Joint Fiscal Office

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MEMORANDUM

To: Representative Janet Ancel, Chair,
Senator Ann Cummings, Vice Chair,
Senator Jane Kitchel
Representative Kitty Toll,
Members of the Joint Fiscal Committee

From: Stephen Klein, Chief Fiscal Officer

Date: July 18, 2017

Subject: July 2017 – Fiscal Officers' Report

What follows is an update of recent developments, some of which will be on the agenda for the July 21 meeting of the Joint Fiscal Committee.

1. FY2017 Revenues Preliminary Closeout

The closeout process for FY 2017 was relatively slow given changes in leadership at various levels of government. The revenue report or schedule 2 of 4:00 PM on July 14 is not the final one and the Office just received the Department of Financial Regulation's (DFR) final figures of FY 2017 receipts available to the General Fund, which are stronger than anticipated.

- **The General Fund**: On a preliminary basis, before direct applications and reversions, the General Fund is $1.2 million over target. With direct applications and reversions, the General Fund is $10.3 over target.
  - Extra receipts from the Secretary of State Fund, Abandoned Property and DFR (more later), offset shortfalls in Attorney General Settlements.
- **The Transportation Fund**: off $3.3 million or just over 1% below forecasts, primarily due to diesel tax and DMV fees being off targets.
- **The Education Fund**: down $900,000, or just under 1/2% below forecast. Lottery receipts were $900,000 over forecast, offsetting roughly $1.9 million in sales tax revenue shortfalls.

The General Fund closeout is the sum of several substantial deviations from expectations. The largest are:

- Personal Income tax revenues were off $13.8 million or 1.8% from forecast. Paid returns were lower and refunds were higher than projected. Withholding taxes were stronger than estimated.

- Sales tax receipts were 1.4% below estimates, which reflects the continuing erosion in receipts. Tom Kavet will talk about this but it could be in part due to changing purchasing as Vermont's demographic changes continue to impact revenues.

- Finally we received a substantial increase in the DFR's direct application receipts above anticipated revenue. In total, the transfer was $31.4 million, which was about $8.7 million above expectations.

    - Roughly $4.3 million of this amount was due to increases in our broker dealer and investment advisor fees. This was a fee increase passed as part of the 2016 fee bill. Assuming the market stays strong, this is expected to be an ongoing source of revenue and is likely to result in a proposed upward adjustment in the FY 2018 budget of about $3.5 million.

    - $3 million is additional receipts from the regulatory insurance fund which are a combination of the retaliatory portion license fees and other producer and appointment fees. These are every-other-year receipts and will not increase FY 2018 expectations.

    - The remainder is a variety of smaller increases, including one-time payments and reduced expenditures.

    - FY 2017 receipts can help with FY 2018 and we will have an expectation of $3.5 million in receipts for FY 2018 and future years.

2. FY 2018

FY 2018 revenues are still being finalized by Tom Kavet and Jeff Carr. The revenue adjustment will consist of two components from the estimator's analysis.

First there is the onetime "above trend" corporate tax refunds. This is estimated at about $16.3 million. This allowed for $15 million in onetime funds to offset this known likelihood.[1] With the potential for FY 2017 surpluses, this onetime need could potentially be reduced.

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[1] Sec. D.105 FISCAL YEAR 2018 ONE-TIME CORPORATE TAX REFUND OFFSET

(a) The Administration and Legislative economists have indicated that one-time corporate tax refunds may result in a revenue downgrade for fiscal year 2018. To address the one-time fiscal impacts of this in fiscal year 2018, the following actions are authorized:

Second, there may be an ongoing base reduction due to weakness in Sales taxes and income taxes. To the extent that this is a small number…less than $10 million, this may be in part, offset by the $3.5 million in extra ongoing receipts from securities fees. For this reason the level or need for any rescission is unknown and will become clear by Friday.

Preliminary indications show a downgrade of $11,680,000 net of corporate refunds. This includes the projected increase from the tax changes made last session.

3. Medicaid Trending

The Medicaid expenditures ended FY 2017 slightly better than budgeted projections. We were able to add funds to the Caseload Reserve, above initial expectations and there may be some reduction in Medicaid pressure for FY 2018. Stephanie Barrett is finalizing the Medicaid report which will be discussed at the meeting.

4. Integrated Eligibility and the Exchange

Dan Smith has updated his review of the Integrated Eligibility system and points out that there has been a period of reevaluation in system development. The Agency of Human Services is in the process of reviewing its approach and expects to have a new plan in place shortly. This fall's reenrollment for the exchange will be a shorter period than last year and run from November 15th to December 31st. Details on how this will unfold could be presented at a later Committee meeting.

5. Federal Health Care and Budget Reductions

While the Agency of Human Services has done some initial analysis of the potential impact of the House Health Care bill proposal on Vermont, the Administration

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(1) As part of the official revenue forecast for fiscal year 2018 under 32 V.S.A § 305a, the Emergency Board at its July 2017 meeting shall hear testimony from the Administration and Legislative economists and adopt a fiscal year 2018 estimate for expected corporate tax refunds above historical trend.

(2) Based on the adopted amount of corporate income tax refunds under subdivision (1) of this subsection, to the extent necessary the following offsets will be made in the order below:

(A) The Commissioner of Finance and Management may review fund balances in State special funds and end of fiscal year 2017 carry forward appropriation balances throughout the Executive Branch. Up to $5,000,000 may be identified for transfer or reversion to the General Fund. To the extent necessary, the Emergency Board will review any proposed fund transfers and under its authority pursuant to 32 V.S.A. § 133(b) make fund transfers at a meeting scheduled on or before September 15, 2017.

(B) Up to $10,000,000 of the Global Commitment Fund balance may be transferred to the General Fund.

(b) Any other revenue adjustments shall be made in accordance with end of the year revenue offsets and the statutory rescission process under 32 V.S.A. § 704.

and the Joint Fiscal Office have been waiting until clarity exists for a more detailed analysis. As you know, the Senate health care bill has not moved forward. The President's budget proposal is also being reworked in Congress so we are holding back from analysis at this point.

6. Proposed Education Health Care Savings

The Agency of Education has begun the process of determining the allocation of the health care savings to supervisory unions and school districts. This needs to be done by August 15th.

A number of technical issues have emerged, including among others, how technical centers are treated, and how positions supported by non-State funds are accounted for. For example, where health care is paid for from federal funding, it is not clear whether the "savings" can be taken in the same way as would be the case with Education Fund positions. The legislation was silent on the treatment of non-State funded positions. Finally the allocation formula for the savings has yet to be determined.

7. State Employees and Teachers' Retirement Funds

- FY 2017 retirement funds investment returns have exceed estimates. Through May, with one month to go, returns were about 10%. With June performance being relatively strong, it is expected that full-year returns for the systems will be 10% or greater.
- Last week the assumed rate of return for the retirement system was reduced from 7.9% to 7.5%. This lower return will increase the funding obligations on an annual basis but better reflects the likelihood of lower investment returns in future years.
- This summer's actuary work will take these factors into account. In addition, they will reflect what have been increased retirements in the teachers' system and other factors.

8. Studies

- **The Minimum Wage Study Committee:** The final appointments were made late last week but not all of them have been notified. We are starting the polling process of the Committee members to set a first meeting. This Committee has five meetings and was initially scheduled to start on or before July 15th. Joyce Manchester recently did an issue brief on two studies of the Seattle minimum wage increase experience at: http://www.leg.state.vt.us/jfo/issue_briefs_and_memos/Issue_Brief_Two_Minimum_Wage_Studies.pdf
- We have not yet begun the TIF study which will probably start in August. We expect to have Sara's replacement at that point.

9. Staff updates

- **Administration:**

- Adam Greshin has taken over as Commissioner of the Department of Finance and Management.
- Emily Byrne has left as Budget Director and is replacing Bill Talbot at the Agency of Education.
- The new Deputy Commissioner of the Department of Finance and Management should be appointed shortly.
- Rebecca Sameroff at the Department of Taxes will be taking a three-month leave of absence for the remainder of July into October.

- **Joint Fiscal Office**
    - Sara Teachout has moved to BlueCross BlueShield of Vermont as Director of Government, Public and Media Relations.
    - We have hired Graham Campbell as Sara's replacement and he will start on August 7th. He is a recent Master's graduate in Economics and Public Policy from the Public Affairs program at the Woodrow Wilson School at Princeton University. He has some work experience in economic analysis at the Bank of Canada, and some summer and in-school experience with the International Monetary Fund, the Federal Reserve Bank of New York, and a planning project for the Port Authority of New York and New Jersey. We expect to have Graham at the meeting. We are delighted to have him and expect him to be a valuable asset to the staff.
    - Chloe Wexler has been working at the Joint Fiscal Office to build capacity to meet education finance needs when Deb Brighton retires.