February 2, 2009

Dear Legislator:

I am writing on behalf of the Citizens Budget Commission to convey our recommendations for the fiscal year 2009-10 budget.

As you know, the State is facing an enormous fiscal challenge. The nation is being hit by the worst recession in 70 years. Job losses statewide are expected to reach 300,000, and Wall Street – which has generated 20 percent of the State's revenue - is undergoing fundamental changes. This economic downturn compounds a pre-existing structural imbalance in the State's budget to create enormous gaps that must be closed – nearly $14 billion next year and rising to $18.6 billion in fiscal year 2011-12.

But there is opportunity in this crisis. New York can emerge a stronger, more competitive state if the right actions are taken in this year's budget. Two strategic policy directions should guide your actions.

- *Avoid excessive reliance on increased taxes.* In this environment, it would be foolhardy to impose taxes and fees that further discourage investment and spending – things desperately needed to propel us out of recession – or that provide greater incentives for residents and businesses to leave New York for lower cost locations. The Governor's Executive Budget proposes $5 billion in new revenue measures; the budget you adopt should reduce this to no more than $2 billion.
- *Build on the Governor's recommended expenditure cuts to make New York's spending more effective and efficient.* Even the potential good news of the rapidly moving and sizable stimulus package from the federal government will not alter the reality that State spending must come down. The federal funds will be temporary and will not help address the large budget gaps that will reappear when the money is gone. To grapple with what are likely to be permanent structural changes in the financial services industry and the downsizing of the State's economic base substantial spending reforms are essential. Whether there are strings and maintenance of effort requirements attached to the federal funds—and we hope there are not—the new economic reality must be faced.

By way of this letter, the Citizens Budget Commission offers a roadmap to help you steer a course that avoids harmful tax increases and makes spending better serve New Yorkers. We recognize that many of the recommended actions will not be popular among certain interest groups, but we believe they are the necessary ways to adjust New York's expenditures to the current economic circumstances while enhancing the state's long-run competitiveness.

To build on the positive proposals in the Executive Budget we recommend more profound reforms in five key areas. These targeted spending reductions will minimize harm to the economy and to public services.

1. **Expand Medicaid reforms.** Medicaid spending per beneficiary in New York is 69 percent higher than the national average, driven in large measure by high expenses for long-term care. The State can no longer afford a Medicaid program so out of line with

national norms. The Executive Budget includes reforms that deserve passage, notably linking payment for hospital inpatient care, nursing homes and home care to patient needs rather than historical institutional costs. Rate reductions that bring New York closer to national norms are also meritorious. However, more needs to be done to lower costs.

Medicaid should be a program that serves the neediest New Yorkers. Eligibility loopholes for long-term care that allow middle-class and wealthy New Yorkers to benefit from the program should be closed. Tightening eligibility to individuals with homes worth less than $500,000 and applying the look-back period for asset transfers to eligibility for home care would save $400 million annually. Controlling excessive utilization of personal care services and expanding managed care would save $600 million annually. Together these efforts would save $1 billion annually over the next few years.

2. **Better target school aid.** The Governor proposed reductions in school aid based on need and ability to pay, targeting the greatest percentage cuts to the wealthiest districts; these cuts should be enacted. In addition, other features of foundation aid should be reformed to promote equity and produce further savings. Two measures in the new aid formulas that work against the principle of allocating school aid based on need, high tax aid and hold harmless provisions, should be eliminated. Eliminating high tax aid would save $205 million in the upcoming fiscal year, and dropping the hold harmless provisions from the past two fiscal years would save about $670 million. Some of these savings could be used to protect the neediest districts from cuts.

3. **Right-size prisons, detention facilities and other institutions.** The Executive Budget recommends closing four prisons and six youth facilities that are underutilized, and eliminates beds at an inpatient mental health facility and an addiction treatment center. These actions save money without compromising services and move the State toward an institutional infrastructure that is the right size for current needs and trends in care. However, even with these closures the State will still be paying for more capacity in costly institutional settings than is needed. The State still operates developmental centers for the developmentally disabled that house clients for whom community care alternatives are more appropriate. The same is true for State-run psychiatric centers, where standards of care have also moved more toward community-based options.

   The Legislature should thoroughly review all the large institutions that the State continues to run to determine which facilities can be closed or consolidated. In the case of prisons, for example, if the Department of Correction's staff and facilities were reduced to a level commensurate with the 15 percent decline in inmate population, the State would save $280 million annually.

4. **Trim overly generous public employee benefits.** The fringe benefit package extended to State employees is more generous than the norm in the private sector and for many other government workers. For example, New York is one of only six states to pay any part of Medicare Part B premiums for retirees, and it's the only state that pays almost the entire premium. Almost all public pension systems – 94 percent – require greater

employee contributions than New York's average of 1 to 3 percent, and the same share of pension systems exclude overtime as pensionable salary while New York includes it. The Executive Budget proposes some changes to scale back compensation for current and retired employees, including the elimination of one 3 percent raise, a reduction in Medicare Part B reimbursements, increased contributions to healthcare premiums from retirees, and the creation of a Tier V in the pension system, which will increase the retirement age, increase employee contributions and scale back final salary calculations.

The Legislature should improve these proposals by requiring a greater share of health insurance premiums to be paid by current and retired employees, bringing healthcare contributions in line with those of other public sector employees. For retirees (many of whom are eligible for Medicare), the Legislature should require a 50 percent contribution to their premium costs and eliminate reimbursement for Medicare Part B premiums. These actions will save annually $430 million and $200 million, respectively. For current employees, the Legislature should increase contributions to family healthcare plans from 18 percent to 22 percent, for a savings of $75 million annually.

5. **Make programs more cost-effective.** The Executive Budget recognizes that some State run programs are not effective and should be eliminated or reformed. It eliminates the ill-conceived and poorly targeted Middle-Class STAR rebate and makes the Empire Zone program, which has had a high rate of businesses failing to meet their job creation and investment targets, more effective. The Executive Budget also includes savings of $16.5 million from agency consolidations and developing shared services to replace overlapping positions in financial management, procurement, human resources, technology, asset management and customer services. Through these efforts the Governor proposes to eliminate 3,000 positions.

   The Legislature should take all possible actions to reduce the size of the State's workforce. The Executive Budget reduces the number of employees in fiscal year 2009-10 to a level still 13,000 higher than it was at the end of fiscal year 2003-04. By examining the root causes of high growth in employment in key agencies, such as SUNY, CUNY and the judiciary, it may be possible to contain growth without damaging core services. If, for example, the size of these agencies' workforces could be brought down to fiscal year 2006-07 levels, savings of $283 million per year would be achieved.

Together, these recommendations provide at least $3.1 billion in savings over the term of the financial plan. These savings should first be used to eliminate tax increase proposals that curtail economic activity and add to the already high cost of doing business in New York. The tax increase on utilities is one such proposal. Additional candidates for replacement in the gap-closing program include the $679 million of health care savings that stems from "assessments" (meaning taxes) on insurance companies that will be passed on to consumers across the State. These assessments are part of $1.9 billion in revenue increases that were mis-categorized as spending reductions in the Governor's budget because in a technical sense they lower spending from the general fund. However, these items do raise revenues by going directly to New Yorker's pocketbooks and should therefore, be counted as tax increase proposals instead. No one will fail to note the higher price they pay for sugared soda, the larger bill for SUNY/CUNY tuition, or the increases in their health insurance premiums as assessments on insurance

companies are passed on. The attached table provides a full list of the proposals that should be counted among the numerous tax, fee, and revenue increase proposals in the Executive Budget.

With the economy in a fragile state and all New Yorkers tightening their belts to adjust to new economic realities in their own households, we recommend that your actions in the coming months help New York emerge as a stronger, more competitive state. Temporary federal funds cannot postpone the inevitable and should be used as flexibly as possible to obviate the need for tax increases that would hinder New York's recovery, not to prop up expenditures that will be impossible to sustain.

Thank you for considering our recommendations. Please contact me or my staff should you have questions or if we can be of assistance in any way.

Sincerely,

Carol Kellermann
President

Mis-Categorized Revenues in the Gap Closing Plan
(dollars in millions)

Non-dietetic soft drink tax	$404.0
Covered lives assessment on insurance companies	240.0
SUNY/CUNY tuition increase	197.0
Timothy's Law Insurance Assessment	179.0
HCRA program shifts to insurance	138.0
Increase hospital surcharge	126.0
Transportation-related fees	97.3
Shift anti-tobacco spending to insurance	71.0
Establish third party healthcare processing fee	63.1
Surcharge on physicians procedures	49.8
Increase in surcharge on auto insurance	48.4
VLT facility hours extension	45.0
Lottery quick draw enhancements	40.0
Restructure clinical lab fees	36.5
Shift public health costs to insurance companies	29.0
Shift financing of Early Intervention to insurers	22.0
Tobacco retail license fee increase	19.0
Physician fees	16.4
Modify family contribution to Childrens Health Program	16.0
Authorize multi-jurisdictional lottery games	11.0
Higher edu assessment on research foundations	10.0
Increase certificate of need fees	4.0
Early Intervention provider fee	1.7
Total	**$1,864.2**