

Spending Cap Commission
October 24, 2016
Meeting Notes

Attendees:

Commission Co-Chairperson William Cibes, Commission Co-Chairperson Patricia Widlitz, Suzanne Bates, Rep. Jeff Berger, Sen. Beth Bye, Sen. Steve Cassano (by telephone), Rep. Christopher Davis, Tom Fiore, Sen. John Fonfara, Robert Frankel (by telephone), Sen. Scott Frantz, Sen. Joan Hartley, Roberto Hunter (by telephone), Sen. Rob Kane, Sen. Michael McLachlan, Lori Pelletier, Richard Porth, Ellen Shemitz, Bart Shuldman, Rep. Richard Smith, Rep. Jonathan Steinberg, Rep. Toni Walker, Rep. Melissa Ziobron (by telephone)

Staff:

Susan Keane, Administrator

Call to Order

Chairperson Widlitz called the meeting to order at 1:09 pm.

Acceptance of the October 17 Meeting Notes

Chairperson Widlitz asked for a motion to accept the October 17 meeting notes. The motion was made by Ms. Pelletier, seconded by Ms. Shemitz. Seeing no further discussion, the meeting notes were accepted by voice vote.

Definition of “General Budget Expenditures”

A. Expenditures for the payment of bonds, notes or other evidences of indebtedness:

Chairperson Cibes explained that after discussions preceding the meeting and input at public hearings, he recommended that the commission treat the aspect of unfunded pension liability as a separate category. He then discussed Proposed Definition 1, which reflects the Constitutional language regarding the treatment of the payment of bonds, notes other evidences of indebtedness:

“As used in this section, . . . “general budget expenditures” means expenditures from appropriated funds authorized by public or special act of the General Assembly, provided (1) general budget expenditures shall not include expenditures for the payment of bonds, notes or other evidences of indebtedness, . . .”

By way of context, Chairperson Cibes remarked that the Co-Chairpersons looked first to the structure of Section 2-33a in developing the proposed definitions. Further, he suggested taking each proposed definition in turn, so that when finished, the end result will resemble Section 2-33a. He added that at the end of the deliberation process, the adopted aspects will be tied into a recommended definition of “general budget expenditures” for inclusion in the final report.

Chairperson Cibes then moved adoption of Proposed Definition 1. The motion was seconded by Ms. Pelletier.

Mr. Shuldman offered the following amendment, which was seconded by Sen. Frantz:

~~... (1) general budget expenditures for any fiscal year shall not exceed those authorized during the previous fiscal year by a percentage which shall be determined by the greater of the percentage increase in personal income or the percentage increase in inflation, and (2) general budget expenditures shall not include expenditures for payment of the principal of and interest on bonds, notes or other evidences of indebtedness as issued by the state treasurer, expenditures pursuant to section 4-30a, or current or increased expenditures for statutory grants to distressed municipalities, provided such grants are in effect on July 1, 1991, and (2) expenditures for the implementation of federal mandates or court orders shall not be considered general budget expenditures for the first fiscal year in which such expenditures are authorized, but shall be considered general budget expenditures for such year for the purposes of determining general budget expenditures for the ensuing fiscal year. As used in this section, "federal mandates" means those programs or services in which the state must participate, or in which the state participated on July 1, 1991, and in which the state must meet federal entitlement and eligibility criteria in order to receive federal reimbursement, provided expenditures for program or service components which are optional under federal law or regulation shall be considered general budget expenditures "other evidences of indebtedness" means a security as defined by federal law.~~

Chairperson Cibes and Ms. Shemitz spoke in opposition to the amendment.

In response to questions and comments by Mr. Hunter, Mr. Shuldman agreed to remove "other evidences of indebtedness means a security as defined by federal law" from his proposed amendment.

Mr. Fiore and Chairperson Cibes expressed their concerns and questions regarding the proposed amendment.

Chairperson Widlitz then called for a vote on the proposed amendment. The amendment failed, with 8 voting yea, and 13 voting nay.

Mr. Shuldman and Chairperson Cibes further discussed Proposed Definition 1.

Chairperson Widlitz called for a vote on Proposed Definition 1. The proposal was adopted, with 20 voting yea, and 2 voting nay.

B. Expenditures pursuant to Section 4-30a:

Chairperson Cibes offered Proposed Definition 2:

"As used in this section, . . . "general budget expenditures" means expenditures from appropriated funds authorized by public or special act of the General Assembly,

provided (1) general budget expenditures shall not include . . . expenditures pursuant to section 4-30a, . . . “

He reminded members that Section 4-30a deals with the creation of the Budget Reserve Fund and expenditures that can be made from the Fund.

Chairperson Cibes moved adoption of the definition. Ms. Pelletier seconded the motion.

Sen. Kane expressed the concern that the commission was taking a piecemeal approach to the consideration of the various components of the definition of “general budget expenditures”. Further, he spoke to the issue of votes being taken, thereby putting members on the record before there was a chance to negotiate the components in defining “general budget expenditures”.

Chairperson Widlitz replied that the proposals were developed in response to members’ requests for proposed language in writing. She stated that members will have the opportunity to amend the proposals. She added that further discussions lie ahead for completing the definitions. Chairperson Widlitz remarked that while she understood Sen. Kane’s concerns, the process is leading to a final report on which everyone will have input and the ability to vote.

Sen. Kane stated that he understood Chairperson Widlitz’s remarks. He again expressed his concern that by the time the final report is voted upon, members will have already been on record as voting in support or opposition to the various components proposed without the ability to negotiate those components.

Ms. Bates asked for clarification on what will be exempted from the Spending Cap under the proposed definition.

Chairperson Cibes responded that the excess monies allowed to be transferred to the State Employee’s Retirement Fund will be exempt.

Ms. Shemitz and Chairperson Cibes discussed the effect of the proposal in allowing excess surplus funds paid toward the State Employees’ Retirement Fund to be exempt under the Spending Cap.

Rep. Smith stated the he concurred with the concerns expressed by Sen. Kane regarding the process. He commented that he does not believe that the components should be considered in isolation; rather, they should be viewed in the context of a final product. He stated that he wanted his fellow commission members to understand that any “no” votes he may cast on agenda items were a reflection of those concerns, as he wants to see how the various components are interconnected before voting in favor of them.

In response to questions from Mr. Shuldman, Chairperson Cibes, Mr. Fiore and Ms. Shemitz provided additional explanation of the provisions of Section 4-30a, as well as the Constitutional amendment.

Ms. Bates provided further explanation of the bipartisan approach that was used in crafting the provision of the Budget Reserve Fund language that allows monies to be funneled into the pension fund once a certain threshold has been reached. She stated that if Proposed Definition 2 is designed to limit only those funds from being exempt from the spending cap, she was comfortable with the proposal.

Chairperson Widlitz called for a vote on Proposed Definition 2. Sen. Kane stated that given his concerns regarding the process, he would be abstaining. The proposal was adopted, with 17 voting yea, and 5 abstaining.

C. The unfunded liability portion of state employees' and teachers' pensions:

Chairperson Cibes discussed Proposed Definition 3, which read as follows:

As used in this section, . . . “general budget expenditures” means expenditures from appropriated funds authorized by public or special act of the General Assembly, provided (1) general budget expenditures shall not include expenditures for payment of bonds, notes or other evidences of indebtedness, expenditures pursuant to section 4-30a, . . . expenditures in years prior to and including fiscal year 2022 for the payment of the portion of the ADEC representing the unfunded liability of any retirement system or alternative retirement program administered by the State Employees Retirement Commission or expenditures in years prior to and including fiscal year 2032 for the payment of the portion of the ADEC representing the unfunded liability of any retirement system or alternative retirement program administered by the teachers' retirement system, or for any such retirement system, expenditures for the payment of the portion of the ADEC representing any increase in the unfunded liability due to any changes in actuarial assumptions and cost methods.

He informed members that the proposal was developed in response to the suggestions and concerns raised at the last meeting. He explained that given the different circumstances for the state employees' and teachers' retirement systems, language was developed for each, and that the language included a phase-in period based on information previous provided by Secretary Barnes and Comptroller Lembo during their presentations before the commission. Further, he explained that during the phase-in period, the expenditures for the unfunded accrued past liability would be exempt from the spending cap, but the exemption would be sunset. Additionally, he explained that the provisions for each system include a “freeze”, with the unfunded liability for SERS being frozen at the level determined by actuarial analysis as of June 30, 2020, and the unfunded liability for TRS being frozen at the level as of the end of the currently established amortization period (SFY 2032). He said that the aim of this proposal is to give the bond rating agencies and the taxpayers some assurance that the state is handling the situation in such a way that the state's bond rating continues to allow the state to borrow money, and to provide some sense of stability to the taxpayers.

Chairperson Cibes then moved adoption of Proposed Definition 3. Ms. Pelletier seconded the motion.

Chairperson Widlitz commented that a lot of work had gone into the proposed definition in order to address the concerns of commission members. She shared that she and Chairperson Cibes wanted to develop a simple statement – that the current unfunded liability would be outside the spending cap, but there would be a “date certain” established that would require that from that time forward all pension costs would be under the spending cap. She informed members that the task was not as simple as originally thought, as there are 3 pension funds, each with their own amortization period. Chairperson Widlitz said that the Co-Chairs sought expert advice from various sources in their efforts to draft a compromise that they believed could work. She spoke of the discussion with Oz Griebel of MetroHartford Alliance following his testimony at the Hartford public hearing, who thought that the adoption of a plan to phase out the unfunded liabilities would demonstrate stability and predictability to the business community.

Ms. Shemitz raised the issue of rebasing. It was determined that the commission would discuss the issue at a future meeting, as it is on the menu of options to be considered/discussed at a later time.

Sen. McLachlan expressed his concern that his previous comments on this topic have been taken out of context. He explained that when he indicated that at the “end of the day” if the topic of unfunded pension liabilities was the last thing on the table for compromise and negotiation to ensure passage by the General Assembly, he meant that inclusion or exclusion of those dollars would be considered along with all the other components of “general budget expenditures” and not acted on alone. He stated that he is not comfortable considering each item individually, as where he may stand on a topic would be influenced by what is done with all the other items. Further, he stated that his willingness to exclude the unfunded pension obligations from the spending cap will be determined ultimately by what is done with all the items being considered by the commission. He shared that given the piecemeal approach being taken and the concerns of Sen. Kane and Rep. Smith, he would be abstaining on this proposal.

Rep. Smith asked Chairperson Cibes if the sunset language were to be adopted, would a three-fifths vote be needed to change it.

Chairperson Cibes responded that the language being considered is intended to be included in the replacement of Sec. 2-33a. He explained that if the replacement is adopted by a three-fifths vote, it would be the incorporation of the Constitutional spending cap in the statutes, and any changes to that language would have to be adopted by a three-fifths vote.

The proposal was further discussed by Rep. Smith and Chairperson Cibes, including a discussion of negotiations with SEBAC.

Rep. Steinberg stated that although he understands Chairperson Cibes’ desire to acknowledge the “wrinkle” that could be created by the need to restructure the assumptions on the returns

on investment, he is not comfortable with attaching it as a contingency to a sunset. He remarked that when he had suggested a sunset at previous meetings, he intended for there to be a very clear sunset without conditions. He stated that he finds it problematic to attach some conditions to the sunset. He suggested that if the commission is going to deal with the issue of return on investment, which he believes to be a legitimate issue, it should be dealt with separately. Further, he commented that the commission can have a conversation regarding what happens in that sunset period, whether it's a schedule or phase-in where a certain percentage of the unfunded liability has to be dealt with in any given year. He believes that an effective sunset is clean and ends without any possible conditions relating to it.

Chairperson Cibes commented that he understood Rep. Steinberg's position. He remarked, however, that if 7% is not an adequate rate of return, and out of necessity the rate must be lower, then in order to assure that a sufficient payment is made to pay off the pension obligation he believes it is reasonable to make it exempt from the spending cap. He commented that otherwise there is a disincentive for the legislature to fully fund the actuarially determined contribution, which would result in the state continuing to "kick the can down the road".

Mr. Hunter commented on the proposal and expressed his appreciation for the work that had gone into its development. After sharing his concerns regarding the timeframe laid out in the proposal and the consideration of actuarial assumptions, he stated that he will support the proposal, although it falls short in his view. He expressed the hope that the commission could get to consensus on an approach and that the legislature can improve upon the language through public comment.

Rep. Ziobron referenced a memo produced by OFA that addressed the unfunded accrued liability exemption from the FY 16-17 spending cap calculation. She shared that the memo included an exhibit that showed the year over year growth of SERS, TRS and JRS through FY 17. She asked if the Co-Chairs had obtained calculations on what the year over year growth would be under the terms of the proposed definition.

Chairperson Cibes responded that he used information in Josh Wojcik's October 5 presentation, which showed the payment schedule from FY 18 through FY 24 for SERS.

Rep. Ziobron reiterated her position that the definitions need to be as simple as possible. She stated that the idea that somehow the pension liability for the foreseeable future will not be taken into account is concerning to her.

Ms. Shemitz offered an amendment to include language that called for the exclusion of the unfunded past accrued liability, provided that any increase in the unfunded accrued past liability due to a failure to make the full actuarially determined annual contribution shall not be exempt from the spending cap. She stated that she offered the amendment in order to make the clear distinction between the debt as it stands now, which would be exempt from the spending cap, and any increase in the core of that debt or in the principle because of a

failure to make an annual contribution, which would be included under the spending cap. Ms. Pelletier seconded the motion.

Sen. Kane inquired if other proposals would be considered regarding this issue. He asked if he could move to open the agenda to include Mr. Hunter's proposal, which had been emailed to members.

Chairperson Widlitz replied that Sen. Kane could make such a motion once the commission had completed its deliberations on the amendment before them.

Ms. Shemitz offered the following language:

As used in this section "general budget expenditures" means expenditures from appropriated funds authorized by public or special act of the General Assembly, provided (1) general budget expenditures shall not include expenditures for payment of bond, notes or other evidences of indebtedness, expenditures pursuant to section 4-30a, expenditures [in years prior to and including fiscal year 2022] for the payment of the portion of the ADEC representing the unfunded liability of any retirement system or alternative retirement program administered by the State Employees Retirement Commission of expenditures [in years prior to and including fiscal year 2032] for the payment of the portion of the ADEC representing the unfunded liability of any retirement system or alternative retirement system administered by the teachers' retirement system, or for any such retirement system [expenditures for the payment of the portion of the ADEC representing any increase in the unfunded liability due to any changes in actuarial assumptions and cost methods] provided that any increase in the unfunded accrued past liability due to a failure to make the full actuarially determined annual contribution shall not be excluded from the definition of general budget expenditures

Ms. Shemitz explained that the intent of the amendment is to capture the issue Sen. McLachlan had raised at a previous meeting, which is that the current pension obligations would be under the spending cap and accrued unfunded liability would be excluded from the spending cap; additionally, there is protection against failure to pay current year obligations being pushed into later debt.

Chairperson Cibes offered a technical change to the amendment. Ms. Shemitz agreed with the Co-Chair's suggestion. The new amendment is as follows:

As used in this section "general budget expenditures" means expenditures from appropriated funds authorized by public or special act of the General Assembly, provided (1) general budget expenditures shall not include expenditures for payment of bond, notes or other evidences of indebtedness, expenditures pursuant to section 4-30a, expenditures [in years prior to and including fiscal year 2022] for the payment of the portion of the ADEC representing the unfunded liability of any retirement system or alternative retirement program administered by the State Employees Retirement

Commission or [expenditures in years prior to and including fiscal year 2032 for the payment of the portion of the ADEC representing the unfunded liability of] any retirement system or alternative retirement system administered by the teachers' retirement system. [or for any such retirement system expenditures for the payment of the portion of the ADEC representing any increase in the unfunded liability due to any changes in actuarial assumptions and cost methods] provided that any increase in the unfunded accrued [past] liability due to a failure to make the full actuarially determined annual contribution shall be considered general budget expenditures.

Sen. Kane asked if the amendment removed the sunset provision, to which Ms. Shemitz responded that it did.

Sen. Kane remarked that the reason the sunset provision was included in the original proposed definition was to advance a compromise. He asked Ms. Shemitz if the amendment would result in an opposite approach.

Ms. Shemitz responded that it was not her intent to do so. She explained that she was attempting to respond to the concerns raised by commission members regarding the dates and the specificity of the dates being tied to any current negotiation with SEBAC, as well the potential for a legislature to not pay the current year obligation in order to push it out, thereby putting it outside the cap.

Sen. Kane responded that he did not see the amendment the same way as Ms. Shemitz. He then asked how "failure" would be defined.

Ms. Shemitz replied that it was her assumption that any language adopted by the commission would be reviewed by the Legislative Commissioners' Office for the appropriate terminology prior to a final vote by the commission. She reiterated that the intent of the amendment is that any nonpayment of the full amount of the current year obligation and any interest on that unpaid amount would be under the spending cap.

Sen. Kane stated that he could not see himself supporting the amendment while there were other proposals to be considered.

Rep. Smith inquired as to the amount of the total unfunded liability. Rob Wysock of OFA responded that for SERS the amount is \$14.9 billion, for JRS the amount is \$153.7 million, and for TRS the amount is \$10.8 billion.

Rep. Smith asked Ms. Shemitz how the amendment dealt with the payment of the unfunded liabilities. He discussed the concerns of the business community regarding stability and how the unfunded liabilities will be paid. He asked how the amendment addresses those concerns.

Ms. Shemitz replied that the business community would know that the unfunded liabilities would be paid because were the current obligation not paid, it would take away from the ability to make other expenditures on key services and infrastructure. She added that under the amendment there is no incentive not to pay the full annual contribution.

Chairperson Widlitz asked Ms. Shemitz what effect, if any, the amendment would have on the current accumulated unfunded liabilities.

Ms. Shemitz responded that the amendment does not have any implications for speeding up or slowing down the payment on the unfunded liability in terms of the spending cap.

Chairperson Widlitz shared her concern that whatever language is adopted by the commission be a strong statement about a plan that addresses the current accrued unfunded liability.

Ms. Bates shared her thought that the amendment took what was meant to be more of a compromise back to the original position, which is just moving the unfunded liabilities out from under the spending cap ad infinitum. She stated that she fears that a perverse disincentive will be created to increase those unfunded liabilities and keep normal costs low by keeping discount rates high.

Mr. Shuldman expressed his opposition to the amendment and the underlying proposal. He stated that he didn't see the business community supporting them either. Further, he recommended that a bi-partisan group of stakeholders be formed to develop a solution regarding the unfunded liabilities.

Ms. Shemitz stated that her intention in offering the amendment was to try to put into language the compromise she thought had been suggested. As it appears that it is not the compromise that she understood to have been suggested, she withdrew her amendment. Ms. Pelletier withdrew her second.

Chairperson Widlitz stated that as the amendment had been withdrawn, the original proposal was now before the commission.

Ms. Bates stated that she was struck by the comments offered by a witness at the public hearing in New Haven as to why he thought everything should be under the spending cap. She shared that he had remarked that as things are moved outside of the spending cap, the state is saying that a certain group of people is privileged over everyone else. She stated that those groups whose interests remain under the spending cap will have to fight for scarcer resources. In addition, she expressed the concern that in moving unfunded liabilities in any form outside the spending cap the incentive to develop meaningful pension reform is removed. She spoke of the efforts in other states and municipalities that have resulted in drastic reductions to unfunded liabilities.

Mr. Shuldman spoke of his concerns regarding the timeframes laid out in the proposal. He stated that he could not support the proposal and does not view it as a compromise.

Rep. Steinberg stated that it appeared that the commission was at loggerheads. He commented that it appeared that there wasn't anything "on the table" that represented consensus. He suggested that the commission have further deliberations, and he offered to work on language for consideration.

Rep. Smith shared that he would also be willing to work with other commission members on language to achieve a compromise.

Chairperson Widlitz agreed that discussion should continue at the October 31 meeting.

Chairperson Cibes moved to table discussion of Proposed Definition 3.

Chairperson Widlitz reminded members that the commission would be holding public hearings on the following dates:

- Wednesday, October 26 from 4 to 7 pm at Eastern Connecticut State University
- Wednesday, November 16 from 4 to 7 pm in Waterbury (venue to be announced)

She announced that the October 31 meeting will be held at 10 am.

Chairperson Cibes remarked that the Co-Chairs had hoped to tie up all loose ends by the end of the meeting on October 31. He informed members that not only this issue, but the other issues listed on the agenda, as well as issues on the menu of options, will have to be addressed at the next meeting.

Mr. Hunter remarked that he felt it was incumbent upon all the commission members to place items before the commission in a timely fashion so that the members had an opportunity to review and consider the proposals in advance of the October 31 meeting.

Mr. Porth expressed his thanks to the members who had presented recommendations and options for discussion. He found them all to be offered in good faith. He recommended that a proposal be developed that makes clear that the normal costs are inside the spending cap and that there is a phased-in approach to dealing with the pension debt. Further, he stated that a responsible course of action is to figure out a way to deal with the current pension debt over time in a way that does provide for the predictability and stability that business leaders are seeking.

Chairperson Widlitz responded that she and Chairperson Cibes thought that their proposal accomplished what Mr. Porth had suggested. She asked the members to take an analytical look at the proposal.

Adjournment

Seeing no further discussion, Chairperson Widlitz adjourned the meeting at 4:12 pm.

Respectfully submitted,

Susan Keane, Administrator