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Beyond Belt-Tightening

by Jack Hoffman

If the administration and the Legislature stick to the fiscal policy they have followed in recent years, Vermonters will be forced to forgo more than $100 million in government services next year.

The administration is in the early stages of developing the fiscal 2010 budget—covering July 2009 through June 2010—which will be presented to the Legislature in January. Based on the latest estimates and current obligations, there is a gap of at least $102 million between expected revenues and the cost of providing existing services (**Figure 1**).

Figure 1. The Budget Gap for Fiscal 2010

General Fund*	$42 million
Medicaid	$38-48 million
Low-Income Heat Energy Assistance Program (LIHEAP)	$20 million
Teacher's retirement (statutory funding requirement)	$2-10 million
TOTAL	$102-120 million

* Assumes a 3 percent inflationary increase over 2009.

If Montpelier continues as it has in the past few years, policy makers will "manage to the money"—that is, cut services to bring spending in line with available revenues, rather than figure out how to raise the money needed to meet obligations for current services.

The public won't know the details of these decisions until the budget reaches the Legislature at the start of the next session. But one thing is certain: $100 million is not the kind of gap that can be closed with a little "belt-tightening."

The administration just proposed a package of spending reductions to close a $32 million gap in the current fiscal year budget. If they insist on cutting their way out of the state's budget problems, they will need to find three times as many cuts for fiscal 2010.

General fund

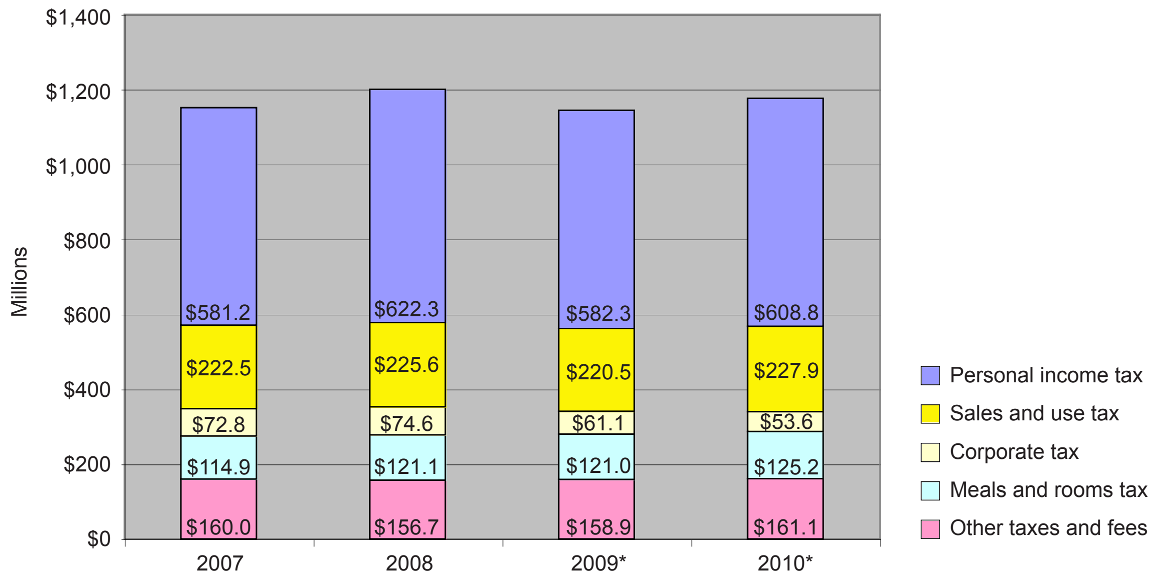
The most recent projections, released in late July, show that the state is likely to take in less revenue in 2010 than it did last year, fiscal 2008. The revenue forecast was lowered in January, lowered further in April, and lowered even further in July. People who work closely with the state budget predict the estimate will be lowered again in November. For now, though, the official forecast is for $1.19 billion in General Fund revenue for 2010.

The biggest drop is forecast for corporate taxes—from $75 million in fiscal 2008 to $54 million in 2010. Income taxes are expected to drop $40 million this year and then rebound some in 2010. But the forecast of $609 million for next year is still below the amount of personal income taxes collected in 2008 (**Figure 2**).

Meanwhile, with even a modest increase, General Fund spending would exceed available revenue. For the last four years, total General Fund appropriations have risen an average of 3.7 percent a year. An increase of just 3 percent would leave the General Fund $42 million short. And that assumes all of the cuts that have been made in this year's budget—putting off computer purchases, restricting out-of-state travel, cutting smoking-cessation programs and the Housing and Conservation Board—can be absorbed again next year.

Even a modest 3 percent increase probably would require additional job cuts in state government and further cuts in services. The current contract for state

Figure 2. General Fund Revenue Change by Major Tax Source, FY2007-FY2010



http://www.publicassets.org/082808U.html

* Projected

Figure 2 shows that Vermont's General Fund revenues are expected to be stagnant from fiscal 2007 through fiscal 2010. The official forecast calls for tax collections to drop in 2009 and recover slightly in 2010, but not back to 2008 levels. Officials in the administration and the Legislature expect the forecast to be lowered even further in November.

employees calls for a 3.5 percent salary increase in fiscal 2010.[1] The pattern in recent years has been to approve pay increases but not all of the funding to pay for them. That has meant that agency and department heads have been forced to use money from other parts of their budgets to cover the pay raises for their employees. In some cases, positions are left unfilled and work is delayed or shifted onto other workers. In other cases, services are delayed or cut back in order to "save" the money needed for pay raises.

Stretched government staffs will affect Vermonters who don't work for the state as well as those who do—for instance, in reduced courthouse hours, less in-home help in assisted living programs, delays in services for home-schoolers, and other disruptions.

Medicaid

For the past few years, Vermont has escaped the expected reckoning on Medicaid funding. But 2010 could be the year it comes due. Vermont shares the cost of Medicaid with the federal government. The split is roughly 60-40, with Vermont paying the smaller share. The projected "Medicaid deficit" is the difference between projected spending for Medicaid and the money that policy makers have designated to cover those costs.

In recent years, the Legislature has relied on one-time state surplus funds to cover the Medicaid deficit, and in fiscal 2004 Vermont got a reprieve when the federal government temporarily increased its match rate. In addition, Vermont has cut back on the amount the state pays providers for treating Medicaid recipients.

There won't be any surplus state funds next year, and Vermont risks losing Medicaid providers if the payments go any lower. Without another windfall from the federal government, which faces a growing deficit of its own, Vermont's Medicaid deficit is forecast to be $38 million to $48 million in 2010. If the state fails to come up with that money, the federal matching share will be lost, as well. The total reduction to Medicaid would be $94 million to $119 million.

The state faces another risk with Medicaid, too. Vermont and Washington no longer share the actual cost of Medicaid services. They are instead splitting the cost of insurance premiums. Until now, Vermont calculated premiums at the end of the year, when the state knew what the Medicaid costs were; that way, the state always covered costs. But that arrangement is over. The state must now set premiums in advance, and the federal government will pay its share. If people need more health care and the money runs out, the state will be on the hook for 100 percent of the excess costs.

LIHEAP

The Low-Income Home Energy Assistance Program is a federal program, but federal funding is not adequate to serve the needs of Vermonters when heating oil costs $4 a gallon. LIHEAP officials estimate that Vermont needs an additional $20 million to provide the same level of protection for vulnerable Vermonters that it did last winter. Even then, the program would only cover 60 percent of a family's annual heating cost.

It's not clear yet where Vermont will get that extra money. Barring a steep and unexpected drop in the price of oil next year, it is safe to assume that Vermont will need to find $20 million to make sure that poor and elderly Vermonters can get through the winter of 2009-2010.

Teachers' retirement

Vermont has been underfunding the teachers' retirement system for more than a decade. A plan to restore full funding was developed in 2006, and the state has made the required contribution in recent years, but the Legislature and the administration have relied on surplus funds and other one-time money to do so. There will be no surplus available for 2010, and, given the state of the economy, the retirement fund's investments can be expected to earn less. That means the state would have to contribute more. We won't know how much until late fall, but the Joint Fiscal Office estimates a figure at $2 million to $10 million above the amount the state is putting into the retirement fund this year.

So far, both legislative leaders and the administration have rejected any consideration of raising revenue to address Vermont's budget problems. One argument they make is that higher gasoline and heating oil prices mean that Vermonters are shelling out $650 million more for fossil fuel energy than they were a year ago.[2] With that extra burden, leaders in Montpelier say, people cannot pay more taxes. The only responsible response to the budget crisis, they insist, is to reduce government spending.

But that response does not take into account the additional cost that will be shifted onto Vermonters as a result of cutbacks in government services. Whether they have to buy new tires and struts after negotiating poorly maintained roads, pay higher premiums and copays for health insurance, or wait longer for their day in court, Vermonters will bear the cost of many of the services that government no longer will deliver. And unlike taxes, which are more likely to be tied to income and ability to pay, costs that result from cuts in government services fall most heavily on those who can least afford them.

ENDNOTES

1 Joint Fiscal Office, Act 206 of 2007-2008 session of the Vermont General Assembly.

2 Estimate provided by the Regulatory Assistance Project, Montpelier, based on Energy Information Agency data.

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