YANKEE INSTITUTE
for Public Policy

Testimony Submitted By Carol Platt Liebau, President of the Yankee Institute for Public Policy, to the Finance Committee on SB 1135.

April 23, 2015

Chairman Fonfara, Chairman Berger, Ranking Member Frantz, and Ranking Member Davis: Thank you for inviting the Yankee Institute for Public Policy to testify on Senate Bill 1135. We appreciate the committee chairs bringing this bill forward, and I'd also like to thank Comptroller Lembo for raising this issue and for working so hard to make it a legislative priority.

My name is Carol Platt Liebau. I am the president of the Yankee Institute, a Connecticut think tank that develops and advances policy solutions to promote smart, limited government; fairness for taxpayers; and an open road to opportunity for all the people of our state.

We are well aware that this is a tough year for lawmakers as you work to get our budget in balance. But as tough as this year is, of course four years ago the situation was even more dire, as Connecticut's people confronted one of the worst recessions in recent memory. Because we were not adequately prepared for an economic downturn of this magnitude, lawmakers decided that they had to raise taxes to close the budget gap.

I'm sure it comes as no surprise to hear that the Yankee Institute did not support these tax increases. We were concerned about their lasting fiscal impact on our state.

Unfortunately, our fears turned out to be justified. Since those tax hikes were enacted, Connecticut has struggled to regain its footing. Although job growth has accelerated slightly, we still lag behind national job growth rates, and we have not yet recovered all of the jobs we lost in the 2008 recession.

In light of these facts, it is particularly important that -- as we start to see some signs of job and revenue growth -- we make wise decisions. Now is the time to set ourselves on the fiscally prudent path, saving for the next "rainy day" instead of finding new ways to spend windfall revenues.

A Yankee Institute study released earlier this year is instructive. It shows that if lawmakers had saved windfall revenues from 1992 to 2012 and kept state spending within the constitutional spending cap, Connecticut would have an additional $5.2 billion in its rainy day fund. As important as the savings mechanisms in this bill are, it is even more critical to restrain the growth of spending if we are ever going to get back on a path to fiscal sustainability.

As you know, our tax system relies heavily on our richest citizens. This structure produces years where state revenues can suddenly exceed projections significantly, or, conversely, can unexpectedly drop below our projected figures. As an aside, we hope that this committee will work with the Tax Review Committee to develop a more stable, less volatile tax structure.

But even within the constraints of the current tax system, the Yankee Institute believes that the plan laid out in this bill is one that can help set the state on a more sustainable trajectory.

In particular, there is a component of this plan that is particularly important to Connecticut's long-term fiscal well-being.

One way this bill would improve the current system is by placing a greater emphasis on paying down Connecticut's long-term pension liabilities, even as it also builds a Budget Reserve Fund.

Under the bill as written, when the Budget Reserve Fund achieves a certain level of funding – 10 percent of current year General Fund expenditures – a portion of excess revenues would then be allocated to pay down the state's pension liabilities.

This provision is crucial. Connecticut's pension debt is hurting our state. When credit rating agency Standard & Poor's recently revised its outlook on Connecticut's debt --from stable to negative, -- the agency cited the budgetary pressure imposed by the cost of public pensions as a factor in its decision.

Notwithstanding any changes made in 2011 -- and despite the state's efforts to catch up on missed payments -- the state's pension debt continues to grow. The most current valuation of the State Employee Retirement Fund shows that it is now only 41 percent funded. In 2010, it was 44 percent funded.

This year, the governor's budget allocates more than $2 billion from the General Fund to the state employee and teachers' retirement funds. Even that isn't enough to keep the debt from growing. Last year, a J.P. Morgan report found that for Connecticut to fund its pension debt and other debt obligations fully, current payments would have to double.

As I conclude, it's worth pointing out that all our state's fiscal challenges are, to a large degree, intertwined. Of course, the first and most urgent problem is Connecticut's current fiscal situation. And this committee can address this problem most effectively by standing firmly against any further tax increases on our state's already-struggling residents and businesses. That will at least prevent any further slowing of our already-sluggish economic growth.

And this bill, in a sense, relies on economic growth. After all, it's the only way to re-energize our state's economy, and increase tax revenues without punishing residents.

When tax revenues do ultimately increase, that will present our second challenge – the long-term volatility of state revenues. The bill before you would go a long way in preventing lawmakers from spending one-time revenue windfalls. It establishes a sensible plan to build a more robust Budget Reserve Fund. In sum, this bill is worthy of your consideration, and the Yankee Institute urges passage of this legislation.

But as much as I hate to conclude on a gloomy note, honesty compels me to point out: Even if revenues should increase and this bill would go into effect, we will still confront a daunting third challenge: Our state pension debt. Of course this bill is a welcome potential effort to shore up our failing pension system, but it is only a very small drop in an increasingly large bucket.

We would welcome the opportunity to discuss ways to reform pension debt in further detail at another time.

For now, I want to thank the committee again for inviting the Yankee Institute to participate in a conversation about Connecticut's long-term fiscal health. Please let us know if we can provide any additional information or insight. We salute your efforts, and we are at your service.