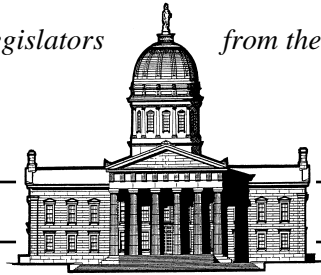


The Fiscal Focus

An update for Vermont Legislators

from the Joint Fiscal Office



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Revenue Update

Forecast Revisions

The Emergency Board met last month to reevaluate the revenue forecast for the three major state funds in FY 2010 and FY 2011. The changes made in November were modest corrections, indicating a stabilization of the state's revenue sources for the first time in over 18 months.

Fund	FY 2010 (\$ millions)		FY 2011 (\$ millions)	
	Change	New Forecast	Change	New Forecast
GF	1.6	1,026.2	(2.3)	1,081.8
TF	(0.5)	212.3	(1.0)	217.8
EF	(0.8)	146.4	(1.2)	151.7

Other than the \$1.6 million FY 2010 general fund increase, all of the other revisions to the general, transportation, and education funds were reductions. The next revenue update will be in January at the start of the legislative session.

FY 2010 Revenue Update

Since the forecast was modified in November, there is only one month of revenue collections to compare with the revised monthly targets. ❖

Fund	FY 2010 Collections through November (\$ millions)		
	Target	Actual	Difference
GF	420.5	421.0	0.5
TF	87.2	86.3	(0.9)
EF	60.5	60.5	0

FY 2011 Budget Gap

Both the JFO and the Administration have determined the estimated FY 2011 budget gap is approximately \$150 million.

The manner in which JFO reached this determination is based on a "steady state" estimated growth rate of 3.5% on the FY 2010 general fund base, including available ARRA funds. This indicates a gap of \$90 million. However, there are several additional items that are above this rate: the largest of these are retirement funding needs, caseload in Medicaid and other programs, including corrections, as well as one-time pressures, including a 27th pay period that occurs every 10-12 years. This total is compared to the current estimate for available general fund revenue. The JFO estimated gap is

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Joint Fiscal Committee Actions

October 28, 2009 – Special Meeting

- Convened a joint meeting with the Mental Health Oversight Committee and authorized continued work on financial arrangements to add a new 28-bed psychiatric wing to the RRMC “Vermont Futures Project.” The Committees requested standing committees receive an update on the plan on or before January 15, 2010.
- Convened a meeting with the Chairs of the House and Senate Committees on Natural Resources and Energy to receive an update on the Memorandum of Understanding (MOU) to transfer ownership of Vermont Yankee Nuclear Power Plant from Entergy Nuclear to Enexus Corporation. Hearings on the issue by standing committees were scheduled for December.
- Received a second update from the administration on FY 2010 Budget Adjustment Pressures (*see article on page six*).

November 12, 2009

- Received an update on FY 2010 budget pressures.
- Reviewed education fund balance sheet: FY 2011 education tax rates will probably increase (*see article on page five*). In FY 2012, ARRA funds will not be available, and this loss of revenue will put additional pressure on the education fund.
- Received the FY 2010 Pay Act Allocations Report. This report on changes in state positions since 2008 is available on the JFO website (FY 2010 Personnel Savings Target Final Report).
- Received a preliminary report on the administration’s Tiger Team savings effort.
- Received an update on the Chittenden County Pilot Project for a substance abuse facility. The Committee encouraged the administration to move forward with the project.
- Received a report from the Choices for Care Subcommittee which met with the administration and providers. They discussed how to define and analyze savings and the potential for changes in operations that could reduce costs. The JFC agreed that this area will require continued discussion during the legislative session.

- Received a report from the tax department on electronic systems for filing and paying property transfer taxes. The implementation date of the project is scheduled for January 2011.
- Received a report from the Current Use Subcommittee on 5 possible proposals to reduce costs.
- Received a revenue update from Tom Kavet (*see article on page one*)
- Held a discussion on the VEGI program – The Committee asked that the Senate Economic Development and the House Commerce Committees review the program parameters using the June 2008 auditor findings as a starting point. ❖

Tax Commission Update

The Blue Ribbon Tax Structure Commission has hired a Staff Director who will begin in January 2010. Michael Costa will be relocating from California where he has been a Chief of Staff at the San Mateo County Board of Supervisors since 2007. His prior experience was in the Massachusetts Legislature. Michael has his B.A. from Bates College and his J.D. from the University of Wisconsin.

Information on the Tax Commission is available at <http://www.leg.state.vt.us/jfo/Tax%20Commission.htm>. ❖

Dear Vermont Legislator,
*This is the third 2009 issue of **THE FISCAL FOCUS**. This is a nonpartisan update prepared by the Joint Fiscal Office staff to keep legislators informed of events during the off-season. As your staff, we believe it is important for a citizen legislature to be kept abreast of local, state, and federal financial developments while the General Assembly is adjourned. This update is sent to all House and Senate members.*

It is important for us to understand what topics interest you so we can incorporate them into future issues. If you have any comments or suggestions, please let us know.

Joint Fiscal Office staff

FY 2011 Retirement Obligations

The state's retirement obligations pose significant budgetary pressure in FY 2011. The Vermont State Teachers Retirement System (VSTRS) funding need is \$63.5 million which is \$22 million over the FY 2010 amount. The Vermont State Employees Retirement System (VSERS) funding need is \$41.6 million which is \$9.4 million over the FY 2010 amount.

The funding need is determined by the annual actuarially required contribution (ARC). For FY 2011, this valuation is based on the year ending June 30, 2009. The ARC has two components – a normal cost, and an amount to amortize the unfunded actuarial accrued liability (UAAL). The normal cost generally means the cost for pension benefits being earned by employees in exchange for services now and is net of employee contributions. The UAAL is the excess of the actuarial accrued liability over the actuarial value of assets. The 30-year amortization period for the UAAL of both systems was reset effective 7/1/08. For FY 2011, in VSTRS, the normal cost is calculated at \$22.8 million with the UAAL at \$40.7 million. In VSERS, the normal cost is \$23.4 million with the UAAL at \$18.2 million.

The main reason for the significant increase in funding need is due to significant growth in the unfunded liability in each system. An unfunded liability can occur based on three variables: underfunding of the ARC in previous years; actuarial gains and losses (differences between actuarial assumptions and actual experience); and changes to the benefit structure. While investment return (i.e., loss) is the predominant factor in the year ending June 30, 2009, other factors include past underfunding in VSTRS and changes to mortality assumptions and other demographic factors for both systems. After accounting for contributions, normal cost, and any changes to system provisions or assumptions, VSERS had an unfunded liability of \$326.5 million on June 30, 2009, and a funded ratio of 78.9%, while VSTRS had an unfunded liability of \$727.8 million and a funded

ratio of 65.4%.

Even assuming full funding of the retirement systems' ARC in FY 2011, continued budgetary pressure in this area is expected. The actuarial method involves the smoothing of assets; the downward trend experienced in investments will not go away in a year or two. This is because the additional portions of investment losses that have not yet been recognized in the actuarial valuations will need to be recognized in subsequent years. Even returns that are far above the anticipated level will not offset this impact. Additional cost pressures in this area are from other postemployment benefits (OPEB) such as health care which is funded on a pay-as-you-go basis. ❖

VT's Unemployment Insurance (UI) System

Last session, the legislature raised unemployment taxes and reduced unemployment benefits for 2010. Vermont's UI Trust Fund also received additional funding from the American Recovery and Reinvestment Act of 2009. Nevertheless, reserves are running low, and the UI Trust Fund balance is expected to become negative in early 2010.

To address this problem, the legislature created a bipartisan study committee last session to undertake a comprehensive study of all issues that affect the solvency of the Vermont UI Trust Fund and develop recommendations for reform to reestablish and assure its long-term solvency.

Member of the study committee met eight times and took testimony from a variety of individuals and organizations representing a broad spectrum of perspectives and interests. The committee has now completed its work and will issue its final written report on or before January 15th 2010. ❖

Reductions in Employee Count

There has been a significant reduction in the number of state employees beginning in the spring of 2008 with the planned reduction of up to 400 positions through attrition. This was followed by the personnel savings targets specified in the FY 2010 budget and subsequent rescission target which relied on the retirement incentive and reductions in force (RIFs). At the same time, additional reductions have been included in line items of the budget.

The JFO has made a comparison of position control reports between April 2008 and November 2009 to understand the change in the actual employee count over this period. The position control reports are a snapshot of all vacant and filled positions by department and title as of a specific date, and this comparison reflects the aggregate of all employment changes between the two dates. The comparison below shows the changes in executive branch-filled positions and then the change in executive branch-classified positions only.

	<u>Apr. 2008</u>	<u>Nov. 2009</u>	<u>Change</u>	<u>% Change</u>
Entire Executive - employees	8,397	7,777	-620	-7.4%
Classified Executive - employees	7,924	7,328	-596	-7.5%

More detailed information by department and title is available through JFO. The number of vacant positions in this time period has been reduced by 11%. There are currently about 400 vacant positions compared to 450 vacant positions in April 2008. The administration provided a similar analysis to JFO by department and by type of separation. Their analysis was between July 2008 and October 2009 and showed a total reduction of 566 classified executive employees.

In this 15-18 month timeframe, 137 of the reductions are due to RIFs, and 243 employees took advantage of the retirement incentive program. The remaining reductions are a result of other attrition which includes voluntary separation from employment or regular retirements and the decision subsequently to eliminate positions. There is, of course, a lot more turnover in the state workforce in the same period. The administration report shows over 1,800 separations, most of which were voluntary. This means that roughly 1,200 of the positions were refilled.

The JFO has also looked at the actions of other northeast states in this regard. Because of the timing of when (and if) positions are reduced in other states, this analysis is likely to change over time. NY has reduced the executive branch ranks by over 3% as of November 2009 and is currently at 2006 levels. MA is at 2005 levels. ME is below 2005 levels, and NH appears to be at 2007 levels. CT is well below 2007 levels (we do not have pre-2007 data for CT). RI is well below its 2005 level of employees. Vermont's executive branch employee count is now comparable to the count we had in 2002. NY and VT appear to have grown the most rapidly prior to 2008 which is the peak for most states. ME, NH, and MA had more modest growth in state employees prior to 2008. ❖

Entergy Nuclear Vermont Yankee

Over the fall, various legislative committees have been holding meetings on issues surrounding Entergy Nuclear Vermont Yankee (ENVY). The topics covered include: the Memorandum of Understanding between the Public Service Department and ENVY regarding the proposed corporate changes; a discussion of the New England power markets; status report of ENVY reliability oversight; a geologists review of the storage site at ENVY; and various other reports. The reports that have been handed out are on our website at <http://www.leg.state.vt.us/jfo/Vermont%20Yankee.htm> ❖

Federal Health Care Reform

Federal Health Care Reform: HR 3590, the Patient Protection and Affordable Care Act, is still being debated on the Senate floor. While the final product is not yet certain, the JFO has done a very preliminary analysis of some of the potential fiscal implications to the state coffers as a result of the Senate Bill.

Some of the potential positive impacts are from an enhanced match rate for SCHIP, a reduction in the size of the Medicare Part D donut hole which will help the VPHARM program, an increase in prevention and wellness grants, and potential Medicare participation in the Blueprint for Health. Some of the potential negative fiscal impacts will result from an expected increase in state spending with no additional federal matching dollars due to an anticipated spike in Medicaid caseloads, the potential loss of supplemental pharmacy rebates currently collected, the potential loss of disproportionate share (DSH) money for hospitals, and the unfunded administrative and system costs associated with implementing the federal reforms.

The House Bill passed in late October. If or when the Senate passes a bill, the two bills will go to conference committee. VT legislative leadership, JFO, and the Legislative Council have all been in constant contact with congressional delegation staff and will continue to monitor the situation. ❖

FY 2010 Education Tax Rates

The consensus education fund outlook indicates that education tax rates will increase next year for the first time since the implementation of Act 68 in FY 2005. The base homestead tax rate will increase from \$0.86 to \$0.882, and the nonresidential tax rate will increase from \$1.35 to \$1.372 per \$100 of fair market value. The base rate on household income will remain at 1.8%.

Several factors related to the current economic downturn have contributed to this education tax rate increase. These factors include: (1) slower growth in property values; (2) faster growth in property tax adjustments; and (3) slower growth in non property tax revenues, including an \$18.4 million reduction in general fund support for education spending. The consensus outlook assumes that education spending

FY2011 Budget Gap

(Continued from page 1)

\$141-\$161 million for FY 2011. The Department of Finance has a similar estimate. The manner in which the administration determined the budget gap looks at the specific increases above the current FY 2010 budget level, line item by line item. This analysis also includes offsets from areas where there are downward pressures, such as the recent agreement between the administration and the state employees, and assumes there will be ARRA one-time funds available for offsetting some of the one-time costs in the budget.

The magnitude of this gap, particularly after having closed considerable gaps in FY 2009 and FY 2010, is very challenging. Of note, in FY 2012 we anticipate an additional gap. The Public Strategies Group (PSG) is working on a set of ideas to address a portion of the shortfall through redesign opportunities. The administration's "Tiger Teams" are looking for savings. However, additional ideas, very tough choices, and creative approaches will be needed. ❖

statewide will grow by only 2% next year.

With this two-cent increase in the education tax rates, the education fund stabilization reserve is projected to be full. However, transferring additional costs, such as teachers' pensions, to the education fund or further reducing non property tax revenues to the education fund will either diminish the size of the reserve or require even higher property tax rates next year.

Education spending in FY 2011 is supported in part by \$38.6 million in ARRA stabilization funds that will not be available in FY2012. In addition, property values are not expected to rebound anytime soon. Consequently, pressure on education tax rates is expected to continue for several years. ❖

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FY2010 Budget Adjustment Pressures

At the October 28th meeting of the Joint Fiscal Committee, the Commissioner of Finance and Management identified some areas of the FY 2010 budget that will need additional funding. These current year budget pressures amount to approximately \$7.5 million and are predominately within the Agency of Human Services. The Administration will be including recommendations to address these shortfalls in the FY 2010 budget adjustment bill, along with spending reductions to offset these increases.

Areas experiencing shortfalls include the Aid to Aged, Blind and Disabled program, costs associated with a delay in federal participation in the state-only pharmacy and Catamount programs, increased caseload in the general assistance and Reach Up programs, increased usage of out-of-state beds in corrections, and a need for state funds in VEDA to allow the draw of federal ARRA funds. In addition, there are three special funds that are experiencing shortfalls that will need to be addressed. There may be additional areas of need that have not yet been identified . ❖



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