State of Rhode Island and Providence Plantations

Executive Summary

Fiscal Year 2012

Lincoln D. Chafee, Governor

Overview

Governor Chafee recommends a budget for fiscal year 2012 totaling $7.661 billion in all sources of funds, a decrease of $450.0 million, or 5.6 percent, from the recommended all funds FY 2011 revised budget of $8.111 billion. Of this total, $3.170 billion, or 41.4 percent, is from general revenue, $2.557 billion, or 33.4 percent, from federal funds, $1.725 billion, or 22.5 percent, from other sources, and $209.5 million, or 2.7 percent, is from restricted or dedicated fee funds.

Recommended general revenue funding of $3.170 billion represents an increase of $204.5 million, or 6.9 percent, over the recommended FY 2011 revised budget of $2.965 billion. Federal funds decrease from $3.011 billion in the FY 2011 revised budget to $2.557 billion in the recommended FY 2012 budget, due primarily to the loss of stimulus-related funding. Other funds also decrease from $1.956 billion to $1.725 billion, due primarily to the loss of unemployment insurance funding provided by the Federal Government.

FY 2012 Budget Restores Fiscal Stability

The significant challenge posed by the projected $295.0 million budget deficit in FY 2012 is a result of both long-term structural imbalances between the projected growth in revenues and expenditures, as well as losses totaling $233.3 million in federal stimulus funds for Medicaid and local educational programs. Governor Chafee's FY 2012 Budget is based upon his goal to restore fiscal stability to Rhode Island's finances, while cognizant of the challenges facing our local governments. Solving the state's long-term fiscal imbalance requires fundamental changes to the state's revenue stream and high growth spending programs that drive the budget. Therefore, the Governor's FY 2012 Budget presents a comprehensive plan that brings the operating budget into balance without relying heavily on one time resources and reduces the projected out year deficits by addressing the high growth expenditures in Human Services programs. The deficit resolution in FY 2012 is derived roughly equally from increased revenues and expenditure reductions. These actions are necessary to ensure that future generations have a government capable of providing essential government services in a cost-effective manner.

Tax Policy Initiatives Will Place Rhode Island in Competitive Position

The FY 2012 Budget includes proposed changes to the sales tax and corporate tax structures that will place Rhode Island in a more competitive position with respect to state tax rates. The sales tax modernization plan proposes to impose a one percent tax on most items previously exempt from the sales tax, and expand the base to include items not previously taxed, such as services. This modernization plan provides for an increased revenue flow which is forecast to be less susceptible in economic downturns, while lowering the current sales tax rate from seven percent (7.0%) to six percent (6.0%). This will make Rhode Island more competitive by placing our rates at or below those of our neighboring states. The one percent sales tax will sunset upon enactment by Congress of the Main Street Fairness Act or other legislation that requires remote sellers to collect sales and use taxes on behalf of the State Such legislation will allow Rhode Island to recapture sales tax lost to Internet sales and protect the investments of Rhode Island's bricks and mortar retail businesses. The FY 2012 Budget promotes fairness and equity in Rhode Island's sales tax structure.

The corporate tax proposal modifies the minimum tax by lowering it for most taxpayers, institutes combined reporting, and phases out one of Rhode Island's largest tax expenditures, the preferential rate provided under the Jobs Development Act. The state's corporate income tax rate will be lowered over a three year period from nine percent (9.0%) to seven and one-half percent (7.5%). These changes will make the state corporate tax structure more transparent and fair and will place Rhode Island's rate at or below our neighboring states.

Overview

FY 2012 Budget Presents Disciplined Plans to Address Funding Dilemmas at State and Local Levels

In addition to addressing the persistent structural operating deficit, this budget plan also resolves the funding crises in the state's Unemployment Trust Fund and the Department of Transportation's capital program. The plans to resolve these funding dilemmas would be implemented over a multi-year period, and would finally address issues that have plagued Rhode Island for years. Governor Chafee's budget also includes a new program to address the underfunding of certain local government long term obligations, including pension plans and funding for Post Employment Benefits Other Than Pensions (OPEB). The program would reward local governments that take steps to appropriately fund these obligations and penalize communities that do not. The new Municipal Accountability, Stability and Transparency (MAST) Fund is designed to encourage local governments to focus on determining the sustainability of current plans and providing increased funding to these obligations where inadequately funded. Additionally, the Governor proposes to require members of the State Employees and Teachers Retirement Plan, State Police Retirement plan, and Judges Retirement plan to pay increased contributions to reduce the unfunded liability of those plans, while the State investigates the need to develop a more sustainable system that provides for a formula driven sharing of the actuarially required contributions. This will result in an additional $40.7 million of increased assets flowing into the fund.

FY 2012 Recommended Budget

While revenues are expected to grow by 6.8 percent or $206.1 million in FY 2012 compared to the FY 2011 revised budget, expenditures, if unconstrained, would grow by 12.1 percent or $332.7 million. Growth in social service programs, (including unfavorable changes in federal Medicaid participation due to the end of the stimulus program costing Rhode Island an estimated $215.4 million), scheduled increases in local aid programs, and public employee pensions and benefits, resulted in an initially projected budget gap of approximately $295.0 million. Additional spending requirements identified during the budget development process, increased the projected deficit to over $331.9 million. This increased spending includes the Governor's commitment to fully fund the new education aid funding formula (requiring an additional $7.5 million above previous estimates) and reversing the trend of reduced funding for Higher Education (requiring an additional $6.7 million).

The challenge of balancing the State Budget is more daunting upon a review of where overall general revenue actually goes. Expenditures from general revenue are projected to total $3.2 billion for FY 2012. By function, spending by Human Services agencies represents the largest share with expenditures, totaling $1.260 billion, or 39.8 percent, of the general revenue budget. This supports health care and prescription drug coverage for low-income children, their parents, seniors and the poor, and community residential and treatment programs for the disabled. This is followed by spending for Education, which totals $1.054 billion, or 33.2 percent, and includes local education aid, support for the university and colleges, and scholarships. General revenue expenditures for General Government and Public Safety comprise $414.4 million (13.1 percent), and $402.2 million (12.7 percent), respectively. General Government includes, along with state operations, state aid to municipalities and direct property tax relief. Finally, expenditures for Natural Resources comprise $40.0 million, or 1.2 percent of total general revenue spending. Transportation expenditures are financed by dedicated gasoline taxes and are not a component of general revenue spending.

Overview

General revenue expenditures by category are primarily devoted to financing grants, local aid and personnel. The largest component is grants and assistance expenditures of $1.125 billion, comprising 35.5 percent of total general revenue spending. Local aid expenditures of $895.3 million represent 28.2 percent of total spending; personnel expenditures of $841.8 million comprise 26.6 percent of the budget; operating expenditures total $132.0 million, or 4.2 percent of the budget; and capital expenditures, including debt service, total $168.8 million, or 5.3 percent of the total general revenue budget.

Shared Sacrifice Will Lead to a More Sustainable Budget in the Future

Compared to the recommended FY 2011 revised budget, FY 2012 personnel expenditures increase by $43.6 million or 5.5 percent; operating expenditures increase by $1.7 million or 1.3 percent; local aid expenditures increase by $21.2 million or 2.4 percent; capital expenditures, including debt service, decrease by $7.3 million or -4.1 percent.

Year after year, Rhode Island's budget process has included feverish efforts to offset non-recurring revenues to finance the growth in expenditures. The combined use of one-time revenues and the unrelenting pace of growth in entitlements and employee benefits has left the State with insufficient resources to reliably fund programs that are important to the citizens of Rhode Island. Important and necessary programs, such as local education aid, assistance for higher education, investments in technology and asset protection and many other issues cannot be addressed sufficiently and consistently, when certain areas of government grow at rates that significantly exceed general inflation and the rate of revenue growth. In recent years, local governments have experienced significant reductions in state aid as the state struggled to balance its budget. In addition, the state government workforce has declined by approximately 1,400 FTE positions or 9.2 percent since the start of FY 2007, and the cost of employer sponsored medical benefits for active employees and retirees has been increasingly shifted from the employer to the employee. Concessions were negotiated with employee unions in FY 2009, FY 2010, and FY 2011 to help balance those budgets. In the FY 2012 Budget, expenditure reductions fall primarily in the Human Services programs, which are those with the highest growth rates in recent years, yet have been the least impacted by reductions due to limitations placed on the state through the acceptance of stimulus funding.

Some of the major highlights contained in the expenditures of the FY2012 Budget include:

- Investment in higher education to position Rhode Island for future job growth, through an increase of $10.0 million in the state's contribution over the FY 2011 enacted level.
- Local education aid increases by a net of $13.2 million over the FY 2011 enacted budget, reflecting restoration of the stimulus funding, full financing of the new funding formula, withdrawal of the Education Jobs money in FY 2012 and increases in housing aid and teacher retirement funding.
- Reductions in the Human Services function totaling $60.5 million, which do not impact eligibility for programs, including service delivery systems change initiatives, restructuring of rates, and consolidation of publically managed facilities.
- A three percent reduction in salary costs in cabinet agencies reflecting constrained hiring, to be negotiated concessions or reductions in wages and benefits and prioritization of activities using performance-based budgeting for savings of $19.3 million.

Overview

The FY 2012 budget proposal makes great strides towards eliminating the structural imbalance that has plagued the Rhode Island budget for the past decade, while ensuring the continuity of fiscal support of programs and services that balance the critical needs of the Rhode Island's most vulnerable citizens and Rhode Island taxpayers.

General Revenue Funding for Local Education Aid totals $849.2 million

General revenue funding for local education aid increases by a net of $13.2 million in FY 2012, as compared to the FY 2011 enacted funding level. The Governor's budget restores $17.6 million of education aid for expiring federal State Fiscal Stabilization Funding and provides $17.1 million for year one of the new funding formula. However, the Governor's budget strategy for FY 2012 incorporates $32.3 million of general revenue reductions to local education aid that will be offset by the funding provided through the federal Education Jobs Fund. Including the availability of these federal funds, education aid provided to local communities, charter schools, and state schools in FY 2012 will be $726.3 million, or $18.0 million more than provided in the FY 2011 enacted budget, when State Fiscal Stabilization Funding is taken into account.

The Governor recommends full implementation of the new education funding formula in FY 2012 at a cost of $17.1 million. Beginning July 1, 2011, the formula will distribute education aid to all local educational agencies (LEA), including districts, charter schools and state schools (with the exception of the School for the Deaf, which will be separately funded). The formula allows for the funding to follow the student and was developed with the following guiding principles: build a strong foundation for all children, improve equity among districts and schools, be transparent, and be financially responsible. The new education aid formula determines the amount of funding each LEA shall receive per year. In order for each LEA to achieve its full level of year one funding, the Education Jobs Fund resources can be used to offset any general revenue reductions that occur in FY 2012. The Governor's budget includes the best data available at the time of the budget submission; however these calculations will be updated using March 2011 student data, including final charter school lottery data, which is expected to be finalized by April 1, 2011.

The enacted formula legislation also allowed for additional funding from the state to districts for certain categorical programs, including high-cost special education, career and technical education, early childhood programs, certain transportation costs, and a limited two-year bonus for regionalized districts. The Governor's budget only recommends new funding for the transportation categorical and regionalized bonus, at a cost of $1.9 million, and level funding for the early childhood program in FY 2012, with the expectation that the other programs will be added in FY 2013.

The Governor's budget includes an additional $1.7 million as compared to the FY 2011 enacted funding level for school housing aid and funds the five percent increase in the minimum state share ratio for the school housing aid program. This minimum will increase to 35 percent for projects completed in FY 2011 that are eligible for FY 2012 housing aid. Total funding of $72.5 million is recommended for FY 2012.

The State's share of teacher retirement costs also increases by $7.1 million over FY 2011 enacted levels to $82.7 million. In addition to anticipated payroll growth, the required rate of contribution for the State share rose from 7.76 percent to 9.09 percent in FY 2012.

Restructuring Human Services Programs

In order to address the high growth in the human services programs, the Departments under the Executive Office of Health and Human Services (EOHHS) came together to coordinate their budget proposals to assure that they were consistent and actionable, and to avoid cross-departmental conflicts. This was the first time that many of the staff that participated in this effort collaborated in such an intensive interagency work process and it produced a number of ideas that will be applied to improve programs and services for FY 2012 and beyond.

Several broad themes emerged from this effort. First are a series of service delivery systems change initiatives, all aimed at rationalizing and managing services supporting persons with behavioral health needs, persons with developmental disabilities, and children and youth in the child welfare system. Several of these initiatives will take advantage of opportunities to obtain enhanced federal matching funds under the new Medicaid Health Home option and/or Money Follows the Person Incentive Grants and the authority to use selective contracting, where appropriate, under the Global Waiver.

Second, rates paid to nursing facilities, hospitals, and home health agencies will be re-structured, and the EOHHS departments will examine the opportunity to selectively contract for home health services.

Third, operations at the Training School, the Veterans' Home, and the publically managed group homes for persons with developmental disabilities will be consolidated or restructured, with no reduction in either census or staffing.

Fourth, a number of structural and functional changes, across all Departments, will be undertaken, aimed at streamlining processes and improving allocation and prioritization of staff resources.

Going forward into FY2013 and beyond, the EOHHS Departments face many strategic challenges, including:

- Examining the implications of Federal Health Reform, as well as a series of federal Maintenance of Effort requirements across all of the Departments;

- Re-engineering Intake and Eligibility processes and identifying where they can be consolidated or merged to better serve the consumer;

- Defining the strategic future of the Rhode Island's 24/7 service programs and the patient and resident populations that they support;

- Developing a thoughtful and comprehensive strategy for licensure to assure value for the public and licensees alike.

The efforts of the EOHHS agencies described above resulted in various proposals that will generate approximately $60.5 million in savings in FY 2012 that have been incorporated into the Governor's recommended budget, with potentially greater savings in later years.

Additional State Aid to Distressed Local Governments with Strings Attached

In FY 2011, the Governor recommends a 50 percent increase in the $10.4 million appropriated for distressed communities in the enacted budget. Under this proposal, an additional $5.2 million will be distributed, for a total of $15.7 million in FY 2011. Currently, as a result of the indices established by Rhode Island

General Laws 45-13-12, the following communities receive funds through the Distressed Communities Relief Fund: Burrillville, Central Falls, East Providence, North Providence, Pawtucket, Providence, West Warwick and Woonsocket (Based on current data, Burrillville and East Providence will no longer qualify going forward). In order to receive the additional state aid, distressed communities must submit a 5-year budget forecast to the Division of Municipal Finance by June 20, 2011 including underlying assumptions for the five year planning horizon. In FY 2012, the Governor recommends that $10.4 million be distributed under this program.

Local governments are facing ever-increasing costs for retirement and retiree health care. These two components represent significant cost drivers for municipal budgets. Given this, Governor Chafee is proposing to create the Municipal Accountability, Stability and Transparency (MAST) Fund. The MAST Fund is designed to encourage local governments to focus on the sustainability of current plans and reduce the unfunded liability of significantly underfunded pension plans. In addition, the MAST Fund addresses the significant unfunded liabilities for Post Employment Benefits Other Than Pensions (OPEB). It is projected that this fund would total $19.3 million, which would be available for municipal governments. Distribution of the MAST Fund receipts to each community is based on the 2009 General Revenue Sharing percent distribution.

Governor Chafee's proposed FY 2012 budget includes an appropriation to the City of Central Falls over two years, $1.8 million in FY 2011 and $4.9 million in FY 2012. The City has been operating under the oversight of a State-appointed Receiver pursuant to *An Act Relating to Cities and Towns – Providing Financial Stability*, codified as Rhode Island General Laws § 45-9-1 et seq., since July 2010. In December 2010, the Receiver issued a report detailing the structural fiscal problems plaguing the City and outlining a variety of reform measures for consideration to restore the City to long-term fiscal stability. Since that time, the City's FY 2010 audit has been completed, identifying an actual year-end deficit of $2.4 million. The Receiver has identified $623,000 in City assets which may be applied to reduce this deficit, leaving a balance of approximately $1.8 million. In addition, the Receiver forecasts a deficit of approximately $4.9 million for FY 2012 that must be resolved to avoid a liquidity crisis in early FY 2012. The City currently has severely limited access to financing and cannot otherwise raise the revenues necessary in the short term to resolve these deficits. The $6.7 million appropriation will eliminate these deficits and resolve the City's projected liquidity problems for FY 2012.

Personnel Funding and FTE Levels

State personnel costs comprise 22.6 percent of total recommended spending in FY 2012. Actual filled positions totaled 13,781.2 as of February 12, 2011, a 195.5 position increase from the 13,565.7 filled position level as of January 2, 2010, but still 1,301.6 FTE below the 15,082.8 FTE level in July 2007. The filled level of 13,781.2 FTE is 1,046.4 FTEs (7.1 percent) less than the enacted cap of 14,827.6.

In order to maintain an acceptable level of critical services and reflecting the availability of federal funds, the Governor recommends an increase in the number of full-time equivalent positions. From the FY 2011 enacted level, the Governor recommends an increase of 180.0 FTE positions bringing the new authorized level to 15,007.6 FTE. This increase is due to 46.0 new federally funded positions in the Department of Health, 22.0 federally funded positions for the administration of the Supplemental Nutrition Assistance Program (SNAP) and 10.0 positions for the Office of Rehabilitation Services/Disability Determination Services in the Department of Human Services, 22.0 positions in the Department of Elementary and Secondary Education financed with the Race to the Top federal grant, 65.0 positions at the Community College of Rhode Island and 6.0 federally funded firefighter positions within the Air National Guard section of the Military Staff.

Overview

In FY 2012, the Governor recommends a total FTE level of 14,990.6, including 785.0 Higher Education federal/sponsored research positions, a net decrease of 17.0 FTE's from the revised FY 2011 level, but a 163.0 increase from the FY 2011 enacted level. The reduction in FTE primarily occurs in the Department of Labor and Training due to the elimination of limited period positions whose funding under the American Recovery and Reinvestment Act will cease in FY 2012. The Department's FTE level decreases by 36.8 in the Workforce Development program and by 5.5 in the Workforce Regulation program. The Department of Children, Youth and Families' FTE level decreases by 29.0 positions due to projected attrition from facilities consolidation and system of care transformation implementation. Offsetting these decreases are 17.5 new professor positions at the Rhode Island College for accreditation requirements and 39.0 additional positions at the new Department of Veterans' Affairs, including a new Director, benefit specialist staff and clinical staff due to an initiative that will result in an increased census at the Veterans' Home. These new positions will be funded from restricted revenues resulting from the increased census.

Focus on the Future-Technology Infrastructure

The FY 2012 budget continues projects to improve State Government information technology by funding projects with statewide interest in the areas of: 1) revenue forecasting and collection through additional enhancements to the Division of Taxation's data warehouse, 2) human resource management by implementing the first phase of the Oracle Human Resources module, and 3) funding for an Internet-based data sharing application for use by local governments when reporting data to the Division of Municipal Finance. Rhode Island must strengthen its technology to enable an innovation economy and to solve the real problems of our day. The Governor recommends $11.5 million from the Rhode Island Capital Plan Fund (RICAP) over a four year period for the installation of the Human Resource module, followed by other modules that are part of the statewide financial management system. An additional $15.5 million is also proposed from the RICAP fund over a five year period for other technology initiatives throughout state government. Ongoing State government projects include a replacement of the outdated system presently used by the Division of Motor Vehicles ($12.8 million), enterprise infrastructure upgrades ($3.9 million), and integrated, web-based licensing capability ($1.0 million).

The Governor's Revenue Program

Addressing the Structural Deficit to Ensure a Future of Prosperity

At the Budget Summit hosted by then Governor-elect Lincoln D. Chafee in December 2010, the general revenue deficits projected by the Budget Office and the Office of Revenue Analysis started at $295.0 million in FY 2012 rising incrementally to $457.8 million in FY 2016. The cause of these projected deficits is two-fold. First, general revenue expenditures shoot up by 10.5 percent in FY 2012, primarily due to the expiration of federal stimulus monies, and then increase on average by 3.3 percent over the FY 2013 to FY 2016 period. Second, general revenues increase by only 0.5 percent in FY 2012, primarily due to the sluggish economic recovery, and then increase on average by 2.4 percent over the FY 2013 to FY 2016 period. To address this ongoing structural deficit, the Governor's FY 2012 Budget proposes to reduce the rate of growth in general revenue expenditures by reforming those expenditure categories with the highest rates of growth and to halt the erosion of the state's revenue base due to structural changes in the state's economy while improving the state's economic competitiveness.

Improving Rhode Island's Business Tax Competitiveness

During the 2010 session, the General Assembly passed and Governor Donald L. Carcieri signed into law historic tax reform legislation that significantly improved Rhode Island's tax rate competitiveness as it pertains to the personal income tax. Governor Lincoln D. Chafee proposes to take the next step in this process through his *Business Tax Competitiveness Proposal.* The Business Tax Competitiveness Proposal is a multi-faceted approach that is designed to support all businesses in the state and make Rhode Island's corporate tax rate competitive with neighboring states. The Governor's Business Tax Competitiveness Proposal consists of five parts: (1) a phased-in reduction in the State's business corporations tax rate beginning in tax year 2012; (2) a phased-in elimination of the Jobs Development Act rate reduction beginning in tax year 2012 for taxpayers that file under the business corporation tax; (3) the implementation of combined reporting for business entities subject to the business corporations tax effective for tax year 2012 and beyond; (4) the subjection of limited partnerships and limited liability partnerships to the state's corporate minimum tax; and (5) a restructuring of the corporate minimum tax and the minimum franchise tax from a flat $500.00 for all filers to a graduated tax that is dependent on a business' Rhode Island gross receipts.

Currently, Rhode Island's business corporation (i.e., corporate income) tax rate is 9.0 percent, the highest in New England, similar to the situation Rhode Island found itself in with respect to the personal income tax prior to the passage of the reform last year. Rhode Island's Jobs Development Act rate reduction is unique among the New England states and was used by only 14 taxpayers in tax year 2008. The Governor proposes to phase-out the Jobs Development Act over a three year period. The proposed incremental changes in the business corporation tax rate and the Jobs Development Act rate reduction are shown below:

Tax Year	Business Corporation Tax Rate	Change in Jobs Development Act
2011	9.0 %	Full Rate Reduction Available
2012	8.5 %	1/3 of Full Rate Reduction Eliminated
2013	8.0 %	1/3 of Full Rate Reduction Eliminated
2014	7.5 %	1/3 of Full Rate Reduction Eliminated
2015 and thereafter	7.5 %	No Rate Reduction Available

The Governor's Revenue Program

The revenue loss to the State from the reduction in the business corporation tax rate from 9.0 to 8.5 percent for FY 2012 is estimated to be $8,525,365 while the revenue gain to the State from the elimination of one-third of the full Jobs Development Act rate reduction is estimated to yield $4,845,502.

Combined Reporting Levels the Playing Field for Smaller Regional Businesses Vis-à-vis Large Multistate Corporations

The implementation of combined reporting for business corporation tax filers effective for tax years beginning on or after January 1, 2012 will bring Rhode Island's corporate filing requirements in line with those of Maine, New Hampshire, Vermont and Massachusetts, with the latter two states adopting combined reporting filing requirements in 2006 and 2009 respectively. Combined reporting is also required by the federal government. Combined reporting will inure the State from tax planning activities engaged in by multistate corporations designed to shift income from higher corporate tax states to lower or no corporate tax states. The end result of these tax avoidance schemes is to shift the burden of state corporate taxation from multistate national firms to local or regional companies that have a smaller national footprint. The Department of Revenue estimates that the implementation of combined reporting will generate $8,891,640 of additional revenue in FY 2012.

The final planks of the Governor's Business Tax Competitiveness Proposal are to treat businesses with similar limited liability protection equitably and to restructure the corporate minimum and minimum franchise taxes to lower the rate for small businesses. With respect to the treatment of businesses with similar limited liability protection, the Governor proposes to subject limited partnerships (LP) and limited liability partnerships (LLP) to the state's corporate minimum tax putting these business entities on par with limited liability companies (LLC) and subchapter S corporations. With respect to the restructuring of the corporate minimum and minimum franchise taxes, the Governor proposes tiered minimum taxes based on a business' Rhode Island gross receipts as follows:

Rhode Island Gross Receipts	Business Structure	Minimum Tax
$0 to $999,999	C-corporation	$500
	S-corporation, LLC, LP or LLP	$250
$1,000,000 to $2,499,999	C-corporation	$1,000
	S-corporation, LLC, LP or LLP	
$2,500,000 to $4,999,999	C-corporation	$1,500
	S-corporation, LLC, LP or LLP	
$5,000,000 and over	C-corporation	$2,000
	S-corporation, LLC, LP or LLP	

The Department of Revenue estimates that the revenue impact of the combined restructuring of the corporate minimum and minimum franchise taxes and the inclusion of limited partnerships and limited liability partnerships is a revenue loss of $6,117,310 in FY 2012.

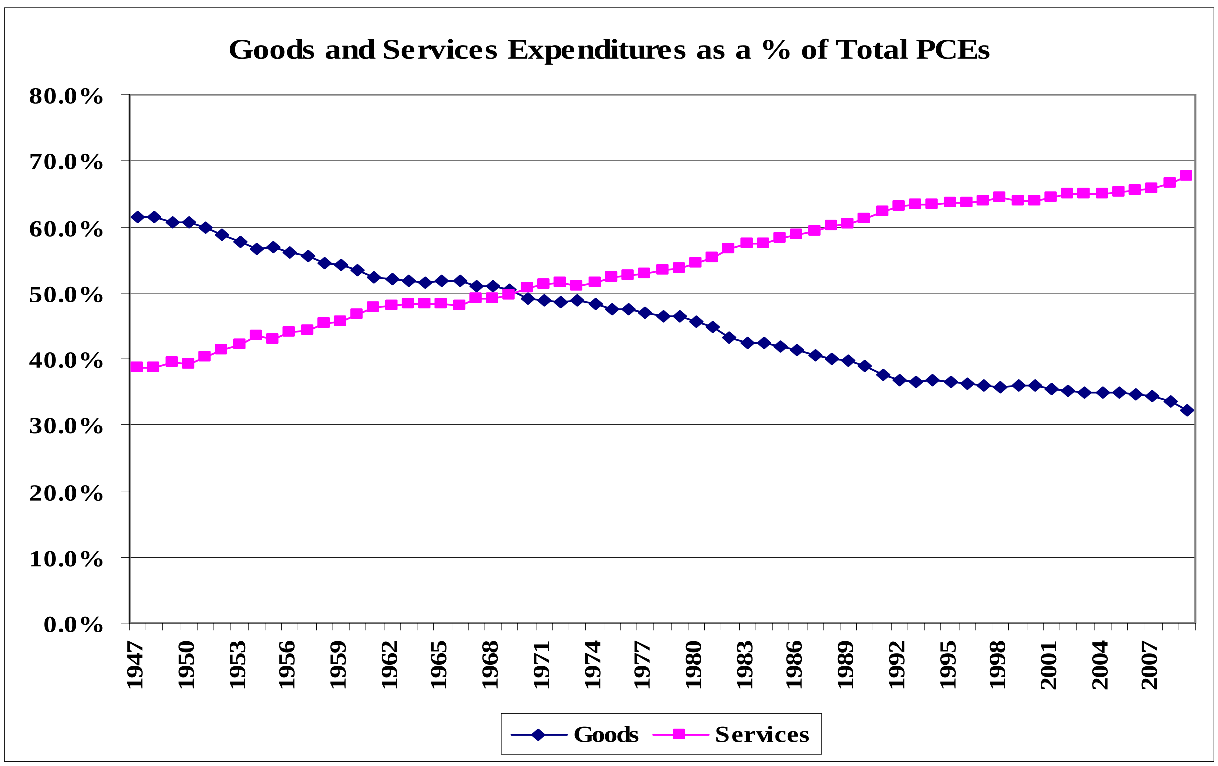
Taken as a whole, the net revenue impact of the Governor's Business Tax Competitiveness Proposal is a revenue loss in FY 2012 of $905,533. The FY 2013 through FY 2016 revenue impact of the Governor's Business Tax Competitiveness Proposal by each component and in combination is shown in the table below:

The Governor's Revenue Program

Proposal	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
Rate Reduction Phase-In	$ (8,525,365)	$ (20,005,564)	$ (33,967,968)	$ (35,345,444)	$ (36,466,135)
Jobs Dev Act Phase-Out	4,845,502	9,345,814	15,367,882	15,991,083	16,498,109
Combined Reporting	8,891,640	9,993,357	10,955,116	11,399,371	11,760,808
Minimum Tax Restructure	(6,117,310)	(6,166,843)	(6,241,142)	(6,290,675)	(6,364,975)
Total	***$ (905,533)***	***$ (6,833,236)***	***$ (13,886,112)***	***$ (14,245,665)***	***$ (14,572,193)***

Ensuring That Rhode Island's Revenue Base Keeps up with Changing Consumption Patterns

The first state to impose a sales tax on the purchase of tangible personal property was Mississippi in 1932. Twenty-five other states had adopted a sales tax by 1938. Rhode Island put in place a 1.0 percent sales tax on July 1, 1947. Rhode Island's sales tax rate was increased in FY 1952 to 2.0 percent, in FY 1958 to 3.0 percent, in FY 1965 to 3.5 percent, in FY 1966 to 4.0 percent, in FY 1968 to 5.0 percent, in FY 1977 to 6.0 percent, and in FY 1991 to 7.0 percent where it has remained. During this time period, a total of 82 exemptions to the sales tax have been enacted into law with 20 of those 82 being enacted since 1992.



Rhode Island's sales and use tax applies to a base that is largely tangible personal property and a very small number of services (primarily telecommunication services). When Rhode Island's sales tax was enacted spending on goods comprised 60.0 percent of total personal consumption expenditures (PCE), while spending on services made up the other 40.0 percent. By 1970 spending on services had surpassed spending on goods. In 2009, spending on services was nearly 70.0 percent of total expenditures while spending on goods was 30.0 percent.

In the mid- to late 1960s, the state sales tax rate was increased by two percentage points or 40.0 percent. These increases did not happen by accident but rather were the State's attempt to maintain the revenue product from the sales tax in the face of a declining sales tax base. More recently, the growing popularity of remote sales that is purchases from vendors that do not have a physical presence in the state, has further eroded sales tax collections, as these vendors are not required to charge, collect and remit the sales tax on the state's behalf. It is estimated that the revenue lost to Rhode Island from remote sales is approximately $70.4 million in 2012.

The Proposed Sales Tax Rate of 6.0 Percent Will Be Lower than Massachusetts' Rate of 6.25 Percent and Connecticut's Proposed Rate of 6.35 Percent

As a means to shoring up the sales tax base from the erosion of the shift in consumption from goods to services and the increase in the number of transactions between Rhode Island consumers and remote sellers, Governor Chafee puts forth his *Sales Tax Modernization Proposal*. The Sales Tax Modernization Proposal has five component parts: (1) a reduction in the state sales tax rate to 6.0 percent; (2) a modernization of the sales tax base to include select services currently not subject to the sales tax and the removal of the current sales tax exemption for certain items with both to be taxed at the 6.0 percent rate; (3) a broadening of the sales tax base from the removal of the current sales tax exemption from certain items and the taxing of these items at a 1.0 percent rate; (4) maintaining the 8.0 percent tax rate for meals and beverages, currently consisting of the 7.0 percent state sales tax rate and the 1.0 percent local meals and beverage tax, with the 1.0 percent differential dedicated to the new Municipal Accountability, Stability and Transparency (MAST) Fund; and (5) retaining the 8.0 percent tax on lodging and room rentals, currently consisting of the 7.0 percent state sales tax and the 1.0 percent local hotel tax, with the incremental 1.0 percent allocated a new Tourism Asset Protection Fund.

The reduction in the state sales tax rate from 7.0 percent to 6.0 percent will make Rhode Island's sales tax rate lower than Massachusetts' current state sales tax rate of 6.25 percent and lower than Connecticut's proposed state and local sales tax rate of 6.35 percent. (Connecticut's current general sales tax rate is 6.0 percent with no local option sales tax.) This reduction will provide Rhode Island based retailers of durable goods, particularly big ticket items such as motor vehicles, furniture and consumer electronics, with a competitive advantage over their counterparts in Massachusetts and Connecticut. The Department of Revenue estimates that the reduction in the sales tax rate to 6.0 percent will decrease revenues by $117,714,286 in FY 2012.

The modernization of the sales tax base will allow the State to preserve its sales tax revenues in the face of increasing consumption by households and businesses of services relative to goods. In addition, removing the current exemption for certain items will help to restore the sales tax base by including more stable elements of consumption. The sales tax base modernization includes the following goods and services that would be subject to the state's sales tax at a rate of 6.0 percent:

The Governor's Revenue Program

Goods Currently Exempt from Sales and Use Tax
Prewritten computer software delivered electronically
Corrective eyeglasses and contact lenses
Nonprescription drugs including medical marijuana
Newspapers
Insurance proceeds from destroyed or stolen passenger car as trade-in allowance
Property or supplies used in the processing or preparation of floral products and arrangements
Services Currently Not Subject to Sales and Use Tax
Garbage and trash collection including certain waste management and remediation services
Taxicabs and other road transportation services
Scenic and sightseeing transportation and support activities and package tours
Couriers and messengers
Moving, storage, including warehousing, and freight services
Photo studios including photographic and portrait photography services
Pet services except veterinary services including testing laboratories
Data processing, hosting, and related services
Facilities support services
Business support services
Investigation and security services including locksmiths
Services to building and dwellings including domestic services, extermination and pest controls services, landscaping services and other support services from commercial providers
Employment agency services
Personal care services including hairdressing salons and personal grooming establishments, diet and weight reducing centers and other personal services
Laundry and dry cleaning services
Recreation and Entertainment to be Subjected to Sales and Use Tax
Membership clubs and participant sports centers including bowling centers but excluding aircraft rental and leasing without pilots and marinas and boat storage
Amusement parks, campgrounds, and related recreational services including fitness and recreational sports centers but excluding sales by elementary and secondary schools, tuitions and fees paid to fine arts schools and promoters of performing arts, sports and similar events
Motion picture theaters including those of post secondary educational institutions
Live entertainment excluding sports and promoters of performing arts, sports and similar events and independent artists, writers, and performers
Spectator sports except elementary and secondary schools and promoters of performing arts, sports and similar events
Museums, historical sites, zoos, parks, art galleries and libraries

Maintenance and Repair, Labor Separately Stated to be Subject to the Sales and Use Tax
Motor vehicle including car washes
Audio-visual, photographic and information processing equipment
Electronic and precision equipment
Commercial and industrial equipment except for manufacturers
Recreational and sports equipment except for boats
Furniture, furnishings, and floor coverings
Household appliances
Clothing and footwear repair, rental and alterations
Watch, clock and jewelry repair
Other Items Subject to the Sales and Use Tax
Professional association dues except for alumni associations, parent-teacher organizations, booster clubs, scouting organizations, veterans membership organizations, political organizations, athletic associations, regulatory or administrative associations, property owners' associations, condominium and homeowners' associations, tenant associations, and cooperative owners' associations

The sales tax base modernization taxed at 6.0 percent is projected to yield $197,594,235 in FY 2012, including the sales tax on medical marijuana and the disallowance of insurance proceeds as the trade-in allowance on private passenger automobiles.

The Currently Exempt Items That Will Be Subject to the 1.0 Percent Sales Tax Does NOT Include Food, Prescription Drugs or Gasoline

The expansion of the sales tax base to include certain items that are currently exempt from the sales and use tax will provide the State with a more stable sales tax base upon which to levy a tax. The sales tax rate proposed for these items is 1.0 percent fulfilling the Governor's campaign pledge to tax at least some exempt items at a 1.0 percent rate. It is important to note that the currently exempt items that will be subject to the 1.0 percent sales tax rate do not include food and food ingredients, prescription drugs, durable medical equipment or gasoline. The list of the currently exempt items subject to the 1.0 percent sales tax is as follows:

Items Currently Exempt from the Sales and Use Tax
Agricultural products for human consumption
Air and water pollution control facilities
Aircraft, including aircraft rental and leasing without pilots, and aircraft parts
Banks and Regulated Investment Companies interstate toll-free calls
Boats or vessels brought in exclusively for winter storage, maintenance, repair or sale
Boats or vessels generally
Boats to nonresidents
Building materials used to rebuild after a disaster
Casual sales
Clothing and footwear
Coffins, caskets and burial garments

Items Currently Exempt from the Sales and Use Tax (Continued)
Coins
Commercial fishing vessels in excess of five net tons
Commercial vessels of more than 50 tons burden
Compressed air
Containers
Dietary supplements
Educational institutions rental charges
Electricity, steam and thermal energy from the Rhode Island Economic Development Corp.
Equipment for research and development
Farm equipment
Farm structure construction materials
Flags
Heating fuels used in the heating of homes and residential premises
Horse food products
Jewelry display product
Manufacturers' machinery and equipment
Precious metal bullion
Promotional and product literature of boat manufacturers
Purchases used for manufacturing purposes
Renewable energy products
Rhode Island Economic Development Corporation project status designees
Rhode Island Industrial Facilities Corporation Lessees
Sales by writers, composers and artists
Sales in municipal economic development zones
Sales to charitable, educational or religious organizations
Sales of trailers ordinarily used for residential purposes
Supplies used in on-site hazardous waste recycling, reuse or treatment
Textbooks
Total loss or destruction of a motor vehicle within 120 days of tax payment
Trade-in value of boats and private passenger automobiles
Transfers or sales made to immediate family members
Transfers or sales related to a business dissolution or partial liquidation
Water for residential use

As a result of the sales tax base expansion to exempt items and the taxing of these items at a rate of 1.0 percent, the State will be put in noncompliance with the Streamlined Sales and Use Tax Agreement (SSUTA). Under the SSUTA, signatory vendors collect on behalf of the State sales and use taxes due on purchases made by state residents and remit the taxes collected to the State. Once Rhode Island is no longer in compliance with the SSUTA, signatory vendors would no longer be obligated to continue the collection and remittance of these taxes to the State. The Governor's proposed 1.0 percent tax on certain currently exempt items is set to sunset when federal legislation is passed requiring remote sellers to collect and remit to the State taxes on transactions between remote sellers and the state's residents. This sunset provision would put Rhode Island back in compliance with the SSUTA contemporaneously with the State being granted the power to collect these taxes.

The Department of Revenue estimates that the imposition of a 1.0 percent sales tax on the above listed exempt items will generate $86,840,462 in sales tax revenue in FY 2012. The revenue lost from the State falling into noncompliance with the Streamlined Sales and Use Tax Agreement is estimated at $1,840,011. Thus, the net revenue impact from the expansion of the sales tax base to certain currently exempt items taxed at a 1.0 percent rate is $85,000,451.

The Governor's Meals and Beverage Tax Proposal Will Provide Financing for the Newly Created MAST Fund

Currently, the state and local meals and beverage tax rate is 8.0 percent, comprised of the state's 7.0 percent sales tax rate and the 1.0 percent local meals and beverage tax rate. Under the Governor's sales tax modernization proposal, the state sales tax rate is being reduced to 6.0 percent. Rather than have the state and local meals and beverage tax rate decline to 7.0 percent with the decrease in the sales tax rate, Governor Chafee proposes to maintain the state and local meals and beverage tax rate at 8.0 percent and to designate the 1.0 percent that previously went to the state to finance the newly created Municipal Accountability, Stability and Transparency (MAST) Fund. The MAST Fund is intended to provide an incentive to cities and towns to employ fiscally prudent budgeting practices and address unfunded liabilities for pensions and Other Post Employment Benefits (OPEB). Cities and towns will receive additional state aid starting in FY 2012 and thereafter if they comply with certain requirements as set forth in statute. The Department of Revenue estimates that the maintenance of the state and local meals and beverage tax rate at 8.0 percent will generate $19,330,231 for the MAST Fund in FY 2012.

The Retention of an 8.0 Percent Tax on the Rental of Rooms and Lodging Will Finance the Newly Created TAP Fund

In a similar vein, the Governor proposes the creation of the Tourism Asset Protection (TAP) Fund to be financed by retaining the tax rate on the rental of rooms and lodging at 8.0 percent. Under current law, the state and local tax on the rental of rooms and lodging is comprised of the state sales tax rate of 7.0 percent and the local hotel tax rate of 1.0 percent. Under the Governor's sales tax modernization proposal, the state sales tax rate is being reduced to 6.0 percent. Rather than have the state and local tax on the rental of rooms and lodging decline to 7.0 percent with the decrease in the sales tax rate, Governor Chafee proposes to maintain the state and local tax rate on the rental of rooms and lodging at 8.0 percent and to designate the 1.0 percent that previously went to the state to finance the newly created TAP Fund. The TAP Fund is designed to provide monies for the construction, improvement, and/or preservation of state assets directly related to the tourism industry. The Department of Revenue projects that the retention of the state and local tax of 8.0 percent on the rental of rooms and lodging will provide $2,620,180 to the TAP fund in FY 2012.

Taken as a whole, the net revenue impact of the Governor's Sales Tax Modernization Proposal is a revenue increase of $164,880,400 in FY 2012. The FY 2013 through FY 2016 revenue impact of the Governor's Sales Tax Modernization Proposal by each component and in combination is shown in the table below:

The Governor's Revenue Program

General Revenue Proposal	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
Sales Tax Rate to 6.0%	$ (117,714,286)	$ (120,734,637)	$ (121,584,056)	$ (122,431,472)	$ (123,280,080)
Base Mod at 6.0%	195,908,719	200,935,408	202,349,074	203,759,406	205,171,721
Exempt Items at 1.0%	86,840,462	89,102,305	89,744,226	90,386,148	91,028,069
Lost Revenue from SSUTA	(1,840,011)	(1,863,398)	(1,878,916)	(1,873,824)	(1,876,279)
Med Marijuana at 6.0%	802,659	1,333,365	1,342,971	1,352,577	1,362,183
No Ins Proceeds as Trade-In	882,857	905,852	912,378	918,904	925,430
General Revenues Total	***$ 164,880,400***	***$169,678,895***	***$ 170,885,678***	***$ 172,111,739***	***$ 173,331,044***
Non-General Rev Proposal	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**	**FY 2016**
MAST Fund	$ 19,330,231	$ 19,833,706	$ 19,976,594	$ 20,119,482	$ 20,262,370
TAP Fund	2,620,180	2,688,425	2,707,793	2,727,162	2,746,530
Non-General Rev Total	***$ 21,950,411***	***$ 22,522,131***	***$ 22,684,387***	***$ 22,846,644***	***$23,008,900***

In addition to the Business Tax Competitiveness and the Sales Tax Modernization Proposals, the Governor's FY 2012 Budget includes a variety of other tax and fee proposals. These items are detailed in the **General Revenues** section of the *Executive Summary*.

The Economy

Introduction

The Consensus Revenue Estimating Conference (REC) convenes at least twice each year, typically within the first ten days of May and November. Historically, the purpose of the conference was confined to forecasting current and budget year revenue estimates. During the 1998 legislative session, the Revenue Estimating Conference statutes were modified to also require the adoption of a consensus economic forecast. Prior to the November 2001 conference, the conferees adopted a forecast for Rhode Island total employment, Rhode Island personal income, and the U.S. consumer price index for all urban consumers (CPI-U) covering the state's prior fiscal year, its current fiscal year, and the budget year.

Beginning with the November 2001 conference, in addition to Rhode Island total employment, Rhode Island personal income and the U.S. CPI-U, forecasts for Rhode Island wage and salary income, Rhode Island dividends, interest and rent, the Rhode Island unemployment rate, the interest rate for ten year U.S. Treasury notes, and the interest rate for three month U.S. Treasury bills are also agreed upon at the Revenue Estimating Conference. Finally, the consensus forecast of these economic variables now includes the prior calendar and fiscal years, the current calendar and fiscal years, the budget calendar and fiscal years, and the next five calendar and four fiscal years.

Economic Forecast

This section describes the economic forecast used as an input for the Revenue Estimating Conference's consensus revenue estimates.

During its November 2010 meeting, a forecast of the U.S. and Rhode Island economies was presented by Moody's Economy.com. The Rhode Island Department of Labor and Training (DLT) also presented current employment and labor force trends in Rhode Island. The conferees heard the testimony of Andres Carbacho-Burgos, an economist with Moody's Economy.com, and Robert J. Langlais, Assistant Director for DLT's Labor Market Information unit.

The Revenue Estimating Conference adopted the economic forecast shown below on November 5, 2010 through a consensus process informed by the testimony of Dr. Carbacho-Burgos and Mr. Langlais. The updated economic forecast made significant changes to the consensus outlook adopted at the May 2010 Revenue Estimating Conference.

As reported at the November 2010 Revenue Estimating Conference, Rhode Island's labor market continued to feel the effects of the "Great Recession". The Rhode Island Department of Labor and Training reported that the unemployment rate decreased to 11.5 percent in September 2010 after peaking at 12.7 percent in December 2009. This was a decrease of 1.2 percentage points recording the lowest unemployment rate since July of 2009 when it was 11.4 percent and the first year over year decrease since before the national recession. There was a year-over-year increase of 3,600 employed Rhode Islanders in September 2010 while the number of unemployed Rhode Islanders declined by 2,500.

Rhode Island establishment employment declined over the period resulting in a decrease of 5,200 jobs from September 2009 to September 2010. The sector breakdown of these job losses were as follows: Retail Trade, -2,100; Accommodation and Food Services, -1,300; Professional and Business Services, -1,200; Manufacturing, -1,200; Wholesale Trade, -900; Arts and Entertainment, -700; Educational Services, -200; and Government, -100. The broad sectors of the Rhode Island economy which added jobs year-over-year in September 2010 were as follows: Health Care and Social Assistance, 1,100; Other Services, 500; Financial Activities, 300; Transportation and Utilities, 200; Information, 200; Natural Resources and Mining, 100; and Construction, 100. In fact, since the January 2007 peak employment of

496,500 jobs, Rhode Island businesses have shed 47,900 jobs as of September 2010, a decline of 9.6 percent.

While there is no official measurement and dating of recessions at the state level, employment is usually used to gauge the cyclical status of the state economy. In FY 2009, total non-farm employment declined by 3.6 percent, followed by a further decline of 3.7 percent in FY 2010. Total non-farm employment is projected to increase by an additional 0.1 percent from 453,200 in FY 2010 to 453,600 in FY 2011. The principals anticipate an increase of 7,400 jobs in non-farm employment for FY 2012 and an increase of 14,700 jobs in FY 2013. Over the FY 2014 through FY 2016 period, Rhode Island's economy is expected to add 36,500 jobs. It should be noted that while adopted growth rates indicate a positive trend from FY 2011 through FY 2014, the adopted number for total non-farm employment during these years is below those adopted for the same period at the May 2010 Conference. It is not until FY 2015 that the estimate for total non-farm employment adopted at the November 2010 Conference excees the estimate adopted at the May 2010 Conference.

The unemployment rate for FY 2011 is projected to decline slightly from 12.3 percent in FY 2010 to 11.8 percent. As recovery takes hold, Rhode Island's unemployment rate is expected to decline rapidly from 11.3 percent in FY 2012 to 5.9 percent in FY 2016. Even at this lower rate, Rhode Island's unemployment rate will be 0.9 percentage points higher than the unemployment rate achieved when the economy peaked in FY 2007.

Personal income is expected to improve to a 2.0 percent rate of growth in FY 2011 up from 0.5 percent growth in FY 2010. The November 2010 Conference estimates for personal income growth suggest a positive upward trend from FY 2011 through FY 2016. It should be noted that the adopted estimates for personal income growth are below, except for FY 2013, the adopted estimates for the same period during the May 2010 Conference. For FY 2012, the projected growth rate for personal income is 3.2 percent, down from 3.7 percent that was adopted in May. For FY 2013 it is 5.0 percent, up from 4.9 percent that was adopted in May. The personal income growth rate is expected to decrease to 4.4 percent in FY 2014 and remain at or above 3.7 percent throughout the remainder of the forecast period. This projection is consistent with the forecast adopted in May 2010.

Similarly, estimates of dividend, interest and rents are expected to increase slightly in FY 2011 before bouncing back considerably in FY 2012 through FY 2016. Wage and salary income growth is estimated to increase in FY 2011 relative to the estimate growth adopted in May 2010 but then decrease relatively in FY 2012 before increasing from FY 2013 to FY 2016 again relative to the estimates adopted in May 2010. Wage and salary income growth is expected to improve beginning in FY 2012 with projected growth of 2.4, percent an increase of 0.8 percentage points from FY 2011. The rate of growth accelerates in FY 2013 to 5.4 percent and remains steady in FY 2014 at 5.3 percent before decelerating in FY 2015 and FY 2016 to 4.2 percent and 3.4 percent respectively.

The U.S. rate of inflation as measured by CPI-U is anticipated to increase to 1.2 percent in FY 2011 from 1.0 percent in FY 2010. The increase is mainly due to the increase in gasoline, fuel oil and natural gas prices combined with the expectation of quantitative easing from the Federal Reserve. The CPI-U is forecasted to increase further in FY 2012 to a 2.0 percent before rising to 2.8 percent in FY 2013. In FY 2014 through FY 2016, inflation is expected to decelerate and settle at 2.2 percent in FY 2016.

From FY 2011 through FY 2012, the interest rate on three month Treasury bills is expected to remain low with rates of 0.3 and 0.7 percent respectively. In FY 2013, the interest rate on three month Treasury bills rises to 2.4 percent then rises again to approximately 3.8 percent in FY 2014 before stabilizing at this rate through FY 2016. The interest rate on ten year Treasury notes is expected to fall from 3.5 percent in FY 2010 to 2.9 percent in FY 2011 but rise substantially to 4.4 percent in FY 2012. The interest rate on ten year Treasury notes is anticipated to peak at 5.2 percent in FY 2013 and then steadily decline to 4.5 percent in FY 2016.

Consistent with the perspective discussed here, the consensus economic forecast reflects the early stages of recovery from the nation's economic crisis in employment, income, and other coincidental economic indicators in the next six years. In particular, employment growth is expected to be positive in FY 2011 through FY 2016 for the first time since FY 2007. More rigorous employment growth is expected in FY 2014 before the rate of growth declines to more sustainable levels in FY 2015 and beyond. Personal income growth is expected to reach its peak in FY 2013 and follow a similar pattern to employment growth over the remaining forecast period.

The Consensus economic forecast for the fiscal years 2011 through 2016 agreed upon by the conferees at the November 2010 Revenue Estimating Conference is shown in the following table.

The November 2010 Consensus Economic Forecast

Rates of Growth	**FY 2011**	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**	**FY 2016**
Total Employment	0.1	1.7	3.2	3.3	2.5	1.7
Personal Income	2.0	3.2	5.0	4.4	3.9	3.7
Wage and Salary Income	1.6	2.4	5.4	5.3	4.2	3.4
Dividends, Interest and Rent	0.1	3.2	6.8	7.2	6.3	5.5
Nominal Rates						
U.S. CPI-U	1.2	2.0	2.8	2.7	2.3	2.2
Unemployment Rate	11.8	11.3	9.2	7.4	6.4	5.9
Ten Year Treasury Notes	2.9	4.4	5.2	4.8	4.5	4.5
Three Month Treasury Bills	0.3	0.7	2.4	3.8	3.9	3.7

General Revenues

Introduction

The Governor's recommended budget is based on estimated general revenues of $3.040 billion in FY 2011 and $3.246 billion in FY 2012. Annual estimated growth during FY 2011 and FY 2012 is 0.8 percent and 6.8 percent, respectively. Estimated deposits of $79.5 million and $91.3 million will be made to the Budget Reserve and Cash Stabilization Fund during these fiscal years. The contributions to the Budget Reserve and Cash Stabilization Fund are funded by limiting annual appropriations to 97.4 percent of estimated revenues in FY 2011 and 97.2 percent of estimated revenues in FY 2012. The revenue estimates contained in the Governor's FY 2011 supplemental and FY 2012 recommended budgets are predicated upon the revenue estimates adopted at the November 2010 Consensus Revenue Estimating Conference (REC) and the Governor's recommended changes to the adopted general revenues.

The Consensus Revenue Estimating Conference is required by statute to convene at least twice annually to forecast general revenues for the current year and the budget year, based upon current law and collection trends, and the consensus economic forecast. The Conference members are the State Budget Officer, the House Fiscal Advisor, and the Senate Fiscal Advisor. Typically, the two required meetings of the Consensus Revenue Estimating Conference occur in November and May of each fiscal year.

FY 2011 Revised Revenues

The principals of the November 2010 Revenue Estimating Conference adopted revenue estimates that were $17.5 million greater than the enacted FY 2011 revenue estimates, an increase of 0.7 percent. As shown in the *General Revenue Changes to Adopted Estimates* table in Appendix A of this document, the Governor's revised FY 2011 Budget recommends an increase of $2.4 million in revenues. This $2.4 million in recommended changes to the FY 2011 adopted estimates breaks down as follows:

- An increase of $97,880 is attributable to the revenue generated by the agreement with the Council of State and Territorial Epidemiologists (CSTE) to develop and participate in an influenza hospitalization surveillance project.
- An increase of $2.3 million is attributable to the transferring of excess bond proceeds from the State Police headquarters project to general revenues.

FY 2011 Revised Revenues vs. FY 2010 Final Revenues

Recommended revenues for FY 2011 are based upon a $22.7 million increase in total general revenues over final FY 2010, or growth of 0.8 percent. Much of this increase can be found in personal income taxes, motor vehicle operator's licenses and registration fees, the lottery transfer, insurance companies gross premiums taxes, sales and use taxes, and public utilities gross earnings taxes. These increases are partially offset by estimated decreases in business corporations taxes, cigarette taxes, and financial institutions taxes.

Personal income tax collections continue to be the single largest source of state general revenues at 30.8 percent for FY 2011. Personal income tax collections are estimated to expand at an annual rate of 4.3 percent or $38.4 million for FY 2011. Much of this increase is due to increased estimated income tax payments of $22.6 million, followed by an increase in withholding payments of $19.9 million. The overall increase, however, is slightly offset by an estimated increase of $4.2 million in refund payments. Final income tax payments are expected to remain flat vis-à-vis final FY 2010 collections.

General business tax collections are projected to drop by $21.8 million or -5.7 percent, due primarily to an estimated decrease in business corporations taxes of $23.5 million and in financial institutions taxes of

$2.1 million. The estimated decline in business corporations taxes is due to the testimony of the Division of Taxation at the November 2010 Revenue Estimating Conference which revealed the occurrence of large, one time payments that will not be repeated in FY 2011. These revenue decreases are partially offset by anticipated increases in insurance companies gross premiums taxes of $2.3 million and public utilities gross earnings taxes of $1.2 million.

Sales and use tax collections are projected to increase by $2.1 million or 0.3 percent, over final FY 2010 collections. Sales and use taxes represent 26.5 percent of total general revenues in FY 2011. For FY 2011 sales and use tax collections are projected to be $805.5 million.

Excise taxes other than the sales and use tax are expected to increase by $1.1 million or 0.5 percent in FY 2011 over final FY 2010 collections due primarily to a projected increase in motor vehicle operator’s licenses and registration fees of $3.5 million. The Department of Revenue, Division of Motor Vehicles has implemented a new collection method beginning in late FY 2010 and as such has seen more timely deposits of receipts. Cigarette tax payments are projected to decrease by $3.3 million in FY 2011 versus final FY 2010 collections. Alcohol excise taxes and motor carrier fuel use tax collections are estimated to increase by $730,523 and $131,130 respectively in FY 2011.

Other taxes are projected to decrease by $1.6 million, or 4.2 percent in FY 2011 relative to final FY 2010 receipts. Of the total decrease in other taxes, inheritance and gift taxes are expected to decrease by $756,952, realty transfer taxes are anticipated to decline by $593,915, and racing and athletics tax collections are projected to decline by $242,221. The expected decrease in inheritance and gift tax collections is due to the fact that the General Assembly increased the estate tax exemption amount from $675,000 to $850,000 effective January 1, 2010. Typically estate taxes are not due until nine months after a decedent’s death. Racing and athletic taxes’ downward trend is expected to accelerate as Twin River has eliminated live greyhound racing on the premises and now solely relies on simulcast racing for pari-mutuel wagering. Racing and athletics taxes are expected to total $1.25 million in FY 2011 a decrease of 16.2 percent from final FY 2010 collections. Realty transfer taxes are expected to total $6.4 million in FY 2011, a decrease of 8.5 percent from final FY 2010 collections.

In the Governor’s FY 2011 Budget, departmental receipts are projected at $334.8 million, an increase of $1.7 million from final FY 2010 collections, or 0.5 percent. It should be noted that the increase in the departmental receipts incorporates the Governor’s proposed revenue enhancement of $97,880 from the CSTE Influenza Hospitalization Surveillance Project.

In addition to the above general revenue components, an increase is expected in FY 2011 for the lottery transfer to the general fund of $2.8 million, or 0.8 percent from final FY 2010. The increased lottery transfer in FY 2011 is due to the results of the November 2010 REC which increased the estimated transfer amount from the video lottery terminals installed at Twin River and Newport Grand by $4.4 million and decreased instant tickets and on-line games by $1.6 million. The gas tax transfer to the general fund no longer occurs and the unclaimed property transfer to the general fund is forecasted to decline by $567,150 in FY 2011 or 9.7 percent. The decrease in the unclaimed property transfer is attributable to the testimony provided by the Office of the General Treasurer at the November 2010 REC.

For FY 2011, other miscellaneous general revenues are projected to increase by $656,768. The increase in other miscellaneous general revenues incorporates the Governor’s proposal to transfer the excess bond proceeds of $2.3 million from the State Police headquarters project to general revenues.

General Revenues

FY 2012 Proposed Revenues

The Governor's recommended FY 2012 Budget estimates general revenues of $3.246 billion, an increase of 6.8 percent from the revised FY 2011 level. The Governor's recommendation is comprised of $2.938 billion of revenue estimated at the November 2010 Revenue Estimating Conference and $307.8 million of changes to the adopted estimates. These changes are shown in the schedule *General Revenue Changes to Adopted Estimates* located in Appendix A of this document.

The largest source of FY 2012 general revenues is the personal income tax, with estimated receipts of $950.0 million, $2.2 million more than the November 2010 REC adopted estimate for FY 2012 or growth of 1.4 percent from the revised FY 2011 amount. This revenue increase is the net result of the Governor's proposal to eliminate an existing tax credit, institute a new top 100 delinquent taxpayers list, and offset lottery winnings for taxes owed to the State Tax Administrator. The Governor proposes the elimination of the Rhode Island Motion Picture Production Company Tax Credit effective July 1, 2011 which is estimated to increase personal income tax collections by $1.3 million in FY 2012. The Governor further proposes for the Department of Revenue's Division of Taxation to publish two top 100 delinquent taxpayer lists; one for individual and one for business taxes. Currently the Division of Taxation publishes a single list of the top 100 tax delinquents that includes both individual and business taxpayers. By publishing a list of 100 individual delinquent taxpayers the number of delinquent taxpayers contacted will increase thereby increasing the amount of collections from delinquent taxpayers. The proposal is estimated to increase personal income tax receipts in FY 2012 by $779,965. Finally, the Governor proposes to require that lottery winnings in excess of $600.00 be offset against debts owed to the State Tax Administrator. The payment of taxes owed from lottery winnings in excess of $600.00 would be the third priority after child support debts and benefit overpayments by the Department of Labor and Training. This proposal is estimated to increase personal income tax collections by $141,457.

General Business taxes are projected to represent 11.5 percent of total general revenue collections in the FY 2012 Budget. Business corporations tax revenues are expected to yield $130.4 million, a decrease of $635,462 from the FY 2012 estimate adopted at the November 2010 REC. This decrease is the result of the Governor's Business Tax Competitiveness Proposal (BTCP). This proposal reduces the corporate income tax rate from 9.0 percent to 7.5 percent over a three year period beginning on January 1, 2012. In addition, the BTCP restructures the corporate minimum and minimum franchise taxes from a flat rate to graduated rates based on Rhode Island gross receipts. These proposals are expected to reduce business corporations tax collections by $8.5 million, and $6.1 million respectively in FY 2012. These revenue reductions are offset by the implementation of combined reporting and the phasing out of the Jobs Development Act over a three year period beginning in 2012, increasing revenues by $8.9 million and $4.8 million respectively. The total Business Tax Competitiveness Proposal reduces business corporation taxes by $905,533 in FY 2012. These revenue reductions are offset by increased business corporations tax collections that result from the repeal of the Motion Picture Production Company Tax Credit effective July 1, 2011, an increase of $139,656, and the publishing of a top 100 delinquent business taxpayers list through the Department of Revenue's, Division of Taxation, an estimated increase of $130,415. The estimated growth rate in business corporations taxes over the FY 2011 revised level is 5.7 percent.

Insurance companies gross premiums taxes are projected to reach $100.9 million in FY 2012. This amount is equal to the revenue estimate for insurance companies gross premiums taxes adopted at the November 2010 Revenue Estimating Conference plus an increase in revenue of $204,966 from the repeal of the Motion Picture Production Company Tax Credit effective July 1, 2011. The recommended growth rate in FY 2012 insurance companies gross premiums taxes over the FY 2011 revised estimate is 2.8 percent.

General Revenues

FY 2012 recommended revenues for the public utilities gross earnings tax, the financial institutions tax, and the bank deposits tax are at the same levels as were adopted at the November 2010 REC. The respective FY 2012 recommended growth rates for these taxes relative to the FY 2011 revised estimates are 2.1 percent, 100.0 percent, and 2.6 percent respectively.

The health care provider assessment on nursing homes is forecasted to yield $41.4 million, a decrease of $428,112 from the estimate that was adopted at the November 2010 REC. This decrease can be attributed to the estimated decline in revenues of $704,000 from the Governor's proposal for nursing home provider rate reform. The decrease is partially offset by increased health care provider assessment tax receipts of $275,888 due to the establishment of a top 100 delinquent business taxpayers list by the Division of Taxation.

Sales and use tax collections are expected to yield $989.5 million in FY 2012, $165.5 million more than was adopted at the November 2010 Revenue Estimating Conference for FY 2012. The Governor's Sales Tax Modernization Proposal includes a reduction in the sales tax rate from 7.0 percent to 6.0 percent which will reduce sales tax collections by $117.7 million; the modernization of the sales tax base to cover some services and items currently exempt from the sales tax, both of which will be taxed at 6.0 percent and are projected to increase sales tax collections by $195.9 million; the taxation of the retail sale of medical marijuana at 6.0 percent, which is estimated to increase sales tax collections by $802,659; the expansion of the sales tax base by taxing certain currently exempt items at a 1.0 percent rate, which is anticipated to increase sales tax collections by $86.8 million; and the disallowance of the use of insurance proceeds from a totaled or stolen motor vehicle as the trade-in allowance for a passenger car which is forecasted to increase sales tax collections by $882,659. As a result of the sales tax base expansion, the state will lose revenues of $1.8 million from becoming non-compliant with the Streamlined Sales and Use Tax agreement. The Governor's proposal to publish a top 100 delinquent business taxpayer list is expected to increase sales and use tax collections by $602,399. Sales and use taxes are anticipated to contribute 30.5 percent to total general revenues in FY 2012.

Motor vehicle operator license and vehicle registration fees are forecasted to equal $42.1 million in FY 2012, a decrease of $9.8 million from what was adopted at the November 2010 REC. This decrease is due to the phase-in of the transfer of the first 20.0 percent of motor vehicle license, registration and title fees to the Intermodal Surface Transportation Fund (ISTF) for use by the Department of Transportation (DOT). Motor carrier fuel use taxes are estimated to reach $1.1 million in FY 2012 and cigarettes tax revenues are expected to total $131.8 million. Each of these recommended revenue amounts are the same as the estimates adopted at the November 2010 Revenue Estimating Conference. Alcohol tax revenues are projected to increase by $200,000 or 1.7 percent in FY 2012 from the revised FY 2011 estimate.

Inheritance and gift taxes are projected to equal $28.9 million, the same amount adopted at the November 2010 REC. Realty transfer taxes are estimated at the same level adopted at the November 2010 Revenue Estimating Conference with anticipated collections of $6.5 million, an increase of $100,000 from the revised FY 2011 estimate. Racing and athletics taxes are also estimated at the level adopted at the November 2010 REC. The adopted estimate of $1.1 million for FY 2012 represents a decline of $150,000, or -12.0 percent, from the revised FY 2011 estimate. Other taxes are expected to comprise 1.1 percent of total general revenues in FY 2012.

FY 2012 departmental receipts are expected to generate $9.8 million more than the revised FY 2011 estimate. Inclusive of the Governor's proposed changes to departmental receipts, total departmental revenues are expected to be $344.6 million in FY 2012, or 10.6 percent of total general revenues. In the licenses and fees category, $146.3 million more is expected due primarily to the Governor's proposal to reinstate the Hospital Licensing fee for one year using the rate of assessment of 5.465 percent and the current base of FY 2009 net patient revenues. The FY 2012 recommended departmental revenues figure includes the following proposals:

- An increase of $141.8 million from reinstituting the hospital licensing fee;
- An increase of $3.0 million from mandating insurance companies to obtain official Division of Motor Vehicles driving record abstracts at least every three years for insurance ratings;
- An increase of $18,720 from implementing a charge for checks returned to the Division of Motor Vehicles due to non-sufficient funds;
- An increase of $1.9 million from increasing the daily and annual pass fees for residents and non-residents on both weekdays and weekends to park at state beaches;
- An increase of $1.2 million from increasing the license fee for securities sales representatives to $75 annually;
- An increase of $41,000 from increasing the license fee for a federally covered advisor to $300 annually;
- An increase of $108,915 from increasing the estate tax filing fee to $50;
- An increase of $122,925 from increasing the letter of good standing fee to $50;
- An increase of $556,092 by levying a surcharge of 4.0 percent on the net revenues of compassion centers;
- An increase of $40,000 from increasing the assessment for fire code violations to $125;
- An increase of $110,000 from instituting a fee of $10 for the Department of Children, Youth, and Families' conducting of applicant background clearances;
- An increase of $786,248 from increasing the Veteran's Home board and support fee to 100.0 percent of resident countable income;
- An increase of $153,576 in probation and parole monies owed from the offset of personal income tax refunds by the Division of Taxation;
- An increase of $74,160 from the indirect cost recovery assessment on the Telecommunication Education Access Fund's restructured fees;
- A decrease of $74,902 from the phase-in of the transfer of the first 20.0 percent of commercial driver's license fees to the ISTF for use by the DOT;
- A decrease of $166,489 from the phase-in of the transfer of the first 20.0 percent of operator control registration reinstatement fees to the ISTF for use by the DOT;
- A decrease of $677,486 from the phase-in of the transfer of the first 20.0 percent of drivers license reinstatement and assessment fees to the ISTF for use by the DOT;
- A decrease of $1.3 million from the phase-in of the transfer of the first 20.0 percent of motor vehicle title fees to the ISTF for use by the DOT;
- A decrease of $371,320 from the dissolution of the Health Services Council within the Department of Health;

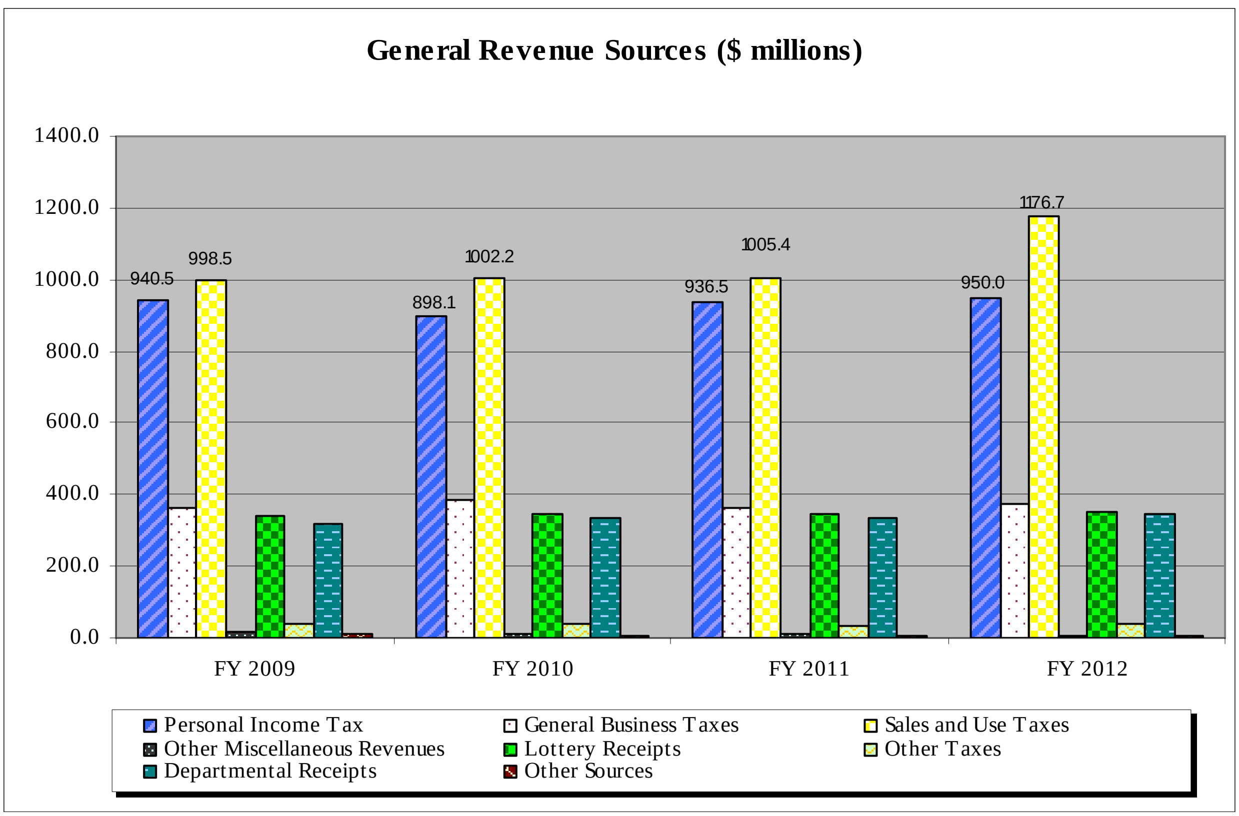
The FY 2012 recommended revenues for the other sources component totals $364.0 million, a decrease of $1.9 million, or 0.5 percent, compared to the revised revenue estimate for FY 2011. The largest component of this decline is the decrease in other miscellaneous revenues of $5.8 million. Other miscellaneous revenues are anticipated to generate $7.3 million in FY 2012 an increase of $3.5 million from the level adopted at the November 2010 Revenue Estimating Conference. This increase can be attributed to the Governor's proposal to transfer $3.5 million in excess reserves from the Rhode Island Resource Recovery Corporation.

Within the gas tax transfer component, the Governor's FY 2012 Budget shows no change from the FY 2011 revised estimate. Effective July 1, 2009, the state's general fund no longer receives any of the revenues generated by the state's $0.32 per gallon gas tax.

Within the lottery category, the recommended FY 2012 budget is $4.0 million greater than the revised FY 2011 Budget, an increase of 1.2 percent. The Governor recommends no changes from the November 2010 REC estimate for the lottery transfer. In FY 2012, the lottery transfer is expected to be $351.5 million and comprise 10.8 percent of total general revenues.

The final category of general revenue receipts is the unclaimed property transfer. In FY 2012, this transfer is expected to decrease by $100,000, or 1.9 percent, from the revised FY 2011 estimate. The unclaimed property transfer is projected to be $5.2 million in FY 2012, and comprises 0.2 percent of all general revenues.

The chart below shows the sources of general revenues for the period FY 2009 – FY 2012. The values of the two major sources of general revenues, personal income taxes and sales and use taxes, are highlighted.



Restricted Receipts and Other Sources of Revenue

Introduction

The Governor's recommended budget proposes changes to revenue sources other than general revenues for FY 2011 and FY 2012. The revenue estimates in the Governor's FY 2011 supplemental budget contains no additional money allocated to restricted receipts. The FY 2012 recommended budget contains an additional $29.7 million in restricted receipts.

FY 2011 Revised Non-General Revenues

For FY 2011, the Governor's Budget proposes no additional money to be allocated as restricted receipts. The FY 2011 supplemental budget proposes restricted receipt amounts as originally enacted.

FY 2012 Recommended Non-General Revenues

The Governor's FY 2012 Budget proposes enhancing the Intermodal Surface Transportation Fund (ISTF) by phasing in the transfer of various Division of Motor Vehicle general revenue fees over a five year period. The Governor proposes the following transfer schedule: 20.0 percent of the total fees in FY 2012, 40.0 percent of the total fees in FY 2013, 60.0 percent of the total fees in FY 2014, 80.0 percent of the total fees in FY 2015 and 100.0 percent of the total fees in FY 2016. The deposit of these transfers into the ISTF will support the Department of Transportation and reduce its need to borrow money to provide for the required state match when leveraging federal highway funds. The net result to the Governor's FY 2012 Budget is an increase in other sources of revenue by $12.0 million in FY 2012. The various fees consist of $9.8 million in motor vehicle registration and driver license fees, $74,902 in commercial driver license fees, $166,489 in registration reinstatement fees, $677,486 driver license reinstatement fees, and $1.3 million in motor vehicle title fees.

In FY 2012, the Governor recommends maintaining the meals and beverage tax at the 8.0 percent rate. The meals and beverage tax is currently comprised of the sales tax rate of 7.0 percent and the local 1.0 percent tax on meals and beverages. The difference between the current 7.0 percent rate and the 6.0 percent sales tax rate included in the Governor's Sales Tax Modernization Proposal will be deposited into the newly created Municipal Accountability, Stability and Transparency (MAST) Fund. The MAST Fund is a restricted receipt account that is dedicated to improving the financial integrity of the cities and towns. It is estimated that $19.3 million will be deposited into the MAST Fund in FY 2012.

The Governor also recommends maintaining the tax on the rental of rooms and lodging at the 8.0 percent rate. The tax on the rental of rooms and lodging is currently comprised of the sales tax rate of 7.0 percent and the local 1.0 percent hotel tax. The difference between the current 7.0 percent sales tax rate and the 6.0 percent sales tax rate included in the Governor's Sales Tax Modernization Proposal will be deposited into the newly created Tourism Asset Protection (TAP) Fund. The TAP Fund is a restricted receipt account that is dedicated to the construction and improvement of state owned tourism assets. It is estimated that $2.6 million will be deposited into the TAP Fund in FY 2012.

The Governor's recommended FY 2012 Budget proposes to expand the Department of Human Services' Children's Health Account Enhancements which currently bills the first $6,000 of expenses to insurance companies that provide coverage to children with special health care needs and have some form of comprehensive third party liability. The Governor's recommendation is to increase the billing limit from $6,000 per child to $7,500 per child. The increase in the billing limit to $7,500 is estimated to generate $4.2 million in FY 2012. These monies will be used to offset the cost of other Medicaid services.

Restricted Receipts and Other Sources of Revenue

The 2010 General Assembly enacted legislation which changed the funding formula for the William M. Davies School. Prior to FY 2012, the William M. Davies School was funded strictly from state aid. In the Governor's recommended FY 2012 Budget the William M. Davies School will be jointly funded by the state and local education agencies. As a result of this proposal, local education agencies will be required to pay the educational costs of local students that attend the William M. Davies School. The Budget Office estimates that this proposal will increase non-general revenues by $685,495. For the FY 2012 Budget the Governor also proposes to require local education agencies to pay the education costs of local children residing at the Department of Children, Youth, and Families' Training School. The Budget Office estimates that this proposal will increase non-general revenues by $2.1 million.

The Governor recommends a reduction in the Telecommunication Education Access fee on land line phones from the current monthly surcharge of $0.26 to $0.15 and the application of this reduced fee to wireless phones. These two fee changes are estimated to reduce Telecommunication Education Access receipts from land line phones by $591,480 and increase Telecommunication Education Access receipts from wireless phones by $1.3 million in FY 2012. The net result is an increase in revenue of $667,440 to the Telecommunication Education Access Fund which supports internet access for schools and libraries.

The Governor also recommends in the FY 2012 Budget the dissolution of the Department of Health's Health Services Council. The resulting dissolution will decrease restricted receipt revenue by $125,000 in FY 2012. Finally, the Governor recommends in FY 2012 increasing the Board and Support fees for residents of the state Veterans' Home from 80.0 percent of a patient's monthly countable income to 100.0 percent of the same dedicating the $196,562 increase in revenue to a restricted receipt account to support the Veterans' Home's operations.

Unemployment Insurance

A Proposal to Restore Trust Fund Solvency

HISTORY

In 1998, The RI General Assembly, at the request of business, enacted a significant change in the computation of the taxable wage base for the Unemployment Insurance (UI) program. Prior to the change which took effect in 1999, the UI taxable wage base was set at 70%of the average annual wage in UI covered employment. In 1998 that amounted to a taxable wage base of $18,200. Starting in 1999, the new law set the UI taxable wage base based on the level of reserves in the Employment Security Fund ranging from a low of $12,000 if reserves exceeded $225 million to a high of $19,000 if reserves fell to $75 million or less on the prior September 30th. Under the new formula, the UI taxable wage base fell to $14,000 in 1999 and then to $12,000 for CY 2000 through 2003. In 2011, our UI taxable wage base is set at the highest level, $19,000. Under the pre-1999 law, the UI taxable wage base would have been $28,800 in 2011.

The problem with this change was that the UI taxable wage base and UI taxes were no longer tied to the rise in employee wages while the benefits paid to unemployed workers remain tied to their wages. So, over time, wages and benefit costs grew with inflation while tax receipts failed to keep up. The reserve targets, which determined the taxable wage base, were set in fixed dollar amounts and the taxable wage base values as a percentage of total wages eroded each year.

In November 2008, the Employment Security Fund had a reserve of $230.1 million. RI's relatively low unemployment rate at the time allowed reserves to continue to grow over the next two years and they peaked at $301.3 million in August 2001. Over the first ten years (1999-2008) after the change in the taxable wage base calculation took effect, it is estimated that employers saw a reduction of over $600 million in the amount of UI taxes that they paid compared to what they would have paid under the pre-1999 UI taxable wage base formula.

At the end of February 2011, the RI had borrowed $229.4 million from the federal government to maintain payments to its unemployed workers. Our total borrowing from the federal government for UI benefits is expected to peak at $291.0 million this spring. While the severity of the current recession has played a major role in the rapid depletion of Employment Security fund reserves, it is clear that if the changes made to the UI taxable wage base calculation in 1998 had not occurred, RI's Trust fund would have weathered the recession and would not have had to borrow from the federal government to maintain UI benefit payments.

EMPLOYMENT SECURITY ADVISORY COUNCIL

The Employment Security Advisory Council (ESAC) convened in October 2009 to begin addressing the problems facing the Unemployment Insurance program and the insolvency of the Employment Security Trust Fund. They reviewed various adjustments that could be made to the UI tax and benefit provisions to bring the financing of the UI program into balance and to help repay the RI's outstanding federal loans for its UI program.

The set of recommendations outlined in this budget article were forwarded to the Governor's office in the spring of 2010 without a formal endorsement of the council. The council felt that it did not have sufficient time to thoroughly understand the complexities of the UI system, but thought that the proposals should go forward for consideration by the legislature. Unfortunately, the proposals were received too late in the legislative process to be considered in the 2010 General Assembly session. The proposals in this article reflect the same basic recommendations as those forwarded in the spring of 2010, but have been modified to phase in some of the UI benefit adjustments over several years.

The table below provides an estimate of the effect of the proposed revenue and benefit adjustments from CY 2012 through CY 2017.

RI DEPARTMENT OF LABOR AND TRAINING

Proposal to Restore Unemployment Insurance Trust Fund Solvency

Summary of Revenue Increases and Benefit Savings by Year

Revenue Items	**Projected Increase in Revenue (in millions)**					
	2012	**2013**	**2014**	**2015**	**2016**	**2017**
1 Taxable Wage Base Change Set equal to 47% of average annual wage in CY 2012 and raise to 50% of average annual wage by 2015.	$4.0	$4.0	$5.9	$7.8	$11.5	$14.2
2 Set the Taxable Wage Base $3,000 higher for the employers at the highest tax rate.	$3.1	$3.1	$3.1	$3.1	$3.1	$3.1
Total Projected Revenue Increase by Year	$7.1	$7.1	$9.0	$10.9	$14.6	$17.3

Benefit Adjustments	**Projected Benefit Savings (in millions)**					
	2012	**2013**	**2014**	**2015**	**2016**	**2017**
1 Freeze the Maximum Weekly Benefit Amount (MWBA) at its July 2011 figure and compute annually thereafter at 57.5% of the State Average Weekly Wage (SAWW).	$1.3	$3.8	$6.0	$8.6	$11.4	$13.0
2 Lower the Wage Replacement percentage from 60% to 50% of the individuals Average Weekly Wage over the next three years.	$2.6	$9.9	$17.9	$24.9	$25.6	$26.3
3 Use the Average of the Two Highest Quarter Wages instead of the Highest Quarter Wages to Compute the claimant's Weekly Benefit Amount.	$2.2	$4.1	$3.9	$4.1	$4.2	$4.3
4 Reduce the Maximum Potential Total Benefits from 36% of the Base Period Wages to 33% of the Base Period Wages.	$0.0	$2.3	$2.2	$2.2	$2.3	$2.4
5 Delay UI Benefit Eligibility by the number of weeks of Severance pay the claimant receives (up to a maximum of 26 weeks).	$1.1	$2.1	$2.0	$2.0	$2.1	$2.1
6 Reduce the Maximum Dependents' Allowance from 5% of the claimant's Weekly Benefit Amount (WBA) to 3% of the WBA over the next two years.	$1.1	$1.9	$2.6	$2.7	$2.7	$2.8
7 Require indivdiuals disqualified from collecting UI for a Voluntary Quit, Misconduct Discharge or a Refusal of Suitable Work to work 8 weeks & earn wages equal to their Weekly Benefit Amount (WBA) in each week to overcome the disqualification.	Unable to determine potential benefit reduction. It is dependent on number of disqualifications each year that are overcome with wages below the WBA.					
Total Estimated Benefit Savings by Year	$8.3	$24.0	$34.6	$44.5	$48.3	$50.9
Sum of Revenue & Benefit Adjustments	$15.4	$31.1	$43.6	$55.4	$62.9	$68.2

Unemployment Insurance

The table below is a projection of RI's Employment Security fund, the level UI taxes and benefits expected to be paid through CY 2020 under our current laws. Absent any action to make changes, it is expected that the Employment Security Fund would remain insolvent until CY 2017. And our ability to grow reserves in ensuing years would be very limited.

RI DEPARTMENT OF LABOR AND TRAINING
Projected UI Fund Taxes, Benefits & Federal Loans if No Action Taken
(revised 2-10-11)

	Taxable Wage Base	Regular State UI Taxes (In millions)	Balance of 0.3% Interest Assess. (In millions)	Federal Interest Charge (In millions)	FUTA* Credit Reduction	Additional FUTA* Taxes (In millions)	Regular State UI Benefits (In millions)	RI Dec. 31 Federal UI Loan Balance (In millions)	Dec. 31 ES Fund Balance (In millions)
2009	$18,000	$184.7	$0.0	$0.0	na	$0.0	$387.3	$127.5	($127.5)
2010	$19,000	$210.0	$0.0	$0.0	na	$0.0	$289.3	$225.5	($194.3)
2011	$19,000	$216.0	$6.5	$9.0	0.3%	$0.0	$249.5	$291.0	($251.0)
2012	$19,000	$219.6	$5.6	$12.4	0.6%	$9.0	$215.7	$265.9	($265.9)
2013	$19,000	$220.7	$7.1	$10.9	0.9%	$18.0	$206.5	$226.6	($226.6)
2014	$19,000	$221.9	$8.7	$9.3	1.2%	$27.0	$197.1	$166.0	($166.0)
2015	$19,000	$223.3	$11.2	$6.8	1.5%	$36.0	$202.5	$98.0	($98.0)
2016	$19,000	$224.7	$14.0	$4.0	1.8%	$45.0	$208.1	$22.4	($22.4)
2017	$19,000	$226.5	$0.0	$0.0	0.0%	$54.0	$213.8	$0.0	$44.3
2018	$19,000	$228.0	$0.0	$0.0	0.0%	$0.0	$219.7	$0.0	$52.6
2019	$19,000	$229.7	$0.0	$0.0	0.0%	$0.0	$224.3	$0.0	$58.0
2020	$19,000	$231.4	$0.0	$0.0	0.0%	$0.0	$229.5	$0.0	$59.9
Totals 2009-2020		**$2,636.6**	**$53.2**	**$52.3**		**$189.0**	**$2,843.3**		

If the changes proposed in this article are implemented, it is projected that RI would be able to fully repay its federal UI loans in 2015 through a combination of $211.6 million in additional federal and state UI taxes and savings of $111.4 million in benefit adjustments. In addition, these changes would allow the RI Employment Security fund to rebuild reserves in preparation for the next recession.

RI DEPARTMENT OF LABOR AND TRAINING
Projected UI Fund Taxes, Benefits & Federal Loans Under Proposed Changes
(revised 2-11-11)

	Taxable Wage Base	Regular State UI Taxes (In millions)	Balance of 0.3% Interest Assessment (In millions)	Federal Interest Charge (In millions)	FUTA* Credit Reduction	Additional FUTA* Taxes (In millions)	Regular State UI Benefits (In millions)	RI Dec. 31 Federal UI Loan Balance (In millions)	Dec. 31 ES Fund Balance (In millions)
2009	$18,000	$184.7	$0.0	$0.0	na	$0.0	$387.3	$127.5	($127.5)
2010	$19,000	$210.0	$0.0	$0.0	na	$0.0	$289.3	$225.5	($194.3)
2011	$19,000	$216.0	$6.5	$9.0	0.3%	$0.0	$249.5	$291.0	($251.0)
2012	$19,800	$226.7	$5.6	$12.4	0.6%	$9.0	$207.5	$250.7	($250.7)
2013	$20,200	$227.8	$7.8	$10.2	0.9%	$18.0	$182.5	$179.6	($179.6)
2014	$20,600	$230.9	$10.7	$7.3	1.2%	$27.0	$162.4	$73.4	($73.4)
2015	$21,400	$234.2	$15.0	$3.0	0.0%	$36.0	$158.0	$0.0	$53.8
2016	$22,000	$239.3	$0.0	$0.0	0.0%	$0.0	$159.8	$0.0	$133.3
2017	$22,600	$243.8	$0.0	$0.0	0.0%	$0.0	$162.9	$0.0	$214.2
2018	$23,400	$245.5	$0.0	$0.0	0.0%	$0.0	$167.4	$0.0	$292.2
2019	$24,000	$247.4	$0.0	$0.0	0.0%	$0.0	$170.9	$0.0	$368.8
2020	$24,600	$249.4	$0.0	$0.0	0.0%	$0.0	$174.9	$0.0	$443.3
Totals 2009-2020		**$2,755.8**	**$45.5**	**$42.0**		**$90.0**	**$2,472.4**		

Transportation Funding

Recognizing the importance of investing in our aging transportation infrastructure, the Governor is recommending that transportation needs to be addressed through a multi-year plan that dedicates increasing amounts of transportation-related revenues to fund the operating and capital costs of the Department of Transportation.

Primary funding for Rhode Island transportation and highway construction spending is provided through the Federal Highway Administration (FHWA), under the authority of the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU). This Act, passed in August 2005, authorizes funds for highway construction, highway safety programs, mass transit operations, and other surface transportation projects for the five-year period 2005 - 2009. Under this program, Rhode Island has received an average of $207.2 million per year through FY 2009. SAFTETEA-LU expired in 2009, but was extended through by Congress for one year in 2010 with Rhode Island receiving $220.9 million in funding. In 2011 financing for the federal highway program has relied on short term continuing resolutions to provide funding. No new program has been introduced to replace the SAFETEA-LU program. The State has chosen over the years to seek approval from the voters through biennial referenda which authorize the issuance of general obligation bonds. This process has resulted in growing debt service expenditures, which consume a growing share of the Department's stagnant gas tax allocation.

This over-reliance on debt to fund transportation improvements has long been recognized as a problem by independent reviewers. In 1996, Governor Almond's Blue Ribbon Panel to Address Transportation Infrastructure Capital Funding identified the debt service problem stating, "the debt service on transportation bonds is a large and increasing burden on the state budget which reduces the amount of gas tax funds available for other purposes." Upon predicting that the debt service burden would peak at $57 million per year with $30 million per year issuance, the 1996 Blue Ribbon Panel recommended that "Rhode Island needs to reduce its reliance on general obligation bonds for transportation funding."

Transportation 2020, the State's long range transportation guide plan, in 2002, highlighted the problem of the increasing debt service eroding the funding available for transportation operations and maintenance. The Rhode Island Public Expenditure Council (RIPEC) cited the Transportation 2020 analysis in recommending that transportation system funding should be reformed with one objective of the reformation to be "diminishing reliance on general obligation bonds for future capital project financing". With the goal of dedicating transportation revenues for transportation purposes, RIPEC further recommended that motor vehicle registrations and driver's license fees be transferred to a transportation fund over a five year period at 20% per year

Governor Donald Carcieri's Blue Ribbon Panel on Transportation Funding, which examined the transportation financing structure in 2008, echoed the findings of the prior studies in its condemnation of routine bonding to fund transportation improvements. The Panel's report states:

> "Continued borrowing and sole reliance on the gas tax is not the solution. The practice of issuing general obligation bonds every two years to match federal funds is unsustainable. This has resulted in very high annual debt service which has severely limited the amount of state gas tax available for maintenance. Gas tax revenue has decreased significantly over time, as has its purchasing power."

While the fundamental problem with the current transportation funding structure has been long identified, no change has been forthcoming.

Governor Chafee proposes to resolve the structural funding dilemma facing the Department of Transportation by dedicating current revenues to transportation purposes to enable the Department to fund

Transportation Funding

Rhode Island's required match on a pay-as–you-go basis. The program, to be implemented over a five year period, would reduce debt service costs over time, such that Rhode Island would be positioned similar to other state's with pay-as-you-go capital programs. The chart below shows the funding progress over the five year period.

Revenue Item	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
Motor Vehicle Registration and License Fees	49,000,000	49,736,415	50,689,262	51,660,432	52,650,279
Commercial Drivers License Fees*	374,508	378,253	382,036	385,856	389,715
Operator Control Registration Reinstatement Fee*	832,445	840,769	849,177	857,669	866,246
Drivers License Reinstatement & Assessment Fees*	3,387,430	3,421,304	3,455,517	3,490,073	3,524,973
Motor Vehicle Title Fees*	6,516,097	6,581,258	6,647,071	6,713,541	6,780,677
Total Available Revenue	**$ 60,110,480**	**$ 60,958,000**	**$ 62,023,063**	**$ 63,107,571**	**$ 64,211,889**
Phase-in of Transfer to DOT at 20.0 Percent per Year	$ 12,022,096	$ 24,383,200	$ 37,213,838	$ 50,486,057	$ 64,211,889
Net General Revenues	**$ 48,088,384**	**$ 36,574,800**	**$ 24,809,225**	**$ 12,621,514**	**$ -**

* FY 2012 figure was adopted at the November 2010 REC. Growth is assumed at 1.0 percent rate.

Notes: The value of Motor Vehicle Registration and License Fees does *not* include revenues received from the imposition of the rental vehicle surcharge.

The Governor's proposed plan will provide approximately $64.2 million by FY 2016, which will enable Rhode Island to eliminate the use of general obligation bonds to provide the state match for federal funds. When the State eliminates the reliance on annual bond issues, debt service will decline, freeing up gas tax revenues for other purposes. The revenues to be transferred to the Intermodal Surface Transportation Fund are not new revenues, but are transferred form the General Fund, and therefore result in decreased resources available for other state expenditures.

Referenda Year	Referenda Recommended	Fiscal Year	Bonds to Be Issued Per Year	Pay Go Match	Total Bonds and Paygo Cash for State Match
November 2010	$ 80,000,000	FY 2011	$ 40,000,000	$ -	$ 40,000,000
		FY 2012	40,000,000	0	40,000,000
November 2012	$ 61,000,000	FY 2013	39,000,000	1,000,000	40,000,000
		FY 2014	22,000,000	18,000,000	40,000,000
November 2014	$ 16,000,000	FY 2015	16,000,000	24,000,000	40,000,000
		FY 2016	0	40,000,000	40,000,000

Additionally, the Governor recommends that the Department of Transportation seek federal approval for tolling of certain roads in Rhode Island, which will provide additional new revenues to address unmet infrastructure needs. This program is expected to take several years to implement and therefore is not expected to impact the capital program until the end of the five year planning horizon. The proceeds from tolls would be utilized to help address the backlog of transportation infrastructure needs.

Municipal Accountability, Stability, and Transparency Fund

Governor Recommends $19.3 Million Incentives to Municipalities for Prudent Fiscal Practices

Local governments are facing ever-increasing costs for retirement and retiree health care. These two components represent significant cost drivers for municipal budgets. Given this, Governor Chafee is proposing to create the Municipal Accountability, Stability and Transparency (MAST) Fund. The MAST Fund is designed to encourage local governments to focus on the sustainability of current plans and reduce the unfunded liability of significantly underfunded pension plans. In addition, the MAST Fund addresses the significant unfunded liabilities for Post Employment Benefits Other Than Pensions (OPEB).

Furthermore, Governor Chafee's proposal includes an incentive to employ fiscally prudent budgeting practices for cities and towns by requiring, for example, cities and towns to provide for a Five-Year Budget Forecast and a fiscal impact statement for changes in health care benefits, pension benefits and OPEB. This information would be submitted to the Division of Municipal Finance.

To partially offset the additional funding requirements for local pension plans and OPEB as set forth under MAST, and to provide an incentive for fiscally prudent budgeting practices, Governor Chafee proposes to finance the newly created MAST Fund by maintaining the state and local meals and beverage tax rate at 8.0 percent. The state and local meals and beverage tax rate consists of the state sales tax rate of 7.0 percent and the 1.0 percent local meals and beverage tax rate. The Governor's Sales Tax Modernization Proposal lowers the state sales tax rate to 6.0 percent. By maintaining the state and local meals and beverage tax rate at 8.0 percent the Governor is able to designate the 1.0 percent that previously went to the state to finance the newly created MAST Fund. It is projected that this fund would total $19.3 million, which would be available for municipal governments. Distribution of the MAST Fund receipts to each community is based on the 2009 General Revenue Sharing percent distribution.

In FY 2012, and thereafter, cities and towns will be eligible for MAST Fund aid if they comply with certain fiscally prudent management practices, and meet the minimum requirements towards adequately funding pensions and Post Employment Benefits Other Than Pensions (OPEB). Commencing in FY 2014 cities and towns will be expected to comply with the statutory requirements, or face a loss in state aid as a result of the reduction of the state's share in the teacher retirement contributions.

Requirement #1 Prudent Fiscal Practices in FY 2012

The MAST Fund is designed in a three-tiered approach, increasing municipal accountability every year. **Starting in FY 2012**, all cities and towns will receive additional state aid if they comply with the following fiscally prudent practices:

- Provide Five-Year Forecast to the Division of Municipal Finance for major funds as defined by generally accepted accounting principles as established by the Governmental Accounting Standards Board (GASB). The forecast has to include two scenarios: One scenario would show a baseline forecast, the other forecast would include pensions and Post Employment Benefits Other Than Pensions (OPEB) funded at 100 percent of the Annually Required Contribution (ARC), separately for the general and unrestricted school funds. The forecast also has to show underlying actuarial assumptions.
- Provide fiscal impact statements to the Division of Municipal Finance for changes in health care benefits, pension benefits and OPEB, reflecting the impact on the unfunded liability and ARC, as well as the impact on the Five-Year Forecast. Fiscal impact statements have to show underlying actuarial assumptions and support for underlying assumptions.
- Provide financial data, such as quarterly reports, adopted budget surveys and the Comprehensive Annual Financial Report (CAFR) on time.

- Join electronic reporting/implement Municipal Uniform Chart of Accounts (UCOA), within six months of implementation.

Requirement #2 Funding Progress for Municipal Pensions in FY 2013 and OPEB Liabilities in FY 2014

Starting in FY 2013, all cities and towns will receive MAST Fund state aid if they comply with the fiscally prudent practices, as spelled out above, and the following requirements to increase funding of pensions:
(A) Cities and towns will be given a maximum of 5 years to achieve 100 percent of their Annually Required Contribution (ARC) or their Annual Pension Cost (APC), whichever is higher, for municipal pension plans. Municipalities shall be required to make their ARC in accordance with generally accepted accounting principles promulgated by the Governmental Accounting Standards Board (GASB). In the first year, the municipality's actual contribution would increase by the difference between the prior year's ARC or APC, whichever is greater and its actual contribution divided by five. For years two through five, the annual actual contribution would increase by the difference between the ARC or APC of the most recent valuation of the immediately preceding year and the actual contribution made by the municipality in the prior year divided by the remaining years. (B) Beginning in FY 2013, cities and towns that have not previously met the goal of 100 percent funding of ARC or APC, whichever is greater, cannot decrease the dollar amount of contribution compared to the preceding year. (C) Starting in FY 2013, cities and towns that have any municipal pension plan that has a funded ratio below 50 percent, as determined in the latest valuation, will be required to make an additional contribution equal to 10 percent over and above the actual contribution made in the prior fiscal year, not including the additional funding as defined in (A). This additional contribution would continue until the municipality's funding ratio is 50 percent or higher.

Starting in FY 2014, all cities and towns will receive MAST Fund state aid if they comply with the fiscally prudent practices and the pension requirements, as spelled out above. In addition, municipalities will be required to increase/start funding for Post Employment Benefits Other Than Pensions (OPEB). Commencing in FY 2014, in any fiscal year in which a municipality does not annually fund its OPEB ARC at 100 percent, as determined in the latest valuation, a municipality would be required over each of the next successive ten years to increase its actual contribution to its ARC. In the first year, the municipality's actual contribution would increase by the difference between the prior year's ARC and its actual contribution divided by ten. For years two through ten, the annual contribution would increase by the difference between the ARC of the most recent valuation of the immediately preceding year and the actual contribution made by the municipality in the prior year divided by the remaining years. In addition, all cities and towns will be required to join a multiple employer trust once this trust is established. Cities and towns that have already established a trust as of June 30, 2010 will not be required to join a multiple employer trust for OPEB, if the city/town adheres to minimum standards established by the state.

Penalties for Non-Compliance Begin in FY 2014- Lost Teacher Retirement Aid

The Division of Municipal Finance will monitor the progress of the cities and towns to fund its ARC. As part of its monitoring, and to determine if a city/town is eligible to receive additional aid under the MAST Fund, the Division of Municipal Finance will use the municipality's audited financial statements and applicable actuarial valuations to make determinations of compliance.

Starting in FY 2014, all cities and towns will continue to be eligible for the MAST funding allocation if they comply with the fiscally prudent practices, and the requirements to increase funding for pensions and OPEB. However, there will be a penalty for non-compliance. Those cities and towns not complying with fiscally prudent practices and the requirements relating to pension and OPEB will experience a decrease of 5 percentage points each year in the state's share of contribution towards the employer cost of the teacher retirement fund, starting in FY 2014.

Retirement System Funding

The Governor recommends that the State take action in FY 2012 to increase funding to the State Employee, Teacher, State Police and Judicial Retirement Systems in order to bolster the assets in those funds. None of the State's pension funds are fully funded, and in fact each of these funds has seen an increase in their unfunded liability over the last year. The sustainability of public pensions needs to be addressed, and once determined, the funding of the appropriate amounts to amortize the unfunded liability must be made a priority. The table below shows the actuarial unfunded liability and projected contributions based upon the 2009 valuation prepared by the actuary.

State Retirement Systems' Unfunded Actuarial Liabilities, Contributions, and Member Counts

	Unfunded Actuarial Liability	Funded Ratio	2009 Actuarial Contribution	Active Members	Retired Members	Inactive Members	Total Membership
State Employees' System	1,836,163,271	59.0%	126,344,715	11,023	11,142	2,496	24,661
Teachers' System	2,892,031,771	58.1%	188,858,198	13,689	9,749	2,466	25,904
State Police System	15,247,960	79.8%	3,340,746	176	4	2	182
Judicial System	4,898,819	88.3%	1,700,174	45	10	-	55
	4,748,341,821		**320,243,833**	**24,933**	**20,905**	**4,964**	**50,802**

** Source: FY2009 Actuarial Valuations prepared by Gabriel, Roeder, Smith & Company*

The Governor proposes that members contribute 11.75% of pay reflecting an increase of 3.0 percent of pay for state employee members and 2.25 percent of pay for teacher members during FY 2012, while the State investigates the need to develop a new sustainable system that provides for a formula driven sharing of the actuarial required contributions. Under current law, the employee contribution is set in statute, so if the required contribution increases as a rate of pay, currently the State's taxpayers pick up the difference. The proposed increase in contributions will not be offset by a reduction in employer contributions, but rather will result in increased cash flowing into the trust funds. The table below provides a historical perspective on the required payroll rates, and the sharing of those required contributions.

	State Employees					Teachers					
Fiscal Year	**Total ARC Contribution Rate**	**Employer**	**Employee**	**Employer Share as a Percent of Total ARC**	**Employee Share as a Percent of Total ARC**	**Total ARC Contribution Rate**	**Employer - State Share**	**Employer - Local Share**	**Employee**	**Employer Share as a Percent of Total ARC**	**Employee Share as a Percent of Total ARC**
1995	19.07%	11.32%	7.75%	59.4%	40.6%	24.52%	6.76%	9.26%	8.50%	65.3%	34.7%
1996	18.20%	9.45%	8.75%	51.9%	48.1%	24.21%	6.22%	8.49%	9.50%	60.8%	39.2%
1997	18.80%	10.05%	8.75%	53.5%	46.5%	24.07%	6.17%	8.40%	9.50%	60.5%	39.5%
1998	19.58%	10.83%	8.75%	55.3%	44.7%	23.75%	6.00%	8.25%	9.50%	60.0%	40.0%
1999	18.60%	9.85%	8.75%	53.0%	47.0%	21.02%	4.90%	6.62%	9.50%	54.8%	45.2%
2000	17.32%	8.57%	8.75%	49.5%	50.5%	24.14%	6.21%	8.43%	9.50%	60.6%	39.4%
2001	16.74%	7.99%	8.75%	47.7%	52.3%	21.51%	5.15%	6.86%	9.50%	55.8%	44.2%
2002	14.34%	5.59%	8.75%	39.0%	61.0%	19.45%	4.22%	5.73%	9.50%	51.2%	48.8%
2003	16.43%	7.68%	8.75%	46.7%	53.3%	21.47%	5.04%	6.93%	9.50%	55.8%	44.2%
2004	18.35%	9.60%	8.75%	52.3%	47.7%	23.22%	5.73%	7.99%	9.50%	59.1%	40.9%
2005	20.26%	11.51%	8.75%	56.8%	43.2%	24.34%	6.12%	8.72%	9.50%	61.0%	39.0%
2006	23.59%	14.84%	8.75%	62.9%	37.1%	25.97%	6.75%	9.72%	9.50%	63.4%	36.6%
2007	27.15%	18.40%	8.75%	67.8%	32.2%	29.14%	8.02%	11.62%	9.50%	67.4%	32.6%
2008	29.52%	20.77%	8.75%	70.4%	29.6%	31.51%	8.97%	13.04%	9.50%	69.9%	30.1%
2009	30.39%	21.64%	8.75%	71.2%	28.8%	29.57%	8.18%	11.89%	9.50%	67.9%	32.1%
2010	29.53%	20.78%	8.75%	70.4%	29.6%	28.51%	7.76%	11.25%	9.50%	66.7%	33.3%
2011	29.53%	20.78%	8.75%	70.4%	29.6%	28.51%	7.76%	11.25%	9.50%	66.7%	33.3%
2012	31.73%	22.98%	8.75%	72.4%	27.6%	31.82%	9.09%	13.23%	9.50%	70.1%	29.9%
Governor's Proposal											
ARC 2012	31.73%	22.98%	8.75%	72.4%	27.6%	31.82%	9.09%	13.23%	9.50%	70.1%	29.9%
Supplemental			3.00%						2.25%		
Total	**34.73%**	**22.98%**	**11.75%**	**66.2%**	**33.8%**	**34.07%**	**9.09%**	**13.23%**	**11.75%**	**65.5%**	**34.5%**

Retirement System Funding

As shown above, the employer share of the annual required contribution for State employees has increased from 59.4 percent to 72.4 percent from 1995 to 2012. The employer share of annual required contribution for Teachers, which is shared 60 percent local government/40 percent State government, has increased from 63.5 percent to 70.1 percent from 1995 to 2012.

	State Police					Judges				
Fiscal Year	**Total ARC Contribution Rate**	**Employer**	**Employee**	**Employer Share as a Percent of Total ARC**	**Employee Share as a Percent of Total ARC**	**Total ARC Contribution Rate**	**Employer**	**Employee**	**Employer Share as a Percent of Total ARC**	**Employee Share as a Percent of Total ARC**
1995	27.80%	20.05%	7.75%	72.1%	27.9%	14.85%	7.10%	7.75%	47.8%	52.2%
1996	29.62%	20.87%	8.75%	70.5%	29.5%	19.55%	10.80%	8.75%	55.2%	44.8%
1997	21.21%	12.46%	8.75%	58.7%	41.3%	32.40%	23.65%	8.75%	73.0%	27.0%
1998	21.41%	12.66%	8.75%	59.1%	40.9%	34.09%	25.34%	8.75%	74.3%	25.7%
1999	20.18%	11.43%	8.75%	56.6%	43.4%	32.11%	23.36%	8.75%	72.7%	27.3%
2000	35.37%	26.62%	8.75%	75.3%	24.7%	39.24%	30.49%	8.75%	77.7%	22.3%
2001	34.64%	25.89%	8.75%	74.7%	25.3%	39.84%	31.09%	8.75%	78.0%	22.0%
2002	36.42%	27.67%	8.75%	76.0%	24.0%	40.33%	31.58%	8.75%	78.3%	21.7%
2003	36.23%	27.48%	8.75%	75.8%	24.2%	42.17%	33.42%	8.75%	79.3%	20.7%
2004	35.52%	26.77%	8.75%	75.4%	24.6%	42.65%	33.90%	8.75%	79.5%	20.5%
2005	37.62%	28.87%	8.75%	76.7%	23.3%	44.94%	36.19%	8.75%	80.5%	19.5%
2006	40.10%	31.35%	8.75%	78.2%	21.8%	44.26%	35.51%	8.75%	80.2%	19.8%
2007	40.53%	31.78%	8.75%	78.4%	21.6%	44.82%	36.07%	8.75%	80.5%	19.5%
2008	39.75%	31.00%	8.75%	78.0%	22.0%	40.82%	32.07%	8.75%	78.6%	21.4%
2009	34.78%	26.03%	8.75%	74.8%	25.2%	32.81%	24.06%	8.75%	73.3%	26.7%
2010	34.78%	26.03%	8.75%	74.8%	25.2%	32.81%	24.06%	8.75%	73.33%	26.7%
2011	33.33%	24.58%	8.75%	73.7%	26.3%	24.94%	16.19%	8.75%	64.92%	35.1%
2012	34.14%	25.39%	8.75%	74.4%	25.6%	27.44%	18.69%	8.75%	68.11%	31.9%
Governor's Proposal										
ARC 2012	34.14%	25.39%	8.75%	74.4%	25.6%	27.44%	18.69%	8.75%	68.1%	31.9%
Supplemental			3.00%					3.00%		
Total	**37.14%**	**25.39%**	**11.75%**	**68.4%**	**31.6%**	**30.44%**	**18.69%**	**11.75%**	**61.4%**	**38.6%**

As shown above, the employer share of the annual required contribution for the State Police system has increased from 72.1 percent to 74.4 percent from 1995 to 2012. The employer share of annual required contribution for the Judges has increased from 47.8 percent to 68.1 percent from 1995 to 2012. Both these plans are relatively new plans, including only those employees hired after December 31, 1987 and December 31, 1989, respectively.

The proposed supplemental payment would be made by employees for all pay days after July, 2011. This payment would be in addition to the annual required contribution, and would enhance assets on a bi-weekly basis and would increase the cash flow of the Retirement Fund. As shown below, this supplemental payment will increase the assets of the systems by an estimated $40.7 million. This will have a direct impact on the unfunded liabilities of these systems and will increase their funding ratios.

Membership Group	FY2012 ARC Contribution	ARC Rate of Payroll	Estimated Payroll Base	Proposed Percentage Supplemental Contribution	Estimated Dollar Value of Supplemental Contribution
State Employees	$149,885,956	22.98%	$652,245,239	3.00%	$19,567,357
Judges	1,605,947	18.69%	8,592,547	3.00%	257,776
State Police	4,265,295	25.39%	16,799,114	3.00%	503,973
Teachers-State Share	82,671,070	9.09%	909,472,717	2.25%	20,463,136
Subtotal -State	**$238,428,268**		**$1,587,109,617**		**$40,792,243**
Teachers-Local Share	120,323,240	13.23%	n/a	n/a	n/a
Total- State and Local Membership	**$358,751,508**		**$1,587,109,617**		**$40,792,243**

Retirement System Funding

The Five Year Forecast reveals the significant growth which is projected in the contributions over the next five years. According to actuarial projections by Gabriel, Roeder, Smith and Company, the annual required employer contribution rate for state employees is expected to increase from 22.98 percent in FY 2012 to 35.88 percent in FY 2016. This reflects an increase in the rate of 12.9 percentage points over a five year period. Based upon projected payroll growth and the forecasted retirement contribution rates, the general revenue funded contribution for state employee members would grow from a projected $88.1 million in FY 2012 to $162.1 million in FY 2016, reflecting growth of $74.1 million in retirement costs for state employees. This pension funding growth of 84 percent from FY 2012 to FY 2016 reflects the largest growth item in terms of percentage growth for a major categorical item.

According to actuarial projections by Gabriel, Roeder, Smith and Company, the annual required employer contribution rate for teacher members is expected to increase from 22.32 percent in FY 2012 to 34.2 percent in FY 2016. This reflects an increase in the rate of 11.88 percentage points over a five year period. State contributions towards the Teacher Retirement System are projected to increase by $57.7 million, from $82.7 million in FY 2012 to $140.4 million in FY 2016.

Combined, the State's employer share contribution for state employees and teachers is projected to grow by $131.8 million from FY 2012 to FY 2016. In terms of dollar growth, this ranks second only to the $210 million growth in the whole category of grants and benefits (Medicaid) as largest dollar growth item in the budget over the planning horizon.

All Sources

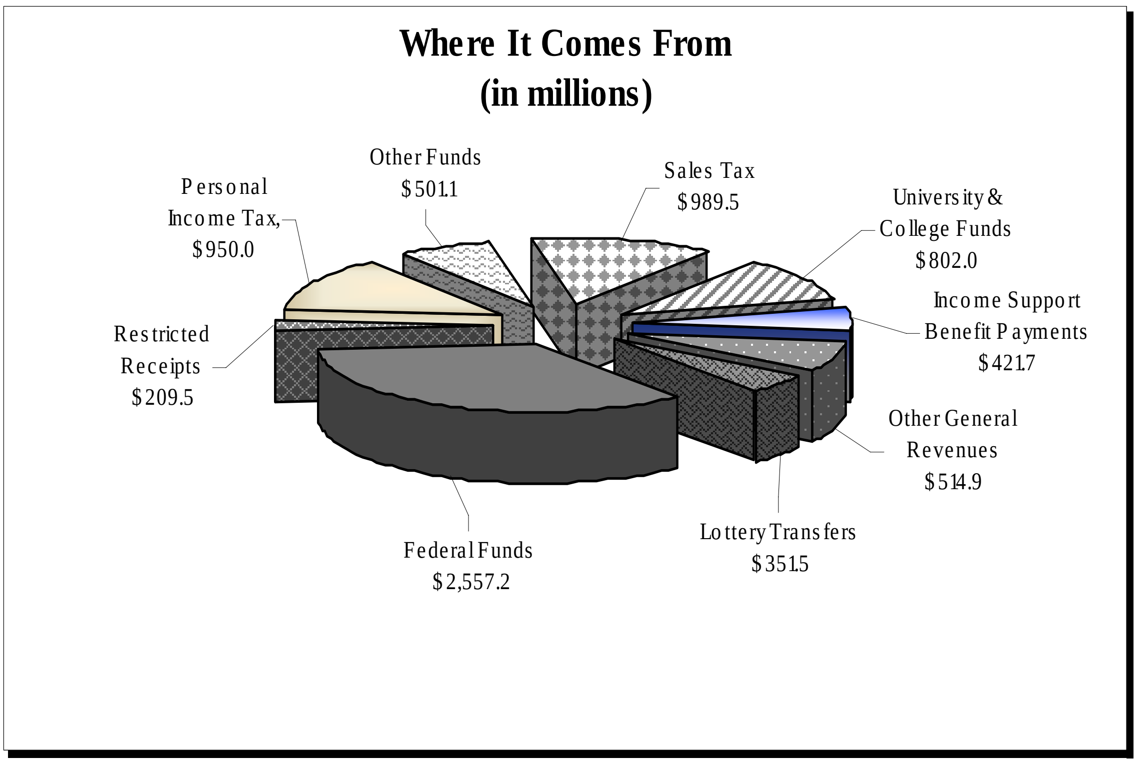
The total budget of $7,297.3 million includes all sources of funds from which state agencies make expenditures.

Federal funds represent 35.0 percent of all funds. Over 69.3 percent of federal funds are expended for human services, primarily for Medicaid.

Income and Sales Taxes combined represent 26.6 percent of all revenue sources.

University and College Funds, and Income Support Benefit payments represent 11.0 percent, and 5.8 percent of the total, respectively.

Remaining sources include: Other General Revenues, 7.1 percent; the Lottery Transfer, 4.8 percent; Restricted Receipts, 2.9 percent; and Other Funds 6.9 percent.



All Expenditures

The Governor's FY 2012 Budget recommendation is $7,661.3 million in all funds comprised of six functional units of state government: human services, education, general government, public safety, transportation, and natural resources.

Approximately 40.7 percent of all expenditures are for human services, comprised of agencies that engage in a broad spectrum of activities including income support, client subsidies, case management and residential support, and medical regulation, prevention, treatment, and rehabilitation services. The FY 2012 recommended budget for all human service agencies is $3,119.6 million.

Approximately 28.3 percent of all expenditures are for education, which includes the Department of Elementary and Secondary Education, Public Higher Education, the Rhode Island State Council on the Arts, the Rhode Island Atomic Energy Commission, the Rhode Island Higher Education Assistance Authority, the Historical Preservation and Heritage Commission, and the Rhode Island Public Telecommunications Authority. The FY 2012 recommended budget for education is $2,170.1 million.

Approximately 17.7 percent of all expenditures are for general government, which includes agencies that provide general administrative services to all other state agencies, and those that perform state licensure and regulatory functions. The FY 2012 recommended budget for all general government agencies is $1,357.2 million.

Approximately 6.2 percent of all expenditures are for public safety, which is the system that provides law enforcement, adjudicates justice, protects life and property, and handles emergencies impacting Rhode Island's citizens. The FY 2012 recommended budget for the public safety system is $475.4 million.

Approximately 5.7 percent of all expenditures are for transportation, which provides for the state's maintenance and construction of a quality transportation infrastructure. The FY 2012 recommended budget for transportation is $435.0 million.

Approximately 1.4 percent of all expenditures are for natural resources, which includes the Department of Environmental Management, the State Water Resources Board and the Coastal Resources Management Council. The FY 2012 recommended budget for natural resources is $104.0 million.