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An Update from the Joint Fiscal Office

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The Fiscal Focus is a nonpartisan update prepared by the Joint Fiscal Office (JFO) staff to keep legislators current during the off-season. As your staff, we believe it is important for a citizen legislature to be kept informed of local, State, and federal financial developments while the General Assembly is adjourned. It is important for us to hear what topics interest you for future issues. If you have any comments or suggestions, please let us know.

Tax Collections Strong in General and Education Funds

The revenues for November finished above target for the month. State revenues in all three major funds were +\$11.9 million or +5.8% ahead of target for the month. Cumulatively the funds are +\$76.5 million or +6.5% above forecast.

General Fund (GF): The General Fund exceeded the forecast in November, finishing ahead of target by +\$8.9million or +7.4%. For the year, the GF continues to track ahead of forecast by +\$68.5 million or +9.2%. Of note, approximately \$10 million of excess revenues can be attributed to a one-time event(s) this fall.

Education Fund (EF): The Education Fund was slightly above target in November, coming in over forecast by +\$1.9 million or +3.3%. The Education Fund remains ahead of forecast by +\$9.5 million or +3.2%.

Transportation Fund (TF): The Transportation Fund was slightly above target for the month of November, ending above forecast by +\$0.7 million or +3.1%. For the year, the TF remains below forecast by -\$1.6 million or -1.2%.

Fund Performance Summary for Fiscal Year 2023 through November (in millions)

| | Nov-22 (millions) | Month Vs. Target | % over (under) target | YTD (millions) | YTD vs Target (millions) | % over (under) target |
|------------------------|----------------------|---------------------|--------------------------|-------------------|-----------------------------|--------------------------|
| General Fund | \$129.7 | \$8.9 | 7.40% | \$812.7 | \$68.5 | 9.2% |
| Education Fund | \$57.5 | \$1.9 | 3.3% | \$308.3 | \$9.5 | 3.2% |
| Transportation Fund | \$23.5 | \$0.7 | 3.1% | \$125.6 | -\$1.6 | -1.2% |

Education Fund Outlook for Fiscal Year 2024

On December 1, the Tax Commissioner submitted a letter to the General Assembly that projected an increase in the average property tax bill based on a consensus Education Fund Outlook prepared by the Administration and JFO. This letter, colloquially known as the “December 1 Letter,” is intended to provide guidance to school boards currently preparing budgets for submission to their voters and serves as a starting point for deliberations by the General Assembly.

The results presented in the December 1 Letter represent a largely ministerial task, as the calculations are highly prescribed and multiple assumptions are statutorily required, including:

- The base homestead property tax rate is \$1 per \$100 of equalized value.
- The base tax rate on household income is 2%.
- The statutory reserve is maintained at 5% of net appropriations.
- The percent change in the average tax bill is the same for all taxpayers.
- All unreserved and unallocated funds from the previous fiscal year are applied towards lowering property tax rates.

With these caveats in mind, the December 1 Letter and consensus Education Fund Outlook result in the following average tax rates.

Average Equalized Rate Changes

| | FY 2023 | FY 2024 | Change |
|-------------------------------------|---------|---------|---------|
| Average Homestead Property Tax Rate | \$1.38 | \$1.31 | -\$0.07 |
| Average Household Income Tax Rate | 2.31% | 2.31% | 0.00% |
| Non-homestead Property Tax Rate | \$1.466 | \$1.386 | -\$0.08 |

While equalized rates are estimated to decrease, the average education tax bill is estimated to increase by 3.7% across all three classes (homestead property, income, and non-homestead property) based in large part on changes in the grand list.

Importantly, as statutorily required, this assumes the entire surplus has been applied to lowering tax rates. If none of the surplus were to be applied to lowering tax rates, the average tax bill across all three classes would increase by an estimated 8.3%.

As policy makers and voters consider the yields, rates, and school budgets for Fiscal Year 2024, the Commissioner pointed out significant reductions of the Common Level of Appraisal (CLA) in some towns, an estimated surplus of \$63 million, and projected growth in education spending of 8.5% as underlying factors driving the projected changes in the tax rates and yields.

Finally, it is important to note that the December 1 Letter is the beginning, not the end, of deliberations for the upcoming legislative session. In the next few months, better information will become available including board-approved budgets for the 2023-2024 school year, the January 2023 consensus revenue forecast for non-property tax sources, and the Budget Adjustment Act for Fiscal Year 2023. All of these inputs will ultimately impact the final yields and property tax rates for FY 2024.

Despite Economic Headwinds, Vermont's Retirement Systems Made Significant Gains in Fiscal Year 2022

According to the latest actuarial valuations, Vermont's unfunded retirement liabilities for state employees and teachers decreased by nearly \$1.4 billion during Fiscal Year 2022. The reforms and one-time contributions contained in Act 114 (2022) explain most of the decline, even as economic conditions challenged the systems and slightly blunted the reform impacts. Below is a summary of the valuations and Fiscal Year 2024 funding needs. More information can be found at this [link](#).

| Vermont's Unfunded Retirement Obligations for State Employees and Teachers | | | | | | |
|--|-------------------------|--------------|-------------------------|--------------|---------------------------|--------------|
| | FY 2021 | | FY 2022 | | Change - FY2021 to FY2022 | |
| | Unfunded Liability | Funded Ratio | Unfunded Liability | Funded Ratio | Unfunded Liability | Funded Ratio |
| State Employees (VSERS) | | | | | | |
| Pension | \$ 1,064,368,199 | 67.6% | \$ 1,038,338,081 | 69.9% | \$ (26,030,118) | 2.3% |
| OPEB | \$ 1,473,073,282 | 7.5% | \$ 802,517,251 | 11.6% | \$ (670,556,031) | 4.1% |
| State Employee Total | \$ 2,537,441,481 | | \$ 1,840,855,332 | | \$ (696,586,149) | |
| Teachers (VSTRS) | | | | | | |
| Pension | \$ 1,950,363,905 | 52.9% | \$ 1,832,425,033 | 57.3% | \$ (117,938,872) | 4.4% |
| OPEB | \$ 1,275,587,042 | 1.1% | \$ 717,851,240 | 5.3% | \$ (557,735,802) | 4.2% |
| Teachers Total | \$ 3,225,950,947 | | \$ 2,550,276,273 | | \$ (675,674,674) | |
| Grand Totals | \$ 5,763,392,428 | | \$ 4,391,131,605 | | \$ (1,372,260,823) | |

Pensions

Both major pension systems improved their funded status and lowered their unfunded liabilities by \$144 million during Fiscal Year 2022.

Act 114 included \$200 million of one-time contributions, plus higher employee contributions to offset employer pension costs and changes to cost of living adjustment provisions. This lowered the unfunded liabilities by an estimated \$36.4 million for the Vermont State Employees' Retirement System (VSERS) and \$30.8 million for the Vermont State Teachers' Retirement System (VSTRS). However, the systems also experienced losses due to retirements and higher-than-assumed rates of inflation that pushed salary growth and cost-of-living adjustments higher.

The systems also faced a difficult investment climate, with market returns of -8.66% and -8.85% for VSERS and VSTRS, respectively. Deferred gains from a strong Fiscal Year 2021 offset some of the losses from Fiscal Year 2022. However, the systems now have deferred investment losses of \$247 million that will drag on future performance as they are "smoothed" into future years' funding calculations. Without Act 114, the difficult economic environment would have led to actuarial losses for both retirement systems. Instead of decreasing, JFO estimates the unfunded liabilities would have increased by approximately \$95 million (VSERS) and \$38 million (VSTRS).

Other Post-Employment Benefits (OPEB)

In addition to pensions, Act 114 also addressed Vermont's underfunded OPEB systems that provide subsidized health care benefits to retired state employees and teachers. Prior to Fiscal Year 2023, the State funded only the annual cost of providing benefits to current retirees (pay-as-you-go). Act 114 established a policy of prefunding these benefits, similar to how pensions are prefunded. Contributions are made over the course of an active member's career, are invested, and fund the cost of their future benefits. Prefunding allows for investment returns to fund most of the cost of benefits, saving tax dollars in the long term, but requires higher costs in the near term than the former pay-as-you-go practice.

The Fiscal Year 2022 OPEB valuations estimate that Act 114 and the shift to prefunding reduced Vermont's OPEB liabilities by \$1.5 billion. Most of this impact (\$770 million for VSERS, \$735 million for VSTRS) is due to the systems adopting a 7.0% discount rate tied to the assumed rate of investment return, which is permitted under a prefunding policy. Like with the pension systems, the gains from Act 114 were offset to an extent by factors like changes to health care costs, participation rate, and lackluster investment performance in the prior year. Despite these factors that increased costs, the two OPEB systems still reduced their liabilities by more than \$1.2 billion combined. OPEB costs are expected to increase by 3.5% (VSERS) and 3% (VSTRS) in future years.

Actuarially Determined Employer Contribution (ADEC)

Below is the annual funding requirement or budgetary impact for each system.

State Employees' Systems — Pension ADEC for Fiscal Year 2024 is \$121.9 million, \$4 million less than the Fiscal Year 2023 levels calculated pre-Act 114 and \$5.9 million more than the Fiscal Year 2023 levels post-Act 114. Act 114 calls for an additional \$9 million supplemental payment toward the unfunded liability, for a total cost of \$130.9 million. These contributions are paid as a charge to agencies according to the various funds that support the active payroll. OPEB ADEC for Fiscal Year 2024 will be \$67.1 million, this is up \$2.6 million from Fiscal Year 2023. Like the state employees' pension system, this cost is charged against active payroll and is across all funds.

Teachers' Systems — Pension ADEC for Fiscal Year 2024 is \$194.3 million, \$10.9 million lower than original Fiscal Year 2023 levels calculated pre-Act 114 and \$0.7 million lower than Fiscal Year 2023 levels post-Act 114. Act 114 calls for an additional \$9 million supplemental payment toward the unfunded liability, for a total cost of \$203.3 million. The portion of the contribution that funds the future retirement benefits of today's active workforce (the normal cost) is \$34.8 million and is paid mostly from the Education Fund. OPEB ADEC is \$61.3 million, up by \$6.5 million from Fiscal Year 2023. Like the teachers' pension system, the normal cost of \$17 million will be paid from the Education Fund.

Fiscal Year 2023 Budget Adjustment Act (BAA) Update

We expect the Administration to provide their budget adjustment recommendation for the current year (Fiscal Year 2023) budget adjustment no later than the week of Jan 9. Several programs are likely to require significant adjustments.

Medicaid and related programs administered by the Department of Vermont Health Access (DVHA) are anticipated to need additional funding. Based on the work of the Medicaid Consensus Group, the total gross increase from state and federal funds is estimated at \$47 million. The State share of this need will be in the range of \$20 million but should be covered by Agency of Human Services (AHS) carryforward resources or the continued Federal Matching Assistance Percentage (FMAP) increase of 6.2%. We are monitoring the impact a federal budget deal could have on the enhanced FMAP and redetermination schedule for current enrollees.

Other areas of pressure include costs in the Department of Mental Health (DMH) at the Vermont Psychiatric Care Hospital for travel nurse contracts and state employees. There is also anticipated Reach Up caseload pressure. The Low Income Heating Assistance Program (LIHEAP) benefit level was set assuming one-time supplemental funds of \$5.8 million. Finally, additional funds are needed to cover the 8% increase in the state troopers' approved collective bargaining agreement.

The Fiscal Year 2023 BAA will make other monetary adjustments as well as updates to certain budgetary language. One-time GF resources are currently available, some of which will be used to meet the BAA needs. JFO expects remaining unallocated amounts to be addressed in next year's (Fiscal Year 2024) budget proposals.

BGS to Begin “Charging for Charging” January 1

The Department of Buildings and General Services (BGS) recently announced that, beginning January 1, it will levy a \$0.26 per kilowatt hour fee for the public use of its electric vehicle charging stations. There are currently 24 ChargePoint Level 2 charging stations that will be subject to the fee, which are located primarily at state-owned office buildings and facilities – including around the Capitol Complex.

Revenues collected through the fees will cover costs for electricity and administrative expenses to operate the chargers, in accordance with 32 V.S.A. §604. As these chargers are intended to be available to the public, users are strongly encouraged to move their vehicles to alternate locations once they are sufficiently charged so others can use the charging stations.

Grant and Limited-Service Position Update

Since the adjournment of the 2022 session, the JFO has received **36 grants** from the Administration. **JFO #3099-3135** are available to review on the [grants spreadsheet](#) on the JFO website.

Joint Fiscal Committee Updates

The Joint Fiscal Committee met on December 14 and reviewed or acted on the following items:

- Received an overview of the Executive Branch Fees and Fund Deficits Report from Commissioner Greshin of Finance and Management.
 - Reviewed the Vermont Emergency Rental Assistance Program (VERAP) and Transitional Housing proposals from Deputy Secretary of Administration Douglas Farnham, Interim Commissioner of the Department for Children and Families (DCF) Harry Chen and Senior DCF Advisor Katarina Lisaius. The committee approved the motion to update the allocations associated with JFO Grant #3034 for VERAP 1 funding.
 - Approved the Land Acquisition donation request from the Department of Fish and Wildlife associated with land in the towns of Mount Holly and Weston.
 - Received an update from the JFO Chief Fiscal Officer that included honoring the retiring members of the Joint Fiscal Committee.
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Joint Fiscal Office Updates

Studies, Committees, and other

Child Care System Funding – JFO has contracted with the RAND Corporation to evaluate the economic impacts of and potential funding mechanisms adjusting Vermont’s existing childcare system. The draft report is being finalized and the final report is due on January 17, 2023.

Global Warming Solutions Act – In response to the charge from the Global Warming Solutions Act, and following JFO’s earlier report, JFO continues to prepare a report on the economic, budgetary, and fiscal implications of potential policies that would enable Vermont to meet its climate goals. The report includes a focus on policies aimed at promoting low- and middle-income household adoption of electric vehicles, heat pumps, and weatherization. JFO is also working to understand the climate change initiatives included in the federal Inflation Reduction Act, and their implications for Vermont.

Income-based Education Tax Study Committee – The Education Income Tax Committee’s final meeting took place on December 21, 2022. The Committee reviewed a draft of the report of findings and recommendations, received testimony from stakeholders, and discussed finalization of the report and next steps. The Committee approved the draft report pending discussed changes. The final report is due on December 30, 2022.

Report on Vermont’s Education Fund – In fulfillment of the charge set forth in Section 19 of Act 127 (2022), JFO continues to work on a report that examines and provides options for structural changes to the Education Fund, including methods for cost containment, the mechanics of setting the yields to include a “constitutionally adequate spending amount,” and the funding of school districts in an equitable manner. This report is due by January 15, 2023.

Funding and Governance Structures of Career Technical Education (CTE) – JFO has entered a contract with Augenblick, Palaich and Associates (APA) to perform work on the funding and governance structures of Career Technical Education in Vermont, pursuant to Section 17 of Act 127 (2022). The JFO has also contracted with Bill Talbott to provide expertise to both the staff of JFO and APA as the study progresses. The JFO has met weekly with APA to discuss progress on the study. The report is due on March 1, 2023.

English Learners and Categorical Aid Study – JFO has contracted with Tammy Kolbe to perform work associated with the English Learners Services and Categorical Aid Study as required by Section 11 of Act 127 (2022).

Vermont 2023 Biennial Tax Expenditure Report – JFO is writing the 2023 Biennial Tax Expenditure Report, which will include a full review of the Vermont Earned Income Tax Credit (EITC). In addition, the tax department is conducting expedited reviews on a few specific areas. The report is due on January 15, 2023.

Livable Wage Study – JFO is working on the biennial livable wage and basic needs budget study, which is due on January 17, 2023. No methodology changes are proposed for the 2023 study. However, JFO does request that the General Assembly consider appointing a technical advisory council, or similar body, to perform a holistic review of the statute and methodology prior to the next study. Act 202 (2008) created a one-time technical advisory council to review the methodology and make changes to the livable wage study statute (2 V.S.A. §526).

Staff Updates

- Theresa Utton-Jerman has accepted a position in the House Clerk's Office. In her time at JFO, Theresa made significant contributions serving the House Appropriations Committee and the Joint Fiscal Committee. We will miss her strong work ethic, and energy. We are looking forward to working with her in the House Clerk's Office.
- Erin Viera has been hired to fill the vacant Senior Staff Associate position and will be serving the House Appropriations Committee. Erin joins JFO after working for the Office of Professional Regulation in the Secretary of State's Office and Norwich University.
- Andrea Smith has been hired to serve as the Committee Assistant to the Senate Appropriations Committee. Her background is in the non-profit and hospitality industry. She has a Bachelor of Science from the University of Vermont.
- Grady Nixon starts on December 27 and will serve as the Fiscal Editor and Appropriations Bill Coordinator. Grady joins JFO after working as a Research Associate for the Hudson Institute. He holds a Master of Arts from King's College London.

We are thrilled to have Erin, Andrea and Grady on board and look forward to introducing you to them!

Notable Dates

Fiscal Year 2023 Budget Adjustment Testimony House Committee on Appropriations

Anticipated to be received in early to mid-January.

Room 11, State House

Inaugural Message of Governor

January 5, 2023 at 2:00 PM

Well of the House Chamber, State House

Governor's Budget Address

January 20, 2023 at 1:00 PM

Well of the House Chamber, State House
