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MEMORANDUM

To: Senator Kenley

From: Jack Ross, Executive Director
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Date: June 19, 2009

RE: General Assembly not enacting budget bill before July 1, 2009.

This memorandum is in response to your request concerning Article 10, Section 3, of the Indiana Constitution, the 2007 Budget Act (P.L. 234-2007), and the issues presented if the General Assembly does not enact a budget bill with general appropriations before July 1, 2009.

I. Generally

As you know, we prepared a memo dated May 26, 1993, on issues arising from the potential occurrence of the General Assembly not providing general appropriations before the beginning of a budget cycle (copy enclosed). The 1993 memo emphasized that this legal question has not been visited in over 100 years, but based on the guidance available we concluded that state government could face a shutdown on July 1, with few exceptions.

There has been no new Indiana case law or specific enactment by the General Assembly that changes our conclusion. We do note that changes have occurred in the Indiana Code regarding continuing statutory appropriations, so the list of these appropriations that was included in the 1993 memo is now outdated.

If the General Assembly does not enact a budget, the State will be venturing into territory not visited by the State since 1887. A state government shutdown presents the immediate question of how to mitigate the resulting hardships and frustrations that will result from a shutdown in the 21st century. The executive, judicial, and legislative departments provide a vast array of services to businesses and individuals each day. Nearly all these services will likely come to a halt on July 1, 2009, if there is no budget by that date.

If the General Assembly does not enact a budget, there will be a tremendous shift of responsibility to the executive department and, likely, the judicial department to determine how much, if any, money in the state treasury the executive may use to provide those services citizens will be expecting. In addition to the constitutional prohibition on using the state treasury, IC 4-13-2-18, concerning the procedures for making a payment from the state treasury, provides in part:

"[e]very expenditure or obligation authorized or incurred in violation of the provisions of this chapter shall be void. Every payment made in violation of the provisions of this chapter

shall be illegal, and every official authorizing or making such payment, or taking part therein, and every person receiving such payment, or any part thereof, shall be jointly and severally liable to the state for the full amount so paid or received."

Because of this emphatic expression of legislative intent and potential personal liability for the State Auditor and Treasurer, the Auditor, Treasurer, or Governor may immediately seek judicial review of their authority to pay money from the state treasury even for immediate public safety and health needs. They may also be named a defendant in cases brought by those affected by a shutdown. The courts may also be asked to address a myriad of other issues in such a case.

II. Basic Principles Restated

For ease of reference, the primary Indiana Constitutional provisions and case law we discussed in the 1993 memo are the following:

- Article 3, Section 1 of the Constitution of Indiana. "The powers of the Government are divided into three separate departments; the Legislative, the Executive including the Administrative, and the Judicial: and no person, charged with official duties under one of these departments, shall exercise any of the functions of another, except as in this Constitution expressly provided."
- Article 10, Section 3 of the Constitution of Indiana. "No money shall be drawn from the Treasury, but in pursuance of appropriations made by law."
- Carr v. State (1891, Ind.), 26 N.E. 778. In this case, the Court noted that the General Assembly has no authority specified in the Constitution to annul a contract it has legally entered into, but it may effectively block a just claim by failing to appropriate money for that claim.

"It may have the might and the means of defeating the enforcement of a contract, yet, in a just sense, have no power to do so. Might and authority do not constitute power in the true sense. To constitute power another element must be present, and that element is right. If right is absent there is no power. **Legislatures may, by a failure to make an appropriation, defeat a just claim, or, indeed, block the wheels of government;** but under the constitution they have no power to do any such thing." Id. at 779. (Emphasis added.)

"[T]here is no power that can coerce the legislature into making an appropriation, no matter how strong the justice of the creditor's claim, nor how plain the duty seems.... Whether an appropriation shall or shall not be made is a legislative question, and over purely legislative questions the courts have no supervision or control. A question of that character is beyond the touch of the judiciary, for one department of government cannot enter the domain of another." Id.

We want to emphasize that no Indiana case has held any Indiana constitutional provision to be a self-executing appropriation, unlike decisions by courts in other states holding they are self-executing (see discussion of the recent Kentucky case below). We have, however, enclosed a list of Indiana Constitutional provisions that include language creating duties.

III. 1993 Memo Update

First, we note that since the 1993 memo was written we have learned that the General Assembly has failed to enact a budget bill before the end of the fiscal year on four occasions, not just once as stated in the middle of page 6 of the 1993 memo. In addition to the failure in 1863 when Governor Morton ran the state on funding he personally obtained and never placed in the state treasury, the General Assembly also did not pass a general appropriation act in 1857, 1871, and 1887. See 8 I.U. Law Journal 341, which discusses the state's borrowing power. In 1887, borrowing was used by the executive and affirmed by the Indiana Supreme Court in Hovey v. Foster, 118 Ind. 502, (Ind. 1888).

As stated above, some continuing statutory appropriations listed in the 1993 memo have been amended or repealed since then and new statutory appropriations have since been enacted. These are mostly appropriations from dedicated funds. However, the total amount of these continuing statutory appropriations, especially continuing state general fund appropriations, is minor (except local taxes collected by the state) when compared to the appropriations for K-12 education, higher education, and Medicaid included in the budget bill. If you like, we will compile a new list of all continuing statutory appropriations.

The only code provisions that are specifically triggered by a failure to adopt a budget are IC 4-10-15-1 and IC 4-15-10-2. The General Assembly enacted this law in an 1869 special session. In brief, this law was a result of no budget being passed in 1857. The Treasurer then refused to pay warrants for operating five state institutions and the institutions closed and sent the residents back to their families or to the counties. The Treasurer was later convinced to pay to operate these institutions. However, in 1859, the General Assembly enacted a law creating a treasury system and specifically prohibited the payment of warrants by the Treasurer. See 8 I.U. Law Journal 341, 343-345, and Acts 1859, c. 138, p. 227, and Acts, 1861, c. 50, p. 112. The law addressing the failure to enact a budget has not been amended since 1869. IC 4-10-15-1 provides that:

"[w]henver there shall be a failure at any regular biennial session of the General Assembly to pass an appropriation bill or bills, making appropriations for the objects and purposes hereinafter mentioned [in IC 4-10-15-2 below], it shall be lawful for the Governor, Secretary and Treasurer of State, until appropriations shall be made by the Legislature, to direct the Auditor of State to draw his warrants on the State Treasury for such sums as they may, from time to time, decide to be necessary for such purposes respectively, not however exceeding the amounts appropriated for the same objects respectively by the last preceding appropriations which shall have been made by the General Assembly; and to pay such warrants as may, from time to time, be drawn and presented, a sufficient sum of money is hereby appropriated."

IC 4-10-15-2 provides that:

"[t]he warrants may be drawn for the necessary and current expenses of the following:

- (1) All psychiatric hospitals (as defined in IC 12-7-2-184).
- (2) The Indiana School for the Deaf, established by IC 20-22-2-1.
- (3) The Indiana School for the Blind and Visually Impaired, established by IC 20-21-2-1.
- (4) The Indiana Veterans' Home.
- (5) The Plainfield Juvenile Correctional Facility."

We believe IC 4-10-15-1 and IC 4-10-15-2 enhance the possibility that a court would limit the use of the state treasury for any purpose other than those specified in these statutes. That is, the court could find that not only is there the constitutional prohibition against drawing money from the state treasury except by appropriation, but more importantly, the General Assembly has in fact addressed the possibility of a failure to enact a budget and in that statute made appropriations and stated it is lawful to draw warrants to pay expenses for only five specific facilities. This is the only law that mentions "a failure at any regular biennial session of the General Assembly to pass an appropriation bill" and it provides for no other purpose.¹

IV. Update on Other States

A. Case Law

The most recent state supreme court decision on the failure to enact a budget was a 2005 decision in Kentucky. Kentucky had a general continuing appropriation law, but it was repealed effective January 1, 1983. Without any statutes like IC 4-10-15-1 and IC 4-10-15-2 that address no budget being enacted, the Kentucky Supreme Court decided on the constitutionality of an overall spending plan prepared by the Governor ("Public Services Continuation Plan"). Fletcher v. Commonwealth, 163 S.W. 3d 852, 871 (Ky. 2005). See enclosed materials from Kentucky.

The Governor chose to implement his Plan and not call a special session. In the Plan, the Governor continued the most recent year's appropriation levels across the entire state budget. The Plan was not limited to funding for emergency or public health and safety matters, such as operating prisons or providing state police protection.

Fletcher held the Plan unconstitutional, stating that Section 230 of the Commonwealth's Constitution should be given its literal meaning and that "[t]he Governor possesses no 'emergency' or 'inherent' powers to appropriate money from the state treasury that the General Assembly, for whatever reason, has not appropriated." *Id.* at 871.

¹ One item not mentioned in the 1993 memo is a practical concern that even if certain programs are supported by a statutory or continuing appropriation, there technically would be no appropriation for the staff necessary to carry out the actual payment. For example, without an appropriation and no staff, how would the State Budget Agency allot funds, how would the State Auditor issue warrants, and how would the State Treasurer pay any warrants that were issued? However, we believe it is more likely that a court would consider it proper and necessary for these agencies, as well as those agencies receiving continuous appropriations for programs, to have personnel funded from the state treasury, without an appropriation, so that the purposes for the statutory appropriations can be carried out. Otherwise, Article 1, Section 21 may be implicated. It provides that "[n]o person's particular services shall be demanded, without just compensation" In addition, Article 1, Section 37, provides that "[t]here shall be neither slavery, nor involuntary servitude, within the State, otherwise than for the punishment of crimes, whereof the party shall have been duly convicted."

Specifically regarding payrolls, SECTION 13 of the 2007 Budget Act, provides in part that "payroll for the period of the last half of June, . . . shall be charged to the appropriation for the succeeding year. . . ." The chief financial officer and general counsel of Connecticut indicated on June 2, 1991, that pay may end after the middle of June under a substantially similar provision in the Connecticut budget act. See enclosed New York Times Article. Connecticut went on to enact three two-week budgets.

On the other hand, Fletcher did recognize that the Kentucky Constitution created mandates that must be carried out regardless of an appropriation. Providing for the common schools was one of nineteen provisions where the court found that "these constitutional mandates must be implemented." Id at 867. The court said "[t]he General Assembly cannot prevent the implementation of constitutional mandates by simply withholding its appropriations power. In the absence of appropriations by the General Assembly, the Treasurer must fund these constitutional mandates at no more than existing levels until the General Assembly provides otherwise." Id at 867. (Emphasis added.) No authority is cited for these spending levels.

B. NCSL Survey of Other States

NCSL reports that several states have recently gone past their deadline for adopting a budget. (See enclosed NCSL report.) NCSL has categorized 43 states into three broad categories. NCSL classifies Indiana as a state where payments can continue only to the five institutions listed in IC 4-10-15-2, as noted above, and as a government "shutdown" state.

1. Temporary appropriation bills. Eleven states are in this category. Five of the seven state legislatures with late budgets in 2003 passed temporary appropriation bills.

2. Constitutional or other provisions or procedures ensure the continuous operation of government during an appropriation lapse. Twelve states are in this category. In California, for example, court rulings have allowed California to operate at funding at levels of the previous year. Indiana is listed in this category but only with regard to institutions listed in IC 4-10-15-2.

3. Government shutdown. Twenty states are listed in this category including Indiana. The most recent example of this was Tennessee's partial shutdown in 2002. NCSL said that during the time of the Tennessee shutdown, classes stopped at public universities, driver's licenses were not issued, and road construction ceased. However, many services such as public health, welfare, child support distributions, mental health, prisons and highway patrols all continued in Tennessee.

V. Specific Questions

In addition, you asked about the following:

(1) Does the Governor have authority to use the state treasury to operate state government generally so as to "take care that the laws are faithfully executed" or as a result of the 2007 Budget Act?

Because of those basic principles discussed in Section II, we believe the answer is no with respect to the day-to-day operation of most state agencies that are funded by a budget act.

² NCSL also reports that there are a variety of costs associated with late budgets, such as increased "operational costs." NCSL points out that "[s]tates may be subject to legal actions from employees or citizens because of lost wages. Without appropriation details, local government and nonprofit organizations are unable to budget, plan or deal effectively with their contractual obligations leading to secondary and tertiary costs to overall government operation. States also pay indefinable costs in terms of a decline in public confidence in elected officials, damage to the state's image and possible difficulty in future personnel recruitment."

In addition, the following statutes and noncode provisions of the 2007 Budget Act suggest that the Governor does not have the authority to require that the state treasury be used for the day-to-day operation of state government.

The 2007 Budget Act provides in SECTION 1 that "Biennium" means the period beginning July 1, 2007, and ending June 30, 2009. SECTION 2 states that "the following sums in SECTIONS 3 through 10 are appropriated for the periods of time designated." Nothing in SECTIONS 3 through 10 of the 2007 Budget Act appropriates operating funds beyond June 30, 2009.

IC 4-13-2-19 provides that "(a) Except as specifically provided for in appropriation acts, every appropriation or part thereof remaining unexpended and unencumbered at the close of any fiscal year shall lapse and be returned to the general revenue fund." (Emphasis added.)

Operating appropriations are generally categorized into broad categories. These operating appropriations and distributions for K-12, vocational education, and higher education cover only fiscal years 2008 and 2009. Below is a brief summary of the operating appropriations by category:

General Government

For the most part, general government operates on general fund appropriations and not continuing appropriations. Thus, on July 1 there would be no appropriation to compensate the staff of practically every state agency in the legislative, judicial, and executive, including the administrative, departments. In addition, local courts and prosecutors receive a substantial appropriation in the budget act. Most importantly, these agencies include the State Police and the Department of Correction.

K-12 Education

Tuition support distributions are specifically appropriated in the 2007 Budget Act, so no funds for distributions would be available after June 30, 2009. This is also the case for other K-12 programs.

Higher Education

Operating, repair and rehabilitation, and fee replacement for debt service are specifically appropriated for the 2008 and 2009 state fiscal years and thus no money will be available after June 30, 2009, if no budget is enacted.

Vocational Education

IC 22-4.1-3-4 requires that federal funds be specifically appropriated. It states:

"[f]unds necessary to support the operating costs of the department of workforce development beyond those approved and appropriated by the United States Congress or approved by federal agencies for the operation of the department and specifically authorized by other provisions of IC 22-4:

(1) must be specifically appropriated from the state general fund for this purpose;"

This specific appropriation is made by SECTION 11 of the 2007 Budget Act.

Medicaid

The federal money for Medicaid is appropriated by SECTION 26 of the 2007 Budget Act. It provides

that "[t]he governor of the state of Indiana is solely authorized to accept on behalf of the state any and all federal funds available to the state of Indiana. Federal funds received under this SECTION are appropriated for purposes specified by the federal government, subject to allotment by the budget agency. . . .". This SECTION does not expire.

However, Medicaid state matching payments are specifically appropriated and therefore, if no budget is enacted before July 1, no money would be available to make the state match after June 30, 2009, which potentially could jeopardize the State's participation in the Medicaid program.

Highways

Highway operating and lease rental payments are specifically appropriated either from the highway fund or the general fund and no money would be available after June 30, 2009, if no budget is enacted.

Debt Service

No appropriation would exist for payments on the leases for the Government Center North, Government Center South, State Museum, McCarty Street Warehouse, Parking Garages, Toxicology Lab, Wabash Valley Correctional, Rockville Correctional, Miami Correctional, Pendleton Juvenile Correctional, New Castle Correctional, Regional Health Care Construction Account, Evansville State Hospital, Southeast Regional Treatment, and the Logansport State Hospital.

The few exceptions to the requirement of an appropriation for spending after June 30th include the five institutions and other continuing statutory appropriations mentioned above. SECTION 1 of the 2007 Budget Act provides that "[a]ppropriations appearing in the biennial column for construction or other permanent improvements do not revert under IC 4-13-2-19 and may be allotted." This provision does not expire. Also, IC 4-13-2-19(b) provides an exception for "special taxes, fees, earnings, fines, federal grants, or other sources which are by law appropriated for special purposes by standing, continuing, rotary, or revolving appropriations." We consider these to be references to continuing statutory appropriations. SECTION 26 of the 2007 Budget Act provides a continuing appropriation of federal funds.

(2) ~~If the Governor does not have general authority to use the state treasury, does the Governor have emergency power to use the state treasury to protect the public health and safety so that the "public order [is] maintained"?~~

~~We believe the answer is no.~~

Protection of the public health and safety are carried out for the most part with budget act appropriations to general government agencies such as the State Police, the Department of Correction, the Department of Homeland Security, and the Department of Health.

The executive or judicial department would have to find a constitutional or statutory mandate that supersedes the necessity for an appropriation. As we stated in the 1993 memo and emphasized above, the Indiana courts have not yet found such a mandate.

(3) Do any "language" provisions in the 2007 Budget Act that are critical to understanding the intent of certain appropriations (such as required reviews, determination of amounts, and other guidance etc.) expire June 30, 2009?

Generally, language below the appropriations in the 2007 Budget Act does not explicitly expire. Although the appropriations are "for the periods of time designated", we believe the language will apply after June 30, 2009, but only for money appropriated from the specific corresponding appropriation.

There are only three explanatory language provisions in the 2007 Budget Act that specifically expire before January 1, 2010. (See enclosed.)

(4) What was identified in 2009 legislation as imminent situations that would occur if no budget is enacted before July 1, 2009?

- Budgeting by schools for 2010 begins in July and the school formula expires December 31, 2009. Local governments also depend on the Department of Local Government Finance in formulating their budgets. The local budget process starts in July.
- IC 20-40-8-19 permits the use of the school capital projects fund for utility services and property or casualty insurance with a limit on the amount for 2009. This section does not expire but the section does not provide a limit after 2009.
- FSSA expires.
- Virtual school provisions.
- Interest forgiveness for loans to charter schools.
- Delay of the July 1, 2009, start of the general reassessment.
- Delay of state fiscal year budgeting for school corporations.
- Technical fixes to HEA 1001-2008, including referenda on controlled projects.
- Reauthorization of the Quality Assessment Fee, which has already expired.

(5) May a school corporation borrow against future state distributions?

We believe that under IC 20-48-1-9 a school corporation, in an emergency, may borrow in anticipation of receipts from the state. This section provides that:

"(a) If the governing body of a school corporation finds and declares that an emergency exists to borrow money with which to pay current expenses from a particular fund before the receipt of revenues from taxes levied or state tuition support distributions for the fund, the governing body may issue warrants in anticipation of the receipt of the revenues.

(b) The principal of warrants issued under subsection (a) is payable solely from the fund for which the taxes are levied or from the school corporation's general fund in the case of anticipated state tuition support distributions. However, interest on the warrants may be paid from the debt service fund, from the fund for which the taxes are levied, or the general fund in the case of anticipated state tuition support distributions.

(c) The amount of principal of temporary loans maturing on or before June 30 for any fund may not exceed eighty percent (80%) of the amount of taxes and state tuition support distributions estimated to be collected or received for and distributed to the fund at the June settlement.

(d) The amount of principal of temporary loans maturing after June 30 and on or before December 31 may not exceed eighty percent (80%) of the amount of taxes and state tuition support distributions estimated to be collected or received for and distributed to the fund at the December settlement. ... ". (Emphasis added.)

(6) Does the noncode bonding authorization for a capital project in a previous budget act expire?

We believe the answer is no.

There is no explicit expiration attached to the provisions that have authorized the issuance of bonds. Indiana law does not recognize a general rule that an implied repeal occurs when another act is adopted on the same general subject. We do not believe the most recent list of authorized capital projects would be considered a cumulative list, thus, superseding or canceling previous authorizations. If this were the intent, we would typically draft such a provision to be as specific as possible in describing the cancellation of any previous authorizations. We also believe an implied repeal of all things in a previous budget act by the enactment of a subsequent budget act would be new legal territory in Indiana that would go well beyond the bonding authorization provisions.

(7) What should be part of a "temporary appropriation" measure?

A temporary appropriation measure would have to be in a bill and not a resolution. Such a measure should include at least a statement on how much is being appropriated and specify a time period. However, it could be very specific and provide an amount for each agency for the specified period as well. It might also include "language" providing guidance on how particular appropriations are to be administered. See enclosed list of considerations for a temporary appropriation measure and "language" from the 2007 Budget Act.

Other states have dealt with their budget deadlines by making temporary appropriations. In 1991, Connecticut passed three two-week budgets in which actual dollar amounts were specified by line item. In 2002, Tennessee enacted the "Essential Government Services Act of 2002" to fund state government for the fiscal years beginning July 1, 2001 and July 1, 2002. Minnesota has also passed temporary appropriation measures. We have included copies of these enactments. Other states have also enacted such measures.

VI. Conclusion

We believe NSCL's characterization of Indiana as a "shutdown" state is appropriate. This belief is based on the following:

- (1) the basic principles that Indiana government is divided into three separate departments and "no person, charged with official duties under one of these departments, shall exercise any of the functions of another";
- (2) that "[n]o money shall be drawn from the Treasury, but in pursuance of appropriations made by law";
- (3) Indiana Code provisions specifically addressing what occurs in the case of a failure to enact a budget;
- (4) the emphatic expression of legislative intent that it is illegal for the Auditor or Treasurer to use money in the state treasury except pursuant to an allotment by the budget agency that is supported by an appropriation; and
- (5) the Carr case holding that the General Assembly may effectively block a "just claim" by not appropriating money for that claim.

The State will be venturing into territory not visited by the State since 1887 if the General Assembly does not provide money to operate state government. The executive is therefore likely to seek judicial review, which will shift responsibility to the executive and judicial departments to determine if there are any

mandated constitutional duties of the executive or judicial department that create a self-executing appropriation thereby making a legislative appropriation unnecessary. If so, the executive and judicial department will have to determine how much money in the state treasury the executive may use to provide the services the citizens will be expecting.

We hope that this memo is helpful. Please let us know if you have questions or need any additional information.