



**STATE OF CONNECTICUT
OFFICE OF THE STATE COMPTROLLER
55 ELM STREET
HARTFORD, CONNECTICUT
06106-1775**

**Kevin Lembo
State Comptroller**

**Martha Carlson
Deputy Comptroller**

December 1, 2011

The Honorable Dannel P. Malloy
Governor of the State of Connecticut
State Capitol
Hartford, Connecticut

Dear Governor Malloy:

I write to provide you with financial statements for the General Fund and the Transportation Fund through October 31, 2011.

OPM is projecting that the General Fund will end Fiscal Year 2012 with a balance of \$79.1 million, an increase of \$3.5 million from last month. As discussed below, OPM has identified various risk factors relating to its current estimates. These risk factors may significantly alter the present financial outlook as the fiscal year progresses.

The original budget plan for Fiscal Year 2012 contained a \$75 million reserve to offset an anticipated increase in the unreserved General Fund balance on a GAAP accounting basis. This new practice of reserving a portion of General Fund revenue in fund balance is the result of the state's move toward GAAP based budgeting. Any remaining projected General Fund balance is reserved for payment of 2009 Economic Recovery Notes in accordance with PA 09-3 JSS.

OPM is estimating an ending balance of \$109.2 million for Fiscal Year 2012 in the Transportation Fund. There is no change in the estimate this month. Debt service savings is offsetting revenue reductions associated with lower than anticipated fuel tax receipts.

I am in general agreement with OPM's analysis, and have similar qualifications on the current General Fund projections. Specifically, as OPM notes, the savings associated with the 2011 SEBAC agreement are still being assessed. With respect to health care costs, the current trend reflects robust enrollment in the Health Enhancement Program (HEP) that will help to yield future savings. However in the short run, higher employee payments associated with non-enrollment will not be realized. OPM has noted that a "significant shortfall" is possible in the employee health accounts. In addition, we await actuarial findings related to estimated pension savings. Additional areas of concern are potential reductions in federal programs and the combined state costs associated with the recent storms. The storm costs and related reimbursements are still being tallied.

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General Fund spending is expected to end the year \$9.3 million under budget. Agency deficiencies of \$12 million are more than offset by anticipated forced savings of \$21.3 million. A \$7.6 million deficiency is projected in the Department of Social Services' Medicaid account. This deficiency is attributed to continued growth in the low income adult population. The Teachers' Retirement Board is experiencing a \$2.4 million deficiency in its health service account due to higher membership. Finally, Public Defender Services is experiencing a \$2 million deficiency in payments to contracted attorneys. The opportunity for deficiency appropriations is limited by the spending cap. The General Fund budget is within \$1 million of its allowable appropriation limit under the constitutional cap. To the extent that allocated lapse savings cannot be achieved through the budget plan mechanisms, other means of achieving savings must be found.

General Fund revenues are currently estimated to fall \$11.1 million short of initial budget projections. It should be noted that a significant percentage of the state's income tax revenue is tied to capital gains. Volatility in the stock market results in volatility in this revenue category. The current unsettled market conditions raise significant concerns, and will be addressed in future projections.

Connecticut's economy continues to show slow and erratic growth. For the twelve months ending in October the state added 10,100 payroll jobs. The September unemployment rate dropped to 8.7 percent. For the period ending in September, wage and salary income in Connecticut was up 4.4 percent from last year. Nationally, corporate profits were up 7.9 percent in the third quarter of 2011. Housing permits were down 8.3 percent from October a year ago and off 75 percent from the peak level reached in 2004. This is consistent with the downward trend experienced in existing home sales. The Connecticut Manufacturing Production Index has held steady against last year. Connecticut's export sector continues to perform well.

I also issue a Comprehensive Annual Financial Report (CAFR) that converts the budgetary based financial reporting to Generally Accepted Accounting Principles (GAAP). From a balance sheet prospective, the GAAP shortfall or unreserved fund balance in the General Fund was \$1.7 billion as of June 30, 2010. This figure will be updated in January 2012 for Fiscal Year 2011.

If you have any questions on this report, please do not hesitate to contact me.

Sincerely,

Kevin Lembo
State Comptroller