

Montana



Comprehensive Annual Financial Report June 30, 2000

MONTANA
COMPREHENSIVE ANNUAL
FINANCIAL REPORT
For the Fiscal Year Ended June 30, 2000

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STATE OF MONTANA
SELECTED STATE OFFICIALS

EXECUTIVE

Marc Racicot

Governor

Judy Martz

Lieutenant Governor

JUDICIAL

J. A. Turnage

Chief Justice

LEGISLATIVE

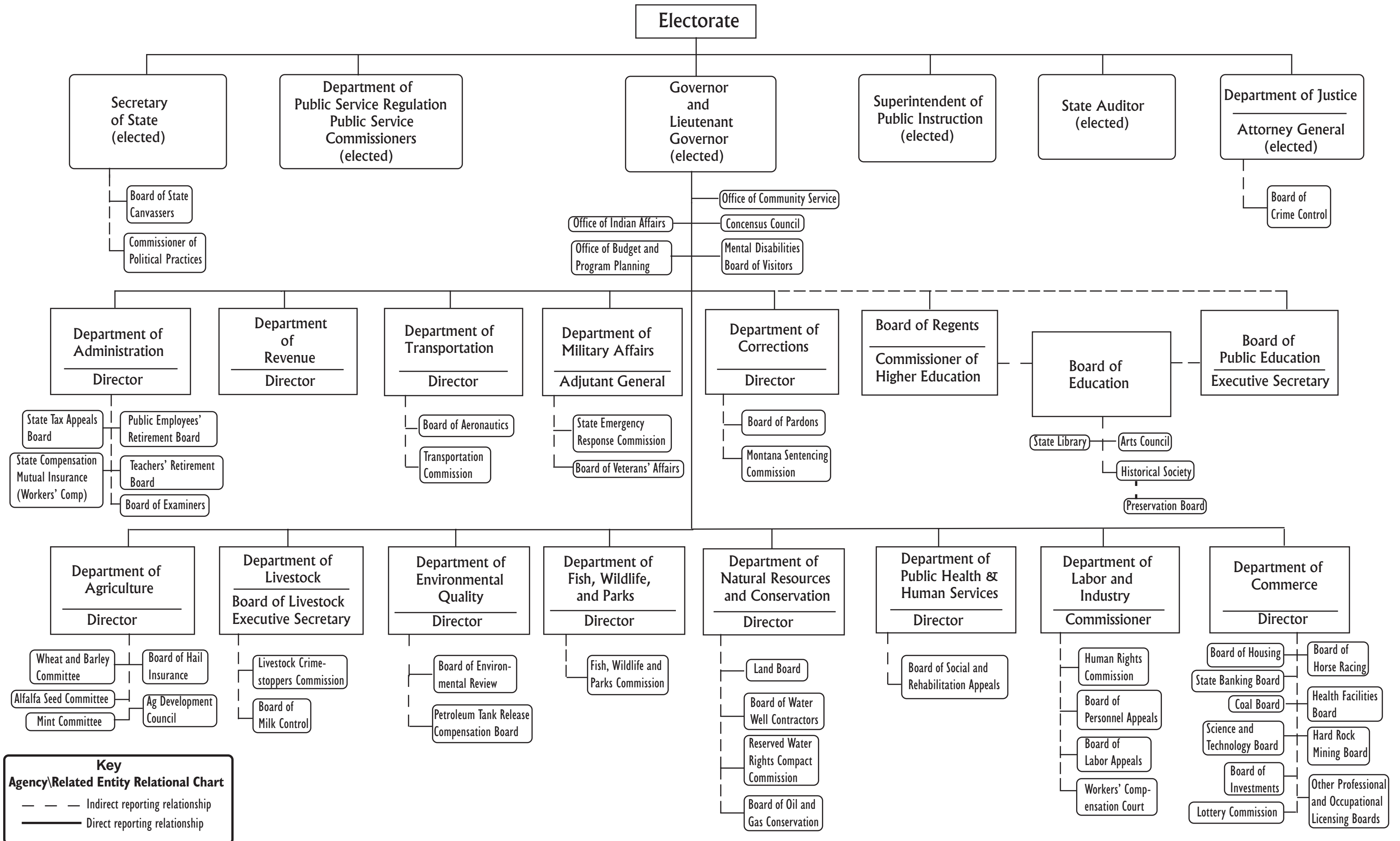
Bruce Crippen

President of the Senate

John Mercer

Speaker of the House

Montana Executive Branch



Key
Agency\Related Entity Relational Chart
 - - - Indirect reporting relationship
 ——— Direct reporting relationship

**STATE OF MONTANA
 COMPREHENSIVE ANNUAL FINANCIAL REPORT
 FISCAL YEAR ENDED JUNE 30, 2000**

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**DEPARTMENT OF ADMINISTRATION
DIRECTOR'S OFFICE**



JUDY MARTZ, GOVERNOR

MITCHELL BUILDING

STATE OF MONTANA

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March 28, 2001

To the Citizens, Governor and Members of the Legislature of the State of Montana:

In accordance with Section 17-2-110, Montana Code Annotated (MCA), I am pleased to submit the Comprehensive Annual Financial Report (CAFR) of the State of Montana for the fiscal year ended June 30, 2000. Responsibility for the accuracy of the data presented and the completeness and fairness of the presentation rests with the Department of Administration. To the best of our knowledge and belief, the enclosed data are accurate in all material respects and are reported in a manner designed to present fairly the financial position and results of operations of the various funds and account groups of the State of Montana. All disclosures necessary to enable the reader to gain an understanding of the State's financial activities are included

Description of the CAFR

This report and the accompanying financial statements and statistical tables were prepared in accordance with standards set forth by the Governmental Accounting Standards Board (GASB).

This CAFR is divided into three main sections: introductory, financial and statistical. The introductory section includes an organization chart for the State, a table of contents and this transmittal letter. The financial section contains the independent auditor's report, the general purpose financial statements, notes to the financial statements, combining statements by fund type, and other schedules. The statistical section includes financial, economic and demographic data.

This report includes all funds and account groups of those entities that comprise the State of Montana (the primary government) and its component units. The component units are entities that are legally separate from the State but for which the State is financially accountable, or whose relationship with the State is such that exclusion would cause the State's financial statements to be misleading or incomplete. The GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the State is able to impose its will on that organization or (2) there is the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the State. The following component units are included in the State's financial reporting entity: Housing Authority, Health Facilities Authority, State Compensation Insurance Fund (Old and New), Public Employees' Retirement Board, Teachers' Retirement System and the Colleges, Universities and Colleges of Technology. These component units are discretely presented in the State's financial statements.

Economic Condition and Outlook

The forecast is for Montana's nonfarm labor income growth to average about 2 percent from 2001 to 2002, down from 2000's growth of 3.5 percent, but 2 percent is the average growth predicted for the first decade of the new millennium. Continued production increases in Montana's basic industries, plus strong construction (primarily highway) activity will be the major contributors to future growth.

Montana's population has been stable at about 880,000 persons since 1997. Net outmigration has replaced the sizable influx of persons during the first half of the 1990's. The population forecast for 2000 has been trimmed down to 885,000 (from 920,000 two years ago) and to 970,000 (from 1,015,000 two years ago) in 2010. Recent reports indicate that Montana did not regain its second Congressional seat in 2000.

While individual agricultural commodity markets continue to be volatile, total Montana agricultural receipts have been unusually stable in the past 10 years. During the 1999/2000 time period, agricultural receipts ranged from about \$2.2 billion to \$2.4 billion. Cattle, wheat and barley comprise about 80 percent of the state's agricultural receipts. During the 1990's, Montana livestock market receipts ranged from a low of \$836 million to a high of \$1.2 billion, with cattle generating 80 percent of those receipts. The fluctuations in receipts are primarily a reflection of cattle price. Wheat prices continue to be depressed by high production; high stocks and weak export demands. However, Montana raises high-protein wheat, and this past year producers of particularly high-protein wheat received as much as \$1 per bushel price premium. In the longer term, Montana has a comparative advantage in the market because the state's land and climate is conducive to wheat production.

The manufacturing sector in Montana, which ranges in production of very complex and sophisticated high technology equipment to cottage industries producing handmade items like jewelry or sporting goods, displayed market conditions that were substantially better in 1999 than in 1998 due to a continued very strong U.S. economy and improving conditions in much of the world. The feared large-scale decline of 1999 did not materialize, and with much better than expected domestic and global economic conditions, virtually all of Montana's manufacturing sectors reported higher prices in 1999. Sales value of all products manufactured in Montana was up several hundred million dollars to approximately \$5 billion in 1999. Market conditions should remain favorable in the upcoming year, and manufacturing activity should continue to increase in Montana.

Wood and paper products markets in 1999 were substantially improved over 1998. With a stronger than expected U.S. economy and modest improvements in the global economy, wood and paper product prices increased dramatically during the first half of 1999. In July 1999 lumber prices were near record levels and 40 percent higher than they were in July 1998. However, in late July prices turned sharply downward and fell steadily into October before rebounding in November and December. In total, however, lumber and plywood prices were 10 to 20 percent higher in 1999 than 1998. Because of somewhat lower levels of U.S. housing starts, lumber and plywood producers expect slightly lower, but more stable, prices in 2000. Timber availability remains the major concern of Montana's industry.

Major Initiatives

In fiscal year 2000, the General Fund unreserved undesignated fund balance rose \$31.6 million over projections due primarily to increased individual income tax collections based on higher wage and capital gains income growth.

The Fifty-sixth Legislature met on May 8, 2000, in response to a special session call issued by Governor Racicot. The Legislature met from May 8 through May 11, 2000. As a result of the special session, three referendums were passed. The first was to repeal the state inheritance tax, the second was to deposit 40 percent of the tobacco settlement funds into a trust fund for tobacco disease prevention programs and the third was to reduce the taxation of light vehicles and eliminate the sales tax on new motor vehicles beginning January 1, 2001. The voters approved all three issues in the November 2000 election. The revenue impact to the General Fund in FY2001 for the tobacco settlement funds is estimated at \$10.1 million. The revenue impact to the General Fund for the repeal of inheritance taxes for deaths occurring after December 31, 2000, is estimated at \$19.2 million for the FY2003 biennium. The revenue impact to the General Fund for the reduced vehicle fees is estimated at \$4.2 million in FY2001.

House Bill 260 passed by the 1999 Legislature proposed a significant change to coal production taxes in an effort to fund economic development projects in Montana. House Bill 260 established a new tax on coal production, the Coal Producers' License Tax, and reduced the Coal Severance Tax. The Montana Supreme Court determined House Bill 260 to be unconstitutional and of no effect. During the Special Legislative Session, House Bill 1 was approved that statutorily appropriates the interest income from \$140 million of the coal severance tax permanent fund that is deposited in the General Fund and is for certain identified economic development programs for the biennium ending June 30, 2001.

In the 2000 Special Session, the Legislature also provided for a reduction in property taxes by increasing direct state aid to school districts from 41.8 percent to 44.7 percent which increased public school support during FY2001 by \$17.8 million above the amount appropriated during the 1999 Legislative Session.

Financial Information

Montana's Statewide Budgeting, Accounting and Human Resource System (SABHRS) is a centrally maintained, fully computerized, double-entry accounting system. SABHRS records are computer-edited.

Management of the State is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the State are protected from loss or misuse and that adequate accounting data are compiled to allow for the preparation of financial statements in accordance with generally accepted accounting principles.

In developing and evaluating the State's accounting system, consideration is given to the adequacy of internal accounting controls. Internal accounting controls are designed to provide reasonable, but not absolute, assurance that the above objectives are met. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits likely to be derived, and that the evaluation of costs and benefits requires estimates and judgments by management.

Budgetary restrictions are imposed via appropriations approved by the legislature or established administratively as provided for by state law. Appropriations are required by state law for the General, Special Revenue, and Capital Projects Funds. The level of budgetary control is generally established by fund. SABHRS is designed to provide budgetary control by preventing spending in excess of legislative and administrative authority and/or available cash. SABHRS also provides for encumbrance accounting as a technique for accomplishing budgetary control.

General Governmental Functions

Revenue sources for general governmental functions, which include the General, Special Revenue, Debt Service, and Capital Projects Funds, increased 12.2 percent from fiscal year 1999 to fiscal year 2000. Revenues from various sources for fiscal year 2000, and the amount and percentage of increases and decreases in relation to prior year revenues, are shown in the following table:

Revenue Source	Amount (in thousands)	2000 Percent of Total	Increase (Decrease) from 1999	Percent Increase (Decrease)
Licenses/Permits	\$ 125,782	4.4%	\$ 7,832	6.6%
Taxes	1,244,622	44.1	53,015	4.4
Charges for Services/Etc.	302,021	10.7	171,271	131.0
Investment Earnings	37,780	1.3	4,210	12.5
Securities Lending Income	4,991	0.2	(1,850)	(27.0)
Sale of Documents/Etc.	9,659	0.3	2,775	40.3
Rentals/Leases/Royalties	487	-	67	16.0
Contributions/Premiums	5,301	0.2	850	19.1
Grants/Contracts/Donations	13,961	0.5	1,655	13.4
Federal	1,078,455	38.1	67,796	6.7
Federal Indirect Cost Recoveries	2,091	0.1	169	8.8
Other Revenues	2,646	0.1	(191)	(6.7)
Total Revenues	<u>\$2,827,796</u>	<u>100.0</u>	<u>\$307,799</u>	

An explanation of significant changes by revenue source follows:

Taxes - The increase in revenues was primarily due to 1) a \$30.7 million increase in individual income tax receipts; 2) a \$12 million increase in corporate income tax collections; and 3) a \$8.1 million increase in fuel tax.

Charges for Services - The increase in revenue was primarily due to 1) ARCO settlement funds of \$136.3 million over what was collected in FY99 and 2) tobacco settlement funds of \$34.8 million.

Federal - The increase in revenue was primarily due to 1) a \$41 million increase in highway construction funds; and 2) a \$31.9 million increase in medical assistance program funds.

Total expenditures for all general governmental functions increased 6.8 percent from fiscal year 1999 to fiscal year 2000. Expenditures by function for fiscal year 2000, and the amount and percentage of increases or decreases in relation to the prior year amounts, are shown in the following table:

Expenditure Function	Amount (in thousands)	2000 Percent of Total	Increase (Decrease) from 1999	Percent Increase (Decrease)
General Government	\$ 154,331	5.8%	\$ 19,250	14.3%
Public Safety/Corrections	203,793	7.7	16,954	9.1
Transportation	442,211	16.7	60,527	15.9
Health/Social Services	889,480	33.5	54,396	6.5
Education/Cultural	622,105	23.4	31,376	5.3
Resource Development/Recreation	87,143	3.3	(11,274)	(11.5)
Economic Development/Assistance	123,903	4.7	3,427	2.8
Securities Lending	4,795	0.2	(1,682)	(26.0)
Debt Service	49,342	1.8	(8,959)	(15.4)
Capital Outlay	76,385	2.9	2,378	3.2
Total Expenditures	\$2,653,488	100.0	\$166,393	

An explanation of significant changes by expenditure function follows:

Transportation - Expenditure increases were primarily due to an increase in federal grant moneys that allowed the Montana Department of Transportation to do more road construction.

Health/Social Services - The expenditure increase was primarily due to: 1) Department of Corrections for contracts to house and provide services to inmates; 2) Department of Environmental Quality for bond forfeiture reclamation work; and 3) Department of Public Health and Human Services for the Children's Health Insurance Program, increased TANF expenditures and provider rate increases.

Education/Cultural - The expenditure increase was primarily for 1) an increase in the BASE aid payments to school districts; 2) federal grants which flow through to the school districts; 3) federal funds to reduce class size; and 4) additional funding to the University system for a student assistance program and community college assistance.

Debt Service - The expenditure increase was primarily due to Department of Justice paying off its Natural Resource Damage Litigation Program debt service obligation.

General Fund Balance

The unreserved undesignated fund balance of the General Fund increased from \$109.674 million at June 30, 1999, to \$146.0 million at June 30, 2000. This represents an increase of \$36.326 million, or 33.1 percent.

Enterprise Operations

The State of Montana provides numerous goods and services to the public on a user charge basis, similar to a private business. Profits from two of these operations, the State Liquor Warehouse and the State Lottery, are used to fund other services provided by the State. Following is a summary of the operating results of these two entities in fiscal year 2000:

State Liquor Warehouse - The State regulates the sale, importation, distribution and manufacturing of alcoholic beverages in Montana. A portion of the liquor sales and excise and license taxes collected through this function along with any profits generated through the administration of this regulatory function, including those from the operation of the liquor stores, are transferred to the General Fund. In fiscal year 2000, \$19.548 million was transferred to the General Fund, compared to \$18.872 million in fiscal year 1999.

State Lottery - the electorate through the passage of Referendum 100 created The Montana State Lottery during the 1986 general election. Profits generated by this operation are transferred to the General Fund and appropriated to the Office of Public Instruction (OPI) for distribution to local school districts and the Board of Crime Control (BCC) for grants to counties for youth detention services. Profits for fiscal year 2000 were \$5.8 million with OPI receiving 90.9 percent and BCC 9.1 percent of the net revenue.

Pension Trust Fund Operations

The State contributes to eight retirement systems and is the administrator of one additional system. The two largest systems, in terms of dollars contributed and employees covered, are the Public Employees' Retirement System and the Teachers' Retirement System. Montana implemented GASB Statement 25 - Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined contribution Plans and GASB Statement 27 - Accounting for Pensions by State and Local Governmental Employers in fiscal year 1996. The funded actuarial accrued liability ratio for all systems continues to improve.

The 1997 legislature enacted legislation that establishes a guaranteed annual benefit adjustment (GABA) for enrolled members or surviving beneficiaries under each of the statewide public employee retirement systems. The annual minimum adjustment of 1.5 percent will begin 36 months after a beneficiary's initiation date. The benefit adjustment, when combined with other benefit adjustments already in law, must equal at least 1.5 percent per year. The GABA automatically covers beneficiaries in the retirement systems for public employees, sheriffs and game wardens. Beneficiaries in the retirement systems for highway patrol officers, municipal police officers, firefighters unified and judges may choose to be covered by GABA or by benefits adjustment mechanisms already in place. The legislation establishing the GABA also provides a mechanism to actuarially fund the Judges' Retirement System.

The 1999 legislature enacted legislation that also establishes a guaranteed annual benefit adjustment (GABA) for certain benefit recipients in the Teachers' Retirement System. A benefit recipient is eligible for the minimum benefit adjustment of 1.5 percent if the retiree's most recent retirement effective date is at least 36 months prior to January 1 of the year in which the adjustment is to be made.

Debt Administration

Montana receives excellent bond ratings from both Moody's Investors Service (Aa3) and Standard & Poor's Corporation (AA-). State debt may be authorized either by a two-thirds vote of the members of each house of the legislature or by a favorable vote of a majority of the State's electors voting thereon. There is no constitutional limit on the amount of debt that may be incurred by the State. The Montana Constitution does, however, prohibit the incurring of debt to cover deficits caused by appropriations exceeding anticipated revenue. General obligation debt increased from \$197.02 million at June 30, 1999, to \$228.269 million at June 30, 2000.

The ratio of general obligation debt to assessed valuation and the amount of general obligation debt per capita are:

	Amount (in thousands)	Ratio of Debt to 2000 Assessed Value	State Debt Per Capita
General Obligation Debt	\$228,269	0.54%	\$258.52

* Based on 1999 estimated Montana population.

Cash Management

The uniform investment program established by the 1972 Montana Constitution directs that the Board of Investments have sole authority to invest State funds. The Board operates under the "prudent person principle" which requires the Board to 1) discharge its duties in the same manner as that of a prudent person acting in a like capacity with the same resources and aims; 2) diversify the holdings of each fund to minimize the risk of loss and maximize the rate of return; and 3) discharge duties solely in the interest of and for the benefit of the funds managed. Permissible investments include bonds, notes, debentures, equipment obligations, common stock (pension trust and higher education funds only), commercial paper, bankers' acceptances, interest bearing deposits in Montana financial institutions, real estate and any other investment in a Montana business that continues existing jobs or creates new jobs. These investments are subject to statutory restrictions for quality and size of holdings. Unless otherwise provided by law, treasury cash is pooled for investment regardless of the fund from which it is deposited and the pool's investment earnings are credited to the General Fund. The Board reported total investment income from investments under its management of \$422.6 million, an increase of 7.8 percent from the \$392.1 million earned last year. The book value of Board-managed investments increased by approximately \$65 million or 1.2 percent to \$6.3 billion at fiscal year-end 2000. The Board publishes an annual audited report of all its investment activity. That report may be referenced for more in-depth investment information.

Risk Management

The State of Montana provides benefit coverage for injured state employees through participation in the State Compensation Insurance Fund (State Fund). The State Fund is a nonprofit, independent public corporation that is managed and controlled by a seven-member board of directors. The Governor appoints the board members for four-year terms. Funding is primarily derived from the premiums paid by policyholders.

At June 30, 2000, assets for the State Fund - Old exceeded liabilities by \$18.56 million. The actuarially determined liability for unpaid claims, including those that were incurred but not reported, decreased to \$117.9 million. This represents a decrease of \$12.2 million in estimated claims liability from fiscal year 1999. The percentage of this liability belonging to the state as a participant is unknown. For the State Fund - New, assets exceeded liabilities by \$139.29 million at June 30, 2000. The actuarially determined liability for unpaid claims, including those that were incurred but not reported, was \$314.9 million presented at face value. In prior years, the unpaid claims and claim adjustments on indemnity losses were stated at their net present value in the financial statements.

The State maintains self-insurance plans for employee comprehensive medical and dental coverage and state property. Under the State Employee Group Benefits Plan the State assumes all the risk for claims incurred by plan members including State employees, elected officials, retirees and their dependents, with three exceptions. The three outside insured products are: vision care insured by the Vision Service Plan Insurance Company, the Yellowstone Community Health Plan, an insured community health option (CHO) available to state employees in four counties in the Billings area and the New West Plan, an insured CHO available to state employees in several counties in the Missoula, Deer Lodge, Helena and Billings areas. Premiums are collected through payroll deductions, deductions through the Public Employees' Retirement System and self-payment. For the period ending June 30, 2000, the plan reported retained earnings of \$20.76 million, a decrease of \$2.98 million over June 30, 1999.

The Montana University System (MUS) Group Benefits Plan offers medical, dental, and vision insurance coverage to employees of the Montana University System, the Montana Higher Education Student Assistance Corporation

(MHESAC), and the State Bar of Montana, as well as their dependents, retirees, and COBRA members. The MUS Group Benefits Plan is fully self-insured. Blue Cross/Blue Shield is the claims administrator for the plan. Managed Care Montana (Blue Cross/Blue Shield of Montana) has a contract for utilization management. The utilization management program consists of hospital pre-authorization, case management and medical necessity review. For the period ending June 30, 2000, the plan reported retained earnings of \$5.4 million, an increase of \$.5 million over June 30, 1999.

The State's property insurance plan provides coverage for general liability, automobile liability, automobile physical damage, and state-administered foreclosure housing units. The State self-insures the \$150,000 deductible per occurrence for most property insurance as well as various deductible amounts for other state property. The state also self-insures against losses of equipment below \$150,000 of value, with state agencies paying the first \$1,000. Commercial property insurance protects over \$2.1 billion of state-owned buildings and contents. The flood and earthquake liability limit is \$400 million per occurrence with a \$1.0 million deductible for earthquakes and a \$0.5 million deductible for floods. Premiums for the plan are collected from all State agencies, including component units. Based on the most recent actuarial report prepared by Tillinghast and issued for the period July 1, 1991 through June 30, 2000, a liability of \$25.3 million, which is discounted and assumes an annual rate of 4 percent, is recorded in the accompanying financial statements for estimated claims including those incurred but not reported. This represents an increase of \$8.2 million in estimated claims liability from fiscal year 1999.

Independent Audit

The financial statements contained in Montana's Comprehensive Annual Financial Report were audited in accordance with generally accepted auditing standards by the Legislative Audit Division. The Legislative Auditor is appointed by and reports to the Legislative Audit Committee. The Deputy Legislative Auditor issued an unqualified opinion on the State's financial statements for fiscal year 2000.

Certificate of Achievement

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the State of Montana for its Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 1999. This was the thirteenth consecutive year that the State received this prestigious award. In order to be awarded a Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized CAFR, whose contents conform to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements.

Acknowledgments

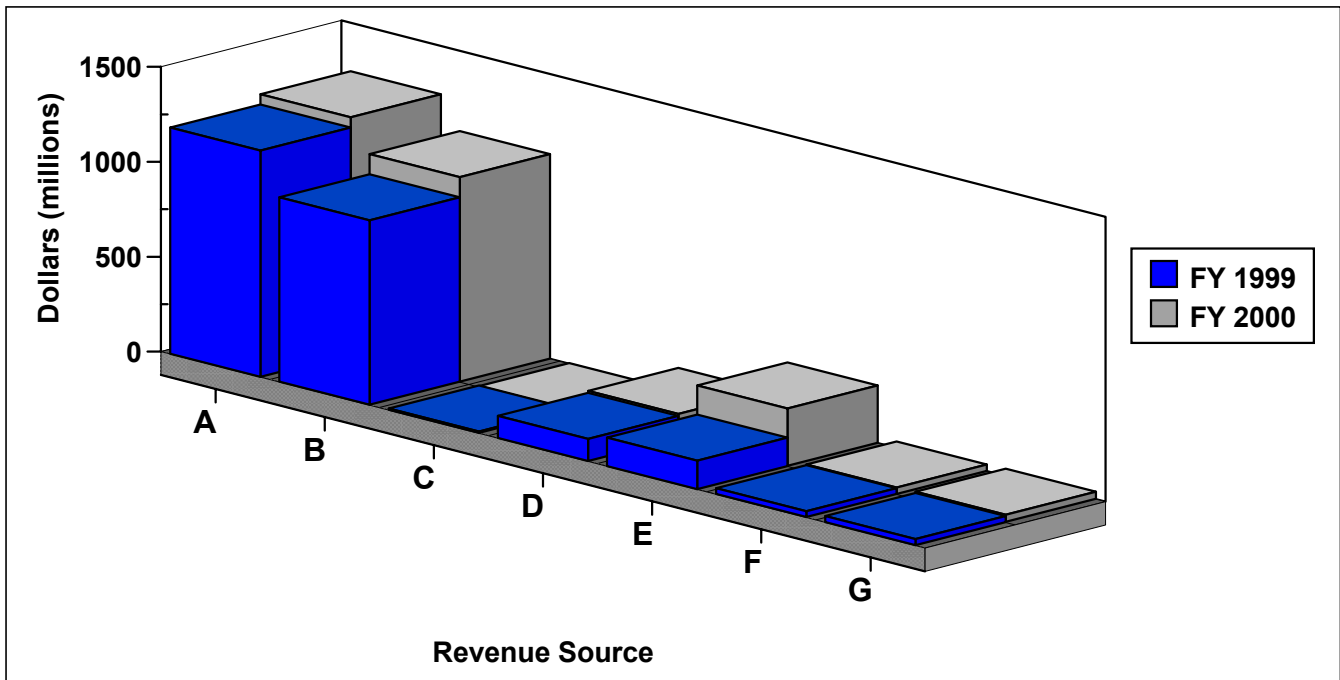
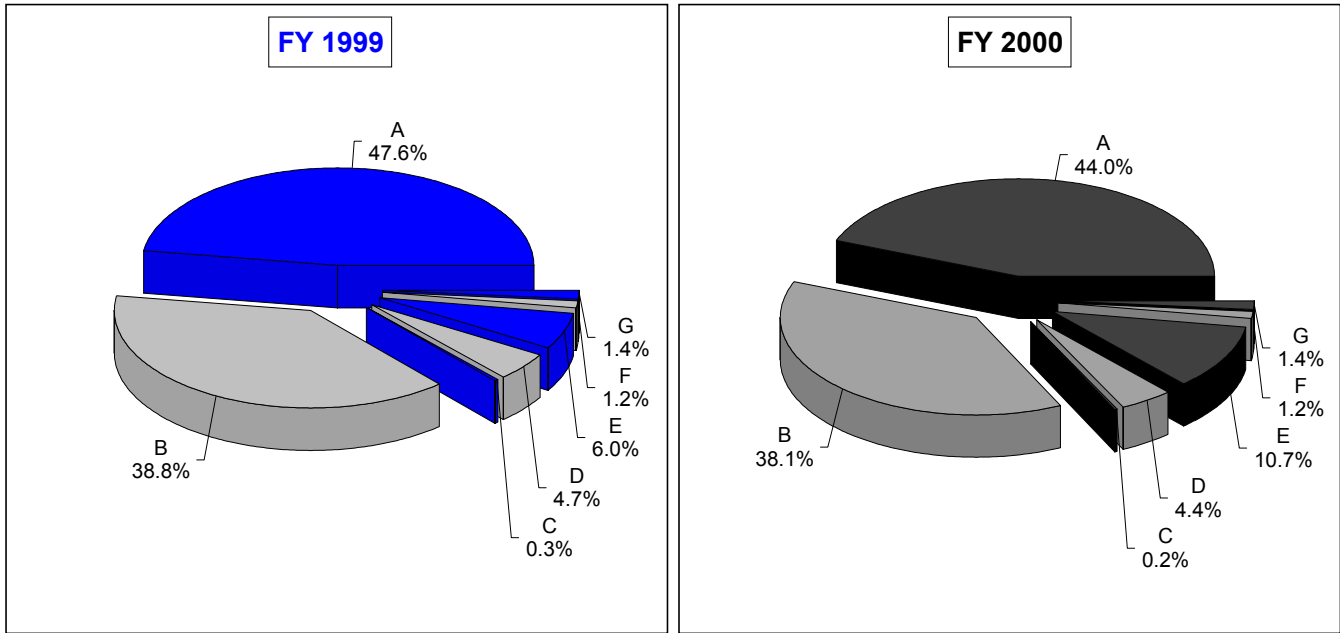
The preparation of this report on a timely basis could not be accomplished without the efficient and dedicated service of the entire staff of the Accounting Bureau and the cooperation of accounting personnel at the individual State agencies. I would like to express my appreciation to Accounting Bureau and other agency personnel who participated in the preparation of this document. I would also like to thank the legislature and all State agencies for their interest and support in planning and conducting the financial operations of Montana in a professionally responsible and progressive manner.

Respectfully submitted,

(Signature on File)

Barbara Ranf, Director
Department of Administration

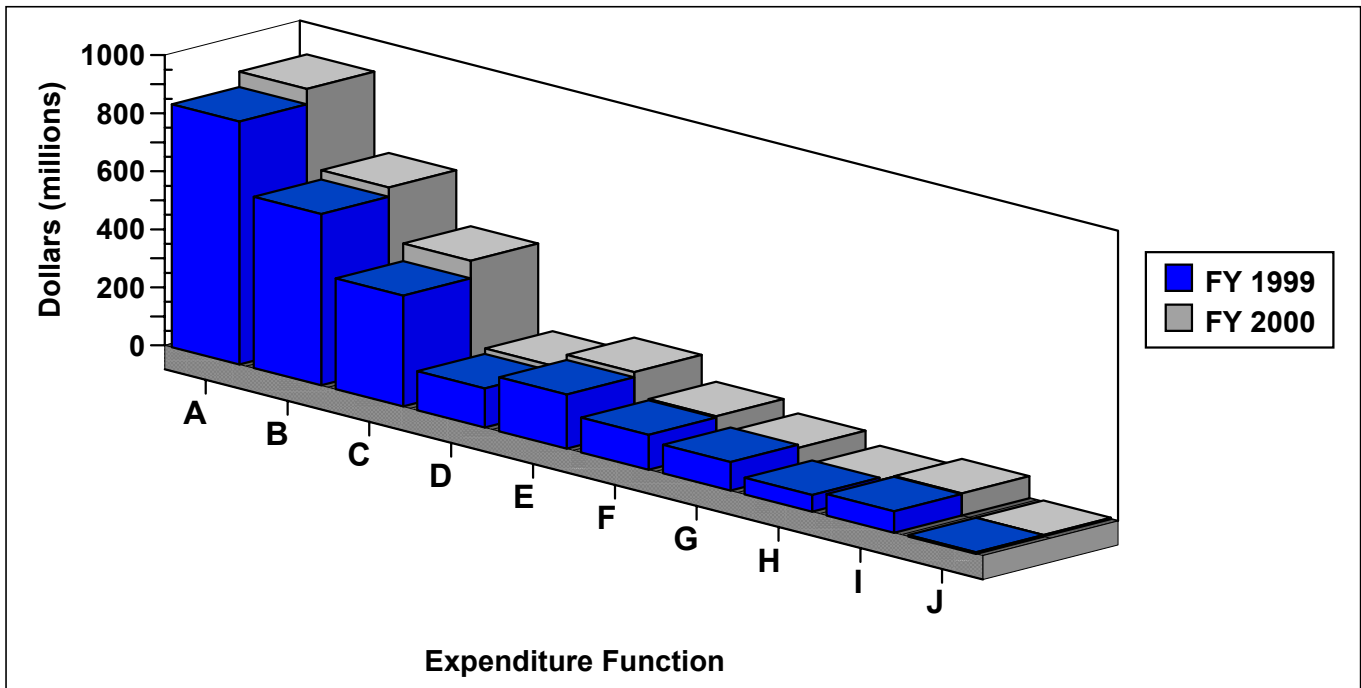
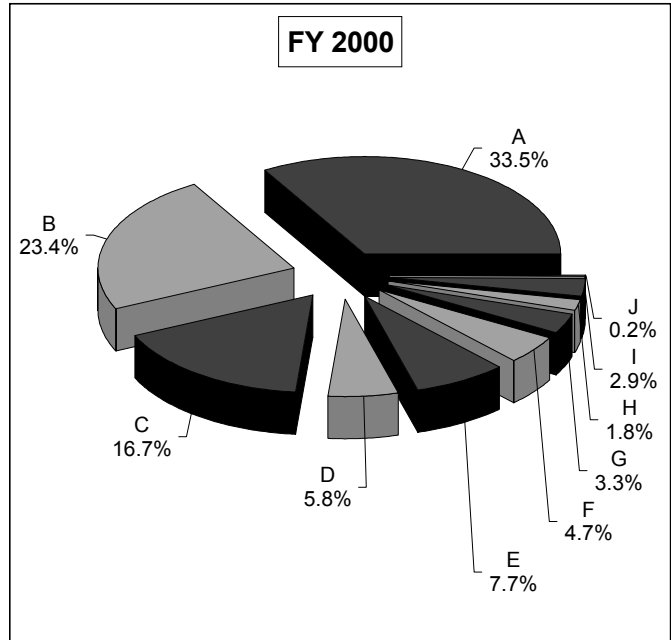
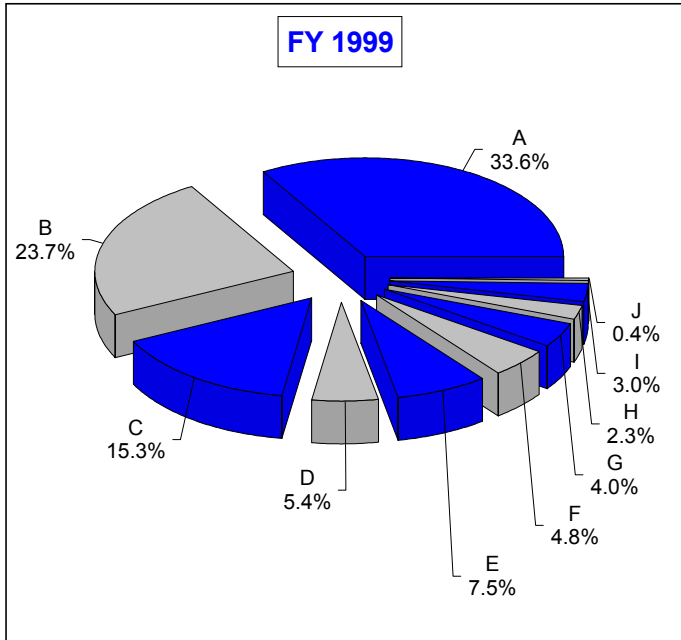
State of Montana Revenues by Source All Governmental Fund Types



Legend:

- (A) Taxes
- (B) Federal
- (C) Securities Lending Income
- (D) Licenses/Permits
- (E) Charges for Services/Fines/Forfeits
- (F) Other Revenues (includes contributions, premiums, rentals, leases, royalties, grants, contracts, donations, federal indirect cost recoveries and sale of documents, merchandise and property)
- (G) Investment Earnings

State of Montana Expenditures by Function All Governmental Fund Types



Legend:

- | | | |
|----------------------------|-------------------------------------|------------------------|
| (A) Health/Social Services | (E) Public Safety/Corrections | (I) Capital Outlay |
| (B) Educational/Cultural | (F) Economic Development/Assistance | (J) Securities Lending |
| (C) Transportation | (G) Resource Dev/Recreation | |
| (D) General Government | (H) Debt Service | |