BLOG | STATE BUDGET

Recommendations to Strengthen the State

NYS Priorities that Promote Recovery, Transparency, Accountability, and Fiscal Stability

January 4, 2022

Governor Kathy Hochul's State of the State address will present her priorities and preview her first Executive Budget, which she will deliver by January 18th. Her budget and policy priorities provide the opportunity to build a strong fiscal future, and to improve transparency and accountability. Wise decisions will bolster New York's continued recovery and reduce future fiscal and programmatic risks. Alternatively, imprudent fiscal management and priorities could set New York on a path to future fiscal instability, risking the State's capacity to serve New Yorkers, including those most in need.

The Fiscal Year 2023 Executive Budget takes on particular significance, being presented amidst improving fiscal conditions, the year after the State enacted significant multi-year spending and tax increases, and during an election year. The fiscal outlook is vastly better than last year, and the State's multi-year budget balance is unprecedented. Tax receipts now exceed pre-pandemic projections, setting the stage for budget negotiations that likely will center on how to allocate plentiful resources without necessarily considering long-term implications. This short-sightedness could be harmful. Future budgets are balanced on the back of federal aid that will end, and the State is still combating the COVID-19 pandemic and a protracted and rocky economic recovery.

In order to have a successful budget, Governor Hochul should prioritize the following ten actions.[1]

Priority #1: Strengthen the fiscal future by staving off a fiscal cliff and saving for the inevitable next recession.

Last January, the State was projecting annual tax receipts shortfalls of $15 billion due to the pandemic and had no assurance that the American Rescue Plan (ARP) would deliver tens of billions of dollars in general fiscal relief and targeted aid. In the year since, tax receipts have improved so much that they are now projected higher than they were pre-pandemic, extraordinary federal aid delivered unprecedented fiscal relief, and the State increased personal income and business taxes.[2]

The infusion of additional State and federal funds is being used to accelerate already high spending growth.[3] Imprudent use of COVID-related federal aids is creating a "fiscal cliff," with approximately $3.5 billion in recurring program spending supported by federal aid in fiscal year 2025 but not thereafter. This year the State should start to identify recurring savings that should grow to $3.5 billion annually by fiscal year 2025 to ensure that drastic service cuts are not required when the federal funds are exhausted.

Furthermore, there inevitably will be a next recession, and the State has long failed to maintain adequate rainy day reserves. While it was commendable that the Midyear Financial Plan Update outlined planned deposits to the Rainy Day Fund and Retiree Health Benefits Trust, the amounts still are insufficient based on receipt losses of prior recessions.[4] Given the strength of receipts to date and the significant spending increases for this and next year already in the financial plan, the State should deposit any receipts above the current projections to these funds. Both are prudent uses of available receipts and build a stronger fiscal future for the State. Also, given the size of the budget increases, other spending priorities should be funded by reallocating planned uses of State funds and federal aid.

Priority #2: Actively manage the massive school aid increase to ensure results for students.

The ARP and other federal COVID aid sources are providing approximately $13 billion in one-time funds for New York's schools. Last year's budget also included unprecedented recurring increases to State school aid spending, especially notable since school aid per pupil in New York State already is double the national average.

To ensure that this massive increase in school aid has the commensurate impact on student learning, the State should use a rigorous performance management process to oversee school aid spending. This should not only monitor how funds are used, but also set goals, monitor results against those goals, and reallocate resources and change programs when results are unsatisfactory. These goals and results should focus on measuring and reversing pandemic-related learning loss, accelerating achievement compared to prior achievement and national benchmarks, and reducing education disparities. Initiatives should be evaluated to identify what works so programs and learning strategies can be either replicated or terminated. With the State on a path to deliver long-litigated spending increases, any future increases should only be targeted to districts, schools, and students with the highest needs.

Priority #3: Stabilize Medicaid and shift toward health system redesign.

The pandemic has highlighted the need for the State's health system to be better prepared and coordinated. To achieve broader, long-term improvements, the State's Medicaid Redesign Team should be reconstituted as a Health System Transformation Team with a mandate to make recommendations to improve healthcare access; affordability for individuals, businesses and the State; quality; and equity. A Health System Transformation Team should identify specific initiatives that improve the effectiveness, efficiency, and equity of public health, primary and acute health care delivery, long term care, and behavioral health.

The Transformation Team also should identify efficiencies and changes to eligibility and program redesign to ensure Medicaid is fiscally sustainable. Immediately prior to the pandemic, the State was undertaking a second round of Medicaid "redesign," engaging the public and stakeholders to identify savings opportunities after significant program spending growth exceeded the budget by billions of dollars. The redesign process was accelerated and then disrupted by the pandemic. Still, persistent issues exist in the Medicaid program, and fiscal issues will continue when temporary federal funding lapses with roughly 1 million new enrollees brought into the program during the pandemic. The State should take steps to improve the program's fiscal stability and outlook by charging the Transformation Team to identify Medicaid efficiencies, program improvements, and savings.[5] Further improvements are still needed in transparency, by bolstering the State's reporting requirements, to coordinate care for the highest-needs enrollees, and to fix the State's global Medicaid spending cap.

Priority #4: Increase budget transparency by publishing a financial plan when the budget is enacted, eliminating gimmickry, restoring oversight, and standardizing accounting.

The State's budget process is mired by inadequate information on proposals' fiscal impacts, transparency, oversight, and accounting standards. Governor Hochul and the Division of the Budget deserve credit for expeditiously releasing an overdue Financial Plan update, an on-time Mid-Year Financial Plan Update, and for working with the Legislature and Comptroller to fulfill Quick Start revenue projections requirements.

The State also should produce a financial plan when the budget is enacted and ensure adequate time and information to evaluate proposals. Current practice is to rush the voting on final budget bills, and for the Governor and Legislature to announce agreement with scant details about the size of the budget, its balance, or multi-year trends. The Governor and Legislature should allow budget bills to age and should release basic financial plan information before and after the budget is enacted. These two actions—which the Governor can commit to without changes in law—would vastly improve transparency in budget negotiations.

The Governor should take additional steps to increase budget accountability and transparency. The State should not obfuscate spending by shifting it off-budget or delaying payments, and should improve oversight by increasing funding to the Authorities Budget Office and restoring procurement powers of the Comptroller's office.[6]

Finally, the State should transition to budgeting and reporting in accordance with Generally Accepted Accounting Principles (GAAP), rather than using a cash basis for budgeting and reporting that leaves the door open to fiscal gimmickry. Basing fiscal management and balancing State Operating Funds in accordance with GAAP on a modified accrual basis would increase the integrity and consistency of the State's financial reporting and decisions, and strengthen its fiscal footing.

Priority #5: Implement data-driven performance management statewide to improve services for New Yorkers.

Governor Hochul will deliver her State of the State address exactly 11 years after her predecessor's inaugural address highlighted the need to measure and manage the performance of State government.[7] That need has yet to be fulfilled. The State has long talked but always balked on using performance management, undercutting its credibility, accountability, and ability to effectively deliver the services New Yorkers fund and deserve.

It is time for New York to heed SAGE advice and implement a statewide performance management system. Such a system would combine managerial action and accountability with key measures of each program's performance — what it costs, how it is delivered, whether it operates efficiently and delivers quality, and its ultimate impact. This would improve operations, show the public how well (or not) its resources are being spent, and increase public accountability and support.

Priority #6: Target and manage economic development activities to ensure the billions spent create and maintain jobs.

The State spends billions of dollars every year on economic development programs, including direct spending and tax expenditures. To ensure this spending delivers results, CBC has long advocated for reforms that would better target and manage economic development activities. Unfortunately, little progress has been made, although Empire State Development did publish a rudimentary database of its spending. Governor Hochul has the opportunity now to make significant improvements.

First, the Executive and Enacted budgets should include a Unified Economic Development Budget (UEDB) that includes the costs of all economic development programs for the coming fiscal year. The UEDB should show the full range of State economic development spending, including tax expenditures, spending at state agencies and authorities, and the value of discounted power offered by the New York Power Authority (NYPA).

Second, the State should improve its reporting of economic development activities in the Database of Economic Development Incentives (also known as the Database of Deals), which currently lacks key information. The Database of Deals should report standardized performance metrics across all programs. Lack of rigorous standard definitions and reporting requirements makes it difficult to compare the results of different types of economic development spending and activities. Standardized measures should include annual program results (such as current jobs compared to jobs when the program began) and compare them to planned performance. Additionally, definitions for job creation and retention should be standardized for all programs, and metrics should differentiate between full-time, part-time, and temporary jobs. For each of the 10 economic regions, the State also should measure broader outcomes, including growth in targeted industries, overall economic growth, and changes in poverty levels. Such reporting and analysis would guide the State toward the best mix of programs and initiatives.

Finally, existing programs—including Regional Economic Development Council spending, film and television subsidies, horse racing industry subsidies, fossil fuel tax breaks, and other targeted programs—should be evaluated to determine how effectively the resources are creating and retaining jobs. A UEDB and improved economic development reporting will make evaluating existing programs much easier.

Priority #7: Ensure the Metropolitan Transportation Authority's (MTA) future stability by increasing the efficiency of its operations and implementing congestion pricing.

The MTA is benefitting from an infusion of federal dollars, but its operating budget has a structural imbalance exceeding $2 billion annually that will emerge when federal aid runs out. In order to stave off future service cuts, tax increases, or extraordinary fare increases, the Governor should vigorously support the MTA to improve the efficiency of its operations, including working with the leaders of its unionized workforce. The MTA can save up to $2.9 billion annually by increasing subway and bus operations and maintenance productivity; increasing bus speeds; reforming how it deploys conductors, including one-person train operation on subways and fare payment modernization on commuter rails; and reducing employee and retiree health spending. In addition, the State should encourage the MTA to continue the practice it adopted in 2009 of increasing fares and tolls biennially to keep up with inflation, and the City to aggressively roll out its discounted Fair Fares program.

Finally, the State should expeditiously implement congestion pricing. The program is expected to generate $1 billion in net annual contributions for the MTA capital plan, which would support $15 billion in investment. Effective implementation of congestion pricing would decrease congestion and emissions, and increase resources for capital investment. It can be done in a fair and sustainable manner that limits unnecessary exemptions and maximizes social benefit. Delays in implementation delay its benefits to congestion, emissions, and mass transit.

Priority #8: Plan and build infrastructure for the future.

The State directly maintains a vast network of roads, bridges, rails, schools, emergency services, and other assets. It also has a critical role in supporting these and other types of assets owned by local governments, public authorities, and private partners. The State spends billions every year on capital projects for those assets and will benefit from extraordinary funding from federal infrastructure legislation.

Unfortunately, the State lacks a comprehensive capital planning process for its assets. Governor Hochul and the Legislature recently made progress, enacting a law to improve reporting of transportation capital asset condition and project progress. But more improvements are needed, including CBC's recommended system for comprehensive capital planning. Prioritizing spending among different transportation modes, infrastructure categories, or service types is difficult. To help, the State should improve its capital planning processes, broadly adopt benefit-cost analysis, better identify needs and resources, plan for maintenance and improvements, and continuously assess the progress of its work. Prioritizing transportation capital planning is a sensible start, as it represents the largest segment of the State's capital program, but a complete approach should be implemented to cover all infrastructure categories.

Each passing year without a comprehensive, long-term capital planning process has a cost, but that is especially true this year with federal infrastructure aid recently approved. Federal funds already make up one-sixth of total capital spending by the State, and the State should identify, allocate, and implement the new federal funds to maximize their benefits.

Priority #9: Increase housing production, housing affordability, and NYCHA's capacity to improve its capital stock and management.

Over the past decade, housing production in New York has lagged job growth and ranks below peers, exacerbating affordability challenges. The State should act to facilitate housing development and affordability, especially downstate. Development proximate to the transit network would increase regional housing supply, help stabilize market prices, and take advantage of recent investments in commuter rail. New York State should follow the examples set by New Jersey, California, Massachusetts, and other states that encourage suburban housing development through a combination of incentives and mandates.

The State should also help improve the New York City Housing Authority (NYCHA) by approving the proposed Preservation Trust, enacting procurement reform, and increasing financial support for Rental Assistance Demonstration (RAD) public-private partnerships that bring in capital and often new management. The Preservation Trust would allow NYCHA to partner with construction management and design firms to bring in new capital resources and oversee renovation of 110,000 public housing units. Procurement reforms would reduce NYCHA's costs by allowing it to use construction manager-build and construction manager-at risk procurement rules. Increasing financial support for RAD conversions at NYCHA by providing tax-exempt bonds and Low Income Housing Tax Credits through the NY Housing Finance Agency and the New York City Housing Development Corporation would facilitate building and unit quality improvements to the benefit of tenants.

Priority #10: Reduce taxes to foster economic competitiveness.

When combined with the New York City and MTA-region taxes, New York State now has the highest top personal income tax rates and top corporate tax rates in the nation. The most recent personal income tax increases made permanent a previous 'temporary' tax hike from 2009 and further raised top rates. This creates two types of fiscal risk. First, it increases the financial incentives for high-income individuals and businesses to relocate or to not move to New York State and City, which is especially important given the impacts of the COVID pandemic and recession on the economy in the near and long term. The most recent federal data show that the State has not added new millionaires at the same rate or amount of other peer states.[8] Second, increased reliance on the personal income tax creates volatility in tax receipts. In the event of a typical recession, the impact to the State's finances will be even greater than past recessions, and (as described above) the State maintains chronically inadequate reserves to accommodate such impacts. Given the State's stronger-than-expected receipts throughout the pandemic, the latest tax increases should be lowered, reversed, or at least allowed to sunset.

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ENDNOTES

1. In addition to the fiscal priorities included in this report, the Citizens Budget Commission also intends to author a report in the near future with recommendations for State budget process reforms to improve fiscal planning, budgeting, transparency, and accountability.
2. New York State Division of the Budget, *2021 Joint Report on Receipts and Disbursements* (November 2021), www.budget.ny.gov/pubs/press/2021/fy23-quickstart/report-fy23-quickstart.pdf.
3. State Operating Funds spending is projected to increase $8.9 billion in fiscal year 2022 and $3.2 billion in fiscal year 2023.These figures represent State Operating Funds Spending growth as reported in the Midyear Financial Plan Update. They do not account for accounting shifts and federal aid offsets. See New York State Division of the Budget, *FY 2022 Mid-year Update* (October 2021), www.budget.ny.gov/pubs/archive/fy22/en/fy22en-fp-

myu.pdf; and Patrick Orecki, *Spending Growth Resumes, Fiscal Cliff Looms* (Citizens Budget Commission, September 2021), https://cbcny.org/research/spending-growth-resumes-fiscal-cliff-looms.

4. CBC analysis reflects that the two-year impact of a typical recession would be approximately $19.6 billion. See David Friedfel, "NYS Revenues in a Recession: Quantifying the Potential Shortfall," *Citizens Budget Commission Blog*, (March 2019), https://cbcny.org/research/nys-revenues-recession.
5. Office of the New York State Comptroller, *Medicaid: Enrollment Growth, COVID-19 and the Future* (December 2021), www.osc.state.ny.us/files/reports/pdf/medicaid-enrollment-growth-covid-19-and-the-future.pdf.
6. See Reinvent Albany, "Watchdogs Support Bill Restoring Comptroller Oversight Powers" (June 2, 2021), https://reinventalbany.org/2021/06/watchdogs-support-bill-restoring-comptroller-oversight-powers/.
7. Governor Andrew Cuomo, "2011 State of the State Address" (speech given in Albany, NY on January 5, 2011), www.c-span.org/video/?297338-1/york-state-state-address.
8. See E.J. McMahon, "NY was leaking income millionaires in pandemic run-up," *Empire Center Blog* (December 7, 2021), www.empirecenter.org/publications/ny-was-leaking-income-millionaires-in-pandemic-run-up/.