



# VT Revenue and Budget Picture: Facing Vermont's Fiscal Challenges

*November 17, 2009 Update*

*Prepared by the Vermont Legislative Joint Fiscal Office*

# Vermont's fiscal challenges: overview

- National Context – Federal and Other State Deficits
- Vermont General Fund Revenues
- Revenue/Budget Actions through FY 2010
- FY 2011 and FY 2012 – General Fund Deficit and Uncertainties
- Budget Steps Underway
- Other Funds
- Vermont Budget Implications

# The Federal context:

- The FFY 2009 deficit was equal to 9.9 percent of gross domestic product (GDP), up from 3.2 percent in 2008.
- This was the highest shortfall—relative to the size of the economy—since 1945.
- The substantial increase in the deficit resulted from both declining revenues and increased spending.
- The CBO estimates that the federal deficit was about \$1.4 trillion in 2009, up from \$459 billion in 2008.

Source: Congressional Budget Office (CBO): November 2009

# Federal context: CBO November 2009

- CBO November 2009 estimates are that total receipts in 2009 were \$419 billion less than receipts in 2008 – a 17% decline, marking the second consecutive year of declines in federal receipts. (Receipts dropped for three consecutive years from 2000 to 2003, declining by a total of 12 percent.)
- CBO estimates are that revenues fell from 17.7 percent of GDP in 2008 to 14.9 percent of GDP in 2009.
- Individual income taxes, the largest source of tax receipts, account for more than half of the total drop in receipts, declining by \$230 billion (or 20 percent).
- *For comparison purposes, from SFY 2008 to SFY 2009 Vermont state income tax receipts fell about 15%.*

# Federal implications for states?

- Does Washington?
  - Provide additional state relief? If so how much? And for how long?
  - Save resources for health care and energy reform
  - Increase the states' financial obligations through subsequent federal legislation

A combination of the three? All are on the table.

State governments have been hit hard by the recession. Revenues have fallen due to a dramatic decline in economic activity (Slide 1)

- Among other states, the most extreme revenue loss is the State of Michigan where FY 2010 projected state revenues have fallen to FY 1988 levels.
- In the State of Florida, reportedly revenues are at FY 2001 levels.
- Vermont's FY 2010 total revenues are below those of FY 2005.

## State governments have been hit hard by the recession. (Slide 2)

- This Fall, Vermont's neighboring states have identified FY 2010 budget gaps estimated at:
  - New York \$3 billion or 5% budget
  - Connecticut \$500 million or 2.9% of budget
  - Massachusetts \$600 million or 2.1% of budget
  - New Hampshire \$32 million or 1.9% of budget
- California has an FY 2010 deficit of \$7 billion and an FY 2011 deficit on percentage basis 2 to 4 times Vermont's projected FY 2011 deficit.

# The Vermont experience is Similar....

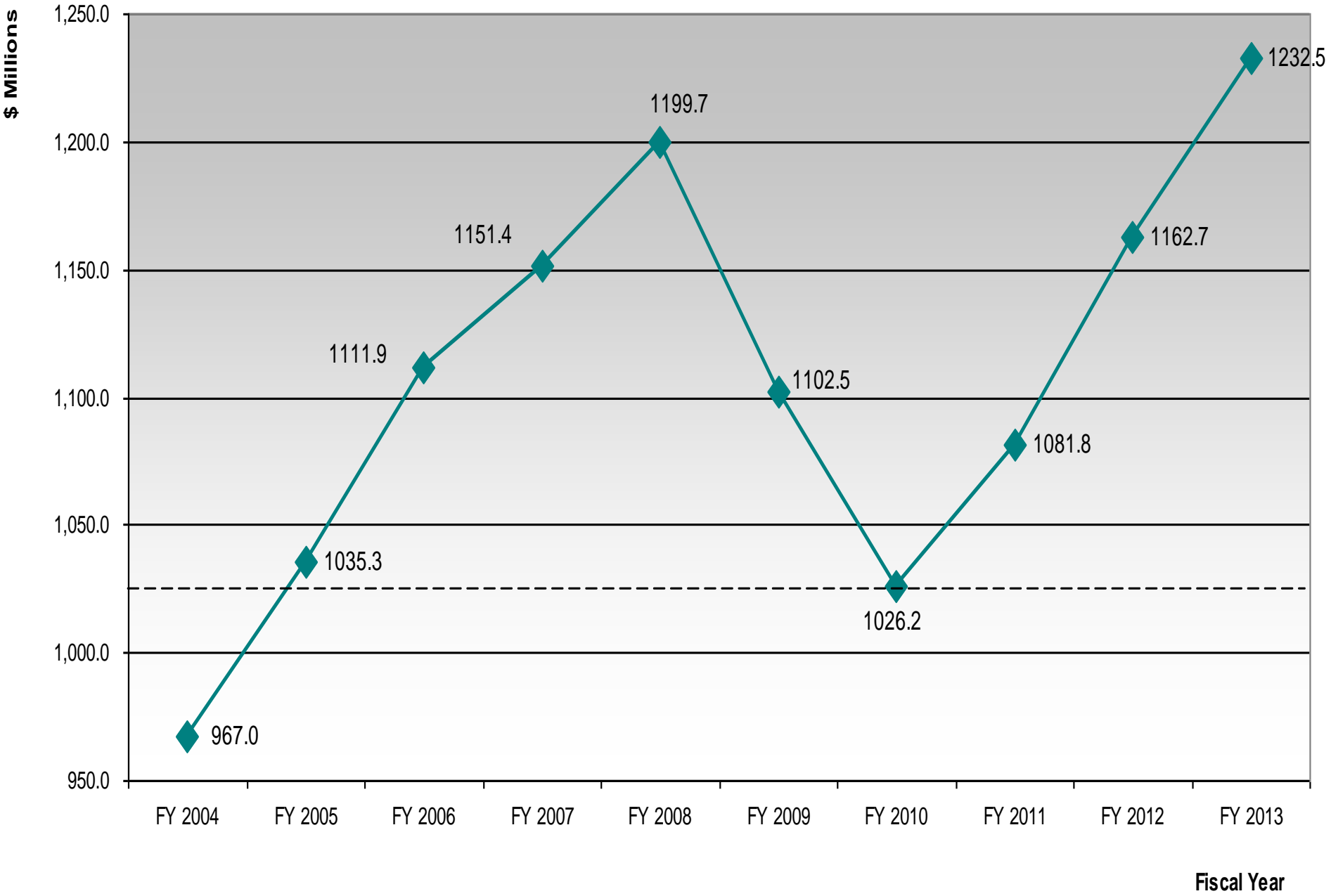
# Less income = less income tax and sales tax revenue and less revenue generally

- In July 2007, FY 2010 income tax revenues were projected at \$650 million. As of November 2009, Vermont economists revised the projection downward to \$489 million, with risk on the downside - a 25% decline.
- In July 2007, FY 2010 total sales tax revenues were projected at \$373 million. As of November 2009, Vermont revised the projection downward to \$310.4 million, with risk on the downside - a 17% decline.
- Overall, since July 2007, total projected available General Fund revenue for FY 2010 decreased from \$1,249 million to \$1,026 million, an 18% decline.
- This was despite a \$20 million increase in tax revenues for FY 2010

# Vermont General Fund revenue growth rates 17 year average: 3.5%, FY 2011-14: 5.8%

Fiscal Yr	Prct grwth	Fiscal Yr	Prct grwth
1998	7.6%		
1999	6.9%	2007	3.5%
2000	6.8%	2008	4.2%
2001	1.5%	2009	-8.1%
2002	-6.5%	2010	-6.9%
2003	3.0%	2011	5.4%
2004	9.9%	2012	7.5%
2005	7.1%	2013	6.0%
2006	7.4%	2014	4.4%

### VT Available General Fund Revenue



# While revenues have been declining, expenses continue to rise

- Corrections has had a 10-year annual average growth rate of 8%,
- State Hospital costs grew at a 10-year average rate of 12%.
- Medicaid, teachers retirement and unemployment insurance are also growing at a pace that far out strips even normal revenue growth.
- In the past, increased federal resources, such as our Medicaid waiver, coupled with the rapid revenue growth experienced prior to 2008, allowed Vermont to avoid deficits.
- A second stimulus package or an extraordinary revenue growth would help, but it is difficult to build a budget unknowns.

# A number of actions have been taken to balance FY 2009 and FY 2010 (Slide 1)

- In FY 2009 and FY 2010, state General Fund appropriations declined by 4.5% and 6.6% respectively.
- Federal stimulus funds were used to make up much of this decline in General Fund appropriations.
- Even with Federal stimulus funding, after the August 2009 rescissions, total General Fund and ARRA expenditures grew at roughly 1% in FY 2010 - far below the trend cost pressures faced by Vermont.

# A number of actions have been taken to balance FY 2009 and FY 2010 (Slide 2)

- The number of active executive branch state employees today has been reduced from a high in April 2008 of 8,397 to an estimated 7,786 as of September 2009.
- Another 25 position reductions are included in the administration's plan to meet the \$7.4 million savings target from the August 2009 rescission plan.
- The number of state employees in Vermont is roughly at 2002 levels, with more reductions possible.
- The reductions have been to both classified and exempt positions.

# A number of actions have been taken to balance FY 2009 and FY 2010 (Slide 3)

- Exempt (non bargaining unit) employees earning over \$60,000 has experienced a 5% pay reduction or equivalent furloughs and no pay increase for the past two years. All exempts, regardless of salary level, had no raise this past July.
- Last session key tax changes included:
  - Reducing the capital gains exemption to \$2,500 for two years then a flat \$5,000 (with some exceptions);
  - A \$5,000 cap on the state and local tax deduction; and
  - Lowered income tax rates, cigarette tax increases, an estate tax exemption set at \$2 million, and a tax amnesty program.

# A number of actions have been taken to balance FY 2009 and FY 2010 (Slide 4)

The Legislature and the Administration have:

- Closed four interstate rest areas;
- Increased individual co-pays for the state's pharmacy programs;
- Reduced health care provider reimbursement, from already insufficient levels, by 2%;
- Closed courts; and
- Cut smoking cessation programs as well as numerous other reductions across state government; and
- Made other cuts through budget and rescission actions,

# Estimated FY 2010 budget adjustment adds pressures to out years

## – One Time \$1.75 M - \$3 M:

- Emergency Relief Assistant Fund      \$ 40,000
- Sarcoidosis Benefit Trust Fund      \$ 150,000
- Petroleum Clean Fund Shortfalls      \$ 750,000
- Delay in Federal match since Oct. (monthly)
  - Cat Waiver Exp. Nov/Dec      \$ 457,000
  - Rx Waiver Exp. Feb/Mar      \$ 350,000

## – Ongoing \$3.8 M:

- AABD COLA      \$ 600,000
- General Assistance Shortfall      \$ 600,000
- Corrections Out-of-state Beds      \$2,600,000

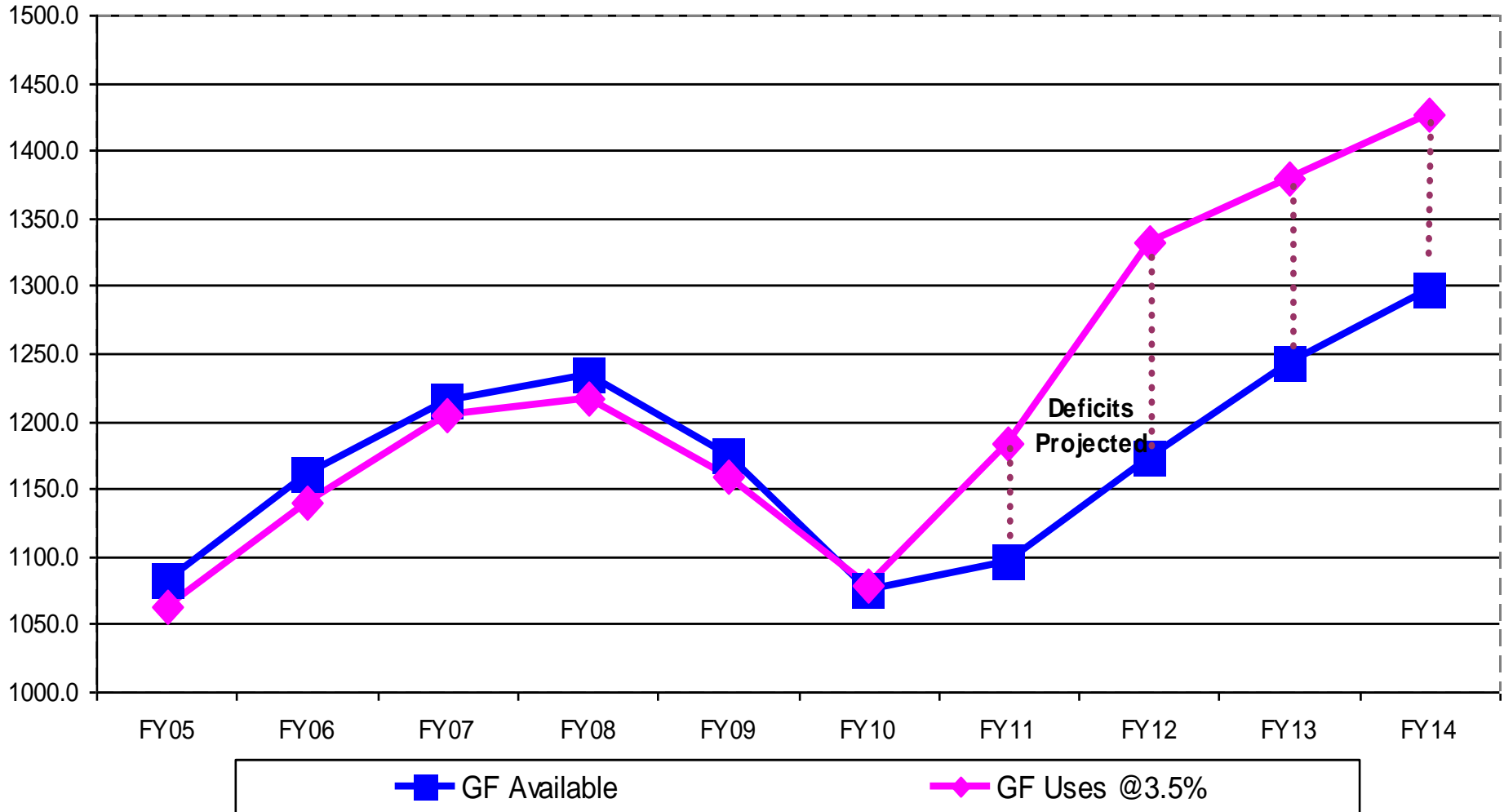
# The next fiscal years will see additional reductions (Slide 1)

- With the federal fiscal stimulus funds spent and budget reductions already made, the revised revenue forecast and budget adjustment pressures, Vermont's state budget is nearly in balance for this fiscal year, 2010. **(-3.4 M) or -.3%**
- Vermont is facing deficits into the future, as stimulus funds are used up.
- The current deficit projection for Vermont is:
  - FY 2011 **(\$ 88 million) = 7% shortfall**
  - FY 2012 **(\$160 million) = 12% shortfall**
  - FY 2013 **(\$136 million) = 10% shortfall**
- Base reductions in one year will reduce future year's deficits
- Budget pressures significantly above the 3.5% growth assumption will increase these deficit projections.
- This models assumes \$38.6 m of ARRA funds for education are replaced with GF. Restoration of the base \$18.4m GF reduction to the Education Fund is not.

# GF Budget Picture - Nov 09 - Projection thru FY14

Assumes 3.5% growth on FY10 base including ARRA,  
(ARRA funds used to support GF Base in FY09=\$75m, FY10=\$175m, and FY11=\$100m)

FY11 Gap solutions that are ongoing in nature will also impact out years



# Even these deficit projections understate the problems faced by Vermont.

- Teachers retirement obligations grew from \$41 million in FY 2010 to \$63 million for FY 2011. State employee retirement costs, grew from \$32 to \$41 million. Without system changes, costs will continue to exceed revenues. Together this represents a \$31 million budget pressure. This is before retiree health care.
- Medicaid and health care caseload growth indicates a state dollar increased need of \$20 to \$30 million over projections for FY 2011.
- By 2012 there will be interest obligations for federal borrowing to meet obligations of the Unemployment Insurance Fund.
- There are \$35 million of currently approved school construction projects awaiting capital funds.
- There is no solution built into the budget for the Vermont State Hospital despite the identified need for a new facility.

# The Legislature and Executive have taken steps to address the structural shortfall. (Slide 1)

- The Legislature's Joint Government Accountability Committee has contracted with Public Strategies Group to find opportunities to do more with less and is working cooperatively with the administration.
- A Legislative Committee on Unemployment Insurance has been working on proposals to address that fund deficit.
- Based on other Legislative action:
  - The Judiciary has developed a restructuring proposal to reduce costs;
  - A current use working group has proposals to reduce program cost;
  - A legislative and executive commission is looking at education system issues; and
  - The Treasurer has a group with legislative and executive participation developing proposals on retirement costs.

# The Legislature and Executive have taken steps to address the structural shortfall (Slide 2)

- Administration actions include:
  - Education finance change proposals;
  - A set of “tiger teams” to find savings opportunities;
  - Budget instructions asking for 8% cuts from FY 2010 levels in FY 2011 budget submissions.
  - Working with the auditor to develop legislatively required results based budgeting skills.
- While there will be many pieces in each of these legislative, and executive and joint initiatives that many will disagree with, they represent some serious thinking about different ways to do things.
- In the next few years the current budget can not be maintained at its present level and difficult decisions will have to be made.

# There are other factors which impact these projections:

- Future year deficits will be impacted by a number of other factors including:
  - Revenues could be greater or less than the annual 5.4 – 7.5% growth rates projected for FY 2011 through FY 2013;
  - Changes in base revenues or spending through legislative or executive actions;
  - Additional Federal legislation, which could include temporary relief while not addressing the multi - year nature of problems (Some relief has been proposed in house health care bill); and
  - Federal health care reform and other legislation which could make the shortfalls worse, or, which could provide some relief.

# Transportation funding has its own set of problems

- Transportation revenues continue to fall short of expectations. November revenue again experienced a slight downgrade.
- As we push for fuel efficiency and smaller cars the state's gasoline and purchase and use tax revenues will continue to be under pressure.
- Legislative action provided some temporary relief, but the infrastructure problems are ongoing.
- This year the legislature created and funded a Transportation Infrastructure Bond (TIB) Fund which will allow much needed transportation projects to go forward.

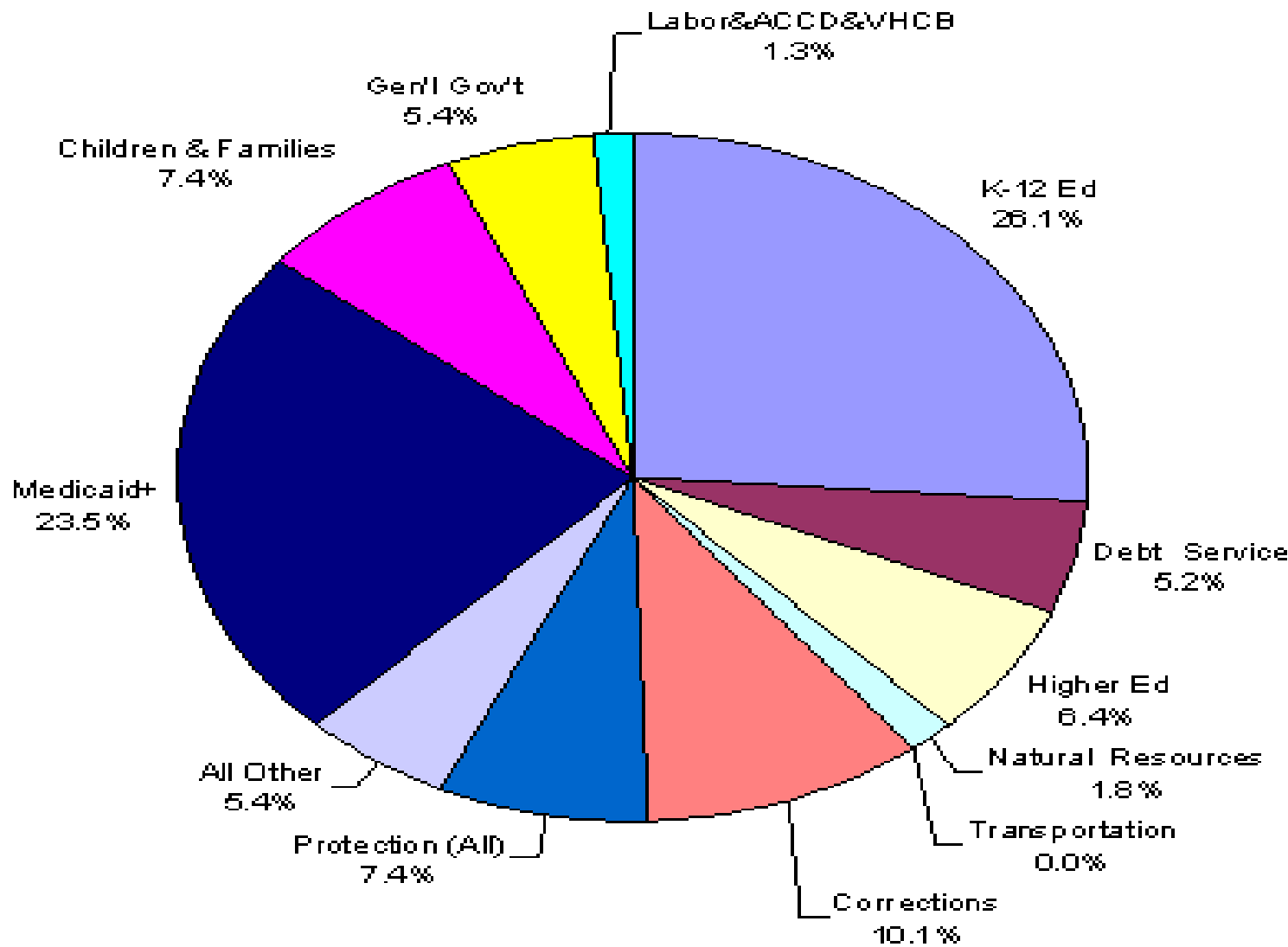
# State property tax rates will likely rise in FY 2011 and beyond

- Grand list value declines will increase tax rates and pressures on household incomes will impact revenues to the Education Fund.
- Local education received substantial stimulus funds in Title 1 & Special Education. As these revenue sources dry up school budgets will face renewed pressures.
- In FY 2011 education spending is projected to increase 2% as student counts continue to fall.
- In FY2012 the ability of the GF to restore ARRA and base reduction while intended may not be achievable
- Under current law we are likely to see the first increase in the education tax rates since Act 68 was enacted.

# Addressing the known General Fund and other fund deficits will require substantial actions

- The state budget supports services that impact the lives and concerns of Vermonters.
- As reductions are made they will impact services and how they are provided.
- The following chart illustrates the use of state general funds. There will be few easy decisions.

# FY10 Budget As Passed - GF and ARRA GF Like = \$1.268 Billion



# In FY 2012 a budget has to be built that is essentially 12% less General Fund than in FY 2010– How would you do it?

- Percent of Total
  - K-12 education 26% \_\_\_\_\_
  - Medicaid 24% \_\_\_\_\_
  - Corrections 10% \_\_\_\_\_
  - Public Safety (state police/judic/other) 7% \_\_\_\_\_
  - Children and Families 7% \_\_\_\_\_
  - Higher Education 6% \_\_\_\_\_
  - Debt Service 5% \_\_\_\_\_
  - Everything else 15% \_\_\_\_\_  
(General gov't, Labor, ANR,  
Economic Development and other)
  - Total 100% 88%

# The State Budget - Context

Once duplications are accounted for

- Total 'Real' FY10 Budget = \$4.6 Billion, including ARRA, which breaks down by funding sources as follows:

– Federal Funds	\$ 1.44 B	31%
– Fed. ARRA Funds	\$ 373 M	8%
– General Fund	\$ 1.09 B	23%
– Education Fund	\$ 1.07 B	23%
– Transportation Fund	\$ 215 M	5%
– Special Funds	\$ 450 M	10%
- The focus of this presentation is the General Fund plus \$174.5m ARRA funds used in place of general funds.
- ARRA: In FY 2010 \$174.5m of the ARRA funds offset General Fund; \$117.2m is for transportation projects and the rest of the ARRA funds are allocated to specified activities that are additional expenditures.