GOVERNOR DANNEL P. MALLOY
BUDGET ADDRESS FOR THE FY 2018 AND FY 2019 BIENNIUM (ABRIDGED)
FEBRUARY 8, 2017

One of the basic principles of our country is that if you're willing to work hard, you should have the opportunity to succeed. You should be able to buy a house, afford health care or send your children to college. It's a fundamental promise that has come to be known as the American Dream. It's why people from around the globe come here in the hope of a better life.

At all levels of our government so much of what we do is really about delivering on that fundamental promise. While we can disagree strongly on policy or politics, we collectively judge ourselves by how many of our constituents have the opportunity for success.

The truth is that, for too long, we've allowed certain communities to be disproportionately impacted by the fiscal challenges facing our state. While we've made advancements in recent years to address this inequity, I don't believe that we've gone far enough.

Disparities have persisted and grown over the years, creating pockets of concentrated poverty in towns both big and small. It's a vicious cycle that we've created, one that handicaps poorer communities, leaving them with the highest tax burdens in the state and causing them to be even poorer still.

The result is a broken, disparate system, where towns are pitted against one another in a constant fight for limited state dollars. As towns have been forced into this race to the bottom, their state government has failed in many places to build the kind of world-class education system necessary for growing a new generation of workers.

We've failed to build a modern transportation system that efficiently moves people or products from one place to another. And we've failed to build thriving, vibrant city centers where industry and businesses want to grow.

The truth is, other states have had the foresight to make necessary investments in these areas, and, as a result they've gained a competitive advantage on us. But it's not too late. The opportunity is before us to turn the tide this year so we can compete nationally and internationally in our own right.

To do it, we'll need to build a better, fairer system for supporting our towns and supporting local schools. We'll need to invest in a modern transportation infrastructure that meets the needs of both our residents and our businesses.

And we will need to grow vibrant city centers- communities that are more than just great places to work- but also great places to live and raise a family. This budget lays the foundation for that kind of progress. Progress that doesn't just help our big cities, but that bolsters every community across Connecticut.

We are a small state, and our towns are intrinsically linked. Growth in Hartford means growth in Bloomfield and Windsor. More jobs in Waterbury means more jobs in Cheshire and Beacon Falls. A more vibrant New London, means a more vibrant Ledyard and Sprague.

We can rise together or we can fall together. We can lift one another up or we can drag one another down. Our future depends on the decisions we make today.

The budget contains a total of $18 billion in General Fund spending. This keeps us within the spending cap and growing at a pace well below inflation. More importantly, it does it while making required increased contributions to our pension systems of more than $357 million. If we enact a budget that spends only this $18.0 billion and no more, the result would be an eight-year period where Connecticut's general fund budget grew an average of only 2%. Compare that to the prior eight years, where state budgets grew at a rate of 4.8%.

This year, we can build on our record of fiscal responsibility. To do it, my plan contains $1.36 billion in new spending reductions. These cuts are not made lightly and I know they will include things that people in this chamber strongly support. Let me assure you, they include things that I myself strongly support.

But our economic reality demands that we re-envision state government. Together, we need to provide essential, core services and we need to find ways to do it at less cost to taxpayers.

This year, while you review my budget, it's natural to focus on what we're cutting back. But I ask that you also recognize the many, many important things we preserve. For example, even as we cut spending, we are still putting millions of dollars toward helping Connecticut's chronically unemployed get back on their feet and back to work. We're still fully funding our critical arts and tourism awards. We're still helping the Department of Housing fulfill its mission of matching every single chronically homeless person to permanent housing- the first in the nation to do it! We're still funding new technology for law enforcement that will help keep crime at historic lows. We're still redeveloping brownfields in every corner of this state, turning blighted properties into economic opportunities. We're still committed to supporting the intellectually disabled, with $3.8 million of new funding in my proposed budget. And finally, even as we cut back, we're still going to keep Connecticut's beautiful state parks open and available to all our constituents.

We're doing all these things, and so much more. Of course, as we continue to make reductions to state agencies, we also need to redefine the relationship between state government and state employees. As I said last month, my administration is engaged in productive conversations with state employee representatives. Those discussions can and will continue to play out in good faith and I'm hopeful that we will reach a positive conclusion in the weeks ahead.

At the same time, I have an obligation to submit a balanced budget to this General Assembly. It's only appropriate that I reflect my goals for labor savings. To that end, to help close the $1.7 billion hole we face, the budget before you assumes $700 million in state employee labor savings. The budget also describes how these savings could be achieved should we fail to reach agreement with our employees, because presenting a budget without planning for this contingency would be irresponsible.

Now, while I will not betray the confidence of my administration's conversations with labor thus far, I do want to say a few things about the potential for a new labor agreement. First, I want to once again acknowledge and commend our state employees for what they've already sacrificed to help balance our budget. More importantly, I'd like to thank them for the hard work they put in each and every day serving the people of Connecticut.

Here's something else I want to recognize – and it's something I would like everyone in this chamber to keep in mind in the coming weeks. State employees have an existing contract, one that was originally negotiated 20 years ago by John Rowland. In other words, we are not starting from scratch when we revisit the SEBAC contract. While it is fair for us to ask for savings, it's equally fair for our employees to also ask for changes, as long as the end result is a more affordable, more sustainable labor agreement.

As I said to you from this podium last month, we cannot talk about more cuts in services and we cannot talk about labor savings without discussing town aid. At more than $5 billion, municipal aid accounts for our single largest state expenditure. And addressing town aid really means that we are addressing educational aid, which amounts to $4.1 billion or 81 percent of all municipal funding from the state.

Here's a simple truth: education is economic development. A pipeline of skilled and prepared workers is essential for thriving industries and growing businesses. It's why we value our state's public education system. It's why it matters so much that we get it right and get it right this year. That begins with our educational cost sharing formula, or ECS.

I believe the updated ECS formula in my budget is more equitable, more transparent, and more fair. For the first time in more than a decade the formula counts current enrollment. We will no longer reimburse communities for students they don't actually have.

By recognizing shifting demographics in small towns and growing cities, state funding can change with time to reflect changing communities. The new formula also uses a more accurate measure of wealth, allowing the state to better direct support to communities with higher concentrations of poverty. By considering a given communities' ability to pay, we can adjust to what taxpayers can actually afford. Because let's be honest: if a city has a mill rate over 40, not only is that city failing its residents, but Connecticut is failing that city.

Combined with my other proposals, this new formula is intended to bring greater accountability and greater flexibility to a system where it has been sorely missing. It is fair and it is honest. It is predictable and it is sustainable.

Let's make it a reality together.

Of course, you can't talk about education funding without talking about Special Education. For the last quarter century, Connecticut has combined Special Education dollars into ECS. But we know that students with disabilities exist in every community regardless of income or zip code. The result is that we've unfairly obscured the real cost of Special Education in our communities. It isn't fair to local leaders trying to balance their budget and it certainly isn't fair to students with disabilities and their families.

In my proposed budget, Special Education is now a separate formula grant from ECS. It also increases funding by $10 million from the current year. And school systems will be required to seek Medicaid reimbursement where available—ensuring that no community leaves federal dollars on the table.

As we work to make ECS and Special Education funding more fair and more equitable, we also have to grapple with how we fund this new system. As I've already said today, part of the way we do it is by continuing to reduce spending in our state agencies and by working to find savings with state employees.

Making those changes helps free up more dollars for cities and towns with higher concentrations of poverty. But we need to do even more. There's a very large portion of education aid that's almost always left out of the conversation. I'm talking about how we pay for teacher pensions.

This year, state government is set to pay $1.2 billion for a system that supports municipally-employed teachers and school administrators. So you see, when we talk about funding for education, we have to include the state contribution to teachers' pensions as part of that conversation.

Now I want to be very clear -- the Teachers Retirement System is a sustainable, well-organized system and hardworking teachers make a 6 percent contribution to it. I am not proposing that teachers' benefits be limited or cut back. The Teachers Retirement System has always been funded without any contribution from towns or cities. My budget does not propose that we demolish that system or shift the entire costs to towns. But this year, as we continue making cuts to state services and as we ask state employees to find savings, we need towns to begin sharing the cost of their employees' pensions.

After all, teachers are municipal employees. The state doesn't pay the pensions of policemen, or firemen, or anyone else. As such, my budget asks our towns and cities – all of them – to contribute one-third of the cost toward their teacher pensions. It isn't just about saving the state money; I believe this is sensible policy.

This funding is based entirely on local decisions on how much towns want to pay their local educators, and how many teachers and administrators they employ. Under my proposal, towns maintain that control, but they do it with some skin in the game.

Let me illustrate for you the disparity that this current system has created in communities across the state. In the current fiscal year, the state is sending $24 million to one of our most affluent municipalities to cover the pension costs of their teachers in a school district that enrolls 8,800 students. Compare that to the City of New Britain, a working class city, which enrolls 10,000 students, where the state will provide only $18 million to cover pension costs for teachers. That's 25 percent less funding for a system with 14 percent more students.

I'm not blaming our wealthy towns for this inequity. It's not their fault. We need to do a better job. We need to make the system more reasonable. And to do that, we need towns to partner with their state in fully-funding teachers' and school administrators' retirement benefits—not all of the cost, but part of it. My budget reflects this partnership- a re-envisioning of education funding to meet 21st century challenges.

Now, I know that state assistance is not always about dollars and cents. Sometimes, we help the most when the state gets out of the way. For our towns to thrive, we must free them from unnecessary burdens. We must remove bureaucratic red tape that isn't producing a discernable benefit for taxpayers.

My budget will give municipalities greater flexibility and additional tools for making local government leaner and more cost efficient. They are designed to increase local control over budgets and contracts, keep down project costs, modernize out-of-date requirements, and remove unnecessary red tape.

Of course, at the same time we are providing mandate relief, we can also increase transparency for how town aid is utilized. For communities that see increased support in this budget, that support can only come with greater accountability for how state dollars are being spent.

Directing state aid and oversight to those who need it the most ensures that the collective strength of a region- or a state for that matter- is that much stronger. It is in our collective best interest that no town is brought to the brink of bankruptcy.

In the past, our state has had various iterations of state boards to oversee towns experiencing financial distress. My proposal builds upon and learns from these past experiences. It will create a Municipal Accountability Review Board chaired by the State Treasurer and the Secretary of OPM. Ultimately, this board, empowered to review municipal finances, will oversee efforts to restore fiscal stability where warranted. Through this tiered accountability framework, we can intervene earlier to help a struggling municipality. And it helps strengthen the state's ability to take actions well before a city or town needs a bailout.

Surely, our towns and cities will sometimes struggle. It is our responsibility to put these municipalities back on the path to fiscal health. We can take action to avoid fiscal crises, and then remove these communities from enhanced state oversight, when appropriate and when they're ready.

The fact is, the prosperity of all Connecticut residents is interconnected, regardless of region or zip code. From the farmer to the factory worker; the nurse to the mechanic; the teacher to the actuary- all are impacted by the successes and failures of Connecticut as a whole.

Unfortunately, far too many of our residents feel as though the system is rigged against them and their communities. A history of shortsighted state government and a record of half-step policy fixes have left people believing that in order for one person or one community to gain, someone else has to lose. I reject that notion.

Dignity, opportunity, prosperity- none of these are a zero sum game. We are all guaranteed access to these fundamental rights. This session, this year, we must reset the system for how we determine town aid. We must ensure that no community or family shoulders more burden than they can bear. We must keep our promise to our students and teachers.

Let's ensure that all Connecticut communities see their fair share of success. Let's give taxpayers, communities, and businesses more predictability and more sustainability. Let's have the courage to collectively tackle the challenge of inequity in town aid. Let's do it so that 10 years from now, no Connecticut city or town needs to levy a mill rate above 40.

It's about more than just how my town or my community or my family did, it's also about other towns and other families as well. We rise and fall together, as one Connecticut. And as one Connecticut, we will prevail.

Introduction

The budget that Governor Malloy is presenting to the legislature is balanced while meeting the most critical needs of Connecticut residents. The budget recommends General Fund expenditures of $18.0 billion in FY 2018 and $18.3 billion in FY 2019. These appropriations reflect year-over-year growth rates in the General Fund of 0.8 percent and 1.8 percent, respectively.

Appropriated Funds Of The State (in millions)		
	Recommended FY 2018	Recommended FY 2019
General Fund	$ 18,000.8	$ 18,320.9
Special Transportation Fund	1,525.1	1,642.7
Municipal Revenue Sharing Fund	340.1	349.0
Banking Fund	30.0	30.0
Insurance Fund	89.8	90.9
Consumer Counsel and Public Utility Control Fund	25.6	25.6
Workers' Compensation Fund	23.8	24.1
Mashantucket Pequot & Mohegan Fund	58.1	58.1
Regional Market Operation Fund	1.1	1.1
Criminal Injuries Compensation Fund	2.9	2.9
Grand Total	$ 20,097.3	$ 20,545.3

Totals may not add due to rounding.

The baseline budget for FY 2018, including updated consensus revenue estimates as well as updated estimates for fixed cost growth, had a gap of $1.683 billion. The Governor's recommended budget closes that gap with $321 million in revenue adjustments and $1.364 billion in expenditure reductions. Those changes roll forward with some adjustments to produce balance in FY 2019 as well.

Baseline Estimate versus Proposed Budget (In millions)						
	Fiscal Year 2018			Fiscal Year 2019		
General Fund	Baseline Estimate	Policy Changes	Proposed Budget	Baseline Estimate	Policy Changes	Proposed Budget
Revenues	$ 17,682.1	$ 320.8	$ 18,002.9	$ 18,038.0	$ 287.4	$ 18,325.4
Expenditures	19,364.6	(1,363.8)	18,000.8	19,954.7	(1,633.8)	18,320.9
Surplus/(Deficit)	$ (1,682.5)	$ 1,684.6	$ 2.1	$ (1,916.7)	$ 1,921.2	$ 4.5

The Governor's budget proposal achieves balance with a combination of challenging moves, including:

- Deep cuts to agency budgets;
- Cuts in employee-related costs. These cuts will be achieved through pension and benefit revisions that are currently being sought in discussions with the state employees coalition, or through layoffs of state workers;
- A new partnership with local governments aimed at redirecting state aid to those communities that most need state assistance;
- Shifting one-third of the costs of the Teachers' Retirement System (TRS) to local governments; and
- Some additional revenue, including fees, enhanced collection efforts, reduction of some tax credits, increased tobacco taxes, and other adjustments.

Context and Framework for Budget Development

These measures are necessary because the state faces a daunting scenario of slow-growing revenues to support fast-growing fixed costs, particularly pension and healthcare costs. Moreover, we face an economy that remains fragile and an unprecedented level of uncertainty about federal revenue, especially federal support for healthcare and federal infrastructure investments. In this environment, calls to solve our budget shortfall with broad-based tax increases must be considered in light of near-term risks to our economic health. In the longer term, we should weigh the value of solving our budget problems today against the ability in the coming years to sustain the most critical parts our healthcare system in the face of deep cuts promised by both Congress and the President.

Slow-Growing Revenue

The Governor's proposed budget is based on the January 2017 consensus revenue estimates, which project total revenue of $17.682 billion for FY 2018, down about 1 percent from the FY 2017 forecast of $17.898 billion. Those baseline revenues are expected to rebound slightly to $18.038 billion in the second year of the biennium. While the main reason that consensus revenue shows a nominal decline between FY 2017 and FY 2018 is the rollout of the 0.5 percent sales tax diversion to the Municipal Revenue Sharing Fund, coupled with scheduled decreases in personal income taxes for beneficiaries of the Earned Income Tax Credit and for retired teachers, it is nonetheless troubling for state revenues to be growing so slowly when the state is not in recession.

Nationally, growth in sales tax collections has been slower than growth in income and the overall economy growth. Analysts point to growing internet sales and changing saving and purchasing habits to explain this apparent disconnect. Regardless of the reason, in Connecticut we can expect to see relatively small increases in sales tax collections over the biennium.

While income taxes continue to grow more strongly than sales taxes, growth is slower than expected for the withholding portion of our income taxes. Consensus revenue estimates assume growth around 3.5 percent compared to over 5 percent in prior non-recession periods. The ever-volatile estimates and finals portion of our income tax remains uncertain. Connecticut has, in its best years, received extraordinarily large tax payments from a relatively small number of individuals. Lagging investment returns in this sector can remove hundreds of millions of dollars from Connecticut's revenue stream, and do so without any advance notice.

The difficulty of projecting these income tax revenues is compounded by uncertainty about federal tax policy, and the complex reactions of sophisticated investors to any anticipated changes. State analysts have significantly reduced their expectations for income tax revenue as a result, but it remains to be seen whether the adjustments are sufficient.

Addressing Long-Term Liabilities

The FY 2018 - FY 2019 biennium promises to be a period in which state government begins to make significant headway on addressing its long-term liabilities. In both major pension funds, contributions are scheduled to rise significantly in FY 2018 and FY 2019 as a result of poor investment returns in recent years, coupled with changes in the accounting of both funds that are intended to calculate appropriate contributions more conservatively.

The Teachers' Retirement Board recently changed its investment return assumption for the teachers' pension system from 8.5 percent to 8 percent. This change, coupled with investment and experience factors, will result in a hike in required employer contributions from $1.01 billion to $1.29 billion, an increase of 27.5 percent. This fund will amortize all unfunded liability by 2032, and has a higher funded ratio than the State Employee Retirement System (SERS).

The State Employees Retirement Commission also lowered its investment return assumption for SERS in the past year, from 8 percent to 6.9 percent. This change was made possible by an agreement to adjust the method and schedule of amortizing unfunded liability. While these changes reduce the risk of multi-billion dollar increases in annual contributions toward the end of the next decade, the funding plan does require increases of around $150 - $180 million each year until payments stabilize at around $2.5 billion annually, up from $1.6 billion today.

In the area of post-employment benefits, FY 2018 will be the first year in which the state is required to match the 3 percent employee contributions to retiree health that were agreed to in the 2011 State Employees Bargaining Agent Coalition (SEBAC) agreement. That will add a new $120 million cost in each year of the coming biennium and beyond. While this new arrangement still falls short of full actuarial funding of retiree health benefits, the total contribution to retiree health care budgeted in FY 2018, including state and employee contributions, plus pay-as-you-go funding for current retirees, equals nearly $1.035 billion.

Coping with Uncertainty in Washington

While the budget makes modest reductions within the Medicaid program, it does not reflect the potentially disastrous consequences to a successful Medicaid program that could result from federal actions under consideration. The possible repeal of all or significant parts of the Affordable Care Act and proposals to reduce federal Medicaid spending by converting the program to a block grant or imposing per capita caps erode the federal-state partnership and the access to health care for Medicaid beneficiaries. Reductions in federal support will likely force Connecticut to limit services, to drastically cut coverage to thousands, and as a result, could shift health care provision to inappropriate and more costly venues such as hospital emergency rooms, shelters and prisons.

Our state already employs existing program flexibilities to innovate. Connecticut, with its unique managed fee for service model and use of data analytics, has implemented and continues to focus on care delivery and value based payment reforms. As a result, our state is one of the few Medicaid programs whose expenditures on a per member per month basis have been relatively steady over the last five years, while first improving and now maintaining excellent outcomes.

An internal work group has already begun to assess the potential impact of ill-advised federal efforts to take medical assistance away from Connecticut residents. Should the Congress act to pass policies negatively affecting our medical program, we will reassess the impacts and develop a set of policy alternatives for consideration. To reiterate, this budget does not reflect any potential changes in federal law, nor does it contain any flexibility to absorb the impact of federal actions to reduce or eliminate support for Medicaid services.

A Budget that Reflects Connecticut Values

In the context of national economic and political uncertainty, slow state-level revenue growth, and an urgent need to address long-neglected liabilities in an aggressive manner, Connecticut should strive to develop a budget that reflects its core values.

This budget should reflect our belief in the value of stability, building a more predictable environment for businesses and families alike. This means finding ways to keep our most important commitments on tax policy and programs for residents. Perhaps more importantly, this means building a budget based on recurring solutions that will help us meet our future challenges as well as our current ones.

This budget should also reflect our Connecticut orientation toward compassion. This budget should strive to dedicate scarce resources to those who need them most, and should acknowledge the sacrifices involved for those who have more. We should use this opportunity to shore up the capacity of our struggling big cities to fend for themselves just as we provide healthcare, preschools, and affordable housing to those families who need a leg up. Do not read this as a call to tax more and spend more. Rather, this budget should reflect our Connecticut compassion as it distributes the scarce funds we do have more fairly and justly.

Reducing Spending

The Governor's proposed budget reduces spending by nearly $1.4 billion in FY 2018 and $1.9 billion in FY 2019. This reduction includes in FY 2018:

Collective Bargaining Savings	$700 million
Municipal Contribution for Teachers' Retirement	$408 million
Agency Reductions (including annualizing 2017 holdbacks)	$256 million

The agency reductions include reinstituting $130 million of agency holdbacks implemented in FY 2017, plus an additional $126 million in net reductions tied to specific policy options. These cuts impact more than 50 agencies and account for 1.8 percent of state spending on top of savings related to labor costs. The options that constitute these cuts do not require significant layoffs, although some policy options may eliminate positions or reorganize specific governmental functions.

A New Partnership with Labor

The Governor's budget proposal includes $700 million in savings from labor in FY 2018 and $868 million in FY 2019. It is anticipated that these savings will be accomplished through an agreement with SEBAC on pension and health benefits, along with agreements with constituent member bargaining units covering wages and other terms.

It is important to note that the current agreement between the state and SEBAC does not expire until 2022, so the state cannot unilaterally change current pension or health benefits. Instead, the state is seeking a voluntary agreement to change pension and benefit terms.

In the unlikely event that the state is unable to come to such agreements, this budget proposal would require state government to take alternative steps, potentially including layoffs of up to 4,200 employees, in order to satisfy that savings target.

A New Partnership with Local Government

The Governor's budget proposal calls for significant changes to the structure and distribution of state aid to local governments. These changes are intended to make municipal aid much more targeted to those communities that have greater service demands - especially in their schools - coupled with lesser ability to pay based on their lower grand lists, higher tax rates, and greater concentration of tax exempt property.

The changes which accomplish this greater needs-targeting of municipal aid include:

- Distributing education aid through two fully-functioning aid formulas. First, a foundation-based Education Cost Sharing (ECS) grant, and second, a sliding-scale reimbursement grant for special education expenses. Ten million dollars in new funding is added to the special education grant compared to FY 2017;
- Eliminating the property-tax exemption for the real property of hospitals. To help address the tax payments due to towns from hospitals which may exceed $200 million, the state will provide $250 million in new supplemental payments to hospitals;
- Maintaining the Municipal Revenue Sharing system adopted in 2015, including the car-tax cap and enhanced payments in lieu of taxes;
- Leaving $75 million in undistributed funding within the Municipal Revenue Sharing Fund to provide for legislatively-directed transitional aid; and
- Requiring that municipalities pay one-third of the cost of the TRS.

These measures are necessary in order to address the shortcomings in our education finance system that were highlighted in the decision last year in the Connecticut Coalition for Justice in Education Funding (CCJEF) case. Connecticut has a constitutional and a moral obligation to fix our current system, in which the quality of a child's public education opportunities is based on the value of real estate in that child's town. Moreover, we can see plenty of examples where that reliance on local property taxes to fund education and other services in our poorest communities - even with state help - results in punitive levels of property taxation leading further to devaluation of property and disinvestment. In our poorest communities we are in a cycle of fiscal distress that makes recovery impossible without systemic change as is proposed in this budget.

Changes in funding formulas and tax systems are necessary, but not sufficient, to resolve the fiscal distress that threatens too many of our communities. In addition, we need to create a system of review and accountability that will identify fiscal stress and introduce measures to alleviate it. We require a set of checks and balances that will ensure that the state's investment in communities leads to growing prosperity, stability, and, most of all, educational opportunities.

The Governor is proposing a four tier system of accountability under which, based on current information, approximately twenty municipalities would be subject to increasing levels of accountability review based on their fiscal condition and the amount of state aid that they receive. The vast majority of the communities would be un-tiered based on their strong fund balances and credit ratings, along with low levels of state aid. Both tiered and un-tiered municipalities would benefit from significant mandate relief, including relief from: the current local budget cap; the minimum budget requirement; and a number of other mandates covering labor, property tax administration, and education.

For communities experiencing varying levels of fiscal stress and/or receiving higher levels of state aid, the proposed legislation would place them in one of four tiers. Tier I is the lowest level within the new accountability structure and would involve review of local finances by the existing Municipal Finance Advisory Commission (MFAC). Municipalities placed in Tier II or III would be referred to the newly formed Municipal Accountability Review Board (MARB), which would provide higher levels of accountability and review. The MARB would also act on requests for exemptions from the property levy cap that would apply to Tier II, III and IV municipalities. The local chief elected official or the MARB could request to place a community in the highest tier, Tier IV. In Tier IV, the MARB would have powers modeled on the successful review board in Waterbury, along with the ability to authorize debt restructuring and deficit financing, including those using a Special Capital Reserve Fund (SCRF) backed by the state to enhance the local credit.

Fixed Costs – A Growing Component of State Spending

For too long, Connecticut failed to plan and to budget for the long term. Past governors and legislatures pushed off debt, entered into agreements they could not afford, and made promises they did not keep. This budget proposes to pay these past-due bills. As a result, fixed cost growth for FY 2018 exceeds revenue growth in the General Fund by nearly $1.3 billion. The largest one-time factors for this difference include:

- Adoption of more conservative actuarial assumptions for the TRS, which is the most significant factor in the projected $278.3 million increase in the state's required contribution to the fund;
- Under the pension funding agreement reached between the administration and the SEBAC, the General Fund contribution to SERS will increase by $77.5 million in FY 2018. These costs are expected to continue to increase by $125 - $150 million per year until leveling-off after FY 2022;
- The final year of repayment of the 2009 Economic Recovery Notes contributes $178.7 million to non-recurring debt service costs in FY 2018; and
- A state contribution of $120 million to the Retiree Healthcare Fund in FY 2018, the first year of matching employee contributions to address Other Post-Employment Benefits (OPEB) underfunding.

Beyond FY 2018, revenue and fixed cost growth are anticipated to be much more closely aligned, as depicted in the table below.

GENERAL FUND FIXED COST DRIVERS
(in millions)

	FY 2018 vs. FY 2017	FY 2019 vs. FY 2018
Revenue Growth*	$ (204.6)	$ 355.9
Fixed Cost Growth:		
Debt Service	$ 253.3	$ (65.3)
State Employee Pensions	79.3	126.7
Teacher Pensions	278.3	41.9
State and Teachers OPEB	203.8	74.7
Medicaid	207.6	126.1
Other Entitlements	24.8	29.7
Total Fixed Cost Growth	$ 1,047.1	$ 333.8
Difference	(1,251.7)	22.1

* Jan. 17, 2017 Consensus vs. Adopted FY 2017 Budget

Education, Workforce and Arts and Cultural Programs

Changes to the Connecticut Technical High School System (CTHSS)

In an effort to be more transparent with CTHSS resources, the appropriation is separated into two distinct accounts to better reflect staffing and operating funding. In addition, in order to provide better service and coordination, the Governor is proposing the reallocation of staff from the department's central office as well as staff within the schools. Fiscal, human resources, and information technology staff will be reallocated to the CTHSS central office to align with CTHSS' recent regional approach, which assigned the schools to one of four regions in the state. The reallocations save $2.7 million and will not impact instruction or require the closure of any schools.

Managing Cost in the Care for Kids (C4K) Program

The Child Care Development Block Grant (CCDBG) was reauthorized in November 2014 and brought with it sweeping changes to the program but no increase in federal funding. The major changes were moving from an eight-month to a twelve-month eligibility redetermination; extension of the child care subsidy during a three-month job search if an enrolled parent loses employment; and a three-month graduated phase-out at the end of the twelve-month redetermination. These changes, while beneficial in keeping families in quality child care for longer, have required that the state no longer accept new applications to the C4K program in order to stay within the available funding. Priority Group 4, which is made up of working parents who earn less than 50 percent of the state median income, was closed to new applicants in August, 2016. The closure of Priority Group 2 (former TFA recipients) and Priority Group 3 (teen parents ages eighteen to twenty-one) followed in January 2017. The Governor's recommended funding for C4K would allow the Office of Early Childhood (OEC) to start accepting those families placed on the waiting list mid-year in FY 2019.

Higher Education Funding

The Governor's proposed budget reduces funding for the public institutions of higher education by 4.3 percent from FY 2017 levels, while sustaining support for important new initiatives including Next Generation Connecticut at UConn, Bioscience at the UConn Health Center, and developmental education at the Connecticut State Colleges and Universities (CSCU). Additionally, the budget consolidates funding at CSCU for the three systems of higher education, the central office, developmental education and outcomes-based funding into a single new operating fund, which provides enhanced flexibility and recognizes efforts by the Board of Regents to better coordinate efforts in service of a statewide mission.

Office of Higher Education (OHE)

This budget makes OHE a separate division within the State Department of Education (SDE) rather than a freestanding agency. The reorganization will enhance and solidify the continuum of pre-K to post-secondary education in Connecticut. Many of the agency's programs, including the National Service Act, the Minority Advancement Program, and the Minority Teacher Incentive Program, complement ongoing efforts at SDE. The new federal Every Student Succeeds Act (ESSA) requires that the pre-K to 12 and higher education systems work together to develop the state ESSA plan, and implement the approved policies and programs included in the plan. The merger of these agencies will facilitate this coordination through the use of shared resources to achieve these important goals and guide Connecticut's educational system into the future.

Housing Programs

To continue his support for the residents impacted by crumbling foundations, Governor Malloy's budget provides $2.7 million, in the Department of Housing (DOH), to subsidize interest rates on loans to remediate the problem.

The Governor's proposed budget also maintains funding for various housing programs, including rental assistance and emergency shelters. The investment in housing programs has been instrumental in Connecticut becoming the second state to end chronic homelessness for veterans and successfully match chronically homeless individuals with housing.

Arts, Culture and Tourism

For FY 2018, the Governor's proposed budget maintains funding for arts and tourism programs. Funding for specific earmarks has been consolidated in separate lines for Tourism and for Arts and Historic Preservation.

The budget also continues to invest in marketing the state as a premier destination for tourism and business growth. Marketing efforts in recent years have proven invaluable in developing this job-rich sector of our economy, particularly in southeast Connecticut with its wide array of tourist destinations.

Department of Economic and Community Development
Arts and Tourism Funding

	Available FY 2017	Recommended FY 2018	Recommended FY 2019
Arts - Line Item Grants[1]	3,085,264	3,085,264	2,849,378
Arts Commission	1,497,298	2,097,823	2,097,823
Total Arts Funding	4,582,562	5,183,087	4,947,201
Change from prior year		600,525	(235,886)

	Available FY 2017	Recommended FY 2018	Recommended FY 2019
Tourism - Line Item Grants[2]	1,525,100	1,525,100	1,343,976
Change from prior year		-	(181,124)

[1] Includes the following grant recipients: Hartford Urban Arts Grant, New Britain Arts Council, Neighborhood Music School, National Theatre of the Deaf, CT Flagship Producing Theaters Grant, Performing Arts Centers, Performing Theaters Grant, Art Museum Consortium, Litchfield Jazz Festival, Arte Inc., CT Virtuosi Orchestra, Greater Hartford Arts Council, Amistad Vessel, New Haven Festival of Arts and Ideas, New Haven Arts Council, Twain/Stowe Homes, and Cultural Alliance of Fairfield.

[2] Includes the following grant recipients: Discovery Museum, Connecticut Science Center, Barnum Museum, Stepping Stones Museum for Children, Maritime Center Authority, Beardsley Zoo, and Mystic Aquarium.

Health and Human Services

Department of Public Health (DPH)

Several significant investments are made in the Governor's proposed budget to fund initiatives designed to enhance public health. Approximately $9.5 million is recommended to make the human papillomavirus (HPV) vaccine universally available to privately-insured eleven and twelve year olds through the Connecticut Vaccine Program, comparable to access now afforded to publicly-insured children through the federal Vaccines for Children program. Vaccination for HPV has been recommended by the Centers for Disease Control and Prevention. Similar to other universally-available vaccines, DPH will purchase the HPV vaccine at a federally-negotiated price that is currently approximately 45 percent lower than the market price, resulting in significant savings for private health insurers who support the childhood immunization program through an industry assessment.

DPH is responsible for ensuring the adequacy and purity of Connecticut's drinking water. The agency accomplishes this through technical assistance, education and regulatory enforcement of state laws and the federal Safe Drinking Water Act. The Governor is proposing additional funding, approximately $630,000 in FY 2018 and $1.9 million in FY 2019, to address projected shortfalls in federal funds that support these efforts and implement a newly proposed public water system "license to operate" program. Beginning in FY 2019, these costs will be offset by fee revenues. Connecticut will join the majority of other states that utilize fees and service charges to support public drinking water programs.

The budget proposes the addition of two positions to support the licensure of urgent care centers. These staff will support the Department of Social Services (DSS) in pursuing a new initiative called “Safe to Wait.” Designed to reduce non-emergent emergency department visits, this program provides Medicaid beneficiaries with information and education about alternatives to the emergency department and connects them to primary care and licensed urgent care centers throughout the state.

Also recommended are two new positions for the Office of Health Care Access (OHCA) to implement the findings of the Certificate of Need (CON) task force. Specifically, these positions will support expansion of monitoring and oversight responsibility over health care mergers and acquisitions, including enhanced post-transfer compliance, and refocused emphasis on increasing access and promoting health equity through identification of unmet health care needs and recommendations to address those needs.

Support for the state’s newborn screening program is consolidated in the General Fund. In past years, newborn screening fees have been diverted in part to support laboratory testing and follow up care by regional treatment centers. The Governor proposes redirecting all fee receipts to the General Fund as revenues, a gain of approximately $3.1 million, and appropriating funding to continue this critical work.

Departments of Developmental Services (DDS) and Mental Health and Addiction Services (DMHAS)

The Governor’s proposed budget preserves funding for critical residential and day services programs in DDS, provides funding to annualize and fund additional placements for individuals aging out of services in the Department of Children and Families (DCF) or local education agencies, and funds additional community-based placements each year for initiatives such as Money Follows the Person. New funding annualizing at $3.8 million is provided to support the efforts of the Intellectual Disability Partnership created last year to develop innovative and cost-effective ways to serve individuals with intellectual disabilities. This funding will help address the waiting list and explore initiatives that can develop a broader continuum of community-based residential services. Additionally, $1.8 million of this funding will stabilize providers undergoing conversion of DDS grant-funded services to Medicaid fee-for-service payments by allowing rates for the lower-paid providers to be increased without having to reduce funding for the higher rate providers. Reductions in funding which previously supported state-operated services were taken to reflect further downsizing of state-operated services like Southbury Training School and regional centers, as well as ongoing conversions of state-operated residential community living arrangements (CLAs) to privately-operated CLAs.

Similar reductions were also taken in DMHAS to reflect the conversion of certain state-operated programming in Local Mental Health Authorities to private providers. Also, in an effort to streamline services and enhance service delivery, DMHAS will centralize detoxification services in Middletown by relocating a 21-bed program from the Blue Hills campus in Hartford. This restructuring will not result in any loss of beds in the DMHAS system. The DMHAS budget also proposes consolidation of advocacy organizations and realigns like funding in a more simplified agency account structure. Further reductions are assumed within the agency’s grant accounts to reflect increased private provider revenue associated with the Medicaid expansion.

Department of Social Services (DSS)

The most significant change in DSS is related to a proposal to revert back to the eligibility levels that were in place under the Medicare Savings Program (MSP) prior to FY 2010, in order to bring Connecticut's eligibility levels more in line with other states. Even with this change, Connecticut's levels will still exceed the majority of other states. Connecticut is also one of only eight states that does not have an asset test for MSP, and the Governor is not proposing to reinstitute one. The proposal will reduce state Medicaid expenditures by $29.6 million in FY 2018 and $39.5 million in FY 2019 ($59.2 million in FY 2018 and $79.0 million in FY 2019 after factoring in the federal share). These savings figures reflect the state's share of Medicaid expenditures, which cover the costs of deductibles, coinsurance and copayments under the Qualified Medicare Beneficiary program, which is by far the largest of the three components of MSP. In addition, because Medicare premiums are paid for (deducted from) Medicaid revenue, less revenue will be needed to cover these costs, resulting in additional revenue of $36.9 million in FY 2018 and $42.1 million in FY 2019. In total, after factoring in some funding to assist with the transition, this proposal will result in net savings to the state of $66.4 million in FY 2018 and $81.6 million in FY 2019.

Another area where the Governor proposes to align Connecticut's program eligibility with that of other states is the proposal to reduce income eligibility for HUSKY A adults to the same level as that for low-income adults under HUSKY D. As of January 2016, Connecticut was one of only a few states still providing coverage to parents and relative caregivers with income over 138 percent of the federal poverty level. This proposal will reduce state expenditures by $500,000 in FY 2018, $11.3 million in FY 2019, and $14.9 million in FY 2020 ($1.0 million in FY 2018, $22.6 million in FY 2019 and $29.8 million in FY 2020 including the federal share). Coverage for pregnant women and children enrolled in HUSKY A will not be impacted.

Effective July 1, 2015, the Medicaid portion of the Birth to Three program was transferred from DDS to DSS while the non-Medicaid portion was transferred to the OEC. As Medicaid participation in Birth to Three continues to grow – currently over 60 percent of program enrollees – the Governor is proposing to move the balance of the program from OEC to DSS to better align Medicaid funding and health services under DSS.

Other proposed reductions include limiting intake to the state-funded home care program, eliminating funding for the small hospital pool, capping adult dental benefits, and consolidating several non-entitlement accounts and programs and reducing their overall funding.

Temporary Assistance for Needy Families

Changes have also been made in the Governor's proposed budget to simplify the Temporary Assistance for Needy Families (TANF) block grant process. Connecticut receives $266.8 million per year under the TANF block grant and transfers 10 percent of this amount to the Social Services Block Grant (SSBG). This SSBG/TANF transfer comes with federal restrictions, reporting requirements and interagency transfers that are administratively burdensome. In the Governor's proposed budget, 10 percent of the TANF block grant is transferred to the Child Care and Development Fund (CCDF) rather than to SSBG/TANF. As a result, the General Fund appropriations for DSS, DOH, and DCF will increase by $10.3 million, in total, and the formerly transferred TANF funds will revert back to normal TANF revenue and be deposited to the resources of the General Fund. The remaining $16.4 million in SSBG/TANF funding, which is currently used by OEC for child day care services, will then transfer to CCDF and continue to be used for child day care services. An additional $10.3 million will also be transferred from OEC's General Fund appropriation to CCDF, such that $26.7 million in OEC services is funded with CCDF dollars. This change results in no net impact on revenue or General Fund appropriations and no reduction in services. By reducing the need for multiple allotment activities, development and revision of interagency memoranda of agreement, funding oversight, and monitoring and federal reporting requirements, this change simplifies administrative activities related to these services for all agencies involved.

Current SSBG/TANF Funding

Department of Social Services	
Human Services Infrastructure - HSI	$1,178,024
Transitional Living - Domestic Violence	194,592
Case Management	110,543
Anti-Hunger Programs	107,304
Supplemental Nutrition Assistance	340,851
Human Resource Development	251,779
Human Resources Development - Hispanic	260,610
DSS - Total	$2,443,703
Office of Early Childhood	
Child Day Care Centers	$15,697,930
Child Care Licensure	666,791
OEC - Total	$16,364,721
Department of Housing	
Rent Bank	$593,028
Rent Finders	326,832
Security Deposit Program	129,646
Special Projects	46,818
Transitional Living Programs	347,254
Emergency Shelters	3,217,194
DOH - Total	$4,660,772
Department of Children and Families	
Residential Treatment	$3,209,614
DCF - Total	$3,209,614
Total SSBG/TANF Funding	**$26,678,810**

Proposed Realignment of SSBG/TANF and Child Care Development Fund Programs

	Shift from SSBG/TANF to GF	Shift from GF to CCDF	Shift from SSBG/ TANF to CCDF	Net Total	
Department of Social Services	$2,443,703	$0	$0	$2,443,703	
Office of Early Childhood	-	(10,314,089)	16,364,721	$6,050,632	
Department of Housing	4,660,772	-	-	$4,660,772	
Department of Children and Families	3,209,614	-	-	$3,209,614	
Recap by funding source:					
General Fund Impact	$10,314,089	($10,314,089)		$0	
CCDF Impact		10,314,089	16,364,721	26,678,810	*
SSBG/TANF Impact	(10,314,089)	-	(16,364,721)	($26,678,810)	*
Net impact of proposal	$0	$0	$0	$0	

* Revenue from TANF will be redirected from SSBG/TANF to CCDF to support this change.

Note: Amounts shown are FY 2019 annualized totals. FY 2018 adjustments reflect a 10/1/17 effective date to align with the federal fiscal year for the SSBG allocation plan.

GF = General Fund
SSBG/TANF = Social Services Block Grant/Temporary Assistance for Needy Families
CCDF = Child Care Development Fund

Health Care Reform and the New Office of Health Strategy

The Governor's proposed budget does not include any adjustments related to the potential repeal of the Affordable Care Act. Even if this were to occur, the timing of any such action and the details of what a replacement might look like are largely unknown. In addition, the Governor's proposed budget does not include any adjustments to reflect potential federal changes to the Medicaid program – reduction or elimination of the enhanced match for low-income childless adults, block granting of the Medicaid program, instituting per capita caps, etc. – nor does it reflect potential federal changes that could impact any of the state's other entitlement programs. There is great uncertainty about the future of Connecticut's federally supported entitlement programs. An internal workgroup is following the discussions closely and will be analyzing the potential impact – both financial and programmatic – on access to health care under any scenarios that may be offered by the administration in Washington.

In order to coordinate efforts to react to potential health care reform changes at the federal level, the Governor is proposing the creation of a new agency, effective July 2018, to be named the Office of Health Strategy (OHS) to enhance coordination and consolidate accountability for the implementation of the state's health care reform strategies. The agency will be under DPH for administrative purposes only and will be created through the consolidation of staff and resources from the Office of Health Care Access (OHCA) currently located within DPH, and the Statewide Innovation Model (SIM) program office and the health information technology officer (HITO) currently located in the Office of the Healthcare Advocate. The executive director of OHS will be responsible for developing a comprehensive and cohesive health care vision for the state, including a coordinated state cost containment strategy.

Working closely with the HITO, the executive director will oversee the state's health information technology initiatives, including the development and administration of the All-Payer Claims Database (APCD), a large-scale database that will collect and aggregate claims data from all public and private payers. The APCD will make this data available to consumers, payers, providers, state agencies, employers and researchers in order to improve quality, access and affordability of health care and the performance of the health care delivery system.

The transition of the SIM program office and OHCA will align the proposed major system reforms in SIM with the data collection and health care system monitoring and planning activities being done by OHCA. It is anticipated that major health care reforms will be complemented and facilitated by health care data collection, analysis, and reporting by OHCA, including hospital financial review.

In addition to having the authority to gather and analyze hospital financial, billing, and discharge data, two other major functions of OHCA are the administration of the Certificate of Need (CON) program and the preparation of the statewide health care facilities and services plan. Transferring the responsibilities of OHCA to OHS will ensure that the overall health system planning functions are aligned with the technological and health care reform initiatives being implemented in the state. Aligning the state's major health care planning and reform initiatives within one office will help prevent duplication of resources, and is expected to streamline efforts to improve access to quality health care services, while also reducing costs.

Department of Children and Families

Governor Malloy is committed to meeting the state's obligations to children and families while moving toward ending over twenty-five years of federal oversight of DCF. The department is dedicating approximately $6.4 million in FY 2017 to enhance support for the stability of children and families, promote early identification and access to treatment, and enhance the parent-child relationship. An additional $8.1 million, for a cumulative total of $14.5 million in FY 2018, is recommended to reflect the annualized costs of these service enhancements. The Governor believes these funds are the minimum necessary to comply with the 2004 Juan F. revised exit plan. The plaintiffs in the Juan F matter may seek additional court intervention in order to bring the state into compliance with outstanding performance requirements.

Protection and Advocacy

The Office of Protection and Advocacy for Persons with Disabilities (OPA) is eliminated effective July 1, 2017 as required by Public Act 16-66. The Governor has indicated his intent to re-designate the Protection and Advocacy system from OPA to a nonprofit entity; this transition creates a more independent system and aligns with a national trend where more than 50 of the 57 states and territories have privately operated programs.

Investigating allegations of abuse and neglect of individuals with intellectual disability is of paramount importance and a vital function of state government. Public Act 16-66 includes a provision to transfer the Abuse Investigation Division (AID) within OPA to the Department of Rehabilitation Services. However, upon further evaluation, the Governor believes that abuse and neglect responsibilities would be better supported through DDS. Transfer of the AID function to DDS will strengthen the abuse and neglect system statewide by providing resources to DDS to create a stronger, more efficient system with improved analytics. This restructuring ensures that all cases will be viewed through a broader definition of what constitutes abuse and neglect, and will eliminate duplication and reporting confusion while maintaining the necessary safeguards of the existing system.

General Government

Closing a Department of Correction Facility

With crime in Connecticut at a 50-year low and recidivism down dramatically, the state's prison population continues to decline. As of January 1, 2017, the total inmate population was 14,532 - down nearly 1,000 offenders from the same time last year. The current inmate population is substantially below the all-time high of 19,894 in 2008.

The Governor is proposing additional Second Chance Society initiatives in this budget, including bail reform. The proposal will prohibit money bail for persons charged with only a misdemeanor with a few exceptions. It allows defendants the opportunity to make a cash deposit of 10 percent of the bail set. In addition, there will be more frequent bail redetermination. These changes are expected to result in approximately 300 fewer defendants being incarcerated. When combined with the continuing trends in declining crime and prison admissions, these changes will allow another prison closure and four additional units in other facilities to be closed during FY 2018. These reductions will result in fewer posts such that existing staff can be redeployed to posts currently being covered by overtime. It is estimated that $11.9 million in staff and operating costs will be saved in FY 2018.

In conjunction with the changes outlined above, the Department of Correction and OPM are undertaking a process to investigate methods of providing inmate medical care. A Request for Information concerning inmate medical services is being issued for the purpose of identifying service delivery models which will best meet the needs of the department and the inmate patients.

Department of Emergency Services and Public Protection (DESPP)

In 2013, Governor Malloy signed sweeping gun control reforms. Those changes, as well as discussion on national reforms, have led to an increased demand for gun permits and thus an increased workload for DESPP in processing background checks, pistol permits, long-gun certificates and ammunition certificates. In order to keep up with the rising costs associated with these workload increases, the Governor is proposing increasing the state portion of the pistol permit fee to $300, making the initial permit $370, renewable every 5 years at $300. By statute, local authorities retain $70 of the initial pistol permit fee. The current fee for a pistol permit is $140 for the initial permit and $70 for a renewal every 5 years. This fee change is projected to increase revenues for the state by $9 million each year.

In addition to updating pistol permit fees, the Governor is proposing that the various background check fees be increased from $50 to $75. As federal requirements increasingly call for criminal background checks for certain employees such as nursing home workers and education professionals, DESPP has seen a spike in requests for background checks with additional growth anticipated in the biennium. Again, with the cost of conducting background checks rising due to increased demand, the fee increase is necessary to support costs of the entire process. This $25 fee increase is projected to generate an additional $2.6 million in revenue annually.

Sharing Responsibility for Financial Support of Resident State Troopers

Currently, the first two resident troopers requested by any given town are provided with towns reimbursing the state for 85 percent of total cost, while each additional trooper is provided at 100 percent of the total cost. The Governor's proposed budget would generate an additional $1.5 million in General Fund revenue by requiring that towns reimburse for all assigned troopers at the 100 percent rate. Additionally, a surcharge of $750 will be assessed for each constable a resident trooper supervises. This surcharge will reimburse DESPP for the additional operational and technical costs resulting from the utilization of the growing number of constables, storage and retrieval of reports and records, increased technology services, desktop computer network support for Nexgen Records Management System and COLLECT (Connecticut On-Line Law Enforcement Communications Teleprocessing) access, mobile technology support for all equipment in vehicles including mobile data terminals, network and GPS devices, and technology system planning. This is expected to result in reimbursements of $195,000 to the General Fund.

Expanding Openness and Transparency Through the Open Data Portal

Governor Malloy's proposed biennial budget includes funding in the amount of $183,500 to support the annual licensing costs for the Open Data Portal which was previously funded through carryforward funds. The Open Data Portal, located within OPM, was launched in February of 2014 through Executive Order 39 and was created to provide to the public open access to data in its rawest form - before it has been aggregated and analyzed. As of January 2017, there are 535 data sets with over 41 million records. The data has been provided from executive branch agencies under the Governor's authority and includes information regarding business, education, environment and natural resources and health and human services.

Collective Bargaining

Baseline funding requirements for FY 2018 and FY 2019 include significant increases in state employee benefits costs. Due to the agreement to modify the state's approach to funding pensions for state employees, including changes in the assumed rate of return and amortization schedule, costs directly budgeted in the General Fund and Special Transportation Fund related to SERS are anticipated to increase by $82.4 million in FY 2018 and an additional $137.1 million in FY 2019. Costs for retiree healthcare are also anticipated to grow by $63.8 million in FY 2018 and an additional $69.7 million in FY 2019, reflective of healthcare inflation and service usage patterns. In addition to the cost of current retiree healthcare benefits, FY 2018 is the first year that the state is required to match employee contributions to the Retiree Healthcare Fund. The state's contributions will match employee retirement healthcare contributions that were negotiated as part of the 2009 and 2011 SEBAC agreements, and are budgeted at $120 million per year for the biennium. As a result of these increased pension and healthcare requirements, fringe benefits costs in the General and Special Transportation Fund grow by more than $265 million in FY 2018 and nearly $250 million more in FY 2019.

In addition to the cost of fringe benefits, the baseline estimate for the biennium includes the potential costs of wage increases. All bargaining unit contracts, with the exception of the contract for the State Police, expired on June 30, 2016. The impact of granting two years of wage increases in a pattern similar to the increases that were granted in FY 2015, across all budgeted funds and including higher education employees supported by appropriated block grants, totals $300.6 million. In FY 2019, an additional year of increases, including for State Police, whose current contract expires at the end of FY 2018, raises this potential cost by an additional $167.6 million.

The Governor proposes labor savings totaling $700 million in FY 2018 and $867.6 million in FY 2019. Discussions are underway with representatives of the state's workforce, but the outcome and timing of those discussions cannot be reflected with certainty in this budget. Because the exact nature of any contract changes is not known, the distribution of savings between fringe benefits and salary accounts, as well as the distribution across funds and branches of government, cannot be determined at this time. Accordingly, all funding for potential wage increases as well as the proposed labor savings amounts have been budgeted centrally in the General Fund.

If an agreement on labor benefit changes is not reached, the budgeted savings may need to be achieved through a substantial reduction in staffing. The proposed labor savings amounts exceed estimated costs for potential wage increases by approximately $400 million in each year of the biennium. Achieving this level of annual savings equates to approximately 4,200 full-time positions and associated fringe benefits. In the event that labor discussions are not fruitful, this budget proposal will require that we identify a specific lay-off plan including service reductions, in order to achieve the budgeted savings. The following chart illustrates the agency-by-agency impact of a pro-rata reduction of 4,200 full-time employees, which is approximately 9.3 percent of budgeted full-time positions for all funds.

Illustrative Distribution of 4,200 Position Reduction

Agency	Position Reduction Savings	Positions
Legislative Management	3,048,999	42
Auditors of Public Accounts	830,921	12
Commission on Women, Children and Seniors	61,804	1
Commission on Equity and Opportunity	61,804	1
Governor's Office	192,279	3
Secretary of the State	583,705	8
Lieutenant Governor's Office	48,070	1
Elections Enforcement Commission	240,349	4
Office of State Ethics	109,874	2
Freedom of Information Commission	109,874	2
State Treasurer	315,887	5
State Comptroller	1,922,792	26
Department of Revenue Services	4,532,296	62
Office of Governmental Accountability	130,475	2
Office of Policy and Management	872,124	12
Department of Veterans' Affairs	1,668,709	23
Department of Administrative Services	4,552,897	62
Attorney General	2,080,736	29
Division of Criminal Justice	3,364,886	46
Department of Emergency Services and Public Protection	11,921,311	161
Department of Motor Vehicles	4,140,870	56
Military Department	288,419	4
Department of Banking	817,187	12
Insurance Department	1,036,934	14
Office of Consumer Counsel	82,405	2
Office of the Healthcare Advocate	199,146	3
Department of Consumer Protection	1,497,031	21
Labor Department	1,325,353	18
Commission on Human Rights and Opportunities	508,166	7
Workers' Compensation Commission	748,515	11
Department of Agriculture	391,426	6
Department of Energy and Environmental Protection	5,280,811	72
Department of Economic and Community Development	611,173	9
Department of Housing	157,944	3
Agricultural Experiment Station	473,831	7
Department of Public Health	3,433,557	47
Office of the Chief Medical Examiner	343,356	5
Department of Developmental Services	20,244,254	274
Department of Mental Health and Addiction Services	23,609,140	319
Psychiatric Security Review Board	20,601	1
Department of Transportation	23,616,007	319
Department of Social Services	13,672,425	185
State Department on Aging	171,678	3
Department of Rehabilitation Services	817,187	12
Department of Education	12,491,282	169
Office of Early Childhood	782,851	11
State Library	377,691	6
University of Connecticut	14,606,353	197
University of Connecticut Health Center	11,660,361	158
Teachers' Retirement Board	185,412	3
Connecticut State Colleges and Universities	31,815,342	430
Department of Correction	42,006,140	567
Department of Children and Families	22,215,116	300
Judicial Department	29,865,082	403
Public Defender Services Commission	3,069,600	42
Net Fringe Benefit Savings	90,787,561	
Total	**400,000,000**	**4,200**

Teachers' Retirement System

The Teachers' Retirement Fund provides pension benefits for all Connecticut teachers. As of June 30, 2016, the actuarial value of the fund's assets was $16.7 billion, while the fund's liabilities totaled $29.8 billion. The Actuarially Determined Employer Contribution (ADEC) for FY 2018 is $1.29 billion, which is estimated to be 30.35 percent of member payroll. Under current law, the state pays the entire ADEC, despite the fact that the state does not make employment decisions for municipal teachers. In addition to the ADEC, the state issued a $2 billion pension obligation bond in 2008. For FY 2018, principal and interest costs on the bond amount to $140 million in addition to the ADEC payment.

The Governor proposes that municipalities begin to contribute one-third of the employer share of the actuarial cost of funding the TRS. Town-by-town amounts for this contribution have been calculated using the most recently available audited Schedule of Employer Allocations and Schedule of Pension Amounts, which shows pensionable salary by employer for the year ended June 30, 2015; these amounts were then used to pro-rate the FY 2018 and 2019 ADEC. Adjustments to the report were made to capture pension costs associated with regional school districts and endowed academies at the level of financially responsible towns based on resident student participation in those multi-town entities.

Municipalities will be required to contribute a total of $407.6 million in FY 2018 and $420.9 million in FY 2019 to the state's General Fund in support of pension costs. Recommended appropriations for the TRS have been reduced by the amount of required municipal contributions. However, the full contribution into the pension fund will continue to be made through a combination of appropriation and transfer of revenue as required by current statute as well as the provisions of the bond indenture.

Retired Teachers' Healthcare

Between FY 2010 and FY 2017, in only one year was the state's contribution to the Retired Teachers' Healthcare Fund at its statutory level of one-third of total healthcare costs. In FY 2010 and FY 2011, the state made no contribution at all, and in the current biennium the state's contribution was frozen at the level of the FY 2015 appropriation.

The Governor's budget proposes returning the state share in support of these costs to 25 percent. This represents a $10 million increase in funding for FY 2018 over the FY 2017 level and an additional $3.7 million increase in FY 2019.

State Contributions to Retired Teachers' Healthcare Fund	
FY 2010	$ -
FY 2011	$ -
FY 2012	$ 35,259,003
FY 2013	$ 15,882,645
FY 2014	$ 16,630,127
FY 2015	$ 18,829,361
FY 2016	$ 19,959,757
FY 2017	$ 19,922,013
FY 2018	$ 29,999,173
FY 2019	$ 33,719,923

Municipal Aid

A New Approach to Municipal Aid

Since 2011, Governor Malloy has endeavored to maintain or increase levels of support for local governments. In FY 2012, total state aid from all sources equaled $4,168.5 million. That year, we projected municipal aid would rise to $4,917.4 million in FY 2016. In fact, FY 2016 municipal aid was higher than that - $5.047.4 million. This has been driven by increases in ECS, school construction and teachers' retirement contributions. This year, the new Municipal Revenue Sharing program further grows municipal aid to nearly $5.1 billion.

These increases have come at a cost. State employment levels are at their lowest level in decades. Our current budget was balanced with over $800 million in difficult cuts. On two occasions – in 2011 and in 2015 – we balanced the budget without cutting municipal aid, but relied, in addition to spending cuts in state government, on state tax increases that impacted businesses and residents.

Today we face another challenging budget year. While revenue growth is slow, we must fund steep increases in pension and retiree health contributions; finish paying off the economic recovery notes from 2009; and keep pace with growth pressure in Medicaid and other human service programs that the state funds. Given the slow economic growth experienced today in Connecticut and nationally, significant tax increases would be potentially self-defeating, especially in areas where we are engaged in fierce interstate competition.

Furthermore, we must address the shortcomings in our education finance system that were highlighted in the decision earlier this year in the CCJEF. We have a moral obligation to fix our current system in which the quality of a child's public education opportunities are based on the value of real estate in that child's town. Moreover, we can see plenty of examples where that reliance on local property taxes to fund education and other services in our poorest communities - even with state help - results in punitive levels of property taxation, leading further to devaluation of property and disinvestment. In our poorest communities we are in a cycle of fiscal distress that makes recovery impossible without systemic change.

In order to fix school funding in Connecticut this year, we are left with no viable choice except to undertake a wholesale reform of all state aid to local governments. We must rely on functioning aid formulas, and accept that less needy communities may need to receive less in order for us to remedy the crisis that our neediest communities face.

ECS and Special Education

In an effort to be more transparent with state special education funding and to provide a rational and verifiable plan for distributing education aid, the Governor is proposing significant changes to how special education and the ECS grant are funded.

Specifically, special education funding that was included within the ECS formula starting in 1996 will be decoupled and reallocated to a new Special Education grant that is funded on a sliding scale based on a town's relative wealth. This means 22 percent, or approximately $448 million, of ECS funding will be reallocated to the new grant. It would also eliminate funding for the Excess Cost – Student Based grant and reallocate the $140 million to the new special education grant. Finally, in an effort to help districts with their special education costs, the Governor adds $10 million in new funding, for a total Special Education grant of approximately $598 million.

The ECS grant has not been distributed by a rational and verifiable formula for a few years, which is a major detriment as pointed out in the recent state trial court decision in the CCJEF case. The ECS grant will be more rational and verifiable by having funding determined by a formula. The remaining funding after reallocating the special education funding is approximately $1.59 billion, and the Governor proposes distributing this funding using an updated ECS formula. The existing ECS formula is the basis for the new formula, with updates because funding for special education is proposed as a separate grant, and the poverty measure previously used in the ECS formula is no longer accurate. The new ECS poverty measure uses HUSKY A data instead of Free and Reduced Price Lunch (FRPL) data, since community eligibility has made FRPL less reliable as a poverty metric. Because HUSKY A enrollment is much larger than the FRPL numbers used previously, the weighting factor is changed from 30 percent to 20 percent. The foundation has been decreased from $11,525 to $8,990 to reflect that special education will be funded through the new Special Education grant. The threshold factor used in determining a town's relative wealth is changed from 1.5 to 1.24 to make the formula more progressive. And finally, there is no minimum aid ratio for Non-Alliance Districts and the minimum aid ratio for Alliance Districts is 10 percent.

In an effort to help the towns mitigate rising special education costs and capture all federal revenue due the state, the Governor is proposing that all towns be required to bill Medicaid for special education services provided on behalf of Medicaid-eligible children. A unique arrangement allows the towns to share in federal revenue received for special education and school based health center billing.

Municipal Hospital Tax and Supplemental Payments

The Governor's proposed budget provides property tax relief by eliminating the real property tax exemption for hospitals, creating a local property tax option and providing supplemental payments to hospitals to help stabilize hospital finances. Based on estimates from the 2015 and 2016 Grand List, if all municipalities hosting hospitals were to implement the local option, it would raise nearly $212.2 million in property tax revenue. The state will provide $250.3 million in supplemental Medicaid payments to hospitals to help address potential tax loss. Due to anticipated federal matching of the supplemental payments, the state's share of these payments is estimated to be $87.6 million, leveraging $162.7 in federal aid to support the state's hospitals.

Payments in Lieu of Taxes

This budget recognizes the challenges faced by municipalities with high mill rates and significant amounts of tax exempt property. Under the Governor's proposed budget, the two payment in lieu of tax programs (PILOTS) target the greatest reimbursement for state owned property and private colleges to the towns that have the greatest portions of exempt properties. Due to the Governor's proposal to make real property owned by hospitals taxable, these properties will no longer be eligible for PILOT reimbursement.

Municipal Revenue Sharing Fund

This budget continues to support municipal revenue sharing through the select payments in lieu of taxes, an additional revenue sharing grant, grants to regional councils of government, support for ECS, and funding the motor vehicle property tax relief, by appropriating a total of $340.1 million in FY 2018 and $349.0 million in FY 2019. Bringing this significant municipal funding source on-budget has the benefit of increasing the transparency of state resources devoted to municipal aid, and also affects the calculation of the debt limit by directing sales tax revenue designated for municipal aid through the General Fund, and then to the Municipal Revenue Sharing Fund.

Municipal Accountability
Governor Malloy is proposing a plan for greater accountability by municipalities receiving higher levels of state aid and showing evidence of fiscal stress. The Governor's initiative to increase education funding, particularly for poorer communities, is tied to the creation of a statewide board that is empowered to review municipal finances and oversee efforts to restore fiscal stability when warranted. Under this plan, the Municipal Accountability Review Board (MARB) is established. The board will have nine members, including the Secretary of the Office of Policy and Management (co-chair), the State Treasurer (co-chair), four members appointed by the Governor, the local chief elected official, a labor representative from an employee group of the municipality and a member appointed by the Governor recommended by the regional Council of Governments. The proposal provides a system of review, with four tiers determined by factors including bond ratings, fund balance as a percentage of revenues, state aid as a percent of the General Fund budget, increased levels of state aid and equalized mill rates. The proposal also eliminates the municipal spending cap requirement for municipalities that are not in Tiers II, III and IV.

The Governor's proposed budget includes funding of $217,319 for necessary staff and related expenses to support the work of the MFAC and the MARB in their work with designated municipalities.

Revenue Proposals

Over the past few years, the State of Connecticut has enacted policies to incentivize the retention and expansion of those industries that are vitally important to our state. Within the defense and aerospace sectors those initiatives have begun to bear fruit whether at Pratt and Whitney, Sikorsky, or Electric Boat – all three whose outlook in our state is the most assured in decades. In this year's budget proposal, the Governor is recommending changes to the Insurance Premiums tax aimed at ensuring Connecticut remains the most desired location for this important sector of our economy. Lowering the Insurance Premiums tax rate from 1.75 percent to 1.5 percent will provide competitive benefits to local insurance companies whether they are conducting business in this state or in other states. This rate reduction will also provide tangible relief for Connecticut policyholders.

This year's budget also makes changes to the state's Estate Tax which is often characterized as being uncompetitive and driving some of the most wealthy citizens away from the state. This proposal would phase-in an increase in the Estate Tax exemption from its current $2 million level to the federal level of more than $5 million over three years. In addition, the maximum lifetime cap on the total amount that could be paid under the Estate and Gift Tax will be lowered from $20 million to $15 million. These changes are aimed at keeping Connecticut competitive in the region for high net worth individuals.

In order to partially address the budgetary shortfall in the upcoming biennium, the Governor is proposing several revenue enhancements. These include eliminating the property tax credit on the Personal Income Tax, lowering the Earned Income Tax Credit to 25 percent of the federal level, increasing various tobacco-related taxes, and modifying minimum bottle pricing under the state's alcoholic beverage laws. These initiatives are expected to raise $195.7 million in FY 2018 and $190.1 million in FY 2019. Other smaller initiatives primarily involve certain fee changes and increasing the current five cent deposit on carbonated beverage bottles to ten cents. The Governor's proposed budget also seeks to enhance the collection of state taxes through the Department of Revenue Services' "Fresh Start Initiative," which is expected to yield $60 million in FY 2018 and $25 million in FY 2019.

Governor's Revenue Proposals Summary February 8, 2017 General Fund (In Millions)		
Legislative Proposals	**Fiscal 2018**	**Fiscal 2019**
Eliminate the $200 Property Tax Credit	$ 105.0	$ 105.0
Increase Cigarette Tax to $4.35 per pack and Other Tobacco Changes	$ 59.8	$ 52.9
Decrease EITC from 27.5% to 25.0%	$ 25.0	$ 26.0
Lower Insurance Premiums rate from 1.75% to 1.50%	$ (11.0)	$ (22.4)
Make Insurance Premiums 3-tier credit cap permanent	17.4	16.0
Make moratorium on film production tax credits permanent	4.0	4.0
Subtotal - Insurance Premium Tax	$ 10.4	$ (2.4)
Gift and Estate modifications	$ -	$ (20.1)
Modify minimum bottle pricing	$ 1.9	$ 2.5
Impact on sales tax due to cigarette and minimum bottle changes	$ 4.0	$ 3.7
Modifications to Ambulatory Surgical Center Tax	$ (1.0)	$ (1.0)
All Tax Related Changes	**$ 205.1**	**$ 166.6**
Fresh Start Initiative	$ 60.0	$ 25.0
Eliminate Sales Tax Transfer To MRSA	$ 340.1	$ 349.0
Transfer to MRSF from the resources of the General Fund	$ (340.1)	$ (349.0)
All Other Revenue Changes	$ 55.7	$ 95.8
All General Fund Revenue Changes	**$ 320.8**	**$ 287.4**

Spending Cap

The Governor’s budget proposal includes language that would implement the Constitutional spending cap passed by state voters in 1992. Connecticut’s Constitution requires the General Assembly to define by law “increase in personal income,” “increase in inflation,” and “general budget expenditures.” These definitions must be passed by a vote of three-fifths in each house of the General Assembly. To date, no such definitions have been adopted by the required legislative supermajority vote.

In order to address the need to adopt such definitions, a bipartisan Spending Cap Commission was convened in 2016 to recommend definitions to the General Assembly. Despite an extraordinary effort from all of its members, the commission was unable to agree upon recommended definitions for the General Assembly’s consideration.

The Governor’s proposal, if enacted by the General Assembly, would honor the compact between state government and voters that has been unfulfilled since 1992. It would put in place a firm and simple spending cap which will ensure the state lives within its means. The proposal:

- Defines “increase in personal income” as the compound annual growth rate of personal income in the state over the preceding five calendar years;

- Defines "increase in inflation" as the increase in the consumer price index for all urban consumers, all items (CPI-U) less food and energy, during the preceding calendar year, calculated on a December over December basis;
- Defines "general budget expenditures" as expenditures from appropriated funds authorized by public or special act of the general assembly, with the exception of:
  - debt service, as required by the State Constitution;
  - expenditures pursuant to the budget reserve fund;
  - federal mandates and court orders in their first year;
  - payment for unfunded liabilities in the state's retirement systems; and
- Requires that a base adjustment be made in the event that any expenditures are converted from an appropriation to another non-appropriated funding source, or vice versa, to prevent gamesmanship surrounding the cap.

The definitions of "increase in personal income" and "increase in inflation" are consistent with the definitions endorsed by the Spending Cap Commission, and other components of the proposal were considered during the commission's deliberations. The Governor's proposed budget complies with the recommended constitutional expenditure cap definition and, if enacted, would contribute to the fiscal stability of the state moving forward.

Capital Proposals

Total proposed new general obligation (GO) bond authorizations are $1.792 billion in FY 2018 and $1.714 billion in FY 2019. These proposed bond authorizations are in addition to those that were previously authorized by the General Assembly and become effective during the biennium, including modified amounts of $265.2 million in FY 2018 and $225.9 million in FY 2019 for the Next Generation Connecticut/ UConn 2000 program, $150 million in FY 2018 and $95 million in FY 2019 for the CSCU 2020 program, $15.82 million in FY 2018 and $12.535 million in FY 2019 for the Bioscience Collaboration Program, and modified amounts of $15 million in FY 2018 and $15 million in FY 2019 for the Bioscience Innovation Fund. The capital budget proposal also includes the cancellation of $190.2 million in prior year GO bond authorizations that are no longer necessary.

Other notable proposed GO bond authorizations include:

- $1.2 billion over the biennium to meet the commitments of the school construction program;
- $60 million over the biennium for grants to Alliance School districts for capital improvements;
- $139.7 million over the biennium for the Connecticut State Colleges and Universities for equipment, technology improvements, and building projects;
- $181.5 million over the biennium for information technology investments and replacement of equipment to enhance state agency efficiency and effectiveness;
- $340 million over the biennium for housing related initiatives in the areas of affordable housing, the state's public housing portfolio, and under the state's successful supportive housing program;
- $125 million over the biennium for the Local Capital Improvement Program;
- $213 million over the biennium for Clean Water fund grants;
- $375 million over the biennium for the Department of Economic and Community Development to continue to provide low interest loans to attract and retain businesses and jobs in the state;
- $100 million over the biennium for the Urban Act Program;
- $40 million over the biennium for redevelopment of brownfields;

- $60 million over the biennium for the Capital Region Development Authority to assist with development in downtown Hartford; and
- $125 million over the biennium to revitalize and renew the XL Center in Hartford.

The Governor is also proposing $1.64 billion in additional special tax obligation bond authorizations over the biennium, including $120 million for Town Aid Road grants, for the Department of Transportation's program for maintaining and improving our highways and transit systems. This funding is in addition to the $1.3 billion previously approved for the biennium under the Let's Go! CT long-term transportation plan.

Finally, the Governor's capital budget includes $508.5 million over the biennium for revenue bonds to finance loans for clean water and drinking water projects.

XL Center

The more than forty year old XL Center in Hartford confronts economic and functional obsolescence and increasing economic challenges from other, newer venues and planned developments in neighboring states. In 2016, a major analysis of the facility was completed which outlined a multiyear transformation program that will allow for the facility to continue operations for the critical fall, winter and spring events which include UConn hockey and men's and women's basketball, minor league hockey and a variety of family events.

The $250 million transformation program is approximately one half the cost of a total replacement project and can be completed with limited operational disruption. Upon completion of the work, the building will have its lifespan extended and will be more competitive and economic to operate and thereby remain a major entertainment venue within the region and bolster its significant economic impact on central business district redevelopment efforts.

Over the last three years, upgrades to some of the electrical and plumbing systems as well as the building's ice making equipment and concessions has extended the building's life cycle. These improvements will be retained as part of the transformation program.

The transformation program will focus first on improvements that will better optimize the building's revenue streams (seating, food and beverage, signage) and greatly increase the efficiency of its dated, failing mechanical, electrical, plumbing, life safety and operational systems. Subsequent phases will address building improvements to meet the expectations of fans, visitors, promoters, production companies and collegiate and professional sports.

School Construction

School construction bond allocations have averaged 26 percent of state general obligation bond allocations over the last five years. Ensuring that schools are productive learning environments is important, but Connecticut has the most generous state school construction program in the country. The Governor is proposing to continue the commitment to school districts while taking a broader view of the need for projects and alternatives to expensive school construction projects at a time when enrollments are declining in a number of school districts. The proposed changes take a realistic view of school construction project components so that state officials can make meaningful recommendations for projects, while ensuring that state tax dollars are used cost effectively.

This proposal would clarify renovation requirements, provide more information to the Governor and General Assembly on a proposed school construction project (including past enrollment and capacity history for the project and the school district and projections for both, efforts to consolidate and reconfigure schools, and the project's readiness for construction), revise the priority list process so that it is submitted to the General Assembly with the Governor's proposed budget, and caps the amount of grants on the list as submitted to and authorized by the General Assembly.

Capping school construction grants on the priority list at $450 million per year, with the total approved by the General Assembly at $500 million, will result in a more strategic approach to school construction around the state. It will also encourage regionalism and the reconfiguring and closing of schools where warranted.

Having the priority list submitted as part of the Governor's proposed budget creates a closer alignment of requested bond funds – and in submitting a report on the various factors for each project, provides more information so that legislators can make informed decisions in acting upon a final school construction priority list.

Conclusion

The baseline for budget development—the consensus revenue estimate released on January 17, 2017, plus estimated expenditures for the biennium before policy changes—results in a gap of nearly $1.7 billion for FY 2018 and $1.9 billion for FY 2019. The Governor's proposed budget resolves this imbalance primarily through proposals to decrease expenditure requirements by nearly $1.4 billion in FY 2018 and $1.6 billion in FY 2019, with the remainder through revenue increases of $320.8 million in FY 2018 and $287.4 million in FY 2019. While difficult, these decisions produce a recommended budget that is balanced and under the spending cap in each year of the upcoming biennium.

Governor Malloy is proposing an all funds budget of $20,097.3 million for FY 2018, a 1.8 percent increase over both estimated FY 2017 expenditures and the adopted FY 2017 budget. The proposed all funds budget for FY 2019 is $20,545.3 million, 2.2 percent above the recommended level for FY 2018. The recommended budget is $148.6 million below the spending cap for FY 2018 and $101.3 million below the cap for FY 2019.