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Countdown to Aug. 2: State prepares for federal funding crisis; D.C. standoff resumes

By Peter Hirschfeld, Vermont Press Bureau

MONTPELIER — The state of Vermont is due to receive about \$150 million from the federal government next month. So what happens if the check never comes?

Programs and services administered by state government rely nearly as much on federal funds as they do on state-level contributions. And as Congress nears the debt-ceiling precipice, officials here are beginning to prepare for a potential disruption in the flow of federal money from Washington, D.C.

"Last week I sent out an email instructing our agencies and departments to draw down all the federal funds we are entitled to by the close of business this Friday," says Finance Commissioner James Reardon.

In the short term at least, according to state Treasurer Beth Pearce, Vermont should be able to forestall any ill effects that may stem from a debt-ceiling impasse. Vermont's share of federal Medicaid money — which accounts for a full third of the \$150 million the state anticipates receiving from the feds next month — will arrive on Aug. 1, a day before the federal government would begin to consider which bills not to pay.

In the short term at least, Pearce says, Vermont's treasury is robust enough to cover the rest.

"We are doing contingency planning around our cash flows, and we feel very confident that if there is a stoppage of federal payments we can manage that on a short-term and intermediate basis," Pearce says.

She says the state's fully funded stabilization reserve — known as the Rainy Day fund — will further insulate the state against having to resort to short-term borrowing to make up for the possible loss of federal money.

But a prolonged stalemate in D.C. could eventually exact a more substantial toll on government-funded services. Just about every government function relies in part on federal money. It's impossible however to know precisely how a government default would impact Vermont, Reardon says.

"The problem is that I don't know what the priority of their payments would be," Reardon says. "And without that information, I just can't predict what kind of position we'd find ourselves in."

Line items in which federal funding has a direct hand — which include everything from paving projects on local roads to Social Security checks for elderly residents — aren't the

only areas of potential hardship. Vermont's triple-A credit rating is also at stake, Pearce says.

Vermont's bonds are considered very low-risk investments, which means the state enjoys very low-interest rates when it comes time to borrow. If the federal government's credit rating drops, however — and it will, if it defaults on its loans — then the downgrade would have a domino effect nationwide. Vermont's AAA rating is so resilient, according to a recent Moody's analysis, that it could withstand a minimal drop in the federal rating. If the federal rating goes down two levels, however, Vermont would see a corresponding downgrade.

Vermont will look to borrow up to \$90 million on the bond market this fall. If the state lost its impeccable rating, and interest rates went up one-half a percentage point, Vermont could be on the hook for an additional \$4.6 million annually in interest payments.

"If there is more risk by virtue of a downgrade ... investors want to be compensated for that additional risk," Pearce says. "It would be regrettable that we would lose our rating after all the hard work Vermonters have done to achieve that rating due to inaction at federal level."

Pearce says residents too would experience an increase in the cost of borrowing. Interest rates on everything from mortgages to car loans to student loans would spike in the event of a government default.

"Education loans are particularly a problem, given that almost every (federal budget) scenario has a reduction in Pell grants for students," Pearce says. "It means you're limiting Vermont students' access to grants for school, and also creating a high cost of financing for student loans."

Reardon says he hopes all the angst-ridden preparation is, in the end, for naught.

"We'll have to see how this plays out," Reardon says. "At this point, we're hoping there's no disruption to providers or recipients of services and programs."

Meanwhile, in Washington, D.C., this morning, the standoff resumed.

A Senate Democrat told the Associated Press that House Speaker John Boehner's failure to get fellow Republicans to back his debt limit bill dramatizes the folly of a "go-it-alone" approach to the financial crisis.

Colorado's Michael Bennet tells CBS's "The Early Show" Boehner's decision to cancel a vote Thursday night on the GOP proposal leaves Senate Democrats and Republicans as the last hope to find a compromise bill. The nation's borrowing authority expires Tuesday, Aug. 2, in the absence of a law renewing the government's borrowing authority.

Bennet says he's "enormously disappointed" with political gridlock, asserting "there's a reason the poll ratings of Congress are in the basement."

He says he's against a temporary extension in the debt limit, arguing that would only allow Congress to postpone the kinds of tough decisions it must eventually make.

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