §§ 16A.103.*

- **Consolidated Fund Statement** – a document produced by Minnesota Management and Budget that summarizes the resources, expenditures, reserves and balances for all of the state’s operating funds (All Funds), including the general fund.
- **General Fund Balance Analysis** – a document produced by Minnesota Management and Budget that summarizes the general fund budget including resources, expenditures, reserves, and balances with comparisons to the forecast and the previous biennium.

Executive Budget Recommendations. The Governor is required to present a three-part budget to the Legislature, including: a budget message, a detailed budget, and a detailed capital budget. The Governor’s budget recommendations must be submitted by the fourth Tuesday in January of odd-years, or the third Tuesday in February for a newly elected governor. *See M.S. §§ 16A.11.*

Budget Review and Adoption by the Legislature. During the legislative session in odd-numbered years (usually January through May), the House and Senate separately consider the Governor’s proposed budget. This is generally done by different legislative finance committees (or divisions) that oversee broad spending areas (K-12 education, Health & Human Services, Agriculture, Transportation, and so on) Committees typically schedule various hearings to publicly review the agency budget books containing budget background materials and the Governor’s recommendations.

Depending on legislative preferences and priorities, the House and Senate develop and adopt legislation providing for a state budget (note, some appropriations are part of permanent law, see definition of appropriations in Glossary). Typically, this is done by passing a tax bill and collection of omnibus appropriations bills, organized around legislative committee structure, that provide for the funding of state agencies and programs. The omnibus appropriation bills may also contain other policy and programs changes. Conference committees are created to work out any differences between the House and Senate versions of omnibus bills and the agreed upon versions of budget bills being repassed by both bodies and sent to the Governor for signature.

Budget Enactment. The Governor may veto whole omnibus bills or individual appropriations within the bills (line-item veto). When the Governor signs budget bills, or when the Legislature repasses budget bills after being vetoed by the Governor, they become law.

SENATE FISCAL ANALYSIS

Role of Senate Fiscal Analyst

Nonpartisan legislative fiscal staff assist the Legislature during the budget development process. In particular, fiscal staff are available to:

- assist Leadership, Committee Chairs, and Members to develop budget options (revenues or spending);
- analyze the state budget and fiscal policy impacts of budget alternatives;
- help draft budget-related legislation;
- develop budget spreadsheets (see below) and other tools to help meet budget targets and ensure enactment of a balanced state budget;
- present budget briefing materials and other overviews to new members, other legislative staff, and tax and budget committees upon request of the Chair;
- model education formula changes, tax law changes, and changes to selected other programs; and
- monitor the implementation of enacted budgets, alert Leadership, Chairs, and Members to budgetary issues, and undertake other analytical projects.

Senate Tracking Documents

Budget tracking spreadsheets developed and maintained by nonpartisan legislative fiscal staff are a key element of the budget process. During the budget decision-making process, they may be used by Leadership, Chairs, and committee caucuses to compare and contrast alternatives in terms of budget targets and resources available. Throughout the process, spreadsheets are a key document that Members and the public look to for identifying and communicating the budget impacts of the legislation being considered. Spreadsheets are typically revised and published at various intervals throughout the budget process, including: the introduction of the forecast and Governor's budget recommendations, the introduction of the committee Chair's recommendations, the adoption of a budget bill by a committee, the passage of a budget bill by the body (original and after any conference committee changes), and upon final enactment. Budget tracking documents for individual committees facilitate the overall tracking of the state budget in an effort to ensure the adoption of balanced state budget. Budget tracking documents for past and future sessions are available via the Senate website at: http://www.senate.mn/departments/office_bio.php?ls=&office_id=1007).

UNIQUE FISCAL ISSUES FOR BUDGET AREAS

While budget process requirements, the role of fiscal staff and spreadsheets, and most budget terms are applicable to all budget areas, each budget area may also have unique characteristics helpful in understanding the budget choices and decisions that will be made.

K-12 Education

- Appropriations are influenced by a variety of variables including: weighted pupil counts, differing property tax bases, teacher seniority, district population density, open-enrollments, school building age, anticipated voter behavior in referendum elections, charter school enrollments, poverty, and English language proficiency.
- Computer simulations are used to model all the variables in the school funding system. The models produce school district data runs, which are used to help inform Senators about the various public policy choices that can be made, such as formula allowance increases or reductions in equalizing factors, and display the effect of a given legislative proposal on each school district.
- Frequently considers fiscal policy choices that also have and impact on local property tax levies. As a result, education funding bills are typically also subject to tax committee jurisdiction.
- Must consider entitlement levels as distinct from appropriation levels. Appropriation levels often differ from entitlement levels, due to appropriation shifts enacted to achieve onetime budget savings. An appropriation shift is a change in the law that allows the state to recognize budget savings by delaying payment of a portion of an entitlement to a later fiscal year. Historically, shifts have been used to help balance a state general fund budget and then automatically restored over time as the economy recovers and to the extent revenues exceed forecasted spending. Typically, there are two types of education shifts, an aid payment shift and a property tax recognition shift.

Health and Human Services

- The state appropriations for agency operations and programs in this area typically involve significant interaction with federal funding. For example, because many administrative functions are jointly funded by the state and federal government, reducing state appropriations for program or administrative functions also results in a reduction in federal funds.
- Federal maintenance-of-effort requirements apply to various programs funded jointly by the state and federal government, such as health care programs and the Minnesota Family Investment program (MFIP).

Environment & Natural Resources

- The operating budgets for state agencies and programs in this budget area receive funding from a various dedicated funds in addition to the general fund. Some nongeneral funds are constitutionally established funds with a specific purpose, such as the Outdoor Heritage Fund and Permanent School Fund, while others statutorily dedicated.
- Considers recommendations from designated Commissions made up of citizens and Legislators that make appropriation recommendations for certain constitutional funds. One example is the Legislative – Citizens Commission on Minnesota Resources (LCCMR) that makes recommendations for the Environment and Natural Resources Trust Fund, which is supported by lottery proceeds.

Energy & Utilities

- While the budgets for these state agencies and programs are subject to appropriation by the Legislature, the cost of operating the agencies and programs is then assessed upon the regulated utilities with those assessments being deposited into the general fund.
- Some assessments are currently situated outside of the state accounting system (Renewable Development Fund) but have recently been the subject of specific legislative appropriation.

State Government

- This budget area appropriates funds to only a portion of the state’s agencies, boards and commissions. Appropriations for the staff and programs of the largest state agencies, such as the Departments of Human Services, Corrections, Natural Resources, others, are funded through other budget areas.
- The agencies funded through this budget area primarily include agencies whose responsibility it is to provide services to other state agencies in support of the overall operations of the State. As such, in addition to the direct appropriations made to the state government agencies, this budget area also oversees the rate-setting process used to determine charges assessed to other state agencies in support of these centralized functions, as well as the human resources and services delivered. For example, the Department of Administration (Admin) is responsible for managing state-owned property, and most state agencies pay rent to Admin, including for janitorial services and building maintenance. The Office of Technology (OET) provides other agencies with IT services supported by charges to those agencies, and Minnesota Management and Budget (MMB) manages the state accounting system and central accounting functions that is partially supported by charges to other agencies. Internal service funds are typically used to account for these interagency arrangements, with over 60 percent of Admin and 90 percent of OET funded through such arrangements.

ALPHABETICAL LISTING OF BUDGETING TERMS

Account — An account is a detailed record of money received into and paid out of the state treasury. When a law specifically requires the creation of an account, it is usually done to dedicate money to certain purposes. *See M.S. 3 16A.53; and 16A.69, subdivision 1.*

Allotment — An allotment is an amount, typically a portion, of an appropriation that is made available in the state accounting system for a defined use during a given period. State agencies develop spending plans for the amounts appropriated to them. *See M.S. 3 16A.011, subdivision 3; and 16A.14.*

Appropriation — An appropriation is an authorization in law to spend money from the state treasury. This is a budgetary control set at the legislative level. While the Governor can veto appropriations, appropriations cannot be created unless approved through the legislative process. The State Constitution expressly bans any spending from the state treasury without an appropriation. *See Minnesota Constitution, article XI, section 1, and M.S. 3 16A.011, subdivision 4.*

- **Direct Appropriation** – an authorization to spend a specified amount of money from a specific state fund, for a limited amount of time, usually one biennium. Omnibus spending bills are made up of mostly direct appropriations.
- **Statutory Appropriation** – (also sometimes called a standing appropriation), an authorization to expend money that is codified in state statute, is ongoing, and usually fluctuates from year to year. There are

two main types of statutory appropriations: open appropriations, and dedicated appropriations. *See M.S. 3 3.23.*

- **Open Appropriations** - an authorization, usually in statute, that makes available for spending an amount sufficient to fulfill a specified need with an “open-ended” amount. These are usually found within the general fund. Debt service and emergency firefighting for wildfires are examples of open appropriations.
- **Dedicated Appropriations** - an authorization, usually in statute, that makes a dedicated stream of revenue available for spending for a particular activity usually tied to that revenue. An example might be specific a fee-for-service used to cover the costs of providing the service.

Biennium — A biennium is a two-year period. In Minnesota, an operating budget is made for a fiscal biennium, which is made up of two fiscal years. For the State of Minnesota, a fiscal biennium begins on July 1 of each odd-numbered year and ends on June 30 of the next odd-numbered year. Fiscal biennia are referenced by their fiscal year names. For example, July 1, 2011, is the beginning of the 2012-2013 biennium. *See M.S. 3 16A.011, subdivision 6.*

Budgetary Balance (Balanced Budget) — The amount left on the bottom

line of the general fund (or another fund) after expenditures and reserve funds are subtracted from the beginning balance plus revenues. The balance could be positive or negative. The Minnesota Constitution requires budgetary balance by prohibiting borrowing beyond the end of a biennium to pay operating expenses for the biennium. Borrowing for cash flow purposes within the biennium is allowed. Revenues plus any balances carried forward from the previous biennium must be greater than or equal to expenditures. *See M.S.   16A.11 and Minnesota Constitution, article XI, section 6.*

Budget Base — The budget base is the common starting point in the construction of the next biennial budget. Minnesota Statute mandates that base budgets be set from current appropriation levels. Minnesota Statutes, section 16A.11, subdivision 3, defines the base as the amount that was appropriated for the second year of the current biennium, unless the appropriation was designated as onetime. This amount is to be carried forward into each year of the following biennium as a common starting point for developing the next budget. Where specific amounts are not appropriated in the second year, such as with dedicated expenditures, the base amount is set at the amount estimated to be expended.

Budget Reserve — The budget reserve is a special account established in the general fund (separate from the cash flow account) that serves as a savings account to be used to offset budget shortfalls during economic downturns. Reserve funds may be reduced, after consultation with the Legislative Advisory Commission, to the extent needed to balance expenditures with revenues. Like the cash flow account reserve, the amount in the budget reserve account is set in law. *See M.S.   16A.152*

Cancellations — Money appropriated but unspent and unencumbered at the end of a biennium or end of the period of time for which the appropriation was made. Because the appropriation—legal authority to expend such funds has expired—these amounts cancel back to the fund from which they were appropriated. The term may also used to refer to legislative action taken to terminate an appropriation earlier than previously enacted.

Capital Budget — The State of Minnesota typically adopts a budget for capital improvement projects (buildings and other physical improvements) each even-numbered year. The focus of the capital budget for the State of Minnesota is the issuance of state bonds (borrowing) and appropriation of the bond proceeds for acquisition of property, the construction of buildings and other physical improvements for the State, the State’s public higher education institutions, and sometimes for local units of government. The property (or improvements to it) must be owned by the State or a political subdivision of the State (usually a county or city) and have an estimated useful lifetime of at least ten years. Most appropriations for capital improvements must be spent within four years of enactment. *See Minnesota Constitution, article XI, sections 2-7 and M.S.   16A.641 and 16A.642.*

Cash Flow Account — A special account established in the general fund (separate from the budget reserve) that is intended to avoid short term borrowing by bridging gaps between revenue flows and expenditure flows during a biennium that result from differences in the timing of when revenues come in relative to when expenditures are made. Like the budget reserve account, the amount in the cash flow account is set in law. *See M.S.   16A.152, subdivision 1*

Enactment — Enactment is the completion of the legislative process referring to a bill becoming law after the bill has been passed by both the House and Senate and signed by the Governor, or repassed by the House and Senate after having been vetoed by the Governor. Note that the provisions in the law may become effective at a later date.

Fiscal Note — A fiscal note is a formal estimate of the fiscal effects that would be caused by the enactment of a bill. Fiscal note requests are initiated by legislative fiscal analysts on behalf of committee chairs or individual senators. Agencies that would be affected by a bill prepare estimates of cost changes (including costs that could be absorbed within existing budgets) and revenue changes the bill would cause. *See M.S. § 3.98*

Fiscal Year — A fiscal year is a 12-month period upon which the State’s budget is based, beginning on July 1 and ending on the following June 30. A fiscal year is numbered by the calendar year in which it ends. The federal fiscal year begins on October 1 and runs through the following September 30. *See M.S. §§ 16A.011, subdivision 14; 375.17; and 471.696.*

Forecasted Programs — Programs where funding levels are adjusted in the forecast based on changed caseloads, enrollments, or average costs; funding formulas for these programs are like entitlements and appropriations may either be open or for a fixed amount based on the forecast estimates available at the time appropriations were made—statute requires adjustments to bring the associated appropriations in line with the most recently forecast amounts.

Fund — A fund is a separate accounting entity in the state treasury that may or may not

contain a set of accounts. Funds may be created in the State Constitution, in state statute, or by the Commissioner of Finance in order to segregate different types of financial activity. A fund usually has language in law establishing it and identifying what money should be deposited into the fund and for what purposes money may be expended from the fund. State statute requires that no fund may carry a negative balance at the end of a state fiscal biennium. *See M.S. §§ 16A.53; 16A.575; and 16A.152, subdivision 4.*

General Fund — The general fund is the State’s main depository for taxes and general revenues. State statute directs that this fund is used “for the usual, ordinary, running, and incidental expenses of the state government and does not include moneys deposited in the treasury for a special or dedicated purpose.” The general fund is the State’s largest and most important fund because it has the most flexibility in its use. *See M.S. §§ 16A.54 and 16A.72.*

Omnibus Bill or Act — A collection of separate bills or appropriations in a single, large bill or act. Often there is a separate omnibus finance bill for each budget area and for taxes.

Revenue Estimate — A revenue estimate is an official fiscal estimate prepared by the Department of Revenue, forecasting the revenue gain or loss from enactment of proposed legislation, or estimating the spending impact of changes to property tax aid and credit programs. Revenue estimates do not identify the costs a state agency or local government may incur (or save) by implementing the proposed change. Revenue estimates are requested by legislative fiscal staff on behalf of the Tax Committee members and other Senators. Revenue

estimates are available on the Department of Revenue Web site at:

http://taxes.state.mn.us/legal_policy/pages/revenue_analysis_revenue_analyses.aspx

Shift; (Budget Shift or Education Shift) — A shift is a change in the law that allows the state to recognize revenues or spending in a different fiscal year without a change in the actual amount that will be collected or paid over time. Shifts have often been used to help balance a state budget and then been restored or unshifted during stronger economic times. The education aid payment shift and a property tax recognition shift are two common shifts.

Shift; Education Aid Payment Shift

— An aid payment shift is an adjustment in the percent of the E-12 formulas that are paid over a two-year period. Education aids are paid over two years. In any given year, most education appropriations are comprised of a percentage of education formulas that are in effect for the current year and a lagging "payment" for education formulas that were in effect for the prior year. An aid payment shift is a reduction to the percent of the formulas that are paid in the current year and an increase in the lagging payment. This reduction creates savings and pushes the cost of a portion of the education system from one fiscal year into the next.

Shift; Property Tax Recognition Shift

— A property tax recognition shift (PTRS) is a change in the law that requires a school district to adjust when it receives revenue derived from property taxes and a corresponding reduction in state aid. Property taxes in Minnesota are paid twice per year, in the month of May and October. The dates on which these payments fall are in two separate fiscal years. The May payments falls at the

end of the fiscal year and the October payment falls four months after the beginning of the subsequent fiscal year. Typically, school districts "recognize" all property tax revenue in the subsequent fiscal year. However, a PTRS occurs when the law is changed to require a district to "recognize" or count the property tax revenue from the May payment in the year in which it is paid. In that situation, schools count their property tax revenue earlier, which allows the state of Minnesota to reduce its state aid payments to schools by an identical amount. This creates onetime savings for the state general fund.

Structural Balance

— Structural balance is a measure of whether or not revenues are greater than or equal to expenditures in a future fiscal year or biennium. This measure differs from budgetary balance in that it does not take into account the beginning balance or reserves.

Tails (or Appropriation Tails)

— Appropriation tails are estimates of future revenue or spending amounts that will continue as base amounts in the next biennium, including estimates to continue current services and estimates of an appropriation, formula, or tax expenditure not scheduled to take effect in a future biennium. These amounts are also recognized in spending forecasts and are used in the determination of whether or not a fund has structural balance.

Targets

— Targets refer to limits on spending (and/or revenues) set during the legislative process to guide budget decision making by legislative committees, and to ensure that collective budget decisions meet expectations for budget balance, revenues, spending, and reserves.

Tax Expenditures — Tax expenditures are statutory provisions that provide tax preferences and reduce the amount of revenue that would otherwise be generated, including exemptions, deductions, credits, and lower tax rates. Tax expenditures are different than a direct spending program in that once enacted they are not usually time-limited and do not need to be reenacted as part of the biennial budget. Tax expenditures are reflected on the revenue side of the budget and are not itemized.

A provision is considered a tax expenditure if the Department of Revenue determines that it meets all of the following seven criteria: (1) it has an impact on a tax that is applied statewide; (2) it confers preferential treatment; (3) it results in reduced tax revenue in the applicable fiscal years; (4) it is not included as an expenditure item in the state budget; (5) it is included in the defined tax base for that tax; (6) it is not subject to an alternative tax; and (7) it can be amended or repealed by a change in state law. The Department of Revenue publishes the Minnesota Tax Expenditure Budget estimating the fiscal impact of Minnesota's tax expenditures. The latest report is available at:

http://taxes.state.mn.us/legal_policy/pages/research_reports_content_expenditure.aspx

Taxation, Impact of — Impact of taxation refers to the initial burden of the tax, experienced by the person or firm legally obligated to pay the tax.

Taxation, Incidence of — Incidence of taxation refers to the ultimate burden of the tax after the person or business firm legally obligated to pay the tax alters its behavior in response (if it does alter its behavior). In some cases, such as taxes imposed directly on households, the tax impact and tax incidence are the same. In other cases, such as taxes on businesses, the incidence is shifted from the business to others. Tax incidence will differ from tax impact if the person paying the tax can shift the burden to others, either through higher prices or lower wages.

Unallotment — An unallotment is an executive branch-initiated reduction to a previous allotment of an appropriation. In the general fund, allotments are made only after the budget reserve account has been fully exhausted. An unallotment has the practical effect of an appropriation reduction but does not change the legal authorization to expend money, and does not change the budget base used for estimates of future spending. *See M.S. § 16A.152, subdivision 4.*

Contact Matt Massman, Lead Fiscal Analyst, at 651/297-8057 or matt.massman@senate.mn

Fiscal Issue Briefs offer background information and analyses on the budget process and specific budgeted issues related to matters that have been or are likely to be addressed by the Legislature. Senate Fiscal Issue Briefs can be viewed on the Office of Counsel, Research & Fiscal Analysis web site at www.senate.leg.state.mn.us/departments and follow the links to the Office of Counsel, Research, and Fiscal Analysis.