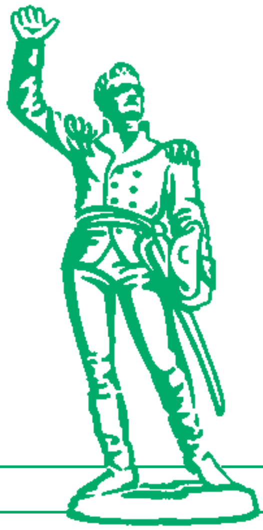
NUMBER 178 JANUARY 2009



The Ethan Allen Letter

IDEAS FOR VERMONT'S FUTURE

A Monthly Publication of The Ethan Allen Institute

INSIDE:

Vermont Democrats Should Embrace Barack Obama's Slogan

COMMENTARY

In July of 1995 William Sorrell, Administration Secretary for Gov. Howard Dean, released a list of 59 "cost-shrinking ideas" for state government, to meet that year's fiscal crunch. The great majority of them proved to be pious hopes unsupported by analysis, schemes for reshuffling bureaucracies, and earnest entreaties to "promote efficiencies". Few if any were ever implemented, but somehow Vermont made it through 1996.

Now, fourteen years later, the Governor and legislators are facing a total of $66 million in General Fund reductions to meet expected revenue shortfalls in Fiscal Year 2009, with upwards of $176 million more necessary for FY 2010.

On December 17 the Joint Fiscal Office released a "master list of reduction ideas", culled from proposals emanating from both the legislature and the administration.

Most of the 140 proposals are predictable: Freeze spending on vehicles and space leases. Impose Reductions in Force (layoffs). Leave vacant positions unfilled. Deplete special funds with unused balances. Reorganize bureaus. Scrap non-productive boards and commissions.. Increase fees, premiums and co-payments. Reduce or eliminate tax exemptions. Plead for more Federal assistance.

Suppose a politically painful but ultimately agreed-to collection of such proposals is adopted by the new legislature. Suppose further that the state can emerge from the hard times, say in 2011, and ride the wave of the Obama economic boom. Then what?

Then as new revenues become available, almost all of next spring's hard-nosed decisions will one by one be reversed. And as soon as the next downturn materializes, governor and legislators will start the same revenue raising and spending reduction exercise that they went through in 1996 and 2009.

There is a way to get off this roller coaster: change the way state government operates. To do that requires investment in a performance review.

Performance review is a careful and deliberate study by knowledgeable and disinterested people of what state government has agreed to do, how it does it, and how what the people want done can be done better and more efficiently. The goal is to balance over the long term the cost of state government's programs and the revenue from taxpayers, without raising taxes that would kill future economic growth.

Performance review has strong bipartisan roots. In Texas Controllers John Sharp (D) and Carole Keeton (R) fed hundreds of cost-saving recommendations to Governors Ann Richards (D) and George W. Bush (R), saving Texas taxpayers billions. Michigan Gov. John Engler (R) was soundly re-elected in 1996 due to the success of his review called PERM, for Privatize, Eliminate, Retain or Modify.

In fact, the Vermont Democratic platform of 2004 pledged that party to conduct a "top-to-bottom 'performance review' of the functions of state government… to find creative, smart new ways to make government

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The Ethan Allen Letter

The Ethan Allen Institute is an independent, non-profit, nonpartisan public policy research and educational organization, incorporated in 1993 under Vermont law.

The Institute sponsors and conducts research on important public policy questions facing the people of Vermont, and makes its findings and recommendations known through various channels to the general public, the news media, and civic leaders at all levels.

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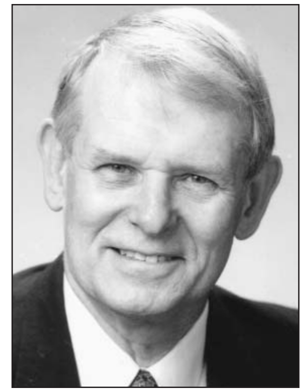
PRESIDENT'S MESSAGE

Have We Gone Bonkers Over Taxes?



Readers may be startled to read "The Only Tax That Needs to be Raised" (p. 4), stating the case for increasing the gas and diesel tax rates. Since when has a limited government, low-tax, free-market institute like EAI joined the tax raisers?

Looking back in our files, I pulled out a commentary entitled "Crash on the Highway" (1/16/96), blasting legislators for raiding the TFund while our highways deteriorate. Another one (8/30/07) called for restoring the diverted third of the purchase and use tax back into the TFund, and exploring Oregon's experimental "pay by the mile" gas tax.

Vermont cannot have a successful economy without a safe, dependable highway system. This is a public responsibility. Since 1923 our policy has been to make highway users pay for that system through a motor fuel tax. Fair enough.

I don't believe I have supported or voted for a tax rate increase in the past 35 years. But this one is different. A safe, dependable highway system is an economic imperative. But over the years we have shortchanged our bridges to the point where even restoring the $20 million a year from the diverted purchase and use tax will not be enough to catch up deferred highway maintenance, and also rehab the 40 Interstate bridges and 157 state highway bridges rated structurally deficient. Highway users who were paying $4.09 a gallon five months ago should be asked to accept an increase from today's $1.64 to $1.69, and they ought to be willing to do so.

As for raising a milk tax, the property tax, the income tax, the capital gains tax, the sales tax, the property transfer tax, the Catamount employer tax, the electric efficiency tax, the heating fuel tax – forget about it.

***Reminder**: Over 200 members have renewed for 2009. Thank you! If you are not among them, please become one of the next hundred!*

Voting Vermont Yankee Off the Island

COMMENTARY

On November 15, Vermont's environmental movement assembled at Vermont Tech for its annual political action conference. This year's motto was "mobilizing the grassroots for healthy, sustainable communities."

The conference-goers absorbed engaging presentations on building innovative root cellars, making better composting systems, and "bringing sustainable local biomass to your community".

But clearly the key issue of the conference was accelerating grassroots political action to force the 2009 legislature to vote the Vermont Yankee nuclear plant off the island. This was evidenced by the three well-attended workshops, totaling three and a half hours, on the subject, presented by the Vermont Public Interest Group (VPIRG) and its antinuclear allies.

Yankee's operating license expires in 2012. Under a law passed in 2006 (Act 160), the legislature authorized itself to settle the question of whether the plant's certificate of public good should be extended beyond that date. A majority of House and Senate can thus vote to shut down Yankee, even if the Nuclear Regulatory Commission finds (as expected) that the plant can be safely operated for another 20 years. No other state has such a law.

The hyperactive – one might say obsessed – anti-nukies absolutely hate the very idea of nuclear energy, here or anywhere except possibly in the sun. They seem to believe that Yankee's electrical output can be replaced by wind turbines, solar cells, and efficiency. It is hard to find any informed energy planner or economist willing to agree to that proposition, at least in the short to medium run.

Ordinarily the Public Service Board issues certificates of public good for the operation of generating plants. The PSB has standards for making such decisions, complex procedures to ensure that all interests are heard, evidentiary rules, and decades of case law to guide its actions.

By contrast, the members of the general assembly have no restrictions whatever on their actions. They will ultimately vote up or down on whether they believe Yankee's continued operation will "promote the general welfare", whatever that may mean. Or whether it will bring them political benefits in their districts.

It is becoming clear in Montpelier, however, that anti-nuclear outrage will not control the issue. The real issue is money.

Entergy, Yankee's owner, is now negotiating with Vermont's two large utilities for a supply contract beyond 2012. If Entergy agrees to continue to sell Yankee's megawatt hours to the utilities at a favorable rate, the anti-nukies will find themselves climbing a very steep hill in their quest to get legislators to simply shut the plant down.

It's not just about the rates paid for power, important as they are to homeowners, businesses, schools, hospitals, and governments. When it bought the plant in 2002, Entergy agreed to a profit sharing provision. If a relicensed Yankee sells electricity above 6.1 cents/kwh, CVPS and Green Mountain Power may reap a windfall of as much as $750 million over a 10-year contract.

How that money would be divided among shareholders, ratepayers and possibly the state itself remains an unsettled question. But the PSB controls rates charged to utility consumers, and it is unlikely to allow all of this windfall to disappear into the pockets of shareholders.

Beyond the potential profit sharing windfall, legislators will also have to take into account Yankee's contribution to the state's coffers. If the plant is forced to close after 2012, most of its 600 employees and contract workers will be out of work. Yankee's current $6 million a year payments to the state, based on power produced, would end.

With the state's 2010 General Fund budget facing a deficit in excess of $100 million, legislators must now focus on some combination of spending cuts and revenue increases. That pressing need will transform the question of "general welfare" into "how much money can Entergy be made to pay for the legislature's permission to continue operating?"

Extorting money from Entergy is a familiar game in Montpelier. In 2003 the legislature shook the company down for $9 million in return for the state's non-objection to increasing the plant's electricity output. Two years later it extracted another $28 million in return for state permission to store its oldest and least radioactive spent fuel rods in dry casks instead of in a water pool.

It's highly likely that in addition to continuing favorable power rates after 2012, the legislative leadership will "ask" Entergy to pay dearly to avoid a political death sentence.

This is not quite the same as a corrupt Governor selling an appointment to a vacant U.S. Senate seat, but it falls under the same broad heading.

The Only Tax That Needs to Be Raised

COMMENTARY

Vermonters, like everyone else, want good roads and safe bridges. At the same time Vermonters, like everyone else, do not want to face higher tax rates, especially in the face of what could be a prolonged recession. Now we have come to the point where these two wants are in serious conflict.

First, examine the condition of Vermont's state highway system. Here are just a few eye openers from data produced by using the objective Federal highway condition standards:

- Twelve hundred long (over 20 foot) bridges on the state and interstate systems are past the age at which preventive rehabilitation will reliably extend their useful life.
- Five hundred of these are classified "structurally deficient".
- Three hundred sixty nine of these bridges are over 50 years old.
- The present fraction of pavement rated "very poor" (21 percent) will increase to 49 percent in just four years.
- One third of highway pavement surfaces are rated "poor", and the fraction will continue to grow if the present level of maintenance spending is not increased.

Reducing this darkening problem requires money. For a while bridge replacement and repaving can be stretched out over more years. But the amount needed to fix the problems increases the longer needed maintenance is stretched out.

The Federal highway fund has just run dry. President-elect Obama has promised to replenish it, but given the rate of federal spending in the last three months, it's not realistic to count on a rescue from Washington. Vermont will have to dig its own way out of its growing highway deterioration problem.

The mainstays of state highway finance – motor fuel taxes – have remained at the present rates since 1997. In 2003 the legislature diverted one third of the 6 percent motor vehicle purchase and use tax, now running around $20 million a year, from the Transportation Fund into the Education Fund to pay for property tax relief.

Since 2004 the sum of motor fuel taxes and purchase and use receipts have declined every year. Auto sales are dropping precipitously. The high gas prices of last summer spurred reduced driving patterns and switching to more fuel-efficient vehicles. Both reduce motor fuel revenues.

Meanwhile since 2004 the inflation cost index for highway construction has run at an annual rate of 10.5 percent, three times the consumer price index.

In 2005 Gov. Douglas proposed to restore the diverted third of the purchase and use tax revenues to the Transportation Fund. That sound proposal succumbed to a wave of opposition. It seems highly unlikely that the incoming legislature, its majority deeply in debt to the education spending lobby, and its minority sensitive to education property taxpayers, will undo the unfortunate tax diversion of 2003.

What about borrowing to fill the highway revenue shortfall, estimated at $4+ billion over the next twenty years assuming low inflation – or as much as twice that if inflation takes off with new Federal money printing?

Long-term borrowing for infrastructure improvements is fiscally responsible – if secured by a dependable revenue stream. Dedicated motor fuel taxes – highway user fees — are our most dependable transportation revenue stream.

Last month Treasurer Jeb Spaulding, a Democrat, courageously proposed a 5 cents per gallon increase in gasoline and diesel taxes, pledged to retire $150 million in new bonds for bridge replacement. A quick start on such bonding would, Spaulding noted, generate badly needed construction jobs in a time of recession.

The Snelling Center for Government's recent survey of Vermont business leaders showed 89 percent in favor of increased highway funding even if it meant a motor fuel tax increase. Even 63 percent of the general public surveyed agreed.

So far Gov. Douglas has been opposed to a motor fuel tax increase. Both he and Spaulding favor restoring the diverted purchase and use tax funds to the Transportation Fund, but both realize that it's not likely to happen. The governor seems to believe that increasing license, registration and other nonfuel fees can be made to solve this problem. It won't.

In early July gasoline prices in Vermont were $4.09 a gallon. Today they have dropped more than half, to $1.64. If there was ever a time to ask motorists to pay another nickel a gallon to improve their likelihood of enjoying a safe and well-maintained highway and bridge system, now is that time.

Gov. Douglas has exhibited a commendable resistance to tax rate increases. This time, however, he ought to join hands with Treasurer Spaulding and jump off the political bridge together – before our real bridges start collapsing.

Transportation Funding Debate: Let's Call a Tax a Tax

"Vermont is currently ranked 42nd in the nation for its bridge conditions. The number of substandard bridges is increasing over time. It is estimated that over the next 10 to 20 years, Vermont needs to spend somewhere between $50 and $110 million more annually to catch up on repairs to deteriorating bridges…My suggestion is a $150 million to $180 million bridge rehabilitation and replacement bonding program, funded by a five cents per gallon assessment on motor fuel distributors.

"The advantages: reduced costs to taxpayers over the long run, putting people to work in the short run, administrative simplicity, and contributions from tourists, and out of state truckers and college students." – Treasurer Jeb Spaulding, *Times-Argus*, 12/14/08.

"Treasurer Jeb Spaulding has commendably offered strong arguments in favor of raising another nickel per gallon on motor fuel to finance bonds for rescuing Vermont's increasingly deteriorating bridges. However I am sorely disappointed at his proposed mechanism for doing that: an "assessment" levied on fuel distributors.

"If we need to raise more money to preserve our highway system – and we clearly do – let's face up to it, and raise the motor fuel taxes. With gasoline down from $4.09 a gallon to $1.91 in only five months, the extra nickel per gallon would bring the cost of gasoline back to what we were happily paying only ten days ago." – EAI President John McClaughry, WDEV 12/17/08.

"[Yesterday] I admitted I was disappointed that Jeb chose to characterize the nickel tax as an 'assessment'. I did so because I am really outraged at people trying to raise taxes while calling them something else. The Democrats in the last legislature tried to levy a "heating fuel savings charge" to fund their prized "thermal efficiency utility". The Vermont Milk Commission wants to impose a 38-50 cents per gallon "assessment" on fluid milk deliveries to groceries.

"Jeb responded to me that reason he calls the nickel a "Motor Vehicle Distributor Infrastructure Assessment" is because he wants to frame the bonds as revenue bonds, not general obligation bonds. That requires convincing the rating agencies that the revenue source supporting the bonds is a new one, not just an increase in an existing tax. The advantage of this approach is that the bonds would not be counted as State debt, would not affect our debt ratios, and would not compete with the rest of the state's capital program.

"That all makes sense. However, I think we ought to call the nickel a gallon what it is, a tax, and that the structuring and language of the bond indenture can be worked out later on once the legislature approves the tax increase." – EAI President John McClaughry, WDEV 12/18/08

"While few people are enthusiastic about new taxes, a large majority supports taxes as part of the [transportation] solution. 89 percent of the business leaders and 63 percent of the general public said they favored a compromise even if it included an equal share from their less favored funding source… A strong majority cited user-related taxes such as gas and diesel taxes rather than income, sales, or property taxes." – *Vermont Roads and Bridges: To Fix or Abandon*, Snelling Center for Government, November 24, 2008.

For more information, see "Vermont Transportation Funding: An Ongoing Dilemma", Joint Fiscal Office, October 2008 (www.leg. state. vt. us./jfo).

Transportation Fund Transfers and Diversions 2003-09

Fiscal Year	GFund>TFund (millions)	TFund> GFund (millions)	P&U tax diversion (millions)
2003	0.0	6.4	
2004	3.4	0.0	
2005	4.7	0.0	28.0
2006	10.0	0.0	26.4
2007	8.0	0.0	27.1
2008	0.0	0.0	28.0
2009	0.0	0.0	29.2
TOTAL	$26.1	$6.4	$138.7

Act 68 of 2003 diverted one-third of the 6 percent motor vehicle purchase and use tax revenues from the TFund to the Ed Fund, beginning in FY 2005. FY09 numbers are projected. JTOC assessments are not counted as transfers. $1.17m is paid annually from the TFund to the Downtown and Trail funds.

NEWS & VIEWS

Coming Event: The 2009 Vermont Economic Outlook Conference will be held Friday, January 9 at the Sheraton Burlington. Featuring Gov. Jim Douglas, EAI Director Dr. Art Woolf and *Washington Post* economic columnist Robert Samuelson. Samuelson is a hard-headed realist who regularly explains the unadulterated facts to some of his more liberal media colleagues. Highly recommended. For reservations: 879-7774, rheaps@vteconomy.com.

Milk Tax Apparently Expires: The Vermont Milk Commission, realizing that their new tax on milk —- coupled with price controls on groceries — faced a lethal reception, apparently put off promoting this positively awful idea until such time as they hope no one will be watching. EAI to VMC: We'll be watching.

A Happy Comparison: Our friends at the Mackinac Center in Michigan hosted John Stossel for their 20th anniversary dinner in Lansing the night before he spoke at our 15th anniversary dinner in Burlington.

Ingham Co. Michigan, home of the state capitol and Michigan State University, has a population of 279,000. Chittenden Co. Vermont has a population of 147,000. Mackinac has a budget of $3 million; EAI's budget is $150,000+/-. Mackinac had 630 guests for their dinner; we had 344. So we think we did pretty well.

Internships Available: The Institute for Humane Studies offers public policy internships for summer 2009 (deadline January 31). Go to their website www.TheIHS.org for full details.

EAI would be pleased to have an intern for a summer 2009 project here in Vermont. If you know a college student who might like such an internship ($1,500 stipend plus project expenses) please encourage that person to apply to IHS by January 31.

Hopeful News from Obama: On the financial crisis: "The answer is not heavy-handed regulations that crush the entrepreneurial spirit and risk taking of American capitalism. That's what's made our economy great. But it is to restore a sense of balance." (CBS 60 Minutes 11/17/08.)

Surprise! "Green Ideas Go Nowhere: Grand environmental plans show little progress in 1 year." *Burlington Free Press* headline (11/23/08). "There is no evidence the state has made substantial progress toward – or will each – the short-term goal set by the governor [and legislature]: reducing greenhouse gas emissions 25 percent below 1990 levels by 2012." Expect to see this story again a year from now.

Vermont's No. 1! This time Vermont is tied (with Idaho) for the nation's lowest per capita carbon-dioxide emissions (US EIA). But that's not good enough for ultra-green Vermont! We need to go from 10 metric tonnes per person per year

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Vermont Democrats Should Embrace Barack Obama's Slogan

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run more efficiently on the resources we have." Unfortunately the Democratic legislature elected that year seems to have forgotten this sound proposal, but it's not too late for them to catch up.

It won't be easy to conduct such a review under the fierce and immediate pressure of huge looming deficits. But it must be done, to prevent the state government from stumbling haphazardly on through the recurring cycle of politically-driven program expansion, increased spending, revenue shortfalls, budget reductions, bottoming out, and then expanding all over again until the next recession.

If the Democratic majority in Montpelier needs leadership guidance, they need look no further than their supreme leader, Barack Obama. In naming his director of the Office of Management and Budget on November 25, the President-elect said:

"In these challenging times, when we are facing both rising deficits and a sinking economy, budget reform is not an option. It is an imperative. We cannot sustain a system that bleeds billions of taxpayer dollars on programs that have outlived their usefulness, or exist solely because of the power of politicians, lobbyists, or interest groups. We simply cannot afford it.

"This isn't about big government or small government. It's about building a smarter government that focuses on what works. That is why I will ask my new team to think anew and act anew to meet our new challenges.... We will go through our federal budget – page by page, line by line – eliminating those programs we don't need, and insisting that those we do operate in a sensible cost-effective way."

What more incentive do Vermont's Democratic legislators need to set in motion a similar review in our state? Perhaps they should make their first act upon returning to the statehouse this week a reaffirmation of their earlier commitment, by wearing buttons reading "Yes We Can!"

Continued From Page 6

NEWS & VIEWS

down to five, or three, or one! Hang the expense! Bring on the taxes, mandates and regulations! Destroy our economy! Nobody's gonna out-Green us! In your face, Idaho.

Vermont Education Spending: "The U.S. average per student expenditure for public elementary and secondary schools in 2007-08 fall enrollment was $9,963. States with the highest per student expenditures were New Jersey ($15,374), New York ($15,286), **Vermont ($14,336)**, Wyoming ($13,967) and Massachusetts ($13,768). Arizona ($5,346), **Utah ($5,734)**, Nevada ($7,133), Mississippi ($7, 175) and Idaho ($7, 305) had the lowest per student expenditures (NEA 12/18/08).

Anyone care to examine how Utah and Vermont schoolchildren compare on the NAEP tests?

The Dooley Premium: The Tax Foundation examined educational spending trends in 18 states whose Supreme Courts mandated education finance "reform". It compared the expected current expenditures per pupil before the judicial mandates, with the actual spending following the mandate (in our case, Act 60).

Of the 18, Vermont was No. 1 in increased spending. By 2004 our per pupil constant dollar spending had risen $3,084 over the pre-Act 60 trend line for the same years. One may consider this as the "Dooley Premium", after Justice John Dooley who authored the (unsigned) opinion in *Brigham v. State*.

Gasoline Taxes, Highway Construction Costs, and Gas Prices

The federal gasoline tax is 18.4¢ per gallon (and 24.4¢ for diesel fuel). The five highest state gas tax rates are CA (43.2¢), CT (42.8¢), NY (40.9¢), IL (40.6¢) and MI (36.2¢). Maine ranks 16th at 29.1¢, MA ranks 27th at 23.5¢, Vermont ranks 38th at 20¢, and NH ranks 39th at 19.6¢. Raising the Vermont gasoline tax rate to 25¢ per gallon would make Vermont rank 21st. Vermont's diesel rate is 26¢ per gallon. (Tax Foundation #56, 10/07)

Over the years 1998-2006 the consumer price index increased at an average rate of 3.0 percent per year. Over the same years the Bureau of Labor Statistics highway construction cost index increased at an average rate of 6.3 percent per year.

The Vermont gasoline tax rate per gallon increased at a rate of 0 percent over those years. Had the gas tax rate kept pace with the highway construction cost index at 6 percent per year, a gas tax of 40¢ per gallon would be needed to provide the revenues for the same amount of paving and bridgework

On December 26 the gas price at the pump nationally (including taxes) dropped to $1.642, a 58-month low. Five months earlier the national average pump price peaked at $4.09 a gallon.

An Introduction to Hansenbabble

"Today I watched a History Channel production on the coming global catastrophe. It began by saying, 'Sea level has risen three feet'. They didn't mention how long it took to rise that much. In fact, sea level has been rising since the last ice age, when it was perhaps 400 feet lower than it is today. For the last few centuries, the rising rate has been an average of 1.6 millimeters per year. But, of course, if they had said, 'Sea level has risen 68 inches in the past thousand years...' that wouldn't even raise an eyebrow.

"The rest of the program was based on the usual, ever popular computer programs of the UN IPCC which predict disaster right around the corner. I have come to refer to all of this as "Hansenbabble" [after Al Gore mentor Dr. James Hansen of NASA].

"Public School teachers are pumping our children full of Hansenbabble every day. The History Channel, The Discovery Channel, and similar TV programs pump out sensationalized science crap and are worshiped by the general public as a fountain of scientific truth. It is a world gone mad.

"Of one thing I am certain: Some years down the road mankind will look back on this point in time and marvel at the mass hysteria that swept over virtually the whole human race. The subject will provide doctoral dissertation subjects for a whole generation of psychology students, and it will take its place in the history books along with the Great Tulip Craze and the Piltdown Man Hoax."

– James Peden, retired atmospheric scientist,
Middlebury (SEPP, 12/21/08)

The Ethan Allen Letter

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January 2009

INSIDE:

MEDIA

St. Johnsbury Caledonian-Record *December 15, 2008*

Forget the Milk Tax Proposal

The [Vermont] milk commission wants to pay dairy farmers a premium for their milk — an admirable goal. The commission, though, wants milk processors and retailers to pay the farmers more money, then eat the cost hike. The idea that government can increase private industry's cost of doing business and not have those increased costs passed along is the legislators' favorite fiction. So far, raising costs without doing harm to anyone is as elusive a goal as a perpetual motion machine or turning seawater into gold…

That's exactly what the milk commission is trying to do and it won't work. The Commission was told their proposal most likely violates the interstate commerce provision of the U.S. Constitution. Senator [Bobby] Starr's response was to say 'we are going to get sued anyway', adding he favored implementing the Vermont premium immediately.

Vermont taxpayers have seen that attitude before, when legislators passed campaign finance laws despite warnings the laws would not survive a constitutional challenge. When the Supreme Court ruled the laws unconstitutional, Vermont taxpayers got stuck paying the winners millions of dollars in legal expenses…

Vermont should make an effort to help farmers any way they can, but not by telling processors and retailers to hand money over to the farmers, then eat the cost.