

KEVIN LEMBO
STATE COMPTROLLER



MARTHA CARLSON
DEPUTY COMPTROLLER



STATE OF CONNECTICUT
OFFICE *of the* STATE COMPTROLLER
55 Elm Street
Hartford, CT 06106

September 30, 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 the legal financial statements for Fiscal Year 2015. These statements have been prepared in accordance with statutory provisions that were designed to incorporate the expenditure accruals of Generally Accepted Accounting Principles (GAAP) into the budget process.

The General Fund ended Fiscal Year 2015 with a deficit of \$113,168,010, which represents six-tenths of one percent of Fiscal Year 2015 budgeted spending. The increase in the deficit estimate from August is the result of higher than expected expenditure accruals and lower than anticipated revenue accruals, which were partially offset by lower appropriation carry-forward funding and positive fund balance adjustments. The enacted budget also reserved \$12.7 million in Fiscal Year 2015 revenue for Fiscal Year 2016.

The deficit will be eliminated through a transfer from the state's Budget Reserve Fund. As a result of this transfer, the balance in reserve will be reduced from the current level of \$519,169,363 to \$406,001,353. The new Budget Reserve Fund balance is equal to 2.2 percent of net General Fund appropriations for Fiscal Year 2016.

In Fiscal Year 2015, General Fund spending was held to growth of 2.6 percent, or \$439.6 million above the prior fiscal year. Three deficit mitigation plans were implemented during the course of Fiscal Year 2015 totaling \$100 million to address projections of a growing deficit.

In the six fiscal years following the large Fiscal Year 2009 General Fund deficit, spending growth in the General Fund has averaged 2.5 percent per year. This compares to average annual General Fund spending growth of 7.3 percent in the four years leading up to that large deficit.

Twenty-six appropriation line-items in the budget account for 87 percent of General Fund spending. In order to control the growth in General Fund spending during the Fiscal Year 2009 to 2015 period, actual dollar reductions were made over the period in several of these large line-items (comparing spending in Fiscal Year 2009 to spending in Fiscal Year 2015). Some notable reductions between those fiscal years included a cut of \$155.8 million in higher education operating support, a decline of \$148.0 million in state employee payroll expense, and a decrease of \$84.8 million in the Department of Children and Families residential board and care program. During that six year period, the largest dollar increases were an additional \$516.1 million to fund the State Employees Retirement System, an increase of \$498.9 million in Medicaid spending, and \$444.8 million more to fund the Teachers' Retirement system. It is important to note that the vast majority of funding to the retirement systems is for individuals that have already retired. These obligations were incurred over many decades, but were not fully funded. These have now become fixed state costs. Pension reforms have substantially lowered pension costs for new hires.

Some of the spending trends listed above were reversed between Fiscal Year 2014 and Fiscal Year 2015. General Fund spending for Medicaid declined \$103.7 million during the period as federal Medicaid spending increased by 16.4 percent. The state employee General Fund payroll expense grew by \$105.5 million as wage increases that had been eliminated in past years were reinstated and critical positions were filled. Higher education operations also experienced a \$31.5 million increase during Fiscal Year 2015.

General Fund revenue growth has been slow to recover from the 2008 recession. Connecticut did not begin to experience sustained job growth until the middle of calendar year 2014. During Fiscal Year 2015 the state added twenty-seven thousand payroll positions. Connecticut's rate of job growth is now close to the national level of gain. The state's unemployment rate has dropped from a high of 9.5 percent in October of 2010 to 5.3 percent. Despite the growth in employment, wages in Connecticut, as in the nation, remain stagnant. In addition, the overall economy as measured by Gross Domestic Product has not attained a full year growth rate of 3 percent or better since the recession ended.

In Fiscal Year 2015 General Fund revenue grew by just 1.6 percent. Revenue fell \$176.2 million short of original budget estimates. Of the major tax categories, the income tax grew by 5 percent, the sales tax was up 2.5 percent and the corporation tax expanded by 4.2 percent. The payroll component of the income tax, which represents about 60 percent of total income tax receipts, grew by just 2.6 percent in Fiscal Year 2015. This is well below the high of 8.1 percent growth (Fiscal Year 2005) that was experienced in the last economic expansion. Declines were posted in Fiscal Year 2015 in the public service corporation tax, the insurance company tax, the tobacco tax and miscellaneous taxes inclusive of the health provider tax.

Fiscal Year 2015 recorded \$13.9 billion in Fiscal Year 2015 operating activity that fell outside the General Fund. The majority of this activity was in the Special Revenue Funds group. These are funds that have dedicated revenue sources to support their programs. This fund category includes federally supported programs, the operating activities of the universities, and the Transportation Fund. Federal grants grew by 10.6 percent in Fiscal Year 2015 over the prior Fiscal Year. This equates to \$545.8 million in additional federal spending. The largest federal increase was in Medicaid. This caused the special revenue fund group to grow by 9.8 percent to total \$11.5 billion in Fiscal Year 2015.

The Transportation Fund ended Fiscal Year 2015 with a positive fund balance of \$180.1 million. Spending increased by 4.5 percent during Fiscal Year 2015 and totaled \$1.3 billion. Since 2009, Transportation Fund spending has grown by an average of 2.7 percent a year.

Capital project spending grew by 12.5 percent between Fiscal Year 2014 and Fiscal Year 2015 to total \$1.7 billion. Since 2009, the average annual growth in capital spending has been 6.3 percent. This is consistent with growth in the private sector use of debt financing as companies took advantage of historically low interest rates.

I also issue a Comprehensive Annual Financial Report (CAFR) that converts the GAAP budgetary basis to the GAAP financial reporting basis. The CAFR accounts for various non-budgetary financial transactions as well as the budgetary basis transactions. From a CAFR balance sheet prospective, the GAAP shortfall or unassigned fund balance in the General Fund was a negative \$727.2 million as of June 30, 2014. I will report the new unassigned fund balance figure for Fiscal Year 2015 no later than February of 2016 in accordance with SEC requirements.

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

Sincerely,

Kevin Lembo
State Comptroller