



Default Budget FAQ September 2018

Up until recently, the law provided that in Official Ballot Referendum (“SB 2”) towns, the default budget is “the amount of the same appropriations as contained in the operating budget authorized for the previous year, reduced and increased, as the case may be, by debt service, contracts, and other obligations previously incurred or mandated by law, and reduced by one-time expenditures contained in the operating budget.” RSA 40:13, IX (b). The statute went on to define “one-time expenditures” as “appropriations not likely to recur in the succeeding budget, as determined by the governing body.”

This sounds simple enough: the default budget is supposed to be the same budget as last year, with certain amounts added or increased as required by the statute. However, terms such as “contracts previously incurred by law” or what really constitutes an expense “not likely to recur” created ambiguity when calculating the default budget. Indeed, in some towns and districts, tensions rose when the default budget frequently exceeded the proposed operating budget for a given year.

As a result, several amendments were made to RSA 40:13 in 2018. This Q&A looks at the law in its new form and provides suggestions for handling your default budget going forward.

What changed in 2018?

In a nutshell, between House Bill 1307 and Senate Bill 342, the Legislature revised the definition of “default budget,” created more specific requirements for what may and may not be included in the default budget, and mandated new notice and transparency requirements.

How will our calculation of the default budget change with these new amendments?

Calculation of the default budget still starts with last year’s budget; the question is which amounts must be taken out, and which amounts that were not included in last year’s budget can be added. As stated above, last year’s budget must be reduced or increased “by debt service, contracts, and other obligations previously incurred or mandated by law, and reduced by one-time expenditures contained in the operating budget.” RSA 40:13, IX (b). Some of this is easy. For example, an

obligation “mandated by law” would be something like the county tax, which municipalities are obligated to pay.

What amounts must be taken out of last year’s budget?

Even prior to the 2018 amendments, RSA 40:13, IX(b) required last year’s budget to be *reduced* by one-time expenditures. The amendments now also require the budget to be reduced by “by salaries and benefits of positions that have been eliminated in the proposed budget.”

What is a one-time expenditure?

“One-time expenditures” are “appropriations not likely to recur in the succeeding budget, as determined by the governing body.” For example, let’s say the town included money in the maintenance line of last year’s operating budget to install new windows in the town hall. Since the window installation was a discrete project that occurred last year, and not something to recur annually (i.e., the town hall doesn’t get new windows every year!), that amount constitutes a one-time expenditure that must be taken out to calculate the default budget.

What employment positions are “eliminated” and must come out of the default budget?

As stated above, the statute now requires last year’s budget to be reduced “by salaries and benefits of positions that have been eliminated in the proposed budget.” It goes on to say that “eliminated positions shall not include vacant positions under recruitment or positions redefined in the proposed operating budget.” So, let’s say your town had an Assistant Public Works Director who retired, and a decision has been made that the position would not be filled—essentially, the position was discontinued when that employee retired. The amount of money in last year’s operating budget that represents the salary, benefits, and costs associated with that position would not be included in the upcoming year’s default budget.

However, if the town intended to fill the Assistant Public Works Director position, but it was just vacant while a search was conducted, the amount of money associated with that position would be included in the default budget.

What about multi-year contracts? More specifically, if the governing body signs a multi-year contract, does the amount for each year automatically get included in the default budget?

HB 1307 also added new subparagraph (c) to RSA 40:13, IX to define the term “contracts” in the default budget definition. This amendment addressed one of the most hotly-debated questions related to the default budget—when the governing body enters into a multi-year contract, can the costs associated with the contract automatically be included in next year’s proposed operating budget *and* next year’s default budget?

This new amendment specifically states that the term “contracts” means “contracts previously approved, in the amount so approved, by the legislative body in either the operating budget authorized for the previous year or in a separate warrant article for a previous year.”

The easiest way to conceptualize this is to put the definition into context.

Take, for example, a waste-hauling contract renewal for a term of three years that the select board signed. Assume the annual amount increases by 10% in year two and 15% in year three. A warrant article could be presented to the voters asking for approval of the entire three-year term, which would include: (1) the purpose of the contract; (2) the term of the contract; (3) the amount to be spent for each year of the contract; and (4) the total amount to be spent over the term of the contract. If that warrant article for the hauling contract is approved, then the three-year hauling contract is a contract “previously approved, in the amount so approved by the legislative body . . . in a separate warrant article.” In the subsequent years’ default budgets, the full amounts (with the increases) may be included in the default budget.

On the other hand, the definition also says that a contract may be approved in the operating budget for the previous year. Look at the hauling agreement again and assume the select board did not present the agreement to the voters in a separate warrant article, but as an appropriation for the purpose of paying the hauling contract included in a line item in the operating budget. In that case, when calculating next year’s default budget, the same amount that was included last year for the hauling contract will be included in the default budget—not the increased amount in the contract.

What are the risks associated with putting the full term of the contract to the voters in a separate warrant article?

The most obvious risk is triggering “no means no.” The voters could vote down the separate warrant article to approve the multi-year agreement and appropriations. When a separate article containing an appropriation is rejected by the voters, it generally means that no money can be spent on the purpose stated in that warrant article. In this context, the voters’ rejection of this article may bring up difficult questions: Have the voters rejected spending any money at all on a hauling contract? Or have they simply rejected the increased amounts in future years? A well-crafted warrant article may help reduce these risks, should the voters reject the article, so that the purpose of spending (e.g., spending any money on waste hauling) is not prohibited by a “no” vote on the article.

What are the risks associated with putting the amount in the operating budget?

There is nothing wrong with this approach—and since there are many types of multi-year agreements signed by the select board, this is often the most efficacious approach—but it does mean that the default budget cannot include the increases that the select board may be on the hook to pay; the budget includes only the same “base” amount as included last year. Let’s go back to the hauling contract: Assume the 2017 budget contained \$100,000 for waste hauling. At the end of 2017, the select board signed a renewal for a contract period of three years: \$105,000 for 2018; \$108,000 for 2019, and \$110,000 for 2020.

What amount goes into the 2018 default budget? The answer, based on the new definition of “contracts,” is \$100,000. The reason? The 2018 default budget is based on the 2017 operating budget, and the 2017 budget contained \$100,000. Therefore, the voters approved the amount of \$100,000 for waste hauling. The default budget should contain \$100,000 and not \$105,000, but your proposed operating budget should contain \$105,000. Don’t panic—keep reading!

But WAIT! Are you saying we're prohibited from paying the annual increases in multi-year agreements signed by the select board? What about salary increases included in an employment contract?

Absolutely not! Remember that the select board has the authority to spend money and the authority to transfer funds from one purpose to another. This authority applies to a default budget as well as an approved proposed operating budget—both are bottom line budgets.

Let's go back to the hauling contract in the question above, where the select board did not submit the contract to the voters in a separate warrant article, and where the 2017 budget contained \$100,000 for waste hauling. We said that the 2018 default budget can contain only the \$100,000—as approved in last year's operating budget—not the \$105,000 contained in the new contract signed by the select board. But the select board can still pay \$105,000 for waste hauling in 2018, even if the town ends up with the default budget. This is because the budget—whether an adopted operating budget or a default budget—is a bottom line budget, and the select board has the authority to transfer from line to line. The board must find the additional \$5,000 elsewhere in the budget. This, of course, means that another area of the budget may suffer, but this is part of the reality of being in a default budget year.

The same rules apply to employment contracts that contain annual salary increases, which is another commonly-debated issue with default budgets. Take, for example, an employee whose salary plus benefits in the 2017 budget was \$100,000 (with a \$50,000 salary). But let's say the select board had also entered into an agreement to pay this employee a 10% increase in the subsequent year. For the 2018 default budget, the board cannot include \$105,000 (\$55,000 increased salary plus benefits); it can put in just the \$100,000 approved by the legislative body in the 2017 budget. That doesn't mean the \$55,000 salary can't be *paid* to the employee—but it does mean that the board will need to move money around to “find” that extra \$5,000. Of course, just like any other multi-year agreement, the select board could ask the voters to approve the full term of the employee's contract, including the pay increases, in which case the pay increases would be included in the default budget.

In fact, while these amendments to RSA 40:13 were pending in the legislature, a judge in the Hillsborough Superior Court, Northern District, found that annual salary increases included in an employment contract, entered into between a town employee and the select board, could not be included in future years' default budgets. *Neal Kurk v. Thomas Clow, et. al*, Docket No. 261-2018-CV-00086. The select board had put into the default budget about \$60,000 worth of salary increases. These increases were the result of various agreements between the board and certain employees. Neither the contracts nor the amounts in the contracts (i.e., the annual increases above and beyond the salary amounts in last year's budget) had been approved by vote of the legislative body. The judge determined that because the appropriations in the contract were not previously approved by the voters, these amounts did not constitute “contracts . . . previously incurred by law.” HB 1307 confirms that ruling by requiring that the amount of money in a contract must be previously approved by the voters through the annual meeting budget process to be included in the default budget.

Although this order came out before the current amendments went into effect, we believe the case represents the intent behind the amendment—that it was targeted at preventing the “unapproved increases” from being put into the default budget by clarifying that contracts must be approved by the legislative body for those amounts may automatically be included in the default budget.

Of course, approved collective bargaining agreements, and the cost increases included therein, are always included in the default budget because those contracts are approved by the voters separately.

Is our default budget per se incorrect if it's more than the proposed operating budget?

No. SB 342 finally settles the question whether the default budget may be higher than the proposed operating budget by amending RSA 40:13, IX(b):

In calculating the default budget amount, the governing body shall follow the statutory formula which may result in a higher or lower amount than the proposed operating budget.

Therefore, as long as the default budget is calculated correctly, it is not “wrong” because it is higher than the proposed operating budget for the year.

What additional disclosure to the public is required?

HB 342 amplifies the notice requirements for the default budget. Adding onto the long-standing requirement that the default budget be disclosed at the first budget hearing, RSA 40:13, XI(a), as amended, further explains the default budget must be “presented for questions and discussion at that hearing,” although many towns and districts already do this. The form used for presenting the default budget must now include the “specific items that constitute a change by account code, and the reasons for each change,” as well as “reductions for eliminated positions and benefits.” Towns and districts will be required to make the “line item details” for these changes available for inspection by the voters.

Since the default budget cannot be amended by the voters, is it “off limits” for discussion at the deliberative session?

HB 1307 has clarified the default budget’s role at the deliberative session. RSA 40:13, IV will now expressly permit voters to discuss and debate the default budget, along with other articles on the warrant. That being said, RSA 40:13, XI(b) still prohibits the voters from *amending* the default budget at the deliberative session.