


**Date:** August 19, 2008  
**To:** Agency Heads  
**From:** Jim Schowalter   
State Budget Director  
**Subject:** FY 2010-11 Biennial Budget Preparation – Part C

This memorandum and attached documents provide instructions on the approach, timetable, and required agency actions for preparation of FY 2010-11 biennial budgets.

The environment for this budget process is one of continued fiscal pressure. At the end of the last legislative session, projections for FY 2010-11 showed that revenues would fall short of current commitments by \$940 million. Additional commitments and inflationary costs should add to this figure. While we do have the good news that year to date revenues exceed earlier estimates, other economic factors suggest that there will still be a sizable gap to address.

To manage this gap, we could simply ratchet down all spending across state government. However, this approach would indiscriminately lower services and performance everywhere. We hope to take a more informed approach and this starts with developing useful information necessary to assess government services, priorities and performance.

Initial work on background information has already started. Per instructions issued in the last month, many agency staff are preparing materials to describe current activities, account for spending, and describe results. These are key elements of the budget documents, and I encourage you to review them to be sure that they adequately describe your activities.

Looking ahead, we will turn our attention to a high level evaluation of your agency's activities. First, in a memo, we would like to know what strategies and activities are leading to your greatest successes, where changes to the operating environment may drive future choices, and what business approaches need improvement. Where applicable, we will also want to know the preliminary outcomes of major initiatives or pilot projects that have been initiated over the past several biennia. This memo is not expected to be comprehensive but instead is your opportunity to identify the choices that will define your agency's future.

The next step in the process is the development of budget options. Based on your agency assessment and subsequent discussions, you should prepare options that help to address your mission within the context of limited funding. Existing programs will compete with one another as well as with transformational ideas and emergency spending requests advanced from other parts of state government.

As your agency develops options, please keep in mind some of the broad themes advanced by the Governor:

- **Transform Government:** State government must transform the way it delivers services to become more consumer friendly and cost-effective.
- **Reward Performance:** Wherever possible, the state should implement performance incentives to make government more market-driven and consumer-oriented.
- **Reduce Cost:** Growth in the overall size and cost of government must be reduced.

The information described above will be the basis for final budget deliberations by the Governor. In the interim, staff from the Department of Finance & Employee Relations and the Governor's office will review each of the budget elements described above and work with you to identify critical options requiring additional work.

Please carefully review the attached budget context and instructions as you continue your internal budget discussions. If we can provide additional information, please let us know.

Thank you.

## **FY 2010-11 Budget Context**

**We are currently spending more than we are collecting.** The state balanced the current budget with measures that included using \$500 million from its budget reserves. Those one-time funds will not be available to balance the next biennial budget (and will need to be replaced).

**Current planning estimates show a significant gap.** A general fund budget gap of \$940 million is projected for FY 2010-11, excluding inflationary pressures. Current estimates anticipate that general fund revenues will grow nearly \$600 million over the current biennium but current law spending is expected to increase by \$1.5 billion.

**Monthly revenues have exceeded expectations.** Our monthly revenue collections have exceeded projections by roughly \$400 million. This is good news but a detailed analysis suggests that most of this improvement will not recur year after year.

**The economic outlook has weakened.** Quick action to deliver federal stimulus funds led to a stronger than expected economy in the first half of 2008. With that boost completed, our national forecasters anticipate little help in offsetting concerns that include high energy prices, inflationary pressure, and continued uncertainty in the housing and credit markets. This could potentially add to the budget gap that we are already anticipating.

**The current law planning estimates do not include general inflation.** Agencies must plan to absorb any increases in the cost of goods or services within their base budget plan. Providing new funding for this purpose will be decided as part of the budget process and will have to compete with other options. Specifically, agencies must anticipate the potential costs of FY 2010-11 labor contracts and build them into their current base funding scenarios. For planning purposes, agencies should use three percent per year for total compensation increases in order to estimate future costs and impact on agency services.

**While emphasis is placed on the state general fund, the same principles apply to other directly appropriated funds and selected others.** For statutory funds, supported by dedicated revenues, the general guideline is that planned spending must remain within projected resources and that priorities still must be set and identified within total overall agency spending. Your Executive Budget Officer will communicate the specific funds that need to be included in this analysis.

### **Formal Budget Documents and the Budget System**

Apart from the steps and information required for budget decision-making, separate agency actions are required to prepare the final budget documents for the Governor's budget. While the process used to reach decisions may be different, the budget documents prepared for the Legislature will be similar to those prepared two years ago. The online budget documents will incorporate agency background materials as well as Governor's recommendations. The budget documents will highlight changes from the current appropriation levels by displaying change items with appropriate explanations of the Governor's decisions.

Separate instructions have been sent to agency staff on the steps and timing necessary to prepare information in the Budget Information System (BIS). This will require that agency staff ensure that historical appropriations and spending data is accurate, that forecast revenues are complete and correct, that compensation budgets and FTE staffing levels are appropriately constructed, and that any required adjustments to calculate the starting point for FY 2010-11 are properly reflected. In general, these steps must be completed by October 15<sup>th</sup> - prior to the November forecast. After the forecast, activity in the budget system will shift to finalizing agency budget decisions, entering change items, and incorporating final recommendations into budget documents for publication.

## FY 2010-11 Budget Development Schedule

### STEP ONE: Assess Current Activities

#### By October 6th

- Agencies should prepare an agency assessment in memo format to the Governor and Commissioner of Finance & Employee Relations. This memo should be no more than five (5) pages in length. It should be a comprehensive self-evaluation that discusses the agency's mission, outcomes, effectiveness and opportunities. At a minimum, it should answer the following questions:
  - What strategies have proven most effective for accomplishing your agency mission? What programs best demonstrate these strategies?
  - What programs or activities need attention or have unclear results?
  - How would the agency meet its highest priorities in the coming biennium within its base funding level? Would staffing changes be needed? Would resources be reallocated from one activity to a different one?
  - What trends outside your direct control are influencing the agency's plan for the future?
- Agencies should attach an inventory of significant initiatives and/or demonstration projects over the past several biennia, provide an update on the status and preliminary outcomes of these projects and how they impact agency operations, and where they fit into agency priorities moving forward.
- Agency memos are not expected to be fund specific. To the extent possible, focus on the agency mission and not the individual funding sources.
- Memos are due to your Executive Budget Officer and Governor's Office Policy Advisor by October 6, and will become the starting point for discussions in subsequent meetings with the Executive Budget Team.

### STEP TWO: Prepare Preliminary Budget Options for Review

#### By November 3rd

- Based on the self evaluation done for the agency assessment memo, agencies should identify preliminary options for the next biennial budget. These options should focus on some of the broad themes advanced by the Governor:
  - **Transform Government:** State government must transform the way it delivers services to become more consumer friendly and cost effective.
  - **Reward Performance:** Wherever possible, the state should implement performance incentives to make government more market-driven and consumer-oriented.
  - **Reduce Cost:** Growth in the overall size and cost of government must be reduced.
- The change item template should be used to describe an agency's preliminary budget options and can be found at: <http://www.finance.state.mn.us/budget/operating/201011/informationforms.html>

- The information provided with these options should be sufficiently complete to assess the programmatic and financial impact of the proposals. These preliminary budget options must also identify relevant Minnesota Milestones or other statewide goals or indicators that relate to the proposal as required under M.S. 16A.10, Subdivision 1c as amended by Laws 2008, Chapter 318.
- For technology-related budget options, agencies should provide the additional information requested in the template to ensure that the Office of Enterprise Technology (OET) is able to review and comment on the project as required under M.S. 16E.03. OET analysts may follow up with individual agencies to request additional information following submission.
- Preliminary budget option narratives and financial data will not be loaded into BBS until later in the decision-making process.
- Options are due to your Executive Budget Officer and Governor's Office Policy Advisor by November 3.
- Following review by Finance & Employee Relations and Governor's Office staff, agencies may be asked to revise their budget proposals and/or provide more specific information.

### **STEP THREE: Executive Budget Team Review and Decision-Making**

#### **Early November through Mid-December**

- A Governor-appointed Executive Budget Team (EBT) for most cabinet and select non-cabinet agencies will evaluate agency options to identify strategies/proposals that will best meet statewide priorities.
- The EBT will prepare a broad statewide budget strategy that will include high-level budget targets as well as areas for improvement, consolidation or alternative service delivery options. This proposal will be finalized for the Governor's review.
- Please note that EBTs will start earlier in the fall for select agencies; these agencies will be contacted individually.

#### **December 4<sup>th</sup> (tentative): FY 2009-11 Economic and Budget Forecast Release**

#### **Mid-December through Mid-January**

- EBT presents recommendations to the Governor.
- Governor finalizes official budget decisions.
  - The November forecast will drive the details of final decision-making for the Governor's budget through the month of December.
  - Agencies may be asked to modify options or produce alternatives consistent with policy directions set by the Governor.
  - Agencies will work with staff from Finance and Employee Relations and the Governor's Office to finalize budget change items.

#### **January 27, 2009 (tentative): Governor's Budget Presented to 2009 Legislature**