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The Governor's Budget Proposal: Revenues, Fixed Costs, and Municipal Aid

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For more than 100 days, Connecticut has operated without a budget, and its children and families have suffered the consequences. As policymakers continue to craft a roadmap for the next two years, Governor Malloy has released a new budget proposal, highlighting some of the major points of contention in recent negotiations.

Policymakers differ most greatly in three areas: revenue, fixed costs, and municipal aid. How they resolve these differences will determine the extent to which Connecticut prioritizes a sustainable budget, growing economy, and equitable society. In this brief, we describe how the Governor's proposal addresses these concerns, how his policies compare to other recently released proposals, and how they would impact children and families.

Revenue

Connecticut's Earned Income Tax Credit (EITC) is one of the state's most effective tools for combating poverty, helping nearly 200,000 households make ends meet in 2015.[i] Despite these benefits, Governor Malloy's proposal will cut the state EITC to 23 percent of the federal credit, raising taxes for low-income individuals by $35 million per year. On average, these individuals make less than $20,000 annually.[ii] Increasing their taxes would place even more obstacles in front of parents trying to provide food, shelter, and financial security for their children.

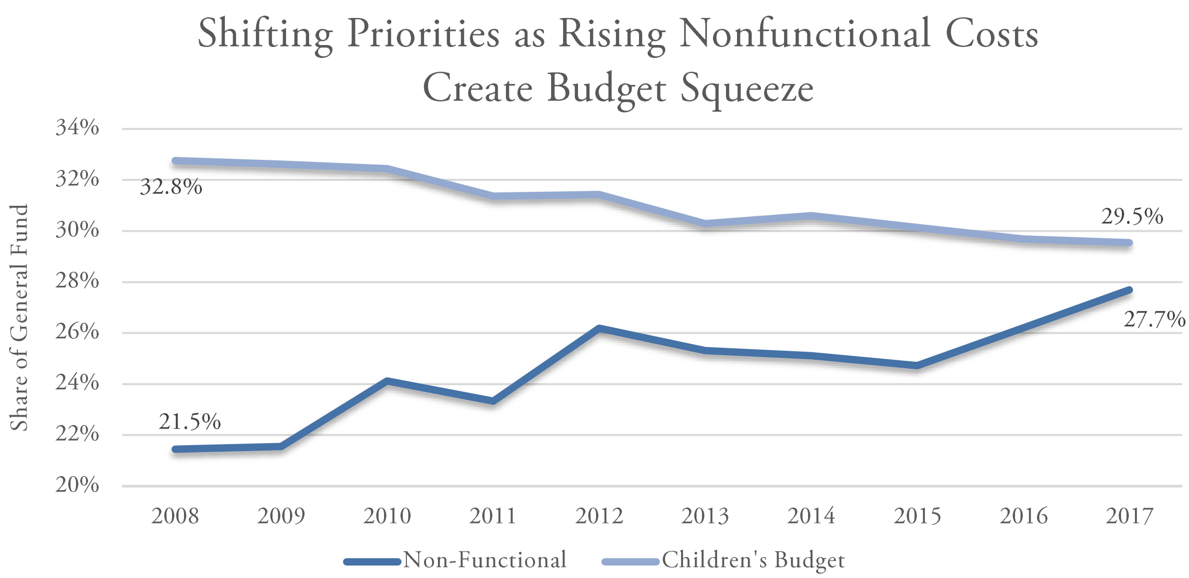
Democrats would cut the state EITC to 25 percent of the federal credit, a $25 million per year tax increase. Republicans would implement a graduated EITC, cutting the credit to just 5 percent for claimants with no children and up to 25 percent for those with three or more children.[iii] This would raise workers' taxes by $75 million per year.

Fixed Costs

Over the last nine years, the share of the budget devoted to children has decreased while the share devoted to Connecticut's pension liabilities for teachers and state employees has increased. Without structural reform, these costs threaten to consume an even larger share of the budget over the coming decades, crowding out direct supports for children and families.

This July, legislators approved a deal between the state government and state employee union that actuaries estimate will save $24 billion over the next twenty years.[iv] However, teachers' retirement fund contributions — another fixed cost — are predicted to increase by $5 billion (500%) by 2032.[v]

The Governor attempts to address teacher pensions' rising costs by requiring municipalities to pay half of the teacher retirement system's "normal cost," or the amount necessary to pay for the pensions of teachers currently teaching. Currently, the state pays for the entirety of teachers' pensions, even though municipal school boards set teacher salaries, thereby determining teachers' pensions. This effectively subsidizes wealthy school districts, which can afford higher salaries for their teachers, who then earn more generous pensions. Sharing this cost with municipalities allows them to internalize part of the cost that they shift onto the state.



Source: CT Voices analysis of budget trends.

In their last budget, recently vetoed by the Governor, Republicans proposed more modest changes to teacher pensions, requiring teachers to contribute an additional two percent of their salary to their pensions by Fiscal Year 2019 (an additional $95 million over the biennium).[vi] Republicans also found further savings from state employees. Part of the July deal extended state employees' negotiated pay and benefits package through Fiscal Year 2027 (FY 2027). The Republicans' budget assumed that the state will change state employees' compensation after 2027, then lowered today's contributions to pay these assumed less generous benefits. This yet again pushes the day of reckoning for unfunded liabilities further down the road.

Municipal Grants

Connecticut's municipalities are its centers of growth, innovation, and learning, and the state's support for its cities towns are essential to their success. In FY 2017, Connecticut provided municipalities with $2.6 billion in such "statutory formula aid," funding services from education to road repair.[vii] Ensuring that the state provides this support in an equitable and adequate manner is essential to building thriving communities.

Lawmakers have been embroiled in protracted negotiations on how to distribute municipal grants. One of the main points of contention is the Education Cost Sharing (ECS) formula, the state's program to equalize education funding among towns. Although the Governor's proposal would reduce ECS funding by $124 million (6 percent) overall, it would protect funding for the lowest-achieving districts. In their last proposal, Republicans would have increased ECS funding by $68 million but held the lowest-achieving districts' share of statutory formula aid constant.[viii]

Parallel to the ECS formula, Payment In Lieu of Taxes (PILOT) grants compensate municipalities for state laws that forbid them from taxing certain kinds of property, including state buildings, private universities, and hospitals. However, the legislature has never fully funded PILOT, meaning that communities with the highest concentrations of tax-exempt property—often low-income cities and towns—have shouldered the burden of hosting regional services without adequate compensation from the state. The Governor combines PILOT and some other municipal grants into a single Municipal Assistance Grant, protecting this funding for 33 of the most disadvantaged cities and towns.[ix]

Conclusion

The solution to Connecticut's budget woes lies not with tax hikes for working families or short-term revenue tweaks. Rather, we need a new approach, one grounded in a commitment to economic growth, shared prosperity, and equitable opportunity for every child in our state. Doing so will require bold action, fearing not taxes or structural forms but rather the lost potential of our children, families, and communities. As the General Assembly heads for what could be the final budget vote of this session, **now is the time to call your legislators** and voice your support for a balanced budget approach that prioritizes children and families.

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[i] Thomas, D., & Noonan, R. (2017, May). Connecticut's Earned Income Tax Credit (EITC) (Issue brief). Retrieved October 19, 2017, from Connecticut Voices for Children website: http://www.ctvoices.org/sites/default/files/EITC%20Brief%20vFINAL.pdf.

[ii] *Ibid.*

[iii] Credits for claimants with one child would be 10 percent of the federal credit while those for claimants with two children would be 15 percent of the federal credit.

[iv] Office of Governor Dannel P. Malloy. (2017, June 6). Gov. Malloy: Actuarial Analysis Affirms Billions in Taxpayer Dollars Will be Saved by Adopting Framework Reached With State Employee Unions [Press release]. Retrieved October 19, 2017, from http://portal.ct.gov/Office-of-the-Governor/Press-Room/Press-Releases/2017/06-2017/Gov-Malloy-Actuarial-Analysis-Affirms-Billions-in-Taxpayer-Dollars-Will-be-Saved.

[v] Aubry, J., & Munnell, A. (2015, November). Final Report on Connecticut's State Employees Retirement System and Teachers' Retirement System (Issue brief). Retrieved October 19, 2017, from Center for Retirement Research at Boston College website: http://crr.bc.edu/wp-content/uploads/2015/11/Final-Report-on-CT-SERS-and-TRS_November-2015.pdf, page 41

[vi] Office of Fiscal Management (2017, October). An Act Providing for the Continued Operation of Essential Functions of the State (LCO 10072). Retrieved October 19, 2017 from Connecticut General Assembly website: https://www.cga.ct.gov/2017/fna/2017HB-07501-R00LCO10072-FNA.htm

[vii] Malloy, D. (2017, October). Connecticut Revised Budget Proposal for the FY 2018 - FY 2019 Biennium (Rep.). Retrieved October 19, 2017, from Office of Governor Dannel P. Malloy website: http://www.ct.gov/opm/lib/opm/Budget/2018_2019_Biennial_Budget/GovMalloyOctoberBudget__10-16-2017.pdf, page 49

[viii] Thomas, J. R. (2017, September 26). State Education Funding to be a Battleground in Budget Dispute. Retrieved October 19, 2017, from https://ctmirror.org/2017/09/20/state-education-funding-to-be-a-battleground-in-budget-dispute/

[ix] More specifically, the Governor combines the Mashantucket Pequot/Mohegan Fund grant, State Owned PILOT, Private College and Hospital PILOT, MRSF: Revenue Sharing Grant, and MRSF: Additional Payment in Lieu of Taxes. He then holds these grants for the 30 Alliance District towns and 3 soon-to-be Alliance District towns (Groton, Thompson, and Torrington) at FY 17 levels after accounting for teacher pension contributions. Finally, the Governor prorates the leftover money for the remaining towns proportionally according to their allocation under the Democrats' most recent budget (LCO 10069).