

Introduction

The FY 2019 budget adjustments that Governor Malloy is recommending today are a reaffirmation of his administration's longstanding commitment to balancing budgets, reducing long term liabilities, and grappling with the profound fiscal mess that Connecticut spent decades amassing, and now has spent almost eight years cleaning up.

This budget is about the future, but deals forthrightly with the present.

The adjustments to the bipartisan biennial budget agreement recommended here will address the immediate challenge created by the reduced consensus revenue forecasts since the budget was adopted. The budget adjusts spending to ensure there are adequate resources to meet the legal and moral requirements of state government. The recommendations offset new spending and revenue shortfalls with spending cuts, cancelled tax cuts, and some new revenues. As always, these are difficult decisions, and the recommendations are made simply because we must balance our budget.

The basic framework of the bipartisan budget remains intact in this proposal. The nearly \$1.09 billion in lapses that were included in the budget agreement for FY 2019 have largely been allocated to agency accounts. Spending reductions are mainly in the form of further reductions to areas already identified by the legislature for reduction in the bipartisan agreement. Revenue changes build on the changes in that budget as well. The few spending increases included are largely technical adjustments intended to ensure adequate resources to meet caseload or other service needs.

There are several small expansions to ensure transitions to the community continue under the Money Follows the Person program in the Departments of Social Services (DSS), Developmental Services (DDS), Mental Health and Addiction Services (DMHAS) and Housing (DOH), to fund emergency placements in DDS, to enhance inmate nutrition in the Department of Correction (DOC), and to stabilize Community Colleges during their ongoing restructuring. Some minor modifications to two newly created funds – Passport to the Parks and the Tourism Fund – are recommended to ensure the original legislative intent can be carried out.

More details regarding all these changes follow.

Addressing the Structural Deficit Created by Bipartisan Budget Agreement

In addition to the adjustments necessary to bring the FY 2019 budget into balance, the Governor's recommended revisions include changes that are designed to significantly reduce the structural deficit created by the bipartisan budget agreement and to comply with section 658 of Public Act 17-2 (June Special Session). In short, we recommend repealing the unaffordable promises of future tax cuts, future program restoration, and future spending growth included in the bipartisan budget.

The fiscal note to the bipartisan budget agreement included the following table showing out-year budget projections, assuming spending continues at budgeted levels plus inflation, and various revenue or other provisions of the law are carried out:

FY 2020 – FY 2022 Fund Balance (in millions)

| | FY 20 \$ | | | FY 21 \$ | | | FY 22 \$ | | |
|--------------|----------|----------|-----------|----------|----------|-----------|----------|----------|-----------|
| | Approp | Revenue | Balance | Approp | Revenue | Balance | Approp | Revenue | Balance |
| General Fund | 19,708.5 | 17,786.7 | (1,921.8) | 20,548.0 | 17,882.4 | (2,665.6) | 21,187.9 | 18,008.3 | (3,179.6) |

Source: Office of Fiscal Analysis. Fiscal note on Senate Bill No. 1502 (Public Act 17-2, JSS), October 25, 2017.

The projected General Fund deficits of \$1.9 billion, \$2.7 billion and \$3.2 billion are staggering, but are mostly the result of provisions in the bipartisan budget agreement that require restoration of \$340 million in municipal aid, a \$516 million tax break for hospitals (and assumptions that supplemental payments and rate increases would be maintained at the FY 2019 level), and tens of millions of new tax cuts, all in 2020. Those structural holes (see table), coupled with a legislative projection of five percent spending growth that year, explain why the future-year deficit projections appear so large. They also show a clear path to addressing those deficits – a path this budget recommends.

| <u>Structural Holes (in Millions)</u> | <u>FY 2020</u> | <u>Maximum Outyear Impact</u> |
|--|-----------------------|--------------------------------------|
| Impact of non-recurring revenues | \$ (213.1) | \$ (213.1) |
| Property tax credit restoration in FY 2020 | (55.3) | (55.3) |
| Pension/annuity exemption - new PIT exemption | (24.6) | (106.8) |
| STEM credit - new PIT credit of \$500 | (3.9) | (19.7) |
| Teachers Retirement exemption restoration in FY 2020 | (8.0) | (8.0) |
| MRSA restoration in FY 2020 | (343.3) | (343.3) |
| RPIA restoration in FY 2020 | (11.0) | (11.0) |
| Car sales tax to STF commences FY 2021 | - | (360.0) |
| Gift and Estate Tax phase-in of federal exemption levels and \$15M cap | (39.5) | (62.3) |
| Smart Start restoration in FY 2020 | (10.0) | (10.0) |
| Tobacco and Health Trust Fund restoration in FY 2020 | (6.0) | (6.0) |
| Hospital Tax reduced in FY 2020 | (516.0) | (516.0) |
| Total Structural Holes | \$ (1,230.7) | \$ (1,711.5) |

These structural holes are self-inflicted wounds. The bipartisan budget includes multiple examples of large revenue diversions scheduled in law to occur in the future; tax cuts planned to take effect in FY 2019 and beyond; and one-time revenues used to balance the budget without making hard choices about revenue and spending. Compare this with 2010. That year, with the Great Recession hanging over the state, the Office of Policy and Management’s (OPM) structural holes calculation added up to \$2.4 billion, including use of one-time stimulus funding, securitization, transportation fund sweeps and the like. These problems stemmed from the crippling recession, not from legislation promising future benefits with no way to pay for them as we have today. If we as a state realistically face our budget challenges, and stop making promises we cannot afford to keep, our problems look much easier to solve.

| GENERAL FUND OUTYEAR BUDGET PROJECTIONS | | | |
|--|-----------------|-----------------|-----------------|
| (\$ in millions) | | | |
| | <u>FY 2020</u> | <u>FY 2021</u> | <u>FY 2022</u> |
| <u>Bipartisan Budget (PA 17-2, JSS)</u> | | | |
| Revenue (January 2018 consensus) | 17,510.1 | 17,612.9 | 17,753.5 |
| Appropriations (per OFA fiscal note) | <u>19,708.5</u> | <u>20,548.0</u> | <u>21,187.9</u> |
| Projected Deficit | (2,198.4) | (2,935.1) | (3,434.4) |
| <u>Governor's Recommended Revisions</u> <i>(See Note)</i> | | | |
| Revenue | 18,708.6 | 18,870.3 | 19,045.4 |
| Appropriations | <u>19,552.7</u> | <u>20,375.2</u> | <u>20,988.7</u> |
| Projected Deficit | (844.1) | (1,504.9) | (1,943.3) |
| Outyear Balance Improvement | 1,354.3 | 1,430.2 | 1,491.1 |
| <p>Note: Office of Policy and Management projection of outyear impacts of recommended revisions to the enacted budget for FY 2019. Because budgets are adopted for a biennium at a time, this forecast does not necessarily reflect the policy proposals that will ultimately be adopted for years beyond the current budget period.</p> | | | |

The budget adjustments recommended by Governor Malloy eliminate many future-year commitments that are not affordable based on our current revenue projections. The result is that projected out-year deficits are significantly reduced from the levels estimated when the bipartisan budget passed. While the out-years will still prove challenging even if all of the proposals in this budget are implemented, adopting the common-sense approach offered by Governor Malloy will make the next few years easier for future governors and legislatures, and more importantly, for Connecticut residents.

A Long-Term Approach to Strengthening the Connecticut Economy

The Governor’s recommended budget adjustments do much more for Connecticut’s future than simply undoing the unrealistic promises made in last year’s budget. This budget builds on a strategy the Governor has pursued over two terms to strengthen the economy while addressing state fiscal problems. This approach requires that Connecticut balance these often contradictory goals:

- Balancing the budget has required the state to downsize its workforce, which reduces the number of jobs in the state for Connecticut workers;
- Lowering investment return assumptions for pension funds reduces the risk of future unfunded liability, but increases the nominal value of those liabilities right away;
- Raising revenue for government activities means that less income is available for private investment; and
- Borrowing capital funds for infrastructure, for housing, or for economic development in order to grow the economy adds to long-term liabilities while other policies are in place to reduce those liabilities.

In finding balance between these goals, the Governor's strategy embodies a patient approach that will allow for gradual resolution of long-term liabilities including debt, pension liability and retiree healthcare, coupled with an urgent demand for short-term actions that balance the budget each year with recurring solutions, not one-time gimmicks. This will allow for the state to make demonstrable progress without causing the economic harm that could come from an effort to fix everything all at once by dramatically increasing revenue or cutting spending in a short period of time. Because of the long-term orientation of this approach, many do not appreciate how well it is working.

Over the last year or more there has been considerable debate in the legislature, the press, and among interested citizens about the seemingly intractable fiscal problems facing the state. Very large long-term liabilities, slow growth rates for our largest revenue streams, and weak or mixed signals on basic economic indicators have combined to create the impression among many that either nothing is being done or, worse, that nothing we do makes any difference. This frustration is understandable, and has led to many calls for radical solutions that promise immediate relief. But we should not turn our backs on well-considered long-term strategies simply because they do not offer instant gratification.

In reality, the all-bad-news story of Connecticut's finances that is told around the state – in newspapers, in electoral debates and at kitchen tables – is incomplete. Sometimes it simply reflects Connecticut's instinctive caution. Sometimes negativity about Connecticut serves some political aim.

The truth is that we have made significant progress down a long, long road but there is more road ahead of us yet to cover. We have not recovered jobs lost in the last recession as well as other states, but we have recovered, and our unemployment rate is a low 4.6 percent. We are not growing in population, but this is the result of factors including both domestic out-migration and reduced birth rates, offset by strong international in-migration, including thousands of well-educated immigrants who are helping our economy to thrive. The growth in the state economy has been slower than the national rate in recent years, but surged above the national average in the third quarter of 2017. We have had good news from large firms like Electric Boat which has passed 16,000 employees for the first time in 25 years, or Aetna, which has elected to retain its headquarters in Connecticut. And in place of headlines about Connecticut firms leaving because of the state pension liabilities, we see stories about those same firms' own growing pension debts. At the end of the day, Connecticut is still one of the richest, best educated, and most productive places in the world, and our future is bright, especially if we maintain continuous effort to pay down debts, invest in our future, and honestly balance our budgets.

Our business sector is strong and strengthening. State budget action can certainly impact both business and consumer confidence in the short-term, but ultimately it is the long-term decisions the state makes that have the most impact on our state's economy. If we want a strong economy, we should continue to follow the plan Governor Malloy has laid out over two terms:

- Invest in transportation infrastructure;
- Invest in our people through education and healthcare;
- Pay down long-term liabilities over time;
- Save costs by reducing staff, reducing future pension commitments, implementing technology and redesigning government services; and
- Balance the budget every year without relying on one-time measures and gimmicks.

Investing in Transportation Infrastructure

Since Governor Malloy first took office in 2011, he has continuously emphasized the critical importance of investing in Connecticut's transportation infrastructure. Connecticut has one of the oldest highway systems in the country, a system that had been inconsistently maintained and had often fallen into disrepair or obsolescence. Governor Malloy has always understood that for the safety of our citizens and the future strength of our economy, Connecticut must reverse this lack of investment in our economic arteries and turn this weakness into a strength.

In February of 2015, Governor Malloy released the \$100 billion, 30-year transportation plan known as *Let'sGoCT!* After working with residents, businesses and stakeholders all across the state, the Governor released this bold vision for a first-in-class transportation system, two-thirds of which is dedicated to simply upgrading our transportation infrastructure to a state-of-good-repair. The additional projects and initiatives represent important, strategic investments that will decrease congestion, help attract and retain a highly talented workforce, ease movement of people and goods, improve quality of life, and position Connecticut for sustained economic success.

This renewed focus on Connecticut's infrastructure has already resulted in major accomplishments over the past seven years – across all modes of transportation and regions of the state – that will continue to bolster our state's economy for years to come. Investments in our airports, our marine ports and harbors, transit-oriented development (TOD), brownfields, and our surface transportation infrastructure and transit systems are already bearing fruit. We have also completed construction of over 36 miles of multi-use trails for pedestrians and bicyclists.

The construction and replacement of the Pearl Harbor Memorial Bridge – the largest single infrastructure project in Connecticut DOT history – was completed on-time and under budget. We are utilizing innovative construction strategies such as the Accelerated Bridge Construction method used to replace two bridges on I-84 over a single weekend in 2014. The work to widen I-84 through the City of Waterbury is underway.

Serious investments in Connecticut's rail systems have occurred, including complete replacement of the catenary system that powers the New Haven Line and new M-8 rail cars for Metro-North's New Haven commuter rail line. These investments, among others, have resulted in a safer and more reliable rail system and record ridership on Metro-North. In 2018 Connecticut will open the new Hartford Rail Line that will connect New Haven to Hartford to Springfield, Massachusetts and is already spurring economic activities in communities all along the line.

Building on the work of prior administrations and our partnership with the federal government, Connecticut unveiled the state's first Rapid Bus Transit System, known as *CTfastrak*, in 2015. This award-winning, nationally recognized system has already surpassed seven million riders, with an average ridership of 19,000 people per week. In addition to providing transit options and flexibility for citizens who need to get to work, the grocery store, or the doctor's office, *CTfastrak* is galvanizing TOD across the system.

Even as the state continued to make these important investments over the past seven years, Governor Malloy acknowledged when he unveiled *Let'sGoCT!* that Connecticut would need to add more revenue to the STF to sustain the plan beyond a few years' ramp-up period. Moreover, a combination of factors such as technological advancements in transportation leading to declining fuel consumption, increasing debt

service, and falling oil prices have accelerated the need for additional funding in the STF. From 1997 to 2000, Connecticut decreased the gas tax by 14 cents, which has resulted in a cumulative loss of \$4 billion in the STF. More recently, the proliferation of electric and hybrid-electric vehicles and greater fuel efficiency have resulted in lower fuel consumption and less gas tax collected. In 2015 the price of oil fell drastically and has yet to recover. This sharp and unexpected decrease in oil prices, accelerated and exacerbated the STF's decreasing revenue to the point where we are today – in urgent need of new transportation funding strategies if we want to continue to make progress.

The choice before the State of Connecticut could not be plainer: raise more revenue for transportation so we can continue maintaining and improving our highways and transit systems. Or do nothing, and watch as the roads and bridges deteriorate, the fares on transit rise despite service cuts, and the state's economy withers.

It is important to note that some have accused Governor Malloy of “raiding” the STF during his tenure to affix blame for the current status of the STF rather than entertain real solutions. These claims of “raiding” are patently false. In fact, under the Malloy Administration, we have expanded the revenues that are dedicated to transportation, committing 100 percent of the Petroleum Products Gross Receipts tax to the STF over the course of 2014 and 2015 and thereafter, and diverting a half-penny of the sales tax to the STF. Given this expansion of STF revenues, coupled with overall budget constraint in the General Fund, in 2015 Governor Malloy called on the legislature to pass a constitutional “lockbox” to protect transportation-related revenue from being swept from the STF and diverted to the General Fund by the legislature or by future legislatures. In 2017, the legislature approved a statewide referendum on this constitutional lockbox, which is scheduled to go to the voters in November of 2018.

In addition to proposing the constitutional lockbox, Governor Malloy also convened the Transportation Finance Panel in 2015. After meeting over the course of nine months, that panel released its final report on January 15, 2016 highlighting the urgency of the issue and a variety of recommendations critical for supporting the STF. Other than passage of the lockbox, Connecticut's legislature has failed to pass a single one of the Panel's revenue generating legislative recommendations, such as increasing the gas tax and implementing all-electronic tolling. In fact, in 2017 the legislature passed a bill prohibiting the DOT from even studying one of the Panel's recommendations. This kind of backwards thinking needs to change if Connecticut is going to fix its ailing infrastructure and position itself for future economic success – our roads and bridges simply cannot fix themselves.

This budget proposal addresses Connecticut's long-term transportation infrastructure needs in a thoughtful and responsible manner. If these recommendations are adopted by the legislature, it will resolve the urgent, near-term revenue problem and ensure the future solvency of the STF. The proposal will also eliminate the need for the impending increases to bus and rail fares, the cuts to rail service, and the massive decrease in the DOT capital budget that will otherwise result in shutting down projects all across the state. This proposal will give Connecticut a future transportation system that is both strong and sustainable, just as the people and businesses of Connecticut deserve.

This budget proposal consists of a combination of expenditure reductions and five major revenue changes. First, the Governor's proposal calls for increasing the gasoline tax by seven cents over the course of four years (from 25 cents to 32 cents). Second, this budget would accelerate transfer of the motor vehicle sales tax to the STF by two years to help address immediate fund solvency needs. Third, the state would impose a new tire fee of three dollars starting in FY 2019. Fourth, the proposal would permanently eliminate

transfers to the School Bus Seat Belt Account beginning in FY 2020, an account that has never been used and is regularly swept for non-transportation purposes. And finally, the Governor's budget calls for Connecticut to institute statewide electronic tolling, which would begin in FY 2023. Highway tolling would help provide the funding necessary to fix some of Connecticut's largest and most expensive infrastructure projects, as well as other important highway projects necessary for easing congestion. Without tolls, Connecticut will never be able to afford these massive projects and the state, its citizens, and its economy will suffer the consequences. Moreover, tolls will finally ensure that motorists from other states pay their fair share when they pass through Connecticut.

Investing in Our People Through Education and Healthcare

Under the leadership of Governor Malloy, Connecticut has made meaningful and substantial progress improving public education from early education to higher education. Guided by the belief that the power of education can give every person an opportunity to succeed, regardless of their unique life circumstances, Connecticut has funded and developed policy for a public education system that prepares students to be college and career ready.

Since 2011, Connecticut has targeted substantial new state resources and efforts where they are needed most – to help students in Connecticut's chronically under-performing, highest-need districts and schools. Alliance Districts, the thirty lowest performing districts in Connecticut, have received millions of dollars in additional state investment, totaling over \$678 million since Governor Malloy launched the initiative. Additionally, the state has invested \$367 million through the Commissioner's Network program and Priority School District grants.

As Connecticut has made targeted and smart investments in education, high school graduation rates have reached record highs and improved for six straight years. Today, the statewide graduation rate is 87.4 percent, up nearly five points since 2011, and significantly above the national average of 84.1 percent. In the 2016-2017 school year, over 29,000 students took over 53,000 Advanced Placement (AP) exams – an increase of 24 percent from 2011-2012. Importantly, traditionally under-represented students are taking more AP exams than ever before. And, the number of chronically absent students in 2016-2017 is down over 1.5 percent from the 2012-2013 school year, indicating that over 10,000 more students are attending school regularly than five years ago.

Higher Education Expansion

Governor Malloy has championed the University of Connecticut (UConn) and the Connecticut State Colleges and Universities systems as important economic drivers for Connecticut with local businesses dependent upon their graduates for their workforce. College affordability and accessibility remain key issues as new demands are placed on higher education to prepare students with the knowledge and skills needed for 21st century jobs.

To best prepare for these challenges, Governor Malloy spearheaded the creation of a new Board of Regents governing body for the state college and university system bringing 17 schools under one umbrella, improving outcomes for students and streamlining functions to the benefit of faculty and staff. This transformation continues as efforts are made to consolidate duplicative functions at the university and community college level and maintain focus and funding on academics.

Further, Governor Malloy understands the importance of investing in UConn – our flagship university and a world class institution of higher learning. Under the Governor’s leadership, UConn has undertaken two different expansion efforts. First, the Governor introduced Bioscience Connecticut, an \$864 million investment in the UConn Health Center, improving UConn’s capacity for bioscience research and development. This investment also helped Connecticut land the acclaimed Jackson Laboratory for Genomic Medicine, co-located on the UConn Health Center campus. Second, Governor Malloy initiated Next Generation Connecticut, a transformative \$1.5 billion investment in UConn over ten years that has increased enrollment, specifically at the engineering school and among women pursuing Science, Technology, Engineering and Math (STEM) degrees. New science and lab space is under construction and a new state of the art dormitory complete with a makerspace and an idea lab is now open. Just last year, UConn reached number eighteen among *U.S. News & World Report’s* list of the nation’s top public universities – UConn’s highest ranking to date.

Health Insurance Exchange

Since taking office, Governor Malloy has been a national leader in the implementation of the Patient Protection and Affordable Care Act (ACA), which was signed into law by President Obama in 2010. One of the state’s major accomplishments under the ACA has been the development and implementation of Connecticut’s Health Insurance Exchange, known as Access Health CT. Connecticut applied for and received one of the first Health Insurance Exchange planning grants from the federal government and the resulting legislation in 2011 established the Exchange as a quasi-public agency. Under the leadership of Lieutenant Governor Nancy Wyman, who chairs the Access Health CT Board of Directors, Connecticut was one of the first states to develop a state-based Health Insurance Exchange with its successful launch in October of 2013. Since its initial open enrollment, Access Health CT has been successful in lowering the number of Connecticut residents without health coverage, helping to reduce the state’s uninsured rate by half to 3.8 percent in 2017.

In 2017, Access Health CT held its fifth open enrollment period which was undoubtedly its most challenging. Not only was the open enrollment period reduced to seven weeks from its traditional three month period, the continuing efforts of the Trump Administration to repeal the ACA confused consumers as to what action they should take. In spite of these challenges, the 2017 open enrollment was very successful with 114,134 Connecticut residents signing up for private health insurance through Access Health CT, a 2.3 percent increase from the previous year. In addition, Access Health CT assisted tens of thousands of Connecticut residents to enroll in Medicaid.

Connecticut was the first state to take advantage of the ACA’s Medicaid expansion opportunities by gaining approval from the federal government in June 2010 to expand Medicaid coverage to an estimated 45,000 low-income adults, who had been enrolled in a more limited health benefit package under the State Administered General Assistance program. Connecticut subsequently expanded Medicaid coverage for childless adults with incomes up to 138 percent of the federal poverty level effective January 1, 2014. Due to these Medicaid expansions, over 220,000 Connecticut residents now have access to Medicaid coverage.

Redesigning Medicaid and Controlling Costs

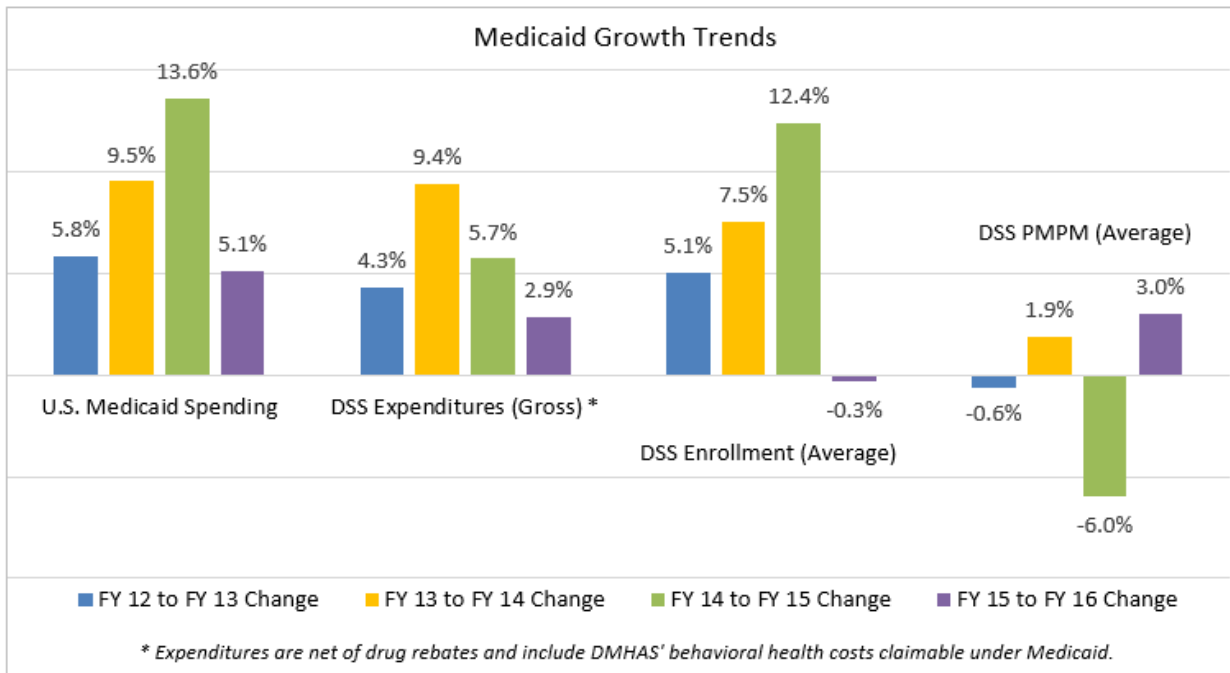
In contrast to the great majority of states, Connecticut moved away from capitated managed care contracts to a self-insured, managed fee-for-service model and launched the new HUSKY Health program

on January 1, 2012. In partnership with Administrative Services Organizations (ASOs) focused on medical, behavioral health and dental services, this self-insured model has been successful on all fronts with improved client care experiences, quality of service and overall cost-effectiveness.

This model has not only streamlined administrative costs, but the extension of state-of-the-art managed fee-for-service to the entire Medicaid and Children's Health Insurance Program population has allowed for a fully integrated set of claims data for over 800,000 covered individuals and has resulted in better health outcomes. HUSKY Health uses data analytics to direct policy-making, program development and operations and employs predictive modeling to identify members in present need of care coordination, as well as those who will need it in the future.

These efforts improve health outcomes while controlling costs. Access to care and provider participation has also increased as a result of targeted investments in prevention, practice transformation, and timely payment for services provided. Under the Malloy Administration, Connecticut has taken advantage of many opportunities available under the Affordable Care Act, maximizing the use of federal funds whenever possible. By coordinating and integrating care, re-balancing long-term services and supports and moving toward value-based payment approaches, HUSKY Health's financial trends compare very favorably with national Medicaid trends.

While total expenditures have increased due to increases in enrollment, per member per month costs have remained remarkably steady over time. *Health Affairs'* June 2017 issue reported that Connecticut's Medicaid program led the nation in controlling cost trends on a per enrollee basis for the 2010-2014 period. Connecticut was reported as having reduced per person spending by a greater percentage (5.7 percent) than any other state. Overall and in Connecticut, Medicaid tracked lower nationally than both private health insurance and Medicare in the cost trend comparisons. Furthermore, for FY 2017, Medicaid expenditures in DSS grew by only 1.1 percent, demonstrating yet again that Connecticut's service model continues to bend the cost curve while improving health outcomes. Connecticut is extremely fortunate to have had such success in controlling Medicaid costs in recent years just as the state has begun to seriously address unfunded pension liabilities. It is critical that this area of the budget remain controlled as the state faces extraordinary pressures with slow revenue growth and large unfunded liability payments in the coming years.



Paying Down Long-Term Liabilities Over Time

The State Employee Retirement (SERS) and Teachers Retirement systems (TRS) suffer from years of insufficient contributions by the state, returns on investments less than the assumed rate of returns, and faulty actuarial assumptions. Today there are unfunded liabilities of nearly \$33.4 billion in our two pension systems – about \$20.3 billion for SERS and \$13.1 billion for TRS.

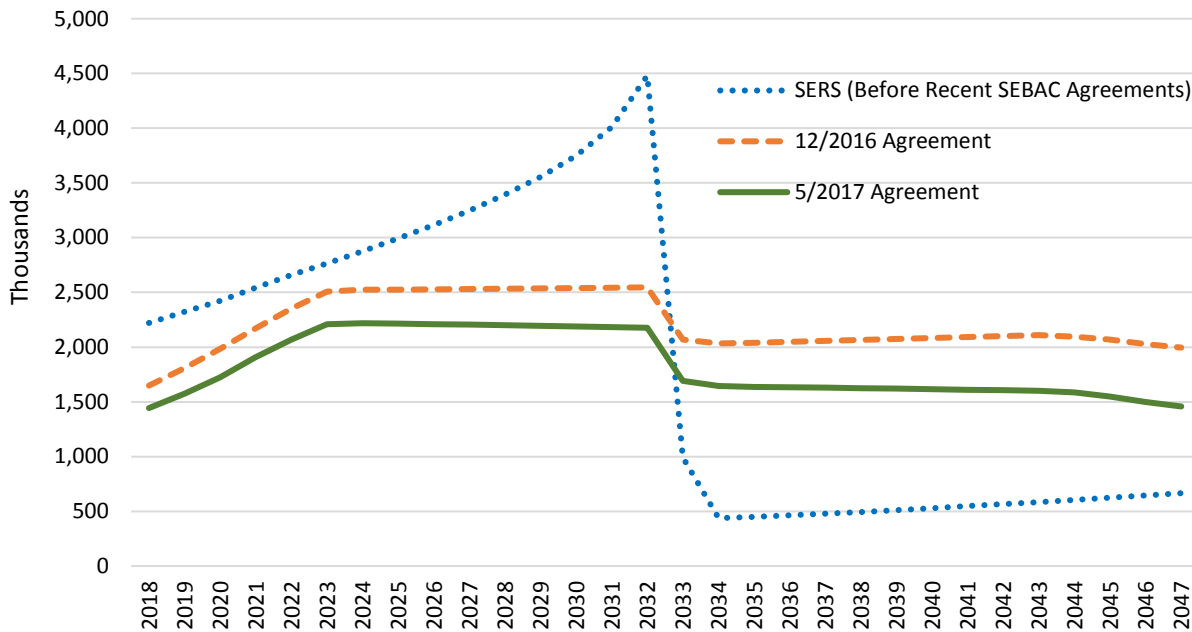
It took the state decades to amass these billions of dollars of unfunded liabilities and it will take decades of difficult budgetary choices and commitments by generations of taxpayers to pay off these debts. Despite the political rhetoric and facile promises, there are no easy solutions to the unfunded liability; it simply must be paid off over time. It will not be solved by dissolving the State Employees Bargaining Agent Coalition (SEBAC) agreement or making statutory changes to lower the state’s contribution now based on a promise to make changes next decade. Even if the State of Connecticut could stop offering any retirement plans to state employees starting today, we would still need to pay off the unfunded liability.

The smart path forward for SERS and TRS requires that we continue to pay at least the full state contribution each year, ensure that our actuarial assumptions are accurate and that we are not tampering with the outcomes with short-sighted and financial disastrous early retirement plans, pension holidays, or unrealistic assumptions. Fortunately, the state is currently on this path for SERS due to the reforms included in SEBAC 2011, the elimination of the SEBAC 4 and 5 contribution adjustments in 2014, SEBAC 2017 and the SERS restructuring changes of December 2016. These agreements have not only reduced the cost of pension benefits for the state going forward, but they also ensure that the pension funding method is actuarially sound and does not put state taxpayers at risk of fiscal catastrophe.

The agreement in late 2016 that lowered the assumed rate of return and made structural changes to the amortization assumptions and methods created a smoother and more predictable payment schedule for the state’s annual contribution. These changes helped avoid the spiking annual contributions the state faced in the late 2020s and early 2030s that could have eclipsed \$5 and \$6 billion per year and would have required significant tax increases or major expenditure cuts. Further, the new system allows for market

shocks to be more easily absorbed, as those are amortized over 25 year periods rather than requiring that they be addressed all at once at the end of a fixed period. We now project a far more stable and predictable future with a peak contribution of \$2.2 billion.

State Employees Retirement System Recent changes have stabilized contributions



Note: The December 2016 agreement made changes to actuarial methods and assumptions, including a reduction in the assumed rate of investment return and revisions to the amortization period for portions of unfunded liability. The May 2017 agreement restructured wages and pension and healthcare benefits.

The SEBAC 2017 agreement also positively impacted the state’s Other Post-Employment Benefits (OPEB) liability. Prior to the agreement, the state’s liability was anticipated to increase by \$1.78 billion in 2017 to a total of \$20.9 billion, but, as a result of the agreement, the net OPEB liability actually decreased to \$17.4 billion.

Without reform, the TRS still faces the same uncertain future of state contributions that could cripple the state’s budget unless action is taken quickly to stabilize the system by adopting a new and more progressive amortization model. Presently, TRS’ amortization schedule would require that nearly all of its unfunded liability be resolved by 2032, thereby forcing the state to meet the normal cost plus resolve \$13.1 billion in unfunded liability in 13 years. The TRS assumed rate of return remains at eight percent, and while investment returns were above that for 2017, historical averages indicate the assumed rate of return over the course of several years is likely to be several percentage points less than eight, which will result in an ever-increasing amount of unfunded liability each year we fail to meet the eight percent target. In addition, TRS uses the less effective “level-percent-of-payroll” approach to calculate amortization payments, which results in ever increasing levels of contributions toward the end of the amortization period. TRS has been undermined over many years through billions of dollars of unfunded liabilities due

to a poor relationship between investment returns and its assumed rate of return, a problematic amortization approach, and insufficient contributions.

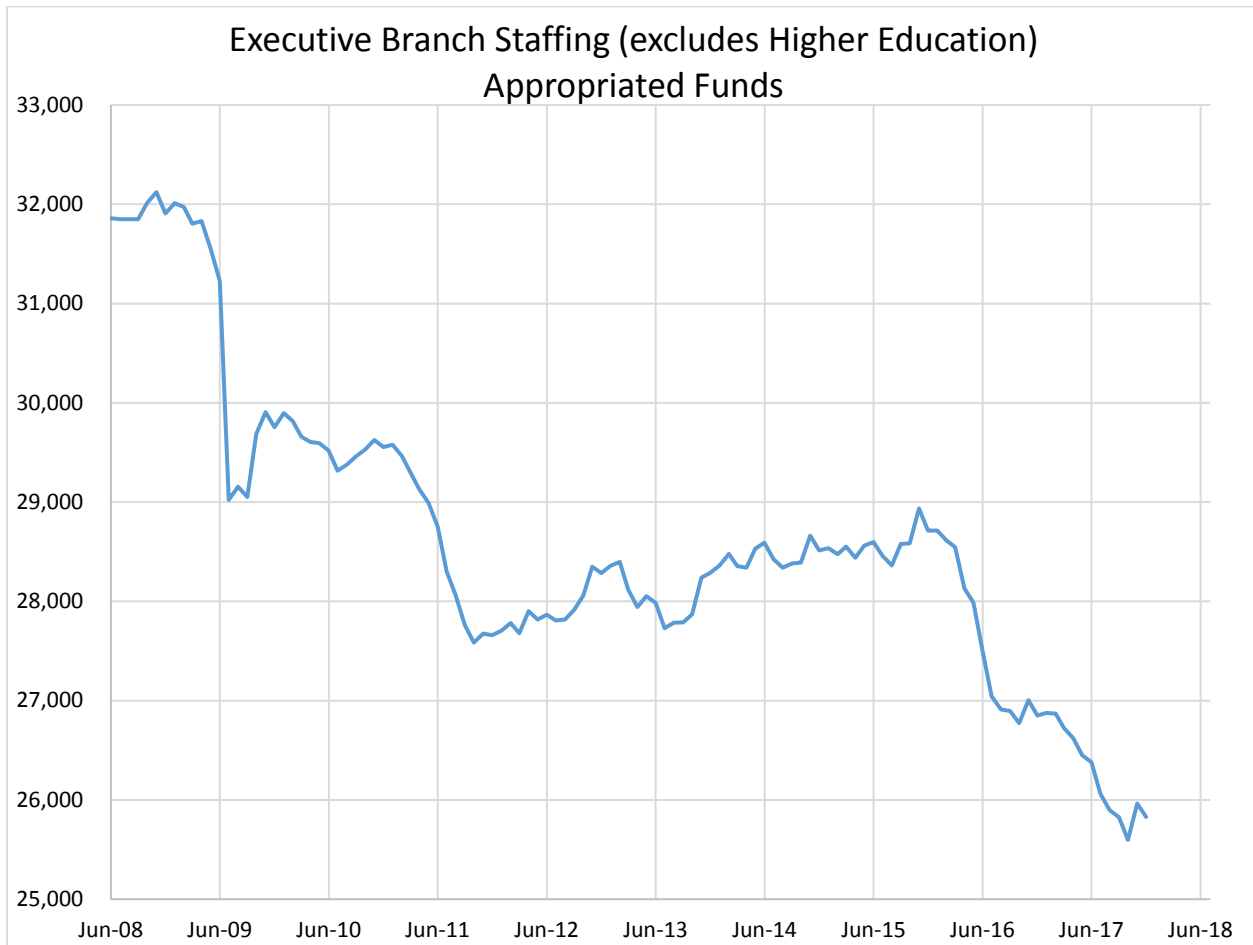
In 2017, as part of his biennial budget proposal, Governor Malloy proposed lowering the assumed rate of return to 6.9 percent, adopting the same amortization methodology as SERS (level dollar, new amortization periods for market returns), which would have drastically reduced future required contributions to the fund and given the state the budget stability it needs moving forward. Those same changes are proposed again as part of this budget.

Saving Costs by Reducing Staff, Reducing Future Pension Commitments, Implementing Technology and Redesigning Government Services

Connecticut state government has made enormous strides in the last seven years as agencies have redesigned services, implemented new technology, and found ways to be more responsive to the public even though reduced budgets have demanded ever-decreasing staff levels. At the same time, the financial relationship between the state and its employees has undergone seismic change, with two major concession agreements dramatically reducing the costs of new employees compared to those hired during previous eras.

Reduced State Staffing

Underlying all of these changes is the dramatic reduction in the number of state employees in the executive branch of state government. At the end of calendar year 2017, there were 25,830 permanent full-time employees being paid from appropriated funds in the executive branch (excluding higher education). That is 3,726, or 12.6 percent fewer than the number at the end of calendar year 2010. To take a longer perspective, this means that executive branch agencies have fewer staff than any time since the 1950s, adjusted for population change. This trend is the result of aggressive action by the Malloy Administration to achieve attrition, as well as some minimal number of layoffs that have occurred from time to time. This attrition has enabled the state to achieve significant budget savings, and has been a major component of savings achieved under both concession agreements with state employees.



Concessions from State Workers

Over the last seven years, Governor Malloy has achieved the most significant concessions from state employees in generations. In addition to employing fewer workers, the state has also made major changes to pensions, healthcare, wages, human resource administration, longevity, and other post-employment benefits. These changes have been achieved at the bargaining table, respectful of the collective bargaining process and in ways that seek to benefit the state while imposing the least possible harm to both employees and residents of the state who consume public services.

A review of these changes clearly demonstrates that the SEBAC agreements in 2011 and in 2017 have had a major favorable budget impact on the state, and that had those agreements not been struck Connecticut would be facing structural deficits that dwarf those faced today. Those two agreements:

- Resulted in wage freezes for five of the eight years from FY 2012 and FY 2019;
- Significantly increased employee contributions for pensions, employee healthcare, and retiree healthcare;
- Extended the minimum retirement age, increased early retirement penalties, and reduced future cost of living adjustments for existing employees; and

- Established austere new pension tiers for new employees – the normal cost of the defined benefit portion of the tier 4 pension plan is only 2.19 percent of salary for normal duty employees and just 0.72 percent for hazardous duty employees.

Various features of the two agreements are shown in the following chart:

| | SEBAC 2011 | SEBAC 2017 |
|------------------------------|--|---|
| <u>Pension Changes</u> | | |
| Employee Contributions | | Increased by 1.5% of salary for all tiers in FY 2018 and an additional 0.5% in FY 2020. |
| Benefits Changes | Minimum COLA reduced from 2.5% to 2.0% for individuals who retire after 9/2/2011. Doubled the reduction penalty for early retirement: from 3% per year to 6% per year. Age requirement for normal retirement increased by 3 years. | Minimum COLA reduced from 2% to 0% for employees who retire after 6/30/2022. Delayed receipt of first COLA after retirement. |
| New Pension Tier | Tier 3 established for employees hired after 7/1/2011. Includes change from 3-year to 5-year final wage smoothing, and a minimum retirement age for hazardous duty employees with less than 25 years of service. | Tier 4 established for employees hired after 7/1/2017. Tier 4 is a hybrid defined benefit / defined contribution plan which includes an employee contribution that is 3% higher than tier 3, a multiplier for defined benefits that is more than 7% lower than tier 3, eliminates the breakpoint, and limits the amount of pension that can be derived from overtime. The defined contribution portion includes a state contribution of 1% and a minimum employee contribution of 1%. |
| Other Pension Plans | | Makes changes to the Higher Education Alternative Retirement Plan, including an increase in the employee contribution and a decrease in the state's contribution to the plan. |
| <u>Employee Wage Changes</u> | | |
| Wage Freeze | Two-year wage freeze: FY 2012 and FY 2013. | Three-year wage freeze: FY 2017, FY 2018, and FY 2019. |
| Other Wage Provisions | | 3 furlough days in FY 2018 for most bargaining units. One-time payments (generally \$2,000) in FY 2019. |
| Longevity | Elimination of the October 2011 longevity payment for capped | Deferral of April 2018 longevity payment until FY 2019. |

| | | |
|---------------------------|---|--|
| | bargaining units and elimination of longevity for new employees. | |
| <u>Healthcare Changes</u> | | |
| Benefits | Increased emergency room (ER) copay to \$35 | Increased ER copay to \$250, increased utilization management, and established a tiered network. |
| Premium Cost Sharing | | Phased-in approximately 25% increase in active employee's share of premium costs. |
| OPEB | All employees to contribute 3% to Other Post-Employment Benefits Fund for 10 years. Increased the amount of state service necessary for retiree healthcare from 10 years to 15 years. | New employees contribute to OPEB fund for 15 years. All retirees are transitioned to a Medicare Advantage plan. Increase in retiree share of premium costs for employees who retire after 10/1/2017 and again in 2022. |

Implementing New Technology and Process Improvement

In addition to modernizing the relationship between the state and its employees, Governor Malloy has overseen a major renewal of the technology that state agencies rely on to provide responsive, cost-effective services. Over the last seven years, agencies have upgraded systems, implemented new technologies, enhanced security, and added new redundant data centers to ensure business continuity. In order to accomplish this work, Governor Malloy initiated the Information Technology (IT) Capital Investment Program, which funds IT projects based on a thorough review of each project's return on investment, while ensuring that projects are completed according to plan.

Since its inception in FY 2013, the IT Capital Investment Program has provided funding for 75 projects with bond allocations of \$286.9 million. As a result, Connecticut has been able to leverage \$334.4 million in federal funding and save millions per year in operating costs. Projects have been approved for 29 agencies throughout state government.

The program is governed by the Information Technology Strategy and Investment Committee, a governance board of agency leaders from cross-functional areas of state government. The Committee meets monthly and has been instrumental in:

- Establishing the funding priorities, rules, processes and procedures associated with the fund;
- Recommending funding of projects submitted under the program in accordance with the goals and priorities; and
- Approving projects budgets, financial reporting, governance model, and project management approach to be employed with respect to approved projects.

Funding priorities are to:

- Make state government more user-friendly and efficient for citizens, businesses and municipalities when transacting business with the state;
- Make information about services and state government more available and easy to find on-line;

- Coordinate efforts with OPM's LeanCT program to implement efficient, modern business practices that result in service delivery improvements for state agencies;
- Increase transparency for the public and policy makers regarding costs, effectiveness and service outcomes within and across state agencies;
- Reduce the costs to the state regarding implementation, use and management of technology systems through shared services, applications and hardware across agency boundaries;
- Implement systems needed in support of health care reform and improving outcomes related to the state's health and human services programs; and
- Ensure the appropriate confidentiality, integrity and availability of the state's valuable electronic or digital data information resources in order to provide an environment in which the state's user community can safely conduct business.

The implementation of new technology has been paired with business process improvement (BPI) under the Governor's Lean initiative, LeanCT. Since its inception in 2013, LeanCT has actively encouraged participation in BPI by over 40 executive branch agencies, several nonprofit provider agencies, municipal leaders, and the legislative and judicial branches of state government. Over 3,000 state employees (roughly ten percent), and nearly 200 nonprofit provider staff, have been trained to use Lean tools and principles to improve service delivery. Hundreds of processes have been analyzed and streamlined using the Lean methodology, a proven scientific approach to collaborative problem-solving. Lean has empowered employees to eliminate waste, remove redundant steps, and add standardization across programmatic, agency, and even, industry lines.

As with the IT Capital Investment Program, LeanCT is similarly guided by a governance board. The Statewide Process Improvement Steering Committee, which meets monthly, is made up of individuals representing fifteen state agencies, spanning all areas of state government.

LeanCT and the IT Capital Investment Program, both managed within OPM, work closely to identify opportunities for inter-agency collaboration, common technology needs throughout state government, and best practices across the system. The two programs promote the concept of improving any process prior to automation, and support state agencies in their implementation of this philosophy.

Connecticut has positioned itself as a national leader for our efforts to align people, process, and technology to enable service delivery in the most cost efficient and effective manner.

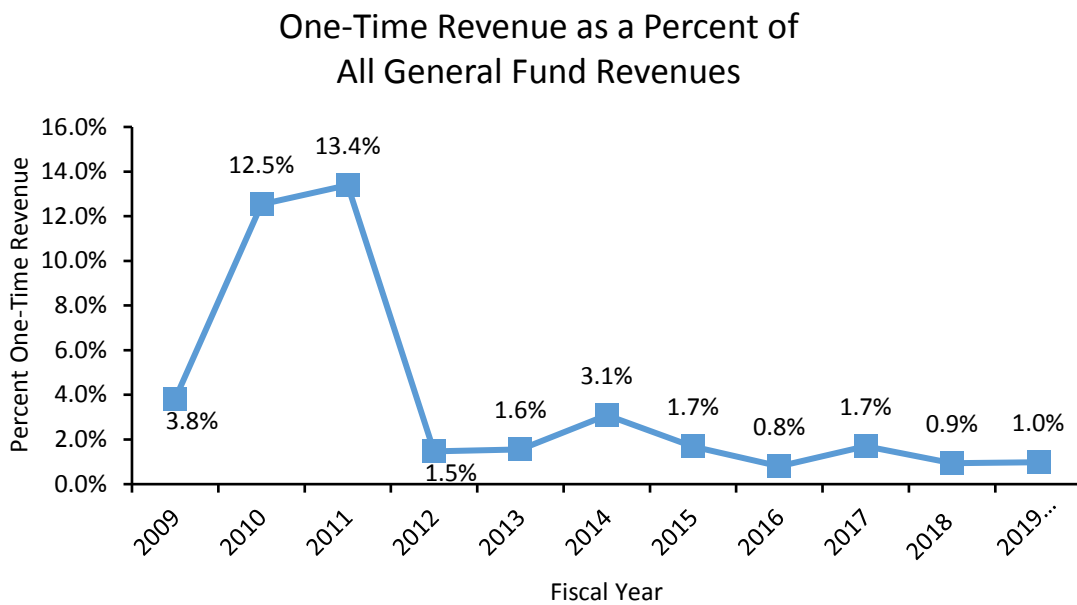
These workplace changes have in many cases been accompanied by changes in the physical workplace as well. Taking advantage of a depressed office market in Hartford, Governor Malloy purchased 55 Farmington Avenue, which now houses several agencies in a state- of-the-art office building. Also, the state acquired the complex at 450 Columbus Boulevard, a modern office environment which now houses a number of agencies that had previously occupied the State Office Building.

The State Office Building is being renovated and will ultimately house the state's constitutional officers, allowing the state to discontinue its costly lease on Elm Street. These moves have allowed the state to not only cut costs for leased space, but will provide cost-effective facilities for state government for years to come.

The changes at agencies also include considerable consolidations. The number of budgeted agencies has been reduced from 81 in FY 2011 to 56 in FY 2019, including the consolidation of the State Department of Education (SDE) and the Office of Higher Education (OHE) that has been occurring over the last year and is proposed to be formalized in this budget.

Balancing the Budget Every Year Without Relying on One-Time Measures and Gimmicks

While the State of Connecticut has certainly faced a difficult period since the great recession of 2008, with slow growth, a precipitous decline in the financial services sector that had fed earlier prosperity in the state, and the inevitable reckoning of our unfunded pension liabilities, the Malloy Administration has made every attempt to balance the state budget each year without relying on deficit funding, misleading revenue forecasts, one time measures, and gimmickry.



Governor Malloy has been focused on long-term improvement to the state’s finances through measures to pay down and constrain future growth in unfunded liabilities; through long-term concessions achieved through collective bargaining; and through economic development strategies aimed at securing long-term, enforceable commitments from our most vital industries. At the same time, the administration has presented and advocated for balanced budgets that rely on straightforward, recurring measures. The budget recommendation made here also achieves balance through restrained spending, financed with recurring revenue measures. It is the challenge of the legislature to consider this recommendation and to pass a final budget that is as responsible and that honors the trust we have with our children to leave state government stronger than we received it from our parents.

The following sections provide additional details regarding the policies that are reflected in the Governor’s budget proposal.

Transportation

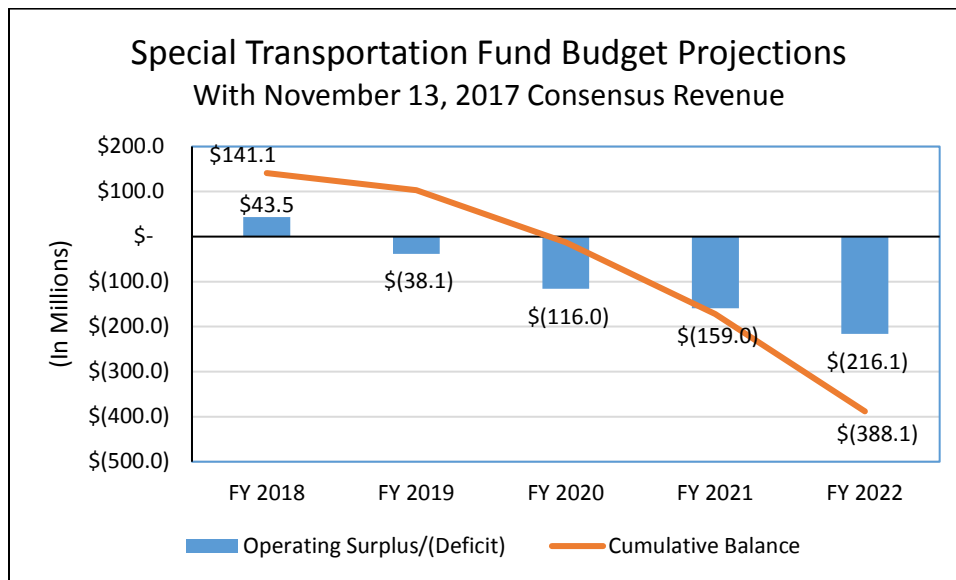
The Challenge We Face

Within weeks of the adoption of a budget for the FY 2018 and FY 2019 biennium, revised consensus revenue estimates for the STF adopted in November 2017 showed a reduction in FY 2019 revenues of \$38.1 million and further reduced out-year revenue expectations. Declines in Oil Companies tax revenue made up over 50 percent of this reduction, largely due to continued low oil prices.

While low oil prices have been great for Connecticut residents, they come at a cost to our ability to fund transportation infrastructure projects and to sustain healthy long range balances in the STF. Combined with tepid or even non-existent growth in the state's motor fuels tax, this trend makes it impossible for the state to continue to develop and maintain a transportation infrastructure system for the 21st century.

| November 13, 2017 Consensus FY 2019 Major Revenue Reductions (In Millions) | |
|--|-----------------|
| Oil Companies Tax | \$(20.4) |
| Sales and Use Tax | (4.4) |
| Motor Fuels Tax | (3.8) |
| All Other | <u>(9.5)</u> |
| Total Revenue Loss | \$(38.1) |

Projections released by the Governor's Office on December 7, 2017, indicated that these new revenue trends would create insurmountable problems in our ability to maintain balanced budgets, limiting affordable access to credit markets and forcing the state to immediately shut down ongoing infrastructure programs. This is an unacceptable outcome for the State of Connecticut and immediate action needed to be taken.



Undesirable Solution – Deferred Projects, Service Cuts, and Fare Hikes

In order to stay within the bipartisan state budget for FY 2018 and FY 2019, and in light of the reduced revenues forecast through the consensus process and in the absence of legislative intervention, the Governor ordered drastic actions to be taken in order to operate within the resources of the STF.

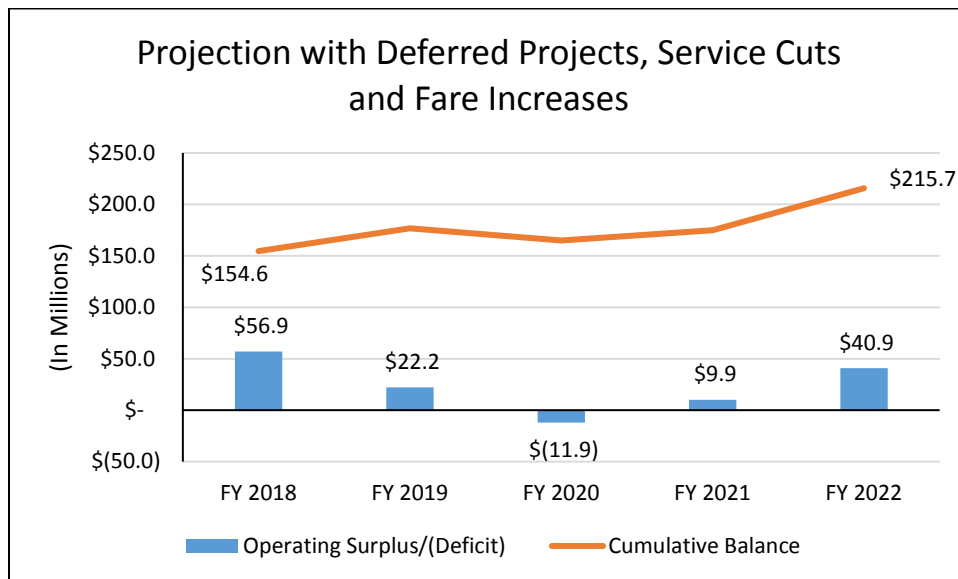
For the DOT, this scenario meant drastic changes to operations, including significant fare increases and various service reductions across the state, including the near-elimination of Shore Line East service.

Specifically, the following reductions would have been necessary in FY 2019 to live within current levels of revenue:

| | |
|--|--------------------|
| Reduce Rail Subsidy by Raising Fare Revenue by 10% on New Haven Line | \$(19,000,000) |
| Eliminate Weekend and Some Off-Peak Rail Service on the Danbury, Waterbury, and New Canaan Lines | (15,000,000) |
| Reduce Transit District Subsidy by 15% | (4,500,000) |
| Reduce Bus Subsidy by raising Fares by \$0.25 | <u>(3,900,000)</u> |
| Total - Expenditure Reductions | \$(42,400,000) |

In addition, capital investments would have to be slashed over the next five years, resulting in a reduction in debt issuance by \$1.1 billion and the deferral of over \$4.3 billion in critical infrastructure projects. These projects include essential bridge maintenance, roadway paving and traffic mitigation. Many of the state’s largest upcoming transportation projects, including the Waterbury Mixmaster and Hartford Viaduct, would have to be delayed, some indefinitely.

Without the addition of new revenues, the result of these actions, along with other smaller changes, would be a STF that was balanced and maintained projected balances into the future. However, this comes at a great cost. Rail fares would have to be raised again by another 10 percent, bus fares would increase by five percent, Shore Line East service would be deeply cut and New Haven branch line service would be reduced.



A Better Way Forward - The Governor’s Budget Recommendation

The severity of the cuts demonstrates the urgency of the need for the Special Transportation Fund to find new sources of revenue. The revenue proposals allow for these cuts to be restored – a total addback of \$42.4 million – and for project deferrals, fare increases, and service reductions to be averted. The Governor is proposing the following revenues in order to bring the STF into balance.

Increasing the Gasoline Tax

An increase in the gasoline tax rate by seven cents to 32 cents over the next four years. Starting in FY 2019 the gas tax will increase by two cents, in FY 2020 by one cent, in FY 2021 by two cents, and in FY 2022 by two cents. This increase will be the first since 1997, when the gasoline tax was 39 cents. The tax was reduced from 1998 to 2000, dropping it to where it is today, at 25 cents.

Accelerating the Transfer of the Motor Vehicle Sales Tax

Public Act 17-2 (June Special Session) provided the Special Transportation Fund with a significant revenue enhancement. Starting in FY 2021, all sales tax collected on the sale of new and used motor vehicles is scheduled to be transferred from the General Fund to the STF. The revenue would be phased-in at 20 percent increments over five years. Unfortunately, this relief would come too late.

In the Governor’s proposal, the diversion of the sales tax on motor vehicles will be accelerated in order to provide more immediate help to the STF. A small portion will be transferred in FY 2019 and then 20 percent of the revenue would begin to be deposited in FY 2020, rising to 100 percent by FY 2024.

Imposing a Tire Fee and Eliminating the School Bus Seat Belt Account

A new \$3 motor vehicle tire fee will be attached to the purchase of new tires. This fee will generate an estimated \$8 million per year for the STF and will help to diversify the revenue of the fund offsetting revenue losses from vehicles switching to electric power from gasoline power. The School Bus Seat Belt account no longer serves its original purpose. The Governor’s budget proposal calls for the elimination of the account, allowing the revenue generated to fund the program to remain in the STF as had been the case prior to 2010. This will provide an additional \$2 million in revenue per year beginning in FY 2020.

Statewide Tolling

The impact of the revenue proposals mentioned above will not be sufficient to finance the major improvements required to maintain a 21st century transportation system. In order to finance major upgrades, including the replacement of the Hartford Viaduct and the Waterbury Mixmaster, as well as other statewide traffic mitigation projects, the Governor is recommending the authority to implement electronic tolling. Preliminary estimates are that tolling could generate \$600-\$800 million per year. While this revenue will not be realized immediately, it is imperative to move forward now in order to allow time for the design and buildout required to establish tolling and realize revenues to support our transportation infrastructure.

| STF Revenue Proposals | | | | | |
|--|-------------|---------------|----------------|----------------|----------------|
| (In Millions) | | | | | |
| | Eff. | FY | FY | FY | FY |
| | Date | 2019 | 2020 | 2021 | 2022 |
| Increase Gasoline Tax by 7 Cents (2, 1, 2, 2) | 7/1/2018 | \$30.0 | \$45.0 | \$75.0 | \$105.0 |
| Accelerate Transfer of Car Sales Tax by 2 Years | 7/1/2018 | 9.1 | 66.9 | 78.7 | 74.9 |
| Impose a Tire Fee (\$3 per tire) | 7/1/2018 | 8.0 | 8.0 | 8.0 | 8.0 |
| Eliminate transfer to School Bus Seat Belt Account | 7/1/2019 | - | 2.0 | 2.0 | 2.0 |
| Institute Statewide Tolling (Effective FY 2023) | 7/1/2018 | - | - | - | - |
| | | \$47.1 | \$121.9 | \$163.7 | \$189.9 |

With the restoration of the STF to solvency, DOT can continue to maintain and provide the same level of services for the citizens of Connecticut.

Expenditure Adjustments

The Governor's budget provides additional funding in the following areas:

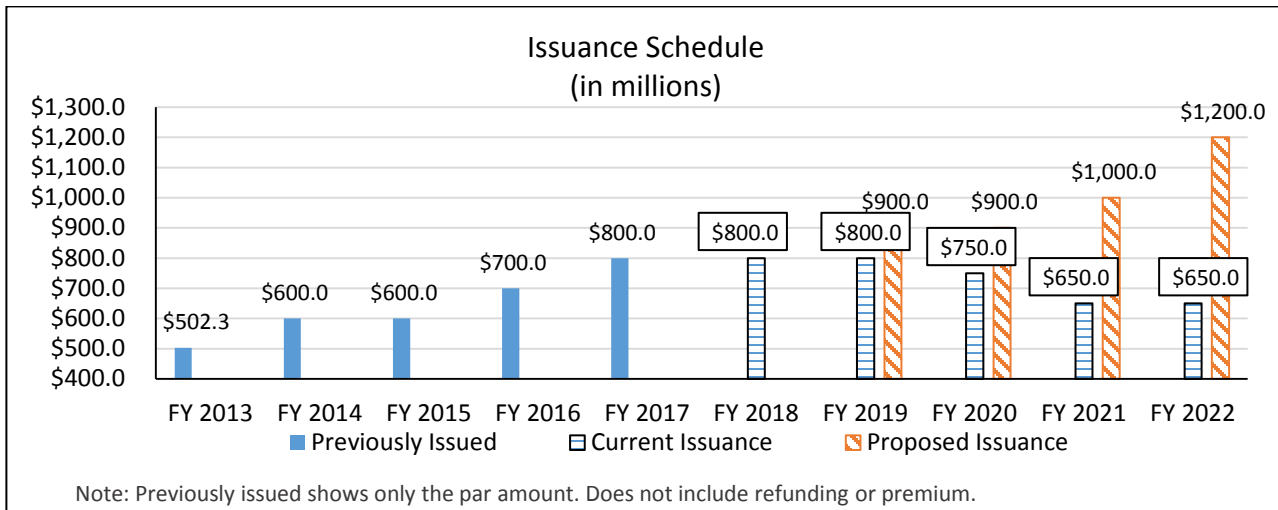
- Rail Operations to align the funding with Metro North's calendar year 2018 budget;
- Bus Operations due to contractual labor, benefit, service and pension increases. Labor, pension and benefit costs make up approximately 78 percent of the total cost of operating CT Transit statewide bus service;
- ADA Para-Transit due to increased utilization and contractual labor increases in this federally mandated program; and
- Pay-As-You-Go to comply with the Department of Energy and Environmental Protection General Permit for the discharge of storm water an additional 40 positions will be provided. The General Permit tasks DOT with developing a Storm Water Management Plan (SWMP) which outlines the best management practices to be implemented to meet control measures outlined in the permit.

To offset the additional funding noted above, some efficiencies were identified after a reassessment of the department's budget and operations:

- Achieving personnel savings by delaying certain hiring;
- Reducing Pay-As-You-Go Program funding by reprioritizing projects;
- Implementing non-service reductions on Metro North Railroad; and
- Annualizing the cost of UConn CTfastrak service subsidy through the collection of current student fees.

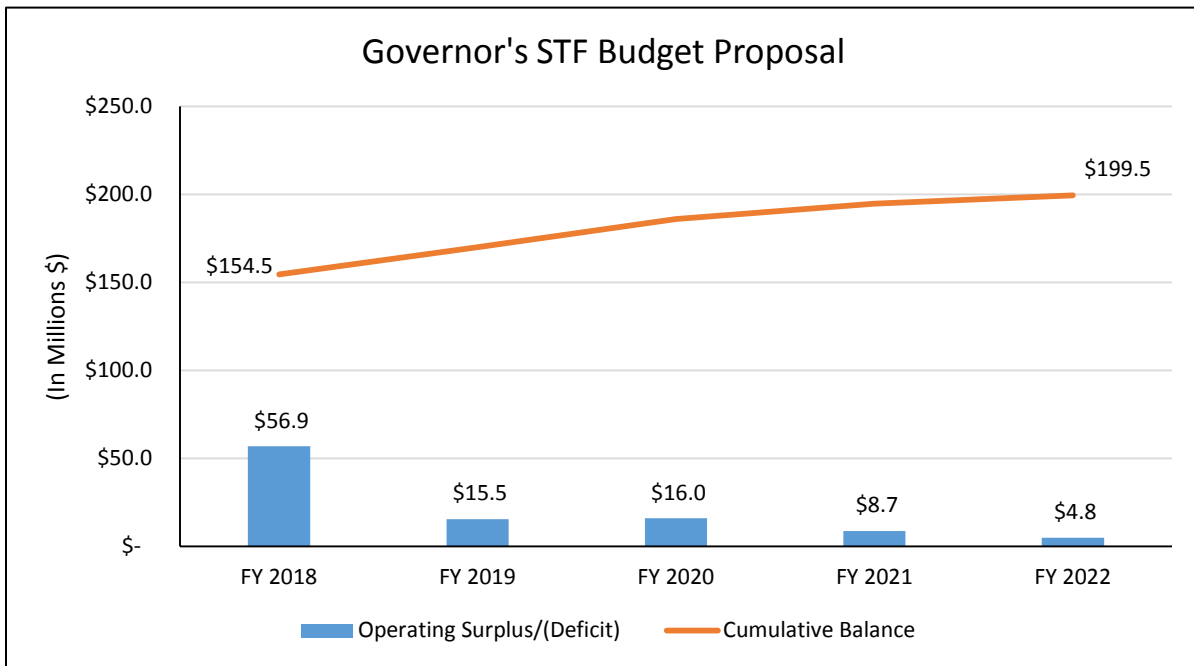
These adjustments are part of the structural changes needed to correct the trajectory of the STF on both the revenue and expenditure sides while maintaining the fund's solvency and creditworthiness.

The additional revenue proposed in this budget would ensure the resources necessary to fund large scale transportation projects are in place. Capital investments will grow from \$800 million in FY 2018 to \$1.2 billion in FY 2022, providing an additional \$1.1 billion of capital outlay to be spent on economy-boosting transportation projects. In total, this schedule will restore the \$4.3 billion in deferred projects and reverse the decades-long underfunding of the state's transportation infrastructure.



In summary, the Governor’s budget proposal will provide a long term solution to the STF while keeping his promise to improve the state’s transportation infrastructure. The proposal does the following:

- Eliminates all proposed rail fare hikes – these increases unfairly target commuters who have seen rail fares increase by more than 26 percent over the last decade;
- Eliminates all proposed bus fare hikes;
- Eliminates service reductions – continues weekend and off peak service to branch lines in the Danbury, Waterbury and New Canaan communities. Also ensures the continued funding of Shore Line East;
- Provides for modest operating surpluses each fiscal year;
- Enhances the cumulative balance in the fund to withstand any unexpected contingencies;
- Sustains the creditworthiness of the fund which will lower long-term borrowing costs;
- Restores capital funding for vital infrastructure projects;
- Leaves future governors and legislatures with the resources necessary to adequately support critical investments in the STF; and
- Provides our citizens with the transportation network they need and demand to compete in the 21st century.



Changes to Wages, Pensions and Health Care Funding

Restructure the Teachers’ Retirement System to Avoid the 2030 Cliff

The restructuring of the TRS has been difficult due to the bond covenant of the pension obligation bonds issued in 2008. The bond covenant was intended to ensure the state continued to meet its obligation of full payment of the actuarially determined employer contributions, which the state is fully committed to carry out. However, the covenant has limited the state’s ability to reduce the risk of multi-billion dollar increases in contributions in the remaining years of the amortization period. Therefore the Governor proposes statutory language to allow the Teachers’ Retirement Board (TRB) to adopt several factors to be used in the valuation with the intention of minimizing this risk. These factors include:

- An appropriate annual investment rate of return assumption that is not greater than seven percent;
- A new closed amortization period for any outstanding unfunded liability of not more than thirty years from the date of the next following valuation of said fund;
- A change to level dollar amortization for any unfunded liability with any phase-in of such change in amortization methodology to be completed over a period of not more than five years; and
- Separate amortization periods of not more than 25 years for any future changes in unfunded liability incurred as a result of market gains or losses.

Similar factors have been adopted for the TRS in stabilizing the growth in contributions

In addition, OPM has retained Cavanaugh Macdonald LLC to be the TRS Viability Commission global consultant. The TRS Viability Commission was established pursuant to Public Act 17-2 (June Special Session) and consists of the members of the TRB and the consultant. The Commission is mandated to develop and implement a plan to maintain the financial viability of the TRS. The Commission must give significance to the capabilities of the state, including:

- The fiscal health of the state;

- The balance in the Budget Reserve Fund, established under section 4-30a of the general statutes;
- The short and long-term liabilities of the state, including, but not limited to, the state's ability to meet minimum funding levels required by law, contract or court order;
- The state's initial budgeted revenue for the state for the previous five fiscal years as compared to the actual revenue received by the state for such fiscal years;
- State revenue projections for the fiscal years during the period in which the proposed plan is to be in operation;
- The economic outlook for the state;
- The state's access to capital markets; and
- The financial capability of the state does not include the state's ability to raise revenue through new or increased taxes.

These initiatives are designed to not only avoid a fiscal crisis in the future by reducing the staggering growth in contributions but, more importantly, they will maintain the financial viability and long term sustainability of the Teachers' Retirement System well into the future.

Other Post-Employment Benefits (OPEB) Funding Progress

In the area of post-employment benefits, the budget continues to decrease the long-term liability of the state. The implementation of a Medicare Advantage plan for the state's Medicare eligible retirees began January 1, 2018. The recommended budget reflects the first full year of savings at \$135 million. According to the most recent valuation, the impact of this program on the state's OPEB liability was a decrease of over \$5.3 billion. In addition, the valuation reflected changes from the 2017 SEBAC agreement for non-Medicare retirees pertaining to premium shares and health care design changes affecting new retirees on or after October 2, 2017. These changes resulted in a decrease in the state's OPEB liability of \$723.6 million. FY 2019 represents the second year of matching the 3 percent employee contributions to retiree health that were agreed to in the 2011 SEBAC agreement. The total contributions to retiree health in FY 2019, including state and employee contributions, plus pay-as-you-go funding for current retirees, equals over \$949 million.

Change in Accounting for the Higher Education Alternative Retirement Plan

Under the state's current accounting methodology, the General Fund appropriation for the Higher Education Alternative Retirement Plan (ARP) supports the state's contribution to ARP, which is a defined contribution retirement plan available to higher education employees. For those employees who are not funded through the General Fund, a cost recovery charge that includes both the cost of the state's contribution to ARP as well as a prorated share of retiree health care costs are credited to the General Fund appropriation. Because most ARP employees are not supported by General Fund appropriations and because an increasing share of the overall retiree healthcare pool is attributable to ARP retirees, the cost recovery from other funds is expected to exceed appropriated expenditures by approximately \$8.2 million in FY 2019. In order to avoid a negative appropriation, the Governor's budget reflects a change in the accounting methodology for ARP whereby any cost recoveries related to non-General Fund employees will be deposited as General Fund revenue rather than as an expenditure offset. This results in a \$35.5 million increase in both General Fund appropriations and revenue.

SEBAC 2017 Budget Adjustments

The labor agreement between the state and SEBAC that was reached last summer resulted in billions of dollars in savings to the state. The adopted budget included bottom line lapses of \$700 million in FY 2018 and \$867.6 million in FY 2019 in order to account for the savings due to the agreement during the biennium. For FY 2018, \$692.5 million of the \$700 million bottom-line lapse was allocated as holdbacks to agency appropriations. Those holdbacks included:

- \$300.6 million in the General Fund Reserve for Salary Adjustment account to reflect the first two years of the three year wage freeze in the agreement;
- \$149.7 million in the General Fund and \$16.4 million in the STF to reflect savings in contributions to SERS in those two funds;
- \$108.2 million in the General Fund and \$2.8 million in the STF to reflect savings for healthcare costs for retired active state employees attributable to both funds;
- \$12.8 million across all appropriated funds to reflect a three-month delay in the payment of the April longevity payment;
- \$26.4 million across all appropriated funds to reflect the impact of furlough days that were negotiated for FY 2018; and
- \$75.6 million in savings for increased attrition, which were only applied to General Fund agencies.

For FY 2019, the Governor has proposed moving the savings related to the agreement into specific lines of appropriation and eliminating the “below the line” lapses. These include the following decreases to agency appropriations:

- \$468.2 million in the General Fund Reserve for Salary Adjustment account to reflect the three year wage freeze in the agreement;
- \$170.2 million in the General Fund and \$18.7 million in the STF to reflect savings in contributions to SERS in those two funds;
- \$190.3 million in the General Fund and \$3.6 million in the STF to reflect savings for healthcare costs for retired active state employees attributable to both funds; and
- \$75.6 million in savings for increased attrition – these savings were only applied to General Fund agencies and are in the same amounts as the FY 2018 holdback for attrition.

Note that no reduction for FY 2019 has been proposed for furlough days as the agreement does not include any furlough savings in FY 2019.

In addition to the funding decreases noted above, the agreement includes \$101.2 million in one-time funds during FY 2019 to support one-time payments that were negotiated for FY 2019 as well as payment of the delayed April 2018 longevity payment during FY 2019. Of the \$101.2 million, \$9.6 million is attributable to the STF and will be supported by funds to be carried forward from OPM’s Reserve for Salary Adjustment account in that fund. The remaining \$91.6 million, attributable to all branches of government and all budgeted funds other than the STF, has been budgeted in the General Fund Reserve for Salary Adjustment account.

Health and Human Services Budget Revisions

Juan F. Compliance

Significant funding is provided to support the Governor's directive that the Department of Children and Families (DCF) exit the *Juan F.* lawsuit under conditions approved by the U.S. District Court in December 2017. Five million dollars is recommended to support 132 child protective services workers hired in the current fiscal year to improve caseload ratios, while \$11.4 million will allow DCF to maintain community-based programming and address service needs to meet agreed-upon outcome measures.

Connecticut Juvenile Training School (CJTS)

The recommended budget reflects savings of \$11.4 million, reflecting the Governor's commitment to close CJTS by July 1, 2018. Admission to the facility ceased in January, to allow DCF to engage in the planned discharge of the youths in residence. The elimination of positions at CJTS will be accomplished in accordance with applicable statutes, regulation, and collective bargaining agreements. To the fullest extent possible, employees will be moved into vacant positions elsewhere in state service.

Restructuring Juvenile Justice Services

Pursuant to Public Act 17-2 (June Special Session), effective July 1, 2018, responsibility for adjudicated delinquent children transferred from DCF to the Court Support Services Division of the Judicial branch. The adopted budget transferred all DCF funding for juvenile justice outreach services to the Judicial Department. The Governor recommends that a net \$6.7 million be transferred back to DCF to support ongoing clinical intervention and other services primarily utilized by non-delinquent youth.

Caseload Growth and Investments in Quality of Care

The Governor's recommended budget provides additional funding in DSS, DDS, and DMHAS to reflect anticipated program requirements.

In DSS, with expenditures trending higher than budgeted, funding for the Old Age Assistance and Aid to the Disabled accounts is increased by \$1.8 million and \$1.4 million, respectively. For the Temporary Family Assistance account, Public Act 17-2 (June Special Session) annualized \$4.5 million in FY 2017 rescissions and reduced baseline funding by \$5.0 million. Because cuts of this magnitude are not achievable, an additional \$5.0 million is provided in FY 2019.

In DDS, the Governor recommends \$5 million in new funding to support placements that can address the most critical needs that arise during the year, including youth caught in emergency departments without adequate placement alternatives and made modest investments in employment/day and residential services for individuals with intellectual disabilities.

The Governor also recommends \$1 million in DMHAS to enhance the management capacity of two distinct hospitals in Middletown, Connecticut Valley Hospital and the new Whiting Forensic Hospital. This funding will address systemic deficiencies and improve quality and oversight in both hospitals in order to maintain federal certification and related federal reimbursement at Connecticut Valley Hospital and to obtain Department of Public Health (DPH) licensure of the new Whiting Forensic Hospital.

Additional funding is recommended to expand the state's Newborn Screening panel to include two additional disorders: Pompe Disease and Mucopolysaccharidosis Type I (MPS 1). This is consistent with

the U.S. Department of Health and Human Services' endorsement of these disorders for inclusion in the recommended universal screening panel.

Wage Increases for Personal Care Attendants

Executive Order 10, signed by Governor Malloy in September 2011, allowed personal care attendants who provide personal care assistance under a Medicaid or state-funded program to organize and collectively bargain such issues as wage standards, training and professional development in order to improve the quality, stability and availability of personal care assistance in the state. The recommended FY 2019 appropriation for Medicaid is sufficient to support the anticipated wages and training costs for the Tentative Agreement reached in January 2018, with action to be taken by the 2018 General Assembly following ratification and submission.

Further Conversions to Privately-Provided Services

The DMHAS service system is a collaborative partnership between publicly and privately-operated services. Annualized savings of \$4.2 million are estimated in DMHAS through the restructuring of some state-operated services and to further convert to private operation which may include services provided by publicly-operated Local Mental Health Authorities (LMHAs). These conversions are not expected to decrease the total number of beds in the DMHAS system of care but instead, the department will evaluate and invest in the highest quality and most efficient community options.

Net savings of \$1.0 million are anticipated in DDS in FY 2019 through the conversion of an additional ten state-operated residential community living arrangements (CLAs) to privately-operated CLAs. Currently, more than 90 percent of CLAs are operated by private providers. These conversions will leave fewer than 30 state-operated group homes by January 2019.

Reduced Reliance on the Insurance Industry

This budget reduces costs imposed through assessments upon the insurance industry by almost 3.7 percent (approximately \$3.5 million). The Children's Health Initiatives account is reallocated from the Insurance Fund to the General Fund, correcting a significant flaw in Public Act 17-4 (June Special Session). Similarly, the Governor recommends funding portions of the Office of Health Strategy through the General Fund.

Modernize Nursing Home Rate Setting

The Governor's recommended budget includes funding to support the development of an acuity-based rate setting system for nursing homes to modernize the reimbursement system, address inequities under the current reimbursement system, recognize resident acuity levels and direct care staffing needs, and increase access to care for higher acuity Medicaid residents. This change will align Connecticut's reimbursement methodology with many other states' Medicaid programs.

Other Human Services Savings Initiatives

The budget proposes to reduce the enhanced reimbursement for primary care providers from 95 percent of the 2014 Medicare fee schedule to 90 percent in order to achieve savings of \$3.5 million (\$8.5 million after factoring in the federal share). The Affordable Care Act required states to increase Medicaid reimbursement for primary care providers to Medicare levels for calendar years 2013 and 2014, which represented an increase of almost 50 percent for Connecticut providers. After 2014, fewer than half the states maintained the higher reimbursement levels with Connecticut continuing the rates at the 2014 Medicare level for services that were considered to be true primary care. The enacted budget reduced

reimbursement for primary care providers to 95 percent and the Governor is proposing to further reduce reimbursement to 90 percent, which is not expected to impact access to care.

While Medicare is the primary payer of graduate medical education (GME), many states voluntarily support these costs through their Medicaid programs. Unlike Medicare, the federal government has no explicit guidelines for states as to whether they should or how they could make GME payments under Medicaid. In Connecticut, hospitals are slated to receive \$21.1 million in Medicaid GME payments in FY 2018. Nearly 70 percent of the state's hospitals will receive funding under the program, with FY 2018 payments ranging from \$10,215 to Lawrence and Memorial Hospital to \$7.97 million to Yale New Haven Hospital. Recognizing the high level of support already provided to hospitals under the enacted budget, the Governor’s recommended budget eliminates Medicaid funding for GME payments for savings of \$10.6 million (\$21.1 million after factoring in the federal share).

The Grants for Mental Health and Substance Abuse Services accounts in DMHAS were reduced by approximately \$3.0 million to reflect a reduced need for state subsidies for uninsured individuals as a result of the implementation of the Affordable Care Act and a FY 2015 \$5.0 million investment in behavioral health rates.

Municipal Aid and Education Funding Revisions

Continuing Support for Municipal Aid

Since taking office, Governor Malloy has demonstrated strong support for municipal aid, while trying to direct limited resources to the neediest communities.

| Grant | Cap Grants at the Lesser of FY 2018 or FY 2019 After Holdbacks | Eliminate Grants to the Wealthiest Communities | FY 2019 Recommended |
|-------------------------------|--|--|----------------------|
| State-Owned PILOT | -4,221,454 | -2,829,163 | 46,603,503 |
| College & Hospital PILOT | -6,950,294 | -1,284,936 | 95,131,701 |
| Pequot | -91,295 | -159,270 | 49,692,228 |
| Town Aid Road (TAR) | - | - | 60,000,000 |
| LoCIP | - | - | 34,999,926 |
| Grants for Municipal Projects | - | - | 60,000,000 |
| Muni Revenue Sharing | -1,597,321 | - | 35,221,814 |
| Municipal Transition | - | - | 15,000,000 |
| Municipal Stabilization | -4,749,008 | -1,499,654 | 30,082,074 |
| Education Cost Sharing (ECS) | - | -8,579,694 | 1,950,511,348 |
| Adult Education | - | -41,945 | 19,832,416 |
| Total | -17,609,372 | -14,394,662 | 2,397,075,010 |

This budget rolls out the FY 2018 holdbacks into FY 2019 and then reduces major statutory formula aid to municipalities by:

- Providing grants to municipalities at the lesser of the FY 2018 or FY 2019 post-holdback amounts; and
- Eliminating grants to the 33 municipalities with equalized net grand list per capita above \$200,000 or more, except for Alliance Districts which are held harmless from this reduction.

Education Cost Sharing (ECS)

The holdbacks applied to the total ECS grant in FY 2018 are annualized into FY 2019. The distribution of those holdbacks will be different on a town-by-town basis, however. The formula that was passed by the General Assembly in Public Act 17-2 (June Special Session) is largely unaltered except for two factors that affect the phase-in of the grant: the base by which towns are phased in, and the phase-in percentage. All other factors in the formula are unchanged. Rather than using the FY 2017 ECS grants as a basis of comparison for phasing in funding, the base has been updated to FY 2018 estimated grants. The phase-in percentage is now 8 percent rather than the 4.1 percent in statute.

Additionally, for FY 2019, ECS is further reduced based on town need as measured by the Equalized Net Grand List Per Capita (ENGLPC). For any town, other than an Alliance District, whose ENGLPC is greater than \$200,000, ECS funding is eliminated.

Restores Funding for Community Colleges

The adopted budget made significant reductions in FY 2019 to only one constituent unit of higher education: the community college system. The Governor recommends restoring \$6.25 million in funding, about half of the reduction the legislature adopted, providing the resources necessary for continued student success.

Other Budget Revisions

Enhancing Budget Transparency – Passport to the Parks

Public Act 17-2, (June Special Session) created the Passport to the Parks non-lapsing account that was to fund expenses of the Council on Environmental Quality, beginning with the fiscal year ending June 30, 2019, and for the care, maintenance, operation and improvement of state parks and campgrounds, the soil and water conservation districts and environmental review teams (ERT). Unfortunately, the law was drafted to require appropriation but none were made, making the program impossible to implement as required. The Governor's budget proposes to fix this problem by moving these government expenditures back on-budget through a separate appropriated fund called the "Passport to the Parks Fund." The Governor's proposal continues to finance these activities through a \$10 fee on passenger, motorcycle, motor home, combination or antique vehicle registrations, camping fees and out of state park admissions. Connecticut residents will be able to enter state parks for free with a Connecticut registered vehicle. Appropriations for the Department of Energy and Environmental Protection and the Council on Environmental Quality are included in the budget as follows:

| | FY 2019 |
|---|---------------------|
| Department of Energy and Environmental Protection | |
| Personal Services | \$ 4,101,924 |
| Park Operational Expenses | \$ 4,114,877 |
| Fringe Benefits | \$ 2,645,331 |
| Soil and Water Conservation Districts and ERTS | \$ 653,000 |
| Total - DEEP | \$11,515,132 |
| | |
| Council on Environmental Quality | |
| Personal Services | \$ 173,190 |
| Other Expenses | \$ 613 |
| Fringe Benefits | \$ 148,390 |
| Total - CEQ | \$ 322,193 |

Shoring up the System that Supports Connecticut's Workforce

Over the years, federal funding to support the Department of Labor's (DOL) programs has become insufficient, in part due to the underfunding of federal programs at the national level (most notably the unemployment insurance system), and partially due to rising fringe benefit costs. As a result, in FY 2016, DOL was forced to implement layoffs as a means to decrease expenditures.

In addition to the FY 2016 workforce reduction, the agency relied on its reserve funding to address the historical shortfalls. Over time those funds have diminished and the agency now requires additional resources to continue its operations. At this point, additional staff reductions are not a viable option as it would erode the agency's ability to provide adequate services to Connecticut residents.

To ensure Connecticut's workers maintain access to quality services, the Governor's budget establishes a 0.05 percent administrative assessment on employers, commencing January 1, 2019, to provide sustained funding for DOL's program operations. In FY 2019, the assessment is anticipated to result in approximately \$5 million and \$9 million when fully annualized. For employers, an administrative surcharge of 0.05 percent equates to a total cost of \$7.50 per year for each employee earning at least \$15,000. For example, an employer with 10 employees earning at least \$15,000 a year would pay an additional \$75 per year.

The proposal to establish an administrative surcharge is not unique. According to the United States Department of Labor, thirty other states impose an assessment for a variety of uses such as administration and workforce training.

To ensure there will be adequate resources in FY 2019, the budget includes a \$500,000 appropriation to DOL until the revenue from the assessment is fully annualized.

Investing in Connecticut's Economy through Enhanced Tourism

For FY 2019, Governor Malloy's budget maintains funding for arts and tourism programs. The budget also continues to invest in marketing Connecticut as a premier destination for tourism and business growth. To that end, the budget increases the hotel occupancy tax two percent to provide dedicated funding for the Tourism Fund.

Funding for Statewide Marketing is increased to \$8 million, nearly double the amount included in the enacted FY 2019 budget. In recent years, investments in marketing have proven invaluable in developing this job-rich sector of our economy, particularly in southeastern Connecticut with its wide array of tourist destinations.

Reorganizing State Agencies

The recommended budget completes two agency reorganizations directed in Public Act 17-2 (June Special Session). The State Unit on Aging and the Office of the Long Term Care Ombudsman were originally transferred to DSS and OPM, respectively. The Governor instead recommends their consolidation under the Department of Rehabilitation Services to follow the federal model for placing aging and disability agencies together.

In addition, the budget transfers the remaining resources necessary to complete the new Office of Health Strategy. Staff and resources from the Office of Health Care Access, the Statewide Innovation Model initiative and the health information technology officer form the agency. This new office will enhance coordination and consolidate accountability for the implementation of the state's health care reform strategies.

This budget also consolidates OHE as the Division of Post-Secondary Education within SDE. This reorganization will enhance and solidify the continuum of pre-K to post-secondary education in Connecticut. Many of OHE's programs, including the National Service Act, the Minority Advancement Program, and the Minority Teacher Incentive Program, complement ongoing efforts at SDE. The two agencies are co-located in the same building, and the merger will facilitate this coordination through the use of shared services, and result in a \$300,000 savings by eliminating four positions and associated other expenses.

Helping Families Displaced by Hurricane Maria and Sustaining Subsidized Assisted Living

Governor Malloy's budget provides funding to support families displaced from their homes by Hurricane Maria. During this time of crisis for our fellow citizens, Connecticut welcomed individuals and families displaced by the tragic event. While the Federal Emergency Management Agency provided temporary assistance, they abruptly ceased aid leaving families vulnerable during difficult times. In order to continue to support these displaced evacuees, Governor Malloy's budget provides \$400,000 for housing and rental assistance.

The budget also provides increased support for the Subsidized Assisted Living Project. Increases in debt service costs are funded to ensure low-income seniors remain in community-based housing settings rather than more costly nursing home care.

Enhancing Funding for Chief Medical Examiner

Currently, the autopsy caseload per medical examiner exceeds standards established by the National Association of Medical Examiners. Funding of \$180,000 is provided to hire an additional pathologist and reduce caseloads.

Improving Inmate Nutrition

Governor Malloy is proposing \$1.5 million – a 10 percent increase in funding – for the Department of Correction's food budget to enhance nutrition for inmates. Health professionals caution that poor diet

can lead to a host of health problems such as diabetes, heart disease and obesity. The investment in improved nutrition is preventative – eating healthier meals while incarcerated and continuing to do so once returning to the community not only improves the individual’s well-being, it results in long-term cost savings to the state. Because an overwhelming majority of those incarcerated are eligible for the Medicaid program upon release, improved health and nutrition will translate to reduced healthcare costs.

Ensuring the Success of New Legislative Requirements by Ensuring Adequate Staffing

The Governor proposes additional resources to support new boards and commissions that were included in the enacted budget for the biennium. In the Office of the State Treasurer, \$90,000 is provided for an additional staff person to assist with the requirements of various pension and fiscal reform working groups and the Municipal Accountability Review Board. In OPM, approximately \$596,000 is recommended for additional staff resources to meet the requirements of recently passed legislation including the all-payer claims database, an annual report that analyzes rates of recidivism in children, a pilot program for testing fully autonomous vehicles, the municipal grant portal, and support for the Municipal Accountability Review Board.

Adjusting Funding for FY 2018 Deficiencies

A number of budget shortfalls are anticipated in FY 2018, largely in Personal Services and Other Expenses, and the following adjustments are proposed to the enacted budget for FY 2019 to ensure sufficient funding is available:

- Division of Criminal Justice – The proposed revisions provide \$400,000 in Personal Services;
- Department of Correction – A total of \$9.8 million is added, with \$8.0 million in Personal Services and \$1.8 million in Other Expenses. Budgeted funds for this agency are insufficient to support current staffing and operating costs;
- Public Defender Services Commission – A \$250,000 adjustment is proposed in Personal Services; and
- Department of Administrative Services – Approximately \$27,000 is added to the Employee Review Board account due to increased hearings.

Gubernatorial Transition Expenses

In order to assist with the transition to a new administration in January 2019, the Governor is proposing \$100,000 be added to the budget of the Office of the Governor. This funding will enable the next administration to ensure appropriate staffing and other necessities are available in a timely manner and will help make the transition seamless.

Revenue Proposals

The Governor's revenue proposals fall into four main categories: restoring balance to FY 2019, reducing out-year budget gaps, addressing recent federal tax changes, and investing in transportation infrastructure.

In order to restore balance to the FY 2019 budget, the Governor is proposing revenue measures totaling \$234.6 million. These include extensions of revenue options already utilized in the biennial budget, including measures related to the property tax credit, cigarettes and other tobacco products, and the hotel occupancy tax supporting the tourism fund. It also makes common sense changes, such as modifications to minimum bottle pricing, which the Governor has previously supported and would benefit consumers.

The Governor is proposing changes to revenue measures in the recently passed biennial budget which would severely reduce the out-year budget gap created by the legislation. Without any action, sun-setting provisions and newly created tax preferences that weren't programmed until FY 2019 or FY 2020 will cost the state hundreds of millions of dollars. This proposal recognizes that state government should not make future promises it can't keep. The Governor recommends eliminating unaffordable new exclusions from the personal income tax and poorly targeted economic development measures such as the 7/7 brownfield tax credit program. As a result, passage of the Governor's proposal would close the current out-year budget gap by nearly \$1.2 billion in FY 2020, \$1.3 billion in FY 2021, and \$1.4 billion in FY 2022. As a result, the budgetary gap faced by the Governor's successor will be significantly lower than the one facing the Governor when he entered office.

In addition, the Governor is proposing several changes in response to the Federal Tax Cuts and Jobs Act of 2017. Decoupling from certain provisions in the federal code will prevent a revenue loss to the state. In addition, a new personal income tax credit offsetting a tax on pass-through entity income will provide small businesses in the state with better tax treatment at the federal level, thereby increasing Connecticut's competitiveness. A provision allowing municipalities to create charitable organizations supporting local interests will give our cities and towns flexibility to continue to provide the services we rely on under the new federal rules.

Finally, the Governor is proposing increases in STF revenue which will facilitate needed maintenance and upgrades to the state's transportation system. As vehicles have become increasingly fuel efficient, the effective motor fuels tax rate on road travel has steadily decreased since the last time the tax was raised in 1997. The Governor proposes increasing the motor fuels tax rate and instituting tolling on our roads. These changes will ensure that the STF is financially stable both today and in the future, allowing Connecticut to build a bridge to the economy of tomorrow.

Capital Proposals

Governor Malloy is proposing \$141 million in additional general obligation (GO) bond authorizations in FY 2019. These proposed bond authorizations are in addition to those that were previously authorized by the General Assembly and become effective in FY 2019, which include \$1.295 billion for various projects and programs, \$200 million for the Next Generation Connecticut/ UConn 2000 program, \$95 million for the CSCU 2020 program, \$12.5 million for the Bioscience Collaboration Program and \$15 million for the Bioscience Innovation Fund. These authorizations are offset by the cancellation of an existing \$40 million in GO bond authorizations.

New proposed GO bond authorizations are:

- \$100 million to continue rehabilitation of the XL Center in Hartford;
- \$25 million to continue information technology improvements in state agencies; and
- \$16 million to construct parking to support redevelopment projects in Hartford.

Alternatives to the Governor's Recommended Revisions

Inevitably, the Governor's proposed FY 2019 budget revisions must be considered by the legislature, which will object to some recommendations and modify others. Those who advocate a different approach to balancing the budget have a range of options to consider in place of the specific spending reductions and revenue increases recommended here. While these alternatives are NOT part of the Governor's proposed revisions, it is instructive, and perhaps helpful to the legislature, to identify some options that they might also consider in achieving a balanced budget. In the General Fund, these alternatives could include:

- Increasing the sales and use tax rate, which is currently 6.35 percent;
- Allowing grocery stores to sell wine;
- Increasing excise taxes on liquor and beer;
- Temporary or even permanent diversion of Community Investment Act funds, perhaps coupled with bringing any remaining spending associated with these programs on-budget to increase transparency;
- Reducing hospital Medicaid rates and/or supplemental payments;
- Re-closing enrollment to the Care 4 Kids program;
- Reduction in services or further privatization of behavioral health care and developmental disability services;
- Eliminating funding for the Renters Rebate program;
- Requiring towns to contribute toward the Teachers' Retirement System;
- Further reducing municipal aid; and
- Legalizing and taxing the recreational use of marijuana.

In the STF, the alternatives to the Governor's proposals to assure both the near- and long-term solvency of the fund and to support transportation infrastructure renewal efforts are clear:

- Increasing rail fares;
- Increasing bus fares;
- Reducing or eliminating transit subsidies;
- Eliminating Shore Line East rail service;
- Reducing or eliminating New Haven branch line rail service, including weekend and off-peak service;
- Closing highway rest areas;
- Eliminating non-ADA service; and
- Cancelling or deferring vital projects like the Hartford Viaduct replacement and Waterbury Mixmaster.

These alternatives in the STF reflect actions that the administration has already begun to undertake and must continue until additional revenues are provided by legislative action.

Conclusion

Governor Malloy is proposing an all funds budget of \$20.73 billion for FY 2019. This is \$70.5 million, or 0.3 percent, above the adopted budget for FY 2019 and only 1.4 percent above the estimated level of FY 2018 expenditures. This is under the projected inflation rate for FY 2019 of 1.6 percent. The recommended budget is \$170.2 million below the spending cap for FY 2019.

Including this budget proposal, expenditures under Governor Malloy have grown by 2.5 percent per annum, well below the rate of growth of the two immediately preceding administrations (40 percent and 47 percent below the two prior administrations). This low growth rate is even more remarkable given the aggressive steps taken under Governor Malloy to address long term liabilities.

SUMMARY OF APPROPRIATION CHANGES

(In Millions)

| | Enacted ³ Appropriation <u>FY 2019</u> | Net Adjustments <u>FY 2019</u> | Recommended Appropriation <u>FY 2019</u> | % Growth Over <u>Enacted</u> |
|--|---|--------------------------------------|--|------------------------------------|
| General Fund | \$ 18,790.6 | \$ 65.4 | \$ 18,856.0 | 0.3% |
| Special Transportation Fund | 1,628.1 | (8.3) | 1,619.8 | -0.5% |
| Banking Fund | 27.4 | 0.4 | 27.8 | 1.4% |
| Insurance Fund | 95.0 | (3.5) | 91.6 | -3.7% |
| Consumer Counsel and Public Utility Fund | 25.6 | 0.1 | 25.7 | 0.4% |
| Workers Compensation Fund | 24.9 | 1.2 | 26.1 | 4.7% |
| Mashantucket Pequot & Mohegan Fund | 49.9 | (0.3) | 49.7 | -0.5% |
| Regional Market Operating Fund | 1.1 | - | 1.1 | 0.0% |
| Criminal Injuries Compensation Fund | 2.9 | - | 2.9 | 0.0% |
| Passport to the Parks Fund ¹ | - | 11.8 | 11.8 | N/A |
| Tourism Fund ² | <u>12.6</u> | <u>3.6</u> | <u>16.3</u> | <u>28.8%</u> |
| Total | \$ 20,658.2 | \$ 70.5 | \$ 20,728.7 | 0.3% |

Notes:

¹ Passport to the Parks Fund is not appropriated in FY 2018 or FY 2019. The Governor recommends appropriating this fund.

² Tourism Fund is effective beginning FY 2019.

³ Enacted FY 2019 appropriation per Public Act 17-2 (June Spec. Sess.) as amended by Public Act 17-4 (June Spec. Sess.).

General Fund

The recommended revised General Fund budget for FY 2019 provides a \$4.0 million operating surplus and is \$65.4 million above the adopted budget for FY 2019. The recommended budget for FY 2019 is only 0.7 percent above the level of estimated FY 2018 expenditures.

GOVERNOR'S BUDGET PLAN

(In Millions)

| | Estimated FY 2018 | Appropriated FY 2019 | Revised Recommended FY 2019 |
|------------------------------------|----------------------|-------------------------|-----------------------------------|
| <u>General Fund</u> | | | |
| Total Recommended Budget | | | |
| Revenues | \$ 18,479.6 | \$ 18,908.2 | \$ 18,860.0 |
| Appropriations | <u>18,719.8</u> | <u>18,790.6</u> | <u>18,856.0</u> |
| Surplus/(Deficit) | \$ (240.2) | \$ 117.6 | \$ 4.0 |
| Proposed Adjustments | | | |
| Deficit Mitigation Measures | <u>\$ 240.2</u> | <u>\$ -</u> | <u>\$ -</u> |
| Total Changes | \$ 240.2 | \$ - | \$ - |
| Revised Surplus/(Deficit) | \$ 0.0 | \$ 117.6 | \$ 4.0 |
| <u>Special Transportation Fund</u> | | | |
| Beginning Balance | \$ 97.6 | \$ 154.5 | \$ 154.5 |
| Revenues | <u>1,554.2</u> | <u>1,628.1</u> | <u>1,635.3</u> |
| Total Available Resources | 1,651.8 | 1,782.6 | 1,789.8 |
| Recommended Appropriations | <u>1,497.3</u> | <u>1,628.1</u> | # <u>1,619.8</u> |
| Surplus/(Deficit) | \$ 56.9 | \$ 0.0 | \$ 15.5 |
| Projected Fund Balance 6/30 | \$ 154.5 | \$ 154.5 | \$ 169.9 |

The January 2018 consensus revenue forecast by OPM the legislature's Office of Fiscal Analysis, which forms the basis for the revenues in this budget, is projected at \$18,625.4 million in FY 2019. Revenue revisions totaling a net \$234.6 million are proposed, and the recommended revenues for this budget total \$18,860.0 million.

Special Transportation Fund

The recommended revised STF budget for FY 2019 includes a \$15.5 million operating surplus and is \$8.3 million below the adopted budget for FY 2019. The recommended budget for FY 2019 is 0.5 percent below the adopted budget, and 8.2 percent above the level of estimated FY 2018 expenditures. Revenues included as part of the January 2018 consensus forecast are projected at \$1,588.2 million in FY 2019. Revenue revisions totaling \$47.1 million are proposed, and the recommended revenues for this budget total \$1,635.3 million.

Budget Reserve Fund

The state's Budget Reserve Fund ended FY 2017 with a balance of \$212.9 million, or 1.1 percent of General Fund appropriations. If the legislature acts to address the projected deficit for FY 2018 without drawing down our reserves, based on the Governor's budget plan and the current consensus revenue forecast the Rainy Day Fund will grow to \$894.9 million, or an estimated 4.6 percent, by the end of FY 2019.

