Lottery Transfer

Concepts Explored

The Commission heard from several speakers who addressed the potential for the Connecticut State Lottery to serve as a vehicle for improving the funding status of the TRS. The Connecticut Lottery is a quasi-public asset valued at approximately $5 billion and generates approximately $345 million in revenue (footnote – Testimony of Greg Smith, President of the Connecticut Lottery) for the state's general fund.

Jim Millstein, CEO of Millstein and Co., appeared before this Commission and revisited a recommendation of the Fiscal Stability Commission that the state contribute the lottery in kind to the TRS at a fair market value. He suggested that this be accomplished in a manner similar to what was done in New Jersey in 2017 wherein the lottery enterprise in its entirety was transferred to the New Jersey state pension funds in a 30-year concession agreement. The lottery enterprise was valued as an asset worth over $13 billion, and part of that transfer, the annual net proceeds of the New Jersey lottery, valued at over $1 billion annually, would flow to the pension funds as well. Francis Chin of American Public Infrastructure LLP was involved in the New Jersey transaction and explained to the Commission that a new actuarial technique was developed to set forth how the ADEC would be calculated, but the impact of this transfer would be an immediate decrease in the unfunded liability and a decrease in the state's ADEC. Although initially budget neutral due to the loss of that same amount in the General Fund, Chin clarified that it shifts to level credit over time.

Millstein identified several potential benefits of such an asset transfer. First, it would provide a dedicated source of funding for the TRS. Second, it would replace the annual appropriation to the TRS from the state budget with revenue from the lottery. Third, it would increase the funded status of the TRS thereby reducing the state's pension liability vis a vis a reduced ADEC. This reduced ADEC would offset the loss of the lottery revenue to the General Fund. Moreover, the improved UAAL would result in an improvement to the state's credit rating. State Treasurer Denise Nappier, however, cautioned that "the General Fund's gain would be the TRF's loss because less cash would flow into the TRF and trigger greater negative cash flows." She also noted that although the value of the lottery concession estimated at $5 billion would be included as a plan asset for actuarial purposes, it would not be valued this way for financial statement purposes in accordance with GASB rules.

The Commission considered an alternate version of that plan in which the Lottery itself would not be transferred, but the revenue of the lottery would flow into the TRS. This concept obviously does not allow the TRS to benefit from receipt of the $5 billion asset itself and thus the TRS would not experience an immediate increase in its funded ratio. However, the annual proceeds would relieve the General Fund of a portion of its ADEC while at the same time reducing the income that the General Fund otherwise would have received, leading some to consider it essentially a wash, or budget neutral.

Treasurer Nappier instead proposed an alternative plan wherein lottery revenues would be monetized by using revenue bonds sufficient to generate cash proceeds of $1.5 billion that would be deposited into the TRF. In addition, $1.5 billion of state owned assets would be transferred into the TRF, and an irrevocable trust would be established. Treasurer Nappier estimated that her proposal would generate approximately $440 million in savings to the General Fund from FY 2020 through FY 2025, and the TRS cash flow would be improved by approximately $560 million. Finally, after FY 2025, the State could pay off the Pension Obligation Bonds for $1.9 billion using the state ADEC and debt service payment for that year. Also, the TRS's investment return assumption could be lowered from 8% to 7%. Nappier insisted that the success of this proposal is dependent on the legislature continuing discipline imposed by the bond covenants and that the legislature should only be permitted to appropriate less than the ADEC by a supermajority vote with public notice. Her plan would result in a significant reduction in the anticipated TRS funding "spike" from $3.25 billion to $1.78 billion. It is important to note, however, that Treasurer Nappier's proposal is dependent on the existence of at least $1.5 billion in state assets that could be transferred to the TRS.

Next Steps

Before any of the above-mentioned proposals can be seriously considered, several steps must be taken. A determination of the exact fair market value of the CT Lottery would be required as would an examination of how/if the management of the Lottery would remain in its current form or be changed.