Spending Cap Commission
Monday, September 26, 2016
Meeting Notes

Attendees:

Commission Co-Chairperson William Cibes, Commission Co-Chairperson Patricia Widlitz (by telephone), Suzanne Bates, Rep. Jeff Berger, Sen. Beth Bye (by telephone), Sen. Steve Cassano, Rep. Christopher Davis, Robert Frankel (by telephone), Roberto Hunter, Sen. Rob Kane, Sen. Michael McLachlan (by telephone), Lori Pelletier, Richard Porth, Ellen Shemitz, Bart Shuldman, Rep. Richard Smith (by telephone), Rep. Jonathan Steinberg, Ron Van Winkle, Rep. Melissa Ziobron

Staff:

Susan Keane, Administrator
Amanda Zabel, Appropriations Committee Clerk

Guests:

Michael Murphy, Office of Fiscal Analysis (OFA)
Chris Wetzel, OFA
Holly Williams, OFA
Rob Wysock, OFA

Call to Order

The meeting was called to order by Chairperson Cibes.

Acceptance of the September 19 Meeting Notes

Chairperson Cibes asked for a motion to accept the September 19 meeting notes. The motion was made by Chairperson Widlitz, seconded by Mr. Hunter. Seeing no further discussion, the meeting notes were accepted by voice vote.

Discussion of Potential Items to be excluded from "General Budget Expenditures"

With regard to the "menu" of items to be considered, Chairperson Cibes remarked that Chairperson Widlitz and he intended for there to be a thorough discussion of the items by members, with the opportunity to determine the need for further explanation or explication at future meetings.

Chairperson Cibes opened the discussion on expenditures for the payment of bonds or notes. At the request of Rep. Ziobron, Chairperson Cibes shared his thoughts on the framework to be used for the discussion. He cited Jim Smith's comments of September 7 - "The constitutional amendment envisioned that only debt service was to be exempted, since placing debt service under the cap could unsettle the credit markets, raise the state's cost of borrowing and possibly lead the state to postpone needed infrastructure improvements." He added that Mr. Smith had remarked that no matter the subject of the bonds or notes, debt service should be exempt from the spending cap. He stated that he shared that opinion.

Chairperson Widlitz remarked that she concurred with Mr. Smith and Chairperson Cibes' opinions. She added that she did not favor restricting the legislature's ability to make investments in infrastructure and economic development, and she supported the current language of the Constitutional amendment.

The topic was further discussed by Ms. Shemitz, Mr. Shuldman, Mr. Van Winkle, Rep. Davis and Rep. Steinberg.

The commission next discussed "bond premiums". Sen. McLachlan shared his thoughts regarding including bond premiums under the spending cap.

Mr. Van Winkle recommended that bond premiums be used only for the payment of the debt service of the state of CT, which is $2.6 billion.

Mr. Hunter referenced a letter sent to Sen. McLachlan by Sarah Sanders, Deputy State Treasurer, which indicated that the Treasurer's Office does use bond premiums in the manner suggested by Mr. Van Winkle. He further shared that Ms. Sanders had suggested that bond premiums might be more effectively used by allocating those proceeds for capital projects.

The issue was discussed by several members. Mr. Van Winkle explained the bond premium process, while Mr. Shuldman and Sen. Kane expressed their concerns regarding bond premiums and shared their thoughts in support of putting limitations on the use of bond premiums to pay for debt service only.

In response to Ms. Bates' question regarding the treatment of bond premiums in the budget process, Rep. Davis commented that they are dealt with on the appropriations side. He expressed his concern regarding the use of bond premiums to offset appropriations for other items.

Michael Murphy from OFA provided background on bond premiums as they relate to the appropriations process. He remarked that they are viewed as a budget balancing tool, rather than a spending cap issue.

Chairperson Cibes asked Mr. Murphy to provide the statutory citation regarding the use of bond premiums for debt service. In addition, he requested that Mr. Murphy provide a written history of the use of bond funds.

Chairperson Cibes informed members that he will send them a copy of Deputy State Treasurer Sanders' letter, as well as links to CT Mirror articles on bond premiums.

Mr. Shuldman, Mr. Van Winkle, Mr. Hunter and Ms. Bates further discussed the bond premium process.

In conclusion, Chairperson Cibes remarked that while the discussion of bond premiums was fruitful, it is more of a balanced budget issue, rather than a spending cap definition issue. Mr. Hunter concurred.

Chairperson Cibes moved to a discussion of "expenditures for the payment of other evidences of indebtedness". He remarked that the Constitutional amendment states that "general budget expenditures shall not include expenditures for the payment of bonds, notes or other evidences of indebtedness", and that the statutory language does not define "other evidences of indebtedness". He reminded members that Public Act 15-244 included language for the 2016-17 biennium that allows for "evidences of indebtedness" to include the portion of the annual required contribution (ARC) representing the unfunded liability of (1) any retirement system or alternative retirement program administered by the State Employees Retirement Commission, or (2) the Teachers' Retirement System (TRS). He stated that the question before the commission is whether or not to adopt the language of PA 15-244 or to adopt some other terminology.

Rep. Smith commented that the state must address its pension debt and make it a part of the spending cap.

Chairperson Cibes remarked that he believes commission members are in agreement that the pension debt must be paid. He shared that he sees the question as being whether the pension debts are more likely to be paid if they are under the cap or outside the cap. Further, he stated that in many years prior to 2014 that state did not make its annually required contribution because other expenditures crowded out those payments. In addition, he stated that he believes that pension obligation payments need to be structured in such a way that it raises the likelihood that the payments will be made; however, he sees the creation of such a mechanism as the role of the Governor and legislature, not as part of defining the spending cap.

The issues regarding the treatment of unfunded pension liabilities were discussed extensively by commission members. Ms. Pelletier spoke of the agreement reached between state employees and former Governor Rowland and legislators regarding pension contributions and the consequences of that action.

Mr. Van Winkle raised the issue of how to treat the costs of other postemployment benefits (OPEB) under the spending cap. He stated that the commission needed information on those costs. He shared that those entities that follow GASB rules must list OPEB costs on their balance sheets.

Chairperson Cibes agreed that OPEB should be considered and that additional information was needed. He pointed out that the post-employment benefits commission created by Governor Rell addressed OPEB. He also recommended the pension system reports by the Boston College Center for Retirement Research and Comptroller Lembo as good resources regarding pension funding issues.

Mr. Hunter recommended that the commission ask OPM Secretary Barnes and Comptroller Lembo to address the commission on pension funding issues.

Members discussed a potential recommendation regarding the development of a structured, phased-in process for dealing with the unfunded pension liabilities under the spending cap over a number of years.

With respect to PA 15-244 (Section 35), Rep. Ziobron asked OFA staff to state the amount of the unfunded liability.

Chairperson Cibes replied that OPM had provided that number - $1,828,000,000 in FY 16 and $1,890,000,000 in FY 17. He added that OFA may have projections for the out years.

Holly Williams, OFA analyst, shared that there is a statutory requirement (CSG 5-156a) for the state to pay the amount annually certified. She added that any modifications to that payment must be agreed to by the state and the State Employees' Bargaining Agent Coalition (SEBAC). In response to Rep. Ziobron's questions, Ms. Williams replied that the unfunded liability in SERS is $1.2 billion. She will forward the amounts for the Teachers' Retirement and Judges Retirement Systems to commission members following the meeting.

Chris Wetzel, OFA analyst, explained the impact of Section 35 of PA 15-244 on the spending cap. He stated that adoption of the language provided $102 million in "room" under the spending cap.

Chairperson Cibes asked OFA staff to provide the responses they gave today in writing for distribution to commission members.

Mr. Porth expressed his thoughts regarding the final recommendations to be presented to the legislature. He remarked that however heartfelt members' positions may be on the issues being considered, it is important for the commission to issue recommendations that will pass in the legislature.

Chairperson Cibes commented that beyond the recommendations to be developed by the commission, there are other questions that may need to be addressed by other entities that are outside the purview of the commission. He identified several issues – discount rates, using a current level percent of payroll versus a level dollar method of amortization, whether the funding of pensions for new employees should be a continuation of a defined benefit plan or a a defined contribution plan. He cautioned members that the commission should not try to deal with those matters.

Members discussed timing issues and members' availability for the remainder of the day. It was agreed that the October 5 meeting would be scheduled earlier in the day to allow for presentations by OPM and the Comptroller's Office and discussion of items not addressed at today's meeting.

Chairperson Cibes recommended that members look at the Comptroller's pension system report and the Center for Retirement Research report, as both reports offer suggestions for how a phase-in of payments on the unfunded liabilities might be structured and the impact it would have on avoiding perpetual increases in unfunded pension liabilities. He remarked that this information would be more for background than resolution of the commission's recommendations.

Mr. Shuldman sought clarification from OFA on various aspects of the pension payment process, including agreements between SEBAC and the administration on reducing pension contributions. In addition, he asked Ms. Williams about the amount of contributions being made and if those amounts were determined using a discount rate.

Ms. Williams responded that the budgeted amount for the contributions is based on what the actuaries have determined is required for both the normal costs and the unfunded liabilities. She confirmed that discount rates are used in the calculations. She added that in addition to the agreements between the state and SEBAC, there are a number of other factors that have affected the unfunded liability, which are outlined in the Center for Retirement Research report.

Chairperson Cibes commented that he believes that the unfunded liability payments were taken outside the spending cap over the last two fiscal years due to the radical increases in the costs, based on actuarial projections. Further, he believes that if the current funding system remains in place, there will be steep increases in the costs of the unfunded liabilities, which raises the question of whether the expenditures for the unfunded liabilities should be appropriated under the spending cap.

Chairperson Cibes asked OFA staff to provide charts regarding 1) the total unfunded accrued liability – past and projected – on an annual basis; 2) the ARC payments, broken out by the normal costs and the unfunded liabilities; and 3) an assessment of the scenarios laid out in the Center for Retirement Research study and the Comptroller's report on pension funding reform.

In response to questions posed by Ms. Bates regarding factors related to the growth of the unfunded liabilities, Ms. Williams stated that she will provide to members a memo on the historical funding of the ARC, including points in time when the ARC was not met and the reasons it was not met.

Speaking to the issue of including the unfunded liabilities as an evidence of indebtedness, Chairperson Cibes spoke to decision by the state to issue $2 billion in bonds to fund part of the Teachers' Retirement System unfunded liability. He shared his belief that in making that decision the state equated the bonding with an evidence of indebtedness. He noted that one of the Comptroller’s suggestions is to issue a small pension obligation bond for the State Employees’ Retirement System that could include the same kind of bond covenant as was included in the TRS bonding – that the state must fund the ARC every year.

Regarding the October 5 meeting, Chairperson Widlitz suggested an 11 am start time.

Chairperson Cibes encouraged members to read the pension studies that have been provided, adding that several members have remarked how helpful they have proven in understanding the pension system issues.

Adjournment

Seeing no further discussion, Chairperson Cibes adjourned the meeting at 12:45 pm.

Respectfully submitted,

Susan Keane

Administrator