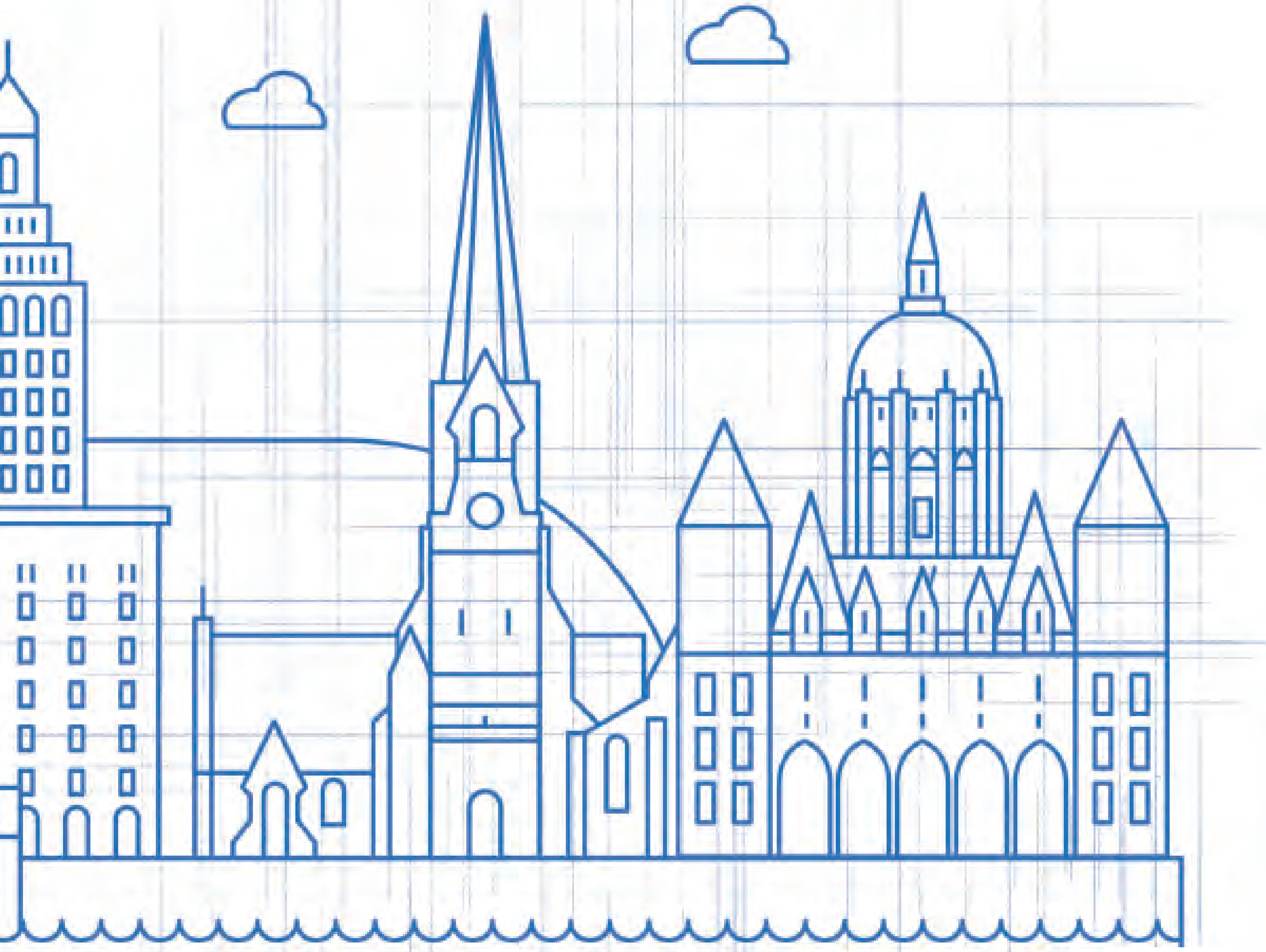
Charter For Change

Blue print for a New Administration

YANKEE INSTITUTE For Public Policy



2019

Dear Governor Lamont,

Thank you for your willingness to shoulder the burden of leadership, and for your commitment to our beautiful state. It's an honor to have the opportunity to work with you in service to the people of Connecticut.

Now that election season is over, we now have the chance to unite to pursue policies that will restore prosperity and help our state thrive. The challenges Connecticut confronts are substantial, and it will certainly require our collective best efforts to surmount them.

As you know, Connecticut absorbed a pair of massive tax increases in 2011 and 2015. They have inhibited Connecticut's recovery from the Great Recession; driven many of our most affluent taxpayers from the state; and made Connecticut less attractive to new enterprises and businesses of long and storied tenure alike.

Yet even as taxes have increased, pensions and other retirement-benefit costs for government workers—the key drivers of the state budget crisis—have remained unreformed. And just last year, the state formalized a SEBAC agreement that, on its face, constrains its options for managing forthcoming budget shortfalls. And so you, our leaders, will be facing agonizing decisions as you deliberate over Connecticut's path forward.

What follows is Yankee Institute's contribution to that crucial discussion. The *Charter for Change* is a compendium–thorough, we hope, but certainly not comprehensive–of reforms that can begin to turn our state around. These reforms ***require no changes whatsoever to the SEBAC agreement***, and can therefore be enacted through the new governor's first budget along with its supporting statutory instruments.

The proposals laid out in the Charter for Change include suggestions on how we can improve the state's budgeting process, reform municipal funding, streamline state regulation, and more. These are common-sense measures aimed at revitalizing our state's economy, balancing its books, and reinvigorating its body politic.

It is time–it is *past* time–for the meaningful reform our state and its people desperately need. Until Connecticut's government-worker pension and benefit funding crisis is addressed without further damage to the state's economy, it is irresponsible and wrong to demand further sacrifices from our already-overburdened taxpayers. Without reform, every revenue increase is effectively swept away by the torrent of unsustainable, endless spending that is bankrupting our state, extinguishing its prospects, and hurting its people.

In short, Yankee Institute cannot support *any* net tax increase of *any* kind until the hard work of major structural reform has been accomplished. Until government shows itself willing and able to adapt to fiscal reality; resist the coercion of powerful special interests that have long benefited from the status quo; and prioritize private sector growth and opportunity over government expansion, the Yankee Institute mantra will remain clear and unequivocal: *Not One Cent More.*

The task before you may not be easy, but it is necessary as never before. Together, let us begin the work of reform, so that we may someday have the satisfaction of knowing that we did our part, in our time, to restore prosperity for our state and opportunity for its people.

Carol Platt Liebau

Carol Platt Liebau
President
Yankee Institute

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Appendices available at yankeeinstitute.org/charterforchange2019

Spending Reform

The fiscal crisis confronting our state does not stem from a lack of revenue. Connecticut's taxes are among the highest in the country, and its people have absorbed two of the largest tax increases in its history within the past decade.

Rather, our state faces a spending crisis. Notwithstanding its significant tax burden, Connecticut will grapple with a deficit that totals more than 10 percent of its budget this coming year—and more than 12 percent in the following year -- with the trend line spiking still further after that.

Responsibility for the fiscal crisis does not rest entirely with recent governments, nor with any single party; much of it results from decades of poor management, overspending and overpromising. In any case, at this juncture, culpability for the crisis is irrelevant, and blame-casting is irresponsible. The pressing question before us is how, together, we can fix the problem with the least possible harm to our state and its people.

Common sense dictates there is only one way to fix a spending problem: by spending less. Because of Connecticut's high fixed costs, this means that the new government must present and pass lean, tight budgets with all unnecessary spending excised. Only then can we regain top-flight borrowing credentials, while realizing the revenue adjustments that are essential for our state to regain its reputation as a national leader in economic growth and business-friendliness.

What follows in this section are reforms that will allow the new government to begin accruing immediate savings and restoring Connecticut's financial standing.

Decrease Reliance on Bonding

Connecticut's debt service payments are one of the most rapidly-growing fixed costs in state government -- and one of the few that are independent of SEBAC. Annual bonding has increased dramatically over the past eight years, and it is time to rethink how, when and why bonded debt is being incurred.

In some cases, it is time to stop bonding altogether. Here, the "economic incentives" provided to businesses in the form of grants, tax credits and "forgivable loans" come to mind.

Dashing hopes that these incentives would spur meaningful growth and result in significant job creation, they instead have had a negligible impact on the state's economy. Indeed, several major businesses that received large incentive packages have either failed to fulfill the promises upon which the funds were contingent or, worse, have left Connecticut altogether. The state's experience with Alexion Pharmaceuticals offers a prime example. Alexion received $51 million in tax credits, loans and grants—and then decided to move to Boston nonetheless.

But the shortcomings of this approach are not limited to a single company or "investment"; they are systemic. According to state auditors, the Department of Economic and Community Development (DECD) has reported inaccurate numbers on the success of its economic incentive programs; in any event (as Yankee Institute will demonstrate in a forthcoming policy study), DECD has both chosen the wrong metrics and is comprehensively undercounting the programs' costs and negative impacts. Accordingly, it makes sense to end the First Five Initiative, the Small Business Express and related "economic-development" projects immediately.

More broadly, state bonding should be reserved solely for high-priority *capital* projects, with the rainy-day fund similarly reserved for unforeseen emergencies. The state has already faced credit downgrades resulting from its debt burden and high expenses. With a new $1.9 billion bonding cap in place, it is prudent for Connecticut to focus its borrowing exclusively on capital repairs and projects.

Even capital bonding can be reduced in the area of school building and repairs. Connecticut spent $5.9 billion on school construction between 2006 and 2015; the state now expends $700 million each year on the debt service for that construction. Our state covers up to 80 percent of school building and repair costs through bonding, depending on the school district.

Much of this spending has been on magnet schools. Some new-school building, though, has exceeded the district need, particularly at a time when most Connecticut school districts' enrollment is declining. In 2016, for instance, the Emmet O'Brien Technical High School unveiled a $94 million renovation -- even as the state considered closing two other technical high schools in the face of budget shortfalls. The renovation's cost exceeded the expense of constructing an entirely new high school. Connecticut bonded $77 million for the project.

The state considered a moratorium on new-school construction in 2011, ultimately abandoning the initiative because it would save only $9.5 million in the second year. Although this savings looks unimpressive when compared to Connecticut's enormous debt load and impending deficits, that fact does not, without more, justify forgoing any opportunity to treat taxpayer dollars with respect. Given the state's decline both in population and in school enrollment – coupled with large, looming deficits – it only makes sense to constrain this and other capital expenses.

See, for example, appendix A, B, C, D, E, F

Reform Affordable Housing Spending

Connecticut borrows significant sums in order to spend them on subsidized housing development. At a Bond Commission meeting in February 2018, for instance, commission members approved $13 million in borrowing in order to provide grants to private developers for housing projects in Canton and Bloomfield, at a cost of $160,000-$172,000 per unit. This is an unnecessary expense.
State leaders can address the need for low-income housing in a better, more cost-efficient way by expanding the state's rental-assistance program, which grants vouchers to low-income families. This approach would empower consumers, rather than enriching well-connected developers.

End Publicly-Funded Campaigns

In an era of fiscal crisis, the noble intentions of the Citizens Election Program (CEP) cannot justify retaining a campaign finance regime that both incurs considerable costs and has significant flaws. CEP is profligate with taxpayer money, mandating payments to candidates running unopposed as well as to those in whom the public has never evidenced much interest, diverting both resources and public attention from contested races or more popular candidates.

What's more, when CEP's payments to viable candidates are delayed – most often in cases of relatively less-well-connected challengers – it can constitute the death knell for an otherwise promising campaign. Nor have Connecticut's tough campaign laws succeeded either in keeping meaningful amounts of third-party money out of state elections or in stopping independent candidates from investing significant amounts of time in fundraising.

It is time to terminate a campaign finance program that is a drain on our state's treasury, even as it achieves few, if any, of its objectives.
Savings: Abolishing the CEP would save approximately $30 million in election years

Privatize More Social Services

All of us share a commitment to offering excellent social services to the neediest and most vulnerable among us. Too often, however, Connecticut and its municipalities offer services through inflexible (and relatively expensive) public agencies. It is time to allow the private or non-profit sectors to provide more social services, as they can do so more effectively (and thus more compassionately), as well as more cost-efficiently, than public agencies.

For example, in Connecticut, disabled and mentally ill residents are served through a pair of state agencies (the Department of Social Services, and the Department of Mental Health and Addiction

Services, respectively) as well as through private non-profit companies. As a result, there are two systems (the public and the non-profit) competing for both patients and employees.

Although the Department of Social Services and the Department of Mental Health and Addiction Services are two of Connecticut’s most expensive agencies and account for a significant portion of the state’s overtime pay, they still have difficulty servicing all those in need. There are currently 1,800 Connecticut families with members on a state waiting list for residential facilities.

The non-governmental entities outperform them – and do so at less expense.
Indeed, private, non-profit agencies have demonstrated repeatedly that they can do the same jobs as their public sector counterparts at approximately one-third the cost, and that they have a far greater ability to provide more people with high-quality care.

The Connecticut Community Non-Profit Alliance estimates the state could save $300 million per year by allowing services to be provided primarily through non-profits. Although the SEBAC agreement prevents any state employee layoffs until 2022, shifting more social services to private non-profit groups will not only save money in labor costs, but allow the state to reduce overtime spending by freeing up more state employees to cover more work shifts.

See, for example, appendix G & H

Tax Reform

Controlling state spending is of unparalleled importance. Spending cuts along are not enough. Connecticut's economy needs to grow. If a state with high fixed costs, like ours, continues to raise taxes and thereby chases taxpayers and businesses from the state, budget deficits are practically inevitable. Without retaining its existing businesses and residents – and attracting new ones – our state's downward economic spiral will almost surely continue.

Connecticut must become more competitive, right away. What follows are the tax reforms that will most quickly and effectively allow our state to begin to reverse the exodus of its residents and businesses (and the resulting erosion of its tax base) – so it can begin to grow again. Although Yankee Institute favors broad-based, structural tax reform, the specific tax changes set forth below constitute an immediate response to our state's present crisis.

Eliminate Estate and Gift Taxes

In a welcome reform, our state raised its estate-tax threshold in 2017; even so, Connecticut remains one of the few states with an estate tax and the *only* state with a gift tax. Although both gift and estate taxes are highly volatile and account for only a small amount of state revenue, their ripple effects are significant and detrimental.

Estate-planning attorneys have testified before the Finance, Revenue and Bonding Committee that they regularly help wealthy Connecticut residents move to states such as Florida specifically to protect against our state's outsized estate and gift taxes. By unintentionally motivating affluent residents to relocate, Connecticut deprives itself of significant pools of income-tax revenue, with spillover effects ranging from loss of human capital to reduced revenue from sales taxes (which would otherwise be paid by those forced to live elsewhere for six months and a day to avoid being classified as state residents).

The estate tax also has the unintended consequence of levying significant and punishing taxes on families whose wealth is based on land ownership or possession of some other illiquid asset. Because the tax applies to real and tangible business property as well as savings, farmers and small-business owners in Connecticut who may have land or other business assets, but less monetary wealth can find themselves crippled by the estate tax, forcing their heirs to sell off the property in order to pay the tax.

Connecticut was labeled the "Most Expensive Place to Die," by CNBC in 2015 – an unwelcome distinction for a state with an aging population, already experiencing significant taxpayer flight and struggling to pay its bills. Rather than addressing this issue by lifting the estate tax threshold once more – playing catch-up with the federal threshold, which was raised again since Connecticut's reform last year – the state should pursue a bolder, more permanent solution.

Like 36 other states, Connecticut should eliminate the estate and gift tax altogether. No other single reform would do more both to convince affluent taxpayers to retain their Connecticut residencies and to offer our state an important competitive advantage over neighbors like New York.

See, for instance, Appendix I, J, K, L, M

Broaden the Sales Tax Base

An important part of revenue-neutral tax reform would be to broaden the base of the sales tax while simultaneously lowering the tax rate. This would permit a lower tax rate to be more fairly and evenly applied across a range of goods and services with no loss of revenue to the state treasury.

Kentucky offers an instructive example. There, lawmakers broadened the base of their sales tax to include services like landscaping; janitorial services; pet care and grooming; small animal veterinary services; fitness and recreational sports; laundry; dry cleaning and linen supply; non-medical diet and weight-loss centers; limousine services; bowling; overnight trailer campgrounds; extended warranties; and other personal services.

Connecticut could broaden the sales tax base to cover similar services and consider including additional goods. Business-to-business services, however, should remain exempt from any effort to expand the sales tax base; subjecting them to sales tax would result in double taxation and have a dampening effect on our state's already-struggling economy.

See, for example, Appendix N

Enact Sensible, Competitive Corporate Tax Reform

For decades, Connecticut grew faster than most other states. Its competitive advantage lay in offering businesses and families a relatively low-tax, high-quality-of-life oasis centrally located between Boston and New York, with easy access to international ports. In recent years, this advantage has been squandered through repeated tax increases, coupled with failure to bring state and local budgets under control.

There are plenty of ways Connecticut can make itself attractive to potential entrants again. These include:

- *Rolling back the corporate tax changes imposed in 2015.* That year, Connecticut instituted combined reporting for corporate-income-tax filers, a move that was very unpopular with the business community because of its cost and complexity. Following this and other changes to the corporate income tax, the state added about $200 million a year to its corporate income tax receipts. In the meantime, hundreds of millions of dollars per year were expended to try – with limited success – to prevent Connecticut-based businesses from fleeing.
- *Eliminating the corporate-tax surcharge.* A ten-percent surcharge remains on the corporate income tax. It is set to expire in 2019. This surcharge should be allowed to expire as planned.
- *Allowing corporate carrybacks and extending carry-forwards.* Connecticut does not allow for net operating loss carrybacks, which hurts our tax competitiveness. This should change.

See, for instance, Appendix O

These tax reforms can be paid for by eliminating the targeted economic incentives that advantage government-favored enterprises at the expense of Connecticut businesses and taxpayers generally. The previous administration spent far more on such incentives than the state collected through the corporate tax increases, as a forthcoming Yankee Institute policy paper will document.

Simplify & Reduce Rates of Income Tax

The state's imposition of a multi-bracketed income tax in recent years has spurred an exodus of residents at the upper end of the income scale, resulting in tax revenue that was significantly less than expected and unanticipated budget shortfalls. It is time to send the message that Connecticut will no longer seek to exploit its highest earners by simplifying and reducing the state income tax.

Yankee Institute proposes moving toward two effective brackets: a zero-percent bracket (no state income tax owed) for the first $25,000 in federally taxable income earned ($50,000 for couples), with a five percent income tax rate for all income above that level. In the alternative, Yankee endorses the Commission on Fiscal Stability and Economic Growth's proposed income-tax reforms, as detailed in its March 2018 report.

Repeal the Business-Entity Tax

First enacted as a "temporary" measure in 2002, Connecticut's Business-Entity Tax (BET) proves the truth of the old adage, "There is nothing so permanent as a temporary tax." The BET charges a biennial $250 to every business in the state just for the privilege of operating in Connecticut. And it charges this flat fee without regard to the relative profitability of the business, thereby burdening start-up, struggling, and small businesses most heavily.

Bringing in less than $20 million per year, the BET sends a clear message to every job-creator contemplating a move to Connecticut: You *owe* the government $250 before you *earn* even one penny. In a state that finds itself in desperate need of growth and economic opportunity, this is unfortunate.

The state has been apt to dismiss the concerns about the BET raised by business and industry in recent years on the grounds that the tax is "nominal." It's worth noting that $250 is hardly "nominal" to a struggling small business, nor is this fee the only charge with which the state of Connecticut and its municipalities burden its businesses, year after year. Eventually, even "nominal" sums add up – and contribute, in their totality, to the bleak business climate that has characterized Connecticut for at least the last decade.

It is time to repeal the Business-Entity Tax – thereby assuring Connecticut's businesses that the state does not feel entitled to their money until they are at least earning some.

Structural & Administrative Reform

If good policies motivated by good intentions are to survive, they must be supported by good procedures, structures and institutions. Restoring Connecticut's prosperity will require elected officials and their staffs to make sound taxing and spending decisions – with an eagle eye out for all available tax and spending cuts – for years to come.

What follows are proposals that would increase the transparency of taxing and spending decisions and processes. Unaccountable, unfunded spending and irresponsible spending commitments have led our state into crisis. Only a rigorous focus on actual, sustainable revenues – and an ironclad determination to keep spending firmly within the limits of those revenues – can lead us out. The structural reforms Yankee Institute presents below are designed to help Connecticut's leaders stay focused on the state's actual resources and avoid being beguiled by tempting wish lists and limitless spending opportunities.

Require Zero-Based & Priority-Based Budgeting

The tax hikes of the recent years—which resulted in unanticipated revenue shortfalls—have demonstrated that taxpayers have already been taxed beyond their ability and willingness to pay. Further tax increases are simply not an option.

Connecticut's struggle to make ends meet over the last decade has resulted in its inglorious status as the state carrying the highest overall debt burden per citizen of any state in the union (with the exception of Alaska, which does not confront the fiscal peril besetting Connecticut because of its Permanent Wealth Fund derived from energy-extraction revenues). Clearly, neither additional taxes nor additional indebtedness is a solution to our state's fiscal woes.

Rather, it makes sense to examine the processes that embed mindless spending into the Connecticut budget. When a family goes shopping, it decides each week what it needs, sets priorities and budgets accordingly. But after the family's last baby has become a toddler, the family stops buying diapers. It would be foolish and unjustifiably wasteful to budget for and purchase diapers—with an annual five percent increase in the diaper fund—until the "baby" has graduated from college.

This scenario, however, is a useful analogy to current state budgeting techniques. State instrumentalities examine previous budgets, add money for new programs, and seek a general increase for other items. Only rarely does a subdivision of the state eliminate a line item as no longer necessary, insufficiently cost-effective, or a needless extravagance. The result is a one-way ratchet: government becomes increasingly expensive, regardless of the taxpayers' ability to bear an ever-expanding burden. This cycle must end.

One commonsense way to curtail the growth of government spending would be to prohibit agencies and other arms of government from budgeting for a new year based on the budgets of previous years. Instead, the state and its instrumentalities would budget from a "zero base," i.e., with the understanding that they will receive funding only if they can justify each line and item of their budgets, based on evidence of expected need for the funds sought for the coming year. Such an approach would weed out spending for "legacy" purposes, help agencies keep their budgets in line, and begin to curb an unsustainable expectation that spending must always rise.

As part of the zero-based budgeting process, the state and its instrumentalities would justify every spending request and include all relevant evidence. State auditors would then be empowered to reject requests that are unjustified or inadequately supported.

Agencies should also be obliged to prioritize their requests, ranking their proposed expenditures in order of importance. That way, if state revenues are insufficient to fund all properly justified requests in the coming year, agencies can nonetheless be fairly funded at a *pro rata* rate that will allocate money to the purposes that the agencies themselves have justified and identified as of greatest value to the state.

Washington State adopted a similar proposal in the last decade when facing a budget deficit similar to the one that now confronts Connecticut. The zero-based budgeting process was instrumental in closing that state's spending gap.

See, for instance, Appendix P

Those opposing this approach have argued that zero-based budgeting simply demands too much of the instrumentalities of government. Of course, this claim ignores the substantial demands that state government makes of the taxpayers who fund these agencies' budgets; surely it is not too much to expect government to demonstrate that the money it extracts from state residents is necessary and justified. And if an agency is truly in need of the funds it seeks and uses them effectively, it should be able to document its proper use of them without much difficulty, thus providing evidence of need for similar funding in the future.

Nevertheless, to demonstrate the efficacy and sustainability of zero-based budgeting, the state might try it as a pilot program in some well-suited agency or set of agencies. The process should be monitored by independent outside auditors to ensure that agency employees are undertaking their work in good faith, and with zeal and efficiency, to ensure a fair test of the program. The auditors can then report on the results of the test program. These results should include information about whether agency employees did, in fact, act with zeal and efficiency in performing their tasks, so that the state might respond to adverse worker-related results not by ill-judging the budgeting program, but rather by improving worker performance.

Meanwhile, recognizing that certain agencies might find it difficult to undertake zero-based budgeting in some cases or some years, the program should include an alternative for them when it is rolled out statewide. In any year in which an agency finds it impossible to perform zero-based budgeting, it might instead elect (actively or by default) simply to absorb a three-percent, permanent, across-the-board budget cut, which will then be built into any "automatic" (i.e., non-zero-based) future budget considerations.

Finalize Taxes & Revenues Before Setting Spending

The sequence of Connecticut's current budgeting process cries out for reform. Currently, the Appropriations Committee develops the state's spending plan independent of the Finance Committee's revenue estimates—and *before* it has even adopted them! This process is obviously backward. The state should first adopt revenue estimates, and only *then* appropriate the money it expects to collect, in accordance with the zero-based budgeting process outlined above. Like any Connecticut family, the state should finalize its revenues before it decides how much to spend.

Consolidate Agencies & Administrative Functions

Even with the best of intentions, over time, it is almost inevitable that some duplication of missions and services between agencies will occur. It therefore makes sense for the state to perform an audit of all state agencies to identify overlapping or duplicative missions and services among them. Where such overlap or duplication is found—or where agency functions could be "internally outsourced" to consolidated units providing the same services to a number of agencies—such efficiencies of scope, scale and specialization should be realized. This would allow the state to eliminate some unnecessary top- and middle-management positions, at the very least.

As agencies and their functions are consolidated, state commissions should likewise be dissolved. In 2016, state lawmakers consolidated several Legislative Commissions into the Commission on Equity and Opportunity and the Commission on Women, Children and Seniors. Taxpayers should not have to pay the state to lobby itself. The state could save $1 million a year by allowing these important interests to be represented by the in-state non-profit organizations already providing these services.

End Supersedence

Even among other union-friendly states, Connecticut is an outlier in the extent of the powers it grants to its government unions. A particularly egregious example of this phenomenon: collectively bargained government-worker contracts can actually supersede properly enacted state law. This has resulted not only in bargaining units exempting themselves from freedom-of-information laws, but also in contracts that actually override state laws designed to protect the public.

In addition, although contracts are required to list the statutes they supersede, subsequent contracts or contract-extensions frequently do not include the statute listings, even as the supersedence itself continues. This makes it nearly impossible for the public to understand which state laws or local ordinances have been overridden by contract—a violation of the spirit of transparency and open government.

The entire system of supersedence erodes the rule of law and undermines foundational principles of representative government. It fundamentally privileges one segment of society above all others, which are denied such special opportunities to override and countermand legislation enacted by the people's duly elected representatives. This unjust and unequal treatment should not stand. The legislature and governor should repeal Title 5, Chapter 68, Sections 5-278 (b) (d) and (e), *appearing at* https://www.cga.ct.gov/current/pub/chap_068.htm.

Set Pension Discount Rates to Average of Previous Decade's Performance

Aside from actual underfunding, nothing has contributed more to Connecticut's current pension-funding crisis than the state's refusal to acknowledge and account for the fact that since about 2002, the world economy has generated substantially lower nominal interest rates on a sustained basis than at any time since World War II. As a result, the state's fixed discount rates remained far too high for far too long; in other words, the state assumed that its pension-fund investments would grow at a rate much higher than they actually have. This phenomenon has contributed significantly to current shortfalls.

The problem has been addressed in part by recent reductions in the discount rate, including a decrease of the SERS rate from 8.5 percent to eight percent, and then even further to 6.9 percent. The TRS rate remains at eight percent, however, and the state seems prepared to use a bond-generated inability to extend its payment period to justify its failure to acknowledge reality: the TRS discount rate remains unrealistically high.

It is time to correct this problem, which combines a lack of transparency with insensitivity to real-world conditions. Yankee Institute therefore proposes that the discount rate for the three main pension funds (SERS, TRS and MERS) be set by statute as the *average of the rate of return actually earned in the preceding ten years*, to be reset on the same day each year as set in statute. This automated, floating discount rate would be far more realistic and aligned with the actual results achieved by the state in recent years. It would also disincentivize risky investment on the part of the state investment boards by creating real-world consequences, in the form of a lower future discount rate, for promiscuous and ill-considered risk taking.

Revoke Pensions for Crimes Committed on the Job

Currently, Connecticut has the power to revoke a state employee's pension only for financial crimes committed on the job—not for any other crime a state worker commits in the course of his or her employment, no matter how heinous.

This is financially unjustifiable and creates outcomes that are morally reprehensible. For instance, a former employee of the Department of Social Services raped two severely disabled women in his care for years before finally being arrested and convicted. He will nevertheless remain entitled to his pension—a fact confirmed by both the Attorney General's Office and the State Comptroller's Office. Likewise, several of the employees arrested for the extensive, sadistic abuse of William Shehadi at Connecticut's Whiting Forensic Hospital will remain eligible for their pensions.

Although episodes as grotesque as these are mercifully rare, on-the-job illegality occurs more often than any of us would like to believe. It's common sense: Connecticut's taxpayers should not be obligated to subsidize generous pensions and post-employment benefits for state employees convicted of illegal behavior *in the course of their work for those residents*. Other states have similar laws. This is a common-sense reform that is long overdue.

In 2018, the Senate passed an amendment authorizing the Attorney General to remove an employee's pension through court action, but the bill never received a vote in the House of Representatives. Such a law, revoking state pensions for those adjudicated convicted of crimes, makes financial, moral, and legal sense. And because the revocation would occur through the judicial process, it would not require any changes to the existing SEBAC agreement.

See, for example, Appendix Q

Reconfigure the Membership of State and Municipal Pension Boards

Connecticut's pension boards do not effectively represent taxpayers' interests. Aside from actuaries – who are themselves selected by union leaders and by the governor, respectively—all board members are either government-employee-union members or gubernatorial appointees. Thus, potentially *all* the members of the boards—and often a significant majority of them—are members of government-employee unions. These board members have vested, personal interests in maximizing pension benefits for employees and retirees, but only a limited and notional interest in representing the long-term interests of taxpayers who not only do not benefit from government-pension largesse, but who must subsidize that munificence.

Pension boards should be reconfigured to ensure that at least half the members not only possess expertise relevant to the boards' specific responsibilities but are likewise free of any self-interest in the boards' dealings—that is, are not government workers who will receive pension benefits. This will provide a block of voices and votes on the boards that are more likely to make informed, objective, dispassionate decisions on pension matters. In fact, in an optimal system, no pension board members would be voting on matters in which they had a personal interest. Under this model, government workers who expected to receive benefits would serve only as non-voting advisory board members.

Regulatory Reform

Regulation is an inevitable feature of the modern state; many business and private activities have spillover effects that modern governments have elected to police by regulation. Thoughtful, sensible and carefully constrained regulation can be a positive good. But overbroad, confusing and punitively-enforced regulation, by contrast, does significant and lasting harm by crippling enterprises that provide jobs, paychecks, benefits, goods and services. Like those they regulate, regulators are capable of error, and the regulatory process—like the fields it regulates—is hardly infallible; all are susceptible to errors, flaws and faults. They therefore benefit from the guidance provided by thoughtfully-constructed regulatory rules and processes. For too long, these rules and processes have been either overlooked or underdeveloped in Connecticut. The proposals below seek to rectify that oversight.

Convert DECD into an "Office of Regulatory Review and State Competitiveness" (ORRSC) with a New Remit

Whenever a business or individual in Connecticut must waste time or money to comply with unnecessary, overbroad, outdated, vague or otherwise inappropriate regulations, our state is mistreating its people. Whenever a potential entrant to Connecticut declines to move to the state because of its unfavorable regulatory regime and the costs it engenders, that is a missed opportunity for our state's economy to grow. And whenever hiring is stifled or a current resident leaves the state, the economy declines. Bad regulation hurts everyone in Connecticut, all the time.

At present, there is no good mechanism through which residents and businesses living and working in Connecticut can seek reliable relief from bad regulation. This must be fixed. Yankee Institute therefore proposes the creation of an Office of Regulatory Review & State Competitiveness (ORRSC) within the state's administration. The ORRSC would be tasked with reviewing and—when appropriate—revising or revoking regulation that is flawed for any of the reasons noted above (or for any other).

In its regulatory-review capacity, the ORRSC would be empowered to receive petitions for review from any members of the public seeking regulatory reform. These petitions would identify the regulation(s) challenged, the reasons for the challenge, and any evidence supporting the challenge. The ORRSC would review these petitions in a timely, statutorily-defined manner and period.

If it found the petition colorable (under a generally accepted, court-approved standard of colorability), the ORRSC would undertake a notice-and-comment process and either issue a revised regulation or repeal the regulation, as it deemed appropriate at the end of the review process. (Any failure to participate meaningfully by an agency within a reasonable, established period should result in a suspension of the regulation until the agency complies and participates fully.) The ORRSC would also be empowered to identify potentially ill-considered regulation and begin a process of review for that regulation on its own authority, without the impetus of a public petition.

In its state-competitiveness capacity, the ORRSC would be empowered to review Connecticut law to identify legal reforms that would boost the state's competitiveness or attractiveness to business or other investment without adding to state spending. The office would conduct its own studies into potential reforms and undertake a comment process, after which it would, if appropriate, propose draft legislation to revise the relevant statute(s). This proposed legislation would be referred to the relevant legislative committee for consideration, along with a report in support of the reforms written by the ORRSC. The office's remit in this field would be limited to proposed statutory reforms that would demonstrably improve the business climate in Connecticut by reducing the overall cost of living or doing business in the state and would either decrease state spending or have no impact on it.

In Section 1 of this Charter, Yankee Institute has discussed the failure of the DECD and its "targeted economic incentives" as currently constituted. Yankee therefore proposes the statutory withdrawal from the DECD of its current functions and authorities and recommends that all qualified and interested non-appointee employees of the current DECD be transferred to the new ORRSC.

Establish Regulatory Safe Harbors

Regulatory agencies should be required to conduct an audit of the regulations they have promulgated. These should be reviewed for duplication, antiquation, overbroadness, vagueness and other weaknesses, and voluntarily revised or withdrawn as appropriate by the agency, following normal agency processes, to redress the defects in the regulation. The agency should then prepare:

(a) a complete list of all regulations enforced by the agency, including a title, short explanation of the regulation, and a link to the relevant language and any supporting or explanatory authority; and

(b) "safe harbor" regulatory-compliance worksheets. These worksheets should identify the types of regulated entities to which they apply, in a manner so that every regulated entity qualifies for some safe harbor. So long as a regulated entity complies with the regulations indicated under the current, applicable worksheet, that entity would not thereafter incur fines or other penalties for non-compliance with any regulations not specifically indicated on the relevant work sheet, until the failure to comply is brought to the regulated entity's attention and a reasonable period to comply has been provided.

Until agencies have completed both (a) and (b), their authority to promulgate new non-emergency regulations should be suspended.

Require Mandatory Cost-Benefit Analysis for All New Regulations

For all new regulations promulgated by the state of Connecticut or any of its instrumentalities, the promulgating agency should be required to undertake complete cost/benefit analysis of the type required of federal agencies under Executive Order 12866 (1981) and its successors. No agency regulation would be deemed to be effectively promulgated unless it were to include a concrete, detailed, cost/benefit analysis, nor unless its quantified benefits, as demonstrated by competent evidence, at least outweighed its quantified costs, as similarly demonstrated. The cost/benefit analysis portion of a regulation would be subjected to the same review and comment process as is required for all other portions of a regulation. Moreover, all cost/benefit analysis would be subject to challenge at the ORRSC under the same rules as any other portion of a regulation. A successful challenge to an agency's cost/benefit analysis conclusions would result in the withdrawal of that regulation.

Eliminate the Minimum Bottle-Pricing Law

Connecticut alcohol can cost up to a whopping 24 percent more than in neighboring states. This is because it is illegal for all liquor industry businesses to sell below cost. Each month, liquor wholesalers set the bottle price and post it with the Department of Consumer Protection, and a wholesaler may not post a price less than the price for a case of bottles divided by the number of bottles in the case, plus an amount that depends on bottle size. Retailers are actually prohibited from selling below the "posted bottle price" plus delivery charges.

The excessive markup that occurs as a result of Connecticut's idiosyncratic and outdated minimum bottle-pricing laws hurts consumers, businesses and the state's economy. It forces consumers either to overpay for alcohol or travel out of state for alcohol purchases. Massachusetts liquor stores have even targeted Connecticut shoppers with "drive for savings" advertisements. This places in-state retailors at a competitive disadvantage and pushes tax money into neighboring jurisdictions.

Understandably, Connecticut's 1,150 small package stores lobby in favor of the law, which allows them to keep their prices competitive with those of larger stores. But this regulatory regime prevents consumers from having access to affordable alcohol and inhibits our state from competing with its neighbors. We should encourage price competition in Connecticut—not discourage or forbid it.

Connecticut is the only state in the country that sets minimum prices for liquor and wine in this manner. Yankee Institute has a simple, elegant proposal with the dual virtues of improving both the lives of Connecticut's thirsty residents and the competitiveness of its economy. Put the public interest before a special interest: eliminate the minimum bottle-pricing law.

Municipal Reform

Some of Connecticut's largest cities—and smaller towns—are in fiscal crisis. They struggle to provide minimally-adequate services for their people, despite charging high rates of property tax and (in some cases) having borrowed to the extent of their capacities.

Primary responsibility for this distressing status quo rests with the cities themselves, of course. Many are significantly mismanaged. Bridgeport, Waterbury and Hartford have all teetered on the verge of bankruptcy in the past; despite ample and dire warnings, city leaders found themselves unable or unwilling to institute the reforms necessary to avert crisis. Despite its close brush with insolvency, Hartford continued to provide massive lump-sum payments to retirees for unused sick time and—after pocketing a bailout courtesy of state taxpayers – backpedaled from efforts to move new hires to a defined-contribution pension plan. After increasing taxes on its residents, New Haven experienced a string of scandals involving bonuses for employees and the purchase of expensive uniforms for office assistants, while laying off teachers. These governments cannot be trusted with additional unrestrained fiscal authority, nor should they be rewarded for their profligacy.

Yet the state bears some measure of culpability as well. It has granted its municipalities only one tool with which to generate revenue – the property tax. This system works well in jurisdictions where land is privately held, property is valuable, and landowners are affluent. Municipalities with such advantages can keep tax rates low while still collecting all the revenue they need, and property owners are able to pay those taxes without difficulty. But this is not the case in municipalities where much of the land is held publicly or by charities like hospitals and private schools, and thus is not subject to property taxation. In those jurisdictions, tax rates must be much higher, because they are spread over a narrower base. The problem is only compounded in municipalities with relatively low property values, where each mill of property tax brings in a proportionally smaller amount of revenue. And the difficulties are further exacerbated if municipal residents are relatively poor, so that it strains their finances to pay these comparatively high tax rates.

No one need be reminded that, like some of its cities, Connecticut also finds itself in grim financial condition. Even if rescuing poorly-run cities made sense – and it does not – the state cannot afford any more bailouts, or even to increase the amount of cash aid it provides to cities. Any help the state can offer to municipalities must be provided on the cheap.

These are the considerations underlying the following proposal. The purpose of the package is to offer cities additional options for raising revenue while curtailing their most egregious excesses. It also aims to allow the municipalities to do more for its residents more cost-efficiently, creating wins for everyone.

I. Optional Municipal Tax Plan

As noted above, the current municipal tax structure, which relies entirely on a variety of property taxes, is both inefficient and unfair in many locales. Yankee Institute therefore proposes authorizing municipalities to enact, at their discretion, a local sales tax of up to one percent. This sales tax authority should be of the greatest relative value in towns where property values are currently low, and where much of the property is untaxed because it is state- or charity-owned. This includes Hartford and the state's other hardest-pressed cities.

In presenting this proposal, however, we recognize that many of Connecticut's municipalities must be restrained from worsening their situations by simply heaping additional taxes onto already overburdened populations without cutting their unbalanced and excessive property taxes. Yankee Institute therefore proposes that each municipality that accepts the sales-tax authorization be required to cut its real property taxes to, *at most*, 90 percent of what those property taxes were on January 1, 2017. Using a past date as the baseline is important, as it will prevent municipalities from gaming the process by raising tax rates significantly in anticipation of the pending cut.

It makes sense to reduce every participating municipality's property taxes by 10 percent for a number of reasons. A uniform statewide cap (of, for example, 50 mills) would result in massive revenue cuts to some of Connecticut's most financially challenged governments while providing no cap at all in other jurisdictions where high property values allow tax rates to remain low. At the same time, however, a 10 percent cut will yield the highest absolute rate cuts in the areas that need relief most – places where the millage rates are highest.

Yankee Institute proposes eliminating the car tax and other personal property taxes on private (non-business) taxpayers for participating jurisdictions, because these taxes are both regressive and expensive to administer. In addition, any municipalities that find their new tax structure results in revenue more than 10 percent higher than that which the property-tax-only structure provided in the last full year of its enactment (adjusted for inflation) should be required to phase out their personal property taxes on businesses. This could be achieved either by increasing the exemption; decreasing the types of personal property to which the tax applies; or in any other ways that would keep inflation-adjusted tax receipts of the jurisdiction no more than 10 percent higher than benchmark-year receipts, until all personal-property taxes have been eliminated. After eliminating all personal-property taxes, if towns find that they are still bringing in more than 10 percent more income than they raised under a property-tax-only regime as a result of accepting the sales-tax facility option, they would be permitted to keep this extra revenue. We will assume that municipalities so situated were those particularly ill served by the property-tax-only regime and consider this additional revenue a positive benefit of the added tax-base flexibility.

Finally, we permit municipalities to elect to maintain property-tax-only regimes at their discretion because some communities already tax at sustainably low mill rates, while containing few entities that undertake transactions that would be subject to sales tax. If forced to participate in the program, these municipalities would find their taxing facilities artificially cut and capped without, in turn, receiving a compensating taxing authority that would effectively make up for the lost revenue. This would only drive currently healthy communities into unproductive deficit for no discernible purpose. The objective, of course, is only to increase flexibility and fairness without adding to citizen tax burdens, not to cripple any communities.

To ward against non-compliance with the property and sales tax caps described above, we ask the legislature to begin the process of writing those caps into the state constitution; authorizing and requiring the Municipal Accounting Review Board (MARB) to take control of the taxing authority of any jurisdiction that violates those caps; and to reset tax rates to comply with the caps. To ward against non-compliance by the legislature (in transferring sales tax revenues to the municipalities as promised) we propose that factor be written into the state constitution, as well.

It cannot be emphasized strongly enough: the offer of a sales-tax facility for participating jurisdictions is made <u>in exchange</u> for the property tax reduction and cap, along with the other provisions detailed above. The Yankee Institute would emphatically oppose granting municipalities any sort of additional taxing authority absent the exchange detailed here.

In sum, then, for municipalities that opt into the program:

A. Cut & cap property taxes

- Cap municipality real-property taxes at 90 percent of levels on January 1, 2017 (or some other day prior to the introduction of this plan, so that municipalities cannot manipulate the caps by increasing rates before the cap is applied) for participating municipalities. The cap is designed so that all participating municipalities make a proportional cut.
- Initiate a constitutional provision to incorporate these caps permanently for participating municipalities.
- Until the constitutional provision is ratified, sanction any municipality that exceeds its cap by removing taxing authority from the municipality and placing it under the authority of MARB.
- Instruct MARB to honor the caps until they are constitutionally mandated.
- Eliminate personal/tangible property tax for non-businesses; reduce and/or phase out the tax for businesses per the outline above.

B. Replace with limited sales-tax authority

- Grant participating municipalities the authority to levy a sales tax of up to one percent, capped at that amount.
- Initiate a constitutional provision to incorporate the one-percent cap on participating municipal sales taxes permanently, while also obliging the state to distribute these revenues to participating municipalities each year.
- Until the constitutional provision is ratified, sanction any municipality that exceeds its cap by removing taxing authority from the municipality and placing it under the authority of MARB, unless the state fails to remit to the municipalities the entire amount raised pursuant to the sales tax authority.
- Instruct MARB to honor the caps until they are constitutionally mandated.

II. Municipal Flexibility

Another way Connecticut can help municipalities help themselves is by reducing the obligations and constraints that burden them. Right now, towns are laboring under the weight of myriad state-dictated restrictions that make it extremely difficult for them to bring their budgets under control. These include constraints on how they bargain with their employees; how many employees they must retain; where their employees can work; how they can change their charters; whether and how they can consolidate their schools; what wages they must pay contracting parties; and much more. It is time to free our many capable, responsible municipal leaders from the shackles of state micromanagement.

Many commentators have observed that Connecticut's 169 municipalities function inefficiently by providing so many services themselves, rather than consolidating them (or joining with overlapping school districts) to create efficiencies of scope and scale. Many fewer have recognized that the municipalities' failure to undertake voluntary regional cooperation stems largely from state-driven restrictions that hinder cooperation and make its benefits difficult to realize. The reforms Yankee Institute proposes below are designed to make it easier both for municipalities to cooperate with each other in providing services and to reap meaningful savings from thoughtful coordination. This is healthy regional cooperation, which reduces the burdens and costs of government rather than adding a new, expensive level of government with the attendant bureaucracy, expense and red tape.

A. Eliminate the Minimum-Budget Requirement

Currently, with a few abstruse exceptions, Connecticut enforces an ill-considered and opaque set of minimum-budget requirements that force municipalities to maintain certain levels of school spending, regardless of the actual needs of the schools and districts required to do the spending. In particular, the requirements fail to take reasonable account of the fact that some schools and districts have seen significant decreases in enrollment in recent years—which fully justify reduced school budgets. Moreover, minimum budget requirements make it difficult for municipalities to benefit financially from sensible and quality-enhancing consolidation or cooperation projects either with other school districts or with their own municipalities (for example, by merging school district and municipal maintenance, book-keeping and other non-educational facilities and staffing).

Minimum-budget requirements should ultimately be eliminated altogether. Although the state plays a legitimate role in ensuring that schools achieve certain minimum educational *results*, these results are not dictated by spending levels: beyond a certain threshold level, education spending does not provide a reasonably germane proxy for education results. As results are and can be regularly measured by student testing and graduation and post-graduation results, there is no justification for using spending as a proxy for results. What's more, it is aggressively harmful to municipalities' and school districts' efforts to secure excellent results for their students in an economically efficient manner.

Until minimum-budgeting requirements are completely eliminated, the state should at least establish zero-based minimum-budget rules that include variables for vital cost components such as the number of students served, and facilities maintained by school districts. They should be designed to reward municipalities for efforts to consolidate schools, districts, and the provision of services in rational and quality-enhancing ways. The metrics should also be generally available and publicly derived so that school districts, municipalities and other interested parties can contribute to their development and published to all parties so that municipalities can determine their own obligations according to an open, public, transparent and predictable process.

B. Increase Municipal Flexibility to Alter Municipal Employees' Retirement System (MERS) Provisions Unilaterally and/or to Exit MERS

For municipalities to be able to decrease costs through voluntarily combining services and other measures, they must be granted flexibility to reduce their greatest cost center: employee pay and benefits. If shared services are to work, it *must* mean creating economies of scope and scale, which *must* mean some reduction of the total number of municipal workers in the various areas of employment. Municipalities must therefore have the option of laying off redundant workers for whom other jobs in their skills areas cannot immediately be found.

Of course, all reasonable measures should be adopted to prevent layoffs; no one wants to lay off workers who can serve the public in other necessary positions. The legislation that grants municipalities the ability to lay off workers when necessary should also authorize municipalities to offer workers jobs outside the localities within which they were hired, and to establish an inter-town job bank that would facilitate such re-assignment offers. (Workers would not, of course, be obliged to accept such offers, but their failure to accept would result in unemployment, not – as currently – in costly, paid non-work within their current locality.)

Municipalities should also be granted the flexibility to reform retirement benefits (both pension and non-pension) for current and future employees for all work not yet performed by those employees, as a means of maintaining municipal solvency and ensuring that the municipalities can effectively balance the interests of all its constituents (not just government employees) while protecting government-employee benefits that have already been earned. This could be achieved by allowing municipalities to opt out of MERS altogether, or by creating this flexibility within the MERS umbrella. Such an initiative could include passing decision-making authority for MERS to the towns.

See, for instance, Appendix R

C. Increase Municipal Authority to Amend Town Charters

Their organizing charters present another hindrance to municipalities in their efforts to implement spending reform and voluntary regional co-operation. These charters, which are difficult to amend, often contain language that requires municipalities to maintain local offices that could better be regionalized or that otherwise thwarts reform efforts. Yankee Institute proposes that the new government pass legislation permitting municipalities to open their charters for limited, pre-specified purposes, including the removal of antiquated language compelling towns to maintain unique facilities that might more efficiently be shared by communities.

D. Increase Municipal Authority to Consolidate Schools/School Districts and to Consolidate Service Provision Between Municipalities and Overlying School Districts

The education system drives local costs in large part. This is unremarkable, as Connecticut's municipalities *ought* to equip its students with a high-quality education. Of course, this costs money. It need not, however, cost as much as Connecticut's towns are spending. Voluntary consolidation of the state's least-efficient schools can result in a high quality of education at a lower cost – but consolidation will not occur unless the process is reasonably manageable, and the towns can realize the potential savings resulting from consolidation.

This requires granting towns the same flexibility to lay off and re-assign TRS employees that it should have for its MERS employees, as set forth above. It also requires allowing towns to be able to sell, lease or otherwise repurpose school lands and buildings once consolidation has occurred, and to be able to divide the proceeds arising from those decisions as they determine in their consolidation agreements.

Relatedly, the state should permit schools to consolidate specialized educational services (including services to special-needs students) without having to undertake full school consolidation. Towns should likewise have the option of consolidating the provision of non-educational services (such as grounds- and book-keeping) with overlying school districts as an additional cost-saving measure.

E. Eliminate Binding Arbitration for Municipal Negotiations / Police and Firefighters Excepted

Municipal aid is the largest non-fixed cost in Connecticut's state budget. As a result of Connecticut's ongoing budget crisis, many municipalities have received (and are likely to continue to receive) less funding from the state for education, infrastructure and payment-in-lieu-of-Taxes (PILOT) than either they have come to expect or to which they feel themselves entitled. This forces more of the costs of municipal government onto the shoulders of local taxpayers.

As municipalities bear increasing portions of total municipal spending, they should likewise have increasing autonomy to restrain that spending. But nothing does more to take a town's fiscal destiny out of its own hands than binding arbitration, and the mandatory pay raises and benefit increases that local-employee unions are able to extract from the arbitration process.

As it is practiced in Connecticut, binding arbitration vests a single, unaccountable arbitrator with the power to overrule a democratically-elected municipal government in a contract negotiation with its unions—thereby forcing the municipality to spend more on labor and benefit costs than it can afford. In 2017, for example, even as Hartford wobbled on the threshold of bankruptcy, an arbitrator awarded the city's Municipal Employees Union a 6.25 percent pay increase, although Hartford could only afford a 5 percent increase. The decision cost Hartford another $1.1 million that it simply did not have. A similar outcome in Waterbury the same year cost the struggling city $2.4 million.

Unlike neighboring states, Connecticut allows binding arbitration for all municipal unions, from librarians and teachers to firefighters. Striving to appear neutral, arbitrators rarely side completely with one side or the other on all issues under arbitration, so municipalities are virtually guaranteed to have to pay more as a result of having entered arbitration than they otherwise would have.

In short, binding arbitration prevents municipalities from negotiating from a position of strength and taxpayer interest. This is particularly important for Connecticut's distressed municipalities, including most of its major cities.

Massachusetts, New York and Rhode Island allow binding arbitration only for public-safety unions such as police and firefighters. New Jersey instituted a 2 percent cap on arbitrated wage increases, making the process less palatable for labor unions. It is time for Connecticut to follow the lead of its closest regional neighbors.

At the very least, arbitrators should be barred from considering a municipality's reserve funds when determining its ability to afford a contract. Reserve funds allow municipalities to save for projects or fill budget gaps without raising taxes, and essentially function as local taxpayers' savings accounts for the town or city. They should not be used to pay for large, often retroactive pay raises for employees.

See, for instance, Appendix X

F. Decrease the Number of Topics Subject to Collective Bargaining

In most states, government employees negotiate about their wages; pensions, other retirement benefits, and many of their work and other rules are set—not through the opaque, back-room and self-interested process of collective bargaining—but by statute and/or ordinance. Connecticut should adopt this approach. In particular, along with the specific lay-off authority proposed above, the state should grant municipalities the authority to set non-compensation employee benefits, employee work rules and other details of municipal employment by ordinance, with such ordinances to become effective at the close of the present municipal contracts.

G. Enact Two-Year Prevailing-Wage Holiday and Relaxation of Set-Aside Rules

Prevailing-wage rules, enforced by the state, require municipalities to pay high minimum rates for skilled labor when they maintain infrastructure or build improvements, rather than paying what the market will bear. These rules are remnants of the Depression era, with all the obsolescence their age implies. In an era when Connecticut's state and municipal budgets are squeezed on all sides, even as its infrastructure ages out of its safe and useful life, prevailing-wage windfalls for special-interests are a foolish luxury that no one should be forced to subsidize.

Yankee Institute therefore proposes a prevailing-wage holiday for two years: all projects commenced within the two-year holiday would be free from prevailing-wage obligations, regardless of when the projects or the work on them are completed, or even when the final agreements for the project are signed. This will allow municipalities a window in which to plan and budget for projects to revitalize their communities at market rates, benefiting all citizens and treating their tax dollars with fairness and respect.

See for instance, Appendix T

While the prevailing-wage holiday is in force, its impact should be studied, with the state set to extend the holiday or make it permanent if a neutrally-conducted, unbiased study demonstrates that suspension of prevailing-wage rules results in high-quality outcomes at lower cost. An interim step toward making the holiday permanent would be to raise the threshold at which prevailing-wage rules apply to all projects (whether new construction or repair and renovation) to exclude smaller projects (setting the threshold at, perhaps, $5 million), and then indexing it to inflation.

The state should also move either to relax construction set-asides or at least to broaden the geographical areas from which the recipients of set-aside contracts can be based, so that municipalities can seek best offers from a wider range of qualifying firms.

Education Reform

In sharp contrast to so many other areas of state and municipal policy these days, Connecticut's education system is not in crisis. Even so, there are exciting opportunities for inexpensive, readily achievable reform that can improve educational opportunities and outcomes for all of Connecticut's students, particularly those who are most vulnerable to failure. Education is an area in which Connecticut's "steady habits" have served it well in the past; however, it may be time to consider some of the cutting-edge innovations that have shown real promise, and delivered real progress, in many of our sister states.

Establish Tax-Credit-Funded ESAs (Prudence Crandall Scholarships)

Education Scholarship Accounts (ESAs) are state-supervised spending accounts that parents use to pay for a variety of approved educational services. With an ESA, parents direct their child's education funding to state-approved schools, courses, programs, and services of their choice. ESAs champion a personal approach to education, where the goal is maximizing each child's natural learning abilities. Unused funds from each school year can be saved for future K-12 or in-state college expenses.

Rather than limiting families to any one particular school, ESAs empower parents with a menu of options from which they can choose. For example: a child with special needs could use the scholarship to attend private school and receive therapy on the side. Another child could learn math and science online, study English and foreign language at home, meet with a tutor twice a week, and save leftover money for future approved education expenses. With an ESA, education is no longer "use it or lose it." Parents decide where the best values are and can direct their child's funds in the most personalized and efficient way.

ESAs currently operate in five states, while more than two dozen other states have introduced legislation to establish their own ESA programs. **These programs save state money,** because the maximum amount awarded to each student is less than the amount spent per-student in a public school.

ESAs work as follows. Businesses and individuals are permitted to donate to nonprofit organizations that provide ESAs to students. In return for their donation, these taxpayers become eligible for a dollar-for-dollar, 100 percent credit against their state income taxes. The program could begin with a cap of $25 million, while adjusting each year thereafter to match parental demand. Eligible students would apply for ESAs and use them at no cost to their parents.

Eligible students should, in the first instance, come from families who are most likely to benefit most from the program and to be disadvantaged by current arrangements. These include students whose families have incomes lower than twice the threshold for participation in the federal free- and reduced-price lunch program (roughly $90,000 for a family of four); those who are diagnosed with a learning disability; or those who come from military families.

Yankee Institute proposes naming these scholarships in honor of Prudence Crandall, who is commemorated with a statue in our state Capitol building. Raised in Canterbury, Connecticut, she fought for women's suffrage and for civil rights and educational opportunities for all Americans—especially the most disadvantaged—facing down the power structures and public opinion that actively and passively deterred such goals. Prudence Crandall is a worthy namesake for a modern educational reform that could offer hope and opportunity to so many of our children who need it most.

Enact Tax Credits for Homeschoolers

It is estimated that more than 1,700 Connecticut students between the ages of five and 17 are homeschooled. This is a miniscule proportion of the total number of our state's school children—estimated at .26 percent of the total school population. But families who exercise their right to homeschool continue to pay full state and local taxes to support schools they do not use, while also bearing the necessary costs of homeschooling, which can exceed $1,000 per year for books, supplies and enrollment in a homeschool program.

Homeschooling costs are much less than families pay in state and local taxes. A tax credit in the amount that families reasonably spend to homeschool their children would offer those families some relief without significantly burdening the state. Currently, 15 other states offer a tax deduction for home schooling expenses, and Connecticut should consider doing so, as well.

See, for example, Appendix U & V

End Separate Funding Formula and Process for Charter Schools

In Connecticut, charter schools are funded separately from other public schools, in a needlessly burdensome process that places them at unnecessary and constant risk of under- or non-funding. This does a grave injustice to the children who attend public charter schools, their families, and the hardworking educators who staff them. Constant financial insecurity and extra procedural hurdles would not be countenanced in any other area of state-sponsored education; it is wrong to subject charter school students and families to a host of significant disadvantages, all in an effort to placate a vocal special interest – one that should be dedicated primarily to the task of educating our children, but which too often demonstrates that it prioritizes other, more self-interested goals. Charter schools should be funded as part of the general Education Cost-Sharing formula.

Prohibit Unionization of School Principals

Massachusetts abolished unions for public-school principals in 1993 as one feature of a very successful education-reform effort. Recent reports highlighting the difficulty of removing underperforming or ineffective principals in our state, along with the success Massachusetts has achieved in educating low-income and minority students compared to Connecticut's poor results in this area, indicate there is wisdom in heeding the Bay State's experience on this issue.

School districts should be granted immediate authority to de-unionize principals and other school administrators as soon as contracts permit.

Reform Teacher Pensions

Teachers' Retirement System (TRS) reform should proceed in accordance with proposals set forth elsewhere in this Charter in general, and regarding SERS and MERS in particular. Workers should be moved to a defined-contribution plan, or at least to a hybrid plan. Such a hybrid plan would have two parts: a defined-benefit portion that shares costs and risks equally between the employer and employees; and a straightforward defined-contribution portion—or an effective equivalent—with an employer contribution. (Recent reforms in Michigan provide a useful model of a sustainable hybrid plan.) This shift should encompass not only new workers but also work not yet performed by current employees.

At the very least – immediately—teacher contributions should be raised significantly. Teachers in Massachusetts currently contribute 11 percent of pay toward their pensions; in Connecticut, the rate is only 7 percent.

Other reforms could include returning Connecticut teachers to the Social Security system and indexing COLAs for retirees to a reliable inflation indicator up to the level of its current cap. Tailoring pension benefits to account for COLA increases in years when there has been little or no increase in the real cost of living likewise merits further study.

TRS also maintains a discount rate at odds with reality. Currently, the fund assumes an 8 percent rate of return on its investments. But TRS returned only 4.8 percent between 2006 and 2016. The gap between the assumed discount rate and real, proven rates of return means that even as the state teeters annually on the brink of insolvency in its efforts to pay the required amortized amounts to catch up on pension funding—it is still falling further and further behind. The next stock market downturn (and there will inevitably be one) will only exacerbate this shortfall; the underfunding crisis; the extent of the state's unfunded liabilities; and the difficulty Connecticut confronts in ever attaining financial health. (Additional discussion of discount rate reform can be found in Section 3E of this Charter.)

Unfunded liabilities in the Teachers Retirement System threaten to grow far faster and more significantly than those of any other state pension fund. Connecticut is currently considering whether it makes sense to transfer state property assets or the lottery system to TRS. Although such measures could help bolster TRS, they will only do so if the state continues to make its currently scheduled payments and does not use the asset transfer to lower payments. These payments are scheduled to jump as much as $6 billion per year—an amount completely unaffordable for Connecticut state government. Reform is urgently required.

See, for example, Appendix W & X

Appendices available at yankeeinstitute.org/charterforchange2019

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