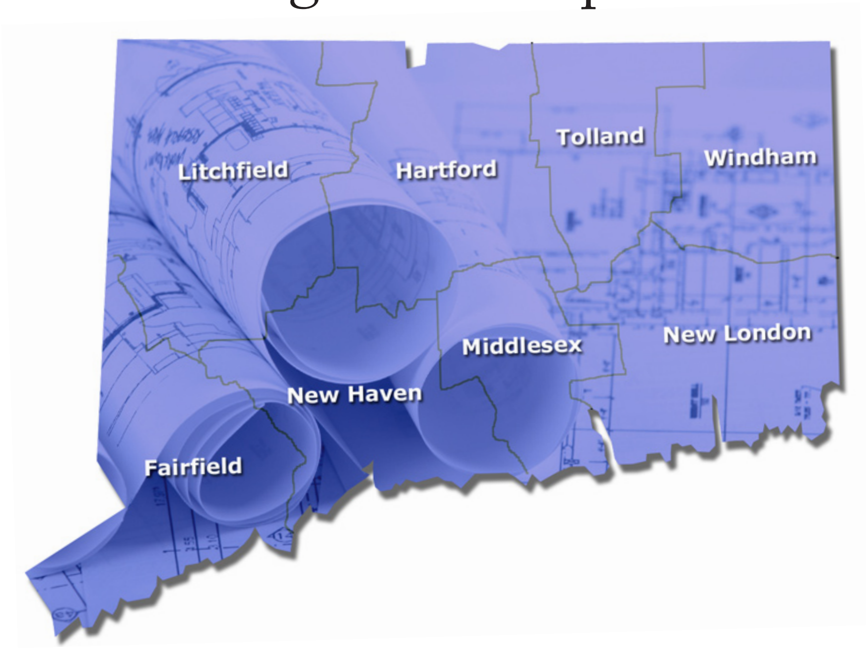
Act Now:

Balance the Budget and Prepare for the Future



In the spirit of the recent awakening of a civically-engaged electorate, we believe that citizens can come together to solve our shared problems. Public-spirited citizens of Connecticut who share our concern for the future and subscribe to the general principles outlined in this two-year budgetary plan are invited to join us.

The authors of this suggested plan are members of a working group of civically-involved citizens convinced that Connecticut can, even in a time of severe fiscal problems, both balance the state budget and lay the foundations for future prosperity. The authors are: Carol Shaw Austad, David Blitz, Leo Canty, Bill Cibes, Shelley Geballe, Jim Horan, Ned Lamont, Matt Nemerson, Paul Petterson and Lyle Wray.

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Executive Summary

In order to secure a prosperous future for all people in Connecticut, we must build an economy that is fully competitive in the global marketplace. During the coming years, we must emphasize investment in the pillars undergirding that competitiveness: innovation, human capital, infrastructure, and the factors that improve the quality of life. And we must make our governments more effective and efficient, focused on achieving results our citizens want.

While we work toward our long-term goals, we must also meet the challenge of an immediate fiscal crisis. There is no panacea to solve our current problems. Instead, hard decisions must be made that employ every available option to balance the state budget while doing no harm to the most vulnerable among us, and preserving the foundations of future prosperity.

No option can be removed from the table. Balanced budget builders cannot start with presumptions that there will be no service cuts, no layoffs, no revenue increases, no payroll modifications or no diminution of the budget reserve fund.

Instead, state leaders – acting on behalf of all of us – must aim to balance a combination of relatively equal contributions from each of three major fiscal buckets:

- Cuts in projected FY10 and FY11 appropriated spending by $700 million or more;
- Reductions in tax expenditures of $700 million or more; and
- Increases in selected taxes and fees by $700 million or less.

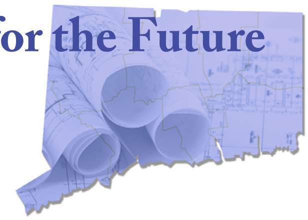
The availability of federal economic stimulus dollars, and prudent use of the rainy day fund, could mean that the part played by each of these three major categories could be less than the stated targets. Specific suggestions for possible actions in each rubric are included in the body of this white paper.

Meanwhile, we must continue counter-cyclical investments in infrastructure that enhances our long-term competitiveness, using both Connecticut capital and federal infrastructure dollars. And we must revamp the way our governments do business, so that they focus on results.

Overall, this plan eliminates the state's structural deficit and balances the budget on a sustainable basis. It shares the burden among all stakeholders; shields the most vulnerable; promotes a smart growth, pro-growth strategy; and protects Connecticut's long-term competitiveness.

With a prudent, constructive, positive approach, we can resolve this crisis and work toward prosperity for all.

Act Now: Balance the Budget <u>and</u> Prepare for the Future



Prosperity for All – A Blueprint for Connecticut's Future presents our recommendations for a long-term vision and a strategic plan to make Connecticut competitive in the future global economy.

But we also recognize that we face the challenge of an immediate fiscal crisis: budget deficits of major magnitude over the next three fiscal years, combined with large unfunded liabilities for retiree pension and health insurance commitments.

The difficulties might lead us to follow the path of least resistance and make decisions that would

- wreak havoc on public services,
- devastate struggling municipalities, and
- render us virtually non-competitive for years to come.

More constructively, we could seize the opportunity to make prudent decisions that would

- address our state's underlying weaknesses by **investing in the foundations for future economic competitiveness,**
- **spare our most vulnerable residents** from the most severe consequences of these difficult times, and
- **fairly share the burden** of the increased taxes that will inevitably be required.

Today's challenges cannot be solved by adhering to the Connecticut tradition of "the land of steady habits." Nor can they be met by an apathetic or uninformed citizenry, nor empty rhetoric, nor self-destructive electoral anger. They cannot be solved by a rainy day fund that is less than one third of the looming deficits, nor can one-shot federal stimulus payments reasonably be expected to close long-term structural operating budget shortfalls.

We must be willing to make the right choices, as well as the tough ones. We must share sacrifice, not merely vent frustration. Most importantly, we need to see these times as transformational, not temporary. Our choices must be about fundamentals, not phantom fixes.

Above all, Connecticut must make a commitment to governmental excellence, based on strategic planning, solid data, benchmarking, regular performance assessment and true accountability for results. Scarce resources must not be squandered. Citizen sacrifice that cannot be avoided must not be abused by old habits of bureaucratic self-preservation.

This is a time to work together, with candor and transparency. We must strive to reach consensus on an unprecedented solution to an unprecedented problem.

We accordingly propose that the Governor and the General Assembly undertake an eight-point program to **balance the budget for FY 2010 and FY 2011**, while at the same time **preserving the state's capacity for future economic competitiveness**.

To close the budget gap in the short-term, there is no silver bullet. What is required is a balanced combination of

- **cuts in appropriated spending**,
- **reductions of tax expenditures,**
- **use of federal economic stimulus dollars, and**
- **judicious revenue increases**,

all in the context of actions that contribute to, rather than compromise, achieving the vision of **prosperity for all**.

Balance the Budget

Immediate Budget Action:

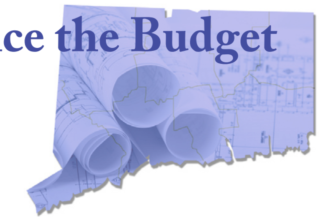
1. Reduce spending by at least $700 million annually.

a. Apply the principles of David Osborne's <u>Price of Government</u> to Connecticut state government. Determine what the "price of government" should be in Connecticut. Then "budget for outcomes" and "set the priorities" of state government. Conduct "strategic program reviews" to decide what programs to keep. "Buy value" and achieve "smarter management." "Reinvent" service delivery to produce lower cost, higher quality solutions by utilizing best practices already tested in other states. Revamp state agency business processes to provide optimum efficiency and effectiveness. Although the "price of government" in Connecticut is already fourth lowest among the fifty states, following Osborne's template can help make further reductions.

b. Initiate and phase in a long-term, "smart spending" program with new approaches to budgetary categories that avoid crippling budget cuts but introduce a path toward necessary change. For example:

1. Adopt a program to emphasize Medicaid home care for elderly patients who would otherwise incur the fiscal and emotional cost of unnecessary nursing home placements. Benefits: Enhanced client well-being and cost savings result from reducing unneeded nursing home care. A cap on the number of nursing home beds may be needed in order to avoid an added layer of service, and hence additional costs.
2. Move non-violent offenders from correctional institutions into appropriate community placements. Benefits: Cost savings result from decreasing the population of overcrowded prisons while providing better transitions back into constructive roles in society for these offenders, reducing recidivism.
3. Enhance community intervention programs that support and preserve families, keeping children at home when safe. Benefits: Cost savings result from reducing unnecessary removal from homes and reducing the need for residential facilities, while enhancing the well-being of families.
4. Encourage municipalities to participate in regionalizing services. Benefits: Cost savings result from the reduction of overhead and elimination of duplication, while providing better service.

Realistically, the elderly Medicaid patients, non-violent offenders and children that could benefit from a smart spending program would not immediately be moved into new service modalities. Hence, the immediate savings would likely be minimal; but over the longer term, focusing on these cost drivers has the potential to achieve significant savings.



c. Re-examine the role of "shadow government" – consultants and outsource vendors – to reduce costs. Contracts should detail specific deliverables, and outcomes should be assessed to ensure that the state gets what it requires. Information about costs should be transparently available to the state and its citizens.

d. Leverage up-front capital from existing energy efficiency and renewable energy funds and other state-supported financial mechanisms to invest in energy-saving projects – like retrofitting electrical fixtures or installing combined heat and power – at state and state-grantee physical facilities. Commensurately reduce appropriations to produce immediate savings for operating deficit reduction.

e. Collaborate with state employees (through SEBAC) to find ways to reduce costs while preserving essential state services and preserving the foundations for the state's long-term economic prosperity. Some immediate goals are to:
   1. Reduce health insurance costs by focusing on prevention services.
   2. Reduce personnel costs through constructive negotiations which modify payroll expenses but save jobs.
   3. Factor in natural attrition (normal retirements and resignations), to the extent it is not already included in the personal services lapse figure.
   4. NOT offer an early retirement program, which defers costs to an already under-funded pension system, loses the expertise of experienced employees and disrupts provision of services.

   Collaboration with workers to identify cost-saving and productivity initiatives has proven extremely helpful in the private sector, which has long used "kaizen" and other "lean" techniques to make business less expensive and more competitive.

f. Until the current fiscal crisis recedes, move spending for "Equipment" from Operating Funds into the capital budget. ($65 million)

2. **Review tax expenditures**, which are "rarely examined," says Osborne, but "offer ripe territory for savings." Increase the transparency of costs and benefits. Conduct a comprehensive review of the $5 billion of tax expenditures in Connecticut to ensure their continued economic and fiscal merit, and their consistency with the long-term vision of the state. Reduce the total by at least $700 million. Among the possibilities are:
   a. Control or cap film tax credits for a savings of $150 - $200 million annually;

   b. Cap "Mixed Use Historic Structure" tax credit for a savings of $40 million annually;

   c. Re-examine other specific corporate business tax credits for economic development which may no longer serve the purpose for which they were intended; perhaps substitute explicit grants for non-specific tax credits;

d. Clothing under $50 ($130 million) offset by a state earned income or low income tax credit ($50 million). This change would also facilitate collection of sales and/or use taxes on Internet and catalog sales.

e. Fuel for heating purposes ($140 million) offset by one-time subsidies for energy-efficient insulation or other rehab;

f. Motion picture leasing or rental ($2.5 million);

g. Motor vehicle parking ($2.5 million);

h. Car washes ($1.0 million);

i. Other miscellaneous tax expenditures (e. g. amusement and recreation services, massage therapist and electrology services, winter boat storage) ($0.7 million).

3. **Wisely use the likely federal counter-cyclical support for state governments.** An estimated $1 billion (+) in SFY 10 and $800 million (+) in SFY 11 of annual operating fund support may be available, depending upon congressionally approved details of a stimulus program, the number of years for which funds will be appropriated and the formulae used to distribute the assistance. The state must quickly determine how such funding can be integrated into a coherent overall package of expenditures to supplement the state's appropriated budget.

   At the present time, it appears that the federal recovery program will provide operating funds for at least:

   a. Medicaid expenditures, at a higher reimbursement rate than the current formula

   b. Financial assistance to elementary and secondary schools to be used for any activity authorized by the Elementary and Secondary Education Act of 1965, the Individuals with Disabilities Act, or the Perkins Career and Technical Education Act of 2006

   c. Financial assistance to public higher education institutions to mitigate the need to raise tuition and fees for in-state students

   d. Grants to elementary and secondary schools to improve and reward improved performance

   e. Special education

   f. Title I programs

g. Public safety and other governmental services

h. Law enforcement assistance

i. Community policing grants

j. Low-income home energy assistance

k. Head Start, and Early Head Start

l. Child Care and Development Block Grants

Other programs may also benefit.

While the state may have some flexibility in using these funds, many programs may require that current state funding be supplemented, but not supplanted, and that there must be "maintenance of effort" at a specified level. In any case, because these are "one-shot" revenues, the state must ensure that it does not rely upon them to the extent that it creates a structural imbalance in its operating budgets after the next one or two fiscal years when these stimulus funds are no longer available.

In addition to supporting the economic recovery act which provides these funds, our congressional delegation should also press Congress to authorize states to collect sales and use taxes on catalog and Internet sales – obviating the need for states to join an interstate compact to do so.

4. **Raise revenues** ($700 million or less) at the state level to avoid cuts in state grants to municipalities, which would shift costs to towns and cities where property taxes would increase. Permanent revenue increases should be limited to the minimum required to maintain a structural balanced budget after the fiscal crisis is over.
   a. Join Maine and other states in imposing a deposit on plastic water bottles, and escheat all unclaimed deposits, including this new one

   b. Collect sales and/or use tax on Internet sales (this also benefits instate merchants currently at a cyber-disadvantage to out-of-state retailers) (See www.e-fairness.org)

   c. Require that every personal income tax filing be accompanied by a use tax form, with a "suggested" use tax schedule in the instructions that shows – by income tax level – the "appropriate" use tax if there are no items costing more than $1,000

   d. Increase the cigarette tax (offset by expenses for smoking cessation programs)

e. Collect sales tax on snack or "junk" food

f. Return the gas tax to 1997 levels: add at least 15 cents to the current level, perhaps phased in

g. Extend sales tax to additional services

h. Increase fees by adjusting all current fees and charges to account for inflation since last adjusted, or to the average national level of fee and service charges; and provide a framework for allowable fees and service charges by localities.

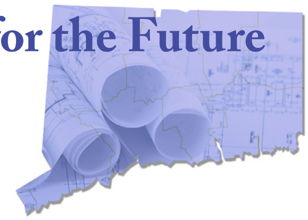
i. Require registration (at a modest fee) of out-of-state partners/owners of LLCs, LLPs, and S corporations, or the like, to enable DRS to determine if these persons are paying personal income tax to the state

j. Convene a Business Tax Commission to review equity and fairness of the corporation tax and its various aspects; follow its recommendations to increase revenue while enhancing equity – without hurting Connecticut's competitive position

k. As a last resort, increase the income tax, fairly and equitably, by up to 1/2 percentage point (together with an inflationary adjustment of exemptions and credits), to be used in the long-term for property tax reform. (The adverse impact of the increase is minimized by the ability to deduct state income taxes on federal tax returns.)

5. **Use a portion of the Rainy Day Fund.** It's raining.
Nevertheless, remember that use of the Rainy Day Fund is a "one-shot" revenue source. In the long run, there must be a structural balance between ongoing revenues and expenditures.

Prepare for the Future



Actions with longer-term consequences:

6. Take immediate steps to set Connecticut government on a path to strategic planning and effective government.

The Governor and the General Assembly should immediately convene one or more summits with the following groups in order to form new, more equal relationships focused on the common good rather than on a constituency's gain. These groups would include:

- The state's mayors, first selectmen and regional leaders to rebalance the relationship between state and local government.
- The state's non-profit and philanthropic leaders to harness their innovation and cost effectiveness in meeting public needs.
- Leaders of the state's global businesses and leading professional service firms to tap their expertise in making rapid change in large institutions.

These summits should culminate in specific policy recommendations, and in a commitment to bring Connecticut to the top tier of high performing state and municipal performance in five years. A good guide for action is The Price of Government, by David Osborne and Peter Hutchinson.

- Establish a Strategic Planning and Management Council that establishes long term goals for the State and monitors each agency's implementation actions;
- Establish a Workforce Excellence Commission whose mission is to recommend a modernization of state workforce work rules, compensation benefits and program costs. Goal: A 10% reduction in the overall cost of delivery of state services.
- Re-create an office that provides independently verified, impartial data relevant to enactment of public policy and outcomes assessment
- Restructure the Office of Policy and Management to provide excellent support of strategic planning, goal setting and performance measurements.

7. Develop a state capital plan – perhaps with the assistance of a Capital Investment Advisory Board – that rolls up existing LoCIP and state plans (e.g. Department of Public Works, higher education) and adds ConnDOT to a five year capital plan that sets multi-year state capital spending priorities in key areas that affect economic competitiveness (e.g. education, transportation, R&D). All sources of funds (state bond financing, tax incentives and federal financing) should be organized by priority areas. For example, Massachusetts has fourteen capital plan priority areas. Enact a law requiring state capital plans on a regular basis (as does recent state law in Kentucky).

Prepare for the Future

Even before the state capital plan is put in place:

- Aggressively use state **bonding for current infrastructure projects** as a counter-cyclical mechanism.

- Wisely use **federal Infrastructure** and **Green Energy funds**.

Aggressively use state bonding for current infrastructure projects as a counter-cyclical mechanism.
State and local governments make up 12% of the national economy and need to participate in the economic recovery. The state should immediately allocate bonding for those infrastructure projects aligned with long-range strategic goals which have already been authorized and for which plans have been drawn, as it recently did for bridge repair and road repaving. And the state should make available bonding that has already been allocated. Investing bond dollars now is a counter-cyclical response to the current recession. Moving forward now provides jobs for currently under-employed workers, and takes advantage of currently downward-trending prices for durable goods and building materials. A spike in income and sales creates revenue for the state. And the payment of interest and principal on bonds comes later in the economic cycle when times are better.

a. UConn 2000

b. CSU 2020

c. Community Colleges

d. Supportive housing (Next Steps)

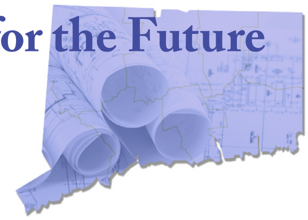
e. Other authorized projects that are ready to go.

Wisely use federal Infrastructure and Green Energy funds.
Immediately develop a prioritized list of ready-to-go projects. As President Obama has said, **if states do not act quickly to invest the money in infrastructure projects, they will lose it**.

Congress may direct a significant percentage of such infrastructure aid directly to municipalities and regions, (if they have legitimate "shovel-ready" projects and not "bridges to nowhere"), so they too should prioritize their infrastructure needs.

As with economic stimulus operating funds, the state must develop a coherent overall plan in which these infrastructure dollars complement the state's own capital program.

Prepare for the Future



At present, the recovery act appears likely to include significant funding for:

a. Highway infrastructure investment, with funds distributed on the basis of the FY 2009 formula, and with no state matching fund requirement

b. Capital investment for transit, with no state matching fund requirement

c. Elementary and secondary school modernization, renovation and repair (but not maintenance), with at least 25% of the funds to be used for energy-saving purposes

d. Modernization, renovation and repair (not maintenance) of higher education facilities, with at least 25% of the funds to be used for energy-saving purposes

e. Capital activities of public housing agencies

f. Energy retrofit projects for elderly, disabled, and Section 8 assisted housing

g. Weatherization assistance

h. Block grants for energy efficiency

i. Neighborhood stabilization through redevelopment of abandoned and foreclosed homes

j. Clean water capital projects

k. Drinking water capital projects

Again, this list is not all-inclusive.

The state should consider the following candidates for some portion of infrastructure funding under the above categories:

Transportation

a. Purchase of Metro North rail cars

b. Construction of the New Haven rail car repair facility

c. Q Bridge rebuild

d. Moses Wheeler Bridge rebuild

e. Danbury rail line rehab

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f. Elements of the New Haven – Hartford – Springfield commuter line (with connector to Bradley Airport)

g. Elements of the Hartford-New Britain busway, or a Hartford-Waterbury rail line, such as the Flatbush Avenue overpass

Housing

a. Preservation and revitalization of existing public housing, and recapitalization and repair of privately owned deed-restricted affordable housing

b. Creation of homeownership opportunities in cities through purchase, rehab, and reselling foreclosed homes for affordable prices

c. Energy-efficient rehabilitation of older residential dwellings, to quickly make jobs available for building-trades' workers and provide an almost immediate return on investment

Other

a. Clean water capital projects

b. Elementary and secondary school modernization, renovation and repair

c. Higher education facility modernization, renovation and repair.

Where federal requirements permit, the state should use for innovative purposes – within the bounds of the state capital plan – some state capital dollars that would otherwise have been allocated for projects that qualify for these infrastructure stimulus funds, such as:

- Transit projects, especially those critical to creating high-speed rail lines for connectivity of all our residents, for which sufficient federal funding is not available
- Remediation of brownfields to a residential standard in smart growth locations
- Capital incentives to towns that create affordable and market-rate housing under the HomeConnecticut plan
- Creation of affordable and supportive rental housing in smart growth locations
- Transit-oriented, energy-efficient mixed-use development, including housing

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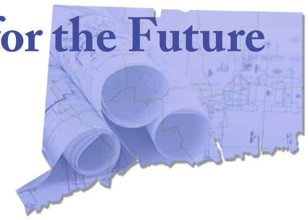

8. **Maintain support for – or at least do no harm to – programs that lead to the achievement of long-term strategic goals.** In making hard decisions about expenditures from the General Fund during this period of fiscal constraint, the Governor and the General Assembly should strive for this. To set the state on the road to prosperity, they should also consider making small additional investments in some critical programs, and establishing some new standards that will have no immediate cost but will set in place the foundation for future progress. The following are important action items, by category:

Do no harm

1. Maintain existing support for priority economic clusters: financial services, biotech, information technology and software, and precision manufacturing.
2. Maintain existing investments in early childhood education, including Care4Kids child care subsidies.
3. Preserve investments in K-12 education. Severe cuts will drive up property taxes and harm services in all Connecticut towns. But especially, do not jeopardize demonstrated progress in urban schools.
4. Preserve supportive operating funding, and need-based student aid, for higher education – at "current-services" levels. With unemployment rising, now is an ideal time for folks to head to (or back to) colleges and universities to get more education and training.
5. Continue state grants to towns, under the HomeConnecticut plan, to plan for higher density zoning in appropriate locations for a combination of market-rate and affordable housing (operating funds), and to incent zoning changes (capital funds).
6. Release already approved funding for the third round of Next Steps supportive housing.
7. Ensure that regional programs do not exacerbate urban disinvestment.
8. Avoid investments and programs that increase vehicle miles traveled.

Foundations for the future

1. Establish the requirement that all elementary school teachers must be qualified to teach reading.
2. Align curricula between secondary schools, community colleges and universities to create a seamless transition.
3. Adopt cost-effective models of health care in both the public and private sectors (e.g., Pitney Bowes, state employees) which contain costs and focus on prevention, for both employers and residents.
4. Develop and implement a statewide strategic plan (supplemented by an appropriate capital plan) for a balanced transportation system, coordinated with the statewide plan for economic development and other statewide plans.

Prepare for the Future

5. Provide adequate dedicated revenues to fund transportation infrastructure: return to at least the 1997 level of the gas tax.
6. Encourage urban investment, and discourage urban disinvestment.
7. Codify a definition of "smart growth" and/or "responsible growth" and its principles in statute, to guide all state investments and regulations.
8. Create a public/private state planning structure, to enhance all state plans but especially the Conservation and Development Policies Plan, which should be given increased applicability.
9. Enhance inter-agency cooperation and collaboration to replace bureaucratic "silos" that frustrate integrated actions.
10. Maintain the discipline to keep a focus on achieving longer-term goals (and not get distracted by the latest headlines).
11. Develop the internal capacity to track and publicly report on our current public investments – both appropriations and tax expenditures – and their financial and non-financial returns.

Small additional investments

1. Provide necessary faculty in critical workforce areas at the community college and university level.
2. Provide outreach/enrollment assistance to enroll more eligible persons in HUSKY, and ensure that enrollees have timely access to needed health care
3. Build on the recent national grant to CRCOG, and the work of the small business clinic at Yale Law School, to create model smart growth zoning codes that towns can adopt.
4. Support maximizing usage of the federal EITC and other federally-funded benefit programs, which encourage workforce participation and help low-income workers stabilize their lives.

The Governor and General Assembly should also consider:

- Increasing the upper limit of the Budget Reserve Fund to 15% of General Fund appropriations.
- Adjusting the statutory spending cap to make the budget base the "allowable" state spending in the previous year, instead of the "actual" spending.
- Including capital gains as part of the income measure for the spending cap.
- Reducing the number of years considered in the measure of the average change in personal income which determines the spending cap.

Conclusion

We all have a stake in our state's prosperity. We believe that when we work together we can positively affect our state's economy and our well-being.

The coalition of individuals and groups that developed this report has many different backgrounds and interests. The particular beliefs, commitments and agendas of its members may differ. But all of its members believe that the state needs to Act Now to balance the budget and prepare for a future that offers **Prosperity for All**.

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