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January 2, 2015

The Honorable Dannel P. Malloy
Governor of the State of Connecticut
State Capitol
Hartford, Connecticut

Dear Governor Malloy:

I write to provide you with financial statements for the General Fund and the Transportation Fund through November 30, 2014.

The Office of Policy and Management (OPM) is projecting a potential deficit of \$31.6 million in the General Fund for Fiscal Year 2015. This is a reduction to last month's deficit estimate of \$13.2 million. There has been a notable decrease in General Fund spending growth across all major appropriation line-item categories between October and November. In order for the current OPM General Fund deficit estimate to be realized, this reduction in the spending growth trend must continue into future months. The deficit projection continues to utilize the November consensus revenue forecast. While there has been some improvement in key economic indicators, as discussed below, current revenue collections do not indicate a positive change to the consensus projections.

The most notable revisions in this month's General Fund estimates are an increase in deficiency requirements of \$59 million and an offsetting increase in lapse savings of \$72.2 million. These changes produce the reduction in the General Fund deficit estimate.

The majority of the increase in deficiency requirements results from an additional \$40 million shortfall in the Medicaid program. As has occurred historically, the anticipated savings initiatives built into the Medicaid budget for Fiscal Year 2015 will not be fully achieved. In addition, the program continues to struggle with federal reimbursement issues and hospital settlement payments above budget expectations.

The lapse increase is primarily the result of a \$65 million reduction in debt service payments. The state continues to benefit from the on-going low interest rate environment created by policies of the Federal Reserve. At present, the state is realizing premiums on bond issuances.

Total General Fund revenue for Fiscal Year 2015 is forecast to fall \$59.3 million short of initial budget projections. The largest single revenue reduction of \$61.2 million is within the federal grants category. Approximately \$25 million of the total reduction was due to issues related to the deferral of Medicaid revenue attributable to the expansion population covered under provisions of the Affordable Care Act. I have identified this as an area of concern in past letters. The remaining shortfall resulted from delays in federal waivers sought by the Department of Mental Health and Addiction Services and from delayed implementation of adoptive and foster care initiatives. As I stated last month, it is imperative that agencies administering federal grant programs provide timely reporting of potential federal claim shortfalls. The ability to manage the budget is compromised by delayed reporting as was evident in last month's downward federal receipts adjustment.

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Statewide expenditures within the General Fund in Fiscal Year 2015 were trending above the 3 percent budget target through the first four months of the fiscal year. As explained above, a significant reduction in spending growth was posted in November. Year-to-date spending is now trending below the original budget. The current General Fund deficit projections anticipate that net spending will close the year approximately \$25 million below the original appropriated level.

The Transportation Fund is expected to close Fiscal Year 2015 with a balance of \$162.6 million. This is a reduction to fund balance of \$13.1 million through Fiscal Year 2015 operations. The most significant shortfall is in the Department of Transportation's Rail Operations account related to Metro North costs.

The state posted another month of job growth in November. The Department of Labor's preliminary payroll employment number for November shows the addition of 4,600 positions. The state has posted job gains in nine of the past ten months reversing an earlier trend of inconsistent job additions. Connecticut has regained 93,200 positions or 78.3 percent of the jobs lost to the 2008 recession. Wages in Connecticut are also beginning to show some upward movement after a long period of stagnation. Average private weekly pay in the state was up 6.1 percent in November from the same month last year. Wages outpaced inflation, which rose 1.3 percent in November.

According to a report from the Warren Group released on December 9th, single-family home sales in Connecticut year-to-date thru October of 2014 rose a robust 7 percent from the same period one year ago. October was the seventh month in 2014 that posted year-over-year growth in sales. The median price of a single family home fell 3.4 percent from October of last year moving down to \$241,600 from \$250,000.

At this writing the stock market is posting solid gains on a year-to-date basis. Gross Domestic Product was up 5 percent in the 3rd quarter after posting a strong gain of 4.6 percent in the second quarter. Corporate profits remained positive in the 3rd quarter rising 3.1 percent from the 2nd quarter. This is down from the 8.4 percent 2nd quarter results.

I also issue a Comprehensive Annual Financial Report (CAFR) as an accounting supplement to the budgetary report. The CAFR includes financial statements for all state funds that are prepared in accordance with Generally Accepted Accounting Principles (GAAP). From a balance sheet perspective, the GAAP shortfall or unreserved fund balance in the General Fund was \$1.217 billion as of June 30, 2013. GAAP deficit reduction bonds in the amount of \$598,500,000 were issued in Fiscal Year 2014 to reduce the shortfall.

If you have any questions on this report, please do not hesitate to contact me.

Sincerely,

Kevin Lembo
State Comptroller