

Joint Fiscal Office

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MEMORANDUM

To: Representative Martha Heath, Chair,
Senator Jane Kitchel, Vice Chair,
Members of the Joint Fiscal Committee

From: Stephen Klein, Chief Fiscal Officer

Date: November 6, 2014

Subject: November 2014 – Fiscal Officers’ Report

What follows is an update of developments, some of which will be on the agenda for the November Fiscal Committee meeting:

1. FY 2015 Revenues - The General Fund - After the first four months of the fiscal year, revenues are down \$11.9 million. For a number of reasons, this understates the level of revenue risk.

- Personal income tax is down \$14.9 million, or 6.3%. Withholding and refunds are large contributors to this shortfall. If these trends continue, the revenue shortfall for FY 2015 and beyond could be larger. As requested at the last Joint Fiscal Committee (JFC) meeting, the Administration and Joint Fiscal staff met to begin the process of ascertaining the reason for this revenue miss. The Tax Department has been pulling some data for Jeff Carr and Tom Kavet to review and we hope to have more information in the next few weeks. Jeff and Tom have been heavily involved in bringing the REMI model up to operational capacity for Health Care impact analysis which has prevented quicker action on the revenue front.
- Sales tax and meals and rooms tax are above forecasts. Both are about 3% over target, which is good. Sales tax is up \$2.5 million while meals and rooms tax is up \$1.6 million. However, these revenue sources represent a smaller share of the total General Fund.
- Corporate revenue is an interesting case. Corporate revenues are tracking 20% over forecast, or up \$4.5 million YTD. However, there is considerable risk in corporate revenues. With the pending sale of IBM to Global Foundries, the impact on corporate tax revenues may be substantial. With water’s-edge unitary taxation, Vermont has benefited from IBM corporate profits. It is not clear that Global Foundries will produce the same level of profit and corporate tax revenues that IBM did.
- The estate tax is difficult to estimate and does not lend itself to monthly targets. If it were to come in monthly, we would have expected \$5.5 million more YTD so it is something of a wild card in forecasting.

2. FY 2015 Revenues - The Transportation Fund - The Transportation Fund is \$1 million, or just over 1%, above YTD targets. A slight shortfall in gas tax revenue is offset by ups in purchase and use tax, diesel tax, and fees.

3. FY 2015 Revenues - The Education Fund - The Education Fund is up \$500,000, or just less than 1%, above forecast. Sales tax and purchase and use tax overages make up for lottery receipts being 19%, or \$1.2 million, below target. Lottery receipts are irregular as to the month they are received so it is premature to worry about any fall off.

4. FY 2016 Budget Gap. Using the existing revenue estimates, we currently project a budget gap of approximately \$100 million. If FY 2015 revenue receipts continue to come in below expectations, the forecast change is likely to result in reduced FY 2016 projected revenue. This would lead to the budget gap being larger. The key budget pressures include: reliance on one-time resources; retirement and retiree health care obligations; Pay Act costs and roll out of last year's increases and employee health care costs; Human Service demands, including Medicaid, and reductions in federal health care funding (FMAP and ACA-related reductions); Education Finance funding; Debt Service; ongoing technology funding needs, and the need to strengthen reserves. We expect to have a document outlining the gap at the meeting.

5. Medicaid - The FY 2016 Medicaid funding need makes up approximately 35% of the budget gap and will need to be addressed. These pressures include decreased revenues including: decreased tobacco funds of \$4.5 million; a base FMAP funding reduction and the partial phase out of the ACA bump totaling \$21 million. Increased spending demands including the second half of Exchange operation funding estimated at \$5.3 million; added caseload and utilization of \$14 million. There is revenue offset from New Adult FMAP funds estimated at \$10.3 million. There is no assumed increase in provider payments; ACO payments or Blueprint funding.

6. Education Outlook - Mark Perrault, Deb Brighton, and the Secretary of Education are completing their financial analysis to enable the Commissioner of Taxes to write her annual letter regarding the Education Fund financing needs and subsequent tax rates. At present, early estimates indicate that the shortfall could result in 4 or more cents added to the statewide tax rate. Overall, education spending is projected to increase by about 3.9%. A large share of the increase is due to pre-K costs being much higher than anticipated. When the Legislature made the eligibility for pre-K services portable, this dramatically increased usage. Mark Perrault will provide more information on this in the weeks ahead as the numbers solidify.

7. Health Care Economic Analysis - As we move to increase capacity to understand the economic impact of health care reform, the Administration and our office are expanding the current capacity of the REMI model. REMI is designed to model economic impacts of major economic changes. The added capacity, called REMI Tax-PI, is a new tool for evaluating the total fiscal and economic effects of tax policy changes. As proposals take shape, for changes in taxes as an alternative to pay for health care, this modeling gives us the capacity to understand the tax fiscal impacts. Tom Kavet and Joyce Manchester are the two consultants/staff who are leading the JFO work on the REMI model. Sara Teachout is also involved. Jeff Carr represents the Administration. The impact of health care finance analysis looms large on our capacity to do other fiscal work.

8. Below Market Leases – Chittenden Unit for Special Investigations (CUSI) lease and below market leases generally - Last session the Legislature passed language in section E.112

of the Appropriations Bill (Act 179), specifically allowing continuation of a below market lease for the Chittenden SIU. As Commissioner Obuchowski updated this lease, he identified and brought to our attention that 29 V.S.A. § 165(h), which governs leasing of property for less than market value, has not been historically followed. The provision was put in place in 1995. It was originally passed as part of the Capital bill - 1995, No. 185 (Adj. Sess.), § 43.

29 V.S.A. § 165(h) governs leasing of property for less than market value. Subdivision (1) allows leases by the Commissioner of BGS for less than market value for periods of up to three years to municipalities, nonprofit organizations, school districts, or to persons whose proposed activities are determined by the Commissioner to serve a public purpose. Below market leases beyond three years, or renewals of existing leases, can only be made with the approval of the Joint Fiscal Committee under 29 V.S.A. § 165(h)(2). As a result of this provision, the Commissioner is carrying out three activities:

- First, BGS staff is identifying and inventorying all below market leases that are in place. BGS is also identifying and inventorying other arrangements through which non-State entities occupy State-owned space at below market rates.
- Second, since recognizing the JFC approval requirement, no new below market leases or extensions have been approved or negotiated.
- Third, the provision and inventory of leases will be brought to the Institutions Committees with any suggestions. The changes might propose notice rather than approval, or possibly involve a process similar to the current grant approval process.

9. Livable Wage Estimates - The Committee will be asked at the November meeting to review changes to the basic needs report methodology. Sara Teachout and Dan Dickerson have been meeting with advocates and others to discuss changes to the existing methodology. There will be some small technical changes as well as a change due to the advent of the ACA for Committee consideration. A separate memorandum will be distributed outlining these issues.

10. Joint Fiscal Office Updates

- **Nathan Lavery:** As you know, Nathan Lavery has left us for the wilds of the Burlington School District. He is the Finance Director for the schools and is responsible for developing its budget. Given the time of year, we are replacing him, in part with Dan Dickerson who has been working with Sara Teachout and, in part with other staff who will be taking on additional responsibilities. We may also contract for assistance in some of the areas he covered, such as Results First. We will assess our need and plan for a longer term solution at the end of the session.
- **Special Education/Paraprofessional Use Contract** – The contract with the UMass Donahue Institute (UMDI) is under way and a major statewide survey is about to occur. Several site visits have been scheduled concurrent with the survey. With the survey being sent to school districts, their awareness of JFO/AOE and UMDI work on reviewing the use of paraprofessionals should increase. The Secretary of Education and her staff have been part of this research effort and will be supportive participants.

- **Health Care Incidence Study** – The RAND Corporation team is working on the health incidence study. We expect a draft toward the end of November. We have been communicating with the Administration to increase the likelihood that it build its proposal on the RAND analysis. After considerable discussion and some review of the numbers, the Administration has agreed to use RAND’s work in health care spending trend analysis from 2012 to 2017. We also expect that RAND work on case studies and impact analysis will be used by the Administration as it presents its analysis of the impacts of Green Mountain Care. The Joint Fiscal Staff continues to participate in weekly phone calls with RAND staff to ensure that data needs are met and coordinated to the extent that can be done.
- **The State House Security Contract** – The contractor has finished a preliminary first draft of the State House Security needs. The Lt. Governor chairs the Committee and will determine the release protocols for the document. For the staff, Catherine Benham is coordinating this project with Rebecca Wasserman of Legislative Council.
- **Kavet, Kappel, and Brighton Contracts have all been renewed for the coming year.** The Kavet contract now runs through September 30, 2015 and was last bid four years ago. Generally, five years is the longest we have gone without a re-bid. The Kappel and Brighton contracts have been extended and as these contracts are small, they are not subject to formal bidding.

11. Summer Study Committee Updates - Several summer studies have begun to meet or have begun to organize.

- **The Special Investigative Unit Study Committee** – This committee began to meet on July 24 and will have its final meeting on December 12th. A draft report is being prepared.
- **ANR Pilot Study** – A study of the formula used by PVR to calculate ANR’s annual payment-in-lieu of taxes is being coordinated by Stephanie Barrett. A draft is being developed for the working group which should go out later this week. Stephanie has led this effort.
- **Renter Rebate Report** – Mark Perrault continues to work with the Vermont Housing Council, the Department of Taxes, and the Agency of Commerce and Community Development on a report of how to develop programs to assist renters in lieu of the current renter rebate program, per 32 V.S.A. § 6066(b). The report also calls for recommendations to make the existing program more effective.

A technical error in the Renter Rebate Education Fund appropriation occurred in the budget that was sent to the Governor and became Act 179 of 2014. A late change of the conference committee which adding back \$1.4 million was correct in the conference report but did not get carried in the version that the Governor signed. This could be addressed in the FY 2015 budget adjustment or through Emergency Board action.