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STATE OF VERMONT
JOINT FISCAL OFFICE

MEMORANDUM

To: Members of the Joint Fiscal Committee

From: Catherine Benham

Date: November 6, 2023

Subject: November 2023 – Fiscal Officer's Report

In anticipation of the November 7 meeting, I have prepared an update of recent developments, some of which may also be on the Joint Fiscal Committee meeting agenda.

1. FY 2024 Revenue Collections Year to Date

The General Fund exceeded its forecast target in October but the Education and Transportation funds lag slightly. In total, the major funds were above the October target by +$3.1 million, or +1.2%. Due to the General Fund's continued positive performance, the funds are +25.4 million, or +2.5%, ahead of forecast so far this year. As a reminder, monthly revenue results may not align with monthly forecasts as well as they typically do because of the effects of the July flood and the deadline extension the Department of Taxes put in place to help flood-impacted individuals and businesses. Total revenue results will likely align with the forecast beginning in November.

Fund Highlights:

a. **The General Fund** was +5.9 million, or +3.7%, above target for the month of October; year to date it is +$31.6 million, or +4.9%, above target.
b. **The Education Fund** was -$1.6 million, or -2.2%, below forecast in October and is -$1.3 million, or -0.5%, below target so far this year.
c. **The Transportation Fund** was -$1.3 million, or -4.8%, below target in October and is currently -$4.8 million, or -4.7%, below forecast this year.

FY 2024 Fund Performance vs Official Forecast (in millions)

	Month of October			Year To Date (YTD)		
	Revenue	Revenue vs Target	% Over Target	Revenue	Revenue vs Target	% Over Target
General Fund	$167.7	+$5.9	+3.7%	$676.8	+$31.6	+4.9%
Education Fund	$68.6	-$1.6	-2.2%	$255.9	-$1.3	-0.5%
Transportation Fund	$25.1	-$1.3	-4.8%	$98.5	-$4.8	-4.7%

2. ARPA and FEMA Funds

As of September 26, all American Rescue Plan Act – State Fiscal Recovery (ARPA – SFR) funds had been appropriated. Per the report from the Administration, approximately $411 million has been spent and close to $638 million remained unspent at that time. At the November Joint Fiscal Committee meeting, Administration officials will deliver testimony on these funds, all of which must be obligated by December 31, 2024, and spent by December 31, 2026.

The ARPA – SFR expenditure report, most recently delivered to the Joint Fiscal Committee at its September meeting, is meant to help the General Assembly identify funds that may be available for reallocation. While the September 26 report provides the unexpended amount, it is not clear how much of these funds are unobligated and available for reallocation. In mid-November, the Joint Fiscal Office will meet with the Administration to determine which of these funds, if any, may remain unobligated and may potentially be available for reallocation. The status of ARPA – SFR funds and related programs will be part of the budget discussion during the upcoming legislative session.

October 31 was the final day for Vermont residents impacted by the July flood to apply for Federal Emergency Management Agency (FEMA) Individual Assistance funds. To date, FEMA has granted more than $22 million in Individual Assistance funds to Vermonters in the nine counties that were deemed eligible by the Agency. The U.S. Small Business Administration has approved over $23 million in low-interest loans for flood-affected businesses. The State has also received a FEMA award of $164 million in Public Assistance funds.

3. State Employees' and Teachers' Retirement Systems

The fiscal year 2023 actuarial valuations for VSERS and VSTRS have been released and are posted on the Treasurer's and Joint Fiscal Office's websites. The Other Post-Employment Benefits (OPEB) valuations are expected in December.

Last year, both retirement systems improved their funded ratios – even when factoring in recent assumption changes from the experience studies. Inflation cooled significantly last year (from 7.6% in June 2022 to 2.2% in June 2023), leading to minor actuarial gains from lower cost of living adjustment (COLA) payments. While investment performance exceeded the 7.0% assumption on a market basis last year, actuarial losses occurred, since losses from prior years are "smoothed" into the funding math. Overall, the total unfunded liabilities for both retirement systems decreased by -$10.25 million and now total $2.86 billion.

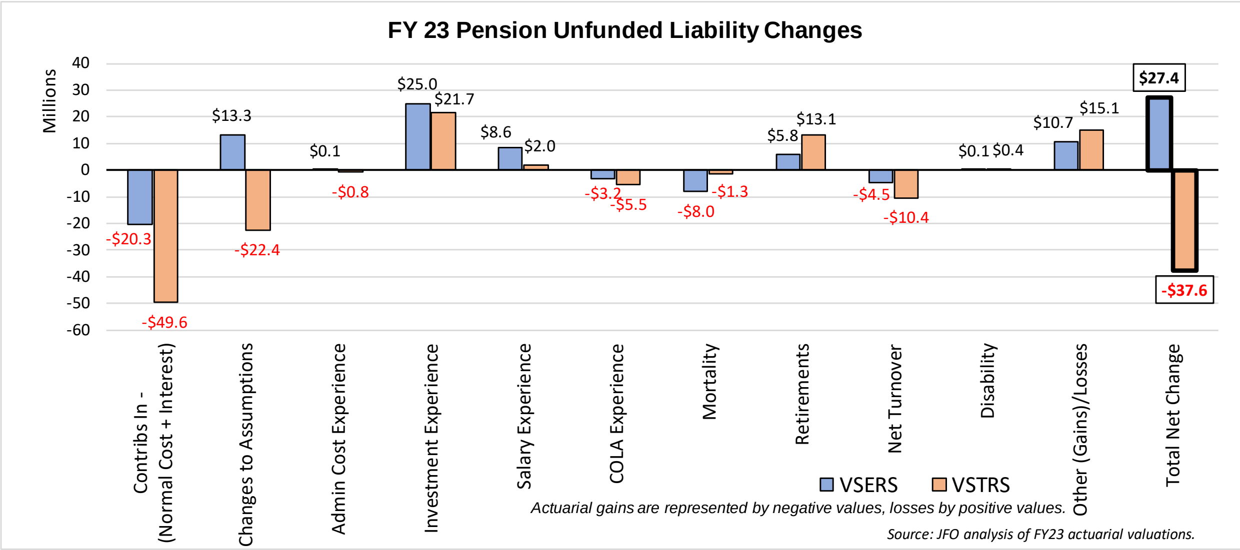
VSERS

- The State employees' retirement system (VSERS) funded ratio based on the actuarial value of assets improved, from 69.85% at the end of fiscal year 2022 to 70.31% at the end of fiscal year 2023 – its highest level since 2019. Net of all experience factors and assumption changes, the unfunded liability increased by $27.4 million to $1.066 billion.

- Investment performance was 7.58% on a market value basis. However, investment performance was 5.95% on an actuarial basis, which reflects the smoothing of deferred losses from prior years. Although there was positive growth, the investment performance fell short of the 7.0% assumption which led to an actuarial loss of -$25 million for fiscal year 2023.
- Lower than assumed COLAs to be paid in calendar year 2024 caused an actuarial gain of $3.2 million for VSERS.
- Several actuarial assumptions were revised in response to the recent experience study. The net impact of these changes was a relatively modest increase to the unfunded liability of $13.3 million.
- The Actuarially Determined Employer Contribution (ADEC) for fiscal year 2025 is $131.35 million. This is a $9.47 million (7.8%) increase above the fiscal year 2024 ADEC of $121.87 million and parallels a similar rate of growth in the active payroll (which grew by 7.7% from fiscal year 2022 to fiscal year 2023). This contribution is paid as a charge to participating agencies and funds in proportion to their shares of the active payroll.

<u>VSTRS</u>

- The teachers' retirement system (VSTRS) funded ratio based on the actuarial value of assets also improved, from 57.28% at the end of fiscal year 2022 to 59.30% at the end of fiscal year 2023 – its highest funded ratio since 2014. Net of all experience factors and assumption changes, the unfunded liability decreased by -$37.6 million to $1.795 billion.
- Investment performance was 7.76% on a market value basis. However, investment performance was 6.12% on an actuarial basis, which reflects the smoothing of deferred losses from prior years. Although there was positive growth, the investment performance fell short of the 7.0% assumption which led to an actuarial loss of -$21.7 million for fiscal year 2023.
- Lower than assumed COLAs to be paid in calendar year 2024 caused an actuarial gain of $5.5 million for VSTRS.
- Several actuarial assumptions were revised in response to the recent experience study. The net impact of these changes was a relatively modest decrease to the unfunded liability of -$22.4 million.
- The ADEC for fiscal year 2025 is $201.18 million. This is a $6.90 million (3.6%) increase above the fiscal year 2024 ADEC of $194.28 million, which is a lower rate of growth than the active payroll (which grew by 5.9% from fiscal year 2022 to fiscal year 2023). The normal cost component of the ADEC ($37.84 million) is paid primarily from the Education Fund. The unfunded liability amortization component ($163.34 million) is paid primarily from the General Fund. Local education agencies typically contribute between $6 and $7 million for federally funded staff, which offsets the State's share of the normal cost and unfunded liability proportionally.



Pursuant to Act 114 (2022), each pension system is expected to receive a $12 million "plus" payment in addition to the ADEC. These additional payments accelerate the amortization of the unfunded liability balance, save the State interest costs, and reduce the rate of ADEC growth in future years. The "plus" payments are expected to increase to $15 million per system in fiscal year 2026 and remain at that level until the respective systems reach 90.0% funded (expected in fiscal year 2033 for VSERS and fiscal year 2035 for VSTRS). When including the "plus" payments, the total fiscal year 2025 funding requirements will be $143.35 million (a 9.5% increase over fiscal year 2024) and $213.18 million (a 4.9$ increase over fiscal year 2024) for VSERS and VSTRS, respectively.

The Joint Public Pension Oversight Committee will convene on November 7 at 12:45 PM to evaluate the results of the recent experience studies and actuarial valuations in greater detail.

4. **Temporary Medicaid Continuous Enrollment**

At the start of the COVID-19 pandemic, the federal government enacted the Families First Coronavirus Reponse Act (FFCRA) which included a provision requiring Medicaid programs to keep beneficiaries continuously enrolled though the end of the public health emergency. This essentially paused eligibility redetermination reviews. For this, states received a temporary increase of 6.2% to their Federal Medical Assistance Percentage (FMAP) rate.

Under the Consolidated Appropriations Act, 2023 (CCA, 2023), Medicaid continuous enrollment ended on March 31, 2023. States were given up to 14 months to return to normal eligibility and enrollment operations, including those for Medicaid redeterminations. According to its Renewal Dashboard, the Department of Vermont Health Access (DVHA) conducted reviews for 31.1% of the Medicaid population by the end of September.

Additionally, the temporary 6.2% FMAP rate increase was phased down. Since April 1, 2023, it has decreased quarterly: to 5.0% on April 1, 2.5% on July 1, and 1.5% on October 1. The FMAP rate increase ceases altogether at the end of calendar year 2023. Between fiscal years 2020 and 2023, the FMAP rate increase resulted in over $300 million in General Fund savings for the State. It is estimated that it will result in an additional $15 million in General Fund savings in fiscal year 2024.

The CCA, 2023, also requires all states to provide 12 months of continuous eligibility for children under the age of 19 who are covered by Medicaid and the Children's Health Insurance Program (CHIP). Preliminary estimates indicate this could have an annualized budget pressure of approximately $2 million and that will need to be addressed in the Budget Adjustment Act.

5. **Legislative Budget**
The Department of Finance and Management released budget development guidelines for fiscal year 2025 on August 31. Agencies and departments are asked to limit base spending increases to 3.0% of fiscal year 2024 General Fund appropriations. However, agencies and departments must absorb all salary, benefit, and Internal Service Fund increases, as well as any other inflationary pressures, within this 3.0% target. These increases include 15.0% for health benefits, an estimated 3.0% for Internal Service Fund charges, the Child Care payroll tax, Family and Medical Leave Insurance, and some retirement cost increases. The Joint Fiscal Office has met with all legislative business units and has started preparing the fiscal year 2025 legislative budget. Later this fall, once the budget is completed, the Joint Fiscal Office will submit it to the Joint Legislative Management Committee for approval.

6. **Joint Fiscal Office Updates**
The Joint Fiscal Office continues to work on numerous research projects. These include issue briefs on pupil weight changes made by Act 127 (2022), wealth distribution in the state, and Medicaid redeterminations. Among other things, the Joint Fiscal Office is working on the fiscal year 2024 fee report, a study on potential funding mechanisms for the Universal Service Fund, and the Basic Needs Technical Advisory Committee report. The RFP the Joint Fiscal Office issued for a report on public infrastructure financing, per Act 72 (2023), received no proposals. The Joint Fiscal Office is currently working on the next steps for this project.

In addition to this work, the Joint Fiscal Office continues to staff multiple committees during the off-session:

a. The Renewable Energy Standard Reform Working Group has met five times so far. During its meetings, the Group has discussed the various challenges the State faces in moving to a 100% Renewable Energy Standard by 2030. With the help of the facilitator the Joint Fiscal Office contracted with, the Group has reviewed data, discussed the state of the energy industry in Vermont and its current Renewable Energy Standard, and conducted internal polling on various decision points. Per Act 33 (2023), the Group must submit both draft legislation and a report on its deliberations to the committees of jurisdiction by December 1. The Group meets again on November 15 to review analysis conducted by the economic modeling consultant the Joint Fiscal Office contracted with.

b. The Basic Needs Budget Technical Advisory Committee, established by Act 54 (2023) met five times over the course of September and October. The committee, the first of its kind since 2008, was tasked with reviewing the assumptions and methodology used for the biannual Basic Needs Budgets and Livable Wage Report. The Committee took testimony from numerous experts, including State Auditor Doug Hoffer and Tom Kavet, both of whom both of whom contributed to the Livable Income Study Committee report in 1999. Joint Fiscal Office staff presented on the assumptions made for the various components of the basic needs budget. As per Act 54, the Committee completed a report with its recommended changes and submitted it to the committees of jurisdiction. The recommended changes for the Joint Fiscal Committee will be presented at the meeting.

c. The Summer Government Accountability Committee, established by Act 53 (2023), met on November 3. Per Act 53, which also repealed the Government Accountability Committee, the Committee is tasked with reexamining the principle of government accountability in the Legislative Branch. Chief Fiscal Officer Catherine Benham provided testimony on the work performed by the Joint Fiscal Office.

d. Both the Joint Information Technology Oversight Committee and Joint Public Pension Oversight Committee meet on November 8.

e. The Joint Legislative Management Committee will meet on November 8.

7. Joint Fiscal Office Staff Updates

a. Sarah Clark departed the Joint Fiscal Office at the end of October to join the Agency of Administration as its Deputy Secretary. She will be missed but we are excited for her and look forward to working with her in her new role.

b. Emily Byrne accepted the Deputy Fiscal Officer position. She has done incredible work as the Joint Fiscal Office’s Revenue Team Lead and we are glad that she has taken over as Deputy.

c. Chris Rupe, the Joint Fiscal Office’s transportation analyst, has accepted and started in the Revenue Team Lead position as an Associate Fiscal Officer. Since joining the Joint Fiscal Office team Chris has deftly managed revenue and budgetary issues relating to transportation and pension funds. He will continue to work on pension topics. We’re happy to have him in the Revenue Team Lead position.

d. The Joint Fiscal Office will begin recruiting for the transportation analyst position soon.

e. Applications for the session-only Senate Appropriations Committee Assistant have been submitted. The Joint Fiscal Office is conducting interviews.

8. Notable Dates

The Joint Fiscal Office will host an all-member briefing on Friday, December 1.