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ABSTRACT

This report provides an overview of New York State's 1999-00 budget. The analysis states that spending for 1999-00 increased by $2.7 billion over the previous year. It portrays a dire situation in which projected budget gaps will be approximately $2.8 billion in 2000-01 and $4.6 billion in 2001-02. The budget does feature planned, year-end fund balances, but the level of nonrecurring resources also increased. It describes how most of the budget's spending increases are driven by current law and the legislative rejection of proposed cuts, rather than by program expansions. The text focuses on how education, local governments, and health and social services fared in the budget. It details how a 7.8 percent state-aid increase is provided for the 1999-00 school year, bringing total aid to more than $12.6 billion. However, this increase is diminished by the budget's failure to advance the equity of the aid distribution and by the lateness of the budget. Local governments received a small, year- to-year increase in revenue sharing aid, and Medicaid received no new cuts. A multiyear tax cut was enacted, but it is claimed that under other measures the budget would have constituted a tax increase. Finally, a description of a five-year capital plan is offered. (RJM)

1999-00 BUDGET ANALYSIS

Review of the Enacted Budget

September 1999

STATE OF NEW YORK COMPTROLLER
EXCELSIOR

H. Carl McCall
State Comptroller

State of New York
Office of the State Comptroller
Office of Fiscal Research & Policy Analysis
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STATE OF NEW YORK
OFFICE OF THE STATE COMPTROLLER

September 1999

To the People of the State of New York:

In a time of relative prosperity, this year's State budget has reached a new low, in both process and result. It was a failure in terms of timeliness, openness and thoughtfulness. The negotiations were carried out in the traditional closed, three-way process and were marked by a level of acrimony and recrimination unusual even for Albany. The mid-summer "conference committee" process was no more than a bad joke — a charade carried on while everyone knew that the real decisions had already been made, or were being made, by three men in a room.

Not surprisingly, the results were bad. In a period of relative financial ease, the leaders nevertheless found need to stuff the budget with all sorts of manipulations, one-shots and other tricks. These actions are objectionable even under dire fiscal circumstances — they are inexcusable in the current environment.

The budget crafters rallied around the Governor's proclaimed conviction that spending growth should be kept below inflation. Various manipulations were contrived to meet this goal, at least in the General Fund ledger, but the truth is that State spending is rising at about one and a half times the rate of inflation. A positive goal of reserving the year-ending $1.8 billion surplus was accomplished, but only after employing nearly $600 million in one-shots. It would have been wiser and more straightforward to avoid these actions and instead reserve less of the surplus. The funds carried over will ease fiscal conditions in the upcoming year or two, but these funds are not recurring resources and the State continues to face a structural imbalance. Estimated budget gaps are $2.8 billion in 2000-01 and $4.6 billion in 2001-02.

New tax cuts were enacted, but only at the expense of delaying the promised elimination of the sales tax on clothing. In fact, as historically counted by the National Conference of State Legislatures, this year's budget action would have constituted a tax *increase,* because the sales tax deferral was greater than the new cuts added. Tax cuts enacted without a solid plan and paid for by sweeping financial problems under the rug may have unintended and difficult consequences in the long run. It would have been better to stand by the promises already made.

The budget contained positive restorations for education and other programs, but in almost every case, the real news was not nearly as good as claimed in the press releases. For example, there was an incremental increase in revenue sharing for local governments, but the funds were delivered in part through an artificial accounting spin-up while the budget reneged on a promise to evaluate and reform the program. Further, the Legislature failed to address the fiscal difficulties many local

governments continue to experience. Nassau County's severe financial and management problems were papered over by giving them a new tax without any oversight, despite an egregious record, making the need for such oversight painfully obvious.

Even with a record increase in school aid, the budget failed to materially advance either efficiency or equity in the aid distribution. As usual, the formulas were manipulated until the traditional regional shares were produced. Most needy school districts would have done better if the Legislature had simply rejected the Governor's cuts and allowed the present law formulas to operate along with the planned expansion of the LADDER programs. The lateness of the budget also resulted in higher-than-necessary taxes in some districts and clearly diminished the effectiveness of the incentive aid programs it contains. For higher education, a series of additions were trumpeted, but most only partially covered the cuts of earlier years. In truth, SUNY and CUNY have been subjected to large budget cuts this year. The small additions for faculty, opportunity programs and child care are completely overshadowed by large unfunded costs for collective bargaining increases, inflation and at SUNY, a sizable hospital revenue shortfall.

The State simply cannot afford to follow this irresponsible path, staggering from year to year without a plan as New Yorkers face an enormous debt burden and the embarrassing annual budget debacle leaves fundamental problems unaddressed. If there is a silver lining anywhere to be found in this year's dismal performance, it may be that New Yorkers have had enough, and that everyone involved in the process finally decides this cannot go on.

Sincerely,

Carl McCall

H. Carl McCall,
State Comptroller

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Overview

All Funds spending increases by $2.7 billion to $73.3 billion, representing growth of 3.8 percent. Reported General Fund spending increases 2.4 percent to $37.4 billion. However, spending is affected by a number of accounting transactions that masks underlying spending growth. When these accounting transactions are excluded, General Fund spending increases 3.5 percent, or 1.4 times the rate of projected inflation, and State Funds spending goes up 4.2 percent, or 1.8 times the inflation rate.

Most of the 1999-00 spending increases, when compared to the Executive Budget, are driven by current law and the legislative rejection of proposed cuts in education and Medicaid, rather than by program expansions. Even the large education aid increase was driven by the phase-in of multiyear programs and by general growth in current school aid formulas. The General Fund budget was balanced with virtually no spending cuts.

Multi-Year Impact of the Budget

The gap estimates presented in the Executive Budget were understated by more than a billion dollars due to the inclusion of unspecified savings and the exclusion of collective bargaining costs. The enacted budget further increased projected gaps.

The State Comptroller estimates future budget gaps will be approximately $2.8 billion in 2000-01 and $4.6 billion in 2001-02. These gaps remain a serious problem for the State. The underlying structural problem is even more apparent without the planned use of the surplus. Without the use of the surplus, these gaps grow to $3.4 billion in 2000-01 and $5.8 billion in 2001-02.

Reserves

One of the positive elements of the enacted budget is the planned, year-end fund balances. In addition to setting aside the $1.82 billion in surplus, the Debt Reduction Reserve Fund deposit increases by $250 million. Reserves, including amounts for future welfare needs, reach nearly $3.4 billion, representing 8.6 percent of General Fund receipts. However, more than one-half of the planned reserves, the $1.82 billion surplus, is expected to be used for budget balancing in 2000-01 and 2001-02.

Non-recurring Resources

The level of non-recurring resources used in the enacted budget increases ten-fold from $64 million last year to nearly $600 million in 1999-00. This is particularly disturbing given the current robust economy. The use of significant one-time revenues to balance budgets was common practice

during economic recessions. The use of non-recurring resources to fund ongoing spending exacerbates future budget imbalance.

Education

School Finance

A $913 million, 7.8 percent state aid increase is provided for the 1999-2000 school year (instead of the $269 million increase proposed by the Governor), bringing total aid to more than $12.6 billion. The Legislature restored the multiyear early childhood and other programs known as the LADDER initiatives.

Even with the large increase in aid, the budget failed to materially advance either the efficiency or the equity of the aid distribution, and most high needs districts would have done better under present formulas without the budget's modifications. The lateness of the budget may have also resulted in higher than necessary taxes in many districts and diminished the effectiveness of the LADDER incentive programs such as pre-kindergarten aid.

Newly required school "property tax report cards" will contain inaccurate information if the State budget continues to be late. It is likely that schools will have to guess about prospective property tax rates without knowing how much state aid they are receiving. Next year, for example, a budget would have to be enacted far enough in advance of the April 22 data submission deadline for school districts to correctly calculate property tax rates.

Higher Education

$150 million was added to the Executive's proposal, the majority of which ($103 million) restored a proposed TAP cut. Most of the other additions, including those for opportunity programs and more full time faculty, were smaller than last year's restorations (subsequently vetoed). SUNY state-operated institutions and CUNY senior colleges lack funding for collective bargaining increases, normal inflation and other costs. These unfunded costs (totaling $58 million at SUNY and $33 million at CUNY) far outweigh the additions for full-time faculty lines, opportunity programs and child care ($5.6 million for SUNY and $4.3 million for CUNY).

A $77 million shortfall at the SUNY Hospitals has resulted in an impoundment of appropriations by the Governor's Budget Director. This action requires the SUNY Board of Trustees to choose between spending reductions at the campuses (reallocating student tuition revenues) or the hospitals (with patient service implications and causing further revenue problems). A tuition increase has also been discussed. Without additional State funding, the hospital shortfall can only be met by taking funds from other purposes or by using temporary solutions such as borrowing.

The independent colleges and universities received incremental increases for the HEOP opportunity program and Bundy direct institutional aid. An increase in the maximum TAP grant sought by these institutions was not provided and the $4,125 maximum grant today covers only about 25 percent of average tuition compared to 40 percent in 1990 and 60 percent in 1974.

Tax Cuts

The enacted budget included a multi-year tax cut package that costs $375 million when fully implemented. The major components of this package include a tax rate reduction for banks and insurance companies and an enhancement of the State Earned Income Tax Credit for lower-income working families. The remaining $100 million is used for 25 different small, extremely targeted tax cuts that have questionable job creation potential.

New tax cuts were enacted while implementation of the permanent sales tax exemption for clothing was delayed for three months. In fact, as historically counted by the National Conference of State Legislatures, this year's budget action would have constituted a tax increase of $42 million, because the sales tax deferral was greater than the new cuts added.

Local Governments

A small, year-to-year increase in revenue sharing aid was provided, but a statutorily constituted task force to evaluate the formula and institute reforms failed to issue its report. Additionally, an accounting spin-up was also used to provide one-time relief to 14 cities. County governments face increased costs and reduced reimbursements for Medicaid, social service and criminal justice programs.

Despite continuing indications of fiscal stress among local governments, the legislation proposed by the State Comptroller, in conjunction with the Governor, to address that issue was not passed. The legislation would have promoted fiscal stability among local governments by providing an early warning of fiscal stress and a standby system for oversight and relief when local situations warrant it.

The budget's response to Nassau County's fiscal problems — adding a new tax without any additional State oversight — is only a stopgap solution. The Comptroller's Office will continue to monitor the situation in Nassau County, but it appears that a stronger oversight mechanism or supervisory board will be necessary to address the problems.

Health and Social Services

The enacted budget includes no new Medicaid cuts. Almost all of the old cost containment measures expired for one quarter but were later reinstated as of July 1, 1999. In contrast to proposed provider cuts of $848 million proposed in the Executive Budget, providers are estimated to receive additional Medicaid revenues of $206 million due to the changes.

Welfare caseloads continue to decline. The federal funding windfall will be used for State and local government fiscal relief, child care funding increases, and further deposits to the contingency fund.

New York is estimated to receive approximately $25 billion over the next 25 years from the tobacco settlement. The final budget created a fund to receive monies, but decisions on its use were deferred.

Debt and Capital

The five year capital plan will be updated for changes made in the enacted budget on or before November 1, 1999. Preliminary analysis indicates that capital spending increases by $328 million. Most of this added spending results in increased debt.

The enacted budget also includes plans to replace the Local Government Assistance Corporation (LGAC) capital reserves with a surety bond. The freed-up reserves would be used to defease outstanding LGAC bonds. It is unclear whether this transaction will result in true economic savings. Absent these savings, it would appear the transaction is being pursued for public relations purposes to simply offset the debt added during budget negotiations.

OVERVIEW OF THE ENACTED BUDGET

This section provides a summary description of the State budget, focusing on the financial plan and changes from the Executive Budget. Most of the spending increases contained in the 1999-00 enacted budget are driven by current law and the legislative rejection of proposed cuts, rather than by program expansions. Even the large education aid increase was driven by the phase-in of multiyear programs and by general growth in the current school aid formulas. The General Fund budget was balanced with virtually no spending cuts. It also retained the $1.82 billion cash surplus from 1998-99 for use in future fiscal years. This was possible because of the following:

✓ Tax collections continue to be robust, despite $1.8 billion in tax cuts being phased in during 1999-00. Excluding the impact of the rollover of the 1998-99 surplus, revenues increased approximately $752 million. Most of this increase is in the personal income tax and is driven by the boom in incomes led by strong financial markets.

✓ Growth for entitlement programs continues to be moderate, with public assistance caseloads declining and moderate Medicaid growth.

✓ Certain non-recurring resources of approximately $400 million are used to offset increased spending.

Overall State Spending

According to the financial plan released by the Division of Budget (DOB), All Funds[1] spending in the budget totals $73.3 billion, an increase of $2.7 billion or 3.8 percent; with State Funds spending increasing at a slightly higher rate of 3.9 percent, and General Fund spending increasing at 2.4 percent.

Spending is understated through the use of several offsets to spending. Without these accounting actions, that are designed to deflate growth, General Fund spending growth would be 3.5 percent — 1.4 times the rate of inflation and State Funds spending would grow 4.2 percent or 1.8 times the inflation rate.

[1]All funds includes State funds plus federal funds. State funds is spending from state imposed taxes, fees and other charges; State funds includes dedicated funds, such as the Lottery. The General Fund contains all state-imposed taxes and fees that are not dedicated to a specific use.

Spending by Fund Type
1999-00 Enacted Budget
(dollar amounts in billions)

Comparison Basis:	Spending	Change	DOB Growth	Adjusted Growth	98-99 Growth
All Funds	$73.3	$2.7	3.8%	4.0%	6.2%
State Funds	$49.8	$1.9	3.9%	4.2%	8.4%
General Fund	$37.4	$0.9	2.4%	3.5%	6.9%

1999-00 General Fund Spending

General Fund spending is projected to increase by $868 million in 1999-00. Almost all the spending increase is due to increased education spending of $908 million (on a fiscal year basis). Other spending for community-based mental hygiene programs, local transportation funding, and revenue sharing increases by $282 million. State operations spending is projected to increase by more than $200 million primarily due to expected increases in payroll costs driven by collective bargaining.

General Fund spending is being offset by a number of accounting actions that reduce the reported growth. These offsets total approximately $400 million. Without the benefit of these offsets, spending would grow to $1.3 billion, or 3.6 percent. The offsets include:

- $250 million transferred out of the Medical Malpractice Insurance Association fund and placed in a special revenue fund to offset General State Charges (GSC) spending. The budget provides for the eventual dissolution of this association and such privatization is expected to produce an additional estimated benefit of $250 million in 2000-01 which is also expected to be used as an offset against GSC spending. There is no programmatic relationship between MMIA and GSC; this is purely an accounting manipulation to reduce General Fund spending levels.

- $100 million from non-recurring excess balances in pools related to the old hospital reimbursement system (NYPHRM) are used to directly offset Medicaid spending. Normally, these types of fund balances are transferred to the General Fund for budget relief. The balances in these pools were allowed to accumulate. This has the effect of depressing State Funds and All Funds spending.

- $45 million from current Health Care Reform Act (HCRA) pools is used to directly offset Medicaid spending. This is expected to provide a one-time reduction in Medicaid spending. This also reduces State Funds and All Funds spending.

- $46 million in General Fund savings from counting an increase in the earned income tax credit (EITC) as part of the minimum State public assistance spending levels required by the

federal government. The EITC is a refundable credit provided to lower income working families. The addition of these expenditures allows the State to lower General Fund public assistance spending by substituting federal block grant funds. This action is expected to generate recurring and increasing General Fund relief in the future.

Change in 1999-00 General Fund Spending
Over 1998-99
With and Without the use of Offsets
(in millions)

Spending Category	Increase with Offsets	Percent Change	Increase without Offsets	Percent Change
Education	$908	7.2%	$908	7.2%
Medicaid	($28)	-0.5%	$117	2.1%
Social Services	($252)	-8.6%	($252)	-8.6%
Other [2]	$282	7.8%	$282	7.8%
State Operations	$207	3.1%	$207	3.1%
General State Charges	($222)	-9.8%	$28	1.2%
Debt service	$2	22.2%	$2	22.2%
Transfers to Other Funds	($29)	-1.0%	($29)	-1.0%
Total	$868	2.4%	$1,263	3.5%

1999-00 General Fund Receipts

General Fund receipts are estimated to increase by $2.6 billion, or 7.0 percent, over 1998-99. However, this increase includes the 1998-99 surplus of $1.82 billion, which is counted as a receipt in 1999-00 ("the rollover"). When receipts are adjusted to reflect surplus rollover set aside for future use, the total receipts available in 1999-00 decreases to $752 million, an increase of 2.0 percent over 1998-99. The growth in taxes is almost entirely attributable to the personal income tax and higher collections associated with strong financial markets.

[2] This category would include community-based mental hygiene, local transportation, and revenue sharing.

1999-00 General Fund Receipts
Change from 1998-99
(in millions)

Revenue Category	Change
Personal Income Tax	$2,872
User Taxes and Fees	$105
Business Taxes	($230)
Other Taxes	($137)
Total Taxes	$2,610
Miscellaneous Receipts	($142)
Transfers to Other Funds	$99
General Fund Receipts	$2,567
Surplus to be carried into 00-01	($1,815)
Available General Fund Receipts	$752

Reported growth in receipts does not reflect the strength of the economy. Tax cuts and accounting actions reduce reported growth by $2.5 billion ($1.76 billion in tax cuts and $661 million in STAR). STAR is the local school tax reduction program funded by the State. Absent these actions, receipts would have grown an estimated 8.8 percent.

Non-Recurring Actions

Non-recurring resources are estimated to total $573 million. This is a disturbingly high level given the current strength of the economy and the existence of a $1.82 billion planned surplus. These actions resemble the poor financial practices used to balance precarious budgets in the early 1990's recession. Non-recurring resources in 1998-99 were only $64 million, and none of them were objectionable. The 1999-00 enacted budget includes:

- A three month delay in implementing the permanent sales tax clothing exemption. Instead, two temporary week-long sales tax clothing exemptions were added. The net result of these actions was to deprive taxpayers of an estimated $100 million in tax savings and provide one-time resources for the financial plan. This was done as additional tax reductions were promised.

- The enacted budget directed Medical Malpractice Insurance Association (MMIA) to transfer $250 million to a special revenue fund that will be used to offset General State Charges spending. MMIA was established in 1983 to provide excess liability insurance to doctors and medical providers. This fund has been raided a number of times in the past; this year's raid brings the total transfers (including interest) to nearly $1 billion. In addition, legislation

provides for the sale of MMIA; the proceeds, expected to be received in 2000-01, will once again be used to offset spending.

- One-time financial plan benefit is provided by the transfer of $100 million from excess balances in NYPHRM pools and $45 million from HCRA pools.
- Permanently deferring one month of Supplemental Security Income (SSI) payments to the federal government generates $45 million.
- Other non recurring resources include: $15 million in loan repayments from the Long Island Power Authority (LIPA), $8 million from the sale of the state office building at 270 Broadway, and debt recovery activities from outstanding traffic tickets.

1999-00 Non-recurring Actions
(in millions)

Description	Amount
Medical Malpractice Insurance Association Transfer	$250
Excess NYPHRM pool balances	$100
Delayed sales tax exemption for clothing	$100
Offset from HCRA pools	$45
11 instead of 12 SSI payments	$45
Other	$33
Total	$573

Changes from Executive Budget

The following table summarizes the changes in available resources and uses from the proposed to enacted budget. Most of the spending additions to the Executive Budget were restorations of proposed cuts in education, health, and higher education. The significant resources included: revenue and spending re-estimates of at least $463 million, mostly in the income tax, sales tax and Medicaid; the MMIA transfer of $250 million; rejection and postponement of proposed and scheduled tax cuts of $223 million; and $191 million in other spending offsets.

Changes from the Executive Budget to the enacted budget
Identified Resources and Uses
(in millions)

Amt	Resources	Amt	Uses
$313	Revenue Re-estimates	$360	School Aid and Other Education
$250	Medical Malpractice Insurance Fund	$355	Health (Medicaid)
$150	Spending Re-estimates	$200	Legislative and Executive Initiatives[3]
$123	Provider Assessments continuation	$150	Higher education
$100	Unexpended balances in NYPHRM pools	$15	Mental Health
$100	Deferral of sales tax clothing exemption	$9	Human Services
$46	Maximization of TANF funds	$10	Criminal Justice
$45	Redirecting of certain HCRA pools	$12	Economic Development
$4	Reprogramming Executive Proposals	$11	Transportation
		$11	General Government
		$1	Debt
$1,131	TOTAL	$1,134	TOTAL

In addition to the resources and the uses identified above, there were up to $200 million in other actions included in the budget. For example, Quickdraw expired for four months, additional lottery revenue raising proposals were partially rejected, certain fee increases proposed by the Governor were rejected, and proposed changes to the STAR program were excluded. These actions decreased revenues compared to the Executive Budget. The lower revenues were offset by available resources including additional revenues available from enacting a lower cost tax cut plan than proposed by the Governor and additional spending reestimates. The net impact on the financial plan is zero, nonetheless, under past practices these actions would have been publicly disclosed and included in the list of resources and uses.

[3] The publicly reported figure of $170 million represented only the legislative initiatives. When the Executive initiatives of $30 million are included the total is $200 million.

Reported Spending Growth

The spending additions to the Executive Budget were reported to be approximately $1.1 billion. However, reported General Fund spending grows by only $213 million from the level proposed in the Executive Budget after 30 day amendments. The difference is the result of spending re-estimates, spending offsets, and other actions that modified Executive proposals.

Comparison of 1999-00 Spending Levels Proposed by the Executive and Enacted
(in billions)

Comparison Basis:	Executive Budget	Enacted Budget	Change
General Fund	$37.1	$37.4	$0.2
State Funds	$49.3	$49.8	$0.5
All Funds	$72.7	$73.3	$0.6

In order to reconcile General Fund spending in the Executive Budget with enacted spending a number of adjustments need to be applied to the $1.1 billion in gross spending additions. The following actions were included in the enacted budget and result in the wide difference between gross spending increases and reported spending growth.

- ✓ General Fund spending offset of $250 million from the MMIA transfer.
- ✓ Accounting modification in the way the $250 million Debt Reserve Reduction Fund (DRRF) is treated.
- ✓ General Fund spending offset of $145 million from the transfer of monies from certain health related pool balances.
- ✓ Spending re-estimates of $150 million, primarily in Medicaid.
- ✓ General Fund spending offset of $46 million from maximizing federal welfare grant spending.
- ✓ Other adjustments of $80 million, consisting primarily of reductions to Executive proposals.

1999-00 Enacted Budget
Spending Changes from Proposed Executive Budget
(in millions)

Description	Amount
Gross Spending Additions	$1,134
MMIA transfer	($250)
DRFF accounting	($250)
Health care pool transfers	($145)
Spending reestimates	($150)
Maximizing federal welfare funding	($46)
Other actions [4]	($80)
Total	$213

[4] Other actions include reductions to Executive proposals and further spending reestimates.

Revised Out-year Gap Estimates

Estimates of the future impact of the adopted 1999-00 budget are presented here to fill a void in the existing State budget process. The Governor is required in his Executive Budget submission to include a financial plan projection for the two years following the budget to allow an evaluation of the State's financial condition and to measure the impact of the Executive Budget. There is no similar requirement for the enacted budget.[5]

The methodology used to prepare the estimates in this report uses the Executive Budget's original forecast and then makes adjustments based on changes included in the enacted budget. The OSC gap estimates for the enacted budget assume the use of the 1998-99 surplus that was set aside in this year's budget as proposed by the Governor. The utilization of the surplus reduces gaps by approximately $615 million in 2000-01 and $1.2 billion in 2001-02.

The estimated gaps presented in the Executive Budget were understated by nearly $1 billion by incorporating unspecified savings in 2000-01 and 2001-02 and failing to incorporate collective bargaining costs. The OSC estimates exclude the unspecified savings because there is no articulated plan on how the Executive plans to achieve them. The OSC estimates incorporate the same assumptions for collective bargaining as does the Executive's revised estimates. When OSC adjustments are made to the Executive Budget estimates, the Executive Budget projected gaps become $2.1 billion in 2000-01 and $3.0 billion in 2001-02.

After reflecting changes made in the enacted budget, OSC projects budget gaps of $2.8 billion in 2000-01 and $4.6 billion in 2001-02. The increase of nearly $800 million in 2000-01 between the time of the proposed budget and the enacted budget represents the annualized impact of spending additions (primarily in education). In addition, OSC assumes there will be spending for legislative initiatives, the Executive does not. Although this spending is not statutorily required, historically enacted budgets include it. An upward revision in out-year revenue estimates helps to offset the loss of certain non-recurring resources. In 2001-02, the estimated gap is projected to increase by nearly $1.6 billion, largely due to the same factors.

[5] The Executive's preliminary estimate of the 2000-01 gap is $1.9 billion, without any of the OSC adjustments. However, these estimates are not officially revised until the next Executive Budget submission. No estimate has been made by the Executive with respect to the 2001-02 gap. The Executive estimate is approximately $900 million lower than the OSC estimate primarily because it includes unspecified savings and lower projections for education and legislative initiative spending. OSC assumes continuing phase-in of LADDER, additional school aid increases of $250 million annually, and reasonable inflation for expense-based education aid.

Revised Estimate of Future Gaps
(in billions)

State Fiscal Year	Executive Budget	OSC Adjusted Executive Budget	Enacted Budget	Change: Adjusted Executive to Enacted
2000-01	$1.143	$2.093	$2.772	$0.795
2001-02	$2.071	$3.046	$4.574	$1.566

Source: Office of the State Comptroller. OSC adjustments exclude unspecified savings and include collective bargaining costs.

Future budget gaps remain a serious problem for the State, particularly in 2001-02 when the gap is estimated to reach $4.6 billion. These estimates understate the extent of the ongoing, underlying, structural imbalance. Without the use of the surplus, the gaps would be $3.4 billion in 2000-01 and $5.8 billion in 2001-02.

The future gaps could be decreased if growth in receipts is better than projected and growth in spending is lower than anticipated. Large upward revenue reestimates have been common for the past three years, and may continue in the future, especially if financial markets continue to perform well. In addition, if welfare and Medicaid caseloads continue to decline and prices remain stable, expenditures could be lower than projected, which would also reduce the gaps. However, revenues could trend lower if Wall Street suffered a significant downturn. A general economic recession is also always a major budget risk.

Reserves

The enacted budget includes almost $3.4 billion reserved for specific future spending needs or rainy day funds. This amount represents 8.6 percent of total General Fund receipts and is much higher than it has been in the recent past. However, more than one-half of this amount, $1.8 billion from the 1998-99 surplus, is expected to be spent in the next two years and does not represent a long-term rainy day fund.

Reserves
(millions)

Source	Amount
Tax Stabilization Reserve Fund	$473
Contingency Reserve Fund	$100
1998-99 Surplus	$1,815
Set-aside for future welfare needs	$548
Set-aside for future child care needs	$200
Debt Reserve	$250
Total	$3,386

These reserves have been created for a variety of purposes, including:

- The use of the Tax Stabilization Reserve Fund is restricted to unplanned budget deficits.

- The Contingency Reserve fund was created to provide reserves that the State could use for litigation-related costs.

- The 1998-99 surplus is set aside to be used for budget balancing purposes. The Executive plans to use $615 million in 2000-01 and the remaining $1.2 billion in 2001-02.

- The reserves related to welfare, $548 million and $200 million, are the result of excess federal funding. The contingency fund for future welfare needs provides a cushion for increased spending resulting from higher caseloads in the event of an economic downturn. The set-aside for child care provides additional funding over the next three years for increased child care needs related to stricter work participation requirements.

While almost all of the above funds have been earmarked for certain purposes, it is possible, with appropriate statutory changes, to use these monies, with the exception of the federal welfare funds, for other purposes. The only clear reserve for economic hardship is the Tax Stabilization Reserve Fund. This type of reserve needs to be expanded to ensure that the State is prepared for an economic downturn.

School Finance

A $913 million, 7.8 percent increase in State aid for the 1999-2000 school year is provided, bringing total aid to more than $12.6 billion. The enacted budget is $644 million higher than the Executive's original proposal (a $269 million, 2.3 percent increase was proposed).[6] The increase was produced by restoring the Executive's proposed cuts and elimination of multiyear early childhood and other programs known as the LADDER[7] initiatives, as well as by growth in the general aid formulas, with some modification.

The Executive's press release on the enacted budget accurately described this year's increase as the largest ever and the last three years as the three largest aid increases in school aid history.[8] Interestingly, however, the increase in aid is identical to the increase that would have been driven by the operation of current law aid programs and formulas without any modification (also $913 million). Further, the changes made in many ways failed to materially advance either the efficiency or the equity of the aid distribution.

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[6]Other education appropriations were increased by $62 million. Together with the school aid appropriations this results in a State fiscal year increase of $360 million above the Executive Budget. See this report's financial overview section for a discussion of the continuing costs of the school aid addition. Note: 9/1/99 State Education Department reestimates show a $948.8 million school year increase, largely due to decreased 1998-99 building aid estimates. This report uses the aid estimates and computer runs presented with the enacted budget.

[7]The LADDER acronym stands for Learning, Achieving and Developing by Directing Educational Resources. These programs, which include pre-kindergarten, class size reduction and minor maintenance aids, were initiated by the Assembly and enacted in 1997, along with the Executive's STAR tax reduction proposal.

[8]Although in the last three years the highest dollar increases in school aid were provided, they did not represent the highest percentage increases. For example, three aid increases during the 1980's were higher in relative proportion:

School Year	School Aid Increase*	% Increase
1999-00	$913 million	7.8%
1998-99	$851 million	7.8%
1997-98	$679 million	6.6%
1987-88	$621 million	9.3%
1984-85	$511 million	10.6%
1980-81	$323 million	9.1%

*As estimated at the time of budget enactment

Source:

Division of the Budget school aid tables and publications, including annual reports entitled: Description of New York State School Aid Programs

School Aid Changes

The enacted budget's increase primarily restores cuts proposed by the Executive while also tinkering with the existing aid formulas and the "transition adjustment" (a calculation that regulates the changes in aid under the largest general aid formulas). The Legislature rejected the Governor's elimination of the LADDER programs, restoring the pre-kindergarten, class size reduction, full-day kindergarten, and minor maintenance programs at planned funding levels. Other recommended cuts were also rejected, including those for BOCES, building aid, limited English proficiency grants, and aid freezes in several categories. A new category of aid for districts meeting certain tax effort specifications was provided (in apparent substitution for a tax freeze/limitation incentive aid program previously enacted but canceled before scheduled implementation this year).[9] Teacher support aid was restored — a $67.5 million program going to the big five cities that was eliminated by veto last year. Also, $145 million was provided to fund the RESCUE program for extraordinary school capital needs. This program was enacted last year but the funding was vetoed; the funds will be provided through State bonding in the capital budget and thus are not included in the $913 million increase.

The Executive Budget had proposed a significant simplification and consolidation of the aid formulas, including a block grant approach for many current categorical aids. These proposals would have provided school districts greater flexibility and allowed for a more accurate and efficient aid calculation, but unfortunately were made in a way that was highly damaging to equity. For example, school district wealth was removed as a factor from the largest portion of the aid calculations and an alternative calculation was made giving the largest increases in aid to districts which had recent enrollment increases (which, on average, tended to be the wealthier districts).[10] Additionally, by including the LADDER incentive programs in the block grant approach, these programs were essentially eliminated. The rejection of the Executive's proposals is thus fortunate from an equity perspective, but it leaves the issue of the inefficiency of the current aid formulas unaddressed.

Aid Distribution

Although the Legislature rejected the Governor's recommendations to remove relative wealth from the operating aid formula and other cuts that would have hurt many needy districts, particularly large urban districts, this budget does not move forward toward greater equity among high- and low-wealth districts, despite the large overall aid increase.

As usual, the budget took an approach that preserves the "shares" of aid going to various regions and types of districts. As demonstrated in the following table, each major regional category receives virtually the same share of aid in 1999-00 as they received in 1998-99, although they

[9]The incentive program was so unworkable as to have been eliminated in the Executive Budget, with its focus on property tax limitations. However, the new aid program duplicates existing high tax effort aid programs (*1999-2000 Final Budget Summary*, N.Y.S. Council of School Superintendents, August 1999).

[10]See *1999-00 Budget Analysis, Review of the Governor's Proposed Budget*, Office of the State Comptroller (February 1999).

received marginally different percentage increases and shares of the increase. The small cities were the only group that can be said to have received even a modest shift, and since they are generally higher needs districts, their having done worse on average than other districts is certainly not an improvement. A status-quo approach of this kind cannot materially address the existing disparities in funding.

Regions/ Types of School Districts	No. Of Districts	CWR	1997-98 Enrollment	1998-99 Combined Aid	1999-00 Combined Aid	Increase	Aid %
Statewide	682	1.170	2,858,300	$11,211,960,278	$12,133,872,870	$921,912,592	8.2%
New York City	1	0.940	1,068,796	$4,013,503,001	$4,348,433,264	$334,930,263	8.3%
Rest of State	681	1.171	1,789,504	$7,198,457,277	$7,785,439,606	$586,982,329	8.2%
Big 4 Cities	4	0.669	130,534	$679,942,807	$730,105,480	$50,162,673	7.4%
Small Cities	57	0.830	257,736	$1,136,724,341	$1,199,144,523	$62,420,182	5.5%
Downstate Suburbs	168	2.292	566,162	$1,683,336,517	$1,820,372,343	$137,035,826	8.1%
Upstate Suburbs	271	0.825	631,429	$2,567,389,787	$2,790,421,479	$223,031,692	8.7%
Rural	181	0.766	203,643	$1,131,063,825	$1,245,395,781	$114,331,956	10.1%
				Percentage Shares			
New York City			37.4%	35.8%	35.8%	36.3%	
Rest of State			62.6%	64.2%	64.2%	63.7%	
Big 4 Cities			4.6%	6.1%	6.0%	5.4%	
Small Cities			9.0%	10.1%	9.9%	6.8%	
Downstate Suburbs			19.8%	15.0%	15.0%	14.9%	
Upstate Suburbs			22.1%	22.9%	23.0%	24.2%	

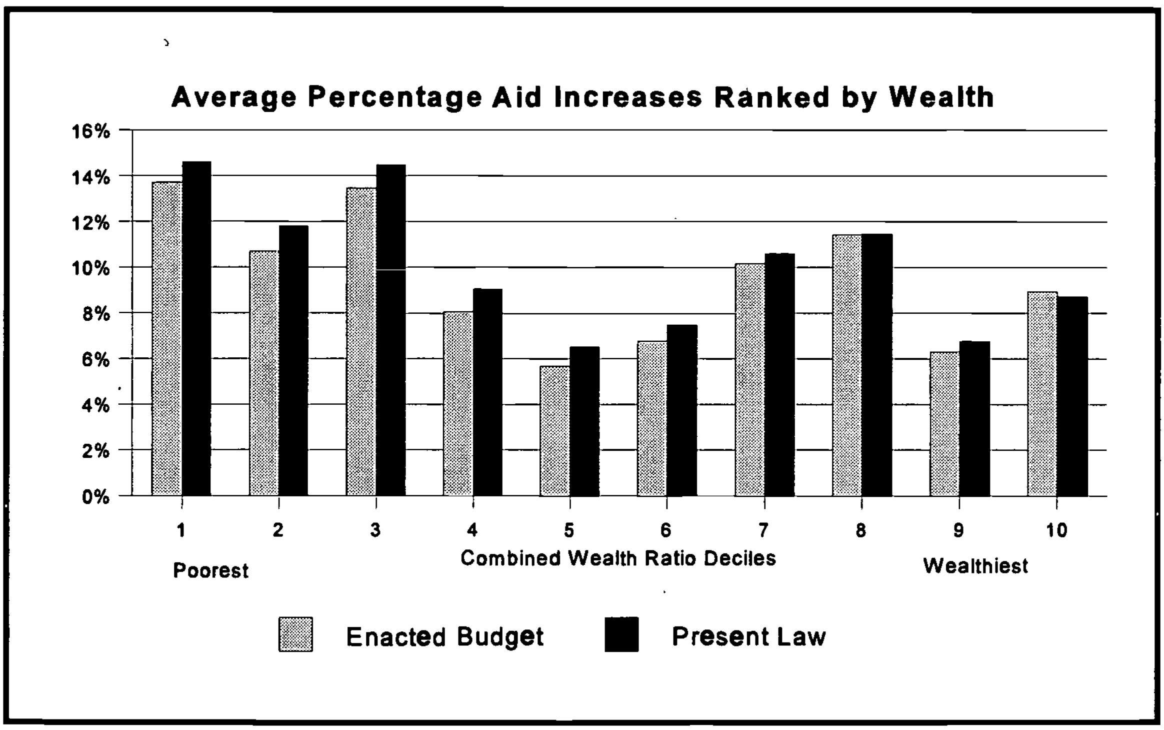
Note: This chart is based on only the computerized aid categories and so does not match the $913 million bottom line school aid increase; it is based on the SED computer run released with the budget (run no. SA990-0), which includes teacher support aid and various other grants and prior year adjustments not usually included among the computerized aid categories.

In accomplishing this distribution, most general school aid formulas were restored to present law levels (i.e., the funding implicit under existing formulas and plans), although there were modifications. For example, there were changes to increase "operating standards aid" and the aid provided through increased weightings for limited English proficient pupils. However, the transition cap was generally tightened in a fashion that reduced the aid increases allowed: a maximum increase of 2.8 percent over the previous year (was 5 percent last year) or a 7.8 percent share of the overall

formula increase calculated if that is higher (was 17.6 percent last year). The enacted budget therefore withholds $104 million more in formula aid from districts than present law would have. In essence, the transition cap was tightened in order to pay for other actions, such as the restoration of teacher support aid and increases for operating standards aid and limited English proficiency. Another change in the transition cap eliminates the guaranteed minimum increase provisions put in place last year (these provisions tended to limit the equalization provided in the formulas).

Since the enacted budget contained a statewide school aid increase this year identical to that produced by the operation of present law formulas, it is possible to compare the average percentage increases under both. The analysis shown in the chart below uses the combined wealth ratio (CWR), which ranks districts by property wealth and income, and a comparison basis similar to that used by the State Education Department (SED). As the chart shows, on average, the poorest groups of school districts would have received greater increases under present law than they did under the enacted budget, and only the wealthiest group received a higher aid increase under the enacted budget than they would have under present law. An examination of the results for individual districts also confirms the general trend shown by the averages.

Interestingly, these results seem to contradict those presented in the Education Department's post-budget analysis, which uses similar measures. The key to this discrepancy is that SED presents a single figure to describe the impact on high needs districts: their overall share of the aid increase. Since New York City is the largest high-need district in the State, this single percentage share approach obscures the impact of the changes on other high need districts. A review of the data summarized in the SED charts shows that only 33 of the 170 districts in their high need category



received a larger increase under the enacted budget than under present law. Eighty percent of the high need districts, in other words, would have done better if present law had been continued without change to the formulas.

Specific Aid Category Changes

Special education funding changes were enacted prospectively (i.e., no changes occur until the 2000-01 school year). Reforms in this area have been discussed for years, and action was finally taken largely because of threats from the federal government to withhold more than $300 million in federal aid if the State's approach could not be shown to encourage inclusion of special education pupils in regular classes.

The aid formula modifications which begin in the 2000-01 school year are intended to have the effect of moving more special education children into regular classroom settings. Specifically, per pupil weightings for children being served 60 percent of the day or more outside of a regular classroom will be marginally decreased over the next three years while students served in integrated settings will receive an increased weighting (which is paid for largely by reducing certain save-harmless provisions). Funding for support services (known by the acronym ERSSA) will also increase slightly, in proportion to general levels of district poverty. In addition to the aid changes, a series of regulatory changes are called for, including various requirements on school districts and SED, which will have to monitor more closely school district referral practices and develop alternative placement and preventative services models. It remains to be seen whether the changes enacted will address the prevalence of minorities in special education programs outside of regular classrooms, an issue raised in the federal correspondence.

The Governor's proposals to cut **BOCES** funding by 25 percent and to eliminate this aid stream in the following year were rejected. While maintaining BOCES as a vehicle for shared services, several changes were made in an effort to reduce costs: BOCES aid is no longer available for educationally related support services and to be eligible for aid, technology agreements with BOCES must be less expensive than what a district would otherwise pay.

Funding is restored for **RESCUE** — for REbuild SChools to Uphold Education, the extraordinary capital needs program enacted in 1998-99 but for which funding was subsequently vetoed. Funds of $145 million are provided for the construction and/or reconstruction of school facilities (primarily instructional space), to be paid through bonds sold by the Dormitory Authority. The $145 million figure represents the initial funding of RESCUE with future funding to be determined later. Last year the $500 million in funding that was vetoed had been planned to meet needs during a four-year period; this mismatch in time periods and the uncertainty over future funding makes a direct comparison between last year's enactment and this year's budget impossible.

RESCUE aid is apportioned to districts based on their share of pupils (with a minimum apportionment of $20,000). The RESCUE funding can be used to pay the local share of a building aid project as long as 2 to 5 percent (depending upon certain factors) is paid by the district.

A prospective change in the **building aid** formula will reduce aid in future years for districts benefitting from a save-harmless provision in the calculation of the aid ratio. For projects approved by voters on/before June 30, 2000, the formula remains the same, including the additional 10 percent incentive. For projects approved on or after July 1, 2000, districts must choose between their current aid ratio plus the additional 10 percent, or the selected aid ratio (i.e., with save-harmless) minus 10 percent.

Late Budget Impact

Despite a record state aid increase, the extreme lateness of this year's budget has dramatically and negatively affected school districts throughout the State by inhibiting their ability to plan and carry out educational programs. As reported by a major local school district organization:

> "The increased aid should in no way overshadow the limitations a late budget places on every school system ... A tardy budget leaves districts with the inability to plan effectively, to recruit competitively, to hire, and to implement training — one month before school opens!"[11]

All school districts outside the big five cites must submit budgets to their voters on the third Tuesday in May, and when the State budget is late, they must do so based on an educated guess about how much school aid they would be receiving. Although passing spending plans without good information on aid is always difficult for schools and their taxpayers, this year the situation was exacerbated because the LADDER education initiatives were excised in the Governor's Budget (although restored in the final enacted budget). These multiyear incentive programs call upon districts to create new programs or change current plans in order to receive funding, and leaving their future in doubt during the period schools were planning for the upcoming school year may have negated or diminished the intended effect. With funding in doubt, many school districts may have been unwilling to proceed with pre-kindergarten programs, additional maintenance projects, full-day kindergarten programs, and class size reduction plans.

Late budgets most significantly impact low-resource, high-needs districts for which State aid programs are more critical. As the school district budget voting day preceded State budget passage (an increasingly commonplace event), local taxpayers had to consider school budgets without good information on what the property tax levy would be. This year the situation was even worse than usual because the budget was delayed far into the summer and some districts filed tax warrants without knowledge of how much aid they would receive. The extreme lateness undoubtedly had the effect of raising taxes in many districts, although the only available evidence is anecdotal.[12]

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[11] Judith A. Chen, President of the Nassau-Suffolk School Boards Association, writing in their monthly publication *newsline* (Volume No. 24, August 1999)

[12] For example, a controversy arose in the Greece school district because it was acknowledged that the tax increase was larger than would have been required had their State aid increase been known before the tax warrant was issued. *School Board Strife Accents Tax Dilemma*, Rochester Democrat and Chronicle, August 26, 1999.

The late budget had other impacts. Magnet schools' summer programs were not funded and they had to delay planning of fall programs. Funding for teacher centers and bilingual education technical assistance centers had been eliminated in the Executive budget, requiring administrators to make contingency plans for new sources of support or to lay off employees, closing their doors for the year.

STAR

The STAR program continues in implementation as scheduled, with non-senior homeowners receiving the first installment of their tax relief this year. The senior exemptions are already fully effective and the non-senior exemptions are being phased in over three years. The cost of the exemptions statewide is expected to slightly exceed $1 billion this year and grow to about $2.3 billion upon full implementation.[13]

Although several administrative changes are made to the STAR program, the changes fall far short of the improvements proposed by the Executive (and supported by a review from the State Comptroller's Office). That review, *Administering STAR — The Need for Better Guidelines and Greater Uniformity in Procedures*, was released in early April 1999 and made additional recommendations. The Executive recommendations that were enacted include:

- Establishing a uniform time frame for age eligibility for the seniors enhanced exemption,
- Various changes providing clearer and more beneficial rules for applying the seniors exemptions when an eligible spouse dies, a senior moves into a nursing home, a residence is shared by siblings and other issues, and
- Increased State funding for administration of the program by local assessors, although the Executive's recommendation was reduced from $17 million to $12 million.

Of the Executive's recommendations not adopted, most significant was establishment of a system in which income verification for the seniors exemptions would be provided by the Department of Taxation and Finance. This proposal not only would have provided more effective verification, it also would have relieved seniors from having to reapply annually to verify their eligibility.

Several new legislative initiatives were enacted. Assessors must forward to cooperative apartment corporations and trailer/mobile home landowners exemption amounts for each applicable tenant. Also, seniors who fail to renew annually will automatically get the lower valued basic STAR exemption.

[13]These amounts reflect only the cost of the property tax exemptions; including the cost of a related State-funded income tax credit in New York City, the program grows to $2.7 billion.

The Comptroller's study included an administrative review and field visits to assessing units and revealed insufficient State guidance and confusion among assessors, resulting in varying rules being applied throughout the State. A number of changes were recommended in that report that can be implemented administratively by the Office of Real Property Services, such as providing comprehensive instructions to assessors to administer the program and clearer instructions for residency verification. However, other recommendations require legislative action, including:

- Amending to the statutory audit provisions to ensure that school districts are not held responsible for exemptions improperly awarded by assessors,

- Providing reimbursement to school districts for interest losses and borrowing costs due to the delayed receipt of STAR revenues, and

- Increasing the amount of unreserved fund balances that can be held by school districts from two to five percent of their budgets.

Last year's payment schedule for STAR will stay in effect for the 1999-00 school year (35 percent in October, 35 percent in November, 10 percent in December and 20 percent in January). The permanent payment schedule recommended by the STAR Cash Flow Study Commission is to take affect in the 2000-01 school year (under which payments that will be disbursed relative to the proportion STAR represents in each district's property tax levy).

Property Tax Report Cards

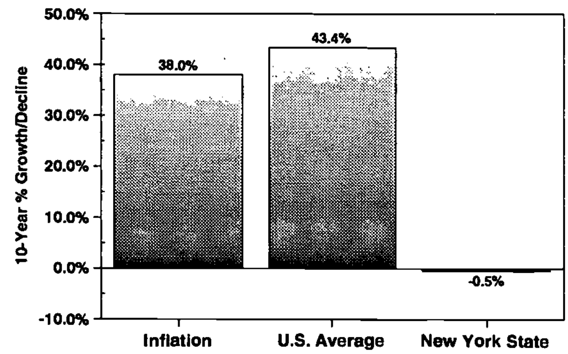
Schools will now be required to send data to SED for the compilation of a "property tax report card" containing information on how their proposed budget will affect property taxes and how the proposed budget and tax rate will compare to the inflation rate for the prior calendar year. SED is then required to tally all districts' tax information and make it available on the Internet, 10 days before the statewide budget vote day, so that taxpayers can compare their district's budget and tax increases with other districts. Both the property tax report card and a newly required notice to voters must compare, using percentages, the proposed budget increase over the prior year with the consumer price index of the prior calendar year. It is interesting to note that at the state level, this year's enacted budget increase compares favorably with inflation only after a series of accounting gimmicks and "move-outs" were used to reduce the General Fund increase.

The statute requires data to be sent to SED at least 24 days before the statewide school district budget vote day. Under this time frame, and given the State's recent budget history, it is highly unlikely that districts will have state aid data, and thus the tax levy information published in the report cards will be substantially inaccurate. As an example, next year the budget vote day is May 16 and thus districts will have to submit data to SED by April 22; in only three of the last 10 years has the State budget been passed by that date. Report card data furnished in advance of budget passage should contain a prominent and substantial disclaimer to the effect that the property tax rate information is only speculative.

Higher Education

The new cuts proposed in the Executive Budget were rejected, and there were some restorations in areas suffering from cuts made in earlier years, as well as some new items. In total, $150 million in additional funding for the 1999-00 State fiscal year was provided, equating to $172 million on a full annual basis. The preponderance of this addition funded restoration of a proposed TAP cut. Most of the other additions were somewhat smaller than last year's restorations (which were vetoed), and they are certainly not large enough to make up for the erosion in higher education funding that has taken place over the past decade.

Long-term Trends in Support for Higher Education
1988-89 to 1998-99



Over the last ten years, New York is the only state in the nation that cut appropriations supporting higher education. New York State's support has been reduced by 0.5% while the national average has increased by 43% and CPI inflation has been at 38%. (Source: Illinois State University *Grapevine*)

The higher education additions at the public universities, moreover, are overshadowed by two major funding issues that were not explicitly addressed in the enacted budget. Both SUNY and CUNY lack funding for increased personal service expenditures (required under collective bargaining agreements) and other inflation and growth in mandatory costs. In addition, a $77 million shortfall at the SUNY Hospitals will have to be covered, potentially through a cut for academic programs at the campuses. A mid-year increase in tuition at SUNY has also been discussed.[14]

Both of these situations were well known during the budget negotiation period and yet were ignored in the final product. The additions to the public university budgets, such as those for full-time faculty, day care and opportunity programs are useful, but they are very small in comparison to the amounts that will have to be found to meet inflationary costs and (in SUNY's case) to fund the hospital shortfall.

The additions to the Executive Budget were as follows:

- TAP — the Executive's proposed cut was rejected and the program is maintained at current grant levels, thus restoring $113 million for the 1999-00 academic year. An increase in the maximum grant level sought by the independent institutions was not provided, however, and the $4,125 maximum grant today covers only about 25 percent of the average tuition at these colleges whereas it covered 40 percent in 1990 and 60 percent in 1974.

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[14] *Tight Budget Concerns SUNY*, Albany Times Union, September 2, 1999.

- Opportunity programs received additional funding totaling $8.3 million on an annual basis (including EOP at SUNY, SEEK/CD at CUNY and HEOP at independent institutions). However, these programs have generally been straight-lined or cut since the late 1980's and a 25 percent across the board cut was imposed in 1995-96. Last year's legislative budget would have essentially restored the 1995-96 25 percent cut (although not the losses to inflation before and after that action), but the additional funding was vetoed. This year's addition is about two-thirds the amount enacted and vetoed last year.

- Community College Aid — A $75-per-student increase in aid provides $14 million more on an annual basis for SUNY and CUNY community colleges. While helpful, this increase is only half of the $150-per-student increase that had been requested by the public university systems — an increase that would have restored the State's share to about one-third, as was originally provided (but still short of the 40 percent share promised and achieved for one year in the 1970's).[15]

- Faculty lines — $6 million is provided to establish more permanent faculty lines at the public university systems and community colleges. This addition is roughly one-third the amount contained in last year's budget for this purpose (but vetoed). While positive, this amount will not by itself make up for the decade of freezes and cuts that have left many campuses with larger numbers of part-time adjuncts than full-time faculty.

- Bundy Aid, which goes to independent colleges and universities based on the number of degrees granted, was increased by $4.2 million to $48.5 million. This increase is helpful, although it is slightly less than last year's enacted and then vetoed increase of $5 million. However, funding today is far below the "statutory level" (i.e., the dollars per degree calculation specified in law). Bundy aid has not been fully funded since 1990-91, at which time it provided $107 million. Even before the impact of inflation, in other words, the program has been more than halved during this decade.

- Funding was restored for the State Education Department's higher education staff and the proposed elimination of their responsibilities was not accepted.

- Other restorations include the FIT charge-back, collaborative programs at CUNY, and Cornell Cooperative extension. Additional funds are also provided for child care for students at the public university systems, for the STEP/CSTEP technology education programs, and various other programs.

- The Jobs 2000 or "J2K" economic development programs are closely related to higher education. The programs include funding for faculty development, Centers for Advanced

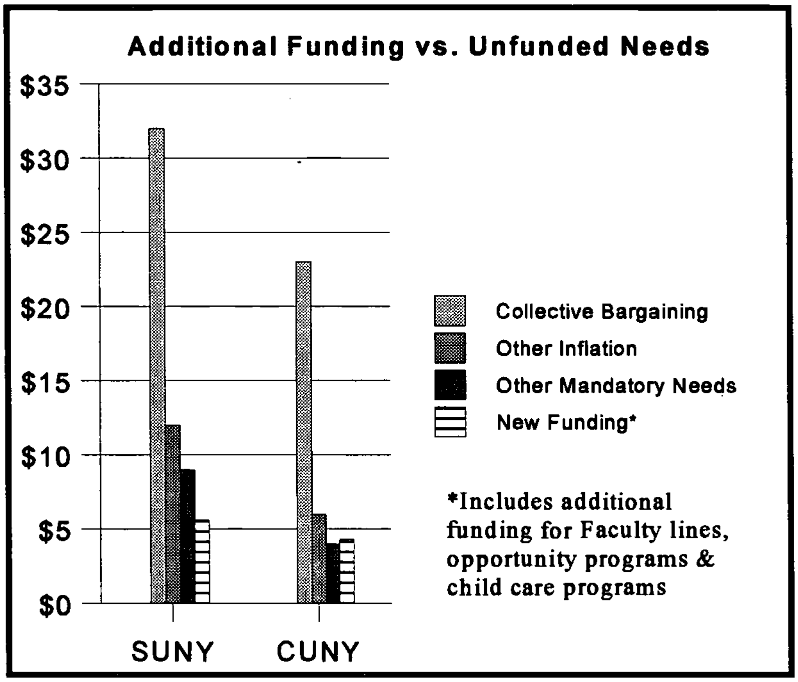
[15]For a full discussion of these issues, see *New York State's Community Colleges: Cost-Effective Engines of Educational Access and Economic Development*, March 1999, Office of the State Comptroller.

Technology (CATS), a capital facilities program, and a technology transfer incentive program, all of which will be coordinated through a new Office of Science, Technology and Academic Research (announced as NYSTAR although bearing no relationship to the school tax relief program with a similar acronym).

Unfunded Salary Increases and Other Costs at SUNY & CUNY

The senior colleges at CUNY and the SUNY state-operated institutions were "straight-lined" in the Executive budget, meaning that no funding was provided for growing costs either for personnel or other inflation and expenses. The largest component of this omission is the substantial and known costs for collective bargaining increases already in place for faculty and staff ($32 million at SUNY and $23 million at CUNY). Other inflationary increases were also unfunded, such as those for rents, library and instructional materials, equipment and specific charges such as building rents. Lastly, both university systems identified certain mandatory needs in their budgets, such as additional operating costs for the new graduate center at CUNY ($4 million) and reduced revenues from interest earnings and other changes in the SUNY income offset account ($9 million).

The legislative additions did not address these costs, although the collective bargaining increases were discussed at the conference committee and the legislative chairs agreed that Executive should fund these increases through a statewide lump-sum reserve appropriation for collective bargaining increases. That appropriation, however, was intended to support agreements to be negotiated during the year, not the signed agreements at SUNY and CUNY. The Executive Budget explicitly intended that these costs and other inflationary increases be funded through reductions elsewhere in the systems; the enacted budget did not alter that situation.



The only adds going directly to CUNY senior colleges and SUNY state-operated institutions are for full-time faculty lines, opportunity program restorations and additional child care for students.

At SUNY these adds total just $5.6 million, whereas unfunded mandatory needs total $58.3 million. At CUNY, a $4.3 million addition contrasts with $33 million in unfunded mandatory needs.[16]

SUNY Hospitals Revenue Shortfall

A $77 million shortfall at the SUNY Hospitals has resulted in an impoundment of appropriations by the Governor's Budget Director. This action requires the SUNY Board of Trustees to choose between spending reductions at the campuses (reallocating student tuition revenues) or the hospitals (with patient service implications and causing further revenue problems). A tuition increase has also been discussed. Without additional State funding, the hospital shortfall can only be met by taking funds from other purposes or by using temporary solutions such as borrowing.

This situation was known during the budget negotiations but was not specifically addressed. The belated actions now being taken administratively could have a serious detrimental impact on SUNY academic programs or on patient care and hospital revenues.

The shortfall resulted from the hospitals' inability to meet their revenue targets, which are developed by the Division of the Budget and built into the appropriation schedules. As of the end of the University's fiscal year in June, a $77 million temporary loan was necessary to avoid a deficit. Although the temporary loan was repaid in September with tuition revenues, the shortfall it revealed still exists, and an even larger revenue shortfall is expected in the current year.

The Governor's Director of the Budget has both the power and responsibility to impound portions of appropriations in order to address revenue shortfalls. On August 24, only 20 days after budget enactment, the Budget Director impounded $77 million from SUNY's appropriations (an amount identical to the year-ending loan). The impoundment was taken against SUNY Special Revenue Fund (345), which includes revenues from tuition and student fees as well as hospital income.[17] In the case of the SUNY appropriation schedule, the Budget Director can withhold funds

[16]The figures for mandatory needs given here differ somewhat from those used by the universities in their budget presentations. At CUNY various member items (that were continued) account for the difference. The SUNY figures for additional enrollments and sponsored research were not included because they could arguably be considered program increases rather than growth in mandatory costs.

[17]Several certificates have been issued by the Budget Director since the master certificate impounded $77 million on August 24. An August 27 certificate revised the master certificate to allocate only 23.5 percent of appropriated funds to cover the first quarter (an approach used by the Budget Division for State agencies generally but which has never before been applied to SUNY and is not being applied to CUNY). A September 1 certificate increased the allocations to 100 percent for all funds except those supporting SUNY's core academic budget and hospital operations; the State's general fund support appropriation remained at a 23.5 percent allocation and slightly more than half of Special Revenue Fund 345 was allocated. The unusual imposition of this type of quarterly, reduced allocation procedure by the Executive may represent an attempt to temporarily mask the approach being contemplated to fill the hospital deficit. There is no other understandable explanation for its imposition on an independently governed university system for which the Executive has previously proposed greater flexibility, particularly at a time when State cash flow needs cannot be said to be pressing. These actions have already caused significant administrative problems at the campuses and the state level.

without indicating whether the reductions are to come from the campuses or the hospitals. The SUNY trustees are then responsible for making that choice in their financial plan.

The State University Trustees have not indicated if the $77 million reduction will come from SUNY campuses or the hospitals. Comptroller McCall wrote to the University's Board of Trustees expressing concern both about the long-term structural problem at the hospitals and threat of the potential cuts to academic programs or a tuition increase.

In a response letter, SUNY's Executive Vice Chancellor said that SUNY "would do everything possible" to avoid a reduction in the core budget and that "at this point, we have no intention of reducing spending on academic programs or diverting student revenues." The letter did not address the issue of whether a tuition increase was being considered.

Action by the Trustees on a financial plan had originally been expected at their September 22 meeting; it has now been deferred until their meeting of October 26. The substantial delay in adopting a financial plan for university operations (two months into the academic year) will undoubtedly cause administrative problems at the campuses.

The Budget Director's impoundment action allows the Trustees to override the Education Law's interchange limits between hospitals and campuses.[18] If the Trustees fail to allocate such a reduction within 30 days, the Budget Director is empowered to do so directly. The override authority would allow the Trustees to reduce campus appropriations approved by the Legislature. A reduction spending authority for academic programs would make tuition and other student revenues available for financing the hospital deficit. Such an action, although it fills in last year's deficit, diverts funds intended to support academic programs.

Without additional State funding or an unexpected surge in revenues, the hospital shortfall can only be met by taking funds from other purposes or by using temporary solutions such as borrowing or other one-time actions. This is also true for the other unfunded costs in the University's budget. It is unlikely that the hospitals will be able to produce enough revenues to recover last year's shortfall, much less generate enough to cover this year's potential imbalance .

A reduction of $77 million — if the entire impoundment were applied to campuses — would represent a cut of nearly 5 percent in the core operating budget. Cuts and freezes over the past ten years have already reduced the portion of SUNY's core budget funded by the State from over 75 percent to roughly 50 percent at present. Another option to cover the shortfall would be to raise tuition or other student fees. This would provide additional revenues that could be used to pay back last year's loan as well as cover any current year shortfall. This approach is fiscally viable, but programmatically objectionable because it would be unfair to students and damaging to access.

[18] These limits are set in Section 355 of the Education Law but modified by certain language included in the budget legislation. The modifying language has been included in budget bills since 1990 and provides greater interchange flexibility than provided in the Education Law. Although this modifying language was a subject of discussion at the budget conference committee, in the end it was retained.

Comptroller McCall has expressed his strong opposition to a tuition increase that would force students to pay for the shortfall at the hospitals.

Part-Time TAP Pilot

A pilot program at CUNY to test a new approach to financial aid for part-time students has been approved for three academic years to begin in the fall of 2000. It has long been theorized that many students for whom part-time study would be advantageous because of their family or employment situations are driven to register for full-time study by TAP eligibility rules. Although the State has a part-time aid program, APTS (Aid for Part-Time Study), it is funded at a low level and the grants are not entitlements, but are distributed on using different (and often inconsistent) methods among campuses. The negative consequences of students being pushed into full-time status include poorer academic performance, retention and persistence problems (e.g., "stopping out") and low graduation rates.

The pilot Part-Time TAP (or P/TAP) program would provide grants equal to a pro-rated share of the regular full-time TAP grant entitlement for students taking at least six but less than twelve credit hours per semester. Only students who had completed 24 credit hours or more at CUNY and obtaining a "C" or better average would be eligible. CUNY estimates that approximately 7,500 of their students will participate, roughly half of whom are now registering for full-time course loads. The pilot is expected to be cost neutral, because there will be offsetting decreases in both TAP and APTS, and an evaluation study is required at the end of the pilot period. Federal Pell grants have been available for part time studies for many years, and this pilot will allow for effective testing of the impact of the State moving toward a fiscally neutral approach to tuition assistance for part-time studies.

Medicaid

The Executive Budget proposed actions that would have reduced General Fund spending by $511 million in 1999-00. Of this amount, $266 million represented new State Medicaid cuts that directly reduced payments to health care providers. The remaining $245 million reduced State Medicaid costs by maximizing federal payments. Providers would have lost an estimated $848 million in Medicaid revenues (federal, state, and local shares). These reductions would have been offset by an estimated net benefit of $82 million by the Executive proposal to accelerate the scheduled elimination of health care provider assessments by one year. Lastly, the Executive proposed continuation of $85 million State Medicaid cost containment measures that have been in place since 1996-97 and were scheduled to sunset on March 31, 1999.

The enacted budget included no new Medicaid cuts. Old cost containment measures, with one exception, expired for one quarter but were later reinstated as of July 1, 1999. A large portion of the proposed State Medicaid actions that maximize federal payments was adopted. The expiration of provider assessments was accelerated three months rather than the proposed one year. State Medicaid costs were offset by balances in certain health care pools. As a result of these actions, State Medicaid costs are reduced by an estimated $206 million and providers are expected to receive a benefit of $268 million in contrast to the proposed cuts of $848 million. In addition, since the introduction of the Executive Budget, Medicaid spending projections for 1999-00 were lowered $103 million. This re-estimate has no provider impact. A more detailed description of each of the major components follow:

- *Revenue maximization actions of $177 million.* Federal funding is maximized through intergovernmental transfers (IGTs) which involve increasing Medicaid payments to county owned nursing homes, drawing down the additional federal match and then sharing the increased federal reimbursement between the State and county governments. Nursing home IGTs are increased $113 million. This is a lower level than proposed by the Governor. Some of the maximizing measures proposed by the Executive were contingent on a lower level of State Medicaid spending and could not be achieved, due to federal restrictions, when significant restorations were made. Other maximizing actions include: $30 million from notwithstanding the cap on provider assessment collections, and $35 million from increasing the local share of Medicaid costs for managed care expenditures.

- *Lapse in old cost containment increased State costs $85 million.* Medicaid cost containment adopted in previous years sunset on March 31, 1999. The enacted budget extended these provisions retroactively to July 1, 1999, losing one quarter of savings for State and local governments, and they now expire on March 31, 2000. [19] In addition, since counties pay a

[19] The one cost containment measure that was allowed to sunset was the home health care fiscal assessment.

share of total Medicaid costs, their budgets will see unanticipated increased costs of $51 million. The lapsed cost containment increased provider Medicaid revenues by an estimated $271 million.

- *Provider gross receipts assessments* were scheduled to be phased out by April 1, 2000. The enacted budget accelerates this phase-out by three months instead of the proposed one year acceleration. The one-quarter speed up reduces provider assessments by $55 million. After accounting for the Medicaid reimbursements associated with some of these assessments, the net benefit to providers is an estimated $41 million.

- *Offsets of $145 million*. State General Fund Medicaid spending will be offset by transfers of $100 million from existing balances in certain NYPHRM pools and $45 million from unexpended Health Care Reform Act (HCRA) pools.

Another $118 million from unexpended HCRA pools, primarily hospital workforce retraining, is reallocated as follows: $60 million for hospitals bad debt and charity care, $18 million for hospitals disproportionately impacted by continuation of old Medicaid cuts, $12 million for clinics' bad debt and charity care, $16 million for priority health programs (as determined by the Governor, Assembly, and Senate), $10 million for rural health, and $2 million for cancer mapping.

Impact of 1999-00 Medicaid Actions
Change from 1998-99
(in millions)

Provider Type	Description	State Medicaid Costs	Provider Medicaid Revenues
Hospitals	Lapsed cost containment	$40	$162
	Transfer from HCRA pools to GF	($45)	($45)
	Acceleration of provider assessment phase-out	N/A[20]	$10
Nursing Homes	Lapsed cost containment	$32	$78
	Additional Intergovernmental Transfers (IGT)	($113)	$0
	Notwithstand cap on provider assessments	($30)	$0 [21]
	Acceleration of provider assessment phase-out	$32	$32
Home Care	Lapsed cost containment	$13	$31
Managed Care	Local share shift and imposition of co-pay	($35)	$0
	Transfer from old NYPHRM pools	($100)	N/A
Combined		($206)	$268

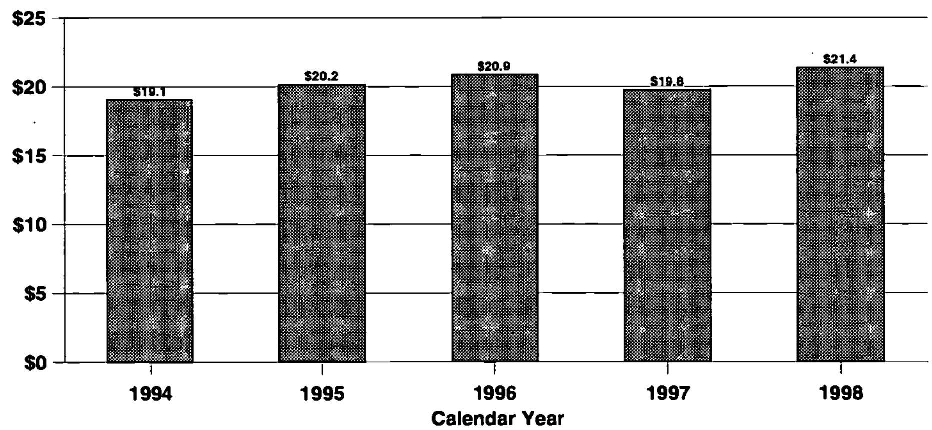
The 1999-00 State General Fund Medicaid spending projection was lowered by $103 million. This represents the recurring effect of lower than expected 1998-99 spending and revised projections for the current year. Medicaid costs have stabilized in recent years, after double digit growth in the early nineties.

[20] There is no impact on the Medicaid budget; however, General Fund miscellaneous receipts will be reduced by $9.5 million.

[21] Although it could be argued that notwithstanding the cap on provider assessments deprives health care providers of planned rebates, the cap on assessment collections has been consistently ignored since it was first created and it does not represent any year to year change in policy.

New York's Total Medicaid Costs

($ in billions)



State General Fund 1999-00 Medicaid costs are projected to decline $28 million, or 0.5 percent compared to 1998-99. Underlying growth in program spending is the normal growth that would occur absent statutory changes. In order to derive underlying program growth, certain adjustments need to be made; they include:

- ✓ impact of lapsed cost containment;
- ✓ value of additional revenue maximizing actions;
- ✓ value of non-recurring spending offsets; and
- ✓ impact of changes in the Medicaid-reimbursable provider assessments.

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Department of Health General Fund Medicaid Spending: Enacted Budget
(dollar amounts in millions)

	Amount	Funding Growth	Program Growth
1997-98 Actual	$5,374	1.5%	4.1%
1998-99 Actual	$5,563	2.0%	4.6%
1999-00 Proposed	$5,535	-0.5%	4.7%

Estimated program growth in State Medicaid spending is approximately 4.7 percent in 1999-00. The rate of program growth is consistent with the experience of the last two years and is below national projections. At the national level, the Congressional Budget Office projects federal Medicaid spending will grow 5.9 percent in federal fiscal year 1999 and 7.5 percent in 2000.[22] While the national estimated growth rates provide some insight into the overall trends, caution must be used when extrapolating to the State since the State's share of total Medicaid costs differ from the federal and local shares and depends on the type of medical service. In addition, the State's population is steady while the rest of the nation is increasing.

Child Health Insurance Plus

Child Health Insurance Plus (CHIP) was created in 1991 to help make health insurance more affordable for children. Many children were ineligible for Medicaid because their families' earnings were over the eligibility threshold, yet these same families earned too little to afford to pay for insurance. CHIP pays for, or subsidizes, health insurance for these children.

The federal Balanced Budget Act of 1997 included a new block grant program for states to provide expanded health insurance coverage for children. New York receives approximately $256 million annually in federal funds. This new funding, combined with existing State funding enabled the State, after some debate, to dramatically expand and improve the current program. [23] Legislation passed last year expanded the number of children eligible for the program, expanded the covered services to include vision, dental and certain mental health visits, and reduced the premium payments made by families.

CHIP spending is projected to total $432 million in 1999-00, representing an increase of almost 85 percent from last year. This substantial increase is attributable to the full year impact of

[22] The Economic and Budget Outlook: An Update. Congressional Budget Office. July 1999.

[23] Initially, the Governor proposed only a modest reduction in the required family CHIP premium contribution and an expansion in the services covered by CHIP (vision, dental and mental health). According to a report by the Office of the State Comptroller entitled Child Health Insurance: Current Issues and Policy Options (June 3, 1998) the Governor's plan left an estimated $650 million in available funding unspent over the next six years.

last year's enrollment increases and further enrollment increases forecast for this year. The State embarked on an aggressive marketing and outreach campaign to alert eligible families and children of CHIP. The results are remarkable -- enrollment has increased from 153,000 in November 1997 to 332,348 in May 1999. The enrollment goal for State fiscal year 1999-00 increases by nearly 100,000 to 300,000, after accounting for the gradual transition of approximately 80,000 Medicaid-eligible children to the appropriate program.[24] Ultimately, the Executive's enrollment target for CHIP is approximately 400,000 children.

Child Health Insurance Program Summary
(in millions)

Program	1998-99	1999-00	Change	Growth
Federal Funds	$151	$278	$127	84.1%
State Funds	$83	$154	$71	85.5%
Total Spending	$234	$432	$198	84.6%

The State portion of CHIP funding comes from the Health Care Initiatives Pool created by the Health Care Reform Act of 1996. This was the legislation that deregulated hospital rates paid by non-Medicaid or non-Medicare payors. This legislation, and the associated surcharges and pools, expires on December 31, 1999.

Tobacco Settlement

New York is estimated to receive approximately $25 billion over the next 25 years as a result of a comprehensive settlement among 46 states and U.S. territories and all the major tobacco companies.

New York's Consent Decree was approved by State Supreme Court on December 23, 1998. The agreement provides for the distribution of the settlement funds with the State's localities since they too paid a share of the increased health costs associated with smoking, particularly in the Medicaid program. New York State would receive approximately 51 percent of the total settlement, New York City would receive 26.7 percent and the balance of 22.3 percent would accrue to other counties.

New York City, Erie and Westchester counties, all of whom had pending related litigation prior to the national settlement, filed an appeal on January 22, 1999 claiming the distribution formula was not equitable. On July 15, the Appellate Division unanimously ruled in favor of the State. The localities did not appeal. The New York settlement is now considered final.

[24] A recent audit by the Office of the State Comptroller found an estimated 41 percent of CHIP enrollees, 63,000 for the period covered by the audit, appeared eligible for Medicaid. Office of the State Comptroller, Management of Child Health Plus Program, Report 97-S-10, April 1998.

The settlement monies will not flow until 80 percent of the settling states achieve "state-specific finality" and the settling states represent 80 percent of the aggregate award, or June 30, 2000, whichever is first. State specific finality is achieved when the consent order is approved by the courts and all appeals have been exhausted. To date, 43 other settling states and territories have obtained state specific finality. While these 43 states represent 80 percent of the number of settling states they do not total 80 percent of the funding. To date, settling states with state specific finality represented 66.94 percent of the funding.

The Executive Budget did not anticipate receiving tobacco monies until SFY 2000-01 but proposed creating a new tobacco fund that would receive all monies and dedicating 75 percent of the State's share of the settlement to reduce debt and the remaining 25 percent to pay for unspecified health initiatives. The final budget created a fund to receive the settlement, but decisions on its use were deferred.

New York will be receiving these tobacco settlement funds because the State and its localities have spent billions of dollars on treating the negative health consequences associated with smoking. Although there are no restrictions on the tobacco funds, future smoking related costs could be reduced if the State wisely spent a substantial share of the newly available resources on health related initiatives including youth smoking prevention. Using a portion of the tobacco settlement to reduce debt may be controversial. Although the State's debt burden is clearly excessive, there are also a host of pressing health care needs. The use of the State's tobacco settlement will likely be an issue in the upcoming Health Care Reform Act (HCRA) renewal debate later this year.

Public Assistance

In 1997, major programmatic and financing changes were made to New York's public assistance programs in response to the federal Personal Responsibility and Work Opportunity Reconciliation Act. Aid to Families with Dependent Children was replaced with Family Assistance which consists of a time-limited cash grant. Home Relief was replaced with a new safety net program for adults, which in many instances will provide non-cash benefits. Both programs have a number of federal and State-imposed work requirements. If the federal work requirements, which gradually increase over the next five years, are not met, the State could face substantial fiscal penalties.

Federal funding is provided to New York through an annual block grant of $2.4 billion. The amount of this grant is based on the 1995 public assistance caseload. Since that time, caseloads have declined significantly and New York now receives a greater share of total program costs from the federal government. The additional amount of federal funding compared to the old program is often called the "welfare windfall."

Each year the base level of the welfare windfall has grown because caseloads continue to decline. In 1997-98, the first year the State received a windfall, the base level associated with that fiscal year was $624 million. This amount has grown to an estimated base level of $937 million for 1999-00. The 1998-99 windfall was underestimated and unspent funds were available for allocation

in 1999-00. When the underestimation of the 1998-99 windfall is included, the funding available for allocation totals $1.43 billion in 1999-00.

Allocation of Available Federal Welfare Windfall Monies
(in millions)

Program	1999-00
Set-Aside for Future Needs	$330
State Fiscal Relief	$166
Local Fiscal Relief	$192
Support for Welfare to Work (training, education, drug screening, etc)	$192
Reserve for Future Child Care Needs	$200
Transfer to Child Care Block Grant	$230
Transition and Incentive funding for local districts	$84
Welfare Systems Redesign	$30
Child Preventive Services	$10
Total	$1,434

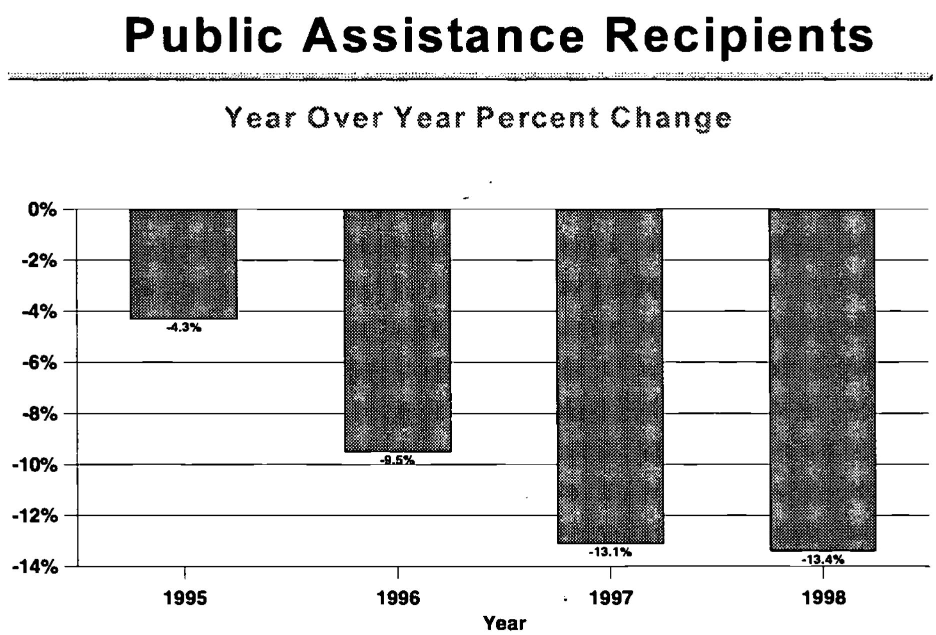
In addition to New York, many other states also have unexpended federal welfare funding balances. There has been discussion at the federal level of taking these balances and using them to offset other desired spending increases. Given this discussion, there is risk that the federal government may take away the balances states have wisely set aside for future needs.

The enacted budget uses $358 million of the welfare windfall to provide general State and local fiscal relief, primarily through a Title XX transfer. An additional $330 million is set aside for future public assistance needs, bringing the total set-aside to $548 million. Funding for employment related programs is $192 million.

In order for the State to draw down the full amount of the federal block grant, spending must meet the required maintenance of effort level (MOE). The estimated MOE is $1.718 billion and the State is currently spending just about that amount. However, as caseload declines persist, it may become more difficult for the State to continue to meet the MOE requirements.

In 1999-00, the State will begin to claim a portion of the Earned Income Tax Credit paid to lower-income working families against the MOE. This assists the State in meeting the MOE requirements, and the spending that would have otherwise been counted under the MOE will be replaced with spending from federal funds. This will provide additional State fiscal relief of $46 million in 1999-00 and expected relief of $150 million thereafter. When the expansion of the EITC is fully implemented, it is expected that the cost of the expansion of the credit will be fully funded through this refinancing.

For calendar year 1998, the monthly average number of public assistance recipients declined 13.4 percent following declines of 9.5 in 1996 and 13.1 in 1997. For 1999-00, the Executive projects the number of public assistance recipients will decline by another 7 percent. The safety net caseload of adults is expected to decline at a faster rate than the family assistance caseload.



Due to the projected decline in caseloads, General Fund spending on the family assistance and safety net programs is expected to decrease 6.7 percent to $742 million. The Supplemental Security Income (SSI) estimated to remain stable and spending to grow by 0.9 percent. This is the net effect of one-time savings of $45 million, introduced in the Governor's 30 day amendments, from only making 11 payments instead of 12, offset partially by scheduled inflationary increases.

Assistance Programs: General Fund
(in millions)

Program	1998-99	1999-00	Change	Growth
Family Assistance	$473	$460	($13)	-2.7%
Safety Net	$322	$282	($40)	-12.4%
State Share of SSI	$587	$592	$5	0.9%
Total	$1,382	$1,334	($48)	-3.5%

General Fund support for the Food Assistance program is reduced to reflect the federal restoration of food stamps to certain non-citizen children, disabled adults and elderly.

The enacted budget contains no new appropriations for evaluation of the new public assistance programs; however, nearly $700,000 in federal and State Funds is reappropriated for this purpose. In June, the Comptroller released a report critical of the State for failing to issue its first evaluation report.[25] In late July, the State has released its first report on the evaluation of welfare reform in New York State.[26] Elements of a successful welfare evaluation program were described in detail in a report from the Comptroller's office in 1997.[27]

Child Care

Total funding for the Child Care Block Grant increases $162 million to $622 million. The block grant was created in 1997-98 and combines the public assistance, transitional, at-risk, and State low income day care into one seamless funding stream. The increase in the block grant is almost entirely due to the transfer of $230 million in federal welfare block grant funds. The increased funding is expected to support at least 13,000 new subsidies, bringing total subsidies to at least 138,000. This estimate incorporates projected increases to rates prompted by the market survey that is required by the Federal government.

In addition, $200 million from the federal welfare block grant is set-aside to create a three year reserve fund to support child care. Of this amount, $175 million would be allocated to local districts and the remaining $25 million would be available, through a competitive process, for other child care capacity building expenditures. The amount allocated to the localities would be based in part on historical child care costs, the availability of child care, and cost of child care. Localities

[25] Office of the State Comptroller, *An Update on the Evaluation of Welfare Reform in New York State.*

[26] The Nelson A. Rockefeller Institute of Government, *After Welfare: A Study of Work and Benefit Use After Case Closings.*

[27] Office of the State Comptroller, *Evaluating Welfare Reform: A Proposal for New York.*

would only be eligible for these additional funds if they had spent all the other sources of child care funding.

The creation of the child care reserve is a step in the right direction. Although there are wide variations in the number of subsidies and slots for child care, the creation of the reserve recognizes the likelihood that further expansions will be needed. A recent audit by the State Comptroller's Office found that better advance planning was required by the agency to ensure adequate child care was available to meet the new federal work requirements under public assistance[28]

[28] Office of the State Comptroller, "Child Day Care Planning under Welfare Reform" (Report 97-S-50), October 19, 1998.

Tax Cuts

The enacted budget includes a package of new tax cuts valued at $58 million in 1999-00 and $375 million when fully implemented in 2003-04. The Executive Budget recommended $218 million in new tax cuts for 1999-00, -$15 million in 2000-01,[29] and $1.031 billion when fully implemented in 2003-04. The fully implemented cost of additional tax cuts was significantly reduced in the final plan. The cost of new tax cuts in the enacted budget is approximately $160 million less than what was proposed in the Executive Budget in 1999-00; $50 million more in 2000-01 and $42 million more in 2001-02; $656 million lower in 2003-04 when fully implemented.

1999-00 Enacted Budget
Changes from Proposed Executive Budget
(in millions)

SFY	1999-00	2000-01	2001-02	2002-03	2003-04
Executive Budget New Tax Cuts	$218	($15)	$198	$650	$1,031
Enacted Budget New Tax Cuts	$58	$35	$240	$327	$375
Difference	($160)	$50	$42	($323)	($656)

The centerpieces of the Governor's proposed tax cut plan were: personal income tax reductions for middle-income families; restructured, lower utility taxes; and rate reductions for banks and insurance companies. The final package includes $150 million in rate reductions for banks and insurance companies so that their tax rates conform to the rates for general corporations. It does not include significant changes for utility companies or middle-income personal income tax cuts. The enacted plan provides an enhancement to the Earned Income Tax Credit (EITC), estimated to reduce taxes by $125 million when fully implemented, designed to provide tax relief to lower-income working families. With the exception of the EITC, nearly all of the new tax cuts accrue to businesses.

The remaining $100 million is used for 25 different, small targeted tax reductions that have questionable job creation potential.

The enacted tax package also includes a three month delay in implementation of the sales tax exemption for clothing slated to become permanent on December 1, 1999. Instead, there will be two temporary one-week exemptions. The net result is $100 million in forgone tax savings for shoppers in 1999-00. The combined impact of new tax cuts and delayed tax cut actions included in this year's budget results in a *net loss* of $42 million in taxpayer savings.

[29] On an aggregate basis, the tax changes in 2000-01 raise revenues. This is due to timing an other effects of the proposed transition from a gross receipts based tax (Article 9) to a net income based tax (Article 9-A).

Tax Cut Actions Included in the 1999-00 Budget
(in millions)

Description	99-00	00-01	01-02	02-03	03-04
Bank and Insurance tax rate cut	$0.0	$2.0	$70.0	$110.0	$150.0
Earned Income Tax Credit enhancement	$0.0	$14.0	$70.0	$117.0	$125.0
Acceleration of provider assessment tax cut	$55.0	$0.0	$0.0	$0.0	$0.0
Subsidiary capital exclusions - utilities	$0.0	$5.0	$17.0	$17.0	$17.0
Alternative Minimum Tax rate reduction	$0.0	$0.0	$12.0	$12.0	$12.0
Pari-mutuel tax cut	$2.0	$4.0	$8.0	$8.0	$8.0
QETC credit enhancement	$0.0	$0.0	$8.0	$8.0	$8.0
Estate tax federal conformity	$1.0	$1.0	$8.0	$8.0	$8.0
Petroleum Business tax cut	$0.0	$0.0	$5.0	$5.0	$5.0
EDZ/ZEA wage credit enhancement	$0.0	$0.0	$5.0	$5.0	$5.0
Gas importation tax cut	$0.0	$1.0	$5.0	$5.0	$5.0
Subsidiary capital exclusions - financial	$0.0	$5.0	$5.0	$5.0	$5.0
Telecommunications sales tax exemption	$0.0	$0.0	$3.5	$4.0	$4.0
Certified Capital Companies credit	$0.0	$0.0	$3.0	$3.0	$3.0
One cent reduction in the beer excise tax	$0.0	$0.0	$3.0	$3.0	$3.0
Airline income allocation adjustment	$0.0	$0.0	$3.0	$3.0	$3.0
Computer hardware sales tax exemption	$0.0	$0.0	$3.0	$3.0	$3.0
Theatrical productions sales tax cut	$0.0	$0.0	$2.7	$2.7	$2.7
Telecommunications excess dividends tax cut	$0.0	$0.0	$2.0	$2.0	$2.0
Defibrillator credit	$0.0	$0.0	$1.5	$1.5	$1.5
Freight forwarder allocation adjustment	$0.0	$0.0	$1.3	$1.3	$1.3
Re-manufacturing credit	$0.0	$0.0	$1.0	$1.0	$1.0
Sales tax exemption for farm equipment	$0.0	$0.0	$1.0	$1.0	$1.0
Small brewery tax exemption	$0.0	$0.0	$0.8	$0.8	$0.8
Manufacturers self-use tax cut	$0.0	$0.0	$0.5	$0.5	$0.5
Farmers income tax credit enhancement	$0.0	$0.0	$0.1	$0.1	$0.1
Boxing and wrestling tax cut	$0.1	$0.1	$0.1	$0.1	$0.1
Alternative fuel tax credit	$0.0	$2.5	$0.0	$0.0	$0.0
SUB-TOTAL	$58.1	$34.6	$239.5	$327.0	$375.0
Delayed sales tax exemption for clothing	($150.0)	$0.0	$0.0	$0.0	$0.0
Temporary sales tax exemption for clothing	$50.0	$0.0	$0.0	$0.0	$0.0
TOTAL	($41.9)	$34.6	$239.5	$327.0	$375.0

Source: New York State Division of the Budget, OSC estimates.

Highlights of the 1999-00 tax cut package

Bank and Insurance Tax Rate Cut. The current 9 percent tax rate is reduced to 7.5 percent in three equal increments over three years beginning with taxable years starting on or after July 1, 2000. This will conform these tax rates to those levied on general corporations.

Earned Income Tax Credit (EITC) enhancement. The enacted budget increases the current EITC from 20 percent of the federal EITC to 22.5 percent in 2000 and 25 percent in 2001. This refundable credit is available to working families earning less than $30,095 annually. Federal welfare funds can finance this expansion because EITC is counted as public assistance expenditures. See public assistance section of this report for more details.

Acceleration of Provider Assessment Tax Cut. Provider assessments will be sunset three months earlier than currently scheduled. This will further reduce provider taxes by $55 million. However, a portion of these assessments are reimbursable through Medicaid rates. The estimated net impact on providers is $41 million. The Governor had proposed a one-year acceleration.

Subsidiary Capital Exclusions - utilities. For purposes of calculating the subsidiary capital tax of the Article 9-A parent, capital of gas and electric subsidiaries will be incrementally excludable. Beginning on or after January 1, 2000, 30 percent of subsidiary capital is excludable, which increases to 100 percent beginning on or after January 1, 2001.

Alternative Minimum Tax (AMT) rate reduction. The corporate franchise alternative minimum tax rate is reduced from 3.0 percent to 2.5 percent for taxable years beginning after June 30, 2000.

Pari-Mutuel Tax cut. The tax rate on "on-track" wagering will be reduced from an effective rate of 3.7 percent to 2.6 percent on September 10, 1999 and then to 1.6 percent on April 1, 2001. This will result in more funds available for the New York Racing Association.

Qualified Emerging Technology Companies (QETC) Credit enhancement. The existing definition of QETC is expanded to include sole proprietorships, partnerships, subchapter S corporations, as well as companies engaged in the re-manufacture of printer, ink-jet and photo imaging cartridges used in office equipment.

Estate Tax Federal Conformity. New York's estate law is modified to conform with Federal tax law by expanding the protection for estates containing closely held businesses and farms. This provision allows estates comprised of closely held businesses to choose the current State small business or the Federal deduction, whichever provides the greatest tax benefit. The federal conformity legislation generally applies to estates of decedents dying after 1997.

Petroleum Business Tax cut. The petroleum business tax (PBT) rate on fuels used for commercial space heating is reduced to approximately 1.5 cents per gallon of distillates and 1 cent per gallon for residential petroleum products and eliminated on fuels used for mining purposes starting April 2001. The dedicated transportation funds, which receive certain PBT revenues, are held harmless.

EDZ/ZEA Wage Credit enhancement. The wage tax credit for wages paid in economic development zones and zone equivalent areas is increased from $1,500 to $3,000 for targeted employees and from $750 to $1,500 for other individuals. The period in which taxpayers may claim the ZEA wage credit is increased from two to five years. The provisions take effect for taxable years beginning on or after January 1, 2001.

Gas Importation Tax Cut. Natural gas imported for use in generating electricity is excluded from the tax imposed on gas imported for self-use.

Subsidiary Capital exclusions - Financial Services. Stocks and indebtedness of subsidiaries are excluded from the definition of subsidiary capital for purposes of the subsidiary capital base tax.

Telecommunications Sales Tax exemption. The telecommunications machinery and equipment sales tax exemption is expanded to include machinery, equipment, and apparatus used or consumed in upgrading cable television systems to allow for the receiving, processing or transmission of telecommunications services. It also includes such equipment and tools used in providing internet access for sale.

Delayed sales tax exemption for clothing. Clothing and footwear priced under $500 was scheduled to be permanently exempt from the sales tax beginning December 1, 1999. This implementation will be postponed three months, thus increasing the sales tax on clothing by $150 million compared to current law. This tax increase will be partially offset by approximately $50 million attributable to the two additional temporary sales tax-free weeks that were added.

Temporary sales tax exemption for clothing. Clothing and footwear priced under $500 will be exempt from the sales tax the week of September 1 - 7, 1999 and January 15 - 22, 2000.

Total Value of Tax Cuts Enacted Since 1994-95
(in millions)

Description	1998-99	1999-00	2000-01	2001-02	2002-03
Personal Income Tax	$ 4,801	$ 5,022	$ 5,267	$ 5,526	$ 5,879
User Taxes and Fees	$ 417	$ 584	$ 1,098	$ 1,138	$ 1,178
Business Taxes	$ 1,187	$ 1,570	$ 1,983	$ 2,151	$ 2,264
STAR (STAR & NYC PIT)	$ 582	$ 1,243	$ 2,037	$ 2,797	$ 2,797
Other	$ 400	$ 732	$ 983	$ 1,318	$ 1,366
Total	$ 7,387	$ 9,151	$ 11,368	$ 12,930	$13,484

Source: Division of the Budget

Incremental Value of Tax Cuts Enacted Since 1994-95
(in millions)

Description	1998-99	1999-00	2000-01	2001-02	2002-03
Personal Income Tax	$ 236	$ 221	$ 245	$ 259	$ 353
User Taxes and Fees	$ 121	$ 167	$ 514	$ 40	$ 41
Business Taxes	$ 69	$ 383	$ 413	$ 168	$ 113
STAR (STAR & NYC PIT)	$ 582	$ 661	$ 794	$ 760	$ 0
Other	$ 205	$ 332	$ 251	$ 335	$ 48
Total	$ 1,213	$ 1,764	$ 2,217	$ 1,562	$ 555

Source: Division of the Budget

Fee Actions

The Governor recommended $288.8 million in actions that enhanced, preserved, or increased revenue. The legislature rejected $121 million of these actions. The enacted budget included $168 million of the Executive's proposals. Lottery accounts for most of the difference between proposed and enacted revenue actions. Authorization for the Quickdraw lottery game expired on March 31, 1999 and was reinstated on August 1, 1999. The four month lapse reduced State revenues by approximately $50 million. Quickdraw is now set to expire on March 31, 2001.

Summary of Revenue Actions
(in millions)

Description	Proposed	Enacted
Revenue Enhancements	$82.6	$16.1
Eliminate existing Quickdraw game restrictions	$45.0	$0.0
Other lottery changes	$20.0	$12.0
Impose additional surcharge on racing and wagering taxes	$13.5	$0.0
County clerks retention fees	$4.1	$4.1
Revenue Preservation	$176.1	$126.1
Eliminate Quickdraw sunset	$148.0	$98.0
Extend Manhattan parking provisions	$1.5	$1.5
Extend the existing pesticide registration fees	$1.6	$1.6
Eliminate the sunset on mandatory traffic surcharges	$25.0	$25.0
Fee Increases	$30.1	$25.5
Correctional Services (commissary prices)	$2.8	$2.8
Environmental Conservation (clean air permits and petroleum fee)[30]	$18.0	$13.4
Health (X-ray registration fee)	$0.3	$0.3
Parks and Recreation (day use park fees, golf fees, pool admission fees, cabin fees, empire passport charge)	$9.0	$9.0
	$288.8	$167.7

The loss of these revenues when compared to the Executive was largely "backfilled" or covered by other revenue actions or spending reestimates.

[30] Although the enacted budget included the proposed increase in the petroleum per barrel fee, due to the late budget, the fee was not imposed until August 9. This four month delay reduced revenue by about $4.2 million.

A variety of provisions in the enacted State budget affect local governments, including revenue sharing and other state aid or reimbursement programs, as well as changes in statute affecting local tax collections and mandates. This year the extreme lateness of the budget made it very difficult for local governments to plan. Federal programs and other events also have an impact, such as this year's changes in the food stamp program and the settlement with the tobacco companies. This section of the report discusses municipal and county governments; school districts are covered in the Education section.

Revenue Sharing

Revenue sharing is an unrestricted intergovernmental aid program, providing over $700 million to local governments (with the predominance of the funding going to cities). The Executive had proposed a small year-over-year increase in revenue sharing of $1.7 million. This was the net result of changes in the distressed municipality aid categories which were also rolled together within a single supplemental aid category, under which increases were provided for the cities of Buffalo, Canandaigua and Niagara Falls offset by reductions in current emergency aid allocations for other local governments. The enacted budget provides additional aid totaling $3.8 million in the new supplemental category, restoring some of the reductions proposed by the Executive, and providing an overall year-over-year increase of $5.5 million.

In addition to this small increase, a speed-up in payment of aid is provided for 14 cities, with the intention of providing temporary "one-shot" relief totaling $98.7 million. The budget speeds up payments from March to December in two installments in December of 1999 and 2000, with the amounts accelerated for the year 2000 continuing to be paid on the schedule indefinitely. The legislation states that the funds "shall be" for the entitlement periods ending the preceding June or July. The purpose of this language is to provide for a local fiscal year "spin-up" of revenues, at least on an accounting sheet basis, to provide temporary or "one-shot" fiscal relief; this would not occur otherwise, because the spin-up of payments does not in actuality cross local fiscal years.[31] Although the cities will receive accelerated payments applying to two local fiscal years (ending in 1999 and 2000) the financial benefit will be felt in the current year — the previous year is already over and any accounting change for that period will flow into the current year either as a surplus or a reduced deficit.

There are substantial accounting issues involved with the approach taken in the budget legislation that the Office of the State Comptroller is now reviewing, and there is some question as to whether the "accounting sheet" spin-up will work for all the cities scheduled to receive it. In any event, local governments should understand that this change is a financial manipulation that will not continue to provide relief in future years. If a local government chooses to avail itself of the spin-up

[31]The City of Albany, which uses a calendar year fiscal year is an exception because the acceleration of revenues from March to December results in an actual cash basis spin-up.

by accruing the revenues, and applies them to recurring annual needs, they will have an equivalent budget shortfall to address in 2001-02. Although certainly many local governments may need fiscal relief, there is reason to be concerned about using a gimmick such as this to provide it.

It should also be noted that last year's statutorily convened revenue sharing task force has apparently been disbanded without having issued recommendations. This group was chaired by the Governor's Budget Director and composed also of representatives from the Assembly, the Senate, the Office of Real Property Services and the State Comptroller's Office. The task force was charged with examining current revenue sharing formulas and the general level of aid provided, as well as with developing a new formula and reporting on or before December 31, 1998. The group's last meeting, scheduled for December 17, was canceled by the Budget Director in a letter expressing regret that the statutory deadline would not be met.

The task force had made progress reviewing the existing aid allocations as well as in evaluating factors and approaches to use in a new formula. However, there were stark differences among the members about the general level of aid that could and should be provided. The legislation creating the task force also provided that if a new revenue sharing formula was not enacted by June 30, 1999 that the provisions of the original revenue sharing statutes would return to effect, raising aid by more than $2 billion. This provision was removed in the enacted budget legislation. The act of simply dropping this statutorily promised review without even any acknowledgment tends to reinforce the public's lack of confidence in the State's governing process. It is highly unfortunate that a topic as vitally important as intergovernmental aid was treated in this manner.

Other Aid Programs, Reimbursements and Costs

The enacted budget:

- Allowed a variety of Medicaid cost containment provisions to lapse for the first quarter of the State's fiscal year (April through June), raising costs for counties by $50.6 million (including $37.2 million for New York City).

- Eliminates recently enhanced funding to counties for Medicaid managed care, lowering reimbursements by some $34.4 million annually (including $21.7 million for New York City).

- Enacts the Executive's proposal for drivers license and registration centralization, an efficiency measure which (despite an increase in the percentage of gross fees county clerks keep for transactions they process) will reduce county revenues by about $4 million annually.

- Enacts the Executive's recommendation to end partial reimbursement to counties for housing low-level felons in county jails at a cost of $25 million annually (including $10.5 million for New York City).

- Increases CHIPS (Consolidated Highway Improvement Program) operations and maintenance funding by $2.6 million annually. The Legislature also restored proposed cuts: $25.6 million in CHIPS capital funds, $4.7 million in Marchiselli aid (representing the State matching share of federal highway and bridge funding). These aid programs together provide approximately $325 million in funds annually to local governments (primarily municipalities other than counties).

- Adds $1.35 million to pick up the full cost of the recent District Attorneys' salary increase.

- Allows local governments to opt out of the permanent sales tax exemption for clothing each year — permitting governments that initially choose to participate, but experience financial difficulties later, to then drop the exemption. The starting date of the general sales tax exemption was also delayed from December 1, 1999 to March 1, 2000 and two new tax-free weeks were added (September 1-7, 1999 and January 15-21, 2000).

- Adds a series of exemptions to the sales tax (including telecommunications items, farming equipment, and various vending, repair and maintenance services) which upon full implementation will annually decrease local government revenues by about $14 million.

Other issues affecting local governments include:

- Food Stamps — changes at the federal level, in combination with the State's approach, passes the $63 million cost of administering the program to the counties (including $40 million for New York City).

- Federal maintenance of effort provisions for TANF (Temporary Assistance to Needy. Families) will result in $75 million additional spending by counties in the 1999-00 State fiscal year; this impact may grow in 2000 and beyond.

- Tobacco Settlement — Counties in New York State are expected to begin receiving their portion of these funds by next year. The precise distribution is not yet known (a detailed discussion of this issue can be found in the Health and Social Services section of this report) but it is generally expected that county governments will receive somewhere in the area of $12-13 billion over the next 25 years (with New York City receiving slightly more than half). The counties expect to receive slightly more than $300 million in calendar year 2000.

The county governments have vigorously objected to the additional costs that they are facing as a result of the State budget, which they estimate to be $250 million annually (including New York City impacts). This figure includes the increased costs occurring under the federal food stamps and TANF programs, as well as the full annual eventual cost of the miscellaneous sales tax exemptions and other changes. Although the tobacco settlement itself provides good financial news for the counties, the down side to this situation is that some State leaders are citing it as justification for passing on increased costs to the counties.

Local Governments in Fiscal Stress

Although most of New York State's local governments have been able to deal successfully with mounting fiscal pressures during the past decade, some have not, experiencing severe financial problems. Deficit financing has been approved for a number of municipalities and in several prominent cases, financial control boards have been put in place to ensure that the structural imbalances creating the problems are addressed.

The State Comptroller, in conjunction with the Governor, has proposed legislation that is intended to promote fiscal stability among New York State local governments. The legislation would provide an early warning of fiscal stress, preclude the necessity of the entire Legislature approving requests for deficit financing by passing such authority on to a five member board appointed by the governor and legislative leaders, provide a level of oversight by the State Comptroller for local governments that are experiencing serious and recurring fiscal stress, or are in default or imminent danger of default on debt service and enable financing through the Municipal Bond Bank Agency for those governments that are unable to sell their obligations in the public debt market. This legislation was introduced, but not passed.

During this session, the State Legislature acted on several requests to help specific local governments address financial problems:

- The Town of Babylon, and the North Babylon and Potsdam school districts sought deficit financing relief from the Legislature and had their bills approved.

- Nassau County sought authorization to impose a one percent tax on real property transfers within the county. This legislation was passed although only after much deliberation about whether such authorization should be contingent upon State oversight of county finances. The bill passed without any oversight provision.

The continuing requests for financial relief highlight the need for a comprehensive approach to addressing fiscal stress among local governments. The budget's response to Nassau County's fiscal problems — adding a new tax without any additional State oversight — is only a stopgap solution. The Comptroller's Office will continue to monitor the situation in Nassau County but it appears that a stronger oversight mechanism or supervisory board will be necessary to address the problems.

Changes to the Proposed Capital and Financing Plan

The five year capital plan submitted with the 1999-00 Executive Budget was a significant departure from recent debt issuance and capital financing plans. In prior years, the capital plan assumed a growing level of debt outstanding, increasing debt service costs, and a shrinking share of capital financed on a pay-as-you-go basis.

The Executive Budget five year capital plan proposed a $1.3 billion increase in debt outstanding in 1999-00 followed by four years of maintaining debt at about that year's $37.5 billion level. The prior capital plan assumed a steady increase in debt, reaching $41.9 billion in 2002-03. The reduction in new debt was proposed to be accomplished by increasing the share of capital spending financed with cash. Total capital spending remained at roughly the same level as the prior plan.

The Governor is required to provide a revised five year capital plan, reflecting changes made between the Executive Budget proposal and enactment, on or before November 1, 1999. Preliminary analysis indicates the net impact of changes to the proposed five year capital plan increases capital spending by approximately $328 million. The bulk of these additions will result in added State debt; however, it is unclear how much of the new debt may be offset by using Local Government Assistance Corporation (LGAC) capital reserves to defease outstanding LGAC bonds.

Moreover, the Executive's original proposed reductions were made possible by significantly increasing the amount of capital financed in cash with State dollars, large projected increases in federal funds, and use of a portion of the national tobacco settlement for pay-as-you-go financing. It is unclear whether any of these assumptions will materialize during the mutiyear period.

The enacted budget made significant changes to the debt and capital portions of the Executive Budget. The net impact of the capital additions was an increase of approximately $328 million in capital spending, with the bulk of the additions resulting in higher State debt.

Capital additions of $583 million include the following:

- ✓ $145 million for RESCUE (REbuilding SChools to Uphold Education program). This program will provide additional funding for school construction and rehabilitation for instructional facilities.

- ✓ $95 million for the Jobs 2000 for New York State program (J2K). This includes $24 million for the Department of Environmental Conservation for water pollution control, $22.5 million for the Environmental Facilities Corporation for Pipeline for Jobs program, and $47.5 million for the new Office of Science, Technology, and Academic Research.

- ✓ $55 million for the housing needs of the mentally ill. Of this amount, $50 million is to be used for payment to municipalities or not-for-profit community providers for acquisition of property, design, construction and rehabilitation of housing for mentally ill persons. Eighty percent of this funding is to be matched 50/50 with local governments. These new resources are expected to support development of 900 community residential beds for mentally ill persons.

- ✓ $15 million for child care facilities development. Funding will be provided for rehabilitation or construction to establish, expand, or develop a licensed child care center or registered school-age program which is intended to serve the needs of low-income working families or an area with demonstrated child care need. These new facilities must be used as child care facilities for at least ten years with an average of 25 percent of its available child care slots set aside for low-income families.

- ✓ $15 million increase in existing programs for affordable housing including: $3.5 million for the affordable housing corporation, $1.0 million for housing opportunities for the elderly program, $4.0 million for the low income housing trust fund, $3.0 million for homes for working families program, and $1.5 million for the public housing modernization program.

- ✓ $120 million for State transportation programs. This reflects a faster pace of contract awards ("letting levels") for state highway, parkway, bridge, and NYS Thruway projects than provided for under the Governor's plan.

- ✓ $30 million in restorations for CHIP and Marchiselli. The Executive Budget had included reductions in these local transportation programs that were restored in the enacted budget.

- ✓ $8.3 million for the Olympic Regional Development Authority for services and expenses related to construction of a combined luge and bobsled facility.

- ✓ $25 million for Empire State Development Corporation for costs related to economic development, land acquisition and heritage trails.

- ✓ $75 million for pay-as-you Community Facilities Enhancement projects. The Governor had proposed reducing this program by $75 million; this was rejected in the enacted budget. Although it does not change the total funding for the program from last year it represents an addition when compared to the Executive Budget and the associated capital plan.

Capital reductions of $225 million include the following:

- ✓ $180 million in State Funds for a third 750-cell maximum security prison. This proposal also included the use of $80 million in federal funding.

- ✓ $75 million for development of a secure youth facility.

The enacted budget included a controversial language change that diverted Clean Water/ Clean Air Bond Act monies from funding for small business compliance with water pollution standards (water and wastewater infrastructure improvements) to funding for new infrastructure for business ventures, with no limitation on the size of the business.

The enacted budget includes an additional deposit of $250 million to the Debt Reduction Reserve Fund (DRRF) as proposed by the Executive. However, the Executive Budget proposed transferring this funding to a special revenue fund. Instead, the funds will remain in the General Fund. Since transfers to other funds are included in disbursements, the Executive Budget "spent" the $250 million by transferring it to the special revenue fund. By leaving the $250 million in the General Fund with no planned spending for the current year, the enacted budget now reduces General Fund spending by $250 million in 1999-00 when compared to the proposed budget. Monies in the DRRF will be used primarily to replace bond financing with pay-as-you-go spending.

The enacted budget also includes plans to replace the current Local Government Assistance Corporation (LGAC) capital reserves with a surety bond. The reserves will then be used to defease outstanding LGAC bonds. When completed, this is expected to reduce LGAC debt by approximately $400 million. Although the details of this transaction have not been fully developed, initial analysis raises questions about whether or not the transaction will result in savings. Bonds should not be redeemed unless there is net present value savings. Without true savings, it appears the transaction would be done solely to reduce the amount of debt for public relations purposes.

Debt Condition

New Yorkers face one of the highest debt burdens and the lowest credit ratings. In the past ten years, debt service on State-supported debt has increased from 3.5 percent of All Governmental funds receipts to 5.0 percent. Debt service is taking a larger and larger piece of State revenues.

Growth in Debt Service Compared to Receipts (dollar amounts in millions)

Fiscal Year	All Governmental Funds Receipts	Total State-Supported Debt Service	Debt Service as a Percent of Revenue
1989-90	$ 44,905	$ 1,577	3.5%
1990-91	$ 47,236	$ 1,511	3.2%
1991-92	$ 51,706	$ 1,922	3.7%
1992-93	$ 54,601	$ 2,198	4.0%
1993-94	$ 57,971	$ 2,266	3.9%
1994-95	$ 61,106	$ 2,490	4.1%
1995-96	$ 62,969	$ 2,749	4.4%
1996-97	$ 62,886	$ 2,827	4.5%
1997-98	$ 66,127	$ 3,195	4.8%
1998-99	$ 70,739	$ 3,387	4.8%
1999-00 (est.)	$ 74,956	$ 3,759	5.0%

Source: Annual Information Statement, August 1999.

New York's state-supported debt burden has increased from $760 per person in 1989-90 to an estimated $2,064 per person in 1999-00. This debt represents over 6 percent of New York's personal income.

Growth in State Related Debt
As a Percent of Personal Income and Per Capita
(dollar amounts in millions)

Fiscal Year	State-Supported Debt	Per Capita	As a Percent of Personal Income
1989-90	$ 13,674	$ 760	3.5%
1990-91	$ 17,174	$ 955	4.1%
1991-92	$ 21,562	$ 1,196	5.1%
1992-93	$ 23,971	$ 1,326	5.4%
1993-94	$ 26,696	$ 1,472	5.8%
1994-95	$ 28,169	$ 1,552	5.9%
1995-96	$ 31,009	$ 1,709	6.2%
1996-97	$ 33,130	$ 1,827	6.3%
1997-98	$ 34,247	$ 1,888	6.3%
1998-99	$ 35,842	$ 1,969	6.2%
1999-00 (est.)	$ 37,561	$ 2,064	6.2%

Source: Annual Information Statement, August 1999.

New York's credit rating by Standard and Poor's and Moody's is the second lowest in the nation, only Louisiana receives a lower rating. In addition, New York has stayed at the bottom while other states have been receiving improved ratings over the years.

Standard and Poor's Ratings of State General Obligation Bonds (As of May 1999)

AAA	AA+	AA	AA-	A+	A	A-
Georgia	Delaware	Alabama	Connecticut	California	**New York**	Louisiana
Maryland	Florida	Alaska	Montana	Hawaii		
Minnesota	Kansas	Arkansas	North Dakota	Massachusetts		
Missouri	Maine	Illinois	Pennsylvania			
North Carolina	New Hampshire	Kentucky	Rhode Island			
South Carolina	New Jersey	Michigan	Vermont			
Tennessee	New Mexico	Mississippi	West Virginia			
Utah	Ohio	Nevada				
Virginia	Washington	Oklahoma				
		Oregon				
		Texas				
		Wisconsin				

Source: Standard and Poor's Corporation.

Moody's Ratings of State General Obligation Bonds (As of May 1999)

Aaa	Aa1	Aa2	Aa3	A1	A2	A3
Georgia	Delaware	Alaska	Alabama	California	**New York**	Louisiana
Maryland	New Jersey	Florida	Arkansas	Massachusetts		
Minnesota	New Mexico	Michigan	Connecticut	Pennsylvania		
Missouri	Ohio	Mississippi	Hawaii	Rhode Island		
North Carolina	Washington	Nevada	Illinois	West Virginia		
South Carolina		New Hampshire	Maine			
Tennessee		Oregon	Montana			
Utah		Texas	North Dakota			
Virginia		Vermont	Oklahoma			
		Wisconsin				

Source: Moody's Investors Services

New York Compared to Other States

According to a Moody's Investors Service report, *1999 State Debt Medians*, New York ranks among the top four of all states in two measures of tax-supported debt burden:

- New York is fourth highest in tax supported debt per capita, with Connecticut, Hawaii, and Massachusetts the three states with heavier debt loads per person. New York's per capita debt of $1,986 is nearly three times the national average of $697.

- Per capita figures do not account for differences in ability to pay for debt among the states. A more precise measure relates debt to the total income of a state's residents. New York ranks fourth in tax supported debt as a percentage of personal income, with the same three states mentioned above having higher burdens. New York's debt burden at 6.6 percent of personal income was over two times the average level of all states.[32]

Debt Reform

It is clear New York needs to improve its debt condition. Although the Executive's proposed capital plan addressed some of the symptoms of New York's weak debt management practices, it did not address the underlying problems. The significant improvements are not required by statute and could be reversed at any point. New York continues to need permanent fundamental reform of its debt practices.

Despite debt reform proposals also being introduced by the majority and minority in both the Assembly and the Senate, the enacted budget included no meaningful debt reform. The Comptroller

[32]Moody' Investors Service, 1999 State Debt Medians, March 1999.

introduced a comprehensive package of debt reform legislation that would create meaningful reform through statute, which could be enacted immediately to limit new debt, and a constitutional amendment, which would provide a permanent solution. Most of the improvements made to the current capital plan are temporary in nature and could easily revert back to less attractive plans.

The package of legislation proposed by the Comptroller would:

- ✓ **Ban back-door borrowing**. The State would be prohibited from using backdoor borrowing through public authorities to finance State projects.

- ✓ **Create a new form of debt to replace back-door borrowing.** This new type of debt would be backed by a dedicated revenue source (to be specified in future legislation). Because this debt would be paid whether or not there is an appropriation, it should result in lower interest rates and reduced borrowing costs.

  The legislation creates two caps to limit debt: the first limits new debt as a percent of personal income; the second cap limits debt service as a percent of revenues. The two-pronged approach will ensure that future debt is affordable. The capital plan submitted with the 1999-00 budget significantly reduces planned debt issuance. If these proposed debt levels are maintained, the caps will not limit debt during the next five years. However, based on the previous capital plan, the caps would have begun imposing limits on new debt in 2001-02. The caps are designed to eventually reduce debt outstanding to a level closer to the national average.

- ✓ **Cap debt**. All future General Obligation bonds and the new revenue debt would be capped at 3.5 percent of state personal income; the cap is cumulative and applies to all debt issued and outstanding after the legislation is enacted.

  - If enacted through statute, the cap could take effect immediately and would be fully phased in at 3.5 percent of personal income in 2008-09. The constitutional amendment would take effect in 2002-03, and would be phased in by 2011-12.

  - The cap would provide a long-term approach to cutting New York's debt -- currently at 6.2 percent of state personal income -- by almost 50 percent.

- ✓ **Cap debt service**. No debt could be issued if the State's total debt service exceeded 5.75 percent of governmental funds receipts. In 1999-00, debt service is projected to represent 5.0 percent of governmental funds receipts. The previous capital plan would have resulted in debt service reaching the cap in 2000-01.

- ✓ **Limit debt to capital projects**. Debt could not be issued to finance operating expenses.

- ✓ **Create a Debt Management Board**. This Board would set policy related to debt management issues (such as refundings, debt structure, credit enhancement) and set policy guidelines on the

use of debt for the capital budget. It would include the Governor, Comptroller, Budget Director, Assembly Speaker and Temporary President of the Senate.

✓ **Require Public hearings**. The Governor would be required to hold public hearings on the capital plan.

✓ **Allow multiple bond acts**. Eliminates the existing prohibition against multiple bond resolutions being placed on the ballot in a single year to encourage more frequent use of GO debt and enhance public participation.

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