RIPEC

Comments on Your Government

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Summary of the Governor's FY 2012 Budget Request

This RIPEC Comments outlines the Governor's FY 2012 budget request and summarizes key policy issues RIPEC has identified. The proposed FY 2012 budget includes all funds expenditures of $7,661.3 million, a decrease of $202.9 million (2.6 percent) from the FY 2011 enacted budget. The majority of this decline is attributable to the loss of federal ARRA funds. Fiscal 2012 general revenue expenditures total $3,169.8 million in the proposed budget, an increase of $227.7 million from the FY 2011 enacted budget.

The following highlights some of the comments contained in this report:

- Budgets are a state's central policy document and must reflect the priorities of the government and, thus, its citizens. As such, RIPEC believes it is appropriate to consider how the proposed budget defines the state's priorities and whether resources are directed to those priorities which reflect the needs and concerns of Rhode Islanders.

- In addition, budgets must account for out-year fiscal implications of spending and revenue decisions to ensure continued delivery of services. As proposed, the Governor's budget includes significant out-year deficits that may be understated given recent revisions to the state's pension obligations.

- Health and human services – and, in particular – Medicaid benefits – continue to be the primary driver of the state's structural deficit as growth in these areas outstrips projected revenue growth. Reforming these systems, while maintaining their integrity, should be a top priority for the state.

- The proposed budget contains a number of one-time adjustments including deferring the repayment of $22.0 million to the state's Rainy Day fund, supplanting $32.3 million in general revenue funds with federal EduJobs money, and $7.7 million in one-time expenditure savings through the state's participation in the Earlier Retiree Reinsurance Program through the Affordable Care Act.

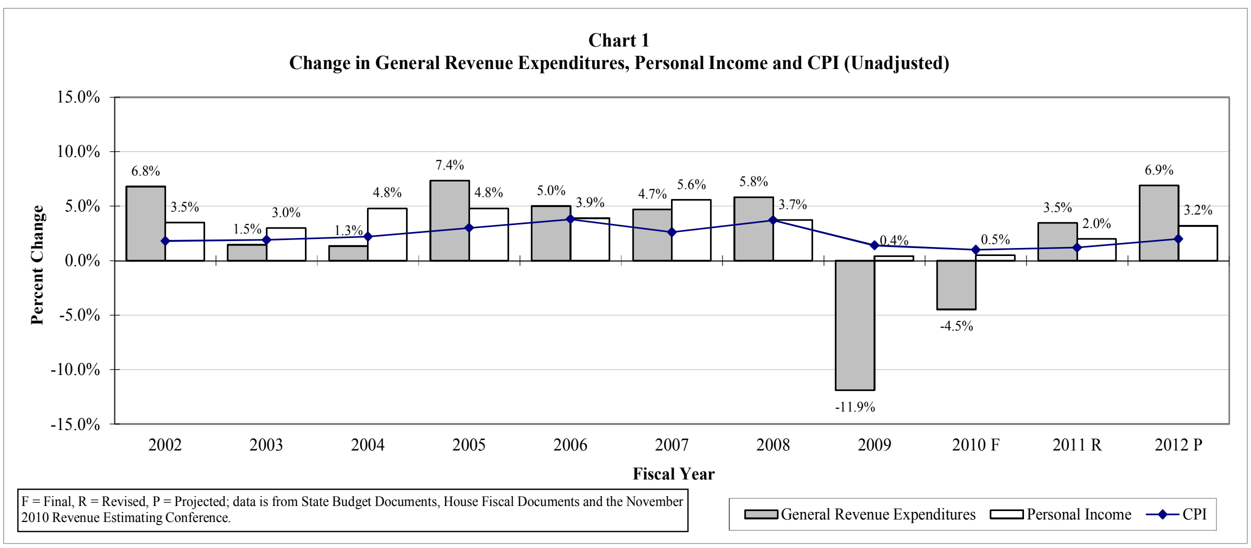
- The May Revenue Estimating Conference projected an increase in revenues over the November estimates. RIPEC believes these resources should not be used to restore cuts to the budget or to implement new programs. Rather, they should be used to maintain the budget's bottom line without additional tax increases, or to offset future projected deficiencies.

RIPEC Comments

The Governor's budget report documents that the FY 2007 budget process began with a projected deficit in excess of $300 million, of which $230 million appears to be related to expiring American Recovery and Reinvestment Act (ARRA) funds the majority of which is the enhanced Federal Medical Assistance Percentage (FMAP). This revenue-expenditure gap is resolved through a combination of revenue increases, expenditure increases and cost-shifting.

Both proposed FY 2011 and FY 2012 budgets include general revenue growth that is higher than projected growth in personal income and CPI in contrast to years prior. Proposed FY 2011 general revenue expenditures of $2,965.3 million are 3.5 percent higher than FY 2010 final spending while proposed FY 2012 general revenue expenditures total $3,169.8 million, an increase of 6.9 percent compared to the FY 2011 revised budget.

In both FY 2009 and FY 2010, general revenue expenditures declined relative to the year prior; however, these declines were largely related to the state's use of ARRA funds to supplant general revenues, rather than meaningful structural change. Other changes have started to address some of the primary budget drivers, but growth in these areas continues to outstrip current and projected revenue growth.



The past three fiscal years have seen historic revenue declines that have exacerbated the state's persistent structural deficit. Rhode Island's economic and fiscal future remains uncertain; while there are signs that the state is beginning to see an improved economic outlook, most signs point to a protracted and uneven recovery. As the state recovers from the recent economic downturn, it is essential it develops a spending plan that is affordable, sustainable, and fiscally responsible. Such a plan will help Rhode Island develop a fair and competitive economic and tax climate, one which will foster economic development and ensure necessary resources to support essential programs. In order to achieve this goal, Rhode Island must focus on controlling the rate of growth in spending, setting investment priorities, and effectively managing its limited resources. RIPEC's budget analysis highlights areas of key concern that warrant particular attention as the state works to craft its revenue and spending plan for the coming fiscal year.

Defining a Strategic Vision for Rhode Island

Budgets are fundamentally policy documents that should define a state's economic and social priorities within the confines of available resources. For too long, the state has been unable to make strategic policy decisions designed to stimulate growth, support essential services and provide funding for long-term investments. While the recent recession had a clear – and historic – impact on the budget, Rhode Island's structural budgetary issues have been a consistent part of the state's fiscal landscape for the better part of the past decade.

The Governor's budget outlines a number of broad policy objectives, such as establishing a secure foundation for the state's transportation funding system, reforming and restructuring health and human services programs, requiring fiscal accountability and transparency at the local level, modernizing the state's sales tax system, and fully funding the recently-enacted education funding formula. The budget the Governor has put forward is a starting point for discussions regarding a shared vision for the future of Rhode Island.

In evaluating these proposals, RIPEC recommends that the General Assembly use the following questions as a guide:

- Does the state's budget have the capacity to adequately fund proposed services or should the implementation of some programs be delayed until the state's fiscal capacity is improved?
- Is program support based on priority, and are service levels and program eligibilities prioritized to meet the state's current policy objectives?
- In which areas could the state benchmark its spending and performance in order to adjust spending limits or improve results?
- How can the state ensure that services are provided effectively, and that agencies, providers and other participants are held accountable for outcomes?
- Are the state's spending and revenue priorities designed to promote economic growth or could they be realigned?

Budget Drivers

"The Fiscal Survey of the States, 2010", published by the National Association of State Budget Officers (NASBO) and the National Governors Association (NGA), notes that Rhode Island's enacted FY 2011 general revenue expenditures of $2,795 per capita are 33.8 percent higher than national general revenue expenditures per capita of $2,089. RIPEC has identified a number of trends that appear to be the main drivers of the state's total spending: human services, personnel, and local aid. If the state is to address its structural deficit and move toward a sustainable budget, growth in these categories, or in specific areas within these categories, must be addressed.

<u>Health and Human Services/Medicaid</u>

Rhode Island continues to be an outliner with regard to Medicaid expenditures; the RIPEC report "How Rhode Island Expenditures Compare" shows that the state is now the highest in vendor payments per capita and has experienced some of the fastest growth in this category in the nation. Information from the Kaiser Family Foundation indicates that Rhode Island has the highest per-enrollee Medicaid spending in the country; Medicaid spending per enrollee in the state was 52.6 percent higher than the national average in FY 2008. Of every new dollar spent by the state since FY 2002, $0.52 has gone to support grants and benefits, and 74.0 percent of this growth is related to increases in medical assistance expenditures. While it is commendable that EOHHS has undertaken a thorough review of the HHS system, and has worked to refine the programs under its purview over the years, the state and its agencies must continue to act to get these costs under control and bring Rhode Island expenditures in line with neighboring states.

Personnel and Retirement

Since FY 2002, personnel expenditures have increased by 17.7 percent, the second largest increase in the budget outside of medical assistance. Of the $252.2 million increase (adjusted) in personnel spending, approximately half is related to growth in the state's retirement expenditures. The recently-completed experience study of the Employees Retirement System of Rhode Island (ERSRI), which reviewed current actuarial assumptions and compared them to actual experience, indicates that the state's annual required contribution (ARC) will rise significantly over the next few years due to changes in actuarial assumptions such as life expectancy and the projected rate of investment return.

Another aspect of personnel costs that will become an increasingly significant issue in the future is the state's funding of its other post-employment benefits (OPEB) liability on an actuarial basis. Funding these on an actuarial, rather than a pay-as-you-go basis, is a prudent fiscal step; however, these costs will continue to increase rapidly over the next 30 years as the state pays down its unfunded liability.

As these costs increase, they will crowd out other expenditures. As such, it is necessary that the state pursue fundamental reform of the system in order to ensure not just long-term sustainability of the pension and OPEB systems themselves, but to allow the state to formulate – and follow through with – strategic policy objectives. At the same time, the process must take into account how changes will affect the composition of the state's workforce and, in turn, how this will affect the state's ability to deliver essential services.

Local Aid

While local aid has declined since FY 2008, due to the elimination of general revenue sharing, the reduction in the motor vehicle excise tax reimbursement, and cuts to state aid to education, local aid remains the third largest share of the state's budget. When local spending is considered, education and municipal expenditures rival the state's total budget.

Fully funding the state's recently-enacted funding formula is an important step towards providing a predictable and stable source of funds to local governments. Moreover, the Governor's support of the funding formula demonstrates a commitment to making a strategic, long-term investment in the state's future. At the same time, RIPEC would urge the state to consider looking into a dedicated source of funds for this program in order to ensure its stability.

The municipal accountability, stability and transparency (MAST) fund represents an important first step towards municipal fiscal sustainability. However, the pension and OPEB ARC requirements as proposed will have the effect of putting increased fiscal stress on those communities least able to respond. If the state is to require local governments to fully fund their pension and OPEB obligations, they must provide local governments with the ability to make fundamental changes to their cost structure similar to the actions already taken by the state.

Revenue Increases

The Governor's proposed budget includes net revenue enhancements of $162.3 million. Of this amount, the majority ($155.7 million) is related to changes in the state's sales and excise taxes. The Governor's proposal to lower the rate from the current 7.0 percent to 6.0 percent and broaden the base may have the effect of creating a more stable revenue base than the current formula, which is highly subject to changes in the state's economic climate. At the same time, expanding the tax to certain items, such as manufacturing inputs, may have a negative impact on businesses in the state. Increasing the cost of doing business in Rhode Island for certain recovering industries may have a dampening effect on the state's economy and changes should be made with caution.

As with the proposed changes to the state's sales tax, there are a number of significant proposed changes to the corporate tax. Rhode Island is recognized as having one of the highest corporate tax rates in the country and lowering the rate may result in improving the state's image within the state and throughout the country. However, the proposal to implement combined reporting should be carefully considered with regard to how it would affect current businesses – particularly those with large capital and payroll investments in the state – and their ability to expand without a change in the apportionment formula. In addition, the change from a franchise fee to a gross receipts tax deserves closer scrutiny; while the proposal may lower the tax burden for some entities, there is limited information on the effect this tax may have on businesses.

New Programs and New Revenues

The Governor's budget includes a number of new initiatives, such as the MAST fund, Tourism Asset Protection (TAP) fund, dedicated funding for the State Department of Transportation (DOT), and the full implementation of the education funding formula. In addition, as noted above, the budget includes a significant increase in new revenues, generated through the expansion of the sales tax. When considering these programmatic and revenue increases, RIPEC believes it is important to take the following into account:

- Do new revenues support new programs, or will the funding for new programs come at the expense of other services?
- Are the state's current and proposed programs in line with the state's priorities?
- If the new programs are supported through new revenues, is the projected revenue growth sufficient to sustain programmatic increases?
- Can the program goals be met without new revenues, can full implementation be delayed, or are there alternate sources of support that may be more effective?
- Are the new programs of greater priority than existing programs or do they merit an increased tax burden on individuals and businesses?

The FY 2012 deficit as shown in the Governor's budget, in part reflects a number of policy choices, such as diverting funds from general revenues into other funds to develop a dedicated source of transportation funding. Given the state's current fiscal situation, and the projected out-year deficits, RIPEC believes that any new program should only be started if there is an attached, dedicated revenue source that is sufficient to sustain the program. Any new program that does not have sufficient support will ultimately erode the state's ability to fund programs and will further contribute to the structural deficit.

While many of the proposed programs have merit, this may not be the most appropriate time to implement them, or to add new revenues. The state may want to consider whether delaying implementation of some of these initiatives may allow for more effective funding and, thus, programs. If the state decides to pursue these programs, their relative value and cost should be evaluated to ensure that any new program is clearly aligned with the state's priorities and goals.

Managing Out-Year Deficits

RIPEC believes the test of fiscal soundness of any budget is whether ongoing revenues are sufficient to support ongoing expenditures, and whether current obligations are appropriately funded and revenue realistically projected. The proposed FY 2012 budget, while balanced for the coming fiscal year, includes significant out-year deficits. These deficits are projected to increase from a $0.9 million surplus in FY 2012 to $411.5 million, or 12.0 percent of available revenues in FY 2016. This does not include the new pension funding requirements recently enacted by the State's Retirement Board which will add approximately $65 million in additional obligations to the FY 2013 budget for state employees and approximately $40 million more for the state's share of teacher retirement. Years of annual structural deficits and repeated out-year projected deficits have inhibited the State's ability to make strategic budget decisions that are needed to stimulate economic growth and support basic services. The state must carefully consider the consequences of enacting another budget that does not fundamentally resolve the state's underlying fiscal imbalance.

Table 1
Projected Deficits FY 2012 - 2016 ($ million)

	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
Available Revenues	$ 3,170.7	$ 3,243.4	$ 3,315.8	$ 3,391.1	$3,437.3
Total Expenditures	3,169.8	3,369.4	3,515.1	3,686.8	3,848.8
(Deficit)/Surplus*	$ 0.9	$ (126.0)	$ (199.3)	$ (295.7)	$ (411.5)
As a % of Available Revenue	0.0%	3.9%	6.0%	8.7%	12.0%

SOURCE: RIPEC calculations based on State Budget Office and House Fiscal Staff budget documents

* Note: the Governor's budget submission and forecast inadvertently misstated personnel growth rates, understating the projected deficit by an average of $35.9 million

Use of One-time Sources

The FY 2013 projected deficit seems to be largely driven by one-time items in the FY 2012 resolution, including deferring the statutorily required repayment to the Rainy Day Fund until FY 2013. Prior to revisions made to revenue estimates in the May REC, the FY 2011 budget would end with a projected deficit of approximately $6.0 million if this payment were to be made in FY 2011 (as in the enacted budget and required by law). Because the May REC has increased revenue projections that will result in a positive budget balance even if the payment is made, RIPEC believes repayment of this fund should be made a priority.

The other significant one-time expenditure shift is the use of the EduJobs funds, $32.3 million, to supplant general revenues for education. In addition to these two items, the budget includes temporary cost-shifting to federal funds for certain behavioral health costs, allowable under the federal health care reform. The increased reimbursement rate will expire in FY 2014 when health care reform is fully implemented.

RIPEC estimates that approximately 15 to 20 percent, roughly $75.0 million, of the FY 2012 budget is resolved through the use of one-time fixes. The state's continued reliance on non-recurring revenues and cost-shifting is a significant contributing factor to its persistent out-year deficits. Ultimately, the use of these sources does not require that the state make needed structural change by allowing for stop-gap measures. If the state is to move along the path of fiscal stability, it must continue to reduce reliance on these sources and make the necessary choices that will have a long-term and sustainable impact.

Responsible Fiscal Management

Based on the most recent estimates from the Revenue Estimating and Caseload Estimating conferences, the State will end FY 2011 with approximately a $65 million surplus (not including the $22 million repayment to the Rainy Day Fund), the first such surplus in a number of years. While these numbers are not yet final, and RIPEC urges the state to exercise caution when building these figures into its FY 2012 budget, the projected surplus indicates that the fiscal trends of the past three years are beginning to reverse. As revenues begin to increase, it is incumbent on the state to first ensure that the budget is structurally balanced before pursuing new programs.

RIPEC recommends that the state first use these funds to repay the Rainy Day Fund, rather than to delay expenditure modifications in FY 2012. Second, the state should consider taking action on issues that will have a long-term impact on the state's expenditures, for example, pre-paying long-term obligations. The state may also want to consider moving one-time expenditures proposed in the FY 2012 budget to the FY 2011 revised budget. These funds should not be used to fund the expansion of programs that will require ongoing support.

The state must be fiscally prudent during these uncertain times. The ongoing structural deficit hinders the state's ability to make necessary strategic decisions that will ensure long-term fiscal stability. The Governor's budget does take steps to address a number of these fundamental structural issues and does begin to take a long-term view of a number of aspects of the budget, such as a permanent and stable funding source for federal highway funding. However, a number of concerns remain with regard to some of the proposals, such as whether the sales tax expansion will negatively impact business and residents, and whether current and proposed programs are prioritized based on the state's policy agenda and their benefit to Rhode Islanders.

FY 2011 Revised and FY 2012 Proposed Budget Summary

FY 2011 Supplemental Budget

The Governor's FY 2011 supplemental budget increases total expenditures by $247.2 million or 3.1 percent more than the enacted FY 2011 budget. Changes from the FY 2011 enacted budget to the supplemental budget include the following:

- General revenue funds increase by $23.2 million (0.8 percent);
- Federal funds increase 3.7 percent, or $107.7 million;
- Restricted receipts decrease by $1.6 million, or 0.8 percent; and
- All other funds (including the gas tax) increase 6.4 percent ($117.9 million).

Table 2
FY 2011 Supplemental Budget

Source of Funds	FY 2011 Enacted	FY 2011 Supp.	Change
General Revenue	$2,942.1	$2,965.3	$23.2
Federal Funds	2,903.5	3,011.2	107.7
Restricted Receipts	180.1	178.5	-1.6
Other Funds	1,838.4	1,956.3	117.9
Total	$7,864.1	$8,111.3	$247.2

SOURCE: State budget documents; RIPEC calculations

Table 3
Changes to FY 2011 Enacted Budget

	FY 2011 Enacted	FY 2011 Revised	Change
Opening Surplus	$0.0	$17.9	$17.9
Reappropriated Surplus	-	3.4	3.4
Subtotal Opening Surplus	*$0.0*	*$21.3*	*$21.2*
Revenues	$3,020.6	$3,020.6	-
November REC Changes to Enacted	-	16.7	16.7
Governor's Changes	-	2.4	2.4
Subtotal Revenues	*$3,020.6*	*$3,039.7*	*$19.1*
Cash Stablization Fund	($78.5)	($79.5)	($1.0)
Total Available Revenues	**$2,942.1**	**$2,981.5**	**$39.4**
Enacted Expenditures	$2,942.1	$2,942.1	-
FMAP Rate Change	-	38.1	38.1
November CEC Changes to Enacted	-	(5.9)	(5.9)
Reappropriations	-	3.4	3.4
Governor's Changes	-	(12.3)	(12.3)
Total Expenditures	**$2,942.1**	**$2,965.3**	**$23.2**
Free Surplus	*$0.0*	*$16.2*	*$16.2*

SOURCE: State budget documents; RIPEC calculations

The FY 2010 closing statements reflect a $17.9 million closing surplus and a re-appropriated surplus of $3.4 million, increasing available FY 2011 revenues by $21.3 million. In addition, the November 2010 Revenue Estimating Conference (REC) increased revenues by an estimated $16.7 million (NOTE: revenues increases projected in the May REC are not included in these estimates). The Governor's budget includes an additional $2.4 million in other miscellaneous revenues. After the $1.0 million cash stabilization adjustment, total net revenues increase by $39.4 million relative to the enacted budget.

The Governor's budget includes a net expenditure increase of $23.2 million. Included in this total is a $38.1 million increase in expenditures related to the reduction in the enhanced FMAP rate, as well as a $5.9 million reduction in spending related to changes from the November 2010 Caseload Estimating Conference (CEC). This does not reflect the additional caseload changes from the May CEC. Additional changes include:

- A $12.6 million increase to aid with winter maintenance costs and to fix the structural deficit at the Department of Transportation;
- Savings of $22.0 million from the proposed delay of the required payback of the rainy day fund borrowing to RICAP until FY 2013;
- Local aid adjustments of $7.0 million including additional distressed communities aid and funding for the Central Falls deficit;
- Statewide personnel and operating savings of $3.7 million; and
- Adjustments to agency expenditures of $6.7 million.

FY 2012 Projected Deficit and Resolution

According to the State Budget Office, Rhode Island faces a projected revenue-expenditure gap of $331.1 million in FY 2012. The original estimate of $294.6 million was based on current services and changes to those estimates based on the Revenue and Caseload Estimating Conferences in November 2010. The additional $36.5 million in the Governor's deficit projections include statutory increases i.e., the increase in education aid and housing aid. However, the proposed budget also includes a number of items, such as increased funding for higher education and support for Central Falls, that reflect policy choices on the part of the Administration.

The proposed budget resolves the deficit through a combination of expenditure reductions or postponements, and increased revenues (primarily changes to the sales tax) resulting in an estimated FY 2012 closing balance of $0.9 million.

Table 4
FY 2012 Deficit

	$ millions
Original Projected Deficit (current services)	$ (318.6)
November REC/CEC Changes	25.0
Revised Deficit Post REC/CEC	**$ (294.6)**
Expenditures	
Education Aid Funding Formula	$ (7.5)
Education Housing Aid	(1.7)
Teacher Retirement	(3.7)
Higher Ed	(6.7)
Central Falls Deficit	(4.9)
Transportation- Structural Deficit	(12.0)
Total Additional Projected Expenditures	**$ (36.5)**
Revised Projected Deficit for FY 2012	**$ (331.1)**

SOURCE: State budget documents

The original projected FY 2012 deficit, based on current services levels, was estimated at $318.6 million. Changes to Budget Office projections resulting from the November 2010 REC and CEC lowered the projected deficit to $294.6 million; however, additional proposed expenditures, including fully funding the education funding formula, increasing support for higher education, addressing the projected FY 2012 Central Falls deficit, and shifting funding from general revenues to other funds to address the DOT structural deficit increased the projected FY 2012 deficit to $331.1 million.

Net additional revenues are estimated to increase by $162.3 million. The majority of this increase is related to the Governor's sales tax modernization proposal, which lowers the rate from the current 7.0 percent to 6.0 percent, expanding the current taxable base, and adding a 1.0 percent tax on certain currently exempt items. This proposal is projected to result in a net increase in general sales taxes of $164.9 million. In addition, the Governor has proposed a restructuring of the corporate income and minimum taxes, which reduces rates, eliminates credits and changes reporting requirements.

Table 5
FY 2012 Budget Deficit Resolution
as Recommended by Governor

	Amount $ millions	% of Total
Opening Surplus	**$16.2**	**4.9%**
Revenue Modifications		
Personal Income Tax	$2.2	0.7%
General Business Taxes	-0.9	-0.3%
Sales and Excise Taxes	155.7	46.9%
Other Revenue Changes	5.3	1.6%
Total Revenue Enhancements	**$162.3**	**48.9%**
Expenditure Modifications		
State Operations		
3.0% across-the-board personnel and operating savings	$19.3	5.8%
Other	3.7	1.1%
Subtotal	*$23.0*	6.9%
Local Aid & Education		
Supplant general revenues with EduJobs funds	$32.3	9.7%
Delay new funding for certain categorical education initiatives	5.2	1.6%
Subtotal	*$37.5*	11.3%
Health & Human Services Agencies		
DCYF System of Care Transformation	$4.9	1.5%
CPS practice changes	8.5	2.6%
Eliminate RIPAE program	1.4	0.4%
Increase federal match for behavorial health services	13.4	4.0%
Nursing home rate reform	6.1	1.8%
"Money Follows the Person" demonstration	2.5	0.8%
Other changes	33.7	10.2%
Subtotal	*$70.5*	21.2%
Debt service reduction	$22.3	6.7%
Other changes	37.0	11.1%
Total: Expenditure Modifications	**$153.5**	**46.2%**
Total	**$332.0**	**100.0%**
Closing Balance	***$0.9***	

SOURCE: State budget documents; RIPEC calculations

The FY 2012 budget as proposed makes a number of expenditure adjustments across a number of state agencies. As proposed, the most significant expenditure adjustments (approximately $60.5 million) are within the agencies under the Executive Office of Health and Human Services, including shifting certain state costs to federal funds and reducing vendor contract costs. Some of the proposed expenditure changes from agencies under the Executive Office of Health and Human Services include the following:

- Nursing home rate reform will change to a price-based methodology ($6.1 million);
- DCYF System of Care Transformation, which makes changes designed to reduce duration of residential placements ($4.9 million);
- Continues practice changes in DCYF that have resulted in declines in caseloads, as well as proposes a number of additional investigative changes ($8.5 million);
- Eliminating the Rhode Island Pharmaceutical Assistance for the Elderly (RIPAE) program and supplanting the program with a smaller-scale program ($1.4 million); and
- Implementing the Affordable Care Act's "Health Homes" provision to switch to 90/10 federal funding for mental health services ($13.4 million in Behavioral Health, Developmental Disabilities and Hospitals, plus an additional $1.3 million in the Department of Human Services).

In addition to the above, the Governor's budget supplants general revenue funds with the federal EduJobs funds ($32.3 million), reduces debt service payments by $22.3 million primarily through a delay in issuance of Historic Structures Tax Credit financing, and delays the Rainy Day Fund repayment ($22.0 million). It should be noted that delaying the repayment of the Rainy Day Fund until FY 2013 results in the $16.2 million proposed opening surplus for FY 2012. If the fund was repaid in FY 2011 (as in the enacted budget and required by law), the state would have a $6.0 million opening deficit for FY 2012. The proposed budget also delays new funding for high-cost special education and career and technical education, level funds early childhood education aid, and level funds FY 2012 municipal aid.

Revenues Summary

General Revenues

General revenues reflect those revenues that may be used for any purpose, as opposed to other sources of funding, which may be used only for specific purposes. These funds represent approximately 40 percent of all funds. The majority of general revenues – 78.2 percent in FY 2012 – are derived from taxes including the personal income tax, general business taxes and sales taxes. The remaining 21.8 percent of the FY 2012 general revenue program is comprised of departmental receipts including the hospital licensing fee, lottery receipts, and other miscellaneous funds.

FY 2011 Revised Revenues

The Governor's FY 2011 revised budget includes a net increase in revenues of 0.6 percent ($19.1 million) when compared to the FY 2011 enacted budget. The majority of these changes reflect revisions made during the November 2010 Revenue Estimating Conference (REC), which forecast a moderate decrease in personal income taxes, minor changes to general business tax collections, and an $18.5 million increase in sales and use taxes. The increase in general sales taxes was partially offset by an anticipated $10.5 million decrease in departmental receipts. Only departmental receipts and other miscellaneous revenues were modified from the November REC.

Table 6
FY 2011R and FY 2012 Governor's Proposed General Revenue Program

General Revenues	FY 2010 Audited	FY 2011 Enacted	FY 2011 Revised	Change	FY 2012 Nov REC	FY 2012 Proposed	Change
Taxes							
Personal Income Tax	$898.1	$937.9	$936.5	-0.1%	$947.8	$950.0	0.2%
General Business Taxes	383.0	361.3	361.2	0.0%	375.0	374.1	-0.2%
General Sales & Use Tax	803.4	787.0	805.5	2.4%	824.0	989.5	20.1%
Other Sales Taxes*	60.5	61.2	64.9	6.0%	65.2	55.4	-15.0%
Cigarette Tax	138.3	134.0	135.0	0.7%	131.8	131.8	0.0%
Other Taxes	37.5	35.8	36.0	0.4%	36.5	36.5	0.0%
Subtotal - Taxes	*$2,320.9*	*$2,317.2*	*$2,339.0*	*0.9%*	*$2,380.3*	*$2,537.3*	*6.6%*
Department Receipts	$333.1	$345.2	$334.8	-3.0%	$197.3	$344.6	74.6%
Other Sources	363.0	358.3	365.9	2.1%	360.5	364.0	1.0%
Total Revenues	**$3,017.0**	**$3,020.6**	**$3,039.7**	***0.6%***	**$2,938.0**	**$3,245.8**	***10.5%***

* Motor vehicle, motor fuel and alcohol sales taxes

Source: State Budget Office documents, RIPEC calculations

FY 2012 Revised Revenues

General revenues in the Governor's FY 2012 proposed budget increase by 10.5 percent ($307.8 million) when compared to the November REC. Slightly less than half of this amount ($141.8 million) is related to the hospital licensing fee, which must be reauthorized every year. The majority of the remainder ($157.0 million) is related to a number of tax changes as summarized in the following section.

Table 7
May 2011 Revenue Estimating Conference - Change in General Revenues ($ million)

Revenue	FY 2011 Enacted	FY 2011 Nov-10 REC	FY 2011 May-11 REC	FY 2011 Nov-May Change	FY 2012 Nov-10 REC	FY 2012 May-11 REC	FY 2012 Nov-May Change
Taxes							
Personal Income	$937.9	$ 936.5	$ 1,003.6	$ 67.1	$ 947.8	$ 1,007.0	$ 59.2
General Business							
Business Corporation	$119.0	$ 123.3	$ 95.1	$ (28.2)	$ 131.0	$ 120.3	$ (10.7)
Public Utilities Gross Earnings	98.0	97.0	104.2	7.2	99.0	99.4	0.4
Insurance Companies	101.3	98.2	68.0	(30.2)	100.7	102.6	1.9
Health Care Provider Tax	39.8	40.5	40.5	0.0	41.8	41.4	(0.4)
All Other Business Taxes	3.2	2.2	3.0	0.9	2.5	2.5	0.0
Subtotal	*$361.3*	*$ 361.2*	310.8	$ (50.4)	$ 375.0	$ 366.2	$ (8.8)
Sales and Use Taxes							
General Sales and Use	$787.0	$ 805.5	$ 810.4	$ 4.9	$ 824.0	$ 828.7	$ 4.7
Motor Vehicle	48.5	51.8	51.5	(0.3)	51.9	51.6	(0.3)
Gasoline	1.0	1.1	1.1	-	1.1	1.1	-
Cigarettes	134.0	135.0	136.9	1.9	131.8	133.5	1.7
Alcohol	11.7	12.0	11.9	(0.1)	12.2	12.1	(0.1)
Subtotal	$ 982.2	*$ 1,005.4*	*$ 1,011.8*	$ 6.4	*$ 1,021.0*	$ 1,027.0	$ 6.0
Other Taxes	$35.8	$ 36.0	$ 57.4	$ 21.5	$ 36.5	$ 37.0	$ 0.5
Total Taxes	**$ 2,317.2**	**$ 2,339.0**	**$ 2,383.6**	**$ 44.6**	**$ 2,380.3**	**$ 2,437.2**	**$ 56.9**
Departmental Revenue*	345.2	$ 334.7	$ 334.1	$ (0.6)	$ 197.3	$ 195.4	$ (1.9)
Total Taxes & Departmentals	**$ 2,662.4**	**$ 2,673.7**	**$ 2,717.7**	**$ 44.0**	**$ 2,577.6**	**$ 2,632.6**	**$ 55.0**
Other Sources							
Gas Tax Transfers	$0.0	$ -	$ -		$ -	$ -	0.0
Other Miscellaneous	5.3	10.9	13.1	2.3	3.8	3.8	0.0
Lottery	346.9	347.5	353.2	5.7	351.5	361.3	9.8
Unclaimed Property	6.0	5.3	7.1	1.8	5.2	6.2	1.0
Subtotal	$ 358.3	*$ 363.7*	*$ 373.4*	*$ 9.8*	$ 360.5	$ 371.3	*$ 10.8*
Total General Revenues	**$ 3,020.6**	**$ 3,037.4**	**$ 3,091.1**	**$ 53.8**	**$ 2,938.0**	**$ 3,003.9**	**$ 65.9**

* FY 2012 estimated Departmental Revenue does not include the Hospital Licensing Fee which must be reauthorized every year. The Governor budgeted an amount of $141.8 million.

Source: November 2010 and May 2011 Revenue Estimating Conference; State budget documents; RIPEC calculations

The May 2011 REC revised the November estimates, increasing total FY 2011 projected revenues by $53.8 million when compared to November, and by $70.5 million when compared to the enacted budget. The largest share of this increase is the projected increase in personal income taxes. Total businesses taxes are projected to decline by $50.4 million, while sales and use taxes are projected to increase slightly ($6.4 million).

The May REC also increased their FY 2012 projections when compared to the November estimates (NOTE: estimators are required to base their estimates on current law; these figures do not include the changes proposed by the Governor). As with the FY 2011 estimates, the largest share of the projected $65.9 million increase was due to growth in the personal income tax. General business taxes were projected to decrease by $8.8 million, while sales and use taxes were projected to increase by $6.0 million.

Proposed Tax Changes

Total proposed tax changes in the FY 2012 budget are projected to increase net tax revenues by $157.0 million. Of this amount, $155.7 million is from changes to the sales tax, including a net $11.0 million shift of revenues to restricted receipts for transportation. The balance is from a projected $2.2 million increase in personal income tax collections, predominantly from the repeal of the motion picture tax credit, and an estimated $0.9 million net decrease in general business tax collections.

Table 8

FY 2012 Proposed Tax Changes

Personal Income Tax	
Repeal of Motion Picture Credit	$1,282,580
Other Changes	921,422
Subtotal: Personal Income Tax	*$2,204,002*
General Business Taxes	
Phase-out of Jobs Development Credit	$4,845,502
Implement Combined Reporting	8,891,640
Phase-in of Rate Reduction	(8,525,365)
Restructure Corporate Minimum Tax	(6,117,310)
Repeal of Motion Picture Credit	139,655
Other Changes	(92,731)
Subtotal: General Business Taxes	*($858,609)*
Sales and Excise Taxes	
Rate Reduction	($117,714,286)
Base Expansion	197,594,235
1% Tax on Formerly Exempt Items	86,840,462
Other Changes	(11,037,612)
Subtotal: Sales and Excise Taxes	*$155,682,799*
Total: All Taxes	**$157,028,192**

Source: State Budget Office documents, RIPEC calculations

General Business Tax Changes

The Governor's proposed FY 2012 budget includes four major initiatives that are projected to decrease net business tax revenue by $0.9 million in FY 2012, but will result in a net decrease in revenue of $14.6 million by FY 2016. These four initiatives include:

- Phasing-in a reduction in the business corporation tax rate from 9.0 percent to 7.5 percent over three years. The proposed FY 2012 tax rate would be 8.5 percent and the rate would reduce by an additional 0.5 percent each year. The budget assumes a loss of revenue of $8.5 million in FY 2012, increasing to a revenue loss of $36.5 million in FY 2016.
- Eliminating the Jobs Development Act rate reduction over a three-year period for an increase in revenues of $4.8 million in FY 2012 and in each subsequent fiscal year until the Act is phased-out. Currently, the Act allows for a 0.25 percent rate reduction for each 50 new jobs created by eligible companies for three years prior to the base year. The reduction cannot exceed 6.0 percent.
- Implementing combined reporting, resulting in a revenue increase of $8.9 million in FY 2012 ($11.8 million in FY 2016). Combined reporting requires multistate corporations to file as a unity business, disallowing shifting of income to lower-tax states. Currently, Rhode Island does not require combined reporting. Within New England, Maine, Massachusetts, New Hampshire and Vermont require combined reporting.
- Restructuring the corporate minimum tax to include limited partnerships and limited liability partnerships to the tax. The current tax and the minimum franchise tax would be replaced with a tiered system that taxes Rhode Island businesses on their gross receipts. Entities incorporated as C-corporations with gross receipts of less than $999,999 would pay a minimum tax of $500, while S-corporations, LLCs, LPs, and LLPs would pay a minimum tax of $250. All entities with gross receipts of over $5.0 million would pay a minimum tax of $2,000. The budget assumes a reduction in revenue of $6.1 million in FY 2012.

Sales Taxes

A number of proposed changes to the state's sales tax system are included in the proposed FY 2012 budget. The proposed changes are projected to result in a net increase of $155.7 million in FY 2012. Of this amount, there is a net increase in revenues of $164.9 million that result from a series of proposed "sales tax modernization" initiatives that include:

- Reducing the state's general sales and use tax rate from 7.0 percent to 6.0 percent for an estimated revenue loss of $117.7 million. Currently, Rhode Island's rate is the highest in New England. Massachusetts currently has a rate of 6.25 percent and Connecticut has a rate of 6.0 percent (proposed to increase to 6.35 percent).
- Expanding the current sales tax base to include items previously not taxed (see table 9). The base expansion is projected to result in a revenue increase of $197.6 million.
- Applying a 1.0 percent tax rate to certain items that are currently exempt, projected to generate an additional net $85.0 million ($86.8 million in additional revenue net of the $1.8 million loss in revenue from noncompliance with the Streamlined Sales and Use Tax Agreement). Items subject to the tax include, but are not limited to, purchases used for manufacturing purposes ($38.9 million), sales to charitable, educational or religious organizations ($10.6 million), clothing and footwear ($6.7 million), manufacturer's machinery and equipment ($2.8 million), agricultural products for human consumption ($2.6 million), and home heating fuel ($2.2 million).

Table 9
Proposed Sales Tax Modernization Program

Rate Reduction	**Est. Loss**
Rate from 7% to 6%	-$117.7
Currently Exempt Items at 6%	**Est. Rev.**
Goods	
Pre-written computer software delivered electronically	$7.6
Non-prescription drugs including medical marijuana	9.3
Other goods	5.1
Subtotal: Goods	$22.0
Services	
Building services including landscaping and pest control	$23.3
Employment agencies	19.1
Personal care services including hairdressers and diet centers	18.6
Business support services	8.5
Other services	53.0
Subtotal: Services	$122.6
Recreation and Entertainment	
Amusement parks, campgrounds and related services	$10.0
Membership clubs	4.4
Other recreation and entertainment	6.4
Subtotal: Recreation and Entertainment	$20.8
Maintenance and Repair Labor	
Motor vehicles including car washes	$18.2
Commercial and industrial exempting manufacturers	2.4
Clothing and footware repair, rental and alteration	2.3
Other maintenance and repair	4.2
Subtotal: Maintenance and Repair	$27.1
All Other	$5.1
Total: Currently Exempt Items at 6%	**$197.6**
Currently Exempt Items at 1%	
Manufacturing inputs, clothing, sales to charitable orgs., etc.	$86.8
Streamlined Sales and Use Tax Agreement noncompliance	-1.8
Total: Currently Exempt Items at 1%	**$85.0**
Total: Elimination of Exemptions	**$282.6**
Net Revenue Change - Sales Tax Modernization	**$164.9**

SOURCE: State Budget Office documents, Senate Fiscal Office documents, RIPEC calculations

Additional Revenue Changes

In addition to the above, the Governor's budget proposes changes to unemployment insurance tax receipts and the creation of two new restricted receipt accounts relating to the proposed sales tax changes, the Tourism Asset Protection (TAP) Fund and the Municipal Accountability, Stability and Transparency (MAST) Fund.

Unemployment Insurance
In October of 2009, the state's Employment Security Advisory Council convened to address the issue of trust fund solvency. The Council developed a series of recommendations that were forwarded to the Governor in the spring of 2010, without the Council's full endorsement, and were not, ultimately, included in the FY 2011 budget.

These recommendations, with some revisions, are included in Article 4 of the Governor's FY 2012 budget as proposed. The recommendations include seven adjustments to claimant benefits, which are discussed in the expenditures section of this report. In addition to the expenditure adjustments, the Council proposed two changes to the state's unemployment insurance tax structure as follows:

- Eliminating the current taxable wage base and replacing it with a flexible wage base. In 2012, the taxable wage base would be set to $19,000 (the current base), or 47 percent of the statewide average annual wage rounded to the next highest multiple of $200. The percentage would increase each year through 2015 when the wage base would be set at 50 percent of the average annual wage. The Department estimates that this would generate an additional $4.0 million in UI contributions in 2012.
- Raising the taxable wage base for employers subject to the highest tax rated group (employers with a current tax rate of 10.0 percent) to $3,000 above the taxable wage base for employers in the eight other groups. The Department estimates that this proposal would generate an additional $3.1 million per year in UI tax revenues.

In addition, the budget as proposed includes an additional $10.0 million in unemployment insurance tax receipts relating to the 0.3 percent increase to the Jobs Development Fund assessment, which will be used to make the required interest payment to the federal government for federal unemployment insurance loans.

MAST and TAP Fund Restricted Receipts
In addition to the sales tax changes as outlined above, the Governor proposes maintaining the meals and beverage tax, levied on prepared food intended for immediate consumption, at 8.0 percent. Communities would continue to receive the 1.0 percent local share ($19.3 million), while the state share would be 6.0 percent, consistent with the lower sales tax rate. The balance would be dedicated to the MAST Fund, which is described in the "Local Aid" section of this report.

The Governor also proposes maintaining the 8.0 percent Hotel Tax at its current rate and dedicating the additional 1.0 percent of revenue ($2.6 million) to the TAP restricted receipt account. Funds from this account would be dedicated to capital projects for state-owned tourism assets. In FY 2012, the Governor proposes using these funds for capital improvements at Fort Adams State Park.

Expenditure Summary

Overview

As proposed, the Governor's FY 2012 budget includes all funds expenditures of $7,661.3 million, a 2.58 percent ($202.9 million) decrease from the FY 2011 enacted budget. The budget includes expenditure reductions in grants and benefits ($331.5 million), capital ($23.0 million) and operating transfers ($7.8 million). Personnel, operating expenditures, local aid and debt service are projected to increase by a total of $159.5 million; of this increase, the largest share is related to personnel expenditures. Although the largest reduction in spending is from grants and benefits, this category remains the largest expenditure category and is more than double the level of personnel expenditures, the next highest category of spending.

Table 10
Rhode Island State Spending - All Funds ($ millions)

By Category	2002	2011E	2011R	2012P	2011E-12P Change
Personnel	$ 1,241.3	$ 1,670.4	$ 1,705.1	$ 1,743.7	$ 73.3
Operating	348.4	624.6	662.2	660.7	36.1
Local Aid	945.3	1,054.0	1,105.6	1,097.2	43.2
Grants & Benefits	2,324.9	3,864.3	3,961.3	3,532.8	(331.5)
Capital	150.1	267.0	305.3	244.0	(23.0)
Debt Service	179.7	233.8	232.9	240.7	6.9
Operating Transfer*	-	150.1	139.0	142.3	(7.8)
Total	*$ 5,189.9*	*$ 7,864.2*	*$ 8,111.4*	*$ 7,661.3*	*$ (202.9)*

By Fund	2002	2011E	2011R	2012P	Change
General Revenue	$ 2,651.7	$ 2,942.1	$ 2,965.3	$ 3,169.8	$ 227.7
Federal Funds	1,465.4	2,903.5	3,011.2	2,557.2	(346.3)
Restricted Funds	92.7	180.1	178.5	209.5	29.4
Other Funds	980.0	1,838.5	1,956.3	1,724.8	(113.7)
Total	*$ 5,189.9*	*$ 7,864.2*	*$ 8,111.4*	*$ 7,661.3*	*$ (202.9)*

E = Enacted, R = Revised, P = Proposed
* Operating transfer is a change in accounting that was not in place in FY 2002
Source: RIPEC calculations based on State Budget Office Data

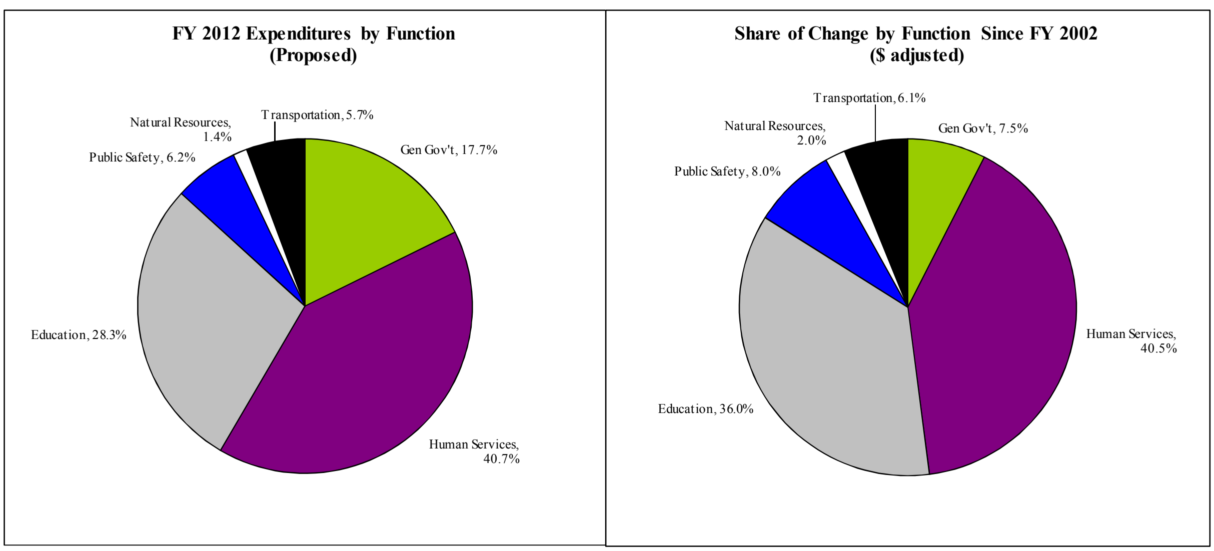
General revenue expenditures of $3,169.8 million account for the majority of expenditures, supporting 41.4 percent of total spending. Expenditures from federal funds (primarily Medicaid funds) of $2,557.2 million are 33.4 percent of total proposed spending and represent the second largest source of support. The majority of the $346.3 million decrease in federal funds is related to the expiration of funds from the American Recovery and Reinvestment Act (ARRA). Expenditures from other funds (primarily university and college funds, and employment and training funds) total 22.5 percent of all spending and are the third largest source of funding in the FY 2012 budget. The Governor proposes a $113.7 million decrease in other funds, which is partially related to the projected decrease in unemployment insurance-related expenditures. The smallest category of expenditures is from restricted receipts, representing just 2.7 percent of the total State budget.

All Funds Expenditures

Rhode Island allocates expenditures by both function and category. Function indicates spending by agencies with like programs and purposes and includes general government, human services, education, public safety, natural resources, and transportation. Chart 2 shows FY 2012 expenditures by function and the adjusted share of growth by function since FY 2002.

- Human services expenditures, which include spending on entitlement programs (e.g., supplemental security income, cash assistance and medical assistance), elderly services, state hospitals, etc., represent the largest share of total FY 2012 expenditures ($3,119.7 million, 40.7 percent).
- Expenditures for human services programs also represent the largest share of adjusted growth since FY 2002 ($576.7 million). These programs have accounted for $0.41 of every new dollar spent since FY 2002.
- Similarly, the $2,170.1 million in proposed education expenditures (i.e., elementary and secondary education, higher education, arts, historical preservation and heritage, and public television) account for the second largest share of expenditure by function in FY 2012 (28.3 percent).
- Since FY 2002, education spending has increased by $513.0 million ($0.36 of every new dollar), the second-largest share of the increase in expenditures over the past ten years.
- Combined public safety, natural resources and transportation represent approximately 13 percent of the FY 2012 budget and 16 percent of adjusted growth over the past ten years.
- Proposed general government expenditures, spending for programs that support all other functions including general government type activities, account for 17.7 percent of FY 2012 expenditures.
- Adjusted general government expenditures have increased by 7.5 percent ($106.9 million) since FY 2002.

Chart 2
Expenditures by Function and Adjusted Share of Change Since FY 2002

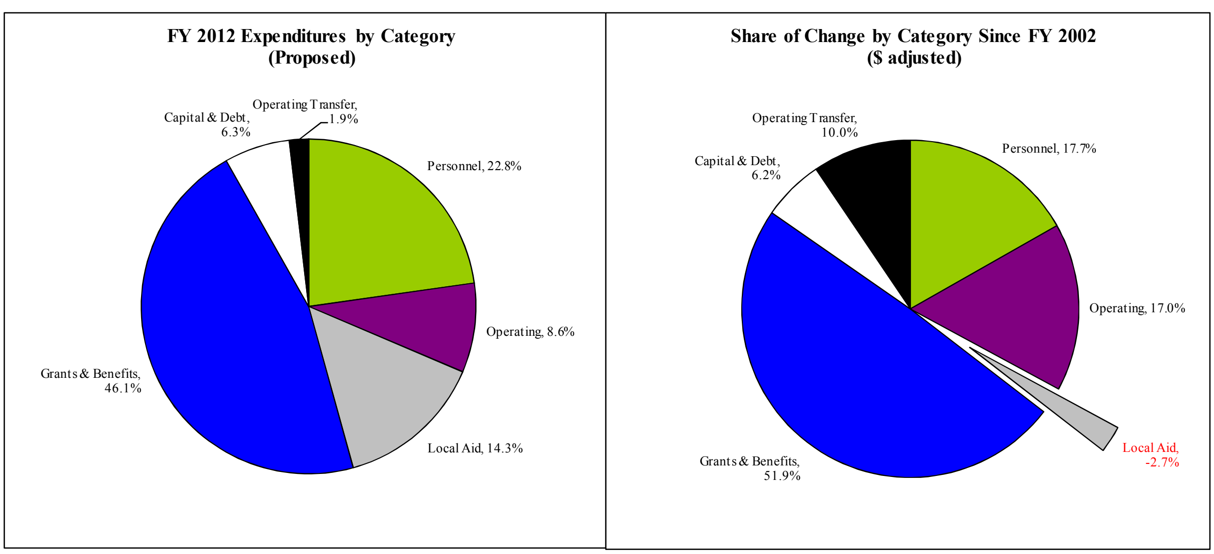


SOURCE: State Budget Office documents; RIPEC calculations

Expenditures are also allocated by accounting categories that reflect what is purchased, i.e., personnel, operations, local aid, grants and benefits, capital, debt service and operating transfers. As shown on Chart 3:

- Grants and benefits spending of $3,532.8 million, for programs that provide direct support to individuals such as Medicaid, child care, and unemployment benefits, represent the largest all funds expenditure category, accounting for 46.1 percent of total proposed expenditures in FY 2012.
- Spending on grants and benefits also accounts for the largest share of the spending increase over the past ten years; of every new dollar spent since FY 2002, $0.52 has gone to support the increase in grants and benefits.
- Combined personnel and operating expenditures, represent the second-largest category of spending in FY 2012, accounting for 31.4 percent of proposed FY 2012 expenditures.
- Since FY 2002, adjusted personnel expenditures have increased by $252.2 million, while adjusted operating expenditures have increased by $242.1 million. Together, these two categories of spending account for $0.35 of every new dollar spent since FY 2002.
- The third largest category of expenditures is local aid, which includes education aid and other direct assistance to municipalities. In the FY 2012 proposed budget, proposed local aid expenditures of $1,097.2 million constitutes 14.3 percent of all expenditures.
- Local aid was the only category of expenditures to see a decrease (on an adjusted basis) between FY 2002 and the FY 2012 proposed budget. Over the ten-year period, adjusted local aid spending has decreased by 2.7 percent.
- Proposed capital and debt service expenditures account for 3.2 percent of the total FY 2012 budget. Since FY 2002, capital and debt expenditures have accounted for $0.06 of every new dollar in state expenditures.
- The $142.3 million operating transfer category reflects transfers between state and quasi-government agencies. The addition of this category impacts the distribution of funds across categories when comparing FY 2002 and proposed FY 2012 expenditures.

Chart 3
Expenditures by Category and Adjusted Share of Change Since FY 2002



SOURCE: State Budget Office documents; RIPEC calculations

General Revenue Expenditures

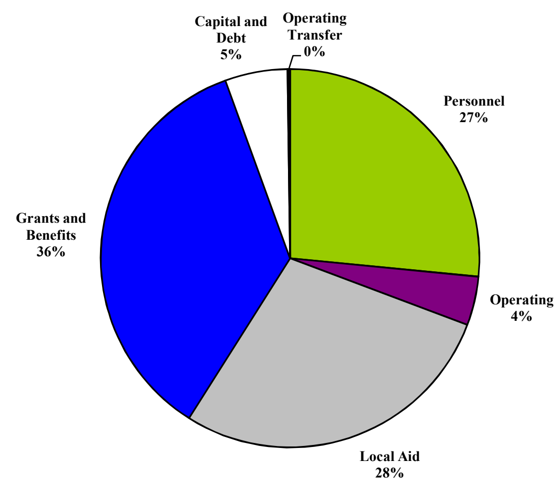
General revenue expenditures – effectively unrestricted spending that is primarily from own-source revenue – account for the largest share of total spending by fund (41.4 percent of all funds spending). Proposed FY 2012 general revenue expenditures of $3,169.8 million are 7.7 percent higher than FY 2011 enacted general revenue expenditures. The majority of this increase ($178.8 million, 78.5 percent) is related to growth in grants and benefits, which can partially be attributed to the expiration of ARRA funds in FY 2012.

Table 11
FY 2011 and FY 2012 General Revenue Expenditures

Expenditure Category	FY 2011 Enacted	% of Total	FY 2012 Proposed	% of Total
General Operations				
Personnel	$794.9	27.0%	$841.8	26.6%
Operations	131.6	4.5%	132.0	4.2%
Subtotal Operations	*$926.5*	*31.5%*	*$973.7*	*30.7%*
Subtotal Grants & Benefits	*$946.4*	*32.2%*	*$1,125.2*	*35.5%*
Subtotal Local Aid	*$875.8*	*29.8%*	*$895.3*	*28.2%*
Capital Expenditures				
Capital	$6.0	0.2%	$6.8	0.2%
Debt Service	158.2	5.4%	162.3	5.1%
Subtotal Capital	*$164.2*	*5.6%*	*$169.1*	*5.3%*
Operating Transfer	*$29.3*	*1.0%*	*$6.6*	*0.2%*
Total	**$2,942.1**	**100.0%**	**$3,169.8**	**100.0%**

Source: State Budget Documents and RIPEC Calculations

Chart 4
FY 2012 Expenditures by Category as a % of Total General Revenue Expenditures



- Grants and benefits spending of $1,125.2 million accounts for 35.5 percent of total FY 2012 proposed general revenue expenditures. Proposed FY 2012 expenditures in this category are 18.9 percent ($178.8 million) higher than FY 2011 enacted spending.
- Spending on personnel and operating expenditures of $973.7 million accounts for 20.7 percent ($47.2 million) of the increase between the FY 2012 proposed and FY 2011 enacted budgets and 30.7 percent of the FY 2012 proposed general revenue budget.
- Proposed local aid expenditures increase from $875.8 million in FY 2011 to $895.3 million in FY 2012, an increase of $19.5 million (2.2 percent). Local aid accounts for 28.2 percent of the total FY 2012 general revenue budget.
- Total proposed general revenue expenditures for capital and debt service increase 3.0 percent, from $164.2 million (5.6 percent) of FY 2011 enacted spending to $169.1 million (5.3 percent) of FY 2012 proposed spending.
- The FY 2012 proposed budget includes a reduction in general revenue-supported operating transfer expenditures of $22.7 million (77.4 percent).

Budget Drivers

Overview

Table 11 outlines total adjusted expenditures between FY 2002 and FY 2012 by expenditure category and select subcategories. As shown on the table, although spending has increased on an adjusted basis, not all categories or subcategories of expenditures have increased over the past decade. For example, adjusted expenditures in seven of the 11 subcategories shown under grants and benefits decreased over the past decade by $189.6 million. This decrease, however, was offset by increases in medical assistance, higher education and other grants and benefits, which increased by a total of $929.1 million. The following provides a summary of expenditure highlights by category and notes areas of budget growth over the past decade. Detailed, select expenditure changes are included in the following sections.

Personnel/Operations

- Proposed expenditures for FY 2012 general operations (personnel and other state operations) of $2,404.4 million are 25.9 percent ($494.3 million) higher than adjusted FY 2002 expenditures. Together, these two categories account for 34.7 percent of the total adjusted growth between FY 2002 and FY 2012.
- Although salaries and benefits account for the largest share of unadjusted growth in personnel costs during the past decade, retirement expenditures account for the largest share of personnel expenditures on an adjusted basis.
- Since FY 2002, retirement costs have increased at a faster rate than any other personnel expenditure and have more than tripled on an unadjusted basis (from $50.9 million to $171.5 million).
- The Governor's proposed FY 2012 budget increases the employee share of the annual required contribution to 11.75 percent of payroll for all employees (state workers, teachers, state police and judges).
- The budget includes a proposal to fully fund obligations relating to other post-employment benefits (OPEB) on an actuarial basis with a 30-year amortization period. In addition, $7.7 million in savings from all funds ($3.9 million in general revenues) are included from the state's participation in the Early Retiree Reinsurance program established through the Affordable Care Act.

Grants and Benefits

- The decline in income supports from $450.6 million to $395.4 million is largely related to changes in unemployment benefits. After increasing significantly over the past three years, unemployment benefits are projected to fall significantly in the FY 2012 budget.
- The proposed budget makes a number of changes to both the financing and the benefit structure of the state's unemployment insurance program.
- As noted above, the $739.5 million increase in adjusted grants and benefits expenditures between FY 2002 and FY 2012 is related primarily to increases in medical assistance ($547.8 million total, 63.0 percent of which is growth in managed care expenditures).

- Growth in Medicaid managed care accounted for almost one-quarter of the growth between FY 2002 and FY 2012. When all other medical assistance is included, these medical assistance accounted for 38.4 percent of the increase in expenditures over the past decade.
- The proposed FY 2012 budget makes a number of changes to medical assistance (Medicaid) programs including provider rate reform, shifting allowable costs to federal accounts, and the elimination or restructuring of programs.
- Adjusted spending on cash supports related to Rhode Island Works (formerly the Family Independence Program), the state's program under Temporary Aid to Needy Families (TANF) has decreased by $70.2 million (66.0 percent) over the past decade.
- Similarly, child care assistance expenditures have decreased by $29.7 million (35.8 percent) during the same time frame.
- Additional changes to programs under grants and benefits include continuing implementation of the "System of Care" transformation under DCYF, elimination of the state pharmaceutical assistance to the elderly program (RIPAE), and changes to assessment and rate reform regarding services to developmentally disabled adults.
- Adjusted grants and benefits for higher education have more than doubled over the past ten years, from $115.0 million to $271.6 million, accounting for 11.0 percent of the total budget increase during this time.

Local Aid

- Local aid was the only broad category in which expenditures declined, on an adjusted basis, over the past decade.
- Two categories, the motor vehicle excise tax phase-out reimbursement and general revenue sharing, decreased by a total of $161.9 million since FY 2002.
- This decrease was partially offset by increases of education aid ($58.3 million), federal aid ($53.6 million), PILOT ($5.8 million) and other aid ($5.5 million).
- The elimination of the reimbursement for the phase-out of the motor vehicle excise tax was the largest decrease in any expenditure category over the ten-year period, representing a 7.7 percent decrease in total spending during the time period.
- Although education aid increased through the early part of the decade, state support for education has fluctuated over the past four fiscal years and FY 2012 support is lower than FY 2007 aid.
- The Governor proposes fully funding the education funding formula while supplanting some general revenue expenditures with federal EduJobs grant funding in FY 2012.
- Increases in proposed FY 2012 "other aid" largely reflect the proposed Municipal Accountability and Transparency (MAST) fund ($19.3 million) and the Central Falls stabilization payment ($4.9 million).

Capital, Debt and Operating Transfer

- The remaining categories, capital expenditures, debt service and the operating transfer account for 8.2 percent of total FY 2012 proposed expenditures.

- Spending on capital and debt accounted for 6.2 percent of the total adjusted expenditure increase over the past decade.
- Proposed FY 2012 expenditures of $484.7 million represent 6.3 percent of the total budget, compared to FY 2002 spending of $396.3 million (6.4 percent of the budget).
- The FY 2012 budget includes a $22.3 million debt service reduction that is the result of lower than anticipated costs associated with historic tax credits.
- The capital budget also includes $48.3 million for technology upgrades.
- In order to reduce the state's reliance on debt financing for transportation, the Governor's budget proposes shifting fees collected by the Department of Motor Vehicles to the Department of Transportation and providing additional funding for the Intermodal Surface Transportation Fund. The expectation is that this would:
    - Eliminate use of general obligation bonds to provide state match for federal funds by FY 2016;
    - Reduce debt service expenditures, which is currently reducing funds available for transportation projects; and
    - Allow for gas tax revenues to be used on highway and surface transportation needs.
- The funds would be shifted over a five-year period at 20.0 percent per year. It is expected that this would provide approximately $64.0 million to the Department of Transportation by FY 2016.
- In addition, the Governor proposes seeking legislative approval for a study of the possibility of tolling on certain roads in the state to provide additional revenues.
- The Governor also proposes the creation of the Tourism Asset Protection (TAP) fund using 1.0 percent of the proceeds from the hotel tax (estimated $2.6 million in FY 2012) to be used for capital improvements at state-owned tourism related areas.
- In FY 2012, the Governor proposes using proceeds from this fund to support capital projects at Fort Adams State Park.
- The operating transfer category, which was not included in the FY 2002 budget, accounts for 1.9 percent of the FY 2012 proposed budget ($142.3 million).

Table 12
Rhode Island State Budget Drivers - All Funds (inflation-adjusted, $ millions)

Expenditure Category	FY 2002 Actual	% of Total	FY 2012 Proposed Base	% of Total	Actual Increase	Percent Change	Share of Increase
General Operations							
Personnel	$ 1,491.5	23.9%	$ 1,743.7	22.8%	$ 252.2	16.9%	17.7%
Operations	418.6	6.7%	660.7	8.6%	242.1	57.8%	17.0%
Subtotal - Operations	$ 1,910.0	30.6%	$ 2,404.4	31.4%	$ 494.3	25.9%	34.7%
Grants & Benefits							
Income Support (TDI & Employ)	$ 450.6	7.2%	$ 395.4	5.2%	$ (55.2)	-12.2%	-3.9%
Medical Assistance - Mgd Care*	309.2	5.0%	654.3	8.5%	345.1	111.6%	24.2%
Medical Assistance - All Other*	805.6	12.9%	1,008.3	13.2%	202.7	25.2%	14.2%
Development Disabilities	183.9	2.9%	183.8	2.4%	(0.1)	-0.1%	0.0%
Child Welfare	122.1	2.0%	102.3	1.3%	(19.8)	-16.2%	-1.4%
TANF	106.3	1.7%	36.1	0.5%	(70.2)	-66.0%	-4.9%
Child Care	83.0	1.3%	53.2	0.7%	(29.7)	-35.8%	-2.1%
SSI	33.6	0.5%	18.9	0.2%	(14.7)	-43.7%	-1.0%
Higher Education	115.0	1.8%	271.6	3.5%	156.6	136.3%	11.0%
Other Grants & Benefits	584.2	9.4%	808.8	10.6%	224.7	38.5%	15.8%
Subtotal - Grants & Benefits	$ 2,793.4	44.8%	$ 3,532.8	46.1%	$ 739.5	37.7%	51.9%
				0			
Local Aid							
Education Aid	$ 776.4	12.5%	$ 834.7	10.9%	$ 58.3	7.5%	4.1%
Motor Vehicle Phase-out	119.5	1.9%	10.0	0.1%	(109.5)	-91.6%	-7.7%
General Revenue Sharing	52.4	0.8%	-	0.0%	(52.4)	-100.0%	-3.7%
PILOT	21.8	0.3%	27.6	0.4%	5.8	26.6%	0.4%
Federal Aid	123.9	2.0%	177.5	2.3%	53.6	43.3%	3.8%
Other**	41.8	0.7%	47.3	0.6%	5.5	13.2%	0.4%
Subtotal - Local Aid	$ 1,135.8	18.2%	$ 1,097.2	14.3%	$ (38.6)	-3.4%	-2.7%
Capital Expenditures							
Capital Expenditures	$ 180.4	2.9%	$ 244.0	3.2%	$ 63.6	35.2%	4.5%
Debt Service	215.9	3.5%	240.7	3.1%	24.8	11.5%	1.7%
Subtotal - Capital	$ 396.3	6.4%	$ 484.7	6.3%	$ 88.4	22.3%	6.2%
Operating Transfer***	$ -	0.0%	$ 142.3	1.9%	$ 142.3	-	10.0%
Total	**$ 6,235.6**	**100.0%**	**$ 7,661.3**	**100.0%**	**$ 1,425.8**	**22.9%**	**100.0%**

Source: RIPEC calculations based on state budget data - State Budget Office, DOA

* Prior to the FY 2010 budget year, the category "Rhody Health" was allocated throughout Medical Assistance including Managed Care; it is now designated as a separate category and included in "all other". As such, year-to-year comparisons should be made with caution.

** Includes: MAST fund; Central Falls stablization fund; pass-through, distressed communities and library aid; property revaluation program; municipal fire and police incentive pay

*** Operating transfer is a change in accounting that was not in place in FY 2001; prior to FY 2009 these expenditures were either in the grants and benefits category or in operations.

Personnel

The proposed FY 2012 personnel expenditures total $1,743.7 million, an increase of $95.2 million, or 5.1 percent, when compared to the Governor's revised FY 2011 budget. When compared to the FY 2002 budget, personnel expenditures increased from $1,241.3 million ($1,491.5 million adjusted). This represents an increase of 40.5 percent (16.9 percent adjusted) and an average annual rate of 4.3 percent. During this time, the unadjusted average cost per full-time equivalent (FTE) has increased 55.8 percent, from $ 60,232 in FY 2002 to $94,031 in FY 2012. When adjusted, the average cost per FTE increased by $21,552.7, or 29.4 percent.

Table 13
State Personnel Costs - Unadjusted

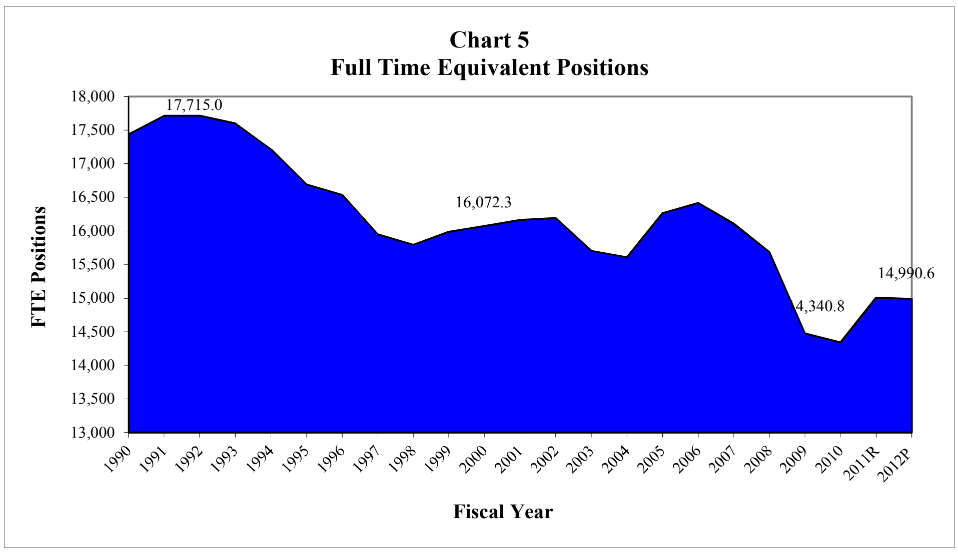
Personnel Costs (Millions)	FY 2002 Actual	FY 2011 Revised	FY 2012 Proposed	FY 2012 - FY 2011 Revised Actual Change	FY 2012 - FY 2011 Revised Percent Change
Salaries & Benefits					
Net Salaries	$ 764.1	$ 902.4	$ 948.4	$ 46.0	5.1%
Adjustment for Temp	(79.0)	(88.0)	(92.9)	(4.9)	5.6%
Overtime	59.8	63.7	48.3	(15.4)	-24.3%
Retirement	50.9	150.9	171.5	20.6	13.6%
Medical	110.5	169.2	169.7	0.4	0.3%
Retiree Health*	-	52.7	56.0	3.3	6.2%
Other Benefits/Payroll**	70.5	85.0	83.3	(1.6)	-1.9%
Salaries & Benefits	*$ 976.7*	*$ 1,336.0*	*$ 1,384.3*	*$ 48.3*	*3.6%*
Funded FTE Positions	**16,191.7**	**15,007.6**	**14,990.6**	**(17.0)**	**-0.1%**
Average Cost Per FTE	**$60,323**	**$90,628**	**$94,031**	**$3,403**	**3.8%**
Other Personnel Costs					
Other Payroll Costs***	$ 105.8	$ 120.6	$ 126.9	$ 6.3	5.2%
Purchased Services	158.8	248.5	232.5	(16.0)	-6.4%
Other Personnel	*$ 264.6*	*$ 369.1*	*$ 359.4*	*$ (9.7)*	*-2.6%*
Total Personnel Costs	**$ 1,241.3**	**$ 1,705.0**	**$ 1,743.7**	**$ 38.7**	**2.3%**

Source: State Budget Office and Personnel Supplements
* Previously included in other costs
** Includes FICA, Holiday Pay, Payroll Accrual and Other
*** Includes temporary and seasonal payroll, unemployment compensation, statewide benefit assessment, anticipated retroactive payments, and workers compensation

Retirement costs remain the fastest growing component of total personnel expenditures over the decade. Expenditures on retirement increased $120.6 million, or 236.9 percent. When these figures are adjusted for inflation, retirement costs increased from $61.16 million in FY 2002 to $171.5 million in FY 2012, or 180.4 percent. In FY 2002, retirement costs accounted for 5.2 percent of salaries and benefits, and have increased to 12.4 percent in FY 2012. The state's actuary recently released a draft report of the pension fund experience study indicating that the actuarial estimate for the FY 2013 annually required contribution (ARC) payment for state employees (excluding judges, state police and teachers) will increase by 35.1 percent, from the current estimate of $182.5 million (5.6 percent of estimated FY 2013 revenues) to a revised estimate of $246.5 million (7.6 percent of estimated FY 2013 revenues). In addition, the Retirement Board-approved changes to the actuarial assumptions increased the normal cost from 9.35 percent to 11.39 percent.

In addition to increases in retirement expenditures, medical costs have increased at a significant rate since FY 2002, growing by 53.5 percent (27.8 percent adjusted). These two categories combined represent 24.6 percent of salaries and benefits in FY 2012 whereas in FY 2002 they accounted for 16.5 percent.

FTE Authorization



In order to manage staffing levels in State government, the State allocates FTE positions to all agencies and departments. These FTE positions now exclude certain positions in higher education that are research-oriented and are financed through Federal or other third-party sources. However, RIPEC continues to include these positions in the totals for comparison purposes. Additionally, some of the positions filled in FY 2011 were hired under the American Recovery and Reinvestment Act (ARRA), which expires in June 2011.

- The FY 2011 Enacted Budget authorized 14,827.6 FTE positions; the Revised Budget includes a total FTE authorization of 15,007.6, which is 180.0 more than in the FY 2011 enacted budget.
- The February 12, 2011 payroll showed a total of 13,781.2 positions filled in the state, which is 1,046.4 FTE positions less than the enacted cap.
- There are a total of 14,990.6 FTEs, including 785.0 higher education positions, authorized in the Governor's FY 2012 budget. This represents a decrease of 7.4 percent over FY 2011 Revised Enacted levels.
- Changes in FTE authorization include: a reduction in the Department of Children, Youth and Families FTE positions by 30.5 positions due to program consolidation; relocation of 80.0 FTE positions associated with administration of the State Medical Assistance Program (Medicaid) to the Executive Office of Health and Human Services (EOHHS); transfer of 23.0 FTE positions from OHHS agencies to OHHS, resulting in a net reduction of 6.6 FTE positions; 180.0 sheriff positions were transferred from Administration to Public Safety.

Retirement

In order to address the growing pension obligations, the Governor has proposed an increase in active state employees' contributions to their retirement fund. All state employee contributions will increase by 3.0 percentage points while teacher contributions will increase by 2.25 percentage points, for a total contribution of 11.75 percent for all employees covered under the proposal. The payment would be in addition to the ARC made by the state and workers. The employer contribution would not be reduced, thus resulting in no budget savings in FY 2012; however, the total supplemental contribution is estimated to generate an additional $40.8 million for the fund.

Based on the most recent experience study released April 13, 2011, unfunded actuarial accrued liability (UAAL) for state employees increased from $2,119 million to $2,700 million, while the UAAL for teachers increased from $3,278 million to $4,133 million. The experience study for state police and judges will be released later this month. Of the four systems (state employees, teachers, police and the judiciary) state employee and teacher retirement funding systems had the lowest funded ratios at 48.4 percent and 48.41 percent, respectively. Between FY 1995 and the FY 2012 proposed budget, the employee share of the annual required contributions (ARC) for teachers decreased from 34.7 percent to 29.9 percent while the state employee contribution as a percent of total ARC decreased from 40.6 percent to 33.8 percent.

Unemployment Insurance Reform

The FY 2011 revised budget includes $590.8 million for unemployment insurance benefits, $95.9 million (16.2 percent) of which is from federal stimulus funds. Unemployment insurance benefits for FY 2012 are estimated at $224.8 million, 100.0 percent of which is from the Employment Security Trust Fund. The lower allocation reflects the expectation that more claimants will exhaust their benefits in FY 2012.

The prolonged recession, high rate of unemployment, and historically weak trust fund reserves have drained the state's trust fund and, as a result, the state has been borrowing from the federal government in order to continue paying unemployment insurance claims (a more in-depth examination of the state's unemployment insurance program and status of the trust fund can be found here). In October of 2009, the state's Employment Security Advisory Council convened to address the issue of trust fund solvency. The Council developed a series of recommendations that were forwarded to the Governor in the spring of 2010, without the Council's full endorsement, and were not, ultimately, included in the FY 2011 budget.

These recommendations, with some revisions, are included in Article 4 of the Governor's FY 2012 budget as proposed. The recommendations include two adjustments to the employer tax, included in the revenue section of this report. The Council also proposed seven changes to the state's unemployment insurance benefit structure as follows:

- Freezing the maximum weekly benefit (MWBA) at its current amount ($551, currently 67.0 percent of the statewide average weekly wage) and reducing the percentage used in calculating the benefit to 57.5 percent of the statewide average weekly wage (SAWW) ($1.3 million in FY 2012).

- Reducing the weekly benefit calculation to replace 50.0 percent (3.85 percent of high quarter wages) of lost wages compared to the current 60.0 percent (4.62 percent of the highest quarter wages) ($2.6 million in FY 2012).
- Changing the method of benefit computation from the claimant's highest quarter wages in the base period to the average of the two highest quarters ($2.2 million in FY 2012).
- Reducing the maximum benefit calculation from 36.0 percent of total base period wages to 33.0 percent of base period wages (no FY 2012 savings).
- Allocating severance pay over a number of weeks based on the claimant's weekly benefit amount, delaying the payment of UI benefits up to 26 weeks ($1.1 million in FY 2012).
- Reducing the maximum dependent's allowance percentage from the higher of $15 or 5.0 percent per dependent to the higher of $15 or 3.0 percent per dependent ($1.1 million in FY 2012).
- Raising the requalification criteria for voluntary quits, misconduct and discharges and refusals of suitable work to eight weeks of work with earnings equal to the claimant's weekly benefit amount (no determinable savings estimate).

These changes are projected to generate savings of $8.3 million in FY 2012, and savings of up to $48.4 million per year when fully implemented.

Human Services/Grants and Benefits Programs

All departments under the Executive Office of Health and Human Services coordinated their budget proposals in order to develop a plan that would best address the rapidly increasing costs of human services programs. The outcome of this process was a series of initiatives aimed at modifying delivery systems including cost-shifting initiatives, streamlining processes and improving allocation or resources through prioritization, rate restructuring, and consolidation or programmatic restructuring.

Medical Assistance

Medical assistance represents the single largest category of expenditures, as well as the fastest-growing category of spending, in the budget. Expenditures as presented on table 13 reflect Medicaid expenditures incurred by the Department of Human Services. These expenditures account for about two-thirds of the total Medicaid budget and include expenditures related to hospitals, nursing homes, managed care (primarily RIte Care), and pharmacy expenditures. It should be noted that prior to the FY 2010 budget year, "Rhody Health" was allocated throughout Medical Assistance including Managed Care; it is now designated as a separate category. As such, year-to-year comparisons should be made with caution.

Between FY 2009 and FY 2011, the state received ARRA funds that were used to supplant general revenue funds. The majority of these funds were through the enhanced federal medical assistance percentage (FMAP), which were used to offset Medicaid-related expenditures and were tied to maintenance of effort (MOE) requirements. These funds are set to expire at the end of the current fiscal year. The Governor's medical assistance budget includes additional general revenues to backfill the loss of these federal revenues ($161.2 million). Table 14 outlines proposed medical assistance spending within the Department of Human Services as proposed.

Table 14
FY 2002 - 2012 Medical Assistance Expenditures ($ millions)

Medical Assistance Program	FY 2002 Audited	FY 2010 Actual	FY 2011 Revised	FY 2012 Proposed	FY 2011 R - 2012 P Change	%
Hospitals	$116.3	$120.9	$122.0	$92.6	($29.4)	-24.1%
DSH	84.3	121.7	122.2	129.8	$7.6	6.2%
Subtotal	*$200.6*	*$242.6*	*$244.2*	*$222.4*	($21.8)	-8.9%
Nursing Homes	$255.1	$334.7	$336.0	$330.5	($5.5)	-1.6%
Home and Community Care	0.9	61.6	73.6	80.0	$6.4	8.8%
Subtotal	*$256.0*	*$396.2*	*$409.6*	*$410.5*	$0.9	0.2%
Pharmacy	$0.0	$12.9	$10.9	$11.3	$0.4	3.7%
Part D Clawback	0.0	26.4	36.4	46.5	$10.1	27.7%
Subtotal	*$0.0*	*$39.3*	*$47.3*	*$57.8*	$10.5	22.2%
Managed Care	$251.8	$546.5	$600.5	$653.3	$52.8	8.8%
Rhody Health	0.0	155.6	175.6	186.2	$10.6	6.0%
Other	213.8	124.5	131.7	121.3	($10.4)	-7.9%
Total	**$922.3**	**$1,504.7**	**$1,608.8**	**$1,651.5**	**$42.6**	**2.6%**
Gen Rev	*$438.0*	*$558.7*	*$631.8*	*$785.6*	*$153.8*	*24.3%*
Stimulus	*$0.0*	*$152.7*	*$133.0*	*$0.0*	*($133.0)*	*-100.0%*

Source: State Budgets, Governor's FY 2012 proposed budget, and RIPEC calculations.

Additional highlights of the Governor's FY 2011 revised and FY 2012 budget include:

- Indexing increases to the reimbursement rate for community hospital services provided through the state's managed care plans to the Center for Medicare and Medicaid Services (CMS) data;
- Reducing the nursing home provider rate reimbursement and revising how nursing homes are reimbursed for treatment;
- Eliminating the Rhode Island Pharmaceutical Assistance to the Elderly (RIPAE) program and using federal funds to support individuals affected by this change;
- Leveraging available $12.7 million in federal revenues from the federal health care reform by providing mental health treatment services under the "health homes" model for two years.
- Shifting expenses to federal funds under the "money follows the person" demonstration grant, which is designed to shift people from long-term care to community facilities, among other cost-shifting initiatives; and
- Savings of $0.4 million (including $0.2 million from general revenues) by using selective contracting for personal care attendant and homemaker services.

Other Human Services Initiatives

- The Governor's budget includes an additional $1.7 million for cash assistance programs, which include TANF/RIWP, child care, SSI and GPA.
- Early intervention program costs will be shifted to available federal funds for general revenue savings of $0.7 million in FY 2011 and $0.5 million in FY 2012.
- An estimated savings of $0.5 million by a series of reforms to DCYF through the "System of Care" initiative.
- The DCYF caseload restructuring initiative will result in $14.6 million of general revenue savings. The caseload in the child welfare and behavioral health programs will reduce the number of residential patients. Initiatives include moving children from residential facilities within 60 days of admittance and increasing community based supports.
- The consolidation of six developmental disabilities state-run group homes will save $1.8 million, $0.8 million from general revenues and affect approximately 30 individuals.
- Continued restructuring of the rates for developmental disabilities services provided to adults and providing services that adequately meet the individual's needs. The Governor projects a savings of $4.6 million, including $2.2 million from general revenues.

Local Aid

Total state aid (aid to local governments excluding federal aid) totals $950.1 million in the Governor's proposed FY 2012 budget. This represents an increase of 11.1 percent since FY 2002 and is $26.4 million (2.9 percent) more than FY 2012 enacted aid. Of the total increase, $24.9 million is related to increases in local aid, almost all of which is the MAST fund and the Central Falls stabilization payment. Education aid is increased by $1.0 million, the net effect of changes in education funding (implementing and fully funding the education funding formula) and the $13.3 million decrease in ARRA fiscal stabilization funds. Charter school aid is now included in "direct education aid", pursuant to the new funding formula. The increase in direct education aid reflects both the implementation of the funding formula to districts and to charter schools in FY 2012.

The FY 2011 revised budget is $2.7 million higher than the FY 2011 enacted budget, reflecting a $4.3 million reduction in education aid and a $7.0 million increase in municipal aid. Reductions in teacher retirement and school housing aid are slightly offset by an increase in ARRA state fiscal stabilization funds. Increases in municipal aid include an additional $5.6 million in distressed communities aid and $1.8 million for Central Falls stabilization.

Table 15
State Aid to Local Government

Major State Aid Program	FY 2002	FY 2011E	FY 2011R	FY 2012P	2011E-2012P Change
Education Aid					
Direct Education Aid*	$566.1	$614.9	$615.6	$660.2	$45.4
Teacher Retirement	31.3	75.6	69.7	82.7	7.1
School Housing Aid	33.2	70.8	68.0	72.5	1.7
Met School	2.2	12.6	12.6	11.6	(1.0)
Charter School Aid (direct and indirect)	6.6	38.0	38.2	0.0	(38.0)
ARRA State Fiscal Stabilization**	0.0	17.9	21.3	4.6	(13.3)
Other Aid***	6.9	3.8	3.8	3.0	(0.9)
Subtotal - Education Aid	*$646.2*	*$833.5*	*$829.2*	*$834.6*	*$1.0*
Municipal Aid					
General Revenue Sharing	$43.6	$0.0	$0.0	$0.0	$0.0
Excise Tax Phase-Out	99.5	10.0	10.0	10.0	0.0
PILOT	18.1	27.6	27.6	27.6	0.0
MAST Fund	0.0	0.0	0.0	19.3	19.3
Central Falls Stabilization	0.0	0.0	1.8	4.9	4.9
Distressed Communities Aid	7.6	10.4	15.6	10.4	0.0
Other Aid****	10.4	12.1	12.1	12.7	0.7
Subtotal - Municipal Aid	*$179.3*	*$60.0*	*$67.0*	*$84.9*	*$24.9*
Pass-through Aid					
Meals and Beverage Tax	$17.6	$18.8	$18.8	$19.3	$0.5
Public Service Corporations Tax	12.2	11.4	11.4	11.4	0.0
Subtotal - Pass-through Aid	$29.8	$30.2	$30.2	$30.7	$0.5
Total State Aid	**$855.3**	**$923.7**	**$926.4**	**$950.1**	**$26.4**

Source: RIPEC calculations based on State and House Fiscal Staff Budget documents
* Includes local school operations, targeted aid, core instruction equity, student equity, professional dev., early childhood, student tech., student language assist., full-day kindergarten, vo-tech equity, group home funding and Central Falls.
** Includes aid to LEAs, Charter Schools and the Met School
*** Includes progressive support and intervention, Hasbro hospital, school visit, RIDE professional dev., textbook loans, school breakfast, telecomm access funds, and the Permanent Education Fund.
**** Includes state library aid, statewide reference library resource grant, library construction reimbursement, municipal police incentive pay, municipal fire incentive pay, and the property revaluation program.

Education Aid Highlights

Total proposed state education aid to local governments for FY 2012 is $834.6 million, including direct education aid (inclusive of charter school aid), teacher retirement, school housing aid, and funding for the Met school. This figure also includes the final disbursement of ARRA State Fiscal Stabilization funds. If these funds were excluded, total proposed state aid to education would be $830.0 million. State-run schools (Davies and the School for the Deaf) are not included in this figure. Proposed FY 2012 funding levels are $1.0 million higher than FY 2011 enacted levels, but remain lower than both FY 2007 and FY 2008 funding levels.

Table 16
Changes to Formula Education Aid ($ millions)

	Districts	Charters	Met/Davies	Total
Enacted FY 2011 Distributed Aid	$632.5	$37.8	$27.9	$698.2
FY 2011 Stablization Shift	-0.7	0.0	0.0	-$0.7
Other Adjustments	-0.3	0.3	0.0	$0.0
All Funds FY 2011 Revised Aid	$631.6	$38.1	$27.8	$697.5
EduJobs General Revenue Reduction	-$29.5	-$1.2	-$1.3	-$32.0
EduJobs Federal Revenue	29.5	1.2	1.3	$32.0
Year 1 Formula Adjustment	13.9	4.8	-1.7	$17.1
All Funds FY 2012 Proposed Aid	$645.5	$42.9	$26.2	$714.5
FY 2012 Change from FY 2011 Revised				
$	$13.9	$4.8	-$1.7	$17.1
%	2.2%	12.6%	-6.0%	2.4%

Excludes transportation and regionalization bonus funds
SOURCE: Senate Fiscal Office documents; RIPEC calculations

Formula education aid as shown on table 16 totals $714.5 million and includes the proposed distribution of $32.3 million in federal EduJobs funds used to offset general revenues in FY 2011 and FY 2012 (NOTE: districts may use the funds in FY 2011. Any funds used in FY 2011 will not be available in FY 2012). The Governor's budget fully funds year one of the Education Adequacy Act, the state's recently-enacted funding formula. The funding formula includes a core instruction amount of $8,333, plus an additional 40.0 percent for each PK-12 student receiving free or reduced-price lunch. The state's share is calculated by multiplying the total amount by the state share ratio (more information on the formula and calculation of the state share can be found here). Additional education aid highlights include:

- Revised FY 2011 education stabilization funds change available funds based on a shift between elementary and secondary education and higher education.
- Funding formula distributions assume a seven-year "phase-in" for districts receiving more revenue under the formula and a ten-year "phase-out" for districts that will see a decrease in state aid.
- Categorical funds for transportation and regionalization and included in the budget, while other categorical funds (high-cost special education, high-cost career and technical start-up funding) are delayed by one year while increased funding for early childhood is delayed for one year.
- School construction aid, group home aid and teacher retirement are adjusted to reflect changes in the current fiscal year and projected FY 2012 expenditures.
- The textbook reimbursement program, which reimburses districts for the cost of providing textbooks to non-public schools, is eliminated.

Municipal Aid Highlights

Recommended total municipal aid is $84.9 million in FY 2012, not including pass-through aid of $30.7 million (plus additional hotel tax revenue of $5.7 million). Proposed FY 2012 municipal aid is $24.9 million (41.5 percent) more than FY 2011 enacted aid. The Governor's FY 2011 revised general revenue expenditures represent an increase of 11.6 percent ($7.0 million) when compared to the FY 2011 enacted budget. In addition:

- The Governor proposes an additional $5.2 million for the distressed communities program in the FY 2011 revised budget. In FY 2012, Burrillville and East Providence will no longer qualify and North Providence will re-qualify.
- Central Falls will receive a total of $2.7 million in FY 2011 and $5.8 million in FY 2012 to cover projected deficits and legal services relating to the non-judicial receivership of the community.
- One percent of the 8.0 percent sales tax on meals and beverages (estimated at $19.3 million) will be dedicated to the Municipal Accountability and Transparency (MAST) fund and will be distributed to municipalities based on the former general revenue sharing formula. In order to be eligible for the funds, municipalities must meet certain criteria:
    - In FY 2012, municipalities must provide a five-year forecast to the Division of Municipal Finance including a baseline forecast and a forecast that includes full funding of pension and other post-employment benefit (OPEB) obligations; provide fiscal impact statements to the Division of Municipal Finance for changes that will affect projected Annually Required Contribution (ARC) payments; and submit financial information on time.
    - In FY 2013, municipalities must comply with the above and: begin to increase pension ARC payments with a maximum time limit of five years to fully fund their ARC payments each year; maintain or increase their dollar contribution if they have not met 100.0 percent of the ARC or Annual Pension Cost (APC), whichever is greater; and increase their annual contribution by 10.0 percent each year if their plan is less than 50.0 percent funded until the fund is at least 50.0 percent funded.
    - In FY 2014, municipalities must comply with the above and: begin or increase funding for OPEB at 100.0 percent or increase their annual OPEB/ARC contribution over a period of ten years, and must join a multiple employer trust if they have not already joined by June 30, 2010.
    - Towns not complying with the above by FY 2014 will face a decrease in the state's contribution to teacher retirement of 5.0 percentage points per year.

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