CONNECTICUT
Policy and Management

Fiscal Accountability Report
FY 2025 – FY 2028

Secretary Jeffrey R. Beckham
December 9, 2024

Presentation Overview

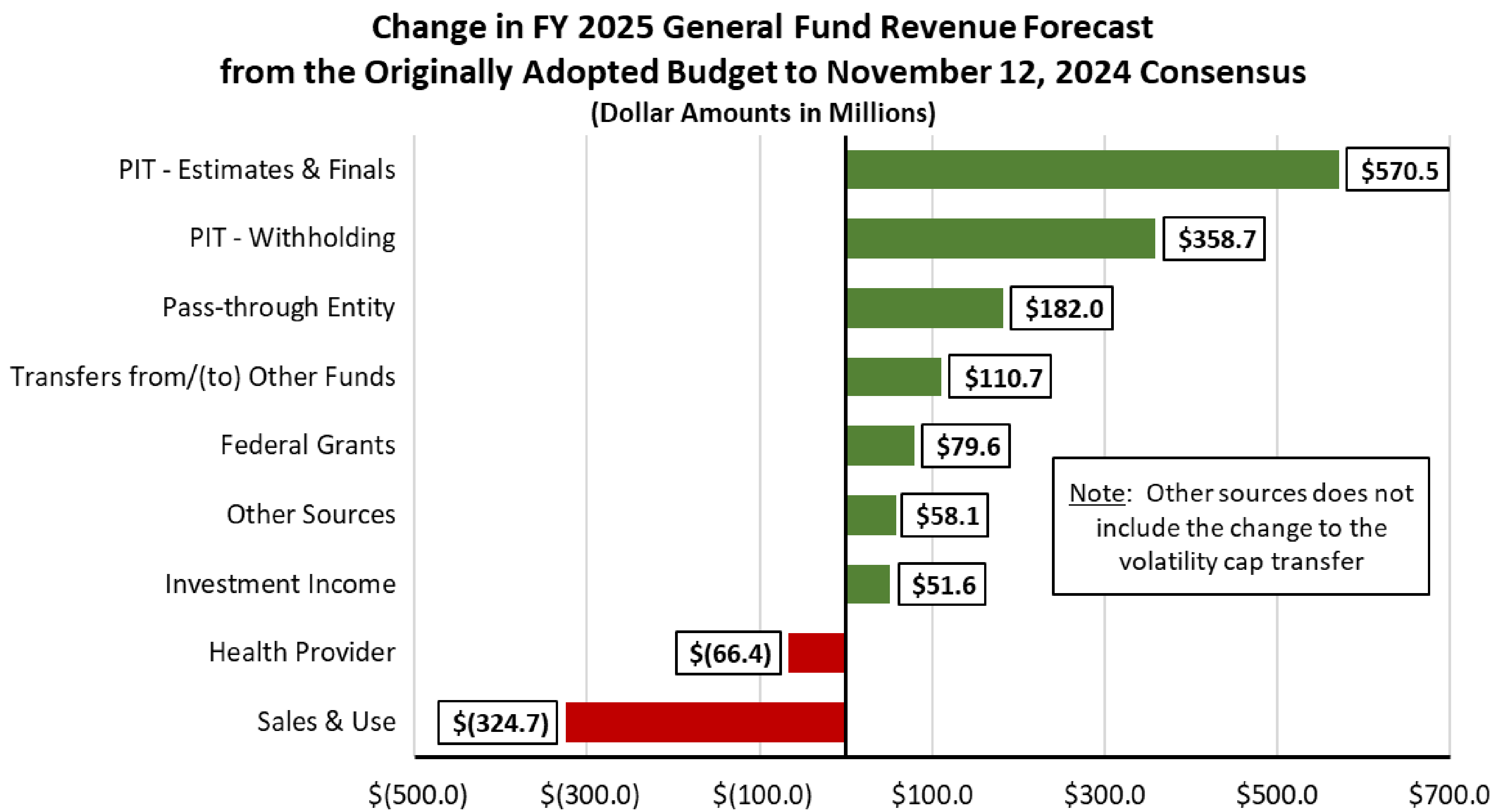
- FY 2025 Operating Projections
- Estimates of FY 2026 – FY 2028 Revenue and Fixed Cost Growth
- Long-term Liabilities and "Fixed Cost" Drivers
- Conclusion and Key Takeaways

Summary of Findings

- FY 2025
  - Operating surpluses are anticipated in both General Fund and Special Transportation Fund
  - General Fund spending exceeds current year appropriations by $383.7 million and now stands $1.08 billion (4.9%) above initial FY 2024 appropriations
- FY 2026 – FY 2028
  - Total General Fund revenue growth is slightly below fixed cost growth for FY 2026, but greater than fixed cost growth in FY 2027 and 2028
    - Growth in Medicaid and retiree healthcare are the largest contributors to fixed cost growth for FY 2026 and FY 2027
  - Revenue growth in the Special Transportation Fund does not keep pace with the growth in fixed costs for debt service on transportation projects
- Long-Term Liabilities
  - Additional contributions to pension funds since 2020 total $8.6 billion and have reduced contribution requirements by $730 million annually
  - Additional contributions to pension funds have significantly reduced long-term pension debt, though funding levels remain below nearly all other states

FY 2025 Operating Results

FY 2025 General Fund Revenue Changes



- **Overall FY 2025 General Fund revenues are up $276.2 million compared to the originally adopted budget**

FY 2025 Estimated Results – General Fund

	FY 2025 Projection (in millions)		
General Fund	Budget	Nov. Estimate	Nov. Est. Variance from Budget
Revenues	$ 23,103.7	$ 23,379.9	$ 276.2
Expenditures	22,805.9	23,189.6	383.7
Operating Results - Surplus/(Deficit)	$ 297.8	$ 190.3	$ (107.5)

Key Reasons for Expenditure Variance:

- No midterm budget adjustments were adopted: Governor's 2/7/24 Proposed Budget would have addressed ~$200 million in expenditure growth
- Since last winter, the projected Medicaid shortfall has continued to trend upward: from an estimated $106.8 million last February to $240 million today
- Staffing levels have continued to grow rapidly and are now above the pre-pandemic FY 18-20 levels that were funded in the budget

FY 2026–2028 Fixed Cost vs Revenue Growth

General Fund Fixed Cost Growth vs. Revenue Growth

(in millions)

	FY 2026 vs. FY 2025	FY 2027 vs. FY 2026	FY 2028 vs. FY 2027
Revenue Growth	$ 499.8	$ 691.7	$ 752.2
Fixed Cost Growth			
Medicaid	$ 167.3	$ 154.3	$ 156.8
State and Teacher OPEB	188.6	159.2	31.0
Debt Service	14.1	122.2	100.5
Other Entitlements	98.6	25.2	27.5
Teacher Pensions	53.7	50.0	(30.7)
State Employee Pensions	(19.2)	18.8	19.8
Total Fixed Cost Growth	$ 503.1	$ 529.5	$ 304.9
Difference	$ (3.3)	$ 162.2	$ 447.3

- Revenue growth for FY 2026 is slightly less than fixed cost growth, primarily as a result of the use of one-time funds in FY 2025
- Revenue growth exceeds fixed cost growth beginning in FY 2027
- Medicaid and retiree healthcare costs are the largest drivers of fixed-cost growth
- Growth in costs not categorized as fixed are anticipated to create significant budgetary challenges next biennium

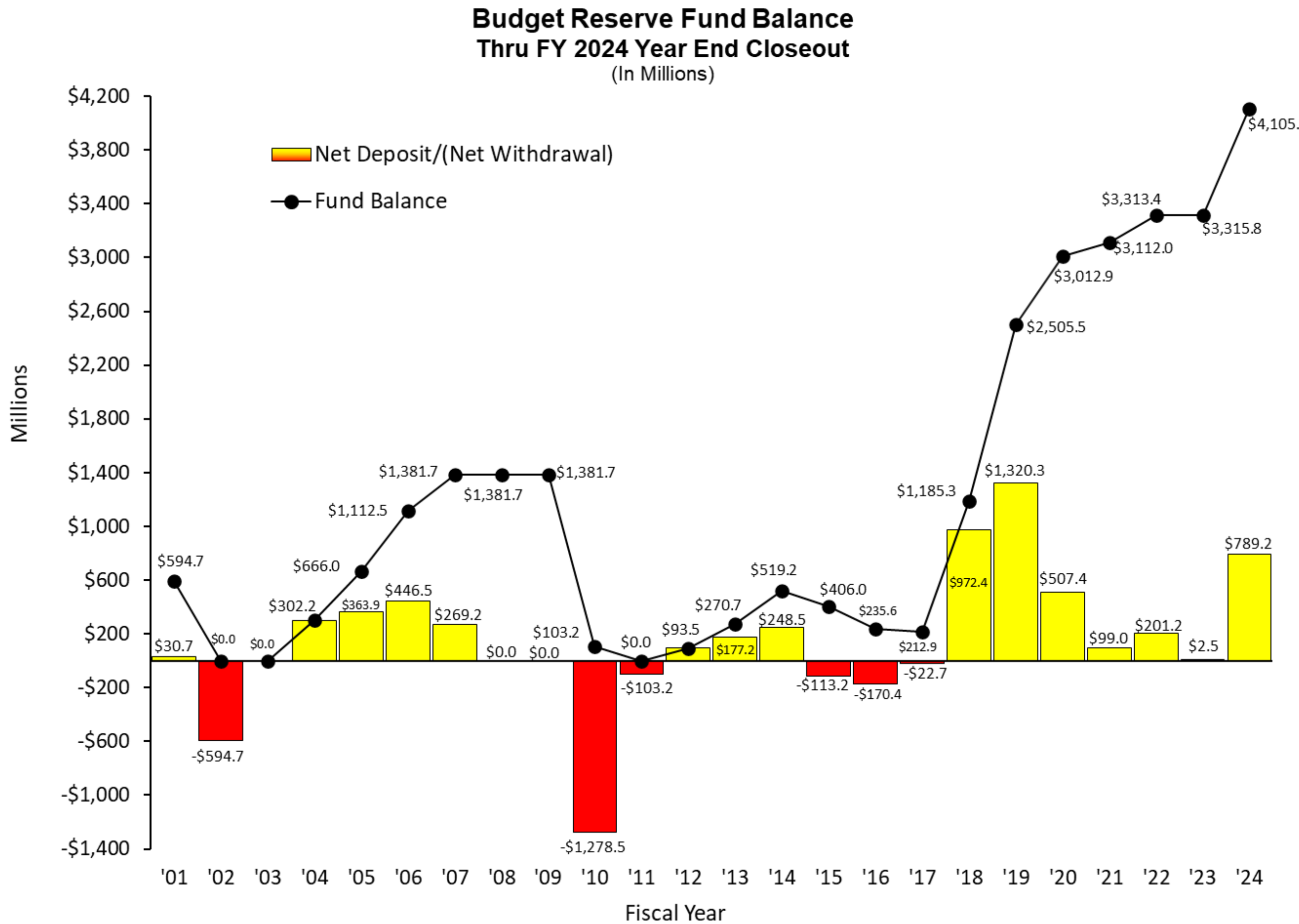
Special Transportation Fund Fixed Cost Growth vs. Revenue Growth

(in millions)

	FY 2026 vs. FY 2025	FY 2027 vs. FY 2026	FY 2028 vs. FY 2027
Revenue Growth	$ 5.6	$ 31.1	$ 30.5
Fixed Cost Growth			
Debt Service	$ 53.3	$ 107.8	$ 100.9
State Employee Pensions	(2.7)	1.0	1.1
Total Fixed Cost Growth	$ 50.6	$ 108.7	$ 101.9
Difference	$ (45.0)	$ (77.6)	$ (71.4)

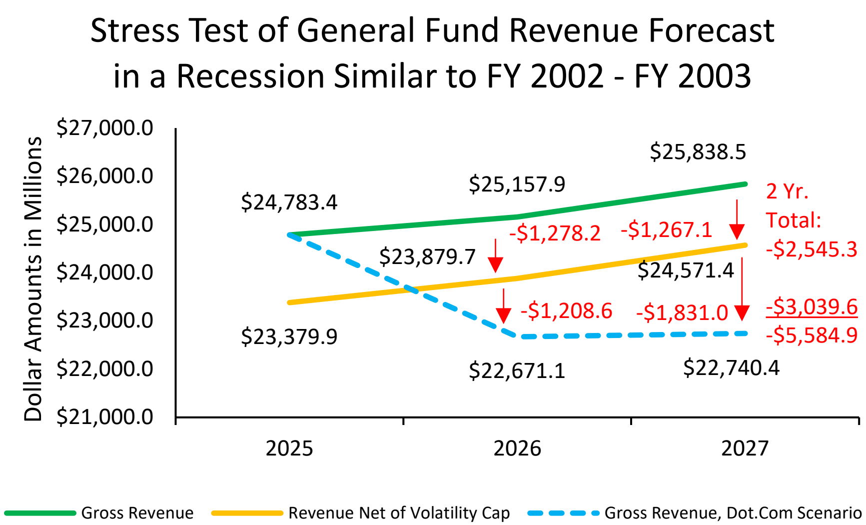
- Revenue growth will not keep pace with rising debt service costs in the Special Transportation Fund
- Without the introduction of alternative financing, additional revenue, or reductions in transportation investments, the expected increase in costs will not be sustainable

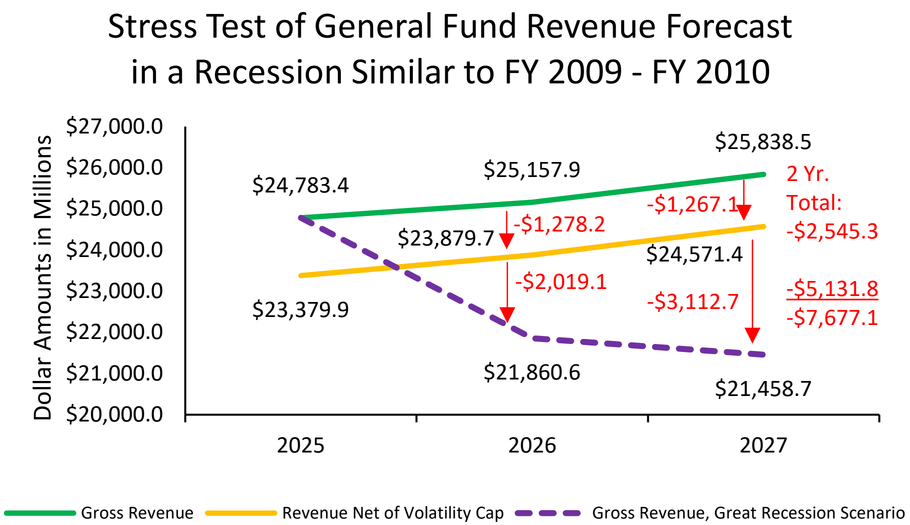
Budget Reserve Fund



- Beginning with the closeout of FY 2024, any amounts between 15% and 18% are to be split between the Budget Reserve Fund and the unfunded liabilities of SERS and/or TRS until the BRF is at 18%
- Following the closeout of FY 2024, the Budget Reserve Fund is at the new 18% statutory limit

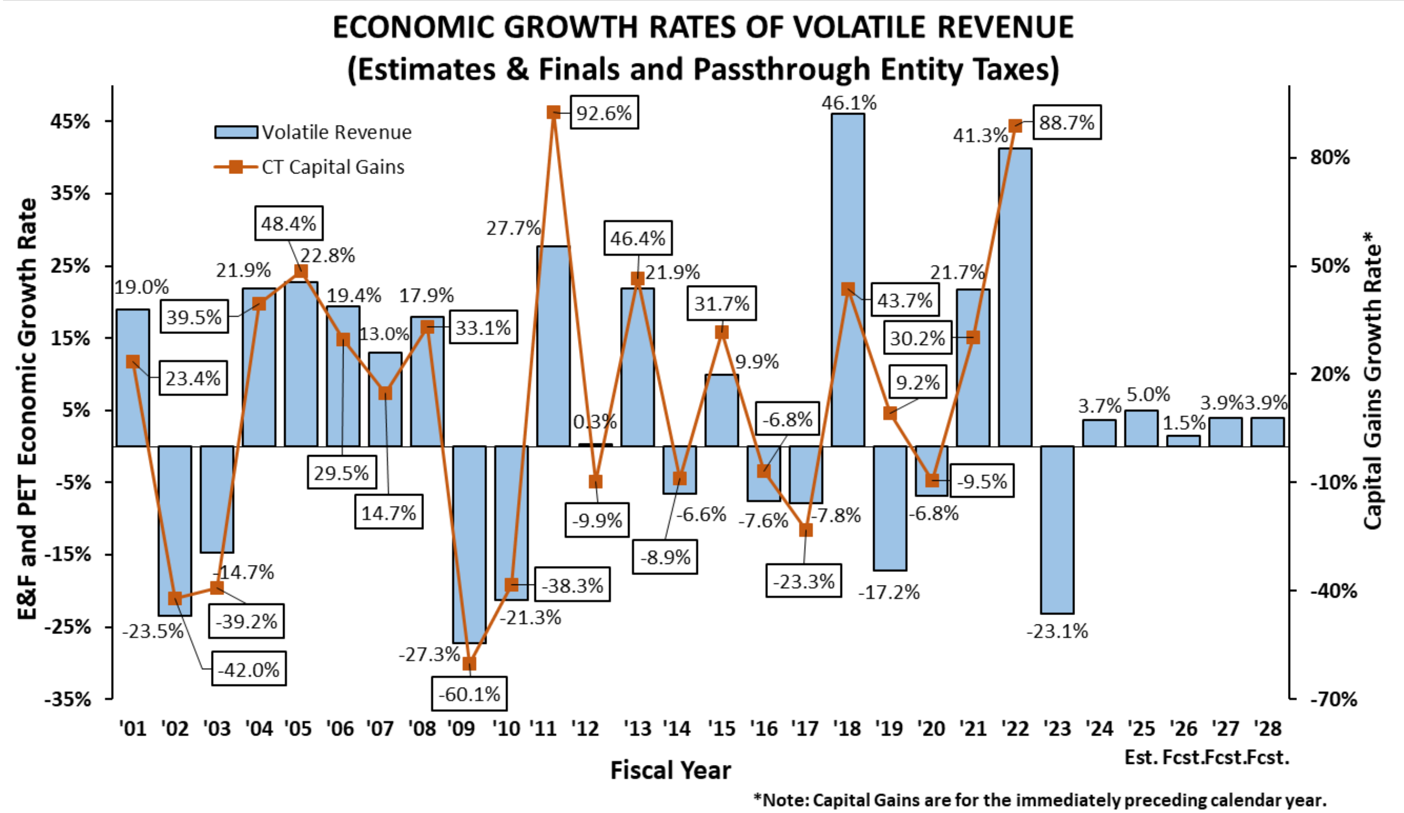
General Fund Stress Test





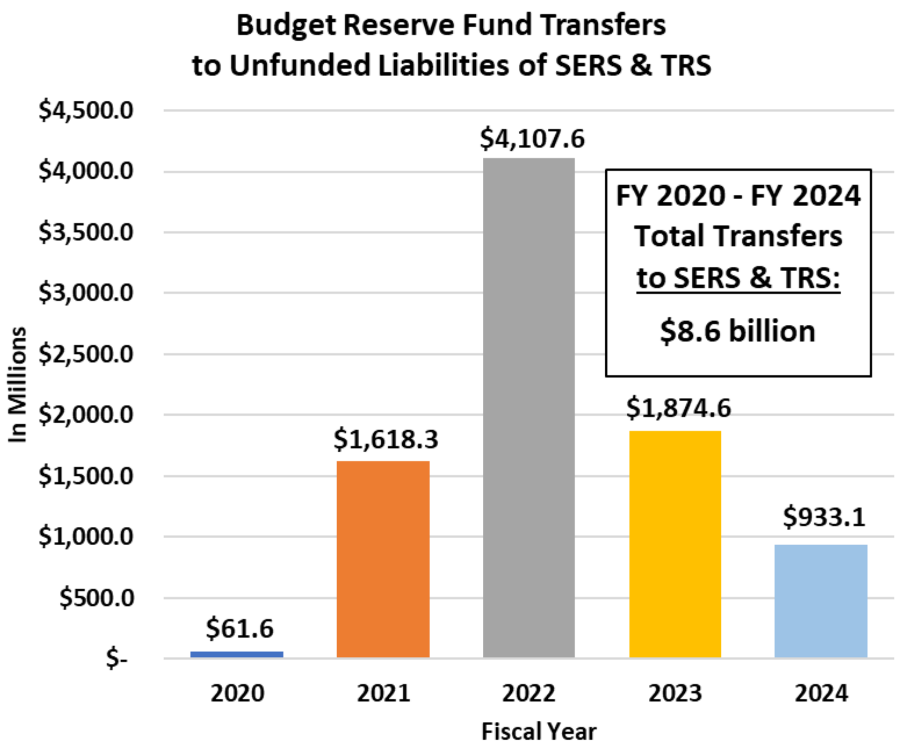
- The above graphs simulate the impact of a recession on Connecticut's revenue forecast
- Recessions similar to the Dot.com and Great Recession would result in a net reduction in General Fund revenue of $3.0 to $5.1 billion
- In addition, $2.5 billion in revenue subject to the current volatility cap would be lost
- Finally, revenues may not immediately return to the pre-recession trend after the 2 years depicted above and could remain on a lower trajectory in the outyears
    - For example, revenues took 5 years to return to their prerecession peak after the Great Recession, excluding policy changes

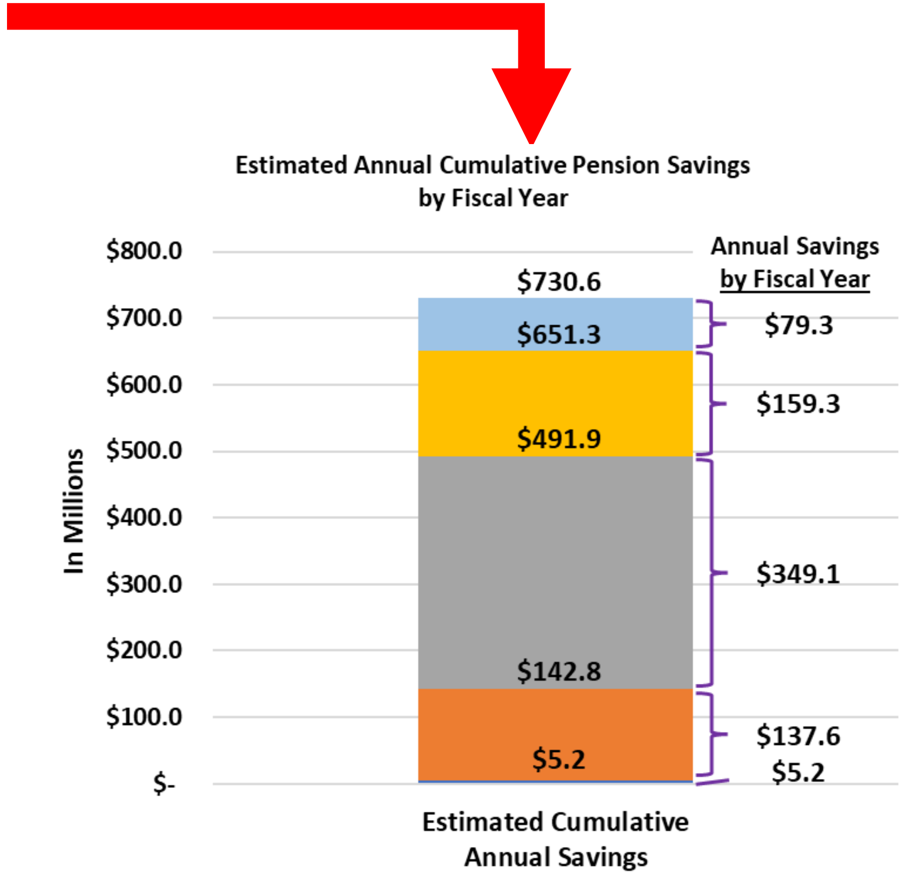
Growth Rates of Volatile Revenues



- The estimated & finals portion of the income tax and the pass-through entity tax are subject to the volatility cap
- Currently, those sources represent approximately one quarter of net General Fund tax revenue
- Receipts are highly correlated with capital gains, and as a result, are highly volatile
- In FY 2025, 73.7% of volatile revenues will be deposited to the General Fund with the remaining 26.3% subject to the volatility cap (based on November 2024 consensus figures)

Additional Contributions to Unfunded Liabilities (Above ADEC)

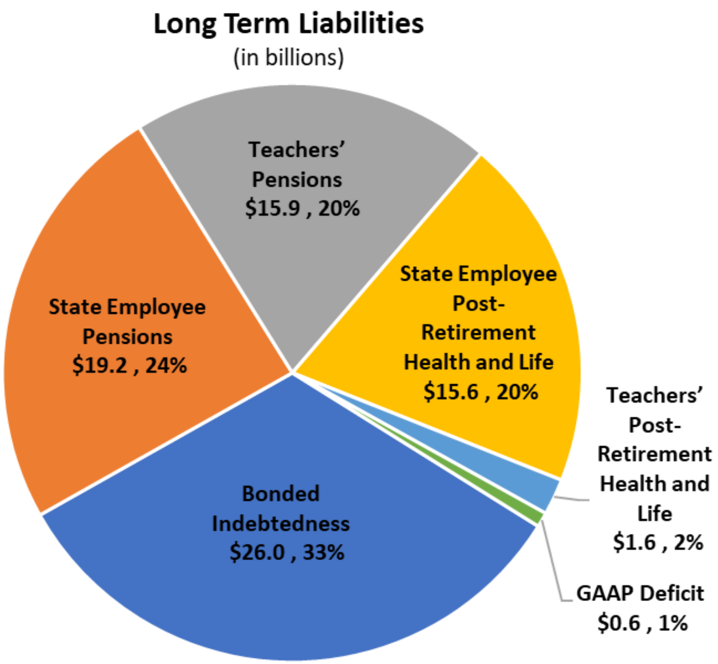




- Almost $8.6 billion has been deposited in SERS and TRS over the past 5 years as a result of BRF reaching the old 15% statutory limit and the new 18% statutory limit at the close out of FY 2024, reducing the state's required contributions by $730.6 million annually for 25 years

Long-Term Liabilities

Long-Term Liabilities

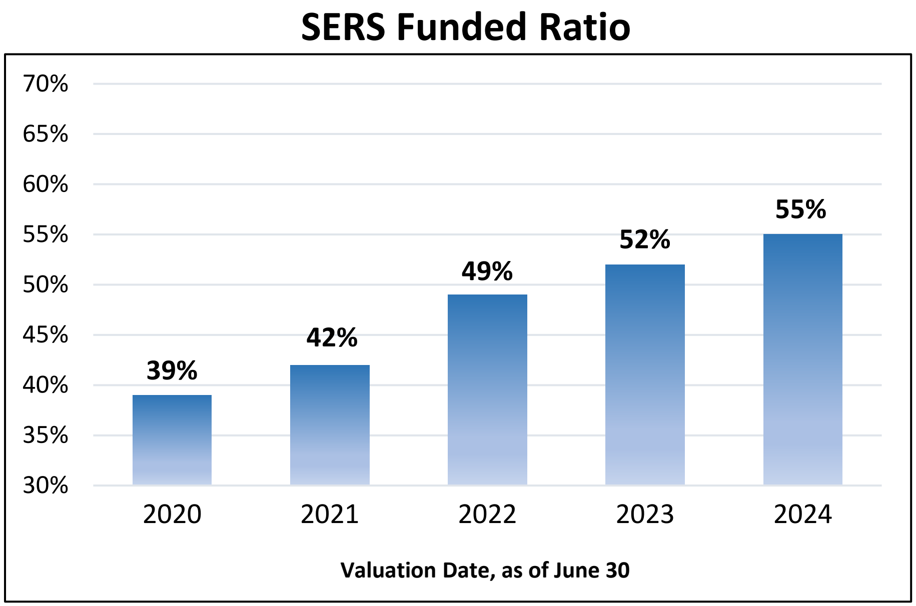


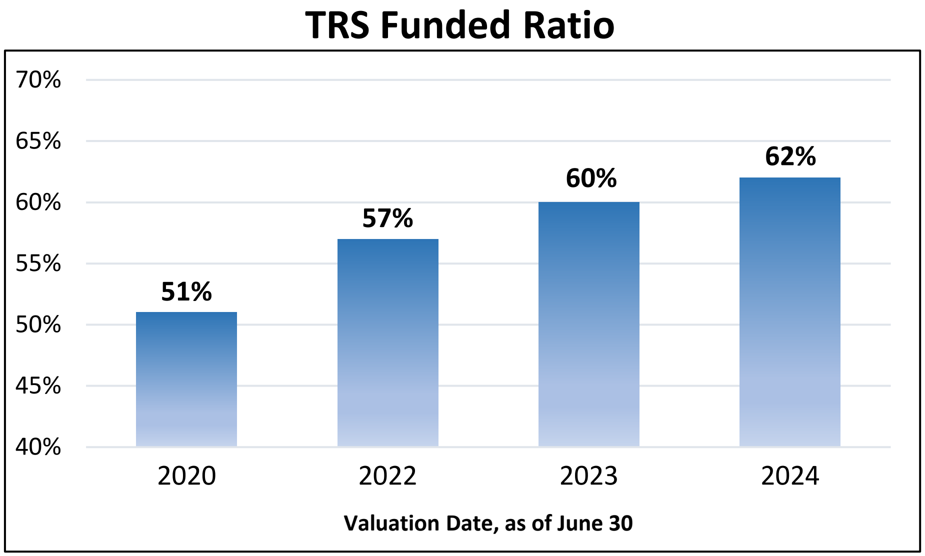
- Long-term liabilities total $79.8 billion
- Down $1.8 billion from last year's FAR and $15.6 billion from the 2021 report
- Over just three years, that represents a nominal decrease of 16% (28% in real dollars)

$ in billions

Long-Term Liability	Nov 2021 FAR	Nov 2022 FAR	Nov 2023 FAR	Nov 2024 FAR
Bonded Indebtedness	$ 27.2	$ 27.0	$ 26.4	$ 26.0
State Employee Pensions	22.7	22.4	20.9	20.1
Teachers' Pensions	18.1	17.1	16.4	15.9
State Employee Post-Retirement Health and Life	23.5	19.5	15.5	15.6
Teachers' Post-Retirement Health and Life	2.8	1.6	1.6	1.6
GAAP Deficit	1.1	0.7	0.8	0.6
Total	**$ 95.4**	**$ 88.3**	**$ 81.6**	**$ 79.8**

Pension Funding Progress

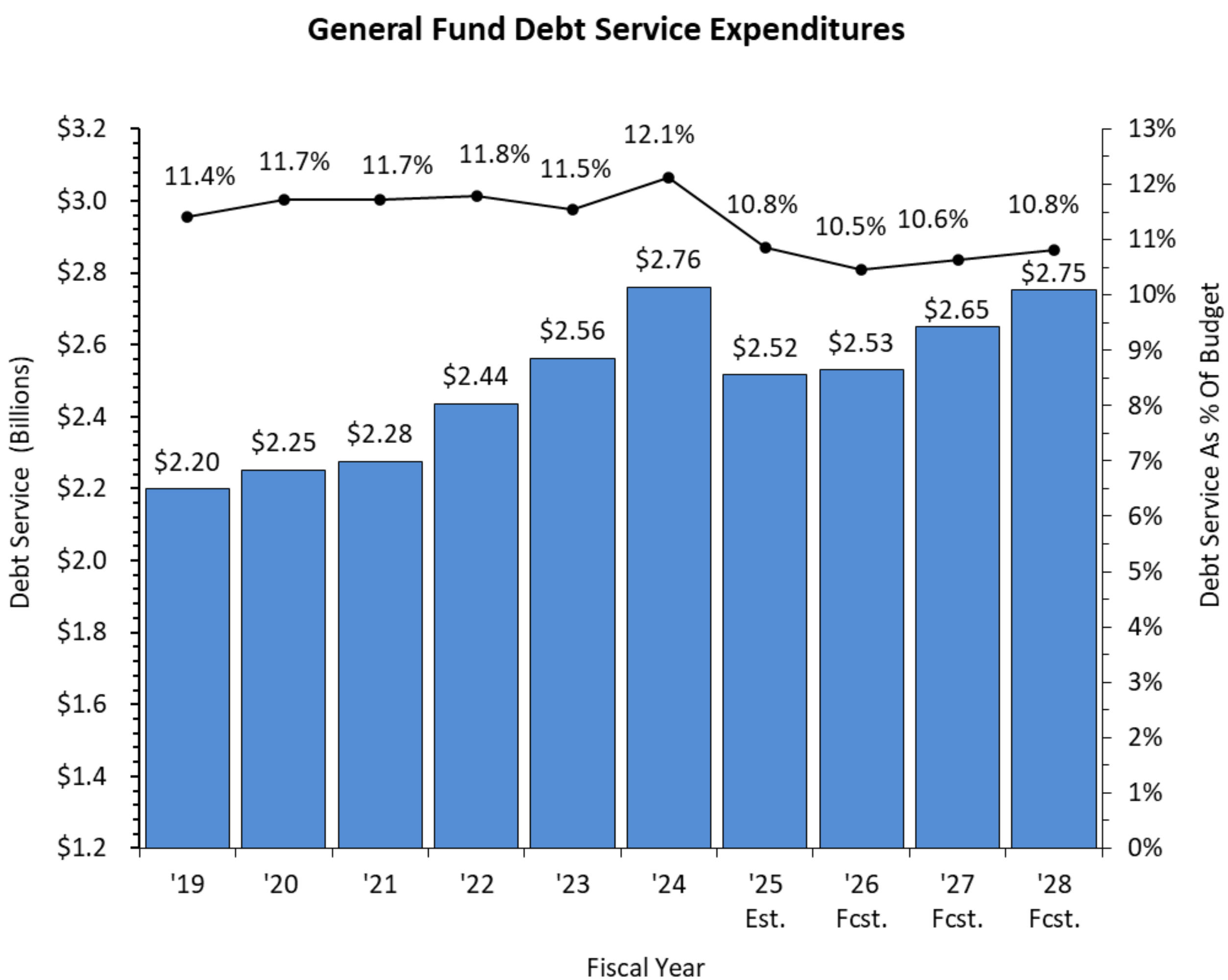




- Additional contributions beyond the annual actuarial required levels have generated significant improvements in SERS' and TRS' funded ratios

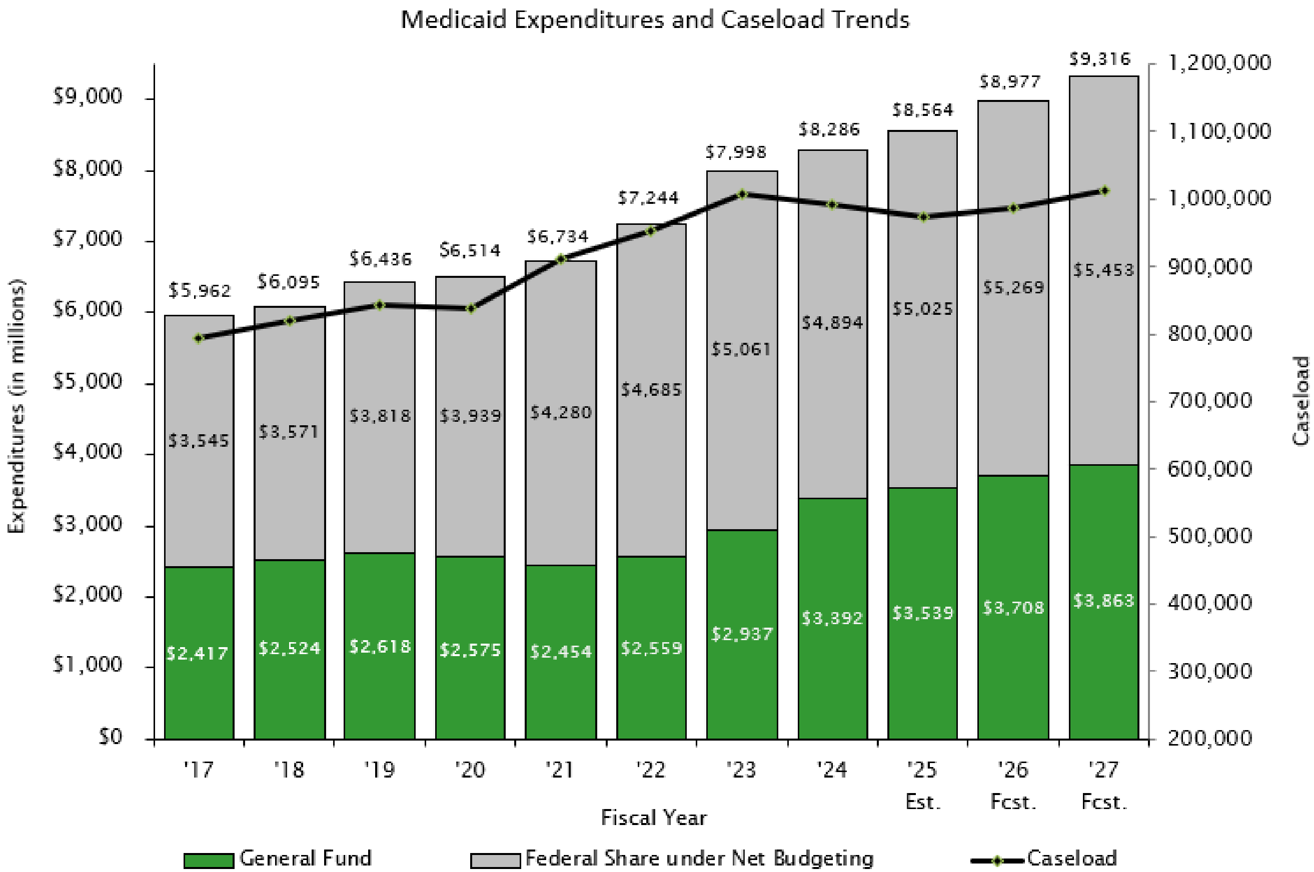
- A funded ratio of 80% is often considered a minimum for healthy pension plans

Debt Service



- Debt Service is expected to remain flat over the next two fiscal years
- FY 2024 includes the payment of the GAAP Conversion Bonds of $211.7 million
- Projections of debt service remain stable, below 11% as a percent of budget out to FY 2028

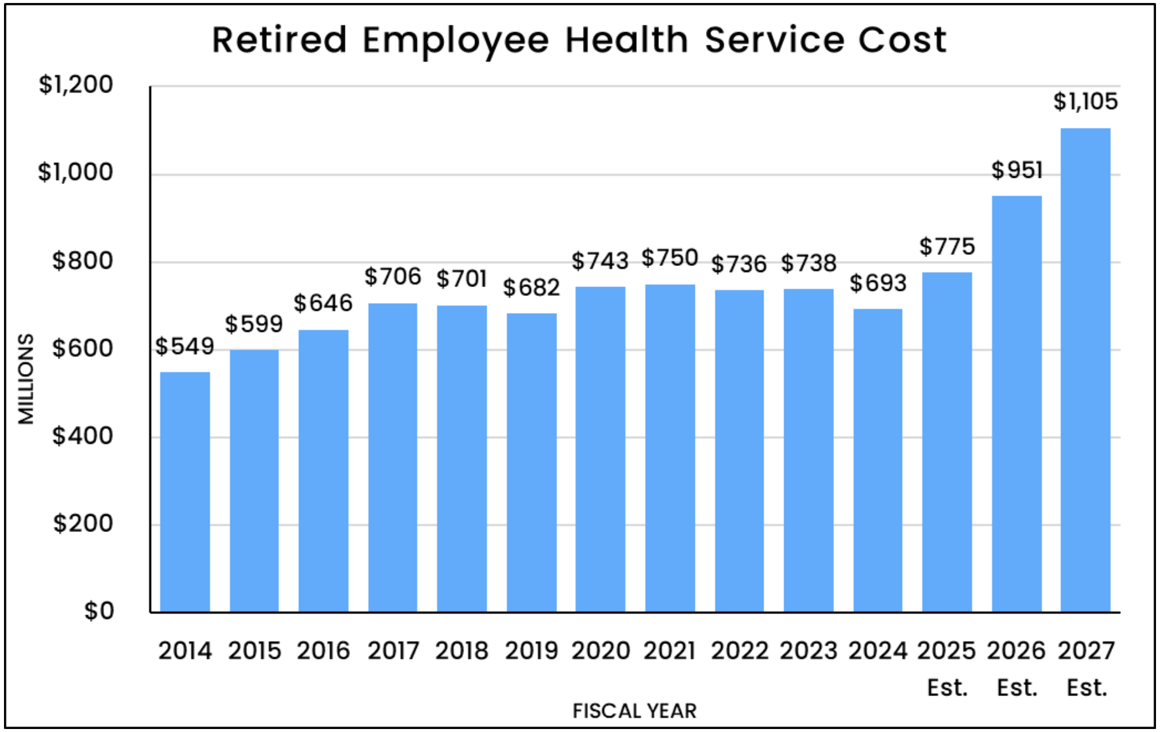
Medicaid



- Enrollment grew significantly during the pandemic, but expenditures did not due to lower overall service utilization
- Since then, enrollment remains higher than pre-pandemic levels and utilization continues to trend upward
- The projected Medicaid shortfall for FY 2025 has increased from $106.8 million last February to $240 million today

- Expenditures have been adjusted to include funds transferred to DSS from DMHAS for behavioral health services which qualify for Medicaid reimbursement but exclude hospital supplemental payments given the significant variance in that area over the years. Caseload figures exclude the limited benefit COVID-19 testing group
- Beginning in calendar year 2020, General Fund requirements were reduced due to enhanced federal reimbursement of 6.2% related to the public health emergency; this enhanced reimbursement was phased out over the three quarters ending December 31, 2023

Retiree Health Service Costs



- The number of Medicare eligible State of CT retirees and CT Partnership members enrolled in the State's Medicare Advantage Plan has grown significantly
  - Since the initial projections in 2022, the number of covered lives has increased from 55,874 to 63,745; an increase of 14%
- Beginning January 1, 2025, the federal Inflation Reduction Act of 2022 limits patient costs in Medicare Advantage plans
  - This will cause employer premiums to increase dramatically

Summary

Fiscal Outlook from Across the Region

Massachusetts budget secretary bracing for 'unavoidable deficiencies'

Gov. Mills vows lean budget in light of projected revenue shortfall

Cutting programs, raising taxes among opposing proposals floated to address gap

Tough choices ahead for R.I. lawmakers staring down $400M FY26 budget deficit

R.I.'s budget picture much bleaker than expected in budget memo

Fiscal experts: New York state must prepare for 'difficult' 2026 budget

Facing budget gap, Gov. Murphy seeks reduced spending and a limit on new hiring

Some pay raises for state workers also on chopping block

Yawning deficit looms as Maryland leaders weigh future cuts, tax hikes

The state faces its worst projected funding shortfall of the past 20 years, with the gap between revenue and spending expected to widen even more than during the Great Recession.

The above headlines were all posted within the last 6 months.

Fiscal Outlook from Across the Nation

Indiana more than $300M off its budget plan through four months of fiscal year

Legislative panel OKs Florida budget outlook warning of potential future shortfalls

Missouri tax revenues declining in first months of fiscal year, raising concerns

A new report from Pew Charitable Trusts shows revenue growth in most states is below inflation after two years of abundant tax receipts

Nebraska faces $432 million shortfall heading into next budget cycle

SOUTH DAKOTA SEARCHLIGHT

GOVERNMENT ENVIRONMENT ECONOMY HEALTH JUSTICE EDUCATION DECISION 2024

ECONOMY GOVERNMENT

Fiscal analysts caution lawmakers as state sales tax revenue dips

With $10B deficit looming, WA governor calls on state agencies to make cuts

Washington's outgoing governor says reductions are needed to balance the next state budget. Lawmakers may also consider new taxes when they convene next year.

California's budget forecasted to be relatively balanced, but no room for extra spending

ILLINOIS | News

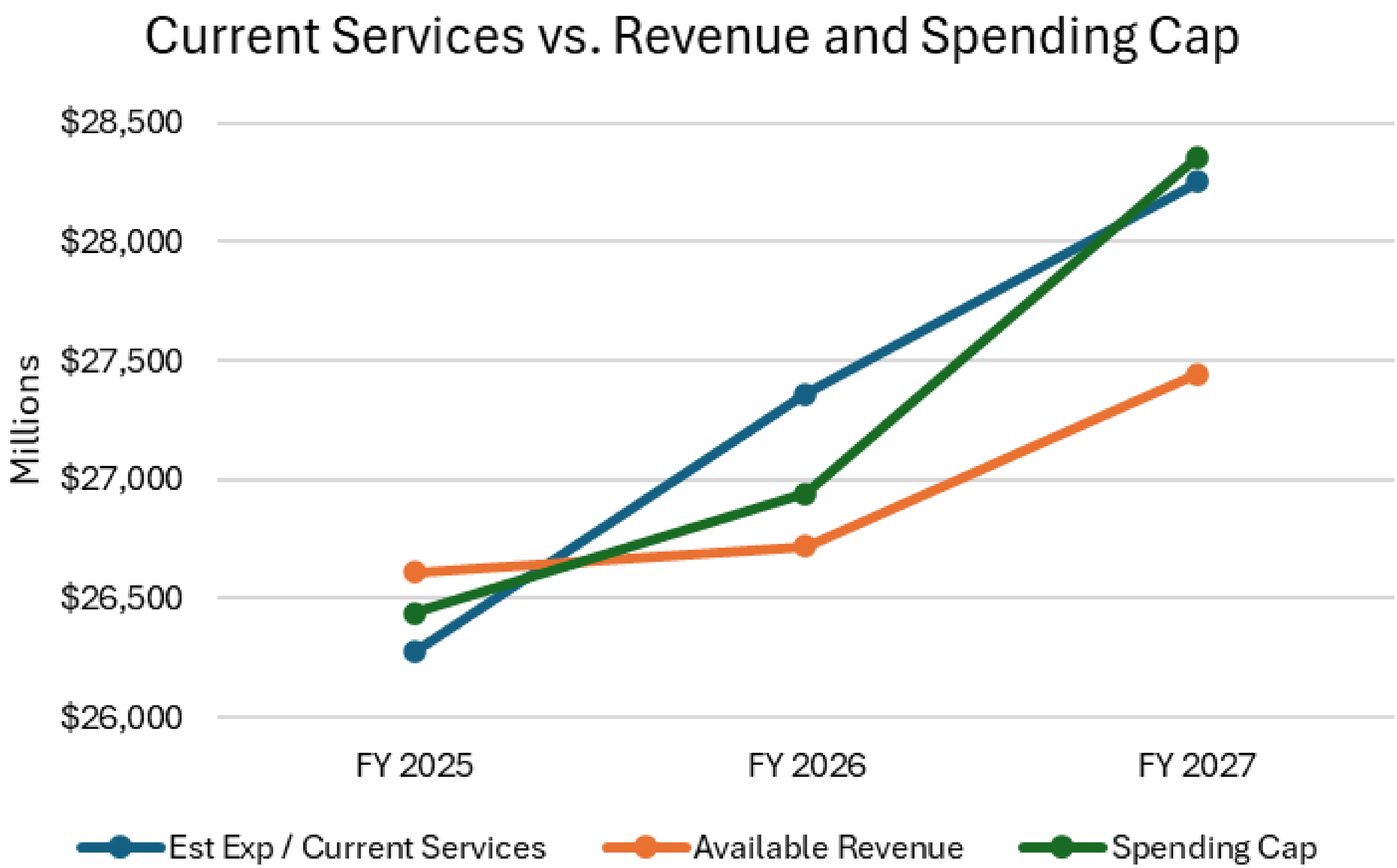
Lawmakers return to Springfield as projected budget deficit looms

Divided MN Legislature will have to pass budget with looming shortfalls this session

Lawmakers are required to get spending and taxes in order for the next two years by the end of June

The above headlines were all posted within the last 6 months.

FY 2026 – 2027 Biennial Budget Challenge



Summary

- The primary issue in FY 2025 is not revenues, it is expenditures and remaining compliant with the spending cap
  - Fortunately, due to the revenue cap, we are still projecting a surplus in CT, whereas many states are already experiencing budgetary difficulties
- General Fund revenues exceed fixed costs growth in the outyears
- Transportation Fund fixed costs exceed revenue growth due to debt service growth
- The state has made great strides in addressing its unfunded liabilities and this is reducing budgetary pressures in the long run
  - However, Connecticut's long-term liabilities are still among the highest in the country
- The Governor is committed to enacting a biennial budget that serves the State's residents, and we look forward to working with the Legislature during the upcoming session