State of Rhode Island and Providence Plantations

Executive Summary

Fiscal Year 2014

Lincoln D. Chafee, Governor

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State of Rhode Island and Providence Plantations
State House, Room 224
Providence, Rhode Island 02903
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Lincoln D. Chafee
Governor

January 16, 2013

To the Honorable, the General Assembly:

The Fiscal Year 2014 budget I recommend to you today was crafted to increase Rhode Island's economic competitiveness and maximize employment in our state.

When Rhode Islanders are working, our other challenges become more manageable. The confidence to create jobs comes from a climate of certainty, stability, and predictability. This budget works to achieve this goal by adhering to a philosophy of fiscal discipline and responsibility. It also contains strategic investments in education, infrastructure, and workforce development and supports and strengthens our cities and towns.

The FY 2014 budget is submitted to you on January 16, 2013 – on time, and the earliest in over twenty years. This demonstrates my Administration's commitment to sending a clear message to taxpayers and businesses within our borders and beyond that we are serious about the fiscal discipline necessary to maintain a pro-economic development and pro-growth environment. For the second consecutive year, the state is projected to finish the fiscal year with a surplus. Additionally, in the FY 2013 revised budget, all state departments and agencies are at or below the initial enacted budget by the General Assembly (notwithstanding re-appropriations and expenditures relating to Hurricane Sandy). This is the result of strong management and a climate of accountability in state government, overseen by the able and dedicated members of my Cabinet.

The budget I submit to you contains no tax or fee increases of any kind, and it will substantially improve Rhode Island's economic climate by reducing the corporate tax rate from 9.0 percent to 7.0 percent over the next three years. This budget also continues to capitalize on Rhode Island's assets by investing in our tourism efforts and the ongoing work of the I-195 Redevelopment Commission.

Throughout my career in public service, I have been committed to quality public education. There is no more important investment we can make than in the potential of our students. That is why, in my first two years as Governor, we have invested over $88.0 million in public K-12 and higher education in Rhode Island. That commitment continues with this budget, which fully funds the K-12 funding formula with an additional $30.3 million in aid and includes an additional $6.0 million for higher education. My goal and expectation is that the leadership of our three state institutions of higher education will couple this funding with savings and efficiencies to ensure no tuition increase this year at the Community College of Rhode Island, Rhode Island College, or the University of Rhode Island. Rising tuitions prevent hardworking and qualified Rhode Island students from attaining a quality education and improving their future prospects – as well as our economy. We must keep tuition rates affordable and allow our students to attend and graduate from college without being burdened with crushing debt.

Because education and training does not end at the gates of our educational institutions, my proposed budget includes $3.0 million to create new workforce development initiatives. It also provides an enhanced child-care subsidy using Temporary Assistance for Needy Families (TANF) block grants coupled with a subsidized job training program to empower low-income Rhode Islanders to get back to work.

Investments to repair and upgrade Rhode Island's ailing infrastructure will produce benefits in both the long- and short-term, boosting our economic competitiveness while getting Rhode Island construction workers back on the job. I am pleased to note that my Administration has taken historic steps in reforming how we finance our transportation system here in Rhode Island. For the first time in recent memory, we are not borrowing to receive our state match for federal support to maintain our highways. This means that our valuable resources can be put toward important repair and improvement projects, rather than debt service. Building on these reforms, this budget includes a number of strategic infrastructure investments, including advancing $11.0 million in Rhode Island Capital Plan (RICAP) funds to get key projects underway as soon as possible. I also recommend modifying the Historic Structures Tax Credit program by providing access to abandoned tax credits in order to entice new construction in our distressed communities and urban centers.

Finally, as I have often said, our state as a whole cannot be successful without improving and maintaining the financial health of our cities and towns. In addition to the $30.3 million in new local education funding, this budget adds $20 million in additional aid to our cities and towns – with particular attention to distressed communities. This funding will help alleviate the pressure on municipal governments to raise property taxes on already heavily burdened taxpayers. I have also allocated $10 million in RICAP funds to support a local road and streetscape improvement program in FY 2014.

Over the past several years, we have come together to do good work on behalf of our citizens, operating Rhode Island government more responsibly and effectively and making needed investments in the future of our state. There remain many challenges ahead, but with those challenges come tremendous opportunities. I look forward to joining with you once again to seize those opportunities. The budget I respectfully submit to you today is an important step toward a stronger and more prosperous Rhode Island.

Sincerely,

Lincoln D. Chafee
Governor of the State of Rhode Island and Providence Plantations

FY 2014 Budget Documents

Governor Chafee's *FY 2014 Executive Summary* is the first of eight documents that contain the summaries of revenue and expenditures on a statewide, functional, and departmental basis and also presents statewide expenditure data by *category* or object of expenditure. This same data is presented in the *Budget* in more detail by program.

The *Executive Summary* contains special reports on Education Aid and State Aid to provide a historical perspective on these state expenditures and also contains a "Budget Primer" which is intended to assist the reader of the budget documents in understanding the budget process in Rhode Island. Specific recommendations for FY 2014 for the departments are presented in this document, as well as the five-year financial projection as provided by law. Further detail is provided in the *Technical Appendix*.

The Budget consists of four volumes that provide an overview of state expenditures, as well as an in-depth presentation of the State Budget by program. The financial data presented for state agencies in *The Budget* for the past two fiscal years (FY 2011 and FY 2012) is generally derived from the appropriation accounting and receipt accounting files of the State Controller, as of the time of year-end closing. In the case of the accounts under the jurisdiction of the Board of Governor's of Higher Education, these columns reflect independently audited records.

The financial data for state agencies for the current fiscal year is from the enacted budget, modified in some cases to reflect recommended supplemental appropriations or withdrawals, revised expenditure estimates by category of expenditure or program, and revised estimates of federal grant awards or restricted receipts. In this document, the general revenue balance forward is included at the account level. The proposed changes to the enacted FY 2013 budget are included in the financial data by program for FY 2013. Totals and subtotals often appear to be inaccurate by small amounts or may disagree by small amounts with other budget and financial documents; this is due to differences in rounding procedures. The annual Appropriations Act is the absolute reference for state appropriation amounts.

The Budget also contains both narrative descriptions of Rhode Island’s quasi-public agencies, authorities and entities, which are component units of state government for financial reporting purposes, and presents financial data provided by these entities. The Budget Office requests that quasi-public agencies and authorities submit information in the format used by the agency; no attempt is made to conform the financial presentation of the agencies data. In most cases, the FY 2013 and FY 2014 information has not been officially approved by the entities' governing bodies.

The *FY 2014 Budget* reports performance measurements for most programs, as required by legislative mandate to develop performance measurements for use in the budget process. Measurements are provided after each programs financing and personnel supplement pages. The *Budget* now contains information that was previously presented in the *Personnel Supplement.* The two documents have been merged. The *Budget* document provides information relating to personnel costs by program. It also reflects capital project summary narratives of all capital projects approved by the Governor as recommended by the Capital Development, Planning and Oversight Commission.

The *Capital Budget* contains information on the Governor's recommended capital improvement plan and contains individual project expenditures as well as contains the debt service component relating to capital improvements and any "pay-as-you-go" capital, which is financed from current revenues.

The *Budget as Enacted* will be prepared after final enactment by the 2013 General Assembly.

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Introduction

Rhode Island is steadily emerging from the recent recession, with unemployment heading in the right direction and a number of key indicators suggesting a strengthening economy.

While this is encouraging news for Rhode Island's economic outlook, we must not let the momentum slip away. We must demonstrate the necessary fiscal discipline at both the state and local levels so that we can ensure taxpayers get high value for their investment in government and adequately prepare for the challenges that lie ahead. Given the ongoing uncertainty at the federal level, Rhode Island must keep its fiscal house in order to remain agile enough to address any effects experienced by federal action or inaction.

Instilling Fiscal Discipline – Back to Basics

Through diligence and hard work, Rhode Island finished FY 2012 with a healthy surplus, nearly $21.3 million more than planned. We are projected to finish FY 2013 with another sizable surplus, totaling $79.3 million. This will represent the third year in a row that the state will have completed its fiscal year with a strong surplus.

My Cabinet members have managed their departments and agencies within their means, and this budget demonstrates their efforts through tight spending controls throughout state government. In fact, my FY 2013 revised budget, which is $28.2 million less than the enacted, reflects a spending plan where <u>each</u> individual agency and department will spend at or less than the enacted level – requiring no additional funding for agency operations. Although there are funds associated with re-appropriations from FY 2012 to support specific expenditures that did not occur on time, and there are additional expenditures totaling $4.1 million associated with unanticipated expenditures related specifically to Hurricane Sandy, the FY 2013 revised budget that I present to the General Assembly does not require any additional support for agencies to operate and meet their obligations.

We must act expeditiously to address the challenges facing our great state. In that spirit, I have submitted the FY 2014 budget on January 16, 2013. I am pleased to note that this submission is not only on time, but earlier than any budget submitted in the past twenty years. I appreciate all of the hard work the state departments and agencies and my budget office put into this effort to adhere to this aggressive timeline. The early submission will provide the General Assembly additional time to thoughtfully and deliberatively review my proposed budget and the initiatives contained within, and I look forward to working with the state's legislative leadership throughout this important process to move Rhode Island forward.

The budget that I submit today on behalf of the Rhode Island taxpayers <u>does not increase</u> any taxes, fees, or charges to support the FY 2014 spending plan. In fact, my proposed budget includes additional tax reform that builds on our recent success on the personal income tax. I am proposing to reduce the state's corporate tax from 9.0 to 7.0 percent over the next three years. This will improve our economic competitiveness, help our existing businesses grow, and encourage others to invest in our wonderful state.

The following recommended budget outlines my FY 2013 revised budget and my FY 2014 proposed budget in greater detail. While we have been able to take advantage of stronger financial management and good fortune to end the FY 2012 and FY 2013 budgets with strong surpluses, I still faced some very difficult decisions to deliver a balanced budget for the General Assembly's consideration. For example, the FY 2014 budget does not include planned cost of living increases for hospitals and nursing homes, and limits the increases permitted to managed care providers.

In addition, the FY 2014 budget proposes to close one special care facility operated by the Department of Behavioral Healthcare, Developmental Disabilities and Hospitals by moving current residents to other long-term care locations. Other initiatives within this department will focus on employment as a first option in rehabilitation services and expansion of options available to individuals that will move them away from psychiatric inpatient stays, emergency room visits and substance abuse detoxification readmissions. Although these proposals will be beneficial in the long term for clients of these programs, there will be a reduction in funds to community providers that service these populations.

While I certainly would have liked to avoid such actions, they were less onerous than some of the other choices that I had before me as my team worked to close the $128 million projected deficit for FY 2014.

Introduction

I set out clear directions to state departments and agencies to identify savings in operations, personnel, and other initiatives that would prevent drastic changes in programs and services, especially those that could impact our most vulnerable citizens. This budget avoids eliminating programs that were once considered as options given the enormity of the deficits we have faced in the past. This budget does not eliminate dental services to low-income adults, does not include additional reductions to mental health and developmental disability support services, and does not eliminate the General Public Assistance Program (GPA). Through the hard work of the Office of Health and Human Services, as well as other departments and agencies that are experiencing reductions in their appropriations, we have been able to stave off such drastic reductions in services. I have asked my departments and agencies to continue their efforts to constrain operating costs to ensure we continue to operate within our means.

These efforts are reflected in the updated five-year forecast, which shows improvement over the forecast from one year ago. Although expenditures are projected to exceed revenues in each of the out-years projected through FY 2018, the gap has narrowed in each year by an average of $80.0 million compared to the FY 2014 – FY 2017 forecast. The operating deficits by fiscal year are projected at $170.5 million in FY 2015, $254.5 million in FY 2016, $377.8 million in FY 2017, and $468.9 million in FY 2018. In percentage terms, the deficits are projected to range from 4.8 percent of spending in FY 2015 to 11.8 percent of spending in FY 2018. The expenditure-side of the budget is estimated to increase at an average annual rate 4.0 percent from the FY 2014 base to FY 2018. Inflation, however, as measured by the United States consumer price index for all urban consumers (CPI-U), is expected to grow at an average annual rate of 2.4 percent over this same period.

The five-year projection for out year revenues is impacted by the expected opening of gaming facilities in Massachusetts in the coming years. Lottery transfers to the State general fund are projected to diminish by a total of $307.6 million over the five year forecast period, due to the increased competition to Rhode Island’s gaming facilities in Lincoln and Newport. Without this impact on Rhode Island’s revenues, the five year forecast would show deficits of $170.5 million in FY 2015, $200.8 million in FY 2016, $264.4 million in FY 2017 and $328.4 million in FY 2018. In FY 2018, the deficit would be 8.3 percent of expenditures, as opposed to the 11.8 percent under the current forecast, or a total of $140.6 million less.

Improving Rhode Island’s Economic Climate

As we work to ensure that the state budget represents a disciplined approach to managing taxpayer resources, it is essential that we direct these resources to what I believe to be our most essential goals – improving Rhode Island’s economic climate and maximizing employment. Strategic investments to get Rhode Islanders back to work and support businesses that are already here will be key to our success.

We have seen from numerous national studies and rankings that Rhode Island is perceived – rightly or wrongly – as noncompetitive. However, we have made a number of significant improvements to our tax climate, our costs of doing business, and our ability to offer a skilled and trained workforce. These rankings fail to reflect the historic reforms we made to our personal income tax system, and do not reflect the aggressive efforts that are underway to improve our regulatory environment. Nor do these rankings really capture our outstanding workforce or our extensive higher education offerings.

But we need to continue to push forward to make our business tax climate more attractive and strengthen our efforts to attract and retain investments here in the Ocean State. This is why my budget contains absolutely no increases in any tax, fee, or charges of any kind. My goal was to combat our projected deficit on the expenditure side of the ledger so we can keep our taxes competitive.

I have also proposed a reduction in the state’s corporate tax from 9.0 percent to 7.0 percent over three years. I have front-loaded the decrease in the tax rate so we can move toward a more competitive corporate tax rate faster, with a 1.0 percentage point reduction in the rate in tax year 2014. Once fully implemented, Rhode Island’s corporate tax rate of 7.0 percent will be lower than both of our neighbors and will no longer be viewed as an impediment to attracting and growing businesses here.

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Investing in our economic climate and improving our competitiveness does not end with tax policy. I have invested an additional $600,000 in the state's tourism marketing efforts, bringing the level to $1.0 million annually. Tourism has been and must remain a key sector of our economy. I have also invested an additional $500,000 in the I-195 Redevelopment Commission to enhance its operations and move ahead with its important work. The former I-195 land represents a unique and rare opportunity to strategically capitalize on the extensive medical and educational assets in our capital city, the benefits of which will resonate throughout Rhode Island.

We were fortunate to have the Rhode Island Public Expenditure Council analyze how we can best improve the state's economic development efforts. One recommendation in particular that I intend to build upon is to develop and cultivate ongoing economic analyses for the state so decision makers have sound information as they work to develop appropriate economic policy. With this in mind, I have invested $150,000 in my proposed budget, and will continue this investment in FY 2015 to support the development of this initiative in concert with the Association of Independent Colleges and Universities, bringing together all 11 Rhode Island private and public higher education institutions' expertise and resources to help move Rhode Island's economy forward.

My Administration has already begun to thoroughly evaluate the impact that state regulations have on small businesses, and I intend to reform those regulations that unnecessarily impede growth. I have directed the Office of Management and Budget to focus on the efforts underway by the Office of Regulatory Reform, and I expect this comprehensive evaluation to be completed by March 31, 2014. While it is only a first step, my FY 2014 budget removes a fee charged to businesses that potentially expose employees to toxic or hazardous substances in the course of their work. These businesses are required to post a list detailing the substances to which employees are being exposed and the rights of the employees regarding hazardous substances on the business' premises. In addition, the businesses are required to pay a fee to the State. The requirement to keep employees informed will not change, but I am recommending that this unnecessary and burdensome fee be eliminated.

Investing in our Education Institutions and Workforce

My commitment to investing in education and our workforce goes hand in hand with our efforts to make Rhode Island more competitive and attractive for economic growth. My first priority was to fully fund the state's school aid formula, including all the categorical aid programs, and my FY 2014 Budget includes $30.3 million in additional education aid to our cities and towns to make sure this is done.

I have also allocated $17.2 million in pay-as-you-go Rhode Island Capital Plan Fund (RICAP) financing over the next six years to invest in repairs at the state's vocational education facilities. We have already invested a considerable amount of taxpayer funding for these schools, and I believe it necessary to protect these facilities to extend their useful life so that future Rhode Island students continue to benefit from their use..

In addition, I remain extremely concerned about the cost of higher education. Rhode Island families have enough burdens and challenges to struggle with – increasing tuition should not be one of them. Therefore, I have included $6.0 million in new general revenue funding for the three institutions of public higher education to ensure there is no tuition increase next year. This will still require our university and colleges to identify savings in their operating budgets to accomplish this goal, but I am confident that the leadership of these institutions will rise to the task and make sure that the opportunity to get a quality education here in Rhode Island remains affordable.

My capital plan includes over $52.5 million in pay-as-you-go funding for various projects to support our higher education institutions in FY 2013 and FY 2014. These infrastructure improvements at all three institutions reflect my ongoing commitment to offering safe and modern learning environments that will continue to attract and retain top students and faculty.

Our investment in our workforce should not stop at the gates of our public learning institutions. Rhode Islanders looking for work or to advance in their careers need appropriate opportunities to learn and grow so that they can be more marketable not only in today's economy, but the economy of tomorrow. Therefore, I have invested an additional $3.0 million in workforce development support, of which I have proposed to spend $1.0 million immediately in FY 2013 and the balance in FY 2014 to develop a Statewide Work Immersion Program. This program will provide meaningful work experiences to students and unemployed adults, as well as assisting businesses in training individuals for employment.

While these investments are important, we can do more. Therefore, I have proposed to allocate TANF Block grant funds to initiate a short-term enhanced child-care subsidy program that is coupled with subsidized job training and work for low income Rhode Islanders currently receiving income support. This will help 400 families and put people back in the workforce without using any general revenue funding. A similar program run by the state a number of years ago resulted in over 50.0 percent of those in subsidized employment retaining the job after the State’s subsidy expired.

Shoring up our Infrastructure

Another key component to getting our economy going and putting Rhode Islanders back to work as soon as possible is investment in our infrastructure. RICAP, our pay-as-you-go capital funding program, offers a number of opportunities to get limited resources on the ground to help get people working. I have included in my FY 2013 revised budget a proposal to advance over $11.0 million in already approved capital projects from future years of our five-year plan to the current year because departments and agencies have demonstrated that these projects are “shovel ready,” meaning if the funding were available, these projects could begin immediately. This is an exciting opportunity to get the trades back to work and improve the condition of our ailing infrastructure.

I firmly believe that targeted investment in our urban centers to improve the condition and usefulness of historic buildings is essential to preserving our heritage while attracting investment in our urban settings. Therefore, my FY 2014 budget includes an initiative to provide access to abandoned historic structures tax credits so we can entice investors into bringing properties in distressed communities back to life and on local tax roles.

We recently took historic steps in reforming how we finance our transportation system here in the Ocean State. The Department of Transportation is now off the habit of borrowing – and paying interest – to receive our state match for federal support to maintain and improve our highways. Working with the General Assembly, we were able to develop a funding strategy to support our match using RICAP financing and fees from the Registry of Motor Vehicles. This past November marked the first time im memory voters did not have to approve a bond referendum to support transportation costs. This is truly remarkable, because over time, the funding we have been allocating to support debt service rather than direct support for our highways and bridges will begin to shift to direct transportation support. This represents a fundamental improvement in how we finance our transportation system.

Similarly, this year we embarked on a program to shift transportation debt service costs from the gas tax to the state’s general fund. We have shifted $8.0 million in FY 2013, which has freed up gas tax proceeds to support transportation projects rather than debt service. I have continued this strategy in the FY 2014 Budget, shifting $10 million in debt service from the gas tax to the general fund. This ensures that we are maximizing our limited transportation resources to improve our roads and bridges. My five-year forecast shows that we intend to increase this shift to the general fund each year until we free the gas tax of debt service and dedicate those funds to transportation improvements.

While most think of roads and bridges when discussing Rhode Island’s infrastructure, in my view it also includes very valuable assets to our economy that preserve our environment. The Department of Environmental Management has been working to acquire Rocky Point, and I have included $2.5 million in pay-as-you-go capital funding to remediate and clean up this land and make sure it is accessible to all Rhode Islanders as quickly as possible. In addition, my budget invests over $3.2 million in pay-as-you-go capital funding to repair piers and docks at the Port of Galilee, which will be matched with $2.9 million in federal funds. Lastly, I have set aside $3.0 million in capital funding for Hurricane Sandy-related capital expenditures we deem necessary to fully recover, repair and protect our infrastructure. We expect federal match for much of these storm-related expenditures.

Introduction

Strengthening our Cities and Towns

While we are certainly making strides in getting Rhode Island's fiscal house in order and maintaining the economic recovery, it is incumbent on all of us to ensure that we continue to adequately support our cities and towns. Rhode Island's 39 municipalities are on the front line of meeting many of our needs, and state investment is critical to their success. Therefore, my budget includes a series of initiatives to assist our cities and towns and to ensure they are successful in delivering quality services to our citizens.

As mentioned earlier, my budget fully funds the local school funding formula with an additional $30.3 million in state support. While this is a critical investment in the education of our young people, it also helps reduce pressure on the local property tax in our communities.

To further support our cities and towns, I have included an additional $20.0 million in local aid in my budget, increasing the distressed community relief fund in both FY 2013 and FY 2014 by $5.0 million each year, and establishing a new $10.0 million state aid program in FY 2014 distributed based on population. It is critical to target these funds towards cities and towns facing the greatest challenges given the current economy, and these funds can help address their financial constraints immediately. In order for communities to access the additional $10.0 million in funds, I am recommending that they must have a locally approved pension improvement plan by November 2013.

This requirement is consistent with the recommendations of the local pension commission and the recent pension reform law enacted in November 2011. It is imperative that our municipalities improve the health of local independent pension plans; these plans need to be sustainable to ensure the benefits are there when needed and to remain affordable to the taxpayers. It would be short-sighted for the state to address its pension plans without outlining a path to a healthier financial position for our locally administered plans.

Another strategic investment in our cities and towns is an additional $10.0 million in pay-as-you-go capital funding through our RICAP program to help communities improve their roads and streetscapes. The state received a $10.0 million premium from bond sales that must be deposited into the RICAP fund. This one-time resource is a perfect opportunity to make a targeted investment in our local roads. These funds will be made available to our cities and towns through a formula based on local road miles to help repave, refurbish, or improve our local streets and streetscapes. Communities have had to limit their investments in roadways given the most recent economic downturn, and this investment will help jumpstart many of the necessary improvements we know are needed.

Establishing the Health Exchange

The FY 2013 Revised Budget and the FY 2014 Budget includes the federal funding for the Health Benefits Exchange, which will serve as a resource for Rhode Islanders and Rhode Island businesses to learn about and easily compare the quality and affordability of their health insurance options, enroll in coverage and, if eligible, access subsidies for coverage. The Exchange is a way for small employers and their employees and individuals to have an advocate and negotiator, and a quality monitor to represent them in their interactions with health insurers and health care providers.

Overview

Overview of the FY 2014 Proposed Budget

The Governor’s FY 2014 Proposed Budget was designed to address a projected $128.0 million operating deficit. Departments and agencies were asked to develop options within their budgets to address a 7.0 percent reduction in their current services budget for FY 2014. “Current services” is defined as what resources it would take to perform the same level of services and program assuming no change in public policy. Although the projected deficit for FY 2014 was somewhat lower than deficits faced in recent fiscal years, previous reductions to and/or program eliminations left fewer options available to balance the FY 2014 budget.

The Governor’s FY 2014 recommended budget was developed to begin addressing the state’s ongoing structural deficit, but also to provide additional assistance to the state’s troubled municipalities, which have experienced large reductions in financial assistance from the state in recent years. Governor Chafee’s FY 2014 Proposed Budget does indeed improve the out-year forecast, and provides resources to our struggling cities and towns. This has been done without asking more of our already burdened taxpayers.

An essential component to reducing the long-term structural deficits was the recent pension reforms to the State’s various pension programs. While very difficult choices were made, the reforms result in providing a sustainable pension program at a price taxpayers’ can afford. The savings derived from the reforms also ensured that the State’s general revenue budget could maintain desired levels of services, programs and staffing necessary to deliver quality services to Rhode Islanders.

The Governor, working closely with the General Assembly and the General Treasurer, enacted historic, comprehensive pension reform legislation in the fall of 2011, resulting in new actuarial rates that are significantly lower than those that would have otherwise gone into effect. As a result of this legislation, projected general revenue spending for FY 2013 was reduced by over $117.9 million. These savings continue to carry forward in the State’s FY 2014 budget.

FY 2014 Proposed Budget: Governor Chafee recommends an all funds budget totaling $8.172 billion for FY 2014, an increase of $92.8 million, or 1.2 percent, from the FY 2013 Revised Budget of $8.079 billion. Of this total, $3.399 billion, or 41.6 percent, is from general revenue, $2.645 billion, or 32.4 percent, is from federal funds, $1.875 billion, or 23.0 percent, is from other sources, and $252.8 million, or 3.1 percent, is from restricted or dedicated fee funds. The Governor’s FY 2014 Proposed Budget includes 15,171.6 authorized FTE positions, which is 69.1 FTE positions higher than what is included in the Governor’s FY 2013 Revised Budget Plan and 145.3 FTE positions more than what is included in the FY 2013 Enacted Budget.

Recommended FY 2014 general revenue funding of $3.399 billion represents an increase of $103.3 million, or 3.1 percent, over the FY 2013 enacted budget of $3.295 billion, and is 4.0 percent higher than the FY 2013 Revised Budget proposed by the Governor. Federal funds decrease from $2.676 billion in the FY 2013 enacted budget to $2.645 billion in the recommended FY 2014 budget. Other funds decrease from $1.895 billion to $1.876 billion.

FY 2013 Revised Budget: Governor Chafee recommends a revised all funds budget totaling $8.079 billion for FY 2013, a decrease of $20.2 million, or 0.25 percent, from the FY 2013 Enacted Budget of $8.099 billion. Of this total, $3.268 billion, or 40.4 percent, is from general revenue, $2.659 billion, or 32.9 percent, is from federal funds, $1.883 billion, or 23.3 percent, is from other sources, and $270.2 million, or 3.3 percent, is from restricted or dedicated fee funds. The Governor’s FY 2013 Revised Budget includes 15,102.5 authorized FTE positions, which is 76.2 FTE positions higher than what is included in the FY 2013 Enacted Budget.

Recommended FY 2013 general revenue funding of $3.267 billion represents a decrease of $28.2 million, or 0.85 percent, from the FY 2013 enacted budget of $3.296 billion, and is 5.1 percent higher than the FY 2012 actual expenditure. Federal funds decrease from $2.676 billion in the FY 2013 enacted budget to $2.659 billion in the revised FY 2013 budget. Other funds decrease from $1.895 billion to $1.883 billion compared to the enacted plan.

Overview

Tax reform: As noted in the introduction of this document, Governor Chafee's revenue plan was very simple – taxpayers have already shouldered enough of the cost of government, and the delicate recovery we are in today should not be derailed by any tax increases. Therefore, Governor Chafee's FY 2014 Proposed Budget <u>does not</u> include <u>any</u> increases in taxes, fees or charges.

In fact, Governor Chafee has introduced an initiative in his FY 2014 Budget to reduce the State's corporate tax rate from 9.0 percent to 7.0 percent over the next three years. The initiative reduces the corporate tax rate from 9.0 percent to 8.0 percent in tax year 2014, and further reduces it to 7.5 percent in tax year 2015 and finally to 7.0 percent in tax year 2016. In order to offset some of the costs of this initiative, the Governor proposes to reduce the benefits of the Jobs Development Tax Credit by 50.0 percent during this period of time. In addition, Governor Chafee proposes to eliminate the Enterprise Zone tax credits that are applicable to the Corporate Tax.

Governor Chafee's revenue plan also accounts for a revenue loss of $385,000 due to eliminating a fee considered a nuisance by businesses - the hazardous substance right-to-know fee.

Expenditure Plan: Governor Chafee focused attention on the current year spending levels and the FY 2014 spending levels to address the projected operating deficits. The challenge of balancing the State Budget is more difficult based upon a review of where overall general revenue actually goes. Expenditures from general revenue are projected to total $3.399 billion for FY 2014, increasing by $131.5 million over FY 2013 revised spending levels.

Human Services agencies represent the largest share of the growth with nearly $67.0 million of the general revenue growth attributed to human services programs. Expenditures totaling $1.337 billion for human services agencies represent nearly 39.3 percent of the total general revenue budget to support various health care and prescription drug coverage programs for low-income children, their parents, seniors and the poor, and community residential and treatment programs for the disabled.

Education is the second largest component of State spending, totaling $1.154 billion, or 34.0 percent of general revenue spending. This includes the State support for local education aid, support for the state university and colleges, and scholarships. General revenue expenditures for General Government and Public Safety comprise $456.6 million (13.4 percent) and $414.2 million (12.2 percent), respectively. General Government includes, along with state operations, state aid to municipalities and direct property tax relief. Public Safety includes the state prisons, Military Staff, State Police, Attorney General and Judicial departments. Finally, expenditures for Natural Resources comprise $37.2 million, or 1.1 percent of total general revenue funding. Transportation expenditures are financed by dedicated gasoline taxes and are not a component of general revenue spending. Note that Governor Chafee's FY 2014 Proposed Budget continues to shift gas tax supported debt service to the state's general revenue fund.

General revenue expenditures by category are primarily devoted to financing grants, local aid and personnel. The largest component is grants and assistance expenditures of $1.248 billion, comprising 36.7 percent of total general revenue spending. Local aid expenditures of $1.002 billion represent 29.5 percent of total spending; personnel expenditures of $825.2 million comprise 24.3 percent of the budget; operating expenditures total $123.9 million, or 3.7 percent of the budget; and capital expenditures, including debt service, total $195.6 million, or 5.7 percent of the total general revenue budget. Due to a proposed change in accounting for hospital and group home expenditures under the Department of Behavioral Healthcare, Developmental Disabilities and Hospitals, the allocation of costs by category for general revenue funds has changed from prior years, with a greater allocation to assistance and grants and less to personnel and operating. On an all funds basis, these adjustments net out and do not impact the comparison with prior years.

General revenue funding for local education aid increases by a net of $28.8 million in FY 2014, as compared to the FY 2013 enacted funding level. The Governor's budget provides $27.6 million for year three of the new funding formula and $3.1 million more for categorical aid. Education aid provided to local communities, charter schools, and state schools in FY 2014 total $945.2 million or $33.8 million more than provided in the FY 2013 Revised Budget.

Education Aid: Beginning July 1, 2011, the new education aid formula began to 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. The Governor's budget includes the best data available at the time of the budget submission; however these calculations will be updated using March 2013 student data, including final charter school lottery data, which is expected to be finalized by April 1, 2013.

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. Governor Chafee's FY 2014 budget recommends fully funding each of these programs at an additional cost of $3.1 million over enacted FY 2013 levels.

The State's FY 2014 share of teacher retirement costs increases by $2.7 million from the FY 2013 enacted levels to $82.5 million. In addition to anticipated payroll growth, the required rate of contribution for the State share increases from 19.29 percent in FY 2013 to 20.68 percent in FY 2014.

Human Services: After education aid, the next largest growth area in the FY 2014 budget is in human service programs. The Departments under the Executive Office of Health and Human Services have implemented a number of initiatives authorized in the FY 2013 enacted budget with the goal of addressing the significant and unsustainable growth in this functional area. These efforts will continue in FY 2014 by implementing proposals recommended by the Governor.

In the Medical Assistance program, the Governor recommends a $14.0 million reduction to the Caseload Estimating Conference's adopted funding level. This is achieved through three distinct policy actions designed to contain the Medicaid program's expenditure growth in FY 2014. First, the Governor recommends reductions to all Medicaid managed care capitation (i.e. monthly cost per member) rates, effective July 1, 2013, for savings totaling $4.4 million in general revenue. Rates will be negotiated so as to limit average annual growth in these rates to 1.6 percent, as opposed to the 3.0 percent increase assumed at the November 2012 CEC. The Governor further recommends a one year freeze at FY 2013 payment rates for inpatient and outpatient hospital services within both the fee-for-service and managed care segments of the Medical Assistance program, yielding $5.2 million in general revenue savings. Lastly, the Governor recommends the suspension of the rate increase to nursing care and hospice facilities scheduled for October 1, 2013, generating savings of $3.9 million in general revenue. The latter two measures will require both statutory amendments as well as the prior approval of the Centers for Medicare and Medicaid Services (CMS); the Governor's FY 2014 Appropriations Act contains legislation designed to meet both objectives.

Personnel: State personnel costs comprise 22.5 percent of total recommended spending in FY 2014. Actual filled positions totaled 13,656.9 FTE positions as of December 29, 2012, a 48.2 position decrease from the 13,705.1 filled position level as of January 14, 2012, and 1,425.9 FTE positions below the 15,082.8 FTE positions level in July 2007. The filled FTE position level of 13,656.9 is 1,396.4 FTE positions less than the FY 2013 enacted cap of 15,026.3 FTE positions.

Overview

In the FY 2013 revised budget, the Governor recommends a FTE position level of 15,102.5, an increase of 76.2 FTE positions from the FY 2013 enacted budget. In the FY 2014 budget, the Governor recommends an increase of 61.1 FTE positions from the FY 2013 revised budget, or 15,171.6 FTE positions.

Personnel costs increase $21.6 million, or 1.2 percent, in FY 2014, as compared to the FY 2013 Revised Budget. The budget assumes no cost of living adjustment for state employees in FY 2014, given that most employee contracts expire on June 30, 2013 and are subject to renegotiation. Until the contracts are resolved, the Governor's budget assumes no significant personnel cost increases or savings.

Governor Chafee's FY 2013 Budget submission last Spring included an initiative to begin analyzing the State's personnel system to identify where improvements can be made to make it more efficient, cost effective and more agile for today's needs. The General Assembly included $250,000 in funding to do this work, and an initial report is nearing completion. The current Merit System was designed and implemented in 1956 with few amendments since that time. Given the tremendous investment the State makes to support its workforce, the Governor believes there are opportunities to modernize the current outdated and cumbersome system and provide more flexibility for the day-to-day hiring and management of personnel, while still maintaining its collective bargaining process. Governor Chafee has included $500,000 in FY 2013 and $500,000 in FY 2014 to continue this work, focusing on reforming the classification system, which serves as the foundation to all personnel actions.

Energy Policy: There has been considerable progress made in developing a centralized effort for the oversight and administration of state and federal energy policies and programs in the State. The development of the Office of Energy Resources (OER) within the Department of Administration has brought cohesion to the process, and therefore, the Governor recommends bringing the balance of these programs within the Office. This will require that the administration of the Renewable Energy Fund program be transferred from the Economic Development Corporation to the Office of Energy Resources. Centralizing energy programs will provide the State with strong policy leadership for energy procurement and project development. The OER will provide more transparency and offer greater access for individuals, businesses, and municipalities looking for information on energy programs.

Transportation Finance: As the Governor highlighted in his FY 2013 Budget submission, the Department of Transportation is facing the same type of ongoing structural deficits that plague the State as a whole. The failure of the gas tax to keep pace with the growth in transportation expenditures will result in projected annual deficits in the Department for the foreseeable future. A significant contributor to this imbalance is the growth in debt service on general obligation debt issued on behalf of the Department and used for the match to federal highway funds. The General Assembly recognized that this method of providing the State match is not sustainable and in the 2011 session, enacted a plan to move the Department off of debt to pay-as-you-go financing for transportation projects.

The General Assembly enacted into law (1) an increase of $30.00 in biannual motor vehicle registration fees in $10.00 increments effective July 1st of 2013, 2014 and 2015; (2) an increase of $15.00 in annual motor vehicle registration fees in $5.00 increments effective July 1st of 2013, 2014 and 2015; and (3) a $30.00 increase in operator license fees in $10.00 increments effective July 1st of 2013, 2014 and 2015. The proceeds from these fee increases are to be used to finance the newly created Rhode Island Highway Maintenance Trust Fund and, combined with a $20.0 million appropriation from the Rhode Island Capital Plan Fund, should be sufficient to provide the necessary match to federal funds. The FY 2014 Appropriations Act makes some technical adjustments to the fee structure to ensure it is implemented as intended.

Although this plan would have long-term benefits to the Department's operating structural deficit, it does not address the short-term operations and highway maintenance needs. As such, in the FY 2014 recommended budget, the Governor continues to deal with the operating deficits in both the short and long term, as well as keep to the plan enacted by the General Assembly to address the capital funding side. The Governor recommends that debt service expenses on transportation debt be moved off of the Department of Transportation's budget and onto the Department of Administration's general revenue funded budget, where most other debt service is budgeted.

The plan would involve decreasing debt service expenses on the Transportation budget by $10.0 million in FY 2014 and to continue shifting debt service to the general fund in the out years until all such costs are being charged to general revenue funds under the Administration budget. Although this will cause more pressure on the general revenue budget and on projected out year deficits, the Governor believes that this is the best way to get the Department of Transportation on to sound financial footing and will ultimately lead to additional funding available for state and local infrastructure projects.

Similarly, the Governor proposes to assist the Rhode Island Public Transit Authority (RIPTA) in addressing projected operating shortfalls in its FY 2013 and FY 2014 budgets by transferring the cost of debt service on general obligation bonds issued on behalf of RIPTA from the Authority's budget to state general revenue. This will free up over $1.6 million of Authority resources in each fiscal year.

Digital Government: As part of the FY 2012 enacted budget, the General Assembly created the Technology Investment Fund. This fund is intended to provide resources to improve State Government information technology through the acquisition of new hardware, software and consulting services, with the goal of more efficient and user-friendly systems. While the financing source for this fund is the sale of state property, the FY 2013 Budget as Enacted included a one-time infusion of $9.0 million to jump-start the fund and get key technology initiatives off the ground. The recently created Office of Digital Excellence is responsible for the process and allocation of these funds.

Performance Management: Governor Chafee has implemented a Performance Management initiative for Rhode Island government departments and agencies to improve the effectiveness and efficiency of state programs and to maximize the value of taxpayer dollars. By developing performance measures and analyzing program data, departments and agencies are able to make better decisions about allocating personnel and financial resources to have the greatest impact.

In FY 2013, departments created new performance measures for their programs, and they now report data on a regular basis to the Office of Management and Budget (OMB). An interagency Performance Management team meets with departmental leadership quarterly to review performance data, determine whether departments are meeting their goals and develop innovative solutions to solve problems.

The Governor's FY 2014 budget submission includes many new performance measures, as well as historical data and targets when available. The OMB will work with remaining departments and agencies to develop performance measures that reflect the impact of their programs. The OMB will also report performance data on a regular basis to improve the transparency and accountability of Rhode Island government.

The following narratives provide a more detailed account of the Governor's FY 2013 Revised Budget and his FY 2014 Budget proposal. This document is accompanied by six other volumes to provide greater detail on the operating and capital budget plan.

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 2012 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 from an economist with Moody's Economy.com, and the Assistant Director for DLT's Labor Market Information unit.

The Revenue Estimating Conference adopted the economic forecast, shown at the end of the section, on November 5, 2012 through a consensus process informed by the testimony provided to the conferees. The updated economic forecast made significant changes to the consensus outlook adopted at the May 2012 Revenue Estimating Conference.

As reported at the November 2012 Revenue Estimating Conference, testimony noted that the state's current economy "lacks spark but is not in recession". The State's economic recovery is being slowed by significant macroeconomic headwinds and uncertainty. In particular, goods-producing industries are essentially seeing no growth, while service-based industries are experiencing enough modest gains to offset the contraction of public sector employment. According to written testimony, the Philadelphia Federal Reserve Bank's coincident index, a measurement of economic activity, Rhode Island's economy bottomed out in 2009 at a level of 143.5. In June of 2012 the index was 148.1, a gain of only 3.2 percent, providing further evidence that Rhode Island's economy, although far from "healthy", is not contracting. These findings mirror three other major indices: the Moody's Analytics Adversity Index, the Rhode Island Current Conditions Index and the Bryant University Current Economic Indicator.

Of particular concern for Rhode Island's economy is the competition from neighboring states. As Rhode Island tries to attract new and develop existing industries, in particular biotechnology and information services, other states are doing the same. These companies may look to Connecticut or Massachusetts for more favorable investment opportunities. Because of these factors and the beginning of Rhode Island's slow economic recovery, Rhode Island's unemployment rate is expected to remain above 10.0 percent until CY 2014 and won't fall below 6.0 percent until CY 2017. Housing prices in the State are projected to bottom out at the end of CY 2012 and show modest increases over the CY 2013 and CY 2014 periods. Personal income growth is anticipated to trail that of the U.S. as a whole, but be positive for the CY 2013 to CY 2015 forecast period. This trend is reversed in CY 2016 through CY 2018 when Rhode Island personal income growth is projected to exceed that of the United States as a whole.

While testimony from Economy.com gave a broad picture of Rhode Island's economic conditions as of November prior to the presidential election, the Rhode Island Department of Labor presented a detail analysis on Rhode Island's labor market. The Rhode Island Department of Labor and Training reported that the Rhode Island unemployment rate declined to 10.5 percent in September 2012. Rhode Island's resident employment figure peaked at 548,900 in December 2006. Rhode Island resident employment in September 2012 totaled 499,400, or 49,500 off the peak.

Rhode Island's seasonally adjusted unemployment rate for November 2012 stood at 10.0 percent. This was up from 9.9 in October 2012 and at the time of testimony was the second straight month over month increase in Rhode Island's unemployment rate.

Rhode Island establishment employment decreased over the period September 2011 to September 2012 resulting in 1,700 job losses. The sector breakdown of job losses were as follows: Government, (1,300); Educational Services, (1,200); Other Services, (900); Trade Transportation and Utilities, (900); Professional and Business Services, (600); Manufacturing, (300); and Information, (100). The broad sectors of the Rhode Island economy which added jobs year-over-year in September 2012 were as follows: Financial Activities, 300; Construction, 800; and Leisure and Hospitality, 2,500. The Natural Resources and Mining sectors of the Rhode Island economy remain unchanged relative to September 2011.

Sector	Jobs Change	Sector	Jobs Change
Government	(1,300)	Information	(100)
Education and Health Services	(1,200)	Natural Resource & Mining	-
Other Services	(900)	Financial Activities	300
Trade, Transportation & Utilities	(900)	Construction	800
Professional & Business Services	(600)	Leisure & Hospitality	2,500
Manufacturing	(300)	**Total Non-Farm**	**(1,700)**

Staff from the Rhode Island Department of Labor and Training (DLT) testified that they expect to see significant revisions to the June 2012 job numbers reported by the Bureau of Labor Statistics (BLS). Using a methodology developed by the University of Massachusetts, DLT staff expects total non-farm employment for June 2012 to be revised upward by 5,700 jobs. It should be noted that Moody's economic forecast incorporated upward revisions to BLS data for forecast numbers, but used current BLS total employment numbers for historical figures. As a result, it is expected that the May 2013 Revenue Estimating Conference will see significant changes to the forecast presented in the next section. The changes by sector as calculated by DLT are shown in the table below.

The Economy

Sector	Jobs Change	Sector	Jobs Change
Professional & Business Services	3,000	Other Services	100
Trade, Transportation & Utilities	2,800	Natural Resource & Mining	-
Leisure & Hospitality	2,700	Information	(700)
Education and Health Services	400	Manufacturing	(1,300)
Financial Activities	200	Government	(1,500)
Construction	100	**Total Non-Farm**	**5,700**

Source: RI Department of Labor and Training, Labor Market Information Unit, Quareterly Cenus of Employment & Wages (QCEW) and Current Employment Statistics (CES) data, Using methodology developed by the University of Massachusetts.

* Difference is a result of rounding

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 2012, total non-farm employment declined by 0.3 percent. In FY 2013, non-farm employment is expected to decrease by 0.4 percent. Total non-farm employment is projected to increase by 1.2 percent from 457,200 in FY 2013 to 462,800 in FY 2014, the first year of positive growth since FY 2007. Over the FY 2015 through FY 2018 period, Rhode Island's economy is expected to add 27,357 jobs. It should be noted that adopted growth rates indicate a positive trend from FY 2014 through FY 2016 before a slowing down in FY 2017 and FY 2018 at rates of growth of 1.9 percent and 0.6 percent respectively.

The unemployment rate for FY 2013 is projected to decline slightly from 11.1 percent in FY 2012 to 10.4 percent. As recovery takes hold, Rhode Island's unemployment rate is expected to decline rapidly from 10.4 percent in FY 2013 to 5.3 percent in FY 2018. Even at this lower rate, Rhode Island's unemployment rate will be 0.4 percentage points higher than the unemployment rate achieved when the economy peaked in FY 2007 of 4.9 percent.

Personal income growth is expected to be 2.6 percent in FY 2013 down from the 3.2 percent growth in FY 2012. The November 2012 Revenue Estimating Conference estimates for personal income growth suggest a positive upward trend from FY 2013 through FY 2017. It should be noted that for FY 2012 through FY 2013 the adopted estimates for personal income growth are below the adopted estimates from the May 2012 Revenue Estimating Conference for the same period. The FY 2012 projected growth rate for personal income is down 0.8 percent growth rate that was adopted in May 2012 of 4.0 percent. For FY 2013 the adopted November 2012 REC estimate is 1.3 percent down from 3.9 percent that was adopted in May. The personal income growth rate is expected to increase to 7.0 percent in FY 2015 and remain at or above 4.4 percent throughout the remainder of the forecast period. This projection indicates that personal income growth will take one more year to accelerate than originally projected in May 2012.

Similarly, FY 2013 estimates of dividend, interest and rents are expected to decrease from FY 2012 growth of 6.5 percent before bouncing back considerably in FY 2014 through FY 2018. Wage and salary income growth is forecasted lower in FY 2012 relative to the projected growth adopted in May 2012. For the FY 2013 to FY 2018 period, the November 2012 growth rates were revised upwards when compared to the forecast adopted in May 2012. Wage and salary income growth is expected to improve beginning in FY 2013 with projected growth of 2.6 percent, an increase of 0.4 percentage points from FY 2012. The rate of growth accelerates in FY 2014 to 5.7 percent and increases again in FY 2015 and FY 2016 to 7.0 percent before decelerating in FY 2017 and FY 2018 to 6.4 percent and 4.8 percent respectively.

The U.S. rate of inflation as measured by the Consumer Price Index for all urban consumers (CPI-U) is anticipated to decrease to 1.9 percent in FY 2013 from 2.9 percent in FY 2012. The decrease 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 rate of growth in CPI-U is forecasted to increase in FY

2014 to 2.5 percent before rising to 2.6 percent in FY 2015. In FY 2016 and FY 2018, inflation is expected to decelerate and settle at 2.3 percent.

From FY 2013 through FY 2015, the interest rate on three month Treasury bills is expected to remain low with rates below 0.8 percent. In FY 2016, the interest rate on three month Treasury bills is expected to rise to 2.6 percent and increase again by 1.1 percentage point to approximately 3.7 percent in FY 2017 before stabilizing at 3.5 percent in FY 2018. The interest rate on ten year Treasury notes is expected to decrease slightly from 2.1 percent in FY 2012 to 1.9 percent in FY 2013 but rise to 3.0 percent and 4.0 percent in FY 2014 and FY 2015. The interest rate on ten year Treasury notes is anticipated to increase again to 4.9 percent in FY 2016 and then decrease to 4.8 percent in FY 2017 and 4.7 percent in FY 2018.

The Consensus economic forecast for the fiscal years 2013 through 2018 agreed upon by the conferees at the November 2012 Revenue Estimating Conference is shown in the following table.

The November 2012 Consensus Economic Forecast

Rates of Growth (%)	**FY 2013**	**FY 2014**	**FY 2015**	**FY 2016**	**FY 2017**	**FY 2018**
Non-Farm Employment	-0.4	1.2	3.0	3.2	1.9	0.6
Personal Income	2.6	5.1	7.0	6.5	5.7	4.4
Wage and Salary Income	2.6	5.7	7.0	7.0	6.4	4.8
Dividends, Interest and Rent	3.2	7.4	11.4	10.3	6.9	4.2
Nominal Rates (%)						
U.S. CPI-U	1.9	2.5	2.6	2.4	2.3	2.3
Unemployment Rate	10.4	9.7	7.9	6.6	5.5	5.3
Ten Year Treasury Notes	1.9	3.0	4.0	4.9	4.8	4.7
Three Month Treasury Bills	0.1	0.2	0.8	2.6	3.7	3.5

Changes from May 2012 to November 2012 Consensus Economic Forecast

Rates of Growth (%)	**FY 2013**	**FY 2014**	**FY 2015**	**FY 2016**	**FY 2017**
Non-Farm Employment	-1.3	-0.5	0.1	0.2	0.4
Personal Income	-1.3	0.2	1.0	1.0	1.1
Wage and Salary Income	-2.1	0.2	1.1	1.0	1.4
Dividends, Interest and Rent	-1.0	0.0	1.5	2.3	1.8
Nominal Rates (%)					
U.S. CPI-U	0.1	0.3	-0.2	-0.2	0.0
Unemployment Rate	0.1	0.3	0.4	0.4	0.1
Ten Year Treasury Notes	-1.2	-1.2	-0.6	0.1	-0.1
Three Month Treasury Bills	0.0	-0.3	-1.1	-0.5	0.2

General Revenues

Introduction

The Governor's recommended budget is based on estimated general revenues of $3.331 billion in FY 2013 and $3.426 billion in FY 2014. Annual estimated growth during FY 2013 and FY 2014 is 1.9 percent and 2.9 percent, respectively. Estimated deposits of $103.8 million and $105.2 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 97.0 percent of estimated revenues in FY 2013 and 97.0 percent of estimated revenues in FY 2014. The revenue estimates contained in the Governor's FY 2013 supplemental and FY 2014 recommended budgets are predicated upon the revenue estimates adopted at the November 2012 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 2013 Revised Revenues

The principals of the November 2012 Revenue Estimating Conference adopted revenue estimates that were $7.5 million greater than the enacted FY 2013 revenue estimates, an increase of 0.2 percent. As shown in the *Changes to FY 2013 Enacted Revenue Estimates* table in Appendix A of this document, the Governor's revised FY 2013 Budget recommends a net increase of $2.8 million in revenues.

The recommended change to the FY 2013 adopted estimates is attributable to anticipated receipts of $4.4 million in overdue payments for the FY 2012 Hospital Licensing Fee. Additionally, the change to the FY 2013 adopted estimates incorporates a decrease of $1.6 million for administrative and staffing expenses associated with the operation of table games at Twin River Casino.

FY 2013 Revised Revenues vs. FY 2012 Final Revenues

Recommended revenues for FY 2013 are based upon a $60.5 million increase in total general revenues over final FY 2012, or growth of 1.9 percent. Much of this increase can be found in personal income taxes, business corporations and franchise taxes, sales and use taxes, and the lottery transfer. These increases are partially offset by estimated decreases in inheritance and gift taxes, other miscellaneous revenues, and the unclaimed property transfer.

Personal income tax collections continue to be the single largest source of state general revenues in FY 2013 at 32.4 percent. Personal income tax collections are estimated to expand at an annual rate of 1.7 percent or $18.1 million for FY 2013. Much of this increase is due to increased final income tax payments of $9.4 million and increased withholding tax payments of $10.9 million. The overall increase, however, is slightly offset by an increase in refund payments by $6.8 million

General business tax collections are projected to increase by $23.7 million or 6.2 percent, due primarily to an estimated increase in business corporations taxes of $12.8 million and an increase in financial institutions taxes and public utilities gross premiums taxes of $4.6 million and $3.4 million respectively. Each component of general business taxes are anticipated to increase when compared to final audited FY 2012.

General Revenues

Sales and use tax collections are projected to increase by $28.3 million or 3.3 percent, over final FY 2012 collections. The anticipated increase in sales and use tax revenues is partially attributable to the passage of a sales tax base expansion on three items effective October 1, 2012 in the enacted FY 2013 Budget signed into law on June 15, 2012. Sales and use taxes represent 26.4 percent of total general revenues in FY 2013. For FY 2013 sales and use tax collections are projected to be $879.4 million.

Excise taxes other than the sales and use tax are expected to increase by $7.3 million or 3.7 percent in FY 2013 over final audited FY 2012 collections due to a projected increase in cigarette and other tobacco product taxes of $6.6 million. The anticipated increase in cigarette and other tobacco product taxes is the result of increased tax enforcement and an increase in the cigarette excise tax rate. Motor vehicle operator's licenses and registration fees, motor carrier fuel use, and alcohol excise taxes tax collections are estimated to increase by $308,436, $267,328 and $126,354 respectively in FY 2013.

Other taxes are projected to decrease by $12.7 million, or 30.5 percent in FY 2013 relative to final audited FY 2012 receipts. Of the total decrease in other taxes, inheritance and gift taxes are expected to decrease by $12.6 million, or 27.2 percent. The expected decrease in inheritance and gift tax collections is attributable to fewer receipts. In FY 2012 several large estate receipts were received and it is anticipated that these receipts will not re-occur in FY 2013. Realty transfer taxes are anticipated to increase by $65,335 and racing and athletics tax collections are projected to decline by $127,003. Racing and athletic taxes' downward trend is expected to continue as Twin River is no longer required to offer live greyhound racing and now solely relies on simulcast racing for pari-mutuel wagering. Racing and athletics taxes are expected to total $1.2 million in FY 2013 a decrease of 9.6 percent from final FY 2012 collections. Realty transfer taxes are expected to total $6.5 million in FY 2012, an increase of 1.0 percent from final audited FY 2012 collections.

In the Governor's FY 2013 Budget, departmental receipts are projected at $351.9 million, an increase of $12.0 million from final audited FY 2012 collections, or 3.5 percent. The increase in the departmental receipts is attributable to anticipated receipts in overdue payments for the FY 2012 Hospital Licensing Fee amounting to $4.4 million and an increase in expected revenues adopted at the November 2012 Revenue Estimating Conference of $7.6 million. It should be noted that only a partial payment is expected in FY 2013 from an overdue payment of a FY 2012 Hospital Licensing Fee. The remainder is expected to be received in FY 2014.

In addition to the above general revenue components, an increase is expected in FY 2013 for the lottery transfer to the general fund of $7.4 million, or 2.0 percent from the final audited FY 2012 transfer. The increased lottery transfer in FY 2013 is due to the results of the November 2012 REC which increased the estimated transfer amount from the video lottery terminals installed at Twin River and Newport Grand by $7.6 million and increased instant tickets and on-line games by $1.4 million from the enacted FY 2013 Additionally, the FY 2013 revised lottery transfer incorporates administrative and operating expenses netted for the operation of table games at Twin River of $1.6 million. Under current law, the transfer to the State occurs after the expense to implement, regulate, and monitor table games by the Division of Lottery and is deducted from the State's share of gross table game revenues.

The unclaimed property transfer to the general fund is forecasted to decrease by $8.3 million in FY 2013 or 56.7 percent from final audited FY 2012 revenues. The decrease in the unclaimed property transfer is based on the testimony provided by the Office of the General Treasurer at the November 2012 REC. For FY 2013, other miscellaneous general revenues are projected to decrease by $15.5 million from final audited FY 2012 revenues.

General Revenues

FY 2014 Proposed Revenues

The Governor's recommended FY 2014 budget estimates general revenues of $3.426 billion, an increase of 2.9 percent from the revised FY 2013 level. The Governor's recommendation is comprised of $3.288 billion of revenue estimated at the November 2012 Revenue Estimating Conference and $138.3 million of changes to the adopted estimates. These changes are shown in the schedule *Changes to FY 2014 Adopted Revenue Estimates* located in Appendix A of this document.

The largest source of FY 2014 general revenues is the personal income tax, with estimated receipts of $1.131 billion, $1.8 million more than the November 2012 REC adopted estimate for FY 2014 or growth of 4.8 percent from the revised FY 2013 amount. This revenue increase is partly the result of the Governor's recommendation for the administration of a special investigation tax unit located in the Division of Taxation. The FY 2014 budget projects increased revenue collections of $1.0 million from the investigation tax unit through the process of more efficiently and effectively identifying, monitoring, and quantifying tax fraud and related activity within personal income tax collections. The Governor also proposes to allow the Division of Taxation to hire out of state collection agencies to more effectively collect debts from non-resident individuals and business. According to the Division of Taxation, there are currently 11,554 non-resident individuals owing the state over $28.89 million. The FY 2014 budget projects increase revenue collections of $750,000.

General Business taxes are projected to comprise 11.2 percent of total general revenue collections in the FY 2014 Budget. Business corporations tax revenues are expected to yield $135.1 million, a decrease of $5.3 million from the FY 2014 estimate adopted at the November 2012 REC. This decrease is partially attributable to the Governor's recommendation to reduce the state's corporate tax from 9.0 percent to 7.0 percent over a three year period beginning January 1, 2014.

The three year tax decrease is as follows:

- Effective January 1, 2014 the business corporation tax rate will decrease from 9.0 percent to 8.0 percent.
- Effective January 1, 2015 the corporate tax rate will decrease from 8.0 percent to 7.5 percent.
- Effective January 1, 2016 the corporate tax rate will decrease from 7.5 percent to 7.0 percent.

The FY 2014 budget estimates decreased revenue collections of $8.0 million as the result of the rate reduction. The Governor also proposes to reduce the value of the business corporation tax reduction title the "Jobs Development Act" (JDA). For tax years beginning on or after January 1, 2014 and before January 1, 2015 the tax benefit a company receives from the JDA shall be reduced by 25.0 percent. For tax years beginning on or after January 1, 2015 and thereafter the tax benefit a company receives from the JDA as of tax year 2013 shall be reduced by 50.0 percent. The FY 2014 recommended budget estimates additional revenue of $2.4 million from the JDA rate reduction. Additionally the Governor recommends the sunset of the Rhode Island General Law Chapter 42-64.3 titled "Distressed Areas Economic Revitalization Act" for tax years beginning on or after January 1, 2014. It is anticipated that revenues will increase by $309,380 as a result of the sunset legislation. The estimated growth rate in business corporations taxes over the FY 2013 revised level is -0.6 percent.

Insurance companies gross premiums taxes are projected to reach $96.8 million in FY 2014, a decrease of $177,932 from the FY 2014 estimate adopted at the November 2012 REC. This decrease is the result of a rate decrease to managed care. The recommended growth rate in FY 2014 insurance companies gross premiums taxes over the FY 2013 revised estimate is 5.4 percent.

General Revenues

FY 2014 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 2012 REC. The FY 2014 recommended growth rate for public utilities gross earnings tax relative to the FY 2013 revised estimates is -1.5 percent. For financial institution taxes the recommend growth rate for FY 2014 relative to FY 2013 revised estimates is -62.2 percent. Bank deposit taxes are expected to grow by 4.8 percent in the FY 2014 recommended revenue level from the revised FY 2013 estimate.

The health care provider assessment on nursing homes is forecasted to yield $43.1 million, a decrease of $430,279 from the estimate that was adopted at the November 2012 REC. This decrease is attributed to the estimated decline in revenues from the Governor’s proposal to suspend the cost of living adjustment nursing homes are scheduled to receive October 1, 2013. The recommended growth rate in FY 2014 health care provider assessment taxes over the FY 2013 revised estimate is 1.8 percent.

Sales and use tax collections are expected to yield $904.3 million in FY 2014, $200,000 more than was adopted at the November 2012 Revenue Estimating Conference for FY 2014. This increase is attributable to the Governor’s recommendation for a special investigation tax unit within the Division of Taxation. The FY 2014 budget projects increased revenue collections of $200,000 from this proposal. Sales and use taxes are anticipated to contribute 26.4 percent to total general revenues in FY 2014.

Motor vehicle operator license and vehicle registration fees are forecasted to equal $48.7 million in FY 2014, the same amount that was adopted at the November 2012 REC. Motor Fuel tax revenues are projected to be $1.0 million, the same as the estimate adopted at the November 2012 Revenue Estimating Conference.

Cigarette and other tobacco products tax revenues and alcohol tax revenues are expected to total $137.4 million and $12.2 million, the same amounts that were adopted at the November 2012 REC. The respective growth rates over the revised FY 2013 estimate for cigarette and other tobacco product taxes is -0.2 percent. Alcohol tax revenues are anticipated to increase by 1.7 percent over the FY 2013 revised estimate.

Inheritance and gift taxes, racing and athletics taxes, and the realty transfer are all equal to the amount adopted at the November 2012 REC. Inheritance and gift taxes are estimated at $35.4 million, racing and athletics taxes are expected to total $1.1 million, and the realty transfer is estimated to generate $6.7 million in FY 2014. Other taxes are expected to comprise 1.3 percent of total general revenues in FY 2014.

FY 2014 departmental receipts are expected to generate $1.4 million less than the revised FY 2013 estimate. Inclusive of the Governor’s proposed changes to departmental receipts, total departmental revenues are expected to be $353.3 million in FY 2014, or 10.3 percent of total general revenues. The anticipated increase in FY 2014 departmental receipts is the result of the one time inclusion of an overdue hospital licensing fee payment in the revised FY 2013 budget. The Governor’s FY 2014 recommended budget includes the reinstatement of the hospital licensing fee at the current rate of 5.350 percent applied to the current base of hospital fiscal year 2011 net patient revenues. The hospital licensing fee rate of 5.350 percent is discounted by 37.0 percent “for all hospitals located in Washington County, Rhode Island” subject to the approval of the Centers for Medicare and Medicaid Services. The 37.0 percent discount yields an effective hospital licensing fee rate for Washington County hospitals of 3.3705 percent. In addition to the hospital licensing fee reinstatement the FY 2014 recommended departmental revenues figure includes the following proposals:

- An increase of $141.3 million from reinstituting the hospital licensing fee at 5.350 percent of 2011 net patient revenues, "except that the license fee for all hospitals located in Washington County, Rhode Island shall be discounted 37.0 percent";
- An increase of $5.6 million from anticipated receipts in overdue payments for the FY 2012 Hospital Licensing Fee;
- A decrease of $384,575 from the elimination of the Department of Labor and Training hazardous substance right to know fee;
- An increase of $40,000 in interest paid on overdue taxes from the creation of a special investigation tax unit;
- An increase of $10,000 in penalties paid on overdue taxes from the creation of a special investigation tax unit;

The FY 2014 recommended revenues for the other sources component totals $412.8 million, an increase of $16.8 million, or 4.2 percent, compared to the revised revenue estimate for FY 2013. Other miscellaneous revenues are anticipated to generate $2.4 million in FY 2014 the same level adopted at the November 2012 Revenue Estimating Conference.

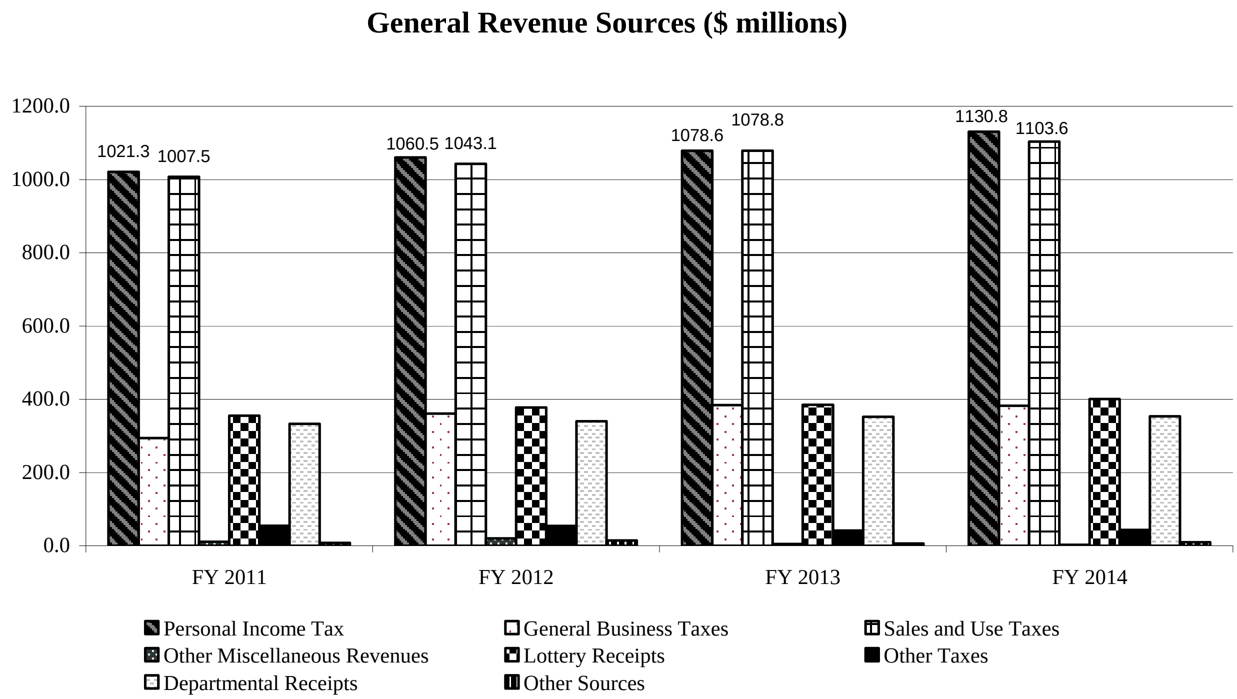
Within the gas tax transfer component, the Governor's FY 2014 Budget shows no change from the FY 2013 revised estimate. Effective July 1, 2009, the state's general fund no longer receives any of the revenues generated by the state's $0.32 per gallon gas tax.

Within the lottery category, the recommended FY 2014 budget is $15.7 million more than the revised FY 2013 budget, an increase of 4.1 percent. The Governor recommended FY 2014 estimate is $4.3 million lower than the estimate adopted at the November 2012 REC. This decrease is to account for the administrative and operating expenses netted against gross receipts for the operation of table games at Twin River. In FY 2014, the lottery transfer is expected to be $400.8 million and comprise 11.7 percent of total general revenues.

The final category of general revenue receipts is the unclaimed property transfer. In FY 2014, this transfer is expected to increase by $3.3 million, or 52.4 percent, from the revised FY 2013 estimate. The unclaimed property transfer is projected to be $9.6 million in FY 2014, and comprises 0.3 percent of all general revenues.

The chart below shows the sources of general revenues for the period FY 2011 – FY 2014. The values of the two major sources of general revenues, personal income taxes and sales and use taxes, are highlighted.

General Revenues



Restricted Receipts and Other Sources of Revenue

Introduction

The Governor's recommended budget proposes changes to revenue sources other than general revenues for FY 2014. The revenue estimates in the Governor's FY 2014 recommended budget contains a net change total of $(645,627) in non-general revenue adjustments.

FY 2014 Recommended Non-General Revenues

The Governor's FY 2014 budget proposes to rename the "Rhode Island Highway Maintenance Trust Fund" the "Rhode Island Highway Maintenance Account" and establish the account in the Intermodal Surface Transportation Fund (ISTF). The ISTF is the State's financing source for the Department of Transportation. In addition, to renaming and establishing an account within the ISTF, the Governor has reevaluated the data and information provided by the Department of Revenue's Division of Motor Vehicles to ensure the original intent of the FY 2013 Enacted Budget's "Rhode Island Highway Maintenance Trust Fund" is implemented beginning July 1, 2014. As a result of this analysis the Governor recommends a decrease of $725,627 to FY 2014 non-general revenue, more specifically the Rhode Island Highway Maintenance Account.

The Governor's recommended FY 2014 budget proposes to classify surplus receipts from the TDD relay program to the commission on the Deaf and Hard of Hearing for a new program. The new program titled the Emergency and Public Communication Access Program (EPCAP) will allow the Commission to further support communication access for the State's deaf and hard of hearing population. The FY 2014 recommended budget includes an increase of $80,000 in non-general revenues for this program.

All Sources

The FY 2014 total budget of $8,172.5 million includes all sources of funds from which state agencies make expenditures.

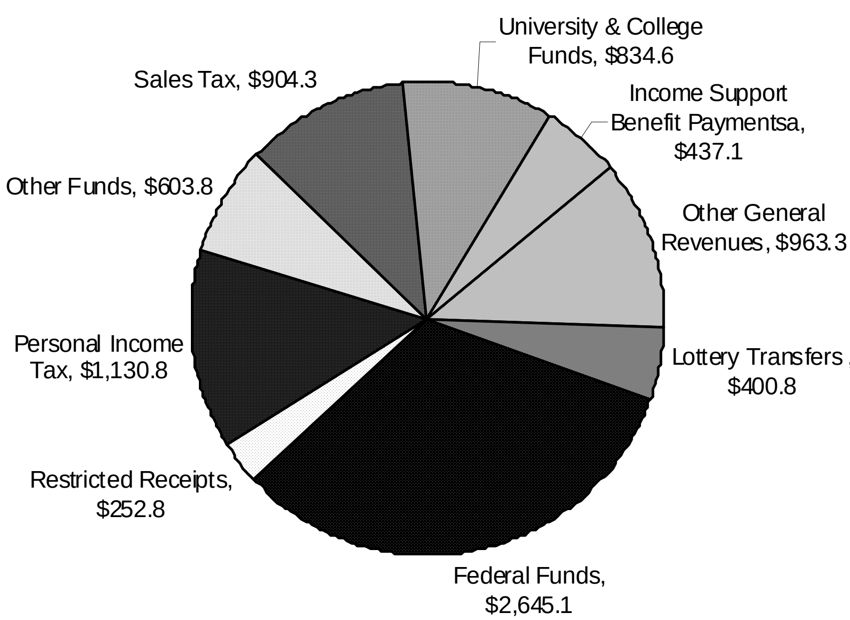
Federal funds represent 32.4 percent of all funds. Over 71.8 percent of federal funds are expended for human services, primarily for Medicaid.

Income and Sales Taxes combined represent 24.9 percent of all revenue sources.

University and College Funds, and Income Support Benefit payments represent 10.2 percent, and 5.3 percent of the total, respectively.

Remaining sources include: Other General Revenues, 11.8 percent; the Lottery Transfer, 4.9 percent; Restricted Receipts, 3.1 percent; and Other Funds 7.4 percent.

Where It Comes From



All Expenditures

The Governor's FY 2014 Budget recommendation is $8.172 billion in all funds comprised of six functional units of state government: Human Services, Education, General Government, Public Safety, Transportation, and Natural Resources.

Approximately 40.1 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 2014 recommended budget for all human service agencies is $3.317 billion.

Approximately 28.4 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, and the Historical Preservation and Heritage Commission. The FY 2014 recommended budget for education is $2.319 billion.

Approximately 17.5 percent of all expenditures are for General Government, which includes agencies that provide general administrative services to other state agencies, assist in developing the state's workforce, assist municipalities in achieving fiscal health, and those that perform state licensure and regulatory functions. The FY 2014 recommended budget for all General Government agencies is $1.431 billion.

Approximately 6.4 percent of all expenditures are for Public Safety, which is the system that provides law enforcement, adjudicates justice, performs correction and rehabilitative services, and handles emergencies impacting Rhode Island's citizens. The FY 2014 recommended budget for the public safety system is $524.6 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 2014 recommended budget for transportation is $469.9 million.

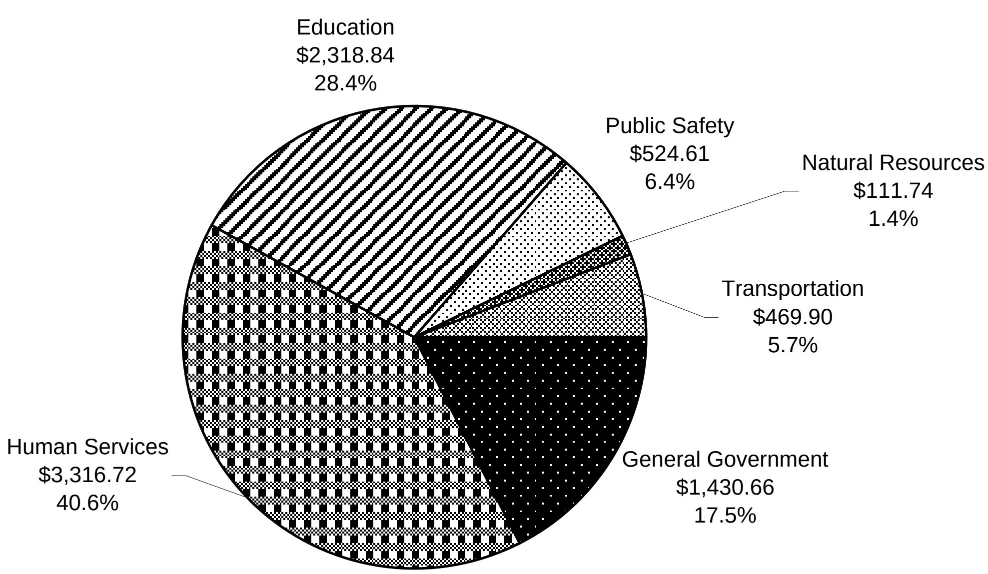
Approximately 1.4 percent of all expenditures are for Natural Resources, which includes the Department of Environmental Management and the Coastal Resources Management Council. The FY 2014 recommended budget for natural resources is $111.7 million.

Expenditure Summary

All funds expenditures for FY 2014 are $8.172 billion. Of this total, $3.399 billion, or 41.6 percent, is from general revenue, $2.645 billion, or 32.4 percent, from federal funds, $1.876 billion, or 23.0 percent, from other sources, and $252.8 million, or 3.1 percent, is from restricted or dedicated fee funds.

On a functional basis, the largest percentage of expenditures is in the Human Services area, which comprises $3.317 billion, or 40.6 percent of the total budget. This is followed by spending for Education of $2.319 billion, which comprises 28.4 percent of all spending, and expenditures for General Government of $1.431 billion, equaling 17.5 percent. Public Safety, Natural Resources and Transportation expenditures make up the balance, totaling $1.106 billion, or 13.5 percent of the total budget.

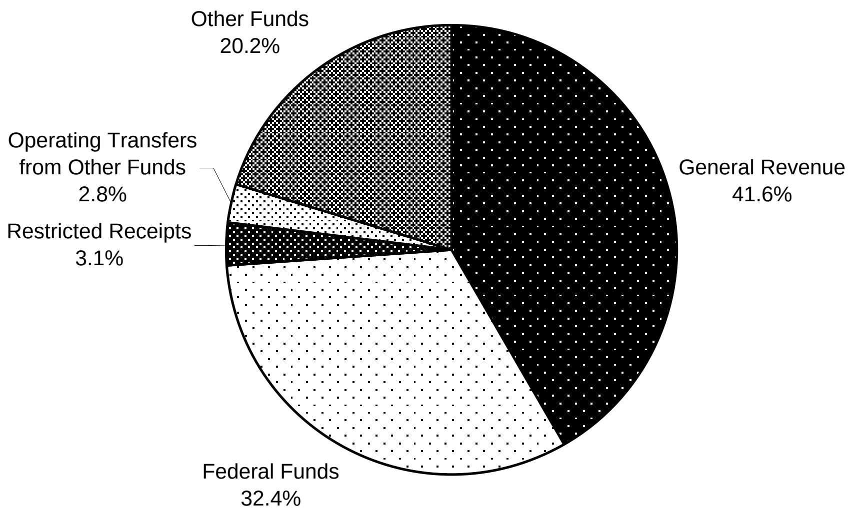
All Funds Expenditures by Function



The second way to view expenditures is by major category. On this basis, the largest share of the FY 2014 budget is for assistance, grants and benefits equaling $3.779 billion or 46.2 percent of the total. This is followed by personnel expenditures, which comprise 22.5 percent, or $1.835 billion, and local aid expenditures, which make up 14.4 percent, or $1.178 million of the total budget. Expenditures for capital purchases and debt service total $649.3 million or 7.9 percent, with the balance of spending used to finance operating expenditures and operating transfers of $731.4 million, or 8.9 percent of the total.

Expenditure Summary

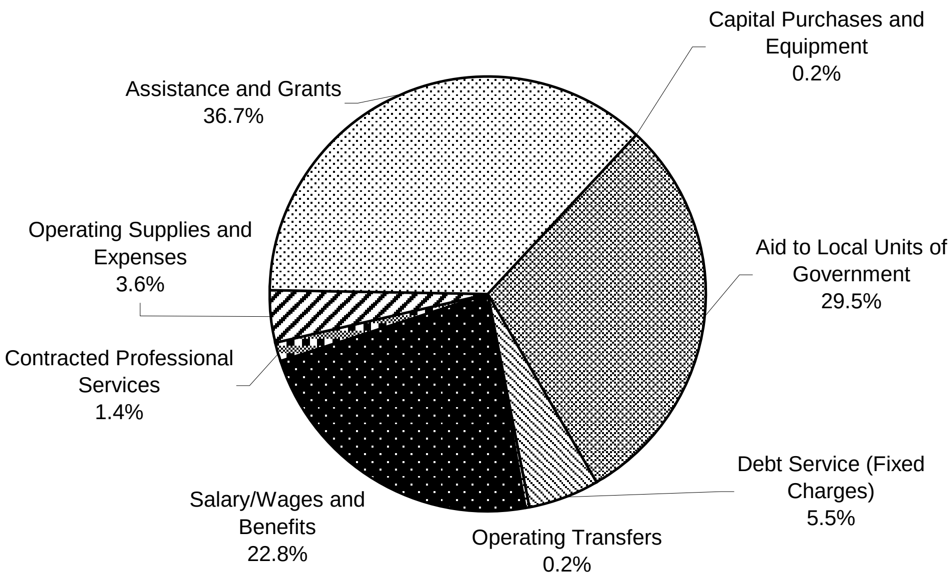
All Funds Expenditures by Source



Expenditures from general revenue total $3.399 billion for FY 2014. By function, spending by Human Service agencies represents the largest share with expenditures, totaling $1.337 billion, or 39.3 percent of the general revenue budget. This is followed by spending for Education, which totals $1.154 billion, or 34.0 percent. General revenue expenditures for General Government and Public Safety comprise $456.6 million (13.4 percent) and $414.2 million (12.2 percent), respectively. Expenditures for Natural Resources comprise $37.2 million, or 1.1 percent of total general revenue spending. Transportation expenditures are financed by dedicated gasoline taxes and are not a component of general revenue spending.

General revenue expenditures by category are primarily devoted to financing grants, local aid and personnel.

General Revenue Expenditures Statewide



Expenditure Summary

The largest components of general revenue expenditures are assistance, grants, and benefit expenditures of $1.248 billion, comprising 36.7 percent of total general revenue spending. Local Aid expenditures of $1.003 billion represent 29.5 percent of total spending; personnel expenditures (including contracted services) of $825.2 million comprise 24.3 percent of the budget; operating expenditures and operating transfers total $131.1 million, or 3.9 percent of the budget; and, capital expenditures and debt service total $192.6 million, or 5.7 percent of the total general revenue budget.

Enacted and proposed expenditures for general revenue funds, by category of expenditure are shown in the following table:

General Revenue Funds Category of Expenditure	FY 2013 Enacted	FY 2013 Revised	Change from Enacted	FY 2014 Recommended	Change from Enacted
Salary/Wages and Benefits	$812.0	$805.1	-$6.9	$776.4	-$35.6
Contracted Professional Services	$46.4	$47.7	$1.3	$48.8	$2.4
Operating Supplies and Expenses	$126.2	$128.8	$2.6	$123.9	-$2.3
Assistance and Grants	$1,152.8	$1,127.2	-$25.7	$1,247.7	$94.9
Capital Purchases and Equipment	$5.6	$10.4	$4.9	$6.7	$1.1
Aid to Local Units of Government	$962.4	$960.9	-$1.5	$1,002.7	$40.2
Debt Service	$184.4	$181.2	-$3.2	$185.8	$1.4
Operating Transfers	$5.9	$6.3	$0.4	$7.1	$1.2
Total	$3,295.8	$3,267.7	-$28.2	$3,399.2	$103.3
(in millions)					

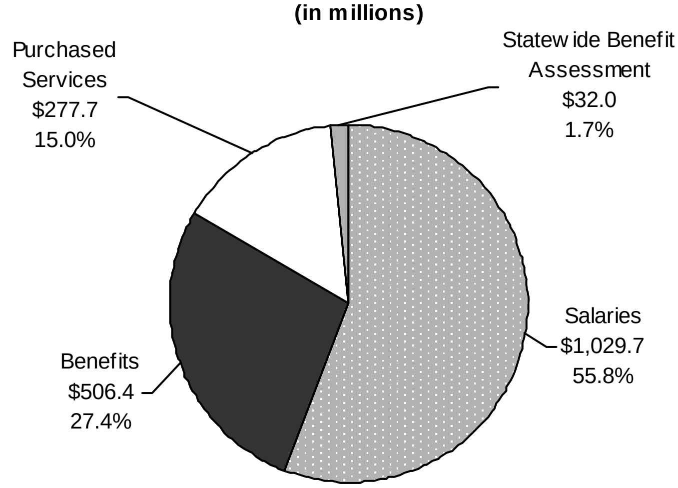
Enacted and proposed expenditures by source of funds are shown in the following table:

Source of Funds	FY 2013 Enacted	FY 2013 Revised	Change from Enacted	FY 2014 Recommended	Change from Enacted
General Revenue	$3,295.8	$3,267.7	-$28.2	$3,399.2	$103.3
Federal Funds	$2,676.3	$2,659.1	-$17.3	$2,645.1	-$31.3
Restricted Receipts	$232.5	$270.2	$37.7	$252.8	$20.2
Operating Transfers	$181.5	$197.1	$15.6	$226.4	$44.9
Other Funds	$1,713.7	$1,685.7	-$28.0	$1,649.1	-$64.6
Total	$8,099.9	$8,079.7	-$20.2	$8,172.5	$72.6
(in millions)					

Personnel Summary

The Governor's FY 2014 recommended budget finances personnel at $1.8 billion. This includes $1.5 billion for salary and benefits (83.2 percent), $277.7 million for purchased services (15.1 percent), and $32.0 million (1.7 percent) for such statewide benefits as severance, unemployment and workers compensation that are funded by a statewide assessment. This total includes expenditures financed from general revenues, federal grants, restricted receipts, other funds, and internal service funds. General revenue finances 44.7 percent of FY 2014 personnel expenditures. Federal funds finance 20.9 percent, Other Funds (primarily college tuition funds) and Internal Service Funds finance 23.3 percent, and restricted receipts finance the remaining 11.1 percent. The personnel supplements provided in the budget volumes contain all expenditures for personnel, including those of the internal service funds, as noted above. Since internal service fund positions are financed through charges to state agencies categorized as operating expenses, totals shown will differ in some cases from personnel costs shown in complementary documents of the FY 2014 Budget. After adjusting to reflect internal service fund personnel expenditures in the personnel category rather than as an operating expense, personnel expenditures constitute approximately 22.5 percent of the state budget, the second largest category of spending (after assistance, grants and benefits).

FY 2014 Personnel Expenditures
(in millions)



Personnel expenditures recommended for FY 2014 increase by $22.2 million from the FY 2013 revised budget, and by $25.4 million (1.4 percent) from the FY 2013 enacted budget. From the enacted budget, direct salaries decrease by 0.8 percent, overtime increases by 25.0 percent, fringe benefits increase by 4.5 percent overall, with retiree health and retirement both increasing by 9.3 percent and 6.2 percent respectively. Medical benefits (including the medical waiver bonus) increase by 1.6 percent.

Rhode Island state government experienced significant attrition from retirements in FY 2009. Between May 1, 2008 and October 1, 2008, 1,396 state employees, who were members of the Employees Retirement System, retired. Overall, state employee full time equivalent positions declined from the FY 2008 final enacted level of 15,688.7 to 14,935.3 in the FY 2012 budget, a reduction of 753.7 positions. The FY 2013 enacted budget reversed this trend, with the addition of 91.3 FTE positions primarily in Human Service agencies to meet program needs in Health, Children Youth and Families, and the Office of Health and Human Services. In the FY 2013 revised budget, the Governor recommends an FTE level of 15,102.5, an increase of 76.2 FTE positions from the FY 2013 enacted budget. In the FY 2014 budget, the Governor recommends a further increase of 69.1 FTE positions from the FY 2013 revised budget, or 15,171.6 FTE positions.

Current Retiree Health Benefit Structure

In order to address the unfunded liability associated with retiree health benefits and reduce the ongoing cost to the taxpayer, eligibility requirements and co-share percentages for retiree health were modified in the 2008 session of the General Assembly. The new plan provided that employees retiring after October 1, 2008 would be eligible for retiree health coverage through the State if they are age 59 or over with a minimum of 20 years of service. For employees retiring before October 1, 2008, an employee with over 10 years of service as of July 1, 2005 was eligible for retirement with at least 28 years of service at any age, or at least 10 years of service and at least age 60, and was therefore eligible for retiree heath. For those employees with less than 10 years of service prior to July 1, 2005, the employee had to be age 59 with at least 29 years of service, age 65 with ten years of service, or age 55 with 20 years of service in order to be eligible for retirement and therefore also eligible for retiree health. The enacted reform modified the co-share percentage to require a 20 percent co-share on the full cost of the early retiree or post-65 plan in which the retiree is enrolled. For those retiring prior to October 1, 2008, the early retirees pay a co-share based on years of service on the active employee rate. For these employees retiring prior to October 1, 2008, who are over age 60 with at least 28 years of service, the state pays 100 percent of the cost of the plan.

Funding of Retiree Health Unfunded Liability

The Governor's recommended budget includes previously added provisions requiring that the State fund retiree health benefits on an actuarial basis and amortize the unfunded liability over a thirty year period. This funding mechanism will provide transparency with respect to the true cost of the benefit offered to state employees after employment. In compliance with GASB Statements 43 and 45, "Other Post Employment Benefits," in July 2007, the State obtained an actuarial estimate of the unfunded liability relating to retiree medical benefits. Pursuant to GASB Statement 45, "Other Post Employment Benefits" the State obtained an updated actuarial valuation of the unfunded liability relating to retiree medical benefits for the period ending June 20, 2009. The unfunded liability as of June 30, 2009 was determined to be approximately $774.7 million, including $673.6 million for State employees, $67.1 million for State Police, $11.8 million for Legislators, and $8.7 million for Judges, and $13.5 million for the State's share for teachers. This was calculated using an investment rate of return of 5.0 percent and assumes that future funding will be on an actuarial basis. The annual required contribution as a percentage of payroll in FY 2013 is budgeted at 6.86 percent, 33.18 percent, 46.35 percent and 7.19 percent (no rate for teachers), respectively. Prior to FY 2011, the State had not set aside any funds on an actuarial basis to address the unfunded retiree medical benefit liabilities. During the 2008 session of the General Assembly, in order to begin funding this unfunded liability, legislation was enacted that would require the State to fund on an actuarial basis and authorized creation of a trust fund for retiree medical benefit liabilities. During the 2009 Session of the General Assembly, this actuarial funding requirement was delayed until FY 2011.

Beginning with the first pay period of FY 2011, the state began providing the resources necessary to the OPEB trust fund to finance retiree health benefit costs on an actuarial basis, which will be used to pay current benefits and hold assets for investment.

Because a new actuarial study had not been completed at the time, the FY 2013 current services targets assumes that retiree health rates would remain the same as in the enacted FY 2013 budget. For FY 2014, the retiree health insurance rates reflect the valuation of the retiree health insurance fund as of June 30, 2011 issued by Gabriel, Roeder, and Smith (GRS) in May 2012. Retiree health is calculated on salaries of different categories of employees, including state employees, State Police, judges, and legislators. The rates also reflect a proposal from the Department of Administration's Office of Employee Benefits to implement a Medicare Exchange for post-65 retirees, where retirees choose between multiple Medicare supplemental plans from different insurers. The State will set up Health Reimbursement Accounts (HRAs) for retires in the state-sponsored health plans and deposit money each month into the account. The amount would be determined by the current level of subsidy the State provides, i.e. a 100 percent subsidized retiree would receive 100 percent of the maximum HRA amount, and an 80 percent subsidized retiree would receive 80 percent of the maximum HRA amount. Approximately 5,300 post-65 retirees currently receive subsidies and an additional 2,700 non-subsidized members are on the plan (spouses and public school teachers).

The Governor recommends total savings of $1.1 million, including $600,000 general revenue based on the more competitive rates available in the open market comparing the State's current plans with available plans in the Rhode Island market. Access to the exchange will provide retirees with additional choices and the ability to buy the plan that best fits their needs each year. The exchange will also provide, for the first time for retirees, access to Medicare Part D plans and access to $0 Medicare Advantage plans. A retiree may choose to purchase a lower cost supplemental plan and use the rest of the HRA funds to purchase a plan for a spouse, for dental or vision expenses, or for payment of the Medicare Part B premium.

Statewide Cost of Living Adjustment

Most current labor contracts expire June 30, 2012. Without a negotiated cost of living adjustment, no accommodation has been made in the FY 2014 Budget for any such increase.

Employee Medical Benefits

The FY 2013 enacted budget for health benefit costs was predicated upon a planning value of $16,956 based on a weighted average of the three cost components consisting of medical, dental, and vision rates for both individual and family plans. The currently active rates for FY 2013, which are the rates used in the revised FY 2013 budget, are revised to a new total of $16,821. This amount is $135, or approximately 0.8%, less than the rates used in the enacted budget.

Based on current and projected balances in the state's Health Insurance Fund, the Governor recommends a medical holiday in FY 2013. The state is self-insured for medical benefits and develops annual working rates based upon prior claims experience, adjusted for medical inflation. This fund is used to pay insurers for medical benefits for state employees. Revenue is generated by assessing state agencies on a bi-weekly basis and by co-shares from employees. In the event that there is a surplus, the balance may be used to reduce the working rates by not charging the state agencies for medical coverage for a particular pay period, known as a medical holiday. Employees paying a co-share based on a percentage of the premium cost are also not charged for the respective pay period. Employees paying a co-share based on a percentage of their pay are still charged. The Governor recommends a statewide reduction of 3.85 percent for medical insurance only.

For FY 2014, the budget instructions contained an estimated planning value equal to $18,433, an increase of 8.7 percent from the original FY 2013 enacted amount of $16,956. This is the increase upon which the statewide target adjustment was based. Subsequent to this, there were several items that are projected to result in savings in medical benefit costs. The first is based on the expectation that the year-over-year increase in costs for health insurance will be lower than assumed in the projections developed by the Budget Office in July 2012 for FY 2014. The Budget Office, based on national trend data and information provided by the state's health insurance provider, United Healthcare, assumed an increase of 10.0 percent in overall medical benefit rates in FY 2014 vs. FY 2013. Based on the surplus in the health insurance fund in FY 2013, the

Budget Office recommends lowering this growth projection from 10.0 percent to 5.8 percent. This is the equivalent of an additional one day medical holiday in FY 2014, although an actual holiday will not be taken; instead, the rates put in effect for FY 2014 will be lowered to match this new growth rate.

In addition, the Department of Administration's Office of Employee Benefits proposed two initiatives for FY 2014 that would result in overall savings in health insurance costs. The Governor recommends these proposals be adopted, which will result in overall savings of almost $2.2 million ($1.4 general revenue) to the fund. The two initiatives are:

- Eliminate health coverage for former spouses of State employees. The State currently covers 405 former spouses, at an annual costs approximately $2.86 million. Many of these former spouses have access to their own employer-sponsored health plan, but instead are on the state health plan because there is no cost to them or because the state health plan provides better coverage. With the creation of the RI Health Exchange, everyone will have access to health care coverage.

  The RI Health Exchange is expected to be operational on January 1, 2014 and will provide access to health coverage for all Rhode Islanders who do not have other coverage, regardless of preexisting conditions. Dependent on income, federal subsidies will be available through the Exchange to help Rhode Islanders pay for coverage.

  The FY 2014 Budget includes a proposal that the State no longer cover former spouses of State employees effective January 1, 2014. These individuals would either move to their own employer sponsored health plan or move to a plan under the RI Health Exchange. This proposal assumes six (6) months of savings or $1.43 million all funds, including $739,000 general revenue.

- Exclude Nexium as a covered prescription and replace with a generic equivalent. The FY 2014 Budget proposes to exclude the drug Nexium from its prescription formularies due to the availability of equivalent generic protein pump inhibitors available to treat the symptoms of heartburn effective July 1, 2013. This proposal is assumed to save $737,000 all funds, $382,000 general revenue.

Further identified savings come in the Dental Cost portion of Health Benefits. The State Employee Dental contract expires December 31, 2013. The contract provides for two one-year extensions. The original contract provided for a maximum increase of six percent (6.0%) in Calendar Year 2013. The contractor, Delta Dental, has offered to extend the contract with a three percent (3.0%) increase if the State expends the contract for the additional two years. The Department of Administration's Office of Employee Benefits proposes that the contract be extended for an additional two years with an increase of three percent (3.0%), as opposed to the six percent (6.0%) increase assumed in the current service projections developed by the Budget Office. The Governor recommends savings of $250,000 all funds, including $140,000 general revenue in FY 2014.

Full-Time Equivalent Positions (FTE)

The FY 2013 enacted budget contained 15,026.3 full-time equivalent (FTE) positions, including 776.2 FTE positions that are federal/sponsored research positions in Higher Education. In order to maintain an acceptable level of critical services and to address new program concerns, the Governor recommends 15,102.5 FTE positions in the revised FY 2013 budget, an increase of 76.2 FTE positions from the enacted level. In FY 2014, the Governor recommends a total FTE position level of 15,171.6, including 776.2 Higher Education federal/sponsored research positions, an increase of 69.1 FTE positions from the revised FY 2013 level and a 145.3 increase from the FY 2013 enacted level.

Personnel Summary

In **General Government**, the Governor recommends a net increase of 7.0 FTE positions in FY 2014 from the FY 2013 enacted budget. The largest decrease is in the Department of Labor & Training, where a reduction of 70.5 positions results from the end of Extended Benefits Unemployment Insurance federal funds. The Governor recommends a 40.5 FTE position increase in the Department of Administration due to program additions and adjustments in the Office of Digital Excellence (5.0), Human Resources (3.5), Planning (1.0), Purchasing (2.0), Capital Properties (1.0), Energy Resources (2.0) (from the Economic Development Council), Information Technology (8.6), and the Office of Management & Budget (2.4). Also in Administration, 15.0 positions are added to staff the Health Exchange. The Governor also recommends the addition of 34.0 FTE positions in the Department of Revenue, 31.0 in FY 2013 in the Lottery Division to supervise table gaming operations recently approved for the Twin River Casino; 2.0 in the Taxation Division related to the creation of a Special Investigation Unit to review and investigate alleged tax law violations; and 1.0 chief financial officer position in the Office of the Director. There are also increases of 1.0 FTE position in the General Treasurer (a legal counsel in the Retirement program), and 2.0 FTE positions in the Public Utilities Commission (1.0 in audits and 1.0 in the consumer unit to deal with utility shutoffs). There is also an increase in FY 2013 of 1.0 consumer affairs FTE position in the Department of Business Regulation's Insurance Regulation program for the Affordable Health Care Act. In FY 2014, the task will be performed through contract services.

In **Human Services**, the Governor recommends a net increase of 101.9 FTE positions in FY 2014 from the FY 2013 enacted FTE authorization. The Governor recommends the following increases:

- 40.2 FTE positions in the Department of Behavioral Healthcare, Development Disabilities, and Hospitals, due to the addition of 41.2 FTE positions to hire more full time employees and the recruit nurses, nursing assistants, attendants, cook's helpers, and community living aides, as well as to transfer a financial officer to the Executive Office Health and Human Services;
- 33.9 FTE positions in the Department of Human Services due to the addition of 6.0 in FY 2013 and 12.0 in FY 2014 limited term positions to implement the Unified Health Infrastructure Project (UHIP), the addition of 7.0 eligibility technicians in the Health Care Eligibility program, 6.0 social caseworker positions and 4.0 SNAP food stamp eligibility technicians in the Individual and Family Support program, and to transfer a financial officer to the Executive Office of Health and Human Services;
- 26.0 FTE positions in the Executive Office of Health and Human Services, 1.0 new position in FY 2013 to administer a supplemental program within the Aging and Disability Resource Centers (ARDC), transfer of 4.0 positions from other human service agencies and add 21.0 administrative staff positions.
- 5.0 FTE positions in the Department of Children, Youth and Families to add 6.0 FTE positions in FY 2013 funded from Race to the Top Early Childhood Learning and other grants, and to transfer a financial officer to the Executive Office of Health and Human Services;.

There is also a net reduction of 3.2 FTE positions in the Department of Health, with additional public health promotion specialists (5.0) offset by reductions in other positions in Central Management, Public Health Information, and Community and Family Health and Equity program, and the transfer of 1.0 associate director of finance position to the Executive Office of Health and Human Services.

Personnel Summary

In **Education**, the Governor recommends a net decrease of 3.6 FTE positions in FY 2014 from the FY 2013 enacted budget. This includes a net increase of 2.0 FTE positions in Elementary and Secondary Education in the Administration for Comprehensive Education Strategy (ACES) program. Public Higher Education includes an increase of 11.0 FTE positions, 1.0 new commissioner, 6.0 new faculty members and 1.0 criminologist position at the University of Rhode Island, and 2.0 new faculty members and 2.0 staff at Rhode Island College. There is also a reduction of 2.6 FTE positions in the Higher Education Assistance Authority. Finally, the Governor recommends a 14.0 FTE position reduction in the Public Telecommunications Authority due to the end of state funding for the agency.

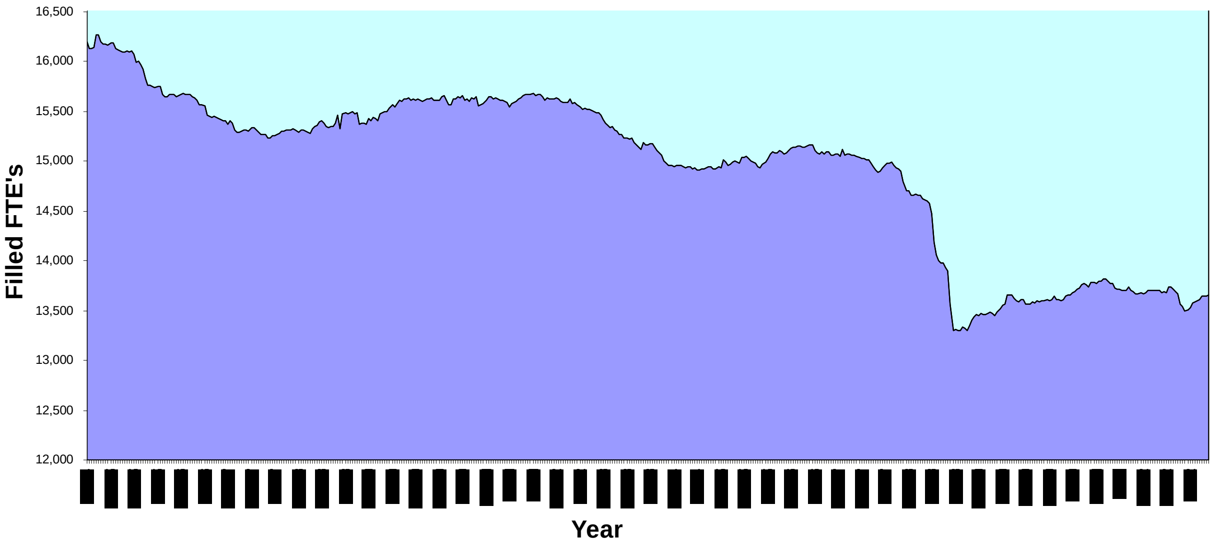
In **Public Safety**, there is a net increase of 47.0 FTE positions in FY 2014 from the FY 2013 enacted budget. The Governor recommends an additional 40.0 FTE positions the Department of Public Safety for the July 2013 State Trooper Academy class, as well as 1.0 public information officer and 1.0 paralegal. The Governor also recommends an increase of 5.0 FTE positions in the Military Staff, in the Emergency management program. These positions will act as coordinators and managers for the state's interoperability communication program, the incident management system, the critical infrastructure program, the domestic preparedness program, and all hazard planning.

In **Natural Resources**, there is a reduction of 8.0 FTE positions in FY 2013 and FY 2014. In FY 2014, there is a 1.0 FTE increase from the enacted budget due to the addition of a clerk position in the Bureau of Natural Resources.

In **Transportation**, the Governor recommends no change from the enacted levels of 772.6 FTE positions, in both FY 2013 and FY 2014.

As directed by the Governor, the overall filled FTE position level must be constrained through careful management by cabinet directors and other agency heads of existing and upcoming vacancies. Actual filled positions totaled 13,656.9 as of December 29, 2012, a 48.2 position decrease from the 13,705.1 filled position level as of January 14, 2012, and 1,425.9 below the 15,082.8 in July 2007. The filled level is 1,396.4 FTE positions less than the enacted cap of 15,026.3 FTE positions. Because of resource constraints, as reflected in the Governor's recommended turnover across most agencies, there are FTE positions in the roster that will not be filled in FY 2013 or FY 2014.

Personnel Summary

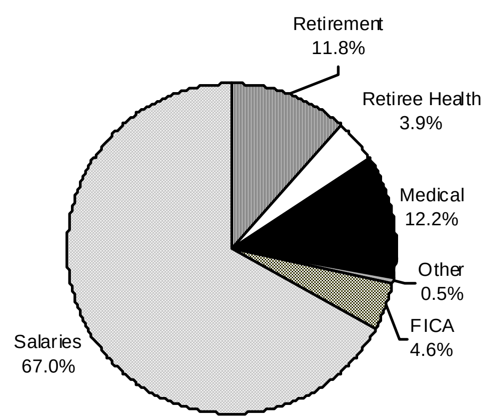


Salaries and Benefits

The largest category of personnel expenditures is for salaries and benefits. Salaries and benefits (including temporary and seasonal) represent $1,536.1 billion or 83.2 percent of total personnel costs. Salaries, including payroll accrual, overtime, holiday, and other salary-related items, equal $1.029.7 billion and fringe benefits equal $506.4 million. Fringe benefit payments include $181.2 million for retirement costs, $187.5 million for medical benefits (including $186.0 million for benefit plans and $1.5 million for medical benefits-salary disbursements), $59.9 million for retiree health benefits, $70.4 million for FICA, and $7.4 million for other benefits, including group life insurance and other contract stipends. In addition, the statewide benefit assessment is included to finance severance, unemployment, employee assistance, workers' compensation payments and administrative costs, and DLT employer assessments, and totals $32.0 million.

Direct Salaries increase by 3.2 percent in the FY 2013 Revised Budget over FY 2012 (audited expenditures), but increase by 1.2 percent in FY 2014 over FY 2013 revised. The FY 2013 budget includes no longevity increases for non-union personnel and for union personnel whose contracts end June 30, 2012, as these were abolished in the FY 2012 enacted budget.

FY 2014 Salaries and Benefits



Personnel Summary

Fringe benefit adjustments increase by 3.2 percent in FY 2013 revised over FY 2012 actual expenditure and increases by 4.5 percent in FY 2014 over FY 2013 enacted. **Retirement** increases by 6.2 percent from the enacted budget in FY 2014 and by 8.8 percent from the FY 2013 revised budget. This includes a one percent defined contribution addition of $6.5 million. Within state agency budgets, state employer retirement contributions are budgeted at 21.18 percent of payroll for FY 2013 enacted and revised, but at 23.05 percent in FY 2014. **FICA** decreases by 1.0 percent in FY 2014 from the enacted budget but increases by only 0.3 percent from the revised budget. **Retiree Health** increases by 9.3 percent in FY 2014 from the FY 2013 enacted budget. The rate remains at 6.86 percent in FY 2013 enacted and revised, and rises to 7.64 percent in FY 2014 for state employees.

The largest fringe benefit increase is in **medical benefits.** The FY 2013 revised budget of $174.3 million includes an overall increase of 8.8 percent over FY 2012 actual expenditure levels. For FY 2014, the recommendation of $187.5 million in medical benefits is an increase of 7.6 percent from the recommended revised budget amount for FY 2013. The increases include estimated reductions in FY 2013 due to a medical benefit holiday and changes in FY 2014 in estimated costs and program modifications.

Workers' compensation costs budgeted directly in the agencies in FY 2013 and FY 2014 are $231,492 and are funded in the Department of Corrections. These amounts reflect the continuation of wages in excess of those amounts received as a result of the Workers' Compensation statute (primarily as a result of assault cases). Since FY 2001, all workers' compensation costs, as well as unemployment insurance and unused leave severance payments, have been paid from a separate Assessed Fringe Benefits Administrative Fund. The fund is financed by a statewide benefit assessment of a fixed percentage of direct salaries that is charged to every department and agency in this document. The FY 2013 revised and FY 2014 budgets are 3.75 percent for regular state employees, no change from the enacted level. However, certain agencies and/or certain employee classifications are not assessed the full rate because they do not receive worker's compensation benefits. Also, certain higher education employees do not receive severance payments. The assessed fringe benefit rate is applied to all direct salaries, except overtime. Expenditures from the fund have grown from $31.1 million in FY 2008 to $43.1 million FY 2009, but decreased in FY 2010 to $28.8 million. The surge in severance payments was due to the large number of employees that retired prior to changes in retiree health benefit provisions, which became effective October 1, 2008. The FY 2013 revised budget is $31.7 million, an increase of 2.5 percent from FY 2012 actual expenditure. The budget in FY 2014 is $32.0 million, an increase of 0.8 percent from the revised recommendation.

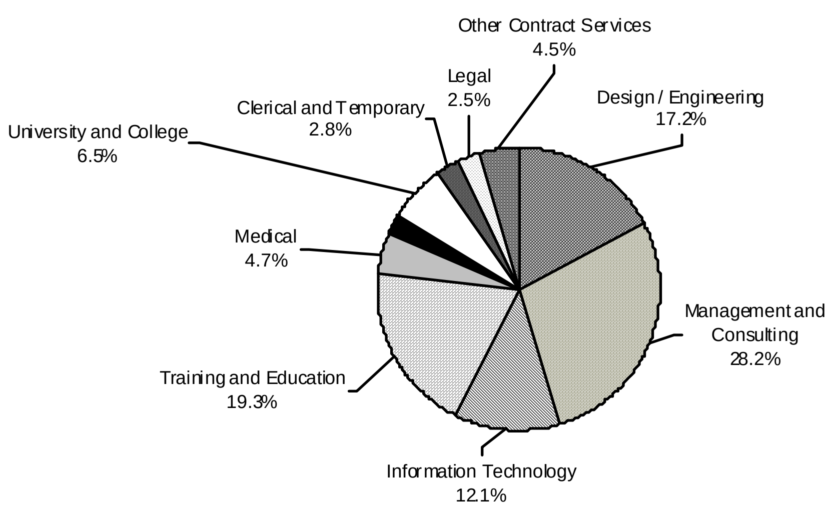
The Assessed Fringe Benefit Fund is used to fund the following: services provided by the Donley Center; services of the Workers' Compensation Court; the Division of Workers' Compensation administrative costs related to workers' compensation activities; workers' compensation benefit payments to employees; payments to workers' compensation providers; unemployment compensation payments; severance payments to employees for unused leave upon termination from state service; and Cornerstone Program administrative costs for the Flexible Health savings account.

Purchased Services

Purchased Services costs in the FY 2014 Budget total $277.7 million, and represent 15.0 percent of total personnel costs. Expenditures in this category are for services provided by outside contractors in cases where special expertise is needed or where it would be less effective to hire full-time employees. Major categories of expenditure are management and consulting services (comprising 28.2 percent of the total), design and engineering services (comprising 17.2 percent), training and education services (comprising 19.3 percent), and information technology services (12.1 percent).

Recommended expenditures in FY 2013 revised are $16.6 million more than FY 2013 enacted expenditures, a 6.0 percent increase in spending for services, including training and education services ($5.9 million), university/college services ($3.7 million), and information technology services ($15.8 million). A major portion of this increase is in the Health Benefits Exchange for the development of the web-based exchange that will be available to Rhode Islanders and Rhode Island businesses. Recommended expenditures in FY 2014 are $14.2 million less than FY 2013 revised. The greatest decreases are in training and education services. A major reason for the decline is the finalization of project work in FY 2013, particularly in the areas of university/college services, information technology and design and engineering services, and the policy goal to reduce contract employee services.

FY 2014 Purchased Services



For each department or agency of state government, the Budget volumes contain an agency summary of personnel costs. For each program, the Budget volumes display all positions and their respective costs. Footnotes will assist readers in understanding variances between the years. Additionally, there are a number of terms used that are not part of every day usage. A Glossary with extended explanations is included in the back of the Technical Appendix. For more information on the codes used to identify the pay scales, refer to the Glossary. Pay scales are provided on the State's Human Resources web site under the Compensation and Classification section.