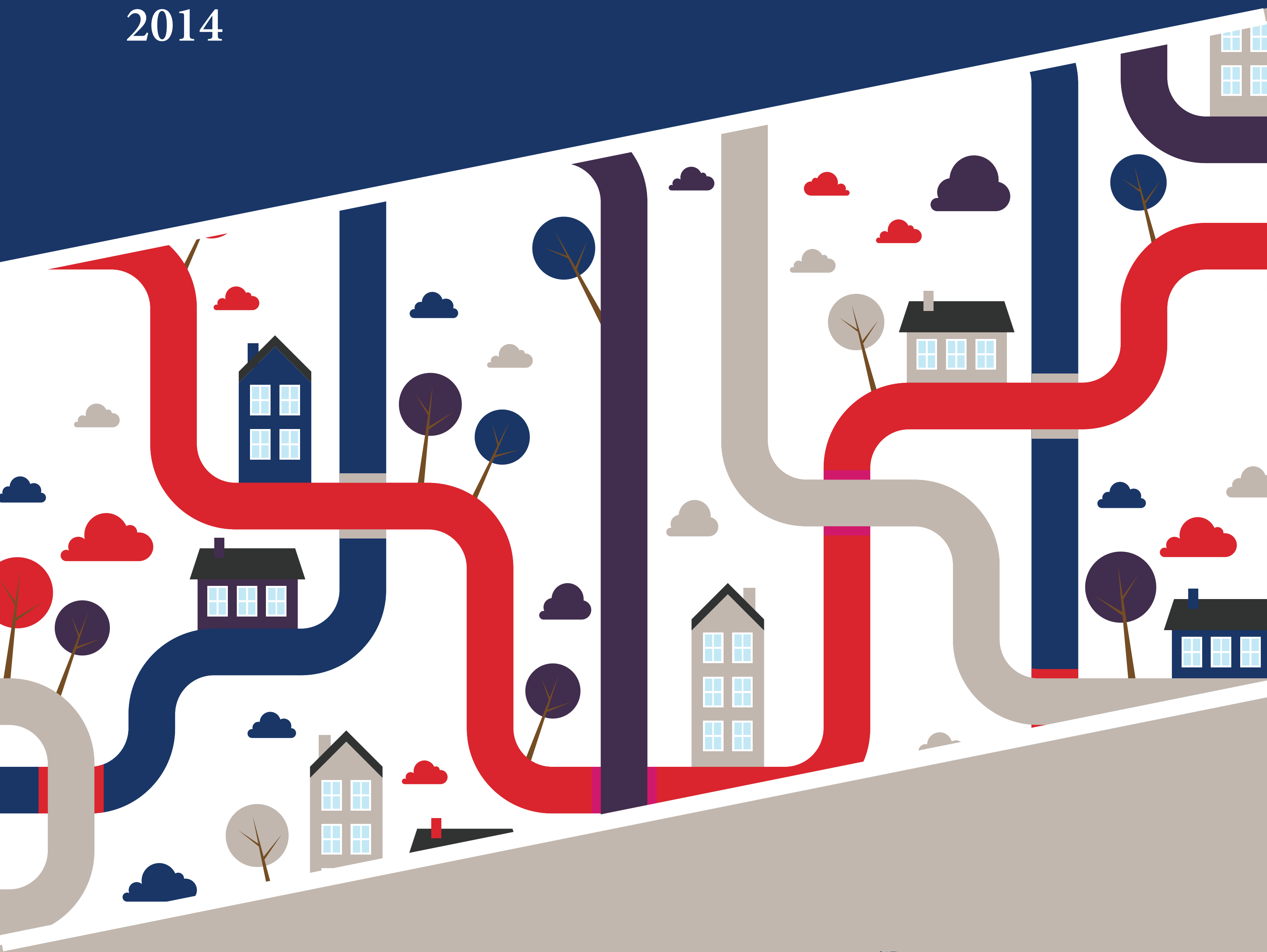
A ROADMAP FOR RENEWAL:
Policy Solutions to Revitalize Connecticut

2014



YANKEE INSTITUTE
For Public Policy

INTRODUCTION

In response to a recent Yankee Institute mailing, several residents – and former residents – sent back the following unsolicited replies:

> ***"I'm considering joining those that have moved out."***
>
> ***"Love what you are doing, but we moved out of Connecticut!"***
>
> ***"Sorry it's too late. We've already been driven from Connecticut by the high taxation and socialist policies of this state."***
>
> ***"I left! Good luck, but I think it's a lost battle!"***
>
> ***"Connecticut is lost! I do not plan on going down with the Titanic!"***

The despair is real as our state struggles with a host of problems, or what we have called our 'List of Lasts': The biggest tax burden in America; the country's highest per capita debt; sluggish population growth; anemic job growth; crumbling infrastructure; and a negative business climate.

Connecticut remains fiscally insecure. There's a projected deficit of $2.8 billion for the next biennium – even after record tax hikes of $1.5 billion in 2011.

The facts are sobering. Our state is on the wrong course. But Connecticut can come back! There remain many reasons for hope, including our educated and engaged population; our enterprising business community; and our beautiful and diverse environment. We are strategically located between two of our nation's most vibrant metropolitan areas, with a coastline that gives us access to international markets via multiple deep-water ports. With capable leadership and the right policies, Connecticut can once again become one of America's strongest, most welcoming states.

Accordingly, we call on the 2014 gubernatorial and state legislative candidates of all parties to adopt the following policies to revitalize Connecticut's economy and renew the prosperity of its people.

I. REVIVING THE ECONOMY

In 2011, Connecticut approved a record $1.5 billion in new taxes and tax increases.[1] By doing so it became one of the few states to respond to the fiscal crisis, brought on by the Great Recession, primarily through tax increases. Even as other states saw the need to rein in spending, Connecticut cut very little; instead, it boosted spending and raised taxes.

The effects of these policy decisions are evident. Raising taxes in the midst of a recession delayed Connecticut's recovery, and, in the years since, high taxes have continued to slow economic growth.

As a consequence, Connecticut has lagged national growth every year since the recession. Although most states have returned to pre-recession employment levels, Connecticut is still struggling to get back on track.

A Hostile Business Environment

Connecticut's businesses have consistently raised concerns about the state's hostile climate for industry, created by the significant tax and regulatory burdens placed on small and large corporations. Some of the recent changes made by state government have made things worse, as the state raised the minimum wage so it will be the highest in the country, and increased the number of mandates placed on businesses. This adds to the already long list of stifling regulations: strict prevailing wage laws; costly workers' compensation; a non-right-to-work jurisdiction; special licensing requirements; and unpredictable land use rules.

University of Connecticut economist Steven Lanza noted in 2011 how the state's burdensome regulatory environment adversely impacts small business, a chief engine of job creation. Certainly, he conceded, government regulation is necessary to protect against fraud and anti-competitive practices. "But in the extreme," Lanza wrote, "government regulations can yield a bewildering knot of red tape that can stymie even the most enterprising of business people or afford a privileged status to the politically-connected few."[2]

We can see the effect of this complicated, burdensome legal regime on our small business community: The number of small businesses in Connecticut shrank from 75,000 in 2006, to 69,472 in 2011, the last year for which official data is available.[3]

In a survey conducted this year,[4] Connecticut earned a "D" from small business owners for its friendliness to small business – putting the state in the bottom five in the nation. Connecticut

1 (Applebome 2011)

2 (Lanza 2011)

3 (U.S. Small Business Administration 2014)

4 Conducted jointly by Thumbtack.com and the Kauffman Foundation

earned failing grades for general business regulations; the state tax code; licensing requirements and fees; environmental regulations; zoning laws; employment, labor and hiring regulations; and health and safety regulations.[5]

Connecticut also received low grades for economic freedom from the Mercatus Center at George Mason University. Citing costly insurance mandates, rigorous occupational licensing requirements, and strict worker's compensation requirements, the state ranked 41st overall for fiscal freedom; 42nd for economic freedom; 43rd for family friendliness; and 42nd for finding a job.[6]

The Mercatus study analyzes economic freedom for those pursuing economic goals, as well as for individuals. It's obvious why our state struggles near the bottom of these national rankings -- in addition to the burdens Connecticut places on its businesses, it also imposes the heaviest tax load in the nation on its citizens.[7]

Crushed by Taxes

Middle class families are especially affected by the state's tax policies. Saddled with property and gas taxes among the highest in the nation, along with high state income taxes, they are struggling to find ways to make ends meet – and, too often, are also looking for work. In reality, the state's tax burden hits the middle class the hardest, because they are less able to move to escape high tax rates, and end up paying a higher percentage overall of their take-home pay to cover the tangle of state and local taxes and fees that increase year after year.

Part of Connecticut's fiscal policy failure stems from its unhealthy dependence on its wealthiest taxpayers to keep the state's budget afloat. The top 1.3 percent of taxpayers (those earning $1 million or more) pays 35 percent of state income taxes.[8] This makes the state's fiscal health subject to the dramatic fluctuations in wealth among its affluent population – a population that is also capable of being highly mobile. This is exacerbated by Connecticut's consistent status at the top of Forbes magazine's "Where Not to Die" list.[9]

Lagging Employment Numbers

Employment has been another struggle for Connecticut. Although the state unemployment rate officially dropped over the past three years, the employment numbers have lagged. In January of 2008, 1.77 million people were working in the state; by the end of June 2014, that number had dropped to 1.75 million.[10]

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5 (Lieber and Daniels 2014)
6 (Ruger and Sorens 2013)
7 ((Tax Foundation 2014)
8 (Cullen 2009)
9 (Ebeling 2013)
10 (Connecticut Department of Labor 2014)

Adverse Impact on Family Formation

Connecticut's ill-advised tax policies and its social programs likewise have an adverse impact on family formation. The result is a host of social ills requiring ever-increasing infusions of taxpayer cash to address.

Over the past ten years, there was a five-percentage point increase statewide in the number of children living with single moms (from 19 to 24 percent), according to census data. In Hartford, almost sixty percent of children now live in single-parent households – and in some Hartford neighborhoods, the figure is as high as eight in ten. Almost half of the children living in Bridgeport and Waterbury live with a single mother, while in New Haven the number is slightly higher than half.[11]

Such family instability has negative effects on child development, according to the Urban Institute. A recent study found that, "Between birth and fourth grade, more than 1/3 of children see their parents marry, remarry, separate, or start or end a cohabitating union. Family instability is positively linked to problem behaviors and some academic outcomes, even at early ages."[12] Connecticut must examine the impact of its policies on family formation and stability.

Crony Capitalism

Equally problematic is the state government's program of subsidizing private companies to move from one locale to another within the state, or to entice them to move into the state with promises of generous tax subsidies and payouts. The "First Five" program has meant shorter commutes for many top CEO's, but has also meant higher taxes for state residents. Bribing companies to stay in or move to Connecticut is not good for long-term growth, and sets up a two-tiered business community inside the state – those who are insiders, who have the government's ear and access to its pocketbook, and those that don't. Instead the state should focus on building a business-friendly climate and on shoring up its aging infrastructure. This, combined with the strengths that already exist here – like an educated population and proximity to two of the biggest markets in the country – should be enough to entice businesses to come and stay.

Given the challenges above, we propose the following action and policies:

- Reduce the regulatory burden on the business community.
- Roll back all of the 2011 tax increases, and eliminate nuisance taxes and fees that cost more to collect than they bring in.
- Streamline and privatize social services; offer poor families greater control over how to spend tax credits.

11 (Rosiak 2012)
12 (Sandstrom and Huerta 2013)

- Eliminate unwarranted exemptions, tax deductions and subsidies given to special allies of the governing class.
- Cancel the minimum wage increases set for 2015-17, leave the minimum wage at the current rate of $8.70 an hour to spur job growth amongst younger workers.
- In 2014 the state legislature instituted a Comprehensive Tax Study. Use this opportunity to find ways to cut taxes on families and businesses.
- Eliminate the Business Entity Tax, which especially penalizes small business owners.
- Reduce the number of professions requiring occupational licenses.[13] Require licensing only where there is a clear public interest.
- Study the impact of the current tax and benefits structure on family formation and stability.
- Streamline environmental permitting.

13 (Murphy 2013)

II. REFORMING OUR PUBLIC EDUCATION SYSTEM

Connecticut's education spending has skyrocketed over the past decade – but there's little to show for it.

Between 2003 to 2012 (the last year for which official census data are available):[14]

- Spending on education per child in Connecticut grew from $10,788 to $16,274 – a 51 percent increase.
- Total revenue – from local, state and federal sources – for Connecticut's education system increased by 38 percent, $7.15 billion to $9.86 billion.
- The number of school-aged children shrank from 577,403 to 522,451, a 9.5 percent drop.

Lots of Money, Little Return

The increased spending has garnered minimal returns. Academic performance has remained flat. In fact, over the last decade, Connecticut students' scores on the SAT (adjusted for participation and demographics) actually decreased by 1.5 percent.[15] Between 2003 and 2009, student achievement on the state's standardized tests grew by only 1 percent.[16]

Connecticut has one of the largest achievement gaps in the country, which means many of our low-income students are leaving high school without the knowledge and skills they need. The Common Core State Standards and the new standardized testing system accompanying the curriculum do not address the achievement gap, in fact they may exacerbate the problem. The state can best address the gap by focusing in on the districts that need it most, and by giving students and parents power to choose what school to attend, particularly at the high school level. The state should also expand its vocational education program and should look closely at new research on how to motivate students to stay in school and take responsibility for their education outcomes.

Not So "Harmless"

If there is a bright spot in Connecticut's educational system, it is the state's willingness to give parents a greater variety of choices about how to educate their children. These efforts should be expanded. Many studies show school choice has a positive impact on student achievement. The emphasis needs to continue to be on quality schools and parental choice.[17]

14 (Coulson 2014)
15 (Coulson 2014)
16 (ConnCAN 2012)
17 (Poiner 2014)

But even as the state expanded options for students, it continued to fund the districts the children left behind as if they were still there. Because school districts are paid based on the number of school-aged children who live within their boundaries, even if students leave a district or attend a charter or private school, districts are "held harmless" – that is, still paid as if they were educating the students who are actually at school elsewhere.

Because the state subsidizes so many of the education costs of some cities, the expense of double-funding students is high. Researchers estimate the state spends almost $190 million each year to double-fund these students.[18] Hartford receives an estimated $47 million a year from the state to pay for students who've left the district; Bridgeport and New Haven both collect an extra $26 million.[19]

In order to control Connecticut's education spending, a top priority should be to institute the "follow the child" method of funding education: Students are assigned a certain amount per year for their education and that amount is paid to the school they choose to attend. Along with saving substantial amounts of taxpayer money, this approach would also offer an incentive for schools to provide a better education to their students, in order to retain the funding each child would carry with him or her.

Common Core Chaos

Along with stagnant student achievement and a limited number of education options, parents and local school boards have also become increasingly frustrated by the national takeover of education and the resulting diminution of local control. The latest federal initiative is the Common Core program, and its testing requirements for all 50 states. Connecticut was an early adopter of the Common Core State Standards. Since then, districts statewide have been working to implement the new standards, along with a new curriculum, new textbooks, and new equipment.

Watching their children struggle with a new curriculum that teachers have not been adequately prepared to teach, parents have pushed back. Peggy Noonan, writing for The Wall Street Journal, noted the many complications that have attended the implementation of a large, one-size-fits-all national academic program.[20]

Any successful educational system must be sensitive to local priorities and local needs. No federal bureaucrat is going to be as keenly aware of the needs or as committed to the well-being of a locality's children as their parents and the other members of their community.

18 (Roza and Fullerton 2013)
19 (Bates 2013)
20 (Noonan 2014)

The College Crisis

Any analysis of Connecticut's educational system cannot ignore state spending on public universities. As professor salaries and infrastructure spending have soared, student tuition has followed suit.

At the University of Connecticut, tuition has increased by a whopping 52 percent over the past eight years – from $8,362 for the 2006-07 school year to $12,700 for 2014-15. Tuition at the other state universities has increased by an average of 46 percent over the same period, from $6,284 in 2006-07 to $9,168 in 2014-15. These dramatic price hikes are pushing college education out of reach for many middle class families, unless they are willing to be saddled with debt.

Part of the reason for the rise in tuition is because of the ever-increasing salaries of professors and other employees.[21] A recent report by the state auditor said the University of Connecticut needs to establish maximum salary levels for professors, and to make sure every professional position is set within a given pay range.[22]

Based on the foregoing, we propose the following policies:

- The state should suspend and re-think implementation of the Common Core State Standards.
- Empower parents by having state money follow children to their school of choice
- Rein in costs and tuition increases at public colleges and universities.
- Connecticut should have a home-grown, rigorous curriculum.
- Implementation of future curriculum changes must be well thought out, with suitable teacher training in place, with funding allocated from existing streams.
- Successful schools should be allowed greater flexibility.
- The menu of educational options for students should expand.
- In order to attract top talent and improve math and science teaching, teachers from diverse professional backgrounds should be welcomed.
- Focus on strengthening parental and local control over curriculum, teacher/administration selection, and compensation.

21 (Thomas 2013)

22 (Geragosian and Ward 2014)

III. IMPROVING OUR INFRASTRUCTURE

A strong state energy and transportation infrastructure is vital to a state's economic success and the well-being of its families and businesses. But when it comes to infrastructure, Connecticut is falling behind.

Misplaced Priorities and Broken Roads

A White House report ranked Connecticut last in the nation for its poor road quality – with 41 percent of the state's roads deemed to be in poor condition.[23] A report card by the American Society of Civil Engineers found that 73 percent of roads in the state are said to be in poor or mediocre condition, and that there are 406 structurally deficient bridges within the state.[24]

State government has consistently raided the special transportation fund, moving money from it into the general fund. It also has devoted large portions of the transportation budget to transit outside of the New Haven-Stamford corridor, while the Metro-North line – a key artery for Fairfield County workers – deteriorates.[25] It is time for the state to reprioritize funding by focusing on its most heavily used roads, bridges and rail lines.

Bad Policies, Inflated Costs

Connecticut spends significantly more on its infrastructure projects than it needs to. That's because the state pays a "prevailing wage" for government construction projects over $400,000 and renovation projects over $100,000. Prevailing wage laws require state and local governments to pay much higher wages than they otherwise would. Although towns have asked for the contract thresholds to be increased, the state legislature has refused to address the issue.

State government also unnecessarily adds to infrastructure costs by frequently closing large contracts to all but union-only bidders, who constitute just 20 percent of the total number of construction companies in the state. This policy may satisfy politically active union bosses, but it dramatically reduces the number of bids on a project and thus increases the final cost to Connecticut's taxpayers.

Better Energy Policy

Along with transportation infrastructure reform, the state is also due for an update to its energy infrastructure. The state has announced plans to expand its capacity to deliver natural gas to

23 (White House 2014)
24 (The American Society of Civil Engineers 2013)
25 (Connecticut Department of Transportation 2013)

consumers. This is vital, as prices of natural gas have fallen significantly as prices of oil and electricity have risen.

High energy costs affect families across the state, and they also impact the state's businesses, particularly those in the manufacturing sector. Connecticut's electricity costs are particularly high, and are expected by rise by another five percent by the end of the decade, according to an upcoming study that will be jointly issued by the Yankee Institute and the Beacon Hill Institute.

The RPS Debacle

Connecticut adopted the Renewable Portfolio Standards (RPS), in 1998. They were most recently amended in 2013. Rather than creating its own sources of renewable fuel, however, the state is spending the vast majority of its RPS money on initiatives in other states – including biomass projects in Maine and New Hampshire.[26] In fact, the state's Department of Energy and Environmental Protection (DEEP) wants to adjust the mandates so the state will be allowed to use taxpayer money to purchase electricity generated by hydropower in Quebec.

Under current standards, electric utilities must obtain at least 27 percent of their electricity from renewable sources by 2020. The RPS mandates cost Connecticut's businesses millions (and drive up prices) by forcing them to find more expensive, less efficient sources of energy to use.

Consumers are suffering, too. Although conservation efforts may have saved us energy, they've cost state residents money, as energy firms have attempted to recoup losses from efficiency efforts through higher rates. WalletHub.com estimates that our residents spend the second most on energy bills in the country, second only to Hawaii.[27]

Based on this research we propose the following policies:

- Spend special transportation money only on transportation projects.
- Revamp prevailing wage laws and open all contracts to every qualified construction firm.
- Increase prevailing wage thresholds and exempt cities and towns that are struggling to keep their budgets in check.
- Move forward with plans to increase access to natural gas.
- Continue to upgrade the bridges and cars used by the Metro-North rail line.
- Expand the state's capacity for and use of nuclear energy.
- Adjust or repeal RPS to give Connecticut greater control over its energy options.
- Develop a 20-year plan with public input to upgrade Connecticut's transportation infrastructure, with particular emphasis on well-traveled roads, highly-used rail lines, and bridges.

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26 (Connecticut Department of Energy and Environmental Protection 2013)
27 (Busemeyer 2014)

IV. CURING HEALTH CARE

The American health care sector has undergone a massive reform effort over the past few years, with serious (and often unwelcome) repercussions for most Americans.

Even as government has been seeking to put more of the health care sector under its control, the private sector has been innovating with new ways to deliver health care less expensively to more people. For example, retail health clinics for less-complex health problems have been established in neighborhood pharmacies, at significantly lower costs than traditional doctor and emergency room visits.[28] In addition, health professionals like nurse practitioners, nurse anesthetists, physician's assistants, and midwives, are providing lower cost health care, where state law allows.

Because of the significant regulations Connecticut imposes on its health insurers, health insurance rates in our state are among the highest in the country. A Kaiser Family Foundation study showed that Connecticut residents paid the sixth highest average monthly premiums.[29]

A major inefficiency in health care stems from the fact that costs are not transparent. Patients visiting a clinic or hospital do not know up front what the rates are for their visits or any procedures. This is a significant flaw in our current system. All health care providers should have to post rates publicly, to allow consumers to compare rates.[30]

After passage of the Affordable Care Act ("ObamaCare"), Connecticut established its own health insurance exchange. According to data supplied by Access Connecticut, of the 197,878 enrollees, only 76,597 enrolled with a private insurance carrier; 121,281 enrolled in Medicaid.

Initially, the federal government is supplementing state budgets to make up for all of the cost of new Medicaid enrollees, but by 2016 states will be obligated to pay 10 percent of those costs for some enrollees, while the state will be on the hook to pay up to 50 percent of the costs for enrollees who would have been eligible under our preexisting Medicaid standards. The state is unprepared to take on these massive new funding obligations.

The state already covers more adults than most other states under Medicaid. Just over half of all states, including Connecticut, cover adults who earn up to 133 percent of the poverty level, while the remaining states provide no Medicaid coverage for childless adults. Connecticut also covers all parents who earn up to 196 percent of the poverty level, which is the second most generous calculation in the country. Most other states, including all of our neighboring states, only cover parents up to 133 percent of the poverty level.[31]

28 (Shultz, Atlas and Cogan 2014)

29 (Kaiser Family Foundation n.d.)

30 (Consumer Reports Magazine 2012)

31 (Centers for Medicare and Medicaid Services 2014)

Based on this research we propose the following policies:

- Reduce the number of insurance mandates to lower the cost of insurance premiums.
- Watch over hospital consolidation to prevent monopoly pricing.
- Give low-income residents more choices by moving some out of Medicaid and onto the exchange created by the Affordable Care Act.
- Allow health professionals to practice to the fullest extent of their training.
- Allow consumers to see provider costs before treatment.
- Maintain consumer control of health care options.
- Lower the Medicaid qualifying income level to at least the ACA recommended level or to a level competitive with those of comparable states.

V. CIVIL SERVICE REFORM

Connecticut must rein in its public sector spending, or it will ultimately go the way of Detroit. Mounting pension debt and other employee costs, coupled with an exodus of taxpaying companies and residents, is a recipe for economic catastrophe.[32] To avoid Detroit's fate, Connecticut must revise its public sector labor agreements.

One of the major decisions facing lawmakers in 2015 is whether or not to renew the no-layoff pledge made by Gov. Dannel Malloy to state employees in 2011. Gov. Malloy made the pledge during contract negotiations, and promised no-layoffs for four years. It would be unwise for the legislature or the governor to renew this pledge, as it restricts the state's ability to manage employees according to its needs – both in terms of total number of state employees, and the number of employees with specific skill-sets. Our lawmakers must have the tools necessary to shape the state workforce according to the needs and demands of our state's citizens, not the other way around.

To further revitalize Connecticut, working conditions for government employees must be brought back into line with those of their private sector counterparts. Government employees in the Hartford metropolitan area make, on average, $10 more per hour than private employees.[33] Public employees collected $34.47 an hour on average, compared to $23.23 an hour for private sector employees in 2010 (the most recent year for which statistics are available[34]). Even among management, public employees hold an almost $5 advantage, earning $40.03 an hour compared to $35.46 in the private sector. And these figures don't take into account the public sector's generous benefit packages.

Also, state employees pay significantly less toward their health care coverage than workers in the private sector. There also has been slower turnover to the high-deductible health savings account (HDHSA) model, which is increasingly the approach favored by many private companies in order to reduce costs. This model offers consumers greater choice and also greater accountability for their health care spending.

Ultimately, state workers have as much reason as other taxpayers to favor sensible public sector reforms. That's because restoring Connecticut's economic vitality and recalibrating government workers' salaries and benefits is the only way to provide long-term security of employment for public employees.

Under the current system, the state will find it extremely difficult to keep its promises to its current and former state employees. Connecticut has underfunded its public employee pensions

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32 (Center for Business and Industry Association 2013)

33 Bureau of Labor Statistics

34 (Bureau of Labor Statistics 2010)

for years; this fact, combined with poor returns on pension investments, means Connecticut residents are significantly in debt to those funds. A recent Yankee Institute study shows that the state owes about $100 billion in pension liabilities and other employee benefit liabilities. This translates to $27,668 of pension debt for every man, woman, and child in Connecticut. [35]

In addition, the state needs to reform its judicial pensions. Judges can be eligible for generous pensions after only a few years of service on the bench. It is time for the state to do away with pensions for state judges, and instead offer judges a more generous salary.

Currently, most state employees are required to belong to a union as a condition of their employment. They can only opt-out of the portion of their union dues that would pay for political activity. State employees should be given a choice of whether or not they want to join a union and pay any union dues. Enacting pro-choice union labor laws would also have the added benefit of making unions more responsive to their membership.

Based on this research we propose the following policies:

- Move to a defined contribution, 401(k) style retirement plan for all new state employees.
- Re-design state employee health insurance plans so that employees pay more for more expensive plans; or move all employees to a high-deductible health savings account plan.
- In future negotiations with public employee unions, insist on contracts that bring wages and benefits more in line with those in the private sector.
- Give workers the choice of whether or not to join a union, and don't make union membership a condition of employment
- End pensions for state judges; offset the lost benefits with higher wages.
- Do not renew the no-layoff pledge.

35 (Moody and Warcholik 2014)

VI. PUBLIC MANAGEMENT REFORM

Connecticut's elected officials and civil leadership are charged with administering a $21 billion annual budget and overseeing a workforce of more than 40,000.

Unfortunately, even after the tax hikes of 2011, the state continues to face projections of continued deficits. If there is any common theme running through all Connecticut's policy challenges, it is the failed management of state resources and personnel.

Connecticut consistently ranks at or near the bottom of surveys measuring economic strength. Our state was recently labeled the worst "sinkhole" state in the nation because we carry $61.4 billion in debt.[36] A recent study from Truth in Accounting found that Connecticut ranked 50th in the nation when it comes to "taxpayer burden." According to the study, each Connecticut taxpayer would have to send our state treasury $48,100 just to fill its current financial hole.[37]

Our taxes are too high, our debt levels are too high, and there is anemic job and income growth.[38] These are all irrefutable signs of poor management by our elected and appointed state officials. Connecticut must apply proven management principles to all branches of state government in order to reverse these damaging trends.

The Surplus That Isn't

In an effort to convince voters that Connecticut's economic challenges had been addressed, state leaders employed a variety of accounting gimmicks to create the appearance of a budget surplus. Tricks used to create a surplus on paper included delaying debt payments; assuming more debt through bonding to cover operating costs; and shifting money from the transportation and other designated funds into the general fund.[39] State Sen. Jason Welch, (R-Bristol) estimated that the state had increased the amount in the general fund – on paper – by more than $1 billion through these contrivances.[40] Also, the state budget doesn't address future spending obligations, like pension debt and the large expansion in Medicaid enrollment. Connecticut taxpayers will soon see the effects of pushing these obligations off into the future.

On its own balance sheet in the state's Comprehensive Annual Financial Report (CAFR), the state admitted that it spent more than it took in.[41] The report conceded that, "From a balance sheet

36 (Truth in Accounting 2014)

37 (Truth in Accounting, "The 2013 Financial Condition of States," www.truthinaccounting.org/library/doclib/2013FSOS.pdf

38 (Yankee Institute 2013)

39 (Stuart 2014)

40 (Welch 2014)

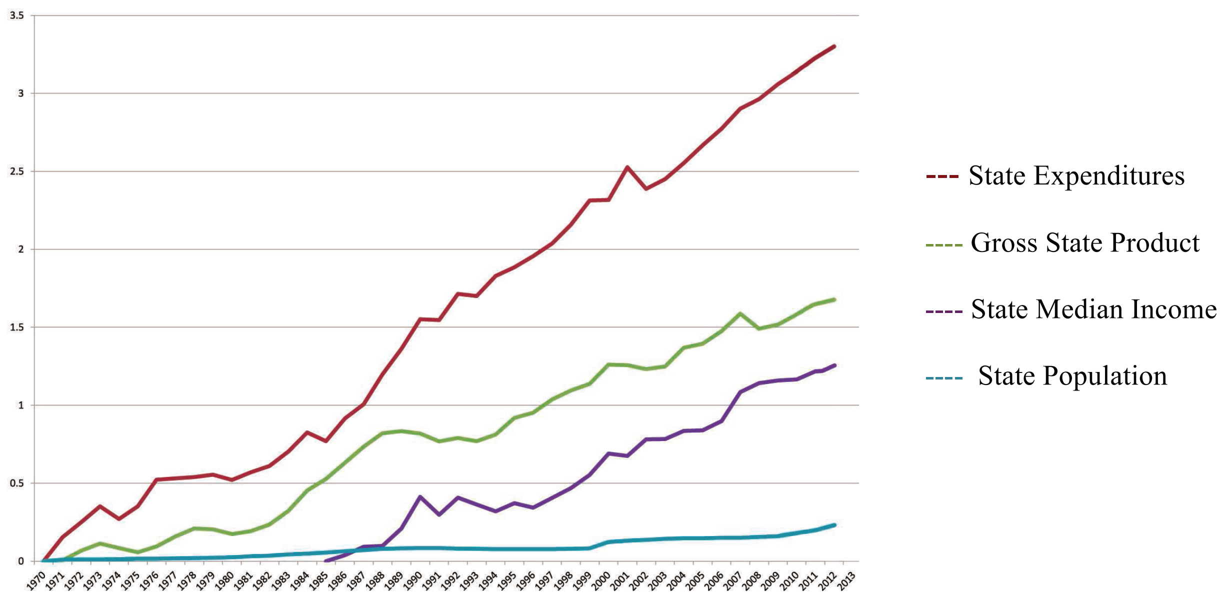
41 (Office of the State Comptroller 2013)

perspective, the GAAP [generally accepted accounting principles] shortfall or unassigned fund balance deficit in the General Fund was $1.217 billion as of June 30, 2013. This represented a deficit increase of $71 million from last fiscal year."

Ignoring the Cap

Connecticut has a constitutionally mandated spending cap, intended to limit the growth in government spending.[42] The cap calculation does not include debt service, grants to distressed municipalities, the first year of spending on court orders, or transfers to the budget reserve fund. The cap is intended to be a strict limitation; it can only be exceeded by a vote of 3/5 of the legislature, or if the governor declares a state of emergency.[43] But in 2013, Gov. Malloy evaded the cap's limitations by failing to account for $6 billion of Medicaid spending in his budget,[44] even though in previous years all Medicaid spending was included in the budget.[45] The practice of evading the cap through budgetary maneuvering has gone on under several successive gubernatorial administrations.

Oblivious to the damage that its unbridled spending inflicts on Connecticut, the state legislature simply continues to approve budgets that increase state spending year after year.



42 The amount of annual spending is pegged to the previous year's percentage determined either by the annual rate of inflation or a five-year moving average growth rate of Connecticut's personal income.

43 (Legislative Staff 2012)

44 He moved the federal government's contributions to Medicaid spending off-sheet.

45 (Avila 2013)

Needed: "Disruptive Innovation"

In the private sector, prices for goods often fall over time. To put it simply, the cycle of cheaper products overtaking their more expensive counterparts in the marketplace is called "disruptive innovation."

By contrast, in the public sector, costs steadily increase. Health care, education, social services and transportation costs climb up and up. Although this is partially due to the labor-heavy functions of government, it is also because government is slower to innovate – after all, as a de facto monopoly, it has no competitors, and there is ongoing political pressure to increase spending.[46]

But a 2012 Deloitte study argued that disruptive innovation can take place in the public sector.[47] In order for it to occur, however, state government must employ market principles in handling its responsibilities and customers. Examples of this phenomenon in the public sector include e-government initiatives that have streamlined and improved government-consumer interactions.

Government must likewise recognize its power to shape markets through its enormous spending power. This should allow government to negotiate aggressively for lower costs of goods – such as prescription drugs and textbooks – or services.

Other ways that state innovations could produce cost savings include:

- Using house arrest combined with electronic monitoring instead of putting non-violent criminals behind bars.
- Expanding online learning to enhance educational options for K-12 and college students.
- Exploring disruptive technologies in state funded health care; examples include retail clinics, tele-medicine, medical tourism, and personalized medicine.[48]

Other Applicable Principles

The state has already taken some steps to apply the manufacturing methodology of "lean production" to state government's "'operating system,' - (its) configuration of assets, material resources, and staff."[49] Lean production assumes an organization should only spend money on

46 (GoveLab, Deloitte 2012). More typical in the public sector is sustaining disruption, which improves services but at a higher cost. Id. at 5.
47 (GovLab, Deloitte 2012, p. 3)
48 (GovLab, Deloitte 2012)
49 (Bhatia and Drew 2006)

things that add value to a customer – in our case, state residents.[50] These principles are being applied in state and local governments across the world; a McKinsey & Company publication outlined how a UK government office achieved significant productivity gains through Lean principles.[51]

Finally, the state should adopt a zero-based approach to budgeting. This practice assumes a "baseline" of zero – rather than the current year's spending – as the starting point for budgeting. Zero-based budgeting "forces managers to scrutinize all spending and requires justifying every expense item."[52]

By instituting these straightforward management practices, Connecticut could significantly reduce spending. This, in turn, would spark increased private sector confidence, ultimately resulting in job growth.

Based on this research, we propose the following policies:

- Strict adherence to the constitutionally-mandated spending cap.
- Eliminate accounting gimmicks and adopting all GAAP accounting principles.
- Apply sound management principles including zero-based budgeting and a cost/benefit analysis of all programs; lean management; and disruptive innovation to increase oversight and accountability to Connecticut's taxpayers.
- Develop and adhere to an overall plan to reduce the state's debt burden and to protect the state's credit rating for bonded funding.

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50 (Lean Enterprise Institute n.d.)

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