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STATE OF CONNECTICUT

OFFICE OF POLICY AND MANAGEMENT

TESTIMONY OF W. DAVID LEVASSEUR, UNDESECRETARY
INTERGOVERNMENTAL POLICY DIVISION
OFFICE OF POLICY AND MANAGEMENT
TO THE
PLANNING AND DEVELOPMENT COMMITTEE
MARCH 5, 2010

REGARDING RAISED BILL 337
AN ACT CONCERNING MUNICIPAL POST EMPLOYMENT BENEFIT FUNDING BONDS

Senator Coleman, Representative Sharkey, and members of the Planning and Development Committee: My name is David LeVasseur, and I am the Undersecretary of the Office of Policy and Management's Intergovernmental Policy. I want to thank you for the opportunity to present this testimony in opposition to Raised Bill 337, An Act Concerning Municipal Post Employment Benefit Funding Bonds, as it is currently proposed. This bill would enable municipalities to issue bonds related to their unfunded liabilities associated with Other Post Employment Benefits, often referred to as OPEBs.

As you may be aware, the Government Accounting Standard Board's Statements 43 and 45 became effective within the past several years. These statements require governmental entities to reflect OPEB liabilities in their financial statements in a fashion similar to how they reflect pension liabilities. In preparation for the impact of these statements on municipalities, the offices of the State Treasurer and OPM established a working group in 2006 that was chaired by then Deputy Treasurer Howard Rifkin and me. The working group was comprised of municipal finance directors, staff from the offices of the State Treasurer and State Comptroller, a bond counsel, an actuary, and an investment advisor. An important task of this work group was to look at changes needed in state statutes governing municipal borrowing and funding practices related to these OPEB liabilities.

At the time, most members of the working group believed it was premature to authorize the issuance of bonds to fund OPEB liabilities in light of the fact that most municipalities were just beginning to get a sense of the size of the liability. The work group was in full agreement, however, that if such authority were to be granted, it should be granted within the framework provided by §7-374c of the Connecticut General Statutes (CGS), which is the statute governing the issuance of Pension Obligation Bonds (POBs). In fact, the working group included model legislation in its report, which we would be pleased to share and discuss with you.

The issues surrounding the issuance of OPEB bonds are similar to those that should be analyzed when deciding whether or not to issue POBs. The relative lack of experience with OPEB bonds across the country and actuarial challenges regarding what level of health inflation to assume, make OPEB bonds potentially more challenging than POBs. As we have seen recently in so many areas of finance, complicated financial transactions are fraught with risks that need to be carefully analyzed and communicated to those who are making decisions. The statute that governs the issuance of POBs provides for this type of analysis and transparency and has, in our view, served local and state policy makers and taxpayers quite well.

The provisions in CGS §7-374c regarding the issuance of POBs, in addition to specifying requirements related to the terms of the bonds and ongoing pension contributions, provides for the State Treasurer and the OPM Secretary to review, analyze, and make recommendations with respect to the municipality's plans to issue POBs. This work must be done within the time frames outlined in the statute. It is important to note that the State's role is limited to reviewing and making recommendations about a municipality's plans, not approving whether the bonds can be issued or not. A number of municipalities have issued POBs under these provisions, and it is our belief that the joint efforts and expertise of the local and state finance officials have both increased the chance for success and mitigated the risks associated with these transactions.

In regard to other issues associated with Raised Bill 337, we have concerns that the definition of the "actuarially recommended contributions" (ARC) is the same ARC definition that helped lead to the problems that Bridgeport is now facing with its POB issuance. This definition has been changed in the POB statute based on the recommendation of the 2006 working group. Another concern is that Raised Bill 337 allows a 48 month period before making principal payments on the bonds, while the POB statute allows 18 months. This provision in Raised Bill 337 may encourage some municipalities to issue OPEB bonds as a means of achieving short-term budgetary savings that result in higher long-term costs for these bonds.

If authority to issue OPEB bonds is allowed, it should be granted using the POB statutory framework, with appropriate modifications to reflect the differences between OPEB and pension liabilities. It would also be appropriate to limit the authority to issue OPEB bonds to one or two pilot municipalities operating under the POB framework to get a better sense of how to structure these transactions and the related statutes. That would be our recommendation, if this legislation is to move forward.

While OPM would welcome the opportunity to work with the committee and other interested parties in framing OPEB bonding legislation that is consistent with Connecticut's tradition of balancing innovation and prudence in its municipal borrowing statutes, we do not believe that Raised Bill 337 strikes the right balance in this regard, especially given the high level of risks associated with these transactions.