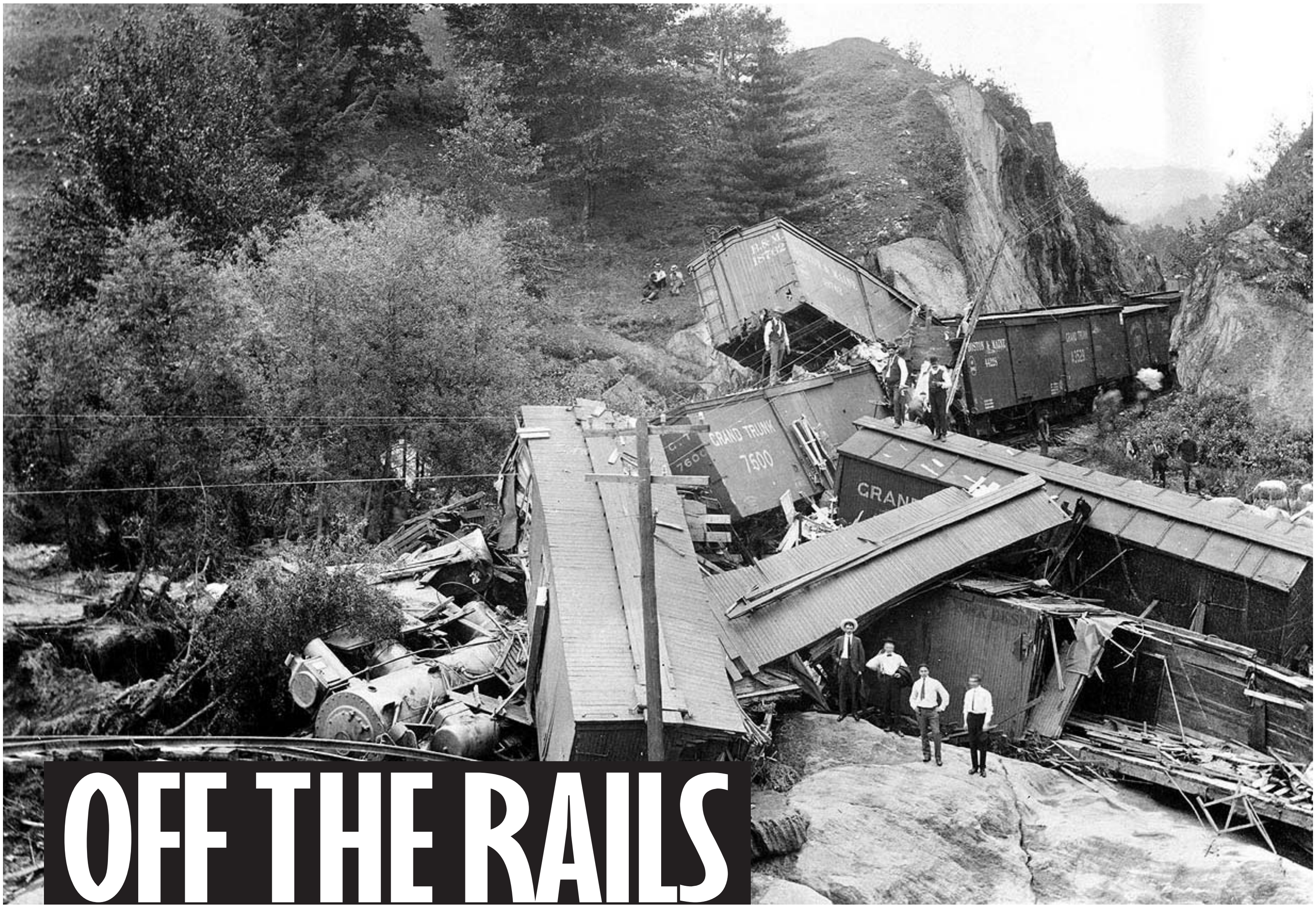

OFF THE RAILS

Changing Demographics, Changing Economics, Accumulating Obligations:

How Will Vermont Cope with a Challenging Future?

OCTOBER 2008

An Ethan Allen Institute Report

Cover photo: Train wreck in Middlesex, Vermont, 1902,
courtesy of the Vermont Historical Society.

This report is an expanded version of *Off the Rails* released in December 2006.

The longer report upon which much of this report is based, Richard W. Heaps and Arthur G. Woolf, “Demographic Changes and Their Fiscal Consequences in Vermont”, was prepared under contract by Northern Economic Consulting, Inc. of Westford, Vermont. That report, including a lengthy appendix on research methodology, can be found on the Ethan Allen Institute’s web site, www.ethanallen.org under “Reports”.

Valuable input on Vermont’s social service programs was performed on contract by Bethany Knight, Northern Knights Consulting, Glover, Vermont.

The members of the Project Advisory Committee listed on the inside back cover contributed valuable insights and editorial suggestions. They do not necessarily endorse all of the recommendations appearing on pages 12-14.

John McClaughry, President of the Ethan Allen Institute, prepared the drafts and edited the final report.

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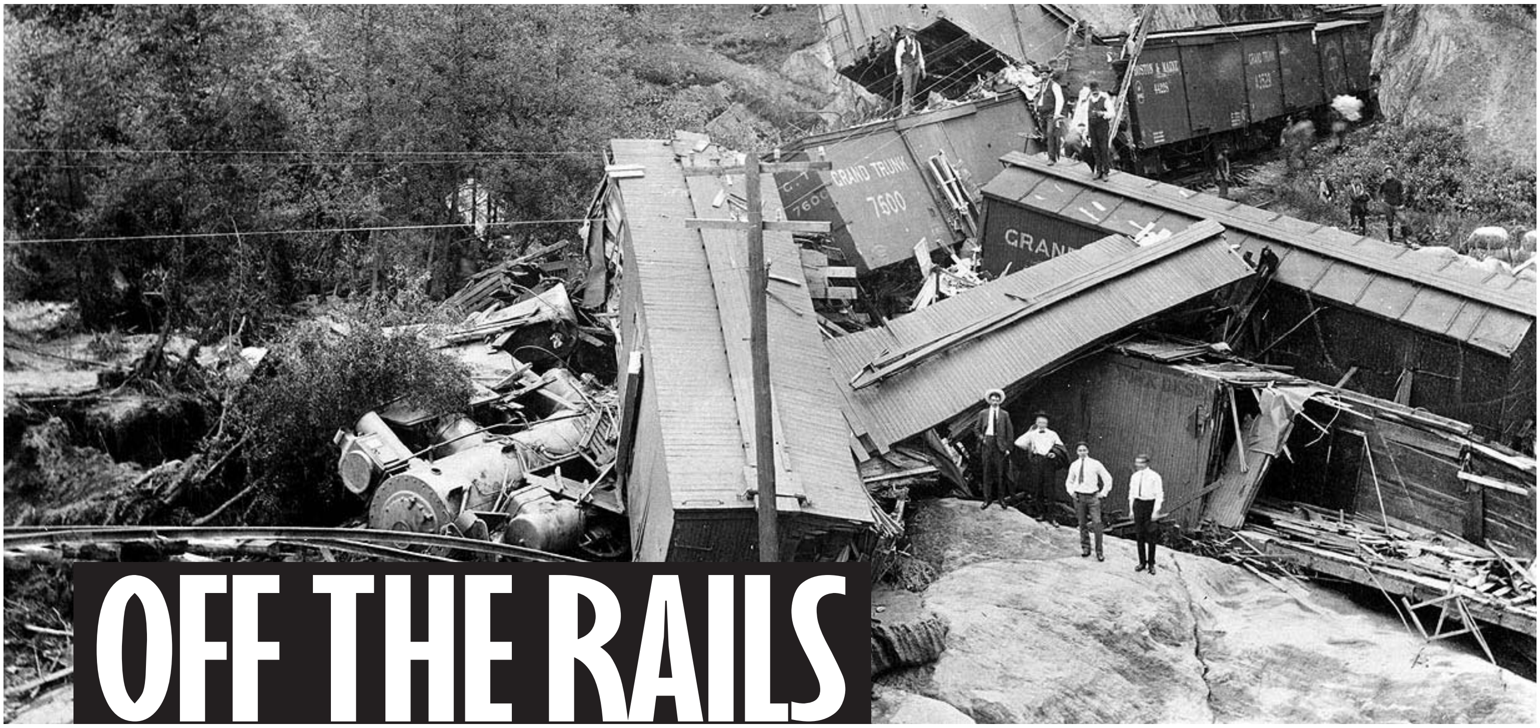


OFF THE RAILS

Changing Demographics, Changing Economics, Accumulating Obligations: How Will Vermont Cope with a Challenging Future?

CONTENTS

OFF THE RAILS

Executive Summary

Until the 2008 economic downturn, and despite high property taxes, Vermont in recent years has experienced good times.

But a long-range analysis of projected demographic trends and their economic implications suggests that Vermont may be steadily heading off the rails.

Vermont's population is getting older. It is already the nation's second-oldest state measured by median age. More of its young people are seeking opportunity elsewhere. The proportion of active wealth producers is declining.

But Vermont's high level of public service spending – especially on public education and human services – is requiring ever-greater tax revenues. There is little reason to believe that over the next 25 years Vermont's taxpayers will be willing and able to pay enough to support the state's spending habits.

By 2030, even if Vermonters are willing to devote an all time high of 18 percent of their adjusted gross incomes to state and local taxes, more than two thirds of all tax dollars collected will be needed just to pay for public education. Almost all of the remaining tax dollars will be required to fund human service programs. And that assumes there will be no new spending programs, like universal preschools or universal taxpayer-financed health care.

The good news is that this problem is not beyond our control.

We can slow the growth of spending for both public K-12 education and human services. We can also create a much more favorable climate for investment, entrepreneurial opportunity, and economic growth. That will increase incomes, enlarge the revenue base, and reduce the rising tax burden.

Increasing tax rates in an attempt to increase government revenues is not a viable option. That would propel Vermont from seventh place to first place in state and local tax burden (measured by total tax revenues/AGI). Such a tax burden would doom the state's efforts to stimulate wealth producing economic growth.

Keeping Vermont on the rails will require transforming Vermont into a state more attractive for productive young Vermonters to stay and work in, and for productive workers from outside the state to migrate into.

This will require changing the state's tax and regulatory policies. It will require improving its educational and work force quality, strengthening its institutions of post-secondary education, and expanding its telecommunications system. It will also require maintaining the high quality of the state's health care system and protecting its environmental amenities.

Those steps would make Vermont more attractive to existing businesses and to new firms that base their enterprise on highly educated, skilled, high-salaried workers.

A conscious decision to implement such policies will take vision and political courage.

It will mean creating a much more favorable climate for investment, entrepreneurial opportunity, and economic growth, and resisting the political temptation to pick and subsidize favored enterprises.

It will mean putting limits on the state government's role as the provider of tax-funded benefits to an increasing proportion of the state's population.

But if Vermont's government and economy are to stay on the rails for our children's generation, there seems to be no other viable choice. We do not have decades to get this right.

Introduction

As little as two years ago (2006), both the state's economy and its fiscal health appeared to be on track.

Vermont's unemployment rate was 3.6 percent, the lowest in New England.

Tax revenues from Vermont's economy were coming in at or above projections.

The FY 2007 general fund budget closed in the black.

Nationally, the economy had been expanding for five years. Federal tax revenues were well above projections. The federal deficit was shrinking.

In October 2006 the Dow Jones Industrials hit their all time high. Retail gasoline prices had dropped 25 percent since the beginning of that year.

In December 2006 it was easy to believe that, despite high property taxes, and many unmet social needs, our state was experiencing good times.

But a long-range analysis of Vermont's future - its demographic trends and their economic implications - suggests that those good times are not likely to last. Vermont may well be slowly but steadily heading off the rails.

As the national economy sagged toward a standstill in 2008, the likelihood of Vermont heading more quickly off the rails steadily increased.

Vermont's demography is changing. Its population is getting older. The proportion of active wealth producers is declining, as more older people live on the fruits of their past activities, and more young people seek economic opportunity elsewhere.

Vermont is the second-oldest state in the union (after Maine). Barring rather dramatic changes, beginning in 2013 there will be a steady drop-off in the number of Vermonters in the 21-64 year age bracket, the prime working years. That means that there will be fewer workers to support our population of children and the non-working disabled and elderly.

Over the past 40 years the people of Vermont have approved public policies that have created expectations of a very high level of public services and benefits, relative to those in other states. Since 1966 responsibility for providing those services and benefits – notably social welfare, health care, and education – have come to be dramatically centralized in the State.

The methods that state government has adopted to meet these obligations have been based on the expectation of a dependably growing revenue base that will be able to meet fiscal needs.

At the same time, Vermont’s legislatures have also put in place policies and regulations that strongly influence economic activity, wealth production, and the use of land and natural resources.

These demographic changes raise the important question: Can the state of Vermont find the revenue it needs to meet its assumed obligations, from a population where active wealth producers are a steadily declining fraction?

If not, what combination of changes should be made in public policy to keep Vermont eco-nomically strong and fiscally viable, whether by

- reversing the demographic trend
- creating the conditions that will generate more tax-producing economic activity
- increasing the tax burden well above current levels
- changing the obligations assumed by the state, and thus the associated costs
- achieving significant efficiencies that will allow the state government to meet its current obli-gations at lower cost
- some combination of the above

Part I of this Report examines the coming demographic changes facing the state.

Part II examines the likely future for the state's economy and fiscal position, consistent with the demographic projections.

Part III examines policies that might be adopted to cope with the coming challenges. It offers a broad-brush conclusion about the most promising path to take to make sure that Vermont's government – and its economy – stay on the rails.

Part IV offers some specific recommendations.

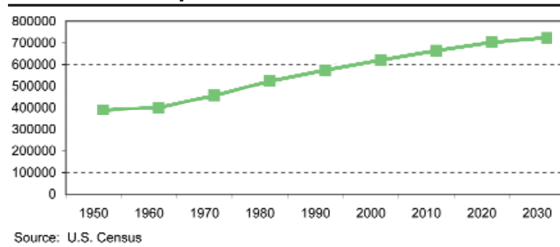
This report strongly concludes that the present mix of demography, economy, and public obligations is not likely to produce desirable results twenty-five years from now.

If wise policy makers do not begin now to create and implement a better model for Vermont's future, our state could, like the train on the cover, go off the rails.

I. Coming Demographic Changes

Vermont's population growth rate is steadily slowing down.

Vermont Population 1950-2030
U.S. Census History and Forecast



The Census Bureau's most recent population projection for Vermont (April 2005) assumes that recent demographic trends will continue into the future.

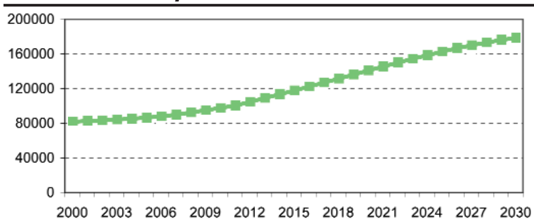
The most noticeable trend in the projection is the slowing rate of population growth expected for Vermont. While growth from 1960 to 1990 exceeded 10 percent per decade, the growth slowed to 8 percent from 1990 to 2000. From 2000 to 2010 growth is projected to slow to 7 percent, then to 6 percent in the following decade, then to just 3 percent from 2020 to 2030.

In absolute numbers, Vermont added 67,000 residents in the 1960s but is projected to add just 21,000 from 2020 to 2030.

This growth will not be uniform for all age groups. The Baby Boom generation will begin to retire in this decade, and swell the ranks of the elderly in the next.

In 2004 81,000 Vermonters were 65 and older, 13 percent of the population. In 2014 this age group will increase to 109,000 or 16 percent. Then in 2024 this group soars to 154,000, or 22 percent of the total. By 2030 there will be 174,000 seniors, 24 percent of the population. From 2005 to 2030 older people will account for all of Vermont's population growth.

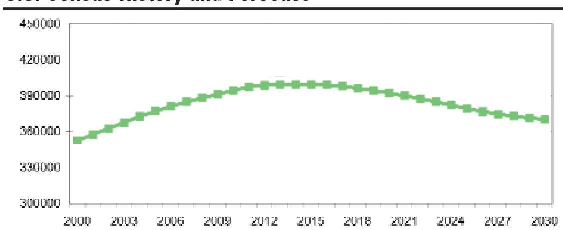
Vermont Population Projection Age 65 and Over
U.S. Census History and Forecast



Source: U.S. Census

Now look at the projection for the working age population, aged 21-64.

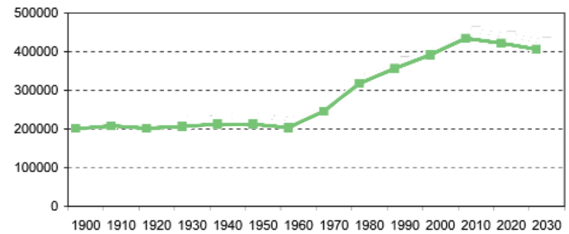
Vermont Population Projection Ages 21-64
U.S. Census History and Forecast



Source: U.S. Census

This is a dramatic change from recent demographic trends in the U.S. Historically, the working age population has steadily grown, helping to expand the economy and generate wealth and pay taxes for the support of families and public programs.

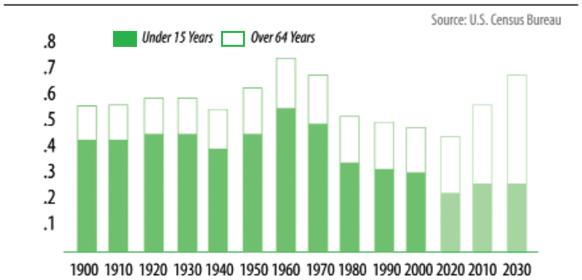
Vermont Working Age Population 1900-2030
U.S. Census History and Forecast



Since 1960 the working age population grew dramatically, but by 2014 the working age population will start decreasing, and by 2030 it will have fallen by 7 percent from its 2014 peak.

The "dependency ratio" is the number of non-working young and old divided by the working age population. Here is the dependency ratio for Vermont from 1900 to the projected level in 2030.

Vermont Dependency Ratio 1900-2030



In 1960 the large number of Baby Boomers had pushed the dependency ratio up to 74 dependents per 100 workers. As these children moved into the work force and had smaller families than their parents, the dependency ratio falls to a projected 44 dependents per 100 workers in 2010. Then the ratio will climb with retirement of the Baby Boomers. By 2030 there will be 67 dependents per 100 workers, or only 1.5 workers for every dependent.

Unlike the 1960s, the high dependency ratio of 2030 will indicate not large numbers of children, but a very large number of seniors. This will pose a serious problem. **How will state government raise the revenues needed to pay for public programs?**

To sum up: Barring significant and unexpected changes, **Vermont's population growth will level off. The population will continue to get older. There will be a relative shortage of people of working age. That diminished group – and their employers – will have to shoulder ever-higher burdens of taxation to support Vermont's generous public service expenditures.**

II. Economic and Fiscal Implications

Vermont will soon face a doubling of its over-65 population, a decline in the working age population, and a decline in the number of young people under age 20. This has important implications for its tax base.

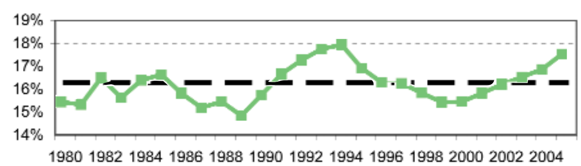
Vermont's state and local governments depend on revenues from three major sources: income taxes, property taxes, and consumption taxes (sales, rooms and meals, liquor, tobacco, etc.). These taxes are based on the income earned and the money spent by Vermonters.

The coming years of slow growth, and then the decline, in the proportion of working age Vermonters will diminish the growth of income and spending. Spending by affluent retirees and tourists will offset some of this shortfall, but not eliminate it.

It is clear that as the number of senior citizens grows and the number of workers decline, there will be a significant reduction in the growth rate of total income earned by Vermonters. Since the ultimate source of tax revenue collected by state and local governments is peoples' ability to pay their taxes – that is, their incomes – **tax revenues will grow much more slowly in the future than in the past.**

Over the past two decades Vermonters have paid between 14.9 percent and 18.0 percent of their Adjusted Gross Income (AGI) in state and local tax payments. In 2006 the Vermont tax burden (17.7 percent) was the seventh highest of any state. The average for that period was 16.2 percent, shown by the dashed line in the graph below. That percentage is assumed to be the level at which Vermonters will allow themselves to be taxed over the next 25 years.

Vermont State and Local Tax Revenues
As Share of Adjusted Gross Income



This methodology suggests that beginning about 2015 the labor force will go into decline. That will even further reduce the growth in tax revenues. **This slowdown in revenue growth is one of the most important impacts of the demographic changes that Vermont governments will face.**

In the past, tax revenues have grown for two reasons. One is the tax revenue per working person. As productivity and real wages rise, so do taxes per worker. The second is the growth in the numbers of working Vermonters.

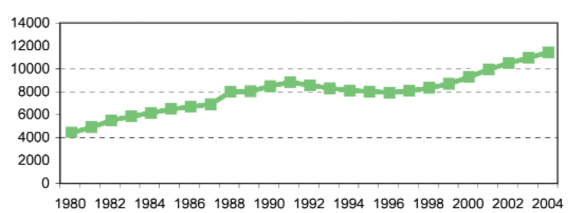
When the number of working Vermonters stops rising, this second component of tax revenue growth will also stop rising. **The leveling off of this component of tax revenue growth will become a major constraint on governments in the decades to come.**

Governments spend most of their revenues in three areas: education, human services (including health care), and transportation. Transportation spending is relatively insensitive to the state's changing demographics and will not be addressed here.

School Enrollments and Education Spending

In the 1996 school year state and local governments spent $940 million (in 2005 dollars) to pay for educating 105,600 K-12 pupils. By 2005 the school population had decreased by 7,200, but spending had increased to more than $1.2 billion, a 27 percent increase in constant dollars.

Vermont Real Per Pupil Spending

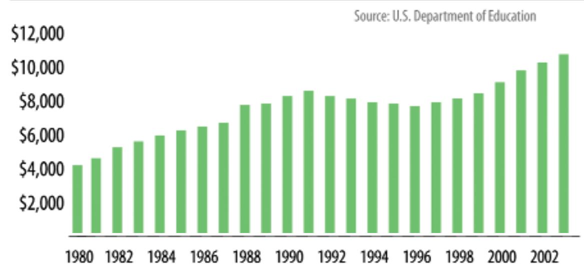


Updated with 2003-04 school spending data from U.S. Dept. of Education. These are in 2005 dollars (as are all OTR numbers).

In school year 2006 the number of pupils declined to 96,600. Over the next decade there will be a further decline of 12 percent. Although school population is predicted to rise again after 2015, in 2030 the number of children attending Vermont's public schools will still be less than in 2000.

From 1992 to 1996 the spending per pupil declined slightly, because the level of state aid was

Vermont Spending Per Pupil in Inflation-Adjusted Dollars

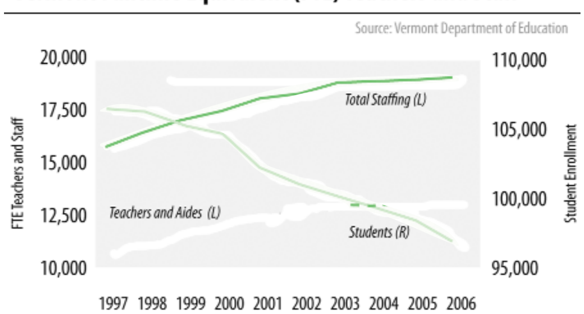


essentially constant and local voters were not willing to increase their property taxes to spend more on schools. But beginning in 1997, Act 60 centralized control of education finance at the state level. From then on spending per pupil has risen steadily in inflation-adjusted dollars.

Over seventy percent of school spending is the salaries and benefits of school employees, principally teachers. Over the same 10-year period the state's public schools added 1,179 more teachers. The pupil-teacher ratio has decreased until by 2006 it stood at 10.9 to one, the second lowest in the nation.

The combination of rising public school staff levels and falling pupil enrollments is by far the major reason why inflation adjusted per pupil spending has risen by 44%, from $8,900 in 1996 to $12,800 in 2005.

Vermont Fulltime Equivalent (FTE) Teachers and Staff

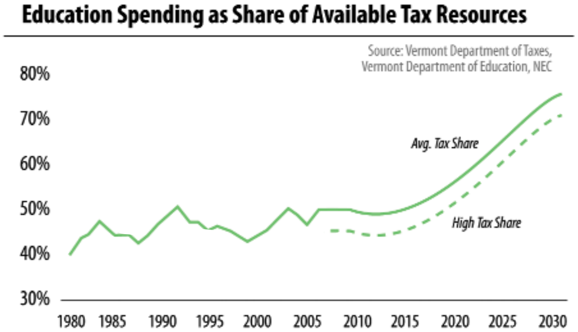


In 1997 there were 10,857 Full Time Equivalent (FTE) teachers and aides in Vermont's public schools. In school year 2006 there were 13,105, a 20 percent increase while the number of students fell by 9 percent. The number of non-teaching employees, which includes aides, administrators, counselors, nurses, librarians, clerical staff and maintenance personnel, rose from 4,926 to 5,964 over the same period, a 21 percent increase.

Historically, from 1980 to 2003 the annual increase in real per pupil spending averaged 3.9 percent. Assuming that rate continues into the future, by 2030 total education spending will be $2.8 billion in 2005 inflation adjusted dollars. There will be 5,000 fewer students enrolled in the public schools than there are today. **This will produce, in 2005 dollars, spending per pupil of $33,400.**

With education spending growing even though the student population is shrinking, education will absorb an increasing share of the slowly growing tax revenues available to Vermont governments, state and local. The graph below shows two scenarios for the share of state and local tax revenues that will be needed to fund public K-12 education.

Education Spending as Share of Available Tax Resources



The first scenario (solid line) assumes that Vermonters will accept an overall tax burden of 16.2 percent of their adjusted gross incomes, Vermont's historical average tax burden. The second scenario (dashed line) assumes that Vermonters will accept a tax burden at the highest end of the range, at 18 percent of AGI.

If Vermonters agree to pay taxes at their average rate of 16.2 percent of their Adjusted Gross Incomes, education spending will absorb 50 percent of those tax revenues through about 2015. After that year the share steadily increases. This is caused by the slowdown in income growth coupled with a reversal of the long decline in the student count. **By 2030 nearly 75 cents out of every tax dollar will be spent on public education.**

The dashed line shows that even if Vermonters are willing to spend 18 percent of AGI in taxes, by 2030 more than two thirds of all tax dollars will be needed to fund education.

This estimate does not include the additional costs that would be incurred by expanding the public school system by two more grades, to include preschool for 3- and 4-year-olds. Such an expansion, authorized by the legislature in 2007, may cost as much as $70 million more per year.

Under either scenario, Vermonters will have serious problems funding education. **The growing share of taxes devoted to education spending will severely constrain the ability of Vermont governments to spend money on all other functions**, including health care, transportation, conservation, environmental protection, housing, community development, corrections, public safety, and the general administration of government.

Given the anticipated demographic changes coming in the next 25 years, this startling consumption of tax revenues by the K-12 school system will force either sharply increased taxes – mainly property taxes – or draconian cutbacks in other areas of government spending.

Human Services Spending

Over the years Vermont state government has assumed many and varied obligations for "human services." This term includes temporary assistance for needy families (TANF); Medicaid; mental health, substance abuse and developmental disability services, vocational rehabilitation, and corrections.

Taken together, in FY2007 these services will consume $469 million, 41 percent of the overall general fund budget of the state.

Medicaid is a matching program (59 percent federal, 41 percent state) that pays for medical services for the poor, through a state-run Managed Care Organization (the current name for a Health Maintenance Organization).

Beginning in 1995 the expanded Medicaid program (Vermont Health Access Plan – VHAP) extended very broad medical coverage not only to "traditional" Medicaid families (low income, aged, blind and disabled), but also to many of the working poor and middle class. It came to include children from families earning three hundred percent of the federal poverty level (for a family of four, $60,000 in 2006). The Clinton administration turned down Gov. Dean's application to include their parents as well.

In 1986 Medicaid covered 39,000 people and spent $25.8 million in state funds. By 1995 it served 81,000 people and spent $104 million in state funds. In 2005 it served 145,847 people with a broad range of services, and spent a total of $309 million in state funds.

The fraction of Vermont's under-65 population served by Medicaid has now risen to 19 percent, making Vermont the third most Medicaid-intensive state in the nation, 46 percent over the national average.

In addition to its medical services program, Medicaid also offers development disability services, personal care services, and mental health and substance abuse services. These services are offered by ten state-funded nonprofit "Designated Agencies" and four nonprofit "Special Service Agencies". The spending through these agencies grew at the rate of 9.3 percent a year between FY1998 and FY2004, almost three times the rate of general fund growth. These agencies obtain about 85 percent of their revenues from government programs.

The Agency of Human Services determines financial eligibility for means tested programs. The Designated Agency then determines, for each eligible client, what services are to be provided, by which providers, in what intensity, and of what duration. The structure of these programs creates a steady pressure to expand the state's financial obligations.

In 2005 the Douglas administration negotiated a first-in-the-nation "Global Commitment" waiver from the federal government. By its terms the federal government agreed to participate in Medicaid spending up to a cap of $4.7 billion over the five fiscal years 2007-2011. In return the state was given wide latitude to change program requirements and use anticipated savings to increase services or expand served populations.

The October 2006 projections for Medicaid predicted an $11 million shortfall in FY2008, increasing to a cumulative program deficit of as much as $279 million by the end of FY2011. If state Medicaid expenditures break through the

Global Commitment cap, state taxpayers will then be responsible for paying 100 percent of the excess costs.

Currently a relatively small share of human services spending goes to the over-65 population, so the growth of that part of the population ought not impose significant new costs to the state.

The major concern with human services spending is its overall rate of growth, not the amount spent on the growing over-65 population. Constant dollar human services spending have grown at a historical rate of 2.4 percent per year. One quarter of that growth is due to population growth, and three quarters is due to increased spending per person served. This spending growth may slow as the state's population growth slows, but a reasonable projection is that growth in spending per person will continue at this historical rate.

The Combined Effect of Education and Human Services Spending

The graph below shows what happens when the best estimates of income growth, per pupil spending growth, and per capita human services growth are combined.

Today education and human services absorb about two thirds of total tax revenues collected by state and local governments in Vermont. That share will stay relatively constant for the next decade. By 2020 it will rise to 77 cents of every dollar collected in taxes by state and local governments. By 2025 88 cents out of every dollar will be spent on for education and human services. **By 2030 virtually all taxes raised by all governments in Vermont will be needed to fund spending for education and human services.**

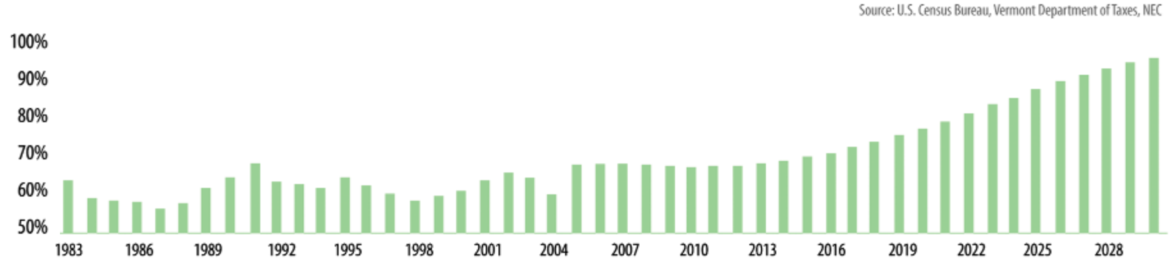
The Political Economy of Demographics and Spending

There are good reasons to believe that the mismatch between economic growth and government spending may well be even more serious than shown.

The state's population appears to be growing more slowly than the Census Bureau's population projection numbers. All of this slowdown appears to be caused by a reduction in the number of young people. These young people are the productive workers of the near future, so this slowdown in tax revenue growth may occur sooner than these projections show.

Further, older people are much more likely to vote than young people. As seniors come to be an increasingly large share of voters in future years, they are likely to ask their representatives for

Vermont Education and Human Services Spending as a Share of Total State and Local Taxes



more services or reduced taxes or both. If legislators vote for more services to seniors, spending pressures will increase. If they vote for targeted tax relief, tax revenue growth will fall below the projections shown above. Either of these outcomes will make Vermont's fiscal situation even more bleak than the projections show.

III. General Policies for Coping with the Coming Challenge

There are several possible ways of dealing with this challenge.

- **Slow the growth of spending for public K-12 education.** Education spending has been rising so rapidly that, even though there will be fewer pupils to education in coming years, education by itself will nearly overwhelm the taxing capacity of the state.

- **Slow the growth of human services spending.** Much of this spending comes from the increasing number of people who are receiving taxpayer-supported health care and other such services. If the state continues to pay for health care for an increasingly large share of the state's population, it will only exacerbate the demographically induced fiscal problems the state will face in the future.

- **Increase taxation to increase government revenues.** If Vermonters are unwilling to constrain government spending on public education and human services, and if Congress does not choose to increase its contribution to these expenditures, the only remaining option is to increase tax rates on incomes, sales, and property.

  In 2004 Vermont ranked fifth in the nation in state and local tax burden on individuals and businesses (tax revenues/AGI). If Vermont's tax burden had been at that year's national average, Vermonters would have had $227 million more in disposable income.

  Increasing taxes only slightly would propel Vermont into having the highest tax burden of any of the 50 states.

  This would be likely to have a severe counterproductive impact on Vermont's economy. In any case, such a sharp tax increase would likely be an unacceptable proposition for increasingly hard-pressed Vermont taxpayers.

- **Increase the growth rate of average worker income.** Income growth per worker might be higher in the future than it has been over the past 25 years. However the magnitude of income growth needed to generate the tax revenues that will be needed to fund the projected cost of services is much larger than any conceivable increase based on worker productivity growth. Raising the growth rate of income productivity per worker is not a feasible solution.

- **Change the underlying demographics of the state.** The present demographic trend will soon make Vermont the state with the nation's highest proportion of senior citizens.

  If Vermont were transformed into a state more attractive for productive young Vermonters to stay and work in, and for productive workers from outside the state to migrate into, this trend could reverse.

  This would obviously require changing the state's tax and regulatory policies. It would require improving its educational and work force quality, strengthening its institutions of postsecondary education, and expanding its telecommunications system. It would also require maintaining the high quality of the state's health care system and protecting its environmental amenities.

Those steps would make Vermont more attractive to existing businesses and to new firms that base their enterprise on highly educated, skilled, high-salaried workers.

A conscious decision to implement such policies will take vision and political courage.

It will mean creating a much more favorable climate for investment, entrepreneurial opportunity, and economic growth, and resisting the political temptation to pick and subsidize favored enterprises.

It will mean putting limits on the state government's role as provider of tax-funded benefits to an increasing proportion of the state's population.

But if Vermont's government and economy are to stay on the rails for our children's generation, there seems to be no other viable choice. **We do not have decades to get this right.**

IV. Specific Recommendations for the 2009 General Assembly

To put Vermont back on the rails, this report has shown that it is imperative that our policy makers

- Slow the growth of spending for public preK-12 education
- Slow the growth of human services spending, including medical care, mental health programs, and corrections,
- Make the state a more congenial place for businesses to create and retain high-income jobs
- Make state and local governments as cost-efficient as possible

Without purporting to be an exhaustive list, here are some important specific recommendations for the 2009 governor and legislature. The recommendations focus on improving the climate for employment and wealth production that can be taxed at reasonable rates to produce the revenues to meet the state's long-term fiscal obligations. They do not address such important issues as education finance and property taxes, tourism, agriculture and forestry, higher education, law enforcement and non-economic issues in general.

A. General

1. The Governor, working with legislative leaders and others, should develop and implement a long-range (25-year) strategic fiscal and operational plan for matching state revenues and spending programs, taking into account the imperative points noted above.

2. The legislature should require annual reports by the Governor describing how well the state did in the previous fiscal year to comply with or amend the strategic plan, naming specific legislative or executive action that threatens compliance.

3. The Governor, with legislative support, should initiate a PERM (Privatize, Eliminate, Retain, Modify) review of all operations of state government, pioneered in Michigan in 1993.

4. The legislature should require fiscal impact statements to accompany all legislation that would increase Vermont's long-range revenue and spending.

5. The legislature and Governor together should commit to resist all proposals to create new or enlarged spending programs that would worsen the long-range fiscal problem facing the state.

B. Taxation

1. The Governor and legislature should commit to a policy of balanced budgets without increasing tax rates or enacting new taxes, whether overt or disguised. The fiscal discipline imposed by a statutory or constitutional tax limitation amendment would be a useful manifestation of that commitment.

Such limitations typically cap the annual rise of state revenue collections to the sum of the percentage increase in population growth and dollar depreciation (inflation). Any excess in revenues over that amount is returned to the taxpayers through rebates or lower tax rates. A tax limitation amendment usually requires a referendum vote of the people to approve any increase in the rates of major taxes (income, sales and use, meals and rooms, state property taxes, etc.)

2. The one possible exception to a tax limitation rule would be increased motor fuel tax rates to finance the maintenance and improvement of our deteriorating highway infrastructure, unless some altogether new method of financing is devised. However, the legislature should decline to increase motor fuel taxes until the diverted one-third of the vehicle purchase and use tax is returned to the Transportation Fund.

3. The legislature should in particular refuse to increase the individual or corporate income tax rates that are a major determinant of a state's economic climate. The present panoply of tax rates has made Vermont No. 1 among the states in tax burden (total tax revenues as a percent of personal income.) Every effort to increase tax rates to finance more government, especially in an economic slowdown, is seen by business as an ominous indication of the orientation of the state's political leadership.

4. The legislature should adopt technical correction provisions that expand the definition of non-taxable equipment used in manufacturing, and require valuation of equipment purchases at the actual price paid.

C. Regulation

1. The legislature should affirm its commitment to the protection of the constitutional right to private property ownership, including the payment of just compensation when rights in property are taken for the use of the public.

2. The legislature should revise Act 250 and related environmental permit criteria to, among other things:

- Provide that the public benefit of well-designed employment- and wealth-expanding development can be considered in determining the overall public good, even if the development would entail diminishing some general environmental values

- Exempt from regulation any wetland that is less than one acre in size, or not attached to a waterway, or is manmade

- Exempt applicants from responsibility for identifying and protecting putative ancient burial grounds and aboriginal campsites

- Exempt applicants from meeting historic structure preservation criteria unless the municipality specifically endorses preservation

- Exempt applicants from endangered species criteria unless the species in question exists nowhere else but in the vicinity of the proposed project

- Provide that use for value-added manufacturing presumptively outweighs the preservation of forest and agricultural soils and the restrictions on "scattered development"

- Require compliance with the esthetics criterion only when the esthetics of the project are objected to by the local government or its planning commission

- Prohibit the practice of requiring applicants to buy their permit by making a cash contribution to a government-designated beneficiary

- Change Act 250's Criterion 10 to require compliance with duly adopted zoning bylaws rather than imprecise and visionary local and regional plans.

In addition, the law should require district commissions to accept state agency and local zoning permits as determinative unless a party can show that they are arbitrary, based on serious errors of fact, or fraudulent.

3. The legislature should require that approval by an Act 250 district commission of a blanket plan for a long-term project is final, unless the Governor certifies in writing that a drastic change of circumstances requires amending the plan in the public interest.

4. DEC permits for projects requiring stormwater management should be issued on a standard of admissible effects on the human population, rather than on the largely speculative "health" of aquatic biota.

5. The legislature should amend state law and employee contracts to provide that arbitrary regulatory and enforcement action against businesses, overt hostility toward persons engaging in economic activity beneficial to the people of this state, and unreasonable and costly delays by state regulatory agency employees are just cause for termination of employment.

6. When a civil service employee attempts to impose onerous conditions as his or her price for signing off on permit applications, the law should allow the applicant to demand that a commissioner appointed by the Governor and confirmed by the Senate personally endorse the imposition of such conditions in writing (as now practiced by Fish & Wildlife).

7. The legislature should adopt a regulatory accountability act, by which one fifth of the members of the House or Senate can force a floor vote to approve or disapprove any agency rule or pending proposal for a rule.

D. Health Care

1. The state should pay the full cost of the health care services it requires medical providers (hospitals, doctors, dentists, nursing homes, etc.) to provide to persons enrolled in state health care programs like Medicaid, VHAP, and Catamount Health. This would end the cost shift that is a major factor in driving up the cost of private health insurance.

2. The legislature should repeal insurance laws that have driven out private insurers; specifically, community rating and guaranteed issue.

3. The legislature should allow insurance carriers to offer affordable low-mandate catastrophic coverage policies aimed at young people.

4. The legislature should create a high-risk pool, as 30 other states have done, to cover uninsurable individuals and transients, up to a limit of one percent of the population. The pool should be financed by beneficiary premiums, assessments on insurers, and appropriations.

5. The legislature should tighten the workers compensation law to make it more difficult for workers to game the system with imaginary work-related injuries, and the Governor should see that the appeals board is composed of individuals committed to fair play regardless of the relative economic positions of the parties.

E. Energy

1. The legislature should vote to approve a 20-year extension of the NRC operating license for Vermont Yankee, the state's low cost electricity producer.

2. The legislature should decline to adopt any new preferential deals, including renewable portfolio mandates, for favored energy producers (notably wind and solar) that would increase the cost of electricity to ratepayers.

3. The state should continue to provide useful energy conservation information to businesses, farms and homeowners, but the legislature should not increase energy taxes to pay for creation of a new or expanded energy efficiency utility.

4. The legislature should reject proposals to install a carbon emissions cap-and-trade plan, whereby electricity ratepayers are taxed to finance subsidies to favored energy producers.

5. The state should relax regulatory and environmental requirements to facilitate the badly needed expansion of electrical transmission capacity.

F. Housing

1. The legislature should reform the tort law to protect building owners, particularly rental housing owners, from costly lawsuits and enormous judgments for relatively minor or speculative causes.

2. The legislature should resist the temptation to insist that new housing be constructed only in designated village centers, and that every development contain "affordable housing" cross-subsidized by other homes.

Project Advisory Group

Participants in the project advisory group agree that the issues presented in this report deserve wide discussion and eventual changes in public policies. They do not necessarily endorse every observation made, or any specific policy prescription flowing from this analysis. Their affiliations are listed for identification only.

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An Ethan Allen Institute Report

The Ethan Allen Institute, founded in 1993, is Vermont's independent, nonpartisan, free-market public policy research and education organization – a "think tank" for issues facing Vermonters.

The Mission of the Institute is to influence public policy in Vermont by helping its people to better understand and put into practice the fundamentals of a free society: individual liberty, private property, competitive free enterprise, limited and frugal government, strong local communities, personal responsibility, and expanded opportunity for human endeavor.

The Institute's areas of interest include

- Vermont's economic future, particularly the vitality and diversity of its competitive free enterprise sector.
- The fiscal practices and condition of state government – taxation, spending, and borrowing.
- State and local regulatory practices, and their effect on the economy and the rights of the people.
- Better education for all Vermont children, and an efficient, accessible health care system, each based on the principles of personal responsibility, competition, and empowered consumer choice.
- The preservation of free, accountable, democratic government, where public decisions are made at the level as close as possible to the people themselves.
- Adherence to Vermont's basic charter of government, the Constitution.
- The strengthening of Vermont community and family life, and the protection of local government from burdensome and costly mandates. The Institute advances these ideas through print and radio commentaries, publications, newsletters, conferences, debates, and public dinners and meetings.

The Institute is supported by the annual contributions of over 600 Vermonters. It is governed by an 11-member Board of Directors and has a 17-member Advisory Council. The Institute is a 501(c)(3) educational organization, contributions to which are tax deductible for individuals and corporations. The basic annual membership is $50.

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