Fiscal Accountability Report
FY 2023 – FY 2026

Secretary Jeffrey R. Beckham
Office of Policy and Management
December 5, 2022

Presentation Overview

- FY 2023 Projections of Operating Results
- Estimates of FY 2024 – FY 2026 Revenue and Fixed Cost Growth
- Long-Term Liabilities and “Fixed Cost” Drivers
- The Economy
- Conclusion and Key Takeaways

Summary of Major Points

- FY 2023
  - General Fund projected surplus of $1.0 billion
  - Special Transportation Fund projected surplus of $317 million
- FY 2024 – FY 2026
  - Fixed costs exceed revenues in FY 2024
  - However, revenue growth outpaces fixed cost growth in FY 2025 and FY 2026
    - This is the second consecutive report highlighting this trend
- Long-Term Liabilities
  - Reduction of $7.1 billion compared to last year's report
  - Progress on healthcare and pensions are the major drivers of improvement
- The fiscal reforms enacted during the 2017 session have played a major role in the improvement in the state's finances
  - The Administration's commitment to addressing long-term liabilities and living within our means is paying dividends
  - The Governor will propose securing these fiscal guardrails beyond FY 2023 via bond covenant

Projected FY 2023 Operating Results

FY 2023 – OPM November 18, 2022, Projections

FY 2023 - OPM Estimates vs. Budget Plan
(in millions)

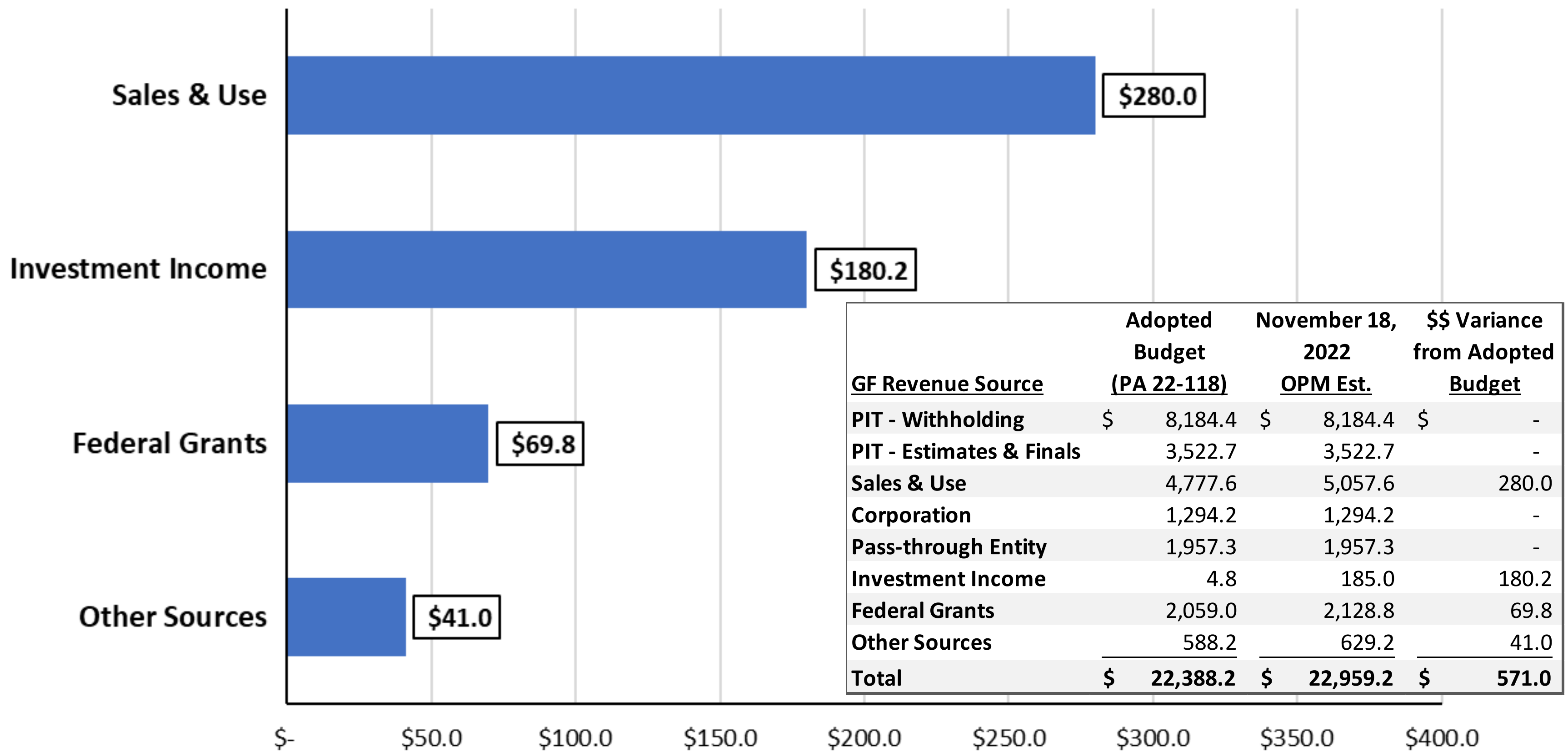
General Fund	Budget Plan	OPM Estimate 11/18/22	Variance from Budget
Revenues	$ 22,388.2	$ 22,959.2	$ 571.0
Expenditures	22,089.2	21,953.9	(135.3)
Operating Results - Surplus/(Deficit)	$ 299.0	$ 1,005.3	$ 706.3
Budget Reserve Fund			
Deposits		$ 2,852.8	
Withdrawals		(4,107.6) [1.]	
Proj. Net Deposit/(Withdrawal) 6/30		$ (1,254.8)	
Special Transportation Fund			
Revenues	$ 2,091.9	$ 2,132.6	$ 40.7
Expenditures	1,826.2	1,815.8	(10.4)
Operating Results - Surplus/(Deficit)	$ 265.7	$ 316.8	$ 51.1
Proj. Fund Balance 6/30		$ 714.6	

Notes:
1. BRF withdrawal includes the projected transfer out of $4,107.6 million in FY 2023 pursuant to Sec. 4-30a, CGS, as the FY 2022 ending balance exceeds the statutory 15% cap. This sum will be deposited as additional contributions to the State Employees Retirement Fund and the Teachers' Retirement Fund.

- The passage of PA 22-1 of the November special session (HB 6001) reduces the projected General Fund surplus by $45.0 million to $960.3 million, and the Special Transportation Fund surplus by $90.0 million to $226.8 million

FY 2023 General Fund Revenue Changes

Change in General Fund Revenue Forecast from FY 2023 Adopted Budget to November 18, 2022 Estimate
(in millions)



GF Revenue Source	Adopted Budget (PA 22-118)	November 18, 2022 OPM Est.	$$ Variance from Adopted Budget
PIT - Withholding	$ 8,184.4	$ 8,184.4	$ -
PIT - Estimates & Finals	3,522.7	3,522.7	-
Sales & Use	4,777.6	5,057.6	280.0
Corporation	1,294.2	1,294.2	-
Pass-through Entity	1,957.3	1,957.3	-
Investment Income	4.8	185.0	180.2
Federal Grants	2,059.0	2,128.8	69.8
Other Sources	588.2	629.2	41.0
Total	**$ 22,388.2**	**$ 22,959.2**	**$ 571.0**

Recent Revenue Trends

- The November consensus forecast adopted a conservative outlook:
  - Still early in the fiscal year
  - Waning impact of federal stimulus
  - Rising interest rates
  - Uncertainty regarding slowing of the economy
- Fiscal year-to-date revenue growth continues to outpace the growth rates assumed in the November 2022 consensus
- A continuation of these trends could result in more positive revisions to FY 2023 revenue

Assumed Revenue Growth Rates vs.
Actual Revenue Growth Rates, FYTD
By Major Source, FY 2023

Source	Adopted Budged Assumed Growth Rate	11/10/2022 Consensus Assumed Growth Rate	10/31/2022 FYTD Actual Growth Rate
1. Withholding	5.0%	4.5%	11.7%
2. Estimates & Finals	-10.0%	-17.0%	11.3%
3. Sales & Use	2.3%	7.6%	15.1%
4. Corporation Tax	2.0%	-1.9%	19.0%
5. Pass-through Entity	-10.0%	-15.2%	14.2%

FY 2023 General Fund Expenditure Projections

FY 2023 General Fund Expenditure Projections
Based on OPM 11/18/2022 Estimate
(in millions)

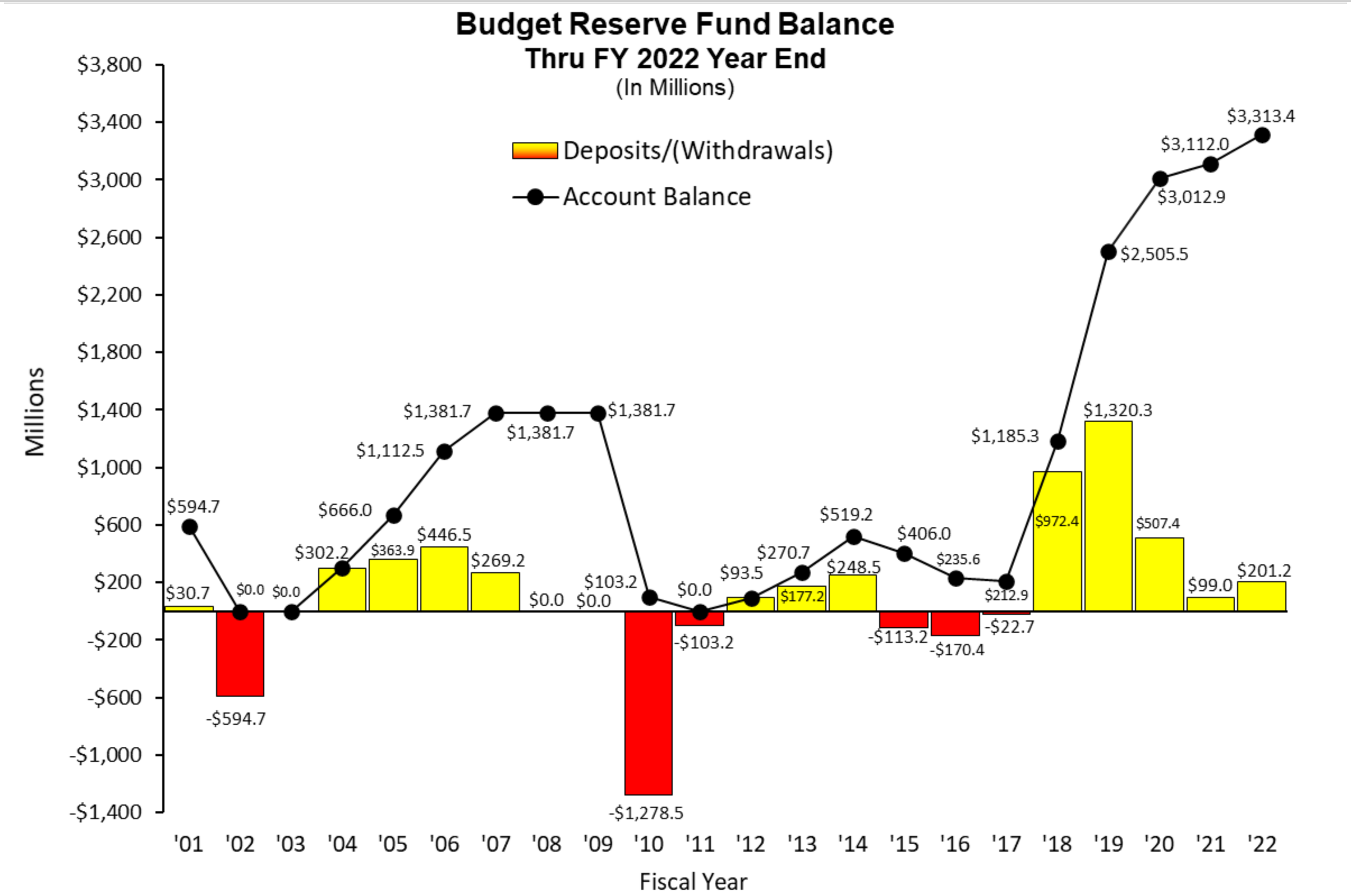
Deficiencies	
1. Dept. of Housing - Congregate Facilities Operation	$ 1.00
2. Dept. of Education - Adult Education	0.70
3. Dept. of Correction - PS and OE	9.00
4. Comptroller-Misc. - Adjudicated Claims	23.00
Total Projected Deficiencies	**$ 33.70**

Lapses (beyond budgeted amounts)	
5. Office of Legislative Management - PS	$ 4.00
6. Auditors of Public Accounts - PS	0.25
7. Secretary of the State - PS	0.15
8. Dept. of Revenue Services - PS	4.00
9. Office of Governmental Accountability - PS	0.15
10. Dept. of Veterans Affairs - PS	0.79
11. Division of Criminal Justice - PS	3.50
12. Agricultural Experiment Station - PS	0.25
13. Dept. of Public Health - PS	3.10
14. Office of Health Strategy - PS	0.60
15. Dept. of Developmental Services - PS and OE	8.60
16. Dept. of Social Services - var., incl. extension of public health emergency and lower utilization	111.40
17. Teachers' Retirement Board - retiree health costs	0.50
18. Dept. of Children and Families - PS, caseloads, lower utilization	5.80
19. Judicial Dept. - PS	1.50
20. Public Defender Svcs Comm - vacancies, cost trends	0.83
21. Comptroller - Fringe Benefits	146.00
Total Projected Lapses	**$ 291.42**

Note: "PS" = Personal Services, "OE" = Other Expenses

Note: Does not include impact of appropriation changes resulting from PA 22-1 of the November special session (HB 6001)

Budget Reserve Fund



- The Rainy Day Fund is at the 15% statutory limit for FY 2023 and is projected to remain there through FY 2026
- Any amounts beyond the 15% limit will continue to be used to pay down long-term liabilities

Summary of OPM Projections of Fixed Cost Growth vs. Revenue Growth For FY 2024 – FY 2026

Year-Over-Year Growth of Fixed Costs vs. Revenue General Fund

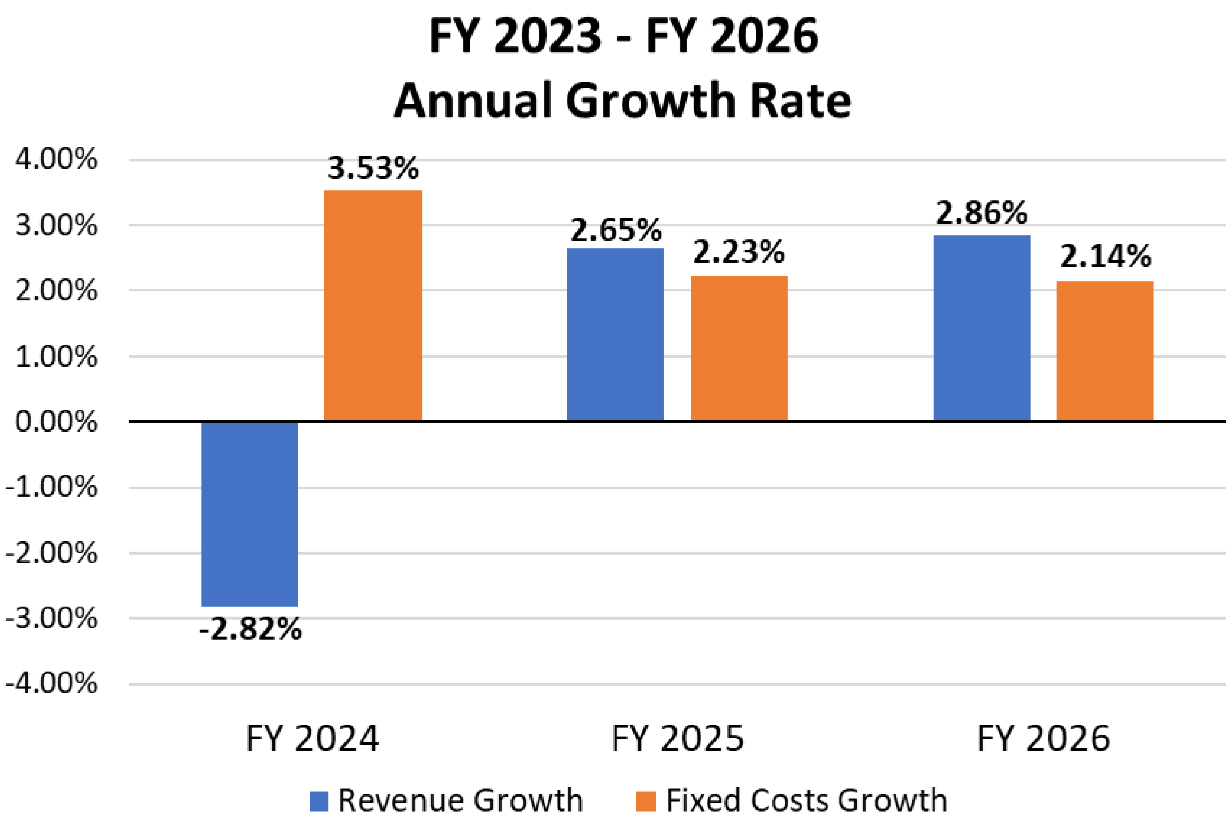
GENERAL FUND
(in millions)

	FY 2024 vs. FY 2023	FY 2025 vs. FY 2024	FY 2026 vs. FY 2025
Revenue Growth	$ (646.6)	$ 590.6	$ 654.2
Fixed Cost Growth			
Debt Service	$ 54.8	$ 149.3	$ 31.4
State Employee Pensions	11.4	(53.5)	(13.2)
Teacher Pensions	(23.5)	4.4	88.6
State and Teacher OPEB	(18.3)	66.9	25.7
Medicaid	391.6	82.5	111.5
Other Entitlements	(6.8)	17.2	18.4
Total Fixed Cost Growth	$ 409.3	$ 266.9	$ 262.4
Difference	$ (1,055.9)	$ 323.7	$ 391.8

- Fixed costs are growing faster than revenue in FY 2024, largely due to one-time factors, but revenue growth is expected to outpace fixed cost growth in FY 2025 and FY 2026
- Growth in pension costs is not anticipated to be a significant driver of future General Fund spending
    - This is mainly due to changes in funding methodologies adopted since 2017 (FY 2023 was the last year of the phase-in to level-dollar amortization for SERS, and the TRS phase-in will be complete in FY 2026) as well as additional contributions made possible as a result of recent budget surpluses and volatility cap deposits

SERS = State Employees Retirement System
TRS = Teachers' Retirement System

General Fund Fixed Costs vs. Revenue Growth



- Revenue decline in FY 2024 is due to loss of significant non-recurring federal aid utilized to balance the budget for the current biennium
- Revenue growth slightly outpaces Fixed Cost growth in FY 2025 and FY 2026

Year-Over-Year Growth of Fixed Costs vs. Revenue
Special Transportation Fund

SPECIAL TRANSPORTATION FUND

(in millions)

	FY 2024 vs. FY 2023	FY 2025 vs. FY 2024	FY 2026 vs. FY 2025
Revenue Growth	$ 209.6	$ (29.3)	$ (13.9)
Fixed Cost Growth			
Debt Service	$ 76.2	$ 63.6	$ 60.1
State Employee Pensions and OPEB	(1.9)	(6.3)	(2.0)
Total Fixed Cost Growth	$ 74.3	$ 57.3	$ 58.2
Difference	$ 135.3	$ (86.6)	$ (72.1)

- “Fixed” cost growth from FY 2024 through FY 2026 is driven by growth in debt service costs, while state employee health and pension costs are anticipated to experience modest declines
- Unlike the General Fund, Special Transportation Fund revenue growth will not keep up with increasing debt service costs
- Without additional revenue or adjustments in transportation investments, the expected increase in costs will outpace the growth in revenues in the long term, impacting fund solvency

General Fund Revenues

General Fund Consensus Projections

General Fund Revenues

FY 2022 Thru FY 2026

(In Millions of Dollars)

	REVENUE					% CHANGE				
	Actual	Projection				Actual	Projection			
TAXES	Fiscal 2022	Fiscal 2023	Fiscal 2024	Fiscal 2025	Fiscal 2026	Fiscal 2022	Fiscal 2023	Fiscal 2024	Fiscal 2025	Fiscal 2026
1. PIT - Withholding	$ 7,886.2	$ 8,184.4	$ 8,420.3	$ 8,766.9	$ 9,110.1	8.9%	3.8%	2.9%	4.1%	3.9%
2. PIT - Estimates & Finals	4,245.6	3,522.7	3,170.4	3,297.2	3,429.1	37.1%	-17.0%	-10.0%	4.0%	4.0%
3. Sales & Use	4,818.1	5,057.6	5,185.6	5,309.4	5,430.2	0.5%	5.0%	2.5%	2.4%	2.3%
4. Corporations	1,401.2	1,294.2	1,306.0	1,346.7	1,389.0	21.5%	-7.6%	0.9%	3.1%	3.1%
5. Pass-Through Entity	2,307.6	1,957.3	1,761.6	1,832.1	1,905.3	48.9%	-15.2%	-10.0%	4.0%	4.0%
6. Real Estate Conveyance	384.5	290.4	287.7	292.6	297.0	-0.1%	-24.5%	-0.9%	1.7%	1.5%
7. Health Provider	955.1	973.8	974.7	978.4	952.2	-8.0%	2.0%	0.1%	0.4%	-2.7%
8. Federal Grants	1,934.9	2,128.8	1,744.2	1,765.9	1,789.1	29.3%	10.0%	-18.1%	1.2%	1.3%
9. Total Refunds	(1,817.0)	(1,978.5)	(2,044.0)	(2,140.7)	(2,201.1)	-2.6%	8.9%	3.3%	4.7%	2.8%
10. Other Taxes	1,300.2	1,180.1	1,146.0	1,144.4	1,141.8	3.4%	-9.2%	-2.9%	-0.1%	-0.2%
11. Other Revenues	(1,425.3)	348.4	360.1	310.3	314.7	-471.5%	-124.4%	3.4%	-13.8%	1.4%
12. Total GF Revenues	**$ 21,990.9**	**$ 22,959.2**	**$ 22,312.6**	**$ 22,903.2**	**$ 23,557.4**	**7.1%**	**4.4%**	**-2.8%**	**2.6%**	**2.9%**

Notes:

(1) Updated to final November 10, 2022 consensus revenue estimates.

PIT = Personal Income Tax

FY 2024 Revenue Gap Due to Policy Changes

Enacted Policy Changes Impacting FY 2024 General Fund Revenue
(in millions)

1.	**Total All Revenue, FY 2023**	**Estimated FY 2023 Revenues, as of 11/10/2022**	**$ 22,959.2**
2.	Personal Income Tax	Expand Angel Investor Tax Credit to Cannabis Businesses	(15.0)
3.	Personal Income Tax	Extend Existing Tax Exemption for Pensions/Annuities to IRAs	(32.5)
4.	Sales and Use Tax	Loss of MRSA Transfer	See Note (1)
5.	Sales and Use Tax	Exemption for Beer Manufacturer/Retailer	(1.3)
6.	Sales and Use Tax	Exemption for Wine Manufacturer/Retailer	(0.5)
7.	Corporate Income Tax	Expiration of 10% Surcharge	(50.0)
8.	Corporate Income Tax	Phase-out Capital Base Tax	(5.7)
9.	Corporate Income Tax	Phase-In R&D Tax Credit from 50.01% to 60% to 70% by IY 2023	(4.3)
10.	Insurance Companies	Captive Insurer Initiative	(7.3)
11.	Alcoholic Beverages Tax	Adjust Alcohol Excise Tax Rate for Beer Only	(2.0)
12.	Admissions & Dues	Repeal Movie Theaters Admissions Tax	(2.5)
13.	Gift and Estate	Phase-in Federal Exemption level from $9.1M to the Federal Level	(10.0)
14.	Refunds of Taxes	Reimburse Beer Mfrs. For SUT Paid on Machinery & Equip.	(0.3)
15.	Refunds of Taxes	Reimburse Wine Mfrs. For SUT Paid on Machinery & Equip.	(2.0)
16.	Transfers Special Revenue	Debt Free College	(2.0)
17.	Transfers Special Revenue	Transfer 100% of Sports Betting Revenue from XL Center to CRDA	(0.6)
18.	Federal Grants	Loss of HCBS Revenue	(83.2)
19.	Federal Grants	Loss of Enhanced FMAP	(90.0)
20.	Transfers To/(From) Other Funds	Resume funding GAAP deficit in FY 2024	(120.8)
21.	Transfers To/(From) Other Funds	Loss of ARPA 2021 - Federal Stimulus	(314.9)
22.	Sub-total, Enacted Policy Changes Impacting FY 2024 (Sum of Lines 2 - 21)		$ (744.9)
23.	Enacted Policy Changes as a Percentage of FY 2023 Revenue (Line 22 / Line 1)		-3.2%

Notes:

(1) Revenues in FY 2024 will be reduced by $276.3 million due to the loss of the transfer from MRSA to the General Fund. However, a corresponding shift of expenditures from the General Fund to MRSA will also occur.

Long-Term Obligations, “Fixed” Cost Drivers and Other Topics

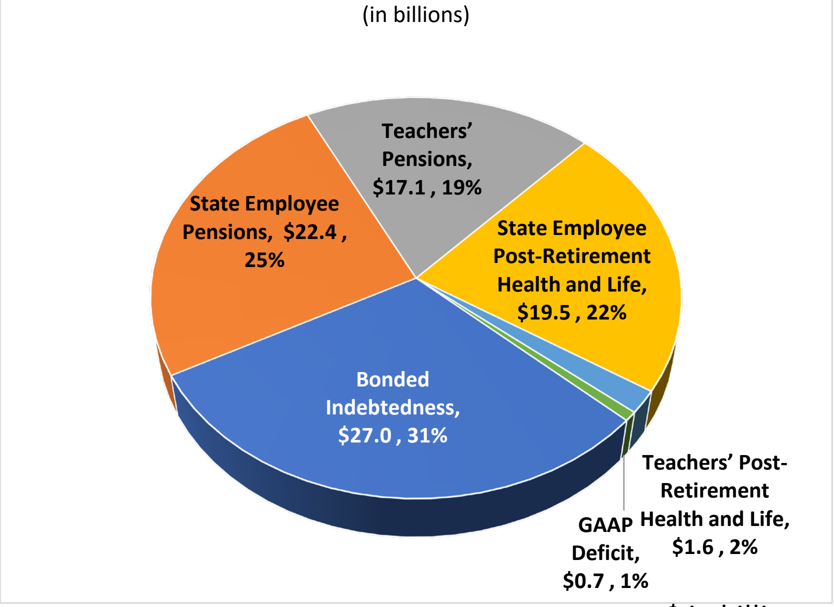
Efforts to Reduce Long-Term Liabilities

- Long-term liabilities have seen a substantial reduction since last year's report – down by $7.1 billion
  - Additional deposits to pension plans (SERS and TRS) have boosted funding levels by increasing fund assets that generate market returns and reduce required state contributions going forward
    - TRS unfunded liability has been reduced by $1 billion in the 6/30/22 valuation compared to 6/30/20
    - SERS valuation expected in December that will reflect more than $3.2 billion in additional deposits this year
  - Healthcare costs have been reduced thanks to competitive bidding of the Medicare Advantage plan by the State Comptroller
    - As a result, our OPEB liability has decreased $4 billion from the last valuation
  - Entitlement growth (e.g., Medicaid) has been modest compared to other states

SERS = State Employees Retirement System; TRS = Teachers' Retirement System;
OPEB = Other Post-Employment Benefits

Long-Term Liabilities

- The state's current long-term obligations total $88.3 billion, down $7.1 billion from the level reported last year

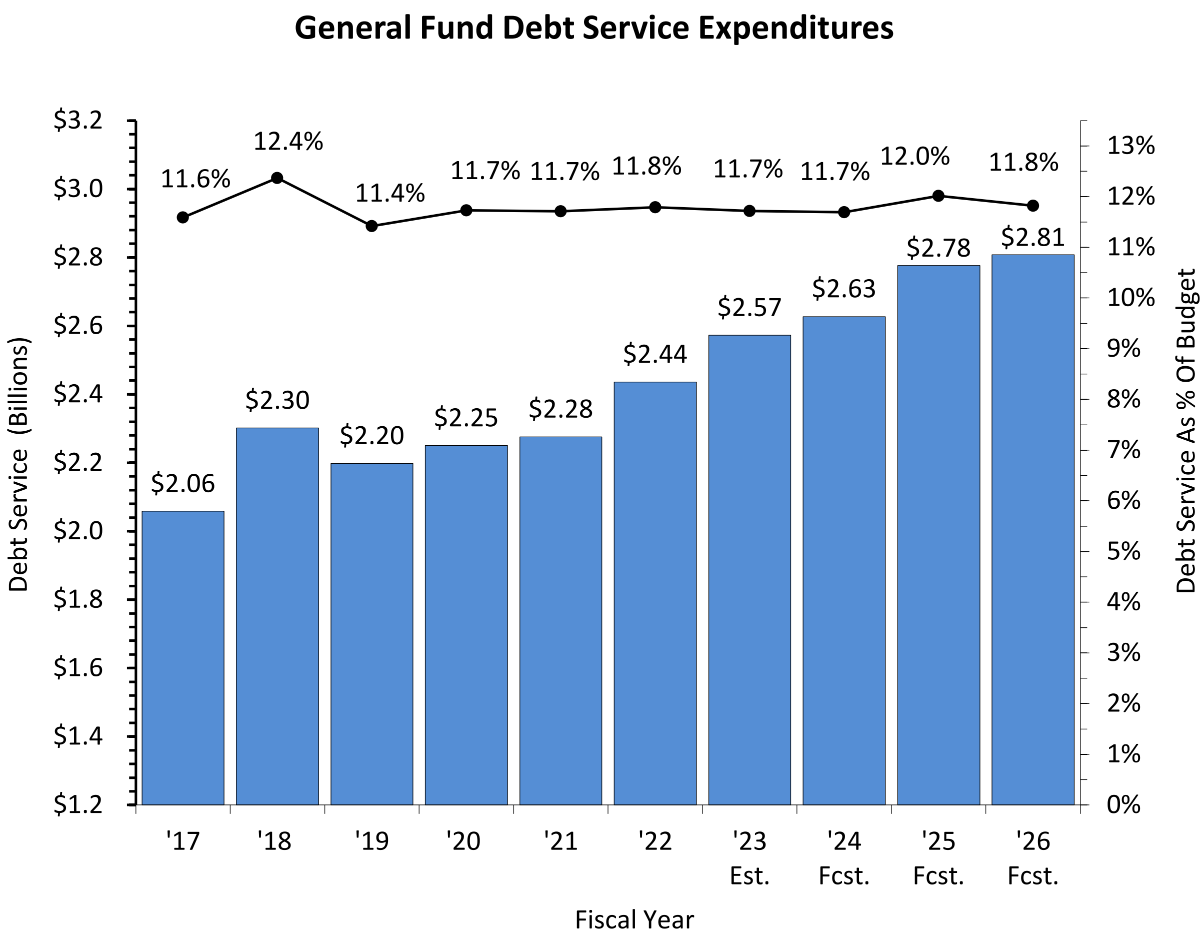


$ in billions

Long-Term Liability	**2022 FAR**	**2023 FAR**	**Change**
Bonded Indebtedness	$ 27.2	$ 27.0	$ (0.2)
State Employee Pensions	22.7	22.4	(0.3)
Teachers' Pensions	18.1	17.1	(1.0)
State Employee Post-Retirement Health and Life	23.5	19.5	(4.0)
Teachers' Post-Retirement Health and Life	2.8	1.6	(1.2)
GAAP Deficit	1.1	0.7	(0.4)
Total	**$ 95.4**	**$ 88.3**	**$ (7.1)**

GAAP = Generally Accepted Accounting Principles

General Fund Debt Service



- The single largest growth driver has been payments for the TRS pension obligation bonds. Scheduled debt service payments will grow from $118.4 million in FY 2021 to $330.2 million by FY 2025, a 178.9% increase
- Despite this, debt service has remained relatively flat as a proportion of the budget
- Continued prudence on debt issuances will help to keep debt service at manageable levels over the next several years

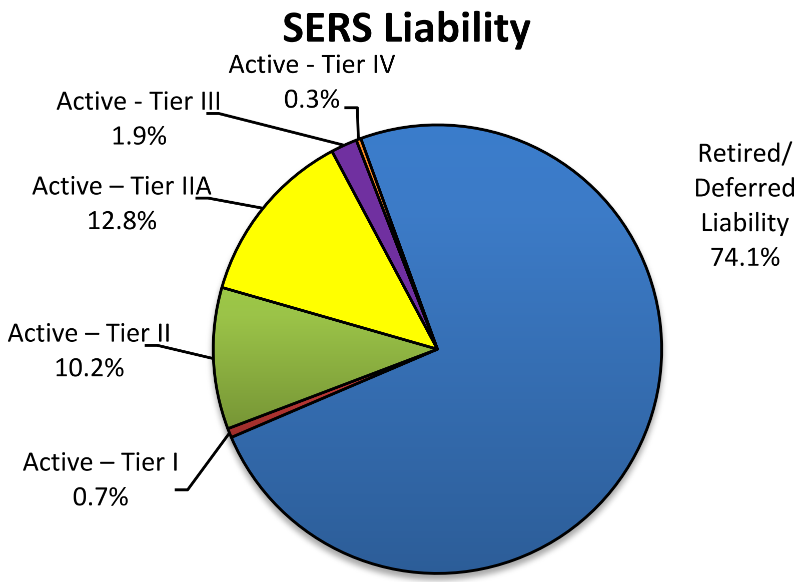
TRS = Teachers' Retirement System

Retirement System Liabilities

State Employees Retirement System

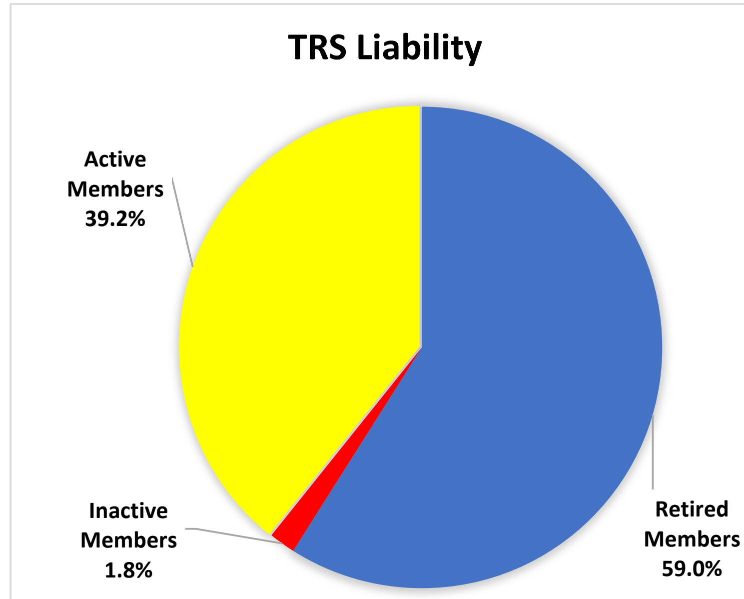
(per 6/30/21 valuation)

- $38.3 billion total liability
- $22.4 billion unfunded liability
- 74.1% of the liability is related to inactive or already-retired employees
- 89.2% of the FY 2023 actuarially determined employer contribution is for the unfunded actuarial accrued liability



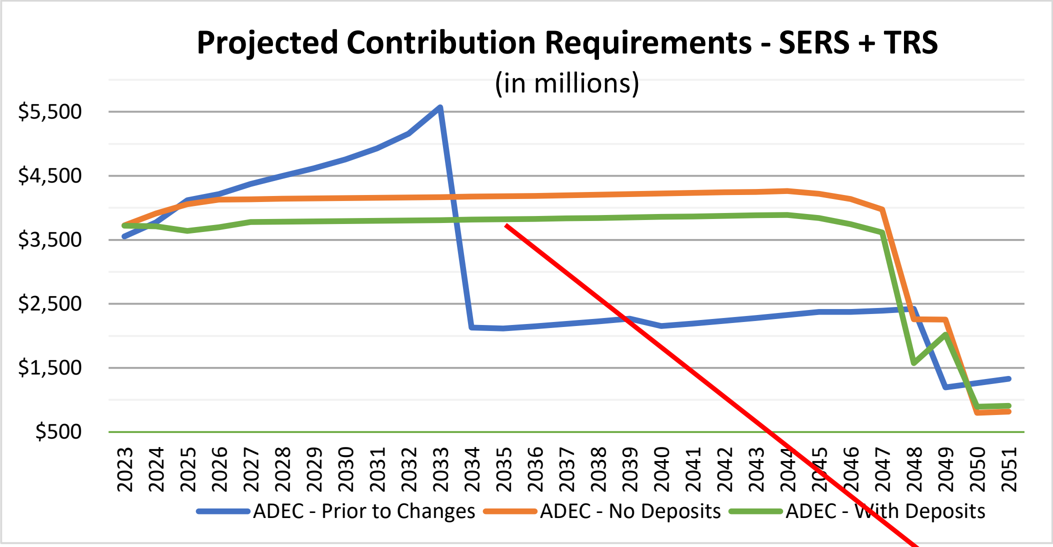
Teachers' Retirement System

(per 6/30/22 valuation)



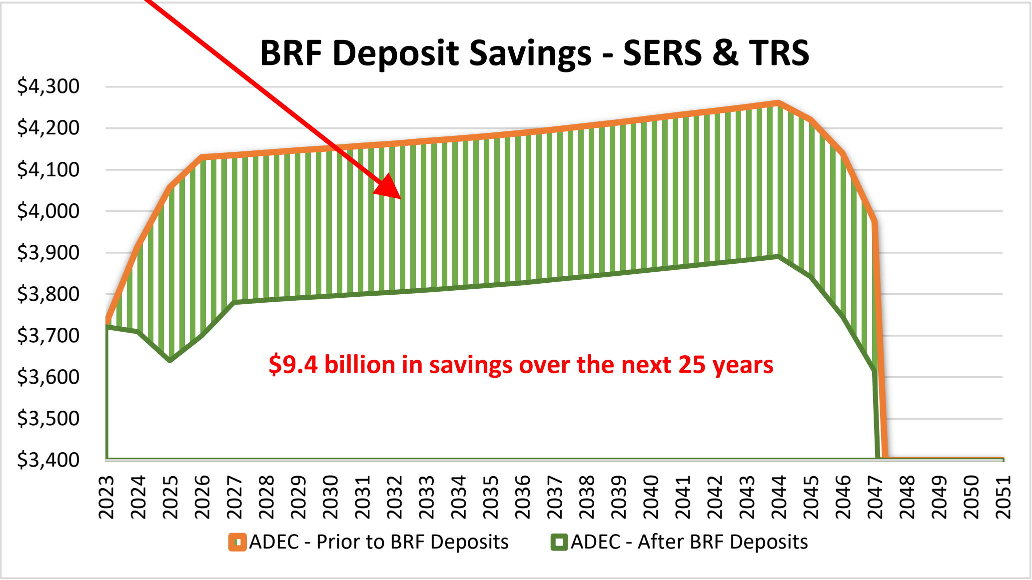
- $39.9 billion total liability
- $17.1 billion unfunded liability
- 60.8% of the liability is related to inactive or already-retired employees
- 82.4% of the FY 2024 actuarially determined employer contribution is for the unfunded actuarial accrued liability

Outlook for SERS and TRS



- Structural changes, combined with significant additional deposits, make the state's projected contributions much more stable and predictable

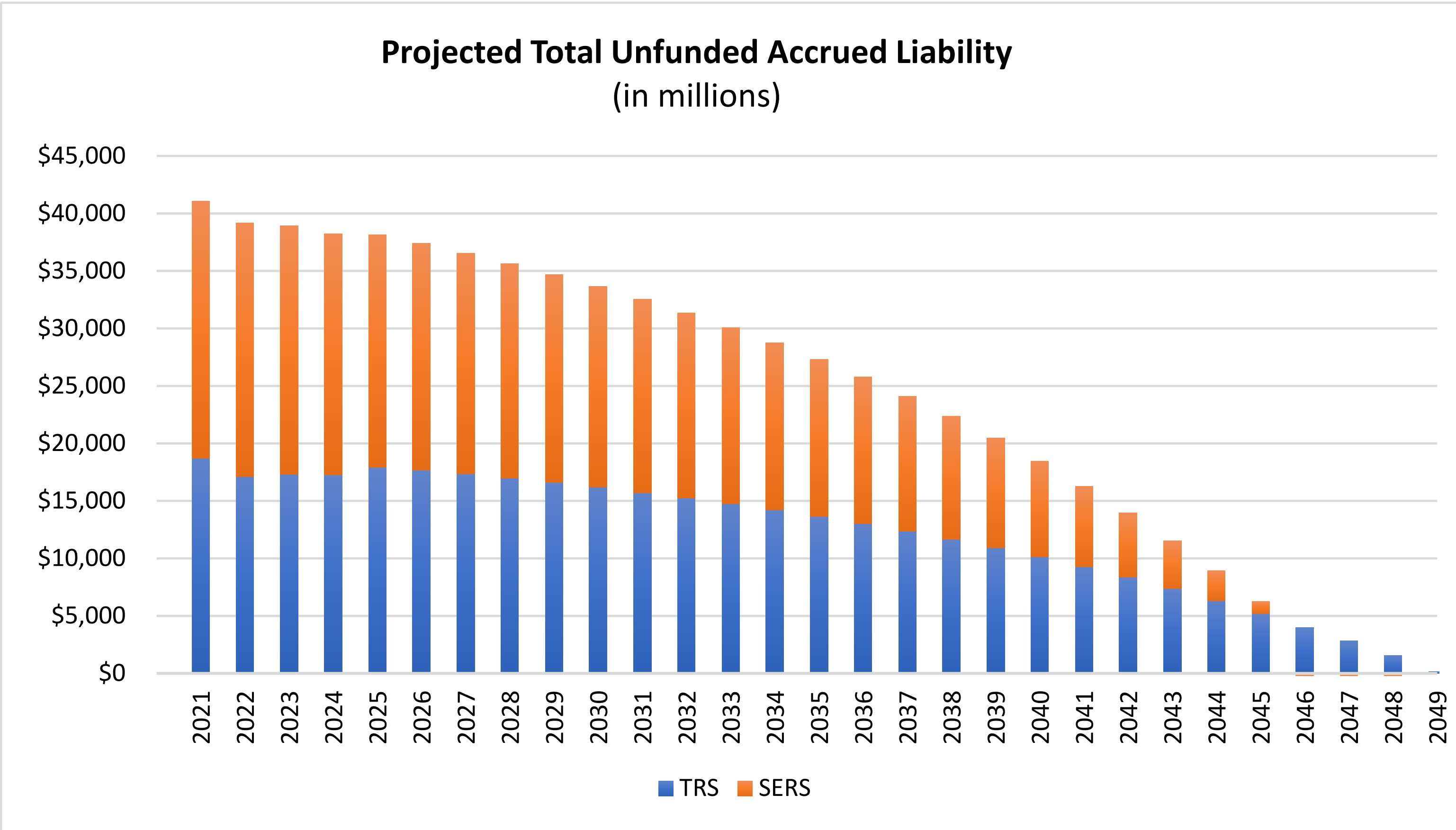
- Substantial recent additional deposits, beyond the required contributions, have further eased budgetary requirements for the next 25 years



SERS = State Employees Retirement System; TRS = Teachers' Retirement System;
BRF = Budget Reserve Fund; ADEC = Actuarially Determined Employer Contribution

Outlook for SERS and TRS

- **Funding discipline will eliminate the existing unfunded liability in SERS by the end of FY 2047 and TRS by the end of FY 2049**



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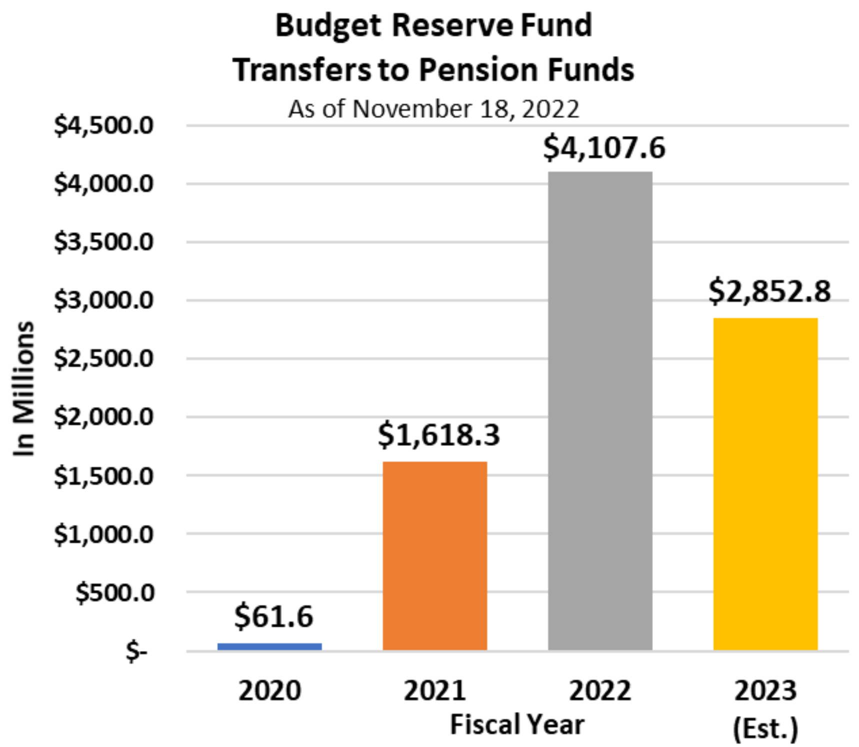
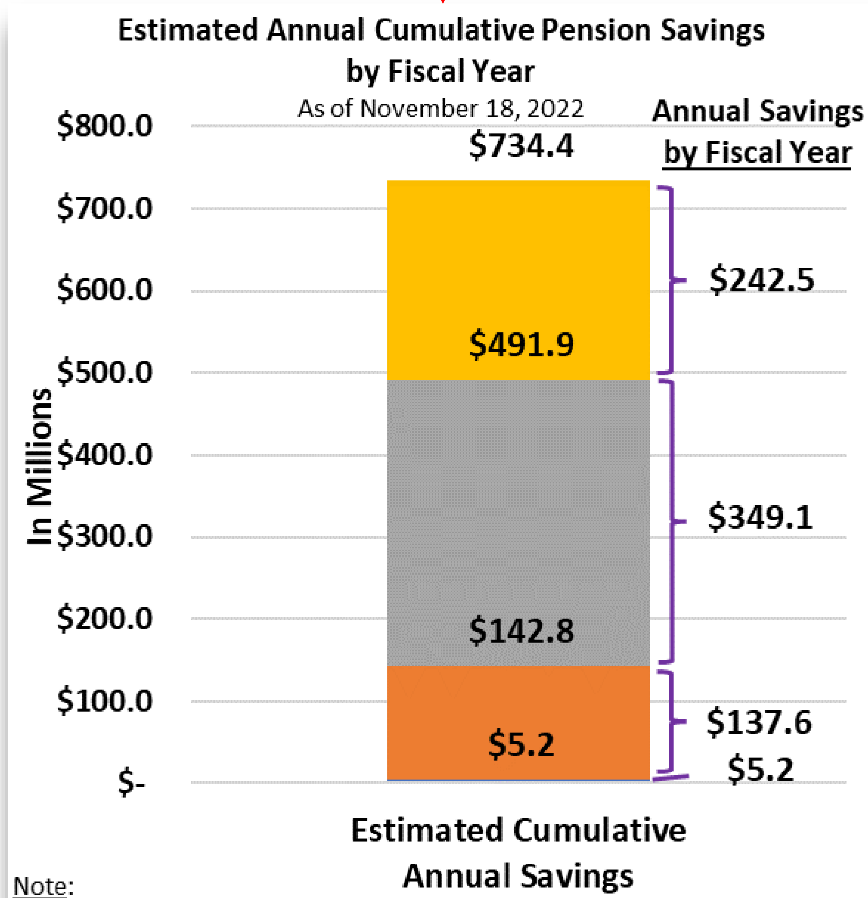
Additional Pension Contributions (Above ADEC)



Note: Transfer amounts are due to the Budget Reserve Fund reaching the 15% statutory limit and are in addition to ADEC payments. FY 2023 projection assumes no growth in FY 2024 appropriations over FY 2023 levels.

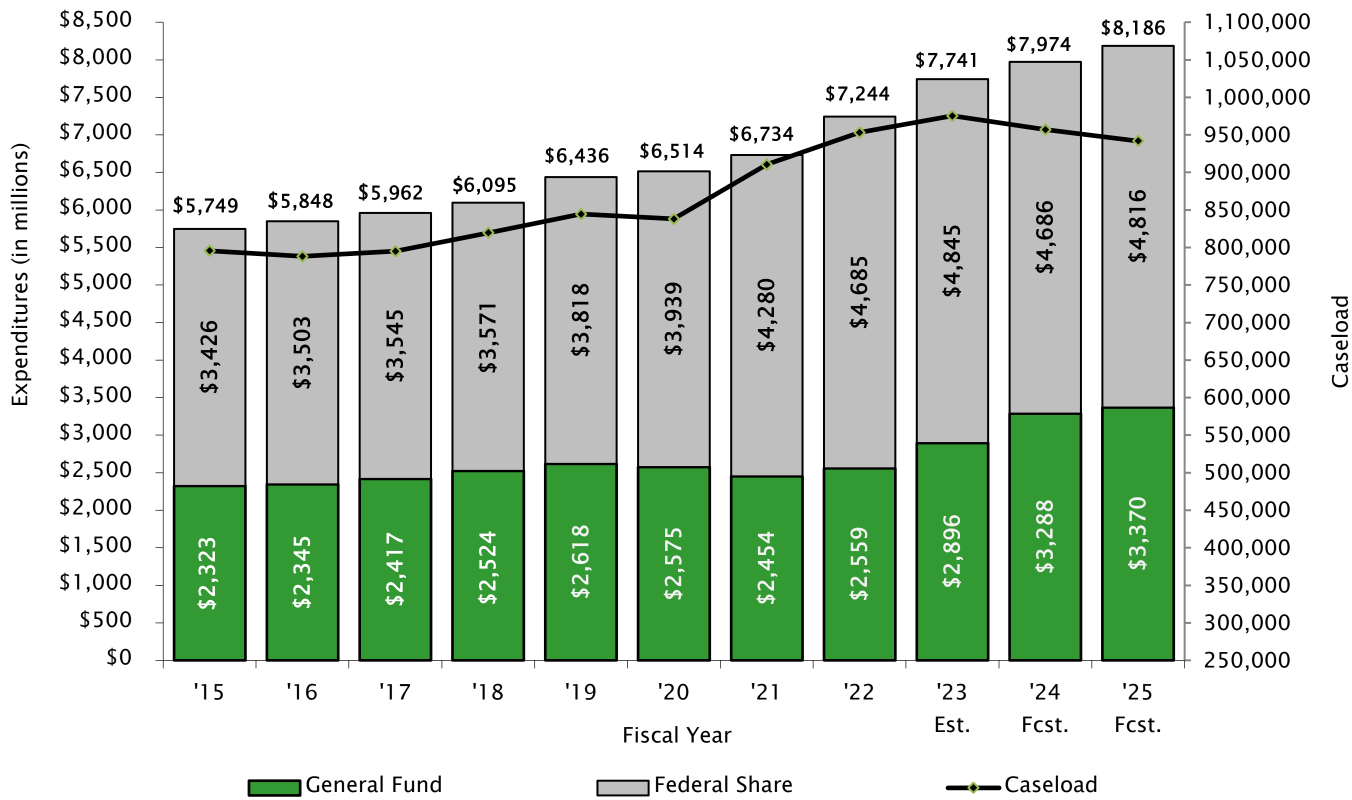


Note:
Assumes $8.5M of annual savings for every $100M contributed above ADEC.

- Nearly $5.8 billion has been deposited in SERS and TRS over the past 3 years, reducing the state's required contributions by $491.9 million annually for 25 years
- Another $2.8 billion could be deposited to the pension funds at the close of FY 2023, reducing required pension contributions by another $242.5 million, for a total of $734.4 million per year for 25 years

SERS = State Employees Retirement System; TRS = Teachers' Retirement System;
ADEC = Actuarially Determined Employer Contribution

Medicaid – Expenditures and Caseload



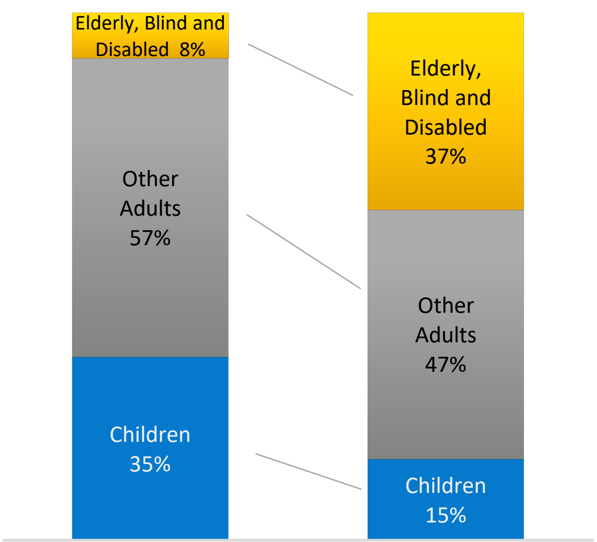
- Expenditures above have been adjusted to include funds transferred to DSS from DMHAS for behavioral health services which qualify for Medicaid reimbursement. Expenditures exclude hospital supplemental payments given the significant variance in that area over the years.
- Caseload figures exclude the limited benefit COVID-19 testing group.

- Medicaid is a $7-8 billion program serving nearly 1 million CT residents

- FY 2020 - FY 2023 General Fund requirements are reduced due to an increased federal share of 6.2% related to the public health emergency; this enhanced reimbursement does not apply to the Medicaid expansion population, which is reimbursed at 90%

Medicaid – Enrollment and Cost Trends

Medicaid - FY 2022



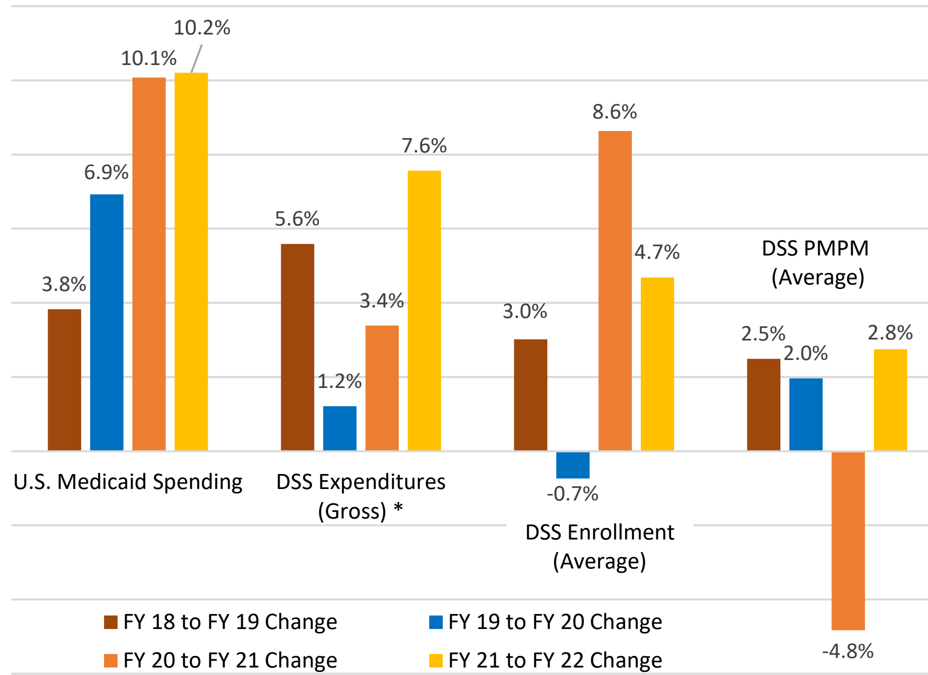
Enrollment
Average Monthly Enrollment = 953,173 *

Expenditures
Total Annual Expenditures = $7,244 million

Average Per Member Per Month = $633

** Excludes the limited benefit COVID-19 testing group*

Medicaid Growth Trends

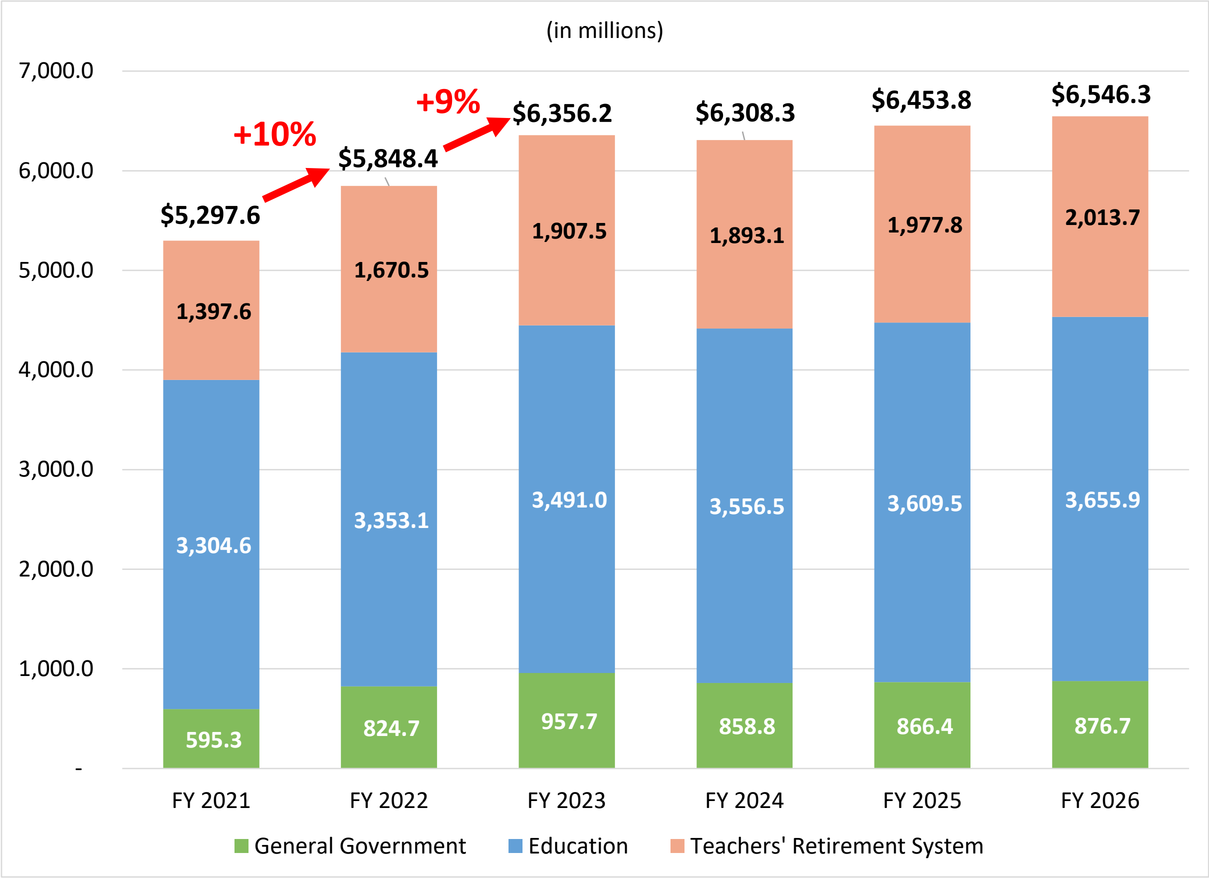


** Expenditures are net of drug rebates and exclude hospital supplemental payments given the significant variance in that area over the years. Enrollment and PMPM figures exclude the limited benefit COVID-19 testing group.*

- Despite caseload growth, cost growth in the Medicaid program remains relatively modest
- Overall spending growth in Connecticut is below the national average

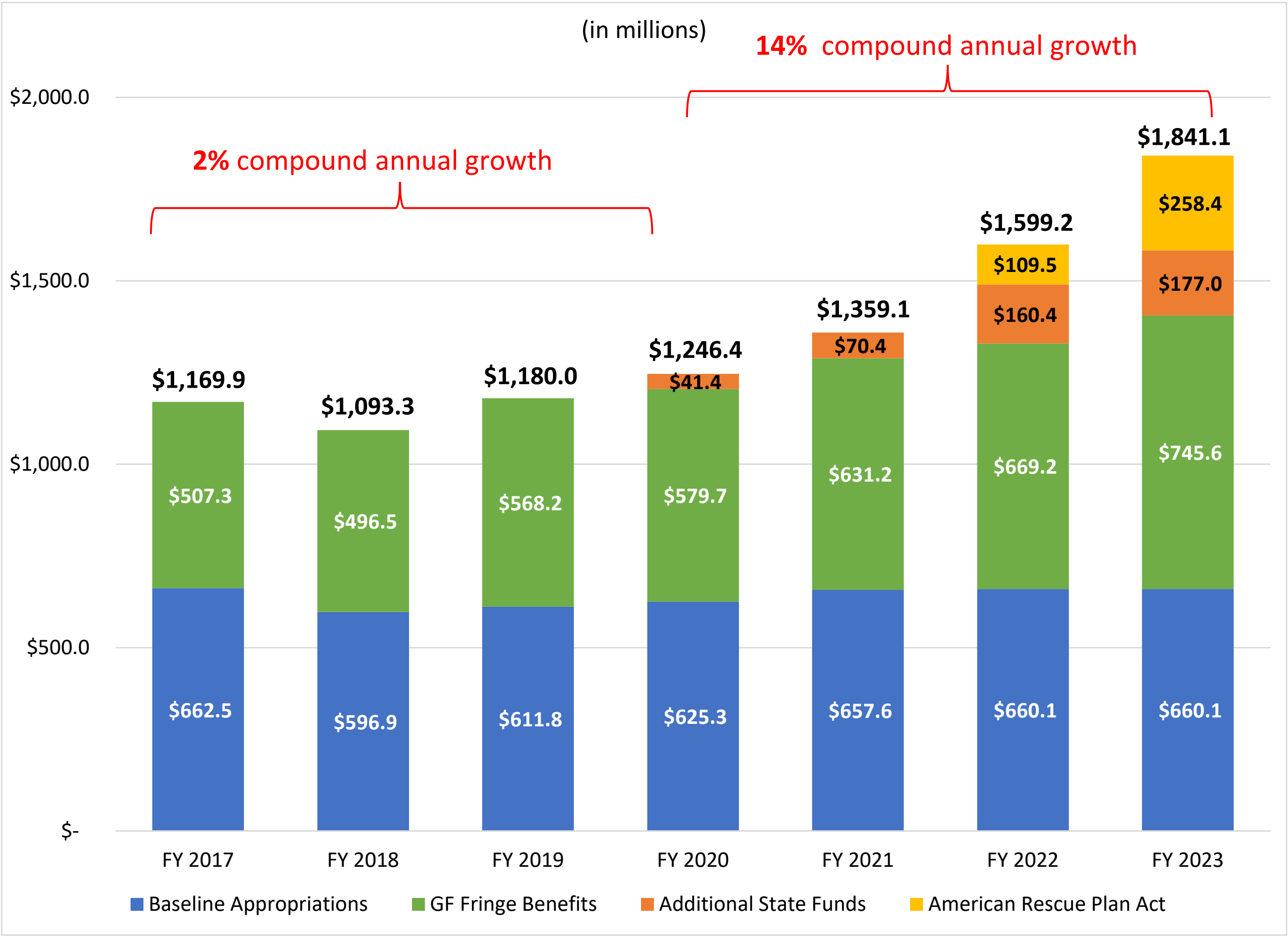
DSS = Dept. of Social Services; PMPM = Per Member Per Month

State Aid to Municipalities



- Estimates for FY 2024 – FY 2026 are according to formulas and appropriations in current law and do not assume future legislative action. Includes bonded aid
- 10% increase from FY 2021 to FY 2022 due largely to expansion of the PILOT and MRSA programs, and debt service schedule on pension obligation bonds for the Teachers' Retirement System
- 9% increase from FY 2022 to FY 2023 due to increased reimbursements for motor vehicle tax cap and increased debt service on pension obligation bonds

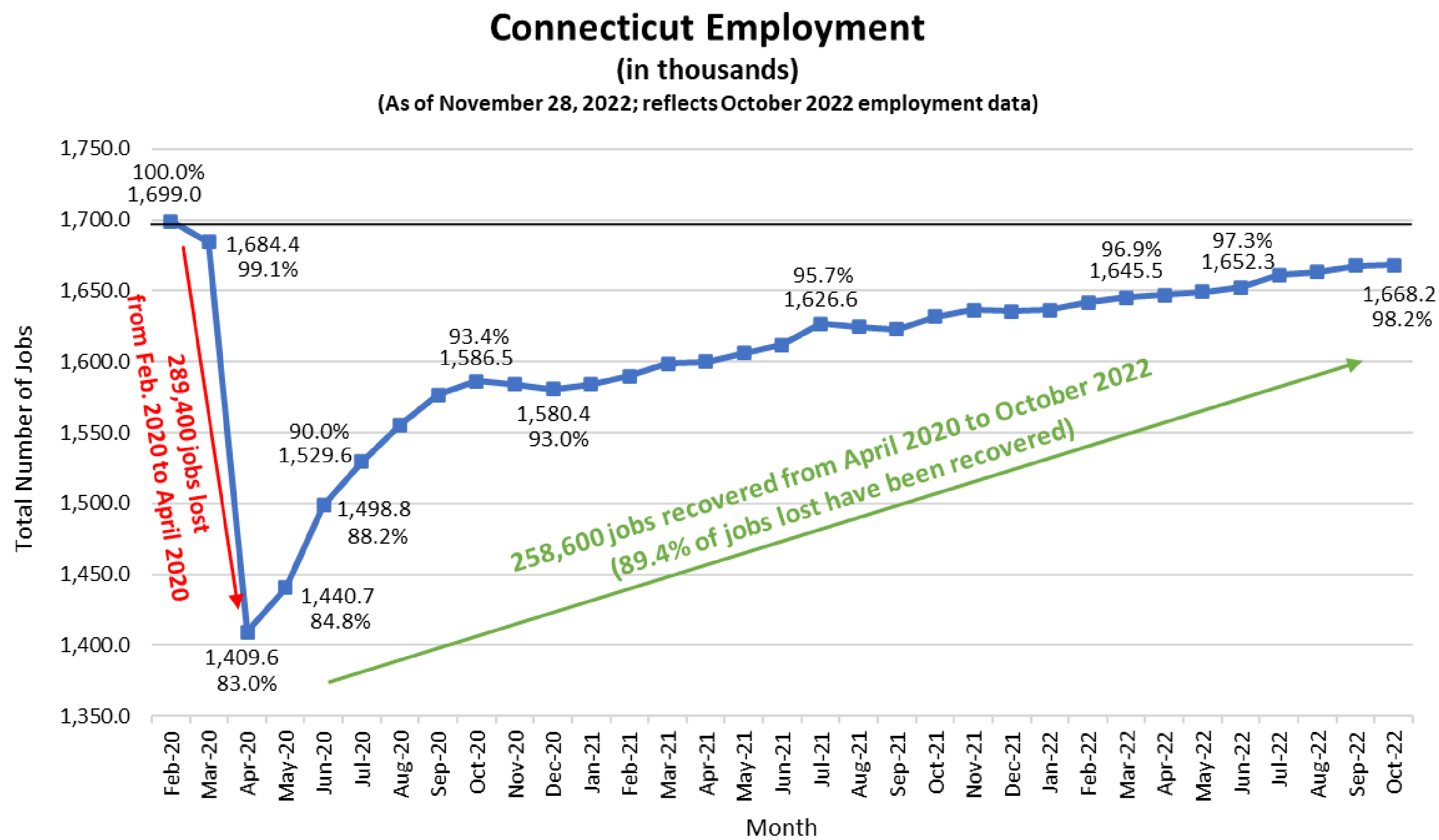
State Support for Higher Education



- The compound annual growth rate of state support for the constituent units of higher education was 14% from FY 2020 to FY 2023
- Most of this increase was funded via one-time sources such as the federal Coronavirus State Fiscal Recovery Fund and carryforwards of prior year General Fund lapsing funds

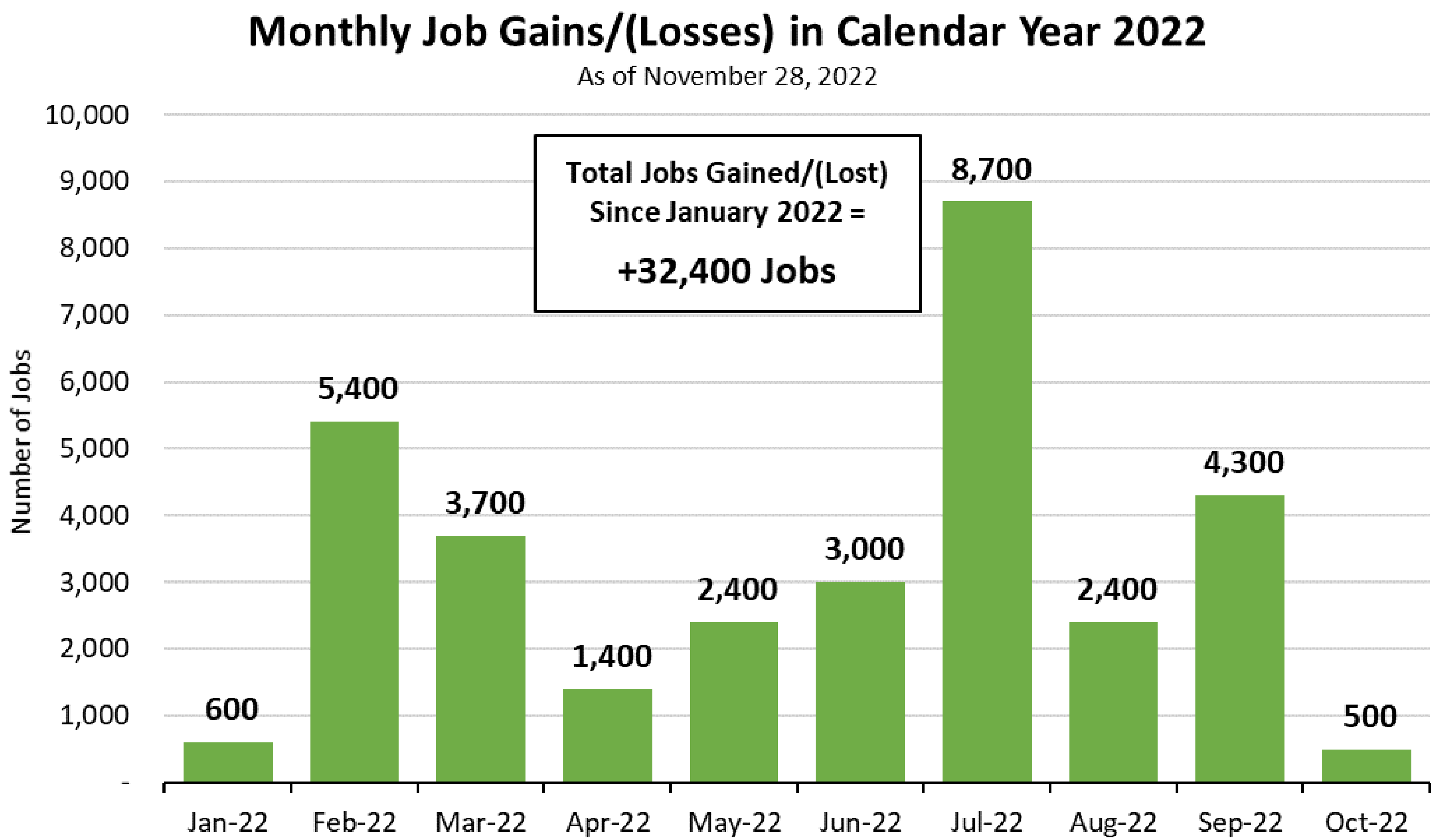
Economy

Pandemic Impact & Recovery on CT Employment



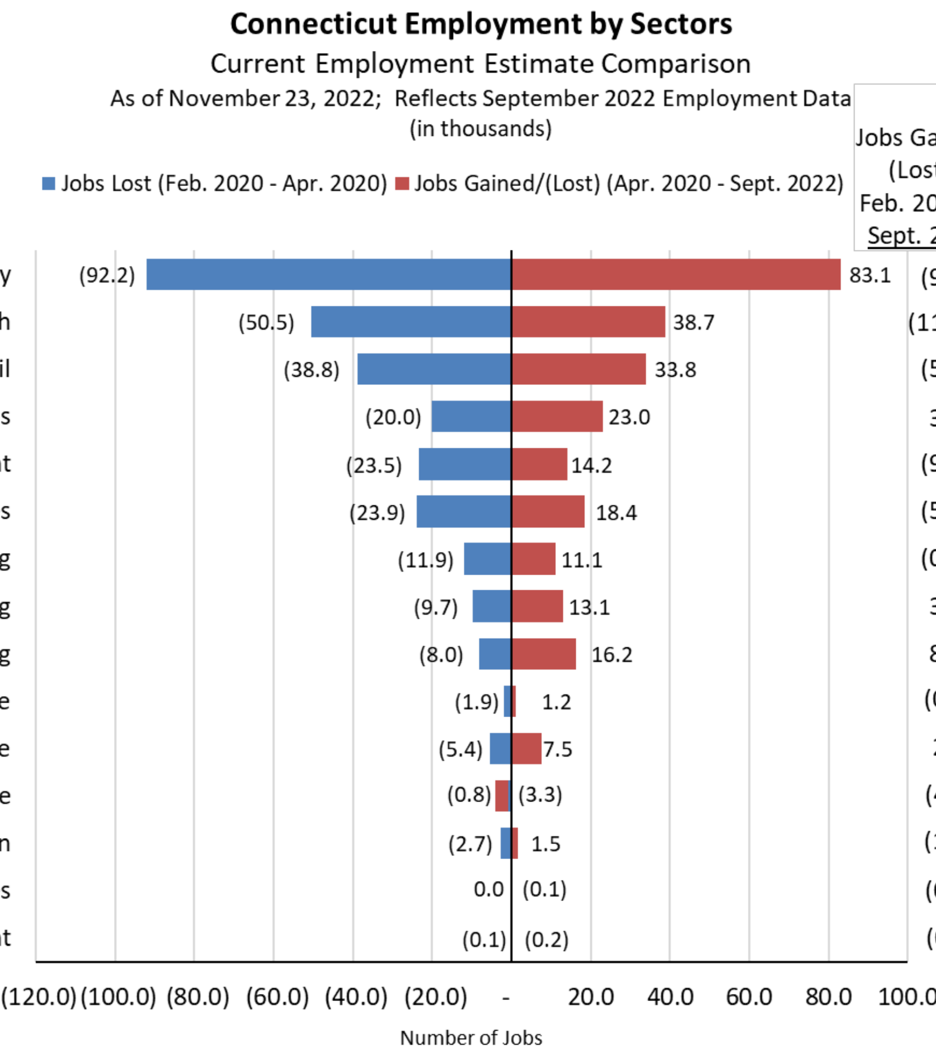
- **89.4% of the 289,400 jobs lost during the pandemic have been recovered**

Connecticut Employment in Calendar Year 2022



- **Connecticut has added jobs every month in 2022**

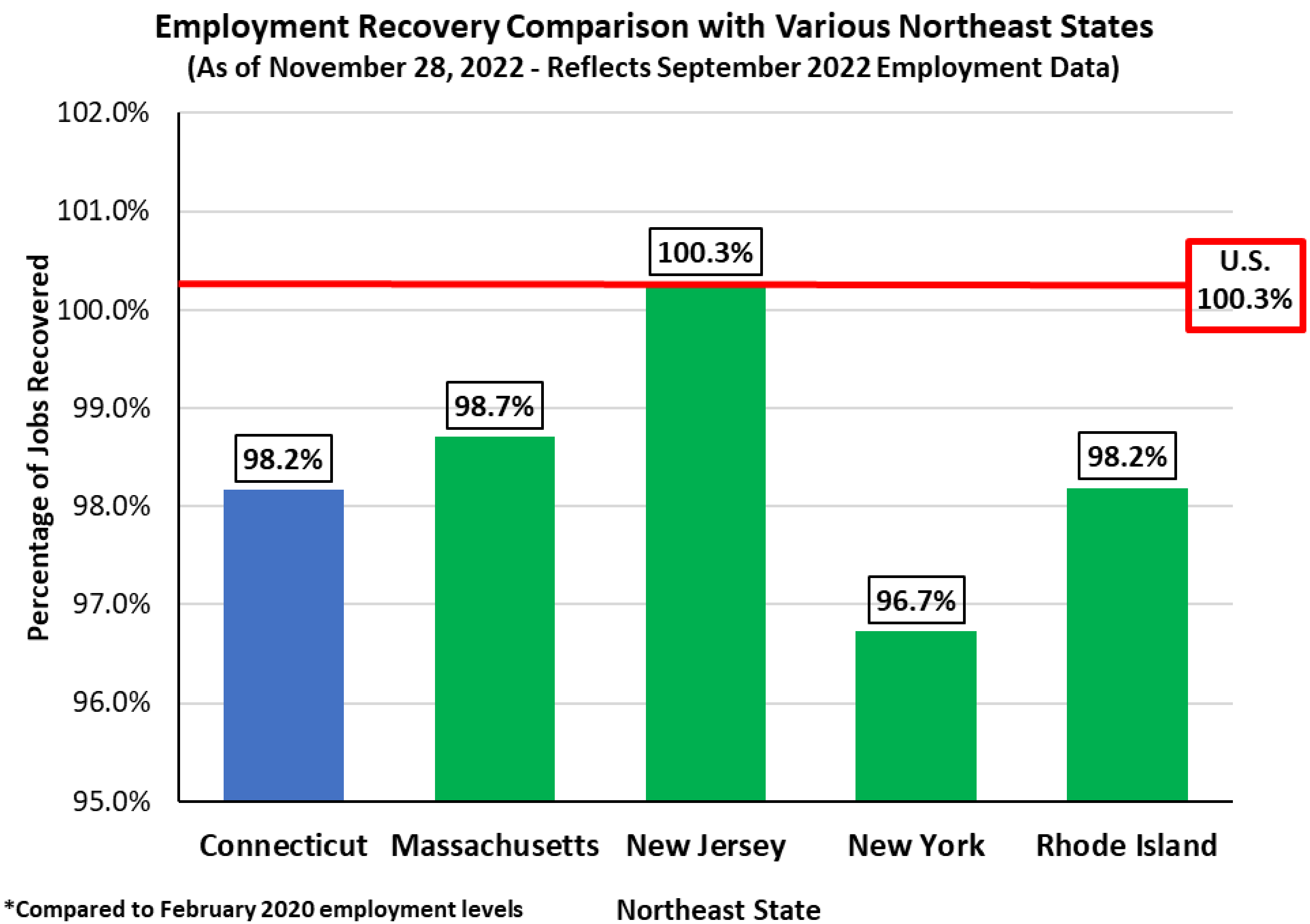
Connecticut Employment Recovery By Sector



Sector	Jobs Lost (Feb. 2020 - Apr. 2020)	Jobs Gained/(Lost) (Apr. 2020 - Sept. 2022)	Jobs Gained/ (Lost) - Feb. 2020 to Sept. 2022	Total Jobs Feb. 2020	Current Job Levels as a % of Feb. 2020 Peak
Leisure & Hospitality	(92.2)	83.1	(9.1)	159.5	94.3%
Education & Health	(50.5)	38.7	(11.8)	351.7	96.6%
Retail	(38.8)	33.8	(5.0)	173.7	97.1%
Professional & Business	(20.0)	23.0	3.0	216.4	101.4%
State & Local Government	(23.5)	14.2	(9.3)	218.1	95.7%
All Other Services	(23.9)	18.4	(5.5)	66.0	91.7%
Manufacturing	(11.9)	11.1	(0.8)	161.0	99.5%
Construction & Mining	(9.7)	13.1	3.4	60.1	105.7%
Transpo & Warehousing	(8.0)	16.2	8.2	55.7	114.8%
Real Estate	(1.9)	1.2	(0.7)	20.1	96.5%
Wholesale	(5.4)	7.5	2.1	59.0	103.6%
Finance & Insurance	(0.8)	(3.3)	(4.1)	102.5	96.0%
Information	(2.7)	1.5	(1.2)	31.5	96.2%
Utilities	0.0	(0.1)	(0.1)	5.1	97.8%
Federal Government	(0.1)	(0.2)	(0.3)	18.6	98.4%

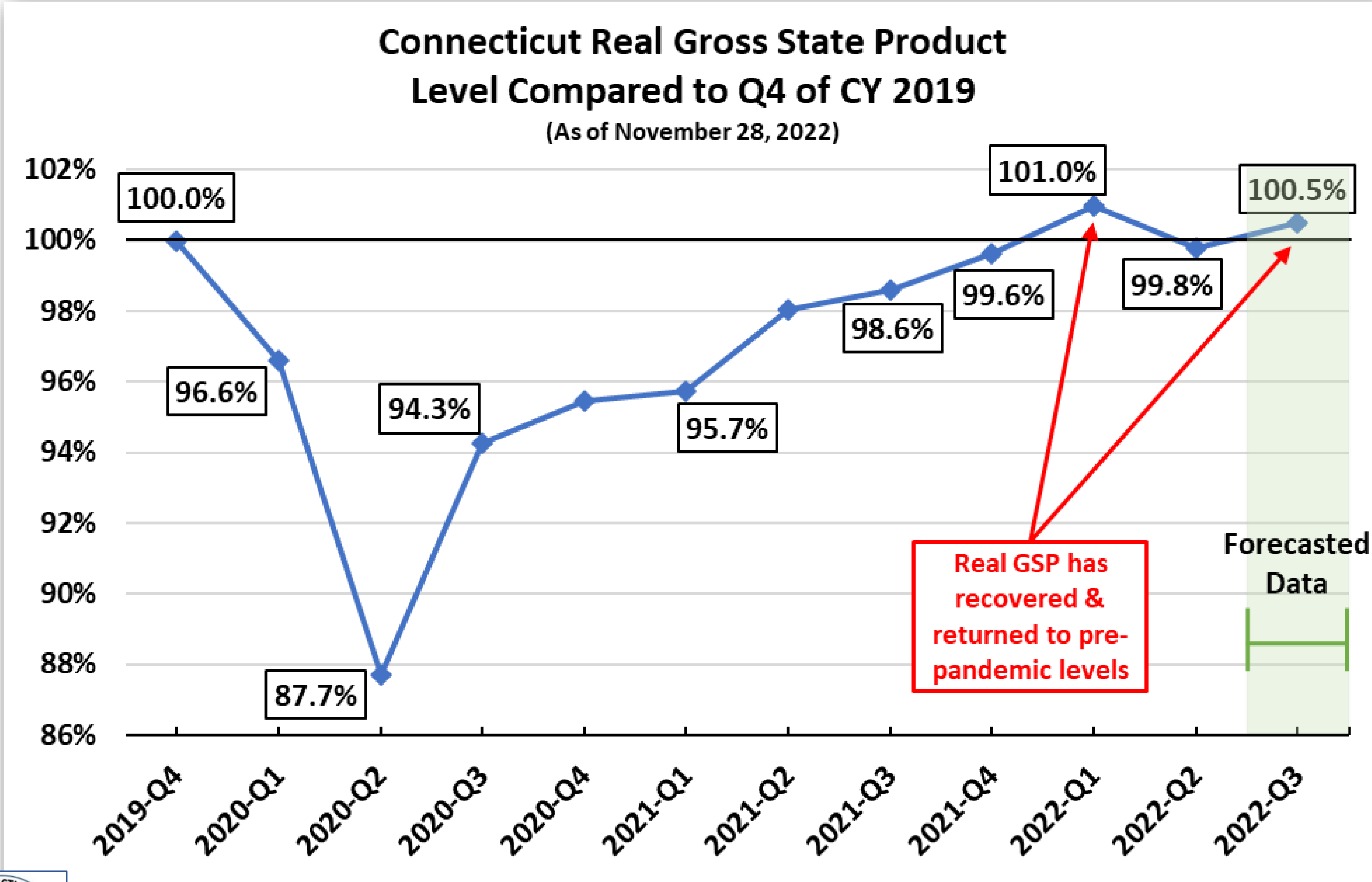
Source: IHS Markit

Connecticut Employment Recovery



- **Connecticut's employment recovery is comparable to neighboring states**

Connecticut Real Gross State Product Has Recovered



Conclusion

Credit Ratings

Rating Agency	Current Rating	Last Upgrade
S&P Global Ratings	AA-	November 2022
Moody's Investor Service	Aa3	May 2021
Fitch Ratings	AA-	May 2021
Kroll Bond Rating Agency (KRBA)	AA	May 2021

- **Connecticut has received a credit rating upgrade from all 4 major credit rating agencies in the last 18 months, with the most recent upgrade from S&P Global Ratings in November 2022**
- **Credit rating <u>upgrades</u> for the state were primarily due to:**
  - Strong financial performance
  - Building up of Budget Reserve Fund (BRF) balance to the 15% statutory reserve cap
  - Supplemental pension payments to reduce unfunded pension liabilities for a 4th consecutive year
  - Strong provisions to promote fiscal discipline
- **Factors rating agencies cite as negatives affecting our credit rating:**
  - High fixed costs for debt, pension, and other post-employment benefits (OPEB)
  - Weakening of budget management policies

Key Takeaways

- A General Fund operating surplus of about $1.0 billion is projected in FY 2023
- The Rainy Day Fund holds over $3.3 billion and is at the 15% limit at the beginning of FY 2023. Balances in excess of 15% will continue to be used to pay down pension liabilities
- Revenue growth is outpacing “fixed cost” growth in FY 2025 and FY 2026, but a significant imbalance is projected for FY 2024, primarily due to loss of non-recurring federal aid and other revenue policy changes that take effect that year
- Long-term liabilities have been reduced $7.1 billion compared to last year’s report
- The Fiscal Accountability Report does <u>not</u> present the entire budget picture for the upcoming biennium – it only presents “fixed costs” vs. revenues
  - The fiscal note when the FY 2023 budget adjustments were passed in May projected a General Fund deficit of $800 million in FY 2024
- **A significant budget balancing task remains for the FY 2024 – FY 2025 biennium**