Budget Development - Table of Contents

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Budget Development

Introduction

The state budget is the foundation for responsible government spending. It has a wide-ranging and far-reaching impact on the well-being of the residents of the Commonwealth. It is the vehicle through which we as a citizenry make investments together for the benefit of us all – investments for the "Commonwealth." It is a policy document, serving to outline how state government chooses to allocate scarce resources to meet a variety of annual and long-term objectives.

Serving as a blueprint for the activities and obligations of the year, the budget reflects our collective judgment about state government's role in our society, obligations to serve its people and strategic investments to secure its future prosperity. Each line item represents a critical service, program or responsibility that the state will perform or provide to families and individuals throughout fiscal year 2012.

The Patrick-Murray Administration's fiscal year 2012 budget is a balanced, responsible budget that reflects the continuing financial challenges confronting the Commonwealth since the start of the economic recession in 2008. It is also a vehicle for an aggressive reform agenda. Despite continued improvement in revenue growth in fiscal year 2012, the additional funding available to the state next year will not be able to offset the loss of one-time resources provided through federal stimulus funding for states over the last three fiscal years.

Having solved for budget deficits totaling over $13 billion since the beginning of the fiscal crisis, the Administration is once again submitting a thoughtfully balanced and responsible fiscal year 2012 budget proposal. After accounting for revenue growth, the state must still spend less next year than this year, while continuing to meet its increased long-term liabilities for pensions, retiree health care and debt service. Furthermore, state agencies will need to find further means to control costs and find efficiencies, stretching every taxpayer dollar further to support their programs and services.

The fiscal year 2012 budget relies on a substantially reduced amount of one-time resources (approximately $386 million), in comparison to this fiscal year, which is balanced with $1.9 billion in one-time sources, in particular $1.5 billion in federal stimulus funds.

Massachusetts, much like virtually every state in the nation, faces unprecedented fiscal challenges as federal stimulus aid ends and pensions and other liabilities add spending pressures to the annual budget. The Administration's budget once again reflects the difficult choices and spending cuts made in response to this reality, while ensuring that the state will be well-positioned in the future to serve its residents. Spending cuts alone will not solve our challenges; in fiscal year 2012 the state will need to fundamentally change the way it does business across an array of government programs, services and operations.

The fiscal year 2012 budget continues to protect investments made in core areas of state government: funding for public education to help close the achievement gap, controlling increasing health care costs, job creation, and addressing youth and urban violence. Protecting these investments will continue to strengthen our economy, and difficult choices made today will allow us to uphold our responsibilities to future generations and position us for growth in the future.

The following sections describe the particular challenges facing the state in developing the fiscal year 2012 budget and highlights the measures proposed to bring fundamental change and innovation to the way the state does business. Graphs and tables have been provided to help illustrate many of the trends and factors affecting the state budget. Also, included within this document is a user guide and glossary to assist in navigating this budget document.

Massachusetts' Government Structure

The government of the Commonwealth is divided into three branches: the Executive, the bicameral Legislature and the Judiciary.

Executive Branch

Chief Elected Positions

Governor
The Governor is the chief executive officer of the Commonwealth.

Lieutenant Governor
The Lieutenant Governor is elected along with the Governor. Together, the two work closely to address important issues facing the Commonwealth.

Executive Council
Also referred to as the "Governor's Council," this body consists of eight members who are elected to two-year terms in even-numbered years. The Executive Council is responsible for the confirmation of certain gubernatorial appointments, particularly judges, and must approve all warrants (other than for debt service) prepared by the Comptroller for payment by the State Treasurer.

Appointed Positions

Governor's Cabinet
The Governor's Cabinet is comprised of eight gubernatorial appointees who assist the Governor in administration and policy-making. With the exception of the Secretary of Transportation, each individual serves as the chief executive of the respective secretariat and falls within the jurisdiction of the seven executive offices.

The seven executive offices are:

- Executive Office for Administration and Finance;
- Executive Office of Health and Human Services;
- Executive Office of Public Safety and Security;
- Executive Office of Housing and Economic Development;
- Executive Office of Labor and Workforce Development;
- Executive Office of Education; and
- Executive Office of Energy and Environmental Affairs.

The Secretary of Transportation, appointed by the Governor to serve as the chief executive officer of the Massachusetts Department of Transportation, also serves on the Governor's cabinet.

Secretary of Administration and Finance
The Secretary of Administration and Finance is the Governor's chief fiscal officer. The activities of the Executive Office for Administration and Finance fall within six broad categories:

- Administrative and fiscal supervision, primarily the implementation of the Commonwealth's annual budget and monitoring of all agency expenditures during the fiscal year;
- State tax law enforcement and collection of tax revenues through the Department of Revenue for remittance to the State Treasurer;
- Human resource management, the administration of the state personnel system, civil service system and employee benefit programs and negotiation of collective bargaining agreements with certain of the Commonwealth's public employee unions;
- Capital facilities management, coordination and oversight of the construction, management and leasing of all state facilities;
- State 5 year capital plan development and implementation; and
- General service administration, including information technology services.

Of note, the Secretary of Administration and Finance serves as Chairperson of the Commonwealth Health Insurance Connector Authority, Co-Chairs the Massachusetts Life Sciences Center and serves as a member of numerous other state boards and commissions.

State Comptroller

The comptroller is responsible for administering and ensuring lawful and reasoned accounting policies and practices. Among the Comptroller's responsibilities are the publication of official financial reports and oversight of fiscal management functions within all state agencies and departments. The Comptroller also administers the Commonwealth's annual state single audit and manages the state accounting system. The Comptroller is appointed by the Governor for a term coterminous with the Governor's, and may be removed by the Governor only for just cause.

The annual financial reports of the Commonwealth, single audit reports and any rules and regulations promulgated by the Comptroller must be reviewed by an advisory board. This board is chaired by the Secretary of Administration and Finance and includes the State Treasurer, the Attorney General, the State Auditor, the Chief Administrative Justice of the Trial Court and two persons with relevant experience appointed by the Governor for three-year terms. The Commonwealth's audited annual reports include financial statements on both the statutory basis of accounting (the Statutory Basis Financial Report, or SBFR) and the GAAP basis (the Comprehensive Annual Financial Report, or CAFR).

Other Elected Offices

Treasurer and Receiver-General

More commonly referred to as the State Treasurer, this individual has four primary statutory responsibilities:

- Collection of all state revenues, with the exception of agency-held funds;
- Management of both short-term and long-term investments of Commonwealth funds (excluding state employee and teacher pension funds), including all cash receipts;
- Disbursement of Commonwealth monies and oversight of reconciliation of the state's accounts; and
- Issuance of almost all debt obligations of the Commonwealth, including notes, commercial paper and long-term bonds.

In addition to these responsibilities, the State Treasurer serves as Chairperson of the Massachusetts Lottery Commission, the State Board of Retirement, the Pension Reserves Investment Management Board, the Massachusetts Water Pollution Abatement Trust and the Massachusetts School Building Authority. The State Treasurer also serves as a member of numerous other state boards and commissions, including the Municipal Finance Oversight Board.

Secretary of the Commonwealth

The Secretary of the Commonwealth, commonly referred to as the Secretary of State, is responsible for collection and storage of public records and archives, securities regulation, state elections, administration of state lobbying laws and custody of the seal of the Commonwealth.

Attorney General

The Attorney General is the chief lawyer and law enforcement officer of the Commonwealth of Massachusetts. The Attorney General represents the Commonwealth in all legal proceedings in both the state and federal courts, including defending the Commonwealth in actions in which a state law or executive action is challenged. The office also brings actions to enforce environmental and consumer protection statutes, among others, and represents the Commonwealth in public utility and automobile rate-setting procedures. The Attorney General works in conjunction with the general counsels of the various state agencies and executive departments to coordinate and monitor all pending litigation.

State Auditor

The State Auditor provides independent and objective evaluations of the Commonwealth's financial and operational activities. The State Auditor is charged with improving the efficiency of state government by auditing the administration and expenditure of public funds and reporting the findings to the public. The State Auditor reviews the activities and operations of approximately 750 state entities and verifies contract compliance of private vendors doing business with the Commonwealth.

Legislative Branch

The Legislature (officially called the General Court) is the bicameral legislative body of the Commonwealth, consisting of a 40 member Senate and a 160 member House of Representatives. Members of the Senate and the House are elected to two-year terms in even-numbered years. Each General Court meets for a two-year period. January of 2011 marked the start of the 187th General Court, which runs through January of 2013. The joint rules of the House and Senate require all formal business to be concluded by the end of July in even-numbered years and by the third Wednesday in November in odd-numbered years. The two legislative branches work concurrently on pending laws brought before them.

Lawmaking begins in the House or Senate Clerk's office where petitions, accompanied by bills, resolves, etc., are filed and recorded in a docket book. The clerks number the bills and assign them to appropriate joint committees. There are 24 of these committees, each responsible for studying the bills which pertain to a specific area (i.e., taxation, education, health care, insurance, etc.). Each committee is composed of six senators and eleven representatives, except the committees on Economic Development and Emerging Technologies, Health Care Financing and Transportation which consist of seven members of the Senate and thirteen on the part of the House.

The standing committees schedule public hearings for the individual bills, which afford residents, legislators and lobbyists the opportunity to express their views. Committee members meet at a later time in executive session to review the public testimony and discuss the merits of each bill before making their recommendations to the full membership of the House or Senate. The committee then issues its report, recommending that a bill "*ought to pass*", "*ought not to pass*" or "*as changed*" and the report is submitted to the Clerk's office.

All legislation proposing an increase in taxes or a new tax must originate within the House of Representatives. Once a tax bill is originated by the House and forwarded to the Senate for consideration, the Senate may amend it. All bills are presented to the Governor for approval or veto. The Legislature may override the Governor's veto of any bill by a two-thirds vote of each house. The Governor also has the power to return a bill to the chamber of the Legislature in which it was originated with a recommendation that certain amendments be made; such a bill is then brought before the Legislature and is subject to amendment or re-enactment, at which point the Governor has no further right to return the bill a second time with a recommendation to amend but may still veto the bill.

Judicial Branch

The judicial branch of state government is composed of the Supreme Judicial Court, the Appeals Court and the Trial Court. The Supreme Judicial Court has original jurisdiction over certain cases and hears appeals from both the Appeals Court, which is an intermediate appellate court, and in some cases, directly from the Trial Court. The Supreme Judicial Court is authorized to render advisory opinions on certain questions of law to the Governor, the Legislature and the Governor's Council. Judges of the Supreme Judicial Court, the Appeals Court and the Trial

Court are appointed by the Governor, with the advice and consent of the Governor's Council, to serve until the mandatory retirement age of 70 years.

Independent Authorities and Agencies

The Legislature has established a number of independent authorities and quasi-public agencies within the Commonwealth, the budgets of which are not included in the Commonwealth's annual budget. These include the Commonwealth Connector Authority, Massachusetts Bay Transportation Authority (MBTA), Massachusetts School Building Authority (MSBA), individual Regional Transit Authorities and other entities. Budgetary information can be requested directly from these agencies.

Local Government

All territory in the Commonwealth lies within one of the 351 incorporated cities and towns that exercise the functions of local government, which include public safety, fire protection and public construction. Cities and towns or established regional school districts provide elementary and secondary education. In addition to schools, various local and regional districts administer water and wastewater and certain other governmental functions. Cities are governed by one of many nuanced variations of the mayor-and-council or manager-and-council form. Most towns place executive power in a board of three or five selectmen elected to one or three-year terms and retain legislative powers in the voters themselves, who assemble in periodic open or representative town meetings.

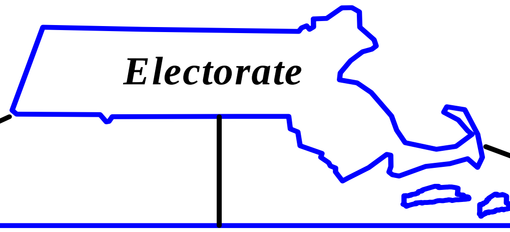
Municipal revenues consist of taxes on real and personal property, distributions from the Commonwealth under a variety of programs and formulas, local receipts (including motor vehicle excise taxes, local option taxes, fines, licenses and permits, charges for utility and other services and investment income) and appropriations from other available funds (including general and dedicated reserve funds). Because property tax levies are limited by Proposition 2½, an initiative petition approved by the voters in 1980, local governments have become increasingly reliant on distribution of revenues from the Commonwealth to support local programs and services (commonly known as "local aid"). The amount of local aid received varies significantly among municipalities.

The cities and towns of the Commonwealth are organized into 14 counties; county government has been abolished in seven of those counties. The county governments that remain are responsible principally for the operation of courthouses and registries of deeds. Where county government has been abolished, the functions, duties and responsibilities of the government have been transferred to the Commonwealth, including all employees, assets, valid liabilities and debts. On January 1, 2010, the remaining six county Sheriffs were moved within State jurisdiction.

Organizational Chart

The following organization chart identifies the present structure of state government and its constituent agencies. The Governor's House 1 budget, and legislation that will be filed concurrent to the House 1 recommendation, proposes consolidations and reorganizations of a number of agencies, including the following:

- Transfer of the Committee of Public Counsel Services from the Judicial Branch to an independent agency at the Department of Public Counsel Services.
- Transfer of the Department of Probation from the Judicial Branch to a newly created Department of Re-Entry and Community Supervision at the Executive Office for Public Safety and Security.
- Consolidation of the Bureau of State Office Buildings in to the Division of Capital Asset Management.
- Streamlining the organizational structure under the Executive Office of Labor and Workforce Development to consist of five consolidated agencies, the Department of Career Services, the Department of Industrial Accidents, the Department Labor Relations, the Department of Labor Standards, and the Department of Unemployment Assistance.



Legislative Branch

House of Representatives
Senate

Executive Branch

Governor
Lieutenant Governor
Governor's Council
Attorney General
Inspector General
Office of the Comptroller
Sheriffs
State Auditor
Secretary of the Commonwealth
Treasurer and Receiver-General
Office of Campaign and Political Finance
District Attorneys
Ethics Commission
Disabled Person Protection Commission
Independent Offices and Commissions

Judicial Branch

Supreme Judicial Court
Appeals Court
Trial Court
Committee for Public Counsel
Board of Bar Examiners
Commission on Judicial Conduct
Mental Health Legal Advisors

State Agencies

Administration and Finance
Executive Office for Administration and Finance
Appellate Tax Board
Bureau of State Office Buildings
Civil Service Commission
Department of Revenue
Developmental Disabilities Council
Division of Administrative Law Appeals
Division of Capital Asset Management and Maintenance
George Fingold Library
Group Insurance Commission
Human Resource Division
Information Technology Division
Massachusetts Office on Disability
Massachusetts Teachers' Retirement System
Operational Services Division
Public Employee Retirement Administration Commission

Public Safety
Executive Office of Public Safety and Security
Chief Medical Examiner
Criminal History Systems Board
Department of Correction
Department of Fire Services
Department of Public Safety
Department of State Police
Massachusetts Emergency Management Agency
Merit Rating Board
Military Division/ Massachusetts National Guard
Municipal Police Training Committee
Parole Board
Sex Offender Registry

Housing and Economic Development
Executive Office of Housing and Economic Development
Department of Business Development
Office of Consumer Affairs & Business Regulations
Department of Housing & Community Development
Department of Telecommunications and Cable
Division of Banks
Division of Insurance
Division of Professional Licensure
Division of Standards

Energy and Environmental Affairs
Executive Office of Energy and Environmental Affairs
Department of Agricultural Resources
Department of Conservation and Recreation
Department of Environmental Protection
Department of Fish and Game
Department of Public Utilities
Division of Energy Resources
State Reclamation Board

Transportation and Public Works
Department of Transportation (MassDot)

Labor and Workforce Development
Executive Office of Labor and Workforce Development
Department of Labor
Department of Workforce Development
Division of Industrial Accidents
Division of Labor Relations

Health and Human Services
Executive Office of Health and Human Services
Executive Office of Elder Affairs
Department of Children and Families
Department of Developmental Services
Department of Mental Health
Department of Public Health
Department of Transitional Assistance
Department of Veterans' Services
Department of Youth Services
Division of Health Care Finance & Policy
Massachusetts Commission for the Blind
Massachusetts Commission for the Deaf and Hard of Hearing
Massachusetts Rehabilitation Commission
Office for Refugees and Immigrants
Soldiers' Home, Holyoke
Soldiers' Home, Massachusetts

Education
Executive Office of Education
Department of Early Education and Care
Department of Elementary and Secondary Education
Department of Higher Education
State and Community Colleges
University of Massachusetts System

Health Care Security Trust

Board of Library Commissioners

Commission Against Discrimination

State Government Organizational Structure in Fiscal Year 2011*

**In fiscal year 2012 the Governor proposes a number of reorganizations and consolidations through the House 1 recommendation and related legislation.*

Overview of the Operating Budget Process

The annual budget is a declaration of the Commonwealth's priorities and a statement on how to allocate the limited collective resources that exist. In a recession, governments have fewer resources but the demand on public services is greater, which can make the budget development process challenging.

The operating budget supports the day-to-day functioning of state government. It pays for programs and services provided on behalf of and to the state's residents, employee salaries, utilities, supplies, insurance, and equipment repairs. The budget is a financial plan, reflecting the state's projected available resources and how it intends to use this funding to operate programs and services and meet its long-term liabilities.

Developing the annual operating budget is a lengthy process that involves all three branches of government, hundreds of agencies and thousands of stakeholders and residents. First, the Governor presents his budget recommendation to the Legislature. Then, the House of Representatives and the Senate will each separately review the Governor's budget and develop their own recommendations. Lastly, the House and Senate work together to reconcile their budgets and send the final bill to the Governor.

The Constitution and Budget Related Laws

The fiscal year is a commonly used term to describe annual budgeting period. State fiscal year 2012 extends from July 1, 2011 to June 30, 2012. In a typical year, state agencies have the authority to spend funding provided for a fiscal year over a 14-month period, after accounting for a two month "accounts payable" period through August during which final payments for costs incurred before June 30 are reconciled and made.

The budget process begins, at the latest, in the fiscal year preceding the fiscal year for which the budget will take effect. For example, planning for the fiscal year 2012 budget began no later than July 2010, a full year before it begins. State agencies develop their budget plans for the next fiscal year with the consideration on "out-years" as well, projecting the costs of current state programs and services over the next two years.

The annual budget process varies from state to state. Here in Massachusetts, the State Constitution and Massachusetts General Laws outline and govern the budgeting process. The Massachusetts Constitution requires the Governor to present a budget to the Legislature within 3 weeks of the beginning of the new session in January. State finance law (Chapter 29 of the Massachusetts General Laws) requires the Legislature and the Governor to approve a balanced budget for each fiscal year. In other words, the Commonwealth cannot spend more than it receives in revenue. Further, during the fiscal year, the Governor may approve no supplementary appropriation bills that would result in an unbalanced budget.

Funds for the Commonwealth's programs and services must be appropriated by the Legislature each fiscal year. The final budget is a law known as the General Appropriations Act (GAA). The GAA specifies how agencies and departments may spend their appropriations and allocates exact dollar amounts authorized for a specific period and purpose. The budget also lists major revenue assumptions and reflects the must up-to-date assumptions for the total amount of resources that can be budgeted from tax collections, reimbursements to the state from the federal government, and other revenues (fees, penalties) that are collected by state agencies. Agencies are not allowed to spend more than what has been appropriated to them in the GAA and supplemental budgets.

Developing Next Year's Operating Budget: FY12 General Appropriations Act

	Fiscal Year 2012 Planning
Department Planning & Secretariat Review (July-September 2010)	Department and agency staff review their policies and programs, develop future plans, and submit budget requests to their respective Cabinet secretary for review. The Cabinet Secretaries evaluate the requests and develop a Secretariat-wide budget. Secretariats were assigned a spending cap by the Executive Office for Administration and Finance (ANF) based on projections at the time of available fiscal year 2012 revenues.
Formal Budget Request (October-December 2010)	Secretariats and agencies submit spending plans to ANF. Independents, Constitutional officers and the Judiciary also submit spending plans. The consensus revenue number is announced. The Executive and Legislative Branches jointly agree and commit to a single tax revenue projection for the next fiscal year. Both the Governor's budget and the Legislature's budget will be based off this number. ANF, under the direction of the Governor's Office, prepares the Governor's budget recommendations. For this year's budget, each Secretariat held hearings across the state to solicit input on programs and services under their jurisdiction from the general public. This input was considered by agencies and ANF in the development of their spending plans.
Governor's Budget (January 26, 2011)	The formal budget begins as a bill that the Governor submits to the Legislature. According to the Constitution of the Commonwealth of Massachusetts, the Governor must propose a budget for the next fiscal year within 3 weeks after the Legislature convenes, which this year translates into the 4th Wednesday of January. In odd years, the Governor's budget is called House 1 (H.1) and in even years it is called House 2 (H.2). Accordingly, the fiscal year 2012 budget will be filed on January 26, 2011. More detailed information regarding the specific budget development process for fiscal year 2011 can be found in the "FY11 Current Year Update" section.
House Budget (February-April 2011)	The House Ways and Means Committee reviews the Governor's budget and then develops its own budget recommendation. Individual members of the House of Representatives submit budget amendments which are then debated on the House floor. Once debated, amended and voted on by the full House, it becomes the final House budget bill and moves to the Senate.
Senate Budget (February-May 2011)	The Senate Ways & Means Committee reviews both the Governor's and House budgets and develops its own recommendation. Individual senators submit budget amendments which are then debated on the Senate floor. Once debated, amended and voted on, it becomes the final Senate's budget bill.

Conference Committee Budget (June 2011)	House and Senate leadership assign members to a "conference committee" to negotiate the differences between the House and Senate bills. The conference committee report can only be approved or rejected, no additional amendments can be made.
Vetoes (June 2011)	Once approved by both chambers of the Legislature, the Governor has ten days to review it. The Governor may approve or veto the entire budget, or may veto or reduce particular line items or sections, but may not add anything. If the Governor does not act within ten days, the conference committee bill becomes law.
Overrides (June 2011)	The House and Senate may vote to override the Governor's vetoes. Overrides require a two-thirds roll-call vote in each chamber.
Final Budget (June - July 2011)	Once the Governor signs the bill with his recommended vetoes, it becomes the budget for the fiscal year. The final budget is also known as the General Appropriations Act (GAA) or "Chapter (# to be determined) of the Acts of 2011." The new fiscal year 2012 begins on July 1, 2011.

Developing Supplemental Budgets
While the GAA is the primary budget law, supplemental budgets are also passed throughout the fiscal year. A supplemental budget authorizes additional spending above GAA levels. A supplemental budget is similar to the GAA but is generally smaller in size. It addresses unforeseen growth/decline in state revenues and or additional expenses/savings. The supplemental budget process is the same as the GAA budget process; supplemental budgets are bills filed with the Clerk of the House of Representatives, debated and passed by both the House and Senate, negotiated in a Conference Committee, and signed by the Governor in order to become law.

The timeline for supplemental budget legislation is usually shorter since supplemental budgets often provide funding for unforeseen situations that need timely resolution. For example, supplemental budget funding may be necessary from year to year to ensure that the Commonwealth can pay for unanticipated additional costs for snow and ice removal. In this case, at the time the GAA became law specific assumptions for the winter's costs for snow and ice removal were in place. As the winter progresses and the state's Department of Transportation begins to manage snow and ice removal, total projected costs may change and additional funding may be necessary.

Overview of State Finance

The state's finance laws are outlined in **Chapter 29** of the Massachusetts General Laws. They require that the Governor file a balanced budget, that the House and Senate each produce a balanced budget, and that the final general appropriation act (GAA) is in balance accordingly. Any supplemental budget bill that may accompany or follow a budget cannot impair the overall fiscal balance. Typically, surplus resources at the end of any given fiscal year will be deposited into the Commonwealth's Stabilization Fund, also known as the Rainy Day Fund. Any further use of the Fund's resources must be explicitly authorized in legislation.

Prior to the Governor's submission of the budget, the Secretary of Administration and Finance and the House and Senate Committees on Ways and Means are required to reach agreement on a "consensus tax revenue forecast" from which to build their spending projections. The consensus revenue process for fiscal year 2012 is discussed in more detail later in this section. In addition to tax revenues, non-tax revenues are forecast within the Governor's budget and factor into the total amount of resources that are available to the state to support its costs in fiscal year 2012.

The Governor's budget recommendations for the fiscal year beginning July 1, 2011 and ending June 30, 2012 are included in the following budget document and companion *Issues in Brief* narrative. This submitted budget is balanced; the revenues projected to be received within the fiscal year under these recommendations are sufficient revenues to fund the expenditures proposed for fiscal year 2012. Supporting financial statements, provided in the following section, identify the major types of revenues to be collected next year and the level of expenditures they will support.

Budget Administration

With virtually no exceptions, expenditures made by an agency within fiscal year 2012 cannot exceed the level of spending authorized for an appropriation account. In limited cases, such as debt service where the Commonwealth is statutorily required to pay debt service regardless of the amount of annual appropriations, state spending may not exceed what is proposed by the Governor and appropriated by Legislature.

State finance law requires the Commonwealth to monitor revenues and expenditures during a fiscal year. As such, the Secretary of Administration and Finance is required to provide quarterly revenue estimates to the Governor and the Legislature, and the Comptroller publishes a quarterly report of planned and actual revenues. Department heads are required to notify the Secretary of Administration and Finance and the House and Senate Committees on Ways and Means of any anticipated decrease in estimated revenues for their departments from the federal government or other sources. Those same parties are also notified if a department projects that any appropriation will be insufficient to meet all expenditures required in the fiscal year by any law, rule, regulation or order not subject to administrative control.

If a revenue shortfall is identified, the Governor is required by section 9C of Chapter 29 to reduce agency appropriations or recommend a transfer from the Stabilization Fund. If additional revenues are available, the Governor may recommend a supplemental budget. At the end of the fiscal year, the Comptroller determines the statutory balance of the budgeted funds and transfers any excess funds to the Stabilization Fund.

General Fiscal Policies of the Commonwealth

The following principles and policies were used to guide the development of the fiscal year 2012 budget:

Financial Reporting

The Commonwealth possesses strong reporting capabilities, supported by accounting and payroll systems that are used consistently throughout state agencies and from which data is updated to an information warehouse.

- State agencies utilize the accounting and payroll systems to ensure adequate audit controls are in place for the purpose of reporting on the receipt and expenditure of tax dollars and other revenues.
- The presentation of the annual Comprehensive Annual Financial Report and official bond statements will continue to adhere to full disclosure.
- Websites will continue to be published to present the annual budget in an interactive format.

Revenue

- In preparation of the annual budget, a consensus revenue estimate for taxes has been agreed upon by the executive and legislative branches, and will serve as the basis for building the budget.
- All revenue received by departments will be deposited with the Treasurer and recorded in the Accounting system, ensuring the timely and transparent receipt of all state funding sources.

Cash Flow

- The Cash Management Division of the State Treasurer's office accounts on a daily basis for cash received into over 600 separate accounts of the Department of Revenue and other Commonwealth agencies and departments.
- The State Treasurer, in conjunction with Comptroller and the Executive Office for Administration and Finance, monitors cash to maximize the Commonwealth's return on investment and minimize the use of borrowing.
- Formal cash flow projections for the then current fiscal year are submitted to the House and Senate Committees on Ways and Means on or before each August 31, November 30, February 28 and May 31. The

projections include estimated sources and uses of cash, together with the assumptions from which such estimates were derived and identification of any cash flow gaps.

- The State Treasurer's office, in conjunction with the Comptroller and the Executive Office for Administration and Finance, develop quarterly and annual cash management plans to address any gap identified by the cash flow projections and variance reports.
- The State Treasurer's office oversees the issuance of short-term debt to meet cash flow needs, including the issuance of commercial paper.

Expenditures

- The Comptroller is responsible for oversight of fiscal management functions, establishment of accounting policies and practices and publication of official financial reports.
- The Comptroller maintains the Massachusetts Management Accounting and Reporting System (MMARS), the centralized state accounting system that is used by all state agencies and departments but not independent state authorities. MMARS provides a ledger-based system of revenue and expenditure accounts enabling the Comptroller to control obligations and expenditures effectively and to ensure that appropriations are not exceeded during the course of the fiscal year.
- MMARS also tracks receivables, payables, fixed assets and other processes management.
- The Comptroller will annually review policies governing transactions in MMARS.

Expenditure Controls

- The amount of all obligations under purchase orders, contracts and other commitments for the expenditures of moneys are required to be recorded as encumbrances. Once encumbered, these amounts are not available to support additional spending commitments.
- As a result of these encumbrances, agencies can use MMARS to determine at any given time the amount of their appropriations available for future commitments.

Internal Controls

- The Comptroller establishes internal control policies and procedures in accordance with state finance law. These policies require all departments to develop and maintain an internal control plan. Agencies are required to adhere to such policies and procedures.
- All unaccounted-for variances, losses, shortages or thefts of funds or property must be reported to the State Auditor, who is authorized to investigate and recommend corrective action.

Reserves

- The Commonwealth will aggressively seek to replenish the Commonwealth Stabilization Fund when able to do so.
- Capital gains tax revenues that exceed $1 billion will be deposited into the Fund to better calibrate spending with reliable revenue streams and to build a cushion against future economic and fiscal uncertainty.
- Any one-time tax revenues collected as a result of a judgment or settlement of outstanding tax litigation that exceeds $10 million will be segregated and deposited into the Stabilization Fund, ensuring that this non-recurring revenue source is not relied on for general budget needs.

Debt Affordability

- The Commonwealth conducts an annual debt affordability analysis to determine the affordable level for the administrative bond cap (determining annual borrowing levels).
- Required funding for debt service and other debt-like instruments will not exceed 8% of budgeted revenues.

Capital Budget

- Bond-funded capital spending will be limited by an annual administrative bond cap. Annual growth in that cap will not exceed $125 million between fiscal year 2012 and fiscal year 2015.
- An annual capital budget will be developed and will focus on affordability, targeted investments in projects that maintain our existing infrastructure and/or promote economic growth, and transparency.

Pensions

- The Commonwealth will continue to follow a pension funding schedule to address our unfunded liability and to pursue reforms that will reduce costs over the long term.

Other Post-Employment Benefits

- The Commonwealth will continue to pursue adoption of a funding schedule to fully fund public employee retiree health care benefits and to pursue reforms that will reduce costs over the long term.

Strategic Fiscal Policies

In developing the fiscal year 2012 budget, special attention was paid in the following areas:

- Cost-containment in the state's various health care programs, including the costs for current and retired state employees and health coverage for low-income and unemployed residents in the Commonwealth.
- Preservation of programs to ensure residents can lead safe and healthy lives and find long-term employment in a competitive global economy:
  - Addressing youth and urban violence through investments in our youth and communities
  - Closing the achievement gap and protecting education funding as a cornerstone of long-term economic growth and opportunity.
  - Increasing job creation through investments that enhance Massachusetts' ability to compete for the jobs and businesses of tomorrow, such as green technology and the life sciences, while ensuring a more competitive environment for the state's private employers in more traditional sectors.
  - Ensuring the state's most vulnerable populations, particularly the disabled and those who have served our country, can continue to receive assistance and life-changing services from the state where needed.
- Adopt government reforms that promote efficiency and sustainability of services and ensure state dollars are stretched further in challenging fiscal times.
  - Pursuing shared service models across state government more aggressively for the most-effective administration and operation of state agencies and programs.
  - Improving state purchasing and procurement processes to leverage state buying power and drive further cost savings.
  - Identifying state functions and activities, such as facility management, that can be better managed and coordinated centrally and flexibly allow the state to allocate resources where needed.
- Identify additional recurring revenues to support worthwhile programs while recognizing the state cannot afford to maintain all programs and services that have been operated in the past.
- Reduce the use of temporary or one-time resources to balance the budget.

Overview of Budget Funds

Government Fund Types account for the general governmental activities of the Commonwealth and are organized as follows:

Budgeted Funds are the primary operating funds of the Commonwealth. They account for all budgeted governmental transactions. Typically, the level of expenditures made annual from these fund sources is "subject to appropriation", meaning that no payments can be made from these funds until they are explicitly authorized in the state budget. The main budgeted funds include the General Fund, the Commonwealth Stabilization Fund, the Massachusetts Tourism Fund, and the Commonwealth Transportation Fund, which are identified by the Comptroller as the operating funds of the Commonwealth. The Governor's fiscal year 2012 proposal will shift the Workforce Training Fund from a budgeted fund to a non-budget special revenue fund.

Non-Budgeted Special Revenue Funds are established by law to account for specific revenue sources that have been segregated from the budgeted funds to support specific governmental activities such as federal grants, funds related to the tobacco settlement and the operations of the state lottery. Typically, these funds are available annually to one or more agencies for dedicated purposes, but do not require annual legislative approval for the use of the funding. Most funds are subject to annual reporting rules and all funds are subject to state accounting and audit practices.

Capital Projects Funds account for financial resources used to acquire or construct major capital assets and to finance local capital projects. These resources are derived from proceeds of bonds and other obligations, which are generally received after related expenditures have been incurred, operating transfer authorized by the Legislature and federal reimbursements. Deficit balances in the Capital Projects Funds represent amounts to be financed.

Fiduciary Funds account for assets held by the Commonwealth in a trustee capacity (Trust Funds), or as an agent (Agency Funds) for individuals, private organizations, other governmental units, and/or other funds.

Expendable Trust Funds account for trusts whose principal and investment income may be expended for a designated short-term purpose. They typically are created administratively for a brief period to allow a state agency to collect one-time revenue and spend this funding for a dedicated purpose. For example, the Department of Public Health receives funding from private organizations from time to time to conduct research and studies on specific issues, and must collect and segregate funding dedicated for this purpose from all other funding sources.

Nonexpendable Trust Funds account for trusts whose principal cannot be spent.

Post Employment Benefit Trust Fund account for the net assets available for plan benefits held in trust for State Employees' and Teachers' Retirement Systems and Other Post Employment Benefits (OPEB) for retirees.

Agency Funds account for assets the Commonwealth holds on behalf of others. Agency Funds are custodial in nature and do not involve measurement of operations.

Individual Budgeted Funds

Statutory balance is defined as *a measure of the fiscal condition which includes current year budgeted revenues and expenditures plus any designated revenues from prior years, stabilization deposit and funds carried forward.* It also includes any use of stabilization or any other non-budgeted reserves. A more general discussion of the funds is below:

The *General Fund* is the Commonwealth's primary governmental fund. All governmental activities not specifically directed to another fund are accounted for in the General Fund. As a result, most budgeted expenditures of the Executive secretariats, the Legislature, Constitutional offices, Judiciary, institutions of higher education and independent commissions are paid for from the General Fund. It similarly receives a significant portion of sales, individual income and corporate taxes, and the full amount of most other governmental taxes. It also receives federal reimbursement generated by the Commonwealth's Medicaid expenditures.

The *Commonwealth Transportation Fund* accounts for road and highway use revenues, including the gas tax, registry fees and 0.385% of the sales tax. The fund is used to pay debt service associated with highway maintenance and construction projects and provides funding for the operation of the independent Massachusetts Department of Transportation (MassDOT). Established as part of the historic transportation reforms implemented in fiscal year 2010, this fund replaced the former *Highway Fund* as the principal source of transportation related revenues and expenditures for the Commonwealth.

The *Massachusetts Tourism Fund,* authorized in section 35J of Chapter 10 of the General Laws, is funded with 35 percent of the State's annual revenues received from the hotel occupancy tax authorized in section 3 of Chapter 64G. In fiscal year 2011, Tourism Fund revenues are estimated to total $41 million. The Fund's use is prescribed in Chapter 10, which includes a formula that assigns various funding levels for tourism promotion programs and activities including the Massachusetts Office of Travel and Tourism, regional tourism promotion agencies, the Massachusetts Office of International Trade and Investment, the Cultural Facilities Fund, and the Massachusetts Convention Center Authority. While funding for the purposes prescribed in the section are being made in this budget, the specific requirements of the fund have been suspended through an outside section in the Governor's fiscal year 2012 proposal.

The *Marine Recreational Fisheries Development Fund* accounts for all recreational saltwater fishing permit fees collected by the director of the division of marine fisheries. Fees collected in this fund shall be used for the development and administration of the recreational saltwater fishing permit program, to support science and conservation programs designed to improve recreational saltwater fishing and other recreational saltwater fishing improvement programs.

The *Commonwealth Stabilization Fund* is a reserve to enhance the Commonwealth's fiscal stability. (A later section describes the Stabilization Fund in more detail.)

Administrative Control Funds account for the revenues generated by certain administrative functions of government, for which the Legislature has required that separate funds be established. These funds include:

- *Temporary Holding Fund* –The fund accounts for cumulative tax revenues during the fiscal year in excess of permissible tax revenues as defined in Section 6A of Chapter 62F of the General Laws. The fund balance is transferred annually to the Stabilization Fund only to the extent that stabilization funds are used to fund expenditures of the Commonwealth. Overall, any remaining balance is transferred to the General Fund.

- *Intragovernmental Service Fund* – Accounts for the charges of any state agency for services provided by another state agency, for example, charges levied by the Human Resources Division for workers' compensation costs.

The *Inland Fisheries and Game Fund* accounts for revenues from license and permit fees for inland fishing, hunting, trapping, and sporting licenses and revenue-producing stamps or the sales of land, rights and properties, gifts, interest, and federal grant reimbursements. These revenues are used for developing, maintaining and operating the Division of Fisheries and Wildlife within the Department of Fish and Game. Annual spending from this fund is subject to annual appropriation by the Legislature, and any unexpended funds remain in the Fund for future use for related purposes.

The *Substance Abuse Prevention and Treatment Fund*, established in the fiscal year 2011 General Appropriations Act, is funded with the proceeds from the fiscal year 2010 removal of the sales tax exemption from alcohol. The revenues were used for public health programs such as alcohol and tobacco addiction services, childhood health and nutrition services, and violence prevention. On November 2, 2010 the state's voters adopted Question 1 which reinstated the exemption of retail sales of alcohol from the states 6.25 percent sales tax. Therefore the Substance Abuse Prevention and Treatment Fund no longer has a dedicated revenue stream to support these programs in fiscal year 2012. However, the Governor's fiscal year 2012 budget recommendation will include funding for these programs through General Fund appropriations.

The *Workforce Training Fund*, authorized in section 2RR of Chapter 29 of the General Laws and administered by the Executive Office of Labor and Workforce Development, provides employers with matching grants of up to $250,000 or more to help train new and incumbent workers. It was established in July 1998, and financed entirely by Massachusetts employers. In fiscal year 2011 the Fund was financed by an employer surcharge of .075% on employees' wages, paid concurrently with payments into the Unemployment Insurance Trust Fund. Annual state revenues from employer contributions total approximately $19 million, and state appropriations for training grants are continually rolled forward into future fiscal years to provide for multiple-year grant awards. House 1 includes a reform to the funding structure of the Workforce Training Fund by funding the program through an "off-budget" trust fund. This change will be responsive to private employers concerns that annual WTF contributions have been diverted in the past from job training initiatives and used for broader budget purposes.

Spending Plan and Budget Proposal Development

The Executive Office for Administration and Finance (ANF) is the state agency responsible for preparing the Governor's budget recommendations and for oversight of the annual budget enacted by the Legislature, known commonly as the General Appropriations Act or the GAA. Under state law, every state agency is required to annually prepare a budget for review and evaluation by the Secretary for ANF. The spending plan typically includes expenditure and revenue estimates for the current fiscal year (2011) as well as the agency's anticipated expenses and receipts for the next fiscal year (2012) based on the assumption that they will maintain the same level of services and programs from one year to the next.

In July of each year, after the General Appropriation Act (GAA) is signed, agencies present spending plans to the Executive Office for Administration and Finance (ANF) to delineate how funds appropriated for the current fiscal year will be spent. These spending plans reflect each agency's plans to operate their programs and services for the current fiscal year. Agencies are also requested to reflect any changes that may be necessary to their operating budgets, whether savings or increased costs, that will result from projects and investments made through the five-year capital plan.

For fiscal year 2011, agencies had to adjust their spending plans to account for the loss of revenues from the Federal Medical Assistance Percentages (FMAP) that the legislature assumed in the budget they sent to the Governor. Since congress had not yet enacted the extension of this revenue, the Governor vetoed all funding related to it. The Governor's veto action forced agencies to react to the loss of the unrealized revenue, and therefore, in addition to agencies preparing spending plans during the summer of 2010, they also developed detailed implementation plans on how they would manage within the reduced funding levels. These implementation plans were developed and vetted in July and spending plans were filed with ANF for review and approval in August.

Fiscal Year 2012 Budget Development

During the months of August and September agencies developed their fiscal year 2012 spending plans using their approved fiscal year 2011 budgets as the base to inform their recommendations for fiscal year 2012. In developing budget recommendations, agencies incorporate projected changes in the programs they provide, such as anticipated changes in staffing, caseload growth, or increases in fixed costs such as fuel and energy costs. Agencies also take into account changes in laws, regulations and policies that will impact programs and services for the next year. Based on revenue projections and the loss of one-time federal stimulus funds and other one-time funds used in fiscal year 2011, agencies were asked to focus on developing spending plans for fiscal year 2012 with an emphasis on controlling or preventing growth in spending over the projected fiscal year 2011 spending levels.

Despite that fact that revenues are growing as the economy recovers, tax revenue growth will not be sufficient to offset the loss of federal reimbursements that were available on a temporary basis through the American Recovery and Reinvestment Act (ARRA) to support the operating budget. To address this budget gap, ANF established spending parameters that would be necessary in fiscal year 2012 to balance the state's budget. Agencies were required to submit proposals that would ensure that total spending fell below fiscal year 2011 appropriated levels. These plans were submitted to ANF and serve as the base for the Governor's fiscal year 2012 budget recommendations.

On December 14th, the annual Consensus Revenue hearing was held by the Administration, the Senate and the House. The three branches received testimony for the Department of Revenue and other economist regarding the amount of tax revenue that could be expected for fiscal years 2011 and 2012. While the testimony suggested that revenues would continue to increase and that the state's economy was recovering, the economists also warned of the continued pressure on caseload driven programs such as Medicaid, housing and welfare programs, as well as the impact of the loss of the federal stimulus funds.

Throughout the fall, ANF continued to work with agencies to develop their spending proposals. Agencies were given the opportunity to review and revise the line items, make reform and re-organization proposals and other changes necessary to live within budgetary parameters and meet core requirements of state government. Following the submission of spending targets, ANF worked with each secretariat to assess the impact of reductions and identify which cuts will be most challenging for agencies to implement. As part of its gap closing activities, ANF has sought to mitigate these reductions to the greatest extent possible.

One methodology ANF implemented to achieve this goal was the creation of an Inter-Secretariat Budget Team (ISBT) to identify and develop additional cost-saving proposals. The team members were selected from across the Secretariats and were charged with developing innovative ideas that would help to mitigate budgetary reductions and improve how government works. This team worked with ANF throughout the budget process and will remain intact after the submission of the fiscal year 2012 budget to ensure timely implementation of the approved solutions.

Fiscal Year 2012 Post House 1 Process

In preparation for the start of fiscal year 2012 (July of 2011), ANF will continue to work with agencies to develop implementation plans well ahead of the beginning of the fiscal year. As part of the H.1 budget development process most agencies have successfully identified areas already where reductions to programs and services will be necessary or where they may capitalize on efficiencies. However, due to the complexity of some recommended programmatic changes, in some cases agencies have not yet been able to determine exactly how they will restructure programs to live within funding levels recommended in H.1. The implementation planning process led by ANF helps to best ensure that all necessary steps are completed to by the beginning of fiscal year 2012 to ensure that agencies will be able to operate at reduced funding levels.

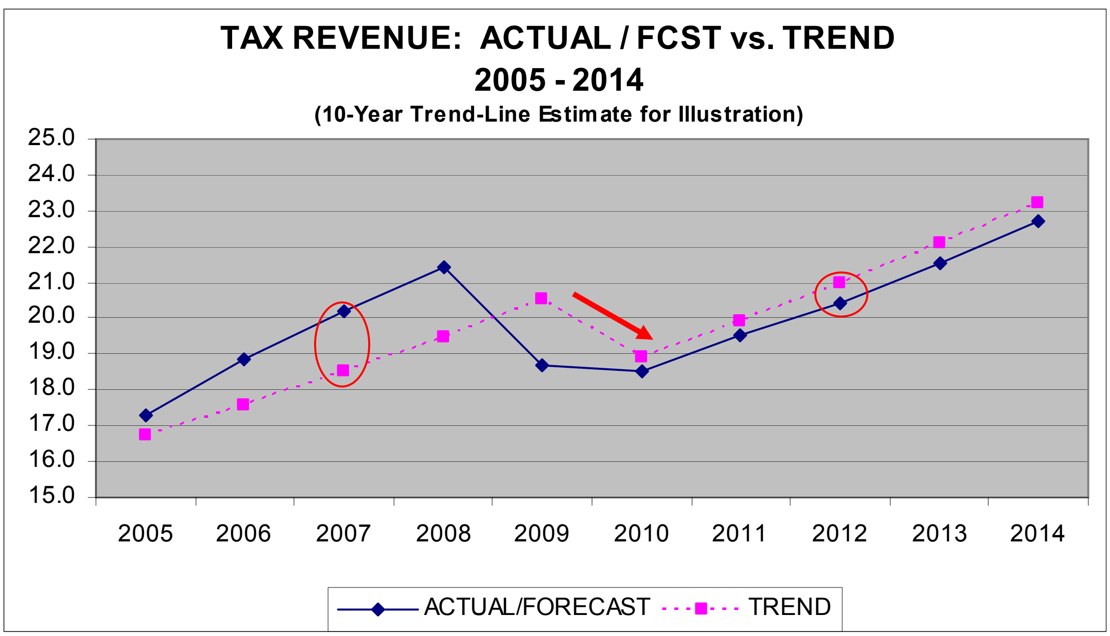
Long-Term Budget Forecasting

The Patrick administration has been working to enhance its long-term financial planning based on best practices prescribed by the Government Finance Officers Association (GFOA). Best practices include the use of a sound conceptual approach, ensuring that near-term decisions measure long-term impacts, and developing a solution framework that is aligned with policy goals. The Commonwealth has implemented a conceptual approach of "structural balance" that is designed to delineate among different causes of fiscal imbalance. The application of this approach identifies three critical challenges facing the Commonwealth: a remaining structural deficit due to the significant reduction in tax revenue since the recession, cost inflation on safety net and health care programs, and the need to improve policy measures to address economic volatility. Each of these challenges is a central feature of our FY12 budget proposal as further described in the conclusion to this section.

Structural Balance Approach and Analysis

The goal of structural balance is to base spending on policy priorities and a predictable level of sustainable revenue. Our supporting analysis includes a five-year forecast for revenue and spending based on historical trends as well as the outlook for the state economy. The forecast includes a projection of tax revenue, based on input from local economists, that also provides the basis to develop an estimated long-term trend-line for tax revenue. The forecast indicates that the state economy will be below trend during a four year recovery period beginning in fiscal year 2012 before reaching a "steady-state" level of long-term tax revenue growth of approximately 5% in 2016. The imputed trend-line was developed using the tax revenue figures from 2016 and discounting revenue back by the estimated 5% annually. A similar approach was taken to develop a pre-recession revenue trend-line and select results of this analysis are highlighted in the exhibit below. (note: the time horizon in the exhibit has been truncated in order to emphasize the key findings discussed below).

Exhibit 1

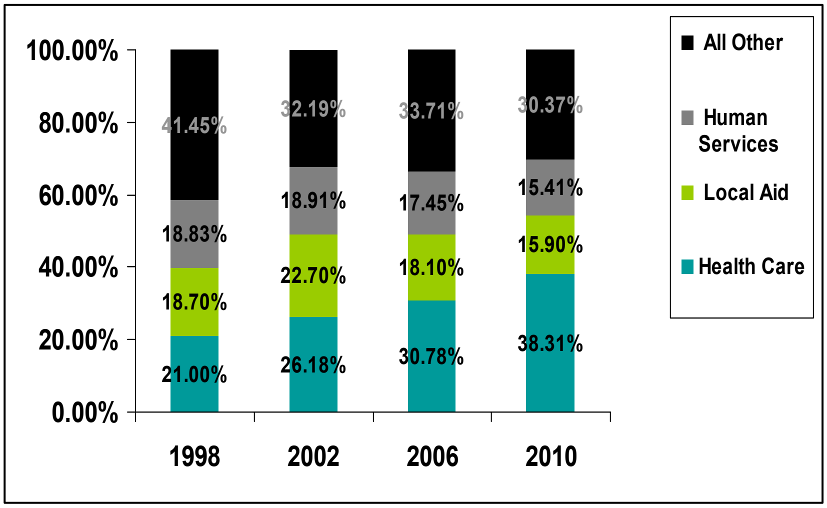


The results of this analysis provide three useful insights into our near-term fiscal challenges. First, tax revenue in FY07 (i.e. pre-recession) was approximately $2 billion greater than the then current trend-line. Second, the impact of the recession on this trend-line after FY09 was a significant downward shift of an additional $2 billion. Finally, the outlook for the economy suggests that recovery in tax revenue will be only modest: approximately $500 million based on the difference between the trend and forecast for tax revenue in FY12. The combined impact of these effects is that the FY12 budget will have approximately $5 billion less in available resource than we had in FY07 on an inflation adjusted basis, with an expectation that only 10% of this amount will be re-couped during the recovery.

The estimates of tax revenue were done in tandem with trend based projections for spending that are largely influenced by health care cost inflation. Health care costs in the state have been growing at 8-9% which has had the effect of increasing the share of health care costs from 31% to 38% over the four year period ending with

FY10 (Exhibit 2). The impact of this increase combined with the reduction in revenue sources described above, is that the Commonwealth will **have approximately 25% less in resource available for non-health care spending in FY12 than was available in FY07**.

Exhibit 2



The growth rate of health care costs also suggests that there could be a further squeeze on other spending and a risk of increasing structural deficits if health care cost inflation cannot be addressed. If current trends continue, for example, the growth in total state spending by FY15 would be approximately 6% (driven by an 8-9% spending rate for health care and a 3% rate for most other programs) as compared to an estimated revenue growth rate of 5%. The 1% differential would result in additional structural deficits of nearly $400 million annually, providing a clear indication that the current levels of health care cost inflation are not sustainable.

The Application of Long-Term Planning to Inform Near-Term Decisions

The structural balance analysis has informed our understanding of the state's fiscal imbalances and our recommendations to address these challenges in the FY12 budget. The revenue forecast and trend-line allows us to employ the $500million cyclical shortfall as a guideline on the maximum use of one time resources that are sustainable over time. Any spending in excess of this amount would continue to sustain a structural deficit or require budgetary spending that is not sustainable. The FY12 budget includes use of $385 million in one time resources, well within the sustainable level based on our cyclical shortfall. This is based in part on the assumption that the state would also restrain spending during a strong economy when tax revenue is above the then current trend-line (see Managing Economic Volatility in the solutions section below).

A Solution Framework Aligned with Policy Goals

The Governor's House 1 proposal for fiscal year 2012 addresses the state's key fiscal challenges through a series of reforms and initiatives that have been informed by our analysis of the state's long-term fiscal outlook. They include:

- Spending reductions and cost-savings to address our structural deficit.

- Lowering Health Care Cost Inflation
  - Proposed strategies that lower health care cost for fiscal year 2012 while we continue to work on longer-term solutions like payment reform.
  - These strategies have been developed with a commitment to maintain Massachusetts status as the nation's leader in health coverage, while recognizing that health care cost inflation must be addressed.

- Managing Economic Volatility
  - Reduce our use of one-time resource to $385 million, down over $2.7 billion from the amount used in fiscal year 2009 and within the $500 million limit established by our long-term financial analysis.
  - Implementing a new law that limits the use of Capital Gains revenues in the budget, the state's most volatile revenue source.
  - Requiring all tax and legal settlements over $10 million to be deposited into the Stabilization Fund.

Fiscal Year 2011 Update

When the Governor signed the fiscal year 2011 budget into law on June 30, 2010, the budget totaled $29.432 million in spending, an estimated 1.4 percent increase from fiscal year 2010 (including state pension costs this amount totaled $30.873 billion). The Governor also vetoed approximately $457 million in spending from the budget, accounting for the $372 million in budgeted federal revenues that had not yet been approved by the US Congress and the picture remained unclear whether federal action could be relied upon. The Legislature overrode approximately $15 million of the Governor's vetoes, increasing total fiscal year 2011 GAA spending to $29.448 billion. At the time the Governor signed the budget he indicated that state agencies, at their current funding levels in the GAA, would need to implement a number of spending reductions within state programs and personnel in order to manage to their available funding.

It is important to note that the fiscal year 2011 budget relied on $2.0 billion of one-time resources, provided mainly from federal stimulus resources (outlined in the table below).

FY2011 One-Timers $s in millions	
Loss of One-Timers:	**2,016.9**
Federal Stimulus (ARRA):	1,552.1
State Fiscal Stabilization Fund	*96.0*
Enhanced FMAP Revenue	*1,244.4*
Other ARRA	*11.7*
EduJobs Funding	*200.0*
Other One-Time Sources:	464.8
Special Disabilities Workload	*160.0*
Special Education (IDEA)	*101.3*
Debt Service Restructuring	*100.0*
Quasi Public Contributions	*25.0*
Trust Sweeps (incl. Springfield)	*58.5*
Other One-Time Solutions	*20.0*

Because of the these one-time resources, the state was spending an additional $397 million outside of its fiscal year 2011 operating budget to support costs that would traditionally be supported through budgeted resources. These items include $101 million in financial reimbursements to school districts for special education costs, $200 million in EduJobs funding provided to school districts for K-12 costs and $96 million in funding for K-12 aid and higher education from the ARRA-funded State Fiscal Stabilization Fund. For comparisons between fiscal year 2011 and fiscal year 2012 spending later in this document, these items are included in order to provide a fuller comparison of the changes in spending between the two fiscal years.

Fiscal Year 2011 Spending Adjustments ($s in millions)	
State Fiscal Stabilization Fund:	*96.0*
EduJobs Funding:	*200.0*
Special Ed. Reimbursements:	*101.0*
total	**397.0**

In August 2010, the US Congress adopted the “Keep Our Educators Working Act of 2010”, commonly known as EduJobs. This legislation provided approximately $449 million in additional federal reimbursements to the state for fiscal year 2011 by extending enhanced Medicaid reimbursements for an additional six month period. In addition, the federal legislation made $204 million in funding available to the state’s public school systems in order to support their efforts to retain or hire teachers and other critical education personnel. This latter funding allowed the state to increase funding to school districts across the state by $200 million ($4 million was retained by the state to administer the funding and related functions) above initial fiscal year 2011 levels and shift approximately $50 million in federal stimulus aid that had originally been budgeted for K-12 aid to the state’s public higher education campuses.

The $449 million in additional Medicaid revenue was provided by the US Congress to ensure states could mitigate some of the planned reductions in employees and cuts to programs and services. Since the funding was subject to appropriation, the Governor and the Legislature worked to development a supplemental budget bill that could address some of the most pressing funding deficiencies, such as in the state’s Department of Corrections, low-income health care programs such as MassHealth and emergency family homeless services. In addition, the Legislature and the Governor agreed to forego the use of $195 million in state reserves in fiscal year, allowing these to be used in future years when federal stimulus aid would no longer be available to the Commonwealth. Chapter 359 was signed by the Governor on October 15, which appropriated $713 million ($294 million of which was provided to make additional hospital payments with corresponding federal revenues). Chapter 359 spending was offset by $216 million in additional revenues, primarily from increased federal Medicaid reimbursements.

A further supplemental appropriation bill was adopted by the Legislature and signed into law on January 4, which provided an additional $333 million ($179 million after accounting for offsetting federal reimbursements). The bulk of this funding was to support increased caseload demand and utilization of the state’s low-income health care programs and other safety net services.

In addition to supplemental budgets already signed into law, the Executive Office for Administration and Finance (ANF) projects additional funding exposures for safety net and unanticipated events that may require additional funding through the remainder of fiscal year 2011. These funding exposures total $242 million. ANF will continue to assess over the course of the year those cases where these exposures may require additional funding, and will seek supplemental funding from the Legislature where it is deemed absolutely necessary.

After accounting for these changes, the table below outlines the total estimated spending for fiscal year 2011.

FY2011 Estimated Spending $s in millions	
FY2010 Spending	29,047
FY2011 GAA	29,448
PACs	*111*
Supplemental Budget - Chapter 359 of 2010	*713*
Supplemental Budget - Chapter 409 of 2010	*333*
Potential Exposures (not yet appropriated)	*242*
Projected FY2011 Surpluses	*(129)*
FY2011 Estimated Spending	**30,720**
FY2011 GAA - % Change from FY2010 Spending	**1.4%**
FY2011 Estimated Spending - % Change from FY2010	**5.8%**

Fiscal Year 2011 Tax Revenue Update

The original consensus tax revenue estimate adopted in the fiscal year GAA totaled $19.050 billion. After accounting for $48 million in tax initiatives adopted for fiscal year 2011 and the “sales tax holiday” signed into law by the Governor in July 2010, the revised consensus figure was $19.078 billion, or 2.9 percent more than was collected in fiscal year 2010.

Tax Collections, FY2010 vs. FY2011 ($s in millions)	
Fiscal Year 2010 Collections:	18,544
Fiscal Year 2011 Consensus:	19,078
Projected Growth	534
% Growth	2.9%

Since July 2010, Massachusetts tax revenue has been performing above the monthly estimates. The increase has been experienced across all major tax categories as well as one-time tax collections from settlements with taxpayers that were not assumed in the original fiscal year 2011 forecast. The Department of Revenue (DOR) and ANF closely monitor the state revenue collections over the fiscal year and consult regularly with nationally-recognized revenue forecasters in order to assess any trends or other factors compared to the consensus forecast. Through December 2010 total tax collections equal $755 million above the year-to-date estimates, or 4.0 percent growth above the $19.078 billion consensus figure. Consequently, on January 18 the Secretary of ANF revised the fiscal year 2011 tax revenue estimate to $19.784 billion.

Tax Collections, FY2011 Consensus and Revised ($s in millions)	
Original FY11 Consensus:	19,078
Revised FY11 Consensus:	19,784
Projected Growth	706
% Growth	3.7%

On November 2, 2010 the state's voters adopted Question 1 which re-instated the exemption of retail sales of alcohol from the state's 6.25 percent sales tax. DOR estimates that the fiscal year 2011 impact from this change will be the loss of tax revenues totaling $46 million, annualizing to $110 million in fiscal year 2012. This revenue loss has been incorporated into the updated revenue projections for each fiscal year.

Fiscal Year 2011 Non-Tax Revenue Update

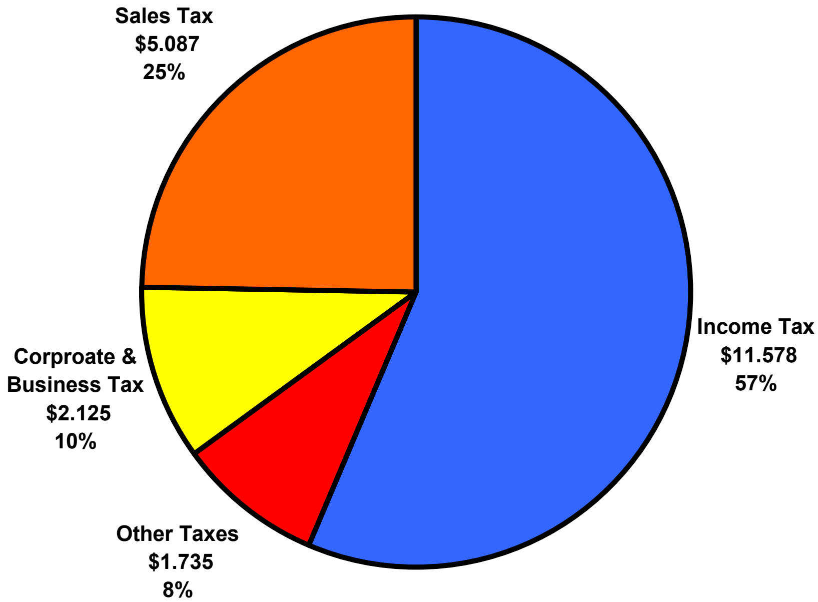
A major adjustment that should be noted in fiscal year 2011 is that ANF is no longer assuming $160 million in federal revenues related to the Special Disabilities Workload. This revenue source corresponds to federal revenues that the state is owed to offset expenditures for services provided by the state to disabled persons who were determined to be Medicare-eligible persons. The state had assumed that Congress would authorize this reimbursement this fiscal year. While ANF and the Executive Office of Health and Human Services continue to actively press the federal government for this reimbursement –which is owed to dozens of other states, as well-ANF believes it is fiscally prudent at this time to remove the funding as a budgeted resource for the fiscal year 2011 budget.

Fiscal Year 2012 Tax Revenues

Tax Revenues

Tax revenues comprise nearly 62% of all revenues (including new revenues proposed in the H.1 recommendations) used to support the Commonwealth's operating budget. Each year the Administration and the House and Senate consult with economists and other groups to gather information and analysis on the condition of the U.S. and Massachusetts economies. They use that information to project state tax revenue for use in the state budget. The following is a general description of the consensus revenue process.

FY12 Consensus Tax Revenue
Estimate of $20.525 (in $ Billions)



General Information Regarding Consensus Revenue

The consensus revenue process is required under M.G.L. c.29, s.5B and states that on or before January 15 the Secretary for Administration and Finance shall meet with the House and Senate Committees on Ways and Means and shall jointly develop a consensus tax revenue forecast for the budget for the next fiscal year, which shall be agreed to by the Secretary and the House and Senate. The law requires that the consensus revenue estimate be placed before the General Court in the form of a joint House and Senate Resolution for full consideration.

On December 14, 2010 the Secretary for Administration and Finance and the House and Senate Committees on Ways and Means held a public hearing in Boston and heard testimony from the Massachusetts Department of Revenue (DOR), the Massachusetts Taxpayers Foundation and the Beacon Hill Institute, and economists from the University of Massachusetts-Boston and Northeastern University. The three branches subsequently agreed upon a fiscal year 2012 tax revenue estimate of $20.525 billion, consistent with testimony presented at the hearing.

As part of the statutorily required consensus revenue process, the Secretary, House and Senate also agree on the amount of tax revenues that will need to be transferred to support the State's Pension Fund, the School Building Authority and the MBTA (Massachusetts Bay Transportation Authority). For fiscal year 2012, these transfers are estimated to total $2.936 billion and will be directed to the following funds:

- School Modernization and Reconstruction Trust Fund = $ 678.1 million
- MBTA State and Local Contribution Fund = $ 779.6 million
- Pension Reserves Investment Trust Fund = $ 1.478 billion

Basis for the Fiscal Year 2012 Consensus Revenue Forecast

Fiscal year 2011 tax revenues are estimated to be $19.784 billion, representing an actual increase of 6.7% and a baseline increase of 5.5% from fiscal year 2010 collections (the baseline calculation adjusts for the impact of tax law and processing changes, so it is a better indicator of underlying economic activity). Through December 2010, fiscal year 2011 year-to-date tax revenues were up 10.1% actual and 7.5% baseline, and were $755 million above the year-to-date benchmark based on the GAA fiscal year 2011 estimate of $19.078 billion (including the impacts of the Economic Development Bill and the Sales Tax Holiday in August 2010). It is expected that as the economy continues to recover, tax collections for the remainder of fiscal year 2011 will increase by $357.5 million, or 3.6% actual, and $378.9 million, or 3.9% baseline, from the same period in fiscal year 2010.

The fiscal year 2012 consensus tax revenue estimate is $20.525 billion, representing revenue growth of 3.7% actual and 5.3% baseline from the fiscal year 2011 revised estimate of $19.784 billion. The fiscal year 2012 estimate assumes that the national and state economies will continue a moderate recovery throughout the fiscal year. In developing the consensus estimate, the Commonwealth relies on economic forecasts from Moody's Economy.com, Global Insight, and the New England Economic Partnership (NEEP). The economic forecasts upon which the consensus revenue estimate is based are as follows:

- The national economy started to recover from the Great Recession in the second half of 2009, but the recovery has slowed down recently. After strong growth in the fourth quarter of 2009 (5.0%, annual rate) and the first quarter of 2010 (3.7%, annual rate), the growth in real GDP slowed down in the second (1.7%, annual rate) and third quarter of 2010 (2.5%, annual rate), and is expected to remain slow until the second half of 2011. Real GDP growth for the full fiscal year 2011 is projected to be 2.5%~2.6% compared to growth of -2.8% in fiscal year 2009 and 0.7% in fiscal year 2010. In fiscal year 2012, real GDP growth is projected to range from 2.6% to 3.5%;

- Massachusetts employment is expected to increase by 1.0% to 1.2% over the remainder of fiscal year 2011, and by 1.0% to 1.2% for fiscal year 2011 as a whole. For fiscal year 2012, Massachusetts employment is expected to change by 0.5% to 1.2%;

- Massachusetts personal income (excluding capital gains) is expected to grow by 2.9% to 3.0% over the remainder of fiscal year 2011 and 2.8% to 2.9% for fiscal year 2011 as a whole. For fiscal year 2012, Massachusetts personal income is projected to grow by 3.5% to 5.0%;

- Massachusetts wages and salaries are projected to increase by 2.3% to 3.2% for the remainder of fiscal year 2011 and 2.2% to 2.9% for the year as a whole. For fiscal year 2012, the growth in Massachusetts wages and salaries is projected to range from 4.4% to 5.2%;

- Massachusetts retail sales growth is expected to range from 4.5% to 5.0% over the remainder of fiscal year 2011 and 4.2% to 4.9% for the fiscal year as a whole. For fiscal year 2012, Massachusetts retail sales are projected to grow by 5.0% to 5.5%;

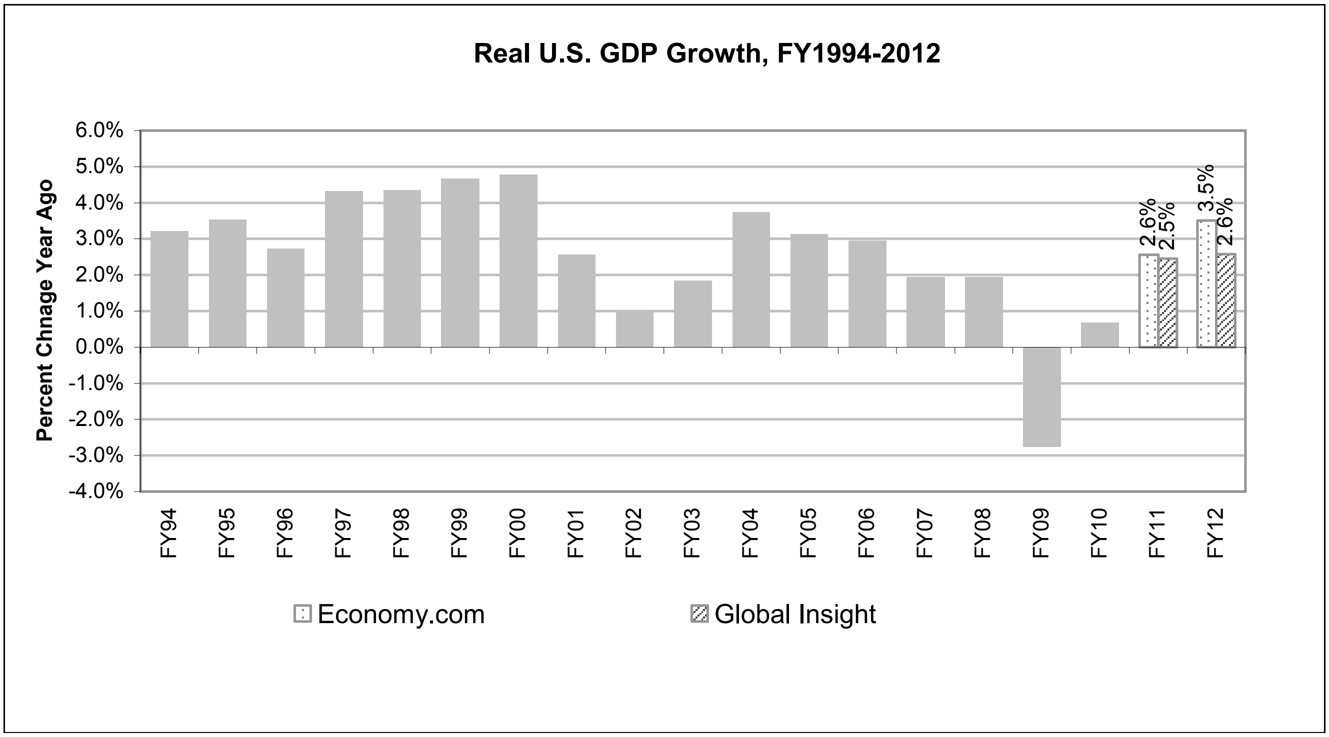
- Corporate profits at the national level are expected to increase by 4.9% to 5.8% over the remainder of fiscal year 2011, and by 10.4% to 12.4% for the fiscal year as whole (there are no forecasts for state corporate profits). For fiscal year 2012, growth in corporate profits is projected to range from 1.1% to 5.8%;

In addition to the economic forecasts described above, the consensus revenue estimate takes into account forecasts for capital gains realizations and taxes. The consensus agreement capital gains forecast is based on the following considerations:

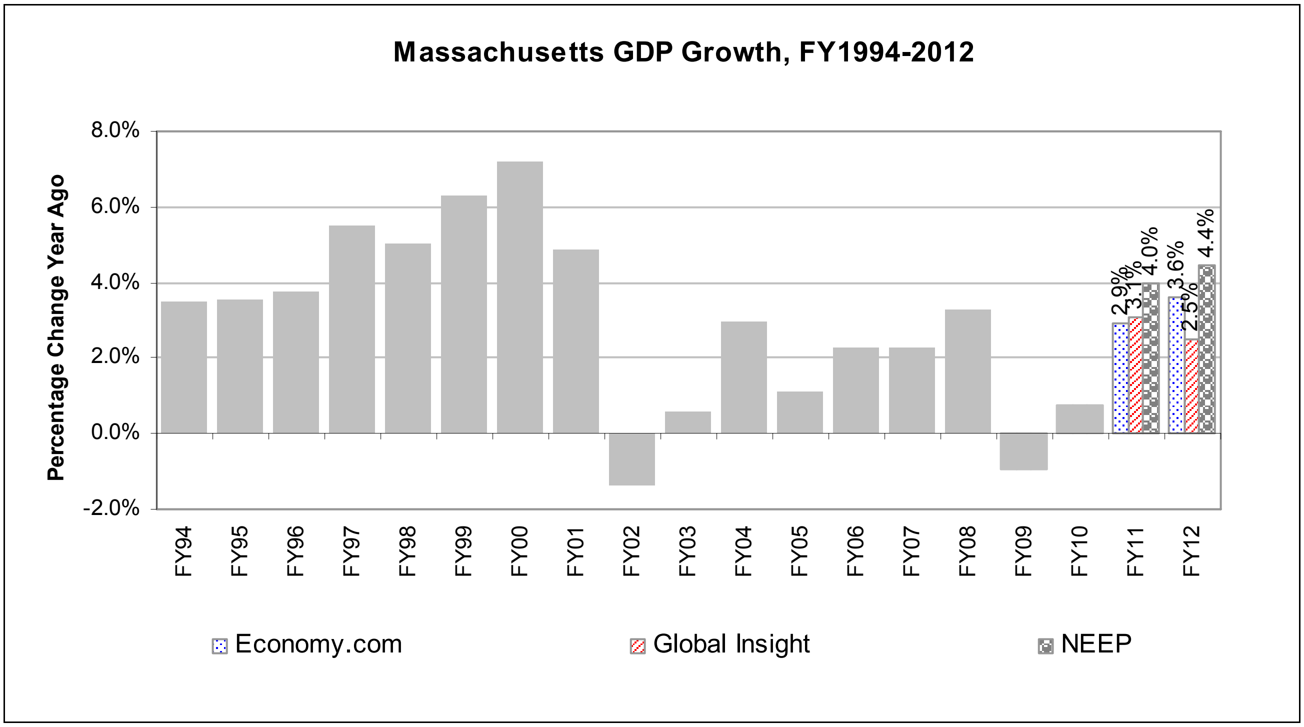
- Preliminary tax year 2009 data indicates that Massachusetts capital gains realizations decreased by approximately 43.3% in tax year 2009, to $8.4 billion. Fiscal year 2010 taxes on those capital gains realizations totaled approximately $497 million, a decrease of approximately $27 million, or 5.1%, from fiscal year 2009 (taxes on tax year 2009 capital gains realizations were paid mostly in fiscal year 2010).

- The stock market, as measured by the average of the S&P 500 over the entire year, rose by 20.5% in calendar year 2010 (which largely determines fiscal year 2011 capital gains taxes), and is expected to increase by 5.2%-9.7% in calendar year 2011 (which largely determines fiscal year 2012 capital gains taxes). Massachusetts capital gains realizations are projected to increase by 17.4% in calendar year 2010 and increase by 16.4% in calendar year 2011.

The charts below show the national and state economic forecasts presented at the December 14, 2010 consensus revenue hearing as well as the consensus estimate assumption for capital gains realizations and taxes, all of which were taken into consideration in developing the fiscal year 2012 consensus revenue estimate.


Real U.S. GDP Growth, FY1994-2012
Percent Chnage Year Ago
6.0%
5.0%
4.0%
3.0%
2.0%
1.0%
0.0%
-1.0%
-2.0%
-3.0%
-4.0%
2.6%
2.5%
3.5%
2.6%
FY94
FY95
FY96
FY97
FY98
FY99
FY00
FY01
FY02
FY03
FY04
FY05
FY06
FY07
FY08
FY09
FY10
FY11
FY12
Economy.com
Global Insight


U.S. Corporate Profits Growth, FY1994-2012
Percent Change Year Ago
50.0%
40.0%
30.0%
20.0%
10.0%
0.0%
-10.0%
-20.0%
-30.0%
-40.0%
10.4%
12.4%
5.8%
1.1%
FY94
FY95
FY96
FY97
FY98
FY99
FY00
FY01
FY02
FY03
FY04
FY05
FY06
FY07
FY08
FY09
FY10
FY11
FY12
Economy.com
Global Insight


Massachusetts GDP Growth, FY1994-2012
Percentage Change Year Ago
8.0%
6.0%
4.0%
2.0%
0.0%
-2.0%
2.9%
3.1%
4.0%
3.6%
2.5%
4.4%
FY94
FY95
FY96
FY97
FY98
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FY00
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FY07
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FY09
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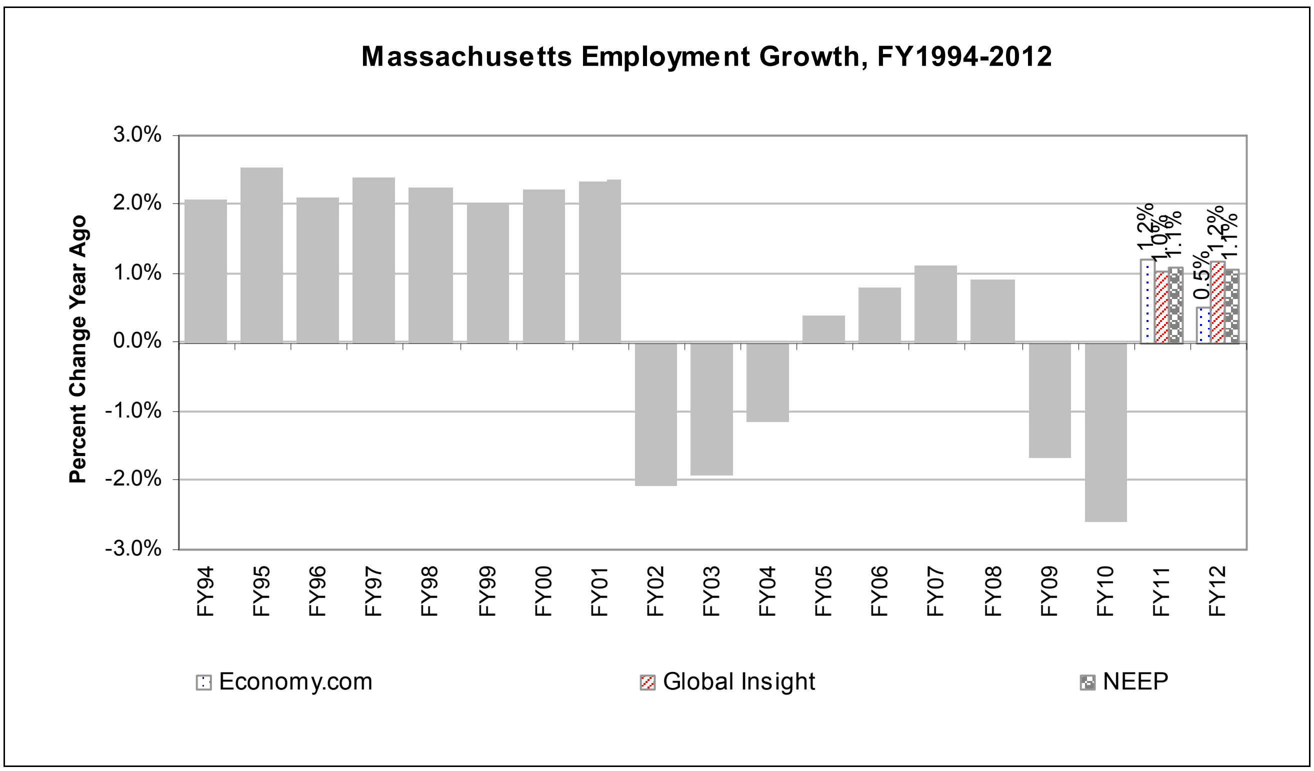
NEEP


Massachusetts Employment Growth, FY1994-2012
Percent Change Year Ago
3.0%
2.0%
1.0%
0.0%
-1.0%
-2.0%
-3.0%
1.2%
1.0%
1.1%
0.5%
1.2%
1.1%
FY94
FY95
FY96
FY97
FY98
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FY01
FY02
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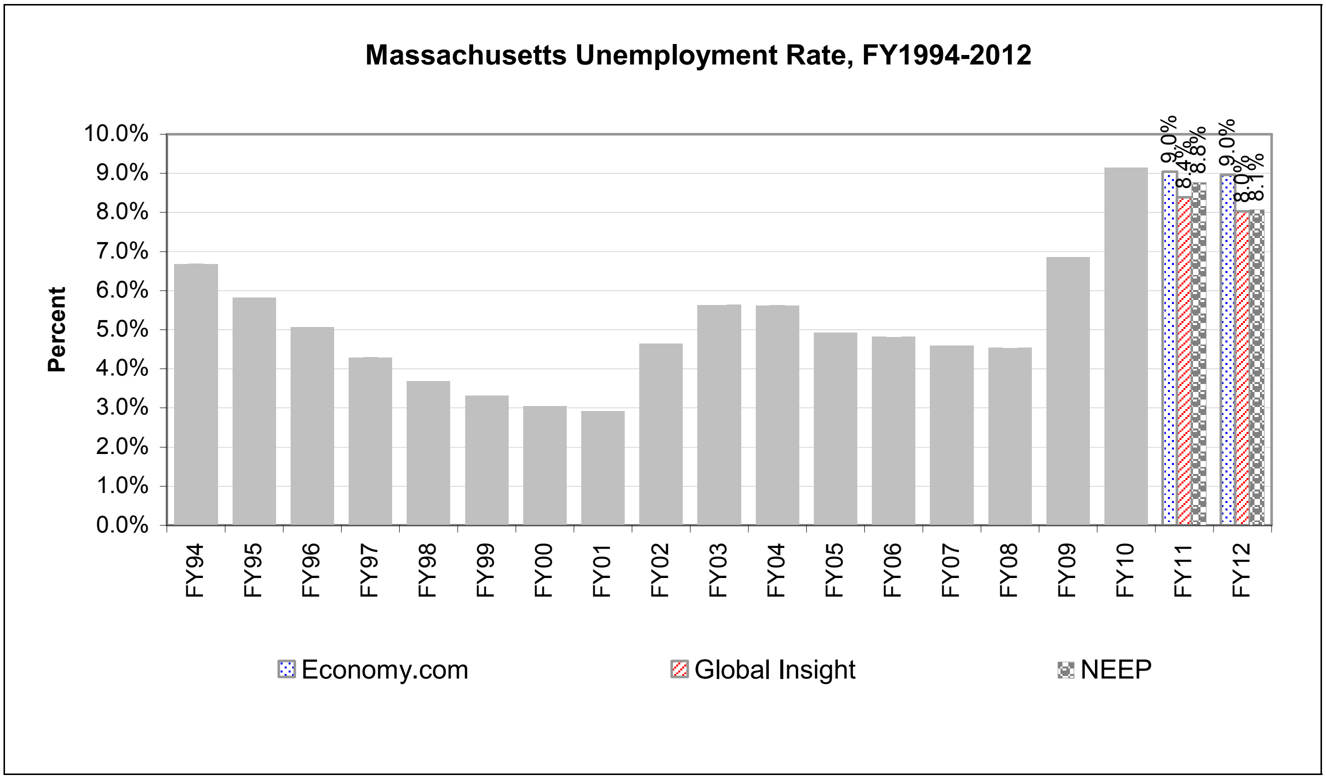
FY11
FY12
Economy.com
Global Insight
NEEP


Massachusetts Unemployment Rate, FY1994-2012
Percent
10.0%
9.0%
8.0%
7.0%
6.0%
5.0%
4.0%
3.0%
2.0%
1.0%
0.0%
FY94
FY95
FY96
FY97
FY98
FY99
FY00
FY01
FY02
FY03
FY04
FY05
FY06
FY07
FY08
FY09
FY10
FY11
FY12
9.0%
8.4%
8.8%
9.0%
8.0%
8.1%
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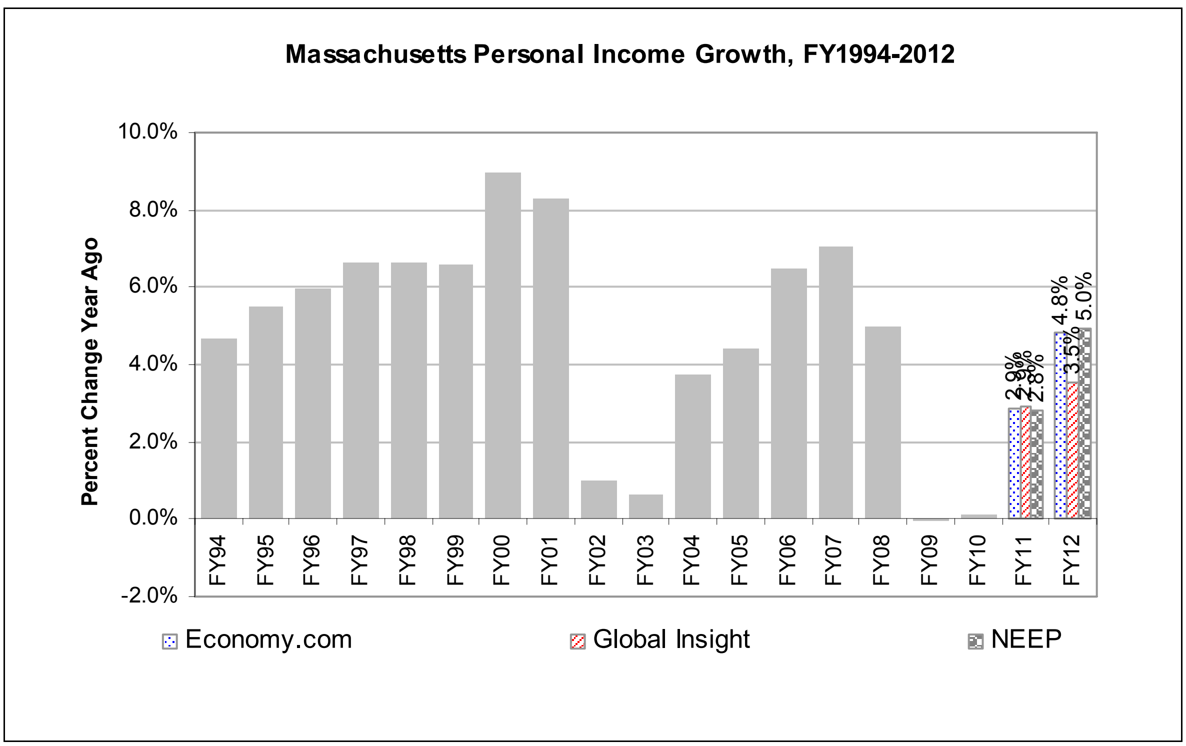
Massachusetts Personal Income Growth, FY1994-2012
Percent Change Year Ago
10.0%
8.0%
6.0%
4.0%
2.0%
0.0%
-2.0%
FY94
FY95
FY96
FY97
FY98
FY99
FY00
FY01
FY02
FY03
FY04
FY05
FY06
FY07
FY08
FY09
FY10
FY11
FY12
2.9%
2.9%
2.8%
4.8%
3.5%
5.0%
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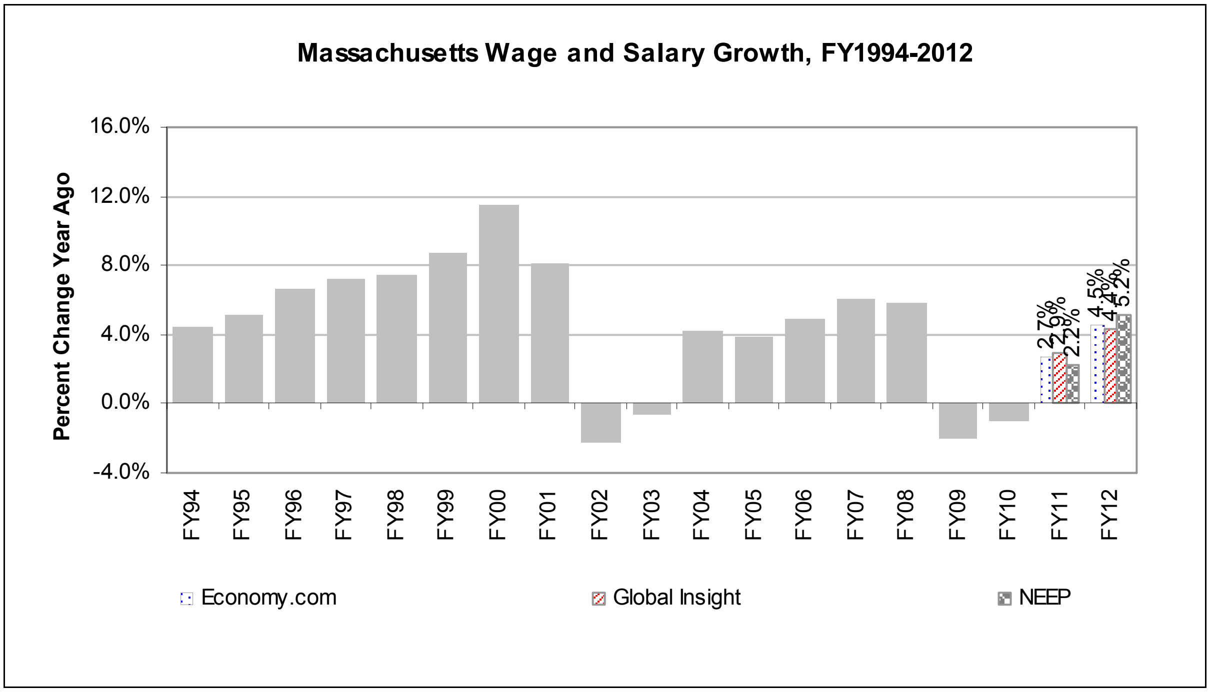
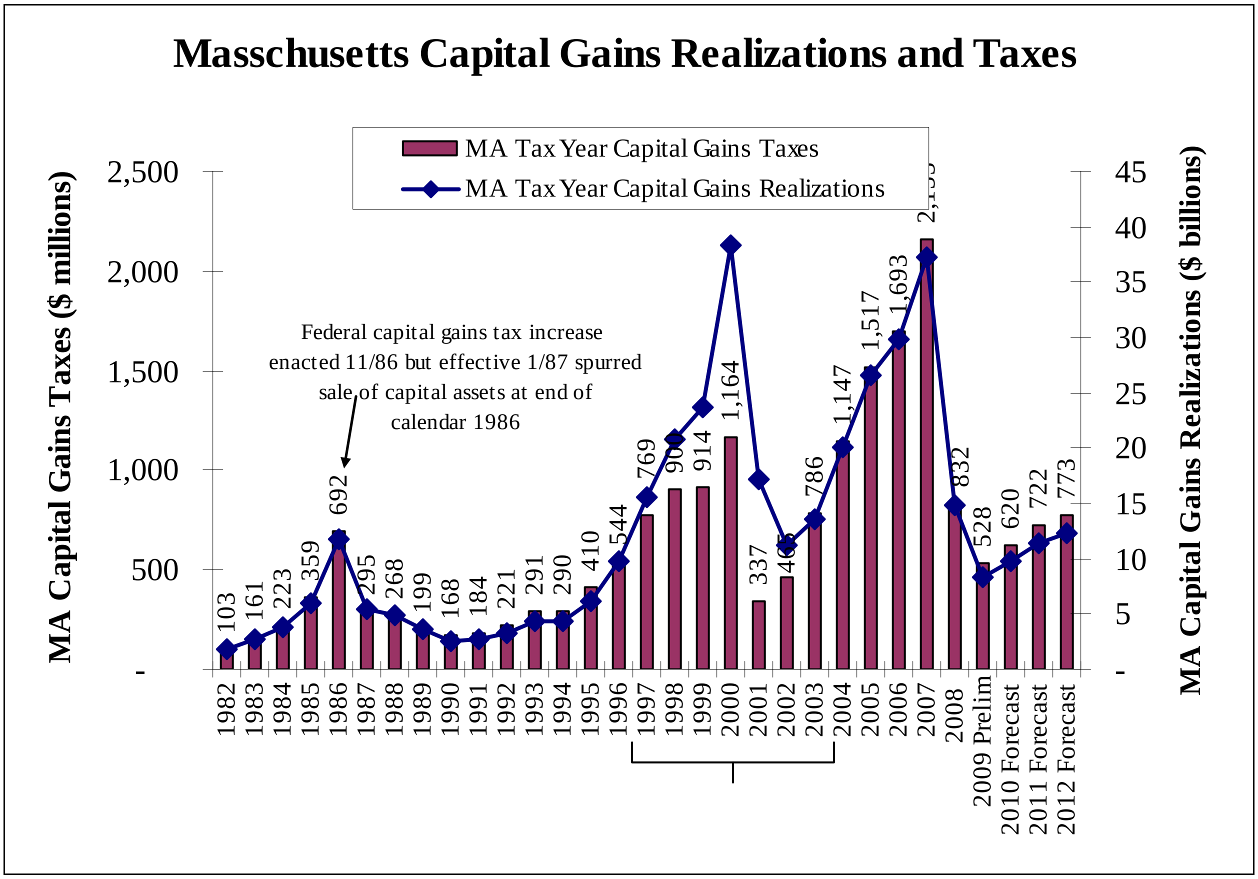

Massachusetts Wage and Salary Growth, FY1994-2012
Percent Change Year Ago
16.0%
12.0%
8.0%
4.0%
0.0%
-4.0%
FY94
FY95
FY96
FY97
FY98
FY99
FY00
FY01
FY02
FY03
FY04
FY05
FY06
FY07
FY08
FY09
FY10
FY11
FY12
2.7%
2.9%
2.2%
4.5%
5.2%
Economy.com
Global Insight
NEEP


Massachusetts Retail Sales Growth, FY1994-2012
Percent Change Year Ago
12.0%
8.0%
4.0%
0.0%
-4.0%
-8.0%
FY94
FY95
FY96
FY97
FY98
FY99
FY00
FY01
FY02
FY03
FY04
FY05
FY06
FY07
FY08
FY09
FY10
FY11
FY12
Economy.com
Global Insight

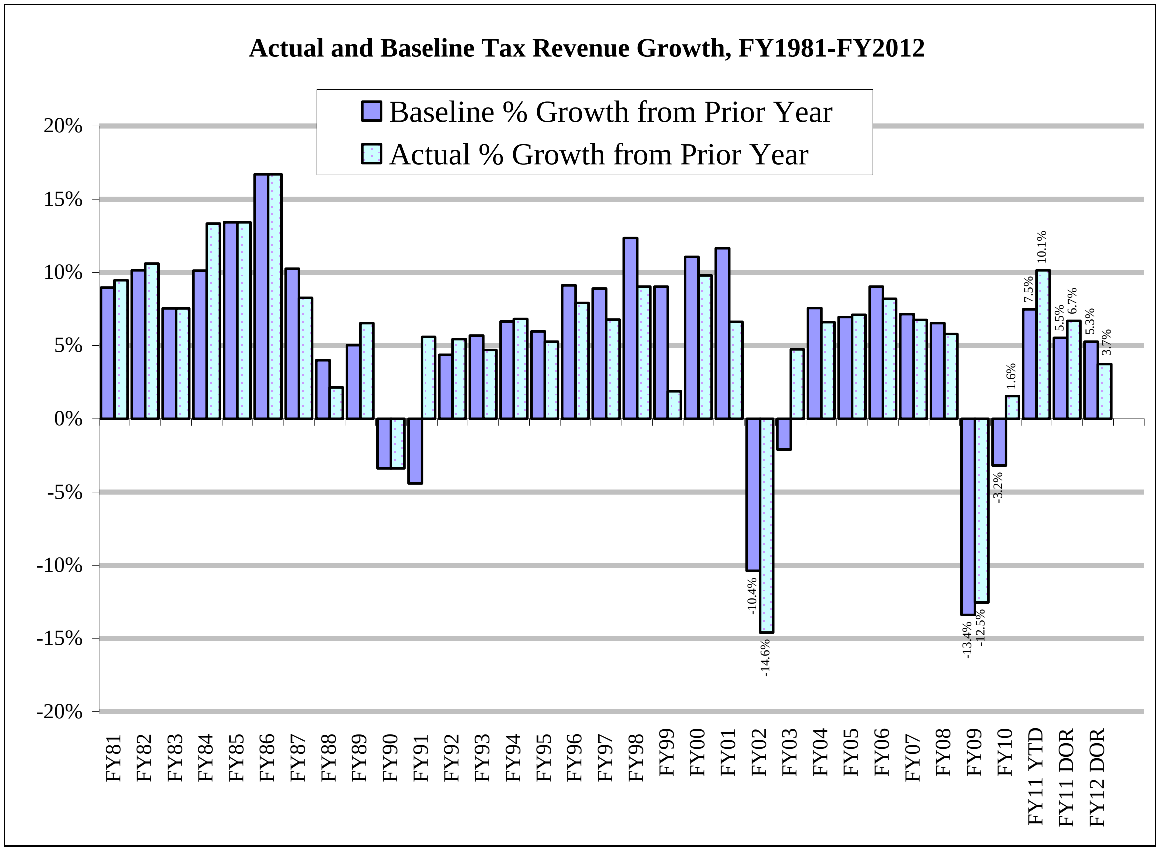


Based on these economic projections and actual tax collections through December 2010, fiscal year 2012 tax collections are projected to grow by $741 million, or 3.7% actual and 5.3% baseline from fiscal year 2011 tax collections, with income tax collections growing by 6.0% actual and baseline, sales tax growing by 3.7% actual and 4.6% baseline, and corporate/business taxes declining by 4.7% actual and increasing by 5.9% baseline, as shown in the chart below.

FY12 Consensus Tax Revenue Forecast

Tax Type	% Actual Revenue Growth from FY11	% Baseline Revenue Growth from FY11	FY12 Revenue Estimate ($ Millions)	FY12 Growth from FY11 ($ Millions)
Total Income	6.0%	6.0%	11,578	651
Withholding	5.0%	5.0%	9,842	468
Sales	3.7%	4.6%	5,087	181
Corporate/Business	-4.7%	5.9%	2,125	-106
Other	0.8%	1.9%	1,736	14
Total	3.7%	5.3%	20,525	741
Memo: Capital Gains Taxes	15.5%	15.5%	744	100

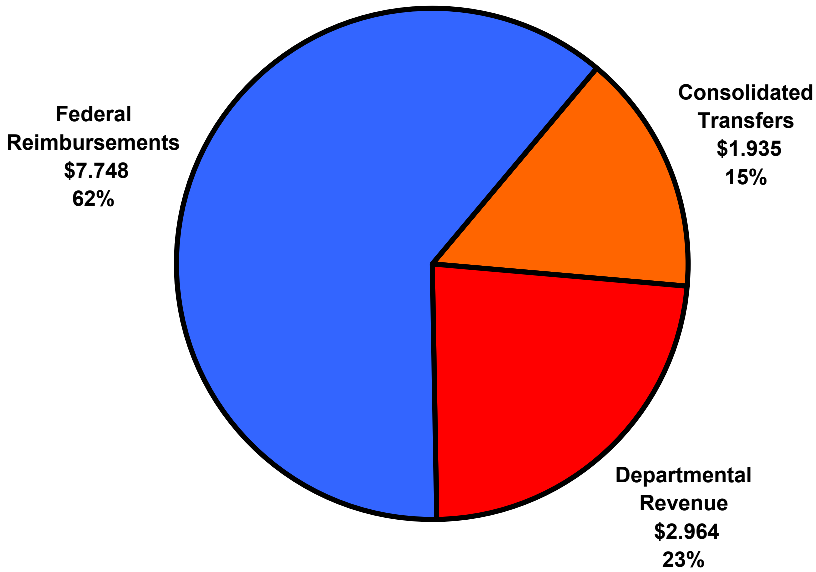
The chart below shows historical trends in actual and baseline tax revenue growth.



Fiscal Year 2012 Non-Tax Revenue Assumptions

The Commonwealth collects and receives revenues from several non-tax sources, including the federal government, various fees, fines, court revenues, assessments, reimbursements, interest earnings and transfers from non-budgeted funds. These revenues are deposited in the General Fund, the Commonwealth Transportation Fund and other operating budgeted funds. The Governor's fiscal year 2012 budget recommendation assumes approximately $12.65 billion in non-tax revenues. Reimbursements from the federal government make up 62% of the Commonwealth's non-tax revenue. The remaining non-tax revenues come from departmental revenues (23%) and operating transfers to fund programs and services off budget (15%). Sections 1B and 1C of this document details the different types of non-tax revenues.

House 1 Total Non-Tax Revenues: $12.647 Billion (in $ Billions)



Federal Revenues
Federal revenues are collected through reimbursements for the federal share of entitlement programs such as Medicaid and through block grants for programs such as Temporary Assistance for Needy Families (TANF) and Child Support Enforcement. The amount of federal reimbursements to be received is determined by state expenditures and federal regulations that govern federal programs. Staff from the Executive Office for Administration and Finance work with agencies to project budget year spending levels for these federally supported programs.

Departmental Revenues
Departmental revenues are derived from licenses, tuition, fees for programs and services, reimbursements and assessments for services including, but not limited to, revenues from the Registry of Motor Vehicles, reimbursement of healthcare costs from municipalities participating in the state's Group Insurance Commission (GIC) health care programs, drug rebate money received by the Executive Office of Health and Human Services, interest earnings received on the state's budgeted fund balances and fees collected by the Secretary of State's Office. To the extent possible, the Administration has minimized fee increases. However, MGL Chapter 7:3B provides for an annual review of fees to confirm that they are sufficient to defray the cost of providing the service. As part of this exercise, the Executive Office for Administration and Finance analyzes historical non-tax revenue receipts and works with agencies to develop budget-year projections for these revenues. During the budget process, agencies are asked to review the fees to ensure they are current and reflect the actual cost of doing business.

As mentioned above, H.1 includes two sections that give a detailed overview of projected non-tax revenue for fiscal year 2012. Section 1B details projected fiscal year 2012 non-tax revenue receipts by the department, board, commission or institution that administers and collects the respective revenue source. The online version of H.1 allows the user to further examine each governmental area and view a title and description of each revenue source contributing to that area's total non-tax revenue. Additionally, the fund statements which are included in the "Financial Statements" section of the budget document offer another view of departmental revenues by operating fund.

Consolidated Transfers

Consolidated transfers reflect inflows to the General Fund from non-budgeted funds which include annual tobacco settlement proceeds received as part of the Master Settlement Agreement with tobacco companies, net revenues from the State Lottery Fund, fringe revenue to recoup the cost of various statewide benefits assessed on non-budgeted funds and revenues from the Commonwealth's Abandoned Property Division. The Executive Office for Administration and Finance solicits agency feedback and uses historical data to project transfers to and from the budgeted funds for the proposed budget year. Section 1C of this document provides further detail behind this revenue type.

Fiscal Year 2012 Budget Challenges

On July 1, 2011 states across the country will be entering their fourth consecutive year of a difficult fiscal environment. For most states, however, the challenges presented by fiscal year 2012 will be different in several ways than the years that have preceded it. Beginning in fiscal year 2009 and continuing through fiscal year 2010, most states experienced a steep decline in state tax collections as economic activity declined under the weight of the global economic crisis. Most states were forced to take a number of measures to address the declining revenues and the simultaneous jump in demand for safety net services, including: implementing dramatic spending reductions through cuts to programs and layoffs of employees; increasing taxes and other non-tax revenues; utilizing state reserves; and relying on temporary federal stimulus revenue.

Fiscal year 2011 is the first time in 3 years states are beginning to see general tax collections recover, although most, including Massachusetts, have not seen them recover to levels comparable to those prior to the beginning of the recession. With the combination of recovering tax revenue and the use of federal stimulus dollars authorized through the remainder of the fiscal year, states have been able to reach fiscal stability this year. The Commonwealth's fiscal year 2011 budget relies on a combination of $1.9 billion in one-time measures, $1.5 billion of which relates directly to federal stimulus and assumes growth of tax revenues from fiscal year 2010 of $1.24 billion. <u>It is important to understand that federal stimulus funds must be used to support the programs and services they were intended for and cannot contribute to the states reserves in any way – they must be spent or the state risks losing access to them.</u>

As the previous sections notes, the state is no longer assuming the receipt of the $160 million in one-time federal Medicaid revenues related to the Special Disabilities Workload (SDW) populations. This lowers the total amount of one-time resources used in fiscal year 2011 that must be accounted for in the development of the fiscal year 2012 budget.

Revised FY2011 One-Timers ($s in millions)	
Total One-Timers:	**1,856.9**
Federal Stimulus (ARRA):	1,552.1
State Fiscal Stabilization Fund	*96.0*
Enhanced FMAP Revenue	*1,244.4*
Other ARRA	*11.7*
EduJobs Funding	*200.0*
Other One-Time Sources:	304.8
Special Disabilities Workload	*-*
Special Education (IDEA)	*101.3*
Debt Service Restructuring	*100.0*
Quasi Public Contributions	*25.0*
Trust Sweeps (incl. Springfield)	*58.5*
Other One-Time Solutions	*20.0*

Beginning in fiscal year 2012 states will need to account for the loss of resources made available on a one-time basis. Even with strong revenue growth in fiscal year 2012, the state can only expect to offset a portion of the impact of the loss of one-time resources.

Bottom-Line Spending Growth
The Governor's fiscal year 2012 budget is balanced and fiscally responsible, reflecting the fact that state spending must align with the resources available to the state. Total state fiscal year 2012 spending is projected to total $30.549 billion. When accounting for the $397 million in off-budget fiscal year 2011 spending that would typically be funded from the state budget, total fiscal year 2012 spending is a 1.8 percent reduction from fiscal year 2011 estimated spending. Since fiscal year 2009, total state spending has only grown by $1.129 billion, an average of 1.0 percent over the four fiscal years.

FY 2012 Spending Growth from FY2011 ($s in millions)

	Estimated FY2011 Spending	H.1 FY2012 Spending	Annual Change	% Change
Projected Spending*	30,720	30,549	(173)	-0.6%
FY2011 Adjustments	397	-		
Adjusted Spending	31,117	30,549	(570)	-1.8%
**excludes annual state contribution for employees' pensions.*				

Changes to State Revenue
For fiscal year 2012 the consensus tax revenue estimate assumes tax collections of $20.525 billion, or $741 M above the revised fiscal year 2011 estimate. When compared to the revised fiscal year 2011 estimate, projected FY 2012 tax growth totals 3.5 percent.

FY11 and FY12 Tax Consensus Figures ($s in millions)	
Original FY11 Tax Consensus Figure:	19,078
Revised FY11 Tax Projection:	19,784
FY11 Revised vs. Original:	706
FY12 Tax Consensus Figure:	20,525
FY12 Consensus vs. FY11 Revised Estimate	**741**

Based on the updated estimates, the resources available as a starting point for building our fiscal year 2012 budget compared to fiscal year 2011 assume the loss of $1.857 billion of one-time resources, primarily from the expiration of $1.55 billion in federal stimulus funds. As noted earlier, the state's tax collections are projected to grow by $741 million next year, a small portion of which will be offset by increased transfers of sales tax revenues to the Massachusetts Bay Transportation Authority (MBTA) and the School Building Authority (SBA). Under state law both the MBTA and SBA receive 16 percent of the total annual sales tax collected by the Commonwealth. Finally, after accounting for the loss of federal stimulus "enhanced" Medicaid revenues and other smaller one-time sources, total non-tax revenues are projected to decrease by $45 million in fiscal year 2012.

Change in Available Resources, FY 2012 vs FY 2011 ($s in millions)	
Loss of One-Time Resources:	(1,857)
Growth in Tax Collections from FY11:	741
Increase Transfer of Tax Revenues for Off-Budget Purposes:	(36)
Growth in Non-Tax Revenues:	(45)
Change in Available Resources for FY12:	(1,197)

Additional Revenues

With available resources being $1.197 billion less than fiscal year 2011 as a starting point, the following measures are proposed to support the fiscal year 2012 budget. The measures (identified in the table below) serve to generate in total, $627.3 million in additional resources in fiscal year 2012 to support state spending. The Governor's budget does not rely on broad-based tax increases nor does it increase available fiscal year 2012 revenues by raising the user fees that state's residents pay for specific government services (such as licenses or permits). Where additional revenue solutions are proposed for fiscal year 2012 they are advanced as limited, responsible and fair measures to support state government services while still mindful that the economic conditions remain challenging for businesses and households.

FY2012 Additional Revenues ($s in millions)	
TOTAL	627.3
Use of Stabilization Fund reserves (one-time):	200.0
Enhanced DOR Tax Enforcement:	61.5
New Revenue Initiatives:	88.8
Expanded Bottle Bill:	20.0
Revenue Maximization:	40.0
Sale of Assets:	15.0
Quasi-Public Contributions:	25.3
Abandoned Property (one-time):	99.0
Expanded Federal Revenue through Medicaid Waiver:	78.0

Spending Growth:
Year-on-year spending growth was provided for a limited number of programs in the state budget, particularly for those items that reflect long-term state liabilities (such as debt service, retiree health costs and pension contributions). The items total approximately $632.1 million in increased spending above fiscal year 2011 spending.

FY 2012 Spending Growth ($s in millions)	
Debt Service	255.7
State Aid for Public Education	139.8
Retirees Health Care	17.3
State Pensions Contribution	37.0
Aid for Special Education Costs	80.0
Annualized MassHealth Spending	100.0
total	629.7

Given that available resources in fiscal year 2012 are projected to be $1.197 billion less as a starting point for comparison to fiscal year 2011 in developing the fiscal year 2012 budget, state spending will need to be reduced below fiscal year 2011 levels. With the additional resource being proposed by the Governor noted above, total state budget resources will be $30.549 billion, or $570 million less than fiscal year 2011. This is further compounded by the state's need to fund increased spending of $629.7 million for the limited number of items in the budget noted above, requiring that other areas in the budget face further reductions totaling $1.2 billion to live within the lower level of resources and to offset these increases in spending.

Furthermore, state agencies will need to implement additional cost controlling measures in order to avoid or mitigate increased cost pressure each may face in their specific programs. This is particularly true for the state's subsidized health care programs for low-income families, the uninsured and state employees (current and retired). The state will implement aggressive cost-controlling measures in order to keep total fiscal year 2012 spending in line with available resources.

Fiscal Year 2012 Budget Solutions

The Governor's budget and language filed concurrently with the H.1 recommendation call for a number of reforms across state government. While the budget preserves many services and programs for the state's most vulnerable populations, it recognizes that the state must fundamentally change the nature by which it operates in order to live with a changing fiscal reality.

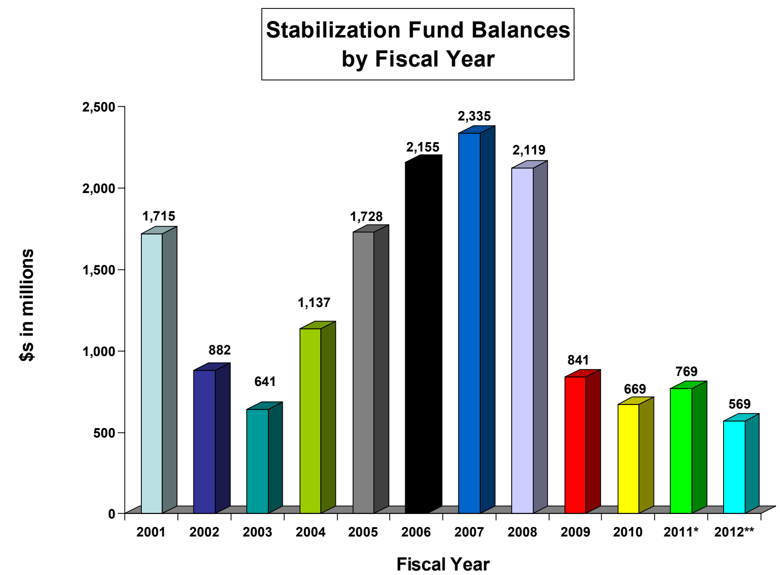
Outlined in the discussion below are the measures taken proposed by the Governor to implement a balanced fiscal year 2012 financial plan. Furthermore, major areas of reform and efficiencies are listed, with an emphasis on what programs and services have been preserved next fiscal year.

FY2012 Additional Revenues ($s in millions)	
TOTAL	627.3
Use of Stabilization Fund reserves (one-time):	200.0
Enhanced DOR Tax Enforcement:	61.5
New Revenue Initiatives:	88.8
Expanded Bottle Bill:	20.0
Revenue Maximization:	40.0
Sale of Assets:	15.0
Quasi-Public Contributions:	25.0
Abandoned Property (one-time):	99.0
Expanded Federal Revenue through Medicaid Waiver:	78.0

The table directly above identifies the additional revenue solutions proposed for fiscal year 2012. Further description of each is provided below.

Use of Stabilization Fund Reserves

The projected fiscal year 11 year-end balance of the Stabilization Fund is projected to total $769 million, assuming that nearly $100 million will be deposited into the Fund this year. The Governor's fiscal year 2012 budget recommendations propose to utilize $200 million in resources from the state's reserves to help to avoid further reductions to state programs beyond those that have already been required. With the $200 million transfers, the total fiscal year 2012 year-end balance will be $569 million (see chart below).



**Reflects FY11 supplemental legislation (Chp. 359 of 2010) that canceled the $100 million draw from the Stabilization Fund adopted in the GAA and deposit of $100 million into the Stabilization Fund.*
***Projected Fund balance after $200 million transfer.*

The Stabilization Fund reserves, when used to support ongoing state spending, must be considered as one-time resources; meaning that this revenue source will not be available for future use and the state will need to offset this loss with comparable new revenues or reductions in spending.

Enhance Tax Enforcement Initiatives

Over the course of the last several fiscal years, the Department of Revenue, like many other state agencies has sought creative solutions to generate additional revenue for the Commonwealth to sustain programs and services through increased enforcements of existing laws already on the books. In fiscal year 2011 the agency is generating an additional $24 million in tax revenues from targeted investments in its tax compliance activities. In fiscal year 2012 the agency proposes to build off that success through a modest investment of $1.2 million, allowing it to expand the number of employees directly performing tax examination, audit and appeals functions. This investment is projected to result in additional tax revenues to the Commonwealth of $61.5 million, primarily through increased assessments and settlements with taxpayers.

New Revenue Initiatives

The table identifies new revenue initiatives that are proposed for the fiscal year 2012 budget. In total these initiatives will generate an estimated $89 million in additional resources for the Commonwealth next year. All but one of the proposals will require legislative changes to the state's existing tax laws to implement them. This language is provided in outside sections of the fiscal year 2012 House 1 recommendation or in legislation the Governor is filing concurrent with the budget.

Fiscal Year 2012 H.1 Revenue Initiatives, by title and amount ($s)		
1	Enforcement of Room Occupancy Tax on Hotel Room Resellers	8,000,000
2	Enhanced Medical Support Compliance for Child Support Cases	9,900,000
3	Manage Life Sciences Tax Credit (administratively)	5,000,000
4	Delay FAS 109 Deductions	45,860,105
5	Fix Corporate Excise Sale Factor	20,000,000
	Total	**88,760,105**

1. Enforcement of Room Occupancy Tax on Hotel Room Resellers

The proposed change would require an Internet room reseller to register with DOR and collect and remit the existing state and local room occupancy excise on the reseller's mark-up. The hotels and motels in Massachusetts would continue to collect and remit tax on amounts they are actually paid, as is the current practice. The revenue impact from this proposal in fiscal year 2012 is $8 million with an August 1st effective date and $8.7 million for the state when fully annualized. This change is primarily technical, serving to clarify present law for collecting an existing tax from resellers as well as hotels.

2. Enhanced Medical Support Compliance for Child Support Cases

State law requires use of a federally mandated National Medical Support Notice. This notice instructs employers and health insurers to provide coverage for children and families pursuant to court orders. While many employers comply with the terms of the National Medical Support Notice, many do not, including failures to send health insurance cards to the custodial parent. This proposal amends the statute to make the penalties for failure to comply with an order for health care coverage consistent with the penalties for failure to withhold or remit child support payments. DOR estimates that increased employer compliance pursuant to this provision will enroll over 1,500 more children in private health care coverage, resulting in approximately $1.9 million in annual cost savings to the Commonwealth.

3. Management of Life Science Tax Credits

Without reducing statutory authorizations, the state would reduce fiscal year 2012 tax expenditures by limiting the actual tax credits that would be refunded or used by the Life Sciences Center in fiscal year 2012 to lower estimated tax payments by eligible corporations. This would generate $5 million in additional fiscal year 2012 revenues next year for the Commonwealth. Implementing these reductions demonstrates a continued effort to share sacrifice among all major priorities and initiatives including the efforts to continue to expand the life sciences sector in Massachusetts.

4. Delay the "FAS 109" Tax Reporting Deduction

The FAS 109 deduction allows publicly traded corporations subject to combined reporting under the 2008 corporate tax reform law to take a deduction of all or some of an amount that will offset the increase in the combined group's net deferred tax liability that would otherwise be shown on its book financial statements as a result of the move to combined reporting. "FAS 109" refers to the financial accounting standards bulletin that requires such corporations to report their deferred tax liabilities (or expected benefits, like credits) to shareholders.

The deduction is spread over seven years commencing in the corporation's taxable year beginning in 2012. The FAS 109 law required corporations that were eligible for the deduction to file a statement with DOR stating the amount of the expected FAS 109 deduction that will be claimed. The responses indicated that total deductions would exceed $178 billion, and the total corporate excise revenue decrease to the Commonwealth that would result from corporations taking those deductions would exceed $535 million over a 7 year period 2012 – 2018 ($76 – 79 million per year).

The Governor's House 1 recommendation delays the implementation of FAS 109 until fiscal year 2013, rather than allowing it to begin in fiscal year 2012. This will increase the amount of taxes collected by the state next year by nearly $46 million. Savings generated from the delay in the implementation of the FAS 109 deduction would be one-time in nature, since they are only proposed to be delayed until fiscal year 2013.

5. Amend Corporate Excise Factoring

This proposal will modernize the sales factor (one of 3 factors by which the MA corporate excise is apportioned among states) by sourcing it based on where services are delivered, rather than where they originate. This will mostly affect large, non-MA companies, e.g. telecom providers. The proposal will help some MA companies hurt by the present sourcing rule. Eleven states, including California, Georgia, Maryland, Maine and Wisconsin, have adopted sourcing generally consistent with the model that DOR is proposing -- i.e. generally sourcing to where services (or the benefit of services) are received.

While these proposals are advanced to increase revenue for the Commonwealth in fiscal year 2012 there are many other tax or related changes that were maintained or preserved next that will help thousands of businesses and families as the state's economy continues to recover.

State Corporate Excise Rate

The fiscal year 2012 budget assumes that there will be no changes to the phase down of the corporate tax rate, scheduled in law to decline from 8.75 percent in tax year 2010 to 8.25 percent in 2011. Next fiscal year, the Department of Revenue estimates this will save 35,000 businesses statewide roughly $185.1 million from this change. In the midst of unprecedented fiscal challenges, it is important to continue to follow through with corporate tax reform and reducing costs for businesses. These changes will help to ensure that the state's small businesses especially are well positioned to continue their economic recovery.

Tax Expenditures

The state provides a number of deductions to taxpayers, whether individuals, families or corporations, totaling over $20 billion in fiscal year 2011 alone. These "expenditures" represent tax revenue the state would otherwise collect but has foregone by providing exemptions, deductions on taxes owed, or credits against annual taxes, for a variety of areas, including charitable deductions, the purchase of most food items, the interest paid on student loans, or the purchase of equipment for the use of high-tech research and development. Given the difficult fiscal challenges the state continues to face next year, the Secretary of Administration and Finance and the Department of Revenue evaluated whether any further changes could be considered for the state's tax expenditures. At this time, these tax expenditures are preserved. Further information on each such tax expenditure is provided in a later section.

Revenue Maximization

Leading up to the development of the fiscal year 2012 budget, the Executive Office of Administration procured a wide-ranging analysis of the current revenue-generating activities by a variety of state agencies, particularly around program integrity and federal revenue claiming. This effort has provide over 100 potential opportunities for the state to pursue to help generate additional federal revenue for the Commonwealth, or to reduce the state's costs in administering a number of programs or benefits provided to residents. The fiscal year 2012 House 1 recommendation would generate $40 million in additional fiscal year 2012 revenues from these initiatives. The Governor's budget would fund a $1 million appropriation to allow for necessary investments to fund revenue enhancement contracts that were not based on contingency-based fee proposals.

Sale of Assets

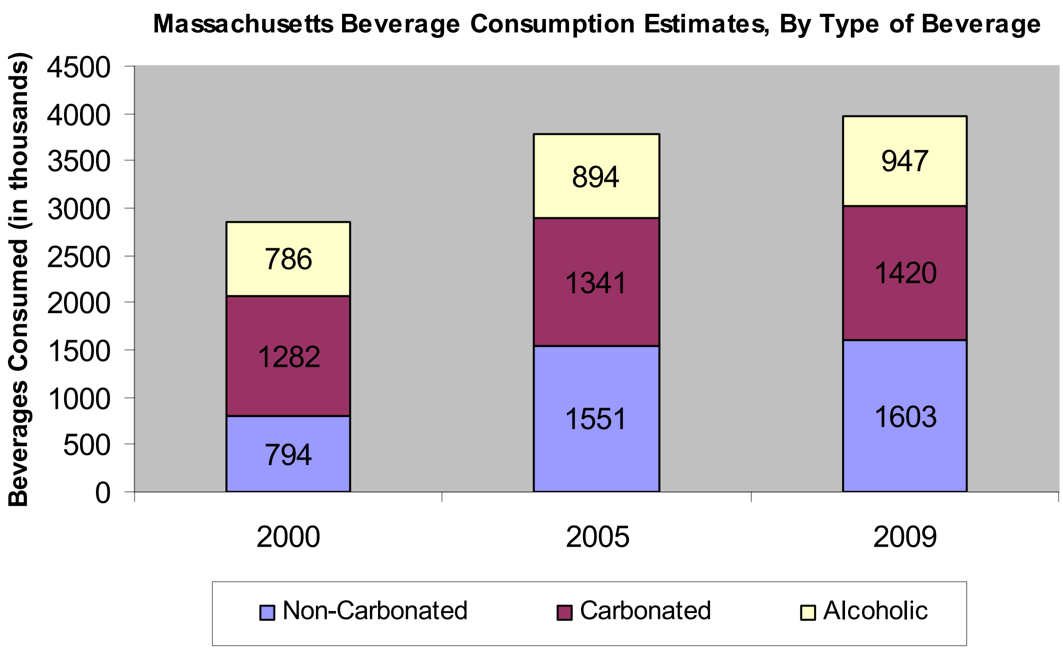
The House 1 proposal assumes the state can generate at least $15 million in additional revenue for the Commonwealth in fiscal year 2012 from the sale of state properties that have been identified by state agencies as underutilized. Additional legislation will be filed by the Governor in January 2011 to allow the state to expedite this process and ensure that it can achieve the assumed savings for next year.

Expand Bottle Deposit

The Massachusetts Bottle Bill, enacted in 1982, is designed to encourage consumers to return their empty soda and beer containers by means of a redeemable $0.05 deposit. The $0.05 refundable deposit is placed on all carbonated sodas, beer and malt beverages. Most bottle deposits are redeemed through two types of sites, redemption centers and large retail stores. Redemption centers are specialized small businesses that provide refunds for empty beverage containers before delivering them to bottlers/distributors. Large retailers often lease vending machines to manage redemptions by their customers. The leasing company delivers bottles to bottlers/distributors for payment, or may sell materials that are recyclable. Under 1989 reforms, bottlers/distributors must maintain a Deposit Transaction Fund for unclaimed deposits. These funds are transferred to the Department of Revenue each month and support government programs.

When the Bottle Bill was enacted in 1982, the beverages covered by the law were limited to carbonated soft drinks, mineral water, beer and other malt beverages. Since that time, the beverage market has changed with bottled water, fruit drinks, iced tea and sports drinks now being some of the most popular choices available. However, these non-carbonated beverages are not covered by the Bottle Bill, and often end up in landfills or along the side of the road.

By revising the definition of “beverages” in Massachusetts General Law, the Bottle Bill can be brought up to date. Consumers will be required to pay an additional $0.05 cents on water, flavored waters, iced teas, coffee based drinks and sports drinks. The Governor’s fiscal year 2012 budget assumes that by adopting these changes the state will collect at least $20 million in additional revenues next year, allowing for $6.5 million in investments in state recycling coordination and redemption efforts.



Quasi-Public Agency Contributions

The fiscal year 2011 budget relies on roughly $25 million in contributions to support state programs that would otherwise need to be funded from the state’s annual operating budget or eliminated. A number of the state’s quasi-public partners have agreed to again provide a role in helping to ensure that vital economic development programs related to tourism and business development as well as cultural facilities and higher education can be sustained in these challenging times. The table below outlines the quasi-public contributions made towards the fiscal year 2012 budget.

FY2012 Quasi-Public Contributions

Program Preserved	Quasi-Public Agency	Amount
Massachusetts Rental Voucher Program	Massachusetts Housing Authority	$ 8,400,000
Small Business Development Center	Growth Capital Corporation	$ 500,000
Wellness Promotion	Commonwealth Connector Authority	$ 2,500,000
Energy and Environmental Affairs Operations	Massachusetts Clean Energy Center	$ 1,000,000
Mass Cultural Council Grants	Massachusetts Development Finance Authority	$ 3,000,000
Office of Small Business	Growth Capital Corporation	$ 700,000
State Permitting Office	Growth Capital Corporation	$ 335,000
Tourism Promotion and Marketing	Massachusetts Convention Center Authority	$ 5,000,000
No Interest Loan Program / Scholarships	Mass Education Finance Authority	$ 1,000,000
Mass Broadband Operations	Mass Tech Collaborative	$ 275,000
International Trade and Investment Promotion	Mass Tech Collaborative / Mass Port Authority	$ 600,000
Soft Seconds Loan Program	Mass Housing Partnership	$ 2,000,000
	total	**$ 25,310,000**

Abandoned Property

Treasurer-elect Steven Grossman has identified additional abandoned properties held currently by the Commonwealth that can be liquidated in the amount of $99 million in fiscal year 2012, above the ongoing annual state revenues estimated to total $89 million next year. These proceeds will be generated from the sale of mutual funds and other securities. The revenue provided from these sales is one-time solution that will not necessarily be available in future years. A further discussion of the state's reliance on one-time resources is included later in this section.

Federal Waiver Reimbursement

The fiscal year 2012 budget assumes that the state will receive an additional $72 million in federal Medicaid reimbursements under the state's waiver for the costs incurred by Designated State Health Programs at agencies such as the Department of Mental Health or the Department of Public Health. This revenue must be approved by the US Centers for Medicare and Medicaid Services (CMS), but reflects additional revenues that CMS has provided to Massachusetts in recognition of its sophisticated and wide-ranging programs that deliver health care services to patients served by a number of agencies.

One-Time Resources

With a modest use of one-time resources totaling $385 million next year, mostly stabilization funds, the fiscal year 2012 budget will have eliminated the state's continued reliance for large portions of non-recurring sources to sustain ongoing expenditures. The proposed use of Stabilization Fund reserves is responsible, leaving a health projected balance of $570 million, while building on continued efforts to take volatile revenue sources, such as taxes on capital gains and one-time settlements with taxpayers, out of the general tax revenue stream and segregate them for the purposes of replenishing the Rainy Day fund. Continued efforts to control state spending will be required in future budget years, but the fiscal year 2012 financial plan well-positions the state to eliminate its structural deficit and prepare for future challenges in the years ahead.

Fiscal Year 2012 One-Time Resources
($s in millions)

OneTime Sources:	**385**
Stabilization Fund Reserves	*200*
Delay FAS 109 Reporting	*46*
Quasi-Public Contributions	*25*
Abandoned Property Proceeds	*99*
Sale of Assets	*15*

Fiscal Year 2012 Spending Highlights from Fiscal Year 2011

As noted in the previous section, after accounting for growth in tax collections and other non-tax resources, additional revenue initiatives, and the loss of one-time sources, the state must reduce spending by roughly $570 million on a net basis. This need to reduce spending is further exacerbated by spending increases that must be funded to support cost increases that cannot be avoided, such as the state's payments to support debt service. After accounting for these increases (roughly $630 million), other state spending must be reduced by $1.2 billion across all state government.

Spending Comparison by Major Government Area, FY2012 Vs FY2011 ($s)				
Government Area Name	FY2011 Estimated Spending	H1 FY2012 Projected Spending	Variance	% Change
Judiciary	782,537,888	455,600,286	(326,937,602)	-41.8%
Independents	4,398,750,691	4,608,735,395	209,984,704	4.8%
Administration and Finance	2,856,900,429	2,586,458,005	(270,442,424)	-9.5%
Energy & Environmental Affairs	194,884,746	192,422,896	(2,461,850)	-1.3%
Health and Human Services	4,703,476,447	4,612,335,033	(91,141,414)	-1.9%
MassHealth	10,240,029,259	10,340,029,259	100,000,000	1.0%
Transportation	370,126,756	363,233,728	(6,893,028)	-1.9%
Housing & Economic Development	371,483,102	348,789,556	(22,693,546)	-6.1%
Labor & Workforce Development	73,778,467	35,446,086	(38,332,381)	-52.0%
Education	6,125,761,162	5,932,977,526	(192,783,636)	-3.1%
Public Safety	939,772,260	1,014,444,706	74,672,446	7.9%
Legislature	60,908,471	58,220,302	(2,688,169)	-4.4%
TOTAL	**31,118,409,678**	**30,548,692,778**	**(569,716,900)**	**-1.8%**

The table above shows funding changes in fiscal year 2012 in comparison to fiscal year 2011 (after adjusting for $397 million in additional non-operating spending for Education this year). The narrative provided lists the major highlights for next year. It is essential to note that almost no area of state government has been spared from reductions, from the judiciary to human services to state parks. The loss of revenue from fiscal year 2011 requires that additional spending measures be taken impacting hundreds of programs and services while requiring further reductions to the state's workforce.

Reflecting government re-organizations outlined further below, there are substantial increases in the Public Safety and Independents budgets. These increases correspond to funding shifted from the Judicial branch each respectively to reflect reforms of the state's Probation Department and the Committee on Public Counsel Services. After adjusting for these shifts and savings adopted in fiscal year 2012 for probation and indigent counsel services, the actual year on year spending changes are the following:

- Public Safety, -2.5 percent
- Judiciary, -8.5 percent
- Independents, 1.1 percent

Non-Executive Branch Agencies

Spending Comparison, Non-Executive Branch Spending, FY2012 vs. FY2011				
Secretariat Name	FY2011 Estimated Spending	FY2012 H.1 Proposed	Variance	% Change
Judiciary	782,537,888	455,600,286	(326,937,602)	-41.8%
District Attorneys	93,014,603	97,384,987	4,370,384	4.7%
Sheriffs	482,660,983	472,895,208	(9,765,775)	-2.0%
Dept. of Public Counsel Services	-	162,660,129	162,660,129	0.0%
Other Consitutionals	127,033,224	119,879,087	(7,154,137)	-5.6%
Legislature	60,908,471	58,220,302	(2,688,169)	-4.4%
Lottery	82,025,440	81,025,441	(999,999)	-1.2%
total	**1,628,180,609**	**1,447,665,440**	**(180,515,169)**	**-11.1%**

Agencies outside of the Executive branch including Constitutional Officers, the Judiciary, District Attorneys and Sheriffs, among others comprise $1.285 billion of the fiscal year 2012 budget recommendations. Some areas of note include –

- ***Judiciary*** –The Governor's House 1 recommends that the Department of Probation move from the Judiciary to the Executive Office of Public Safety and Security. The funding amount being transferred is $97.5 million, which reflects that probation responsibilities for youths will remain within the state's Trial

Court Department. Coupled with $46 million in fiscal year savings from reforms in indigent counsel services (see below), the overall budget for the Judiciary is 8.5% below the fiscal year 2011 estimated spending. Most Judicial funding was reduced by 2 percent in fiscal year 2012. But the H.1 recommendation assumes that the state will be able save roughly $14 million next year through reforms proposed by the Governor to the state's probations functions. These savings are reflected in the reduced Judicial spending amounts, increasing the percent reduction in fiscal year 12 spending.

- ***Committee for Public Counsel Services*** – House 1 proposes sweeping reforms to the manner in which the state provides constitutionally-required legal services to defendants determined to be unable to afford counsel. By shifting from the overwhelming reliance on private attorneys to a system that is fully operated under a new Department of Public Counsel Services state with staff attorneys, the Governor's budget assumes that the state can save $46 million in fiscal year 2012. The House 1 recommendation also proposes to change the governance of the agency by requiring that the chief counsel of DPCS be appointed by the Governor and eliminating the existing CPCS board.
- ***Sheriffs*** – Fiscal year 2011 reflects the first full year that all sheriffs' offices are funded as state departments through the annual operating budget. The fiscal year 2012 House 1 reduces funding for all state sheriffs by 2% below fiscal year 2011 estimated spending. It should be noted that the fiscal year 2011 spending levels reflect nearly $18 million in supplemental funding provided or proposed this fiscal year to the various state sheriffs' offices.
- ***District Attorneys*** – The funding provided for the 14 district attorneys' offices increases in fiscal year 2012 by 5 percent from fiscal year 2011 estimated spending. This increase is provided to address increase caseloads faced by each DA while supporting each DA's efforts to reduce and prevent crime. The prosecution of crime is a core state service provided by the state and it is essential to fund this adequately.
- ***Other Constitutional Officers*** – With very limited exceptions the funding for the Constitutional offices (Attorney General, Treasurer, Auditor, Secretary of State) has been reduced by 2 percent below estimated fiscal year 2011 spending levels.
- ***Lottery*** – The state's Lottery Commission oversees the state's various lottery and gaming operations. The Commission generates over $800 million in annual revenue, which supports, in part, local aid distributions to the state's cities and towns. Funding in fiscal year 2012 for Lottery operations is reduced by $1 million from fiscal year 2011 estimated spending levels.
- ***Legislature*** – The funding in fiscal year 2012 is 2 percent less than the estimated fiscal year 2011 estimated spending levels, after accounting for one-time investments in legislative redistricting needed in fiscal year 2011.

Debt Service

Spending Comparison, Debt Service, FY2012 vs. FY2011				
Secretariat Name	FY2011 Estimated Spending	FY2012 H.1 Proposed	Variance	% Change
Debt Service	2,009,959,911	2,265,680,431	255,720,520	12.7%

In order to fund the necessary improvements to the state's transportation infrastructure as well as to make investments in our higher education system, housing, high-tech industries, and other job-creating projects, the state bonds capital spending and supports this borrowing with annual debt service costs on the operating budget.

State debt service spending in fiscal year 2012 totals $2.265 billion, an increase of 12.7 percent from fiscal year 2011 levels of $2.010 billion. The fiscal year 2011 budget assumed a one-time savings in annual debt service costs of $100 million from the restructuring of certain debt service payments. After accounting for this change, total debt service spending increased by 7.3 percent in fiscal year 2012.

Executive Branch Agencies

Spending Comparison, Executive Branch, FY2012 vs. FY2011				
Executive Branch Government Area	FY2011 Estimated Spending	FY2012 H.1 Spending	Variance	% Change
Governor's Office	4,624,525	4,536,906	(87,619)	-2.0%
Administration and Finance	2,888,286,010	2,615,621,643	(272,664,367)	-9.4%
Energy and Environmental Affairs	194,884,746	192,422,896	(2,461,850)	-1.3%
Health and Human Services	4,703,476,447	4,612,335,033	(91,141,414)	-1.9%
Transportation	370,126,756	363,233,728	(6,893,028)	-1.9%
Education (excl. aid for K-12 and Higher Ed.)	1,036,799,161	1,114,272,494	77,473,333	7.5%
Housing and Economic Development	371,483,102	348,789,556	(22,693,546)	-6.1%
Labor and Workforce Development	73,778,467	35,446,086	(38,332,381)	-52.0%
Public Safety and Security	939,772,260	1,014,444,706	74,672,446	7.9%
Transfers to Health Care and Other Funds	1,770,661,187	1,574,362,762	(196,298,425)	-11.1%
total	**12,353,892,661**	**11,875,465,810**	**(478,426,851)**	**-3.9%**

Funding for Executive Branch Agencies for programs and services that fall within each of these government areas totals $11.875 billion for fiscal year 2012, which compares to $12.354 billion in FY11, a 3.9 percent reduction from fiscal year 2011 spending levels. Several factors contribute to the varying levels of increases and decreases among them:

- ***Executive Office of Education (EOE)*** – The budget recommendation for the Secretariat for Education (excluding Chapter 70 and aid to Higher Education campuses discussed below) increases by 7.4% above the fiscal year 2010 estimated spending. The fiscal year 2012 budget provides $80 million in additional funding from FY11 levels for reimbursements to cities and towns for costs in support of special education programs and services. Most other education programs were funded at the same levels provided in the fiscal year 2011 General Appropriations Act (GAA), particularly those that will support the Governor's efforts to address the achievement gap among the state's residents with respect to academic achievement and readiness for the jobs of tomorrow. A modest $3 million investment is made for the Secretary of Education to target funding to those programs and services that best position the state to leverage $250 million in federal Race to the Top education aid, provided over a four-year period, to find innovative solutions to improving the state's education systems. In the face of difficult funding challenges, when many agencies must reduce spending below fiscal year 2011 levels, the House 1 proposal has avoided pulling back on key investments for educating the state's residents.

- ***Executive Office of Health and Human Services (EOHHS)*** – Recognizing the importance of maintaining critical safety net programs and services, the Governor has limited budget reductions to EOHHS agencies and preserved, where possible, programs and services that support the state's most vulnerable populations. Reductions have been avoided in services provided to veterans and have been largely limited in programs that serve the developmentally disabled. Furthermore, the fiscal year 2012 will not adopt broad-based reductions to cash assistance received by families in need nor does it pull back on critical investments to provide more cost-effective care for the disabled in community based settings. Not all reductions could be avoided; state human services agencies will need to reduce their current workforce which will affect the speed in which they can provide services. Furthermore, the state will need to explore ways to manage the operation of state hospital facilities more cost-effectively, and may need to close facilities to live at reduced funding levels.

- ***Executive Office of Public Safety and Security (EOPSS)*** – As mentioned earlier, a significant re-organization is being recommended which would transfer large portions of the Office the Commissioner of Probation from the Judiciary to the Executive Office of Public Safety as a new Department of Community Supervision. In addition, the Department of Correction (DOC) is committed to seeking changes and efficiencies through the Governor's proposed Crime Package pending before the Legislature to achieve savings. Two DOC facilities will need to be closed and the proposed criminal sentencing legislation will help ensure that the state can reduce its overall inmate population in a smart and safe manner without major impacts on current overcrowding levels. Funding provided for the Massachusetts State Police is reduced in fiscal year 2012 from fiscal year 2011 levels, but these reductions can be mitigated, in part, through increased levels of trooper retirements. House 1 proposes the adoption of an annual surcharge on auto insurance policies, which can support critical police recruitment and training initiatives necessary to ensure public safety and adequate trooper levels. Wide-ranging reductions to core public safety functions, such as layoffs to existing state troopers or the closure of a large number of prison facilities, have been avoided in next year's budget.

- ***Massachusetts Department of Transportation (MassDOT)*** – Fiscal year 2011 represents the first full year for the operation of the consolidated Department of Transportation, commonly known as MassDOT. The agency continues to leverage its new structure to seek efficiencies and savings in areas such as procurement and personnel spending. The fiscal year 2012 budget reduces the state operating budget contribution to MassDOT funding by $15 million from fiscal year 2011 levels. This will limit the ability in fiscal year 2012 of MassDOT to provide subsidies to regional transportation agencies as well as to support all planned capital projects and programs. The fiscal year 2012 budget will avoid reductions to staff in the Registry of Motor Vehicles that would create additional challenges to the agency to meet consumer demand for motor vehicle licensing, registration and other services.

- ***Executive Office of Energy and Environmental Affairs (EOEEA)*** – Fiscal year 2012 funding for EOEEA is approximately 1.3 percent below fiscal year 2011 estimated spending. This reflects a $6.25 million investment for increased efforts to promote recycling coordination across the state, which is funded through increased revenues generated by expanding the bottle deposits to include bottled water and sports drinks. After adjusting for this investment, total spending at EOEEA will be 4.6 percent less than fiscal year 2011 levels. To the best extent possible, core programs and services were preserved at the Department of Environmental Protection and the Department of Conservation and Recreation. However, each agency must seek consolidations and reorganizations as a way to operate at reduced funding levels. DEP will re-structure the manner in which it provides oversight of environmental regulations and will explore consolidating facilities and regional locations. The state and urban parks functions at DCR will be fully consolidated helping the agency to live at reduced funding levels in fiscal year 2012.

- ***Executive Office of Housing and Economic Development (EOHED)*** – Fiscal year 2011 funding is approximately 6.1% below fiscal year 2011 estimated spending, with the bulk of the savings coming from reforms proposed to the delivery system for homeless services. The Department of Housing and Community Development (DHCD) will strengthen the state's family homelessness programs by limiting emergency shelter for families that truly need it while providing the remaining families at risk of homelessness with more appropriate and cost-effective housing alternatives. DHCD will leverage innovations that have already been adopted in concert with Lieutenant Governor Tim Murray's Inter-Agency Council on Housing and Homelessness (ICHH) to target resources appropriately to the level of need. The remaining savings in fiscal year 2012 at EOHED will be achieve through the shifting of costs in support of economic development programs to funding contributions provided from quasi-public agencies with related missions.

- ***Executive Office of Labor and Workforce Development (EOLWD)*** – The total contribution from the state operating budget for EOLWD programs in fiscal year 2012 is reduced by 52 percent from the previous year. This reduction does not correspond to substantial elimination of state programs or services. Rather, the Governor's fiscal year 2012 House 1 recommendation proposes legislation that will move all spending (estimated at $29 million in fiscal year 2011) from the Workforce Training Fund off-budget into a dedicated trust fund that is not subject to annual appropriation. All industry contributions to this fund will remain from year to year in the WTF, allowing for improved predictability and transparency of the use of these resources. The fiscal year 2012 budget does call for an increase to the funding provided for the Summer Jobs/YouthWorks program operated by the Commonwealth Corporation. In combination with additional supplemental funding filed by the Governor in January 2011, total funding for this program for the summer of 2011 will equal $8 million.

- ***Executive Office for Administration and Finance (ANF)*** – Spending for appropriations under ANF is reduced by 9.4 percent from fiscal year 2011 levels. Much of this reduction is attributed to the elimination of one-time collective bargaining reserves for negotiated agreements that have been ratified with state labor unions across the Executive branch, sheriffs' offices and higher education campuses. Another main driver of reduced ANF spending is a $65 million reduction to the state's unrestricted local contribution to cities and town. This reduction is partially offset by $10 million in investments to support efforts by municipalities to regionalize their services and seek additional cost savings measures through best practices. In addition, the Governor proposes to provide further relief to cities and towns by expanding the options at their disposal to control health care spending. Statewide, cities and towns are expected to save more than $110 million through seeking lower cost options to their existing employees' health care plans, as well as from shifting retirees from locally-funded health care plans to those that are partially supported with Medicare contributions. Finally, state health care spending for employees' coverage through the Group Insurance Commission (GIC) will be held to fiscal year 2011 levels. While this does not reflect a year-on-year reduction in projected spending, it is expected that the GIC will need to utilize aggressive cost-saving measures, including seeking lower cost provider networks for employees to access care.

- ***Transfers to Health Care and Other Funds*** – Fiscal year 2011 was the first year in which transfers to off-budget funds where shown in the budget as direct appropriations. In total, the state will spend $1.574 billion in fiscal year 2012 on transfers, primarily to the Commonwealth Care Trust Fund, the Medical Assistance Trust Fund, and the State Retiree Benefits Trust Fund. Total spending in fiscal year 2012 will be $196 million less than fiscal year 2011 levels, which is primarily related to the state's reduced spending on payments to hospitals through the MATF as well as payments made this fiscal year that were originally authorized for fiscal year 2010. These payments are one-time in nature and are fully supported with federal revenues and do not reflect a reduction in programs and services.

School Aid for Public K-12 Education

Spending Comparison, K-12 Aid, FY2012 vs. FY2011				
Executive Branch Government Area	**FY2011 Estimated Spending**	**FY2012 H.1 Spending**	**Variance**	**% Change**
Public Education School Aid (Chapter 70)	3,851,193,043	3,990,519,338	139,326,295	3.6%

The fiscal year 2012 budget provides $3.991 billion in aid for public education (grades K-12) to local school districts, which represents a year-on-year increase in state-funded school aid of $139.8 million, or 3.6 percent greater than fiscal year 2011 state funding. It should be noted that in fiscal year 2011, local school districts received approximately $221 million in federal stimulus assistance ($21 million in ARRA State Fiscal Stabilization Funds and $200 million in EduJobs aid provided in August 2010). Even after accounting for the fact that fiscal year 2011 spending is roughly $121 million greater than the operating budget only contribution, the fiscal year 2012 recommended funding levels still reflects a total increase in aid to cities and towns in the face of challenging fiscal times.

The state's contribution to quality education and opportunities for all of its residents is a core priority of the Patrick-Murray Administration. The fiscal year 2012 House 1 recommendation continues to build off of the state's earlier commitments to preserve Chapter 70 investments in our K-12 education, a fundamental tool in addressing the achievement gap and ensuring that today's students will be prepared to compete for the jobs of tomorrow.

Aid to Higher Education Campuses

Spending Comparison, Higher Education, FY2012 vs. FY2011				
Executive Branch Government Area	FY2011 Estimated Spending	FY2012 H.1 Spending	Variance	% Change
Aid to Higher Education Campuses	835,187,294	823,033,934	(12,153,360)	-1.5%

The state funding provided to the 29 universities and community colleges across the states will be reduced in fiscal year 2012 by 1.4 percent or $12.2 million. This reduction, however, reflects the fact that public universities, beginning in fiscal year 2012, will be able to "retain" all tuition payments collected from students from out of state that attend their campuses. In total state universities will be able to retain $19.6 million in additional revenue in fiscal year 2012 and the state appropriation was adjusted downward to reflect this change. In addition, the Department of Higher Education will oversee a new innovation reserve, funded at $7.5 million in fiscal year 2012, which will provide competitive grants to universities and community colleges to support their efforts to better streamline their operations and seek collective cost-saving efficiencies. The fiscal year 2012 funding does not restore over $70 million in ARRA-funded State Fiscal Stabilization Fund that were available to the campuses in fiscal year 2011 to support their operations.

MassHealth (Medicaid) Spending

Spending Comparison by Major Government Area, FY2012 Vs FY2011 ($s)				
Government Area Name	FY2011 Estimated Spending	FY2012 H.1 Spending	FY2012 H.1 vs. FY2011 Spending	Percent Change
MassHealth	10,240,029,259	10,340,029,259	100,000,000	1.0%

The Massachusetts Medicaid program (MassHealth) provides comprehensive health insurance to approximately 1.28 million low-income Massachusetts children, adults, seniors and people with disabilities. The Administration's fiscal year 2012 budget includes $10.34 billion for the MassHealth program, essentially level funding from fiscal year 2011 estimated spending level of $10.24 billion, after accounting for the full-year costs of supplemental funding provided this year.

Like nearly every state in the union, the Massachusetts' Medicaid program experienced exceptional growth, and related spending, during the economic downturn that began in 2008. Total Medicaid spending growth averaged 8.8 percent across all states in fiscal year 2010, and is expected spending to see a further 7.4 percent increase FY2011. Likewise, enrollment growth averaged 8.5 percent nationally and expected to reduce slightly to 6.1 percent this year.

Governor Patrick's and Lieutenant Governor Murray's fiscal year 2012 budget seeks to achieve ground-breaking progress in health care cost containment – with a vision for maintaining the Commonwealth's historic coverage gains and high-quality care while making health care spending more affordable for the state and taxpayers. The Administration's goal is to leverage the state's immense purchasing power to be a force for rewarding models that provide cost-effective, high-quality coverage and care to those who rely on state health insurance and better coordinate government's health care purchasing decisions. A further discussion in this narrative elaborates on the types of measures necessary in fiscal year 2012 to be taken to control the growth in MassHealth spending.

Reforming the Way the Government Does Business

The Governor's House 1 budget, and concurrent legislation filed with the fiscal year 2012 recommendation, reflects the need for state government to change the way it does business. Adopted in the House 1 recommendation are a number of reforms and initiatives that will help state agencies perform core business more effectively while ensuring the state government programs and services are provided to residents in the most cost-effective manner. There will be necessary reductions required of agencies to live within the funding available to them in fiscal year 2012. However, the following reforms and initiatives described below can help to mitigate the impact of funding reductions as well as make sure every tax dollar is stretched to the fullest extent possible.

Criminal Justice Reform

Criminal justice reform is essential to both enhancing public safety and to the Commonwealth's sound fiscal management. States across the country are re-examining sentencing and corrections policy to manage under constrained operating budgets, and Massachusetts cannot afford to be an exception. On an annul basis, the Commonwealth spends approximately $47,000 per offender.

The Governor proposes extensive reforms throughout the entire system that incorporate best practices and well-documented research in the field of criminal justice. This reform plan includes legislation that will toughen criminal sentences for repeat violent offenders while repealing mandatory minimum sentences for non-violent drug crimes. The proposal, when public safety permits, favors community supervision of criminal defendants and offenders, saving the Commonwealth tens of millions of dollars over the next ten years. This approach reduces recidivism, incarceration rates and sky-rocketing costs, while effectively transitioning inmates back to society.

As noted previously, unavoidable spending cuts within the Department of Correction's fiscal year 2012 budget will result in the closure of two prisons. Prison closures do not result in any inmate releases as inmates will be relocated to other prisons within the Department of Correction. The Governor's sentencing reform legislation will help alleviate additional overcrowding that would otherwise result from prison facility closures. To allow the Department of Correction and Sheriff Departments to best operate under reduced budgets,

The Governor also seeks to restore confidence in both the Department of Probation and the Parole Board by consolidating both departments under a new executive branch agency, the Department of Re-entry and Community Supervision. This new agency will supervise all forms of community supervision from defendants in early pretrial stages of the criminal process to inmates released after incarceration. The Governor's H.1 budget reflects this consolidation by providing $114.7 million for the new department, which is proposed in legislation filed concurrent with the budget.

This budget also includes an overhaul of the Commonwealth's system for providing criminal defense for indigent persons. This recommendation would shift funding currently provided for the Committee for Public Counsel Services (CPCS) under a new, independent agency titled the Department of Public Counsel Services. The chief counsel of the DPCS will be appointed by the Governor and will be authorized to fund indigent counsel services that are provided entirely by state staff attorneys, saving more than $45 million. Savings are generated from the elimination of a system that relies almost entirely on the use of private attorneys that bill for services by the hour.

Controlling Health Care Costs

The Patrick-Murray Administration is proposing an aggressive procurement reform strategy to help manage costs in all state health care programs (MassHealth, Group Insurance Commission, and the Commonwealth Connector Authority) which will serve to encourage members and state employees choose lower-cost settings and streamlining the purchase of health care plans and services throughout state and local government.

The Governor will file legislation that proposes new tools for cities and towns to help manage their own employees' health care costs. These costs, incurred for both current and retired employees, reflects the biggest municipal budget buster. The Governor proposes a new local health insurance plan design process that will achieve real savings for cities and towns with meaningful labor participation in the process, and a requirement that all municipalities enroll their eligible retirees in Medicare, as this federal program covers a substantial portion of that population's health care costs.

Small businesses will also benefit from this proposal through updates launched by the Connector to its Commonwealth Choice program, which creates a streamlined, simplified process for small businesses and individuals to shop for unsubsidized, name-brand health insurance, saving them money by making it easier for them to understand their options and choose better-priced health plans. The Connector will also be eliminating a fee it currently charges small businesses to shop through Commonwealth Choice, and will receive $10 million in the budget to offer premium discounts for certain small businesses which purchase coverage through Commonwealth Choice and set up wellness programs for their employees. This will reduce premiums for qualifying small businesses by up to 5%.

Homeless Shelter Reform

Building off of the fiscal year 2010 reorganization of services provided to individuals and families that are homeless or at-risk of becoming so, the House 1 proposes to move forward with the Patrick-Murray Administration's comprehensive strategy to reform emergency shelter and housing delivery systems for families. These changes will help advance our goal of ending homelessness in our Commonwealth by continuing to focus on moving families to housing first, while providing critical safety net services to stabilize families for long-term success. This proposal will also help address on-going budget challenges caused by dramatic caseload growth in recent years. In this next phase of reform proposals, we will implement measures that are effective and cost efficient, and will ensure a more streamlined and compassionate response for families facing homelessness.

Municipal Relief

The fiscal year 2012 budget continues the Patrick-Murray Administration's unprecedented support for cities and towns. We have provided many tools for municipalities that are needed to mitigate reductions, generate savings and create efficiencies at the local level. Our approach includes a number of measures worth more than $160 million that will provide cities and towns with relief, reform and expanded opportunities to offset the tough funding decisions municipalities are facing.

New fiscal reality demands that we invest in and incentivize innovation among local governments to find new and more efficient ways to delivery local services. Modest investments are proposed to provide financial support for one-time or transition costs related to regionalization and other efficiency initiatives to improve the quality and efficiency of local government service delivery in ways that achieve cost savings. These efforts also include establishing a program to enhance performance management, accountability, and transparency for local governments. This incentive will be overseen by municipal officials and administration officials with the support of the Collins Center for Public Management at the University of Massachusetts Boston.

Enhanced Emergency Response

The budget establishes authority for the Governor to temporarily draw funds from the stabilization fund to cover the immediate emergency response costs incurred by natural disaster and other unanticipated events that are not eligible for federal reimbursement funds. As shown by the Greater Boston water main break on May 1, 2010, when emergencies strike agencies must scramble to funding disaster response and relief efforts. Depending on the stage in the fiscal year, agencies may need to seek emergency appropriations from the Legislature. This measure is necessary to help make sure agencies have access to immediate resources, where necessary, until the Legislature is able to provide additional funding.

Commonwealth Performance, Accountability and Transparency (CPAT)

This budget establishes a new office of Commonwealth Performance, Accountability and Transparency to promote greater accountability through performance management, enhanced transparency, ensuring access and opportunity and promoting greater program integrity. CPAT will implement the Commonwealth's performance management program (MassGOALS) and work with other state agencies and quasi agencies to advance performance management statewide. The office will coordinate federal grants and implement the Federal Financial Accountability and Transparency Act (FFATA) which passed in September 2006, enhance budget forecasting and fully develop the Commonwealth's transparency website.

This past year, the Lieutenant Governor chaired a Fraud, Waste and Abuse taskforce. One of the many recommendations that have come out of that effort is to ensure the Commonwealth develops stronger connections between the various oversight agencies like the State Auditor, the Attorney General, and the Inspector General with the various program integrity units that exist in the Executive Branch. CPAT will help coordinate these various activities and do everything we can to ensure program integrity throughout the Commonwealth.

Inter-Secretariat Budget Team (ISBT)

At the Governor's request, the Executive Office for Administration and Finance (ANF) assembled an interagency workgroup on December 1st to review possible budget efficiencies, reforms and savings initiatives called the Inter-Secretariat Budget Team (ISBT). Below are highlighted the major savings initiatives that are adopted within the fiscal year 2012 budget. In general, the ISBT focused on savings that avoided direct service delivery disruption through greater efficiencies through additional agency tools.

Shared Services

The majority of executive branch agencies in the Commonwealth carry out administrative operations separately within a given department. Although the business or programmatic missions of such departments are understandably distinct and separate, tremendous opportunity exists to re-organize administrative operations across departments, consolidating and/or sharing “like” functions where possible. The House 1 budget seeks to increase administrative efficiencies and savings through: improving delivery of administrative services and simplify, streamline and standardize processes in all possible cases; ensuring we have the most efficient and cost effective administrative teams possible; standardizing purchasing policies, solicitation, and decision making processes to achieve best pricing options and improve quality of purchased goods and services; and, enabling secretariats to tailor their implementation strategy to reflect the attributes of their organization, while moving toward a common goal and common outcomes on a shared timeline. Incentives will be developed to recognize the successful and aggressive implementation of shared services by agencies.

Procurement Reform

According to a recent report from the Pew Center on the States, state governments purchase nearly $200 billion in goods and services annually, with Massachusetts purchasing as much as $5 billion annually. While various procurement reforms and vendor discounts have been implemented over the past several years, recent examples from the Department of Transportation (MassDOT) suggest that substantial savings can still be achieved through a more aggressive approach toward procurement reform, with a greater emphasis on cost. For the fiscal year 2012 budget, it estimated that $30 million could be saved by implementing the following general approach: placing a greater emphasis on aggregation of purchase through shared service; creating a Chief Procurement Officer within each Executive Office and a “Purchasing Cabinet” to develop more strategic aggregate purchasing opportunities; and, learning from the MassDOT experience, examine the state’s standard terms and conditions to determine where modifications can lead to substantially better cost outcomes.

Better Management of State Assets

As the Commonwealth continues to recover from the recession, it is imperative that our state agencies take a more proactive and strategic approach to how we manage our inventory of state-owned real property and leased facilities. As a concept, strategic asset management provides a foundation from which to monitor the Commonwealth’s real property holdings and lease agreements in order to optimize return on investment, value maximization, economies of scale and other efficiencies and benefits to the Commonwealth and its residents. By identifying under-utilized assets and piloting a new economic development / value maximization effort with MassDevelopment, substantial income can be generated in FY 2012

After a thorough review of state-owned real property holdings, ISBT identified and examined several land holding which could be considered surplus and disposed of during FY 2012. Specifically, ISBT identified more than 180 acres and approximately 8 structures as surplus, with a potential combined value of between $7.75 – 17.8 million.

Improving Coordination of Transportation Services

Several state agencies across state government purchase transportation services on behalf of state clients they serve, most notably the Executive Office for Health and Human Services (EOHHS) and MassDOT. The Governor’s House 1 proposal will establish an interagency Commission to examine opportunities for restructuring, improved coordination, enhanced federal revenue collection, streamlined eligibility criteria and other major reforms to the paratransit system. In parallel with this effort, EOHHS and the MBTA/MassDOT will be working to implement a new revenue collection effort that could generate additional federal funds for the General Fund.

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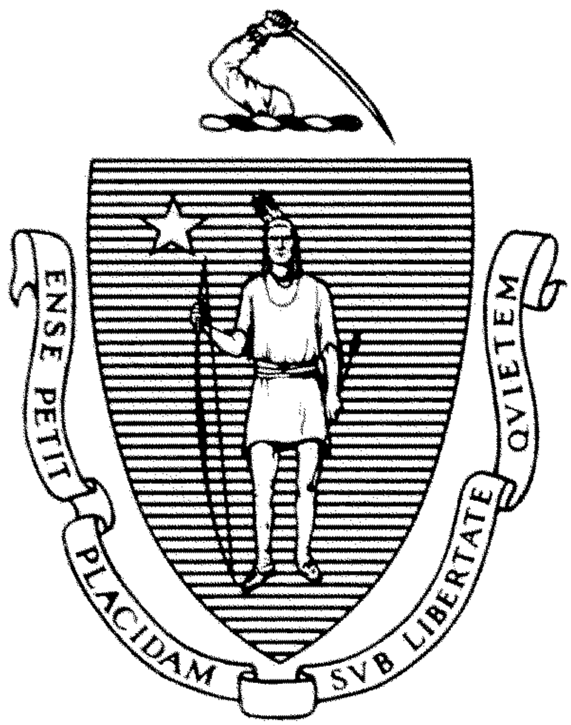
Fiscal Year 2012 Budget Recommendation



Health Care Cost Containment

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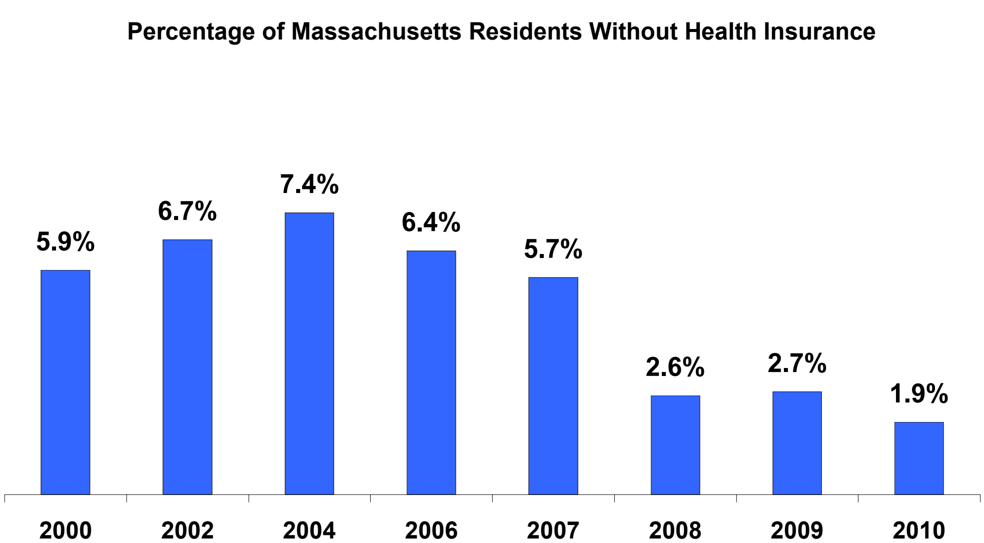
Health Care Cost Containment

Section I: Introduction

The Commonwealth is a national leader in ensuring access to quality, affordable health insurance. More than 98% of our residents have coverage, the highest rate of coverage in the nation – with nearly all children (99.8%) and seniors (99.6%) insured.



Source: Massachusetts Division of Health Care Finance and Policy. Key Indicators Report. November, 2010.

Racial and ethnics disparities in coverage have been significantly reduced. Since the enactment of health care reform, an even *higher* percentage of Massachusetts employers are offering health insurance to their employees, bucking a national trend.

Evidence of the impact of health care reform in Massachusetts is clear. Thousands who formerly relied on receiving care in over-burdened emergency rooms now have access to primary care through their own doctors. More than 90% of adults in Massachusetts report having a regular source of care. Since reform more adults are making a visit for preventive care, and 63% of men have had colonoscopies.

Health care reform benefits not just our residents but also our economy. Healthier people mean a more productive workforce for the Commonwealth. Likewise, investing in health care strengthens our world-renowned medical sector –where interventions ranging from improved routine care for diabetics to life-saving interventions for rare conditions save lives - and as an engine for job creation; and a magnet for research dollars and human talent. The Administration's separate, ground-breaking investment in life sciences creates enormous potential synergies with our commitment to health care reform, together ensuring Massachusetts' status as *the world leader* in health care.
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The success of the Massachusetts model is also reflected in the enactment of national health care reform (the Patient Protection and Affordable Care Act). National health reform is based significantly on our approach in the Commonwealth, requiring all states to set up Exchanges modeled on the Massachusetts Health Connector,

requiring those who can afford coverage to maintain it, reforming insurance laws to open the doors to coverage for all consumers, and broadening access to subsidized health insurance for those who need it. With our leadership in coverage expansion, we are poised to implement national reform in Massachusetts successfully and broaden opportunities for affordable coverage for our residents.

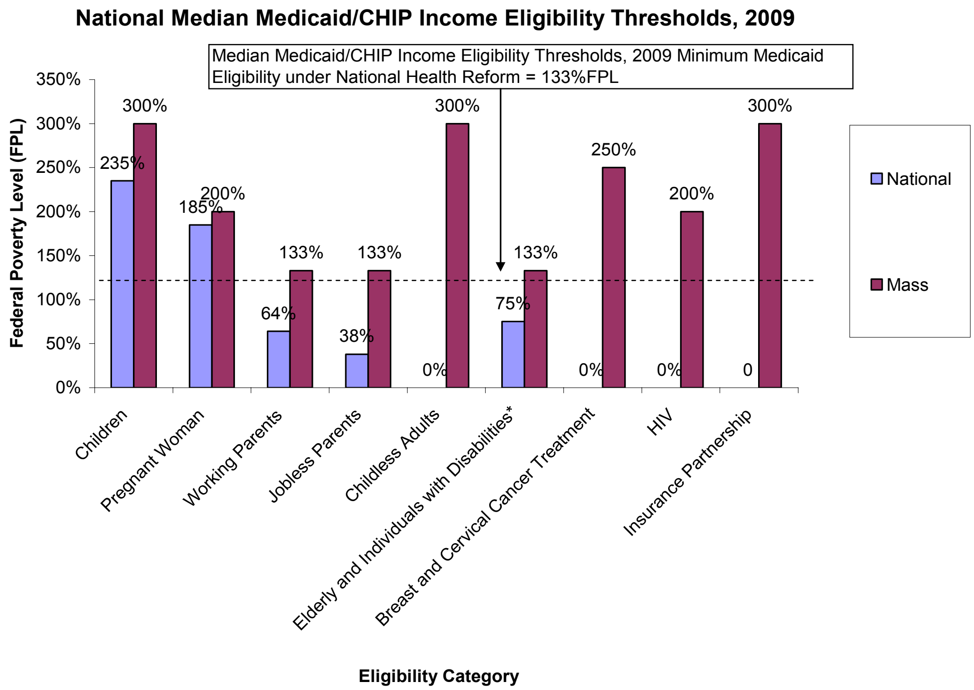
The Patrick-Murray Administration is deeply committed to the successful implementation of health care reform, partnering with the Legislature to provide policy leadership on key implementation decisions and the funding needed to offer affordable coverage to those in need. Much of the success of health care reform is due to a strong community effort, relying on partnerships with providers, insurers, consumers and businesses to ensure that health coverage is accessible, understandable, and comprehensive. Throughout the most profound economic downturn of our time, these stakeholders worked with the Administration and Legislature to maintain coverage. As unemployment rose nationally and here in Massachusetts, access to affordable coverage through our health reform initiatives kept the Commonwealth's residents healthy.

The Administration has carefully managed the finances of health care reform. Independent, non-partisan analysis underscores that the incremental state costs of health care reform have been moderate and in line with original expectations. Recent enrollment growth in state-subsidized coverage is a natural consequence of an economic downturn and a sign of *strength* of the Massachusetts model, protecting coverage for residents who have lost their jobs. Private health insurance (largely through employment) remains the dominant form of coverage in the Commonwealth.

However, while the incremental costs of health care reform have been moderate, the total costs of state-subsidized coverage create a difficult challenge for the Commonwealth. These costs – a function of our eligibility standards and enrollment, the frequency with which care is sought, and how and where care is provided – are occupying an ever-increasing share of the state budget. Spending in state subsidized health care programs have grown by double digits since fiscal year 2008 while other programs like Local Aid, higher education, public safety, environmental protection services, and economic development have all been reduced. Health care spending for our subsidized coverage programs consumes more than 35% of the state budget. Based on long term forecasts conducted by the Executive Office for Administration and Finance, were health care costs were able to continue to grow at these historic rates it would consume approximately 50% of state spending by 2020**.** Health care spending has been crowding out key public investments that, among other things, likewise significantly impact the health and welfare of our citizens and the historic trends are unsustainable. While all states are struggling with the growth of health care spending, the higher cost of care in Massachusetts means that employers, families and municipalities are also wrestling with the ongoing challenge of choosing between health care and spending on job creation and other family and public needs.

These are not insurmountable challenges. There are opportunities to control health care costs by promoting care delivery in lower-cost, high-quality settings, improving the coordination and management of care, placing a greater focus on prevention, and adopting innovative payment models that reward high-value care instead of high-volume care. With the scale of the health insurance coverage it purchases, the state is well-positioned to capitalize on these opportunities and drive positive innovation in our health care insurance and delivery systems, containing costs while maintaining coverage and improving quality of care. The state also has opportunities to achieve greater efficiencies and continuity of coverage within state-subsidized programs by aligning coverage standards and coordinating on procurements. Taking advantage of these opportunities is particularly imperative for fiscal year 2012, where the elimination of enhanced federal Medicaid matching funds as a budget-balancing tool renders the need for immediate action to achieve health care cost savings imperative.

Governor Patrick's and Lieutenant Governor Murray's fiscal year 2012 budget seizes the moment to achieve ground-breaking progress in health care cost containment – with a vision for maintaining the Commonwealth's historic coverage gains and high-quality care while making health care spending more affordable for the state and taxpayers. For each of the state's health care programs -- MassHealth, Commonwealth Care, the Group Insurance Commission and the Medical Security Program – the budget proposes bold changes emphasizing the power of competition and innovative contracting to promote continued access to coverage and high-quality care while achieving significant cost savings. The Administration's goal is to leverage the state's immense purchasing power to be a force for rewarding models that provide cost-effective, high-quality coverage and care to those who rely on state health insurance and better coordinate government's health care purchasing decisions. It would maintain eligibility for all state-subsidized health insurance programs – under the most generous eligibility standards in the nation (see below).



Note: Medicaid income eligibility for most elderly and individuals with disabilities is based on the income threshold of Supplemental Security Income (SSI).SOURCE: Based on a national survey conducted by the Center on Budget and Policy Priorities for Kaiser Commission on Medicaid and the Uninsured, 2009.
* Senior and disabled individuals can be up to any income if they meet a certain buy-in criteria

Separately, the Administration is planning on filing comprehensive payment reform legislation in the coming weeks that will, across the health care delivery system, promote movement away from “fee-for-service” payments to providers towards “global payments” and other models that better reward evidence-driven, coordinated, preventive care. In combination with the Administration’s budget initiatives, this legislation will place Massachusetts squarely in the forefront of national efforts to contain health care costs while ensuring high-quality coverage and care.

Section II: Health Coverage

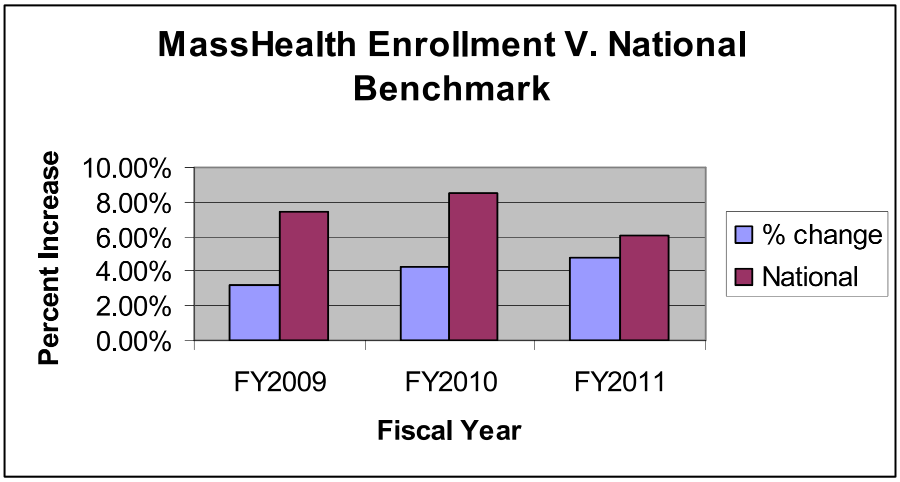
MassHealth

The Massachusetts Medicaid program (MassHealth) provides comprehensive health insurance to approximately 1.29 million low-income Massachusetts children, adults, seniors and people with disabilities. The Administration’s fiscal year 2012 budget includes $10.34 billion for MassHealth, essentially level funding from the fiscal year 2011 estimated spending level of $10.24 billion. Due to tremendous fiscal pressures in fiscal year 2012 stemming principally from the loss of more than $1.2 billion in enhanced federal matching funds, the Administration established aggressive spending targets for all state programs, in some cases reducing funding below fiscal year 2011 levels.

Massachusetts is not the only state with a Medicaid budget that has experienced exceptional growth. Medicaid budgets across the nation have experienced unprecedented spending increases. Enrollment in Medicaid historically mirrors trends in the economy, with more individuals turning to public assistance during tougher times. Total Medicaid spending growth averaged 8.8% across all states in fiscal year 2010, and spending is expected to increase by 7.4% in fiscal year 2011. Enrollment growth averaged 8.5% nationally and is expected to decrease to 6.1% in fiscal year 2011.[1]

[1] Kaiser Commission on Medicaid and Uninsured, “Hoping for Economic Recovery, Preparing for Health Reform: A Look at Medicaid Spending, Coverage and Policy Trends” September, 2010.

While Massachusetts is experiencing the same caseload and spending pressures, our projected increases in these areas are well below national benchmarks. This is likely attributable to a stronger health insurance coverage base prior to the economic downturn.



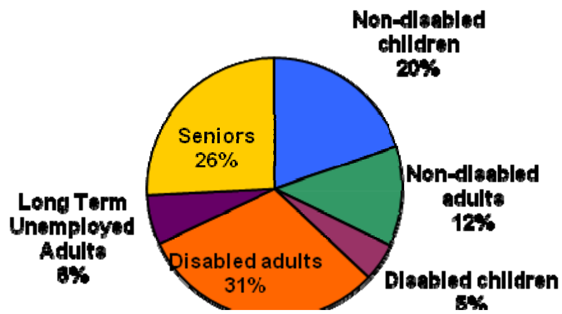
Enrollment and utilization are the greatest cost drivers in MassHealth and are sensitive to changes in economic climate. From fiscal year 2008 to fiscal year 2010, long-term unemployed adults (unemployed for 12 months or more) represented the fastest growing population in Medicaid, increasing by an average of 16.6% each year. Non-disabled adults represent the next highest category of growth, increasing by an average of 4.44%. Overall, from fiscal year 2008 through fiscal year 2011, MassHealth enrollment grew by approximately 146,000 people.

MassHealth Average Enrollment (in Member Months)

	Fiscal year 2008	Fiscal year 2009	Fiscal year 2010	Projected fiscal year 2011	Projected fiscal year 2012
Non Disabled Children	459,712	469,618	486,806	501,815	519,700
Non Disabled Adults	263,247	273,315	283,176	297,685	314,181
Disabled Children	26,501	26,510	27,371	29,273	30,424
Disabled Adults	207,559	210,506	213,952	223,585	232,326
Long Term Unemployed Adults	66,921	79,642	96,221	110,782	124,235
Seniors	125,483	125,874	128,380	132,194	134,658
Total	1,149,423	1,185,465	1,235,907	1,295,335	1,355,523
% change		3.1%	4.3%	4.8%	4.6%

Medicaid continues to be a primary source of health care for low-income children, and projected to be the largest MassHealth population group at 41% in fiscal year 2012. The senior and disabled populations account for almost 30% of enrollment and more than 60% of total MassHealth spending. Programs experiencing the largest annual cost increases are those that serve seniors and the disabled.

FY12 Maintenance Expenditure Projections By Population



Payments to MCOs have increased annually by an average of 12.43% from fiscal year 2008 to projected trends in fiscal year 2011, primarily due to an enrollment increase of 86,400 members over four years and federal requirements to maintain actuarially sound rates. Without smart cost-saving changes to MassHealth, the Commonwealth could face an $800 million shortfall in fiscal year 2012 and the prospect of across-the-board cuts to services. Even beyond the need to achieve savings to address immediate, economy-driven fiscal challenges facing MassHealth, containing MassHealth costs is critical to the long-term sustainability of health care reform and the long-term ability of the state budget to invest in the *full range* of public needs. Success on this front would not only maintain our health care safety net for all who need it as well as facilitate other key public investments, but also – given the scale of MassHealth – drive positive innovation in the delivery of care throughout our health care system.

Given these short- and long-term challenges and opportunities, MassHealth will be pursuing aggressive strategies to manage its fiscal year 2012 budget. Unlike other state programs, MassHealth costs are difficult to constrain, since expenditures are driven by caseload and eligibility is primarily controlled by eligibility standards fixed by the federal government. Despite these challenges, MassHealth has developed proposals to improve payment efficiency while preserving services for MassHealth enrollees.

Starting immediately, MassHealth plans to conduct a competitive procurement that will focus on reducing costs while providing quality care to over 800,000 members. The procurement will include both the managed care and the Primary Care Clinician plan but will not include seniors or dual eligible members. The goals of the procurement are to ensure access and quality care for members at the lowest cost. MCO's and providers who demonstrate the ability to provide this care will have the opportunity to expand membership. The procurement process will promote innovative approaches to care management and delivery as well as payments for services for this population. In addition, MassHealth will begin to lay the foundation for a comprehensive plan to promote the efficient delivery of care for MassHealth members under age 65 with a focus on care integration and care management for the highest-risk populations.

This procurement strategy will only mitigate a certain amount of growth in MassHealth costs that would otherwise occur. MassHealth plans to undertake several other steps such as constraining provider and capitation rates, limiting payments for preventable admissions, implementing small co-pays for some services, adopting additional program integrity measures, and limiting coverage for certain optional benefits.

Beginning in fiscal year 2011 and continuing in fiscal year 2012 and beyond, MassHealth will be launching a project to manage the dual population that is eligible for Medicare and Medicaid. A pivotal building block in systemic transformation to improve the delivery of health care and make health care costs sustainable for the long-term is MassHealth's initiative to integrate Medicare and Medicaid for young dual eligible adults.

MassHealth's dual eligible adults ages 21-64 have disproportionately experienced the shortcomings of the fee-for-service payment system and fragmented, uncoordinated care, simply because few alternatives are available to them. MassHealth's goal is to develop a Medicare and Medicaid integrated service delivery model option for dual eligible adults that:

- builds on Massachusetts' knowledge and experience with integrated care programs;
- further promotes the goal of assuring that every member establishes a primary source of ongoing coordinated care;
- offers access to the benefits of integrated care, similar to what exists now for seniors;
- provides an alternative to the fee for service (FFS) system; and
- offers an option that meets individual needs and personal preferences.

MassHealth is engaged in discussions with consumer advisory groups to ensure that this new integrated care model meets the needs of the younger dual eligible population and is attractive to members so that they will want to enroll. The new model's care entities will be accountable for the delivery, coordination, and management of health and community support services that promote improved outcomes and living with dignity and independence in the community. MassHealth envisions that the Medicare and Medicaid benefits would be administered jointly through an integrated financing mechanism at the state level such that dual eligible individuals would experience their coverage as a single, integrated care program. The Commonwealth is continuing to pursue this concept with the federal government.

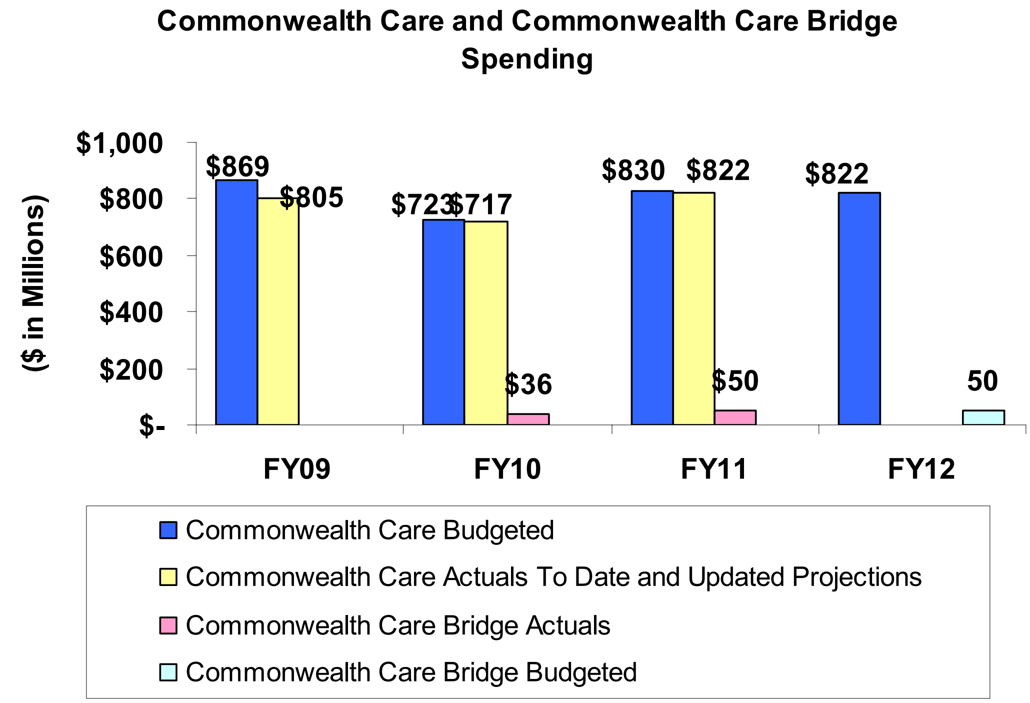
Fiscal Year 2012 MassHealth Cost Control Initiatives (in millions)

	Gross	Net
Rates	$ 150	$ 75
Capitation Cost Controls	$ 169	$ 84
Benefits/copays	$ 66	$ 33
Program Integrity	$ 13	$ 7
Procurement and Payment Strategies	$ 351	$ 175
Medicare Integration (Duals Initiative)	$ 50	$ 25
Total	$ 798	$ 399

Commonwealth Care

The Commonwealth Care program was created with the enactment of health care reform and is administered by the Health Connector. The program provides health insurance coverage for individuals under 300% of the federal poverty level that do not have access to employer-sponsored insurance. Commonwealth Care fully subsidizes individuals under 100% of the federal poverty level and institutes a sliding scale of member premiums for those above that income threshold. It provides health care services through a fully capitated insurance model. As of January of 2011, there are 160,824 members enrolled in Commonwealth Care, excluding the Aliens with Special Status population (*see next section on Commonwealth Care Bridge*).

The budget provides $822 million for Commonwealth Care in fiscal year 2012, equivalent to currently projected fiscal year 2011 spending. These funds are designed to maintain eligibility for the program and pay for moderate additional enrollment (including coverage for individuals that transition from the Medical Security Plan to Commonwealth Care after their unemployment benefits expire).



The Administration envisions that the Health Connector will conduct a procurement process for the Commonwealth Care program, which will incent aggressive bidding and achieve savings by rewarding innovative, lower-priced health plans with increased membership. Under this vision, the Health Connector would strengthen existing program rules that currently provide incentives for some Commonwealth Care members to select lower-priced plans. This competitive procurement strategy would aim to leverage premium savings that enable the Health Connector to maintain eligibility for comprehensive coverage, pay for growing enrollment, and minimize increases in cost-sharing within a level-funded budget. In addition, the procurement will require MCO's to work with the Health Connector in developing payment reform proposals in coordination with the MassHealth procurement. Overall, this approach intends to encourage game-changing innovations in contracting and care management that can help achieve sustainable health care cost savings inside and outside of the Health Connector.

Commonwealth Care Bridge

Aliens with Special Status (*legal* immigrants who have resided in the U.S. for less than five years) lost eligibility for Commonwealth Care in fiscal year 2010, due to the extreme fiscal challenges created by a national economic downturn and the fact that the federal government does not reimburse states for health insurance coverage for this population. Instead, a separate investment of $40 million was appropriated to provide health insurance for this population. This coverage is now available through the newly created Commonwealth Care Bridge program. The Commonwealth Care Bridge program was maintained in fiscal year 2011 at a projected cost of $50 million.

Commonwealth Care Bridge currently provides coverage to 20,389 Aliens with Special Status, who were enrolled over a three-month period from October to December of 2009. Enrollees have been eligible to receive comprehensive coverage through a network of providers that fully meets the Connector's Commonwealth Care network adequacy standards. While cost-sharing is in some instances higher than that for Commonwealth Care and some benefits are excluded, steps have been taken to reduce any hardships for members.

The Administration's fiscal year 2012 budget includes level funding of $50 million for the Commonwealth Care Bridge program. This program will continue to be run by the Secretary of Administration and Finance, the Secretary of Health and Human Services and the Executive Director of the Connector. The budget aims to maintain coverage for current Commonwealth Care Bridge enrollees through fiscal year 2012.

This funding for coverage for Aliens with Special Status reflects the Administration's continuing commitment to providing health insurance to these legal residents of the Commonwealth. The Administration's ultimate goal remains fully integrating Aliens with Special Status into Commonwealth Care. While that is not possible in the current fiscal environment (particularly given current federal reimbursement policy), national health reform will help by providing federal funding for subsidized coverage for Aliens with Special Status starting in 2014.

The Administration intends to keep the same benefit and cost-sharing structure for Commonwealth Care Bridge, given fiscal constraints and our goal of maximizing capacity of the program, but will continue to take steps to mitigate hardships.

Medical Security Program

The Medical Security Program (MSP) provides health insurance assistance for Massachusetts residents with family income less than 400% FPL, while they are receiving unemployment benefits. There are two different types of coverage offered through the MSP program: Premium Assistance and Direct Coverage. The Premium Assistance program is for COBRA eligible claimants, who may be reimbursed for up to 80% of their monthly premium, subject to a cap. The Direct Coverage program is for claimants not eligible for COBRA, or those who qualify for a waiver---they may enroll in coverage procured by the Division of Unemployment Assistance (DUA). There is no monthly premium for this option, but claimants are subject to equal co-payments at all income levels. The Medical Security Trust Fund which funds the Medical Security program has been under enormous fiscal stress due to continued extensions of unemployment benefits.

To pursue savings and improve alignment of state-subsidized health insurance programs, the Administration is requesting that the Health Connector work with the Division of Unemployment Assistance (DUA) to conduct a new, competitive procurement for MSP Direct Coverage and restructure the program to maintain eligibility for adults and children up to 400% FPL, while more closely matching Commonwealth Care coverage. Under this reform, members would receive coverage under plan types modeled after Commonwealth Care with a progressive cost-sharing and premium structure and improved continuity of coverage. The program would continue to be financed through employer contributions to the Medical Security Trust Fund. This initiative reflects a "shared responsibility" solution to maintaining health insurance coverage for families receiving unemployment assistance despite unprecedented fiscal stress on the Medical Security Trust Fund – combining recently increased employer contributions to the Medical Security Trust fund, program savings through a re-procurement and coverage re-design, and continued state contributions.

Group Insurance Commission

The Group Insurance Commission (GIC) will contain costs for state employees' health care by negotiating lower rates and providing an incentive for employees to join limited network plans. The GIC will conduct a full open re-enrollment that will incent employees to move to limited network coverage, which costs less than broad network plans. The full open re-enrollment will require state employees to choose a plan during the annual open enrollment period in May. Historically, only 2% of active state employees actively select a plan during the annual open enrollment; those who do not are simply re-enrolled in their existing plan. In fiscal year 2012, state employees that move to a limited network plan will pay a lower premium for health insurance, as well as receive a reimbursement that is equal to three months of premium payments. The employees that move to the lower-cost plan in fiscal year 2012 will save on average an estimated $800 for individual coverage and $1,700 for family coverage. Employees moving to lower-cost plans will also result in tens of millions of dollars in savings for GIC. These savings, combined with controls on rate increases will allow the GIC to live with a level budget. Those employees who want to stay in a broad network plan will have that option.

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Health Safety Net

Overseen by the Division of Health Care Finance and Policy, the Health Safety Net (HSN) reimburses hospitals and community health centers for health care services provided to low-income uninsured or underinsured residents. Prior to the enactment of health care reform, this financing mechanism was known as the Uncompensated Care Pool. The Health Safety Net is financed by dedicated revenues from an assessment on hospitals ($160 million) and an insurer surcharge ($160 million), other offsetting revenues ($70 million), and any state contribution from the General Fund.

Although success in expanding enrollment in health insurance through health care reform has resulted in decreased Health Safety Net utilization and payments, economic pressures from the recession have resulted in increased HSN utilization over the past three years. An unstable economy naturally lends itself to individuals ‘cycling’ in and out of short-term employment and underinsurance; the trends in the HSN from fiscal year 2010 through fiscal year 2011 reflect these natural increases in the burden on safety net care.

Health Safety Net Trust Fund- Sources			
	FY10	FY11	FY12
Assessments	$ 320.00	$ 320.00	$ 320.00
Offset	$ 70.00	$ 70.00	$ 70.00
Commonwealth Contribution	$ 30.00	$ 30.00	$ 30.00
Total Sources	**$ 420.00**	**$ 420.00**	**$ 420.00**

Health Safety Net Trust Fund- Uses			
	FY10	FY11	FY12
Hospital Costs	$ 372.0	$449-$474	$449-$499
CHCs	$ 42.0	$ 64.7	$ 65.0
Demos (Admin)	$ 6.0	$ 6.0	$ 6.0
Total Uses	**$ 420.0**	**$520-$545**	**$520-$570**

To help reduce the burden on hospitals in Health Safety Net fiscal year 2011 (October 2010- September 2011) for providing care to the uninsured and underinsured, the budget provided $30 million in a General Fund contribution to offset 2011 costs.

Despite the unprecedented fiscal challenges of fiscal year 2012, the Administration is maintaining a $30 million General Fund contribution to the Health Safety Net in its fiscal year 2012 budget proposal. We will continue to closely monitor the Health Safety Net and refine projections for fiscal year 2011 and 2012 demand based upon updated information

Section III: Other Cost Containment Initiatives

Municipal Health Care

Municipal employee health costs are having a serious impact on local government finances and the provision of core municipal services such as education and public safety. Current municipal health insurance cost trends are not sustainable. The Administration is proposing a new local health insurance plan design process that will achieve material savings for cities and towns. This could save more than $94 million. In addition, all municipalities will be required to have their eligible retired local employees enrolled in Medicare as their primary source of health insurance coverage, as this federal program covers a substantial portion of their health costs. This is required of all eligible state employees and could save the 60% of municipalities not currently enrolled in Medicare $15 million to $30 million.

Small Business Health Care Cost Containment

The Health Connector will be launching updates in July to its Commonwealth Choice program, which creates a streamlined, simplified process for small businesses and individuals to shop for unsubsidized, name-brand health insurance, saving them money by making it easier for them to understand their options and choose better-priced health plans.

- The Health Connector will eliminate a fee it currently charges small businesses to shop through Commonwealth Choice. This fee was already significantly lower than those charged when small businesses shopped through other intermediaries, and now it will be eliminated starting in July.
- The Administration's fiscal year 2012 budget includes $10 million (including $2.5 million contribution from the Health Connector) to enable the Health Connector to implement a provision of Chapter 288 calling on it to offer premium discounts for certain small businesses which purchase coverage through Commonwealth Choice and set up wellness programs for their employees. This will reduce premiums for qualifying small businesses by up to 5%.
- The Health Connector will be enhancing the Commonwealth Choice shopping experience by enabling small businesses and individuals to search whether a desired hospital or doctor is covered through the health plans they are considering.

Money Follows the Person Demonstration Project

In January 2011, Massachusetts applied to join Washington D.C. and the 29 other states already participating in "Money Follows the Person Rebalancing Demonstration" (MFP). With federal support, states will have additional programmatic and financial tools to rebalance their long-term care systems through the following:

- increasing the use of home and community-based services (HCBS);
- decreasing the use of institutional care;
- eliminating barriers that restrict flexible use of Medicaid funds; and
- ensuring quality assurance and quality improvement

The approval of the project will strengthen the Administration's Community First initiative to transition long term care residents to the community from facility settings and improve MassHealth's quality infrastructure, data resources and reporting capabilities. MassHealth also plans to create two new Home and Community-Based Waivers for MFP Demonstration participants who will need more intensive supports on an ongoing basis once they transition from facilities.

Patient-Centered Medical Home Initiative (PCMHI)

The Administration has committed to assist 46 primary care practices, including community health centers, hospital-affiliated primary care offices, and group and solo practices, to transition into certified medical homes focused on integrated and patient-centered care. PCMHI establishes a foundation for transforming the primary care landscape in Massachusetts through these pilot sites. It targets the elimination of fragmented and uncoordinated care delivery and improvements in chronic disease management. Patient-centered practices recognize the patient as an individual, respect the patient's values, language and culture, and promote the exchange of information about care options between patients and providers.

Selected primary care practices will work toward mastering core competencies in patient-centered care over the course of three years and will receive training support, technical assistance and funding from the state. To help practices achieve core competencies and transform their operations, each participating practice will receive on-site, individualized coaching from a medical home facilitator and membership in a learning collaborative that includes in-person conferences, online trainings and evidence-based performance evaluation.

The Executive Office of Health and Human Services will oversee and evaluate the success and challenges of the pilot sites to further refine and spread the medical home model to additional practices in the future.

Electronic Health Record (EHR) Initiative

The American Recovery and Reinvestment Act of 2009 (Recovery Act) amended the Medicaid statute to provide for a 100% Federal financial participation (FFP) match for state expenditures for provider incentive payments to encourage Medicaid health care providers to adopt, implement, upgrade or meaningfully use certified EHR technology. It also established a 90% FFP match for reasonable state expenses related to administration of the incentive payments and to promote EHR adoption and health information exchange.

Adoption and meaningful use of interoperable EHRs can improve patient care in a number of ways including making the health care system more efficient by simplifying administrative procedures for doctors and patients; improving health care quality by making patient health information, available at all points of care; improving health outcomes and reducing costs through earlier diagnosis and characterization of disease; reducing adverse events through an improved knowledge of each patient's medical history, potential for drug-drug interactions; and increasing efficiencies related to administrative tasks, allowing for more interaction with and secure transfer of information to patients, caregivers and clinical care coordinators.

The Administration is committing $500,000 as the state share to operate the implementation of the MassHealth Electronic Health Record (EHR) initiative, which will offer provider incentive payments with 100% federal participation funding to encourage Medicaid health care providers to adopt, implement, upgrade or meaningfully use certified EHR technology. MassHealth plans to distribute up to $50 million to approved health care entities to support transitions to electronic health record systems in fiscal year 2012.

Full Time Equivalent (FTE) Assumptions

Chapter 29, Section 6 states that "The operating budget shall indicate the number of positions proposed to be authorized for each state agency or such other public instrumentality for the ensuing fiscal year, the number of positions for each state agency in the current and ensuing fiscal years and such other information as may be held to explain the anticipated results of the proposed expenditures".

To address this requirement, the House 1 recommendation includes employee counts summarized at the Government area level. Additional detail is included throughout the Budget Recommendations to indicate the employee level within specific departments.

Effect of the Budget on Personnel to Date

Reduction in Workforce

Since the fall of 2008 the Administration has provided strict FTE caps to the Executive Branch Departments, prioritizing hiring in areas where positions are critical for public health and safety or where a position results in additional revenue or cost savings for the Commonwealth. FTE caps are implemented at the department level and reviewed regularly by ANF budget analysts to ensure agencies are taking the necessary steps to live within capped levels.

FTE caps are meant to be consistent with amounts allocated for FTE spending. If an agency does not project that enough funding is available to maintain an FTE level, a "reduction in force" plan must be submitted to the Human Resources Division within ANF. These plans are reviewed for their impact on public health and safety or other impact on service levels provided to the Commonwealth's residents. Agencies are asked to ensure that everything that possible is done to avoid a meaningful impact on users of state services as a result of layoffs.

Between the fall of 2008 and December 2010, the state workforce for jobs in the Executive Branch funded with operating dollars has declined by 3,350 jobs. The reduction can be attributed to layoffs, attrition and retirement across all agencies in the Executive Branch. Furthermore, after accounting for an increase of 2,700 positions in January 2010 corresponding to transition of seven county sheriffs' offices to state agencies, Non-Executive Branch (Judiciary, Legislature, Sheriffs, Higher Education) agencies have seen a decline of roughly 2,500 positions.

EXECUTIVE BUDGETARY JOBS			
BENCHMARK*	01/20/07	*Jobs:*	37,473
BENCHMARK*	10/11/08	*Jobs:*	38,285
PREVIOUS PAY PERIOD	12/18/10	*Jobs:*	34,952
CURRENT PAY PERIOD	01/01/11	*Jobs:*	34,935
VARIANCES VS. CURRENT			
YTD VARIANCE FROM*	01/20/07	*Jobs:*	(2,538)
YTD VARIANCE FROM*	10/11/08	*Jobs:*	(3,350)
PREVIOUS VS. CURRENT		*Jobs:*	(17)
BENCHMARK VS. CURRENT*	10/11/08		38,285
**1269 jobs adjusted for MassDOT reform as of 11/01/2009*	01/01/11		34,935
		Job Variance	**(3,350)**

H.1 Employment Levels

In reviewing the funding levels available to them for 2012, agencies must critically evaluate their employee level and determine further reductions are necessary to maintain a balanced budget. The fiscal year 2012 H.1 recommendation estimates 66,242 FTEs. This amount includes FTEs from both Executive and Non-Executive departments as well as positions funded from the operating accounts listed within the budget.

State Budgeted FTEs, Executive and Non-Executive by Fiscal Year

	FY2011	FY2012	Variance
Executive Branch			
Administration and Finance	2,740	2,752	12
Education	521	519	(2)
Energy & Environmental Affairs	1,991	1,821	(170)
Health and Human Services	19,644	19,477	(167)
Housing & Economic Development	728	731	3
Labor & Workforce Development	311	311	-
Public Safety	8,433	9,669	1,236
Transportation	-	-	-
Executive Total	***34,368***	***35,280***	***912***
*Executive Adjusted Total**	*34,368*	*34,045*	*912*
Non-Executive			
Independents	3,671	3,586	(85)
Sheriffs	5,933	5,627	(306)
Higher Education Campuses	13,683	13,683	-
Judiciary**	7,058	7,133	75
Legislature	960	933	(27)
Non-Executive Total	***31,305***	***30,962***	***(343)***
*Non-Executive Adjusted Total**	*31,305*	*30,660*	(645)
GRAND TOTAL	65,673.0	66,242.0	569.0
Adjusted Grand Total	*65,673.0*	*64,705.0*	*(968.0)*

**H.1 proposes to re-organize the Department of Community Supervision (formerly Commissioner or Probabtion and Community Corrections) from the Judiciary to the Executive Office of Public Safety.*
***H.1 proposes to increase the fiscal year 2012 FTEs by as many as 1,537 new staff attorneys and other support positions at the newly created Department of Public Counsel Services. For comparison purposes these FTEs are eliminated from the FY2012 Non-Executive Adjusted Total*

The fiscal year 2012 projected budgeted FTEs reflects the Governor's proposal to transform the cost-ineffective manner in which the state currently provided constitutionally-required legal services to indigent criminal defendants. The Governor proposes to shift from a system that relies almost entirely on expensive private attorneys that bill for hourly services to a system that is staffed entirely by salaried state employees. The new system will require adding up to an additional 1,537 attorneys, investigators and state support positions (as reflected in the budgetary FTE amount of 66,242) but will generate approximately $46 million in savings from fiscal year 2011. Total budgeted FTEs are projected to increase by 569 positions in fiscal year 2012, but absent of this change they would be reduced by roughly 970 positions to 64,705 FTEs. This compares to current budgeted FTE levels of up to 65,673 in fiscal year 2011.

Workforce Planning Goals

As discussed earlier, the Executive Office for Administration and Finance (ANF) and the Human Resources Division have worked together to implement clear policies surrounding employees. Each fall, ANF engages each agency in a spending plan process in which each account is evaluated to determine how funds will be spent for the current fiscal year. This requires a detailed description of employees for the current year - including those currently on staff, positions that are open and intended to be filled and new positions for which funding is available. The goals of the employee caps that have been in place since fiscal year 2009, at the start of the fiscal crisis, and the subsequent review of all employee spending are to:

- Restrain Growth in State Employee Levels - Since payroll is a large portion of many agency expenditures, and reductions in force can take so long that savings cannot be realized in a fiscal year, caps are needed to manage hiring within available funding levels. Although some hiring may have small costs for the current year, the full year value of new staff have budget impacts that must be considered.
- Mitigate Shifts to Other Funding Sources – Employees come onto the state payroll several ways including the operating budget (FTEs and contractors), the capital budget, federal grants and trusts. All sources are carefully reviewed to ensure we are maintaining compliance with employment laws and also to ensure that we are not using one time sources to pay for ongoing costs.
- Manage Overtime Costs – Although hiring restrictions are important, overtime costs must be considered to ensure that proper staffing levels are maintained for public health and safety where responsibilities are 24 hours / 7 days per week. Oftentimes, the savings of FTE restrictions are simply shifted to higher overtime. Therefore, prudent management of both overtime and staffing levels must be evaluated.

During fiscal year 2011 FTE caps have continued to be in place in order to continue to manage the state workforce. For the Executive Branch, head count will be managed for all funding sources but specifically for the operating budget funds recommended in the H.1 recommendation.

Key initiatives Impacting the State Workforce

MassDOT Reform

In June 2009, Governor Patrick signed Chapter 25 of the Acts of 2009 creating the new, streamlined Massachusetts Department of Transportation (MassDOT). MassDOT represents a merger of the former Executive Office of Transportation and Public Works (EOT) with the Massachusetts Turnpike Authority (MTA), the Massachusetts Highway Department (MHD), the Registry of Motor Vehicles (RMV), the Massachusetts Aeronautics Commission (MAC) and the Tobin Bridge. The new organization also assumed responsibility for many of the bridges and parkways formerly operated by the Department of Conservation and Recreation (DCR). Implementing the reform act has lead to changes in the classification of transportation FTEs, namely the transition of the 1,200 former EOT and DCR budgetary FTEs to an off budget trust fund.

Sheriffs

A year ago, Governor Patrick proposed the alignment of all 14 Massachusetts State and County Sheriffs under the state budgeting and finance laws. The Legislature approved the Governor's proposal through passage of the sheriff transfer legislation, Chapter 102 of the Acts of 2009, which was approved by the Governor on August 6, 2009. This act transferred the remaining 7 county sheriff departments to the Commonwealth effective January 1,

2010. Since then, sheriff departments have successfully transitioned onto the state budgeting and accounting system and all sheriff employees have been placed on state payroll, increasing the state FTE count by approximately 2,750 employees. However, this does not represent a parallel increase in state spending as sheriff operations prior to the transfer were predominantly funded by the Commonwealth. Additionally, deeds excise revenue previously funding sheriff operations will now be remitted to the Commonwealth.

Information Technology Realignments

Because of an initiative to transfer all information technology employees to secretariats, those employees that have routinely been funded from off-budget sources are being transferred into Intragovernmental Service Fund accounts where they will report to staff at the secretariat-level, but continue to be paid from the off-budget sources. This represents an “increase” of nearly 300 FTEs on the overall totals.

Contractor / Capital Conversions

Given the cost associated with paying for employees from capital funds and the renewed focus on wage enforcement efforts, every effort continues to be made to convert contract employees to full-time equivalents, and to transfer employees onto the operating budget. Along with conversions that have already been made, H.1 includes an outside section that allows for certain capital and operating costs to be exchanged so that appropriate operating dollars spent on capital needs can be shifted to the capital budget and vice versa. This section will have an impact on our budgeted employee level but it should be noted that these are not new state employees, they are just new to the operating budget.

Other Considerations

Like all departments, the non-executive branch agencies will be working to evaluate impacts on employees. Additionally, because funding at the Higher Education campuses comes from various sources, some employee impacts may be mitigated. Additionally, certain FTE increases due to compliance with legal settlements and to address needs around public health and safety must be considered.