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March 28, 2003

The Honorable Calvin K. Y. Say
Speaker of the House of Representatives
Twenty-Second State Legislature
State Capitol, Room 431
415 S. Beretania Street
Honolulu, Hawaii 96813

The Honorable David Y. Ige
Senator, Sixteenth District
Twenty-Second State Legislature
State Capitol, Room 215
415 S. Beretania Street
Honolulu, Hawaii 96813

Dear Speaker Say and Senator Ige:

Re: Executive Restrictions on Appropriations and Lapses

You have each raised questions relating to the preparation of the six-year program and financial plan and budget and budget execution processes. Although the questions are different, because they are related, we will answer them together.

First, in a letter dated February 26, 2003, that was addressed to Governor Linda Lingle, Speaker Say asked whether the Administration believed that it was necessary for the Legislature to reduce appropriations for fiscal year 2002-2003 by amending Act 177, Session Laws of Hawaii 2002, in order to appropriate them for future expenditure in the 2003-2005 biennium budget that is in the process of being developed. Speaker Say seeks clarification as to: (1) whether the executive branch believes that it is unable under the allotment system, part II of chapter 37, Hawaii Revised Statutes ("HRS"),

to implement its proposed funding restrictions for fiscal year 2002-2003; or (2) whether the executive branch believes that it would be improper for the biennial budget bill for 2003-2005 to incorporate, as revenues, the proposed restrictions for fiscal year 2002-2003 unless they were reflected as reduced expenditures in the budget adopted legislatively for 2002-2003. As to the first item, Speaker Say further inquired whether there is a particular executive restriction that is being proposed that is somehow prevented by chapter 37. As to the second item, we understand that Speaker Say believes that Attorney General Opinion No. 83-4 addressed only the incorporation of proposed executive restrictions for a particular fiscal year as revenue in the budget for the same fiscal year.

Although the letter dated March 8, 2003 from Senator Ige requested our opinion regarding the use of budget restrictions and lapses in developing the executive budget, the concerns relate more to the development of the six-year program and financial plan.

We answer your questions as follows:

1. The Department of Budget and Finance does not believe that it is unable under chapter 37, HRS, to implement its proposed funding restrictions for fiscal year 2002-2003. We concur and know of no reason why the executive branch cannot exercise its authority under part II of chapter 37, HRS, to reduce allotments for the fiscal year in progress. We do not know of any particular executive restriction that is being proposed that cannot be imposed under chapter 37.

2. The Department of Budget and Finance believes and we concur that it would be improper for the biennial budget for fiscal biennium 2003-2005 to incorporate as revenues the proposed restrictions for fiscal year 2002-2003 unless those restrictions were reflected as reduced appropriations in the budget adopted legislatively for fiscal year 2002-2003. Appropriations for fiscal year 2002-2003 that are restricted through the allotment system are not "available resources" for purposes of budget

preparation pursuant to section 37-71, HRS. The restricted appropriations are still appropriated and cannot be used for another purpose until the appropriations lapse[1] or are reduced by subsequent legislation.

We believe that the analysis and reasoning set forth in Attorney General Op. No. 83-4 are still correct. We further clarify that its reasoning is not limited to prohibiting the counting of "restrictions" in one fiscal year as "available resources" for that same fiscal year. The restrictions imposed in one fiscal year also cannot be counted as "available resources" for the next fiscal year.

3. Senator Ige's question actually appears to relate to the six-year program and financial plan. Section 37-69, HRS, relating to the six-year program and financial plan, specifically anticipates that estimates of future amounts will be used. Using historical data to make estimates for a future fiscal period is, we believe, an acceptable planning tool.

   Nevertheless, to the extent Senator Ige is inquiring whether our conclusion as to restrictions is applicable to lapsed funds for purposes of preparing the budget, we answer yes.

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[1] The power of appropriation has been defined as the authority "to set apart from the public revenue a certain sum of money for a specified object, in such manner that the executive officers of the government are authorized to use that money, and no more, for that object and no other." Opinion of the Justices to the Senate, 375 Mass. 827, 832-33, 376 N.E.2d 1217, 1220-21 (1978) (Internal quotations and citations omitted).

DISCUSSION

A. Budget Execution.

The legislature and the executive have distinct roles in the continuum that is the budget and appropriation process. Beginning with the appropriation, the State Constitution is clear that the authority to appropriate moneys for the working of state government rests with the legislature[2]. Once the appropriations bill has been enacted and the fiscal year begins, the legislative work is complete and it is the executive branch's responsibility to implement the budget.

In recognition of the fact that circumstances may change after the budget has been determined and when the legislature is not in session, the allotment system was established in part II of chapter 37, HRS, in order to meet the ongoing requirement to maintain a balanced budget. The allotment system is a method by which appropriations made by the legislature are distributed to the expending agencies and managed by the executive branch of government. The fiscal year, beginning on July 1 of each calendar year, is divided pursuant to section 37-32, HRS, into four allotment periods, beginning on the first days of July, October, January, and April. Executive branch expending agencies will not receive the appropriation for an allotment period until they have submitted to the Director of Finance an estimate of the amount required to carry on the work of the expending agency for that period and the estimate is approved, increased, or decreased by the Director of Finance pursuant to action 37-74, HRS. Pursuant to section 37-35, HRS, the

[2] Article III, Section 1: "The legislative power shall be vested in a legislature . . ."; Article VII, Section 5: "No public money shall be expended except pursuant to appropriations made by law." See, also, Article VII, Section 9. ("In each regular session in an odd-numbered year, the legislature shall transmit to the governor an appropriation bill or bills providing for the anticipated total expenditures of the State for the ensuing fiscal biennium.")

allotments can be approved, reduced, or modified "having due regard for:

> (1) The probable further needs of the [expending agency] for the remainder of the term for which the appropriation was made;
> (2) The terms and purposes of the appropriation, the progress of collection of revenues, and the condition of the treasury; and
> (3) The probable receipts and total cash requirements for the ensuing quarter . . . ."[3]

The allotment system, then, is a plan of distribution and apportionment of appropriations during the course of the fiscal year for which the appropriations are made. Part II of chapter 37 allows the governor to reduce expenditures of the executive branch or any of its agencies below their appropriations whenever actual revenues are less than the revenue estimates upon which the appropriations were originally based.

Although sometimes people refer to a restriction as a change in the appropriation, that is not the case. The appropriations act is not amended; rather the timing and amount of distribution of the appropriation is affected. The governor cannot, by restrictions, make substantive changes to the appropriations act. The governor merely affects the timing of distribution. The distribution can be changed up to the end of the fiscal year because the money in question is appropriated, i.e., set aside for a specific purpose for a specific period of time. The appropriation sets aside that money for a specific purpose until the money is used, or until the appropriation has lapsed as provided in article VII, Section 11 of the State Constitution and Sections 37-41 and 40-66, HRS, or the appropriation is lapsed by legislative action.

The allotment system has as an objective the maintenance of a balanced budget. The allotment system allows the governor to accomplish at the end of the budget process what the governor is

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[3] Sections 37-36 and 37-37. See, also, Section 37-74(c)(3), HRS.

required to do when the six-year financial plan and budget are initially submitted to the legislature.

B. Budget Preparation.

Article VII, Section 8 of the State Constitution provides in pertinent part:

> [T]he governor shall submit to the legislature a budget in a form provided by law setting forth a complete plan of proposed expenditures of the executive branch, estimates as provided by law of the aggregate expenditures of the judicial and legislative branches, and anticipated receipts of the State for the ensuing fiscal biennium, together with such other information as the legislature may require . . . . The budget prepared by the governor . . . shall also be submitted in bill form. The governor shall also, upon the opening of each such session, submit bills to provide for such proposed expenditures and for any recommended additional revenues or borrowings by which the proposed expenditures are to be met.

The constitutional provisions relating to the budget and financial plan are implemented by chapter 37, HRS. Part IV of chapter 37, entitled "The Executive Budget," describes in detail the information and format that the governor is supposed to provide to the legislature. Section 37-65, HRS, specifically provides that, among other things, "[t]he governor shall . . . formulate and recommend for consideration by the legislature the State's long-range plans, a proposed six-year state program and financial plan and a proposed state budget."

Section 37-71, HRS, contains the statutory outlines of what the executive budget should contain[4]. The biennium "budget" is

[4] Subsection (g) of Section 37-71 provides that the budget and the six-year program and financial plan may be combined into a

the program and budget recommendations of the governor for the ensuing two fiscal years.[5] The budget must contain:

(1) The state program structure;
(2) Statements of statewide objectives;
(3) The financial requirements for the next two fiscal years to carry out the recommended programs; and
(4) A summary of state receipts and revenues in the last completed fiscal year, a revised estimate for the year in progress, and an estimate for the succeeding biennium.

In practice, the governor must develop the financial plan and proposed budget several months before the financial plan, budget, and appropriations are considered by the legislature.

Section 37-71(d)(1)(A) refers to "the total state resources anticipated from existing taxes and nontax sources at existing rates, by resource categories (including the available fund balances or deficits and anticipated bond receipts)" (emphasis added).

In Attorney General Op. No. 83-4 we stated, "It is our opinion that, for purposes of §37-71, 'available fund balances' mean the unappropriated surpluses of the several state funds. It does not include the 'savings' resulting from executive restrictions on the expenditure of appropriations made pursuant to the allotment system . . . because such savings are not projected income for budgetary purposes but rather, a result of expenditure controls to be exercised following adoption of the budget." Until the end of the fiscal year when the related appropriation is lapsed, the "savings" are appropriated moneys. As noted in footnote 2 of Opinion No. 83-4, "savings" resulting

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single document. It is our understanding that it has been the practice of the executive for many years to submit the six-year program and financial plan and budget as a single document and to submit the budget in bill form as well.

[5] The supplement budget is submitted in the same manner as the biennial budget. See, § 37-72, HRS.

from the use of the allotment powers may become part of the unappropriated surplus of a fund only upon expiration of the fiscal period for which the appropriation is made, pursuant to sections 40-66 and 40-67, HRS.

If the exercise of the spending powers under the allotment system results in "savings" in appropriated funds, those savings may not be reallocated to another purpose except pursuant to a legislative appropriation. Furthermore, those savings will not lapsed back to a fund that may be appropriated until the fiscal period of the appropriation expires. For example, if money is appropriated from the general fund for a specific purpose for the fiscal year ending June 30, 2003, and through the allotment system restrictions are imposed that result in savings of $1,000,000, that $1,000,000 is not part of the general fund's available balance until July 1, 2003, the day after the period of the appropriation ends, unless the legislature reduces the amount of the appropriation before the appropriation period expires. It is only upon expiration of the fiscal period that the savings -- the unused money -- will no longer be subject to the charge of the appropriation and will revert to the funding source of the appropriation and become an "available resource." Moreover, as we concluded above, restrictions do not reduce appropriations because, until the end of the fiscal period, the restriction can be lifted and the full amount of the appropriation can be expended.

C. The Six-Year Program and Financial Plan.

The six-year program and financial plan and budget are planning documents. They require the executive to estimate costs and resources. Section 37-69, HRS, anticipates the use of estimates in developing this document. Subsection (c) of section 37-69 enumerates the information that is to be included in the financial plan. Included in that information, in subsection(c)(5), are "[f]inancial summaries displaying the State's financial condition, actual for the last completed fiscal year, and estimated for the fiscal year in progress and each of the next six fiscal years (emphasis added)."[6] Consistent

[6] § 37-69(c)(5), HRS. See, also, § 37-69(c)(6), which relates to balances of special funds.

with Opinion No. 83-4, the estimated amounts do not include "restrictions," but only include an estimate of the amount of appropriations that will be lapsed, based on historical experience. In determining the estimated amount of resources (in this case general and special fund balances) that will be available in a future year, it is not unreasonable, in our view, to use historical experience in any number of ways. The Council on Revenues in making its estimates, relies on historical experience, among other things, in making its quarterly revenue projections for the State.

As we understand the process, when the executive prepares the six-year program and financial plan and budget pursuant to Section 37-69, HRS, one of the categories displayed as a "resource" is a category called "lapses." We understand that this category and the number in the category are based upon historical experience and is an average of the actual amounts that have lapsed in a number of prior years. The number is calculated by the Department of Accounting and General Services and is provided to the Department of Budget and Finance. We have been informed that the executive has been using a historical average of lapses since at lest as long ago as 1984, either calling it a resource or a reduction in expenditures.

As noted above, the "budget" is a document that relates to proposed expenditures for the ensuing biennium. The budget may be submitted with the six-year program and financial plan, but it is not part of the six-year program and financial plan. Unlike Section 37-71(d)(1)(A), HRS, which expressly directs that only "available resources" be considered in formulating the budget, Section 37-69(c)(5), HRS, provides only as follows:

> (c) The financial plan for the ensuring six fiscal years shall more specifically include:
>
> . . . .
>
> (5) Financial summaries displaying the State's financial condition, <u>actual for the last completed fiscal year, and estimated for the fiscal year in progress and each of the next six fiscal years</u>, ...

Accordingly, it is permissible to use estimates and, historical averages to formulate the plan. It is not necessary to limit the information used in the six year program and financial plan to "available resources," or to accelerate the efforts of restrictions and or lapses by legislation that reduces amounts previously appropriated for the year that a plan is being developed. Using restrictions pursuant to the allotment system established in part II of chapter 37, HRS, is a tool to satisfy the constitutional requirement of not spending beyond the State's actual resources. It comes into play only if the purpose of the appropriation can be accomplished with less or when the actual resources available to the State are less than what was anticipated. In contrast, the historical experience of capturing the actual amounts lapsed for use in estimating the size of resources available in the future is acceptable and is a reasonable planning device.

We believe that using the historical experience is a reasonable planning tool.

We hope that we have clarified this matter so that the budget for the 2003-2005 fiscal biennium can be completed. Should you have additional questions, please do not hesitate to contact us.

Very truly yours,

Diane Erickson
Deputy Attorney General

APPROVED:

Mark J. Bennett
Attorney General