A Citizen's Guide to the CT State Budget

CT Voices for Children

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Overview

What is the Connecticut State Budget, and why should we care about it?

The *Connecticut State Budget* is a daunting document – more than 700 pages of charts, graphs, text, lots and lots of numbers, and some very small print. It is also, however, one of the state's most fundamental policy documents for it defines what programs and services will receive financial support from the state, and describes how the responsibility of funding these programs and services is to be shared among Connecticut taxpayers. (*Connecticut State Budget 2001-2003*, prepared by the Office of Fiscal Analysis, can be found at www.cga.state.ct.us/ofa.)

In the current state fiscal year (which runs from July 1, 2001 through June 30, 2002) our state government plans to collect about $13 billion in taxes and other revenues and spend this money on everything from running our courts and protecting children from abuse to operating our public colleges and providing health care to our poorest children. Our state government also will borrow money for capital projects like school construction, highway maintenance, open space purchases, and grants and loans to businesses to support economic development. Under our state constitution, the members of the CT General Assembly and the Governor have important responsibilities in this budget process – both in deciding how to raise revenue and then where to spend it. Their decisions define the priorities of our state.

However, as citizens and as taxpayers, we also have a responsibility -- to make sure our leaders' priorities reflect our values and that their budget decisions meet our needs. Very often, significant budget changes are made with little media attention or public input. By understanding and monitoring the budget process, and making our voices heard, we can hold our leaders accountable. We can ensure that our state implements the programs we value and spreads the burden of financing them fairly.

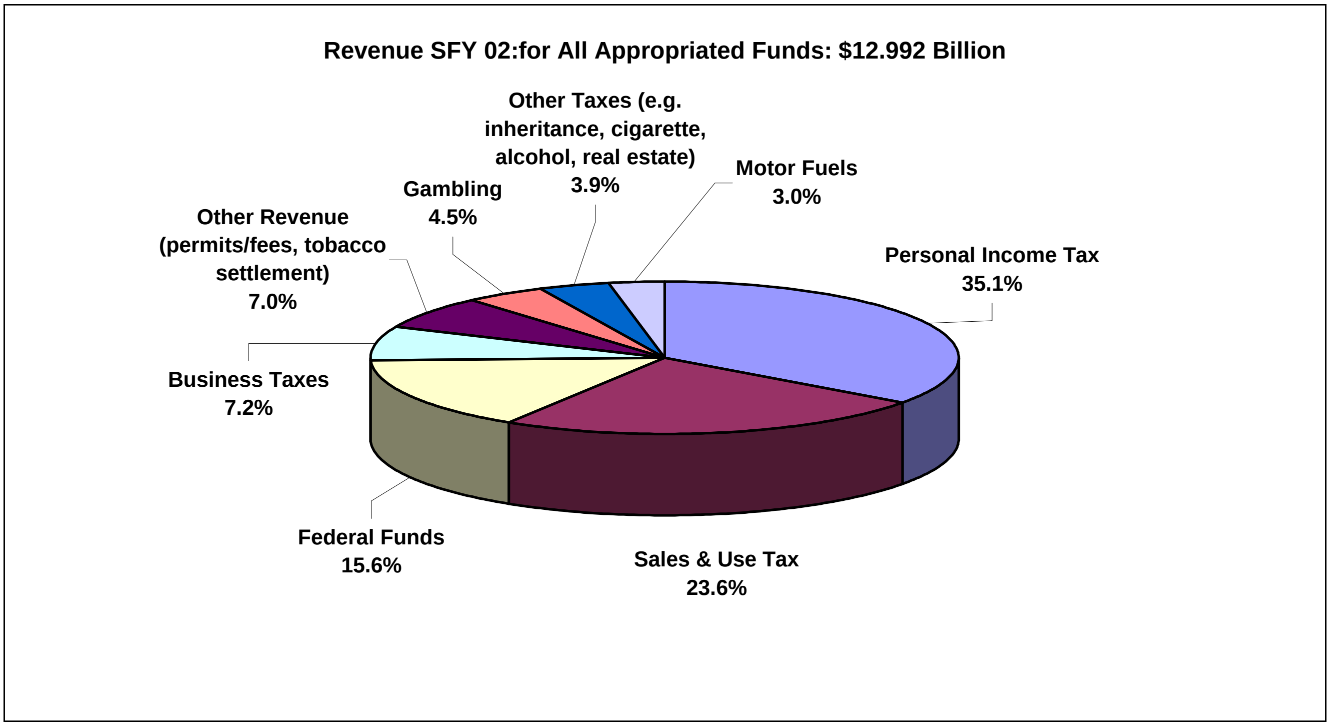
Though the *Connecticut State Budget* is a formidable document, the thinking that must go into it is – in many ways – like the thinking each of us must do to manage our own family's budget. Like a family, the state cannot spend more for its on-going expenses than it has in income – the budget needs to be balanced. Like a family, the state can borrow money (through bonding), but if it puts too many expenses on the state "credit card" it has the same consequences as when a family accumulates too much debt on its credit cards or has too high a mortgage. Each month, more of its income goes to pay off debt, leaving less for all other expenses. Also -- like a family -- when the state's funds get tight, tough choices must be made – whether (and how) to cut spending, how best to increase income, whether to borrow money and collect on debts, whether to tap into savings, or some combination of all of these.

This brief guide is intended to provide a roadmap to understanding the components of the state budget, how it is created, some of the priorities and choices it reflects, and how you – a citizen and taxpayer – can stay informed and make your voice heard as budget priorities are being decided.

Revenue

Where does the state get its money?

Currently, about 73% of the state's revenues come from a variety of taxes (e.g. the personal income tax, sales and use tax, and various business taxes), about 16% from the federal government, 5% from gambling revenues, and 7% from other sources (such as permit and license fees and the tobacco litigation settlement). The state's single largest source of revenue is the Personal Income Tax. Second is the Sales and Use tax that both businesses and individuals pay when they buy many goods or services. During State Fiscal Year 2002 (July 1, 2001 through June 30, 2002)[SFY 02], the state plans to take in a total of nearly $13 billion in revenue from these sources in these proportions:



As noted below, some of the state's taxes are imposed on individuals, others on businesses, and a few on both. Here is a little more information about each of the state's primary revenue sources, in order of their contribution to total state revenues in SFY 02:

Personal Income Tax (34% of revenues) is imposed on the earnings, dividends, interest, capital gains, and other income of individuals. The income that is taxable in CT is defined generally as a person's adjusted gross income for federal income tax purposes (i.e., the amount reported on line 33 of the IRS' Federal Income Tax 1040 form). Though the state adopted a capital gains tax in 1969, a dividends tax in 1972, and a tax on interest in 1984, it repealed these taxes in 1992, adopting – instead – this current personal income tax.

Revenue from this tax increased from about $520 million in 1991(from the tax on capital gains, interest, and dividend income) to more than $4.2 billion in 2000. CT taxes the income of any person who lives in CT, and also some people who only work in the state or who only live here for part of the year. The tax is 3% on all CT taxable income up to a certain threshold, and 4.5% on income above the threshold (the threshold varying by taxpayer filing status). CT's 4.5% "top bracket" rate is 5th *lowest* among states with an income tax, though CT continues to rank first among all states in per capita income (at $40,640, 37% above the national average). By comparison, New York's top bracket rate is 6.85%, while the top bracket rates in New Jersey and Massachusetts are 6.37% and 5.3%, respectively (with, in Massachusetts, a 12% rate on certain capital gains income).

This tax is CT's most progressive tax. That is, its burdens fall more on the state's wealthier residents than on its poorer residents. In the 1999 income year, CT residents who reported an adjusted gross income of $200,000/year *or more* were only 4% of all resident taxpayers, but paid 47% of the total state personal income tax paid by residents. By contrast, 17% of our poorer residents who filed state income tax returns in 1999 paid *no* state income tax at all. For some, this was because their income fell below the threshold at which state income tax is imposed. For others, who owed some income tax, it was because the credit against the state income tax for property taxes paid was more than the amount of tax due. Indeed, the increase in the credit a taxpayer can claim for property taxes paid (from a maximum of $100 in 1997 to $500 in 2000) has more than doubled the proportion of resident taxpayers with no state income tax due (only 7% had no state income tax liability in 1996).

Sales and Use Tax (24% of revenues), first adopted in CT in 1947, applies to both individuals and businesses. As a general rule, all sales/leases of *goods* to consumers and businesses are taxable unless they are specifically exempted from the tax, while sales of *services* are taxed only if they are specifically identified as being subject to the tax. The tax rate is 6%, with certain exceptions. If the seller of a taxable good or service does not charge the buyer the sales tax, the buyer is responsible for paying the tax.

Sales taxes are considered *regressive* taxes. That is, people who are poorer pay a greater share of their income in sales tax than those who are wealthier. Also, Connecticut's sales tax "base" is relatively narrow. That is, rather than imposing the tax on *all* sales of goods and services (which provides a more stable revenue source, is easier administratively, and could generate the same amount of revenue, but with a tax rate less than 6%), CT has well more than 150 exemptions from the sales tax for all manner of things -- from sales of food and of clothing that costs less than $75 per item, to sales of gold and silver bullion, massage therapy services, high-speed data transmission equipment, and direct mail advertising services.

Federal Funds (16% of revenues) come to CT in several ways, and for multiple purposes. CT receives substantial federal funds as *partial reimbursement* for certain services the state funds, such as health insurance to low-income children and families through Medicaid/HUSKY and foster care services to children who are abused and neglected. For example, in SFY 02 CT will spend nearly $2.2 billion on Medicaid services. The federal government will reimburse CT 50% of this sum; these federal funds will be deposited in the state's General Fund as revenue. CT can claim reimbursement in these programs only if the programs comply with the very detailed federal statutes and regulations that establish them. CT also receives federal *grant* funds for specific purposes. For example, CT will receive about $225,000 from the federal government to study the impact on children of the state's welfare reform program. The use of such funds is limited to this purpose.

In addition to these federal revenues that help pay for certain specific budgeted expenditures, CT receives a number of block grants from the federal government, such as the Social Services Block Grant (SSBG) and the Temporary Assistance for Needy Families Block Grant (TANF). States have significant discretion in the use of federal block grant funds; allocation decisions are made within rather broad guidelines established by the federal government that define target populations and uses of funds. In CT, the specific uses of block grant funds are established through a state agency allocation plan that is submitted for approval by the legislative committee(s) with oversight of that agency. Approval of the full legislature is *not* required.

For example, federal law specifies that CT's $20.8 million SSBG grant in FFY 01 could only be used to provide social services to low-income "vulnerable persons or families with special emphasis on those groups which are less able than others to care for themselves (e.g. special needs children, youth, and elderly)." The CT Department of Social Services, administrator of the SSBG block grant, chose to use these funds to pay for a wide variety of services for low-income individuals, including child day care, family planning, legal and substance abuse services.

Importantly, in FFY 00[1], CT received only about $0.63 in federal spending for every dollar paid in federal taxes, the lowest return among all states (and down from $0.78 received for every dollar paid in 1990). Though this is due in part to CT's wealth (we pay more in federal income taxes per capita, and CT's federal reimbursement rate is lower than the rate in poorer states), it is also due in part to CT's failure to claim all the federal funds to which it is entitled. Moreover, between SFY 01 and SFY 02, federal funds to the state are projected to fall by more than $133 million. This will transfer more of the burden of funding certain programs to the state.

Business Taxes in SFY 02 will provide 7.2% of revenues, compared to 13.3% of all appropriated state revenues in 1996. This decline in revenue share from all forms of tax on business is due to rate reductions, new tax credits, exclusions, deductions, and exemptions ("tax expenditures") and the repeal of some taxes altogether.

The corporate business tax, one of the state's business taxes, was adopted in 1915. It taxes the income of corporations and other entities that conduct business in the state. Its tax rate has been markedly reduced over the 1990s -- from 11.5% (in 1984-1994) to 7.5% (in 2001). There also are increasing numbers of exemptions, deductions and credits that corporations can claim to reduce their tax liability; for some CT companies these have cut the amount of corporate business taxes owed to CT to virtually nothing. As a result of these rate and base changes, corporate business taxes will contribute only 3.6% of total state revenues in 2002, compared to 6.7% in 1996.

Other business taxes include those imposed on public service, insurance, and petroleum companies and – until it was repealed this year -- on hospitals' gross receipts. Over the late 1990s, these taxes too have been markedly reduced.

Other Revenues account for the remaining 19% of state revenues and come from a variety of sources: gambling (4.5%, of which 2.6% come from Indian Gaming Payments); the tax on gasoline and diesel fuel (3.0%); the inheritance tax (1.5%); funds from the tobacco litigation settlement (0.9%); the cigarette tax and the real estate conveyance tax (0.8% each); the alcohol beverage tax (0.3%) and a variety of other taxes and fees (such as the gift tax, license fees, fines, permit fees).

Over the 1990s, the financial burden of supporting state government and state-funded services has shifted increasingly away from CT businesses and onto CT's individual taxpayers. Moreover, increasing numbers of tax exemptions, exclusions and credits have eroded the base of the sales and use tax, and the business taxes, as described below.

What are "tax expenditures" and why do they matter?

The legislature has the power to make various sorts of exceptions to each of the taxes listed above, and over the years, a very long list of exceptions has accumulated. These tax exemptions, deductions, rate

[1] FFY stands for Federal Fiscal Year, which runs from October 1 through September 30. SFY stands for State Fiscal Year, which runs from July 1 through June 30.

reductions, and credits collectively are called ”tax expenditures” for they provide preferential financial benefits to a group of taxpayers through the tax code. In essence, rather than taking in money through taxes and then spending it on an individual or business through a direct appropriation of state funds, they simply “spend” money by not collecting taxes that would otherwise be due from an individual or business. Though we discuss tax expenditures in this part of the *Guide* because they are part of the revenue “side” of the budget, they should be viewed as state spending as well.

A tax **exemption** means that particular goods or services, or particular individuals, companies or entities, are not subject to that specific tax. For example (as noted above) CT exempts sales of more than 150 goods and services from the sales tax. Tax **reductions** mean that a particular individual or business pays a lesser rate of tax. Tax **credits** offset – dollar for dollar – any tax due to the state. That is, when a business or individual is given a tax credit, the value of the credit is actually subtracted from the total amount of taxes owed.

Like direct government spending on programs and services, tax expenditures can serve various important policy purposes. Some tax expenditures seek to make the tax code fairer, while others are designed to encourage a particular kind of behavior on the part of a corporation or individual. For example, one tax credit is available to corporations that use clean alternative fuels, to encourage such use. Some tax expenditures are enacted to spur economic growth. Corporate tax credits to help offset the costs of research and development fall into this category; they are designed to encourage innovation that will spur economic growth. Indeed, some of these credits are now *refundable*; if the value of the credit is greater than the tax the company owes CT, CT writes a check to the company for the difference.

Some tax expenditures benefit a very limited number of taxpayers. For example, the exclusion of domestic insurance companies from the corporation business tax benefits just 10 corporations, and results in a revenue loss of $20 million/year. Only one corporation claims the credit for “Research and Development Expenses at Aerospace Companies,” saving that company $60 million in taxes each year.

Tax expenditures are an overlooked form of spending. They do not need to be re-enacted every year and unless a “sunset” date is placed on a tax expenditure provision, it continues indefinitely (or until amended or repealed). By contrast, the state’s direct expenditure of funds on salaries, programs, services, buildings and other purposes must be *re*-appropriated in each budget period and are adopted only after detailed review, public hearings, and lengthy debate and negotiations.

Importantly, CT’s tax expenditures erode its revenue base. In SFY 02, the projected loss in revenue from CT’s tax exemptions, deductions, and credits is more than $3.7 *billion*, or almost 29% of the year’s *total* revenues of $13 billion. The *General Fund* revenues CT will lose in SFY 02 because of exemptions, deductions and credits – as well as *rate reductions* -- adopted since 1991 against various taxes that CT *businesses* pay will total nearly $1.29 *billion*. Indeed, if CT were to close all the loopholes in the sales tax that now benefit businesses and individual taxpayers, sales tax revenues would increase from $3.25 billion to $4.65 billion in SFY 02.

Despite declining revenues from an economy in recession and a growing budget deficit, CT continues to cut its revenues through new tax expenditures. In SFY 02, CT is phasing in additional tax expenditures that will reduce our revenues by $291 million (compared to revenues in SFY 01). More tax cuts are scheduled to be phased in through SFY 06, and will *continue* to reduce our revenues – *despite projected budget deficits* – unless the General Assembly acts affirmatively to delay or repeal them.

As a citizen and taxpayer, it is important to monitor the new tax breaks proposed and adopted each year—they can encourage responsible corporate behaviors of various sorts, provide tax relief to overburdened working people, or simply generate vast windfalls for particular corporations. To help, every two years, the General Assembly's Office of Fiscal Analysis (OFA) produces a *Tax Expenditure Report* for the biennium, which reports the various exemptions, reductions, and credits for all taxes, the revenues we are losing from each of them, and the reasons they exist. In some cases, the OFA reports that tax expenditures are the result of political "expediency" – that is, "expenditures of this type violate one or more of the principles of a high-quality revenue system without any apparent counterbalancing or compensating precept." Repeal of such provisions would add needed revenues to state coffers. A new requirement for periodic review and re-adoption of *all* tax expenditures would assure that they continue to serve important state interests as times change.

What is bonding and why does it matter?

Like many CT families, CT pays for some of its expenses with its "credit card." The state borrows money to pay for capital projects like school and prison construction, just as a CT family might get a mortgage to buy a home or a loan to buy a car. CT also borrows money to pay for certain financial assistance programs that provide funds to municipal, business, and non-governmental entities through grants and/or loans. CT also extends the state's credit backing to bonds issued by certain quasi-public bond-issuing authorities; CT becomes responsible for *this* indebtedness if the issuing party fails to make payments.

CT borrows money by issuing bonds, which investors buy. The State Treasurer sells bonds several times a year, based on the cash requirements for bond-funded projects. The state then pays off this indebtedness over time. By using bond debt, CT is able to spread out the costs of major projects that will last for many years and that will provide long-term benefit to the state, rather than having to fund the projects with cash in a single fiscal year. However, as is true with loans that a family takes out to cover major purchases,[2] the total cost of a project paid for with borrowed money is greater than one paid for in cash -- since one must pay back not only the funds borrowed, but also interest.

In part because of the constraints of the state spending cap (see below), CT has used borrowed money not only for large capital projects, but also to pay for some of its current operating expenses—a recent trend that makes the budget appear more sound than it actually is, and in fact passes current costs on to future generations. In recent years, for example, CT has used bond funds to pay for 24-speed bicycles, grave markers, nitrogen infiltration studies, and some of the costs in running the state Department of Public Works (DPW). According to the State Comptroller, of the $1.126 billion in new debt CT issued in SFY 00, $489 million (43%) was for infrastructure or other assets benefiting future generations of taxpayers, while the remaining $637 million (57%) was used to fund on-going state operating expenses.

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[2] If, for example, an individual borrows $1,000 for one year at 5% interest to make a major purchase, and repays the loan in one payment at the end of a year, the individual needs to pay back not only the $1,000 but also $50 in interest for having borrowed this sum for a year (or some other amount, depending on the calculation method used). Thus, the total "cost" of the purchase ends up being $1,050 rather than $1,000 (the cost if the person had simply paid cash). If the interest rate is higher (or if the money is borrowed for a longer period of time), the total cost of the purchase made with borrowed funds will be even greater.

CT's propensity to turn to its "credit card" to pay for state expenses, *even in* the late 1990s when the state enjoyed very large General Fund budget surpluses, has resulted in CT leading the nation in net tax-supported debt per capita, with $3,037 of debt per state resident in 2001. (By comparison, per capita debt in Massachusetts in 2001 was $2,957, in New York $2,020, and in New Jersey $1,935). Indeed, CT's bonded debt per person has *more than doubled* over the past decade and, at this point, CT is adding about $1.2 billion in debt each year, while retiring only about $700 million. This increasing indebtedness provides two particular challenges to state budgeting:

- Large amounts of debt require high annual debt service (principal and interest) payments. In SFY 89, just before CT entered the *last* recession, 6.2% of CT's total appropriated funds were spent on debt service ($385 million). In SFY 02, 11% of CT's total appropriated funds will be spent paying off debt ($1.44 *billion*).

- Debt service is a fixed cost that cannot be quickly adjusted when state revenue growth slows and budget deficits are projected. In tough financial times a high debt load can cripple a state's capacity to respond effectively to fiscal challenges. Interestingly, if CT had kept its debt service payments to only 6.2% of all appropriated funds (as it was in SFY 89), this year's debt service payments would be $627 million *less* – and this money could be used to balance the SFY 02 state budget and meet other critical state needs.

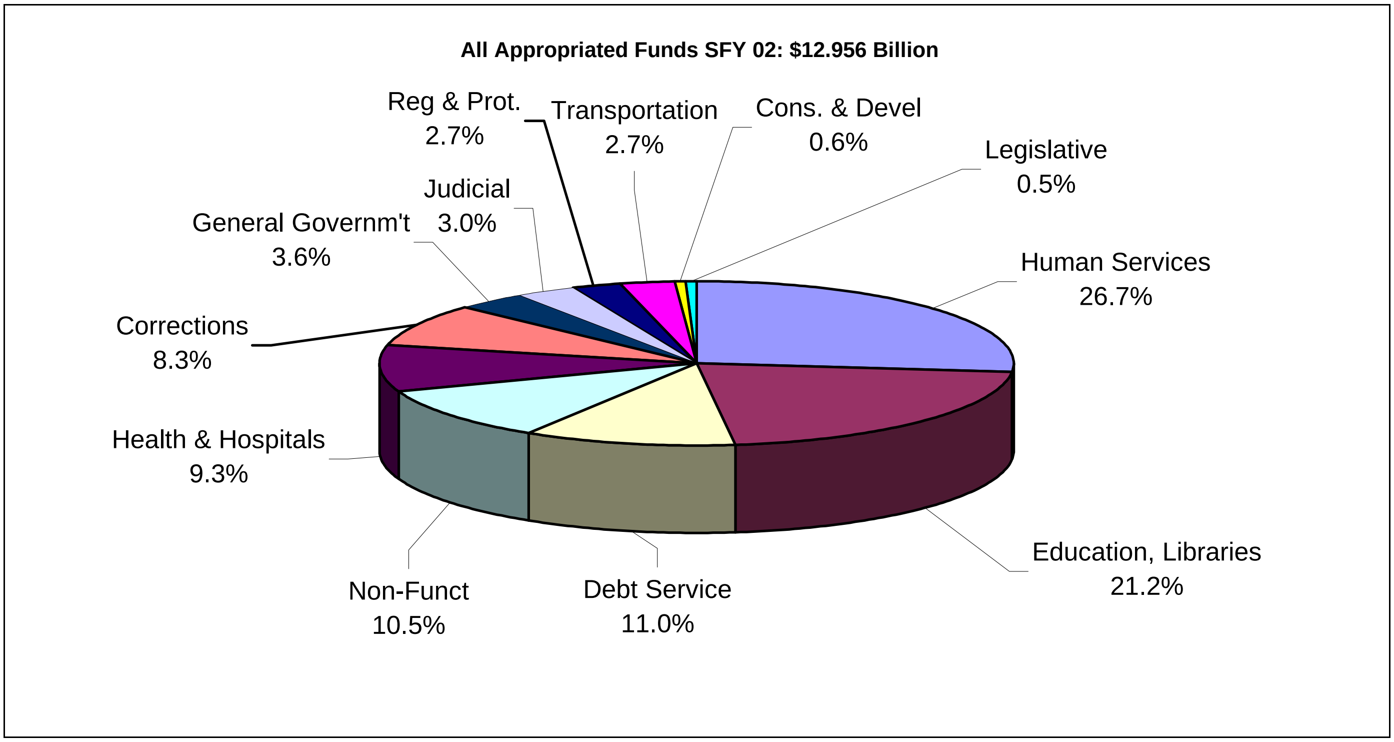
Importantly, CT's total *bonded* debt (about $9.72 *billion* in SFY 00) constitutes only about half of the state's total long-term indebtedness. The other area of significant state indebtedness is in unfunded pension liabilities (which represent currently about $7.6 billion of additional debt).

Appropriations

Where does the state spend its money – by function of government?

For SFY02 (July 1, 2001 through June 30, 2002), the state has appropriated a total of $12.96 billion for spending. Of this sum, about $11.89 billion will be spent through the state's General Fund, $841 million through the state's Transportation Fund, and the balance through the state's other, smaller funds.

In order by share of all appropriated funds, the following are the budget's functional categories and brief descriptions of the agencies and entities included therein. The SFY 02 appropriations noted are *prior* to rescissions and excluding lapses. Note: Brief descriptions of the purpose and functions of these various state agencies are included each year in the *Governor's Budget* and *Governor's Budget Summary* (on-line at www.opm.state.ct.us/budget/2001-2003Budget/GovBudget.htm).



Human Services largely covers spending by the Department of Social Services (DSS) which provides a range of services and supports for CT's most needy. About 80% of DSS' SFY 02 $3.5 billion in appropriated funds will be spent on health care, chiefly Medicaid ($2.45 billion). (Note: about ¾ of these Medicaid funds are spent on health services and long-term care for CT's poor elderly and disabled residents; while ¼ provides health care to poor children and their parents.) Also included is funding for various food, shelter, child care, income support programs, and services that promote independent living.

Education, Libraries includes spending on primary, secondary, and higher education. $1.46 billion of the State Department of Education's (SDE) $1.9 billion budget is distributed to towns through education equalization grants to improve the equity of school funding across district lines. SDE also funds a range of other primary and secondary school programs and services, including magnet and charter schools, the vocational-technical schools, supplemental funding for priority school districts, and special education excess costs. The higher education portion of this budget category includes funding for the various state universities—UCONN ($191 million), the UConn Health Center ($74 million) the Connecticut State Universities ($139 million), the Community-Technical Colleges ($124 million), and Charter Oak State College ($2 million), as well as the Department of Higher Education ($51 million). The education budget also includes funding for the State Library ($15 million) and services for the blind and deaf ($17 million).

Debt Service consists of principal and interest payments on the state debt (bonds). In SFY 02, this totals slightly more than $1 billion. As discussed above, this is one of the two types of state spending reviewed by the Finance, Revenue and Bonding Committee, rather than the Appropriations Committee. The other is "tax expenditures" (which do not appear as "appropriations" for reasons discussed earlier).

Other Non-Functional. This category includes accounts that do not automatically fit into one of the other categories of government, such as funding for benefits for current and retired state employees (e.g. social security taxes, health and retirement benefits). Also included are such items as grants to towns from the Mashantucket Pequot and Mohegan Fund, and reimbursements to towns for loss of property taxes on state-owned and private, tax-exempt property (PILOT).

Health and Hospitals includes the expenditures of the Departments of Public Health ($78 million), Mental Health and Addiction Services ($432 million), and Mental Retardation ($696 million), as well as the Office of Health Care Access ($3 million) and the Office of the Chief Medical Examiner ($5 million).

Corrections includes funding for the Department of Correction ($520 million), which administers and staffs the adult prison and jail system. It also includes funding for the Department of Children and Families ($550 million). DCF has statutory responsibility for child protective services (child abuse/neglect), children's mental health and substance abuse services, and juvenile justice. Also included under corrections is funding for the Children's Trust Fund ($5 million for prevention of child abuse/neglect) and the Parole Board ($10 million).

General Government includes a diverse group of offices and agencies, including the Governor, Lieutenant Governor, State Treasurer, State Comptroller, and Attorney General. The agencies that receive the greatest proportion of funding in this category are the Office of Policy and Management ($171 million), the Department of Revenue Services ($62 million), the Division of Criminal Justice ($41 million), the Department of Public Works ($41 million) and the Departments of Veterans Affairs and of Administrative Services ($28 million each). Other agencies include those concerned with elections, freedom of information, information technology and workforce development.

Judicial primarily includes the funding for the Judicial Department ($350 million), which funds the operations of our courts, court support services, the state's juvenile detention centers, and various alternatives to incarceration programs. Judicial also includes funding for the state's Public Defender Services ($34 million), which provide attorneys to indigent persons who are accused of criminal acts.

Regulation and Protection includes funding for the Departments of Public Safety ($137 million) and the Military Department ($7 million). It also includes funding for the Department of Consumer Protection ($11 million) and the Department of Labor ($53 million), an agency that over the 1990s has been given broader responsibility for all the state's workforce training and development programs. Also included is funding for agencies whose charge is advocacy and protection – the Office of the Victim Advocate, the Office of the Child Advocate, the Office of Protection and Advocacy for Persons with Disabilities, and the Commission on Human Rights and Opportunities.

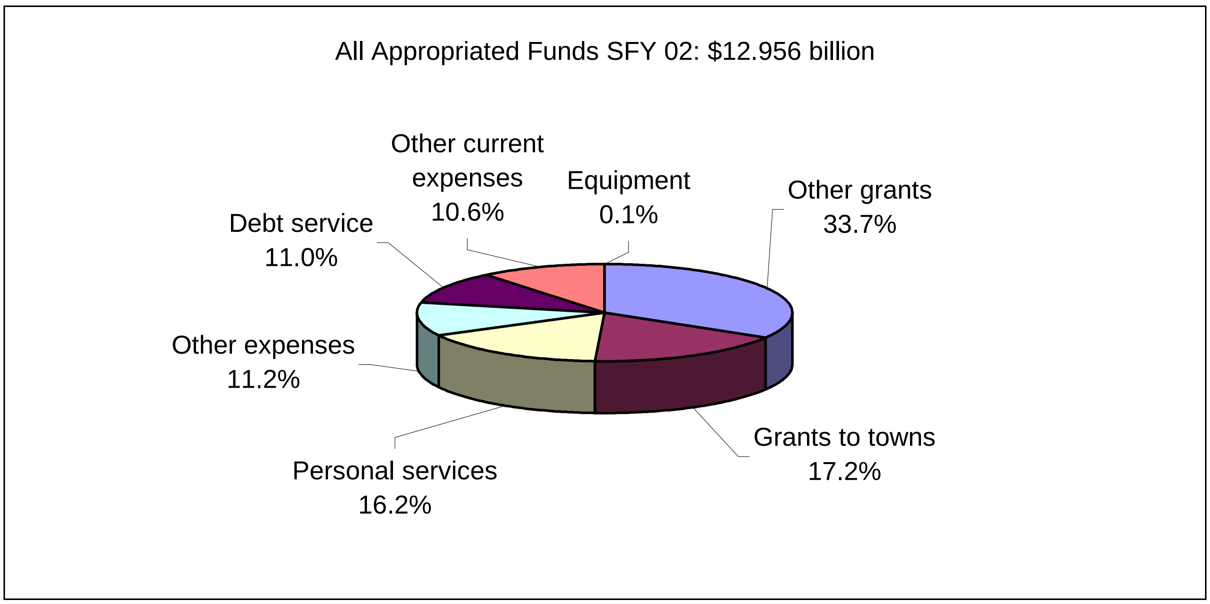
Transportation funds the Department of Transportation, the agency responsible for road construction and maintenance and for public transit. DOT receives its funding from both the General Fund *and* the Special Transportation Fund.

Conservation and Development includes funding primarily for the Department of Environmental Protection ($39 million), Department of Economic and Community Development ($24 million), Department of Agriculture ($5 million), and the Agricultural Experiment Station ($6 million) -- agencies that work to protect CT's environment and natural resources, support its agriculture, and attempt to meet its needs for affordable housing and responsible economic and community development.

Legislative includes funding for the salaries of legislators, legislative research and support staff and all the other operations of the Office of Legislative Management ($49 million), which facilitates the day-to-day functioning of the legislature. It also includes funding for the Auditors of Public Accounts ($9 million), who audit the books and accounts of each state agency, state-supported institutions, and public and quasi-public bodies created by the legislature. This part of the budget also includes funding for the Permanent Commission on the Status of Women, the Commission on Children, the African-American Affairs Commission and the Latino and Puerto Rican Affairs Commission, which all are charged with informing policy leaders about matters within their respective areas of concern.

Where does the state spend its money – by type of spending?

Another way to understand how the state spends its money is by the type of expenditure it makes. The following chart illustrates the allocation of all appropriated funds in SFY 02 by type of expenditure:



Other Grants (33.7%) are direct payments to institutions, agencies, or individuals that are not part of a state agency's operating budget. They include Medicaid payments (which are 19% of *all* CT's appropriated funds), cash assistance benefits to families (1%), and teachers' retirement benefits (2%). Other examples are contractual services provided by non-profit organizations.

Grants to Towns (17.2%) are direct payments to towns for a specific purpose or reimbursements to towns for certain expenses already made. The education equalization grants discussed earlier (14% of *all* CT's appropriated funds) make up the largest portion of the state's payments to towns. It should be noted that these education grant payments are made to the *towns*, and not to the Boards of Education.

Personal Services (16.2%) includes compensation for the services of officials and state employees (but excludes higher education, at $95 million).

Other Expenses (11.2%) includes payments for contractual services, supplies and materials, and other expenditures that are not properly assignable to other standard accounts (such as employee fringe benefits, Lottery prizes and student aid grants).

Debt Service (11%), as noted above, is payment of interest and principal on the state's bonded indebtedness.

Other Current Expenses (10.6%) are authorizations that can be spent on personal services, contractual services, equipment or fixed charges, so long as the funds are spent in connection with the purpose for which they specifically were authorized. It *includes* higher education, at $95 million.

Equipment (0.1%) includes all items of equipment with a value over $1,000 and a useful life of more than a year, as well as all books and periodicals, tapes etc. purchased by the State Library or other libraries, regardless of cost. NOTE: This is an unusually small proportion of the budget because, increasingly, equipment with a useful life of at least five years is being purchased using bond funds through the Capital Equipment Purchasing Fund, administered by OPM, so is not shown as part of the operating budget.

What are CT's "biggest ticket" expenditures?

The biggest single state budget item is Medicaid, which in SFY 02 cost about $2.45 billion, or about 19% of *all* appropriated funds. CT receives 50% reimbursement from the federal governments for its Medicaid expenditures; when received, these funds are deposited into the General Fund and counted as revenues to the state.[3] Importantly, though the elderly poor make up only about ¼ of state residents who receive Medicaid, their health care costs consume about ¾ of all Medicaid funding. By contrast, poor children and their parents comprise about ¾ of all Medicaid recipients, but use only ¼ of Medicaid funding. The next largest expenditures are for compensation for active state employees ($2.123 billion), education equalization grants (ECS)($1.46 billion), and debt service for all budget funds ($1.44 billion).

Interestingly, more than $2.2 billion of the SFY 02 budget will be spent on state grants to towns, and of this $1.76 billion is for education-related programs and services (including the ECS grants). Other grants to towns include payments in lieu of taxes (PILOT) to help cover lost property tax on exempt state-owned and non-profit property and on new manufacturing machinery and equipment. Other grants provide funding for school-based health centers, local health departments, property tax relief for seniors, and a number of other town needs. Such financial assistance to towns helps reduce reliance on local property taxes. A summary table of the state appropriated grants to towns in SFY 02 is included in the *Connecticut State Budget,* while a town-by-town analysis of all grants is reported by the Office of Fiscal Analysis, *Statutory Formula Grants to Municipalities.* *www.cga.state.ct.us/ofa/documents/August2001StatutoryGrants.pdf*

Is all state spending in the General Fund budget?

Of the $12.956 billion in appropriated funds in SFY 02, nearly all are included in the General Fund (about 92%). For this reason, the General Fund commonly is referred to as "the state budget." However, the state also has several smaller, specific-purpose funds that are funded by their own revenue streams. For example, the Transportation Fund ($841 million in SFY 02) pays for road maintenance and is largely funded by motor vehicle taxes, licenses, and fees. Other dedicated funds include state regulatory funds for banking, insurance, and public utilities; the Workers' Compensation Fund, and the Mashantucket Pequot and Mohegan Fund. Finally, as discussed earlier, two specific

[3] Thus, the total spending of *state tax dollars* on Medicaid really is about $1.2 billion (with an equal investment in Medicaid by the federal government).

types of "spending" are actually decided as part of the *revenue* side of the budget—debt financing and tax expenditures.

Budget Formulation & Implementation

What IS the state budget and the budget cycle?

CT has a two-year (biennial) budget. The budget is adopted in odd-numbered years, and revised – as needed – in even-numbered years. The final budget is incorporated in a number of bills, all adopted generally toward the end of the legislative session each spring:

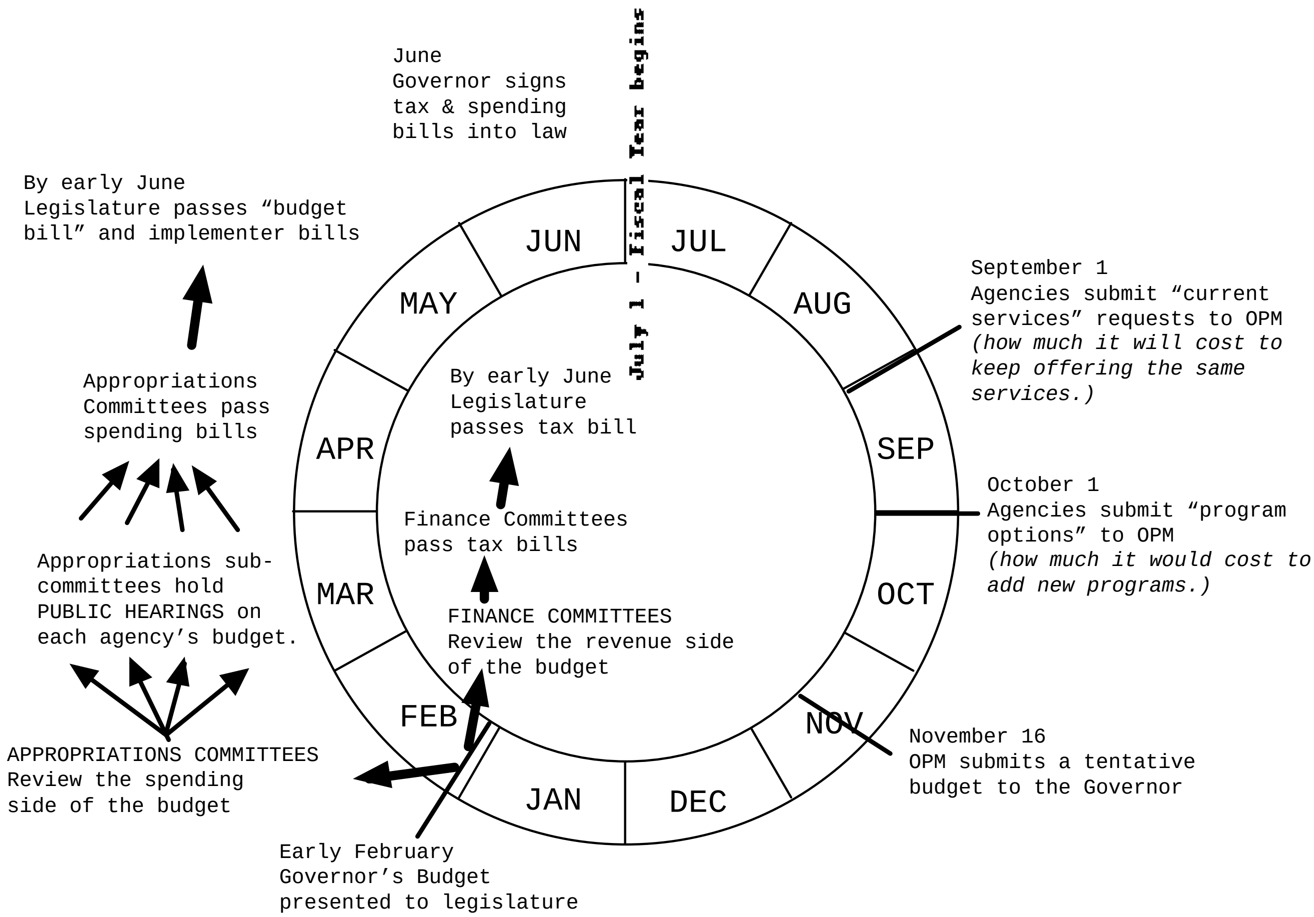
- The "budget bill" which defines how much is to be spent by the various state agencies on their various programs, services, and staff, and that must include legislative revenue estimates. The budget bill includes "back of the budget" language (i.e., text that is literally at the end of the budget bill) that sets out what funds may be carried forward and for what purposes, and provides legislative direction on other aspects of the budget.

- "Budget implementers" that provide greater detail on how funds in the budget bill are to be spent. For example, in the 2001 session the legislature added $400,000 to DSS' Medicaid budget in its budget bill, then specified in an implementer bill that these funds were to be used to fund a breast and cervical cancer prevention and treatment program. (In more recent years, these budget implementers also have been used as vehicles for making policy changes that are less directly related to budget implementation.)

- One or more revenue-related bills that make adjustments to the state's tax code and otherwise impact on state revenues.

- A "bond package" for the financing of new and revised capital projects that usually includes: a) a special act that authorizes new general obligation (GO) bonds for state agencies and programs and amends bond authorizations passed in prior years (either by changing the purpose for which the funds are to be used or the amount of funding authorized for a particular project); b) a public act that increases bond authorizations contained in statutes (like Urban Act bonds and Clean Water Fund bonds); and c) one or two public acts that increase Special Tax Obligation (STO) bond authorizations for transportation-related projects.

But before this final budget is adopted, a long period of legislative review of budget proposals, public hearings, and negotiations that influence what ends up in it. The following diagram outlines what the cycle roughly looks like in odd-numbered years when the biennial budget is being adopted (note that the timelines for agency submissions to OPM are dictated by OPM; they may differ somewhat from year to year from the dates shown here). In even-numbered years, the state makes "adjustments" to the second year of the biennial budget-- which are often very substantial -- through more or less this same process.



An important thing to note about the budget cycle depicted above is that it is really two processes: one that primarily decides how to raise money, and another that decides how to spend money. Once the Governor’s proposed budget reaches the General Assembly, the Finance, Revenue and Bonding Committee considers those parts of the budget that pertain to taxes, revenues, and bond requests, while the Appropriations Committee considers proposals to spend funds on the many programs and services supported with state dollars.

In addition to considering two different “sides” of the budget, these two committees have quite different tasks before them. On the “revenue side,” the Finance, Revenue and Bonding Committee does *not* have to review each element of the state tax code each year, and decide which aspects should be kept and which repealed. Rather, once a change is made to the tax code (such as to exempt the sale of food from vending machines from the state sales tax), it typically remains in effect forever unless changed by some future legislative action. So, this Committee focuses on proposed changes to the tax code. In stark contrast, decisions about state spending are reviewed by the Appropriations Committee -- budget line by budget line -- each and every year. All appropriations must be *re*-authorized every budget cycle, or they cease to exist.

In understanding how the budgetary priorities of the state are set, both processes are critical. While it is probably easier for each of us to understand how decisions about appropriations (spending) affect important priorities and issues in Connecticut, for at least two reasons, the decisions on the revenue “side” of the budget are just as crucial (particularly since the “spending cap” was adopted in 1992):

- Sometimes the state cannot spend more money to achieve a particular policy goal *even when* it has the extra revenues to invest because any additional spending would violate the spending cap. This was the case in the late 1990s when the economy was extremely strong. As discussed earlier, in such situations CT could – and did on any number of occasions – circumvent the cap through the revenue "side" of the budget – achieving the same goal by using bond funds or by passing a tax expenditure.

  For example, the managed care plans that provide health services to low-income children and their parents came to the state saying that the fees they were being paid by the state through Medicaid were inadequate. Simply increasing their fees would not only have been a new expenditure subject to the spending cap, but would also have threatened the state's compliance with federal law. So, to keep these plans participating, the state first exempted them from paying the insurance premiums tax on these Medicaid policies, and then – in a subsequent legislative session – also gave them a tax credit (now worth nearly $15 million) against the insurance premiums tax they were required to pay on their commercial policies.

  Both of these techniques to "spend" through the revenue side of the budget – through tax expenditures and bonding -- have long-term budget consequences. They reduce state revenues in future years, and increase the proportion of appropriated funds that must be used to pay debt service.

- Decisions to cut tax rates and create new tax loopholes reduce the funds available to fund essential state services in future years. As discussed earlier, over the prosperous late 1990s, CT made many structural changes to its tax code that reduced state revenues by billions of dollars. Now that the economy is weak and the expenses associated with a weak economy and a nation at war are increasing, these structural changes are contributing to our decline in state revenues. The resulting deficit, in turn, is triggering calls to cut spending for a variety of programs and services that serve important public purposes (see below).

For these reasons, the formulation and implementation of *both* "sides" of the budget -- the appropriations "side" and also the revenue "side" – are described in more detail below.

How is the state budget formulated?

State law defines the procedures by which the state budget is to be formulated and implemented (see Conn. Gen. Stat. §§4-69 *et seq.*). A short summary of key steps follows:

<u>Preparing the Governor's Proposed Budget/Budget Revisions</u> (May through early February). Beginning in May, state agencies start work on their budget requests for the fiscal year that begins July 1 of the following year – some 15 months later.

Around August 1 (11 months prior to the effective date of the budget being prepared), the Office of Policy and Management (OPM)(the Governor's budget and policy office) sends forms and instructions to the state agencies for use in formally submitting budget materials to OPM. In even-numbered years, the materials the agencies prepare for OPM will include their estimates of the funding necessary to provide -- in the succeeding year --the *same services* as in the current fiscal year (with necessary adjustments for inflation, annualization of partial year costs, projected caseload increases or declines, the completion of projects and other known events with impact on the budget). This is known as the "current services" budget. Depending on OPM's instructions, agencies may also transmit proposals for new programs and services (“expansion” options), proposals to cut programs or services (“reduction” options) and/or proposals to reallocate funding among agency accounts (“reallocation” options).

In odd-numbered years, agencies send OPM their proposals for *adjustments* and *revisions* to the second year of the biennial budget, as needed. The August 2001 memo from OPM to agency heads directed that a listing of program priorities and reduction and reallocation options were due back to OPM by the end of October. It also stated that if an agency identified some new need that had to be met, the agency had to request a reallocation of existing resources – not request additional funding.

During the fall, OPM’s budget analysts review the agencies’ budget requests and prepare recommendations for those agencies within their jurisdiction, based on their analysis of the effectiveness of existing programs and the need for changes. The Secretary of OPM then reviews these recommendations, makes adjustments based on the administration’s determination of which needs have highest priority and its revenue estimates, and sends the revised recommendations to the Governor for review.

The Secretary of OPM must provide any newly-elected Governor with a tentative budget, including all necessary revenue and expenditure estimates, by November 15. The Governor-elect can hold hearings on this proposed budget, and agency heads must attend and OPM staff must attend to assist in the transition.

The Governor presents the proposed biennial budget (or proposed budget revisions in even-numbered years) to the General Assembly in early February. The proposed biennial budget must include four parts: 1) the Governor’s budget message (with content as specified in Conn. Gen. Stat. §4-72); 2) recommendations for appropriations for every agency for each fiscal year of the biennium (with content as specified in Conn. Gen. Stat. §4-73 -- including recommendations for operating budgets, bonding requirements for capital projects, and staffing); 3) drafts of the appropriations, bonding, and revenue bills to carry out the recommendations made in parts 1 and 2 (Conn. Gen. Stat. §4-74); and 4) an economic report that analyzes the current status of the CT economy and the impact of the proposed budget on it (Conn. Gen. Stat. §4-74a). Also included must be estimated revenue and expenditure projections for the three fiscal years *after* the two-year budget (“out-year” projections). This provides a clearer understanding of how the proposed budget impacts on state revenues and expenditures several years in the future. The Governor is also responsible for preparing a five-year Capital Projects and Facilities Plan.

Legislative Review of the Governor’s Proposed Budget/Budget Revisions. Once the Governor’s proposed budget is presented to the General Assembly, the review of the proposed budget is divided. The “spending” side of the budget is referred to the Appropriations Committee, a 53-member committee that also has responsibility for approving all block grant allocation plans and labor contracts, as well as reviewing all bills with any impact on expenditures. The “revenue” side of the budget is referred to the Finance, Revenue and Bonding Committee. Both of these Committees (like all others in the General Assembly) have members from both the House and Senate and are co-chaired by a State Senator and a State Representative.

The Appropriations Committee holds a public hearing on each agency’s budget. Also, in work sessions, the 12 subcommittees of the Appropriations Committee review the operating budgets of the agencies in the subcommittee’s area of cognizance with the agency heads, OPM staff, and budget staff from the General Assembly’s Office of Fiscal Analysis (OFA). These sub-committees (Collective

Bargaining, Conservation and Development, Elementary and Secondary Education, General Government A, General Government B, Health and Hospitals, Higher Education, Human Services, Judicial and Corrections, Legislative, Regulation and Protection, Transportation), with the help of OFA, then develop recommendations for presentation to the full Appropriations Committee, through its chairpersons. After the committee chairs review and refine the subcommittee recommendations, they are put into the Committee's appropriations bill. After approval by the Appropriations Committee, OFA prepares a committee budget report that contains a description of legislative intent for all changes that the Appropriations Committee voted to make to the Governor's proposed agency budgets.

Concurrently, the Finance, Revenue and Bonding Committee, with the help of its two subcommittees (Bonding and Special Revenue), reviews the revenue and capital portions of the proposed budget. This Committee also holds public hearings on its "side" of the budget, as well as on any other proposed revenue and bonding bills. Subcommittee recommendations are prepared for the full Committee with OFA's help. These are reviewed and refined by committee chairs, and put into the revenue and bonding bills to be voted on by the full Committee.

In addition, many other bills (or amendments) introduced in a legislative session by members of the General Assembly may have fiscal implications. Those that impact on spending are referred to the Appropriations Committee; those with revenue or bonding implications are referred to the Finance, Revenue and Bonding Committee. OFA prepares fiscal notes that estimate the costs or savings to the state and municipal government if the bill passes. Fiscal notes are prepared (by the OFA analyst with budgetary responsibility for the affected agency) for every bill and amendment that reaches the House or Senate floor as an objective, non-partisan statement of fiscal impact. If such bills then are approved by these "money" committees, their costs (or savings) must be considered in the overall reconciliation of the budget.

Because the Connecticut Constitution requires that the state's budget be balanced (i.e., the state may not budget for a deficit), projected expenditures cannot exceed revenue estimates. This requires that the spending approved by the Appropriations Committee must match the Finance Committee's proposals (and estimates) for generating revenue. To accomplish this, the committee bills are further negotiated among legislative leadership and the Governor; necessary modifications are made. The final budget bills are then voted on by the full General Assembly, commonly near the very end of the Session (and sometimes in a Special Session convened after the regular session, in years with particularly difficult budget negotiations). The bills are then signed by the Governor.

In even-numbered years, the process for legislative approval is similar. The Governor's proposed revisions to the biennial budget follow the review process described above, with slight changes in timing because this session is a "short" session that convenes in February and ends in the beginning of May (while the "long" session in odd-numbered years begins in January and ends in the beginning of June).

After the budget (or budget revisions) is adopted by the legislature and approved by the Governor, OFA publishes its formidable "budget book." Entitled the *Connecticut State Budget*, it provides detailed information on agency budgets, including newly-authorized expenditures and expenditure reductions, changes in state taxes and other revenue measures, and bonding. It can be found on-line at www.cga.state.ct.us/ofa.

How is the state budget implemented?

Agency budget allotments. Agency appropriations (the expenditures authorized by the General Assembly) are administered by OPM through an allotment process. Shortly after the budget is adopted, each state agency prepares a spending plan that must be reviewed by OPM and approved by the Governor before the July 1 start of the new fiscal year. Funding is then allotted to the agencies by OPM on a quarterly basis, based on their annual spending plans. Agencies prepare monthly financial statements to allow executive and legislative oversight of expenditures.

Agency adjustments. Agencies can ask OPM to make adjustments in their quarterly allotments, or to transfer funds from one appropriation account to another. However, if a transfer is more than 10% of the original appropriation or $50,000 (whichever is less), it must be approved by the Finance Advisory Committee (FAC). Also, there may be no transfer of funds from the General Fund to any agency that is in excess of that agency's regular appropriations, except on recommendation of the Governor and after FAC approval. The FAC is a joint legislative-executive body composed of the Governor, Lieutenant Governor, Treasurer, Comptroller, two Senate members of the appropriations committee appointed by the Senate President (with not more than 1 from the same political party) and three House members of that committee appointed by the House Speaker (with not more than 2 from the same political party).

Allotment restrictions. If the Governor determines that there has been a change in circumstances or that estimated revenues will not be enough to finance the year's appropriations in full, the Governor may restrict the allotment of appropriated funds after filing a report with the Appropriations and Finance Committees. Also, each month the State Comptroller is required to prepare a statement on the financial status of the state that is sent to the Governor and made available to the legislature and the public. If this monthly statement projects a budget deficit that is greater than 1% of total General Fund appropriations, the Governor *must* restrict allotments.

The Governor's allotment restrictions generally cannot exceed 5% of the amount in any agency budget account, or more than 3% of total appropriations in a fund. However, the Governor may – with the approval of the FAC – reduce overall appropriations by more than 3% of the total in any fund and by more than 5% of any appropriation, provided that any change that cuts more than 5% of the total appropriation from any fund requires the approval of the full General Assembly.

Bonding. After the legislature passes the bond package, bond funds are not immediately spent on projects. Instead, specific decisions about where to spend bond money are made by the Bond Commission, which meets monthly and consists of the Governor, Treasurer, Comptroller, Attorney General, Secretary of OPM, Commissioner of the Department of Public Works, and the Co-Chairs and Ranking Members of the Finance, Revenue and Bonding Committee. Each month, the Governor puts particular projects on the Bond Commission's agenda; the Commission can only act on projects on this agenda. For this reason, and because capital construction can take quite a long time, bond authorizations can remain on the books for several years before the money is actually spent.

Who are key players in the budget process?

Historically, the *Governor* has had the greatest impact on the state budget process. The Governor's proposed budget (or budget revisions) sets the stage for debate -- it is the document the legislature reviews and modifies. Until the *General Assembly* gained professional budget staff after the 1970s, changes made in the Governor's budget tended to be relatively minor. Now, the legislature is able to conduct a more in-depth review of the Governor's proposed budget and provide some independent leadership and vision. In addition to Senate and House leadership, the Co-Chairs and Ranking Members of the General Assembly's "money" committees – the Appropriations Committee and the Finance, Revenue and Bonding Committee – have particular influence in the budget process.

The Office of Policy and Management (OPM) is the executive branch's budget office. The Governor appoints the Secretary of OPM. OPM develops the Governor's budget proposal, and monitors implementation of the budget once approved.

The Office of Fiscal Analysis (OFA) is the legislature's budget office. It is staffed by non-partisan legislative staff who report to the Office of Legislative Management. OFA assists the legislature in drafting the final budget and in analyzing and preparing a fiscal note on each bill and amendment that comes to the floor of the House or Senate that outlines its potential costs and/or savings to the state and local governments. It also analyzes current services estimates, tracks and forecasts expenditure and revenue levels, develops forecasting models and out-year expenditure and revenue projections.

The *State Comptroller* is CT's chief fiscal officer, responsible for keeping the state's books. The Comptroller decides the mode of keeping and reporting on all public accounts, and publishes a monthly statement on the state's financial status, as well as comprehensive annual reports on the state's revenue, expenditures and other relate information. The Comptroller is popularly elected by voters statewide.

The *State Treasurer* administers CT's billions of dollars of investments, including pension funds and trust funds. The Treasurer also is popularly elected by voters statewide.

The *Auditors of Public Accounts* provide independent and objective analyses, opinions and recommendations on the operations of state government and its effectiveness in safeguarding the state's assets. The auditors – one Democrat and one Republican – audit the books of every state agency every two years. They are appointed by the legislature.

The *Department of Revenue Service* (DRS) is the state agency that collects the state's taxes. The Commissioner of DRS is appointed by the Governor.

What are some of the constraints on the budget process, and how do they affect budget decisions?

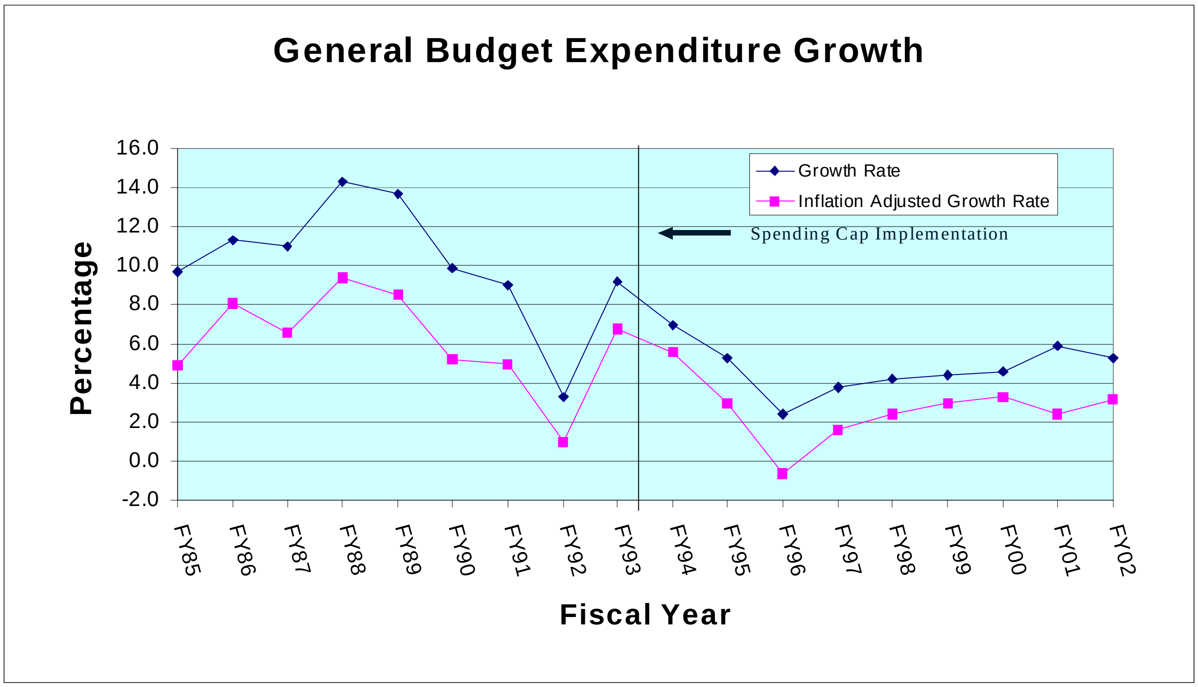
CT faces a number of constraints as it puts together its budget. They include the requirement to maintain a balanced budget and not exceed the state spending cap, to comply with federal mandates and court orders, and to keep bonded indebtedness below the statutory limit.

Balanced budget requirement and state spending cap. In 1992, when the state passed the income tax, the 28th Amendment to the Connecticut Constitution was adopted. The amendment requires that the state budget be balanced – general budget expenditures may not exceed estimated revenues. Together with CT's statutory cap on spending, it also limits growth in state spending from one year to the next to the *greater* of the five-year average in growth in CT's personal income[4] or the twelve-month rate of inflation. The state may exceed this cap only after an emergency declaration by the

[4] Interestingly, the measure of personal income used *excludes* capital gains income, an important source of revenue in a state with CT's wealth.

Governor, followed by a three-fifths majority vote of both houses of the General Assembly. Excluded from spending cap restrictions are funds earmarked for debt service, grants to distressed municipalities that were in effect on July 1, 1991, or the first year costs of implementing court orders or federal mandates. The cap applies to spending through the General Fund, the Transportation Fund and multiple other funds.

The spending cap has contributed to a decline in the growth of state spending. Between 1987-1991, state spending grew nearly 11% each year. From 1991-1995, it grew about 6.4% per year. From 1995-2001 it grew about 5.0% per year (excluding surplus spending on one-time expenditures). However, the cap also has allowed "real" (inflation-adjusted) growth in the budget, as illustrated in the following chart:



It is also true that the spending cap has been exceeded in each of the last four years --- to allow CT to spend the millions of dollars of General Fund surplus that had accumulated. In SFY 01, the Governor issued a declaration of "the existence of … extraordinary circumstances," that included nine straight years of budget surpluses, a fully funded Budget Reserve Fund, and state needs that required additional state funds. In SFY 00, the cap was exceeded by $230 million; in SFY 01 by about $600 million. Many of the surplus fund expenditures sought to avoid the issuance of debt or were used for expenses that were primarily one-time in nature. However, some of the others were not. Moreover, now that the SFY 02 budget is in deficit, the Governor has proposed re-directing SFY 01 surplus funds from their originally-intended purposes to on-going operating expenses to help balance the budget.

Because the spending cap exists, it also has been more difficult to increase funding for existing programs and services, or fund new ones — even if revenues are plentiful. Consequently, as discussed earlier, some programs and services that would have been funded ordinarily through appropriations are, instead, being "funded" through the revenue side of the budget – by tax credits and other preferential tax treatment, or by using bond funds.

One of the peculiarities of the state spending cap is that it tends to limit growth in *federal* spending on CT programs. This is a direct consequence of how CT budgets – using "gross" rather than "net" budget figures. For example, DSS' Medicaid account shows $2.65 billion in expenditures. However, CT receives federal reimbursements equal to about 50% of this sum which, when received, are simply counted as revenues. Thus, though CT's total state expenditure on Medicaid is about $1.3 billion, the appropriated budget for Medicaid is *double* this amount. DSS' budget line shows a "gross" budget for Medicaid, not its "net" budget after federal reimbursements are deducted. Because this total amount (state *and* federal) is what is appropriated, all is subject to the spending cap's limit on growth. The consequence of this is that the cap can deter – and *has* deterred -- CT from claiming federal funds to which it is entitled.

Federal mandates. CT's receipt of federal funding is conditioned on its compliance with all restrictions and requirements associated with that funding. For example, although CT is not required to participate in the Medicaid program or the Title IV-E foster care program, the receipt of millions of dollars of federal funding to help cover the costs of these programs (that provide health care to low-income residents and care for abused children, respectively) is conditioned on compliance with all federal laws and regulations governing the conduct of the programs. One of the key requirements of the Medicaid program for children is that all children and youth receive Early and Periodic Screening, Diagnosis and Treatment (EPSDT) --- periodic screening for health, mental health, dental, vision and hearing problems and all medically-necessary treatment to address identified problems. If CT fails to assure that such children receive this care, it risks losing millions of dollars of federal reimbursement funds.

Court orders. Over the years, a variety of court orders have been issued – by both state and federal courts – that require CT to do certain things to comply with federal and state law. For example, the Consent Decree in the federal class action case Juan F. requires DCF to follow certain procedures and maintain certain staffing levels to enhance the care of children reported to it as abused or neglected. The CT Supreme Court decision in Horton v. Meskill required CT to change the way it finances public education (and resulted in the use of ECS grants). Often, these court orders require the appropriation of additional funds, or the re-allocation of funds, to address the legal wrong the court requires CT to correct. Funding to comply with such court orders is mandatory; failure to do so subjects responsible state officials to being found in contempt of court.

Limitations on state indebtedness. State law (Conn. Gen. Stat. §3-21) puts a ceiling on the total amount of General Obligation (GO) bonds the General Assembly may authorize – 1.6 times the total General Fund tax receipts projected (unless required to meet cash flow needs or emergencies resulting from natural disasters). The State Treasurer must certify that any bill authorizing bonds does not violate the debt limit before the legislature can vote on the bill. The Treasurer also must compute CT's aggregate indebtedness each January 1 and July 1, and certify this to the Governor and General Assembly. If the indebtedness reaches 90% of the ceiling amount, the Governor must review each bond act for which obligations have not yet been incurred, and recommend to the legislature priorities for repealing these authorizations. As of July 1, 2001, net SFY 02 GO bond indebtedness was $11.78 billion, or about 84% of the debt limit. Net SFY 03 indebtedness is nearly 85% of the limit.

What are "deficiencies," "lapses," "carry forwards," "budget surpluses" and "budget deficits" — and why don't the numbers seem to add up?

In a budget of $13 billion, it is not surprising that some spending is less than expected while some spending is more, just as revenues may come in more or less than projected. Changing economic times, delays in program start-ups, caseload changes, and even catastrophes like September 11 can all impact on the budget's actual revenues and expenditures. Adjustments, therefore, always need to be made. As a result, the budget may appear to be a moving target, and sometimes the numbers just don't seem to add up. The following describe some adjustments that are commonly made.

Deficiencies. Each year, some state agencies exceed the appropriations given them. DSS typically overspends its Medicaid budget, for example. Both the Military Department and the Department of Public Safety have deficits this year of $1 million each, due to increased overtime costs to respond to terrorist and public health threats.

In SFY 01, deficiencies in agency budgets totaled nearly $140 million and the General Assembly approved three deficiency bills to "cover" these shortfalls through a combination of new appropriations (from "surplus" funds that were available because tax revenues were exceeding projections), reduced appropriations in other accounts, and fund transfers. This year (SFY 02), projected General Fund agency deficiencies are expected to be about $60 million (as of December 2001).

Lapses. Each year, the state anticipates that each agency will not actually spend all the money appropriated to it. This unexpended portion of an appropriation, remaining at the end of a fiscal year, is called a "lapse." Administrative lapses (savings) can result when staff positions go temporarily unfilled, or when new staff members come in at lower salaries than were budgeted. Program lapses, by comparison, are achieved when there are delays in program startup, or caseloads decline, or there are greater efficiencies, or other savings. A certain amount of "lapse" is built into each agency's budget. Administrative lapses are generally divided up proportionately among agencies; it is up to each agency to find these savings within their budgets in the coming year. In addition, agencies can be told that they *must* achieve savings in certain accounts – these are mandated lapses.

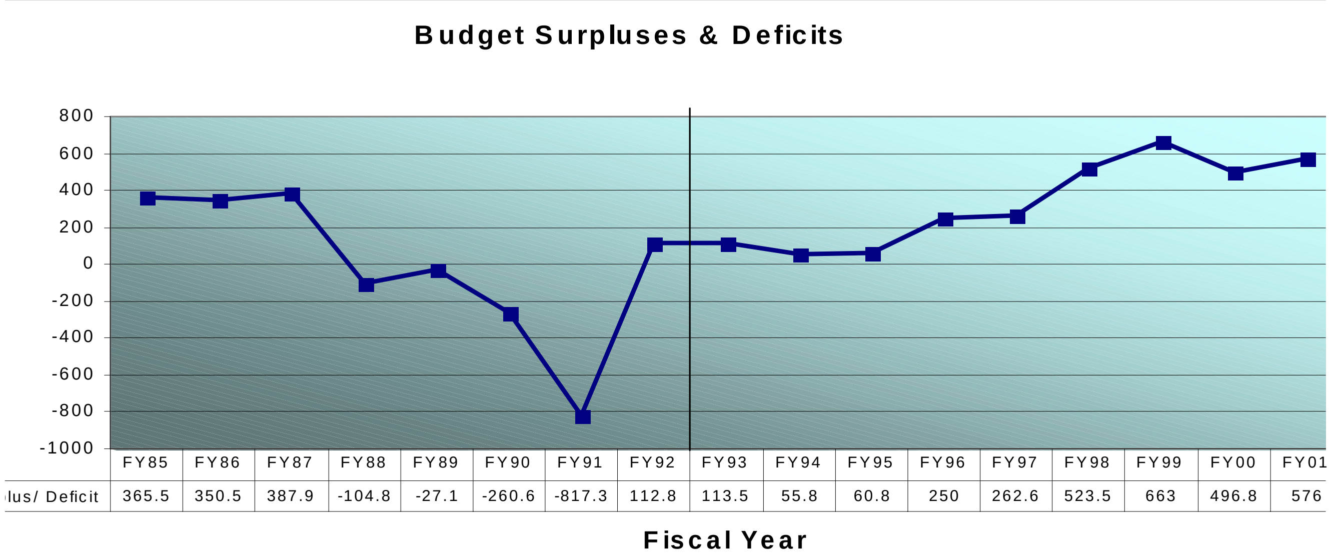
The pie charts at the beginning of the section on Appropriations (showing all appropriated funds for SFY 02 as $12.956 billion) reflect, in fact, "net" appropriations – that is, "gross appropriations" for SFY 02 of $13.04 billion *less* about $119 million in estimated lapse. Of this, about $75 million is in anticipated administrative and program lapses, while the balance is in mandated savings. In the months since the SFY 02 budget was adopted, however, the SFY 02 budget deficit has grown. Accordingly, the Governor and General Assembly have directed that there be additional lapses to help balance the SFY 02 budget.

Carry forwards. Carry forwards are appropriated amounts that the agency did not spend within one fiscal year that can be "carried forward" for spending in the next fiscal year. If unspent money in a budget account is not carried forward, it returns to the General Fund and must be re-appropriated to the program (or to some other program) through the general budget process. The amounts that can be carried forward from one fiscal year to the next, and the purposes for which they may be used, are defined by statute (e.g. Conn. Gen. Stat. 4-89) or by other legislation (such as the budget act itself). About $765 million was carried forward from SFY 01 to SFY 02, including $576 million in SFY 01 surplus funds. In the *Connecticut State Budget*, carry forwards are shown in agency budgets under the category "additional funds available."

<u>Budget surpluses.</u> When revenues collected in a given fiscal year exceed projected revenues by a *greater* amount than actual expenditures exceed the budgeted expenditures, a budget surplus results. In the late 1990s, for example, CT's economy was very strong and revenues from all the state's major taxes far exceeded projections, while the state spending cap limited growth in expenditures. As a result, CT enjoyed substantial budget surpluses in the General Fund at the end of each fiscal year – more than $3 billion total in fiscal years 1995 through 2001, including about $576 million in SFY 01 alone. General Fund surpluses have been used to build the Budget Reserve ("Rainy Day") Fund to 5% of General Fund expenditures, to pay cash for certain capital projects to avoid debt, and for a wide variety of other purposes (including tax rebates, supportive housing, arts, recreation and culture grants, higher education state matching grants, and municipal revenue sharing/impact aid).

<u>Budget deficits.</u> When revenues collected in a given fiscal year fall *below* projected revenues, without a corresponding decline in actual expenditures, a budget deficit results. Such is the case in CT now. In March 2001, the longest economic expansion in United States history ended and the nation officially entered a recession. The state's slowing economy has resulted in slower revenue growth than in prior years; estimated General Fund revenues for this fiscal year (SFY 02) are projected to fall far short of the budget plan. As noted above, projected expenditures are also greater than planned; General Fund agency deficiencies of as much as $60 million are also projected.

The following chart shows the cycle of state budget surpluses and deficits over the past 17 years:



Like a family facing a deficit in its household budget, CT has a variety of options that can be used alone, or in some combination, to bring its budget into balance. It can increase its revenues (such as by repealing or delaying the phase-in of new tax cuts, closing tax loopholes, enacting new taxes such as an increased tax on cigarette sales or on the income of the state's wealthiest residents). It can collect on debts (such as by being more aggressive in claiming federal funds to which the state is entitled). It can put more expenses on the state's credit card (such as by using bond funds for school construction, rather than cash from the SFY 01 surplus). It can figure out ways to spend funds more effectively, and can delay or cut spending – always being careful to assure that essential needs are met. And it can tap into its savings (the state's Budget Reserve Fund, see below).

As of December 2001, by actions taken by the Governor and the legislature in the November 2001 Special Session, CT had reduced its estimated deficit for SFY 02 by about $200 million through a combination of rescissions (cuts) to original SFY 02 appropriations, new mandated lapses, and cuts in spending financed with SFY 01 surplus funds (with the transfer of some of this planned spending to debt financing). CT also elected to delay the continued phase-out of its state inheritance tax. Despite these deficit-reducing actions, however, a significant deficit remains in the SFY 02 budget that the Governor proposed to address through further rescissions and lapses, reductions in carry-forward funds, cuts in SFY 01 surplus-funded initiatives (including substantial cuts to community mental health services), and – in December -- a transfer of $41 million of the tobacco litigation settlement funds to the General Fund.

What is the "Budget Reserve" or "Rainy Day" Fund?

The Budget Reserve Fund was established in 1978. By law, it may have a balance of up to 5% of net General Fund appropriations (well below the national average of 8%). The Fund can be used to finance state operating deficits only at the *end* of a fiscal year; it cannot be used to balance a proposed budget for the coming fiscal year. It is – in essence – the state's savings account; a resource to be tapped when state's financial situation turns bleak. For this reason, it is often called the state's "rainy day" fund. At the end of the fiscal year, any budget surplus first must go to replenishing the Fund, and then to paying off the state's bonded debt or any other uses on which the General Assembly decides.

In the late 1980s, when CT was entering its last recession and budget deficits emerged, CT began withdrawing funds from the Rainy Day fund: $116 million in 1988, $102 million in 1989, and $102 million in 1990. By the end of SFY 90 the fund was depleted, though the recession was not to end until 1992. There were no funds available to offset CT's $965 million cumulative deficit in SFY 91. This crisis led the legislature to adopt the personal income tax. As a result of an improving economy and this fundamental change in the state's tax structure, CT began replenishing its Budget Reserve Fund in 1995. By 2001, the Fund had $595 million in it.

As discussed above, CT now again faces a deficit. One option to address this problem is tapping the Rainy Day Fund.

Some express concern that using these funds to balance the budget will provoke a budgetary catastrophe comparable to what occurred in the early 1990s. Others believe the two situations are not comparable; CT now has a more diverse and resilient economy, and an income tax that is both more stable than sales and corporate taxes, and also a more efficient revenue source in a state with CT's wealth. In addition, as discussed above, other options exist to help balance the budget (e.g., repeal or delay of scheduled tax cuts, repeal of tax loopholes, more aggressive claiming of federal revenues, enactment of a cigarette tax, use of bond funds rather than surplus funds for capital projects). The use of some of these can reduce the need to rely solely on the Rainy Day Fund to balance the budget.

Making Your Voice Count

How can I keep up with the budget process?

The most crucial step in affecting the budget process is trying to follow it as it happens. This is a challenging task. Fortunately, it is now easier to keep track of the progress of bills (including budget bills) through the CT General Assembly's web site: www.cga.state.ct.us. A detailed guide to the legislative process is available online from the state at www.cga.state.ct.us/olm/guide/guide.htm..

However, the truth is that despite good on-line access to pending bills, agendas of committee hearings, and even transcripts of hearings and debates, it can be very hard to keep up to date with the budget process as it unfolds. Many budget decisions are made in the closing weeks of the Session, by a small group of legislative leaders and the Governor. The budget bill and the budget implementer bills are voted on in the closing days of the Session (and more recently in Special Session after the close of the regular session), and can be many pages long. There is little time even for legislators who are being asked to vote on the bills to know all that is in them.

Connecticut Voices for Children is one of many organizations that can help you follow the progress of the budget. Voices' website, www.ctkidslink.org, includes information about the status of particular legislative items that affect children and families and provides updates on state tax and budget issues. Voices' electronic newsletter – *E-Notes* – is published weekly during the legislative session, and includes legislative updates. Your own Representative and Senator too can help you understand the status of budget issues in which you are interested – and your request to them will also let *them* know that you care about a particular issue.

How can I try to influence state budget decisions?

There are several ways to make your voice heard in the budget process:

- If you have an idea for a new program or service, or for some other way to spend state funds smarter, prepare your case. Research your concerns/proposals and develop cost or savings estimates. Write up a brief summary or fact sheet. Determine which agency has responsibility for the budget in your area of concern and try to meet someone in the agency *before* they send their budget requests to OPM. Then try to meet with, write, or call the Governor or someone on the Governor's staff about your idea. The best way to ensure that your item is in the final budget is to have it included from the beginning.

- Get a copy of the budget options of state agencies with responsibility for areas that concern you. Review them to see what the agency is proposing. Let the agency, OPM, and the Governor's Office know about your concerns and thoughts.

- Meet with your own state Senator and Representative, *before* the session, to explain any proposals you have, or to discuss any concerns you have about the budget. Enlist their help. You are *their* constituent!

- Review the Governor's budget (or budget revisions) when it is released, and then meet with, write and/or call your elected representatives, the Chairs and Ranking Members of legislative committees with jurisdiction over the issues that interest you, and the Chairs and Ranking

Members of the Appropriations or Finance Committees and/or Subcommittees appropriate to any part of the budget that worries or interests you.

- Testify at the public hearings (or submit written testimony) on budget proposals. Attend the hearing at which the agency head presents its budget. Listen to legislators' questions and concerns and, when appropriate, follow up with them either in person or by mail.

- Monitor the "back room negotiations" on the part of the budget of interest to you. While this may sound impossible, it is easier if you are linked into an advocacy organization that shares your interest and retains a lobbyist to monitor issues at the Capitol full-time. It also helps if you have formed a relationship with a legislator or legislative staffer who can let you know what is happening.

- Write Letters to the Editor and Op-Eds for your local newspaper to make your interests and concerns public. Encourage others to do so too. Try to get a reporter to do a story or two on the issues that concern you. Press attention is a good way to get legislators' attention.

- Always remember to thank legislators, agency staff, and legislative staff in writing after you meet with them and when they pass the budget, regardless of the outcome. You may be back next year.

The *Citizen's Guide to the Connecticut State Budget* was written by Shelley Geballe, Co-Director of CT Voices for Children, with the assistance of by Ellen Scalettar, Senior Policy Fellow, Janice Gruendel, Voices' Co-Director, and Joey Fishkin, Voices' Young Policy Fellow. The *Guide* was produced with the generous support of the Melville Charitable Trust, the Charles Stewart Mott Foundation, the Annie E. Casey Foundation/National Center for Children in Poverty, and the Fisher Foundation.

Comments on ways to make this *Guide* more useful are much appreciated – please e-mail to Yalie4567@aol.com. Other Voices' publications on state tax and budget issues can be found on Voices' website, www.ctkidslink.org.

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