Nassau County Interim Finance Authority

NIFA

REVIEW OF THE MAY 1, 2009 NASSAU COUNTY MULTI-YEAR FINANCIAL PLAN UPDATE AND RELATED MATTERS

May 28, 2009

NASSAU COUNTY
INTERIM FINANCE AUTHORITY

DIRECTORS

Ronald A. Stack
Chairman

Stanley Kreitman

Paul J. Leventhal

Gregory J. Raphael

Robert G. Smith

Christopher P. Wright

STAFF

Evan L. Cohen
Executive Director

Jane F. Cunneen
Acting Treasurer

Laurie A. Leat
Corporate Secretary

Maria Kwiatkowski
Deputy Director

Jeremy A. Wise
General Counsel

Table of Contents

I. INTRODUCTION

At its meeting on December 3, 2008, NIFA's Directors concluded that the County's Multi–Year Financial Plan for Fiscal Years 2009–2012 (the "Plan") was in compliance with the NIFA Act. However, they also found that the Budget and Plan were problematic because they:

(1) Assumed optimistic rates of economic recovery and growth despite the crises affecting the Nation, the region and the County.

(2) Relied on non-recurring revenues and further depletion of reserves, which were already at very low levels.

(3) Created few new or significant revenue generators.

(4) Used optimistic projections of, as yet unproven, cost saving measures.

(5) Deferred debt service payments.

(6) Contained initiatives that required uncertain State and County legislative approvals.

Consequently, the Directors of NIFA recommended that the Plan be closely monitored and required the County Executive to submit a contingency plan in January of 2009 (the "Contingency Plan") and an updated Plan to NIFA no later than May 1, 2009 (the "Update").

What follows is an analysis and review of the County's Contingency Plan, Update, and fiscal health as of this writing. If the reader desires to more fully understand NIFA's opinions regarding the County's financial position, they should also read NIFA's October 21, 2008 and December 3, 2008 reports on the Plan, which can be found on the NIFA website at www.nifa.state.ny.us.

[THIS PAGE IS INTENTIONALLY LEFT BLANK]

II. SUMMARY OF FINDINGS

The County Executive has prepared the Update to address an estimated $130 million deficit in the FY 2009 Budget and the continuing deficits in the Out-Years. The Update has succeeded in presenting a roadmap to a balanced Budget, but only if the County successfully implements the strategies outlined in its Contingency Plan to eliminate the shortfalls it projects within its 2009 baseline. Even if these strategies are successful in FY 2009, they do not adequately address continuing baseline gaps in the Out-Years.

For FY 2009, the Update includes such gap-closing items as labor concessions (achieved and expected); funds to be received from the Federal government as part of its stimulus package; and anticipated revenue from the recently approved Red Light Camera ticketing program and the sales tax on residential energy.

We emphasize our concern that these strategies will close the projected gap only if:

1. *the County does not experience negative growth in sales tax receipts beyond the 6% decline from FY 2008 that it is currently projecting, and/or*

2. *other negative variances, such as from a failure to achieve its labor savings target, do not materialize.*

While the Update acknowledges the significant fiscal challenges that remain to be addressed, it also continues the County's reliance upon skill in managing through crises and obtaining bipartisan support for uncertain State and County legislative initiatives. It also lacks sufficient long term structural changes, which are still needed in the Out-Years.

A lack of long-term planning and fiscal discipline led to the County's initial fiscal crisis, which was the impetus for the creation of NIFA. Consequently, NIFA has continually urged the County to institutionalize sustainable long-term budgeting practices, which do not rely on short-term solutions to systemic problems. Past practices exacerbated the structural imbalance between current revenues and expenses.

The County's budgeting and planning process have improved since the creation of NIFA and this progress has helped the County during the current global economic crisis, but much work remains to be done. We will continue to assist in the furtherance of our shared mission by providing our expertise and resources to that end.

MAJOR FINDINGS

We find that the County has fulfilled the requirement by NIFA that it submit an Update, but in doing so, it has:

1) Continued to rely on non-recurring resources, the expertise of the current Administration, optimistic assumptions, and certain unsuccessful initiatives of prior years.

2) Balanced its Budget through the use of: bond proceeds to pay for operating expenses; the draw-down of reserves and fund balance; and one-time revenues such that its recurring expenditures still exceed its recurring revenues.

3) Continued to show significant Out-Year budget gaps that are anticipated to grow from $72.3 million in FY 2010 to $225.9 million in FY 2012.

ADDITIONAL FINDINGS

The County has:

1. Underestimated Nassau County's potentially deeper exposure than other counties to the economic downturn and resultant sales tax declines because of its escalated property values and significant exposure to Wall Street's job losses.

2. Utilized $23.2 million of bond proceeds, which resulted from an over-issuance of bonds, to close a gap in the FY 2008 operating budget rather than the more appropriate use thereof, which would have been to retire an equal amount of bonds.

3. Paid $58.8 million of certiorari refunds in FY 2008 from bonds proceeds and only $40 million from its operating budget on a pay-as-you-go ("PAYGO") basis, a reduction in its PAYGO program and a backtracking from its commitment to discontinue the use of bond proceeds to pay cert claims.

4. Planned to use $28 million of bond proceeds in FY 2009 to pay for certiorari refunds.

5. Experienced significant turnover in its Office of Management and Budget, which is ctritical to the County's recovery and planning efforts.

6. Appointed a new assessor to once again try to reduce the amount of refund liability on commercial property cases, which have traditionally been the area of highest exposure for the County.

7. Announced that it will be the beneficiary of approximately $80 million (over the next two years) in non-recurring Federal stimulus relief that will be used to subsidize operating expenses. While these funds help close gaps through next year, they merely postpone the difficult decisions that must be made when those funds are no longer available.

8. Assumed that once it downsizes through early and/or accelerated retirements, health and safety concerns will not force the replacement of certain key employees.

9. Increased significantly its planned cash flow borrowings and resultant interest costs in FY 2009 from $260 million in the Plan to $315 million in the Update.

10. Utilized aggressive assumptions regarding certain new revenue streams and savings in such areas as voluntary separations and retirements.

11. Increased the property tax levy in the Major Funds by $32.7 million in FY 2009 (4.2%), and planned further increases of $31.6 million in FY 2010, $64.5 million in FY 2011 and $98.7 million in FY 2012.

12. Continued to balance its budget with one time resources taken from its significantly depleted reserves. It is noteworthy that the drawdown of these reserves in better economic times has limited the amount available to cushion the impact of the current economic crisis.

[THIS PAGE IS INTENTIONALLY LEFT BLANK]

III. FY 2008 OPERATING RESULTS

The County reported that it ended FY 2008 with an operating surplus of $2.1 million. However, in the County Comptroller's report on the FY 2008 year-end results he agreed with NIFA's assessment that the FY 2008 surplus included the use of a significant amount of non-recurring revenues and bond proceeds as operating income, thereby contributing to a large and growing structural deficit.

The County's underlying financial weakness can be measured by examining the magnitude and direction of the structural deficit - the difference between recurring revenues and expenditures. The Comptroller noted that the structural deficit had grown in each of the last four years from $36.8 million in FY 2005 to $59.0 million in FY 2006, $122.0 million in FY 2007, and $122.9 million in FY 2008. His conclusion means that the structural deficit in FY 2008 was larger than at any time since FY 2001, as discussed beginning on page 23.

When we examined the County $2.1 million surplus, we found that it was based on the following major actions:

- draw down of limited designated reserves — $48.3 million
    - pensions - $24.5 million
    - tobacco proceeds - $23.0 million
    - termination payments - $0.8 million
- use of fund balance — $17.9 million
- use of bond proceeds to pay operating expenses — $82.0 million
    - resources to pay tax certiorari refunds - $58.8 million
    - resources from over-funded capital projects - $23.2 million

These actions are troubling because:

- Use of bond proceeds and off-budget reserves to pay operating expenses masks an imbalance that many would characterize as a deficit, and also exacerbates the budgetary gaps that must be resolved in future years, both by deferring the necessary steps to correct the imbalance and layering on debt service for current year borrowings.

- The County has continued to rely on its practice of bonding items that should be funded with operating income; for example, tax certiorari refunds and non-certiorari judgments and settlements.

In our view, a true structural surplus will only arise when the necessary steps are taken so that current County services can be sustained by revenues generated in the same year. This is prudent fiscal practice and is also more equitable to future generations that are otherwise forced to pay debt service on bonds used to provide “budgetary balance” in the current fiscal year.

IV. STATUS OF FY 2009 OPERATING RESULTS

As a condition of its approval of the County's Plan, NIFA required the County to develop a comprehensive contingency plan to address the risks in the Budget, which were increased by the rapidly deteriorating economy. In compliance with this requirement, the Administration submitted a contingency plan to NIFA on February 2, 2009 (the "Contingency Plan").

The County estimated in its Contingency Plan that, in the absence of corrective action, it faced a potential $130 million budget gap in FY 2009. This estimate was driven by a $100 million projected shortfall in sales tax revenue, inclusion of $20 million of revenues in the budget from initiatives that were not yet approved by the State, and an anticipated $10 million shortfall in investment income. The County also identified an additional $37 million in other risks that it maintained could be offset by budgeted contingencies and other intra-year positive variances.

The County currently projects that, after implementing the corrective actions articulated in its contingency plan, and as described below, it will end FY 2009 with a modest operating surplus in its Major Funds by offsetting certain negative variances with certain positive variances.

These negative variances include:

- $75.4 million – shortfall in sales tax revenue;
- $40.5 million – additional termination payments to retiring employees;
- $11.0 million – shortfall in available 2008 surplus;
- $10.5 million – initiatives requiring State approval;
- $6.6 million – increased Social Services caseload expenditures;
- $5.9 million – higher Workers' Compensation costs; and,
- $5.5 million – lower investment income from reduced interest rates.

The County projects a number of offsetting positive variances in certain expenditures and revenues, including significant prospective workforce-related savings. The positive variances also include the temporary relief from Medicaid expenditures afforded by the Federal stimulus plan (American Recovery and Reinvestment Act of 2009), and the bonding of termination payments it expects to make this year to certain retiring employees.

These positive variances include:

- $51.0 million – capitalizing additional termination payments;
- $42.2 million – additional Federal Medicaid funding (FMAP);
- $38.2 million – lower salaries and wages from labor negotiations (net);
- $8.1 million – lower fringe benefits due to premiums and headcount (net);

- $5.8 million – reduced interest costs due to lower rates and the timing of certain borrowings;
- $5.5 million – lower payments to local governments (sales tax distribution);
- $5.4 million – lower general and utility expenses.

<u>Sales Tax</u>

Sales tax revenue comprises almost 40% of the County's total revenue stream, which makes this an area that both the County and NIFA need to continue to monitor carefully. The Update has reduced the County's FY 2009 sales tax forecast by $75.4 million to $962.4 million based on its revised assumption that baseline sales tax revenue will decline by 6% from FY 2008 levels. This forecast includes an additional $18 million the County estimates it will realize from the imposition of a new sales tax on residential energy.

While the County's current forecast is more conservative than assumed in the Budget, year-to-date collections have been down 10.4% compared to the same period in 2008. However, the County anticipates that the current weakness in sales tax receipts will moderate in the coming months and average out to its revised target of negative 6%. We calculate that the remaining sales tax receipts for FY 2009 can fall by no more than 1.8% below last year's levels in order for the County to reach its revised target.

The County is hopeful that the Federal stimulus program will begin to boost the economy by the summer and result in increased consumer spending and concomitant sales tax revenue. However, there is disagreement among economists about the timing or likely effectiveness of the stimulus. We remain skeptical based upon recent government reports that continue to indicate further declines in retail sales activity.

Contingency Plan

As noted in the resolution of NIFA's Directors at their December 2008 meeting, submission of a detailed contingency plan to NIFA in early 2009 was a major factor in their decision to conditionally approve the County's Plan. NIFA requested the Contingency Plan be submitted within that timeframe for two reasons:

1. To prepare for what many believed was an escalating economic downturn; and,

2. To address risks in the Plan that were identifiable, such as labor savings, overtime expenditures, departmental revenues, and the amount of the FY 2008 budgetary surplus.

The Administration submitted the Contingency Plan on February 2, 2009. It demonstrated that the County understood the enormity of the challenge it faced by projecting a deficit of $130 million in FY 2009. The projection included a downwardly revised sales tax growth rate assumption of negative 6%. The Contingency Plan Strategy is outlined in the following table and its major components are discussed below.

FY 2009 CONTINGENCY PLAN STRATEGY

PROJECTED DEFICIT	$130 MILLION
	(in millions)
Sales Tax	$100.0
State Legislative Actions	20.0
Investment Income	10.0
CONTINGENCY PLAN	
FEDERAL GOVERNMENT	
Stimulus Package/FMAP	$40 - $50
NY STATE GOVERNMENT	
Cigarette Tax	$ 20.0
Ticket Surcharge	6.0
Red Light Cameras	4.0
or	
Home Heating Fuel Tax (Sales Tax Extension)	$ 18.0
HHS Vertical Program Cuts	12.0
Local Government Assistance to Villages	1.2
LABOR AND MANAGEMENT	
Layoff of 250 PBA Employees	$ 13.0
Layoff of 320 CSEA Employees	10.0
Layoff of 100 Correctional Officers	8.7
Ordinance Employee Savings:	5.0
County Closing-26 Days	20.0
or	
7% Salary Reduction	$ 55.0

The County's three-point Contingency Plan provided the specificity lacking in previous submissions. Even so, it is now apparent that some of the expected "solutions" to the current fiscal crisis and projected deficit will not be realized.

Federal Government

The County expects to receive money from the Federal stimulus plan that is providing direct assistance to local governments. One form of assistance is provided by temporary increases in the Federal Medical Assistance Percentage ("FMAP"), a percentage used to calculate the Federal contribution to the Medicaid program for the period of October 1, 2008 through December 31, 2010.

The Update includes the receipt of approximately $42 million in FY 2009 and almost $39 million in FY 2010. While helpful in the near term, the funding is non-recurring and will not provide recurring budget relief in the Out-Years.

State Government

The County is also counting on revenue initiatives to help reduce the current and Out-Year gaps by instituting new tax and fee programs that would provide recurring revenue streams. Of the three proposed, only the Red Light Cameras legislation has passed and is ready to be implemented. Under a five-year pilot program, the County is planning to have completed installation of 111 cameras at 47 intersections by December 2009. The County estimates that it will collect approximately $4 million in FY 2009 and $20 million annually in the Out-Years. While the County has a reasonable methodology for its projections, actual results are uncertain.

The Cigarette Tax, although recently approved by the Nassau County Legislature, still requires State approval. This revenue initiative is not currently a dependable contingency. Similarly the Ticket Surcharge, which would provide State relief to the County for its patrol of State highways, is also problematic.

The County has also indicated that it may have to make substantial cuts to its Health and Human Services programs by as much as $12.0 million, but only if other State approval is not received for new taxes or County employee concessions are not adequate to cover its budgetary shortfalls.

These cuts are proposed within programs that do not receive New York State Aid or Federal reimbursement. Therefore, their funding levels are completely within the discretion of the County. The County departments that could be affected are:

- Health Department
- Mental Health, Chemical Dependency, & Developmental Disabilities
- Senior Citizen Affairs
- Department of Social Services
- Youth Board

The County has stated that the programs considered for cuts would not be eliminated. Core services would remain intact, but programs that have been expanded in recent years would be trimmed.

In these difficult economic times with more Nassau County citizens losing jobs, the need for these services will probably grow, not decline. Therefore, we urge the County to carefully consider the impact of cutbacks in these areas.

Labor Concessions

Salaries and related costs comprise nearly half of the County's operating expenses. Consequently, the Contingency Plan carefully examines this area in order to provide necessary savings in both the current and Out-Years.

Originally, the County highlighted a layoff target of approximately 700 employees as its primary method of achieving salary savings. Currently, savings are expected to be realized through a variety of labor concession agreements rather than layoffs.

The original projection of $55 million in savings from labor concessions included ShOA and Ordinance employees in its computation. At the time of the Update, ShOA had not come to an agreement with the County regarding proposed savings strategies. Therefore, the negotiated labor concessions are expected to yield savings of only $49.1 million in FY 2009. The key elements of the plan are summarized in the following sections.

Lag Payroll

The County plans to realize savings by lagging payroll by two weeks. The projected current-year savings is approximately $21.4 million and is based on agreements by the County's unions, excluding ShOA. The projected budget relief accounts for nearly half of the anticipated labor savings in FY 2009. Employees will receive the full amount of the lag payroll upon separation so the budgetary impact will vary depending upon when the employees ultimately leave County service. However, this represents only a timing of expenses, deferred to subsequent periods, and not an overall savings in the aggregate.

Attrition

The County projects attrition savings from CSEA-represented employees of $7.5 million in FY 2009 and $15.0 million in each of FY 2010 and FY 2011. Although the County is basing its projection on the assumption of 325 separations, the costing conservatively is applied to only 200 of those positions to account for separation expenses as well as the potential that some of these positions may be in titles that are partially "reimbursable" by Federal money or must be refilled for health or safety reasons. If the County does not meet its targets, it has stated that it will consider other labor cost-saving measures such as lay-offs.

Pay Raise Deferrals

The total savings from pay raise deferrals for CSEA employees is approximately $7.5 million in each of FY 2010 and FY 2011. These savings will be accomplished by deferring the payment of raises scheduled to be earned in those years until FY 2014 and FY 2015, respectively. It is noteworthy that the employees are not forgoing raises for the years indicated, but merely deferring when they are received. This means that the County will realize budget relief in FY 2010 and FY 2011, but in same fashion as the lag payroll initiative, it will incur these expenditures as well as already scheduled increases in the years when they are paid.

Holiday/Equipment Pay

The projected amount of savings for holiday/equipment pay for police unions is approximately $6.9 million in FY 2009. Payment for three holidays eliminated in each of FY 2009, FY 2010, and FY 2011 will be added to each employee's vacation bank or cashed out at separation. Similarly, payment for equipment and clothing allowances in those years will be deferred and paid out upon separation.

Police Unions Headcount Plan

These savings are attributable to a combination of planned headcount reductions and proposed civilianization of some positions. The County projects savings of $7.3 million in FY 2009, $15.2 million in FY 2010 and $16.9 million in FY 2011.

The County has stated that labor's willingness to make these concessions has helped to avoid the lay-off of hundreds of employees and the need to implement a proposed 26 day County shut-down. However, both of these options, lay-offs and a County-wide closing, are still available should the County not meet its voluntary separation targets or receive local and State approval to bond associated termination costs.

While the labor concessions may provide budgetary relief, we remain concerned that the voluntary termination incentive program may result in termination expenditures as high as $75 million in FY 2009, a majority of which the County plans to finance with bond proceeds. The County's plan to issue debt to pay this expense places a burden on future taxpayers in the form of debt service costs.

Bonding for operating expenses was part of the pattern that led the County into a fiscal crisis necessitating the formation of NIFA. We also warn that some of the other labor concessions (e.g. lag payroll and wage deferrals) merely defer salary related expenses in order to achieve savings in the near term, thereby placing additional stress in later years.

NIFA is also concerned about how the anticipated loss of several hundred employees coupled with the high number of current vacancies will affect programs and services. Even if the County successfully consolidates functions and institutes efficiencies to mitigate these headcount reductions, the County may be creating a vacuum of highly qualified, well trained and efficient senior level employees.

In short, while the County and its employees have worked cooperatively to form agreements that can provide savings in its salary and wages baseline, the Administration must work to manage the headcount reductions in a manner that will preserve the quality of programs and services that the taxpayers of Nassau County have come to expect in return for their high taxes.

V. MULTI-YEAR FINANCIAL PLAN UPDATE

THE BASELINE

The County estimates that when compared to the adopted Plan, its baseline gaps have improved by $36.0 million in FY 2010, but have grown by $8.5 million in FY 2011 and $26.5 million in FY 2012, as shown below.

BASELINE GAPS
FY 2009-2012

($ in millions)	FY 2009	FY 2010	FY 2011	FY 2012
Adopted MYP	$0.0	($108.3)	($165.0)	($199.4)
MYP Update	0.0	($72.3)	($173.5)	($225.9)
Change	**$0.0**	**$36.0**	**($8.5)**	**($26.5)**

The improvement in FY 2010 can be attributed, in part, to annualized salary savings the County expects to realize from significant headcount reductions in FY 2009 and from the deferral of contractual increases originally scheduled to be earned and paid in FY 2010 and FY 2011. The favorable projection also includes the full year value of revenue ($39.4 million) the County expects to realize from its imposition of a sales tax on residential energy, beginning in mid-2009.

Part of the increased gaps that are projected in FY 2011 and FY 2012 can be attributed to the impact of current sales tax weakness, which was mitigated in FY 2009 and FY 2010 by non-recurring solutions, such as temporary Federal Medicaid relief and wage deferrals.

While the County's estimate of its Out-Year baseline gaps has not increased significantly, they are still large in relation to the budget. In addition, should the local economy experience a deeper and/or more protracted contraction than assumed, sales tax weakness would be exacerbated thereby increasing the size of the gaps. We also note that the County has left unchanged its projection of Out-Year pension costs, which are likely to increase significantly beginning in FY 2011 due to investment losses incurred by the State retirement system.

These baseline gaps are unsettling because the permanent gap-closing options provided by the County have not changed and remain uncertain. In general, they require State legislative approval, which to date, has not been forthcoming. While the County has pursued gap-closing initiatives such as health insurance relief, a cigarette tax, and video lottery terminals at Belmont Park, these Out-Year "place-holders" may need to be replaced with realistic options in order to balance the FY 2010 budget, which will be submitted in approximately three months.

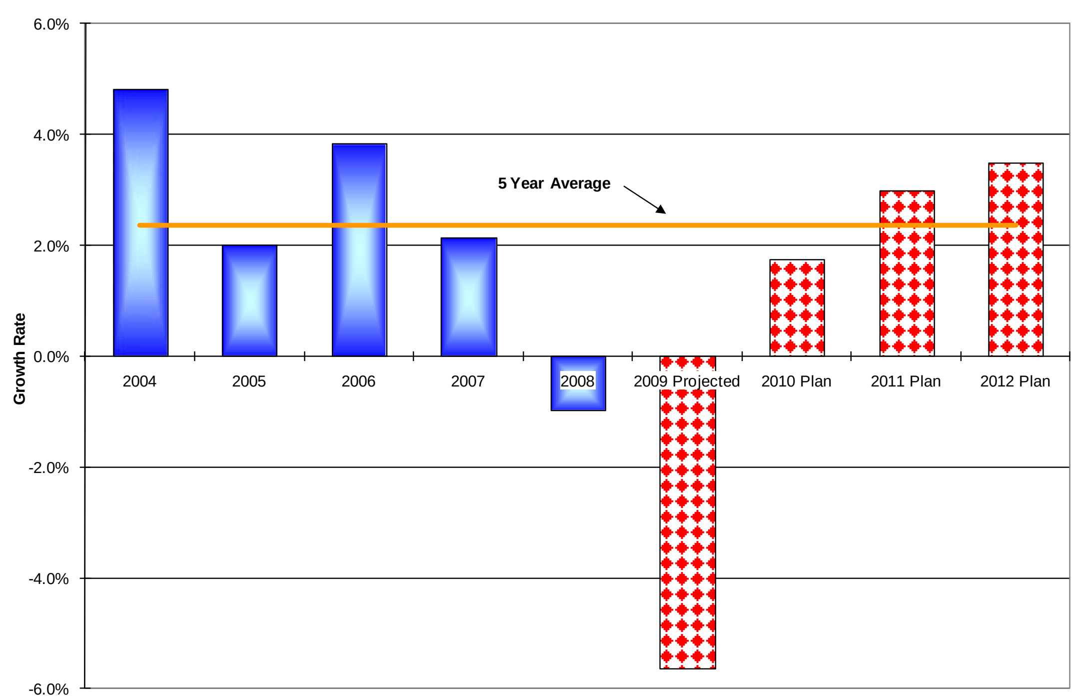
Sales Tax

As discussed earlier in this report, sales tax revenue comprises almost 40% of the County's total revenue stream, which makes this an area that both the County and NIFA need to continually monitor. Although the County reduced its forecast of sales tax revenue for FY 2009, it has left unchanged its growth rate assumptions for FY 2010, FY 2011, and FY 2012, which we believe may be optimistic.

The County assumes that the economic weakness will abate toward the end of FY 2009 and translate into sales tax growth of 1.75% in FY 2010, 3.0% in FY 2011, and 3.5% in FY 2012, as shown in Chart 1. Combined with the projected additional revenue expected to be generated by the County's new sales tax on residential energy, the County estimates that sales tax collections will grow from $962.4 million in FY 2009 to $1.07 billion in FY 2012.

While these projections are not unreasonable based on historical performance, we remain concerned that the current economic downturn may be more protracted than assumed by the County because a number of positive economic factors which contributed to past growth, full employment and rising housing prices, are not yet present.

(Chart 1)
ANNUAL SALES TAX GROWTH HAS
AVERAGED 2.4 PERCENT DURING THE LAST FIVE YEARS



GAP-CLOSING PROGRAM

The elements comprising the County's gap-closing program, as shown below, remain substantially unchanged from the Plan. Many of the initiatives have been included for a number of years with only moderate success and some have experienced repeated delays in various stages of implementation.

GAP-CLOSING PLAN
FY 2008-2011

($ in millions)	FY 2009	FY 2010	FY 2011	FY 2012
County Projected Baseline Gap	**$0.0**	**($72.3)**	**($173.5)**	**($225.9)**
Baseline Measures:				
Health Insurance Cost Reductions	$0.0	$9.0	$14.0	$14.0
Annual Property Tax Increase	0.0	31.6	64.5	98.7
Smart Government Initiatives	0.0	10.5	19.7	20.2
Workforce Management	0.0	5.7	14.0	20.0
Subtotal – Gap-Closing Initiatives	**$0.0**	**$56.8**	**$112.2**	**$152.9**
Remaining Gap	**$0.0**	**($15.5)**	**($61.3)**	**($73.0)**
Options to Close Remaining Gap:				
Debt Restructuring	$0.0	$0.0	$5.0	$5.0
Cigarette Tax	0.0	26.4	26.4	26.4
Video Lottery Terminals	0.0	20.0	20.0	20.0
FIT Reimbursement	0.0	0.0	4.1	4.1
Fast Food Tax	0.0	11.8	11.8	11.8
Discretionary Programming Reductions	0.0	12.0	12.0	12.0
Subtotal – Options	**$0.0**	**$70.2**	**$79.3**	**$79.3**
Surplus - Assuming All Options	**$0.0**	**$54.7**	**$18.0**	**$6.3**

Smart Government Initiatives

The County's gap-closing plan includes Smart Government Initiatives ("SGIs") in the amount of $10.5 million in FY 2010, $19.7 million in FY 2011 and $20.2 million in FY 2012.

SGIs have not had a good track record of success even though we commend the County for their creation and the innovative zeal they try to capture. Consequently, we are glad to see that the County has not relied heavily upon their SGIs in the Update and in many cases have scaled back expectations.

The Update removed the Risk Management initiative, but restored the moribund Automated Time and Leave System initiative in the Out-Years. Overall, SGIs were reduced by $3.2 million in FY 2010, $0.65 million in FY 2011, and $1.6 million for FY 2012 due to reductions in all previous SGIs caused by delays in implementation. A brief summary of some of the major initiatives follows the Table.

SMART GOVERNMENT INITIATIVES
FY 2010-2012

Vertical	Initiative	2010	2011	2012
Law Enforcement & Public Safety	Electronic Court Appearance	250,000	500,000	520,000
	Housing Non-County Inmates	750,000	1,250,000	1,750,000
Health & Human Services	Program Reductions	1,000,000	1,000,000	1,000,000
Management, Budget & Finance	Revenue Options	1,100,000	1,100,000	1,150,000
	Commercial Tax Grievance Filing Fee	0	3,400,000	3,400,000
	Automated Time & Leave System	2,400,000	2,400,000	2,400,000
	Enterprise Resource Planning System	5,000,000	10,000,000	10,000,000
	TOTAL	10,500,000	19,650,000	20,220,000

Electronic Court Appearance is designed to utilize technology within the Correctional Center to improve efficiency through video conferencing. Savings from this SGI have been reduced by half for FY 2010, remain the same for FY 2011 and receive a marginal increase of $20,000 in FY 2012. The reason projected savings have been pushed back is because the Department of Information Technology needs to review the technological infrastructure within the Correctional Center facility before choosing the best technology required for implementation.

Another Correctional Center initiative is a reimbursement program for housing non-County inmates. The Correctional Center is interested in expanding its current practice of housing Federal inmates to include other jurisdictions (e.g. Suffolk County). This initiative was also included in the Plan at $1.5 million for FY 2010, $2.5 million for FY 2011 and $3.5 million for FY 2012, but has greatly reduced its projected savings by half for each of these years.

Although various Health and Human Services initiatives have been introduced in past plans and updates, this initiative proposes a reduction in vendor payments for three of its programs; namely, the Youth Board, Senior Citizens, and Social Services. The proposed reductions are $1.0 million for each of the Out-Years. The County is stressing that, although it has included this as an option in the past, it has never had to resort to implementing this initiative and hopes to avoid doing so in the Out-Years as well.

The Update delays until FY 2011 the Commercial Tax Grievance Filing Fee, which the County had previously projected would generate annual revenue of $3.4 million beginning in FY 2010. This initiative requires State legislative approval, which has still not materialized. While the County intends to pursue sponsorship and passage of this initiative for FY 2010, it assumes no revenue until FY 2011. Because the County has been pursuing this SGI for a number of years to no avail, we are doubtful that this initiative will ever be achieved.

The County has been pursuing an Automated Time and Leave Management System that it believes will provide more accountability and help streamline time and leave reporting by consolidating functions and reducing manual processing of time and leave information. It is expected to be phased in over a number of years and the savings are projected at $2.4 million for all Out-Years.

The Enterprise Resource Planning System ("ERP") is an Information Technology project that hopes to utilize technology to improve processes and procedures throughout the County by replacing or enhancing existing systems such as, but not limited to, the financial and human resources management systems. The projected savings of $5.0 million in FY 2010 and $10.0 million in each of FY 2011 and FY 2012 remains unchanged from the Plan.

Workforce Management

The County continues to achieve significant savings in personal service expenditures because each year it holds approximately 300 of its budgeted positions vacant. This construct results in budgetary surpluses of approximately $20 million each year, exclusive of associated fringe benefit expenses. As of this Update, the variance between budgeted positions and "on-boards" is 351 positions. Additionally, the County expects to achieve savings through attrition whereby some new vacancies not already identified will also be held unfilled unless they receive grant funding or are determined to be directly related to revenue production.

Historically, the majority of the workforce management savings have resulted from not filling vacant positions in the Correctional Center, the Probation Department and Police Headquarters. With the implementation of the voluntary termination program proposed to various unions within these departments, these savings are already accounted for in the Contingency Plan and reflected in the baseline projections.

Property Tax Levy Increases

The Update maintains the County Executive's proposal to implement annual increases in the property tax levy by 3.9% in the Out-Years. The increases will raise property tax revenues by $31.6 million in FY 2010, $64.5 million in FY 2011, and $98.7 million in FY 2012. While completely within the County's control, it is unclear if there is sufficient legislative or other political support for these proposed increases.

If these annual tax increases are approved by the County Legislature, they will result in growth of the Major Funds tax levy by FY 2012 of $391.5 million or 76.3% since FY 2000. While this is a high percentage increase, the County maintains that its share of the total property tax burden (

for the average resident) has fallen during the comparable period.

Health Insurance Cost Reductions

While the County has recently demonstrated success with securing labor savings, as discussed in the Labor Concessions section of this report, it has had much less success extracting long-term savings from modifications to its employee fringe benefits package as proposed in past plans and updates.

The County now acknowledges that it is restricted in its ability to manage and reduce employee health care costs; therefore, it is pursuing negotiations with the State Division of Budget and the New York State Health Insurance Program ("NYSHIP") to contain costs. In FY 2009, because of reserves that had accumulated at NYSHIP, the health insurance premium increased by only 1.1% over FY 2008. That resulted in a savings of approximately $9.5 million compared to the Plan.

The County is continuing to work with DOB and NYSHIP to seek enhancements that would control health insurance growth rates in the Out-Years and is optimistically projecting annual savings which grow from $9.0 million in FY 2010 to $14.0 million for FY 2011 and FY2012. We are skeptical of this initiative.

PAYGO Judgments and Settlements

Since the creation of NIFA, the County has discussed a transition to paying for non-certiorari judgments and settlements in its operating budget. These have been funded in the capital budget; a practice which the Administration understands is not optimal.

Every municipality encounters judgments and settlements in the normal course of business. Within a limited range, these costs are predictable and paid for out of operating income. Consequently, they should be budgeted as part of the normal operating budget. Only in the case of extraordinary judgments or settlements should they be funded through borrowing or from an appropriate reserve.

Options to Close Remaining Gap

Even if all of the previously discussed gap-closing actions were successful, and baseline growth rate assumptions were correct, projected gaps would remain of $15.5 million in FY 2010, $65.3 million in FY 2011, and $73.0 million in FY 2012. The Update continues to assume that these gaps can be closed through a number of options which have previously been unsuccessful and whose viability is highly questionable. For FY 2010, the more significant of these options include $26.4 million from a cigarette tax, $20.0 million from video lottery terminals at Belmont Park, and $11.8 million from a new fast food tax. The County further assumes that these revenues would remain flat through the Plan period.

We question these initiatives because the County needs State legislative approval for these actions and there are indicators that support and passage of these items is unlikely. For example, a recent franchise agreement between the State of New York and the New York Racing Association does not provide for the installation of video lottery terminals at Belmont Park. Additionally, the County's requests to impose a fast-food tax on "unhealthy" food items and to impose a $2.00 per pack tax on cigarettes have garnered little support in Albany.

We are unable to evaluate the viability of the discretionary program cuts and debt restructuring initiatives because they lack specificity in the Update.

[THIS PAGE IS INTENTIONALLY LEFT BLANK]

VI. AREAS THAT REQUIRE FURTHER REVIEW

Notwithstanding the many accomplishments of the County, a number of major challenges and concerns identified in our previous report remain including the significant reduction of reserve balances, the Nassau Health Care Corporation, tax certiorari, and debt issuance.

RESERVE BALANCES

As discussed in our October 2008 staff report, Section 3667 (4) (c) of the NIFA Act requires that the financial plan include "adequate reserves…to maintain essential programs in the event that revenues have been overstated or expenditures underestimated for any period." The legislative intent was that monies be available for unplanned or extraordinary events.

The County understands the wisdom of maintaining reserves. In fact, the County attributes its past success at securing a series of bond ratings upgrades, in part, to "the accumulation of a growing unreserved undesignated fund balance." Those reserves gave rating agencies comfort that the County was protected against an economic downturn such as the one we are now experiencing.

Looking at the concept of General Reserves from the most inclusive perspective, they consist of any monies that are held in reserve by the County and which could be used to fill unanticipated gaps anywhere in the budget. For presentation purposes we have taken those resources which most closely follow this definition and combined them into what we have labeled, General Reserves. Those reserves are composed of the following: Retirement Contribution, Bonded Indebtedness, Employee Accrued Liability, Unreserved Fund Balance, and Tobacco Settlement.

As shown in Chart 2, the County's General Reserves are projected to fall to $67.5 million by the end of FY 2009. This illustrates the County's imprudent use of $217.3 million in reserves, built up in prior years, to pay for recurring expenditures over the five year period since FY 2004. With this temporary infusion of funds the County provided a level of services that it could not have otherwise sustained.

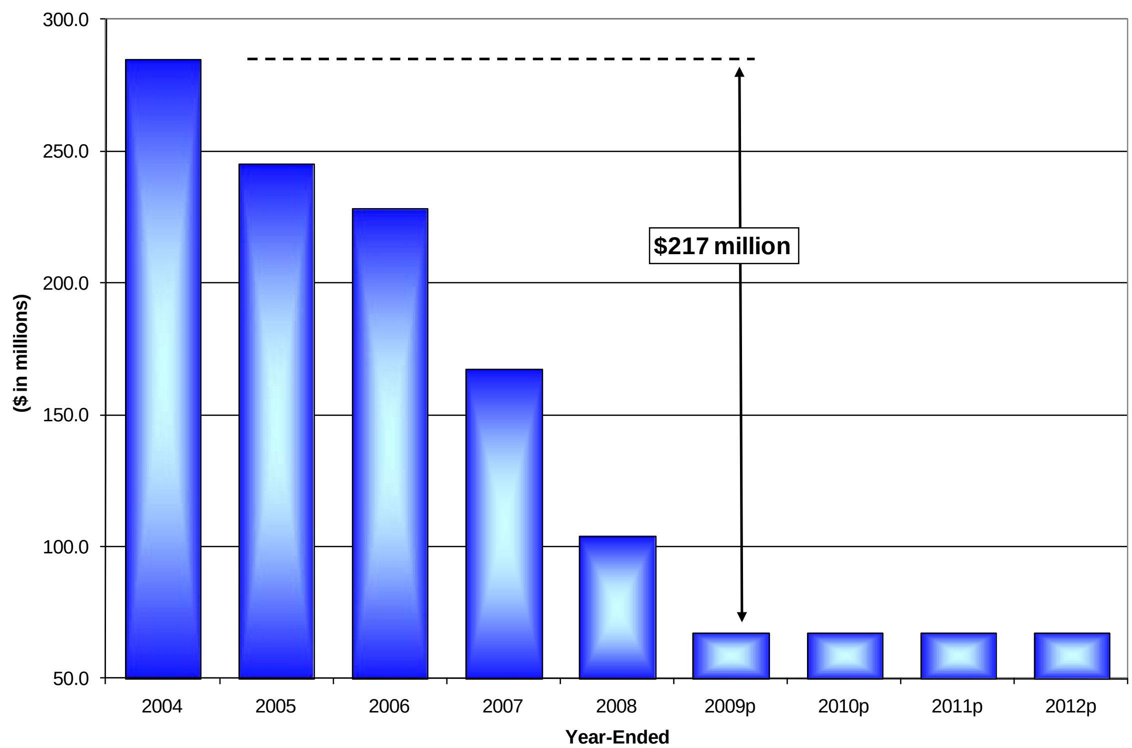
Likewise, the County has drawn additional resources from other reserves it maintains for certain specific purposes. Since these monies are restricted, the County cannot tap them for general budget balancing needs.

A detailed breakdown of the amount in each of the reserve funds, which we have categorized as General and Restricted Reserves, is available in the Appendices.

While other municipalities also use reserves to balance their budgets, their use of these resources postpones the difficult decisions necessary to achieve continuing structural budget balance. Having an adequate reserve is even more critical for Nassau

County given: its reliance on volatile sales tax revenues; the unpredictability of its social service costs in terms of caseload and related expenses, and its reliance on State funding for some of its programs. All of these issues add uncertainty to the budget process and increase the need for reserves, which should be built during "good times" so that they are available during an economic downturn. Because the County used significant amounts of its reserves during "good times," there are limited resources available to cushion the budgetary effects of the current economic crisis.

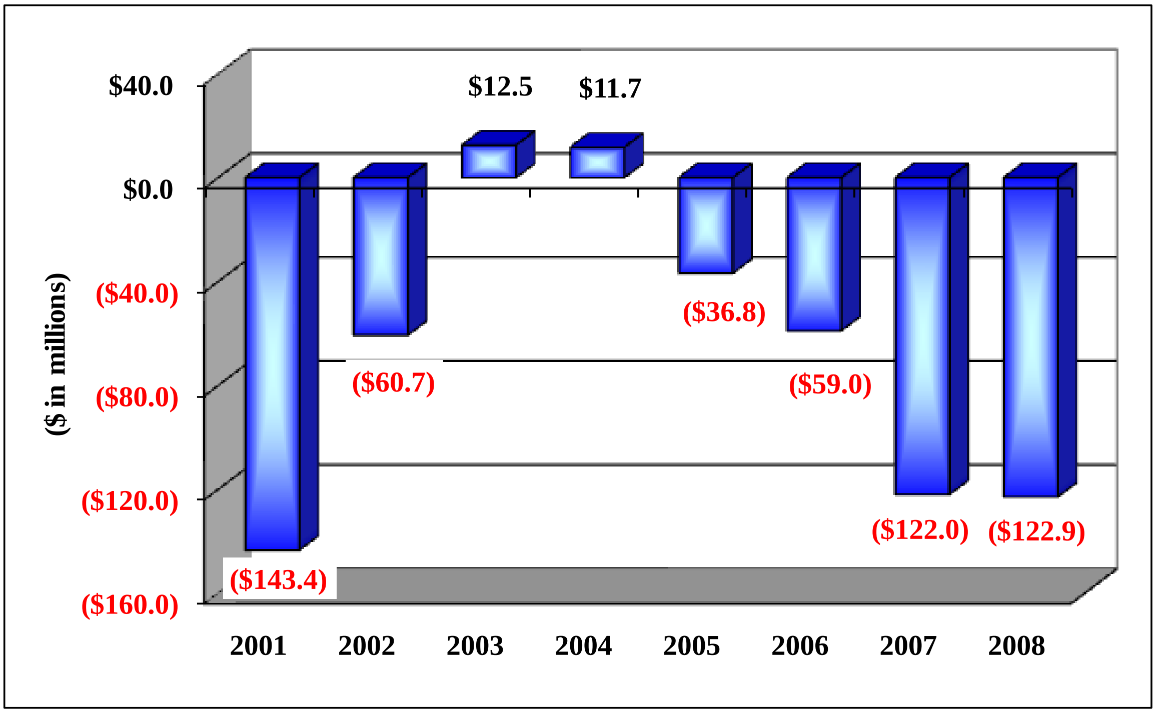
(Chart 2)
COUNTY GENERAL RESERVES HAVE DECLINED SHARPLY SINCE FY 2004



The County's FY 2010-2013 Multi-Year Plan should begin to replenish these reserves to appropriate levels. In fact, the County's proposed Fund Balance and Reserve Policy mandates the replenishment of its unreserved fund balance by direct appropriation in the event that for two successive years the County's level of unreserved fund balance falls below 4% of normal expenditures made from its General Fund and the County-wide Special Revenue Funds.

Chart 3 illustrates how the County's use of its reserves, combined with its continued dependence on other non-recurring resources to ensure short-term balance, has undermined the County's progress in attaining long-term structural balance (recurring revenues equal recurring expenditures). The County's recent fiscal actions have reversed its progress and dramatically increased the structural imbalance despite periods of relative economic strength. The structural deficit has grown in each of the last four years from $36.8 million in FY 2005 to $59.0 million in FY 2006, $122.0 million in FY 2007, and $122.9 million in FY 2008. This means that the structural deficit in FY 2008 was larger than at any time since FY 2001.

(Chart 3)
PROGRESS TOWARD STRUCTURAL BALANCE HAS REVERSED



NASSAU HEALTH CARE CORPORATION

The financial health of the Nassau Health Care Corporation ("NHCC") and its potential impact on Nassau County has been a major concern for NIFA since its inception. Perennial operating losses and the concomitant erosion of cash balances have been difficult to counteract, but at least there now appears to be an improvement in accountability and a modest turnaround in operating results. Even so, NHCC has not been able to achieve the "break-even" status that it has previously projected.

NHCC currently projects that it will end FY 2009 with a deficit of nearly $9.0 million after all gap-closing measures are applied to its projected baseline gap of $32.6 million. To mitigate the baseline gap of $32.6 million, NHCC is counting on continuing to receive $18 million in Nassau County mission payments/Article VI funding through FY 2012 as well as Federal/State aid of between $3.3 million and $3.5 million for the term of the Plan. NHCC also continues to pursue certain ambitious gap-closing initiatives that it believes will generate significant budget relief including a voluntary physician program and other enhanced services and rate adjustments.

NHCC continues to see some improvement in its monthly net patient service revenue within the A. Holly Patterson Nursing Home which shows a small profit; however, receipts continue to fall short of budgeted targets at the Nassau University Medical Center. Operating expenses continue to exceed budget, most notably for employee salaries and fringe benefits and the voluntary union concessions that NHCC was counting on have failed to materialize. In addition, NHCC also has had to absorb approximately $2.7 million in cuts that result from the adopted State budget.

NHCC recently refunded $220.8 million of its bonds and secured new letters of credit in an effort to improve the performance of its variable rate demand bonds. The long term success of this transaction is yet to be determined; however, regardless of its ultimate success, NHCC's variable rate debt is still a major portion of its budget and has the ability to fluctuate widely.

The County has provided significant financial support to NHCC and will continue to do so in the future through its annual mission payments and by acting as guarantor for all of NHCC's in outstanding debt. We hope that NHCC can remain viable without additional use of scant County resources.

CERTIORARI

Resolution of the certiorari problem, such that the County could pay for this expense out of its operating revenues ("PAYGO"), was seen as essential to Nassau County's return to fiscal stability. To assist in this process, the State Legislature authorized NIFA to borrow up to an additional $800 million to eliminate the County's backlog of certiorari claims and prepare it for PAYGO. The County was also given $5 million of State aid to assist it in streamlining the tax certiorari claims process.

ANNUAL PAYMENTS FOR CERTIORARI CLAIMS (BUDGETARY BASIS)

Activity ($ in millions)	FY 2006 Actual	FY 2007 Actual	FY 2008 Actual	2009 Projected
Current-Year Operating Funds	$19.6	$50.1	$40.0	$50.0
Prior-Year Surplus	$50.0	$25.0	$0.0	$0.0
Debt	$1.0	$12.0	$58.8	$28.0
Total	**$70.6**	**$87.1**	**$98.8**	**$78.0**

Those monies were, at the time, deemed sufficient to solve the County's problem and have long since been spent. Unfortunately, the County continues to borrow for the payment of large portions of its certiorari claims, thereby postponing its transition to PAYGO funding. In fact, the County plans to continue its borrowing program through at least FY 2012.

As a result of the County's policy of borrowing to pay certiorari claims, it is already carrying approximately $150.6 million in debt service costs in FY 2009 solely related to its certiorari program. This constitutes almost 6% of the County's total budget for its Major Funds.

We also note that in response to the certiorari crisis, the County rapidly hired new employees, built in-house expertise, and invested in computers and sophisticated modeling programs. We had anticipated that some of these technological changes would have resulted in not only fewer valid claims, but productivity savings. Instead, budgets have increased and the number of claims is surprisingly stable.

DEBT ISSUANCE

Several important matters have occurred since the Plan was adopted that impact the County's issuance of debt and payment of debt service.

1. **Refunding –** Recently, NIFA refunded $282.96 million of its variable rate bonds to fixed rate bonds. The refunding was requested by the County because of its need to lessen its exposure to variable rate debt.

   Simultaneously, NIFA also issued $20.1 million of fixed rate bonds to generate present value savings of over $1 million for the County.

2. **Liquidity Substitution -** NIFA has also replaced Dexia as a liquidity provider for some of its remaining variable rate bonds with stronger credits. It is anticipated that this will result in lower interest rates on NIFA's remaining variable rate bonds.

3. **Recent County Ratings –** The County recently asked for ratings in connection with its proposed issuances of General Obligation Bonds, Series 2009. The County's ratings were maintained, but the rating agencies expressed their concerns regarding the County's dwindling reserves, reliance on one time revenues and declining liquidity.

   While we praise the County for having been previously upgraded to its current rating, Nassau County is still an outlier. Most "A"-rated counties are smaller and poorer; in fact, the only other large county that we could find that is rated as low as Nassau County is Wayne County, Michigan. Even though Nassau County is among the wealthiest large counties in the Country (measured either by household income or by taxable property values), its financial condition remains relatively weak for such a comparatively affluent demographic.

4. **Cash Flow Borrowings –** The County re-commenced cash flow borrowings in FY 2005 and has increased the levels steadily each year, which is evidence of deteriorating balances and liquidity. In 2009 the

situation continues to deteriorate. The County's RAN borrowing was projected to be $130 million in the Plan and in the Update is projected to be $165 million. The TAN borrowing was projected to be $120 million in the Plan and in the Update is projected to be $140 million. This is a total increase of $55 million with resultant interest costs.

5. **Capital Borrowing and Spending Patterns –** Over the years the County has had a poor record of predicting its capital needs and timely spending money that was raised for those purposes. At the end of the 2007 fiscal year the County discovered that it had borrowed $39 million more for capital purposes than it needed and once again in 2008 discovered that it had borrowed $23.2 million more than it needed.

   In the same fashion as in 2007, in 2008 the County redirected the unspent bond proceeds to its operating budget where it was used to pay debt service. This action freed up $23.2 million in resources that had already been budgeted for this purpose, thereby resulting in a budgetary windfall in FY 2008 from borrowings rather than revenue growth or expenditure reductions.

   The fiscally prudent response to this windfall would have been to call or redeem an equivalent amount of outstanding bonds. Instead, future taxpayers are bearing the burden of paying for bonds whose proceeds were used to benefit only current year taxpayers.

6. **Nassau Health Care Corporation –** The County's debt burden continues to be under stress because of its guaranty of NHCC debt. This currently accounts for approximately 9% of the County's debt.

   While the County has made this decision with open eyes, they should not forget that NHCC has significant cash flow problems. Were NHCC to default on its bonds, this would not only be catastrophic for patient care, but also for the fiscal health of Nassau County.

   The County should not be lulled into complacency because of its current position that it is no longer going to directly subsidize NHCC beyond its historic mission payments. In fact, it continues to provide a huge hidden benefit by allowing the use of its credit to support NHCC bonds.

VII. APPENDICES

GLOSSARY

Budget – The first year of the Plan.

Fund Balance – The excess of the assets of the fund over its liabilities, reserves and carryover.

General Reserves – any monies that are held in reserve by the County and could be used to fill unanticipated budget gaps.

Major Fund – is the term the County uses to refer to the departments that comprise its General Fund, Fire Commission Fund, Police District Fund, Police Head Quarters Fund.

Multi-Year Financial Plan ("the Plan") – The County's four-year projection of baseline operating revenues and expenses and its plan for closing any projected gaps.

Out-Years – FY 2010-2012

Pay-as-you-go – A term used describe a financial policy where capital outlays are financed from current revenues to avoid incurring costly debt financing or issuing new debt.

proposed Budget – Fiscal Year 2009 proposed Budget submitted September 15, 2008

proposed Plan – County Executive's proposed FY 2009-2012 Multi-Year Financial Plan

Plan – Adopted FY 2009-2012 Multi-Year Financial Plan

Restricted Reserves – monies held in separate accounts and usually restricted by law as to their use.

Tax Certiorari (certs) – Grievances filed by Nassau County property owners contesting the assessment of their properties.

Update – Multi-Year Financial Plan Update submitted May 1, 2009

ACRONYMS

AFA - Adjunct Faculty Association

AHP - A. Holly Patterson

ARC - Assessment Review Commission

ARS - Auction Rate Securities

Authority - Nassau County Interim Finance Authority

CON - Certificate of Need

CSEA - Civil Service Employees Association

COLA - Cost-of-Living Adjustment

CPI - Consumer Price Index

DAI - Detectives' Association Inc.

District - Sewer and Storm Water Resource District

DOH - Department of Health

FMAP- Federal Medical Assistance Percentage

FY - Fiscal Year

FTE - Full-time Equivalent

HEAL - Healthcare Efficiency and Affordability Law

ICR - Institutional Cost Report

LIRR - Long Island Railroad

MTA - Metropolitan Transit Authority

NHCC - Nassau Health Care Corporation

NUMC - Nassau University Medical Center

NCC - Nassau Community College

NCCFT - Nassau Community College Federation of Teachers

NIFA - Nassau County Interim Finance Authority

OMB - Office of Management & Budget

OTPS - Other than Personal Services

PAYGO - Pay-as-you-go

PBA - Police Benevolent Association

PINS - Persons in Need of Supervision

RANS - Revenue Anticipation Notes

SGIs - Smart Government Initiatives

ShOA - Sheriff Officers Association

SOA - Superior Officers Association

SNA - Safety Net Assistance

SSWFA - Sewer and Storm Water Finance Authority

TANF - Temporary Assistance for Needy Families

TANS - Tax Anticipation Notes

VRDB - Variable Rate Demand Bond

SUMMARY OF COUNTY RESERVES

	General Reserves						Restricted Reserves				
Year	Retirement Contribution	Bonded Indebtedness	Employee Accrued	Unreserved Fund Balance	Tobacco Settlement	Sub-Total	Tobacco Borrowing	SSWRD	SSWFA	Sub-Total	Total
YE 2004	$79.8	$25.0	$28.9	$90.5	$60.6	$284.8	$0.0	$32.4	$60.9	$93.3	$378.1
2005 Uses	($35.0)	$0.0	($7.5)	$0.0	($22.3)	($64.8)	$0.0	$0.0	($11.5)	($11.5)	($76.3)
2005 Contributions	$24.8	$0.7	$0.0	$0.0	$0.0	$25.5	$0.0	$30.5	$0.0	$30.5	$56.0
YE 2005	$69.6	$25.7	$21.4	$90.5	$38.3	$245.5	$0.0	$62.9	$49.4	$112.3	$357.8
2006 Uses	($34.2)	($10.9)	($1.3)	($13.4)	($23.0)	($82.8)	($10.3)	$0.0	($53.3)	($63.6)	($146.4)
2006 Contributions	$16.0	$0.0	$1.3	$27.0	$21.2	$65.5	$125.9	$58.8	$23.7	$208.4	$273.9
YE 2006	$51.4	$14.8	$21.4	$104.1	$36.5	$228.2	$115.6	$121.7	$19.8	$257.1	$485.3
2007 Uses	($26.4)	($14.8)	($6.3)	($38.1)	($23.6)	($109.2)	($10.5)	$0.0	($0.7)	($11.2)	($120.4)
2007 Contributions	$0.0	$0.0	$0.0	$23.8	$24.6	$48.4	$4.7	$40.2	$0.0	$44.9	$93.3
YE 2007	$25.0	($0.0)	$15.1	$89.8	$37.5	$167.4	$109.8	$161.9	$19.1	$290.8	$458.2
2008 Uses	($24.5)	$0.0	($0.8)	($17.9)	($23.0)	($66.2)	($51.4)	($32.6)	($8.9)	($92.9)	($159.1)
2008 Contributions	$0.0	$0.0	$0.0	$2.1	$0.7	$2.8	$2.4	$0.0	$0.0	$2.4	$5.2
YE 2008	$0.5	($0.0)	$14.3	$74.0	$15.2	$104.0	$60.8	$129.3	$10.2	$200.3	$304.3
2009 Uses	($0.5)	$0.0	($11.0)	($10.0)	($15.3)	($36.8)	($29.0)	($41.0)	($5.4)	($75.4)	($112.2)
2009 Contributions	$0.0	$0.0	$0.0	$0.0	$0.3	$0.3	$0.3	$0.0	$0.0	$0.3	$0.6
YE 2009	($0.0)	($0.0)	$3.3	$64.0	$0.2	$67.5	$32.1	$88.3	$4.8	$125.2	$192.7
2010 Uses	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	($16.7)	($40.4)	$0.0	($57.1)	($57.1)
2010 Contributions	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$1.1	$1.1	$1.1
YE 2010	($0.0)	($0.0)	$3.3	$64.0	$0.2	$67.5	$15.4	$47.9	$5.9	$69.2	$136.7
2011 Uses	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	($14.9)	($44.4)	$0.0	($59.3)	($59.3)
2011 Contributions	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$1.0	$1.0	$1.0
YE 2011	($0.0)	($0.0)	$3.3	$64.0	$0.2	$67.5	$0.5	$3.5	$6.9	$10.9	$78.4
2012 Uses	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	($10.0)	$0.0	($10.0)	($10.0)
2012 Contributions	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$2.0	$2.0	$2.0
YE 2012	($0.0)	($0.0)	$3.3	$64.0	$0.2	$67.5	$0.5	($6.5)	$8.9	$2.9	$70.4