



SENATE OF VIRGINIA

Senate Finance Committee

John H. Chichester **Senate Retreat** **Thursday, November 16, 2006**

Once again, let me welcome each of you to the Senate's annual retreat. A strong turnout always is gratifying, but that is particularly the case in a year when much has been asked of you already. Your willingness to "hit the road" yet again and give up two more days is a real testament to your fortitude and commitment.

Hopefully, you view these sessions as I do – as an opportunity to get "grounded" in what is to come. The dialogue that we have on emerging trends and policy responses to those trends can only improve the way we govern.

Let me highlight a few of our topics.

First, we have asked Dr. John Petersen, a nationally recognized expert on public finance to share a presentation that he made in August at the National Conference of State Legislatures. Dr. Petersen's observations are in the context of change – how state public finance has changed over time and how those changes may translate into future benefits or challenges to public policy.

Next, we will turn to the annual staff review of Virginia's revenue and budget outlook for the upcoming session. You will not be surprised to find that we have improved the structural balance of Virginia's budget through responsible actions we have taken in recent years. And, this makes our job much easier in the short session.

We went into overtime last session, but when the dust finally settled, we had one of the best two-year budgets that I can remember. For the first time in many years, we passed a **real biennial budget** that recognized all our known obligations and left no large second year "holes" for the short session. The best example of this fiscal discipline was inclusion of salary

increases in both years of the biennial budget for our state and state-supported employees and proper amortization of our fringe benefit costs.

In addition, we were able to include two-year salary increases for local school teachers, albeit a “place holder” in the second year. One of the budget adjustments we will consider in January is the actual amount of that second year increase for teachers. Obviously, other short session budget adjustments will be needed because no crystal ball is perfect.

And that brings me to the final point that I want to make on our first day of deliberations.

We should all take pride in the fact that our budget is structurally sounder than it was a few years ago. We have a budget that largely meets obligations for both years of the biennium. And, we have refilled our Rainy Day Fund in anticipation of the next economic downturn. Most likely that downturn will begin within the next few years, and Virginia will be hit harder than the nation because the economic downturn will coincide with a reduction in defense spending

Virginia is much more dependent on defense spending than other states. Homeland security and defense contracts have substantially buoyed our growth in recent years, and it will be more than a minor blip when the tide turns.

With this in mind, I want you to think back about ten years. We were in the middle of the dot.com bubble, riding high -- sort of like we've felt for the past couple of years. In Virginia, we got a little “heady.” We began enacting a series of tax credits and other tax relief that ultimately totaled about \$1.5 billion a year, when we included local car tax relief. Then, we hit another recession, and you know the rest of the story.

And so, as we revel in our current good fortune and look to the future, I hope that we can learn from the past. You will see clearly from today's presentation that our revenue growth has in fact begun to slow.

But, as an election approaches, we always feel the temptation to “live for the moment.”

I hope that we can resist that temptation. I hope we will remember that the estate tax and other tax relief we passed last session will take \$160 million out of our revenue stream each year in the next biennium. And I hope we will remember that there is “unfinished business” on the budget side. We have not funded all of the SOQ revisions recommended by the Board of Education, and we have not fully phased in higher education base adequacy funding.

And, quite frankly, there is “unfinished business” on the tax side as well. We reduced the sales tax on food by 1 ½ percent a year ago. But, there still is a state food tax of 1 ½ percent. If we feel the overwhelming urge to do something on the tax side, I hope that we will remember this “unfinished business” and try to find a way to address this most basic tax relief.

Now, let’s turn to the afternoon’s agenda. I’d like to first welcome Dr. John Petersen . . .