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Treasurer of the State of Connecticut
SUBMITTED TO THE APPROPRIATIONS COMMITTEE
FEBRUARY 16, 2016

Good afternoon, Senator Bye, Representative Walker, and all of the members of the Appropriations Committee. Thank you for the opportunity to submit testimony concerning Governor Malloy's proposed midterm budget adjustments for Fiscal Year 2017, for both the Office of the Treasurer and for debt service.

Treasury's Budget

As it concerns the Treasury's general fund budget, I well understand that in this environment, there are no sacred cows. We accept that cuts need to be made across the board.

The Governor's budget proposal would reduce our general fund budget for FY17 by $290,552, a portion of which is attributable to annualized FY16 lapses. What is of great concern is the shifting of estimated fringe benefits of approximately $1.2M into a block grant and including it in the Treasury's general fund budget. Although this is simply an estimate from the Office of Policy & Management, it appears to shift the risk of higher than estimated actual fringe benefits onto the Treasury. Given the lack of flexibility caused by the reductions in the FY17 general fund budget, absorbing any additional costs would be a challenge and could potentially weaken the Treasury's core functions.

Debt Service Budget

The Governor proposed a $10 million increase in the general fund debt service budget as a midterm budget adjustment for FY17. We agree with this adjustment, given that it reflects the increased size of the next UConn bond sale from $200 million to $300 million to support higher capital spending levels for University improvements.

With this adjustment, the difference between the Treasury's latest general fund debt service estimates and the Governor's proposed adjusted budget for FY17 is $74.3 million. The Treasury is not the only one concerned about the adequacy of next fiscal year's debt service budget. I understand that the Office of Fiscal Analysis projects that at least $51M may need to be added to this budget for FY 17.

The primary source of the difference in the general fund debt service is the projection of bond premium, funds received at the closing of the bond sale that investors provide up front in exchange for a higher coupon rate on the bonds. In this market of low interest rates, many investors seek this bond structure. For the General Obligation bonding program only, these bond premiums are used to fund interest payments, creating short-term budget savings.

For the first time ever, my office budgets bond premium but at lower levels than the Governor included in his proposed budget for the 2016/17 biennium, which the Legislature adopted with only minor changes. Actual bond premiums on bonds issued so far this fiscal year have come in very close to the Treasury's estimates, exceeding them by only $6.4M, but are lower than the amount included in the adopted budget. This is the reason the Deficiency Bill for the current fiscal year already includes a $35M adjustment for general fund debt service.

Moreover, it supports my warnings last year that the debt service budget that passed with bond premiums budgeted could be inadequate. In other words, this deficiency, for the 2016/2017 biennium was not created by the amount of bond premiums that actually came in, but rather was caused by OPM, and subsequently the legislature, adopting an overly aggressive approach to projecting the use of bond premiums to help fund the debt service budget for FY 2016.

Make no mistake: the Connecticut Treasury's tradition of working tenaciously and successfully to find responsible ways to help address our State's fiscal challenges will continue unabated. However, when it comes to structuring bond sales, my decisions will be guided on what is in the best interest of current and future taxpayers. This means that for the General Obligation bonding program, we will look carefully for buyers of lower coupon bonds when favorable market conditions warrant such consideration, as we've always done, and not just sell all bonds at a premium to bring in as much up-front budget savings as possible. To do otherwise would come at the expense of delaying the inevitable -- higher debt service down the road.

The prudent issuance of debt by the Treasury and continued low interest rates may provide additional relief to the budget, but may not be able to fully close the gap. An additional adjustment to the general fund debt service budget for FY 17 is therefore advisable. Failure to do so may result in the need for another deficiency bill to fund debt service, as is required for the current fiscal year.

As for the **Special Transportation Fund**, we are in agreement with the Governor's proposed adjustments to the debt service budget.

Thank you for the opportunity to offer input on this budget process. I would be happy to take any questions that you may have.