

The Bondholder's Budget: Connecticut's Experiment in Tax and Expenditure Limits

Sam Whipple

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In 2017, Connecticut enacted new fiscal restrictions to cap state spending, revenue volatility, appropriations, and bonding, which were to be “locked” in bond covenants and enforced via *contract*. This marks a startling turn in state tax and expenditure limits (TEs). Peer states have statutory or constitutional guardrails on the budgeting process, but none hands such great control to the bondholders. Now, using the threat of a lawsuit, Connecticut's bondholders can block lawmakers from amending the fiscal caps as economic circumstances evolve over time. Far from a budgetary best practice, the fiscal restrictions are likely to impair Connecticut's long-term economic health. Accordingly, this Paper presents several strategies for safely exiting the “bond lock” covenants and restoring budgetary control to the General Assembly.

Table of Contents

- I. **Introduction: Connecticut’s Fiscal Report Card**..... 3
- II. **State TELs in Theory and Practice** 4
 - A. *TEL Typology*..... 5
 - B. *Economic Efficacy*..... 6
 - C. *TELEs as Democratic Distrust* 8
- III. **New Rules: The 2018 Budget Standoff**..... 10
 - A. *Four Budgetary Caps*..... 12
 - 1. Spending Cap..... 12
 - 2. Volatility Cap..... 13
 - 3. Appropriations Cap..... 15
 - 4. Bond Cap..... 16
 - B. *Locked in Place*..... 17
- IV. **Downstream Consequences** 20
 - A. *The Bond Cap “Drafting Error”: A Case Study in Fiscal Restrictions* 22
 - 1. Exercise the Emergency Clause 23
 - 2. Refund and Reissue the Bonds 24
 - 3. Pursue a Legislative or Judicial Remedy 24
 - B. *Interaction of the Spending, Volatility, and Appropriations Caps* 27
 - C. *Inefficient Budget-making* 30
 - D. *A Bondholders’ Lawsuit*..... 31
- V. **Removing the Fiscal Handcuffs**..... 33
 - A. *Pause or Repeal the Bond Lock*..... 33
 - B. *Account for Outstanding Bonds*..... 35
 - 1. Accommodating Current Bondholders 35
 - 2. Clearing the Covenants by Refunding..... 37
 - 3. Invalidating the Bond Lock..... 37
- VI. **Conclusion: A Roadmap for Responsible, Democratic Budgeting**..... 39

I. Introduction: Connecticut's Fiscal Report Card

As one of America's wealthiest states, Connecticut has long maintained a liberal model of social services. In recent years, however, the State has struggled to finance those commitments. Due to its reliance on the financial sector, Connecticut was among the most-affected states during the recession of 2008. Since then, personal income growth has fallen flat,¹ and employment has remained below its pre-recession peak.² State lawmakers, too, have felt the squeeze. After neglecting state pension funds for some seventy years, Connecticut faces an iceberg of unfunded liabilities, which has caused debt service to crowd out discretionary spending.³ By 2023, annual contributions to the State employees' and teachers' pension funds could top \$4 billion.⁴

In 2017, legislators tasked a private commission with finding recommendations to achieve fiscal stability and economic growth. Their final report⁵ played into a growing narrative that Connecticut required strict fiscal discipline to right the ship. This seeped into the legislature, too, which adopted a series of new budgetary controls. It implemented or revised four fiscal

¹ Ruth Mantell & Joe Fleming, *State Economic Growth Uneven Since Recession Began*, PEW (May 2, 2018), <https://www.pewtrusts.org/en/research-and-analysis/articles/2018/05/02/state-economic-growth-uneven-since-recession-began> (showing annual personal income growth at 0.6%—last in the nation).

² Keith M. Phaneuf, *Is Connecticut's Slowing Job Growth a Sign of Something Worse?*, CT MIRROR (Mar. 22, 2019), <https://ctmirror.org/2019/03/22/is-cts-slowng-job-growth-a-sign-of-something-worse> ("Connecticut is the only New England state that has not recovered all of the jobs it lost during the 2008–2010 recession. The latest numbers show it has regained 81 percent of the 120,000 positions lost during that time."). This is attributable to shrinking public-sector employment. Private-sector employment has fully recovered from the recession, but it has not added enough jobs to offset the public-sector losses. *Id.*

³ Keith M. Phaneuf, *Pension Debt Stands Between Lamont and Fiscal Stability for CT*, CT MIRROR (Feb. 15, 2019), <https://ctmirror.org/2019/02/15/pension-debt-stands-between-lamont-and-fiscal-stability-for-ct> (noting that debt costs have risen from about 10% of the General Fund in 2000, to nearly 33% in 2019).

⁴ Marc E. Fitch, *Connecticut Law Requires Full Funding of Pensions, SEBAC Overrode It*, YANKEE INST. (Sept. 26, 2018), <https://yankeeinstitute.org/2018/09/26/connecticut-law-requires-full-funding-of-pensions-sebac-overrode-it>. By comparison, combined payments to those funds were about \$1.3 billion as of 2010. *Id.*

⁵ Robert Patricelli & James Smith, *Final Report*, CONN. COMMISSION ON FISCAL STABILITY AND ECON. GROWTH (Mar. 2018), available at <https://ctrising.org/the-report> (click link to download Report 1.0).

“caps,” and it required that the State contract with bondholders to leave the caps *unchanged* through 2023. That contract—known as the “bond lock”—marks a startling turn in state budgeting controls. Rather than making the structural changes necessary to ensure responsible budgeting, Connecticut tied its hands to rigid rules, ill-suited in an evolving economy. Contrary to Wall Street’s initial optimism,⁶ the bond lock will carry long-term consequences for the State. After forecasting those eventualities, this Paper presents three options for safely exiting the covenants. Prompt action is imperative, before the bond lock further damages Connecticut’s fiscal standing.

II. State TELs in Theory and Practice

State-level tax and expenditure limitations (TELs) emerged during the 1970s taxpayer revolt and gained popularity when the economy slowed in the early 1990s.⁷ Two of the better-known examples are California’s Proposition Thirteen⁸ and Colorado’s Taxpayer Bill of Rights (TABOR).⁹ While the precise mechanisms vary among states, TELs generally aim to restrict the growth of government revenue or expenditures. One common TEL approach is to limit year-over-year changes to some fixed percentage, calculated from the inflation rate or the growth in

⁶ See *infra* notes 102-103 and accompanying text.

⁷ *The State of State (and Local) Tax Policy: What Are Tax and Expenditure Limits?*, TAX POL’Y CTR. 2 (2018), https://www.taxpolicycenter.org/sites/default/files/briefing-book/what_are_tax_and_expenditure_limits.pdf.

⁸ Adopted via ballot initiative in 1978, California’s Proposition Thirteen limits year-over-year increases in taxable property value to just two percent, even if the market value exceeds that rate. Liam Dillon, *Proposition 13 has Strictly Limited Property Tax Increases since 1978. Voters Could Get a Chance to Change That*, L.A. TIMES (Oct. 17, 2018), <https://www.latimes.com/politics/la-pol-ca-prop-13-changes-20181017-story.html>.

⁹ Colorado’s TABOR sets a formula to cap the government’s allowable tax revenue, based on population growth and inflation, and requires that any excess revenue be refunded to the citizens. Voters approved it as a constitutional amendment in 1992. Anna Staver, *TABOR FAQ: Colorado’s Taxpayer Bill of Rights Explained*, DENVER POST (June 21, 2019, 1:16 PM), <https://www.denverpost.com/2019/06/20/tabor-colorado-taxpayer-bill-of-rights>.

personal income.¹⁰ Over half the states now utilize TELs for revenue, spending, or both.¹¹ They operate in addition to balanced-budget requirements, which exist in every state but Vermont.¹²

Connecticut had one TEL in place prior to 2017: a constitutional spending cap dating to 1992.¹³ Connecticut is the first, however, to enforce TELs via state bond covenants. This decision to experiment with TEL design is ill-advised in light of the academic and policy literature. Connecticut's move more likely reflects a distrust in democratic budget-making, rather than a genuine attempt to boost long-term economic health.

A. *TEL Typology*

TEL design varies significantly across the states. When drawing comparisons, researchers look to a few distinguishing variables: the method of adoption, the activities limited, the indexing measure, and the stringency of waiver requirements.¹⁴ On these metrics, Connecticut's new TELs are more restrictive than average.

First, Connecticut's newest TELs were enacted by statute, not by constitutional referendum. This statutory route is the more common method of adoption;¹⁵ but in Connecticut's case, it limited the opportunity for public discourse. In fact, legislators passed the

¹⁰ *The State of State (and Local) Tax Policy*, *supra* note 7, at 1.

¹¹ Elizabeth McNichol, *Impact of Connecticut's Constitutional Spending Cap on Connecticut's Future*, CTR. ON BUDGET & POL'Y PRIORITIES 1 (Dec. 13, 2018), <http://www.ctvoices.org/sites/default/files/LMN%20CBPP.pdf> (presented at the 2018 Connecticut Voices for Children Budget Forum).

¹² *Policy Basics: The ABCs of State Budgets*, CTR. ON BUDGET & POL'Y PRIORITIES (Feb. 7, 2013), <https://www.cbpp.org/sites/default/files/atoms/files/PolicyBasics-StateBudgets.pdf>.

¹³ Conn. Const. amend. XXVIII (adopted November 25, 1992).

¹⁴ Sharon N. Kioko & Christine R. Martell, *Impact of State-Level Tax and Expenditure Limits (TELs) on Government Revenues and Aid to Local Governments*, 40 PUB. FIN. REV. 736 (2012); Thad Kousser et al., *For Whom the TEL Tolls: Can State Tax and Expenditure Limits Effectively Reduce Spending?*, 8 ST. POLITICS & POL'Y Q. 331 (Winter 2008); Tucker Staley, *The Effect of TELs on State Revenue Volatility: Evidence from the American States*, PUB. BUDGETING & FIN. 29, 31 (Spring 2015).

¹⁵ *The State of State (and Local) Tax Policy*, *supra* note 7, at 2.

new TELs without a public hearing, during a special legislative session.¹⁶ Second, Connecticut’s TELs limit a broad range of budgetary decisions beyond taxing and spending—including bonding and appropriations. They still fall short of the nation’s most stringent TELs, since Connecticut’s do not require that excess revenues be refunded to the taxpayers;¹⁷ instead, they are swept into the “rainy day fund.” Next, Connecticut’s indexing measure is average, since it incorporates personal income growth and not only inflation.¹⁸

On the waiver requirements, Connecticut’s TELs are true outliers. In other states, TELs are considered “stringent” if they require a legislative supermajority or popular vote to override.¹⁹ Connecticut’s caps require a three-fifths supermajority *and* an emergency declaration by the Governor, all backed by the threat of a bondholder lawsuit.²⁰

B. Economic Efficacy

The economic scholarship on state TELs is mixed, at best. When properly designed, TELs can be effective at limiting the size of state government—albeit at the cost of discretionary spending, such as social services, education, and municipal aid. Due to those cutbacks, there is less evidence to link TELs with improvements to a state’s long-term economic health.

¹⁶ The budget deal (containing the four fiscal caps and the bond lock statute) passed in October 2017. The only public hearing occurred months later, in March 2018, and concerned whether to *delay* the effective date of the already-enacted bond lock law. See *infra* note 105 and accompanying text.

¹⁷ *The State of State (and Local) Tax Policy*, *supra* note 7, at 1 (describing TELs in Colorado and Oregon with mandatory refund provisions).

¹⁸ See *infra* Section III.A.1 (for the spending cap’s indexing measure); Section III.A.2 (for the volatility cap’s indexing measure).

¹⁹ Staley, *supra* note 14, at 31.

²⁰ For full discussion, see *infra* Section IV.D.

To the first point, later studies (conducted after the wave of state TELs in the early 1990s) mostly agree that TELs are effective in restricting taxes and spending.²¹ One study examined the stricter category of TELs—those requiring a supermajority legislative vote or a popular referendum to exceed spending limits, as in Colorado’s TABOR—and associated them with a 2% reduction in state spending.²² Generalizing across states is difficult, though, given the varying design features. Where TELs limit specific types of revenue—for example, the property tax, as in California’s Proposition Thirteen—states become increasingly reliant on other non-capped revenue streams.²³ Furthermore, where TELs are too stringent for policymakers to adapt with changing economies over time, revenue volatility can *increase*.²⁴ And where TELs fail to account for changes in the state/local funding share, costs can shift between those levels of government.²⁵

Even under an optimal TEL that avoids those side effects, the reduction in state taxing and spending is unlikely to promote long-term economic growth. The empirical literature consistently finds no positive relationship²⁶—which can be explained by the squeeze on state

²¹ Megan Randall & Kim Reuben, *Sustainable Budgeting in the States: Evidence on State Budget Institutions and Practices*, URBAN INST. 59-61 (Nov. 2017), https://www.urban.org/sites/default/files/publication/93461/sustainable-budgeting-in-the-states_2.pdf (reviewing literature on the fiscal efficacy of state TELs). Data constraints limited the conclusiveness of earlier studies, which had looked only at the 1970s wave. *Id.*

²² *Id.* at 59-60 (citing Kim Rueben, *Tax Limitations and Government Growth: The Effect of State Tax and Expenditure Limits on State and Local Government*, PUB. POL’Y INST. CAL. (1996)).

²³ *Id.* at 61 (citing Mark Haveman & Terri A. Sexton, *Property Tax Assessment Limits: Lessons from Thirty Years of Experience*, LINCOLN INST. LAND POL’Y (2008), https://www.lincolninst.edu/sites/default/files/pubfiles/property-tax-assessment-limits-full_0.pdf).

²⁴ Staley, *supra* note 14, at 29.

²⁵ Kioko & Martell, *supra* note 14; Bert Waisanen, *State Tax and Expenditure Limits*, NAT’L CONF. OF STATE LEGIS. (2010), <http://www.ncsl.org/research/fiscal-policy/state-tax-and-expenditure-limits-2010.aspx>.

²⁶ Randall & Reuben, *supra* note 21, at 60 (citing Suho Bae et al., *Economic Effects of State-Level Tax and Expenditure Limitations*, 72 PUB. ADMIN. REV. 649 (2012); A.L. Campbell & M.W. Sances, *State Fiscal Policy during the Great Recession: Budgetary Impacts and Policy Responses*, 650 ANNALS AM. ACAD. POL. & SOC. SCI. 252 (2013); Therese J. McGuire & Kim S. Rueben, *The Colorado Revenue Limit: The Economic Effects of TABOR*, 40 STATE TAX NOTES 459 (2006); James M. Poterba & Kim Rueben, *Fiscal News, State Budget Rules, and Tax-Exempt Bond Yields*, 50 J. URBAN ECON. 537 (2001)).

spending. Discretionary categories face the brunt of budget cuts, affecting education, municipal aid, and human services.²⁷ This is particularly problematic in a state like Connecticut, which depends heavily on human capital and has traditionally employed a robust public sector. If Connecticut's new TELs force a continued contraction in state employment and social investment, they could prove to be a drag on the economy.

C. TELs as Democratic Distrust

TELs are not constructed in a vacuum. They are the products of distinct political moments, often involving deep economic uncertainty. This was true during the 1970s and 1990s waves of TEL adoption, and it held equally true for Connecticut. Accordingly, TELs are best seen not as the paramount of sound budgeting, but as a pronouncement of distrust in the legislature.

A 2005 study by Irene Rubin bolsters this view, concluding that state TELs have more to do with political currents and electoral institutions than with the level of state taxation.²⁸ For example, Colorado's state tax burden was comparatively low when voters approved TABOR in 1992, the most rigid state TEL at the time.²⁹ The dispositive factor there was the ease of initiating a ballot issue, even without a groundswell of public opinion. An open process, as in Colorado, can be "hijacked by a few determined wealthy companies or interest groups."³⁰

²⁷ Rachel Silbermann, Sam Whipple & Jamie Mills, *Connecticut's Radical New Budget Rules: Locking in Decreased Investment in our State for the Next Decade*, CONN. VOICES FOR CHILDREN 10-12 (Mar. 2019) <http://www.ctvoices.org/sites/default/files/b19CTBudgetRules.pdf>.

²⁸ Irene Rubin, *The State of State Budget Research*, 25 PUB. BUDGETING & FIN. 46, 50-51 (2005).

²⁹ *Id.* (describing TABOR's unique refund requirement, whereby excess revenue must be returned to the taxpayers).

³⁰ *Id.* at 51.

In many ways, this narrative fits the facts in Connecticut. There was growing economic unrest and a general distrust in the outgoing administration; but it fell far short of a taxpayer revolt. In fact, the new TELs originated *entirely* in the legislature, and they never went to the voters for input or approval. Within those chambers, the Commission on Fiscal Stability and Economic Growth had dominated the discourse, declaring in its final report:

State government's *fiscal instability* is itself a root cause of our poor economic growth because it leads to a lack of confidence by the business community and among state residents. Re-igniting economic growth requires Connecticut to *regain fiscal stability*.³¹

This closely mirrored a narrative from the Connecticut Business and Industry Association: that Connecticut's woes stemmed from an uncontrolled spending problem among legislators. In their view, "That rate of spending growth has fed a cycle of budget deficits followed by tax hikes followed by more budget deficits, hampering the state's post-recession economic recovery as *fiscal instability* clouds private sector investment and job creation."³²

With new backing from the Commission, the idea stuck. To that divided legislature, TELs likely appeared the easiest way to "regain fiscal stability." Nonetheless, tying the chambers' hands was a profound statement of distrust in the democratic budget-making process.³³ With this lens, one can better anticipate the effects of Connecticut's new TELs.

³¹ Patricelli & Smith, *supra* note 5, at 6 (emphasis added).

³² FIXING CONNECTICUT'S FISCAL PROBLEMS: SPENDING REFORMS, LONG-TERM SOLUTIONS, BEST PRACTICES, CONN. BUS. & INDUS. ASS'N 2 (2017), available at https://www.cbia.com/wp-content/uploads/2017/05/Fix-CT-Spending_0517.pdf (emphasis added).

³³ Alex Knopp, Opinion, *Six Reasons to Repeal the 'Doomsday Bond Covenant'*, CT NEWS JUNKIE (Feb. 2, 2018), https://www.ctnewsjunkie.com/archives/entry/20180202_op-ed_six_reasons_to_repeal_the_doomsday_bond_covenant.

III. New Rules: The 2018 Budget Standoff

Connecticut's budget battle for Fiscal Year 2018 was the longest in State history.³⁴ Lawmakers faced the daunting challenge of closing a \$3.5 billion forecast deficit over the biennium.³⁵ With an 18-18 tie between Democrats and Republicans in the Senate—and only a narrow Democratic margin in the House—legislators failed to adopt a budget by June, when the official legislative session adjourned.³⁶ In Special Session, they finally passed a *Republican* budget on September 16, 2017, when a handful of fiscally conservative Democrats voted with the GOP bloc.³⁷ Democratic Governor Dan Malloy vetoed it on September 28,³⁸ sending legislators into bipartisan negotiations.³⁹ In the interim, the State ran for 123 days without a budget⁴⁰—operating instead on executive order, per the Governor's emergency powers.⁴¹ That declaration pertained solely to spending; and without any new revenue to balance the budget, only bare-bones appropriations could be authorized. Accordingly, to retain key government services, the

³⁴ Fiscal Year 2018 commenced on July 1, 2017, and ended on June 30, 2018. From July to October 2017, there was no budget in effect. Daniela Altimari & Christopher Keating, *Veto Prolongs Connecticut's Longest Budget Stalemate Ever*, GOVERNING (Oct. 2, 2017, 10:25 AM), <https://www.governing.com/topics/finance/tns-malloy-budget-veto-connecticut.html>.

³⁵ *Id.*

³⁶ Keith M. Phaneuf, *Malloy Prepares CT for Life Without a New State Budget*, CT MIRROR (June 30, 2017), <https://ctmirror.org/2017/06/30/malloy-prepares-ct-for-life-without-a-new-state-budget>.

³⁷ Christopher Keating, *State Budget in Chaos as Key Democrats Bolt for GOP, Malloy Vows Veto*, HARTFORD COURANT (Sept. 16, 2017, 12:25 PM), <https://www.courant.com/politics/hc-pol-budget-vote-again-friday-20170915-story.html>.

³⁸ Office of the Governor, *Veto Message for Pub. Act No. 17-1* (Sept. 28, 2017), available at <https://portal.ct.gov/-/media/7E66E95D3D9A4843A42B0F6B42769259.pdf>.

³⁹ Daniela Altimari & Christopher Keating, *As Talks Continue, Malloy Vetoes GOP-Backed Budget Bill*, HARTFORD COURANT (Sept. 28, 2017, 5:30 PM), <https://www.courant.com/politics/hc-pol-malloy-possible-veto-20170928-story.html>.

⁴⁰ Isabel Bysewicz, *Malloy Ends Historic Budget Impasse*, YALE DAILY NEWS (Nov. 3, 2017, 1:53 AM), <https://yaledailynews.com/blog/2017/11/03/malloy-ends-historic-budget-impasse>.

⁴¹ Governor Malloy's executive order cited the "Vesting" and "Take care" clauses of the Connecticut Constitution (Article 4, Sections 5 and 12 respectively), as well as his power under Section 3-1 of the General Statutes to "take any proper action concerning any matter involving the enforcement of the laws of the state and the protection of its citizens." See Exec. Order No. 58 (June 30, 2017), available at <https://portal.ct.gov/-/media/C28A235895764639AA819BFBABAE575B1D.pdf>.

executive order entailed steep cuts to education and social services.⁴² Further cuts loomed if a budget deal could not be reached: “About 85 communities would see their education cost sharing grants, the biggest source of state funding for public education in Connecticut, cut to zero in October.”⁴³ The legislature ultimately ended the stalemate on October 26, 2017, acting with veto-proof, bipartisan majorities.⁴⁴ Their new two-year budget deal⁴⁵ had been drafted independently from the Governor.⁴⁶

Underlying this budget impasse was a deep concern for the State’s unfunded liabilities. The Republican budget had sought to cut spending and alter State pension plans, in order to “avert[] the much deeper cuts Malloy must impose in the absence of any adopted spending plan.”⁴⁷ In his veto message, Governor Malloy had responded that the budget was “unbalanced, unsustainable, and unwise.”⁴⁸ Accordingly, in the bipartisan negotiations, legislators sought strict fiscal discipline. Their final bill defined four budgetary caps—on spending, volatility, appropriations, and bonding—which were to be “locked” into the State’s bond covenants, limiting the legislature’s ability to revisit them.⁴⁹

This “locking” mechanism is unique among state TELs, as it added a *contractual* layer atop the constitutional and statutory caps. For each bond issued over a specified period, the State

⁴² Keith M. Phaneuf & Mark Pazniokas, *Malloy Vetoes Budget, Seeks ‘Honest Dialogue,’* CT MIRROR (Sept. 28, 2017), <https://ctmirror.org/2017/09/28/malloy-vetoes-budget>.

⁴³ *Id.*

⁴⁴ Bysiewicz, *supra* note 40.

⁴⁵ Pub. Act No. 17-2 [hereinafter 2017 Budget Implementer].

⁴⁶ Bysiewicz, *supra* note 40 (“In the past few weeks, top lawmakers have largely excluded Malloy from negotiations.”).

⁴⁷ Phaneuf & Pazniokas, *supra* note 42.

⁴⁸ *Id.* (quoting Governor Malloy’s veto message).

⁴⁹ Pub. Act No. 17-2 [2017 Budget Implementer] §§ 709 (the spending cap), 704 (the volatility cap), 705 (the appropriations cap), 712 (the bond cap), 706 (the bond lock).

was to pledge—in the bond covenant—that it would not alter any of the budgetary caps.⁵⁰ That provision, known as the “bond lock,” is the primary focus of this Paper. First, a brief overview of the four caps is required.

A. *Four Budgetary Caps*

1. Spending Cap

In 1992—shortly following the passage of a new State income tax—Connecticut voters adopted a twofold constitutional spending cap, approved by referendum as the Twenty-Eighth Amendment.⁵¹ The spending cap contained a balanced budget requirement and a limitation on year-over-year increases in general budget expenditures.⁵² Spending increases would be capped at the greater of either the five-year average growth in personal income or the inflation rate.⁵³ The legislature, however, was to define key terms in the calculation.⁵⁴ It took them twenty-five years to do so—up until the 2017 budget deal.⁵⁵ In the interim, prior *statutory* spending caps had governed, per an Attorney General opinion.⁵⁶ By finally adopting legislative definitions, the 2017 budget implementer gave the spending cap full constitutional force.⁵⁷ The term “general budget expenditures” now sweeps in most appropriated funds—including grants to distressed municipalities, which were formerly excluded from the statutory cap.⁵⁸ Bond payments,

⁵⁰ *Id.* § 706 (introducing a ten-year bond lock). *But see infra* note 88 (clarifying that before this provision went into effect, legislators reduced the bond lock to a five-year formulation).

⁵¹ Conn. Const. amend. XXVIII.

⁵² Stan McMillen et al., *Connecticut’s Spending Cap: Its History and an Alternative Spending Growth Rule*, U. CONN. CTR. FOR ECON. ANALYSIS 1 (Sept. 2005), <https://webshare.business.uconn.edu/ccea/studies/Connecticut's-Spending-Cap-History-Alternative-Spending-Growth-Rule.pdf>.

⁵³ *Id.*

⁵⁴ CONN. CONST. amend. XXVIII. (“The general assembly shall by law define ‘increase in personal income,’ ‘increase in inflation’ and ‘general budget expenditures’ for the purposes of this section. . .”).

⁵⁵ Silbermann, Whipple & Mills, *supra* note 27, at 3.

⁵⁶ McMillen et al., *supra* note 52, at 2.

⁵⁷ Silbermann, Whipple & Mills, *supra* note 27, at 3.

⁵⁸ *Id.*

expenditures on court orders, and payments into State pension funds are a few categories that the legislature chose to exclude from its new definition, for purposes of the constitutional cap.⁵⁹

To exceed the constitutional spending cap, the Amendment prescribes a single method: first, the Governor must “declare[] an emergency or the existence of extraordinary circumstances,” then the legislature must vote by a three-fifths majority to exceed the cap.⁶⁰ The legislature is free to amend the definitional language passed in 2017; but this too requires a three-fifths majority, per the terms of the Amendment.⁶¹ Thus, Connecticut’s allowable spending growth was limited to about 2% annually for 2018 and 2019.⁶²

2. Volatility Cap

Legislators first approved a volatility cap in 2015, which was set to take effect in 2021.⁶³ The 2017 budget implementer accelerated that date and also revised its mechanics.⁶⁴ Former State Comptroller Kevin Lembo backed the original 2015 cap in order to stabilize major revenue streams that were widely recognized as volatile.⁶⁵ Though all revenue sources rise and fall with the business cycle, Connecticut’s were particularly unreliable given the State’s dependence on

⁵⁹ *Id.* Payments into the State Employee Retirement System (SERS) are excluded from the definition of “general budget expenditures” only through 2022, and payments into the Teacher’s Retirement System (TRS) are excluded only through 2026. This left lawmakers with a short window to shore up the pension funding ratios, without crowding out other general spending. *See id.*

⁶⁰ CONN. CONST. amend. XXVIII.

⁶¹ *Id.* (“The enactment or amendment of such definitions shall require the vote of three-fifths of the members of each house of the general assembly.”).

⁶² McNichol, *supra* note 11, at 5. Since Connecticut’s personal income growth has lagged, *see* Mantell & Fleming, *supra* note 1, the spending cap grew at the U.S. inflation rate of about 2%.

⁶³ Pub. Act No. 15-244, § 164. The delayed effective date was desirable because it left time to study and revise the cap. Another possible consideration was to ensure that the initial calculation of the volatility threshold (which used a ten-year look-back on revenue streams) would not be skewed by outlier data from the Great Recession.

⁶⁴ Silbermann, Whipple & Mills, *supra* note 27, at 5.

⁶⁵ Kevin Lembo, *Stabilizing Connecticut’s Revenue Stream with the Budget Reserve Fund*, OFF. ST. COMPTROLLER, https://osc.ct.gov/brf/docs/BudgetReserveFund_policybrief.pdf.

capital gains and corporate taxes.⁶⁶ Thus, the proposal sought to ensure that legislators would not rely on one-time surges (or “revenue windfalls”) for general budgeting. Instead, the cap would automatically deposit excess revenue into the Budget Reserve Fund (BRF, or “rainy day fund”), where they were to be saved in order to offset future shortfalls.⁶⁷ The 2015 proposal used a ten-year look-back on volatile revenue sources (adjusted for normal revenue growth) to set the threshold for “excess” revenue, with any remainder being automatically deposited.⁶⁸

Ultimately, Lembo’s 2015 volatility cap never went into effect. Instead, the 2017 budget implementer created a new volatility cap, effective on passage.⁶⁹ That cap set a precise revenue threshold—\$3.15 billion—indexed to a five-year average of income growth.⁷⁰ Though the threshold originally covered only the “estimates and finals” portion of the personal income tax,⁷¹ legislators amended it to sweep in an additional revenue source, the affected business entity tax.⁷²

Critics argue that the threshold is set too low—prompting “rainy day” deposits even in years with a forecast deficit.⁷³ Over time, they anticipate that the indexing mechanism will cause “normal” revenue growth to be captured as “volatile,” and thus sequestered from the general budget.⁷⁴ The 2018 budget implementer sets forth one path to amending the threshold: the

⁶⁶ *Id.* at 3 (noting that capital gains dropped 60% in 2009, “contributing to a significant decline in . . . revenue of \$904 million.”).

⁶⁷ *Id.* at 1.

⁶⁸ *Id.* at 9.

⁶⁹ Pub. Act No. 17-2 [2017 budget implementer] § 704.

⁷⁰ *Id.* The five-year indexing was added in the 2018 budget implementer, Pub. Act No. 18-81 [hereinafter 2018 budget implementer].

⁷¹ “Estimates and finals” refers to personal-income tax paid in quarterly increments by earners who do not participate in ordinary paycheck withholding. It consists of small business income and capital gains, and it is known to be an especially volatile revenue stream. See Christine Stuart, ‘Over-Performing’ Revenue Sources Help CT End Fiscal Year with Surplus, MIDDLETOWN PRESS (July 1, 2019, 4:04 PM), <https://www.middletownpress.com/middletown/article/Over-performing-revenue-sources-help-CT-end-14064624.php>.

⁷² Pub. Act No. 18-49, § 7.

⁷³ Silbermann, Whipple & Mills, *supra* note 27, at 5-6.

⁷⁴ *Id.* Full discussion of these criticisms occurs in Section IV.B, *infra*.

legislature may obtain a three-fifths vote to raise (or lower) the dollar amount, “due to changes in state or federal tax law or policy or significant adjustments to economic growth or tax collections.”⁷⁵ Absent such a vote, the \$3.15 billion threshold for volatile income is in force.

3. Appropriations Cap

The appropriations cap first appeared in the 2017 budget implementer, with a delayed effective date of July 2019.⁷⁶ Its goal is to ensure that the legislature does not appropriate every last dollar of anticipated revenue. To that end, the cap limits authorized appropriations to a fixed percentage of total estimated revenues.⁷⁷ Beginning in fiscal year 2020, the legislature only may appropriate 99.5% of estimated revenues. Thereafter, the percentage drops steadily until fiscal year 2026, when it settles at 98%.⁷⁸

The statute includes similar exit options for exceeding the appropriations cap. The Governor must “declare[] an emergency or the existence of extraordinary circumstances,” and secure a three-fifths vote of the legislature.⁷⁹ This functions *only* for the fiscal year in progress.⁸⁰ For the purposes of enacting an adjusted appropriation and revenue plan, however, a simple majority vote of the legislature suffices to exceed the cap for the fiscal year in question.⁸¹

⁷⁵ Pub. Act No. 18-81 [2018 budget implementer] § 20(a)(2).

⁷⁶ Pub. Act No. 17-2 [2017 budget implementer] § 705.

⁷⁷ Revenue estimates are required in each state budget under Section 2-35(b) of the General Statutes. “The state budget act passed by the legislature for funding the expenses of operations of the state government in the ensuing biennium shall contain a statement of estimated revenue, based upon the most recent consensus revenue estimate or the revised consensus revenue estimate issued pursuant to section 2-36c, itemized by major source, for each appropriated fund, and supplied by the joint standing committee of the General Assembly having cognizance of matters relating to state finance, revenue and bonding.”

⁷⁸ Pub. Act No. 17-2 [2017 budget implementer] § 705(a).

⁷⁹ *Id.* § 705(b)(1)(A).

⁸⁰ *Id.* § 705(b)(1)(B).

⁸¹ *Id.* § 705(b)(2).

4. Bond Cap

The bond cap is a new, hard limit on the Treasurer’s ability to *issue* General Obligation (GO) and credit revenue bonds.⁸² As of July 2018, the Treasurer may not issue more than \$1.9 billion of such bonds in a single fiscal year; going forward, that amount is indexed to the CPI.⁸³ Governor Lamont, however, has pledged to adhere to an even stricter standard through a voluntary “debt diet” that will control rising interest costs.⁸⁴

There are additional, preexisting constraints that apply earlier in the bonding process. Before a bond is issued in Connecticut, it first must be *authorized* by legislation and *allocated* to projects and programs by the State Bond Commission (SBC).⁸⁵ The process is a funnel: not everything authorized will pass the SBC, and not everything allocated will be issued by the Treasurer. The initial constraint—which long predates the new bond cap—applies to the authorization stage, limiting the State’s total indebtedness at any given time to 160% of General Fund tax receipts for the fiscal year in progress.⁸⁶ Above that balance, the legislature is still forbidden from authorizing any further bonding. The new bond cap is an additional layer of protection. It applies later, capping bond *issuances* at \$1.9 billion per fiscal year.

⁸² *Id.* § 712(f)

⁸³ *Id.*

⁸⁴ Christine Stuart, *Lamont Wants to Put Connecticut on ‘Debt Diet,’* CT NEWS JUNKIE (Feb. 12, 2019, 10:33 AM), https://www.ctnewsjunkie.com/archives/entry/20190212_lamont_wants_to_put_connecticut_on_debt_diet.

⁸⁵ Letter from Steven Kitowicz, Principal Budget Specialist, Office of Policy & Mgmt., to Jamie Mills, Dir. of Fiscal Policy & Econ. Inclusion, Conn. Voices for Children (on file with author).

⁸⁶ Conn. Gen. Stat. § 3-21(a). The aggregate indebtedness limit dates to 1957. Pub. Act No. 57-640. In 1991, it was reduced to 160% of fiscal year tax receipts (from an original 450%). Pub. Act No. 91-3. Forty states limit the amount of aggregate debt; as with TELs, the policy design (including calculation methods, exempted borrowing categories, and exit options) varies significantly among states. Reuben & Randall, *supra* note 21, at 51-53.

B. Locked in Place

The bond lock, first appearing in the 2017 budget implementer, adds a contractual reinforcement to the four caps. It requires by statute that the Treasurer include a pledge (or “covenant”) in State bonds issued during the twenty-five month period between May 15, 2018, and July 1, 2020, which establishes a *moratorium on new legislation affecting the caps*.⁸⁷ Specifically, those bondholders are promised that no legislation taking effect between May 15, 2018, and July 1, 2023, can amend the four caps or change the State’s obligation to comply.⁸⁸ Thus, “[u]ntil 2023—or at least until all bonds containing the covenant are repaid fully—the four caps must remain in effect, exactly as they existed on May 15, 2018.”⁸⁹

The bond lock itself contains two exit options, modeled on analogous language found in several of the statutory caps. To suspend the bond lock and alter the underlying caps at will, the legislature can either (1) provide “adequate . . . protection [for] the holders of such bonds,”⁹⁰ or (2) follow the fiscal emergency procedure (i.e., “the Governor declares an emergency or the existence of extraordinary circumstances” followed by a three-fifths vote of the legislature).⁹¹ In the latter case, the suspension applies only for the fiscal year in progress at that time,⁹² so an emergency must be redeclared annually to achieve permanent changes to the caps.

⁸⁷ Silbermann, Whipple & Mills, *supra* note 27, at 8.

⁸⁸ Pub. Act No. 18-81 [2018 budget implementer] § 21. The 2017 budget implementer contained similar language, § 706, except that it set the moratorium to ten years. Before § 706 could take effect, however, the 2018 budget implementer amended that period to five years. Thus, the bond lock never held force in its ten-year form.

⁸⁹ Silbermann, Whipple & Mills, *supra* note 27, at 8. Recall, though, that several of the fiscal caps contain their own exit provisions, which are swept under the bond lock. If legislators secured supermajority votes and cleared other procedural hurdles described in the particular fiscal cap, they presumably could alter the cap without taking the extra step of suspending the bond lock.

⁹⁰ Pub. Act No. 18-81 [2018 budget implementer] § 21(aa)(1)(i).

⁹¹ *Id.* § 21(aa)(1)(ii).

⁹² *Id.* § 21(aa)(1)(ii)(III).

Clearly, this is an onerous process. It requires the Governor to acknowledge a fiscal emergency, and it empowers a minority of the legislature to block the amendments. This difference is especially stark when compared to the ordinary method for altering the caps. The most-protected of the four—the constitutional spending cap—would require a three-fifths majority to redefine the key language, or a three-fifths majority and a fiscal emergency to exceed the cap outright.⁹³ All other caps, however, are statutory. Absent the bond lock, they could be amended by a simple majority vote of the legislature (plus the Governor’s signature), *without* fiscal emergency. Even those caps that contain a more restrictive exit procedure⁹⁴ could be changed, as the exit procedure is itself a statute—repealable by simple majority.⁹⁵

In essence, the bond lock has given constitution-level protection to statutory budget rules. S&P praised the bond lock on those very grounds: “Restricting financial perspectives through bond covenants might have the effect of amending a state’s constitution, but without the delay and messy process of going to the voters.”⁹⁶ Table One illustrates this effect. In absence of the bond lock, all fiscal caps (excluding the constitutional spending cap) can be amended via simple majority vote.

⁹³ CONN. CONST. amend. XXVIII. Furthermore, the Amendment allows redefined language to apply prospectively, whereas the bond lock’s emergency procedure can only apply for the fiscal year in progress.

⁹⁴ For example, the appropriations cap requires a three-fifths majority and fiscal emergency. Pub. Act No. 17-2 [2017 budget implementer] § 705(b)(1); *see supra* Section III.A.3.

⁹⁵ As a general rule, the legislature cannot bind future legislatures to a supermajority requirement simply by passing a regular statute. For that, a constitutional amendment would be necessary. By way of analogy, the U.S. Senate needed *only a simple majority* (not a filibuster-proof supermajority) to invoke the “nuclear option” and restrict its standing rules on the filibuster. *See* Paul Kane, *Reid, Democrats Trigger ‘Nuclear’ Option; Eliminate Most Filibusters on Nominees*, WASH. POST (Nov. 21, 2013), https://www.washingtonpost.com/politics/senate-poised-to-limit-filibusters-in-party-line-vote-that-would-alter-centuries-of-precedent/2013/11/21/d065cfe8-52b6-11e3-9fe0-fd2ca728e67c_story.html.

⁹⁶ *Could Connecticut’s Proposed Bond Covenants Lead the Way to a New Financial Management Tool for Other U.S. States?*, S&P GLOBAL RATINGS (Mar. 28, 2018), https://www.capitaliq.com/CIQDotNet/CreditResearch/RenderArticle.aspx?articleId=2013604&SctArtId=451129&from=CM&ns_l_code=LIME&sourceObjectId=10484513&sourceRevId=1&fee_ind=N&exp_date=20280328-20:35:06 [hereinafter S&P Report].

Table One: Effect of the Bond Lock on Amending Fiscal Caps

	With Bond Lock, Using Caps' Statutory Exits	With Bond Lock, Using Lock's Statutory Exit	Without Bond Lock (changes are prospective)
Spending Cap	Fiscal emergency + 3/5 vote in each house (to exceed cap); OR 3/5 vote in each house (to change definitions)	Fiscal emergency + 3/5 vote in each house (to exceed cap); OR 3/5 vote in each house (to change definitions)	Fiscal emergency + 3/5 vote in each house (to exceed cap); OR 3/5 vote in each house (to change definitions)
Volatility Cap	3/5 vote in each house (to adjust threshold due to changes in tax law, economic growth, or tax collections)	Fiscal emergency + 3/5 vote in each house (to change cap for one year only); OR "Adequate protection" for bondholders	Simple majority vote (assuming the supermajority requirements are severed)
Appropriations Cap	Fiscal emergency + 3/5 vote in each house (to exceed cap for one year only); OR Simple majority vote (for an adjusted appropriation & revenue plan)	Fiscal emergency + 3/5 vote in each house (to change cap for one year only); OR "Adequate protection" for bondholders	Simple majority vote (assuming the supermajority requirements are severed)
Bond Cap	No exit specified	Fiscal emergency + 3/5 vote in each house (to change cap for one year only); OR "Adequate protection" for bondholders	Simple majority vote

Bonds issued since May 15, 2018, contained the locking covenant, as required.⁹⁷ Three GO bond issuances have occurred: \$500 million in June 2018, \$890 million August 2018, and \$1 billion in March 2019.⁹⁸ Thus, the fiscal restrictions have contractual force. Changing the caps, outside the prescribed procedure, would violate the covenants of these outstanding bonds. This would empower bondholders to bring a lawsuit for “technical default,” arguing that the State breached its contractual duty to abide by the caps.⁹⁹

There is good reason to anticipate that some or all of the budgetary caps will need to change before 2023.¹⁰⁰ The bond lock has made such amendments difficult, at best. If the legislature cannot effectively exercise its exit options to amend the budgetary caps, the bond lock will carry steep unforeseen consequences.

IV. Downstream Consequences

The bond lock rests on a critical assumption: that the underlying caps are in fact budgetary best practices, which *should* be difficult to change. Indeed, Connecticut’s fiscal imbalance largely was driven by a decades-long accumulation of unfunded liabilities, imposed

⁹⁷ Silbermann, Whipple & Mills, *supra* note 27, at 8.

⁹⁸ Press Release, Office of the State Treasurer, June Sale of \$500 Million of General Obligation Bonds Will Include Covenant to Lock In Fiscal Discipline (May 23, 2018), <https://www.ott.ct.gov/pressreleases/press2018/PR05232018BondSaleToIncludeCovenant.pdf>; Press Release, Office of the State Treasurer, General Obligation Bond Sale Signals Market Support of the State’s Efforts to Strengthen its Fiscal Health, Yields \$30 Million in Long-Term Debt Savings, Record-Setting Level of Retail Orders (Aug. 20, 2018), <https://www.ott.ct.gov/pressreleases/press2018/PR08202018MarketSupportsGOBondSale.pdf>; Press Release, Office of the State Treasurer, Treasurer Wooden Announces Historic General Obligation Bond Sales Record as Investors Cite Positive Momentum for Connecticut (Mar. 29, 2019), https://www.ott.ct.gov/pressreleases/press2019/PR032919TreasurerWooden_HistoricGOBondSalesRecord.pdf.

⁹⁹ Silbermann, Whipple & Mills, *supra* note 27, at 8. Ordinary default refers to a failure in repayment, whereas “technical default” involves the breach of other loan terms. *Technical Default*, BLACK’S LAW DICTIONARY (2d ed. online).

¹⁰⁰ See *infra* Section IV.B.

shortsightedly by past legislatures.¹⁰¹ Initial warm reactions to the bond lock praised its forced fiscal discipline¹⁰² and the reduced interest rates therefrom.¹⁰³ Conversely, if the caps prove ill-suited to the future economy, they have become very challenging to amend. It is unlikely that a Governor would go to the lengths of an emergency declaration, or that the legislature would secure a supermajority vote, absent truly perilous circumstances.¹⁰⁴

The result, then, is that Connecticut is bound to the hard rules written by that party-tied Senate in 2017. In no other context does a single legislature write binding rules for the next five (or ten) budget years. And even in that case, it would be imperative that the legislature solicit feedback from economic experts and public stakeholders via open hearings—none of which took place during the bipartisan budget negotiations.¹⁰⁵ Now that the lock is in place, however, the legislature should anticipate its likely consequences.

¹⁰¹ Christine Stuart, *Lamont Will Need to Confront ‘Iceberg’ of Unfunded Pension Liabilities*, CT NEWS JUNKIE (Feb. 19, 2019, 12:29 PM), https://www.ctnewsjunkie.com/archives/entry/20190219_amont_will_need_to_confront_iceberg_of_unfunded_pension.

¹⁰² S&P Report, *supra* note 96.

¹⁰³ The Treasurer’s press releases, *supra* note 98, are all prime examples. Over the last two bond issuances, those press releases claim about \$75 million in long-term interest savings. Though impressive, it is impossible to disentangle those interest savings from (1) falling long-term interest rates across the board; and (2) Governor Lamont’s vocal commitment to a “debt diet” – which could have been accomplished without the bond lock. Indeed, S&P specifically cited the debt diet when upgrading Connecticut’s outlook: “The outlook change to positive reflects the increased likelihood . . . that the state’s high debt levels could moderate if the governor’s proposal for a new ‘debt diet’ is carried through into policy.” Press Release, Office of Governor, Statement from Governor Lamont’s Office (May 1, 2019), <https://portal.ct.gov/Office-of-the-Governor/News/Press-Releases/2019/05-2019/Statement-From-Governor-Lamonts-Office-2>.

¹⁰⁴ Knopp, *supra* note 33 (characterizing the exit option as “an unwieldy and ineffectual remedy. . .”). Insofar as the purpose of the bond lock was to provide assurance to bondholders, declaring emergency to suspend the bond covenants undermines that goal. More likely, the declaration would prompt a spike in the interest rates demanded for new bond issuances. *Id.*

¹⁰⁵ Keith M. Phaneuf, *Legislature Willing to Listen Before Locking In Fiscal Restraints*, CT MIRROR (Mar. 8, 2018), <https://ctmirror.org/2018/03/08/legislature-willing-listen-locking-fiscal-restraints> (referring to a public hearing on whether to delay the bond lock, which was already law). On the bond lock’s initial adoption, the ranking House Republican on the Finance, Revenue and Bonding Committee “acknowledged they were developed chiefly during closed-door, bipartisan budget negotiations last October, and haven’t received a lot of public scrutiny.” *Id.*

A. *The Bond Cap “Drafting Error”: A Case Study in Fiscal Restrictions*

The first signs of trouble emerged mere months after the bond lock went into effect. In the spring 2018 Session—before the bond lock took force—the legislature moved to amend the bond cap in order to alleviate a crowd-out problem.¹⁰⁶ Legislators from both parties realized that three innocuous categories of borrowing—refinancing bonds, short-term revenue anticipation notes (RANs), and bonds for transportation projects—would count towards the hard \$1.9 billion bonding cap, displacing the State’s capacity to borrow for initiatives such as school construction and economic development.¹⁰⁷ Accordingly, on May 9, 2018, the legislature passed a law amending the bond cap to *exclude* any refinancing bonds and short-term RANs from the calculation, as well as \$500 million in transportation bonds (spread evenly over calendar years 2018-19).¹⁰⁸

The effective date of that law, unfortunately, read July 1, 2018—instead of immediately “on passage.”¹⁰⁹ The bond lock had taken force seven weeks prior, pledging that no legislation effective after May 15, 2018, would alter the caps. And in June, the Treasurer issued bonds

¹⁰⁶ Silbermann, Whipple & Mills, *supra* note 27, at 8.

¹⁰⁷ *Id.* The refinancing bonds would save money by reducing long-term interest rates, the short-term RANs would be repaid quickly after issuance, and the transportation bonds would enable much-needed investment in infrastructure. See Christopher Keating, *Sale of Connecticut Bonds Offers Encouraging Glimpse of a State with an Improving Financial Picture*, HARTFORD COURANT (July 25, 2019, 7:03 PM), <https://www.courant.com/politics/hc-pol-ct-treasurer-bond-sale-20190725-c7e4mhimxfh3tjdhxtd4sgczwe-story.html>; Rick Funaro, *Connecticut’s Infrastructure Ranked as One of the Worst in U.S.*, CT POST (Aug. 6, 2018, 3:55 PM), <https://www.ctpost.com/news/article/Connecticut-s-infrastructure-ranked-as-one-of-the-13135192.php>.

¹⁰⁸ Pub. Act No. 18-178, §§ 16(f)(2)(C), 41(b). For bill history, see H.B. 5590, 2018 Leg., Reg. Sess. (Conn.), available at https://www.cga.ct.gov/asp/cgabillstatus/cgabillstatus.asp?selBillType=Public+Act&which_year=2018&bill_num=178.

¹⁰⁹ Prior drafts of the bill *had* read “effective on passage;” and there is good reason to believe that the change to July 1 was a legislative oversight. See *infra* notes 117-121 and accompanying text.

containing that covenant, as required by law.¹¹⁰ Thus, if the State attempted to utilize any of the three new bond cap exceptions, it would risk violating the June bond covenant and triggering a technical default.¹¹¹

The Treasurer’s Office realized this conflict in September 2018 and alerted the Governor that it would be “complying with the initially adopted and more constrained bond cap,”¹¹² notwithstanding the July amendment. That letter also presented three possible strategies for effectuating the recently enacted bond cap exemptions,¹¹³ explored in greater detail below.

1. Exercise the Emergency Clause

First, Connecticut could follow the newly prescribed procedure for suspending the bond covenants: an emergency declaration by the Governor, followed by a supermajority vote in the legislature. Because the suspension is only valid for one year, this formal escape mechanism would need to be repeated annually for the entire duration of the bond lock,¹¹⁴ effectively nullifying it. From a political standpoint, this also would require that newly-elected Governor Lamont place the State in continuous “fiscal emergency” throughout his first term—likely denying him a second.

¹¹⁰ Letter from Denise L. Nappier, State Treasurer, to Dannel P. Malloy, Governor (Sept. 18, 2018), available at <http://www.yankeeinstitute.org/wp-content/uploads/2018/10/DLN-Letter-to-Governor-RE-Bond-Cap-Glitch-9-18-18.pdf> [hereinafter Treasurer’s Letter].

¹¹¹ Silbermann, Whipple & Mills, *supra* note 27, at 8.

¹¹² Treasurer’s Letter, *supra* note 110, at 2.

¹¹³ *Id.* at 2-3.

¹¹⁴ Silbermann, Whipple & Mills, *supra* note 27, at 9-10.

2. Refund and Reissue the Bonds

Alternatively, the Treasurer suggested that the State could refund and reissue the June bonds. This would be expensive; in addition to the banking fees and interest rate risks involved, the letter notes that advanced refunding would be federally taxable.¹¹⁵ Furthermore, the plan assumes that the legislature would then amend the bond lock statute to sweep in the bond cap exemptions (i.e., change the moratorium on new legislation to begin *after* July 1, 2018).¹¹⁶ If properly executed, though, a refunding plan would carry the advantage of clearing away defective bond covenants.

3. Pursue a Legislative or Judicial Remedy

Finally, the Treasurer's letter considered pursuing alternative remedies "to what clearly appears to have been an unintended legislative action."¹¹⁷ That description matches well with the "Scrivener's Error" doctrine, wherein a court may correct "a mistake in writing [o]r copying."¹¹⁸ Moreover, it fits the facts. The July 1 effective date appeared in an amendment; previously, the bill had read "*effective on passage*."¹¹⁹ Other sections of that amendment were set effective July 1 to coincide with the new fiscal year, which likely explains the change. Had the three new bond cap exemptions remained effective on passage, they would have taken effect *before* the bond lock began on May 15. Further evidence of the error appears in Section 41 of the final bill, wherein

¹¹⁵ Treasurer's Letter, *supra* note 110, at 3 (noting "federal tax restrictions on advance refundings," which would raise the State's cost of refinancing).

¹¹⁶ Silbermann, Whipple & Mills, *supra* note 27, at 9-10.

¹¹⁷ Treasurer's Letter, *supra* note 110, at 2.

¹¹⁸ *Clerical Error*, BLACK'S LAW DICTIONARY (2d ed. online). For an example of the Scrivener's Error doctrine in practice, see, e.g., *Monge v. Acabbo*, No. NNHCV146046515, 2016 Conn. Super. LEXIS 2748 (Conn. Super. Ct. Nov. 1, 2016); *King v. Burwell*, 135 S. Ct. 2480 (2015).

¹¹⁹ Compare Section 3 of the bill as voted out of committee (available at <https://www.cga.ct.gov/2018/FC/pdf/2018HB-05590-R000643-FC.PDF>) with Section 16 of the amendment (available at <https://www.cga.ct.gov/2018/amd/H/pdf/2018HB-05590-R00HA-AMD.pdf>).

the legislature outlines a borrowing schedule for the \$500 million in exempted transportation bonds.¹²⁰ It would be incongruous to specify the amount of exempted borrowing for 2018-2019, if the exemptions could not be utilized until 2023. Based on the floor debate transcripts, no legislators caught this change to the effective date or anticipated its consequences.¹²¹ Therefore, a reviewing court likely would be within its powers to correct the effective date.

The Scrivener's Error doctrine, however, has never been applied in the Connecticut appellate courts.¹²² One lower court decision, *Monge v. Acabbo*, did utilize Scrivener's Error to read court entry fees into an itemized list of recoverable costs.¹²³ Judge Ecker wrote that "[t]he legislative choice under review is odd enough to cause one to ask whether the policy choice reflected in the literal language of the statute was a choice ever really made by the legislature."¹²⁴ He concluded that court entry fees had been inadvertently stricken from the statute by a scrivener's error in an 1893 amendment,¹²⁵ under remarkably similar circumstances to the 2018 bond cap amendment. Were the issue to reach the Connecticut Supreme Court, there is a

¹²⁰ Pub. Act No. 18-178 § 41(b).

¹²¹ House Transcript, Session of May 9, 2018, at 467-73, available at <https://www.cga.ct.gov/2018/trn/H/pdf/2018HTR00509-R01-TRN.pdf>; Senate Transcript, Session of May 9, 2018, at 333-38, available at <https://www.cga.ct.gov/2018/trn/S/pdf/2018STR00509-R00-TRN.pdf>. Debate was brief and without mention of the bond lock. The transcripts also show unanimous passage in both houses.

¹²² *Monge*, 2016 Conn. Super. LEXIS 2748, at *20 ("Connecticut's appellate courts have not yet had occasion to determine whether the scrivener's error doctrine is accepted as a tool of statutory construction in this state."); *see also* Silberman, Whipple & Mills, *supra* note 27, at 9.

¹²³ 2016 Conn. Super. LEXIS 2748.

¹²⁴ *Id.* at * 19.

¹²⁵ *Id.* at * 28 ("[A] scrivener's error provides the only conceivable explanation for the bizarre textual swerve that occurred in 1893. Very likely, a legislative clerk or aide. . . erroneously added an extra semi-colon, and thereby unintentionally rearranged the terms in a way that subtly but undeniably impaired the logic of the statutory enumeration. No other explanation seems plausible.")

reasonable chance that the Scrivener’s Error doctrine would be adopted explicitly; in fact, *Monge’s* author now sits as a Justice.¹²⁶ It is not, however, a certainty.

Perhaps concerned that a Scrivener’s Error theory might not be persuasive, former Connecticut Attorney General George Jepsen developed a separate remedy for the bond cap language. He issued an opinion harmonizing the bond cap exemptions with the language of the bond lock, following the established practice of construing statutes so as to avoid incoherent results.¹²⁷ By his reading, the legislature intended to lock in the caps *as amended* by any law “already passed prior to May 15, 2018. . . .”¹²⁸ This would sweep in all legislation from the spring Session, which concluded May 9,¹²⁹ then pledge no further changes. Certainly, the bond cap exemptions had *passed* prior to May 15, even if they were not *effective* until July 1. Accordingly, the Attorney General concluded that the Treasurer could immediately utilize the full bond cap exclusions.¹³⁰

It is worth noting, however, that the Attorney General’s opinion did not immunize the State from technical default on the bonds issued in June 2018. If bondholders were to sue the State, the opinion would be reviewed in court against a plausible textual argument that the bond covenant language (“taking effect”) cannot be read to cover legislation that was merely “passed” prior to May 15, 2018. Consequently, as the 2019 legislature drafted Connecticut’s first full

¹²⁶ *Biographies of Supreme Court Justices: Associate Justice Steven D. Ecker*, ST. CONN. JUD. BRANCH, <https://www.jud.ct.gov/external/supapp/justiceEcker.html>.

¹²⁷ Letter from George Jepsen, Att’y Gen., to Denise L. Nappier, State Treasurer (Nov. 21, 2018), available at https://portal.ct.gov/-/media/AG/Opinions/2018/2018-04_Bond_Covenant.pdf [hereinafter AG’s Opinion].

¹²⁸ *Id.* at 9. (“Because we cannot assume that the legislature intended to completely and repeatedly contradict itself, the only plausible explanation is that the legislature intended to bar any *new* public act, or any public act *other than one already passed prior to May 15, 2018*, that would alter the covenants in question.”).

¹²⁹ *2018 Connecticut Legislative Session*, BALLOTPEDIA, https://ballotpedia.org/2018_Connecticut_legislative_session.

¹³⁰ AG’s Opinion, *supra* note 127, at 2.

biennial budget under the bond lock, it approved a joint resolution to “ratify and confirm” the Attorney General’s reading of prior legislative intent.¹³¹ Compared to the Attorney General’s opinion alone, the joint resolution is entitled to even greater deference in discerning the intent behind the bond cap exclusions.¹³² Thus, one year later, the risk of an adverse court ruling finally has diminished.

The difficulties of effectuating the bond cap exemptions—which had passed the legislature unanimously¹³³— illustrate the consequences of locking in fiscal policy. Actually utilizing the bond cap exclusions approved in May 2018 required an alert by the Treasurer, a formal opinion by the Attorney General, and a subsequent resolution by the General Assembly. Moreover, the Attorney General’s opinion is a one-time patch that would not cover any *newer* amendments to the budgetary caps. As economic circumstances evolve up to 2023, the caps might become ill-suited for modern budgeting needs; but by then they will be even more onerous to amend. While it is impossible to accurately forecast the State’s economy five years out, legislators can anticipate that interactions among the several fiscal caps will cause ever greater interference with budget-making as the fiscal years progress.

B. Interaction of the Spending, Volatility, and Appropriations Caps

Though the legislature ultimately managed to effectuate its bond cap exceptions, further problems lie on the horizon. The spending cap, for example, permanently “ratchets down”

¹³¹ H.R. J. Res. 170, 2019 Leg., Reg. Sess. (Conn.), available at https://www.cga.ct.gov/asp/cgabillstatus/cgabillstatus.asp?selBillType=Bill&bill_num=HJ00170&which_year=2019.

¹³² See, e.g., *Red Lion Broadcasting Co. v. FCC*, 395 U.S. 367, 380-81 (1969) (“Subsequent legislation declaring the intent of an earlier statute is entitled to great weight in statutory construction.”).

¹³³ *Bill Status: Substitute for Raised House Bill 5590*, CONN. GEN. ASSEMBLY (2018), https://www.cga.ct.gov/asp/cgabillstatus/cgabillstatus.asp?selBillType=Bill&which_year=2018&bill_num=5590 (linking to roll-call votes for the House and Senate).

allowable spending after a year of decreased revenue.¹³⁴ The hypothetical, appearing in a report by Connecticut Voices for Children,¹³⁵ runs as follows: Suppose a normal economy in year 1, a recession in year 2, and a recovery in years 3-4. Because Connecticut must achieve a balanced budget,¹³⁶ lower revenue in year 2 requires lower spending as well. And, per the constitutional amendment, *actual spending* in the prior year becomes the base from which the next year's spending cap is calculated.¹³⁷ Thus, when revenue rebounds in years 3-4, spending remains constrained. For those years, "it treats the state budget like Connecticut is still in a recession, even when revenues have recovered, forcing unnecessary cuts and slowing economic growth."¹³⁸ On the contrary, the State should be *spending* during a recovery, to sustain economic growth and shore up low-income residents still affected by the downturn.¹³⁹ This could be so if the spending cap were calculated based on *allowed* spending, without automatic rebasing when revenue declines.¹⁴⁰ Unfortunately, the spending cap's mechanics are now locked in their current form.

The volatility cap also contains defects due to its hard threshold of \$3.15 billion. The Connecticut Voices for Children report forecasts that this fixed threshold in the volatility cap will require over \$550 million in BRF deposits during fiscal years 2020-2021, despite combined deficit projections of about \$4 billion.¹⁴¹ Accordingly, the volatility cap will compound the effects

¹³⁴ Silbermann, Whipple & Mills, *supra* note 27, at 4.

¹³⁵ *Id.*

¹³⁶ CONN. CONST. amend. XXVIII.

¹³⁷ *Id.*

¹³⁸ Silbermann, Whipple & Mills, *supra* note 27, at 4.

¹³⁹ This is a next-best alternative to Keynesian deficit spending. Since states have balanced-budget requirements, *see supra* note 12 and accompanying text, deficit spending is limited by the balances of their "rainy day" reserve funds. When revenues start to increase during the recovery period, states can return their spending to pre-recession levels; then once the economy is strong, states can replenish their reserve funds. *See generally* James C. Garand et al., *Fiscal Policy in the American States*, in *THE OXFORD HANDBOOK OF STATE AND LOCAL GOVERNMENT POLITICS* (Donald Hader-Markel ed., 2013) (discussing state fiscal policy in a Keynesian framework).

¹⁴⁰ Silbermann, Whipple & Mills, *supra* note 27, at 4.

¹⁴¹ *Id.* at 5.

of spending cuts and set up a vicious cycle with the spending cap, as the diversion of revenues away from current spending further reduces the allowable spending in future years.¹⁴² It also will remove some revenue-raising options from consideration, since new revenue would be diverted to the BRF. This could be corrected if the threshold were raised or if the cap were returned to its original 2015 form. Once again, the bond lock precludes such changes, unless legislators can clear onerous procedural hurdles to invoke one of the exit options.¹⁴³

Finally, the appropriations cap further amplifies the “ratcheting down” effect just described.¹⁴⁴ Recall that the appropriations cap places a “cushion” between expected revenue and appropriated spending. The volatility cap first reduces the expected revenue available for appropriation; then the cushion is applied as a second reduction. The two effects stack to suppress actual spending, “and thus lower the next year’s spending limit further.”¹⁴⁵ Whether legislators anticipated this interaction is unclear. Nonetheless, they locked it in place via the bond covenants. If the future deficit projections prove accurate, Connecticut will begin to feel the squeeze. Spending limits, combined with growing fixed costs, will force cuts to discretionary spending—including education grants and municipal aid¹⁴⁶—with far-reaching distributional consequences for America’s third-most unequal state.¹⁴⁷

¹⁴² *Id.* at 7.

¹⁴³ *Id.* at 5–6.

¹⁴⁴ *Id.* at 7.

¹⁴⁵ *Id.*

¹⁴⁶ *Id.* at 10–13,

¹⁴⁷ Estelle Sommeiller & Mark Price, *The New Gilded Age: Income Inequality in the U.S. by State, Metropolitan Area, and County*, ECON. POL’Y INST. 19 (July 19, 2018), <https://www.epi.org/files/pdf/147963.pdf> (showing a ratio of 37.2 between the average incomes of Connecticut’s top 1% and its bottom 99%, trailing only New York (44.4) and Florida (39.5)).

These scenarios are only a sampling of how the caps could backfire in an evolving economy. Hard limits are, by their nature, unmalleable. And the burdensome exit options make it all the more likely that arbitrary rules will stay “locked in,” even as they drag on growth.

C. Inefficient Budget-making

The arbitrariness of Connecticut’s budget rules was on prominent display during the legislature’s 2019 Session, when the General Assembly designed its first full biennial budget under the caps and subject to the bond lock. Legislators advanced multiple proposals to raise revenue and increase bonding capacity; but ultimately, they needed to prioritize compliance above efficient economic policy.

For example, legislators opened the Session proposing a surcharge on capital gains income¹⁴⁸ and a new tax on pass-through entities,¹⁴⁹ which raised questions of whether and how the revenue could be spent. If revenue fell under a category subject to the volatility cap, it would be swept automatically into the BRF. Moreover, the spending cap would limit general budget expenditures overall. To be clear, the skewed calculus extends beyond revenue-raising decisions. Supposing that legislators identified opportunities to reduce spending, they would need to proceed with caution because even a one-time spending reduction rebases the spending cap for subsequent years.¹⁵⁰ In the bonding arena, legislators also proposed to abolish the statutory

¹⁴⁸ Keith M. Phaneuf, *Democrats Push Back on Lamont, Renew Bid to Tax Connecticut’s Wealthiest Households*, CT MIRROR (May 1, 2019), <https://ctmirror.org/2019/05/01/democrats-push-back-on-lamont-renew-bid-to-tax-cts-wealthiest-households>.

¹⁴⁹ Keith M. Phaneuf, *Business Groups Hope to Sink Tax Hike on Pass-Through Entities*, CT MIRROR (May 31, 2019), <https://ctmirror.org/2019/05/31/business-groups-hope-to-sink-tax-hike-on-pass-through-entities>.

¹⁵⁰ See *supra* Section IV.B.

limitation on special tax obligation (STO) bonds for transportation projects,¹⁵¹ one of the few categories outside the bond cap.

These artificial budgeting constraints might help to explain why broader proposals—such as progressive income tax increases urged by the citizens’ group Fair Share Connecticut¹⁵²—failed to generate momentum. Under the new budget rules, not all revenue is created equal. Legislators must consider which sources can be readily appropriated, before weighing efficiency and desirability. In other words, the caps have forced lawmakers to work *ad hoc* around the new fiscal rules, rather than craft a holistic budget.

D. A Bondholders’ Lawsuit

The force keeping those caps in place is the threat of a bondholders’ lawsuit, based on the bond lock covenants. If Connecticut alters any of the caps outside the prescribed mechanism, it will trigger technical default.¹⁵³ Even assuming no further changes, there is *already* some risk due to the bond cap exemptions.¹⁵⁴ The case for technical default is more straightforward if the legislature attempts to alter another cap.

Merely filing a lawsuit would carry its own set of foreseeable consequences. It likely would startle the bond markets and divert resources at the Attorney General’s Office to preparing a defense. If the lawsuit is ultimately successful, the costs would be severe.

¹⁵¹ H.B. 7424, § 375, 2019 Leg., Reg. Sess. (Conn.).

¹⁵² Christopher J. Keating, *Wealthy Connecticut Residents Propose \$1 Billion in New Taxes on Themselves and Other Millionaires*, HARTFORD COURANT (May 14, 2019), <https://www.courant.com/politics/hc-pol-millionaires-tax-letter-20190514-erdbpjck6fg4farophgj74f6b4-story.html>.

¹⁵³ For an explanation of “technical default,” see *supra* note 99 and accompanying text.

¹⁵⁴ *Supra* Section IV.A.

As a threshold matter, bondholders likely have standing to sue. Assuming they accepted a lower interest rate in exchange for the promise of strict adherence to the fiscal caps,¹⁵⁵ bondholders would be injured by losing the greater security afforded to them under the covenant. Moreover, Connecticut would be unable to invoke sovereign immunity. State laws altering the budgetary caps would “impair[] the obligation of contracts,”¹⁵⁶ in violation of the federal constitution – a case in which the sovereign immunity defense does not apply.¹⁵⁷ Quite plausibly, such a lawsuit could proceed.

The most speculative element of a bondholders’ lawsuit concerns the appropriate remedy; but none is desirable from the State’s perspective. A court likely would balk before ordering the legislature to strictly abide by the original caps (i.e., specific performance), under separation of powers concerns. Instead, the court probably would award an increased interest rate or direct an accelerated – perhaps even immediate – payment schedule. Either cures the bondholders’ injury: the higher interest rate offsets any returns forfeited in reliance on the bond lock, and the accelerated payment schedule ensures that the bondholders collect in full. Neither, however, is palatable for the State. Connecticut would face an unanticipated spike in borrowing costs¹⁵⁸ or an accelerated repayment of up to \$2.4 billion in outstanding bonds.¹⁵⁹

¹⁵⁵ Indeed, S&P cited the bond lock among its reasons for changing Connecticut’s outlook to “positive.” *Connecticut; Appropriations; Gas Tax; General Obligation; General Obligation Equivalent Security; Moral Obligation*, S&P GLOBAL RATINGS: RATINGSDIRECT (Mar. 19, 2019) (on file with author). *But cf. supra* note 103 (arguing that the upgrade to Connecticut’s bond outlook is more directly attributable to the Governor’s voluntary “debt diet”).

¹⁵⁶ U.S. CONST. art. I, § 9, cl. 1.

¹⁵⁷ See *Ex Parte Young*, 209 U.S. 123 (1908). This stems from the Supremacy Clause, U.S. CONST art. VI, § 1, cl. 2.

¹⁵⁸ Notably, this would immediately negate any short-term gains realized by the upgrading of Connecticut’s bond outlook. See *supra* notes 103 & 155.

¹⁵⁹ Per the Treasurer’s press releases, *supra* note 98, Connecticut issued about \$500 million of GO bonds in June 2018, \$890 million in August 2018, and \$1 billion in March 2019.

Fortunately, this situation can be defused. As Part V argues, it is possible—with the right sequence of legislation—for lawmakers to safely remove the bond lock, allowing legislators to adapt the underlying caps in accordance with budgetary best practices.

V. Removing the Fiscal Handcuffs

Considering the bond lock’s downstream consequences, the preferable policy is to restore the legislature’s ability to make informed democratic decisions about future budgets. That requires releasing the bond lock, well in advance of its 2023 expiration date. The two necessary steps are as follows: (1) “stop the bleeding,” by either pausing or repealing the bond lock statute before any new GO bonds are issued; and (2) account for the three past bond issuances that already contained the locking covenant. While this path demands legislative and executive courage, the stakes of inaction are clear.

A. *Pause or Repeal the Bond Lock*

First, legislators would need to direct the Treasurer to discontinue the issuance of locking covenants in future rounds of bonding. This would limit the number of locking covenants outstanding, making the problem finite and correctable. Indeed, pausing or repealing the bond lock is a prerequisite for the corrective measures in step two; otherwise, the problem would return whenever the Treasurer issued additional locking covenants.¹⁶⁰ The Treasurer plans to issue an additional \$800 million of GO bonds in November 2019.¹⁶¹ Unless the legislature

¹⁶⁰ In theory, the legislature could proceed in reverse order (i.e., address the outstanding bond covenants, then suspend the bond lock). However, legislation to address the outstanding covenants would be futile if not promptly accompanied by legislation to repeal the bond lock. Step one is more time-sensitive—and more immediately attainable—which informs this Paper’s ordering.

¹⁶¹ *Forward Financing Calendar: 2020 Fiscal Year*, STATE OF CONN. TREASURER’S OFFICE, https://www.otl.ct.gov/debt_forwardfinancingcalendar.html.

intervenes before that date, the November bonds will contain the locking covenant. Since the 2019 Session has formally adjourned, this stopgap legislation would require a Special Session.¹⁶²

Recall that the bond lock is a *statutory* creation.¹⁶³ Once the covenants are issued in actual bonds, the lock becomes contractual; but the Treasurer’s duty to include the covenants originates only in statute. Thus, if the statute were suspended or repealed,¹⁶⁴ the Treasurer would cease to include the locking covenant in all *subsequent* bond issuances. That change can be accomplished by a simple majority vote of the legislature.¹⁶⁵

It is worth clarifying here that the bond lock covenant does not contain a “circular reference,” such that it promises no changes to the bond lock statute itself. This becomes apparent when breaking down the language. The bond covenants pledge that no legislation within the moratorium period may amend:

(A) section 4-30a of the general statutes . . . [the volatility cap], (B) section 2-33c . . . [the appropriations cap], (C) section 2-33a . . . [the spending cap], (D) subsections (d) and (g) of [section 706] [the bond cap’s limit on SBC authorizations], and (E) section 3-21 [the bond cap’s limit on Treasurer issuances].¹⁶⁶

The bond lock statute, codified at Section 3-20(aa) of the General Statutes, receives no mention. To accomplish the circular reference would have required a clause (F) to the effect of:

¹⁶² Advantageously, the debate over highway tolls could provide an independent platform for calling that fall session. See Mark Pazniokas, *Lamont Leaves Tolls for Special Session*, CT MIRROR (May 21, 2019, 5:05 PM), <https://ctmirror.org/2019/05/21/lamont-shifts-to-budget-leaves-tolls-for-special-session>.

¹⁶³ Pub. Act No. 17-2 [2017 budget implementer] § 706.

¹⁶⁴ Functionally, suspending the bond lock statute through July 1, 2023, would have the same effect as an outright repeal, but it might be politically preferable for some legislators.

¹⁶⁵ Letter from Jamie Mills, Dir. of Fiscal Policy & Econ. Inclusion, Conn. Voices for Children, to Rep. Matt Ritter (Mar. 28, 2019) (on file with author).

¹⁶⁶ Pub. Act No. 17-2 [2017 budget implementer] § 706.

“and section 3-20 of the general statutes, as amended by this section.” Because this is lacking, the bond lock statute is free to be changed—prospectively, at least—via the normal legislative process. Moreover, current bondholders would have no cause to object, since their previously issued covenants would be unaffected. To account for the bonds already outstanding, additional legislation is necessary.

B. Account for Outstanding Bonds

Having suspended or repealed the bond lock statute, the legislature is still prohibited from changing the budgetary caps; doing so would violate the bond covenants already issued. Accordingly, the legislature would need to accommodate, clear, or invalidate those covenants.

1. Accommodating Current Bondholders

The legislature’s first option relates back to the *other* statutory exit from the bond lock: providing “adequate . . . protection [for] the holders of such bonds. . . .”¹⁶⁷ This allows the legislature to change the volatility cap, appropriations cap, and bond cap by simple majority¹⁶⁸—provided that the bondholders are simultaneously protected.¹⁶⁹ The spending cap would continue to receive constitutional protections, changeable as provided in the Twenty-Eighth Amendment.¹⁷⁰

To better understand “adequate protection,” suppose, for example, that the legislature guaranteed repayment on the outstanding bonds by dedicating proceeds from the State Lottery

¹⁶⁷ Pub. Act No. 18-81 [2018 budget implementer] § 21(aa)(1)(i). *See supra* Section III.B.

¹⁶⁸ The volatility cap and appropriations cap contain their own supermajority requirements; however, that language is all statutory and could be repealed by a simple majority—but for the bond lock. *See supra* notes 94–95 and accompanying text.

¹⁶⁹ Silbermann, Whipple & Mills, *supra* note 27, at 14.

¹⁷⁰ CONN. CONST. amend. XXVIII; *see supra* note 93 and accompanying text.

to that purpose. If Lottery revenues were sufficient to service that debt, then changing the budgetary caps would have no bearing on the State’s ability to repay its bonds. Bondholders would be unharmed, and the cap amendments could proceed on a simple majority vote. To use this option, though, there are two hurdles to clear. The legislation must secure bondholders’ investments to their satisfaction, and it must survive scrutiny under the Contracts Clause of the federal Constitution.

It is important to involve the bondholders in determining what satisfies “adequate protection,” lest they bring a lawsuit to challenge the decision. Before designating a funding stream to protect repayment, legislators should look carefully to the impact on bondholders. Ideally, they would utilize a public process, where bondholders have an opportunity to comment on the proposed change.¹⁷¹ This would entail the added difficulties of assembling diffuse bondholders and reaching consensus—indeed, one might expect holdouts who attempt to exact additional concessions¹⁷²—but it also would demonstrate good faith by the State to adequately protect investors’ returns.

The Contracts Clause is an additional constraint on altering the budgetary caps via “adequate protection.” It prohibits states from passing any law “impairing the obligation of contracts.”¹⁷³ Amending the caps would alter Connecticut’s contractual promise to the bondholders that they must remain in effect, unchanged, through 2023. Therefore, any possible

¹⁷¹ Silberman, Whipple & Mills, *supra* note 27, at 14.

¹⁷² *Id.* Consider, for example, the 7% of bondholders who refused to accept Argentina’s sovereign debt restructuring. Those “vulture funds” held out for repayment in full and even resorted to litigation. Martin Guzman & Joseph E. Stiglitz, Opinion, *How Hedge Funds Held Argentina for Ransom*, N.Y. TIMES (Apr. 1, 2016), <https://www.nytimes.com/2016/04/01/opinion/how-hedge-funds-held-argentina-for-ransom.html>.

¹⁷³ U.S. CONST. art. I, § 10, cl. 1.

impairment would need to withstand scrutiny under the Contracts Clause. The leading test, appearing in *United States Trust v. New Jersey*, requires the state to show that the impairment is (a) not substantial, and (b) “reasonable and necessary to serve an important public purpose.”¹⁷⁴ Again, this would be done by building a robust factual record, in cooperation with bondholders, to show that the alternative funding stream will adequately protect their interests.¹⁷⁵

2. Clearing the Covenants by Refunding

The Treasurer outlined a second alternative in response to the bond cap “drafting error,” noting that the outstanding bonds could be refunded and reissued.¹⁷⁶ This was already an expensive option back in 2018, and the subsequent bond issuances have only raised the cost of refinancing. If pursued, though, it would clear the problematic bond covenants entirely, thereby releasing the bond lock.¹⁷⁷

3. Invalidating the Bond Lock

Lastly, the State could challenge the bond lock head-on. There is a plausible claim that the bond lock was “unconstitutional from its inception.”¹⁷⁸ The Connecticut Constitution vests lawmaking power in the General Assembly,¹⁷⁹ which legislators partially ceded via the bond lock. Essentially, the bond lock gave bondholders a contractual check on the lawmaking power of

¹⁷⁴ 431 U.S. 1, 28-32 (1977). *See also* Home Building & Loan Ass’n v. Blaisdell, 290 U.S. 398 (1934) (upholding state legislation to limit creditors’ foreclosure remedies—notwithstanding the Contracts Clause—given the exigency of the Great Depression).

¹⁷⁵ Silberman, Whipple & Mills, *supra* note 27, at 14.

¹⁷⁶ *Supra* Section IV.A. *See also* Treasurer’s Letter, *supra* note 110, at 3.

¹⁷⁷ Silberman, Whipple & Mills, *supra* note 27, at 14.

¹⁷⁸ *Id.* (citing Knopp, *supra* note 33).

¹⁷⁹ CONN. CONST. art. III, § 1.

future legislatures, not yet elected. Alex Knopp, a former State legislator, has written on this issue and offered a useful hypothetical.

Since the creation of new judgeships is an expensive personnel item, could the General Assembly in its wish to “tie the hands” of future legislators for budget discipline require the treasurer to include a covenant in future GO bonds that no additional judgeships shall be created and no additional judges shall be confirmed by the General Assembly between 2018 and 2028?¹⁸⁰

Those powers, so the argument goes, are non-delegable; they are entrusted not to bondholders, but specifically to the General Assembly as chosen by future electorates.¹⁸¹ If the bond lock is unconstitutional, then the covenants are unenforceable, and the budgetary caps could be amended by ordinary legislation.¹⁸² This would, however, require an opinion by the new Connecticut Attorney General, and perhaps a day in court.¹⁸³

It is imperative to the democratic process that voters and legislators retain control over budget-making. The bond lock signed away significant discretion; but it is possible to change course, by any of the three strategies herein described, before the consequences become severe. Though responsible budgeting was a laudable goal, excessive hand-tying was dangerous. Removing the fiscal handcuffs should be a high priority, warranting a Special Session in fall 2019.

¹⁸⁰ Knopp, *supra* note 33.

¹⁸¹ *Id.*

¹⁸² See *supra* notes 94-95 and accompanying text (clarifying that statutory supermajority requirements could be stricken from the statutory caps via legislation passed with a simple majority).

¹⁸³ Silbermann, Whipple & Mills, *supra* note 27, at 14.

VI. Conclusion: A Roadmap for Responsible, Democratic Budgeting

Connecticut faced a crossroads in 2018. Though it has begun walking down the Fiscal Commission’s path of forced austerity – reinforced by an untested form of contractual TELs – the State still can correct course by exiting the bond lock and repairing the four caps.

The current path is well-trodden. Rather than promoting long-term growth, overly stringent TELs *undercut the foundation of a healthy economy*. Indeed, the spiral from budgetary disinvestment to economic stagnation is well established in Kansas, Louisiana, Oklahoma, and other states that aggressively limited their taxing and spending.¹⁸⁴ By contrast, a visionary legislature would make forward-looking investments in inclusive opportunity.¹⁸⁵ Restrictive TELs are utterly incompatible with that strategy.

Connecticut can and should implement procedural improvements to budget-making. One plan endorsed by the Fiscal Commission *and* its critics – yet still unadopted – is to task a joint legislative committee with developing long-range fiscal plans and short-term budget targets.¹⁸⁶ This is perhaps the antithesis to the bond lock, as it *empowers* future legislators to craft intelligent and responsive fiscal policy. Budget-making belongs there, with the legislature; not with the bondholders.

¹⁸⁴ Jeremy Pilaar & Sam Whipple, *Testimony Regarding the Final Report of the Connecticut Commission on Fiscal Stability and Economic Growth*, CONN. VOICES FOR CHILDREN (Mar. 23, 2018), <http://www.ctvoices.org/sites/default/files/2018ZZ-00000-R000323-Pilaar%2C%20Jeremy%2C%20Yale%20Law%20School%20LAC-TMY.PDF>.

¹⁸⁵ See, e.g., Wesley Tharpe, *People-Powered Prosperity: A People-First Economic Vision for Georgia*, GA. BUDGET & POL’Y INST. (Feb. 2018), <https://cdn.gbpi.org/wp-content/uploads/2018/02/GBPI-People-Powered-Prosperity.pdf>.

¹⁸⁶ Patricelli & Smith, *supra* note 5, at 7; *Commission on Fiscal Stability and Economic Growth: Hearing of Jan. 24, 2018*, (testimony of Alex Knopp, at 6-7), available at https://www.cga.ct.gov/fin/tfs/20171205_Commission%20on%20Fiscal%20Stability%20and%20Economic%20Growth/20180124/Alex%20Knopp%20Testimony.pdf.