Policy Brief ■ March 2022

Risky Business:
What Could Happen If NYS Spends More… More... And Much More

By Patrick Orecki

The fiscal year 2023 State budget is being negotiated in the context of apparent unprecedented State fiscal strength, though economic and pandemic uncertainties serve as stark reminders to be prepared for emergencies. Despite Governor Kathy Hochul's Executive Budget proposing a $10 billion increase in State Operating Funds (SOF) spending, both houses of the Legislature propose to add approximately $6 billion more. If adopted, these proposals would create significant future budget gaps, sap the State's ability to save for a future emergency or inevitable next recession, and likely set the stage for budget cuts or economically counterproductive tax increases down the road.

Improving tax receipts, extraordinary federal fiscal relief, and higher than anticipated revenue from tax increases last year provide an historic opportunity to address many priorities, make unprecedented deposits to reserves, present a budget balanced for the next four years, and be on a path to let last year's tax increases expire. (Appendix 1 shows how the early pandemic projected four-year $60 billion receipt shortfall evolved into a $55 billion receipt surplus.)

CITIZENS BUDGET COMMISSION

Bolstered by these receipts, Governor Kathy Hochul's Executive Budget proposes to increase substantially SOF spending in fiscal year 2023—$10.1 billion (8.5 percent), after adjusting for off-budget shifts, payment timing, and other accounting maneuvers. (See Appendix 2.) While the financial plan shows State spending increasing by $3.7 billion (3.2 percent), this does not include, for example, $2 billion in unspecified COVID relief or the proposed $2.2 property tax rebate. Even with this proposed increase, the budget is balanced through fiscal year 2027, and $15 billion would be added to reserves by fiscal year 2025. These reserves are critical to weather a future recession, especially important given the rocky economic recovery and potentially optimistic long-term State revenue assumptions. Still, the budget lacks plans to restrain spending growth over time; this restraint is needed for fiscal stability and to ensure last year's temporary tax increases sunset as scheduled or earlier.

Despite the Executive Budget providing significant resources to address many needs, the Legislature's one-house budgets propose to spend billions of dollars more, lifting the already massive proposed fiscal year 2023 spending increase to roughly $16.2 billion (13.6 percent). These plans would prevent the State from building the needed reserves proposed by the Governor and open out-year budget gaps estimated to be $7.7 billion in fiscal year 2026. Adopting these proposals would likely put the State on a path to a future fiscal crunch, requiring budget cuts, more tax increases, or both in four years' time. This would damage the State's competitiveness even if the economy continues to grow. When the next recession hits, the State would be woefully unprepared; the possible three-year receipt shortfall could total $40 billion based on the three recessions prior to the pandemic.

The Governor and the Legislature should adopt a budget that keeps to the Executive Budget's top line on spending and focuses on allocating the $5 billion available for relief and recovery (comprised of the funds unallocated for relief, proposed for the homeowner tax rebate, and from the consensus forecast). Along with federal COVID aid, there are tens of billions of dollars over time to meet many priorities. To deliver results New Yorkers need and deserve, the Governor and Legislature should diligently manage and provide oversight of funded programs by developing plans, identifying goals, measuring activities and results, and ensuring accountability by managers and local governments. This, in conjunction with putting funds in reserves as the Governor proposed, will ensure the continued fiscal stability needed to take care of New Yorkers over time and to roll back the tax increases so New York is a competitive location for residents and businesses.

PROPOSED SPENDING GROWTH GREATLY EXCEEDS PAST TRENDS

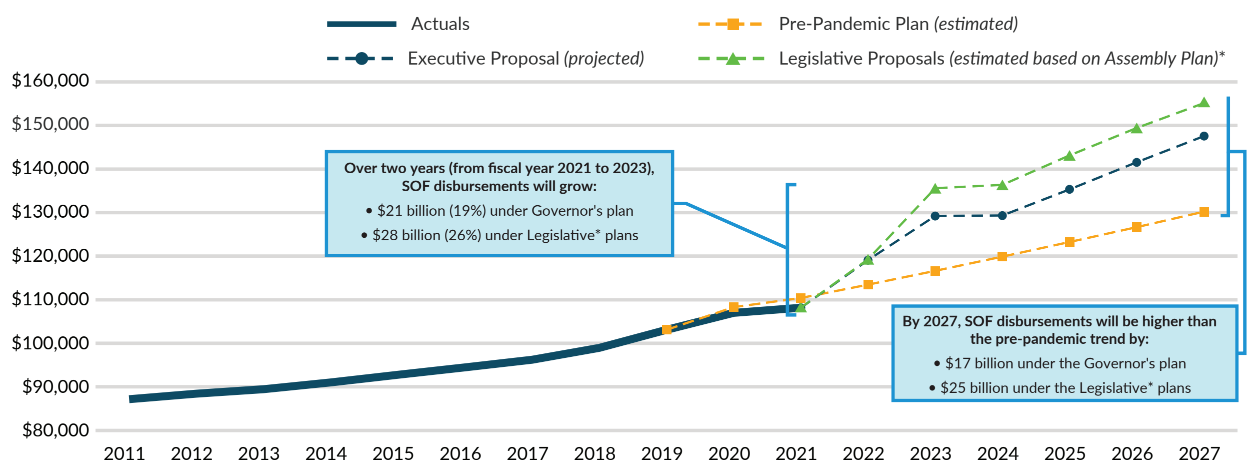
Higher receipts have already supported massive spending increases; spending in the current year, fiscal year 2022, will increase roughly $11.0 billion over last year. The Governor's budget proposal – with rising spending on school aid, Medicaid, recovery programs, and temporary targeted tax relief – would significantly increase spending in fiscal year 2023 by another $10.1 billion (8.5 percent). Thus, over two years, SOF spending would grow $21 billion—the same amount it grew over the prior ten years, from fiscal year 2011 to fiscal year 2021.[1]

Analyzing the impact of the Legislature's proposals is difficult because they do not provide needed multi-year fiscal data. However, the Assembly reports that its proposal adds $6.1 billion in SOF disbursements above the Governor's proposal, bringing its annual proposed increase to $16.2 billion.[2]

The Senate's proposal does not include the same level of summary data. However, totaling its specific proposals indicates the Senate's plan would increase spending about as much as the Assembly's. While there are some different priorities, both houses provide similar levels of funding provided for childcare, wages of home care aides, health coverage for ineligible immigrants, utility arrears payments, rental relief, and other purposes, with slight differences in approach to a few programs (such as a temporary motor fuel tax suspension only proposed by the Senate).

Before the pandemic, adjusted SOF disbursements were increasing 2.8 percent annually, based on the fiscal year 2017 to fiscal year 2021 period). Assuming SOF spending continued to grow 2.8 percent annually from fiscal year 2021 (the onset of the pandemic), it would reach $130.2 billion in fiscal year 2027.[3] Under the Governor's proposal, SOF disbursements will reach $147.6 billion by that point, $17.4 billion higher than the pre-pandemic trend. Importantly, a portion of this growth ($2.2 billion in fiscal year 2023) comes from continuing last year's agreement to increase education aid significantly over time. Assuming the Legislature's proposed increases for fiscal year 2023 recur in subsequent years, spending would reach approximately $155.2 billion, $25 billion above trend, by fiscal year 2027. (See Figure 1.)

Figure 1: Adjusted State Operating Funds Disbursements, Fiscal Years 2011 through 2027
(dollars in millions)



Notes: (*) The "Legislative Proposals" values are based on the Assembly's one-year SOF disbursements variance of $6.1 billion more than the Executive Budget in fiscal year 2023, and added to adjusted Executive Budget projections in each out-year. The out-year projections are increased further by $1 billion in fiscal year 2024 and $2 billion annually beginning in fiscal year 2025 based on proposed growth in childcare spending, and reduced by $500 million each year beginning in fiscal year 2024 to account for one-time utility arrears spending in fiscal year 2023. "Pre-Pandemic Plan" data reflects actual for fiscal year 2011 through fiscal year 2019, financial plan projections for fiscal years 2020 through 2024 from the Fiscal Year 2021 Executive Budget Financial Plan, and trended projections for fiscal year at 2.8 percent annual growth based on prior years' data. "Executive Plan" reflects actuals and projections from the Fiscal Year 2023 Amended Executive Budget Financial Plan adjusted as outlined in the Appendix.

Sources: New York State Division of the Budget, *Fiscal Year 2023 Amended Executive Budget Financial Plan* (February 2022), and prior editions; and New York State Assembly, *2022-23 Assembly Budget Proposal* (March 2022), p. 1.

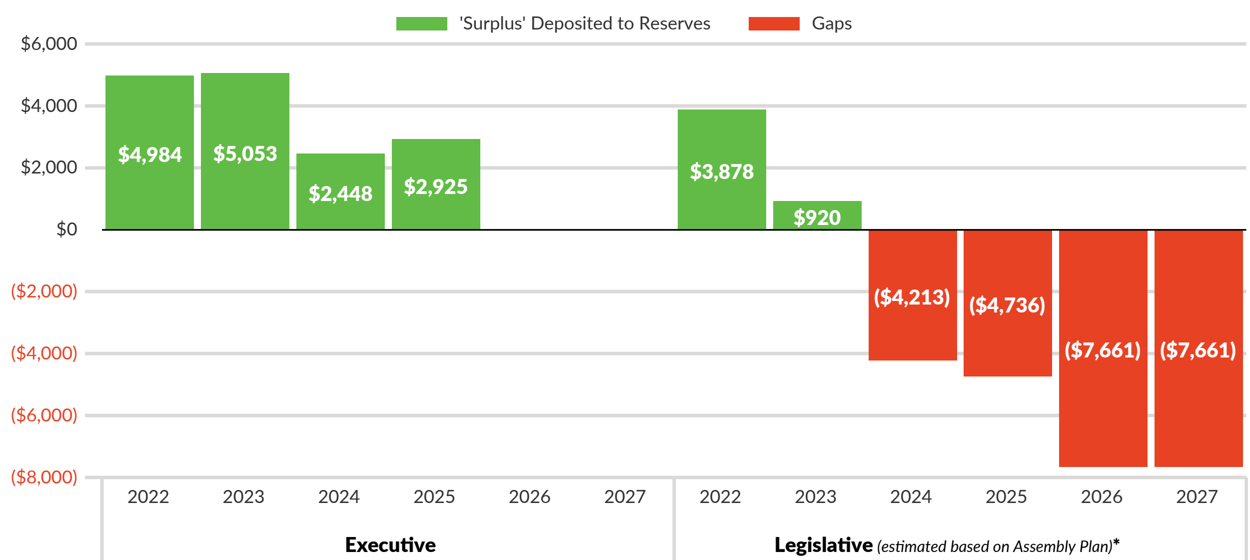
FUNDING HIGHER SPENDING ELIMINATES RESERVES, CREATES OUT-YEAR DEFICITS

The Legislative proposals do not specify how they would fund the additional annual spending for fiscal year 2023 and beyond. The Assembly plan reflects lower proposed deposits to reserves in fiscal year 2023, instead using the funds to support higher spending. The plan does not present reserve balances in out-years, but it is reasonable to assume the proposal also would reduce the Governor's proposed reserve deposits in fiscal years 2024 and 2025. Since the proposed spending is higher than the Governor's reserve deposits, it would create budget gaps in those years. These gaps would even be larger in fiscal years 2026 and 2027, since the Executive Budget does not include reserve deposits after fiscal year 2025.

Figure 2 illustrates how the Legislative proposals hamper reserves and create gaps. Whereas the Governor's proposal adds $15 billion to reserves and maintains budget balance, the Legislative proposals would add only $4.8 billion to reserves and open budget gaps that could grow from $4.2 billion in fiscal year 2024 to $7.7 billion beginning fiscal year 2026.

Figure 2: Annual Surplus Deposits to Reserves and Budget Gaps: Executive Budget and Legislative Proposals, Fiscal Years 2022 through 2027

(dollars in millions)



Notes: (*) The "Legislative" reserves deposits are as outlined in the Assembly's one-house budget report for fiscal year 2023. It is further assumed that additional SOF spending will preclude further deposits to reserves beginning in fiscal year 2024, creating budget gaps in the out-years. Gaps are based on the Assembly's one-year SOF disbursements variance of $6.1 billion more than the Executive Budget in fiscal year 2023, and added to adjusted Executive Budget projections in each out-year. The out-year projections are increased further by $1 billion in fiscal year 2024 and $2 billion annually beginning in fiscal year 2025 based on proposed growth in childcare spending, and reduced by $500 million each year beginning in fiscal year 2024 to account for one-time utility arrears spending in fiscal year 2023.

"Executive" reflects projections from the Fiscal Year 2023 Amended Executive Budget Financial Plan.

Sources: New York State Division of the Budget, *Fiscal Year 2023 Amended Executive Budget Financial Plan* (February 2022); and New York State Assembly, *2022-23 Assembly Budget Proposal* (March 2022), p. 1.

While the State currently could lift its emergency savings to $19 billion in total, keep the budget balanced, and put itself on a path to reduce its highest-in-the-nation taxes in the coming years, the one-house proposals likely would deposit woefully inadequate reserves, create significant budget gaps, and chart a path to even more tax increases and possibly wrenching budget cuts. Furthermore, while these scenarios rely on unabated economic expansion, a typical recession would result in approximately $15 to $17 billion in annual tax receipts shortfalls (a conservative estimate given that the tax structure was made more volatile after last year's tax increases).

WHAT'S MISSING?

There are two glaring omissions from the budget proposals. First, the Legislative one-house proposals do not include multi-year financial plan tables needed to understand and evaluate their spending plans more accurately. In January and March, CBC called for improvements in budgeting transparency, including publishing basic financial plan tables that show the receipts and disbursements with the one-house and enacted budgets. This is critical to identifying proposals' or agreements' fiscal and possible service impacts for the next year and for the future.

Second, the budgets do not include provisions to implement statewide performance measurement and management. New York has the highest per pupil school aid spending in the country, highest per capita Medicaid spending in the country, massive economic development deals, and significant spending across myriad other programs. Yet, it lacks a management and accountability system and appropriate goals and performance metrics to ensure and assess how successful its spending is in delivering results efficiently for New Yorkers. It's past time to implement performance management in New York.

CONCLUSION

The Governor and Legislature are working toward an enacted budget agreement, presumably to be announced around April 1. That agreement will increase annual spending by billions of dollars next year, to be followed by growth in the future. New York has long spent and taxed more than other States, as measured in various ways, but the rate of proposed spending growth – especially in the Legislature's plans – is far greater than in recent years. Even under the Governor's more prudent proposal, State spending would grow by more over two years than it did in the whole previous decade. Furthermore, this does not include the massive infusion of federal COVID aid.

New York now has the opportunity to fund important priorities, set aside significant reserves, stabilize its outlook, and roll back its nation-leading taxes to protect New York's competitiveness and tax base. This is an historic opportunity, but it is at great risk, with the potential to spend even more than the Governor proposed and little focus on ensuring the funds get used wisely and deliver results for New Yorkers.

APPENDIX 1: HOW A $60 BILLION SHORTFALL BECAME A $55 BILLION SURPLUS

At the onset of the pandemic in April 2020, the State projected a pandemic-induced tax receipts shortfall of roughly $15 billion annually, or $60 billion over four years. A projected shortfall of this magnitude was consistent with a typical recession in New York. To contend with the expected shortfall, the State prepared to withhold spending across the board while also using targeted federal fiscal relief to help balance the budget.

However, as the months passed the tax receipts shortfall did not come to pass. In fact, tax receipts came in much stronger than expected. Three revenue sources helped the State reverse its fiscal outlook:

1. Base tax receipts: Throughout 2020, the State repeatedly exceeded its tax receipts projections. In January 2021 the State Division of the Budget began re-estimating receipts projections to reflect the improving outlook. In each quarterly financial plan update since then, the State has raised its tax receipts projections significantly. In fact, the $60 billion four-year tax receipts shortfall is now a tax receipts surplus of $18 billion (before accounting for tax increases and federal fiscal relief).
2. Federal fiscal relief: Since the onset of the pandemic, the State has benefitted from targeted federal fiscal relief that helped offset State spending, principally through the Coronavirus Relief Fund and enhanced federal medical assistance percentage (eFMAP) in Medicaid. Then in March 2021 the American Rescue Plan provided the State with another $12.7 billion in general fiscal relief. When federal fiscal relief is added to improved base tax receipts, the cumulative surplus increases to $42 billion over the four-year period.
3. State tax increases: In April 2021 the fiscal year 2022 enacted budget raised personal income tax and corporate tax rates, generating approximately $4 billion per year in additional tax revenues (ostensibly to fund massive increases in State school aid spending). Added to the base tax receipts and federal fiscal relief, the tax increases result in a four-year surplus of $55 billion compared to pre-pandemic projections.

Taken together, the improvement in State tax receipts, federal fiscal relief, and State tax increases flipped the script for the State. (See Table 1.)

Table 1: State Tax Receipts Impacts Since March 2020

(dollars in millions)

	FY 2021	FY 2022	FY 2023	FY 2024	4-Year Total
Initial Pandemic-Related Receipts (Shortfall)/Surplus	($13,471)	($15,789)	($15,362)	($15,362)	**($59,984)**
Receipts (Shortfall)/Surplus after Base Tax Receipts Re-estimates	($5,556)	$5,783	$8,977	$9,200	**$18,404**
Receipts (Shortfall)/Surplus after Base Receipts and Federal Fiscal Relief	$1,755	$21,512	$9,972	$9,200	**$42,439**
Receipts (Shortfall)/Surplus after Base Receipts, Federal Relief, and Tax Increases	$1,755	$25,015	$14,296	$13,435	**$54,501**

Notes: Initial Shortfall reflects the difference between pre-pandemic tax receipts projections and the Fiscal Year 2021 Midyear Financial Plan. Base tax receipts re-estimates include the net adjustments to tax receipts from pre-pandemic projections to the Fiscal Year 2023 Executive Budget Financial Plan, less the estimated impact of tax increases in the Fiscal Year 2022 Enacted Budget Financial Plan. Federal Fiscal Relief includes federal aid used to offset SOF disbursements, including, the Coronavirus Relief Fund, enhanced Medicaid funding, CARES school aid, and ARP state fiscal relief. Tax Increases includes the impact of personal income tax and corporate tax increases as estimated in the Fiscal Year 2022 Enacted Budget Financial Plan.

Sources: New York State Division of the Budget, *Fiscal Year 2023 Amended Executive Budget Financial Plan* (February 2022), and prior editions; and New York State Assembly, *2022-23 Assembly Budget Proposal* (March 2022), p. 1.

APPENDIX 2: CALCULATING ADJUSTED STATE OPERATING FUNDS DISBURSEMENTS

CBC calculates "adjusted" SOF disbursements growth by accounting for accounting maneuvers. Over the years, this repeated analysis has shown that the State was not adhering to its self-imposed 2 percent spending cap. Accounting maneuvers included shifting certain dedicated tax receipts off-budget, accounting changes to shift the School Tax Relief (STAR) program to a tax credit, Medicaid payment deferrals, and other actions that impacted the timing or accounting of spending.

This year, adjustments are also made to account for one-time spending initiatives proposed in the Executive Budget. Adjustments are made to add the $2.2 billion homeowner tax credit program and $2 billion unallocated COVID relief pot – both of which are not included in reported spending – to the disbursements totals. Year-to-year trends are also impacted by temporary federal fiscal relief that offset SOF disbursements with federal funds. Table 2 summarizes the adjustments, and reflects that reported spending growth of 3.2 percent from fiscal year 2022 to fiscal year 2023

When these accounting maneuvers are adjusted for, the short-term and long-term spending growth figures are even larger. Spending in the budget year (fiscal year 2023) is actually $10.1 billion higher than reported. Thus, the year-to-year growth rate from fiscal year 2022 to fiscal year 2023 is about 8.5 percent (greater than reported growth of 3.2 percent). Over the two-year period since the onset of the pandemic, adjusted SOF spending growth is set to increase by more than $20 billion (nearly 20 percent).

Table 2: Adjusted State Operating Funds Spending Growth
(dollars in millions)

	Actual		Projected					
	FY2020	FY2021	FY2022	FY2023	FY2024	FY2025	FY2026	FY2027
Reported SOF Spending	**$102,160**	**$104,207**	**$115,226**	**$118,907**	**$123,412**	**$128,911**	**$135,913**	**$141,142**
Reported SOF Growth Rate	*2.0%*	*2.0%*	*10.6%*	*3.2%*	*3.8%*	*4.5%*	*5.4%*	*3.8%*
Value of Short-term Liquidity Borrowing Repayment	$0	($4,500)	$0	$0	$0	$0	$0	$0
Reported SOF Spending *(adjusted for liquidity borrowing repayment)*	**$102,160**	**$99,707**	**$115,226**	**$118,907**	**$123,412**	**$128,911**	**$135,913**	**$141,142**
Reported SOF Growth Rate	*2.0%*	*-2.4%*	*15.6%*	*3.2%*	*3.8%*	*4.5%*	*5.4%*	*3.8%*
Adjustments for Delays, Deferrals, and Shifts	**$4,829**	**$1,161**	**$896**	**$9,332**	**$5,923**	**$6,434**	**$5,644**	**$6,422**
STAR Actions	$1,280	$1,297	$1,392	$1,594	$1,768	$1,951	$2,141	$2,321
MTA Payroll Taxes (off-budget)	$1,837	$1,906	$1,984	$2,066	$2,151	$2,240	$2,333	$2,429
Medicaid Deferrals (net)	($599)	$702	$54	$55	$57	$59	$61	$62
Tobacco Master Settlement Funds (off-budget)	$315	$294	$362	$362	$362	$362	$362	$362
COVID-related Payment Processing Delays	$1,385	($1,385)	$0	$0	$0	$0	$0	$0
Debt Prepayments (net)	$1,033	($2,682)	($1,801)	$1,075	$1,125	$1,265	$500	$1,000
Homeowner Rebate "Tax Credit" (Proposal)	$0	$0	$0	$2,200	$0	$0	$0	$0
Unspecified COVID Relief Pot (Proposal)	$0	$0	$0	$2,000	$0	$0	$0	$0
All Other	($421)	$1,028	($1,095)	($20)	$460	$557	$247	$247
Adjusted SOF Spending	**$106,989**	**$100,868**	**$116,122**	**$128,239**	**$129,335**	**$135,345**	**$141,557**	**$147,564**
Adjusted SOF Growth Rate	*3.8%*	*-5.7%*	*15.1%*	*10.4%*	*0.9%*	*4.6%*	*4.6%*	*4.2%*
Federal Aid Offsets	**$0**	**$7,311**	**$2,984**	**$995**	**$0**	**$0**	**$0**	**$0**
Enhanced Medicaid Funding	$0	$3,420	$2,984	$995	$0	$0	$0	$0
COVID Relief Funds	$0	$2,722	$0	$0	$0	$0	$0	$0
School Aid (used as offset)	$0	$1,169	$0	$0	$0	$0	$0	$0
Adjusted Spending on SOF Purposes *(including federal aid offsets)*	**$106,989**	**$108,179**	**$119,106**	**$129,234**	**$129,335**	**$135,345**	**$141,557**	**$147,564**
Adjusted SOF Growth Rate (including federal aid offsets)	*3.8%*	*1.1%*	*10.1%*	*8.5%*	*0.1%*	*4.6%*	*4.6%*	*4.2%*

Note: Due to a drafting error, a previous version of Appendix Table 2 misstated the value of "Medicaid Deferrals," "COVID-related Payment Processing Delays," and "Debt Prepayments" in certain years. This error did not impact any of the subtotals or totals, and was corrected on March 25, 2022.

Sources: CBC analysis of New York State Division of the Budget, Fiscal Year 2023 Amended Executive Budget Financial Plan (February 2022), and prior editions.

ENDNOTES

[1] New York State Division of the Budget, *Fiscal Year 2023 Amended Executive Budget Financial Plan* (February 2022), www.budget.ny.gov/pubs/archive/fy23/ex/fp/fy23fp-ex-amend.pdf, and prior editions; and New York State Assembly, *2022-23 Assembly Budget Proposal* (March 2022), p. 1, https://nyassembly.gov/Reports/WAM/AssemblyBudgetProposal/2022/2022AssemblySummary.pdf.

[2] Because the Assembly and Senate proposals fund many of the same initiatives, it is assumed that the Senate's proposal provides for a similar level of spending growth. "Legislative Plan" values are based on the Assembly's one-year SOF disbursements variance of $6.1 billion in fiscal year 2023 and added to adjusted Executive Budget projections in each out-year. The out-year projections are further increased by $1 billion in fiscal year 2024 and $1 billion in fiscal year 2025 based on proposed growth in childcare spending and reduced by $500 million each year beginning in fiscal year 2024 to account for one-time utility arrears spending in fiscal year 2023.

[3] Projected growth of 2.8 percent is based on adjusted SOF disbursements growth from fiscal year 2017 to fiscal year 2021. This rate of growth is higher than the State's previous target growth rate of 2.0 percent, and higher than CPI inflation of roughly 1.8 percent over the same period. This rate of projected growth does not account for higher current inflation rates.

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