THE ARMONK AGENDA:

Next Steps for Fiscal Reform in New York State

OCTOBER 2006

NEW YORK'S NONPARTISAN VOICE
FOR EFFECTIVE GOVERNMENT

OVERVIEW

…a consensus on priorities for legislative action.

On April 7–8, 2006, the Citizens Budget Commission (CBC) convened a conference in Armonk, New York with the goal of identifying widely supported, high-priority measures for fiscal reform in New York State. This document highlights those measures in order to raise awareness and promote discussion of them in the coming year.

The specific areas of reform targeted at the conference were the realignment of state and local fiscal responsibilities in order to lower local government's tax burdens, changes in debt management in order to lower the State's debt burden and make more effective use of borrowing, and improvements in the annual budget process in order to make it more accountable, timely and transparent. These topics are the most pressing areas for fiscal reform in New York State.

The goal of the conference was to develop a consensus on priorities for legislative action. Participants in the conference included 150 civic, government, business, and labor leaders from across the state, as well as editorial writers, academics and policy experts. Following panel presentations and small group discussions, the participants were asked to rate the importance of specific policy options. From this voting process 12 high-priority steps emerged – the four policies garnering the most votes in each of the three reform areas constitute the "Armonk Agenda."

Founded in 1932, the Citizens Budget Commission (CBC) is a nonpartisan, nonprofit civic organization committed to influencing constructive change in the finances and services of New York State and New York City governments.

In order to highlight important issues of fiscal reform in the coming year, this document summarizes background material, deliberations and voting results at a conference organized by the CBC on April 7–8, 2006.
The summary was drafted by Darcie Harvey, Research Associate, under the direction of Elizabeth Lynam, Deputy Research Director, and Charles Brecher, Research Director. Brecher is also a Professor at NYU's Wagner School.
The conference background material and a full report on the voting results at the conference can be found at the CBC website http://www.cbcny.org.

THE ARMONK AGENDA

...12 high-priority steps emerged.

LOWERING LOCAL TAXES

1. Reduce State-mandated local government Medicaid costs more than authorized by the 3 percent cap on local growth enacted in 2005.
2. Redesign State school aid programs including STAR to better serve poorer districts and thereby lower their local school tax burden.
3. Redesign the State-mandated pension benefits for future state and local government workers through changes such as raising the minimum retirement ages, increasing the required employee contributions, eliminating inclusion of overtime in benefit calculations, and eliminating variable supplements for uniformed workers.
4. Lower Medicaid expenditures by eliminating long-term care eligibility loopholes that extend benefits to middle-class residents.

LOWERING AND BETTER MANAGING STATE DEBT

1. Discontinue issuance of State-funded debt to cover operating deficits.
2. Integrate public authorities' proposed borrowing for capital investments with the State's capital plan in order to prevent inefficient use of borrowing capacity.
3. Subject public authority borrowing to more rigorous financial review by an enhanced Public Authorities Control Board or by the Division of Budget.
4. Reduce the State's future debt by lowering capital spending and/or increasing pay-as-you-go financing.

MORE ACCOUNTABLE AND TRANSPARENT ANNUAL STATE BUDGETS

1. Prepare more extensive multi-year financial plans.
2. Enforce and build upon new requirements for reporting by public authorities.
3. Require that lump-sum appropriations meet specific program criteria and be subject to sunshine provisions.
4. Publish the Adopted Budget in a format similar to the Executive Budget.

BUILDING MOMENTUM FOR REFORM

Significant progress has been made in reducing the Medicaid burden on local governments.

The Armonk conference was not the Citizens Budget Commission's only recent effort to build wide support for State fiscal reform. In 2003, the Commission held a conference in Palisades, New York focused on five problems:

1. New Yorkers are the most heavily taxed Americans.
2. New York's debt burden is among the highest in the nation.
3. New York has large and recurring budget gaps.
4. New York's budget process lacks timeliness, transparency and responsibility.
5. Improvements in fiscal practices are hampered by unresponsive governmental institutions.

The initial conference yielded ten reform items known as the "Palisades Principles." They are widely credited with triggering public interest in fiscal reform and subsequent responses by the State Legislature. Measures authorized in the name of "fiscal reform" since the Palisades conference include some that represent significant progress, others that are less substantial but represent notable first steps, and two that were steps backward in the sense of being distractions or counterproductive.

Progress on Medicaid. Significant progress has been made in reducing the Medicaid burden on local governments. In 2004 legislation relieved local governments of responsibility for financing the Family Health Plus component of Medicaid under a phased-in schedule spanning two years; the timetable was accelerated in 2005, and local governments are no longer responsible for this part of Medicaid, effective October 2006. In 2005 legislation placed a cap on the growth in local governments' Medicaid obligation; over three years, from fiscal year 2005–06 to 2007–08, the maximum growth drops from 3.5 percent to 3.0 percent and remains at 3.0 percent thereafter. This represents substantial savings since Medicaid expenditures have been growing about triple that rate in many years. These measures will save local governments about $1.1 billion in the current fiscal year.

Other Notable Steps. The Legislature and the Governor have agreed on additional measures consistent with the Palisades Principles. However, in each case the progress is limited and does not achieve fully the intended reform.

- Putting Health Care Reform Act funds "on-budget." Beginning in fiscal year 2004–05 the Governor included about $4.5 billion of health care expenditures that had been "off-budget" in the Executive Budget, adding to transparency. Some smaller off-budget items remain and new ones were created in 2006.

- Enacting the Public Authority Accountability Act. This 2005 legislation set some new standards for public authorities and created an Authority Budget Office to report on the finances of authorities. However, the Office's mandate is limited and additional measures are needed to make authorities more accountable.
- Using legislative committees in budget formulation. In 2005 and 2006 the Legislature relied on formal committees that held open meetings to help shape the enacted budget.

Two Distractions. Two legislative initiatives in fiscal reform were unsuccessful; the first would clearly have been a step backward, and the second was a mix of pluses and minuses. Proposal One was a proposed constitutional amendment that the Legislature put before the voters in 2005. It was a misguided effort to encourage on time budgets through the use of contingency measures that would come into force when the budget was late. However, the measures were counterproductive, creating incentives for late budgets by giving the Legislature enhanced powers in the contingency budget process. Voters rejected it in November 2005.

In June 2006, near the close of the 2006 session and without hearings, the Legislature passed another set of provisions to change the budget process. It included desirable elements such as requiring multi-year financial plans and a binding revenue forecast mechanism, but also had problematic components including: (1) a shift in the start of the fiscal year from April 1 to May 1 that could cause cash flow problems for the State in meeting school aid payments; (2) establishing two-year school aid appropriations that create more favorable budgetary rules for school aid than for all other types of expenditures; and (3) creation of an Independent Budget Office that (despite its name) was not designed to be politically independent. Governor George Pataki vetoed the bill in August.

The defeat of Proposal One and the possibility that the Legislature would take constructive action in 2006 were the critical features of the environment for the Citizens Budget Commission's conference in April. In that context the discussion of priority measures focused on three topics – changing the division of responsibilities between the State and its localities in order to reduce local taxes, better managing and reducing State debt, and making the State's annual budget process more accountable and transparent.

THE ARMONK AGENDA:
▸ LOWERING LOCAL TAXES

The local government tax burden is by far the highest in the country and is 158 percent of the national average.

New Yorkers pay extremely high taxes. (See Table 1. The analysis in this and other tables includes comparisons among all 50 states, but focuses on 11 major competitor states that are the other nine largest states by population and New York's geographic neighbors.) Measured as a share of personal income, the combined State and local tax burden of New Yorkers is the highest in the nation, fully 26 percent above the national average.

More than half the tax dollars paid by New Yorkers go to local governments rather than the State government. It is the local tax burden that causes New York's dubious distinction as the tax leader. The State portion of the tax burden ranks a lower 24th and is close to the national average. In contrast, the local government portion is by far the highest in the country and is 158 percent of the national average. Placing the majority of the tax burden on local governments is inefficient and inequitable, causing economic harm in the places with the greatest promise for job growth and placing heavy tax burdens on people in the poorest areas.

The high local taxes are not confined to New York City. While the local tax burden in New York City is 165 percent of the national average, the figure for the rest of New York State is fully 152 percent of the national average

Table 1
State and Local Taxes per $1,000 of Personal Income
New York and Competitor States, Fiscal Year 2001–02

	State and Local Taxes			State Taxes			Local Taxes		
State	Amount	Percent of US Average	50-State Rank	Amount	Percent of US Average	50-State Rank	Amount	Percent of US Average	50-State Rank
New York	**$131**	**126%**	**1**	**$64**	**104%**	**24**	**$67**	**158%**	**1**
Ohio	111	107%	11	62	100%	29	49	116%	3
California	106	102%	17	68	111%	18	38	88%	30
New Jersey	104	100%	21	55	90%	40	49	115%	5
Connecticut	104	100%	27	62	101%	28	42	98%	18
Illinois	101	97%	29	55	89%	42	47	110%	11
Pennsylvania	101	97%	31	59	97%	35	42	98%	19
Georgia	100	97%	34	57	93%	37	43	101%	15
Massachusetts	96	92%	40	59	97%	34	36	86%	32
Texas	95	92%	42	46	75%	48	49	116%	4
Florida	94	90%	44	53	86%	44	41	96%	22
US Avg	**$104**	**100%**	**NAP**	**$62**	**100%**	**NAP**	**$42**	**100%**	**NAP**

Source: State of New York, Department of Taxation and Finance, Office of Tax Policy Analysis, New York State Tax Sourcebook, January 31, 2006.

Note: NAP denotes not applicable.

New Yorkers are not paying unusually high local taxes because their locally elected officials want to impose this burden. Rather the local taxes are imposed because State-level policies require the counties and cities to raise the money. Three significant State policies that drive the local tax burden are: (1) a highly expensive and unusual Medicaid mandate; (2) limited and badly targeted school aid; and (3) costly mandates for public employee pension benefits and other constraints on labor relations.

THE MEDICAID MANDATE

New York's Medicaid program is unique in two ways. First, the State requires local governments to pay an unusually high share of the total costs. Second, the cost of the program is greater than every place else.

The High Local Share. New York State requires its local governments (New York City and the other 57 counties) to pay a greater share of Medicaid costs than does any other state. As noted earlier, a cap was placed on the growth in this local share beginning in 2005, but the remaining burden is still well above that in all other states. In the current fiscal year local governments in New York will pay about $7 billion or 16 percent of the program's total cost of $45 billion. In contrast, 30 states require no contribution from their counties, and the other 19 states that have some local financing keep it to a far smaller share than does New York. For example, New Hampshire requires counties to pay 50 percent of the non-federal share of nursing facility costs for Medicaid patients, but the local share of Medicaid represents only about 7.4 percent of total expenditures. New Jersey requires counties to pay 11 percent of psychiatric hospital care and also requires contributions for nursing facilities and administration, but the local share represents less than 1 percent of total Medicaid expenditures.

High Program Costs. Local governments are paying a high share of the most expensive Medicaid program in the nation. New York's average spending per beneficiary is $7,912, fully 176 percent of the national average of $4,487. (See Table 2.) Among New York's competitors, the closest cost is in Connecticut, but its cost is nearly $1,200 or 15 percent less per beneficiary.

What are the State policies that cause New York's high costs? Three features of New York's program stand out:

1. Paying providers non-competitive rates. The State pays hospitals, nursing homes and other institutional providers more than is necessary in competitive markets.
2. Allowing eligibility loopholes for long-term care. Many middle class elderly residents qualify for long-term care by taking advantage of loopholes that let them transfer or shield assets and income.
3. Failing to limit excess utilization of some services. New York has not relied on managed care as heavily as other states, thereby failing to get the benefits of controls on inpatient hospital use, and it permits far greater use of personal care services for the chronically ill than does any other state.

The Citizens Budget Commission has estimated that changing these policies could save more than $5.8 billion annually. (See Table 3.)

Table 2
Medicaid Spending per Beneficiary, Federal Fiscal Year 2003

STATE	SPENDING PER BENEFICIARY	50 STATE RANK
New York	$7,912	1
Connecticut	$6,764	5
New Jersey	$6,349	8
Massachusetts	$6,134	9
Ohio	$5,756	12
Pennsylvania	$5,489	14
Illinois	$5,131	15
Florida	$4,048	38
Texas	$3,750	40
Georgia	$3,093	48
California	$2,770	49
US Average	$4,487	NAP

Source: Centers for Medicare and Medicaid, Fiscal Year 2003 National MSIS Tables http://www.cms.hhs.gov/MedicaidData SourcesGenInfo/02_MSISData.asp. Revised 01/26/2006, Accessed on 8/23/2006.

NAP= Not Applicable

Table 3
New York State Annual Medicaid Savings from Three Strategies (dollars in millions)

STRATEGY	TOTAL	FEDERAL	STATE	LOCAL
Close long-term care eligibility loopholes	$960	$480	$384	$96
Reduce non-competitive rates	$2,966	$1,483	$1,063	$419
Hospital rates	820	410	205	205
Nursing home rates	1,600	800	640	160
ICF rates	546	273	218	54
Rationalize utilization	$1,912	$956	$699	$257
Increase managed care enrollment	436	218	109	109
Reduce personal care hours	1,476	738	590.4	147.6
TOTAL	$5,838	$2,919	$2,146	$772

Sources: See sources in Citizens Budget Commission, *Medicaid in New York: Why New York's Program is the Most Expensive in the Nation and What to Do About It*, April 2006.

BAD GRADES FOR SCHOOL AID

Relatively limited and badly targeted State aid for school districts is another cause of the high local tax burden. New York State provides about 51 percent of the non-federal revenue to its local school districts, a proportion less than the national average of 54 percent, making New York 31st among the 50 states in this form of aid.

State aid is generally intended to help districts with limited wealth fund an adequate package of services for their children. Without state aid, poorer districts would have to tax themselves much more heavily than wealthier districts in order to raise the same level of funding per pupil. State aid should help equalize the tax burdens among districts, but New York's programs do not do this as effectively as they should. (See Table 4.) For example, Great Neck (a wealthy community in Nassau County) is able to raise $19,149 per pupil in local revenue – nearly four times the statewide average – by imposing a tax rate of $7.70 per $1,000 of tax base – a rate little more than half of the statewide median. In contrast, Utica (a poorer upstate city) imposes a tax burden well above the statewide average, but the added effort yields less than half of the statewide median revenue per pupil ($2,272). These fiscal inequities create significant inequality in the quality education students receive due to the wealth (or lack thereof) of the families in their local district.

The School Tax Relief (STAR) program is a large and exceptionally inequitable school aid program. Created in 1997, it has grown in annual appropriations from $582 million in 1999 to $3.4 billion in the current fiscal year. STAR provides State aid to districts with the amount based on the size of a local property tax exemption granted by the local school board to its residential property owners. The allowable amount of State aid increases with the average value of homes in the district, so richer communities receive more aid than poorer communities. (A special arrangement exists for New York City where there is no separate school tax and there are relatively few homeowners.) As shown in Figure 1, the poorest districts receive the smallest amounts of STAR aid per pupil, and the wealthiest districts receive an average of 28 percent more per pupil than the poorest districts.

Table 4
Fiscal Characteristics of 11 Selected School Districts
School Year 2003–04

DISTRICT	LOCAL REVENUE PER PUPIL	TOTAL REVENUE PER PUPIL	LOCAL SCHOOL AND MEDICAID TAX EFFORT*
New York City	$6,569	$13,640	15.5
Big 4			
Buffalo	2,327	14,678	14.8
Rochester	3,601	14,594	21.5
Syracuse	2,923	13,121	17.4
Yonkers	5,352	16,922	7.6
Other Upstate Urban			
Binghamton	3,999	11,479	15.5
Utica	2,272	11,204	18.5
Upstate Rural			
Massena	4,559	12,024	17.3
Wealthy Suburban			
Great Neck	19,149	21,816	7.7
Scarsdale	16,703	19,353	7.0
Poor Suburban			
Roosevelt	4,311	18,020	10.4
Statewide Median w/o NYC	**$5,437**	**$13,480**	**13.3**

* Tax base is an equally weighted average of personal income and real property values. Medicaid data is for calendar year 2003, rate is revenue per $1,000 of base.

Sources: New York State Education Department, Office of Management Services, Fiscal Analysis and Research Unit, School District Fiscal Profiles, Masterfile for 2003–04, <http://www.oms.nysed.gov/faru/Profiles/profiles_cover.htm> (August 20, 2006); Medicaid expenditures by county from the New York State Department of Health, Medicaid Expenditures and Eligibles by County, Calendar Year 2003, http://www.health.state.ny.us/nysdoh/medstat/medicaid.htm> (August 20, 2006). Medicaid expenses allocated to school districts based on the district's share of its county's tax base.

PASSING THE BUCK ON PENSION BENEFITS AND OTHER LABOR COSTS

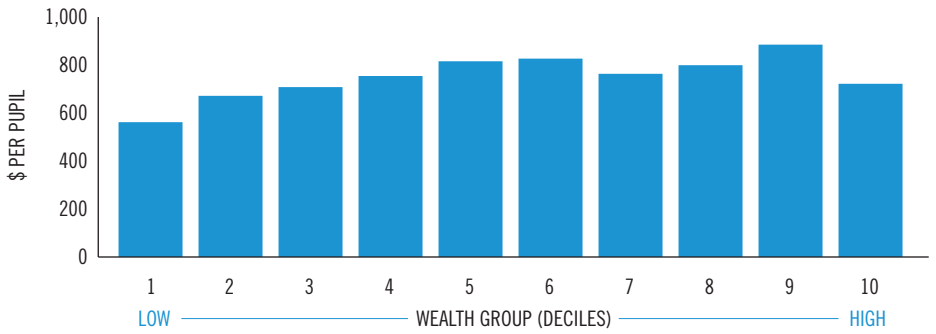
Local governments and school districts in New York employ about 1.5 million people. The compensation of these workers is set through bargaining between the elected heads of these organizations and the workers' unions, but this process is limited and constrained by State laws. The State's regulation of collective bargaining can sometimes bid up local costs. Most importantly, the pension benefits of local government employees are set by the State Legislature and are outside the scope of collective bargaining. The problem with this process is that the people deciding the cost are not the ones who must raise the money. The result is an exceptionally generous pension arrangement mandated by the State Legislature on local governments.

New York's local government employee pension arrangements do not follow the dominant model in the private sector in which employers make a set or "defined" contribution on behalf of the employee. Instead, they follow the model still prevalent among state governments in which the retired employee is entitled to a set or defined benefit based on their wages and years of service. But among the states, New York stands out for its relatively generous benefits:

- New York has a low required employee contribution. Among New York's four "tiers" of workers (groups defined based on when they were hired), only two are required to make any contribution, and in those instances contributions are 3 percent or less and are not required after 10 years of employment. In contrast, about 74 percent of state and local government employees in other systems are required to contribute more than 3 percent of their earnings.
- New York's benefit calculation formula gives credit for overtime earnings. Nationally only 6 percent of full-time state and local government employees can count overtime in their pension formula.
- New York grants "variable supplements" to retired uniformed workers in New York City. These annual payments or "Christmas bonuses" have been growing and will equal $12,000 per retiree in 2007. Other areas do not have such arrangements.

The School Tax Relief (STAR) program is a large and exceptionally inequitable school aid program... the poorest districts receive the smallest amounts of STAR aid per pupil...

Figure 1
STAR Program Payments Per Pupil by Wealth of School District
Fiscal Year 2004



Sources: New York State Education Department, Office of Management Services, Fiscal Analysis and Research Unit, School District Fiscal Profiles, Masterfile for 2003–04, <http://www.oms.nysed.gov/faru/Profiles/profiles_cover.htm> (August 20, 2006)

...unusually generous pension plans are no longer necessary for government to recruit and retain a quality workforce.

- New York has a low retirement age. There is no minimum age for police and firefighters, eligibility starts at 50 for workers in selected jobs designated as physically taxing, and at 55 for most others. In contrast, the retirement age for the federal Social Security program has been raised from 65 to 67 in recognition of increased longevity among the workforce.

Although generous pension and fringe benefit plans used to be considered necessary compensation for relatively low-paying governments, this is no longer the case. National and regional data for New York demonstrate that in many cases for the same or similar occupations, State and local government workers receive higher hourly wages than workers in the private sector. Therefore, unusually generous pension plans are no longer necessary for government to recruit and retain a quality workforce.

While pension benefits are legally outside the scope of collective bargaining, local officials can bargain with workers over other fringe benefits and cash wages. However, the framework for this bargaining is set by State law. The State's Taylor Law establishes the rules for mediation and arbitration in labor disputes, and some provisions have been used in ways that local officials feel creates disadvantages for them. The mandated criteria that arbitrators must use include a government's ability to pay, but local officials believe its relative importance should be greater. The State's system also creates opportunities for union gains in one jurisdiction to almost automatically be incorporated in the agreements for others who bargain later.

THE NEXT STEPS

The Armonk conference participants voted these four measures as the highest priorities in seeking to lower local government taxes:

1. Reduce State-mandated local government Medicaid costs more than authorized by the 3 percent cap on local growth enacted in 2005.
2. Redesign State school aid programs including STAR to better serve poorer districts and thereby lower their local school tax burden.
3. Redesign the State-mandated pension benefits for future state and local government workers through changes such as raising the minimum retirement ages, increasing the required employee contributions, eliminating inclusion of overtime in benefit calculations, and eliminating variable supplements for uniformed workers.
4. Lower Medicaid expenditures by eliminating long-term care eligibility loopholes that extend benefits to middle-class residents.

THE ARMONK AGENDA:

LOWERING AND BETTER MANAGING STATE DEBT

Debt is an important fiscal tool. However, it is essential to strike a balance between borrowing for necessary infrastructure projects and keeping debt service payments affordable with a competitive tax burden. New York State has not achieved this balance. It borrows too much, sometimes borrows for the wrong reasons, and does not always get the greatest possible benefits from its borrowed funds.

New York State... borrows too much, sometimes borrows for the wrong reasons, and does not always get the greatest possible benefits from its borrowed funds.

State debt can be divided into three categories based on the types of revenues pledged to repay the debt – government supported debt, project revenue backed debt, and private conduit debt. Government supported debt is repaid with the state government's general revenues (primarily taxes). Project revenue debt (issued by public authorities) is repaid with the revenues generated by the project; toll roads and bridges are the classic example. Private conduit debt also is issued by a public authority; it is issued on behalf of a private individual or firm in order to take advantage of federal tax exemptions (often for economic development or for private housing), and the debt is repaid by the private entity's revenues and is not legally an obligation of the government. Conduit debt is also issued by State authorities on behalf of local governments.

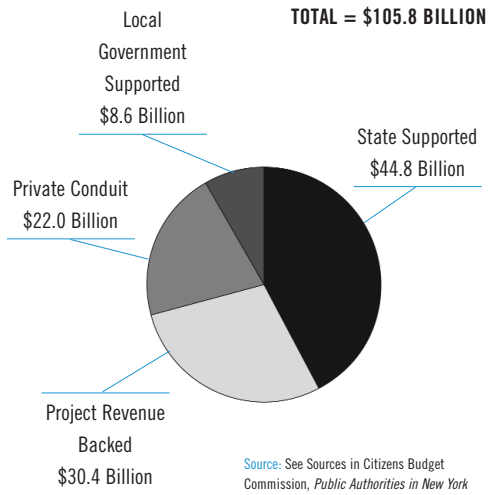
As shown in Figure 2, the State and its authorities had an estimated total of $105.8 billion in debt outstanding at the end of fiscal year 2004–05. Of that total, $44.8 billion or 42 percent was backed by State revenues. Only $3.9 billion of the State-supported debt was issued directly by the State; the rest was issued by public authorities on behalf of the State, a practice known as "backdoor borrowing" because it circumvents a State constitutional requirement that voters approve State borrowing in a referendum. Another $30.4 billion or 29 percent was borrowed by authorities and is backed by project revenues. The remainder is conduit debt issued by authorities, with the bulk issued to help private parties.

EXCESSIVE AND MISUSED STATE DEBT

The dual problems with State-supported debt are: (1) too much debt; and (2) too much of it is used for the wrong purpose. The case for the charge of excessive borrowing has been supported in research by the Citizens Budget Commission. A comprehensive measure of debt burden calculated for the 50 states shows New York to rank third and to be in a "danger zone" where the high debt burden puts New York at a competitive disadvantage. (See Figure 3.)

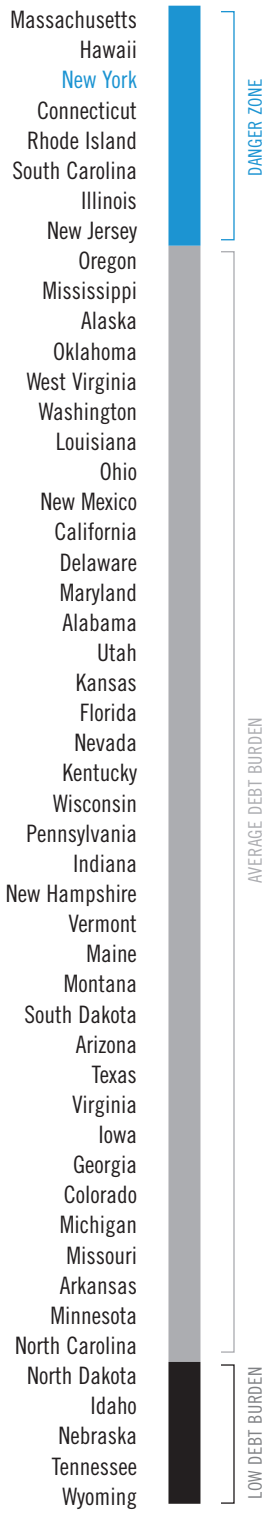
The misuse of debt arises when the State borrows in order to pay for operating deficits. Debt should be restricted to paying for long-term capital projects; it should not pass the cost of current services onto future taxpayers. However, about $11.5 billion of outstanding State supported debt, 21 percent of that total, was used to pay for operating expenses. All of this inappropriate borrowing has been done by public authorities through the "backdoor" mechanism.

Figure 2
New York State and State Authority Debt Outstanding
Fiscal Year 2005



Source: See Sources in Citizens Budget Commission, *Public Authorities in New York State*, April 2006.

Figure 3
State Debt
Danger Zone Analysis
Fiscal Year 2003



Source: Citizens Budget Commission, *New York's Endangered Future: Debt Beyond Our Means*, September 2005.

The State's growing debt has also been used to reduce earlier reliance on "pay-as-you-go" financing for capital projects. This term refers to paying for capital investments with current operating revenues, a practice that avoids debt. In recent years the State has been increasing its capital investments, but decreasing the share financed on a pay-as-you-go basis. This type of financing has fallen from 54 percent of capital spending in fiscal year 1996 to an average of 40 percent in the current capital plan, which covers five years and ends in fiscal year 2011.

LACK OF COORDINATION AND REVIEW OF PUBLIC AUTHORITY DEBT

While public authorities do extensive "backdoor" borrowing on behalf of the State, much of their financing activity is more appropriate borrowing in the form of project revenue backed debt or conduit debt. However, the projects undertaken by public authorities are not well coordinated with the State's own capital plan. The State's capital budget process does not include such coordination, yet authorities manage major elements of public infrastructure. State authorities with assets valued at more than $1 billion include the Metropolitan Transportation Authority, Thruway Authority, Long Island Power Authority, and New York Power Authority.

The project revenue backed debt and the conduit debt of public authorities is not given sufficient advance review. Such review should be adequate to protect the State from an authority taking on a project that might not be financially viable and might lead to pressure for the State to "bail out" the project. Currently, several of the State authorities are required to obtain approval from the Public Authorities Control Board (PACB) for the financing of any project. However, the current practices of the PACB suffer from three limitations: (1) much authority borrowing is exempt from PACB review; (2) the review of covered borrowings is not sufficiently rigorous or transparent; and (3) the timing of the review is typically a "last step" in the planned borrowing that can delay transactions.

THE NEXT STEPS

The Armonk conference participants voted these four measures as the highest priorities in seeking to lower and better manage State debt:

1. Discontinue issuance of State-funded debt to cover operating deficits.
2. Integrate public authorities' proposed borrowing for capital investments with the State's capital plan.
3. Subject public authority borrowing to more rigorous financial review by an enhanced Public Authorities Control Board or by the Division of Budget.
4. Reduce the State's debt by lowering capital spending and/or increasing pay-as-you-go financing as a share of total capital spending.

THE ARMONK AGENDA:

▸ MORE ACCOUNTABLE AND TRANSPARENT ANNUAL STATE BUDGETS

The process by which the State of New York shapes and adopts its annual budget lacks timeliness, accountability and transparency.

LATE BUDGETS

The State's fiscal year begins on April 1st, and its budget should be in place before then. Late budgets impair the ability of State agencies, local governments and school districts to plan and manage effectively. If they do not know how much money they will have until well into their fiscal year, they cannot use it wisely and they face risks of under-spending or over-spending. In addition, without a budget the State cannot make aid payments to school districts, causing some to have to borrow to meet cash flow needs.

Until 2005 New York had a 20-year streak of late budgets, with the delay extending into August in some years. In 2005, in response to widespread dissatisfaction with the record of late budgets, the budget was passed shortly before the new fiscal year began. In 2006 a budget was enacted in late March, but it proved to be only a temporary measure. In June the Legislature added $1.1 billion in expenditures. The Governor agreed to much of this added expense, meaning the actual budget was not put in place until well after the beginning of the fiscal year.

One factor contributing to budget delays in New York is the absence of a mechanism for fixing revenue estimates relatively early in the debates. Eight of New York's 11 competitor states have a "binding revenue forecast" mechanism that obligates the relevant parties to agree on available revenues relatively early in the process, so that debate can focus on how to use the money rather than on how much is available. The mechanisms used in other states include independent agencies or the state's comptroller.

LIMITED ACCOUNTABILITY

For democracy to work, citizens must know what their elected representatives are doing and be able to hold them accountable for their choices. This is not always the case for New York State's budget.

Accountable budgets require that decisions be informed by data relating to long-run fiscal consequences. But New York is weak in multi-year financial planning. There is no requirement that the Legislature identify and report the multi-year consequences of their actions. In this sense, the Legislature and the Governor are not accountable for the long-run consequences of their eventual agreement.

The importance of multi-year financial planning is recognized by rating agencies. With the exception of Florida, Georgia and South Carolina, states that received AAA ratings in 2005–2006 were states whose financial reporting spanned four or five years. (See Table 5.)

Table 5
Financial Plan Reporting New York, Competitors and States with High Ratings

State	Reports on GAAP Basis	Multi-Year Expenditure Forecast	Years Beyond Current Budget Cycle
NY and Competitors			
California	X	-	-
Connecticut	-	X	3
Florida	-	-	-
Georgia	X	X	1
Illinois	X	X	1
Massachusetts	-	X	1
Michigan	X	X	1
New Jersey	X	X	3
New York	X	X	2
Ohio	X	-	-
Pennsylvania	X	X	4
Texas	-	-	-
States Rated AAA/Aaa*			
Delaware	-	X	5
Florida	-	-	-
Georgia		X	1
Maryland	-	X	4
Minnesota	-	X	4
Missouri	-	X	4
North Carolina	-	X	4
South Carolina	-	-	-
Utah	X	X	5
Virginia	-	X	4
50 State Total	**20**	**32**	**(AVG. # OF YEARS) 2**

Source: National Association of State Budget Officers, "Budget Processes in the States," January 2002; National Conference of State Legislatures, "Legislative Budget Procedures," <http://www.ncsl.org/programs/fiscal/lbptabls/index.htm>, accessed March 14, 2006.

* Ratings by Moody's, Fitch, and Standard and Poor. M unicipal Bond Market Association. Research Municipal Bond Credit Report, June 2006. State General Obligation Bond Ratings, page 3. Florida rated high by S&P only; Minnesota and North Carolina rated high by Fitch and S&P only; South Carolina rated high by Moody's and Fitch only. Note that New York's GO ratings or 2006 were Aa3 (Moody's), AA (S&P), and AA- (Fitch), which are the same as the ratings for 2005.

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A glaring gap in budget accountability is the placing of large lump sums in the budget to be allocated later by "memorandum of understanding" (MOU) among the legislative leaders without wider public discussion and scrutiny. Allocating funds by MOUs, that may or may not be released for public scrutiny, reduces accountability and transparency and defeats the intended purpose of a public budget process. It also contributes to an increase in spending on "pork," items that benefit only individual legislative districts and not broader statewide goals.

Performance measurement is a management technique that can promote accountability. It helps citizens learn the impact of budget decisions on public services, and it helps agency heads use their resources effectively. Some states such as Florida and Texas have made great strides in incorporating performance measures in their budget deliberations and documents, but New York's efforts have been lackluster.

Perhaps the ultimate failure in budget accountability for a state is when it incurs an operating deficit and faces repeated budget gaps. Deficits mean that the costs of services consumed in a given year are borne by those paying taxes in another year. The individuals getting the benefits of services are not the same as those paying for them. New York State's financial performance has varied over the years, but the record includes several years with significant operating deficits. (See Table 6.) Large deficits occurred in fiscal years 2001–02 and 2002–03, and the current year is projected to have a general fund deficit of about $1.6 billion. Equally troubling is that the budget enacted for the current year is projected to lead to a budget gap in the next fiscal year of nearly $4.2 billion.

Table 6
State of New York General Fund and All Funds Surplus/(Deficit), GAAP Basis (dollars in millions)

	GENERAL FUND		ALL FUNDS	
FISCAL YEAR	ANNUAL SURPLUS/(DEFICIT)	ACCUMULATED SURPLUS/(DEFICIT)	ANNUAL SURPLUS/(DEFICIT)	ACCUMULATED SURPLUS/(DEFICIT
1995–96	380	-2,928	432	-1,234
1996–97	1,933	-995	2,060	826
1997–98	1,562	567	1,800	2,626
1998–99	1,078	1,696	1,323	3,949
1999–00	2,229	3,925	3,030	6,979
2000–01	32	3,957	1,373	9,571
2001–02	-3,420	901	-4,447	7,264
2002–03	-4,221	-3,320	-4,304	2,960
2003–04	3,039	-281	3,237	6,197
2004–05	827	546	2,110	8,307
2005–06	1,636	2,182	3,849	12,156
2006–07 (estimated)	-1,620	562	-2,553	9,603
2007–08 (projected)	-4,178	-3,616	N/A	N/A

Sources: Fiscal years 1985–86 to 2004–05 data are from State of New York, Office of the Comptroller, Comprehensive Annual Financial Report, fiscal year 1981–82 to 2004–05 editions; fiscal years 2005–06 to 2008–09 data are from State of New York, Division of Budget, "2006–2007 Enacted Budget Report", May 12, 2006, and "2006–2007 New York State FInancial Plan, First Quarterly Update", July 31, 2006.

N/A – Not Available

LIMITED TRANSPARENCY

In recent years much progress has been made in the presentation of the Governor's Executive Budget. Previously "off-budget" items have been included, more information has been provided, and its format has become easier to understand. The same is not true of the budget eventually adopted by the Legislature. This "budget" takes the form of multiple appropriations bills and is in a format that is neither easily understood nor comparable to the one used by the Governor.

The budgetary process for the public authorities also lacks transparency. While the State Comptroller reports on the financial results of major State public authorities in that office's comprehensive annual report, much less information on authorities has been available as part of the State budget process or from the authorities themselves. The Public Authorities Accountability Act passed in 2005 and recent regulations issued by the State Comptroller address some of these deficiencies. The Authority Budget Office created by the new Act and the Comptroller's efforts have the potential to improve significantly the transparency of public authorities. However, it is unknown whether the two offices will effectively coordinate their efforts or cooperate to produce a "big picture" perspective on the finances and performance of the multiple state and local authorities.

NEXT STEPS

The Armonk conference participants voted these four measures as the highest priorities in seeking to enhance accountability and transparency:

1. Prepare more extensive multi-year financial plans.
2. Enforce and build upon new requirements for reporting by public authorities.
3. Require that lump-sum appropriations meet specific program criteria and be subject to sunshine provisions.
4. Publish the Adopted Budget in a format similar to the Executive Budget.

Accountable budgets require that decisions be informed by data relating to long-run fiscal consequences.

Deficits mean that the costs of services consumed in a given year are borne by those paying taxes in another year.

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