STATE OF CONNECTICUT
OFFICE OF POLICY AND MANAGEMENT

TESTIMONY PRESENTED TO THE APPROPRIATIONS COMMITTEE
March 5, 2010

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Testimony Regarding
House Bill No. 5017, AN ACT CONCERNING THE GOVERNOR'S RESCISSION AUTHORITY,
and
House Bill No. 5019, AN ACT CONCERNING THE BUDGET RESERVE FUND
AND OTHER BILLS

Senator Harp, Representative Geragosian, Senator Debicella, Representative Miner, and distinguished members of the Appropriations Committee, thank you for the opportunity to offer testimony in support of two Governor's bills: House Bill 5017, AN ACT CONCERNING THE GOVERNOR'S RESCISSION AUTHORITY, and House Bill 5019, AN ACT CONCERNING THE BUDGET RESERVE FUND.

As you know, during difficult budget years, the law provides for the Governor to make adjustments to agency budgets to address changes in circumstances since the budget was adopted. This is commonly referred to as the Governor's "rescission" authority. Over the last two years, the Governor has utilized this power to help maintain budgetary balance—in fact, there have been seven rounds of rescissions implemented since the beginning of FY 2009, with $178.2 million rescinded in FY 2009 and $51 million rescinded in FY 2010.

Currently, the Governor may rescind up to 5% of any appropriation or 3% of any fund if there has been a change in circumstances since the adoption of the budget that is presenting a problem in keeping the budget in balance or the Comptroller projects a deficit that is 1% or greater than the amount of the General Fund. House Bill No. 5017, AN ACT CONCERNING THE GOVERNOR'S RESCISSION AUTHORITY, would add additional tiers of rescission authority to address deep budget shortfalls. Specifically, the bill would allow the Governor to rescind up to 10% of any appropriation or 6% of any fund if the Comptroller projects a deficit of more than 3% but less than 5% of the General Fund, and up to 15% of any appropriation or 10% of any fund if the state deficit is projected to be 5% or more of the General Fund. It's worth noting that the currently forecast deficit of approximately $504 million would not trigger the proposed increased level of rescission authority.

ENHANCED RESCISSION AUTHORITY

	Amount of General Fund Deficit as Projected by Comptroller	Governor's Rescission Authority	
		Per Appropriation	Per Fund
Current Law:	circumstantial	5%	3%
Proposed:	1% to 3%	5%	3%
	3% to 5%	10%	6%
	5% and above	15%	10%

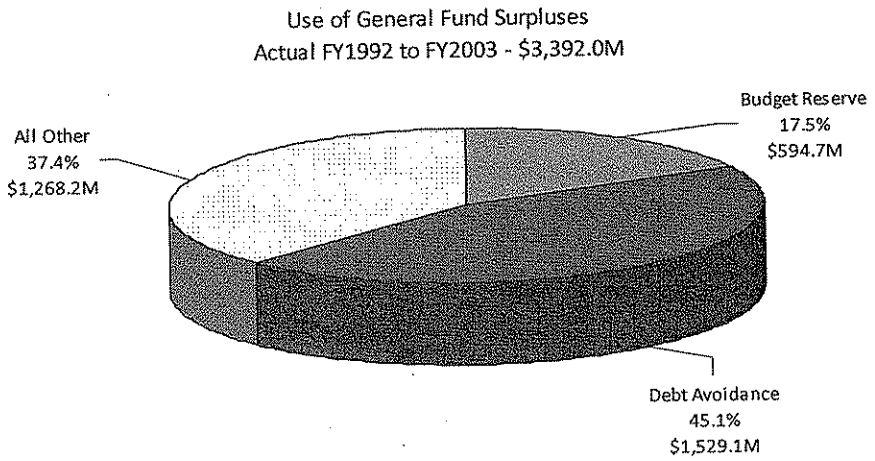
This proposal does not give a Governor unlimited power to reduce appropriations: in fact, rescission authority has a number of legal and practical constraints. First, current law prohibits the Governor from rescinding aid to municipalities, accounting for more than $2.2 billion of our state budget. Additionally, as a practical matter, the Governor is unable (in the absence of clear evidence of over-funding) to rescind funds in a significant portion of the state's budget, including debt service, pension contributions and entitlement programs. These are legal obligations that must be funded, and account for more than $6.7 billion of our state budget. The Governor is also unable, as a practical matter, to rescind funds which would result in an expenditure level less than required under the federal American Recovery and Reinvestment Act, such as certain education-related funding; expenditures related to court orders and consent decrees; and payroll expenses for state employees as a result of the job security provisions of the recent SEBAC agreement. These limitations present an even greater challenge as the size of the deficit increases.

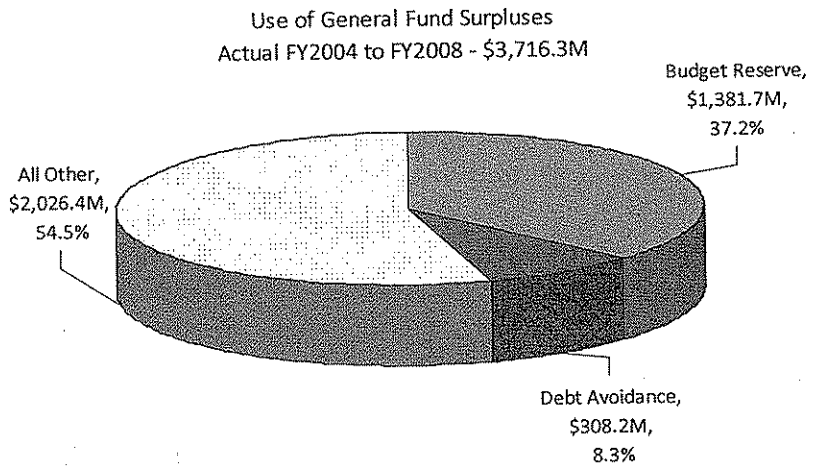
Developing a state budget is – and should remain – a balanced process involving all three branches of government. However, when the state budget is badly out of balance, the Chief Executive of our state must have the tools to help restore equilibrium. The Governor's proposed expansion of rescission authority when circumstances worsen is a modest – but necessary – change that will help address significant future budget shortfalls.

House Bill No. 5019, AN ACT CONCERNING THE BUDGET RESERVE FUND, requires that 50% of any surplus projected by the Comptroller in the cumulative monthly financial statements for January or May be immediately deposited into the Budget Reserve Fund. There are two main reasons for this proposal: First, to protect a portion of any surplus that may emerge during the fiscal year from being spent, and, second, to rebuild the state's rainy day fund.

In the past, surpluses have engendered substantial new state spending which becomes difficult to reduce and increases required annual appropriations in the

out years. These actions contribute to state budget deficits as there is no commensurate revenue stream to support ongoing programs funded out of one-time surplus. Going forward, the state needs to curb its use of surpluses to increase spending.





In addition, it is imperative that the state begin to rebuild its rainy day fund. The fund was a valuable tool in helping to bridge the downturn in revenue forecast for FY 2010 and FY 2011; the problem would have been significantly worse if the state did not have $1.4 billion in reserves. Moving to restore that fund will be evidence to the bond rating agencies of the state's renewed commitment to fiscal prudence and will position the state to better weather the next economic downturn.

The change called for in this bill will not impact any existing programs. It will decrease the likelihood of future deficits, enhance the state's ability to deal with economic downturns in the future, mitigate future program cuts and tax increases, and help to stabilize our bond rating.

You also have two other proposals before you today regarding the Budget Reserve Fund: Proposed House Bill 5105, AN ACT CONCERNING TRANSFERS OF GENERAL FUND SURPLUS TO THE BUDGET RESERVE FUND, and House Bill 5394, AN ACT INCREASING THE AMOUNT OF UNAPPROPRIATED SURPLUS DEPOSITED IN THE BUDGET RESERVE FUND. Both would increase the maximum permissible balance of the rainy day fund from the current level of 10 percent to 15 percent. Proposed House Bill 5105 goes further and, like the Governor's proposal, would require interim transfers to the Budget Reserve Fund during the fiscal year. We are supportive of both concepts, but most important is the discipline to actually ensure that any surplus funds actually reach the Budget Reserve Fund prior to being appropriated.

In addition to the Governor's legislative proposals, we would like to offer some observations regarding various other bills that are before the committee today. Several themes are apparent in these measures, including: spending cap definitions, Generally Accepted Accounting Principles, additional reporting requirements, and RBA/benchmarking.

Spending cap definitions

In 1991, as part of the compromise for enacting the income tax, the General Assembly passed a statutory expenditure cap and directed that an expenditure cap be voted upon by the public at large in the general election of 1992 as an amendment to the state's constitution. The amendment was overwhelmingly ratified by the Connecticut electorate by a 4 to 1 margin. Since the legislature has yet to adopt definitions for the constitutional expenditure cap, the Attorney General has opined that the definitions for the statutory expenditure cap remain in place and that any amendments thereto would require a three-fifths vote of each house. Proposed Senate Bill 3, AN ACT REDEFINING TERMS CONCERNING THE SPENDING CAP, and Proposed House Bill 5073, AN ACT CONCERNING THE CONSTITUTIONAL SPENDING CAP, would implement definitions for the constitutional expenditure cap. OPM is supportive of formally adopting definitions for the constitutional expenditure cap and looks forward to working with the committee to refine these proposals. The Administration would like to be included in the drafting of any final legislation to assure that the intent of the framers of the constitutional balanced budget requirement is upheld.

Generally Accepted Accounting Principles

Proposed Bill No. 5044, AN ACT CONCERNING GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, and Proposed Bill No. 5107, AN ACT MANDATING THE USE OF GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, would both amend Section 3-115b of the Connecticut General Statutes to require that the Comptroller and the Secretary of the Office of Policy and Management use Generally Accepted

Accounting Principles (GAAP) in the preparation of financial documents and the state budget. The current statutory language is permissive and allows the Comptroller and the Secretary to initiate a process for moving toward GAAP standards. However, the proposed language of these bills would require that such principles be adopted immediately.

OPM believes that GAAP-based budgeting is a sound fiscal practice. The state's weak balance sheet has been cited in the past by the credit rating agencies as an area in which Connecticut is clearly deficient. Moreover, Section 7-394a, CGS, requires towns in the state to report their finances on a GAAP basis, so the state should not use a different standard. Unfortunately, however, this bill leaves the legislature out of the requirement to adopt a budget based on GAAP principles. If this bill were adopted and the legislature was not also required to develop a budget using GAAP, budget discussions would take on an "apples versus oranges" quality.

However, while the Comptroller currently produces the Comprehensive Annual Financial Report on a GAAP basis, Connecticut's budget is based on a modified cash accounting basis: revenues are generally already on an accrual basis of accounting, whereas expenditures remain on a cash basis of accounting. Moving immediately to GAAP-based accounting would require recognition of the current GAAP shortfall, which is more than $1.1 billion. The bill is silent as to how this accumulated GAAP deficit would be amortized, which is problematic given the reality of attempting to bring the FY 2011 budget into balance.

If the issues of the legislative adoption of the budget and the amortization of the current shortfall were appropriately addressed, the Administration would be supportive of this legislation.

A complementary measure is House Bill 5393, AN ACT CONCERNING THE ESTABLISHMENT OF AN ACCOUNT TO FUND THE TWENTY-SEVENTH STATE PAYROLL PERIOD. This bill would fund the 27th payroll which occurs every 11 years by requiring the General Assembly, beginning in FY 2013, to appropriate each year one-tenth of the amount projected to be required. The Comptroller proposed the establishment of this fund during the 2009 legislative session and this bill incorporates many of the language changes suggested by OPM. OPM is supportive of this bill as it would move the State closer to GAAP accounting principles. However, it also would require the discipline to actually set aside the required resources each year. Unfortunately, the state's history is not good on this latter point.

Additional reporting requirements

Several bills would layer new reporting requirements on top of existing requirements. Senate Bill 356, AN ACT CONCERNING MONTHLY REPORTS ON PERSONNEL STATUS FOR STATE AGENCIES, is unnecessary. The substance of this bill would be to require new data to be created and provided by OPM to OFA

regarding positions, specifically requiring OPM to provide a "copy of monthly position data, which shall include for each state agency the positions vacated and the positions filled during such month". This is not something OPM creates or maintains now and represents a new task for which we would have to allocate resources. It should be noted that the intent of this bill can be fulfilled through standard CORE-CT reports in conjunction with data warehouse queries. These queries and reports are available to OFA staff and can be run for individual agencies using any effective date desired. OPM does not currently produce a report contemplated by this bill, and would not be able to provide the specified information for CORE-CT limited-scope agencies, such as higher education, the Judicial Branch, and Legislative Management.

Senate Bill 359, AN ACT CONCERNING REPORTING BY STATE AGENCIES, is unnecessary. Perhaps the committee is unaware, but currently, every expenditure, contract, project, employee and position carries a CORE-CT program coding designation - the system does not allow a null or "all programs" value. If the intent of the bill is to prescribe standards for "limited scope" agencies, then it falls a bit short of the mark. Additionally, OPM already provides "an electronic version of all data generated by the CORE-CT system that is used to prepare the budget document" to OFA, with such data being revised as necessary as we go through the recommendation process. Again, to the extent that this is requiring new data, sorted and maintained in a manner that is not currently provided for, then additional resources would have to be allocated to carry out this task. The data used by OPM is already available to OFA, so it is unclear what problem this legislation is attempting to address.

It should be noted that the Judicial Branch and the constituent units of higher education generally do not have data of this sort on the CORE-CT system; rather they maintain independent data systems not accessible outside those agencies. This requires a researcher to make inquiry of those agencies for the desired information. Any attempt by the legislative staff or the executive staff to obtain this kind of information for those agencies would not, therefore, be facilitated by this bill.

RBA/benchmarking

With respect to Senate Bill 358, AN ACT CONCERNING RESULTS-BASED ACCOUNTABILITY, we think it is unnecessary to have a statutory requirement that each agency head designate an employee as the RBA liaison. Most agencies have staff who act as liaisons with the legislature. Further, the Appropriations Committee and the Office of Fiscal Analysis should be well aware of the relevant agency staff and should know who can answer programmatic as well as financial questions. We are not aware of any situations where the legislature was unable to determine how to contact an agency regarding either a programmatic or fiscal question.

We have concerns about House Bill 5395, AN ACT CONCERNING BENCHMARKS FOR STATE-FUNDED PROGRAMS AND SERVICES. First, let me say that we support the idea of program benchmarks. Any review of a given public policy should start with consideration of the relative worth of the program in a world of limited resources. Given the state's financial crisis, we think the spirit of this legislation—that ineffective programs should be terminated—is laudable. But some practical problems arise in the administration of the scheme envisioned by this language. As you know, public budgeting is a process of reconciling competing demands for extremely limited resources. The final budget that is enacted is often the product of compromise, and often certain spending initiatives are added or modified in order to effect the passage of the overall budget. So in that context, how should "effectiveness" be defined, and who should define it? Without defining the term "effectiveness" it is unclear what standard should be applied. For example, in human services there are a growing number of, but still relatively few, interventions that rise to the standard of being called "evidence based," and the means required to achieve such a statistical standard of effectiveness is well beyond the reach of existing state resources. Is it the committee's intention that the vast majority of programs funded through the human services agencies be cancelled in two years because we cannot conclusively prove the effectiveness of those programs?

Further, the bill does not define "programs and services." Is the Executive Branch to determine the "effectiveness" of each of the thousands of medical procedures covered under the Medicaid program? What if the program is effective, but of a low priority compared to other needs—does that mean we should continue to fund the program? What is a reasonable timeframe within which to gauge the effectiveness of a program—is two years adequate? What if a program is funded but the support apparatus for that program—enabling legislation, agency staff, or necessary operating expenses, for example—is insufficient, delayed, or nonexistent? OPM supports the elimination of programs and services that are ineffective, however we believe that such a blanket approach to categorizing all state services is impractical. From a fiscal standpoint, implementation of this bill would require the addition of staff as well as expanded and enhanced information systems, which we can ill afford at this time.

The good news is that most of what this bill seems to be trying to accomplish actually gets done - perhaps not always in as exacting or specific a process as this bill contemplates - through the budget review process that happens at every state agency, at OPM and in the development of the Governor's annual budget proposals. It also inherent in the appropriations process in the legislature. Furthermore, review of programs' effectiveness is often undertaken as part of the regular work of the staff of the legislative Program Review and Investigations Committee, the Auditors of Public Accounts and the research and oversight work done by the legislative Office of Fiscal Analysis and Office of Legislative Research.

Other measures

Proposed House Bill 5070, AN ACT CONCERNING THE DEBT SERVICE LINE ITEM IN THE STATE BUDGET, requires that the current one-line debt service appropriation instead be appropriated according to the agency and purpose for which the debt service payments are being made. The concept behind the bill is clearly well-intended, but implementation may be impractical for a number of reasons. First, there are over 50 agencies that have received bond funds, so the budget would need to reflect, at a minimum, 50 line items assuming each agency had just one project or purpose. Second, this bill would eliminate the state's flexibility in paying the debt service on variable rate bonds. If rates increase for one particular bond issue, numerous transfers would need to be approved by the Finance Advisory Committee in order to cover the increased costs in a variety of small line items. Third, projected bond issues for the upcoming year could not be appropriated as envisioned by the bill because final projects/purposes will not have been determined at the time the budget is adopted. Fourth, tracking debt service costs per year, per bond issue, and per project/agency would be exceedingly difficult and could require substantial additional resources both for the Office of the Treasurer as well as for OPM. As an alternative, we are confident that if a question about a specific project arises, the Treasurer's Office would be able to provide detailed information in response. OPM is happy to work with the committee or the sponsor of this bill to identify the true cost of individual bond projects so that the Legislature and the public can be better informed, at the outset, as to what will ultimately be required to pay for projects paid for by state bond proceeds.

Proposed House Bill 5106, AN ACT CONCERNING A COMMISSION ON STATE EMPLOYEE PENSION AND POST EMPLOYMENT BENEFIT LIABILITIES, calls for the establishment of a Commission to propose, before December 15, 2010, a long-term plan for reducing unfunded liabilities in the state employees' retirement system and state employee post-retirement health and life insurance benefits. This bill is duplicative of the Governor's Executive Order No. 38 issued on February 3, 2010 which established a State Post-Employment Benefits Commission. This Commission will, before July 1, 2010, deliver a report to the Governor that:

1. Identifies the amount and extent of unfunded liabilities for pensions and other post-employment benefits;
2. Compares and evaluates the advantage and disadvantages of various approaches for addressing unfunded liabilities and post-employment benefits; and
3. Proposes a short and long term plan or plans for addressing unfunded pension liabilities and post employment benefits.

In our view, the approach taken through the Executive Order is superior to the proposal under HB 5106 because of the breadth of expertise and opinion represented on the State Post-Employment Benefits Commission, namely certified public accountants, certified actuaries and the business community.

Proposed H.B. No. 5163, AN ACT REQUIRING THE ESTABLISHMENT OF A SEARCHABLE DATABASE FOR STATE EXPENDITURES, has a laudable goal: increased transparency and accountability. Unfortunately, implementation of this bill would likely entail some cost, so we cannot support it at this time. Further, this bill is not specific as to the level of detail as well as the owner/maintainer of the database. Should this bill move forward, I would suggest the Comptroller's office, as the party responsible for the state's accounting system, as the appropriate entity to fulfill the bill's intent.

We are not opposed to Senate Bill 354, AN ACT CONCERNING BIOMEDICAL RESEARCH TRUST FUND RESEARCH GRANTS, which would expand the research fields that may receive grants in aid to include Alzheimer's disease and diabetes. Currently, grants in aid from the Biomedical Research Trust Fund support research in the fields of heart disease, cancer, and tobacco-related diseases. However, expanding the scope of research fields eligible to receive these research grants would mean that research funds could be spread among more fields of study, potentially resulting in reduced grants for any particular research effort.

We are not opposed to Senate Bill 355, AN ACT CONCERNING CAPITAL IMPROVEMENTS REQUIRED BY THE DEPARTMENT OF DEVELOPMENTAL SERVICES. This bill allows the Department of Social Services, on a limited basis, to adjust a private facility's rates for capital improvements if they are required by the Commissioner of the Department of Developmental Services for the health and safety of the residents and are made during fiscal years ending June 30, 2010 and June 30, 2011. Based on current trends, it is anticipated that funding could be available on a limited basis for these improvements in the Governor's FY 2011 budget.

We have concerns about Senate Bill 357, AN ACT CONCERNING REDUCTIONS TO STATE CONTRACTS, since reductions have programmatic impacts, and potentially state or federal statutory and/or regulatory impacts, and should not be unilaterally decided upon by the vendor. The state agency shares responsibility for how services are provided and for program outcomes. Currently, state agencies contract for specific services towards specific outcomes and will need to determine what impact funding reductions have on each program and each contract, then work with the contractor to implement the reduction. Reductions may impact service delivery and the state agency has the obligation and should retain the power to determine what services it will continue to receive under the contract. It is appropriate and necessary that the state work with the contractor on these issues. OPM would be happy to work with the committee on refining this proposal toward those ends.

Senate Bill 360, AN ACT CONCERNING FLEXIBLE SPENDING ACCOUNTS, would allow the Comptroller to transfer funds from the Social Security account for anticipated savings due to employee participation in flexible spending account programs established in CGS 5-264b through 5-264e, inclusive. These are accounts for dependent care spending and for flexible health care spending. It is troubling that there would be no restriction on how much the Comptroller can withdraw from the social security account and there would be no requirement to consider the health of the social security account. There may be inadequate funds in a given year to meet the requirements of the state for social security and even in that year the Comptroller would be allowed to transfer from the fund. It is generally inadvisable to transfer money from one account to pay for administrative fees for another program without limitation and without any regard to the actual state of that account. If money for administrative costs is needed, the determination of the amount needed to cover administrative costs should be subject to gubernatorial and legislative review and the standard appropriation process. For these reasons, we oppose this bill and respectfully request that the Committee take no action on it.

I would like to again thank the committee for the opportunity to present this testimony. I respectfully request the committee to act favorably on House Bill 5017 and House Bill 5019, and I am happy to answer any questions you may have.