by the State board of education. Membership in the system for those covered classes is a condition of employment. The membership is made up of:

- general teachers who were hired prior to 1984 and did not join the non-contributory system (Group A), with a contribution rate of 5.5 percent of payroll (contributions cease upon attainment of 25 years of creditable service);
- terminated vested members of the non-contributory system (Group B); and
- all other general teachers (Group C), with a contribution rate of 3.40 percent.

The State appropriates funding for pension costs associated with the above two plans. In fiscal years prior to 1982, both systems were solely contributory. Under legislation effective July 1, 1981, Vermont State employees and State teachers could elect to transfer their current memberships from a contributory to a non-contributory membership class (see Note 5 E. Single Deposit Investment Account). However, in 1990, the Legislature again made both systems contributory effective July 1, 1990, for the VSTRS and January 1, 1991, for the VSERS. The State's contribution to each system is based on percentage rates of each member's annual earnable compensation. These rates include a "normal contribution" rate and an "accrued liability contribution" rate and are calculated based upon the liabilities of each system as determined by actuarial valuations.

At June 30, 2009, VSERS and VSTRS membership consisted of:

	VSERS	VSTRS
Active employees:		
Vested	5,752	8,076
Non-vested	2,343	2,723
Total active employees	8,095	10,799
Retirees & beneficiaries of deceased retirees currently receiving benefits:	4,797	5,910
Terminated employees entitled to benefits but not yet receiving them (vested):	798	721
Inactive members:	939	2,655
TOTAL PARTICIPANTS:	14,629	20,085

The largest concentration of members by system are Group F in the VSERS system and Group C in the VSTRS system, accounting for 93.9 percent and 99.8 percent , respectively, of the total active members of each system. While health care benefits vary, these groups do have a similar benefit structure for pensions, although COLA provisions were adjusted, as noted below for Group F members, with a corresponding contribution rate increase:

Benefit Comparison VSERS Group F and VSTRS Group C

Selected Benefit Categories:	VSERS Group F	VSTRS Group C
Maximum Retirement Allowance	50% of Average Final Compensation (AFC)	50% of Average Final Compensation (AFC)
Benefit Formula	1.25% x service prior to 12/31/90 + 1.67% on 1/1/91	1.25% x service prior to 6/30/90 + 1.67% on 7/1/90
Average Final Compensation (AFC)	Highest 3 consecutive years, excluding unused annual leave payoff	Highest 3 consecutive years, excluding payments for anything other than service actually performed
Early Retirement Reduction	Normal allowance reduced by 6% for each year commencement precedes age 62	Normal allowance reduced by 6% for each year commencement precedes age 62.
Early Retirement Date	Age 55 with 5 years of service	Age 55 with 5 years of service
Normal Retirement Date	62 or 30 years of service	62 or 30 years of service
Member Contributions	5.1% of earnings	3.4% of earnings adjusted each year for changes in the cost of retiree medical insurance; currently 3.54%

Note: see below for changes for Group F members hired after 7/1/2008.

Under legislation enacted in fiscal year 2008, VSERS benefits were modified in three respects for members hired on or after July 1, 2008. First, the maximum benefit payable was increased from 50 percent to 60 percent of the average final compensation (AFC). Second, the eligibility condition for an unreduced benefit changed from the attainment of age 62 or 30 years of service to age 65 or a "rule of 87," attainment of that number through a combination of years of service and age. Third, for members not eligible for an unreduced benefit, the reduction for early retirement changed from a uniform 6 percent per year to one determined on a service-based schedule.

The remaining significant provision of the same legislation makes changes to retiree cost of living (COLA) adjustments. The annual-cost-of living adjustment (COLA) applicable to the benefits of Group F members retiring after July 1, 2008, rose from 50 percent of the annual increase of the Consumer Price Index (CPI) to 100 percent of the annual increase in the CPI index, up to a ceiling of 5 percent, effective January 1, 2014. Only current Group F members who were actively contributing into the system on June 30, 2008, and retire on or after July 1, 2008, will be eligible for the enhanced COLA in 2014. Group F members who terminated service or transferred to another group plan prior to June 30, 2008, are not eligible for the new

COLA unless they return to active Group F service after July 1, 2008, and it is prior to retirement.

Vermont's benefits for these groups are modest when compared to other state public retirement plans. In reviewing the value associated with each year of service, Vermont service year benefits (1.67 percent) are low compared to the median of 1.85 percent. Also, the limitation of the retirement benefit (50 percent for all but VSERS Group F hired after 7/1/08) is extremely low. The cost-of-living adjustments seem to be slightly on the positive side of a continuum of benefits, as are early retirement eligibility provisions. These factors were considered when identifying possible recommendations with the objective of maintaining basic provisions that would not make the plans less competitive than the mainstream of other state public systems. As a result, the emphasis of the Commission was to explore the raising of the age for eligibility for normal and early retirement (with a corresponding increase in the maximum benefit) which is also consistent with the increases in life expectancy and work productivity.

VSERS Group C members account for 5.4 percent of the system's active members while Group D accounts for just 0.6 percent of the total. Their benefit structures include:

Benefits - VSERS Group C

Selected Benefit Categories:	VSERS Group C	VSERS Group D
Maximum Retirement Allowance	50% of Average Final Compensation (AFC)	100% of Final Salary
Benefit Formula	2.5% x service	3.33% x service (after 12 years in group D)
Average Final Compensation (AFC)	Based on highest 2 consecutive years of pay	Final salary at retirement
Early Retirement Reduction	No reduction	Normal allowance reduced by 3% for each year commencement precedes age 62.
Early Retirement Date	Unreduced at age 50 with 20 years of service	Age 55 with 5 years of service
Normal Retirement Date	Age 55 (mandatory)	Age 62
Member Contributions	6.98% of earnings	5.1% of earnings

Again, the Commission directed its efforts at reviewing impacts of raising retirement eligibility ages as opposed to making major changes to the basic benefit structures.

A more detailed listing of benefits by system and group is attached as Exhibits #1 (for VSERS) and #2 (VSTRS). In addition, a number of key benefit provisions are compared to state public plans in New England (Exhibits #3 and #4). Exhibits are located on pages 22-25 of this report.

Medical Insurance Plan Descriptions

Vermont State Employees' Retirement System

Employees retiring directly from active State service for any reason (disability, early, or normal), may carry whatever coverage is in effect at that time into retirement for themselves and their dependents. During the lifetime of the retiree, currently only 20 percent of the cost of the premium will be paid by the retiree. If the retiree chooses the joint and survivor pension option, and predeceases his or her spouse, the medical benefits may also continue for the spouse, along with the pension. However, generally the surviving spouse must pay 100 percent of the cost of the premium. In addition, once retirees become eligible for Medicare coverage (at age 65) it is mandatory that they enroll in both Medicare Part A and Part B as soon as possible. Medicare thus becomes the primary insurer, with the State plan becoming secondary. The retiree's State insurance premium costs will then decrease in recognition of this change.

If an employee, other than a Group C member, does not retire directly from State service, he or she is not eligible to participate in the State's medical insurance plan. Group C members who terminate with 20 or more years of service, but are not yet 50, may pick up the medical coverage at the time they begin retirement benefits. If the insurance is terminated at any time after retirement, coverage will not be able to be obtained again at a later date.

Based on legislation enacted during fiscal year 2008, Group F employees hired after July 1, 2008, will receive a tiered retiree health care reimbursement based on completed years of service. As part of the enacted legislation, Group F employees hired after July 1, 2008, also have the ability to recapture (access) subsidized health insurance at 80 percent upon initiation of retirement benefits in a manner comparable to regular retirements. This applies even if the employee terminated prior to his or her early retirement date, providing the member has 20 years of service upon termination of employment. At the time, this initiative was projected to realize a savings of approximately $265 million over 30 years on a pay-as-you-go basis.

As of June 30, 2009, 3,571 retirees were enrolled in the medical plan in the single, spouse, and family plan options. The retirees contributed $5.1 million in premiums and incurred $26.7 million in claims expenses for the fiscal year ending June 30, 2009. The State's fiscal year 2009 contributions to the VSERS included, on a pay-as-you-go basis, $18.1 million for the State's share of the cost of the premiums. The VSERS paid S17.9 million in premiums, on a pay-as-you-go basis, to the Medical Insurance Fund for this benefit in fiscal year 2009.

State Teachers' Retirement System

Retirees in the VSTRS plan participate in multi-employer health coverage plans operated by the Vermont Education Health Initiative (VEHI) which is managed jointly by the Vermont School

Boards Insurance Trust and the Vermont-National Education Association. VEHI partners with Blue Cross Blue Shield to provide health insurance to retired and active teachers.

Members of the VSTRS have access to three medical benefit plans in retirement. The plans are identical to those offered to active teachers in public school systems in Vermont. Members may pick up medical coverage under one of the plans offered for themselves and all eligible dependents at the time of retirement, or anytime thereafter during one of the semi-annual open enrollment periods. If the member has a minimum of 10 years of creditable service at the time of retirement, the system picks up 80 percent of the retiree's premium only, based on the cost of the "standard plan" as defined by statute; the retiree must pick up the full cost of the premium for all covered dependents. As of June 30, 2009, 3,932 retirees are enrolled in the single, spouse, and family medical plan options. The retirees contributed $10.96 million in premiums and the system contributed $16.7 million in premiums and paid $16.4 million, on a pay-as-you-go basis, in fiscal year 2009.

Once a retiree becomes eligible for Medicare coverage (at age 65), it is mandatory that he or she enroll in both Medicare Part A and Part B. Medicare becomes the primary insurer and the Teachers' medical plans become the secondary carrier. Two of the plans offered become "carve-out" plans to coordinate with Medicare, and one of the plans is replaced with a true Medicare supplemental plan. The premiums for all plans are reduced in accordance with the decrease in liability once Medicare becomes primary.

Exhibit #1

VSERS Group Comparison

Group Comparison	Group A	Group C	Group D	Group F
Employee Contributions	5.10% of gross salary	6.98% of gross salary	5.10% of gross salary	5.1% of gross salary
Average Final Compensation (AFC)	Highest 3 consecutive years, including unused annual leave payoff	Highest 2 consecutive years, including unused annual leave payoff	Final salary at retirement	Highest 3 consecutive years, excluding unused annual leave payoff
Benefit Formula	1.67% x creditable service	2.5% x creditable service	3.33% x creditable service (after 12 years in Group D)	1.25% x service prior to 12/31/90 + 1.67% x service after 1/1/91
Maximum Benefit Payable	100% of AFC	50% of AFC	100% of Final Salary	50% of AFC **#1(see footnote at bottom of chart)**
Normal Retirement (no reduction)	Age 65 or 62 with 20 years of service	Age 55 (mandatory)	Age 62	Age 62 or with 30 years of service **#2(see footnote at bottom of chart)**
Post-Retirement COLA	Full CPI, from a minimum of 1% up to a maximum of 5%, after 12 months of retirement	Full CPI, from a minimum of 1% up to a maximum of 5%, after 12 months of retirement	Full CPI, from a minimum of 1% up to a maximum of 5%, after 12 months of retirement	50% CPI until 1/1/2014; 100% of CPI thereafter, from a minimum of 1% up to a maximum of 5%, after reaching age 62, or (if retired after June 30, 1997) 30 years service
Early Retirement Eligibility	Age 55 with 5 years of service or 30 years of service (any age)	Age 50 with 20 years of service	Age 55 with 5 years of service	Age 55 with 5 years of service
Early Retirement Reduction	Actuarially reduced benefit if under 30 years of service	No reduction	3% per year from age 62	6% per year from age 62 **#3(see footnote at bottom of chart)**
Post-Retirement Survivorship Options	100% and 50% (with or without pop-ups), all actuarially reduced based on age of beneficiary	70% spousal survivorship with no reduction in retiree's benefit	100% and 50% (with or without pop-ups), all actuarially reduced based on age of beneficiary	100% and 50% (with or without pop-ups), all actuarially reduced based on age of beneficiary
Benefit Eligibility - Other (Vested Rights, Disability, Death-in-Service)	5 years of service (vested and disability) 10 years of service, or age 55 with 5 years (death-in-service)	5 years of service (vested and disability) 10 years of service (death-in-service)	5 years of service (vested and disability) 12 years of service, or age 55 with 5 years (death-in-service)	5 years of service (vested and disability) 10 years of service, or age 55 with 5 years (death-in-service)
Disability Benefit	Unreduced, accrued benefit with minimum of 25% of AFC	Unreduced, accrued benefit with minimum of 25% of AFC, with children's benefit of 10% of AFC to maximum of 3 concurrently	Unreduced, accrued benefit with minimum of 25% of AFC	Unreduced, accrued benefit with minimum of 25% of AFC
Death-in-Service Benefit	Disability benefit or early retirement benefit, whichever is greater, with 100% survivorship factor applied plus children's benefits up to maximum of three concurrently	70% of accrued benefit with no actuarial reduction applied, plus children's benefit	Disability benefit or early retirement benefit, whichever is greater, with 100% survivorship factor applied plus children's benefits up to maximum of three concurrently	Disability benefit or early retirement benefit, whichever is greater, with 100% survivorship factor applied plus children's benefits up to maximum of three concurrently
Medical Benefits	80% of total premium	80% of total premium	80% of total premium	80% of total premium **#4(see the footnote at bottom of chart)**

If new to the membership of the Vermont State Retirement System on or after July 1, 2008, the following provisions are applicable to the Group F plan:

#1 60% of AFC

#2 Age 65 or a combination of years and service equal to 87

#3 Sliding scale for early retirement penalty based on years of service at retirement

#4 Pro-rated percentage of total premium based on years of service at retirement

Exhibit #2

VSTRS Group Comparison

Group Comparison	Group A	Group C
Employee Contributions	5.5% of gross salary	3.40% of gross salary
Benefit Formula	1.67% x creditable service	1.25% x service prior to 6/30/90 + 1.67% x service after 7/1/90
Maximum Benefit Payable	100% of AFC	50% of AFC
Average Final Compensation (AFC)	Highest 3 consecutive years, including unused annual leave, sick leave, and bonus/incentives	Highest 3 consecutive years, excluding all payments for anything other than service actually performed
Normal Retirement (no reduction)	Age 60 or with 30 years of service	Age 62 or with 30 years of service
Post-Retirement COLA	Full CPI, up to a maximum of 5% after 12 months of retirement	50% CPI, up to a maximum of 5% after 12 months of retirement or with 30 years
Early Retirement Eligibility	Age 55 with 5 years of service	Age 55 with 5 years of service
Early Retirement Reduction	Actuarial reduction	6% per year from age 62
Post-Retirement Survivorship Options	100%, 75%, and 50% (with or without pop-ups), all actuarially reduced based on age of beneficiary	100%, 75%, and 50% (with or without pop-ups), all actuarially reduced based on age of beneficiary
Benefit Eligibility - Other (Vested Rights, Disability, Death-in-Service)	5 years of service (vested and disability) 10 years of service, or age 55 with 5 years (death-in-service)	5 years of service (vested and disability) 10 years of service, or age 55 with 5 years (death-in-service)
Disability Benefit	Unreduced, accrued benefit with minimum of 25% of AFC	Unreduced, accrued benefit with minimum of 25% of AFC
Death-in-Service Benefit	Disability benefit or early retirement benefit, whichever is greater, with 100% survivorship factor applied, plus children's benefit up to maximum of 3 concurrently	Disability benefit or early retirement benefit, whichever is greater, with 100% survivorship factor applied, plus children's benefit up to maximum of 3 concurrently
Medical Benefits	80% of retiree's premium with 10 years of service	80% of retiree's premium with 10 years of service

Characteristics of State Public Pension Plans in New England

Category	Vermont	Maine*	New Hampshire	Connecticut	Massachusetts*	Rhode Island
Employee Contribution	5.10%	7.65%	5.00%	None	9% + 2% of pay above $30,000	8.75%
Employer Contribution	7.61%	17.01%	8.74%	4.9% (as of 6/30/05)	6.64%	18.40%
Benefit Formula	1.67% x years x Final Average Salary (FAS)	2% x years x Final Average Salary (FAS)	Age 60-64: 1.67% x year x Final Average Salary; age 65 and above: 1.5% x years x Final Average Salary (FAS)	1.33% + .5% for salary above Social Security breakpoint	2.5% x years x Average Final Salary (FAS)	[(1.6% x 1st 10 years) + (1.8% x 2nd 10 years) + (2% x years 21-25) + (2.25% x years 26-30) + (2.5% x years 31-37) + (2.25% x year 38)] x Final Average Salary (FAS)
Maximum Benefit Payable	60% of FAS	No Limit	100% of FAS	75% of FAS	80% of FAS	75% of FAS
Eligibility for Retirement	Age 65 OR any Rule of 87	Age 60 with 10 years of service; or age 62 with 5 years of service	Age 60 with any number of years of service	Age 62 with 5 years of service OR age 60 with 25 years of service	Age 65 with 10 years of service OR any age with 20 years of service	Age 59 with 29 years of service; or age 65 with 10 years of service
Post Retirement COLA	50% of CPI up to a maximum of 5%, compounded until 1/1/2013; full CPI with maximum of 5% thereafter	Full CPI up to 4%, compounded	Ad Hoc	60% of CPI, with minimum of 2.5% and maximum of 6%, compounded	Ad Hoc with 3% maximum for 1st $12,000 of benefits, compounded	CPI up to 3% after 3rd anniversary of retirement, compounded
Early Retirement Eligibility	55 with 5 years of service	Any age with 25 years of service	Age 50 with 10 years or service OR when age plus service = 70	Age 55 with 10 years of service OR at any age with 25 years of service	Age 55 with 10 years of service	Age 55 with 20 years of service
Early Retirement Penalty	Actuarial sliding scale	6% per year from normal retirement age	1.5% - 6.67%, depending on years of service	6% OR 4%, depending on years of service	0.1% in the formula multiplier for each year under age 65	Actuarially Reduced
Vesting Requirement	5 years of service	5 years of service	10 years of service	10 years of service	10 years of service	10 years of service
Actuarial Method	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal
Funding Ratio at 6/30/08	100.80%	73.90%	67.80%	53.30%	85.10%	53.40%
Assumed Interest Rate	8.25%	7.75%	8.50%	8.50%	8.25%	8.25%
Assumed Inflation Rate	3.25%	4.50%	3.50%	4.00%	3.50%	3.00%

Note: Maine and Massachusetts are not covered by Social security.

7/142009

Exhibit #4 – Characteristics of Teacher Public Pension Plans in New England

Characteristics of Teacher Public Pension Plans in New England

Category	Vermont	Maine*	New Hampshire	Connecticut*	Massachusetts*	Rhode Island
Employee Contribution	3.54%	7.65%	5.00%	6.00%	5.00% - 11.00%, depending on date of entry	9.50%
Employer Contribution	7.38%	16.72%	8.93%	15.28%	16.00%	19.64%
Benefit Formula	1.67% x years x Final Average Salary (FAS)	2% x years x Final Average Salary (FAS)	Age 60-64: 1.67% x year x Final Average Salary; age 65 and above: 1.5% x years x Final Average Salary (FAS)	2% x years x Average Final Salary (FAS)	2.5% x years x Average Final Salary (FAS); teachers who eleted into RetirementPlus and have 30 or more years receive an add'l 2% for years above 24	[(1.6% x 1st 10 years) + (1.8% x 2nd 10 years) + (2% x years 21-25) + (2.25% x years 26-30) + (2.5% x years 31-37) + (2.25% x year 38)] x Final Average Salary (FAS)
Maximum Benefit Payable	50% of FAS	No Limit	100% of FAS	75% of FAS	80% of FAS	75% of FAS
Eligibility for Retirement	Age 62 OR any age with 30 years of service	Age 60 with 10 years of service; or age 62 with 5 years of service	Age 60 with any number of years of service	Age 60 with 20 years of service OR any age with 35 years of service	Age 65 with 10 years of service OR any age with 20 years of service	Age 59 with 29 years of service; or age 65 with 10 years of service
Post Retirement COLA	50% of CPI up to a maximum of 5%, compounded	Full CPI up to 4%, compounded	Ad Hoc	Between 3% and 5%, depending on date of retirement, compounded	Ad Hoc with 3% maximum for 1st $12,000 of benefits, compounded	CPI up to 3% after 3rd anniversary of retirement, compounded
Early Retirement Eligibility	55 with 5 years of service	Any age with 25 years of service	Age 50 with 10 years or service OR when age plus service = 70	Age 60 with 10 years of service OR at any age with 25 years of service	Age 55 with 10 years of service	Age 55 with 20 years of service
Early Retirement Penalty	6% per year reduction from age 62	6% per year from normal retirement age	1.5% - 6.67%, depending on years of service	6% OR 4%, depending on years of service	0.1% in the formula multiplier for each year under age 65	Actuarially Reduced
Vesting Requirement	5 years of service	5 years of service	10 years of service	10 years of service	10 years of service	10 years of service
Actuarial Method	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal
Funding Ratio at 6/30/08	84.90%	73.90%	67.80%	63.00%	69.60%	53.40%
Assumed Interest Rate	8.25%	7.75%	8.50%	8.50%	8.25%	8.25%
Assumed Inflation Rate	3.25%	4.50%	3.50%	3.00%	3.00%	3.00%

Note: Maine, Massachusetts and Commmecticut are not covered by Social Security.

7/14/2009

The Sustainability Gap

Benefits are earned throughout a career rather than simply when are funds paid out to retirees. In order to meet these obligations, each system has developed a funding plan to accumulate monies, which, properly invested over time, will fund member retirements. The plans, when fully funded and operating under appropriate actuarial assumptions that correspond to demographic, economic, and workforce experience, and with manageable benefit design, have the effect of reducing volatility and providing the assurance that funds will be available to pay for benefits at member retirement.

As of the FY 2008 valuation, VSERS had an unfunded liability of $87.1 million while VSTRS had an unfunded liability of $379.5 million. The FY 2009 unfunded liabilities have increased to $326.5 and $727.8 million, respectively, significantly reducing the funding ratio to 80.9% for VSERS and 65% for VSTRS, down from 94.1% and 78.9% respectively.

The severe decline in the financial markets and subsequent economic recession has resulted in investment declines in Vermont as well as all other States. This has adversely impacted the funded status. While investments have triggered severe deterioration of funding levels, the problem has been brewing for some time in the form of an aging workforce, a baby boomer retirement bubble, longer life expectancies and a retirement benefit design that is not consistent with these trends.

As noted in a PBS Frontline report (Pernot, "Why Does Retirement Cost So Much?" May 16, 2006):

> "The driving force behind the growing cost of retirement is the fact that the baby boomers will spend more time in retirement than any previous generation. According to the Center for Disease Control, a 65-year-old can now expect to live another 18 years, on average. American seniors are living 50 percent longer than they were in the 1930s, when Social Security set 65 as the benchmark retirement age"

Investment losses and demographic pressures put additional budgetary pressures on the State at a time when Vermont faces fiscal stress from declining revenues, increasing unemployment and housing market declines. As noted by the Joint Fiscal Office, the recent history has been marked by significant revenue decline (JFO, "Vermont revenue Picture: Facing Vermont's Fiscal Challenges", November 17, 2009):

- 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 percent 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 percent decline.

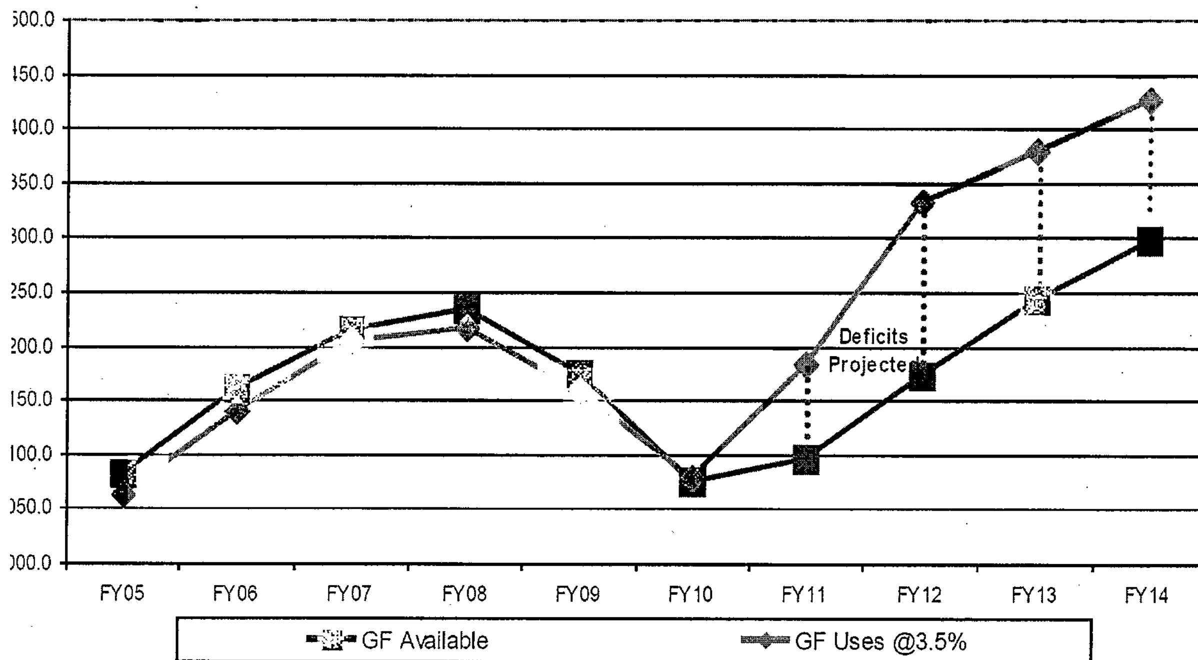
- Overall, since July 2007, total projected available General Fund revenue for FY 2010 decreased from $1,249 million to $1,026 million, an 18 percent decline.

- This was despite a $20 million increase in tax revenues for FY 2010 (during the last legislative session).

As noted by JFO, Vermont's FY 2010 total revenues are below those of FY 2005. While stimulus funds have provided some relief, Vermont has a long-term structural imbalance and will experience significant budget shortfalls that must be addressed by the Legislature and the Governor:

GF Budget Picture - Nov 09 - Projection thru FY14

Assumes 3.5% growth on FY10 base including ARRA,
(ARRA funds used to suppoprt GF Base in FY09=$75m, FY10=$175m, and FY11=$100m)
FY11 Gap solutions that are ongoing in nature will also impact out years



At the time this chart was developed by JFO the FY 2011 deficit was projected to be $88 million. That number is now closer to $150 million.

While an economic recovery and investment rebound would obviously be welcomed, this would not solve the problem. The States consulting actuaries were asked to complete an analysis bringing the assets of the VSERS and VSTRS forward at the assumed rates of return indicated at the top of each column, applying the so-called smoothing method used to determine the actuarial value of assets, and combining the results with the projected normal

cost and accrued liability of each system to show what the required state contribution for FY 2012 would be. The results show that even if the overall rate of return on assets in fiscal year 2010 substantially exceeds the assumed 8.25 percent rate of return, the FY 2012 required state contribution to both systems can be expected to exceed those developed in the most recent actuarial valuations. This is because additional portions of investment losses that have been not yet been recognized in the actuarial value of assets will have to be recognized in the 2010 valuation, and even a rate of return as high as 15 percent on the market value of each system's assets will not be high enough to offset them. At a positive 15 percent rate of return, well above the assumes actuarial rate of return of 8.25 percent, the unfunded liability for the VSERS system will again increase to $369,229,953 lowering the funding ratio even further to 77.41 percent. For VSTRS, the unfunded liability would increase to 813,954,713 and the funding ratio would drop to 63.28 percent. Also note that the unfunded liability is 133 percent of the projected payroll for the entire year for the VSTRS system. In the projections stated above, costs and liabilities are made using the actuarial assumptions employed in the valuation, so no positive or negative impacts of other actuarial assumptions (mortality, workforce separations, etc) are included.

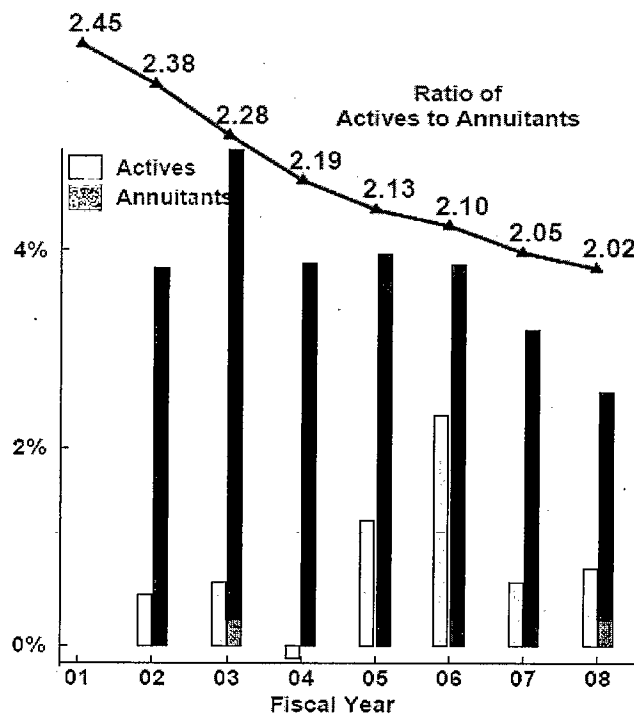
While investment markets have rebounded somewhat, assets of the retirement funds as of 12/31/09 are still 15 percent lower than the high water mark of 2007. Further there is no guarantee that the rebound will continue. In fact, as far as economic recovery is concerned, the Legislature's consulting economists (see Kavet, Rockler & Associates, "November 2009 Economic Review and Revenue Forecast Update", November 17, 2009) state that "real estate and housing markets will be slow to heal and remain credit-sensitive " and that risks to the forecast "are mostly on the downside."

Our actuaries estimate that it will take more than twenty years at our current actuarial investment rate of return of 8.25 percent to get back to fiscal year 2008 funding level. This rate may be a difficult benchmark, especially if the aging workforce and increased benefit payments, as noted in the next section, create a need to move to a higher percentage of liquid assets. It would not be prudent to rely on future market returns above the assumed rate of return to solve the problem.

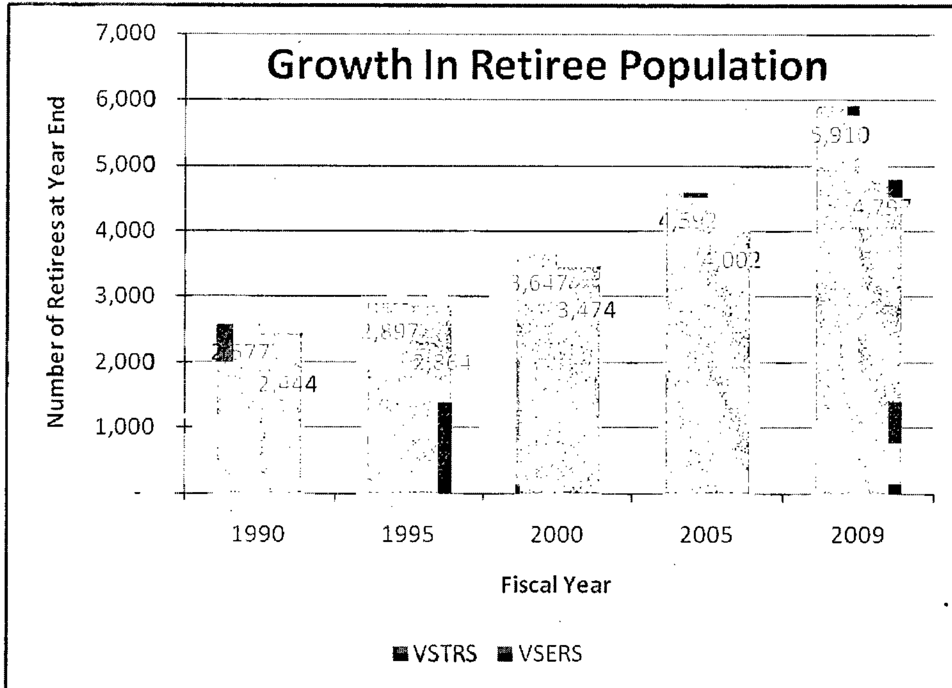
Vermont significant budgetary pressures and must respond to them in a deliberate and measured way to maintain the integrity of its retirement systems. Without immediate intervention, the costs to support the existing plans may go well beyond state government's ability to find additional tax resources or expenditure cuts.

Demographics of Aging

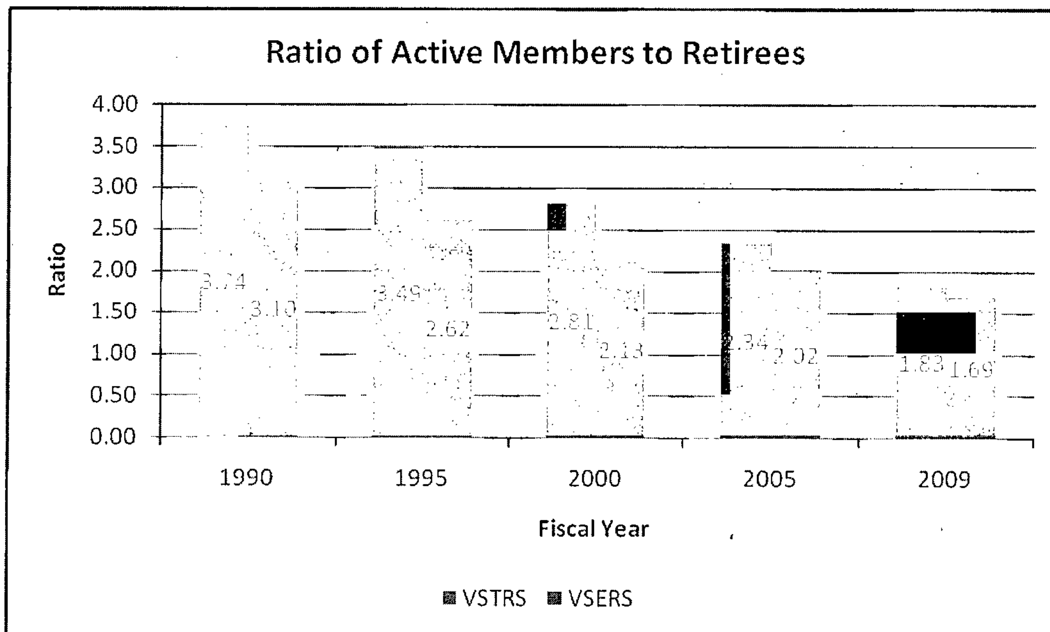
One important demographic trend placing additional stresses on the pension systems is the aging of the workforce and increased life spans of retirees. In the 2008 Public Fund Survey, the National Association of Retirement Administrators noted that "the rate of growth in annuitants has been outpacing the rate of growth in active (working) members (NASRA, Public Fund Survey of Findings FY 08, October 2009). As noted in the graph provided by NASRA, the ratio of actives to annuitants has declined from 2.45 in FY 2001 to 2.02 in FY 2008:



The Wisconsin Legislative Council's 2008 Comparative Study of Major Public Employee Retirement Systems issued in December 2009 showed declining ratios of active to retired participants. According to published reports, 47 of the 87 systems surveyed had an active employees-to-retired-employees ratio of less than two, as compared to 17 of the systems in the 2000 report (Plan Sponsor, "Public Plans' Number of Retirees Growing Faster than Active Participants", December 24, 2009). Vermont has a similar trend. Both the VSERS and VSTRS retiree populations are growing, due to increasing numbers of retirees and the fact that people are living longer.



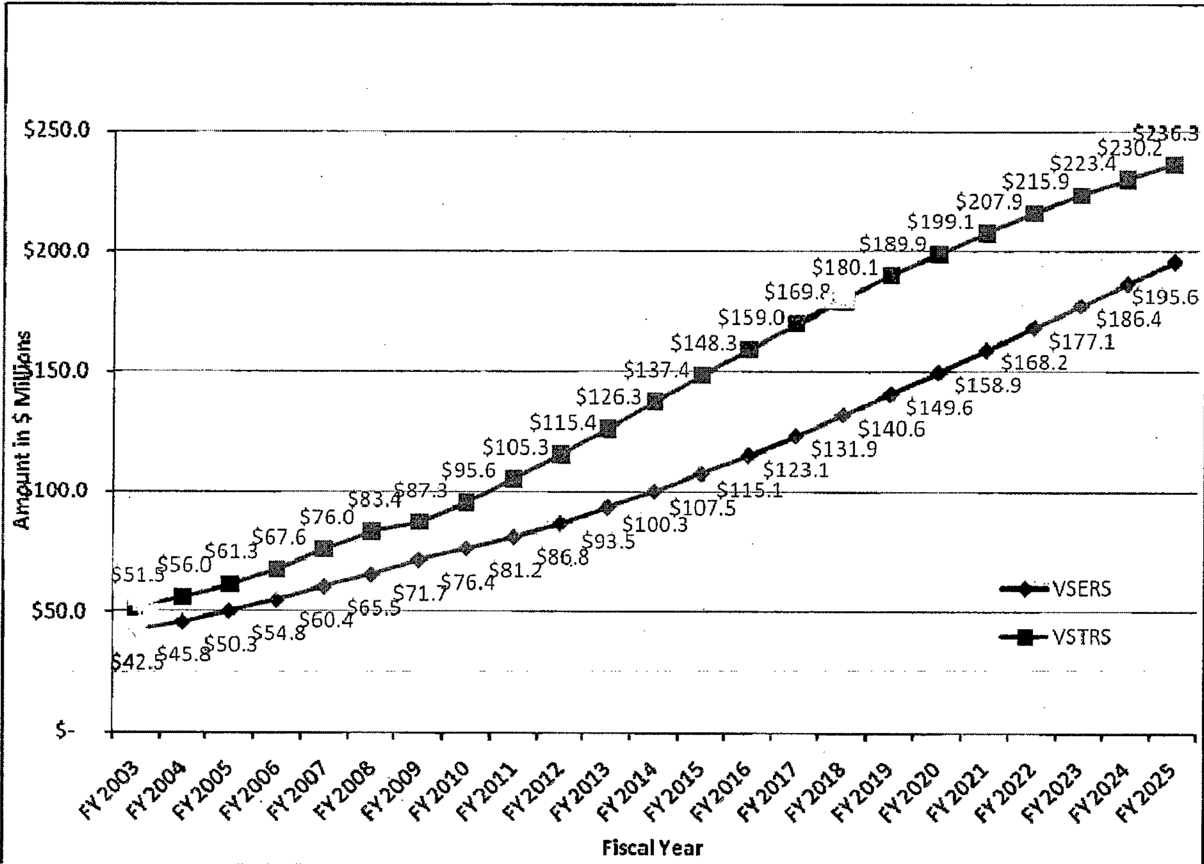
In addition, the ratio of active members to retirees is decreasing:



Unlike a "pay-as-you-go" plan such as Social Security, the actuary takes this in account when developing models to prefund benefits. However, the increasing trend may get ahead of actuarial mortality assumptions, creating actuarial losses. In addition, these trends are indicative of a maturing plan and can make it more difficult to achieve the objectives of full

funding, not just for the pension plan but especially for the severely underfunded OPEB plans. It also creates more volatility in employer contribution rates. Further, as more funds are needed for benefit payments, a trend readily apparent in Vermont, the systems have a greater negative cash flow (benefit payments exceed contributions), requiring more liquid assets to fund these payments. This creates a greater likelihood of adjustments to asset allocation plans which could adversely impact assumed and actual investment rates of return.

Pension Benefit Payouts: Actual and Projected



Review of Recommendations

The National Context

In reviewing these recommendations, it should be noted that this crisis is not unique to Vermont and that many other States are taking action, some quite similar to Vermont. A December 2009 publication by the NCSL notes that, "over the years from 2005 through 2009, 18 states have enacted such changes to reduce long-term costs of retirement plans." More changes are on the way. As noted by the National Conference Public Employment retirement Systems (NCPERS) and the NSCL:

> "The principal theme in pension legislation in 2009 was the need to make future pension costs manageable in the light of states' straitened fiscal circumstances and the losses most retirement trust funds have experienced. Few benefit increases were enacted, and reductions in various forms appeared in a number of states." (NCPERS, Pension and Retirement Plan Enactments in 2009 State Legislatures, 2009)

Consistent with Vermont's analysis of the funding, economic, and demographic issues, the NCSL notes that:

> "Even if financial markets improve, and help retirement trust funds recover, the state fiscal crisis, political and demographic issues will continue their stress on retirement systems.... I'd expect additional states to make the kinds of changes I have reported for 2009--broad programs of increases in employee and employer contributions; higher age and service requirements for retirement; smaller post-retirement benefit increases." (NCSL, Presentation, Fiscal Leaders Seminar, December 10, 2009).

The National Association of Retirement Administrators recently compiled a list of "Responses to 2008 Market Decline and Rising Pension Costs." (copy is included in the appendices to this report.) Based on that report and the NSCL studies, some efforts consistent with those of Vermont are evident as well as some that go further than recommended by the Commission. The list below is illustrative rather than comprehensive.

- Study Commissions:
  - Several states (Illinois, Kansas, Maine, Montana, Nebraska, New Mexico, North Carolina), along with Vermont, have formal commissions studying the entire structure of all their state retirement plans this fall.

- Other states, including Rhode Island and New Hampshire, have completed studies recently and have implemented some changes as a result.

➢ Employee Contributions:
  - New Mexico, Nebraska, Kentucky, Idaho, and Texas increased required employee contributions for current employees.
  - Connecticut, Nevada, and New Hampshire raised contribution rates for future employees.
  - In Nebraska, beginning September 1, 2009, the school employees' contribution rate increased from 7.28 percent to 8.28 percent.
  - The Colorado PERA Board, an Iowa Legislative Committee, and the Minnesota Teachers' Retirement Association, have recommended increases to employee and employer rates.
  - The legislature is expected to consider higher employee and employer contributions in Wyoming.

➢ Benefit or Age of Retirement Date Changes:
  - A number of states reduced benefits in conjunction with new-hires after a prescribed date. Changes included adjustments to COLAs, raising the age of normal and early retirement, changes to vesting, increasing years for FAS calculations, and others.
  - Louisiana and Rhode Island reduced post retirement benefits for existing state employees.
  - The Rhode Island changes are estimated to save in the neighborhood of $50 million in general fund expenditures in FY 2010.

As noted previously, our consulting actuaries maintain that recovery is a long-term proposition. Our actuaries estimate that it will take more than 20 years at our current actuarial investment rate of return 8.25% to get back to Fiscal Year 2008 funding levels. Some have suggested that we wait out the current downturn and re-assess the landscape in a year or two. The longer we wait, the worse the problem and the more severe the ultimate fix.

Specific Recommendations of the Commission

<u>**CATEGORY: General Framework**</u>

RECOMMENDATION ONE: Make no change to the following.

- Pension or retiree health benefits for those already retired.

- Pension or retiree health benefits for anyone close to retirement, which the Commission defined as within five years of eligibility for a particular benefit.

It should be noted that "five years from normal retirement eligibility" for purposes of these recommendations means the member must be either 5 years or less from normal retirement age for their group plan, or have a minimum of 25 years of service as of the date the retirement legislation is enacted. If a member has begun making a purchase of service that is documented in the system prior to December 31, 2009, the total years of service being purchased may count toward the total years of service as of the effective date of the legislation. No service that is initiated after January 1, 2010, will count toward total creditable service as of the effective date.

- Basic provisions (maximum benefit, multiplier, COLA, etc.) that would make the plans less competitive than the mainstream of other state public systems.

RECOMMENDATION TWO: Do not replace the current defined benefit plan and transition to a defined contribution plan.

The Commission did discuss and consider the possibility of a transition from the current defined benefit plans for all teachers and most state employees to a defined contribution or cash balance type plan. Telephone dialogues took place with retirement officials in other states with experience in this area. These states included Florida which currently offers both a defined benefit and defined contribution plan to employees, Nebraska which moved after many years from a defined contribution plan to a cash balance plan, and West Virginia which has moved back and forth between defined contribution and defined benefit plans on more than one occasion.

Proponents of a defined contribution/cash balance approach point out that the employer and employee contribution rates are more stable and predictable, that these plans provide greater portability for employees, that few employees in the private sector have access to defined benefit plans, and that in the long run defined contribution/cash balance plans can be expected to be less expensive for the employer (State).

Opponents of defined contribution/cash balance plans believe that they provide less retirement security for employees, shift financial risk from the employer to employees, cost more in the near and intermediate term as employers maintain two systems for many years, are less attractive to employees, and are less efficient or effective from an investment perspective.

The majority of the Commission chose not to recommend adoption of a defined contribution/cash balance plan for teachers or state employees at this time. The majority did recommend further consideration of this issue in the future.

RECOMMENDATION THREE: Full funding of Pension ARC.

The Commission recommends that the Legislature and the Governor continue to fully fund the annual actuarially required contribution (ARC) for the state and teachers' pensions as calculated after any or all recommendations made below are enacted. While budget constraints may

create pressures to reduce or limit full funding, continued discipline in fully funding the ARC is critical to the long-term sustainability of the pension funds. "Rate holidays" or other forms of underfunding do not address the real problem and only exacerbate the fiscal stresses because lost investment opportunity will increase future funding needs, hitting strapped budgets even harder. Beyond the harm to the pension fund, it could potentially impact the State's credit rating. As noted by Moody's Investors service (Special Comment: Employee Pension Costs Pressure State and Local Governments, November, 2009):

" A broad deterioration in funding levels for public sectors adding to fiscal pressure on some state and local governments could contribute to negative rating actions for select issuers in the next several years ... The problem for some issuers will be exacerbated by decisions by select governments to defer pension contributions during periods of budgetary stress... A reduction in plan contributions would not appear consistent with the challenging environment in which most pensions presently exist (underline added)."

While the Commission believes that the significant recommendations included in this report are necessary to preserve the stability and the integrity of the pension systems, these actions are fair to taxpayers and members of the system only if the State meets its obligations. If the plan is to be sustained, all parties must share the pain and meet their obligations.

RECOMMENDATION FOUR: Fund OPEB Obligations.

To date, the VSERS OPEB plan has set aside just over $5.7 million against an OPEB liability of $775 million. The teachers' system has no assets but has an unfunded actuarial liability of $872.2 million. Unlike the state system where the "pay-as-you-go" portion is budgeted and funded in a separate OPEB Trust fund, the health care expenses for VSTRS are paid out of the pension fund and are treated as an actuarial loss to the system, creating additional financial stresses on the pension system. While there was no consensus on a solution to this issue, the treatment of teacher health care is reviewed below, in the "Review of Outstanding Issues" section of the report.

Health care costs over the last decade or more have risen at a much higher rate than the rate of inflation, and while some stabilization of that trend is expected, costs are projected by our actuaries to continue to exceed CPI. The situation for the teachers' health care payments is reaching a critical phase.

The Retirement Commission unanimously voted to include a recommendation to the Legislature to develop, without delay, a structural plan and process to fund the OPEB obligations and set money aside in a material way in a separate, independent funding mechanism.

CATEGORY: Pension Plan Recommendations

RECOMMENDATION FIVE: Revisions to Normal and Early Retirement Ages.

Background Discussion: Normal retirement is defined as the age, number of years of service, or both, that a member must attain in order to qualify for full retirement benefits without an actuarial reduction to the pension. In addition to stand alone age or service requirements, some plans have adopted "Rule of X" requirements under which a person can retire with normal retirement benefits through attainment of that number through a combination of years of service and age. For the majority of State employees (Group F) and teachers (Group C), normal retirement is currently age 62 years or retirement at any age with 30 years of service. Under legislation enacted in fiscal year 2008, VSERS Group F benefits were modified so that the eligibility condition for an unreduced benefit changed from the attainment of age 62 or 30 years of service to a "Rule of 87."

As noted in the previous sections of this report, demographics are changing; people are living longer and they are able to contribute to the workforce later in life. They are a valuable resource to governments and educational institutions as these employees provide valued institutional knowledge and experience in the workplace. From a pure pension economics standpoint, the maturing of a pension system, as evidenced by the declining ratio of active members to retirees, creates additional volatility and strains on pension systems, especially during periods of financial stress. The extension of the years at which an individual may retire with unreduced benefits has a significant impact on the fiscal health of the system, as funds may be invested for longer periods of time and the total disbursements over the span of the retirement will be less.

In the case of early retirement, where an individual commences receipt of retirement benefits prior to the attainment of normal retirement eligibility, the pension is reduced from the amount that would have been received if the person had reached the normal retirement requirements. This is done to maintain system health as, at least in theory, the retiree would receive a benefit that is cost neutral, i.e., is not subsidized by contributions of other members. It also is an equity issue in that the adjustment should create an "equivalent benefit." Since the Commission is extending normal retirement, the recommendation is also made to create a similar pattern for early retirement. In addition, the Commission recommends using full actuarial reductions rather than percentages or factors that may not fully address the need to achieve a cost neutral impact. This does not create savings for the pension plan, in that the member is accruing additional benefits for that same time, but it does create additional OPEB savings (health care).

Recommendation

State Group F and Teachers' Group C:

- Raise normal retirement age from 62 or 30 years at any age to 65 or rule of 90 (combination of age and years of service) for those more than five years from normal retirement eligibility.

- Raise the early retirement age from 55 to 58 for those more than five from early retirement eligibility.

State Group D:

- Raise normal retirement age from age 62 to age 65 for those more than five years from normal retirement eligibility.

State group C:

- Raise the early retirement age to 52 from 50 for those more than five years from early retirement eligibility.

RECOMMENDATION SIX: Lengthening the salary compensation period (average final compensation).

Background Discussion: For defined benefit systems, the final average salary used in conjunction with a "multiplier" to calculate the pension benefit, is generally the member's highest earnings over a specified number of years. Sometimes there is a requirement that the years be consecutive; in some systems the highest years are used. In most, but not all, the member's highest salary will be the amount of salary he or she earned immediately prior to retirement. The VSERS Group F and VSTRS Group C members currently have a three highest consecutive years requirement. The Wisconsin Legislative Council released its biannual "2008 Comparative Study of Major Public Employee Retirement Systems" in December 2009. It notes that 55 of the 87 plans it surveyed used some form of a three-year model, the next most utilized average being five years (by 18 of the 87 plans). A review of recent legislative initiatives summarized by NCSL and NCPERS indicate recent efforts by several states to move to a longer compensation period. These reduce the impact of significant increase in the compensation of members in the last year or two of service, which may or may not be intended to increase pension benefits and more accurately reflect the wage earnings over an extended period.

<u>**Recommendation**</u>

State Group F and Teachers' Group C:

- Use a five-year compensation period instead of a three-year period to calculate benefits for those more than five years from retirement eligibility.

State Group C:

- Use a three-year compensation period instead of a two-year period to calculate benefits for those more than five years from retirement eligibility.

State Group D:

- Use a two-year compensation period instead of final salary to calculate benefits for those more than five years from retirement eligibility.

The following are sample calculations for various groups to demonstrate the difference in an average monthly benefit that would result from the changes in the AFC calculation changes as recommended. These examples do not reflect any of the other changes that are being contemplated.

Vermont State Teachers' Retirement System

Group C Plan

Example #1: 16.821917 years of service

3 year average = $58,827; annual maximum benefit = $16,524

5 year average = $56,366; annual maximum benefit = $15,840

Difference = **$684** annually

Example #2: 33.00 years of service

3 year average = $72,889; annual maximum benefit = $36,192

5 year average = $70,214; annual maximum benefit = $34,860

Difference = **$ 1,332** annually

Vermont State Retirement System

Group F Plan

Example #1: 16.346153 years of service

3 year average = $77,432; annual maximum benefit = $21,137

5 year average = $74,129; annual maximum benefit = $20,236

Difference = **$901** annually

Example #2: 40.24359 years of service

3 year average = $43,255; annual maximum benefit = $21,628

5 year average = $41,183; annual maximum benefit = $20,592

Difference = **$1,036** annually

Group C Plan

Example: 26.339726 years of service

2 year average = $124,928; annual maximum benefit = $62,464

3 year average = $117,306; annual maximum benefit = $58,653

Difference = **$3,811** annually

Group D Plan

Example: 31.281119 years of service

Final salary = $128,827; annual maximum benefit = $128,827

2 year average = $127,786; annual maximum benefit = $127,786

Difference = **$1,041** annually

RECOMMENDATION SEVEN: Increasing the Maximum Benefit.

Background Discussion: The maximum benefit establishes limit on the amount of pension benefits that may be received by a retiree. Increasing this cap would provide an opportunity for increased benefits to employees who choose to work more than thirty years. Right now most teachers and state employees are capped at their maximum retirement benefit of 50 percent of average final compensation (AFC) after 30 years of service (exception is VSERS Group F members hired after 7/1/08). With this change members would receive 60 percent of AFC after

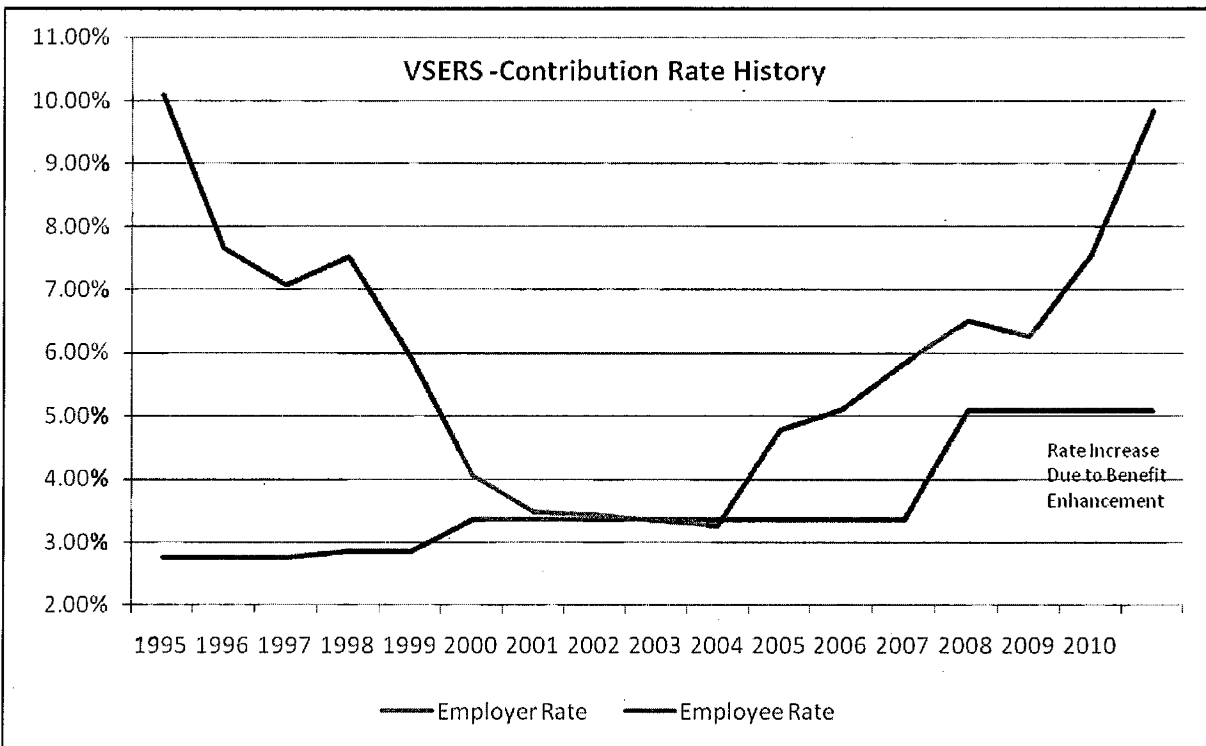
36 years of service. The overwhelming majority of public plans have higher caps than 50%; many with no cap at all. This would have the result of rewarding longer service and provide some mitigation to both the AFC change and the adoption of the "Rule of 90" for normal retirement. Group F members hired after 7/1/08 currently have the 60 percent cap.

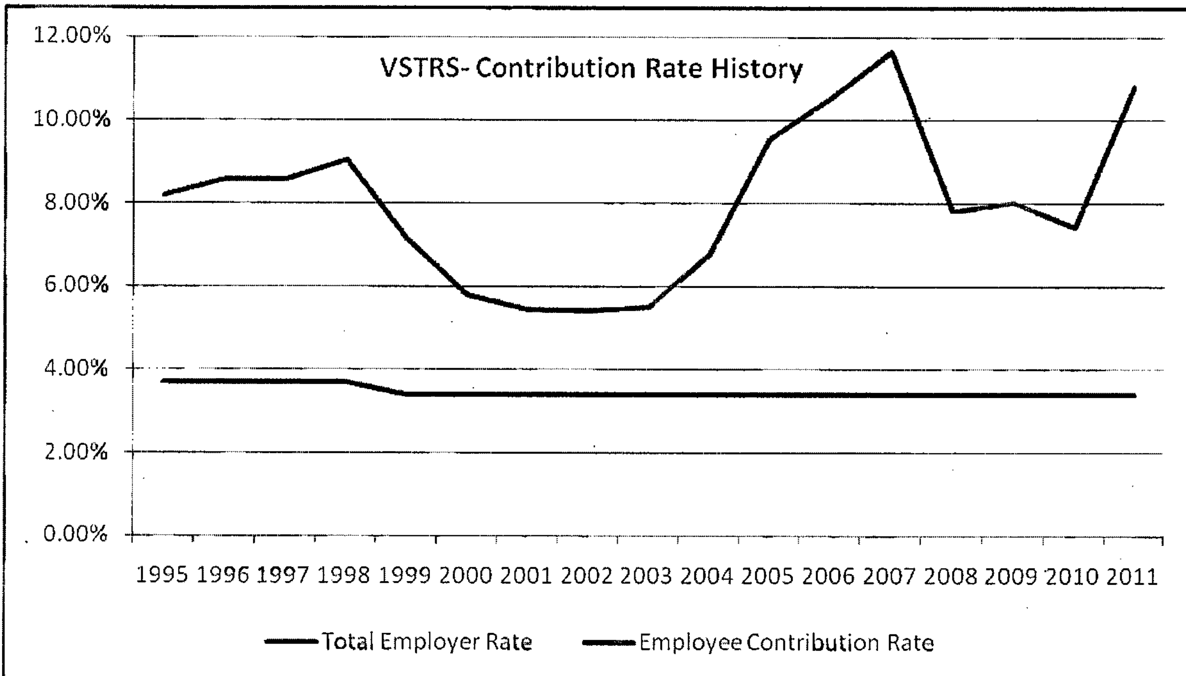
Recommendation

Increase the maximum benefit from 50% to 60% of final compensation for State Group F and Teachers' Group C for those more than five years from retirement eligibility.

RECOMMENDATION EIGHT: Revising the contribution rate ratio and rates for employer and employees.

Background Discussion: While contribution levels for state employees and teachers have remained constant in recent years, the State's share, represented as a percentage of payroll, is much more volatile and generally represents a more significant share of the contribution to the pension benefit.





The Commission is recommending employment of a "risk sharing" approach to the payment of necessary contributions to fund the system in FY 2011 and subsequent years. Essentially, the total contributions required to meet the funding needs of the system would be calculated by the actuary on an annual basis. This would include the employer and employee contributions. The additional need over the previous year's base, or in optimum economic climates, reductions to contributions, would be spread across both employer and employees' estimated contributions. Instead of having a fixed employee contribution rate set in statute, with the State/employer contribution rate floating on an annual basis, the Commission recommends a proportional contribution system between the State and employees/teachers. This would require both employers and employees to pay the established percentage of the increased costs of pension benefits that result in market downturns or when other variables that result in performance that do not meet assumed actuarial experience. When actuarial experience is exceeded, the contribution rate for both employers and employees would go down. It is important to remember that rate/risk sharing creates a partnership; employer and employee contributions will rise and fall in tandem. Both parties will have a stake in keeping benefit, administrative, and other costs in check.

As part of its review the Commission studied a number of rate sharing options and their impacts on the employer ARC and employer and employee rates, incorporating all other pension recommendations above. These are summarized on the next page.

Preliminary Projected Fiscal Impact Summary: Commission Recommendations to Pension Plans

VSTRS –	Employer ARC	Employee Contribution %	State Contribution
FY 2010 actuarial recommendation & appropriation:	$41.5 million	3.4%	7.4%
FY 2011 actuarial recommendation, no changes:	$63.5 million	3.4%	10.8%
FY 2011 recommendation, changes, no cost sharing	$56.7 million	3.4%	9.67%
FY 2011 recommendation, changes, 3.5% state increase	$43.0 million	5.47%	7.32%
FY 2011 recommendation, changes, 50/50 sharing*:	$50.1 million	4.25%	8.53%
FY 2011 recommendation, changes, 50/50 sharing**:	$37.5 million	6.39%	6.39%
FY 2011 recommendation, changes, 60/40 sharing***:	$45.0 million	5.11%	7.67%

Changes = Normal retirement at 65/rule of 90, early retirement at 58 with actuarial equivalent reduction for early commencement, lengthening salary averaging period from three years to five years, increase in maximum benefit from 50% to 60% of FAS; changes not applicable to those presently within five years of normal retirement (for early retirement change, exclusion applies to those now within five years of early retirement eligibility).

Sharing:
* 50/50 using FY 2010 as baseline (based on changes above)
** 50/50 of total required contribution (based on changes above)
*** 60/40 of total required contribution (based on changes above)

VSERS –	Employer ARC	Employee Contribution %	State Contribution %
FY 2010 actuarial recommendation & appropriation:	$32.0 million	5.1%	7.6%
FY 2011 actuarial recommendation, no changes:	$41.6 million	5.1%	9.8%
FY 2011 recommendation, changes, no cost sharing	$36.4 million	5.1%	8.62%
FY 2011 recommendation, changes, 3.5% state increase	$33.1 million	5.83%	7.84%
FY 2011 recommendation, changes, 50/50 sharing*:	$34.3 million	5.56%	8.11%
FY 2011 recommendation, changes, 50/50 sharing**:	$28.9 million	6.84%	6.84%
FY 2011 recommendation, changes, 60/40 sharing***:	$34.7 million	5.47%	8.20%

Changes = Normal retirement at 65/rule of 90, early retirement at 58 with actuarial equivalent reduction for early commencement, lengthening salary averaging period from three years to five years for Group F, from two to three for Group C, and from final salary to two years for state Group D, increase in maximum benefit from 50% to 60% of FAS; changes not applicable to those presently within five years of normal retirement (for early retirement change, exclusion applies to those now within five years of early retirement eligibility).

Sharing:
* 50/50 using FY 2010 as baseline (based on changes above)
** 50/50 of total required contribution (based on changes above)
*** 60/40 of total required contribution (based on changes above)

The results of application of these rates to an employee's pay will vary depending on the rate of pay and the rate configuration adopted. Ranges of impact by various rate sharing strategies are as follows:

VSERS

Employee Contribution

	Baseline	Tied to 3.5% State Increase	50/50 using 2010 as baseline	50/50 sharing of total	60/40 sharing of total
	5.10%	**5.83%**	**5.56%**	**6.84%**	**5.47%**
Salary					
$30,000	$1,530	$1,749	$1,668	$2,052	$1,641
$35,000	$1,785	$2,041	$1,946	$2,394	$1,915
$40,000	$2,040	$2,332	$2,224	$2,736	$2,188
$45,000	$2,295	$2,624	$2,502	$3,078	$2,462
$50,000	$2,550	$2,915	$2,780	$3,420	$2,735
$55,000	$2,805	$3,207	$3,058	$3,762	$3,009
$60,000	$3,060	$3,498	$3,336	$4,104	$3,282
$65,000	$3,315	$3,790	$3,614	$4,446	$3,556
$70,000	$3,570	$4,081	$3,892	$4,788	$3,829

VSTRS

Employee Contribution

	Baseline	Tied to 3.5% State Increase	50/50 using 2010 as baseline	50/50 sharing of total	60/40 sharing of total
	3.40%	**5.47%**	**4.25%**	**6.39%**	**5.11%**
Salary					
$30,000	$1,020	$1,641	$1,275	$1,917	$1,533
$35,000	$1,190	$1,915	$1,488	$2,237	$1,789
$40,000	$1,360	$2,188	$1,700	$2,556	$2,044
$45,000	$1,530	$2,462	$1,913	$2,876	$2,300
$50,000	$1,700	$2,735	$2,125	$3,195	$2,555
$55,000	$1,870	$3,009	$2,338	$3,515	$2,811
$60,000	$2,040	$3,282	$2,550	$3,834	$3,066
$65,000	$2,210	$3,556	$2,763	$4,154	$3,322
$70,000	$2,380	$3,829	$2,975	$4,473	$3,577

Employee contributions in both systems are pre-tax contributions under Section 414(h) employer pick-up provisions and will therefore reduce the member's tax liability while he or she is employed.

Recommendation

The Commission chose to recommend a sharing of the total annual contribution, with the State share capped at the 3.5 percent growth target to accommodate the expenditure growth rate target of the Joint Fiscal Committee.

Cost Impacts of Pension Recommendations

Buck Consultants analyzed the Commission's recommendations to determine their financial and actuarial impacts of the above recommendations. The pension recommendations above, if adopted, would cut the FY 2011 actuarially required contributions for the State pension system from the actuary's recommendation of $41.6 million to $33.1 million and for the Teachers' pension system from $63.5 million to $43.0 million, a combined reduction of $29 million or 28%, and would produce significant savings for many years. Of the $29 million reduction in the State's FY 2011 contribution, $12 million results from benefit revisions and $17 million comes from increased employee contributions. The impact of the various recommendations, excluding the rate sharing, is outlined for each system below.

Summary of Fiscal Impacts: VSERS Recommendations

	Baseline Before Recommendations	Individual Components of Recommendation				Combined Recommendation Package Without Rate Sharing
		Age 65 or Rule of 90	Early Retirement & Rule of 90	Recommended Changes to AFC	60% Salary Cap	
NORMAL COST EMPLOYER	$23,334,122	$19,236,962	$20,205,997	$21,075,233	$23,392,634	$19,110,506
ACCRUED LIABILITY	1,544,144,066	1,506,950,166	1,505,921,599	1,529,292,721	1,563,452,860	1,512,825,881
UNFUNDED LIABILITY	326,506,488	289,312,588	288,284,021	311,655,143	345,815,282	295,188,303
FY 2011 ARC	$41,581,656	$36,290,324	$36,407,795	$39,441,225	$43,759,841	$36,449,613

Summary of Fiscal Impacts: VSTRS Recommendations

	Individual Components of Recommendation					
	Baseline Before Recommendations	Age 65 or Rule of 90	Early Retirement & Rule of 90	Recommended Changes to AFC	60% Salary Cap	Combined Recommendation Package Without Rate Sharing
NORMAL COST EMPLOYER	$22,828,834	$18,896,875	$19,777,164	$21,655,115	$23,357,007	$18,838,189
ACCRUED LIABILITY	2,101,837,843	2,040,655,962	2,059,100,549	2,083,298,780	2,120,003,744	2,051,972,216
UNFUNDED LIABILITY	727,758,506	666,576,625	685,021,211	709,219,443	745,924,407	677,892,878
FY 2011 ARC	$63,501,219	$56,175,450	$58,061,082	$61,291,404	$65,044,634	$56,723,725

The current column is the baseline for comparative purposes, based on the FY 2009 actuarial valuation and represents the FY 2011 actuarially required contribution absent any recommended changes. Each component of the recommendations was analyzed to approximate its individual impacts. Independently, each of these recommendations has an impact, but they are interdependent and change as each component impacts others. The actuary then ran a hypothetical model with all of the above pension recommendations to ascertain a combined savings, prior to rate sharing.

In FY 2011, the savings for the pension recommendations above (excluding rate sharing) are $5,132,043 for VSERS and $6,777,494 for VSTRS. The largest single impact for each system is the adoption of the age 65 or "Rule of 90" for normal retirement. Early retirement changes as recommended do not add savings on the pension side, and in fact add costs, but create offsetting savings in the tiered health care OPEB scenario described below. In the case of VSERS, the proposed extension of the average final compensation and the 60 percent maximum cap basically offset each other, while there is a net gain to the system of approximately $666,000 in the VSTRS system.

The combined recommendation would also reduce the liability in future years. While this is an extrapolation based on the current actuarial valuations, adoption of these recommendations would result in savings over the baseline of approximately $6.2 million in 2015 and $7.7 million in 2020 for VSERS and, for the same years, $8.1 million and $10.3 million for VSTRS.

If rate sharing is applied as recommended by the Commission, with a 3.5 percent employer cap, approximately $17 million is reduced from the employer ARC. In addition, other possibilities reviewed by the Commission are also noted:

	VSERS Employer ARC	VSTRS Employer ARC	Total Combined ARC
FY 2010 actuarial recommendation & appropriation	$32.0 million	$41.5 million	$73.5 million
FY 2011 actuarial recommendation, no changes:	**$41.6 million**	**$63.5 million**	**$105.1 million**
FY 2011 recommendation, changes, no cost sharing	$36.4 million	$56.7 million	$93.1 million
FY 2011 recommendation, changes, 3.5% state increase*	**$33.1 million**	**$43.0 million**	**$76.1 million**
FY 2011 recommendation, changes, 50/50 sharing**:	$34.3 million	$50.1 million	$84.4 million
FY 2011 recommendation, changes, 50/50 sharing***:	$28.9 million	$37.5 million	$66.4 million
FY 2011 recommendation, changes, 60/40 sharing****:	$34.7 million	$45.0 million	$79.7 million

Notes:
*3.5% State ceiling increase configuration is recommended by the Commission

** 50/50 using FY 2010 as baseline (based on changes above)
*** 50/50 of total required contribution (based on changes above)
**** 60/40 of total required contribution (based on changes above

CATEGORY: Health Care Recommendations

RECOMMENDATION NINE: A Tiered Medical Premium Copayment Structure.

Background Discussion: Under the State System, members may continue their medical coverage for themselves and all eligible dependents in retirement for the remainder of their lifetime, and only pay 20 percent of the premiums for all covered lives. The only stipulation is that the member must be eligible to draw their pension immediately upon separation of service, meaning that they must be at least age 55 and have at least 5 years of service. The only deviation to this configuration is for Group F members whose membership began in the system on or after 7/1/2008. For those members, a "tiered health" plan is in place, based on years of service at retirement. The State pays 80 percent at 20 years, 60 percent at 15 years, and 40 percent at 10 years.

In the Teachers' System, a member must have a minimum of 10 years of service at retirement, and they will receive 80 percent of their premium paid by the system, based on the standard medical plan. The retired teacher must pick up the full premium for all covered dependents.

Under the scenarios above, a retiree receives 80 percent of their medical premium paid by the system for the remainder of their life, with as little as 5 years of service. This is very generous and very expensive to the respective systems. It is not only more affordable but fairer for the percentage of the system's subsidy to be tied to the number of years of service accrued by the member. This method not only rewards longevity, but mirrors the way that pension benefits

are calculated by providing long-term members with a higher benefit than short-term members.

The Commission explored a number of health care options centering on the concept of applying a tiered health care system for all members of both systems new tiered system would apply to all of those not within five years of eligibility to draw this benefit. Possible tiers included:

30 percent - 10yrs	50 percent - 15 yrs	70 percent - 20 yrs
40 percent - 10yrs	60 percent - 15 yrs	80 percent - 20 yrs
40 percent - 10yrs	60 percent - 20 yrs	80 percent - 30 yrs

The Commission also considered not allowing access to the health benefit until age 60 or age 65.

Recommendation

The Commission recommends a tiered medical premium copayment structure based on length of service. Instead of the current straight 80/20 split of retiree health insurance premiums utilized for most retired teachers and state, a new tiered system would apply to all of those not within five years of eligibility to draw this benefit.

The new employer share for the tiered system would be:

40 percent - 10yrs	60 percent - 20 yrs	80 percent - 30 yrs

RECOMMENDATION TEN: Provide the Ability to "Recapture" the Retiree Health Benefit.

Background Discussion: For most VSERS employees (with the exception of Group F employees hired after 7/1/08) and group C members there is no access or "recapture" if you do not carry state insurance at the time you retire. Therefore if you leave state service but do not retire until a later date, you cannot recapture this benefit in the VSERS system. In the VSTRS system, members currently have the recapture option available with ten years of service but do not have spousal coverage. Providing a recapture option was seen as consistent with rewarding longevity and was viewed as a more equitable treatment for members.

Recommendation

The Commission recommends providing the ability to "recapture" the retiree health benefit to those with 20 or more years of service when they begin drawing benefits. This opportunity is not currently allowed for state employees and is allowed for teachers with 10 or more years of service.

Cost Impacts of Health Care Recommendations

The charts below are based on analyses prepared by Buck consultants to identify the impacts of these changes on both the cash expenditure (pay-as-you-go costs) for health and the development of the OPEB ARC, incorporating full accrual. The following analyses also incorporate, as assumptions, the recommended changes to normal and early retirement described above.

For both systems, the pay-as-you-go does not change appreciably, if at all, in the early years, although there are some savings as you get further out in years. The addition of spousal coverage adds additional financial stresses to the current pay-as-you-go expenditures and is not affordable, given the current lack of appropriations to support teacher health care expenses, without an offsetting increase to employee contributions.

The impact on the ARC is, however, much more significant. Assuming limited prefunding for VSERS and no prefunding for VSTRS, there are sizeable savings on a full actuarial accrual basis in FY 2011, $15.4 million for VSTRS and $6.6 million for VSERS with greater savings in the out years.

VSERS Tiered health Care at 40%, 60% and 80% at 10, 20 and 30 years of service				
	Baseline		**For employees > 5 yrs from retirement**	
	w/o recapture	**w/ recapture**	**w/o recapture**	**w/ recapture**
Total Active Member Liability	468,333,367	491,204,926	433,396,102	**449,515,273**
Retiree Liability	312,414,941	312,414,941	312,414,941	**312,414,941**
Total Liability	780,748,308	803,619,867	745,811,043	**761,930,214**
Normal Cost	34,759,864	36,590,423	29,809,106	**31,069,652**
Assets	5,748,582	5,748,582	5,748,582	**5,748,582**
Unfunded Accrued Liability	774,999,726	797,871,285	740,062,461	**756,181,632**
Amortization of Unfunded Liability	23,238,214	23,924,013	22,190,627	**22,673,957**
ARC	57,998,078	60,514,436	51,999,733	**53,743,609**
Projected Cash Payments				
2011	30,450,971	30,664,880	30,296,434	**30,450,909**
Projected ARC				
2011	63,578,771	66,333,881	57,017,455	**58,926,874**

VSTRS Tiered Health Care at 40%, 60% and 80% at 10, 20 and 30 years of service				
	Baseline		For employees > 5 yrs from retirement	
	w/o spouse	w/ spouse	w/o spouse	w/ spouse
Total Active Liability	480,458,988	632,567,208	**409,919,649**	537,910,713
Retiree Liability	391,777,332	391,777,332	**391,777,332**	391,777,332
Total Liability	872,236,320	1,024,344,540	**801,696,981**	929,688,045
Normal Cost	33,745,199	44,306,494	**21,661,787**	28,198,018
Assets	-	-	**-**	-
Unfunded Accrued Liability	872,236,320	1,024,344,540	**801,696,981**	929,688,045
Amortization of UAL	25,221,028	29,619,293	**23,181,358**	26,882,266
ARC	58,966,227	73,925,787	**44,843,145**	55,080,284
Projected Cash Payments				
2011	21,911,328	23,367,423	**21,911,328**	23,367,423
Projected ARC				
2011	64,656,785	81,039,069	**49,212,660**	60,430,639

Comments on Other Proposals Reviewed by the Commission

Actuarial Assumptions

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. State statute provides that at least once in each five-year period, the State's actuary is to make an investigation into the mortality, service, and comprehensive experience of the members and beneficiaries of the system and make recommendations for certain modifications of the actuarial assumptions, as needed.

As a matter of practice, it is recommended that changes in methods or assumptions be considered only in conjunction with a full experience study, unless a significant event impacts their use. In the current economic climate a number of actuarial assumptions might vary from experience including investment rate of return and wage inflation and CPI changes. For instance, a decrease in the assumed rate of investment return would increase the calculated unfunded liability and increase the ARC. On the other hand, a decrease to the wage inflation would decrease accrued liabilities, reduce the unfunded liability, and decrease the ARC.

Assumptions are interdependent and should be consistent with one another. In addition, short-term anomalies may not hold into the future. For instance, wage inflation assumptions may be out of sync with recent collective bargaining, but the future is still uncertain. Inflation

assumptions could be lowered for now but the potential for inflation with the economic stimulus initiatives at the national level could quickly result in another change. Finally, credit agencies may see some of these changes as pragmatic approaches rather than disciplined funding practices.

The Commission has elected to recommend against any changes to the actuarial assumptions.

Lengthening the Amortization Period

In 2008, the General Assembly the amortization period for VSERS was reset for thirty years beginning 7/1/2008. The previous thirty year amortization period set by statute was set to expire in 2018. Even without the recent investment experience, resetting the amortization period made sense. As reported by the consulting actuaries, unusually short periods create greater volatility in the ARC. If there were no amortization at all, gains and losses would be absorbed in one year. Resetting the VSERS amortization period therefore did have a significant impact on the FY10 and now the FY11 ARC. Longer amortization periods reduce the payment toward the unfunded liability by stretching them over longer periods.

In the case of VSTRS the thirty year amortization period for amortization of the unfunded liability was restarted effective 7/1/2006 as a result of a previous recommendation made by the 2005 Commission on Funding the State Teachers' Retirement System. This was done in concert with a change in the actuarial funding method from "Frozen Initial Liability" or FIL to "Entry Age Normal or EAN", for both VSTRS and VSERS. Under the previous method, the unfunded liability was frozen at 1988 levels. Any impact of underfunding subsequent to the "freezing" of the liability in 1988 fell to normal cost instead of being added to the unfunded liability as in more conventional funding methods.

At the time the legislature made the change to restart the VSERS liability effective 7/1/2008, VSTRS was also set to the same date as was the municipal system (VMERS). This was done as an administrative convenience so that all three systems were on the same schedule. It had little impact on the VSTRS ARC as the system was only two years into the previous thirty year schedule.

As a result of these actions, the current amortization periods are not far from the limit set by the Government Accounting Standards Board (GASB) and any re-amortization to thirty years would have little impact. Some States have however, given, the significant investment loses, have opted to temporarily extend the amortization period even further, to forty years. Again this will lessen the annual ARC in the short run but will have the effect of increasing overall interest costs, similar to the effect of extending your mortgage payment. In addition, states and coal governments extending the amortization period will be required under GASB to recalculate the ARC using the thirty year amortization for financial statement purposes and show a liability (net pension obligation) for any underfunding of the ARC on the balance sheet.

The Commission did not recommend an increase in the amortization period.

Pension Obligation Bonds

Some states have sold pension obligation bonds (POBs) to provide cash in order to lower unfunded liabilities and to invest to meet future benefit payments. The Commission benefited from a presentation by Thomas Howard, Executive Director of the Kentucky Office of Financial Management, on this subject. The ultimate goal of the use of POBs is to lower costs for the system. This will happen if the investment return on the proceeds of the borrowed money is greater than the interest costs. If that turns out not to be the case, the State and the retirement systems would be in worse shape than if the bonds had not issued in the first place. The sale of pension obligation bonds converts the pension funding obligation from a soft liability for the State, which can be adjusted to meet changing economic conditions, into a firm legal commitment codified in a bonded liability. On the one hand this will add discipline to the funding obligation and on the other hand it will significantly curtail the State's budgetary flexibility in meeting the myriad obligations it may have. This financing technique is not commonly utilized by highly rated states and has enjoyed mixed results. The Commission felt that the risks of issuing POBS outweighed the potential benefits and recommended against utilization by the State of Vermont.

Education Fund

Part of the legislative charge to the Commission was to consider funding methods, including contributions from the State, municipalities, and employees. This charge was interpreted as applying to the VSTRS system, as, while teachers are employees of local districts, there is currently no local contribution to cover either teacher pension or retiree health costs. The "employer" share of the pension contribution is made entirely by the State. The 80 percent "employer" share of retiree health insurance is paid from the assets of the pension fund.

The Commission did consider transferring all or a portion of the employer contributions for teacher pensions to the Education Fund. Reasons stated for why this might be appropriate included improvement of transparency for total educational expenditures, increased accountability between incurrence of liabilities and responsibility to pay, and improved likelihood of full funding on a consistent, dependable basis.

One scenario the Commission reviewed would have:

- Continued to pay for unfunded pension liabilities (about 2/3 of the total contribution) from the General Fund and transferred normal costs to the Education Fund or directly to local districts with a multi-year phase-in. This would have avoided shifting the burden of any past underfunding by the State to local districts via the Education Fund.
- Continued paying the employer share of VSTRS retiree health insurance for those already on the job as is. For new hires, districts would be assessed on a prefunding actuarial basis with the proceeds deposited in a dedicated trust fund to pay for future health care.
- Revised VSTRS Board Governance by increasing membership from six to seven, adding a school board member and a superintendent and removing the BISHCA Commissioner or designee.

In the end, the majority of the Commission voted not to include any recommendation to transfer any part of the obligation for funding teacher pension or retiree health benefits to the Education Fund or local districts. The reasons for this position varied among Commission members, but included recognition that such a transfer would increase property taxes unless concurrent cost reductions were implemented at the local level, and a desire not to have the debate on this hot-button topic overshadow consideration of the remaining Commission recommendations to improve the affordability and sustainability of the retirement plans.

The Commission does emphasize that the current process for funding retiree health care of teachers cannot continue as is and immediate corrective measures need to be taken as discussed in the next section.

VSTRS Health Care

Regulatory Context: Pension plans are expected to provide primarily pension benefits. Where health care benefits are provided through the same plan (not the predominant model), they must, according to IRS code, be subordinate to the pension benefits and must also be managed through a separate "sub trust." IRS code establishes a 25 percent limitation on contributions to a 401(h) sub trust. One of the many conditions that a pension program must meet is that the "aggregate actual contributions" for medical benefits do not exceed 25 percent of the "total actual contributions" to the plan after the date it first offers medical benefits. Our historical analysis indicates that we have not exceeded the 25 percent limitation in aggregate. However, health care increases exceed the estimated increase for benefits (based on increasing populations and wages and other demographics). It is clear that at some time in the future we will reach this ceiling, which if not addressed, could have adverse consequences to the entire pension fund or the ability to provide adequate health care benefits.

Funding Context: In the case of the State system, "pay-as-you-go" health care premiums are explicitly budgeted, along with other administrative expenditures, and are budgeted as an "add-on" to the actuarial required contribution for pension benefits. That provides an ongoing funding mechanism. A "true-up" is conducted each year, impacting future appropriations, accounting for any surpluses or deficits in the planned expenditures. In the Teachers' system, health care is treated as a loss to the system and therefore impacts the contribution level calculated by the actuary. It is in essence "retrospective financing," always incorporating a lag. As such, there are no explicit current appropriations to pay for the health care expenses. Without an explicit appropriation, funds cannot be transferred to an OPEB trust or similar fund to pay for these.

Funding Need: FY 2009 health care "pay-as-you-go" health care premiums totaled $16,421,176. In order to create a separate fund to pay these costs, we would need to appropriate similar amounts of funds, in the order of $16 to $17 million plus, going up each year. Over time, funding this will reduce the pension ARC, which incorporates a heath care portion, but not at a 1:1 ratio; and new resources are needed to "jump-start" funding for a separate health care fund.

A number of concepts were discussed:

1. Directly assess local education agencies (LEAs) for a portion of retiree pay-as-you-go health care (cost of premium payments) funding for existing active members as of 7/1/2010 or future new hires, or both of these categories of participants. If phased in, this proposal has the advantage of a gradual phase-in and will take some of the pressure off the 25 percent health care threshold issue.

2. A variation to the above would be to assess LEA for new hires on a "prefunded basis" instead of a pay-as-you-go basis. Funds would then be deposited in an OPEB Trust fund, earning interest, and providing a phase in of prefunding.

Spousal Coverage

The teachers' system currently pays 80 percent of the retirees' premium only, based on the standard plan. The retiree must pick up the full premium for all covered dependents. This would primarily be a spouse, although it is not unusual for a retiree to also have one or more children still in school as well. A retiree who must have two person coverage will pay $616.44 per month, which jumps up to $970.44 per month for family coverage. This is cost-prohibitive for many teachers, and is actually a very real deterrent for a teacher who wishes to retire. Although the majority of the Commission members voted not to add a spousal subsidy for Vermont State Teachers' Retirement System members because of the cost, it is an issue that should be discussed in more depth to determine if there are alternative ways of paying for some level of subsidy that would enable retirees to better afford medical coverage for their dependents.

Conclusion

Failure to address the issue of the sustainability of our public retirement plans now will surely lead to larger problems later and the need for more draconian steps, failing both the employees and the taxpayers. As stated early in this report, the recommendations of this Commission attempt to strike a balance, recognizing both the public policy and economic context in which the current benefit structures operate. We do not make our recommendations lightly and hope that the Legislature, the Governor, and all interested parties recognize the urgent need to balance these concerns and create sustainable plans. Change will occur, either by careful long-term planning, by default, or in crisis. Clearly, there are no easy solutions, but there are fiscally and socially responsible steps we can take.

While we believe that these recommendations provide a solid course of action, we also recognize that there is a range of options inherent in each, with varying impacts on the overall cost of benefits. We see this report as the foundation of a meaningful dialogue within which varying proposals can be reviewed. We look forward to working with you and all interested parties through the coming legislative cycle to meet our mutual goal of a fair, equitable, and sustainable retirement system that provides benefits to the labor force and the state economy.

Acknowledgments /Bibliography

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- Ice Miller, LLC
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- Legislative Joint Fiscal office

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Statutory Reference

Act No. 1 of the 2009 Special Session
Sec. E.135.1 COMMISSION ON THE DESIGN AND FUNDING OF RETIREMENT AND RETIREE HEALTH BENEFITS PLANS FOR STATE EMPLOYEES AND TEACHERS

(a) A commission is created to review and report on the design and funding of retirement and retiree health benefit plans for the state employees' and teachers' retirement systems. The commission is charged with making recommendations about plan design, benefit provisions, and appropriate funding sources, along with other recommendations it deems appropriate for consideration, consistent with actuarial and governmental accounting standards, as well as demographic and workforce trends and the long-term sustainability of the benefit programs. The joint fiscal committee may provide benchmark targets reducing the rate of expenditure growth for retirement and retiree health benefits to the commission to guide the development of recommendations.

(b) The commission shall comprise the following members:
(1) one member of the house of representatives, appointed by the speaker of the house;
(2) one member of the senate, appointed by the president pro tempore of the senate;
(3) the state treasurer, who shall chair the commission;
(4) the secretary of administration or designee;
(5) the commissioner of education or designee;
(6) one member of the public with pension and benefit experience appointed by the governor;
(7) one member of the public with pension and benefit experience appointed jointly by the speaker of the house and the president pro tempore of the senate.

(c) The report shall include, but not be limited to, the following:
(1) an evaluation of current benefits structures and contribution characteristics in comparison to other comparable public and private systems;
(2) an estimate of the cost of current and proposed benefits structures on a budgetary, pay-as-you-go basis and full actuarial accrual basis;
(3) a five-year review of benefit expenditure levels as well as employer and employee contribution levels and growth rates and a three-, five- and ten-year projection of these levels and rates;
(4) based on benefit and funding benchmarks, options for providing new benefit structures with the objective of adequate benefits within the established cost containment benchmarks;
(5) funding methods, including contributions from state, municipalities, and employees, to achieve these objectives; and

(6) an evaluation of whether current governance, oversight, and lines of authority are appropriate and consistent with funding objectives.

(d) During the course of its deliberations and prior to any final recommendations being made, the commission should solicit input from the affected parties, such as employees, taxpayers, and organizations representing those parties, including the Vermont state employees association, Vermont– NEA, and the Vermont league of cities and towns.

(e) The commission may select and oversee outside expert benefit and legal expert advisory services as it deems appropriate. An amount of $150,000 is appropriated for this purpose in Sec. B.1101(a) of this act.

(f) On or before December 18, 2009 the commission shall file a report and recommendations with the governor and the general assembly.

(g) The commission shall also provide the report to the board of trustees of the state employees' and teachers' retirement systems for their consideration, deliberation, and comment to the general assembly.

(h) Administrative support shall be provided by the office of the state treasurer.

(i) Legislative and public members shall be entitled to per diem compensation and expenses as provided for in § 406 of Title 2 and § 1010 of Title 32 respectively.

Commission Votes

Retirement Commission Votes
December 15, 2009

1. Should we recommend benefit changes for employees already vested?

YES	NO
Jeb Spaulding	Terry Macaig
Jeanette White	
Neale Lunderville	
Bill Talbott	
Doug Wacek	
David Coates	

2. If we are going to recommend benefit level changes for employees not close to retirement, what do we mean by 'close'? More than five years from retirement eligibility?

YES	NO
Jeb Spaulding	Terry Macaig
Neale Lunderville	Jeanette White
Doug Wacek	Bill Talbott
David Coates	

3. Would contribution level increases apply to everyone, all groups, all employees in the system?

YES	NO
Jeb Spaulding	Terry Macaig
Neale Lunderville	Bill Talbott
Doug Wacek	
David Coates	
Jeanette White	

State Group F and Teachers' Group C

4. Raise normal retirement age from 62 or 30 years at any age to 65 or rule of 90 (combination of age and years of service) for those more than five years from normal retirement eligibility?

YES	NO
Jeb Spaulding	Terry Macaig
Neale Lunderville	Jeanette White
Doug Wacek	Bill Talbott
David Coates	

5. Raise the early retirement age from 55 to 58 for those more than five years from early retirement eligibility?

YES	NO
Jeb Spaulding	Terry Macaig
Neale Lunderville	
Doug Wacek	
David Coates	
Jeanette White	
Bill Talbott	

State Group D

6. Raise normal retirement age from 62 to age 65 for those more than five years from normal retirement eligibility?

YES	NO
Jeb Spaulding	Terry Macaig
Neale Lunderville	
Doug Wacek	
David Coates	
Jeanette White	
Bill Talbott	

State Group C

7. Raise the early retirement age to 52 from 50 for those more than five years from early retirement eligibility?

YES	NO
Jeb Spaulding	Terry Macaig
Neale Lunderville	Bill Talbott
Doug Wacek	
David Coates	
Jeanette White	

State Group F and Teachers' Group C

8. Use a five year compensation period instead of a three year period to calculate benefits for those more than five years from retirement eligibility?

YES	NO
Jeb Spaulding	Terry Macaig
Neale Lunderville	Bill Talbott
Doug Wacek	Jeanette White
David Coates	

State Group C

9. Use a three year compensation period instead of a two year period to calculate benefits for those more than five years from retirement eligibility?

YES	NO
Jeb Spaulding	Terry Macaig
Neale Lunderville	Bill Talbott
Doug Wacek	Jeanette White
David Coates	

State Group D

10. Use a two year compensation period instead of final salary to calculate benefits for those more than five years from retirement eligibility?

YES	NO
Jeb Spaulding	Terry Macaig
Neale Lunderville	Bill Talbott
Doug Wacek	
David Coates	
Jeanette White	

11. Increase the maximum benefit from 50% to 60% of final compensation for State Group F and Teachers' Group C?

YES	NO
Terry Macaig	Neale Lunderville
Jeb Spaulding	Doug Wacek
Jeanette White	
David Coates	
Bill Talbott	

12. Sharing cost of total actuarial contribution changes (50/50, 60/40) to be determined by actuary to get to 3.5% recommendation?

YES	NO
Jeb Spaulding	Terry Macaig
Neale Lunderville	Jeanette White
Doug Wacek	Bill Talbott
David Coates	

13. Implement a tiered system so that degree of premium assistance is linked to length of service for those more than five years from retirement eligibility:

40% - 10 years   60% - 20 years   80% - 30 years

YES	NO
Jeb Spaulding	Terry Macaig
Neale Lunderville	Jeanette White
Doug Wacek	Bill Talbott
David Coates	

14. Provide ability to 'recapture' health benefit with 20 years of service upon drawing of retirement benefit?

YES	NO
Terry Macaig	Bill Talbott
Jeanette White	Neale Lunderville
Doug Wacek	
Jeb Spaulding	
David Coates	

15. Include a comment discussion was held concerning adding spouses to coverage for Vermont State Teachers' Retirement System members. There was a vote held and 5-2 voted not to add spouses for Vermont State Teachers' Retirement System members.

YES	NO
Terry Macaig	Doug Wacek
Jeb Spaulding	Neale Lunderville
	Jeanette White
	David Coates
	Bill Talbott

16. Include a comment discussion was held concerning the Education Fund/local districts contribution to pension and/or retiree health costs.

YES	NO
Terry Macaig	
Jeb Spaulding	
Doug Wacek	
Neale Lunderville	
Jeanette White	
David Coates	
Bill Talbott	

17. Include a comment the Commission encourages legislature to examine the issue of the payment of the employers' share of VSTRS retiree health insurance.

YES	NO
Terry Macaig	
Jeb Spaulding	
Doug Wacek	
Neale Lunderville	
Jeanette White	
David Coates	
Bill Talbott	

18. Include a comment which includes the Commission's recommendation of further consideration for a defined contribution/cash balance plan alternative to the current defined benefit plan.

YES	NO
Bill Talbott	Terry Macaig
Neale Lunderville	Jeanette White
Doug Wacek	Jeb Spaulding
David Coates	

19. Include a comment that discussion was held concerning use of pension obligation bonds to pay off a portion of the unfunded liability, but there is no recommendation to use pension obligation bonds.

20. Include a comment discussion was held and there is not a recommendation to lengthen the amortization period for unfunded liabilities from 30 years.

YES	NO
Bill Talbott	
Neale Lunderville	
Doug Wacek	
David Coates	
Terry Macaig	
Jeanette White	
Jeb Spaulding	

20. Include a comment discussion was held and there is not a recommendation to revise the assumptions.

YES	NO
Bill Talbott	
Neale Lunderville	
Doug Wacek	
David Coates	
Terry Macaig	
Jeanette White	
Jeb Spaulding	

21. Finally, the Retirement Commission unanimously voted to include a recommendation to the Legislature to begin a structural process to fund the OPEB obligations and set money aside in a material way in a separate, independent funding mechanism.

Appendices

Legislative Joint Fiscal Committee Benchmark Target Recommendation

ONE BALDWIN STREET
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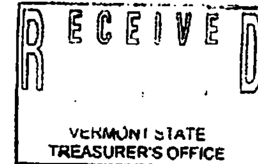
STATE OF VERMONT
LEGISLATIVE JOINT FISCAL COMMITTEE



August 12, 2009

Jeb Spaulding
Office of the State Treasurer
109 State Street
Montpelier, VT 05609-6200

RE: Legislative Joint Fiscal Committee Benchmark Target Recommendation

Dear Treasurer Spaulding,

Pursuant to Sec. 135.1 of Act 1 of the 2009 Special Session, the Legislative Joint Fiscal Committee (JFC) has met and discussed providing the Commission on the Design and Funding of Retirement and Retiree Health Benefits Plans for State Employees and Teachers with benchmark targets for the rate of expenditure growth for retirement and retiree health benefits to guide its development of recommended reforms to the retirement systems.

The JFC considered the recent performance of a number of indicators that reflect state revenue and spending trends and broader economic trends; examples include the general fund growth rate and the state and local price index.

After considering this information, the Joint Fiscal Committee recommends a benchmark target of 3.5% for the rate of expenditure growth for retirement and retiree health benefits.

The JFC recognizes the fact that controlling the rate of expenditure growth will require difficult decisions on the part of the Commission, the legislature, and system participants. The JFC also recognizes that this recommendation serves as a guide and does not bind the Commission; however, in the event that a higher growth rate is targeted, the Commission should be specific as to how it is to be financed.

Sincerely,

Michael J Obuchowski

Rep. Michael Obuchowski
Legislative Joint Fiscal Committee, Chair

VT LEG 248954 1

Responses to 2008 market decline and rising pension costs

State	Contribution Rates	Benefits	Actuarial Methods/Processes	Study Commissions	Proposed Changes
AK					
AL					Legislature is expected to consider the following changes when it convenes in January: a 1% increase in employee contributions, effective immediately; benefit based on highest 5 of 10 years of service, rather than highest 3; for new hires, minimum retirement age of 60 rather than any age with 25 years of service; for new hires, eligibility for DROP at age 60 with 25 years of service; extend amortization period from 20 to 30 years.
AR					
AZ	Employee and employer contribution rates will rise from 9.0% to 9.6% as of 7/1/10. These rates include the health insurance benefit supplement.				The ASRS has suggested the legislature consider the following for new hires a) increasing normal retirement eligibility from Rule of 80 to 85; b) raising FAS from 3 years to 5; c) limiting refunds for terminating members to 25% of employer contributions (current law permits up to 100% after 10 years of service). These changes have been suggested previously to the legislature but have not been approved.
CA	CalPERS adjusted state, local and school employer contribution rates via modifications described in Actuarial Methods/Processes.		CalPERS added an employer rate smoothing methodology for local governments and school employer rates. The technical changes include: 1) Expanding the current rate smoothing corridor from 80% to 120% of market value of assets (MVA) to 60% to 140% of MVA in the first year, to 70% to 130% in the second year, then back to 80% to 120% of MVA in the third year. 2) Isolating and amortizing investment gains and losses in the next three years using a fixed and declining 30-year period as opposed to the current rolling 30-year amortization period.		A taxpayer rights group has filed ballot initiatives that would establish a new tier of pension benefits for all public employees in the state. Among other provisions, the changes would 1) impose maximum multipliers on new hires, such as 2.3 for police and fire, 1.25 for general employees, and 1.65 for general employees outside Social Security; 2) impose minimum retirement ages of 58 on police and fire, and the Social Security retirement age for general employees; 3) place a cap on pensions of 75% of workers' pay; 4) exclude from the pension benefit overtime, bonuses, unused sick and vacation leave; 5) require that future benefit changes be subject to public vote; and 6) require that full costs of retiree health care benefits be paid by employees and employers, to end the accumulation of unfunded liabilities. The initiative must receive the requisite number of valid signatures to appear on the November 2010 ballot.
CO	The CO Legislature eliminated for fiscal years 08-09, 09-10, and 10-11 the state's annual contribution to the fire and police pension association (FPPA), to assist in amortizing the unfunded accrued liability of old hire pension plans; resumes the state's annual contribution to the FPPA beginning in FY11-12, and extends the contribution through FY 14-15.				CO PERA Board recommended to legislature revisions that include: increases to employee and employer contribution rates; reduced (from 3.5% to max of 2.0%) auto-COLAs for current and future retirees; delay onset of COLA to 12 months after retirement; revising return-to-work rules to, among others, require retirees returning to work to make contributions that do not accrue a benefit nor are available to the member; increase the final average salary period from 3 years to 5; adopt Rule of 90 with minimum age 60 for all employees unvested on 1/1/11; adjust early retirement reduction for those ineligible to retire by 1/1/11 to reflect true actuarial cost; and other changes as described at www.copera.org. Also, the CO Fire & Police Pension Assn. Board recommended legislation to allow its members and employers to vote to increase employee contributions to the main DB plan from the current 8% (employer contributions would remain unchanged at 8%).
CT					
DC					
DE	The state's contribution rate will increase in FY11 from 6.01% to 7.4%				Legislature is likely to consider reducing retirement multiplier for new hires, from 1.85% to 1.67%.
FL		The legislature terminated eligibility of retired members to receive a second benefit by returning to work and increased the required break-in-service from 1 month to 6.			

Sources: Retirement systems, NCSL, media reports

Compiled by NASRA

12/22/2009

Responses to 2008 market decline and rising pension costs

State	Contribution Rates	Benefits	Actuarial Methods/Processes	Study Commissions	Proposed Changes
GA	TRS increased employee rates effective 7/1/09 from 5.0% to 5.25%, and employer rates from 9.28% to 9.74%. Effective 7/1/10, TRS employee rates will increase again, to 5.53%, to 10.28% for employers.	Legislature approved prohibition of COLAs to members of ERS and the Judges retirement system hired after 6/30/09. Also, passed legislation designed to limit spiking: for new hires, limited the increase in retirants' final year's salary to 5%; for existing members, the employer must pay ERS of GA for the present value of the impact of any increase above 5% to the system.			
HI					
IA					A legislative committee has proposed the following: raising contribution rates from 11.95% to 13.45%, which are paid 60% by employers and 40% by employees; raising the vesting period for new hires from 4 years to 7; raising FAS period to 5 years from 3; and a higher reduction for early retirement, intended to reflect the true actuarial cost.
ID	The Idaho PERS Board elected to phase in contribution rate increases, shared 1/3 by employees and 2/3 by employers, as follows: 1.5% each on 7/1/11 and 7/1/12, and 2.31% effective 7/1/13. By 7/1/13, employer rates for general employees and teachers will be 13.65% and 8.19% oremployees; employer rates for public safety will be 13.99% and 10.04%.	Idaho law requires that the Board implement a negative COLA if the August to August CPI-U is negative. The CPI-U was negative 1.48%. Thus the Board initially established a COLA of that amount. The Board had to consider rate increases before they could consider any retro COLA (i.e. the UAL amortization period must be at or below 25 years after the COLA.) After approving statutorily-required contribution rate increases (see Contribution Rates), the board approved a COLA of 2.48%, effectively increasing benefits for most retired members by 1%.			
IL	Legislature authorized issuance of $4.3 B in pension bonds to fund contributions to the state retirement systems in FY10, which may be issued in 1/10. Contributions will rise for employers in the IL Municipal Retirement Fund.		IMRF Board increased funding corridor from 10% to 20%; revised amortization period from a closed 22-year period (which would have declined to 10) to a rolling 30-year; and employers were given an option to pay the ARC or to phase in contribution rate increases. Also, legislature approved conversion from market value of assets to five-year smoothing for SURS, SERS, and TRS, effective with the valuations dated 6/30/09. No funding corridor was specified. Remaining 80 percent of 2009 losses will be recognized in subsequent actuarial valuations.	Pension Modernization Task Force met over summer and fall; components of report were adopted by task force sub-committees, but report in its entirety was not adopted. The report provides background on covered topics and appendices with individual opinions. The report is accessible at the task force's website: http://www.illinois.gov/gov/pensionreform/	For the SERS, TRS, and SERS, the legislature is expected to consider various proposals when it convenes in 2010, including: lower defined benefit formulas (different formulas for SS coordinated and noncoordinated); higher retirement ages; longer vesting periods; lower maximums; caps on salaries that could be used for retirement purposes; elimination of the survivor benefit program; and elimination of early retirement programs.
IN	Upon recommendation of the actuary, the IN PERF Board approved an employer contribution rate increase for the state from 6.5% for FY10 to 7.0% for FY11. As an agency plan, the average contribution rate for local units also increased, from 7.143% to 7.552% for the same years.				
KS				The Kansas Legislature's Joint Committee on Pensions, Investments and Benefits is studying a wide range of options, including: increasing employer and employee contribution rates, lowering the multiplier for future service, issuing bonds in lieu of an employer contribution increase, and a mandatory defined contribution plan for new employees. The Committee expects to make recommendations for statutory changes in the 2010 legislative session.	
KY	Based on recommendations from its actuary, the KRS board requested employer contribution rates that are sharply higher for several plans above current levels; the General Assembly will approve the actual rates during its 2010 session. The GA in 2006 established a schedule for reaching the ARC by 2024; the GA may or may not comply with that schedule in FY 11.	The General Assembly approved, and the governor signed in 2008 a number of changes affecting KRS participants, including reduced pension benefits for new hires, higher employee contributions for all participants, and modifications to the auto-COLA by limiting it and authorizing the General Assembly to suspend it		A working group appointed by the governor met and produced a report in 2008; no other study commissions are in place.	KRS expects during the 2010 General Assembly attempts to define "full funding" as 80% funded (based on a January 2006 Government Accountability Office report entitled, "State and Local Government Retiree Benefits"): http://www.gao.gov/new.items/d08223.pdf

Responses to 2008 market decline and rising pension costs

State	Contribution Rates	Benefits	Actuarial Methods/Processes	Study Commissions	Proposed Changes
LA	The employer rate is scheduled to rise to 22% in FY 13 from 18.6% in FY 10.	Legislature modified COLA provisions for statewide systems to retain more assets in the trust funds to amortize the unfunded liability, limiting future COLAs and changing the terminology from "cost-of-living" to "permanent benefit increase." COLAs also are limited to those retired at least one year and who have reached age 60. Also, approved bill allowing a member of any statewide retirement system who retires after 7/1/09 to self-fund a guaranteed 2.5% annual COLA through an actuarial reduction of benefits. Any COLAs provided supplement the self-funded annual 2.5%.	Legislature authorized the refinancing of unfunded liabilities for LASERS and TRS of LA over a 30-year period beginning in FY10.	The Commission on Streamlining Government was created to reduce the cost of state government, through all means available, including efficiencies, economies, and greater effectiveness. The commission inquired about LASERS' retirement incentive programs and cost saving measures.	The Commission on Streamlining Government recommended a defined contribution plan for new employees. The Commission also recommended allowing the purchase of air time for eligibility and closing the DROP program effective 1/1/2015. Legislation is required to implement any of these recommendations.
MA					A commission has been studying pension benefits during 2009 and is expected to submit recommendations for consideration by the 2010 general assembly. Also, a gubernatorial candidate has proposed pension reforms that include an annual pension cap of $90k and pension benefit based on lifetime earnings
MD					
ME		Legislature approved a bill amending existing statutes to provide that if the inflation rate in a given year is less than zero, benefit levels for current retirees will not be reduced.		Legislature established a task force to study creation of a new unified plan that would require all new hires to be enrolled in Social Security and Medicare, would coordinate retiree health benefits with the new plan, and provide a defined benefit plan. The combined actuarial costs of the new plans are to be divided equally between employers and employees. The task force is to report no later than 3/1/10.	
MI	Some MERS employers increased rates in 2008 and MERS has advised others that higher rates may be forthcoming.	MERS adopted a bridged or tiered benefit system, allowing a municipality to lower the benefit multiplier on a prospective basis.	MERS temporarily suspended a declining amortization schedule. For 08 and 09 valuations, the amortization period will remain at 28 years for unfunded accrued liabilities, then to resume declining in 10 at 1-year increments until reaching 20 years in 17. Also, revised actuarial assumptions to reflect increases to employer contributions for assumptions for turnover, retirement and FAS.	MERS is working with the state on fiscal responsibility for plan design changes.	MERS Board is evaluating raising the retirement age, lowering the discount rate for service credit purchases, and prohibiting use of overtime in FAS.
MN					The TRA Board is recommending a shared sacrifice approach, via the following legislative package: 1) A phased increase in employer and employee contributions, from 5.5% each to proposed 7.5%, phased in over 4 years, rising by 0.5% each year. After the phase-in, TRA is requesting authority for an auto contribution stabilizer that provides the board with authority to set future contribution rates (within boundaries) should the system have a contribution deficiency. 2) A 2-year suspension on annual benefit increases followed by a more permanent reduction in the COLA from 2.5% to 2% until the funding ratio reaches 90%. 3) Reduction in the interest rate paid on refunds of contributions from 6% to 4%. 4) Reduction in the annual increase for deferred benefits to 2%. Deferred benefits are paid to members who terminate, leave their money on deposit with TRA, and later collect a benefit. The deferral interest rate is applied to the member's benefit beginning from the member's termination date to collection of the benefit. Also, the PERA Board adopted a legislative position supporting: 1) a reduction in annual benefit increases from 2.5% to 1.0% until the funding ratio reaches 90%; 2) an increase of 0.25% in both employee and employer contribution rates; 3) a reduction in the interest rate paid on refunds of contributions from 6% to 4%; 4) reduction in the annual increase for deferred benefits to 1%; and 5) increase in vesting period for new hires, from 3 years to 5.

Responses to 2008 market decline and rising pension costs

State	Contribution Rates	Benefits	Actuarial Methods/Processes	Study Commissions	Proposed Changes
MO	The MOSERS employer contribution rate will rise 7/1/10 from 12.75% to 13.81%; MOSERS is non-contributory for employees. The PSRS/PEERS Board voted to increase the contribution rates for 09/10 and 10/11. PSRS was increased by 1% each year (the maximum annual increase allowed by law). The rate for PEERS increased by 0.5% in 09/10 and 0.26% in 10/11 (the maximum annual increase allowed by law). Contributions are paid equally by employers and employees of both systems.		MOSERS temporarily widened the funding corridor, from 120% to 130%, to moderate required increase in contribution rates.		
MS	MS PERS board approved increased employer contribution rates, from 12.0% to 13.56%, effective 7/1/10.			The MS PERS Board voted to establish a commission to study legal issues associated with increasing the employee contribution rate; this commission will remain in place to review the plan's benefit structure, with possible recommendations to legislature in 2011.	Governor has proposed higher employee contributions, lower employer contributions, and rolling back recent benefit enhancements, including an auto-COLA.
MT				Legislature established an interim committee to examine and recommend funding and benefit changes in the statewide public employees' and teachers' retirement systems.	
NC	In line with the historical funding policy of always contributing the ARC, the employer contribution for the state system is due to increase from 3.57% in FY10 to 6.71% in FY11. The employer contribution for the local system is due to increase from a base rate of 4.80% to 6.35% as of 7/10.			NC Retirement System Board established the Future of Retirement Study Commission to recommend the retirement benefits that should be provided to future hires of state and local government. The commission is scheduled to begin meeting 1/10.	
ND				Legislature directed the HR Management Services to study how to retain state workers who are nearing retirement; relates to workforce recruitment and retention.	
NE	Legislature increased school employees' contribution rate by one percent, from 7.28% to 8.28%, effective through 2014. Employer rates will rise also, from 7.35% to 8.36%. The state also committed to paying $20 million annually to the school pension fund for 5 years. Also, increased employee rate to the state patrol fund, from 13% to 15%, to match the employer rate.				
NH	Legislature increased employee contribution rate from 5% to 7% for those hired after 6/30/09. Increased employer contribution rate for non-state government employers from 65% of the annual required contribution in FY09 to 70% in FY10 and to 75% in FY11 (state government contributes the remainder).				Actuary has recommended sharply higher employer contribution rates that would take effect 7/1/11.
NJ	Legislature reduced required contributions of municipal employers by one-half; remainder may be paid over a 15-year period.				
NM	For the two-year period beginning 7/1/09, legislature increased employee contribution rates for all public employees, including teachers, by 1.5%, and reduced the contribution rate for all employers by the same amount.	Legislature in 2009 created new retirement plans for state and municipal general members of the PERA other than peace officers. Retirement eligibility under the new plans is any age and 30 of service, age 67 and five years of service, or the "Rule of 80". The bill also contains a new retirement plan for members of the Education Retirement Board (ERB), in which eligibility for retirement is the same as under the new PERA plans, except benefits are reduced for a member retiring under the rule of 80 if the member is under 60 years old. The new retirement plans are effective 7/1/11 and will apply to employees hired on or after 7/1/10.		Legislature created the retirement systems solvency task force, to study the actuarial soundness and solvency of the state retirement plans and the health care plan of the retiree health care authority, and to prepare a solvency plan for each entity. The solvency plans are to include analyses and recommendations that address: 1) employer and employee contributions; 2) retirement eligibility; 3) the number of retirement plans; 4) retirement benefits; 5) investment policy and asset allocation; 6) disability retirement and benefits; 7) actuarial assumptions; 8) health insurance plan benefits and eligibility; 9) the costs of health insurance plans; and 10) member services.	The legislature is planning to increase the size of the PERA board from 12 to 16 by adding 3 outside investment professionals (to be appointed by our board) and the State Auditor. This stems from the poor returns last year and the legislature's view that the PERA board lacks investment expertise that may have lessened the losses. The legislature also is proposing creation of an Alternative Investment Advisory Committee should PERA investments in Alternative assets reach $500 million. This group would oversee and advise the board on the investments in that asset class. These committees will be made up of both board members and outside investment professionals with experience in that particular asset class. Each committee will be made up of 5 members.

Sources: Retirement systems, NCSL, media reports

Compiled by NASRA

12/22/2009

Responses to 2008 market decline and rising pension costs

State	Contribution Rates	Benefits	Actuarial Methods/Processes	Study Commissions	Proposed Changes
NV		Legislature approved changes for those hired **after** 1/1/10. For non-public safety members, eligibility for current members is 65/5, 60/10 or 30 years of service. This **bill** changes 60/10 to 62/10. For public safety officers, eligibility of current members is 65/5, 55/10, 50/20 or **25** years of service. This bill removes the 25-and-out **option.** For current members, the actuarial reduction for early retirement is 4% per year, prorated for months short of **a** year; for those joining on or after 1/1/10, it will be 6% **per** year, prorated. For current members, the benefits formula is 2.5% of FAC times years of service before 7/1/01, plus 2.67% for years of service earned thereafter. This bill removes the higher benefit factor for service after 7/1/01 for new hires. For new hires, FAS will exclude increases in compensation to 10% per year for the 60-month period that begins 24 months before the 36 months used in the calculation of FAC. Employees so limited are entitled to **a** prorated refund of their contributions for the appropriate period. Also, the legislature reduced the COLA for new hires, from the current method that provides a gradually-increasing COLA up to 5% annually for those retired 14 years. New hires will receive a COLA that rises to 4% annualy after 12 years of retirement.			
NY	**As of 1/1/10, employee rate for new hires rises from** 3.0% **for the first 10 years and 0% thereafter to 3.0% lifetime** for **State employees and 3.5% lifetime for teachers.**	The legislature approved a new tier for those hired on or after 1/1/10, featuring a) 10-year vesting (up from 5); b) a cap on the portion of the retirement benefit that can come from overtime pay; and 3) larger reductions for early retirement (pre-62). For state employees, no unreduced retirement permitted prior to age 62. For teachers, unreduced retirement is permitted prior to age 62 if at least age 57 and 30 years of service. For teachers, benefit multiplier of 2.0% starts at 25 years of service instead of 20.			
OH					The Ohio Retirement Study Council directed statewide plans to submit proposals for restoring sustainability, which the legislature is expected to consider in 2010. Proposals vary by system. For example, the STRS, P&F, and Highway Patrol Systems proposed higher contribution rates for employees and employers. All but the Highway Patrol system proposed more stringent eligibility criteria for both normal and early retirement, thru either higher age or more years of service, or both. All but STRS proposed reducing payments to retiree health care funds. For detail on each systems' proposal, see the comparative grid at the Ohio Retirement Study Council website: http://www.orsc.org/uploadpdf/Updated_Comparative_Summary.pdf
OK					
OR	Under current actuarial methods (including fair market value of assets), employer contribution rates generally would increase from 12% to 18% on 7/1/11. This increase is capped by a rate collar policy adopted by the PERS board, which limits biennial employer contribution rate increases to 6% of covered payroll if the employer's individual or pooled funded status falls below 80% (excluding pension obligation bond side accounts). Most PERS employers would be below this level, although some employers may still have an individual funded status above 80%, so their rate increase would be limited to 3% of covered payroll. Member contributions are fixed in statute at 6% of covered salary.				The PERS board is considering revising its rate collaring policy. For example, they may choose to revise the upper limit **on** employer rate increases so they would slope from a 3% maximum increase at 80% funded to a 6% maximum at 70% funded, instead of rising from 3% to 6% in one step if funded status falls below 80%. Alternatively, they may impose an ad hoc limit on employer rate increases for the 11-13 biennium at 3% or 4.5% of covered payroll, instead of having them rise the full 6% (assuming the employer's funded status falls below 80%).
PA	Legislature approved bill permitting City of Philadelphia to raise sales tax to fund cost of pension benefits.		Legislature approved bill permitting City of Philadelphia to extend funding amortization period to reduce near-term costs.		

Responses to 2008 market decline and rising pension costs

State	Contribution Rates	Benefits	Actuarial Methods/Processes	Study Commissions	Proposed Changes
RI		Reduced benefits for state employees, teachers and judges not eligible to retire on or before 9/30/2009, by increasing retirement age to 62 with a methodology that proportionally changes age requirement based on years of service, so the closer one is to retirement, the less the impact. Also, increased FAS calculation period from 3 years to 5, and reduced COLA to lesser of CPI or 3.0%. Also, allows purchased credit to count toward total service time but not toward vesting (as in current law), and provides that credit must be purchased at full actuarial cost after 6/16/09.			
SC					
SD			Reduced assumption for expenses and increased funding period from 20 to 30.		In November 2009, the SDRS board proposed a reduction in the auto-COLA, from 3.1% to 2.1%, linking COLA to plan funding level, and a reduction in the benefit for terminating plan participants. Also, the legislature is expected to stiffen return-to-work provisions, including reducing retirement benefit and eliminating benefit accruals for employees who have returned to work.
TN	Effective 7/1/10, employer contribution rate for teachers will increase from 6.43% to 9.05%, and for state employees from 13.02% to 14.91%.		Adjusted funding period to 20 years, from 18.		
TX	Legislature increased state employee contribution rate from 6.0% to 6.45%. The State may increase its contribution to 6.95% based on interpretation of the appropriations bill and an AG opinion. If the state contribution increases, the employee contribution will rise to 6.5%. Also, the state contribution (employer) rate to TRS was increased from 6.58% to 6.644% after the Attorney General ruled a $500 13th check was not structured properly by the Legislature.	For state employees hired after 9/1/09, normal retirement eligibility increases to 65/10 or the Rule of 80 at age 60, with a reduction for each year of age under 60. Current provisions are 60/5 or the Rule of 80 with no minimum age. Also, new hires may no longer apply unused annual leave or sick leave toward retirement eligibility, but may continue to use in determining the annuity amount. FAS period increases from highest 36 to highest 48 months. Annuity will be reduced 5% for each year short of age 60, with a maximum reduction of 25%. Similar provisions apply to newly-hired law enforcement and custodial officers, who have a normal retirement age of 55. Also, return-to-work changes require employers who hire an employee who retires after 9/1/09 to pay the ERS trust fund a surcharge equal to the retirement contribution that the employer would make for an active employee, and to wait at least 90 days before hiring an employee who retires after 5/1/09.	Actuarial cost method for funding purposes was changed such that the total liability is based on the benefit provisions for each member and the normal cost rate is based on the benefit in effect for members hired after August 31, 2009		
UT			Board approved broadening funding corridors from 80/120 to 75/125. Also, the amortization period was moved from 20-year open to 25- year fixed, but moving each year over the next 5 years to a 20-year open period again.		Legislature is expected to consider freezing the existing DB plan and providing a different plan for new hires. The new plan will be either a pure DC plan or a hybrid plan which will include a DB plan with a 1% multiplier combined with a DC contribution. Retirement eligibility will be based upon Social Security eligibility. The new plan would be for all public employees, including public safety, firefighters, judges, teachers, and others. Existing employees may have their 30-year at any age retirement moved incrementally to 35-year eligibility, and public safety and firefighters may move from 20- to 25-year retirement eligibility. Since the existing plans are noncontributory, members cannot be asked to pay into the system. The new plan will have a contributory element.
VA			Temporarily suspended 120/80 funding corridor; "substantial asset losses have been recovered since the valuation date, and a 5-year projection of contribution rates shows little difference with or without the corridor."	The legislative watchdog agency, JLARC, issued a study on state employee compensation in December 2008, which devotes a chapter to retirement benefits and presents a number of changes in plan design that would produce either short or long-term savings.	The VRS Board is requesting an increase in contribution rates for state employees and school teachers, currently funded at 11.26% and 13.81% respectively, to 13.46% and 17.91%. Requested rates are unlikely to be funded, however, due to major budget reductions. When the General Assembly convenes in January, numerous proposals are expected. Among those that will gain most attention are 1) phase in a mandatory employee contribution that was eliminated in the 1980's; 2) revise the COLA formula to change the manner in which it matches the CPI; and 3) increase the age at which new members can qualify for an early unreduced retirement benefit.

Sources: Retirement systems, NCSL, media reports

Responses to 2008 market decline and rising pension costs

State	Contribution Rates	Benefits	Actuarial Methods/Processes	Study Commissions	Proposed Changes
VT			Legislature extended funding period of the VRS from 2018 to 2039.	Legislature created a commission to review and report on the design and funding of retirement and retiree health benefit plans for state employees and teachers. The commission is charged with making recommendations about plan design, benefit provisions, and appropriate funding sources, along with other recommendations it deems appropriate for consideration, consistent with actuarial and governmental accounting standards, as well as demographic and workforce trends and the long-term sustainability of the benefit programs. The joint fiscal committee may provide benchmark targets reducing the rate of expenditure growth for retirement and retiree health benefits to the commission to guide the development of recommendations.	
WA			Legislature directed reduction in salary growth assumption, from 4.25% to 4.0%; postponed adoption of revised mortality tables and minimum required contribution rates; and directed that new funding method be phased in, saving an estimated $450 million over the biennium.		
WI	The WRS governing board increased the 2010 contribution rates by 0.6% for general category employees, of which 0.3% is on the employer portion and the other 0.3% is on an employee-related portion (which the employer can agree to pay). The rates for general category employees were 10.4% of salary in 2009 and will be 11.0% of salary in 2010.	Generally, monthly annuities on the Core Fund component of plan benefits decreased 2.1% effective May 1, 2009 as a result of the 2008 market decline. In addition, monthly annuities on the Variable Fund (a voluntary all-stock option) portion of plan benefits decreased 42% effective May 1, 2009 as a result of the 2008 market decline.			
WV		Legislature established new, consolidated statewide plan for new public safety hires, featuring lower benefits and 40-year funding bases.			
WY					Legislature is expected to consider higher employer and employee contributions. Also, a closed plan for firefighters is considering increasing its amortization period from 10 years to 20.

Legal Advisory Report, Ice Miller, LLP

Report begins next page.

VERMONT COMMISSION ON DESIGN AND FUNDING OF RETIREMENT AND RETIREE HEALTH BENEFITS

LEGAL ADVISORY REPORT

Preliminary Draft

Attorney-Client Communications

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REVIEW OF VERMONT LAW AND ANALYSIS:

Beth Pearce
VERMONT STATE TREASURER'S OFFICE

October 5, 2009

I/2375859.7

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I. INTRODUCTION

Pursuant to a Request for Proposals ("RFP"), Ice Miller LLP ("Ice Miller") was retained by the Vermont Commission on Design and Funding of Retirement and Retiree Health Benefits Plans for State Employees and Teachers ("Commission") to perform the following services: (a) Review constitutional, legal, and contractual issues relative to the provision of, and revision thereto, of governmental pension and retiree health benefits; (b) Advise the Commission on the legality, under state and federal law, of options to modify existing Vermont State benefit design, structure, and contribution levels consistent with the charge of the Commission; (c) Review proposed pension benefit, design, or contribution level revisions to assure compliance with IRS and other regulatory compliance for governmental plans; and (d) Provide other legal consultation services as requested by the Commission.

This report addresses (a) and (b) described in that RFP.

Ice Miller works with retirement systems in 32 states and has had the opportunity to review the constitutional and state law protections in most of those states. The purpose of this report is to provide you with an overview of those constitutional and state law protections, and then to identify how Vermont fits into that overview. A detailed summary of state constitutional provisions and cases is attached as Appendix A to this report.

Vermont state employees participate in the Vermont State Retirement System ("VSRS"). Vermont public school teachers participate in the Vermont State Teachers' Retirement System ("VSTRS"). The Vermont municipal employers and their employees may participate in the Vermont Municipal Employees' Retirement System ("VMERS"). We will address solely the VSRS and VSTRS in this report.

The purpose of this report is not to recommend or suggest any particular changes to the benefit structure, but rather to provide background on the legal issues associated with changes. Of course, any decisions on benefit changes would also require consideration of many other ramifications, to identify but a few:

- sufficiency of benefits,
- competitiveness of total benefit package for public employees,
- effects of changes on retirement decisions, retention, recruitment, and workforce demographics,
- effects on funded status, and
- employee and employer contribution needs.

This report cannot predict the outcome of any particular litigation. The outcome of litigation depends on the specific facts and issues that are presented, how the litigants argue their respective cases, and how a court applies the law. The Vermont Attorney General's office is responsible for advising state agencies directly on these matters.

II. FRAMEWORK FOR ANALYSIS

A. Federal Constitutional and Common Law

1. The Contract Clause

Article I, section 10, clause 1 of the United States Constitution states: "No State shall ... pass any ... Law impairing the Obligation of Contracts." ("Contract Clause"). This clause applies only to the States (the Due Process Clause applies to the federal government and provides similar protection). There is no specific definition of what constitutes a contract or whether pension obligations are covered.

The Contract Clause was drafted to prevent states from enacting debtor relief laws, but under Chief Justice Marshall the Contract Clause was given an expansive reading to prohibit states from impairing agreements to which the state was a party. Ronald D. Rotunda and John E. Nowak, Treatise on Constitutional Law § 15.8 (4th ed. 2007) ("Rotunda and Nowak").

2. The U.S. Trust Case

In 1977 the United States Supreme Court issued United States Trust Co. v. New Jersey, 431 U.S. 1 (1977). In this case the New Jersey legislature sought to repeal legislation implementing a limitation agreement which was designed to reassure Port Authority bondholders regarding the financial security of the bonds. The Court found that because the legislation was seeking to relieve the state of its own obligations, deference to legislative judgment was not appropriate. Therefore, the Court assessed whether the state's action was "necessary and reasonable." The Court found the law to be neither, because alternative means were available to promote the goals of the legislation.

Any analysis of state action needs to consider the possible applicability of the Contract Clause. If federal courts were to treat governmental pensions as constituting contracts (to whatever degree), the courts could follow basic three-step analysis for determining whether legislation which impairs the contractual obligations of a governmental unit violates the Contract Clause:

a. Step One: Contractual Relationship: Does a contractual relationship exist? The Supreme Court has stated that "[i]n general, a statute is itself treated as a contract when the language and circumstances evince a legislative intent to create private rights of a contractual nature enforceable against the State." United States Trust Co., 431 U.S. at 17, n.14. Additionally, "the obligations of a contract long have been regarded as including not only the express terms but also the contemporaneous state law pertaining to interpretation and enforcement." Id. at 19, n.17.

b. Step Two: Substantial Impairment: Does the legislation constitute a substantial impairment of a contractual relationship?

(i) Rights v. Remedies. There is no clear distinction between rights and remedies, but laws regulating only the form of remedies to enforce state obligations may be considered an insubstantial impairment of the contract.

(ii) Reservation of Right to Modify. From the beginning, the Supreme Court has held that, if a state reserved the right to modify the terms of the contract, either by a provision in the contract or a general statutory scheme, the state could subsequently modify the contract without violating the Contract Clause. See, e.g., Trustees of Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518, 666 (1819) (Story, J. concurring opinion). However, later cases have required a very explicit reservation to allow modification if a third party has accrued rights under the contract—a general reservation is insufficient. If a state explicitly reserves the right to modify benefit levels, any subsequent modification may be considered an insubstantial impairment. See Rotunda and Nowak.

c. Step Three: Narrowly Tailored to Serve a Public Purpose: Is the law that impairs the obligation justified by a significant and legitimate public purpose? Is the method used to advance the public purpose reasonable and necessary?

(i) Police Powers v. Economic Obligations. A state cannot bargain away its police powers, which are necessary for the protection of the health and safety of its citizens. However, states will be held to their economic obligations if unrelated to a police power. See Rotunda and Nowak.

(ii) Reasonable. Whether a method is reasonable should be judged in light of whether the effects which the legislation is seeking to remedy "were unforeseen and unintended by the legislature" when the statute creating those obligations and rights was adopted. United States Trust Co., 431 U.S. at 27.

(iii) Necessary. To be considered necessary, two conditions must be satisfied. First, no less drastic modification could have been implemented. Second, the state could not have achieved its stated goals without the modification. Id. at 29-30.

B. Overview of Other State Laws

We have attached to this report a multi-state survey of constitutional provisions and case law, concerning pension and retiree health benefit protections. See Appendix A.

1. Constitutional Provisions

As is indicated in Appendix A, states fall into three categories with respect to state constitutional protections for pension and retirement benefits:

a. No constitutional provision. This would the category in which Vermont would fall.

b. General constitutional protection of contracts.

c. Specific constitutional protection of pension and retirement benefits.

2. Court Interpretation of Constitutional Provisions

a. For states with no constitutional provision, a limited number of state courts have found that pensions are a gratuity to which no protection applies. Other states in this category have applied the federal Contract Clause.

b. For states where a general constitutional contract clause protection is applied to pension and retirement benefits, there is a wide variation among state courts as to when that contract clause protection vests:

(i) Upon commencement of employment

(ii) Upon commencement of participation in the plan.

(iii) After fulfilling service requirements

(iv) Upon eligibility for a pension

(v) Upon retirement.

c. For states with specific constitutional protection of pension and retirement benefits, the cases are more apt to find an earlier vesting of the contract than in those states with only a general contract clause.

d. Courts in states which recognize a constitutional protection of pension and/or retirement benefits have also recognized that benefits may be subject to modifications in limited circumstances. These limited circumstances include:

(i) Where a disadvantage is offset by an advantage.

(ii) Where a change is reasonable and necessary to preserve the pension system.

(iii) Where a change is reasonable and necessary to maintain the integrity of the pension system.

(iv) Where the creator of the plan has reserved the right to amend the plan.

We believe that preservation of the pension system may be a different concept from maintaining the integrity of the pension system. Although this difference is not fully developed in the cases, we believe that the sustainability of the pension system (funding, contribution levels, benefit levels, cash flows) is clearly the key concept in maintaining a pension system. On the other hand, integrity may encompass benefit design and benefit administration issues, such as avoiding benefit spiking, compliance with federal laws, and achieving the goals of the pension system.

3. What Generalizations are Found from Other States?

From Appendix A, there seems to be little variation among the state law decisions on the following points:

a. Those individuals who are hired after a change occurs cannot claim that their rights have been impaired.

b. On the other hand, in most states employees who are actually retired and receiving benefits are protected as to the benefit being paid (barring erroneous benefit payments, and perhaps not as to any prospective changes (e.g., COLAs) to the benefit).

c. In most states, employees who are currently eligible for an immediate benefit have protected rights to that benefit.

d. In contrast, in most states, when constitutional or statutory language specifies vesting requirements, individuals who have not satisfied those requirements probably have lesser or no protection.

As to the remaining population, there are numerous cases across the country that explore all these issues, and they reach different conclusions. We realize this is not a "bright line" situation, but rather, a complex and nuanced one.

4. Questions Left Unanswered by Court Cases

What is often left unanswered by the general holdings of existing court cases is what is the exact nature of the protection afforded by the Constitution:

a. If an employee started employment when benefits were X and benefits over time have been increased to 2X, is the employee who is still working vested in X or 2X?

b. Does the protection cover solely the "core" retirement benefit, e.g., X% times years of service times final average salary?

c. Does the protection cover any other benefits, e.g., post-retirement benefit increases, employee/employer contribution levels?

d. Does the protection extend only to benefits accrued to the date of the impairment, or to the completion of the person's career?

III. VERMONT AUTHORITY

A. Vermont Constitution

We understand from the Treasurer's office that there is nothing in the Vermont Constitution concerning contract or pension rights. This would place Vermont in the "company" of Connecticut, Delaware, Kansas, and Maryland. However, in each of these states, state courts

have established certain protections for contractual rights. Therefore, in the next section of this report, we summarize existing Vermont cases and indicate how they compare to other state law cases and the U.S. Trust case.

B. Vermont Case Law

1. Burlington Case

The first Vermont case to consider contractual rights with respect to public pensions appears to be the Burlington Fire Fighters' Association v. the City of Burlington, 543 A.2d 686 (Vt. Sup. Ct. 1988). This case involved a City retirement ordinance amendment enacted on October 29, 1984, made retroactively effective to July 1, 1983. The plaintiffs (the Burlington Fire Fighters' Association and the Burlington Fire Fighters' Officers Association) challenged the validity of the retroactive application of the ordinance. The ordinance itself contained a number of benefit improvements, but did increase both the amount (4½% to 6%) and the period (25 to 35 years) of employee contributions. The challenge was not to the City's authority to change pension benefits, but rather to apply changes retroactively. The Vermont Supreme Court found that the City had the power to enact retroactive provisions since "absent express statutory constitutional language to the contrary, the ability to enact retroactive provisions to the pension ordinance may be necessarily fairly implied from the powers which have been expressly granted . . .", citing 24 V.S.A. 1121, 1122 and Senter, 72 Vt. at 113, as well as 6 McQullin Mun. Corp. § 20.70 (3rd ed. 1988) since "(in the absence of constitutional prohibition, retroactive municipal legislation is permissible unless it interferes with contract obligations or vested rights)." The Burlington case did not consider benefit changes to VSRS or VSTRS. However, we believe that analyzing the case gives some indication of the Court's thinking on the question of what legal approach would be applied if the Vermont legislature modifies benefits for VSRS and VSTRS.

In considering contract impairment, the court found

> . . . where an employee makes mandatory contributions to a pension plan, that pension plan becomes part of the employment contract as a form of deferred compensation, the right to which is vested upon the employee's making a contribution to the pension plan. See *Snow v. Abernathy*, 331 S.2d 626, 631 (Ala.1976) (pension is vested contract right upon acceptance of plan); *Olson v. Cory*, 27 Cal.3d 532, 540, 636 P.2d 532, 537, 178 Cal.Rptr. 568, 573 (1980) (pension plans create vested contract rights accruing upon acceptance of employment); *In re State Employees' Pension Plan*, 364 A.2d 1228, 1235 (Del.1976) (pension is vested contract right for employees who fulfill pension's eligibility requirements); *Halpin v. Nebraska State Patrolmen's Retirement System*, 211 Neb. 892, 898, 320 N.W.2d 910, 914 (1982) (public employee pensions are deferred compensation and create "'reasonable expectations which are protected by the law of contracts'") (quoting *Pineman v. Oechslin*, 494 F.Supp. 525, 538 (D.Conn.1980)).

Having found a contract right, the Vermont Supreme Court then considered the Contract Clause of the United States Constitution. U.S. Const., Art. I, § 10, Cl. 1:

> To trigger the constitutional protection of the Contract Clause, there must first be an impairment of a contract. *Id.* [*United States Trust Co. v New Jersey*, 431 U.S. 1, 17, 97 S.Ct. 1505, 1515, 52 L.Ed.2d 92 (1977)]. Assuming plaintiffs establish the existence of an impairment, such impairment only violates the clause if it is not reasonable and necessary to achieve an important public purpose. *Id.* at 25, 97 S.Ct. at 1519. The United States Supreme Court has suggested that an overall determination of reasonableness be used to evaluate challenged legislation under the Contract Clause. *Id.* at 22 n. 19, 97 S.Ct. at 1517 n. 19 (citing *Home Building & Loan Ass'n v. Blaisdell*, 290 U.S. 398, 445-47, 54 S.Ct. 231, 242-43, 78 L.Ed. 413 (1934)). An employee's vested pension rights may, therefore, be modified prior to retirement if such modifications are reasonable, since it allows the pension system to adapt to changing conditions. See *Olson*, 27 Cal.3d at 541, 636 P.2d at 537, 178 Cal.Rptr. at 573; *Singer v. City of Topeka*, 227 Kan. 356, 366, 607 P.2d 467, 475 (1980); *Bakenhus*, 48 Wash.2d at 701-02, 296 P.2d at 540.
>
> [7] To be sustained as reasonable, "'alterations of employees' pension rights must bear some material relation to the theory of a pension system and its successful operation . . ..'" *Bakenhus*, 48 Wash.2d at 702, 296 P.2d at 540 (quoting *Allen v. City of Long Beach*, 45 Cal.2d 128, 131, 287 P.2d 765, 767 (1955)); see *Singer*, 227 Kan. at 366, 607 P.2d at 475. Furthermore, any changes in the plan which result in disadvantage to the employees must be accompanied by comparable new advantages. *Bakenhus*, 48 Wash.2d at 702, 296 P.2d at 540 (citing *Allen*, 45 Cal.2d at 131, 287 P.2d at 767).

The court found that:

> In the instant case, the amendments to the pension plan bear close relationship to the continued success of the pension system to meet the changing needs of municipal employees. Plaintiffs agree that the City had the power to amend the pension ordinance and that the changes made by the new ordinance are beneficial. Although the amendments have a retroactive effect, the fact that legislation is retroactive is not by itself sufficient to establish a violation of the contract clause. *United States Trust Co.*, 431 U.S. at 17, 97 S.Ct. at 1515. In this case the retroactive effect of the increased benefits is simply being offset by the requirement of retroactive contributions. In effect, we find that plaintiffs have not shown that the ordinance amendments created a constitutional impairment of their contract.

The court also rejected an equitable estoppel argument.

2. **Cases Cited by Burlington Case**

The Vermont Supreme Court cited a number of cases in the Burlington case from other states.

First, for the proposition that a right becomes vested "upon the employee's making a contribution to the pension plan" four cases were cited. This section gives additional details on those cases:

- Snow v. Abernathy, 331 So.2d 626 (Alabama Sup. Ct. 1976): Largely based on voluntary participation and employee election, case concluded that there had been a vesting of contract rights, citing Smith v. City of Dothan, 279 Ala. 571 (Alabama Sup. Ct. _____).

- Olson v. Cory, 636 P.2d 532 (Calif. Sup. Ct., 1980: Case concluded that limits on cost-of-living salary increases cannot be applied to judges who are mid-term if the judge served prior to January 1, 1977. It also discussed the rights of those in pension payment status. The court relied on "a long line" of California cases holding that a "public employee's pension rights are an integral element of compensation and a vested contractual right accruing upon acceptance of employment" citing Betto v. Board of Administration, 582 P.2d 614 (Calif. Sup. Ct.) and Kern v. City of Long Beach, 179 P.2d 799 (Calif. Sup. Ct.). The court summarized the position that while an employee does not obtain any absolute right to fixed or specific benefits, there are strict limitations on the conditions which may modify the pension system in effect during employment. Modifications must be reasonable and disadvantageous changes should be accompanied by comparable new advantages. The case did not seem to rely on voluntary contributions as a crucial factor.

- In re State Employees' Pension Plan, 364 A.2d 1228 (Del Sup. Ct. 1976): Delaware has a mandatory contribution structure. The court found that vested pension rights exist at least as to individuals who have statutory vested rights or who have otherwise fulfilled eligibility requirements for a pension.

- Halpin v. Nebraska State Patrolmen's Retirement System, 320 N.W.2d 910 (Nebraska Sup. Ct., 1982): This case involved a change to the calculation of the benefit for state police. The court found that the Nebraska statutes at issue contained no provisions preventing vesting until a certain time, thus legitimate expectations were raised that the amounts in issue would be included in the calculation.

Second, in order for the Contract Clause to apply, the Vermont Supreme Court found there must be an impairment of the contract which is not reasonable and necessary to achieve an important public purpose, such as allowing the pension system to adapt to changing conditions. The court cited three cases:

- Olson (see above).

- Bakenhus v. City of Seattle, 296 P.2d 536 (Supreme Court of Washington, 1956): Washington Supreme Court found a pension is deferred

compensation for services rendered, as a gratuity would be prohibited under the Washington Constitution as a gift of public funds, and further found that the contractual promise arises at employment. The court found this contract was for a "substantial pension" at the time of fulfillment of the prescribed conditions. The court recognized that the pension rights could be modified prior to retirement, "but only for the purpose of keeping the pension system flexible and maintaining its integrity."

- See also Allen v. City of Long Beach, 287 P.2d 765 (California Supreme Court, 1955)

- Singer v. City of Topeka, 607 P.2d 467 (__________, 1980) See Brazleton v. Kansas Public Employees Retirement System, 607 P.2d 510 (Kansas Supreme Court) court rejected a "hard and fast rule" of no change, since there "may be times when changes are necessary to protect the financial integrity of the system or for some other compelling reason which would mandate and justify some unilateral changes."

3. Summary of Burlington Approach

The Vermont Supreme Court in the Burlington case upheld a retroactive contribution increase for a municipal plan under the theory that the ability to retroactively amend is implied from the ability to enact. However, the court placed limits on retroactive legislation in an instance where the legislation interfered with contract obligations or vested rights.

Because there is no Vermont constitutional provision on contract obligations or vested rights, the Vermont Supreme Court looked at the contract clause of the U.S. Constitution and the U.S. Trust case. Under the U.S. Trust case, there are three questions to be analyzed:

- Does a contract exist?
- Has the contract been impaired?
- Is the impairment reasonable and necessary to achieve an important public purpose?

Applying the U.S. Trust case to the facts in Burlington, the Vermont Supreme Court found that the amendments bore a close relationship to the continued success of the pension option and that the impact of the retroactive contributions was offset by enhanced benefits. In this situation, no constitutional impairment was found.

4. How Does the Burlington Approach Compare to the U.S. Trust Case and Other State Cases?

a. If/When a Contract Arises.

The cases that were cited by the Vermont Supreme Court with regard to if/when a contract arises for pension benefits do not necessarily present a consistent picture, demonstrating the challenge in reconciling cases with different facts and different underlying statutes. If the

Burlington decision indicates that all four cases should be applied, then one way to achieve that would be to use the following interpretations from the cases:

(i) A voluntary participation system creates vested contract rights when the election to participate or contribute is made by the employee.

(ii) In a mandatory system, an employee who has met statutory requirements for vesting or for a pension has contractual rights to that vested amount or that pension.

(iii) In a mandatory contribution system, an employee has the right to participate in the pension system upon employment, but has no absolute or fixed right to a benefit until the employee meets the statutory requirement for vesting or for a pension.

(iv) An impairment does not exist if there is a balance between disadvantageous and advantageous changes.

The above interpretation would be consistent with what we have previously characterized as the generally accepted position in many states and with the U.S. Trust case.

b. Whether an Impairment is Reasonable and Necessary.

The cases that were cited by the court with regard to whether an impairment was reasonable and necessary to achieve an important public purpose present a consistent picture. The cases cited would permit an impairment in the following circumstances:

(i) When the impairment is reasonable and necessary to achieve an important public pursuit such as to protect the financial integrity of the system or to keep the pension system flexible, or

(ii) When there is a compelling reason that justified unilateral actions.

This interpretation would also be consistent with the position in many states and with the U.S. Trust case.

5. Jacobs Case

The next case to consider is Jacobs v. State Teachers' Retirement System, 816 A.2d 517 (Vermont Supreme Court 2000). In this case Ms. Jacobs brought a class action suit against VSTRS to recover the amount of a service purchase plus interest, claiming the system had breached statutory and fiduciary duties to her. The question presented to the Court was whether VSTRS was protected by sovereign immunity so that Jacobs and other class members could not recover. The Court concluded that (1) the State of Vermont would ultimately be responsible for the payment of any money judgment paid to the plaintiffs and (2) the system was an arm of the state. As a result, the Court held that sovereign immunity prevents a suit for money damages absent a waiver. Ms. Jacobs took the position that under a contract theory the state had waived its immunity. Her specific claim was that VSTRS had not provided her with accurate

information and that constituted a contract breach. The Court considered this argument but did not decide whether Ms. Jacobs had established that a contract existed. Instead the Court issued a very narrow decision on the issue that a failure to provide accurate information was not a breach of contract. In its discussion of this decision, the Court stated the following:

> State-created contract rights may be entitled to constitutional protection. See Halpin, 320 N.W.2d at 914. As a result "before governmental action will be held to grant a constitutionally protected contract right, the intent to do this must be expressed in clear and unmistakable language." Robert T. Foley Co. v. Wash. Suburban Sanitary Comm'n, 289 A.2d 350, 358 (Md. 1978). Thus there is a "recognized presumption that statutory enactments do not create contractual obligations in the absence of an 'unmistakable' intent on the legislature's part to do so." McGrath, 88 F.3d at 19.

6. Summary of Jacobs Reasoning

The Jacobs case is a narrowly drawn decision. However, it is very important in the following respects:

1. At least with respect to VSTRS, it makes available the argument of sovereign immunity as a defense to legal action, although there could possibly be a waiver of that immunity for a contract breach.

2. It seems to stand for the proposition that a contract is only created through government action if the intent to create a contract is clearly and unmistakably expressed.

7. How Does the Jacobs Case Compare to Other States Case Law?

The Jacobs case addresses an issue that is an important part of the U.S. Trust analysis – has the state created a contract. The Jacobs case is very helpful in providing direction to look specifically at state legislative action to determine if a contract has been created.

8. Kaplan Case

In July, 2009, the Vermont Superior Court issued a decision in Kaplan v. Morgan Stanley & Co., 47 EBC 1891 (Vermont Sup. Ct., 2009). This case involved the Town of Stowe and its police pension programs. It was decided on a statute of limitations basis, but the court discussed equitable estoppel ("which requires a showing that a defendant's conduct in some way induced the plaintiff to delay bringing suit") and equitable tolling (which applies "either where the defendant is shown to have actively misled or prevented the plaintiff in some extraordinary way from discovering the facts essential to the filing of a timely lawsuit, or where the plaintiff has timely raised the same claim in the wrong forum").

C. Vermont Attorney General

We were supplied by the Treasurer's Office with a number of Attorney General letters and memoranda. These were not official opinions of the Attorney General. This section contains a discussion of the ones we thought would be most relevant to the Commission 's work.

1. <u>2002 McShane Memorandum</u>

On January 10, 2002, a memorandum was issued by Mike McShane, as Assistant Attorney General, regarding the potential for legal challenge if legislation was passed to establish a year of service requirement for the retiree medical state subsidy and to establish a minimum number of years of service to be eligible for a retirement benefit. The memorandum stated that:

> The Contract Clause of the United States Constitution limits the ability of states to pass laws that impair contractual obligations. The Contract Clause does not absolutely prohibit laws, which impair contractual obligations. Rather the United States Supreme Court has held that laws, which result in substantial impairment of contractual relationships, are prohibited unless the impairment is reasonable and necessary to serve an important public purposes. General Motors v. Romein, 503 U.S. 181 (1992).

This memorandum also addressed the status of Vermont state law as follows:

> I am aware of no decision from the Vermont Supreme Court that holds that the Vermont State Employees Retirement System creates contractual rights. [Footnoting that "There is a case suggesting that the municipal retirement system is contractual in nature. Burlington Fire Fighters v. City of Burlington, 149 Vt. 293."] However, most courts that have addressed this question in other states have held that public pension plans do create contractual rights.

This memorandum went on to emphasize that "[I]f it is assumed that the Retirement System creates contractual rights, the more difficult question is to whom do those rights apply." Mr. McShane then reviewed a Maine case finding that contractual rights of members not yet receiving pension benefits were not violated by changes in the system. He also commented that some state cases (not Vermont cases) suggest "there is a substantial risk in applying benefit reductions to existing employees, particularly employees who have vested."

The memorandum identified the following legal analysis, which follows the U.S. Trust approach:

> In order to successfully challenge the proposed legislative changes any plaintiff would have to establish the following:
>
> 1. That the Retirement System creates contractual rights and benefits.
> 2. That the plaintiff has rights which are protected under the contract and that those rights are impaired by the amendments.
> 3. That the impairment of rights are not reasonable and necessary to serve an important public purpose.

2. 2003 and 2005 Asay Memoranda

On June 2, 2003 [also dated May 29, 2003], a memorandum was issued by Ms. Bridget Asay, an Assistant Attorney General concerning changes to teachers' retiree health benefits. This memorandum stated that:

> The Vermont Supreme Court has not directly considered whether state retirement benefits are constitutionally protected. But the Court has recognized, in the retirement context, that "[s]tate-created contract rights may be entitled to constitutional protection." Jacobs v. State Teachers' Retirement Sys., ____ Vt. ____, 816 A.2d 517, 526 (2002). To find a constitutionally protected contract right, the State's intent to create such a right 'must be expressed in clear and unmistakable terms.' Id. The Court in Jacobs stated further that 'statutory enactments do not create contractual obligations in the absence of an 'unmistakable' intent on the legislature's part to do so.' Id.

(Note: The same language as immediately above was also used in a November 14, 2005 memorandum from Ms. Asay, again on health benefit rights.) The ultimate conclusion in both the 2003 Asay memorandum and the 2005 Asay memorandum was:

> At most, members who retired after May 22, 1996, may have constitutionally protected rights to (1) access health and medical benefits through plans approved by the Board, with the Board retaining discretion to determine the terms of those plans; and (2) have the System pay some portion of the cost of health and medical benefits, with the Board retaining discretion to determine the System's share of the cost. It is not clear whether a court would find these rights enforceable. Because the amount and scope of the benefit is left to the Board's discretion, a court might find that the Legislature did not intend to create enforceable rights. On the other hand, a court might conclude that the right to access health and medical benefits in some form is clear, and that right is valuable enough, even if retirees must pay most of the cost, to be constitutionally protected.

3. 2005 McShane and Griffin Emails

Earlier in 2005 there was an exchange of emails between the Attorney General's Office and Cynthia Webster. The original question from Ms. Webster was whether anything in the state retirement statutes directly states that it is not possible to reduce retirement benefits. Mr. McShane's response (dated March 31, 2005) was:

> There is not a specific statutory provision that so states. However, U.S. Constitution contains what is referred to as the Contract Clause. The Contract clause has been interpreted to invalidate legislation which impairs vested contract rights. The Vermont Supreme Court has discussed the contracts clause in situations which are not exactly on point. The clause is found at Article I, Section 10 of the Constitution. It is an enumeration of the powers denied to the states and quit [sic] directly states that no state shall pass a law "impairing the obligation of

contracts." Of course it is possible to change benefits for new hires but vested contract rights cannot be retroactively altered.

Mr. Griffin responded that same date that:

> I agree with Mike that 'vested contract rights cannot be retroactively altered.' The more interesting question in the context of a public retirement system is what contract rights have 'vested' and what changes might be characterized as 'retroactive.' The answers to these questions would depend on the nature of the benefits (for example, cash or insurance), the specific statutory language that governs those benefits, any statutory and plan changes over time, the extent of those changes, the circumstances of particular retirees and other factors.

Mr. Griffin then cited the Asay 2003 Memorandum and concluded:

> It is difficult to predict how the courts will ultimately decide these issues, and the outcomes may be very fact specific. To my knowledge the AG's Office has not done the research and analysis that would be needed to provide legal advice on any proposals to alter any retirement benefits other than that reflected in the Asay memorandum.

4. <u>2006 Rice Memorandum</u>

We note that there is also a June 5, 2006 memorandum from William H. Rice, Office of State Treasurer, reviewing whether the State Employee Retirement Board has the same discretion to change state retiree medical benefits as the Asay memoranda reflects for teachers' retiree medical benefits. The memorandum reviewed the statutory provisions regarding modifications of retiree medical benefits for state employees and then reviews the <u>Burlington</u> standard:

> "where an employee makes mandatory contributions to a pension plan, that pension plan becomes part of the employment contract as a form of deferred compensation, the right to which is vested upon the employee's making a contribution to the pension plan." <u>Burlington Fire Fighters Association v. City of Burlington</u>.

The memorandum further observed that the Vermont Supreme Court had determined that vested pension rights may be modified prior to retirement if such modifications are reasonable "since it allows the pension system to adopt to changing conditions." <u>Id</u>. at A.2d at 690. The memorandum also observed that the Vermont Supreme Court had:

> established a two part test of reasonability: 1) "[t]o be sustained as reasonable, alterations of employees' pension rights must bear some material relation to the theory of a pension system and its successful operation" and 2) "any changes in the plan which result in disadvantage to the employees must be accompanied by comparable new advantages." <u>Id</u>. 149 Vt. at 298, 543 A.2d at 690.

5. Summary of Attorney General Analyses

The memoranda from the Assistant Attorneys General have reviewed the Burlington case and found that it would have limited application to the question of whether state pension benefits can be modified. The memoranda have generally followed the U.S. Trust case in that a three part analysis must be followed:

1. Is there a contract and what are the terms of that contract?

2. Has that contract been impaired?

3. Is there a legally acceptable reason for that impairment?

With respect to retiree health benefits, the memoranda have not concluded whether there is state law protection for retiree health benefits, although there may be some protected rights to access.

These memoranda are very consistent with general state law principles and the U.S. Trust case. We will consider these memoranda in more detail as we consider the Commission's specific questions.

IV. APPLICATION OF CONSTITUTIONAL AND STATE LAW PRINCIPLES

A. Pension Benefits

Following the rationale in the Vermont cases (primarily Burlington and Jacobs), we have reviewed the statutes governing VSRS and VSTRS to identify statutory provisions that could be construed as clearly established contract rights with respect to pension benefits. This is in keeping with the U.S. Trust case and the AG Memoranda which set forth the first step in the analysis as identifying if a contract has arisen.

a. In this regard, we believe that in VSRS the legislature has identified an individual with 5 years of creditable service as being "vested." Such a member may allow employee contributions to remain in VSRS and "receive a deferred vested retirement allowance," based on their compensation and service at termination. (Title 3, Chapter 16, § 465)

b. With regard to VSTRS, we believe this same status is established under Title 16, Chapter 55, § 1940(a).

c. With regard to benefit payment, we also believe that the Vermont statutes establish entitlements at certain combinations of age and service. See for example Title 16, Chapter 55, § 1937(a) for VSTRS and Title 3, Chapter 16, § 455(13) for VSRS.

d. In addition, both VSTRS and VSRS are established as qualified governmental pension plans under Internal Revenue Code Sections 401(a) and 414(d). Under these Sections, benefits must be vested upon attainment of normal retirement age

and upon plan termination, to the extent funded. (***Note***: Both VSTRS and VSRS were submitted for IRS approval and those applications are still pending.)

Based upon the foregoing and applying the general principles of the state law cases and the Jacobs rationale, we believe the contractually protected members would be:

a. VSRS and VSTRS members who have reached normal retirement age are vested in their benefits because the legislature has clearly said that VSRS and VSTRS are qualified, governmental pension plans.

b. VSRS and VSTRS members who have reached eligibility for normal or early retirement benefits have a contract right in those benefits because the legislature has said that they are entitled to these benefits.

c. VSRS and VSTRS members who have at least five years of service are vested in their accrued benefit and thus have a contract right with respect to that benefit (leaving open the question of what is a member's "accrued benefit" at any point in time, and whether the protection extends to benefits not yet earned or accrued).

d. VSRS and VSTRS members who do not have five years of service are not vested in a benefit and thus have no contract right.

We realize that this analysis leaves a "middle group" (those who are vested but have not reached eligibility for a benefit) where the Commission must analyze whether a contract right exists with respect to a particular benefit feature. In this regard, we recommend that the Commission do additional fact finding with respect to any specific changes it is interested in. This would include identifying if there has been any modification to the plan with respect to that benefit feature at any time or times during the career of the middle group. This will be helpful to measure the length of time that the benefit feature has been applicable. The Commission may also wish to consider any other relevant facts concerning any new tiers or coverage changes affecting the middle group.

Under the U.S. Trust case and the state law principles, including cases cited in the Burlington case, these contractually protected benefits could be modified ("impaired") in the following situations:

a. Where a disadvantage is offset by an advantage.

b. Where the stability or the integrity of the pension system requires the change and the change is reasonable.

c. Where a compelling situation requires unilateral change.

B. Retiree Health Benefits

With regard to retiree health benefits, Title 3, Chapter 21, Section 631 provides that

"the secretary of administration may contract on behalf of the state with any insurance company ... to secure the benefits of franchise or group insurances. Beginning July 1, 1978, the terms of coverage under the policy shall be determined under section 904 of this title [collective bargaining], but may include ... hospital, surgical, and medical benefits for any class or classes of state employees or for those employees and any class or classes of their dependents. *** For purposes of group hospital-surgical-medical expense insurance, the term "employees' shall include ... former employees ... who are retired and receiving a retirement allowance from the Vermont state retirement system or the state teachers' retirement system of Vermont.

As stated in the Asay Memoranda, it is not clear from the above whether the extension of medical coverage to retirees is intended to be a contractual right by the legislature. If the a court were to find that a contract exists, it appears that the contract would only be for access to coverage, not for a particular level of benefits or for a particular level of premiums.

V. VERMONT QUESTIONS

A number of questions have been identified as being helpful to understanding how to apply the legal framework described above.

A. Pension

1. Summary of Pension Groups

a. There are four defined benefit groups under VSRS for state employees. Each group must considered separately for certain purposes:

(i) Group F for state employees

(ii) Group D for judges

(iii) Group C for state law enforcement officers

(iv) Group A original retirement plan which some members elected to remain in, and predecessor to plan F.

b. For VSTRS, there are basically two groups remaining:

(i) Group C for public school teachers employed within the State of Vermont on or after to July 1, 1990. Group B members as of on July 1, 1990, are now in Group C.

(ii) Group A for public school teachers employed within the State of Vermont prior to July 1, 1981 and elected to remain in Group A.

2. Raising Retirement Age

Questions: Can the legislature raise normal retirement and/or early retirement age for all current state employees and teachers? Certain current state employees and teachers? Non-vested state employees and teachers? Could ages be changed to reflect the Social Security structure?

Analysis: Based upon Jacobs and Burlington and the general state law principles, it appears that a court could find that the Vermont statutes are intended to create certain contractual rights in a pension benefit.

a. Assuming that a court would find that contractual rights apply, raising normal and/or early retirement ages for any member who had already reached eligibility for a retirement benefit would not be permissible without an offsetting advantage or unless reasonable and necessary to preserve the pension system.

b. It is not clear whether the court would find that a vested member who had not reached retirement age would receive the same degree of protection, or only be protected in the amount of benefit earned to the point of the change. If the court found either, the court would then likely need to decide if the change in retirement age was an impairment. If yes, then the court would likely analyze whether the impairment was reasonable and necessary to protect the financial integrity or flexibility of the pension system.

c. Because the legislation has not expressed any intent to create a contract for a non-vested member, under general state law principles, a court could uphold a change in normal and/or early retirement age for a non-vested member.

3. Revise Early Retirement Criteria

Questions: Can the following elements be modified with respect to early retirement:

- Age eligibility restriction?
- Application of penalty based on actuarial cost?

Analysis:

a. We believe changing the early retirement age would follow the analysis outlined in 1 above.

b. As to changes in the actuarial reduction factors, a good argument can be made that this either is not a contractually protected provision, or even if it is a protected provisions, reasonable modifications should be considered as a reasonable and necessary actions to retain the integrity of the plan. Actuarial factors, such as life expectancy, change over time. Boards typically retain the ability to review their plan's actuarial experience and modify assumptions and factors based on the actuary's recommendations. We see this as presenting different arguments than changing the age. As to the first

question, whether it is a contractually protected benefit, we note Title 3, Chapter 16, § 459(d) provides early retirement reduction factors as follows:

(i) Group A (except DOC facility employees) – early retirement is "actuarial equivalent of normal retirement allowance." "Actuarial Equivalent" is defined in § 455(a)(2) as "a benefit of equal value under the actuarial assumptions last adopted by the retirement board under subsection 472(a)(h)." That subsection gives the board the express right to modify the assumption by resolution.

(ii) Group F (except for certain exceptions) – early retirement is reduced by .5%/month under age 62; although if a group member first participated on or after July 1, 2008 the reduction varied by years of service but was measured from 65.

(iii) Group D – early retirement reduced by .25%/month under age 62.

Therefore, it seems clear the legislature reserved the right to change the assumptions for Group A. Groups D and F are less clear as to whether there is a contract right in the early reduction factor. If the court found there was, it would then likely analyze whether the impairment was reasonable and necessary to protect the financial integrity or flexibility of the plan. One question to consider is whether the reductions for Groups F and D represent actuarial reductions as of the time that they were implemented (o/a 1990)

c. Group C is entitled to retire at age 50 with 20 years of service without penalty for early retirement. Without a showing of necessity, we do not believe that these eligibility conditions could be changed for a member who has reached either the normal retirement of 55 or the early retirement of 50 and 20.

If the Commission wishes to consider changes in this category, it may wish to identify all the requirements for each group and plan for early retirement and normal retirement and create a protected category in each group and plan of all members who meet those requirements. We also think the Commission would want to review what changes (if any) had been made in the different factors over time. Lastly, the Commission will want to have an actuary consider whether the factors would be different today if they were to be "actuarial equivalents" of the unreduced benefit.

4. Increase Employee Contribution Rates For All Groups and Consider Appropriate Contribution Rates for Different Groups or Plans

Questions: Would it be possible to raise contribution rates for all current state employees and teachers, in order to provide long-term sustainability for the current plan and benefit levels? Certain current state employees and teachers? Non-vested state employees and teachers? Would it be possible to tie employee contributions to salary or age?

Analysis:

a. Title 3, Chapter 16, § 473(b) establishes employee contribution rates as follows:

(i) Group A: The amounts so allocated as regular contributions shall be determined as if the rate of contribution of four percent has been continuously in effect in the predecessor system from which such amounts were transferred and the balance of any amount so transferred on account of any group A member shall be deemed additional contributions. In the case of group C members who were members as of the date of establishment and D members all contributions transferred from predecessor systems shall be deemed regular contributions. Those members who, prior to the date of establishment of this system, had been contributing at a rate less than four percent shall have any benefit otherwise payable on their behalf actuarially reduced to reflect such prior contribution rate of less than four percent.

(ii) Groups C and F: Contributions shall be made on and after the date of establishment at the rate of five percent of compensation except at a rate of 6.18 percent of compensation for each group C member unless the member was a group C member on June 30, 1998 in which case contributions shall be at the rate of six percent of compensation for each group C member who has elected not to have his or her compensation from the state be subject to Social Security withholding or at the rate of five percent of compensation if the member elected to have compensation from the state subject to Social Security withholding and at the rate of five percent of compensation of each group F member and, commencing July 1, 2019, at the rate of 4.75 percent of compensation for each group F member.

Consequently, it appears as though the legislature has already changed the employee contribution rates in the past, sometimes with some "grandfathering." We are unaware that there has been any contract impairment found. This would suggest that there was not a reasonable expectation of a contract right to a particular rate for the entire career. The Commission would likely want to have a complete history of the different contribution rates and the previous changes, as well as an actuarial study giving the effect on the rates.

b. As provided in state cases, if there is a contract right in a particular rate, any increase in contribution rates can be deemed appropriate if offset by benefit improvements. Additionally, if increased contributions were reasonable and necessary to maintain the retirement system, state cases would support the proposition that contributions could be increased without a benefit improvement. The U.S. Trust case would support the proposition that a change in a contract (if it existed) could be modified if reasonable and necessary.

c. We would have to research decisions and guidance under the Age Discrimination and Employment Act if the Commission wishes to consider age based contributions. There has been litigation on that issue.

5. Revise Multiplier Used to Calculate Benefits for All Groups and Plans

Questions: Can the legislature change the multiplier going forward for all current state employees and teachers? Certain current state employees and teachers? Non-vested state employees and teachers? ***Note:*** Assume that for the time already earned, the current multiplier would be used, but going forward a lower multiplier would be used.

Analysis:

The general state law principles and the Vermont cases do not provide any guidance on whether there is a contract right that prevents prospective changes in the multiplier. In certain states that follow a strict contract law approach, a prospective change in a multiplier would be considered a contract impairment. If we looked to federal law, this approach would be permitted since only the benefit accrued (or earned) to the date of the change would be preserved.

We think there would likely be no contract right for the non-vested employees and teachers. We also believe that based upon the AG Memoranda and the state case law principles it would be defensible to take the position that prospective multiplier changes are permissible

6. Revise Vesting Period

Questions: Can the legislature change things like vesting period (5 to 10 years) for all current state employees and teachers? Certain current state employees and teachers? Non-vested state employees and teachers?

Analysis: "Vesting" is established by Title 3, Chapter 16, § 465(a), as five years for a deferred vested retirement allowance. Under the general state law principles, we believe that a court would hold that increasing the number of years would not be permissible for a member who already had five years unless there was an offsetting advantage or unless the change was reasonable and necessary to preserve the pension system. For non-vested members, we believe the change would likely be permitted.

7. Define Types of Income Eligible for Calculation of Average Final Compensation (AFC)

Question: Can the elements of AFC be modified? Based upon our conversations with retirement system staff, we understand the definition of AFC to be described as follows:

a. VSRS Group A is a closed group with just a few members. AFC for this group is similar to Group C, that is, the highest 3 consecutive fiscal years, or the last 36 months including unused annual leave pay off.

b. VSRS Group B is a closed non-contributory group with just a few active members.

c. VSRS Group C (Public Safety): AFC is the average of gross pay for the last 24 months of employment or any 2 consecutive fiscal years. AFC consists of gross pay, but does not include the payment of unused sick leave, except that ½ of the time period of sick leave at the final annual salary can be substituted for the period of lowest pay. Contributions are not made on this amount. With regard to State Troopers, there is a cap on the amount of overtime that can be counted.

d. VSRS Group D (Judges): AFC consists of the statutory pay for the year in which the judge retires. For example, if the legislature sets the annual salary rate at $125,000 for FYE June 2010, then the AFC for a judge who retires in that Fiscal Year is $125,000 regardless of whether the judge has received $125,000 by the time he/she retires.

e. VSRS Group E is a closed plan.

f. VSRS Group F (most State employees): AFC is the average of gross pay for 3 consecutive fiscal year or the last 36 months of employment. AFC excludes unused annual leave pay off. AFC includes compensatory time and personal time. Contributions are also made on these amounts.

g. VSTRS Group A (Only 25 left): AFC is the highest 3 consecutive years, including unused annual leave, such leave, and bonus/incentives.

h. VSTRS Group C: AFC is the 3 consecutive year average. AFC is based upon what they earn as teacher plus compensation for extracurricular activities. This is the same base for benefits and contributions. AFC cannot include any retirement incentives. The Board has to approve any increase that exceeds 10% year to year.

i. VSTRS Group B is closed.

Analysis: The pension contract (to the extent it exists) likely includes the definition of AFC. "Average final compensation" is defined in Title 3, Chapter 16, § 455(a)(4). In every case except judges, the term refers to "average annual earnable compensation." Title 3, Chapter 16, § 455(a)(8) defines that as the full rate of compensation that would be payable to an employee if the employee worked the full normal working time for the employee's position. Therefore, in general, the definition of AFC would be considered part of the benefit that is vested and/or protected for employees – so that protected categories would include vested members and members eligible for a benefit. However, it may be that a change for a member of a protected group would be permissible if the change was needed for integrity of the retirement system – for example, to prevent benefit spiking. In addition, the Commission may want to review when any prior changes to the definition occurred in VSRS Groups C and F and VSTRS Group C.

8. **Review Impact of Going From a Three Year to Five Year Salary Calculation for AFC**

Question: Can the calculation of AFC be expanded to include 5 years instead of 3?

Analysis: As to the first point of whether there is a constitutionally protected benefit, the normal retirement benefit for groups in VSRS is based on "average final compensation"(except for judges, which is based on their salary). Title 3, Chapter 16, § 459. "Average final compensation" is defined in Title 3, Chapter 16, § 455(a)(4) as the "average annual earnable compensation" in the three (for Group A and F: two for Group C) consecutive fiscal years or last three (two) employment years. Therefore, as noted above, the definition of AFC would be considered part of the benefit that is vested and/or protected for employees – so that protected categories would include vested members and members eligible for a benefit.

If the Commission is interested in further considering this, the Commission may also want to consider whether a special protected group of those within 3 or 5 years of retirement eligibility should be created, so that any change here would allow some additional security for that population.

9. **Revise COLA Changes and Revise Definition of CPI**

Questions: Can COLAs be changed, including a revision to the definition of CPI?

Analysis: Title 3, Chapter 16, § 470 establishes the COLA provisions. Every group has a COLA based on CPI. For some group it is either a full or half-COLA. Group A, C and D's COLA is as follows:

> as of June 30 in each year, commencing June 30, 1972, a determination shall be made of the increase or decrease, to the nearest one-tenth of a percent, in the ratio of the average of the Consumer Price Index for the month ending on that date to the average of said index for the month ending on June 30, 1971 or the month ending on June 30 of the most recent year subsequent thereto as of which an increase or decrease in retirement allowance was made. If the increase or decrease, so determined, equals or exceeds one percent, the retirement allowance of each beneficiary in receipt of an allowance for at least one year on the next following December 31st shall be increase or decreased, as the case may be, by an equal percentage. Such increased or decrease shall commence on the January 1st immediately following such December 31st. Such percentage increase or decrease shall also be made in the retirement allowance payable to the beneficiary in receipt of an allowance under an optional election, provided the member on whose account the allowance is payable and such other person shall have received a total of at least 12 monthly payments

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by such December 31st. The maximum adjustment of any retirement allowance resulting from any such determination shall be five percent and the minimum shall be one percent, and no retirement allowance shall be reduced below the amount payable to the beneficiary without regard to the provisions of this section.

Group F members' COLA is as follows:

> as of June 30 in each year, commencing January 1, 1991, a determination shall be made of the increase and decrease, to the nearest one-tenth of a percent of the Consumer Price Index for the preceding fiscal year. The retirement allowance of each beneficiary is receipt of an allowance for at least one year on the next following December 31st shall be increased or decreased, as the case may be, by an amount equal to one-half of the percentage increase or decrease. Commencing January 1, 2014, the retirement allowance of each beneficiary who was an active contributing member of the group F plan as of June 30, 2008 and who retires on or after July 1, 2008 shall be increased or decreased, as the case may be, by an equal percentage of the Consumer Price Index for the preceding year. The increase or decrease shall commence on the January 1st immediately following such December 31st. The adjustment shall apply to group F members receiving an early retirement allowance only in the year following attainment of age 62, provided the member has received benefits for at least 12 months as of December 31 of the year preceding any January adjustment. The maximum adjustment of any retirement allowance resulting from any such determination shall be five percent and the minimum shall be one percent, and no retirement allowance shall be reduced below the amount payable to the beneficiary without regard to the provisions of this section.

The language of the statute provides that benefits "shall be increased or decreased" indicating that in specified circumstances the benefits shall be adjusted up or down as a result of CPI. This would seem to mean that a decrease resulting from CPI would be part of the contract and/or there has been a reservation of rights to amend the contract.

10. <u>Review Potential of Limiting Allowable Earnings After Retirement</u>

a. <u>VSTRS</u>: Teachers may "retire" and receive a pension so long as they occupy a non-qualified position – that is, a position that is not covered by VSTRS. If a retired teacher returns to a position covered by VSTRS, then the retiree is not allowed to earn more than 60% of a teacher's salary.

b. VSRS: A retired state employee may not return to active permanent employment. However, a retired state employee may return to a temporary or contractual position.

Analysis: As noted in Section VI, state law changes with regard to the reemployment of retirees have been made in other states. This is an area where, if a contractual right is found, changes may be made to preserve a pension system's integrity.

11. Member Options

Questions: Could the legislation offer an option to all current state employees and teachers for an increase in the employee contribution rate to retain existing benefit levels versus retaining the existing contribution rate but with reductions in some of the benefit levels and/or plan provisions? Certain current state employees and teachers? Non-vested state employees and teachers?

Analysis: There is no clear guidance on this point under the Vermont cases, but we believe the analysis would be similar to that above.

However, an additional concern would be that the Internal Revenue Service is very restrictive on elections with respect to employee levels of contributions if those contributions are pre-tax. Thus, additional tax analysis would be needed if the Commission is interested in pursuing any solutions involving member options.

B. Retiree Health Care

The Treasurer's Office has advised us that a couple of years ago, Vermont instituted, in legislation, a new tiered retiree health coverage plan for new state employees. Instead of being able to get 80% coverage retiring after 5 years of service and age 55, new state employees must work 10 years to get 40% coverage, 15 years for 60% coverage, and 20 years for 80%. Could the legislation apply that system to all current employees? Certain current employees? Same question for teachers.

Analysis: Based upon the Jacobs analysis, it is not clear that any contract has been established with respect to any term of retiree health coverage for retirees. Therefore, it may be permissible to make any of these changes.

- Could the legislature provide no retiree health benefits for new state employees and/or teachers?

Analysis: We believe the answer is yes.

- Can the legislature change retiree health coverage for already retired state employees and/or teachers?

Analysis: We do not believe that the legislature has established any right to health insurance other than coverage under the program. It appears that the terms of that coverage can be modified.

VI. RECENT STATE ACTIVITY

A. Pensions

Many other states are considering a range of pension and/or retiree medical changes, and in some cases have actually passed legislation containing changes. We thought the Commission would want to be aware of this activity. For this discussion we relied heavily on a National Council of State Legislatures ("NCSL") report ("State Revisions and Retirement Legislation 2009"), dated August 17, 2009, as well as information from the National Association of State Retirement Administrators ("NASRA"). See also "Trends in Public Sector Retirement Systems" presented in Commission's August 20, 2009 meeting.

The changes may be briefly summarized as follows.

a. **Changes for New Hires**. Six states created new benefit structures for new hires. In two of those states (Georgia and Louisiana) the primary effect was an elimination (Georgia) or limitation (Louisiana) on post-retirement benefit increases. In the other four (Nevada, New Mexico, Rhode Island and Texas), the changes were more extensive – affecting retirement ages, service requirements, the amount of the benefit or COLA, and/or the amount of the reduction for any early retirement. The other type of change for new hires was to change employee contribution. For example, New Hampshire increased the employee contribution from 5% to 7% for new members (effective July 1, 2009).

b. **Employee Contribution Changes for Existing Employees**. Nebraska and New Mexico and Texas increased employee contributions for existing employees (1% increase in Nebraska for school employees for five years, 2% increase for state patrol and a 1.5% increase in New Mexico for two years, and a .45% increase for Texas ERS members). Employee unions in New Mexico have brought action to overturn these changes as unconstitutional. Texas also added an employee contribution (.5%) in a previously non-contributing plan (law enforcement and custodial members).

c. **Benefit Changes for Current Employees**. Bills were passed in a few states that impacted current members. Those changes tended to be very targeted at particular features. Notable examples include the following:

- eliminated of ability of elected officials to be credited with a full year's credit for as little as one day of service and/or receive a "termination allowance" (Massachusetts),
- eliminated "out-of-grade" accidental disability pensions (Massachusetts),
- revised the compensation definition for benefit calculations (Massachusetts),

- imposed a period of separation before retiree could be retired
  - 90 days (Texas ERS)
  - 180 days (Arkansas)
  - 60 days (Kansas) (Note: Kansas also imposed special payments for employees and employers for rehired retirees),
- imposed restrictions on working in retirement for certain elected officials (West Virginia),
- imposed suspension of retirement benefit for rehired retiree less than NRA (Georgia),
- suspension of benefits in certain reemployment situations (Indiana).

d. **<u>Benefit Reductions for Current Retirees</u>**. None, except a few COLA changes.

B. <u>Health</u>

The accounting changes imposed by the Government Accounting Standards Board have caused many states to review their benefits and their funding for retiree health care. See "Trends in Public Sector Post Retirement Health Care Benefits" in Commission's August 20, 2009 materials for general summary.

There were changes to retiree health programs in the 2009 sessions. Examples include the following:

a. New Hampshire (added withholding to help fund retiree health coverage).

b. New Mexico (increased employer and employee contributions to fund).

c. Creation of new funding vehicles for retiree medical (Georgia, Delaware, Alaska).

d. Kentucky (established employer rate schedule for retiree medical).

JAMES H. DOUGLAS
GOVERNOR

State of Vermont
OFFICE OF THE GOVERNOR

State of the State Address
January 7, 2010

Mr. President, Mr. Speaker, members of the General Assembly, distinguished guests, my fellow Vermonters:

Before I begin today, I want to acknowledge the loss of two dedicated public servants, Representative Ira Trombley and Representative Rick Hube. Our thoughts are with their families and we are grateful for their contributions to our state.

* * *

Each morning the people of our state awake with a simple hope: to build a better future for themselves, their families and the generations that will follow. Throughout our history, Vermonters have mustered the strength to meet each day with the wisdom, ingenuity, and tireless work ethic of our Yankee forebearers.

From towns, villages and cities, they've elected representatives to bring that same focus to the People's House. It is here where we carry forth our proud tradition of self-government – always striving to forge a state, nation and world better than before.

Today, that work is far from done. In these uncertain times, we must transform our public and economic framework by redesigning how we deliver state services and refocusing efforts to create jobs and ensure economic security for Vermonters. Out of necessity and because it is the right thing to do, we must act now to write the next chapter in the proud history of Vermont.

* * *

As we gather to embark on this work, let us keep in mind our friends and neighbors serving in Iraq and Afghanistan, and those preparing to leave. Our service men and women are asked to defend self-government and individual freedom in a part of the world where there is too little of both. Their efforts contribute to a noble legacy forged by Vermonters from the Battle of Bennington to Cedar Creek, from the beaches of Normandy to the streets of Baghdad. These brave men and women embody the best of the Vermont spirit and their sacrifice inspires us all.

* * *

I've seen, time and again, the will of Vermonters to change, reform and make better this great state. I've seen what can be accomplished when we work together, putting the public good before self interest. Indeed, the last decade has been full of such accomplishments.

When it comes to keeping our neighborhoods safe, there will always be more to do, but our shared commitment gives me confidence that we will be ever vigilant. I'm proud that we have worked together to send a clear message to sexual predators that they will be prosecuted and severely punished in Vermont. And while illicit drugs still destroy too many young lives, the DETER program has increased our efforts with better education, prevention, treatment and rehabilitation for those who suffer from addiction, as well as strengthened enforcement against drug dealers.

* * *

Vermont's commitment to our natural resources is unwavering. The Clean and Clear Action Plan is a model for how government, citizen groups, farmers and others can work together to reduce pollution in our waterways. We've led on climate change by partnering with other northeastern states in the Regional Greenhouse Gas Initiative. And we were the first state to join California in adopting more stringent standards for automobile emissions, ultimately forcing the federal government to follow our lead. Our environmental leadership is a source of pride that sets us apart and gives us a leg-up in the green economy.

* * *

That Vermont is the healthiest state comes as no surprise. It's in our nature to be active, enjoy our outdoors, and eat healthy. We've taken our message to young Vermonters with our Fit and Healthy Kids program, to working Vermonters with our Worksite Wellness programs and to older Vermonters with my Commission on Healthy Aging. And we've achieved groundbreaking health reforms with our innovative Blueprint for Health, the Global Commitment waiver and Catamount Health. In just two years, we have seen our uninsured rate drop by 25 percent. And with the Blueprint, we're beginning to bend the curve on costs. By combining coordinated care, health information technology and payment system reform, we are eliminating duplicative, unnecessary services and creating a more efficient and effective health care system.

These common sense approaches are not only being emulated in Washington; they are delivering real results here at home. Rhonda Rose of St. Johnsbury is a Blueprint for Health success story. Rhonda's chronic illness was a significant challenge, draining her bank account, as well as drawing heavily on state resources. Her local community health team stepped in and made a full assessment, taking the necessary actions to get her health back on track and prevent expensive emergency room visits. Not only has Rhonda's health improved, but she's been able to go back to work and is enjoying life again. I'm very pleased that Rhonda can join us in the balcony today.

As we look to make programs and services better and more affordable, we need only to look to these achievements, particularly in health care, as a beacon for the kind of positive change that's possible when we work together toward a common goal. In that spirit we must partner again.

* * *

Our successes are threatened by massive budget shortfalls, unfunded liabilities and a broken system of education funding. Working families have been battered by recession and employers weakened by state policies that are barriers to job creation.

The trajectory of the Vermont economy for the next decade will be shaped by our decisions this year. If we are content to limp out of this recession, hobbled by flat job growth, we can choose to recycle old ideas and hope for a different outcome. But if we want to spring out of this recession – strong and nimble – we must have the heart to reform, the wisdom to act and the courage to stand against those who will say it cannot be done.

Mere "recovery" is not enough for Vermonters who have persevered through this long season of decline. We must strive for a healthy and growing economy, prepared to compete with states next door and countries around the world. Prepared to compete – and win.

These times demand new thinking – they demand bold action – and they demand it now.

* * *

A balanced and responsible budget is at the core of getting our state on track. Make no mistake: there will be many unenviable choices among worthy priorities. The solutions required to close the gap will invariably draw objection and complaint. Although we will consider constructive alternatives, this is not the time nor the place for the reflexive defense of the status quo.

If we put off hard decisions for yet another year, we will be left with a cumulative deficit of a half billion dollars over the next three years – our worst choice, by far.

Two days ago, we took an important step in the right direction when I was joined by legislative leaders to announce the results of our collaborative effort to find sustainable savings.

Representatives Obuchowski and Sweaney, Senator Snelling and my Administration worked together on a plan that will save $38 million in the General Fund next year – resulting in millions more in savings down the road. This is the type of break from business-as-usual that is essential for our success. By setting this agreement in law by the end of this month, we can move forward with greater certainty on the tougher budget challenges ahead.

* * *

Access to our courts and the timely resolution of cases is one of the fundamental obligations of state government. Ensuring that Vermont's judicial system is financially sustainable is of utmost importance. In the past year, the Judiciary has pitched in to help meet our fiscal challenges. While furloughs and occasional Court closings were necessary, they are not acceptable long-term solutions.

The recommendations of the Commission on Judicial Operations provide a blueprint for a stronger and more affordable system of justice. I know some ideas are controversial; some changes depart from long-held traditions; and the necessary rebalancing will affect certain districts and constituencies. But like all of our decisions this year, narrow interests must take a backseat to the broader public interest. The General Assembly must give these recommendations due consideration, finding in them, as I have, a path forward.

* * *

These are just two steps in the process of building a balanced, responsible and sustainable budget. The spending plan I will present on January 19th will be informed by these and other efforts underway to address our $150 million General Fund shortfall.

With 40 percent of the total state budget spent in human services, many of the tough choices we must make will affect this system. Service providers will be asked to find efficiencies. Some beneficiaries will have to accept reductions in order to preserve benefits for the most vulnerable. Still some programs and grants will be significantly reduced or eliminated. But we will lessen these impacts by redesigning how we deliver services. To assure that Vermont's safety net is sound even in the most challenging economic times, we must reform.

Our redesigned system will be easy to navigate, with a single point of entry and flexible options, catering to individual needs. We will work with service providers to ease their administrative burden. Our focus will be on outcomes for Vermonters – providing a clear and direct path back to health, employment and independence. Success will be measured not by how much we give, but by how well we help Vermonters move from assistance to self-sufficiency.

* * *

While our budget deficits are daunting, we must always keep in mind that they are a symptom – not the cause – of the everyday challenges of the people of our state. Last year, Vermonters median household income fell by nearly $1,900 from the year before. Our workforce shed more than 10,000 jobs since October 2008. And Vermont's population is among the slowest growing in the nation, with more people leaving the Green Mountain State than moving in.

These numbers tell a sobering story. If we want to keep the jobs we have, if we want to get our small businesses to succeed in a global economy, if we want to attract rather than turn away people and potential companies, then we need to focus on the fundamentals.

Employers of all sizes, in all sectors, have made clear what they need to restart the engine of our prosperity: lower taxes; universal broadband and wireless; reliable, affordable energy; a well-trained workforce; and an education system that is top-notch without being top-dollar.

A Vermonter who is employed doesn't need an unemployment check; a Vermonter earning a good wage doesn't need state assistance to help pay the bills; and a young Vermonter with a stable job can put down roots and strengthen a community. That's why I call on lawmakers to join me in putting the economic success of Vermonters first.

* * *

The single most consequential action we can take to encourage a healthy economy is to address the crushing weight of Vermont's tax burden. Time and again, employers tell me that our heavy taxation is stifling job creation, making it more difficult to retain our next generation. Increasing taxes, yet again, would only hasten our disturbing demographic and employment trends.

To spur job growth, we need to take steps to roll back last year's key tax increases, encourage growing companies with proven incentives and shore up the unemployment insurance trust fund with a responsible, balanced approach.

* * *

As you might remember, I opposed the income and estate tax increases passed by this Assembly last year. Those changes have swelled the ranks of Vermonters who are looking at other states – like New Hampshire or Florida – for their new, permanent residences.

For those who are quick to say "good riddance," think again. When we lose a long-time Vermonter to another state, we lose the community involvement, we lose the charitable giving, and we lose those deep roots that give Vermont its unique character – not to mention the tax revenue.

While my first choice would be to unwind all of the increases at once, that is not feasible in the face of our current condition. Instead, we must address the critical components most detrimental to job creation as soon as possible and commit to buy back all of the increases – plus make additional tax cuts when the economy improves.

* * *

Governor Dick Snelling's plan to respond to the recession of the early 1990's was invoked many times last year to justify tax increases. But one key element of that plan – one that made it palatable at the time – was omitted. I ask the Legislature to, this year, honor the second critical part of the Snelling plan and enact a sunset for its tax hikes, while continuing to lock down the income tax rates. This action will send a clear signal

to Vermonters and businesses that we are listening to their concerns and working to meet their needs.

Further, the estate tax was increased last year to collect a greater portion of assets from deceased Vermonters. This change is particularly unfair to farmers whose assets are not easily mobile. It is a punitive tax that discourages farmers and small business owners from passing along their life's work to sons and daughters. And, in the long run, it will have a tangible, detrimental effect on our revenues, as individuals change their residency to another state. I ask legislators to join me in rolling back this tax increase.

* * *

Until we lower our overall tax rates to competitive levels, we need programs like the Vermont Employment Growth Incentive as part of our economic development tool kit. Since 2007, this employment program has authorized incentives for nearly 2,000 new jobs, and saved more than 2,000 existing jobs that might have been lost if employers chose to relocate out of state. The program has helped employers of all shapes and sizes, from small firms such as Vermont Timber Frames of Bennington, to medium-sized employers like SB Electronics in Barre, to large companies like Green Mountain Coffee Roasters. As long as our tax burden remains high, I propose eliminating the VEGI cap to keep pace with the growing demand from potential employers.

* * *

These tax proposals are a critical step in our efforts to restore employer confidence and send a message that Vermont is ready to compete for jobs. Unfortunately, the cumulative effect of these changes will still not equal the inevitable increase in unemployment taxes. That is why we must act this year to make our unemployment insurance trust fund solvent. A modest reduction in benefits coupled with phased-in increases in the taxable wage base is the prudent course to getting this fund back on solid footing.

* * *

There are additional investments in economic development that we can make now. I renew my call to use nearly $9 million from the federal stimulus act for job creation. This money will help train workers, provide access to capital for small businesses and farms, promote tourism and enhance our telecommunications infrastructure. Employers have told us what they need – now is the time for us to listen and act.

* * *

When a company comes to our state with 50, 30 or even 15 new jobs, we trip over ourselves to welcome them. When a valued employer is looking to expand or move elsewhere, we work feverishly to keep them here. We have such a company: one that employs hundreds of Vermonters at good wages; makes hundreds of thousands of dollars in charitable donations; and pays millions in taxes every year. Yet, some are eager to shut it down.

The decision about Vermont Yankee is central to our economic future and to maintaining a green energy portfolio. And it's a decision that should be left to the federal and state regulators – away from the political fray.

For the hundreds of Vermonters employed at Vermont Yankee and many more who benefit from its economic impacts; for the thousands of Vermonters whose jobs depend on our competitive electric rates; and for a stable, clean energy future, this Legislature should vote to let the Public Service Board decide the case for re-licensing.

* * *

Communications and energy factor into nearly every major decision an employer makes. In the post-recession economy, the two will be inextricably linked and for Vermont to compete globally, we must have the best of both working seamlessly together. Whether it is information technology, manufacturing, farming, education, or health care, a strong communications and energy infrastructure is critical to the Vermont economy.

Fortunately, we start this new decade from a solid foundation built through years of hard work, planning and foresight. In 2007, the Legislature joined me in setting forth a very ambitious goal: universal broadband and wireless in every part of the state this year. The e-State initiative was – and remains – one of the most forward-looking, statewide telecommunications plans in the nation. Although the recession has slowed our efforts, we have made tremendous progress.

Thanks to our head start, Vermont has been well positioned to take advantage of the opportunities provided by the American Recovery and Reinvestment Act – ARRA. While other states asked for planning funds, Vermont sought and won major federal grants for technology implementation. With nearly $70 million in ARRA funds, plus an additional $120 million in investment by Vermont utilities, we are building a high-capacity, fiber-optic backbone that enables next generation innovations to take root and grow in our state.

Part of this backbone is our Smart Grid – a breakthrough in energy conservation. The Smart Grid will help families save on electric bills by knowing the best time to use appliances. Businesses will cut costs by choosing to operate equipment when it is least expensive. And Vermonters will be prepared to take advantage of new technologies – such as electric cars – to cut emissions and clean our air.

From this high-speed backbone, we are working with telecommunications providers to build out our "middle mile" connection points into schools and libraries across the state.

The final stop for Vermont's high-speed network is in every home and workplace. This is where it gets complicated for a state that is comprised of steep rugged hills and winding dirt roads. There are some places you can't get to from here – and, frankly, I don't want to change that.

But for families and businesses that want to get connected and are still not served by high-speed internet, I propose a "Backroads Broadband" program to spur local providers

to build last mile connections. For two years, the Vermont Telecommunications Authority will delay the cost of a high-speed internet connection into the home or office. For the providers, this means a guaranteed return for a limited window and a great incentive to run the final stretch of line to every customer. This is not an ongoing program for either customers or providers – it is a use it or lose it deal that will speed us toward meeting our e-State goal of universal coverage.

* * *

For employers and employees alike, the attraction of a state wired from stem to stern is powerful. Businesses of all sizes can be connected at every hour to clients around the world. Small footprint firms can be close to our lakes and mountains without sacrificing sales. Telecommuting options multiply for everyone.

Within state government, the investments in a wired future will be pivotal in our efforts to deliver high quality services more affordably.

With each new connection, the network's potential grows for applications both public and private – helping Vermonters succeed from the office to the classroom.

* * *

The ever-growing burden of property taxes threatens the financial security of Vermonters and the potential of our employers. Getting a handle on this cost is essential to our economic future.

In the last decade, total net education property taxes have nearly doubled from just over $450 million to $900 million today. And that $900 million accounts for only two-thirds of what Vermonters actually pay to support education. Almost half of income taxes, a third of sales taxes and a third of the purchase and use tax go to pay the total bill.

Containing costs is the only way to halt the climb of property tax bills and make our state affordable for families and businesses. That is why I continue to fight so hard to put the brakes on spending and to reform our broken funding system. In recent years, I called for caps on education spending, but we took only a small step in containing costs with the two-vote approach. Last year, I renewed my call to cap school spending as part of another push for comprehensive reform.

Another year has passed: ideas have been offered; groups have met; studies of studies have been studied again; but little has been done. Despite the recession and near zero inflation, school budgets are still projected to rise by two percent next year. Property taxes are slated to increase by $59 million. And for the first time since the enactment of Act 60, the statewide property tax rate will increase – by two cents – to cover ever-increasing costs, with an additional 20 cent jump over the following two years – pushing residential rates 26 percent higher than today. These facts paint a disturbing picture of a future burdened by increasing property taxes – suppressing job creation and homeownership.

Meaningful reform must address each of the three core drivers that push property taxes higher year after year. Foremost, we need to cut costs and bring spending in line with reasonable standards. We must modernize our antiquated education bureaucracy. And we must be prepared to disentangle the twisted funding system born with Act 60. We can and must change, reform and improve education funding and, indeed, education in Vermont.

* * *

Since 1997, school staffing levels have increased by 23 percent, while our student population has decreased by 11.5 percent. The number of teacher's aides has gone up 43 percent. The number of support staff has gone up 48 percent. For every four fewer students a new teacher, teacher's aide or staff person was hired. There are 11 students for every teacher – the lowest ratio in the country – and a staggering five students for every adult in our schools. With personnel costs accounting for 80 percent of total school spending, it's no wonder that our K-12 system is among the most expensive in the nation at $14,000 per student per year.

In most organizations, if your customer base is shrinking, you make adjustments to stay within budget and, at a minimum, you stop hiring. Although some will be quick to scold that "education is not a business," neither is Medicaid or public safety or environmental conservation. But in each of these areas, if we ignore the basics of prudent financial management, we imperil the services that we provide. Until labor costs in our schools are brought under control, taxpayers can expect their bills to grow every year and the onus of the property tax will continue to threaten a healthy economy.

* * *

I appreciate the difficulty of reducing personnel costs. Over the past two years, the State has taken necessary – and sometimes painful – steps to find labor savings through vacancies, retirements, and, when all else failed, layoffs. I am grateful to state employees who last week ratified, by a wide margin, a new contract that is in the public's interest. A three percent wage reduction frozen for two years is a meaningful and important contribution to the greater challenges that face Vermont.

To date, we have not seen similar agreements between teachers and school boards. In fact, teachers' salaries have continued to rise during this recession. If teachers' contracts mirrored the recent state employee contract, there would be no need to raise property tax rates in 2011.

* * *

Current staffing and compensation levels cannot be maintained as the student count continues to decline. If we simply move from our current 11 to 1 student/teacher ratio to 13 to 1, we would still have one of the lowest ratios in the country, while saving as much as $100 million. If we want to make education costs sustainable, we must return balance to classrooms.

I propose that over four years we bring our statewide student/teacher ratio to affordable levels. By leveraging the retirement bubble among teachers, we would be able to achieve significant savings through attrition alone – without any disruption in the classroom. This is not an early retirement incentive, but a mechanism to fill only one vacancy for every two retirements. Based on our experience in state government, this approach is sensible, achievable and much preferable to the alternative.

To further rein in the massive growth in labor costs, I propose requiring that new teachers' contracts establish a minimum 20 percent share for health insurance costs. State employees and many others in both the private and public sectors have accepted a 20 percent share as the standard contribution.

* * *

Our school governance structures are a vestige of the 19th century and, like our unsustainable personnel costs, must be reformed. We have 290 separate school districts – one for every 312 students – 63 different supervisory bodies and a State Board of Education. That's a total of 354 different education governing bodies for a state with only 251 towns. We spend, by some estimates, nearly triple the national average for school administration. There is no doubt that we have room to make our system of education more efficient and affordable.

A recently issued report from the Transformation Policy Commission outlined changes aimed at improving student outcomes. One recommendation – consolidating into as few as 12 education districts – highlights that a 21st century governance system can provide more than cost savings. A modern system opens the schoolhouse doors and allows students to explore new learning opportunities, in different settings, with the latest technologies.

Reforming the outdated school governance bureaucracy is long overdue. The plan put forth by legislators and my administration two days ago calls for a five percent reduction in governance spending in the next fiscal year and an additional 10 percent reduction in 2012. Streamlining services, centralizing back office functions and consolidating districts will be necessary to meet the challenge. Restraining governance spending will allow us to make investments in reforms, classroom technology and, most importantly, our students.

* * *

At the root of our education funding challenge is a system that's substantially eroding local control. Each year the connection between your school budget vote and your property tax bill becomes more and more distant. Expanded subsidies mask true costs. The budget you approve is not the budget you are billed for. And even as tax rates decrease, property tax bills increase.

This is the upside-down world spawned from Act 60. When there is confusion, there is no control. If we are not serious about reforming this system, your Town Meeting vote

will become an empty action and local control will be dead. We must not allow this to happen.

At thirteen years old, our education funding regime has grown into an unmanageable maze of exemptions, deductions, prebates, rebates, cost-shifts and hidden funding sources. Overlapping rings of complexity keep all but a few experts from understanding the many moving pieces. This is not good tax policy, not good government, and, if you ask most Vermonters, not good for much of anything. It's time to pull back the curtains and let the sun shine in on how education is funded. Transparency – Who is paying? What are we paying for? What are the results? – has been a missing element of education financing since the passage of Act 60.

Something most Vermonters may be surprised to learn is that taxpayers are funding 1,000 students who don't exist. These so-called "phantom" students are a creation of our system. When a school reports its per-pupil count each year, that number can only decrease by 3.5 percent from the previous year – regardless of how steep the actual decline. For schools shrinking year after year, this policy compounds the distance between reality and what Vermonters pay for. I propose increasing the cap to ten percent this year, then gradually phasing it out over three years.

* * *

When I first went to Town Meeting, each voter knew that a vote for increased spending was a vote to increase his or her property taxes. Vermonters were generous, but careful.

As education funding evolved, income sensitivity was created as a necessary safety valve to ensure that low income people weren't forced from their homes by high property taxes. Over time – and over my objections – the program was expanded to more and more people with higher and higher incomes. What started as assistance to the less fortunate has grown into an entitlement for over two-thirds of taxpayers, some with incomes as high as $110,000.

From a school budgeting perspective, income sensitivity subsidies distort decision-making by divorcing the majority of voters from the real cost of education. Next year 70 percent of Vermonters will be shielded from the full brunt of education spending decisions. When an increasing number of voters are exempted from paying the full share, higher school budgets become easier to pass. The natural check and balance of the old-time Town Meeting is gone.

While that might seem like good politics to some, it is terrible policy. Each expansion of the subsidy pushes increased costs to a shrinking number of residents and businesses and further erodes local control. It sends spending and property tax bills ever higher – making our economy less competitive.

The push for greater expansions has also led to extreme inequities in the system. There are over 6,000 Vermonters receiving a property tax subsidy who own homes valued at $400,000 or more. Of those, there are 136 people who live in $1 million homes being subsidized.

In the education fund, income sensitivity payments are a growing, dark cloud blocking out more important priorities. This program is expected to grow by $26 million next year – a jump of 18 percent. It will be a full 11 percent of the entire education fund – bigger than the special, technical and adult education programs combined.

If left unchanged, by 2012, the program will cost $183 million – 54 percent more than just four years earlier. As the cost of income sensitivity grows, it leaves less money for important education priorities. The choice between directing education resources to our children and growing this subsidy is an easy one.

By making progressive eligibility adjustments and curbing payments on homesteads valued greater than $400,000, we can put the program on a sustainable course – preserving it for those who need it most.

I recognize that changes to the income sensitivity program will impact some taxpayers, but bringing common sense to this subsidy is an essential step to reducing the overall cost of education and providing real property tax relief for all in the years to come. In fact, if income sensitivity payments were not increased this year, there would no increase in the residential property tax rate. Our goal must be to reduce the need for exemptions over time with responsible school spending decisions and a robust tax base that allows for lower rates.

My proposals for education reform go to the heart of runaway spending and, taken together, stop the projected two cent increase, plus drop the rates by another penny. Compared against a system left unreformed, my proposal will result in $33 million in lower property taxes – a welcome break for taxpayers.

* * *

As we work to reform education financing and bring balance back to our system, we cannot lose sight of our underlying purpose: to provide high quality learning opportunities at a cost that doesn't strangle our economy, forcing our children to leave in search of jobs, taking our education investment with them.

Throughout Vermont, efforts are underway to help students who learn in different ways, at different times. We must always be on the lookout for new ways to ensure our system of education is serving the needs of today's students.

Currently, Vermont schools are prohibited by law from accessing out-of-state distance learning programs. This is a barrier to a student who is, for example, interested in learning Chinese, while earning credits toward graduation. If a school sought to provide a new Chinese program for this student, or even a group of students, they would have to hire a new teacher with the expertise – a costly step.

Allowing students to access approved distance learning programs from around the country is a simple, affordable change we can make to improve quality and increase

opportunities. And it is a change that complements our efforts to wire schools and apply new technologies to the classroom.

No longer can we settle for the old paradigm that says the only way to improve education is to spend money to hire a teacher for a classroom. Instead, new thinking, creative ideas and an impulse toward change that excites, empowers and improves the education of our children must guide us in constantly reforming education in Vermont.

* * *

In all our efforts, Vermonters will judge us on the sum of our work, not the parts. They will judge us on our ability to get our economy moving again and on our ability to work together and craft a sustainable budget. If ever there were a time in our state's history for public servants to join together, and to dedicate ourselves completely to the economic strength and individual prosperity of our people, that time is now.

* * *

As a young man, 37 years ago, I took my seat in this Assembly for the first time. I listened as Governor Davis bid farewell to the office I am now so honored to hold. That morning, the departing Governor spoke of a foundation rooted in fiscal responsibility, efficient government and environmental protection. But that foundation was not an end in itself; rather it served to help Vermonters face a fundamental question he posed: "How shall we preserve the Vermont way of life?"

Like all under this Golden Dome, I've shared in the joys, sorrows, accomplishments and disappointments of daily life here and across our state. I've been a first-hand witness to, and participant in that "Vermont way of life."

I've seen it in a neighbor helping stack wood or pull a car from a deep rut in mud season. I've heard it in Town Meeting debates and deployment speeches. I've felt it on the coldest winter night and on a windy autumn day. And I've known it in the service of a firefighter, a church deacon or the anonymous volunteer just doing her part to better the community with no expectation of thanks.

The "Vermont way of life" is something not easily defined. It's rooted in a common decency and eternal hope for a better future. It's a shared love of this land and respect for one another. And I can attest that it is something worth preserving; something worth defending; something worth fighting for.

As we embark on the road ahead, let us take strength and comfort from the knowledge that others, who've come before, have succeeded in keeping for this generation the promise of Vermont. But let us be humbled in the understanding that it is our duty to keep that promise for those who follow.

God bless each of you and the great State of Vermont.

# # #

State of the State Briefing Document 1/7/10

JAMES H. DOUGLAS
GOVERNOR

State of Vermont
OFFICE OF THE GOVERNOR

Governor Jim Douglas
Final State of the State Address
Briefing Documents
January 7, 2010

"In these uncertain times, we must transform our public and economic framework by redesigning how we deliver state services and refocusing efforts to create jobs and ensure economic security for Vermonters. Out of necessity and because it is the right thing to do, we must act now to write the next chapter in the proud history of Vermont."

- Governor Jim Douglas, State of the State Address, Thursday, January 7, 2010

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Introduction

Since taking office in 2003, Governor Douglas has worked diligently on behalf of Vermont residents to change, reform and strengthen our great state. The last decade has seen many accomplishments in a number of areas, including environmental protection, public safety, and health care. These successes have helped build a strong foundation, but one that is being threatened by massive budget shortfalls, unfunded liabilities and a broken system of education funding. In his speech, Governor Douglas stated, "Working families have been battered by recession and employers weakened by state policies that are barriers to job creation.

"The trajectory of the Vermont economy for the next decade will be shaped by our decisions this year. If we are content to limp out of this recession, hobbled by flat job growth, we can choose to recycle old ideas and hope for a different outcome. But if we want to spring out of this recession – strong and nimble – we must have the heart to reform, the wisdom to act, and the courage to stand against those who will say it cannot be done.

"Mere 'recovery' is not enough for Vermonters who have persevered through this long season of decline. We must strive for a healthy and growing economy, prepared to compete with states next door and countries around the world. Prepared to compete – and win. These times demand new thinking – they demand bold action – and they demand it now."

In his final State of the State Address, Governor Douglas proposed creative solutions and a path forward toward success by working collaboratively with legislators to craft a balanced and responsible budget – the task at the heart of getting our state back on track. These briefing documents provide further detail regarding some of Governor Douglas' important proposals.

Jobs – Growth - Prosperity

"If we want to keep the jobs we have, if we want to get our small businesses to succeed in a global economy, if we want to attract rather than turn away people and potential companies, then we need to focus on the fundamentals."

- Governor Jim Douglas, State of the State Address, Thursday, January 7, 2010

All across Vermont, employers and employees are standing strong in an economic climate more difficult than any seen in generations. As a new decade begins, we must embrace the policies that Vermonters in every economic sector need to restart the engine of our prosperity: lower taxes; universal broadband and wireless technology; clean, reliable and affordable energy; a well-trained workforce; and an education system that is as efficient as it is effective.

As public servants, it is our responsibility to ensure that the next generation will inherit a strong, vibrant Vermont. If we are to live up to that responsibility, we cannot leave behind a tax structure that is unfair and unaffordable, a technological infrastructure that is outdated and inefficient, or an unemployment insurance fund that is overleveraged or bankrupt.

In his speech, Governor Douglas laid out a firm commitment to economic recovery and charted the path toward a prosperous future. He proposed tax relief for struggling businesses, allocating federal stimulus funds into economic development programs and a plan to put government spending on a sustainable path. He discussed the need for a reliable energy future and an education system that teaches our students without taxing them out of state when they graduate. If we make these commitments now, in the early days of this new decade, we can put Vermont on a path to prosperity for generations to come.

Governor Douglas' proposals include:

- **Investments in job creation** – eliminate the $10 million cap in the Vermont Employment Growth Incentive program.

- **Tax relief to farmers and small business owners** – protect farmers, small-business owners and older Vermonters from increases in the capital gains and estate taxes enacted during the last legislative sessions.

- **Responsibly addressing the unemployment insurance fund shortfall** – use a balanced approach that does not place an unfair burden on either employers or the unemployed.

- **Securing a clean and reliable energy future** – relicense Vermont Yankee so that it will remain a valued employer and a reliable supplier of clean and affordable electricity.

- **Building out our advanced telecommunications infrastructure** – bring broadband access to every corner of our state along with an advanced fiber-optic network.

Capital Gains Tax

In the 2009 session, the Legislature enacted changes in the tax treatment of capital gains income, but their plan did not provide protection for anyone under 70. These changes resulted in $9.3 million in new taxes to help fund ongoing spending increases.

Favorable treatment of capital gains income encourages entrepreneurship and investment, protects the retirement income of seniors, and eases the transfer of small, family-owned businesses from one generation to the next.

Governor Douglas proposes to roll back the capital gains tax changes made by the Legislature last year.

- Effective January 1, 2011, long-term capital gains will again be eligible for the 40% exemption, as they were in tax year 2008.

- The individual income tax rate decreases effective in 2009 and 2010 will remain in effect.

While removing the capital gains exemption could be justified if all the revenues were used to lower tax rates for working Vermonters, spending $13 million, a sizable portion of the proceeds – as the Legislature did – amounts to a tax hike on already over-taxed residents.

Estate Tax Reform

Changes the Legislature made in the capital gains and estate taxes have swelled the ranks of Vermonters who are looking at other states – like New Hampshire or Florida – for their new, permanent residences. In addition, the estate tax change was particularly unfair to farmers whose assets are not easily mobile. It is a punitive tax that discourages farmers and small business owners from passing along their life's work to sons and daughters.

Vermont currently piggybacks on the federal estate tax, with some modifications. Last session the Legislature amended the Vermont estate tax to block the federal rise in the exclusion amount to $3.5 million, leaving Vermont's tax with an exclusion of $2 million for individual estate taxpayers.

The Legislature also intended to block the one-year federal repeal of the estate tax, but changes to law did not accomplish this, leaving the Vermont statutes around the estate tax ambiguous. Given this confusion, we propose the Legislature clarify its intent to decouple from the underlying federal statute and implement a permanent $3.5 million estate tax exemption.

The official FY11 revenue forecast for the estate tax is $18.1 million based on the current $2 million exemption. The Governor's proposal would save Vermont taxpayers $3.5 million in estate taxes. It's important to understand that while current federal law sunset the estate tax for calendar year 2010, it also instituted a new capital gains tax on the sale of estate property upon which the state "piggy-backs." The proceeds from that new capital gains tax on inheritances is expected to be $3 million for a 12-month period. Therefore, to avoid double taxing inheritances,

once with an estate tax and yet again with the capital gains tax, the Legislature must revisit the estate tax and raise the exemption to the Governor's recommend.

With Vermont's high marginal income tax rates, there is little justification for taxing the estates of Vermonters who have built their businesses here, or farmers looking to pass on their legacy.

Removing Cap on Vermont Employment Growth Incentives (VEGI)

Since its inception in 2007, the VEGI Program has had extremely positive results:

- Number of Active Authorizations: 28
- Amount of Incentives Authorized: $16 million
- Estimated New Job Creation (direct & indirect): 3,987
- Estimated New Payroll: $84 million
- Estimated Average Compensation: $54,984
- Estimated New Capital Investments: $137 million
- Estimated Net Revenue Return to the State: $12.4 million

However, the program is currently capped at $10 million annually. The projects authorized during late 2009, which will commence new economic activity during calendar 2010, total $4,913,838, committing 49% of the 2010 annual cap.

The application process for the January 28, 2010 Vermont Economic Progress Council (VEPC) Board meeting is already poised to put the program over its annual cap. Applications to be considered at that board meeting could include three companies who plan to file applications for incentives estimated at more than $6.3 million. When combined with the $4.9 million already authorized, the incentives total $11.2 million, exceeding the cap.

In addition, VEPC and Agency of Commerce and Community Development staff have met with several other companies who are seriously considering starting, relocating, or growing a company in Vermont. These new applicants are projecting the creation of several hundred jobs and millions of dollars in capital investment, some in environmental technology sectors.

Failure to eliminate the cap could mean a lost opportunity to attract hundreds of new high-paying jobs, millions in capital investment in clean and environmental technology sectors, and the generation of over $6 million in new net tax revenues to the state.

Vermont's Unemployment Insurance Trust Fund

Vermont, like many states, is faced with a crisis in its unemployment insurance (UI) trust fund. The best solution to unemployment is a strong economy driven by a vibrant economic development policy that enables Vermonters to find quality jobs. These jobs must come from diverse economic sectors and different sizes of employers that are geographically dispersed throughout our state. Policies that meet these objectives will help sustain a stable job base. Failure to consistently support a strong economic development policy results in risks to our economy far beyond the crisis we face with our UI trust fund.

Addressing the UI trust fund crisis requires a balanced approach that does not unfairly place the burden of returning the fund to solvency on either employers or the unemployed. The Administration is proposing such a plan, with phased-in increases in the taxable wage base and modest adjustments to certain unemployment benefits. This combination will begin to return our trust fund to solvency before Vermont experiences another recession.

Vermont made deliberate choices to increase unemployment benefits without addressing increases in our UI taxes. Twice the Legislature increased UI benefits (expenses) above the cost of living, ranking Vermont above the national average in a number of benefit areas. However, the Legislature failed to address income to the trust fund, leaving us to spend down our UI trust fund at a time it should have been growing. This coupled with high unemployment, means we will be forced to borrow from the federal government to pay UI benefits in 2010 and beyond.

Failure to take comprehensive action last year has meant that our problem has grown by an additional $30 million. If we don't act this year, the fund will be in deficit for the foreseeable future, leaving us unprepared to handle the demands of the next downturn. Because borrowing eliminates a federal tax credit for business and because the money must be paid back with interest, failure to act also prolongs both the tax increase on employers and the direct hit to future General Funds. We must act now.

Phased-in tax increases: Vermont has above average UI tax rates compared to other states, yet the taxable wage base that employers use to calculate those taxes remains low. We are proposing phased-in increases in the taxable wage base over the next 4 years from the current $10,000 to $18,000, as well as indexing future wage base increases to increases in benefits, to assure trust fund solvency down the road. We've also included a trigger to lower the taxable wage base if the fund balance grows too high.

Changes in benefits: Vermont has a generous unemployment benefits system, but we must balance that system to assure sustainability of the fund and availability of a workforce. Our proposal includes adjustments that will continue to keep benefits at or above national averages, as well as addresses seasonal issues and issues of fairness for those who are unemployed due to their own misconduct.

Examples of benefits adjustments include:

- Reinstituting the one-week waiting period that Vermont had until 2000, making us now one of only 13 states that have no waiting period. The annual savings would vary but would be approximately $5 million in 2010.

- Calculating the weekly benefit amount based on a full year of wages versus the two quarters presently used.

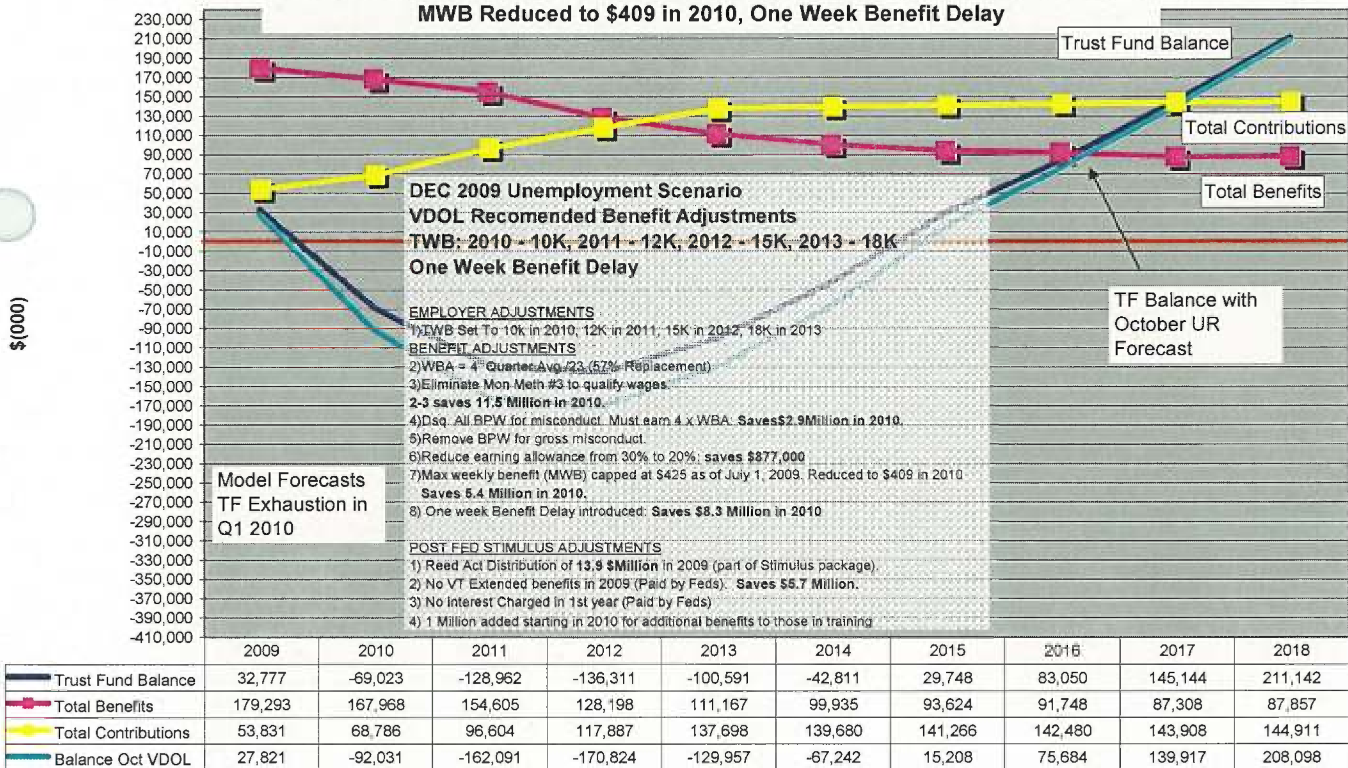
- Disqualifying a person fired for misconduct from receiving UI benefits. Presently there is only a delay in receiving benefits.

- Increasing the penalty for workers fired for gross misconduct which is typically violence or theft in the workplace.

The proposal recognizes that unemployment insurance is an employer-financed program designed to ensure some level of economic stability during recessionary periods. It seeks to balance the solution between the needs of employers and the needs of the unemployed. The plan requires some borrowing but minimizes those impacts as much as possible without jeopardizing the economic health of employers and the unemployed.

12/23/2009

Vermont UI Trust Fund Projection: Dec 2009 Unemployment Scenario - VDOL Rec Benefit Adj. TWB = 10K in 2010, 12K in 2011, 15K in 2012 and 18K in 2013, MWB Reduced to $409 in 2010, One Week Benefit Delay



	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Trust Fund Balance	32,777	-69,023	-128,962	-136,311	-100,591	-42,811	29,748	83,050	145,144	211,142
Total Benefits	179,293	167,968	154,605	128,198	111,167	99,935	93,624	91,748	87,308	87,857
Total Contributions	53,831	68,786	96,604	117,887	137,698	139,680	141,266	142,480	143,908	144,911
Balance Oct VDOL	27,821	-92,031	-162,091	-170,824	-129,957	-67,242	15,208	75,684	139,917	208,098

SOURCE: VDOL Benefit Finance Model, December, 2009

State Fiscal Stabilization Fund (ARRA)

Last year the Governor proposed using one-time money from the State Fiscal Stabilization Fund (SFSF) of the American Recovery and Reinvestment Act (ARRA) for job creation and economic stimulus. The Legislature disagreed and instead, used much of the money for on-going state expenses. The Governor again proposes that these responsible investments be undertaken using SFSF funds, including:

- $1 million to the Vermont Training Program to restore the Legislature's reduction in FY10 from $2.8 million to $1.8 million. This reduction in funding means this critical program will serve 1,800 fewer Vermonters and 40 fewer companies this year. An independent firm hired in 2008 to determine the program's return on investment found that for every dollar invested in the program, the state realizes $2.67 in revenues over and above the invested dollar; therefore the reduction in funding will result in a revenue loss of approximately $2.67 million for FY 10.

- $1 million to assist businesses impacted by the closure of the Lake Champlain Bridge or other economic factors, through a combination of direct grants and low-interest loans.

- $3.17 million to the Vermont Telecommunications Authority for the Backroads Broadband Project. This project will complete the universal broadband access goal of Act 79 by incenting providers to serve Vermont's most hard-to-reach areas and encouraging swift adoption by consumers in newly-served areas.

- $500,000 for the Vermont Department of Tourism and Marketing to assist in marketing Vermont as a vacation destination. According to an analysis conducted by Economic and Policy Resources, Inc. for the Department of Tourism and Marketing, estimated visitor spending in Vermont was $1.61 billion in 2007. That resulted in an estimated $3.1 billion impact on Vermont's $22.7 billion Gross State Product, about 13.7 percent of the state's total, and 37,490 direct and indirect jobs, about 12 percent of the state's total employment of 300,941 for that year.

- $1 million to VEDA to provide subsidized loans and credit support to farmers and expand on the programs VEDA used to assist farmers in 2004, 2006 and 2009. Through the 2009 program, VEDA provided $6.6 million in loans at subsidized rates and allowed farmers to use the loans to consolidate existing open accounts for needed inputs such as feed, fuel and fertilizer.

- $2 million to the Vermont Economic Development Authority (VEDA) to buy down the interest rate on loans it makes to Vermont companies; the money would leverage a total of $22.5 million in low-cost loans, which VEDA estimates would positively impact 2,335 jobs and create an additional 637 jobs.

VEDA LOAN SUBSIDIES FUNDED WITH FEDERAL STIMULUS FUNDS

WITH ADDITIONAL $2,000,000 (TOTAL = $3,000,000) AMERICAN RECOVERY & REINVESTMENT ACT (ARRA) APPROPRIATIONS

ARRA Program as of 12/31/09	#LNS	$ LOANS	$ PROJECTS	SUBSIDY $	JOBS IMPACTED AT CLOSING	JOBS CREATE/RET (0-2 YEARS)
LOANS CLOSED 2/17/09 - 12/31/09	23	$7,731,441	$26,859,351	$592,970	705	216
LOANS APPROVED, NOT CLOSED	9	6,780,026	29,004,142	542,070	269	206
ENERGY EFFICENCY LOANS	16	$677,126	$1,216,201	$78,600		
ARRA SUBSIDY LOANS	48	$15,188,593	$57,079,694	$1,213,640	974	422
REMAINING AVAILABLE (ESTIMATE)	50	$22,500,000	$76,893,000	$1,799,000	2,335	637
ESTIMATED ARRA SUBSIDY TOTAL	98	$37,688,593	$133,972,694	$3,012,640	3,309	1,059

ESTIMATED COST PER JOB IMPACTED $910; CREATED/RETAINED $2,845;

Technology Investments

Businesses – including the self-employed – increasingly depend on high-capacity affordable broadband and predictable, reasonable energy costs. Vermont will be able to provide both of these necessary economic incentives due to a number of factors:

- The head start Vermont has achieved since 2007 through the E-State initiative;
- Success in winning a $69 million dollar ARRA grant for Smart Grid deployment;
- Electric utility plans for a further investment of over $120 million dollars in Smart Grid and communications;
- A significant public safety communications infrastructure effort;
- Vermont Telecommunications Authority (VTA) support for, and coordination of, fiber to schools, government offices and other critical institutions, as well as towers for mobile communication;
- Existing VTA bonding authority and the availability of low-interest Recovery Zone Facility Bonds for telecommunications projects;
- Legally enforceable commitments by Comcast and FairPoint for 100% coverage of new communities;
- A number of outstanding and anticipated requests for stimulus funding for broadband and broadband adoption, at least some of which are likely to be approved;
- The Backroads Broadband Project that will help complete the task of bringing affordable high speed broadband to the most remote parts of the state, spur rapid adoption in formerly unserved areas, and fill in where stimulus funds are not available; and
- A rapid transition to e-government which will provide better service to Vermonters at sustainably lower cost.

The Smart Grid projects will allow both businesses and consumers to tailor their electrical use to take advantage of low off-peak rates. By the end of 2012, most of Vermont will be covered by Smart Meters and we will be poised to use relatively low cost electricity to replace petroleum-based fuels, both for transportation and home heating. Assuming the relicensing of Vermont

Yankee, we should be able to widen our advantage in electrical rates over other New England states. The Smart Grid also makes good use of small and medium-sized alternative energy sources so we will be better able to grow distributed electricity generation.

Vermont electric utilities are in the process of building at least 1,200 miles of high capacity fiber to nearly every area of the state. This construction will be largely completed in the next two years and does not depend on state or federal funding. Using this backbone for general communication as well as energy-related purposes, we will be able to reduce wholesale and institutional broadband costs to those typically found in metropolitan areas. Businesses which value Vermont's unparalleled quality of life, environmental ethic and skilled workforce will find themselves well-connected when they locate here. This connectivity is valuable to Vermonters and the Vermont economy by itself, but it is also the information backbone for the Smart Grid, cellular towers, public safety, e-Health, e-Government, and e-Education.

Re-license Vermont Yankee

Decisive action on our long-term energy future is critical to our economic future. The decision about the future of the Vermont Yankee nuclear power plant is important for employers – both large and small – who rely on affordable and competitive electric rates. It's important as we seek to maintain a clean energy portfolio and move to more renewable sources. And it is everything to hundreds of employees, who pay taxes and contribute to the Vermont economy.

The Vermont Yankee nuclear power plant is not only a substantial source of revenue for the state, but is a significant employer, expected to average over $100 million per year annually in full-time salaries to employees over the next 20 years, if re-licensed.

Since 2004, there has been a tax on net megawatt hours of generation produced by the facility. It is assumed for the revenue/burden analysis that the taxes generated by this arrangement will approximate the taxes levied on energy production in the future should the license be extended. Over three calendar years, the plant is projected to produce 4.86 GWh per year on average. The resultant electrical energy tax from that level of generation is $2.9 million per year, $57.3 million total over 20 years, or a net present value of $36.0 million in 2012 dollars.

Vermont Yankee also pays its education taxes based on generation, and with a 3-year average generation of 4.86 GWh per year, the tax revenues are projected to be $2.1 million per year, a 20-year total of $41.8 million, or a net present value of $26.3 million.

Vermont Yankee currently ranks among the 60 largest private and public employers in Vermont, and is in the top 5 in the Windham County area. Its economic impact over a 20-year period is estimated to range from a low of $1.5 billion to a high of $5.1 billion, representing between 0.2% and 0.6% of estimated Gross State Product over the 20 years.

The Governor urges the Legislature to vote to let the Public Service Board decide the case for re-licensing; to let Federal and state regulators make this important decision, away from the political fray.

Education Reform

"The ever-growing burden of property taxes threatens the financial security of Vermonters and the potential of our employers. Getting a handle on this cost is essential to our economic future."

- Governor Jim Douglas, State of the State Address, Thursday, January 7, 2010

Vermont's K-12 education system is among the best resourced in the United States. According to Department of Education (DOE) statistics, Vermont ranks first in the ratio of students to teachers at 11 to 1. This is 54% higher than the national average of 15.4 to 1. Vermont ranks 4th in public school revenues per enrolled student at $16,210, or 43% higher than the national average of $11,369.

However, when it comes to wealth, Vermonters are not in the top tier. DOE statistics show that Vermont ranks 24th in personal income per capita at $34,623. This amount is below the national average of $36,629.

When Act 60 passed the Legislature in 1997, it equalized access to education spending by all school districts. At the time, it was clearly understood that low spending school districts would be encouraged to spend more given the improved access to funding through the statewide property taxes. However, even since 2005, school spending and property taxes have continued to grow at very rapid rates. In 2005, the net residential property tax was $254.2 million. For 2011, it is projected to be $375.6 million, equaling an annual growth rate of 6.7%. Similarly, the non-residential property tax has grown from $385.8 million to $562.8 million, for a 6.5% annual growth rate.

This growth was not driven by more students in the classroom, as the student population actually decreased over this 6-year period from 99,994 to 92,631 or 7.4%. Despite this decline, education spending rose from $1.06 billion to $1.37 billion. On a per pupil basis, spending grew at the annual rate of 5.63%. The core driver of these increases has been increased staffing at our schools.

Since 1997, staffing levels have grown by 23%, from 15,555 to 19,145 while at the same time the student population has decreased by 11.5%, from 106,341 to 94,116.

Income sensitivity payments have grown from $92.3 million in 2005 to a projected $167.8 million in 2011 for an increase of 82%. Basically, income sensitivity transfers the burden of the property tax from eligible beneficiaries to property tax payers who are not eligible, namely non-residential property owners and property owners with household incomes above $90,000. Even with recent changes that placed an $8,000 cap on benefits, 363 owners of homes valued at $800,000 or more receive a benefit, and of this group, 136 people living in homes valued at $1 million or more get a subsidy.

Given the above statistics, the challenge before us is to sharply bend the education spending curve to one that is affordable to Vermonters, as well as reconstruct the Act 60/Act 68 education funding machinery so that it supports sustainable spending for the future.

The Choices Before Us (And the Status Quo is Not Among Them):

If left unchecked, residential property tax rates will rise by 26% over the next 3 years. That increase, combined with a $150 million budget deficit, mean that doing nothing is not an option. Relative to the Education Fund, three major goals for this legislative session must be:

1. To lower property tax rates: Current projections call for a 2 cent increase in both the residential and non-residential property tax rates this year. The combination of these tax increases and dramatically slower growth in the grand list this year, result in $59 million in new taxes. If left unchecked, the 3-year rate increase is projected to be 22 cents for both residential and non-residential. During this recession, we must seek to lower property tax rates on households and businesses struggling to make ends meet.

2. To lower property tax rates through constraints on education spending: As noted above, the core driver behind the growth in education spending is increased staffing levels in our schools. Pressure needs to be exerted that not only inhibits such increases, but actually results in staffing decreases to more affordable levels.

3. To lower property tax rates through rebalancing the income sensitivity program: The cost of income sensitivity to the education fund is growing at exorbitant rates. For fiscal 2011, the estimate is an increase of $26.2 million – 18% higher than this year. Through rebalancing the income sensitivity program, not only will the direct costs of this program be diminished, but indirectly, voter behaviors will be affected such that higher levels of education spending will not be as readily approved.

To achieve the above, the Governor offers the following proposals:

- Property Tax Rates: Rather than increase rates by 2 cents, as currently projected, the Governor proposes to lower both the residential and non-residential rates by 1 cent, from $.86 to $.85 and $1.35 to $1.34 respectively.

- Income Sensitivity: The Governor proposes to right-size the Legislature's eligibility increases over recent years by making income sensitivity subsidies more progressive based on income levels. For incomes between $60,000 and $75,000, the minimum percentage of income should be 2.25%. For incomes from $75,000 to $90,000, the minimum percentage of income should be 3.5%. Further, the benefit should be limited to the first $400,000 of a homestead residence.

  In addition, to provide assistance to those of low and moderate income, the Governor proposes to enhance benefits. These include raising the renters rebate income eligibility

cap from $47,000 to $54,000 and lowering income requirements for the program so that low income households receive a greater benefit. These thresholds have not changed since 1995.

- Efficient Governance: In Vermont, we have 290 separate school districts – one for every 312 students – 63 different supervisory bodies and a State Board of Education. That's a total of 354 different education governing bodies for a state with only 251 towns. There can be no doubt we have room to make our system of education more efficient and affordable. Yet, the Education Fund and property tax payers support two expensive programs that discourage consolidation. Over the next three years, the Governor proposes to phase-out the small schools grants and the "phantom student" subsidy. The latter pays school districts for non-existent students by limiting an annual enrollment decrease to 3.5% even though the actual decrease may be much more. These changes, in addition to those recommended by the Public Strategies Group, can save over $25 million during the next few years.

- Reduce Education Costs:

  Health Care Premiums: State employees pay 20% of their healthcare premiums while taxpayers cover the rest. Many taxpayers cover more than 20% of premium costs while some cover the full cost. It is reasonable for teachers to be on par with state employees and cover 20% of health care premiums. As contracts come up for renewal, such a requirement should be incorporated in each contract with local teachers' unions.

  Reduced Staffing Levels: As noted above, Vermont has the lowest overall ratio of students to teachers at 11 to 1, according to the DOE. Vermont needs to set an affordable standard for this key ratio. The Governor recommends a 13 to 1 statewide ratio as this is far below the national average of 15.4 to 1 and still among the best in the nation. At a 13 to 1 ratio, Vermont would be ranked as 8th best in the nation, just between New Hampshire to our east, New York to our west and well above Massachusetts to our south.

  The Governor's proposal is to leverage a retirement bubble over the next few years to achieve the savings. For example, if only one position were filled for every two retirements, Vermont could achieve a 13 to 1 teacher pupil ratio over the next approximately 4 years, saving the education system over $100 million.

  There are many methods to achieve this standard: from statutory position caps at the district or supervisory union level; to restricting access to the State Teachers' Retirement system as the "check valve" to ensure a portion of positions vacated due to retirements are not filled. We will work with the Legislature to develop the most appropriate mechanism to accomplish the goal and achieve the savings.

- School Construction Assistance:

  Like teachers' retirement costs, school construction costs properly belong in the education fund. These costs have been historically borne by the general fund, despite

significant increases in the transfer of general funds to the education fund and the redirection of tax revenues, such as the sales tax and purchase and use tax, from the general fund to the education fund.

The Results of These Reforms

The Governor's proposals for education reform go to the heart of runaway spending and, taken together, stop the projected two cent increase, plus drop the rates by another penny. Compared against a system left unreformed, the Governor's proposal will result in $33 million in lower property taxes – a welcome break for taxpayers.

Budget Address
1/19/10

JAMES H. DOUGLAS
GOVERNOR

State of Vermont
OFFICE OF THE GOVERNOR

Governor James H. Douglas
2010 Budget Address
January 19, 2010

Mr. President, Mr. Speaker, members of the General Assembly, distinguished guests, my fellow Vermonters:

In the late fall of 1927, the skies opened and a great flood devastated our state. Vermont's transportation, industrial and agricultural infrastructure was washed away over two long days.

On a visit back home less than a year after the flood, President Coolidge noted "the splendid recovery." He remarked that "Transportation has been restored. The railroads are in a better condition than before. The highways are open to traffic for those who wish to travel by automobile."

The Great Flood of 1927 was a defining moment in our state's history not just for the magnitude of destruction, but for the effort to rebuild that followed.

Today, the crisis we confront is economic: a Great Recession. For two long years, Vermonters have been hard hit by this downturn and the foundation of our economy is in need of rebuilding. That work is slowly beginning on factory floors and in offices, at home businesses and on construction sites. But progress is fragile and there is much hard work ahead.

Just as Vermonters did more than 80 years ago, we must rebuild better than before. This year we will be judged not just by our ability to pass a balanced budget, but by whether that budget prepares our state and its people for a stronger tomorrow.

* * *

The principal reason for our budget shortfall is the economic challenge facing Vermonters. In just over a year, more than 10,000 jobs have been lost and last year median family income fell nearly $2,000 from the year before. Although Vermont's unemployment rate is among the lowest in the nation, our workforce is shrinking and too many are underemployed. As a result, state revenues are $20 million below those of 2006 and a staggering $100 million below where they were at the height of the economic bubble in 2008.

While Vermonters have found it harder to pay the bills, General Fund programs have seen unsustainable increases and new pressures. Demand for human services will grow by $50 million, pension contributions are projected to increase by $29 million, and $75 million in federal recovery funds relied on for this year are no longer available. Without corrective action the shortfall in the fiscal 2011 General Fund will be $150 million.

With revenues not expected to return to pre-recession levels until 2013, our fiscal crisis extends far beyond today. Without sustainable reductions, the fiscal 2012 shortfall will balloon to over a quarter billion dollars – more than we spend on economic development, environmental protection, public safety and higher education combined.

To protect the most vulnerable now and in the future, we must make sustainable reductions to break free from the dangerous cycle of managing deficits year on end. To make our economy more competitive and state government more affordable, we must invest in job creation to grow our tax base and find efficiencies to reduce cost. And to preserve the greatness of Vermont, we must protect that which sets us apart – our safe communities and our cherished natural environment. The budget I deliver today meets each of these objectives.

* * *

This year, we must employ new thinking and embrace creative approaches. It is critical to move ahead on the agreement between legislative leaders and my Administration to identify millions in sustainable savings through "Challenges for Change." While I understand that some may be skeptical, we have little choice but to ensure this effort succeeds. If the targets are not met, the money must be found with deeper reductions to state services. But I am confident that we will accomplish our goal to focus limited resources on the most critical needs of Vermonters. I am accounting for all $37.8 million outlined in these challenges in my fiscal 2011 budget and expect that the annual savings will be even greater in years to come.

The agreement to set the challenges into law this month will achieve savings sooner rather than later and allow us to move ahead to address the remaining $112 million General Fund shortfall. Doing so will require looking to those areas of government that are growing the fastest and consuming the greatest resources – human services, pensions and education.

* * *

We have long measured our compassion by how we help neighbors in need; when the hour is dark, the hearts of Vermonters have always burned bright. We are rightly proud of our strong human services network – a gold standard among states.

Through Choices for Care, Catamount Health, the Blueprint and other innovative health and human services reforms, we've built a solid foundation that is helping vulnerable Vermonters find a path to health, employment and independence.

But we cannot deny that the sharp growth in demand for human services in recent years threatens the overall stability of our budget. Nearly one-third of our population receives services from the State. Next year, the Medicaid system alone will serve 172,000

Vermonters. Since the beginning of the decade, overall spending for human services has more than doubled – a growth rate of three-and-a-half times inflation.

Even last year, as we struggled to fill a significant budget shortfall, total human services spending grew by $100 million. Much of that increase was funded through the use of one-time federal money.

While there has been discussion about a second recovery package or brief extensions of Medicaid dollars, we cannot place the sustainability of our programs at the whims of Washington.

I am not counting on additional federal assistance in my budget. But even if new aid does eventually come our way, we must recognize that federal recovery funds will not flow forever, nor should they. We must take responsibility for our own programs and begin to step down our funding levels gradually and responsibly. By starting now the difficult process of realigning human services spending within currently available resources, we will spare programs from devastating cuts when the federal spigot is inevitably turned off.

Any additional funds from Washington must be used to transition to a more effective, efficient and affordable state government, while investing in one-time efforts to create jobs and grow our tax base.

* * *

The most difficult budget choices will be in the Agency of Human Services. This is both because of its sheer size – the largest percentage of the state budget – and because these cuts will unquestionably have an impact. I propose General Fund changes of $53 million in human services – of which approximately one-quarter will be direct service reductions for beneficiaries. These choices are necessary in order to sustain critical programs and benefits today and in the future.

My human services budget is guided by three key principles. First, we strive to protect the most vulnerable Vermonters by asking some beneficiaries and providers to carry a greater share of costs. Next, we seek to adjust services incrementally for the broad population rather than cut out some groups entirely. Finally, in all decisions, we focus on helping people achieve better outcomes, not safeguarding the status quo.

The impacts of the recession – continued unemployment, reduced earnings and the housing crisis – have increased the number of Vermonters seeking assistance. That's why my budget funds caseload increases, ensuring that Vermonters can access essential services. It also supports inflationary increases for the 39 Vermont nursing homes that accept Medicaid payments, and funds the growing needs of those with developmental disabilities who depend on state support to ensure their health, welfare, safety and full community inclusion.

Our focus on meeting these critical needs necessitates major adjustments and tough choices elsewhere in the Agency. I propose eliminating over 20 grants to direct service providers within our system and reducing many more, including those that I have supported and advanced over the years: Housing and Supportive Services grants that fund

wellness programs in senior housing settings; the Neighbor-to-Neighbor Americorps program; the senior companion program; and mentoring, to name a few.

I propose tightening eligibility requirements for the attendant services program to include an income and asset test. This is an important program that supports independent living for disabled adults who need assistance with daily activities and we must ensure its sustainability into the future.

In order to maintain benefits for low income families served by the Reach Up program, responsible reforms are needed, such as removing recipients from the program when they chronically refuse to complete their family development plan or meet work requirements. Further, I propose once again establishing a time limit for Reach Up recipients who do not meet hardship criteria; a five-year limit is very generous at any time, but particularly now in the face of our fiscal challenges.

My budget also includes a series of adjustments focused on providers, including: targeted reimbursement rate reductions for home health agencies; across-the-board grant and rate reductions for smaller providers working with the Department for Children and Families; and increased receipts of $7 million from hospitals by keeping their tax rate at the same level as last year.

Further, to uphold our strong commitment to alcohol and drug abuse programs, which I've long championed, we must better align services with needs. Because we have seen underutilization of some inpatient adolescent services, I propose funding them on an as-needed basis with a corresponding reimbursement rate reduction.

We know that these proposals will be a struggle for some organizations that are already adjusting to reductions made last year. As such, we are committed to working with non-profits to reduce administrative burdens that detract from their ability to deliver efficient quality care.

While we make these difficult decisions, we must continue our investment in our innovative Vermont Blueprint for Health. That's why my budget supports the continued expansion of this successful program, with the goal of having it available in all communities within two years. I also call on our private insurance partners to make this goal achievable. The Blueprint is our best hope for slowing the growth in health care spending while improving the quality of health care received – something that all Vermonters want and need.

* * *

Vermont's Medicaid program is among the most generous in the nation. We can all be proud of efforts to expand coverage, because better health outcomes are achieved when people get care before they become sick. But maintaining coverage for the greatest number of people will mean scaling back benefits for some.

Throughout the summer and fall state workers were asked to take a fresh look at areas of government where we could do better. One such Tiger Team considered improvements to our Medicaid system. After reviewing ten states that, like Vermont, provide generous services, the team saw that Vermont sets few limits on utilization. For example, we pay for an unlimited number of emergency room visits. Capping ER visits that do not result

in hospitalization at 12 per year will bring Vermont more in line with peer states – saving money to preserve this benefit for everyone in the system.

Another example is the adult dental benefit, now set at a maximum $495 per year. By reducing the cap to $200 per year, we will save over a half million dollars in the General Fund, without eliminating this important benefit altogether.

Insuring more Vermonters is the goal of Catamount Health. During this economic downturn, when many other states have seen an increase in uninsured residents, Vermont's numbers have remained steady. In fact, during the past two years, we've succeeded in lowering our uninsured rate, which is now among the lowest in the nation. To make certain that Vermonters have access to affordable, quality care, we need to protect Catamount by making it sustainable. This will require a significant increase in deductibles, which will also more closely align our program with industry standards.

In our Medicaid programs, most premiums have not been increased since 2006. Modest increases next year for a number of these programs are necessary to protect them during tough times.

Finally, this budget will increase our focus on fraud detection and program integrity – ensuring that those applying for benefits meet the income and asset requirements. By more closely monitoring provider billing, we will ensure that services are paid accurately. And by making small, but important, investments now, we can curtail inappropriate usage to realize savings and preserve programs for those with real needs.

I understand that these changes will generate considerable debate, but I've seen the alternatives and they are much worse. These decisions are responsible without being draconian and they put our safety net on a sustainable path for years to come.

* * *

Our pension systems are likewise in crisis. If we do not change course, future Legislatures will be unable to keep our retirement promises to state workers and teachers. Without reform, the total required contribution from all funds for the two systems will grow by $32 million – an incredible one-year increase of 43 percent. In the General Fund, pension contributions are projected to consume 8 percent of available resources next year, squeezing out other priorities. Moreover, the unfunded long-term liabilities in the systems exceed $2 billion and, if not addressed, will threaten benefits and state budgets for years to come.

Last year, this Legislature established a Commission to review these systems and make recommendations to safeguard their solvency while holding the State's pension contribution to a reasonable three-and-a-half percent growth rate.

I want to commend the Commission – Treasurer Spaulding in particular – for its hard work and leadership. Their recommendations to adjust retiree age, final benefits and the annual contribution are responsible approaches, and as such I include them in my budget.

Although these changes will be difficult, inaction would be irresponsible. It is important to remember that while the retirement age will increase and employees will be asked to contribute more, this is necessary to protect a guaranteed benefit. Retired state

employees and teachers are assured pensions and subsidized health care for life – something most Vermonters do not receive.

* * *

The pension system is a problem of not just how much we pay, but also of who pays. Currently, the teachers' retirement system is funded entirely by the General Fund, despite the fact that the salaries used to calculate pensions are set at the local level.

Teacher retirement, like salaries or student transportation, is an education expense, pure and simple, and should be borne by the Education Fund. But if the expense of the retirement system is transferred without offsetting cuts to education spending, it will raise property taxes. Let me be absolutely clear: that is not what I am proposing.

Instead, as part of my education reforms, I propose to phase teachers' retirement costs into the Education Fund over four years. With the reforms I have proposed to normalize the student to teacher ratio, and by asking teachers to pay 20 percent of their health care premiums, the additional expense of teachers' retirement is covered. In fact, my package of education proposals will cut property tax rates by one cent next year – rather than require a two-cent increase if no action is taken.

Those who attempt to parse my proposals to justify a claim of a tax increase should be reminded that by advocating for the status quo they are, in fact, supporting a $59 million property tax increase. That is a burden Vermonters simply cannot afford.

* * *

In the General Fund, $38 million in government efficiency challenges, $53 million in human services adjustments, $25 million in pension changes, $10 million in education reforms and $5.5 million in labor savings from the contract ratified by state workers bring us a long way to covering our $150 million shortfall. But there are other reforms we must undertake to balance the fiscal 2011 budget and deliver sustainable savings for taxpayers.

One such effort is an evaluation of the 300 boards and commissions that regulate or advise on everything from world trade to well drilling. While most provide a valuable service, some have not met for years while others share similar missions and constituencies. I asked one of the Tiger Teams to consider efficiencies and savings throughout this system. As a result of their recommendations, I will present a plan to the General Assembly to abolish, consolidate or otherwise modify as many as 50 Boards and Commissions.

* * *

Just as we focus our efforts within state government, we must also seek efficiencies from those entities that receive a large share of their budgets from taxpayers. Our affordable housing programs provide critical services to Vermonters of various income levels and stages of life. Assuring that the people of our state can meet basic housing needs has long been a priority of mine. That's why I asked a Tiger Team to look at ways to enhance our affordable housing efforts, while making our statewide network sustainable.

For a small state, we have a surprising number of entities devoted to affordable housing. At the state level, the Vermont Housing Finance Agency, the Vermont Housing and Conservation Board, the Vermont State Housing Authority, Housing Foundation Incorporated and the Department of Economic, Housing and Community Development all share an affordable housing mission. Frequently these state level entities negotiate with one another to channel separate investments into the same projects. And with 130 employees, managed by four separate boards, consisting of 37 board members, three executive directors and a commissioner, I believe, as the Tiger Team found, that there are real opportunities to do more for affordable housing with greater efficiency.

For instance, the staffing costs for these entities amount to $9 million. By redesigning the system to achieve just a 10 percent savings in personnel costs, $900,000 annually could leverage over $20 million in new affordable housing investments. I have asked Commissioner Brooks to convene the stakeholders to look into opportunities, such as this, to improve our system.

* * *

As we strive to bring our budget back to sustainable levels, investments must continue in Vermont's infrastructure that support existing industries and spur economic growth.

During the past seven years we've increased our commitment to transportation – catching up after decades of underfunding. I propose reducing the raid on the Transportation Fund by an additional $3.5 million next year, directing that money to municipalities to support our town highway program. I'm proud that during my tenure we will have restored nearly $68 million to the Transportation Fund for investment in our roads, bridges and culverts.

We have worked together, on a bipartisan basis, to strengthen our commitment to transportation. Between this year and next, Vermont will spend more than $400 million paving our roads and fixing our bridges – an unprecedented effort.

Last year, we increased our overall transportation budget by $140 million. While much of that growth was a result of the federal stimulus act, we made the most of the opportunity. In spite of, or perhaps because of, our long winters and short construction season, Vermont was a national leader in the quick deployment of stimulus dollars.

We will build on our aggressive efforts by increasing our transportation investment by $14 million more next year. My budget includes $113 million for bridge and culvert construction and maintenance – a 20 percent increase over fiscal 2010. And in the last four years, we have increased spending on preventative maintenance from $8 million to over $35 million in this budget.

As in other areas of state government, our commitment should not be measured by funding alone. Because of the "Road to Affordability" we are deploying these transportation resources more efficiently and with a better return on investment. By doing a better job of keeping up with work today, we are saving money in the future.

Our transportation infrastructure is, quite literally, the foundation of our economic prosperity. A safe and efficient system of roads and bridges is central to the flow of goods and commerce and to a stronger economy. I was proud to sign the bill you just

passed removing heavy trucks from our town and village centers by allowing them access to our interstate system. At a time when our traditional industries need a boost, truckers, loggers and manufacturers will benefit from this pilot effort, saving time and money, as well as improving our environment.

* * *

Good environmental practice is smart fiscal policy. The Green Mountain State continues to be a leader in energy efficiency and the use of alternative sources of power – saving Vermonters money and contributing to a cleaner environment. Our efforts have been bolstered by more than $30 million from the federal stimulus act – money appropriated for purposes of the Clean Energy Development Fund. But to date $17 million has not been allocated to projects.

Because it is critical to get this money out the door quickly to support our growing renewable energy market and create jobs and because it is important that state government be an example, I propose redirecting $9 million immediately to our state buildings and parks. To save taxpayer dollars and make needed efficiency improvements at the Waterbury State Office Complex, $6 million will be used to demonstrate the full potential of these investments. Another $2 million will equip the new Bennington state office building and courthouse with a geothermal heating and cooling system. Every year in Bennington we will use 30,000 fewer gallons of oil, conserve 510,000 kilowatt hours of electricity and avoid emitting 640 tons of carbon dioxide into the atmosphere – not to mention save $175,000 for taxpayers. The remaining funds will be used to make improvements at our state parks, where exciting efficiency and renewable energy projects are already underway.

These efforts are part of an $80 million Capital Bill, which also includes $25 million to upgrade and rehabilitate our facilities to modernize state government. Our capital investments will employ thousands of tradespeople across Vermont and are critical to maintaining high quality services as we confront enormous fiscal challenges.

* * *

When opportunities arise to improve state programs and services through the use of technology, we cannot blink. Efforts to streamline processes and functions across state government not only save money; those who need assistance benefit as well. Every visit to a different office and every minute spent filling out paperwork is time away from caring for a child or searching for a job. By creating one central point of entry, we can make it easier for Vermonters to navigate the bureaucracy and receive assistance to get to self-sufficiency.

That's why, as part of my capital bill, I propose $8 million in information technology investments to help streamline state government. For state employees, new tools will allow them to spend more time delivering services and less time filling out paperwork. For taxpayers, costs will be reduced through efficiency and better coordination. And for those accessing programs, a new MyVermont portal will serve as a virtual kiosk – one-stop shopping – where information can be entered to immediately access the appropriate services anywhere in state government.

By redesigning our technological infrastructure we can make better use of our limited resources. And because of this effort we will be on course to achieve a paperless state government.

* * *

Today, Vermont is facing the convergence of two demographic challenges – slowing growth rates and an aging population. These trends threaten to erode our workforce and our tax base, making it harder to support the generous level of services we expect.

The promise of stable employment, good wages and vibrant communities is what will ultimately keep young Vermonters here and attract working families to our state. That's why, especially now, we must strengthen our investments in next generation technologies, economic development and affordable higher education.

* * *

Since we embarked on the ambitious e-State initiative three years ago, much progress has been made. Today, more Vermonters are able to access technologies that will improve their health, expand their knowledge and help them compete for new employment. But our work will not be finished until those opportunities are available to every Vermonter in every corner of the state.

To make more progress toward our goal, we will leverage already approved bonding authority and private capital to build "middle mile" fiber capability to schools, hospitals and other public institutions by allocating $5 million in Capital funds to the Vermont Telecommunications Authority.

This investment will be complemented by over $3 million in federal stimulus funds for the "Backroads Broadband" program – defraying the initial cost for those in the hardest-to-reach places and creating an incentive for providers to bring service the last mile.

I thank Senator Illuzzi and the members of the Senate Economic Development Committee, as well as the House Commerce Committee, for their commitment to quickly move a jobs bill with funding for this broadband program.

* * *

Other aspects of that bill are just as critical to Vermont's economic future. Restoring funds for workforce training, helping small companies access needed capital and supporting businesses in our tourism sector are important investments. And so is removing the Vermont Employment Growth Incentive cap to help Vermont compete and attract new jobs.

But the most significant action we can take to spur job creation and broaden our tax base is to make our tax climate more competitive. Policies that influence individuals to change their residency to other states, that keep employers from hiring and that discourage a business from locating in Vermont altogether will ultimately make it more difficult to find a good job here and will lessen our ability to support state programs.

Sunsetting last year's capital gains changes and rolling back the estate tax increase – a

$10 million impact on the General Fund – are prudent investments in a growing economy and more robust tax base. These changes are necessary to send a clear signal to employers and employees alike that Vermont is serious about competing for jobs in the post-recession economy.

* * *

An investment in higher education is an investment in the promise of a more prosperous tomorrow. It must continue to be a priority even during these difficult times. The uncomfortable fact is that our institutions of higher learning are some of the most expensive in the country, with among the lowest levels of state support. Assuring that every Vermonter who seeks a post-secondary opportunity can afford it is a goal we must constantly strive to attain. And providing those opportunities is critical to the retention of our next generation and assuring that it has the tools, training and education for 21st century jobs.

As part of our effort I recommend a base increase for higher education with $5.5 million shared among UVM, the State Colleges, and VSAC. I also propose restoring $1.5 million of base funding to our Next Generation scholarships. And I am asking for $2 million each in capital funds for UVM and the State Colleges for facility upgrades and other infrastructure needs.

* * *

For over 200 years, Vermonters have been bound together by close communities and by our distinct love of this land. A shared commitment to a better tomorrow is rooted in our proud heritage. As we work to balance our budget and prepare our state and its people for a future of opportunity and prosperity, we must not forget that which sets us apart, that which defines who we are as Vermonters.

Preserving what is so special about this state begins with ensuring that our communities are safe and that each Vermonter has access to a fair and functioning system of justice. I want to again recognize the leadership of the Judiciary and the Commission on Judicial Operations for their efforts to make our system of justice sustainable, even in difficult financial times. I am including their recommendations in my budget.

A sound Judiciary is necessary to complement the important work of our state law enforcement professionals. These men and women work day in and day out, in dangerous situations, to keep us safe and secure. With 13 new troopers and an additional nine preparing to train, our State Police force will be at its highest levels in the past decade.

This year we will have a State Trooper assigned to every regional Special Investigation Unit, where they will work with local and county officers to bring to justice those who prey on our most vulnerable. And to further aid their efforts, we are moving forward with a state-of-the-art forensic lab, scheduled for occupancy this coming October.

I am proud that even during these tight fiscal times we have been able to increase our support for our law enforcement professionals, as well as other public servants working hard to keep us safe, such a our firefighters. That's why I continue to support fire

training efforts. All our public safety professionals deserve our deepest respect and thanks.

* * *

Many tears have been shed as families bid their farewells to our brave men and women now being deployed overseas. We are proud of them, their patriotism, their valor, and their dedication to those ideals we hold dear. We must assure that their families receive the support they need during the long separation. We must also be fully prepared to provide for the needs of our troops when they return home. My budget provides the resources to keep our commitment to do both.

* * *

Vermont is blessed with many natural gifts from our green mountains to our rolling, open farm lands to our lakes, rivers and streams. Preserving our natural environment is an obligation we have to the next generation. Clean waterways, healthy wildlife and vibrant forests are an economic, as well as environmental, imperative for our state.

Working with our federal, municipal and non-government partners, we have made an unprecedented commitment to Lake Champlain through the Clean and Clear program – investing more than $50 million in efforts to improve water quality, leveraging an additional $52 million in federal funding. We have worked to enhance the stability of streams and rivers, improved management of our vast network of dirt roads, protected and restored wetlands and limited pollution from construction site runoff.

The Agency of Agriculture has provided technical assistance to farmers to develop and implement soil-based conservation practices and nutrient management plans – preventing discharges from barnyards and fields. To continue this good work, I propose $8 million in General and Capital funds to support our Clean and Clear priorities within the agencies of Agriculture, Transportation and Natural Resources.

* * *

Our farmers are keepers of our unique landscape and protectors of our strong environmental ethic. While all Vermonters have struggled through this recession, farmers have been further stressed by a prolonged period of low milk prices. As part of the jobs bill, $1 million should be dedicated to helping our agricultural community weather the storm this year.

The Farm to Plate initiative is working to foster growth in both the farm and food sectors. By directing $100,000 of the Sustainable Jobs Fund appropriation to this initiative, we will increase access to healthy, affordable, local foods, while supporting our farm economy.

Ultimately, our agricultural industry requires the federal government to reform the antiquated milk pricing system, allowing Vermont farmers to compete fairly in the national market. I will continue to support the efforts of our congressional delegation and others who are working to deliver the reforms our farmers need.

* * *

Of the eight budgets I have proposed, this is the most challenging by far. The magnitude of our shortfall demands new approaches and creative thinking. It calls for difficult reductions in worthy programs and a dedicated focus on the most pressing needs of our people.

But our purpose is not simply to patch together a budget for next year; rather our aim is to set our state on solid ground for the next generation. That's why we must continue to strive for a growing and vibrant economy – one that opens the doors of opportunity across our state. Now is not the time to look back and protect the status quo.

The budget I deliver today looks to the future by putting state government on a sustainable course, by investing in the potential of our people and by protecting that which makes this place so special. It is but one part of the effort to rebuild our economy and restore our prosperity.

From the depths of this Great Recession, we must find the courage to make difficult decisions, act boldly and lead fearlessly. We will not fail if together we renew our commitment to a stronger tomorrow.

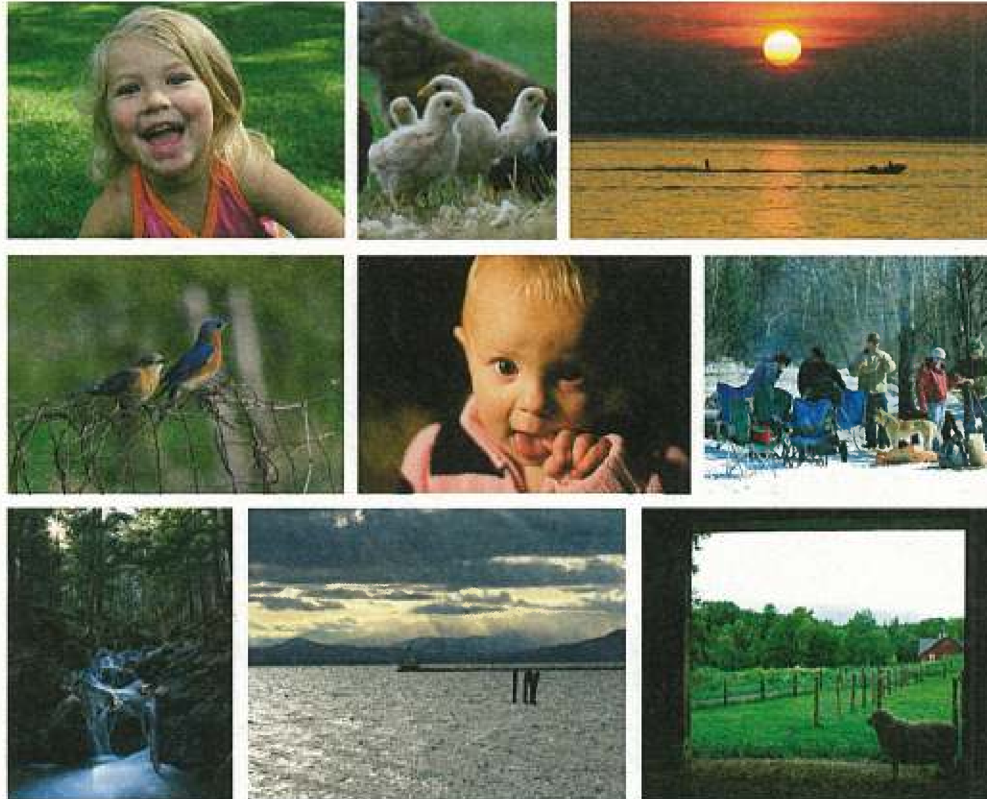
God bless each of you and the great State of Vermont.

# # #

FY 2011 Executive Budget Recommendations

VERMONT

Our Commitment to a Stronger Tomorrow



Fiscal Year 2011 Executive Budget Recommendations

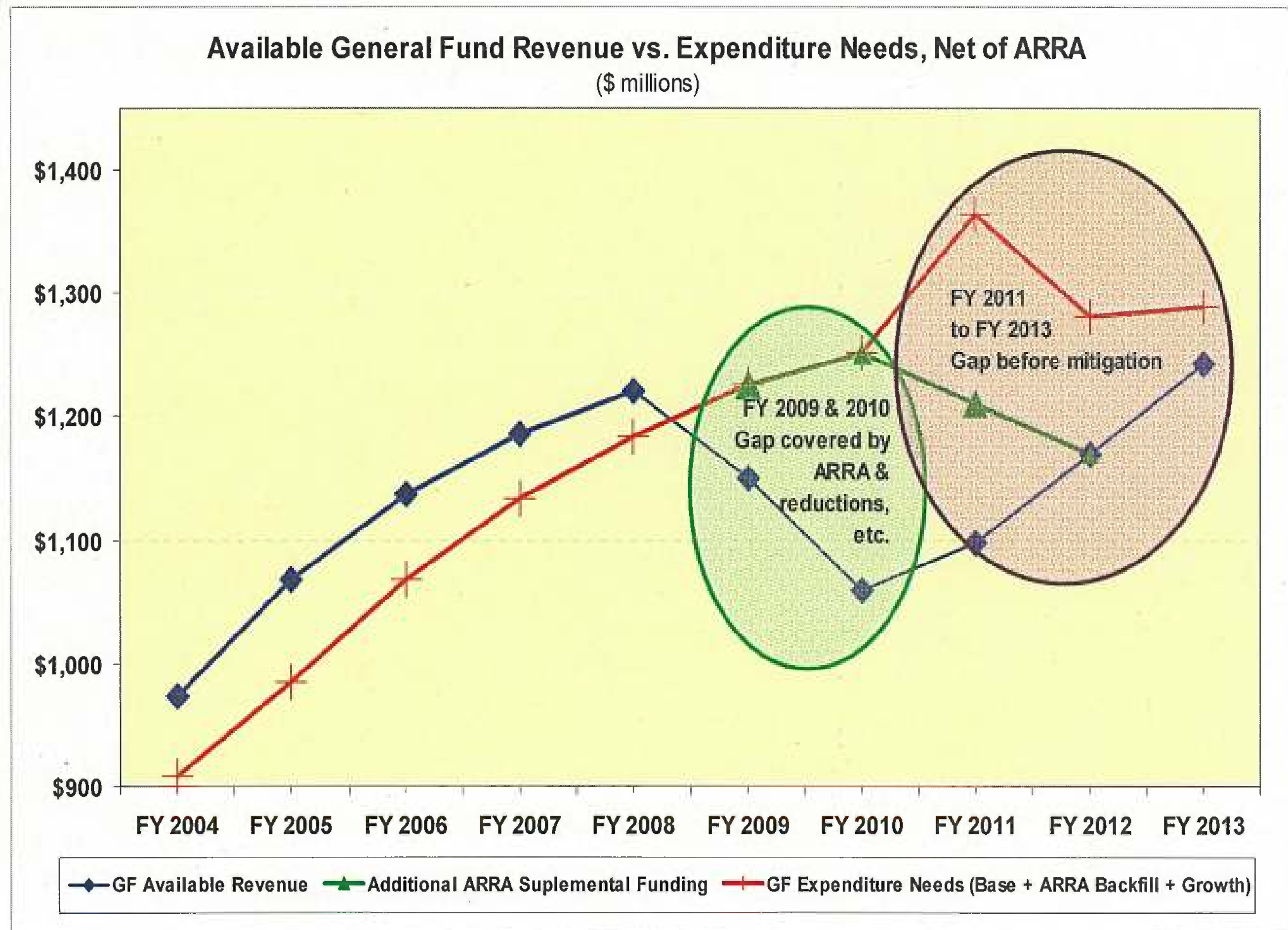
James H. Douglas
Governor of Vermont
January 19, 2010

RESOLVING VERMONT'S FISCAL CHALLENGES FOR FUTURE GENERATIONS

BASE GENERAL FUND SPENDING MUST BE REALIGNED

Short Term Federal Stimulus Money Is Not The Long Term Solution

Vermont is faced with fiscal challenges unseen in a generation. Although the economic situation appears to be stabilizing, the recession has impacted Vermont with an unemployment rate at 6.4% and General Fund (GF) revenues reduced below the fiscal year (FY) 2006 level. How we handle these challenges will determine whether we limp out of the recession or create the conditions for a vibrant recovery. One year ago many hoped that the federal stimulus package would fill the budget gaps while being a bridge to better times. In February 2009, Congress passed the American Recovery and Reinvestment Act ("ARRA"). The purpose of the $787 billion program was to jumpstart the economy, create and retain jobs, and help states with their burgeoning budget gaps, from its inception through December 31, 2010. The program includes: increased federal participation rates or extended benefits in certain existing programs; defined purpose discretionary grants; and State Fiscal Stabilization Funds (SFSF). The increased and extended programs and SFSF funds effectively provided supplemental funding for General Fund (GF) budget gaps for FY 2009 through the 2nd quarter of FY 2011. The stimulus money was only a partial and temporary response. We must now deal with the loss of more than 40% of the ARRA funds in FY 2011 and the loss of the remainder in FY 2012. The base budget gaps temporarily filled by ARRA require General Funds to backfill, in addition to meeting inflationary increases and beginning to resolve unfunded liabilities. Unmitigated, we face a cumulative GF budget gap for FY 2011 - FY 2012 of more than $250 million, as shown on the chart to the right.



January 19, 2010

Dear Members of the General Assembly and Fellow Vermonters:

Vermont families and businesses continue to feel the impact of the Great Recession. Many of our friends and neighbors are out of work. Others have had their hours cut and are struggling to make ends meet. This deep economic contraction is the principal reason for the budget gap we must address.

For fiscal year 2011, Vermont faces a $150 million General Fund shortfall that will require tough, but necessary, decisions throughout state government. The wide chasm between spending pressures and available revenue does not abate in fiscal year 2012 and will demand aggressive action and our full attention for years to come. We must acknowledge the reality before us and rise to meet the challenge together and with resolve.

I was pleased to begin this year's legislative session with an agreement on "Challenges for Change" – a joint plan between my Administration and the Legislature to save $38 million by redesigning state services to deliver better outcomes. This break from business-as-usual thinking will be an essential part of our success in coming years. Still, we must engage in the next set of decisions necessary to close the remaining $112 million gap.

Today I present a budget that responsibly closes that remaining shortfall while putting state government on the path to address future fiscal concerns. There will be many difficult choices, especially in human services, but we must resist the temptation to use reserves and additional one-time federal money as temporary patches – decisions that will only worsen our problems in fiscal year 2012 and beyond.

The state budget must be made sustainable today, while we commit to a stronger tomorrow. We must work diligently to ensure Vermonters have access to essential state services, while resisting new taxes that will aggravate future budget challenges. And we must make smart investments in job creation, technology and higher education, so we can help get Vermonters back to work – strengthening our economy and growing our tax base.

I ask you to take the time to understand the entirety of my budget proposal, because the challenges we face are not solely in the General Fund. We must also bring bold reforms to our education system and stand firm in our support for transportation. A comprehensive fiscal strategy is necessary to address the economic challenges facing Vermont.

I know you appreciate the magnitude of the task before us and I look forward to working with you as we move forward toward a stronger tomorrow.

Sincerely,

James H. Douglas
Governor

FY 2011 General Fund Budget Gap Analysis

Category ($ millions)	Revenue	Appropriations & Net Transfers	(Shortfall)/ Surplus
Projected Revenue			
Current Law Revenue (January 2010 - Emergency Board)	$ 1,086.60		
Direct Applications & Reversions (recurring)	10.00		
Total Available Revenue FY2011	**1,096.60**		
Upward Pressures			
Base Appropriations + Transfers (FY10 post-rescission)		**1,065.35**	
Base Pressures			
VSTRS & VSERS		28.77	
Human Service Caseload & Utilization		42.94	
All Other Human Service		8.73	
Administration, incl. insurance & internal service fund needs		5.29	
Public Safety & other protection		2.79	
Homeowners & Renters Rebate, and Current Use Tax		3.97	
Debt Service		1.45	
Subtotal: Base Pressures		**93.94**	
All One-Time Pressures		14.11	
Subtotal: One-Time Pressures		**14.11**	
Loss of Offsetting ARRA Funds (vs. FY 2010)			
Public Safety (SFSF)		4.40	
Long Term Care		11.23	
Global Commitment		55.13	
Department for Children & Families		6.16	
Subtotal: GF ARRA Offset Loss		**76.92**	
Total Upward Pressures		**184.97**	
Total (Shortfall)/Surplus	**$ 1,096.60**	**$ 1,250.32**	**$ (153.72)**
Adjustments			
Base (Reductions)/Increases			
Human Services		(53.67)	
Education Fund Reforms		(10.41)	
Pension Reforms		(25.00)	
Tax "Roll back"	(9.90)		
"Challenges" Savings		(37.88)	
Labor Contract		(5.50)	
Natural Resources		(1.36)	
Pay Act		(3.73)	
Judicial Reforms		(1.00)	
Housing Consolidation	5.90		
Higher Education		5.56	
Next Generation Scholarships		1.50	
Vermont Telecom Authority		0.75	
JTOC		3.50	
Homeowners & Renters Rebate		1.47	
Special Education Medicaid	6.89		
Small Claim fees to GF	0.30		
Subtotal: Base Adjustments	**3.19**	**(125.77)**	
One-Time Adjustments			
Special Funds (BISHCA - direct app increase)	14.70		
Gross Receipts Weatherization	2.30		
Prior fiscal year carryforward	4.96		
Budget Stabilization Reserve (remains at 5%)		(2.80)	
Subtotal: One-Time Adjustments	**21.96**	**(2.80)**	
Total Adjustments	25.15	(128.57)	0.00
Grand Total Net of Adjustments	**$ 1,121.75**	**$ 1,121.75**	**$ (0.00)**

Fiscal Year 2011 Deficit Mitigation

For FY 2011, the difference between anticipated revenues and needed appropriations is significant. The current FY 2011 GF Consensus Revenue Forecast plus direct applications, reversions, other revenue adjustments, and a $4.96 million carryforward result in projected total available revenues of $1,121.75 million. Without further mitigation, the deficit for FY 2011 is projected to be $153.72 million.

This deficit is due primarily to growth in Human Services caseload and utilization, Vermont State Employees and Vermont State Teachers' Retirement Systems, other human service increases, increases in homeowners/ renters rebates and current use taxes, other inflationary increases across state government, and the loss of $77 million in ARRA funds previously available to support base GF needs.

For FY 2011, the Governor asked all areas of government to share in sacrifices necessary to bring appropriations to a sustainable level, along with the Challenges for Change initiative, and reforms to Education funding. The Governor's FY 2011 Budget Recommendations present a balanced GF budget for FY 2011.

Federal Stimulus Impact

Cumulatively, between FY 2009 and FY 2011, of the $806 million in total estimated ARRA funding, approximately $382 million is for enhanced federal participation rates for Medicaid and other federal entitlement programs. This effectively allowed the State to trade base General Fund dollars for ARRA funds, enabling a reduction in the amount of state funds necessary to match federal monies. The remaining ARRA receipts target one-time discretionary grants or projects.

The GF base budget gaps for FY 2009 and FY 2010 were ameliorated though a combination of ARRA funds, rescission, labor reductions, and one-time funding from other sources. The amount of ARRA funds available to offset base GF needs begins to decline in FY 2011 with the loss of $77 million of "base" ARRA funds, and concludes during FY 2012 with the loss of the remaining $113 million of "base" ARRA funds. These lost ARRA funds create upward pressure on the GF in addition to the annual inflationary upward budget pressures. The following chart summarizes total ARRA receipts used for both GF base expenditures and one-time grants and projects.

SUMMARY OF FEDERAL STIMULUS FUNDING BY FUNCTION [(1)]

FUNCTION	FY 2009		FY 2010		FY 2011		CUMULATIVE ARRA	
	AMOUNT	%	AMOUNT	%	AMOUNT	%	AMOUNT	%
Regular ARRA Funds:								
General Government	-	-	-	0.0%	-	0.0%	-	0.0%
Protection [(a)]	-	-	35,451,349	9.4%	18,539,819	7.4%	53,991,168	6.7%
Human Services	75,916,880	42.6%	166,555,162	44.3%	86,014,634	34.1%	328,486,676	40.7%
Labor			7,793,753	2.1%	4,571,772	1.8%	12,365,525	1.5%
General Education [(b)]	-	0.0%	-	0.0%	46,719,169	18.5%	46,719,169	5.8%
Higher Education			-	0.0%	-	0.0%	-	0.0%
Natural Resources			-	0.0%	1,467,187	0.6%	1,467,187	0.2%
Commerce & Community Development			1,982,000	0.5%	1,529,195	0.6%	3,511,195	0.4%
Transportation	59,680,000	33.5%	117,197,648	31.2%	54,524,670	21.6%	231,402,318	28.7%
Other:								
Human Service programs	3,414,832	1.9%					3,414,832	0.4%
Labor	400,000	0.2%					400,000	0.0%
Clean water; and drinking water capital grants	38,933,000	21.8%					38,933,000	4.8%
Secretary of Administration - entrepreneurial seed capital			(2,150,000)	-0.6%			(2,150,000)	-0.3%
Secretary of Administration - to VEDA for job creation			3,400,000	0.9%			3,400,000	0.4%
Secretary of Administration - to VT training program			200,000					
Secretary of Administration - to Tourism			500,000	0.1%			500,000	0.1%
State Fiscal Stabilization ARRA Funds [(2)]								
SFSF for State Police [(a)]	-	0.0%	6,550,000	1.7%			6,550,000	0.8%
SFSF for General Education [(b)]	-	0.0%	38,575,036	10.3%	38,575,036		77,150,072	9.6%
Total ARRA	**178,344,712**	100.0%	**376,054,948**	100.0%	**251,941,482**	100.0%	**806,341,142**	100.0%

(1) Appropriations funded through the federal American Recovery & Reinvestment Act of 2009 ("ARRA").

(2) State Financial Stabilization Fund (SFSF) monies, including:

(a) State Police ARRA funding included regular ARRA funds plus $6.55 million of SFSF funded through an ARRA Interdepartmental transfer.

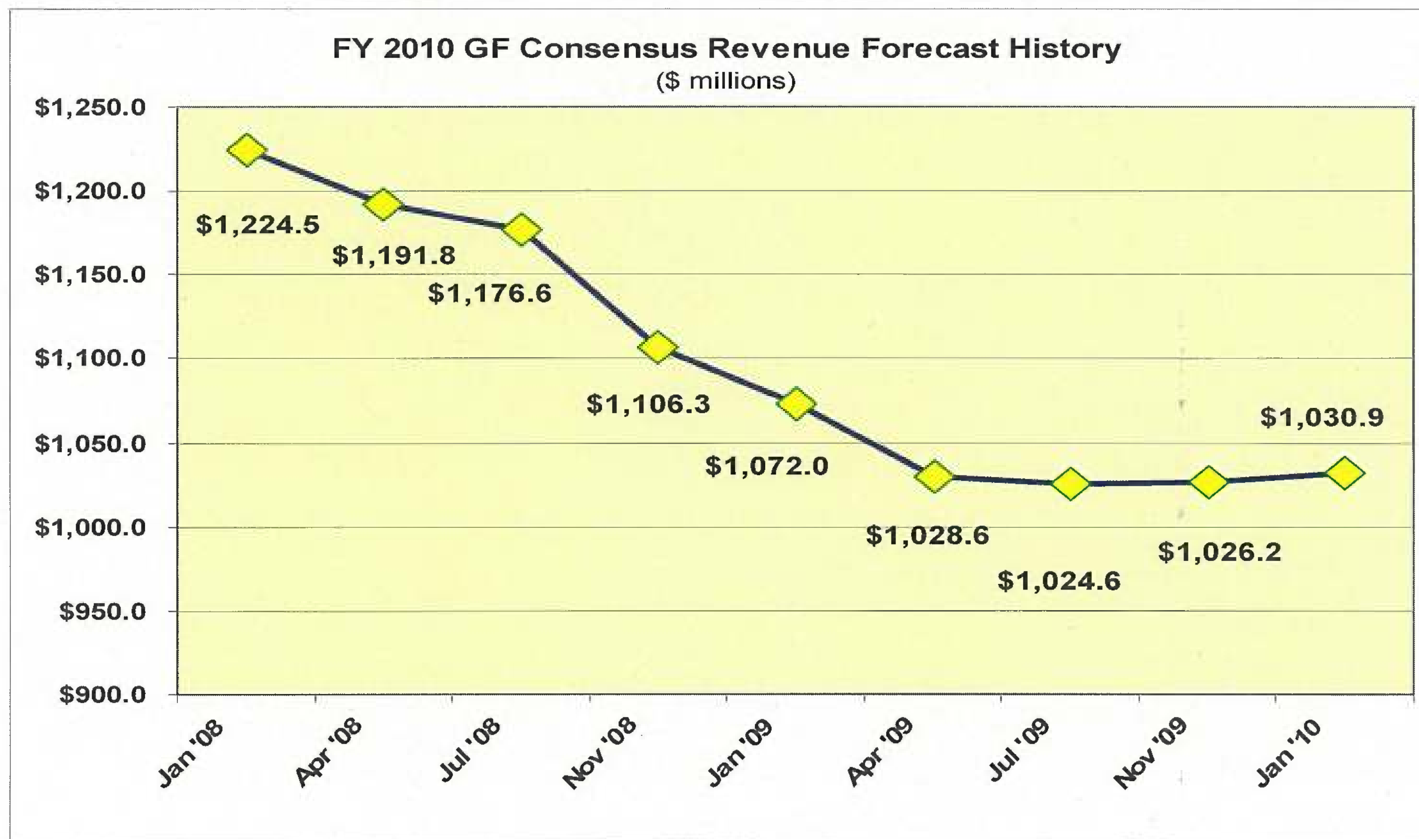
(b) General Education funding included regular ARRA funds plus $38.57 million each year (FY 10 and FY 11) of SFSF funded through an ARRA Interdepartmental transfer.

FISCAL YEAR 2010 BUDGET ADJUSTMENTS

FY 2010 Consensus Revenue Forecast

Due to the downward spiral of the national economy and the long slow recovery ahead, the Emergency Board opted to meet and revise the Consensus Revenue Forecast quarterly during FY 2009 and the first half of FY 2010. Normally, and in accordance with statute, the Emergency Board meets twice a year, in January and July. The FY 2010 revenue forecasts over the last 24 months show the dramatic decline in the General Fund, even though it has stabilized.

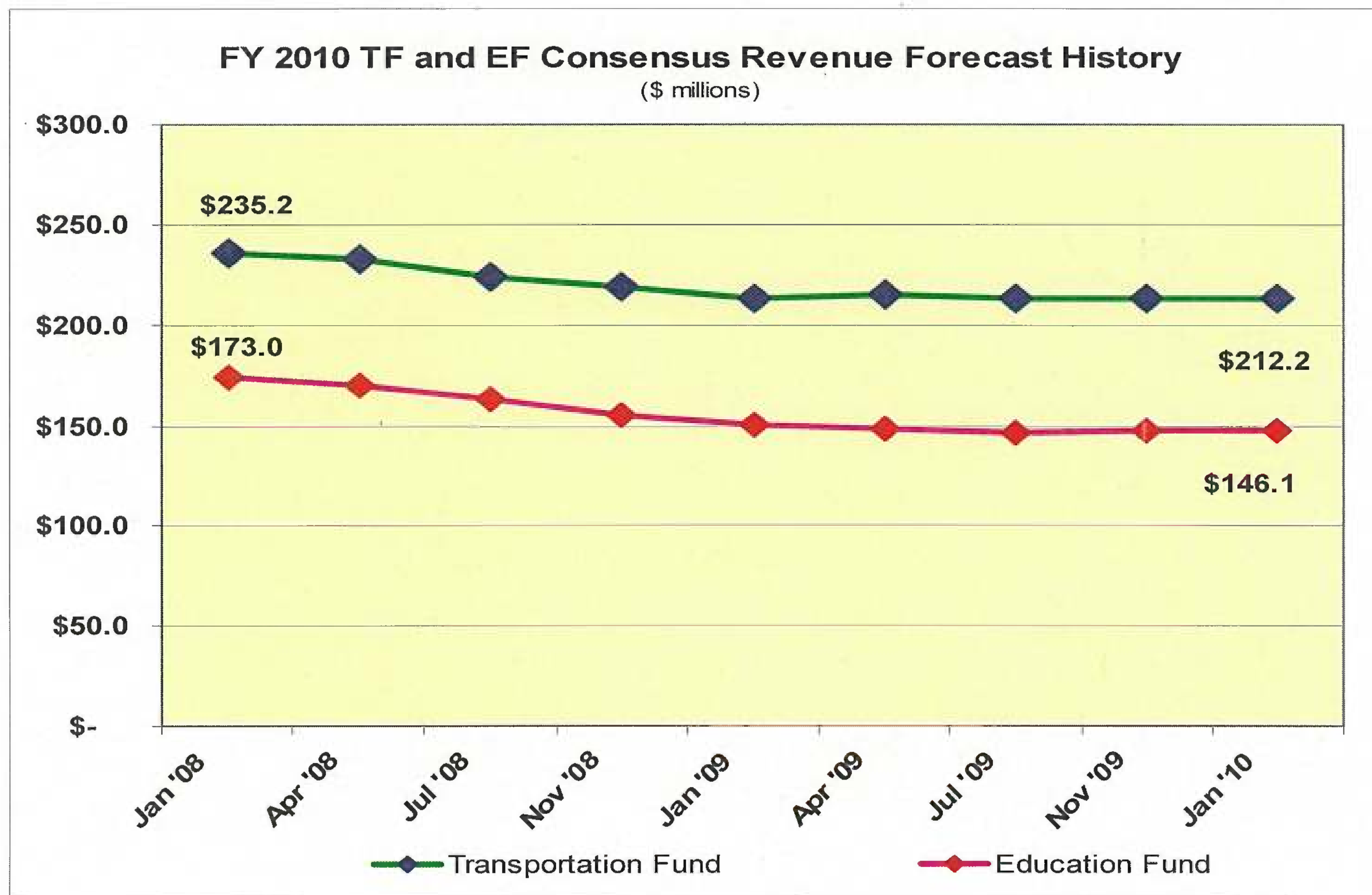
From the initial Consensus Forecast in January 2008 to the most recent forecast in January 2010, the General Fund has declined by $193.6 million, or -15.8%. $135.6 million is due to the drop in Personal Income Tax receipts and $37.5 million is due to the drop in Sales & Use Tax receipts. Together, these two revenue categories account for 89.4% of the total forecast decline over the last 24 months. The history of changes to the FY 2010 Consensus Revenue forecasts over the last two years is shown on the following chart.



The Transportation Fund and Education Fund Consensus Revenue forecasts were also revised quarterly by the Emergency Board over the last 24 months.

From the initial Consensus Forecast in January 2008 to the most recent forecast in January 2010, the Transportation Fund forecast declined $23.0 million or -9.78%. Half ($11.5 million) of this decline was due to Motor Vehicle Purchase & Use Tax. The forecasts for Gasoline Tax and Diesel Tax also declined by $2.8 million and $3.7 million respectively. Cumulatively, the reduced forecasts in Motor Vehicle Purchase & Use, Gasoline Tax, and Diesel Tax account for 78% of the forecast decline.

The Education Fund Consensus Revenue Forecast declined $26.9 million (-15.5%) over the same period. The Education Fund saw a downgrade in proportion to the Transportation Fund downgrade in Motor Vehicle Purchase & Use tax receipts.



Fiscal Year 2010 Recommended Appropriation Adjustment

The Governor's FY 2010 Budget Adjustment Recommendation reflects changes in the General Fund appropriations totaling $15.03 million, and -$1.47 million in the Transportation Fund. A summary of the General Fund and Transportation Fund adjustments are shown in the table below. A more detailed table by appropriation and across all funding sources is shown in the Tables and Chart section.

Governor's FY 2010 Summary Budget Adjustment Recommendation
General and Transportation Fund Appropriations

Appropriations - FY 2010 Budget Adjustment - Major Items: ($ millions)	General Fund	Transportation Fund
Agency of Human Services (AHS):		
Office of the Secretary - Global Commitment (GC)	10.00	
Department for Children & Families - AABD	0.78	-
Department for Children & Families - General Assistance	0.74	-
Department of Corrections - Out of State Beds	2.64	-
All Other - AHS	(0.46)	-
Sub-total Agency of Human Services	13.71	-
Other Units of Government:		
Administration - Information & Innovation	0.12	-
Treasurer's Office - Retirement Health Insurance	0.97	-
Treasurer's Office - Supplemental Assistance to Survivors Fund	0.03	-
Military - Air Sovereignty Mission	0.03	-
Public Safety - Fire Safety Division	0.60	-
Debt Service	(0.53)	(0.00)
All other Departments	0.10	-
Agency of Transportation	-	(1.47)
Sub-total Other	1.32	(1.47)
Total Appropriation Adjustments	**15.03**	**(1.47)**

* differences due to rounding

FISCAL YEAR 2011 RECOMMENDATIONS

FY 2011 Consensus Revenue Projections

On January 13, 2010, the Vermont Emergency Board approved the current consensus revenue estimate for FY 2011 of $1,086.6 million. This latest revision increased the General Fund revenue forecast by $4.8 million, up slightly from the previous forecast of $1,081.8 million in November 2009. The FY 2011 Transportation Fund revenue projection was revised to $218.0 million from the previous forecast of $217.8 million in November 2009, an increase of $0.2 million. The forecast for the non-property tax portion of the FY 2011 Education Fund was also adjusted to $151.3 million, versus the November 2009 forecast of $151.7 million, a decrease of $0.4 million.

The reduction of FY 2011 GF consensus revenues to below FY 2006 levels against expenditure pressure surpassing FY 2010 levels, results in a projected GF budget gap of approximately $153 million, before mitigation. The Governor's FY 2011 GF Budget Recommendation includes bold steps and broad government reforms that will close the FY 2011 budget gap without relying on additional federal support beyond the current ARRA program.

Looking ahead to FY 2012 and FY 2013, the state economists forecast revenue increases for the General, Transportation, and Education Funds.

Throughout the entire economic downturn, the Governor has steadfastly resisted calls to draw down the State's budget stabilization reserves. These reserves are intended for use when the state experiences unanticipated and unavoidable deficits near the end of the fiscal year, with no opportunity to put in place reductions necessary to close the gap prior to fiscal year end. The Governor's proposed FY 2011 budget maintains these reserves at their statutory levels.

Fiscal Year 2011 Revenue Forecasts History

($ millions) Fund Name	January 2009	April 2009	July 2009	November 2009	January 2010	Jan. 2010 vs. Jan. 2009	
						$ Change	% Change
General Fund	$1,124.1 m	$1,086.7 m	$1,084.1 m	$1,081.8 m	$ 1,086.6 m	-$ 37.5 m	-3.3%
Transportation Fund	$ 218.9 m	$ 211.4 m	$ 217.9 m	$ 217.8 m	$ 218.0 m	-$ 0.9 m	-0.4%
Education Fund	$ 155.2 m	$ 153.4 m	$ 152.9 m	$ 151.7 m	$ 151.3 m	-$ 3.9 m	-2.5%

Human Services

Vermont is rightly proud of its strong human services network – a gold standard among states. Through Choices for Care, Catamount Health, the Vermont Blueprint for Health and other innovative health and human services reforms, we've built a solid foundation that is helping vulnerable Vermonters find a path to health, employment and independence.

However, we cannot deny that the sharp growth in the demand for human services in recent years threatens the overall stability of our budget. Nearly one-third of our population receives services from the State. Next year, the Medicaid system alone will serve 172,000 Vermonters. Since FY 2000, overall spending on human services has increased 114%, an annual growth rate of 8%. In that same time period, inflation has only increased 25%.

Even last year, as we struggled to fill a significant budget shortfall, total human service spending grew by $100 million. Much of that increase was funded through the use of one-time federal recovery money. We must recognize that federal funds will not flow forever, nor should they. Vermont must take responsibility for ensuring the sustainability of its own programs. By starting the difficult process of realigning human service spending within currently available resources now, we will protect needy Vermonters from even more devastating cuts when the federal spigot is inevitably turned off.

The Governor's Recommended Budget is balanced, compassionate and sustainable. Vermonters expect that basic services for the many will be preserved - not just an enhanced benefit for the few. This budget proposes the elimination of some human service programs, appropriation reductions for many others and level funding for most remaining initiatives. At a time when there are difficult reductions across state government, it is essential to evaluate the mission, efficacy, and structure of human service providers to ensure they are in harmony with our core mission.

Although there is some diminished pressure on the budget due to low national inflationary trends, continued unemployment and reduced earnings have increased the number of Vermonters utilizing Agency of Human Services (AHS) programs. That's why this budget funds increases in caseload throughout AHS to ensure that Vermonters can get the help they need. However, in the face of this growing need, the loss of federal stimulus funding combined with revenue challenges results in difficult reductions in all areas of the budget.

Department for Children and Families (DCF)

There are several upward pressures in the DCF budget. Some are driven by the loss of ARRA dollars; others are driven by continued stress on programs as more Vermonters access services. Programs within DCF are proposed to be decreased in several areas to respond to these fiscal challenges. They include:

- *Provider Rates*: Reimbursement rates will decrease by 3% for most providers within the DCF system, including community programs, residential programs, and foster and adoptive parents.
- *Reduced Services:* Several service areas will absorb reductions. These include reduction of Reach Up Support Services and elimination of Individual Development Accounts.
- *Increased Quality Control and Enforcement:* Several programs show decreased costs associated with enhancing overall quality control and enforcement efforts.

Finally, DCF will be a major player in the restructuring of government programs, working toward greater effectiveness and efficiency, including the modernization of benefits eligibility and the merging of children's services for high risk children and families.

Reach Up

Low income families, who are struggling to enter the workforce, are served by our state's Reach Up Program. The FY 2011 budget has been raised substantially to address the increasing number of families now eligible for the program. To partially fund some of those increased costs, the Governor proposes strategically decreasing the level of some benefits. In each instance, these changes will save state dollars, increase incentives to fully meet work participation rates, and assist families who are working hard to move out of poverty. Three proposed policy changes are:

- Inclusion of $125 in Social Security Income (SSI) benefits as "family income" in calculating eligibility;
- Removing recipients from the program when they chronically refuse to complete their family development plan or to meet work requirements; and
- Preventing people who don't meet "hardship criteria" from receiving benefits for more than 5 years.

Department of Corrections

In Corrections, the Justice Reinvestment Initiative created through Act 179 of the 2008 Legislative session will continue, including investment in transitional housing, chemical dependency treatment programs, and other evidence based measures to reduce recidivism.

Department of Disabilities, Aging and Independent Living (DAIL)

In coming years, DAIL will focus on working with our many community partners to ensure that scarce resources are targeted to those who most need assistance. For example, the General Fund portion of the Attendant Services Program, which serves individuals with severe and permanent disabilities, will be redesigned to include income and asset requirements.

We are pleased to be able to support Vermont's 39 nursing homes that accept Medicaid payments to continue their important caregiver work by funding inflation in the amount of $2.8 million.

Over 2,000 Vermonters with developmental disabilities depend on state-supported programs to ensure their health, welfare, safety and to promote full community inclusion. This year we are able to provide nearly $6.7 million in caseload funding, including almost $1.8 million for new high school graduates.

In order to preserve our core programs, to the extent possible in these economic times, GF support for numerous smaller programs and services has been reduced or eliminated. For example, funding for the Housing and Supportive Services program has been eliminated and the five Area Agencies on Aging will see a 3% reduction in GF support.

Department of Health

The Vermont Department of Health (VDH) and their public health partners across the state have risen to the challenge of responding to the 2009 H1N1 influenza. Vermont has immunized more than 140,000 people, including over 50,000 doses administered at school clinics. The VDH proposed budget will continue to support public health efforts surround-

ing H1N1 as well as other public health preparedness programs.

Yet, as with all AHS departments, VDH must make some difficult budget decisions in this challenging fiscal environment. In Alcohol and Drug Abuse Programs, while we propose to maintain the current women's residential bed capacity at Valley Vista, it is clear from the service delivery data that the adolescent bed capacity has been consistently underutilized. The proposed budget moves adolescent care services to an "as needed" basis, with a corresponding reduction in the rate of payment.

Reductions in several grants are proposed, including grants to Area Health Education Centers. In addition, other small grants will be eliminated, such as those to the Kidney Association and the Addison Parent Child Center.

Department of Mental Health (DMH)

Substantial progress has been made on issues related to the Vermont State Hospital (VSH). We anticipate that the federal Center for Medicaid and Medicare Services (CMS) will certify VSH by July 1, 2010, reinstating Medicare and Medicaid reimbursement. Recognizing that this facility requires replacement, the FY 2011 capital budget includes funding for the proposed new fifteen (15) bed secure residential facility in Waterbury. The anticipated federal funds supporting the VSH allow $8 million in GF to be redistributed to other AHS programs.

In our community mental health system we are faced with the economic challenge of providing for our citizens with mental health and substance abuse conditions in a sustainable manner. We have already begun to work with the Designated Agencies to redesign such care in our state, and in collaboration with the Blueprint for Health to enhance these services. We must continue to improve care, but do so in a fiscally responsible manner that matches our resources.

Medicaid and Health Care Reform

The Office of Vermont Health Access (OVHA) is responsible for the management of Medicaid, the State Children's Health Insurance Program (SCHIP) and other publicly funded health insurance programs in Vermont. OVHA is the largest health insurer in Vermont in terms of dollars spent and the second largest health insurer in terms of covered lives. As of 2009, OVHA is the home of state oversight and coordination of Vermont's expansive Health Care Reform initiatives, which are designed to increase access, improve quality, and contain the cost of health care for all Vermonters. OVHA also now has responsibility for Vermont's health information technology (HIT) strategic planning, coordination and oversight.

Despite challenging financial times, the number of Vermonters lacking health insurance decreased from 9.8% in the fall of 2005 (61,056) to 7.6% (47,286) in the fall of 2008. This low rate of residents lacking health insurance is the second lowest in the nation and remained steady despite increased unemployment. This is due to increased enrollment in state-subsidized health care programs under the *Green Mountain Care* umbrella. The increased enrollment of almost 25,000 Vermonters is a health coverage success that, at the same time, has contributed to the state's budget pressures.

Our fiscal challenges demand that we address the long term sustainability of our publicly-supported health care programs. Although we have benefited from increased federal Medicaid match through ARRA, these increased funds are temporary and slated to expire on December 31, 2010, half way through FY 2011. As such, we must act now to bring these long term costs in line.

A Tiger Team effort helped point to four areas that could provide more efficiency in the use of our limited resources and / or maximize reimbursement potential:

- *Benchmark Vermont's benefit allowances through peer state comparisons with states of similar high standards to Vermont.* By examining the benefit structure of similar states across the country, OVHA has identified several categories of service that may be managed more efficiently through clinical operations changes (e.g., service limitations, prior authorizations, targeted provider reimbursement changes).

- *Maximize access to private insurance through the Health Insurance Premium Payment program (HIPP).* We will increase our efforts to enable Medicaid beneficiaries to access their employer's insurance without incurring additional costs or forgoing benefits that they would have received through the Medicaid program.

- *Expand the utilization of Vermont's premium based system.* In order to sustain our generous programs for low income Vermonters, we must request that a number of Green Mountain Care program participants contribute through targeted increases in premiums after the Maintenance of Effort (MOE) requirements in ARRA expire on December 31, 2010.

  The Governor is strongly committed to continuing support for the premium assistance programs associated with Catamount Health and employer-sponsored insurance. However, in these fiscal times, we must re-evaluate the very generous cost sharing benefits in the existing Catamount Health Plans, and increase the deductible to bring it in line with industry standards.

- *Make Administrative Improvements.* We must strengthen the relationship between the OVHA Program Integrity (PI) Unit and the Medicaid Fraud and Residential Abuse Unit (MFRAU) in order to better identify and eradicate waste, fraud and abuse.

  Similarly, our efforts must be strengthened to ensure that the funds supporting the programs for our beneficiaries are used efficiently and appropriately. For example, reimbursement for pharmaceuticals must reflect the true costs of the drugs and not artificially inflated prices. And we must ensure that transportation services for Medicaid beneficiaries are provided in the most efficient manner possible.

This proposal asks more from providers that have the financial capacity - from targeted rate adjustments for some providers to freezing the hospital provider tax rate in FY 2011. OVHA is committed to working with these providers to reduce administrative burdens that diminish their ability to deliver efficient quality care.

OVHA's Coordination of Benefits (COB) Unit will also continue to successfully focus on ensuring that the appropriate insurer covers the costs of care when an OVHA beneficiary has dual coverage (e.g. Medicare, private insurance); and will pursue casualty or estate recovery of Medicaid costs. In FY 2009, the COB unit recovered $8.6 million that supports our Green Mountain Care programs and is on track to recover a similar amount in FY 2010.

In combination, all of these efforts will help our programs be sustainable as we transition to any new programs that will emerge under federal health care reform.

Vermont Blueprint for Health

Recognizing that any truly comprehensive health care reform needs to address quality and cost, we continue to expand

the Vermont Blueprint for Health. Supported by investments in this budget, we will continue to negotiate with insurers for a rapid rollout of the Blueprint to the remaining Vermont communities; our hope is to have the Blueprint in all hospital service areas by 2011 and in all practices across the state by 2012. In the past 18 months, we have launched the Blueprint multi-payer Integrated Medical Home Pilots in three areas of the state that are changing the way care is delivered at the local level and ultimately will slow the growth in health care costs. We also are collaborating with Maine, New Hampshire, Massachusetts and Rhode Island, with support from the Milbank Foundation, to develop a New England wide medical home pilot initiative, and will be applying for a Medicare Demonstration grant to have full Medicare participation in the Blueprint effort.

During 2008 and 2009, we implemented a fee to support HIT for primary care providers and further our statewide health information exchange network and a 340B Pharmacy program to decrease the pharmaceutical cost for Federally Qualified Health Clinic (FQHC) patients. We also began implementation of a multi-payer claims database to increase our understanding of Vermont's health care utilization, expenditures, and performance across all payers and services. We also are participating in a pair of external two-year evaluations to assess the success of our efforts to improve access and affordability for health care coverage.

In addition, OVHA continues to implement initiatives to help improve the quality of health care services for our most vulnerable citizens and also to contain costs of these publicly-supported programs. OVHA's Chronic Care Initiative (CCI) is providing care coordination for beneficiaries with the most significant needs, including those who are taking Buprenorphine. The CCI program is expected to yield a savings of $6.4 million in FY 2010.

Education

"The ever-growing burden of property taxes threatens the financial security of Vermonters and the potential of our employers. Getting a handle on this cost is essential to our economic future."

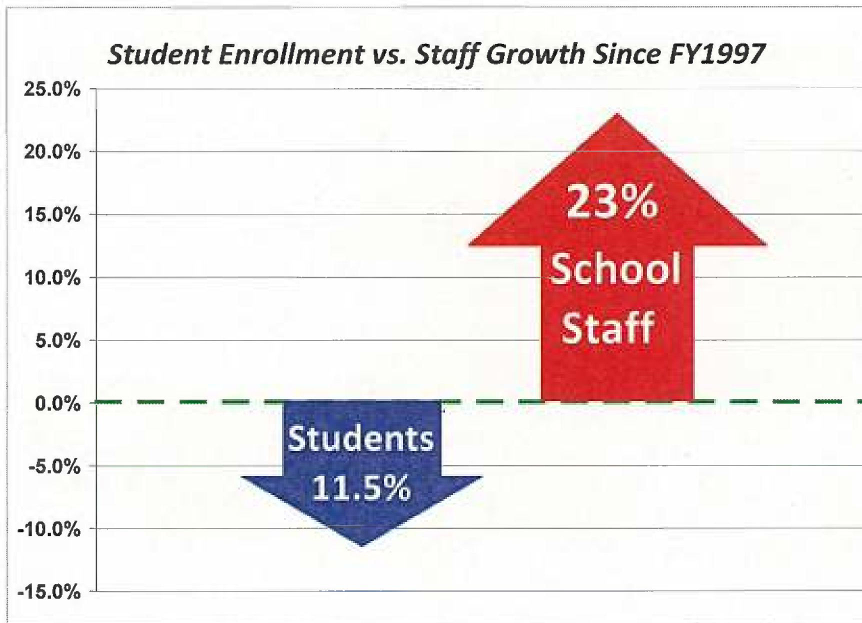
- Governor Jim Douglas, State of the State Address, Thursday, January 7, 2010

Vermont's K-12 education system is among the highest staffed per pupil in the United States. According to Department of Education (DOE) statistics, Vermont ranks first in student-to-teacher ratio at 10.8:1. This is 44% higher than the national average of 15.5:1.

However, when it comes to wealth, Vermonters are not in the top tier. Federal statistics show that Vermont ranks 24th in personal income per capita at $34,623, an amount below the national average of $36,629.

When Act 60 passed the Legislature in 1997, it was clearly understood that low spending school districts would be encouraged to spend more given the improved access to funding through the statewide property taxes. However, since 2005, school spending and property taxes have continued to rapidly grow. In FY 2005, the net residential property tax was $254.2 million. For FY 2011, it is projected to be $375.6 million, equaling an annual growth rate of 6.8%. Similarly, the non-residential property tax has grown from $385.8 million to $562.8 million, for a 6.5% annual growth rate.

This growth was not driven by more students in the classroom, as the student population actually decreased over this 6-year period from 99,994 to 92,631 or 7.4%. Since 1997, staffing levels have grown by 23%, from 15,555 to 19,145 while the student population has decreased by 11.5% (see chart on next page).



Income sensitivity subsidies are projected to grow to $167.8 million in FY 2011, an annual increase of 18.5%. Remarkably, this increase of $26.2 million is larger than the projected $21.3 million growth in education spending. Basically, income sensitivity transfers the burden of the property tax from eligible beneficiaries to property tax payers who are not eligible, namely non-residential property owners and property owners with household incomes above $90,000. In 2009, there were over 6,000 Vermonters receiving a property tax subsidy who own homes valued at $400,000 or more, and of this group, 136 people lived in homes valued at $1 million or more.

If left unchecked, property tax rates will continue to rise over the next 3 years. Doing nothing is not an option. Three major goals for this legislative session must be:

- Lower property tax rates: Current projections call for a 2 cent increase in both the residential and non-residential property tax rates next year. The combination of these tax increases and dramatically slower growth in the grand list, result in $58 million in higher taxes. During this recession, we must seek to lower property tax rates on households and businesses struggling to make ends meet.
- Constrain education spending: As noted above, the core driver behind education spending growth is increased staffing. Pressure needs to be exerted that not only inhibits such increases, but actually results in staffing decreases to affordable levels.
- Rebalance income sensitivity subsidies: The cost of income sensitivity to the Education Fund is growing at exorbitant rates. Through rebalancing the income sensitivity subsidies, not only can the direct costs be diminished, but costs will be tempered indirectly, as more voters will be sensitive to school spending increases.

To achieve the above, the Governor offers the following proposals:

- Property Tax Rates: Rather than increase rates by 2 cents, as currently projected, the Governor proposes to lower both the residential and non-residential rates by 1 cent, from $.86 to $.85 and $1.35 to $1.34 respectively.
- Income Sensitivity: The Governor proposes to make income sensitivity subsidies more progressive. Currently, all homestead property owners with incomes less than $90,000 are limited to paying no more than 1.8% of their income as adjusted by their local education spending inflator. Under the Governor's proposal, those earning less than $60,000 would pay no more than 1.8% of their income times their local inflator. For incomes between $60,000 and $75,000, the maximum income percentage would be 2.25% times the local inflator. For incomes from $75,000 to $90,000, the maximum income percentage would be 3.5% times the local inflator. Further, the income sensitivity calculation for

all homeowners with incomes below $90,000 would be based upon the house site value up to $400,000.

In addition, to provide assistance to those saving to purchase a home, the Governor proposes enhancing the renter rebate benefit by raising the income eligibility cap from $47,000 to $54,000. This threshold has not changed since 1995.

- Efficient Governance: The State Board and Department of Education have made the "Transformation of Education" a priority with a focus on the governance structure as a key platform on which to build better outcomes for students. In Vermont, we have 290 separate school districts – one for every 312 students – 63 different supervisory bodies and a State Board of Education. That's a total of 354 different education governing bodies for a state with only 251 towns. It is imperative during this upcoming year that some form of school district consolidation occurs. In addition to the significant savings this would bring from reducing the duplication of administration salaries and operating costs, there are even greater benefits for students. By aligning Vermont's current districts into larger bodies, students are given greater choice of programs and activities within their region to find their individual path to success.

Further, the Education Fund and property tax payers support two expensive programs that discourage consolidation. The Governor proposes to phase-out the small schools grants over the next two years and the "phantom student" subsidy over the next three years. The latter pays school districts for non-existent students by limiting an annual enrollment decrease to 3.5% even though the actual decrease may be much more. These changes, in addition to those recommended by the joint "Challenges for Change," can save over $40 million during the next two years.

- Reduce Education Costs:

Health Care Premiums: State employees pay 20% of their healthcare premiums. It is reasonable for teachers to be on par with state employees and cover 20% of their health care costs. As contracts come up for renewal, such a requirement should be incorporated in each contract with local teachers. This commonsense change will save taxpayers about $15 million over the next three years.

Reduced Staffing Levels: As noted above, Vermont has the lowest overall student-to-teacher ratio at 10.8:1. Vermont needs to set an affordable standard for this key ratio. The Governor recommends a 13:1 statewide ratio as this is far below the national average of 15.5:1 and still among the best in the nation. At a 13:1 ratio, Vermont would be ranked among the top ten states in the nation, just between New Hampshire to our east, New York to our west and well above Massachusetts to our south. This approach will save taxpayers over $100 million over the next four years.

There are many methods to achieve this standard from statutory position caps at the district or supervisory union level to leveraging retirement by restricting access to the State Teachers' Retirement system as the "check valve" to ensure a portion of positions vacated due to retirements are not filled. The Administration will work with the Legislature to develop the most appropriate mechanism to accomplish the goal and achieve the savings.

- School Construction Assistance: School construction costs properly belong in the Education Fund. These costs have been historically borne by the General Fund in addition to significant increases in the transfer of General Funds to the Education Fund. The Governor proposes that the Education Fund cover $5 million of

school construction costs each year for the next eight years to fully retire the obligation.

- Teachers' Retirement: Like school construction, the cost of the teachers' retirement is supported entirely by the General Fund – this despite being an education expense driven by contract decisions made at the local level. As teachers' pension and post-employment health insurance costs grow, they squeeze out General Fund priorities like human services and public safety. The Governor proposes to phase teachers' retirement costs into the Education Fund over a four-year period beginning in FY 2011, approximately $10 million next year.

The Governor's proposals for education reform go to the heart of runaway spending. Rather than a 2 cent increase in property tax rates, the Governor's proposals result in a 1 cent decrease. Compared to leaving the system "as is", the Governor's proposals result in $35 million in lower property taxes in FY 2011 – a welcome break for taxpayers.

State Employees' and Teachers' Retirement Changes

Last year, in response to warnings from the Governor, Treasurer, legislative leaders, and concerned citizens, the General Assembly established the *Commission on the Design and Funding of Retirement and Retiree Health Benefits Plans for State Employees and Teachers* to analyze Vermont State employees' and teachers' pension plans, as well as retiree health benefits. Without significant reforms, the total annual cost of funding the retirement systems will increase from $73.5 million this year to $103.5 million in FY 2011, exacerbating an already wide budget gap.

The Commission crafted a series of recommendations to hold down retirement costs to the 3.5% expenditure growth target established by the Joint Fiscal Committee. The Commission's final proposals include increasing the early and normal retirement age, lengthening the salary compensation period, increasing the maximum benefit, linking the contribution levels for the employer and employee, and adding tiers to qualify for post-employment health insurance premium cost sharing.

Active employees within 5 years of eligibility for early or normal retirement will not be impacted by these recommendations. Also, it is important to note that none of these proposals affect current retirees; as the Commission's report clearly states: "*Under no circumstances, however, do we consider any recommendations of this report to apply to current retirees of either system.*"

The Governor applauds the Commission – and, in particular, the leadership of State Treasurer Jeb Spaulding – for its exceptional work on this difficult challenge. The Governor's budget advances the Commission's recommendation which will save the General Fund approximately $25 million in FY 2011.

For the Commission's final report, visit:
http://www.vermonttreasurer.gov

Higher Education

It is clear that education and training beyond high school is critical for Vermonters and beneficial to the state as a whole. While the long term trend is that incomes are rising for college graduates, real incomes are declining for those with only a high school education. More than two-thirds of Vermont's fastest-growing occupations require postsecondary training, making access to affordable postsecondary education a necessity. Further, college graduates contribute nearly twice as much in federal, state, and local tax payments as high school graduates. For many Vermonters, a need-based financial assistance program is essential to ensure access to affordable postsecondary education options.

Vermont students and families face difficult challenges in paying for education and training beyond high school. In addition to funds for the University of Vermont (UVM) and Vermont State Colleges (VSC), the State also provides funding through the Vermont Student Assistance Corporation (VSAC) for incentive grants and non-degree grants, the Vermont Opportunity Scholarship, and the Vermont Honor Scholarship. All these enable many Vermont students to enroll in postsecondary programs that best meet their educational needs.

For FY 2011, the Governor proposes a base increase of $5.5 million shared by UVM, VSC, and VSAC. Also, the Governor proposes $2 million each in capital funds for UVM and VSC for facility upgrades and infrastructure needs.

Next Generation Scholarships also play an important role in encouraging Vermont high school students to continue their education and training. By providing much-needed financial aid to Vermont students who might not otherwise consider college affordable, these scholarships boost students' aspirations, turning their focus toward academic achievement and less on how to pay for college.

Next Generation funding for the non-degree grant program is essential to meeting the needs of Vermonters seeking to acquire, keep, or expand their employment skills. Non-degree grants are the only source of non-loan, need-based financial aid for adult students taking courses at institutions such as vocational/technical centers and trade-specific training schools. This type of grant is unique to Vermont and is particularly useful for working Vermonters.

To make higher education more affordable for young Vermonters, the Governor proposes to restore $1.5 million to our Next Generation Scholarship Fund.

Human Resources

Collective Bargaining

This past fall, the State of Vermont negotiated a historic collective bargaining agreement with the Vermont States Employees' Association (VSEA) that will govern three of the four major bargaining units of state employees for fiscal years 2011-2012. This agreement, necessitated by an unprecedented economic downturn, will result in a 3% pay reduction for all classified employees in FY 2011, no across-the-board adjustments (commonly referred to as a COLA) in FY 2011 or FY 2012, and a freeze on all step increases for the duration of the contract. The Governor is grateful for the sacrifice made by our state employees; this agreement provides essential savings for state government at a time when every dime matters.

DHR Consolidation

The Governor has approved a statewide consolidation of human resources across the Executive Branch of state government. This consolidation will bring agency and department human resource professionals under the direct management of the Department of Human Resources (DHR) for the first time. Under this new structure, DHR will be well positioned to support state agencies and departments in the administration of its workforce through best management practices. This will promote better HR communications and the consistent application of employment policies, practices and laws, to the benefit of employees and the employer. Skillful and consistent management practices will maximize workforce efficiency, productivity, and job satisfaction, while minimizing potential grievances and legal claims. Simply put, this consolidation will ensure that the State of Vermont maintains its status as the premier employer in the state.

Economic Development

Recognizing the many challenges businesses face during this prolonged downturn, the Governor proposes utilizing discretionary ARRA funds to boost economic development. This proposal includes $2 million to the Vermont Economic Develop-

ment Authority (VEDA) to provide subsidized lending and credit support to new and existing Vermont businesses, as well as money for telecommunications and agriculture initiatives, noted elsewhere in this document.

In 2008, an independent study estimated that every dollar invested in the Vermont Training Program (VTP) results in $2.67 in state revenues. In recognition of the program's high rate-of-return and the pressing need for high-wage jobs, the Governor proposes to add $1 million in funding for the VTP. Adding these funds to the VTP will ensure that 40 employers and 1,800 Vermonters have access to the program this year.

Vermont's natural beauty and outdoor sports are valuable assets that can generate growth and create jobs. Therefore, the Governor's proposal includes an additional $500,000 for the Department of Tourism and Marketing to promote Vermont as a vacation destination.

The Governor also commits $1 million to assist businesses impacted by the closure of the Lake Champlain Bridge through a combination of direct grants and low-interest loans.

Investing in Affordable Housing

For FY 2011, the Governor proposes to level fund the transfer of property transfer tax receipts to the Vermont Housing Conservation Board (VHCB) at $6.1 million. These funds, in addition to other special and federal funds, result in an increase in VHCB funding in FY 2011 to $23.8 million, or $3.9 million over the FY 2010 level.

For the longer term, one of the Governor's Tiger Teams took a close look at ways to maintain, and even enhance, investments in affordable housing. Overall, the team found that the state's affordable housing community achieves good work for Vermont families.

However, there is an alphabet soup of statewide affordable housing entities: VHFA, VHCB, VSHA, HFI, and DEHCD. Among these entities, 130 employees are managed by four separate boards with 37 individual board members, three executive directors, and one commissioner – all costing about $9 million in personnel expenses.

These publicly funded entities frequently negotiate with each other to channel their separate investments into the same affordable housing project.

Through a redesign process, a 10% savings in the $9 million staffing costs of statewide entities would free up $900,000 annually. Savings from redesign would support new investments in affordable housing of over $20 million. The Governor has asked Commissioner Brooks to convene a meeting of key customers and leaders in our affordable housing community on the numerous opportunities identified by the Tiger Team to enhance our investments in affordable housing.

The full Tiger Team housing report can be found at: http://aoa.vermont.gov/.

Taxes

In recent years, Vermont has made some progress in improving both our corporate and income tax programs. In 2004, the Governor proposed that Vermont move to "unitary combined" reporting for the corporate income tax, thus closing a tax loophole used by large, multi-state corporations. This allowed Vermont in 2006 and 2007 to lower the State's top corporate tax rate from a national rank of 5th highest at 9.5% to 13th highest, tied with New Hampshire, at 8.5%. Last year, the Governor's efforts to lower the State's personal income tax rates also achieved some success.

However, while lowering income tax rates last year, the Legislature made other changes that increased tax burdens. Changes the Legislature made in the capital gains and estate taxes have swelled the ranks of Vermonters who are looking

at other states – like New Hampshire or Florida – for their new, permanent residences. In addition, the estate tax change was particularly unfair to farmers whose assets are not easily mobile. It is a punitive tax that discourages farmers and small business owners from passing along their life's work to sons and daughters.

Capital Gains Tax

In the 2009 session, the Legislature enacted changes in the tax treatment of capital gains income, but their plan did not provide protection for anyone under 70. These changes resulted in $9.3 million in new taxes to support spending increases.

Favorable treatment of capital gains income encourages entrepreneurship and investment, protects the retirement income of seniors, and eases the transfer of small, family-owned businesses from one generation to the next.

Governor Douglas proposes to sunset the capital gains tax changes made by the Legislature last year.

- Effective January 1, 2011, long-term capital gains will again be eligible for the 40% exemption, as they were in tax year 2008.
- The individual income tax rate decreases effective in 2009 and 2010 will remain in effect.

Removing the capital gains exemption could be justified if all the revenues were used to lower tax rates for working Vermonters. However, using a sizable portion of the proceeds to support spending, as the Legislature did, amounts to a tax hike on already over-taxed residents.

Estate Tax Reform

Vermont currently piggybacks on the federal estate tax, with some modifications. Last session the Legislature amended the Vermont estate tax to block the federal increase in the exclusion amount to $3.5 million, leaving Vermont's estate tax with an exclusion of only $2 million.

The Legislature also intended to block the one-year federal repeal of the estate tax, but changes to law to accomplish this were not precise, leaving the state law ambiguous. Given this confusion, we propose the Legislature clarify its intent to decouple from the underlying federal statute and implement a permanent $3.5 million estate tax exemption.

The official FY 2011 revenue forecast for the estate tax is $18.1 million based on the current $2 million exemption. The Governor's proposal would save taxpayers $3.0 million in estate taxes. It's important to understand that while current federal law sunsets the estate tax for calendar year 2010, it also instituted a new capital gains tax on the sale of estate property upon which the state piggybacks. The proceeds from that new capital gains tax on inheritances are expected to be $3.0 million for a 12-month period. Therefore, to avoid double taxing inheritances, once with an estate tax and yet again with the capital gains tax, the Legislature must revisit the estate tax and raise the exemption to the Governor's recommend.

With Vermont's high marginal income tax rates, there is little justification for taxing the estates of Vermonters who have built their businesses here, or farmers looking to pass on their legacy.

Transportation

During the past seven years we've increased our commitment to transportation – catching up after decades of under-funding. Since the Governor first came to office, $13 million has been returned to the Transportation Fund for use on our roads, bridges and culverts. This budget proposes reducing the raid on the Transportation Fund by another $3.5 million, directing that money to municipalities across our state through our town

highway program.

For FY 2010, our transportation budget increased $140 million. Much of this growth is a result of the federal recovery act – an opportunity of which we've made the most by working in a strong bi-partisan fashion. Vermont is a leader in how it spends its transportation stimulus money. As the ARRA program rolled out during the spring and summer of 2009, VTrans was hailed by the national press for being the third best transportation agency in the nation when it came to putting its stimulus money to work quickly.

This budget includes $14.0 million more in transportation spending versus FY 2010; an increase of $155 million over the pre-ARRA FY 2009 adjusted budget. VTrans plans to pave 90 miles of Interstate this coming construction season. By November 2010, VTrans will have resurfaced 50% of Vermont's 640 interstate one-lane miles since 2006.

The FY 2010 budget saw paving top $100 million for the first time ever, while the FY 2011 budget sees bridge funding top $100 million for the first time. Between this year and next, Vermont will spend more than $400 million paving its roads and fixing its bridges, funding levels that are unprecedented in the State's history.

Since the establishment of the Governor's *Road to Affordability* program in FY 2007, VTrans has increased spending on preventative maintenance from $8.1 million annually to $35.4 million in the proposed FY 2011 budget, a 335% increase.

All this recent attention to bridges and pavement is beginning to show progress. In 2008, 36% of Vermont roads were in very poor condition, while in 2009 the percentage fell to 34%. With about $100 million expected to be spent this coming construction season, this percentage will continue to drop and be even lower by the end of 2010.

The news is similarly good when it comes to bridges. In 2004, 11.2% of Vermont's Interstate bridges were structurally deficient. Today, just 7% are structurally deficient. Similarly, in 2004, 18.5% of town highway bridges were structurally deficient, while today just 15.9% are structurally deficient.

Not everything is trending in the right direction. The percentage of structurally deficient state highway bridges has increased slightly, from 20% in 2004 to 20.4% today. But with an FY 2011 bridge budget topping $100 million, VTrans anticipates that the overall positive progress for Vermont's bridges will continue.

Progress also continues to be made with public transportation. Since the Governor took office, Vermont's public transit budget has nearly doubled from $12.7 million in FY 2003 to $24.7 million in FY 2011. This increase has resulted in the creation of dozens of new bus routes serving all corners of the state, and has helped reduce Vermont's carbon emissions and greenhouse gases.

Capital Infrastructure

In the Governor's FY 2011 capital budget there is a continued emphasis on, and commitment to, the modernization and sustainability of critical state infrastructure to support the needs of all Vermonters. The Capital Bill provides funding for the development and future construction of the State's Health Laboratory in collaboration with the University of Vermont.

The Governor is also recommending that $25 million be appropriated to upgrade and rehabilitate buildings and facilities. Major maintenance funding for Buildings and General Services, Forest and Parks, Fish and Wildlife, the Military, the University of Vermont, and Vermont State Colleges will help to better serve hundreds of thousands of Vermonters. This aspect of the Governor's proposal represents immediate investment and will employ thousands of trades people across a wide spectrum of disciplines from both large and small companies and businesses.

Last year, the Legislature appropriated $31.6 million of ARRA money to be awarded by the Clean Energy Development Board. Of this amount, $17.1 million remains unobligated to specific projects. The Governor proposes that $9 million be used to fund state projects that meet the objectives of the Clean Energy Development Fund (CEDF). Using this money on state projects will get the money into the economy quickly and will save taxpayers millions of dollars in operating expenses as well as reduce administrative overhead.

Part of our commitment to a better environment and lower costs in the future is to make State government, itself, a leader in the use of renewable energy. The new state office building in Bennington will use geothermal energy – energy from the ground – for both heating and cooling. Using $2 million of the $9 million, the State will save 30,000 gallons of oil, 510,000 kilowatt hours of electricity, and avoid emitting 640 tons of CO_2 into the atmosphere – not to mention save $175,000 for taxpayers each year. This is a very tangible example of how good environmental practice is also good fiscal and economic policy.

Within Vermont State Parks, the Governor proposes spending $1 million for fiscally sound alternative energy programs, including solar hot water for showers and burning wood pellets.

The remaining $6 million will fund energy efficiency projects for the State complex in Waterbury. There are $10 million of backlogged efficiency projects within the complex.

Information Technology

Years ago, buying an airline ticket was a complex and time consuming experience: you went to a travel agent, waited around for someone to see you, the agent made a bunch of phone calls, and finally you got a paper ticket. Then, at the airport, you waited in line to check in and trade your ticket for a boarding pass. Today, you make almost all your travel arrangements on the web including printing your boarding pass. For those without internet access or needing help, there are kiosks at airports and helpers who stand ready to assist.

It is time for Vermonters to have these same technological advantages when dealing with their state government. Although the State has done a good job automating some transactions, primarily in the Tax Department and the Department of Motor Vehicles, we can and must go further.

Antiquated systems deny state agencies both the information needed to deliver the correct benefits to the right people without gaps or duplication and the information needed to measure outcomes. Better client-focused systems will help us deliver aid more precisely where it's needed at less cost for delivery.

Consider individuals who seek assistance from our Agency of Human Services. Today they must travel to a state office, wait for a person to assist them and then provide detailed information to that person who transfers it to a form. Often they don't know the answers to some of the questions or have not brought in required documentation. Sometimes they've gone to the wrong office because they didn't know which program operated from where. Yet another visit, and doing more "agency time," is needed, taking them away from child care, work, or looking for a job. And then they go home and wait--perhaps for weeks--to find out whether they qualify.

Now imagine a web portal called myvermont.gov. Vermonters seeking any type of state assistance populate one page on this site with their personal information on any available computer – at home, at work, or at their local library. The portal links to all state and federal programs in an orderly and understandable way. If a visit to a state office is still needed, the client will know exactly what information to bring. For those clients who either don't have computer access or who simply want help completing forms, a visit to any State client service office will do. As in the airport, there will be kiosks and helpful state employees to assist them.

To move rapidly toward this future, the Governor proposes $8 million in the capital bill for technological modernization. This investment will move the State toward a more efficient paperless state government and will reduce the annual amounts the State spends on inefficient procedures. By the end of 2011, no state internal procedures should be dependent on physical paper flow and all new records will be electronic. Almost every transaction between the State and its clients will be available online and through kiosks, although the State will preserve telephone and personal transaction capability as well. The default for outgoing communication from the State will be electronic.

Further, the State will begin the implementation of an electronic purchasing system that will reduce administrative cost and allow for better quotes and lower prices. Small Vermont firms say they cannot afford to produce the documents required by State bids. Allowing online bidding will give these firms the opportunity to compete for state business.

The State will move to modern technologies like server virtualization and cloud computing in order to create greater flexibility and reduce future capital and operating costs for information technology. The State is also consolidating all common functions including email and conferencing across the Executive Branch.

e-State Initiative

Within the next few years, broadband and wireless access across our state will be essential if we hope to have a strong and healthy economy. Vermonters will need these services as part of their daily life: at work for communication, sales and purchasing; and at home for accessing myvermont.gov, e-health, e-education, and for personal use.

The Governor proposes over $3 million in stimulus money for the Backroads Broadband program to speed Internet adoption and serve the hardest-to-reach Vermont residences. The capital budget also proposes $5 million for the Vermont Telecommunications Authority (VTA) to leverage already approved revenue bonding authority and private capital to build "middle-mile" fiber capability to schools, hospitals, and government offices. These funds will also accelerate cell tower build-outs. The recommended $750,000 operating budget for the VTA will allow quick progress towards accomplishing the e-State initiative.

As high-speed internet becomes ubiquitous, the Vermont Interactive Television network (VIT), which has served us well, will be supplanted. Given its fixed locations and inability to support remote video access from homes and offices, a period of transition is necessary. The Governor proposes to level-fund VIT in FY 2011 but then step down to 50% funding in FY 2012 and zero funding in FY 2013. These funds will be assigned to the Vermont State Colleges to facilitate this transition.

Boards and Commissions

In the course of reviewing every area of state government for opportunities to streamline operations and for efficiencies, one of the Governor's Tiger Teams made a thorough review of Boards and Commissions. No complete list existed, as they are sprinkled throughout our statutes, and are associated with departments and programs throughout state government. The team found approximately 300 such groups, and surveyed their associated departments as to their level of activity and value to state government operations. Not surprisingly, many have been inactive for years, and some that remain active have questionable value. In addition, there are opportunities for consolidation and cost savings.

In the next few weeks, the Administration will present to the Committees on Government Operations its recommendations to abolish, consolidate or otherwise modify as many as 50 Boards and Commissions. While the direct budgetary savings

are modest, this kind of housekeeping is essential to the continued smooth operation of government.

Judiciary

In 2008, the Commission on Judicial Operations was created by the Legislature to review the current structure of Vermont's court system. The Commission's Report to the Legislature recommended wide-sweeping, but necessary, changes to the current system. The recommended changes will improve access to courts for all Vermonters while saving $1 million annually.

The Commission recommended several steps to achieve a judicial system that is unified both administratively and financially including consolidation of the court system, a restructuring of the probate courts, elimination of the judicial role of assistant judges, and an increase in the use of technology. The Judiciary has submitted a plan to the Legislature to achieve this needed reorganization and modernization while ensuring all Vermonters have access to our courts. The Governor has included this plan as part of his FY 2011 budget recommendation.

Protection

The Governor's FY 2011 budget continues to honor the State's commitment to protect children and families as we expand the number of Special Investigation Units (SIUs) in Vermont. This budget will increase the number of SIUs from eight (8) units to ten (10) units covering all regions of the State. This will provide the benefit of the program to all Vermonters consistent with the intent of the Administration and Legislature.

The Vermont State Police hired thirteen new troopers in July 2009. These new law enforcement officers have completed training and are now deployed statewide. An additional nine recruits have also been hired and will graduate from the Vermont Police Academy on May 28, 2010. With these additional troopers our State Police force will be at the highest level during the Governor's tenure.

Maintaining troop levels in the State Police force has allowed staffing of the Drug Task Force to remain steady, a critical component of the State's response to a dramatic increase in heroin distribution during the past several years.

To support our public safety officers, the State has moved forward with a new state-of-the-art forensic laboratory, scheduled for occupancy this coming October. The forensic laboratory also continues to maintain its national accreditation status, and the expanded Emergency Operations Center is scheduled to be in operation in the spring of 2011.

Environmental Protection

The Agency of Natural Resources (ANR) continues to succeed in performing its core mission with a restricted budget. The Agency is effectively making use of alternate funding sources and structural efficiencies. Work will continue to be brought into alignment with available funds, including federal reimbursement.

The Department of Environmental Conservation's Division of Geology is proposed to be transferred to the University of Vermont. The pollution prevention activities of the Environmental Assistance Office will be merged into the Waste Management Division to create the Waste Management and Pollution Prevention Division. Other efficiencies and the prioritization of core functions will allow ANR to continue to protect Vermont's natural resources in these difficult times.

Clean and Clear Action Plan

In 2004, the State of Vermont adopted an aggressive plan for reducing pollution and protecting Vermont's waters statewide, including controlling algae-feeding phosphorus discharges to

Lake Champlain. Since 2004, our Clean and Clear program has supported hundreds of water quality projects from improvements in municipal storm water systems to planting over 7,000 acres of winter rye as a cover crop to reduce spring erosion.

Over the past six months, ANR has revised the implementation plan for the Lake Champlain Phosphorus Total Maximum Daily Load (TMDL). More than 300 Vermonters contributed to this revised plan, which was delivered to the Legislature this past week.

The proposed funding for Clean and Clear in FY 2011 includes $8 million in state operating and capital funds to support the priorities assigned to the Agencies of Agriculture, Transportation and Natural Resources.

The budget includes a pass-through appropriation for support of the Lake Champlain Citizens' Advisory Committee, which provides input to the General Assembly, the Lake Champlain Basin Program, and ANR on issues related to the management and protection of Lake Champlain.

The Watershed Improvement appropriation provides the funding to support watershed education efforts and projects that protect, restore, or enhance Vermont's watershed resources.

Support for Vermont Farmers

Even in these difficult times, the Governor's recommended budget reflects concern for farmers across Vermont. The Governor proposes:

- $1 million in ARRA funds to be dedicated to lower borrowing costs for farmers using VEDA's agricultural loan program.
- Financial assistance for farmers to maintain vegetated buffers along waterways, to develop alternative manure management technologies, and for nutrient management planning.
- $100,000 for the Farm-to-Plate initiative through the Vermont Sustainable Jobs Fund.
- Support for Vermont agricultural fairs with a state stipend of $175,000 and capital improvements of $180,000 through the Capital Bill.

The Governor also proposes to continue with the Vermont Farm to School Network. This network provides statewide leadership, coordination, and advocacy to advance new and existing Farm to School efforts in Vermont classrooms, cafeterias and communities.

By accessing alternate funding sources, the Agency of Agriculture, Food and Markets is able to maintain level funding and align its structure to current needs to fulfill its crucial regulatory, development and policy role for the State.

Tables and Charts

The following pages contain charts, tables and statistics relating to the FY 2010 Budget Recommended Adjustment and the FY 2011 Governor's Executive Budget Recommendations.

FISCAL YEAR 2010 BUDGET RECOMMENDED ADJUSTMENT

FUNCTION / Department	Appropriation Title	2009 (Spec Sess) Act 1 Section Amended	General Fund	Transportation Fund	Education Fund	Special & Tobacco Funds	Global Commitment Fund	State Health Care Resources Fund	Catamount Fund	Federal Funds	ARRA (1) Funds	Other (2) Funds	Combined Funds
	FY 2010 As Appropriated		**1,088,279,019**	**213,555,681**	**1,313,626,522**	**280,719,087**	**965,735,967**	**156,955,519**	**27,208,601**	**1,456,100,724**	**373,350,323**	**216,703,194**	**6,092,234,637**
Rescission approved by Joint Fiscal Committee 8/18/09			(17,558,157)	-	1,800,000	1,068,343	(5,129,926)	(1,516,973)	-	(3,505,055)	(300,857)	630,430	(24,512,195)
Adjustments to reductions included in as passed and rescissison													
Alternate Savings Plan (2009 Spec Sess Act 2 Sec 10(d))			4,311,811	-	-	(1,298,861)	(2,644,254)	-	-	(3,995,038)	(292,190)	(1,170,955)	(5,089,487)
Labor Savings Plan			267,932	(1,713,505)	-	(217,485)	(736,253)	-	-	(945,569)	(81,356)	(778,744)	(4,204,980)
AHS Grant and Contract Reductions (2009 Spec Sess Act 1 Sec B.1104)			44,695	-	-	10,600	(643,133)	-	-	(378,870)	(71,066)	-	(1,037,774)
Distribution of Premium Rate Holiday (from Labor Savings Plan)			-	-	-	-	-	-	-	(4,909)	-	-	(4,909)
	FY 2010 Revised Budget (Post Rescission)		**1,075,345,300**	**211,842,176**	**1,315,426,522**	**280,281,684**	**956,582,401**	**155,438,546**	**27,208,601**	**1,447,271,283**	**372,604,854**	**215,383,925**	**6,057,385,292**
FY 2010 RECOMMENDED BUDGET APPROPRIATION ADJUSTMENTS :													
GENERAL GOVERNMENT													
Information and Innovation	Communications and Information Technology	B.101	120,798	-	-	-	-	-	-	-	-	(254,006)	(133,208)
Information and Innovation	Health Care Information Technology	B.102	-	-	-	(2,547,601)	(339,500)	-	-	-	-	-	(2,887,101)
Finance & Management	Financial Operations	B.104	-	-	-	-	-	-	-	-	-	4,006	4,006
Tax	Administration/collection	B.109	-	-	-	(97,503)	-	-	-	-	-	-	(97,503)
Buildings & General Services	Engineering	B.111	13,502	-	-	-	-	-	-	-	-	-	13,502
Lottery Commission	Lottery Commission	B.143	-	-	-	-	-	-	-	-	-	200,000	200,000
	TOTAL GENERAL GOVERNMENT		**134,300**	**-**	**-**	**(2,645,104)**	**(339,500)**	**-**	**-**	**-**	**-**	**(50,000)**	**(2,900,304)**
PROTECTION													
Public safety	State Police	B.209	(122,000)	-	-	-	-	-	-	-	-	-	(122,000)
Public safety	State Police	B.209	(2,150,000)	-	-	-	-	-	-	-	(4,400,000)	6,550,000	-
Public safety	Fire Safety	B.212	122,000	-	-	-	-	-	-	-	-	-	122,000
Public safety	Fire Safety	B.212	600,000	-	-	-	-	-	-	-	-		600,000
Military	Military - Air Service Contract	B.216	33,000	-	-	-	-	-	-	-	-	-	33,000
Criminal Justice Training Council	Criminal Justice Training Council	B.221	89,718	-	-	-	-	-	-	-	-	-	89,718
Public Service	Regulation & Energy	B.235				(31,592,500)							(31,592,500)
	TOTAL PROTECTION		**(1,427,282)**	**-**	**-**	**(31,592,500)**	**-**	**-**	**-**	**-**	**(4,400,000)**	**6,550,000**	**(30,869,782)**
HUMAN SERVICES													
Secretary's Office	Global Commitment	B.301	12,886,127	-	-	579,460	-	(2,587,084)	(2,812,913)	2,449,006	3,771,061	-	14,285,657
Office of Vermont Health Access	Administration	B.306	-	-	-	2,547,601	339,500	-	-	-	-	-	2,887,101
Office of Vermont Health Access	Medicaid Program - Global Commitment	B.307	-	-	-	-	2,415,420	-	-	-	-	-	2,415,420
Office of Vermont Health Access	Medicaid Program - Long-term Care Waiver	B.308	(1,232,421)	-	-	-	-	-	-	(2,298,457)	(549,043)	-	(4,079,921)
Office of Vermont Health Access	Medicaid Program - State Only	B.309	(2,138,656)	-	-	-	(1,887)	-	3,817,374	-	-	-	1,676,831
Office of Vermont Health Access	Medicaid Non-waiver Matched	B.310	35,885	-	-	-	-	-	-	1,560,226	(1,060,380)	-	535,731
Health	Administration & Support	B.311	(241,918)	-	-	-	(915,379)	-	-	(21,155)	-	-	(1,178,452)
Health	Public Health	B.312	91,765	-	-	-	542,558	-	77,000	(181,892)	-	-	529,431
Health	Alcohol and Drug Abuse Programs	B.313	(20,000)	-	-	-	1,246,634	-	-	-	-	-	1,226,634
Mental Health	Mental Health	B.314	83,391	-	-	-	2,037,286	-	-	203,048	-	-	2,323,725
Mental Health	Vermont State Hospital	B.315	-	-	-	(75,000)	-	-	-	-	-	-	(75,000)
Dept. for Children & Families	Administration & Support Services	B.316	-	-	-	-	75,000	-	-	-	-	-	75,000
Dept. for Children & Families	Family Services	B.317	524,000	-	-	-	(1,553,750)	-	-	144,375	-	-	(885,375)
Dept. for Children & Families	Child Development	B.318	(202,379)	-	-	-	462,087	-	-	-	-	-	259,708
Dept. for Children & Families	Aid to Aged, Blind, and Disabled	B.320	784,800	-	-	-	-	-	-	-	-	-	784,800
Dept. for Children & Families	General Assistance	B.321	744,960	-	-	-	100,000	-	-	-	-	-	844,960
Dept. for Children & Families	Reach Up	B.323	49,745	-	-	1,450,000	-	-	-	(700,000)	2,290,176	-	3,089,921
Disabilities, Aging, & Independent Living	Administration & Support	B.329	-	-	-	-	-	-	-	-	-	50,903	50,903
Disabilities, Aging, & Independent Living	Advocacy & Independent Living	B.330	(300,000)	-	-	-	481,047	-	-	-	-	-	181,047
Disabilities, Aging, & Independent Living	Vocational Rehabilitation	B.332	-	-	-	-	-	-	-	-	(126,720)	-	(126,720)

FUNCTION / Department	Appropriation Title	2009 (Spec Sess) Act 1 Section Amended	General Fund	Transportation Fund	Education Fund	Special & Tobacco Funds	Global Commitment Fund	State Health Care Resources Fund	Catamount Fund	Federal Funds	ARRA (1) Funds	Other (2) Funds	Combined Funds
						FISCAL YEAR 2010 BUDGET RECOMMENDED ADJUSTMENT							
Disabilities, Aging, & Independent Living	Developmental Services	B.333	-	-	-	-	4,291,500	-	-	-	-	-	4,291,500
Disabilities, Aging, & Independent Living	TBI Home & Community Based Waiver	B.334	-	-	-	-	78,000	-	-	-	-	-	78,000
Corrections	Correctional Services-Out-of-State Beds	B.339	2,642,524										2,642,524
	TOTAL HUMAN SERVICES		**13,707,823**	**-**	**-**	**4,502,061**	**9,598,016**	**(2,587,084)**	**1,081,461**	**1,155,151**	**4,325,094**	**50,903**	**31,833,425**
LABOR													
Labor	Administration	B.400	-	-	-	-	-	-	-	-	(875,000)	-	(875,000)
	TOTAL LABOR		**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(875,000)**	**-**	**(875,000)**
EDUCATION													
Education	State - Placed Students	B.503	-	-	(3,300,000)	-	-	-	-	-	-	-	(3,300,000)
Education	Adjusted Education Payment	B.505	-	-	1,350,000	-	-	-	-	-	(38,575,036)	38,575,036	1,350,000
	TOTAL EDUCATION		**-**	**-**	**(1,950,000)**	**-**	**-**	**-**	**-**	**-**	**(38,575,036)**	**38,575,036**	**(1,950,000)**
NATURAL RESOURCES													
Environmental Conservation	Air and Waste Management	B.714	-	-	-	750,000	-	-	-	-	-	-	750,000
	TOTAL NATURAL RESOURSES		**-**	**-**	**-**	**750,000**	**-**	**-**	**-**	**-**	**-**	**-**	**750,000**
COMMERCE AND COMMUNITY DEVELOPMENT													
Housing and Community Affairs	Housing and Community Affairs	B.801	-	-	-	(408,700)	-	-	-	-	-	-	(408,700)
	TOTAL COMMERCE & COMMUNITY DEVELOPMENT		**-**	**-**	**-**	**(408,700)**	**-**	**-**	**-**	**-**	**-**	**-**	**(408,700)**
TRANSPORTATION													
Transportation	Program Development	B.903	-	(1,980,513)	-	-	-	-	-	336,026	-	2,574,559	930,072
Transportation	Town Highway Emergency Fund	B.918	-	520,000	-	-	-	-	-	-	-	-	520,000
	TOTAL TRANSPORTATION		**-**	**(1,460,513)**	**-**	**-**	**-**	**-**	**-**	**336,026**	**-**	**2,574,559**	**1,450,072**
DEBT SERVICE													
Debt Service	Debt Service	B.1000	(52,740)	(4,738)	-	-	-	-	-	-	-	-	(57,478)
Debt Service	Short Term Borrowing	B.1000.1	(476,792)	-	-	-	-	-	-	-	-	-	(476,792)
	TOTAL DEBT SERVICE		**(529,532)**	**(4,738)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(534,270)**
OTHER (with $$ appropriation changes)													
Secretary of Administration	Entrepreneurs' Seed Capital Fund (VEDA)	B.1101(a)(12)	2,150,000	-	-	-	-	-	-	-	(2,150,000)	-	-
Treasurer	State Employees Retirement System	B.1101(a)(13)	965,000	-	-	-	-	-	-	-		-	965,000
Military	Survivors of casualties of war on terrorism	B.1101(a)(14)	30,000	-	-	-	-	-	-	-	-	-	30,000
Secretary of Administration	VEDA - Vt Jobs Fund		-	-	-	-	-	-	-	-	-	-	-
Secretary of Administration	Economic Development for job training	B.1101(b)(2)	-	-	-	-	-	-	-	-	-	-	-
Secretary of Administration	Tourism & Marketing	B.1101(b)(3)	-	-	-	-	-	-	-	-	-	-	-
Secretary of Administration	Public Safety - State Police	B.1101(b)(4)	-	-	-	-	-	-	-	-	6,550,000	-	6,550,000
Secretary of Administration	Secretary of administration - secretary's office	B.1101(b)(5)	-	-	-	-	-	-	-	-	38,575,036	-	38,575,036
	TOTAL OTHER		**3,145,000**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**42,975,036**	**-**	**46,120,036**
	TOTAL APPROPRIATION CHANGE		**15,030,309**	**(1,465,251)**	**(1,950,000)**	**(29,394,243)**	**9,258,516**	**(2,587,084)**	**1,081,461**	**1,491,177**	**3,450,094**	**47,700,498**	**42,615,477**
FY 2010 APPROPRIATION AFTER BAA RECOMMENDATION			**1,090,375,609**	**210,376,925**	**1,313,476,522**	**250,887,441**	**965,840,917**	**152,851,462**	**28,290,062**	**1,448,762,460**	**376,054,948**	**263,084,423**	**6,100,000,769**

(1) Federal American Recovery & Reinvestment Act of 2009 (federal stimulus).

(2) Other Funds include: TIB, Fish & Wildlife, Local Match, Trust Funds, Enterprise Funds, Internal Service Funds, and Interdepartmental Transfers.

General Fund Summary
Fiscal Years 2008 - 2012
($ in Millions)

	Actual FY 2008	Actual FY 2009	Governor's Recommended Adjustment FY 2010	Governor's Recommend FY 2011	Forecast FY 2012
Sources					
Current law revenues	1,199.74	1,103.98	1,030.90	1,086.60	1,158.60
VEDA debt forgivness	-	-	(0.20)	-	-
Direct applications, transfers in & reversions	16.64	37.71	16.77	24.70	10.00
Other bills and tax changes	-	6.12	10.34	(0.41)	(16.91)
Additional property transfer tax to GF	3.15	1.30	5.52	5.90	7.08
For appropriation from GF reserve	10.87	19.13	14.85	4.96	-
Total sources	**1,230.39**	**1,168.24**	**1,078.17**	**1,121.75**	**1,158.77**
Uses					
Base appropriations, including ARRA offset	1,162.70	1,286.23	1,264.70	1,220.24	1,151.82
Budget adjustment and rescission(s)	12.08	(27.31)	2.10	-	-
	1,174.78	1,258.92	1,266.80	1,220.24	1,151.82
Percent increase/(decrease)	4.44%	7.16%	0.63%	-3.68%	-5.61%
Less Base ARRA funding	-	(76.33)	(192.27)	(113.29)	-
Base Appropriation Net of ARRA	1,174.78	1,182.59	1,074.53	1,106.95	1,151.82
Budget adjustment - one time	6.14	(42.65)	-	-	-
Other Bills	0.10	1.82	2.56	-	-
One-time appropriations	12.46	2.23	13.28	11.55	-
One-time waterfall and other adjustments	6.79	2.30	-	-	-
Total uses	**1,200.27**	**1,146.29**	**1,090.38**	**1,118.50**	**1,151.82**
Subtotal operating surplus (deficit)	**30.12**	**21.95**	**(12.21)**	**3.25**	**6.95**
Allocation of surplus - Transfers (to) /from other funds					
Transportation fund	-	-	1.71	-	-
Education fund	4.70	(0.67)	-	-	-
Tobacco settlement fund	-	3.65	-	-	-
Reserve for bond issuance premium	-	-	1.18	-	-
Catamount fund	(3.50)	-	-	-	-
Next generation fund	-	(7.29)	(3.29)	(4.79)	(4.79)
Human services caseload reserve	-	0.96	16.22	-	-
Federal funds (Part "D" refund)	(0.26)	-	-	-	-
Internal service funds and assorted funds	(8.51)	0.78	(1.34)	(1.25)	(0.75)
Total transfers (to) / from other funds	(7.57)	(2.58)	14.47	(6.04)	(5.54)
Reserved in GF (designated)					
Budget Stabilization Reserve	(2.62)	(2.17)	2.70	2.80	(1.41)
Reserved in GF Surplus/Other Reserve	(19.93)	(17.20)	(4.96)	-	-
Total reserved in the GF (designated)	(22.55)	(19.37)	(2.26)	2.80	(1.41)
Total allocated	**(30.12)**	**(21.95)**	**12.21**	**(3.25)**	**(6.95)**
Unallocated operating surplus (deficit)	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Stabilization Reserve 5% statutory level	**57.84**	**60.01**	**57.31**	**54.52**	**55.93**
GF Reserves (cumulative)					
Budget Stabilization Reserve	57.84	60.01	57.31	54.52	55.93
Human Services Caseload Reserve	17.24	16.29	0.07	0.07	0.07
Bond Premium/Other Short Term Reserves	0.95	1.18	-	-	-
Reserved in GF Surplus Reserve	18.98	14.84	4.96	-	-
Total GF Reserve Balance	**95.01**	**92.32**	**62.34**	**54.58**	**55.99**

* Results may not add due to rounding.

Transportation Fund Summary
Fiscal Years 2008 - 2012
($ in Millions)

	Actual FY 2008	Actual FY 2009	Governor's Recommended Adjustment FY 2010	Governor's Recommend FY 2011	Forecast FY 2012
Sources					
Current law revenues	223.08	203.69	212.20	218.00	226.60
Proposed fee bill and new revenue	-	0.67	-	(0.07)	(0.07)
Direct applications & reversions	4.80	-	-	-	-
For appropropriation from TF Reserve	3.22	0.63	-	-	-
Total sources	**231.10**	**204.99**	**212.20**	**217.93**	**226.53**
Uses					
Base appropriations	228.95	198.50	211.74	215.81	224.43
Budget adjustments and rescissions	-	7.17	(1.47)	-	-
One-time approps from prior year	-	-	-	-	-
Total uses	**228.95**	**205.67**	**210.28**	**215.81**	**224.43**
Subtotal operating surplus (deficit)	**2.15**	**(0.68)**	**1.92**	**2.12**	**2.10**
Allocation of surplus					
Transfers (to) / from other funds					
General Fund	-	-	(1.71)	-	-
Downtown Fund	(0.73)	(0.40)	(0.40)	(0.40)	(0.40)
Central Garage Fund	0.10	1.49	(1.12)	(1.12)	(1.12)
VT Recreational Trail Fund	(0.37)	(0.37)	(0.37)	(0.37)	(0.37)
Other Funds	-	0.73	-	-	-
Total transfers (to) / from other funds	(1.00)	1.44	(3.60)	(1.89)	(1.89)
Reserved in the TF (designated)					
Budget Stabilization Reserve	(0.53)	(0.09)	1.01	(0.23)	(0.28)
Bond Reserve	-	(0.67)	0.67	-	
Reserved in TF Surplus Reserve	(0.62)	-	-	-	-
Total reserved in the TF (designated)	(1.15)	(0.76)	1.68	(0.23)	(0.28)
Total allocated	**(2.15)**	**0.68**	**(1.92)**	**(2.12)**	**(2.17)**
Unallocated operating surplus(deficit)	-	-	-	-	-
Stabilization Reserve up to 5% Statutory Level	**11.20**	**11.29**	**10.28**	**10.51**	**10.79**
TF Reserves (cumulative)					
Bond Reserve	-	0.67	-	-	-
Budget Stabilization Reserve	11.20	11.29	10.28	10.51	10.79
Reserved in TF Surplus Reserve	0.62	-	-	-	-
Total TF Reserve Balance	**11.82**	**11.96**	**10.28**	**10.51**	**10.79**

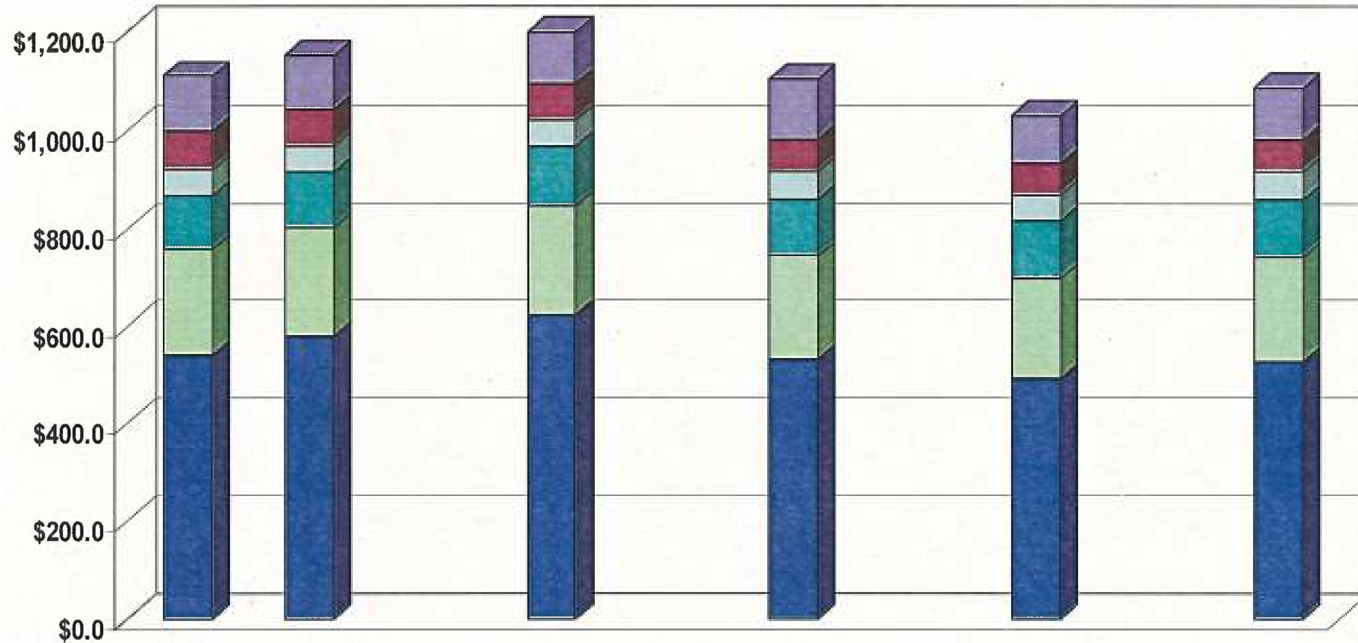
Results may not add due to rounding.

Education Fund Summary
Fiscal Years 2008 - 2011
($ in Millions)

	Actual FY 2008	Actual FY 2009	Governor's Recommended Adjustment FY 2010	Governor's Proposed FY 2011
Sources				
Current law revenues	28.29	24.00	24.43	25.13
Sales & use tax	112.80	107.05	103.20	107.00
Lottery revenue	22.71	20.95	20.40	21.00
Non-residential tax	477.48	524.10	558.19	548.83
Homestead Tax	321.43	352.71	347.91	380.24
General fund appropriations	280.20	291.13	240.80	240.80
Medicaid reimbursement	6.45	-	-	-
Direct applications/reversions	-	-	-	-
Interest on fund balance	(1.31)	0.26	0.10	0.20
Total sources	**1,248.05**	**1,320.20**	**1,295.03**	**1,323.20**
Uses				
Base appropriations [1]	1,259.24	1,321.29	1,313.47	1,334.10
Appropriation savings	(3.39)	(2.02)	-	(11.27)
Total uses	**1,255.85**	**1,319.27**	**1,313.47**	**1,322.83**
Subtotal operating surplus (deficit)	**(7.80)**	**0.93**	**(18.44)**	**0.36**
Allocation of surplus/(deficit)				
Transfer to/(from) the stabilization reserve	1.15	1.69	(8.32)	0.36
Transfer to/(from) continuing appropriations	1.33	(1.57)	(3.49)	-
Transfer to/(from) unallocated	(10.28)	0.82	(6.64)	-
Total allocated	**(7.80)**	**0.93**	**(18.44)**	**0.36**
Education fund reserves				
Budget stabilization reserve	**29.39**	**31.08**	**22.76**	**23.13**
Minimum statutory reserve at 3.5%	**20.57**	**21.76**	**20.81**	**20.73**
Maximum statutory reserve at 5%	**29.39**	**31.08**	**29.73**	**29.61**

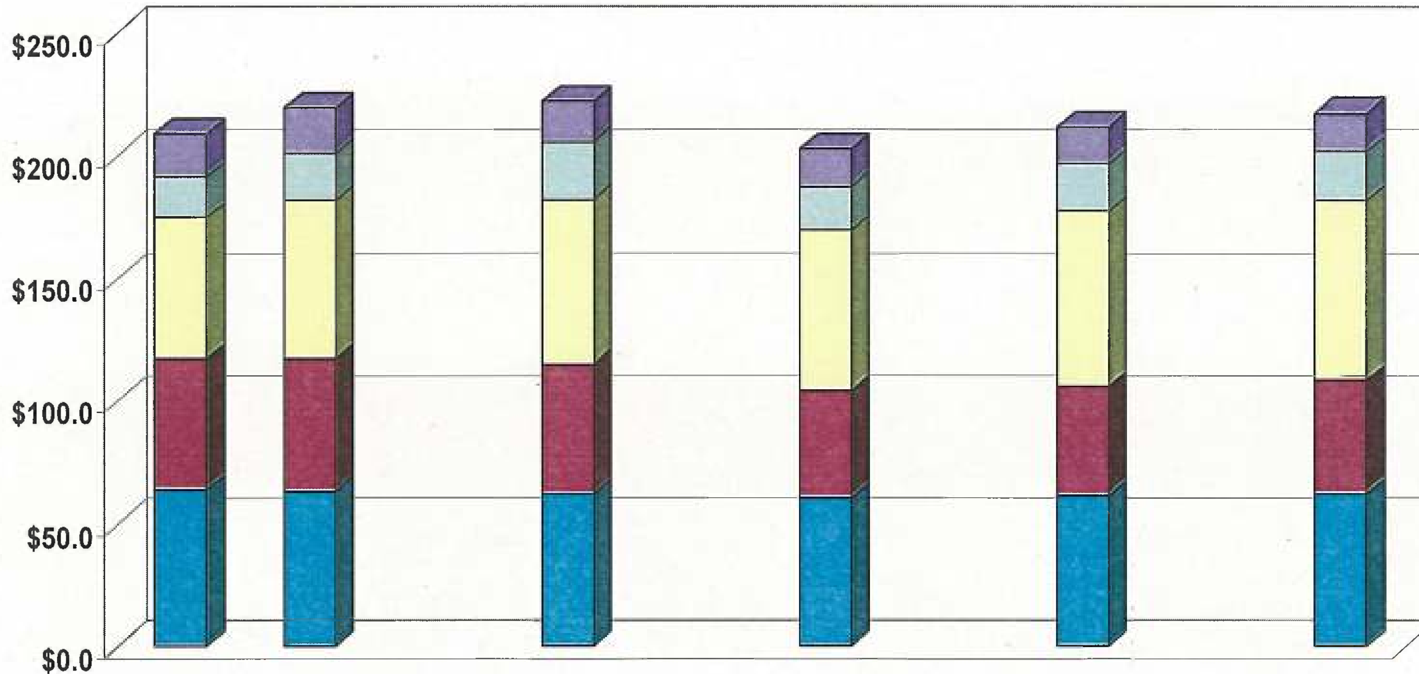
*Results may not add due to rounding.

General Fund Revenue by Component
FY 2006 to FY 2011



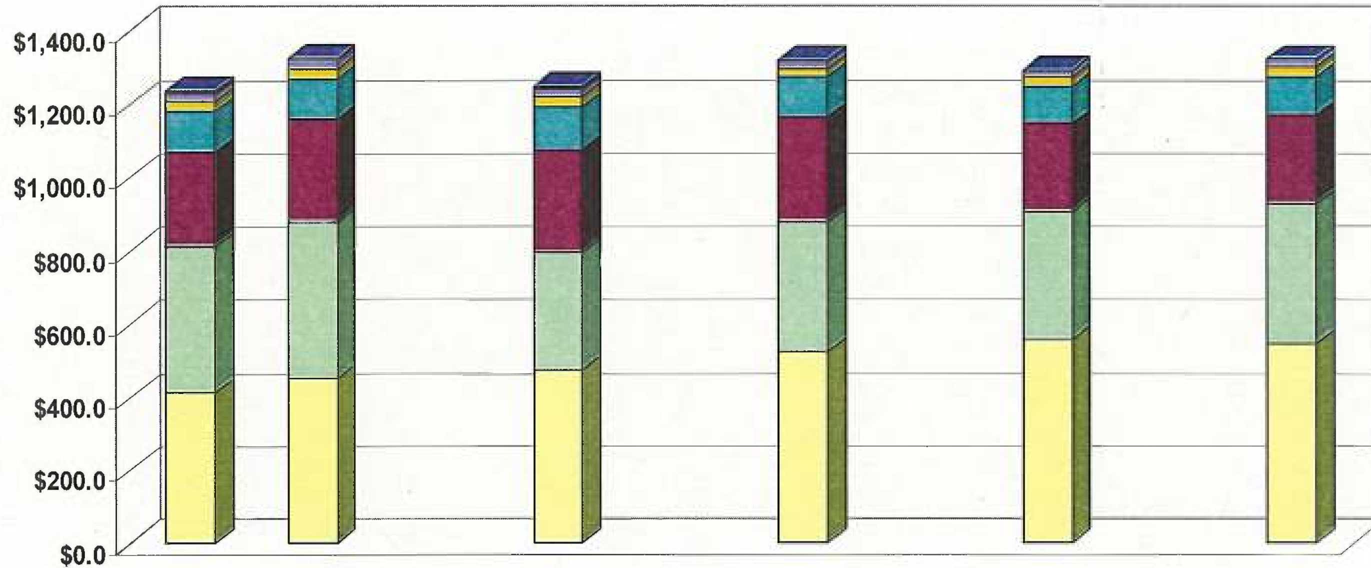
($ in Millions)	FY 2006 Actual	FY 2007 Actual	% Change 2006-2007	FY 2008 Actual	% Change 2007 - 2008	FY 2009 Actual	% Change 2008 - 2009	FY 2010 Projected	% Change 20090-2010	FY 2011 Projected	% Change 2010 - 2011
Other	$ 112.8	$ 107.1	-5.0%	$ 101.3	-5.4%	$ 122.6	21.0%	$ 97.8	-20.2%	$ 103.3	5.6%
Corporate	$ 75.9	$ 72.8	-4.0%	$ 74.6	2.4%	$ 66.2	-11.3%	$ 63.1	-4.6%	$ 65.7	4.1%
Insurance	$ 52.5	$ 52.9	0.7%	$ 54.9	3.9%	$ 53.7	-2.1%	$ 55.2	2.8%	$ 56.7	2.7%
Meals and Rooms	$ 111.8	$ 114.9	2.8%	$ 121.1	5.4%	$ 117.1	-3.3%	$ 116.4	-0.6%	$ 120.1	3.2%
Sales and Use Taxes	$ 216.9	$ 222.5	2.6%	$ 225.6	1.4%	$ 214.1	-5.1%	$ 206.4	-3.6%	$ 214.0	3.7%
Personal Income Tax	$ 542.0	$ 581.2	7.2%	$ 622.3	7.1%	$ 530.3	-14.8%	$ 492.0	-7.2%	$ 526.8	7.1%
Total	$ 1,111.9	$ 1,151.4	3.5%	$ 1,199.8	4.2%	$ 1,104.0	-8.0%	$ 1,030.9	-6.6%	$ 1,086.6	5.4%

Transportation Fund Revenue by Component
FY 2006 to FY 2011



($ in Millions)	FY 2006 Actual	FY 2007 Actual	% Change 2006-2007	FY 2008 Actual	% Change 2007 - 2008	FY 2009 Actual	% Change 2008 - 2009	FY 2010 Projected	% Change 2009-2010	FY 2011 Projected	% Change 2010 - 2011
Diesel Fuel Tax	$ 17.7	$ 18.0	1.6%	$ 16.6	-7.8%	$ 15.5	-6.6%	$ 15.0	-3.2%	$ 15.6	4.0%
Other Revenues	$ 17.1	$ 19.2	12.2%	$ 23.7	23.3%	$ 18.0	-24.0%	$ 19.1	6.1%	$ 19.8	3.7%
Motor Vehicle Fees	$ 57.4	$ 65.4	14.0%	$ 67.5	3.2%	$ 65.5	-3.0%	$ 72.1	10.1%	$ 74.0	2.6%
Purchase & Use Tax	$ 53.9	$ 53.8	-0.3%	$ 52.7	-2.0%	$ 44.0	-16.5%	$ 44.7	1.6%	$ 46.3	3.6%
Gasoline Tax	$ 63.8	$ 63.6	-0.3%	$ 62.6	-1.6%	$ 60.6	-3.2%	$ 61.3	1.2%	$ 62.3	1.6%
Total	$ 209.9	$ 220.0	4.8%	$ 223.1	1.4%	$ 203.6	-8.7%	$ 212.2	4.2%	$ 218.0	2.7%

Education Fund Revenue by Component
FY 2006 to FY 2011



($ in Millions)	FY 2006 Actual	FY 2007 Actual	% Change 2006-2007	FY 2008 Actual	% Change 2007 - 2008	FY 2009 Actual	% Change 2008 - 2009	FY 2010 Projected	% Change 20090-2010	FY 2011 Projected	% Change 2010 - 2011
Other	$ 6.6	$ 4.3	-34.9%	$ 5.2	20.0%	$ 0.9	-82.0%	$ 0.1	-85.7%	$ 0.2	80.5%
Lottery Revenue	$ 22.8	$ 23.3	2.2%	$ 22.7	-2.6%	$ 21.0	-7.7%	$ 20.4	-2.6%	$ 21.0	2.9%
Current Law Revenue	$ 28.8	$ 28.8	0.0%	$ 28.3	-1.8%	$ 24.0	-15.2%	$ 24.4	1.8%	$ 25.1	2.9%
Sales & Use Tax	$ 108.5	$ 111.2	2.5%	$ 112.8	1.4%	$ 107.1	-5.1%	$ 103.2	-3.6%	$ 107.0	3.7%
General Fund Approp.	$ 259.3	$ 282.4	8.9%	$ 280.2	-0.8%	$ 291.1	3.9%	$ 240.8	-17.3%	$ 240.8	0.0%
Homestead Tax	$ 394.5	$ 422.5	7.1%	$ 321.4	-23.9%	$ 352.7	9.7%	$ 347.9	-1.4%	$ 380.2	9.3%
Non-Residential Tax	$ 418.1	$ 455.1	8.9%	$ 477.5	4.9%	$ 524.1	9.8%	$ 558.2	6.5%	$ 548.8	-1.7%
Total	$ 1,238.6	$1,327.6	7.2%	$ 1,248.1	-6.0%	$ 1,320.9	5.8%	$ 1,295.1	-2.0%	$ 1,323.2	2.2%

STATE OF VERMONT - FY 2010 APPROPRIATIONS - BUDGET ADJUSTMENT RECOMMENDATIONS

Funding Sources	FY 2009 Final Appropriation	FY 2010 Governor's BAA Recommend [d]	% Change Prior Year	All General Government: General Government	All General Government: Property Tax Assistance [e]	Protection to Persons & Property	Total Human Services: Corrections	Total Human Services: Non-Medicaid	Total Human Services: Medicaid/LTC Federal & State Only
General Fund (GF)	1,146,278,770	1,090,375,609	-4.88%	38,730,484	27,076,058	88,086,583	127,781,678	146,325,834	167,522,111
Transportation Fund	212,845,156	210,376,925	-1.16%	-	-	28,352,807	-	-	-
Education Fund (EF)	1,321,957,273	1,313,476,522	-0.64%	-	9,403,687	-	-	-	-
Fish & Wildlife	15,426,252	16,355,474	6.02%	-	-	-	-	-	-
Special Funds [b]	436,307,790	447,169,342	2.49%	8,777,196	-	69,746,412	1,732,283	58,310,888	223,939,098
Sub-Total	3,132,815,241	3,077,753,872	-1.76%	47,507,680	36,479,745	186,185,802	129,513,961	204,636,722	391,461,209
Adjust for inter-fund appropriation:								-	
GF Transfer to EF	(291,127,800)	(240,803,944)	-17.29%	-					
Total State Funds after EF Transfer	2,841,687,441	2,836,949,928	-0.17%	47,507,680	36,479,745	186,185,802	129,513,961	204,636,722	391,461,209
percent of total	63.99%	59.95%		1.67%	1.29%	6.56%	4.57%	7.21%	13.80%
Federal Funds	1,354,779,066	1,448,762,460	6.94%	841,770	-	46,284,751	584,861	217,423,178	762,448,160
Federal ARRA Funds [c]	178,344,712	376,054,948	110.86%	-		35,451,349	-	30,672,439	135,882,723
Total Funds Before Dedicated Dollars	**4,374,811,219**	**4,661,767,336**	6.56%	**48,349,450**	**36,479,745**	**267,921,902**	**130,098,822**	**452,732,339**	**1,289,792,092**
percent of total	98.51%	98.52%		1.04%	0.78%	5.75%	2.79%	9.71%	27.67%
Dedicated Sources									
Local Match	2,553,311	2,993,800	17.25%	-	-	-	-	-	-
Enterprise Funds	8,254,019	8,669,664	5.04%	3,016,105	-	4,802,581	-	-	-
Pension Trust & Private Purpose Trust Funds	55,251,374	58,583,801	6.03%	31,002,159	-	-	-	10,000	-
Sub-Total	66,058,704	70,247,265	6.34%	34,018,264	-	4,802,581	-	10,000	-
Total Funds and Dedicated Sources	**4,440,869,923**	**4,732,014,601**	6.56%	**82,367,714**	**36,479,745**	**272,724,483**	**130,098,822**	**452,742,339**	**1,289,792,092**
	100.00%	100.00%		1.74%	0.77%	5.76%	2.75%	9.57%	27.26%
Funds Sources that are duplicated in the above appropriations:									
Internal Service Funds	66,118,435	70,929,433	7.28%	52,448,828	-	-	1,632,530	-	-
Interdepartmental Transfer	32,670,160	45,286,838	38.62%	5,933,570	-	9,663,948	3,490,225	13,813,867	362,654
Interdepartmental Transfer - ARRA	-	45,125,036	0.00%	-	-	6,550,000	-	-	-
Global Commitment Fund	900,965,265	965,840,917	7.20%	188,393	-	1,898,824	3,094,144	-	955,215,673
Total	999,753,860	1,127,182,224	12.75%	58,570,791	-	18,112,772	8,216,899	13,813,867	955,578,327
Memo: Total All Appropriations	5,731,751,583	6,100,000,769	6.42%	140,938,505	36,479,745	290,837,255	138,315,721	466,556,206	2,245,370,419

NOTES (this page):

(a) 2009 Special Session Act 1, plus other 2009 session and 2009 special session Acts.

(b) Special Funds include Tobacco Fund, Catamount Fund, State Health Care Resources, Next Generation Fund, and Transportation Infrastructure Bond Fund.

(c) American Recovery & Reinvestment Act of 2009 (federal stimulus bill).

(d) Governor's FY 2010 Recommended Budget Adjustments, submitted to the General Assembly on January 19, 2010.

(e) Includes Homeowner rebate; Renter rebate; reappraisal and listing payments; and municipal current use.

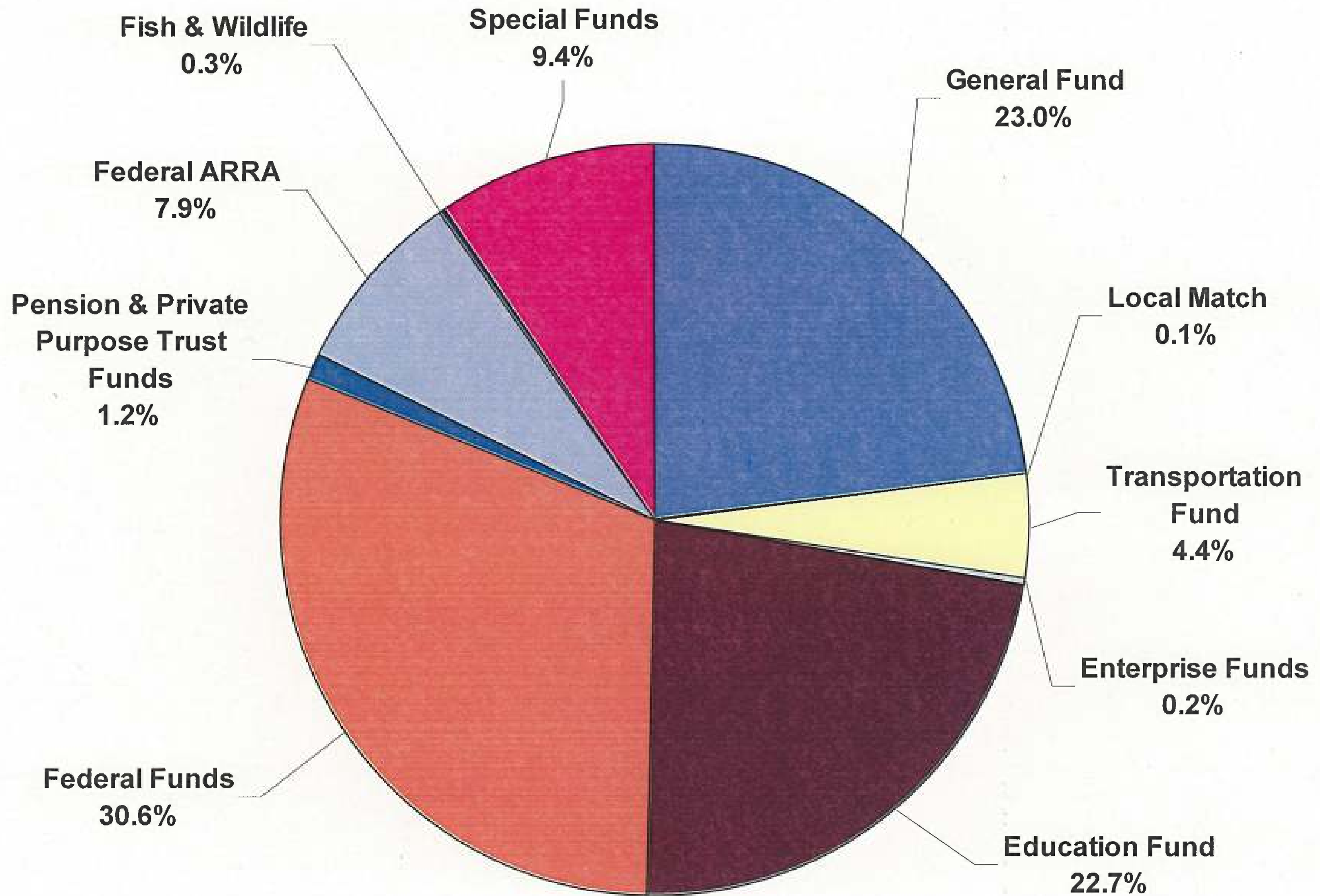
STATE OF VERMONT - FY 2010 APPROPRIATIONS - BUDGET ADJUSTMENT RECOMMENDATIONS

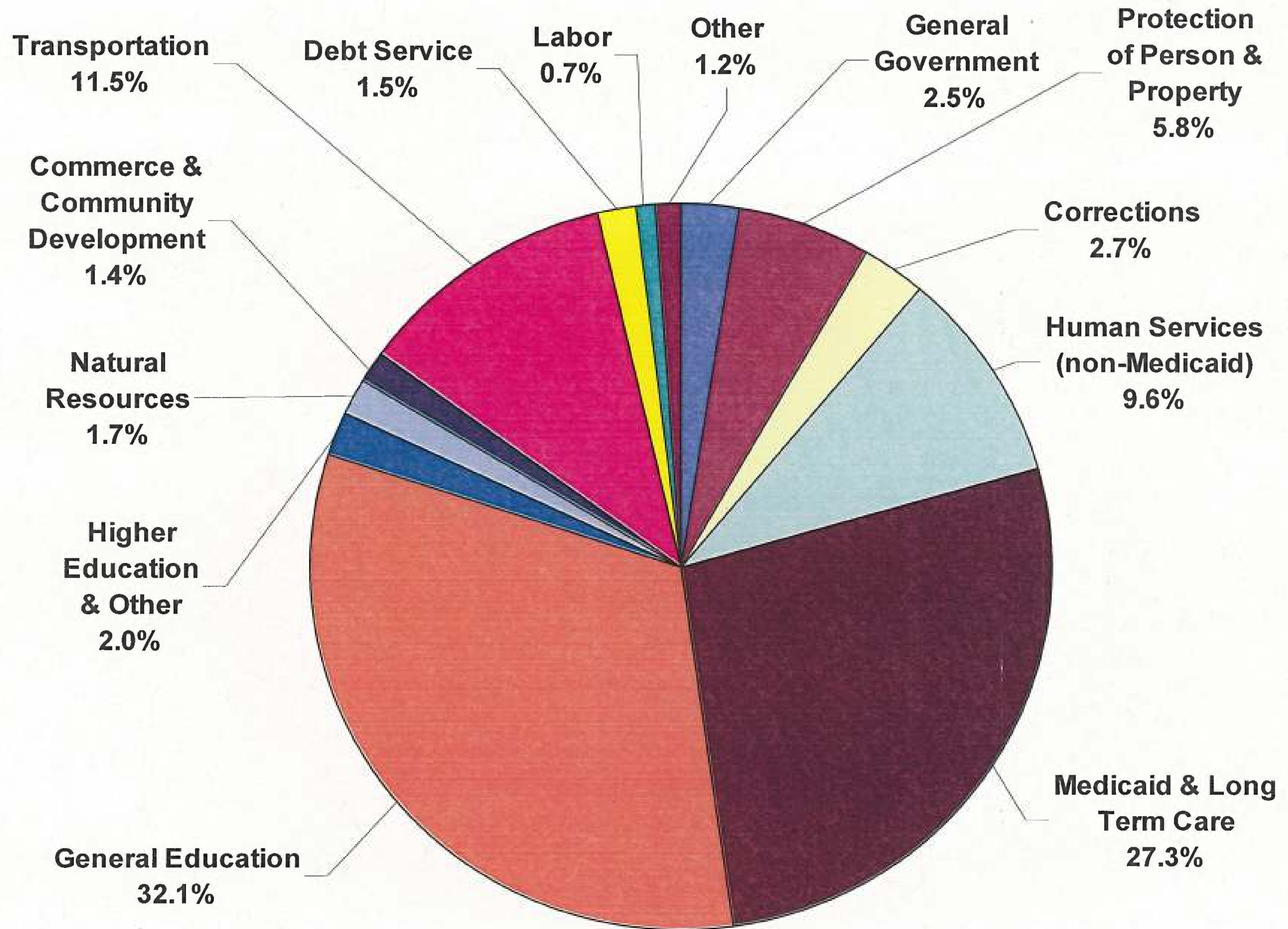
Funding Sources	Labor	General Education	Higher Education & Other	Natural Resources	Commerce & Community Development	Transportation	Debt Service	Other
General Fund (GF)	2,494,633	289,851,627	91,550,748	21,104,000	14,720,095	-	65,391,180	9,740,578
Transportation Fund	-	-	-	-	-	178,418,341	3,555,777	50,000
Education Fund (EF)	-	1,304,072,835	-	-	-	-	-	-
Fish & Wildlife	-	-	-	16,355,474	-	-	-	-
Special Funds [b]	3,637,300	17,321,479	3,293,000	28,753,682	12,474,912	15,140,377	2,499,715	1,543,000
Sub-Total	6,131,933	1,611,245,941	94,843,748	66,213,156	27,195,007	193,558,718	71,446,672	11,333,578
Adjust for inter-fund appropriation:								
GF Transfer to EF		(240,803,944)						
Total State Funds after EF Transfer	6,131,933	1,370,441,997	94,843,748	66,213,156	27,195,007	193,558,718	71,446,672	11,333,578
percent of total	0.22%	48.31%	3.34%	2.33%	0.96%	6.82%	2.52%	0.40%
Federal Funds	21,198,676	121,738,245	-	14,715,898	35,348,231	228,178,690	-	-
Federal ARRA Funds [c]	7,793,753	-			1,982,000	117,197,648	-	47,075,036
Total Funds Before Dedicated Dollars	**35,124,362**	**1,492,180,242**	**94,843,748**	**80,929,054**	**64,525,238**	**538,935,056**	**71,446,672**	**58,408,614**
percent of total	0.75%	32.01%	2.03%	1.74%	1.38%	11.56%	1.53%	1.25%
Dedicated Sources								
Local Match	-	-	-	-	-	2,993,800	-	-
Enterprise Funds	-	-	-	-	850,978	-	-	-
Pension Trust & Private Purpose Trust Funds	-	27,571,642	-	-	-	-	-	-
Sub-Total	-	27,571,642	-	-	850,978	2,993,800	-	-
Total Funds and Dedicated Sources	**35,124,362**	**1,519,751,884**	**94,843,748**	**80,929,054**	**65,376,216**	**541,928,856**	**71,446,672**	**58,408,614**
	0.74%	32.12%	2.00%	1.71%	1.38%	11.45%	1.51%	1.23%
Funds Sources that are duplicated in the above appropriations:								
Internal Service Funds	-	-	-	-	-	16,848,075	-	-
Interdepartmental Transfer	2,403,838	30,466	-	2,178,179	158,998	7,251,093	-	-
Interdepartmental Transfer - ARRA	-	38,575,036	-	-	-	-	-	-
Global Commitment Fund	-	1,032,320	4,411,563	-	-	-	-	-
Total	2,403,838	39,637,822	4,411,563	2,178,179	158,998	24,099,168	-	-
Memo: Total All Appropriations	37,528,200	1,800,193,650	99,255,311	83,107,233	65,535,214	566,028,024	71,446,672	58,408,614

NOTES (this page):

(b) Special Funds include Tobacco Fund, Catamount Fund, State Health Care Resources, Next generation Fund, and Transportation Infrastructure Bond Fund.

(c) American Recovery & Reinvestment Act of 2009 (federal stimulus bill).


FY 2010 ADJUSTED BUDGET ALL FUNDING SOURCES - by FUND
Total $4,732,014,601
Fish & Wildlife
0.3%
Special Funds
9.4%
General Fund
23.0%
Federal ARRA
7.9%
Local Match
0.1%
Pension & Private
Purpose Trust
Funds
1.2%
Transportation
Fund
4.4%
Enterprise Funds
0.2%
Federal Funds
30.6%
Education Fund
22.7%


FY 2010 ADJUSTED BUDGET ALL FUNDING SOURCES - by FUNCTION
Total $4,732,014,601
Transportation 11.5%
Debt Service 1.5%
Labor 0.7%
Other 1.2%
General Government 2.5%
Protection of Person & Property 5.8%
Commerce & Community Development 1.4%
Corrections 2.7%
Human Services (non-Medicaid) 9.6%
Natural Resources 1.7%
Higher Education & Other 2.0%
Medicaid & Long Term Care 27.3%
General Education 32.1%

STATE OF VERMONT - FY 2011 APPROPRIATIONS - GOVERNOR'S BUDGET RECOMMENDATIONS

Funding Sources	FY 2010 Governor's BAA Recommend [c]	FY 2011 Governor's Recommend [d]	% Change Prior Year	All General Government: General Government	All General Government: Property Tax Assistance [e]	Protection to Persons & Property	Total Human Services: Corrections	Total Human Services: Non-Medicaid	Total Human Services: Medicaid/LTC Federal & State Only
General Fund (GF)	1,090,375,609	1,118,501,932	2.58%	40,774,787	32,516,653	104,903,583	133,396,480	142,687,027	229,540,533
Transportation Fund	210,376,925	215,809,557	2.58%	-	-	24,852,807	-	-	-
Education Fund (EF)	1,313,476,522	1,322,833,018	0.71%	-	12,762,715	-	-	-	-
Fish & Wildlife	16,355,474	17,113,525	4.63%		-	-	-	-	-
Special Funds [a]	447,169,342	455,988,967	1.97%	9,456,078	-	69,188,974	1,961,322	59,827,874	232,324,554
Sub-Total	3,077,753,872	3,130,246,999	1.71%	50,230,865	45,279,368	198,945,364	135,357,802	202,514,901	461,865,087
Adjust for inter-fund appropriation:									
GF Transfer to EF	(240,803,944)	(240,803,945)	0.00%	-	-	-	-	-	-
Total State Funds after EF Transfe	2,836,949,928	2,889,443,054	1.85%	50,230,865	45,279,368	198,945,364	135,357,802	202,514,901	461,865,087
percent of total	59.95%	60.63%		1.74%	1.57%	6.89%	4.68%	7.01%	15.98%
Federal Funds	1,448,762,460	1,547,314,639	6.80%	955,372	-	57,153,489	170,962	233,377,045	774,650,820
Federal ARRA Funds [b]	376,054,948	251,941,482	-33.00%	-		18,539,819	-	16,346,132	69,668,502
Total Funds Before Dedicated Doll	**4,661,767,336**	**4,688,699,175**	0.58%	**51,186,237**	**45,279,368**	**274,638,672**	**135,528,764**	**452,238,078**	**1,306,184,409**
percent of total	98.52%	98.39%		1.09%	0.97%	5.86%	2.89%	9.65%	27.86%
Dedicated Sources									
Local Match	2,993,800	2,193,885	-26.72%	-	-	-	-	-	-
Enterprise Funds	8,669,664	8,677,624	0.09%	2,891,578	-	4,972,629	-	-	-
Pension Trust & Private Purpose Trust Funds	58,583,801	65,916,620	12.52%	37,673,233	-	-	-	10,000	-
Sub-Total	70,247,265	76,788,129	9.31%	40,564,811	-	4,972,629	-	10,000	-
Total Funds and Dedicated Source	**4,732,014,601**	**4,765,487,304**	0.71%	**91,751,048**	**45,279,368**	**279,611,301**	**135,528,764**	**452,248,078**	**1,306,184,409**
	100.00%	100.00%		1.93%	0.95%	5.87%	2.84%	9.49%	27.41%
Funds Sources that are duplicated in the above									
Internal Service Funds	70,929,433	70,655,901	-0.39%	51,637,680	-	-	1,540,358	-	-
Interdepartmental Transfer	45,286,838	41,994,828	-7.27%	5,991,990	-	8,833,753	4,056,444	13,746,487	357,667
Interdepartmental Transfer - ARRA	45,125,036	38,575,036	-14.52%	-	-	-		-	-
Global Commitment Fund	965,840,917	1,038,660,106	7.54%	195,053	-	1,898,824	3,094,144	-	1,028,007,430
Total	1,127,182,224	1,189,885,871	5.56%	57,824,723	-	10,732,577	8,690,946	13,746,487	1,028,365,097
Memo: Total All Appropriations	6,100,000,769	6,196,177,120	1.58%	149,575,771	45,279,368	290,343,878	144,219,710	465,994,565	2,334,549,506

NOTES (this page):

(a) Special Funds include Tobacco Fund, Catamount Fund, State Health Care Resources, Next Generation Fund, and Transportation Infrastructure Bond (TIB) Fund.

(b) American Recovery & Reinvestment Act of 2009 (federal stimulus bill).

(c) Governor's FY 2010 Recommended Budget Adjustments, presented to the General Assembly on January 19, 2010.

(d) Governor's FY 2011 Recommended Budget, presented to the General Assembly on January 19, 2010.

(e) Includes Homeowner rebate; Renter rebate; reappraisal and listing payments; and municipal current use.

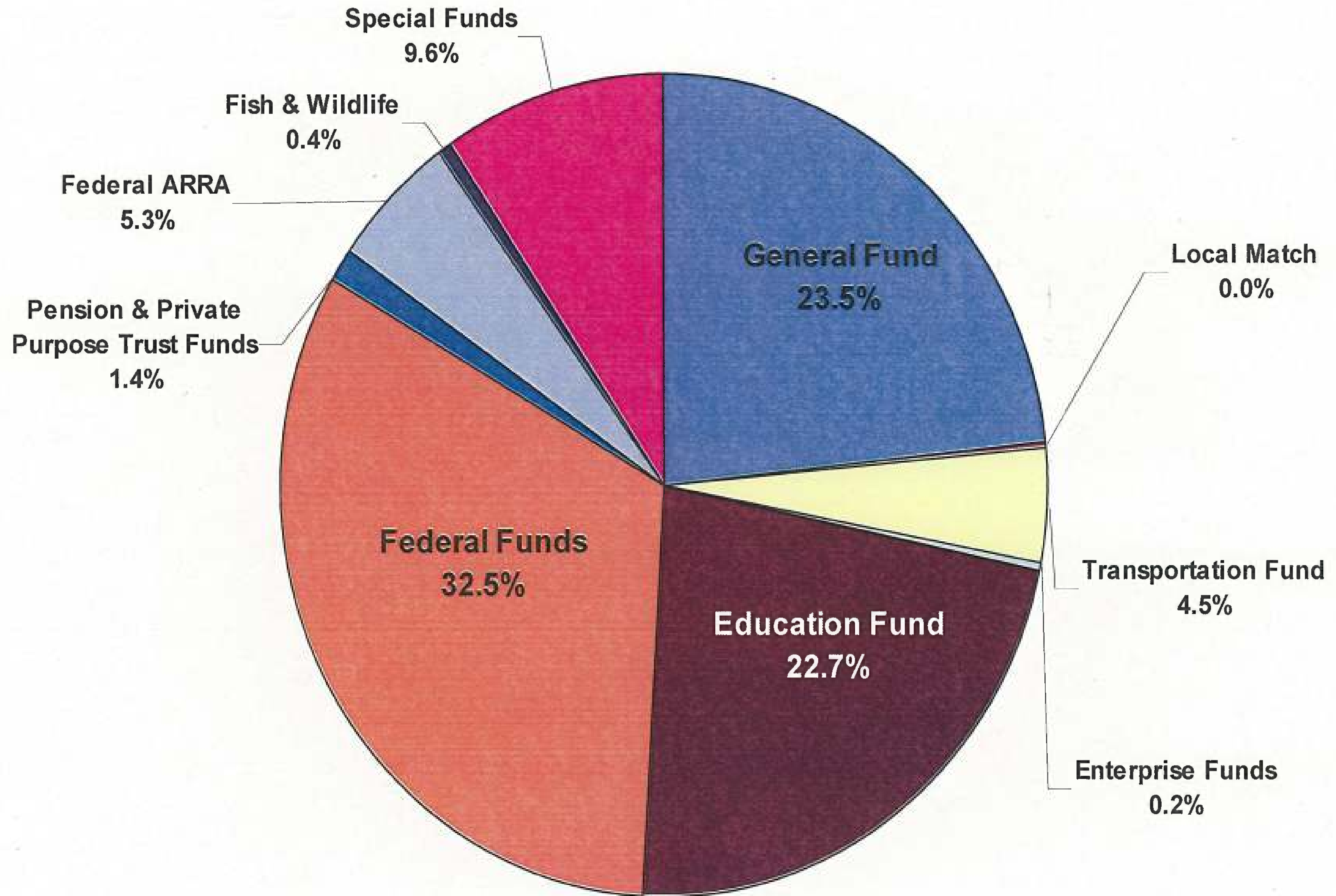
STATE OF VERMONT - FY 2011 APPROPRIATIONS - GOVERNOR'S BUDGET RECOMMENDATIONS

Funding Sources	Labor	General Education	Higher Education & Other	Natural Resources	Commerce & Community Development	Transportation	Debt Service	Other
General Fund (GF)	2,561,430	301,249,932	85,895,267	20,207,475	13,704,312	-	67,372,470	(56,308,017)
Transportation Fund	-	-	-	-	-	185,185,770	3,482,640	2,288,340
Education Fund (EF)	-	1,321,340,303	-	-	-	-	-	(11,270,000)
Fish & Wildlife	-	-	-	17,113,525	-	-	-	-
Special Funds [a]	3,765,862	16,728,905	4,793,000	29,196,488	11,163,919	16,555,766	1,026,225	-
Sub-Total	6,327,292	1,639,319,140	90,688,267	66,517,488	24,868,231	201,741,536	71,881,335	(65,289,677)
Adjust for inter-fund appropriation:								
GF Transfer to EF		(240,803,945)						
Total State Funds after EF Transfer	6,327,292	1,398,515,195	90,688,267	66,517,488	24,868,231	201,741,536	71,881,335	(65,289,677)
percent of total	0.22%	48.40%	3.14%	2.30%	0.86%	6.98%	2.49%	-2.26%
Federal Funds	23,172,655	128,720,522	-	14,659,151	39,026,536	275,428,087	-	-
Federal ARRA Funds [b]	4,571,772	46,719,169		1,467,187	1,529,195	54,524,670	-	38,575,036
Total Funds Before Dedicated Dollars	**34,071,719**	**1,573,954,886**	**90,688,267**	**82,643,826**	**65,423,962**	**531,694,293**	**71,881,335**	**(26,714,641)**
percent of total	0.73%	33.57%	1.93%	1.76%	1.40%	11.34%	1.53%	-0.57%
Dedicated Sources								
Local Match	-	-	-	-	-	2,193,885	-	-
Enterprise Funds	-	-	-	-	813,417	-	-	-
Pension Trust & Private Purpose Trust Funds	-	28,233,387	-	-	-	-	-	-
Sub-Total	-	28,233,387	-	-	813,417	2,193,885	-	-
Total Funds and Dedicated Sources	**34,071,719**	**1,602,188,273**	**90,688,267**	**82,643,826**	**66,237,379**	**533,888,178**	**71,881,335**	**(26,714,641)**
	0.71%	33.62%	1.90%	1.73%	1.39%	11.20%	1.51%	-0.56%
Funds Sources that are duplicated in the above appropriations:								
Internal Service Funds	-	-	-	-	-	17,477,863	-	-
Interdepartmental Transfer	1,500,001	29,561	-	2,853,275	635,670	3,989,980	-	-
Interdepartmental Transfer - ARRA	-	38,575,036	-	-	-	-	-	-
Global Commitment Fund	-	1,053,092	4,411,563	-	-	-	-	-
Total	1,500,001	39,657,689	4,411,563	2,853,275	635,670	21,467,843	-	-
Memo: Total All Appropriations	35,571,720	1,882,649,907	95,099,830	85,497,101	66,873,049	555,356,021	71,881,335	(26,714,641)

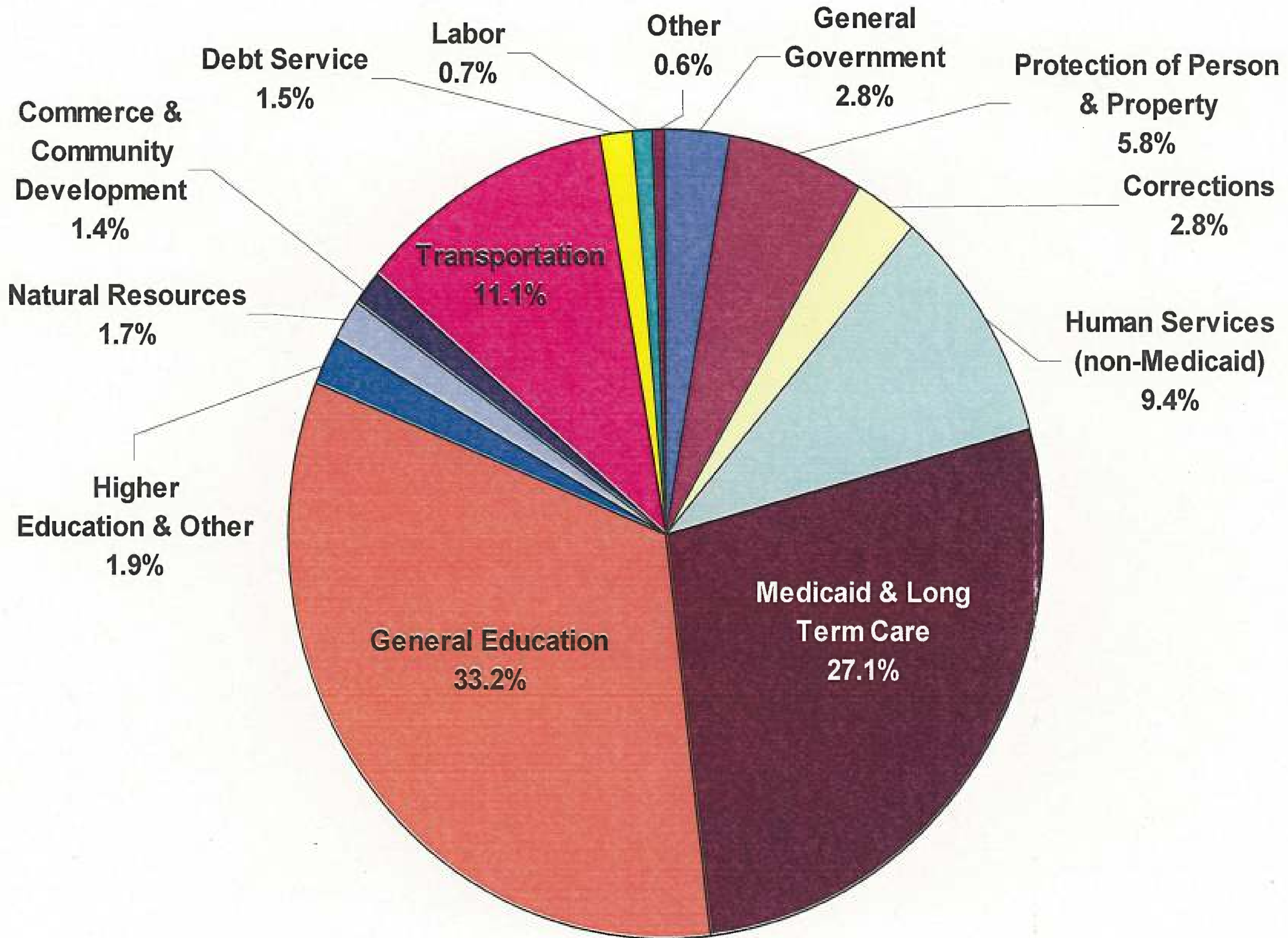
NOTES (this page):

(a) Special Funds include Tobacco Fund, Catamount Fund, State Health Care Resources, Next Generation Fund, and Transportation Infrastructure Bond Fund.

(b) American Recovery & Reinvestment Act of 2009 (federal stimulus bill).


FY 2011 ADJUSTED BUDGET ALL FUNDING SOURCES - by FUND
$4,765,487,304
Special Funds
9.6%
Fish & Wildlife
0.4%
Federal ARRA
5.3%
Pension & Private
Purpose Trust Funds
1.4%
General Fund
23.5%
Local Match
0.0%
Federal Funds
32.5%
Transportation Fund
4.5%
Education Fund
22.7%
Enterprise Funds
0.2%

FY 2011 ADJUSTED BUDGET ALL FUNDING SOURCES - by FUNCTION
$4,765,487,304



TOTAL APPROPRIATION HISTORY FY 2007 - FY 2011 (All Funds)

Funding Sources	FY 2007 Final Appropriation	FY 2008 Final Appropriation	FY 2009 Final Appropriation	FY 2010 Recommended Adjustment [a]	FY 2011 Governor's Recommend [b]	% Change FY 2011 vs. FY 2010
General Fund (GF)	1,159,981,529	1,200,271,408	1,146,278,770	1,090,375,609	1,118,501,932	2.58%
Transportation Fund	223,986,116	228,952,078	212,845,156	210,376,925	215,809,557	2.58%
Education Fund (EF)	1,307,981,532	1,254,540,148	1,321,957,273	1,313,476,522	1,322,833,018	0.71%
Fish & Wildlife	12,481,014	13,850,694	15,426,252	16,355,474	17,113,525	4.63%
Special Funds & Other Funds [c]	381,839,377	427,290,903	436,307,790	447,169,342	455,988,967	1.97%
Sub-Total	3,086,269,568	3,124,905,231	3,132,815,241	3,077,753,872	3,130,246,999	1.71%
Adjust for inter-fund appropriation: GF Transfer to EF	(268,720,000)	(280,200,000)	(291,127,800)	(240,803,944)	(240,803,945)	0.00%
Total State Funds after EF Transfer	2,817,549,568	2,844,705,231	2,841,687,441	2,836,949,928	2,889,443,054	1.85%
percent of total	67.33%	68.35%	63.99%	59.95%	60.63%	
Federal Funds	1,310,517,486	1,257,860,692	1,354,779,066	1,448,762,460	1,547,314,639	6.80%
Federal ARRA Funds [d]	-	-	178,344,712	376,054,948	251,941,482	-33.00%
Total Funds Before Dedicated Dollars	**4,128,067,054**	**4,102,565,923**	**4,374,811,219**	**4,661,767,336**	**4,688,699,175**	0.58%
percent of total	98.64%	98.57%	98.51%	98.52%	98.39%	
Dedicated Sources						
Local Match	3,044,123	2,951,403	2,553,311	2,993,800	2,193,885	-26.72%
Enterprise Funds	7,862,307	8,150,473	8,254,019	8,669,664	8,677,624	0.09%
Pension & Private Purpose Trust Funds	46,020,607	48,594,698	55,251,374	58,583,801	65,916,620	12.52%
Sub-Total	56,927,037	59,696,574	66,058,704	70,247,265	76,788,129	9.31%
Total Funds and Dedicated Sources	**4,184,994,091**	**4,162,262,497**	**4,440,869,923**	**4,732,014,601**	**4,765,487,304**	0.71%
	100.00%	100.00%	100.00%	100.00%	100.00%	
Fund Sources that are duplicated in the above appropriations:						
Internal Service Funds	65,533,719	66,190,616	66,118,435	70,929,433	70,655,901	-0.39%
Interdepartmental Transfer	34,178,601	35,628,944	32,670,160	45,286,838	41,994,828	-7.27%
Interdepartmental Transfer - ARRA	-	-	-	45,125,036	38,575,036	-14.52%
Global Commitment Fund (c)	782,588,332	819,516,803	900,965,265	965,840,917	1,038,660,106	7.54%
Total	882,300,652	921,336,363	999,753,860	1,127,182,224	1,189,885,871	5.56%
Memo: Total All Appropriations	5,336,014,743	5,363,798,860	5,731,751,583	6,100,000,769	6,196,177,120	1.58%

NOTES:

(a) Act 1 of the 2009 Special Legislative Session, plus other bills; adjusted for Rescission #1 approved by Joint Fiscal Committee 8/16/09, and the Governor's proposal for additional budget adjustments presented to the General Assembly January 19, 2010.

(b) Governor's Recommended Budget Adjustment for FY 2010 presented to the General Assembly on January 19, 2010.

(c) Includes Tobacco Fund, Catamount Fund, State Health Care Resources, Next Generation Fund, and Transportation Infrastructure Bond (TIB) Fund.

(d) American Recovery & Reinvestment Act of 2009 (federal stimulus bill).

SELECTED FUNDS - FY 2011 COMBINED BUDGET RECOMMENDATIONS

General, Transportation and Special Funds (a)

Agency/Department/Program	FY 2011 Gov Recommend GF	FY 2011 Gov Recommend TF	FY 2011 Gov Recommend SF + Tob	FY 2011 Recommended Appropriation	FY 2010 Recommended Appropriation
GENERAL GOVERNMENT					
Administration Agency:					
Secretary of Administration	658,760	-	-	658,760	654,403
Information and Innovation	20,911	-	-	20,911	211,847
Finance & Management	882,783	-	-	882,783	806,362
Human Resources	1,689,278	-	280,835	1,970,113	1,989,314
Buildings and General Services	5,207,957	-	50,000	5,257,957	4,586,740
Tax	14,309,315	-	1,167,901	15,477,216	14,384,336
Libraries	2,534,917	-	132,656	2,667,573	2,619,901
Total Agency of Administration	25,303,921	-	1,631,392	26,935,313	25,252,903
				-	
GIS	-	-	408,700	408,700	408,700
Auditor of Accounts	399,951	-	53,099	453,050	475,107
State Treasurer	1,130,500	-	1,636,099	2,766,599	2,574,551
Labor Relations Board	194,699	-	2,788	197,487	199,235
Executive Office	1,372,674	-	-	1,372,674	1,362,366
Governor-elect	-		-		-
VOSHA Review Board	26,583	-	-	26,583	23,604
Use Tax Reimbursement	11,700,000	-	-	11,700,000	10,807,403
Municipal Tax - Homeowner rebate	16,736,859	-	-	16,736,859	13,725,647
Renter Rebate	4,079,794	-	-	4,079,794	2,543,008
Lt. Governor	167,212	-	-	167,212	163,334
Legislature	7,087,268	-	-	7,087,268	6,722,189
Legislative Council	2,282,993	-	-	2,282,993	2,294,319
Legislative Information Technology	894,587	-	-	894,587	882,857
Sergeant at Arms	559,433	-	-	559,433	540,139
Joint Fiscal Office	1,354,966	-	-	1,354,966	1,484,376
PILOT/Montpelier Services	-	-	5,684,000	5,684,000	5,084,000
Corrections PILOT	-	-	40,000	40,000	40,000
TOTAL GENERAL GOVERNMENT	**73,291,440**	**-**	**9,456,078**	**82,747,518**	**74,583,738**

SELECTED FUNDS - FY 2011 COMBINED BUDGET RECOMMENDATIONS

General, Transportation and Special Funds (a)

Agency/Department/Program	FY 2011 Gov Recommend GF	FY 2011 Gov Recommend TF	FY 2011 Gov Recommend SF + Tob	FY 2011 Recommended Appropriation	FY 2010 Recommended Appropriation
PROTECTION TO PERSONS AND PROPERTY					
Attorney General	3,785,911	-	1,515,000	5,300,911	5,093,034
Court Diversion	1,204,776	-	519,997	1,724,773	1,724,784
State's Attorneys/SIU	9,439,940	-	32,775	9,472,715	8,246,477
Center for Crime Victim Services	1,118,448	-	5,424,117	6,542,565	6,320,613
Sheriffs	3,599,330	-	-	3,599,330	3,466,825
Defender General	11,329,341	-	638,552	11,967,893	11,455,548
Military	3,402,624	-	83,529	3,486,153	3,242,549
Criminal Justice Training Council	1,592,462	-	531,285	2,123,747	2,031,637
Liquor Control	-	-	296,306	296,306	296,306
Secretary of State	1,741,157	-	4,834,524	6,575,681	6,392,696
BISHCA	-	-	14,096,063	14,096,063	13,265,022
Public Safety	31,333,355	24,852,807	11,337,855	67,524,017	56,273,680
Agriculture	5,253,396	-	7,132,742	12,386,138	12,050,655
Public Service Department	-	-	12,180,237	12,180,237	13,563,598
Enhanced 911 Board	-	-	4,605,803	4,605,803	5,487,045
Public Service Board	-	-	2,814,863	2,814,863	2,757,926
Judiciary	30,784,588	-	3,145,326	33,929,914	34,245,944
Human Rights Commission	318,255	-	-	318,255	271,463
TOTAL PROTECTION	**104,903,583**	**24,852,807**	**69,188,974**	**198,945,364**	**186,185,802**
				-	
HUMAN SERVICES				-	
Human Services Agency:				-	
AHS - Secretary's Office	4,805,220	-	430,847	5,236,067	5,678,889
AHS - Secretary's Office - Global Commitment	113,337,417	-	49,002,275	162,339,692	116,245,223
Human Services Board	49,713	-	-	49,713	51,331
Corrections	133,396,480	-	1,961,322	135,357,802	129,513,961
Health	11,422,432	-	8,797,825	20,220,257	19,324,212
Mental Health	11,879,457	-	1,656,836	13,536,293	22,718,967
Office of Vt Health Access	117,753,059	-	3,016,174	120,769,233	102,424,185
Department for Children and Families	95,733,623	-	28,820,199	124,553,822	118,206,922
Disabilities, Aging and Independent Living	16,818,721	-	1,128,159	17,946,880	19,347,703
TOTAL HUMAN SERVICES AGENCY	505,196,122	-	94,813,637	600,009,759	533,511,393
				-	
Commission on Women	296,822	-	5,000	301,822	290,478
RSVP	131,096	-	-	131,096	131,096
Veterans' Home	-	-	11,615,802	11,615,802	10,931,473
TOTAL HUMAN SERVICES	**505,624,040**	**-**	**106,434,439**	**612,058,479**	**544,864,440**

SELECTED FUNDS - FY 2011 COMBINED BUDGET RECOMMENDATIONS

General, Transportation and Special Funds (a)

Agency/Department/Program	FY 2011 Gov Recommend GF	FY 2011 Gov Recommend TF	FY 2011 Gov Recommend SF + Tob	FY 2011 Recommended Appropriation	FY 2010 Recommended Appropriation
Labor	2,561,430	-	3,371,790	5,933,220	5,737,861
TOTAL EMPLOYMENT & TRAINING / LABOR	**2,561,430**	**-**	**3,371,790**	**5,933,220**	**5,737,861**
				-	
GENERAL EDUCATION				-	
Department of Education	8,673,388	-	16,728,905	25,402,293	26,141,160
GF Appropriation to Education Fund	240,803,945	-	-	240,803,945	240,803,944
Teachers' Retirement	51,772,599	-	-	51,772,599	40,228,002
TOTAL GENERAL EDUCATION	**301,249,932**	**-**	**16,728,905**	**317,978,837**	**307,173,106**
				-	
HIGHER EDUCATION AND OTHER				-	
University of Vermont	39,328,123	-	-	39,328,123	36,740,474
Vermont Public Television	547,683	-	-	547,683	547,683
Vermont State Colleges	25,541,180	-	-	25,541,180	23,818,343
Vermont Interactive TV	785,679	-	-	785,679	785,679
Vermont Student Assistance Corp.	19,608,602	-	-	19,608,602	18,363,607
N.E. Higher Education Compact	84,000	-	-	84,000	84,000
TOTAL HIGHER EDUCATION AND OTHER	**85,895,267**	**-**	**-**	**85,895,267**	**80,339,786**
				-	
TOTAL EDUCATION	**387,145,199**	**-**	**16,728,905**	**403,874,104**	**387,512,892**
				-	
NATURAL RESOURCES				-	
Agency of Natural Resources:				-	
ANR - Central Office	5,976,498	-	17,797	5,994,295	6,200,091
Environmental Conservation	6,913,638	-	18,012,946	24,926,584	25,510,039
Fish & Wildlife	1,180,253	-	-	1,180,253	1,101,852
Forests, Parks & Recreation	5,370,370	-	9,199,859	14,570,229	14,504,387
Total Agency of Natural Resources	19,440,759	-	27,230,602	46,671,361	47,316,369
				-	
Natural Resources Board	766,716	-	1,965,886	2,732,602	2,541,313
TOTAL NATURAL RESOURCES	**20,207,475**	**-**	**29,196,488**	**49,403,963**	**49,857,682**
				-	

SELECTED FUNDS - FY 2011 COMBINED BUDGET RECOMMENDATIONS

General, Transportation and Special Funds (a)

Agency/Department/Program	FY 2011 Gov Recommend GF	FY 2011 Gov Recommend TF	FY 2011 Gov Recommend SF + Tob	FY 2011 Recommended Appropriation	FY 2010 Recommended Appropriation
COMMERCE & COMMUNITY DEVELOPMENT				-	
Agency of Commerce & Comm Development				-	
ACCD - Administration	2,726,075	-	-	2,726,075	2,630,244
Housing & Community Affairs (b)	-	-	-	-	5,181,683
Economic, Housing & Community Development	6,108,660	-	4,551,257	10,659,917	5,023,576
Tourism & Marketing	3,279,810	-	6,000	3,285,810	3,443,075
Total Agency of Commerce & Comm Development	12,114,545	-	4,557,257	16,671,802	16,278,578
Council on the Arts	507,607	-	-	507,607	507,607
Vermont Symphony Orchestra	113,821	-	-	113,821	113,821
VT Historical Society	795,669	-	-	795,669	795,669
Housing & Conservation Trust	-	-	6,606,662	6,606,662	8,326,662
VT Humanities Council	172,670	-	-	172,670	172,670
TOTAL COMMERCE & COMMUNITY DEV.	**13,704,312**	**-**	**11,163,919**	**24,868,231**	**26,195,007**
				-	
DEBT SERVICE	**67,372,470**	**3,482,640**	**1,026,225**	**71,881,335**	**71,446,672**
TRANSPORTATION				-	
Agency of Transportation				-	
AOT Division Appropriations and Programs	-	121,917,530	-	121,917,530	118,344,005
AOT Dept. of Motor Vehicles	-	23,096,730	-	23,096,730	23,040,703
AOT Town Highway Programs	-	40,084,966	-	40,084,966	36,946,742
Total Agency of Transportation	-	185,099,226	-	185,099,226	178,331,450
				-	
Transportation Board	-	86,544	-	86,544	86,891
TOTAL TRANSPORTATION	**-**	**185,185,770**	**-**	**185,185,770**	**178,418,341**
Pay Act	556,500	-	-	556,500	4,282,138
Other Reductions	(68,416,402)			(68,416,402)	
One-Time Approrpiations	11,551,885	2,288,340	-	13,840,225	16,117,402
OTHER	-	-	4,793,000	4,793,000	6,438,000
APPROPRIATION TOTAL	**1,118,501,932**	**215,809,557**	**251,359,818**	**1,585,671,307**	**1,551,639,975**

(a) Does not include the following funds: Education, Fish & Wildlife, Global Commitment, State Health Care Resources, Catamount, Next Generation, Enterprise, Local Match, Pension, Trust, Internal Service and Interdepartmental Transfer funds.

(b) Housing, Community Affairs and Econcomic Development combined in FY 2011.

SELECTED FUNDS - COMBINED APPROPRIATION HISTORY

General, Transportation and Special Funds (a)

FY 2007 - FY 2011

Agency/Department/Program	FY 2007 Final Appropriation	FY 2008 Final Appropriation	FY 2009 Final Appropriation	FY 2010 Recommend Adjusted Appropriation	FY 2011 Recommended Appropriation
GENERAL GOVERNMENT					
Administration Agency:					
Secretary of Administration	984,985	920,232	747,540	654,403	658,760
Information and Innovation	-	736,537	581,624	211,847	20,911
Finance & Management	1,174,751	1,048,822	957,117	806,362	882,783
Human Resources	3,177,942	2,757,841	2,301,741	1,989,314	1,970,113
Buildings and General Services	9,358,802	9,692,596	7,788,598	4,586,740	5,257,957
Tax	14,446,934	14,762,420	14,150,029	14,384,336	15,477,216
Libraries	2,754,540	2,842,165	2,592,618	2,619,901	2,667,573
Total Agency of Administration	31,897,954	32,760,613	29,119,267	25,252,903	26,935,313
GIS	411,685	430,210	408,700	408,700	408,700
Auditor of Accounts	574,336	578,456	541,941	475,107	453,050
State Treasurer	2,343,296	2,686,169	2,588,944	2,574,551	2,766,599
Labor Relations Board	204,362	211,142	189,168	199,235	197,487
Executive Office	1,482,508	1,534,310	1,379,676	1,362,366	1,372,674
Governor-elect	-	-	-	-	-
VOSHA Review Board	19,998	23,327	22,806	23,604	26,583
Use Tax Reimbursement	8,113,944	8,861,267	9,850,000	10,807,403	11,700,000
Property Tax Assistance	2,250,000	-	-	-	-
Municipal Tax - Homeowner rebate	-	11,206,140	12,921,868	13,725,647	16,736,859
Renter Rebate	-	-	2,386,756	2,543,008	4,079,794
Lt. Governor	146,747	155,032	155,113	163,334	167,212
Legislature	7,199,906	6,886,840	7,243,021	6,722,189	7,087,268
Legislative Council	2,005,212	2,125,647	2,264,917	2,294,319	2,282,993
Legislative Information Technology	585,415	623,590	880,407	882,857	894,587
Sergeant at Arms	600,801	617,701	609,445	540,139	559,433
Joint Fiscal Office	1,256,470	1,270,579	1,272,602	1,484,376	1,354,966
PILOT/Montpelier Services	3,484,000	3,634,000	4,684,000	5,084,000	5,684,000
Corrections PILOT	40,000	40,000	40,000	40,000	40,000
TOTAL GENERAL GOVERNMENT	**62,616,634**	**73,645,023**	**76,558,631**	**74,583,738**	**82,747,518**

SELECTED FUNDS - COMBINED APPROPRIATION HISTORY

General, Transportation and Special Funds (a)

FY 2007 - FY 2011

Agency/Department/Program	FY 2007 Final Appropriation	FY 2008 Final Appropriation	FY 2009 Final Appropriation	FY 2010 Recommend Adjusted Appropriation	FY 2011 Recommended Appropriation
PROTECTION TO PERSONS AND PROPERTY					
Attorney General	5,713,360	6,273,914	5,985,097	5,093,034	5,300,911
Court Diversion	1,604,534	1,604,534	1,724,534	1,724,784	1,724,773
State's Attorneys/SIU	7,976,620	8,623,849	9,085,231	8,246,477	9,472,715
Center for Crime Victim Services	6,001,408	6,777,259	7,329,555	6,320,613	6,542,565
Sheriffs	3,093,503	3,353,439	3,419,208	3,466,825	3,599,330
Defender General	9,543,838	10,079,614	11,147,581	11,455,548	11,967,893
Military	3,270,409	3,381,936	3,460,130	3,242,549	3,486,153
Criminal Justice Training Council	1,845,067	1,914,657	1,897,495	2,031,637	2,123,747
Liquor Control	289,768	289,645	296,306	296,306	296,306
Racing Commission	1,000	1,000	-	-	-
Secretary of State	4,592,792	4,560,941	5,845,205	6,392,696	6,575,681
BISHCA	12,975,828	13,289,105	13,494,796	13,265,022	14,096,063
Public Safety	57,103,194	58,257,595	61,372,203	56,273,680	67,524,017
Agriculture	12,746,380	13,623,719	12,519,984	12,050,655	12,386,138
Public Service Department	9,642,865	10,065,968	10,231,626	13,563,598	12,180,237
Enhanced 911 Board	3,931,601	3,356,610	5,482,486	5,487,045	4,605,803
Public Service Board	2,757,097	2,752,841	2,817,349	2,757,926	2,814,863
Judiciary	30,522,025	33,603,336	33,383,446	34,245,944	33,929,914
Human Rights Commission	285,925	311,382	266,426	271,463	318,255
TOTAL PROTECTION	**173,897,214**	**182,121,344**	**189,758,658**	**186,185,802**	**198,945,364**
HUMAN SERVICES					
Human Services Agency:					
AHS - Secretary's Office	4,318,906	4,635,410	4,677,019	5,678,889	5,236,067
AHS - Secretary's Office - Global Commitment	158,692,085	159,795,726	131,527,655	116,245,223	162,339,692
Human Services Board	49,283	50,977	49,178	51,331	49,713
Corrections	111,052,492	117,605,108	126,668,271	129,513,961	135,357,802
Health	42,561,960	18,137,095	18,746,513	19,324,212	20,220,257
Mental Health	-	21,373,099	21,874,430	22,718,967	13,536,293
Office of TV Health Access	121,225,950	132,130,989	113,907,951	102,424,185	120,769,233
Department for Children and Families	98,623,312	121,259,715	120,951,011	118,206,922	124,553,822
Disabilities, Aging and Independent Living	19,631,950	19,867,516	19,999,136	19,347,703	17,946,880
TOTAL HUMAN SERVICES AGENCY	556,155,938	594,855,635	558,401,164	533,511,393	600,009,759
Commission on Women	260,201	267,552	277,177	290,478	301,822
RSVP	131,096	131,096	131,096	131,096	131,096
Veterans' Home	10,193,494	10,466,920	10,672,788	10,931,473	11,615,802
TOTAL HUMAN SERVICES	**566,740,729**	**605,721,203**	**569,482,225**	**544,864,440**	**612,058,479**

SELECTED FUNDS - COMBINED APPROPRIATION HISTORY
General, Transportation and Special Funds (a)
FY 2007 - FY 2011

Agency/Department/Program	FY 2007 Final Appropriation	FY 2008 Final Appropriation	FY 2009 Final Appropriation	FY 2010 Recommend Adjusted Appropriation	FY 2011 Recommended Appropriation
Labor	5,220,335	5,280,195	5,291,790	5,737,861	5,933,220
TOTAL EMPLOYMENT & TRAINING / LABOR	**5,220,335**	**5,280,195**	**5,291,790**	**5,737,861**	**5,933,220**
GENERAL EDUCATION					
Department of Education	33,658,474	33,219,608	27,865,146	26,141,160	25,402,293
GF Appropriation to Education Fund	268,720,000	280,200,000	291,127,800	240,803,944	240,803,945
Renter Rebate	-	2,277,149	-	-	-
Teachers' Retirement	24,446,729	32,549,097	33,549,097	40,228,002	51,772,599
TOTAL GENERAL EDUCATION	**326,825,203**	**348,245,854**	**352,542,043**	**307,173,106**	**317,978,837**
HIGHER EDUCATION AND OTHER					
University of Vermont	36,976,719	38,271,188	36,740,473	36,740,474	39,328,123
Vermont Public Television	596,785	605,737	564,620	547,683	547,683
Vermont State Colleges	23,971,763	24,810,775	23,818,343	23,818,343	25,541,180
Vermont Interactive TV	847,944	858,163	769,119	785,679	785,679
Vermont Student Assistance Corp.	18,481,892	19,128,758	18,363,607	18,363,607	19,608,602
N.E. Higher Education Compact	80,000	84,000	84,000	84,000	84,000
TOTAL HIGHER EDUCATION AND OTHER	**80,955,103**	**83,758,621**	**80,340,162**	**80,339,786**	**85,895,267**
TOTAL EDUCATION	**407,780,306**	**432,004,475**	**432,882,205**	**387,512,892**	**403,874,104**
NATURAL RESOURCES					
Agency of Natural Resources:					
ANR - Central Office	7,174,286	7,401,861	7,552,887	6,200,091	5,994,295
Environmental Conservation	25,021,910	25,696,307	24,277,732	25,510,039	24,926,584
Fish & Wildlife	2,096,314	2,128,649	1,134,531	1,101,852	1,180,253
Forests, Parks & Recreation	15,244,555	15,595,682	15,299,204	14,504,387	14,570,229
Total Agency of Natural Resources	49,537,065	50,822,499	48,264,354	47,316,369	46,671,361
Natural Resources Board	2,742,438	2,827,318	2,746,988	2,541,313	2,732,602
TOTAL NATURAL RESOURCES	**52,279,503**	**53,649,817**	**51,011,342**	**49,857,682**	**49,403,963**

SELECTED FUNDS - COMBINED APPROPRIATION HISTORY

General, Transportation and Special Funds (a)

FY 2007 - FY 2011

Agency/Department/Program	FY 2007 Final Appropriation	FY 2008 Final Appropriation	FY 2009 Final Appropriation	FY 2010 Recommend Adjusted Appropriation	FY 2011 Recommended Appropriation
COMMERCE & COMMUNITY DEVELOPMENT					
Agency of Commerce & Commerce Development					
ACCD - Administration	2,184,996	2,894,771	2,521,630	2,630,244	2,726,075
Housing & Community Affairs	7,266,119	7,191,952	5,372,581	5,181,683	-
Economic, Housing & Community Development	5,699,910	5,729,541	5,524,266	5,023,576	10,659,917
Tourism & Marketing	4,338,938	4,114,213	3,765,688	3,443,075	3,285,810
Total Agency of Commerce & Commerce Development	19,489,963	19,930,477	17,184,165	16,278,578	16,671,802
Council on the Arts	529,618	545,618	507,607	507,607	507,607
Vermont Symphony Orchestra	118,780	122,343	113,821	113,821	113,821
VT Historical Society	733,393	828,342	770,635	795,669	795,669
Housing & Conservation Trust	14,630,883	15,383,258	13,449,095	8,326,662	6,606,662
VT Humanities Council	180,599	185,599	172,670	172,670	172,670
TOTAL COMMERCE & COMMUNITY DEV.	**35,683,236**	**36,995,637**	**32,197,993**	**26,195,007**	**24,868,231**
DEBT SERVICE	**69,129,965**	**68,698,029**	**71,459,051**	**71,446,672**	**71,881,335**
TRANSPORTATION					
Agency of Transportation					
AOT Division Appropriations and Programs	123,249,032	128,331,583	117,211,319	118,344,005	121,917,530
AOT Dept. of Motor Vehicles	19,315,280	24,588,202	22,196,373	23,040,703	23,096,730
AOT Town Highway Programs	40,740,841	38,359,409	37,866,610	36,946,742	40,084,966
Total Agency of Transportation	183,305,153	191,279,194	177,274,302	178,331,450	185,099,226
Transportation Board	84,600	87,106	89,802	86,891	86,544
TOTAL TRANSPORTATION	**183,389,753**	**191,366,300**	**177,364,104**	**178,418,341**	**185,185,770**
Pay Act	5,805,219	1,192,197	2,969,635	4,282,138	556,500
Other Reductions	-	-	-	-	(68,416,402)
One-Time Approrpiations	-	-	6,745,000	16,117,402	13,840,225
Other	47,427,402	47,547,442	7,293,000	6,438,000	4,793,000
APPROPRIATION TOTAL	**1,609,970,296**	**1,698,221,662**	**1,623,013,634**	**1,551,639,975**	**1,585,671,307**

(a) Does not include the following funds: Education, Fish & Wildlife, Global Commitment, State Health Care Resources, Catamount, Next Generation, Enterprise, Local Match, Pension, Trust, Internal Service and Interdepartmental transfer funds.

(b) Housing, Community Affairs and Econcomic Development combined in FY 2011.

As specified in 32 VSA §311, the following reports on the financial integrity of the state employees' and teachers' retirement systems.

Contribution Levels

VSERS

As a result of the June 30, 2009 actuarial valuation, the actuary for the Vermont State Employees' Retirement System (VSERS) recommended a contribution during fiscal year 2011 of $41,581,656 to the pension plan (VSERS pension) and $39,436,550 to the Vermont State Employees' Other Post-Employment Benefits (VSERS OPEB) plan.

The actuary's recommended contribution to the VSERS pension incorporates the recommended normal contribution of $23,334,122 (5.52% of estimated payroll) plus $18,247,534 for the annual contribution towards the unfunded actuarial accrued liability (UAAL). To calculate the state's contribution, the actuarial recommendation has been reduced by $395,625 for the Treasurer's estimate of a FY 2011 contribution by town participants in VSERS, making the state's net contribution for the actuarial recommendation $41,186,031. The state also contributes an amount to prepay the Treasurer's estimate of non-healthcare administrative expenses which for fiscal year 2011 is $7,262,903. This amount has been adjusted for two factors: for a reconciliation of actual contributions to actual expenses for the most recently completed fiscal year which allowed a $1,304,769 reduction for over-contributing in FY 2009 and a reduction for estimated FY 2011 investment fees of $5,012,095, which is commonly not prepaid in other retirement plans. These reductions result in a state contribution of $946,039 in FY 2011 to cover anticipated non-healthcare administrative expenses. Added to the net contribution for the actuarial recommendation, the state's planned total contribution to the VSERS pension for FY 2011 will be $42,132,070.

The actuary's recommended contribution to the VSERS OPEB is $39,436,550 incorporates the recommended normal contribution of $15,845,807 plus amortization of the unfunded actuarial liability of $23,790,743.

The state's planned contribution to the VSERS OPEB during fiscal year 2011 is $27,000,000 which is the Treasurer's estimate of VSERS retiree health care costs. It is anticipated that VSERS coverage of retiree prescriptions will produce Medicare Part D reimbursements to the system of approximately $1.8 million which will be deposited into the VSERS OPEB during fiscal year 2011.

VSTRS

As a result of the June 30, 2009 actuarial valuation, the actuary for the Vermont State Teachers' Retirement System (VSTRS) recommended a contribution during fiscal year 2011 of $63,501,220 to the pension plan (VSTRS pension) and $33,805,841 to the Vermont State Teachers' Other Post-Employment Benefits (VSTRS OPEB) plan.

The actuary's recommended contribution to the VSTRS pension incorporates the recommended normal contribution of $22,828,834 plus $40,672,386 for the annual contribution towards the unfunded actuarial accrued liability (UAAL). The actuary's recommended contribution to the VSTRS OPEB incorporates the recommended normal contribution of $11,086,976 plus

amortization of the unfunded actuarial liability of $22,718,865.

The state plans to achieve full funding at the actuarially recommended contribution level for the VSTRS pension for FY 2011 through a combination of $51,772,599 in general funds, $10,408,996 in education funds and an estimated $1,319,625 of Medicare Part D reimbursement funds. The state does not plan to make a contribution to the VSTRS OPEB during fiscal year 2011. The VSTRS OPEB has no pre-funding and no assets. Payments for retired teachers' health care costs, estimated to be $20,000,000 in FY 2011 will continue to be paid from the corpus of the VSTRS pension.

Funding Levels

Based on Governmental Accounting Standards Board Reporting Requirement Number 25 (GASB 25), the funded ratios for the State Employees' and Teachers' Retirement Funds for the period ending June 30, 2008 are 78.9% and 65.4% respectively. The funded ratios for the State Employees' and Teachers' OPEB Funds for the period ending June 30, 2009 are 0.7% and 0.0% respectively. The Administration, Treasurer's Office, Legislature and other affected parties will need to work together to develop a multi-year plan to address funding pension plan and OPEB liabilities. A very productive bi-partisan retirement commission worked to develop some very significant recommendations for consideration and adoption during the 2010 legislative session. The Governor's proposal advances the Commission's recommendations which will save the General Fund approximately $25 million in FY 2011.

Acknowledgements

This Executive Summary and the Governor's Recommended Budget could not have been prepared without the extraordinary efforts of all the staff in the Budget & Management Office of the Department of Finance and Management. Their concern for the State of Vermont, dedication, attention to detail and overall tenacity are greatly appreciated.

The Department of Finance and Management would like to thank Agency and Department heads across state government with special thanks to the State's Business Managers and finance staff. Their contribution to the overall success of this presentation of the Governor's budget is greatly appreciated.

Please contact any of the following with any questions regarding this publication at (802) 828-2376:

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This publication is available for viewing or printing at the Department of Finance and Management's Website, under "Key Budget Documents" at: http://finance.vermont.gov/state_budget/rec

Fiscal Year 2011
Our Commitment to a Stronger Tomorrow

Fiscal Year 2011 Executive Budget Recommendations
is a publication of the
Vermont Department of Finance and Management,
James Reardon, Commissioner.

The purpose of this publication is to inform members of the Vermont Legislature, state and local government officials, and Vermont citizens of the Fiscal Year 2011 Budget Recommendations of Governor James H. Douglas.

This publication is available for viewing or printing at the
Department of Finance and Management's Web Site
http://finance.vermont.gov/state_budget/rec

This book is printed on recycled paper.

Challenge for Change Reports

CHALLENGES FOR CHANGE: RESULTS FOR VERMONTERS

STEERING TEAM REPORT TO THE JOINT LEGISLATIVE GOVERNMENT ACCOUNTABILITY COMMITTEE

JANUARY 5, 2010

VT LEG 251508.1

WHAT IS A "CHALLENGE?"

In 1961 there were no proposals on how to get to the moon. In fact, NASA engineers were appalled when President Kennedy challenged them to find a way to get there by the end of the decade. Leaders should not put a thought out there, they reasoned, unless there is certainty that it can be realized. And if the President had said "My consultants have a plan to get to the moon," NASA engineers' first reaction would be to tell him why the consultants are wrong. Kennedy, on the other hand, knew that real change begins not with known certainties, but with bold aspirations; and he knew NASA had great people who could figure it out if they were pushed to do so.

Similarly, the process of reforming Vermont government services is not *beginning* with proposals developed by outside consultants. Rather, the development of specific proposals is best done by fully engaging Vermont state executives and lawmakers. Innovation starts with questioning old assumptions. Each of the challenges that is being put forth suggests the strong possibility that redesigning the way services are delivered can produce better outcomes with less cost. And, some key design principles for a new way of doing things are offered with each challenge.

The best challenges have these features:

- **A good challenge is unequivocal.** These challenges don't ask people if they can find savings. Rather, in these challenges, the savings are **taken** in the FY11 and FY12 budget process. There is no argument about money. The money is not there to spend. The challenge is to deliver the same or better result *with the money that is available.*

- **A good challenge is bold.** Most of the meat of these challenges comes, not from PSG, but from people in the legislative and executive branches of Vermont state government. Yet most of these ideas are too bold for an individual to raise without being immediately shot down by the forces of the status quo. This process is allowing bold ideas at least to be put on the table for dialog.

- **A good challenge is framed in terms of value.** From the citizens' perspective, value is *results produced for the dollar*. Value is a ratio. These challenges are not just about money; they are about better results with less money. In contrast to a "cut," challenges give Vermonters hope that at least some of the budget balancing solution will be a winner for them.

- **A good challenge involves support.** These opportunities outlined in the following pages challenge people to stretch in terms of the value they offer, but also provide them with some tools to succeed. One-time investments associated

with many of the challenges are one form of support as are some of the "redesign options" offered with each challenge.

How will these ideas germinate and grow?

Our experience suggests challenges like these are a good way to start the process of change. One way or the other, the budget will be adjusted to a spending level Vermonters can tolerate. Changing the way services are delivered so that results can improve despite less money, however, will require a lot more work.

These are the rough stages that will follow:

1. **Design.** Meeting these challenges means applying new kinds of thinking to the specific areas involved. It won't happen naturally. We are all too conditioned to think in the same old ways. "Design" can be a structured, rapid process for adding a lot of the necessary meat to the bones of these challenges. *It can even take place during the upcoming legislative session* so that legislators and the Governor can see more specifics before approving the concept. Good designs can be produced in two to three weeks if the design process is intensively supported with people facile in new thinking.

2. **Detailed Planning.** Designs provide a blueprint; construction plans are also necessary. Here, again, champions of change must produce urgency by demanding rapid planning. Normally, doing our regular jobs comes before planning something new. We turn our attention to the new thing as the calendar permits. West German Chancellor Kohl's cabinet told him it would take 10 years to plan the reunification of West and East Germany (at his demand, they planned and reunified in eight-and-a-half months). Detailed planning can also be done in a matter of weeks.

3. **Dealing with resistance.** There will be great resistance to every one of these challenges. This is natural; in fact, it is desirable because the resistance can teach us what we need to know to make the changes successful. We have found that the best approach is not to try to overcome the resistance, but rather, to embrace it. Embracing the resistance does not mean yielding to it. On the contrary, it means persisting but also learning from it. Beginning with the Steering Team, and soon thereafter with the Governor and legislators, this process will commence as soon as the challenges are released. Only persistent committed leadership will sustain the challenges through the pressure of the resistance. These challenges each need champions willing to provide that leadership.

4. **Supporting Implementation.** Those charged with implementing these ideas will need support from the Governor and the General Assembly. Theirs is not an easy task. Once they see that this is a change that is going to happen, new champions will emerge and carry the concepts to fruition.

5. **Promoting Learning.** What is learned from making these changes will be the fuel for many other innovations. The learning must be captured and it must be instilled. As instigators of the change, the Governor and General Assembly need to refrain from engaging in efforts to give credit or attach blame. Rather, it is most powerful to keep asking the question: "What are we learning?" This is the best way to hold people accountable for meeting the challenges.

What is the fiscal impact of the challenges?

The eight challenges issued here will address an estimated $38 million general funds and $12 million in property tax pressure in FY 2011. In FY 2012, after full implementation, it is estimated to reduce spending $72 million in general funds and $26 million in property tax pressures.

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General Government

1 - Charter Units

The Challenge

Select units of state government will be held accountable for producing and improving measureable results while spending $2 million (GF) less in FY11 and $4.5 million (GF) less in FY12, or generating a like amount in entrepreneurial (non tax or fee) revenue.

Redesign Options

Units of government, which could be an agency, a department, a program or a project, will have the option to enter into Charter Agreements. These Charter Units will pioneer a new "bureaucracy-busting deal." Charter Units may be selected by asking for volunteers or by inviting a few trusted unit leaders to be accountable for improving results and spending fewer general funds or generating additional revenue. In return, they are exempt from many bureaucratic requirements. Charter Units will lift their eyes from *rules* to *results.*

Charter Units are authorized by legislation, and commitments are documented in annual Charter Agreements, negotiated and signed by each unit leader and the Governor. Legislation may require periodic progress reporting to legislators. Charter Units must collectively contribute a very modest percent of their total general fund operating budgets totaling at least $3 million in 2011, and $5 million in 2012, with investment dollars set aside each year to foster Charter Unit innovation.

One-time Investment

For each year Charter Units are authorized, an investment will be made available in a Charter Unit grant fund to foster innovation. Charter Unit applications may request funding to streamline processes and improve services. Investment of $1 million will be made in FY11 and $500,000 will be made in FY12.

The Bottom Line

	FY 2010 (in Millions)	FY2011 (in Millions)	FY2012 (in Millions)
Appropriation	$1,477.3 **All state less TF, EF, Debt, and Tax Relief**		
Charter Unit Results		Outcomes in Charter Agreements	Outcomes in Charter Agreements
Investment		$1.0	$0.5
Net GF Savings		$2.0	$4.5

2 - Performance Contracting and Grant Making

The Challenge

Get better outcomes from contractors and grantees at a 3.5% lower cost in FY11 and 10% less cost to the state in FY12.

Redesign Options

It is estimated that Vermont executes a total of $200 million worth of contracts and grants each year. All but a very few of these contracts pay vendors for hours or other units of effort, *not for results.* You get what you pay for.

The federal government and many state governments are putting increased emphasis on using measured results as the determinant of payment. This is not essentially a "bonus" system but rather paying when an outcome is delivered rather than paying when an hour is devoted to the work. There is considerable evidence from these cases that when you pay for outcomes you get better outcomes (often at less cost). If, on the other hand, you pay for effort, you will get more effort. Vendors and grantees tend to do that which earns them the most money.

But revenue isn't the only consideration for vendors and grantees. Vendors are also very interested in profit and grantees are interested in minimizing administrative costs. Most of them will emphatically agree that the cost of delivering services to most governments is considerably higher than the cost of delivering such services in the private sector. There is a lot of red tape; the state of Vermont pays for this red tape in higher contractor fees and grant administration allowances. In the best practices, performance contracting also means that the state carefully reviews with the vendor or grantee all of the requirements, reports, and other obligations *with an eye toward reducing the cost of compliance for vendors while still maintaining compliance with essential conditions.* Such a review can significantly reduce the cost of compliance for the vendors and grantees and therefore, the price of the contract/grant.

Performance contracting can be initiated in the solicitation process. But existing contracts can also be renegotiated—especially multi year contracts. In either case, performance contracting means *negotiating* with the vendor a contract that (a) reduces the total price, (b) reduces red tape, and (c) pays for results.

Experience shows that savings upwards of 15% of the contract value can be achieved even as results are also improved. Design options for pursuing this opportunity include the following steps:

- Capture 3.5% savings in FY11 and 10% savings in FY12 by reducing the appropriations associated with these contracts and grants by that amount.
- Put all contractors and grantees on notice that they, too, are expected to shoulder some of the fiscal pain.
- Challenge state agencies to immediately begin developing performance agreements with new and existing vendors and grantees.
- In FY11 provide agencies with an outside resource experienced in performance contracting to help with the development of RFP's and the renegotiation of existing contracts.
- Bring on-line in FY12, a very small unit in the Secretary of Administration's office that promotes and oversees performance contracting and performance grant making.
- Build a simple information system that informs policy makers and the public about what results Vermont is getting for its professional service contract dollars.

Investment

In FY11 and again in FY12, a one-time investment of $500,000 will be made available to the Secretary of Administration to (a) build a simple information system that tracks personal service contracts; and (b) contract for help in negotiating performance contracts.

In FY12 an office of performance contracting will be established; over the course of the year they will take over the management of performance contracting from the temporary outside resource engaged for this purpose.

The Bottom Line

	FY 2010 (in Millions)	FY2011 (in Millions)	FY2012 (in Millions)
Appropriation	$200m Gross (includes grants - no TF construction included)		
Index of Results % Contract/Grant			
Investment		$0.5	$0.5
Reallocation for Oversight			$0.5
Net Total Savings		$6.5	$19.5
Net GF Savings		$2.6	$7.8

Protection Function

The Judiciary was charged separately to review and redesign systems to achieve a specific savings target. This was not included in the PSG scope of work. The Commission on Judicial Operation which was created by an act of the Vermont Legislature in May 2008 and charged with conducting a thorough review of Vermont's court system, with the goal of providing for more efficient and effective delivery of judicial services. In May 2009, the Commission was further directed to identify at least $1 million in savings in the FY 2010 budget. The proposal is available online at www.vermontjudiciary.org/MasterPages/WhatsNew-CommissionJudicialOps.aspx.

With the Judiciary proposal, there is the potential for changes and investments at the criminal justice and protection organizations that impact the Judiciary. Such changes could result in savings to these organizations and complement the Judiciary proposal as well as the Corrections and Regulatory Challenges included in this report.

Human Services

3 - A Client Centric, Results-Based Human Service Package

See also Parts A thru D

The Challenge

To redesign the State's human service and health care delivery model into a client-centric, integrated system that improves outcomes while being affordable within tight budget constraints. Four different applications of this concept (Parts A-D) are presented as individual challenges in this package. There are undoubtedly other client centric applications in the human service arena.

Summary of Current System Weaknesses

State human service professionals struggle to create unified and integrated support to consumers and communities. The existing operating environment is rigid and often hinders coordinated policy and practice, as well as inadvertently promotes redundancy and inefficiencies, while failing to address a person or family's multiple, interrelated needs. Federal funding is a primary – although not the only – contributor to this deficiency as it supports an array of public sector human services that operate in programmatic, fiscal and reporting silos.

The administration of financial standards is one of the most complicated and costly components of the eligibility process. Standards vary from program-to-program and caseworkers – as well as applicants and beneficiaries – often have a difficult time understanding what is required and what is not. Program differences relative to income and resources tests often create disincentives and inequities for those moving towards self sufficiency.

Along these lines, redundancies in service delivery are also evident. Some clients interact with a number of caseworkers and/or agencies to receive services that could be better organized by a single person who is given the discretion and flexibility to address the problem comprehensively and align necessary direct services for the client. Today, disparate federal efforts provide categorical supports that do not foster personal growth.

Further, the current system is largely designed to pay providers through fee-for-service units rather than through bundled or capitated payments or paying for outcomes. In addition, the same provider may have a number of contracts with the State for different services for the same client, thereby increasing the complexity of tracking outcomes to reward results.

Overall Vision

The Client

The State's vision begins and ends with the client. Adopting best practices from Vermont's groundbreaking *Blueprint for Health*, human service clients will have a "medical home" for state services where a "community care team" will help guide them to self-sufficiency using an integrated, individualized approach.

This approach will make the myriad of federal and state programs invisible to the client. Instead of receiving separate assistance from WIC, fuel assistance, food stamps, Reach-Up, and child care subsidy, a primary care manager could comingle funds or service allocations into one budget – and then clients would create self-sufficiency plans ("exit strategies") designed to move them out of poverty as quickly as possible.

These plans would consider the "cliff study" and be designed to reward individuals or families for positive outcomes, rather than create disincentives for progress. Further, instead of a number of programs subsidizing partial needs, these plans will allow clients to make decisions much like non-subsidized families do and further develop their self-sufficiency skills.

The System

To achieve this client centric approach, the State will seek to redesign the delivery system through the more effective and efficient alignment of financial and staff resources across public sector programming, such as economic benefits, social services, health and human service programs. The focus will shift from one of units of service or single benefit packages to one of quality and results. Developing more integrated and streamlined client and fiscal management strategies will reflect:

- A holistic and consistent framework for assessing and prioritizing needs;
- Single-point, unified intake and care management consistent with principles used in the *Blueprint for Health*;
- System maximum communication and effective use of benefits are applied when more than one service or type of support is being provided to a single consumer or family;
- Intelligent data collection and analysis at state, provider and client level to support the ongoing assessment of service quality, financial metrics and organizational improvement; and
- Linking payment to results.

The state will redesign service delivery to work seamlessly across federal programs to:

- Create more efficient administrative processes and oversight requirements at the State and provider level;
- Eliminate duplicative business processes, program monitoring and fiscal and data reporting requirements and thus reduce implementation costs;

- Create more efficient payment mechanisms that combine funding streams, create incentive reimbursements and move to performance based contracting rather than individual fee-for-service payments or traditional economic and social benefit options;
- Prioritize initiatives based on the demographics, risk factors and specific needs of its citizens.

Federal Waiver

In order to derive maximum benefit from the redesign, the state will seek a *Global Commitment*-style super-waiver from Washington that covers all human service programs across a number of federal agencies, including HHS, USDA, and HUD. The waiver will provide for unprecedented flexibility from federal requirements. The state will pass the flexibility granted by the federal government through to its service providers. Additional flexibilities should not be construed to release the state or providers from obligations to ensure that consumer rights are protected and payments are appropriate.

While a federal waiver is preferable, the overall redesign should not be contingent on the waiver. In fact, the overall project should be structured on independent tracks, so if any one track fails, the other tracks would be unaffected. As tracks ultimately intersect and join together, the whole of the project will be greater than the sum of its parts.

Technology is the Key

While the state works on actual program integration as described above, we can use technology to harmonize programs from the client's point of view to achieve better outcomes and to deliver better service with fewer resources.

Conceptually, each client of the state will start with a web page, which, after initial registration, will become the online point of entry for the state. This system will be designed so that data entered for one program such as employment status, income, number of dependents, etc. will not have to be reentered for another program. The portal will be client centric rather than program-oriented; it will serve as the front end to rules-based logic which will determine which programs and benefits and services the client is eligible for, based on a single flexible rules engine. New services can be added by subject matter experts who do not have to be programmers.

Since not all clients have access to either the internet or to the equipment, knowledge, or motivation to use it, state offices will have kiosks where functionality will be available with touch screen, document, and card reader capability. A successful model for this system is airline check-in, where all travelers are encouraged either to perform functions online or at the kiosk where attendants are available to instruct and help. This is a basic change from the old service paradigm of a client waiting in a line, finally talking to an